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It’s Getting Better

A Monday Morning Musing from Mickey the Mercenary Geologist

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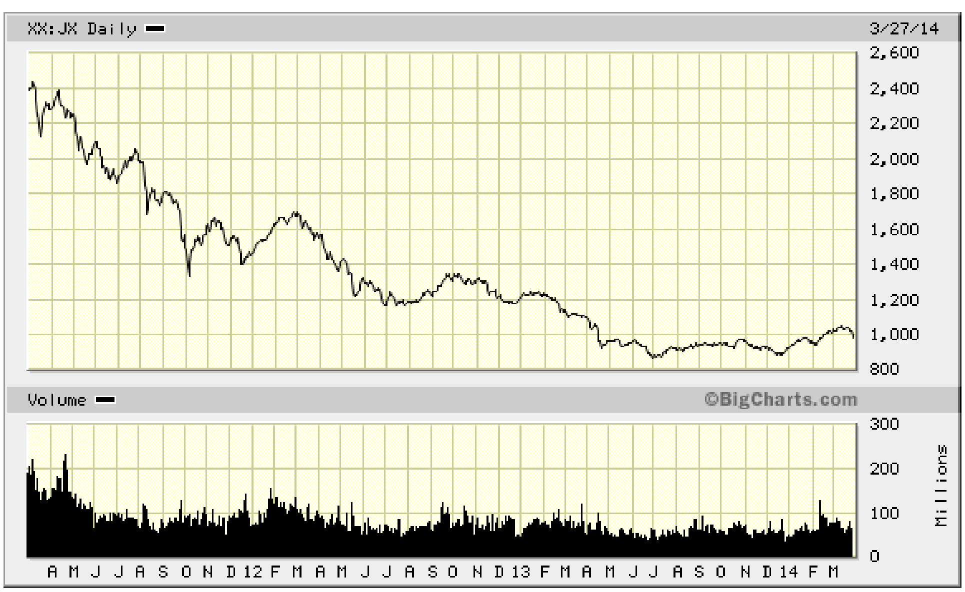
In assessing the junior resource market, I now feel bold enough now to quote these words from a song on the best rock and roll album ever recorded:

I admit it's getting better
A little better all the time (It can't get no worse)
Lennon and McCartney, from Sgt. Pepper’s Lonely Hearts Club Band (1966).

Indeed, it is getting better, a little at a time.

The bear market for junior resource stocks began on Monday March 7, 2011, and has continued unabated for over three years. If you are skeptical about the statement, this chart of the Toronto Venture Exchange Index illustrates my point. The post-global economic crisis high of 2440 occurred on March 4, 2011, the last trading day before the annual Prospectors and Developers Association Convention (PDAC):

