

Why Gold Mining Stocks and Warrants are Up so Dramatically

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Every investor has a wide array of asset classes and investment vehicles to consider – stocks; bonds; commodities; funds; options; LEAPS; etc. and the relatively unknown and misunderstood category called ‘warrants’. This article discusses the reasons behind the performance to date of commodity related company stocks (i.e. gold, silver and other metal miners and oil and gas operators) and their associated warrants vis-à-vis the aforementioned categories.

Week after week throughout 2009 the warrants of natural resource companies in North America have outperformed their associated common stock, the various stock market indices and gold bullion and silver even more. It begs the question: What’s going on here? There are three overriding reasons as discussed below.

Americans Investing in Canadian Securities Profiting from Strengthening Canadian Dollar

The U.S./Canadian dollar exchange rate is undergoing a major reversal. Since the beginning of the year the U.S. dollar has weakened 7.2% against the Canadian dollar.

Most commodity stocks and associated warrants are traded on the Canadian TSX or the CDNX and, as such, in Canadian dollars. This makes it that much more profitable for American investors to own such stocks and warrants than to own U.S. equities, gold and silver which are all priced in U.S. dollars.

True, currency plays can also go the other way, but most economists are of the opinion that the U.S. dollar is in a long-term decline vis-à-vis other currencies and, in particular, commodity currencies such as the Canadian dollar. Indeed, many economists foresee the Canadian dollar being at par with the U.S. dollar by the end of 2009. That would equate to a further 9.6% appreciation for Americans in the value of their Canadian dollar denominated holdings i.e. a possible 17.5% in additional profits over the course of 2009.

There you have it and it is worth repeating. Americans who used their U.S. dollars to buy Canadian denominated equities at the beginning of 2009 have received a 7.2% greater return on their Canadian investments to date than have their Canadian neighbours to the north. Were the U.S. dollar to continue its descent as anticipated, they would see a further 9.6% return by year’s end. That is impressive. It would appear that this is no time to look a gift horse in the mouth!

Indiscriminate Selling in 2008 Presenting Extraordinary Buying Opportunities in 2009

Another reason for the outperformance of commodity stocks and their associated warrants is that they declined so dramatically last year from their 2008 highs (i.e. the stocks by 58.2% and the warrants by 80.1%) that they have nowhere to go but up and up they are going at a rapid clip.

It is interesting to note about warrants is that, while they outperform their associated stocks considerably in a bull market, they drastically underperform such stocks in a bear market and that is just what happened in 2008. While that might seem rather disturbing on the surface it is not really of that much concern because the benefits of investing in warrants are realized over a long time horizon - as much as 8 years in the case of one warrant available on the market today – and, as such, warrants are a true buy-and-hold investment vehicle. With 50 of the 115 warrants associated with natural resource companies having duration periods of 24 months or more there are a large number of companies to choose from and ample time for many warrants to work their magic.

(For those who may not know warrants give the holder the right, but not the obligation, to purchase the common shares of the company at a specific price within a specific time period after which, if not exercised, they expire worthless.)

Increases in Price of Gold will Increase Mining Company Profits and Share Prices

A third reason that commodity stocks and their associated warrants (and particularly those of gold and silver mining companies) are outperforming all other asset classes is the expectation by most pundits that the price of gold will escalate rapidly in price (i.e. to \$1,600, \$2500, \$5,000 or even more) in the next few years (even by next year, say some). This will have a significant positive impact on the profitability of gold mining companies. For example, if gold were priced at \$950/oz., and the cost of production was \$400/oz., and two years later gold had risen to \$1600/oz., and the cost of production had escalated by 20% to \$480/oz. then the mining company's profit margin would have gone up from \$550/oz. to \$1120/oz. (i.e. from 57.9% to 70.0%).

With the cash flow of a mining company going up dramatically, the size of the resource and the value of a company going up dramatically and the profits of a company going up dramatically as well, one could reasonably expect the share price of a mining company's stock to go up dramatically too. Those understanding this relationship are now also aggressively buying warrants at their still oversold base which is also driving their prices up dramatically as the numbers below reflect.

Investor Advantage Rests with Those who Know the Secret of Future Warrant Leverage

The above being said, it should be noted those considering the purchase of warrants should not buy them with their eyes closed. There are many factors to take into consideration before doing so. The three most important considerations, of many, are one's estimation of the future prospects of the mining company of interest and, as such, its projected future stock price; secondly, the duration of the warrant associated with the mining company; and thirdly, the stated price (i.e. the strike or exercise price) and terms at which the warrant can be redeemed for the actual stock.

If one is of the considered opinion that the share price of the mining company being evaluated will increase significantly in price before the warrant expires and that the exercise price of the stock is sufficiently low to effect the option to buy the stock then major excess profits - as much as 10-fold - can be made by investing in the warrant instead of the stock itself. That is what warrant investing is all about - leverage.

To better understand which warrants are best positioned to realize over-and-above (i.e. leveraged) gains vis-à-vis their associated stock a twenty dollar investment in the extensive database details and leverage calculations offered by preciousmetalswarrants.com should be seriously considered.

Commodity Related Stocks and Warrants are Outperforming Gold by Large Margin YTD

	% Appreciation*
	Year-to Date**
Warrants (24+mo duration)	149.0
Stocks (with warrants)	94.0
CDNX	56.8

HUI	31.6
GDM	30.3
TSX	28.3
Silver	39.2
Gold	10.7
S&P 500	1.8

*all calculations based on U.S dollar equivalents

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As the above table shows, year-to-date natural resource companies that offer warrants are up 94.0% and the warrants associated with those stocks are up 149.0%. Silver is up a very respectable 39.2%. And gold? In spite of all the recent hype gold bullion is only up 10.7%.

In conclusion, those concentrating on the future prospects for gold need look no further than the present performance of natural resource related companies and specifically gold and silver mining companies and their associated warrants. **This year commodity related stocks have outperformed gold by 8.8 to 1 and their warrants have outperformed gold by 13.9 to 1.**

The above analysis begs the question: Now that you know what others don't shouldn't you add some gold and/or silver mining stocks to your portfolio? Better yet shouldn't you own some well chosen long term associated warrants? It is not too late and the financial rewards could be truly outstanding.

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