



The Eight Ps

1. People

Property

THE EIGHT **P**S OF RESOURCE STOCK EVALUATION

By Doug Casey

I've been asked "What's the secret of finding winning gold, silver, and other natural resource stocks?" more times than I can even begin to count. And for over 20 years, my answer has remained pretty much the same: the Eight Ps.

The Eight Ps is a relatively simple question-and-answer process we use as part of our due diligence on the stocks we consider for recommendation in our monthly newsletters: *Casey International Speculator* and *Casey Energy Report*, and, for more active traders, our premium alert services, the *Casey Investment Alert* and *Casey Energy Confidential*. Only a small fraction of companies successfully make it through the Eight Ps screening and into the pages of our publications.

As you'll read, the Eight Ps process is relatively simple and, with a little practice, you, too, can use them to screen any and all resource stocks you are considering for your portfolio. At the very least, answering the questions will give you a much better understanding of the true potential of a company.

P₁ PEOPLE

The first question you want answered is "Who are the key players involved with the company?" As is the case with all human beings, some are more skilled, more honest, and harder working than others.

To state the obvious, Boy Scout virtues like honesty, thrift, courage, and diligence are always good traits for your management teams, as are competence, knowledge, experience, and, perhaps most important, a track record of success.

You can find this information from a variety of sources, starting with management biographies (increasingly available on company web sites), then doing your research by talking with the managers themselves or their investor relations staff. Use a service like Stockwatch.com to research the track record of the companies that the management has been involved with previously (during their tenure, of course)... and don't hesitate to ask your broker or even competitors what they think about the people in the deal. Despite being a multibillion-dollar, global business, the mining and resource industry is actually a pretty small village. If someone is a known snake oil salesman or poseur, chances are good you'll be able to ferret out that fact with just a couple of phone calls.

In addition to trying to sort out the black hats, a key goal of this exercise is to find out if investors have made money in their past deals. Or, if things didn't work out too well—mining is a high-risk business, after all—did the company at least make an honest attempt to "do the right thing" for their shareholders? Remember, nothing succeeds like success.

While we are on the topic of People, it is worth noting that there has been a noticeable gentrification of the mining business during the 20-year-long bear market that ended in 2001. Everyone in

the business is complaining about the fact that they can't find qualified mining engineers and exploration geologists because so many have retired or are getting ready to. It is understandable: it would take a fairly odd engineering school graduate to opt in to what is perceived as a politically incorrect and faltering "Choo-Choo Train" industry, rather than taking their degree down the street to a more lucrative or modern line of business. As someone who habitually looks for the opportunity embedded in just about any crisis, we use the labor shortage as a useful leading indicator by watching the career moves of the superstar mining pros. The good ones are in such demand that they can work for pretty much any company they want to... and so, as is human nature, gravitate to those projects which they believe will provide them with the best personal upside. Conversely, if the good people start to jump ship from a company, it may be a negative indicator.

In the final analysis—bet on the winners.

(Useful Resource: [Casey International Speculator](#) now includes the Explorers' League—a unique service that follows the careers of the world's most successful mine finders and builders. In order to be inducted into the Explorers' League, an individual must have a minimum of three economic deposits to one's name... no small feat, considering that probably 99% of the geologists in the business retire without a single deposit to their credit. If you're not currently a subscriber to [Casey International Speculator](#), there is no better way to benefit from our own application of the Eight Ps.)

P₂ROPERTY

As you approach the topic of "property," keep in mind that between 95% and 99% of all the properties controlled by mining companies will never actually become mines. That's because finding a mineral deposit with the potential to host an economic resource is time consuming and expensive. And unlocking the economic value of the embedded minerals is even more so. The cost of building a mine and a mill starts at a minimum of \$50 million these days, and can climb to a billion or more.

The good news is that you can make a fortune investing in companies that, for one reason or another, will never go into the production stage. It's all a matter of timing and knowing when to sell.

But back to the question of property. Regardless of whether or not a company ever develops a mine, the big money flows into companies with big mineral resources—and it is the big money flowing into a company that drives the price of your shares higher and provides you with the liquidity to exit with your profits intact.

That's the reason why the bigger and more geologically credible the prospective deposit, the better. How can you tell an ore body (definition: a deposit that can be economically mined) from moose pasture (definition: a large piece of land, usually located in the middle of absolutely nowhere that is good for nothing better than moose grazing)?

