



Bullion University: 7

Gold vs. cash - which is the better savings asset?

There is an almost eternal debate between the merits of using physical gold and silver as a monetary system compared to using a fiat system implemented by legislative decree.

And whilst we firmly believe that gold and silver are far superior monetary standards; that we never should have abandoned them, and that the root cause of the GFC was excessive credit/money creation, the reality is that, at least for now, we do live in world where fiat money is the dominant form of money, especially the US dollar, which still acts as the global reserve currency.

Physical gold and silver are on the periphery, out of the minds (and portfolios) of the majority of investors.

Ignoring the respective monetary qualities of either form of money for a moment though, the most important thing any investor can focus on is, which is the more effective form of money to save in?

Is it smarter to save in gold, or in fiat, paper money?

To answer this, we've gone all the way back to 1971 when Richard Nixon abandoned the Gold Standard.

We've taken the average US dollar gold price for each and every year since that day, and assumed that we had purchased 1 extra ounce every year at the average price in each year since then.

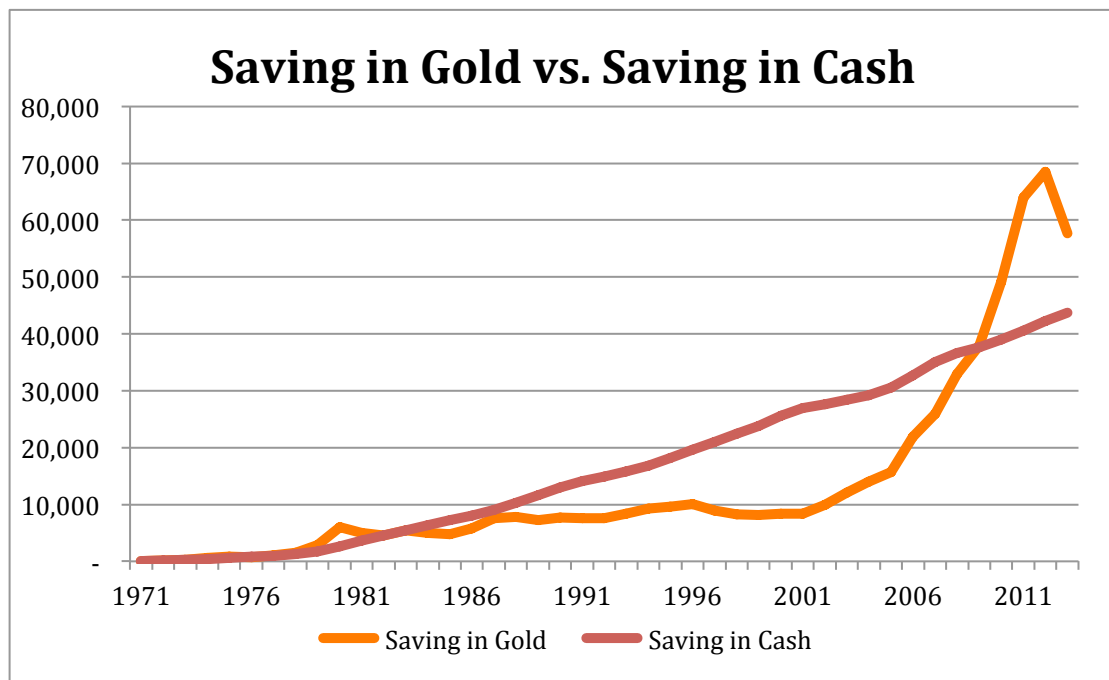
We've also taken the Federal Reserve Funds rate for every year since 1971, and compounded the returns for money invested in 'cash', assuming that instead of buying 1 ounce of gold in 1971 for \$41 (yes it was that cheap back then), you had put \$41 in the bank instead.

We've also added in an annual contribution equivalent to the cost of the ounce of gold in each particular year to the opening bank balance, so that the total amount of money invested in both gold and cash is the same over the whole period.

So, which ended up being the better investment?

As you can see from the chart below, the answer is a no brainer. Saving in gold has been a much smarter idea.

Note that the numbers below aren't adjusted for inflation (which would affect both returns equally), nor has taxation been accounted for.



The following table provides some more clarity on the outperformance of gold, and some of the numbers involved.

Metric	Gold	Paper Dollars
Amount Invested	\$19,976	\$19,976
Final Value	\$57,663	\$43,679.67
Multiple of Return	2.89	2.19
Average Gain	11.21% p.a.	5.70% p.a.
Best/Worst Decade	39.54%/-3.36%	9.44%/1.84%

As you can see, the outperformance one would have benefited from by investing in gold is quite significant - an investor in gold would have accumulated just under \$14,000 more (\$13,983.33 to be precise) than the investor in cash.

That's a healthy percentage when you consider the total invested is only \$19,976, and highlights the clear benefits saving in gold can provide to an investor.

The post-GFC world

What's even more important is what has happened since the GFC struck. As we know, cash rates have essentially been stuck at zero, heading down from 5% in 2007 to 2% in 2008 and to 0-0.25% from then onward.

Indeed, an investor in cash, despite having on average \$40,000 invested in a bank account the past 6 years, has earned less than \$1000 in interest in this period.

This is the ugly side of the Federal Reserve's zero interest rate policy that has frustrated anyone trying to save the supposedly 'old-fashioned way', and it is an issue affecting the entire developed world, including Australia now, with our interest rates at all time lows.

Alternatively, since the GFC, had an investor saved in gold (the real 'old-fashioned way' to save), over the last 5 years they would have seen the value of their savings nearly double, from just shy of \$33,000 at the end of 2008 to over \$57,000 today.

But gold is volatile!

Despite the fact that gold has clearly been a better savings asset, there is a potentially justifiable concern around the volatility of gold.

Cash in a bank obviously doesn't change in value on a day-to-day basis, even though the rate of return does change in line with interest rates set by the central bank and the relevant bank you keep your money with.

In order for this story for change, and for the value of cash in a bank to be worth more than savings in gold, the gold price would need to drop to basically USD \$1000 (\$1008 to be precise using the modelling in this article).

Whilst anything is possible, in an environment of ultra-low interest rates, central bank money printing, low yields on financial assets and elevated economic uncertainty, the fundamentals underpinning the precious metal market are overwhelmingly bullish.

With that in mind, it's likely (although not certain) that the gold price will rise in the years ahead.

On the flip side of the coin, interest rates on cash are likely to remain at historical lows (i.e. zero in real terms), as the amount of debt owed by governments, individuals and businesses prevents a meaningful interest rate rise, which would cause huge problems in the economy.

Therefore, whilst it's definitely accurate to say that cash in a bank is a less volatile way to build savings on a day-to-day basis, long-term wealth builders, and long-term savers have been far better saving in physical precious metals.

It's unlikely this will change in the foreseeable future.

For those of you interested in the merits of physical gold vs. cash in a bank, [we highly recommend the following video.](#)

This article was written on Monday 30th September 2013, using the London PM Fix USD Gold price of USD \$1341 which was struck on Friday the 27th September.

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