

# HALLGARTEN & COMPANY

## Coverage Update

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## Sage Gold

(TSX-V: SGX, FSE: RSEP, OTCBB: SGGDF)

Strategy: Long

Key Metrics			
Price (CAD)	\$0.105		
12-Month Target Price (CAD)	\$0.49		
Upside to Target	367%		
12 mth high-low	\$0.085-\$0.27		
Market Cap (CAD mn)	\$11.28		
Shares Outstanding (millions)	107.4		
Fully Diluted (millions)	180.3		
	<b>FY17e</b>	<b>FY18e</b>	<b>FY19e</b>
Consensus EPS		n/a	n/a
Hallgarten EPS (CAD)		(\$0.05)	\$0.01
Actual EPS (CAD)	-0.21		
P/E	n/a	n/a	7.9

# Sage Gold

## Production Starts to Roll

- + Production was achieved in the 4<sup>th</sup> quarter of 2017
- + Minimal capex due to existing mine and utilisation of McEwen Mining's Black Fox mill for processing
- + Sage cleverly bought out the 40% minority interest in the Clavos project from Kirkland Lake Gold for a bargain CAD\$1 million in 2016
- + Enhanced return metrics since PEA was published in April 2013 due to decline in Canadian dollar exchange rate against the USD
- + Dewatering to 270 metre level complete with only 30 metres remaining
- + Further exploration over the last eight months has shown the potential to expand resource both along strike and downdip
- × Technical difficulties, largely related to weather, have slowed initial production
- × Financing markets remain tight, but company has managed a small placing in February
- × Upside for gold is limited to just above the current price in our opinion

### **Moving into the Producer Category**

Sage Gold, through persistence, survived the down years and as recovery set in snapped up the 40% share held the Kirkland Lake (after it had taken over St Andrew Goldfields). The mine has now resumed production and is doing so on minimal capex. In this update on our previous coverage we shall examine the progress made thus far and the potential upside at its Clavos mine.

### **Refresher on the Background**

The Clavos mine is located within the Timmins mining camp in German, Stock and Clergue townships and is comprised of 69 patented and leased claims and 14 unpatented claims. The patents, leases and claims are 100% owned by SGX. The Clavos property comprises 2,540 hectares in total area. Clavos is close geographically (20kms) to the Hoyle Pond mine which has produced more than 2.4mn ozs since 1985 and is still in operation.

The Clavos deposit was mined briefly between mid-2005 until August 2006 and again until May 2007. The processed production from the Clavos Project from the beginning of 2006 until shutdown of operations in 2007 totalled 120,746 tonnes grading 4.3 g/t Au containing 16,745 ounces of gold.

### **Geology**

Gold mineralization occurs in a series of quartz and quartz-carbonate veins which are interpreted from

the drilling to be steeply dipping and east-west striking, roughly parallel to the PFZ. There are five gold-bearing zones for which mineral resources have been estimated. These are the Hangingwall Zone (HW Zone), the Footwall Zone (FW Zone), the Contact Zone, the Sediment Zone, and a group of miscellaneous intersections listed as Other Mineralization.

Of these zones, the HW Zone has been the main target of past mining activities.

The HW Zone and FW Zone represent the majority of the mineralization at Clavos and vary from 1.5 m to more than 3.0 m in horizontal thickness along the south and north contacts of the feldspar porphyry bodies respectively. These zones consist of quartz and quartz-carbonate veins and stringers hosted within a sulphide-rich package of fuchsite and sericite altered ultramafic volcanic rocks. Up to 10% sulphides consisting of pyrite arsenopyrite, and rarely galena, gersdorffite (nickel arsenide), chalcopyrite occur as disseminated grains in the altered host rock and within narrow fractures/veinlets within the quartz veins. Gold occurs as coarse nuggets predominantly within the quartz veins but occasionally within the volcanic host, and also as inclusions within the sulphide grains.

#### **The Black Fox Mill – a Key Consideration**

Part of the strategy to minimize the capital spend at Clavos is the utilization McEwen Mining's nearby mill to process the ore from the mine. The mill is a 2,500 tonnes per day carbon in leach (CIL) facility with electricity supplied from a local 27kv power line.

Sage Gold has signed a binding toll milling agreement with McEwen Mining over the flow of ore they expect to send to the mill, processing up to 200,000 tonnes per year for a total of 1.1 million tonnes over the estimated seven-year mine life of the Clavos Mine.



