Gold in Portfolio: A Long-term or Short-term Diversifier?

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ABSTRACT

The purpose of this paper is to evaluate the role played by gold in a diversified portfolio comprised of bonds and stocks. The continuous wavelet transform analysis is applied to capture the correlation features between gold and other risky assets at a specific time horizons to determine whether gold should be included in a diversified portfolio. This paper uses the U.S. stock, bond, and gold data from 1990 until 2013 to investigate the optimal weights of gold obtained from the minimum variance portfolio. Empirical findings suggest that little evidences support that gold acts an efficient diversifier in traditional stock and bond portfolio. Gold typically has been a long-term diversifier in the traditional portfolio comprised of bonds and stocks only before the early 2000s and acts as a short-term diversifier in times of crisis periods. The significant drop in the long-term weight of gold indicate that gold loses much of its long-term role in the diversified portfolio. These findings are useful for portfolio managers to justify the gold's diversification benefits over different investment horizons.

Keywords: gold, commodity diversifier, investment horizons, continuous wavelet analysis

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