CNMC Goldmine Holdings Limited

Sitting on a gold mine

SINGAPORE | MINING | INITIATION

- Abundant resources and reserves at Sokor field with extracted gold grade higher than cut-off grade.
- Current minimum ore processing capacity is expected to be ramped up in the upcoming future, from the current 1.2mn tonnes per annum.
- All-in sustaining cost and All-in cost trended down over the past 5 years and are currently maintained at around US$500/oz.
- Other resources such as Silver, Lead, and Zinc have yet to be explored, thus the value of these resources are not priced in yet.
- The acquisition of Pulai Project is awaiting to be sealed and expected to create positive synergies.
- We initiate coverage on CNMC with a **Buy** rating and a DCF-derived target price of **S$1.03** using a cost of equity of 9.8%. Together with an estimated dividend of SG cents 1.4 for FY16, implied upside is **102.6%**.

Investment Thesis

- The imbalance between supply and demand in the physical gold market is not the main driver of gold price.
- Exponential increase in global monetary supply due to several rounds of quantitative easing inflated asset prices, including gold.
- Gold, a safe haven asset, performed well during recessions; we see signs of an impending recession from recent slowing US economic data.

Investment Actions

We initiate coverage on CNMC with a **Buy** rating and a DCF-derived target price of **S$1.03,** using a cost of equity of 9.8%. Together with an estimated dividend of SG cents 1.4 for FY16, implied upside is **102.6%**.

15 September 2016

Buy (Initiation)

CLOSING PRICE	SGD 0.515
FORECAST DIV	SGD 0.014
TARGET PRICE	SGD 1.030
TOTAL RETURN	102.6%

COMPANY DATA

O/S SHARES (MN) :	883
MARKET CAP (USD mn / SGD mn) :	619 / 892
52 - WK HI/LO (SGD) :	1.1 / 0.97
3M Average Daily T/O (mn) :	1.16

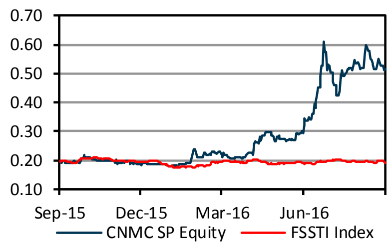
MAJOR SHAREHOLDERS (%)

INNOVATION CHINA LIMITED	26.3%
MESSIAH LIMITED	13.0%
NG ENG TIONG	11.9%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	0.0	(2.9)	8.1
STI RETURN	(4.6)	(9.2)	(16.5)

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY15	FY16e	FY17e	FY18e
Revenue (USD mn)	36.5	44.5	49.5	55.8
EBIT (USD mn)	14.8	14.0	21.5	24.6
Net Profit (USD mn)	10.7	16.6	19.2	22.7
P/E (x)	5.1	18.7	16.1	13.6
P/B (x)	1.6	6.2	4.5	3.4
EV/EBITDA (x)	2.1	10.7	8.8	6.9
Dividend Yield (%)	3.6	1.3	1.6	1.8

Source: Company Data, PSR est.

VALUATION METHOD

DCF (Cost of Equity: 9.8%; Terminal g: 0.0%)

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Company Background

- Commenced operation in 2007, CNMC is the first gold miner listed on Catalist board in SGX in 2011.
- The group is engaged in gold production and related businesses such as exploration, mining, and the processing of ore into gold dores.
- Currently, the group is focused on the flagship project, Sokor Gold Field Project, which is located in the State of Kelantan in Malaysia. Covering an area of $10km^2$, Sokor is estimated to contain 618,000 ounces of JORC-compliant gold resources, including mined ore reserves, as of Dec-2015. The field is comprised of four identified areas, namely, Manson's Lode, New Discovery, Sg. Ketubong, and Rixen.
- As of Dec-2015, total measured, indicated and inferred gold mineral resources for the Sokor Gold Project were 13.83mn tonnes at 1.39g/t gold with contained gold of 618,000 ounces (2014: 10.81mn tonnes at 1.5g/t gold with contained gold of 506,000 ounces).

  In Jun-2016, the group signed a non-binding letter of intent with Pulai Mining Sdn Bhd to acquire a 51% stake. Pulai mining is a brownfield with 11 licenses covering roughly $38.4km^2$ to explore and mine for gold, iron ore, and feldspar.

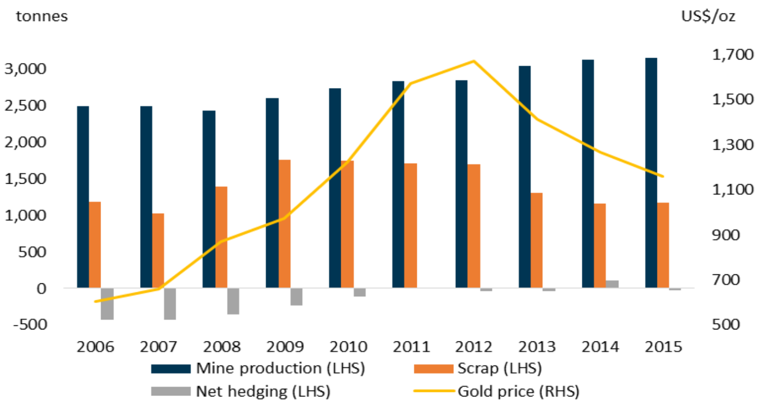
Investment Thesis

1. Overview on supply and demand of the gold market

Eye on the gold value chain, there are mainly five gold supply channels, namely, mine production, artisanal production, recycled gold, official sector sales, and net producer hedging. Mine production dominates the majority of supply and sees relatively lower volatilities in numbers yearly, while the latter three channels are subject to the macroeconomic environment, resulting in volatile supply.

According to the GFMS Gold Survey 2016, referring to Figure 1, the supply from mine production has been trending up over the past decade, from 2,497 tonnes in 2006 to 3,158 tonnes in 2015. Scrap supply (artisanal production and recycled gold), the second largest contribution, was relatively price-sensitive, tracking the rise and fall of the gold price, since the scrap holders selectively and speculatively monetised gold in hand during the upswing period and were deterred to sell when gold price was under downward pressure. Likewise, net producer hedging, which is the change in the physical market impact of mining companies' gold loans, forwards and options positions, moved inversely with market price and expectation. In the gold bull market, gold miners leveraged financial instruments to defer deliveries at a higher price, while in the bear market, they locked in the selling price in order to avoid further downfall.

