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After PDAC, opportunity emerges in junior miners

Turmoil breeds opportunity

The TSX Venture Exchange often dips following the annual Prospectors & Developers Association of Canada (PDAC) convention held each March in Toronto, and this year is no exception. Interest in junior mining conferences even declined with PDAC essentially flat versus 2012, the Mineral Exploration Roundup conference dropping 5%, and the Cambridge House Vancouver Resource Investment Conference attracting 13% fewer attendees.

Part of the market decline can be attributed to the current financing environment and the solvency of many junior companies. According to Canaccord Genuity analysts, over 575 junior mining companies have less than $500,000 in cash and equivalents reflected on their last reported balance sheets (predominantly September 2012). Analysts believe that many companies are likely struggling to cover overhead and do not have the funds to invest in exploration and development.

Turmoil breeds opportunity. Many analysts suspect that underfinanced junior companies will be forced to undertake austerity measures and divest assets. While unfortunate for those companies, it is welcome news to those with healthy balance sheets who can use their advantage to acquire quality assets at discount prices. For the discerning (and patient) investor, spending some time sifting through the rubble could prove to be worth the effort.

Given the current state of the junior market, potential investors should first determine the capital position of the company. According to Sprott Asset Management, a publicly-traded junior exploration shell needs a minimum of $300,000 to $400,000 per year to stay afloat and a company with anything less than $500,000 is extremely vulnerable.

If a company is well financed, the question is how long they can remain solvent. Investors should find out about current and projected burn rates. If a company has cash now but is burning through its reserves due to onerous costs or poor decisions, their cash advantage will soon dissipate. Assuming a company is careful with their finances and perhaps planning accretive acquisitions, investors need to determine how the company plans to finance the acquisitions and when cash flow can be expected.

Quality management is key. A junior mining company can have the best property on the market but, if the management team lacks the experience to get things done, the underlying value will never come to fruition. Management should also have a significant vested interest in the company.

Analysis should be done to assess who currently owns the shares. Investors should determine the prices of previous financings and whether the stock from those financings is free-trading. If shares are purchased at higher levels than previous

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financings, then investors need to be concerned whether existing shareholders will be doing any profit-taking, thereby affecting stock price.

Finally, investors should also assess the overall quality of the assets. Not only should the property have high potential for good exploration results, it must be in a politically stable jurisdiction with the necessary infrastructure in place to execute plans.

The junior markets have certainly been difficult the last few years; however, there will always be leading companies who emerge victorious. Investors who do their homework will know who is coming out of the turmoil stronger and better.

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