Barrick Gold (TSX:ABX) Soars: Should You Follow Warren Buffett to Safety?

Description

Warren Buffett's new stake in **Barrick Gold** (TSX:ABX)(NYSE:GOLD) likely shocked many investors. We all knew that the Oracle of Omaha has been playing it cautious amid the COVID-19 pandemic, given the risk that the world economy could fall into a depression. However, having slammed gold as an investment many times in the past, many may be fearful that Buffett's newfound love for gold may be a sign that we could be due for a rerun of the years that followed the 1929 stock market crash.

Warren Buffett may be playing it cautiously, but that doesn't mean we're in for an imminent market meltdown. Heck, Buffett's stake in Barrick Gold is still dwarfed by many of his other equity holdings that could get clobbered if the markets were to crash. So, before you conclude that Buffett is the market's new biggest bear, I'd urge you to take overly ominous commentary over Buffett's recent gold stake with a fine grain of salt.

Why? I believe Warren Buffett is merely adapting to the times with his latest gold investment.

The U.S. Fed is printing ridiculous sums of money, and the risk of a sudden surge in inflation is a threat to Buffett's massive cash position. To Buffett, gold may be an unworthy asset in normal market conditions. Today, the markets are anything but normal. Given near-zero interest rates and the rising threat of inflation, gold suddenly went from being an unproductive, unworthy asset to becoming a vital hedge against both inflation and volatility. That's not to say Barrick stock is a safe investment that's without its own slate of risks, though.

Gold shines in an unprecedented environment like this

In a prior piece, I recommended Barrick Gold stock as my preferred way to play a second market crash. I was a huge fan of the management team and the fact that the company had a bountiful dividend that was likely to grow at an above-average rate over time. I was also an advocate of allocating up to 5-10% of one's portfolio to high-quality gold miners like Barrick to combat both market volatility and pandemic-induced inflation risks, also noting that gold and gold miners were akin to some sort of insurance policy against a plunging market.

“Gold stocks are like an insurance policy for your portfolio. When the broader market melts down, and there’s a liquidity crunch amid a panic-driven rush to the sidelines, gold stocks can hold their own. They’re one of the few stocks [capable of] trading in the green in a market-wide sea of red.” I said.

“Gold isn’t just a great way to help your portfolio lower its beta (ABX sports a 0.33 beta), but it’s also a great inflation risk that pays a 1.1% dividend yield (it’s not much, but for a gold miner, it’s something!)”

Should you follow Warren Buffett by scooping up shares of Barrick Gold?

Barrick Gold is the gold standard when it comes to gold miners.

Still, after surging 11.3% on Monday, following news of Buffett’s stake, you’d be paying a hefty Buffett premium to get into the stock here. While I am a massive fan of Barrick and gold as an investment in this kind of wild market, I’d be reluctant to recommend the stock after such a profound single-day pop and would encourage investors to wait for a meaningful pullback before considering initiating a position.

Barrick is a wonderful business, and it’s a good idea to stand in Buffett’s corner, but one must not neglect the stock’s valuation, which is now far too stretched. As gold prices continue on the retreat, Barrick could be at risk of pulling back, and you may get a chance to get a better cost basis than the Buffett over the coming months, especially we’re in for some good vaccine news.

I think Buffett is merely hedging himself against the threat of inflation with his stake in Barrick and don’t think the stock is undervalued or ripe for a near-term bounce. As such, I wouldn’t follow Buffett if you seek to make a quick profit by riding on his coattails because odds are, you’ll likely lose money.

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joefrenette