Transcript of
Fortuna Silver Mines, Inc.
Q4 and Full Year 2023 Financial and Operational Results Call
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Participants

Carlos Baca - Vice President of Investor Relations, Fortuna Silver Mines, Inc.
Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.
Luis Dario Ganoza - Chief Financial Officer, Fortuna Silver Mines, Inc.
Cesar Velasco - Chief Operating Officer of Latin America, Fortuna Silver Mines, Inc.
David Whittle - Chief Operating Officer of West Africa, Fortuna Silver Mines, Inc.

Analysts

Don DeMarco - National Bank Financial

Presentation

Operator

Good morning, everyone and welcome to the Fortuna Silver Mines Q4 and Full-Year 2023 Financial and Operational Results Call. At this time, all participants have been placed in a listen-only mode and we will open the floor for questions following the presentation. [Operator Instructions]. Please note, this conference is being recorded.

I will now turn the conference over to your host, Carlos Baca, Investor Relations. Carlos, over to you.

Carlos Baca - Vice President of Investor Relations, Fortuna Silver Mines, Inc.

Thank you, Jenny. Good morning, ladies and gentlemen. I would like to welcome you to Fortuna Silver Mines fourth quarter and full-year 2023 financial and operational results conference call. Hosting the call today on behalf of Fortuna will be Jorge Alberto Ganoza, President, Chief Executive Officer and Co-Founder; Luis Dario Ganoza, Chief Financial Officer; Cesar Velasco, Chief Operating Officer, Latin America; and David Whittle, Chief Operating Officer, West Africa.

Today's earnings call presentation will be available on our website at fortunasilver.com. As a reminder, statements made during this call are subject to the reader advisories included in yesterday's news release and in the earnings call presentation, financial figures contained in the presentation and discussed in today's call are presented in U.S. dollars, unless otherwise stated.

Before I turn over the call to Jorge, I would like to indicate that this earnings call contains forward-looking information that is based on the company's current expectations, estimates and beliefs and is subject to a number of risks, uncertainties and other factors that could cause actual results to differ materially from a conclusion, forecast or projection made in the forward-looking information. A description of these risks, uncertainties and other factors is set out in the company's annual information form, for the financial year ended December 31, 2022. The annual MD&A for the financial year ended December 31, 2022 and the interim MD&A for the third quarter 2023, which are all publicly available on the SEDAR website.

Certain material factors or assumptions were applied by the company in drawing a conclusion or making a forecast or projection as reflected in the forward-looking information made in this call. These material factors or assumptions are also described in the company's annual information form for the financial year ended December 31, 2023. The annual MD&A for the financial year ended December 31, 2023, and the interim MD&A for the third quarter 2023. The company assumes no obligation to update such forward-looking information in the future, except as required by law.

I would now like to turn the call over to Jorge Alberto Ganoza, President, Chief Executive Officer and Co-Founder of Fortuna.

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

Thank you, Carlos. Fortuna had a strong close to 2023. In the fourth quarter, we recorded $66 million in free cash flow from ongoing operations which is consistent with the $70 million recorded in the third quarter. We achieved a record 136,000 gold equivalent ounces in the period as well and realized an average gold price of $1,990 per ounce, yielding record sales of $265 million or consolidated ASIC for the period was $1,509 per gold equivalent ounce.

We're using the strong proceeds of the business to advance payments on our corporate credit facility, paying $40 million in the third quarter, $41 million in the fourth quarter. And subsequent to year-end, we paid an additional $25 million between the end of February and early March. We have a favorable debt-to-EBITDA ratio of 100:0.3 and a total net debt of approximately $83 million, providing enhanced flexibility to our balance sheet through debt reduction is one of our capital allocation priorities in 2024, and we expect to achieve zero net debt during this year.

Another capital allocation priority is funding high-value organic growth opportunities in the portfolio and attractive acquisitions in the regions where we are already established. For $38 million exploration program this year includes 200,000 meters of drilling with a focus on Diamba Sud in Senegal and Séguéla in Côte d'Ivoire. For reserve replacement, our priorities continue to focus on the San Jose and Yaramoko mines. In the short to medium term, both the Diamba Sud project in Senegal and the Séguéla mine in Côte d'Ivoire are our strongest drivers for growth and value.

