게재확정일자 : 2006. 03. 10

Global Gold Decoupling from the Dollar and Its implications*

Dae-Seok Chae
Dongguk University
Hyung-Doh Hur
Dongguk University

Contents

Abstract

Gold prices are rising around the world in all major currencies. This is a telltale sign of a Stage Two gold bull where gold decouples from the US dollar. In this study, We analysed a confluence of factors seem to be feeding gold's gains and the typical shape of a secular gold bull---gold bulls' three stages.

Stages one, two, and three of a secular gold bull are defined by the major changes. Each stage, considered in turn, makes perfect sense when described in terms of global investor demand. Since Stage One is currency-devaluation driven, the young gold bull is most noticeable in terms of the dominant eroding currency. Now after three or four years of stage one, Stage Two arrives. Stage Two marks a momentous event when gold decouples from the local-currency devaluation.

In the case of our gold bull today, Stage Two will be here when gold starts consistently rising faster than the dollar is able to fall. After five or so years of Stage Two gains, gold has a chance at going ballistic in stage three. Stage Three is only ignited if the general public around the world starts growing enamored with gold investing.

In summary, the first stage being when insiders and professionals invest in the market. The second stage is when the general public and financial media recognizes that the bull market is real. The third stage is the mania stage when people feel that not only is the bull market real, but it is a must own situation. Through the study we found that gold is entering it now.

Key Words : Gold Bull Market, Gold Bulls Three Stages.

* This is supported by the research program of Dongguk University

Ⅰ. Introduction

Gold prices are rising around the world in all major currencies. On December 12, 2005, gold surged to a $541.80/oz, the highest level for the precious metal since March 1981, when gold fixed at a high of $547.25/oz. This is a telltale sign of a gold bull where gold decouples from the dollar. Investors traditionally pile into gold as a safe haven when the dollar drops, inflation rises and economic calamity looms. Today, price dynamics in gold largely is determining by speculative interest or investment demand, backed by a myriad of justifications like inflationary risks, energy price led economic slowdown, expectations of a US dollar correction, soaring physical demand, supply-side contraints, hopes of large scale central bank buying and so on.

In this paper, we will analysize a confluence the factors seem to be feeding gold's gains or gold bull market. Moreover, secular gold bull have three distinct stages driven by growing investor demand. We will examine these stages and their implications for today's gold bull.

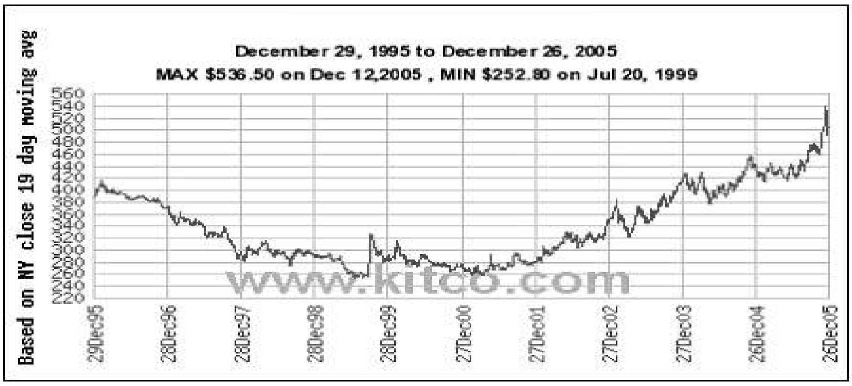
Ⅱ. Global gold bull and the main reasons

The price of gold rose above the psychological level of $500 an ounce for the first time since 1987, extending a rally that has defied market tradition and perplexed some traders and money managers. As the chart 1 shows, gold is going to keep going up, the metal reached a 24-year high on December 12, 2005.

Chart Ⅱ-1. Gold price, $ per ounce (London fix)

Source : World Gold Council, 2005.

Chart Ⅱ-2. 10 year gold ($USD)

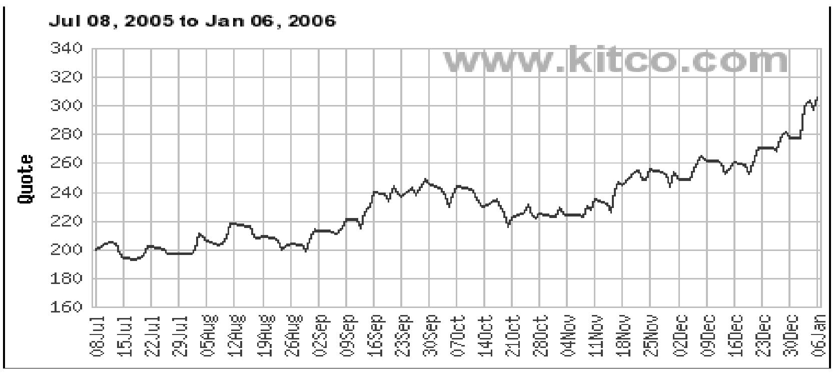


Source : Kitco, 2005.

Our above chart 2 shows, gold prices have been moving higher for nearly five years, but a big acceleration has come in recent months. On December 12, 2005, price shot above $540 on ounce during the day's trading, the highest level since 1981. Due to some profit taking, gold is now trading around $500 an ounce, still up around 20 percent for the year.

That run-up has also given a big lift to a gold-related stocks including producers New mont Mining Corp. and Placer Dome One, which have both seen double-digit gains this year. Contrast that with what the stock market has done since the start of 2005; The Dow Jones industrial average has gained just shy of 1 percent; while the Standard & Poor's 500 stock index is up about 5 percent since early January, 2005[1]. Our next chart 3 contains this trend.

Chart Ⅱ-3. 6 Month HUI Index



Source : Kitco, January 03, 2005
HUI(AME GOLD BUGS Index) is comprised of 15 of the largest unheadged gold mining stocks.

1) Contracosta Times, December 21, 2005.

The bull market in gold is certainly generating a lot of contending opinions. We look at the case for a gold bull. Not surprisingly, while the raw price data is absolutely indisputable, there are a myriad of varying opinions on whether gold is going higher or lower and why.

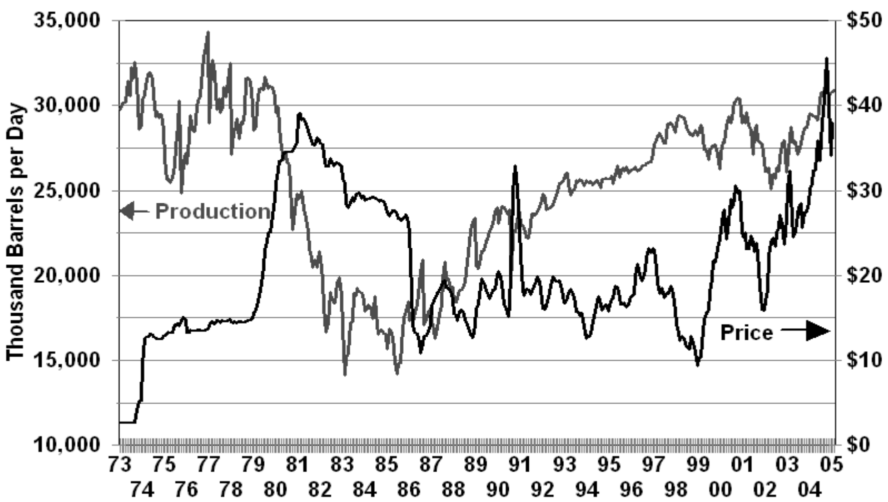
Our gold world view is long-term bullish as we believe gold is going higher, and is in a massive secular bull market that ought to gallop higher for many more years, perhaps a decade, before it fully runs its course. Why do we believe gold is in a bull market likely to run for many years yet? We will briefly outline the major reasons.

