Wheaton Precious Metals

Still shining

Q2 results

Metals & mining

Despite a second quarter in which ounces produced but not yet delivered to Wheaton Precious Metals (WPM) increased, earnings from operations were just US$2.8m (or 3.2%) below our earlier published estimate of US$85.7m. In addition, management formally changed its dividend policy, from 20% of average cash generated by operating activities to 30%, which thus allowed it to declare a relatively generous third quarter dividend of 10c/share compared with our prior expectation of 6c. Silver sales exceeded gold sales for the first time since Q316 (in the ratio 54:46). Finally, WPM also announced that it had entered into an "early deposit" agreement whereby it will advance US$65m to Desert Star in return for the right to purchase 100% of the silver and gold production from Kutcho in British Columbia at 20% of the spot price of the metals over the life of the mine.

Year end	Revenue (US$m)	PBT* (US$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/15	648.7	223.6	53	20	38.9	1.0
12/16	891.6	269.8	62	21	33.3	1.0
12/17e	843.4	279.7	63	34	32.6	1.6
12/18e	951.8	395.0	89	42	23.1	2.1

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles and exceptional items.

San Dimas reaction excessive

Notwithstanding solid quarterly results, WPM's shares fell C$2.11 in the three trading days following the announcement of its results, which we attribute to the tribulations of Primero, which operates the San Dimas project and over which WPM has a streaming agreement. San Dimas will account for c 8.5% of WPM's silver equivalent production in FY17 and approximately 17.5% of EPS. We value WPM's San Dimas stream at US$959.9m, or US$2.17 per WPM share, on the basis of its long-term precious metals price assumptions or US$684.2m, or US$1.55/share, on the basis of the current spot price of silver. Including the share price declines after WPM's Q316 results in November, the stock market thus appears to be discounting the loss of substantially all the San Dimas stream to WPM despite the latter having security over the asset, which seems excessive.

Valuation: US$38.29, or C$48.00

Assuming no material purchases of additional streams (which is unlikely), we forecast a per share value for WPM of US$38.29, or C$48.00 (vs US$37.52, or C$51.25, previously) in FY20 (at average precious metals prices of US$23.98/oz Ag and US$1,362/oz Au), implying a 27.9% pa total internal rate of return for investors in US dollar terms over the next three and a half years. These valuations rise to US$44.21, C$55.42 and 32.0% in the event that Vale doubles Salobo's processing capacity within that same time frame. In the meantime, WPM's shares are trading on near-term financial ratios that are lower than those of its royalty/streaming 'peers' on 100% of financial measures considered on page 16, and the miners themselves in at least 44% of the same measures, despite being associated with materially less operating and cost risk. Additional potential upside still then exists in the form of the optionality provided by the development of major assets such as Pascua-Lama.

30 August 2017

Price	**C$25.87**
Market cap	**C$11,429m**
	C$1.2535/US$
Net debt* (US$m) at 30 June 2017 *Exdividend	876.4
Shares in issue	442.0m
Free float	100%
Code	WPM
Primary exchange	TSX
Secondary exchange	NYSE

Share price performance

%	1m	3m	12m
Abs	1.5	(6.9)	(25.9)
Rel (local)	1.8	(4.9)	(27.9)
52-week high/low		C$37.8	C$22.8

Business description

Wheaton Precious Metals is the world's pre-eminent pure precious metals streaming company, with c 30 high-quality, precious metals streaming and early deposit agreements relating to assets in Mexico, Peru, Canada, Brazil, Chile, Argentina, Sweden, Greece, Portugal, the US and Guyana.

Next events

Q3 results	October/November 2017

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Edison profile page

Wheaton Precious Metals is a research client of Edison Investment Research Limited

Investment summary

Company description: Pre-eminent precious metals streamer

Wheaton Precious Metals acquires the right to purchase streams of precious metals from producing or near-producing mines in return for a combination of a fixed upfront payment and an ongoing payment (in US$/oz). Typically, it focuses on by-product precious metals streams as this offers the greatest arbitrage opportunity between the perceived value of the stream to the producer and the perceived value of the stream to WPM. Specifically, however, it seeks to build long-term value by entering streaming agreements with large, relatively financially stable counterparties operating premium high-margin projects in the lowest quartile (and certainly the lowest half) of the cost curve.

Valuation: Base case C$48.00 in FY20

Excluding FY04, WPM's shares have historically traded on an average P/E multiple of 27.1x current year basic underlying EPS (cf 32.6x Edison or 34.7x consensus FY17e, currently). Applying this multiple to our long-term EPS forecast of US$1.41 in FY20 (at forecast precious metals prices of US$23.98/oz Ag and US$1,362/oz Au), implies a potential value for WPM shares of US$38.29, or C$48.00 in that year, which implies a 27.9% internal rate of return to investors buying Wheaton Precious shares currently at C$25.87 in US dollar terms over three and a half years.

Financials: 16.4% financial leverage

As at 30 June, WPM had US$76.6m in cash (ex-dividend) and US$953.0m of debt outstanding under its US$2bn revolving credit facility (which attracts an interest rate of Libor plus 120-220bp and matures in February 2017), such that it had net debt of US$876.4m overall, after US$124.7m (US$0.28/share) of cash inflows from operating activities during the quarter. Relative to the company's equity, this level of net debt equates to a financial gearing (net debt/equity) ratio of 19.7% and a leverage (net debt/[net debt+equity]) ratio of 16.4%. This is well within the tolerances required by WPM's banking covenants (see page 16-17). All other things being equal and assuming no further major acquisitions (which is unlikely), we estimate that WPM's net debt position will decline organically, to US$750.8m (after a payment of US$70m in respect of its Rosemont stream) by the end of FY17 (equating to gearing of 14.8% and leverage of 12.9%), and that it will be net debt free approximately midway through FY19.

Sensitivities: Metals prices ±10% changes EPS by ±22cps

Our slightly revised financial forecasts for FY18 are conducted at precious metals prices of US$21.54/oz Ag and US$1,220/oz Au and are high relative to the consensus average of 65.6c, within a range of 34-91c. As such, they almost exclusively demonstrate WPM's operational gearing to a normalisation of the silver price relative to the gold price from its current, almost unprecedented Au/Ag ratio of 75.2x to a more typical 56.6x. Note that, at current spot prices (of US$17.43/oz Ag and US$1,310/oz at the time of writing), our basic EPS forecast for FY18 is 70c.

San Dimas

We value WPM's San Dimas stream at US$959.9m, or US$2.17 per WPM share, on the basis of Edison's long-term precious metals price assumptions or US$684.2m, or US$1.55 per WPM share, on the basis of the current spot price of silver. Note that these values compare to a C$2.11 per share price decline in the value of WPM's shares since it announced its results after the market close on Thursday 10 August until the close on Tuesday 15 August, which (in addition to its falls after Q316 results in November) appears to suggest that the stock market is discounting the loss of substantially all of the San Dimas stream to WPM (ad infinitum) despite its security over the asset.

Q217

WPM's results in Q217 were closely aligned with our prior expectations (see our report, Formerly Silver Wheaton (SLW), published on 18 May 2017) and Exhibit 1, below. Production was slightly above our expectations at three assets (Penasquito, Antamina and Other Gold) and fractionally below our expectations at San Dimas, Constancia, Sudbury, Salobo and Other Silver. Otherwise, there was an 11.4%, or 0.8Moz under-sale of silver relative to production (cf 19.8%, or 1.3Moz, under-sale in Q117) and a 7.9%, 6.2koz under-sale of gold relative to production (cf a 4.2%, or 3.5koz, over-sale in Q117), resulting in a temporary build-up of ounces produced but not yet delivered as at 30 June. Note that, during the course of a year, WPM almost invariably experiences a period of inventory build, which is then, typically, 'flushed through' in the final quarter of the year. While revenues were 7.7% below our expectations for the quarter, therefore, this was almost exactly offset by a 10.6% reduction in the total cost of sales, such that earnings from operations were just 3.2%, or US$2.8m, below our published estimate, at US$82.9m. In addition, management formally changed its dividend policy, from 20% of average cash generated by operating activities to 30%, which thus allowed it to declare a relatively generous third quarter dividend of 10c/share compared with our prior expectation of 6c/share. Silver sales exceeded gold sales, in this case in the ratio 54:46, for the first time since Q316.

