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No: 17, 29 April 2013

What's the point of gold?

It has been a scary time for gold bugs. The world's favourite fear asset has suffered its largest one day loss for 30 years, prompted by a combination of worries about an early end to the Fed's QE programme and the prospect of a fire sale by Cyprus to help ease their financial problems.

It is easy to understand why the sale of gold by the Cypriots could cause a wobble, not least because it could be the start of something more sinister: Italy and Portugal are much larger holders of gold, and it is not inconceivable that they could also be forced sellers at some point. The removal of QE, however, is more of a puzzle, in that it would almost certainly trigger much greater volatility in stock markets, and a return to a keenness amongst investors to hold a proportion of their assets in tried and tested 'risk-off' assets such as bullion. This would help to revive the demand for all sorts of safe haven assets, not just gold.

Our own view remains unaltered, which is that we see the inclusion of a modest investment in gold in the portfolios we look after as a form of insurance. Nobody buys insurance hoping that it will prove to be good value: we mainly buy insurance hoping that it will be a waste of money, but in the meantime will help us sleep at night. Gold is still the perennial safe harbour for people who worry about the debasement of paper currencies, inflation, and most other plagues that can destroy wealth.

Despite the falls of the last fortnight, this continues to be the case, and long term prudent investors (the types who buy insurance) should ignore the day to day fluctuations and remember why gold remains an important, but quite small, component of the well diversified portfolio.



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