Gold Price: Should Investors Buy Gold Stocks on the Dip?

Description

Gold stocks pulled back from multi-year highs in recent days. Is the bull run over, or simply taking a pause before another surge higher?

Gold market rally

Gold traded for about US$1,300 per ounce at this time last year. The price started to rally in late May and continued to move higher through the summer months of 2019, driven by fears that the trade war between China and the United States would trigger a global recession.

Gold topped US$1,560 in early September. Profit taking then kicked in and investors moved to the sidelines as reports started to emerge that trade negotiations were making progress between the two economic giants. By late November, gold was back to US$1,450.

At that point, the rally started to pick up steam again, even as an announcement emerged that the United States and China had reached a phase-one trade agreement. The arrival of the coronavirus added new demand in early 2020. Gold surged to US$1,700 in early March. It then tanked with global equity markets through the worst of the crash, but has since recovered. Gold hit a closing high near US$1,770 on April 14, but has trended lower in the past two weeks.

At the time of writing gold trades at just below US$1,700 per ounce.

Gold market outlook

Gold topped US$1,900 in 2011 before the multi-year slide that took it to US$1,050 in late 2015. Investors now want to know if gold and gold stocks are headed to new all-time highs.

Analyst projections are certainly getting more bullish. A year ago, most pundits considered the idea that gold could hit US$2,000 a gold-bug fantasy. Now, several analysts are expecting a move to US$2,000 sometime in the next 12 months. A report from **Bank of America** released April 21 suggests the yellow metal could hit US$3,000 in the next 18 months.

That’s a 50% increase on the bank’s previous target.

The call points to a long-held belief among gold lovers that the world will one day lose confidence in all fiat currencies and investors will rush to buy gold to protect their wealth. “Paper money”, they claim, will be worthless. If that day arrives, we will all be in serious trouble.

Governments around the world are cutting interest rates and unleashing unprecedented monetary and fiscal stimulus programs to battle the worst economic slowdown since the Great Recession. Trillions of dollars of government debt already trades at negative rates. In this environment, no-yield gold starts to look pretty good.

On the supply side, there might also be an incentive to buy gold. Lockdowns are hitting gold production at a time when demand is rising. In addition, new high-grade deposits are harder to find.

The rise in the price of gold is impressive over the past year, but it doesn’t appear to be driven by rampant speculation. As such, more upside could be on the way and the US$3,000 target in the next 18-24 months doesn’t sound so unbelievable, especially in the current environment.

Should you buy the dip in gold stocks?

The share price of a popular ETF that tracks gold mining stocks, TSX:XGD, is down about 5% in the past week. That’s not a significant pullback, given the fact it is up 70% since March 13.

Profit taking could continue in the near term if investors start to rotate more funds out of gold miners and back into cheaper sectors on the hopes that the worst of the pandemic is over. As such, I wouldn’t back up the truck right now.

That said, the outlook for gold and gold mining stocks over the next five years should be positive. If your portfolio is underweight gold, or you are a strong believer in the long-term bull case for the precious metal, it might be a good idea to start adding exposure on any additional weakness.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

1. TSX:XGD (iShares S&P/TSX Global Gold Index ETF)

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Date
2025/08/16
Date Created
2020/05/01
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