



## Brent Cook's **Exploration Insights** **Turning Rocks Into Money**

### **Exploration Insights**

by Brent Cook

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### **The Rant**

#### *Prospect Generators Redux*

The "Prospect Generator" or joint venture model is an exploration business strategy which attempts to efficiently deal with two of the key tenets of minerals exploration: 1.) over time intellectual expertise finds mineral deposits and 2.) the very business of exploration is exceptionally high risk. In effect the generator business model capitalizes on a junior company's intellectual advantage in a particular region or deposit type and passes on the high cost and risk of exploration to better-funded partners. In this way shareholder dilution is minimized and ultimately shareholders are exposed to more chances of success, albeit owning less of the big prize.

In the August 16, 2008 EI letter we discussed prospect generators and the joint venture model. This is a subject with which many of you are familiar and have contacted me about. Rather than re-hashing how this exploration business model works I recommend you read the Aug. 16 Rant. This week I include an updated spreadsheet illustrating some important statistics and comparisons for the group. As with the previous prospect generator discussion, we are offering you an interactive spreadsheet for your own research. If you are a subscriber and would like the spreadsheet just send a message to [subscriptions@explorationinsights.com](mailto:subscriptions@explorationinsights.com) and in the subject line type "generator spreadsheet".

On a share price basis the generators have by and large fared no better than the rest of the junior market participants since last year—terribly. Their business model has also become more difficult to implement. Junior partners are running out of money and are often unable to continue funding exploration as they slowly fade into the background. Major mining companies have also cut back on the exploration front, preferring to focus on ground immediately adjacent to their active mining operations (brownfields exploration). Funny thing is, when you talk to these generator guys and gal they are actually quite excited by the prospects for their future.

For the most part prospect generators have been locked out of participation in the property acquisition game over the past few years due to the availability of easy money and the lax evaluation criteria used by competitors. Much of the ground they may have desired was either staked or optioned at prices they were unwilling to pay given the high-risk nature of the properties. Likewise, major mining companies had been able to vend off good exploration properties for unreasonable front-end and back-in deals that ultimately leave the participating junior with little upside.

In exploration it doesn't make financial sense to pay money for the privilege of spending money on something that has a very low chance of success-- obvious, right? Unfortunately for many investors, a large percentage of junior deals struck during the boom times were never measured in terms of a (positive) cash flow model. To be successful with the prospect generator model the deals ultimately have to be acceptable to the intended client: a mining company. This puts a tight yoke on an otherwise excitable geologist.

Now the tide has turned in the exploration sector. Many properties are being relinquished due to high holding, option or work commitment costs. The majority of junior exploration companies have spent the dough investors gave them drilling-- usually missing. They are running out of money and will have to either walk away from properties or strike any deal they can.

Companies with both money and brains are now able to get their hands on the 10's of millions of dollars worth of information generated by previous exploration for almost nothing. David Caulfield at Rimfire Minerals points out that they are seeing more deals and properties than ever before. "Even the majors are coming to us with possible strategic relationships that would employ our group's exploration skills yet leave us with a valuable position if successful." The majors recognize the cost efficiency of using prospect generators versus the general inefficiency of their own human relations-safety-accounting-politically correct, decimated and demoralized exploration departments- *in my opinion!*

Anyway, for comparative purposes Fig. 1 below includes some of the more important generator company statistics. There is obviously more to these companies than the table shows and I include brief comments on each following the table. Although I clearly have a lot of respect for these companies, there are no specific new recommendations today. Do use today's letter to help in your own investment decisions and talk to a company if you have any questions about their activities-they know them best.