A confluence of factors seen to be feeding this gold's gains.

(1), To start, concerns about rising inflation due to higher energy costs have contributed to the rally. Gold is considered a "safe haven" investment during uncertain economic or political times. As more and more investors perceive the dire threat of inflation to their families' futures, they will naturally migrate into gold. Inflation is a diabolical and immoral stealth tax imposed on the populaces.

Chart Ⅱ-4. Crude Oil Production(Mbbl/d)

OPEC Countries



Source : Wtrg, 2005.

From the chart 1 and 4, we can fined the similarity of the price cycle of the both. Gold increases have happened during a time when the oil have risen. Thus, the market will realize that we've entered an inflationary recession(a.k.a stagflation) as the 1970s, and they'll start buying gold as an inflation hedge.

(2) Gold supplies also appear to be dwindling. For instance, output from three of the largest producing nations --- South Africa, Australia and the United States--- fell 20 percent from 2000 to 2004, according to

Credit Suisse Boston.[2)]

Gold is unusual in that it is both a commodity and a monetary asset. Because it is virtually indistructible, all the gold that has even been mined still exists above ground in some form or another and, theoretically, the majority of above-ground stocks could easily the mobilized. that is to say that they are in simple, relatively unfabricated form. As us result of this feature, any upward spike in price is often met by the resale of above-ground stock and this is one of the reasons why the gold price is historically less volatile than the majority of other commodity prices. It also explains why gold's forward markets are generally(but not always) orderly. As table 1 shows, total gold supply for 2004, was a 14% decrease. all categories of supply were lower than a year earlier. There was a 12% decreases in total mine supply in comparison to the same period a year earlier, but the principal cause was a higher reduction pace of de-hedging by mining companies.

Table 1. World gold supply and demand

tonnes	2002	2003	2004	% ch 2004 vs 2003
Supply				
Mine production	2,589	2,593	2,461	-5
Net producer hedging	-412	-270	-427	...
Total Mine supply	2,177	2,322	2,035	-12
Official sector sales[2]	545	617	475	-23
Old gold scrap	835	939	829	-12
Total Supply	3,557	3,879	3,338	-14
Demand				
Fabrication				
Jewellery	2,656	2,477	2,613	5
Industrial & dental	357	380	409	8
Sub-total above fabrication	3,013	2,857	3,022	6
Bar & coin retail investment[3]	387	310	391	26
Other retail investment	-48	-18	-49	...
ETFs & similar[4]	3	39	133	237
Total Demand	3,355	3,188	3,498	10
Balance[5]	202	691	-160	...
London PM fix (US$/oz)	309.68	363.32	409.17	12.6%

Source : GFMS Ltd. The data are consistent with supply and demand data published by GFMS Ltd but adapted to the WGC's presentation. 1. Provisional. 2. Excluding any delta hedging of central bank options. 3. Jewellery data are on a fabrication basis and quarterly data differ from consumption data shown in end-use gold consumption. 4. Exchange Traded Funds and similar. 5. This is the residual from combining all of the other data in the table. It includes institutional investment (other than ETFs), stock movement and other elements as well as any residual error.

2) Ibid.

Table 2. End-use gold consumpti

Tonnes	2003	2004	Q1'04	Q2'04	Q3'04	Q4'04	Q1'05	Q2'05	Q3'05[2]	% ch Q3'05 vs Q3'04	% ch ytd '05 vs ytd '04
Jewellery consumption	2,477	2,613	575	636	603	798	685	728	613	*2*	*12*
Industrial & dental	380	409	101	109	101	99	98	111	107	*6*	*2*
Electronics	233	259	65	70	64	61	61	72	70	*11*	*2*
Other industrial	80	83	19	22	20	22	22	24	20	*-1*	*7*
Dentistry	67	68	17	17	17	17	15	16	16	*-3*	*-6*
Identifiable investment	331	475	100	91	75	209	206	106	118	*56*	*62*
Retail investment	292	343	83	86	77	96	118	108	80	*3*	*24*
Bar hoarding	178	248	58	67	58	66	80	81	53	*-9*	*17*
Official coin	107	114	35	29	25	25	39	30	26	*3*	*6*
Medals/imitation coin	25	29	6	7	8	8	10	10	9	*9*	*35*
Other identified retail invest.[3]	-18	-49	-16	-16	-14	-3	-11	-13	-7	...	...
ETFs & similar products[4]	39	133	16	5	-2	113	89	-2	38	...	...
Total end-user consumption	3,188	3,498	776	836	779	1,107	989	946	838	*7*	*16*
London pm fix, $/oz	363.32	409.17	408.44	393.27	401.30	433.80	427.35	427.39	439.72	*10*	*8*

$m	2003	2004	Q1'04	Q2'04	Q3'04	Q4'04	Q1'05	Q2'05	Q3'05[2]	% ch Q3'05 vs Q3'04	% ch ytd '05 vs ytd '04
Jewellery consumption	28,937	34,374	7,556	8,039	7,786	11,134	9,407	10,008	8,673	11	20
Industrial & dental	4,437	5,385	1,324	1,373	1,299	1,384	1,344	1,532	1,509	16	10
Electronics	2,722	3,408	850	885	823	845	834	984	996	21	10
Other industrial	933	1,086	250	273	259	304	299	325	281	9	16
Dentistry	782	891	224	215	217	235	211	223	232	7	2
Identifiable investment	3,867	6,253	1,309	1,153	971	2,918	2,836	1,456	1,661	71	73
Retail investment[5]	3,407	4,508	1,093	1,092	997	1,336	1,620	1,478	1,131	13	33
ETFs & similar products	460	1,745	215	61	-26	1,582	1,217	-22	531	...	589
Total end-user consumption	37,241	46,012	10,189	10,566	10,056	15,435	13,588	12,996	11,844	18	25

Source : GFMS Ltd. 1. Identifiable end-use consumption excluding central banks. 2. Provisional. 3. “Other retail” excludes bar and primary coin offtake; it represents mainly activity in North America and Western Europe. 4. Exchange Traded Funds and similar products including LyxOR Gold Bullion Securities, Gold Bullion Securities (Australia), streetTRACKS Gold Shares, NewGold Gold Debentures, We will analyze about the long-term supply trend and production cycles at the continuing chapter.

