

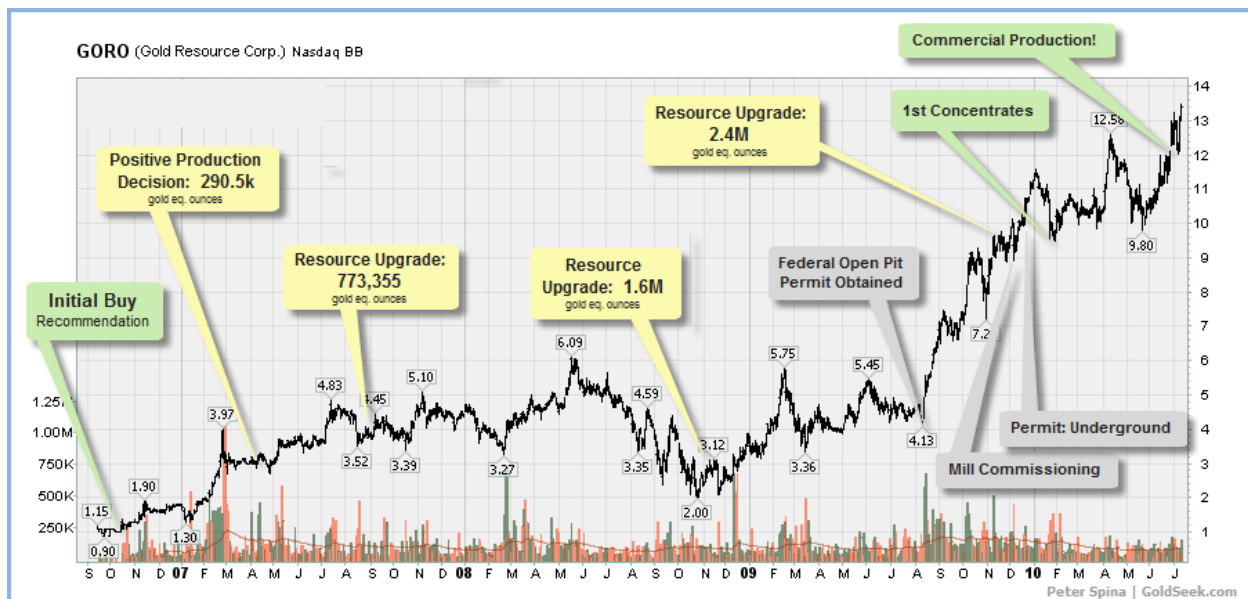
Gold Producer Targeting \$0 Mining Costs Reaches Commercial Production; Investors Preparing for Dividends and More!

14 July 2010

Commercial Production, NYSE: AMEX, Dividends – Update:

Gold Resource Corporation (GORO) made a significant announcement on July 1st by reaching **commercial production**. **1st year production** is forecasted to be **70,000 ounces** at a **\$200 cash cost**. By **year 3**, production is projected to ramp up to **200,000 ounces** gold equivalent (gold and silver) at a **\$0 cash cost**, as base metals offset costs.

The company continues to have an impressive share structure, with just **under 50 million shares** outstanding. The company has **no debt** and just announced application to list on **NYSE: AMEX**, which should open the company further up to new sources of investment capital. With the company now starting to produce strong cash flow and intending to distribute **1/3 of cash flow to investors in a form of dividends**, investors continue to revalue the share price.



The chart above shows the share price since IPO in Q3 of 2006 along with some annotations of major milestones. [Click on chart to enlarge.](#)

Give Me a Reason to Sell:

Gold Resource Corporation has undoubtedly become a very successful investment for investors as the share price continues to hit new price records, easily attracting new investment capital. What has made this company so incredibly successful is what I see as a combination of talent, vision, experience, hard-work, an incredible mining asset and perhaps one of the most important aspects to investors, management which understands what investors want. And with **management owning around 1/5th of the company**, they are highly motivated investors-managers.

Since meeting with management in 2006, the same principals-goals remain in place. Bring an ultra-low cost asset into production (done), minimizing shareholder dilution during the process (accomplished), and **reward investors with a strong share price and through dividend distributions** (completed, in progress and pending).

That is what takes me to the question; **give me a reason to sell!** Gold Resource Corp. has successfully not only outperformed the gold price but **outperformed the vast majority of public gold mining companies**, from the explorers to juniors to seniors. Yet now in commercial production, continuing to expand the size of its resources, I find it difficult to sell at these levels and under current gold-market circumstances.

