



The Mercenary Geologist's Gold Review: Q4 2010

A Monday Morning Musing from Mickey the Mercenary Geologist

Contact@MercenaryGeologist.com

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This is the last in a year-end series updating the companies I cover by commodity sector. My previous comprehensive review of these companies was sent to subscribers on July 23 ([Mercenary Musing, July 26, 2010](#)) and this musing will use that report date as reference.

Today we briefly review the gold market in the second half of 2010 and provide detailed updates on four gold companies: **Amarillo Gold Corp (AGC.V)**, **Animas Resources (ANI.V) Ltd**, **Goldgroup Mining Inc (GGA.T)**, and **Otis Gold Corp (OOO.V)**. I am a shareholder of each and Amarillo, Goldgroup, and Otis are sponsors of my website.

Over the past five months gold has turned in one of its best performances since the nine year bull market began in mid 2001. From a low of \$1162 on July 27, gold has been on quite a run and reached an all time high of \$1424 on December 3. Folks, that's a 23% gain.



The rising gold price has carried the gold miners, developers, and explorers along for the ride. Average peer valuation for advanced explorers with significant in-the-ground gold resources has increased from \$85 to over \$155 per ounce. However, only two of my four gold companies have participated in kind.

Let's take a look at each one individually:

I have been involved with **Amarillo Gold Corp (AGC.V)** since its reverse takeover of a shell in November of 2003 and initiated coverage in late winter at 65 cents ([Mercenary Musing, March 1, 2010](#)). After a brief run to 90 cents, it backed off and was trading at 72 cents on July 23. I toured the company's two flagship projects in Brazil in mid-October.

In recent weeks, Amarillo has showed considerable strength, reaching an all-time high of \$1.90 on December 22. The company achieved its double, the payoff for any of our speculations, in nine and a half months. Its latest close was at \$1.79.



News from Amarillo has been quite positive over the past five months:

- In August the company announced positive metallurgical results at Mara Rosa and solicited bids for a pre-feasibility study.
- In early September it announced the first 43-101 resource for the Butia deposit at Lavras do Sul with an inferred and indicated total of 523,000 ounces of gold at an average grade of 0.84 g/t Au at a 0.3 g/t cutoff.
- In October the company commenced a 7000 m drill program at Mara Rosa and added a third rig in early November. This program is to define reserves, produce samples for metallurgical process, acid drainage, and environmental baseline studies, and generate geotechnical data for pit slope design. AGC added an experienced mine development and metallurgical engineer, Frank Baker, to its staff to lead Mara Rosa thru pre-feasibility.
- In early November, environmental and social studies at Mara Rosa were started with a local Brazilian firm.
- In mid December, it announced a new discovery at Lavras do Sul thru soil sampling. The prospect will be drilled once permits are approved, likely in the second half of 2011.

With about \$3.0 million in cash, four rigs turning on two projects until mid-December, and the Mara Rosa pre-feasibility study budgeted at \$4.0 million, AGC will go to the market for an equity financing sooner than later in 2011. Because trading volumes are very low and have been problematic for the company, I think the financing should be offered to retail brokers and lay investors and include a warrant to improve liquidity.

Amarillo Gold Corp has 56.1 million shares outstanding, 1.6 million ounces of qualified resources, a price of about \$1.80, and is currently valued at \$63 per ounce gold in the ground. This is half of the advanced gold explorer peer valuation for December. Even using the more conservative valuation of \$90 an ounce in July, AGC remains undervalued with respect to its peers. I hope that the company will choose to increase its marketing efforts in the New Year as this is a compelling but largely unknown story.

I also have a long involvement with **Goldgroup Mining Inc (GGA.T)** thru its predecessor company Sierra Minerals Inc where I was a founding RTO shareholder in late 2003. I initiated coverage of Goldgroup in early July at 65 cents and it rewarded readers with a double in four and a half months. The all time high of \$1.43 was hit on December 7 and it closed Friday at \$1.16.



