Market upswing

2022 looks bright for juniors that can capture the attention of both new investors and traditional players

By Alexandra Lopez-Pacheco

In December 2021, Kinross Gold purchased the junior exploration company Great Bear Resources for $1.8 billion. That is the kind of fairy-tale ending every junior is hoping for, and it is also the kind of news that inspires Deepak Varshney.

Varshney heads two junior miners and spends much of his time raising capital for them. He believes successes like Great Bear motivate other exploration companies to keep going, even during times when financing is hard to obtain.

"When you see a success like that, I think it's good for the industry as a whole," said Varshney, CEO of both Xander Resources, which is exploring for gold, lithium and nickel deposits in Quebec and Ontario, and Usha Resources, whose focus is on identifying high-grade precious and base-metal deposits in Ontario, Arizona and Montana. "There is hope when you see a company being bought out or discovering something and making it work. I think it's a good thing for the whole industry. It's fantastic."

When it comes to raising capital, the junior mining sector has borne the brunt of the downturn in metal and mineral prices that first hit in 2012 and squeezed mining's share of the capital markets into a much smaller one. Many investors turned their backs on mining and switched to tech start-ups, then cannabis and more recently, cryptocurrencies.

Peter Nicholson, CEO of Wealth Creation Preservation & Donation Inc. (WCPD), which has helped mining exploration and development companies finance their projects with flow-through shares since 2006, said financing mining, especially exploration projects, has been an uphill battle for the better part of the last decade.

"There was a blip in 2016 when it was easy for about six months and then it got back to being miserable. A lot of the older geologists I spoke to who are in their 70s and 80s think it might have been the worst [time in living memory] to raise capital," he said. "Few people cared about mining. It was seen as a dead industry. Then came COVID-19. It's been awful in so many other ways, but it did shine a light on copper, commodities and gold as a safe haven."

At the time of writing this article, the SARS-CoV-2 variant known as Omicron was driving a fifth wave in Canada and the world, with rapid exponential growth. In these times in which uncertainty has become the norm, it is difficult to predict what the other side of the Omicron wave will look like. With that caveat, so far, over the last two years, the decade-long bear market for mining has been morphing into a bull market. That has opened up more opportunities for junior exploration and development mining companies to raise capital so they can show their metals the light of day.

Robust markets

While mining has still not regained its 2011 peak share of the pie, markets were pretty robust for juniors in general at the end of 2021. The top-ten-ranking mining companies in the TSX Venture Exchange, home to many mining juniors, saw a 520 per cent increase in their share price in 2020 and a massive 1,092 per cent growth in their market capitalization. The trend persisted in 2021 when the TSX Venture Exchange saw an annual increase of 23.9 per cent in the volume of shares traded and more than a 100 per cent jump in their value.

Not all juniors' ability to access capital benefitted from the resurgence of metals prices, however. According to Natural Resources Canada, the number of junior companies decreased by 11 per cent in 2020, while their combined spending increased by eight per cent to $1.03 billion.

In practice, Alan Hutchinson, a partner at the law firm Osler, Hoskin & Harcourt LLP who specializes in mining and corporate finance and securities, explained that investors have been selective recently. "Certain companies have been able to access capital and access it in a prominent way, which captures a lot of attention and focus," he said. "But there are still impediments for juniors to accessing the market."

Alex Bruvels, a partner at McMillan LLP, who also specializes in mining and capital markets and securities law, shared a similar observation. "Although there is a lot of interest in the space, there is a high volume of junior companies all vying for investor intentions, so although there are a lot of dollars available, there is definitely competition."

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Hutchinson also noted that opportunities for juniors to get financing over the last two years have seemed to come in windows. "[The mining companies] have to be very strategic and timely about when they do it. And that's a phenomenon I've seen play numerous times," he said.

It can be very challenging for companies to time their financing deals to effectively seize these windows of opportunity in the market. To do so, said both Hutchinson and Bruvels, companies need to be very organized with all their information and securities filings up to date. Additionally, Bruvels advised companies to also contact any third party whose consensus will be required to close a financing deal and to talk with all service providers, including auditors and legal counsel, before they begin negotiating.

