Sprott Gold Equities Strategy

Q3 2024 Commentary

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John Hathaway, Senior Portfolio Manager, joined Sprott Asset Management on January 17, 2020, following Sprott's successful acquisition and reorganization of the Tocqueville gold strategies. The Sprott Investment Team welcomes Hathaway, along with Victor Huwang, Director, U.S. Operations. The Sprott Investment Team offers world-class expertise in the active management of precious metals equities. Visit sprott.com for more information.

The Stage Is Set

October 1, 2024

We believe the stage is set for a powerful advance in gold mining equities. While the 27.71% year-to-date advance in the bullion price could (but won't necessarily) take a breather for the rest of 2024, significant catch-up potential for deeply undervalued gold miners has been barely exploited.

With gold trading at all-time highs, precious metals mining shares are just beginning to stir. GDX (VanEck Vectors Gold Miners ETF[1] and a proxy for gold mining shares) has increased 28.41% year-to-date, only slightly more than the metal's year-to-date gain of 27.71% (as of 9/30/2024). Looking at the five-year total return comparison (10/1/2019 to 9/30/2024), mining stocks gained 58.71%, distantly lagging gold's 78.92% rise.

We have addressed the disconnect between gold bullion and gold equities in previous commentaries. Gold stocks, in our opinion, are coiling for a sharp advance during the remainder of 2024. At the time of writing, GDX is breaking out above a five-year trading range that looks very similar, with a six-month lag, to gold's breakout earlier this year.

Figure 1a./b. Gold Bullion vs. Gold Mining Stock Prices (2019-2024)

Source: Bloomberg. Data as of 9/30/2024.

[1] VanEck Vectors Gold Miners ETF (GDX) tracks the overall performance of companies involved in the gold mining industry.

Favorable Fundamentals for Gold Miners

The investment fundamentals for miners have rarely been so favorable against a backdrop of such disinterest. The Q3 2024 average gold price (the most important single variable for miners' earnings and cash flow) will exceed Q2 by 5.2% sequentially, and 2023 by 18.8% year-over-year. For many companies, production is weighted toward the second half; we believe we may see blockbuster Q3 earnings reports later in October and early November.

Looking ahead to 2025, we expect production costs to remain stable or even decline in the event of a recession. Profit margins could expand even if the U.S. dollar gold price marks time (which we don't expect). Figure 2 depicts the relationship between gold and commodity prices (CRB Index[2]). A rising trend line tends to be exceptionally bullish for the earnings of gold miners.

Figure 2. Ratio of Gold Price to CRB Index (2022-2024)

Source: StockCharts.com. Data as of 8/30/2024.

Gold Is Still Underpriced

A key factor in the underperformance of mining shares is general disbelief that current gold bullion prices are sustainable or capable of further increase. In our view, the breakout in the gold price is not a fluke. The many contributing factors include (but are not limited to) de-dollarization, central bank buying, seemingly intractable U.S. fiscal issues, a possible recession, further monetary malpractice by the Federal Reserve (and other central banks) and the worrisome geopolitical landscape. Still, gold skeptics far outnumber believers. Proof can be seen in the forecasts for future gold prices from a broad array of financial firms (compiled by Beacon Securities; individual estimates by firm in Appendix A).

[2] The Commodity Research Bureau Index (CRBI) acts as a representative indicator of today's global commodity markets. It measures the aggregated price direction of various commodity sectors.

Figure 3. Gold Price Forecast

	2024	2025	2026	2027
Gold Price Forecast	**$2,279**	**$2,397**	**$2,232**	**$2,096**

