INVESTMENT NOTE
DECEMBER 2021

REAFFIRMING EQUINOX GOLD INVESTMENT THESIS

A deeply discounted gold opportunity

MASSIFCAPITAL

THESIS

Equinox is a mid-tier gold producer specializing in North and South American Assets with top-tier management and a fully-funded growth pipeline that will roughly double production by 2024 and is currently trading at ~0.5x of our probability-weighted net asset value (NAV).

FIRM OVERVIEW

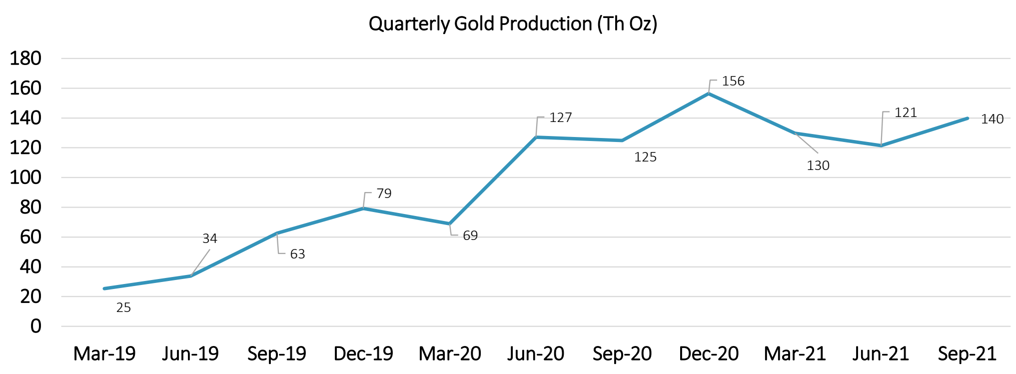
Equinox Gold is a North and South American focused gold miner that has advanced from a single run-down asset in 2018 to a multi-asset producer and developer that will soon be mining more than 1-million ounces of gold per year.

The firm has built itself up through a mixture of intelligent brownfield extensions of existing assets, greenfield development, and M&A. The firm is led by Ross Beaty, a well-known and highly accomplished entrepreneur within the mining industry, best known for his time as founder and CEO of Pan American Silver, the world's largest independent silver miner. Mr. Beaty currently owns 8% of EQX and is the largest single shareholder. The executive team and directors have built more than 50 mines over nearly 500 years of cumulative mining experience. Between Mr. Beaty and the management team, only one other producing gold miner we are aware of has greater insider ownership.

The firm has a strong balance sheet, with a US$400 million revolver, cash flow from seven operating mines in a robust gold price environment, and supportive long-term shareholders. The firm has a clear plan to produce more than one million ounces of gold per year from its existing asset base and development projects. Of the firm's existing assets, seven mines Mesquite, Castle Mountain, Los Filos, Mercedes, Aurizona, Fazenda, and RDM are all in production. Two mines, the Santa Luz and Greenstone, are in construction, and the firm is also advancing expansion projects at Los Filos, Aurizona, and Castle Mountain.

EXISTING PRODUCTION

EQX currently has seven operating mines with expected production of between 560,000 and 625,000 ounces this year. Proven and probably reserve across all assets is 16.4 million oz.



EQX management has grown existing production at a quarterly CAGR of 19% since Q1 of 2019.

FUTURE GROWTH

The firm currently has five growth projects underway that, when all in operation, sometime in 2024, will boost firm production to more than 1.2 million ounces at an average AISC of between $750 and $850 an ounce. Growth projects include:

Santa Luz Project: Full-scale construction is underway with the objective of restarting production at the mine, located in Bahia State, Brazil, during the first quarter of 2022. Santa Luz is expected to produce 903,000 oz of gold over an initial 9.5-year mine life, with additional upside from underground mineral resources. Initial Capex is roughly $103 million, and construction is 70% complete as of the end of the 3rd quarter of 2021.

