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Gold's weakening outlook threatens miners' credit ratings

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Moody's now basing ratings on $1,100 (U.S.) an ounce instead of $1,200, compounding beleaguered industry's problems

Moody's Investors Service cut its gold price forecast for the year, putting the credit ratings of Canada's largest precious metal producers at risk of a downgrade as they battle an industry slump.

Reflecting the sharp drop in gold prices, Moody's on Wednesday said it will use an average bullion price of $1,100 (U.S.) an ounce instead of $1,200 to determine a company's credit rating.

"The increasing risk of lower prices suggests that key credit metrics of certain producers are stretched for current ratings in the absence of mitigation through cost reductions or other actions," Moody's said in a report announcing the lower gold price outlook.

Last year, gold fell nearly 30 per cent to $1,200 an ounce and has traded close to that level for the past few months. The weaker price forced producers to write down assets, cut jobs, and suspend dividends and projects.

A credit downgrade would put companies in a more precarious financial position and make it more expensive for miners to borrow funds.

It's the latest threat to an industry still suffering the fallout from an ill-timed spree of high-priced acquisitions and expensive mine developments in recent years. Now, gold companies are far less profitable or losing money, and the weaker gold price puts some of their unmined reserves at risk.

"The next story is the writedowns of reserves because of the low gold price," said John Ing, president of Maison Placements Canada.

"It won't only be the gold price that will fall, but their expensive reserves and resources," Mr. Ing said.

Gold companies' current reserves were calculated using higher prices, when gold was on the rise.

For example, Barrick Gold Corp., the world's biggest producer, used $1,500 to calculate its reserves. The company has said a $300 drop in its gold price assumption would result in a less than 10 per cent decline in its proven and probable gold reserves (if all other assumptions and inputs remained the same).

The world's second largest producer, U.S.-based Newmont Mining Corp., used $1,400 to calculate its reserves. Mid-tier Canadian producer Agnico Eagle Mines Ltd. used a $1,490 price assumption for its mines that have a shorter life and $1,345 for its longer-life mines.

Credit rating cuts would compound the industry's problems. Canada's largest gold producers, including Barrick, Kinross Gold Corp. and Goldcorp Inc., all have coveted investment grade ratings. Still, the companies' ratings are among the lowest investment grade ranks at Moody's. Barrick is rated Baa2, the second lowest investment grade rating; Kinross is Baa3 (the lowest investment grade rating) and Goldcorp is rated Baa2.

Pawel Rajszel, an analyst with ***Veritas Investment Research***, said there is a high risk that gold companies' debt would be downgraded.

"Producers' margins are already thin, so small changes to the assumed gold price will likely have a significant impact on the resulting credit metrics," ***Mr. Rajszel*** said. "Credit downgrades are but another headwind for gold companies as access to capital becomes more costly."

Moody's said it will examine miners' year-end results and will talk to the companies about further cost reductions.

"We think the fourth quarter of 2013 will provide key data points to help determine which if any of the ratings do need to come down," said Moody's senior credit officer Darren Kirk. "Certain ratings will likely be impacted."

Barrick has taken the most drastic steps to improve its balance sheet. The company suspended development of its expensive Pascua Lama mine in South America, raised $3-billion to reduce its debt load, sold mines and cut jobs.

Similarly, Kinross slashed its capital expenditures, cut its dividend and delayed making a decision on expanding its Tasiast gold mine in West Africa.

Companies are due to start reporting their fourth-quarter results in February.