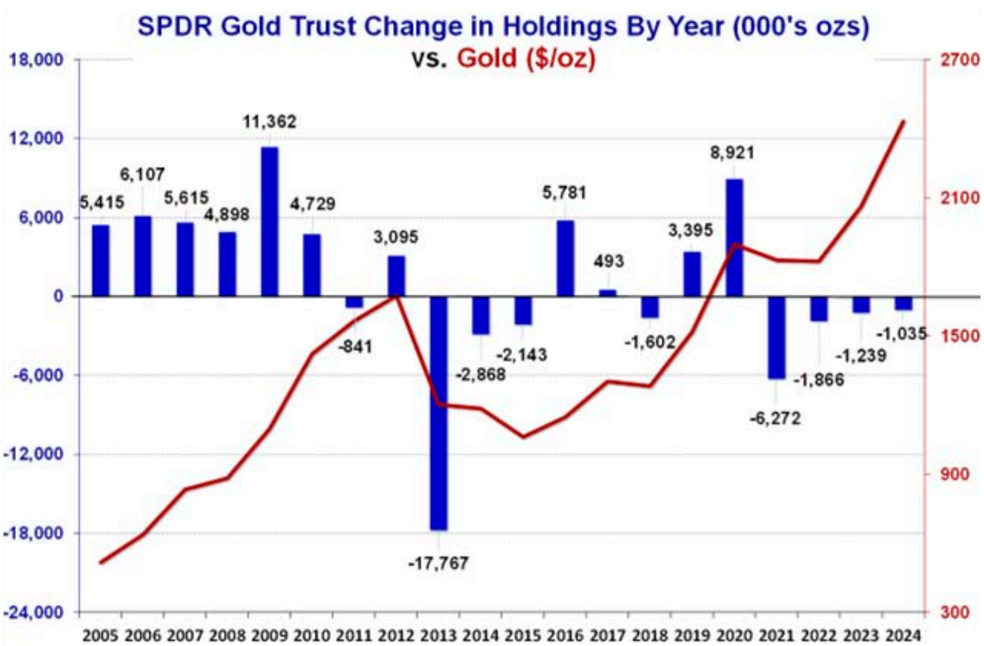
Who would invest in a gold mining stock with such a negative price outlook? While there are a few outliers, the consensus does not regard current prices as sustainable. We attribute collective bearishness to inattentiveness, lack of understanding, intellectual laziness, disinterest, and incompatibility with the groupthink underpinning mainstream financial market positioning.

For the sake of brevity, we will not elaborate here on the multiple forces (some admittedly speculative) that could power the further gains in monetary metals that we expect. Extensive commentary on our rationale can be found in our previous commentaries, as well as from many other observers.

Western Investors Continue to Ignore Gold

For now, it is enough to note that gold's 78.92% five-year advance has occurred with almost no participation from U.S. and European investors. Negative investment flows have persisted in both ETFs backed by physical gold and mining stocks, as shown in Figures 4 and 5.

Figure 4. SPDR Gold Shares ETF (GLD) Change in Holdings by Year (2005-2024)



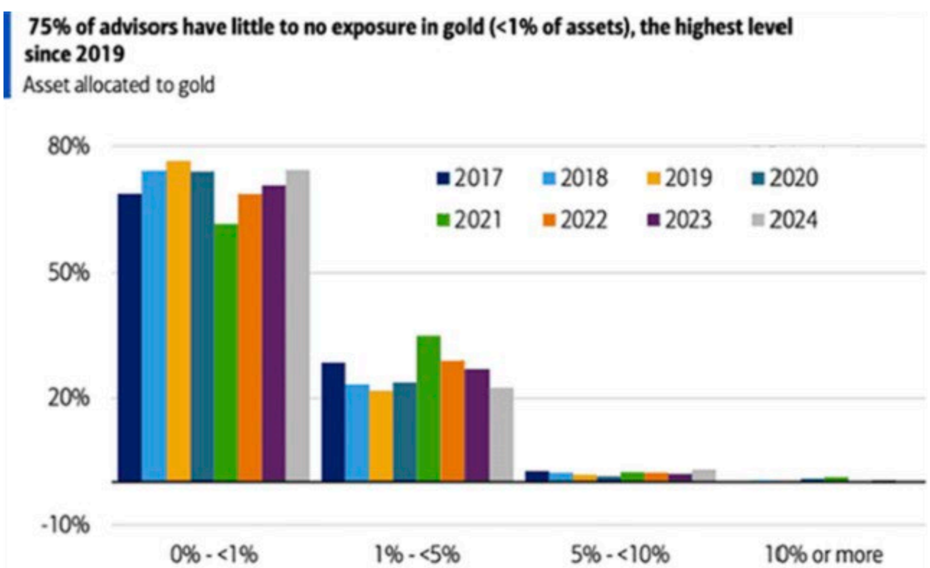
Source: Meridian Macro Research. Data as of 6/30/2024.

Figure 5. Current Shares Outstanding for GDX (2019-2024)

Source: Bloomberg. Data as of 9/30/2024.

Figure 6 shows that the positioning of financial advisors to precious metals is at a five-year low.