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New investors, more investors

Between COVID-19's impact on metals prices and the Canadian federal government's favourable changes to Canada's flow-through share regime in 2020, which allows exploration companies with a non-taxable income to essentially sell off their tax-deductible expenditures at a premium and helps fund junior projects, WCPD saw a surge in its high-net-worth and hedge-fund clientele's interest in purchasing flow-through shares. The increase was not the only thing that changed. "We have found more and more people who want to buy our flow-throughs who have had zero previous exposure to mining," said Nicholson.

While this is a natural outcome of an upswing in commodity prices, many, including Jessie Liu-Ernsting, founder and principal consultant of Keystone Resource Solutions, believe there is a new factor at play. "I think the reason for a lot of brand new investors to mining, not just retail, but institutions as well, is because of the decarbonization trend."

Or, as Nicholson puts it, investors are realizing that "no metals, no green future."

Updating mining's story

To open the door wider to the capital markets and the opportunities presented by decarbonization, the industry as a whole needs to do a better job at telling its story – including its progress in environmental and social governance (ESG).

"I've been almost thrown out of gatherings," said Nicholson. "I went to social-impact conferences both in Cambridge, England, and Chicago and they asked me how I got in. They told me they didn't support mining and oil and gas. I had to explain to them we're not your grandfather's mine anymore."

Alex Christopher, president of the Prospectors & Developers Association of Canada (PDAC), agrees one of the big challenges the industry faces is educating a broad spectrum of society about today's responsible mining practices. "Whether it is with respect to land management or the environment, community engagement and investor management, I think we need to recognize this is becoming a very high-tech industry," he said. "I don't necessarily think the general public understands the level of technology that's in place in our mines and in our exploration practices. They don't even realize that the vehicles employed in the harsh mining environment are actually far more cutting-edge technology than the vehicles people are driving on the road."

At the same time, most experts agree that juniors today, including exploration companies, should be looking ahead and considering their project's potential ESG impact even if they do not expect to build the asset themselves.

"Investors want to make sure even exploration companies have a risk-management framework that takes ESG into consideration," said Liu-Ernsting. "It's just like when you are building a house, you have to build it on a strong foundation otherwise it's not sustainable."

Failure to have such a framework, Liu-Ernsting warned, could result in the asset being viewed as higher risk by potential buyers down the road and negatively impact the purchase price.

Virtual opportunities

Through much of 2020 and 2021, access to capital went largely virtual. "I think that's created both barriers and opportunities with a lot of executives essentially grounded, not being able to go out and market and fly all over the world," said Liu-Ernsting. "There are not a lot of opportunities to interact face to face. But [there are] opportunities to attend a lot more conferences virtually and there are a lot more new entrants to the marketplace for smaller companies, and a lot of the underwriters are also organizing investor conferences as well. There is a lot of opportunity for air time, although that in itself does mean increased competition."

Varshney believes that higher commodity prices and public interest in decarbonization, combined with a new generation of young mining executives and marketing teams, are expanding the opportunities for juniors to connect with a wider audience of retail and young high-net-worth investors, especially during the pandemic.

Social-media startups and tech companies without revenues might have been the hottest bets that took many a retail investor away from mining in the first decade of the century, but now some miners are using social media to win investors back.

"You are attracting a younger group of investors by putting out the information in the channels that they use [and explaining] that these metals are not necessarily dirty and that we can develop them in a responsible way as there is no way of getting away from using them," said Liu-Ernsting.

Varshney said there has been a surge in the number of young people in the retail investor market. "I can tell you this, I don't think we would have been advertising or putting together a

YouTube channel or having social media or Instagram for a company, but that's something we do now because the young retail crowd like to be engaged."

He and other young mining CEOs he knows even discuss building a presence on TikTok and working with influencers to get people interested in their companies and projects. "They might buy five thousand or 20 thousand shares, but if 100 [retail investors] buy ten thousand shares, that's a million shares," he said.

During the pandemic, thanks to greater virtual exposure, Varshney said he has been approached by many international investors. "I had a guy call me up from Iceland, of all places, and say 'Hey, can I take part in your financing?' Now we have investors in Norway, Singapore and all over the world. It's a global thing."

The younger crowd may have been the early adopters, but a lot of older mining CEOs who have historically not put as much value on things like social media are now paying more attention to populating their profiles with up-to-date information or using social media channels, according to Liu-Ernsting. "I've seen more and more of them recognize its importance."

This, said Varshney, is just the beginning. The new generation of mining exploration founders and executives will likely be exploring innovative ways to raise capital, including using new blockchain technologies.

