Gold Price Crash: Should You Buy Gold Stocks Now?

Description

Gold just pulled back off the record highs and mining stocks gave up a chunk of their recent gains. Momentum investors who missed the big rally are now wondering whether this is a good time to start a new position in gold stocks.

Gold price threats

Gold fell US$150 per ounce in recent trading, from the record near US$2,050 to below US$1,900. The price of the yellow metal is back to US$1,950 at the time of writing.

Gold stocks saw a round of profit taking, as well. Most of the big names are down more than 10% from the recent highs.

The sell-off came as a result in a jump in U.S. treasury yields. As bond prices fall, their yields increase. This makes treasuries more appealing for safe-haven investors. The knock against gold is that it doesn't provide any yield. As such, any increase in treasury yields tends to be negative for the price of gold.

We could see bond yields continue to creep back up in the near term, especially if the US economy appears headed for a V-shaped recovery. Any positive news on a COVID-19 vaccine in the next few months would also likely put pressure on gold prices.

The pullback was expected. Gold surged from US$1,800 on July 16 to a closing high of US$2,069 on August 6. That's a massive move over a short period of time. Further downside wouldn't be a surprise in the coming days or weeks.

Gold price support

The rally actually began in the spring of last year. In fact, gold rose more than 50% since late May of 2019. The surge through the end of 2019 came as investors searched for a safe place to park cash amid ongoing trade tensions between the United States and China. That situation remains in place and the rhetoric could escalate as the U.S. election approaches.

The pandemic provided another boost to gold demand. Plunging bond yields across the globe and unprecedented stimulus measures by central banks sent interest rates and treasury yields to very low levels. Negative yields already existed in Japan and parts of Europe.

Monetary and fiscal stimulus efforts are expected to continue. Some economists say it is just a matter of time before the U.S. joins the negative-rate club. In that scenario, the price of gold likely has more room to run.

Analysts continue to maintain lofty targets for the gold price. In the past week I saw estimates ranging from US$2,100 to US$3,000 for the next 12-18 months.

Should you buy gold stocks now?

Near-term volatility should be expected, but investors might want to start nibbling on any additional downside. Gold miners can generate significant profits at current gold prices.

Barrick Gold, for example, just raised its dividend by 14%. The company uses US$1,200 as its assumed long-term gold price when making investment decisions. Barrick Gold's balance sheet is arguably the strongest in the company's history right now and the stock appears cheap in the current environment.

Barrick trades near $35 per share at the time of writing. The stock recently topped $40. It traded above $50 back in 2011 when gold hit its previous peak just above US$1,900.

Conditions remain favourable for higher gold prices in the medium term. Investors without exposure to the market can take advantage of the latest pullback to add gold miners to their portfolios.

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