Gold Stocks Might Be Next in Line for Dividend Cuts

Description

The COVID-19 pandemic is wreaking havoc on the economy. Very few industries are able to weather the storm. Even gold stocks aren't immune, which has investors perplexed.

Despite significant volatility, however, the price of gold is flat over the past month. In comparison, the **iShares S&P/TSX Global Gold Index ETF** (TSX:XGD) has lost approximately 8% of its value. Although much better than the **S&P/TSX Composite Index** (-23%), gold stocks tend to outperform the metal in a gold bull market.

Why is this time different? Well, it's quite simple. Producers need people — and people are susceptible to COVID-19. Similarly, the gold industry has not been deemed an essential service. As such, they could be mandated to shut down.

This reality was front and centre this past week when **Agnico Eagle** (TSX:AEM)(NYSE:AEM) and **Newmont Goldcorp** (TSX:NGT)(NYSE:NEM) were impacted by the Ontario and Quebec shutdowns. Are the dividends now at risk? Let's take a look.

One of the world's leading gold stocks

After the Ontario and Quebec announcements, Newmont now has four mines on care and maintenance. Together, they account for approximately 20% of company production. The mines are located in Argentina, Canada and Peru. The moves were in direct response to ongoing efforts by these countries to mitigate the spread of COVID-19.

Notably, this gold stock has no confirmed COVID-19 cases among its workforce and is taking the necessary proactive measures to ensure the safety of employees.

Further to the mine shutdowns, Newmont pulled 2020 guidance. It expects that some production could be deferred into 2021. However, 2020 costs may be materially impacted depending on the length of the shutdown. As such, expect lower margins and profitability in 2020.

On the bright side, the remaining 80% are operating in line with production guidance. The company also appears to be well capitalized, with $2.2 billion in cash and more than $5 billion in liquidity.

The dividend accounts for just 15% of earnings, which provides the company some flexibility. Given this, there is no immediate risk to the company’s dividend.

A shutdown that materially impacts output

While Newmont is equipped to handle the shutdown, Agnico’s situation is more challenging. Agnico Eagle is being forced to ramp down operations in Quebec where the gold stock has three mines: LaRonde, Goldex and Canadian Malartic.

Moving these mines into care and maintenance will have a big impact on the company’s output. Combined they account for 876 ounces, which is approximately half of Agnico’s 2019 gold production. The expectation is that the mines will see little activity until at least April 13, 2020.

To make matters worse, the company’s mines in Nunavut — Meliadine and Meadowbank — are also operating at reduced levels and account for approximately 19% of 2019 production. If operations resume in a timely manner, a short-term disruption is manageable. If however, the shutdown lasts for months, Agnico Eagle will certainly feel the pinch.

Agnico’s dividend is well covered, with a payout ratio of approximately 40%. Despite this, the company has much less flexibility than Newmont. This is especially true given the impacts on production are more pronounced. Approximately 68% of gold output has been impacted by COVID-19 measures.

Should these measures remain in place for longer than expected, shareholders can expect a dividend cut or a temporary suspension altogether.

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