<b>Prospect Generators</b>						
'April 10, 2009						
Company	Altius	Almaden	AuEx	Eurasian	Kaminak	
Symbol	ALS	AMM	XAU	EMX	KAM	
Shares Out	28,381,818	45,759,145	34,383,457	28,515,645	36,467,520	
Share Price	\$6.88	\$0.77	\$2.12	\$0.98	\$0.10	
Market Cap	\$195,266,908	\$35,234,542	\$72,892,929	\$27,945,332	\$3,646,752	
Cash	\$160,000,000	\$12,000,000	\$10,400,000	\$9,500,000	\$4,300,000	
Marketable Securities	\$10,287,000	\$650,000	\$0	\$800,000	\$760,000	
Enterprise Value	\$24,979,908	\$22,584,542	\$62,492,929	\$17,645,332	-\$1,413,248	
Cash/share	\$5.64	\$0.26	\$0.30	\$0.33	\$0.12	
Securities/share	\$0.36	\$0.01	\$0.00	\$0.03	\$0.02	
Hard Asset/share	\$6.00	\$0.28	\$0.30	\$0.36	\$0.14	
Premium to Assets	13%	64%	86%	63%	-39%	
JV's	14	11	11	3	4	
09 JV expenditure	\$3,500,000	\$5,000,000	\$11,700	\$5,000,000	\$625,000	
09 Co expenditure	\$2,000,000	\$750,000	\$9,000,000	\$3,000,000	\$500,000	
Past JV expenditure	\$80,000,000	\$60,000,000	\$10,000,000	\$3,300,000	\$12,000,000	
Company	Lara Res.	Miranda	Mirasol	Rimfire	Riverside	Virginia
Symbol	LRA	MAD	MRZ	RFM	RRI	VGQ
Shares Out	19,246,501	44,892,010	29,258,181	25,707,251	17,800,000	29,201,776
Share Price	\$0.29	\$0.27	\$0.17	\$0.24	\$0.44	\$3.70
Market Cap	5,581,485	12,120,843	4,973,891	6,169,740	7,832,000	108,046,571
Cash	\$3,300,000	\$10,500,000	\$4,500,000	\$5,900,000	\$3,000,000	\$39,000,000
Marketable Securities	\$3,000,000	\$300,000	\$0	\$95,039	\$0	\$55,000,000
Enterprise Value	-\$718,515	\$1,320,843	\$473,891	\$174,701	\$4,832,000	\$14,046,571
Cash/share	\$0.17	\$0.23	\$0.15	\$0.23	\$0.17	\$1.34
Securities/share	\$0.16	\$0.01	\$0.00	\$0.00	\$0.00	\$1.88
Hard Asset/share	\$0.33	\$0.24	\$0.15	\$0.23	\$0.17	\$3.22
Premium to Assets	-13%	11%	10%	3%	62%	13%
JV's	2	8	3	8	3	4
09 JV expenditure	\$1,500,000	\$1,500,000	\$1,000,000	\$700,000	\$730,000	\$5,000,000
09 Co expenditure	\$1,500,000	\$1,900,000	\$1,600,000	\$1,200,000	\$1,300,000	\$3,000,000
Past JV expenditure	\$1,500,000	\$9,000,000	\$3,000,000	\$32,000,000	\$0	\$23,000,000

(Fig. 1- Prospect generator spreadsheet as of April 10, 2009)

Altius Minerals is the quintessential prospect generator and an EI portfolio member. With the help of John Tognetti, Haywood Securities, the company went public at C\$0.20 right at the beginning of the resource bear market of 1997. Over the ensuing 11 years Altius spent C\$10 million on developing and vending conceptual exploration ideas. These ideas were subsequently turned into C\$80 million worth of partner exploration through 50 joint ventures. They also paid C\$13 million for a small royalty on the Voiseys Bay nickel mine. Last year the royalty stream paid back the initial investment and is set to continue pumping out cash for at least another 20 years. Their overall business has generated over C\$220 million in sales and shows a compound share growth of 37%. They are now perpetually funded, with the revenue streams more than covering their annual burn. Al Korelin of the Korelin Economics Report and I sat down with VP Exploration Roland Butler in Calgary last week. You can listen to the interview here:

<http://www.kereport.com/DailyRadio/Daily040809.mp3>

Next is Almaden Minerals with \$14 million in cash, and gold bullion from their deposit worth about C\$1.5 million. Almaden has consistently been able to bring in joint venture partners as evidenced by the 11 current joint ventures and the recent deal struck with Antofagasta Minerals. The deal covers what appears to be a new porphyry copper prospect in Puebla, Mexico: yeah- a grassroots porphyry copper agreement in this lousy base metal environment. For a 60% interest Antofagasta must spend US\$7 million in exploration and pay \$1 million to Almaden over a five-year period. They can then take their interest to 75% by funding and delivering a

feasibility study. From what I have seen of the data this is a very sexy property. When and if I get to it you will be the first to know.

Both AuEx Ventures and Eurasian Minerals are in the EI portfolio and have previously been discussed in some detail. AuEx has a 49% participating interest in a developing gold discovery in Nevada. Eurasian has what I believe to be a high potential gold project in Haiti. We will have more to say on Haiti after a property visit.

Kaminak Gold recently spun out their Angilak uranium project into Kivalliq Energy. This resulted in Kaminak holding 11.7% of Kivalliq. Kaminak shareholders received 0.8 of a common share of Kivalliq plus 0.5 of a purchase warrant. This deal illustrates the company's commitment to shareholders both by issuing them shares and by offsetting the KAM dilution to another entity.

