Are Gold Stocks Set to Rebound in 2017?

Description

The epic fall of gold prices that occurred back in 2011 was a turning point for the precious metals industry that saw largely inefficient processes and bloated operations replaced with an emphasis on lower-cost, higher-production facilities and a razor-like focus on debt reduction and lower operational costs.

The precious metals rally we witnessed in the first half of last year was brought to a halt by a series of unprecedented events that shook markets worldwide and had both positive and negative impacts on the gold market. Additionally, the occasionally feverish growth of crypto-currencies, such as Bitcoin, in recent weeks has also impacted gold prices and will likely continue to do so throughout the year.

Despite this, a handful of gold producers, including **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX) and **Yamana Gold Inc.** (TSX:YRI)(NYSE:AUY), remain strong investment options for 2017.

Here's a look at why both Barrick and Yamana are great investment opportunities now more than ever.

Lower costs, greater efficiency

During the lean years following the 2011 collapse of gold prices, both Yamana and Barrick were flirting with all-in sustaining costs (AISC) that were US$900 per ounce or, in some cases, US$1,000 per ounce.

Yamana has gotten AISC down to US$804 per ounce in the most recent quarter — down US$85 per ounce in the past year and down from over $910 in the past three years. Yamana continues to work on getting costs lower by placing emphasis on higher-performing, lower-cost facilities.

The change at Barrick was even more dramatic. In 2013, Barrick had AISC of US$915 per ounce, which was considered one of the lowest in the industry. In the most recent quarter, Barrick set a new record-breaking low of just US$704 per ounce for AISC.

Why is this important?

When gold prices were significantly higher, costs were more readily absorbed. The sudden drop in prices forced gold producers to become more efficient to maintain vanishing margins. Once the market recovered, as it did in the first half of last year, the lower margins translated into significantly higher revenues for gold companies.

Lessons learned — debt is a priority

Gold miners typically carry a huge debt load, and for good reason. Setting up a mine and beginning operations requires a huge amount of capital that could sometimes take years to recoup from the output of a mine.

Turning back to the 2011 price collapse, both Barrick, Yamana, and nearly every other gold producer on the market had a significant amount of debt. To add to this, as prices continued to fall over the course of the following five years, margins evaporated and miners turned to selling assets and credit facilities to keep businesses running.

In the case of Barrick, just under two years ago, the company had a staggering amount of debt that was over US$13 billion. Management embarked on a turnaround plan and targeted debt reduction of US$3 billion for 2015, and a further US$2 billion over the course of 2016 and this year. Barrick has even alluded to the possibility of being entirely debt free within a decade.

Yamana also undertook an ambitious debt-reduction plan, targeting $300 million over the course of this year. Part of that debt-reduction plan calls for selling off a number of assets that are not core to the company. Chief among those were subsidiary mines in Brazil, which the company recently attempted to offload through an IPO.

Debt reduction was one of the key factors in both Barrick and Yamana registering strong growth throughout 2016 and will likely remain a key focus of both companies this year as well.

What about gold prices?

After rallying over 15% for the first half of 2016, gold prices retreated in the second half of the year, registering only moderate gains for the year.

Some experts speculate that gold prices could be subject to another rally this year with gold hitting US$1,300 per ounce. That rally will primarily be fueled by a growth in demand for precious metals in markets such as China and India, the ongoing uncertainties relating to the incoming Trump presidency in the U.S., and the potential for additional election surprises in both France and Germany later this year.

In any event, both Barrick and Yamana are both great investment options that are better prepared for price fluctuations than they've been at any time over the past few years.

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