

Yamana Gold: An Industry-Leading Organic Growth Profile

Jan. 11, 2021 12:10 PM ET

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About: [Yamana Gold Inc. \(AUY\)](#)



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Long/Short Equity, Momentum, Gold & Precious Metals

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Summary

Yamana Gold is down nearly 25% from its year-to-date highs despite a brilliant acquisition in Q4 and a massive improvement in its balance sheet.

Given the Phase II Expansion at Jacobina and addition of Wasamac, Yamana has the potential to produce over 1.1 million GEOs in FY2024, with this figure not including Agua Rica.

Even with this impressive organic growth profile, the company is trading at below 14x estimated FY2020 free-cash-flow.

Given Yamana's industry-leading organic growth profile, improving cost profile, and competitive dividend yield, I would view dips below \$5.15 as low-risk buying opportunities.

It's been an exciting couple of months for Yamana Gold (NYSE:[AUY](#)) shareholders, but despite positive news from Agua Rica and the recent acquisition of [Monarch Gold \(OTCOX:MRQRF\)](#). However, despite this recent news, the stock remains in a slump, nearly 25% from its year-to-date highs. The good news is that this deep correction has significantly improved the valuation, especially when we factor in Yamana's industry-leading organic growth profile. In fact, despite one quarter being disrupted due to COVID-19, Yamana is trading at barely 14x estimated FY2020 free cash flow. Given the company's improving cost profile with Jacobina Phase II and competitive dividend, I believe dips below \$5.15 will provide low-risk buying opportunities.



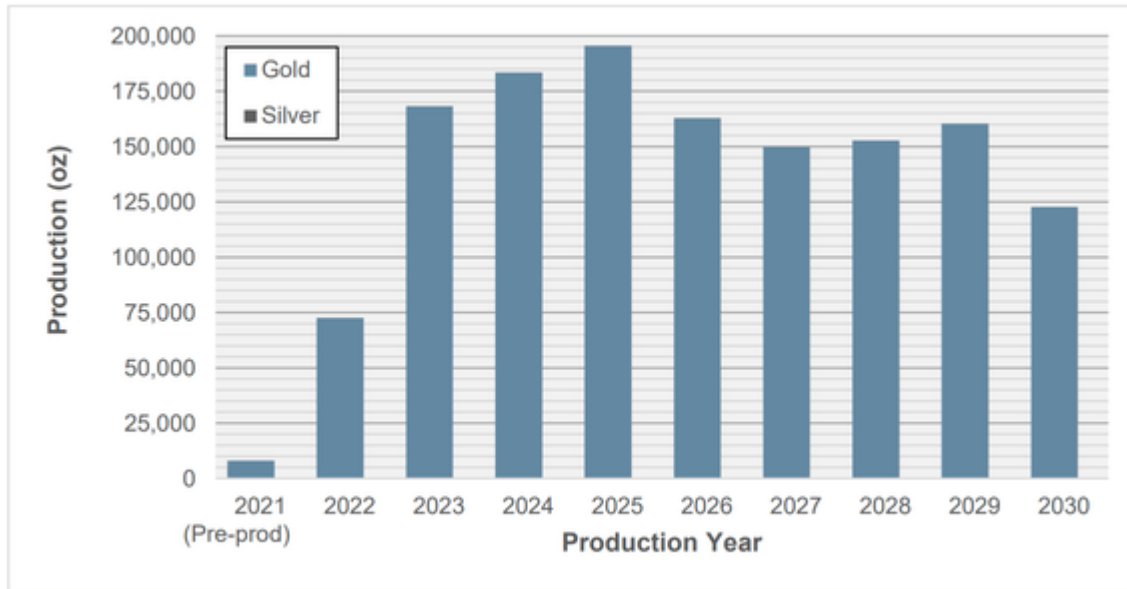
(Source: Company Presentation)

