EQUITY RESEARCH
GOLD… as an alternative

COLLINS SARRI STATHAM
INVESTMENTS

Research Report
ADVISORY SERVICES

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Gold "comes in from the cold"

Recent equity market volatility has helped gold overcome its reputational issues. The yellow metal peaked at just over $1900 / oz in September 2011 but has spent most of the last four years between $1050-$1300 / oz. Recent gold buying is a function of:-

a) Heightened global equity and currency market volatility
b) Reduced expectations for Federal Reserve rate hikes over 2016
c) Increased perception of US/ UK political risks over 2016 necessitating a liquid global asset denominated in USD and benefiting from "safe haven" status (albeit with a tarnished reputation).

What precisely has changed?

According to World Gold Council (www.gold.org) data gold demand in Q4 2015 rose 4% to 1,117 tonnes. This suggests improving gold supply/ demand fundamentals.

Supply of Gold:-

i) Annual gold mine production up 1% (its slowest rate since 2008) whilst recycling activity dropped to multi-year lows during the 2012-15 down cycle.

Demand for Gold:-

i) Consumer demand remained resilient over Q4 (US +6%, India +6%, China +3%, East Asia +5%) balanced out lower demand from EU -7%, Middle East -18% and Russia -26%.

ii) Overall as World Gold Council 2015 data shows, gold demand was resilient and almost unchanged (-0.3%) suggesting buyers kept buying and were incentivised by the lower average price (-$106.30 / oz) over 2015.

Tonnes	2014	2015
Jewellery	2,480.8	2,414.9
Technology	346.4	330.7
Electronics	277.5	263.3
Other Industrial	49.0	48.6
Dentistry	19.9	18.9
Investment	815.4	878.3
Total bar and coin demand	1,000.5	1,011.7
Physical Bar demand	725.2	731.6
Official Coin	203.0	212.6
Medals/Imitation Coin	72.2	67.4
ETFs & similar products[1]	-185.1	-133.4
Central bank net purchases	583.9	588.4
Gold demand	4,226.4	4,212.2
London PM fix, US$/oz	1,266.4	1,160.1

Source; World Gold Council

Chronic product oversupply/ dependence on China is a key factor for base metals. But this is not the case for gold (supply +1%/ demand -0.3%) over 2015. In 2016 we expect demand growth to continue the Q4 trend and outstrip supply growth.

SPDR Gold Trust (NYSE:GLD) ETF….. BUY

The SPDR Gold Trust is a highly liquid ETF (exchange traded fund) that is listed on the New York (NYSE), Singapore, Tokyo, Hong Kong and Mexican stock exchanges. It is the world's largest fund holding 760.3 tonnes of gold (equating to 24.44m oz) in physical form. The ETF share price closely tracks the underlying gold assets (close to 0.5% premium) and is low cost. The SPDR Gold Trust is basically an easy way for investors to obtain exposure to the underlying gold assets (track the gold price) without having to worry about the costs of gold ownership (storage, insurance, lending activities).

Company	Spider Gold Trust GLD
Share Price ($)	117.93
Target Price ($)	135.00
52 Wk Hi/Low ($)	120.83/100.23
Shares O/S	236m
Market Capitalisation	$30.2BN
Avg Daily Volume	1.1M
Dividend Yield	0%

Source; Fidessa plc

Key Catalysts

There are numerous potential catalysts for gold over 2016 that would impact GLD:-

a) A nervous period prior to June 23rd UK referendum, encouraging diversification out of STG and EUR assets helping gold.
b) Poll gains for Donald Trump ahead of November 2016 Presidential election
c) Expansion in EU and Japanese bond purchases, more quantitative easing
d) Reductions in nominal interest rates/ negative nominal interest rates

Key Risks to Price Target

i) The Spider Gold Trust ETF invests over 99% of assets in physical gold hence risk of tracker error (the difference between commodity and fund return). This is a US dollar ETF listed on the NYSE hence there is currency risk and equity/ commodity related risks for STG based investors.
ii) The costs incurred by the Spider Gold Trust ETF may vary due to the changing costs for insuring and storing gold

Hochschild Mining….. BUY

Hochshild Mining is a leading precious metals company focused on the exploration and mining of gold and silver in Peru and Argentina via four underground mines. Hochschild recently completed a $100m rights issue and repaid $105m in debt considerably strengthening its balance sheet. The new Inmaculada mine is a low cost property ($13-$14 per ounce) which has produced ahead of forecast (7.1m oz) v 6.5m oz forecast.

Company	Hochshild Mining
Share Price (p)	67
Target Price (p)	95.00
52 Wk Hi/Low (p)	100/39
Shares O/S	505.57m
Market Capitalisation	£338.8m
Avg Daily Volume	2.6m
Dividend Yield	0%

Source; Fidessa plc

Key Catalysts

The $100m rights issue and other measures have cut debt by $104m to $366m enabling the team to fund capital expenditure plans over 2016. These plans, including developing the Pablo vein and reach a target of 32m silver oz over 2016.

Hochschild Mining revenues were split broadly equally between gold and silver, though Hochschild increased attributable gold production to 166koz from 100k oz in 2014. Our expectation is the group will achieve higher hedge values for 2017 helping revenue and profit forecasts.

Key Risks to Price Target

i) Hochschild Mining revenues are sensitive to volatile pricing for gold and silver.
ii) Both countries of operation, Peru and Argentina are high risk locations for mining assets and subject to changing regulatory and fiscal regimes
iii) Gold and silver mines can experience deterioration in the grade extracted which reduces output and increases waste material, there are other unpredictable operational risks that can impact mine performance.
iv) Hochshild Mining is a mid-cap company which may experience periods of lower liquidity.

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SELL: The company’s valuation appears too high having regard to material uncertainties, declining profit prospects or has sizeable funding requirements. A sell recommendation may also be applied where the board have failed in key objectives or appear to be frequently changing strategy. A sell recommendation means the analyst expects the share to fall to the price target on the note.
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