Los Filos Expansion: Los Filos was acquired as part of the Leagold Merger; the current expansion project includes the development of the underground Bermejal deposit and expansion of the Los Filo open-pit mine, and construction of a carbon-in-leach processing facility to complement the existing heap leach facilities. Average annual production from the expanded Los Filos will be 350,000 oz at an AISC of $694. The mine has P&P reserves of 4.5 million oz.

Greenstone: Management acquired a 50% interest in the Greenstone Project through its acquisition of Premier Gold Mines and acquired an additional 10% from Orion Mine Finance Group in April 2021. The project will be advanced in a 60/40 joint venture partnership by Equinox Gold and Orion. Construction started earlier this year with an expectation that the open-pit mine would produce more than 5 million ounces of gold over an initial 14-year mine life at an AISC of less than $700 an ounce. The initial capital cost of development is $1.23 billion. The first gold pour is expected in H1 2024.

Aurizona: The planned expansion of the Aurizona mine includes an underground development and satellite open-pit deposits. The expansion will extend the Aurizona mine life to 11 years, with an average annual production of 137,000 oz of gold per year and a life-of-mine total output of 1.5 million oz of gold. Total initial capital costs are estimated at $154 million. Sustaining capital for the life of mine is estimated at $383 million.

Castle Mountain: Castle Mountain was designed as a multi-phase asset, with the first phase commencing operations on September 17, 2020. The Phase 2 Expansion will increase production from the mine to over 200,000 ounces with a life of mine AISC of $858/oz.

CAPITAL ALLOCATION

The gold mining industry has suffered several bouts of lousy capital allocation in recent years, making investors rightly skeptical of the industry. Although it is challenging to say the industry has turned a corner in terms of capital allocation discipline, there are certainly indications. More importantly, EQX has a demonstrated track record of intelligent capital allocation that bucks the trend of the broader industry.

The history starts with the firm's acquisition from New Gold of the Mesquite Mine in 2018. At the time of purchase, the asset had a limited life of no more than three or so years. Since the acquisition, Mesquite has generated free cash flow for the firm of roughly $139 million vs. the acquisition cost of $158 million, which is a FCF return on invested capital of 87% since September 2018. Additionally, management has invested in understanding the asset geology and has added more than 670K oz of gold to the assets resource base.

The Aurizona mine, an open-pit mine in Brazil, started production roughly a year after the Mesquite acquisition. To bring the Aurizona mine into production (it had been placed in care and maintenance in 2016), EQX management invested roughly $160 million. By the end of the second quarter of 2021, Aurizona, had yielded approximately $175 million in free cash flow for the firm, a FCF return on invested capital of roughly 109% in less than three years. Management also expanded the asset resource base, adding roughly 820Koz of gold.

EQX management has proven that they are not a one-trick pony when it comes to capital allocation with two spinouts of non-core assets: Solaris Resources and I-80. EQX has retained ownership in both spinouts, and the capital appreciation associated with the ownership stakes has been impressive. The combined value of the firms stakes in both companies is roughly C$377, or approximately C$1.4 in value per share. EQX shareholders have benefited from a combined 301% increase in the value of the equity stakes since their respective spinouts.

These three examples demonstrate smart capital allocation in the context of acquisitions (Mesquite), smart capital allocation in the context of organic growth (Aurizona) and smart capital allocation in the context of asset management within a broader portfolio of assets (Solaris/I-80).

INVESTMENT CONTEXT

We have invested in gold miners since Massif Capitals' inception in 2016. In the last three years, our investments have included: Continental Gold (taken out by Zijin Mining), Barrick Gold (sold), and two Ross Beaty-related firms: Equinox Gold and Lumina Gold. Of these four positions, we still hold Lumina and Equinox.

