The relevance of gold for Australian Self-Managed Super Funds

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Gold, in Australian dollars (AUD), delivered positive returns in 2022 and this has continued so far in 2023. It has attracted attention: not only have global central banks continued to buy gold , but Australia's sovereign wealth fund has also added gold to its portfolio.

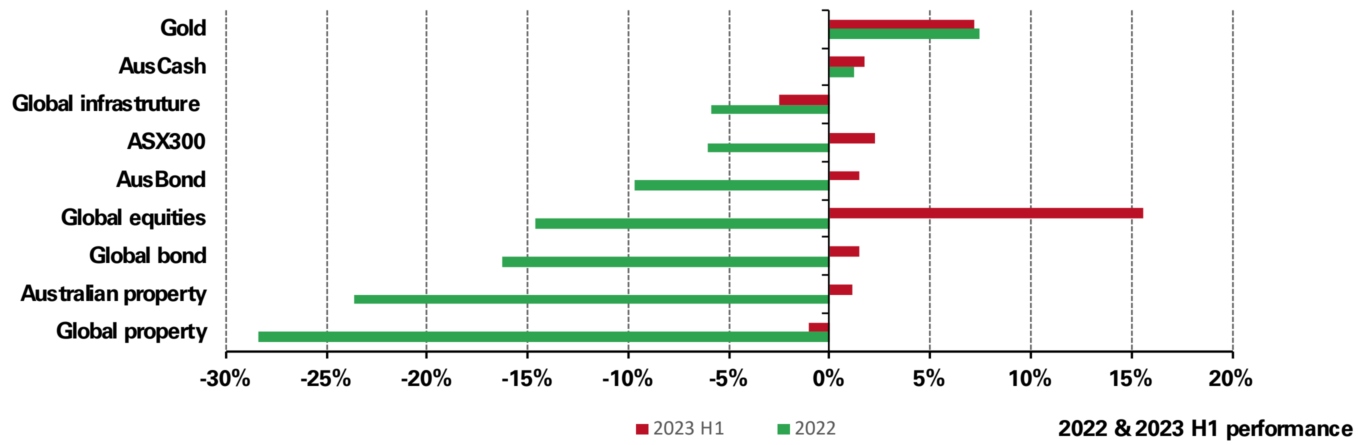
Looking further into 2023, most assets may see headwinds as stagflationary pressures intensify; our analysis, based on historical data, shows:

- gold has historically posted superior returns during stagflationary periods
- gold can improve the risk-adjusted return of a portfolio comprising of asset classes traditionally held by Self-Managed Super funds (SMSF).

Gold continues to perform in 2023

Following a staggering 2022, gold in AUD has continued to outperform major assets this year (Chart 1). While most assets plunged last year amid high inflation and rising rates, gold delivered a 7% return.[1] So far in 2023, gold has been spurred on (+7%) by intensifying expectations that major central banks will end their monetary tightening cycle, as well as by fears of a potential recession ahead.[2] As noted in our 2023 Mid-year Outlook, gold may remain well supported in H2 as yields could remain relatively stable and the dollar might weaken. And should global economic conditions deteriorate, gold may experience stronger safe-haven demand during the second half.

Chart 1: Gold's performance has topped major assets in 2022 and so far in 2023
Annual returns on major assets in Australian dollars (%)*



*As of 31 December 2022. 2023 Y-t-d refers to 30 June 2023. Based on LBMA Gold Price PM, AusBond Bank Bill Index, AusBond 0+ Composite Index, Bloomberg Barclay Global Agg, ASX300 Index, MSCI World Index, ASX300 A-REIT Index, FTSE EPRA/NAREIT Developed ex-Australia Index, FTSE Developed Core Infrastructure Index. All calculations are in AUD.

Source: Bloomberg, World Gold Council

[1] Based on LBMA Gold Price PM in AUD, data to 31 December 2022.

[2] Based on LBMA Gold Price PM in AUD, data to 30 June 2023.

Table 1: The Future Fund's summary of portfolio implications and reactions

Portfolio implications	More alpha	More volatility	More granular	More correlation caution	More domestic exposures	More defensive levers, inflation protection
Levers activated	More private equity	Focus on liquidity and dynamic asset allocation	Detailed levers for DM/EM	Broader currency basket	Added to infrastructure	Added gold, commodities, tangibles, alternatives

Source: The Future Fund, Position Paper – The death of traditional portfolio construction?, December 2022

Gold's strength has been attracting attention. Central banks remained committed buyers in Q1 2023, adding 228t to global reserves after a record level of annual buying in 2022 (1,078t). Even though their buying spree could slow, we expect global central banks to remain net gold purchasers in 2023. And as our 2023 Central Bank Survey shows, over the next 12 months, 24% of central banks expect their gold reserves to increase whilst 71% believe global gold reserves will rise []

In its most recent position paper, the Future Fund, Australia's sovereign wealth fund, announced the addition of gold to its portfolio. Their paper indicates that challenges such as high inflation and the weakened defensive nature of foreign currencies may have prompted its decision to buy gold – risks that are also found within an SMSF (Table 1).

