

The interviews below are to give you a feel for the Resource Sector. You must be either a contrarian or a victim!

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Bullion vs. Silver in the Ground: Assessing the Risks and Rewards Nov. 2013

Did you see Lawrence at the New Orleans Investment Conference? If so, for a limited time we are offering a *discount* subscription rate. Click here to access this limited time offer <http://resourceopportunities.com/discountsubscription>

Many companies in the resource sector try to sell themselves to investors as proxies for the underlying commodity. Every company in the industry that has any sort of resource works out the market value of the company divided by the ounces or pounds. The implication is that if you can buy silver in the ground for, say, fifty cents an ounce, then an investment in the company will increase at a faster pace than the price of silver.

In arriving at those measures of value per ounce, of course every company uses the approach that makes them look best against a carefully selected peer group. Some use market value per ounce. Others use enterprise value per ounce. For the number of ounces, they can use proven and probable reserves, reserves plus resources, measured and indicated resources or total resources.

And, in determining the number of ounces, some companies stick with the number of ounces of silver. Most companies with byproduct gold will convert the gold to silver equivalent. A few companies will convert the base metal credits to silver equivalent ounces. I don't like incorporating base metals into a silver equivalent, because most investors are looking at these companies as a play on precious metals.

It is vitally important that investors recognize that every ounce of silver in the ground is different from every other ounce of silver in the ground. Comparisons against peers are useful only as rough indicators of potential value and should be carefully evaluated.

Let's look at an example of the share price of a silver company over time compared to the price of silver. Please note that this is not a rigorous analysis. It is intended as a first pass to arrive at some broad observations.

For many years, Silver Standard was a go-to silver equity for investors wanting exposure to the silver market. As expected, the Silver Standard share price rose much faster than the silver price from 2003 to 2007. In that time, the silver price rose three-fold while the Silver Standard share price rose by nine-fold. That is, Silver Standard rose 3 times faster than the silver price.

But, look what happened in 2008. Silver lost 50% of its value, while Silver Standard lost 80% of its value. Silver Standard rebounded much faster than silver after the global financial crisis, but then lagged the silver price.

Over the past two years, silver again lost 50%, while Silver Standard lost over 80%.

Silver Standard went through a fundamental change over the past four years, which may account for the disconnect from the silver price in the past few years.

The first level observation is that the equity value of a silver company can provide leverage to a rising silver price.

However, that leverage also applies on the downside.

If we look a little closer, there are some other observations. In 2003, Silver Standard had about 330 million ounces of silver in the ground. By 2007, the company had about 1.2 million ounces. One could argue that the increase in value of Silver Standard matches the gain in the silver price plus the gain in resource ounces.

In other words, there may not be direct leverage to the silver price. Rather, the share price tracked the silver price, with the extra gain coming from the growth in silver resource.

In looking at some of the larger silver-dominant companies which have been around for the past 10 years, it is very clear that most of these companies have gone through swings in value far greater than the moves in the silver price. Again, this suggests leverage to silver. But, there is more to the story.

I have included the XAU in the summary as the index does include some silver companies. I wasn't able to find a better silver index, at least not one that has been around for a decade. The XAU is obviously dominated by gold companies, but it gives some indication of how the larger precious metals companies have performed.

Interestingly, most of the companies underperformed silver across the ten years. Half of the companies also underperformed in reaching a maximum value greater than the silver maximum.

If we looked at a broader cross-section of silver companies, which means looking at more of the exploration companies, we would see that the vast majority will have underperformed the silver price.

Now, this is a brutal time in the resource markets. Prices are down across the board, and maybe this is not a good time to be doing this kind of analysis. However, there are some useful observations.

It would appear that silver did better than the larger companies. And almost certainly, silver did better than the average company in the space.

But, silver did not do better than all equities. This analysis tells us that carefully selected companies can greatly outperform silver.

Let us have a closer look at the companies that did out-perform silver. What can we learn from these companies?

First Majestic rose more than **six times** faster than silver over the decade. It was more than four times ahead in reaching a maximum. So, what did First Majestic do to outperform the metal price? In that time, First Majestic developed five mines and assembled an extensive portfolio of development projects. Clearly, they weren't just sitting back waiting for the silver price to move or for the markets to recover. Management executed on a deliberate business plan that created enormous value.

Similarly, Endeavour developed three silver mines and assembled an exploration and development pipeline.

Fortuna Ventures developed a couple of profitable silver mines to outperform silver.

Silver Wheaton pioneered an entirely new investment approach: streaming. In executing that strategy, they went from a standing start to become one of the world's largest silver companies in less than a decade. Along the way, they generated

returns far ahead of the silver price.

The conclusion here is that the companies gained in value not just from the exposure to the silver market, but also because a smart management group executed a business plan which enhanced the value of the company.

The most successful of these companies have generated gains in shareholder value several times greater than the moves in the metal price.

In short, investors reward companies for enhancing value. Those gains in value can arise in several ways:

- Expanding resources
- Advancing projects toward production
- Achieving production.

It is especially important to build a company with multi-mine status. It's really important to understand the importance of becoming a multi-mine company.

Let's assume that there are two mining companies, with identical mines. If those companies merged, the value of the combined company would be significantly more than the sum of the values of the two smaller companies. The higher value arises from several factors:

- There are corporate and administrative synergies.
- There may be operating synergies.
- They will most likely achieve operating efficiencies: simply put: a typical small mine development company is run by a small group of professionals each of whom wears a few hats. A larger mining company can support a team with broader and deeper skills in each field.
- Reduced risk: Investors will see a multi-mine company as being less risky, with operational risk spread over multiple mines.
- Better access to capital: a larger company can tap into institutional investors that may not be willing to invest in smaller companies.

In spite of the clear enhancements in value, too few companies merge. Now is an excellent time to be aggressive in looking for ways to add value.

Everybody wants to know if this is the bottom of the market. Quite frankly, it may be some time yet before the popular press tells us that the resource market has turned up. In my opinion, many of the companies in this sector are still grossly over-valued. They may only be trading at a penny or two, but if they have no projects and no money, how much are they really worth?

By the time that someone rings a bell and announces that the market has hit bottom, many of the better quality companies will have doubled or tripled in value. The best quality companies are always the first to recover. People closest to the industry are quietly accumulating some of the better companies.

This is the time to buy. Don't wait until the markets are already on an uptrend.

But, be selective. A few of these companies will increase 10-20-30 fold in value over the next few years.

Mining Industry Outlook on Aug. 2013

After a really dismal year for the resource industry, there are finally signs that the market is at the bottom.

Before looking at where the markets are headed from here, let's have a quick look at a couple of indicators of the junior resource market to show just how bad the destruction has been.

The Toronto Stock Exchange Venture Index is not a perfect measure, with junior resources roughly two thirds of the index, but is probably the best indicator available of the overall junior resource market. The VIXJ declined 66% from its high in early 2011 to the low point in late June.

Another indicator is the Market Vectors Junior Gold Miners ETF, which is based on replicating the Market Vectors Global Junior Gold Miners Index. This index involves gold and minor silver, with a focus on small producing companies, but including a range of development stage and exploration companies. That index lost 82% of its value from the high in 2011 before a small rebound over the past couple of weeks.

Enough has been said here and by others about how bad the resource markets have been over the past year and the reasons for the annihilation of the sector.

Everybody wants to know when the market will turn. The little upticks at the end of both of those charts provide some cause for optimism. Those charts and others like them have shown false starts over the past year. That might be the case here again, but there are a number of factors suggesting an upturn in the not too distant future.

I'm not expecting a sharp upturn, like we saw in early 2009. The resource market at this time is very different than we have ever seen before. There is a huge and growing divergence between those junior resource companies that have real assets versus the thousands of other companies which have good intentions of making a discovery in the future but at this time, they have neither a discovery nor the cash to fund a discovery.

In 2008, share prices and commodity prices across the board fell hard, but then rebounded quickly and pretty much in tandem. Somebody could have rung a bell on January 2, 2009 to signal the bottom of the market.

Within two weeks, the venture index was up nearly 30%. It went on to triple in just over two years. Investors who came into the market in late 2008, when the negative sentiment was at its peak, on average, tripled their money in 26 months.

