# Select Equities

**Institutional Research & Dealing**

# stock brief

RECOMMENDATION: BUYat 6.5 cents

Stock Code: WPG
Last Sale: 6.4 cents
Market Cap: $48.4m
Valuation 9 cents
Risk Level: High

# WPG Resources Ltd

Lower costs in 2H17 expected after disappointing 1H17

**13-Mar-17**

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**Risk Factors**

1. WPG's revenue/profit is mainly determined by gold prices and $A/$US rate
2. Underground mining at Challenger has previously had unexpected problems increasing costs
3. Metallurgy issues can happen but both mines looks well understood.
4. Current Reserves are only sufficient for a 3 to 4 year mine life but this ignores highly prospective undrilled areas.

**CHALLENGER GOLD MINE(100%WPG)**

- In Mar-16 WPG Resources Ltd (WPG) and the privately owned DMPL(the company related to the underground mining contractor Pybar) acquired the South Australian Challenger underground gold mine (730 kms north-west of Adelaide) as a 50/50 JV for $1m from listed Kingsgate Consolidated(KCN). Assets included a 600k tpa CIP operating plant, cash backed rehabilitation bonds of $2.6m and no residual employee/contractor liabilities.
- In May-16, the mine was restarted for about $4m with Pybar as contractor with WPG guidance of 50k oz for FY17.
- Challenger has operated since 2002 producing >1.1m oz of gold from two main lodes. In 2015 KCN wrote down the gold Resource estimate to 194k oz from the 2014 estimate of 635k oz due to mining difficulties and expectation that part of the resource would not be mined. Challenger currently has 277k oz in Measured and Indicated Resources including 83.4k oz in Reserves. The remodelling of various lodes, the Deeps and SSW discovery (about 300m from the Challenger West orebody)is highly likely to extend the current 3 year mine life plan.
- In July-16 WPG acquired DMPL's 50% interest for $9m and 25m unlisted 30-Sep-18 options with an 11 cent exercise price. This was funded by a $7.4m placement at 6.5 cents per share and a 1 for 6 rights issue raising $6.1m also at 6.5 cents.
- On 4-Oct-16, the dispute in the JV with Tyranna(TYX) for the exploration licences that surround the Challenger mine was resolved with WPG retaining 100% of the Challenger Deeps tenements EL 5661.In summary, the other gold tenements in the Western Gawler Craton remained at 34% WPG and 66% TYX. On 24-Jan-17,TYX announced a 219k oz. maiden resource estimate for the JV known as the Jumbuck Gold Project with more drilling planned for 2017 to achieve the target of 500k oz .Any developments would use the Challenger mill.
- On 12-Dec-16,WPG unexpectedly advised a 2k production downgrade for Challenger in 1H17 with the expected Dec qtr gold of 12,400 oz compared to the Sept qtr of 12,138oz due mainly to mine development issues. Pybar added a 3rd jumbo rig in mid Jan-17 to rectify the situation.

**TARCOOLA GOLD MINE(100%WPG)**

- In May 2014, WPG acquired the Tarcoola (100% interest) and the Tunkillia (70% interest) from Mungana Goldmines for a total of $1.5m cash and 7.5m WPG shares. In excess of $20m had been spent by other parties on exploration resource definition drilling, and permitting at these projects At that time, Mungana's 59% controlling shareholder, Kagara was in liquidation. The projects are 165/130km respectively south of the Challenger gold mine.
- In early Nov-16,the Tarcoola PEPR was approved and a $1.8m rehabilitation bond was lodged.The Ore Reserve estimate for Tarcoola is 710k tonnes of 3.1g/t containing 71k ounces of gold. Following capex of $5m(including the bond),the first ore was transported to the Challenger mill in mid Jan-17.The mine life for the open pit mine is expected to be 2 years and the treatment period at the Challenger mill 3.5 years to give 20k oz gold pa. There appears good exploration potential for the mine life to be extended by >12 months.

**TUNKILLIA DEPOSIT(100%WPG)**

- Tunkillia was discovered in 1997 and is a blind orebody with no prior production.
- On 26-Nov-14, WPG acquired the residual 30% interest owned by Helix Resources (HLX) to move to 100%.Key terms of the deal included WPG pay HLX $0.5m cash and 10m WPG shares, upon mine construction a further $0.5m cash plus 10m WPG shares and a 1% NSR.
- The resource estimate was recast in Feb-15 to 558k oz of 1.4gm gold and 1.5m oz of silver following WPG"s adoption of a higher cut-off grade.. The geology of the area is very similar to the nearby big deposits of Olympic Dam/Prominent Hill and Kalgoorlie W.A. Exploration will commence in the Mar-17 qtr. following the previous April-16 encouraging 10 hole RC program.