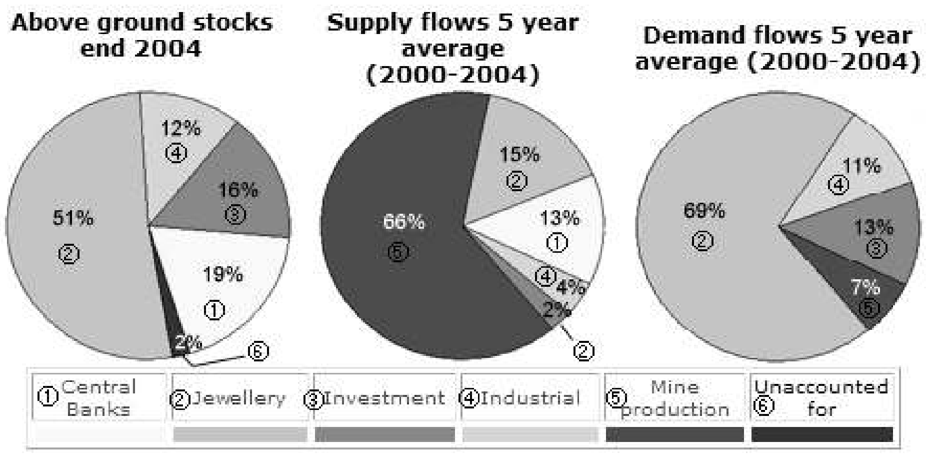
(3) At the same time, as table 1 shows demand for gold is also cleanly accelerating.

① While central banks have been net sellers of gold for much of the past two decades, there are indications that some, including those in Russia, Argentina and South Africa, plan to increase the gold portion of their reserve s[3]. Officials in these countries have all said that they may increase their gold reserves[4].

② Also up sharply 2005 is demand for gold jewelry, which accounts for about three-quarters of global demand .

In fact, global jewelry consumption --- led by big gains in India and China, thanks to their rapidly expanding economies --- increased nearly 12 percent for the first nine months of 2005, according to the World Gold Council. Our chart 5 shows, on the demand side, jewellery has been the largest component of demand. The demand flows shown in the diagram to the right are based on fabrication demand, which differs slightly from the consumption demand data. Jewellery fabrication demand for a given year, for instance, would tell you how much gold was used in jewellery manufacturing during that period, whereas consumption demand would tell you the gold content of all gold jewellery reported as having been sold that year.

Chart 5. Gold supply and demand



source : GFMS Ltd

Over the 12 months to June, the dollar value of jewellery demand reached record levels at an annual rate of over US$38billion, exceeding, for the first time, the peak levels of 1997(chart 6).

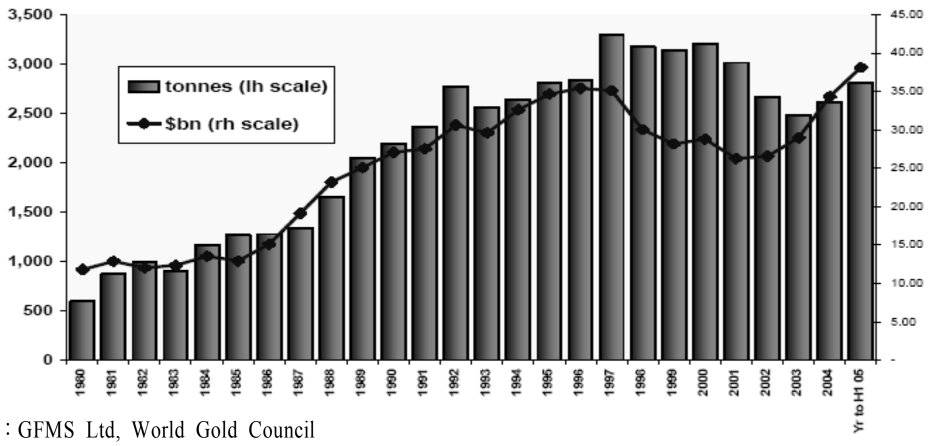
3) Conrad Bud, Gold's Crazy Action in the Week of 12/16/05, Kitcocasey, December 19, 2005.
4) Washington Post, November 30, 2005.

The strong growth in demand for gold jewellery continued in the Q3'05 with a rise of 2% in tonnage and 11% in value(Table 2).

Good economic growth and sustained promotion of gold jewellery in key markets continued to drive demand but the sharper rise in the gold price during the second half of September started to deter buying in some regions.

Nevertheless, with a 10% price rise, even the modest 2% increase in tonnage terms produce a substantial 11% increase in dollar terms in the demand for gold jewellery. Demand in the twelve months to September 2005 reached $39.2bn, exceeding the previous record set in the 12 months to June 2005.

Chart 6. Jewellery demand in tonnes and $



Source : GFMS Ltd, World Gold Council

③ Gold prices have also gotten a big jolt from the sharp increase in investment and speculative demand. Not only are investors buying gold outright --- bars of gold as well as coins --- but there has been huge surge in interest and commodities funds.

The third quarter of 2005 witnessed a 56% year-on-year growth in net investment demand for gold. Retail investment was 3% higher in tonnage terms than the same period in 2004 as continued interest in gold purchasing was offset by some selling back by investors to take advantage of higher gold prices.(Table 2)

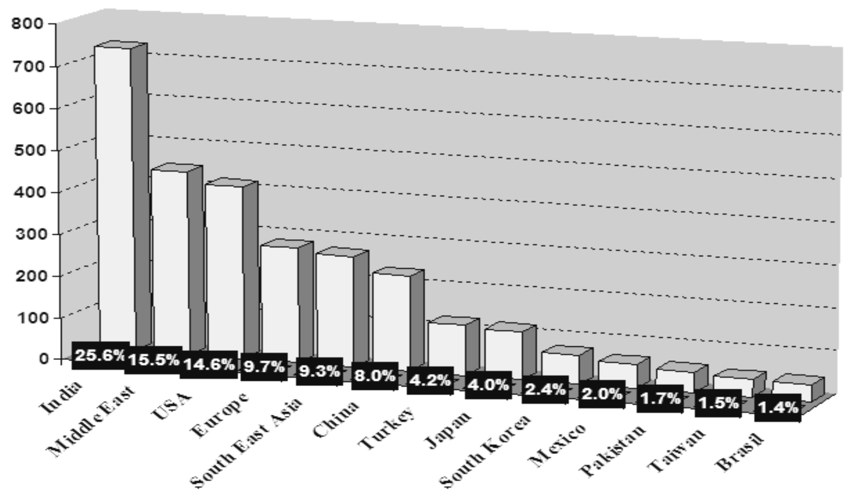
Exchange Traded Funds(ETFs)[5] and similar products grew throughout the third quarter, rising by 38 tonnes. The bulk of net buying was seen in streetTRACKS Gold Shares which is Quoted on the New York Stock Exchange(GLD), with additional buying in Barclays iShares Comex Gold Trust and the London listed LyxOR Gold Bullion Securities. Investments in ETFs and similar products in the first weeks of the fourth quarter have continued to grow, and with the recent listing of LyxOR GBS on Euronext, this trend is expected to continue.

