Devina Mehra: Investors must see through gold's glitter as a risk-free investment

Devina Mehra | 23 April 2025

Simply put, it is not always the metal's value going up. (Pixabay)

SUMMARY

The metal is in vogue as a 'safe haven' in these times of global uncertainty, but an evaluation of its track record shows why it's overhyped as one. There are better investments to be made, especially with gold prices now at an all-time high.

The phrases 'risk free asset' and 'safe haven' have come back into vogue as far as gold is concerned. This is an addition to the inflation-protection narrative that was prevalent a year or so ago.

As we all know, the price of gold has skyrocketed and is at an all-time high. US President Donald Trump's tariffs and antics have put a question mark on the future of the US dollar (*see my last column*), and suddenly in most open forums, I am getting a lot of questions about gold.

So is gold really a safe haven or risk free? What does the data show?

Taking a wide-angle lens to look at gold prices for 50 years offers a wholly different picture from its general image.

The metal reached a price of over $666 per ounce in September 1980. Where was it some 19 years later in September 1999? At $255 per ounce—a full 62% lower! It crossed the $666 price next in 2007, nearly 27 years after the first high. The next high? $1,772 in 2012. And then a 40% fall to $1,062 three years later. A new high had to wait eight years to 2020, post the covid panic.

That, ladies and gentlemen, is the story of gold in a few sentences.

Gold as a safe haven? Doesn't look like it, does it? So were our grandmothers wrong in putting their savings into gold? Not quite. Indians were in a peculiar position until fairly recently, as there were capital controls and hence Indians could not invest in overseas assets. And that is why the rupee price trend of gold looks reasonable.

Simply put, it is not always the metal's value going up. A large part of the uptrend reflects the rupee going down. In short, for Indians, gold was a hedge against rupee depreciation. The only accessible one. So the rupee chart of gold prices looks okay. Remember that now other global assets are also available for investment and there's no reason to be locked into gold. Also, given the return data floating around, looking at its performance over one year, five years or even 10 years may mislead you, as the start date is usually carefully selected in such analysis.

Next question: Gold may not have done very well on an absolute basis, but it is still a relative safe haven, isn't it? So let us see how gold has done versus equities—over the long term.

Does gold provide better inflation protection than, say, US equities?

Data since 1950 shows that when adjusted for inflation (i.e., in real terms), gold has experienced a much steeper maximum price drawdown (nearly 82% from high to low) compared to US equities (around 64%). Even more compelling is the fact that the US equities real-return index exhibits a generally upward trend, while gold's real-return index has seen significant swings.

Gold, in contrast to its reputation, has been no safe haven, with bigger price drawdowns than equities and greater volatility.

Hence, gold can be part of your asset allocation—just not a very large part. And an all-time high price is not the point at which you should be aggressively adding to your position. Note that Indian households have begun to sell rather than buy gold. Since the discussion started with how uncertainty introduced by US policies has begun to make gold look better, there is another side-light to it: Is the gold held globally by central banks safe?

If all bets on US laws and institutions are off, Germany and other countries must wonder whether their central bank gold held in the US is safe anymore. New York sits on thousands of tonnes of gold, all of it belonging to nations other than the United States of America. It is literally the City of Gold!

The Federal Reserve of New York has more than 6,000 tonnes of gold in its basement. And this does not even belong to the US. As the website of the Federal Reserve of New York states, "As of 2024, the vault housed approximately 507,000 gold bars, with a combined weight of 6,331 metric tons. The vault is able to support this weight because it rests on the bedrock of Manhattan Island, 80 feet below street level and 50 feet below sea level."

As the US keeps its own gold at Fort Knox and some other military establishments, the gold at the Federal Reserve mostly belongs to the central banks of other countries around the world. This safe-keeping started around World War II and has been continued by many countries thereafter. There is, of course, an elaborate security system (and maybe there is a heist movie or series waiting to be made on this).

Also, gold bars are not considered fungible, which means that each central bank gets back the very gold bars that it had kept inside. This is also partly because gold bars are never 100% gold. As we studied in school, this is a very malleable and ductile metal, which means that it can be drawn into extremely thin sheets or wires. Hence, as every Indian knows, gold jewellery is never made out of 100% pure or 24-carat gold. So also with gold bars. Some other metal needs to be added to the mix to give it solidity.

So, besides the fact that investors have to decide whether or not to invest in gold, central banks have to decide whether the US is a good jurisdiction anymore to physically house their gold holdings.

The author is chairperson, managing director and founder of First Global and author of 'Money, Myths and Mantras: The Ultimate Investment Guide'. Her X handle is @devinamehra