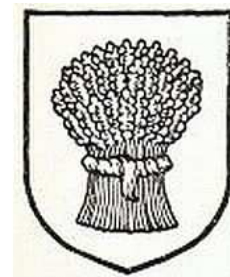


Monday, February 9, 2015



# HALLGARTEN & COMPANY

## Coverage Update

Christopher Ecclestone  
[ceccestone@hallgartenco.com](mailto:ceccestone@hallgartenco.com)

## Almonty Industries (AII.v) Strategy: Long

Key Metrics		2014	2015e	2016e
Price (CAD)	\$ 0.70		n/a	n/a
12-Month Target Price (CAD)	\$ 1.32		\$0.19	\$0.26
Upside to Target	89%			
High-low (12 mth)	\$0.52 - \$0.95			
Market Cap (CAD mn)	\$ 39.1			
Shares Outstanding (millions)	55.90			
Market Cap (pro-forma)	\$ 72.1			
Shares O/S (pro-forma est.)	103.00			
Consensus EPS			n/a	n/a
Hallgarten EPS			\$0.19	\$0.26
Actual EPS		\$0.24		
P/E		2.9	3.7	2.7
Dividend		\$ 0.0272	\$ 0.05	\$ 0.05
Yield		3.9%	7.1%	7.1%

# Almonty Industries

## Merger with Woulfe Makes a Tungsten Major

- + Merger with Woulfe mining gets the ball rolling on Tungsten consolidation
- + Deal takes a major project that was dead in the water and lights a fire under it
- + Strong balance sheet and cashflow at Almonty mitigates against major needs to finance the new addition's capex
- + The projected capex has been halved to \$74.4mn by right-sizing the project
- + Almonty has announced a special cash dividend of \$0.0272 per share in August 2014 (and intends to declare dividends on an annual basis)
- + China has been restricting exports in recent years. This may be either due to a desire to stockpile material for its own future use or a sign that heavy over-exploitation in recent decades has left the country in a vulnerable supply situation
- \* The Tungsten price has shown itself to be highly volatile in recent years. If it falls below \$250 per MTU, investment dries up and some mines become uneconomic

### **Bulking Up at Almonty**

The announcement of the merger between Almonty and Woulfe (CSE:WOF) took us by surprise despite the fact that we had been advocating the creation of a geographically diversified Tungsten player for some years now. The combined business will have two producing tungsten assets located in Spain and Australia and pre-construction assets in South Korea and Spain. We had also mentioned Woulfe as maybe the initiator of this process rather than the target. In any case it's good news.

Almonty's principal assets are the Los Santos tungsten mine, producing 1,100 tpa of WO<sub>3</sub>, and the Wolfram Camp tungsten and molybdenum mine in Queensland Australia, which produced 700 tonnes of WO<sub>3</sub> in 2013. It is working towards the commissioning of the Valtreixal tin/tungsten mine in north western Spain with anticipated production in 2017.

