



Warren Buffett Buys Barrick Gold (TSX:ABX): Should You Own Gold or Gold Mining Stocks Today?

Description

Warren Buffett shocked markets in recent days when his **Berkshire Hathaway** revealed a new position in **Barrick Gold** ([TSX:ABX](#))(NYSE:GOLD) stock.

Barrick Gold stock rally

The news sent Barrick Gold's share price soaring by more than 10%. It also lifted the stock prices of most major gold mining companies as well as the price of [gold](#) itself and that of ETFs focused on gold or gold mining stocks.

The US\$562 million investment in Barrick Gold by Berkshire surprised long-term Buffett followers. The Oracle of Omaha, as he is known, has historically presented a negative view on gold.

It's true that the yellow metal isn't really good for much other than making jewelry. However, gold has an appeal as a safe-haven investment.

The case for owning gold vs. the gold miners

Gold is expensive to store and the price can be volatile, but owning the metal directly or through a gold ETF avoids some of the potential risks associated with the gold miners.

Mining companies often operate in countries where government intervention can quickly turn a positive asset into one that is essentially worthless. At the very least, operations can be halted for months, as local politicians look to rewrite agreements on fees, taxes, or royalties.

Mining stocks also come with environmental risk. Nasty chemicals are used to extract gold from the rocks. Wastewater ponds sometimes leak. Lawsuits are always a risk, especially when something goes wrong.

Equipment can fail, fuel costs can rise, workers might go on strike. Activists sometimes disrupt operations. Pandemics can shut down production.

Owning the metal, rather than betting on the gold miner, removes much of these risks. In fact, the drop in production across the industry this year due to COVID-19 hurts revenue for the mining companies but tightens supply and supports higher gold prices.

The case for owning gold miners instead of gold

Berkshire's decision to bet on a single gold miner, rather than a basket of top mining [stocks](#) or the metal directly, relates to perceived value. Taking on all the added risk must be justified by the upside potential the firm sees in Barrick Gold's share price.

In effect, the bet assumes the stock is very cheap relative to Barrick Gold's earnings potential in the near to medium term.

Barrick Gold is the second-largest gold mining company on the planet. The firm owns five of the top 10 mines in the world and has annual production as high as five million ounces of the yellow metal. The balance sheet is in great shape thanks to an aggressive turnaround program that monetized non-core assets and reduce debt in recent years.

Gold's significant price rise means Barrick now generates strong cash flow. The board just raised the dividend by 14%.

The share prices of gold miners tend to rise or fall more than the price of the metal. For example, Barrick Gold's share price is up 67% in 2020. The price of gold is up about 32%.

Is gold or Barrick Gold a better bet?

The market factors providing the tailwind for gold and the gold mining stocks should remain in place through the end of 2020 and into next year. Negative bond yields, the U.S. election, trade tensions with China, the pandemic, and massive stimulus measures by central banks should all be supportive of higher gold demand, as investors seek a safe place to put cash.

If you want the conservative way to play the gold rally, go with an ETF that simply owns bullion or buy gold bars at your bank. Otherwise, Barrick Gold or a gold miner ETF might provide a shot at better gains but would also bring more downside risk when sentiment reverses.

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aswalker

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