



New Gold Inc. Is Betting Big on This Mega Gold Project

Description

With its stock down nearly 60% in the past 12 months, **New Gold Inc.** ([TSX:NGD](#)) is exploring every option for turning its business around. Fortunately, it has one promising mega project that has the potential to bring profits back to life, even with historically low gold prices.

Its Rainy River project, which will produce 325,000 gold ounces annually, is set to begin commercial production by late 2017. With an all-in sustaining costs of just \$670 per ounce (\$100s cheaper than most mines), it should be a game changer for the company.

Unfortunately, the mine is expected to cost upwards of \$900 million. With \$880 million in debt and only \$325 million in cash last quarter, New Gold has been forced to look at alternative options for financing this costly, but promising project.

Going all in on Rainy River

Lately, New Gold has turned to selling assets to help fund development at its Rainy River project. While this is likely a less preferable option, it will result in New Gold being even more reliant on Rainy River's success.

For example, New Gold recently entered into an agreement to sell its interest in the El Morro project for \$90 million in cash and a 4% royalty on production. El Morro is a huge project containing 2.7 million ounces of gold reserves and 1.95 billion pounds of copper. Under full production, it should produce 300,000 ounces of gold and 300 million pounds of copper annually.

While it still has a 4% royalty on production, it is significantly smaller than its previous 30% stake. Using the proceeds to develop Rainy River means that New Gold is giving up production in other mines to bet big on a single venture.

Will it now sell its royalty?

A sure sign that New Gold is desperate is if it ends up selling its 4% royalty on El Morro production. If that's the case, there should be plenty of bidders for the royalty stream such as **Franco-Nevada Corporation**

, **Silver Wheaton Corp.**, or **Sandstorm Gold Ltd.** Estimates show that it's likely that New Gold would fetch \$60-80 million at today's gold price.

By sacrificing future royalty cash flows for immediate cash, investors can be certain that the company is tying its future to the Rainy River mine if it ends up selling the stream.

Can New Gold's strategy succeed?

On September 15 management reiterated the project remains on budget, with a total budget of \$877 million, and on time, with first production targeted for mid-2017. It also reaffirmed the mine's all-in costs of \$670 an ounce. If New Gold can manage to achieve these targets, expect the stock to have significant amounts of capital appreciation assuming gold prices don't fall even further.

Currently, New Gold will likely need to raise additional money to fund the remaining expenditures at Rainy River. This is easier said than done in this gold-price environment.

Still, the company was able to surprisingly unload its stake in El Morro for an attractive sum and could still sell its royalty stream for another \$60-80 million. With a total of \$575 million in cash next quarter and additional financing options still on the table, New Gold might just pull it off.

CATEGORY

1. Investing
2. Metals and Mining Stocks

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1. TSX:NGD (New Gold Inc.)

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