There was a huge influx of new money during 2009 and 2010. Quite frankly, many of those investors were pretty naïve with regard to the junior resource markets. Investors who bought companies on the basis of an expected discovery have been sorely disappointed in all but a very few cases.

Many investors are continuing their efforts to unload the shares that were bought during that period of euphoria.

The share prices of those companies which do not hold anything of value and are out of cash are destined to fall further, even though they may be down 90 percent or more from the highs.

The investors who are buyers in the junior resource market at this time are pretty savvy and they are highly selective. They are buying shares in the higher quality companies. Until recently, they just kept bids under the market price, waiting for the market to come to them, which it did.

Perhaps sensing that the prices for those quality companies have bottomed, investors have begun to push the prices higher.

Many high quality companies will double or more before there is a consensus that the market is at the bottom. A bottom to the overall market may not come for some time yet, as

investors are still trying to unload shares of companies that they simply want to be rid of. Many of those companies are still trading well above their fundamental values.

There is certainly further downside risk in the overall resource markets. But, for the higher quality companies, there is a great deal more upside potential than downside risk at this time.

Resource Market Sentiment

The big gold mining companies have taken yet another round of multi-billion dollar write-downs in the latest quarter, leading some people to believe that they will not be buying any new gold deposits (and therefore junior companies) for a long time. It may well be true that the big Western mining companies will not be buying more metal deposits in the near future. But, that does not signal a lack to takeovers of junior companies.

In the past month, Alamos Gold (AGI-TSX) offered to buy two juniors, both for cash, at prices well above the recent market prices. The bid for Esperanza Resources (EPZ-TSXV), which we follow in Resource Opportunities, was 38% above the average trading price.

The mid-tier producers, for the most part, have strong balance sheets and are looking to expand. There are also hundreds of international mining companies, many based in emerging countries like China and Brazil, which have cash and are actively evaluating the many bargains available at this time.

The sudden collapse of metal prices this year caught many companies off guard, slashing or

eliminating profits. As a result, some companies are now facing serious financial distress, which is very unfortunate for shareholders of those companies. The flip side is that companies in a strong financial position are able to acquire assets at bargain prices.

There is a lot of money to be made at this time in the resource markets, for companies and for investors. Share prices and asset prices are at bargain levels, making this a good time to be buying shares or shopping for mining industry assets.

Fortunes were made in this industry by those who loaded up in late 2008 or in 2001, times when market sentiment was at rock bottom levels.

Monday, March 17, 2014
Sprott Global

[Rick Rule: Coming Natural Resource Market Will 'Elate or Terrify You'](#)

Rick Rule, Chairman of Sprott Global Resource Investments Ltd., has been involved in natural resource for four decades.

Rick says he expects some familiar patterns to emerge in the coming year.

See below for his most recent comments.



Photo credit: Cambridge House International

Sprott Global: Rick, you've predicted an impending bear-market bottom in precious metals and natural resources. Are we there now?

Rick Rule: I believe we are. We'll see a rising market with higher highs and higher lows. We'll also see high volatility -- which one day will elate you and another day will terrify you. That's the way this works.

As we've [discussed](#) before, bear markets lead to bull markets; and this bear market will end at some point. Let's take a look back to 2003. The first third of the year was truly terrifying. Buyers were exhausted and a lot of people were selling. The price charts of both commodities and equities looked like ski hills, falling rapidly from the upper left to the lower right of the page.

In the middle part of the year, we had a 'flat-line' experience. Sellers were exhausted but buyers were exhausted too. So the stock charts were horizontal.

At the end of the year, we began to see 'bifurcation.' The best of the issuers and some of the commodities caught bids. In the absence of sellers this caused dramatic price moves upwards on relatively small volume. Some of the juniors -- like Eurasian Minerals Inc., Almaden Minerals Inc., or B2Gold Corp. -- went up by double-digits with only minor buying.

That was a classic sign that the bear market bottom had been passed. Today, we have seen this 'flat-line' period in 2013. To signal a start of a new bull market, we should see rising volumes and higher prices.

In the past, a new bull market was preceded by 'issuer capitulation.' The better players among small exploration and mining companies -- 'juniors' -- understand that you cannot simply survive. You have to advance your project and grow. You need to deliver value to investors. And for that you must raise money.

In July of 2000, the very best of the exploration companies, which were run by such mining legends today as Ross Beatty, Bob Quartermain, or Lukas Lundin, said:

"We need to raise money. We need to advance our projects, whatever it takes."

When that decision was made in 2000, it kicked off a spectacular rally in some of the juniors -- mainly those that received financing.

Meanwhile, the 'worst' of the juniors continued downwards. But the best of the juniors produced high returns during this period. And that is ultimately what kicked off the bull market.

Rick, back in October you mentioned that investors should reorganize their portfolios at the bottom. What is it they need to do?

People -- including me -- don't want to admit defeat.

Somebody who bought a stock at \$4 that is selling at 40 cents today will often think: "I can't sell this stock at 40 cents. If I do, I'll lose \$3.60." The truth is you've already lost the \$3.60.

All that matters is what you do with the 40 cents. It doesn't matter that you paid \$4 for this stock. If you believe it's selling for 40 cents and it's worth 90 cents, that's OK. You have made a decision with the 40 cents you have left in the stock. But don't hold on because it's too painful to sell.

Getting rid of such a stock is difficult. But the price you paid for a stock is irrelevant to your decision today.

Today, what asset classes do you think will lead a natural resource recovery?

The safest commodities to buy are those that are selling below what it costs to produce them. In these cases, the commodity price must go up or the industry that produces them will go out of business.

For example, platinum and palladium are priced below production cost, so the industry will likely start to decrease production. But platinum and palladium are highly valuable, for one reason because they purify the air coming out of cars' exhaust pipes.

Uranium is another example. It cost us \$70 a pound to mine. It sells for \$35 a pound. Either the price goes up or nuclear power plants shut down – and the lights go out. It's that simple.

With commodities like platinum, palladium, and uranium, if the prices do not go up, we will stop enjoying the benefits they produce.

15 years ago, I made a similar call on copper. It cost the industry a buck and a quarter to make a pound of copper, but copper was selling for 80 cents a pound. Either the price of copper had to go up or we would run out of copper. Copper is essential to modern life – especially in providing electricity. Sure enough, the price of copper went up.

To me, these are 'comfortable' speculations. But the exploration stocks, where you take a lot more risks, is where you can also make much higher returns – if you are right.

In this 'ragged edge' of the speculation spectrum, there is one critical task: to identify the best of the companies – those with real assets, proven management expertise, and solid prospects. I believe even the worst of these will probably triple in price over three or four years. The best may generate tenfold or fifteen fold returns.

But you're going to have to take a lot of risk to get those big returns. In order to get these 10 or 15-fold returns, you're going to have to take several individual losses to your portfolio.

And you're going to contend with a lot of volatility that is beyond your control. I believe the decline in the gold price from \$1,900 to \$1,200, for instance, was not the end of a secular bull market. I think it was a cyclical decline within a secular bull market.

The great bull market of my youth, in the 1970s and 1980s, was truly an epic bull market. The gold price rose from \$35¹ an ounce to \$850 per ounce². Natural gas prices rose from 25 cents a thousand cubic feet to over \$2.5³.

In that 10 or 12-year bull market, there were probably 10 or 12 price declines in gold of 20 percent or more -- cyclical declines in a secular bull market.

In the middle of that bull market, at the end of 1975, and in 1976, the gold price had run from \$35 an ounce to \$200 an ounce, and fell by fully 50 percent -- from \$200 an ounce to \$100 an ounce. Many people lost their courage or their conviction and got shaken out of the gold trade -- missing the move in gold from \$100 an ounce to \$850 an ounce over the next five and half years.

In the current recovery, we will see higher highs and higher lows. We will see 20 percent perturbations in price that will either elate or terrify you depending on your individual positions.

Rick, will we then see higher volatility from here on out?

Well, I was surprised by the lack of volatility since the events of 2008. I had expected the market to experience much more volatility than it has.

What happened is that the market was sedated -- injected with substances in the form of quantitative easing and short-term credits. But artificial benefits of short-term credit will be less and less effective in the market just as increasing doses of heroin are less and less felt by the addict. One of the results of this addiction will be volatility.

