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800 Dollars an Ounce? That's Where Gold Prices Could Head

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A much maligned study last year by several economists is now seemingly prophetic in regards to gold prices. Gold bugs and contrarians that push that metal were quick to dismiss the study out of hand, saying that the unlimited QE and economic factors would keep the gold rally strong. Now with the rapid descent into a bear market, it has ETF investors along with some investors that bought physical at its peak searching for the exit.

Contrarian investors, the normal gold bugs you see on tv see this as a great buying opportunity. Also the way in which gold has collapsed could be indicative of something broader in the equity market. One such collapse happened just before the Lehman crisis and another before the Jackson Hole, WY meeting which essentially stick saved the stock market. So while it looks terrible out there for gold buyers, it could be setting up to just jump higher on an unknown equity market event, be it the unwinding of QE or something external.

The authors of the report say that right now gold buyers are in the first stage of the famous 5-stages of grief, denial. Inside the report they account for under-reported inflation which may justify higher valuations. They tie the average ratio of inflation to CPI and show a 3.2-1. Right now, gold stands at 6.03-1, even after its tumble below $1400. This is where they get the implied value of near $800 per ounce. The economist that took part in the study also served as a commodities manager once and heavily invested in gold, so there isn't a predisposed bias.

Their view is that gold is disconnected in a major way from its fair value, and as history has shown, it always returns to it.

While ETF or paper gold buyers may be getting hit, a return to $800 per ounce may not be a bad thing for physical buyers. Their rationale for holding physical is wholly different than the average ETF trader. They are looking for a store of value longterm against what they perceive will be an eventual downfall of fiat currencies. The ETF investor is a bandwagon jumper looking to move to one hot sector to the next search for returns.

Time will tell what happens in the gold market, but right now it looks as if the bears have firmly grabbed the market and are at times crashing it downward.

Tags: gold bear market gold prices

Cliff Moore

An old school financial journalist, Cliff Moore brings that old-hat experience to Trade the Newsroom. He specializes in political coverage and focuses his attention on the gyrations coming out of the world's central banks and their impact on the bond and equity markets.

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