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Factors That Should Lead To Higher Gold And Silver

In This Issue:		
Precipitate Gold	Paramount Gold	U.S. Gold
Silver Viper	Notes: FSM, RBMNF	New idea: Delta Resources

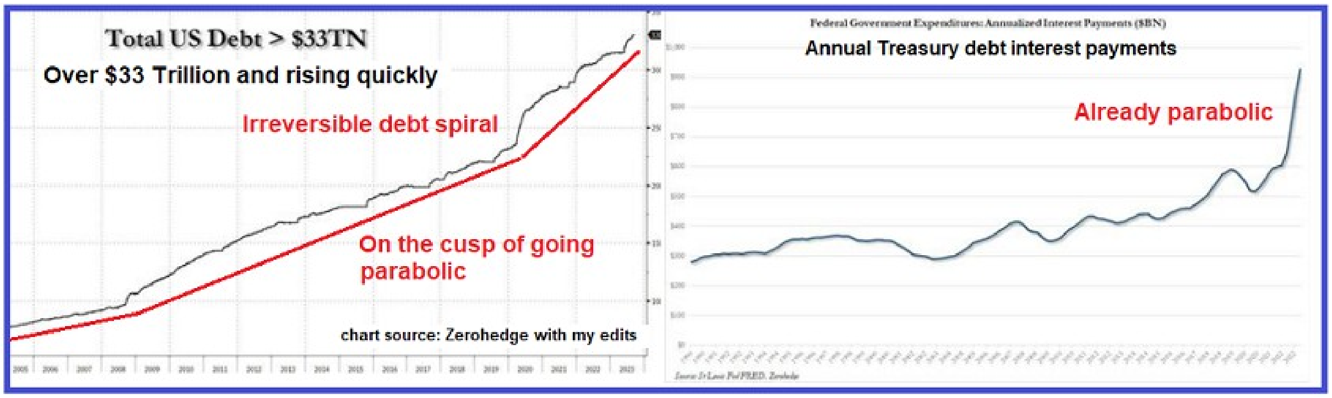
A subscriber asked me if I'm worried about downward pressure on the prices of gold and silver given the Fed's current monetary policy and the potential for the dollar to stage a big rally. The short answer is "no" for a few reasons.

To begin with, the Fed's monetary policy definitionally is not "hawkish" or "tight." While the "real" interest rate using the 10-yr Treasury break even calculus (10-yr Treasury yield minus the 10-yr TIPS yield) currently is 2.35%, this is a bogus number. The TIPS yield is derived from CPI "inflation," which we know is highly flawed. Thus the 10-yr TIPS yield does not reflect the actual rate of price inflation.

Based on how the CPI was calculated in 1980, John Williams' (Shadowstats.com) has the real rate of inflation at around 12%. This is more inline with most peoples' actual experience. With the 10yr Treasury at 4.41% and using Shadowstats' inflation calculation, the real interests are more like negative 7.6%. Negative rates are dollar devaluative, which jis why gold does well in a negative interest rate environment.

Additionally, while the Fed is paying lip service to its Quantitative Tightening program, the Fed over the course of the last 17 months has reduced its balance sheet by just 10%, whereas it took just 13 months to more than double its size. Furthermore, the Fed has shown a propensity to inject $100's of billions back into the banking system at the first sign of problems with banks. Not only did it throw $400 billion immediately at the regional bank crisis, it set up a QE-like liquidity facility for the banks under which $107 billion has already been drawn. This too is dollar devaluative and positive for gold (and silver).

Another reason I'm not concerned about the effect of Fed policy on gold and silver is the reckless and extreme mismanagement of the Federal Government finances. The amount of outstanding Treasury debt is now over $33 trillion, up $1 billion in just the last three months. The interest cost is about to exceed $1 trillion annually. Both look like they're starting to go parabolic:



The spending deficit for the Government's FY 2023, which ends on September 30th, is projected to exceed $2 trillion. Once Congress manages to approve the FY 2024 budget, I expect the 2024 spending deficit to again project at north of $2 trillion, though maybe not initially, for purposes of political expediencey.

Moreover, the United States' foreign financiers (China, Japan, Saudi Arabia etc) have been reducing the amount of new Treasuries they are willing to buy. This leaves the Fed plus its EU Central Bank cronies to do the heavy lifting or rates will spiral higher. Until the Fed reinstates QE, the rate of new issuance will drive long-term rates much higher. I don't see the Fed or the Treasury letting that happen, which means there will be a lot more QE in some shape or form in the near future.