5) ETFs use investors' money to buy gold bullion.

Other institutional investment demand appears to have risen sharply in September due to fears of rising inflation and the political shock. The rise in price itself, as well as data confirming the strength of demand in the first half of 2005, encouraged further interest in gold.

④ One of the most popular is that oil-rich countries in the Middle East are using gold as a new place to park some of their vast energy profits. Middle East, which has been the third largest gold consumer eating up over 15.5% of the gold world annual demand by itself, enjoys the windfall of oil price.

Chart 7. Geographical market demand breakdown :



Source : World Gold Council, 2005.

⑤ Central banks in Asia and elsewhere are diversifying foreign reserves by moving money out of U.S. Treasuries and into gold. Chinese, Taiwanese, and Japanese Central Banks now want to increase the percentage of their gold reserves, to protect themselves against having too many dollars or euro reserves.

⑥ The third quarter was a strong quarter for industrial demand in gold. An upturn in electronics demand was responsible for 6% year-on-year growth in tonnage terms (16% in dollar terms) in industrial and dental demand, following a first-half year that was essentially flat. Electronics demand itself rose 11% year-on-year. The primary reason for the strong electronics demand figures was the exhaustion of the high inventory levels seen at the beginning of the year.(Table2)

A particularly large rise in electronics demand was seen in Japan, where offtake jumped 23%. This reflected healthy sales of consumer electronics and semi-conductors, signalling a need for manufacturers to prepare for the seasonally high fourth quarter.

Ⅲ. Gold's supply and demand imbalance, and production cycles

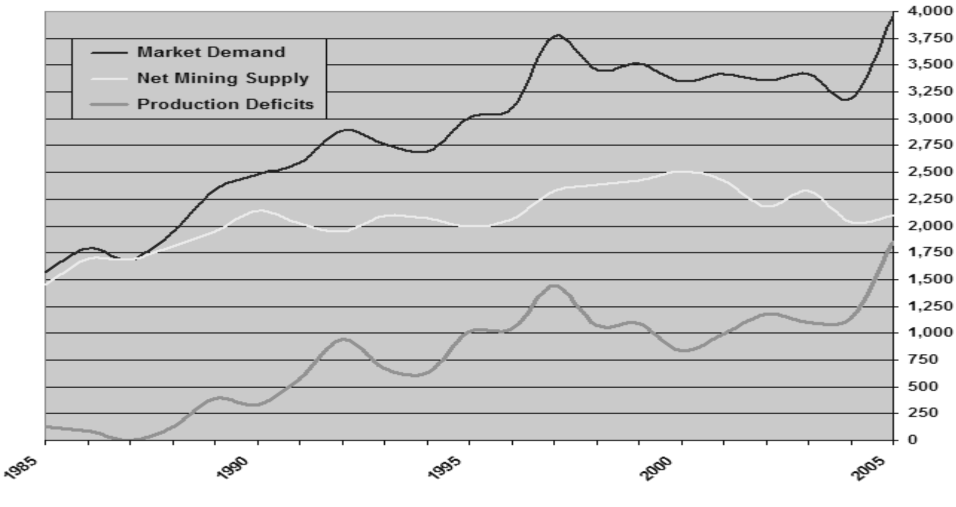
1. Supply does not satisfied demand.

The chart 8 below shows annual market demand compared to mining production, and the resulting annual gold production deficits from 1985 to 2005. During the last 20 years, mining production has only satisfied an ever decreasing part of the market demand. The trend has now started to worsen, as overall demand is on a sharp rise again, with Bullion Banks having to start covering their short gold positions to repay central banks.

According to statistics from the World Gold Council, and GMFS[6], world demand for gold increases 15.96% in the First3 Quarters of 2005 compared to the same period in 2004(2,772 tonnage vs 2391). At the same time, gold production declined by 114 tonnage in 2004, the greatest annual fall in tonnage terms since WWⅡ. In 2005, South Africa, the largest gold producing country is reporting a 7% decline in it's gold production.

Although total annual gold production has gone up from 1,500 tonnage in the late 1970's to 2,500 tonnage in year 2000, market demand for gold has increased faster than mining output was even able to deliver during the last 20 years. Additionally, with gold mining operations nearing the end of their lives and reduction in exploration and development expenditure over the past years analysts suggest that global production is likely drop further over the next few years.

Chart 8. Gold's market demand and net mining supply



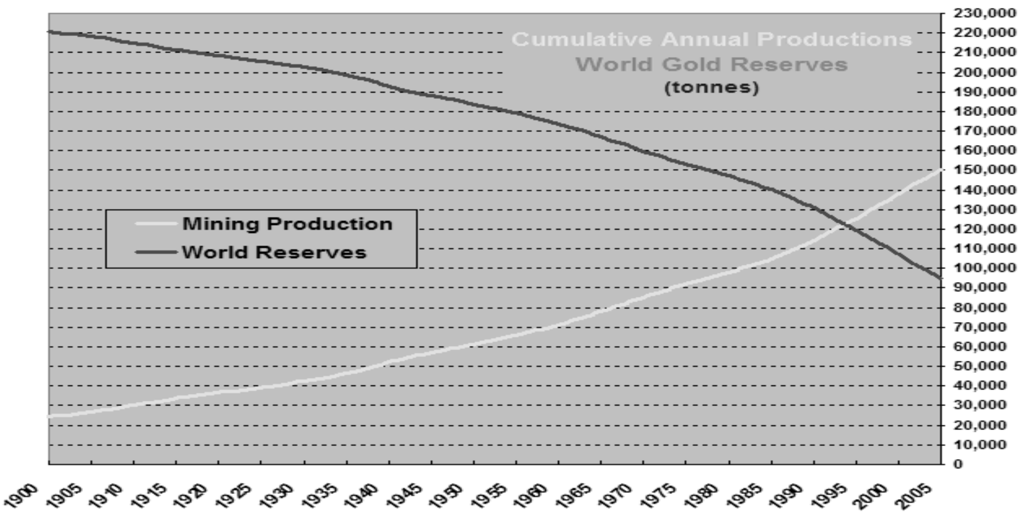
Source : Anygoldnow, 2005

6) Anygoldnow, 2005

Recent and future higher gold prices are expected to entice exploration companies into investing exploration again. However, should they be successful, it will take another 5 years after new gold discoveries will be made before additional production output could kick in, because of the huge financing/work involved in starting new gold mine operations.

The chart 9 below shows that the amount of gold that has ever been produced(mined) is now much larger than the world gold(unmined) reserves. At current annual demand rates(about 3,000 tonnage), world gold reserves[7] will dry out completely in about 25 years. 84% of the gold ever produced by humanity has been mined since 1900. 60% of the gold ever produced has been mined since 1950, at an accelerating pace.

Chart 9. Gold mining / reserves



Source : Anygoldnow, 2005

2. The cycles of production of the gold

We have to warn the reader that there are two types of figures on this chart. From 1840 untill 1900, the world golden production is given in million francs and after 1900, it is given in tonnes of gold, but it changes nothing this study. We do not use the technical analysis because We don’t want to mix the various works. We just wish to highlight the cycles of production of the gold which seem very regular[8].

