Why Kirkland Lake (TSX:KL) Dropped 10% After Agnico Deal

Description

Shares of **Kirkland Lake Gold** (TSX:KL)(NYSE:KL) fell 10% this week after news came out that the gold miner would be merging with **Agnico Eagle Mines** (TSX:AEM)(NYSE:AEM). The merger would create a company with a market capitalization worth over $30 billion, as of writing. So, why the drop?

What happened?

Shares dropped after the announcement that Agnico would be purchasing Kirkland Lake for about $13.4 billion. It's yet another deal in a slew of deals happening within the gold mining industry over the last few years, with a break during the pandemic. For every share of Kirkland Lake an investor owns, they will now receive 0.7935 of an Agnico share.

Under the merger, the pair will now exist under Agnico's name, with a board and management team derived from both companies. The deal, therefore, values each Kirkland Lake share at about $50.60, which was a discount of 9% after shares of the stock closed on Monday. Therefore, the recent drop by 10% seems to be warranted; however, it may now be fuelled by something else entirely.

So what?

The further drop is likely from investor fear on several accounts. First, investors may fear that the value of the company was off. Then, investors may fear that the share price would drop further. As for Agnico, shares were down just over 1%, which likely comes from the massive price tag associated with the purchase. However, Agnico remains confident that it expects to have $2.3 billion in liquidity, even after the merger.

On top of that, Agnico currently has a mineral reserve of 48 million ounces of gold and future development and exploration projects underway. This is great news from the large miner, as many of the biggest gold producers have struggled in the last few years from poor exploration and development.

Furthermore, the pandemic has not helped things, nor has inflation. Rising production costs, poor production in the last few years, and inflation all weigh heavily on the gold mining industry. So, finding ways to grow through other means has become a necessity for these major mines.

Now what?

Kirkland Lake, for its part, was already going through an acquisition spree over the last few years, as was Agnico. So, the pair together will create a powerhouse when the deal is finalized in December, or the first quarter of 2022. While the company isn't the largest in the world, it certainly will have the market share in Canada.

Shares of Agnico are still down about 30% year to date, after peaking one year ago. While sales are set to climb for the company in the next few years, it's true that inflation weighs heavily on this stock. Luckily, the mass amount of reserve it has will keep cash coming in. This is likely why Agnico can afford to purchase Kirkland in the first place.

Before the merger, analysts liked Agnico for its consistent long-term track record. It continues to trade at a premium to peers, even though it's not the largest producer. With that being said, today could be a great time to buy the stock on this pullback. Agnico continues to trade at a P/E ratio of 16.15 and an EV/EBITDA of 6.9. Plus, you can lock in a dividend yield of 2.77%.

Bottom line

This could create the third-largest gold producer in the world, and that's something Canadian investors should be interested in. This major merger may have a few hiccoughs in the first few years, but that's what makes it a strong investment today. Agnico and Kirkland combined have long-term production that will see decades of cash come in. The low-risk miner just became a contender for the top gold stock.

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