Exhibit 1: Wheaton Precious Metals Q217 vs Q217e and Q117*

US$000s (unless otherwise stated)	Q116	Q216	Q316	Q416	Q117	Q217e	Q217a	Chg** (%)	Diff*** (%)
Silver production (koz)	7,570	7,581	7,651	7,589	6,513	6,699	7,192	10.4	7.4
Gold production (oz)	64,942	70,249	109,193	107,332	84,863	81,458	78,127	-7.9	-4.1
AgE production (koz)	12,733	12,852	15,084	15,218	12,454	12,726	12,898	3.6	1.4
Silver sales (koz)	7,552	7,142	6,122	7,506	5,225	6,699	6,369	21.9	-4.9
Gold sales (oz)	65,258	70,757	85,063	108,931	88,397	81,458	71,965	-18.6	-11.7
AgE sales (koz)	12,759	12,451	11,913	15,249	11,412	12,726	11,625	1.9	-8.7
Avg realised Ag price (US$/oz)	14.68	17.18	19.53	16.95	17.45	17.11	17.09	-2.1	-0.1
Avg realised Au price (US$/oz)	1,175	1,267	1,336	1,205	1,208	1,248	1,263	4.6	1.2
Avg realised AgE price (US$/oz)	14.70	17.06	19.57	16.95	17.35	17.11	17.18	-1.0	0.4
Avg Ag cash cost (US$/oz)	4.14	4.46	4.51	4.59	4.54	4.50	4.51	-0.7	0.2
Avg Au cash cost (US$/oz)	389	401	390	389	391	395	393	0.5	-0.5
Avg AgE cash cost (US$/oz)	4.44	4.84	5.10	5.04	5.11	4.93	4.90	-4.1	-0.6
Sales	187,511	212,351	233,204	258,491	197,951	216,284	199,684	0.9	-7.7
Cost of sales									
Cost of sales, excluding depletion	56,636	60,208	60,776	77,617	58,291	62,322	56,981	-2.2	-8.6
Depletion	71,344	75,074	73,919	88,365	63,943	68,262	59,772	-6.5	-12.4
Total cost of sales	127,980	135,282	134,695	165,983	122,234	130,584	116,753	-4.5	-10.6
Earnings from operations	59,531	77,069	98,509	92,509	75,717	85,700	82,931	9.5	-3.2
Expenses and other income									
- General and administrative****	10,844	9,959	9,513	4,123	7,898	8,500	9,069	14.8	6.7
- Foreign exchange (gain)/loss	0	0	0	0			41	N/A	N/A
- Net interest paid/(received)	6,932	4,590	6,007	6,664	6,373	6,176	6,482	1.7	5.0
- Other (income)/expense	1,160	1,599	1,380	843	94	0	283	201.1	N/A
Total expenses and other income	18,936	16,148	16,900	11,630	14,365	14,676	15,875	10.5	8.2
Earnings before income taxes	40,595	60,921	81,609	80,879	61,352	71,024	67,056	9.3	-5.6
Income tax expense/(recovery)	(384)	615	(1,377)	(184)	128	0.0	-556	-534.4	N/A
Marginal tax rate (%)	(0.9)	1.0	(1.7)	(0.2)	0.2	0.0	-0.8	-500.0	N/A
Net earnings	40,979	60,306	82,986	81,063	61,224	71,024	67,612	10.4	-4.8
Avg no. shares in issue (000s)	402,952	436,726	440,635	440,635	441,484	441,484	441,784	0.1	0.1
Basic EPS (US$)	0.10	0.14	0.19	0.18	0.14	0.16	0.15	7.1	-6.3
Diluted EPS (US$)	0.10	0.14	0.19	0.18	0.14	0.16	0.15	7.1	-6.3

Source: Wheaton Precious Metals, Edison Investment Research. Note: *Excluding impairments; **Q217 vs Q117; ***Q217 actual vs Q217 estimate; ****forecast excluded stock-based compensation costs.

Salobo was affected by conveyor belt and plant repairs during February, as well as by lower grades. Compared to Q216, however, Salobo, Penasquito and Antamina all benefited from processing higher-grade ore in Q217, albeit Antamina's performance was tempered by a lower silver recovery. Constancia was affected by the processing of lower-grade ore, as anticipated by Hudbay, while Sudbury experienced the inevitable effects of its regular three-week scheduled maintenance for all surface operations in June as well as its Furnace #2 rebuild, which took it offline for the entirety of Q2, prior to the smelter complex transitioning to a single furnace flow sheet in Q417. Developments at San Dimas are the subject of a separate section below.

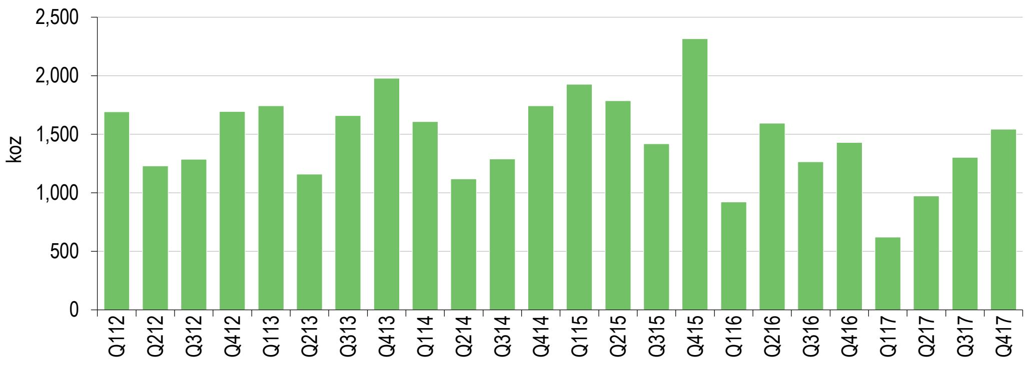
San Dimas

San Dimas produced 973koz silver attributable to WPM in Q217, compared to 623koz in Q1 and our prior expectation of 1,086koz, after the conclusion of a two-month strike in April. Operations resumed on 18 April and a phased restart of the mine began on 22 April. Subsequently, a 13-day suspension of milling activities in mid-June followed the failure of an anchor block affixed to one of eight cables supporting the tailing suspension bridge. However, mining operations continued uninterrupted during that time with ore being stockpiled at the mill site. Full plant operations resumed on 24 June and the ore stockpile was fully processed in mid-July.

Since mid-July, Primero (the operator) has reported a material deterioration in employer-employee relations to the point that it believes that labour disruptions may continue to adversely affect operations at the mine into the future.

In the aftermath of the strike, Primero's production guidance for FY17 was 4.5-5.5Moz Ag. It is maintaining this guidance, but is now erring towards the lower end of that range. This compared to WPM's guidance at the time of its FY16 results in March (see our update note published on 29 March 2017) of 4.0Moz after an assumed three-month strike (vs two months actual) and our current, relatively conservative, expectation of 4.4Moz, which assumes a return to the average quarterly production rate of 1.5Moz per quarter only in Q417.

Exhibit 2: San Dimas silver production attributable to WPM, Q112-Q417e (koz)



Source: Edison Investment Research, Wheaton Precious Metals

As such, we are forecasting that the San Dimas stream will account for 16.0% of total production attributable to WPM in FY17 and 8.5% of silver equivalent production.

Politics

In the longer term, however, Primero has opined that, despite investment, exploration at San Dimas has failed to identify any replacement for the depleting Roberta and Robertita veins and that, in the absence of suitable alternatives (or changes to the operating environment), mining rates above 1,800tpd may not be sustainable (vs nameplate capacity of 2,500tpd) – in which case it may not be able to comply with its financial obligations to lenders and its mine life may therefore become significantly shorter as a result of its consequent inability to invest in exploration and development.

As a result, it has also indicated that there is material uncertainty regarding its ability to continue as a going concern and suggested that revisions to the silver purchase agreement between it and WPM may be appropriate and/or necessary.

Further, in February 2016, Primero announced that its Mexican subsidiary had received a legal claim from the Mexican tax authorities, Servicio de Administración Tributaria (SAT), seeking to nullify the Advance Pricing Agreement issued by SAT in 2012, which confirmed Primero's ability to pay taxes in Mexico on the sale of silver at actual prices realised by its Mexican subsidiary in connection with silver sales under Primero's silver purchase agreement (SPA) with WPM for the tax years 2010-14. In the event that SAT is retroactively successful in nullifying the deal, it may seek to audit and reassess Primero's Mexican subsidiary in respect of sales of silver in connection with the Primero SPA for the tax years 2010-14 and tax Primero on such sales at higher than realised prices, as opposed to the actual prices realised under the Primero SPA. Self-evidently, this could have a material adverse effect on Primero's results of operations, financial condition and cash flows. Primero has indicated that it has notified the government of Mexico that the measures taken against it by the SAT breach several provisions of Chapter 11 of the North American Free Trade Agreement (NAFTA) and that it has the option to commence international arbitration proceedings pursuant to Article 1119 of the NAFTA.

