

# K92 Mining Inc.

## Precious Metals - Producer

**Rating**  
**BUY**  
unchanged

**Price Target**  
**C\$12.50**↑  
from C\$8.75

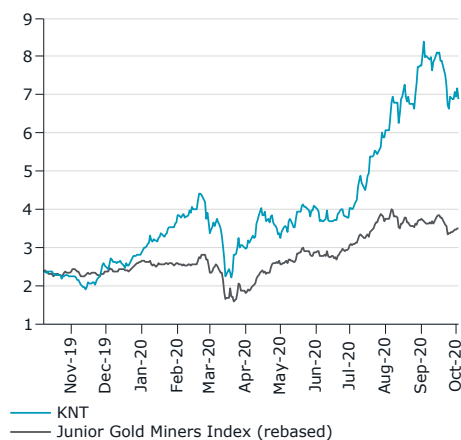
**KNT-TSXV**

**Price**  
**C\$6.79**

### Market Data

52-Week Range (C\$) :	1.55 - 8.50
Avg Daily Vol (000s) :	1,608
Market Cap (C\$M) :	1,457.6
Shares Out., Basic (M) :	214.7
NAV /Shr (C\$) :	12.60

FYE Dec	2019A	2020E	2021E
EPS Adj&Dil (US\$)	0.16	0.23↓	0.60↑
Previous	-	0.25	0.50
Total Cash Cost By-Prod.(Gold) (US\$/oz)	494	683	610
Gold Production (000oz)	80	93	147



Priced as of close of business 5 October 2020

K92 Mining owns and operates the Kainantu gold and copper mine in the Eastern Highlands province of Papua New Guinea.

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## Pounding the table on one of the best ore bodies we've ever seen

We reiterate our **BUY** rating but increase our target price to **C\$12.50** from \$8.75. We have incorporated exploration upside in addition to the Q2/20 resource update (note [here](#)) and have envisioned a slightly different future operating scenario than is outlined in recently PEA (note [here](#)). We believe the Kora system and surrounding epithermal vein sets represent one of the best ore bodies we have seen first-hand. Beyond this quarter (which we expect to be 20.1koz AuEq – due in large part to Phase 2 commissioning), we would be aggressively building a position in the name.

### Investment highlights and model updates

- We model 444koz with a full ramp up to beyond Phase 3 numbers by 2025 (vs PEA at 2023).
- We model 1.3Mt/a (vs PEA at 1Mt/a). Largely due to 400kt/a plant (currently in use) which is set to sit idle in the study. We do not think this is likely and believe the ore body and ongoing twin incline will support increased throughput.
- LOM operating cash costs of \$389/oz and AISC of \$517/oz vs PEA of \$202/oz and \$362/oz respectively. We believe this is a key area for further upside to our target.
- Exploration upside of 1.0Moz, which incorporates the potential porphyry target as well as historic high-grade epithermal resources of 1.3Moz.
- We employ a scenario analysis (P.10) which outlines an upside to our target price of \$20.52 and a downside, worst case scenario of \$6.72. This, in our view, shows a risk profile skewed to the upside supportive of our BUY rating and Top Pick status.

The company is gearing toward 10 drill rigs on site to test both near mine epithermal and regional porphyry type targets. We expect Blue Lake (porphyry) drill results toward the end of the year or into early Q1/21. In our view, the Porphyry potential changes the game. K92 does not need it to fulfill the valuation we have outlined; however, intersecting broad width porphyry mineralization in a region known for these systems makes K92 an immediate take out target.

Consistent, high-grade mineralization has been the norm for Kora and Kora north since late 2017. We expect the mine could continue to outperform the resource grade. Kora link and other, smaller, non-resource constrained veins or stringers have and could continue to provide grade especially as the tonnage is pushed. Dilution in this case is not zero grade from what we observed on site last year. Couple that with continuity (i.e. a surface expression mining levels below and drill holes well below the bottom workings) and you're left with a world class mineral system in the infancy of extraction.

### Valuation

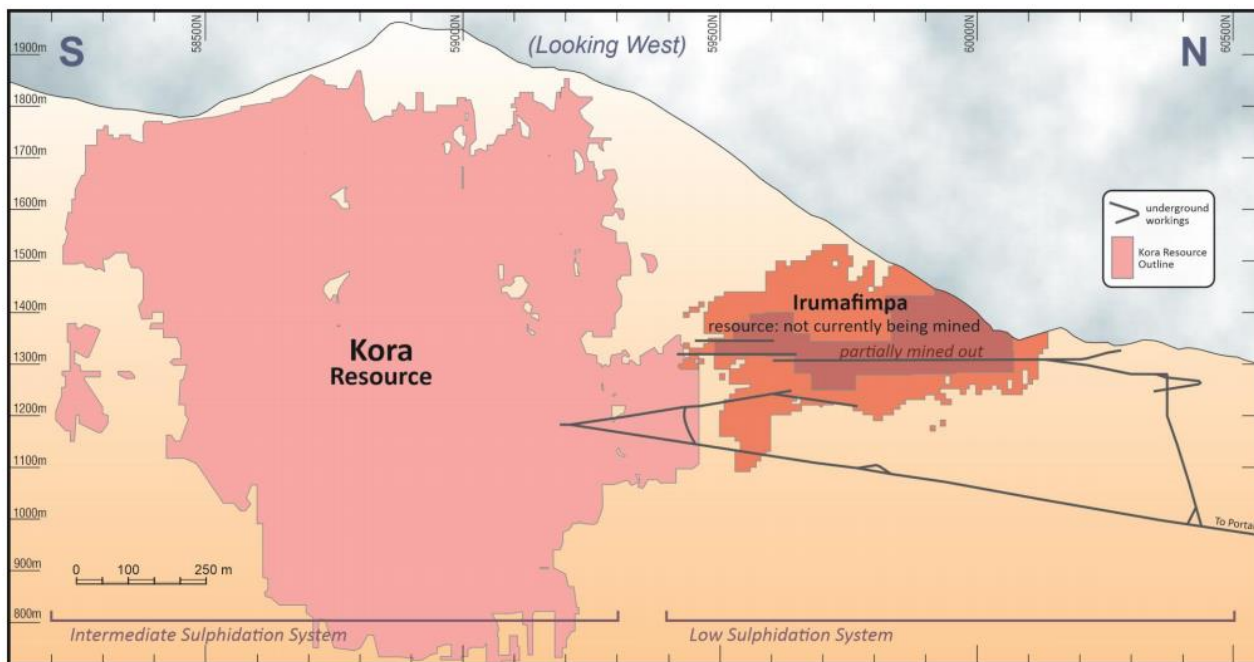
We maintain our BUY rating and are increasing our target price to C\$12.50 from C\$8.75 due an update to our Kainantu mine model, increasing long-term throughput and based on recent exploration results supporting the exploration potential of the property. Our operating NAV increases to C\$4,274M (up from C\$3,391M) based on adjustments to throughput and production. We increased our exploration NAV to C\$300M from C\$89M. Our target is predicated on a 50:50 weighted 0.9x P/NAV applied to our operating NAV of C\$19.76 and a 7.0x EV/EBITDA multiple applied to our 12-month forward EBITDA. We increased our P/NAV multiple based on historic P/NAV multiples in positive gold environments. We note that during 2009 gold producers traded at 1.4x P/NAV, and we believe there is still positive momentum in the current market. We add in corporate adjustments of \$0.81 to reach a target NAVPS of \$12.60, which we round to \$12.50. This generates an 84% return to target, supporting our BUY rating.

## Pounding the table on one of the best ore bodies we've ever seen

### The current state

K92 released an updated resource for the Kora deposit in April 2020 (see our previous [note](#)), which is highlighted in Figure 1 below. We believe that exploration potential at this mine supports future expansion upside and model slightly more than the 2020 resource calculation. Our model accounts for an extra 3Mt at an average of 9g/t Au and 0.9% Cu of additional ore to be processed, which we outline in greater detail below.

