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March 22, 2023

CME Group

Gold for Stock and Bond Investors

Tariq Dennison

TEP, Wealth Manager
GFM Asset Management

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GFM
ASSET MANAGEMENT

Gold for stock and bond investors

Overlaying inflation protection with futures & options

by Tariq Dennison

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Image credit: MS Office Stock Photo

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About Tariq Dennison TEP

- Independent Advisor Managing Accounts on the IBKR platform
 - US Advisor: GFM Asset Management LLC
 - HK Advisor: GFM Group Limited
- In the market since 1998
 - Commerzbank (NY, London, Frankfurt)
 - Bear Stearns (NY)
 - J.P. Morgan (NY)
 - Canadian Imperial Bank of Commerce
 - Societe Generale (HK)
- Masters in Financial Engineering
 - University of California at Berkeley
- Lecturer at ESSEC Singapore
 - Fixed Income
 - Alternative Assets
- Focus on US-Asia corridor
- Author “Invest Outside the Box”



Gold Fundamentals

- Why gold has value
 - Supply types & geography
 - Demand types & geography
- Gold vs inflation
- The curve that pushes gold prices up and down
- Big idea: “Return stacking” aka “Overlay”

Examples

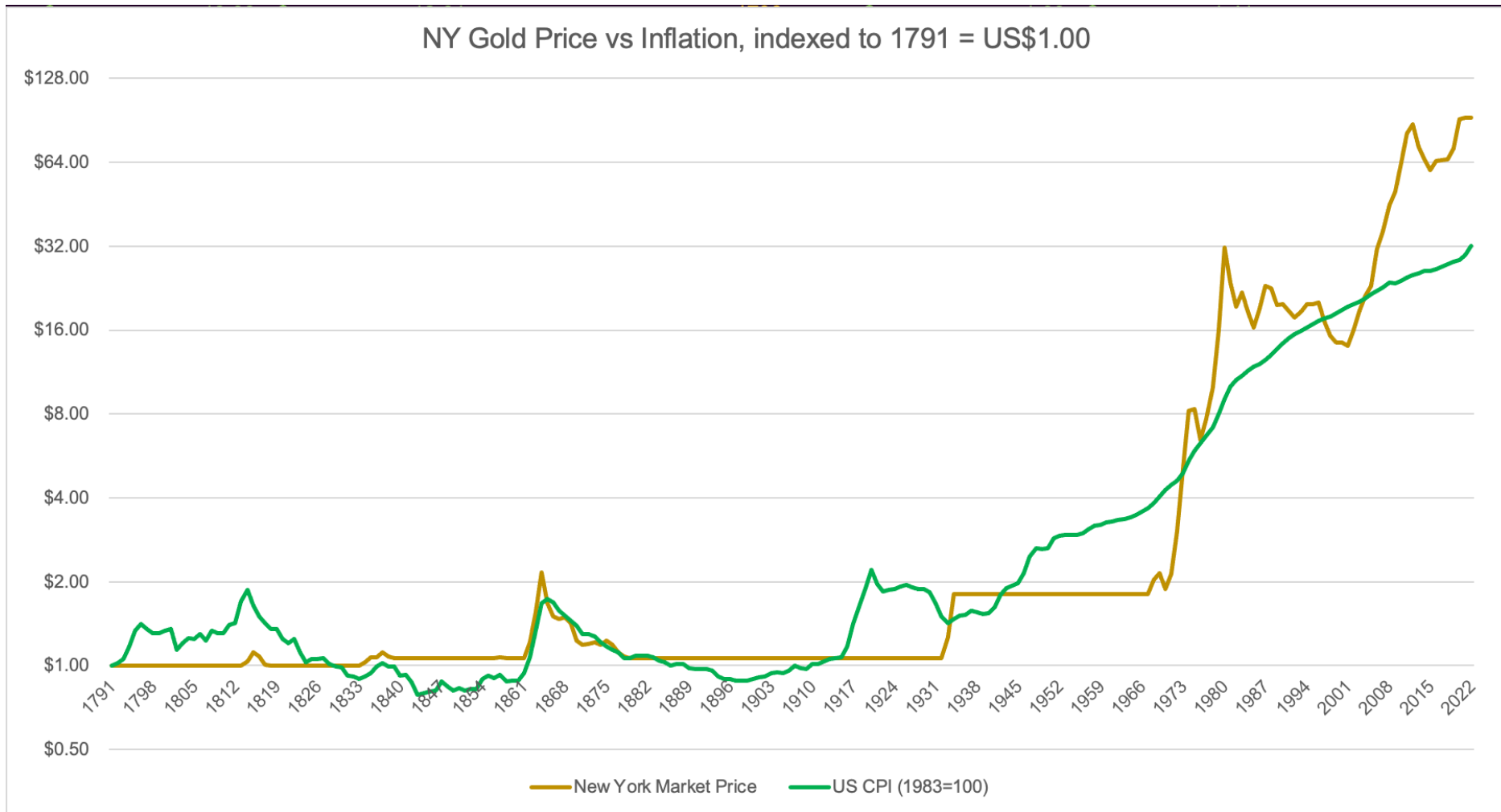
- Gold & Silver, for centuries
- Oil since 1901
 - *10 Jan 1901 = Spindletop in Texas*
- Spices, 1453-1947
 - *1453 = Fall of Constantinople*
 - *1947 = Indian Independence*
- Sugar, 1493-1806
 - *1493 = Columbus brings sugar cane*
 - *1806 = Britain blockades Napoleon, Europe switches to sugar beets*
- Expect more metals with the rise of EVs...

Gold

What is gold, and why consider buying it?

- Element 79, relatively chemically & industrially inert
- Costs to store it, without yield
- Compared with land / real estate, gold is:
 - Fungible: one ounce interchangeable with another
 - Portable: high value / transport cost ratio
 - Divisible: usable in coins and value accounting
- Limited and expensive **supply** makes it attractive as a relatively stable store of relative value, but **only if** buyers (**demand**) think it does!
- **Important to note:** Gold comes with risks and potential downsides, including as storage and security costs, lack of cash flow or dividends, and potential price volatility.

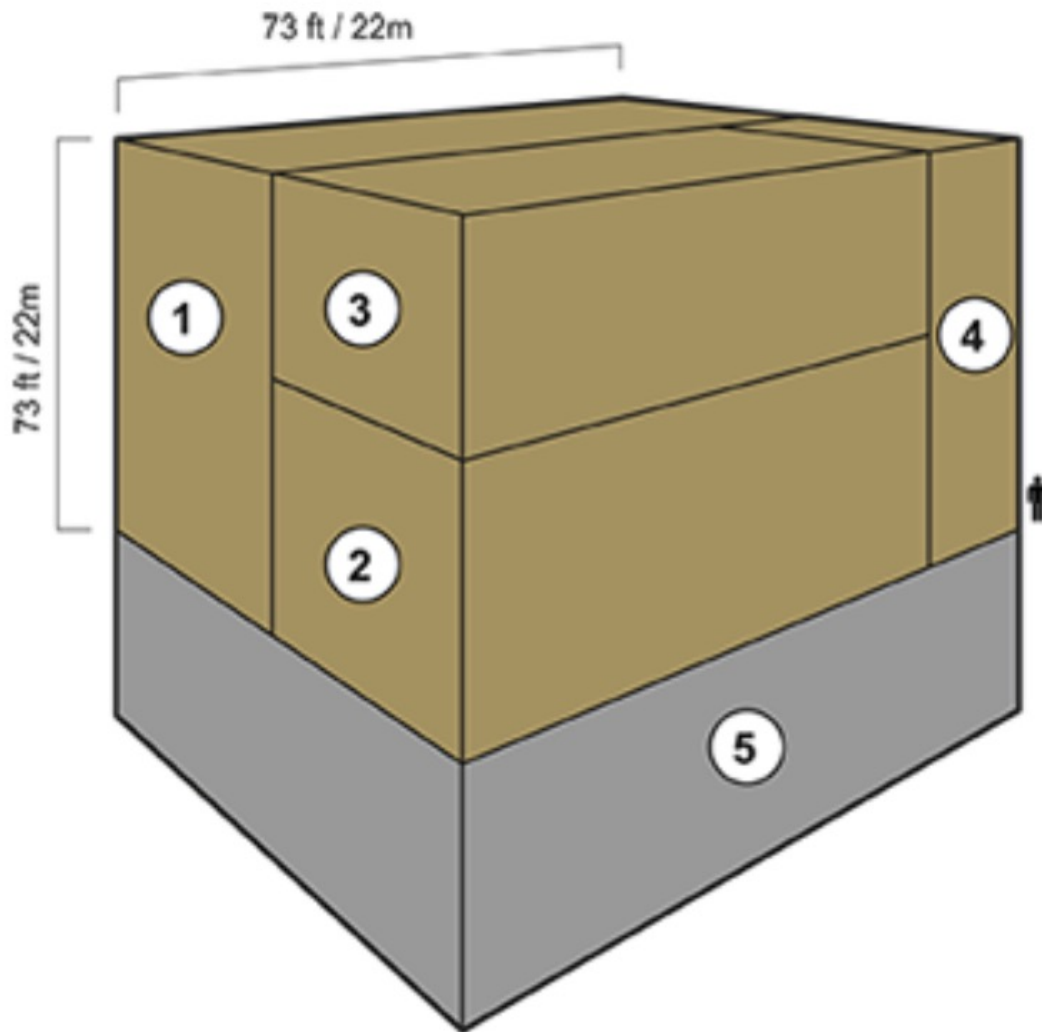
Gold vs US Inflation Since 1791



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Source: <https://www.measuringworth.com/datasets/gold/result.php>