Lara Exploration actually made a C\$2.4 million profit last year from the sale of a phosphate deposit. This year they will continue their strategic alliance with Spratt Resource and are actively working on new advanced phosphate targets. Concerning their current portfolio projects (nickel, tin, copper and iron), they are primarily updating and refining the data package to present to potential partners. Fieldwork has slowed as President Miles Thompson and his team review a number of new opportunities. Miles says that "so far a number of interesting projects are showing up but by and large the damage in the exploration sector is not yet bad enough for us to see real bargains. As work, spending and holding costs start to accelerate we should see more reasonable deals over the next 18 months."

Miranda Gold will probably be facing a decreased drilling budget this year as some joint venture partners have cut back on exploration. Nonetheless, Miranda's geologic team continually impresses. They have been out staking claims based on some very original conceptual ideas that eventually should attract the interest of larger gold mining companies. With C\$11 million in the bank and a burn of about C\$1.9 million per year, President Ken Cunningham feels they are in a good position to expand upon their business model. However he points out that "we cannot afford to make a mistake with our money. There are a lot of tired old dog properties out there that junior companies are now trying to pass off. They are of no value to us."

Mirasol Resources has been stealthily executing their business model and is trading at slightly less than cash in the bank. President Mary Little has consistently managed to execute strong joint venture deals with mining companies. They currently have three joint ventures and active eight projects within a portfolio of 18 properties. Virtually all of these are on virgin properties (never systematically explored or drilled) which they generated through modern spectral analysis and good old boots on the ground. Mary is targeting the execution of three new joint ventures for this year.

Jason Weber, President of Rimfire Minerals, made a good point regarding the opportunities they are seeing now. Good exploration people that have been cut free from the majors are showing up on their doorstep. They are coming with ideas they may never have been allowed to pursue and are interested in a grubstake agreement with Rimfire. Jason also pointed out "that the majors are also coming back to us inquiring about some of the ideas we pitched them on five years ago. They are suggesting alliances and deals we can work with." I suspect we will see them add to their Australian and Canadian business portfolio this year.

Riverside Resources is a new entrant to the prospect generators having listed just over a year ago. They have structured a strategic alliance with Kinross covering Mexico, where President John-Mark Staude most recently worked for Teck-Cominco. They also have junior explorer Arcus Development working on two projects. Riverside is in the process of raising about C\$1 million through a 2.5 million share unit financing at C\$0.40.

Finally, Virginia Mines is going about business the same way they have for over 15 years: grassroots generative exploration and intelligent business deals in Quebec. Virginia knows Quebec geology better than probably any other company and benefits nicely from government rebates of up to 45% for exploration expenditures. A recent example of President Andre Gaumond's business savvy is the acquisition of Breakwater Resources' 50% interest in the Coulon base metal discovery. Approximately C\$33 million had been spent on the property by Noranda then Breakwater, of which Virginia contributed C\$11 million. After government rebates and C\$2 million in management fees Virginia's expenditure amounted to ~C\$4 million. Breakwater had earned the 50% from Virginia by spending about C\$20 million on the property. Virginia bought that 50% back for 1.666 million shares: effectively C\$4.75 million.

Virginia also receives a monthly C\$100,000 royalty payment from Goldcorp. These are royalties paid in advance of a variable 2% to 3.75% royalty due to them when the Eleonore deposit goes into production. Assuming a 2.5% royalty on 300,000 ounces of annual production beginning in 2013 at an \$800 gold price and discounted 5% returns them pre-tax C\$55 million at a 1.2 US\$/C\$ exchange rate. This shows up in the spreadsheet on the marketable securities line. By the way, three Canadian securities firm analysts put a \$90 million valuation on the royalty. In addition to the royalty from Goldcorp, shareholders of the old Virginia Gold received C\$10 per share for the deposit when it was purchased and shares of the new Virginia Mines spin out which we are discussing today. Not at all a bad deal and exactly what the generator model allows a company to do over time.

So that's the generator list. I personally own and have been involved with all of the companies discussed above. Without exception they are run by honest, competent and experienced management teams whose goals are aligned with shareholders. It's probably obvious that these are not companies or business plans to speculate in hoping for a quick and easy payoff. These are long term investments in people who approach minerals exploration as a business that requires time and risk management. If this exploration model appeals to you, buy them when they are cheap after gaining confidence in the management. The spreadsheet provided today is a starting point.

For inclusion in the EI portfolio there is one additional criterion. I need also to see a project that could make a material difference to a company. Although I obviously will not get it right all the time, that is the edge I think we can capitalize on. We are currently betting on Eurasian and AuEx. Looking forward we do not know who is next in line for a big discovery: we are certainly keeping watch though.

That's the way I see it.

Brent Cook

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