Endeavour Silver Corp.

2020 Q4 and Year End Conference Call

Conference Call Transcript

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Speakers:

Bradford Cooke
Chief Executive Officer

Dan Dickson
Chief Financial Officer

Don Gray
Chief Operating Officer

Galina Meleger
Director Investor Relations

Operator:

Welcome to the Endeavour Silver Corp. 2020 Fourth Quarter and Year End Financial Results Conference Call.

I would now like to turn the conference over to Galena Meleger, Director, Investor Relations, for opening remarks. Please, go ahead.

Galena Meleger:

Thank you, Operator. Good morning, everyone, and welcome to the Endeavour Silver 2020 Fourth Quarter and Year End Financial Results Conference Call.

With me on the line today, we have the Company's Chief Executive Officer, Bradford Cooke; our Chief Financial Officer, Dan Dickson; and our Chief Operating Officer, Don Gray.

Before we get started, I'm required to remind you that certain statements on today's call will contain forward-looking information within the meaning of applicable securities laws. These may include statements regarding Endeavour's anticipated performance in 2021 and future years, including revenue and cost figures, silver and gold production, grades and recoveries, and the timing and expenditures required to develop new silver mines in mineralized zones. We do not intend to, and do not assume any obligation to, update such forward-looking information, other than as required by applicable law.

On behalf of Endeavour Silver, I'd like to thank you again for joining our call, and I will now turn it over to our CEO, Bradford Cooke.

Bradford Cooke:

Thank you very much, Galena, and welcome everybody to this year end financials call for Endeavour Silver.

Maybe I'll just start with some highlights. 2020 turned into a very challenging year with the COVID pandemic, but ultimately was one of our most satisfying years, as our operational group really came through in the crunch. We drove our costs down and, coupled with higher metal prices, drove significantly higher revenues, higher cash flow, higher earnings. We turned positive in terms of earnings for the first time in three years.

Notwithstanding the government-mandated two-month suspension of mining operations throughout Mexico, we were not only able to meet our 2020 original production guidance, we delivered higher production at lower costs at each of the three operating mines.

Perhaps last, but not least, in terms of high level comments, we obviously continued to focus on safety as our number one priority, and for the second year in a row Guanacevi, our largest mine, posted more than a million hours worked without a lost time accident, so kudos again to our operations team.

Let me touch on some numbers in today's news release, and then we'll open it up for Q&A.

As I mentioned, it was a very good year in 2020, and we've certainly finished the year with a bang. Fourth quarter sales were $61 million, up 81% year-on-year, cash flow was $22 million, up from negative $8 million a year ago, and net income was almost $20 million, with $0.13 a share, up from a net loss of $18 million a year ago.

Moving to the full year highlights, we posted $140 million of revenue, up 15%, cash flow of $29 million before working capital changes, up from negative $9 million, and net income of $1.2 million, up from a net loss of $48 million in 2019.

Our production was solid at 6.5 million ounces of silver and equivalents, the only equivalent being gold. That was actually down 9% from the prior year due to the closure of a now non-core operation in the El Cuba mine.

Cash costs at $5.55 per ounce of silver net of the gold credits was down 57%, so a significant reduction in cash operating costs, and the all-in sustaining costs were $17.59 per ounce net of gold credits, down 17% year-on-year.

We finished the year with a very strong balance sheet, $61 million cash, $70 million working capital, and just a reminder that we started 2020 with $23 million, so it was a heck of a year for adding cash to the balance sheet.

So, those are the financial highlights from today's news release. I think, Operator, why don't we open this up now for Q&A?

Operator:

Certainly. We will now begin the question and answer session.

The first question comes from Jake Sekelsky with Alliance Global Partners. Please go ahead.

Jake Sekelsky:

Hey, Brad and team. Congrats on a strong fourth quarter, and thanks for taking my questions.

Bradford Cooke:

Thanks, Jake.

Jake Sekelsky:

Just two quick questions on Terronera. Can you just provide us some colour around the timing of the feasibility? I guess, are you seeing any delays in the timeline due the pandemic? I know some of your peers have been seeing extended turnaround times on studies, and whatnot, so I'm just curious how confident you are in the timeline for that.

Bradford Cooke:

We're still reasonably confident. We had our quarterly management meetings last week and the report from our Director of Project Development was that we're almost bang-on, 50% complete feasibility study. Wood is the engineering consultant conducting the study on our behalf, but our Director of Project Development is very active, obviously, in the whole process. We are targeting a mid-summer receipt of the full feasibility study, and that would allow us to go to the Board for a development decision thereafter.

