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Alternative Answers

By GREGORY ZUCKERMAN

In this column, we answer your questions about alternative investments. Send them to reports@wsj.com.

Q: How would an investor buy Canadian government bonds?

Dan Hogan
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A: Rates on U.S. Treasury bonds are so low that some investors are looking for alternatives. U.S. corporate bonds sport higher yields, but they have dropped dramatically in the last six months and now aren't yielding much more than Treasurys. Junk bonds still have higher yields, but are riskier. At the same time, the U.S. dollar continues to fall, sparking interest in investments in stronger currencies, such as the Canadian dollar, which has benefited from the rise in energy prices and other commodities found in Canada.

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Investors can purchase Canadian bonds, as well as those of some other nations, from many larger brokerage firms, says Steven Stahler, who helps run The Stahler Group, an investment advisory firm based in Baton Rouge, La. He recommends 10-year Canadian government bonds that mature in June 2019 and yield nearly 4%, above the 3.2% yield of comparable U.S. Treasurys.

Some exchange-traded funds also track the returns of Canadian bonds. The iShares CDN DEX Short Term Bond Index Fund, for example, seeks to replicate the performance of five-year bonds issued by the government of Canada, and has a yield of about 4%. This ETF has gained about 7% in the past year.

"The downside is the minimum investments [for individual Canadian bonds] can be quite high for smaller, safety conscious investors," says Mr. Stahler. Usually the minimums are $50,000 to $100,000, he says, much higher than those of ETFs.

There are various risks to playing the foreign bond market, especially today, says Mr. Stahler. If the U.S. dollar rebounds, then gains in Canadian bonds will be cut when they are converted back into U.S. dollars. And interest rates in both markets are low, so any move higher will hurt the value of the bonds, as investors shift to new, higher-yielding bonds.

Q: What is the best way to invest in gold?

A: Gold prices are surging as major currencies drop in value. But determining the best investment option can be confusing.

Exchange-traded funds, such as SPDR Gold Trust (GLD), and those focused on mining companies, such as Market Vectors Gold Miners ETF (GDX), have great appeal to small investors because they allow daily trading, have low minimum investments and charge low fees. The Gold Miners ETF, which tracks the stock performance of gold miners, is up 50% this year, while the Gold Trust ETF, which roughly tracks the price of gold and represents gold bullion, has gained more than 30%.

Investors in bullion-backed ETFs like Gold Trust are considered to have an ownership stake in physical gold, which is a collectible item, says Paul Ahern, senior vice president at WealthTrust-Arizona. If an investor holds the ETF for more than a year before selling, the same minimum tax rate of 28% that is used for collectibles will be applied. If an investor sells the position prior to one year, then ordinary income-tax rates apply. An ETF that holds gold-mining stocks is taxed at the 15% maximum long-term capital-gains rate if held for more than a year. Mr. Ahern recommends investing in Gold Trust in a self-directed IRA, if possible.

Precious metals-focused mutual funds also have small minimum investments but have varied returns. The Tocqueville Gold Fund (TGLDX), for example, is up about 90% this year, though it charges an annual management fee of almost 1.5%, while Fidelity Advisor Gold A (FGDAX), is up about 47% and charges a 1.2% management fee.

One way to avoid the costs levied by ETFs and mutual funds is to buy gold bars. But storing gold safely can be costly, so this may be a good move only for investors who already have somewhere safe to keep it.

Buying gold coins is another option for individual investors. At American Precious Metals Exchange in Edmond, Okla., gold coin and bar sales more than tripled from Jan. 1 through Oct.

31 from the same period a year ago. Coins, however, usually cost a bit more than their gold and silver content because of the expense of producing and distributing them.

Some investors, such as hedge-fund manager John Paulson, have been buying up gold miners such as AngloGold Ashanti Ltd. Miners generally do better than gold prices when gold rises, and worse when gold falls, giving them more upside but also more risk.

Mr. Ahern says new investors are buying gold near all-time high prices, "so we would urge caution and suggest investors employ a stop/loss order," or a stock order that places a level at which the stock would be sold, to avoid suffering big losses if gold tumbles.

Purchasers of gold '"call" options pay a premium for the right to buy gold at a specific price at a future date. A seller of a gold option, or the purchaser of a gold "put" option, wagers that gold prices will fall. Some say buying inexpensive "out of money" options, or those on gold at much higher prices, is the best way to capture potential upside for gold without risking too much money.

Joe Quinlan, chief market strategist at U.S. Trust, Bank of America Private Wealth Management, advises investors holding big gold-related investments to write long-dated covered calls against gold ETFs, or to sell calls that expire at least a year in the future. That step can help protect a portfolio from any sharp move down in gold prices.

— Mr. Zuckerman is a special writer in The Wall Street Journal's New York bureau and is the author of "The Greatest Trade Ever: The Behind-The-Scenes Story of How John Paulson Defied Wall Street and Made Financial History." He can be reached at gregory.zuckerman@wsj.com.