STONEBRIDGE
Capital Advisors

Is Gold a Good Investment?

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INTRODUCTION

Gold is a precious metal that has been used for millennia in artifacts, jewelry, coins, and industrial purposes. Along with its beauty and utility, gold served as a medium of exchange in ancient times and as the basis of the world's monetary systems while operating under the Gold Standard until 1971.

During times of severe economic and market stress, gold has been a more stable store of value versus other financial assets. Gold is also considered a hedge against inflation. But is gold a good investment and does it make sense in a diversified portfolio?

Gold has been a good store of value.

Gold is a physical, precious metal with a long-duration life. Gold has been an important store of value due to its relative rarity, ability to track general price fluctuations over time and acceptance as a means of payment for all types of transactions.

Global Central Banks understand these unique characteristics by maintaining reserve assets in gold with Central Banks holding approximately 20% of all the gold that has been mined throughout history (World Gold Council – Gold Reserves by Country).

Because of its status as a reserve asset and its intrinsic value characteristics, gold has favorably weathered significant stock market corrections. During rising economic and/or geopolitical uncertainty that can cause stock prices to decline, investors may reduce exposure to more volatile assets, such as stocks, and seek out "safe haven" assets like U.S. Treasuries or gold.

Gold can act as an inflation hedge.

Gold has traditionally been viewed as an effective hedge against inflation, which is the broad increase in the prices of goods and services in an economy. For example, during the 1970's, gold experienced a dramatic increase in price during a period of very high inflation, while for most of the 1980's and 1990's, gold prices declined, despite modest inflation throughout the period.

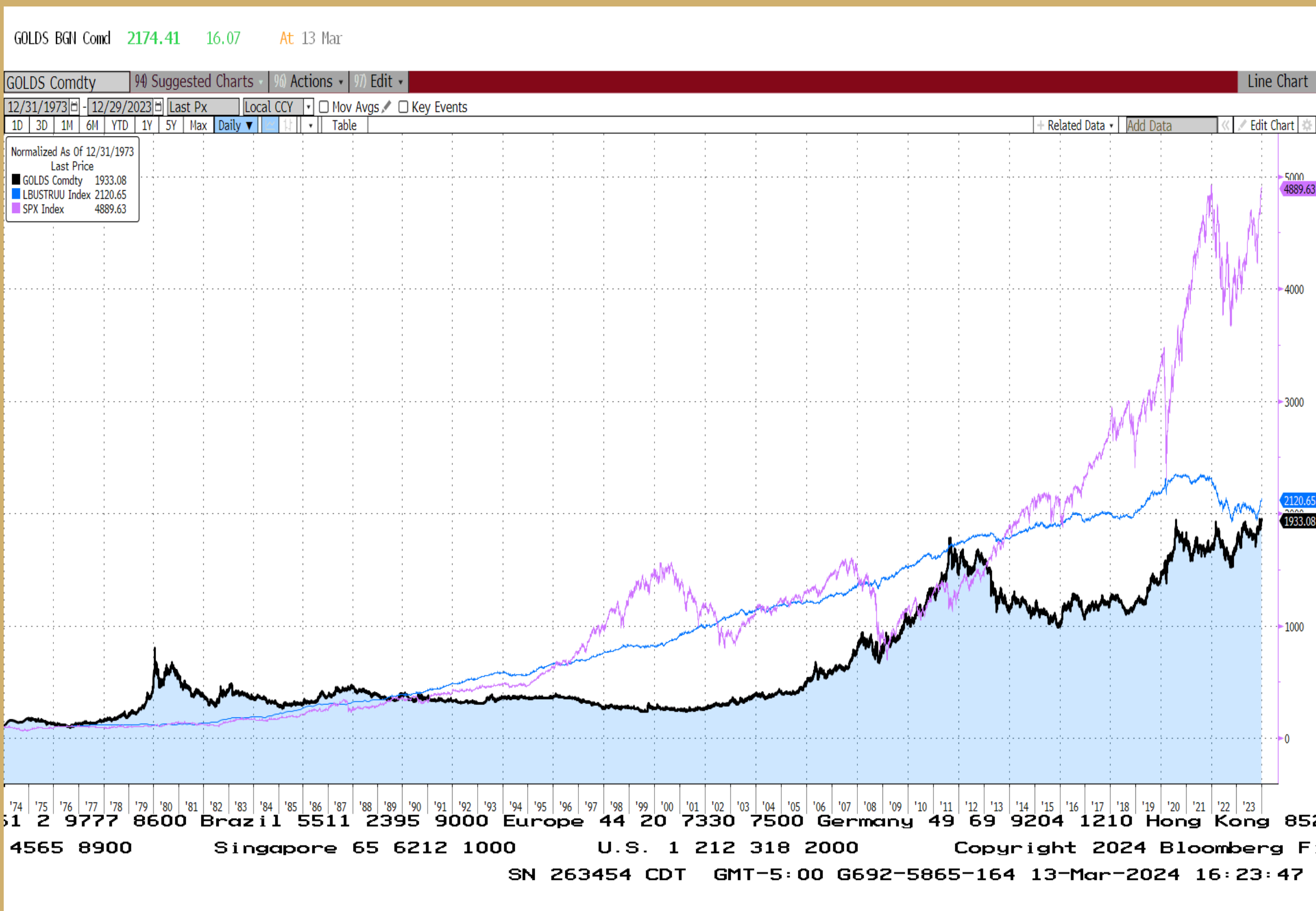
More recently, gold prices have increased with higher inflation, money supply growth and rising global uncertainty. Over the long-term horizon, gold prices generally track consumer prices and monetary dynamics. However, it is important to note that gold prices can divert from short term inflation trends.

