



The SA Bullion Gold Report

Second Quarter 2018

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Table 1: Gold Performance to 30 June 2018 (% per annum)¹

	Quarter ²	1 Yr	3 Yr	5 Yr	10 Yr	Since 31/12/1999
Gold in US Dollar	-5.5	0.6	2.2	1.0	3.0	8.5
Gold in Rand	10.7	7.2	6.2	7.8	9.0	13.1
Gold in Euro	0.0	-1.5	0.9	3.3	6.2	7.4

¹ Based on LBMA PM Fixes.

² Not annualized for periods of less than one year

Table 2: Quarter-End Gold Prices and Exchange Rates¹

	Gold in US\$/ oz	R/\$ rate	Gold in R/ oz ²	\$/€ rate	Gold in €/oz
30 June 2008	930.25	7.83	7,282.13	1.58	589.21
30 June 2009	934.50	7.82	7,305.13	1.41	664.89
30 June 2010	1,244.00	7.59	9,443.93	1.23	1,012.70
30 June 2011	1,505.50	6.86	10,321.86	1.45	1,040.07
30 June 2012	1,598.50	8.21	13,123.35	1.27	1,260.45
30 June 2013	1,192.00	9.97	11,881.85	1.30	914.39
30 June 2014	1,315.00	10.64	13,986.58	1.37	962.66
30 June 2015	1,171.00	12.34	14,451.28	1.11	1,046.19
30 June 2016	1,321.50	14.91	19,703.56	1.11	1,187.50
30 June 2017	1,243.50	13.00	16,164.25	1.14	1,089.93
30 June 2018	1,250.45	13.85	17,323.96	1.16	1,074.14

Note 1: Gold prices in US\$ and € are LBMA PM Fixes.

Note 2: Gold price in Rand from Rand Refinery.

Note 3: Previous quarter-end gold prices were \$1,323.85, R15,656.29 and €1,074.57.

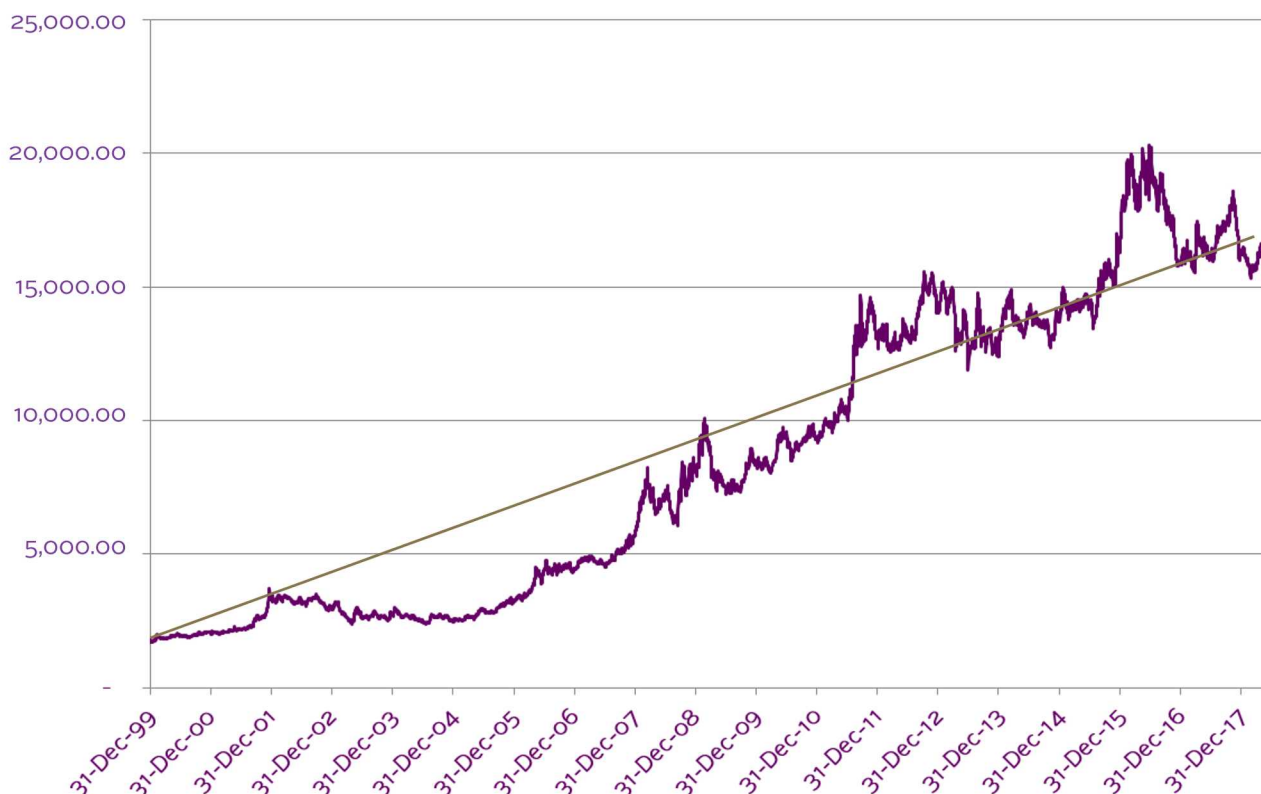
Note 4: Gold prices at 31/12/1999 were \$290.25, R1,785.04 and €289.09