Yamana Gold was one of the few million-ounce gold producers to play offense in H2, with the company moving in to [acquire development-stage Monarch Gold](#) in Quebec. Monarch Gold was acquired for less than \$70.00~ per reserve ounce and adds [1.76 million ounces of high-grade gold](#) to Yamana's reserve base. This was a brilliant deal, but even more exciting was the [recent news](#) of the Agua Rica integration, combining Agua Rica with the Alumbreira plant and infrastructure. Yamana will hold a 56%~ stake in the massive copper project, and this should significantly beef up gold-equivalent ounce production (GEO) long-term. These two developments, including the Phase II Expansion at Jacobina, have given Yamana strong organic growth potential relative to its million-ounce producer peers. Let's take a closer look below:



(Source: Company Presentation)

As I noted in my previous article, Yamana's acquisition of Monarch is important for two reasons: margins and jurisdictional risk. While Yamana Gold's flagship operation (50% ownership of Canadian Malartic) helps its jurisdictional profile, the bulk of its operations are in South America, with these countries generally ranked as Tier-2 jurisdictions. Meanwhile, Yamana's costs have consistently come in above \$1,050/oz, roughly 8% above the [FY2019 industry average](#) of \$980/oz, and in the higher end of the range relative to its senior producer peers. Fortunately, Monarch's Wasamac Project offers exceptional margins and an improved jurisdictional profile, killing two birds with one stone in terms of helping its multiple in the future relative to peers.



(Source: Monarques Gold Technical Report)

As shown in the chart above, the 2018 economic study completed for Wasamac envisioned 170,000~ ounces of gold production in FY2023 and 185,000~ ounces in FY2024, with a long-term average annual production profile of 142,000 ounces. This timeline looks ambitious as pre-production was expected to begin in FY2021, and I would be surprised if pre-production began before Q3 2022. However, if we assume the timeline is pushed back by 15 months, this means that Wasamac could produce over 70,000 ounces in FY2023 for Yamana (2022 in the above chart) and 170,000 ounces in FY2024 (2023 in the chart). This would move the needle quite a bit in terms of annual GEO production, with Yamana's current production profile just shy of 1,000,000 ounces. Notably, costs at Wasamac are expected to come in at \$630/oz, among the lowest costs for undeveloped gold projects globally.



(Source: Author's Chart)

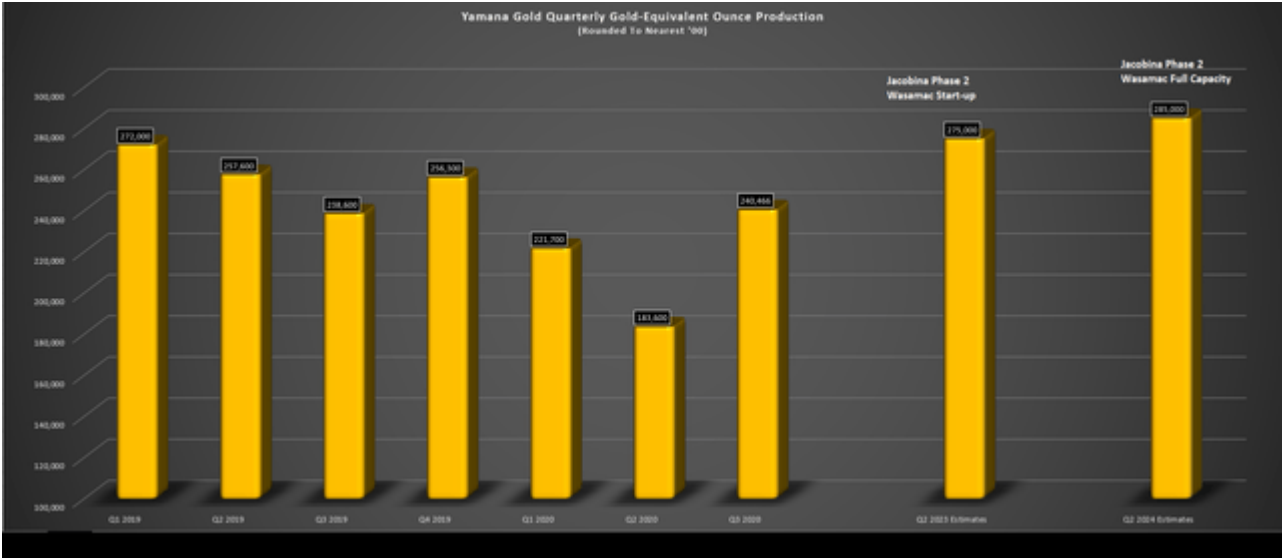
Meanwhile, Yamana Gold released a [Phase II Study](#) for its Jacobina Mine in Brazil earlier this year, with projections for 230,000 ounces of annual gold production, up from 175,000 ounces currently. The significant increase in annual production comes with modest capex of less than \$60 million and is expected to be completed in FY2023. Therefore, assuming