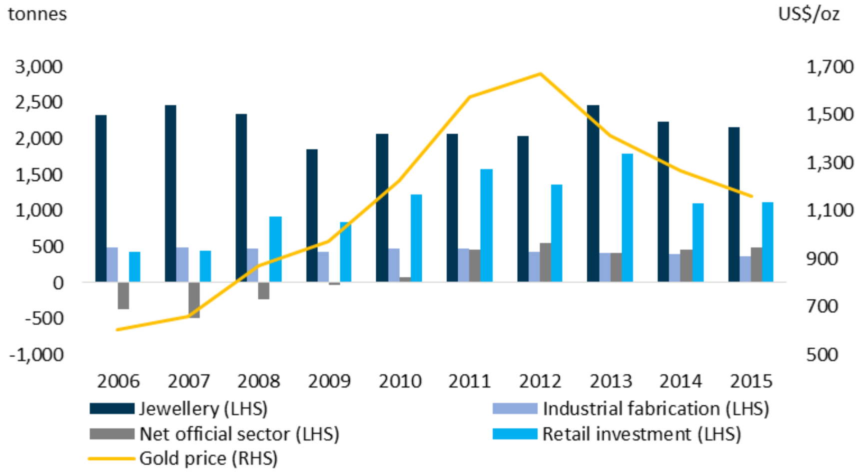
Figure 1. World gold supply breakdown



Source: GFMS, Thomson Reuters, PSR

As for the demand drivers for gold, demand generators can be classified into 4 broad categories - jewellery, investment, official sector, and industrials. Over the last decade, demand derived from jewellery-making and investment purposes ranked as the top two, which were influenced by the market sentiment towards gold price. However, the amount of industrial demand was on an apparent downtrend, with the drop from 482 tonnes in 2006 to 361 tonnes in 2015, due to the development of substitute materials. Lastly, since the 2008 global financial crisis turmoil, the official sector, especially central banks and major financial institutions, started increasing their gold reserves, reversing a previous trend, partly due to the authorities' weakening faith in the fragile currency markets. Rising regional conflicts worldwide also lifted the demand for gold in treasury vaults. After all, gold has been recognised as the perfect risk avoidance asset amongst all.

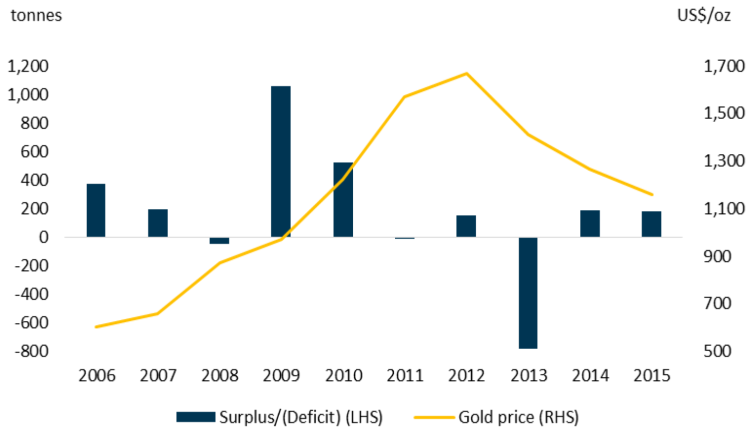
Figure 2. World gold demand breakdown



Source: GFMS, Thomson Reuters, PSR

As shown in Figure 3, global gold supply and demand balances were shifting between surpluses and deficits over the past decade. Here we need to indicate that gold price is not mainly driven by the imbalance between supply and demand, but is more driven by monetary supply (we elaborate on this in the following paragraphs). Fluctuations in gold price in turn drive demand and supply dynamics. When gold price is riding on the tailwind, producers are inclined to expand production to capture the higher margin, while investors and consumers will take advantage of lower gold prices when gold prices move down, thereby boosting demand.

Figure 3. World physical gold supply and demand

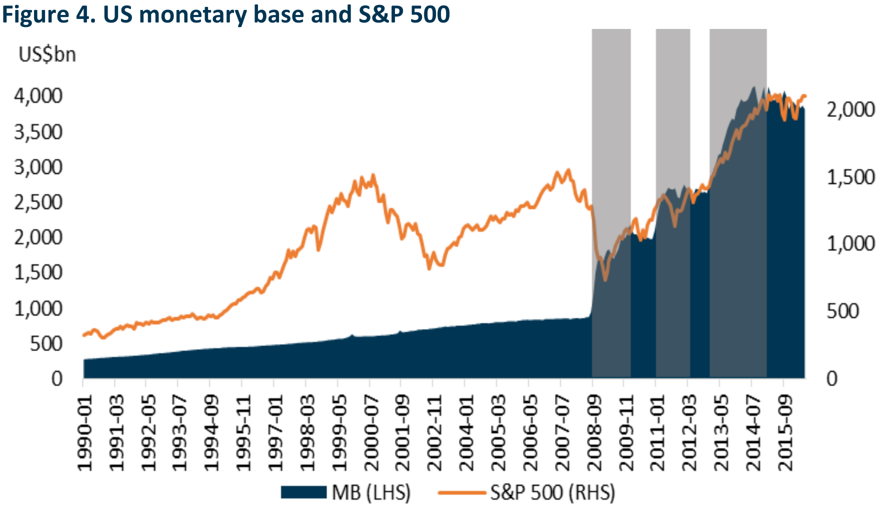


Source: GFMS, Thomson Reuters, PSR

2. Main driver of gold price: Money supply

US started to launch the quantitative easing (QE) program in order to deal with liquidity crunch during the subprime crisis in 2008. A total three rounds of QE lasted for seven years, initiated in 4Q08 and ended in 4Q14. Referring to Figure 4, the three rounds of QE (highlighted in grey) distorted the normalised growth of monetary base over the past decades. As a result, asset prices were inflated exponentially. For instance, US equity market reached a new high in early 2013 right after the 3rd round of QE was announced. With the continuation of QE, S&P 500 index skyrocketed and reached the all-time high of 2,193 in Aug-16. The flooded monetary base tremendously boosted liquidity which drove equity prices up.

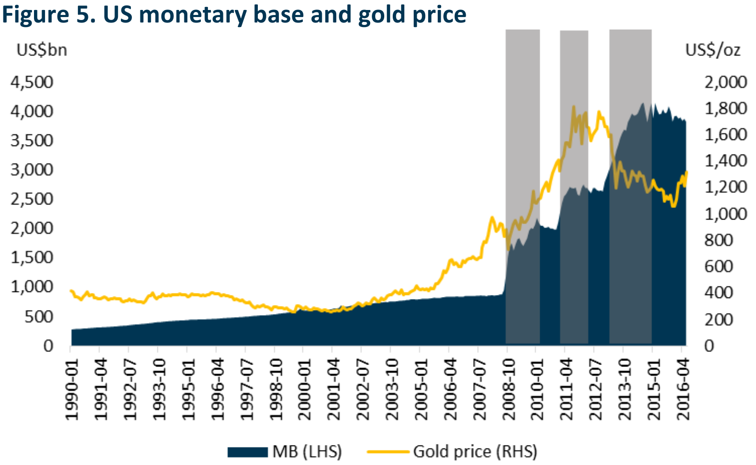
Figure 4. US monetary base and S&P 500



Source: Bloomberg, PSR

Referring to Figure 5, the gold bull market began in 2005 and ended in 2012. Subject to dire sentiment widely spreading during the subprime crisis, those gold positions were inevitably liquidated. However, gold rallied swiftly right after the 1st round of QE was announced, since the market pursued less risky assets, among which gold is viewed as a traditional safe haven. Benefiting from the 2nd round of QE, the unstoppable inflows of capital pulled up gold prices to the all-time high level of US$1,920/oz. The paradox was triggered in 2012 because gold markets turned the other way round when more capital was pumped into the market during the 3rd round of QE. One of the reasons could be investors shifted capitals to equity and bond markets to pursue higher yields. Therefore, the gold price was supressed.