Both the current Treasury debt level and the expected much higher level of Treasuries outstanding are not lost on the precious metals sector, which is why I believe gold has been holding firm above $1900 and silver has been holding $23. Once the Fed flinches on QT/QE, the value of gold and silver priced in dollars will reprice quickly and substantially higher - similar to the late 2008 - mid-2011 bull run.

Finally, regardless of rising nominal interest rates and the Fed's current faux-hawkish policy stance, physical demand in the Asian countries plus India and the middle east is very strong right now. The premium paid above the spot price on the Shanghai Gold Exchange hit a record high recently. The rationalization was that China's gold import curbs implemented to slow down the outflow of yuan from China that paid for the gold created a shortage of supply vs demand. China recently removed the import curb but the premiums on the SGE remain elevated (**SGE gold premiums**) - note: the data in those charts linked is sourced from the Shanghai Gold Exchange.

Additionally, it seems there's a renewed appetite for gold in Japan. Gold recently hit an all-time high in Japan priced in yen because of the recent decline in the value of the yen. But there's also a demand component. Gold buyers in Japan are paying a premium to the spot price, reflecting strong demand for physical gold relative to supply: "In Japan, where domestic gold rates were trading at record levels this week, dealers charged $0.5 premiums. A Tokyo-based trader said that it is 'surprising' that local investors are buying gold at these high levels" (**Reuters**).

As with Japan, the demand for gold is strong in Saudi Arabia, where gold priced in riyals hit a record level this month (**source link**). The riyal rose vs the dollar in the first half of 2023 and has been stable vs the dollar since then. This means that the rising price of gold there is not attributable to currency devaluation per se but is a function of supply and demand.

Two more sources of strong demand for physical gold are Russia and the United Arab Emirates. In early August, **Russia announced** that its Central Bank would resume buying gold after it halted purchases in January 2022 to conserve cash in the face of oil sanctions imposed by the U.S. Russia's demand, whether the Central Bank sources domestically produced gold or imports it, will further stress global supplies. Adding to this is the fact that the UAE has become the biggest importer of Russian produced gold, buying roughly one-third of Russia's annual mine production (**Bloomberg**).

The point here is that, even with demand from India lower than usual for this time of year (as reflected by the discounts observed in India currently), several other countries in Asia and the Middle East have increased their gold importation. I believe this is why the repetitious attempts to push the price of gold and silver lower recently in the paper derivatives markets in London and New York have been unsuccessful. Moreover, despite the common mis-perception that the Fed's "hawkish" policy is bearish for gold and silver, the prices of both metals have not only been resilient buy, in my opinion, are consolidating for a big move higher in the near future.

Company Updates

Precipitate Gold (PREIF, PRG.V - US$0.04) - PRG reported that Barrick Gold has begun a diamond drill (core) program within the Lithocap Zone on PRG's Pueblo Grande project, which is adjacent to Barrick's Pueblo Viejo gold in the Dominican Republic. Lithocaps are geological formations that are laterally and vertically extensive, and can host high-sulphidation near-surface gold mineralization as well as host a "hidden" copper-gold porphyry at depth. Pueblo Viejo is one of the largest high-sulphidation districts in the world.

The program will drill up to ten holes on the Lithocap Zone immediately adjacent to the Pueblo Viejo mining pits. Barrick's expanded drill program on Pueblo Grande is targeting near-surface gold mineralization as well as the possibility of a concealed copper-gold porphyry-style target at depth below the gold mineralization. It's possible that Barrick believes there's discoveries to be made on Pueblo Grande because deep porphyry drilling is expensive.

Recall that Barrick signed a deal to earn a 70% interest in Pueblo Grande. At the same time it invested $1mm in PRG's equity. The deal was signed three years ago. Barrick must spend $10 million on exploration and drilling within six years. Barrick has already paid PRG $5 million for part of the Pueblo Grande property in order to build support facilities for the expansion of the Pueblo Viejo processing facility.

If Barrick makes material discovery with this program, I believe PRG's stock will double quickly. I also think Barrick might make a move to acquire PRG. If Pueblo Grande hosts a gold deposit, will make the Pueblo Viejo mine even more valuable. We own an underweight position in PRG. I don't know that I would go crazy loading up on PRG shares, but I think at the current price level that the optionality upside potential outweighs the downside risk in the event that Barrick does not make any discoveries on Pueblo Grande. Keep in mind that PRG has a little more than 3 cents US$ per share on its balance sheet and a very low burn rate.

