Mining Journal

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‘New’ ventures rarely successful

The company formerly known as Mustang Resources threw in the towel during 2018, jettisoning multiple promises to investors in a credibility sapping and industry damaging strategic about-face.

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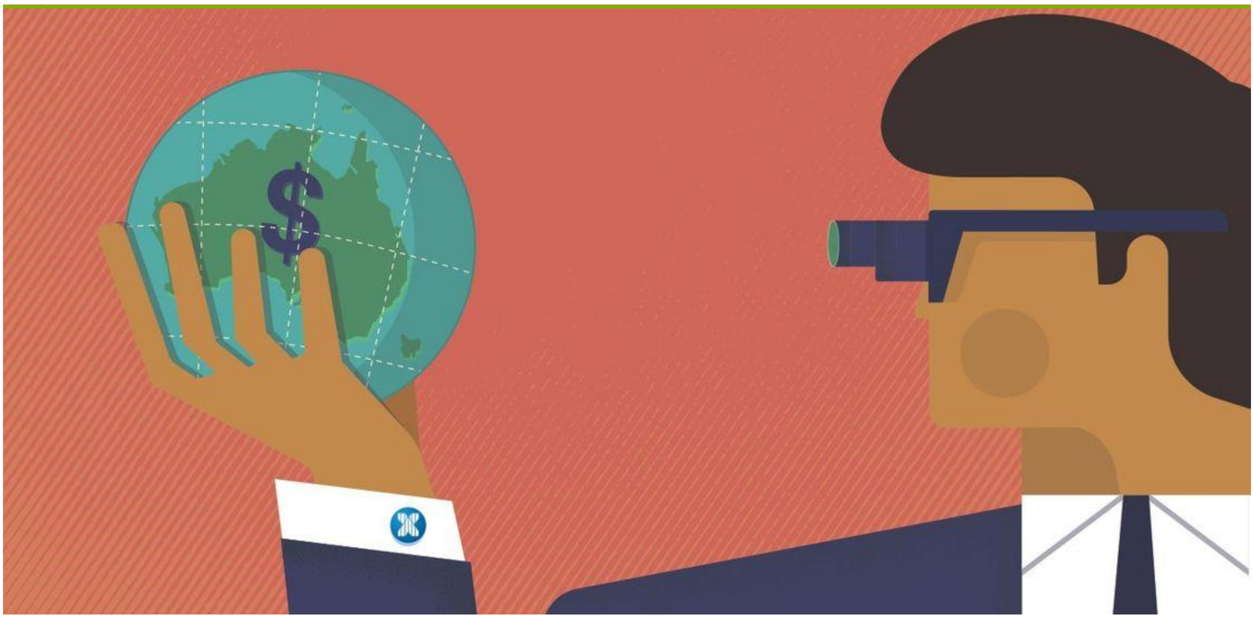

20 December 2018

During 2017, I wrote two ‘From the Capital' columns about ASX-listed Mustang Resources. The first, published on April 5, 2017, described how a company with a previously peripatetic and undistinguished corporate history since listing in 2002 was setting out to break the industry's capital management mould.

At the time, the focus of Mustang's attention was the Montepuez ruby field in Mozambique, adjacent to the operations of then AIM-listed Gemfields. The unusual commodity exposure drew considerable investor interest, as I described in a second column on November 16, 2017.

In a potentially radical break from conventional capital market practices, then chief executive Christiaan Jordaan had said publicly that the company would return the entirety of its operational cash flows from the ruby project to investors. Jordaan held out hope that a company with a market capitalisation of A$50 million (US$35 million) could be generating A$40-70 million of distributable cash within two or three years.

Jordaan's innovative capital management proposal extended to the company's Caula graphite deposit, also in Mozambique and along strike from Syrah's giant Balama project. He said he would bring in external funding after demonstrating a viable resource at Caula and possibly divest the asset to prevent any ambiguity about the company's focus.

Mustang's approach would have been a repudiation of an industry compulsively hooked on using cash flows from one project to fund subsequent exploration or mining efforts and, in the process, permanently lowering returns from investing in the sector.

I was cheered by the company's expressed belief in a new returns model. At the same time, I had to acknowledge "the instinctive reaction of anyone with even a brief history of contact with the industry will be scepticism, perhaps even outright disbelief, about the willingness of Mustang Resources to break with the conventional treatment of investors".

> **"The company has become a billboard advertisement for why investors should give short shrift to anyone saying 'we are different'"**

During 2017, the company reported a steady build up in saleable gemstone inventory, holding out the prospect of a windfall from a planned October sale. Expectations, which drove a fourfold share price rise, were dashed when Mustang realised a paltry A$713,456 from the 405,000 carats offered to industry buyers. Within two weeks, Gemfields reported receiving US$55 million for 605,229ct.

A new chief executive was appointed as the company more or less admitted that its grasp of the ruby market had been inadequate and it commenced a rethink, after having already abandoned an earlier sales strategy, about how to proceed next. A third strategy in three years left it with a dilapidated investment proposition and an 80% lower share price within a month.

I speculated, in my second of the two 2017 columns, that graphite might prove a handy distraction from the company's woes. True to form, the company has dropped its flagship ruby project in favour of graphite as it also hopped aboard the vanadium bandwagon in an even more meandering quest for strategic direction.

An evocative name change to New Energy Minerals added smoke to the growing assemblage of mirrors as the company checked a standard list of industry practices, including a share consolidation and a purge of historical company announcements from its website, to help obliterate an awkward history.

The company agreed in July 2018 to divest its ruby interests to Fura Gems, a Canadian company with ruby mining properties in the same region, for A$10 million due in scrip over two years and with limits on disposal for up to four years. New Energy Minerals committed to an eventual in-specie distribution of the acquired Fura shares in a sop to shareholders wanting to retain a ruby market exposure.

The seemingly impressive price tag heroically assumed a tripling in the share price of the buyer to derive the inflated valuation. In late November 2018, the company backtracked on the payment and distribution plan after welcoming the chance to swap the promised Fura shares for A$2.8 million in cash immediately amid an increasingly uncomfortable financial position.

In January 2018, Mustang had boasted a A$19.95 million funding package from "a major US institutional investor". This was expensive money with the potential to materially dilute existing shareholders. This, too, seems to have turned pear shaped as the parties are now at loggerheads in the Supreme Court of Western Australia with the funding party claiming New Energy Minerals tried to short change it by A$2.5 million in attempting to exit their deal.

Meanwhile, the company had located a so-called strategic investor in Hong Kong to back its Caula graphite development. At the end of November, the investor put A$1.5 million into the company in exchange for a 16% stake and has contributed A$3.5 million for a 50% interest in the entity holding 80% of Caula.

Over the journey, shareholders have lost even the slightest residual exposure to the gem market to which they had been attracted. Any novel capital management initiatives have been discarded. The Caula interest has been prematurely diluted. The battery metal exposure is a mere copy of what is available through numerous others, many with more credibility, on the same bandwagon. The company faces more in legal liabilities than it ever reaped from the ruby market.

The benefit of any doubt has shifted conclusively. The company has become a billboard advertisement for why investors should give short shrift to anyone in the industry saying "we are different".

Mine development is a uniquely tough business. Accessing mineralisation is hard enough. Then, hitting every development milestone, in the right order, at the right time comes with a low probability no matter how skilled or highly motivated those in charge might be.

Throwing in the towel in misguided pursuit of an easier way displays a sure sign of having failed to comprehend the nature of the task and blights the value of everyone's future endeavours.

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