As David Whittle, our Chief Operating Officer for West Africa will explain later. At Séguéla, at the end of December, we are processing ore at a rate which is 26% higher than nameplate capacity and encountering positive grade reconciliation at the starter Antenna pit in the fourth quarter, we obtained 24% more gold ounces than predicted by the reserve model. And the priority continues and the property continues to offer tremendous discovery opportunities, which we are diligently pursuing with our exploration.

At Diamba Sud, we currently hold 850,000 ounce gold resource, which we cataloged as historical and has not been incorporated to our consolidated resources. We expect to enhance our knowledge of the mineral deposits and expanded with our ongoing 45,000-meter drill program and being in a position by year-end to deliver a preliminary economic assessment. And both the San Jose and Yaramoko mines, we continue pursuing reserve replacement with well-funded drill problems. At San Jose, we are targeting in achieving high-grade silver gold discovery made in 2023. And in Yaramoko we have achieved a lot of success expanding reserves on the fringes of the Zone 55 deep ore body. We will be reporting on results from our exploration programs in West Africa and Latin America later in March.

And another capital allocation consideration is our share buyback program, which was under a temporary restriction placed by the credit facility bank syndicate. This restriction was lifted by us in early January. And with the financial results blackout behind us, we may now participate again in the market and considering available liquidity, capital allocation opportunities and the state of the company valuation in the market, we may be participating again in the market, as I said.

So with that, I will now let our Chief Operating Officer provide some further detail on our operations to the region. So we can start with West Africa. David, do you want to go ahead?

David Whittle - Chief Operating Officer of West Africa, Fortuna Silver Mines, Inc.

Thanks, Jorge. Séguéla and Yaramoko had a successful fourth quarter from both a safety and production perspective. Both mines recorded zero LTIs and Yaramoko reached an exceptional milestone of three years LTI fleet in 2023 and attained ISI 1401 and ISI 45001 certifications. In the fourth quarter, Séguéla produced 43,096 ounces of gold, a 37% improvement compared to the previous quarter and delivered 78,617 ounces of gold to 2023, outperforming annual production guidance by 5%.

The Yaramoko strong production performance delivered 28,235 ounces of gold leading to 117,711 ounces of gold for the year, achieving the higher end of the revised annual production guidance. In the fourth quarter, Séguéla mine 409, 293 tonnes of ore, with an average gold grade of 3.4 grams per tonne and 2,214,681 tonnes of waste strip ratio of 5.4. Ore process was 397,267 tonnes at 3.62 grams per tonne of gold. Mining operations focused mainly on the Antenna pit to drive ore feed to the processing plant. But the Antenna pit ore road and other development was completed and top soil and waste stripping commenced with 104,472 tonnes of waste stripping being achieved. Preparations for the mining of the Koula pit commenced during the quarter with great control drilling and ore road construction being undertaken.

Processing plant operations continue to ramp up beyond the nameplate capacity of 154 tonnes an hour during the quarter, achieving an average throughput of 186 tonnes per hour. In December, an average throughput of 194 tonnes per hour was attained 26% higher than design. A partial mill reline was undertaken in February, and we are now successfully further testing throughput constraints. Gold recovery for the quarter was 94.9%, slightly ahead of the 94.5% design recovery, benefiting from the higher head grade.

The second lift of the tailing storage facility is currently under construction and is expected to be completed by the end of this quarter. This will assure adequate tailings storage for another two years of production of the increase throughput upgrades. Séguéla's strong performance resulted in both a cash cost of $341, and an ASIC of $737 per ounce of gold, both below guidance. At Yaramoko, mine production in the fourth quarter of 2023 was 112,906 tonnes at an average grade of 7.33 grams per tonne gold. Mining operations were primarily sourced from the 55 Zone underground mine. Development and stoping operations at the Bagassi South mine contributed 10,162 tonnes and 6.05 grams per tonne gold to the above outputs with batch treatment and Bagassi ore sharing a very close correlation to the mine ore.

