



The price of gold has risen to \$1,900 an ounce, or about 25 per cent, since the start of the year REUTERS

No sign of a bubble in this golden opportunity

The Analyst

By Mark Dampier



One investment that divides opinion time and again is gold. Investors either tend to be gold bugs or gold bears, with few lying in between. The bears have been calling the top of the market ever since gold reached around \$500, doubling the level it was when Gordon Brown famously sold most of the UK's remaining gold reserves. With every rise of \$100 since then the gold bears have continued to call the top. Yet having now reached \$1,900 an ounce the dynamics of gold don't seem to have changed. For there to be a bubble there has to be some completely irrational buying and I see little evidence of this so far.

The simple fact is that western currencies are being debased. Inflation is running far higher than interest rates meaning the value of each dollar or pound is losing its spending power, a trend exacerbated by the money printing process of quantitative easing (QE). It isn't anything new. The dollar has lost some 97 per cent of its purchasing power over the past 40 years; it just seems that the process is taking place faster than ever today. Ben Bernanke has quite candidly told us not to expect interest rates to rise for the next couple of years, so is it any surprise that the extreme levels of economic uncertainty have seen gold push up to new levels?

Although the strong case for gold persists, I can't help but feel the opportunity has now moved to gold equities rather than bullion. The price of gold is up around 25 per cent since the start of the year but the FTSE Gold Mines Index is up only 3 per cent. Some funds such as BlackRock Gold and General are down a couple of per cent and cer-

FUND FACT BOX

BlackRock Gold & General

Initial charge	5.00%	Yield	n/a
Annual charge	1.75%	Fund size	£2,991m

Managed by: Evy Hambro
Launch Date: 07/04/1988

Junior Gold Trust

Initial charge	5.25%	Yield	n/a
Annual charge	1.75%	Fund size	£42m

Managed by: Angelos Damaskos
Launch Date: 01/10/2010

Source: Hargreaves Lansdown

tain gold funds focused on smaller producers have dropped by 8 to 9 per cent. So while physical gold has rallied gold equities have lagged far behind. The last time we saw a dislocation of this kind was during the credit crisis in 2008 when, after the initial stages of the crisis, gold equities roared back and went on to strongly outperform physical gold.

In 2010 the average gold price was \$1,224 per ounce and the average production cost across the industry was \$557 per ounce. So far in 2011 gold has averaged \$1,496 per ounce, so even if labour and raw material costs have risen by 10 per cent or more mining companies must surely be making higher profits. Gold shares are also very cheap based on historic valuations. Price-to-earnings ratios are much lower than they were in 2005 yet profits are rising strongly. One of the reasons why gold equities may have slipped out of favour, at least temporarily, is that they have been caught up with the whole mining and commodities sector sell-off. Here we have seen quite large falls partly based on the increased danger of a slowing world economy. Yet gold is not really an industrial metal so it should perform somewhat differently to the likes of copper.

Of course my belief is predicated on the gold price staying high. It will obviously fluctuate, and rises

Smith & Williamson Global Gold & Res.

Initial charge	5.00%	Yield	n/a
Annual charge	1.75%	Fund size	£72m

Managed by: Robert Lyon & Ani Markova
Launch Date: 03/12/2004

Way Charteris Gold Portfolio

Initial charge	5.25%	Yield	n/a
Annual charge	1.75%	Fund size	£21m

Managed by: Ian Williams
Launch Date: 01/02/2010

and falls of more than \$50 an ounce in this sort of environment are to be expected. But while real interest rates are negative and there are continued worries surrounding banks I see gold remaining a popular investment.

Those looking for their first foray into the area might consider BlackRock's Gold and General Fund, which is the largest in the sector. Its size gives plenty of liquidity but does mean it will predominantly be invested in the largest gold mining companies. Smith and Williamson's Global Gold and Resources Fund is still reasonably large but has more smaller producers, which could perform better over the long term, though they can be more risky. Finally, for those wishing to concentrate purely on smaller gold shares, Junior Gold Fund and WAY Charteris Gold Portfolio should also be beneficiaries of any sustained gold strength. These are much smaller so they could be more affected by flows into and out of the funds, but they are also nimble enough to take full advantage of opportunities among the smaller producers.

Mark Dampier is head of research at Hargreaves Lansdown, the asset manager, financial adviser and stockbroker. For more details about the funds included in this column, visit www.h-l.co.uk/independent

No Pain, No

By Derek Pain



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