Gold SUPPLY by sector, visualized

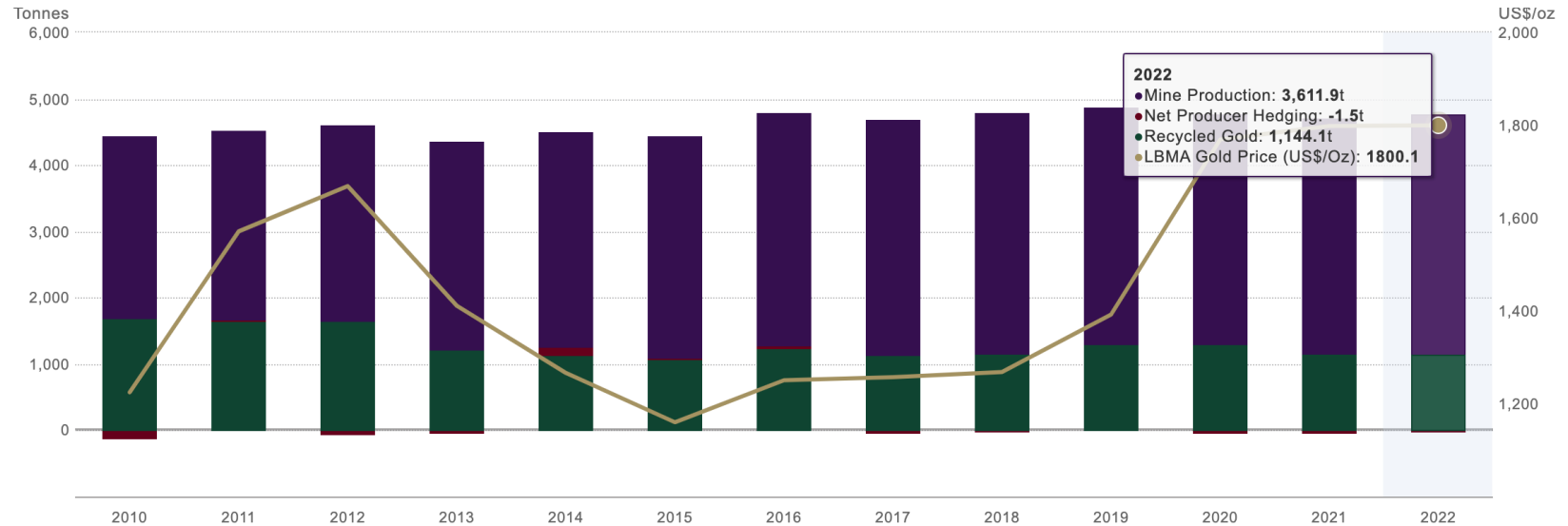
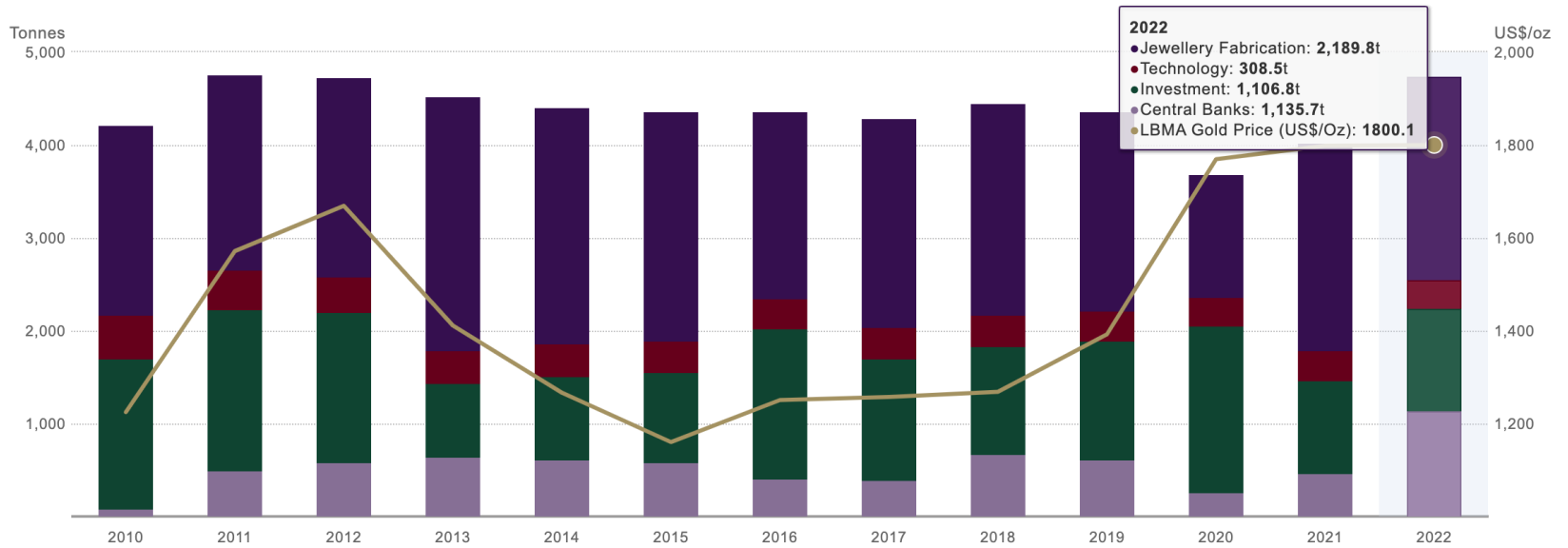


Total above-ground stocks (end-2022): 208,874 tonnes

1. Jewellery ~95,547t, 46%
2. Bars and coins (including gold backed ETFs) ~46,517t, 22%
3. Central banks ~35,715t, 17%
4. Other ~31,096t, 15%
5. Proven reserves ~52,000t

Source: <https://www.gold.org/about-gold/gold-supply/gold-mining/how-much-gold>

Mines ~75% of Supply, Jewellery ~50% of Demand



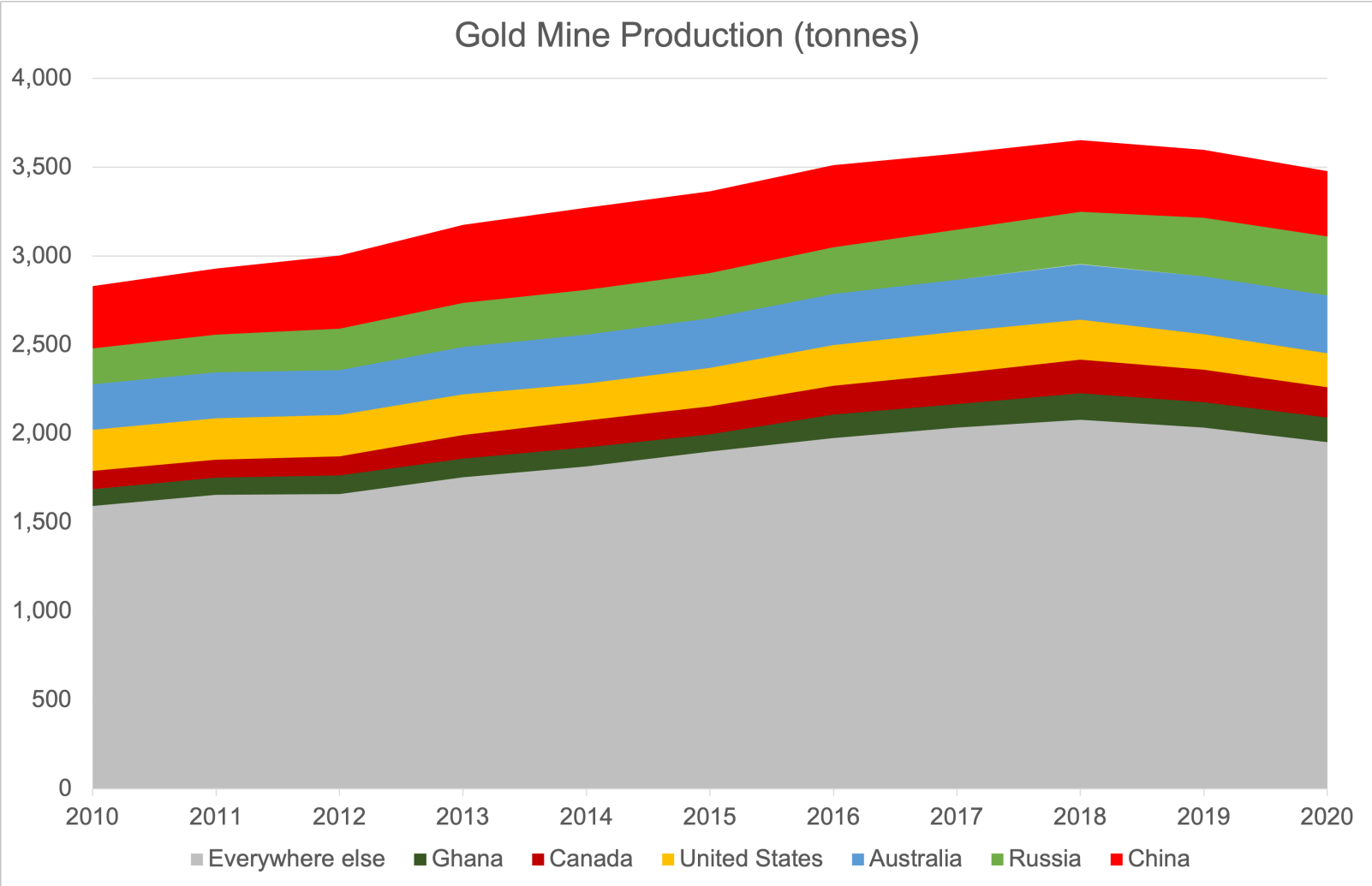
Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.



Source: <https://www.gold.org/goldhub/data/gold-demand-by-country>

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Where those gold mines are...

