

Action Note

Equity Research

Published and distributed by TD Securities Inc.

November 6, 2023

Metals & Minerals

Capstone Copper Corp.

(CS-T) C\$4.99

Mantoverde On Track for Year-End Completion

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Event

We have updated our estimates for Capstone following Q3/23 results.

Impact: SLIGHTLY NEGATIVE

- Overall, Q3/23 was not a great quarter from a production standpoint, as reliability issues at Pinto Valley and Mantos Blancos impacted throughput performance. Production in Q4 is expected to improve, driven by higher grades at PV and improved reliability issues. **The company has maintained its H2/23 copper production guidance of 83kt-93kt (full year 163kt-173kt), with C1 cash costs trending towards the upper end of guidance of \$2.55-\$2.75/lb.**
- Ramp-up at Mantos Blancos will take more time and capital** — The company is working on a plan to improve operational performance and ramp up Mantos Blancos to its design throughput of 20ktpd after another weak quarterly performance (14.2ktpd in Q3, -3% q/q). The company notably addressed some bottleneck issues in Q3 following a six-day planned shutdown, but new tailings handling and pumping infrastructure is required to achieve the full run-rate. A total of \$20mm is required to make these changes through early-2024, and the asset is not likely to achieve its design capacity until at least Q2/24, which we now reflect in our estimates.
- Mantoverde sulphide expansion remains on schedule for completion by year-end** — Overall capital increased 5% to \$870mm, half of which was related to inflationary pressures, while the remaining half was related to project improvements, including additional rotainers (concentrate transport), a water reservoir, and additional camp and warehouse infrastructure. Importantly, the project completion remains on track for commission and feeding first ore to the mill by year-end, with a targeted ramp-up to design capacity by mid-2024.

TD Investment Conclusion

We are lowering our target price to C\$7.00 from C\$7.50 and maintaining our BUY rating. Our lower target price reflects a combination of higher costs and a slower-than-expected ramp-up at Mantos Blancos. Capstone has one of the best organic growth stories in our coverage universe providing strong leverage to copper. The company's assets are also located in what we would consider favorable mining jurisdictions, with long operating track records.

Recommendation:	BUY
Risk:	HIGH
12-Month Target Price:	C\$7.00 ↓ Prior: C\$7.50
12-Month Dividend (Est.):	C\$0.00
12-Month Total Return:	40.3%

Market Data (C\$)

Current Price	C\$4.99
52-Week Range	\$3.20 - \$7.25
Mkt Cap (f.d.) (\$mm)	\$3,507.7
EV (\$mm)	\$4,936.4
Current Dividend	\$0.00
Dividend Yield	0.0%
Avg. Daily Trading Vol.	2,285,749

Financial Data (C\$)

Fiscal Y-E	December
Shares O/S (f.d)(mm)	702.9
Float Shares (mm)	567.7
Net Debt (\$mm)	\$965.8
NAVPS	\$6.92

Estimates (US\$)

Year	2021A	2022A	2023E	2024E
EPS (Adj.)	0.60	0.14	0.00	0.43
EPS (Adj.) (old)	—	—	0.03	0.61
EBITDA (\$mm)	432.2	352.8	251.4	852.7
EBITDA (\$mm) (old)	—	—	245.3	1,012.9
CFPS (f.d)	0.91	0.38	0.23	0.98
CFPS (f.d) (old)	—	—	0.24	1.11

EPS (Adj.) Quarterly Estimates (US\$)

Year	2021A	2022A	2023E	2024E
Q1	0.16	0.14	0.02	—
Q2	0.17	(0.01)	(0.02)	—
Q3	0.09	(0.02)	(0.02)	—
Q4	0.18	0.06	0.02	—

Valuations

Year	2021A	2022A	2023E	2024E
EV/EBITDA	8.3x	10.2x	14.3x	4.2x
P/CFPS (f.d)	4.0x	9.6x	15.8x	3.7x
P/E (Adj.)	6.1x	25.9x	—	8.4x

Supplemental Data

Year	2021A	2022A	2023E	2024E
Cu (US\$/lb)	4.23	4.00	3.86	4.10
Cu Prod. (mmlb)	187	345	363	521

Net debt balances are shown in US\$.

All figures in US\$, unless otherwise specified



Company Profile

Capstone Copper is a Canadian mining company primarily focused on copper production, with producing assets in Arizona, Mexico, and Chile. The company also owns the advanced-stage Santo Domingo project in Chile.

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Details

Capstone reported Q3/23 adjusted EBITDA of \$62.8mm, above our estimate of \$50.9mm and slightly below consensus of \$63.6mm. Adjusted EPS of -\$0.02 was slightly below TD and consensus of \$0.00, driven by higher depreciation expenses. The EBITDA beat relative to our estimate was driven largely by lower operating costs.