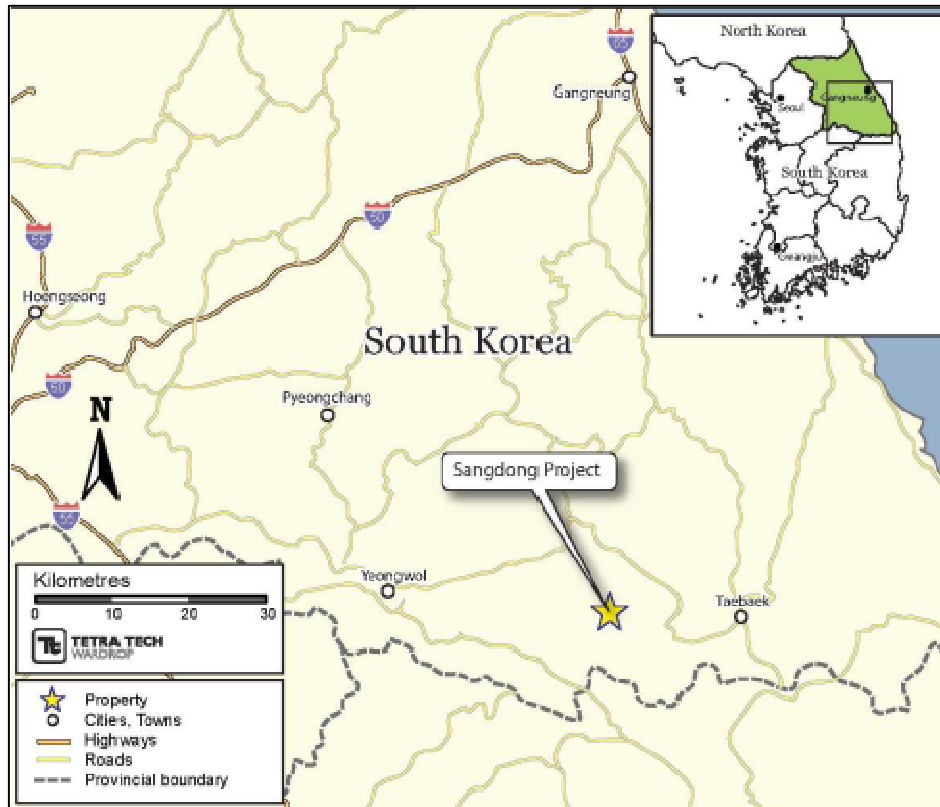
The mining space has needed a Tungsten champion for some time now (as do some of the other specialty metals). A series of one-mine/one-country Tungsten plays have come to grief due to their mono-focus and their failure to look beyond the mine-life of their main asset. Almonty dared to make a move on Ormonde to secure its future in Iberia and when blocked did not skulk off to sulk but rather regrouped and added an asset in Australia. Now it is adding short-term production in South Korea.

### **The Prize – the Sangdong Tungsten-Molybdenum Project**

Woulfe's principal asset is the 100%-owned Sangdong Tungsten/Molybdenum project located in South

Korea, located 187km southeast of Seoul. However this is subject to a third party – the very fickle Israeli group IMC - which may purchase a 25%-ownership interest in Sangdong for US\$35 million. The property is comprised of 12 Mining Rights with an aggregate area of 3,173 hectares.

The Sangdong project was, before its closure in 1992, the world's leading producer of tungsten for 40 years. Low metal prices, not the exhaustion of resources, led to the mine's premature closure. The historical production rate averaged 600,000 tpa mainly from the six-meter thick Main Vein.



The scoping study indicates that the property has over 40 years' of mine life remaining. Substantial underground infrastructure is in place and Woulfe has reopened the mine to a distance of 1.4 km. The above-ground infrastructure includes access to roads, water and power.

Drilling conducted by KORES in 1980-1987 discovered a deep molybdenum deposit below the remaining tungsten skarn resources. The molybdenum content in the Sangdong mineralized zones ranges from 0.04% to 0.06% MoS<sub>2</sub> and an additional zone of molybdenum mineralization, as outlined by historical drilling, lies below the Sangdong mineralized zones.

Woulfe recently completed a de-risking review of its final Feasibility Study report based on the Tetrattech 2012 feasibility report on the Sandong project. We shall discuss mining plans further along in this review.

## **The Deal**

In late January it was announced that Almonty had entered into an agreement with Woulfe Mining to merge the businesses of the two companies. Those with longer memories will recall we have covered Woulfe several times in the past, with fluctuating sentiments towards management, but never wavering in our interest in the asset itself.

The deal in this instance was a non-binding letter of intent to combine the businesses of the two companies and create what Almonty claimed to be the leading tungsten company outside of China.

Under the terms of the LOI, Almonty shall acquire all of the outstanding common shares of Woulfe at a price of CAD\$0.08 per share to be satisfied by each Woulfe share being exchanged for a fraction of an Almonty common share, with such fractional Almonty common share having a fair market value on the effective date of the proposed Transaction of CAD\$0.08 (fair market value will be determined based on the Almonty volume weighted average trading price for the five trading days ending on the third trading day prior to the effective date of the Proposed Transaction). The Almonty issuance is capped and collared and cannot be greater than 0.1231 of one Almonty common share (CAD\$0.65 Almonty VWAP) or less than 0.0942 of one Almonty common share (CAD\$0.85 Almonty VWAP).