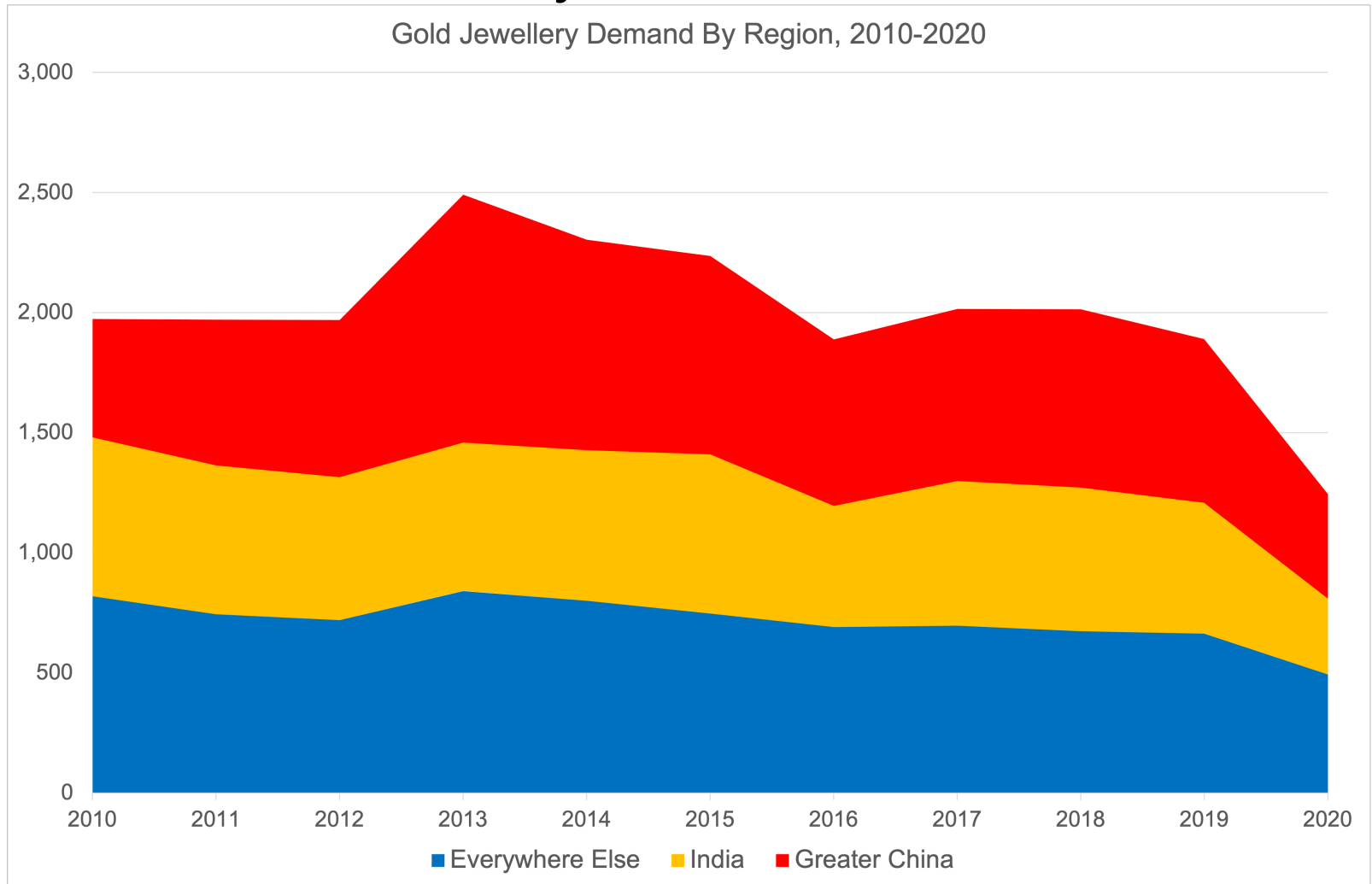


Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.

Source: <https://www.gold.org/goldhub/data/gold-production-by-country>



... versus where the buyers are



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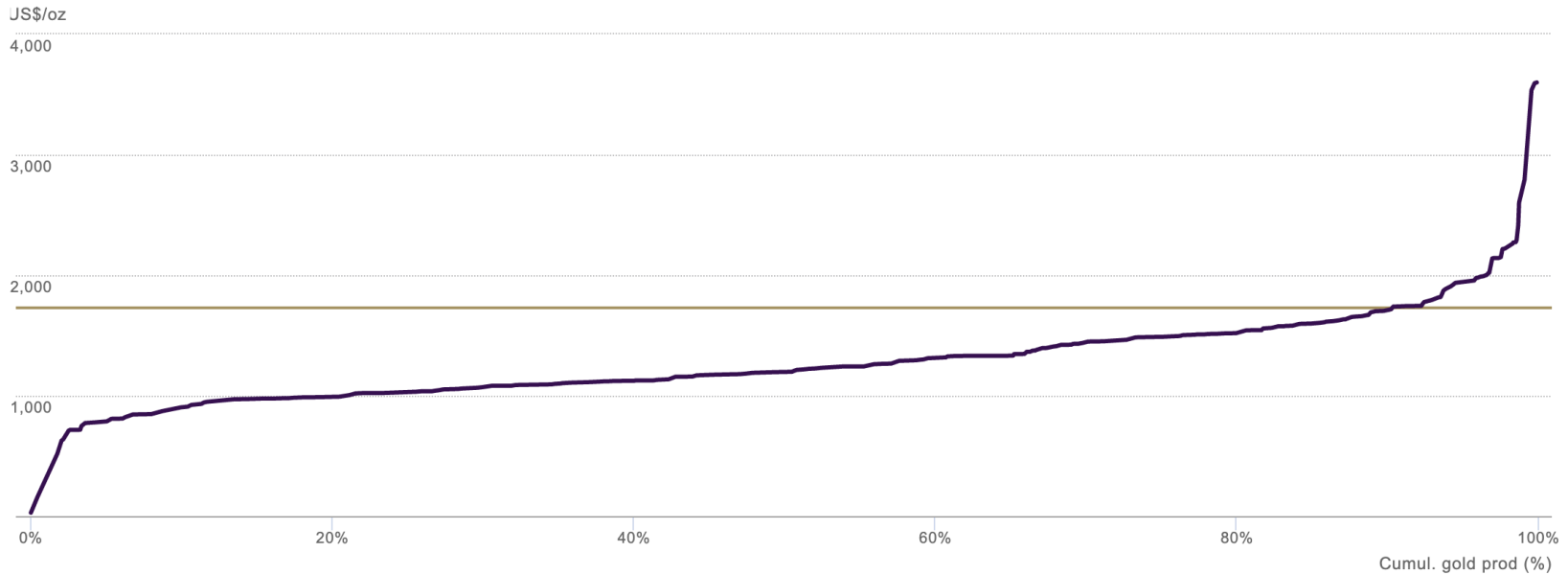
Source: <https://www.gold.org/goldhub/research/gold-demand-trends/gold-demand-trends-q3-2021>

The All-In Supply Cost (AISC) Curve

Visualizing the price impact of incremental supply and demand

Q3'22 AISC curve

PDF PNG



All-in Sustaining Cost (US\$/oz) Quarterly Avg Gold Price (US\$/oz)

Data as of 30 September, 2022

Sources: Metals Focus Gold Mine Cost Service; [Disclaimer](#)

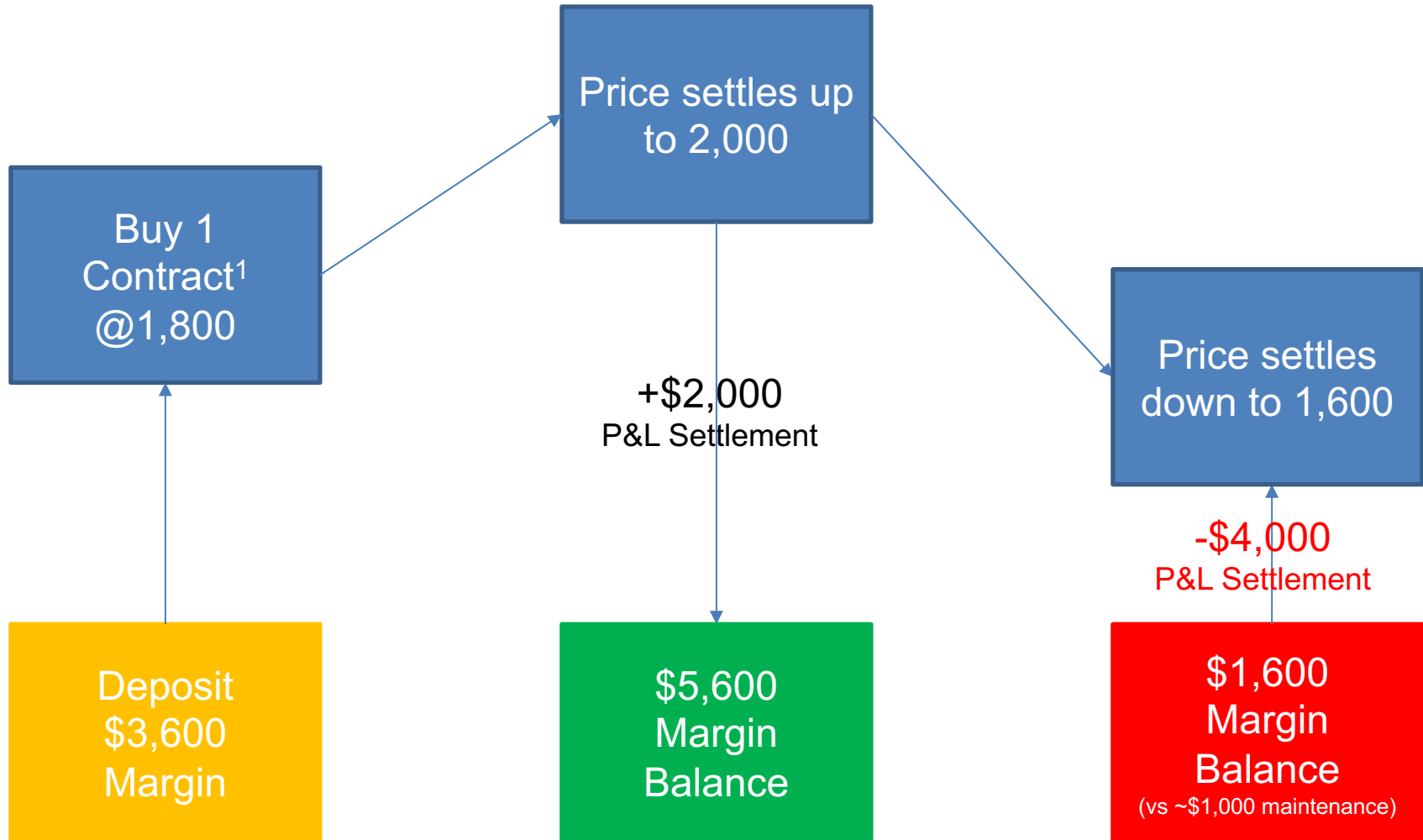
Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.