In November 2016, Sage Gold signed a custom milling agreement with Primero Mining Corp. In October 2017, McEwen Mining completed the purchase of the Black Fox Mill and other nearby assets from Primero, thereby inheriting the custom milling agreement with Sage Gold. The mill was previously owned by St Andrew when they were also operator of the Clavos gold mine. Many of the current McEwen Mining operating team at the mill were part of that St Andrew team and are familiar with the Clavos ore, having previously processed approximately 120,000 tonnes. It is currently estimated that approximately 183,000 tonnes of Clavos ore will be processed annually, with an estimated 1.1 million tonnes processed over the expected seven year mine life of the Clavos Project. The cost under the toll milling agreement is very competitive. Since McEwen Mining does not currently have sufficient mill feed from its operations to support the capacity of the Black Fox Mill, the Clavos mill feed forms an important and meaningful contribution to the successful operation of the mill complex.

The haul road between Clavos and the mill is owned jointly by Sage and McEwen Mining. The haul road is not part of the Provincial highway system and enabling Sage to use larger haul trucks between Clavos and the mill than would otherwise be permitted on the Provincial highways.

The original plan was that ore from the mine would be loaded underground and trucked directly to the mill. However this was altered to crushing at the mine where it is now stockpiled there (for reasons explained anon) and then trucked to the mill which alternates between feed from Clavos and feed from the Black Fox mine in 4,000-16,000 tonne batches.

### **The Mining and Processing Plan**

The PEA for the Clavos deposit dates back to April 2013. It envisaged a mine production rate of 600 tonnes per day was selected as being optimum for the mineralized structures contained within the Clavos deposit. . The PEA was defined at a base case gold price of US\$1,500 per ounce at a USD to CAD exchange rate of 1:1 with a base case gold price of CAD\$1,500 per ounce. However, the current price of gold in Canadian dollars is in excess of CAD\$1,700 per ounce. The mine is currently permitted to produce at a rate of 700 tpd.

Within the PEA, it was estimated that approximately 1,148,900 tonnes will be mined and processed from the existing Mineral Resource estimate which was calculated at a CAD\$1,600 per ounce gold price, using a 2.75 g/t Au cut-off and a 60 g/t Au capped grade. This tonnage was based on a 2.75 g/t cut-off proposed tonnage estimate, with a 60 g/t cut grade, and would permit a life of mine of seven years (with a two-year payback) to extract 70% of the outlined mineral resource estimated tonnage of Indicated 1,258,400 tonnes plus Inferred 796,000 tonnes.

The PEA estimated:

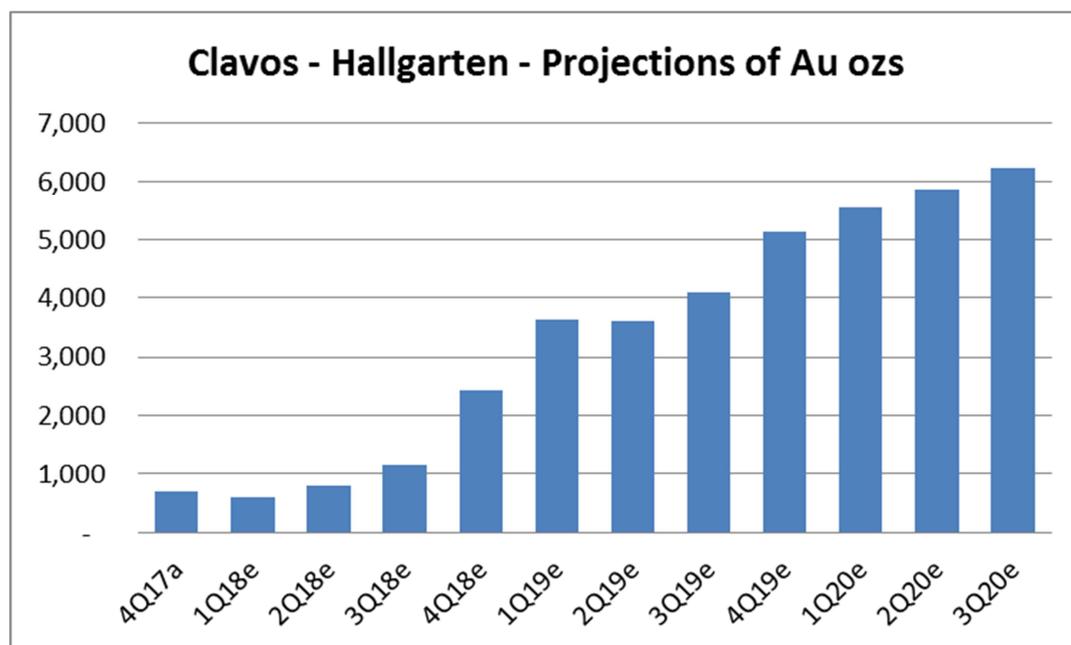
- LOM Capital Expense and Sustaining Capital per ounce was estimated at CAD\$1,266, including Operating Cost and Royalties
- Average head-grade of gold ranging from 6.45 g/t in Year One to 4.37g/t in Year Seven

