

July 12, 2021

CERRADO GOLD (CERT: TSXV)

BUSINESS DESCRIPTION

Cerrado Gold is a Toronto-based mining and exploration company with an expanding portfolio of precious metal assets in South America. The company owns and operates Minera Don Nicolas (MDN), a newly producing gold and silver mine in Argentina. The mine is located in a prolific mining belt that includes mines owned by large global players AngloGold, Newmont and Yamana, and is being explored for further expansion. It also owns Monte do Carmo (MDC) in Brazil, a gold mine in the exploration and development stage. Management expects these two assets to transform the company into a mid-tier gold producer.

Cerrado was founded in 2017 on the basis of the MDC opportunity in Brazil, and acquired the newly producing MDN mine in March 2020. The company went public in 1Q21. Cerrado's strategy is to generate cash flow from the MDN mine in Argentina that will support its exploration efforts at both sites. In 1Q21, the company boosted gold production by 45% from the prior quarter and lowered production costs despite the impact of COVID-19 in Argentina, which resulted in lost operating days. Because of the pandemic's impact on the ramp up in production and costs, management expects production of 45,000 ounces at a cost of \$1,100 per ounce, and free cash flow of \$10-15 million in 2021.

By the end of 2021, the company expects run-rate production of 55,000 ounces from the conventional MDN operation, and an additional 30,000 ounces from a heap-leach operation, which uses a low-cost process to extract lower-grade ores from their source mineral. It expects these operations to generate \$50 million in annual free cash flow, with \$35 million from conventional operations and \$15 million from the heap-leach operation, both assuming an average gold price of \$1,800 per ounce. Including projected annual production of 150,000-200,000 ounces from MDC, Cerrado sees the potential for run-rate production of up to 285,000 ounces by the end of 2024 — close to the threshold of 300,000 ounces for mid-tier producers and implying more than 400% growth between 2021 and 2024.

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KEY STATISTICS

Key Stock Statistics

Recent price (7/8/21, CAD)	1.24
52 week high/low (CAD)	1.76 - 0.93
Shares outstanding (M)	84
Market cap (M, CAD)	104.2
Dividend	Nil
Yield	Nil

Sector Overview

Sector	Materials
Sector % of S&P 500	2.8%

Financials (\$M)

Cash & Mkt Securities	14.0
Debt	8.0
Working Capital (\$M)	0.6
Current Ratio	1.0
Total Debt/Equity (%)	65.0%
Payout ratio	NM
Revenue (M) TTM	32.2
Net Income (M) TTM	NM
Net Margin	NM

Risk

Beta	NA
Inst. ownership	5%

Valuation

P/E forward EPS	NA
Price/Sales (TTM)	3.2
Price/Book (TTM)	5.4

Top Holders

Franklin Templeton Investment Funds

Management

CEO	Mr. Mark Brennan
President	Mr. Cliff Hale-Sanders
COO	Mr. Kurt Menchen
Company website	www.cerradogold.com

PRICE CHART



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Cerrado is aggressively exploring to expand its total resource footprint. In 2019, the company had 813,000 ounces of inferred resource at the MDC site in Brazil. Its current resource profile is 1.725 million ounces, divided nearly evenly between the two sites. By the end of 2021, Cerrado expects to identify 3.3-4.0 million ounces of gold, with 60%-65% coming from the MDC site in Brazil. It also expects to reach 5 million ounces of resource by 2024.

As noted above, the MDC site in Brazil was the basis for the formation of Cerrado Gold. Due diligence on the site confirmed the initial outlook for 5-10 million ounces. The site consists of a primary gold deposit of 2.0-2.5 million ounces, with several satellite deposits. Following the initial inferred classification of 813,000 ounces, Cerrado conducted a preliminary economic assessment (PEA), which yielded a robust after-tax net present value (NPV) of \$430 million using a 5% discount rate and an internal rate of return of 76%. The analysis assumed a gold price of \$1,550 per ounce. Importantly, the analysis suggested a production cost of less than \$500 per ounce, in the lowest 5% of global gold mines. By comparison, Cerrado looks for higher production costs of approximately \$1000 per ounce at MDN in Argentina, but still expects the associated free cash flow to be substantial. In Brazil, Cerrado is updating its mineral resource estimate to reflect its recent drilling programs. This will inform a new and expanded PEA, which will be followed by a more robust feasibility study, likely in the second half of 2022, on the larger resource estimate.