Overall production in the quarter totalled 40.3kt (TD 41.1kt), at consolidated C1 costs of \$2.88/lb Cu (TD \$2.98/lb). Production in the quarter was impacted by another unscheduled downtime (eight days) of the Pinto Valley crushing circuit due to some equipment replacements and repairs. Milling rates at Mantos Blancos continue to struggle to ramp up to design of 20ktpd. Efforts are being made to de-bottleneck the circuit, which we expect will likely take until sometime in H1/24.

Liquidity and FCF — The company remains in a good financial position with total liquidity of \$424.5mm (\$419.6mm in Q2/23), including cash (\$128mm) and short-term investments of \$130mm, along with \$295mm undrawn on the corporate revolving credit facility. We calculate negative FCF of \$136mm in the quarter given the heavy spend at Mantoverde.

Exhibit 1. Q3/23 Results

	Q3/22	Q4/22	Q1/23	Q2/23	Actual Q3/23	TDS Est. Q3/23	Var. %	q/q %	y/y %
Production (kt)									
Cozamin	6.4	5.8	5.2	6.6	5.9	6.1	-2%	-11%	-7%
Pinto Valley	14.1	15.0	12.8	12.7	13.6	13.8	-1%	7%	-4%
Mantos Blancos	13.6	14.2	14.1	11.7	12.2	12.5	-3%	4%	-11%
Mantoverde (100%)	12.2	10.5	8.5	8.4	8.6	8.8	-2%	2%	-30%
Total Copper Production, kt	46.4	45.5	40.7	39.4	40.3	41.1	-2%	2%	-13%
Sales									
Average Copper Price, (US\$/lb)	\$3.52	\$3.64	\$4.06	\$3.84	\$3.80	\$3.80	0%	-1%	8%
Total Copper Sales (kt)	44.2	44.7	37.5	40.1	38.7	40.1	-4%	-3%	-12%
Cash Costs, US\$/lb									
Cozamin	\$1.20	\$1.40	\$1.72	\$1.63	\$1.85	\$1.80	3%	13%	54%
Pinto Valley	\$2.60	\$2.48	\$3.09	\$2.98	\$2.83	\$2.90	-3%	-5%	9%
Mantos Blancos	\$2.68	\$2.09	\$2.68	\$3.15	\$2.82	\$3.02	-7%	-10%	5%
Mantoverde	\$3.87	\$3.65	\$4.02	\$3.92	\$3.74	\$3.88	-4%	-5%	-3%
Consolidated Cash Costs, Net (US\$/lb)	\$2.76	\$2.50	\$2.96	\$3.01	\$2.88	\$2.98	-4%	-4%	4%
Consolidated AISC, Net (US\$/lb)	\$3.52	\$3.59	\$3.67	\$4.00	\$3.99	\$3.87	3%	0%	13%
Financial Results									
Revenue (\$mm)	\$308.7	\$362.6	\$335.6	\$333.9	\$322.2	\$331.2	-3%	-4%	4%
Operating Costs (\$mm)	\$271.4	\$240.8	\$240.4	\$274.0	\$245.1	\$259.0	-5%	-11%	-10%
Royalty (\$mm)	\$2.2	\$3.1	\$3.0	\$3.1	\$2.7	\$3.3	-19%	-12%	22%
Operating Margin (%)	na	21%	13%	1%	4%	5%	-24%	149%	nm
Depreciation (\$mm)	\$46.3	\$43.1	\$47.9	\$51.9	\$62.4	\$52.6	19%	20%	35%
EPS (Reported)	\$0.05	(\$0.03)	(\$0.03)	(\$0.05)	(\$0.05)	(\$0.00)	nm	nm	nm
EPS (Adjusted)	(\$0.02)	\$0.06	\$0.02	(\$0.02)	(\$0.02)	(\$0.00)	nm	nm	nm
Adjusted EBITDA (\$mm)	\$34.1	\$80.5	\$65.3	\$43.4	\$62.8	\$50.9	23%	45%	84%
CFO (b.f WC, \$mm)	\$13.9	\$99.5	\$41.7	\$11.4	\$41.0	\$44.4	-8%	259%	196%
CFPS (b.f WC)	\$0.02	\$0.14	\$0.06	\$0.02	\$0.06	\$0.06	-7%	258%	194%
Capex (\$mm)	\$185.3	\$149.7	\$174.3	\$137.1	\$173.0	\$179.5	-4%	26%	-7%
Free Cash Flow (\$mm)	(\$175.6)	(\$130.4)	(\$185.3)	(\$155.0)	(\$136.4)	(\$153.6)	nm	nm	nm
Cash & Equiv. at End of Qtr (\$mm)	\$194.5	\$170.3	\$99.5	\$116.1	\$128.0	\$87.5	46%	10%	-34%
Working Capital	\$207.9	\$163.7	\$119.3	\$149.1	\$97.3	\$94.0	3%	-35%	-53%
Long Term Debt	\$509.5	\$599.1	\$696.0	\$822.1	\$917.7	\$913.5	0%	12%	80%
Net Debt	\$313.2	\$483.1	\$655.0	\$834.9	\$965.8	\$981.5	-2%	16%	208%

