Why this portfolio manager sees the return of gold's glory days — and it's not just megamerger mania

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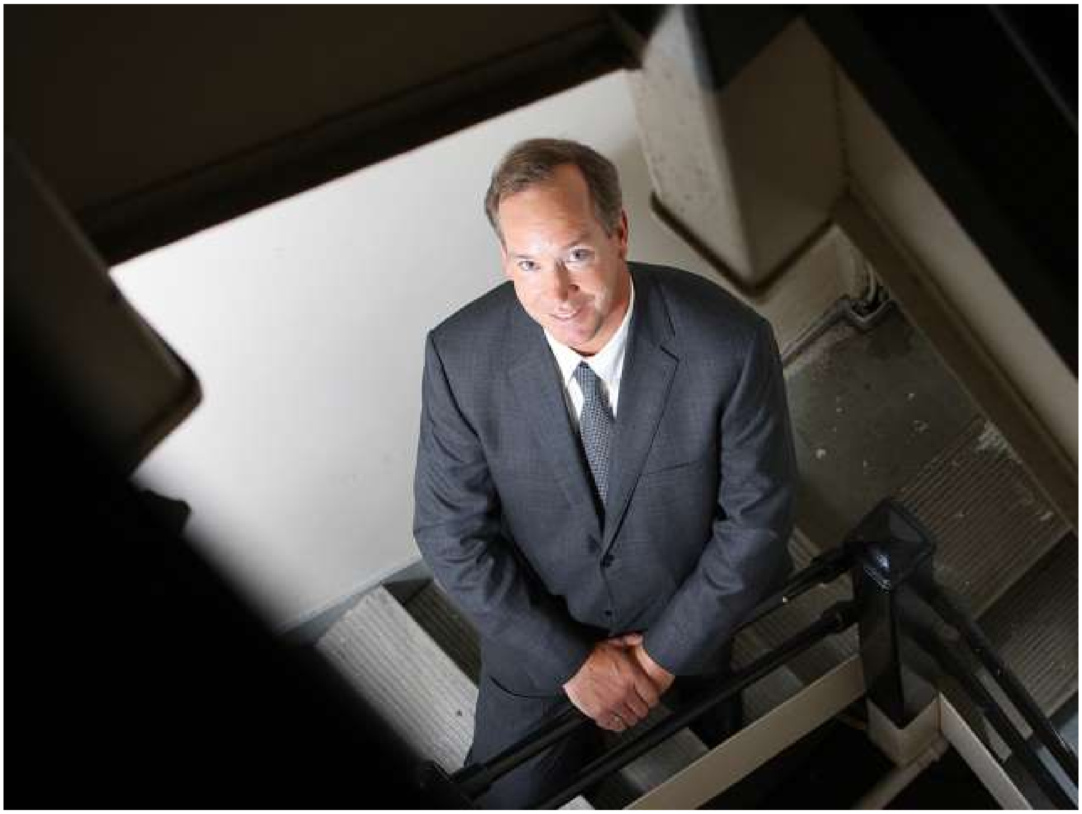
Gold bars and toads on display at a jewellery shop in Seoul. Park Ji-Hwan/AFP/Getty Images

David MacNicol has always described himself as a contrarian, so while investors have been exiting gold en masse for years, the natural reaction for him was to stay put.

Now the president and portfolio manager of Toronto-based investment firm MacNicol & Associates believes things are turning back in the yellow metal's favour.

"We think we're at the end of a cycle and at a turning point for gold and it has everything to do with interest rates and debt levels," said MacNicol, who thinks the precious metal's role as a safe haven remains intact.

Gold prices soared to a high of US$1920.70 an ounce from US$270 during an 11-year bull market between 2001 and 2012. After hitting a floor in 2012, the price has never quite recovered. Since then, investors have remained sour on the Canadian gold mining sector, which was the victim of poorly-executed mergers that left companies struggling to clear their balance sheets.



