How to Build the Ideal Gold Portfolio

Chris Lowe
March 01, 2019
12 min read

This week, we're back to one of our favorite topics – gold.

As regular readers know, we believe we're in the early stage of a bull run for gold.

And we're getting set up to profit.

In last week's dispatch, I (Chris) talked to one of our go-to gold investing experts here at Legacy Research, E.B. Tucker, about why gold prices are headed higher.

We also talked about how you can use gold mining stocks to add some speculative oomph to the price of bullion.

Ideal Portfolio

This week, E.B. and I take a deeper dive into how to build the ideal gold portfolio.

If you don't already know him, E.B. heads up our *Strategic Investor* advisory. He's also an industry insider who sits on the board of a fast-growing gold royalty company.

E.B. is a firm believer that the cornerstone of any gold portfolio is the physical metal.

Physical gold has survived every major financial crisis in history – making it the ultimate safe-haven asset.

But you may be surprised at the gold investment he says should make up the biggest part of the mix.

It's a type of gold company that doesn't own mines directly… but instead, owns "slices" of lots of other people's mines.

E.B. also has advice on how to potentially make 10x your money on the most speculative gold investment of them all.

I hope you enjoy this week's conversation. I consider it… along with Part I of my conversation with E.B. last week… to be a master class on gold investing. But make sure to let us know your thoughts after you're done reading – you can email us at feedback@legacyresearch.com.

Q&A With E.B. Tucker (Part II)

Chris Lowe: In last week's *Legacy Inner Circle*, you said the 12% rally in gold we've seen since last summer is just getting started. You also talked about how our members could "leverage" the coming gains by buying shares in gold mining stocks.

This week, I want to talk about how to build a gold portfolio from the bottom up.

We've already talked about the importance of physical gold… and why gold stocks amplify the gains of the physical metal. But all gold stocks are not created equal. Let's start by breaking down the options.

E.B. Tucker: The three main categories are called the majors, the juniors, and the explorers. We talked about the majors last week. They're the big mining companies with operations around the world and market values of $10 billion and over. Think Newmont Mining, Goldcorp, and Barrick Gold.

So let's move on to the juniors and explorers. Juniors produce about half to a quarter of what the majors produce. They may operate two or three mines that produce 1 million ounces a year.

The juniors don't have the global scale the majors have. They're often regionally focused. So they may have two mines in Canada and one in Nevada. And that's it.

Chris: Why would you invest in these smaller companies if the larger ones control more assets and have more stability?

E.B.: If a junior miner discovers one more deposit, it means a big increase in its production. Whereas, if a major discovers one more deposit now, it's not that big a deal.

For example, before they announced the proposed merge earlier this year, majors Newmont Mining and Goldcorp were running mines with attributable, proven gold reserves of 65.4 and 52.8 million ounces, respectively. With a company that size, it's hard to move the needle with any single new discovery. So the growth potential for the majors is a lot less than it is for the juniors.

Chris: What kind of shape are the juniors in today?

E.B.: The juniors are eking out just enough money to survive. They're having a hard time accessing capital markets. Mainstream investors are so down on gold that even the higher-quality juniors are struggling.

That may sound bad. But it's actually a great time to buy. Junior gold miners are one of the most beaten-down and hated groups of stocks out there. The VanEck Vectors Junior Gold Miners ETF (GDXJ), which tracks a basket of about 50 of the most commonly traded gold mining stocks, has plunged 82% since peaking in December 2010.

Chris: What about the last category of gold miners – the explorers?

E.B.: When you see a move higher in gold, exploration stocks have these crazy moves higher. Even garbage exploration stocks months away from running out of money go on these massive rallies when gold catches people's attention and moves higher.

Exploration stocks are pure speculations. They have no assets in the ground. They're out there hoping to find a deposit… as long as someone keeps giving them money to look for it.

Despite this, people love exploration stocks. They say, "Well, you never know. They might drill into the ground and find something." And that's true. Explorers sometimes find gold. And that's when we see these explosive moves higher.

Take NovaGold Resources, for example. NovaGold was trading at about $0.40 in December 2008. Two years later… after a few strategic partnerships boosted the company's gold reserves by 6 million ounces… it traded up to $14.46 per share – a gain of about 3,500%.

Still, you need to be extra-careful with exploration stocks. Your upside potential is 1,000%-plus. But your downside potential is 100%. That's why I recommend that most folks keep their exposure to the explorers to a minimum.

Chris: We'll get to the exact breakdown you recommend for an ideal gold portfolio in a moment. First, there's a different type of gold stock we haven't mentioned yet.

We've been talking about gold miners so far. But what about gold royalty stocks? You understand how these companies work better than most. Where do they fit into the picture?

E.B.: Royalty companies finance mining companies in return for a payment – or royalty – on what the miners produce.

I'm a big fan of royalty companies. Mining stocks are great as short-term speculations. But royalty companies are great as long-term holdings. They're the kind of gold stocks you buy and hold.

