

# Growth Stocks Weekly

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**Performance:** 1996 116.9%; 1997 28.1%; 1998 36.4%; 1999 39.4%; 2000 180.9%; 2001 -50.5%; 2002 18.7%; 2003 28.8%; 2004 166.7%; 2005 28.2%; 2006 153.3%; 2007 8.8%; 2008 -25.2%

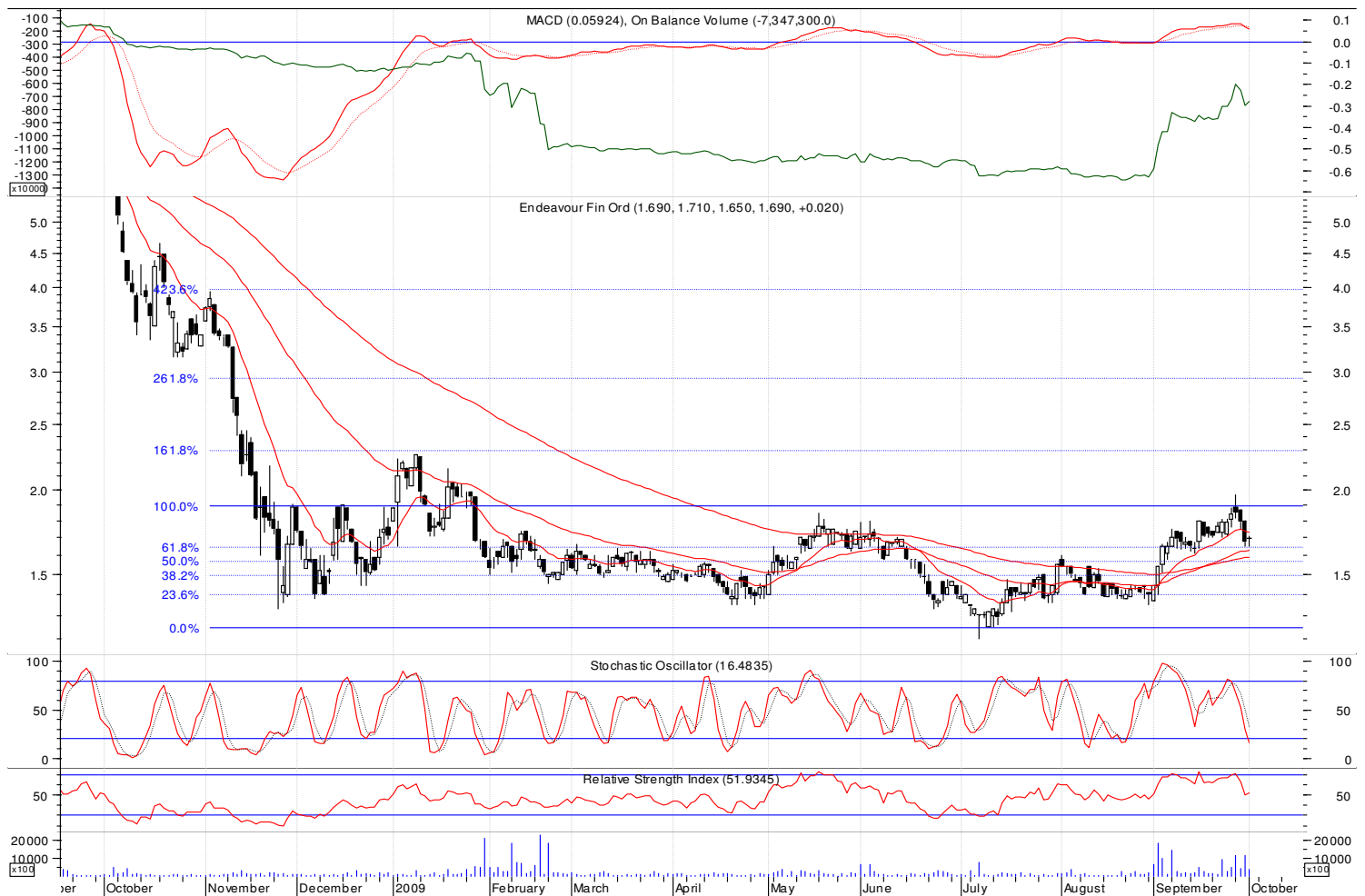
## Junior Gold and Natural Resource Sector Report

October 2, 2009

### The Smart Money – Signs of Life

#### UPDATE

#### Endeavour Financial Corporation (EDV-TSX)



Daily chart: High C\$11.24, Low \$1.20, Last Trade \$1.69

#### **A Value Proposition**

Endeavour is an independent merchant banking company focused on the global natural resources sector. The Corporation offers advisory services in project, corporate and debt capital markets; equity financings; mergers

and acquisitions; and strategic business development. Endeavour also provides equity and bridge loans in support of clients, transactions, and other market opportunities. Accessing its global industry networks, Endeavour creates and launches new growth companies as both an advisor and investor and has an enviable track record. The current market downturn has created a unique opportunity from several perspectives.

Endeavour recently reported its quarterly financial results as at June 30, 2009, revealing a net asset value (NAV) of \$2.78/share. Cash and investments marked-to-market represented \$2.16/share of that, with the balance being the book value of their merchant banking business. We suspect that the NAV has risen since then with the general resource market, but given Endeavour's share closing price of \$1.69 today, Endeavour is trading at a 39% discount to its reported NAV. To bring Endeavour's stock in line with that NAV it would have to gain 64%. That spread alone offers a compelling opportunity, but the story gets much better than that.

