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HALLGARTEN & COMPANY

Portfolio Strategy

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Model Mining Portfolio:

Undeclared War in Metals & Minerals

Performance Review – March 2018

Model Mining Portfolio

Undeclared War in Metals & Minerals

- + **More Zinc projects, like Telson's Campo Morado, are gearing up. Most are mid-sized so nothing to upset the apple cart of an undersupplied market.**
- + **Tungsten prices continue to creep inexorably higher**
- + **The Vanadium price has gained a second wind and is moving up again**
- + **US duties on depleted Uranium imports from China may be first recognition of the damage that Uranium imports have dealt to US uranium self-sufficiency**
- ✘ **The Gold price is becoming an inanimate object unresponsive to any outside stimuli**
- ✘ **Base metals are drifting aimlessly with Copper at one point even threatening to slip under the $3 per lb mark**
- ✘ **Cobalt continues to rise to the joy of promoters, but bringing nearer the day at which it will need to be replaced in key battery metal configurations**
- ✘ **US government stockpiles of Helium should be sold out in the near future – another victim of short-termism**
- ✘ **The Canadian dollar is improving against the US dollar with implications for the margins of gold producers north of the border**

The Phoney War Gets Real?

In the latter months of 1939 into early 1940 the British referred to the quiescence in the period after the declaration of war against the Axis Powers as the Phoney War. As it turned out it was not exactly so "phoney" but managed to lull some of the combatants into a state that made them more vulnerable when the bullets actually started flying.

Love him or hate him, Donald Trump has certainly fired the first shots from the side of the "Good Guys" in what has been a long undeclared war over global commodities and economic dominance. The "foe" in this battle is clearly China. That the Chinese have used dirty tricks is undoubted, that the West has been feeble, accommodating and downright appeasing is also undoubted.

The WTO was supposed to be umpire in the new global trade game, however it has long been clear that the WTO is a weapon that is only sharpened on one side. If China had never joined the WTO (a League of Nations for our times) then those countries that play by the rules would have been a lot less blinkered in the response to the gradual Chinese "mission creep" that they have been subject to in a whole swathe of industries whether they be steel, textiles or plastics.

For those of us in the mining industry the blatant manipulation of export quotas, import quotas, taxes and duties thereon have been perennial bugbears, with the Rare Earth space being the poster boy for blatant manipulation. Other areas (e.g. the "FANYA metals") have been also victims of price ramping, metals hoarding, criminality, misinformation and disinformation. Traders in metals have long regarded the Shanghai warehouses as little more than an oversized shell game used to control the prices of commodities at a global scale.

In this "war" it has been the private sector that has been picked off. Governments on the other hand have glad-handed with the enemy seeing deluges of "cheap stuff" as a good way of pushing down inflation and keeping the wages of domestic "riffraff" under control through job exporting to enemy territory. The main two pushbacks against this were the Brexit vote in the UK and the Trump election but other signs have been there, for those that want to see them, such as the upsets in the German, Austrian and Italian elections over the last year.

Tungsten is a microcosm of the issue. China has distorted the Tungsten market much as it has distorted so many others. China has brutally manipulated the price of this metal for decades and almost managed to wipe out the Western producers (much as it did with Antimony) with the policy goal being to overrun the machine tool sector through its Tungsten dominance. This put Western manufacturers of this equipment (chiefly the Germans and Swedes) on notice that they needed guaranteed non-Chinese supplies to evade predatory Chinese manouevres. That machine tools are a key component in many defence industries goes without saying.

To deal with this one of the major European machine tool players decided to "sponsor" Almonty's survival and expansion by paying over the market price for APT to ensure that Almonty survived and prospered as an alternative to the inevitable Chinese near-monopoly if it had gone under.

Western machine tool makers are particularly vulnerable to supply disruptions as, we might tactfully say, it would be to the benefit of Chinese toolmakers to have foreign competitors experience supply problems from the Chinese tungsten mines. If any investors doubt that that might happen then they would be naive indeed.

This defensive action by a Western end-user was a rare one though. The predatory actions of China have gone largely unchecked. The purchase for an over-the-top price of the newly opened Beaverbrook Antimony mine in Newfoundland was quickly followed by its closure with the highly expectant local workforce finding themselves on the dole and Canada finding its entrance into the Antimony space forestalled. Peru was left bemused when the Galeno copper/gold/moly property of Northern Peru Copper was bought by the Chinese for CAD$455mn in 2007 and then put in the freezer. Then we have even dirtier games like the seizure (from Trimetals Mining) of the Malku Kota silver/indium project in Bolivia, which effectively blocked the Korean flatscreen manufacturers from getting access to 25% of the world's Indium. We expect this to eventually make its way into Chinese hands when no-one is looking. Other manouevres in Bolivia involve positioning themselves in the massive lithium Salar de Uyuni.