At the time Sage took full control of the mine there was substantial existing infrastructure in place, including underground ramp access to the 300 metre level, underground levels developed every 25 metres, power to site, surface ventilation system and a water management system. The project has an existing mining permit valid up to 2019.

In the Clavos mine plan, there is readily available 847,133 tonnes of the 1,148,900 tonnes to be extracted prior to having to extract the remaining 301,767 tonnes which includes removing the crown pillar. The remaining 45% of the Indicated and Inferred resource estimate was not included in the mineralized material extraction scheduling process.

A 23-month period to undertake mine dewatering (done), mine rehabilitation (done), definition/delineation diamond drilling (on-going) and pre-stope development (on-going) is envisaged to achieve a full production rate (in years four and five of the seven years) of 600 tonnes per day, or 210,000 tonnes per annum based on 350 operating days per year.

Below can be seen our projections, including the first quarter of actual production:



These projections are subject to change with the revised mine plan.

### The Production Ramp-up

Mining activities are directed to developing and extracting mineralized blocks associated with stope blocks identified in the PEA. The plan was start (at commercial production) with 40-50 tpd production with cut & fill mining of the stopes. An incremental 40tpd per day will be added to production, every

thirty days, until capacity is reached. The rate of acceleration of mining will be contingent upon the availability of working capital and the results of the new mine plan.

To date, on the 150 west metre level, development and mining activities have accessed both hangingwall and footwall PEA stope blocks. Definition drilling suggests that the lower boundaries of some of the PEA stope blocks on the 150 west metre level are closer to the access drift than originally anticipated which is reducing the amount of development required before reaching the stope block. Mining on the 150 east metre level has been ongoing in the hangingwall zone at grades that are comparable to the 3.27 g/t Au grade for this stope block in the PEA. The 200 east metre level is being developed and mined in both the hangingwall and footwall zones.

The Clavos mine is dewatered down to the 270 mL with 30 metres remaining to dewater. However, additional infrastructure, including electrical and ventilation, is required to access levels below the 200 mL. This infrastructure is being sourced. The grade x thickness model illustrates that the highest grade x thickness intersections occur below the 200 metre level. The historical records of the Clavos deposit indicate that the previous operator developed down to the 285 mL but did not extract a significant amount of material. It is therefore anticipated that these developed stopes were left in-situ.

The company completed four mill runs between October 2017 and January 2018, as part of its “bulk sampling” program, yielding approximately 1,031 ounces of gold from 18,272 tonnes processed. The material processed so far, primarily represents lower-grade, pre-stope development rock mined by Sage Gold, as well as broken rock left by St Andrew. Processing of the next bulk sample shipment to the Black Fox mill was recently completed.

Underground drilling, blasting and the transport of mineralized material to surface is continuing on the 150 west, 150 east and 200 east metre levels. The current intention is to develop a long hole stope between 100 and 150 West in the footwall structure. The long hole stope will encompass the stope blocks listed in the Preliminary Economic Assessment of 2013. The PEA forecast long hole stope costs of \$85/tonne.

Development also is continuing on 150E and 175E on the Footwall structure with the aim of driving east for the purpose of accessing the hanging wall and footwall stopes that were previously defined in the economic model associated with the PEA.

In addition, cross cuts will access longhole stopes developed by the previous operator for the purpose of removing remnant mineralized material.

From an operational perspective, severe cold weather hampered outside surface crushing at Clavos with numerous mechanical failures limiting the movement of crushed mineralized material from Clavos to the Black Fox mill. The crushing contractor implemented various measures in order to limit breakdowns associated with the cold operating conditions. As a precaution Sage is developing stockpiles at both the mine and mill sites. Progress at Clavos in 2017 was also hampered by Hydro One’s delayed connection

of the mine to the grid. This and the weather issue impacted costs and precipitated a need for further working capital.