Bumpy road ahead

Markets may be vulnerable to negative shocks for the remainder of the year – most notably stagflation (Chart 2). This is a key concern shared by the Future Fund, highlighting that we may face an environment where inflation remains elevated and growth slows over the coming years. This scenario could be amplified by factors such as geopolitical conflicts.

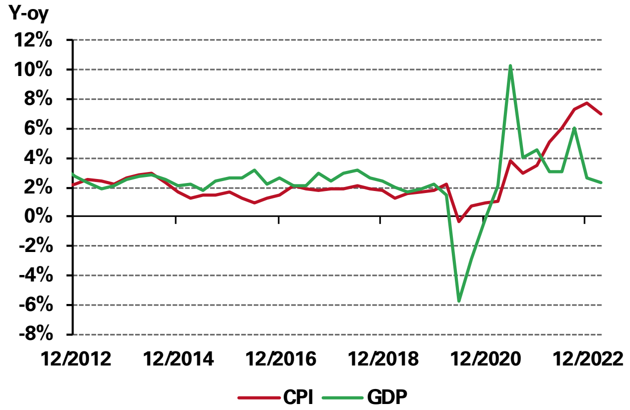
"In this kind of environment there is a real risk of simultaneous slow growth, high unemployment and rising prices…"

– The Future Fund, Position Paper – The death of traditional portfolio construction?, December 2022

In Q1 2023, Australia's quarterly consumer price index (CPI) rose to 7% y/y (Chart 2); well above the target range of 2 to 3% and topping economists' consensus expectation of 6.9%. As the Reserve Bank of Australia (RBA) noted in its June meeting, when it surprised investors with another 25bps hike, upside risks to the inflation outlook has increased and it might be difficult to achieve a soft landing for the local economy.

In the meantime, the future growth projection for 2023 has been dialled down further, from 1.8% to 1.5% according to Bloomberg's economic forecasts in January and June.

Chart 2: Australia's inflation remains elevated while GDP growth has weakened

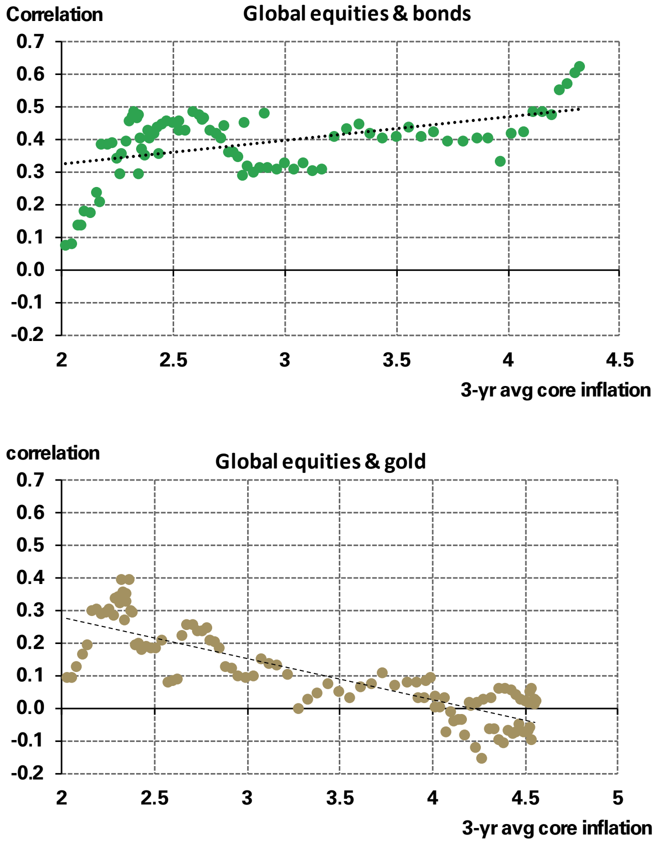


*As of 31 March 2023.
Source: Australian Bureau of Statistics, Bloomberg, World Gold Council

Cross-asset implications

Elevated inflation can, broadly speaking, create significant issues for investors. For instance, the correlation between bonds and equities – two asset classes that represent a large proportion of many SMSFs – tends to rise during high-inflationary periods. Gold, on the other hand, remains an effective diversifier as inflation rises (Chart 3).

