The Benefits of Buying Physical Gold

JOSHUA ROTBART
J. Rotbart & Co.

"At the end of the day what we say, if the economy is good, people buy gold jewelry. When the economy is bad, people buy gold for investment and central bank buys it for investment. There's always very, very firm demand for gold, which means it's a very, very liquid asset."

What is the role of gold in a client's portfolio?

People buy gold for a few reasons. Gold is used for portfolio diversification. People invest about 5% to 10% of their portfolio in gold because this investment reduces the risk on one's portfolio, so it's a diversification strategy. Gold, because of its inverse correlation to the financial markets, then usually it will gain value while other assets are losing value.

Another reason is that gold is a very liquid global currency, like crypto to some extent. It's not issued by any government. There's no counterparty risk and it's recognised globally. It's very liquid. You can take your physical gold anywhere in the world and sell it - liquidate it for your local currency.

Gold is still part of our monetary system. Central banks are buying gold in bigger and bigger quantities and at a faster pace. The reason is that governments know that their currencies should be based on some gold holdings in the central banks.

And finally, gold has a very good demand. It's a very liquid market. If you look at that demand in general, physical gold is consumed mostly by jewelry and central banks, for investment and for industrial use.

At the end of the day what we say, if the economy is good, people buy gold jewelry. When the economy is bad, people buy gold for investment and central bank buys it for investment. There's always very, very firm demand for gold, which means it's a very, very liquid asset.

Obviously now in terms of high inflation, gold is a great hedge against inflation. Why? Because it keeps the value of our money. The reality is that the value of cash is going down, and the higher the inflation is, actually the value of our money is then deteriorating further. Gold keeps its purchase power, meaning that what we could buy with one ounce of gold, we could buy the same thing or even more than what you could have bought 10 years ago, 20 years ago, or even six months ago, because it's really about store value, about being able to maintain the value of our money.

What are the specific reasons clients buy physical gold today?

The reason generally people buy gold, especially now, is that we live in a very unstable, unpredictable and volatile world. Look at what has happened since 2020, since COVID and all the events that happened later like the hike

GET IN TOUCH
[View Joshua Rotbart LinkedIn's Profile]
[Find out more about J. Rotbart & Co.]

in interest rates, the growing concerns around debt in the US, geopolitical issues like the war in Ukraine, the decoupling between China and the US or generally the Western countries. We really do live in a volatile and unpredictable world.

What clients now see is how useful gold is, especially during this period. Even if you look at the performance of gold during COVID 2020, gold went up 23% in dollar terms. Gold went up, actually year-to-date in 2022, gold depreciate in pound almost 12%, because the economy in the UK was quite bad. Overall, clients are more concerned now with these specific issues - where are we heading in terms of geopolitics, in terms of the economy, in terms of inflation and it helps them understand more and more the importance of gold.

Especially since COVID, people see the value of their investment is going down 20%. My MPF in Hong Kong lost 20% of its value because they invested in the local stock exchange in 2022. My gold portfolio actually appreciated. A client can see the difference and why gold is so powerful, especially in volatile times like now.

The reason people look at physical gold versus ETFs or paper gold is security. Because with physical gold you don't have counterparty risk. You hold the assets, you store it, it's yours. When you buy paper gold, you're actually buying a promissory note. You buy unit trusts, issued by a third party, that guarantees to give you that price of gold in the future when you liquidate it.

If your concern is like many of the investors today of systematic risk in the financial system, or over-leverage of existing gold holdings or debt issues in the US or other countries, then of course buying paper gold will not cut it. Because people want the safety, they want the security, they want to be able to know that they don't have counterparty risk. If something happens tomorrow, there's a meltdown in the market, there's a bank going bankrupt like we see now, they can still go and redeem their gold without any issues.

Now the question is how do you buy physical gold? It seems like a very complicated and cumbersome process to go and look for it. The best advice I can give is don't go to the street shops, the street retailers. Do a little bit of research. The physical market or the gold market is still monitored by the London Bullion Market Association. The refiners of the product need to be members of the London Bullion Market Association, the LBMA. The logistic company, the dealers should be members of the LBMA. We work in a tight ecosystem that provides this solution in a very professional manner.

When you go and buy it at a shop, you'll pay high premiums on the product, on your investment and you may have issues selling it later. What we say to clients, especially to high-net-worth client or at least people who want to invest more than USD100,000 which is our minimum, is come to us, or companies like us, that can provide you the entire solution. Source the gold from reputable refinery, transport it, store it in a good private vault location that is safe, that has insurance coverage. Don't put it in your house, in a home safe that can be broken into or stolen. Make it professional investment. Put it with companies that have insurance policy, they have storage facilities and that can provide you the entire service from start to finish.

Today, you have professional storage facilities in all the major centers. For us, we are a Hong Kong and Singapore based company, so we of course focus in Asia. I would say the strongest demand we've seen in the last few years is for storage in Singapore because of its safety, stability and the good infrastructure for trading gold and storing it. But of course, Hong Kong is still a great place to store gold and we see growing demand for Zurich and Geneva, Switzerland, at the end of the day, has been a gold trading hub for decades.

We are seeing also clients diversifying, so we see clients put in Frankfurt for example, UK, we have a growing number of clients storing in Canada, actually in Toronto. We have clients that want to move their assets to Sydney. For me, the idea of storage is where the client feels safe. We cannot tell a client, Singapore is great, Hong Kong is not safe, or Zurich is great or London is not safe. It's where the client feels it's safe.