Over the last two years, said Liu-Ernsting, "there really haven't been a ton of creative solutions for junior explorers so for the most part it's still the traditional options before cash flow. One thing I'm seeing, although not yet in Canada, that is newish is that some European funds are offering debt solutions to pre-revenue companies. It's not really prudent. If you don't have cash flow, you could easily find yourself in a loan-to-own situation and you can lose your asset."

Royalties and streaming

Typically, the closer to development a junior company is, the more likely it will be able to access traditional financing. "For [late-development] companies, it becomes about what the cost of financing is," said Christopher. "And how easy it is to get approved. I think the last few years have been a bit of a struggle, but it's never easy if you're looking to develop your first deposit and you're not actually a producer to begin with."

That challenge is likely the top reason there has been an upswing in streaming, an alternative financing solution for junior mining development companies. Streaming first appeared in 2004 when what is now one of the world's largest streaming companies, Wheaton Precious Metals, was spun out from the Vancouver-based gold major Goldcorp (now Newmont) as a way to raise capital to develop the mining company's San Dimas gold mine in Mexico. It was "a method of crystalizing the value of our non-core by-product silver production to generate the necessary capital to continue growing Goldcorp," Randy Smallwood, Wheaton's CEO, told *Mexico Business News* in 2015.

Streaming agreements consist of the mining company selling a percentage of its metals to the streaming company for an agreed upon payment at a discounted price when production begins. In exchange, the streaming company provides the mining company with upfront payments. This differs from royalty agreements, which were introduced into the market in the 1980s, and involve the mining company selling a percentage of future profits in exchange for upfront payments.

"The advantage streamers have over the banks is that the banks aren't always interested in funding a lot of the mid-tier emerging producers," said Hutchinson. "The classic [type of] project that really gave rise to streamers in general is that mid-tier company that is Scotch-taping together their mine finance from a number of different sources to get the necessary capital because no single entity in the banks or the markets is willing to provide the financing."

Streaming has evolved over the years with even majors chasing streamers during cash-strapped periods. Some analysts believe that for juniors looking to sell their companies, having a streaming arrangement may be perceived as losing future profits that devalue the company. Others, however, believe streaming is less dilutive than equity-based deals.

Vincent Metcalfe, CEO of the Nomad Royalty Company, sees his company as a long-term partner to mining projects. Founded in 2020, Nomad completed the acquisition of Orion Group and Yamaha Gold in deals totalling US$333.3 million in the same year. In 2021, Nomad closed several stream deals, including one with Greenstone Gold Mines for its project 275 kilometres northeast of Thunder Bay, Ontario, for US$95 million of upfront cash payments and another with South African Ivanplats (which is 64 per cent owned by Ivanhoe Mines) worth US$75 million in payments for its Platreef palladium-rhodium-platinum-nickel-copper-gold project located in Limpopo, South Africa.

Metcalfe believes the streaming sector has been growing because it has developed new and more favourable structures and options than what it offered in the past and because these solutions are more cost-effective than traditional debt and equity financing.

"When you are looking at project debt, you are looking at 10 per cent-plus in interest in most cases," said Metcalfe. "On the equity front, you are looking at typically at least 10 per cent when you are raising equity. You have to pay about a 10 per cent discount, plus you have to pay fees to the brokers."

With streaming, he said, the cost is between five and 10 per cent. Additionally, "when we invest in the project, we are investing in the life of the mine," he said. "So, we are here from day one until that mine closes. We are the longest possible type of investor. What that means is when the company is dealing with us, they realize we don't just want to get paid back in two or three years. We're able to put our payback over a much longer period, which allows the company to have more flexibility in financial assurance versus debt, which normally would be over a four- to seven-year term. Well, that debt has to be paid back within four years. With the stream, you push that payback out with less of a financial impact each year. It's really that we are creating partnerships here."

Some things are certain

The 1980s innovation that led to royalties and the early 2000s introduction of streaming, according to Hutchinson, "unlocked investment potential and capital for many companies," he said. "I think moving forward, someone is probably going to come up with something new."

In the meantime, one thing that won't change is the determination of mining entrepreneurs in Canada to keep drilling to find valuable deposits and drilling down to find financing opportunities. "There is money out there," said Varshney. "You just have to find it." CIM