You have said that investors must be willing to do the work to understand their investments. What if they entrust this task to someone else, like a financial advisor? What would you tell an investor to ask their financial adviser?

First of all, ask "Why you?"

There are hundreds of thousands of people who are willing to tell you what to do with your money and make a commission.

The answer had better include a specific focus on whatever sector you want to invest in.

If you are interested in financial services stocks, then your adviser had better know something about the financial services sector. The institution that he or she works for had better have a specific focus on these stocks as well.

In an investment world as diverse as it is today, no institution -- let alone any individual -- has sufficient expertise across the length and breadth of the market.

If your adviser doesn't have specific expertise with regards to the topic that you are asking him or her to address, fire them.

The second thing to ask your adviser is to describe their view of current market conditions. What circumstances do they believe are driving the market? What are the correct strategic moves for an investor? If the adviser can't give a good response, fire the adviser.

The third thing is you need to ask is: "What specific support do you get from your institution that makes you competitive?"

Take Sprott as an example. We are probably the world's largest investor in micro-cap natural resource equities. We have the ability to address these companies either as investors or as lenders. But our size and scale mean that we are able to focus more on evaluating resources by employing geologists, geophysicists and engineers than any of our competitors.

Our strategic advantage is simply that we are a \$7-billion institution in terms of assets under management and largely focus on natural resources.

But if somebody came to Sprott and asked us, "Should I buy a thousand shares of General Electric?" they shouldn't listen to our response because we have no experience or focus pertaining to General Electric.

On the other hand, if somebody asks us a question about small-cap or micro-cap oil and gas or mining shares, we are probably better prepared than any competitor in the world to answer those questions.

You mentioned that in the earlier years of the firm, you would spend around 20 percent of the company's revenues on research – for example analyzing the geology of deposits or the economics of a mine. Why is this research so important?

In the natural resource exploration business, it's not really about physical assets. I would call these companies the research and development businesses of the natural resource sector. They are trying to answer research questions that will create value to someone – like determining the nature of a geological anomaly, the size of an ore body, or whether a deposit is economic to mine.

The human resources of these small companies are their most important assets.

How do you evaluate the potential of a project and a research team?

First, you want to know what question they are trying to answer.

Is it the question that will add the most value, when answered? What thesis do they currently have, and is it supported by the facts that are available? Is their process to prove or disprove their theory valid? How will they know that they have answered the question pursued in their research?

In other words, if a company raises \$10 million for a drilling program, will they have the good sense after spending \$3 million dollars to understand that their thesis isn't valid? Will they save the \$7 million dollars left for some other useful purpose? Or will they spend the whole \$10 million dollars because they raised it?

The success that I have enjoyed in natural resources has really come from a fairly small number of extremely good decisions that yielded extraordinary returns.

Getting an answer to the research question requires 18 months. A project as a whole, where there are multiple questions that must be answered, can take half a decade.

This is why we devote so many resources to acquiring knowledge about projects and management teams. We need to determine what management teams actually know their stuff; what their plan is; how well they stick with their plan; and what the value of their research might be.

Ben Graham pointed out that in the short term the market is a voting machine. It's a source of noise. It represents people's intuition and feelings. In the long term, it's a weighing machine. It values what things are worth. You make money in the market by exploiting the gap between how people feel about things in the short term, and what they are really worth.

You need to establish a basis for evaluating these projects in order to decide whether the market's current price is cheap or expensive. For me, that involves spending lots of money on geologists and engineers to help figure that out.

Rick, when we look at the broad stock market today, represented by the Dow Jones and the S&P 500, are you seeing an impending bear market? How will that impact the nascent recovery in natural resources?

When I look at the balance sheets and income statements of the largest industrial and financial companies in United States, I am struck by what great companies they are.

They responded to the 2008 collapse by strengthening their balance sheets. They are holding excess cash. Their operating margins are very strong.

But is this strength sustainable? Are their margins at all-time highs because they have become better businesses? Or is this because interest rates are artificially low, so demand is higher and their cost of borrowing is lower?

The yields on certificates of deposits and long-term bonds are artificially low now. This drives more people into stocks, which may explain these companies' performance.

If interest rates rise, it will raise costs for companies that rely on debt to run their businesses. At the same time, it will lower their attractiveness to investors because bonds and savings will pay higher yields.

The impact that a rise in interest rates could have on these markets makes me nervous to think about. I expect it would either be very negative or catastrophic.

Rick, how do you view water as an investment opportunity?

You need to know a few things about the water market. You don't have a water market in places like British Columbia where the challenge is to make it go away.

You have a water market in places like the west and southwest United States. For water markets to emerge water must be scarce and the society must be rich enough to pay for water.

There's a shortage of water in Djibouti but it doesn't matter because you can't sell it to anybody. You want to focus on a place like California or Texas where water's value is highest because it is most scarce, and the population can afford to pay for it.

Throughout most of our history, water has been cheap because there was more supply than there were uses. But that reality is coming to an end.

Water's cheapness has caused it to be used inefficiently. As a result, here in California for example, 85 percent of the water that we use contributes to 3.5 percent of GDP -- in agriculture.

Only 15 percent of the water in the State of California contributes to the other 96.5 percent of GDP.

Why such an imbalance? Water has been allocated by voters rather than the market. 80 years ago, when farmers and the State held the political power, they created a water rights system that kept water cheap for farming. Today, the political fight necessary to reverse these decisions and to deregulate the price of water hasn't happened in California, because of the political cost of going against the rural constituents. Meanwhile, there has been ample water.

The last time we had a big drought in California was in 1977. It was an enormously disruptive event. People had to do things like ration how many times they flushed their toilets. A considerable inconvenience!

And in 1977, there were almost 12 million fewer people in the state. In other words, there were 12 million fewer straws in the barrel. We offset the shortage of water in the state by overdrawing our allotment of Colorado River water. But that was before lots of people lived in places like Las Vegas or Phoenix.

When we finally get a full-blown water shortage in California -- probably sometime in the next decade -- water will change in price dramatically. I believe it could go up ten-fold.

Rick, you have said this will be your last big cycle in natural resources. As a Director of Sprott Inc., how do you hope to shape the organization for the future?

Financial companies like Sprott are really just made up of people. Sure, you can look at our balance sheet, at our physical addresses, and at our wonderful art collection. But when the last person goes home, all we have left are desks and phones.

Our investment in the future involves recruiting and training new people. We need to grow our human resources because they're the only real resources we have.

Yes, we have a potent balance sheet. We have important mandates from individual investors, institutions and even nations. Our real hope is to nurture the next generation and the subsequent generation of investors who will take the mantle from investment leaders like Marc Faber, Eric Sprott, John Embry, or me.

Our outreach programs aim to convey the paradigm gained by 35 years of investment experience at Sprott to investors who can employ it profitably and enhance the reputation of this firm.

Sprott will aim to continue the critical contrarian thinking that has led to the success of investors in my generation, and took Sprott from being one man to a multi-billion-dollar organization. We

want to arm the second and third generation with the knowledge and the attitudes that are part of the Sprott franchise. And it's going to be a lot of fun.

One of the huge benefits I've gotten from my affiliation with Sprott was unintended. I have received great personal joy from mentoring younger talent. I didn't realize the psychological and intellectual benefit that I would get from that.

It is at least equal to the gratification that I've gotten from analyzing stocks. And the benefit that I have enjoyed from that has been tremendous in the last 35 years.

I am one of those guys who never really worked a day in his life. I get up and I am eager to go to work. I now have the opportunity to imbue other people with that advantage, while profiting monetarily in my declining years as a large shareholder of Sprott. It is almost fictionally good fortune for me.

Rick Rule, Chairman of Sprott US Holdings Inc. Thanks for your comments.

Thank you for the opportunity.

Rick Rule has devoted over 35 years to natural resource investing. His involvement in the sector is as broad as it is long; his background includes mineral exploration, oil & gas exploration and production, water, agriculture, and hydro-electric and geothermal energy. Mr. Rule is a sought-after speaker at industry conferences, and a frequent contributor to numerous media outlets including CNBC, Fox Business News, and BNN. He founded Global Resource Investments in 1993 and is now a Director of Sprott Inc., a Toronto-based investment manager with over \$7 billion in assets under management, and CEO and President of Sprott US Holdings Inc., where he leads a team of skilled earth science and finance professionals who enjoy a worldwide reputation for resource investing.