**Figure 1: April 2020 resource**

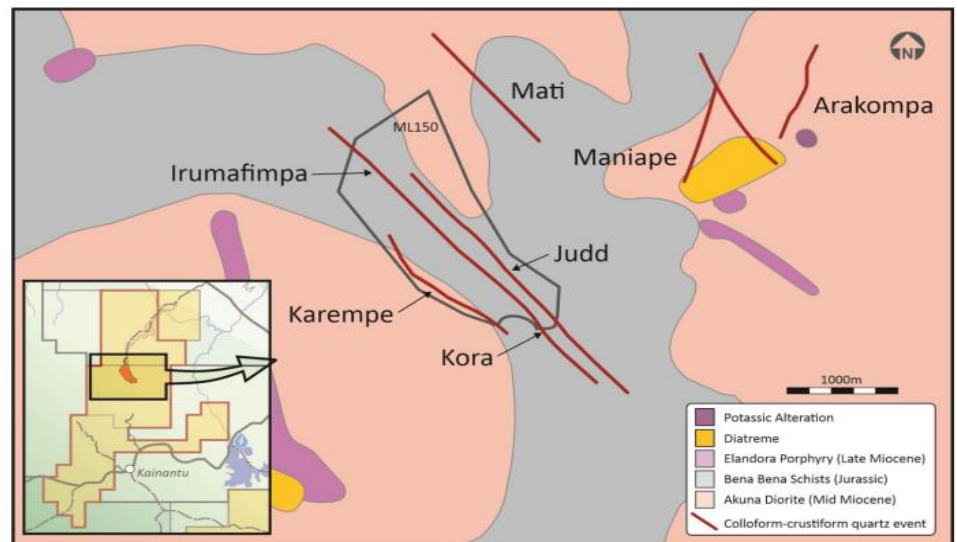


Source: Company Reports

## Near mine high priority targets

K92 has been drilling some of its high priority targets recently including the Irumafimpa extension, Kora, Judd and Karempa. The map below identifies the high priority near-mine targets that K92 believes could add significant resources to its current mineral resource estimate and be added into the future mine plan as these targets exist near current mine infrastructure. In our view, low incremental cap-ex would be required to add future minable tonnes.

**Figure 1: Near-mine targets**

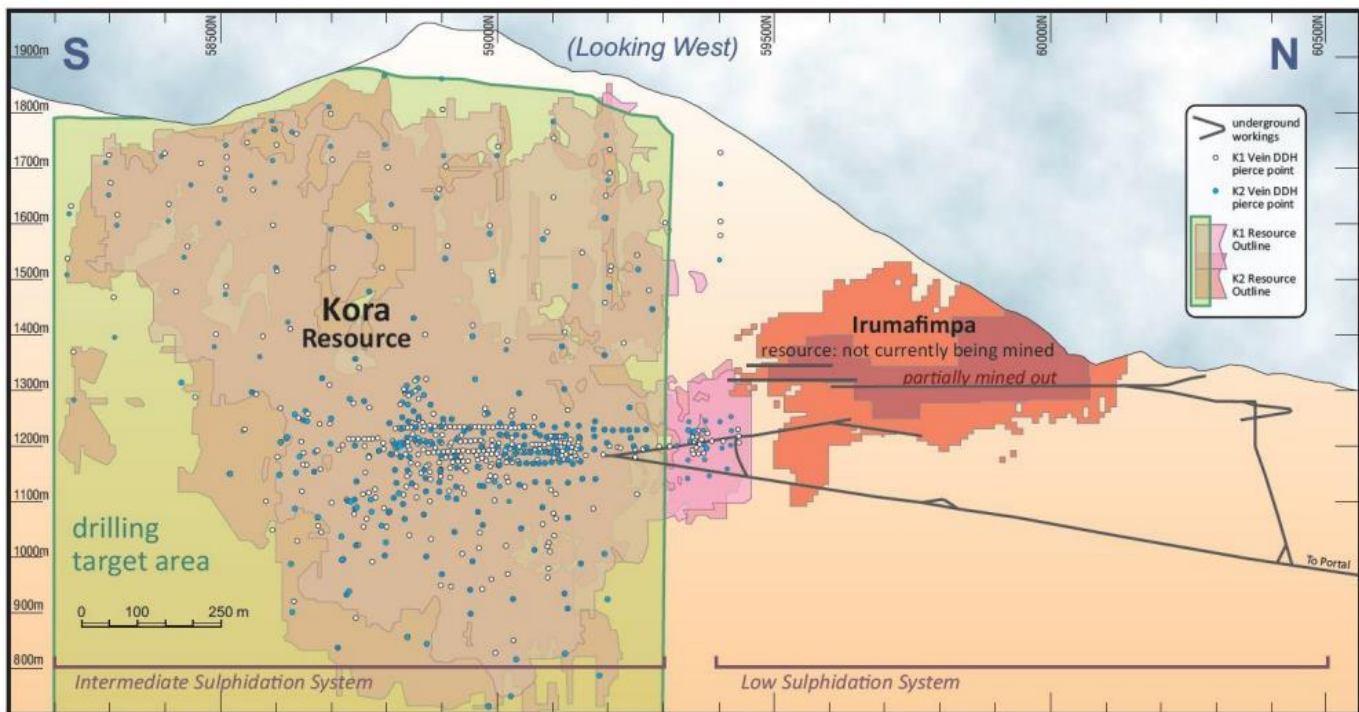


Source: Company Reports

### Kora and Kora Deep

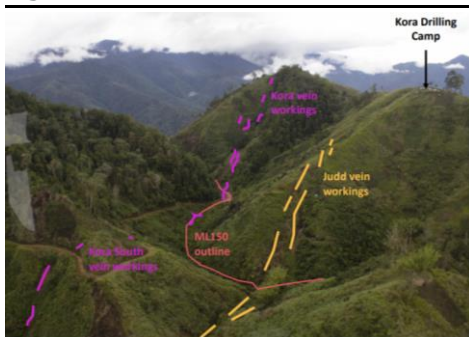
- Near the current resource area. 25% of it remains undrilled and Kora is open at depth.
- Drilling has recently focused on increasing density toward the south, including drilling from the most southerly underground access, which helps bolster our thesis that the vein system extends materially in that direction. Another key takeaway from the drilling is wide, long-hole amenable intersections are made, further supporting the switchover to this mining method as part of Phases 2 and 3.
- Drill results from Kora also consistently deliver bulk intercepts (true widths +18m), which we believe could imply future bulk mining with larger-scale stopes, potentially driving improved project economics with larger tonnage and lower unit costs. We believe that a bulk mining scenario supports our modelled mill capacity.

Figure 2: Kora and Kora deep drilling



Source: Company Reports

Figure 3: Kora and Judd South



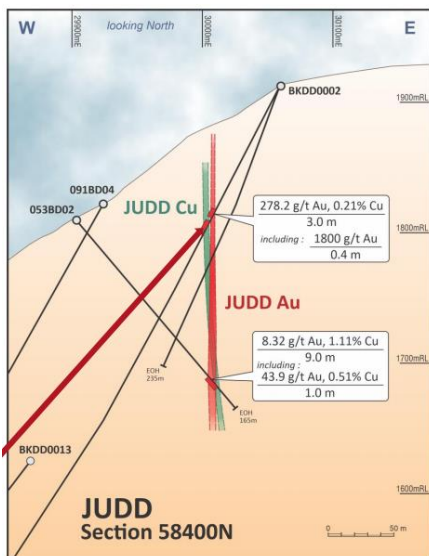
Source: Company Reports

### Kora South and Judd South

- The structure hosting these targets extends more than 1km beyond the mining lease to the south. There is outcropping and historical mining on these structures, some of which have not yet been drill tested by K92.
- Hole KMDD0225 was drilled from the most southerly drill bay underground, and it intersects the highest copper grade of 3.59% Cu in the K2 vein. The drill bay was only recently completed in July and K92 is planning to continue drilling to the south and hopes to have its next further south access ready in Q4. This drill cutout will be able to test Kora South beyond the current mining lease. The Kora South vein has been traced ~1km beyond the mining lease and was historically mined in the 1960s and 1970s by local miners.
- We believe that Kora South offers longer-term potential upside as it does not sit on the current mining lease. In our opinion, there is more than enough exploration and expansion potential on the current mining lease and if K92 proceeds with extending its lease or applying for a new one, it would not impact the progress of a potential Stage 3 expansion to 1Mtpa.