In the short term, in the event that Primero is not able to continue to operate as a going concern, it may (i) be unable to deliver some or all of the silver ounces due from San Dimas to WPM according to its SPA, (ii) otherwise default in its obligations under the SPA, (iii) cease operations at San Dimas if it is uneconomic to continue to operate the mine and/or (iv) become insolvent.

While WPM is open to the possibility of a renegotiation of the terms of the San Dimas stream with Primero (eg to include gold as well as silver), in contrast to Primero, its position is that San Dimas is an asset that has been producing for over 150 years and that judicious budgeting and appropriately targeted exploration investment should have been able to extend the mine's life into the foreseeable future and, as such, there is no need to revise the silver purchase agreement. From a legal perspective, it regards itself as having security over the integrity of its stream in the form of San Dimas's assets (although it would not wish to operate the mine itself) and therefore regards Primero's financial tribulations as both "healthy" and "manageable" from the perspective of a free market economy philosophy. In the meantime, Primero has initiated a strategic review process. It is also known to have received a number of proposals from interested parties regarding the potential acquisition of San Dimas.

Background

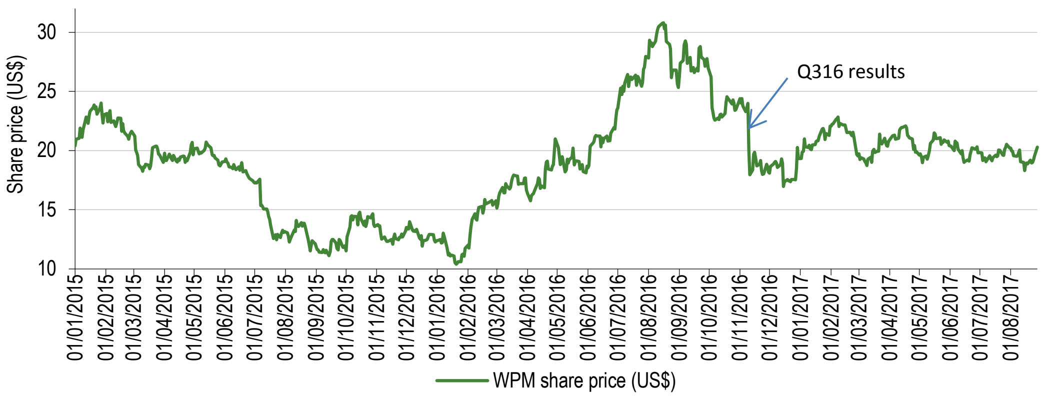
The San Dimas mine consists of three underground gold-silver operations, using primarily mechanised cut-and-fill and long-hole stoping mining methods, located in Mexico's San Dimas district, on the border of the Durango and Sinaloa states. With over 100 epithermal bonanza-type mineralised gold-silver veins, the San Dimas gold-silver deposit is one of the most significant precious metal deposits in Mexico. The veins vary in width from <1cm to over 15m, but typically average c 2m, and in strike from a few metres to more than 2km. It was first mined in 1757, with historical production from the district since then being estimated at 11Moz gold and 582Moz silver, affirming it as a world class epithermal mining district.

Goldcorp acquired San Dimas in 2002 for US$75m and, on 15 October 2004, entered into a silver purchase agreement with WPM, whereby the latter would purchase 100% of the silver produced by Goldcorp's Luismin mining operations (primarily the San Dimas and Los Filos mines) for a period of 25 years, for an upfront payment of C$46m in cash and 108m WPM shares, and an ongoing payment equal to the lesser of US$3.90/oz silver (subject to an annual inflationary price adjustment) and the then prevailing market price of silver. On 30 March, the two parties amended the Luismin silver purchase agreement, eliminating any capital expenditure contributions previously required to be paid by WPM, in consideration of which it issued 18m further shares to Goldcorp and a US$20m one-year, non-interest bearing promissory note, which was paid in full on 29 March 2007.

In August 2010, Primero (formerly known as Mala Noche Resources) acquired San Dimas from Goldcorp for US$510m in cash (US$216m), scrip (31.2m shares valued at US$184m), a US$60m convertible and a US$50m five-year note, leaving Goldcorp with a 36% share of the company. As part of the acquisition, WPM also agreed to an amended silver purchase agreement such that the term of the agreement was extended to the life of mine, in return for which Primero would deliver to WPM the first 6Moz of payable silver produced at San Dimas per annum plus 50% of any excess.

In Q116, output at San Dimas fell by 60.2%, quarter-on-quarter, to 0.9Moz attributable silver (vs 2.3Moz in Q415) as Primero reported that it had implemented new safety standards at the mine. As a result, mill throughput was limited to 1,639tpd. This recovered to above 2,500tpd in April. However the addition of ground support resulted in a modified mine plan for the remainder of 2016, with the company targeting higher-grade stopes at lower tonnages, with the result that a long-planned mill expansion to 3,000tpd was deferred. After recovering to something close to normal operating conditions in Q216, production at San Dimas was affected by high unplanned worker absences and a failure to achieve mine plans in Q316, which resulted in reduced development rates and also a number of delayed ventilation improvement projects. This, in turn, limited access to certain high-grade areas of the mine and caused Primero to revise its silver production guidance to 5.5-6.0Moz for FY16 and coincided with a US$6.04 decline in the share price of WPM in the two days immediately following the announcement of the latter's Q316 results after the market close on 9 November:

Exhibit 3: WPM share price, 1 January 2015 to present, daily (US$)



Source: Thomson Reuters Datastream

Primero's production guidance of 5.5-6.0Moz for FY16 implied output of 1.7Moz of silver during the Christmas quarter. In fact, production was 1.4Moz in Q4, after which workers called their two-month strike in mid-February (see page 4, above).

Material exceptionality

San Dimas was the fourth largest unique contributor to WPM's sales in Q217 and, arguably, should have been the third largest under normal circumstances. Prior to Q217, we forecast that San Dimas could sustainably produce 6.8Moz silver per annum attributable to WPM, which equates to 24.1% of our forecast for WPM's silver production in FY18, 15.5% of its silver equivalent (AgE) production, or 14.0% of AgE production at the currently prevailing spot price of silver. While its contribution to WPM is therefore not immaterial, in the historical context, it is worth bearing in mind that the San Dimas stream was specifically put into WPM by Goldcorp in 2004 and WPM floated as a means of showcasing the streaming business model, and that otherwise WPM would not, in the ordinary course of business, expose itself to such a material stream from an asset with such a junior operator (note: Primero's market capitalisation at the time of writing is C$22m at a share price of C$0.115/share).

Economics

On the basis of our production forecast of 6.8Moz of silver attributable to WPM per annum from San Dimas, the cash-flows associated with its stream would be those shown in Exhibit 4 (at both long-term and spot silver prices).

Exhibit 4: San Dimas cash flows to WPM, 2012-26e (US$m, unless otherwise indicated)

	Historical						Forecast								
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Production (koz)	5,905	6,542	5,760	7,449	5,212	4,442	6,828	6,828	6,828	6,828	6,828	6,828	6,828	6,828	6,828
Cash flow at LT Ag price	158.0	129.4	80.8	82.5	68.9	56.3	117.3	124.4	133.3	130.8	123.1	122.0	119.7	117.9	119.9
Cash flow at spot Ag price	158.0	129.4	80.8	82.5	68.9	56.3	89.2	88.9	88.6	88.3	88.0	87.6	87.3	87.0	86.7

Source: Edison Investment Research, Wheaton Precious Metals

Discounted at Edison's standard 10% discount rate for mining companies, these cash-flows are valued at US$959.9m, or US$2.17 per WPM share, on the basis of Edison's long-term silver price assumptions or US$684.2m, or US$1.55 per WPM share, on the basis of the current spot price of silver (US$17.43/oz at the time of writing). Note that these values compare to a C$2.11 per share price decline since WPM announced its results after the market close on Thursday 10 August until the close on Tuesday 15 August (as well as the US$6.04/share price decline at the time of WPM's Q316 results), which appears to suggest that the stock market is discounting the loss of the entire San Dimas stream to WPM despite its security over the asset.

