1 Key Risk Every Investor Should Understand

Description

June's Brexit, in which voters opted for the United Kingdom to leave the European Union (E.U.) and market panic ensued, highlighted just how vulnerable financial markets are to geopolitical pressures. This makes it important for investors to monitor, understand, and mitigate the impact of geopolitical risks on their portfolios.

Let's take a closer look at one key risk that has the potential to trigger the next global economic crisis.

Now what?

The Brexit reminded investors that the E.U. is replete with economic and political cleavages that could cause it to slip into crisis or even collapse, potentially triggering the next worldwide economic crisis.

You see, despite the implementation of austerity measures, quantitative easing, and negative interest rates, the Eurozone has yet to experience any meaningful economic recovery. The majority of the economies of its member states are still trapped by burdensome amounts of public debt and ailing banking sectors, curtailing the likelihood of any real economic recovery happening soon.

This becomes clear when looking at Italy, the third-largest economy using the euro, where bad loans in the banking sector come to well over $500 million–a very worrying 21% of GDP. With this equates to a third of all bad debt held by banks in the Eurozone, Italy's fragile banking sector could very well trigger Europe's next economic crisis.

This could spread like wildfire across the region as negative interest rates and quantitative easing fail to throw off the shackles of economic fragility that have engulfed the E.U. since the global financial crisis.

The fallout of such a crisis wouldn't be confined to the Eurozone because the E.U. is the world's largest economy; therefore, such a crisis would inevitably spill over into the global economy.

It would have a sharp impact on commodity prices and could very well contribute to China's economy declining further because the E.U. is its largest export market. The negative effect wouldn't be restricted to commodities such as iron ore, coking coal, copper, or nickel; crude would also suffer because the Eurozone is the world’s single largest importer of oil.

This certainly doesn’t bode well for Canada’s economy. Not only would it place further strain on an already beleaguered energy patch, but it would also adversely affect the economy, because the natural resources sector is responsible for generating 17% of Canada’s nominal GDP in 2015.

The impact wouldn’t stop there; the E.U. is Canada’s second most important trading partner; it receives about 9% of all exports.

So what?

The parlous state of the E.U.’s economy continues to weigh heavily on the global economic outlook and is one of the greatest threats to its health. Among the best ways to hedge against this risk is to invest in precious metals.

Gold and silver have long been recognized as store of values, making them important safe-haven assets. One of the best ways to obtain this exposure is with precious metals streamer **Silver Wheaton Corp.** (TSX:SLW)(NYSE:SLW), which provides diversified exposure to precious metals; gold is responsible for 43% of its revenue and silver for 57%.

It also gives investors the same leveraged exposure to gold and silver as miners but with a far lower degree of risk. This is because it doesn’t operate any mines; instead, it provides funding to miners in exchange for either a royalty from the gold and silver produced or the right to buy it at a price that is significantly lower than the market price.

As a result, it has far lower costs, reporting second-quarter costs of US$4.46 per ounce of silver and US$401 for gold. This means profitability will grow at a greater rate than higher-cost miners as gold and silver appreciates.

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1. Investing
2. Metals and Mining Stocks

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1. Editor's Choice

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1. TSX:WPM (Wheaton Precious Metals Corp.)

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mattdsmith