### Resource Estimate

The NI43-101 resource estimate dates from October 2012 and was prepared by Roscoe Postle Associates which estimated Indicated mineral resources of 1,258,400 tonnes at 4.81 g/t Au totalling 194,700 ounces of gold and Inferred mineral resources of 796,000 tonnes at 4.7 g/t Au representing 121,000 ounces. These resources are reported at a base case cut-off grade of 2.75 g/t Au and individual assays have been capped at 60g/t.

<b>Clavos - Resource Estimate</b>				
@ 2.75 g/t cut-off				
		<b>Tonnes</b>	<b>Au g/t</b>	<b>Au Ozs</b>
<b>Main Zone</b>				
	Indicated	1,167,100	4.88	183,000
	Inferred	636,000	4.80	98,000
<b>960 Zone</b>				
	Indicated	91,300	3.99	11,700
	Inferred	160,000	4.50	23,000
<b>Totals</b>				
	<b>Indicated</b>	<b>1,258,400</b>	<b>4.81</b>	<b>194,700</b>
	<b>Inferred</b>	<b>796,000</b>	<b>4.70</b>	<b>121,000</b>

### Exploration Work

Continued underground mineral exploration and stope definition/delineation diamond drilling is an important part of the mining operation as detailed mine planning and layouts are dependent upon the availability of information on the grade and configuration of the mineralized structures encountered.

There has been limited drilling down plunge and down dip of the existing Clavos deposit. Historical drill holes yielded high grade intersections 300-400 metres down dip of underground workings:

- KC99-131 : interval from 341m to 350.6m grading 30.5 g/t over true width of 7.38m.
- KC00-159 : interval from 298.5m to 306.5m grading 24.26 g/t over true width of 6.15m.
- KC99-137 : interval from 408.13m to 411.13 grading 30.83 g/t over true width of 2.13m.
- KC99-155W : interval from 650.8m to 655m grading 17.91 g/t over true width of 3.23m.

It should be noted that grade capping was applied to individual assays exceeding 90 g/t.

Sage completed a number of drill holes down plunge of the eastern end of the underground workings and one hole down dip of the centre portion of the Clavos deposit which showed potential economic intersections east, down dip and down plunge of the known Clavos deposit.

In mid-2017 the company announced the results of its surface drilling program which was targeted at the 340-metre gap between the Main Zone and the 960 Zone.

The drill program has yielded three important results:

- the continuity of gold mineralization, specifically the Contact Zone, across the gap between the main mine zone and the 960 zone
- the discovery of a new gold zone (CL-17-07 -- 4.09 g/t Au over 4.2 metres) 100 metres south of the existing sediment zone
- the discovery of the footwall intersection in CL-17-08 of 5.15 g/t over 3.9 metres

The intersection in hole CL-17-08 is important as it opens up approximately 300 metres of strike length of potential mineralization west of the western end of the 150 m west level in the upper part of the existing mine workings.

The results of the eastern drilling open up the possibility of driving further east off the 285 level (mine elevation) through mineralized material out to the 960 zone and potentially further east.

The program consisted of 2,873 metres of surface diamond drilling involving nine drill holes completed from the start of the year to early April. Seven holes were drilled east of the existing mine infrastructure and west of the 960 zone. Two holes were drilled west of the existing mine infrastructure.

The weighted average grade of the composite intervals vary from 16.76 g/t over 1.8 metres returned from drill hole CL-17-02 and 4.43 g/t over

Hole ID	Length (m)	From (m)	To (m)	Av. Grade g/t	True Width (m)
CL-17-01	266	163.5	164.8	1.69	0.9
CL-17-01		174.5	177.3	3.36	2.0
CL-17-02	347	149	152.05	4.32	2.1
CL-17-02		228	229.8	16.76	1.3
CL-17-03	386	181.6	182.6	3.32	0.7
CL-17-03		197.4	199.4	4.93	1.4
CL-17-04	284	191.4	192.4	1.59	0.7
CL-17-05	374	341.65	343.15	3.12	1.1
CL-17-05		364.75	366.5	2.56	1.2
CL-17-06	372	258	263.5	4.43	2.8
CL-17-07	387	268	269	3.89	0.7
CL-17-07		375	381	4.09	4.2
CL-17-08	188	144	149.5	5.15	3.9
CL-17-09	269	91	96.7	1.83	4.0

four metres returned from drill hole CL-17-06.

