

Ticker: SVM AU

Market cap: A\$140m

RECOMMENDATION (unc): BUY

Net cash: A\$2m

Price: A\$0.38/sh

TARGET PRICE (up): A\$0.56/sh

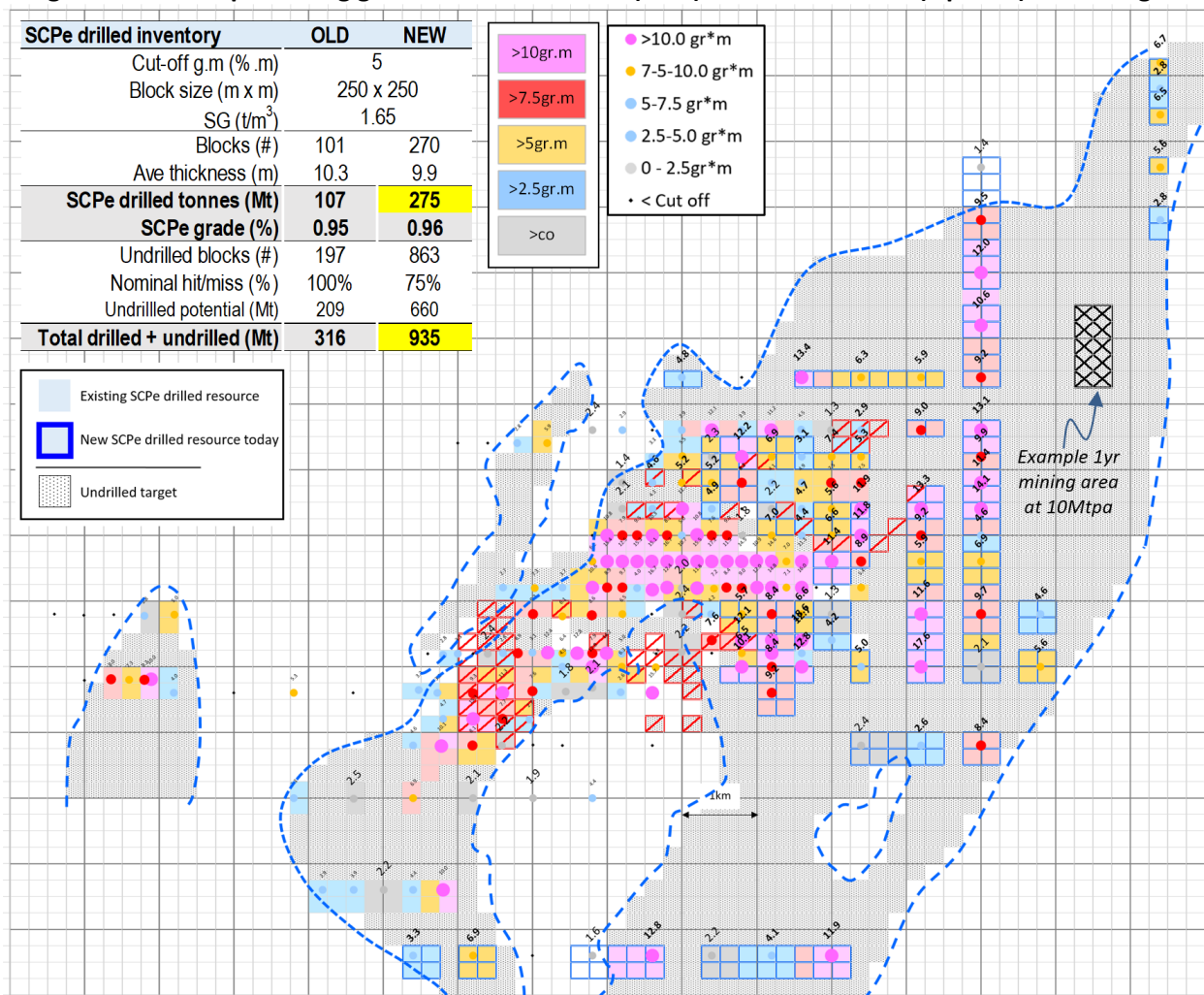
Project: Kasiya

Country: Malawi

RISK RATING: SPECULATIVE

We estimate drilling has lifted the drilled and undrilled potential from 107Mt to 275Mt, and 316Mt to 935Mt, respectively. If confirmed by drilling, the potential target detailed in Figure 1 could take Sovereign beyond 'will be a mine' into a world-class asset equalling, or potentially exceeding, the best existing mines globally. This all comes from a surprise tripling of the deposit footprint to ~66km², while infill drilling continued to confirm the quality with numerous intercepts of >8m @ >1% rutile. Based on just 5% in-situ valuation (ie US\$60/t rutile vs. ~US\$1,200/t spot) over our drilled 275Mt estimate, we maintain our BUY rating and lift our target price from A\$0.35/sh to A\$0.56/sh. With multiple channels to grow this further including potential for +20% value from graphite credits, a maiden resource scheduled for 4Q20, and PEA in 1H21, we expect momentum to continue and have a high conviction on this name.

Figure 1. Plan map showing grade.meter drill holes (dots) and SCP resource (squares) on 1km² grid



Source: SCP estimates

Tripling of rutile footprint puts Kasiya into ‘world class’ status with billion tonne potential

Sovereign’s latest 82 holes were split between infill, near-mine extensions to the south and east, and more distal step outs to the far south and far NE of the core drilling area. **Step out** results ~4km south of core areas returned highlights of 12m @ 1.1% rutile, and 12m @ 1.0%, delineating two trends that continue to be open to the south toward the previously drilled ‘Railroad’ target a further 10km south. Highlights up to ~4km northeast include 14m @ 0.9% rutile, 12m @ 0.8%, and 8m @ 0.9% (with 4m @ 1.1-1.2% from surface). These areas extend the mineralised footprint from a ~7.5km x 3km to ~16km x 6km (Figure 2). **Infill** drilling included 31 holes targeting the centre of the deposit, with highlights of 16m @ 1.16% and 12m @ 1.07% (with 2-4m @ 1.2-2.2% from surface). The tripling of the footprint lead management to indicate the potential for this to become ‘one of the largest rutile deposits in the world’. Drilling was limited at depth by hand-auger penetration, with potential for free-dig ore to continue to base of saprolite ~25m below surface. This drilling has