Yamana can meet this timeline, this is yet another solid pillar for production growth. As the chart above shows, Q1 2023 production could grow from 44,100~ ounces (current) to 57,500~ ounces, adding another 13,000 ounces per quarter to Yamana's production profile. Like Wasamac, this production is coming at improved costs, with estimated Phase II [all-in sustaining costs of \\$727/oz.](#) This is a solid improvement from FY2020 guidance of \$890/oz.



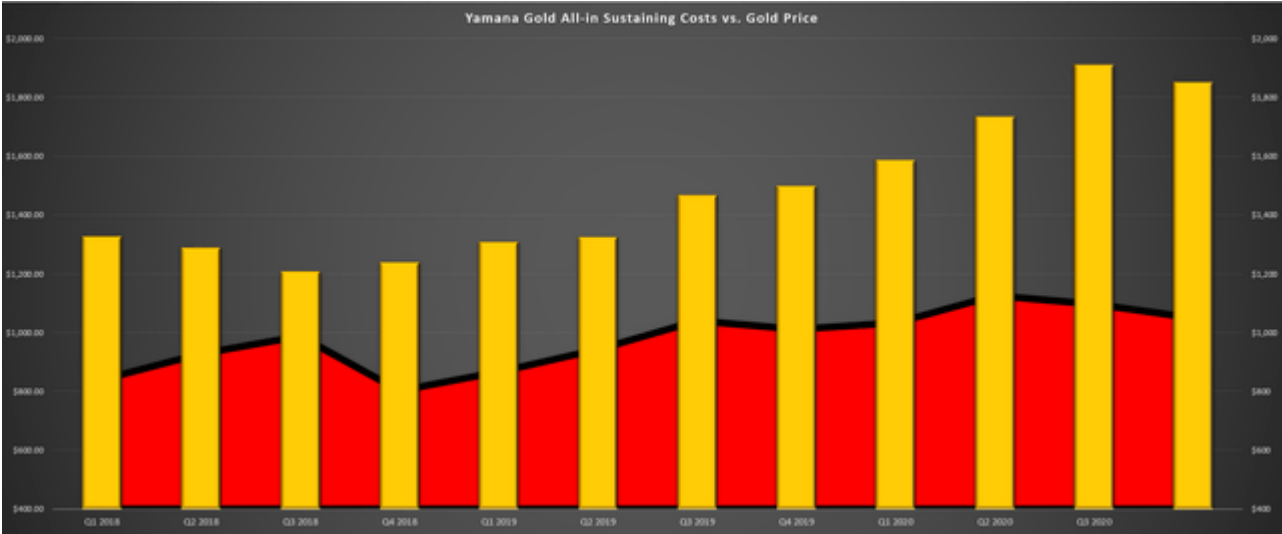
(Source: Company Website)

If we look at the chart below of Yamana's quarterly GEO production, we can see that Jacobina and Wasamac (if built) should have a material effect on the company's production profile. This is because I would expect Jacobina Phase 2 to be nearly complete by Q2 2023 and Wasamac to be starting up production at nearly half capacity. This would translate to 275,000 GEOs in Q2 2023, a 15% increase from the current production rate. Meanwhile, production should increase to 285,000 GEOs in Q2 2024, assuming Wasamac is running at full capacity by then (170,000~ GEOs per year). Assuming these goals are met, we would see a nearly 20% increase in production from current levels, and this assumes no contribution in this production profile from Agua Rica. Given that most million-ounce producers have minimal growth between now and FY2024, this makes Yamana Gold a stand-out name.