Source: <https://www.gold.org/goldhub/data/aisc-gold>



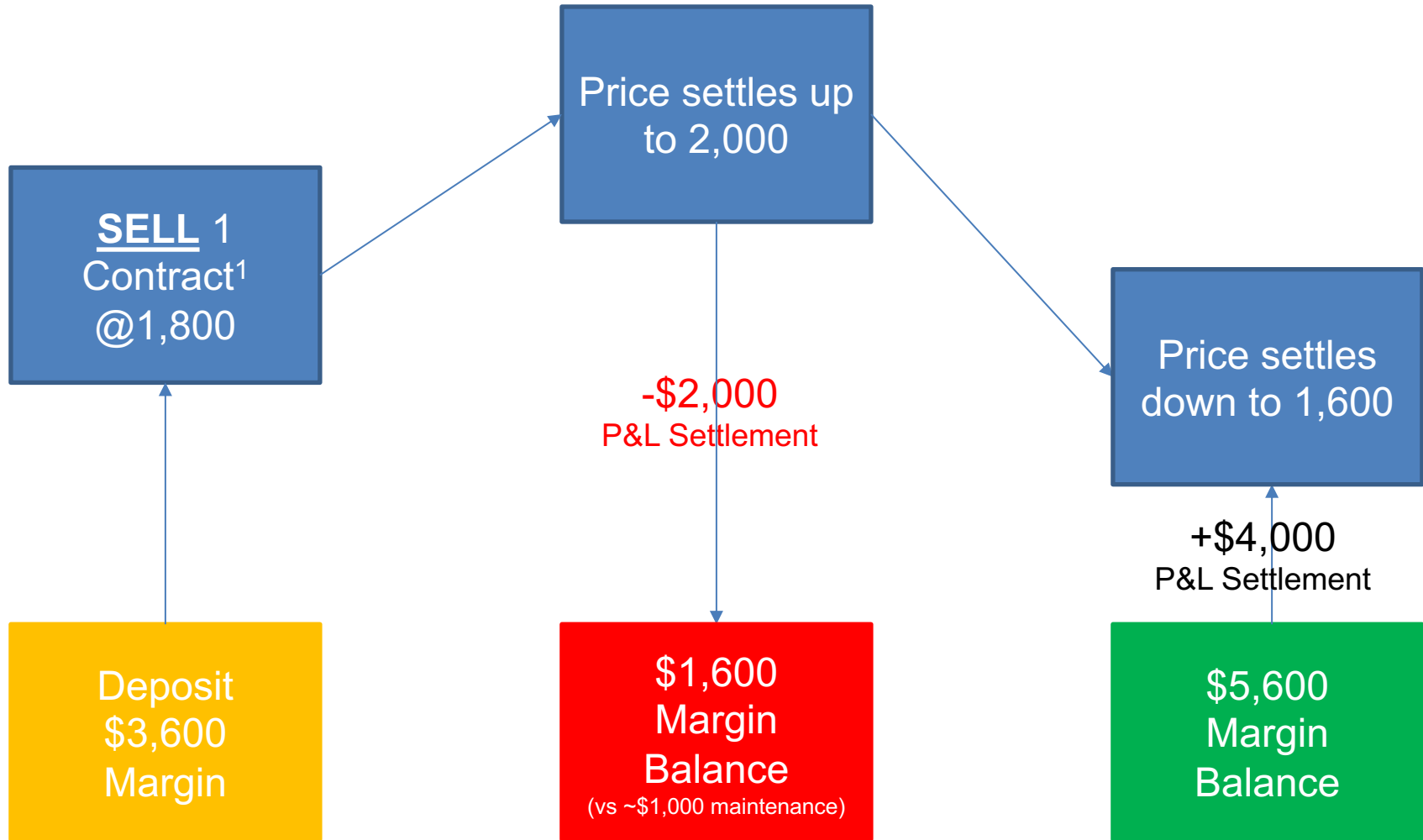
Big Concept:
“Stacking” or
“Overlaying” Gold
on top of your
stocks or bonds

Refresher: How Futures Work



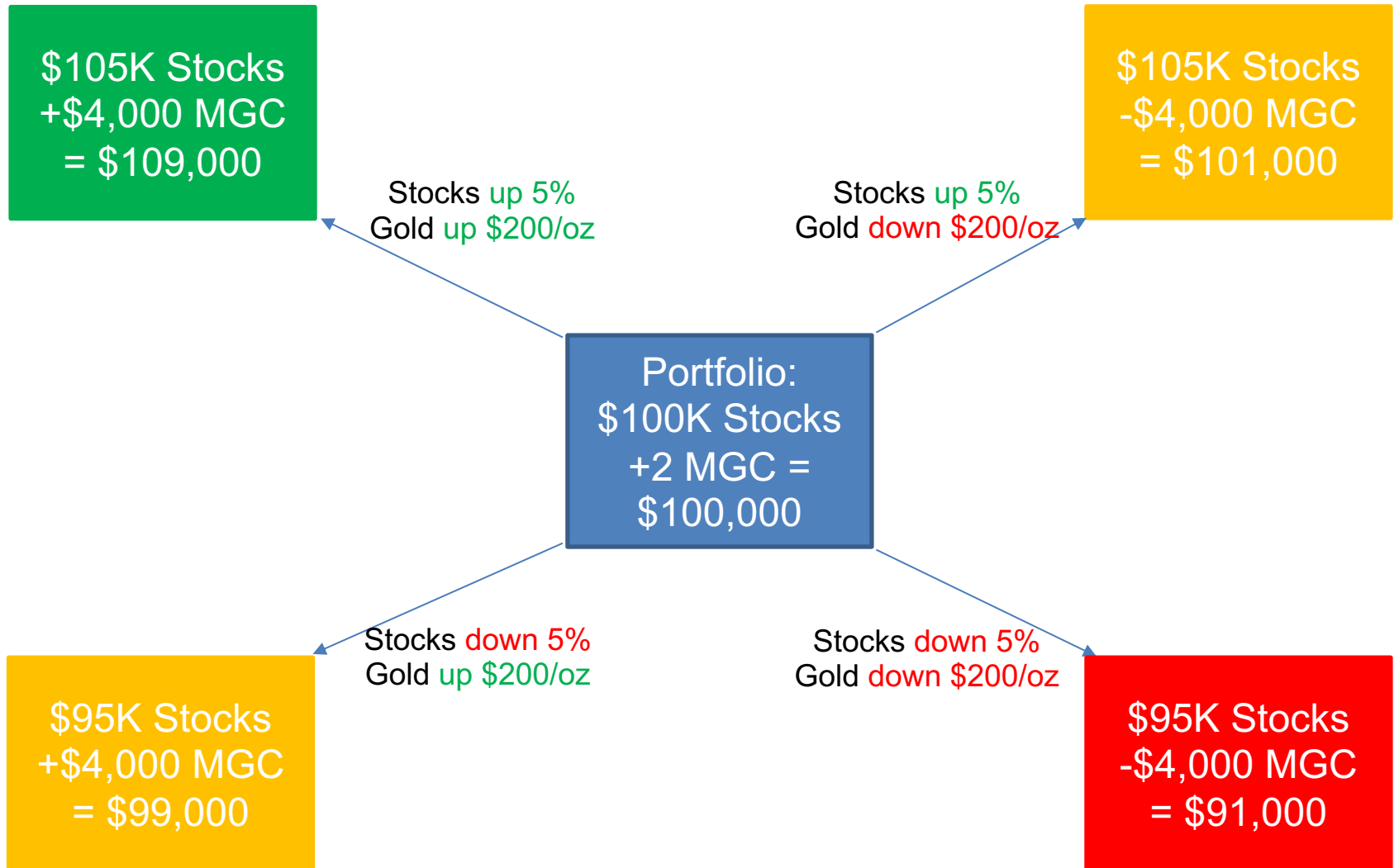
¹ Micro Gold Future, \$10 per point

Futures make selling short as easy as going long



¹ Micro Gold, \$10 per point

How “Return Stacking” Works



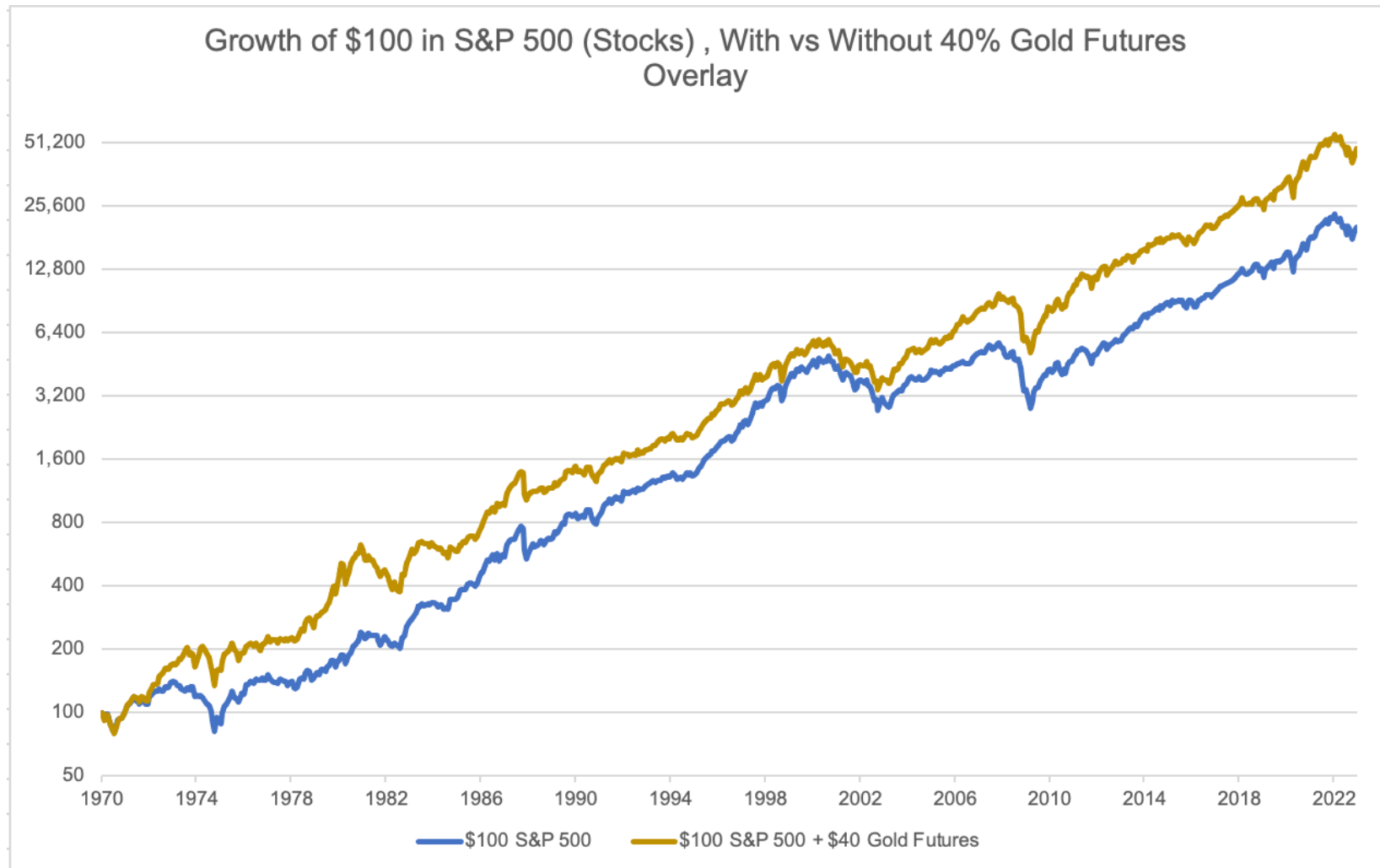
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Different ways of doing this “return stacking”