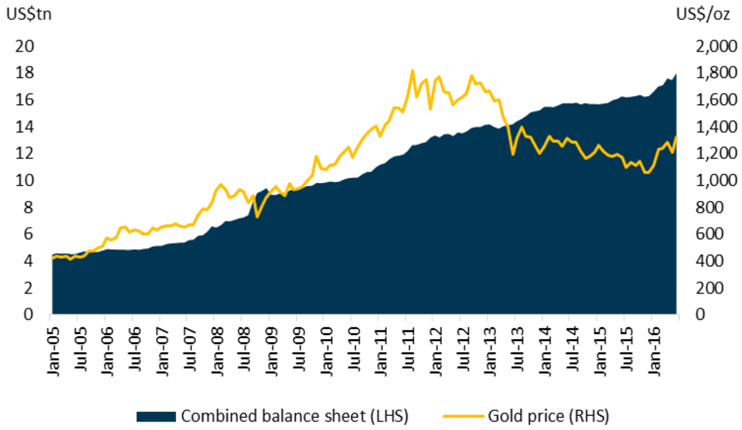
Figure 5. US monetary base and gold price



Source: Bloomberg, PSR

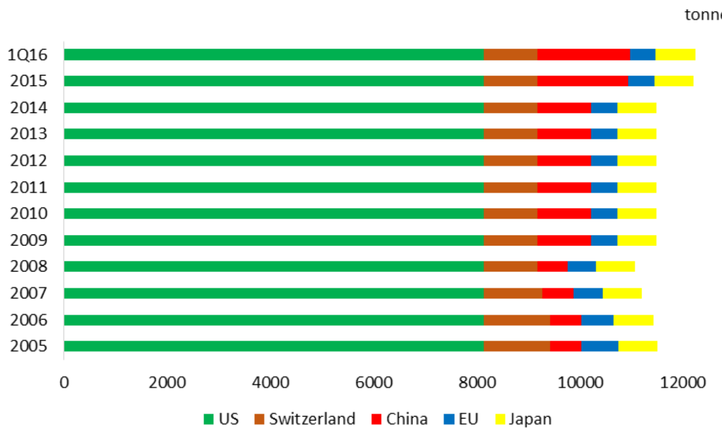
Central banks are responsible for controlling the money supply, thus the expansion or contraction of their balance sheets can be viewed as the proxy for the direction of money supply. When the supply of fiat currencies outpaces the stock of gold bullion, gold prices will rise and vice versa. Referring to Figure 6, the combined balance sheet of major central banks, namely Federal Reserve (Fed), People Bank of China (PBOC), Bank of Japan (BOJ), European Central Bank (ECB), and Swiss National Bank (SNB), indicates the universal expansionary monetary policy. Correspondingly, gold price has aligned with the increment of money supply until the price correction occurred in 2012. Though, according to World Gold Council (WGC), the total official gold reserves of those central banks mentioned above were increased in recent years, referring to Figure 7, the tonnage growth substantially fell behind the growth of money supply. Therefore, we do believe that gold price has overly corrected and will have more potential room to grow.

Figure 6. Combined balance sheet (Fed, PBOC, BOJ, ECB, SNB) and gold price



Source: Bloomberg, PSR

Figure 7. Official gold holdings



Source: WGC, PSR

3. Gold performed well in recessions

Gold has been treated as a safe haven asset, especially during times of recessions or crises. The reason behind this pattern where investors increasingly pursue gold during such periods of economic turmoil is the anticipation of monetary and fiscal stimulus, which immensely expands the monetary base. Accordingly, gold, which is priced by paper money, becomes more valuable. Referring to Figure 8, the average return of gold over the past 6 recessions (highlighted in red) is 22.2%, and gold generated positive returns in each period.

Figure 8. Gold price during recession periods

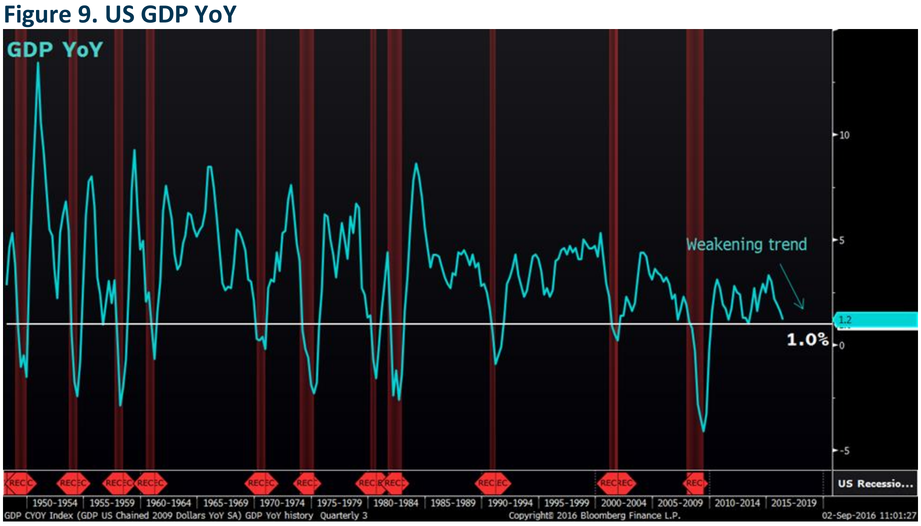
Period	Price_beg (US$/oz)	Price_end (US$/oz)	Return (%)
11/73 - 03/75	95	178	87.8%
01/80 - 07/80	512	614	19.9%
07/81 - 11/82	426	436	2.3%
07/90 - 03/91	352	357	1.4%
03/01 - 11/01	267	275	2.9%
12/07 - 06/09	783	930	18.8%
Average			**22.2%**

Source: Bloomberg, PSR

Is the next recession coming soon? We need to take a look at several economic barometers to judge. Here we trace US GDP growth and unemployment rate back to 1940s and track industrial production rate even further down back to 1920s.

Figure 9 shows that when US GDP YoY growth fell below 1%, the economy was either underwhelmed in a recession or stepping into a recession. US GDP growth had decelerated since 2015 and reported at 1.2% for 2Q16. A recession could be approaching us now when the growth rate is approximating to 1%, the alert line.