The CAD\$0.08 price represented a 22.7% premium to Woulfe's 30-day volume weighted average price for the period ending January 26, 2015. Upon completion of the merger, Woulfe shareholders will own approximately 41% to 48% of the merged entity, depending on the Almonty VWAP. Frankly this is a VERY good deal for the shareholders of the beaten-down Woulfe. Most prominent amongst these are the Dundee group of Ned Goodman.

Completion of the merger is subject to the usual due diligence process by both companies, which is expected to be completed within the next 30 days.

## **The Resource**

There have been various resource estimates on this deposit since its listing in Canada. After the Dundee interests ousted the management group it went through the usual "blame the outgoing management" routine and determined: "after a detailed review during the calendar year 2013 that it was urgent and necessary to reassess and de-risk the 2012 TetraTech Feasibility Study of the Sangdong Project". While we are no great fans of mining consulting firms, we found little to fault in the original FS as the Wesson's has applied a requirement that capex come in as low as possible with copious use of cheaper labour (imported from Fiji) and second-hand equipment.

Now while the Wesson group is never renowned for being as solicitous of GS&A as of capex, we felt this rewriting of history was just as excuse to mothball the project pending better financing markets and IMC getting their act together on whether they were supporting the project or not.

Woulfe commissioned AMC Consultants Pty Ltd. of Melbourne in August 2014 to undertake a Mineral Resource Update.

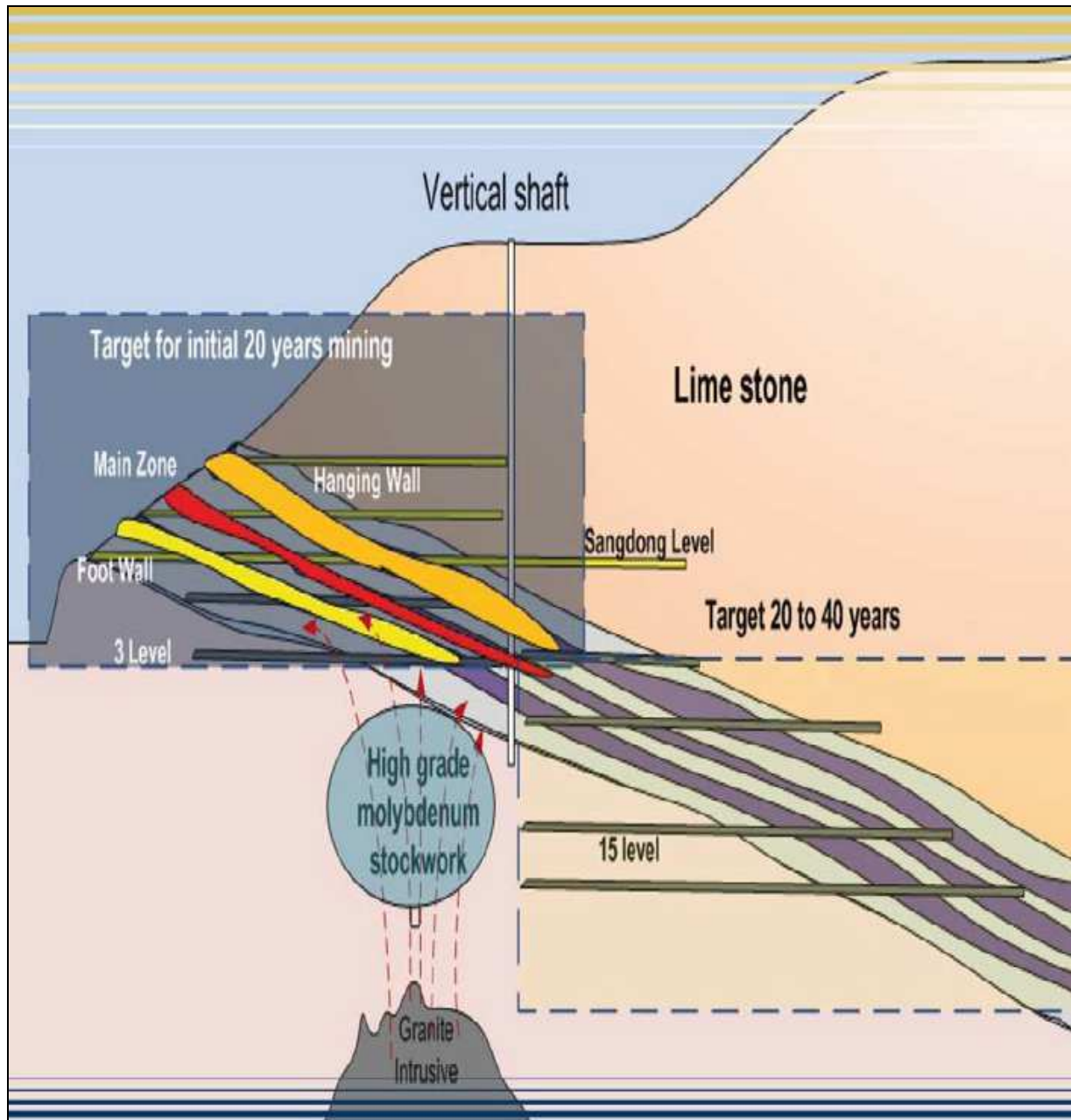
The following table, extracted from the AMC Report, shows the Mineral Resource and metal content for the Sangdong Property as of September 15, 2014. The cut-off grade of 0.4% WO3.