- Hold stocks and/or bonds, buy gold futures
- Hold stocks and/or bonds, sell puts on gold (see options section later)
- Hold gold ETF, buy stock index and/or bond futures
- Hold cash, buy all stock, bond, and gold exposure via futures
- Hold physical gold, deposit margin at IBKR to maintain stock and bond exposure via futures

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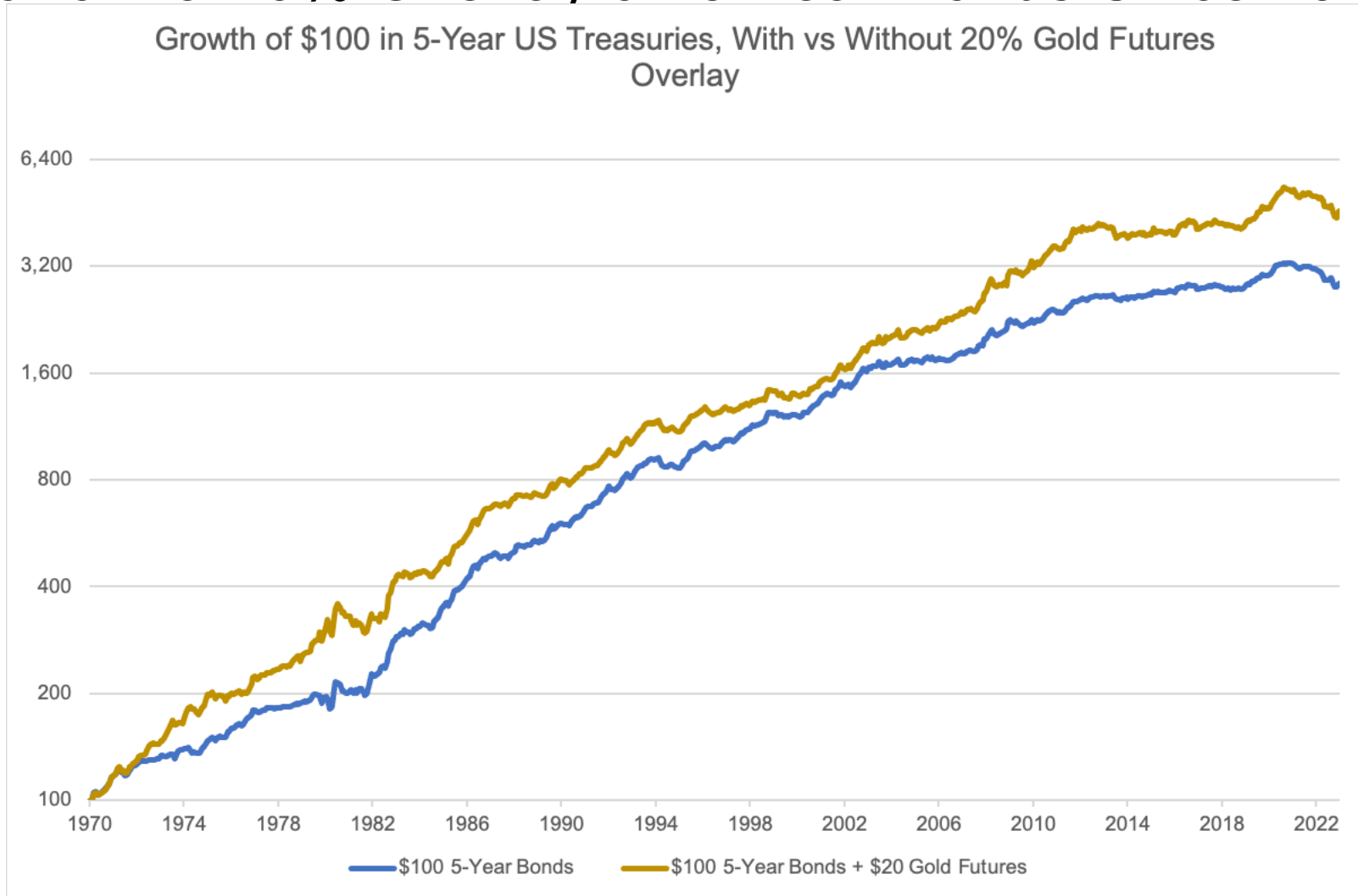
Pro-forma 40% Overlay on S&P 500 Since 1970



Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.

Source: Dimensional Fund Advisors, Author's Calculations

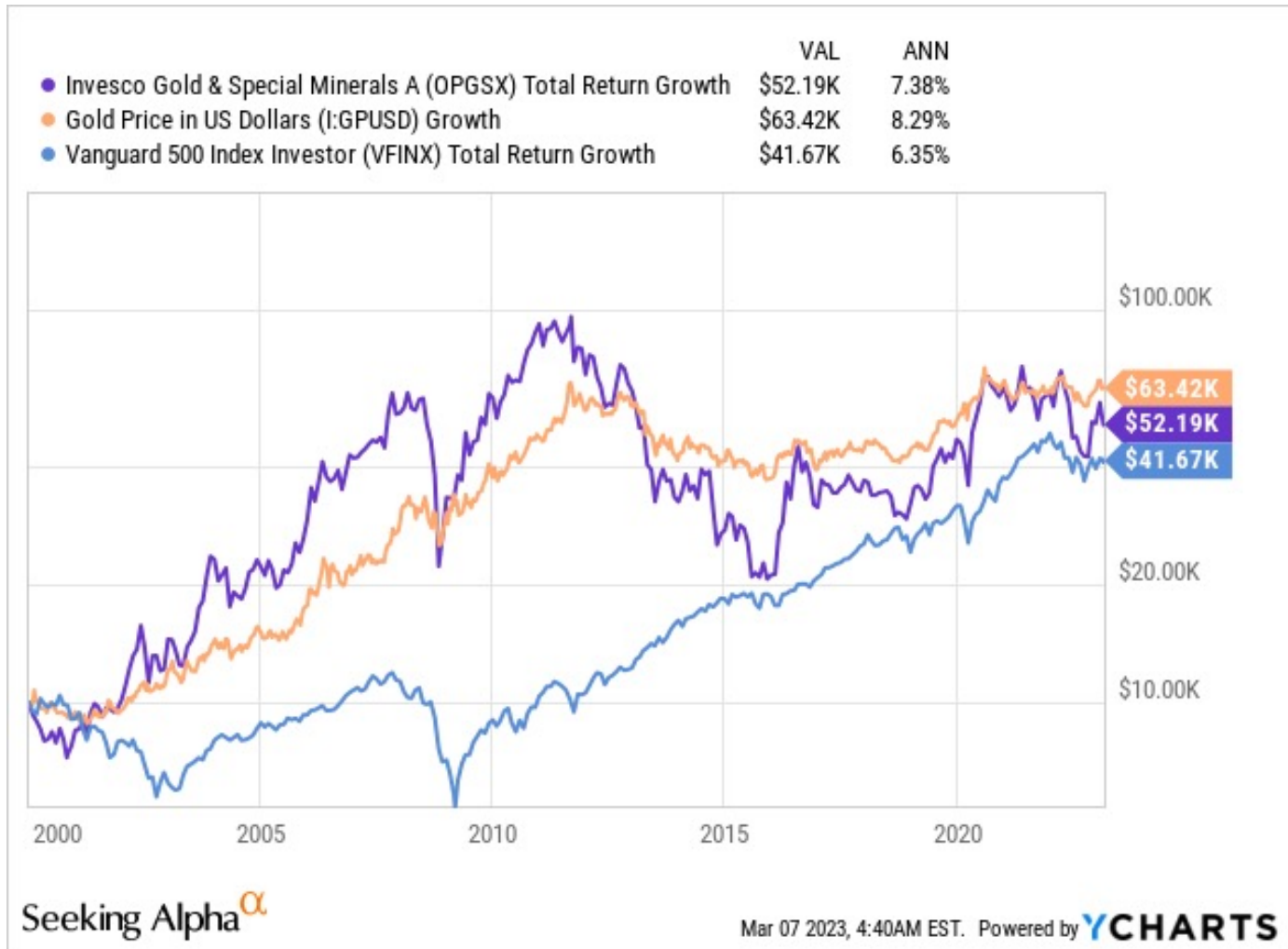
Pro-forma 20% Overlay on 5-Year Bonds Since 1970



Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.

Source: Dimensional Fund Advisors, Author's Calculations

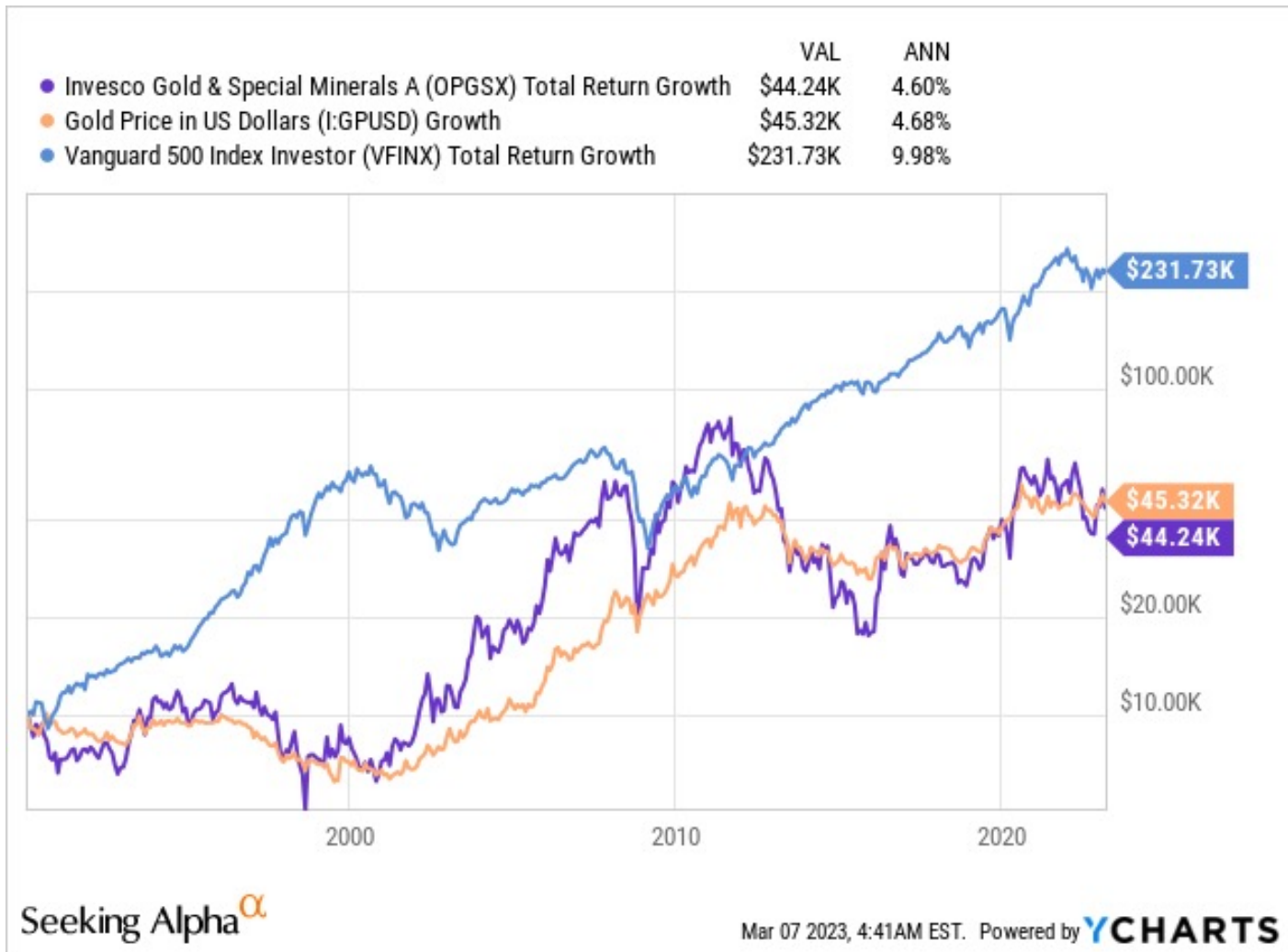
What about gold mining stocks? Since 2000:



