Should You Add Silver Wheaton Corp. to Your Portfolio?

Description

Gold and silver stocks are taking a breather right now after a big run that began in November and carried right through the new year. The move has been interesting this time because it occurred despite a strong surge in the value of the American dollar.

Economic conditions in the U.S. continue to improve but the market is still wary of a potential financial crisis in Europe, increased fighting in Ukraine, a possible ground war in Iraq, and a Chinese real estate bubble that could pop at any time.

Silver Wheaton Corp. (TSX:SLW)(NYSE:SLW) is one option to play a rally in the precious metals markets. The stock is up 28% in the last three months and investors are wondering if the company is going to continue its upward trend or reverse course and head back toward the $20 mark.

Let's take a look at the current situation to see if the stock should go on your watchlist.

Low supply costs

Silver Wheaton is a streaming company, not a miner. The business model is quite unique because the company pays mining companies an upfront sum to secure long-term or life-of-mine supply of gold and silver byproduct. The precious metals normally come from facilities designed to mine different metals, such as copper.

In exchange for the payment, Silver Wheaton gets a great deal on the silver and gold that it receives.

How good a deal?

In the third quarter of 2014 Silver Wheaton reported an average silver cost of $4.16 per ounce. The company's average gold cost came in at $378 per ounce. These prices are substantially lower than the market values of both gold and silver.

In fact, operation margins in the third quarter were better than 70% and the numbers for the fourth quarter of last year and Q1 2015 will probably be better.

Strong financial position

Weak commodity markets tend to benefit Silver Wheaton because it gains negotiating leverage over the companies it deals with. In the current environment, mining companies are having a tough time accessing capital for development and exploration programs. Issuing stock is very dilutive because share prices are extremely depressed and the debt market wants high premiums for lending in a risky market.

Silver Wheaton can negotiate great terms right now on new deals because it offers an appealing option for securing cash.

Silver Wheaton finished Q3 2014 with $233 million in cash and a $1 billion credit facility. This allows the company to take advantage of any opportunities that might arise as miners look to secure funds.

Production outlook

Silver Wheaton's supply pipeline is filling up nicely. In 2015 the Constancia project is set to go into production and expansion projects at other facilities are producing strong results. Even if gold and silver prices remain at current levels, Silver Wheaton should see improved earnings this year.

Risks?

Technical investors might be concerned that Silver Wheaton failed to break through the $30 mark in the latest run. The last three times the stock took a run at $30 per share, it quickly fell back toward $20. At the moment, it seems that the stock could be doing the same thing again.

CATEGORY

1. Investing
2. Metals and Mining Stocks

POST TAG

1. Editor's Choice

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