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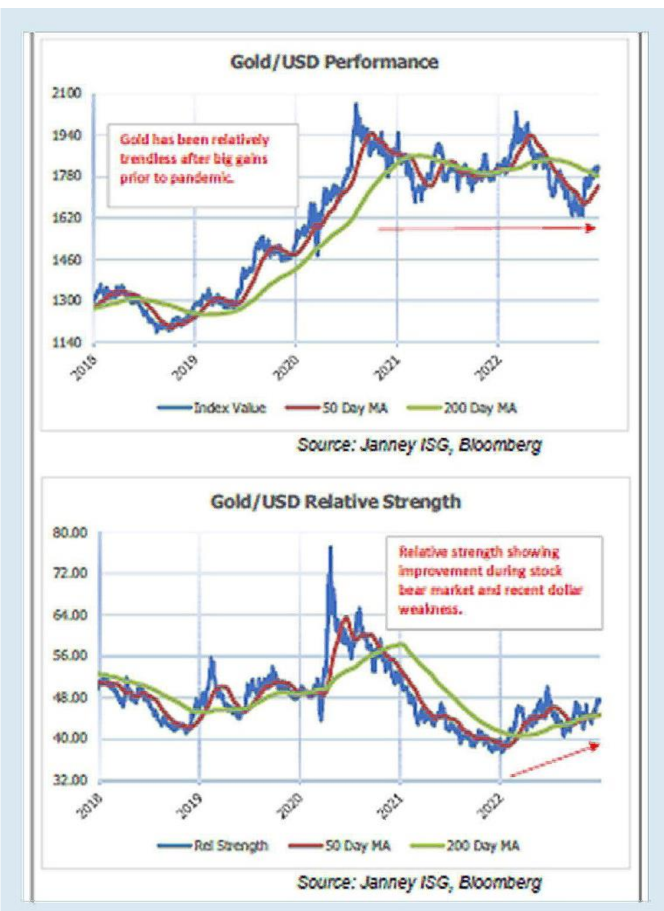
THE IMPACT OF GOLD FROM A DIVERSIFICATION STANDPOINT

Gold has long been considered a valuable hedge against equity bear markets and its low correlation with equities provides valuable portfolio diversification that has been consistent over time.

One of the market's oldest maxims is that investors flee to gold in times of distress. It's a call back not only to the days of the gold standard in the U.S. but even alludes to ancient times when gold was a primary mode of currency. In that light, 21st century investors are right to be skeptical of something seemingly so antiquated. Not to mention, gold bulls' penchant for hyperbole has rightly drawn criticism. However, just sticking to data, gold's historic value as a diversification asset has been fairly consistent over time, especially in bear markets. While there is no reason at present why this might change, **past results and trends are never guaranteed to continue**.



Holding uncorrelated investments helps diversify a portfolio. A robust exposure to a range of risk factors can help stabilize portfolio return and help investors avoid sharper drawdowns in bear markets. Gold's five-year beta is just 0.10 (10yr just 0.05). A beta of 1 means an investment moves in lockstep with the broader equity market. A beta greater than 1 implies the investment is *more* cyclical than the broader equity market, while less than 1 implies it is *less* cyclical. For example, the cyclical Consumer Discretionary sector has a 5-year beta of 1.15, while the defensive Consumer Staples has a 5-year beta of just 0.62.

Gold's 0.10 beta means equity market movements have little to no influence on/relation to gold's price movements. Compared to, say, the commitment required for a zero-beta hedge fund, gold ETFs could be a more affordable alternative. However, as with any investment, suitability will vary depending on each investor's circumstances and goals. This is not a recommendation but a tool in the toolbox.

How can gold and equities move so independently?
Two of gold's main historic drivers have been geopolitical instability and weak economic growth, both headwinds for equities. On the other hand, easy monetary policy and a weak dollar typically prop up gold, but so too equities.

Takeaway

Gold's low correlation with equities could help add portfolio diversification in addition to its own return. The macro environment at present is exhibiting three typically bullish signs for gold: 1) an uncertain near-/medium-term economic outlook in the U.S., 2) broad & continued geopolitical instability caused by Russia's war in Ukraine and China's increasingly murky political/economic landscape, despite recent reopening after a 3-year lockdown, and 3) the Fed being in the later stages of a tightening cycle, with potentially easier monetary policy on the horizon.