Chart 3: Gold is a more effective diversifier than bonds at higher inflation levels
Correlation patterns of bonds and equities, gold and equities at different inflation levels*

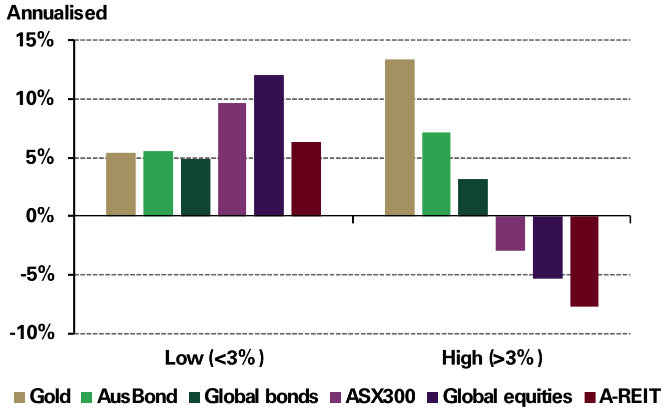


*Note: Based on monthly data of MSCI World Index, Bloomberg Global Treasury Index (AUD hedged) and LBMA Gold Price between 1990 and 2021. All calculations in AUD.

Source: Bloomberg, World Gold Council

In fact, gold has long been considered a hedge against inflation, and historical data confirms this (Chart 4). Also, the annualised return of 7.6% in AUD over the past 20 years has outpaced CPI both in Australia and globally.[3]

Chart 4: Gold has historically performed well in periods of high inflation
Major asset returns in AUD during high and low inflation environments*

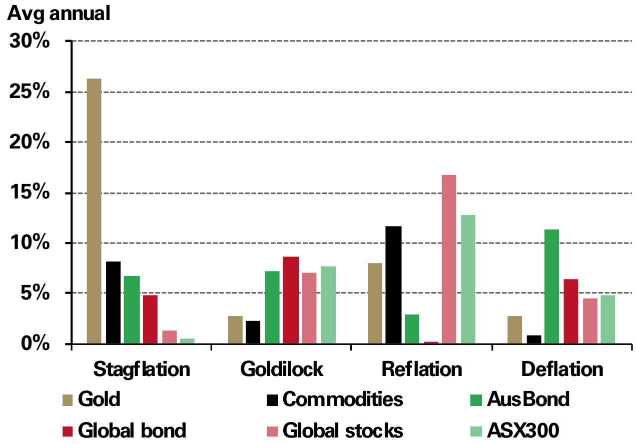


*Based on Australian quarterly CPI, AusBond 0+ Composite Index, Bloomberg Barclay Global Agg, ASX300 Index, ASX300 A-REIT Index and MSCI World Index between Q4 1992 and Q1 2023. All calculations in AUD.

Source: Bloomberg, World Gold Council

Stagflationary pressures pose challenges for all investor portfolios. Stagflation can severely disrupt financial markets and hamper the performance of major assets. But historical data shows that gold, a safe-haven asset, has benefited investors with attractive returns during such periods (Chart 5).

Chart 5: Gold has delivered superior performance during stagflationary periods in Australia
Major asset returns in AUD during different economic scenarios*



*Data between Q1 1973 and Q1 2023. ASX300, AusBond, Global bond and Global stocks only date back to the 1990s. All calculations in AUD. Based on quarterly data of Australian GDP, CPI, LBMA Gold Price PM, AusBond 0+ Composite Index, Bloomberg Barclay Global Agg, ASX300 Index, MSCI World Index and Bloomberg Commodity Index.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

3 For more, see: Gold Price Returns | Gold Prices | World Gold Council

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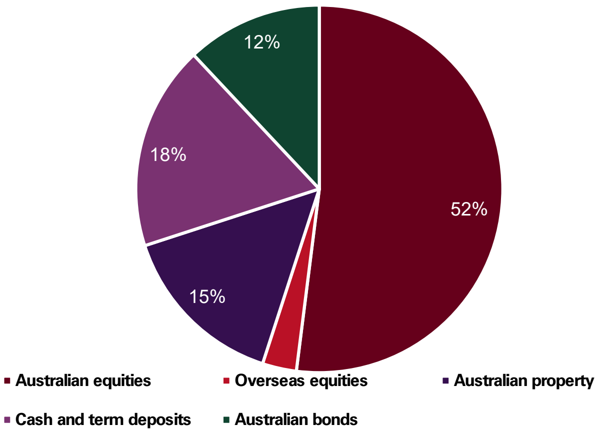
Gold's portfolio impact

Our analysis shows that a portfolio comprising assets typically held by SMSFs (Chart 6) would have achieved higher risk-adjusted returns and lower drawdowns with an allocation to gold (Chart 7).