Source: Ycharts

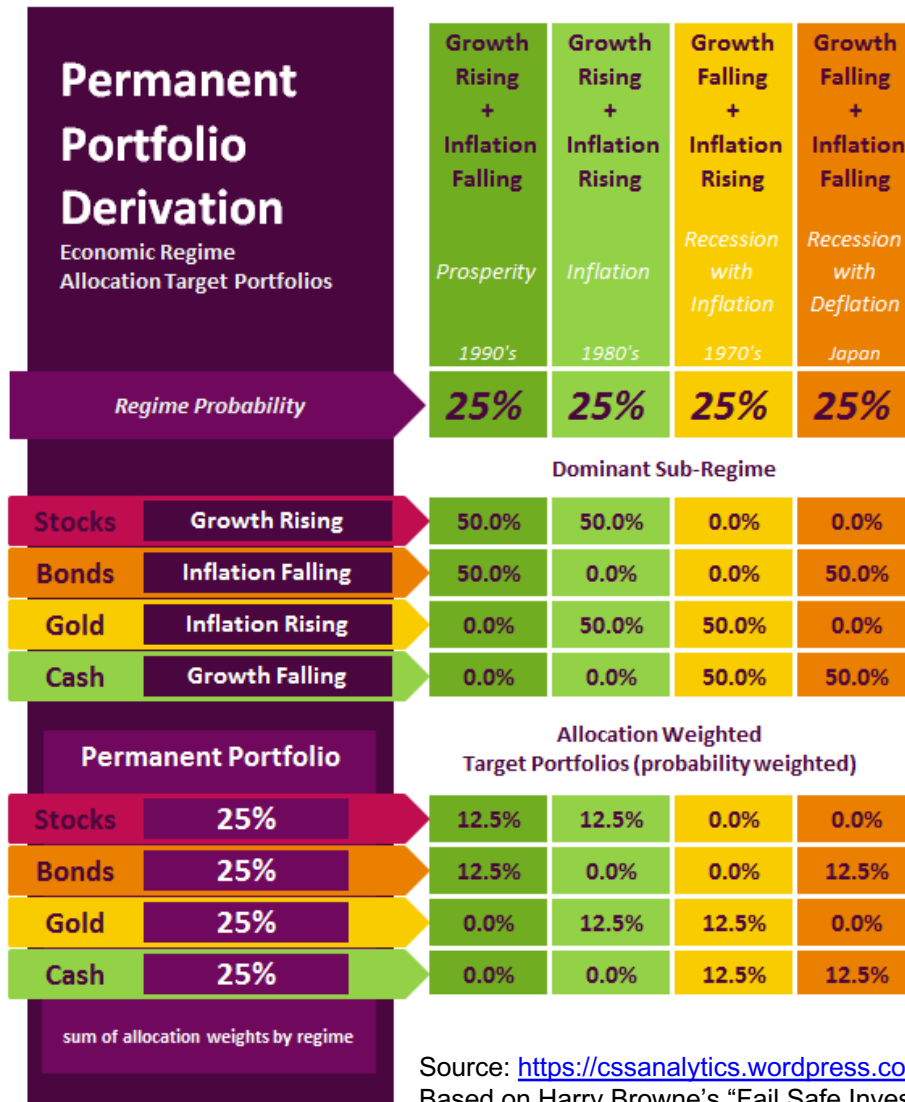
Mining risks: Investing in gold mining stocks comes with additional risks, such as operational risks at the mine, regulatory risks, and exploration risks.

Since 1990:



Mining risks: Investing in gold mining stocks comes with additional risks, such as operational risks at the mine, regulatory risks, and exploration risks.

Rather, consider gold's role in "The Permanent Portfolio"



- Private equity can compliment / replace some public stocks
- Hedge funds can replace some public bonds in a low rate environment
- Commodities, collectibles, and other hard assets can compliment or replace gold
- The most liquid of the above can compliment the cash allocation

Source: <https://cssanalytics.wordpress.com/2012/11/01/permanent-portfolio-derivation-and-historical-performance/>
Based on Harry Browne's "Fail Safe Investing"

Micro gold futures & big gold options on IBKR TWS

“Big” Gold (GC) vs Micro Gold (MGC) on IBKR TWS

	LAST	CHANGE
GC ∞ Apr26'23 @COMEX	◆ 1817.20	-7.70 -0.42%
MGC ∞ Apr26'23 @COMEX	◆ 1817.40	-7.50 -0.41%

DESCRIPTION File Configure

Gold

Security Type **FUT**
 Underlying **GC IND**
 Contract Month **APR23**
 Expiration Date **APR 26 '23**
 Last Trading Date **APR 26 '23 13:30 EST**
 Currency **USD**
 Multiplier **100**
 Exchange **COMEX**
 Trading Class **GC**
 Symbol **GCJ3**
 Product Type **Metal**
 Settlement Method **Physical Delivery**
 Physical Delivery **Not permitted at Interactive Brokers**

Trading Schedule: February 28, 2023 [Calendar](#)
 Regular Trading Session 09:30 - 17:00 (22:30 - 06:00 your time)
 Total Available Hours 18:00* - 17:00 (07:00 - 06:00 your time)
 Exchange Time Zone US/Eastern

** Times in italics are on the calendar date preceding trade date*

Margin Information

Margin Requirements Per Contract [More](#)

Initial **11692.58 USD**
 Maintenance **9354.06 USD**

DESCRIPTION File Configure

E-Micro Gold

Security Type **FUT**
 Underlying **MGC IND**
 Contract Month **APR23**
 Expiration Date **APR 26 '23**
 Last Trading Date **APR 26 '23 13:30 EST**
 Currency **USD**
 Multiplier **10**
 Exchange **COMEX**
 Trading Class **MGC**
 Symbol **MGCJ3**
 Product Type **Metal**
 Settlement Method **Physical Delivery**
 Physical Delivery **Not permitted at Interactive Brokers**

Trading Schedule: February 28, 2023 [Calendar](#)
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 Exchange Time Zone US/Eastern

** Times in italics are on the calendar date preceding trade date*

Margin Information

Margin Requirements Per Contract [More](#)

Initial **1169.26 USD**
 Maintenance **935.41 USD**

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Source: Interactive Brokers, 28 Feb 2023



Sample Micro Gold Trade

The screenshot displays the 'ORDER ENTRY' window for 'MGC ∞ Apr26'23 @COMEX'. The order is a BUY order with a quantity of 1, limit price of 1800.00, and routing to COMEX. The order confirmation dialog shows the following details:

Financial Instrument	Bid	Ask	Last
MGC ∞ Apr26'23 @COMEX	1816.00	1816.20	1816.10

Order Description
 BUY 1
 Order Type LMT Routing COMEX Time in Force DAY
 Limit Price 1800.00 Clearing IB

Messages

Amount	Balances (in USD)
Amount 18,000 USD	Current Change Post-trade*
Commission (est.) 0.77 USD	Equity with Loan 388,948 -0.77 388,948
Total 18,000.77 USD	Initial Margin 37,085 1,127 38,212
	Maintenance Margin 31,042 902 31,944
	Position 0 1 1

*This is a current projection and is subject to change.
[Margin Requirements Per Contract](#)

Don't display this message again.

Buttons: **Override and Transmit** (disabled), **Cancel** (active)

DATA POWERED BY

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Trading gold via futures

- Only need to fund margin
- Long leverage financing rate built in
- Short position as easy as long position
- What you see is what you pay
- Need to "roll" every contract expiry

... vs an ETF

- Need to fund in full
- Margin loan (interest) to leverage long position
- Need to borrow shares to short
- Expense ratio charges gold reserves over time
- Can buy and hold "forever"

Full-size gold (GC) also has options...