Table 3: Calendar Year Performance of Gold

	% US Dollar	% ZA Rand	% Euro
2008	4.3	41.1	9.7
2009	25.0	-0.4	21.1
2010	29.2	16.1	38.2
2011	8.9	33.0	12.6
2012	8.3	13.6	6.2
2013	-27.3	-11.8	-30.3
2014	0.1	10.4	13.4
2015	-11.4	19.1	-1.1
2016	7.7	-2.5	13.3
2017	12.2	1.3	-2.6
2018 year-to-date	-3.1	7.7	-0.6

Figure 1: Gold Price in US Dollar from 31 December 1999 (LBMA PM Fix)

Figure 2: Gold Price in Rand from 31 December 1999 (Rand Refinery First Pricing)



Gold Price Action

Dollar Gold (gold priced in US Dollars) had mostly a declining quarter to produce a poor result. Rand Gold (gold priced in South African Rands) had a rising April, flat May, and rising June to produce a very strong result.

In the most recent 10 years Dollar Gold handsomely outperformed cash in the bank with a compound annual return of 3% versus an effective zero percent. Similarly, Rand Gold handsomely outperformed cash in the bank with a compound annual return of 9% versus approximately 4%.

In the eighteen and a half years of this 21st century the returns are even more impressive, with Dollar Gold returning a very strong 8.5% (annualized) and Rand Gold returning a stellar 13.1% (annualized).

Gold in an Investment Portfolio

The Case for Investing in Gold is our position paper that sets out our rationale for investing in gold. We published this document in 2007 and it remains unchanged in the Library section of www.sabullion.co.za today.

In summary, the key reasons that we advocate for holding some gold are:

1. The need to have some cash close to hand (and we view gold as currency) so as to take advantage of out-sized opportunities when they present themselves – usually a handful of times in a lifetime; and
2. To diversify - so as to benefit from overall long term price rises while simultaneously limiting the impact of specific loss-making investments. This covers not only stock market losses but also losses related to inflation and currencies.

Wisdom and Theories

When it comes to investing we believe in good old common sense, and one old piece of advice that we like is “don’t put all your eggs in one basket”. This advice is very old. It is to be found in the Bible, in Shakespeare’s Merchant of Venice, and many other revered pieces of literature.

Moving on to more recent times, we at SA Bullion, have been avid students of finance (at universities and at investment firms) for some decades. We have studied the theories of great academics like Benjamin Graham and the analysis of great investors like Warren Buffet and my own old mentor – Allan Gray. And when naming names, the standout name is Harry Markowitz.

Dr Markowitz is recognized as the father of Modern Portfolio Theory. In 1990 Dr Markowitz won the Nobel Prize for his pioneering work in modern portfolio theory. He conducted breakthrough research on risk, return, correlation and diversification as they apply to investment portfolios.

