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# NORTH AMERICAN GOLD MINING STOCKS

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## CONTINENTAL GOLD CORP.

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| Traded NASDAQ (CNTVF) | 1989 Price Range: $9.25 High, $2.50 Low |
| Price 3/2/90: $7.63 | Shares Outstanding: 7,109,323 |
| Hotline Recommendation 2/18/90: $7.63 | Quality Rating "B" |

Measure it any way you want, Continental Gold's Mt. Milligan gold/copper deposit makes it one of the more undervalued junior gold mining firms in North America today! Whether you compare the company's market value with annual projected gold production, ore reserves, operating cost per ounce, discounted present value, or projected price/cash flow, Continental Gold appears to be a substantially undervalued stock. Sure, there are added risks attached to any pre—start up mining company. The share price is in our opinion substantially undervalued at present because 30% joint—venture partner BP Canada is seen by many investment professionals as having "added a fly in the ointment" by introducing a lawsuit aimed at obtaining all of Continental's 70% interest in Mt. Milligan (more about litigation later). However, it is our view, that these added risks provide the adventuresome investor who buys Continental at its current price level, the likely opportunity of doubling, tripling or quadrupling his investment over the next year!

By anyone's definition, Mt. Milligan can only be termed a "world class" mineral deposit. At this stage of the company's development it looks like this project will produce at least 300,000 ounces of gold and 64 million pounds of copper per year. It is indeed possible that the project will produce closer to 400,000 ounces of gold and 100 million pounds of copper annually depending on final feasibility studies. Incredible as it seems, with an 80¢ copper credit factored in, the operating cost of producing an ounce of gold is expected to be somewhere between $30 and $40/oz! By at least one account (reportedly from a major mining firm), the Mt. Milligan property has over 450 million tons of ore already delineated, which if true, will enable this project to produce at the above noted levels for approximately 35 years! Whatever actual reserves are, it appears likely that a very large, long life copper/gold production facility will become a reality at Mt. Milligan during the next two or three years. As the market wakes up to this fact, Continental's stock should leap straight off the charts!

Mt. Milligan Discovery
Fort St. James, British Columbia

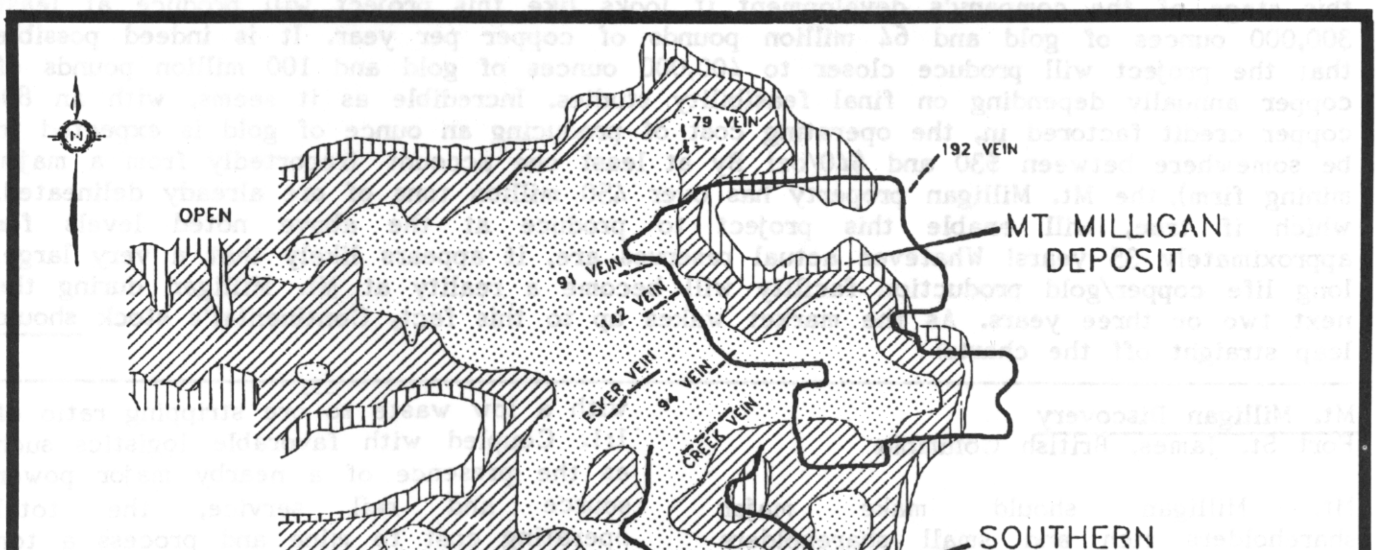
Mt. Milligan should make major shareholders rich and small shareholders very happy. This project which has over 450 million tons of low grade copper and gold reserves looks like it should become one of North America's larger gold mines and most certainly its lowest cost gold producer by a large margin! The company's claims encompass a 42 sq. mile area 50 miles northeast of Fort St. James and 150 miles north of Prince George, B.C. The geometry of the deposit delineated thus far should will allow for open pit mining with a low waste to ore stripping ratio of 1:1. Coupled with favorable logistics such as the presence of a nearby major power source and rail service, the total operating cost to mine and process a ton of ore is expected to amount to around $6.78 per ton. Assuming copper is priced at $1.00/lb. (it is now around the $1.15 level), a ton of ore will carry a copper value of $4.92. With an average gold grade of 0.025 oz/ton and a $400 gold price, the gold value per ton of ore would amount to $10.00, thereby rendering an operating cash flow of $8.14 per ton.

