Billionaires Stan Druckenmiller and George Soros Just Sold Their Gold Stocks: Should You?

Description

Before the election of Donald Trump, the case for gold-stock ownership looked strong, and nobody articulated it better than Stan Druckenmiller, who's averaged 30% returns since 1986. Druckenmiller's case was simple: falling corporate cash flows combined with rising debt (which had diverged to a degree not seen since World War II) along with negative interest rates and record stock valuations made gold extremely attractive.

It was so attractive that Druckenmiller made it one of his largest allocations. Immediately after the election, however, Druckenmiller made the news by stating he had dumped his entire gold position the night of the election; his previous reasons for owning gold are now gone.

His main reason was that Trump's policies will unleash strong economic growth. He thinks for a short-term period of 18 months, Trump's massive tax cuts, de-regulation, infrastructure spending, and rising deficits could lead to economic growth of 4%. This would also come with a rise in interest rates (which is bad for gold prices).

As a result, Druckenmiller is now shorting bonds and betting on the U.S. dollar. Shortly after Druckenmiller made this announcement, it was also revealed that George Soros dumped his gold holdings as well and moved some of the money into energy and pipeline names. Like Druckenmiller, Soros also has an excellent long-term record of returns.

With this in mind, should shareholders of names such as **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX) take profits and exit or continue to hold?

The case against gold

Before looking at some of the positives for gold, it is important to look at the negatives which Druckenmiller explained. There are basically three things that are thought to move gold prices down: a strengthening U.S. dollar, rising interest rates, and falling levels of risk and volatility in the stock market.

Trump's policies should result is rising interest rates and a rising U.S. dollar. These things all come from rising growth, and several of Trump’s policies are sure to boost U.S. GDP growth above currently low levels, at least for a period of time.

Trump is proposing that U.S. corporate taxes be reduced from 35% to 15% and that corporate profits held offshore only pay a 10% tax to come back into the country. At the same time, Trump is proposing up to a trillion dollars of infrastructure spending. These policies would do well for economic growth, which would in turn lead to strength in the U.S. dollar and rising interest rates.

Stronger growth combined with repatriating corporate profits will attract investors to the U.S. dollar, which is why Druckenmiller stated he is bullish on the dollar (this is especially true given weak growth elsewhere in the world). This is bad news for gold, since gold and the dollar typically move opposite to each other.

At the same time, these policies are sure to increase interest rates. The Federal Reserve has been holding off an increase in rates, but Trump’s inflationary policies will likely result in the Federal Reserve hiking rates, starting December, to control future inflation increases. This could also be bad for gold prices, which are commonly thought to decline as interest rates rise.

It likely won’t be as bad for gold as some think

Fortunately, there are some positive tailwinds for gold prices as well. Firstly, while interest rates will be rising, gold prices do not always fall as long-term interest rates rise, especially if the rises are gradual. For example, the World Gold Council stated that over time, average gold returns were positive as long as interest rates increased gradually and didn’t reach extremely high levels (over 4%). Druckenmiller stated that he thinks rates could go to 3%.

In addition, economic headwinds have not disappeared completely. Stock markets are still trading at record valuations, and a recent poll showed that half of economists believe a recession will occur during Trump’s presidency simply due to the fact that the current expansion has lasted so long.

The end result is that investors in gold miners should consider taking some profits if possible, but still keep holdings for the long term.

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