¹ www.kitco.com

² <http://www.cbsnews.com/news/is-golds-price-drop-just-the-beginning/>

³ <http://www.eia.gov/dnav/ng/hist/n9190us3m.htm>

The video recording of our talk with Rick will be published shortly.

You can also view Rick's recent take on the market with smallcappower.com [here](#).

Video interview of Rick Rule: <http://youtu.be/DDLUNmHX0w8>

Panel discussion of the resource sector: <http://youtu.be/Og6j9U7TDsU>

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Rick Rule: Which Companies Will Bring in the Green?

TICKERS: BCM, FSM; FVI; F4S, GUY, PPP, SSO; SSRI, THO; TAHO

Source: Karen Roche of *The Gold Report* (3/17/14)



Thoughts turn to green on St. Patrick's Day. Rick Rule of Sprott US Holdings believes the resources bull market is about 18 months from arriving and there could be multiple promising entry points in the market this summer. But in this interview with [*The Gold Report*](#), he says that this rebound may not look like the one investors are expecting and shares tips on how to spot companies that may have pots of gold at the end of the rainbow.

COMPANIES MENTIONED: BEAR CREEK MINING CORP. : [FORTUNA SILVER MINES INC.](#) : [GOLDCORP INC.](#) : [GUYANA GOLDFIELDS INC.](#) : [PRIMERO MINING CORP.](#) : SILVER STANDARD RESOURCES INC. : [TAHOE RESOURCES INC.](#)

RELATED COMPANIES

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- : [SANTACRUZ SILVER MINING LTD.](#)
- : [TIMMINS GOLD CORP.](#)

The Gold Report: In a call with Sprott clients last week, you said that the junior resource market is at an intermediate-term top right now and there will be good summer entry points. Why is the market at a top now instead of May, which is more typical? Should investors wait until the summer entry points to get into good juniors?

Rick Rule: The top could continue through mid-May. If investors have positions in their portfolios that they aren't thrilled with, they should use this market to sell. One of the things I've noticed is that if an investor paid \$1 for a stock and the stock is at \$0.35—even if the stock was valueless—they are unwilling to sell it for \$0.35. In many cases, the stocks that fell from \$1 to \$0.25 or \$0.35 are now selling at \$0.50 or \$0.60. My suggestion is that this is a great time to take advantage of it.

"Tahoe Resources Inc. has one of the finest silver deposits in the world."

I want to draw people's attention to the fact that the market is up 40% in some cases from its bottom. Amazingly, people are more attracted to that than a market that exhibited bargain basement prices.

Although I believe that the market has bottomed, we're going to be in an upward channel with higher highs and higher lows, but we are certainly going to exhibit the volatility that the market is famous for. It's my suspicion that the summer doldrums will see lows that, while higher than last summer, are substantially lower than the prices that we're enjoying today.

TGR: Gold has been above \$1,300/ounce (\$1,300/oz) for several weeks. Is that influencing the market?

RR: Gold certainly is a bellwether commodity for the junior resource sector. For 25 years, people have referred to junior mining in many circumstances as junior gold. That's misinformation because the junior resource sector encompasses a variety of commodities. My suspicion is that we have put in lows in the precious metals and they will trade higher, but not straight up. The gains will need to be consolidated. It will be volatile on the way up.

TGR: If it's a misconception that gold is the bellwether commodity, what key commodities do you look at to support the claim that we bottomed out in the summer of last year?

RR: Virtually the entire complex, with the exception of copper, which has stayed pretty weak. Zinc has begun to cooperate. While uranium hasn't cooperated, the sentiment for uranium juniors and the premium associated with Uranium Participation Corp. (U:TSX) has certainly done better. The energy complex has seen oil up \$10/barrel and natural gas doubled. Platinum and palladium are up substantially, although that may be a consequence of fears about an embargo against Russian palladium supplies and a response to labor unrest in South Africa. However, generally, the whole commodities complex, including the soft commodities, even in the face of bumper grain crops, is doing well since last summer.

TGR: What do you attribute that to?

RR: There are a couple of reasons. The whole sector was oversold. We've participated in a bit of a dead cat bounce. The long-term thesis has a lot to do with the increasing ability of the bottom of the demographic pyramid to increase its standard of living, which involves more commodities. I'd say that the great unsung hero of a rebound in the fortune of commodity producers has been the increasingly constrained supply of resources. The demand side on resources has been very slow because this recovery in the West has been a false, paper recovery. It hasn't been accompanied by capital spending or jobs. It's an interest rate-led recovery with flat auto sales and home starts.

What has kept commodity prices stronger than what some investors thought they would be has been the constrained supply growth in the face of constrained demand. In sectors that were regarded as horrifically oversupplied, like natural gas, two things have happened: Cheap natural gas prices have led to more utilization of gas for power generation at the same time that Mother Nature threw the polar vortex at us.

This sort of supply response isn't limited to natural gas. On the precious metals side, the industry has spent tens of billions of dollars during the past 15 years on exploration, construction and production. The production numbers for precious metals have been going sideways for gold and silver and going down for platinum and palladium. Supply constraints on a global basis led to the bottoming and then the recovery of commodity pricing.

TGR: If we don't have enough supply to meet demand, even if demand stays flat, we would see commodity prices going up. But aren't we still seeing some growth in developing countries as the poor become richer and invest in commodity-intensive products?

RR: That will be evident in future years. This year is simply a recovery from the oversold conditions of 2013. That's normally the way bear markets become bull markets; they normally are a reaction to oversold situations.

TGR: Are the capital markets coming back to the commodity groups now to finance them? Will that financing ultimately result in increased supply?

RR: There is an increasing amount of equity available for the better companies in the junior resource space. This is precisely the set of circumstances that we talked about in our [interview](#) last summer, which we referred to as bifurcation. The best 20% of the issuers have begun to find bids, not just in the junior capital markets, which is where the share prices are up, but also in financing markets. An increasing number of bought financings are getting done. For the bulk of the juniors, of course, that capital isn't available—and good riddance. They'll go away.

Probably a bigger question is going to be where the project and development financing will come from. The large private sector banks that used to fund construction and permanent finance for major resource projects have been less willing to take those loans onto their balance sheets, choosing instead to become financial arrangers. A situation where everybody's a financial arranger and nobody's a funder means that projects haven't been getting funded.

We believe that the likely lenders going forward will be sovereign wealth funds and superannuation or pension funds with a long-term horizon. But that hasn't worked itself out yet. While there is a refreshing ability for the better juniors to get stop-gap equity financing, what is still missing from this market is the senior project financing. That's something that Sprott is working very hard to address.

TGR: What will be the catalyst that will move sovereign wealth funds, pension funds or Sprott into doing those large capital financings?

RR: The time horizons of 10–20 years that are required in project finance correspond well to the needs of pension, superannuation and sovereign wealth funds. Because they are already equity investors, the balance sheet risk with being a senior secured lender will fit well with their needs. It's just something that they haven't done before. This is a natural progression that hasn't occurred yet, and we hope to facilitate it.

TGR: Why is there a natural progression of moving these large project capital financings to a pension or sovereign wealth fund?

RR: Legislation in place now on a global basis for large banks forces them to be providers of capital to sovereign governments. If JPMorgan Chase has a loan to Greece on its books that is selling at 70% of par, European Union rules allow JPMorgan to carry that bond at 100% of par if it says it intends to hold it to maturity. In other words, the rules allow the bank to mark the loan to myth as opposed to the market. If the same sort of loan was made by JPMorgan to a private party, even a solvent private party, unlike an insolvent sovereign, the carrying value on that loan would have to be reduced, which would reduce the capital base of the bank.

As a response, the banks have become conduits that accept deposits on a global basis and borrow very short-term money from sovereign lenders and then relend the money to sovereign borrowers on a longer-term basis. They profit from the same type of arbitrage—borrowing short and lending long—which was the demise of the U.S. savings and

loan business. This may or may not be a great business strategy. It's one they've been, in effect, forced into as a consequence of banking regulations that came about after the 2008 liquidity crisis.