As an investment, gold is more volatile than stocks.

Gold's historical risk and return can be compared to other investments such as stocks, bonds, REITs, and other alternative assets. Gold could be considered a risky asset because its historical risk profile is more akin to stocks than bonds. Over the last 50 years, gold provided a lower return with more risk than U.S. Large Cap Stocks. Over the last 20 years, gold has provided a greater return with more risk than stocks, as indicated by Graph 1. While it is always difficult to predict future returns, investors should have a higher risk tolerance when investing in gold due to its elevated risk profile.

Graph 1 | Price of Gold, S&P 500, Bloomberg U.S. Aggregate

Indexed to 100, Last 50 Years



***Source**: Bloomberg Finance L.P. (03/13/2024)*

Why is the price of gold volatile?

Gold prices will fluctuate with changes in supply and demand, as well as changes in interest rates, differences in foreign exchange and geopolitical dynamics. Gold differs from many asset classes because it does not produce an income stream, while investments such as stocks and bonds produce dividend and interest income that can help mitigate volatility.

How do I invest in gold?

Gold can be owned as bullion, coins, jewelry or through financial assets tied to gold. Ownership of physical gold may create costs related to storage and insurance. Physical gold ownership can be less liquid than other financial assets due to delivery requirements and dealer markups. Investors can gain access to gold without physical ownership through investments that hold gold including mutual funds and exchange traded funds.

Gold's place in a diversified portfolio.

Individual investments, whether stocks, bonds or alternative assets, generate returns with risks associated with those returns. To achieve a higher return, an investor must be willing to accept additional risk. The risk and return characteristics of individual investments are important elements to determine a portfolio's expected return and risk profile. An additional key consideration of efficient portfolio construction is the interaction between the individual investments and asset classes held in the portfolio.

Investments that move in the opposite direction of one another can lower the overall risk profile of a portfolio. The price of gold tends to move independently from stocks and in the same direction as bonds. Gold's unique interaction with stocks means adding gold can improve portfolio diversification by lowering the expected risk of a portfolio. Because gold tends to move directionally with bonds, some of gold's diversification benefit is reduced in a portfolio that holds bonds.

Does Stonebridge use gold when building client portfolios?

Stonebridge has not utilized gold because we believe efficient portfolios can be built with traditional stocks, bonds, and cash. Gold has been a store of value during volatile markets, but U.S. Treasury Bonds have generally performed well as a safe haven during stock market corrections. While gold traditionally has been an inflation hedge, stocks have also been an effective hedge against inflation because companies can grow earnings and dividends by passing through higher prices to customers. Higher earnings and dividends generally lead to higher stock prices.

Over the long term, gold has experienced more volatility with lower returns than stocks. This means gold has not been as efficient as stocks in producing returns versus the risks assumed. Gold also does not produce an income stream like bonds and dividend paying stocks, which historically, has been an important driver of portfolio returns.Gold as an isolated investment has many positive attributes, many of which are also captured by traditional asset classes. Stonebridge believes efficient portfolios built with stocks, bonds and cash will continue to serve our clients through market cycles that include favorable and unfavorable investing environments.

Sources: *Invest in Gold – A Portfolio Diversifier with Staying Power, Gold White Paper, Q1 2024, State Street Global Advisors; World Gold Council; Bloomberg*