Are We Near the End of the Gold Bull Market? I Don't Think So

Some usually gold-friendly commentators have suggested we may be near a top in the price of gold. They note that the discussion of gold by the mainstream press may be hinting at that. Your editor does not believe we are anywhere near a top in the price of gold or at least not in the "real" price of gold. I say that because I believe that most people have not yet begun to understand how close to a complete meltdown of our financial system we are. Nor do most people understand—because they have been propagandized to the contrary—that the very policies that are being proposed by the Bush and Obama Presidencies are the same policies that were tried and failed during FDR. Roosevelt's secretary of the Treasury said as much when he admitted that unemployment was as high after 8 years of Roosevelt as it had been when he took office. And as he noted, the government had taken on "a lot of debt to boot!"

One of my subscribers, a friend and Austrian-leaning economic thinker, is Antony Herrey. Regarding the notion that gold could be nearing its peak, Antony sent out the following e-mail, addressing that thesis. With his permission we are passing it on to you:

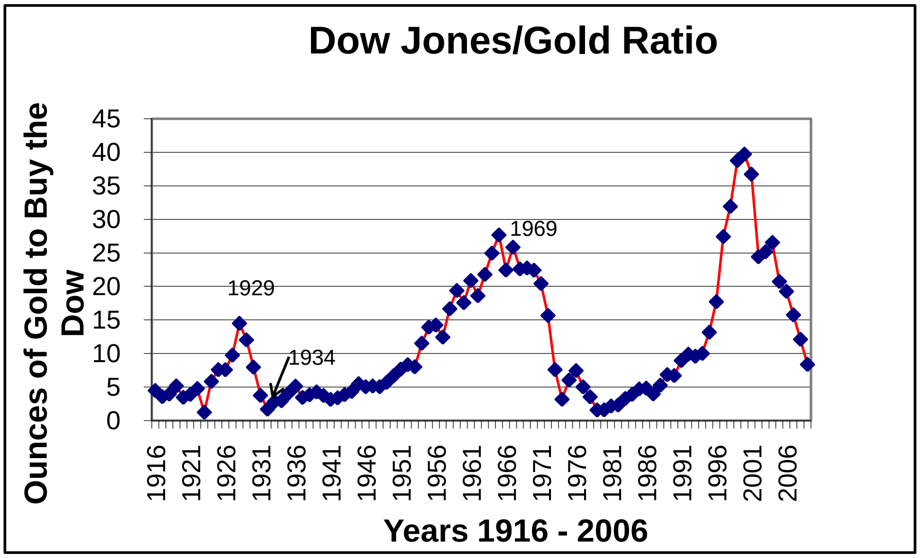
"In the late 1990s, when I would inspect progress of the construction work for a large office project I was developing, a major concern for me and my general contractor, as we faced critical deadlines, was the extent to which drywall installers, sheet-metal benders, and assorted other tradesmen were preoccupied by the stock market. I'll never forget entering a 25,000 square foot floor, where some fifty men who were supposedly putting up ceiling air conditioning ducts, were standing around in knots of maybe 5-10 individuals busily comparing notes about the dot-coms they had purchased and how far they were rising just then on the market. Walking around them, I could hear these guys spouting all the chatter taken from CNBC—earnings/share, P/Es, yields, moving averages, and all the rest. For me in the years leading up to 2000 this was a revelation.

"Reports like today's FT article make me yawn because we are still so far from the real gold frenzy I consider inevitable some years from now. When the Dow/gold ratio gets down to around 5, then I foresee that the common Joe who has never even held a gold coin in his hand will begin frantically to follow the gold market. He and his buddies will be spending their waking hours trying to buy gold, figuring out how to hold it, following the latest reports on price, volume, etc., etc.

"By that time, the august media like the FT, the NYT, the Economist, Fortune, etc., that now treat people like us with condescension, will become slavish cheerleaders and will cover every conceivable corner of the gold industry with intense focus as they realize that Joe Six-Pack and all his brethren have become gold bugs. That is when we shall have to begin worrying about how to exit the madness.

"We ain't seen nothin' yet!" Antony Herrey

THE DOW/GOLD CHART



Historically, since about the time the Federal Reserve Bank was created, when equity markets bottomed, the Dow to Gold ratio approached 1.0. Actually, the chart on your left is a rather crude chart because, except for this past week, all data points are as of Dec. 31 of each year starting in 1916. With various years at market bottoms we have seen a ratio very close to a 1:1. That latest one was in 1980 when gold hit $850 and the Dow was well below 1000.

Assuming you believe history is fated to repeat, you might be justified in suggesting a major move in gold vis-à-vis stocks has already taken place because the Dow to Gold ratio has already declined from around 44 times at its peak to a mere 8.39 times this week. However, if you bail out of gold now, you would still be giving up a potential eightfold increase in gold vis-à-vis stocks. Moreover, my friend Ian Gordon suggests that this time around, we may see a gold to Dow ratio of 0.25:1.0 because of the enormity of debt that has been built up in an environment, which for the first time in history has not been subject to the rigors of a gold standard in any country in the world. Simply put, wealth destruction that is destined to take place may be far worse than what took place in the 1930s. *Ian's views would be consistent with those of Dr. Robert McHugh who is suggesting we may be facing a "cataclysmic nation changing decline that corrects the bull market that began in 1718!* If we are indeed destined for that kind of a decline, then I think all bets are off with respect to how high gold's purchasing power may rise. Note I did not say how high gold might rise to. Rather I'm referring to how much an ounce of gold may buy.

I know there are arguments for a "strong" dollar because when you get one of these major credit contractions the senior currency becomes the strongest because borrowers rush out to cover their dollar short positions when they are forced to repay loans. And I do not discount the possibility that this process, which has been going on in spaces since the Lehman Brothers collapse, will continue. But with trillions of dollars being created out of thin air, it is my view that gold is likely to continue to increase against all currencies, only less so against the dollar if the global system continues to deflate. And by the way, we think that process could accelerate once it becomes apparent to the markets that the Obama stimulus programs are totally ineffective in stemming the deflationary tide.