TGR: How might that play out over the next decade?

RR: That's a many headed question. If we have a situation where short-term interest rates go up—where central banks are less able to manipulate short-term interest rates—it will have an extremely unpleasant outcome for the large banks.

TGR: You mentioned earlier that Sprott was looking at playing a role in that natural progression from the large banks to other types of fundees. What specifically is the role for Sprott there?

RR: Sprott has had discussions with many of the largest sovereign and pension investors in the world, including the National Pension Service of Korea, for which we manage some money. We have begun the process of educating these very large investors about the nature of project finance and how project finance might solve some of their investment needs. It's an area that these very large investors hadn't had much experience or interest in.

TGR: We've been talking about major debt project funding. Might these also come up in private placement opportunities, or do private placements fund other types of resource opportunities?

RR: Private placements have traditionally been on the exploration, development or preconstruction side of junior natural resource companies. This range of companies enjoyed unprecedented access to capital in 2003–2011. The consequence of that access to capital was a spectacular bull market that gave way to a spectacular bear market where the excesses of that period had to be exorcised. The issuers confused the optimal conditions with normalized conditions. The consequence has been that companies believe that the pricing circumstance that they enjoyed in 2003–2011 was normal as opposed to optimal. Issuers will be forced to be rational in 2014 simply as a consequence of their need for capital.

TGR: Are the latest financings discriminating or financing broadly across the sector?

RR: It's been very discriminating, and it has to be. The junior resource business taken as a whole is valueless. Almost three-quarters of the issues on the exchange have no net-present value (NPV). The arithmetic consequence of that is any financing these poor quality companies do takes place at sub-\$0 cost of capital. The better companies have found a bid. The better companies have been able to attract the financing. We need to take the bottom half of this industry and we need to flush it so that more money is focused on better projects and better companies.

TGR: Are you feeling a bit cautious about the potential continuing upmarket?

RR: I feel great about it. My experience has been that bear markets are always the authors of bull markets. While history doesn't repeat, it certainly rhymes. The severity of the decline that we have experienced was at once the

consequence of the extraordinary bull market that preceded it, but it's also indicative of the type of response that we're going to enjoy.

Make no mistake, the magnitude of this decline was as spectacular as anything I've seen since the mid-1980s. I feel the bull market that we are going to come into sometime in the next 18 months to 2 years will probably be as good a bull market as any I've ever experienced, and I've experienced some spectacular ones.

TGR: I was looking at the performance of the Sprott funds. The energy fund returned 23.4% in Q3/13 and Q4/13 while the gold and precious metals fund had a return of -4.2%. If the resource market bottomed in the summer of last year, how do you explain the difference between these two funds?

RR: The uptick in oil and gas equities happened faster because free cash flows recovered more quickly and because these energy issuers are generally better companies. It was easy to measure the impact of higher natural gas prices on the oil and gas juniors because they were producing. When the natural gas price went off its \$1.90 million British thermal units (\$1.9 MMBtu) low up to \$4 MMBtu, the impact on producers' income statements on a quarterly basis was immediate and dramatic.

An increase in the gold price from \$1,100/oz to \$1,300/oz for a company that is not yet producing gold is one that has to be factored in an NPV calculation to future cash flows. It took longer to work its way through the system.

TGR: There have been some really dramatic turnarounds so far this year in the gold and precious metals fund: [Tahoe Resources Inc. \(THO:TSX; TAHO:NYSE\)](#) was down 9% in Q4/12 and is up 48% year to date (YTD); [Guyana Goldfields Inc. \(GUY:TSX\)](#) was down 36% in Q4/13 and is up 67% YTD; and [Silver Standard Resources Inc. \(SSO:TSX; SSRI:NASDAQ\)](#) was up 25% last year, and is up 44% this year. What do you attribute this dramatic turnaround to over the last few months?

RR: It's a turnabout in market sentiment. The middle part of last year, the stock charts went sideways on no volume—exhausted sellers, exhausted buyers. At the end of last year, those stocks began to catch some bids. The people who had to sell, sold. We began to notice small inflows of cash at Sprott into our resource-oriented mutual funds at the end of last summer. We were no longer forced sellers, and we became nominal buyers.

I think our experience mirrored the experience of the rest of the institutional investing community. The consequence was fairly dramatic moves up on small volumes in some ludicrously oversold equities. We've come into a period where there's a better balance between buyers and sellers.

TGR: Are you expecting to see modulation in increases in the fund because it had a dramatic turnaround?

RR: That's the theme of this call. My suspicion is that we've been through the worst of the bear market, that the bear market bottom will not be a "V," it will be saucer shaped, and it will take 12–18 months from now before we're truly in a bull market. The gains that we've just enjoyed will need to consolidate. They may go a little higher before they go

lower, but the truth is that a recovery will see higher highs and higher lows, and will also feature the volatility that this sector is so famous for. The recovery is in its very early stages.

TGR: Can you comment on some of these companies in the fund that have had large YTD performances?

RR: I think we have a combination of circumstance here. Tahoe is, if not the finest, then one of the finest silver deposits in the world. It answered the question of "could it overcome its social license issues and mine construction issues by getting into production." It delivered value. The naysayers were proven wrong. The small increase in the silver price certainly helped it, too.

Similarly, [Primero Mining Corp. \(PPP:NYSE; P:TSX\)](#) outperformed production expectations and then announced an acquisition of a development project that allowed the market some visibility as to how it might grow going forward.

Guyana Goldfields simply was a recovery from a ridiculously oversold level.

Silver Standard delivered improved performance in Argentina. It added some meat to the bones. The market liked the fact that it, in the last six months of last year, seemed to get its hands on the production difficulties that it was having at the Pirquitas mine.

More recently, the company enjoyed a tremendous share price spurt as a consequence of its acquisition of the Marigold mine in Nevada from [Goldcorp Inc. \(G:TSX; GG:NYSE\)](#) that shows the way for it to increase cash flow and profits on an accretive, per-share basis. It might allow Silver Standard to develop the rest of its portfolio internally without external funding.

[Bear Creek Mining Corp. \(BCM:TSX.V\)](#) got social license in Peru. There had been questions as to whether either of the company's development projects would be able to be developed given local opposition in Peru. Bear Creek got the backing of every prominent local group and a landmark agreement between the central government of Peru and the local government that would allow for more equitable distribution to the region of tax, royalties and the social rents from mining. Historically, in Peru, the regions have borne all the costs of mining while the center has collected all the social rent.

[Fortuna Silver Mines Inc. \(FSM:NYSE; FVI:TSX; FVI:BVL; F4S:FSE\)](#) continues to impress with its ability to operate midsize silver mines. Its two operations have consistently met its promises. That set it apart from an industry where probably 75% of the project news has been disappointing. Fortuna, as a consequence of meeting projections quarter after quarter, has begun to develop a loyal shareholder base among silver speculators.

TGR: With St. Patrick's Day on the horizon, what company is really going to have the luck of the Irish and bring in the green?

RR: For your readers in the West and the Southwest, water will be a real important topic of discussion. We've had a situation in the West and the Southwest where water has been priced politically, which means it's been delivered as a

right irrespective of its supply and the cost of distributing it. The consequence of that has been gross misdistribution, which has worked as long as nature has cooperated. But nature this year has ceased to cooperate. We're going to see tremendous distortions in water pricing across the West and the Southwest, and that will have spinoffs in areas like food cost. The very low cost of food that Americans have enjoyed in the last 40 years has had to do with the subsidies afforded to farmers for water supply.

Here in California, there are now several water districts whose allocation of water from the state and federal government is zero. Growing, as an example, almonds or pistachios or plums—pick a crop, really—in the summer in California with zero water allocation is very difficult. This is going to be a subject that is going to play very large among investors. It's something that Sprott has been involved in through my own efforts for two decades. It's something that we're trying to get a lot more involved with in the next two or three years.

California had a pretty good drought in 1977 that caused us to do things like flush our toilets on alternative days and not wash our cars. It had much more profound economic consequences than that. The interesting thing for Californians to note is that since 1977, two important things have changed: There are 12 million more of us with our straws in the sponge, but the sponge hasn't increased at all. At the same time, the safety valve Californians had from the Colorado River is gone. The consequences will be very dramatic.