Revenue/cost estimates were presented in an engineering study of the project by the very reputable Wright Engineers Limited dated April 13, 1989 and were based on a delineated tonnage of only 200 million tons. Continental has now commenced a $7.1 million feasibility and government permitting program for the project. Given that substantially greater tonnage figures have already been established, the Wright Engineers report may prove to be ultra conservative in terms of future cash flow projections. Nonetheless, Wright's 200-million ton report provides a valid starting point and as such serves to show just how undervalued Continental's shares actually are. Given a 200-million ton deposit, Wright Engineers projected an annual operating rate of 13 million tons. Applying the above noted revenue/cost numbers, the project would generate an operating profit of $105,814,000 per year. Continental's 70% interest would sum up to an annual profit of $74 million.

To get an idea of the magnitude of this project and to see that significant potential for discovering additional gold reserves exists at the Mt. Milligan Project, we call your attention to Exhibit I. The 200 million ton reserve was delineated from the area enclosed within the solid black lines known as the Mt. Milligan Deposit. This tonnage estimate does not include potential reserves from Southern Star Deposit or other areas outside the Mt. Milligan Deposit area. The Mt. Milligan Deposit which measures approximately 1,100 meters north and south by approximately 1,200 meters east and west compares to the entire claim area of 42-square miles. Much of the 42-square mile claim area, although not pictured in exhibit I, is considered to provide excellent potential for the discovery of additional mineralization based on airborne geophysical survey work and geological mapping. A minimum of nine other anomalous intrusive center targets adjacent to a large batholith size pluton have been spotted on the larger claim area.

