



Inflation Alert! Buy Gold Stocks to Protect Your Portfolio

Description

The U.S. federal reserve did something incredible this week. They tried to convince us that inflation, especially increased inflation, is a good thing. Even though many news outlets forecasted this eventuality, I still sat with my jaw hanging open when I heard it from the chairman himself.

I suppose it makes sense from their point of view. Global economies, including the U.S. and Canada, now have a ton of debt on their balance sheets. The increased debt loads are essentially liabilities that the central banks and governments have transferred from companies and individuals to public ledgers in an attempt to keep economies moving.

It was no secret that many countries at all levels were highly indebted to going into the health crisis. We were in no shape to face a crisis, so the government stepped in to keep things going.

Inflation

There are basically three ways for countries to get rid of debt. They can tighten their belts and enforce austerity, pay back debt slowly with increasing domestic earnings, or inflate their way out of debt by increasing inflation, so countries can pay back debt issued with more expensive dollars with cheaper ones as inflation erodes the value of the earlier debt.

Austerity is painful, as was seen in the case of Greece back in the early 2010s. No one wants to go through a painful period of less spending where standards of living are reduced and jobs are lost. In democratic nations, austerity can be political suicide.

The second way to reduce debt is through debt repayment based on improving economic conditions. At the moment, this possibility seems pretty impossible. We are going through a massive recession that could get worse in a hurry if government supports are reduced.

That leaves debt reduction through inflation. Essentially, this strategy comes down to governments debasing currencies through money printing. Debt borrowed in yesterday's dollars is cheaper today since they become progressively cheaper as money-printing continues.

Invisible tax

Although inflation is beneficial for the highly indebted, it is painful for anyone holding cash. Anyone who holds their savings in dollars is taxed by having their spending power taken from them by central banks. You lose purchasing power as your dollar decreases over time.

You can protect yourself by owning an asset like gold. Gold is considered to be a hedge against inflation. One piece of gold stays as one piece of gold. You can't print more. So, as currencies lose value, gold increases relatively in value.

Gold stocks

If you believe that gold is an inflation hedge, it can pay to own gold stocks. Companies like **Yamana Gold** ([TSX:YRI](#))([NYSE:AUY](#)) are frequently [dividend-paying](#) organizations that are even starting to raise their payouts. Investors no less famous than Warren Buffett have begun buying into gold names, so you have to assume that there is potential for capital appreciation.

Many companies, Yamana included, are even raising their payouts. Yamana, for example, has [raised its dividend](#) four times over the past couple of years. Those increases amount to a total cumulative increase of 250% over the past year. At the current stock price, Yamana now pays a dividend of 1.22%.

If inflation is a thing, and gold prices continue to rise, then it is reasonable to assume that gold companies will continue to generate increasing earnings and free cash flow. In Q2 2020, for example, Yamana generated 60.3 million in free cash flow. That powered its dividends as well as \$101 million in net debt repayments.

The bottom line

Inflation kills your savings, but it is a boon for the gold sector. It is wise to have holdings of gold companies like Yamana. Many companies are using their increasing free cash flow to do the right things such as increasing dividends and paying down debt. Those choices will pay off in a rising gold price environment and protect your investments from inflation.

CATEGORY

1. Investing

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1. NYSE:AUY (Yamana Gold)
2. TSX:YRI (Yamana Gold)

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