Carlisle Goldfields – Snackfood for a new Alpha Predator

In the absence of anything exciting in the gold price arena (and the absence of any prospect thereof) the chief impetus for movement is takeover or merger rumours and so far this year that has been quite a bit of movement to stir the pulse of stocks that otherwise are merely waiting out the extended drought in mine financing. Carlisle Goldfields (TSX:CGJ | OTCQX:CGJCF) has received a kicker in recent weeks with the announcement of the merger of its largest shareholder, AuRico, with Alamos Gold. In the wake of meeting with the management in London last week, I shall look here at some of the ramifications.

The Gold Elephants' Mating Dance

Back in the middle of the month it was revealed that Alamos Gold (TSX:AGI | NYSE:AGI) had agreed a merger with AuRico Gold (TSX:AUQ | NYSE:AUQ) to turn two smaller mid-tier companies into a large mid-tier gold producer. The main assets are two long mine-life, cash flow-generating gold mines: AuRico's Young-Davidson mine in Ontario, Canada, and Alamos' Mulatos mine in Sonora, Mexico. The transaction was styled as a merger of equals with a transaction equity value of approximately US$1.5 billion. There is also going to be a SpinCo with various leftover pieces embedded in it. Interestingly the partners viewed the pre-existing AuRico stake in Carlisle as NOT one of the odd-and-sods and decided it would be kept as the potential pipeline for the main company.

Former Alamos and AuRico shareholders will each own approximately 50% of MergeCo (named Alamos Gold Inc.) and the shares of the SpinCo will be doled out pro-rata to existing shareholders of both companies. The deal is expected to close in June of this year.

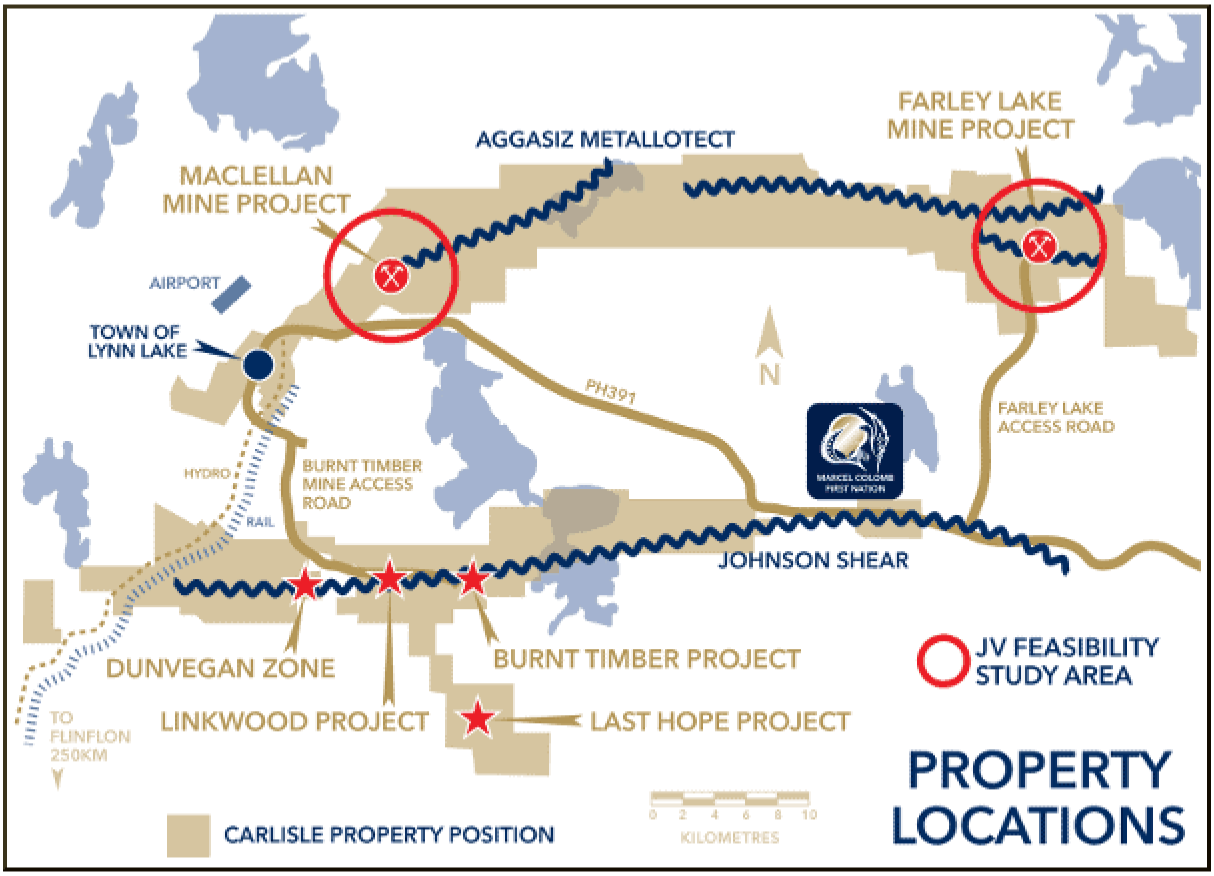
The new entity will be no slouch in the gold producing rankings as it is expected to produce 375-425,000 oz of gold in 2015 in Mexico and Canada with the potential to grow organically to over 700,000 oz of gold annually. The development portfolio is anchored by quality, low-cost projects in Turkey as well as three projects in North America (Esperanza, Lynn Lake and Quartz Mountain). The company will also be cashed to the gills, as well as having cashflow, with a pro-forma cash position of US$427 million and net cash of US$94 million.

