Research: Gold as an inflation hedge in a time-varying framework

Although physical gold ownership is widely regarded as a ‘safe haven’ and inflation hedge today, empirical research on the hedging properties of gold led to ambiguous results and provided evidence for instabilities in the relationship between gold prices and inflation; while long-run analysis supports the hypothesis of gold being an inflation hedge, there is not necessarily a linear relationship in the short run.

A new study published by Joscha Beckmann and Robert Czudaj specifies the non-linear dynamics more precisely and provides a measure of the usefulness of gold as an inflation hedge over different time periods and for four major countries, namely the U.S. the U.K., the Euro zone and Japan.

Methodology

The authors use a monthly dataset including the price for gold denominated in U.S. Dollar, British Pound Sterling, Euro and Japanese Yen as well as the consumer price index and the producer price index of the USA, the UK, the Euro Area, and Japan. The gold price data has been provided by the World Gold Council and covers a sample period from December 1969 to December 2011.

Results

The study finds that

★ Gold is partially able to hedge future inflation in the long-run.
★ This ability tends to be stronger for consumer prices in general as well as for the USA and the UK compared to Japan and the Euro Area.
★ The adjustment of the general price level seems to depend on whether or not the economy is in “normal times” or times of turmoil.

These results are of significant importance from the investor’s point of view; the authors note that “...the effectiveness of gold as an inflation hedge crucially depends on the time horizon. Over the very long-run, gold is useful as a partial hedge since a cointegrating relationship prevails.

However, during some periods where no price adjustment is observed, gold is not able to shield a portfolio. This may be illustrated by a simple example of an investor who buys gold at the beginning of a period with no adjustment and sells at the end of the corresponding period. ”

The paper can be downloaded here: Source
Gold

Fund Profile – True Hedge Strategic Gold Fund

U.S.-based True Hedge LLC is in the process of launching a multi-strategy gold investment fund. The fund's manager Don Scammell (formerly Scammell Partners) explains why investors should consider gold now and explains the fund's strategy.

The case for gold as a foundational asset in the portfolio

Scammell expects global markets to be in a state of significant change resulting in challenges for investors: Global monetary expansion, a diminishing amount of "risk free" assets, an increasing frequency of financial and social stress events and inflection points being reached in major asset cycles will expose investors to higher volatility, more tail risk, below-average returns in major asset classes and inflationary value destruction.

Since empirical analysis shows that gold performed well specifically in turbulent times, a dedicated portfolio may help investors to overcome those difficulties. The idea of the True Hedge Strategic Gold Fund is to provide an effective hedge against portfolio volatility, tail risk, and inflation without sacrificing returns.

Investment strategy

The fund will invest in a mix of three types of gold assets and strategies:

- **Gold bullion** as a store of value.
  
  The assets will be stored at the safest, most reputable vaults outside of the United States and will be fully allocated and insured by Lloyd's of London.

- **Gold futures** to enhance returns.
  
  The gold futures component of the fund will be managed by the general partner using a proprietary strategy that employs a daily position reversal that pivots around the two daily fix determinations by the fix consortium and attempts to benefit from the divergence of market impact between the commercial/speculator market participants and the physical/investor participants.

- **Gold equities** to enhance returns.
  
  A focused buy and hold portfolio of particular companies in the mining and precious metals sectors that have proven to possess the best business models, most proven management teams, and the highest returns in the mining complex.

The fund’s portfolio will consist of 50% gold bullion, 30% gold futures and 20% gold equities and close at $200 million AuM due to possible liquidity constraints with the futures strategy.
Fund terms

<table>
<thead>
<tr>
<th>Manager/General Partner</th>
<th>True Hedge, LLC</th>
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</thead>
<tbody>
<tr>
<td>Inception date</td>
<td>TBA</td>
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<tr>
<td>Management fee</td>
<td>2%</td>
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<tr>
<td>Performance fee</td>
<td>50% of gross returns above gold</td>
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<tr>
<td>Lock-up</td>
<td>12 months from contribution of initial investment</td>
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<tr>
<td>Redemption frequency</td>
<td>Semi-annually, January 1st and July 1st</td>
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<tr>
<td>Minimum investment</td>
<td>$500,000 (US$)</td>
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