Source: Company, TD Securities Inc.

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Outlook

Reiterating H2/23 production guidance but trending towards the upper end of costs

– Despite the soft Q3 production results, the H2/23 production target of 83kt-93kt copper is unchanged, with C1 cash costs trending to the upper end of cash guidance of \$2.55-\$2.75/lb. Full-year guidance remains at 163kt-173kt at C1 cash costs of \$2.75-2.85/lb. The company now expects Q4 to be the strongest production quarter for the year, with improvements at Pinto Valley and Mantos Blancos.

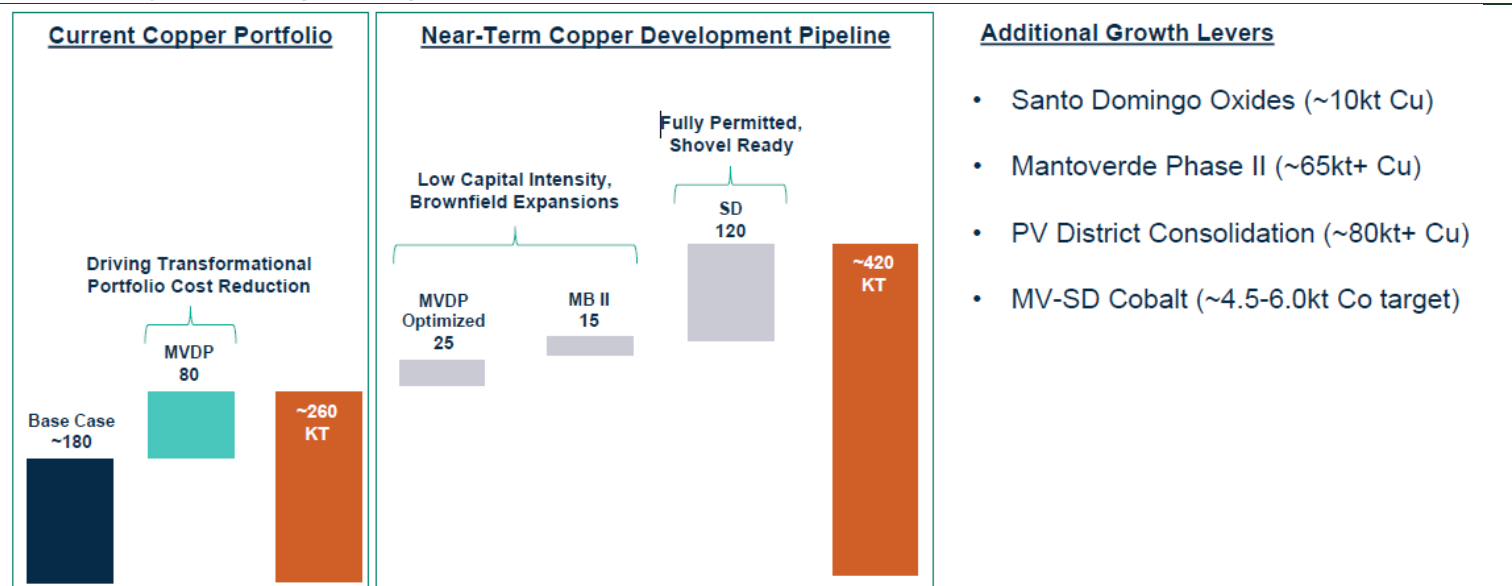
Santo Domingo Feasibility study update delayed to H1/24 – The optimized FS is now expected to be delivered in H1/2024 to allow additional time to account for recent metallurgical test work and updated mine plan and finalize other "key value drivers" within the study.

Other growth projects – In addition to the production growth from MVDP, Capstone has a number of other organic growth drivers in its pipeline. First and foremost, the company is looking at incremental expansions of both Mantos Blancos (MB II) and Mantoverde (MV Optimization).