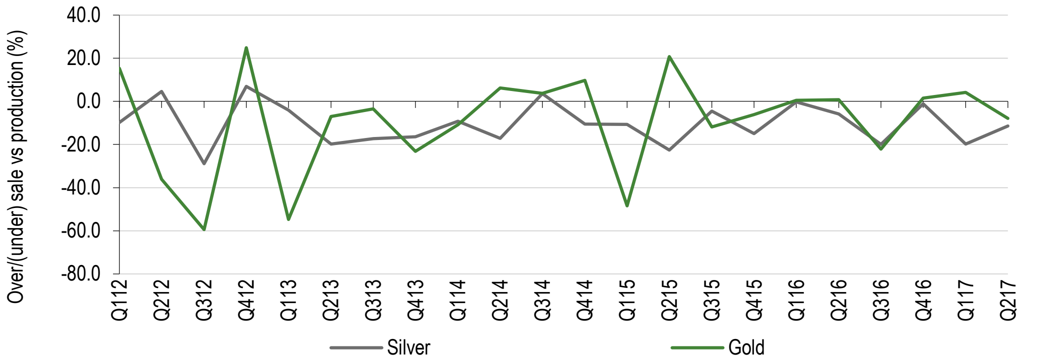
Stated alternatively, we estimate that the entire San Dimas stream is worth US$0.11 in EPS to WPM in FY17. Note that, pending further developments, we are currently forecasting a full and normal contribution from San Dimas in FY18.

On 30 March, Wheaton Precious and certain of its subsidiaries provided a guarantee to the providers of Primero's revolving credit facility (capped at a maximum of US$81.5m plus interest, fees and expenses) until November, when the RCF falls due. WPM regards this as sufficient time for Primero to work through its strategic review process and therefore expects a resolution to the situation either before, or in, November. In the meantime, US$35m in consideration of Primero's sale of its Black Fox mine will be offset against the RCF. Primero is also unable to redraw on the RCF. In return, Primero will pay a fee to Wheaton Precious of 5%, which will be recognised as a guarantee fee and allocated to 'other income'.

Ounces produced but not yet delivered – 'inventory'

Sales of silver and gold recorded 11.4% and 7.9% under-sales relative to production, in Q217, compared to long-term average under-sale rates of 10.4% and 9.3%, respectively.

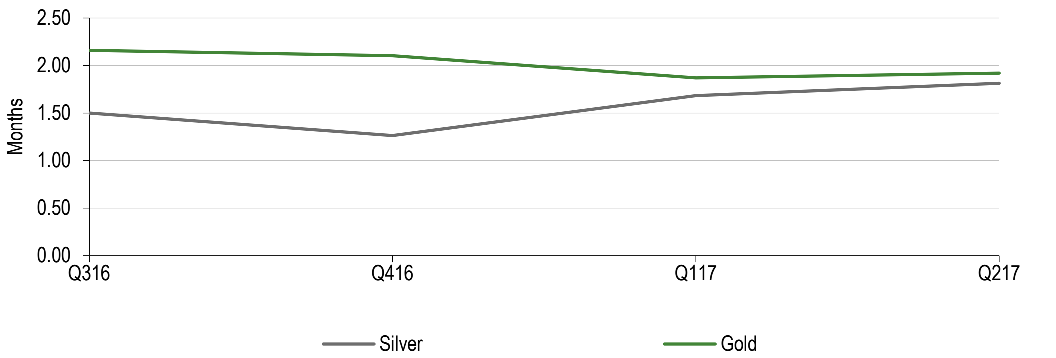
Exhibit 5: Over-/(under-) sale of silver and gold as a percentage of production, Q112-Q217



Source: Edison Investment Research, Wheaton Precious Metals

As at 30 June, payable ounces attributable to Wheaton Precious produced but not yet delivered amounted to 4.2Moz silver and 52,900oz gold (cf 3.9Moz silver and 51,500oz gold in March, 3.2Moz silver and 61,700oz gold in December and 3.8Moz silver and 63,300oz gold in September). This 'inventory' equates to 1.81 months and 1.92 months of forecast FY17 silver and gold production, respectively (cf 1.73 months and 1.85 months in Q117, 1.25 months and 2.1 months of forecast FY16 production as at end-December, and 1.5 months and 2.3 months as at end-September), or 1.88 months on a silver equivalent basis (cf 1.8 months as at end-March, 1.6 months as at end-December and 1.9 months as at end-September) – slightly below WPM's target level of two months.

Exhibit 6: WPM oz produced but not yet delivered, Q316-Q217 (months of production)



Source: Edison Investment Research, Wheaton Precious Metals

Note that, for these purposes, the use of the term 'inventory' reflects ounces produced by WPM's operating counterparties at the mines over which it has streaming agreements, but which have not yet been delivered to WPM. It in no way reflects the other, more usual use of the term in the mining industry itself, where it is typically used to refer to metal in circuit (among other things), and may therefore (under certain circumstances) be considered to be a consequence of an operation's metallurgical recoveries.

Future developments

Penasquito – According to Goldcorp, the Pyrite Leach Project (PLP) achieved construction progress of 14% and engineering progress of 94% by the end of the quarter. Concrete works remain underway, and mechanical works installation has commenced and is ramping up. Major procurement activities are now nearing completion, while material and equipment is arriving and major works contractors have mobilised to site. As such, the PLP remains on track for completion by the end of 2018 and is expected to result in additional production of 4-6Moz Ag per annum, of which WPM's share is 25% (see Exhibit 9). In addition, a carbon pre-flotation facility (dubbed the Carbon Pre-Flotation Project, or CPP) is also now being incorporated into the project, which is designed to allow Penasquito to process ore that was previously considered uneconomic (including 'significant amounts' already in stockpiles). CPP earthworks are now reported to be substantially complete and concrete works underway, while the mechanical works contractor has mobilised and will ramp up from Q317.

Rosemont – Hudbay has now completed an updated feasibility study for its Rosemont project in Arizona, according to which the mine will be a traditional open pit, truck and shovel operation with an expected 19-year mine life. Hitherto, Hudbay has indicated that a precondition for its development of Rosemont is a copper price of US$3.00/lb (cf US$3.08/lb at the time of writing). As per its announcement of 7 June, the US Forest Service (in the form of the Coronado National Forest Supervisor) has now issued the final Record of Decision for Rosemont, which is one of two key federal permits for the project to progress, along with the Section 404 Water Permit from the US Army Corps of Engineers.

Kutcho

On the same day as its Q2 results, WPM also announced that it had entered into a non-binding agreement with Desert Star regarding an "early deposit" arrangement over the Kutcho project in British Columbia. Under the terms of the agreement, WPM will advance US$65m to Desert Star in return for the right to purchase 100% of the silver and gold production from Kutcho at 20% of the spot price of the two metals until 51,000oz Au and 5.6Moz Ag have been delivered, at which point the stream will decrease to a 66.67% share for a term of the life of the mine. Of the US$65m, US$7m will be advanced to Desert Star on an "early deposit" basis, in order to fund a definitive feasibility study (DFS), environmental study & impact assessment and other related documents. Following these and receipt of permits and the onset of construction, WPM may then elect to either advance the balance to Desert Star or terminate the agreement, in which case it will be entitled to the return of the US$7m less US$1m payable on certain triggering events. Conversely, WPM will be required to make an additional payment of up to US$20m in the event that processing throughput is increased to 4,500tpd or more within five years of attaining commercial production. WPM has also agreed to participate in up to 14% of a Desert Star equity financing to a maximum of C$4.0m, where such funds are to be used for the acquisition of the Kutcho project.

Kutcho project description

The Kutcho property is located approximately 100km due east of Dease Lake in the Liard mining division of northern British Columbia. The site is located at an elevation of approximately 1,500m, has an average annual temperature of -1°C and experiences 50cm of precipitation annually, half of which is snow. The site is currently accessible via a 900m gravel airstrip located 10km from the deposit and a 100km long seasonal road from Dease Lake that is only suitable for off-road vehicles during the summer months.

The Kutcho property contains three main mineralised zones: Main, Esso and Sumac. Only the Main and Esso deposits have been used in the mine planning and economics of the PFS, the Sumac deposit being excluded owing to its resources being at an inferred level of confidence only. Esso and Main are c 1.5km apart.

The Esso deposit is located approximately 420m below surface and extends vertically for about 200m. The Main deposit has a strike length of about 1.5km while Esso has a strike length of about

600m. The deposits vary in thickness from 3-20m and have dips ranging from 30-70°. The Main deposit extends from surface to about 250m in depth.

