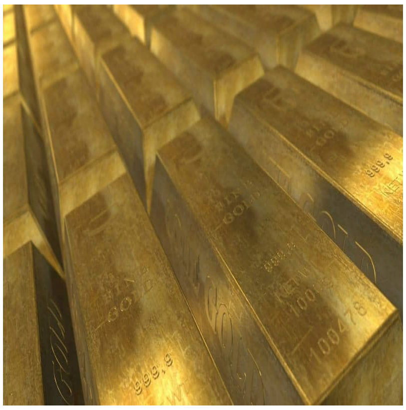

Should Gold Stocks Be on Your Buy List?

Description

Volatility has returned to equity markets in 2018, and that is renewing interest in gold as a way to hedge against future uncertainty.

Let's take a look at the current situation in the market to see if this is the right time to add gold and the miners to your portfolio.

Bull case

Gold is up from US$1,240 per ounce in December to the current price of US$1,350. That's a nice gain for holders of the yellow metal, and more upside could be on the way.

Why?

Analysts are starting to rumble about possible U.S. inflationary threats in the coming years, as a tight labour market in the United States bumps up against the potential for an overheated economy, driven by the Trump administration's stimulative policies. Gold's ability to serve as a hedge against inflation is often debated, but there is a widespread view that it provides protection, especially in situations where an event triggers a short-term spike in prices, as we saw in the late 1970s and early 1980s.

In theory, central banks around the world would step in and raise interest rates to keep inflation in check. That's likely to be the case, but despite the best efforts of the greatest financial minds on the planet, things sometimes get out of control.

The other argument for stronger gold prices is linked to geopolitical and financial market threats. The global economy is in pretty good shape, but concerns over a potential U.S.-China trade war are making investors uneasy. In addition, the war in Syria is straining Russia's relationship with western Europe and the United States. Throw in the ongoing war in Yemen and the unpredictable leader in North Korea, and you get a series of global hot spots that could erupt at any moment and destabilize financial markets.

Bear case

Rising interest rates tend to be negative for gold, as they increase the opportunity cost of owning the non-yielding yellow metal. As rates rise, there is a risk that significant funds could flow out of gold and into fixed-income alternatives.

Higher interest rates in the United States can also put upward pressure on the U.S. dollar, in which gold is priced. That hasn't happened in the past year, however, as the dollar actually lost ground against a basket of key currencies, even as the U.S. Federal Reserve increased interest rates three times.

Should you buy?

Ongoing volatility is expected in the gold market, and investors shouldn't blow off the interest rate headwinds. That said, there is a case to be made for allocating funds to the sector. Gold stocks have not responded significantly to the rise in the price of gold in recent months, and some names could be undervalued today.

For example, **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX) currently trades at $16.30 per share. A year ago, it sold for $26 when gold was below US$1,300 per ounce. The company continues to make progress on its debt-reduction efforts and remains the world's largest producer.

I wouldn't back up the truck, but if you are a long-term gold bull, it might be worthwhile to take a small contrarian position in Barrick, while the stock remains out of favour.

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