Heartwood Investment Management

30 November 2018

Investment Insight

Weekly Insight

Turning to gold in uncertain times

We have marginally increased our exposure to gold across the portfolios. Why have we chosen to do this now?

For much of 2018, gold's long-held status as the ultimate safe haven has appeared to be under fire. It has not fulfilled its traditional role - protection against geopolitical and investment market risk and a hedge against both inflationary and deflationary environments - to any great effect. The metal has struggled to perform in an environment of rising real yields (yields minus inflation) and a strong US dollar. Investors have flocked to US-based assets as growth strengthened and the dollar became the safe-haven of choice.

October's bout of market turbulence though, woke gold from its slumber when a surge in US Treasury yields (falling prices) triggered a sell-off in equities. Gold was in demand once more amid ongoing fears surrounding the outlook for global growth, as well as some concerns over US inflation ahead.

Assessing gold's true value is problematic - the metal does not provide a cash flow in the same way as equities or bonds, has only a few industrial uses and incurs storage costs. Although in the short term the gold price will likely continue to be dictated by the direction of real yields and the US dollar, as we move from being late in the current economic cycle to the end of the cycle, we expect gold to benefit from increased demand as investors position for a recession. (Gold tends to benefit from a consistent drop in real yields during the lead-up to recessions and thereafter.)

The importance of portfolio diversifiers today

At this point in the cycle, historically, we would have looked to bonds to provide an obvious diversification solution for our portfolios. But with bond markets now often moving in tandem with equities, and given rising levels of global inflation, bonds are unlikely to provide the same the level of diversification benefit as in the past.

As a result, and cognisant of the investment landscape around us, we have been slightly increasing our exposure to gold across portfolios. As one of very few diversifiers which has recently been working to offset market nerves, we believe the current demand for gold's safe haven status demonstrates clear underlying investor priorities surrounding diversifying and de-risking.

Investment markets have calmed somewhat in the wake of October's volatility, further heartened by what has been perceived (correctly or otherwise) as a more accommodative tone from the US Federal Reserve on the pace of future interest rate rises.

Nonetheless, we believe that in this late cycle environment – which has proven challenging for almost all asset classes in 2018 so far – adding to portfolio diversifiers remains a wise investment strategy.

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Clear Thinking

Contact

To find out more about the Heartwood strategies, visit our website or contact your local representative.

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