A few years ago Dr Markowitz was asked for advice on investing. His response was one word – diversify. When pushed for explanation he followed this up with “Remember that the future will not necessarily be like the past. Therefore we should diversify.”

Risk and Return

There are many ways in which risks and returns can be analysed. Of course it goes without saying that these are rearward looking analyses, and we must remind ourselves that “the future will not necessarily be like the past”.

We produce this quarterly report that includes various forms of performance data and we have recently commenced producing quarterly Fact Sheets that can be found in our online Library. The fact sheets include the most widely accepted piece of risk measurement, namely maximum drawdown. Maximum drawdown is simply the biggest possible downhill on a graph from a high point to a low point. In the time since commencing the SA Bullion gold facilities, the data for the period 31/3/2007 – 31/3/2018 indicate:

Cumulative performance:	226% in Rand and 88.1% in Dollar
Maximum drawdown:	-31.1% in Rand

Over 20 years the facts speak even more strongly in favour of gold.

Clearly there has been risk, as with all currencies, but much less so than for the US Dollar and South African Rand, and there has been considerable return.

Correlation and Diversification

Gold has been a prized store of value for at least 5,000 years. Gold has been a form of currency since King Croesus of Lydia struck the first gold coins approximately 2,500 years ago. The United States Dollar has been in existence for 105 years. The unbacked United States Dollar as we know it today has been in existence for 47 years.

Whereas most currencies were backed by gold (either directly or indirectly) until 1971, today none are. The effect of zero-backing since 1971 has been steep loss of value for all currencies (except gold), sometimes with dramatic step-downs.

In times of currency or economic crisis gold tends to perform well – as the safehaven currency. Yet over the long run when economic growth has been strong – gold has performed well, then too. This is because of the physical uptake of gold as jewellery and investment. This is the dual nature of gold.

Recent studies using weekly performance data have analysed the correlation of gold to the S&P 500 (the index of 500 large companies listed in New York) over the period March 1987 to March 2018. Results of the study follow:

S&P 500 Performance	Correlation with gold performance
Very strong	Highly positive
Middling	Approximately zero
Very Poor	Highly negative

Source: Bloomberg and the World Gold Council

This means that where stock markets have been up dramatically, gold has done well. Where stock markets have been down dramatically, gold has done well. Where stock markets have been inbetween these two extremes, gold might have done anything as it is disconnected at that time.

Having some gold exposure can provide an advantage for risk-adjusted returns compared to a portfolio with no gold exposure as it can mitigate losses in times of market stress. As such, it enhances overall portfolio performance.

In a study conducted by Bloomberg, ICE Benchmark Administration and the World Gold Council researchers studied institutional investors with an asset allocation equivalent to the average US pension fund for the period 12/2006 to 12/2016. Specifically, they looked to see whether such a fund would have benefited from a 2%, 5% or 10% allocation to gold. The findings were that the average pension fund would have benefited in all scenarios by reduced risk and increased returns. Viz

Gold Allocation	Annualised Volatility %	Annualised Return
0%	12,7%	4,7%
2%	12,4%	4,8%
5%	12%	5%
10%	12%	5,2%

Source: Bloomberg, ICE Benchmark Administrators and World Gold Council

How much gold should one have in a diversified portfolio?

Our starting position is to look at the world as if it were a single diversified portfolio. As such it represents the average investor.

The World has an investment portfolio consisting of shares, bonds and gold valued at around \$150 trillion. The total of all gold in circulation has a value of around \$7.5 trillion. This equates to a gold exposure of approximately 5%.

It is our view that investors should take guidance from the total market and regard a 5% allocation to gold as their neutral position. Investors should deviate from this default position depending on two factors:

1. their generally desired exposure to cash and currencies; and
2. their view of stock and bond markets.

As one's view of stock and bond markets becomes more buoyant, so one's exposure to cash and gold should decrease. Conversely, as one's view of stock and bond markets becomes more pessimistic, so one's exposure to cash and gold should increase.

A handwritten signature in dark ink, reading "Hilton Davies" with a stylized flourish underneath.

Hilton Davies
11 July 2018