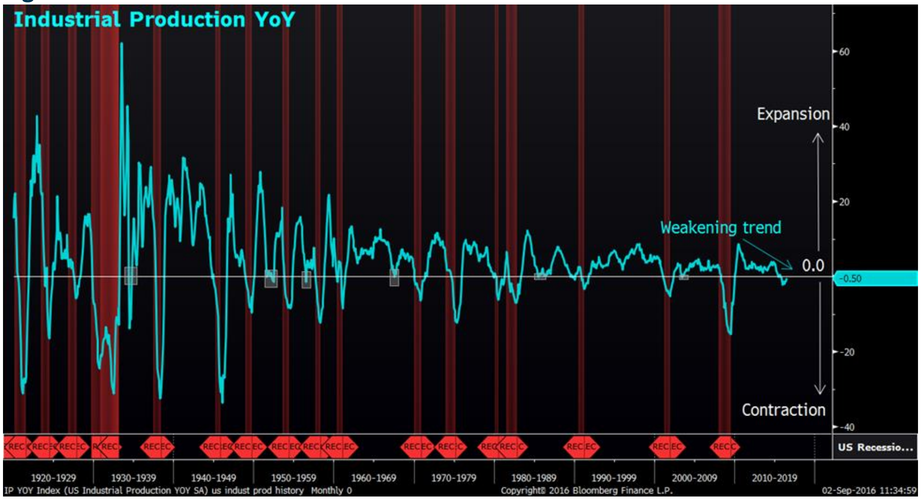
Figure 9. US GDP YoY



Source: Bloomberg, PSR

At the manufacturing side, shown in Figure 10, there were 23 periods of contraction and 6 failed (July 1934, April 1952, July 1956, July 1967, July 1985, June 2003) to bode a recession shown by the highlighted box, implying an accuracy rate of 73%. The failed signal showed that the duration of contraction lasted less than 4 months. However, the current downtrend of industrial production has been lasting for 11 months, implying US economy is heading towards a recession.

Figure 10. Industrial Production YoY



Source: Bloomberg, PSR

Another indicator is the unemployment rate turning point, referring to Figure 11. When the Unemployment Rate ticked up above the 12-month moving average and formed a bottom, the US Economy tended to enter into a period of recession. 10 out of 14 instances have been proved to signal a recession successfully with 71% implied accuracy. The unemployment rate increased from 4.7% in May-16 to 4.9% in Aug-16, and is only 0.1% away from the current 12-month moving average of 5%. Again, this strengthens our expectation of the arrival of a recession.

Figure 11. US Unemployment Rate

Source: Bloomberg, PSR

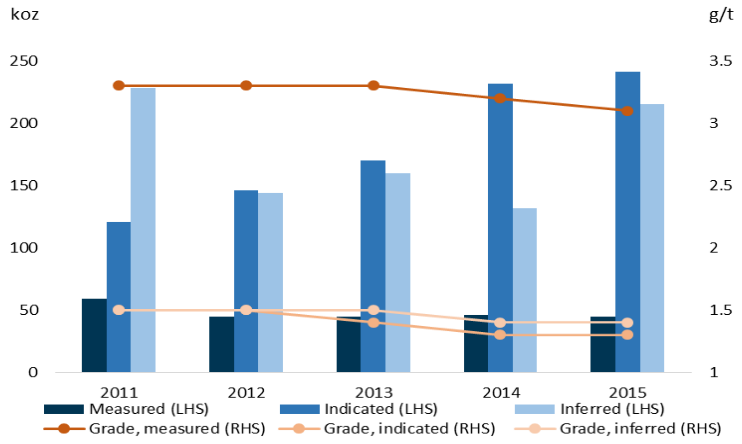
In a nutshell, throughout history, there have been several predictable repeating patterns when we analyse the economy, though we are aware that historical patterns may not neccesarily give a good forecast of the future. What we discussed above convinced us that there is a higher probablility of an impending recession, and gold will soon show its investment value when recession and market fears set in.

Investment Merits

1. Sokor project has had abundant resources and reserves to explore so far.

CNMC has been hiring Optiro Pty Ltd (Optiro), the independent advisory services firm, to provide mineral resource estimates. Referring to Figure 12, we summarised the historical levels of mineral resources of Sokor project over the past 5 years. The total gross amount of measured and indicated gold, which could be converted to a probable ore reserve, according to the guidelines of the JORC Code (2012), has been trending up due to the incremental amounts of indicated gold and the flattish amount of measured gold. Meanwhile during the period, the respective gold grade of measured, indicated, and inferred gold dipped 0.2g/t, 0.2g/t, and 0.1g/t, but we think the mild declines would not impact the business significantly, as the cut-off grade (lowest grade to be considered of economic value) is much lower than the current level, shown in Table 1 to 3.

Figure 12. Gross contained gold to CNMC and gold grade



Source: Company, PSR

Since there was no activity related to the Ketubong deposit over the past 4 years, no ore reserve estimate was reported for it. The gross amounts of ore reserves and mineral resources of Manson's Lode, New Discovery, and Rixen pits attributable to CNMC have been increasing amidst a declining rating of the gold grade. However, compared to the cut-off grade, which is based on 95% mining recovery and 5% dilution at zero grade as well as a gold price of US$1,100/oz, the ore reserves and mineral resources gold grades are substantially higher, enabling CNMC to maintain its lucrative high margins.

Table 1. Manson's Lode pit ore reserves and mineral resources

	2012	2013	2014	2015
Ore Reserves				
Tonnes (kt)	98	98	95	111
Grade (g/t)	3.5	3.5	3.4	3.4
Contained gold (koz)	11	11	10	12
Additional Mineral Resources				
Tonnes (kt)	290	390	390	598
Grade (g/t)	2.3	2.1	2.1	1.6
Contained gold (koz)	22	26	26	30
Cut-off grade (g/t)	1.2	1.2	1.4	1.4

Source: Company, PSR

Table 2. New Discovery pit ore reserves and mineral resources

	2012	2013	2014	2015
Ore reserves				
Tonnes (kt)	120	120	120	287
Grade (g/t)	3.5	3.5	3.5	3.3
Contained gold (koz)	14	14	14	31
Mineral resources				
Tonnes (kt)	400	400	400	496
Grade (g/t)	2.8	2.9	2.9	1.6
Contained gold (koz)	36	37	37	25
Cut-off grade	0.5	0.4	0.5	0.4

Source: Company, PSR

Table 3. Rixen pit ore reserves and mineral resources

	2012	2013	2014	2015
Ore reserves				
Tonnes (mt)	2.4	2.8	3.1	3.7
Grade (g/t)	1.3	1.3	1.3	1.1
Contained gold (koz)	100	120	127	137
Mineral resources				
Tonnes (mt)	2.3	3.9	3.1	5.3
Grade (g/t)	1.3	1.2	1.1	1.2
Contained gold (koz)	95	114	107	197
Cut-off grade	0.5	0.5	0.4	0.3

Source: Company, PSR

2. Awaiting the ramping up of capacity in the foreseeable future

CNMC conducts a combination of heap and vat leaching processes in three yards, with the heap leach being the predominant processing method in 2015. By the end of Apr-16, the Group expanded the leaching capacity by another 200k tonnes/year. Together with the previous capacity of 1mn tonnes/year, total current minimum capacity stands at 1.2mn tonnes/year. Shown in Table 4, the tonnage of ore processed was lifted exponentially over the past 4 years, and it reached the production peak in 2015. According to the management, 2.2mn tonnes ore processed was close to the maximum capacity. With 20% increase in leaching capacity in 2016, we expect the output of gold dore will surpass last year's amount.

