Royal Gold Inc.

Fiscal 2019 Q2 Conference Call

February 7, 2019 at 12:00 p.m. Eastern

CORPORATE PARTICIPANTS

Alistair Baker - *Director, Business Development*

Tony Jensen – *President and Chief Executive Officer*

Mark Isto – *Vice President Operations*

William Heissenbuttel – *Chief Financial Officer and Vice President of Strategy*

Bruce Kirchhoff – *Vice President, General Counsel and Secretary*

PRESENTATION

Operator
Good day, ladies and gentlemen, and welcome to the Royal Gold Fiscal 2019 Second Quarter Conference Call. All participants will be in listen-only mode. After today's presentation there will be an opportunity to ask questions. If you would like to ask a question, please press star, then one. If you would like to remove your question from the queue, please press star, then two. Please note this event is being recorded.

At this time, I would like to turn the conference over to Alistair Baker, Director of Business Development. Please go ahead.

Alistair Baker
Thank you, Operator. Good morning, and welcome to our discussion of Royal Gold's Second Quarter 2019 results. This event is being webcast live and you will be able to access a replay of this call on our website. Participating on the call today are Tony Jensen, President and CEO; Bill Heissenbuttel, CFO and Vice President of Strategy; Mark Isto, Vice President, Operations; and Bruce Kirchhoff, Vice President, General Counsel and Secretary.

This discussion falls under the Safe Harbor provision of the Private Securities Litigation Reform Act. A discussion of the company's current risks and uncertainties is included in the Safe Harbor and cautionary statement in today's press release and slide presentation, and is presented in greater detail in our filings with the SEC. Tony will give you an overview of the quarter, followed by Mark with an update on our operating results. Bill will then provide a financial update. And Tony will close out the call with some commentary on the current market environment. We'll then open the lines for a Q&A session.

Now, I will turn the call over to Tony.

Tony Jensen
Thanks, Alistair. Good morning, everyone, and thank you for joining the call. I'll begin on slide 4. Our revenue for the quarter was $97.6 million, down slightly from our previous September quarter of $100 million. Volumes were down slightly over the same period by about 3%, which is consistent with the guidance we provided in our last quarterly call. Metal prices were roughly in line with the last quarter, with realized gold and copper prices up 1% and silver prices down 3%.

Earnings for the quarter were $0.36 per share, which included a tax benefit of approximately $6 million and a loss of $3.6 million due to the mark-to-market on the value of equity securities. Bill will provide further details on these items in his remarks.

Operating cash flow was $59 million, which comfortably allowed the payment of another $16.4 million in dividends during the quarter. Consistent with previous years, our board announced on November 13 that the dividend was increased from $1 to $1.06 per share for the calendar quarter of calendar year. Paying a growing sustainable dividend is one of our key strategic objectives at Royal Gold and this increase continues our record of consistently raising our dividend since it was initially introduced in 2000. We have now returned approximately $460 million to shareholders in the form of dividends over the same period.

We also continuing to strengthen our balance sheet during the quarter. With working capital of $167 million and an undrawn revolving credit facility of $1 billion, we now have approximately $1.2 billion of

total liquidity and are well positioned for new investment opportunities.

On slide 5, I'd like to take a few minutes to give you an update on the Peak Gold project. As a reminder, this is the project that we have been working on in the Tintina gold belt near Tok, Alaska, with our joint venture partner Contango ORE. We own 40% and manage the joint venture, and Contango owns 60%.

Last quarter, I gave some highlights of the preliminary economic assessment results we released in September, and commented that with the PEA behind us, we would now turn our focus to maximizing the value of our interest in the project. The PEA gives an excellent starting point for the definition of the project, but a significant commitment will be required from here to advance the technical and permitting work to realize the full value of the project and the extensive property package. We believe that Peak Gold, with its relatively high grade and low cost, is a very attractive opportunity for an operating company to advance.

