

Equities

Mine Mutual Funds For Gold Plays

Melinda Peer, 10.23.09, 10:40 AM ET

Gold price forecasts vary as wildly as the ways that investors are advised to play the popular inflation hedge--which is why gold-oriented mutual funds are appealing to investors looking to take a more active approach than is possible with an exchange-traded fund. Even within all the gold-focused mutual funds, however, different strategies abound, making it essential that investors do their homework.

Diverging price expectations aside, most analysts consider gold's long-term outlook robust but see a near-term pullback for the precious metal. S&P Equity Research analysts have a positive fundamental outlook on gold and gold-mining stocks for the next 12 months.

"Based on our expectation for increased production and a further rise in the gold price for 2010, we look for another increase in sales and earnings for this group," said S&P analyst Leo Larkin.

Mutual funds can take a lot of the headache out of investing in mining stocks (for a fee), which are favored over physical gold by investors bullish on gold prices because mining stocks offer operating leverage. (See "[Gold Spikes, Miners Go Higher](#).") In addition to gold prices, gold equities are also impacted by management-related factors, earnings performance, geopolitical risks, production costs and exploration projects, among other variables.

With so many factors at play, it's especially important and investors learn as much as they can about a fund's strategy and how it's positioned vs. its peers, according to S&P equity analyst Todd Rosenbluth.

The Midas Fund, for example, hunts for mining stocks with strong growth potential.

"It isn't really a gold bug fund--we're capital appreciation bugs," said portfolio manager Tom Winmill. "We're most interested in growth and appreciation--we just happen to do it in gold mining."

The fund's top three holdings include Eldorado Gold, Compania de Minas Buenaventura and Kinross Gold. While the fund boasts a year-to-date return of 71.4%, it only gets two stars of a possible five from the S&P's MarketScope Advisor mutual fund rankings.

"It's not stacking up against other funds," Rosenbluth said. "Although it's been an above-average performer in the past year, in the past three years, its performance has been below average: down 2.5% while the peer average is up 11%. Plus, it's more expensive than the average fund with a net expense ratio of 2.4% while the peer average is 1.5%."

S&P mutual fund rankings use past performance as a starting point to gauge how funds stack up against their peers. The ranking system also examines the funds' cost factors and underlying securities using S&P equity and credit research.

Rosenbluth said Midas holds some securities that S&P sees as having above-average risk and several securities for which S&P lacks analysis, making it difficult to rank. That likely stems from the fund's consideration of lesser-known companies with strong growth profiles--a riskier bet, judging from its past performance against other gold-oriented funds.

MarketScope gives Franklin Gold & Precious Metals a top five-star rating because it has been in the top quartile on a three-year basis--up 15%--and has an expense ratio of only 0.9%.