Goldgroup has made considerable exploration progress since we last examined it in detail:

- The company initiated major drill programs at its two flagship exploration projects with 30,000 meters scheduled at Caballo Blanco and 18,500 meters at San Jose de Gracia.
- It released drill results from vein systems at San Jose de Gracia including 22.2 g/t Au over 7.8 meters, 105 g/t Au over 1.7 meters, and 333 g/t over 5.5 meters.
- It released drill results from two RC holes at Caballo Blanco, a twin and a step-out. As expected, both encountered long intervals of low grade gold mineralization and provided material for column leach testing.
- It raised \$3 million in a private placement with strategic investor Sam Magid.

Other news of note includes the divestiture of nine million shares by Lundin's NGEx Resources.

Results from the company's gold mining operation at Cerro Colorado in Sonora State were not positive. Cash costs have risen significantly over the past year and the production goal of 25,000 ounces in 2010 will not be met. In its nine month MD&A, Goldgroup documents operating costs per ounce of \$1056 compared to \$664 in 2009. 2010 production is now forecast at 20,000 to 22,000 ounces.

The company attributes the much higher cash cost and production shortfall to a higher strip ratio with pushback to access higher grade ore. A normal strip ratio of 1:1 and better gold recovery via secondary crushing are projected for 2011. Cerro Colorado is an established gold mine but it is a small and high cost operation and is likely to remain so.

GGA has a current cash position of \$14.1 million and is funded for the next year to complete its advanced exploration and development programs at Caballo Blanco and San Jose de Gracia.

It has 43-101 qualified gold resources at three properties including the 100% owned Cerro Colorado gold mine in Sonora, advanced exploration at 70% owned Caballo Blanco in Veracruz, and 50% earn-in at the San Jose de Gracia project in Sinaloa. Attributable resources to the company in all categories are 1.0 million ounces. With 88.9 million shares outstanding and a current price of \$1.16, market capitalization is \$103 million giving a valuation per ounce in the ground of \$103.

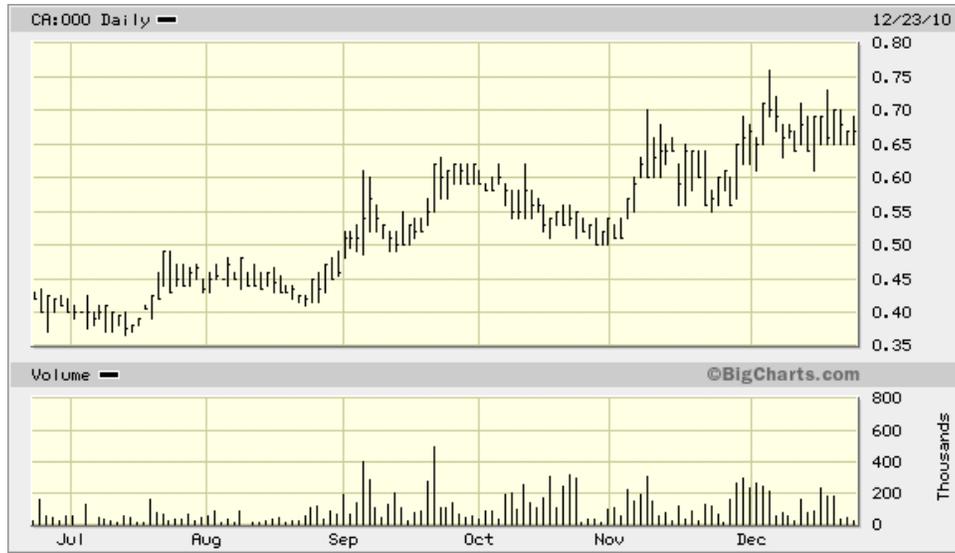
Goldgroup remains undervalued compared to its advanced gold exploration peers. Our speculation in Goldgroup Mining Inc has been successful with 120% return on investment in less than five months. The company was undervalued when I first covered it and remains so with respect to its peers. However, in my opinion the peer valuation of \$155 is unsustainable in the current market where gold exploration companies are overbought.