Hole CI-17-07 has intersected a new sediment zone located 100 metres to the south of the Pipestone thrust fault returning 4.09 g/t over six metres. Drill holes CL-17-08 and 09 intersected significant mineralization at the footwall zone and contact zone establishing continuity along the 150-metre level (mine elevation).

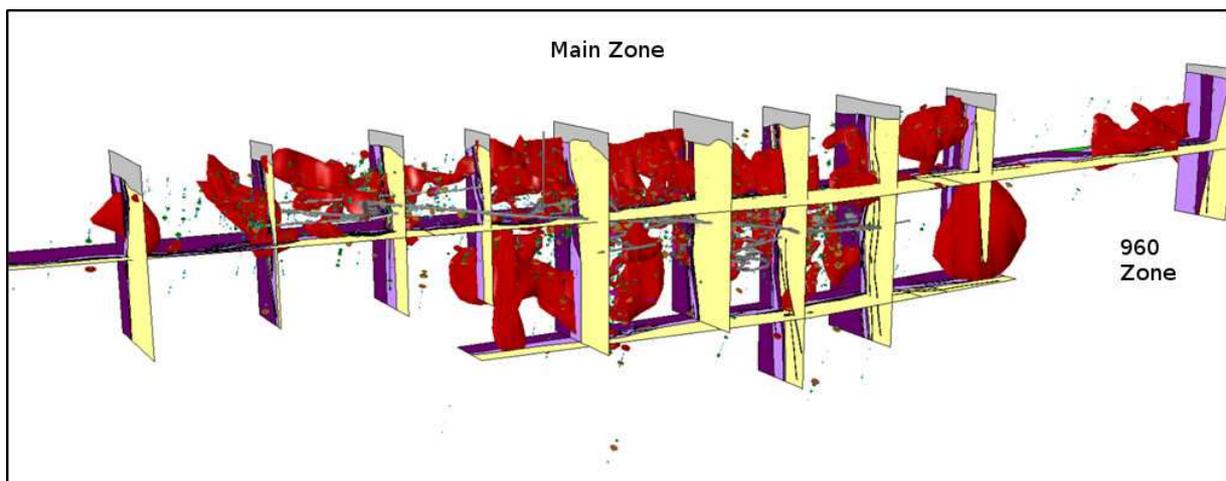
Seven holes targeted a shallow-plunging flexure proximal to offsetting structures possibly controlling gold, arsenopyrite, pyrite quartz vein mineralization located in the altered ultramafics and porphyries flanking the Porcupine group sediments demarked by the Pipestone fault structure. A systematic drill hole spacing of 60 metres was employed to define the plunge orientation of some of the high-grade shoots located proximal to the existing mine infrastructure.

### Resource Expansion

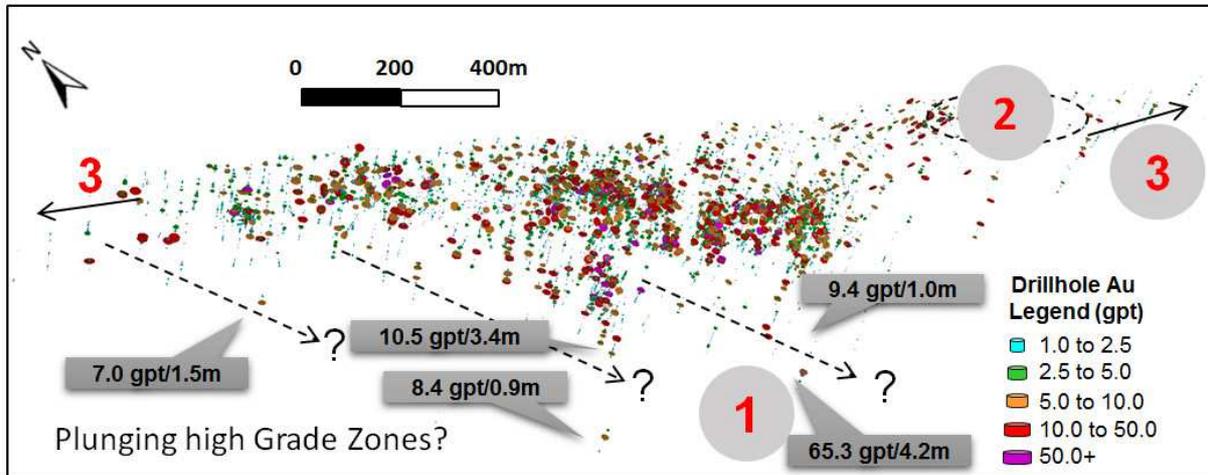
The management of Sage Gold intends to complete a new estimate of Mineral Resources and Mineral Reserves utilizing 1,000 surface and 550 underground drill-hole composites that are now in the gradex thickness database. An additional 200 drill-hole assay composites from more recent underground definition and exploration drilling will also be incorporated.

