

Brian Ostroff: Looking for Value in PMs and Finding Adventure

Source: George Mack of *The Gold Report* 04/15/2011



Finding companies with growth potential is just the start for Windermere Capital, according to Managing Director Brian Ostroff. An active philosophy and deep technical expertise allow the firm to invest "anywhere along the spectrum" from exploration to production, all the way to operation. In this exclusive interview with *The Gold Report*, Brian delves into the gold-silver value proposition and names a couple of promising players in the Abitibi.

The Gold Report: Brian, let's start with you telling us about Windermere Capital.

Brian Ostroff: Windermere is an investment manager. We currently oversee two hedge funds with a natural resource focus. [The Breakaway Strategic Resource Fund](#) and the [Navigator Fund](#) are both offshore hedge funds based in the Cayman Islands. They serve high net-worth individuals, family offices and institutional investors.

TGR: Do they have an open-ended structure or are investors committed to a cut-off investment?

BO: Both are open-ended. Navigator is a monthly. Breakaway is a quarterly.

TGR: So they're corporations. Do they trade on an exchange?

BO: Yes, both funds trade on the Irish Stock Exchange, and they are quoted there. Subscriptions are done directly with the fund.

TGR: What is Windermere Capital's investment philosophy?

BO: In terms of the basic investment theory behind both of our funds, we feel that we are quite different than most of the other funds in our space. For starters, we have strong technical expertise. Most of the people here have technical backgrounds as opposed to a financial or capital markets background.

We have two partners in our fund. One is a group called Ocean Partners, which is made up of the former ores and concentrate trading team at Pechiney. When Alcan bought Pechiney, these guys did a management buyout. They do business in roughly 35 countries and have a physical presence in 15. They are geologists, mining engineers and metallurgists, and their global

footprint allows us to send someone to an opportunity quickly. Our other partner is Peter Hawley and his group. These guys have all been in the business for +30 years building and operating mines. Once again, this is an area where we think we have an advantage. We can look at various assets, not only as financial guys, but also with a deep understanding of the geology and the likelihood of it going into production.

The other area where we think differently from other funds is that a lot of funds do their due diligence and write their checks, make their investment. We find that our work really begins after we've written the check. We're not activist investors, but we're definitely active. We tend to take fair-sized stakes in companies, and then we try to help it going forward by making additions to its board, perhaps helping it operationally, assessing its assets and either helping the company divest or find other assets.

TGR: Active versus activist implies that you do everything but management—seed, assistance, banking, financing.

BO: We certainly assist in all those roles. We do not take board seats. What we do is find people in the industry with whom we have a relationship, people we think can help advance the company. With regards to our investment theory, we are extremely value oriented. Primarily, we invest in the micro- through mid-cap stages; but our alpha really comes from the micro-cap stuff. We tend to look at a company, assemble a peer group and try to understand why the company we're looking at is considerably cheaper than its peer group. Once we understand that, we gather around the table with our partners to have an honest discussion as to what the issue may be and what we can do to fix it. Once we get to the point that we think we can help close that gap with the target's peer group, we have a discussion with management to see that we're all on the same page.

Once again, we are active—not activist. We have a meeting of the minds and when everyone is comfortable with the business plan, we tend to make our investment. Of course, that's only in situations where we have large stakes. We use the mid-cap companies to move our positions around and get exposure to various metal groups. In the micro-cap space, we tend to take a position anywhere between 10% and 19.9%.

TGR: Micro cap is what, US\$10–\$75 million?

BO: Yes, actually, US\$10–US\$100M. If we've done a good job with that micro cap, hopefully, it really starts to grow from there.

TGR: The idea is to get it over US\$100 million in market cap, so mutual funds can buy it?

BO: Yes.

TGR: Would you tell us about the differences between your two funds?

BO: The Breakaway Strategic Resource Fund is mining only. Due to the technical expertise to

which I had alluded, it can make investments anywhere along the spectrum. The fund was first conceived in the dark days, just coming out of the global crisis. We felt there were a lot of good assets that were orphaned or had been lost and financial players had taken them over. We were looking to buy distressed assets, even outright buying the properties or mines. We do structured debt through our partners and offtake deals all the way through outright investment in the company's equity. I like to describe Breakaway as a complete "rocks to stocks" Investment vehicle.

TGR: And what about Navigator?

BO: Navigator is all natural resources. Aside from mining, it also does energy and agriculture, paper and forest, etc. Its investments are primarily in publicly traded equities; however, we do have some room for near-public investments (i.e., those that we think can go public within about six months).

TGR: Does Breakaway Strategic also buy equity in private companies?

BO: Yes, Breakaway looks anywhere along the spectrum, and it'll outright buy a mine if the opportunity presents itself.

TGR: So, does Breakaway Strategic own precious metals?

BO: Yes. Both funds have a fair-sized stake in some precious metals companies.

TGR: Where do you stand on precious metals? Are you bullish on gold, silver, platinum, palladium, whatever?