1) Regular cycles of the golden production

For 164 years, the golden production has regular cycles between bottom and heights.

7) Monetary gold stocks, producers' investories, processors' inventories, stocks of holders for profit or safety.
8) Dani 2989, August, 2004.

(1) Tops.-the last four cycles :

There are four summits of production of the gold in the world, on 1845, 1915, 1942, on 1970 and 2001. Here is their length :
1870-1915 = 45 years
1915-1942 = 27 years
1942-1970 = 28 years
1970-2001 = 31 years
If we look at the average of these four cycles is of 32.75 years between every summit of cycle.
In 2001, the production seems to have marked a summit with 2600 tonnes of golden production. The cycle since the previous summit of 1970 is of 31 years, while three previous cycles are of 33.3 years.

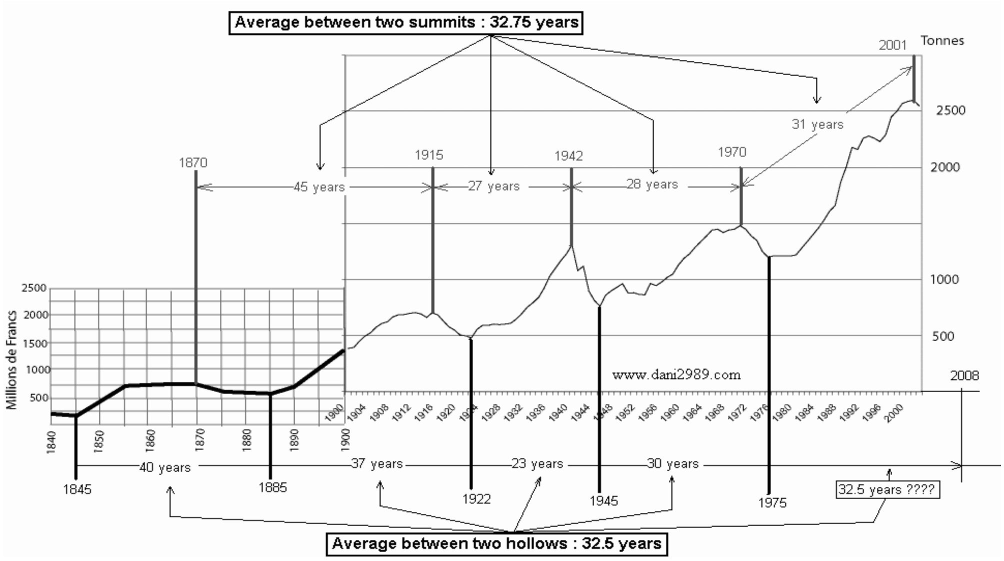
(2) The hollows of production of the gold.

The last four cycles : There are four hollows of production of the gold since 1840 : 1845, 1885, 1922, on 1945 and 1975.
Here is their length :
1845-1885 = 40 years
1885-1922 = 37 years
1922-1945 = 23 years
1945-1975 = 30 years
If we look, the average of these four cycles is of 32.5 years between every hollow of cycle. In 1975, the production marked a hollow of 1200 tonnes of golden production. The cycle since the previous hollows is 30 years. When will take place the next hollow? If one account 32.5 the years since 1975, it indicates a hollow of production in 2008.

(3) Hollows and summits of production of the gold are regular.

Summits arrive every 32.75 years and hollows every 32.5 years. It is surprising to see how every hollow and every summit are spaced out by the same number of years. Even the less precise figures from 1840 till 1900 go to the same direction.

Chart 10. World production gold



Source : Dani 2989, August, 2004.

2) The decline of production of the gold.

Have the periods of declines of the production resemblances?

A) That it is the amplitude of the declines of the production of the gold?

That it is the amplitude of decline between a summit and a following hollow?

1870-1885 = 200 million francs of decline = 26.7 % of decline

1915-1922 = 223 tons of gold = 31.7 % of decline

1942-1945 = 358 tons of gold = 32 % of decline

1970-1975 = 280 tons of gold = 18.9 % of decline

If we make the average of all these declines : 27.3

A decline is on average 27.3 % of the increase which precedes it.

B) That it is the amplitude of the declines of production of the gold in the time?

How long lasts a decline after a summit?

1870-1885 = 15 years of decline

1915-1922 = 7 years of decline

1942-1945 = 3 years of decline

1970-1975 = 5 years of decline

The average of these four declines is of 7.5 years.

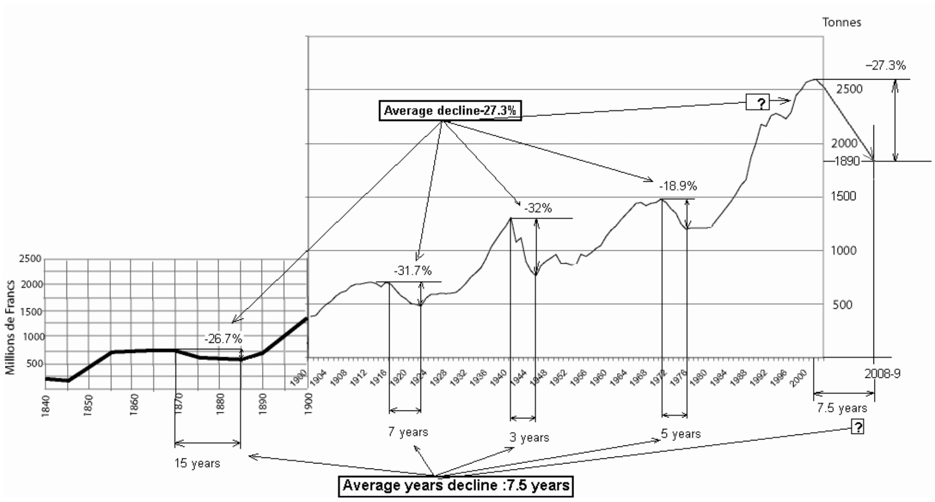
Four cycles of decline of production of the gold lasted on average 7.5 years.

C) If 2001 is a summit?

If 2001 is a summit and what we apply these statistics, here is what it gives :

In 2001, the golden production was 2600 tonnes of gold. If we shield the average of the previous declines of 27.3 % production, the next hollow of production is 1890 tonnes of gold (look at the arrow on the graph). The average of the last four declines of production is of 7.5 years. If we add it at the top of 2001 we obtain 2008-2009. The projection of the statistics of the previous cycles of decline of the gold gives a decline of the 1890 tonnes production for 2009.

Chart 11. World production gold



Source : Identical with Chart 10.

3) Explanation.

It is possible to make a certain number of remarks about these cycles of production of the gold.

Summit of 1870 = dates the French-German war and there is a decline of the production of the old gold-bearing discoveries of the middle of the 19th.