validated the step-out vectoring methodology, opening the door to even more regional growth, with potential described by the company as ‘immense’. A maiden resource estimate will focus on the core ~30km² (of ~66km²), and is scheduled for 4Q20 after one further batch of drill results. This is to be followed by a PEA scheduled for 1H21, including graphite by-product potential.

Figure 2. Plan map showing (A) regional outline and (B) existing (green) and new (orange) footprint



Source: Sovereign Minerals

Our view

Put simply, the quality of intercepts and the increase in footprint reported far exceeded our expectations. We think the recent metallurgical results, and drilling up until now, firmly put Kasiya into the ‘will be a mine’ category with a simple question of size and profitability, including ~20% upside potential from graphite credits. Today’s results completely change this, lifting Kasiya into world-class potential in terms of both grade and size in our view. In this case, CEO Julian Stephen’s long-standing commitment to Malawi, combined with consultant Ben Stoichovitch’s experience in mineral sands, have unlocked what now appears not just to be an asset, but a new province. This represents an interplay between geology and value, as the rare metamorphosed precursor combined with near-surface weathering enrichment combine to create both size and high metallurgical quality.

SCP drill resource estimate lifts from 107Mt to 275Mt, potential now approaching 1Bt

We chart a “drilled inventory” reflecting areas in a ~250m radius around existing drilling, or with drill holes on either side of a 250m block, potentially reflecting the maiden resource potential (Figure 1). To this we add a ‘global target’, adding undrilled areas between economic hits for potential size with nominal 75% hit/miss ratio, which if validated by drilling could be booked in perhaps 12-24M. In both cases, we exclude some blocks under small local villages and government farms. At a grade x meters cut-off of five (eg. 5m @ 1% rutile), our drilled inventory lifts from 107Mt to 275Mt, while our global target lifts from 316Mt to 935Mt. In the short-term, it would appear the company should now comfortably achieve our prior hoped for 200-300Mt maiden resource. In the long-term, this clearly represents a major step-change in resource potential. The larger resource targets are speculative, as large areas remain undrilled and are up to 2km from the closest drill hole.