In June 2017, a pre-feasibility study (PFS) was prepared for Desert Star by JDS Energy & Mining of Vancouver. According to the PFS, the deposits are planned to be mined predominantly by underground methods via two separate portals to the two deposits. The underground mine is envisioned to produce at an average annual rate of c 0.9Mtpa for 12 years. A small starter open pit will extract about 0.4Mt of ore from the Main deposit to provide preliminary mill feed material and non-potentially acid-generating construction material. Planned underground mining methods are sublevel, long-hole stoping for steeper dipping zones, and mechanised cut-and-fill for shallower dipping areas. Both methods will use paste backfill. Ore will be trucked from underground to the process plant, which is adjacent to the Main portal. The processing plant will operate year-round at an average rate of 2,500tpd. The processing plant will consist of primary crushing, semi-autogenous grinding, a ball mill, sequential copper and zinc flotation, concentrate de-watering, tailings disposal and back-fill production. Copper rougher product will be re-ground prior to cleaning. About one half of the total tailings will be placed underground and 1.0Mt in the mined-out open pit. Approximately 178kt Cu, 253kt Zn, 5,576koz Ag and 51koz Au will be recovered from the deposits over the mine life from an average head grade of 2.01% Cu, 3.19% Zn, 0.37g/t Au and 34.6g/t Ag. In order of economic value, payable metals found in the deposits are copper, zinc, silver and gold.

Ordinarily, we would assume that a DFS would take a year from a PFS, financing would take a further year and construction two years, such that we would anticipate Kutcho entering production in approximately 2022. Thereafter, we would expect the following cash flows to accrue to WPM over the course of the mine's initial 12-year life:

Exhibit 7: Kutcho cash flows to WPM, 2022-33e (US$m, unless otherwise indicated)

Year	FY22e	FY23e	FY24e	FY25e	FY26e	FY27e	FY28e	FY29e	FY30e	FY31e	FY32e	FY33e
Production (oz Au)	3,000	4,000	5,000	5,000	5,000	5,000	4,000	4,000	3,000	3,000	3,000	2,000
Production (koz Ag)	387	454	503	623	526	606	428	328	347	332	325	158
Cash flows to WPM (US$m)	10.1	12.2	13.9	15.9	14.4	16.2	12.0	10.2	9.3	8.9	8.7	4.8

Source: Edison Investment Research, Desert Star

When set against initial advances of US$7m in FY17 and US$58m in FY20, these cash flows yield a net present value of US$4.7m, when discounted at Edison's standard mining discount rate of 10%, and imply an internal rate of return to WPM of 11.7% in US dollar terms from FY17 to FY33 (assuming that the agreement is allowed to run its course and is not terminated).

Exceptional business plan

Wheaton Precious Metals acquires the right to purchase streams of precious metals from producing or near-producing mines in return for a combination of a fixed upfront payment (in US dollars, typically in either cash or WPM shares) and an agreed upon ongoing payment (in US$/oz). Typically, it focuses on by-product precious metals streams as this offers the greatest arbitrage opportunity between the perceived value of the stream to the producer in the equity market and the perceived value of the stream to WPM. Specifically, however, it seeks to build long-term value by entering streaming agreements with large, relatively financially stable counterparties operating premium, high-margin projects in the lowest quartile (and certainly the lowest half) of the cost curve. As well as providing comfort regarding the sustainability of the underlying operation, this strategy also helps to mitigate geopolitical and operating risks. In addition, it provides a degree of flexibility if projects are not developed according to plan (eg as evidenced by WPM's ability to successfully renegotiate a series of amendments with Barrick regarding the latter's Pascua-Lama project). Unlike a number of its peers, WPM has restricted itself solely to precious metals streaming agreements and does not participate in the base metal and oil and gas markets. This strategy has the beneficial side effect that it also exposes WPM to the traditional premium multiples afforded to precious metal companies compared to base metal ones. Notwithstanding its silver heritage, however, WPM describes itself as “agnostic” in terms of its preference for either silver or gold streams, which formed the basis of its decision to change its name from Silver Wheaton to Wheaton Precious Metals earlier this year.

Latterly, WPM has engaged in a number of “early deposit” contracts whereby it has contracted to buy gold and silver streams from the Cotabambas and Toroparu mines in South America and the Kutcho mine in British Columbia, thereby effectively becoming a relatively low-cost financing component of these projects at a time when the availability of both debt and equity financing to junior mining companies is uncertain and their associated costs relatively high.

Streaming agreement characteristics

While royalty companies compete with WPM to some extent in the provision of capital to the mining industry, there are notable differences between the two business plans. Royalties are typically linked to tenement areas, for example, and also typically relate to a mine’s primary output, whereas streaming arrangements are governed by a commercial agreement between two companies (albeit often relating to a single mine) and typically relate to a mine’s secondary, or by-product, output. A summary of the unique features of WPM’s streaming business plan and how it distinguishes itself from other investment opportunities in the mining industry is provided below.

Compared to exchange traded funds (ETFs), WPM:

- has exposure to exploration success in the form of extended mine lives;
- has exposure to levels of production;
- is operationally geared to changes in metals prices;
- balances costs and revenues, such that inventory held is minimal at the WPM level; and
- pays a dividend.

Compared to mining companies, WPM:

- has no exposure to capital cost overruns;
- has no exposure to operating cost overruns;
- is only exposed to grade fluctuations inasmuch as they affect production levels rather than margins;
- has a predetermined level of inflation applied to its own unit cash costs; and
- is unaffected by changes in a host country’s mining tax and regulatory regimes.

Compared to royalty companies, WPM:

- has geared exposure to metals prices; and
- typically negotiates and exploits the value differential around a secondary, or by-product, metal stream, rather than being applied to all metals streams including the primary one.

A key advantage for WPM compared to potential competitors is its size, scale and valuation, which allows it to raise equity on a non-dilutive basis to fund new streams, or even to issue counterparties with equity in consideration of new streams.

Cornerstone assets

WPM has five cornerstone assets (San Dimas, Penasquito, Antamina, Constancia and Salobo). The following is an analysis of the financial returns generated as a result of the application of WPM’s investment criteria to one of its cornerstone assets – Penasquito.

Penasquito

A gold-silver-lead-zinc mine, located in Mexico and operated by Goldcorp, Penasquito has consistently been regarded as one of WPM’s key cornerstone assets. The stream relating to this asset was acquired late in 2007 for US$485m plus US$3.56m in costs and US$15.761m in capitalised interest. The first silver-bearing lead and zinc concentrate was delivered from the mine in 2009 after production at its first 50,000tpd sulphide process line was ramped up on schedule and on budget. During the ramp-up period, metal recoveries, concentrate grades and concentrate quality were within expected ranges. At the same time, construction of a second 50,000tpd sulphide process line was progressing towards planned completion in Q310. After exceeding ramp-up expectations, Penasquito became WPM's second largest contributor of silver production in 2010 and, after further expansions, it finally surpassed San Dimas to become WPM's largest contributor of silver production in 2012, by which time it held the title of Mexico's largest precious metals mine, one of the world's largest and lowest-cost gold-silver mines and one of Goldcorp's most significant cash flow generators. After adjusting the mine's production schedule to reflect a targeted mill throughput rate of 110,000tpd, rising to in excess of 115,000tpd beyond 2015, Penasquito is now forecast to yield average annual production attributable to WPM of c 7Moz Ag per year plus an additional 4-6Moz pa (of which 25% will be attributable to WPM) once the Pyrite Leach Project is commissioned in FY19.

Compared to an initial investment of US$504.3m, Penasquito has yielded the following historical and forecast cash flows to WPM:

Exhibit 8: Penasquito cash flows to WPM, 2008-26e (US$m)

	Historical									Forecast									
Year	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Cash flow	2.3	6.9	52.2	126.8	162.2	105.2	106.0	85.1	54.1	65.7	121.2	140.1	162.3	159.3	150.1	148.7	145.9	143.8	146.1

Source: Edison Investment Research, Wheaton Precious Metals

On an undiscounted basis, therefore, Penasquito paid back WPM's initial investment in 2014. When discounted at Edison's standard mining discount rate of 10%, the mine has already returned US$410.7m to WPM (as at end FY16) in 2007 money terms and is also worth a residual US$821.3m in 2017 money terms. Applying a 10% discount/hurdle rate, payback is indicated in H119 in 2007 money terms.

By contrast, applying a 10% discount/hurdle rate over the entire stream of income yields an ultimate value of US$759.0m, which is directly comparable to the stream's acquisition cost of US$504.3m in 2007 money terms. Stated alternatively, the stream will provide WPM with an internal rate of return of 15.2% from the point of acquisition in 2007 to 2026. In addition, there is substantial underground potential beneath the current open pits, providing excellent opportunities for further exploration growth and expanded and/or extended silver production.

