Gold vs. Long Duration Treasuries: Which One is a Better Long Term Diversifier Right Now?

By Vineer Bhansali | February 9th, 2026

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In a recent conference, I heard Nobel Prize winner Robert Engle talk about long term risk. To quote:

> *"A risk is a bad outcome which has some probability of occurring.*
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> *A long-term risk is from an event which is far in the future.*
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> *Assets exposed to long term risk are less desirable than assets that are not. If the risk goes up, the price will go down even if the risk is far in the future.*
>
> *Further, a hedge portfolio is one that is long assets that benefit from this risk materializing and short assets which are adversely impacted from it.*
>
> *Hedge portfolios cost money.*
>
> *Shorting the hedge portfolio earns risk-premium for those who can afford to warehouse it."*

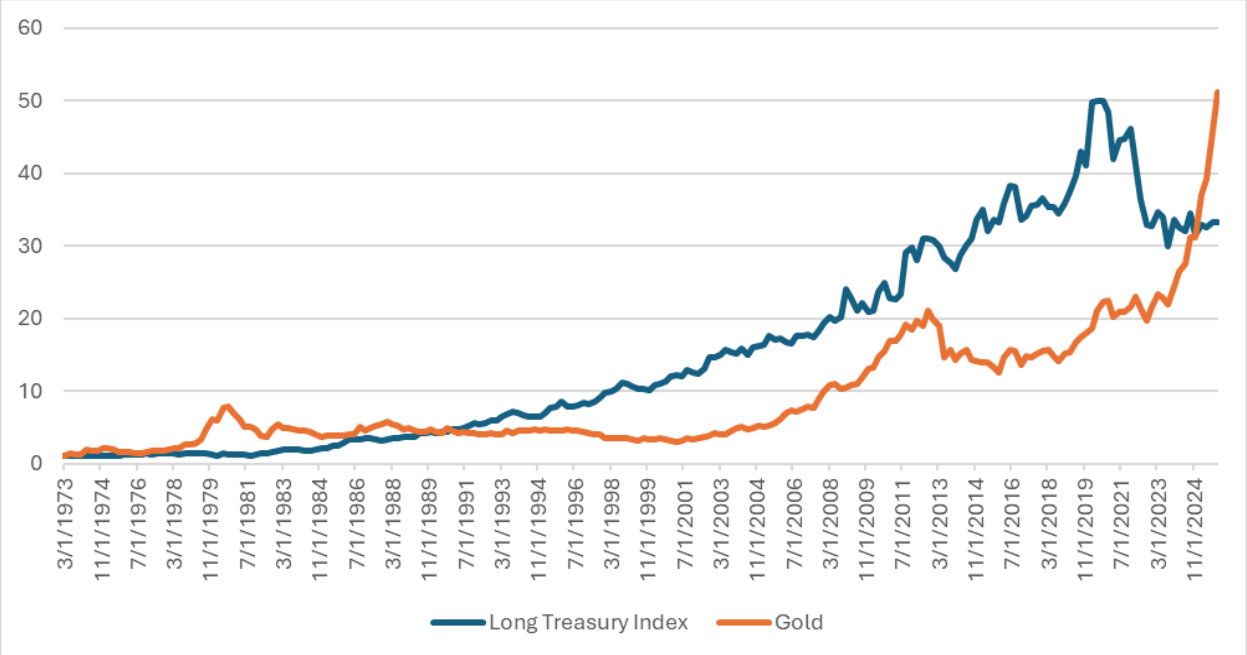
Let us talk about the two main macro hedges in play today: gold and long-duration bonds.

For those who have been following the bond markets over the last three decades, long-duration bonds fit the description of a hedge portfolio against equities perfectly – in the rear view mirror. But as the fear of inflation risk increased starting right after COVID-19, they have done quite badly. If bonds were diversifiers against equity risk, then by the definition above, owning bonds should have cost money over the three decades prior to COVID-19, but on the contrary, bonds made money even as they diversified. This is because inflation risk, which is anathema for bonds, never surfaced during the pre-COVID-19 period. Indeed, inflation risk fell. Investors got a massive freebie – return and free diversification.