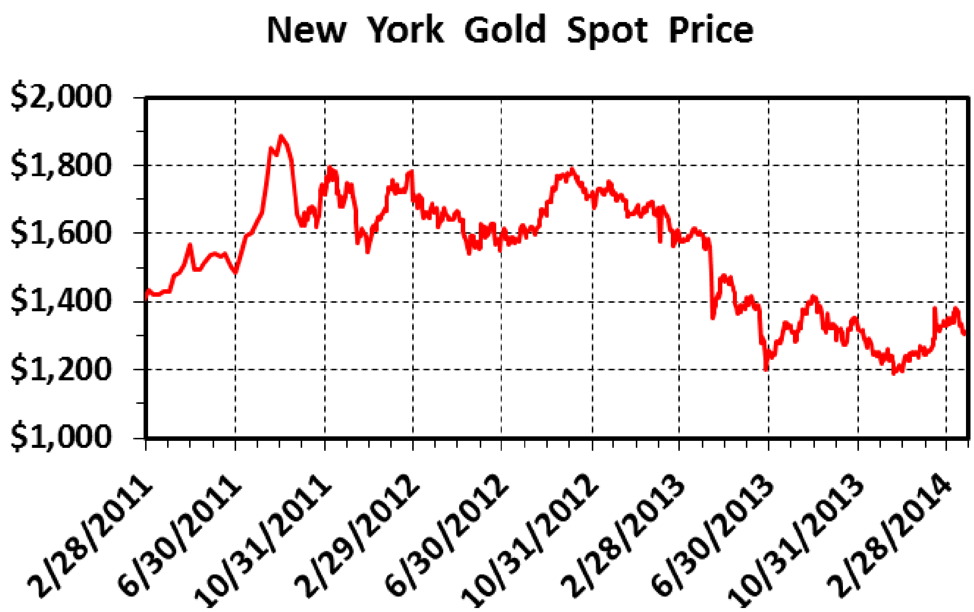


With today's close of 990, the Toronto Venture Exchange Index has given up 60% of its high three years ago. However, the Index has gained 15 % since the post-crash low of 860 on June 27, 2013 and is up 10% since mid-December.

That said, it has come off over 5% from an 11-month high of 1046 on March 12. The recent weakness correlates with drops in gold and copper prices. Since March 14, gold has fallen from $1382 per oz to $1296; since March 7, copper went from $3.21 per lb to $2.92 before rebounding this week to close at $3.03.

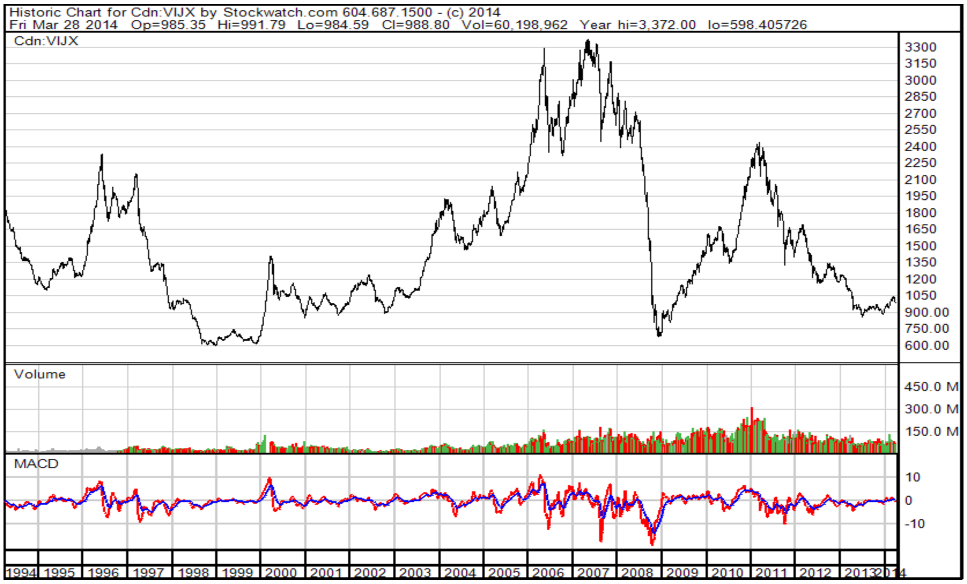
Given nine months of hindsight, it appears the bear bottom occurred at the beginning of the summer doldrums in late June and that this bottom was tested during tax-loss season in mid-December.

It is generally accepted that as goes gold, so goes the junior resource market. Let's test that idea by charting the value of gold in US$ from the bear market beginning to now:



The supposed correlation of the Venture Index and gold price does not hold up over the past three years. However, with a little help from my friend, I discovered something in another chart that looks more compelling.

This 20-year chart combines the Vancouver Stock Exchange Index from 1994-2000 and the Toronto Venture Exchange Index from 2000-2014:



I draw your attention to a 21-month time period from early Q2 1998 to the beginning of 2000 when the Vancouver Index first took a steep nosedive over four months and then was range-bound for the next 17 months.

Now let’s compare that period with one beginning in February 2013 when the Venture Index again took a steep four month fall, and has been range-bound for the past 10 months.

Also note the lack of volatility during 1999 and also since mid-2013, with the MACD hovering around zero in both instances.