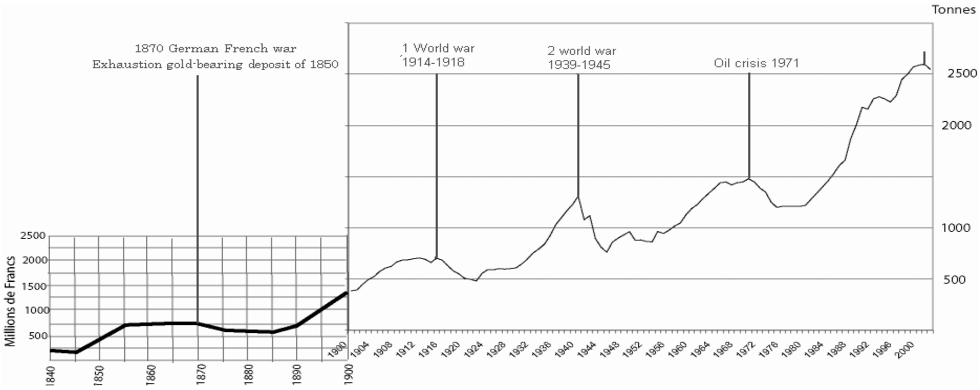
Summit of 1915 = dates the First World War.

Summit of 1945 = dates the Second World War.

Summit of 1971 = it is the oil crisis.

Summit of 2001 = the decline of the investment and of the investigation.

Chart 12. World production gold



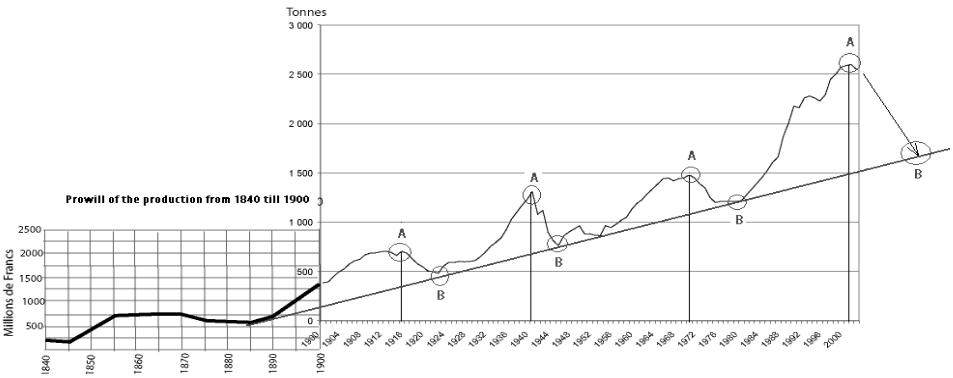
Source : Identical with Chart 10.

For summary, we can say that if the cycles apply as previous cycles, it is possible that in 2008-2009, the golden production falls to 1890 tonnes, what implies a price increase of the gold because the demand it does not seem to want to fall. In this analysis of the golden production, it is just question of the cycles and the figures.

4) An old support.

There is a right-hand side of tendency which exists since the beginning of the century. It serves as support for every important hollow. Every time the production marks a called major summit A, it returns to get touch her support the point B some years later. The right-hand side of tendency works for 100 years, is it going to continue? If the production joins the right-hand side, it gives an objective in the zone of the 1650 tonnes of gold a year.

Chart 13. World production gold



Source : Identical with Chart 10.

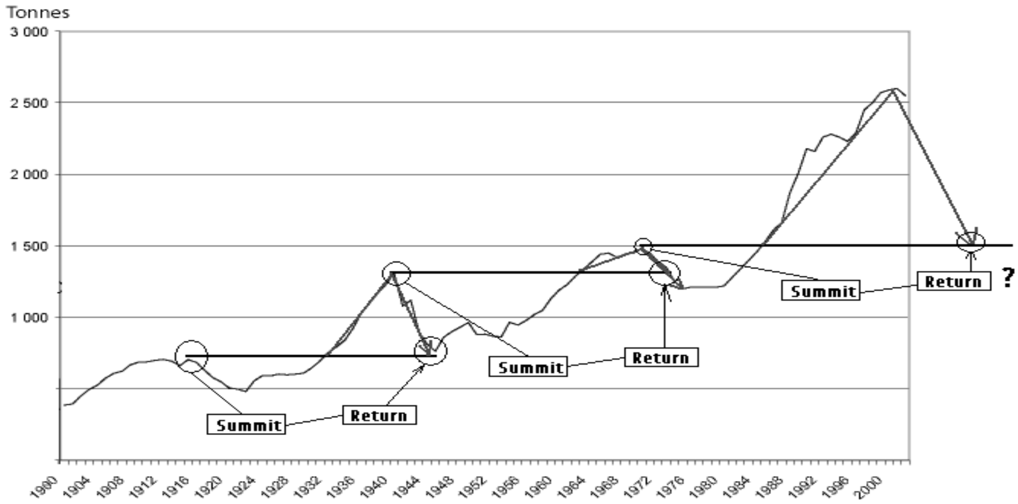
5) Hollows and summits.

It is interesting to observe that further to every major summit the golden production returns at the level of its previous summit.

After every major increase, the minimum objective is the previous summit, it worked during every cycle of decline and increase from 1900 till 2000.

If this method works, an objective of 1500 tonnes must be reached, this corresponds at the top of 1970.

Chart 14. World production gold



Source：Identical with Chart 10.

Ⅳ. Gold bulls' three stages and gold's decoupling from the dollar

1. Gold bulls' three stages

Secular gold bulls have three distinct stages driven by growing investor demand. We examine these stages and their implication for today's gold bull. The word secular, which has a dictionary definition of "going on from age to age", is used to describe any major market trend that runs for a long period of time.

The Great Gold Bull of the 1970s, for example, ran from 1970 to early 1980 exactly one decade. While gold did not rise in every single year, when you look at a long-term chart, this secular bull market is utterly unmistakable.

In this study, the absolute minimum amount of time necessary for a trend to attain secular status is three years. If any trend runs for less than three years, then it should be considered cyclical instead of secular. Thus it is pointless to even think in secular terms until a trend has been fire-tested and battle-proven for at least three years.[9)]

From april 2001 to the end of 2005, the requisite three-year minimum necessary to catapult gold's current bull market into the ranks of seculardom, gold has soared higher. Since we are already four years into gold's present bull, We have to start thinking in secular terms. Only then we can begin to understand what wonders might lay ahead for gold.

Now naturally the tools used to analyze a strategic bull are far different from those used to speculate on short-term tactical trends oscillating with in the primary secular trends. While various technical tools are crucial for short-term tactical seculation, long-term analysis is exclusively dependent on fundamentals.

The most foundational of all the fundamentals is supply and supply. As long as demand exceeds supply, prices will be forced to rise over the long term. Higher gold prices lead to higher supplies of gold as miners around the world rush to capitalize on the increased profit margins in their product.