**MANAGEMENT**

- On 1-July-16, Cornel Parshotam was appointed Chief Operating Officer and is based in Adelaide. His 38 years of experience includes Head of Operations/GM at BHP's Olympic Dam.
- On 19-Dec-16, Managing Director Martin Jacobsen unexpectedly resigned due to ill-health.
- On 22-Dec-16, Wayne Rossiter (CFO since July-13) was appointed Chief Operating Officer His previous experience includes mining engineer roles and extensive overseas experience.
- Founder/Executive Chairman Bob Duffin has also reaffirmed this continuing role for the foreseeable future. WPG's Chief Geologist since 2004 remains Gary Jones (based in New Zealand) who is also one of the founding WPG directors and has 45 year's experience.
- On 1-Mar-17,Cornel Parshotam was appointed an alternate director to Gary Jones.

**1H17 RESULT SNAPSHOT (released 13-Mar-17)**

- Gold sales revenue from the Challenger mine for the 6 months to 31-Dec-16 was $41m (nil pcp).WPG held 100% of Challenger from 1-Aug-16 and attributable revenue was $37.7m with no revenue from the Tarcoola mine as processing ore started mid-Jan-17.
- Gold production for the half was 24,567 ounces (in line with guidance) from the treatment of 309,305 tonnes of ore including 78k of low grade stockpiles with average recovery rate of 94.7%.The guidance of 12-Dec-16 indicated lower than planned development rates at Challenger resulting in very high All-In-Sustaining Costs(ASIC) of $A1,550 per oz recovered with the average gold price received $A1,689 per oz. The grade processed was a low 2.61 g/t  due to increased tonnage of low grade material treated. The WPG quarterly cashflow and activities reports released 31-Jan-17 contained most of this information.
- EBITDA for the half was $0.6m with depreciation and amortisation of $4.7m resulting in a loss of $4.1m (pcp loss of $1.1m).Cashflow from operating activities was $7.5m(pcp negative $1m).Equity raised was $16m with payments of $9.6m for the 50% of Challenger from DMPL,$2.9m on mine development at Challenger,$2m on pre-stripping of waste at Tarcoola,$1.1m on exploration,$3.1m on fixed plant and equipment totalling $18.4m for the half. Cash as at 31-Dec-16 was $9.7m (pcp $4.6m).
- Directors comment that near mine exploration at Challenger has indicated that the CSSW structure plunges in parallel with the main Challenger ore lodes. Drilling in the M3 structure has yielded highly encouraging results and mining activities in this new area, not currently included in the resource and reserve estimate, is anticipated to commence prior to 30-Jun-17.Systematic drilling of the other lodes will be used to plan initial mining in the “Challenger Deeps”.The near mine exploration at Tarcoola will include a larger soil sampling program and a small Reverse Circulation drilling program in 2H17.
- Directors comment that an advanced data analysis of historic drilling at Tunkillia in 2H17 will be analysed with 3D software with the aim of defining the structure of the gold hosting quartz lodes to generate higher grade gold target zones beneath the already defined mineralisation.
- Directors comment that the dispute with Tyranna Resources over the Western Gawler Craton JV was resolved during the half with WPG now holding an approx. 28% interest. The new agreement allows WPG to continue development of the Challenger lodes in Challenger Deeps as 100% owner of this area.

**FY17 GUIDANCE**

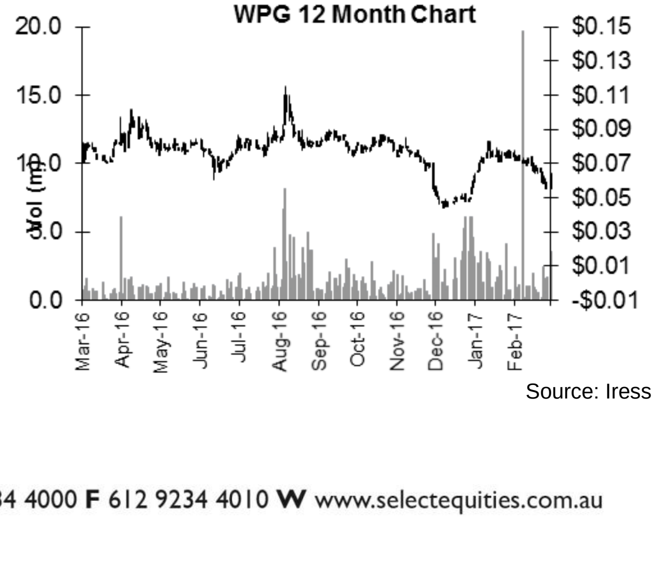
- Updated guidance for the combined Challenger and Tarcoola mining operations for FY17 is in the range of 52k to 56k.Directors expect unit costs of production will fall as ounces produced increases due to the large proportion of fixed costs at Challenger and the ASIC is expected to fall in 2H17.Studies of production capacity at the Challenger treatment plant also indicate that an increase from the current 600k tpa to 700k tpa  is possible with no material loss of gold recovery and without further capex. The potential to increase to 800k tpa with some limited capex is also being examined.

