How to Start Investing in Gold Using ETFs

Description

Investing in gold is a great way to diversifying portfolio. For example, as inflation hit 40-year highs this year, and interest rates rose, both stocks and bonds fell in tandem. Conversely, gold has managed to retain its value, falling just -0.27% compared to the 10% loss suffered by the S&P 500 index.

Gold is perceived both as a store of value and safe-haven asset, making it an investment of choice for individuals seeking safety from geopolitical risk, weak economies, or currency devaluation. Its lower correlation to both stocks and bonds makes it a great choice to round out a portfolio.

While Canadians can buy physical hold bullion or invest in gold miner stocks, an easier way might be to buy a gold exchange-traded fund (ETF). These funds can either hold deposits of physical gold bullion in vaults or a portfolio of gold miner stocks. Let's look at some funds for each approach!

Physical gold ETF

iShares Gold Bullion ETF (TSX:CGL) offers exposure to a vault of bullion stored in trust with a custodian. The contents are audited frequently, and each share of CGL you purchase corresponds to a fractional ownership of the gold hoard. As a result, CGL's price tracks the spot price of gold fairly well.

CGL is currency hedged. Because the price of gold trades in U.S. dollars (USD) but CGL trades in Canadian dollars (CAD), fluctuations in the USD-CAD exchange rate can cause volatility in its price. CGL uses a derivative called a futures contract to minimize this, so your returns match the price of gold and are not affected as much by foreign exchange changes.

In terms of fees, investing in CGL will cost you an annual expense ratio of 0.55%, deducted from your total investment. For example, an investment of $10,000 in CGL will cost you around $55 annually in fees. This is more expensive than the average index fund but typical for a commodities fund.

Gold miner ETF

An alternative to physical gold ETFs are ETFs that hold gold miner stocks. Compared to the former, gold miner ETFs tend to have more positive expected returns but are higher correlated to the stock market given that their underlying holdings are stocks, not actual gold. This gives them less diversifying power.

Still, gold miner ETFs are a great way to tilt to gain gold exposure while still investing in stocks. A great option is **iShares S&P/TSX Global Gold Index** (TSX:XGD), which holds 47 small-, mid-, and large-cap gold miner stocks from Canadian, U.S., and South African markets.

XGD currently pays a strong forward annual distribution yield of 3.76% but hasn't had the greatest historical performance, posting an average annual 10-year total return of -1.22%. The fund is also fairly pricey with an expense ratio of 0.61%, which is slightly higher compared to CGL.

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