As we consider our next steps in potentially bringing in a new partner, we would ideally like to convert our interest in the project to something that is closer in line with our core business, which could mean taking partial consideration for our interest in some form of stream on this or another asset in a new partner's portfolio. Remember that we already hold a royalty on the underlying ground, so an important consideration will be to make sure that any new partner will dedicate the resources to advance the project as a priority. We are also very cognizant of the importance of this project to the local community, and a responsible development plan will be a key consideration before a change in management occurs.

Scotiabank has been retained to assist in identifying interested parties in advancing Peak Gold. We expect that the process will continue over the next several months and we'll provide further updates as and when we are able.

Now I'll turn the call over to Mark for a discussion on our operating results.

Mark Isto
Thanks, Tony. Starting on slide 6, I'd like to discuss some of our recent developments at several of our operating key properties. At Mount Milligan, 2018 production was very good, considering the constraints on throughput caused by water restrictions. Gold and copper production for calendar year 2018 achieved the high end of the revised guidance published in August, and gold production was 195,000 ounces compared to the guidance range of 175,000 to 195,000 ounces. Copper production was 147.1 million pounds compared to the guidance range of 40 million to 47 million pounds. During the December quarter, production from Mount Milligan was 60,000 ounces of gold and 11.8 million pounds of copper.

Sufficient water supply has been an issue at Mount Milligan for several quarters. The operation was designed to use surface water runoff for makeup process water, but during the past three years, this area of British Columbia has seen precipitation levels that are about half of what long-term records indicate. As a result, process water has been in short supply in the past couple of years. As you can see on the graph at the bottom of the slide, quarterly average throughput has suffered since late 2017, when the issue became apparent.

With respect to water sourcing and associated permitting activities at Mount Milligan, Centerra has reported that permitting applications are in process to draw additional flow during the spring melt period for the next three years from each of Philip Lake, Rainbow Creek, and Meadow Creek. If these applications are approved, Centerra plans to store this additional water in the tailings facility for use

during the remainder of the year, which will allow operations to continue at full capacity.

In addition to this strategy, which is intended to bridge the need in the medium term, Centerra is also completing a regional water inventory to identify other long-term sources that could provide additional water through the end of the mine life. For calendar year 2019, mill throughput at Mount Milligan is expected to be reduced during the remainder of the winter season to properly manage the water balance until water flows increase in the spring. Once the spring melt has commenced, which typically occurs in April, mill throughput levels are expected to return to full capacity.

The second half of calendar 2019, Centerra expects to achieve an average throughput of approximately 55,000 tons per day. For the full calendar year, Centerra expects Mount Milligan's total payable gold production to be in the range of 155,000 to 175,000 ounces and payable copper production to be in the range of 65 million to 75 million pounds. Note, that while the gold production guidance is lower than actual calendar 2018 production and copper production guidance is higher, using current gold and copper prices in the midpoint of the 2019 guidance, net revenue to us for our gold and silver streams at Mount Milligan would be slightly higher than calendar 2018.

Moving on to slide 7, I would like to provide some comments on Rainy River and Peñasquito. At Rainy River, ramp-up efforts by the new management team are continuing, with good progress achieved through 2018. The December quarter was very good, with mill throughput reaching a run rate of almost 26,000 tons per day, which is the first full quarter in which the mill averaged a daily run rate above the target 24,000 tons per day. Availability was low, at 80%, due in part to a 10-day suspension for mill repairs, which brought the average throughput down to 21,000 tons per calendar day, but the higher run rate demonstrates good progress.

In addition to the higher throughput, we saw higher grade for the quarter at 1.42 grams per ton. All this contributed to a strong gold production, which was up 39% from the previous quarter to 77,000 ounces and full calendar-year production of 227,000 ounces. As management has been improving the performance of the open pit, New Gold has decided to defer the underground development plan to 2020 and spend this calendar year reviewing the underground development scenarios.

Turning to Peñasquito. First gold production from the Pyrite Leach Project on November 29 and commercial production was achieved shortly thereafter in December. We are very pleased to see this project completed ahead of schedule, as it is expected to recover approximately 35% of the gold and 42% of the silver currently reporting to tailings, which is expected to add 1 million ounces of gold and 44 million ounces of silver over the remaining life of mine. All of this additional production is subject to our 2% NSR.