So what is a share of GORO worth to me? When determining what a share of GORO could be worth, I take quite a few circumstances into consideration. Among them are: A mine life with around decade+ production (GORO is near this mark and expanding), resources increasing (significant upside through exploration – system is large and growing! Big upside through ongoing exploration), key shareholders, a quickly strengthening treasury, a growing production profile: 70,000 -> 200,000 gold eq. ounces, production costs reducing from an already low \$200 to \$0/ounce.

With gold trading around **\$1,200** and silver around **\$18**, and in my opinion heading higher by year's end and significantly higher over the next 2-3 years, should GORO meet its objectives, we will see a significant cash flow generator. So with the current gold price, GORO should generate around **\$70 million in year one production cash flow** (70k ounces at \$200/ounce cost). *Even applying a fully-diluted share structure (53M)*, I come up with \$1.32 per share in operating positive cash flow. Producers with similar production profiles are seeing valuations with a 10-12+ operating cash flow expansion (I would contend that GORO should easily receive a premium when considering the ORE GRADES), which would produce \$13.20-\$15.84 a share valuation, but just based off initial production levels.

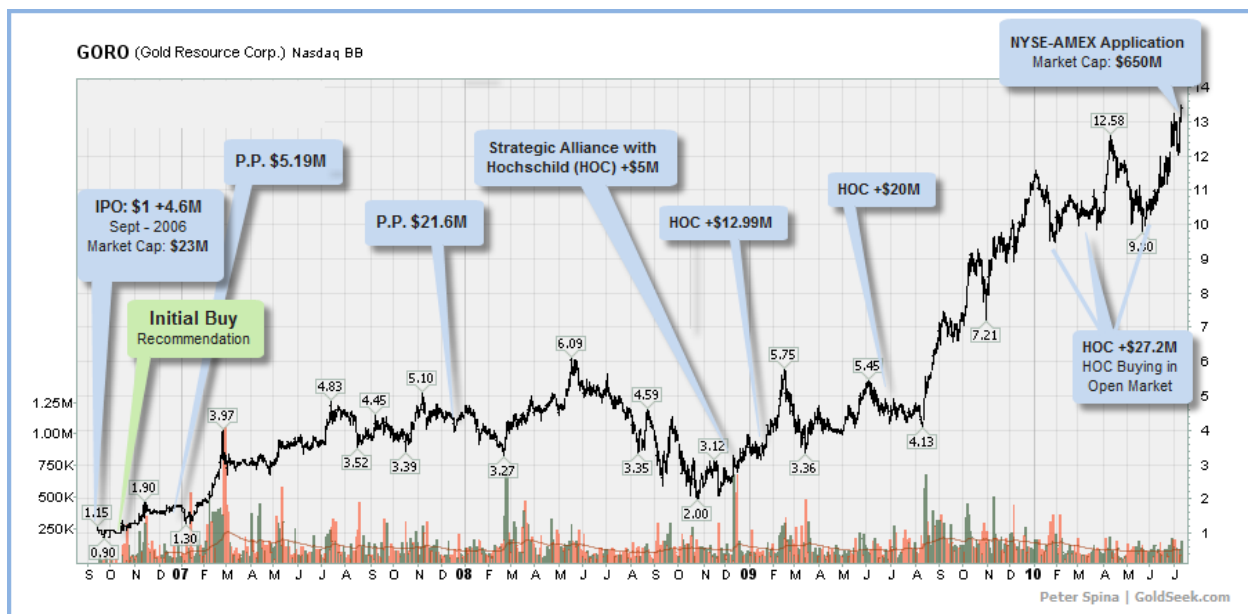
But the real treat is as the underground mine comes into production, which saw *accelerated development* with Hochschild's recent investments. Therefore reaching upwards of **200,000 gold equivalent ounces may come sooner**. Using full production figures and the associated fall in **production costs to \$0+/-**, we could see upwards of \$1/4-**billion** in operational cash-flow per year. That translates into roughly **\$4.53 a share**. Using relative valuation metrics, a 10-12+ operational cash-flow multiplier, that projects a valuation of just over **\$45-54/share**. **Plug in a \$1,500 gold price scenario**, then the valuation continues to move to even more impressive levels. When using other industry valuation models, I receive similar share price projections.