On the processing plant, 110,445 tonnes were treated at an average grade of 7.16 grams per tonne gold, with a recovery at 98.3%. The decreased processing tonnes are attributed to a planned shutdown for 11 days in December '23. The enhanced production resulted in the cash cost in ASIC at Yaramoko being below the lower end of annual guidance for the year at $870 and $1,499 per ounce of gold, respectively. Development operations and diamond drilling success and will further strike extensions of the 55 Zone ore body to the East of the expected mining boundaries as well as strike extensions and minable displays of the QV Prime ore body at the Bagassi South mine. Back to you, Jorge.

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

Thank you, David. And Cesar, you want to provide your report, please.

Cesar Velasco - Chief Operating Officer of Latin America, Fortuna Silver Mines, Inc.

Yes. Thank you, Jorge, and good afternoon to everyone. In 2023, our Latin American operations successfully delivered 130,310 ounces of gold, 5.9 million ounces of silver, 40.9 million pounds of lead and 55.1 million pounds of zinc. Consolidated gold production achieved guidance, enabled mainly by Lindero producing 101,238 ounces. The consolidated silver production was 7% below guidance due to San Jose's lower tonnage extracted from the mine as it has to deal with a 15-day stoppage at the beginning of the year, operational difficulties thereafter and reduced grade profile as we are operating at the tail end of reserves.

Base metals with its exceptional lead and zinc production was 28% and 15% above guidance, respectively. Starting in Argentina, Lindero's gold production for the fourth quarter was 29,591 ounces, a significant increase of 41% when compared to the previous quarter. This increase was enabled by higher gold production and the extraction of 4,600 ounces contained in fine carbon and copper precipitate. Gold production for the year totaled 101,238 ounces, achieving midpoint of annual production guidance. In the fourth quarter, a total of 2.1 million tonnes of ore were mined at a stripping ratio of 0.6:1, leading to a stripping ratio of 1.14:1 for the year, aligned with the mining plan.

During the same period, a total of 1.6 million tonnes of ore were placed on the leach pad at an average gold grade of 0.63 grams per tonne containing an estimated 31,665 ounces of gold. Lindero's annual cash cost of $920 million and ASIC of 1,565 per ounce of gold were both within guidance. To note, cash cost on ASIC have been affected by adverse in-country macroeconomic conditions during 2023, compounded by an increase in sustaining capital expenditures mainly related to the heap leach expansion project. These costs were partially offset by improved copper byproduct sales totaling $7.7 million.

As of the end of February 2024, the $41 million leach pad expansion project is approximately 28% progress with completion planned by the end of 2024. Those $41 million equates roughly to $410 on the ASIC for 2024. While this investment weighs heavily on the company's ASIC as for this year, it would greatly benefit Lindero by allowing the placing of reserves over the next decade.

In Mexico, San Jose produced 1 million ounces of silver and 6,341 ounces of gold in the fourth quarter of 2023 with average head grades of 145 grams per ton and 0.91 grams per ton, respectively. Total production for 2023 was 4.7 million ounces of silver and 28,559 ounces of gold, 12% and 16% below annual guidance, respectively.

The decrease in production, as I mentioned before, is attributed primarily to the 15-day illegal union blockade in the second quarter. The associated disruption to operations thereafter, a silver and gold head grade reconciliation to reserves at the lower end of guidance range and the mine that offers less operational flexibility, and it is working on the tail end of reserves.

We continue to experience significant inflationary pressures in Mexico beyond what we see in other countries where Fortuna operates. The 2023 cash cost of $14.40 and ASIC of $19.40 per silver equivalent ounce were above guidance. Higher costs are mainly explained by a significant appreciation of the Mexican peso, which affects approximately 50% of our total cost in addition to higher labor, contractor material and consumable costs, lower ounces produced and lower head grades, all of which are also carried into 2024 estimates.

Based on exploration outcomes, and the remaining life of reserves, the company is preparing to execute a multi-year progressive mine closure and monitoring plan, in strict compliance with government regulations and adhering to high international standards. In Peru, the Caylloma mine produced 330,478 ounces of silver at an average head grade of 88 grams per tonne in the fourth quarter. Silver production for 2023 totaled 1,227,060 ounces surpassing the upper end of guidance by 10%.