First off, start by ignoring claims made by mining company executives that are not derived from, at the minimum, drill results. (This advice applies in spades if the claims are not in writing for all the world to see.)

A favorite stunt used by some mining executives is to tell you that they have identified a major potential resource, using grab, chip, or trench samples. In plain English, those terms mean that geologists working for the company: (a) literally grab some rock from the surface of the property; (b) chip some rock from an outcropping; or (c) cut a trench across some interesting rock on the property... and then send the more prospective samples to a laboratory for assaying. As geologists are not paid to send in uninteresting rocks (otherwise known as “dirt”) to the lab, you can rest assured that grab, chip, and trench samples reflect the best possible rock the geologist can find.

Don't get me wrong. Finding highly mineralized rock on the surface of a property is a good thing. Just don't mistake it for a reliable predictor that an ore body rests beneath. Likewise, don't accept gross value calculations that are derived by simply multiplying, say, the price of gold by the inferred number of ounces of gold in a deposit. Such a simplistic approach to valuation completely ignores the costs associated with getting the minerals to market, which can be affected by engineering problems, physical position of the ore body, metallurgy, commodity prices, stripping ratios, cost of transporting ore (if required), the cost of building the mine and any processing facilities, the cost of financing, and so much more.

What to do? We may, on occasion, buy stocks that have only the earliest-stage indication of a mineral deposit—if we like the management/exploration team and know that they are fishing in the right pond. A company with respected management, a prospective property, and the money to embark on a good-sized drill program can make for a very good speculation.

Typically, however, we focus on companies that have tested their geological theories with a drill program and come up with logical results. And we will usually get a second opinion from a consulting geologist who will verify the company's interpretation of the data.

Next, if the story looks sufficiently interesting, myself or one of our research team will often visit the property—even if it's located in Outer Mongolia or some fly-infested corner of Africa. It is one thing to read about the geological characteristics of a property, but it's another thing altogether to examine the rock yourself, then look the geologist in the eye and ask him to describe his theory about deposit. Geologists are usually not very convincing storytellers.

So, when it comes to property, make sure that you are investing in companies that are chasing elephant-sized deposits... that don't insult your intelligence by pretending that early sampling or gross value calculations represent anything other than wildly speculative assumptions... and for companies with significant drill results, whose geological theory makes sense.

At the end of the day, before any decision is made on building a mine, the company will commis-

sion a bankable feasibility study—an exhaustive document that can cost millions of dollars to prepare. Only once that document is completed and confirms that an economic ore body exists can you assume that a mine may actually be built... and even then any number of factors (financing, metal prices, other company priorities, *etc.*) can stand in the way of it becoming a reality.

Put another way, never forget that you are not investing in this sector for the joy of seeing a mine built—but for the spectacular returns that can be made along the way to finding out whether or not a mine could be built.

A couple of final observations on this point. (1) Look for companies with more than one prospective large property. That way, if there is bad news (*e.g.*, poor drill results on one property), you have some downside protection from the company's other properties. (2) When a stock in your portfolio goes up by double or triple digits, don't forget to sell enough to lock in your returns and, ideally, scrape your original investment off the table. That way you are taking a free ride on any further upside potential and are protected if the next bit of news is negative.

P₃HINANCING

When we look at financing, we're essentially trying to match up the company's next-phase objectives with its ability to finance the cost of attaining those objectives.

Put another way, when we consider buying a junior explorer based upon prospective early drill results, the timing of our purchase may be predicated on the company's ability to finance a more extensive drill program to better define the size of the target mineralization. In this case, you have to ask, "Where's the money for the drill program going to come from?" Do they have it in the bank? Are they going to do another financing and, if so, what will the dilution factor be if we buy our shares today?

Or, are they going to keep their own corporate treasury intact and instead look for financing from a deep-pocketed senior mining company? If so, how much of the company or the rights to future development on the property will they have to give up?

Armed with the information of who is writing the checks, you then have to ask yourself, "How likely is the company to get the money they need?"

For this assessment, we again have to take management into account—*i.e.*, money follows success, and the successes the executive team has had in the past are directly correlated to how easily they can find financing in the future. Finding financing at a reasonable price will also depend on the quality of the property, the stage the company is in, the current share structure, and so on.

This is probably as good a time as any to share with you an important concept regarding invest-

ing in this sector. Namely, that the size of your returns will largely be a function of timing your investment before certain “ifs” are answered ... and then having the answers be good ones.

