



What the Osisko Acquisition Means for Investors in Yamana Gold

Description

It would appear one of the most hotly contested takeover battles in Canada's beleaguered gold mining industry has ended with **Goldcorp** (TSX: G)(NYSE: GG) electing [not to raise](#) its hostile offer for Osisko Mining ([TSX: OSK](#)). This leaves **Yamana Gold** ([TSX: YRI](#))([NYSE: AU](#)) and **Agnico Eagle Mines** ([TSX: AEM](#))([NYSE: AEM](#)) set to acquire Osisko for \$3.9 billion in cash and stock.

The deal values Osisko at \$8.15 per share or a premium of 18% over its current share price and will essentially see Yamana and Agnico each receive half of Osisko's assets. Osisko's current management team will take over a new company with \$155 million in cash and a 5% royalty on its flagship Malartic mine in Quebec.

What does this mean for investors and who is the key winner from the deal?

For the year-to-date Yamana has seen its share price plunge 13%, whereas Agnico's has remained flat and Osisko's has climbed 53%. The key driver of Osisko's share price hike is the speculation surrounding the takeover, whereas Yamana's share price continues to be battered with the company failing to perform. But the big winners out of this deal are Yamana and its shareholders.

Over the last three years, Yamana has been battling anemic sales growth with 2013 revenue plunging 21% compared to 2012 and 15% in comparison to 2011. Even more concerning is Yamana's 2013 operating cash flow – an important indicator of a gold miner's operational performance — has plunged over the same period, falling 44% compared to 2012 and 47% compared to 2011. This concerning trend is underpinned by an even more worrisome trend — Yamana's annual gold production continues to remain flat.

Gold production for 2012 only came in at 1.2 million ounces, while for 2013 the company missed its initial guidance by 25% reporting gold production had remained flat year-over-year at 1.2 million ounces. More worrisome is 2014 production — before the completion of the Osisko deal, it was estimated to be around 1.4 million ounces, a mere 17% increase compared to 2013.

Yamana is also a higher risk producer because it is solely dependent on gold production from mines located in riskier Latin American jurisdictions, particularly Argentina, which accounts for around 13% of

its total gold production. It was a series of challenges associated with some of those jurisdictions that saw it miss its 2013 gold production guidance and book a number of impairment charges across those assets for 2013.

This underscores the importance of the acquisition for Yamana, because it gives the company a low-cost, high quality mine asset located in the stable, mining-friendly jurisdiction of Quebec. The acquisition will boost Yamana's gold reserves by around 5 million ounces, with the Malartic mine reported to have total gold reserves of 10.1 million ounces.

If the price of gold continues to fall, potentially to as low as \$1,050 per ounce, these reserves will be reappraised and reduced because they were calculated using a gold price of \$1,475 per ounce.

It will also boost Yamana's annual gold production by around 238,000 ounces, which is an increase of 17% over its original 2014 production guidance of 1.4 million ounces. The low cost operation of the Malartic mine is highlighted by Osisko's estimated 2014 cash costs per ounce produced of between \$580 and \$635.

As one of the lowest cost producers in the gold mining industry, with estimated 2014 all-in-sustaining-costs of \$925 per ounce, Yamana is well positioned to build profitability even if gold prices continue to soften, particularly since its costs are lower than many of its peers, including Goldcorp, which has forecast for 2014, \$1,000 per ounce.

With Yamana having recently touched a 52-week low of \$8.25 per share and off by 28% over the last year, the company increasingly appears attractively valued when a number of industry-specific valuation ratios are considered. Yamana is currently trading with an enterprise value of 9 times EBITDA and \$348 per ounce, which is significantly lower than Goldcorp's enterprise-value of 17 times EBITDA and \$386 per ounce. It is also lower than Agnico Eagle's EV of 11 times EBITDA but higher than its EV of \$340 per ounce of gold.

Agnico Eagle and its shareholders are also set to reap the same benefits Yamana will receive as a result of the Osisko acquisition receiving 50% of the company's assets by way of the deal.

Foolish bottom line

While not a game changer for Yamana, it is clear the company will significantly benefit from the share of Osisko it has acquired. The acquisition may also just be the catalyst required to lift Yamana's lagging performance and boost its waning share price.

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