This Mineral Resource estimation will be the basis for a Pre-Feasibility incorporating the results from surface drilling from east and west of the mine and underground drilling within the mine infrastructure. Sage has now completed all of the geological modeling related to the Clavos deposit. This modeling includes all the lithological units including the mafic and siliceous intrusives. Gold mineralization at Clavos is almost exclusively associated with the intrusives as vein systems on the margins of the intrusives or as quartz breccia zones within the intrusives.

The cross-section that follows shows the significant potential to “join the dots” at Clavos. Firstly there is the connection on the Main Zone to the 960 Zone.



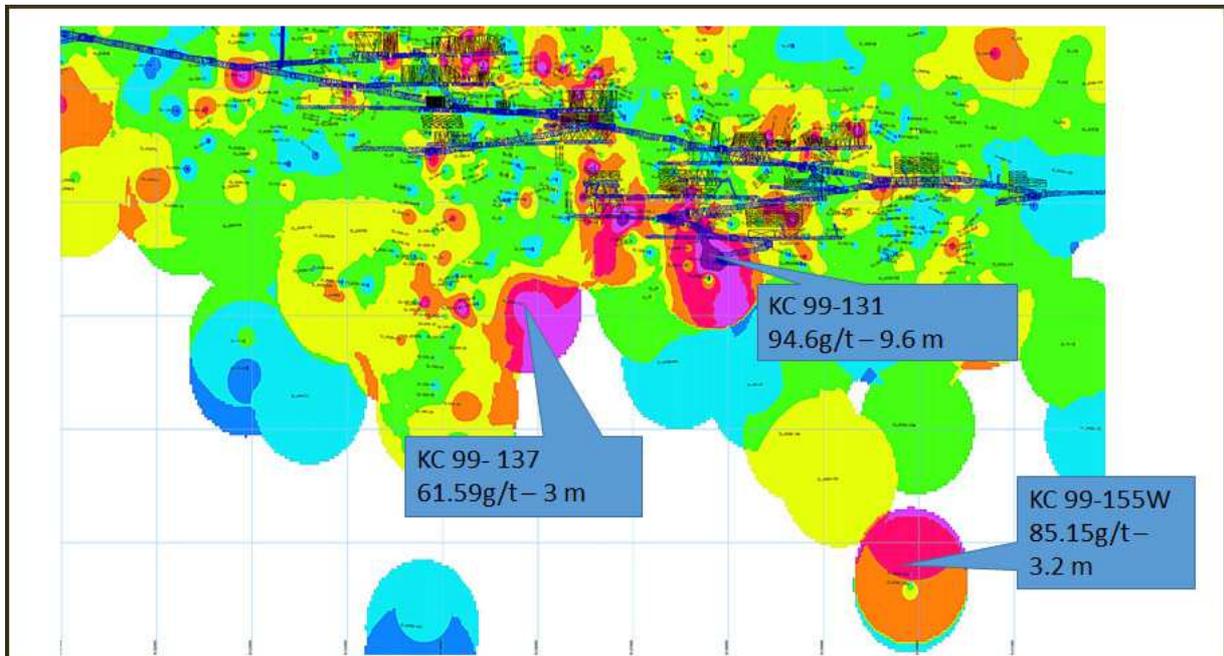
Then there is the potential along strike and down-dip as shown in the drill hole schematic below.



The target areas include:

- Plunging high-grade zones (shown at 1)
- Potential connection between the Main Zone and 960 Zone (shown at 2)
- Extension along strike (east and west directions – marked as 3)

Below can be seen the grade thickness map (with some high-grade holes highlighted).



Underground definition drilling commenced in May 2017 on the 100 metre east level. Further underground drilling will follow from the 225 level to fill in up plunge from KC99-137 and from the 285 and 300 levels to test up plunge from KC99-131 and 155W.

The company expects to publish a new NI 43-101 Resource Estimate in the second quarter of 2018. It will then move to publication of a PFS by year end (even though it expects to already be in production by then but needs a PFS so it can announce production expectations).

In December the company released results from its underground exploration program utilizing two drills, strategically positioned from two drilling bays, to test an exploration target identified by historical Kinross era drill holes KC-99-131, KC-99-137 and KC-00-176, spanning a distance of 200 metres between 513600E and 513800E.