BO: Yes. I believe that we continue to be in a secular uptrend that will lead us significantly higher, but there will always be bumps along the way.

TGR: Why are you bullish on precious metals?

BO: I've always believed that gold is a currency. Ultimately, investors have a choice—put their money in dollars, yen, euros or pounds, as they choose or in gold. The one difference is that gold, unlike paper currencies, has to be found and mined. Last year, gold production was up about 3%. That compares with all the central banks around the world that are just printing money.

Now, I don't put myself in the camp of being an absolute doomsayer, in terms of the fiat currencies or the U.S. dollar. What it really comes down to is—if the Americans print 20% more dollars, the Europeans print 20% more euros and the British print 20% more pounds, you can't all of a sudden come up with 20% more gold. The relative valuation continues to favor gold.

TGR: What about silver?

BO: We love silver. It has definitely come into the forefront and has been a much better performer. Like many people who like silver, the physical market characteristics are very positive. Ultimately, we view silver as gold on steroids. When you're in these uptrends and everyone's looking at precious metals, silver tends to perform much better. We think that, as the whole precious metals bull market proliferates and more average investors start to look at it, silver at US\$35–\$40/oz. might be more appealing than gold at US\$1,400–\$1,500/oz.

As bullish as we are on precious metals, we're even more bullish on precious metal stocks. We believe they are very cheap. If one was to go back 20 or 30 years on the XAU (the Philadelphia Gold and Silver Index) and do a relative valuation to the price of gold, one would see that it is still trading under the band at which it typically trades; so, we think there's value there. Additionally, if one was to take a look at the TSX Venture Index as a benchmark (obviously, not all the stocks on the TSX Venture are just mining but it has a high percentage of them), that index is still considerably lower than where it was in May 2007.

TGR: Let's stay with the XAU. You say it is trading at a discount to its traditional band. Could you tell me, to what is it trading at a discount?

BO: To physical gold. In other words, if you were to look at the valuations of gold stocks to physical gold, you would see that, historically, gold stocks are still trading well under their norm given where gold prices are. Of course, that can correct in one of two ways: Either the gold stocks relative to gold can appreciate or gold relative to the gold stocks can depreciate. Because we are still in a secular uptrend in precious metals, our feeling is that the stocks, ultimately, will catch up to the metal, as opposed to the metal catching up to the stocks.

TGR: So, you believe that the risk is greater to the upside than it is to the old s?

BO: Correct.

TGR: You mentioned that there was more value in silver due to the psychological perception of silver's price per ounce versus that of gold. Does that imply greater volatility?

BO: It does; and in terms of value, I'm quick to say that value is a relative thing. So, is there value in silver? I'm not sure. Our feeling is that silver offers a better opportunity relative to gold—but make no mistake about it, silver is a lot more volatile. If we get a downturn in precious metals, silver will fall harder than gold.

TGR: Sticking to that value theme, could you say more about silver stocks offering value relative to the actual metal?

BO: There are very few producing silver names, and this is particularly valid for people who are looking for leverage in silver and don't want to go into the bigger names, like [Pan American Silver Corp. \(TSX:PAA; NASDAQ:PAAS\)](#) or [Silver Wheaton Corp. \(TSX:SLW; NYSE:SLW\)](#). If their interest is in something a little more speculative, there aren't many names that are already in production in the 2–5 million-ounce (Moz.) range. As more and more money comes into the

sector with fewer names to invest in, those stocks should continue to get a disproportionate lift.

TGR: In effect, fewer opportunities mean greater demand?

BO: Exactly.

TGR: To recap, you see gold and silver as a store of value. If you can't print more gold, you have to find it. And if you do, it just adds value to the entire gold supply. If I'm not putting words in your mouth, isn't this a currency devaluation play?

BO: Yes, that is the basis of our theme for investing in precious metals.

TGR: So, where do you find value?

BO: We think there are opportunities in niche stories—a company out there that the market hasn't paid much attention to or, perhaps, a commodity that hasn't received much attention. Those opportunities still exist and will always exist; they just get that much more difficult to find as a market matures.

TGR: Can you give me some specific places that an investor might look?

BO: [Adventure Gold Inc. \(TSX:V:AGE\)](#) is one of our large portfolio holdings. It's a company led by a wonderful management team; Marco Gagnon is the CEO. His whole team comes from larger firms. In its three-year existence, the company has assembled a large portfolio of properties in the Abitibi. Its general philosophy is that the best place to find gold is right beside other gold mines that either are operating or will be in production soon. Adventure has accumulated close to 20 properties, which is quite a handful for a small company. But, it's done a very good job of prioritizing.

It has what we would consider four flagship properties. The first one is the Meunier 144 property, which is in West Timmins. When [Lake Shore Gold Corp. \(TSX:LSG\)](#) bought over in West Timmins, it encircled Adventure's property. As a result, Adventure made a deal that allowed Lake Shore Gold and [RT Minerals Corp. \(CNSX:RTM\)](#) to earn a stake in Adventure's property by spending US\$3 million in drilling. Adventure's property is right beside Lake Shore's Timmins and Thunder Creek zones, which are going into production. The theory is that the down-dip extension of those two deposits enters into Adventure Gold's property, and it is currently being drilled to test that theory.