Chart 6: Hypothetical SMSF portfolio

Asset allocation comprising assets typically held by SMSFs



*As of 31 December 2022.

Source: World Gold Council

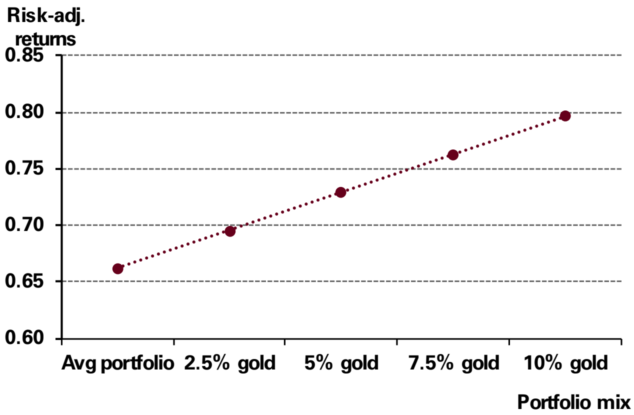
Moreover, investment performance over the past 3, 5, 10 and 20 years emphasises gold's positive impact across various investment horizons (Table 2).

Conclusion

Gold's stability and defensiveness, among its other qualities, have caught investors' attention supported by its strong performance.

Chart 7: Adding gold over the past 20 years would have increased risk-adjusted returns of a hypothetical SMSF

Risk-adjusted returns of a hypothetical portfolio with and without gold



*Based on AUD performance between 31 December 2002 and 31 December 2022.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

This year we anticipate elevated inflation and an economic slowdown, key ingredients of stagflation. This could severely disrupt financial markets and hurt investors' portfolios. Examining past data we find that not only can gold remain an effective equity-risk diversifier when inflation is elevated, it also posts superior performance in a stagflationary environment.

Gold is often viewed as a safe-haven asset, or even an investment portfolio insurance policy. But historic data shows that its performance during both stable *and* volatile conditions is highly competitive compared to other popular assets held by SMSFs.

Table 2: Gold has increased risk-adjusted returns while reducing portfolio volatility and maximum drawdowns

Comparison of an average hypothetical SMSF and an equivalent portfolio with 5% gold over the past 3, 5, 10 and 20 years based on AUD returns

	3-year		5-year		10-year		20-year	
	No gold	5% gold	No gold	5% gold	No gold	5% gold	No gold	5% gold
Annualised returns	2.6%	3.0%	4.6%	5.0%	6.3%	6.4%	6.4%	6.5%
Annualised volatility	15.0%	14.0%	12.3%	11.5%	10.2%	9.6%	9.6%	9.0%
Reward to risk	17.4%	21.6%	37.4%	43.6%	62.2%	66.7%	66.2%	72.9%
Maximum drawdown	-20.3%	-18.6%	-20.3%	-18.6%	-20.3%	-18.6%	-38.1%	-34.4%

*As of 31 December 2022.

Source: Bloomberg, ICE Benchmark Administration, World Gold Council

About the World Gold Council

We're the global experts on gold.

Leveraging our broad knowledge and experience, we work to improve understanding of the gold market and underscore gold's value to individuals, investors, and the world at large.

Collaboration is the cornerstone of our approach. We're an association whose members are the world's most forward-thinking gold mining companies. Combining the insights of our members and other industry partners, we seek to unlock gold's evolving role as a catalyst for advancements that meet societal needs.

We develop standards, expand access to gold, and tackle barriers to adoption to stimulate demand and support a vibrant and sustainable future for the gold market. From our offices in Beijing, London, Mumbai, New York, Shanghai, and Singapore, we deliver positive impact worldwide.

World Gold Council
15 Fetter Lane, London EC4A 1BW
United Kingdom

T +44 20 7826 4700
W www.gold.org

For more information

Jeremy De Pessemier, CFA
jeremy.depessemier@gold.org
+44 20 7826 4789

Johan Palmberg
johan.palmberg@gold.org
+44 20 7826 4786

Krishan Gopaul
krishan.gopaul@gold.org
+44 20 7826 4704

Louise Street
louise.street@gold.org
+44 20 7826 4765

Ray Jia, FRM
ray.jia@gold.org
+86 21 2226 1107

Juan Carlos Artigas
Global Head of Research
juancarlos.artigas@gold.org
+1 212 317 3826

John Reade
Market Strategist,
EMEA and APAC
john.reade@gold.org
+44 20 7826 4760

Joseph Cavatoni
Market Strategist,
North America
joseph.cavatoni@gold.org
+1 212 317 3844

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