With respect to production, Goldcorp processed higher carbonaceous ore in the December quarter from the Chile Colorado pit, which had some negative impacts on gold recovery. During calendar 2019 Goldcorp expects grades and recoveries to improve, as the mine benefits from the completion of the multi-year waste stripping campaign in the Peñasco pit as well as a full year of production from the Pyrite Leach plant.

Finally, we are pleased to see that the combined Newmont Goldcorp has identified Peñasquito as a core asset in the portfolio of the merged company. Peñasquito is a significant asset in our portfolio, and it's great to know it will continue to be managed by a strong operator.

I'd like to wrap up on slide 8 with a few short comments on some of the other key development stories in our portfolio. At Barrick's Cortez mine, production to us was approximately 20% lower in the December quarter compared to the prior year quarter because of lower production subject to our

royalty. We expect to see increased production from Crossroads as waste stripping advances through 2019. We expect to receive a Crossroads production profile update during the March quarter, and should be in a position to share that with you on the next quarterly conference call.

Turning to Barrick's Pueblo Viejo mine, gold production was lower this past quarter compared with a year ago, due to lower grade and recovery, caused in part by higher organic carbon in the ore. While this lower production was disappointing, the main story at this operation is the growth potential resulting from the pre-feasibility study currently underway for the combined expansion project, which includes the pre-oxidation heap leach pad, a new mill and floatation concentrator, and additional tailings capacity.

On a 100% basis, Barrick expects that this project could increase throughput by 50% to 12 million tons per year, allowing the mine to maintain an average gold production of approximately 800,000 ounces after 2022. This project has the potential to convert roughly 7 million ounces of measured and indicated resources to proven and probable reserves. We look forward to hearing updates from Barrick on the progress of the pre-feasibility study work underway.

Finally, at Golden Star's Wassa mine in Ghana, operations continue to perform well. Wassa produced 150,000 ounces of gold in calendar 2018, and Golden Star is expecting calendar 2019 production of 170,000 to 180,000 ounces, which is 13% to 20% higher than the 2018 production level. The milling rate is expected to increase in calendar 2019 from 3,500 tons a day to a target of 4,000 tons per day in calendar 2020, and capital has been allocated to upgrade infrastructure and complete additional delineation in stope drilling.

Deep drilling at Wassa is continuing to show positive results, and a PEA on the optimal long-term development is expected in the second half of 2019.

Although the bulk of the upside we've seen from our Golden Star investment has been from Wassa, improvements at Prestea and raise development, long-hole drilling, and blasting productivities are expected to continue, supporting an increased production rate in calendar 2019. During the December quarter, the plant at Prestea was converted to a low tonnage, high-grade configuration, allowing efficient processing of this target mining rate.

I spent the last week in Ghana with Golden Star and was impressed by the progress being made at Wassa. I was also encouraged by the work being undertaken at Father Brown. As you may remember, this is a high-grade surface ore feed from Wassa in the past and Golden Star is evaluating the opportunity to supplement the Wassa mill with underground feed from Father Brown. The Wassa mill has an installed capacity of 7,500 tons per day compared to the 2019 target feed rate of only 3,500 tons per day.

I'll now turn the call over to Bill to discuss our financial results.

William Heissenbuttel
Thanks, Mark. I'll turn your attention to slide 9. As Tony mentioned at the beginning of his remarks, revenue this quarter was $97.6 million on volume of 79,600 gold equivalent ounces. This volume was in line with our expectations, as we discussed during our fiscal first quarter conference call. Earnings were $23.5 million, down from adjusted earnings of $28 million in the second quarter of the last fiscal year. Although there were a number of specific items related to the new tax law that impacted both quarters.

With respect to volume, we saw GEOs decline 11% in fiscal Q2 relative to the same period last year. Volumes were impacted by lower gold stream sales from Andacollo and Pueblo Viejo, which were

partially offset by higher gold and copper sales from Mount Milligan and improved contribution from Rainy River.

We also saw a reduction in royalty revenue due to lower production at Peñasquito and Cortez, which was partially offset by $2.5 million of royalty revenue this quarter from Voisey's Bay. This is the third quarter for which we've received royalty contribution from Voisey's Bay. Metal prices had a negative effect and were down across the board, with gold down 4%, silver down 13% and copper down 9% year-on-year.