Cerrado Gold expects to begin construction on the MDC site in 2023, with first production in late 2024. The company expects the mine to produce 150,000 high-value ounces of gold annually, and to become larger than the MDN mine. We expect the production schedule to vary based on the findings of the drilling program and the revised resource estimate.

The company's exploration activities in Argentina are expected to expand the estimated resource from a current 900,000 ounces to 1.3-1.5 million ounces in the second half of 2021. Management has identified multiple high-priority targets on the site that have seen only limited exploration under previous ownership. The site is expected to develop high-grade gold that can be brought into production quickly. Importantly, exploration at the Argentina site has not yet progressed to underground drilling and has been limited to extracting gold from the open pit area. As such, we view the Argentina project as being in the discovery phase, despite producing the initially identified resource, with prospects for future growth. For reference, AngloGold, a large player in the region, recently cited a total resource of 8 million ounces at its site, well above the 2 million ounces initially identified during the exploration of the site's open pit.

COMPETITIVE ADVANTAGE

Cerrado's executive team has a record of success in managing mineral projects in South America from early-stage exploration to mine development and production. Its leadership and investor teams have worked together on multiple projects, including Desert Sun Mining, which, after a significant resource expansion, was sold to Yamana. Management's experience working with mining industry leaders throughout South America has provided the company with new opportunities, such as the MDN mine in Argentina. MDC was presented to the company by founders of Belo Sun Mining, a Brazilian company with a market cap of approximately \$300 million and whose partners' company is Cerrado's largest shareholder.

In our view, progress at the MDN mine in Argentina highlights the executional capabilities of Cerrado's management team. Since its acquisition by Cerrado in early 2020, the mine has significantly increased production, as evidenced by its strong 1Q21 results. Management is currently targeting 45,000-55,000 ounces of production at MDN in the first full year under its control, up from 25,000 ounces previously. The company is using strategic drilling to expand the resource at MDN, underscoring management's ability to maximize production while also generating strong free cash flow that can support future exploration. We expect these expansion efforts to boost investor interest in Cerrado, which went public in 1Q21.

Lastly, we note that both the MDC and MDN projects benefit from favorable topography and strong local infrastructure. In Brazil, Monte do Carmo has access to reliable power lines, water supplies, and skilled labor, and is located near a national airport. In addition, the project has obtained permits covering 58,000 hectares (nearly 150,000 acres). In Argentina, MDN is accessible from nearby ports, and although airport and highway transportation are not in the immediate vicinity, a gas pipeline runs parallel to the highway and groundwater is readily available.

ANALYST COMMENTARY: EARNINGS

In 1Q21, Cerrado posted a net loss of \$5.7 million or \$0.10 per share. However, in our view, this loss is less significant than the company's strong increase in gold production, which rose 45% from the prior quarter, and declining per ounce production costs. We also believe that Cerrado's current market cap of \$104 million CAD (\$83 million USD), using Cerrado's fully diluted share count of 84 million, does not adequately reflect current production and expected free cash flow at the Argentina mine, or the strong prospects of the MDC mine in Brazil (whose initial PEA in 2020 suggested an after-tax NPV of \$430 million, using a 5% discount rate). We also expect the projected

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PEER COMPARISON

Company	Ticker	Recent Price (\$)	52-Week High (\$)	52-Week Low (\$)	Mkt. Cap (\$MIL)	1-yr Price Change (%)	1-yr Rev Growth (%)	1 YR EPS Growth (%)	P/E Ratio	Beta	Yield (%)
CERRADO GOLD	TSXV: CERT	1.24*	1.76*	0.93*	104*	1	NM	NM	NM	NA	NA
BELO SUN MINING CORP.	TSX: BSX	0.57*	1.44*	0.57*	250*	-28	NM	NM	NM	0.65	NA
CORVUS GOLD INC.	TSX: KOR	3.26*	4.26*	2.17*	414*	3	NM	NM	NM	1.52	NA
CALIBRE MINING CORP.	TSX: CXB	1.61*	2.80*	1.36*	546*	1	320	NM	6.8	2.92	NA

* Canadian Dollars (CAD)

value of MDC to rise further after the company conducts a new PEA. Over time, we expect higher production and updated resource reports to drive increased investor interest in Cerrado, and narrow the gap between the company's market valuation and NPV.

