Adventure Capitalist

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Buy One of the Greatest Gold Companies for Under $1 a Share

Rob McEwen had a ton of doubters early on…

That's what he told me in San Francisco a few weeks ago at the Silver Summit and Resource Expo.

This 20-year-old investment conference attracts some of the greatest minds in the resource sector. And I was thrilled to be able to spend some one-on-one time with McEwen.

He is 65 years old and a small, soft-spoken man. At first glance, you would never guess he's one of the most-driven and innovative thinkers in the mining industry.

McEwen's work ethic can be traced back to his late dad Donald McEwen. Donald was always fascinated with gold. He traveled the world to visit some of the biggest mines. And he shared many of his experiences with Rob at the dinner table.

Donald started his own securities firm that specialized in mining. Rob recalls how mining prospectors were often at his house in the 1970s, looking to get financing from his dad.

Rob worked at his Donald's investment firm in the summers while earning his MBA. He also worked at Merrill Lynch for a brief period before buying control of his father's company in the early 1980s.

Around the same time, Donald created a separate holding company for gold mining shares and gold bullion. This took place about three years before Donald passed away.

He named the holding company Goldcorp (GG).

By the late 1980s, Rob was looking to grow the company. He set his sights on the Dickenson Mine. It was located at Red Lake in western Ontario. The first gold produced from this mine dates back to 1948.

The Dickenson Mine was not producing much gold at the time. However, Rob believed the mine had huge potential. That's because it was sitting next to the Campbell Lake mine — one of the biggest, high-grade gold mines in the world.

Rob used Goldcorp (which he controlled after his father passed) to bid for Dickenson. But he wasn't the only one interested in the property. Ned Goodman, billionaire and founder of wealth management firm Dundee Corp., also bid on the property.

Ned was a rival mining investor at the time. He sought a court injunction against McEwen. Yet, *with one day to go before the Goldcorp offer expired*, an Ontario judge threw out Goodman's case.

In April 1989, McEwen gained control of Dickenson and its Red Lake gold mine.

This should have been a huge milestone for Goldcorp.

Instead, shareholders and family members turned on McEwen.

McEwen Fights Critics Head-on

After winning control of the Red Lake mine, McEwen was ready to drill. However, he needed to transform Goldcorp from a holding company into an operating company.

Without getting too technical … an operating company could "more easily" raise the millions in cash needed for exploration. Plus, Goldcorp's share price was depressed due to its "holding company" status.

By the early 1990s, McEwen named himself CEO and replaced the entire board of Dickenson Mines. He fought off a class-action lawsuit by a major shareholder. He also fought aggressively against relatives, as most believed Goldcorp would be a complete failure after the acquisition.

By 1995, McEwen's organizational problems were behind him. He invested $10 million to explore Red Lake. Just six weeks later, Goldcorp published its first drilling samples (from nine holes). The grade in these samples *averaged 9.08 ounces of gold per ton.*

To put this in perspective, this grade was 30 times higher than the average grade that was previously mined at Red Lake.

Keep in mind, some of the smartest people in the industry thought Red Lake was a dead project. The economics did not work. That's why shareholders and family members strongly opposed the purchase of this mine.

McEwen's instincts were dead-on. But before he could pop the champagne and celebrate, he ran into another major problem…

In June 1996, members of the United Steelworkers of America walked off the job at Red Lake.

Now, disagreements between companies and unions happen all the time. For centuries, we've seen workers walk off jobs across a lot of industries in an effort to get paid more money or restructure their benefits.

However, the strike at Red Lake lasted for nearly 4 years!

McEwen's production managers begged him to settle. Instead, he hired more-educated workers. He also housed 150 non-union workers on site who continued to do exploration work.

His idea to play hardball with the union was not based on ego. McEwen knew he needed a change of attitude at the site. Plus, there was little room for him to negotiate. After all, production costs at Red Lake (pre-strike) were $360 an ounce. This was only 5% below the market price of gold back then.

By 2000, McEwen offered strikers a severance package, a signing bonus and stock options. He also hired back 45 of the 180 workers who went on strike.

This left only one small problem.

Goldcorp's geologists had difficulty coming up with an exact estimate of how much gold could be mined from Red Lake. More important, his team could not identify an exact location to drill.

McEwen's solution to this problem was highly controversial. His own geologists were skeptical. *Yet, his innovative idea wound up changing the landscape of the entire exploration industry.*

The 'Goldcorp Challenge'

In 1999, McEwen attended a conference at MIT for young company presidents. That's where he learned about Linus Torvalds and his massive team of software developers.