In a recent note entitled *America's Metals, Minerals, and Materials Misery*, Mickey Fulp a well-known commentator on the metal's space noted "China is our primary, secondary or tertiary source for 31 commodities, mainly specialty metals and industrial minerals with small markets" and then goes on to say "Of the 31 for which we are dependent on China as the first, second, or third largest supplier, seven are stockpiled: cobalt, germanium, lithium, quartz crystals, titanium, tungsten, and yttrium".

Quite clearly China has a key grip on the US (and the West's) supply of critical metals and that the stockpiles are inadequate or non-existent to counter this. This leaves the West extraordinarily vulnerable to Chinese machinations.

So what are the manifestations of this undeclared war:

- Accumulation of metals both above and below ground in a broad geographical spread of jurisdictions
- In-country stocks of metals that are revealed and unrevealed at will effecting prices in the global market
- Substantial control of supply of a number of strategic metals
- Strategy to force the value-added and upgrading of metals within the "mothership"
- A large émigré population inserted into Western economies in strategic positions in commerce and educational/research institutions

We could go on but we feel that the rise of China bears all the hallmarks of something more than just the rise of a new economic power. One could draw parallels to the period 1900-14 when the rising Germany seemed set to topple the long-dominant Britain off its economic throne. A key difference now is that in that tussle Britain was strongly resourced in minerals both onshore and offshore while Germany was disadvantaged in not having the same reach. If Germany had tried the same tactics then, as China is trying now, the First World War would not have been postponed to as late as 1914.

One might remember Pig-Iron Bob. This was the Australian PM, later Sir Robert Menzies, who was chastised in the 1930s for selling Australian pig iron to the Japanese. Come 1941, he found the Japanese were returning the pig-iron in the form of bombs, just as the critics had foretold.

We have a situation where the West in now in a type of thrall best compared to that of the small insect being eyed up by the Preying Mantis. The victim does not know it's in peril until its head is bitten off. In many ways the mining industry has been ground zero for observing the territorial landgrab which has not, so far, involved armies on the move.

Politicians (and the public) need to seize back the initiative from corporates who have seen China as their lunch ticket providing cheap goods and on-going downward pressure on ornery industrial workers. Their self-interest has sold everyone else down the river. The Faustian deal of selling one's soul to China for some brass farthings is already being seen in some quarters for what it is. It's time for the West to get smart and defend its interests (and mineral assets) before it is too late.

Portfolio Changes

There were four portfolio changes during the month of March:

- Augmented our Long position in Ascendant Resources. Bought 100,000 shares in ASND.to at CAD 97 cents per share on the 27th of March.
- Closed our Long position in Patagonia Gold. Sold 2,000,000 shares in PGD.L at UKP 1.40 per share on the 27th of March.
- Closed our Long position in Teranga Gold. Sold 120,000 shares in TGZ.to at CAD$4.15 per share on the 19th of March
- Opened a Long position in Telson Mining. Bought 200,000 shares in TSN.v at CAD 79 cents per share on the 19th of March.

We had made a substantial gain on our Teranga position (which was also very oversized) so we decided to take profits on that during the month.

Patagonia Gold has been a continuous source of frustration and disappointment. Its failure to respond positively to either the change of government or improved margins (in theory) for gold operators eventually decided us on the need to part company.

The surfeit of cash from Teranga meant that we have become excessively liquid. To remedy this we decided to enhance our position in Ascendant Resources despite it having gained strongly since initiation of the original position. Having met with Telson Mining (another company having picked up ex-Nyrstar assets) we decided to initiate a position in that Zinc miner also.

The old expression about putting lipstick on a pig comes to mind with Bacanora's delisting from the TSX-V to focus on its AIM listing. Effective at the close of business on Friday, March 23, 2018, the common shares of Bacanora Minerals Ltd were delisted. This resulted from a newly incorporated U.K. company (Bacanora U.K.) acquiring 100% of the company's shares pursuant to an arrangement agreement dated Feb. 16, 2018. Bacanora Minerals shareholders received one share of Bacanora U.K. for every share held. The stock managed a bounce in early trading on the back of an announcement that the Prudential insurance company had (just) passed the 10% reporting threshold. That this looks like a ramping exercise is purely coincidental.