MB II offers the potential to add a further 15ktpa of copper production – The project involves the integration of excess capacity in the crushing circuit, to increase throughput from the existing target of 20,000tpd to 27,000tpd. Management expects the largest cost component to be an expanded mining fleet and believes the capital for the project will be under \$100mm to complete. Management also believes the expansion can be done in incremental stages, reducing the initial capital outlay. **The study is not expected until H2/24, when it is anticipated that MB will be at design capacity.**

Mantoverde Optimization could add a further 25ktpa of copper production – This project involves increasing the design capacity of MVDP from a targeted 32ktpd up to 45ktpd. Management believes the major components within the project's existing comminution and flotation circuit are already capable of achieving 45ktpd, and the project could be completed for approximately \$150mm. **The study is expected in H1/24.**

Exhibit 2. Organic Development Pipeline Potential



Source: Company

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Exhibit 3. Production, Outlook, and Guidance

Exhibit C1 Production, Outlook, and Guidance									
	2021A	2022A	TD Estimates						CS Guidance
			Q1/23A	Q2/23A	Q3/23A	Q4/23E	2023E	2024E	2023E
Copper Production (kt)									
Sulphides Business									
Cozamin	24.4	24.5	5.2	6.6	5.9	6.1	23.8	25.2	23.4 - 24.4
Pinto Valley	60.5	56.8	12.8	12.7	13.6	15.8	54.9	61.5	53.5 - 56.5
Mantos Blancos	-	29.0	10.8	8.4	9.1	10.6	38.9	47.0	40.2 - 43.7
Mantoverde (100%)		0.0					0.0	67.1	
Total - Sulphides	84.9	110.3	28.9	27.7	28.7	32.4	117.6	200.8	117.1 - 124.6
Cathode Business									
Mantos Blancos		12.3	3.3	3.3	3.0	2.7	12.2	2.5	11.6 - 12.6
Mantoverde (100%)		36.3	8.5	8.3	8.6	9.4	34.7	35.2	36.0 - 40.0
Total - Cathode	0.0	48.6	11.8	11.6	11.6	12.0	47.0	37.7	46.0 - 48.0
Total Cu Production (Consolidated)	84.9	158.8	40.7	39.3	40.3	44.4	164.6	238.5	163 - 173.0
C1 Cash Costs, US\$/lb									
Sulphides Business									
Cozamin	\$0.96	\$1.24	\$1.72	\$1.63	\$1.85	\$1.78	\$1.74	\$1.58	
Pinto Valley	\$2.16	\$2.63	\$3.09	\$2.98	\$2.83	\$2.46	\$2.82	\$2.41	
Mantos Blancos ¹	-	\$2.54	\$2.68	\$3.15	\$2.82	\$2.88	\$2.87	\$2.93	
Cathode Business									
Mantoverde (100%) ¹	-	\$3.63	\$4.02	\$3.92	\$3.74	\$3.48	\$3.78	\$2.13	
Consolidated Cash Costs, Net (US\$/lb)	\$1.81	\$2.63	\$2.96	\$3.01	\$2.88	\$2.71	\$2.88	\$2.31	\$2.75 - \$2.85
Consolidated AISC Net (US\$/lb)	\$2.41	\$3.46	\$3.67	\$4.00	\$3.99	\$3.52	\$3.79	\$3.05	
Capex (\$mm)	\$133	\$560	\$174	\$137	\$228	\$153	\$692	\$450	\$620
Exploration (\$mm)	\$3	\$10	\$1	\$2	\$2	\$3	\$7	\$8	\$10

Note 1: TD's Mantos Blancos and Mantoverde cash costs estimates and company guidance presented on a consolidated (sulphides + cathode) basis

