Will the Looming Trade War Benefit Gold Miners?

Description

The global economic upswing in conjunction with emerging supply constraints has helped fuel the latest oil rally and generate renewed confidence among financial markets. This has led to a stronger U.S. economy, which along with higher interest rates, have helped buoy the U.S. dollar, thereby hitting precious metals hard. In recent weeks, gold has tumbled, falling from over US$1,340 an ounce to trading at around US$1,223 per ounce. There are concerns that gold could fall further, especially when the Feds hike rates again, which will cause the dollar to firm.

Nevertheless, a range of factors that could give gold a lift in coming months, notably rising geopolitical risk and the Trump administration's approach to trade.

Now what?

Trump has put the world on course for a major trade war. Not only has he slapped tariffs on imports from China, but has also been threatening to put further tariffs in place on up to US$500 billion of Chinese imports. Beijing has threatened to respond in kind while also launching a complaint with the World Trade Organisation (WTO).

If a trade war emerges, it will have a harmful impact on global economic growth. Some economists have estimated that it would destroy 4% of global trade and could shave up to a full percentage point off global gross domestic product (GDP).

Aside from exacerbating the slowdown of an already cooling Chinese economy, it would also impact U.S. economic growth. Consultancy Oxford Economics believes that it would clip 0.1% off U.S. GDP, triggering a noticeable increase in unemployment by wiping out 100,000 jobs during 2019.

The threat an all-out trade war poses to the global economy shouldn't be underestimated when rising oil prices and higher interest rates are also weighing on growth.

In a world where free access to markets and trade liberalisation have been key factors since the end of World War Two, the advent of such a trade war along with other economic pressures could trigger a global recession. If that occurred, the Feds would put interest rate hikes on hold because of a weaker

U.S. economy, which in turn would cause the dollar to soften; that would be beneficial for gold prices.

Any marked decline in economic growth would spark alarm in financial markets, causing investors to stampede for the exits as they hunt for safe haven investments. That would be beneficial for gold because it is perceived to be the ultimate safe haven asset.

So what?

These latest events make it essential for investors to hedge against growing economic risks by investing in gold. One way to gain levered exposure to the yellow metal is by investing in gold miners with proven operations.

A miner that appears attractive at this time is **Detour Gold Corp.** (TSX:DGC). Its share price dropped off a cliff to be 18% lower over the last three months because Detour was forced to lower its 2018 annual guidance. This occurred because of operational changes and outages at its flagship Detour Lake Mine. Forecast 2018 forecast gold production was reduced by to 2% to a maximum of 635,000 ounces while all-in sustaining costs were expected to be 11% greater than originally planned. These revisions are expected to slash free cash flow in half.

However, this has created an opportunity for investors seeking levered exposure to gold. The quality of Detour's operations remain fundamentally unchanged. It has implemented a new mine plan aimed at improving productivity and identifying efficiencies, which, when compared to the original plan, is expected to add an additional 50,000 of gold production for 2019 and 2020. It should also see production and other costs fall, further boosting Detour's profitability. The successful implementation of this plan along with any recovery in gold will give Detour's stock a healthy boost.

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