Kiplinger's PERSONAL FINANCE

>> **INVESTING** // METALS November 2011

GOLDEN OPPORTUNITY?

The price of gold could still go higher, but invest in small doses. BY KATHY M. KRISTOF
(excerpt)

NO INVESTMENT HAS SHINED as brightly as gold over the past decade. If you had invested $10,000 in gold bullion in January 2001, your 36.89 ounces of the precious metal would have been worth more than $67,000 by September 1, 2011. That beat the pants off stocks. The same investment in Vanguard Total Stock Market Index Fund (symbol VTSMX), for example, would have been worth $12,445 after the same ten-year period. …

Aside from gold's stellar recent results, the metal is a good portfolio diversifier because its price tends to move in the opposite direction of stock prices – and often bond prices, too. Plus it is a great hedge against "black swans" – unexpected and catastrophic financial events – and a falling dollar.

Yet even many of gold's most enthusiastic advocates suggest that investors dedicate just a fraction of their long-term portfolio to the metal – if any at all. The reason: Gold produces no earnings, nor does it boast a dividend yield. It appreciates or depreciates based on supply and demand. Right now, demand is high, thanks to a decade of rotten stock prices, a souring U.S. economy and worries about the value of currencies in a world where the list of deeply indebted nations is long and growing. Some central banks in developing countries, such as China and South Korea, have also started buying gold, boosting demand. Moreover, interest rates are so low today (they're actually negative in many instances after accounting for inflation) that the metal's lack of yield doesn't hinder buyers.

When world economies are stable and stock and bond markets appear attractive, gold simply can't compete and its price tends to languish. For example, during the booming 1980s and 1990s, the metal's price did nothing but fall. "It's a defensive hedge," says David Kudla, chief investment strategist at Mainstay Capital Management, "People buy gold to hedge against inflation, against deflation, against economic or political uncertainty. We have all of those concerns – and real concerns about the debasing of currencies worldwide right now."

Buy on dips. Kudla expects gold prices to keep climbing until the U.S. government gets serious about cutting the deficit and entitlement programs – and he has little hope that will happen soon. Still, he says, investors should hold no more than 15% of their assets in gold, and they should buy only when the price dips because the metal's price is historically high. …

You can buy gold in a variety of ways. You can pick up coins, bars, gold-mining stocks and exchange – traded funds that track the price of gold. But the costs of trading and storing bullion, as either bars or coins, can be significant. Dealer markups and shipping – and – storage costs can shave the typical investor's return by 10% to 15%. Gold – tracking ETFs hold bullion on behalf of investors, so you don't have to pay fees for a safe – deposit box.

Most experts prefer gold ETFs over mining stocks. That's because the stocks are affected by many factors other than the metal's price, including stock market conditions. Prices of individual gold stocks are often considerably more volatile than the metal itself – and the metal is plenty volatile on its own. …