



Is the Outlook for Gold Improving? Signs to Watch

Description

Despite Warren Buffett once famously stating that gold is a worthless investment because of its lack of utility, it remains a favorite among investors. This is because it's seen as both a hedge against inflation and a safe haven investment should markets collapse.

Already this year, gold has rallied off the lows resulting from the Fed's tapering of quantitative easing at the end of 2013 and from a sell-off in emerging markets that invoked further fears of a general market collapse. But these are not the only factors that affect the price of gold. There are many constantly changing indicators that make it difficult for investors to predict whether gold will continue to recover or fall to new lows.

What are the key drivers of gold prices?

Analysts are divided as to which direction the price of gold will move. Investment bank Goldman Sachs has predicted gold will fall to as low as \$1,050 per ounce by year's end, whereas a number of industry insiders believe it will continue to rally.

The price of gold has several key drivers, such as demand from central banks, general demand from investors who consider gold a safe haven, and the gold jewelry market.

What are recent indicators saying about which way gold prices will move?

Currently, gold continues to hover around the \$1,300 per ounce mark, which is an almost 8% gain for the year-to-date. This, coupled with gold's recent rally, has sparked renewed interest among investors not only in acquiring physical bullion but also in the beaten-down gold-mining industry. There are also signs the price of gold may remain at this level, or even continue to appreciate, for some time yet.

According to the World Gold Council, jewelry demand for gold grew 3% year-over-year to 571 tons, which is the largest first-quarter volume since 2005. Central bank demand continues to remain strong with the first quarter of 2014 being the 13th consecutive quarter of net purchases by central banks. This demand is supported by concerns over an uncertain global economic outlook.

But investment demand in the first quarter of 2014 fell 2% compared to the same quarter in 2013, while gold bar and coin demand plunged a massive 39% for the same period. This can be attributed to investors shifting funds to growth-oriented investments as stock markets continue to rally on better-than-expected economic data showing improvement in the global economy.

However, this weakness in investment demand was offset by the global gold supply remaining relatively flat for the first quarter of 2014, increasing by a mere 1% compared to the equivalent quarter in 2013. This was even the case despite mine supply growing during the quarter as gold miners sought to take advantage of the rally in gold prices. The key reason for this was a significant drop in the amount of recycled gold coming onto the market.

What does all of this mean for investors?

While there is considerable uncertainty, and even pessimism, surrounding the outlook for gold, first-quarter indicators show that the current price may in fact be sustainable for the remainder of the year. This is despite better-than-expected global economic growth and a resurgent Chinese economy, which could apply further downward pressure to the gold price.

So: Is now the time to invest in gold? If so, what is the best investment?

Investors have a range of options. They can either choose to hold physical gold, invest in a gold ETF, or invest in gold-mining stocks. Given that a number of gold miners are trading at significantly depressed prices and that many are moving to slash production costs and boost profitability in a difficult operating environment, investing in stocks is my preferred choice.

Two mining companies that stand out are **Barrick Gold** ([TSX: ABX](#))(NYSE: ABX) and **Goldcorp** (TSX: G)(NYSE: GG). Both have seen their share prices plunge over the last year, to be down by 17% and 10% respectively.

But both have worked hard to realign their operations so as to remain profitable in a difficult operating environment governed by a volatile outlook for precious metal prices. This has seen their production costs fall significantly, with Barrick's all-in-sustaining-costs falling by 7% quarter-over-quarter and 11% year-over-year to \$833 per ounce. In contrast, while Goldcorp's all-in-sustaining-costs shot up 4% quarter-over-quarter, they dropped an impressive 26% year-over-year to \$840 per ounce.

Both companies also took a number of impairment charges across their assets at the end of 2013, writing down the value of marginal assets and goodwill as well as recalculating their gold reserves using a lower realized price per ounce. That has left both companies well-positioned to take advantage of the shifting gold market, as they will remain profitable should the gold price fall further and boost profitability if it continues to rally.

CATEGORY

1. Investing

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1. NYSE:B (Barrick Mining)
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