GC ∞ Apr26'23 @COMEX PUT/CALLS (Side by Side) 1815.20 -9.70 (-0.53%)

APR / JUN OG 100 56 DAYS MAY / JUN OG 100 86 DAYS JUN / AUG OG 100 112 DAYS MORE

FOP last trading day is MAY 25 '23 underlying FUT contract is JUN 28 '23

TABBED VIEW PUT/CALL All STRIKES COMEX TRADING CLASS 100

IV: 13.7%

CALLS					PUTS						
OPTN O...	VOLUME	BID	ASK	DELTA	STRIKE	OPTN O...	VOLUME	BID	ASK	DELTA	STRIKE
23		2	87.70 x 88.40	0.725	1765	30	59	21.60 x 22.10	-0.280	64	
28		2	84.20 x 84.90	0.711	1770	52	53	23.10 x 23.50	-0.294	6	
226		2	80.80 x 81.50	0.697	1775	353	58	24.60 x 25.10	-0.309	62	
2		1	77.50 x 78.20	0.682	1780	198	66	26.20 x 26.70	-0.324	17	
2		1	74.30 x 74.90	0.667	1785	12	54	27.90 x 28.40	-0.339	17	
11		1	71.10 x 71.80	0.651	1790	59	54	29.70 x 30.30	-0.354	17	
		1	68.00 x 68.70	0.636	1795	21	46	31.60 x 32.20	-0.370	17	
1.68K	2	1	65.00 x 65.70	0.620	1800	3.80K	179	33.70 x 34.00	-0.386	1	
18		3	62.10 x 62.80	0.604	1805	39	59	35.60 x 36.20	-0.402	17	
46		19	59.30 x 60.00	0.588	1810	348	38	37.80 x 38.30	-0.419	11	
20		25	56.60 x 57.30	0.571	1815	40	1	40.00 x 40.60	-0.435	17	
60		31	54.00 x 54.70	0.555	1820	568	56	42.30 x 42.90	-0.451	17	
243		35	51.50 x 52.10	0.538	1825	7.37K	38	44.80 x 45.40	-0.468	17	
69		37	49.00 x 49.70	0.522	1830	847	2	47.30 x 47.80	-0.484	11	
87	7	5	46.70 x 47.30	0.506	1835	95	38	49.90 x 50.40	-0.501	11	
108	2	43	44.40 x 45.00	0.489	1840	82	38	52.50 x 53.10	-0.517	11	
137		7	42.30 x 42.80	0.473	1845	50	36	55.30 x 55.90	-0.534	17	
5.07K	1	7	40.20 x 40.70	0.457	1850	3.00K	11	58.20 x 58.70	-0.550	11	
10		43	38.10 x 38.70	0.441	1855	205	29	61.10 x 61.80	-0.566	34	
1.72K		7	36.20 x 36.80	0.426	1860	1.45K	23	64.10 x 64.80	-0.581	28	
113		7	34.40 x 34.90	0.410	1865	116	16	67.20 x 67.90	-0.597	21	
569	4	7	32.60 x 33.10	0.395	1870	659	1	70.40 x 71.10	-0.613	6	

OFF Strategy Builder

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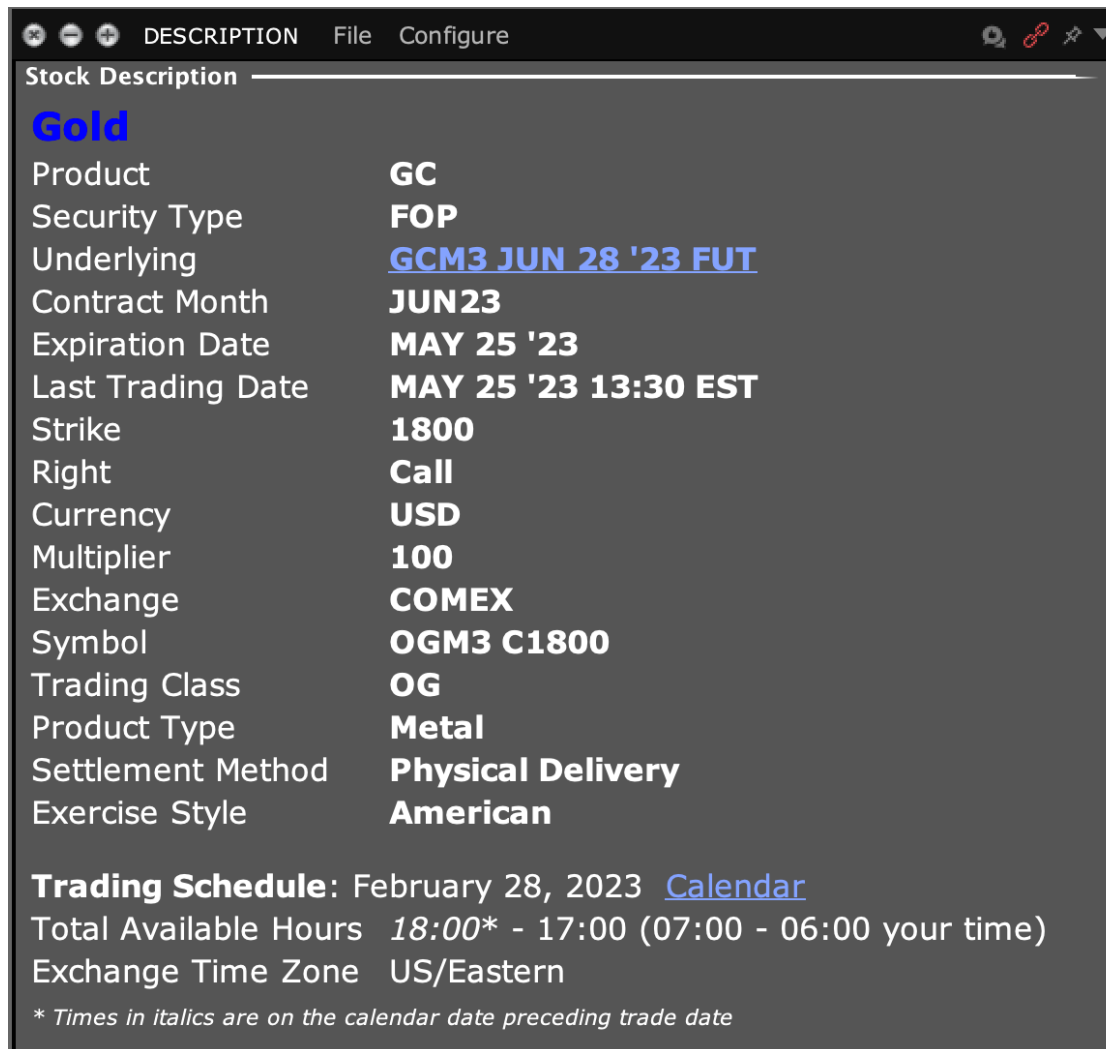


Source: Interactive Brokers, 28 Feb 2023

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Description of an 1800 strike call on GC

This one was quoted at \$6,600/contract



The screenshot shows a window titled "DESCRIPTION" with a menu bar containing "File" and "Configure". The main content area is titled "Stock Description" and lists the following details for a Gold Call option:

Gold	
Product	GC
Security Type	FOP
Underlying	<u>GCM3 JUN 28 '23 FUT</u>
Contract Month	JUN23
Expiration Date	MAY 25 '23
Last Trading Date	MAY 25 '23 13:30 EST
Strike	1800
Right	Call
Currency	USD
Multiplier	100
Exchange	COMEX
Symbol	OGM3 C1800
Trading Class	OG
Product Type	Metal
Settlement Method	Physical Delivery
Exercise Style	American

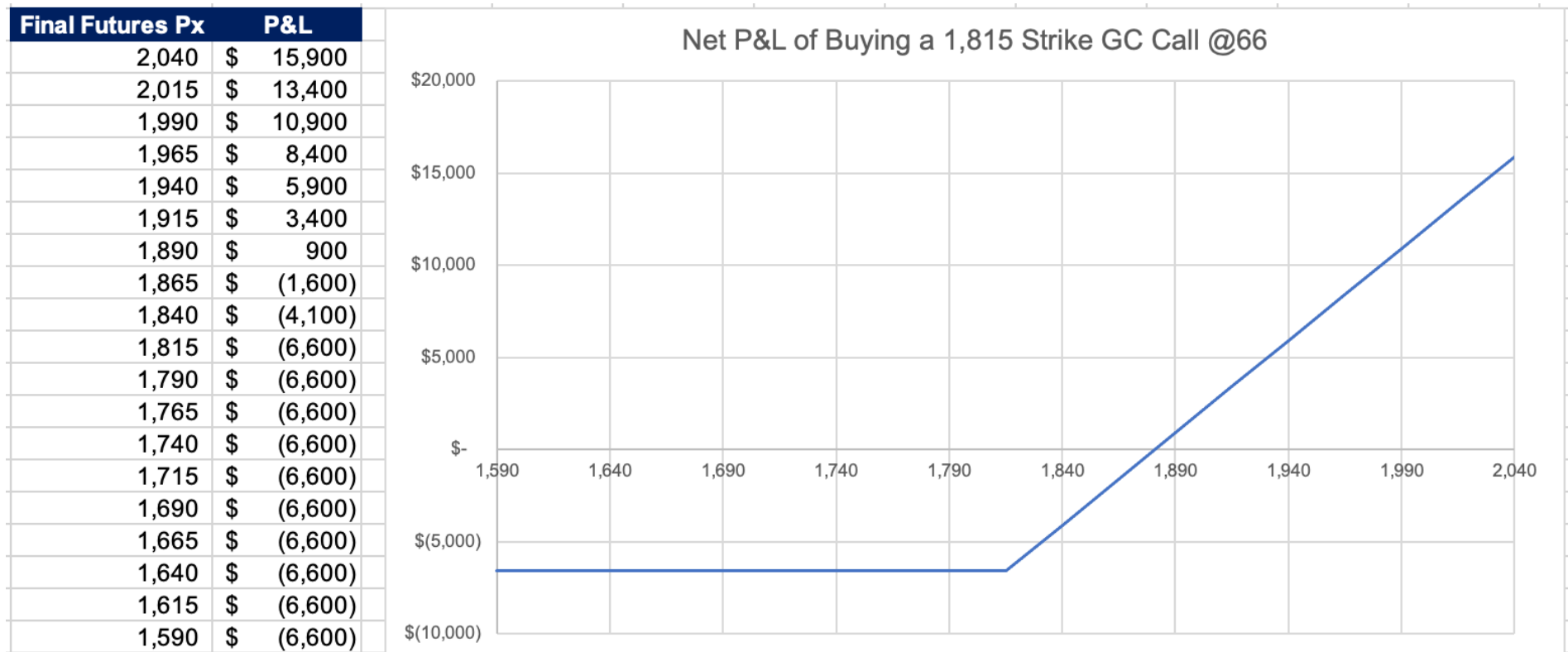
Trading Schedule: February 28, 2023 [Calendar](#)
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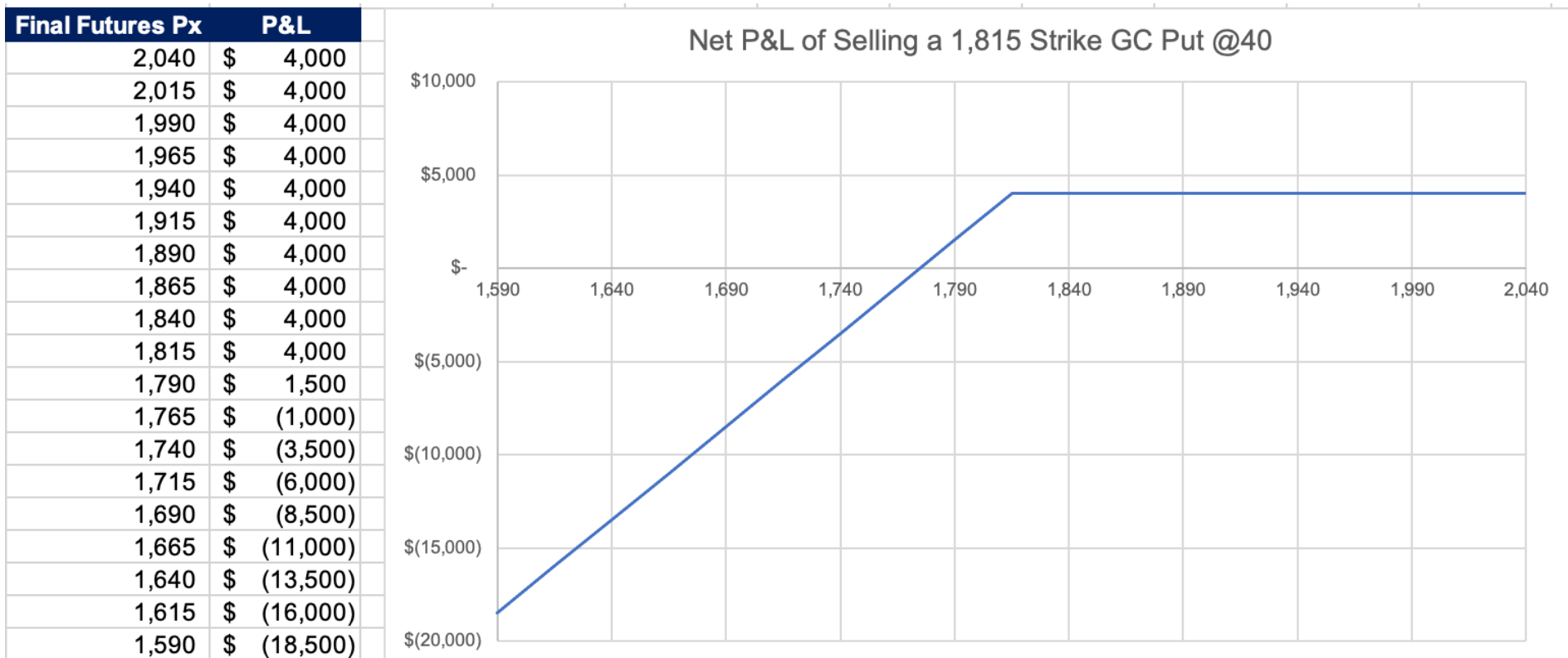
Sample payoff diagram of buying that call option



