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Money Matters
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Gold... WHERE WILL PRICES GO?

The price of gold recently topped $1,900 a troy ounce before falling back again. While jewellery consistently remains the largest source of global demand, gold's safe haven status continues to influence prices.

In order to do a "rich-cheap" analysis in terms of historical price levels, gold is often discounted to its "real" value using US inflation as a deflator. This way gold is trading near an all-time high. However this is not entirely appropriate as the US accounts for less than 10% of global gold demand. In China and India who account for over 50% of global demand, by discounting gold prices by nominal increases in wages in these countries, gold has remained more affordable. While the price of gold has increased, wages have also increased lessening the impact of higher prices. The general uptrend in gold prices over the past decade has more than any other factor been due to growth in Asia.

Since the onset of the financial crisis in 2007, western investors, who throughout the early to mid 2000s shunned gold, have returned through purchasing exchange traded funds, gold bars and coins. Central banks who were net sellers of gold over the same time period have also reversed that trend. While not the largest source of demand, both cases have put upward pressure on gold prices. Combined with high inflation in fast growing emerging economies and fears over the strength of the US dollar, these factors together may have elevated gold beyond its "fair" price, with investors in panic mode.

While our research suggests gold has the potential to increase due to growth in Asia and because of its safe haven status, it may be subject to sharp corrections. Gold may rebate if the European sovereign debt crisis is solved, if the US gets their own fiscal house in order or a slowdown in Asia. With this in mind gaining exposure to up or down movements in gold prices within a certain trading range may be an ideal way to play gold prices. Such a strategy can be replicated through the use of derivatives.

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