Linus created a free operating system called Linux. He shared his code — used to create this system — with the world. This opened up his operating system to thousands of other programmers (called open source) who can then modify and improve the system.

McEwen thought this idea could be applied to exploration.

In March 2000, McEwen launched the "Goldcorp Challenge." He put up nearly $600,000 in prize money to anyone who could find the best method to mine its 55,000 acre Red Lake property.

Goldcorp published all of its data (four hundred megabytes worth) on its website. This included data from Red Lake dating back to 1948.

As McEwen said …

"We'll ask the world to tell us where we're going to find the next 6 million ounces of gold."

This move was highly controversial.

For over 100 years, mining companies kept their data in-house. This information is top-secret and never shared with the public. Even Goldcorp's top geologists were skeptical about sharing information.

But news about the contest spread through the industry like a wildfire. In just a few weeks, more than 1,000 people from over 50 countries began crunching the data through the Internet.

Geologists were not the only ones to respond with ideas. Graduate students, mathematicians and consultants also weighed in. McEwen was floored with the amount of responses and the advanced methods — like physics, computer graphics and intelligence systems — used to crunch the data.

When all was said and done…


FAST COMPANY

HE STRUCK GOLD ON THE NET (REALLY)

ROB MCEWEN OWNED AN UNDERPERFORMING GOLD MINE IN NORTHWESTERN ONTARIO, AND HE NEEDED NEW IDEAS ABOUT WHERE TO DIG. SO HE BROKE NEW GROUND — AND MADE DATA ON THE MINE AVAILABLE ONLINE TO ANYONE WHO WANTED TO HELP. EUREKA! THE INTERNET GOLD RUSH WAS ON.

A 2002 FastCompany.com headline
suggested McEwen struck Internet gold

The contestants identified 110 targets on Red Lake for potential drilling. Roughly 50% of these targets were new to Goldcorp.

More important, substantial amounts of gold were found on over 80% of these targets.

McEwen's use of open source technology helped turn Red Lake from a struggling property into one of the biggest producing gold mines in the world.

It propelled Goldcorp from a small $50 million company into a *$10 billion gold producing giant.*

I'm sure McEwen's early shareholders and family members no longer doubt him. From 1994 through 2005, Goldcorp surged nearly 1,300%. **That's over 100% returns annually!**

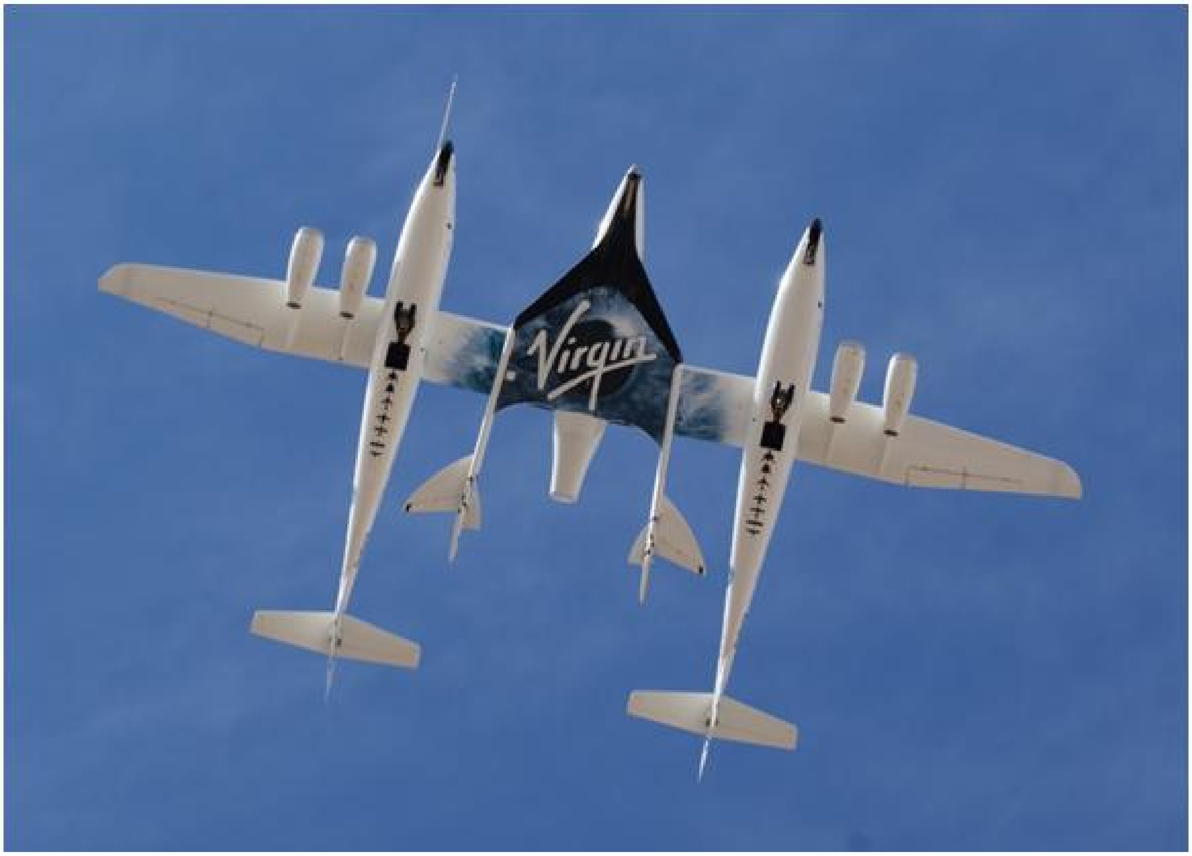
In 2005, McEwen stepped down as CEO of Goldcorp. This was shortly after the company acquired Wheaton River. This opened the way for Ian Telfer (CEO of Wheaton River) to become the new CEO of Goldcorp.

