Does Silver Wheaton Corp. Deserve to Be in Your Portfolio?

Description

Silver Wheaton Corp. (TSX:SLW)(NYSE:SLW) has fallen nearly 40% since the middle of August.

That's bad news for investors who jumped in at the top, but contrarian types with a long-term, positive view on the precious metals markets are wondering if the sell-off is overdone.

Let's take a look at the streaming company and the outlook for gold and silver to see if this might be a good time to buy.

The streaming model

Silver Wheaton doesn't own any mines; the company simply provides mining companies with funds to help them move their projects from development to production.

In return for the cash infusion, Silver Wheaton is given long-term or life-of-mine rights to purchase gold or silver produced at the mine for a very attractive price.

How attractive?

The company reported Q3 2016 cash costs of US$4.51 per ounce of silver and US$390 per ounce of gold. Silver Wheaton received an average of US$19.53 per ounce of silver sold and US$1,336 per ounce of gold sold in the quarter, so the margins are pretty sweet.

Gold is becoming a larger part of the mix, hitting 109,200 ounces in Q3 compared to just 58,600 ounces of gold in Q3 2015.

Overall, the streaming model is attractive because it gives investors a way to play the gold and silver sectors without taking on the direct operational risks that come with owning the miners.

Gold and silver market

Precious metals have been on a steep slide since the U.S. election. That wasn't supposed to happen in response to a Trump win, but the market often zigs when the herd expects it to zag, and this is a perfect example.

Going forward, gold and silver could go either way.

Supporters of the precious metals say Trump’s anti-trade stance could trigger chaos in global markets and lead to strong gold demand as investors look for a safe place to hide.

Gold bugs also believe Trump’s plan to slash taxes and unleash a boom in infrastructure spending will fuel inflation, which also tends to be positive for gold.

On the opposite side of the fence, pundits say Trump’s policies will continue to drive up the value of the U.S. dollar, in which gold is priced, thus making the metal more expensive for foreign buyers.

Analysts also see the potential for more aggressive interest rate hikes by the Federal Reserve in 2017 and beyond if Trump’s plans heat up the U.S. job market and economic growth.

Higher rates are often negative for gold because they raise the opportunity cost of hold the non-yielding yellow metal.

Silver normally rides gold’s coattails, but it can diverge from time to time. Supporters of silver say the global solar energy boom is going to be positive for silver demand in the coming years, and the lack of new mine developments could tighten the market in the medium term.

Should you buy?

Owning stocks in the precious metals sector requires a positive view of the gold and silver space over the medium term. If you are in that camp, Silver Wheaton is a smart way to play the group.

At this point, however, I would keep the position small until a clear upward trend is reestablished in the market.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

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

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