

True North Gems

Major industry player signs three-year off-take

First off-take signed

Metals & mining

True North's binding agreement with major Asian gemstone polisher Chinastone, details a three-year commitment for the latter to purchase US\$7m (C\$9.9m) of Aappaluttoq stones per year for an initial three-year term. Stones will be sold at market prices, paid for solely in cash. This is a major step forwards for the company, and brings on-board a major player in the gemstone market. True North intends to develop this partnership to engage further buyers for its highly marketable and conflict-free pink sapphires and rubies. Consistency of supply is a unique selling point for the company and is underpinned by Aappaluttoq's mine plan being based on an NI43-101 compliant resource.

Year end	Revenue (C\$m)	PBT* (C\$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/13	0.0	(1.7)	(0.7)	0.0	N/A	N/A
12/14	0.0	(1.4)	(0.5)	0.0	N/A	N/A
12/15e	0.0	(5.2)	(1.1)	0.0	N/A	N/A
12/16e	48.8	35.0	7.3	0.0	2.2	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Deal satisfies 41% of 2016 break-even revenue

Production costs to extract and process gemstones are inherently low at Aappaluttoq due to its gemstones cropping-out at surface and the relatively simple nature of mining and processing gemstone material. Therefore, while this initial C\$9.9m per year deal constitutes 20% of our FY16 revenue forecast, it would also cover approximately 41% of True North's total production and corporate costs for 2016. One further deal of this magnitude would practically eliminate a need for additional funding in 2016. Note that if production and corporate G&A costs are maintained as per our forecasts and the C\$48.8m revenue target is achieved, True North's EBITDA margin would be 77%. If only C\$24m of revenue is achieved (the amount required for it to break even for the year), EBITDA margin reduces to 42%.

Chinastone aligned with True North's strategy

True North's new partner states on its website that it only deals in natural gemstones and does not buy treated material. This is sympathetic to True North's marketing of an Arctic natural source of pink sapphires and rubies, and in our opinion supports the cachet of selling stones from this unique Greenlandic source.

Valuation: Forecasts revised for forex

Our base case valuation uses True North's 18 March 2015 PFS on the Aappaluttoq deposit and we move our C\$/US\$ forex rate from 1.33 to 1.41. Considering this deal was announced to market on 28 January 2016, and Chinastone's size and pedigree, we consider True North is still capable of satisfying our C\$48.8m revenue target. Therefore, we revise our previous C\$0.37 per share base valuation to C\$0.41 per share. This section should be read in conjunction with our [December 2015 update](#), which details the company's complex financing structure.

1 February 2016

Price **C\$0.16**

Market cap **C\$49m**

C\$1.41/US\$

Net cash (C\$m) at 30 Sept 2015 3.3

Shares in issue 307.5m

Free float 88%

Code TGX

Primary exchange TSX-V

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 3.0 9.7 9.7

Rel (local) 8.9 20.8 27.2

52-week high/low C\$0.19 C\$0.10

Business description

True North Gems is developing its 85.4%-owned (65% on completion of the mine by its JV partner LNSG) and exploitation (mining) permitted Aappaluttoq ruby and pink sapphire mine in Greenland.

Next event

Further sales agreements H116

Analysts

Tom Hayes +44 (0)20 3077 5725

Charles Gibson +44 (0)20 3077 5724

mining@edisongroup.com

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Exhibit 1: Financial summary

	C\$000s	2013	2014	2015e	2016e
Year-end 31 December		IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue		0	0	0	48,801
Cost of Sales		0	0	(1,749)	(7,825)
Gross Profit		0	0	(1,749)	40,975
EBITDA		(1,593)	(1,222)	(5,239)	37,496
Operating Profit (before amort. and except.)		(1,593)	(1,222)	(5,239)	34,980
Intangible Amortisation		0	0	0	0
Exceptionals		0	0	0	0
Other		0	0	0	0
Operating Profit		(1,593)	(1,222)	(5,239)	34,980
Net Interest		(57)	(149)	10	15
Profit Before Tax (norm)		(1,650)	(1,371)	(5,229)	34,995
Profit Before Tax (FRS 3)		(1,650)	(1,371)	(5,229)	34,995
Tax		0	0	0	(841)
Profit After Tax (norm)		(1,650)	(1,371)	(5,229)	34,154
Profit After Tax (FRS 3)		(1,650)	(1,371)	(5,229)	34,154
Average Number of Shares Outstanding (m)		233.7	295.8	306.1	306.1
EPS - normalised (c)		(0.7)	(0.5)	(1.1)	7.3
EPS - normalised and fully diluted (c)		(0.7)	(0.5)	(1.1)	7.3
EPS - (IFRS) (c)		(0.7)	(0.5)	(1.1)	7.3
Dividend per share (c)		0.0	0.0	0.0	0.0
Gross Margin (%)					84.0
EBITDA Margin (%)					76.8
Operating Margin (before GW and except.) (%)					71.7
BALANCE SHEET					
Fixed Assets		24,467	27,988	55,637	66,460
Intangible Assets		0	0	0	0
Tangible Assets		24,467	27,988	55,637	66,460
Investments		0	0	0	0
Current Assets		729	2,343	8,357	27,990
Stocks		0	0	671	643
Debtors		18	35	0	4,011
Cash		271	1,989	7,367	23,017
Other		440	319	319	319
Current Liabilities		(1,390)	(1,346)	(939)	(1,520)
Creditors		(1,390)	(715)	(307)	(889)
Short term borrowings		0	(631)	(631)	(631)
Long Term Liabilities		(1,113)	(1,160)	(6,278)	(4,980)
Long term borrowings		(894)	(877)	(5,995)	(4,697)
Other long term liabilities		(219)	(283)	(283)	(283)
Net Assets		22,694	27,825	56,777	87,949
CASH FLOW					
Operating Cash Flow		(1,423)	(1,800)	(5,806)	34,094
Net Interest		(57)	(149)	10	15
Tax		0	0	0	(841)
Capex		(2,091)	(2,913)	(4,270)	(16,321)
Acquisitions/disposals		50	0	0	0
Financing		3,786	5,945	10,326	0
Dividends		0	0	0	0
Net Cash Flow		265	1,083	260	16,947
Opening net debt/(cash)		9	623	(481)	(741)
HP finance leases initiated		0	0	0	0
Other		(879)	21	0	0
Closing net debt/(cash)		623	(481)	(741)	(17,688)

Source: Company accounts, Edison Investment Research

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