A Zijin takeout drove our exit from Continental, and our exit from Barrick was value-based exit. Although the businesses are different, we hypothesize that Equinox and Lumina provide similar gold exposure to the portfolio in the context of return drivers: Lumina is event-driven with a theoretical sale of the firm's key asset, and Equinox is a value play. Both have suffered this year. In the case of Lumina, there is not much to do; they own an asset they are trying to sell, they will either succeed at that within our time frame, or they won't. In the meantime, we sit on our hands.

Equinox is different. The firm is a producing gold miner with a rapidly expanding multi-asset portfolio. We suspect that over the time-period 2019 through 2025, they will be one of the fastest-growing producers in the gold space. The story is not complex, the management team is well known, yet the market does not appear to appreciate the situation.

The context with which this year's fall has occurred is essential. Year-to-date, gold is down only 5.4%; major producers are down roughly 20% (Angico-Eagle, Barrick, Kinross, Newmont), and mid-tier producers are down 16%.[1] Inflationary pressures certainly seem to be impacting results, or so third-quarter calls with management teams would have us believe. Still, economy-wide inflation tends to prompt increased interest in gold (for right or wrong). This means that while the inflationary pressure at the firm may weigh on costs/margins, the inflation we are experiencing in the economy more broadly would theoretically support the industry equity. This has not been the case though.

What's working in our portfolio rarely attracts our attention to the degree positions that are not working do. While we can rarely identify the exact reason for under-performance with conviction, as the short contextual discussion above demonstrates, we do like to reaffirm our thesis and underlying assumptions within the presence of under-performance.

In reaffirming our Equinox thesis, we find reasons for incremental adjustments to our valuation but no reasons to question our initial thesis. The firm's recent under-performance is likely a combination of the above elements, and without an explanation for the under-performance that is actionable, Equinox remains cheap, in our opinion.

VALUATION

We believe that Equinox Gold has a probability-weighted[2] value of C$18.3, an expected return from the current price of 118% as of the close on December 1, 2021.

At current gold prices, the firms projected cash flows discounted back at their cost of capital suggests a valuation of C$24.2 per share. A sustained 15% drop in gold prices and a 400-basis point increase in their discount rate suggests a C$14 per share valuation. Its current share price at C$8.5 is equivalent to a similar drop in gold prices, an elevated discount rate, a 50% reduction in the planned volume produced out of Los Filos and removing 100% of the over half a billion CAD in cash on its balance sheet. In other words, a lot needs to go wrong at the firm; the market needs to see significant weakness or some combination of both to arrive at its current valuation.

We believe the concerns about the recent work stoppages at Los Filos warrant less concern than the market appears to be placing on them. The management team has a proven history of political risk management skill, so we expect them to handle the associated challenges. Political risk is funny though, and people do the darndest things, which is one of the reasons we have taken a blended approach to our valuation. Reducing Los Filo's performance via reduced gold output seems to be one such reasonable approach.

Equinox does not necessarily have the gold mining world's most fantastic assets. They are not bad assets, but they are not Tier 1 assets under any definition. Warren Buffett is well known for commentating that he never wants to own a business an idiot can't run because eventually, an idiot will run the business. Mining firms suffer significantly from being businesses that idiots cannot run, nothing is straightforward, and you don't control the price of the "product" you sell. But when you get a confluence of three variables: good assets that need not be fantastic, a robust price environment, and competent management, management can usually create significant shareholder value. Equinox appears to be in just such a situation.

Footnotes

[1] *In this case we chose the following names to look at as mid-tier: B2Gold, Centerra, Coeur Mining, Eldorado, Iamgold, Lundin Gold, Oceana Gold, Perseus Mining, Pretium, SSER Mining, Torex Gold, Yamana*

[2] *Note that the probabilities we use are subjective and discrete, they should be interpreted as the mathematical manifestation of our belief in "the strength of the tendency, inherent in the [a] specified physical situation, to realize the event – to make it happen." (pg.395, Realism and the Aim of Science, Karl Popper).*

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