



Going for the Gold

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As the world's troubles mount, gold glitters brighter. Gold has attracted investors throughout the centuries, protecting their wealth and providing a "safe haven" in troubled or uncertain times.



From the first discoveries of gold in ancient times, its beauty and ease with which it could be worked have inspired craftsmen to create ornaments, as symbols of wealth and power. The first gold coins were struck in the eighth century BC and have been used for legal tender since the sixth century BC.

Central banks have been major holders of gold for more than 100 years. The

U.S. went to a gold standard in 1879. By 1914 most countries in the world were on a gold standard. In 1933, President Franklin Roosevelt took the US off the gold standard to allow the massive debt that would be required to stimulate and shore up the American economy. In 1971, President Nixon ended the US gold standard. At that point the price of gold bullion was allowed to float freely and find its own level. Since that time, gold prices have fluctuated greatly.

Gold has attracted investors throughout the centuries as a safe haven and as a potential hedge against inflation and dollar fluctuations. In addition, investors have sought gold for reduced volatility and diversification.

Gold's history as a safe haven in troubled times can be demonstrated. In volatile and uncertain times, there is a flight to quality as investors seek to

protect their capital by moving it into assets considered to be safer stores of value. Gold is among a handful of financial assets that do not rely on an issuer's promise to pay, offering refuge from default risk. It does provide some insurance against extreme declines in asset values in unsettled times.

Gold's record as a hedge against inflation is more difficult to support. Today gold trades for approximately \$900 an ounce, little more than its price in 1980. If gold had kept up with inflation, it would be selling for \$2,000 an ounce today. Moreover, gold prices are very volatile, in the past year, they have ranged from \$650 per ounce to \$1,000 per ounce and then fell halfway back again.

Gold, therefore, has been more of a crisis hedge than an inflation hedge. When Lehman Brothers failed in September 2008, investors flocked to

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The Push For Paperless

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In addition, we are consolidating our two newsletters. Sherpa Insight has been providing monthly investment and financial planning insights in a hard copy version since August 2001. Sherpa Snapshots, our electronic newsletter designed to track the pulse of the economy, has been published since March 3, 2009. Starting May 19th, we will be consolidating the two publications and issuing them bi-weekly in an electronic format only. **So, unless you specifically request it, this will be your last newsletter in hard copy form.**



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Gold (continued)

gold. According to the World Gold Council, retail demand for gold bullion in the fourth quarter of 2008 was almost five times what it was in the same period in 2007. The question is: Does the current price of gold reflect the fact that investors think we are in a crisis or do they think a crisis is coming in the future? Ultimately, an investment in gold, therefore, is based upon the belief by the investor that a crisis will occur that is not already “discounted” into the current price of gold.

Assuming one concludes that they would like to invest in gold, this can be accomplished in four basic ways:

- Exchange Traded Funds (“ETF”s), such as GLD
- Gold coins, bullion and bars
- Gold mining stocks and other certificate programs
- Within a precious metals asset class investment

ETFs are the easiest and most direct way to invest in gold. The New York Stock Exchange’s offering, which trades under the symbol GLD, tracks the price of gold bullion. It’s very liquid and moves with the market. Furthermore, the ETF actually owns 82,000 gold bars weighing 400 troy ounces each. That’s \$31 billion of

bullion stashed away in an HSBC vault in London, that’s audited on a regular basis.



If someone wants to hold gold physically, that’s not so easy. When buying bullion, investors can expect to pay premiums of 10% or more above the spot gold price. In addition, there are questions about the authenticity of the bullion/bars and then investors need to consider space and storage for the gold. Furthermore, because of the amounts involved, there have recently been documented scams of companies taking the investor’s money and never delivering product.

Investments in gold mining stocks and other certificate programs are indirect investments. These are not a pure play on gold as they are also impacted by the company’s ability to find and mine gold profitably. This adds a further level of risk.

Lastly, exposure to gold can be obtained through an investment in a precious metals ETF or mutual fund. Since such a fund might also hold silver, platinum and other precious metals, you get a little more

diversification as well. Because of the volatile nature of gold and other precious metals, we recommend that such an investment be handled in a tactical manner, not as a long-term strategic investment. As an example, 20% of our DTIS program in December ‘08 was invested in the Rydex Precious Metals Fund. That fund appreciated 39% that month. However, in January the fund dropped considerably and we stopped out, meaning we sold the position once it decreased 6% because it met our self-imposed risk-management rule.

In summary, we see gold as a crisis hedge and a volatile investment. And, from time to time it can be an excellent part of a well-monitored tactical investment strategy. We are happy to discuss gold and any other investment opportunity at any time. Please give us a call.

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