Lead and zinc production for the quarter was 10.8 million pounds and 14 million pounds with head grades averaging 3.84% and 5%, respectively. Caylloma delivered strong base metal production in 2023, totaling 40.9 million pounds of lead and 55.1 million pounds of zinc, surpassing guidance by 28% and 15%, respectively. Enhanced production was the result of positive grade reconciliation to the reserve model in levels 16 and 18 of the Animas vein.

Back to you, Jorge.

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

Thank you. We will now proceed with a review of our financial results, Luis please.

<u>Luis Dario Ganoza - Chief Financial Officer, Fortuna Silver Mines, Inc.</u>

Yes. Thank you. So for Q4 2023, we have recorded a net loss attributable to Fortuna shareholders of $92.3 million, explained by an impairment charge of $90.6 million related to the anticipated closure of the San Jose mine in late 2024. As has been previously disclosed, the updated mine plan is scheduled to exhaust mineral reserves by the end of this year compared to mid-2025 as previously planned.

Adjusted net income in the period was $20.6 million or $0.07 per share compared to $6.4 million or $0.02 per share in the prior year. In the quarter, we have adjusted for several non-recurring items, all of them except one are non-cash charges. I will briefly describe them on a pretax basis. The main one is the impairment at San Jose, as I just mentioned. Under cost of sales, we have adjusted $15.4 million of write-downs comprised of $9.5 million of materials inventory at various sites and $5.9 million of low-grade stockpiles at Lindero.

The materials inventory write-downs are related to a reassessment of consumption plans at San Jose in the face of the shortened life of mine for $4.4 million with a balance corresponding to Yaramoko and Lindero. The write-down of low-grade stockpiles at the Lindero mine was triggered by anticipated higher costs to completion over the life of mine. It is worth pointing out that this write-down doesn't necessarily bring into question the economic viability of the stockpiles as the decision to stockpile low-grade ore follows an incremental cost logic, while the accounting allocates costs based on an average cost method.

Under the line item labeled write-off of mineral properties, we have adjusted for a full $5.3 million amount, which is related to Greenfield's exploration projects in Mexico and Argentina. Under other expenses, we have adjusted for a $6.4 million severance provision at San Jose related to the scheduled mine closure and $1.2 million of custom penalties at Séguéla related to the construction phase.

So back to adjusted net income. The main drivers of the increase over Q4 2022 were the contribution of the Séguéla mine, which explains the 71% higher volume of gold sold and higher gold price of 15%, which resulted in an average of $1,990 per ounce for the quarter. Our cash cost of sales per gold equivalent ounce sold was $840 compared to $873 in the prior year.

As David mentioned, cash costs at Séguéla was $322 per ounce, that would be $376 per ounce if we included capital leases related to the mining contractor, which are reported as part of ASIC, but excluded from cash cost per ounce. The contribution of low cost ounces from Séguéla was partially offset by higher cash cost per gold equivalent ounce at Yaramoko, Lindero, and San Jose in the quarter.

For Yaramoko, this was primarily due to higher operating costs in Q4, partially offset by higher head rates. In the case of Lindero, the higher cost per ounce was mostly aligned with the expected reductions in head rates consistent with the mine plan. And for San Jose, this was mainly due to a shortfall of production in the quarter compared to the mine plan and lower head rates and the effect of the peso appreciation as noted by Cesar.

Depreciation and depletion for the quarter was $71.6 million compared to $44.5 million in the prior year. The increase of $27 million is explained by the higher gold equivalent ounces sold and higher depletion per consolidated gold equivalent ounce of $67. This higher depletion on a per ounce basis is related primarily to Séguéla where total depletion and depreciation was $26 million including $17 million corresponding to the purchase price allocation from the Roxgold acquisition.

On income taxes, we have recorded $27 million of current income tax compared to $7.8 million in Q4 2022. The increase is mostly explained by Séguéla. We note that tax paid in the quarter was $6.3 million as we will be paying taxes for the first time at Séguéla in 2024.

Moving on to free cash flow and liquidity. We reported $66 million of free cash flow from ongoing operations. This is after sustaining CapEx and corporate expenses. Our total liquidity at the end of the quarter was $213 million, up $51 million from the end of September 2023, reflecting the strong free cash flow generation in the quarter. We paid down $40.5 million of debt in Q4 2023 and have made, as Jorge pointed out, subsequent payments of $25 million up to the beginning of March.