**Figure 4: Judd section 58400N**

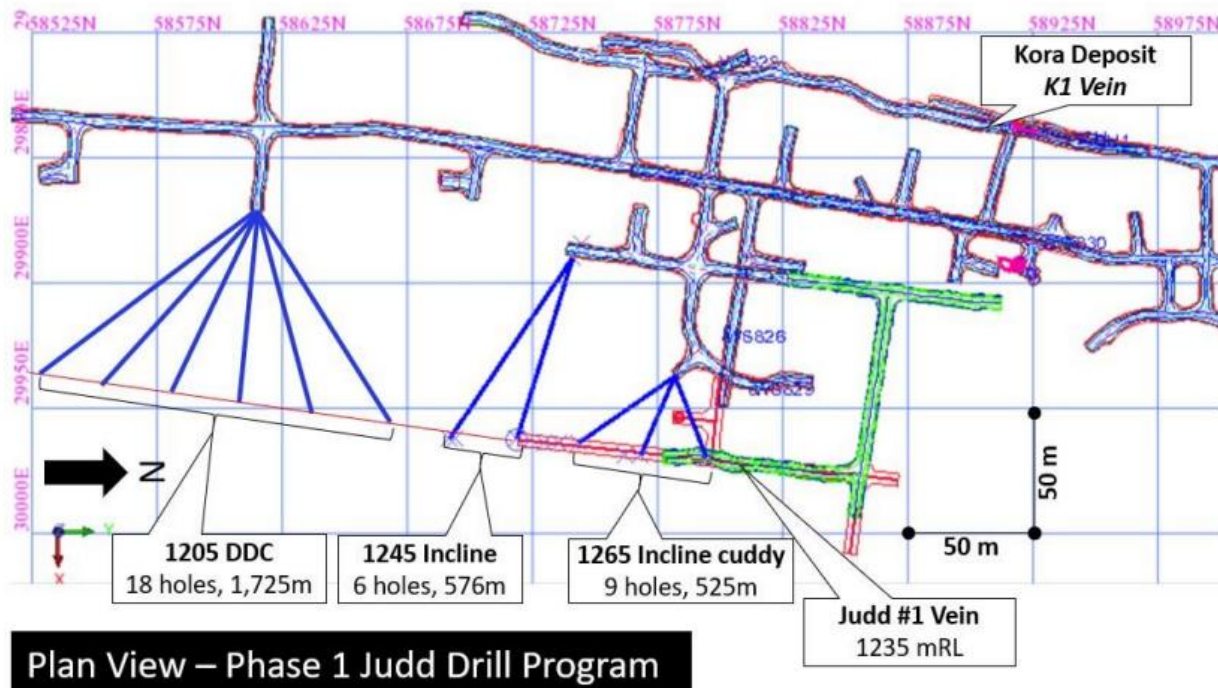


Source: Company Reports

### Judd

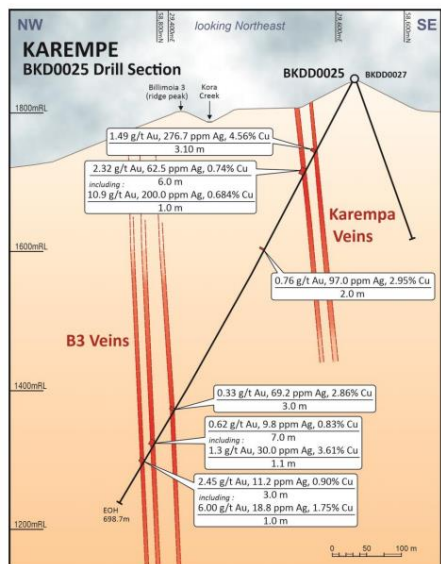
- Running subparallel to Kora and 100-150m from existing mine infrastructure, this vein has high-grade historical intersections. The four Judd veins are near-mine, high-priority exploration targets.
- The Judd vein set has a strike of ~2,500m and is within the mining lease. It is parallel to Irumafimpa and Kora, 50-100m from the main incline. There has been little exploration done on the vein system and Judd is not currently dominated as part of the very large gold equivalent resource that was outlined in April.
- A bulk sample was recently completed. There was approximately 109m of development from grade control channel sampling for a total of 6,200t @ 5.5 g/t AuEq (3.6 g/t Au, 1.11% Cu, 19 g.t Ag) with an average thickness of 3.4m. Judd has a potential strike of ~2.5km and a vertical extent of 700m and remains open at depth. As a result of the bulk sample, K92 is now completing a Phase 1 drill program at Judd and will also extend the bulk sample development drive.
- The drill program will consist of 33 holes targeting strike extensions from the development drive of ~250m in addition to up-dip, down-dip and step-out drilling
- We believe recent results demonstrate the near-mine expansion potential that exists within the confines of the mine. Judd #1 is only one of four veins which we believe could lead to additional resource upside.
- Due to the grade demonstrated, Judd would likely be blended with higher grade material or contribute more meaningfully to the mine plan once Phase 3 (much larger tonnage mill, Mt/a) is operational.

**Figure 5: Judd vein and bulk sample**



Source: Company Reports

Figure 6: Karempa veins



Source: Company Reports

### Karempa:

- Karempa is located 400-450m from existing infrastructure with artisanal workings present at surface.
- The vein now has a strike length of over 1,500m and is hosted in granitoid with extensive porphyry system like phyllic alteration. There is also a West to Northwest arc-parallel feature that has demonstrated higher grades in North-South subsidiary tension shears.
- Karempa could potentially be accessed from existing underground infrastructure. K92 is currently drilling Karempa as a next priority target.

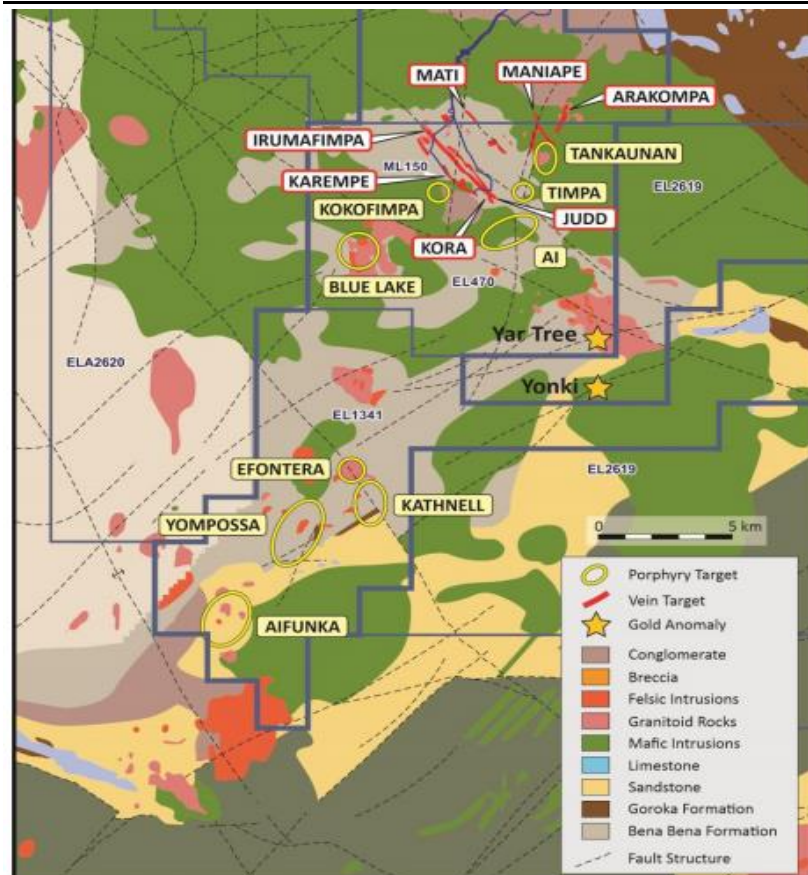
### Maniapa and Arakompa:

- Both have historical resources. Arakompa: 789koz @ 9.0 g/t and Maniapa: 560koz @ 2.2 g/t.