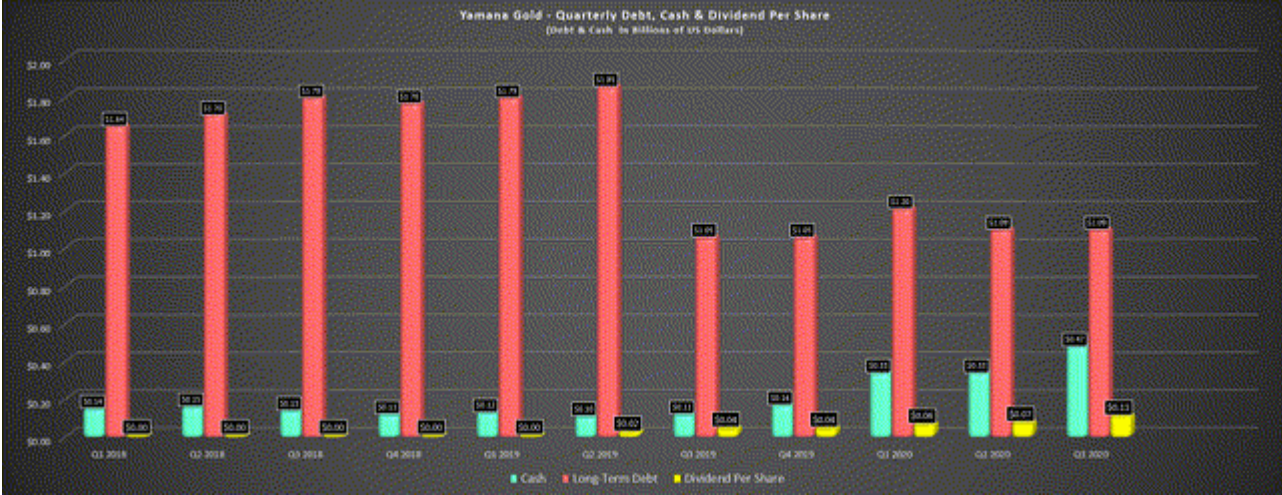


(Source: Author's Chart, Author's Estimates)

While a couple of years might seem like a long to wait for meaningful growth, it's worth noting that Yamana Gold is already firing on all cylinders. As shown in the chart below, the company is on track for its fourth consecutive quarter with all-in sustaining cost margins above \$600/oz, a massive improvement from two years ago when the spread was barely \$300/oz (the red shaded area is costs vs. gold price in yellow). This significant improvement in margins due to a higher gold price with stable costs has allowed the company to continue paying down debt and massively increase its dividend yield. In fact, Yamana's net debt is down from \$1.75~ billion 15 months ago to \$620~ million, while the dividend yield is up from \$0.02 per share annually to \$0.11 per share. At a share price of \$5.40, this represents an attractive and very competitive 2% yield in a market where it's hard to find solid yield coupled with growth.