Finally, at the end of 2023, our total net debt was $83 million, down from $134 million in September of 2023. Back to you, Jorge.

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

Thank you. Operator, we can open the room for Q&A.

Operator

Perfect. Thank you very much. We are now opening the floor for questions. [Operator Instructions]. Thank you. Our first question is coming from Don DeMarco of National Bank Financial. Don your line is live.

Q: Thank you, operator. And good morning Jorge and team. A couple of questions on Séguéla. First off, looking at your guidance, I mean, what drove Séguéla ASIC guidance higher in '24? Because we see that Q4, you're still running at $737 an ounce, but then the midpoint next year is $11.70?

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

Yes. As you can see, Don, in the second half of the year or average strip ratio has been around 5.4%, and that is set to increase in accordance to our plan to around 8% to 9%. The life of mine strip ratio of Séguéla is around 13%. We have initiatives to optimize that with the underground trade-off studies that are ongoing right now, but that's what's currently in the plan.

So in the second half of the year, in the first two quarters of production, we have benefited from low strip ratios and shorter haulage distance. Moving onward into 2024, first strip ratios will increase in accordance to plan and our haulage distances will increases. So yes. That's basically where the explanation is at.

Q: Okay. Thank you. Also as a go, we've seen three quarters in a row now where recoveries have increased. Q4 was 95%. Should we flatline 95% from here on? Or do you expect it to increase further?

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

David, do you want to tackle that question?

David Whittle - Chief Operating Officer of West Africa, Fortuna Silver Mines, Inc.

Yes, I can respond to that. Obviously, the first couple of quarters, we were mining predominantly the Antenna Stage 1 ore, which was probably higher grade than the life of mine grade. So we're expecting still to retain around that 94.5% to 95% in terms of the life of mine recovery.

Q: Okay. Good to know. Shifting over to San Jose. You're spending $5 million on drilling this year at San Jose at Yessi. What do you need to find here to be able to keep the mine open? Or is that even an auction?

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

No, it's certainly an opportunity that we value. So we currently have three drill rigs advancing on the Yessi. I have to say that it took us a while to understand the geology of the -- and the geometry of this structure. It has an orientation, a strike orientation that is different to what we're used to seeing, and that is made it difficult at the beginning, but we find it as an exciting feature of this new vein.

But now we have a well-defined plan that we are hitting hard with drilling before it was a bit drilled to understand, and now is we're drilling for volume. So I would expect that by midyear, we have a better graph on how meaningful this discovery is. As I always say here, we had at the Yessi an exciting discovery. Now we need to see it through into an exciting resource, right? We are currently working for that second component of this.

And as I said, we're hitting it hard all of our drilling. The $5 million is our funding drilling that are concentrated in this area. And we don't know the limits of it yet. And the expectation is that we can define volumes and resources, tonnages starts getting a grasp on that by midyear. So that will dictate -- that outcome will dictate or view on how to treat the mine plan moving forward.

As it sits today, we're exhausting reserves by the year-end. We have other resources in the mine, and the team is currently working on optimization opportunities and on the Victoria resource, for example, to see if we can extract some more and waiting at the same time for outcomes of the Yessi vein exploration. Also I think we'll have a better idea of how the winding down of -- potential winding down of mining will look closer to midyear. But parallel to all of this, we are advancing updating our plans and keeping flexible.

Q: Okay. Sounds great. We'll look forward to an update on Yessi around midyear then. Thank you, Jorge. That's all for me.

Operator

Thank you very much. [Operator Instructions]. Okay. We don't appear to have any further questions in the queue at the moment. I will now hand back over to Jorge for any closing comments.

Jorge Alberto Ganoza - President, CEO and Director, Fortuna Silver Mines, Inc.

I just want to stress that our business continues to show strength from the perspective of free cash flow generation. It has been a good end of the year, and we look to an exciting 2024. So with that, Carlos, you want to...

Carlos Baca - Vice President of Investor Relations, Fortuna Silver Mines, Inc.

Thank you very much, Jorge. I would like to thank everyone for listening to today's earnings call. Have a great day.

Operator

Thank you very much. That does conclude the conference call for today. You may disconnect your phone lines at this time, and have a wonderful rest of the day. Thank you for your participation.