Should You Buy Shares of Silver Wheaton Corp.?

Description

Here's a remarkable number for you: Last week, the European Central Bank settled US$2.2 billion of covered-bond purchases as it started its latest effort to revive the euro-area economy. And it doesn't take a rocket scientist to figure out what the end result of this policy will be: inflation.

The best way to protect your wealth from rising prices is to own hard assets like precious metals. However, if you want exposure to gold or silver, you have to be smart about it. Storing hunks of metal in a vault isn't the best investment strategy over the long run.

But investors still have plenty of options. Take **Silver Wheaton Corp.** (TSX: SLW)(NYSE: SLW), for example, the largest streaming metals company in the world. Here are three reasons to consider adding this silver stock to your portfolio.

1. Better than owning precious metals

You won't hear many in the resource business say this, but precious metals are bad investments. Unlike stocks or bonds, they generate no income or dividends. Fifty years from now, your silver coins will likely have the same purchasing power as they do today.

That's not the case with Silver Wheaton. This is a real business that can grow and compound over time. If you had purchased a share of this company back in 2004, you would have had a claim to about 1.5 ounces of silver. Today, that same share now represents 6.5 ounces of silver reserves.

As you can see in the chart below, this has resulted in a big difference in performance. Here the base is equal to 100.

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2. A smart business model

Silver Wheaton is like the financier for miners. It doesn't actually operate any mines itself. Rather, the firm loans money to mining companies through streaming contracts.

Here's how it works: Silver Wheaton provides the cash that mining companies need to build a new project. But rather than charge interest, Silver Wheaton is given the right to buy a percentage of the mine's gold or silver production. This is usually at a steep discount to spot prices.

This business model has a lot of advantages over your regular mining business. Given that the company's expenses are mostly fixed, investors don't have to worry about cost overruns. And because it pays only $4.65 per silver equivalent ounce on average for supplies, Silver Wheaton generates absurdly high profit margins.

3. A big, wide moat

When Warren Buffett is asked what he looks when investing in a business, his answer is usually the same: a big, wide moat. In the same way it protected castles from attackers, a moat protects the business from rivals. It's some sort of edge that allows a firm to earn excess returns for shareholders year after year.

Silver Wheaton has a moat around its business that is two miles wide and filled with angry sharks. The firm is the biggest streaming metals company in the world. That gives it credibility within the silver mining industry.

Silver Wheaton's size and experience makes it a No. 1 choice for financing. That gives it a competitive advantage when structuring deals. Over the past five years, the firm has generated gross margins around 70%, levels that rivals could never hope to match.

Of course, this company isn't a slam dunk. Aside from the obvious risk of falling metal prices, Silver Wheaton shares could suffer if its partners shut down mines. However, for investors looking for exposure to the resource industry, there's no better bet than Silver Wheaton.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

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

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