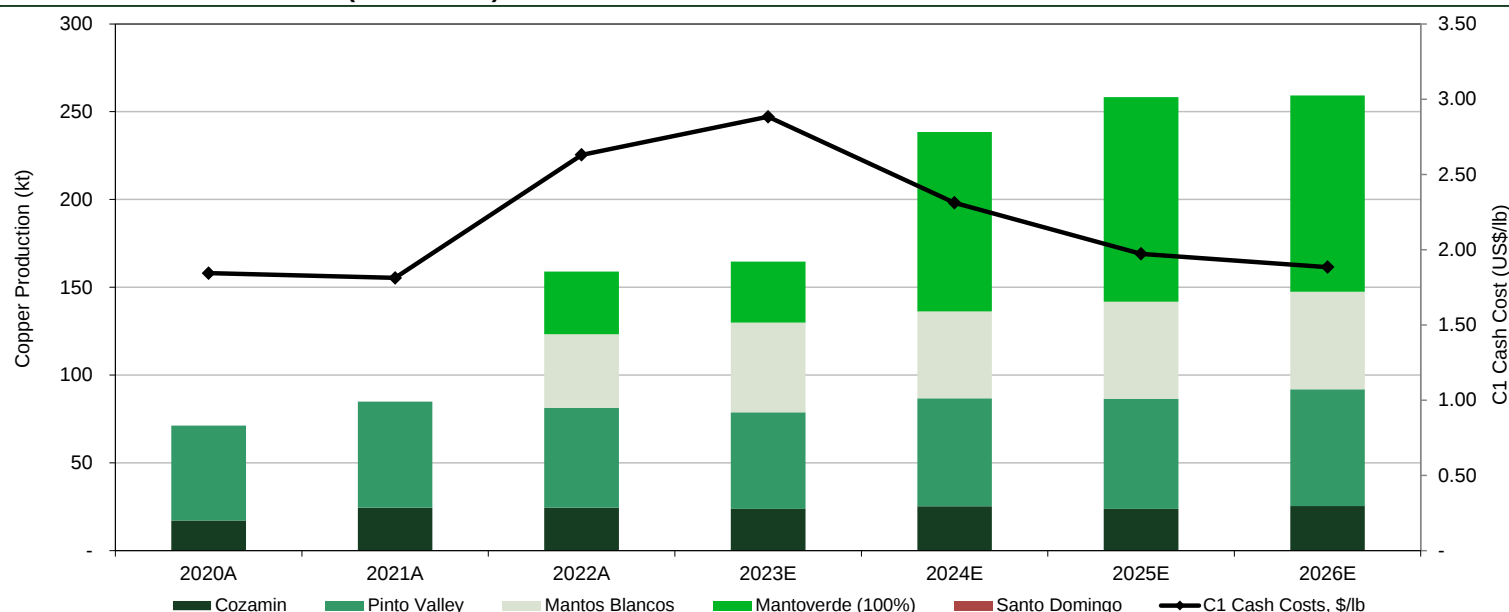
Source: Company, TD Securities Inc.

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Exhibit 4. Production Profile (100% basis)



Source: Company, TD Securities Inc.

Potential milestones/catalysts:

- MVDP completion and commissioning – Q4/23
- Updated Santo Domingo FS including MV-SD district synergies – H1/24
- MVDP Optimization Feasibility Study – H1/24
- Mantoverde Phase II Feasibility Study (twinning of Phase 1, ~90ktpd) – H2/24
- Mantos Blancos Phase II Feasibility Study – H2/24
- Pinto Valley District Growth Study – H2/24
- MV-SD Cobalt Roaster Feasibility Study – H2/24

Valuation

Capstone is currently trading at 0.70x our base-case 8% NAVPS estimate of C\$6.92 (previously C\$7.00) using a 0.78 Canadian dollar/U.S. dollar exchange rate vs. its peer-group average of 0.85x.

Justification of Target Price

Our target price of C\$7.00 is based on an EV/2024E EBITDA multiple of 6.0x (weighted 40%) and a 1.0x (unchanged) multiple to our Mining Assets NAV-8% weighted 60%.

Key Risks to Target Price

The main risks facing the company include financial, technical, political, and forecasting risks related to deposit size. Among other things, these include risks related to copper, gold, silver, zinc, lead, and fuel prices; the governing fiscal and legislative regimes; the timing of key developments; market conditions; capital and operating costs; foreign exchange rates; resource estimates; operating parameters; permitting; environmental issues; indigenous people; debt levels/the potential for a covenant breach; and staffing and key personnel retention.

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Capstone Copper Corp.	CS-T	n/a

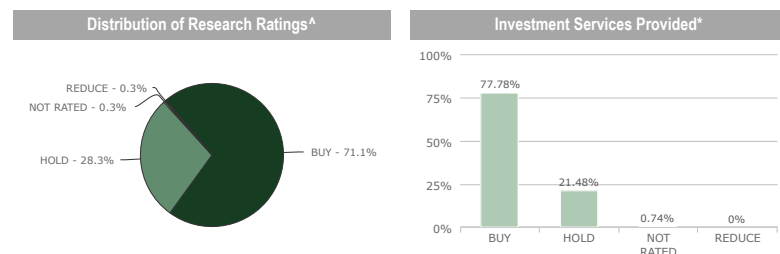
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On November 14-17, 2022, we visited Capstone's Mantos Blancos, Mantoverde and Santo Domingo assets in Chile. The Mantos Blancos, Mantoverde, and Santo Domingo assets account for approximately 12%, 30%, and 15% of our mining NAV estimate, respectively. The company provided on site transportation, accommodation, and meals.

Price Graphs

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