Should Gold Producers Remain in Your Portfolio?

Description

Gold has been viewed as a store of wealth for as long as people have been extracting the precious metal from the earth. For most of that time, gold has steadily appreciated in value thanks in part to the high demand, limited availability, and the general view that gold is a store of wealth.

Back in 2011, the gold market was on a tear, nearing US$1,900 per ounce. Gold producers were earning huge profits, and the price of gold enabled them to be dismissive about costs. When gold prices finally plummeted in a multi-year drop that saw gold hit sub-US$1,100 per ounce, producers finally got serious about cutting costs and addressing ballooning debt.

One such producer is **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX). Barrick is one of the largest producers in the world, and while the company is relatively healthy and posting strong results today, several years ago the company was valued by some investors as a candidate for bankruptcy.

The Barrick turnaround

Just under three years ago, Barrick held a staggering US$12.8 billion in debt, which was considerably more than what the company was worth. With gold prices still depressed, Barrick engaged in an aggressive turnaround that was focused on increasing efficiency and cash flow, while reducing debt.

To that end, Barrick is now one of the most efficient gold producers in the market with all-in sustaining costs averaging US$730 per ounce over the past year. Debt has been reduced by US$5 billion in just the last two years, and the company has stated it will be completely debt free in under a decade.

Between increased efficiency and a recovery in gold prices, Barrick has posted favourable results that have improved free cash flow considerably. Over the past year, annual cash flow has tripled to US$1.5 billion, the highest free cash flow has been, even when compared with 2011 when gold prices were north of US$1,900 per ounce.

Even better, by nearly halving overall debt, Barrick is paying considerably less in interest, which has pushed the company up even further.

Barrick's annual report for fiscal 2016 revealed a very different company than it was in previous years. Barrick posted net earnings of US$655 million, or US$0.56 per share for the year, on annual revenue of US$8.56 billion. Barrick's free cash flow for the year hit US$1.5 billion.

Part of that much-improved balance sheet is attributed to Barrick divesting some non-core assets over the past few years. Earlier this month, some sources claimed that Barrick was looking at different options for the company's Lagunas Norte mine in Peru, which holds an estimated value of US$1.4 billion and proven and probable reserves of 4.2 million ounces as of the end of 2016.

Lagunas Norte, which is now entering its end-of-life phase, has served Barrick well; it was responsible for over nine million ounces of gold produced over the past decade.

One of the options that Barrick is exploring, apart from selling the mine, involves extending the life of the mine by nearly a decade, garnering nearly 2.2 million ounces in production through a secondary process the company developed to extract gold from the material that was otherwise classified as waste.

Is Barrick a good investment?

Barrick remains one of the best investments in the market for investors looking to invest in the precious metals sector. With industry pundits now forecasting gold prices to appreciate to US$1,300 per ounce by year end, the highly efficient and capable Barrick could stand to benefit greatly.

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dafxentiou