Figure 6. Advisors Hold Little Gold (2017-2024)



Source: BofA Global Research. Data as of 2/26/2024.

When Western capital market investors decide to reallocate a small portion of their capital to gold, and there are multiple reasons why they might, the metal's price will likely move higher. The impact on mining company shares, which collectively have a market capitalization approximately equal to Home Depot or Costco's, would, in our opinion, substantially exceed the percentage increase in the metal's price.

It is worth noting that following the launch of GLD (SPDR Gold Shares ETF)[3] in 2004, inflows of approximately 38 million ounces were sufficient to help fuel a 300% rise in the gold price from slightly less than $600 to $1,900 in August 2011, a seven-year span. Since 2010, the quantity of money (M2)[4] has increased 248% while the quantity of gold has increased (through mine output) only 22.2%. The quantity of U.S. dollars that could be exchanged for gold has increased 10x relative to the quantity of physical gold over the past 15 years.

Measured against the ratio of U.S. dollars to gold creation, the five-year 70% increase in the gold U.S. dollar price seems both sustainable and probably inadequate. Liquidity created by the Fed's decade-long policy of ultra-low interest rates and QE (quantitative easing) initially found its way into overvalued equities and assorted other financial assets. A small leakage from those positions would represent enormous buying power relative to available metal.

Early-Stage Bull Market for Gold

The current bull market for gold is embryonic, in our opinion. The classic hallmarks of an early-stage bull market include widespread skepticism and general underpositioning. The inevitable transition of investor psychology from pessimism to exuberance takes several years. Long-term investors in mining stocks are beginning to experience a small amount of daylight with the year-to-date rally.

The temptation to cash in gains that are paltry relative to years of unproductive returns is difficult to resist. We advise further patience. In our view, valuations remain exceptionally attractive assuming only the continuation of spot pricing for precious metals. Inflows into the tiny precious metals mining universe have barely started. The upside potential that likely lies ahead may be well worth any additional wait.

[3] The SPDR Gold Shares ETF (GLD) tracks the price of gold bullion in the over-the-counter (OTC) market.

[4] M2 is a measure of the money supply that includes cash, checking deposits and easily convertible near money. M2 is a broader measure of the money supply than M1, which includes cash and checking deposits.