Matching the world’s best

A good comparison is the current ‘best’ rutile deposit globally, Sierra Rutile. That asset was purchased by Iluka in 2016 for an EV ~US\$320m. At the time rutile prices stood at ~US\$715/t (~US\$1,200/t now), and the asset came with a global resource of 730Mt @ 1.15% rutile equivalent (1.05% rutile with ilmenite and zircon credits). Sierra Rutile, an aged legacy asset, has struggled to ramp up with write-downs since, but still provided 10% of Iluka’s EBITDA in CY19. Give Iluka’s A\$4.0bn EV, 10% of that equates to ~A\$410m value. This sense checks well with an EV/in-situ. Specifically, Sierra Rutile was sold with US\$6bn in-situ value or at ~5.5% in-situ. Applying that to our drilled and global targets for Kasiya at spot US\$1,200/t rutile implies a valuation of A\$170-577m, with the upper end clearly dependent on drill success. Another view comes from production; Sierra Rutile produced 185kt of rutile in CY19; our drilled resource estimate could supply this for >30 years, and even at just a 50% reserve conversion, our global target could produce this for 24 years. At this point what becomes clear to us is that EV/in-situ or DCF valuations are rather moot given this overlooked Australia junior looks to hold at least an equal, if not superior, asset to the current leading asset globally. Most importantly the wider licence has barely been explored.

Too big for the majors NOT to buy?

Simplistically the TiO₂ market is dominated by low-value ilmenite, and almost double the TiO₂ content rutile. This means the majority of the sector relies of high-input, high-waste/emission ilmenite upgrading. The step change could come from substituting ilmenite-derived TiO₂ feed stocks with rutile. While the counterbalance is price sensitivity, the market is increasingly moving toward hard-caps on waste, meaning end users become less price sensitive. Of course the big picture is the asset could become a victim of its own success given its potential to supply so much rutile. Although a Hollywood problem for Sovereign, it could be rather a thorn in the side of existing and/or high-cost producers. The implication to us is that M&A may no longer just be accretive for potential buyers, but *necessary* when framed in the context of market protection given the large sunk capex by majors in ilmenite mining and conversion capacity and strong push toward improved ESG.

Maintain BUY rating and lift PT from A\$0.35/sh to A\$0.56/sh

We maintain our BUY rating and lift our target price from A\$0.35/sh PT to A\$0.56/sh. We base this on an EV/in-situ, taking *only* our drilled resource estimate of 275Mt and applying a nominal 5% in-situ value (ie US\$60/t rutile vs. ~US\$1,200/t spot). Given our in-situ value may lift by 20% with graphic credits, the overall resource potential is some four time larger than our drilled resource estimate. There is plenty of room to grow from here.

Table 1. SCP valuation for Sovereign

Kasiya in-situ value @ 935Mt (US\$bn)	3.2	Basic shares on issue (m)	383
Kasia @ 5% insitu value (US\$m)	158	Dilutive options (m)	38
Kasiya asset valuation (A\$m)	217	Average strike (A\$/sh)	0.16
Plus cash on hand (A\$m)	2.7	Fully diluted shares (m)	420
Nominal graphite valuation (A\$m)	10.0	SCP NAV/sh (A\$/sh)	0.56
Plus cash from dilutive options (A\$m)	5.8	Recommendation	BUY
Sovereign group NAV (A\$m)	235	Price target (A\$/sh):	0.56

Source: SCP

Why we like Sovereign Metals

1. Pure rutile deposit increases margin, addresses downstream ESG requirements
2. Unique metallogenesis drives large grain size and premium low-deleterious product
3. On hydro power, hydro mineable, on modern rail to port with allocation
4. From surface asset speeds resource drilling, eases mining on mine-and-backfill basis
5. Potential 'province scale' discovery with 8,000km² of unique geology largely undrilled

Catalysts

- **2H20:** Ongoing regional drill results ('footprint' drilling)
- **4Q20:** Maiden JORC compliant resource estimate for Kasiya
- **1H21:** PEA
- **2021:** Sampling of highest ranked 6-8 regional prospects targeting Kasiya-style, high-grade rutile

