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President Trump or Not, You Should Ignore Everyone and Buy Gold Stocks

Description

The election of Donald Trump as president has had an enormous effect on gold markets. Gold prices plunged over 8% off highs set on election night to levels not seen since June. Many see Trump's election as the end of the bullish case for gold. Rising interest rates are bad for gold prices (since gold pays no yield), and Trump's economic plan has created massive expectations of rising interest rates.

In fact, the 10-year U.S. bond yield was 1.83% on October 31, and since then it has risen to 2.29%. This is a massive increase for such a short period, and this level of interest rate had not been seen since December 2015. To make matters worse, the market now has a nearly 100% expectation that the Federal Reserve will boost short-term interest rates in December.

Markets are expecting that Trump's massive tax cuts and infrastructure spending will be pro-growth, which will in turn lead to rising inflation (and therefore rising interest rates to keep that inflation under control). The markets, however, are missing some key points.

Stock markets are still incredibly overvalued

Gold is likely to do well if stock markets do poorly, and investors are forgetting that President Trump or not, the U.S. stock market is incredibly expensive. It just takes a quick look at some valuation measures to reveal this.

The Shiller price-to-earnings ratio (which looks at earnings for the past 10 years divided by the current price of the U.S. S&P 500 index) is currently 27.07. The long-term average is 16.7, and the market only exceeded these levels three times since 1880—during the Tech Bubble (which ended in a massive crash), before Black Tuesday (which also resulted in a massive crash), and before the Great Recession.

Many say these high values are justified because interest rates are low (which makes stocks more attractive since investors can't earn a good return anywhere else). This may be true, but interest rates are now increasing. During the last debate, Donald Trump said that stocks are in a bubble, and even a slight increase in interest rates would lead to a crash in stock prices.

While it is possible to make a case for record stock valuations in a period of historically low or declining interest rates, with interest rates now normalizing, investors should not expect stock prices to continue growing.

This is good news for gold prices.

There is a risk of a recession

According to a recent *CNN* article, the average period of economic growth is about five years. The current expansion, however, has been going on for seven years. In other words, periods of economic growth do not last forever, and the current period is getting fairly old. This means there is a decent chance that Trump will experience a recession during his first term as president.

A recent survey by *CNN* shows that half of economists think a recession will occur during a Trump presidency, and the fact that the U.S. economy is growing at such a slow pace (only about 2% annually) does not give the U.S. economy much room to avoid a downturn.

During a recession, gold would likely do well as investors flock to gold during periods of uncertainty.

Gold production is set to decline

At the end of the day gold is a commodity like any other, which means that supply and demand also work to control its price. Many think that the global production of gold actually peaked already, and gold production has been contracting since 2013. New gold mines are difficult to come by and are of lower grade, which means it costs more to produce less gold.

This is good news for potential gold stock owners. **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX), is currently trading at levels not seen since March of this year, and being the world's largest and most stable gold producer, now is a good time to purchase shares.

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