Since 1977, people have moved to places like Phoenix, Tucson, Salt Lake City and Las Vegas. We don't have the ability to overdraw our allotment anymore. The way that we got out of the predicament in 1977 is not a way out this time. It's going to have profound consequences. I don't know what they are, but it's going to have profound consequences.

TGR: How do you play the water sector and this drought? You can't get more rain. Are we looking at desalination? Are we looking at better water conservation?

RR: There is no play in the near term. The answer in the intermediate term is going to have to be more market pricing for water—and people are going to hate that. The way I'm playing it is to buy shares of companies that own water rights associated with their agricultural operations. My bet is that the California legislature does something that's logical. I realize that's a bet that plays against history. But my hope is that farmers are allowed to cease doing stupid things such as growing rice in the desert and are allowed to sell the water that they would have wasted growing rice in the desert to people who want to use it to flush toilets and brush teeth. If that takes place, there's as much as a 90% arbitrage in the converting of agricultural water to urban and municipal use.

If we did that, by the way, we wouldn't have a water crisis in California. We'd have a lot less agricultural production. But the truth is, if we had a market-clearing price for water in California, we wouldn't be having this discussion at all.

TGR: But if we had a market-clearing price for water in California, what would happen to the agricultural component of the California economy? What would that mean overall for the state?

RR: Remember that California agriculture contributes less than 4% of state GDP and consumes 85% of the state's water. I suspect that gross farm receipts would stay the same. We would have 25% or 30% of the farmland in California fallow, and we would have higher crop prices across lower production. That's the inevitable consequence that we have to face. The idea that we take water and we irrigate a desert to cut eight crops of alfalfa and we export that alfalfa in bales to China for its dairy industry is the equivalent of us exporting water below our cost of production to subsidize the Chinese dairy industry. If you say to suburban homeowners, the Cadillac communists in West L.A. or Mill Valley, that they have to sacrifice \$150,000 worth of landscaping at their houses, or be willing to pay 300% or 400% more for water so that they can subsidize the production of dairy in China, the political equation regarding water pricing in California could change. And that would confer enormous benefits on the people who understood the arbitrage of marking privately held agricultural water rights to market.

TGR: What's to keep the California government from taking away those agricultural water rights or redefining them so that that arbitrage is minimized or eliminated?

RR: Zero. The People's Republic of California will ultimately confiscate the product of intelligent savers but, mercifully, California is extremely inefficient, and it won't get around to fashioning the political compromise necessary to steal that wealth for three or four years.

TGR: Can you share with us some of these companies that have water rights that can turn agricultural water into urban-use water to take advantage of this arbitrage situation?

RR: Sure, with a caveat that these are companies I own as opposed to companies that I recommend to your readership. I own J.G. Boswell Co. (BWEL:OTCPK), which is the largest of the California corporate farmers; Limoneira Co. (LMNR:NASDAQ), which is a grower and developer in Ventura, Calif.; and PICO Holdings Inc. (PICO:NASDAQ), which is the Physicians Insurance Company of Ohio, a water-rights owner in Nevada and Arizona.

TGR: That's ironic. The Physicians Insurance Company of Ohio owns water rights in Arizona and Nevada?

RR: That's a story for a different interview.

TGR: I appreciate your time, Rick.

RR: My pleasure. Thank you.

[Rick Rule](#), CEO of Sprott US Holdings Inc., began his career in the securities business in 1974. He is a leading American retail broker specializing in mining, energy, water utilities, forest products and agriculture. His company has built a national reputation on taking advantage of global opportunities in the oil and gas, mining, alternative energy, agriculture, forestry and water industries. You can hear more from Rule and other Sprott experts by signing up for [Sprott's Thoughts](#).

Do You Know How to Spot a Superstar?

The World of Energy

Marin Katusa, Chief Energy
Investment Strategist



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If you had met Warren Buffett, Bill Gates, or Steve Jobs just before they became famous and incredibly wealthy and they pitched you on investing in their company, do you think you would have had the knowledge and faith to feel comfortable putting your money in their venture?

It's a difficult question to answer because we all would like to think so. But in reality, deep down in our gut, we know we wouldn't have put our money at stake with an unknown, unless, of course, we'd had enough time to study their company and to get to know them well enough beforehand—and to do so, you would have needed some sort of advantage over the rest of the market.

Now, if you had been a member of the Homebrew Computer Club Newsletter in 1976 and you read Bill Gates' open letter to all computer hobbyists, you would have had some insights on how Gates was different from all the other contributors to the newsletter, and how he understood not just the technical aspects of the software business, but had the foresight to understand the financial implications as well.

But most likely you weren't a subscriber to the Homebrew Computer Club Newsletter, and you didn't hear about Microsoft or Bill Gates until

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he was already raking in millions and the smart money had made their fortunes.

No Nerds Need Apply

Over a decade ago, I went to my first resource investment conference. I was young, I knew nobody in the business, and none of my friends wanted to come along with me, so I went alone... and was completely overwhelmed. I felt out of place and awkward, and had no idea where to start—a feeling, I’m sure, that most people looking to invest in the junior resource sector can relate to.

I realized very quickly that all the books I’d read on investing, including my obsession with Warren Buffett, hadn’t prepared me at all for what I experienced at that first investment conference. I numbly walked around, not knowing what to look for, and when some company representative on the trade show floor tried to get my attention as I walked by their booth, I felt too awkward and shy to ask any questions.

It all changed for me when I saw a herd-like rush to the speakers’ hall. Not really knowing what was going on, I followed the crowd, as nothing creates a crowd like a crowd, right?

Who was speaking?

Doug Casey.

At that time, I had no idea that Doug Casey would later become my mentor, close personal friend, and business partner.

The Grandmaster of Resource Stock Evaluation

That day, Doug virtually burst with his legendary, no-holds-barred wit. He went up on stage and ripped into “Baby Bush” and the US government. The crowd was soaking it up, laughing and nodding at his every word. Up to that point, I’d never heard anyone speak like that, and I didn’t know what to think of Doug. All I knew was that he was

different and that he knew what he was talking about. This man was brilliant.

Then he got into how most of the companies in the junior resource sector are like burning matches and not worth the paper their certificates are printed on. That one statement resonated with me. It confirmed my gut feeling about the hours I spent walking around the show floor looking at all the companies, with nothing to show for it.

What Doug said next changed my life forever. I remember it as if it happened five minutes ago.

"It's People you need to do your research on. I invest in PEOPLE, not the rocks. Great People will find you great rocks and make you a lot of money."

At university, I took undergraduate geology and other earth science courses for two reasons: first, because I was interested in them; second, and more importantly, to keep my academic scholarship, I needed to have certain electives outside of my discipline—and let's face it, "rocks for jocks" was an easy way to juice up my GPA. Geologists will never admit this to you, but they're on the low end of the hierarchical order in the academic-science departments at universities. The counselors encourage the smart guys to pursue math, physics, or engineering degrees, not geology degrees.

Never in any of my geology courses did the professors talk about the mining business or the junior resource sector, or even that the hub of the junior resource sector was in fact the very city I received my first undergraduate degree in. What did they tell us then, you may ask...

I do remember one professor who told the whole class that whatever we decided to do with our careers, we should make sure not to get an undergraduate degree in geology, because there were no jobs. Little did I know at the time, as is typical for academics, that he was as wrong as

could be.

Back to Doug.

When Doug got into his talk about people, I had a moment of clarity. I knew right there and then that I was going to switch careers and somehow make my claim in the junior resource sector.

For the next five years, I spent almost all of my spare time learning about the junior resource sector. At that time, websites and email were just being adopted by resource corporations, and I was able to communicate with industry professionals who were more than happy to answer my questions or direct me to the people who would be able to answer them. I was motivated, aggressive, and passionate about my research.

With every day of research, I became more and more comfortable and confident. I created databases not just on the projects, but more importantly, on the people running the companies. I went through public documents and followed their own investments and price/cost basis. Every investment I made started with analyzing not just the people and their history and track record, but also their hard-dollar commitment to the venture, their experience, specialization, and their own network.