David MacNicol, the president and portfolio manager of Toronto-based investment firm MacNicol & Associates, believes gold is at a turning point. Peter J. Thompson/National Post

But a new string of mega-deals appears to have brought some excitement back to the sector, especially from institutional and retail investors who predict further acquisitions are on the way.

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Some central banks also may be warming back up to the yellow metal. According to the World Gold Council, central banks purchased more gold in 2018 than they had in any single year since 1967. China and Russia are among the known buyers.

Quietly, the price of bullion has also surged to US$1,329 an ounce as of 4 p.m. on Monday since hitting its 52-week low of US$1,182 an ounce in August.

The rising prices are important, but the reason MacNicol has remained devoted to his gold investments is because he believes interest rates will continue to rise.

As debt levels continue to climb to what MacNicol described as “unsustainable levels” in the U.S., rising rates may make it difficult for the government to service its debt, which could result in inflation and currency volatility — two good signs for gold investors, MacNicol said.

MacNicol, who has been invested in gold since 2002, has continued to raise his clients' exposure to the precious metal.

"What we have to do is protect portfolios and gold tends to be one of the best hedges against currency movement and inflation," MacNicol said.

MacNicol handles the portfolios of about 250 clients and tailors them toward retirement. The firm has $250 million in assets under management and another $250 million under advisory.

MacNicol does not run a fund and so his clients have segregated accounts. About 55 per cent of a standard portfolio is in stocks, 25 per cent in alternative assets including real estate, private equity and hedge funds and 20 per cent in fixed income. His investments in gold — in the physical metal and in stocks — take up between five to seven per cent of the majority of these portfolios.

Barrick Gold Corp. is among five core gold stocks that David MacNicol is still buying. Acacia

Most of his clients have holdings in five core gold stocks that he's still buying: Barrick Gold Corp., Newmont Mining Corp., Wheaton Precious Metals Corp., Wesdome Gold Ltd. and Aurania Resources Ltd.

Barrick was poised to become the world's top producer, taking over for Newmont, after announcing a $6.5 billion merger with Randgold Resources Ltd in October. Not to be outdone, Newmont announced a $10 billion merger with Goldcorp Inc. in January which would have likely seen it grab its position back from Barrick.

Then on Monday, Barrick launched a hostile US$18-billion bid for Newmont in a deal that would have the potential to create a true juggernaut in the sector.

MacNicol said he believes the latter deal would be a blockbuster, but is skeptical that it will go through because there is no premium being offered.

While takeover mania is usually good news for a sector, it isn't just the heavyweights that MacNicol has his eye on.

He is also excited about Aurania — a junior miner with a market cap of only $34 million.

The stock is down nine cents year-to-date, closing at $2.73 on Monday. It's a risky pick, MacNicol admits, and his portfolios will likely only have a one to two per cent exposure to the name, but it has the potential to boost his clients' returns this year, he said.