Royalty companies may have royalties on 10, 20, maybe 30 years of production. They don't care if that gold is hard to get out of the ground… or if the mining company's margins are razor-thin… or if it has to lobby some foreign government to keep ownership of its mine.

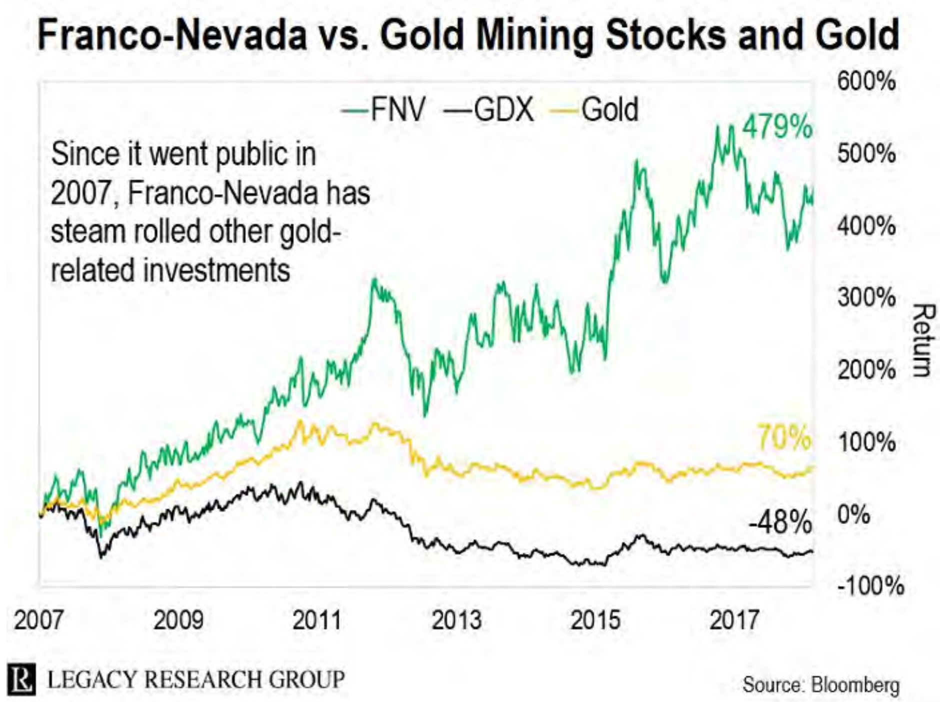
Royalty companies own 1% or 2% of that miner's production – regardless of how hard or costly it is to dig the ore out of the ground. Whatever the miner gets out, the royalty company owns a share of it.

Chris: Can you give us an example of how this model works?

E.B.: Take Franco-Nevada. It's the biggest gold-focused royalty company in the world.

It went public in 2007. Since then, it has steamrolled other gold-related investments.

If you'd bought shares of Franco-Nevada when it returned to the public market in 2007, you'd be up 479% today. Over the same time, physical gold is up just 70%. And the VanEck Vectors Gold Miners ETF (GDX) – a good proxy for the global gold mining sector – is down 48%.



Chris: Is the outperformance of Franco-Nevada over regular gold miners down to the difference between the business models of a royalty company and a company that goes out there and actually digs rocks out of the ground?

E.B.: Royalty companies have great business models. As long as there's no trouble with the mines in their portfolios, they're just in the business of cashing royalty checks.

They know what the mine's going to produce because it's planned by engineering firms in advance. The management of a mining company goes to market and says, "We can produce 1 million ounces a year for 10 years." If you buy a 1% royalty on that, every year for 10 years, you're going to get a check for the value of 10,000 ounces of gold.

Chris: No business model is without risk. Talk me through the possible downside for royalty companies.

E.B.: Look, if there's an earthquake, and production goes on pause for a year, your royalty payments will stop. Let's say you've secured 1% of production. If production goes to zero for the year, your royalty will, too.

You'd think that would hurt the royalty company's share price. And sometimes it does. But with a larger royalty company such as Franco-Nevada, the risk is very low. It has a list of royalties as thick as a phone book. It doesn't matter in the long run to Franco-Nevada – or its shareholders – if one is down.