Furthermore, CNMC had just received the approval from Kelantan State Lands and Mines Office (PTG) of Malaysia for large scale operation for Sokor gold field project. The approval enables CNMC to mine unlimited amounts of ore at Sokor with the mining lease extended to 2034. There is no doubt that the Group is planning to expand operations in order to lift gold production volumes, thus we expect more gold output in the upcoming years.

Table 4. Sokor production statistics for 2012 to 2015

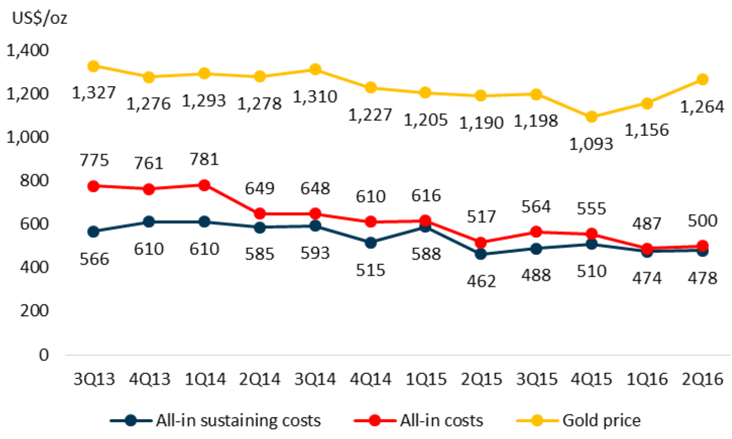
Commodity	Production statistics	2012	2013	2014	2015
	Rixen				
Mined	Ore tonnes mined (claimed)	90,000	323,000	1,362,138	2,236,674
	Ore tonnes processed	90,000	386,000	1,362,138	2,236,674
	Ore stockpiled (not processed as at 31 December)	63,000	63,200	-	-
Gold	Calculated grade (g/t)	0.3	1.07	0.94	0.61
	Recovered gold (oz)	861	11,800	27,685	29,645
	New Discovery				
Mined	Ore tonnes mined (claimed)	-	31,000	-	-
	Ore tonnes processed	-	31,000	-	-
Gold	Calculated grade (g/t)	-	1.14	-	-
	Recovered gold (oz)	-	1,100	-	-
Silver	Calculated grade (g/t)	-	N/A	-	-
	Recovered silver (oz)	-	690	-	-
	Manson's Lode				
Mined	Ore tonnes mined (claimed)	50,000	-	-	-
	Ore tonnes processed	46,791	-	-	-
Gold	Calculated grade (g/t)	0.65	-	-	-
	Recovered gold (oz)	984	-	-	-
Silver	Calculated grade (g/t)	75.00	-	-	-
	Recovered silver (oz)	112,451	-	-	-
Lead	Calculated grade (%)	0.003	-	-	-
	Recovered lead (kg)	1,397	-	-	-
Zinc	Calculated grade (%)	0.004	-	-	-
	Recovered zinc (kg)	1,752	-	-	-
	Total				
Mined	**Ore tonnes mined (claimed)**	**140,000**	**354,000**	**1,362,138**	**2,236,674**
	Ore tonnes processed	**136,791**	**417,000**	**1,362,138**	**2,236,674**
Gold	**Calculated grade (g/t)**	**0.42**	**0.96**	**0.94**	**0.61**
	Recovered gold (oz)	**1,845**	**12,900**	**27,685**	**29,645**
Silver	**Calculated grade (g/t)**	**75.00**	**N/A**	**N/A**	**N/A**
	Recovered silver (oz)	**112,451**	**690**	**20,886**	**22,057**
Lead	**Calculated grade (%)**	**0.003**	-	-	-
	Recovered lead (kg)	**1,397**	-	-	-
Zinc	**Calculated grade (%)**	**0.004**	-	-	-
	Recovered zinc (kg)	**1,752**	-	-	-

Source: Company

3. Low all-in cost offers buffer against fall in gold prices

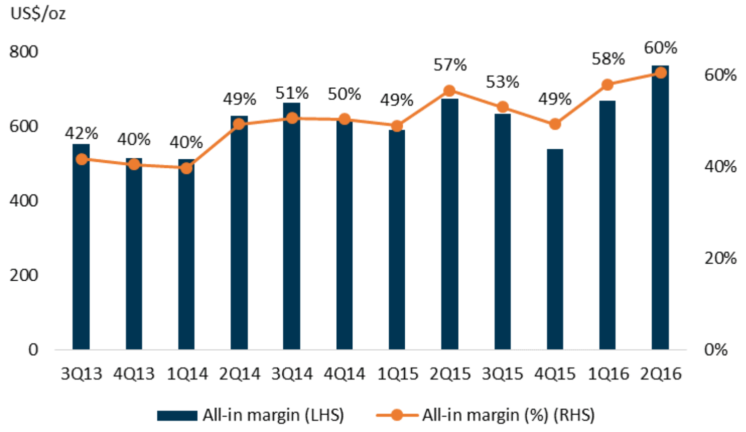
In order to improve profitability, expanding ore processing capacity and reducing operating costs are the most effective ways given that gold price is driven by the market and beyond the company's control. CNMC has been striving to lower all-in sustaining costs (AISC) and all-in cost (AIC), and maintain them at a low level. With the increasing gold production volume, the Group is reaching economies of scale, and as a result, AISC and AIC have been trending down, referring to Figure 13. Moreover, the convergence of AISC and AIC was due to a reduction in costs related to new operations and construction of facilities. As shown in Figure 14, the all-in margin averaged at US$612/oz (48% in percentage term) over the last 12 quarters.

Figure 13. AISC, AIC, and gold price



Source: Company, PSR

Figure 14. All-in margin



Source: Company, PSR

There are three major factors which enabled the Group to drive the downtrend of AISC and AIC. Firstly, open pit mining technique, an ore extraction process that is conducted at the surface of a mining site, is applicable to the deposits at the Sokor. Meanwhile, the group prioritised heap leach (HL) sources (Rixen, then New Discovery) and left the carbon-in-leach (CIL) processing (Manson's Lode) to the later part of the schedule. In other words, the Group mines the lower cost pits prior to higher cost pits. Referring to Table 5, since the Group currently focuses on mining at Rixen pit and keeps silent at other pits, the surge in mining costs is not expected in the near term. Secondly, apart from the blasting and drilling fleet, which are outsourced because of lack of related licences, the mining fleets, as well as administrative and technical services staffs, are all in-house employees. Thus, the Group is able to reduce the labour cost outflows to contractors, who charge a premium for providing services. Lastly, the Group has been ordering raw materials like leaching chemicals directly from China instead of procuring from the local market. Through these measures, CNMC further compresses the operating costs.

