



Pending Default or Deep Value? Investors Assess Tahoe Resources Inc.

Description

Any time a mining company receives news that a constitutional court ruling upholding the suspension of their operating licence has taken place, investors being to panic. For **Tahoe Resources Inc.** (TSX:THO)(NYSE:TAHO), the panic appears to be real, as shares slid more than 20% in early trading on Friday following the announcement that a Guatemalan high court had upheld the previous decision of a lower court to temporarily halt operations at Tahoe's Escobal mine.

As it happens, the Escobal mine, located 40 km southeast of Guatemala City, is one of the world's largest silver mines and remains the largest revenue and earnings generator for the mining company overall.

Here's why this ruling is a big deal for Tahoe shareholders.

First of all, it has become evident that Tahoe may no longer be able to achieve its mid- to long-term guidance with respect to revenue and earnings and is likely to revise its forward guidance accordingly. Markets being the way they are, it appears analysts have already done the scenario analysis to determine what Tahoe's intrinsic value would be if the preliminary ruling is upheld, and the aforementioned 20% one-day loss in market capitalization likely represents a big chunk, if not all, of the reduction in future free cash flows relating to this event.

The final constitutional ruling in this case will come after the hearing, which was scheduled for August 28; until then, constructing a valuation for Tahoe will become an exercise of probabilities: either Tahoe will be able to convince the Guatemalan courts that its subsidiary, Minera San Rafael, should be able to continue operations, or the final decision will support the previous two rulings.

The other huge impact of this ruling which investors will need to price in is the increased risk of financial distress stemming from the company's ability to meet its debt covenants tied to the Escobal mine. The debt many mining companies hold is secured by the underlying operations of the firm. Thus, should operations be halted, companies like Tahoe may be in deep trouble. Tahoe has already indicated that it will not be able to access the full capacity of its most recent revolving credit facility, also indicating it may be subject to potential credit events or defaults moving forward.

Bottom line

This is certainly very negative news for Tahoe, a company which has seen its market capitalization plummet, losing more than 80% of its value since 2014. The risks may simply outweigh the rewards in this case, and investors considering Tahoe need be aware that this is a very risky play, one which should be handled with extreme caution, even after dropping 20% intra-day on Friday.

Stay Foolish, my friends.

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