Brock Salier

Partner, Sprott Capital Partners
M: +44.7400.666.913
bsalier@sprott.com

Justin Chan

Director, Sprott Capital Partners
M: +44.7930.719.019
jchan@sprott.com

Chris Tonkin

Research Associate, Sprott Capital Partners
M: +44.7470.766.724
ctonkin@sprott.com

Equity Research

DISCLOSURES & DISCLAIMERS

This research report (as defined in IIROC Rule 3400) is issued and approved for distribution in Canada by Sprott Capital Partners LP ("SCP"), an investment dealer who is a member of the Investment Industry Regulatory Organization of Canada ("IIROC") and the Canadian Investor Protection Fund ("CIPF"). The general partner of SCP is Sprott Capital Partners GP Inc. and SCP is a wholly-owned subsidiary of Sprott Inc., which is a publicly listed company on the Toronto Stock Exchange under the symbol "SII". Sprott Asset Management LP ("SAM"), a registered investment manager to the Sprott Funds and is an affiliate of SCP. This research report is provided to retail clients and institutional investors for information purposes only. The opinions expressed in this report are the opinions of the author and readers should not assume they reflect the opinions or recommendations of SCP's research department. The information in this report is drawn from sources believed to be reliable but the accuracy or completeness of the information is not guaranteed, nor in providing it does SCP and/or affiliated companies or persons assume any responsibility or liability whatsoever. This report is not to be construed as an offer to sell or a solicitation of an offer to buy any securities. SCP accepts no liability whatsoever for any loss arising from any use or reliance on this research report or the information contained herein. Past performance is not a guarantee of future results, and no representation or warranty, expressed or implied, is made regarding future performance of any security mentioned in this research report. The price of the securities mentioned in this research report and the income they generate may fluctuate and/or be adversely affected by market factors or exchange rates, and investors may realize losses on investments in such securities, including the loss of investment principal. Furthermore, the securities discussed in this research report may not be liquid investments, may have a high level of volatility or may be subject to additional and special risks associated with securities and investments in emerging markets and/or foreign countries that may give rise to substantial risk and are not suitable for all investors. SCP may participate in an underwriting of, have a position in, or make a market in, the securities mentioned herein, including options, futures or other derivatives instruments thereon, and may, as a principal or agent, buy or sell such products.

DISSEMINATION OF RESEARCH: SCP's research is distributed electronically through email or available in hard copy upon request. Research is disseminated concurrently to a pre-determined list of clients provided by SCP's Institutional Sales Representative and retail Investment Advisors. Should you wish to no longer receive electronic communications from us, please contact unsubscribe@sprott.com and indicate in the subject line your full name and/or corporate entity name and that you wish to unsubscribe from receiving research.

RESEARCH ANALYST CERTIFICATION: Each Research Analyst and/or Associate who is involved in the preparation of this research report hereby certifies that:

- The views and recommendations expressed herein accurately reflect his/her personal views about any and all of the securities or issuers that are the subject matter of this research report;
- His/her compensation is not and will not be directly related to the specific recommendations or view expressed by the Research analyst in this research report;
- They have not affected a trade in a security of any class of the issuer within the 30-day period prior to the publication of this research report;
- They have not distributed or discussed this Research Report to/with the issuer, investment banking group or any other third party except for the sole purpose of verifying factual information; and
- They are unaware of any other potential conflicts of interest.

UK RESIDENTS: Sprott Partners UK Limited ("Sprott") is an appointed representative of PillarFour Securities LLP which is authorized and regulated by the Financial Conduct Authority. This document has been approved under section 21(1) of the FMSA 2000 by PillarFour Securities LLP ("PillarFour") for communication only to eligible counterparties and professional clients as those terms are defined by the rules of the Financial Conduct Authority. Its contents are not directed at UK retail clients. PillarFour does not provide investment services to retail clients. PillarFour publishes this document as non-independent research which is a marketing communication under the Conduct of Business rules. It has not been prepared in accordance with the regulatory rules relating to independent research, nor is it subject to the prohibition on dealing ahead of the dissemination of investment research. It does not constitute a personal recommendation and does not constitute an offer or a solicitation to buy or sell any security. Sprott and PillarFour consider this note to be an acceptable minor non-monetary benefit as defined by the FCA which may be received without charge. This is because the content is either considered to be commissioned by Sprott's clients as part of their advisory services to them or is short term market commentary. Neither Sprott nor PillarFour nor any of its directors, officers, employees or agents shall have any liability, howsoever arising, for any error or incompleteness of fact or opinion in it or lack of care in its preparation or publication; provided that this shall not exclude liability to the extent that this is impermissible under the law relating to financial services. All statements and opinions are made as of the date on the face of this document and are not held out as applicable thereafter. This document is intended for distribution only in those jurisdictions where PillarFour is permitted to distribute its research.

