

# Why Is Gold Not Much, Much Higher?

by [Jonathan Davis](#)

24th March 2017



Practically everything that could have been said about gold has been said.

You know that the market bottomed around the year 2000 at around \$250/oz.

It soared to around \$1,000 by 2008. Then it crashed in the general asset price collapse, that year, to around \$700.

But then it soared again in the post-recession reflation to over \$1,900 by 2011. (Silver, by the way, had even larger movements, in percentage terms).

Then, as long term holders know only too well, it crashed again to around \$1,050/oz by January 2016.

Over the last 14 months it has had another roller-coaster ride, rising to \$1,370 (July) and back again to \$1,120 in December.

Just when it seemed to be back in a bull market (\$1,260 just at the end of February): BAM! It moved sharply down to \$1,195 by 6 March.

Wow! What a ride.

You also know that mining of gold is at multi-year, if not multi-decade lows, yet demand remains constant.

You know that the four refiners of gold in Switzerland are working flat out and everything they sell goes East to India, China and Russia.

You know that Germany has been repatriating all its gold.

You even know that one ounce of gold, today, buys essentially, for a professional, the same as an ounce in ancient Rome for a, then, Senator – a suit / a toga; leather shoes and belt / sandals and belt.

In other words, it has been written over and over again that gold should rise into the thousands of US dollars per ounce.

Yet, as I write it stands at just over \$1,240/oz.

And I hear you ask the same question that everyone asks: Why isn't it much, much higher?

To answer that, firstly, we have to go back to basics.

Gold is deemed by many to be the only true currency. Indeed, it has retained its purchasing power over at least 5,000 years.

However, never before have central banks been so instrumental in determining asset prices in global markets, nor has there been such deflation.

Let's look at the latter first.

Commodities, including gold, are priced in US dollars. A rising dollar generally brings commodity prices down and vice versa.

The US dollar soared between 2011 and early 2015. Thus, we have had very low inflation or even deflation for years.

Since then, against the normal basket of currencies (euro, yen, sterling, etc.) it's essentially flat. It's been down and up but, after two years, it is where it was in March 2015.

So, with the dollar no longer rising this has, of itself, been helpful to the prices of commodities and gold. If the dollar was to fall, sustainably, this could have a major inflationary effect and boost gold prices.

When I look at dollar charts, now, and compare to other major currencies, I see weakness entering the market and I can see material moves higher in the euro, yen, sterling, etc., over several months.

This could be strongly positive to gold.

It has been clear for a long time that monetary policy has been aimed at boosting stock markets. Here is a long term (60 year) chart of stock prices (S&P 500 index) versus commodity prices (CRB Index):



For (whatever) reason, over the last 40+ years, stock prices have, almost continually, outperformed commodity prices.

Indeed, since the crash of 2008/09 you would have made great profits investing in US stocks and selling short commodities.

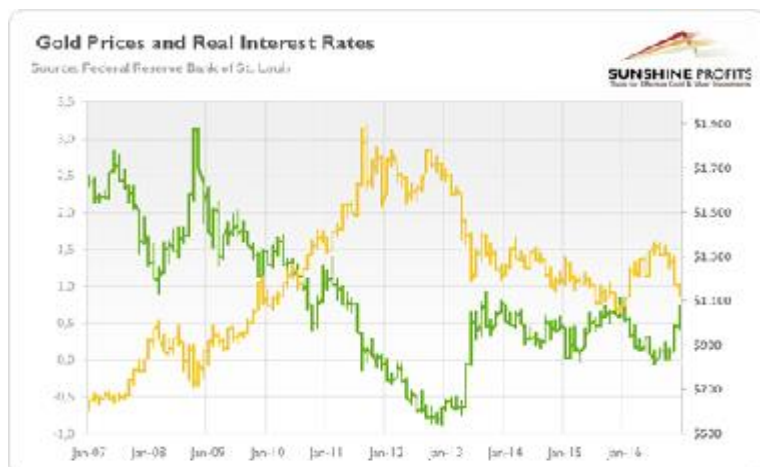
The ratio is at all-time highs. Note, though, the percentage rate of annual change stands at around zero, down from a whopping 60% a couple of years ago.

It was also at the 60% level just before the beginning of the multi-year bull market in commodities and gold, at the turn of the century.

One has to wonder if the rate of change next goes negative i.e. commodities OUTPERFORM stocks...

It seems to me, with a falling dollar we could well see commodities and gold outperform stocks (i.e. the percentage rate of change in the above chart turns negative).

Another factor in gold prices is the real interest rate (the base rate minus CPI).



For the last 10 years, at least, there has been a strong inverse correlation between the gold price (right hand axis) and real interest rates (left hand axis).

On Wednesday 15 March the Fed raised the rate (for the second time in three months). However, real rates remain as low as they have been for many years. This is bullish for gold.

Finally, we turn to technical analysis.

Simple trend lines show both resistance and support are close, between around \$1,280, to the upside, and \$1,150 to the downside:



Break up or down out of the huge multi-year wedge and the market will, likely, be telling us what the future holds. Note the RSI is on a rising trend, suggesting upwards momentum.

Also, latterly, from 2013 to early 2016, as prices fell the RSI did not become oversold (under 30). On top, in the late 2016 correction, the RSI had a clear higher low. These are also bullish for gold.

In October 2016, my clients increased their portfolio holdings in gold and gold mining shares to a) the largest ever and b) the largest part of portfolios.

So, I've been putting our money where my mouth is.

I must add the following note of caution.

There has to be at least a 40% probability that we have at least one more lurch down in deflation in the short to medium terms.

In that scenario, I might find that – even if gold and miners do well (possibly exceptionally well) for months – I have to divest of the holdings.

In such a deflationary scenario, there is a case for gold going back to below December 2015 levels, i.e. below \$1,050/oz and perhaps even as low as \$500.

For now, though, I and my clients are heavily long. Nothing is forever and we must adjust portfolios according to market conditions, NEVER what we believe should be!

Jonathan Davis is the presenter of The Booms and Busts Show. [You can subscribe here.](#)