Paramount Gold (PZG - $.28) - PZG completed an updated resource estimate on its Sleeper gold project in Nevada after digitizing and validating the Sleeper database (database verification) which captured $10's of millions of historical work on the project since the original

AMAX gold discovery hole in the 1980's. This included a revision of gold and silver values against original assay certificates, drill hole logs and verification of over 300,000 samples containing gold and silver assays. The updated estimate shows 1.897 million ozs of measured/indicated gold at roughly 0.36 gpt plus 20.6 million ozs of measured/indicated silver (low grade which can be used as cost credits). In addition there's 1.2mm ozs of indicated gold and 9.4 million ozs of indicated silver.

Of course in this market the stock did not react to the news. Currently PZG's future valuation is predicated on the success of getting the Grassy Mountain project Federally permitted and over the finish line. The Feasibility Study for Grassy Mountain shows a project with a base case ($1,750 gold) NPV of US$114 million. At $1,900 gold the NPV is $146 million. PZG's current market cap fully-diluted is US$19.5 million, which in my view is a joke.

I've always thought that the PZG management would get Grassy Mountain over the finish line and sell the mine to a strategic buyer while spinning-off and advancing Sleeper. That was the formula the management used when it sold Paramount Gold and Silver to Coeur for $146 million in 2014 for the San Miguel project while spinning off Sleeper. In 2015 PZG acquired Grassy Mountain. We own a slightly overweight position in PZG. I think this stock has the potential to be a 5-bagger at least if/when it makes a positive construction decision on Grassy Mountain. Kinross, Centerra and Anglogold Ashanti are three prospective suitors.

US Gold (USAU - US$3.52) - USAU has been light on news flow because the Company is basically in "waiting mode" to receive a permit to construct and operate a CK Gold mine. It expects a permit approval decision in early 2024. While advancement of CK continues, the Company has time to allocate to exploration. It announced on September 12th the completion of a "hyperspectral" study of the Keystone Project.

Hyperspectral imaging uses spectroscopy to identify geologic anomalies with the potential to host precious metals mineralization. Changes in the physical or chemical properties of rocks and minerals show up via the various colors in a hyperspectral image. This technique assigns a wide spectrum of colors beyond the primary red, green and blue colors generated by standard geophysical studies. This provides even more information from the imaging.

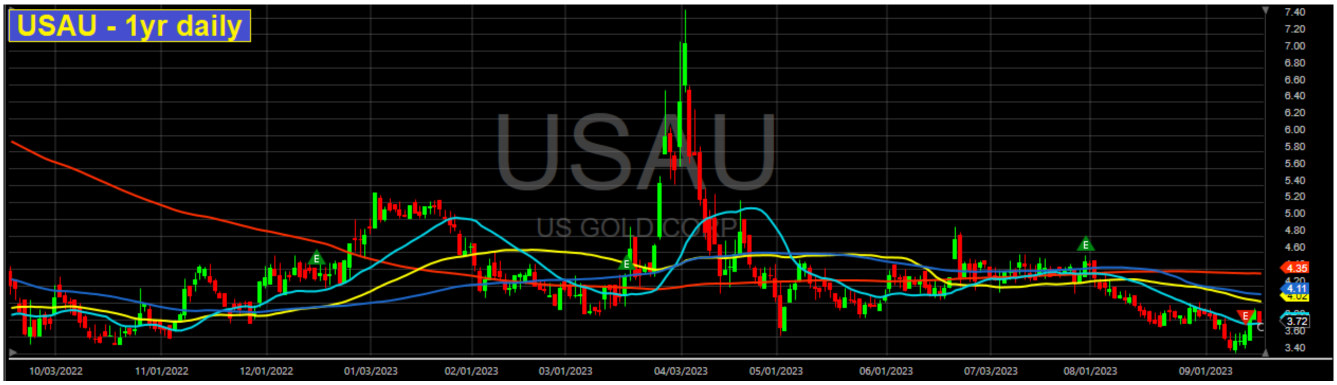
The results of the study have confirmed the Company's view about the opportunities at existing target areas and added other targets that otherwise would be difficult to identify on Keystone's 20-square mile land package. The Company has a crew in the field conducting surface investigations in order to prioritize drill targets with discovery potential.