McEwen said, "Goldcorp grew significantly in size and complexity. This includes the demands of the many governmental and regulatory agencies the company reports to." He also said, "Goldcorp demands a new boss to take the company to the next stage of development."

But this statement was more about being politically correct than the actual truth.

You see, McEwen is one of the most-innovative people in all of mining. He's a resource executive who loves technology — which is a rare find in the industry. In fact, a few years ago he spent time on a zero-gravity plane with his close friends Elon Musk (high-tech billionaire), James Cameron (Hollywood director) and Jim Gianopulos (CEO of Fox Films Entertainment).

McEwen also booked his ticket (along with dozens of other influential people) to fly to space on billionaire Richard Branson's SpaceShipTwo plane. The launch is expected to take place in 2017.



However, McEwen's always had an "old school" way of doing business. He believes the top goal for any company is to be profitable. He is a master of economics — only taking on low-cost projects in the gold industry. *And he rarely uses debt to grow a company.*

The new Goldcorp was changing its business model. They were about to take on huge amounts of debt to grow the business. **And McEwen wanted no part of it.**

For example, Goldcorp had zero debt and a market cap of around $10 billion when McEwen resigned in 2005…

Today, Goldcorp has a market cap of $9 billion. Yet, the gold-producing giant is sitting on $2.5 billion in debt … it reported an earnings loss for three straight years … and it was forced to take billions of dollars in losses (write-downs) on several of its projects.

And the stock has lost plenty of luster, to boot.

Meanwhile …

McEwen is Building The 'Next' Goldcorp

In 2012, McEwen decided to create another mining powerhouse…

He already owned huge stakes in **U.S. Gold** (owned 26% of the shares outstanding) and **Minera Andes** (owned 27% of the shares outstanding).

He then decided to merge these two companies and form **McEwen Mining (MUX)**.

McEwen's goal as chairman is to *"outrun what Goldcorp has become."*

McEwen Mining (MUX)			
Market Cap:	$265M	Insider Ownership:	25%
Revenue (TTM):	$75M	Volume (Avg Monthly):	733K
Earnings (Last Q):	$0.01	**Balance Sheet**	
Operating Cash Flow (TTM):	$11M	Cash:	$31.7M
Price / Book:	0.6x	Long-Term Debt:	$5.1M

One way to make this happen was to merge his two companies (McEwen was Chairman and CEO of both companies). This would provide McEwen Mining with scale, or put the company on the radar of institutional investors.

You see, Minera was generating cash flow. However, the company had no project pipeline. Meanwhile, U.S. Gold was the opposite of Minera. The company had little cash at the time — but it did have an impressive pipeline with huge potential.

In 2012, McEwen Mining began trading on the NYSE. The company's market cap grew to $1.4 billion before crashing alongside the rest of the commodity markets.

Its resource portfolio included:

- Gold Bar and Tonkin (gold projects) in Nevada
- El Gallo (gold/silver projects) in Mexico, and
- San Jose (gold / silver) and Los Azules (large copper project) in Argentina.

McEwen's San Jose and El Gallo are producing mines.

