Should You Buy Gold Under a Trump Presidency?

Description

Gold equities have given up most of their gains from their fantastic run earlier this year following the sharp sell-off in the physical metal towards the critical US$1,200/oz handle. The reason behind the drawdown can largely be attributed to the certainty of a December interest rate hike in the United States and the ensuing strength of the U.S. dollar, which gold has an inverse relation to.

Further exacerbating gold's bearish outlook are the fiscally expansive policies of president-elect Donald Trump, which are expected to send interest rates (and the greenback) higher. With the fundamental outlook largely negative for gold, should investors forego the precious metal for other opportunities?

Rising inflation expectations are bad for gold

Donald Trump was elected on campaign promises of lower taxes, increased fiscal stimulus, and an outlandish GDP growth target of 3-4% annually. If enacted, all of these policies will be inflationary for an economy that is already close to full employment and might force the U.S Federal Reserve to hike rates at a much steeper rate than originally anticipated.

In such conditions of rising interest rates (both real and nominal), the cost of holding a non-yielding asset such as gold increases, especially when compared to inflation-linked securities such as U.S. TIPS.

fredgraph Image not found or type unknown

Gold vs. 10-year Treasury Inflation Protected Securities (TIPS) – (Source: St. Louis FRED)

Furthermore, gold demand has been trailing supplies in Q3 2016. According to the World Gold Council, gold demand fell 10% year over year, 992.8 tonnes with across-the-board drawdowns in central bank holdings, jewelry production, and bars, largely outpacing gold ETF inflows.

Has gold lost its lustre?

Even though the conditions for the precious metal are looking rather bleak for the time being, a case can still be made to go long gold equities. A study by the CFA Institute has shown that a portfolio with even incremental exposure to gold can significantly outperform equities in other metals such as silver and grossly outperform a portfolio with purely equity holdings.

Moreover, a portfolio with precious metals exposure fared much better during periods of central bank tightening–where we are now–as opposed to easing. But the study does come with a caveat: the performance of the gold-hedged portfolio very much depends on the strength of the underlying equities that make up the asset allocation.

gold-annualized

Image not found or type unknown

Annualized returns of a U.S. Equities only portfolio vs. precious metal exposure (Source: Author generated based on “Can Precious Metals Make Your Portfolio Shine?”- Conover et al., CFA Institute

While the study does not prescribe any specific stocks, attention should be directed towards miners with the fundamental muscle to weather a sustained gold sell-off until demand picks up once again. One such name that should be familiar to all Foolish investors is **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX), which has some of the lowest all-in sustaining costs of the senior miners. Furthermore, Barrick is in the midst of deleveraging its balance sheet and should be debt free within a decade.

So, in summation, don’t worry about the knee-jerk reaction to the Trump presidency; look to use this opportunity to get at least some exposure to the shiny stuff and hold for the long term.

CATEGORY

1. Investing
2. Metals and Mining Stocks

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. NYSE:B (Barrick Mining)
2. TSX:ABX (Barrick Mining)

Category

1. Investing
2. Metals and Mining Stocks

Tags

1. Editor's Choice

Date
2025/08/17
Date Created
2016/11/21
Author
ajtun