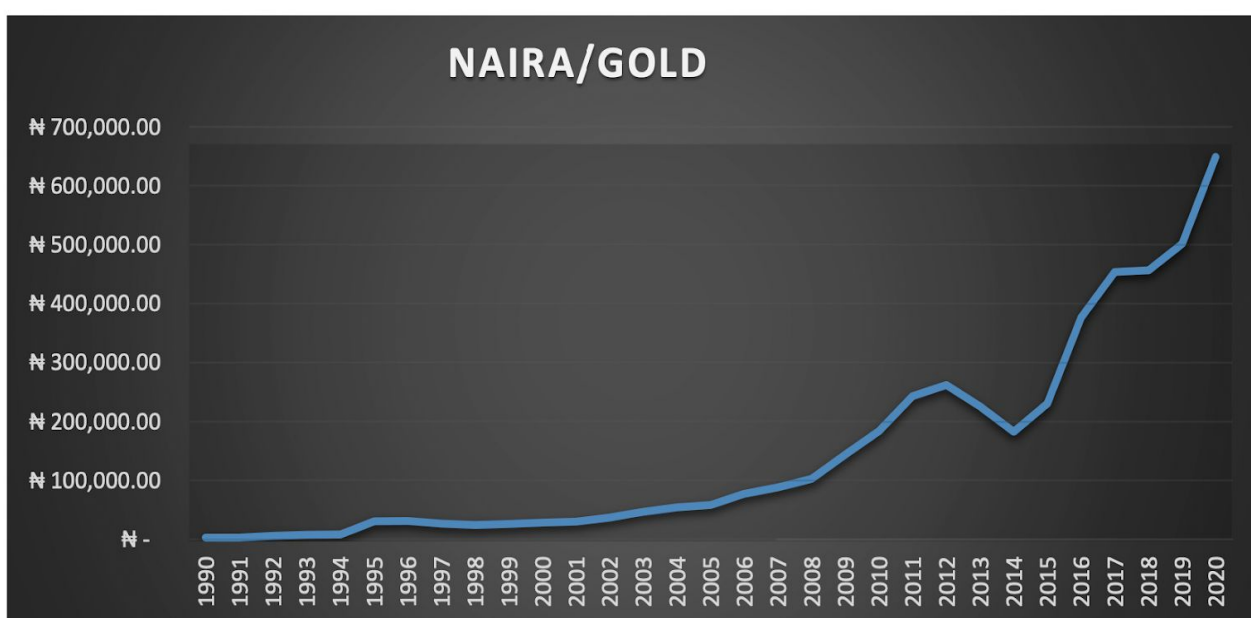




Arguments for Gold

The short answer to whether gold is a viable hedge against naira devaluation is: Yes. In fact, at the time of this writing, gold has averaged a **38% return** on the naira every year for the last 30 years.



There are few reasons to believe that gold should perform better than its average return over the next 3 years. It is more likely than not that we are at an inflection point and gold is likely to outperform its historic average over the next few years. The central purpose of this short paper is to examine that likelihood.

Why Gold Is Likely To Remain A Viable Naira Hedge:

It is somewhat important to understand the practical role gold currently plays in the international monetary system. That role is primarily a bet against the current monetary system; a type of non-expiring put.

The cycle for the last 5 decades has been: when the monetary system is chugging

along according to plan and expectations, gold tends to float without meaningful price action. As the signs of exhaustion increase, some bullish attention is given to gold again. Then as liquidity dries up, gold does poorly in the short term as many investors sell their gold hedge for necessary currency liquidity. As governments provide system-wide liquidity, gold picks up again (almost as a bet against the uncertain monetary system), runs, finds its level, and settles.

If we zoom out, the price of gold acts like a put on the dollar reserve system, and as the odds of failure becomes higher or merely feels higher, the price of gold rises.

Naira?

As international liquidity dries up, and governments interfere to pump the flow, Emerging markets (EM) are typically last to the party. They suffer the dearth of hard currencies the most, and that quickly reflects on the strength of local EM currencies. For several reasons beyond the scope of this paper, Nigeria is in a horrible dollar situation and the naira is particularly vulnerable to decline at this time.