Another golden opportunity for investors

23 October 2007

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A few days ago we noticed an article claiming that gold would soar from its current levels of around USD 750 per ounce all the way to USD 3,000 per ounce over the next decade. At first glance, one is likely to throw the article aside and mutter something about nutty gold bulls but a closer look reveals that gold would 'only' have to grow by 15% per annum compounded over the period to accomplish this feat.

The problem for local investors is twofold. Investing in the precious metal is a risky business and avenues for investment are limited. Until recently South African investors could purchase Krugerrand (and hold the physical commodity) or buy gold shares for direct exposure to profits (and losses) from gold production. Each option came with its pros and cons.

On the negative side, Krugerrands held sentimental value, often well in excess of the value of the physical gold they contained. Many investors overpaid for their gold coins. And this problem was exacerbated by clever marketing strategies to sell specially minted 'collector' coins. The best bet was probably the standard 1-ounce Krugerrand. Although a good proxy for gold, individual investors paid excessive fees to trade this coin. Gold mines, on the other hand, exposed investors to all manner of additional risk. Share prices fluctuate with economic conditions, falling hard after mining accidents, worker strikes and the like. Investing in gold mining stocks not only gives exposure to the gold price but to the operational risks that goes with the business of mining.

Twenty first century alternatives

Today investors have a number of alternatives. Instead of pouring cash directly into listed companies like Gold Fields and Harmony, they can purchase units in a gold Exchange Traded Funds (ETF). This option is available through ABSA's NewGold ETF which can be bought and sold directly through an equity broker.

The institution issuing the ETF holds physical gold to back the product NewGold is 100% backed by allocated gold. **And the product enjoys a strong correlation with the gold price if gold moves up, so does the value of the ETF.**

Dr Vladimir Nedeljkovic of Absa Capital's Debt Capital Markets: "Gold is widely seen as a safe haven and there is flight to quality investments at this point in time. NewGolds performance comes on the back of the increasing market demand for the yellow metal."

In the last couple of days a new player has emerged through with local investors can purchase gold bullion. The company is SA Bullion Fund Management a dedicated gold bullion investment manager, established jointly by Cape Town based Hilton Davies and Germiston-based Rand Refinery, the world's largest refiner of gold. "What we sought to do is to create an investment vehicle where investors can take full ownership of bullion and do so at low administrative cost with complete security. As such, investors are not investing in a gold derivative, commonly known as paper gold, where there is credit risk related to the issuer; similarly there is no stock market risk involved," said Davies

Using Krugerrand to underpin the fund

We mentioned earlier that the Krugerrand was possibly not a great way for an individual investor to gain access to the gold market. Thus it was interesting to learn that Gold Bullion would use the 1-ounce gold coin as its investment vehicle of choice. The argument is that the cost associated with this type of gold investment is eliminated through volume trading and that wholesale prices can be passed on to the investor.

Johan Botha, global markets executive at Rand Refinery says: "As SA Bullion's strategic partner we are delighted to bring the mainstream of investors into the gold market, particularly as we hold an extremely bullish view on gold." Since 2000 the precious metal has been on the recovery path. It rose slowly until the end of 2003 before powering ahead. SA Bullion says that gold has returned 24.8% per annum over the last three years (in rand terms). It certainly appears the commodity bull market remains intact.

With the world jittery about higher oil prices, a possible Turkish incursion into Iraq and sub-prime concerns, investors could well push the gold price higher. But be warned gold goes through cycles like any other commodity or market.

Editor's thoughts:

For as long as we can remember, gold has been punted as the ultimate store of value in times of market uncertainty. Many investment analysts believe the metal would be a more attractive bet if it had industrial applications, like platinum. Do you think gold is a good investment, and what would make you consider buying the precious metal? Send you comments togareth@fanews.co.za