WPM's assets

As at Q216, WPM has agreements over more than 20 major metals streams, summarised in Exhibit 9 below.

Exhibit 9: WPM precious metals streaming and early deposit agreements

Asset	Owner/operator	Location	Attributable production to be purchased (%)		Per ounce cash payment* (US$/oz)		Term of agreement	Date of original contract
			Silver	Gold	Silver	Gold		
San Dimas	Primero	Mexico	6.0Moz + 50% of excess	0	4.28		Life of mine	Oct 2004
Yauliyacu**	Glencore	Peru	1.5Moz + 50% of excess	0	8.74		Life of mine	Mar 2006
Penasquito	Goldcorp	Mexico	25	0	4.13		Life of mine	Jul 2007
Salobo	Vale	Brazil	0	75		400	Life of mine	Feb 2013
Sudbury	Vale	Canada	0	70		400	20 years	Feb 2013
Antamina***	Glencore	Peru	33.75/22.5	0	20% of spot		Life of mine	Nov 2015
Barrick								
■ Pascua-Lama	Barrick	Chile/Argentina	25	0	3.90		Life of mine	Sep 2009
■ Lagunas Norte	Barrick	Peru	100	0	3.90		8.5 years	Sep 2009
■ Pierina	Barrick	Peru	100	0	3.90		8.5 years	Sep 2009
■ Veladero	Barrick	Argentina	100	0	3.90		8.5 years	Sep 2009
Other								
Los Filos	Goldcorp	Mexico	100	0	4.29		25 years	Oct 2004
Zinkgruvan	Lundin	Sweden	100	0	4.27		Life of mine	Dec 2004
Stratoni	Eldorado	Greece	100	0	4.18		Life of mine	Apr 2007
Minto	Capstone	Canada	100	100	4.14	318	Life of mine	Nov 2008
Neves-Corvo	Lundin	Portugal	100	0	4.18		50 years	Jun 2007
Aljustrel	I'M SGPS	Portugal	100	0	4.06		50 years	Jun 2007
Keno Hill	Alexco	Canada	25	0	3.90		Life of mine	Oct 2008
Rosemont	Hudbay	US	100	100	3.90	450	Life of mine	Feb 2010
Loma de La Plata (Navidad)	Pan American	Argentina	12.5	0	4.00		Life of mine	Not finalised
777	Hudbay	Canada	100	50	6.02	408	Life of mine	Aug 2012
Constancia	Hudbay	Peru	100	50	5.90	400	Life of mine	Aug 2012
Early deposit								
Toroparu	Sandspring	Guyana	50	10	3.90	400	Life of mine	Nov 2013
Cotabambas	Panoro	Peru	100	25	5.90	450	Life of mine	Mar 2016
Kutcho	Desert Star	Canada	100****	100****	20% of spot	20% of spot	Life of mine	Aug 2017

Source: Wheaton Precious Metals, Edison Investment Research. Note: *As at 31 December 2016; subject to an annual inflationary adjustment with the exception of Loma de La Plata and Sudbury. **In Q415, WPM amended its silver purchase agreement with Glencore at Yauliyacu, such that the term of the agreement, which was set to expire in 2026, was extended to the life of mine; in addition, with effect from 1 January 2016, Glencore was obliged to deliver to WPM a per annum amount equal to the first 1.5Moz of payable silver produced at Yauliyacu plus 50% of any excess at a price that was increased by US$4.50/oz from the original agreement plus, if the market price of silver exceeds US$20/oz, 50% of the excess, to a maximum of US$10/oz. ***WPM is entitled to 33.75% of silver production at Antamina until 140Moz have been delivered and 22.5% thereafter, for a 50-year term that can be extended in increments of 10 years at the company's discretion. ****See Kutcho section on page 9, above.

Market potential

WPM is effectively exposed to two different types of market within the mining industry – that of 'balance sheet repair' and that of 'development'. Over the course of the past three years, the majority of new business offered to WPM has been of the former type. In this respect, WPM estimates the size of the potential market open to it to be at least the 70% of the c 870Moz of silver production in FY16 that was produced as a by-product of either gold or base metals mines (ie approximately 609Moz silver per annum). This compares with WPM's production in FY16 of 30.4Moz Ag – ie WPM estimates that, to date, it has penetrated less than c 5.0% of its potential market.

Recently, however, WPM has observed a shift in the type of business that is being brought to it, from 'balance sheet repair' towards 'development' (eg Kutcho). Typically, these opportunities are smaller than 'balance sheet repair' type opportunities (eg in the range US$100-400m), but more numerous (WPM estimates that it has seen 150 such opportunities over the course of the past three to four years, of which it has concluded deals over three).

FY17 by quarter

Production

Official management guidance is for silver production of 28Moz and gold production of 340,000oz in FY17. This compares with our (marginally) updated forecasts of 27.8Moz silver and 330,500oz gold, respectively, ie our forecasts are relatively conservative. Over the next five years (including 2017), WPM is estimating average annual silver production of approximately 29Moz and gold production of 340,000oz.

General & administrative

WPM continues to expect non-stock general and administrative expenses in the range of US$33-35m for the full year – ie c US$8.5m per quarter – including additional legal costs relating to its dispute with the Canadian Revenue Agency. Investors should note that our financial forecasts in Exhibits 10 and 13 specifically exclude stock-based compensation costs.

Financial

In light of the above factors, our revised quarterly operational and financial forecasts for WPM for the remainder of FY17 are as follows:

Exhibit 10: Wheaton Precious FY17 forecast, by quarter

US$000s (unless otherwise stated)	Q117	Q217	Q317e	Q417e	FY17e (old)	FY17e (new)
Silver production (koz)	6,513	7,192	6,916	7,156	27,285	27,778
Gold production (oz)	84,863	78,127	83,765	83,765	333,852	330,521
AgE production (koz)	12,454	12,898	13,289	13,518	51,555	49,840
Silver sales (koz)	5,225	6,369	6,916	7,156	25,997	25,667
Gold sales (oz)	88,397	71,965	83,765	83,765	337,386	327,893
AgE sales (koz)	11,412	11,625	13,289	13,518	50,512	49,840
Avg realised Ag price (US$/oz)	17.45	17.09	16.55	16.71	17.00	16.91
Avg realised Au price (US$/oz)	1,208	1,263	1,259	1,269	1,238	1,249
Avg realised AgE price (US$/oz)	17.35	17.18	16.55	16.71	17.02	16.92
Avg Ag cash cost (US$/oz)	4.54	4.51	4.52	4.52	4.50	4.52
Avg Au cash cost (US$/oz)	391	393	395	395	394	394
Avg AgE cash cost (US$/oz)	5.11	4.90	4.84	4.84	4.95	4.92
Sales	197,951	199,684	219,927	225,882	859,596	843,444
Cost of sales						
Cost of sales, excluding depletion	58,291	56,981	64,346	65,432	249,918	245,051
Depletion	63,943	59,772	67,902	68,253	273,263	259,869
Total cost of sales	122,234	116,753	132,249	133,685	523,181	504,920
Earnings from operations	75,717	82,931	87,679	92,198	336,415	338,524
Expenses and other income						
- General and administrative*	7,898	9,069	8,500	8,500	33,398	33,967
- Foreign exchange (gain)/loss		41			0	41
- Net interest paid/(received)	6,373	6,482	6,023	6,023	24,901	24,901
- Other (income)/expense	94	283	0	0	94	377
Total expenses and other income	14,365	15,875	14,523	14,523	58,393	59,286
Earnings before income taxes	61,352	67,056	73,156	77,675	278,022	279,238
Income tax expense/(recovery)	128	-556	0	0	128	-428
Marginal tax rate (%)	0.2	-0.8	0.0	0.0	0.0	-0.2
Net earnings	61,224	67,612	73,156	77,675	277,894	279,666
Avg no. shares in issue (000s)	441,484	441,784	441,484	441,484	441,484	441,709
Basic EPS (US$)	0.14	0.15	0.17	0.18	0.63	0.63
Diluted EPS (US$)	0.14	0.15	0.17	0.18	0.63	0.63

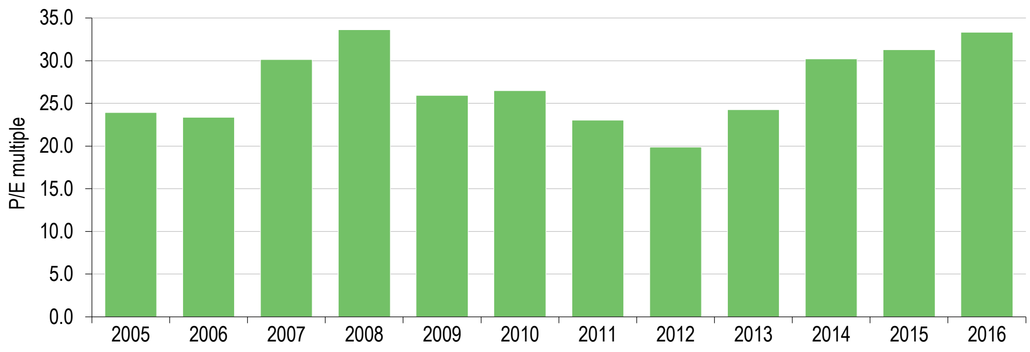
Source: Wheaton Precious Metals, Edison Investment Research. Note: *Forecasts exclude stock-based compensation costs.