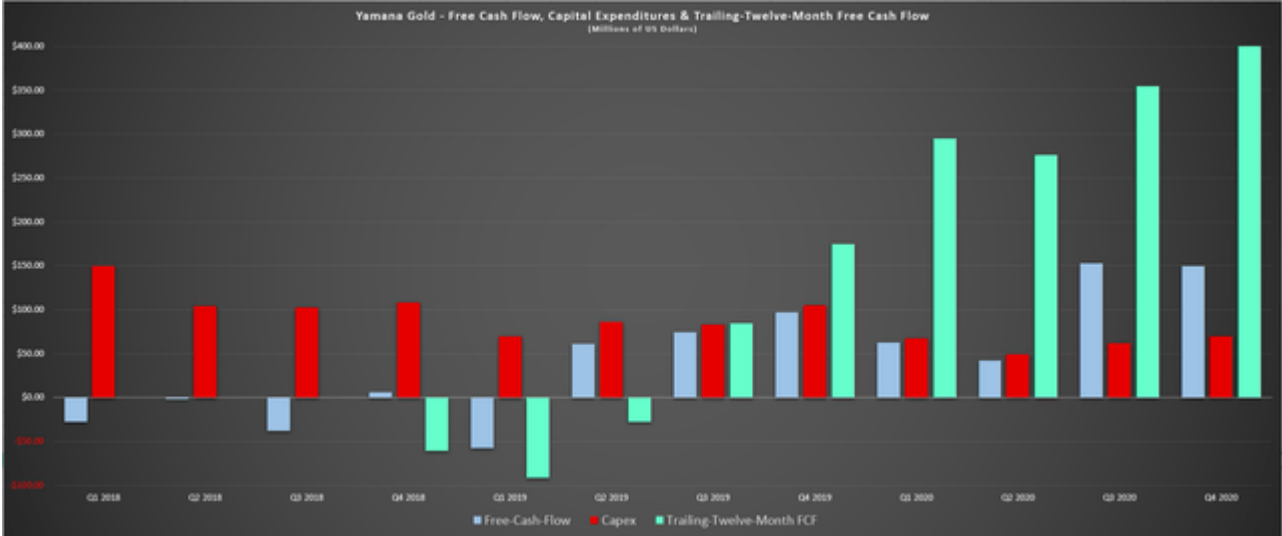
(Source: Author's Chart)



(Source: Author's Chart, Company Filings)

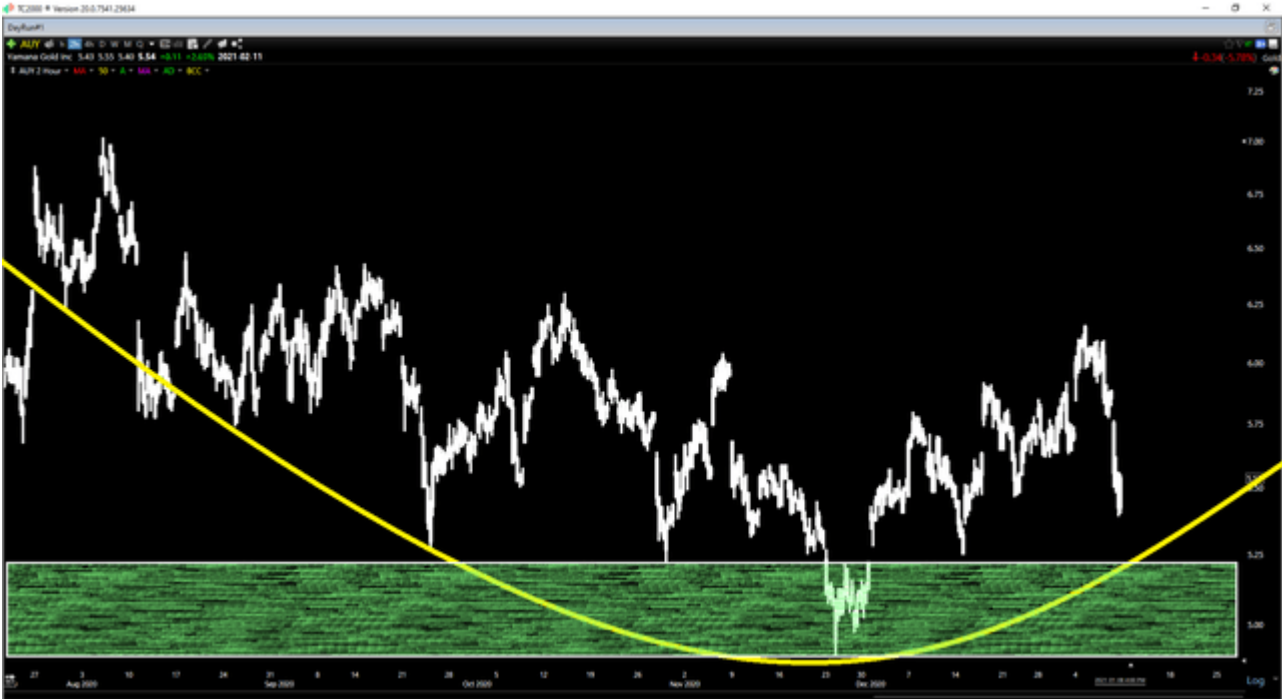
It's certainly discouraging to see the correction we have in Yamana, but the good news is that it's done a lot for the senior producer's valuation. As shown below, the company reported over \$150 million in free cash flow in Q3 and is on track to report between \$390 million to \$405 million in free cash flow in FY2020, based on my estimates. Based on Yamana's market cap of \$5.27~ billion, this means the stock is trading at just 13.3x~ free cash flow based on my midpoint estimate of \$397~ million. This estimate is based on Yamana's year-to-date free