A successful future for the company depends on development of Caballo Blanco into a large, low cost, open pit, heap leach gold mine within a time frame of two or three years. San Jose de Gracia is an attractive asset but the company presently can earn 50% and will need to purchase the remaining 50% in an equity and/or cash deal with privately-held Dyna Resources to make it a profitable operation.

In my opinion, Goldgroup has the share structure, people, and projects to reward shareholders with continued success in the mid to long term. For me, GGA is not a short term trade but an investment and I remain a committed shareholder of the company. But with that said, I recently sold a small tranche of GGA shares near its all-time high thru my normal programmed selling on the uptick.

CEO Keith Piggott and I will meet in Vancouver in three weeks to review the company's plans for the future and discuss sponsorship renewal.

Otis Gold Corp (OOO.V) joined the legion of MercenaryGeologist.com sponsors in early March 2010 ([Mercenary Musing, March 8, 2010](#)). It was trading at 52 cents then, hit a low of 38 cents during the July summer doldrums, was 55 cents upon my last musing on the company ([Mercenary Musing, September 20, 2010](#)), reached its 52 week high of 76 cents on December 6, and closed most recently at 67 cents:



Otis looks quite bullish on the sixth month chart. However, the company has lagged its peers over the past year, returning less than 50%. This is despite progress and robust drill results at its flagship Kilgore project.

News since my last report on Otis Gold includes:

- The summer drill program at Kilgore's Mine Ridge deposit has returned significant in-fill and extension intercepts including 56 m of 1.4 g/t Au, 30 meters of 2.5 g/t Au, 46 meters of 1.3 g/t Au, 41 meters of 1.3 g/t Au, and 88 meters of 1.3 g/t Au. Assays from 20 of 35 holes have been reported and the resource is being upgraded and the number of contained ounces expanded.
- In October Otis Gold raised \$2.7 million. Placees included the Galena Fund, a strategic investor that can increase its allotment to 11% of the shares outstanding and with warrant exercise, can control 19.5% of the company.
- In late November Otis acquired 100% of the Kilgore project for additional staged payments of \$1.75 million and 2.0 million shares from former JV partner Bayswater Uranium. The company can issue these payments from its current working capital position of \$3.4 million.

Despite all this good news, Otis Gold remains severely undervalued with respect to its peers. 43-101 qualified resources are 487,000 ounces in all categories at Kilgore and 235,000 inferred ounces at the Oakley project in southern Idaho giving a total of 722,000 ounces gold. With 33.4 million shares outstanding and a current price of 67 cents, market capitalization is about \$22 million. Therefore, the company's gold in-the-ground is valued at only \$31 per ounce.

Near term catalysts for the company include assays from the remaining 15 holes at Mine Ridge. I am confident from previously released results that its Mine Ridge resource will grow significantly when a new resource is estimated in Q1 2011.

Perhaps more importantly for the stock price will be assays from the company's five holes at the Dog Bone Ridge target. These holes reportedly hit strong alteration and mineralization similar in thickness to Mine Ridge intercepts. A gold-silver discovery at Dog Bone Ridge could be the game changer for OOO.

Let's hope the gold gods are good to Otis Gold and the next time I write about the company it will no longer be an undervalued stock. The clock is ticking, we have less than three months to get our double, and company management is aware of my position.

Our final company is **Animas Resources Inc (ANI.V)**. Although not a sponsor, ANI is a website affiliate and one of my core junior resource investments. I have been a shareholder since its pre-IPO financing and participated in three subsequent private placements. I wrote about ANI twice ([Mercenary Musing, November 3, 2008](#)); [Mercenary Musing, April 13, 2009](#)) in addition to the July 23 update.