Noble Group is a situation in a state of flux with a debt restructuring threatening the equity holders.

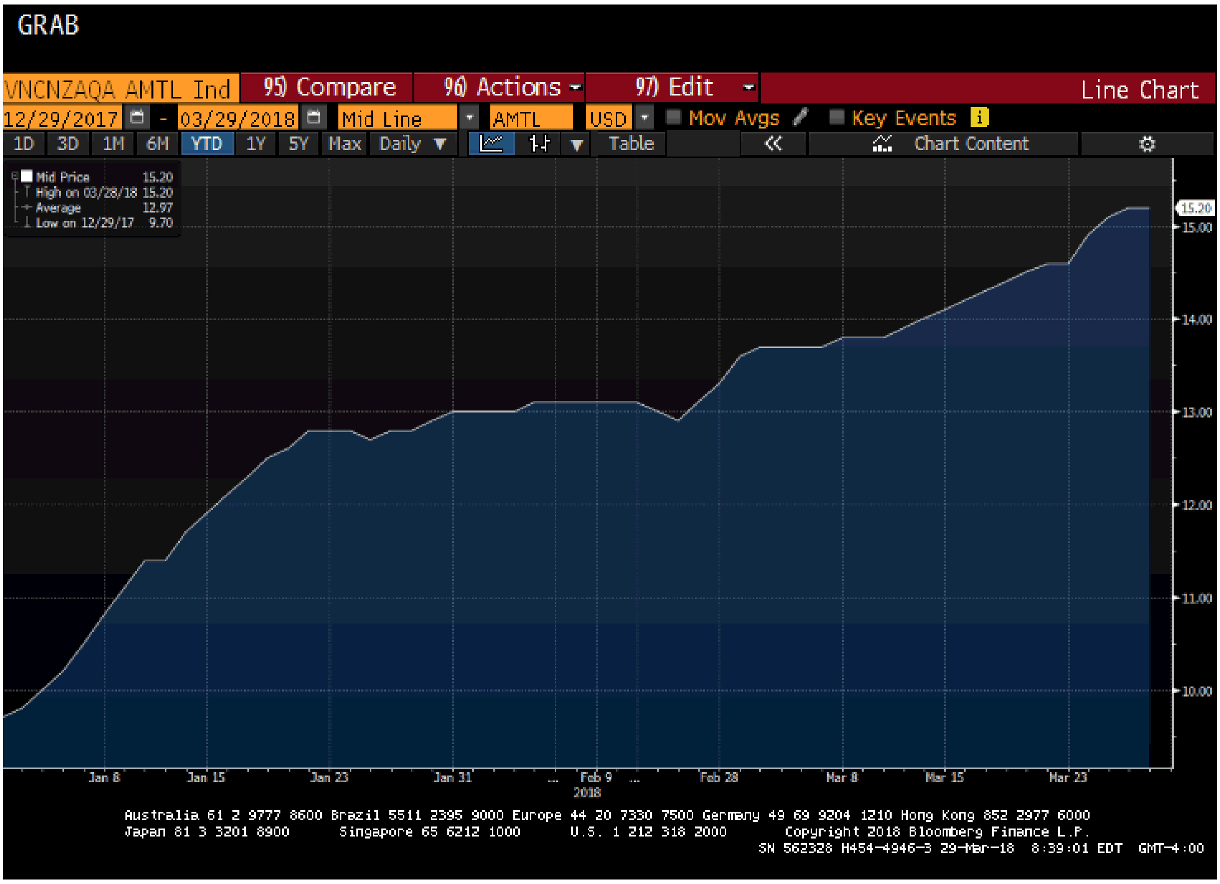
How that plays out for our position is not clear as yet.

The Portfolio Move

The portfolio shed some more value in March closing at $4.974mn down from US$5.044mn at the end of February. Cash rose again to $1.373mn from $1.150mn during the month due largely to the Teranga sale.

Vanadium Back to the Upside

Unlike its spiking movement last year the recuperation in Vanadium has been somewhat like that of Tungsten, gradual and "easy does it". This minimizes the dangers of a pump-and-dump from hot money trading metals that trade in small lots at the best of times. The price has now breached the $15 per lb mark and that is without any Chinese *diktats* (yet) on V content in steel alloys.