<b>Sangdong - NI43-101 Resource - Oct 2014</b>					
	<b>Zone</b>	<b>Tonnes</b>	<b>WO3</b>	<b>MoS2</b>	<b>Contained</b>
		<b>mn</b>	<b>%</b>	<b>%</b>	<b>WO3 metal</b>
					<b>Mn tonnes</b>
Measured	Main	0.55	0.61	0.066	0.33
	F2	0.86	0.56	0.057	0.48
	F3	0.74	0.55	0.057	0.41
Measured Total		<u>2.15</u>	<u>0.57</u>	<u>0.059</u>	<u>1.22</u>
Indicated	HW	0.19	0.46	0.095	0.09
	Main	0.31	0.62	0.031	0.19
	F2	0.58	0.55	0.029	0.32
	F3	0.57	0.53	0.026	0.31
Indicated Total		<u>1.66</u>	<u>0.55</u>	<u>0.036</u>	<u>0.91</u>
Measured + Indicated		<u>3.81</u>	<u>0.56</u>	<u>0.049</u>	<u>2.12</u>
Inferred	HW	7.93	0.68	0.089	5.38
	Main	0.34	0.74	0.047	0.26
	F2	0.93	0.53	0.073	0.49
	F3	0.76	0.48	0.047	0.37
	F4	1.31	0.52	0.053	0.69
Inferred Total		<u>11.28</u>	<u>0.64</u>	<u>0.08</u>	<u>7.18</u>

### **The Road to Production**

The scoping study on the Sangdong project was completed by Wardrop in March 2010. This signalled an NPV of US\$462 million at an APT price of US\$250 per mtu. The scoping study was to an accuracy of approximately 30% and confirmed the project's economics at that lower tungsten price. That was then followed up by the 2012 Feasibility Study to which we have already referred.

After the scoping study Woulfe's then management started moving forward aggressively with project construction plans. The crushing and grinding sections of the process plant were well advanced at the time we wrote our last major note on Woulfe in December 2012 and all necessary major equipment had been specified. In October 2011, the company took delivery of Metso minerals front end crushing equipment and the Terex feeding equipment which represented the first equipment delivery to the mine site. The equipment was purchased at a significant discount to value. In addition Woulfe had indicated it would be purchasing new European-made crushing and grinding equipment.



