Mining Journal

Blackham survives funding trauma

Blackham Resources – once one of Australia's most overpriced gold stocks – has been given another chance to prove its worth.

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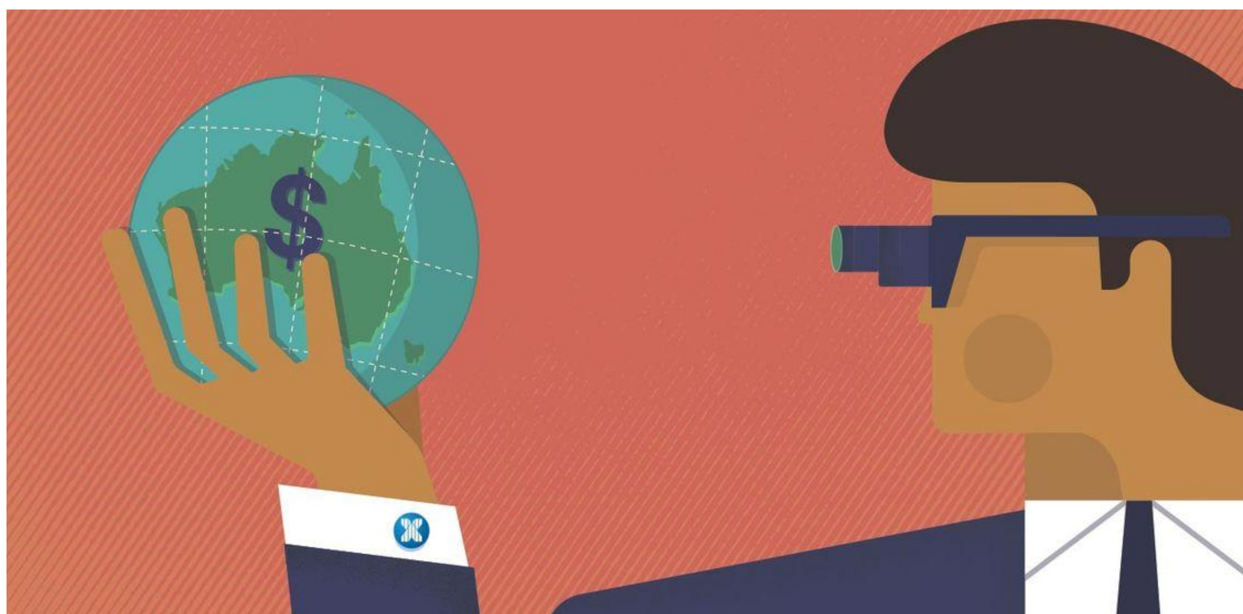

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As soon as they had commenced production in October 2016, Blackham directors were raising expectations of a speedy transition to annual gold output of 200,000 ounces.

If Blackham had fulfilled its promise, it might have easily had a market capitalisation of A$250-300 million (US$192-230 million). Instead, it has a $112 million price tag despite a fivefold increase in the number of shares on issue after worse than anticipated production and cost outcomes and an aborted project funding.

The company's removal from the S&P/ASX All Ordinaries share price index this month followed a share price fall of more than 90%.

The company is still talking about reaching its 200,000oz goal but the timing is more nebulous as further studies are completed and it prioritises getting the basics right first.

The company has consolidated a 1,100 square kilometre tenement package on the Norseman-Wiluna gold belt covering four large-scale gold systems suitable for open pit and underground development over multiple sites.

With a prime location came a critically important windfall. The company was able to buy processing infrastructure adjacent to its tenements from a corporate liquidator. The bargain basement $2 million initial payment in 2014 probably saved the company over $100 million in up-front capital.

In October 2015, Blackham directors were telling investors they could spend just $28 million to produce 100,000oz of gold a year for four or five years to generate operating cash flows of $185 million. At the time, the company had a market value of $44 million. The Blackham investment proposition was equivalent to buying a bond with a 27% yield.

Multiple styles of mineralisation in a variety of sites was no boon for a company with limited capital and personnel resources

The Wiluna plant's 20-year operating history before being acquired by Blackham provided some confidence that, with the right ore mix, its near-term annual production target could be met.

By August 2016, the company had tweaked its production intentions but its market value had rocketed to $294 million. In exchange, an investor would be entitled to operating cash flows of $234 million, according to the company's analysis at the time.

The overly exuberant expectations implied in the prospective negative return signalled a company ripe for re-pricing.

Writing in Mining Journal in June 2017, I characterised the company as still expensive having been one of the most overvalued stocks in the sector.

The existing plant was built to process free milling ores from the Wiluna mine. It has limited capacity to handle sulphide ores. The expansion phase of the project, aiming for 200,000 ounces a year over nine years with a plant capable of processing sulphide ores from lower grade openpit orebodies, will require $114 million, according to the company's August 2017 feasibility analysis.

The 2017 analysis put a value on the expanded Matilda-Wiluna mining complex (before corporate costs and tax) of $455 million using a gold price of $1,700 per ounce and an 8% discount rate.

The chosen discount rate - up from 5% in some earlier studies - still exaggerated the equity investment proposition insofar as actual costs of debt were just under 13% in the second half of 2017. Eighty five percent of project funding is now coming from relatively expensive equity.

I once queried company managing director Bryan Dixon about the potentially detrimental impact on corporate credibility of unrealistically low discount rates to inflate valuations. He simply shrugged, smiled and said he was just copying what everyone else did. Hopefully, Blackham directors did not delude themselves about the value of what they were proposing.

The timing of the company's expansion plans is now less certain against the backdrop of having to husband increasingly costly funds and reduce existing debt after an earlier institutional funding commitment was withdrawn unexpectedly in December 2017.

In January, mining contractor MACA Limited said it would support a recapitalisation of Blackham Resources through a secured $14.3 million loan and, in February, the company raised $36 million in an underwritten share entitlement offer.

In the immediate future, through extensions of existing orebodies and fresh discoveries, the company is looking to create an indefinitely rolling five-year mine life from free milling ore.

Historical mining operations were underground. The company wants to use openpit reserves to add scale and improve project economics.

The company has foreshadowed an annualised production rate of 40,000-45,000oz during the first half

of 2018 after having produced just 61,181oz during the whole of 2017 when lower than planned production and higher costs left it financially stretched.

Blackham directors may have been disadvantaged by too many choices. Multiple styles of mineralisation in a variety of sites was no boon for a company with limited capital and personnel resources.

Directors never had a clean canvas on which to work. Rather, they have continually tried to mix and match the pieces of a jigsaw puzzle from which others, too, had been unable to assemble a coherent picture.

Now, on paper at least, there is a stronger investment proposition. Even with a discount rate to more realistically reflect development and exploration risks, the company's future value profile retains sufficient momentum for a return in the vicinity of 175-200%.

Since completion of the recent equity raising, the share price has more then doubled. The depressed pricing used to attract investors played a role as did the company's confirmation it achieved a higher production rate and lower costs in the first weeks of 2018. Investors remain interested.

Conclusive evidence of near-term targets being met for more than just a month or two will help build the valuation case.

Beyond that, the challenge will steepen. Having to delay expansion to consolidate its financial base raises the risk of investors growing impatient or disillusioned about progress.

A seemingly solid value proposition is once again, and possibly for the last time, the lure to stay the course.

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