**PROFIT FORECAST/VALUATION**

- The current gold price of US$1207 per oz and $A/$US of 75.65 cents translates into a 32% higher Australian price of $A1596 per oz. In 2H17, assuming production of 6.5k oz from Tarcoola and 25k oz from the Challenger operations and  an ASIC of $1300 per oz gives a pre-tax profit of $6.2m in 2H17.A FY17e net profit of $2.1m with no tax payable is achievable.
- In FY18, production of 20koz  from Tarcoola and 60koz from Challenger from 700k of ore, a US$1225 gold price with a $A/$ US of 75c and an ASIC of $A1200 per oz then with no tax a net profit of $19.7m is possible.
-  Using assumptions for the 3 years to FY20 of a US$1225 gold price, $A/$US of 75 cents, production of 80k oz pa, ASIC of $A1200 per oz and a discount rate of 10%,no tax in FY18 gives a valuation of 9 cents per share. No value is included for Tunkillia/Tyranna JV and using $11/oz in resource gives >$7m or 1 cent per share.
- WPG profit/valuation is very sensitive to movements in the gold price with WPG getting $A1733 oz in Jun-16.A $US100 increase adds nearly 3 cents to the valuation. A 5 year mine life also adds 4 cents to the valuation.

| June Year End | FY16A | 1H17A | FY17E | FY18E |
|---|---|---|---|---|
| Production (oz) | 3.4 | 24.6 | 56.1 | 80.0 |
| Cash Costs-ASIC(A$/oz | 3195.0 | 1550.0 | 1400.0 | 1200.0 |
| Total Revenue($m) | 17 | 37.7 | 88.2 | 130.8 |
| EBITDA ($m) | -8.3 | 0.6 | 12.1 | 29.8 |
| Net Profit ($m) | -8.3 | -4.1 | 2.1 | 19.7 |
| EPS (¢) | -2.3 | -0.6 | 0.3 | 2.6 |
| DPS (¢) | 0.0 | 0.0 | 0.0 | 0.0 |
| PER (x) | -2.8 | -11.6 | 23.3 | 2.5 |
| Ent. Value/EBITDA (x) | -4.6 | 65.9 | 3.2 | 13 |
| Yield (%) | 0.0% | 0.0% | 0.0% | 0.0% |
| # Shares (m) | | | | 756.0 |
| Avg. Mthly Volume (m) | | | | 32.3 |
| Market Cap ($m) | | | | 48.4 |
| Cash 1H17A ($m) | | | | 9.7 |
| Enterprise Value ($m) | | | | 38.7 |

Source: Company Reports and Select Equities Research




Source: Iress

# WPG Resources Ltd

Select Equities Research
Small Caps

| Code | | WPG |
|---|---|---|
| Last sale ($) | 13-Mar-17 | 0.064 |
| # shares (m) | | 756.0 |
| # options (m)-unlisted 30-9-18 (11c to pay) | | 37.5 |
| # incentive rights | | 21.9 |
| Mkt cap ($m) | | 48.4 |
| Cash 1H17A | | 9.7 |
| Enterprise Value | | 38.7 |