With respect to certain items of note, we experienced two this quarter. The first is related to tax. In this quarter, we experienced the benefit of approximately $6 million or $0.09 a share due to additional utilizable foreign tax credits resulting from US tax reform. While we had previously estimated taxes payable under the new tax law, we, like all other US taxpayers, needed additional regulations from the IRS in order to fully reflect its impact. We were able to recognize that impact with respect to foreign tax credits this past quarter. While we don't expect any further material impacts, many aspects of the law remain unclear, so further guidance received from the authorities could cause some additional adjustments to our tax calculation. We now expect our full year tax rate will be in the range of 18% to 22%, down from the 23% to 27% range we provided last quarter.

With respect to the second item of note this quarter, we had a $3.6 million loss or $0.045 a share net of tax as a result of the mark-to-market movement in the equity positions we hold. We have previously discussed the new accounting standard for the recognition and measurement of financial instruments we adopted on July 1, 2018, that gives rise to this income statement impact. Continued volatility from the standard can be expected in the future to the extent we continue to hold these positions. We always like to remind you that our low share count makes relatively small earnings changes appear more significant on a per share basis.

G&A expense for the quarter was $7.4 million, down from $9.6 million from the prior year quarter, and $9.9 million in the first fiscal quarter of 2019. The reduced G&A spend experienced this quarter is more in line with typical levels, as it does not include the high levels of spending associated with the Vale litigation, the most significant contributor to the higher G&A in the previous quarters.

Our DD&A expense for the quarter was $38.8 million, or $488 per gold equivalent ounce, which was a $3.2 million decrease over the prior year quarter, reflecting our lower GEO volumes.

Our cash from operations was approximately $59 million, down from $76 million from the prior year quarter, directly related to lower volumes and prices, and higher cash taxes paid during the period. At the end of December, we held approximately 25,000 gold equivalent ounces in inventory. We expect sales for the current quarter to be on the order of 5% higher with a modest pull on our metal inventory levels.

I'll now turn to slide 10 and finish my comments with a summary of our financial position. Our liquidity position continued to strengthen over the quarter. We ended December with cash of $157 million, approximately $40 million higher than the end of the September quarter, and we had working capital of $167 million. These figures, coupled with our undrawn $1 billion revolving credit facility, provide us with total liquidity of almost $1.2 billion. Our only indebtedness is the $370 million of convertible bonds, which mature on June 15, 2019. We have available, and still plan to use, cash on hand and our revolving credit facility to repay the notes of maturity.

I'll now turn the call back over to Tony.

Tony Jensen
Thanks, Bill, and Mark, both of whom are fighting some pretty serious colds. So thanks for fighting through that. I'll conclude on slide 11, following on Bill's last comment about our liquidity and strong financial position, and what that means to us in today's market.

We often say that there are three ways that new business opportunities come to us. The first is through balance sheet restructuring; the second is through financing of development projects; and the third is through financing M&A transactions. Royal Gold has been active in all of these areas at different times in our history, and opportunities will present themselves from each of these sources at different times and frequencies, depending on the market environment. We were extremely busy in the 2014 to 2016 period helping to refinance balance sheets, but the industry is now much better capitalized and balance sheet restructuring is not a major source of new business today.

More recently, many of the opportunities we've been working on have been financing development projects, which is the second source of new business opportunities. With the continued growth in the trend of passive investing and generally negative investor sentiment towards the mining industry, there has been a lack of new equity in the sector, which has typically been a major source of financing for new projects. The cost of debt has also been rising, and many companies are hesitant to use debt financing, given recent history. As a result, we have been very busy working to try to fill the gap by providing capital to project development opportunities, which are typically smaller transactions than what we saw in the 2014 to 2016 period.

With respect to the third source of new business, M&A, we're seeing some very interesting business opportunities, given the state of play of the mining market. Firstly, the consolidation we've seen among the largest companies in the gold sector will present opportunities for us to provide cash financing to bidders who are interested in acquiring non-core assets spun out from the larger merged entities.