## Regional targets

In addition to near mine targets, there are several porphyry targets on the its 725km<sup>2</sup> land package. The company is currently drill testing Blue Lake and Yompossa with surface sampling recently completed on the Yonki skarn and porphyry target. The regional targets are porphyry targets, whereas the near mine targets are vein. Although the veins offer high grade sweeteners, the porphyry targets have the potential to offer higher tonnage opportunities that could significantly increase the current resource.

Figure 7: Regional and near mine targets



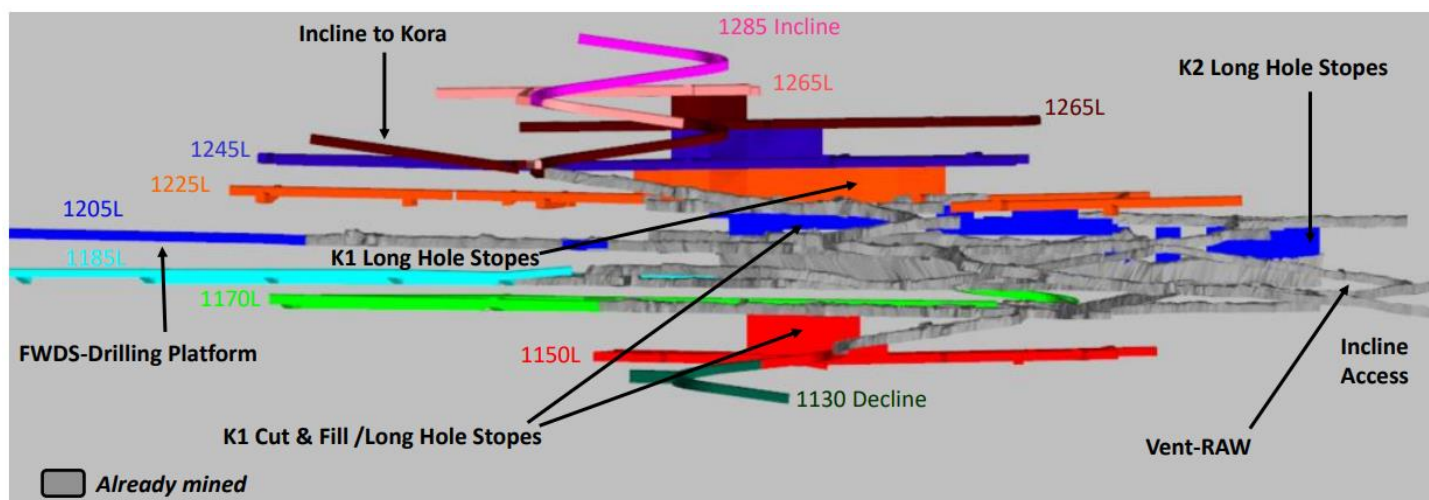
Source: Company Reports

## Kainantu Mine

### Current developments

- Official commissioning of Phase 2 is expected in Q3/20 with full expansion from 200ktpa to 400ktpa in Q4/20.
- As a result of the ramp-up, the company indicated that it would be processing lower grade material in Q3/20 and we expect production to be lower this quarter at 20.1koz AuEq (down from 26.9koz AuEq in Q2/20) at an average head grade of 9.5 g/t (down from 17.6 g/t in Q2/20).
- The twin incline for the Stage 3 expansion underway and K92 has initiated an FS with completion targeted for mid-2021.
- By the YE20, development work will have increased the number of sublevels to 8 (Figure 8) which help increased operational flexibility and throughput.

