Why Warren Buffett Was Right About Gold

Description

It is difficult to fathom the enthusiasm that some investors have for gold and their claims that an epic rally is ahead. Not only is the shiny yellow metal down by a massive 44% from its high price of US$1,921.50 per ounce, but there are signs that its value as an investable asset continues to be eroded.

Let me explain.

Now what?

Unlike other precious metals such as silver, platinum, and palladium, gold has very few industrial uses, and this means that the majority of its demand comes from investors.

As a result, gold, as Warren Buffett famously pointed out, has no utility. Its value is left open to the vagaries of the market, and there are few, if any, fundamental indicators that let us truly predict whether gold will rise or fall.

Then you have to consider that gold is a zero-yield asset.

This makes it a particularly unattractive investment in an environment where interest rates are rising. Now, with the Fed flagging a December rate rise, the price of gold is coming under significant pressure as investors exit gold and move to assets that will provide higher yields.

Here at the Motley Fool, we believe that one of the easiest ways to achieve investing success is by investing in stocks with reliable and steadily growing dividends. This makes gold a rather unattractive asset in which to invest.

Finally, there are the claims that gold is the best store of value, making it the ultimate safe-haven asset and a valuable hedge against economic and geopolitical uncertainty.

This could be the case, but after looking at the data it is clear that gold has been one of the worst-performing and most volatile assets of the last 40 years. We only need to look at recent events in order to see how poorly gold has performed during times of geopolitical and economic crisis, when in theory it should have performed well. These crises include the ongoing economic crisis in Europe, the conflict in the Ukraine, the growing likelihood of a market meltdown in China, and escalating conflict across the Middle East.

However, despite these events gold has remained in a downward spiral to now hover around its lowest price in over six years.

These factors make gold an unattractive investment, and with indicators of a stronger U.S. dollar, gold can only fall further.

So what?

Despite the claims of some industry insiders and analysts, beaten-down gold miners remain highly unattractive investments, and I don't expect to see any recovery in that industry for some time to come. Even industry stalwart **Goldcorp Inc.** (TSX:G)(NYSE:GG) is unattractive because with its cost of production (as represented by its all-in costs) close to the US$1,000 mark, it is only generating a thin margin at the current gold price.

Then you have to consider that Goldcorp used an average price of US$1,300 per ounce to calculate its gold reserves. With gold trading well below this price, it will be forced to revise its gold reserves downwards. This phenomenon won't be restricted to Goldcorp, but will affect the majority of the miners, and this will cause their book value to fall and place further pressure on their share prices.

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2. Metals and Mining Stocks

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