

Mexican Silver Miners – a Piranha Pond in the Making

With the pace of takeovers hotting up in the stricken mining industry even the most cashed-up companies are coming under scrutiny as potential targets. While there are thousands of miners out there only a few hundred are likely targets as the rest do not have worthwhile projects, attractive metals or jurisdictions or enough cash on hand to overcome the aforementioned shortcomings. If we are looking at projects as the key asset of the prey then the project generally has to be hyper-economic and also very advanced. Applying all these criteria narrows down the field substantially. Being a producer is a trump card that makes any miner worth considering.

However, to review all the potential victims is a herculean task so in this commentary I shall look mainly at Mexican plays in the silver business and review what combinations could be imagined.



First Majestic/Silvercrest

The first shot in the battle for consolidation was fired by First Majestic and hapless Silvercrest shareholders have come out worse for the wear. FM extracted an outrageous \$8mn termination fee out of Silvercrest when usually break-up fees are related to the cost of the acquirer in the event the transaction falls through. There is no way that First Majestic will be \$8mn out of pocket in legal fees for a plain vanilla takeover...

Therefore, Silvercrest has locked itself in a room with First Majestic and then swallowed the key. This is an effective way to scare off other predators but considering that FM is

getting the better of the deal in any case, management at Silvercrest have not done their own shareholders any favours by refusing to countenance other bidders. All in all, it is an odious deal. However just because Silvercrest does not know how to do a fair deal, does not mean that other management's in the space are as hapless.

Conjuring with Some Names

The fall of Silvercrest to the predatory blandishments of First Majestic leaves Great Panther and Fortuna Silver as the main "unattached" silver plays in Mexico. As we have made clear elsewhere we would have viewed a Silvercrest/GPR tie-up as infinitely preferable to what has played out. Interestingly both of the remaining prospective targets are both Mexico/Peru plays now. A tie-up between Fortuna and GPR is an interesting concept to conjure with. One might also muse upon the possibilities of Hochschild (HOC.L) combining with one or both of these entities. Farther out in left-field is Sierra Metals (the former Dia Bras), the ARC Capital entity, which is also ensconced in Mexico and Peru and very well-cashed up. However, it is also too much inclined to thinking it can seize control without a takeover premium being offered and various of its plays (e.g. Largo Resources) show it may not be mistaken.

Great Panther Silver – Tasty & Vulnerable

One of our "best in class" picks in the silver space is Great Panther Silver, which has recently diversified into Peru by buying Nyrstar's Coricancha silver/lead/zinc mine there. With a tidy \$18mn in cash in the bank and several producing silver mines in Mexico (one with meaningful base metals) the company strikes us as a target in waiting. The only pity is that it did not move on Silvercrest (or vice versa) before First Majestic started snooping about.

With production hitting records in recent quarters and cash costs declining steeply the company has all the look of an

accretive target for a predator.

The current valuation of GPR surprisingly does not contain one iota of takeover premium and this is frankly ridiculous because the Silvercrest deal shows that bottom-fishers are trawling the waters looking for lone surfers to pull under if the valuation is low and the prospects sound. GPR fits both those criteria.

Hochschild – Aristocrats of Peruvian Mining

This company is a strange animal. While London-listed it is actually a Peruvian company owned by a very long-established Peruvian family, famous in base metals circles. The company has mines in Peru, Argentina and Mexico. It seems that there is a quite a Peru-Mexico axis apparent in a number of these players. This might have to do with both countries having such a strong history of mining amongst local entrepreneurs.

With a market cap of GBP £312mn at the current time it is a company with the heft to be a predator rather than mere prey. Therefore Great Panther could be a tasty morsel for it to munch on and digest easily. It would provide a significant beefing up of its Mexican position and its Peruvian expertise could be put to work on moving Coricancha forward.

Another target could be Fortuna Silver. Ironically this company's best asset in Peru was a 'throw-away' of Hochschild's that became a company-maker for Fortuna.

Fortuna Silver – Needing More Projects

This TSX-listed company is also Peruvian owned and managed. It started out with some starter mines in Peru and then added an off-the-beaten-track mine in Oaxaca in the south of Mexico, where Canadian miners scarcely ever ventured. However with a market cap of over CAD\$540mn, it would virtually be a merger of equals if it combined with Hochschild and then one wonders whether two powerful Peruvian families could get on together

or would it be a case of “this town is not big enough for the both of us”?

Acquiring Great Panther would be a good move for Fortuna as it would diversify the company further as it currently only has two mines. The current market cap of Fortuna though makes it an unlikely takeover candidate unless it came into the sights of a group like Pan American Silver. However that company has been licking its wounds for a long time after a series of ill-fated purchases.

Sierra Metals – Stealthy Mover

This company has shown little inclination to doing its deals in public. Creeping acquisitions are its management group’s forte with unsuspecting shareholders never knowing they are about to get eaten until the fangs sink in. Once again this company is run by a scion of an old Peruvian mining family in the guise of a New York private equity fund manager by way of the investment banking world.

This company is most definitely not afraid of base metals as it has mines in both Peru and Mexico that are predominantly in lead, zinc and copper but all with precious components in the mix. The group was cobbled together out of Dia Bras (which had been a case of creeping takeover and then with a daring move on a company listed on the Lima stock exchange in 2011, the Yauricocha mine was brought on board. This in itself shows that ARC is not above making a bid when it really wants something.

With a market cap of over CAD\$350mn Sierra also could indulge in a merger of equals with Hochschild or Fortuna but again the issues of “Latin Families” comes into play. No such problem picking off Great Panther though.

Nieves – Out of Sight but Not Out of Mind

It’s worth mentioning one unlisted asset which is the Nieves

property that was owned until recently by Quaterra. This is now ensconced in a private US group called Blackberry. It has long been one of the most interesting assets we have encountered in Mexico, however under Quaterra's benign neglect it was going nowhere and missed the opportunity to be sold when silver hit \$50 back in 2011. When silver next gets going we suspect that this shall be on a number of companies' shopping lists.

Silver Bull – a Play for Base Metal Hunters

Passing mention might be made of this unfortunately named small cap company which we met and liked when it was called Metalline. It owns the Sierra Mojada property in Mexico. New management (when we last met them) didn't leave us super-impressed. However, it might be worth any of the names conjured with here taking it over (particularly Sierra though) and most likely this will happen when the Zinc/Lead shortage starts to really bite and it is reflected in metal's prices.

Conclusion

All this talk of merger-mania makes us feel hungry. Nothing like a bit of blood in the water to attract the sharks or the piranha at least. The names to ponder are not as numerous as in the past but still there are some which are still so undervalued as to provide a bit of takeover premium, a scarce commodity these days.