Appendix A. Gold Price Forecasts by Company

Firm	Forecast as of	2024	2025	2026	2027	2028
Citigroup Inc	18-Sep-24	2,360	2,875			
JPMorgan Chase & Co	16-Sep-24	2,398	2,775	1,800	1,800	1,600
BMI, a Fitch Solutions company	16-Sep-24	2,250	2,150	2,000	1,900	1,750
MUFG Bank	13-Sep-24	2,450	2,894	3,100		
Standard Chartered Bank	10-Sep-24	2,268	2,650	2,488	2,275	
BMO Capital Markets Corp/Toronto	10-Sep-24	2,300	2,300	1,615	1,500	1,500
Deutsche Bank AG	6-Sep-24	2,291	2,350	2,300	2,355	1,800
Goldman Sachs Group Inc/The	6-Sep-24	2,357	2,686			
ING Groep NV	5-Sep-24	2,388	2,700	2,680		
Bank of America Merrill Lynch	5-Sep-24	2,365	2,750	2,625	2,448	2,270
Intesa Sanpaolo SpA	3-Sep-24	2,360	2,490	2,600	2,700	2,800
Landesbank Baden-Wuerttemberg	3-Sep-24	2,200	2,325			
HSBC Holdings PLC	2-Sep-24	2,305	2,105	2,025	2,000	1,818
Commerzbank AG	20-Aug-24	2,500	2,550			
Julius Baer	16-Aug-24	2,340	2,563	2,650	2,500	2,300
Bradesco BBI SA	25-Jul-24	2,252	2,200	2,200	2,200	2,244
Westpac Banking Corp	8-Jul-24	2,270	2,220	2,280	2,350	2,430
Barclays PLC	4-Jul-24	2,259	2,200	2,200	1,850	1,500
Berenberg	26-Jun-24	2,296	2,350	2,300	2,100	
MPS Capital Services Banca per le Imprese SpA	24-Jun-24	2,105	3,000			
Market Risk Advisory Co Ltd	24-Jun-24	2,278	1,700	1,775		
Macquarie Group Ltd	20-Jun-24	2,276	2,425	2,200	2,000	2,100
Societe Generale SA	19-Jun-24	2,380	2,500	2,150		
BNP Paribas SA	24-May-24	2,085	2,015		1,600	
Australia & New Zealand Banking Group Ltd	9-May-24	2,043	2,593	1,963	1,780	
Incrementum AG	11-Apr-24	2,450	2,600	3,100	3,600	
Morgan Stanley	4-Apr-24	2,219	2,163	2,000	1,800	1,800
Panmure Gordon & Co PLC	2-Apr-24	2,156	1,950	1,900	1,750	
Australian Government	28-Mar-24	2,023	2,030	1,924	1,875	1,883
Panmure Liberum	27-Mar-24	2,037	1,815	1,700	1,631	1,601
ACF Equity Research Ltd	25-Mar-24	2,400				
	Average	**$2,279**	**$2,397**	**$2,232**	**$2,096**	**$1,960**
Beacon Securities	**12-Aug-24**	**$2,250**	**$2,100**	**$2,000**	**$1,900**	**$1,800**
Forecasts Made 180+ days ago (*)						
Raymond James Financial Inc	1-Jan-24	1,850	1,700	1,700	1,700	1,700
Bank of Nova Scotia/The	1-Jan-24	1,900	1,700	1,700	1,700	1,700
CIBC	1-Jan-24	1,700	1,650	1,650	1,650	1,650
National Bank of Canada	1-Jan-24	1,825	1,750	1,675	1,675	1,600
RBC	1-Jan-24	1,700	1,700	1,650	1,600	1,600
Credit Suisse Group AG	1-Jan-24	1,700	1,650	1,650	1,500	1,650
Cantor Fitzgerald LP	1-Jan-24	2,000	2,000	2,000	2,000	2,000
TD Securities	1-Jan-24	2,000	1,850	1,800	1,700	1,700
Paradigm Capital Inc	1-Jan-24	1,750	1,650	1,650	1,650	1,650
Cormark Securities Inc	1-Jan-24	1,900	1,900	1,900	1,900	1,900
PI Financial	1-Jan-24	1,900	1,900	1,900	1,900	1,900
Stifel Nicolaus & Co Inc/Denver CO	1-Jan-24	1,813	1,750	1,750	1,750	1,750
Canaccord Genuity	1-Jan-24	2,100	2,176	2,227	2,262	2,227
Eight Capital	1-Jan-24	2,000	1,900	1,800	1,700	1,700
Bell Potter Investments Pty Ltd	1-Jan-24	1,950	1,975	1,975	1,975	1,950
UBS Group AG	1-Jan-24	2,075	1,956	1,775	1,725	1,600
Haywood Securities Inc	1-Jan-24	2,200	1,900	1,900	1,900	1,900
Capital Economics Ltd	29-Dec-23	2,050	2,130			
Emirates NBD PJSC	19-Dec-23	1,963				
National Australia Bank Ltd	3-Aug-23	2,019	2,130			
Jefferies LLC	20-Jun-23	1,900	1,900	1,750	1,500	
H.C. Wainwright	20-Jun-23	1,900	1,900	1,900	1,900	
Desjardins Securities Inc	19-Jun-23	2,000	1,900	1,775	1,775	
Toronto-Dominion Bank/Toronto	25-May-23	2,000				
M Partners	24-May-23	1,900	1,900	1,900	1,900	
Laurentian Bank Securities	23-May-23	1,750	1,750	1,750	1,750	
ICBC Standard Bank PLC	19-May-23	1,700	1,650	1,650	1,650	
Natixis SA	14-Feb-23	1,830				
	Average	**$1,906**	**$1,876**	**$1,819**	**$1,786**	**$1,785**

Source: Beacon Securities. Data as of 9/24/2024.

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Please contact the Sprott Team at **888.622.1813** for more information. You can also email us at **invest@sprott.com**.

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INVESTMENT RISKS AND IMPORTANT DISCLOSURE

Relative to other sectors, precious metals and natural resources investments have higher headline risk and are more sensitive to changes in economic data, political or regulatory events, and underlying commodity price fluctuations. Risks related to extraction, storage, and liquidity should also be considered.

Gold and precious metals are referred to with terms of art like store of value, safe haven and safe asset. These terms should not be construed to guarantee any form of investment safety. While "safe" assets like gold, Treasuries, money market funds, and cash generally do not carry a high risk of loss relative to other asset classes, any asset may lose value, which may involve the complete loss of invested principal.

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