For the time being however, the company

EXHIBIT I



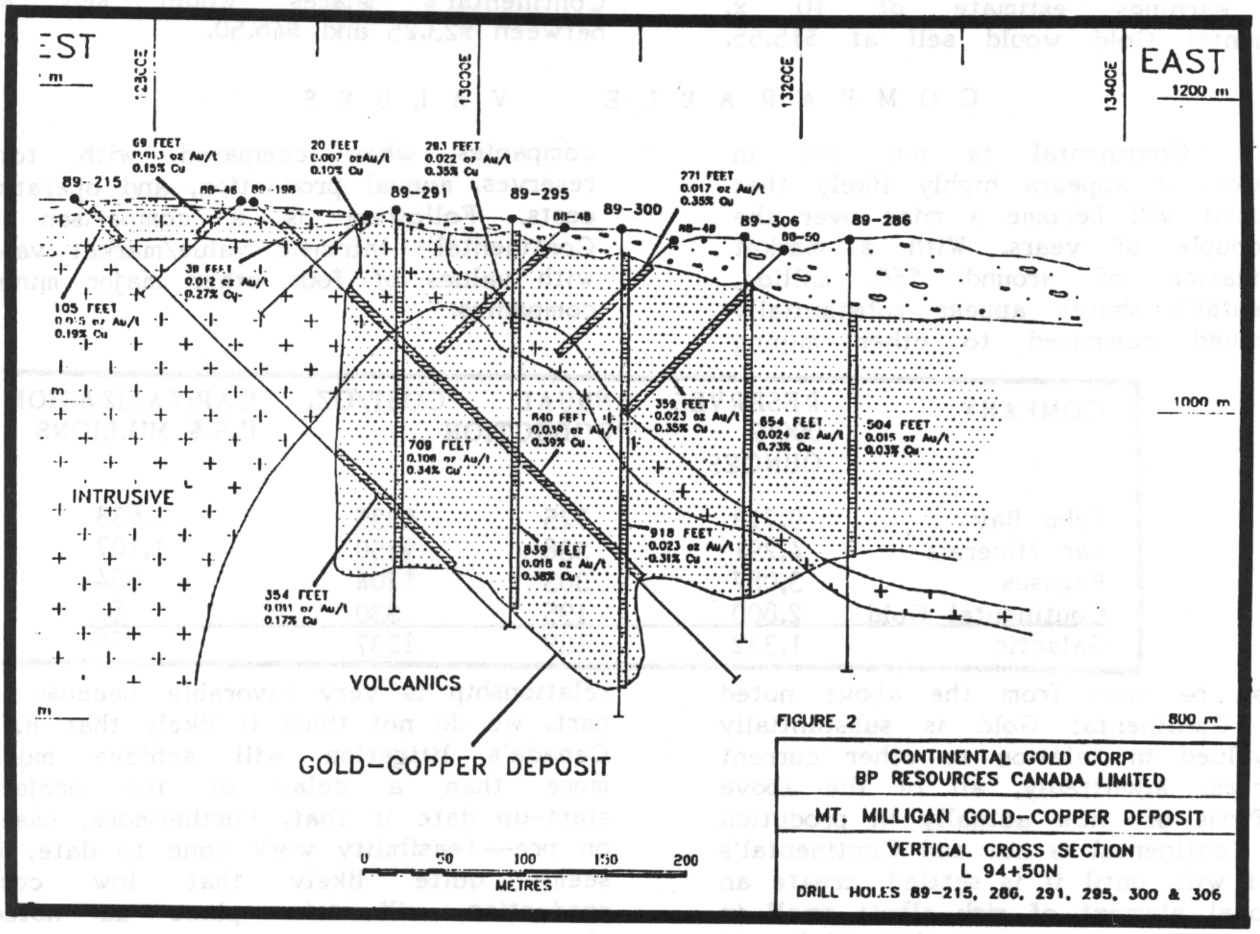
more than has its hands full with exploration and development of Milligan, Southern Star and other areas immediately surrounding those two deposits. For example, the various veins radiating out from the circular area starting with vein 192 to the north east and ending with the Creek Vein striking in a southwest direction from the enclosed area appear to contain significant high grade gold mineralization. Most junior mining companies would be happy to have but one of these veins because it appears as though each could represent a small but profitable deposit. So far the only significant work done on these veins has been on the Esker Vein and the Creek Vein. However with an estimated width of 15 ft. and a gold grade of 0.30 oz. gold/ton in these veins, it is clear that significantly more gold and copper waits to be found directly outside the Mt. Milligan Deposit area pictured in Exhibit I. and shown as high, medium and low grade disseminated sulphide material. Indeed it would appear possible that ultimate reserves may be even greater than the 450 million tons already mentioned, from the pictured area.

Exhibit II, which represents a vertical cross section of the enclosed area looking east, helps to illustrate the favorable geometry of the deposit. Of significance is the substantial depth of the vertical drill holes, which contain continuous gold/copper mineralization as well as the relatively shallow overburden over much of the deposit (average 50 ft.). If we were to show other cross-sections of the enclosed area, a similar picture would appear. With a deposit of this size, very large, low cost bulk tonnage mining methods can take place.

## Profit Potential for Continental

Capital costs of a 13 million ton per year project are estimated at around \$190 million. Continental's share of this expense would amount to \$133 million. Based on Continental's current share

