Why a Fear of Conflict With North Korea Is Not a Good Reason to Buy Gold Stocks

Description

The world is a bit on edge due to the crisis between the U.S. and North Korea and the possibility of an imminent conflict. The consequences of a conflict would undoubtedly be far reaching and impact all corners of the world in one way or another. Conventional wisdom says that investors should be buying up gold stocks at a time like this, since the price of gold is likely to increase if a conflict breaks out. However, I'm not convinced this is the case, and you shouldn't be so quick to assume that either.

If you want to invest in gold because the gold mining company is operating well, has strong financials, and you think it has a bright future, then certainly go for it. However, if your main reason for investing in gold stocks is because of a potential conflict, allow me to give you three reasons why you should think twice.

There is no evidence the price of gold goes up due to a conflict

Since 2001, gold prices were on a continuous climb that lasted about a decade, and although there were periods of fluctuation, they did not have any lasting impact. Although there was financial uncertainty and conflict during that time, during the Gulf War in the early '90s, the price of gold actually declined.

A more likely driver of the price of gold could be financial markets overall. The highest level gold ever reached was in August of 2011 amid concerns of debt levels in Europe and also when the U.S. saw its credit rating downgraded.

However, due to the number of factors and economies that can impact the price of gold, it would be difficult to pinpoint any one item as being solely responsible for the price movement, regardless how big the event. People can point to the Financial Crisis in the U.S. during the late 2000s as evidence of a relationship between gold prices and a lack of stability, but gold was rising before that crisis even occurred, when times were good.

An increase in the price of gold doesn't mean gold shares will take off

There are many variables that impact the price of gold, and also many things that can impact a company's overall stock price. Gold prices more than quadrupled from 2001 to 2011, while **Barrick Gold Corp.'s** (TSX:ABX)(NYSE:ABX) stock price more than doubled during this time, and although that is an impressive climb over the course of 10 years, it is certainly not a one-to-one relationship.

Gold stocks are a lot more volatile than the TSX

In the past 10 years, the TSX has outperformed both Barrick Gold and **Goldcorp Inc.** (TSX:G)(NYSE:GG) with a return of over 11%, while the two gold stocks declined by over 30%. This was a time when gold prices fell, but even in the last six months, when the price of gold has been seeing upward momentum, the TSX's losses of 2% have been less than Goldcorp's decline of 15% and Barrick Gold's drop of 8%.

Bottom line

Trying to predict commodity prices is difficult because there are many different variables involved. Stocks driven by commodities also possess a lot of risk, with one example being what has happened to oil and gas stocks in just the past few years. A safer route would be to find stocks that are not impacted by wild swings in commodity prices.

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