IMPORTANT DISCLOSURES FOR U.S. PERSONS: This research report was prepared by Sprott Capital Partners LP ("SCP"), a company authorized to engage in securities activities in Canada. SCP is not a registered broker/dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution to "major U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). Any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through Sprott Global Resource Investments Ltd. ("SGRIL"), a broker dealer in the United States registered with the Securities Exchange Commission ("SEC"), the Financial Industry Authority ("FINRA"), and a member of the Securities Investor Protection Corporation ("SIPC"). Under no circumstances should any recipient of this research report effect any transaction to buy or sell securities or related financial instruments through SCP.

SGRIL accepts responsibility for the contents of this research report, subject to the terms set out below, to the extent that it is delivered to a U.S. person other than a major U.S. institutional investor. The analyst whose name appears in this research report is not licensed, registered, or qualified as a research analyst with FINRA and may not be an associated person of SGRIL and, therefore, may not be subject to applicable

Equity Research

restrictions under FINRA Rule 2241 regarding communications by a research analyst with a subject company, public appearances by the research analyst, and trading securities held by a research analyst account. To make further inquiries related to this report, United States residents should contact their SGRIL representative.

ANALYST CERTIFICATION / REGULATION AC: The analyst and associate certify that the views expressed in this research report accurately reflect their personal views about the subject securities or issuers. In addition, the analyst and associate certify that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

SPROTT CAPITAL PARTNERS EXPLANATION OF RECCOMENDATIONS: Should SCP issue research with recommendations, the research rating guidelines will be based on the following recommendations:

BUY: The stocks total returns are expected to be materially better than the overall market with higher return expectations needed for more risky securities markets

NEUTRAL: The stock's total returns are expected to be in line with the overall market

SELL: The stocks total returns are expected to be materially lower than the overall market

TENDER: The analyst recommends tendering shares to a formal tender offering

UNDER REVIEW: The stock will be placed under review when there is a significant material event with further information pending; and/or when the research analyst determines it is necessary to await adequate information that could potentially lead to a re-evaluation of the rating, target price or forecast; and/or when coverage of a particular security is transferred from one analyst to another to give the new analyst time to reconfirm the rating, target price or forecast.

NOT RATED ((N/R): The stock is not currently rated

Research Disclosure		Response
1	SCP and its affiliates collectively beneficially owns 1% or more of any class of the issuer's equity securities ¹	YES
2	The analyst or any associate of the analyst responsible for the report or recommendation or any individual directly involved in the preparation of the report holds or is short any of the issuer's securities directly or through derivatives	NO
3	An SCP partner, director, officer or analyst involved in the preparation of a report on the issuer, has during the preceding 12 months provided services to the issuer for remuneration other than normal course investment advisory or trading execution services	NO
4	SCP has provided investment banking services for the issuer during the 12 months preceding the date of issuance of the research report or recommendation	YES
5	Name of any director, officer, employee or agent of SCP who is an officer, director or employee of the issuer, or who serves in an advisory capacity to the issuer	NO
6	SCP is making a market in an equity or equity related security of the issuer	NO
7	The analyst preparing this report received compensation based upon SCP's investment banking revenue for the issuer	NO
8	The analyst has conducted a site visit and has viewed a major facility or operation of the issuer	NO
9	The analyst has been reimbursed for travel expenses for a site visit by the issuer	NO

Sprott Capital Partners Equity Research Ratings:

Summary of recommendations as of September 2020	
BUY:	22
HOLD:	0
SELL:	0
UNDER REVIEW:	0
TENDER:	0
NOT RATED:	0
TOTAL	22

¹ As at the end of the month immediately preceding the date of issuance of the research report or the end of the second most recent month if the issue date is less than 10 calendar days after the end of the most recent month