The company has a 49% stake in San Jose. It's located in the Santa Cruz province of Argentina. It's an underground operation located about 12 miles away from Goldcorp's huge Cerro Negro project. Cerro Negro is expected to produce over 400,000 ounces of high-grade gold in 2015.

San Jose produced 94,161 gold ounces and 6.5 million silver ounces in 2014. That works out to roughly 46,000 gold ounces and 3.2 million silver ounces (49% stake) for McEwen. The company expects San Jose to produce 46,500 ounces of gold and 3.1 million ounces of silver for 2015

El Gallo (includes two projects) is located in Mexico's Sinaloa State, along the foothills of Sierra Madres. Commercial production began in 2013. The following year, El Gallo 1 produced a record 38,200 ounces of gold and 26,000 ounces of silver.

El Gallo 2 is projected to produce over 100,000 gold equivalent ounces annually. *All-in production costs are roughly $800 per gold equivalent ounce.* **This makes El Gallo one of the lowest-cost producing mines in the world.**

As you can see from the map below, McEwen's El Gallo project is in close proximity to several huge gold- and silver-producing properties.

Last month, the company raised El Gallo's production guidance from 138,000 ounces of gold equivalent ounces to 153,000. This will result in an increase in cash flow in 2016 and beyond.

El Gallo also has huge expansion potential. The El Gallo Mine Complex (100% owned by McEwen) consists of five gold discoveries and two silver discoveries. This opens the door for more exploration once silver and gold prices recover from these super-depressed levels.

Future catalysts include McEwen's Gold Bar project (located in Nevada). Experts expect this to be the company's next major producing mine. A recent feasibility study indicates the mine could produce 65,000 ounces of gold annually.

Permits for Gold Bar have already been filed. McEwen estimates that they could receive regulatory approval by January 2017. The cost of production for the Ruby Hill and Cortez mines (competitors' mines located near Gold Bar) are under $750 an ounce.

If the all-in costs at Gold Bar are similar to its peers, we could see production start as early as 2018.

McEwen's Los Azules mine is one of the largest undeveloped high-grade open-pit copper projects in the world. And the recent change in leadership in Argentina could provide a huge catalyst for McEwen Mining.

An updated Preliminary Economic Assessment (PEA) suggests that Los Azules contains *nearly 20 billion pounds of copper*. It also contains 3.3 million ounces of gold resource and over 100 million ounces of silver resource. (Each estimate includes indicated and inferred.)

Due to the rough political landscape in Argentina, Los Azules has been a dead project for a while. In fact, McEwen was looking to sell the project since 2012.

However, the new president (elected last month) announced plans to open up Argentina to foreign investments. He also promised to lift currency controls — which discouraged foreign investments in the past.

In other words, the Los Azules mine is now a major asset for McEwen.

Commodity prices would need to move higher before it's economical to develop. But the recent election is a huge win for McEwen, who could wait to develop this asset … or even sell it and a much-higher price than he could have in 2012.

Why You Should Buy
McEwen Mining Right Now

I talked earlier about my one-on-one meeting with Rob McEwen in San Francisco. Our meeting — which consisted of me asking tons of questions — lasted about 45 minutes.

Shortly after, I started doing my own homework on the company. In short, I wanted to find out why this gold-producing company — led by one of the smartest and innovative thinkers in the entire mining industry — *was trading in line with some of the riskiest junior mining stocks who were not producing anything*.

The reason was simple.