I see some very interesting parallels to what we saw happen a few years ago in Australia, where the gold industry was reborn by buyers of non-core assets, who are able to see the potential to reinvest in those assets. Examples would be Northern Star and Evolution, who grew into multibillion dollar market-cap companies by acquiring, recapitalizing and rejuvenating assets that major gold companies had defined as being too small and mature to maintain in their portfolios.

The second interesting thing about today's environment is that market valuations have reached levels we've never seen before, and we are busy working on ways to take advantage of what we think is a disconnect of fundamental asset values in a world where precious metal assets are in short supply. Regardless of where the opportunities come from, we have been patiently building our financial capacity and are well positioned to take a leading role in any opportunities when we see the potential to add high-quality investments to our portfolio. Our cash and access to capital are valuable differentiators for us as we consider new opportunities.

Operator, that concludes our prepared remarks, and we'd be grateful for some opportunities to answer questions.

QUESTIONS AND ANSWERS

Operator
We will now begin the question-and-answer session. To ask a question, you may press star then, one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw form the question queue, please press star, then two. At this time we will pause momentarily to

assemble our roster.

The first question is from Josh Wolfson of Desjardins. Please go ahead.

Josh Wolfson
Thanks. A first quick question on Voisey's Bay. The revenue that we saw in the fourth quarter, is that something we should expect roughly going forward with the new agreements?

Tony Jensen
Josh, I think that's a pretty good run rate. That's a very stable operation, we don't expect major variances from the production itself. The only variance that, of course, we're not in control of would be the nickel price.

Josh Wolfson
Right, I won't hold you accountable for those changes. And I guess bigger question on the Peak Gold JV. I understand, there is obviously a lot of conversations that are happening that are confidential, but maybe just bigger picture, our understanding is that Royal Gold is interested in streams but, given its stake in the asset level, it's interested in Contango as well as having royalties. It would seem to be the interest that it would be too large to convert to just stream, so in the conversations that are happening, are there any sort of disclosures or information you can provide on how the company would resolve that, or what its best sort of outlook would be there?

Tony Jensen
Thanks for the question, Josh. We are, at this point, coming to the market with Contango as well, so they also are part of our market test. And we'll see whether this is the right time to monetize our asset or not, only the market will tell us that. But we think it should be quite valuable, and certainly, the consideration that Contango might want and what we might want are different things.

But let me just speak to the Royal Gold side of that discussion, and let's not limit ourselves to potential compensation to just Peak Gold. Perhaps there's another asset in the portfolio of an acquiring company that we might be able to obtain a stream up on as well. And I kind of like that strategy. It's obviously self-serving, because it puts us over the core part of our business, but it also allows the acquiring company to pay for the acquisition over time out of the production from our asset, and not simply transfer a whole bunch of cash to us on day one.

So we don't know if we're going to be successful in that strategy. We think it makes sense, and we're hopeful that it will make sense to some of the parties that are looking at the project.

Josh Wolfson
That's good. Thank you very much.

Operator
Again, if you have a question, please press star, then one.

The next question is from Alex Hunchak of CIBC. Please go ahead.

Alex Hunchak
I was wondering if you could just remind me of the timeline of those permits that Centerra is waiting for right now. I'm assuming that they don't apply to the, sort of, April of this year ramp-up, but that they are kind of needed for next year to avoid having to ramp back down again, is that right?

Tony Jensen
Thanks, Alex. We understand that Centerra is expecting the ability to increase the flow rate at the sources they already have, like rainbow Creek and Meadows Creek. And we understand that they expect the permits to come before the spring melt, which is absolutely crucial and will allow them to capture more of that spring melt and retain it into the tailings facility. So that's what I can tell you on the permit side.

I think your question, part two, was a bit around production, but let me just say that in the guidance that Mark gave you, the lower first quarter production, I believe at 30,000 ton per calendar day, was incorporated into that production schedule. So if they're able to do better than that, obviously that would be a benefit to the guidance they've put out already.

Alex, is that responsive to both parts of your question?

Alex Hunchak
I think that covers it. That's great. Thanks a lot.