The crusher was designed for 2.4 million tonnes per annum and the initial milling capacity will be 1.2 million tonnes per annum, but can be readily expanded to 2.4 million tonnes. There are real indications that the tungsten markets will remain strong and that molybdenum prices may return to historical highs, which could justify an increase in production.

The flow sheet is conventional, with two-stage crushing followed by rod mill grinding and flotation, and tungsten concentrate further processed to produce APT.

In October 2011 the company received an explosives license, built an underground storage facility and initiated the first blast since closure in 1993. The F2 foot wall ore body was blasted. This zone will be the initial point of mining and representative of the initial years of operations. The mine has now been reopened from one level in the base of the valley floor to the top of the mountain and across the entire 1.2 km strike of the ore body. During the opening, many new target areas were discovered which were initially prepared by Korea Tungsten prior to the 1993 closure of the mine.

This level of advancement is exactly why Almonty is paying such a high price in dilution to get its hands on this project for while not exactly “plug n play” it is pretty near to being so, with a lot of the capex already having been expended at the time Dundee moved in to oust the Wesson’s shortly after our last review.

### **Mining**

The 2012 TetraTech Feasibility Study produced mineral resource estimates at a cut-off grade of 0.15% WO<sub>3</sub> based on the bulk mining approach that the Wessons decided to pursue. However, the AMC Report, uses a cut-off grade of 0.4% WO<sub>3</sub> based on a more selective mining approach being considered.

Under the new scheme, the first phase of development of the Sangdong Property will be focused between Level -1 to the Taebaek Level which are three immediately reachable levels above a further 15 levels to be de-watered progressively after start-up of operations, which represent reasonable prospects of eventual economic extraction in the current management’s view. The mine is anticipated to produce 450,000 tonnes of ore in Year 1 of production and reach the final 12 year life of mine capacity of 640,000 tonnes per year, in Year 2.

The main parameters of the proposed mining operation are:

- ✓ Life-of-mine (LOM) in Current Mine Plan of 12 years
- ✓ Time to Reach Mining Rate 2 years
- ✓ Probable Reserve of 13.3 million tonnes at a grade of 0.425 % WO<sub>3</sub>
- ✓ Recovery 81%
- ✓ Average Annual WO<sub>3</sub> Concentrate Production 3,828 to 4,705 tonnes
- ✓ Capex of US\$74.4 million compared to a previous projection of US\$151 million

As for the project economics, AMC estimated:

- ✓ Average annual revenue WO<sub>3</sub> concentrate of US\$62.1 million
- ✓ Earnings Before Sustaining Capital - Annual Average of US\$31.8 million
- ✓ Pre-tax IRR of 26%
- ✓ Project Total NPV @ 5% Discount Rate of US\$156 million