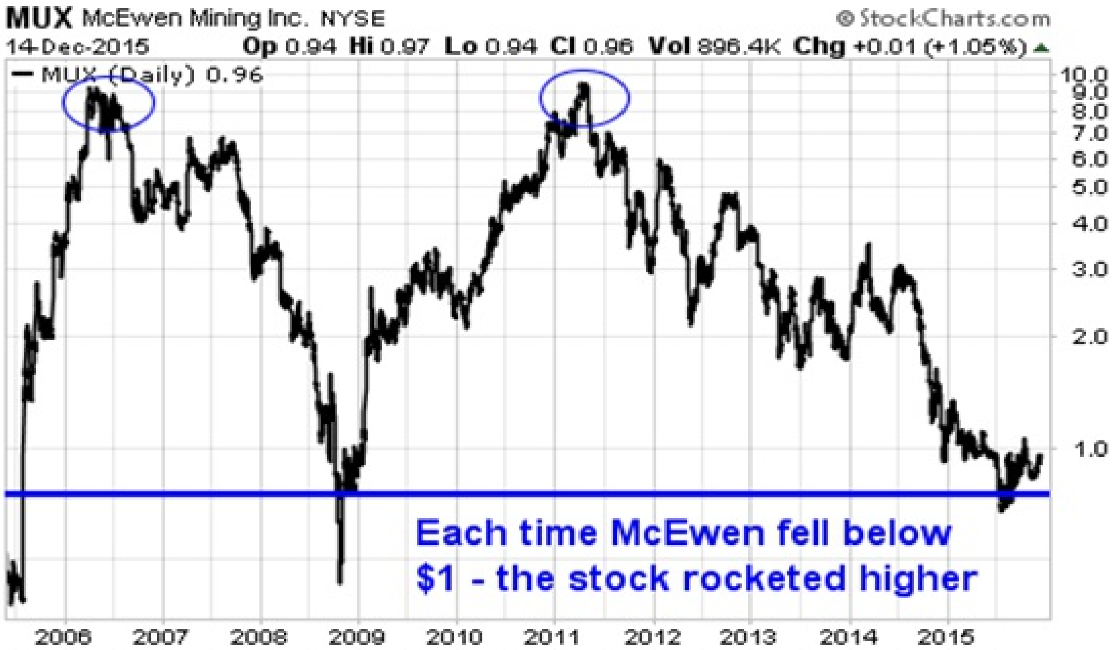
It's one of the biggest bear markets in commodities in 30 years. *Every commodity-related company* is being taken down regardless of fundamentals or who is running the company.

This kind of disconnect only happens during EXTREME times. In other words, there are only a few times during your life where you can buy some of the world's greatest companies for pennies on the dollar.

For example, you could have bought **General Electric**, **Bank of America** and **Ford** for under $5 a share during credit crisis. People who invested in these quality names in early 2009 are likely sitting on life-changing gains.

McEwen Mining could provide similar returns for investors willing to buy the stock today.

McEwen is currently trading under $1 a share. As you can see from the chart below, McEwen only fell below $1 a share twice over the past 10 years. Both times, *the stock surged to over $9 a share.*



Keep in mind … *McEwen is not an early-stage exploration company that's not generating revenue. The company is not in dire need of cash.*

In fact, McEwen generated $75 million in revenue over past 12 months. They are currently producing gold … generating a profit … and have a super-strong balance sheet.

This puts McEwen in a class of its own considering most companies in the industry — including the biggest gold producers — have weak balance sheets and are reporting huge losses.

But before we consider buying McEwen, we must make sure it passes our…

5-Rule System to Follow
Before Buying Any Mining Stock

In *Adventure Capitalist*, I've talked numerous times about my unique system for buying mining stocks. It's basically a set of 5 rules experts follow before putting money to work in junior mining companies. These experts include Rick Rule, Jeff Phillips, Marin Katusa and Frank Holmes…

These legends have more than 100 years of combined experience analyzing, financing and investing in resource stocks. They have followed these specific rules throughout their careers. That's why they have the best track record for picking small, early-stage resource companies.

The five rules include…

1. **Invest alongside an experienced management team**: Find a team that has taken a mine from early-stage development to production.
2. **Cash is king**: Make sure the company has enough money to develop its projects.
3. **Geography**: Be sure the company operates in mine-friendly areas of the world.
4. **Infrastructure**: Make sure the company's properties have roads, water and electricity already in place. These are huge expenses that are often overlooked.
5. **Insider ownership**: Be sure management has a stake in the game.

<u>McEwen Mining easily fits into our system.</u>

Rule #1 Experienced Management Team

I explained throughout these pages how Rob McEwen is one of the most-innovative and -respected executives in the resource industry. He has over 30 years' experience financing and building companies from the ground up. This includes Goldcorp — which became the largest gold producer in the world.

McEwen also has a history of operating profitable companies that generate cash flow. He exercises financial discipline and will not build a mine unless the project can generate at least a 20% internal rate of return (IRR). He also looks for a quick payback period and projects with low expenditures (capex).

Plus, McEwen almost always maintains a strong balance sheet and rarely uses debt (leverage) to grow a company. Having a strong balance sheet can significantly lower your risk during bearish times, which happens often in the volatile and cyclical resource sector.

Rule #2 Cash is King

McEwen Mining is sitting on a net cash position of $25 million. The company is also cash flow positive and pays a dividend. To put this in perspective, most mining companies are losing money today. This includes big producers like Goldcorp and Kinross.