| June Year End | FY16A | 1H17A | FY17E | FY18E |
|---|---|---|---|---|
| **Financial Perfomance($m)** | | | | |
| Gold Sales | 15 | 37.6 | 88.1 | 130.7 |
| Other Income | 0.2 | 0.1 | 0.1 | 0.2 |
| Total Revenue | 17 | 37.7 | 88.2 | 130.8 |
| Operating Costs | -3.6 | -35.2 | -72.1 | -95.0 |
| Royalty | 0.0 | 0.0 | 0.0 | 0.0 |
| Exploration write-off | -2.4 | 0.0 | 0.0 | 0.0 |
| Corporate/other | -3.9 | -1.9 | -4.0 | -6.0 |
| EBITDA | -8.3 | 0.6 | 12.1 | 29.8 |
| D&A | 0.0 | 4.7 | 10.0 | 10.0 |
| EBIT | -8.3 | -4.1 | 2.1 | 19.8 |
| Net Interest | -0.1 | 0.0 | -0.1 | -0.1 |
| Abnormals | 0.0 | 0.0 | 0.0 | 0.0 |
| PBT | -8.3 | -4.1 | 2.1 | 19.7 |
| Tax Expense | 0.0 | 0.0 | 0.0 | 0.0 |
| NPAT | -8.3 | -4.1 | 2.1 | 19.7 |
| EPS(¢) | -2.3 | -0.6 | 0.3 | 2.6 |
| EPS(¢) adj | -2.3 | -0.6 | 0.3 | 2.6 |
| DPS (¢) | 0.0 | 0.0 | 0.0 | 0.0 |
| NTA (¢) | 0.0 | 2.1 | 2.2 | 3.9 |
| Book Value / Share (¢) | 1.8 | 2.6 | 2.7 | 4.4 |
| **Valuation/Performance Ratios** | | | | |
| PER (x) | -2.8 | -11.6 | 23.3 | 2.5 |
| PER (adj) | -2.8 | -11.6 | 23.3 | 2.5 |
| Ent. Value/EBITDA (x) | -4.6 | 65.9 | 3.2 | 1.3 |
| Revenue Growth (%) | n/a | n/a | n/a | 48.3% |
| EBITDA Growth | n/a | n/a | n/a | 145.6% |
| NPAT Growth | n/a | n/a | n/a | 848.4% |
| P/NTA (x) | n/a | n/a | 2.9 | 1.6 |
| P/BV | 3.6 | 2.5 | 2.4 | 1.5 |
| Yield (%) | 0% | 0% | 0% | 0% |
| Franking | 0% | 0% | 0% | 0% |
| Payout Ratio | 0% | 0% | 0% | 0% |
| EBITDA/Total Revenue | n/a | 1.6% | 13.8% | 22.8% |
| NPAT/Total Revenue | n/a | -11.0% | 2.4% | 15.1% |
| Current Ratio (x) | n/a | 1.1 | 1.1 | 1.1 |
| Interest Cover (x) | n/a | n/a | -33.5 | -165.2 |
| Net Debt/Equity (%) | 0.0% | -50.3% | -53.4% | -71.6% |
| ROE (%) | -129.9% | -21.5% | 10.3% | 59.4% |
| ROA | -45.8% | -9.1% | 4.5% | 33.2% |

| Interim Results ($m) | 1H16A | 2H16A | 1H17A | 2H17E |
|---|---|---|---|---|
| Gold Sales | 0.0 | 15 | 37.6 | 50.5 |
| Other Income | 0.0 | 0.2 | 0.0 | 0.1 |
| Total Revenue | 0.0 | 17 | 37.7 | 50.5 |
| Operating Costs | 0.0 | -3.6 | -35.2 | -36.9 |
| Royalty | 0.0 | 0.0 | 0.0 | 0.0 |
| Exploration write-off | -0.3 | -2.1 | 0.0 | 0.0 |
| Corporate/other | -0.8 | -3.1 | -1.9 | -2.1 |
| EBITDA | -1.1 | -7.2 | 0.6 | 11.6 |
| D&A | 0.0 | 0.0 | 4.7 | 5.3 |
| EBIT | -1.1 | -7.3 | -4.1 | 6.3 |
| Net Interest | 0.0 | -0.1 | 0.0 | -0.1 |
| Abnormals | 0.0 | 0.0 | 0.0 | 0.0 |
| PBT | -1.1 | -7.2 | -4.1 | 6.2 |
| Tax Expense | 0.0 | 0.0 | 0.0 | 0.0 |
| NPAT | -1.1 | -7.2 | -4.1 | 6.2 |