**Figure 8: Kora development and stoping plan**

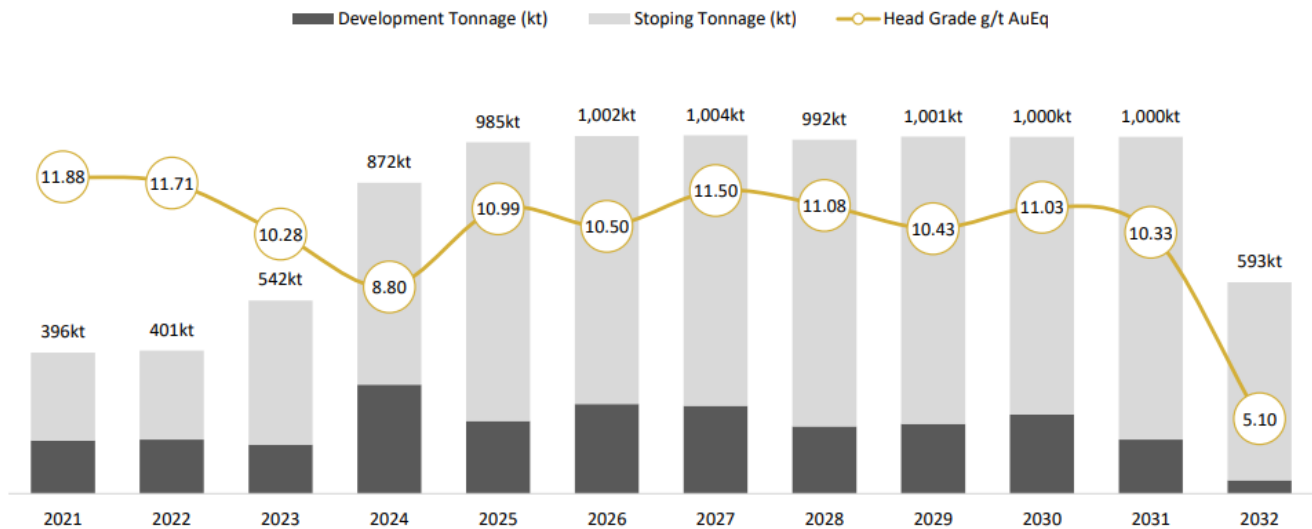


Source: Company Reports, Canaccord Genuity estimates

### CG model updates

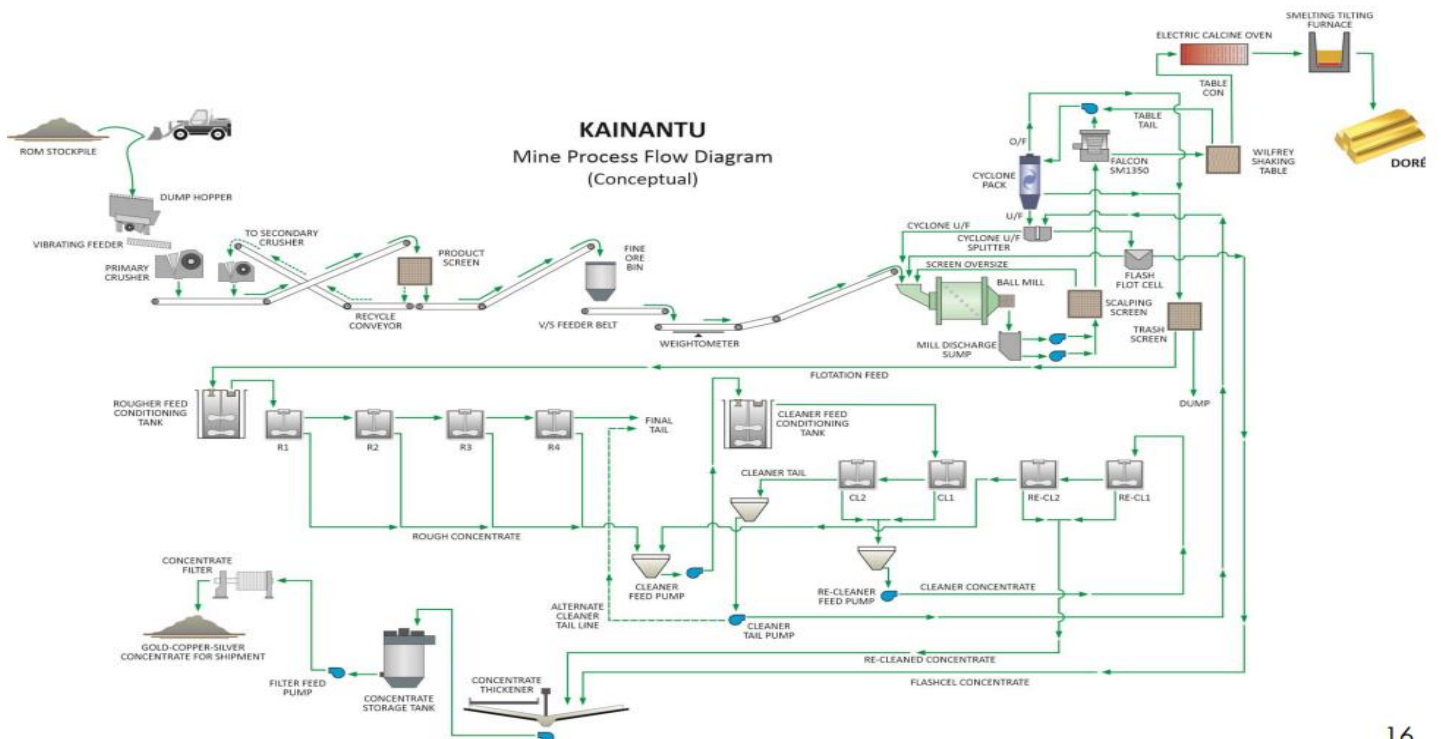
- We model an operation with a 13-year mine life based on the resource listed in Figure 1. We forecast a mill expansion from 400ktpa to 1.5Mtpa by 2025, increasing AuEq production from 289koz/a to 442koz/a. This generates a US\$3,063M NPV5% at long-term gold prices of US\$2,015/oz vs. the PEA NPV5% of US\$1,500M at US\$1,500/oz gold.
- The PEA outlines an operation based on 400ktpa from 2021-2023 followed by a ramp up to 1Mtpa in 2024. We imagine a slightly different scenario, where K92 can ramp up to ~1.3Mtpa. Based on the PEA, a new mill will be constructed for the 1Mtpa scenario, leaving a 400ktpa idle. We envision the company will have built up enough resources to support keeping both mills processing ore, increasing the total available throughput to 1.3Mtpa.
- We have added 3Mt at an average grade of 9 g/t Au and 0.9% Cu as additional exploration upside we expect to be realized from one of the numerous targets outlined previously. We believe due to the high prospectivity of the region that our ~1Moz Au additional resource is conservative.

Figure 9: PEA LOM material movement



Source: Company Reports

Figure 10: Updated flow sheet



Source: Company Reports



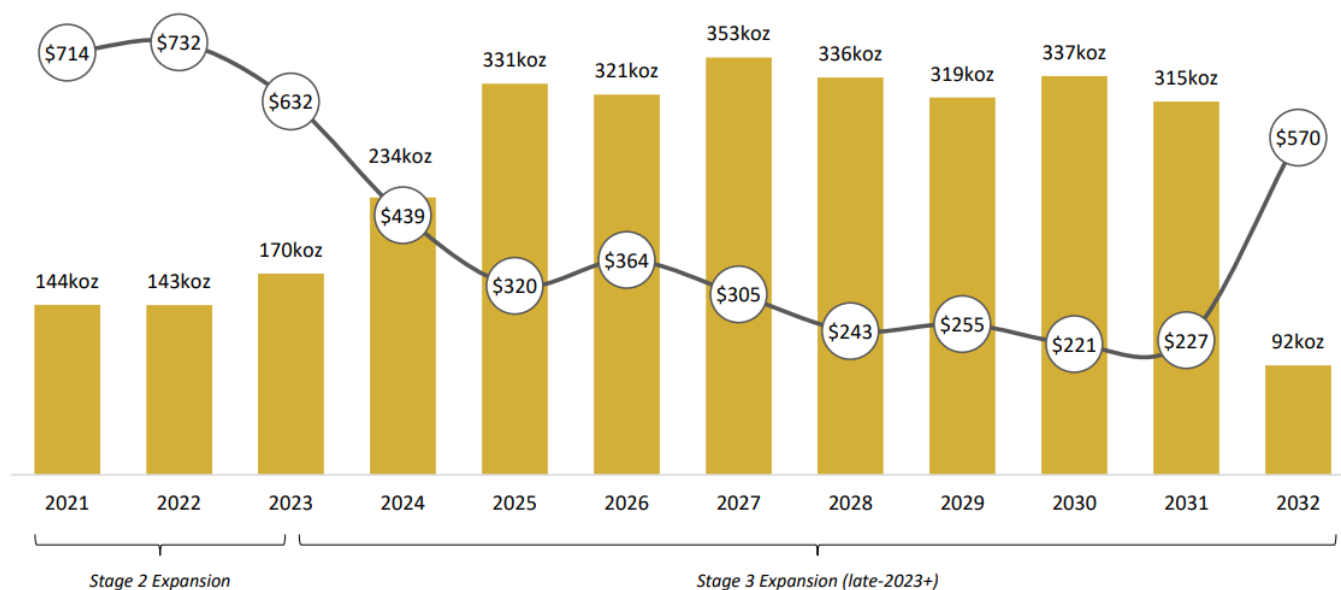
Figure 11: Key model parameters

CG Kainantu mine model 100% Basis		LOM
<b>INPUTS</b>		
Gold Price	US\$/oz	\$2,015
Copper Price	US\$/lb	\$3.00
Silver Price	US\$/oz	\$25.83
<b>OPERATING METRICS</b>		
Avg Au Grade	g/t	10.1
Avg Cu Grade	%	1.10%
Avg Ag Grade	g/t	18.2
Avg LOM throughput	Mt/a	1.19
Gold Recovery	%	94%
Avg Annual AuEq Producti	koz/a	360
Avg Annual Au Production	koz/a	352
Avg Annual Cu Production	Mlbs/a	28
Avg Annual Ag Production	koz/a	535
Mine Life	Years	13
<b>COSTS</b>		
Expansion Capital	US\$M	\$175
Sustaining Capital Cost	US\$M	\$536
Mining & Milling	US\$/t	\$110
LOM By-Product Cash Cost	US\$/oz	\$389
LOM By-Product AISC	US\$/oz	\$517
NPV5%	US\$M	\$3,063

