Is Barrick Gold (TSX:ABX) Stock a Buy on the Dip?

Description

Investors who missed the big rally in gold and gold stocks through the summer are wondering if the recent pullback is a signal to start a new position or stay on the sidelines.

Let's take a look at the current situation in the gold market and try to determine if **Barrick Gold** (TSX:ABX)(NYSE:GOLD) deserves to be on your buy list.

Gold rally

Gold soared from US$1,300 per ounce at the end of May to US$1,560 a month ago. The precious metal then pulled back through most of September to the recent low near US$1,470.

Fears about a slowing global economy due to the ongoing U.S.-China trade war helped drive demand through the summer. In addition, the chaos in the British government has investors wondering if a no-deal Brexit could actually become a reality. Civil unrest in Hong Kong is stoking concerns that China could eventually resort to more forceful measures to stamp out the protests. Add in the attack on Saudi Arabia's largest oil-processing facilities, and you can see why global traders are seeking out safe-haven assets.

Interest rates also come into play in the gold market. A year ago, most pundits expected to see three rate hikes in the United States in 2019. As we now know, they were wrong. The trade war with China has had an impact on the U.S. economy and that forced the Federal Reserve to cut rates, twice!

Lower interest rates in the United States tend to be positive for gold as they reduce the opportunity cost of owning the yellow metal, which doesn't offer any yield.

The U.S. isn't the only country trying to prop up the economy by cutting rates. Central banks around the world are doing the same thing in an effort to combat slowing economic activity. The risk for investors is that a race to devalue currencies against the U.S. dollar could erode buying power and wealth.

Gold is priced in U.S. dollars, so owning bullion is viewed as one way to protect capital.

In Canada, for example, the loonie was on par with the U.S. dollar at the beginning of 2013. Today, a loonie is worth just $0.75 American, and that has occurred without the Bank of Canada cutting its interest rate.

Another development that has spurred gold buying is the trend to negative bond yields on global government debt. Reports suggest more than 25% of the world's government bonds, including those of Japan and several European countries, now trades at negative yields.

In that environment, no-yield gold starts to look like a good place to put money.

Should you buy Barrick Gold?

Barrick Gold recently slipped from $26 per share to below $23. Profit taking is likely part of the reason as gold pulled back, and investors who bought the stock around $16 in the spring decide to book gains.

Barrick Gold is a giant in the global gold mining sector with five of the top 10 mines on the planet. The company spent the past few years cleaning up its balance sheet and streamlining the corporate structure. It even raised the dividend.

Barrick also merged with Randgold Resources to create a powerhouse that has expertise in key gold regions, including the Americas and Africa.

The longer gold holds its gains, the better the margins will be for Barrick. Production is roughly five million ounces per year, so a US$200 increase in the price per ounce adds US$1 billion in revenue on an annualized basis.

Looking ahead, all the economic and geopolitical risks that drove gold higher in the past few months remain in place. In addition, the effects of the trade war are starting to become more evident in economic reports in the United States.

The manufacturing purchasing index just came in at 47.8%, the lowest reading since June 2009 and the second consecutive monthly contraction. This has helped gold bounce back above US$1,500.

Barring any shock announcement of a trade deal between the U.S. and China, it wouldn't be a surprise to see gold could hit a new 2019 high before the end of the year.

If you are a gold bull, Barrick deserves to be on your radar today. The market might be underestimating the firm's potential to generate significant free cash flow.

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