Oil’s Latest Dip Makes Now the Time to Invest in Gold

Description

Gold has whipsawed wildly since the end of 2016 because investors are reacting violently to any piece of news regarding the outlook for the global economy and financial markets. While equities recently surged to new highs, oil’s latest plunge, in which it tapped its lowest price in seven months, is good news for gold.

Now what?

Weak oil means lower prices for a wide range of petroleum products that are important elements of modern economic activity, meaning inflation will stay lower for longer. The likelihood of weak crude for the foreseeable future remains high, primarily because of greater than expected activity in the U.S. energy patch, which has caused production to swell.

In fact, it has even been speculated that if crude remains at these levels, the rate of inflation will fall below the levels forecast by the Fed. This reduces the likelihood of the number of rate hikes that have been priced in to financial markets occurring over the course of 2017, which is a positive for gold.

You see, gold and interest rates are negatively correlated. Higher rates increase the opportunity cost associated with holding a non-yielding asset such as gold, particularly when compared to those assets where the yield increases as rates rise.

Furthermore, rising interest rates typically mean that economic activity is growing, making equities and other growth assets superior investments in such an environment.

The likelihood that oil prices will remain constrained for at least the foreseeable future coupled with growing geopolitical risk has caused the outlook for the lustrous yellow metal to improve significantly. This caused gold mining stocks to rally sharply over the last week, propelling the largest gold mining exchange traded fund, **Van Eck Vectors Gold Mining ETF**, almost 3% higher.

So what?

Now is the time for investors to consider bolstering their exposure to gold. While many investors prefer to invest in larger gold-mining stocks, it is the smaller miners and streamers that offer the greatest potential reward.

My top pick among junior gold stocks is **Osisko Gold Royalties Ltd.** (TSX:OR)(NYSE:OR). Since last discussing the precious metals streamer in May this year, it has surged by almost 17%, and there are signs that it has further to rally.

Earlier this month, Osisko purchased a portfolio of 74 royalties and streams from U.S. private equity firm Orion Mine Finance Group for just over $1 billion. The transaction, which was immediately cash flow accretive, not only substantially expanded its asset base, but further diversified Osisko's portfolio by broadening its exposure to silver and adding a diamond royalty. Once bedded down, the deal will give Osisko's earnings a solid boost, which should translate into further gains for its share price.

Because Osisko is a streamer rather than a miner, it does not engage in high-risk mining activities, thereby reducing the risk associated with the investment. Patient investors will be rewarded by its sustainable 1% yield as they wait for the stock to appreciate further.

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