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Royal Gold, Inc. NasdaqGS:RGLD

Earnings Call

Thursday, August 3, 2023 5:00 PM GMT

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Call Participants

EXECUTIVES

Alistair Baker
Vice President of Investor Relations & Business Development

Martin Raffield
Vice President of Operations

Paul K. Libner
CFO & Treasurer

William H. Heissenbuttel
President, CEO & Director

ANALYSTS

Cosmos Chiu
CIBC Capital Markets, Research Division

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Presentation

Operator

Hello, and welcome to the Royal Gold's 2023 Second Quarter Conference Call. My name is Elliot, and I'll be coordinating your call today. [Operator Instructions]

I would now like to hand over to Alistair Baker, Vice President, Investor Relations and Business Development. The floor is yours. Please go ahead.

Alistair Baker
Vice President of Investor Relations & Business Development

Thanks, Elliot. Good morning, and welcome to our discussion of Royal Gold's Second Quarter 2023 Results. This event is being webcast live, and you will be able to access a replay of this call on our website. Speaking on the call today are Bill Heissenbuttel, President and CEO; Martin Raffield, Vice President of Operations; and Paul Libner, CFO and Treasurer; Randy Shefman, General Counsel; and Dan Breeze, Vice President, Corporate Development of RG AG are also available for questions.

During today's call, we will make forward-looking statements, including statements about our projections and expectations for the future. These statements are subject to risks and uncertainties that could cause actual results to differ materially from these statements. These risks and uncertainties are discussed in yesterday's press release and our filings with the SEC. We'll also refer to certain non-GAAP financial measures, including adjusted net income and adjusted net income per share. Reconciliations of adjusted net income and adjusted net income per share to the most directly comparable GAAP measures are available in yesterday's press release, which can be found on our website.

Bill will start with a review of the quarter. Martin will give some commentary on the portfolio, and Paul will wrap up with a financial summary. After the formal remarks, we'll open the lines for a Q&A session. I'll now turn the call over to Bill.

William H. Heissenbuttel
President, CEO & Director

Good morning, and thank you for joining the call. I'll begin on Slide 4. Our second quarter was relatively steady, and we provided solid financial results.

Revenue was $144 million for the quarter, and operating cash flow was strong at $108 million. Earnings were $63 million or $0.97 per share. After adjustments, adjusted earnings were $0.88 per share. We continued our practice of returning capital to shareholders and made a dividend payment of $1.50 per share for the quarter. We also maintained our focus on the balance sheet and repaid $100 million of the outstanding balance on the revolver, leaving us with liquidity at the end of the quarter of just over $700 million.

With respect to the revolver, we completed an amendment to extend the maturity for another two years to June 2028. The source of capital has been a key strategic financing tool that has allowed us to finance our growth over the past several years without issuing equity.

Despite a market in which some companies have seen lenders exit credit facilities, sometimes requiring a reduction in the size of those credit facilities, I'm pleased to report that all of our lenders continue their participation in our revolving credit. The significant support of our commercial banking partners is very much appreciated.

With respect to potential new business during the quarter, we announced the signing of a commitment letter to acquire precious and base metal royalties for $250 million on the producing Serrote and Santa Rita mines in Brazil as part of the acquisition financing of the mines by ACG Electric Metals. This potential acquisition is subject to a number of closing conditions, including negotiation and execution of definitive

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documentation and the closing of ACG's acquisition of the mines from Appian Capital. The conditions have not yet been satisfied, and there are no other details we can provide on the transaction at this time.

I'll now turn the call over to Martin to provide some comments on the portfolio.

Martin Raffield
Vice President of Operations

Thank you, Bill. Turning to Slide 5, I'll give some comments on the second quarter revenue. Overall revenue for the quarter was $144 million with a volume of 73,000 GEOs. Our Royalty segment contributed revenue of $38 million, down from $42 million in the prior year quarter.

While we saw higher revenue from the Cortez Legacy Zone and new revenue from the Cortez CC Zone and King of the Hills royalties, the increase was more than offset by lower revenue from Penasquito and Voisey's Bay. At Penasquito, operations were suspended in early June due to a labor dispute and at Voisey's Bay, production was impacted due to a maintenance shutdown from May to July at the Long Harbour processing plant and the transition from the Ovoid open pit mine to the new underground operations.

