

Q&A

Exploration need not be so risky

Steve Poulton on rolling the discovery dice and rebuilding investor confidence in juniors

When commodity prices collapsed from 2013, investors lost both money and confidence in the traditional, single-asset junior resources company. Investors wanted less risk and an opportunity for near-term cash flow. The mining industry is not famous for its response time, so, it was prescient the foundations for Altus Strategies – a company of companies built to manage exploration risk – started working on this concept back in 2007. CEO Steve Poulton explains the genesis of the model.

Mining Journal: How did you get into mining?

Steve Poulton: I grew up close to the world-famous Jurassic coast in Dorset, meaning geology was front and centre in my formative years. I undertook a geology undergraduate and was fortunate to be tutored by Dr Bob Foster, a well-known and well-regarded economic geologist. Bob was a fantastic lecturer who shone a spotlight on the commercial pathways for geologists.

I completed a masters at Camborne [School of Mines] and was keen on junior exploration, however, there was no junior market in the UK – it was just after Bre-X and gold was in a deepening bear market. I spotted an advertisement in a free newspaper for an office manager with Mano River – one of the very few, UK-based juniors. I struck a deal with them to wear a few hats, if they'd teach me about the junior market. The chairman and founder was Guy Pas, a serially successful resource entrepreneur, and the CEO was Dr Tom Elder, a highly commercial and esteemed former Rio executive. They represented a formidable team. I ended as a director of Mano and both Guy and Tom are now advisors to Altus.

MJ: Has the industry forgotten how to explore?

SP: Some parts of it have. The biggest risk for an exploration company is not finding something. In its simplest terms, it's a statistics game. You're constantly trying to stack the discovery odds in your favour, by making the right calls on how you allocate resources. Critically, the risk there's nothing to be discovered in an area of interest is high. As an industry, we've not managed that risk well or shown investors it can be mitigated.

It's a sweeping statement, but many industries have been financialised over the past 30-or-so years, mining included. We've seen serious money from investment banking directed at fee-related M&A activity and leveraging balance sheets. This has prompted larger miners to favour acquiring growth at a premium rather than investing in exploration.



Altus chief executive Steve Poulton reckons exploration risk is too high not to be shared

In the vacuum created by the absence of majors, and the more recent decimation of traditional exploration juniors, new competition for assets has appeared. These include PE groups and emerging-market investors who have even deeper pockets, operate outside of the traditional market and assign a strategic premium to assets. This means competition for assets has been growing. Mid-tiers reacted fastest by taking direct stakes in juniors or their projects. Many majors are now doing the same. A scramble for assets looks like it's underway.

MJ: What is the project generator model?

SP: We identify early-stage opportunities, secure licences, explore, then seek partners. We do this across multiple commodities and in countries across Africa to spread individual project risk and increase the chance of success by exposing ourselves to as many projects as viable.

Third-parties carry the financing burden, meaning our shareholders avoid excessive dilution. The management of project generators often have larger shareholdings, in part down to the anti-dilution benefits of the model. Ensuring management is aligned with shareholders is perhaps the most important condition precedent when considering an investment.

Investors gave up on exploration partly because of the cyclical nature of the business, but also because shareholder money was simply being spent on many things other than exploration and, though the reward was high for, maybe, one in 100, the returns for most were negative. Most juniors have good intentions, but we don't believe the traditional approach is the smartest way for investors to gain exposure to exploration upside.

From an investment perspective, an asset manager would never buy just one or two stocks so we don't understand why an explorer would focus on just one or two projects – the returns can be spectacular, but so is the failure rate.

MJ: Firms like Altius Minerals and EMX Royalty Corp (TSX) have evolved into royalty firms, is that where this is heading?

SP: On each deal we do, we aim to retain a royalty. Royalties offer a potentially perpetual income stream without the financing risk, meaning they're a very elegant way of delivering shareholder returns. But it is difficult to go out and buy a royalty without paying fair market value.

Our model allows us to naturally generate, at some point, perhaps 20-30 royalties across Africa in multiple commodities, along with other project and equity interests. That's a business we think would be attractive to larger royalty groups as their own royalties start to fade and they need to replenish portfolios. Our potential income is from selling assets, selling a royalty or retaining a royalty stream.

MJ: Are you seeing the investor backing?

SP: A number of institutions are savvy to the model and want to back exploration. We are having good conversations with them and, in many cases, we're seeing investments. Spratt is an example. They invested in 2012 and have built their holding over time – they're respected for their ability to pick winning themes.

We've also had an institution take a position in Altus specifically because we are managing exploration risk similarly to how they manage portfolio risk. That is telling and hopefully other institutions will recognise this.

That said, right now I don't think there's much institutional appetite for grassroots exploration, regardless of the form it takes. Some of this is a function of cut-offs institutions have in terms of market capitalisations etcetera, but these thresholds tend to change as the market evolves.

MJ: Who's the most important person in mining?

SP: Xi Jinping must be a contender. China accounts for more than 50% in demand for so many metals and has a clear ambition to secure future supply, along with the markets through which metals trade.

MJ: If you could recommend one book, what would it be?

SP: 'The Map That Changed the World: William Smith and the Birth of Modern Geology' by Simon Winchester. It's the true story of how a humble Englishman, William Smith, through genius and tireless effort, despite personal and professional setbacks, completed the first recorded geological map of UK strata. If there's ever an inspiring story befitting a Hollywood movie, this is it. ■