Trickle Research

Every raging river, every great lake, every deep blue sea starts … with a trickle

Earnings Update: Q3-Fiscal 2018
Allocation Upgrade and Price Target Downgrade

Gold Resource Corporation
NYSE American: GORO

Report Date: 11/16/18

12- 24 month Price Target: *$7.35

Allocation: *5

Closing Stock Price at Initiation (Closing Px: 07/27/18): $6.49

Closing Stock Price at This Update (Closing Px: 11/15/18): $3.90

Gold Resource Corporation

(NYSE American Stock Symbol - GORO)

http://www.goldresourcecorp.com

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Disclosure: Portions of this report are excerpted from Gold Resource's filings, website(s), presentations or other public collateral. We have attempted to identify those excerpts by *italicizing* them in the text.

For Q3 2018 Gold Resource reported significantly lower revenues that we had originally modeled. Revenues came in at $24.26 million versus our estimate of $31.12 million, or a difference of $6.86 million. Just under 1/2 of the difference was related to the stark compression in metals prices over the period, while the balance was largely related to substantially lower silver grades primarily at Arista. The metal prices we understand, but the silver grades were markedly lower and unexpected. Understand, we recognize grades are a moving target one quarter to the next, and we have been told by management that they are mining their way up to what they believe will be better grades at Arista, so some gold and silver degradation was expected (although it has been offset by some better grades from the base metals) but silver grades getting cutting essentially in half is alarming to us. Obviously, the question is, is this an anomaly or the new normal? Again, the difference between 70 grams per ton silver and 140 grams per ton silver is around $4 million in revenues per quarter at prevailing milling and price thresholds. We are trying to get some clarity from management on this issue.

Expense line items were all largely in line with our estimates especially once we adjusted the model for the revenue shortfall.

Clearly, metals prices are a big driver in the Company's results. Recall from our initial thesis, while we believe investors need to consider some sort of gold exposure and we think owning miners is a good way to do that, these issues have marked exposure to metals prices, and this quarter provides a stark example of that. Granted, the 92 days in Q3 probably encountered one of the more pronounced metals sell-offs we have seen in a similarly short period of time, so we view the results as atypical, but again, this drives home the point of just how tied the success of these companies is to metals prices.

Looking ahead, it looks to us like they are beginning to achieve higher tonnage than our original model assumed. Going back over the old production data, we think this quarter was a record in terms of company production. On the other hand, we have some concerns about ongoing grades. As we noted above, management indicates that they are mining up to what they believe to be better grades at Arista. It may be that as they are simply moving more rock to get to those better grades, which is perhaps impacting tonnage (higher) and resulting grade control (lower). Frankly, we are not sure what to expect over the next quarter or two as they get to better rock. Again, we are waiting on some clarity from management. In the meantime, we have made a few adjustments around the dichotomy of higher tonnage versus lower grades.

Of course, the hammer here remains metals prices. While we must admit, watching prices fall as precipitously as they have is a bit unnerving. However, volatile asset prices are not exactly uncommon these days, which we frankly think plays into our narrative regarding central bank policy and its potential impact on gold prices. On the other hand, we also remain guarded to the notion that the global economy could be slowing, which may not be good for base metals. All of that said, we think our main thesis remains intact, which is that if gold trades over the next 12-24 months, especially given the start-up of gold operations at Isabella (which appear to be on track by the way), we think Gold Resource should reflect higher valuations around those two variables, and perhaps markedly higher than our estimates depending on how much higher (in that event) it trades.

Given the above, as we noted, we made some adjustments to the model regarding, higher production, lower grades and lower metals prices, especially the base metals. As a result of those adjustments, we are increasing our allocation of Gold Resource from 4 to *5 largely as a result of the marked compression in the stock, but we are also establishing a new (lower) 12-24 month price target of **$7.35. We will reassess each of these as we move ahead.

Projected Operating Model

Gold Resource Corp.						
Projected Operating Model						
By Trickle Research LLC						
	(actual)	(actual)	(actual)	(estimate)	(estimate)	(estimate)
	3/31/18	6/30/18	9/30/18	12/31/18	Fiscal 2018	Fiscal 2019
Consolidated Statements of Operations (000's)						
Sales, net	$ 32,151	$ 30,768	$ 24,258	$ 25,800	$ 112,977	$ 136,747
Mine cost of sales:						
Production costs	$ 15,535	$ 17,579	$ 17,363	$ 18,042	$ 68,519	$ 88,106
Depreciation and amortization	$ 3,493	$ 3,579	$ 3,515	$ 4,004	$ 14,591	$ 16,015
Reclamation and remediation	$ 203	$ 89	$ 87	$ 39	$ 418	$ 205
Total mine cost of sales	$ 19,231	$ 21,247	$ 20,965	$ 22,085	$ 83,528	$ 104,326
Mine gross profit	$ 12,920	$ 9,521	$ 3,293	$ 3,716	$ 29,449	$ 32,421
Costs and expenses:						
General and administrative expenses	$ 2,354	$ 2,225	$ 2,140	$ 2,316	$ 9,035	$ 9,935
Exploration expenses	$ 1,185	$ 1,251	$ 1,304	$ 970	$ 4,710	$ 4,949
Other expense, net	$ 278	$ 510	$ 568	$ 250	$ 1,606	$ 475
Total costs and expenses	$ 3,817	$ 3,986	$ 4,012	$ 3,536	$ 15,351	$ 15,359
Income before income taxes	$ 9,103	$ 5,535	$ (719)	$ 179	$ 14,098	$ 17,062
Provision for income taxes	$ 3,646	$ 1,781	$ 62	$ 68	$ 5,557	$ 4,964
Net income	$ 5,457	$ 3,754	$ (781)	$ 111	$ 8,541	$ 12,098
Net income per common share:						
Basic	$ 0.10	$ 0.07	$ (0.01)	$ 0.00	$ 0.15	$ 0.21
Diluted	$ 0.09	$ 0.06	$ (0.01)	$ 0.00	$ 0.15	$ 0.21
Weighted average shares outstanding:						
Basic	57,120,077	57,315,472	57,642,966	57,642,966	57,430,370	57,642,966
Diluted	57,911,299	58,314,123	58,314,123	58,314,123	58,213,417	58,314,123

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Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "Speculative Buy" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.

A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.

A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.