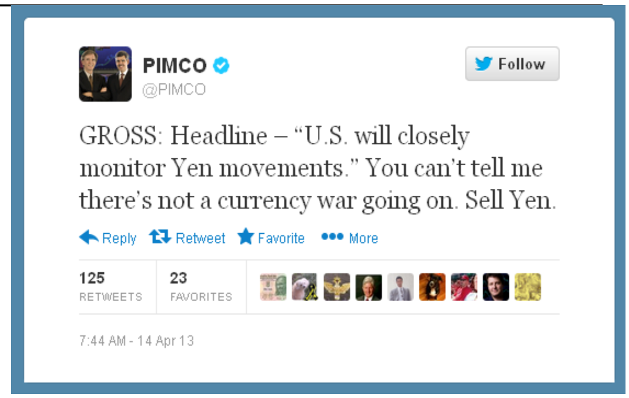
# The end of the run?

*Gold Comment—$1350*

Anybody remember Andy Smith? We do. Mr. Smith was the irreverent analyst at Mitsui Metals who, a decade or so ago, into and through the trough of the bear market, held the position that all the gold in all the central banks would get dumped into the open market by next Tuesday. On the heels of this, those crazy Indians will get wise, grow up, and liquidate their gold stocks in favour of money-in-the-bank, which is where money always belonged in the first place. This was an era when good central banking meant portfolio optimization, the US dollar traded like a work of art, and Alan Greenspan chaired the Fed. Mr. Smith was (and presumably still is) English; he wrote very well. And for a long time, he was right. Central banks did cough up their metal, all chased down by an enthusiastic dealer community. This all happened back in the $250-$300 days.




***A Pimco tweet from over the week-end: Sell Yen and, … buy what?***

Now we hear this is going to happen all over again starting with, …, Cyprus! Behind this country's 14mt is an additional 3000mt (+/-) from other European deadbeats. And if the ECB can shakedown Cyprus for its 14mt, what's to stop it from doing the same with the other European deadbeats? Sell now, sell often!

The Cyprus news hit the market at a sensitive time, with the metal's *raison d'etre* brought into question. The Fed has been printing with abandon *forever* and all the gold market had done of late was yawn, as though gripped by a bad case of *ennui*. If gold doesn't seem to care about this, then why should anyone else? If gold can't/won't move now, when the rate of money creation would swamp the value of all the gold ever mined in a few short years, then when will it ever move? Obviously, the investment was no longer "working", as it were. Besides, what gold equity portfolio wasn't cut by two-thirds? Who isn't tired of the scene, the rhetoric and that cast of characters? Now that it is the S&P making headlines, things apparently back to normal, who needs it? This seems to have been the mood, ripe for a nudge.

And a nudge it got. Here we are at $1360/oz, down 10% on the day and off 30% from the highs of 2011. "The End of the Gold Era!" headlined one report. Really?

This sharp correction is taking place in a macro-environment that has never been more supportive for gold nor more obvious to its observers. The US fiscal situation beggars belief. A trillion per year deficit, much of this for debt service, with debt service costs at 50 year lows. Any rise in rates would only be fuel on the fire, so that won't happen. The Fed is pumping $100b/month to ensure as much. More brazen yet are the Japanese. It is less the additional $50b/month that they are pumping into their system, and more the forthright manner in which they are doing it: "We're devaluing. Whatcha going to

Pollitt & Co. Inc.
11 King Street West, Suite 1950, Toronto, ON. Tel: 416.365.3313
625 Boulevard René Lévesque Ouest, Bureau 930, Montréal, QC. Tel: 514.395.8910

do about it?" Bill Gross of Pimco tweeted over the week-end: "Sell Yen." Ok - *and buy what?* What currency is not being adulterated to oblivion? The forces that drove gold from $250/oz to $1500/oz+ haven't gone away and nor, then, has the secular bullish trend in gold. This is what is more properly known as a shake-out.

But before we turn around, it is fair to ask: How low could it go? Of course, we don't know. There have been comparisons made to the 50% retrenchment back in 1976, when the metal retreated from $200 back to $100. At the time, equity markets had recently recovered from the '73-74 bear market and the euphoria of liberalized US ownership laws was starting to fade. Murray (of the firm's namesake) got down to one contract and a barren apartment in midtown. It was the time of the Montreal Olympics. We remember it well.

We don't see $1000 in the cards, as apt as the comparison to 1976 may be. A $1000/oz handle today is far worse, from the perspective of primary production, than $100 thirty-five years ago, when so much more of production came from deep-level South African mines. Squeals from miners, or sell-side stress tests blinking red, would provide a powerful corrective signal. We feel this would start in earnest at around $1300/oz, for whatever that is worth.

If we can't predict the sharpness of the pullback, we do feel more comfortable in saying that the sharper it is, the shorter it will be, and this has been very sharp indeed. Certainly, the necessary ingredients for a secular bear market in gold are entirely absent. Rates are not going up. Long term primary supply is anemic at best. Monetary authorities have indicated, if not by word then by deed, that they intend to destroy the system as we know it. Never has a set-up been so attractive. We hear other commentators agree with these views, but only from the perspective of "the long term." Isn't the "long term" happening right now?

The last time the spectre of central bank selling swept the market the context was entirely different. Cyprus is not considering selling the metal because it is a "zero-yield deadweight" in a portfolio (*as per* Smith a decade ago) but rather because it has been the only asset to survive a decade of train-wreck decisions by the very same policy makers so-feted back in the day. Put differently, the country's gold is the only thing left to sell. The investment served its purpose to a 'T', a lesson that will not be lost on them nor other candidate central banks.

Once this brush-clearing exercise has run its course, we don't think this lesson will be lost on the broader market either.

**Douglas Pollitt**
dpollitt@pollitt.com

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