Source: Canaccord Genuity estimates

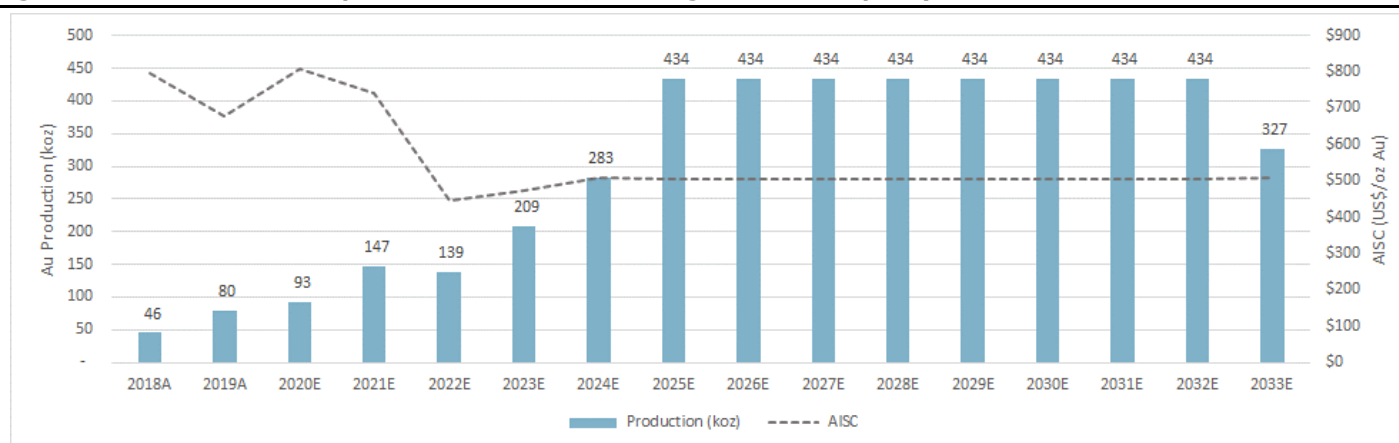
- **New mill:** The 1Mtpa processing plant will use conventional milling, gravity and floatation recovery. The flowsheet will be largely consistent with the current circuit; however, it will implement one-stage crushing (vs. two-stage) and SAG milling (vs. ball milling). There will also be Dore produced onsite. Currently the company only produces a concentrate that gets processed offsite. An updated flowsheet can be seen in Figure 10.
- **Operating costs:** We model operating costs at \$110/t, 15% above the PEA at \$94/t. Our costs could be conservative as the mine plan indicates it will long hole stope approximately 80% of mined material, offering a cheaper higher tonnage mining method compared to the more expensive and selective cut and fill method that will be used only 20% of the time.
- **Capex and sustaining capital:** We model Stage 3 capex of US\$175M, 30% above PEA estimates of US\$125M and sustaining capital of US\$447M, 20% above PEA estimates of \$341M.
- **Cash costs and AISC:** We model LOM cash costs of \$366/oz (PEA: \$202/oz) and AISC of \$494/oz (PEA: \$362/oz). We believe the company could outperform our estimates as the mining method continues to become more weighted to long hole stoping. However, even at AISC of \$700/oz (\$678/oz Q2/20 AISC) considering spot gold prices, the company generates over \$1,200/oz all-in margins.

Figure 12: PEA LOM production schedule and By-product AISC (US\$/oz Au)



Source: Company Reports

Figure 13: CG modelled LOM production schedule, showing additional capacity



Source: Canaccord Genuity estimates

## Scenario analysis

We employ a scenario analysis to explore difference bull and bear cases and their respective effect on our base case NAVPS.

### Bear cases:

**A. 30% government ownership:** Under the current Mining Act in Papua New Guinea, the government can only gain up to 30% ownership of a project if the mining license is new. Since the Kainantu mine is already in production, under the current rules the government has no right to 30% ownership. There have been media reports, however, that the government is considering changing the mining act including possible changes to government ownership (see Appendix A for more detail). In this case, we assume that the government changes the rules to be able to take 30% ownership of a project at any time, which we believe is unlikely. This decreases our NAVPS by \$2.65 to \$9.95.

**B. No expansion to 1Mtpa:** If K92 does not proceed with the 1Mtpa mill expansion, this would decrease our NAVPS by 17% to \$10.50.

**C. 10% lower grades:** We model conceptual resources, if the company find these ounces but at grades 10% lower (8.1 g/t Au and 0.6% Cu) this would decrease our NAVPS by \$0.31 to \$12.29.

**D. 30% higher costs:** We estimate Opex 15% higher than the PEA and Capex 30% higher than the PEA. If these costs come in additional 30% higher then what we estimate, this reduces our NAVPS by 7% to \$11.78.

### Bull cases:

**E. PEA costs:** Assuming we use \$94/t operating costs and \$125M for expansion capital as listed in the PEA, this would increase our NAVPS by 4% to \$13.15.

**F. 10% higher grades:** Assuming the K92 finds our conceptual ounces at a 10% higher grade, this increases our NAVPS by \$0.31 to \$12.91.

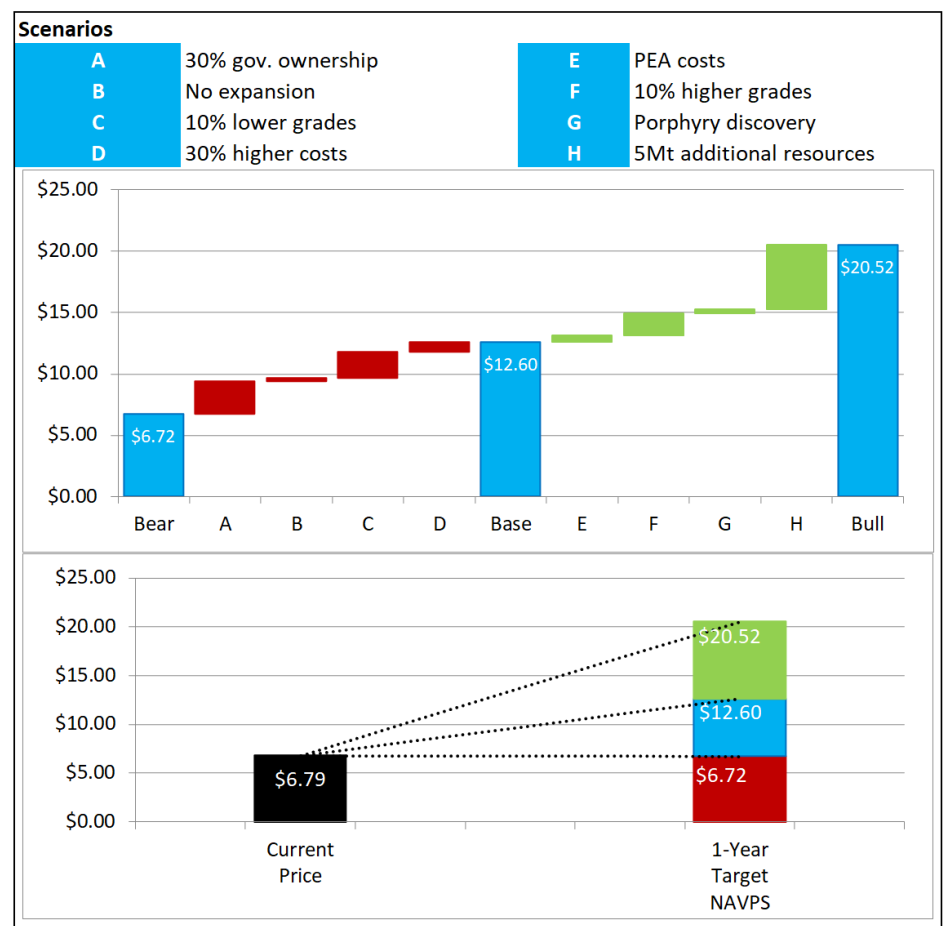
**G. Porphyry discovery:** Blue Lake represents the exploration upside that has just begun to be explored. However, based on initial exploration results, there are many features of the deposit that appear to indicate a porphyry deposit. We have given Blue Lake a conservative potential value of C\$500M. Based on our current in-situ database, the average AuEq in-situ value for 2P reserves is US\$87/oz, which implies a reserve of 4Moz AuEq. If the deposit is a porphyry, the resource/reserve could be

much larger. If we consider this conservative base, the discovery of a porphyry increases our NAVPS by 14% to \$14.39.

**H. 5Mt additional resources:** Assuming K92 finds an additional 5Mt of resources, beyond what we model, the NAVPS increases by \$5.27 to \$17.87.

Our downside scenarios (A-D) suggest a bear case target NAVPS of C\$6.72, or -1% from the current stock price. Alternatively, our upside scenarios (E-H) suggest a bull case target NAVPS of C\$20.52, or 63% up from our base case and 201% from current levels. In our view, K92 has a risk profile skewed to the upside, supportive of our BUY rating. Any one of these bull case factors could support future upside to K92's valuation. Moreover, the country's history of volatility and any execution of future operations present considerable risk.