Of little relevance to Carlisle is the SpinCo, which will walk away with the Kemess project, a 1.5% NSR on the Young-Davidson mine, a 2% NSR on the Fosterville mine, a 1% NSR on the Stawell mine and US$20 million in cash.

From the Carlisle standpoint the most important thing (after not being chucked in the SpinCo hopper) is that the current representative of AuRico on the Carlisle board, Peter MacPhail (currently COO of AuRico) is going to segue over into the same role of COO at the merged group.

Why Carlisle Makes the Cut

To refresh the memory, Carlisle Goldfields is focused on development of its Lynn Lake Gold Camp in Lynn Lake, Manitoba. The company has NI 43-101 compliant mineral resource estimates on five deposits within its Lynn Lake Gold Camp, four of which form the basis for the December, 2013 PEA (Farley Lake, MacLellan, Burnt Timber, and Linkwood).



The main focus is the past-producing Maclellan Mine which has road access, power line, a head-frame, hoist house and shaft to 448 metres (with five levels), ramp access from surface to 420 metres below, maintenance building, core shack, vent raise, mine water settling ponds, and other mine infrastructure. The Maclellan Mine started production in July

1986 and closed in October 1989. Reported production amounted to 969,680 tonnes grading 5.36 g/t Au. Production was derived from four main zones. During mining, the deposit was accessible from surface by the central shaft and a ramp that passes through the Nisku Zone on the east side of the property. The shaft was used primarily for the hoisting of ore and limited movement of personnel. The ramp system was used for moving personnel, equipment, and supplies throughout the mine. Initially mining was by cut-and-fill methods. Difficulty in attaining production targets led to a change to long-hole mining but the increased production and lower mining costs were offset by lower mill-heads due to increased dilution. All of this has to be taken in the context that the gold price back then was a mere fraction of its current levels.

The Original AuRico Deal

The symbiotic relationship with AuRico dates back to November of last year when Carlisle announced that AuRIco was subscribing for 70.6 million common shares of Carlisle at a price of CAD$0.08 per share, for total consideration of approximately CAD$5.6mn This represented approximately 19.9% of the issued and outstanding common shares of Carlisle on a non-diluted basis.

At the same time, AuRico entered into a joint venture agreement with respect to the Lynn Lake Gold Camp under which AuRico acquired a 25% interest for an initial cash contribution of CAD$5mn, with the option to earn up to an additional 35% interest by funding CAD$20mn on the Project over a three-year period and delivering a feasibility study within that time period.

The PEA – Opting for Open Pit

Despite Maclellan having the entire underground infrastructure, Carlisle is contemplating working this deposit as an open pit. With this as the strategy, the company announced in February of last year, its revised PEA, prepared by Tetratech, for Maclellan and the neighbouring Farley mine. The results included a pre-tax Net Present Value at a 5% discount rate of $411mn with a pre-tax Internal Rate of Return of 34%. Initial capital costs came in at $185mn (including $35mn in contingencies). This was based on a conservative US$1100 gold price revenue model. The PEA envisaged:

- LOM Au production of 1.74 million oz and 1.59 million oz of silver
- LOM average head grade of 2.2 g/t Au

There will be a central milling facility with an initial milling capacity of 3,750 tpd in years 1-4 and ramping to full capacity of 7,500 tpd in year 5 of a 12-year mine.

Fortunately the company took the message from the tough financing environment and rejigged the PEA so that it came in with an initial capital cost approximately $90mn lower than that of the original 10,000 tpd PEA. The next phase is the expensive one of undertaking the feasibility study but at least the burden of that falls upon AuRico (and now Alamos).

With the PEA at least the Lynn Lake project has been “right-sized” in an age of gargantuan gold mines that struggle for profitability. It will be interesting to see whether the new owners (if Alamos move to bring Carlisle into the fold) will persist with the idea that Maclellan be pursued as an open pit (with the commensurate heavy stripping ratio) when all the underground is still in place. The Young-Davidson mine after all is an underground mine. Reviving Maclellan becomes more plug and play if an underground option is chosen. The interesting question is then raised as to whether the partners might not decide to chance tack on mine design earlier rather than later rather than waste time and money on a FS for an open pit when ultimately another course might be preferred by the bigger partner.

Conclusion

Being signaled as the favoured project in the pipeline of a newly-minted miner of size is not a bad thing in this day and age. The stake that Alamos has in Carlisle positions them to move in for the kill when the various triggers have been tripped and frankly, even at a takeout price of $100mn or thereabouts, Carlisle is small change for the new Alamos.

The mine-life at Lynn Lake, even with the current resource, is long and with lots of extra territory to explore and expand operations. Carlisle, either standalone or subsumed in Alamos, could have a whole mining district under its aegis.

The prospect of being taken out also raises the question of whether Carlisle should start looking for a further project itself so it too can create a SpinCo in the event of its takeout by Alamos or in the event that Alamos just decides to acquire the property rather than the company. This would leave Carlisle mightily cashed up. Abraham Drost does not look like a man ready to hang up his saddle. A cashed up Carlisle might become something of a predator itself..