Adventure also joint ventured (JV'd) its Dubuisson property, which is right beside [Agnico-Eagle Mines Ltd. \(TSX:AEM; NYSE:AEM\)](#) Goldex Mine. A couple months ago Agnico, picked up 51% of Dubuisson through payments and drilling commitments. Agnico will continue to drill the property out, starting within the next month or so. What interests us about Adventure is that it's almost a hybrid model. The company will option off some of its properties and keep others to work on itself.

Adventure recently put out drill results from its third flagship property, Pascalis-Colombière. This is the area surrounding and including the old L.C. Béliveau Mine, owned by Cambior. Cambior had mined it up until the early 1990s and, over a four-year period, it produced close to 170,000 ounces (Koz.) of gold. With gold prices coming down back then, Cambior closed the mine. Subsequently, [IAMGOLD Corporation \(TSX:IMG; NYSE:IAG\)](#) bought Cambior and viewed Pascalis as a non-core asset. Adventure picked up the property and has come out with very encouraging drill results. It's important to note that production at that historic mine had been done only down to the 300-meter level, which, in Val-d'Or, is not very deep. But the company believes there's still a lot of gold to be found beneath the existing and to the west of the mine.

The fourth flagship property that Adventure is working is the Granada Extension, which is next to [Gold Bullion Development Corp. \(TSX.V:GBB\)](#) Granada Property. Adventure picked this property up toward the end of 2010 and has received some encouraging sampling results. The belief is that the Granada Extension is similar to [Osisko Mining Corp. \(TSX:OSK\)](#) Malartic property. You're looking at a large tonnage, low-grade type deposit. Gold Bullion has drilled aggressively and put out a non-compliant NI 43-101 block model, showing 2.5 Moz. in a relatively small area.

Adventure's other properties also are in historic areas: Detour East, which is east of [Detour Gold Corp. \(TSX:DGC\)](#) property and Casa-Berardi, near the operating [Aurizon Mines Ltd. \(TSX:ARZ; NYSE.A:AZK\)](#) space.

These properties, coupled with the fact that the company has close to US\$4M in cash and cash equivalents sets Adventure up very well. It has a lot of opportunities. With four properties now being worked, we think Adventure will generate a lot of news flow. We're quite optimistic that, with a US\$35M market cap, the market has not really given this company the attention it is due.

TGR: Could Lake Shore and Agnico, the two JVs Adventure is working with, act as something of a poison pill in hindering a takeout of Adventure?

BO: Our feeling would be that, if there were any interest in the company, it would probably be property by property. It is unlikely that one company would come in and take all those assets. Case in point, if drilling proves out the down-dip extension from Lake Shore's property, Lake Shore might be interested in the Meunier property. If Agnico's drilling proves out that there is more gold beside its Goldex mine, we would see Agnico having an interest in that property. Adventure's assets are spread out within the Abitibi region, so we would see logical buyers on a property-by-property basis as opposed to an outright acquisition of the company itself. Particularly on its four flagship properties, we feel that any one of those could be a company-maker.

TGR: That is a great story, Brian. Do you have another one?

BO: Our funds are fair-sized holders of a company called [Cartier Resources Inc. \(TSX.V:ECR\)](#), which is a gold resource exploration company in the Abitibi. It is earlier stage than Adventure, in that its properties are more grassroots. There is

some historic drilling, but we think the opportunity is more a combination of being in the right location and having an excellent management team that can move these properties along. Cartier owns a significant land position along the Cadillac Fault, an area that has seen significant interest by companies like Osisko and Aurizon. It also has assembled other very interesting properties within that area and has embarked on an aggressive drill campaign that we think should start to prove out some potential.

TGR: Brian, thank you for your time.

Brian Ostroff joined [Windermere Capital, Inc.](#) in 2009 and is a managing director. His area of focus is the junior and mid-tier mining sector. His previous experience includes a stint as a proprietary trader at a major Canadian bank and four years trading on his own. He also worked at the M&A advisory firm Goodrich Capital, where he was the Canadian managing partner overseeing mandates across a spectrum of industries with a focus on display technologies and mining. He worked at RBC Dominion Securities, where his focus was on smaller-cap special situations and alternative investments. Brian is a graduate of the University of Toronto. He can be reached at atbostroff@windermerecapital.com, 514-908-4202.

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- 2) The following companies mentioned in the interview are sponsors of *The Gold Report*: Detour and Aurizon.
- 3) Brian Ostroff: I personally and/or my family own shares of the following companies mentioned in this interview: RT Minerals, Adventure Gold, Cartier Resources and Silver Wheaton. I personally and/or my family am paid by the following companies mentioned in this interview: None.
- 4) Windermere Capital (through its various entities) owns RT Minerals, Lake Shore Gold, Adventure Gold and Cartier Resources. </br