

## Letter

### Gold shares versus krugerrands

In a recent article Affleck-Graves & Barr (*S.Afr.J.Bus.Mgmt.* 1986, 17:49-55) have demonstrated that over the past few years, Krugerrands have produced sub-optimal returns, in comparison with gold shares, for the South African investor.

A mild argument arose between the authors and Addleson (*S.Afr.J.Bus.Mgmt.*, 1986, 17:117) who argued that *ex-post* analysis cannot form the basis for *ex ante* forecasts and planning. Whilst this is a legitimate argument, known as Hume's logical problem of induction — that is whether we are entitled to infer unobserved cases from observed cases, however many — I would like to draw attention to another pernicious problem. Krugerrands, as all forms of physical gold, provide insurance against a risk which is not captured by the traditional risk surrogate, the variability associated with the return from the investment.

Gold coins and bullion are desired not only for their expected returns but also for their characteristics. Physical gold is an internationally recognized form of 'money', is easily transferable, and is anonymous. During troubled times, (i.e. war, revolution, etc.),

people like to hang over tangible, easily transferable and exchangeable assets and they are not very interested in the return of their investment. Thousands of Europeans saved their lives exchanging gold coins, (mainly British Sovereigns) for food or for a crossing to another country during World War II.

Obviously, Krugerrands provide an insurance which is not available through ownership of gold shares. In addition, tangible gold has an aesthetic value not available in gold shares and the two assets are different in the degree of tax protection that they provide to their owners. Using the variability of returns as a risk surrogate, is a useful exercise only under the restrictive assumption that investors are interested only for stable and high returns.

It seems that it is premature to suggest that investors will or should modify their behaviour on the basis of Affleck-Graves' & Barr's study, even if similar studies over longer periods provided evidence that returns of gold shares out-perform that of Krugerrands. The development of a multidimensional risk surrogate, able to incorporate a variety of risks, is in need and would be a contribution to knowledge in the area of portfolio selection of assets with different characteristics.

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