What You Need to Know Before Investing in Precious Metals Stocks

Description

Commodity-related stocks are more difficult to grasp than the average stock. Precious metals stocks in particular move more or less with the underlying commodity prices of gold and silver.

These stocks can perform badly across multiple years because low commodity prices reduce the profitability of these businesses.

Here's an overview of the landscape.

Precious metals miners

Even the world's biggest gold producer, **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX), could not be exempt from the downdraft that occurred recently. Its shares went on a multi-year decline from 2012 to 2015, which more or less tracked the decline of the price of gold.

But this year, as the gold price recovered (up about 13% year to date), Barrick Gold made a remarkable recovery and appreciated 100%. However, its shares are still nearly 60% lower than they were five years ago.

Similarly, **Goldcorp Inc.'s** (TSX:G)(NYSE:GG) share price declined more than 60% from 2012 to 2015, but the shares are 15% higher than they were a year ago.

Streaming companies

Precious metals streaming companies, such as **Franco Nevada Corp.** (TSX:FNV)(NYSE:FNV) and **Silver Wheaton Corp.** (TSX:SLW)(NYSE:SLW) are safer ways to gain exposure to precious metals than the precious metals miners.

Franco Nevada is a gold-focused royalty and streaming company that provides a safe dividend, which it has increased for nine years.

It has a diversified portfolio across 340 assets. Geographically, it earns 49% of its revenues from Latin America, 19% from Canada, 15% from the U.S., and 17% from the rest of the world.

The company is less risky than the miners, and it provides upside potential should the price of gold rise. The company has outperformed gold and the S&P/TSX Global Gold Index since it had its initial public offering in 2007.

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Silver Wheaton is the world's largest precious metals streaming company. It makes an upfront payment to its partnered mining companies. In return, it buys a percentage of their future silver or gold production at a predetermined price, so it profits from the difference between the cost and the actual precious metals prices.

For example, in 2015 Silver Wheaton paid US$4.17 per oz of silver and US$393 per oz of gold and had cash margins of 73% and 66%, respectively.

Without any exploration costs and with a portfolio with more than 25 years of mine life based on reserves, the company is set to remain profitable across various stages of the precious metals cycle.

The takeaway

If you want large gains from the sector, invest in precious metals miners such as Barrick Gold and Goldcorp. However, be careful of getting caught in a multi-year decline.

Don’t try to catch the bottom, but wait until gold and silver prices have sustainably recovered from a bottom before buying.

The streaming companies are a safer way to gain exposure to gold and silver. And the recent pullback brings them to better valuations for your consideration.

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1. Dividend Stocks
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TICKERS GLOBAL

1. NYSE:B (Barrick Mining)
2. NYSE:FNV (Franco-Nevada)
3. TSX:ABX (Barrick Mining)
4. TSX:FNV (Franco-Nevada)
5. TSX:WPM (Wheaton Precious Metals Corp.)

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Date
2025/08/23
Date Created
2016/11/23

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