Source: Author's calculation

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Another option example: selling (aka “writing”) a put

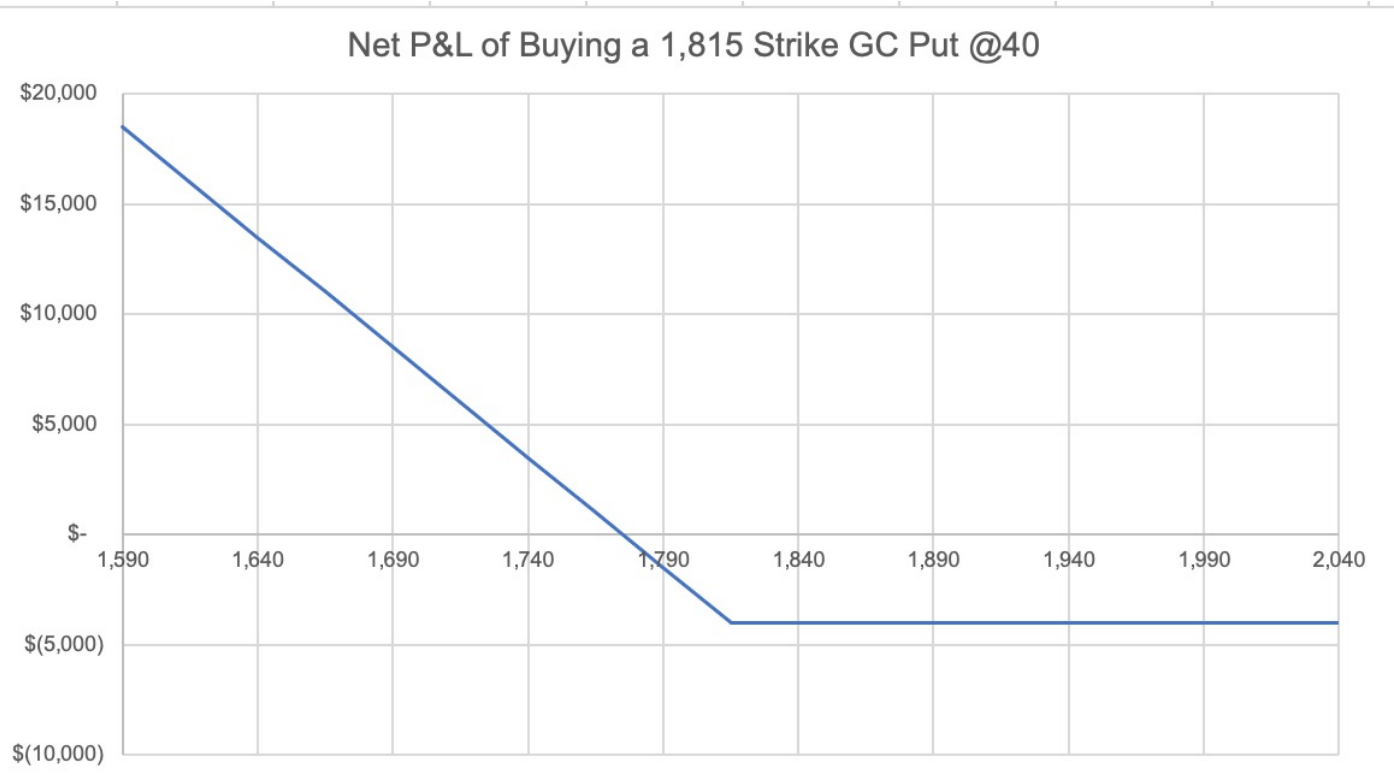


Source: Author’s calculation

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If you expect gold to fall (or want to hedge), you could instead buy this put

Final Futures Px	P&L
2,040	\$ (4,000)
2,015	\$ (4,000)
1,990	\$ (4,000)
1,965	\$ (4,000)
1,940	\$ (4,000)
1,915	\$ (4,000)
1,890	\$ (4,000)
1,865	\$ (4,000)
1,840	\$ (4,000)
1,815	\$ (4,000)
1,790	\$ (1,500)
1,765	\$ 1,000
1,740	\$ 3,500
1,715	\$ 6,000
1,690	\$ 8,500
1,665	\$ 11,000
1,640	\$ 13,500
1,615	\$ 16,000
1,590	\$ 18,500



Source: Author's calculation

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Using strategy builder to build a call spread on gold

This one costs \$2,300, all lost if gold <\$1,815 in May, \$5,000 paid out if gold >\$1,865

PUT/CALLs (Side by Side)
1815.50 -9.40 (-0.52%)

APR / JUN
OG
100
56 DAYS

MAY / JUN
OG
100
86 DAYS

JUN / AUG
OG
100
119 DAYS

MORE

TABBED VIEW
PUT/CALL
All STRIKES
COMEX
TRADING CLASS
100

CALLS						PUTS										
OPTN O...	VOLUME	BID	SIZE	BID x ASK	DELTA	ASK	SI...	STRIKE	OPTN O...	VOLUME	BID	SIZE	BID x ASK	DELTA	ASK	SI...
20	7	56.80	7	56.80 x 57.40	0.572	57.40	30	1815	40	1	39.80	65	39.80 x 40.40	-0.434	40.40	75
60	31	54.20	31	54.20 x 54.80	0.556	54.80	37	1820	568	65	42.20	65	42.20 x 42.70	-0.451	42.70	11
243	60	51.60	60	51.60 x 52.20	0.539	52.20	70	1825	7.37K	65	44.60	65	44.60 x 45.10	-0.467	45.10	11
69	81	49.10	81	49.10 x 49.80	0.523	49.80	73	1830	847	2	47.10	65	47.10 x 47.60	-0.484	47.60	11
87	7	46.80	64	46.80 x 47.30	0.506	47.30	4	1835	95	65	49.70	65	49.70 x 50.20	-0.500	50.20	11
108	2	44.50	64	44.50 x 45.00	0.490	45.00	11	1840	82	64	52.30	64	52.30 x 52.80	-0.517	52.80	4
137	64	42.30	64	42.30 x 42.90	0.474	42.90	74	1845	50	61	55.00	61	55.00 x 55.60	-0.533	55.60	36
5.07K	1	40.20	64	40.20 x 40.80	0.458	40.80	73	1850	3.00K	11	57.90	57	57.90 x 58.40	-0.549	58.40	4
10	64	38.20	64	38.20 x 38.80	0.442	38.80	74	1855	205	29	60.90	29	60.90 x 61.40	-0.565	61.40	7
1.72K	76	36.20	76	36.20 x 36.90	0.426	36.90	74	1860	1.45K	23	63.80	23	63.80 x 64.40	-0.581	64.40	7
113	64	34.40	64	34.40 x 35.00	0.411	35.00	74	1865	116	16	67.00	16	67.00 x 67.70	-0.597	67.70	21
569	4	32.60	72	32.60 x 33.20	0.395	33.20	76	1870	659	1	70.10	1	70.10 x 70.70	-0.612	70.70	1

Strategy Builder Strategies

ACTN	RT	CNTRCT	MNTH	STRIKE	TYPE	DELTA	THETA	BID/ASK	SIZE	
Buy	1	JUN '23	1815	Call	0.572	-0.268	56.80 x 57.40	7 x 30	Snapshot	
Sell	1	JUN '23	1865	Call	0.411	-0.270	34.40 x 35.00	64 x 74	Snapshot	
Jun 1815/1865 Bull Call						0.162	0.002	21.80 x 23.00	7 x 30	Delayed

Clear All Legs
+ PROFILE
+ Add to Watchlists

21.80
23.00

BID
MID
ASK

Order Entry
LMT QTY 1 LMT PRC 0.00 DAY advanced
Margin Impact: 1,895 USD
Submit Order

Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations. There is a substantial risk of loss in trading futures and options. Past performance is not indicative of future results.



Gold vs Bitcoin

- “Scarcity as a Service”
- Only one element 79, only 21 million Bitcoin
- Supply curve related to the cost of “mining”
- Demand not related to usage
- Bitcoin is a digital asset with a much shorter track record that is subject to greater volatility and regulatory uncertainty.
- More on Crypto in another presentation...

Questions?

GFM Contact

Tariq Dennison

<https://gfmasset.com>

TDennison@gfmgrp.com

Twitter: [@QuantOfAsia](https://twitter.com/QuantOfAsia)

Seeking Alpha: TARIQ DENNISON