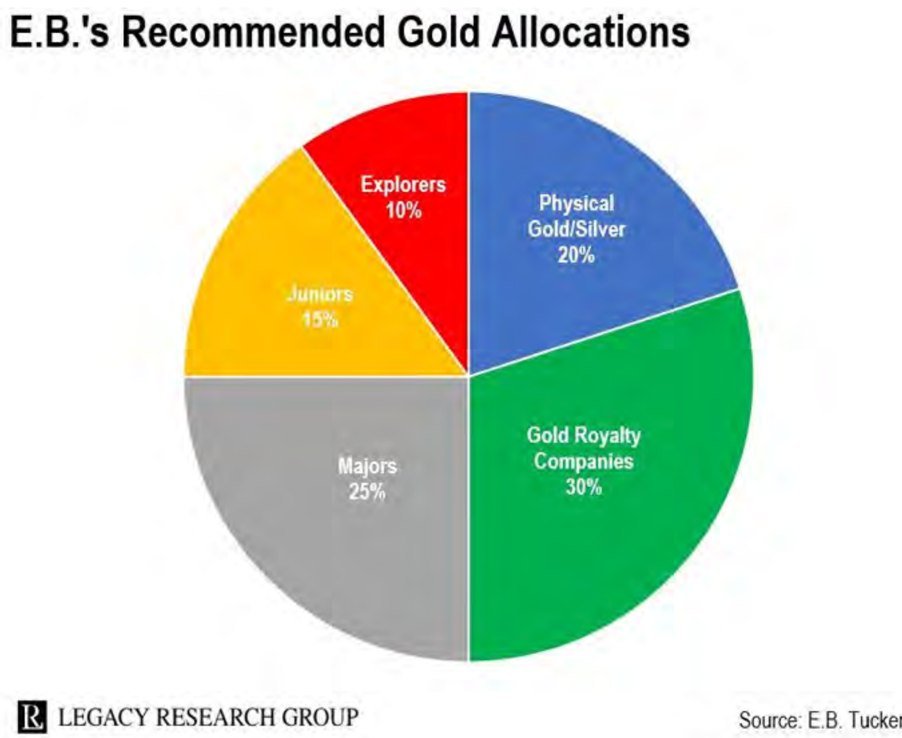
That's what you need to grasp about investing in royalty companies. They give you the benefit of diversification because they own "slices" of production across multiple mines. The bigger the royalty company, and the more diversified its portfolio of royalties, the safer the bet.

Chris: Let's say there's someone reading this who has yet to buy any gold. How should they get started with building a gold portfolio from scratch?

E.B.: First off, you'd never want all of your portfolio to be in gold. We're talking here about a part of your overall portfolio mix.

But let's say you have a chunk of money you want to put into the gold market. I would have 20% of that in the physical metal – a mix of bars and coins. I'd have another 30% in gold royalty stocks. That half of your gold portfolio is your disaster insurance.

Once you have that, I'd take the other half and put 25% into the best-of-breed gold mining majors... 15% into the most promising juniors... and 10% into the most promising explorers.



Chris: I'm a little surprised that you'd put 10% in explorers. That may seem like a lot for some folks, given how speculative these are.

E.B.: It's a great point. Most explorers won't find any gold. But you can make 10 times your money speculating on the right explorer. So putting 10% of your overall gold portfolio into these speculations is appropriate. All you need is one of them to succeed... and you turn 1% into 10%.

Chris: Before we wrap up, I know a lot of readers are going to want to know where silver fits into all of this. Should silver be part of your ideal precious metals portfolio?

E.B.: Silver is hard to store. It's less dense than gold. So $1,000 worth of physical silver takes up a lot more space than $1,000 worth of physical gold.

More important, silver acts like gold's crazy stepchild. It can move as much as three times as fast as gold, percentage-wise – in both directions. After its last bull-market peak in September 2011, for example, gold dropped from $1,900 down to $1,060 an ounce in November 2015 – a 44% loss. Silver plunged all the way from $50 in April 2011 to about $12 in January 2016 – a 76% plunge.

With silver, you have to buckle up. I'd recommend your readers hold a bigger percentage of gold than silver when it comes to physical metals. For example, 15% gold and 5% silver would work. But I wouldn't go much higher than that with silver.

Chris: Before you go, I know you you've just launched your new service, *Strategic Trader*, this week. Can you tell us a little bit about that?

E.B.: I believe 2019 is going to be a very volatile year. The thing is, I've made some of my biggest gains during times of high volatility.

In *Strategic Trader*, we're set up to capitalize on this volatility through elite trading strategies that I've used throughout my career. Right now is not just a good time to use it, it's a perfect time.

We have a five-part proprietary system that helps us pinpoint 1,000%-plus winners… with the least amount of risk and upfront cash. Our strategies are a way to make big money… without betting the farm.

Massive upside, capped downside. That's our mantra. And we think the next few months here could present some major money-making opportunities.

What to Do

Chris here – That wraps up the second part of our deep-dive conversation with E.B. about gold.

If you haven't already, make sure and catch the first part here. You'll hear more from E.B. on why he sees gold prices headed to $1,500 by the end of the year.

Once you're fully caught up… it's time to take action.

The first step, as E.B. says, is to buy physical gold.

How much depends on your personal preference. But here at Legacy, we recommend you have between 5% and 10% of your overall wealth in gold and gold-related assets.

And E.B. recommends 20% of that is in bars or coins. So, if you have 10% of your portfolio in gold… and 20% of your gold allocation in the physical metal… that's 2% of your overall portfolio in physical gold.

For more on how to buy gold, make sure and check out the *Gold Investor's Guide* here.

Regards,

Chris Lowe

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