To provide a counterpoint to bonds, let us also talk about an asset that has done quite well over the period since COVID-19: Gold. Starting in 2020, it caught up and exceeded bond returns as a new regime surfaced. This new regime has been inflationary, and gold responded

to the sudden rise of this hidden risk, amongst other risks related to geopolitics, threats to Fed independence etc. Over this period long duration bonds have lost money, not in the least because developed market central banks bought up bonds during COVID and right after at nosebleed high prices (low yields) and hence artificially inflated prices which had to come back to earth.

In the chart we see how the long Treasury bond market index has fared against gold over the last fifty years (since March 1973). It is stunning to see that after lagging for many years, in a half decade gold has made up all the lost ground and now is winning the horse race against long Treasuries. That despite having had no yield! The last time this happened was probably way before long duration Treasuries had become part of every institutional portfolio. This time the culprits might be central banks again – though mostly from countries that are called "developing".



Bloomberg Long Duration Total Return Index vs. Gold Index. Values are rebased to start at 1 in March 1973. Source: LongTail Alpha

So, has gold re-taken its role as the ultimate diversifying asset against long term risks?

First, some theory. If duration is a diversifier, then we can summarize the potential of duration as a diversifier by analyzing the longest maturity Treasury zero coupon bond.

Currently this crown is held by the zero coupon Treasury "Strip" (the coupon bearing Treasury is literally "stripped" off its coupons and principal) maturing in November 2055. It pays no interest on the way to its 30-year maturity, and redeems at par. If you were to buy this bond today, at its yield of roughly 5%, its price is 23 cents, and its duration is roughly 30 years. If you buy this bond and yields fall 1% instantaneously in response to economic growth faltering, you would make a little bit over 30% from the duration and convexity (this is essentially a mathematical identity). The whole institutional investment space has used this fact, along with the negative correlation of stocks to bond prices, to use long duration Treasuries (and its cousins), such as long duration interest rate swaps, to "hedge" equity or growth risk.

The reason all this works is because return of principal is guaranteed, and the net present value of that principal rises when yields fall. So, while falling yields play an important function in making duration-based instruments good hedges when inflation is low, it is the guarantee of getting your principal back where this and all hedging gets its real power from. What if we lived in a world where we were not guaranteed the principal of a zero coupon bond? Of course that bond, despite its long duration, would not be a good hedge. What if you were guaranteed the principal in funny money, but the real currency could be debased? Again, the duration of the bond would not make much impact on its real, economically relevant diversification potential. It would be outright silly for you to buy a long duration, zero coupon bond for diversification from a person who could default on you through either an actual default or debasement. In other words, duration is only good if there is no potential of default, in any form, ever! Otherwise Argentina's bonds (a serial defaulter), would be a great way to hedge equity risk, which of course it isn't.

One reason why gold has done so well recently is that the "other" global central banks have quietly accumulated more gold in dollar terms than their hoard of Treasuries (see for example the chart here which has made lots of headlines) and pushed up its price in the process. For the first time in thirty years, they own more gold than Treasuries in US dollar terms, and the direction of travel is towards even more gold, not less. What do they know that the rest of us don't? I won't repeat all the reasons for this, but what we are seeing is a secular shift away from long duration Treasuries to gold as a diversifier, and it is not because gold has better "duration". The root cause is that the Treasury is an obligation, full faith and credit, of the US. So, armed with a printing press, the US will never default nominally on that obligation. But, it can, and likely will, make the value of those Treasuries go down relative to other assets; i.e.

inflate away the value, since paying back almost 40 trillion of debt in constant real terms is very hard to do. One might even say its quite rational for the debtor to inflate away a large debt rather than default. So while long duration Treasuries have duration, when the terminal value of the obligation is in a much weaker currency, the benefits of the duration exposure can be more than negated by this potential of real capital loss. Gold is not the obligation of any one country, and no one single central bank can control its value over the long term, so it is somewhat more protected, and since it is virtually indestructible, it is also not possible to devalue against all currencies at the same time. As a matter of fact, the longer the horizon, the less important the discounting effect becomes, and the more important the return of capital becomes. The longer the horizon, the more likely that the value of the debt is driven close to zero.