Telson Mining – Another Phoenix from Nyrstar's Ashes

In the annals of mining history it will be written that Nyrstar's big mistake was buying high and selling low. Thus far three companies have appeared on the radar as bottom fishers picking up Nyrstar's leftovers and showing (potentially) what can be achieved from assets that Nyrstar could not make a go of. Two we have highlighted in the recent past are Morumbi (now Ascendant Resources), Great Panther Silver and now Telson Mining (the former Soho Resources) is added to the group.

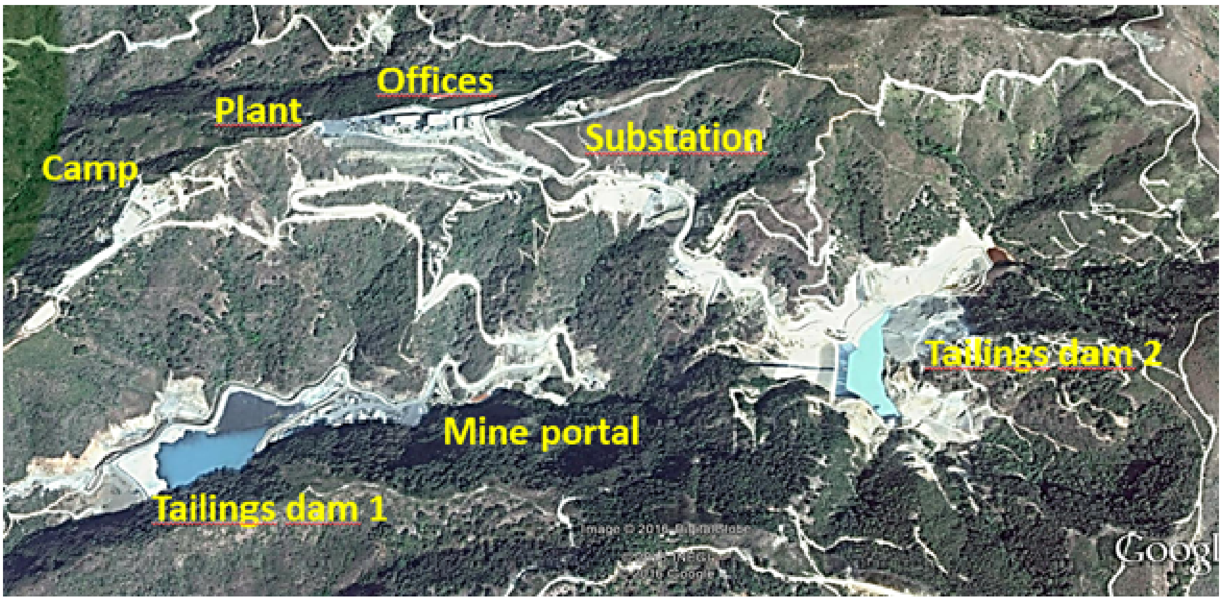
We met with Telson in London mid-March and it was an illuminating sign of how Canadian miners can change their spots. Traditionally Canadian geos have stuck to the tired (and nonsensical) mantra that they must find a deposit then sell it. This strategy has singularly failed for droves in recent years. In this case though the long-time CEO, Ralph Shearing (a geologist) has drafted in a crew of Mexican mining experts to facilitate in the company integrating its $20mn purchase of Nyrstar's Campo Morado asset in Guerrero state in Mexico. This asset had been a key drawcard of the $420mn purchase of Farallon Resources by Nyrstar in December of 2010.

With its impeccably bad timing Nyrstar sold this asset in June 2017 to Telson Resources just as Zinc was in moving into turbocharged mode. Ever was it thus…

That Telson decided to drop the "Resources" from its name and switch to "Mining" was one in the eye for do-nothings of the TSX-V "explore till you drop" school of thought.

The company terms itself as being in pre-production at two projects and advancing towards commercial production at both of these over the coming months of 2018.

The Campo Morado project hosts several polymetallic massive sulphide deposits containing zinc, copper, silver, gold and lead mineralization. Five deposits have been extensively drilled: G9, El Largo, Reforma, Naranjo and El Rey.



The project is comprised of a previously mined underground multi-metal mine with infrastructure, installations and equipment capable of processing 2,500 tonnes of material per day. Farallon began mining operations at the G9 Mine at Campo Morado in April 2009. After Nyrstar purchased Farallon it continued mining operations at G9 mine with some production from the El Largo deposit until production was suspended in January 2015 and the mine was placed on care and maintenance. Just in time for the Zinc price upturn, we might note.