**Figure 14: Scenario analysis**

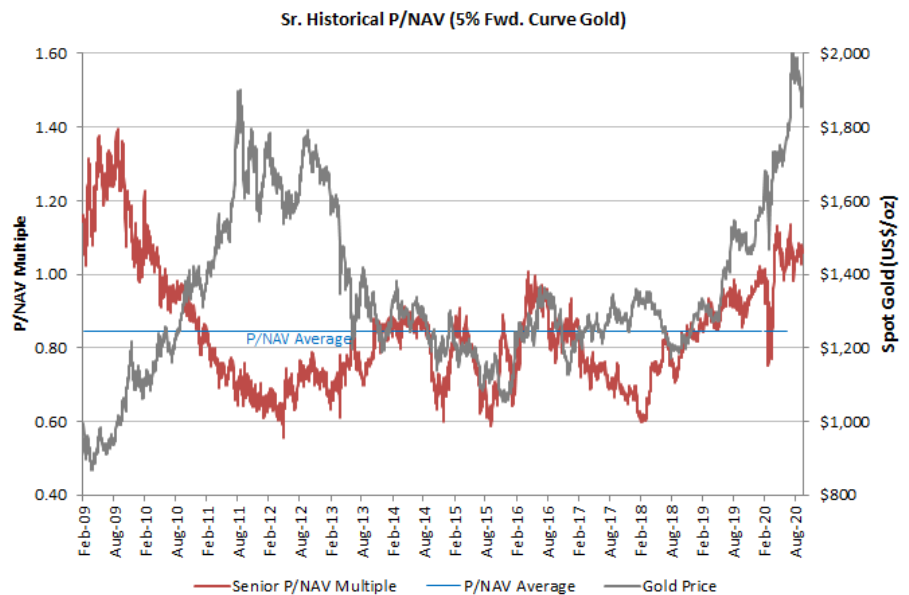


Source: Canaccord Genuity estimates

## Peer multiple comparison

We have adjusted our P/NAV multiple for Calibre based on the current gold price environment and our bullish stance on gold equities. Figure 6 compares past trading multiples and shows that as the gold price increased in 2009, P/NAV multiples traded at up to 1.4x P/NAV for covered gold producers. We conservatively have only increased our P/NAV multiple to 0.9x from 0.8x, however believe there is room to the upside. If we increased our multiple to 1.4x, this would add \$4.94 to our NAVPS increasing it to \$17.54. In addition, we conservatively use a 7.0x EV/EBITDA multiple applied to our 12-month forward EBITDA. Covered peers currently trade at 8.4x, if we adjust our EV/EBITDA multiple to 8.0x this adds \$0.39 to our NAVPS increasing it to \$12.99. Combining both would give us an unrounded NAVPS of \$17.93.

**Figure 15: Historic P/NAV multiples**



Source: Canaccord Genuity estimates

## Valuation

We maintain our BUY rating and are increasing our target price to C\$12.50 from C\$8.75 due an update to our Kainantu mine model, increasing long-term throughput and based on recent exploration results supporting the exploration potential of the property. Our operating NAV increases to C\$4,274M (up from C\$3,391M) based on adjustments to throughput and production. We increased our exploration NAV to C\$300M from C\$89M. Our target is predicated on a 50:50 weighted 0.9x P/NAV applied to our operating NAV of C\$19.76 and a 7.0x EV/EBITDA multiple applied to our 12-month forward EBITDA. We increased our P/NAV multiple based on historic P/NAV multiples in positive gold environments. We note that during 2009 gold producers traded at 1.4x P/NAV and we believe there is still positive momentum in the current market. We add in corporate adjustments of \$0.81 to reach a target NAVPS of \$12.60, which we round to \$12.50. This generates an 84% return to target, supporting our BUY rating.



Figure 16: NAV and target generation

NAV and Target Generation		WACC Method		
		C\$M	C\$/sh	% Total
Operating Assets				
	Kainantu (1)	\$4,274	\$18.46	90%
Total Operating NAV		\$4,274	\$18.46	90%
Exploration & Development Assets				
	Exploration potential (2)	\$300	\$1.30	6%
Exploration & Development NAV		\$300	\$1.30	6%
Corporate Adjustments				
	Working Capital	\$174	\$0.75	4%
	G&A	-\$10	-\$0.04	0%
	Long-term Liabilities	\$0	\$0.00	0%
	ITM Warrants & Options	\$24	\$0.10	1%
Net Corporate Adjustments		\$188	\$0.81	4%
Corporate NAV		\$4,763	\$20.57	100%
Shares (Fully Funded, M)				231
Target Generation				
	Operating NAVPS		\$18.46	
	Exploration NAVPS		\$1.30	
	Multiple		0.90x	
	Adjusted Project NAVPS		\$17.78	
	Net Corporate Adjustments		\$0.81	
	EV/EBITDA Multiple		7.00x	
	Target		\$12.60	
Target Price (Rounded)			\$12.50	
Projected Return			84.1%	
Implied P/NAV(5%) at Current Share Price			0.54x	
		1. After-tax DCF discounted at WACC (5.0%) 2. In situ		

Source: Company Reports, Canaccord Genuity estimates

Figure 17: K92 P&L

KNT:TSX	\$ 6.79	SHARE DATA					COMMODITY DECK	2019A	2020E	2021E	2022E	+2025E
Target Price (C\$)	\$12.50	Basic Share Count (m)	215				Gold Price	\$1,392	\$1,797	\$1,984	\$1,976	\$2,015
Recommendation	BUY	FD Share Count (m)	231				Silver Price	\$16.20	\$20.60	\$25.21	\$25.33	\$25.83
Market Cap (C\$m)	\$1,458	Trading Volume (000)	1,608				Copper Price	\$2.73	\$2.66	\$3.00	\$3.25	\$3.00
Enterprise Value (C\$m)	\$1,436						CAD/USD	\$0.75	\$0.74	\$0.75	\$0.74	\$0.74
NAV SUMMARY (5%)												
Operating Assets	CAD\$m	C\$/sh					BALANCE SHEET	2019A	2020A	2021E	2022E	2023E
Kainantu	\$4,274	\$18.46					Cash & Equivalents	\$21,612	\$43,898	\$114,023	\$192,268	\$303,977
Exploration & Development Assets	\$300	\$1.30					Working Capital	\$25,046	\$59,646	\$129,771	\$208,016	\$319,725
Corporate adjustments							Total Debt	\$0	\$0	\$0	\$0	\$0
Working Capital	\$174	\$0.75					Shareholder Equity	\$124,690	\$177,919	\$282,345	\$427,446	\$647,604
G&A	(\$10)	(\$0.04)					Enterprise Value	\$1,451	\$1,436	\$1,414	\$1,344	\$1,265
Long-term Liabilities	\$0	\$0.00										
ITM Warrants & Options	\$24	\$0.10					RATIOS - CG DECK	2019A	2020E	2021E	2022E	2023E
Sub-total	\$188	\$0.81					P/E	7.4x	5.2x	2.0x	1.7x	1.1x
Total Operating NAV	\$4,763	\$20.57					P/CF	4.8x	3.6x	2.4x	1.7x	1.1x
Shares (Fully Funded, M)	231						EV/EBITDA	(2.2x)	(0.6x)	(0.2x)	(0.2x)	(0.1x)
Target Generation							Sustaining FCF (US\$)	\$3,924	\$36,535	\$70,125	\$80,052	\$111,709
Operating NAVPS	\$18.46						Total FCF (US\$)	(\$25,276)	\$13,163	\$52,625	\$36,302	\$41,709
Exploration NAVPS	\$1.30						FCF Yield	(9.5%)	5.0%	19.8%	13.7%	15.7%
Multiple	0.90x											
Adjusted Project NAVPS	\$17.78						OPERATING SUMMARY	2019A	2020E	2021E	2022E	2023E
Net Corporate Adjustments	\$0.81						Gold Production (koz)	80	93	147	139	209
EV/EBITDA Multiple	7.00x						Copper Production (klbs)	913	2,452	3,149	10,708	14,311
Target	\$12.60						Silver Production (koz)	23	55	100	192	272
Target Price (Rounded)	\$12.50						GEO Production (koz)	82	94	149	142	212
							By-product cash costs (US\$/oz)	\$494	\$683	\$610	\$308	\$343
							Co-product cash costs (US\$/oz)	\$515	\$760	\$693	\$576	\$565
							By-product AISC (US\$/oz)	\$680	\$809	\$740	\$446	\$475
							Co-product AISC (US\$/oz)	\$701	\$879	\$817	\$727	\$710



Source: Company Reports, Canaccord Genuity estimates

## Appendix A - Papua New Guinea

As excerpted from our Australian colleague Reg Spencer's recent report on Kingston Resources (note [here](#)), Papua New Guinea is made up of four regions broken into 22 provinces. The four regions are the Highlands, Islands, Momase and Southern Region. K92's property is located 140km from Lae, 21km from Kainantu township and 56km from Goroka, the capital of the Eastern Highlands Province.