Importantly, we expect the new PEA for the Brazil project to enable Cerrado to secure financing on favorable terms. The development of this mine will be capital-intensive, requiring investment of \$130-\$150 million. However, if the new PEA indicates an internal rate of return in line with the 76% projected in the initial report, Cerrado should be able to choose among various financing structures that would not require a dilutive equity offering. We expect this to be the company's preferred route. We note that the management team holds a roughly 35% ownership stake, and did not use equity to fund the MDN acquisition.

MANAGEMENT

Mark Brennan is Cerrado Gold's CEO and co-chairman. He is a founding partner and executive chairman of Ascendant Resources Inc. and executive chairman of Vanadium One Iron Corp., and has more than 30 years of financial and operating experience in the Americas and Europe. Mr. Brennan most recently served as president and CEO of

Sierra Metals Inc., a major zinc-lead-silver-copper mining company with operations in Peru and Mexico. Prior to that, he was the president and CEO of Largo Resources Ltd., and a founder of several resource companies, including Desert Sun Mining, Brasoil Corp., James Bay Resources, Morumbi Oil and Gas, and Admiral Bay Resources.

RECENT DEVELOPMENTS

In June 2021, Cerrado appointed Dr. Sergio Gelcich, PGEO, as VP of Exploration, succeeding Robert (Andy) Campbell, who has retired from day-to-day operations but remains a company director. Dr. Gelcich is a senior exploration geologist with more than 20 years of industry experience. He was most recently exploration director at Hudbay Minerals. Dr. Gelcich is a member of the Association of Professional Geoscientists Ontario (APGO) and serves as Cerrado's "Qualified Person," as defined in National Instrument 43-101.

In May 2021, Cerrado reported 1Q21 results, which included a 45% sequential increase in gold production despite challenges from the pandemic. The results reflected successful exploration efforts in both Brazil and Argentina. The company also substantially lowered production costs over the course of the quarter, and remains on track to meet its production, cost, and free cash flow targets for 2021.

Steve Silver

INCOME STATEMENT

Growth Analysis (\$MIL, CAD)	2019	2020	Q1 2021
Metal Sales	0.0	32.2	11.2
Gross Profit	0.0	32.2	11.2
Production Costs	2.4	24.9	9.4
Sales Expenses and Royalties	0.0	4.1	1.0
Operating Income	-2.9	0.7	0.0
Finance Items	0.0	4.5	-1.4
Pretax Income	-2.9	-11.9	-5.2
Tax Rate (%)	NA	6	9
Net income	-2.9	-12.6	-5.7
Diluted Shares	39.6	44.8	58.5
EPS	-0.07	-0.28	-0.10
Dividend	NA	NA	NA
Growth Rates (%)			
Revenue	NA	NA	NA
Operating Income	NA	NA	NA
Net Income	NA	NA	NA
EPS	NA	NA	NA
Valuation Analysis			
Price (\$): High	NA	NA	NA
Price (\$):Low	NA	NA	NA
PE: High	NA	NA	NA
PE: Low	NA	NA	NA
PS: High	NA	NA	NA
PS: Low	NA	NA	NA
Yield: High	NA	NA	NA
Yield: Low	NA	NA	NA
Financial & Risk Analysis (\$MIL, CAD)			
Cash	0.0	6.6	14.0
Working Capital	-4.4	-2.0	0.6
Current Ratio	0.0	0.9	1.0
LTDebt/Equity (%)	8	51	65
Total Debt/Equity (%)	0	NA	NA
Ratio Analysis			
Gross Profit Margin	NM	22.8%	16.0%
Operating Margin	NM	NM	NM
Net Margin	NM	NM	NM
Return on Assets (%)	NA	NA	NA
Return on Equity (%)	NA	NA	NA
Op Inc/Int Exp	NA	NA	NA
Div Payout	NA	NA	NA

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