



3 Key Highlights From Silver Wheaton Corp.'s Results

Description

Silver Wheaton Corp. (TSX: SLW)(NYSE: SLW) is the largest precious metal streaming company in the world and derives approximately 75% of its revenue from the sale of silver and 25% from the sale of gold.

The company's business model is based on contractual arrangements to purchase, in exchange for an upfront payment, the silver and gold production of precious metals producers, including **Vale SA (ADR)**, **Barrick Gold Corp.**, and **Goldcorp Inc.** The price that Silver Wheaton pays for production averages approximately U.S.\$4 per ounce of silver and U.S.\$400 per ounce of gold, ensuring a fixed cost to the company.

Lower second-quarter profits

The company's second quarter of 2014 operating and financial results were reported on Wednesday. Profit per share declined by 10% to U.S.\$0.18 per share compared to U.S.\$0.20 for the same period a year ago. Operating profit and cash flow from operations declined by 18% as a result of lower sales revenue and lower margins. The financial outcome was below consensus estimates.

Sales revenue is a function of the quantities of silver and gold sold and average realized prices. Total silver equivalent ounces sold, or silver and gold sales combined, increased by 3.5% to 7.5 million ounces, but the average realized price declined by 14%, resulting in sales revenue 11% below the previous year. The cost of sales was only slightly lower as the company has multi-year purchase contracts with silver and gold producers at pre-determined prices, which result in a fairly stable cost of sales over time.

Overall expenses were sharply lower during the quarter, mainly as a result of a non-recurring item in the comparable period in the previous year, as well as much lower interest expenses. The lower interest bill was caused by the capitalization of a larger portion of the interest expense than in the previous year.

Another factor that propped up the net profit was the appearance of a tax credit recorded in the income statement. It is unsure whether the effective zero income tax situation of the company is sustainable,

and the cautionary comment regarding an ongoing audit by the Canada Revenue Agency of the company's international transactions covering the 2005 to 2010 taxation years was repeated again in the results announcement. This will remain a risk for the future profitability of the company until the CRA has announced the outcome of their audit.

Dividend payments are linked to operating cash flows whereby 20% of the average of the previous four quarters' operating cash flow is distributed to shareholders. A quarterly dividend of \$0.06 per share was announced; this compares to a dividend of \$0.10 paid in the same period last year.

Production results mixed

Attributable silver equivalent production for the quarter amounted to 8.4 million ounces, which was 4% lower than the same period a year earlier and the lowest production level in six quarters. However, for the first six months of the year, production was 2% higher at 17.4 million ounces.

The company again repeated its expectation to receive production of approximately 36 million silver equivalent ounces in 2014, slightly more than the 2013 production level. By 2018, production is expected to increase to 48 million ounces, which implies growth of 33% over the period.

Future performance will depend on the silver price

The financial performance of the company is highly dependent on the level of the silver price and to a lesser extent on the the gold price. Unsurprisingly, the share price also tends to closely track movement in the silver price.

The silver price has been declining for the past three years since it reached a peak of almost \$50 per ounce in early 2011, but has been relatively stable at around \$20 per ounce for the past year. However, Silver Wheaton's share price performed well over the past few months, adding 35% since the start of the year, possibly because of reports that George Soros made an investment in the company.

The share price may come under pressure as a result of the below par quarterly performance. However, the company has a great business model and its financial performance will improve when precious metal prices start to move up again.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:WPM (Wheaton Precious Metals Corp.)

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