cash flow of \$258~ million and estimates for above \$135 million in free cash flow in Q4 based on higher production but offset by slightly lower metals prices.



(Source: Author's Chart, Company Filings)

While 13.3x FY2020 free cash flow estimates might look a little high, it's worth noting that COVID-19 derailed Q2 production due to shutdowns, and FY2021 free cash flow could come in as high as \$550 million with a more normal year for operations and gold price above \$1,800/oz. Based on this metric, Yamana is trading for less than 9.6x next year's free cash flow. This is a very reasonable valuation considering the organic growth potential stemming from Wasamac, Jacobina Phase II, and Agua Rica. Let's see how the technical picture looks:



(Source: TC2000.com)

If we look at the short-term chart above, we can see that Yamana is trying to carve out a cup-shaped base, with strong support in the \$4.95-\$5.20 area. In [my previous article](#) on Yamana, I noted that dips below \$5.15 would provide a great entry, and there was an opportunity to pick up the stock in this zone briefly in late November. While I would prefer not to see this low

tested in the \$5.00 area to make for a cleaner chart, I would expect this to be a buying opportunity yet again if we test the \$5.15 level. This would coincide with a 5th test of the cup-shaped base the stock is building and a second test of the pivotal \$4.95 - \$5.20 support zone.



(Source: TC2000.com)

Short-term charts can be helpful, but the bigger picture is generally much more important to see if we truly see something on the lower time frames. As shown above, Yamana Gold broke out of a massive base earlier this year and continues to consolidate above its breakout level. This is a very bullish development, and I see no reason to call this a failed breakout unless the stock dips below \$4.50. Therefore, while this correction has been very messy and frustrating for those that overpaid for the stock, minimal technical damage has been done here to date.



(Source: Company Website)

It's easy to be bearish on Yamana Gold after a deep four-month correction from its highs, but it's worth noting that zero real damage has been inflicted to the big picture here. Meanwhile, the fundamental thesis has continued to strengthen with incremental growth opportunities from Wasamac and Jacobina Phase II, and Agua Rica now in the wings long term. *Based on a reasonable valuation for Yamana of less than 10x FY2021 estimated free cash flow, I believe we are nearing another buying opportunity here if this weakness continues. Therefore, I remain optimistic long term despite the depth of this correction, and I would view any pullbacks below \$5.15 as buying opportunities.*

Disclosure: I/we have no positions in any stocks mentioned, and no plans to initiate any positions within the next 72 hours. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

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