

# Why Own Gold?

## The Facts on Why Gold Is a Good Investment

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There are six primary reasons why investors own gold:

1. [As a hedge against inflation.](#)
2. [As a hedge against a declining dollar.](#)
3. [As a safe haven in times of geopolitical and financial market instability.](#)
4. [As a commodity, based on gold's supply and demand fundamentals.](#)
5. [As a store of value.](#)
6. [As a portfolio diversifier.](#)

Gold is a monetary metal whose price is determined by inflation, by fluctuations in the dollar and U.S. stocks, by currency-related crises, interest-rate volatility and international tensions, and by increases or decreases in the prices of other commodities. The price of gold reacts to supply-and-demand changes and can be influenced by consumer spending and overall levels of affluence.

Gold is different from other precious metals such as platinum, palladium and silver because the demand for these precious metals arises principally from their industrial applications. Gold is produced primarily for accumulation; other commodities are produced primarily for consumption. Gold's value does not arise from its usefulness in industrial or consumable applications. It arises from its use and worldwide acceptance as a store of value. Gold is money.

In contrast to other commodities, gold does not perish, tarnish or corrode, nor does gold have quality grades. Gold mined thousands of years ago is no different from gold mined today. Therefore, gold existing in the aboveground gold stock is interchangeable with newly mined gold.

The early 1980s presented a once-in-a-lifetime opportunity to buy stocks. Today, the opportunity appears to be in gold: the market conditions that are plaguing your stock portfolio are jet fuel for hard assets.

Like today, the 1970s were a time of huge budget deficits, loose monetary policy, energy-supply challenges and open-ended wars. Today, the combined costs of waging the wars in Iraq and Afghanistan and fighting terrorism at home are eating up bigger and bigger chunks of the nation's gross domestic product. The U.S. government is facing seemingly insurmountable budget and trade deficits, compounded by trillions in unfunded liabilities stemming from entitlement programs such as Social Security and Medicare.

In the coming decade, as the dollar likely suffers one of the great meltdowns in monetary history, gold will reclaim its place at the center of the global financial system. Gold's value, relative to most national currencies, has soared to new records. Central banks – especially those in China, India and Russia – have stopped selling their gold and instead are buying it by multiple tons, helping to drive up the price.

**Take a look at the following summary of the six primary reasons for investors to own gold. They may never be more relevant than they are today.**

## **1. HEDGE AGAINST INFLATION**

Gold is renowned as a hedge against inflation. The most consistent factor determining the price of gold has been inflation - as inflation goes up, the price of gold generally goes up along with it. Since the end of World War II, the five years in which U.S. inflation was at its highest were 1946, 1974, 1975, 1979, and 1980. During those five years, the average real return on stocks, as measured by the Dow, was -12.33%; the average real return on gold was 130.4%.

Today, numerous factors are conspiring to create the perfect inflationary storm: extremely stimulative monetary policy, multibillion-dollar bailouts for banks and corporations, a precarious dollar, a mammoth trade deficit, and America's status as the world's biggest debtor nation. In a vote of no confidence for the dollar, gold and other commodity prices are breaking tradition and continuing to rise even when the dollar rallies.

## **2. GOLD - HEDGE AGAINST A DECLINING DOLLAR**

Gold is bought and sold in U.S. dollars, so any decline in the value of the dollar causes the price of gold to rise. The U.S. dollar – for now – is the world's reserve currency: the primary medium for international transactions, the principal store of value for savings, the currency in which the worth of commodities and equities is calculated, and the currency primarily held as reserves by the world's central banks. However, now that it has been stripped of its gold backing, the dollar is nothing more than a fancy piece of paper. Indeed, the greenback's value has been shored up amid Europe's sovereign-debt crisis, but its future will not be so bright when the United States' own debt disaster begins to hit home in the coming years.

## **3. GOLD AS A SAFE HAVEN**

Gold has often been called the "crisis commodity" because it tends to outperform other investments during periods of political or economic tension. The very same factors that cause other investments to suffer will traditionally cause the price of gold to rise – which is why having some of your assets allocated to gold investments makes such a stable, robust portfolio.

As national debts rise, banks fail, and currencies around the world begin to lose value, governments rescue themselves with the printing press, making their currency worth less and gold worth more. Gold has always risen the most when confidence in government is at its lowest.

## **4. GOLD - SUPPLY AND DEMAND**

Demand for gold is outpacing supply. Gold production is declining. Opening a new mine takes about seven years of preparation on average, making it hard to address the supply issue quickly. Global gold production has not surpassed its record output in 2000, leading some experts in the mining industry to wonder whether the world has hit “peak gold.”

## **Growing Demand - China, India and Central Banks**

Both China and India have been purchasing unprecedented quantities of gold, not only at the central-bank level but also by encouraging their increasingly well-off citizens to accumulate bullion. With the greenback looking increasingly frail over the long haul, China will only be buying more gold in the future as it attempts to divest itself of some of its estimated \$2 trillion in U.S. dollar reserves.

Demand for gold also is surging from central banks, which have become net buyers since 2009 after several years of selling an average 400 tons per year. In fact, central banks last year added the most gold to their reserves since 1964. The official sector looks to be net buyer of gold for years to come.

## **5. GOLD – STORE OF VALUE**

One major reason investors look to gold as an asset class is because it will always maintain an intrinsic value. Gold will not get lost in an accounting scandal or a market collapse; it will never be just a worthless piece of paper. Economist Stephen Harmston of Bannock Consulting had this to say in a report for the World Gold Council:

“Although the gold price may fluctuate, over the very long run gold has consistently reverted to its historic purchasing power parity against other commodities and intermediate products. Historically, gold has proved to be an effective preserver of wealth and a safe haven in times of economic and social instability. In a period of a long bull run in equities, with low inflation and relative stability in foreign exchange markets, it is tempting for investors to expect continual high rates of return on investments. It sometimes takes a period of falling stock prices and market turmoil to focus the mind on the fact that it may be important to invest part of one’s portfolio in an asset that will, at least, hold its value.”

## **6. A CRITICAL REASON ON WHY IT’S IMPORTANT TO OWN GOLD: PORTFOLIO DIVERSIFIER**

Investment advisors recognize that diversification of investments can improve overall portfolio performance. Gold is the ideal diversifier for a stock portfolio, simply because it is among the most negatively correlated assets to stocks – which means, when stocks go down, gold goes up.

The key to diversification for risk reduction is finding investments that are not closely correlated to one another. Most stocks are closely correlated and most bonds are closely correlated with each other and with stocks, but gold reacts to a different set of market conditions entirely.

Gold also serves as a hedge against the erosion of the purchasing power of paper money, known as currency devaluation. Although the price of gold can be volatile in the short-term, gold has maintained its value over the long-term even – or perhaps especially – when currencies fail.