Telson Mining Corporation purchased the Campo Morado Mine from Nyrstar in June 2017 and restarted mining operations under a preproduction plan and initiated production of zinc concentrates in October 2017. Telson intends to advance preproduction towards full commercial production during 2018. The purchase price of the Nyrstar Group subsidiaries that own the Campo Morado Mine was US$20mn of which US$3.5mn has been paid and the balance of US$16.5mn is due to be paid on or before June 13, 2018.

At Campo Morado, Telson has re-commenced mining and processing operations with pre-production from mine development on a trial basis at 1,400 tonnes per day and intends to advance towards commercial production at full capacity of approximately 2,500 tonnes per day during 2018.

For a very long time the Tahuehueto Project, located in north-western Durango State was the main target at Telson/Soho. While it is currently in pre-production the deal with Campo Morado has somewhat stolen the limelight. Mining is proceeding at approximately 150 tonnes per day utilizing a toll mill for processing and the project has entered a construction phase with a timeline to be producing on site in its own mineral processing plant capable of milling at least 1,000 tonnes per day towards the end of 2018.

Nevertheless regular metal concentrate delivery and sales are underway from both projects even though commercial production has not been declared. We were told that Campo Morado at least should be declared as commercial production before the end of 2Q18.

Bringing one Zinc mine into production is feat enough in this day and age and now Telson has two on the verge of commercial production. The message from other Nyrstar cast-offs is that invariably these deposits were not understood or developed correctly by their erstwhile owner and that they do better on the “second-go-around”. Telson is one of the few companies that have positioned themselves in the right metal at the right time. We have added a position to the Model Mining Portfolio during the month.

Parting Shot

Back-biting seems to have returned to the mining investment scene. Our first encounter with this was during the Rare Earth boom. Certainly opinions were divided over different mineralisations but as the players in the space came to realise that there might only be a finite number of spaces in the Rare Earth lifeboat the fight for position in this vessel of salvation turned vicious. Did it take the form of being more competent, more honest and being the best stewards of investors’ funds? No, it took the form of bitchy innuendo and savage stiletto attacks on the executives of “competing” companies. However it was not only some executives who indulged in this, it was their partisans, in many cases investors who had hocked their grandmother's glass eye to get a position in Tin Pot Rare Earths and suddenly found it wasn't worth a brass *razoo*. Curiously though, these investors (and managements) imagined that by bad-mouthing their *confreres* that somehow it will help their own share price go up. The main effect was to throw the whole sub-space into disrepute as a pack of caterwauling fishwives.

Then in recent times we have seen this recur in the Lithium space. One would think there was enough gravy to go around but instead we witnessed sharp elbows flailing on all sides. We attended a lunch for one of the Argentine lithium plays where the speaker blithely waved his arm and claimed that one of the Chilean players "had problems with their licenses". Wrong… Then another had their map of the many lakes in Argentina and had conveniently included only the very biggest players and smallest players and removed all mention of any of the developers that were the same size as they were. Or there was the TSX company that removed all the other TSX players from their map and only mentioned the ASX "competitors' perceiving that they might be accidentally be giving a free plug for their Canadian brethren if they were shown on the map. And finally there was a company that kept referring to Bearings Lithium as the owner of the Maricunga deposit despite it only having a 17% stake, because to mention the real owner/manager might have investors heading off in that direction.

Lastly we have the muttering under the breath about a famed new/old Zinc play in the US northwest where a certain old chestnut about the former major shareholder in the shell that was repurposed keeps being dragged up as a reason not to believe in what is clearly the deposit with the most potential to add meaningfully to US Zinc production in the short to medium term.

There are reasons to highlight the comparatives on projects but to indulge in needless stiletto-wielding is not helpful to one's own equity positions in companies in the same sub-space. As we observed recently to one of the survivors in the REE space, the companies that were most vigorous in their backbiting in the Rare Earths Boom 1.0 are now no longer with us.