USAU intends to start a drill program for which it is already permitted, that will encompass up to 22 angled and vertical drill holes within five "high potential" target areas. It also has planned follow-up drilling on the Nina Skarn and Sophia target areas. Long-time subscribers might remember that these two targets were considered highly prospective by the two previous head geologists (Ken Coleman and Dave Matthewson). Two "wildcat" holes are planned for a target area called Greenstone Gulch. And there's two other target areas for which follow-up holes are planned.

Recall that the Keystone project sits about eleven miles south/southeast on trend from Barrick's Cortez Hills mine complex, which is one of the biggest mines in Nevada with more than 20 million ozs of gold. Keystone also sits nine miles north/northeast on trend from McEwen Mining's Gold Bar mine.

Historical drilling on Keystone going as far back as 1967 by the likes of Newmont, Chevron and Placer Dome (acquired by Barrick) encountered some gold mineralization but the holes averaged 427 feet, which is too shallow for the type of geologic (Wenban Formation) formation at Keystone. The Wenban Formation in the Cortez trend area is a limestone structure composed of an upper unit about 500 feet thick and a lower unit up to 2,500 feet thick. Based on the deeper drilling from 2016 to 2019 done by USAU, the Company believes there's discoveries to be made in the lower unit section of the target areas.

As with most other junior micro-cap project development stocks, USAU has been beaten into the ground but it appears that it may have bottomed and begun to turn higher:



While the stock has underperformed GDXJ, which is not a good comp for the micro-caps because the average market cap for GDXJ components is $3 billion, USAU has out-performed or performed in-line with most of its peers.

USAU continues to be by far our largest holding. I will probably add even more shares at this level (or lower) once I become more confident that the sector is headed sustainably higher. There's two catalysts that should catapult the stock. The first is the approval of the permits required to construct and operate CK Gold. The other catalyst would be a big discovery at Keystone. We know the permit decision is expected in early 2024. The timing of the drill results will depend on when the drill program begins. I think a positive event from either catalyst could take USAU to US$10 or higher.

Silver Viper (VIPRF, VIPR.V - US$0.07) - Several subscribers have asked me about Silver Viper with the price in the 6 to 7 cents area US$. It's been a while since the Company has released any news other than the private placements to raise capital. I know they are currently doing the prep work for a drill program.

I chatted briefly with Steve Cope (CEO) to see if there is an expected timeframe to start the drill program and if there's any other catalysts that might move the stock price. He said he's anxious to get the drill turning as soon as possible but they have not established a firm start date yet. They'll be drilling the El Rubi deposit zone with the goal of expanding the mineralized footprint. This will be followed with test drilling on new targets on the El Molino target zone, which lies south-east of the El Rubi deposit. Initial surface work (chip-channeling) along with geochem analysis shows that El Molino exhibits continuously high gold and silver "anomalies" along a south-east trend. An updated resource estimate will be released after the drill program.

I think this is a good level to buy VIPR or add to an existing position. The stock was beaten down from selling pressure from the last private placement. The selling comes from accounts who strip the warrants and dump the stock or who shorted shares to hedge the private placement shares until the lock-up period expires. Steve said there is one more small block he's trying to move.

That said, I think the chart is starting to look bullish now that the selling pressure has mostly subsided:

I think this stock has the potential to at least triple if/when we get a nice, sustained move higher in gold and silver. The US$14 million market cap for VIPR is a joke given that it has an estimated resource of 260k ozs of gold and 12.9 million ozs of silver and most of the resource is open pit. Steve said fundamental catalysts that could move the shares will be drill results plus an updated resource estimate that will incorporate the results from the upcoming drill program.

Quick notes on Fortuna Silver and Rugby Resources: FSM announced earlier this week that it has officially closed the acquisition of Chesser Resources. Recall, Chesser is advancing the Diamba Sud project in Senegal, West Africa. Diamba Sud has an existing resource estimate of 850k ozs of indicated/inferred gold with average grades between 1.5 gpt and 1.9 gpt. I had dinner with the Company this week. The plan is to start drilling to upgrade and expand the resource in order to evaluate the economics of a potential mine. Senegal is a mining friendly jurisdiction with several gold producers operating there already. In addition, Seguela is now ramped up and will likely start to contribute a substantial amount of free cash flow to the Company. In my opinion, the potential economics that will be generated by FSM's portfolio of mines is substantially underestimated by the market right now.