For instance, you can pick up a quick double by investing in a company after initial mineralization has been identified by some of the rudimentary, early-stage exploration sampling mentioned earlier—if the mineralization is subsequently confirmed at depth through a credible drill program.

If a comprehensive follow-on drill program confirms your initial results and demonstrates that your property contains a significant deposit, it’s back to the bank. If the company is then able to attract a deep-pocketed partner to fund additional drilling or even a bankable feasibility study, your stock lights up again.

If the bankable feasibility study confirms that the property can be economically mined, it’s happy times once more.

I am skipping over a lot of other events that can trigger an overnight double or triple in your shares... including the vending-in of an attractive new property... pulling a “glory hole”... having a well-known mining pro join the management group... the company hiring a competent public relations firm... even being written up by a renowned stock analyst. Any of those, and more, can do the trick.

The opportunity to hit numerous home runs throughout the rapidly evolving life of a resource company is a major differentiator between resource shares and garden-variety investments where stock gains are based on long-range business plans and new product development—it’s like Mattel actually drilling for the next Barbie doll.

Back to the topic of Phinancing: the bottom line is that you need to clearly understand where the money to move a project forward is going to come from—and at what cost to you as a shareholder. This is an important question because running out of money and being unable to quickly find more at the right price is akin to a giant “TILT” on a stock.

P₄APER

Paper and financing go hand in hand, since capital is almost always raised in form of new shares being issued. As a result, analyzing the structure of the company is as important as the geology of a company’s property holdings. That’s because some companies will too quickly dilute existing shareholders by raising money from sweetheart financings completed through private placements, often with full warrants. While I personally think these are wonderful—and I have made more than a few dollars by participating in private placements myself—there is a right way and a wrong way for a company to do financing.

To that end, we probably spend more time looking at the financial structure of a company than any other aspect. How many shares are outstanding? Who owns the shares? What percentage does management own? (I like to see management have a clear incentive for success.) Are any seed or private-placement shares about to come free trading and, if so, when and in what quantity? The last question can be very important from a timing perspective. Take a position in a stock just before a large number of cheap shares from a private placement come free, and you could be trying to catch a falling safe. Conversely, if you wait a bit, then put in a cheap bid, you can buy smart.

It is always worth understanding who's got the paper, at what price, and when the company may issue more. And don't forget to go through the simple process of multiplying the number of shares outstanding, fully diluted, by the current share price to come up with the market capitalization—always a useful indication of value. In overheated markets, it is not unusual to see companies with little more than early-stage drill results on land located somewhere north of Timbuktu boasting a market cap in the hundreds of millions.

Sure, they might get lucky, but are you really willing to bet your money on it?

P₅ROMOTION

“You can have the greatest product in the world, but still go broke if no one knows about it” is an old business adage that holds true in mining as well.

In more instances than I can remember, I've come across a well-run company turning up strong results on a geologically attractive property in a mining-friendly country... and the shares of the company are selling for pennies.

In these cases, the missing element is “Promotion”—the fine art of being able to communicate your story to the broad community of investors and analysts. I have a soft spot in my heart for these companies, which are typically run by mining engineers and geologists—scientifically minded individuals who sincerely believe that if they do their work well, the market will eventually discover them. While that occasionally happens—and finding an under-promoted company can offer us a terrific opportunity—more often than not these companies run out of cash and are unable to raise additional financings... at least at a cost that is not usurious to shareholders.

There are, of course, important nuances. If you can find an under-covered company with real merit that has just hired an investor relations staff or engaged a firm that specializes in corporate public relations, you can make a very nice return very quickly as the company gets the recognition it deserves.

Regardless, a company with an active investor/media awareness program will generate trading volume, driving your shares up and, again, giving you the opportunity to get your profits off the

table when you decide to sell. Therefore, before you invest you should ask company executives about their specific plans to get the company noticed.

So, promotion can be a good thing. It can, however, also be a bad thing when a company is built solely around promotion. It is that kind of company that proves true the old Mark Twain quip that a gold mine is “a hole in the ground with a liar standing over it.”

If you do your homework, however, it won't be long before you'll be able to tell the real cowboys from the ones that are all hat and no cattle.

P₆OLITICS

You may wonder what politics have to do with mining, but that would demonstrate a dangerous naïveté... because politics touch virtually every aspect of life, in literally every country in the world.