The first six drill holes tested in the vicinity of KC-99-137 with weighted average grade composites listed below. Hole 3531-196 has been completed and assays are pending. All holes have successfully tested favourable Hangingwall and Footwall mineralized structures at Clavos at depths ranging from the 975 metres above sea level (asl) to the 865 metre asl. In the company's view the results from this drilling will potentially extend existing mineral resource blocks.

Hole_ID	Easting	Elevation	From (m)	To (m)	Interval* (m)	Grade (g/t Au)
CL-3531-191	513565	940	148.4	150.0	1.6	5.46
CL-3531-192	513595	920	177.0	179.8	2.8	16.60
CL-3531-193	513612	975	162.0	164.4	2.4	3.50
CL-3531-194	513572	865	220.0	221.4	1.4	1.46
CL-3531-195	513615	900	197.5	201.0	3.5	3.00

\*Intervals reported are downhole lengths and are not corrected to true widths

These holes have been completed with a B-15 electric/hydraulic drill from a south drift cross-cut bracketing the 120 metre gap between Kinross hole KC-99-137 and KC-00-176 piercing the 350 mL elevation. There is no existing mine infrastructure in this region.

In December of 2017 the company was undertaking a five-hole underground drilling program using an air/electric drill, testing between Kinross holes KC-99-131 and KC-00-176 at elevations ranging from the 280 mL to the 300 mL. This drilling program is near existing mine workings.

### **The Gold Prepayment Financing**

In September of 2016, Sage agreed a Gold Prepayment financing with Cartesian Royalty Holdings. Under the agreement Cartesian committed to provide Sage with CAD\$9.65mn payable in two tranches. In

consideration, Sage agreed to deliver to CRH 15% of gold produced at Clavos commencing on the later of (i) the beginning of Commercial Production and (ii) 12 months from the date of payment of the first tranche of the Gold Prepayment, but in all cases no later than December 27, 2017, for a period of 72 months of Commercial Production, subject to a minimum total delivery of 16,100 ounces of gold and a maximum of 26,000 ounces of gold. In the event that the minimum has not been delivered within the 72 months, the delivery obligation will continue until the minimum has been delivered to CRH. The obligations under the Gold Prepayment are secured against all of the assets of Sage, including its interest in the Clavos project.

As per the Gold Prepayment Agreement, Sage Gold received the first tranche of CAD\$4.39 million in November 2016, the second tranche of CAD\$2.0 million in March 2017 and the third and final tranche of CAD\$3.26 million in July 2017. In February 2018, the first repayment to CRH was made pursuant to the Gold Prepayment Agreement.

### **Recent Financing**

As noted, in order to minimize the amount of start-up capital required, a decision was made to utilise contract crushing, hauling and milling. Consequently the company is somewhat constrained by the scheduling of services of these outside parties resulting in the working capital cycle being longer than originally planned, which has necessitated additional financing.

In January 2018 the company undertook a Treasury offering which, due to stronger demand than expected, became a four-tranche offering of units at the price of 11 cents per unit. Each unit consisted of one common share of the company and one common share purchase warrant. Each warrant entitles the holder to purchase one common share at an exercise price of 16 cents for a period of 24 months following the closing of the offering.

The offering, comprising the first tranche closed on Jan. 15, 2018, the second tranche closed on Jan. 18, 2018, and the third tranche, consists of the sale of 17,264,953 units in the aggregate for gross proceeds of \$1,899,074.86. Following the completion of the second tranche, 103,496,473 common shares will be issued and outstanding. The third tranche of the offering consisted of the sale of 7,298,909 units for gross proceeds of \$802,879.99. The fourth tranche of the offering consisted of the sale of 3,914,726 Units for gross proceeds of \$430,620.01.

As a result of the interest in the issue, the offering was oversubscribed, and total proceeds amounted to nearly \$2.36mn, representing an over-subscription of \$1mn.

In addition to the above, Sage's management is in the process of negotiating an equipment loan facility in order to provide funding to access the high grade stopes below the 200 mL identified by St Andrew.

### **Risks**

Amongst the risks at the current time are:

- Gold price risk
- Financing in the markets is still tenuous
- Difficulties or inability to expand resource

The gold price is somewhat in the lap of the gods. We have been relative bears on gold (with a no-change stance) and ironically now that the Trump election presages inflation, the gold bugs have gone into retreat fearing higher interest rates more than they fear inflation. This is rather paradoxical. If inflation stirs on the back of loose fiscal policy then the gold price could be a beneficiary.