Operator
The next question is from Tanya Jakusconek of Scotiabank. Please go ahead.

Tanya Jakusconek
Good morning gentlemen. I have two questions, and one of them is just a clarification just so that I understand. Just on the guidance that was provided for fiscal Q3, I just want to make sure that I understood it, it's going to be about 5% higher than fiscal Q2 on your stream sales? Was that what you said?

Mark Isto
That's correct.

Tony Jensen
That's correct, Tanya.

Tanya Jakusconek
And modest pull on the inventory levels, is that on all three inventories?

Mark Isto
We think of the inventories in gold-equivalent ounces. We don't separate it by metal.

Tanya Jakusconek
Okay. Okay, that takes care of that one. And then, just maybe coming back to the M&A environment, and this one's for you, Tony, or whoever wants to take this question. I mean, there's a lot of assets out there now for sale and obviously lots can happen that there, but just from yourself, when you look at your third option of financing M&A transactions, perhaps just a little bit about, is there a certain level of geopolitical risk that you are looking at? So, for example, perhaps, you don't want more exposure to Africa, or are you looking at streams over royalties, some of these assets may not be able to take on the streams or maybe there are some. So maybe a little bit more on your strategy there.

Tony Jensen
Yes, Tanya, thanks for the question. So we very much will not compromise our three pillars of due diligence, where we look at the project itself and the quality, and can it sustain the stream. We often

look at that project from the operator's perspective, and we don't want our stream to push the project up into the fourth quartile. And so, that's just a very basic guidance that we do in any acquisition.

The second pillar would be the people and making sure that we have a very comfortable operating team and capable operating team to manage the asset. And then, finally, would be the place, and we're always going to be guided by our geopolitical risk appetite and being able to get comfortable wherever the asset is at. And any one of those may be a showstopper for us in investing in a project. And when they all three come together, then that's a recipe for investment for us.

So we won't cross any--I think you've been with us long enough to know the areas that we're comfortable in. There are certain countries in Africa that we're comfortable operating in, we're very much comfortable up and down the Americas, with the obvious exceptions. And certainly in Asia-Pacific, there's many places there, particularly in Australia, that we would be quite comfortable doing business in. So those are a bit of bread-and-butter, but our strategy won't change as we think about this new environment.

Tanya Jakusconek
And the new environment, Tony, are you focused mainly on gold and silver, because there are some non-gold assets that may be coming up for sale, are you looking at any of those, or streams on those?

Tony Jensen
We very much are quite pleased to be probably the highest percentage of gold, the highest percentage of precious metals certainly of the major streamers. And that's where our focus is. And I always caveat that to say if I, on a small investment basis, could get an interest in something that is non-precious metal but would very much be a decent rate of return on a long-term asset, we might take a look at it, but we're not out there focusing on it. We're very much focused on the precious metals.

Tanya Jakusconek
Okay. And then I guess my last one just on the M&A, I know I ask you this almost every quarter, Tony, but sort of the size range for us. Now that we have a new financing M&A sort of environment. The last time I think we talked about most of the deals you were looking at were somewhere I think in the $200 million to $300 million range.

Tony Jensen
Yes.

Tanya Jakusconek
What sort of range are we looking at now, in this new environment?

Tony Jensen
I would say $200 million, plus or minus, would be probably the best guidance that I could give there. I think $300 million might be a quite sizable deal in this market environment.

Tanya Jakusconek
Okay, perfect. Thank you so much, and good luck.

Tony Jensen
Thanks, Tanya.

CONCLUSION

Operator
This concludes our question-and-answer session. I would like to turn the conference back over to Tony Jensen for closing remarks.

Tony Jensen
Well, thank you for taking the time to join us. And on the call we also have Dan Breeze, who is in our Zug office. Dan manages our international business development activities, and we're absolutely just pleased and tickled to have Dan join our team, starting on the start of this year, and he's already off to an impactful start. So I look forward to Dan taking an active role on these calls and future sessions. But a big shout-out and welcome to Dan to our Royal Gold team.

With that, we thank you for your interest, and we look forward to speaking again in the very near future. Bye for now.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.