Politics can make or break a promising junior stock. Remember that a lot of the gold deposits found today are located in fly-blown Third World countries and backwater banana republics. That's why it is so important to research the political climate in a country where your company wants to go mining—is the government stable, are there rebel groups or kidnap gangs operating around your mine site? Is the country prone to nationalizing foreign interests at the first sign of financial trouble? These are all good questions to ask company executives.

Perhaps the biggest threat to mine development these days, however, is ecopolitics. Try to build a mine in the remotest corner of the remotest desert in the US and be prepared to have your application blocked by the Committee of Friends of the Box Turtle. And it is not just the US but a wide range of countries—to name just two, Romania and the Dominican Republic—where the permitting process can take many, many years.

It is for that reason that you will so often see mining projects being promoted in areas such as Mongolia or Eritrea—countries that are sufficiently desperate for money that they tend to be more tolerant of the mine aesthetics. (In case you are wondering, almost all new mining projects now factor in the cost of reclaiming the land once the mineral deposit has been mined out.)

One of the reasons why I find it so worthwhile to personally visit a mine site—and so far I've traveled to over 175 countries and counting—is that it gives me an upclose opportunity to assess the mood of the locals and the greed level of politicians. Politics count.

P₇USH

Push is the answer to the question: “What's going to move this stock?”



Often, impending or foreseeable drill results are the Push that's going to bring us the returns we seek. That's because we usually see the fastest, most dramatic increases in share price at the time when a small company makes a big discovery. And none of the years of preparation, surface work, geophysics, *etc.* count for anything until and unless drilling defines an economic tonnage of ore.

But Push can be anything: a successful transition to production, an major increase in the price of the underlying commodity, positive metallurgy or engineering reports, positive feasibility studies, a green light given to construction, a merger or an acquisition, realization of a royalty, the resolution of legal or political or regulatory difficulties... even a big promotional push can be the Push we're looking for.

Generally then, Push is any important development that either adds value to the company or removes a negative.

And if we can clearly see the Push coming, or see what look like favorable odds of it happening, we have a basis for speculation on rapid returns in our desired timeframe (12 months).

"What's the Push?" is a question we ask ourselves about every company we evaluate—and if we can't see the Push, we turn our attention elsewhere. Why park cash in even a great company, if it has no Push?

P₈PRICE

A deposit may be worthless if the market price of the embedded minerals is "X," but may become economic if the embedded mineralization goes to "2X." At "3X," the project may be worth hundreds of millions.

It is one of the more laborious aspects of analyzing resource companies that, as the price of the underlying commodity rises, you have to re-review your assessments on companies and properties almost across the board.

For instance, a few years ago, we were following a strategically minded copper company that used low copper prices to inexpensively buy a huge package of proven properties. Back when copper had been selling for 75 cents a pound, no one had wanted anything to do with the company. As copper went over \$1.00 a pound, the company's in-situ resources became worth hundreds of millions of dollars and everybody and their uncle wanted to own the company. Our shares quickly doubled.

So, periodically, as resource prices rise, we do a reassessment of the companies we have previously evaluated and found unattractive due to the Price factor.

Also on the topic of Price, it is essential that you use rational price expectations when calculat-

ing the potential for your investment. Ultimately, gold might go as high as \$2,000 or even \$3,000 an ounce. But if achieving those high levels will be required in order for your company to do well, you are taking an unhealthy level of risk. So, ask yourself: “What will this company be worth at \$500 per ounce? Will it be able to justify its current market cap?” If the answers are positive, you may be on to something.

CLOSING THOUGHTS

At Casey Research, we have always been big believers in making the trend your friend ... and the real money is to be made by investing ahead of the masses. Consequently, our approach has been to look for solid speculations in sectors of little public interest because that allows us to buy cheap and, if we are right, sell high as the crowds rush in.

Even a casual glance at the current state of the US economy—the engine that drives much of the world—tells us that the end of a long road is ahead. The fact is that the US government cannot endlessly take on debt, bail out every major bank and corporation, and create money by the truckloads. In time, the fundamentals will prevail—as we are already seeing—and tangible investments such as gold and silver will become the investment of choice of intelligent investors looking to avoid the negative wealth effect of a rapidly eroding dollar.

The metals’ rise in recent years is a clear sign that the trend is now the friend of resource stocks. Because there is only a limited number of quality resource investments available, as the serious money begins to flood into them, investors who take a position now will be very well rewarded.

If you are seriously considering investing in natural resources, don’t put it off. The leverage on these investments can turn dimes into dollars ... if you exercise diligence and take the time to carefully work through the Eight Ps.



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