Barrick, Goldcorp down early on Goldman's call to short gold

Description

Last week it was Societe Generale that piped up with its prediction that the price of gold is set to fall. This week, it's Goldman Sachs. In a note this morning, Goldman indicated their new year-end target for gold is $1,450/oz in 2013 and $1,270/oz in 2014. The price of gold currently sits at $1,578/oz.

Goldman's rationale is based on the metal's recent lacklustre performance in the face of a flare up in Eurozone risk and disappointing U.S. economic figures. In addition, their economists' are calling for U.S. economic growth to accelerate to an above trend rate later this year.

The release also indicated that risks are skewed to the downside meaning the fall could be faster and longer than they currently expect. This is because speculative long positions in gold across COMEX futures and ETFs remain near record highs.

From one analyst to another

To put this call into perspective from the standpoint of the producer's stocks, we turn to some recent work by the team at RBC Capital Markets. RBC indicates that if the price of gold were to languish at the $1,200/oz level for 12 to 36 months there would be significant financial pressure placed on the likes of **Barrick** (TSX:ABX,NYSE:ABX) and **Kinross** (TSX:K,NYSE:KGC). These companies, along with several others, would be required to cut capital spending, seek out new capital to complete existing projects, place high cost operations on care and maintenance, and cut dividends.

The RBC piece also provided an estimate for what gold price the Tier 1, Tier II, and Tier III producers were currently discounting. The Tier I group, which includes Barrick, Kinross, **Goldcorp** (TSX:G,NYSE:GG), and **Newmont** (NYSE:NEM) has baked in, on average, a price of $1,520/oz for the commodity – not far from the current level. The Tier II and Tier III groups are discounting a price of $1,360/oz and $1,300/oz respectively. The company that appears to be discounting the lowest gold price is **Dundee Precious Metals** (TSX:DPM). DPM is currently reflecting a gold price of $876/oz.

Foolish Takeaway

Two shops have trimmed their expectations for gold and more could jump on the bandwagon as the herd forms. If you are looking to maintain an exposure to the precious metal, according to RBC's work, the Tier II and Tier III producers are the place to be as a hair-cut to the commodity is already reflected by the shares. Under Goldman's scenario, more pain could be in store for the majors, especially Barrick and Kinross given their relatively stretched balance sheets.

Fool contributor Iain Butler is short $32 July 2013 put options on Goldcorp and owns shares outright in Barrick Gold. The Motley Fool has no positions in the stocks mentioned above.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:NEM (Newmont Mining Corporation)
2. TSX:ABX (Barrick Mining)
3. TSX:DPM (Dundee Precious Metals Inc.)
4. TSX:K (Kinross Gold Corporation)

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