The company's strong balance sheet is a positive on many levels. With assets becoming cheaper by the day in the resource space, McEwen can use its cash to purchase projects trading for just pennies on the dollar. Also, a strong balance sheet (coupled with great assets) makes McEwen Mining a potential takeover candidate.

Rule #3: Geography

Most of McEwen's assets — including its two producing projects — are located in Nevada and Mexico. These are two of the most mine-friendly districts in the world. The company also owns assets in Argentina, which carries a high degree of geopolitical risk.

However, after 12 years of the same regime … a new president was elected in Argentina last month. He's pro-mining and expected to open up the country to foreign investments. This has led to front-page stories of how top money managers and institutions are now pouring money into Argentina.

More important, McEwen says he would never operate in a country where his workers' lives are at risk. This keeps his focus mostly in the Americas and Europe.

Rule #4: Proper Infrastructure

Making sure a company has proper infrastructure usually applies to investing in junior miners. That's because these small early-stage plays need to build facilities, roads and electricity *before* pulling one ounce of gold out of the ground.

These massive costs — which could run well over $10 million depending on the project — are often overlooked by inexperienced management teams and investors.

McEwen Mining is a producing company. They already have infrastructure in place. Plus, Rob McEwen is a seasoned veteran. Like I explained earlier, he has a solid history of exercising financial discipline before buying any asset. This includes buying projects with infrastructure already in place, or projects that are in close proximity to major producing mines.

Rule No. 5: Insider Ownership

Rob McEwen is a huge fan of insider ownership. In a recent interview he said, *"I listen to management's pitch and if it sounds interesting I ask about their share ownership. If I find they are talking a big story without having* *a large investment in their firm, then my interest starts to fade."*

McEwen has always been a huge shareholder in his companies. In fact, **he owns 25% of McEwen Mining.** In other words, he has a big stake in the game. He stands to lose the most money if McEwen Mining is not successful. And he stands to gain the most if the company is successful.

Also, McEwen does not pay himself a salary or a bonus, and he does not have any options. This is a rarity in the mining industry. Most executives pay themselves handsomely — regardless of performance — and have tons of options. In short, McEwen's goals are 100% aligned with shareholders'.

For perspective, I've researched hundreds of small mining companies over my 20-year career. Probably fewer than 3% pass my five-rule system for buying mining stocks.

There are still *more* reasons why I like McEwen Mining right here and now.

Bringing it All Together …

McEwen Mining is one of the rare gems in the resource space.

It's a gold producer that has extremely low operational costs. This allows McEwen to generate positive cash flow, maintain a strong balance sheet and be profitable in one of the worst environments for resource companies in 30 years.

The company has seen huge production growth (in gold equivalent ounces) since 2012. This trend is expected to continue in the years ahead. McEwen's cash balance and cash flows are also expected to trend higher in the years ahead. This is based on gold prices not falling much from current levels.

Turning to valuation, McEwen is trading at a 50% discount to its tangible book value. At this price, the market is placing almost no value on the company's assets in Argentina. This is important for new investors since the political landscape in Argentina is much more favorable following the recent election.

Based on my estimates, McEwen should be trading north of $1.40 a share. That's about 50% higher than the current price. However, if the market stabilizes and gold prices move higher over the longer term, we could easily see 300%-plus gains.

My forecast could prove conservative. Remember, the last two times McEwen fell below $1 a share — *the stock surged to $9 (see chart above).* This amounted to more than 800% gains for investors who bought the stock under $1 and sold shares near the top.

<u>**Action to Take:**</u>

> **Buy McEwen Mining (MUX) under $1.05 a share.**
>
> **Once establishing a full position, set a 35% stop.**

This would put your stop around $0.65 a share, or below the lowest level the stock has traded in over 10 years. In other words, this stop should allow you to hold the stock and invest alongside Rob McEwen for years instead of months.

All my research tells me that McEwen Mining offers investors huge longer-term returns. However, this recommendation (along with every other investment) does have risks. If gold prices fall below $900 an ounce, McEwen will see declines in cash flow, its treasury and earnings.

The company could experience operational problems at its producing mines. This could result in a huge decrease in production — which would negatively impact sales, earnings and eventually the stock price.

McEwen is a small-cap company. It also operates in one of the most-volatile industries in the world. This means the stock could have huge price swings on a monthly basis. This type of volatility may not be suited for risk-averse investors.

Subscribers should understand these risks before investing in McEwen. However, most of these risks seem to be priced into the stock, based on my research.

If you like the potential risk-vs.-reward setup in McEwen, be sure to enter your buy order as soon as you can.

Good investing,
Frank Curzio