Our stream segment revenue was $106 million, up slightly from the prior year quarter. The largest variances were due to higher revenue from Pueblo Viejo and Khoemacau and lower revenue from both Mount Milligan and Andacollo. Khoemacau continued to operate at the target throughput rate of 10,000 tonnes per day for the second consecutive quarter after completing the ramp-up and reaching nameplate capacity in December last year.

I'll now turn to Slide 6 and give some comments on notable developments at the operations. At Mount Milligan, Centerra reported that mining of the ore waste transition zone is now mostly complete, and they are on track to access the higher-grade copper and gold from Phases 7 and 9 in the second half of the year. For the full year 2023, Centerra expects gold production to trend near the low end of its 160,000 to 170,000 ounce guidance range and copper production towards the midpoint of its 60 million to 70 million pound guidance range. Recall that we typically see a 5- to 6-month lag between production at the mine and stream sales, so we won't see the benefit of the stronger second half production until sometime in the first half of 2024.

At Pueblo Viejo, I visited the site in late June to get an update on the expansion process and the status of the issues related to silver recovery. I was impressed with the progress overall and several components of the expansion have already been commissioned. Silver recovery has remained an issue, and I think it's fair to say that Barrick's focus has been on maintaining gold production while completing the expansion rather than optimizing silver production. However, I came away feeling comfortable that Barrick understands the issues with silver recovery, and they have a strategy to address those issues as the expansion commissioning progresses.

Silver is an important driver of overall all-in sustaining costs at Pueblo Viejo, and there are other stakeholders who also want to see the silver recovery improve. Barrick expects that silver recovery will improve during the third quarter and reach target rates during the fourth quarter. That said, there was a further deferral of silver deliveries of 89,000 ounces during the quarter, and the total deferred amount was 608,000 ounces at the end of June. We don't expect any material deliveries of deferred ounces for the remainder of the year while the expansion is commissioned and ramps up to full production levels. And we expect it will take several quarters to deliver the entire deferred amount after the plant is running at full capacity.

Finally, at Penasquito, Newmont reported in mid-July that operations remain suspended after strike action was taken by the National Union of Mine and Metal Workers on June 7. Newmont is working to resolve the dispute, but has not provided an estimate as to when operations could restart, and they have withdrawn 2023 guidance for Penasquito.

At this point, we are maintaining our total sales guidance of 320,000 to 345,000 GEOs for 2023. However, if there are no other unforeseen events at our producing properties and operations at Penasquito remain

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suspended through the remainder of 2023, total GEO sales may come in around the low end of the guidance range. Note also that our 2023 guidance does not include any impact from potential acquisitions.

I'll now turn the call over to Paul for a review of our financial results.

Paul K. Libner
CFO & Treasurer

Thanks, Martin. I'll now turn to Slide 7 and give an overview of the financial results for the quarter. For this discussion, I'll be comparing the quarter ended June 30, 2023, to the prior quarter.

Revenue was $144 million for the quarter, which was in line with the prior year. The main drivers of the variance in our revenue this quarter were lower sales at Andacollo, the impacts from the strike at Penasquito and a shutdown of the Long Harbour processing plant at Voisey's Bay. The downward impacts to our revenue this quarter from Penasquito and Voisey's Bay were partially offset by new revenue of approximately $6 million from the additional Cortez royalty interest we acquired during the second half of 2022.

With respect to metal prices and compared to the prior year quarter, the price of gold was up by 6%, silver was up 7% and copper was down 11%. Gold remains the dominant revenue source making up 77% of our total revenue, followed by silver at 15% and copper at 6%.

Turning now to Slide 8. G&A expense was in line with the prior year quarter at $9 million. Although inflationary pressures continue to have some impact on others within the metals and mining sector, our cash G&A costs have remained low or less than 5% of total revenue.

Our DD&A expense decreased to $38 million from $44 million in the prior year quarter. On a unit basis, this expense was $527 per GEO for the quarter compared to $562 per GEO in the prior year period. The DD&A rate on a unit basis declined in the current quarter due to lower depletion rates at Mount Milligan and Pueblo Viejo, which were the result of reserve additions at the end of 2022.

