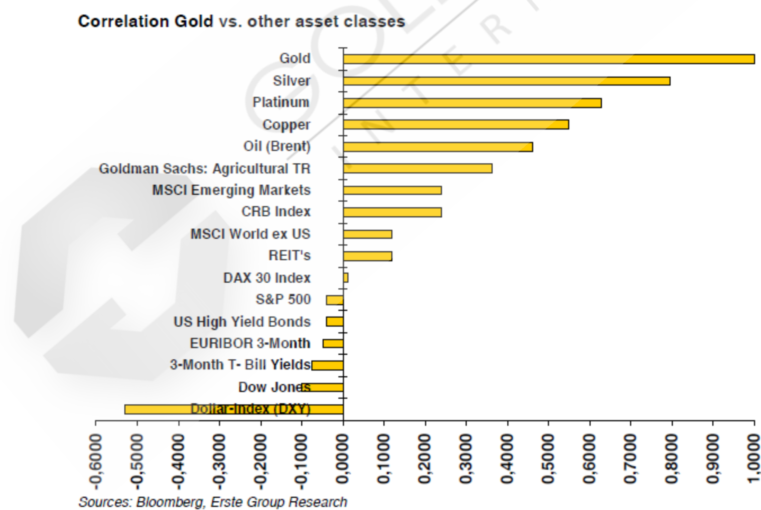
GOLD BULLION
INTERNATIONAL

Gold's role in a diversified portfolio

Portfolio diversification refers to reducing investment risk by purchasing a variety of different assets. Even though an individual asset or asset class may outperform another in a given timeframe, a portfolio containing multiple assets may deliver higher risk-adjusted returns than the individual components. Although a random selection of assets will reduce the overall risk exposure, diversification is more efficient if the assets held are not correlated.

Gold as a non-correlated Asset

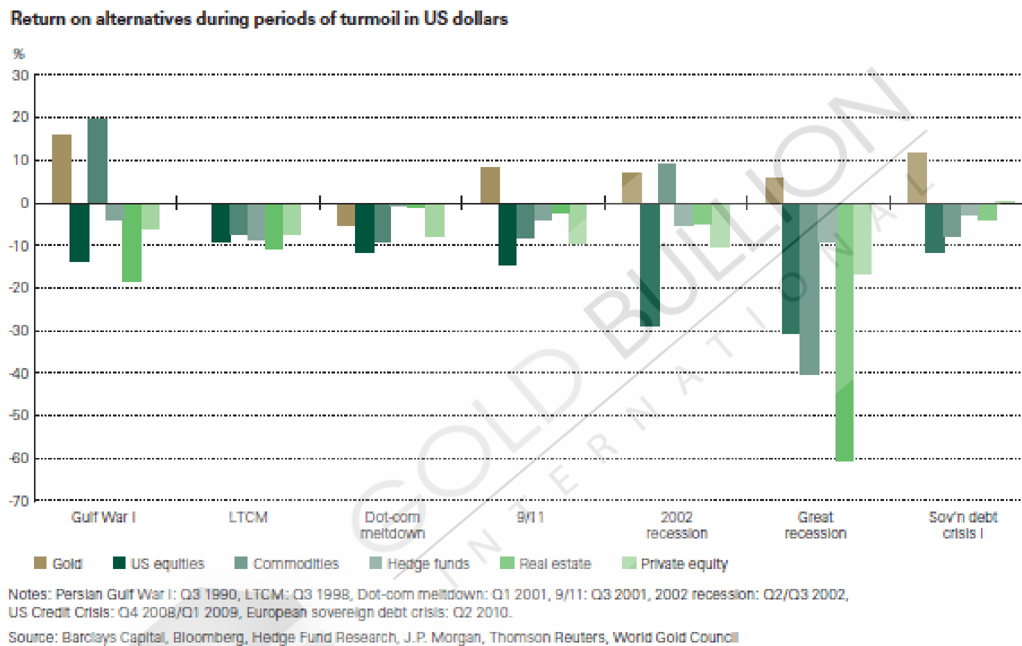
The most effective way to diversify a portfolio and preserve wealth in the financial markets is to invest in assets that have a low correlation to each other. Gold is the ideal diversifier for a financial portfolio; it has a low correlation to many widely held portfolio assets. Over the past twenty years, gold's performance has been negatively correlated to most traditional asset classes (charted below).