Table 5. Mining costs

Mining costs			
Mining cost - Rixen	US$ /t	1.00	CNMC 2014 / 2015 data
Mining cost – New Discovery	US$ /t	2.65	Optiro estimate
Mining cost – Manson's Lode	US$ /t	3.38	Optiro estimate
Processing recovery			
Heap Leach	%	65%	CNMC 2014 / 2015 data
CIL	%	80%	Optiro estimate
Processing costs			
Heap Leach	US$ /t ore	1.90	CNMC 2014 / 2015 data
CIL	US$ /t ore	33.00	Optiro estimate
Administration and Royalty	US$ /t ore	3.10	CNMC 2014 / 2015 data

Source: Company

However, with the depletion of ores at Rixen pit, the mining will start to shift to New Discovery and Manson's Lode, resulting in higher mining costs. We expect AISC and AIC to increase correspondingly as the mining shifts. In a nutshell, we expect AISC and AIC to increase, driven by capacity expansion, but still fluctuate within the range between US$500/oz and US$600/oz.

How Do We View CNMC?

Endeavours to mining business itself

CNMC's business model is purely simple, extracting gold from ores mined from the ground and selling it. Based on track record, CNMC does not keep any stocks of physical gold. Furthermore, according to Optiro Qualified Person's Report, gold bullion is sold on the spot market to local buyers, and there are no prevailing supply and demand constraints in the local gold industry. Therefore, finding buyers and monetising the gold bullion would not be an issue for CNMC. Besides, the Group does not hedge or arbitrage on the gold price and FX (MYR/USD). Management mentioned that transactions are based on average intraday spot price and FX. When gold price is on the uptrend, miners benefit more without hedging, and vice versa. From management's point of view, CNMC strategizes to maximise gold production and minimise operating costs. We think that CNMC is still at the early stage of exploration and production, and its focus on mining is the right move. After all, the output of underlying assets is the determinant of the mining business.

Other treasures underground awaiting to be explored and monetised

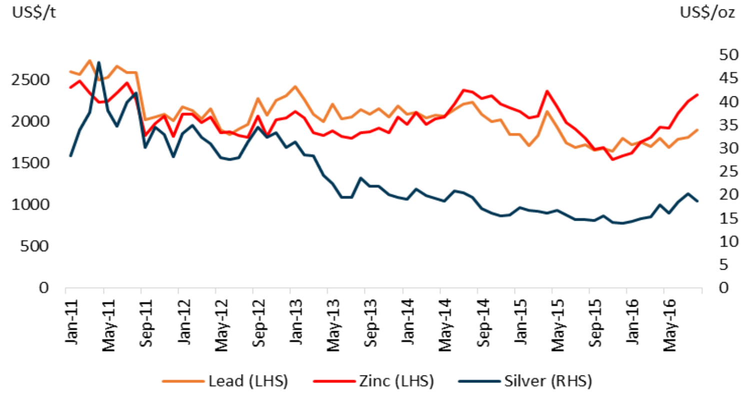
CNMC has only engaged in gold mining so far, except in 2012 when it also mined at Manson's Lode pit and shipped those concentrated ores containing silver, zinc, and lead to China for separation and extraction. As Table 6 shows, there is abundant Silver, Lead, and Zinc resources, awaiting to be mined. The respective average prices are US$24/oz for silver, US$2063/t for Lead, and US$2028/t for Zinc over the past 5 years, and all started to rally in early 2016, (see Figure 15). So far, the value of these resources has not been priced into the valuation of CNMC, so we believe potential upside for profitability and stock price is large.

Table 6. Sokor Project - Miner resources at Dec-15

Category	Mineral type	Gross attributable to licence			Gross attributable to CNMC			
		Tonnes (millions)	Grade (Au g/t, Ag g/t, Pb%, Zn%)	Contained metal (Au koz, Ag koz, Pb t, Zn t)	Tonnes (millions)	Grade (Au g/t, Ag g/t, Pb%, Zn%)	Contained metal (Au koz, Ag koz, Pb t, Zn t)	Change from previous update (%)
Measured	Gold	0.56	3.1	56	0.46	3.1	45	-2%
Indicated	Gold	7.14	1.3	297	5.78	1.3	241	+4%
Inferred	Gold	6.13	1.4	265	4.95	1.4	215	+63%
Total	**Gold**	**13.83**	**1.4**	**618**	**11.18**	**1.4**	**501**	**+22%**
Measured	Silver	0.33	63	674	0.27	63	546	+2%
Indicated	Silver	0.17	73	398	0.14	73	322	+10%
Inferred	Silver	0.71	28	645	0.57	28	522	+36%
Total	**Silver**	**1.21**	**44**	**1,717**	**0.98**	**44**	**1,391**	**+15%**
Measured	Lead	0.33	1.7	5,632	0.27	1.7	4,562	+1%
Indicated	Lead	0.17	1.7	2,925	0.14	1.7	2,370	+11%
Inferred	Lead	0.71	1.7	12,245	0.57	1.7	9,918	+188%
Total	**Lead**	**1.21**	**1.7**	**20,802**	**0.98**	**1.7**	**16,850**	**+67%**
Measured	Zinc	0.33	1.7	5,535	0.27	1.7	4,483	+1%
Indicated	Zinc	0.17	2.0	3,299	0.14	2.0	2,672	+8%
Inferred	Zinc	0.71	1.5	10,781	0.57	1.5	8,733	+142%
Total	**Zinc**	**1.21**	**1.6**	**19,615**	**0.98**	**1.6**	**15,888**	**+51%**

Source: Company

Figure 15. Silver, Lead, and Zinc spot price



Source: Bloomberg, PSR

Catalyst: Pulai project

Pulai Mining produced and sold more than 260kg of gold worth approximately RM38mn from Mar-11 to May-13. Besides, though there were no deliberate efforts to systematically explore feldspar deposits, more than RM500k in revenue was still generated through feldspar mining in 2015. The previous exploration suggested that Pulai has similar mineralisation features (geological background, tectonic structure, and geochemistry) as the Sokor gold mine. Besides, Pulai mine also contains iron ore resources, around 10,000 tonnes of which were extracted with the grade ranging from 50% to 55%. According to Management, on the premise that CNMC manages to seal the deal, it could possibly take three years to commence mining operations and generate decent positive cash flows. Therefore, we can expect positive synergies in the foreseeable future once the acquisition is accomplished.