The decrease was partially offset by increased depletion expense at Cortez due to the newly acquired royalty interest and additional depletion expense at Khoemacau, which was a result of higher silver sales due to the continued ramp up when compared to the prior year quarter. We continue to expect DD&A for the full year to be in the range of $490 to $540 per GEO.

Interest expense increased to $8.4 million for the quarter from $1.4 million in the prior period. The increase was due to higher average amounts outstanding under our revolving credit facility when compared to the prior period. The all-in interest rate for borrowings under our credit facility was 6.7% at the end of the second quarter.

Tax expense for the quarter was $2 million, resulting in an effective tax rate of 3.1%. This compares to a tax benefit of $5.9 million in the prior year period. Both periods included discrete tax benefits attributable to the release of a valuation allowance on certain deferred tax assets. Excluding the discrete tax benefit, our effective tax rate would have been approximately 17% for the current quarter. We continue to expect our effective tax rate absent discrete tax items to be in the range of 17% to 22% for the full year.

Net income for the quarter was down over the prior year to $63 million or $0.97 per share. After adjusting for the discrete tax benefit, the change in fair value of equity securities, and a one-time non-cash adjustment made to our Williams royalty revenue, our adjusted net income was $57 million or $0.88 per share, which is higher than the adjusted net income in the prior year quarter of $54 million or $0.81 per share.

Our operating cash flow was strong again this quarter at $108 million compared to $120 million in the prior year. The decrease during the quarter was a result of higher interest payments on our revolving credit facility and lower royalty revenue.

I will now turn to Slide 9 and provide a summary of our financial position at the end of the quarter. During the quarter, we repaid $100 million on the revolving credit facility and reduced the amount drawn on the facility to $400 million. For the first six months of 2023, we have repaid $175 million of our revolver

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balance and in keeping with our approach to capital allocation, we expect to repay the remaining $400 million revolver balance as cash flow allows. The $600 million undrawn revolver capacity, combined with $102 million of working capital, provided us total available liquidity of just over $700 million at the end of the quarter.

As Bill noted earlier, we extended the maturity of our $1 billion revolver out two years to June 2028, and I want to echo his sentiment that we greatly appreciate the strong and continued support of our entire bank group.

With respect to further material financial commitments, assuming satisfaction of all closing conditions for the potential acquisition of the royalties from ACG, we anticipate the purchase price for the royalty assets would be made from cash on hand and an approximate $200 million draw on the revolving credit facility.

That concludes my comments on our financial performance for the quarter, and I will now turn the call back to Bill for closing comments.

William H. Heissenbuttel
President, CEO & Director

Thanks, Paul. I want to briefly mention something that is becoming more topical for our sector—that's the implementation of a global minimum tax or GMT. At this time, we do not anticipate any significant impact due to this worldwide rollout for a couple of reasons. First, we currently fall below the annual revenue threshold of EUR 750 million, so the GMT would not apply to us. Second, as a U.S. domiciled company, our royalty revenue is taxed to various rates all in excess of 15%, and our streaming business has been subject to the U.S. GILTI minimum tax since 2018. The GILTI tax rate is currently 13%, rising to 16% in 2026. As a result, we don't expect the implementation of a GMT at a rate of 15% will have a material impact on our business.

And finally, I want to comment on Mark Isto's pending retirement, which we announced in May. Since joining Royal Gold in 2015, Mark has been a key part of Royal Gold, and he has grown and strengthened our internal technical capacity. Mark will be missed, but he's done a great job of building talent within our technical team, and I'm confident that Martin has the right skills to lead that team when he assumes Mark's responsibilities. Mark will be with us for a few more weeks, but I hope you'll join me in wishing him well in his retirement.
Operator, that concludes our prepared remarks. I'll now open the line for questions.

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Question and Answer

Operator

[Operator Instructions] First question comes from Cosmos Chiu with CIBC.

Cosmos Chiu
CIBC Capital Markets, Research Division

Maybe my first question is on Mount Milligan. And thanks, Martin, for letting us know and confirming that there's the lag between production and payment to Royal Gold. But my question is, you kind of mentioned it in the press release as well, logistical delays due to the strike at the Port of Vancouver. How does that impact the Mount Milligan deliveries? And is concentrate shipped out from there, supplies coming in from there? Like what should we consider?

William H. Heissenbuttel
President, CEO & Director

Cosmos, thanks for the question. Martin, can I ask you to take a crack at that one?

