

# GRANT'S

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## Let's bury the gold

A friend proposes to strike it rich in gold by giving the public what it wants. What the public wants is mining stock. We know that by the stupendous valuations accorded mining companies at a time of stable gold prices. People want mines—so let's give them mines, our friend proposes. Let's buy some gold, bury it, dig it up and sell it.

Consider Echo Bay Mines, a large Canadian property with an enormous (67 times) ratio of price to earnings. Echo Bay has some 94.6 million shares outstanding on the American Stock Exchange with an aggregate capitalization (at 28½ a share) of some \$2.7 billion. Its relatively modest debt is approximately balanced by its equally modest current assets.

Now then, our friend says, let's just go out and buy \$2.7 billion's worth of gold (5,886,000 ounces at \$458 an ounce) and bury it. We'll pull it back out of the ground and sell it in regular quantities over the next 12 years (483,686 ounces a year).

We quote from our friend's business plan:

To keep excavation costs down, I suggest loading the bars into inexpensive surplus railroad tunnels somewhere along the old anthracite routes at a capital cost of, say, \$1 million. The use of potholes on New York City streets, while geologically feasible, would detract from the dignity of the enterprise and increase security costs. I suggest Golden Recycle as a possible corporate moniker.

Now then, what would our income statement look like?

At \$458 an ounce, assuming \$1 mil-

lion in annual operating expenses and a 12-year, straight-line depreciation of our mine site, you get: revenues of \$221.5 million; operating expenses of \$1 million, and operating cash flow of \$220.5 million. Now, then, subtract depletion of \$221.5 million, depreciation of \$80,000 and—presto—there's a loss of \$1 million, or thereabouts. The tax advantages of a reported loss have been obvious for years to Kohlberg, Kravis & Roberts.

The accompanying table presents a comparison of Echo Bay with Golden Recycle, with Golden Recycle, we submit, showing up to advantage.

Our friend elaborates:

In addition to being far more financially attractive, Golden Recycle has a superior operating margin, lower costs, no environmental exposure and fewer labor problems. Production rates can be

accelerated at modest cost or slowed, with little adverse effect on operating margins. Unlike other gold mines, it can be located, and if necessary relocated, in the most politically stable and favorable tax environments.

Several technical objections can be dealt with summarily. It is true that Echo Bay Mines has an ongoing exploration effort. In the first six months of 1987, exploration costs burned up cash at the blazing rate of \$4 million a year. It is our hope that Golden Recycle might be able to devote some portion of its \$161 million of excess annual cash flow to remedy any problems of self-perpetuation. To the extent such expenditures are incremental expenses, since the company has no taxable income, these costs might be partially recoverable through the creation of additional tax-loss carryforwards to be offset against future income.

There is no provision in the Golden

### The case for recycling

	Echo Bay (pro forma)	Golden Recycle
Market capitalization (\$ millions)	\$2,696	\$2,696
Reserves (thousands of ounces)	5,550	5,886
Annual sales (thousands of ounces)	456	483.7
Cash production cost/ounce	\$ 224	\$ 2
Operating cash flow (\$ millions)	59.8	220.5
Future operating cash flow of reserves at present prices (\$ millions)	727.8	2,683
Annual after-tax earnings (\$ millions)	31.6	(1.0)
Market capitalization/ounces of reserves (\$)	486	458
Market capitalization/ounces of annual production (\$)	5,912	5,574
Price/cash flow	45x	12.2x
Price/earnings	85x	N/A

Recycle figures for promotional markup. I leave that to the fertile imaginations of the readers of *Grant's* as to how such sums might be painlessly exacted.

As desirable an investment as Golden Recycle may be, it is arguably an even more lucrative investment banking project. Morgan Stanley, Goldman Sachs, First Boston or any other reputable applicant is invited to contact this office, day or night.



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