Finding new gold deposits that are large enough to mine is exceedingly difficult, and ever once they are discovered it takes years to dig shafts and spin a new mine up to operational speed. For this reason, historically the total global gold supply only grows by an average of a couple percent or so each year. Faster growth is impossible at almost any gold price due to the extreme difficulty to bring new gold deposits to market.[10)]

Thus, on the gold production end supplies are very inelastic to price. Regardless of how high the gold price goes there will be not be a flood of newly mined gold as ramping up global gold production fast is simply not viable. But there is another potential supply of gold beyond mining, which comes from investors choosing to sell gold that they have preciously purchased.

Since gold is rarely destroyed, virtually all the gold ever mined still exists in various forms today, from bars sitting in secure vaults to jewelry adoring women around the world. Investors who own this gold can generally be divided into two distinct groups with vastly different motivations, official central banks and private investors. As these investors choose to sell their gold, it can cause additional supply to come onto the markets at various times.

Central banks rightfully see gold, the ultimate over the human history, as a threat to their fragile fiat-paper currencies, so they tend to act irrationally. Rather than buying low and selling high like a private investor, central banks buy and sell at the wrong times. Central banks tend to exacerbate secular trends.[11)]

At the end of long gold bears central banks wrongly assume that gold is finally becoming worthless so they

9) Hamtilton Adam, Gold's bull's three stages, Zeaillc, 2004.
10) Gold sheetlinks.com/prodution.
11) Ware Dick, The IMF and Gold, Research Study 26, World Gold Council, May 2001.

sell and drive the bear lower. At the end of long gold bulls they worry that their particular fiat paper does not have enough gold backing so they buy and force the bull higher. If the goofy bureaucrats who ran central banks had to trade for a living they would soon go broke by selling low and buying high.

But, during all of world history, and only about 20%, or 30,000 tonnage, is controlled by various central banks today. While 20% is certainly not trivial, it is the private investors that control the other 80% that really hold gold's destiny in their hands.

Since newly mined gold can only grow total world supplies by a couple percent a year at best, and central banks only control 20% of the above-ground gold and tend to buy and sell at exactly the wrong times lengthening secular trends, the real force to be reckoned with in the gold world is private investors. It is to these private investors, people around the world like you and I, that we must look to understand secular gold bulls.[12)]

The key to a secular gold bull is the demand or supply that private investors generate worldwide as they, buy or sell gold. It isn't mining supplies, it's not central banks, but it is the collective gold transactions of hundreds of millions or even billions of individual investors worldwide buying and selling gold that ultimately sets its price and determines its fortunes.

Whether we are talking about computers, pizza, cars, whatever, the lower the price the higher the demand grows for a particular product. This is a normal downward-sloping demand curve. But with gold, and indeed most other investments, the demand curve is far from normal. As all contrarians know, in the investment world the higher the price of an investment climbs the greater demand becomes. It is all backwards. In the financial world higher prices don't retard demand, instead they actually breed demand!

The higher the price of gold climbs, the more potential investors will become aware of its impressive returns. As they buy in over time, the marginal investment demand will drive gold even higher, putting it on the radar of even more investors worldwide. This investor demand creates a wonderful virtuous circle, with higher gold prices leading to more interest and higher demand which in turn leads back to higher gold prices and feeds the cycle.[13)]

And remember that private investors collectively control 80% of the world's gold, so if demand is growing in this realm it is almost irrelevant what the mines can pull or what nefarious machinations the central banks happen to be up to.

The whole secular gold game unfolds in terms of private investor demand for gold, as we are collectively the dominating force in the gold market.

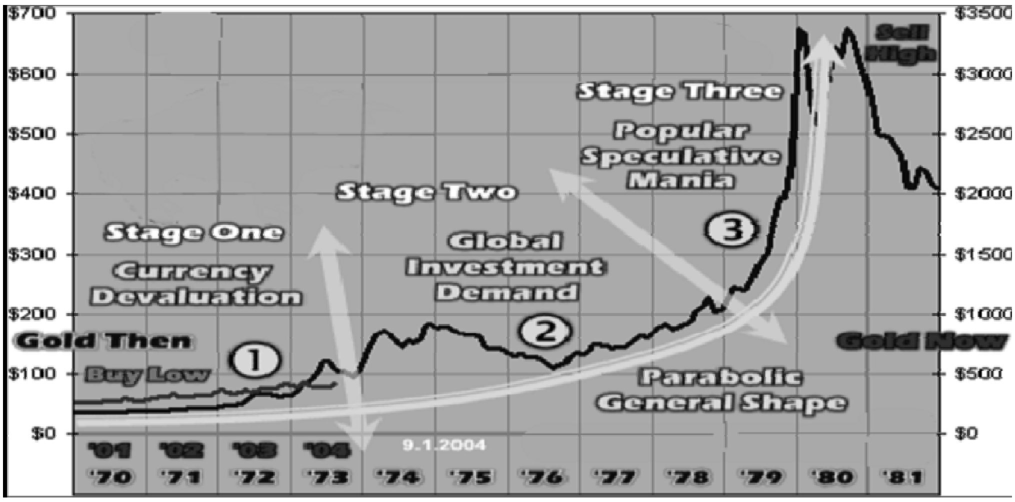
Thus it is not only important to realize that it is not mines or central banks that ultimately, drive, gold prices, but private investor demand, it is also crucial to understand that global gold investment demand only grows with

12) Goldsheet links.com/pjroduction by country.

13) Lawrence Colin, Why gold different from nother assets;, World Gold Council, March, 2003.

higher gold prices. Using this gold supply-and-demand fundamentals, we can divide secular gold bulls into three distinct stages based on pure global investment demand.

Chart 15. Gold bulls' three stages anatomy of a great gold bull



Source : Hamilton Adam, Gold Bulls' Three Stages, Zeillc, September 3, 2004.

The first important thing to note on this secular gold bull chart 15 is the typical parabolic shape of a secular gold bull. All secular bulls that ultimately culminate in bubbles exhibit this distinctive pattern of price increases continuously accelerating over time. As the arrow yellow parabola shows, this acceleration is almost imperceptible in the early years, picks up dramatically in the middle years, and is breathtaking in the final years.

The left axis of this chart corresponds to the blue line(①, ②and ③) of the Great Gold Bull of the 1970s. Interestingly, since we used monthly data, this 1970s gold bull is ever a bit understated. While the all-time monthly high close for gold is under $700 as this chart show, gold actually soared to $850 per ounce briefly in January 1980 at the top of its East mania.

The right axis defines the red line (from '01 to '04), which is our current gold bull to data from January 2001 to 2004 in monthly terms.

As you can see, the early slopes of this gold bull and the early years of the 1970s Great Gold Bull match remarkably well today, just as gold did from 1970 to 1973, it is once again stealthily climbing the initial modest upslope of the arrow(yellow) parabola. If our current specimen continues to hold the course plotted before it in the 1970s, gold will ultimately trade over thousands of dollars per ounce before this decade ends.

The key to understanding this parabolic shape that all secular bulls ending in bubbles assume is to understand the changing investment demand profiles throughout a secular bull. The constantly accelerating parabolic profiles is driven by shifting investment demand over the life of secular bull. The higher an investment price gets, the higher demand grows and a positive feedback loop is created.

