Summertime Potpourri – AAV, ABM, FOM, LAC, SDX, VLE, PLU

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Solstice Reflections

Being a resource investor in this market requires a zen-like demeanour and the patience of a saint… though the amount of swearing involved for some can make the saint designation somewhat difficult these days. Just when you think the gold or metals are catching a bid, they fade again, further testing the resolve of the faithful; and at this stage if you're still in the resource sector in any way, shape, or form, you are certainly capable of some form of faith. I spend a lot of time looking at 5- and 10-year charts these days and seeing how far most of my watch list is from the lows on those longer-term charts and generally find some comfort there. For example, I pulled up a 10-year chart on Yamana (YRI.TO) yesterday while talking to a friend about the gold sector, and lo-and-behold it's pretty much at the bottom of its 10-year range. To take the point further, Teck (TCK.B) is a decent materials bellwether (whether you like it or not), and its chart pretty much looks like doo-doo on all time scales. Everyone's favourite Canadian copper small caps, Copper Mountain (CUM.TO) and Capstone (CS.TO), are also near 10-year lows. Pull up 10-year charts on Freeport (FCX.US) and Newmont (NEM.US) if you're still not convinced. Now, I'm not one to call bottoms, but it doesn't take a rocket scientist to know that ownership in the precious and base metals sectors is clearly somewhere in the "trough" zone. When they will recover is the million dollar question, but I think it would be hard to argue with the fact that we are closer to the bottom than the top, and buying the exact bottom is notoriously difficult (and it better be "when" not "if"… because if we are thinking in "if" terms, that doesn't bode well for global markets in general).

The energy sector is in a similar situation (though arguably not as bad as most stocks are closer to the middle of their 10-year range), but try telling that to someone invested in it. Small cap names in particular are reflecting the fact that even energy specialists are off foraging in greener pastures these days… or maybe just fishing at the lake as they wait for some form of life to re-emerge in sector funds flows.

Anyway, all of this is not to say anything other than it's tough out there in resource land and that optimism is the only thing standing between the patient resource investor and capitulation at times like these.

Covering the Bases

I've been traveling in one form or another for most of the last month, so keeping up with writing has been a challenge. The following is a quick-hit summary of names that I've written on in the past for the benefit of anyone interested in my two cents on the names. I follow a lot more names than I write on, but these are names that have been discussed since last fall here on the Hydra site.

AAV - Flawless execution. One look at AAV's stock chart says it all. No longer is AAV the Rodney Dangerfield of the natural gas producers. I can think of very few 1-year charts in the energy sector that are as pleasing as that of Advantage, which hit a 52-week high yesterday, closing at C$7.95. At these prices, AAV isn't cheap, but you pay for quality and the street isn't asleep at the switch any more on this name.

ABM - As I said before… if you haven't traded it, you haven't made any money on the name. I still see this as a project of significant importance to Canada's energy industry, but with the recent and unexpected departure of the largest shareholder and CEO (though Mr. Kriangkum does remain on the board), clearly something is afoot internally at the company. In the same vein, AGM voting results released today suggest underwhelming support for three of ABM's existing directors, which may indicate that there is a shake up coming at the board level. Clearly the company is in a state of flux and in the meantime Scott MacDougall has been appointed interim CEO. Athabasca's Firebag project is just too tempting for me to drop it at this stage and I'll follow this asset for as long as it takes to definitively see if Firebag can become one of Canada's most strategic frac sand sources. Where else can I get a project that could be capable of generating $1B of life-of-project after-tax cash flow from capex of less than $100 million? Will ABM catch the market's imagination again? Putting the Susan Lake Syncrude lawsuit to bed would be a good start.

FOM - Refer to the metals market discussion above. If FOM is good enough for Pierre Lassonde, it's good enough for me. It's a project with camp-scale potential and a clean balance sheet in a great jurisdiction. This story really hasn't bloomed yet, aside from that odd spike to $0.45 a while back, but I see no reason to change my view on it. Infill drilling at the Bigstone deposit this winter showed the ability of that deposit to generate impressive drill results and some scoping-level metallurgical test work is planned for completion by the fall of 2015. Foran is pretty much back at all-time lows and I believe that patient money could be rewarded in the long term.

LAC - It has a pulse, though the trading looks like there is at least one seller capping it in $0.40-0.45 range. I'm a believer in lithium for the long-term and LAC seems content to bounce between $0.30 and $0.45 for now. It's a huge resource, coming in at the world's 3rd largest by some estimates. I think it's pretty well de-risked in terms of chemistry and the brine appears amenable to POSCO's new lithium extraction technology. Here's hoping that the battery revolution continues and that POSCO and LAC formalize some kind of commercialization agreement in the coming months.

SDX - No change here from my initial note, but I would point out this Bloomberg title that was sent to me by a friend last week: "Egypt Hungry for Gas Imports as Output Falls Amid More Demand". That pretty much says it all. Egypt is signing up new partners abroad to meet internal gas demand needs. SDX still has to acquire, process, and interpret data on its likely-gas-prone South Disouq block, but I would say that SDX is not something to be dismissed just because of its 2 cent stock price. Patience is required.

VLE - According the the AGM presentation on the company's website, the Banarli 3D seismic acquisition program was completed on June 10th. Processing and interpretation should take 2-3 months, which leads me to believe that Banarli drilling should be on tap in early Q4. To some people that might seem like a long way away, but it's already June 23rd and three months from now VLE could be on the cusp of starting what might be the most important drill campaign in years for its small and loyal shareholder base. The stock has been fading on light volume as of late, repeating the pattern of the prior two years, but I think this year will be different in light of the pending Banarli activity. The enterprise value of VLE is somewhere around $22-25 million right now, which implies an EV/CF ratio of less than 2x (and a pristine balance sheet). It's a small international energy company in Turkey, so I understand the lack of broader market interest, but given the average production from the three Gurgen wells comes in around 400 boepd on a per well basis, it's not hard to see that VLE could look a lot different a year from now if Banarli starts clicking for them. This is probably one my my favourite names at the moment in terms of risk-reward and timing to a known catalyst.

PLU - The company has closed its 45 cent private placement, raising just under $3.4 million with strong support from its shareholder base (including Bob Disbrow who now owns about 18.5% of the company). The money will allow PLU to complete initial drilling in new areas of known surface uranium mineralization and, perhaps more importantly, complete a new PEA that incorporates the recent (positive) resource update. I suspect that PEA may show production costs falling below $20/lb, which will put an exclamation mark on PLU's status as one of the largest low-cost development projects on the planet. Eventually I think that market awareness will find its way to PLU, but as the Tom Petty song goes, ".... the waaaaaiiiiting is the hardest part".

Uranium spot prices have been ticking higher on low volume and just about everywhere I look, I see developments that would appear to be positive for the long-term outlook for the sector. Twenty-five reactors are now under application for restart in Japan, Saudi Arabia and Russia have signed a civil nuclear cooperation agreement (16 new plants are planned over the next 20 years), ERA's Ranger Deeps mine expansion has been put on hold, and China and India both continue to look for ways to meet their energy needs that do not involve coal.

All the best and happy hunting.

(Disclosure: The following represents my opinions only. I am not receiving any compensation for writing this article, nor does Hydra Capital have any business relationship with companies mentioned in this post. I am long AAV, ABM, FOM, LAC, SDX, VLE, and PLU.)