By analogy, these patterns suggest that there will be another six-seven months before we can expect this bear market to show some sustained improvement.

We will not hope for or expect an abrupt spike to the upside like occurred in early 2000. That came as the high-tech bubble migrated north from the Silicon Valley to Seattle and then on to the Vancouver junior market, bringing a horde of orphaned companies that could not be financed stateside. This spike was quickly followed by an equally impressive fall, although it did result in establishment of a much higher base for the Vancouver Index.

I’m not buying that the recent mass movement of junior “miners” into the medical marijuana venue will manufacture a mania like the dot.com buzz of year 2000.

I’m just sayin’ folks, that the current pattern looks similar to me. But please realize that I’m a fundamentals guy and I don’t know enough about technical analysis to even be considered dangerous.

Based on what I do know, here are factors I see as encouraging given recent fundamentals of the junior resource sector:

- A select minority of good companies on the TSXV has led the rally, particularly in the gold, copper, and uranium spaces. This short rally has not been broad-brushed: although many stocks are higher, most are still in the toilet waiting to get flushed.

- The “PDAC curse” that has overhung the bear market for the past three years has not appeared so far in 2014.
- Venture capital has begun to flow back into our sector via both hedge fund movement into the commodities sector and private placement financings by “smart money” in the junior equities space.
- New discoveries and positive drill results are being rewarded with sustained liquidity. Recent successes have not simply generated selling opportunities for those anxious to exit the market.
- A more positive outlook has been championed by contrarians like yours truly and some other usual suspects in recent interviews and at investment conference presentations.

That said, we are approaching a typically unsettled season for junior equities, with these negative factors:

- There is usually a seasonal weakness in gold with no “love trade” from Valentine’s Day until an Indian festival in early May.
- The old adage of “sell in May and go away” is still in play.
- The summer doldrums of July and August, when most Northern Hemisphere market players go on extended vacations, looms large.
- Liquidity remains very low. The TSXV has averaged 71 million shares traded per day since the first of the year. This is less than half of the daily volume from September 2010 thru April 2011.
- Many companies need to fail and be delisted. However, the Venture Exchange continues to ease its financing rules thus allowing bad companies to survive. Rest assured this large contingent cannot prosper.

The three-month-long rally in the junior resource market is encouraging but, as shown by this week’s losses, tenuous at best. Only time will tell if it has staying power. According to the charts and fundamentals presented, we should have clarity on a trend in the market within six or seven months. That timeline is October to November; one to two months after investors come back to the marketplace post-Labor Day. In the meantime, I expect the market to be somewhat directionless.

The mantra at this year’s PDAC was “cautiously optimistic” that we are in for a better market going forward.

Paul the optimist said, “It’s getting better all the time” while John the pessimist replied, “It can’t get no worse.”

As an optimist, I’ll take Paul’s side. But in tribute to John, my favorite Beatle, it can’t get no worse than 2013.

Ciao for now,

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Acknowledgement: I kindly thank a fellow *economic* geologist, who chooses to remain anonymous, for alerting me to the chart similarities discussed above.

The **Mercenary Geologist Michael S. "Mickey" Fulp** is a Certified Professional Geologist with a B.Sc. Earth Sciences with honor from the University of Tulsa, and M.Sc. Geology from the University of New Mexico. Mickey has 35 years experience as an exploration geologist and analyst searching for economic deposits of base and precious metals, industrial minerals, uranium, coal, oil and gas, and water in North and South America, Europe, and Asia.

Mickey worked for junior explorers, major mining companies, private companies, and investors as a consulting economic geologist for over 20 years, specializing in geological mapping, property evaluation, and business development. In addition to Mickey's professional credentials and experience, he is high-altitude proficient, and is bilingual in English and Spanish. From 2003 to 2006, he made four outcrop ore discoveries in Peru, Nevada, Chile, and British Columbia.

Mickey is well-known and highly respected throughout the mining and exploration community due to his ongoing work as an analyst, writer, and speaker.

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