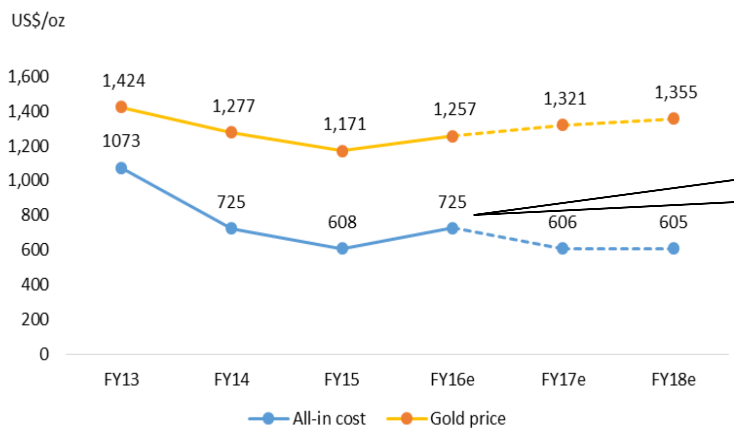
Key Assumptions

Y/E Dec (US$'000)	FY14	FY15	FY16e	FY17e	FY18e
Ore tonnes processed (tonnes)	1,362,138	2,236,674	2,534,897	2,684,009	2,952,410
Capacity (tonnes)	1,000,000	1,000,000	1,133,333	1,200,000	1,320,000
Production volume (ounces)	**26,122**	**31,206**	**35,367**	**37,447**	**41,192**
Implied gold grade (oz/tonne)	0.019	0.014	0.014	0.014	0.014
Gold price (US$/oz)	**1,277**	**1,171**	**1,257**	**1,321**	**1,355**
Total revenue	33,213	36,471	44,456	49,468	55,815
EBIT	**14,796**	**13,976**	**21,541**	**24,643**	**28,840**
EBIT Margin (%)	44.5%	38.3%	48.5%	49.8%	51.7%
NP	**12,243**	**10,666**	**16,550**	**19,216**	**22,739**
NP Margin (%)	36.9%	29.2%	37.2%	38.8%	40.7%

In Ap-16, CNMC's minimum ore processing capacity reached 1.2mn tonnes. We estimate the future ore tonnages processed on pro-rata basis.

We expect the implied gold grade to maintain at 0.014 oz/tonne.

We derive the estimated future spot gold price from Bloomberg



The surge of AIC is due to the payment to PTG and other authorities in Kelantan, and the amount is up to RM20mn, which is approximately equivalent to US$4.9mn

Valuation Methodology

From FY12, Management started generating increasingly positive Cash flows from Operations (CFO), amidst the downtrend of gold price. This was due to management's effort to expand capacity to achieve economies of scale. In other words, the impact of the declining gold price was offset by a substantial increase in production volume of gold. In FY14 and FY15, the Group started generating enough CFOs to cover capital expenditures.

Here we use discounted cash flow (DCF) which is based on free cash flow to equity (FCFE) as the valuation method to value CNMC.

Y/E US$'000	FY16e	FY17e	FY18e
CFO	27,142	31,271	36,625
FCinv	(8,155)	(3,935)	(4,655)
Net borrowing	100	80	60
FCFE	19,087	27,416	32,030
PV of FCFE	17,383	22,741	24,196
Terminal value			326,837
PV of terminal value			246,902
Total PV	311,223		
Weighted average number of ordinary shares	407,693,000		
Cost of equity	9.80%		
Sustianable growth rate	0%		
Target price (US$)	0.76		
Target price (S$)	**1.03**		

Investment Risks

Here we list the key risks for consideration:

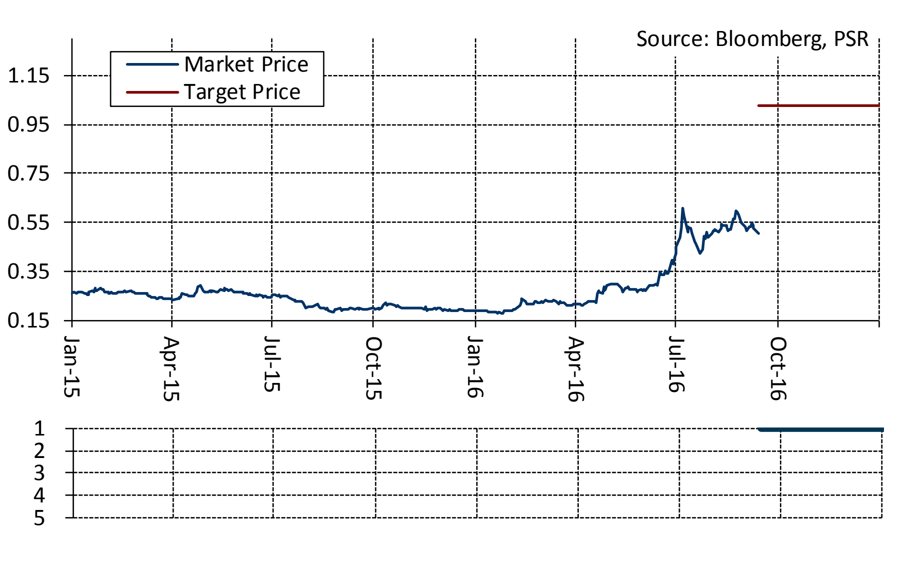
Risk	Remarks
	Upside
Gold price	CNMC's sales of gold bullion are based on intraday spot gold price. If it surges to a higher level, the top line will increase substantially.
Gold grade	The gold grade is determined by the mineralisation features in nature. It has nothing to do with operations and market movements. If the extracted ores happen to be higher grade ones, the production volume will increase, given the same processing capacity.
Capacity	The control of capacity is at the discretion of company strategy. Currently, we see higher probability that the company will keep expanding it.
FX	The functional currency is RM while the presentation currency is US$. It can see currency translation surplus when RM appreciates against US$.
	Downside
Gold price	If gold price trends down, the profit margin will be shrunk.
Gold grade	Lower gold grade requires the company to expand capacity in order to maintain similar profitability.
Ore reserves and resources	Profitability will taper off after ore reserves and resources are being depleted if no new mines are found.
FX	When RM depreciates against US$, it will suffer from currency translation deficit.
Policy	Mine resources are actually owned by the state government. Any unfavourable policy changes can turn the business the other way around.