Martin Raffield
Vice President of Operations

I'll take a crack at it, Cosmos. Thanks for the question. I'm not sure whether I can give very much detail around there. I think the comment relates to shipments of material out of the port rather than supplies coming into the port, and we don't really have any visibility on how that might impact us going forward, but it's there as a note and obviously, something that Centerra is keeping an eye on and understands could be an issue.

Cosmos Chiu
CIBC Capital Markets, Research Division

Okay. Great. Maybe a question on Khoemacau. I see that revenue was down quarter-over-quarter. Silver deliveries also was down slightly quarter-over-quarter. I guess my question is -- I know you're still ramping it up to kind of nameplate capacity. I know in Q1, there was some lower grade upper zone 5 top-down sort of approach in terms of mining sequence, and so that impacted it. And I thought Q2 was going to be slightly better than Q1 and then continued to improve. But maybe I'm wrong. Could you maybe talk about Q2 performance and also what we could expect from Khoemacau for the rest of the year?

Martin Raffield
Vice President of Operations

Bill, would you like me to continue with that one?

William H. Heissenbuttel
President, CEO & Director

Yes. Keep going.

Martin Raffield
Vice President of Operations

All right. Yes. I think the slight down that we saw in Q2, Cosmos, is really the sort of thing that we would expect from this type of underground operation as they go through areas with different grades. They have the normal sort of operating issues that mines have, especially fairly large underground operations like this one. I don't think there's anything that causes us any concern about what we've seen between the difference between Q1 and Q2, and I think that we expect the remainder of the year to be -- to track consistently at the 10,000 tonnes a day with the grade equivalent to where we've seen it so far. So no concerns with that downturn. I think it's just part of the normal running of this type of operation.

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Cosmos Chiu
CIBC Capital Markets, Research Division

Understood. Likely a question for Martin once again, but Penasquito, I saw that you booked $6.105 million of revenue in Q2. Given the ongoing strike, should we expect anything in Q3? Or is there some -- still some residuals coming out from Q2 deliveries that go into Q3? Like what should we sort of consider when modeling Q3 for Penasquito?

Martin Raffield
Vice President of Operations

I -- look, I don't -- I wouldn't comment on that at the moment in terms of what is going to happen at Penasquito going forward. Yes, I don't think I can make a comment on that at the moment.

Cosmos Chiu
CIBC Capital Markets, Research Division

Okay. But assuming that it stays on strike, would there be anything coming in from Q2's production? That's my question. I know it's hard to say it's going to come back on.

Martin Raffield
Vice President of Operations

Yes. It's hard to say, but there may be a small amount coming in, in Q3.

Cosmos Chiu
CIBC Capital Markets, Research Division

Got it.

William H. Heissenbuttel
President, CEO & Director

And Cosmos just appreciate the fact that Penasquito is -- there was a royalty that we purchased from a third party. We didn't write the contract and therefore, that's one asset where a lot of times, we find out when you find out. It's not as though we have regular monthly updates on what might be in the system.

Cosmos Chiu
CIBC Capital Markets, Research Division

Of course. Understood. And maybe one last question. Bill, I heard what you commented on Serrote and Santa Rita. There's really no update at this point in time. But could you remind us in terms of the conditions that need to be satisfied for you to go ahead and close this transaction? And what's your ultimate obligation? Is there a time line in terms of when these conditions need to be satisfied? And ultimately, what if you don't get satisfied, what's your obligation?

William H. Heissenbuttel
President, CEO & Director

Yes. I think the public comments that we made when we did our press release in June, negotiation of documentation and the closing of the acquisition, which was also in my prepared remarks, those are the conditions that we've spoken about. Of course, there are other ones. Yes, and as with all things we do like this, there is a drop dead date at some point, but, as I said in my comments, I'm just not going to say anything more about it.

Operator

We have no further questions. I'll now hand back to Bill Heissenbuttel, President and CEO, for closing remarks.

William H. Heissenbuttel
President, CEO & Director

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Well, thank you for taking the time to join us today. We appreciate your interest in Royal Gold, and we look forward to updating you on our progress during our next quarterly call.

Operator
Ladies and gentlemen, today's call is now concluded. We'd like to thank you for your participation. You may now disconnect your lines.

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