Investing in Gold? This Stock May Be Your Safest Option

Description

Investing in gold can be tricky.

The most direct option is to buy a gold ETF like **SPDR Gold Trust** or **iShares Gold Trust**. Often, however, these ETFs purchase futures contracts, not gold itself, potentially leading to pricing discrepancies over the long term.

Another option is to buy stock in a gold miner. If history is any suggestion, this is a risky way to make a long-term bet on gold.

Mining companies have proven terrible stewards of capital, chasing ever-larger projects in pursuit of growth over shareholder value. Even if gold prices increase, you can be left out of the run by investing in the wrong miner.

How should gold bulls invest? Metals streaming companies are a great, under-the-radar option. Meet **Sandstorm Gold** (TSX:SSL)(NYSE:SAND).

What is a metals streaming company?

Buying gold itself is fairly straightforward. Buying stock in a gold miner is similarly intuitive. But what is a metals streaming company?

Streaming companies help finance mining projects. In return, these companies receive streaming agreements that essentially give them the rights to purchase future production at attractive prices.

For example, Sandstorm Gold has a streaming agreement with the Black Fox Mine located outside Matheson, Ontario. Sandstorm Gold provided the financing necessary to complete additional exploration activities. In return, the company has the right to buy 8% of future production for US$540 per ounce, a 50% discount to prevailing market prices.

A better bet than mining companies

Given how these agreements are structured, metals streaming companies have much lower risk profiles than mining companies.

First, they can spread their bets across many projects. Since 2009, Sandstorm Gold has acquired 185 streaming deals located around the world, some with more established mining companies and others with emerging players, balancing the risk and reward opportunities of its portfolio.

Second, metals streaming companies aren't on the hook for cost overruns or project difficulties. Execution is left entirely up to the mining company.

Previously, I had a chance to interview Sandstorm Gold CEO Nolan Watson. He highlighted the risk tradeoff investors make when buying stock in a mining company.

"To want to own a miner instead of a royalty company you have to assume that the miner can deliver what they say, within the timeframe that they outline, and that they won't have any technical problems or metallurgical problems," he told me. "On a spreadsheet, mining companies can look cheaper, but in reality, almost none of the underlying assumptions when building and operating a mine go as planned, which is why the royalty companies are better investments."

Get ready for cash flow

Sandstorm Gold has one major advantage versus its mining peers: it's cash flow positive.

At current commodity prices, the company should generate US$60 million in free cash flow in each of the next three years. From 2022 through 2024, annual free cash flow is expected to surpass US$100 million.

At that time, the company will be able to return large amounts of capital to shareholders or pursue deals to ramp cash flow even faster. Either way, the company looks like a much more reasonable bet than buying a mining stock.

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