# Gold's precious mettle

## Gold is back in the limelight. But now there's a better way of investing in the precious metal than just buying bullion

Once again, political and economic uncertainty is pushing to the fore gold's attractions as an investment haven. But this time investors wanting to allocate capital to the precious metal have a better option than just buying bullion bars or futures contracts. Gold mining stocks are looking particularly good value. Indeed, gold miners have become such an attractive proposition that they're proving irresistible to some of the industry's best informed bargain hunters – their rivals.

Ever since Barrick Gold took over Randgold Resources last September for $6 billion – and then followed up with a hostile $18 billion bid for rival Newmont in February – there's been growing enthusiasm for mergers and acquisitions in the sector.

When miners start acquiring each other, this suggests the market is under-pricing the value of their assets, namely the gold they've yet to mine. What's more, not only are gold miners' stocks attractively valued relative to their reserves and the price of bullion, but also compared with the materials sector as a whole and with global equities in general.

Gold mining stocks are trading at a price-to-book ratio of 1.4 times against a 10-year average of 1.9 times. And valuations are well below those of the wider materials sector and global equities, on ratios of 1.5 and 2 times respectively[1]. The sector was hit hard by a downturn earlier in 2018 in gold prices and has been slow to recover.

We've responded accordingly, broadly taking as much of a position in gold mining stocks as in the precious metal itself – around a 2 per cent weighting in each (as at March 2019).

### Hedging with gold

But while we see good potential upside in gold miners from further industry consolidation, their main attraction is as a relatively inexpensive proxy for the precious metal itself. Gold is attractive because it doesn't move in lockstep with other major asset classes, and also has a habit of showing its mettle during times of crisis.

Take last autumn. In October, when most investors were caught flat-footed as both equities and bonds simultaneously headed south, gold bucked the trend. It has continued to rise since and has gained some 10 per cent since the start of the fourth quarter of last year.

As Dirk Baur at Dublin City University and Brian Lucey Trinity College Dublin explain, "gold is a hedge against stocks on average and a safe haven in extreme stock market conditions."[2] That's to say, although gold is just a moderate hedge against equities and bonds during normal market conditions, it's a very good one in times of crisis.

And that's particularly relevant now given that many parts of the world are in the grip of political upheaval. On their own, the trade show-down between the US and China, Brexit and increasingly regular bouts of political turmoil in Italy would be enough to justify taking out some crisis insurance. But add to that a sea-change in global monetary policy, and investors have plenty to contend with.

For instance, there is still a risk that central banks could overdo policy tightening by missing warning signs of an economic slowdown. Alternatively, even if, say, the US Federal Reserve puts the brakes on further interest rate hikes this year, it doesn't have a great deal of leeway to support growth in case of economic weakness. Notwithstanding that the Fed has been raising rates since the end of 2015, US borrowing costs are still near historic lows. Meanwhile, stopping the Fed's balance sheet reduction is one thing, restarting quantitative easing would be quite another. The former is eminently possible, the latter, politically hazardous.

Instead, any economic boost will most likely have to come in the form of further fiscal stimulus. With deficits already high, that becomes strong medicine with seriously inflationary side-effects. And as real asset, gold provides a good haven against an inflation-inspired erosion of the dollar's value.

Meanwhile, in a world of low interest rates, the opportunity cost of holding gold – forgoing yields on income-generating assets – declines.

**Written by Andrew Cole, head of multi-asset, London, Pictet Asset Management**



[1] MSCI Materials and MSCI ACWI indices. Data as at 31.12.2018.
[2] "Is Gold a Hedge or a Safe Haven? An Analysis of Stocks, Bonds and Gold" Dirk Baur and Brian Lucey, The Financial Review 45 (2010) p. 217