



of San Diego

HOME

PLANNER RESOURCES

SHOULD YOU RUSH INTO GOLD?

Gold is back, with a vengeance. Should you invest in it?

After languishing in investment exile through much of the 1980s and 1990s, down as much as 70 percent from its January 1980 high of \$850 an ounce and outshined by financial investments such as large cap stocks and bonds, gold is making a splashy return. The price of gold hit a seven-year high in October at \$390 an ounce. Gold stock mutual funds were the top-performing mutual funds in 2002, with returns around 85–100 percent, and a gold mining company was the top-performing large-cap stock, returning 52 percent. And in 2003, gold mutual funds were up 26 percent through September, according to Lipper Inc.

So, should you buy gold? If you do, in what form? What percentage of your portfolio should you devote to it? Whoa, not so fast, caution many financial planners. Gold may have a place in your portfolio, but it should be a small one at best.

Gold traditionally has been viewed as a hedge against wars and political unrest, high inflation, or other uncertain economic times. And some people just like the idea of owning an investment they can hold, if only theoretically, in their hands.

Because of its defensive quality, gold has a low correlation with most other types of investments—that is, it typically doesn't move up and down in concert with stocks, bonds, cash or real estate. If they're down, gold is apt to be up, and vice versa. That's why some investment experts often like to include it in portfolios. Despite its volatility, its inclusion can actually reduce the risk and boost the overall returns of a portfolio—as long as gold comes in small doses.

While some gold enthusiasts recommend allocating as much as one-third of a portfolio to gold and other precious metals, most financial planners recommend keeping gold to five

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percent or less. Investors with small portfolios probably shouldn't bother with gold at all, and some planners think that admonition should apply to all investors. They prefer clients invest instead in real estate investment trusts or even commodities as assets with low correlations to stocks and bonds.

A big challenge for including gold in a portfolio is the investor's willingness to suffer through long stretches of steep declines or simply mediocre returns. Despite the huge returns in 2002 and 2003, gold funds over the past ten years annually returned a paltry 1.3 percent, according to Lipper Inc.

Another risk is that, as so often happens with investments that suddenly become hot, investors may have missed much or even all of the recent run-up. Some gold experts expect prices to continue to climb, perhaps to \$600 an ounce, particularly if U.S. deficits continue to grow, the economy struggles and terrorism holds center stage. But if the economy and the world scene improve, the price of gold could quickly stumble, though demand for gold as a commodity might offset the decline.

As is usually the case when it comes to investing, it's better to have a well-diversified portfolio in place at all times. That way, when an asset gets "hot," you already own that asset and are able to take advantage of its run-up. Loading up on an asset after it becomes hot usually means you end up buying high and selling low—exactly what happened to many investors who came late to the high-tech party in the 1990s.

Still think gold might have a place in your portfolio? You have several ways to buy gold. The easiest way is to buy gold-mining stocks, either directly or through stock mutual funds. Just be aware that the price of gold-mining stocks usually rise—and fall—much faster than the price of gold itself. Also be aware that fees for gold stock funds, as is common with sector mutual funds, typically run significantly higher than for large and mid cap mutual funds.

While direct ownership of gold is less volatile, it's a more difficult way to own gold. You can buy gold coins, but they have their own volatility. You also can buy gold bullion from brokers, but transaction costs and storage fees typically are steep.

Gold, along with other precious metals, is also ripe for investment scams. So be cautious how and where you buy gold—if you buy gold at all.