Slowly, I learned about the other aspects of the business that no CFA or MBA textbook discusses, such as private placements, the involvement of key power brokers, and which companies have the financial backing of the largest investment bankers, brokers, and fund managers.

The People factor is a much more complex dynamic than the geology. (I'm sure most geologists wouldn't agree with that statement, but those same geologists probably have never made a big score either.) Follow the smart money. The right people will be able to assess which are the right type of rocks, and also which rocks to avoid, as well as political, permitting, social, and financing risks.

A few years after my grand epiphany, in 2004 Doug Casey and I crossed paths again when we were both invited to a meeting with a uranium company we were invested in. As prepared as I thought I was, I learned very quickly during that meeting that I couldn't hold a candle to Doug. I was in awe of how he rifled off question after question, not just focusing on the geology but about the players associated and their relationships. That in turn created spinoff questions, and I received a lot of the invaluable information that Doug had built upon over 20 years in the business at that point.

At that meeting, it dawned upon me that Doug really did have a superior understanding of the People factor in the junior resource sector. He really knew the good, the bad, and the ugly, and most importantly, whom to write a check to.

This brings me to the original question of this missive...

Would You Be Able to Spot a Superstar Before His Big Score?

That's precisely why I created the **2014 Casey NexTen** list. I canvassed not just my own network, but all of Doug's network and all of the established, big industry insiders to find the next batch of resource superstars. Through our network and decades of experience in the junior resource sector, we were able to put together an amazing list of the next generation of resource titans in the making.

If you are reading this now, **this is your Homebrew Computer Club Newsletter moment**. You have not just Doug Casey and my network, but the top recommendations of the most successful resource investors who have helped make this list.

Case in Point: Amir Adnani

Take for example, Amir Adnani and his company Uranium Energy Corp (UEC), which we recommended as a Buy in the November 2008 issue of the *Casey Energy Report*. Obama had just won the election, and I

clearly remember the weakness in the junior resource sector due to the global financial crisis at that time. Within a year of that recommendation, Amir Adnani returned +1,000% gains to *Casey Energy Report* subscribers and became the first member in the Casey Ten-Bagger Club.

At the time, I'd known Amir personally for a long time. He always impressed Doug and me as very professional, smart, and incredibly hard working. He did his homework, and in the years since, he has built UEC into a low-cost producer and has positioned his company and shareholders by producing up to 2 million pounds of uranium annually, with a rising uranium price.

UEC was a huge win for subscribers who bought during that first recommendation in the *Casey Energy Report*, and with Japan announcing it will restart two of its 48 nuclear reactors this year, we see all the stars aligning for the uranium sector as a whole.

We weren't the only ones to take notice, as Asia's wealthiest man, Li Ka-shing, and Rick Rule have also backed UEC and Amir Adnani. Warren Gilman, chairman and CEO of Li Ka-shing's resource fund CEF, stated in the most recent UEC press release, ***"Our investment in UEC is based on the uniqueness and quality of [its] assets as well as the strength of its management team. We are pleased to continue our support of the company as UEC continues to position itself as a leading, domestic uranium producer in the U.S."***

Doug Casey's 9 Secrets for Successful Speculation

Metals & Mining Monday

archives

Louis James, Chief Metals & Mining Investment Strategist

Dear Reader,

The issue uppermost on my mind as I write today is the trouble I see ahead for my dear friends in Ukraine. My fears for my former students in the country are a personal matter, however, so I

won't dwell on that. What's common to us all is that the situation could impact us as investors, even though few of us have any direct exposure to companies or assets in the region.

The tension itself is a bullish factor for gold, but there's much, much more at stake, even if the conflict does not turn into an actual war between East and West. I'm sorry to say that I do expect war in Crimea, but I do not expect the West to get directly involved. The fallout of open war with Russia is just unthinkable for Europe, and almost as costly and destructive for the US.

But it would be foolish for anyone to imagine that Russia will not respond to the sanctions US lawmakers are proposing in response to the Crimean vote yesterday. Those responses could hit the EU hard, given Europe's dependence on Russian gas, and that affects China, the US, and all of us as participants in the global economy.

The bigger threat, however, could be the economic consequences of a successful Russian effort to dethrone the US dollar as the world's reserve currency. Confidence in the USD is the linchpin of the confidence game the Fed has been running for years. If US dollars lose their privileged global reserve-currency status, it could precipitate wholesale dollar dumping by foreigners who are said to hold many times more dollars than are in circulation in the US.

And that could be the proverbial "it"—the spark that ignites a collapse in the purchasing power of the USD, leading to Doug Casey's long-predicted Greater Depression.

I'm not predicting what will be, but I do see the world edging closer to the abyss than it has been since those panicky days after the collapse of Lehman Brothers. As I've said before; in today's shaky global economy, we are all speculators now—and those who know it have an advantage over those who do not.

Perhaps, then, this is a good time to review some of the lessons I've learned from Doug, because if there's anyone best prepared to ride out the storm and to speculate on it successfully, it's Doug Casey.

Whatever happens next, I hope you find my story and the summary of what I've learned from Doug to be of value.

Sincerely,



Louis James
Senior Metals Investment Strategist
Casey Research

Rock & Stock Stats	Last	One Month Ago	One Year Ago
Gold	1,381.95	1,318.60	1,590.70

Silver	21.44	21.42	28.81
Copper	2.94	3.26	3.54
Oil	98.89	100.13	93.38
Gold Producers (GDX)	27.73	26.35	37.25
Gold Junior Stocks (GDXJ)	44.62	44.04	66.32
Silver Stocks (SIL)	14.53	14.53	18.08
TSX (Toronto Stock Exchange)	14,227.66	14,054.76	12,799.91
TSX Venture	1,033.64	996.35	1,112.61

Doug Casey's 9 Secrets for Successful Speculation

[Louis James](#), Chief Metals & Mining Investment Strategist

When I started working for Doug Casey almost 10 years ago, I probably knew as much about investing as the average Joe, but I now know that I knew absolutely nothing then about successful speculation.

Learning from *the* international speculator himself—and from his business partner, David Galland, to give credit where due—was like taking the proverbial drink from a fire hose. Fortunately, I was quite thirsty.

You see, just before Doug and David hired me in 2004, I'd had something of an epiphany. As a writer, most of what I was doing at the time was grant-proposal writing, asking wealthy philanthropists to support causes I believed in. After some years of meeting wealthy people and asking them for money, it suddenly dawned on me that they were nothing like the mean, greedy stereotypes the average American envisions.

It's quite embarrassing, but I have to admit that I was surprised how much I *liked* these "rich" people—not for what they could do for me, but for what they had done with their own lives. Most of them started with nothing and created financial empires. Even the ones who were born into wealthy families took what fortune gave them and turned it into much more. And though I'm sure the sample was biased, since I was meeting libertarian millionaires, these people accumulated wealth by creating real value that benefited those they did business with. My key observation was they were all very serious about money—not obsessed with it, but conscious of using it wisely and putting it to most efficient use. I greatly admired this; it's what I strive for myself now.

But I'm getting ahead of myself. The reason for my embarrassment is that my surprise told me something about myself; I discovered that I'd had a bad attitude about money.

This may seem like a philosophical digression, but it's an absolutely critical point. Without realizing that I'd adopted a cultural norm without conscious choice, I was like many others who believe that it is unseemly to care too much about money. I was working on saving the world, which was reward enough for me, and wanted only enough money to provide for my family.

And at the same instant my surprise at liking my rich donors made me realize that—despite my decades of pro-market activism—I had been prejudiced against successful capitalists, I realized that people who thought the way I did never had very much money.

It seems painfully obvious in hindsight. If thinking about money and exerting yourself to earn more of it makes you pinch your nose in disgust, how can you possibly be effective at doing so?

Well, you can't. I'm convinced that while almost nobody intends to be poor, this is why so many people are. They may want the benefits of being rich, but they actually don't want to be rich and have a great mental aversion to thinking about money and acting in ways that will bring more of it into their lives.

So, in May of 2004, I decided to get serious about money. I liked my rich friends and admired them all greatly, but I didn't see any of them as superhuman. There was no reason I could not have done what any of them had done, if I'd had the same willingness to do the work they did to achieve success.

