



# HEAVY METAL

## Precious metal investing

April 2009

The mere mention of buying gold or silver usually elicits a variety of responses: dismissive, rolling eyes to eager, heightened eyebrows. Regardless of one's inherent investment bias, there are times when precious metals deserve some portfolio consideration. Is now one of those times? While it may seem we are arriving late to the party, as gold has risen 3 fold in the past decade<sup>i</sup>, I contend the band is just warming up. In this month's *Fiscal Fitness*, we'll consider the timing, appropriateness and vehicles for precious metal investing.

### Timing

Successful investing in gold, silver, platinum, & palladium is all about timing. From a macro-economic view, metals usually do well during inflationary and uncertain economic periods. Currently, the economic malaise is in full force and we sense the inflationary pressures will begin to be felt within the next 6-12 months. The unprecedented fiscal stimulus should eventually pressure the US dollar (precious metals are all priced in American dollars). Additionally, the entire Fiat money system<sup>ii</sup> is being called into question by both the mainstream and the GGR<sup>iii</sup> ground swell. While we're not advocating a 38 Special purchase, we do think this shift in social sentiment could have longer term repercussions.

From a seasonality standpoint, precious metals tend to bottom during the summer months before Asian demand drives up prices in the 4<sup>th</sup> quarter. We like to buy on pronounced weakness vs. momentous strength. Average investors tend to get caught up in the fervor of big moves. Trust us, be patient and wait for inevitable pullbacks to nibble. Never forget the old adage: Gold takes the escalator up and the elevator down.

### Appropriateness

While happily married, I've heard gold investing can be similar to ex-wives: painfully volatile, pay very little income and have large carrying costs. Many consider gold shiny and worthless; but silver, platinum and palladium all have industrial uses. During periods of economic expansion, they can do quite well. Historically, gold has a negative correlation to the equity markets thereby providing suitable diversification - so from an asset allocation standpoint, precious metals usually work. But given its volatility and lack of income we wouldn't promote more than a 5-7% portfolio allocation and would slowly scale into the position.

### Investment Vehicles

We question physical possession in precious metals as the best *investment* method. Sure, the glistening gold coins and silver bars look great and make good conversation; but there are hidden costs. Insurance, storage, & commissions can easily be 10-15%. Liquidity is another concern: buying and selling costs can easily incur 5% spreads from a reputable dealer. Instead, we advocate buying the gold (GLD), silver (SLV) or platinum (PGM) exchange traded indices. You can buy/sell with ease and have price transparency.

For the more adventurous, consider actual mining companies but be forewarned: they can be treacherous. They carry operational and market risks. There's nothing more frustrating than waking up to see Gold up \$40/ounce and your gold mining stock is down 30% because a mineshaft caved. You were correct on direction but wrong on execution. The index ETF for mining stocks is GDX.

Metals investing may not be universally suitable but we do think adverse periods warrant consideration. Modest participation could offer some portfolio luster to an otherwise drab social-economic environment.

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<sup>i</sup> [30 year Gold Prices](#)

<sup>ii</sup> [Fiat Money](#)

<sup>iii</sup> Guns, Gold & Rations