Mining Model Portfolio as at: 31-Mar-18

	Security	Initiated	Currency	Price Avg.	Current	Portfolio Weighting	Increase in Value	Target
Long Equities								
Various Large/Mid-Cap	Teck Resources (TECK.B)	5/29/2009	CAD	22.46	33.18	9.9%	47.7%	$38.00
	NevSun (NSU)	3/23/2012	CAD	3.45	3.07	3.5%	-11.0%	$5.00
	Sherritt International (S.to)	7/11/2013	CAD	1.78	1.13	3.9%	-36.5%	$2.50
	Metals X (MLX.ax)	29/5/2014	AUD	0.98	0.72	2.2%	-26.4%	$1.00
Trading House	Noble Group (CGP.SG)	15/11/2017	SGD	0.2	0.08	1.3%	-59.8%	$0.30
Uranium	Uranium Participation Corp (U.to)	10/20/2010	CAD	7.01	3.86	2.2%	-44.9%	$6.00
	Western Uranium (WUC.cx)	7/5/2016	CAD	2.25	0.78	1.1%	-65.3%	$4.80
	GoviEx (GXU.v)	6/29/2015	CAD	0.08	0.20	5.5%	143.4%	$0.50
Zinc/Lead Plays	Zinc ETF (Zinc.L)	1/15/2010	USD	7.04	9.45	2.8%	34.2%	$11.00
	Canadian Zinc (CZN.to)	12/9/2011	CAD	0.82	0.13	0.4%	-84.1%	$0.70
	Ascendant Resources (ASND.v)	10/31/2016	CAD	0.49	0.96	6.5%	96.4%	$1.70
	Telson Mining (TSN.V)	3/19/2018	CAD	0.79	0.84	7.0%	6.3%	$2.00
	Nyrstar (NYR:BR)	9/28/2009	Euros	65.1	5.71	3.7%	-91.2%	€ 11.00
	Southern Silver Exploration (SSV.v)	8/25/2016	CAD	0.26	0.485	2.8%	86.5%	$0.94
Gold Producers	Para Resources (PBR.v)	2/17/2017	CAD	0.23	0.19	2.2%	-17.4%	$0.58
	Westgold (WGX.ax)	12/6/2016	AUD	2.01	1.50	3.0%	-25.4%	$2.40
Copper Producer	Coro Mining (COP.to)	2/23/2015	CAD	0.03	0.1	2.3%	233.3%	$0.30
	RNC Minerals (RNX.to)	11/17/2016	CAD	0.33	0.25	1.7%	-24.2%	$0.60
Royalty Trust	Abitibi Royalty (RZZ.v)	5/31/2017	CAD	9.1	10	2.5%	9.9%	$18.00
Processor	IBC Advanced Alloys (IB.v)	4/29/2016	CAD	0.3	0.25	0.6%	-16.7%	$1.40
Driller	Cabo Drilling (CBE.v)	9/28/2016	CAD	0.025	0.01	0.5%	-60.0%	$0.08
Tungsten Producer	Almonty Industries (AII.v)	7/31/2015	CAD	0.36	0.5	5.7%	38.0%	$1.00
Copper Explorer	Asiamet Resources (ARS.v)	4/28/2016	CAD	0.05	0.12	4.0%	135.0%	$0.12
	Panoro Minerals (PML.v)	1/22/2018	CAD	0.32	0.37	2.5%	14.1%	$0.65
	Western Copper & Gold (WRN.to)	4/25/2017	CAD	1.57	1.02	2.3%	-35.0%	$2.74
Lithium	Neometals (NMT.ax)	7/31/2014	AUD	0.04	0.32	3.6%	764.9%	$0.45
	Lithium Power Intl (LPI.ax)	10/25/2017	AUD	0.44	0.34	2.3%	-22.7%	$1.38
Scandium Explorer	Scandium International (SCY.to)	8/23/2016	CAD	0.14	0.19	2.6%	35.7%	$1.00
Gold Explorer	Banyan Gold (BYN.v)	11/14/2017	CAD	0.07	0.06	1.8%	-14.3%	$0.25
Graphite Producer	Elcora Resources (ERA.v)	29/5/2014	CAD	0.2	0.35	4.0%	75.0%	$0.64
Graphite Developer	Talga Resources (TLG.ax)	8/25/2016	AUD	0.27	0.83	4.7%	213.2%	$0.90
REE Explorer	Northern Minerals (NTU.ax)	6/9/2011	AUD	0.23	0.08	1.2%	-65.9%	$0.28
	NET CASH					$1,373,730		
						Weighting		
Shorts	Bacanora (BCN.L)	12/4/2015	GBP	0.825	0.935	38.40%	-13.30%	£0.60
	Lithium Americas (LAC.to)	10/25/2017	CAD	10.1	6.98	36.8%	30.9%	$5.00
	Galane Gold (GG.v)	4/28/2016	CAD	0.06	0.06	24.8%	0.0%	$0.03

Current Cash Position	**1,373,730**
Current Liability on Shorts Not Covered	**205,887**
Net Cash	**1,579,616**
Current Value of Bonds	**0**
Current Value of Long Equities	**3,394,543**
TOTAL VALUE OF PORTFOLIO	**4,974,159**

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