Is This Beaten-Down Gold Miner a Worthwhile Investment?

**Description**

Intermediate gold miner **New Gold** (TSX:NGD)(NYSE:NGD) has been roughly handled by the market, losing 64% over the last year, despite gold losing a mere 1%. Much of this can be blamed on management revising production forecasts downwards and a raft of issues impacting operations at New Gold's Rainy River mine. While there are concerns over New Gold's ability to unlock value, there was a significant improvement in its operational performance during the fourth quarter 2018, which lifted its overall annual performance.



## Improved operational results

Gold production for the final quarter of 2018 expanded by 26% quarter over quarter and 68% year over year to 97,428 gold ounces. Full-year production of 315,483 gold ounces was more than double the 149,009 ounces produced a year earlier. The significant increase in gold output can be attributed to the Rainy River mine, which commenced commercial production in October 2017. After experiencing a series of operational issues that impacted production at the mine, New Gold implemented a short-term operational plan aimed at addressing a range of shortfalls at the mine to enhance its performance.

That strategy has delivered solid results for the miner. The volume of ore mined at Rainy River during the fourth quarter was 3% greater than a year earlier, while the average gold grade increased by 51% to 1.42 grams of gold per tonne of ore (g/t) mined, and the recovery rate rose 3% to 89%. As result of those improvements, gold production at Rainy River grew almost threefold year over year to 77,202 ounces.

These developments were the key reason for a sharp reduction in the mine's operating expenses, which, for the fourth quarter, were US$648 per gold ounce sold, or less than half of the US$1,432 per ounce reported for the equivalent period in 2017. Total cash costs also fell substantially to US$641 per gold ounce sold, which was 55% lower.

Regardless of those lower production costs, Rainy River's all-in sustaining costs (AISCs) rose by almost 1% year over year to US$1,054 per gold ounce sold. That can be attributed to increased spending on mine development and maintenance activities caused by the unplanned challenges associated with ramping up production at the mine.

Despite these significant improvements at New Gold's flagship Rainy River mine, it reported a 2018 net loss of US$1.2 billion compared to US$108 million for the year prior. This worrying and substantial increase in New Gold's net loss, however, was not caused by operational failings but rather a large impairment charge recorded against the value of its Rainy River and Blackwater mines totaling almost US$1.1 billion. Those charges related to accounting procedures rather than failings at either mine.

## Stronger financial position

Toward the end of 2018, New Gold closed the sale of its Mesquite mine for US$158 million, boosting its liquidity and strengthening its balance sheet. This saw the miner finish 2018 with US$104 million in cash and an undrawn credit facility with US$289 million available, giving it total liquidity of US$393 million.

New Gold does, however, have a burdensome debt load with long-term debt totaling US$781 million, which is a somewhat worrying three times trailing 12-month operating cash flow. The risks associated with that debt are mitigated not only by New Gold's considerable liquidity but also by the fact that there are no material repayments due until 2022. This provides New Gold with ample time to benefit from firmer gold and build its cash holdings.



## Why buy New Gold?

The miner's poor performance after the commissioning of its flagship Rainy River miner certainly unnerved investors, leading to it being savaged by the market and losing 64% over the last year.

Nevertheless, fourth-quarter and full-year 2018 results show a marked improvement in the performance of Rainy River, which, along with forecast higher 2019 gold production and firmer gold, will give earnings a healthy bump. Those factors, along with New Gold being marked down so heavily by the market, means that the risk/reward equation has moved in favour of investors, making now the time to make a contrarian bet on the miner.

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