Jake Sekelsky:

Okay, that's good to hear. Then, just switching gears to exploration, in the release you touched on some greenfield exploration of the new concessions at Terronera, and I'm just curious what's the budget for that, and how much of a priority is it that relative to exploration across the rest of the portfolio.

Bradford Cooke:

Our Terronera budget this year for drilling, mostly untested veins on this very large property, is $2 million, and we're focusing in two main areas this year.

The southeast extension of the main reserve in the Terronera vein is still open to the southeast and we're testing an area about a kilometre further south, along the same vein structure. It does splay into two or three different parallel veins at that point and we've had some encouraging results so far.

The other one is on one of the newly acquired properties to the west of our original holdings at Terronera. It's a big vein. It's called Los Cuates. So, big as in up to 30 (inaudible 7:54) and we've traced it for 3 kilometres. We've just started testing various portions of that vein system.

So, early days yet, but we are hopeful that coming out of this year we'll have not only a new discovery, but some new resources at Terronera.

Jake Sekelsky:
Okay, got it, that's helpful. That's all from my end. Thanks again, guys.

Operator:
The next question comes from Heiko Ihle with H.C. Wainwright. Please go ahead.

Heiko Ihle:
Hey, Brad. Thanks for taking my questions.

Bradford Cooke:
Hey, good morning.

Heiko Ihle:
Your firm recently exceeded $1 billion in market cap. Congratulations. Has this done anything to your investor base, and on that same note, have you seen people interested that are able to purchase shares that previously weren't allowed to do so, and have the whole thing feed on itself a little bit? Have you seen anything like that? Have you gotten phone calls from people you've never really heard of before, funds that have mandates, like a market cap minimum?

Bradford Cooke:

Absolutely, Heiko. I don't know if we're seeing it yet, but in the coming 12 days Endeavour is certainly under review to be added to not one, but two indices. We certainly qualify, or appear to qualify, for the GDX, inclusion in the GDX Index. We're currently on the GDXJ. But, we're also in line, and could possibly qualify, for the S&P TSX 500 Index. Both indices actually do their additions in, I think, the third week of March, so it's coming up here pretty quick. We're hopeful that, given our US$1 billion market cap, that we do qualify to meet these two new indices, which is not just index buying, but a number of investors, institutional investors who only buy index stocks, so it could open the door for more institutional involvement.

Heiko Ihle:
Very helpful, thank you. Shifting gears quite a bit, I was going through your $12.8 million in net deferred income taxes on Page 39 of the financial statements. The figure includes $18.4 million of tax loss carryforwards. Are there expiration timelines for these assets, and if so, what's the timeline? Also, we're now in March, albeit March 1. Have you managed to recover anything of this sum year to date?

Dan Dickson:
Yes, Heiko, good question, way to get into the depth of those financials, Note 26 or 36. In that note, we actually show the expiration dates of our loss carryforwards. We are recognizing an asset related to those temporary differences, I believe $9 million at Guanacevi and $3 million at Bolañitos. The timeline to actually chew through those loss carryforwards is about 16 months for Guanacevi and less for Bolañitos, it should be in 2021, so less than 12 months. Q1 has continued …

Heiko Ihle:
Am I understanding you correctly, that some of these are expiring this year?

Dan Dickson:
No, sorry, they're …

Heiko Ihle:
You're looking at (d) on Page 40; correct?

Dan Dickson:

I'm not looking at it, but I'm familiar with the note. Ultimately, the—typically, a loss carryforward lasts for 10 years in Mexico, and I think some of them start running out in 2025 for us, but we'll use those loss carryforwards in 2021, Heiko, just based off the profitability. In regards to your question are we eating some of that up now, it's similar. Like, our production in Q3 and Q4 show that we're now making profit for tax purposes in Mexico. That's continuing here in Q1. We put out our guidance for 2021, and we expect to be profitable at these prices. Hence, using up those loss carryforwards.

Heiko Ihle:
Got it. Thanks for taking my questions. I'll get back in the queue, and stay safe.

Dan Dickson:
Thanks, Heiko.

Operator:
The next question comes from Joseph Reagor with Roth Capital Partners. Please go ahead.

Joseph Reagor:
Good morning, guys, and thanks for taking the questions.

Bradford Cooke:
Yes, thanks, Joe.

Joseph Reagor:
Looking at kind of the results from the fourth quarter, Guanacevi, you had slightly higher direct costs there. It seems like part of that was related to the purchasing of ore. Were there any other factors driving higher costs there, and then what are your thoughts on purchasing ore going forward?