Peer comparison

Company	Bloomberg Ticker	Mkt Cap (SGD mn)	EV (SGD mn)	EV/EBITDA TTM	P/E	P/B	Net D/E (%)	ROA (%)	ROE (%)
CNMC Goldmine Holdings Ltd	CNMC SP	211.8	176.9	4.3	10.8	3.8	Net Cash	3.8	5.8
Singapore									
Wilton Resources Corp Ltd	WILR SP	167.8	161.4	#N/A N/A	#N/A N/A	5.5	Net Cash	-13.0	-13.5
Hong Kong									
Hengxing Gold Holding Co Ltd	2303 HK	415.6	476.3	13.6	36.6	4.7	65.0	5.8	13.4
Zhaojin Mining Industry Co Ltd	1818 HK	4,086.1	7,519.6	18.2	58.0	2.3	82.1	1.1	3.9
Zijin Mining Group Co Ltd	2899 HK	12,986.4	18,177.9	12.8	53.9	1.7	73.2	1.0	3.2
China									
Chifeng Jilong Gold Mining Co Ltd	600988 CH	2,508.3	2,518.7	#N/A N/A	63.3	5.5	Net Cash	5.9	9.2
Western Region Gold Co Ltd	601069 CH	3,214.1	3,204.2	48.2	135.8	9.6	12.4	4.7	7.3
Shandong Gold Mining Co Ltd	600547 CH	11,608.1	12,516.8	#N/A N/A	51.6	5.6	36.5	4.7	11.4
Australia									
Rand Mining Ltd	RND AU	172.1	170.9	5.0	16.2	2.9	Net Cash	16.7	19.6
Ramelius Resources Ltd	RMS AU	241.6	197.1	2.2	7.7	1.7	Net Cash	15.7	24.3
Silver Lake Resources Ltd	SLR AU	265.0	232.3	4.2	59.6	1.4	Net Cash	1.7	2.4
Average				**19.6**	**59.3**	**4.6**	**53.8**	**5.7**	**9.7**

Source: Bloomberg, Phillip Securities Research (Singapore) Estimates

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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Financials

Income Statement

Y/E Dec (US$'000)	FY14	FY15	FY16e	FY17e	FY18e
Revenue	**33,213**	**36,471**	**44,456**	**49,468**	**55,815**
EBITDA	**17,847**	**17,962**	**26,109**	**29,696**	**34,410**
Depreciation & Amortisation	(3,051)	(3,986)	(4,568)	(5,053)	(5,570)
EBIT	**14,796**	**13,976**	**21,541**	**24,643**	**28,840**
Net Finance Inc/(Exp)	36	463	842	1,345	1,913
PBT	**14,832**	**14,438**	**22,383**	**25,988**	**30,753**
Tax	489	(1,010)	(1,565)	(1,817)	(2,150)
Net profit begore NCI	15,320	13,429	20,818	24,171	28,603
Non-controlling interest	3,077	2,762	4,268	4,955	5,864
Net Profit , reported	**12,243**	**10,666**	**16,550**	**19,216**	**22,739**

Per share data

Y/E Dec (US cents)	FY14	FY15	FY16e	FY17e	FY18e
EPS, reported	3.0	2.6	4.1	4.7	5.6
DPS	0.5	0.7	1.0	1.2	1.4
BVPS	6.2	8.2	12.2	16.7	22.1

Cash Flow

Y/E Dec (US$'000)	FY14	FY15	FY16e	FY17e	FY18e
CFO					
Profit for the year	15,320	13,429	20,818	24,171	28,603
Adjustments	3,343	7,528	6,391	6,725	7,157
WC changes	(446)	(882)	(555)	(563)	(580)
Others	(265)	155	488	938	1,445
Cashflow from ops	**17,952**	**20,230**	**27,142**	**31,271**	**36,625**
CFI					
CAPEX, net	(2,836)	(2,894)	(2,015)	(2,615)	(3,215)
Exploration & Evaluation Exp	(2,064)	(1,253)	(6,140)	(1,320)	(1,440)
Cashflow from investments	**(4,900)**	**(4,146)**	**(8,155)**	**(3,935)**	**(4,655)**
CFF					
Dividends to Company	(1,148)	(2,155)	(3,456)	(4,324)	(5,067)
Dividends to NCI	(448)	(753)	(1,105)	(1,394)	(1,636)
Others	(464)	(143)	(43)	(20)	(20)
Cashflow from financing	**(2,060)**	**(3,050)**	**(4,604)**	**(5,738)**	**(6,724)**
Net change in cash	**10,992**	**13,034**	**14,382**	**21,598**	**25,246**
Effects of exchange rate	(859)	(3,239)	(1,000)	(1,200)	(1,350)
Ending cash	**12,340**	**22,135**	**35,517**	**55,915**	**79,811**

Balance Sheet

Y/E Dec (US$'000)	FY14	FY15	FY16e	FY17e	FY18e
ASSETS					
Exploration & Evaluation Assets	4,990	2,085	6,169	5,617	5,292
Mine Properties	6,517	9,617	10,026	10,174	10,220
PP&E	7,569	8,163	7,397	6,826	6,328
Others	-	-	-	-	-
Total non-current assets	**19,076**	**19,866**	**23,591**	**22,616**	**21,840**
Cash	12,340	22,135	35,517	55,915	79,811
Trade receivables	613	832	957	1,100	1,266
Inventories	802	869	999	1,149	1,321
Others	-	-	-	-	-
Total current assets	**13,755**	**23,835**	**37,473**	**58,164**	**82,398**
Total Assets	**32,831**	**43,701**	**61,064**	**80,780**	**104,238**
LIABILITIES					
Trade payables	3,157	2,999	2,699	2,429	2,186
Borrowings	73	43	20	20	20
Dividend payable	761	917	1,186	1,392	1,648
Others	311	347	445	495	558
Total current liabilities	**4,301**	**4,305**	**4,350**	**4,336**	**4,413**
Borrowings	176	100	80	60	40
Others	542	1,250	1,250	1,250	1,250
Total non-current liabilities	**718**	**1,350**	**1,330**	**1,310**	**1,290**
Total Liabilities	**5,019**	**5,655**	**5,680**	**5,646**	**5,702**
Shareholder Equity	**25,160**	**33,495**	**49,811**	**68,265**	**90,164**
Non-controlling interest	2,653	4,551	5,573	6,869	8,372

Valuation Ratios

Y/E Dec	FY14	FY15	FY16e	FY17e	FY18e
P/E (x)	6.5	5.1	18.7	16.1	13.6
P/B (x)	3.2	1.6	6.2	4.5	3.4
EV/EBITDA (x)	4.0	2.1	10.7	8.8	6.9
Dividend yield (%)	2.0	3.6	1.3	1.6	1.8
Growth & Margins (%)					
Growth					
Revenue	99.8%	9.8%	21.9%	11.3%	12.8%
EBITDA	154.1%	0.6%	45.4%	13.7%	15.9%
EBIT	68.9%	-5.5%	54.1%	14.4%	17.0%
Net profit	356.9%	-12.9%	55.2%	16.1%	18.3%
Margins					
EBITDA margin	53.7%	49.2%	58.7%	60.0%	61.7%
EBIT margin	44.5%	38.3%	48.5%	49.8%	51.7%
NP margin	36.9%	29.2%	37.2%	38.8%	40.7%
Key Ratios					
ROE (%)	49%	32%	33%	28%	25%
ROA (%)	37%	24%	27%	24%	22%
Net Debt or (Net Cash)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

Source: Company, Phillip Securities Research (Singapore) Estimates

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

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