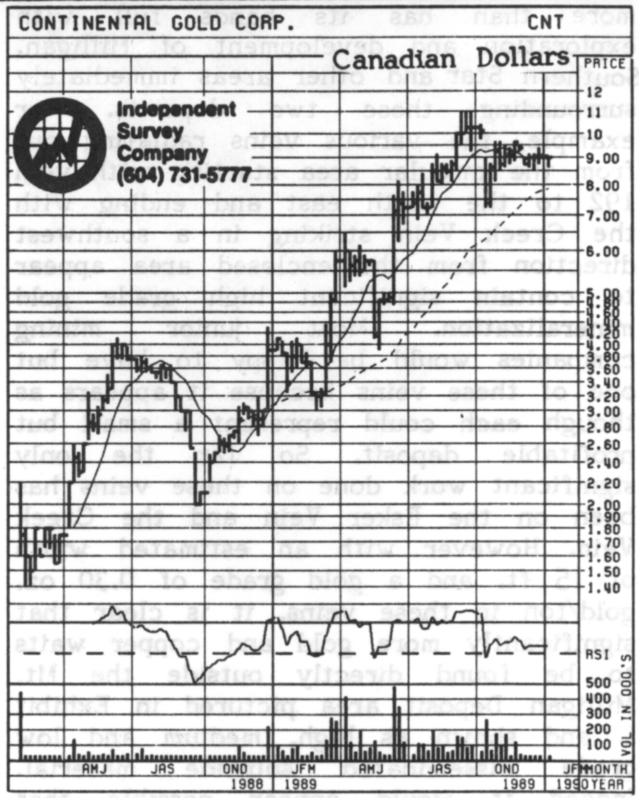
# EXHIBIT II



price, it would need to issue approximately 17.7 million more shares to finance its portion of capital expenditure from this point onward should it use only equity financing. Due to this substantial shareholder dilution, we would expect Continental to minimize straight equity financing. Upon receipt of a bankable feasibility study, we anticipate a combination of debt/gold loan financing to be used to get this project into production.

Based on the above noted 200 million ton project assumptions, the company will have had its initial investment returned after approximately 2 years at which time its tax loss cary--forward would be used up. As a result, Continental's share of federal, provincial and mining taxes is expected to total around $34.4 million per year, leaving the company with total annual cash flows of $32.6 million.

Assuming for the moment that Continental financed its way into production solely through equity, it would have approximately 25 million shares outstanding. Based on a conservative price earnings estimate of 10 x, Continental Gold would sell at $15.55.




More commonly, established gold mining firms sell at a multiple of between 15 and 30 times cash flow, in which event Continental's shares would sell at between $23.25 and $46.50.

## C O M P A R A B L E   V A L U E S

Although Continental is not yet in production, it appears highly likely that its deposit will become a mine over the next couple of years. With a market capitalization of around $50 million, Continental's shares appear substantially undervalued compared to other mining companies when compared with total reserves, annual production, and operating costs. Following is a comparison of Continental's intrinsic value/market value with values of four other major mining companies:

| COMPANY | RESERVES 000'S OUNCES | ANNUAL PRODUCTION | COST/OZ. | CAPITALIZATION U.S.$ MILLIONS |
|---|---|---|---|---|
| Echo Bay | 9,712 | 725 | $235 | 1,633 |
| Lac Minerals | 4,291 | 338 | $250 | 1,107 |
| Pegasus | 3,087 | 303 | $204 | 334 |
| Continental Gold | 2,800 | 195 | $30 | 52 |
| Galactic | 1,332 | 139 | $237 | 136 |

As can be seen from the above noted chart, Continental Gold is substantially undervalued in relation to other current producers. Admittedly, all of the above gold firms are now actually in prodution while Continental is not and Continental's lawsuit will, until it is settled, create an additional element of risk albeit small in our opinion. In our view, the risk/return relationship is very favorable because in part, we do not think it likely that B.P. Canada's litigation will achieve much more than a delay of the project start-up date if that. Furthermore, based on pre— feasibility work done to date, it seems quite likely that low cost production will take place as noted above.

## Gold Loan Financing

From the shareholders' point of view, the best means of financing this project would be through a gold loan. Based on the above noted revenue/cost assumptions, the project should pay back the initial investment in just under two years. Given a capital expenditure of $190 million, Continental and its joint-venture partner could finance capital expenditure by borrowing 475,000 ounces of gold and selling the proceeds in the market at $400. Given that 475,000 ounces is a relatively small portion of total reserves (perhaps over 5 million ounces of gold) and that the project should be a very low cost operation, it is your editor's opinion that Continental should be able to secure gold loan financing on highly favorable terms.

For Continental's current shareholders, a gold loan would be fantastic because the above noted cash flows for their company would be divided by 7.5 million rather than 25.5 million. Instead of annual cash flows of $1.55, they would realize per share cash flows of $5.27. In this event, a price/cash flow projection of 10 x would take Continental's shares to $52.27. At 30 times cash flow, Continental's shares would sell at an astounding $158 per share!! And remember, we are not counting on anything other than gold and copper prices slightly below current prices!