Dan Dickson:
Yes, Joe, you're right, we did purchase more ore. Obviously, with higher prices, we're seeing more of the local miners bring third-party ore to our processing plant, which we're required to process, I believe, up to 10% of local ore just under the terms of when that plant was built. The other things that's coming through our cost structure in Q4, and it's

going to persist in 2021, is royalties and special mining duties. As we're more profitable in Mexico, we're paying more special mining duties, and that goes into our KPI metrics, and the royalties coming from El Curso, which is a property we acquired in 2019, we didn't have any upfront capital, but it does have a big royalty on it. Significant of our production is actually coming from El Curso, about 50% for 2021, so that's going to persist through our cost structure going forward.

Joseph Reagor:

Okay, and then on the tax front, I saw some commentary, I can't remember from which government person, but basically that the Mexican government expects less investment in Mexico in the coming years because their tax structure has become more cumbersome and more expensive, and that they believe people are going to look to invest in South America instead. Do you think that there's any opportunities to see them kind of roll back some of the taxes they added kind of just after the last peak in the gold cycle, or is that wishful thinking?

Dan Dickson:

I think at this time it's wishful thinking, based off the current government regime that's there. You're hearing a lot of rhetoric out of Mexico with regards to how much Mexican mining companies and Canadian mining companies are paying in taxes. This special mining duty was introduced in 2013, plus the environmental duty, which was 0.5% on gross revenue for precious metal companies. I would guess that none of that is going to get rolled back during this regime. Quite frankly, it would be great if taxes got lower in all jurisdictions, but I would think that going forward there, I'd always be conservative and hope that it stays where we're at now, and we'll be comfortable with that.

Bradford Cooke:

Maybe I can give some more colour to that. President AMLO didn't come out last week in a press conference and state no new mining taxes. I guess we're supposed to take that as good news. In the overall scheme of things, the total tax burden in Mexico is around 52%, 53%, so right up there with Canada and some other countries, not exactly the cheapest jurisdiction in the world. They would love to have more investment, but Mexico is caught in the middle of this COVID pandemic, with a crash in employment, a crash in tax incomes to the government, and no financial relief in Mexico for poor people, like there is in Canada or the States. So, I think it's steady as she goes in terms of taxes in Mexico.

Joseph Reagor:

Okay, and just continuing on that, and maybe one other thing just real quick, is that part of the reason the Company has started to look at South American opportunities, and then on that note, any update on what to expect from Parral this year?

Bradford Cooke:

So, yes, we diversified in recent years our exploration projects. We have three active and world-class prospects in northern Chile, we really like Chile as a country, and we're looking at other South American jurisdictions, as well as North America, so not just exclusively Mexico.

Then, Parral, after a one-year hiatus in terms of exploration drilling, we resumed in January drilling at our Parral project, with a $2 million budget, to try and grow the resource base there. We've basically got two more years to grow the resource base before Parral goes to economic studies and Terronera is up and running. We'd love to have our Project Development Team move straight from Terronera to Parral in 2024.

Joseph Reagor:

Okay, thanks. I'll turn it over.

Operator:

The next question comes from Craig Hutchison with TD Securities. Please go ahead.

Craig Hutchison:

Hi, good morning, guys, and thanks for taking the question, just a question on reserves and resources. You still have fairly substantial indicated resources at Bolañitos. What are the opportunities to have some of those resources sort of converted into reserves, and do you see the mine life at Bolañitos sort of extending well into next year at this point?

Bradford Cooke:

Yes, Bolañitos is a bit different that Guanacevi, because the main area we're mining is underneath the village of La Luz, which really prevents us from being able to drill from surface. Almost all of our drilling in these recent years of the La Luz vein system has been from underground, and of course that then—it's a cost reward exercise to see how far ahead we want to drill.

Can we convert indicated resources to reserves? Certainly, to some degree, but we typically run a one-year reserve envelope and an additional couple of years of resources, and I don't think that's going to change just because of the constraints of drilling ahead of the reserve envelope. Metal pricing could have some beneficial impact on conversion of resources to reserves, as well.

Craig Hutchison:
Could you remind me what's the budget for Bolañitos in terms of exploration this year?

Dan Dickson:
It's $2.25 million for brownfield exploration this year.

Craig Hutchison:
Okay, great. Thanks, guys.

Bradford Cooke:
Thanks for your questions.

Operator:
The next question comes from Lucas Pipes with B. Riley. Please go ahead.

Lucas Pipes:
Hey, good morning, everyone, and well done on the quarter, congratulations there.