Last week we highlighted Endeavour's proposal to take control of junior gold producer Etruscan Resources (EET-TSX) through a US\$43 million financing at a price of \$0.30 per share. Through this financing, and by acquiring another ~20% of Etruscan's fully diluted shares outstanding in a private transaction, Endeavour will own 54% of the outstanding shares, effectively paying \$107 for each of Etruscan's proven & probable gold ounces, and \$53 for the measured & indicated resources – a steal.

The financing will be used to restructure Etruscan and position it to benefit from a strong gold price going forward. The proceeds will pay down 50% of Etruscan's US\$700/ounce gold call options (US\$23 million), pay down US\$8.5 million of unsecured debt, fund working capital for the Youga mine and fund general corporate working capital.

One Bay Street analyst noted that even though this is largely dilutional for Etruscan with only a \$62.1 million market cap, this is a positive development that responds directly to criticism that had left Etruscan orphaned. Its hedge book, its poor balance sheet, its failure to deliver at Youga (Burkina Faso) and management's failure to focus on one core group of assets to drive value will all be addressed through this deal.

Endeavour is very bullish on gold. So by reducing the hedge book, Endeavour's investment in Etruscan achieves significantly greater exposure to a rising gold price. After the restructuring, around 80% of the life of mine production from the Youga mine is leveraged to spot gold. The restructuring also significantly reduces the obligations associated with financial derivatives (those gold hedges), reduces the outstanding convertible debentures by US\$8.5 million and boosts working capital by US\$11 million, so the balance sheet is vastly improved. As part of the restructuring, US\$5 million of long-term debt from two lenders will convert into equity participation, also at a price of \$0.30 per share.

The deal brings Endeavour management onto the Board with four nominees proposed: Frank Giustra, Gordon Keep, David Street and Neil Woodyer. Given Endeavour's control position, they will likely initiate some divestiture of Etruscan assets to further improve the balance sheet and better position the company for growth. New management will need to demonstrate that Youga can perform to expectations, and Etruscan's balance sheet may still be less than pristine after the financing, but this transaction puts the company in a much better position going forward, with an experienced Board of Directors.

We previously pointed out that the market expected Endeavour to complete a large \$400 million financing with Middle Eastern money, but as it stands we hear the potential sources are not yet ready to commit. Endeavour management indicates that Etruscan is only the first of several investment opportunities they have identified, and co-investment partners may yet be invited in on a deal-by-deal basis.

In this environment cash is king. Right now \$115 million will buy a huge amount of production or proven ounces in the ground. Many acquisition targets – especially in the junior sector – are trading at pennies on the dollar and need cash – and other than the major mining companies who typically move at glacial speed anyway, nobody else has the money, reputation or on-the-ground expertise necessary to quickly gain traction and make deals.

### **Quick Review**

We went into last year's meltdown holding a modest portfolio position of 10,000 Endeavour shares, with an average cost of \$2.40 per share. We had taken periodic profits over the years since our first purchases back in 2004, and Endeavour treated us well, proving to be an excellent proxy through which to position into the junior resource sector on a diversified and discounted basis.

In February 2009 Endeavour completed a public offering of 65 million units at a price of \$1.77 per unit, which included an over-allotment option, to raise gross proceeds of \$115,005,750.

Endeavour has the ability to position in deals early, and at prices mostly inaccessible to the public, so we took advantage of the post crash period with the addition of a further 25,000 shares at \$1.60 back on May 12, 2009. We now hold 35,000 shares at an average \$1.83 per share.

In June Endeavour entered into an exclusive agreement with Arrayan Capital Advisors LLC, whose principal is Eduardo Garcia. Arrayan is a boutique advisory firm providing investment banking advisory services for debt raising, asset acquisitions and capital restructurings to clients in Latin America. Endeavour recently raised \$400-million of debt financing to fund the oil and gas infrastructure in Colombia by Endeavour for Pacific Rubiales. Advisory fee income should continue to form a strong source of cash flow for Endeavour.

At June 30, 2009 the Corporation had cash and cash equivalents of \$121.8 million, investments of \$71.0 million and a working capital position of \$192.9 million.

### **Conclusion**

Neil Woodyer, Endeavour's CEO, has often spoken of the gold sector as being dysfunctional – that these junior companies in particular are not getting valued the way he thinks they could be – and so this is where he is focusing Endeavour's talents and capital.

Endeavour's overall strategy is to create value through opportunistic and strategic investments in gold producers with a plan to build an intermediate sized gold company, thereby attracting a higher valuation and returns for shareholders. We believe the Etruscan deal will prove to be the first of several such deals over the coming months, and that while Endeavour is looking globally at whatever opportunities exist in the gold sector, most of the value to be found in the sector is in the junior producers.

It would be difficult if not impossible for investors to consistently match Endeavour's ability to select winners and realize on their potential. Its shares are an excellent proxy for investment exposure to a secular bull market in commodities, which we believe is underway.

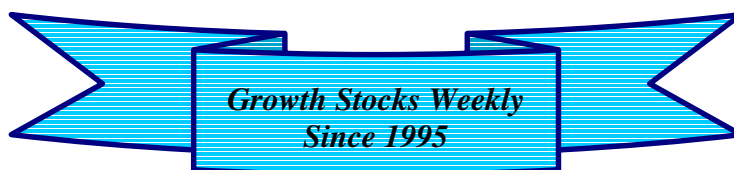
Given management's track record of timing, their creative deal structuring, and their ability to create value, investors would do well to pay close attention to this brain-trust's next moves in an effort to recover Endeavour's market capitalization and management's somewhat sullied reputation.

Endeavour has now shown its hand, kick-starting the process of value creation, and the share price testing technical support at \$1.60. Volume has picked up since early September, and a trend of higher lows and higher highs is now in place.

With delivery of this report we will add 15,000 shares at market to hold 50,000 shares.

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