Compared with our previous forecast for FY17, production is unchanged, the silver price has been revised down fractionally for Q317 and the gold price up fractionally. In the aftermath of these revisions, our updated basic EPS estimate of 63c for FY17 remains unchanged. It compares to an average consensus estimate (source: Bloomberg, 30 August 2017) of 59.5c within a range of 51-67c. Note that our FY17 basic EPS estimate rises to 66c in the event that precious metals' prices remain at current levels (viz US$17.43/oz Ag and US$1,310/oz Au).

Valuation

Excluding FY04 (part year), WPM's shares have historically traded on an average P/E multiple of 27.1x current year basic underlying EPS – ie excluding impairments (cf 32.6x Edison or 34.7x consensus FY17e, currently – see Exhibit 12).

Exhibit 11: WPM's historic current year P/E multiples



Source: Edison Investment Research. Note: FY14 EPS excludes impairment charge.

Applying this multiple to our long-term EPS forecast of US$1.41 in FY20 (at Edison's average long-term precious metals prices of US$23.98/oz Ag and US$1,362/oz Au in FY20) implies a potential share value for WPM shares of US$38.29, or C$48.00 in that year (cf US$37.52, or C$51.25, at the time of our last note in May 2017).

In the meantime, from a relative perspective, it is notable that WPM is cheaper than its royalty/streaming 'peers' in 100% of the valuation measures used in Exhibit 12 and on multiples that are cheaper than the miners themselves in at least 44% of the same valuation measures, despite being associated with materially less operational and cost risk, in particular.

Exhibit 12: Wheaton Precious valuation cf a sample of major operating and royalty/streaming companies

	P/E (x)		Yield (%)		P/CF (x)	
	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2
Royalty companies						
Franco-Nevada	81.7	73.8	1.1	1.1	31.7	30.0
Royal Gold	51.8	43.2	1.0	1.1	20.2	18.6
Sandstorm Gold	93.5	89.9	0.0	0.0	17.8	19.5
Osisko Gold Royalties	59.5	48.9	1.0	1.1	30.6	23.2
Average	**71.6**	**63.9**	**0.8**	**0.8**	**25.1**	**22.8**
Wheaton Precious (Edison forecasts)	**32.6**	**23.1**	**1.6**	**2.1**	**16.7**	**14.0**
WPM (consensus)	**34.7**	**31.5**	**1.4**	**1.6**	**16.8**	**15.4**
Gold producers						
Barrick	23.8	23.4	0.7	0.7	7.6	7.8
Newmont	28.9	31.4	0.7	0.8	3.1	3.1
Goldcorp	33.6	28.4	0.6	0.6	9.6	8.4
Newcrest	30.5	20.7	1.0	1.4	10.9	9.6
Kinross	47.3	39.6	0.0	0.0	5.9	5.4
Agnico-Eagle	67.4	59.9	0.8	0.8	15.1	14.8
Eldorado	37.7	13.4	0.9	0.3	12.0	5.8
Yamana	87.3	22.7	0.7	0.7	5.8	3.9
Randgold Resources	31.1	26.0	1.9	2.3	18.5	16.1
Average	**43.1**	**29.5**	**0.8**	**0.8**	**9.8**	**8.3**
Silver producers						
Hecla	74.1	22.6	0.2	0.2	12.6	8.1
Pan American	34.1	23.5	0.5	0.6	13.4	10.0
Coeur Mining	53.7	19.7	0.0	0.0	9.2	6.9
First Majestic	201.2	31.5	0.0	0.0	13.6	8.9
Hocschild	39.8	21.6	1.2	1.6	7.7	5.9
Fresnillo	32.9	26.9	1.4	1.7	19.2	15.1
Average	**72.6**	**24.3**	**0.5**	**0.7**	**12.6**	**9.2**

Source: Bloomberg, Edison Investment Research. Note: Edison WPM FY18 forecasts assume precious metals prices of US$21.54/oz Ag and US$1,220/oz Au. Priced on 30 August 2017.

Sensitivities

Currently, we make no provision for either future expansion at Salobo or related expansion payments in our long-term forecasts. However, in the event that Salobo were to be expanded from 24Mtpa to 48Mtpa by the addition of a further two 12Mtpa processing lines by 1 January 2021 – thereby attracting the maximum incremental payment from WPM to Vale – we estimate that it would increase our estimate of WPM's earnings in FY20 by a material US$0.22/share. This, in turn, would increase our forecast value per share for the company to US$44.21, or C$55.42 at prevailing FX rates (compared with US$43.31, C$59.16 previously), implying an internal rate of return to investors buying WPM shares currently at C$25.87, equivalent to 32.0% pa in US dollar terms over three and a half years.

Please see separate section on pages 4-7 for financial and valuation sensitivities specifically relating to the San Dimas mine.

Financials

As at 30 June, WPM had US$76.6m in cash (ex-dividend) and US$953.0m of debt outstanding under its US$2bn revolving credit facility (which attracts an interest rate of Libor plus 120-220bp and matures in February 2017), such that it had net debt of US$876.4m overall, after US$124.7m (US$0.28/share) of cash inflows from operating activities during the quarter. Relative to the company's equity, this level of net debt equates to a financial gearing (net debt/equity) ratio of 19.7% and a leverage (net debt/[net debt+equity]) ratio of 16.4%. It also compares with a net debt position of US$980.2m as at 31 March, US$1,068.7m as at the end of December 2016, US$1,219.5m as at the end of September 2016 and US$1,362.7m as at the end of December 2015 and is consistent with WPM continuing to generate c US$100-150m per quarter from operating activities before financing and investing activities. Otherwise, assuming the operational performance set out in Exhibit 10, we estimate that WPM's net debt position will decline organically, to US$750.8m by the end of FY17 (equating to gearing of 14.8% and leverage of 12.9%), and that WPM will be net debt free approximately midway through FY19, all other things being equal and contingent on its making no further major acquisitions (which is unlikely). Self-evidently, such a level of debt is well within the tolerances required by its banking covenants that:

- net debt should be no more than 0.75x tangible net worth (which was US$5,030.7m as at end-June 2017 and which we forecast to be US$5,071.3m as at end-December 2017); and
- interest should be no less than 3x covered by EBITDA (we estimate that net interest will be 22.7x covered in FY17).

Note that the C$191.7m letter of guarantee that WPM has posted re 50% of the disputed taxes relating to its dispute with the Canadian Revenue Agency (CRA) (see below) has been determined under a separate agreement and is therefore specifically excluded from calculations regarding WPM's banking covenants.

CRA

There have been no further substantive developments regarding WPM's dispute with the CRA since our update note of 15 February 2016.

WPM notes that the CRA's position is that the transfer pricing provisions of the Income Tax Act (Canada) in relation to income earned by WPM's foreign subsidiaries should apply "such that the income of Silver Wheaton [*sic*] subject to tax in Canada should be increased by an amount equal to substantially all of the income earned outside of Canada by the company's foreign subsidiaries for the 2005-2010 taxation years". Should this interpretation be upheld, we would expect it to have potentially profound consequences for Canada's status as a supplier of finance and capital to overseas destinations in general (ie not just to the mining industry).

Earlier this year, WPM's CEO, Randy Smallwood, was quoted as saying that the company is willing to settle its tax dispute with the CRA via a payment of C$5-10m "with gritted teeth", but still believes no payment should be required. As such, the C$5-10m quoted reflects no admission or error, but rather an appreciation of the costs involved in going to a full trial and also of the effect that the issue is having on WPM's share price rating relative to its peers (see Exhibit 12).

