# Global Matters Weekly

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Belvest 研富

# Has gold lost its shine?

by Stephen Nguyen, CFA Portfolio Strategist

As we approach the end of 2022, it is worth reflecting on asset class returns this year. Global equities and bonds have both suffered significant declines and as a result the traditional balanced portfolio, anchored by these two asset classes, has struggled. Risk assets have had a torrid time due to a combination of factors including bleak economic and earnings outlooks, inflation concerns and heightened geopolitical tensions, which have all weighed on investor sentiment. Surprisingly, gold which has traditionally been deemed as a 'safe haven' asset has also disappointed this year. Gold is often thought of as a hedge during market downturns and in an inflationary environment, so why has it struggled this year? And does it still warrant a place in investors' portfolios.

Gold attracts its fair share of criticism as an 'unproductive' asset, but the same can be said of cash. Unlike cash, gold doesn't pay any income, which makes it difficult to value.

It is worth exploring gold's relationship with other 'income' producing safe haven assets and inflation. This year we have witnessed a significant repricing in nominal interest rates across most advanced economies, the most notable being in the US where rates have risen from close to 0% to 4% today. All else being equal, as nominal rates rise, the opportunity cost of holding non-income bearing assets increases and therefore dents the appeal of the yellow metal for savers looking to earn a positive yield. However, we have also experienced rapidly rising inflation which erodes the purchasing power of paper money and theoretically should increase the attractiveness of gold. So why haven't we seen this in terms of gold prices?

The final piece of the puzzle which provides a better explanation to gold pricing is its relationship with real (inflation-adjusted) interest rates. The two are negatively correlated: as real rates increase; the price of gold is driven down. Despite high levels of inflation, investors have been placing more emphasis on the pace of the rise in nominal rates which has proved to be a major headwind for gold.

Although the relationship is weaker, we believe that US dollar strength has also provided another headwind for gold in in the past year, as this makes it more expensive for investors holding currencies other than dollars, since gold is priced in dollars.

Despite the headwinds mentioned above, it is worth reminding ourselves of gold's role in multi-asset portfolios. Historically, gold has proven its ability to preserve its purchasing power when compared to fiat money as it cannot be devalued by central banks, and it serves as an insurance policy at times of geopolitical tensions or any systemic / credit events. Typical insurance policies pay out should a specified event occur, but in a truly dire scenario this is no more than a pledge and you must question the ability of the counterparty to deliver. This is a fundamental risk in all insurance as historically there have been scenarios in which the private sector was unable to cope, requiring intervention from the state. Gold does not bear this type of default or counterparty risk. Lastly, gold has shown to have little to no correlation with other risk assets over the long-term and certainly at the peak of severe market shock.

Whilst it is difficult to predict, we believe that the Fed is getting close to peak rates with the significant portion of rate rises behind us, and in our view the US dollar is also nearing its peak; both of which could be supportive for gold. Severe market stress occurs infrequently however it happens often enough to justify an allocation to this precious metal. The recent turmoil in cryptocurrency is a useful reminder for investors as to what is the ultimate alternative to fiat currency. Gold's long and illustrious status can continue to shine.


For more information, please contact your adviser or alternatively contact:

Belvest Investment Services Limited
**研富投資服務有限公司**
9th Floor, Centre Mark II
305-313 Queen's Road Central
Sheung Wan, Hong Kong

Tel +852 2827 1199
Fax +852 2827 0270
belvest@bis.hk
www.bis.hk

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