Although Animas has an impeccable group of people in its management, technical team, advisors, and strategic investors, a tight share structure, and prospective gold projects in Mexico and Nevada, it has continually disappointed with drill results. It was a 32 cent stock on July 23, went to 54 cents, and now is back to 28.5 cents with its latest drilling bust at Golden Arrow, Nevada. ANI has working capital of \$1.4 million.

Here's the six month chart:



Since our update, Animas has released the following material news:

- It announced a molybdenum porphyry system was encountered while drilling for gold at its Santa Gertrudis, Sonora, Mexico property.
- It completed a 35 cent private placement with insiders and strategic investors to raise \$1.7 million.
- It announced conversion of historic resources to 43-101 qualified inferred resources in the Santa Gertrudis district; in whole containing 557,000 ounces in nine small deposits.
- It announced that no significant gold was found in 16 holes on its Round Mountain-style Golden Arrow Joint Venture in south-central Nevada.

After recent drill failures at Santa Gertrudis and Golden Arrow, Animas has one project with potential for a large gold discovery remaining on its books: the former Kinsley Mountain mine in northeast Nevada. I am bullish on its geological potential in a Long Canyon-type target that will be drilled in summer 2011.

However, in my opinion Animas requires new projects and/or a change of corporate direction to be successful and reward its dedicated shareholders.

In October 2008 I urged the company to monetize its numerous small deposits at Santa Gertrudis by vending to active miners in Mexico with production experience in low tonnage, open pit, heap leach gold mines. Although my suggested business plan has not been implemented to date, I trust that the company will advance on that front in the near future.

Meanwhile, we await drill results from Kinsley Mountain late next summer. I have not sold a share of Animas Resources since early March 2008 when it traded above \$1.50. I have bought five times on weakness in the past two and a half years. But I will be honest with you and state that my patience is growing thin.

Finally I provide an update on a company that was dropped from coverage upon expiry of the six month contract on May 1. Oremex (ORM.V) was trading at 14 cents when I alerted subscribers on December 11, 2010; by July 23 it had fallen to a 52 week low of 6 cents. I had determined to sell my entire position if I could break even before the end of 2010 or take a tax loss if it didn't reach 15 cents by then. With positive news from three formerly minor Mexican gold-silver projects and a strategic placement by Sprott Asset Management, Oremex traded at 29.5 cents on November 10 and our double was gained in 11 months. My projected short term capital loss has turned into a nice short term capital gain.

In this raging bull market for gold, gold miners, and gold explorers, my one bad choice of companies in the past year suddenly has turned into a double and a profitable trade.

Folks, this is not exactly rocket science.

May you all enjoy a happy holiday weekend with family and friends.

Ciao for now,

Mickey Fulp
Mercenary Geologist



The [Mercenary Geologist Michael S. "Mickey" Fulp](#) is a Certified Professional Geologist with a B.Sc. Earth Sciences with honor from the University of Tulsa, and M.Sc. Geology from the University of New Mexico. Mickey has 30 years experience as an exploration geologist searching for economic deposits of base and precious metals, industrial minerals, uranium, coal, oil and gas, and water in North and South America, Europe, and Asia.

Mickey has worked for junior explorers, major mining companies, private companies, and investors as a consulting economic geologist for the past 22 years, specializing in geological mapping, property evaluation, and business development. In addition to Mickey's professional credentials and experience, he is high-altitude proficient, and is bilingual in English and Spanish. From 2003 to 2006, he made four outcrop ore discoveries in Peru, Nevada, Chile, and British Columbia.

Mickey is well-known throughout the mining and exploration community due to his ongoing work as an analyst, writer, and speaker.

Contact: Contact@MercenaryGeologist.com

Disclaimer: I am a shareholder of Amarillo Gold Corp, Animas Resources, Ltd, Goldgroup Mining Inc, and Otis Gold Corp; Amarillo Gold, Goldgroup Mining, and Otis Gold Corp are current sponsors of my website; I hold options in Goldgroup Mining thru my previous relationship with Sierra Minerals.

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