

Is This The Cheapest Large Cap In The S&P/TSX Composite (Part 3)?

Description

Who doesn't love a bargain? Whether it's stocks or sweaters, everyone loves a deal. And I am definitely a cheapskate when it comes to stocks. That's why I set up a screen to uncover a list of large cap Canadian stocks trading at what could be very attractive valuations.

In [Part 1](#) of this series, I outlined the importance of screening to narrow the field and arrive at stock ideas that warrant further research. Here in the remaining parts, the field has been whittled down even further by tightening the screening criteria from [Part 1](#). These tightened parameters are outlined in the table below:

Metric	Parameter	Screen 1	Screen 2
Market Capitalization	Greater Than	\$5 billion	\$10 billion
Price/Book Value	Less Than	2.0	1.5
Price/LTM Norm EPS	Less Than	13	13
LTM ROE	Greater Than	10%	10%

From a pool of 43 that met the \$10 billion market cap minimum, three profitable big cap companies that trade at relatively cheap multiples have been revealed. They are listed below:

Company Name	Market Cap (MM)	P/BV	P/E	ROE
Magna International (TSX:MG,NYSE:MGA)	\$11,764	1.31	12.2	16.0%
Barrick Gold	\$34,102	1.42	11.0	12.9%
Suncor Energy (TSX:SU,NYSE:SU)	\$51,192	1.28	10.1	12.3%

Source: Capital IQ

Let's dig in to the second name on the list to see if it warrants an investment at this time.

Barrick Gold (TSX:ABX, NYSE:ABX)

Barrick is the largest gold miner in the world. Like Magna (TSX:MG, NYSE:MGA) in [Part 2](#), Barrick was born of humble beginnings and it too has gone on to become a tremendous Canadian success story. In recent years however, Barrick's stock price has been anything but a success.

The company has experienced tremendous growth as revenues have expanded from \$2.3 billion in 2005 to \$14 billion in the most recently completed twelve month period. This growth has come largely as a result of an aggressive acquisition campaign and new mine developments. The rising price of gold has also contributed.

The issue for Barrick has been costs. As revenues have expanded, gross margins have essentially been flat. In 2005, Barrick's GM was 47.6%, and in the last 12 months this figure checked in at 48.9%. This is not the sign of an attractive business model.

Ideally, as revenues grow, costs should remain flat, or at the very worst, increase at a more moderate pace. This is known as a "scalable" model. If cost growth is in line with revenue growth, management really isn't creating any value. Some term this "growth for the sake of growth".

In addition, since late 2004, investors have had an alternative way to invest in gold than the more traditional mining route. The introduction of the **SPDR Gold Trust ETF** (NYSE:GLD) provided investors with a liquid, cheap (in terms of fees), direct way to invest in the price of gold. GLD has been a wildly popular vehicle, currently sporting a market cap of \$71 billion. This compares to Barrick, remember the largest gold miner in the world, and its market cap of \$34 billion.

This combination of no real value creation and another way to play the commodity has Barrick, and many gold miners, sporting multiples that are far below historic norms. This can sometimes be an attractive scenario for investing. The problem is, I have no insight into determining whether or not this phenomenon is temporary. Nobody does.

I am very confident that the ETF dynamic is here to stay and this will probably prevent multiples from ever going back to historical levels. The game has changed. The question is, will Barrick's management suddenly find a way to begin creating value? Don't know. Without some sort of insight into this issue, I would steer clear of Barrick regardless of how cheap it looks.

Be sure not to miss the [full list of names that made it through the initial screen](#) in Part 1 of this series. In addition, [take a closer look at the valuation of Canadian auto part giant Magna](#) and uncover the rationale behind why one of Canada's leading energy companies, [Suncor](#), appears in this collection of discounted large caps.

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Fool contributor Iain Butler owns shares in Magna International ([TSX:MG](#)). The Motley Fool has no positions in the stocks mentioned above.

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- 1. NYSE:B (Barrick Mining)
- 2. TSX:ABX (Barrick Mining)

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