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Callinan Cash Arms Dalton for Further Deals

• *Market conditions have got "even better", says Altius boss Brian Dalton* • *"By better, I mean worse."* •

IN LATE 2013, Altius Minerals owned just one cash-flowing royalty, a 0.3 per cent claim over Vale's Voisey's Bay nickel mine in Labrador. Less than 18 months later and it is now sitting on 13 in 9 different commodities, including coal, potash, copper and zinc.

It is a rapid transformation for a company that until recently was seen by the market as a frontier exploration stock in a high cost region, the remote snowy no-man's land of northeastern Canada. Its latest deal however, a C$112m ($90m) takeover of Callinan and its 4 per cent royalty over the 777 mine in Flin Flon, positions the company for yet more acquisitions.

Altius is paying C$10m in cash and C$102m in stock, but cash of C$36m sitting on Callinan's balance sheet allows Altius to take a third bite at the current mining downturn, having already swallowed a portfolio of royalties in 2014.

"This is an opportunity-rich environment," chief executive Brian Dalton told analysts on a conference call, saying signatures had been traded in the small hours of Thursday morning. Market conditions in the last year have got "even better", he said. "By better, I mean worse, by most people's perspective, but bad markets are when companies are built and grown."

Callinan Royalties

Founded in 1927, Callinan moved to the main board of the Toronto Stock Exchange just two weeks ago, having recently settled a legal dispute with HudBay Minerals, the operator of 777, an underground copper-zinc mine. The settlement rolled its royalty from a net profits interest, heavily exposed to the cost of underground mining, into a flat 4 per cent royalty on revenue.

Altius has maintained a toehold in Callinan, but the settlement opened the door to combining the two companies, Dalton said, with a takeover unanimously backed by both boards. "It's an obvious deal," says US-based investor Adrian Day of Adrian Day Asset Management, a large shareholder in both companies. "It's a logical fit and there'll be a lot of cross-ownership, so I think people are going to be happy to get Altius paper."

Stripping out Callinan's cash and Altius' existing 6 per cent stake and the deal cost 5 to 7 times Callinan's royalty cash flow of $10m to $13m per annum. As of HudBay's latest update, 777 (above) has a 6 to 8-year mine life, which Dalton says is a "minimum", given the mine's history of 50 per cent reserve replacement. "There's a lot of upside in that deposit," he said.

"Callinan have a very nice royalty," Adrian Day agrees, "but they were paying a dividend and there was nothing at this point plugging that gap when 777 depleted."

Copper, Zinc, Juice

For Altius, the deal lifts its royalty revenue to C$45m per annum, a 39 per cent hike per share. "We get important additions of copper and zinc," Dalton said. "It's a much rounder portfolio."

Royalty groups are currently glued to precious metals, but Altius has rapidly consolidated a royalty portfolio in base metals and bulk commodities, emulating the diversified strategy of the mining majors, though at the royalty level. It is a market at least 6 times larger than gold and silver, with longer resource lives. "Long lives generally mean expandability," Dalton said, "and if you're in the royalty business, expandability is the juice."

Message Board

Altius CEO Brian Dalton told a conference call on Thursday that he plans to consult investors on when to introduce a dividend. Here's the initial reaction from stock message boards:

"A dividend is a profoundly bad idea... In this environment, they can really make hay."

"The main thing for Callinan shareholders is they are in safe waters now."

"Just to play devil's advocate: what if 777 doesn't extend much beyond the projected 8 years? Then it would seem to me that we just got diluted..."

"Altius either will trade close to its peers or it will be taken over by its peers."

"They should probably put off the payment of dividends for when commodities markets are booming and they can't find other uses for their cash."

"I tend to trust [Altius] to be in the best position to know if they should offer a dividend or not."

All Eyes

"They've been so disciplined at deploying capital," says Day, "and they're very close to having the cash flow to just constantly be on the lookout for more deals. I think at this point, they see a lot of good deals in the market."

Altius is already heavy on pre-production royalties in uranium and iron ore, generated by its exploration business, but Dalton's drive to consolidate non-gold royalties should turn eyes to London-listed Anglo Pacific, its closest listed peer.

Whilst Altius has held up in the current market, Anglo Pacific, which holds a sizable royalty over Rio Tinto's Kestrel coking coal mine in Australia, has halved in the last year. "We're not going to be aggressive at all in the precious metals space," Dalton said. "We want to define this space."

3,500%

"Altius is growing this business in a relative vacuum," wrote Scotiabank analyst, Mike Hocking, who says shares are trading below 14 times full-year earnings. That compares to 46 and 49 times for Osisko and Franco-Nevada, its gold royalty peers, and 20 times for Labrador Iron Ore Royalty, a spin-off from Rio Tinto's iron ore operations in Canada.

Shares in Altius however have risen 3,500 per cent since Dalton listed the business in his twenties in 1997. "Some of our shareholders have been with us for 17 years," he said, answering questions on a possible dividend, "and we think it's about time."

"It's a wonderful success story," says investor Rick Rule, one of Dalton's earliest backers. "This young guy, I've known him since he was a painfully thin, T-shirted geologist. To watch his progress over the last 20 years, it has been very profitable to participate in."

Prospect Generators Prove their Mettle

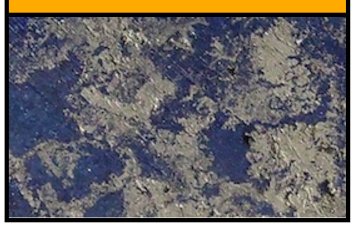
In bull markets their project partners plough money into their properties and in bear markets they mop up acreage and the assets of failed juniors, to be optioned on when markets return. Pioneered by Altius, the prospect generator model (almost unheard of in London) is a counter-cyclical answer to high risk exploration.

Thriving in the current downturn, its backers are enjoying a deserved spell in the sun.

Virginia Mines

Virginia plied the model in Quebec, leading to its Eleonore gold discovery, which it sold to Goldcorp retaining a royalty. Its C$1.3bn merger with Osisko last month in the midst of a gold bear market makes it a standout example of the model's success.

Reservoir Min.



As a conventional junior, Reservoir could never have afforded the deep drilling in Serbia that led to its Timok discovery, but by optioning the project to copper giant Freeport, it has emerged with a valuable share in the biggest copper discovery of the decade.

Lara Exploration

Led by Miles Thompson, who is also chairman of Reservoir, Lara plies the model in Brazil, Peru and Chile. Partners have included Antofagasta, Hochschild and Chile's Codelco, which is currently funding drilling at Lara's Liberdade project, Brazil.

Eurasian Min.

Like Altius, Eurasian has rolled prospecting success into royalties, including claims over part of Newmont's gold operations in Nevada and Reservoir's Timok discovery in Serbia. From Austria to Australia, the company is aggressive in mopping up land.

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