

MANAGING OUR RISKS CONTINUED RESPONSE/MITIGATION TO OUR RISKS

1. IMPACT OF METAL PRICES AND GLOBAL MACROECONOMIC DEVELOPMENTS

RISK DESCRIPTION

Macroeconomic events could create an adverse impact on our sales and profits, and potentially the economic viability of projects. These events include:

- A decrease in precious metal prices, which is the primary driver for this risk. The average realised price for gold remained flat year-on-year (+0.1% vs. 2017) while silver experienced an 8.3% decrease.
- Revaluation of the Mexican peso. In 2018, the peso was devalued by 1.6% versus the average spot exchange rate of the US dollar.
- General inflation in Mexico. This was 4.9% in Mexican peso terms during 2018. The specific inflation affecting the Company was 2.6% in US dollar terms.
- A decrease in the price of our by-products. In 2018, the average realised prices for lead and zinc decreased 7.4% and 5.7% respectively, over the previous year.

RESPONSE/MITIGATION

Our hedging policy remains guided by the principle of providing shareholders with full exposure to gold and silver prices. However, following shareholder approval for the acquisition of 44% of Penmont (and associated companies) in 2014, we initiated a specific hedging programme to protect the value of the investment made in the acquisition, using a collar structure to allow partial continued exposure to gold prices. The volume associated with this phased hedging programme was strictly limited to up to 44% of production associated with the acquired Penmont assets and will not be extended to other assets in the Group. The initial total volume hedged was 1,559,689 oz of which 1,213,537 oz have expired as at the end of 2018 (366,432 oz expired in 2018) with no corresponding cash impact in 2018.

We are not precluded from entering into derivatives to minimise our exposure to changes in the prices of lead and zinc by-products. In 2017, the Group hedged a portion of our by-product lead and zinc production with maturities starting in 2018. The combined profit during 2018 was US\$ 1.6 million.

 See note 29 in the Financial Statements page 211 for more details.

Furthermore, we have hedging policies in place for foreign exchange risk, including those associated with capex related to projects. In 2018, we entered into a number of foreign exchange forward contracts denominated in euros, Swedish kronor and Canadian dollars.

 See note 29 in the Financial Statements page 210 for more details.

In terms of inflation, we experienced an increase in one of our main energy inputs over the previous year, with the average cost of diesel (USC\$/lt.) rising by 7.7%. On the other hand, the weighted average KWH (USC\$) decreased by 6.4%. We will continue to identify and maintain efficiency initiatives to reduce our energy consumption.

DESCRIPTION OF RISK LEVEL

According to the majority of silver and gold financial analysts, the volatility of metal prices is expected to continue to reduce. Medium term projections are likely to favour stronger and more stable prices due to the unpredictable global conditions which include: the view that US economic growth will slow, and that the Chinese economy is likely to suffer from the negative effects of any trade war. In summary, the macroeconomic backdrop is likely to favour a rotation back to safe haven assets.

KEY RISK INDICATORS

- Gross profit sensitivity to the percentage change in precious metals price and to the Mexican peso/US dollar exchange rate.
- EBITDA sensitivity to the percentage change in metals price and to Mexican peso/US dollar exchange rate.

RISK APPETITE

HIGH FOR METAL PRICES, MEDIUM FOR ALL OTHER MACROECONOMIC DEVELOPMENTS

Risk rating (relative position)

2018: Very high (1)

2017: Very high (1)

LINK TO STRATEGY



CHANGE IN HEAT MAP