Lo and behold, it was two months later that Doug and David offered me a job at Casey Research. That's not magic, nor coincidence; if it hadn't been Casey, I would have found someone else to learn from. The important thing is that had the offer come two months sooner, being a champion of noble causes and not a money-grubbing financier, I would have turned it down.

I'm still a champion of noble causes, but how things have changed since I enrolled in "Casey U" and got serious about learning how to put my money to work for me, instead of me having to always work for money!

Instead of asking people for donations, I'm now the one writing checks (which I believe will get much larger in the not-too-distant future). I can tell you this is much more fun.

How did I do it? I followed Doug's advice, speculated alongside him—and took profits with him. Without getting into the details, I can say I had some winning investments early on. I went long during the crash of 2008 and used the proceeds to buy property in 2010. I took profits on the property last year and bought the same stocks I was recommending in the ***International Speculator*** last fall, close to what now appears to have been another bottom.

In the interim, I've gone from renting to being a homeowner. I've gone from being an investment virgin to being one of those expert investors you occasionally see on TV. I've gone from a significant negative net worth to a significant nest egg... which I am happily working on increasing.

And I want to help all our readers do the same. Not because all we here at Casey Research care about is money, but because accumulating wealth creates value, [as Doug teaches us](#).

It's impossible, of course, to communicate all I've learned over my years with Doug in a simple article like this. I'm sure I'll write a book on it someday—perhaps after the current gold cycle passes its coming manic peak.

Still, I can boil what I've learned from Doug down to a few "secrets" that can help you as they have me. I urge you to think of these as a study guide, if you will, not a complete set of instructions.

As you read the list below, think about how you can learn more about each secret and adapt it to your own most effective use.

Secret #1: Contrarianism takes courage.

Everyone knows the essential investment formula: "Buy low, sell high," but it is so much easier said than done, it might as well be a secret formula.

The way to really make it work is to invest in an asset or commodity that people want and need but that for reasons of market cyclicalities or other temporary factors, no one else is buying. When the vast majority thinks something necessary is a bad investment, you want to be a buyer—that's what it means to be a contrarian.

Obviously, if this were easy, everyone would do it, and there would be no such thing as a contrarian opportunity. But it is very hard for most people to think independently enough to risk hard-won cash in ways others think is mistaken or too dangerous. Hence, fortune favors the bold.

Secret #2: Success takes discipline.

It's not just a matter of courage, of course; you can bravely follow a path right off a cliff if you're not careful. So you have to have a game plan for risk mitigation. You have to expect market volatility and turn it to your advantage. And you'll need an exit strategy.

The ways a successful speculator needs discipline are endless, but the most critical of all is to employ smart buying and selling tactics, so you don't get goaded into paying too much or spooked into selling for too little.

Secret #3: Analysis over emotion.

This may seem like an obvious corollary to the above, but it's a point well worth stressing on its own. To be a successful speculator does not require being an emotionless robot, but it does require abiding by reason at times when either fear or euphoria tempt us to veer from our game plans.

When a substantial investment in a speculative pick tanks—for no company-specific reason—the sense of gut-wrenching fear is very real. Panic often causes investors to sell at the very time they should be backing up the truck for more.

Similarly, when a stock is on a tear and friends are congratulating you on what a genius you are, the temptation to remain fully exposed—or even take on more risk in a play that is no longer undervalued—can be irresistible. But to ignore the numbers because of how you feel is extremely risky and leads to realizing unnecessary losses and letting terrific gains slip through your fingers.

Secret #4: Trust your gut.

Trusting a gut feeling sounds contradictory to the above, but it's really not. The point is not to put feelings over logic, but to listen to what your feelings tell you—particularly about company people you meet and their words in press releases.

“People” is the first of Doug Casey's famous [Eight Ps of Resource Stock Evaluation](#), and if a CEO comes across like a used-car salesman, that is telling you something. If a press release omits critical numbers or seems to be gilding the lily, that, too, tells you something.

The more experience you accumulate in whatever sector you focus on, the more acute your intuitive “radar” becomes: listen to it. There's nothing more frustrating than to take a chance on a story that looked good on paper but that your gut was warning you about, and then the investment disappoints. Kicking yourself is bad for your knees.

Secret #5: Assume Bulshytt.

As a speculator, investor, or really anyone who buys anything, you have to assume that everyone in business has an angle. Their interests may coincide with your own, but you can't assume that.

It's vital to keep in mind whom you are speaking with and what their interest might be. This applies to even the most honest people in mining, which is such a difficult business, no mine would ever get built if company CEOs put out a press release every time they ran into a problem.

A mine, from exploration to production to reclamation, is a nonstop flow of problems that need solving. But your brokers want to make commissions, your conference organizers want excitement, your bullion dealers want volume, etc. And, yes, your newsletter writers want to eat as well; ask yourself who pays them and whether their interests are aligned with yours or the companies they cover.

(Bulshytt is not a typo, but a reference to Neal Stephenson's brilliant novel, [Anathem](#), which defines the term, briefly, as [words, phrases, or even entire books or speeches that are misleading or empty of meaning](#).)

Secret #6: The trend is your friend.

No one can predict the future, but anyone who applies him- or herself diligently enough can identify trends in the world that will have predictable consequences and outcomes.

If you identify a trend that is real—or that at least has an overwhelming amount of evidence in its favor—it can serve as both compass and chart, keeping you on course regardless of market chaos, irrational investors, and the ever-present flood of bulshytt.

Knowing that you are betting on a trend that makes great sense and is backed by hard data also helps maintain your courage. Remember; prices may fluctuate, but price and value are not the same thing. If you are right about the trend, it will be your friend. Also, remember that it's easier to be right about the direction of a trend than its timing.

Secret #7: Only speculate with money you can afford to lose.

This is a logical corollary to the above. If you bet the farm or gamble away your children's college tuition on risky speculations—and only relatively risky investments have the potential to

generate the extraordinary returns that justify speculating in the first place—it will be almost impossible to maintain your cool and discipline when you need it.

As Doug likes to say; it's better to risk 10% of your capital shooting for 100% gains than to risk 100% of your capital shooting for 10% gains.

Secret #8: Stack the odds in your favor.

Given the risks inherent in speculating for extraordinary gains, you have to stack the odds in your favor. If you can't, don't play.

There are several ways to do this, including betting on People with proven track records, buying when market corrections put companies on sale way below any objective valuation, and participating in private placements. The most critical may be to either conduct the due diligence most investors are too busy to be bothered with, or find someone you can trust to do it for you.

Secret #9: You can't kiss all the girls.

This is one of Doug's favorite sayings, and though seemingly obvious, it's one of the main pitfalls for unwary speculators.

When you encounter a fantastic story or a stock going vertical and it feels like it's getting away from you, it can be very, very difficult to do all the things I mention above. I can tell you from firsthand experience, it's agonizing to identify a good bet, arrive too late, and see the ship sail off to great fortune—without you.

But if you let that push you into paying too much for your speculative picks, you can wipe out your own gains, even if you're betting on the right trends.

You can't kiss all the girls, and it only leads to trouble if you try. Fortunately, the universe of possible speculations is so vast, it simply doesn't matter if someone else beats you to any particular one; there will always be another to ask for the next dance. Bide your time, and make your move only when all of the above is on your side.

Final Point

These are the principles I live and breathe every day as a speculator. The devil, of course, is in the details, which is why I'm happy to be the editor of the [Casey International Speculator](#), where I can cover the ins and outs of all of the above in depth.

Right now, we're looking at an opportunity the likes of which we haven't seen in years: thanks to the downturn in gold—which now appears to have subsided—junior gold stocks are still drastically undervalued.

My team and I recently identified a set of junior mining companies that we believe have what it takes to potentially become 10-baggers, generating 1,000%+ gains. If you don't yet subscribe, I encourage you to try the *International Speculator* risk-free today and get our detailed **10-Bagger List for 2014** that tells you exactly why we think these companies will be winners. [Click here to learn more about the 10-Bagger List for 2014.](#)

Whatever you do, the above distillation of Doug's experience and wisdom should help you in your own quest.

[Share](#) or [Comment](#) on "Doug Casey's 9 Secrets for Successful Speculation" by Louis James