Working capital will remain tight until the grade of the bulk sample shipments increases as the company mines higher grade zone targets over the next two months and increases mining rates. Longer term it would be attractive to issue equity (at a much higher price) to dilute the Cartesian position as its shares become vested or the warrants are exercised.

The latest drill results show there is more to find in all directions at Clavos. Grade control is improving as knowledge and understanding of the deposit has improved, which will culminate in the estimation of an updated Mineral Resource, potentially enabling mine life extension.

### **Conclusion**

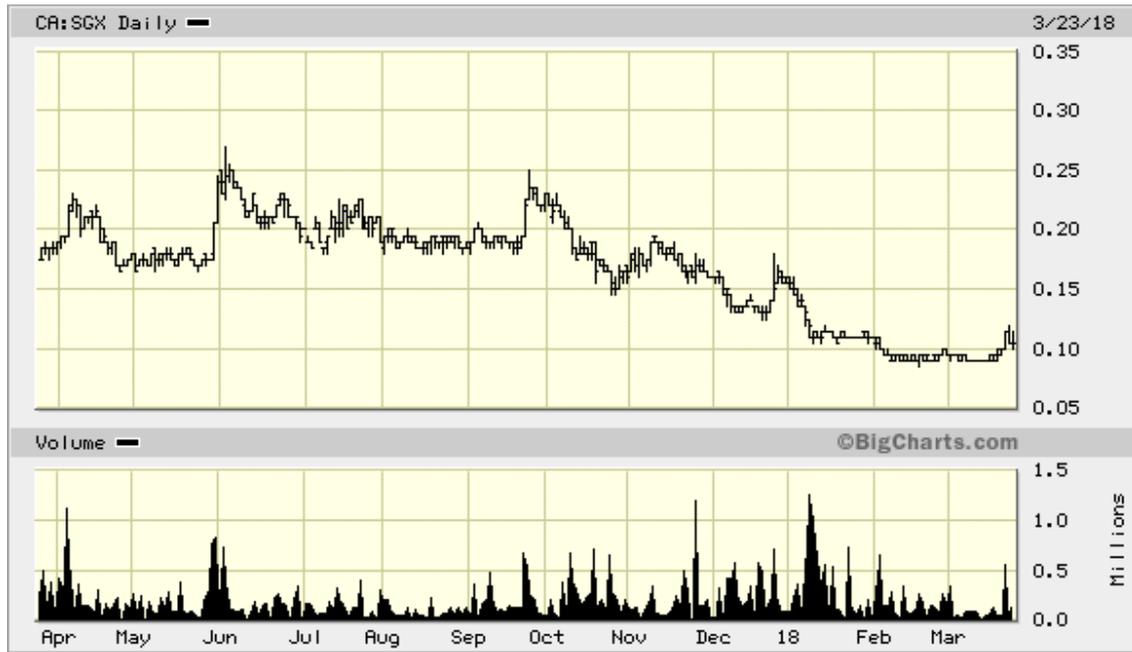
The move to production rarely runs smoothly and at Clavos this has been no exception with five shipments having been sent to the mill despite exceptionally adverse weather conditions in recent months.

With dewatering of the lower levels nearing completion, production should be ramping up in the first half of 2018. With mining stocks having retreated from 2016 highs the old discriminator of producer versus developer/explorer comes back into play and the move by Sage Gold into production moves it into the most favoured category of mining stocks, those with cashflow.

The current year will give management the opportunity to show how a junior can succeed where a well-known mid-tier could not. The secret, we believe, is a combination of a team that is heavy with skills from first tier players (two of the board are involved at Yamana) combined with restoring the previous synergies of the various assets and doing so with a strict approach to costs and efficiencies.

Therefore we reiterate our **Long** rating on Sage Gold with a twelve-month share price target of CAD\$0.49.

Monday, March 26, 2018



## Important disclosures

I, Christopher Ecclestone, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers.

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Company's Disclaimer: Sage Gold completed and filed a Preliminary Economic Assessment on April 22, 2013 in relation to the Clavos project. The PEA does not indicate the economic viability of the estimated Mineral Resource and is preliminary in nature, includes Inferred Resources that are considered too speculative geologically to have the economic considerations applied to them that would enable them to be categorized as Mineral Reserves and that there is no certainty that the PEA will be realized. Mineral Resources that are not Mineral Reserves do not have demonstrated economic viability.