Precious Metals Streamers — a Lower Risk Way to Gain Exposure to Gold and Silver

Description

Looking for a reliable income producing investment that bolsters the defensiveness of your portfolio and helps to hedge against risk as well as growing economic uncertainty? Look no further than precious metals streamers.

The latest sharp pullback in gold and silver has created an opportunity for investors to boost their exposure to precious metals and protect their portfolios against a looming economic downturn.

While many pundits look to miners as being one of the best means of gaining exposure to precious metals, it is the streamers such as **Osisko Gold Royalties** (TSX:OR)(NYSE:OR) and **Wheaton Precious Metals** (TSX:WPM)(NYSE:WPM) that offer a superior means of gaining levered exposure to precious metals.

Lower costs and higher margins

A key advantage they have over gold and silver miners is that their business model endows them with substantially lower costs, as mining is an extremely financially intensive activity. It requires significant amounts of capital to develop and sustain a gold mine.

Continental Gold is developing one of the world's largest and highest-grade gold projects; the Buritica mine in Colombia is estimated to cost US$512 million in pre-production development expenses.

After commencing commercial operations, it is estimated that a further US$273 million will need to be spent over the mine's 14-year life just to sustain production at forecast levels of up to 300,000 gold ounces annually. That's a tremendous burden for any miner, but especially for a small gold producer like Continental Gold.

Mining's capital-intensive nature makes it virtually impossible for all but the largest senior miners to significantly diversify their producing mining assets.

The low-cost nature of streamers is underscored by Wheaton Precious Metals' 2018 results, when it reported cash costs of US$409 per gold ounce produced. That is significantly lower than senior miner **Newmont Mining,** which reported consolidated cash costs of US$708 per ounce.

This means that streamers can generate solid margins at gold and silver prices, which would cause losses for a miner and are significantly more profitable when precious metals rally.

It is also important to note that because streamers don't own or operate mines, they aren't required to invest additional capital in development and maintenance to sustain production. This frees up additional funds for investment in the acquisition of streaming and royalty agreements as well as further bolstering profitability.

Reduced investment risk

Precious metals streamers don't engage in hazardous mining activities, meaning that they are not exposed to the numerous operational hazards that can cause production outages, higher costs or reduce output.

Instead, in exchange for receiving a royalty on the volume of gold and silver sold by a miner or the right to purchase those precious metals at marked discount to their spot price, they provide finance to precious metals miners.

Miner's typically are unable to widely diversify their operations because of the vast amounts of capital required to develop an ore body and bring it to commercial production, which makes them highly dependent on a small number of operations for their production and hence earnings.

Tahoe Resources' travails with its flagship Escobal mine in Guatemala illustrates just how badly things can go for a miner. Escobal**,** which is the world's third largest silver mine**,** was responsible for generating around 45% of Tahoe's revenue.

After operations were shuttered in 2017 because its licence was suspended by the Guatemalan courts, Tahoe's earnings took a heavy hit.

There is also no guarantee that a commissioned mine will perform as forecast. The ongoing headaches experienced by **Pretium Resources** at its cornerstone Brucejack mine illustrate this hazard.

A combination of lower than expected ore grades and flawed mine design caused gold production, grades and recoveries to fall short of estimates, which saw Pretium's stock roughly handled by the market.

Streamers can significantly reduce this risk by holding a widely diversified portfolio of streaming and royalty agreements across mines, companies and jurisdictions.

Osisko Gold Royalties holds a portfolio composed of 135 royalties, streams and precious metals off takes covering 17 producing mines and 11 projects under development, while industry leader Wheaton has 23 separate precious metal interests covering 19 producing mines and 9 development projects.

This considerable diversification across operations, assets and countries minimizes the impact of production outages or other issues at any of those producing mines caused by operational or regulatory difficulties.

What does it mean for investors?

Precious metals streamers are a less risky way for investors to gain exposure to gold and silver. Highly diversified portfolios of mining interests coupled with low costs and minimal exposure to operational hazards make them a low-risk means of gaining exposure to precious metals.

In fact, some pundits have likened their risk profile to being almost ETF like because of the reduced degree of risk associated with their business model.

It should be noted that the streaming and royalty agreements are attached to the mine and not the operator, meaning there is little to no counter party risk in the event of the miner going bankrupt.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

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