3 Reasons Why Gold Is a Poor Investment

Description

I have always found it hard to understand why some investors passionately believe that gold is the ultimate investment. While it performed spectacularly at the time of the global financial crisis, it has been one of the poorest performing and most volatile asset classes over the last 40 years.

Now what?

Since peaking at an all-time high of US$1,917.90 per ounce in 2011, gold is now off by 44% to be under US$1,080 per ounce, and there are three critical indicators highlighting that it has a lot further to fall.

Firstly, a stronger U.S. economy does not bode well for the price of gold.

The U.S. economic recovery continues to gain momentum, and the Fed has taken a positive view of the outlook for the U.S. economy. The Fed is set to hike interest rates in December. A rate rise will increase the opportunity cost of holding gold, and this will trigger a flight from gold as investors move to investments that offer higher yields.

Secondly, gold lacks utility and has very few industrial uses.

This means that its price is not a function of supply and demand. Its value is determined by the currency in which it is priced: the U.S. dollar. When the dollar appreciates in value, the price of gold falls, and vice-versa when the dollar depreciates.

With the U.S. economy growing ever stronger and an impending rate hike, the value of the dollar can only increase, which is bad news for the price of gold.

Finally, gold is often touted as one of the best safe-haven investments for uncertain times, but there is increasing evidence that is not the case.

Recent geopolitical and macroeconomic events failed to lift the price of gold, leaving it languishing at under US$1,100 per ounce.

There is also very little evidence to suggest that it is a good hedge against inflation. Studies show that over the last 40 years there is very little correlation between inflation and the price of gold.

Each of these factors portend poorly for the outlook for gold and could be just enough to push its price under US$1,000 per ounce.

So what?

If gold slips under US$1,000 per ounce, this will be extremely bad news for beaten-down gold miners because many are struggling to remain profitable. This would force them to shutter operations and revise their gold reserves downward. It would even make the gold miners that are attracting a lot of positive attention, such as **Kinross Gold Corporation** (TSX:K)(NYSE:KGC), unattractive investments.

You see, with gold at US$1,079 and all-in costs of US$1,000 per ounce, Kinross is only making a thin margin. When gold slips under US$1,000 per ounce, it will then be generating a loss on every ounce of gold it mines.

It is a similar story for many other gold miners, and the current harsh operating environment coupled with the poor outlook for gold means that the pain is far from over for gold-mining stocks. This makes them an investment that investors should avoid at this time.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

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