On the risk side, one factor to consider is to see what if gold prices pulled back? With GORO's large profit margin, say a \$200 an ounce drop in gold to \$1,000 an ounce (cash flow would fall to \$3.77/share at full production) would not affect the profit margins to the degree a producer which requires \$600 an ounce gold price to break even. In that scenario, GORO's profit margin would decline 16.6% versus a 33.3% for the \$600/ounce producer. Sure, there is more leverage for that risk, but that makes GORO a significantly safer investment in my view. Should gold drop to \$600 an ounce, how many gold miners would be able to survive?

The Hochschild Factor

When Hochschild (a mid-tier gold producer, major silver producer) entered as a strategic investor in late 2008, the development of GORO was about to successfully accelerate. Hochschild has historically focused on epithermal low sulphidation veins. So the investments into GORO seemed quite fitting. Not only has HOC done very well as an investor into GORO, they have provided another strong **3rd party validation of the asset and the company along with accelerating development of the asset.**

The agreement between GORO and HOC was to give HOC the opportunity to become a significant shareholder. The details of the arrangement includes a **standstill through February 2011** in which **HOC can increase its position in GORO up to 40%** (at 40% they will have 2 of 5 board director seats). The other major component has been HOC was given right of first refusal to any financings until commercial production was successfully reached – which GORO announced entering on July 1st. In fact, with commercial production just about on a steady and successful level, it is unlikely GORO will need to finance going forward. They will have instead become focused on distributing profits back to shareholders.



History of initial private placements and subsequent investments with GORO's strategic investor – Hochtchild Mining (HOC). Also of note, GORO's market cap has increased by 28 times since going IPO (\$23 -> \$650M). [Click on chart to enlarge.](#)

With roughly **\$65 million** in private placements made directly with GORO (with a current market value around **\$200M** – HOC is up over 300%!) and just recently some **purchases out of the open market**, HOC now is **approaching 30%** equity interest in GORO. *Therefore, now that GORO has been successfully funded to commercial production, the need for future financings appear quite slim, HOC will most likely need to continue to purchase shares out of the open market should it wish to reach the 40% mark.*

That means **over 5 million shares would have to be purchased to reach that 40%** level of ownership over the next several months. With GORO's tight share structure and now as it enters into commercial production, combined with the record gold and near record silver prices, I see there being little chance of HOC being able to pick up that position size around these current prices.

More realistically, they will have to see a significantly higher share price to convince shareholders like myself to shed off some shares or they will have to approach the next largest shareholders, management or other large funds. But it is my guess that they are in a similar position like many investors including myself. Under current conditions, GORO shares would have to be significantly higher to interest me.

So it is likely that at minimum, HOC should have strong interest in GORO should there be a pullback, giving some stability to a correction and ability to accumulate a larger position. Then there is the other possibility that HOC will continue to increase its equity interest into GORO, continuing its open market purchases along with other investors. That could be a powerful force as well going forward as there seems to be an ever increasing appetite for GORO now as it continues to produce positive results. And if HOC decides to pause any further accumulation, they can be quite pleased of accelerating their own returns on their very successful investment into GORO.

Conclusion

In [late 2006 I wrote](#) that,

"Gold Resource Corporation [OTCBB: GORO] is not a name most gold investors have heard of yet. With the IPO of Gold Resource Corp. back in mid-September at \$1/share, one of the newest gold companies on the market has yet to receive the recognition it deserves. Time will change this as the company and its properties are noticed."

Nearly four years later, and despite being **one of the most successful gold production stories**, Gold Resource Corporation still has a limited profile even after reaching **commercial production this past July 1** – the upside being there are a lot of potential investors who have yet to be introduced to GORO. Shareholders have little to complain about with GORO shares **appreciating over 1,300%** since its IPO in the 3rd quarter of 2006.



Beginning with a shareholder-friendly vision to become one of the world's **ultra-low cost gold producers**, GORO has achieved this major milestone. This signals the next stage of the company's evolution with the company now entering into a strong cash flow position; **shareholders are likely to see substantial dividends**.

I view the current situation in GORO as one which could **quickly revalue the company**, share price **over the coming months**. I believe we have begun to see the initial start of this process over the past few weeks. That is why I continue to keep GORO as **my largest investment** holding and carrying on the belief from late 2007 in which I described GORO as "[A Great Investment in a Great Bull Market!](#)"

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Disclosure, Conflict of Interest: *I am long Gold Resource Corporation. The company is an advertiser on GoldSeek.com, which I am the President of. I have not been compensated to publish this report. I continue to be positively biased on GORO and have been since going public in 2006. These are my opinions and mine solely. I am not a registered investment advisor. I strongly urge you to do your own investment due diligence. I strongly urge you to research Gold Resource Corporation.*

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