## The Lawsuit

From where we sit in New York, it appears to us that the lawsuit launched by B.P. is a move to reduce embarassement and blame for letting a junior mining firm beat it to the discovery. Essentially, what we understand B.P. to allege is that Continental's amalgamation with United Lincoln in March 1989 gives rise to a first right of refusal in favour of BP to acquire all of the interest in the Mt. Milligan property held by United Lincoln, namely 69.84%. It should be noted that six weeks prior to the amalgamation BP was provided with all documentation relating to the Continental Gold/United Lincoln amalgamation including those aspects of the procedural step which BP has now taken issue with. During this period BP raised no complaints, issues or objections and for six months after the amalgamation during which time it continued to act in accordance with the joint venture terms before raising a complaint. It is our belief that as the project began to develop into a world-class mine, embarrassed management at BP sought to save their corporate skins by launching a lawsuit. To do less would be admitting a big mistake and that could hurt someone's carreer badly.

Assuming Continental is successful in defending itself in this suit (we expect it will be), Continental can be expected to countersue BP. The company has alleged that the actions taken by BP thus far have resulted in its losing a $15 million line of credit and that it has caused a major Canadian mining company to suspend discussions with the senior officers of Continental relating to a proposed offer for all the outstanding shares of Continental Gold Corp. at a substantial premium over the market price at the time of around Can $11.

## Take—over Possibilities

We understand that a number of major North American gold and copper mining companies are not only talking to Continental but also spending tidy sums of their own money to study the Mt. Milligan project. During the past ten years, major mining companies have not explored for copper because the copper price, until just recently was very low. With gold prices staying considerably above the cost of mining many deposits during that time frame, most exploration effort has been directed toward gold discoveries. As a result, few new copper mines have opened during recent years while other major mines are near the end of their lives. Mt. Milligan could provide substantial copper production for a major Canadian or U.S. copper producing company for many years into the future.

From a gold mining company's view point, where else can you find a project that will enable production of gold at $30 or $40 per ounce of gold? It seems to us **that if there is any justice in the world, Continental shareholders should be the beneficiaries of a bidding war amongst most of North American's major gold and copper mining companies.** One likely major company interested in Mt. Milligan is Rio Algom which has been buying shares of Continental Gold. At last report, Rio held 628,053 shares or 8.6% of Continental Gold. Furthermore, we understand that numerous other major mining companies (mostly Canadian) have not only expressed an interest in obtaining Continental's shares but also have been spending substantial sums of money to "study" the Mt. Milligan project. This fact suggests to us that 1) There will be competition for the project and 2) They do not believe that BP Canada will win their lawsuit.

With regard to a bidding war, our fear is two-fold: 1) A true all out takeover battle will not result and 2) Old time shareholders of Continental having purchased their shares at substantially lower prices may be satisfied with a far less than optimum sale price. With a potential loss in court old time shareholders may be satisfied to accept "a bird in hand." In that event, investors who buy the stock now may have to be satisfied with a price of between say $10 and $15. In our opinion, that would not be a fair deal for Continental shareholders.

The trump card we hope the company will play would be that of exercising its option to "go it alone." Given the world class nature of this deposit, Continental with Robert Hunter at the helm would in our view, attract additional quality talent as required to run the project efficiently.

SUMMARY

There is little doubt in our minds that BP Canada's legal action against Continental has hurt its stock significantly. Although we do not expect Continental to lose its lawsuit, if the B.C. court rules in favor of BP, Continental's share price would certainly fall substantially lower.

It is our view that Continental will emerge from the lawsuit unscathed when a British Columbia court reviews the case in November of this year. By that time or prior to it, Continental's shares should run substantially higher either as a result of a takeover or from a favorable resolution (from Continental's viewpoint). **When the legal smoke clears we believe that Continental will in retrospect, appear to have been one of the most obvious " I should have bought" junior gold stocks in years. We recommend that all but the most risk averse subscribers buy Continental at current levels and sell 1/2 when the stock doubles. At that time we will advise whether to hold or sell your remaining 1/2.**

For additional information contact the company at: Suite 1020 - 800 West Pender Street, Vancouver, B.C., Canada V6C 2V6. Telephone: (604) 684-6365. We also highly recommend that you call geologist and stockbroker Steve Azadian at Advest, (800) 635-8887 or (516) 232-3900.

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