
# From The Maven Letter: Jan 22, 2020

I get asked a lot of questions during conferences. The topics range all over the map, but not surprisingly one question comes up more than all the rest:

> *"What's your top pick stock right now?"*

I have three responses, depending on the person asking. To figure out which answer to give, I ask:

> *"Do you want a high-risk exploration bet? Do you want medium-risk exposure to gold? Or do you want a low-risk opportunity?"*

Here are my picks in each category.

## Low Risk: Morien Resources (TSXV: MOX)

Morien Resources has been in the Maven Metals portfolio for some time. I've always liked its approach: own a significant royalty on a long-life coal mine being built by a company that likes to go big and pay out the majority of royalty income to shareholders as dividends.

The stock has climbed into Top Pick position today because key catalysts are around the corner.

Morien's royalty is on the Donkin mine in Nova Scotia, owned by Kameron Colleries. Kameron is part of the Cline Group, which until this year was headed by Chris Cline. Cline made a fortune by foreseeing the need for coal and building big mines in Illinois.

In July Cline was killed in a helicopter crash that took the lives of six others. The shocking and tragic event also put a pall over MOX stock because, without Chris at the helm, there was suddenly less certainty that Kameron would expand Donkin.

The expansion matters because of the structure of Morien's royalty. MOX gets 2% of net smelter returns on the first 2M tonnes of production each year and 4% of net smelter returns on any tonnes above 2M tonnes per annum.

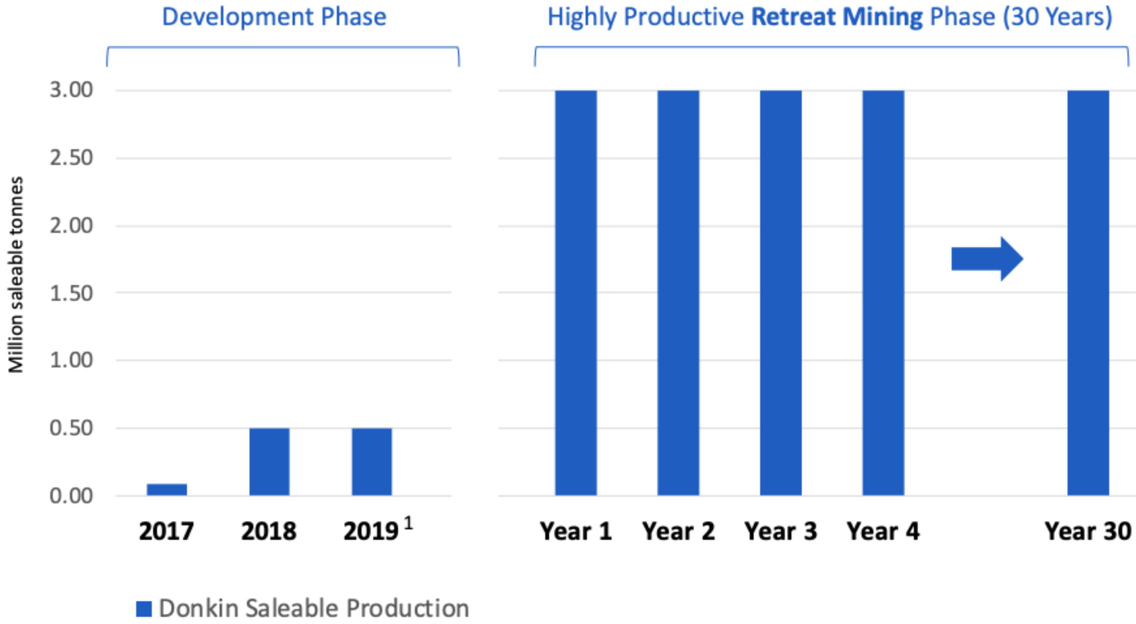
The current mine plan has Donkin churning out 3 million tonnes per year. Morien's royalty performs nicely at that level: using conservative coal price assumptions, Donkin pays Morien about $6 million annually if it produces 3 million tonnes of coal a year.

If Donkin expands to 6 million tonnes a year, the royalty pays out more like $20 million a year, again using conservative coal prices.

Of course, if coal prices do better than baseline, Morien's royalty income grows.

We've known all of this for some time. Why is MOX suddenly a top pick?

1. **The mine will start really producing this year**. Donkin started operating in 2017 but coal mines spend their first 2-3 years driving headings to prepare for full operations. Think of two parallel tunnels, 3.6 km apart. When they reach the edge of the resource the tunnels will turn 90 degrees and head towards each other, creating a rectangle of coal. Once that's done, it's time for retreat mining. Here's how production changes going from development mining to retreat mining:




**The key point is: expansion or not, Donkin output will ramp up dramatically in the next 12 months.** That means Morien's royalty income will ramp up.

2. **Long wall?** Under the current mine plan, retreat mining will happen with continuous mining machines that leave behind pillars. That mining method is expected to generate the 3 million tonnes of coal per year. The other option is to retreat using long wall mining. The Cline Group has used long wall at many operations; Nova Scotia is familiar with long wall. Odds are good that Kameron will decide to long wall instead. Long wall operations are more efficient and so produce more coal per year. A longwall at Donkin would produce at least 6 million tonnes a year. The amount Morien rakes in from a 6-million-tpa Donkin mine is almost silly - $20 million a year at least, for a company with a current market cap of $28 million – which is why I wouldn't expect Morien to last long following a long wall announcement.

3. **There are two possible outcomes for Morien and both work very well.**
    - Donkin sticks to a 3-million-tpa mine plan and Morien collects $6 to $9 million a year in royalties, depending on the coal price. Morien is committed to returning most (80%) of its royalty income to shareholders, which would translate to roughly $0.07 per year in dividends. That represents a dividend yield of 13% against the current share price of $0.53.

- Morien gets bought. Kameron is certainly a contender, as they would like to erase the royalty, but they wouldn't be the only interested party. There are many royalty companies out there who would love to have that Donkin cash flow. Whoever makes a move will have to offer a premium, of course.

I know: a coal royalty is the last thing you'd think I would be all excited about right now. But the progression to retreat mining is happening in a few months and will re-rate the stock. Kameron will decide before that happens whether to long wall; if they do, the news will re-rate the stock.

And Morien are incredibly good stewards of shareholder capital. They have been buying back stock like mad, which has reduced the share count by 13% since 2015. Fewer shares means higher dividends. Management has been buying, boosting its stake from 5% to almost 16% since 2013. Fewer shares available to trade should amplify gains upon good news.

And the current dividend, while small, still means a dividend yield of 2.3%, which if you can believe it is higher than all gold royalty companies.

**Major production growth, potential for a key expansion decision, a tight structure that keeps getting tighter, a good dividend yield now set to grow significantly in the near term, and two good potential outcomes** – when a friend asked, jokingly, "Hey Gwen, where should I put all of my life savings?" My answer was Morien.

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