Bradford Cooke:
Thanks, Lucas.

Lucas Pipes:
Joe asked most of my questions earlier, but I'll add some follow-up questions. First, on the purchased ore, can you remind us how we should think about margins on that business? Thank you.

Dan Dickson:

Yes, from a margin standpoint, we look to—we pay about 60% of the value of that ore, and ultimately, when it's all said and done, we share about 35% to 40%, with the processing costs and royalties that get put in place. Ultimately, it's about 10%. Last year, we were closer to 11% total production came from tolled ore, which is the highest we've historically ever been. If you go back through the last 10 years, we've processed about 6% of our throughput through tolled ore. So, at current prices, I would imagine we're going to be closer to 10% again this year, and generally follow the same formula, from a purchasing standpoint, of shooting for that 40% profit margin from it.

Lucas Pipes:

Very helpful, very helpful, I appreciate that detail. Then, second follow-up question, just on Chile. Brad, you mentioned how you liked being there, but what's kind of the priority in terms of allocating capital towards that region, and, very high level, kind of what are some of the catalysts we might see looking forward to when it comes to your Chile opportunities? Thank you.

Bradford Cooke:

Thanks, Lucas. We've been in Chile for, I think, eight years. We've generally run $0.5 million to $1.5 million annual budgets, so we've actually done pretty significant investment to acquire, explore and prepare for drilling our three projects. We're currently drilling one of them. The Paloma project in the far north of Chile is, arguably, 5 million ounce gold equivalent, high sulfidation epithermal target, so open pit, potentially bleach, but early days yet. We just started drilling it last year and we hope to have some results here in the next month or two.

We're probably going to partner our copper-rich projects. Cerro Marquez has copper/gold periphery. Again, we've spent several years and several million dollars grooming it, it's drill-ready, and we've had a lot of expressions of interest from copper majors, so we've signed some confidentiality agreements, and our preference is to bring on a partner at Cerro Marquez, which leaves our third project, Aida, and Aida is our extension of the Bolivian Silver Belt down into northernmost Chile. Again, it's drill-ready. It's a massive alteration zone with very strong indications of open-pit silver. We don't have the drill permit yet, we expect it late this year, and it would lead to a drill program at Aida either this year or next year.

So, we really like northern Chile. We've focused on world-class prospects when we acquired these things during the bear market. We're not done yet. We'll keep continuing to try and grow that pipeline. The whole goal of our Chilean exposure is to get into a discovery that has world-class potential and ultimately to add it to the development pipeline.

Lucas Pipes:
This is very helpful colour, I appreciate all the detail, and continued best of luck. Thank you.

Bradford Cooke:
Thanks.

Operator:
The next question comes from Henry Westerndar (phon 23:30), a private investor. Please go ahead.

Henry Westerndar:
Well, gentlemen, you seem to have had a very, very good fourth quarter, and that strikes me that the future in 2021, and beyond, could be very substantial, and without pushing the envelope too far, could you comment on 2021?

Bradford Cooke:
In terms of our public guidance, we've guided our production to be silver to slightly higher than last year, so I think 6.1 million to 7.1 million ounces of silver equivalent production forecasted this year. Obviously, the performance in Q4, with the lower costs and higher metal prices, is a pretty good guide for how we're going to do financially this year. We don't provide financial guidance, but Q4 is certainly a good indicator.

Henry Westerndar:
You provided a little when you said that you're going to use up the cash loss carryforward in Mexico this year. Would you say you're going to use it up very, very safely, just about use it up, or is it dicey?

Dan Dickson:
Using up both loss carryforwards, it's just a function of production and

what we've used historically from a cost standpoint. We have multiple entities in Mexico, and at Guanacevi, from 2016 to 2019, we had challenges financially and we came away with loss carryforward, and, hopefully, like I say, the next 16 months, we eat through those loss carryforwards.

Henry Westerndar:

Excellent, excellent. For what it's worth, I've been with you since 2003, up and down, and I think we're going up again. Thank you, gentlemen.

Bradford Cooke:

Thanks for your questions.

Operator:

The next question comes from Rahim Mama with Arcadia Economics. Please go ahead.

Rahim Mama:

Hi, guys. Thank you for having me. Congratulations on a great quarter four. My question has to do around—has to do with the developments that rose during quarter four, and mostly quarter one; specifically, with the silver squeeze and the manipulation of the price of silver on the COMEX. My question is does Endeavour have any strategic plan to deal with this, to combat the manipulation? An idea I've heard is withholding 5% of production. I just want to hear your answers around that and the future concerning that.