Just for kicks, and while we are on the topic of duration, if the duration of the longest existing Treasury is about 30 years, we may ask what the duration of gold is? If one were to run a regression of gold returns on inflation adjusted yields, that number, the "empirical duration", is between 15 and 30 years, depending on the era and period one uses to estimate the duration. On the other hand, I argue, the fundamental, theoretical duration of Gold is essentially infinite since it is essentially indestructible! Thus, putting it on the same footing as an interest sensitive instrument, where the discount factor is the real Treasury yield curve, is a mistake, and so is the concept of an interest rate duration for gold. Statistical correlations do not make causal relations. The duration based calculus can only hide the fact that for a real, long-term diversifier, it is not the mathematical duration that matters, but the return of principal. For gold there is no terminal date for the redemption of principal, and there are no intermediate "coupons" or "dividends" either. Rather than being a weakness, one could call this a strength if one wants the value to be stored forever. Since gold does not mature and does not pay a coupon, it does not make sense to compute an interest rate duration for it other than for mathematical curiosity.

So why is interest rate duration for gold even relevant? The main reason is historical and has to do with the current paradigm for risk based portfolio construction. Markets have been conditioned to duration being a negatively correlated risk factor to equity risk, and we have lived in an investment climate where the equity "beta", and its bond market cousin, "interest rate duration", are the way investors create portfolios that have quantitatively measurable exposures. In other words, we have had the luxury to compartmentalize the asset allocation

exercise in terms of the risk-factor exposures of assets to risk-factors such as equity beta, duration, credit duration etc. We should not forget that the reason such an approach works is because it is assumed that there will be full redemption of the principal. When this fundamental assumption is dropped, the risk-factor based approach cannot be of much help in constructing portfolios since asset risks cannot be mapped neatly into risk-factors.

This is where gold, well, shines. While it does not have a predictable interest rate duration or equity beta, it has a quality that seems to be getting more and more valuable in the minds of both large central banks and retail investors – it is a way to guarantee the return of principal for a very long horizon. That's why it is becoming the zeroth order diversifier for portfolios and outperforming long duration Treasuries. There is indeed nothing wrong with owning long duration Treasuries as a diversifier, it is just that they are not the only game in town when the problem that is being solved is the guarantee of return of investment over the very long term.

Coming back full circle to Professor Engle's definition – if not getting the real (inflation adjusted) principal back is the long term risk far in the future, either due to possible defaults or inflation, and this event has some probability of happening, then assets like gold that will benefit from the probability of this risk rising will rise in price, and one should be willing to pay a premium (i.e. no yield) to own them. Shorting this hedge asset may earn a premium if the risk does not materialize. We should also allow for the possibility that the rapid rise in gold might be reflecting the increased probability of this risk, but not fully. If this is true, then holding gold and shorting long duration Treasuries will be the right hedge portfolio. On the other hand, if this probability of principal loss is over-priced in the market, then one should hold less or no gold and more long-term Treasuries. They are just different ways to diversify.

Putting it all together, the market is behaving quite rationally, and thus logically getting to the point where the holdings of gold and long duration are converging to be about the same. Tautologically one could argue that the recent catch-up in the price of the gold reflects the fact that it was under-owned, since the long term risks we just discussed were under-appreciated. If so, then there is much more room above for prices to grow if the probability of the long term risk we discuss turns out to be larger than what the market is pricing. I, for one, will not be surprised if in the path from here to there, the price of gold is many multiples of what it is today, while the price of long duration bonds, well, goes nowhere.

Important Disclosures

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