Earlier this week the volume on Rugby Resources increased quite a bit and the stock ticked higher. A subscriber who owns the shares asked if I knew any reasons for this. I touched base with Rob Grey at the Company, who told me that Rugby recently hosted several potential strategic partners at the Cobrasco project in Colombia to help Rugby continue advancing the project. Recall that Rio Tinto is in a JV partnership with a private company advancing a similar copper porphyry project adjacent to the east of Cobrasco. I suspect Rio is just one of a handful of large, global copper producers who might have keen interest in the project. At its current price of 5 cents US$, if you can manage to source some shares there, RUG is worth allocating a small amount of speculative capital given the limited downside at this price and the potential upside if a major producer comes in to help develop the project.

New idea - Delta Resources (DTARF, DLTA.V - US$0.14) - My friend and colleague, Trevor Hall (Mining Stock Daily), showed me this idea. DLTA is advancing two early-stage exploration projects, Delta-1 in Ontario, Canada and Delta-2 in Quebec, Canada. I think DLTA has merit as a highly speculative junior play because, after a deep-dive that included a conversation with the CEO (Andre Tessier), I believe the potential upside outweighs the downside risk if DLTA-1 can not be advanced successfully to an operating mine.

DLTA changed its name from Golden Hope Mines to Delta Resources in July 2019. In October 2019 the Company signed an option agreement to acquire 100% interest in the Eureka Gold Discovery property in Ontario, renaming it the Delta-1 project (as the first project acquired under the new name). Shortly thereafter it signed an agreement to acquire 100% interest in the property named Delta-2. The Company also had the Bellechasse-Timmins project in Quebec, which it sold to Yorkton Ventures in 2022 for C$1.7 million, retaining a 1% NSR on the project.

The Delta-1 project is located in Thunder Bay, Ontario in the Shebandowan Greenstone Belt. Greenstone belts are composed of volcanic rock and interspersed with sedimentary rock. They typically contain high mineral content and are likely to contain high quantities of gold, copper, iron, zinc, silver and nickel. The project is located in the same geologic setting as Goldshore Resources' Moss Lake gold project, which is currently estimated to have 4.17 million ozs of gold at 1.1 gpt (open pit). Historically 42 holes were drilled to test for copper-nickel targets. The property had been dormant since 2003 (the price of gold was $300 - $400 back then).

DLTA began exploration activities on Delta-1 in 2020. Geochem surveying, sampling and mapping confirmed the presence of a gold-mineralized "halo." The 2021 drill program returned wide intercepts of economic-grade gold, similar to the Moss Lake deposit, located to the west of Delta-1 on the same geologic structure. The highlight assay showed 1.25 gpt Au over 18 meters. The 2022 drill program results drew investor attention. Visible gold was intercepted and all nine holes intersected the gold-bearing zone. Assays from the headline drill hole intercepted 14.8 gpt Au over 11.9 meters within a broader interval of 5.92 gpt Au over 31 meters. Keep in mind that the Delta-1 mineralization is near-surface, open-pit style with drilling to date going down only to 200 meters. This drill program gained the attention of potential strategic partners.

At the beginning of 2023, DLTA announced a 5,000 meter program. The Company continued to hit broad zones of near-surface visible gold and high-grade intercepts. 100 meter step-out holes to the east also encountered wide intervals of gold mineralization along with visible gold. The Company raised C$10 million through flow-through and standard units. Subsequently it acquired additional claims to expand the size of the property, announced a new 20,00 meter drill program and added a second drill.

The first drill results, though they looked good to me, disappointed the market. This where i think the opportunity lies to acquire "cheap" DLTA shares. The stock ran from 4 cents US$ in late 2022 to 41 cents by April 26, 2023. It then started selling off along with the rest of the sector, particularly juniors. It closed at 26 cents the day before the 1st drill results from the 20k drill program were announced but dropped down to 14 cents after the results were announced.

The Delta-2 project is located 35km southeast of the town of Chibougamau. Optioned in 2021 from Cartier Resources and fully-acquired in 2022, Delta-2 is a VMS formation with gold-copper mineralization. Recall that VMS deposits- volcanic massive sulphide ore - host polymetallic mineralization, typically copper, zinc, gold, silver and lead. They generally host moderate-sized, moderate-to-high grade deposits. Canada hosts several large VMS camps.

The 2021 exploration program produced a gold discovery in which two drill holes encountered two mineralized zones with visible gold identified. Additional drilling in 2022 encountered four areas of interest that included a gold-enriched target area, a copper-enriched target area and two zinc-enriched target areas.