Bradford Cooke:

Well, thank you for your question. I guess I've got two different answers, because there's really two different issues here.

With regard to our sales strategy and whether we withhold or accelerate silver sales, that's typically a short-term decision based on our short-term view on the direction of the silver price. We have in the past, for instance, when we felt that the silver price was rising, held back our sales. For instance, most recently, last September, we built up a finished goods inventory because of the crash in the silver price late September, in the presumption that silver would bounce back in Q4, which it did with a bang, and we were able to sell that accumulated inventory and make extra profit on it. So, we do this from time to time.

It's a sales strategy.

With regard to the infamous silver short squeeze, I have a lot to say on it, and I actually posted an "Ask the CEO" comment on our website a few weeks ago, so you're welcome to go read that, but my view on this is perhaps a bit different than most. I don't think it was a silver squeeze. I think it was a classic pump-and-dump by some knowledgeable investors who did purchase $3, $5 call options on silver before posting on Reddit. Those options on the Tuesday before the Reddit posting were $0.35, $0.30 to $0.35, and on the following Monday, after promoting it for three days, those options were worth $1.65. So, I think some smart investors made a lot of money on that very short-term pump-and-dump. I don't think it was a squeeze at all.

Secondly, it's very difficult to squeeze silver, because banks are generally agnostic to the silver price. What I mean by that is that they're generally neither long nor short, or more accurately, they're long physical, sitting in vaults, and they're short paper. Banks, using fractional banking, do lend out their assets. If you run down to the local branch, your cash is being lent out several times, and that is probably the case in silver, but it's not manipulation, it's simply a function of what banks do. To be honest, if investors were to try and squeeze silver and buy physical, buy the ETF, buy the call options, what's a bank going to do? They're sitting on physical. So, they're the ones who are actually going to make money at higher prices, and they can roll out of—like, they're typically hedging their silver, right, and it doesn't cost them anything to roll out of a short position and set it higher, and roll out of it and set it higher, and they could do that all the way up to $1,000 silver.

So, I don't think there is a mother of all squeezes to be had in silver. I think it's a function—by the way, this is my last comment on this. Silver, amongst all the metals traded in the options and futures market, is different. Why is it different? Because of all the common metals, it's the only one that is a by-product of other mines. It's a by-product of copper mines, lead, zinc mines, gold mines, and those big, diversified global producers of copper, lead, zinc and gold typically sell forward their silver, lock in the revenue stream for their by-product, so they are unhedged on their primary products.

What that means is that silver, amongst all the metals, has a massively higher derivative book compared to the other metals, and compared to physical, and that's because diversified miners sell forward their silver. Who buys it? The banks enter into those forward contracts. So, now they have not only physical, they have a commitment to buy more physical, and because they're agnostic, they balance that long commitment with a derivative short. That's the structure of the silver market.

I think it's very, very challenging to try and squeeze something like silver, because the main beneficiaries of higher silver prices would be the bankers and the miners.

Rahim Mama:
Okay. So, kind of going off that—this is my last question and thank you for your answer—what is your projection for silver in 2021?

Bradford Cooke:
Crystal ball. Well, I'm not shy when it comes to forecasting internally, but I rarely do it externally. We obviously think that there's a silver bull market well underway, precious metal market well underway. It's probably got years to run. I say that for two reasons.

In the case of precious metals, primarily gold, there's a whole backdrop of record low interest rates, massive government intervention, no change in the Fed view for at least two more years, maybe three, so the fundamentals underlying a higher gold price, and therefore a higher silver price, are very strong.

But, silver, again, is not just a precious metal, it's an industrial metal, and the industrial side of silver is really taking off. Silver is a green metal. You can't have an electronics industry without silver. You can't have solar affordable (inaudible 31:55) power without silver. You can't have electric vehicles without silver. You can't have 5G technology, telephonics without silver. I think there is an emerging appreciation, finally, amongst generalist investors that silver is a go-to metal in a green economy.

Rahim Mama:
Okay. Thank you very much for your answer.

Bradford Cooke:
Thanks for your questions.

Operator:

This concludes the question-and-answer session. I would like to turn the conference back over to Bradford Cooke, the CEO, for any closing remarks.

Bradford Cooke:

Well, thank you, Operator, and thanks all for listening in today. Obviously, this was a great year, 2020 was a great year for us, very satisfying, after some challenging years. Q4 was a great way to finish the year and I think it's a good guide to how we expect to do in 2021. Thanks again. Stay tuned.

Operator:

This concludes today's conference call, you may disconnect your lines. Thank you for participating and have a pleasant day.