Approximately 75% of PNG's export earnings are derived from mining and mineral exports (including gold, copper, oil, natural gas and other minerals) and as a result are an integral part of the country's economy. There are numerous world class mines that are currently in operation. including Porgera (250kozpa), Ok Tedi (280kozpa Au + 100ktpa Cu) and Lihir (0.9Mozpa) gold mines, and the +40ktpa Ramu nickel/cobalt operation. In addition to operating mines, PNG hosts a number of world class development projects including Wafi Golpu (27Moz) and Frieda River (20Moz Au + 13Mt Cu).

The 1992 Mining Act is the principal legislation governing mining exploration and development in PNG. Under the Act, all minerals existing on, in or below the surface of any land in PNG, including any minerals contained in any water lying on any land in PNG, are the property of the State. The Mining Act provides the framework for exploration and production of minerals and is administered by the Minerals Resource Authority (MRA). A self-funded body, the MRA was established under the Mineral Resources Authority Act in 2005 and administers the Mining Act. The tenements that can be granted under the Mining Act include:

- Exploration license
- Mining lease
- Special mining lease
- Alluvial mining lease

Royalties to the state are set at 2% of the value of the mined product and landowners are entitled to 20% of the royalty paid. In addition, a small 0.25% levy is payable to the MRA and corporate income tax is typically levied at 30%.

The State also has a right to acquire up to a 30% stake in mining projects (acquisition price specified as the pro rata share of accumulated exploration expenditure on the exploration license). The right is not typically taken up on small and medium-sized projects and the Government may negotiate for an equity interest in projects of up to 5% on behalf of local landowners.

### **Possible changes to the Mining Act**

There have been recent media reports that there could be changes to PNG's Mining Act so that the Government could capture downstream value through in country refining, payment of social levy to landowners, and possible changes to Government ownership in projects. This would affect concentrate production and the royalty structure. Based on the possibility of a change to the royalty structure, we have increased our royalty to 3.5% from 2.5% to be conservative.

# Appendix: Important Disclosures

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## Investment Recommendation

Date and time of first dissemination: October 05, 2020, 21:33 ET

Date and time of production: October 05, 2020, 21:33 ET

## Target Price / Valuation Methodology:

K92 Mining Inc. - KNT

Our operating NAV increases to C\$4,274M (up from C\$3,391M) based on adjustments to throughput and production. We increased our exploration NAV to C\$300M from C\$89M. Our target is predicated on a 50:50 weighted 0.9x P/NAV applied to our operating NAV of C\$19.76 and a 7.0x EV/EBITDA multiple applied to our 12-month forward EBITDA.

## Risks to achieving Target Price / Valuation:

K92 Mining Inc. - KNT

**Gold Price:** As is the case for all mines, revenue is largely derived from underlying commodity price(s). In this case, gold and copper prices are the key commodities to which the company is sensitive. Companies that have higher costs demonstrate more leverage to commodity prices and may be preferred ways to play an upswing in the gold and copper prices. Our model demonstrates mid-range costs, meaning the company should have moderate leverage to the gold and copper price.

**Political risk:** The 1992 Mining Act is the principal legislation governing mining exploration and development in PNG. Under the Act, all minerals existing on, in or below the surface of any land in PNG, including any minerals contained in any water lying on any land in PNG, are the property of the State. There is a framework in place to develop mineral resources; however, there are media reports that the government could be reconsidering the terms of the mining act to capture downstream value through in-country refining, payment of social levy to landowners, and possible changes to government ownership in projects. This could result in higher royalties and companies losing partial ownership of projects.

**Local community relations and project management:** Strong community relations are currently in place and K92 has been able to gain the trust of the local landowners. This resulted in access being granted to areas which had previously not undergone detailed exploration. In 2017, a group of landowners representing the Bilimoia Interim Landowners Association (BILA) entered the mine and caused major damage to some mining equipment and infrastructure. Although minor in relation to the project as a whole, issues like this can cause halts and delays in operation. A resolution was signed with the BILA which the company believes has addressed the underlying issues, and there is an MOA and work ongoing to expand business opportunities for the Landowners group.

**Seismicity:** This is a tectonically active region with a major active fault running through the valley some 20km to the north, roughly perpendicular to the property package and strike of the Kora lode system. We believe there is a very real risk of a major earthquake, which could cause catastrophic damage underground or hamper site services or infrastructure in and out of the region.

**Topography:** The property is located proximal to rugged topography that has rivers transecting lower-lying areas. The elevations range from 400m to 1600m above sea level and the vegetation is largely rainforest with some areas of shifting agriculture in valley floors, although the main site itself is relatively flat with no logistical restrictions on groundworks (for tailings or site expansions) should the company require them. If the company discovers a porphyry, given the typically large scale of this type of operation the topography could pose a challenge to its development in the future.

## Distribution of Ratings:

### Global Stock Ratings (as of 10/05/20)

Rating	Coverage Universe		IB Clients
	#	%	%
Buy	531	61.32%	54.80%
Hold	173	19.98%	41.04%
Sell	14	1.62%	35.71%
Speculative Buy	125	14.43%	79.20%
	866*	100.0%	

\*Total includes stocks that are Under Review

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**HOLD:** The stock is expected to generate risk-adjusted returns of 0-10% during the next 12 months.

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**NOT RATED:** Canaccord Genuity does not provide research coverage of the relevant issuer.

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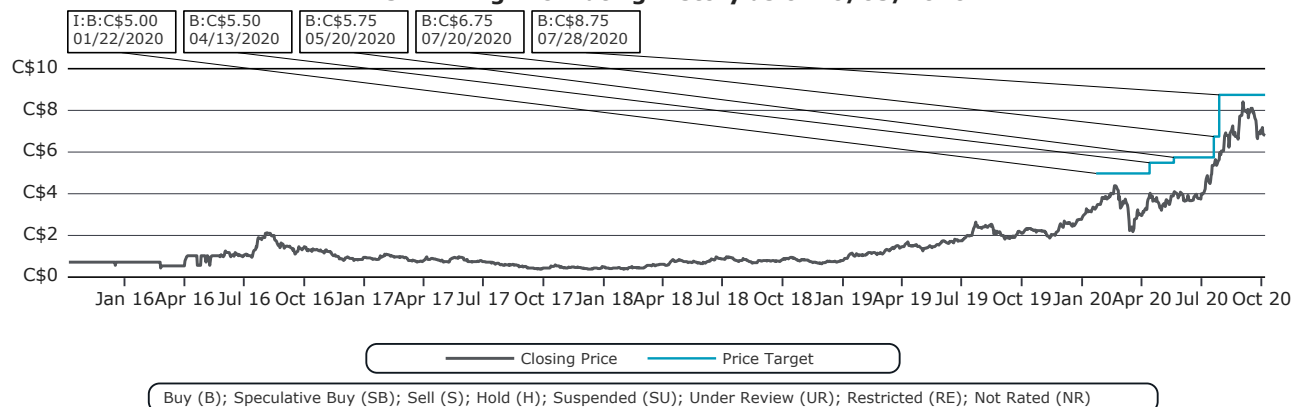
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### K92 Mining Inc. Rating History as of 10/05/2020



## Past performance

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