In a healthy economic environment with strong growth and low inflation, gold typically underperforms equities, bonds, property and cash. However, its lack of correlation with other assets plays a key role in stabilizing the long term value of a portfolio during uncertain economic times. For example, gold tends to outperform most asset classes under various unfavorable economic conditions: periods of high inflation, deflation and stagflation.

Tail-risk Insurance

An allocation to gold also provides the investor with "tail-risk" insurance. Unlike traditional assets classes and alternative investments, there has not been any significant statistical correlation between gold and economic data or business cycles. This may be due to the fact that gold is highly liquid and does not contain any credit risk. In contrast to shares or bonds, there are zero liabilities attached to gold.



Gold returns tend to outperform other assets in periods of economic and financial turmoil. For example, during seven periods regarded to be 'tail-risk' events from January 1987 – June 2011, the majority of portfolios that included gold performed better (by either posting gains or reducing losses) than those without.

Allocation to Gold

According to independent analysis by Oxford Economics, investors can benefit from adding a separate gold allocation, regardless of inflation. For an investor with a medium-risk tolerance profile, they estimate that gold's share of an optimal portfolio is about 5%. However, during periods of high inflation, or low inflation coupled with lower economic growth, the optimal allocation should be greater. Currently, the average allocation to gold in a portfolio is far less than 5% which shows that as a whole, investors are under-allocated.

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Effect on optimal asset allocations in different scenarios for investors with a mainstream risk profile*

Scenario	Cash	Equities	Gilts	Property	Gold
Base case allocations, %	5	45	30	15	5
Higher inflation scenario	unch.	++	--	-	++
Lower inflation & lower growth scenario	unch.	--	++	-	unch.

Key:
++ denotes a significantly higher number.
– denotes a lower number.
–– denotes a significantly lower number.
unch. denotes unchanged.

*Mainstream risk profile defined as investors with a portfolio volatility between 10% to 20% per annum.

Source: Oxford Economics

An allocation greater than five percent to gold is optimal (as seen in the charts below), under the following circumstances:

- A more inflationary long-term scenario
- Weaker growth and low inflation for more risk-averse investors

Effect on gold optimum weightings in different scenarios

Scenario	Risk Tolerance* Low	Risk Tolerance* Average	Risk Tolerance* High
Base case allocations, %	9	5	0
Higher inflation scenario	++	++	++
Lower inflation & lower growth scenario	+	–	unch.

Key:
++ denotes a significantly higher number.
+ denotes a higher number.
– denotes a lower number.
unch. denotes unchanged.

*Low risk tolerance is defined as investors with a portfolio volatility of 10% per annum, average with 15% per annum and high is 20% per annum.

Source: Oxford Economics

Performance of various assets in different scenarios 2011-2015[1]

	Baseline[4]	Deflation[5]	Stagflation[6]	Inflation[7]
Gold	1	3	2	5
Equities[2]	5	2	3	4
Bonds[3]	2	4	1	1
Cash	4	5	5	3
House Prices	3	1	4	2

1 Performance based on a 1-5 scale (5=best performance; 1=worst performance).
2 The Wilshire 5000 Index is used for US equities.
3 10-year US Teasury bonds used as a proxy for all US bonds.
4 Baseline scenario is the average scenario depicting the normal of steady growth and moderate inflation.
5 Deflation scenario is representative of markets marked by depreciating prices.
6 Stagflation is an economic scenario that combines high inflation and negative growth.
7 Inflation scenario is a scenario of high inflation and average growth.

Source: Oxford Economics

Gold is a highly effective vehicle for diversification and risk management. It consistently exhibits a low to negative correlation to most traditional asset classes and has provided much needed “safe-haven” qualities especially during periods of economic and financial turmoil. Investors with varying degrees of risk tolerance can benefit from an allocation to gold in all types of market conditions, especially during periods of economic uncertainty.