### **Bridge Loan**

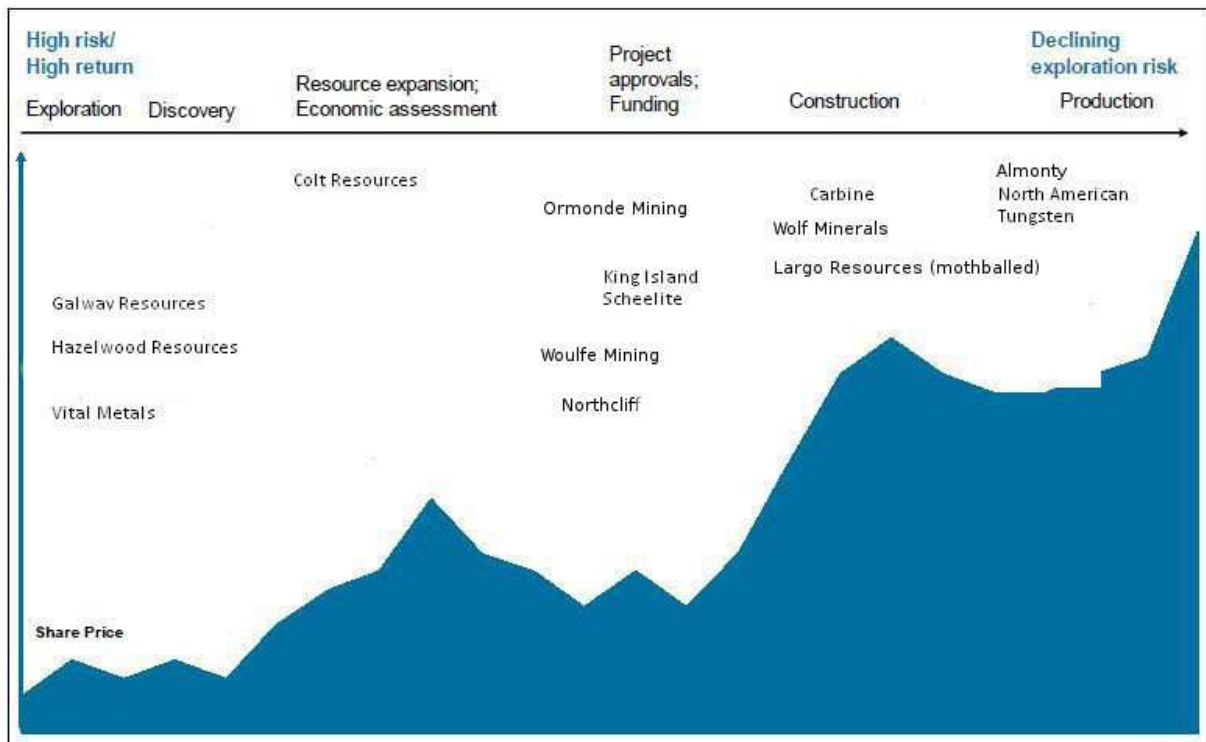
It is worth noting that Almonty provided Woulfe with a lifeline of a CAD\$150,000 unsecured bridge loan,

and up to a further CAD\$150,000 unsecured bridge loan will be made available upon the execution of the definitive agreement which will be used for basic working capital needs. The Bridge Loan will mature on the earlier of April 30, 2015 or closing of the merger, subject to extension with the agreement of Almonty, will bear an interest rate of 12% per annum payable at maturity and will rank *pari passu* with Dundee Corporation’s existing unsecured convertible debt of Woulfe.

**The Tungsten Lifecycle Chart**

Our all-purpose Lifecycle chart serves particularly well, in the case of Tungsten, to show the state of progress of the various players vis-à-vis each other on the exploration-production continuum (not that some players, irrespective of which metal, imagine themselves production-bound).

Almonty is shown at the far right side amongst the “alive and kicking” Tungsten plays. Woulfe is in the centre where it has been stuck, idling, for several years now.



**Risks**

The risks on the Sangdong purchase for Almonty are:

- Some sort of counterbid. This would need to come from a player outside the listed Tungsten players as none of the listed companies are in any condition to better Almonty as a merger partner
- Korea is an untried mining zone for foreign operators. Things have been good so far but one