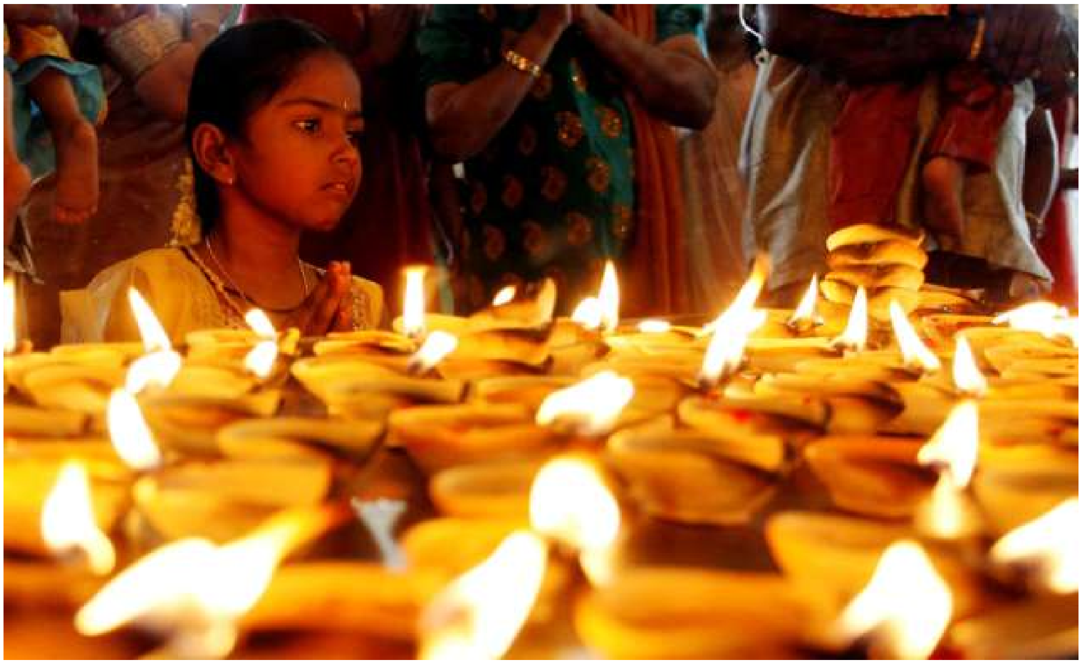
"When we meet with clients we tell them that might be an outlier and it might be cut in half or it might double," MacNicol said.

Based on the company's valuation, his own technical evaluation and earnings momentum, MacNicol has attached a $6.37 target on the stock.

Much of Aurania's prospects rely on its "lost cities" project in Ecuador that aims to uncover two cities of legend that were said to have vast gold reserves. Exploration teams are searching through more than 200,000 hectares of land, but have yet to begin drilling. Last week, Aurania announced it would be undertaking a rights offering to raise $6.35 million which suggests to MacNicol that they may be close to drilling.

Balancing out the risk he's taking in Aurania is MacNicol's position in Wheaton, the stock in his gold portfolio with the least amount of growth potential. Wheaton, unlike his four other core holdings, is not a gold miner. The Vancouver-based companies is a silver and gold streamer, meaning that it pays upfront for the option to acquire the precious metals from a mine that it does not own. Streamers, MacNicol said, are safer than miners because the stock does not face the same risk of downward pressure during drilling delays or labour issues on the front-line.

The stock is up 13.2 per cent year-to-date, closing Monday at $29.65, and pays a 1.7 per cent dividend. Since 2016, it has steadily traded between $19 and $30.



A Hindu devotee offers a prayer in front of oil lamps during Diwali, or the Hindu festival of lights. Nov. 9, is the biggest gold-buying day in the year as it is considered to be an auspicious day to purchase bullion. AP Photo/Daniel Chan

“It’s a nice, safe one you can put in your portfolio and not worry about,” MacNicol said.

MacNicol may continue adding to his positions in his core gold holdings, but won’t make any massive moves until the summer. That’s when gold prices tend to retest their floor, he said, because of monsoon season in India. Since 2015, gold prices have dropped substantially between July and September in every summer but one. Prices tend to pick up again in the fourth quarter during India’s wedding season and Diwali, MacNicol said.

Should gold futures, which MacNicol watches studiously, continue to track well at that time, he’ll consider increasing his exposure to close to 10 per cent. Usually cautious with investments in junior miners, MacNicol may also buy in on ETFs such as the VanEck Vectors Junior Gold Miners ETF if he sees the market taking off.

Of course, gold investing has been difficult for investors to time properly in the past, due to the volatility associated with the sector. So MacNicol knows he could be wrong.

“Six months from now you might be laughing at me saying that wasn’t a good call, but I’ll know in the meanwhile that I’ll have that insulation,” he said.

“It’s sort of like your portfolio fire insurance. You never want to collect on it, you never want your house to burn down, but you want to have it there just in case.”