Is the Yamana Gold Takeover a Buy Signal for Gold Stocks?

Description

South African miner **Gold Fields** is buying **Yamana Gold** (TSX:YRI)(NYSE:AUY) for roughly US$7 billion in an all-share deal that is the latest in a string of consolidation moves in the gold industry in recent years.

Yamana Gold takeover

Yamana Gold investors will receive 0.6 of a Gold Fields share for each Yamana share they own. Investors didn't get that big a pop in the share price, however, due to the steep drop in the value of Gold Fields stock on the news. At the time of writing, Yamana shares are up just 3% to about $7 on the **TSX Index** from the May 30th close. The business will keep its head office in Johannesburg. Gold Fields shareholders will end up owing 61% of the new company, while Yamana shareholders with own 39% of the new firm.

When the deal closes, Gold Fields will become the world's fourth-largest gold producer. Yamana has attractive mines in key gold-producing regions in the Americas, including sites in Brazil, Argentina, Chile, and Canada.

Long-term Yamana shareholders might not be overly excited. They are getting a premium on the recent trading range for the stock in an era where no-premium deals have become common, but Yamana Gold is still well below it highs a decade ago, when the stock traded for $19 per share.

Gold market outlook

Gold miners are making good money at current gold prices. Even after the pullback the market has endured since the rally in early March that saw gold surge above US$2,000 per ounce, gold currently trades near a profitable US$1,840 per ounce. That's up from the low around US$1,800 the market hit two weeks ago.

The recent upswing could be the start of a new rally. The U.S. dollar has weakened after a strong surge. That trend could continue if markets start to see signals that U.S. inflation has peaked. Gold is priced in American dollars, so any drop in the value of the dollar against a basket of other major currencies often puts a tailwind behind the price of gold.

The crypto rout could also be a driver of new gold demand in the coming months. Investors in cryptocurrencies took a beating in recent months. **Bitcoin** and others are off the lows but still down 50% from the 2021 highs. Volatility could drive crypto investors back into gold through the end of 2022.

Inflation remains high and is expected to be a problem for some time until central bank rate increases can tame the surge in prices. Gold has historically found favour as a hedge against inflation. The yellow metal is also viewed as a safe-haven asset when investors are concerned about risks in the financial markets. The war in Ukraine and threats of a recession caused by rising interest rates could nudge more cash into gold over the next 12 months.

Are gold stocks a buy?

Investors who are of the opinion that the price of gold will maintain its current level or drift higher in the next couple of years might want to consider adding gold stocks to their portfolios. The top producers now have strong balance sheets and are generating significant free cash flow. The pullback in the prices of gold stocks over the past two months appears overdone, and the sector is arguably undervalued.

Smaller players could get bought as the industry continues to consolidate, but I would focus on the majors who are pumping out strong free cash flow, rather than buying smaller producers on the hopes of getting a buyout premium.

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