I had an in-depth conversation with Andre Tessier, the CEO, who came to the Company in 2019 along with a change-over in upper management and the Board. Delta-1 was acquired from a prospector, who still has 1.75% NSR which can be acquired by the Company. The Company was attracted to Delta-1 because of the size of the geologic alteration package. The plan is to advance an open pit resource before spending the resources to explore the underground potential.

Drilling to date has focused on defining the overall "footprint" of mineralization and understanding the control structures and geometry of the mineralization and potential deposit. "Control structures" are the geologic attributes and hydrothermal alteration that control the formation of mineral-bearing veins. Understanding of the specific control structures of a mineralized area affects the understanding of the technical aspects of exploration and mining, including grade control, resource estimation, targeting, etc.

I asked about the big sell-off in the stock after the "game changer" holes described above from the 2022 drill program were released. At the start of the current drill progarm the Company announced that it was going to do 100 meter step-out holes to the east of the known mineralization to test a 200 meter, on-strike geophysical attribute (magnetic low) like the one that produced the existing assays. It sounds like retail piled into the shares on the assumption that the first step-out results would produce the fat assays from the 2022 drill program. Andre said the anticipation took on a life of its own.

The assays released apparently disappointed the market despite one assay that intercepted 1.79 gpt gold over 128.5 meters starting at 25.5 meters below the surface and 2.16 gpt gold over 97.5 meters starting at 25.5 meters below the surface. For an open pit configuration, these are home run holes. The market did not like holes further to the east that returned grades generally below 0.5 gpt - grades but that would be considered sufficiently economic in a Carlin trend project. We had a chuckle over that. But these are "first pass" holes testing the targets. Andre believes that the Company will hit higher grades in targeted areas with follow-up drilling.

With respect to the Delta-2 project, I asked why Cartier Resources was willing to sell the project. He said that Cartier has decided to sell ancillary projects in order to focus on advancing its 8.8 million gold resource Chimo Mine project into a mine. DLTA management has elevated Delta-1 as the flagship project and will put Delta-2 on the back burner. That said, the Company raised flow-through money in the last financing that needs to be spent on exploration activities by year-end and will use some of it to do some exploration drilling on Delta-2.

Bottom line - I need to stress that both Delta-1 and Delta-2 are very early stage exploration projects. The series of drill results at Delta-1 are very encouraging. The Company is convinced that Delta-1 hosts an economic deposit. The objective now is to define the scale and grade. The Company's game plan is to de-risk Delta-1 enough to attract a strategic acquirer to take it over the finish line with DLTA management possibly spinning-off Delta-2 and moving on to develop that project.

Andre said that the Company has several non-disclosure agreements with strategics who want access to data the room to monitor the project. I think Wesdome, Alamos and Agnico Eagle are potential acquirers. That said, it will take a strong, extended bull move in the sector before strategics move to acquire projects until they've become almost completely de-risked.

In my opinion, DLTA is worth using some high-risk/high-return capital for a potential 5-10 bagger. I believe the recent sell-off, which appears to have come from the retail momentum chasers, provided a good entry level to minimize the downside risk. While Andre said there's a seller from the last financing that stripped the warrants and is now selling the stock, a couple of DLTA's largest shareholders who want to own more shares are buying those shares and Coremark (the deal underwriter) makes sure that they get first look when the shares become available.

The biggest shareholders are 1832 Asset Management (owned by Scotiabank) and some big Quebec funds. Management and insiders own 9%, after taking C$1.4 million of the last $10 million capital raise. The Company has not spent much on promotion. When it does I believe the shares will attract a much wider base of shareholders.

There's 98.5 million primary shares, with 35 million warrants and 7.8 million stock options, for a total of 144 million fully-diluted shares. However 17.4 million of the warrants are struck too high to be considered relevant (40 to 63 cents C$, with the stock at 19 cents C$). Most of the stock options are in the money or near-money. For purposes of my valuation and potential upside analysis, I'm using 123.9 fully-diluted shares. At the current price this gives DLTA a US$17.3 million valuation.

Assuming we get a sustained rally that takes gold over $2,000 and silver into the high $20's, I think DLTA could double or triple quickly. Especially if more holes from the current drill program hit good grades. Forty-four holes from the current ongoing drill program have been completed with 23 reported so far. This means there will be a lot of potential positive news flow coming. I have started a position in my personal account (about a 1/3 of what I'd like to own) but have not put any in our fund yet (we have a lot of high-risk/high-return plays) but I intend to do so eventually.