Link to Article

How gold is getting its sheen back

Gold is far more precious than what the majority of us may believe, at least as an investment tool if not as a currency. And the day isn't far when it will be back as the underlying value of currency, according to Ned Naylor-Leyland, a Fund manager at Old Mutual Global Investors.

NED NAYLOR-LEYLAND
Old Mutual Global Investors

AND THAT DEVELOPMENT WILL BE DIRECTLY LINKED to the trend of balance sheet expansion at central banks across the world. Before explaining the link between central banks' inflated balance sheet and the value of gold, Naylor-Leyland had this advice to offer: hold your gold in as close to physical form as possible and at the very least in 'paper' form.

That's because physical gold doesn't carry any financial obligation unlike a bank deposit or a U.S. treasury bond, which is simultaneously someone's asset and someone else's obligation. That's why central banks hold gold as fully allocated bars in physical form as it carries no obligation - it's just asset money.

The G20 Central Banks have 18.2 percent of their own reserves in gold bars and central banks have been buying gold and selling U.S. treasury bonds, according to the gold fund expert.

Physical gold

Bridgewater Associates Founder Ray Dalio says "...most people should have roughly 10% of their assets in gold, not only as a good, long-term investment, but also for its effectiveness in diversifying the other 90% of assets people hold."

Naylor-Leyland at OMGI considers his fund to be the closest to obligation-free forms of gold. It blends the physical metal with the equities and uses silver as well.

People who seek to counter this view on gold would cite the growth in equities, he notes and points to the trend of big institution money like sovereign wealth funds, selling fixed interest and buying equities. Central Banks and sovereign wealth funds selling down cash and

bond positions and holding equities instead, has been hugely supportive of equity markets globally and resulted in the rally. Any investor who agrees that analysing the balance sheet of a company is key to making a sound investment decision will also agree that the 900 percent expansion in the balance sheet of central banks is something that requires analysis too, Naylor-Leyland says to drive home his point.

Skyrocketing equities

It's wrong to ignore the ballooning balance sheet of central banks or to pretend it doesn't matter. Naylor-Leyland notes that this lies at the heart of the neo Keynesian economic model which they sell to you as being fact and of course you know well it's not, it's a theoretical construct which supports everything that you own. It doesn't make it right, it's just what you agree to it being the case. And gold is your hedge against all of this. Even better, if you manage it properly and hold it in sufficient quantity it can also be a huge money-making opportunity.

That view finds echo in a note written by Deutsche Bank's Michael Hsueh and Grant Sporre last year, where they say there is more value in gold when viewed against the aggregated balance sheet of the 'big four' global central banks -- the Fed, ECB, BoJ and PBoC.

The balance sheet of the Fed, ECB and BoJ alone touched $4.5 trillion in April this year, according to a separate Bloomberg News report. The Fed's balance sheet in 2008 was just $0.9 trillion.

Gold standard

DB's Hsueh and Sporre wrote: "Over the same period [2005 till Aug. 2016] as the aggregate central bank balance sheet expanded by 300%, global above ground stocks grew by 19% in tonnage terms or c.200% in value terms. If we were to assume that the value of gold should appreciate to keep the overall value of the big four aggregate balance sheet equivalent to that of the value of the above ground gold stocks, then gold should be trading closer to USD 1,700/oz."

Gold rose 0.4 percent on Saturday, December 2 to USD 1,282.30 per ounce. The precious metal is up 9.7 percent this year, according to data from spot market.

And as regards the huge pile of debt from government to state to corporate, Naylor-Leyland calls them the 'Fiat' debt, which he anticipates will never be repaid and predicts a new monetary system within five years that involves gold.

Crypto and Bitcoin are rebooting the conversation of what money is and how payments work. When the paper conflagration occurs, which is what the Central Bank balance sheets data points to, then the gold price will behave like Bitcoin is now. Naylor-Leyland sees Bitcoin as paving the road for gold to re-enter the monetary system in a formal way, because of course gold's only issue has been its divisibility and its portability, people's ability to use it, and the digitalisation of currency is assisting to resolve some of these challenges.

According to the Naylor-Leyland, the Iranians, Russians, and Qataris are already settling oil and gas transactions in Shanghai in gold, without involving dollars by selling oil and gas in RMB and converting it into gold that's held in bonded warehouses in Shanghai in the free trade zone. All that indicates to going back to the pre-1971 arrangement, when the dollar was used to capture gold's price.

"It's all right there in front of you, you just have to recognise what's going on." ■