In the meantime, Wheaton Precious is approximately halfway through the case 'discovery process' with the CRA, designed to provide both sides with the opportunity to arrive at an out-of-court settlement before formal proceedings commence. This discovery process is likely to last until the end of the year and any potential out-of-court settlement would therefore be likely to occur shortly after this date. Otherwise, however, the company has stated that it is willing to go to trial if a 'principled' settlement is not possible (which is likely to be towards the middle of 2018).

Exhibit 13: Financial summary

US$'000s	2012	2013	2014	2015	2016	2017e	2018e
Dec	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue	849,560	706,472	620,176	648,687	891,557	843,444	951,821
Cost of Sales	(117,489)	(139,352)	(151,097)	(190,214)	(254,434)	(245,051)	(249,386)
Gross Profit	732,071	567,120	469,079	458,473	637,123	598,394	702,435
EBITDA	701,232	531,812	431,219	426,236	602,684	564,427	668,468
Operating Profit (before amort. and except.)	600,003	387,659	271,039	227,655	293,982	304,557	412,496
Intangible Amortisation	0	0	0	0	0	0	0
Exceptionals	0	0	(68,151)	(384,922)	(71,000)	0	0
Other	788	(11,202)	(1,830)	(4,076)	(4,982)	(418)	0
Operating Profit	600,791	376,457	201,058	(161,343)	218,000	304,139	412,496
Net Interest	0	(6,083)	(2,277)	(4,090)	(24,193)	(24,901)	(17,493)
Profit Before Tax (norm)	600,003	381,576	268,762	223,565	269,789	279,656	395,003
Profit Before Tax (FRS 3)	600,791	370,374	198,781	(165,433)	193,807	279,238	395,003
Tax	(14,755)	5,121	1,045	3,391	1,330	428	0
Profit After Tax (norm)	586,036	375,495	267,977	222,880	266,137	279,666	395,003
Profit After Tax (FRS 3)	586,036	375,495	199,826	(162,042)	195,137	279,666	395,003
Average Number of Shares Outstanding (m)	353.9	355.6	359.4	395.8	430.5	441.7	441.8
EPS - normalised (c)	166	106	75	53	62	63	89
EPS - normalised and fully diluted (c)	165	105	74	53	62	63	89
EPS - (IFRS) (c)	166	106	56	(-41)	45	63	89
Dividend per share (c)	35	45	26	20	21	34	42
Gross Margin (%)	86.2	80.3	75.6	70.7	71.5	70.9	73.8
EBITDA Margin (%)	82.5	75.3	69.5	65.7	67.6	66.9	70.2
Operating Margin (before GW and except.) (%)	70.6	54.9	43.7	35.1	33.0	36.1	43.3
BALANCE SHEET							
Fixed Assets	2,403,958	4,288,557	4,309,270	5,526,335	6,025,227	5,844,358	5,660,385
Intangible Assets	2,281,234	4,242,086	4,270,971	5,494,244	5,948,443	5,767,574	5,583,601
Tangible Assets	1,347	5,670	5,427	12,315	12,163	12,163	12,163
Investments	121,377	40,801	32,872	19,776	64,621	64,621	64,621
Current Assets	785,379	101,287	338,493	105,876	128,092	446,071	838,124
Stocks	966	845	26,263	1,455	1,481	1,514	1,709
Debtors	6,197	4,619	4,132	1,124	2,316	2,311	2,608
Cash	778,216	95,823	308,098	103,297	124,295	442,246	833,807
Other	0	0	0	0	0	0	0
Current Liabilities	(49,458)	(21,134)	(16,171)	(12,568)	(19,057)	(24,397)	(24,825)
Creditors	(20,898)	(21,134)	(16,171)	(12,568)	(19,057)	(24,397)	(24,825)
Short term borrowings	(28,560)	0	0	0	0	0	0
Long Term Liabilities	(32,805)	(1,002,164)	(1,002,856)	(1,468,908)	(1,194,274)	(1,194,702)	(1,194,702)
Long term borrowings	(21,500)	(998,136)	(998,518)	(1,466,000)	(1,193,000)	(1,193,000)	(1,193,000)
Other long term liabilities	(11,305)	(4,028)	(4,338)	(2,908)	(1,274)	(1,702)	(1,702)
Net Assets	3,107,074	3,366,546	3,628,736	4,150,735	4,939,988	5,071,330	5,278,982
CASH FLOW							
Operating Cash Flow	720,209	540,597	434,582	435,783	608,503	569,321	668,404
Net Interest	0	(6,083)	(2,277)	(4,090)	(24,193)	(24,901)	(17,493)
Tax	(725)	(154)	(204)	(208)	28	856	0
Capex	(641,976)	(2,050,681)	(146,249)	(1,791,275)	(805,472)	(79,000)	(72,000)
Acquisitions/disposals	0	0	0	0	0	0	0
Financing	12,919	58,004	6,819	761,824	595,140	0	0
Dividends	(123,852)	(160,013)	(79,775)	(68,593)	(78,708)	(148,325)	(187,351)
Net Cash Flow	(33,425)	(1,618,330)	212,896	(666,559)	295,298	317,951	391,561
Opening net debt/(cash)	(761,581)	(728,156)	902,313	690,420	1,362,703	1,068,705	750,754
HP finance leases initiated	0	0	0	0	0	0	0
Other	0	(12,139)	(1,003)	(5,724)	(1,300)	0	0
Closing net debt/(cash)	(728,156)	902,313	690,420	1,362,703	1,068,705	750,754	359,193

Source: Company sources, Edison Investment Research

EDISON

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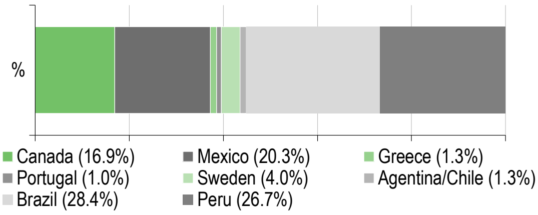
Revenue by geography



Management team

President and chief executive officer: Randy Smallwood

Mr Smallwood holds a geological engineering degree from the University of British Columbia and is one of the founding members of WPM. Before joining the original Wheaton River group in 1993 as an exploration geologist, he worked for Homestake, Teck and Westmin Resources. In 2007, he joined WPM full time as executive vice president of corporate development, before being appointed president in January 2010 and CEO in April 2011.

Gary Brown: Senior vice president and chief financial officer

Mr Brown brings almost 25 years of experience as a finance professional to WPM and holds professional designations as a chartered accountant and a chartered financial analyst, as well as having earned a Master's degree in accounting from the University of Waterloo. Prior to joining WPM in 2008, he was the chief financial officer of TIR Systems. He is a director of Redzone Resources and has held senior finance roles with CAE Inc, Westcoast Energy, and Creo Inc among others.

Chairman: Douglas Holtby

Mr Holtby is the vice chairman of the board and lead director of Goldcorp. He is also a director of the BC Cancer Foundation and president and CEO of Holtby Capital Corporation, a private investment company. He has a long history of serving in a variety of senior board positions since 1982, including, among others, WIC Western International Communications, Canadian Satellite Communications Inc and Allarcom. He is a fellow chartered accountant and a graduate of the Institute of Corporate Directors – Director Education Program at the University of Toronto, Rotman School of Management.

Senior vice president, corporate development: Haytham Hodaly

Mr Hodaly is an engineer with a BASc in mining and mineral processing engineering and a Master's in engineering, specialising in mineral economics. He brings over 16 years of experience in the North American securities industry to WPM. Prior to joining WPM, he was a director at RBC Capital Markets with responsibility for global mining research and before that, he was co-director of research and senior mining analyst at Salman Partners Inc. During his tenure, he helped to establish Salman Partners as a leading independent, resource-focused and research-driven investment dealer.

Principal shareholders	(%)
Franklin Resources	10.19
BlackRock	9.89
VanEck Associates	6.17
Carmignac Gestion	3.02
Vanguard Group	2.35
FMR LLC	2.20
Toronto-Dominion Bank	1.51

Companies named in this report

Franco-Nevada (FNV), Royal Gold (RGLD), Sandstorm Gold (SSL), Osisko Gold Royalties (OR), Barrick (ABX), Newmont (NEM), Goldcorp (G), Newcrest (NCM), Kinross (K), Agnico-Eagle (AEM), Eldorado (ELD), Yamana (YRI), Randgold Resources (RRS), Hecla (HL), Pan American (PAAS), Coeur (CDE), First Majestic (FR), Hocschild (HOC), Fresnillo (FRES), Desert Star, Primero (P).