| June Year End | FY16A | 1H17A | FY17E | FY18E |
|---|---|---|---|---|
| **Financial Position ($m)** | | | | |
| Cash | 4.6 | 9.7 | 10.8 | 23.7 |
| Trade Debtors | 1.2 | 3.5 | 3.5 | 3.5 |
| Inventory | 3.2 | 5.6 | 5.6 | 5.6 |
| Investments | 0.0 | 7.2 | 7.2 | 7.2 |
| Prop.,Plant&Equip. (net) | 0.4 | 13.5 | 13.5 | 13.5 |
| Intangibles | 6.2 | 3.5 | 3.5 | 3.5 |
| Other | 2.5 | 2.4 | 2.4 | 2.4 |
| Total Assets | 18.2 | 45.5 | 46.4 | 59.4 |
| Trade Creditors | 5.5 | 16.2 | 16.2 | 16.2 |
| Debt | 0.0 | 0.0 | 0.0 | 0.0 |
| Provisions | 6.4 | 10.0 | 10.0 | 10.0 |
| Other | 0.0 | 0.0 | 0.0 | 0.0 |
| Total Liabilities | 11.8 | 26.2 | 26.2 | 26.2 |
| Net Assets | 6.4 | 19.3 | 20.2 | 33.1 |
| Issued Capital | 31.3 | 47.8 | 47.8 | 47.8 |
| Accum Losses/Reserves | -25.0 | -28.5 | -22.9 | -3.2 |
| Total Equity | 6.4 | 19.3 | 20.2 | 33.1 |
| **Cash Flows ($m)** | | | | |
| Net Receipts | -1.5 | 7.5 | 12.1 | 29.8 |
| Net Interest | 0.1 | 0.0 | 0.1 | 0.1 |
| Tax Paid | 0.0 | 0.0 | 0.0 | 0.0 |
| R&D Grants | 0.3 | 0.0 | 0.0 | 0.0 |
| Operating Cash Flow | -1.2 | 7.5 | 12.2 | 29.9 |
| Capex & Acquisitions | 0.0 | -17.3 | -20.0 | -12.0 |
| Asset Sales & Divest | 0.7 | 0.0 | 0.0 | 0.0 |
| Mine Exploration/Develop | -1.7 | -1.1 | -2.0 | -5.0 |
| Investing Cash Flow | -1.1 | -18.4 | -22.0 | -17.0 |
| Change in Equity (net) | 5.7 | 16.0 | 16.0 | 0.0 |
| Change in Debt (net) | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividends | 0.0 | 0.0 | 0.0 | 0.0 |
| Other | -0.2 | 0.0 | 0.0 | 0.0 |
| Financing Cash Flow | 5.6 | 16.0 | 16.0 | 0.0 |
| Net Inc/Dec Cash | -3.3 | 5.1 | 6.2 | 12.9 |
| Cash at Yr End | 4.6 | 9.7 | 10.8 | 23.7 |
| **Gold Production** | **FY16A** | **1H17A** | **FY17E** | **FY18E** |
| Challenger (koz) | 3.4 | 24.6 | 49.6 | 60.0 |
| Tarcoola (koz) | 0.0 | 0.0 | 6.5 | 20.0 |
| Total Production (koz) | 3.4 | 24.6 | 56.1 | 80.0 |
| Cash Costs-ASIC (A$/oz | 3195 | 1550 | 1400 | 1200 |
| Grade Processed g/t au | 1.8 | 2.6 | 2.8 | 3.0 |
| Price Received (A$/oz) | 1733 | 1689 | 1620 | 1633 |
| **Price Assumptions** | **FY16A** | **1H17A** | **FY17E** | **FY18E** |
| Exchange Rate (A$/US$) | 0.75 | 0.75 | 0.75 | 0.75 |
| Gold ($US/oz) | 1300 | 1267 | 1225 | 1225 |
| Gold ($A/oz) | 1733 | 1689 | 1633 | 1633 |

| Valuation * | $m | cps |
|---|---|---|
| DCF @ 10% Discount Rate | 69.8 | 9.0 |
| DCF @ 15% Discount Rate | 64.4 | 8.3 |

*Based on 3 years production of 80koz pa +$US1225 gold price for FY17
ASIC per oz $A1200 +US$/$A 0.75.No value for Tunkillia/Tyranna JV.

| Mineral Resource Gold | 000/t | g/t | oz |
|---|---|---|---|
| Challenger* | 945.0 | 9.11 | 277.0 |
| Tarcoola** | 973.0 | 3.12 | 97.5 |
| Tunkillia*** | 12320 | 1.41 | 558.0 |
| **Ore Resource Gold** | **mt** | **g/t** | **oz** |
| Challenger* | 558.0 | 4.65 | 83.4 |
| Tarcoola** | 710.0 | 3.10 | 71.0 |

*completed 30 June 2016 ** completed 29 August 2016
***completed 4 February 2015

| Major Shareholders | No of FPO (m) | % |
|---|---|---|
| Bob Duffin | 57.8 | 7.6% |
| Jalinsons | 38.2 | 5.1% |
| Commonwealth Bank | 29.0 | 3.8% |

The top 20 shareholders hold 41.7% as at 17/10/16

Source: Company Reports and Select Equities Research

# Select Equities Directory

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