A lot of the time whether the client has access to their holdings, especially since COVID when travel was restricted. We had a client that got locked out of their gold. If you store it with a professional company like us and you reside in Europe, you can still sell your holdings that are in Switzerland or in Singapore. But if you are residing in Europe and you store it in a safety deposit box in a bank in Singapore and there's travel restrictions, you cannot take your gold.

What has been the impact from the recent banking issues?

We see a lot of questions about stability of banking systems, whether in the US or Switzerland. Credit Suisse is of course the big name that comes to mind. The immediate reaction of clients is to try and get assets outside those banks, outside the banking systems. Which leads us to the question of why would you store your gold in a bank's vault?

At the end of the day, and again more clients realise it now because of the issues with the banking system, gold is your safe money. It's your insurance policy for any day, for times when there's crisis. You don't want to keep it with a bank because it may not be safe. There are systematic risks when you put it in a bank because all our financial assets anyhow are within the banking system. I think this safe portion, this 5% to 10% of physical gold should be kept separate to your financial assets in a non-bank private vault.

There are many options globally, other than J. Rotbart and Co. There are other companies globally that offer these services. The immediate reaction to the collapse of various banks is to get my gold out of the banking system. I don't know what's going to happen if my bank is folded. I need to get this money outside the banking system, and that's what we do at J. Rotbart and Co.

What's the connectivity today between gold and crypto?

To be very direct, there's no connectivity between crypto and gold. There used to be a lot of talk around Bitcoin being the new gold, Bitcoin being a store of value. But we know now as we get the data and we see the price behavior of Bitcoin, that actually Bitcoin usually correlates with the financial markets and is not a good store value. I think the question that a crypto investor had in the beginning of the crypto buzz, is whether it can replace gold. I think the answer is negative; Bitcoin cannot replace gold.

Having said that, we do see a lot of clients that as part of their diversification, they have gold as a safe asset and they have crypto as the more risky asset with, I would say, a high potential for gains. What we see in our activity is that a lot of clients come to us because either they want to convert from the volatile world of crypto to stable world of gold, or sometimes vice versa. They want to move from gold because they

believe there's another boom coming to the market.

Of course, it's a matter of timing with the market. We haven't seen too many clients moving from gold to crypto in the last year. Obviously if you look at the price of Bitcoin, it hasn't done well. We've seen more clients actually moving from crypto to gold. But of course we know that this may change, so we are keeping our options for client to do both of these transfers between those two assets. But definitely the one thing we do see is that clients are more open to have both assets rather than just one of them. If you're crypto investors, you're open to having gold now. If you're a gold investor, you say maybe I should have some crypto in my portfolio.

Can clients borrow against physical gold?

Mostly since the pandemic started in late 2019, we have had requests from clients that actually needed some cash flow, either to buy other assets that were at a bargain price if you like, or they needed cash for their business because it was shut down due to COVID restraint. However, those clients didn't want to sell their gold portfolio because obviously gold was doing very well both during COVID and since.

We came up with a solution of lending clients money using their precious metals holdings as collateral, and the process is very simple. Clients can bring either existing bullion or buy new bullion from us. We can store it for them in any of our locations. We have 12 locations globally that we can store the gold at, and the client can take up to 85% of the value of their portfolio as a loan.

Because we are not a bank, of course our terms are more flexible. We are not closing position, we're not very strict about closure of positions and margin calls. We have the rules, but we work with the client and understand what the client needs in order not to surprise them with requests for liquidation and so on.

We do not limit the flow of the funds. Clients can take a loan using their gold as collateral and invest it in any avenue they want to. If clients have better investment opportunities in the market, that's one option. A lot of the time the client will take a loan, the client will buy gold from us, will take a loan and re-invest it with the private bank or with the asset managers.

I think it's worked quite well from a client point of view, for our partners in the private wealth industry because they don't lose AUM. For us, it keeps everyone in a win-win solution where the gold is there to appreciate, it still appreciates at 8% to 10% like gold appreciates every year, but they can still use the cash for other purposes.

How does that lending process work?

At J. Rotbart and Co. we have a few companies in our group. One of our group is a monthly lending regulated business here in Hong Kong. The technicalities around the lending arrangement is that J. Rotbart and Co. Bullion Company actually protects and customised clients holdings on behalf of the money lending company, which is again part of our group and is a licensed business here in Hong Kong. It's a tri-party arrangement between the client and two of our group companies.

Basically, clients are still the owner of the goods, but the client waives possession as long as the loan is not paid. In case the value of the gold goes down, for example, we lend up to 85% of the gold's value and the value in gold price dropped, let's say it's 7%, then we will have a margin call. We'll call the client and we'll say you need to top up the collateral or pay back some of the loan. We give them, of course, a few days, work with the client. We're not a bank, we're very flexible in terms of early payment measures.

Of course if there's further depreciation in the price of gold, we will close the position and we will sell the gold and cover the loan. But I have to say it never happened to us, never happened to us for two reasons. One, gold's price is quite stable. For gold to lose 10% of its value in a few days, I think it's happened last time maybe in the seventies. It just doesn't happen.

But also our clients are usually the families and individuals that have worked with us for decades. We've been in this business for 13 years, so we want to maintain the relationship. A lot of the time, even if legally we are allowed to close the position, we will work with the client and try to understand if there's cash coming in anytime soon, assess our risk and decide whether it's right to close the position or not.

So far actually, we haven't done that because there is enough margin between the loan to value that we lend to clients and the price of the gold. Again, we're quite flexible on this. Of course we're not going to lose money. It's still a loan that needs to be paid, but we will work with the client if there are any issues. ■