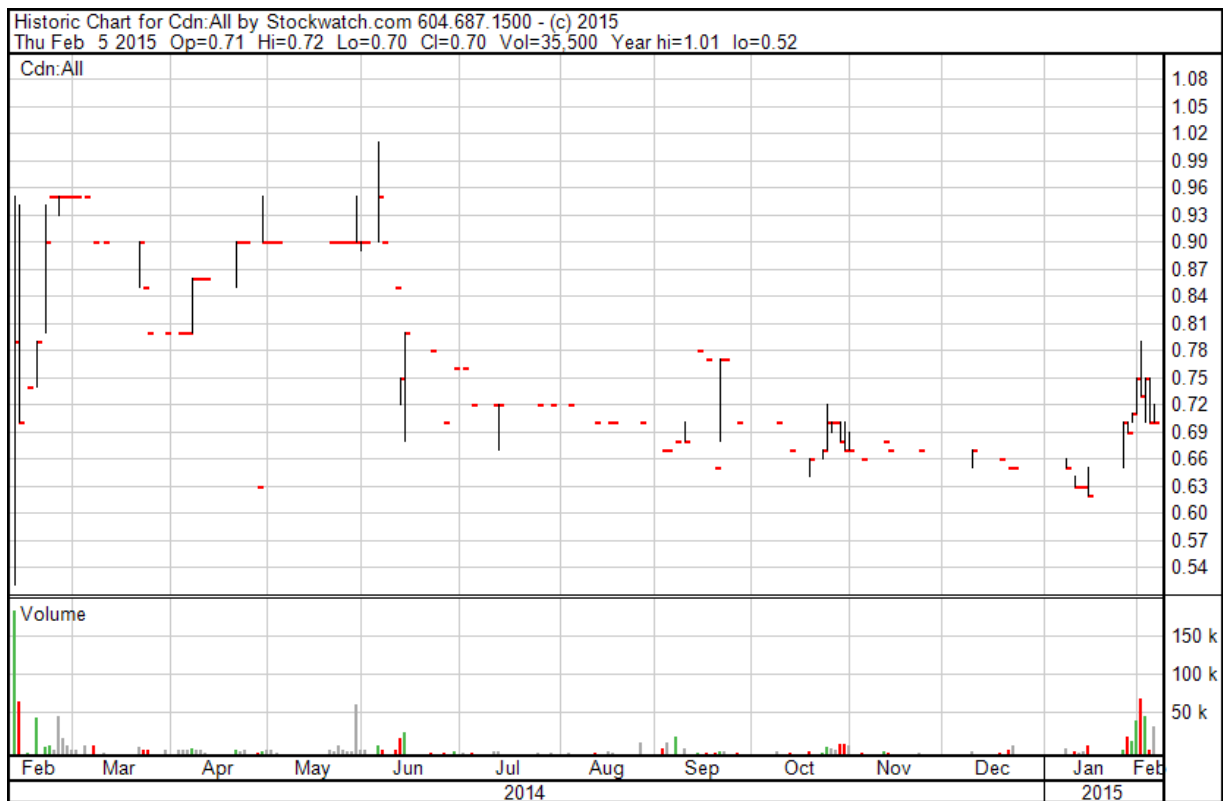


- never knows
- Sudden weakness in the Tungsten price could disadvantage the drive to production
- Technical issues may raise their head

### Conclusion

The long awaited consolidation is happening but alas it's only one company initiating the process. If the current deal plays out to plan then we would expect maybe one or two more mines to be rolled in, and we should not discount the possibility that Almonty will circle back to gets its teeth into Ormonde at some point.

Our strategy call on Almonty remains a Long stance with our target price for the next 12-months remaining at CAD\$1.32.



Monday, February 9, 2015



## 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. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Hallgarten's Equity Research rating system consists of LONG, SHORT and NEUTRAL recommendations. LONG suggests capital appreciation to our target price during the next twelve months, while SHORT suggests capital depreciation to our target price during the next twelve months. NEUTRAL denotes a stock that is not likely to provide outstanding performance in either direction during the next twelve months, or it is a stock that we do not wish to place a rating on at the present time. Information contained herein is based on sources that we believe to be reliable, but we do not guarantee their accuracy. Prices and opinions concerning the composition of market sectors included in this report reflect the judgments of this date and are subject to change without notice. This report is for information purposes only and is not intended as an offer to sell or as a solicitation to buy securities.

Hallgarten & Company or persons associated do not own securities of the securities described herein and may not make purchases or sales within one month, before or after, the publication of this report. Hallgarten policy does not permit any analyst to own shares in any company that he/she covers. Additional information is available upon request.

© 2015 Hallgarten & Company, LLC. All rights reserved.

Reprints of Hallgarten reports are prohibited without permission.

### Web access at:

Research: [www.hallgartenco.com](http://www.hallgartenco.com)

60 Madison Ave, 6th Floor, New York, NY, 10010