Stages One, Two, and Three of a secular gold bull are defined by the two major slope changes in this standard secular-bull parabolic ascent. Each stage, considered in turn, makes perfect sense when described in terms of global investor demand.

Gold is ultimately money, and during Stage One bulls it trades like another currency[14]. One of the primary reasons why the Stage One upslope is so moderate is that the main reason gold rises initially is due to a devaluation of the dominant currency in which it is priced, obviously the US dollar today.[15] As the US dollar bear has festered in recent years, and as the dollar eroded in the early 1970s, gold is a direct beneficiary of the dollar's losses. As the dollar grinds lower, the gold/dollar exchange rate rises.

Since Stage One is currency-devaluation driven, the young gold bull is most noticeable in terms of the dominant eroding currency. Since April 2001 gold's gains have been greatest in the US since it is the US dollar that is devaluing. But from foreign-currency perspectives, such as the Europeans', gold has traded largely sideways in recent years. Stage One gold bulls witness gains that are roughly one-to-one with currency losses, so they are most evident in local-currency terms.

Now since these early Stage One bulls are only apparent to contrarian investors in the country with the dominant devaluing currency, overall investment demand is low. Not only is gold coming off a multi-decade secular bear so not many folks believe in it, but it has no established momentum so only hardcore contrarians will even consider it. The total capital the contrarians command is very small relative to the markets as a whole, so initial gold buying on the local-currency devaluation is rather anemic and makes for a tepid initial upslope.

Now after three or four years of Stage One, Stage Two arrives. Stage Two marks a momentous event when gold decouples from the local-currency devaluation. In the case of our gold bull today, Stage Two will be here when gold starts consistently rising faster than the dollar is able to fall. This key decoupling works on multiple fronts to really kindle investment demand around the world and marks the first significant steepening of the parabola's upslope.

Even more importantly in Stage Two though, since gold's gains start outpacing the dollar's losses gold starts rising in virtually all currencies worldwide! Rather than appearing flatlined, a mere product of the dollar's misfortune, gold starts showing up on foreign investors' radars as it consistently carves new local-currency gold highs around the world. And not surprisingly foreign investors, who generally know how fragile governments and fiat currencies truly are, far more receptive to gold investings.

---

14) Harmston Stephen, Gold as a Store of Value World Gold Council, Research Study No.22, November, 1998.
15) Neuberger Anthony, Gold Derivatives, World Gold Council, May 2001.

Gradually these foreign investors start buying gold and global investment demand accelerates. The more global capital that is poured into gold, the faster its price rises tracking the accelerating parabolic upslope. And of course the faster gold's price rises the more new capital it attracts. This virtuous circle on a global scale is what fuels the strong gains of Stage Two, which provocatively utterly dwarf Stage One. While gold went from $257 to $427, or 66% higher in Stage One so far, it should trade considerably above $1,000 before Stage Two ends, or another 134% higher from here.

After five or so years of Stage Two gains, gold has a chance at going ballistic in Stage Three. Stage Three is only ignited if the general public around the world starts growing enamored with gold investing. When the gold bull spreads beyond the usual investment class to the general public so much capital deluges into gold so rapidly

Naturally a vertical upslope is totally unsustainable and cannot last for much longer than a year at best. Stage Three is a captivating time for the early contrarians who rode the entire gold bull from its early Stage One days to its mania days. Vast gains rapidly multiply, yet a sustained vertical ascent on a long-term chart is dire warning sign that the party will soon be ending. Contrarians are torn between riding gold just a little longer and immediately selling it all.[16)]

Not surprising the greatest gains of all are found in Stage Three. Extrapolating today's bull-market data on a 1970-style gold parabola, gold could easily shoot form $1,000 to over $3,500 if the public enters and ignites a popular speculative mania. This massive 250% gain in Stage Three alone is roughly twice as great as Stage Two's 134% and four times as great as Stage One's 66%. As the parabola model suggests, secular bull gains multiply exponentially until the bubble pops and the mania comes crashing down.

It is crucial to realize that time unfolding secular parabola is totally dependent on only one force, global investment demand for gold. Mines just can't wrest enough gold free from Earth fast enough to stop this parabola once it is in motion and central banks' relatively small 20% control of global gold supplies isn't enough to stop the other 80% when gold lust spreads from contrarians to mainstream investors to ultimately the general public.

And, unlike normal demand profiles, gold investment demand only increases as gold prices march higher in currencies around the world. The higher the gold price goes, the more demand it spawns, at least until the public jumps in, foments a bubble, and all the capital available to chase gold is already in leading to the bubble bursting and the end of the secular bull market.

If you note the transition in the chart 14 from Stage One to Stage Two, it looks like our current gold bull is almost there. For a variety reasons We agree and believe that Stage Two is probably right around the corner today.

16) Hamilton Adam, Gold Bull's Three Stages, Zeillc, September. 3, 2004.

2. Global gold highs and gold decoupling from the dollar

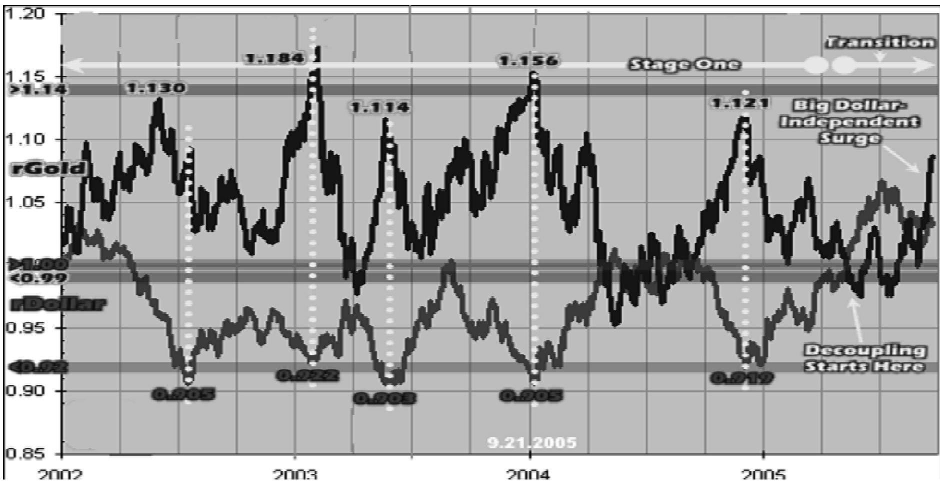
Gold prices are rising around the world in all major currencies[17]. This is a telltale sign of a Stage Two gold bull, where gold decouples from the US dollar. Over the past few months gold is appearing to be decoupling from the US dollar. Thus may be the transition to Stage Two, where gold profits soar.

The Ancients Metal of Kings has majestically carved a series of new bull-to-date highs, breaking out to the upside after consolidating for the better part of a year.

Before we get into the charts suggesting that gold is starting to decouple from the dollar, it is important to understand gold-bull stages again. Great gold bulls tend to have three stages over their lifespans, which unfold consecutively as gold carves a long-term parabola over a decade or more.

Stage One is primarily currency-devaluation driver. This is what we have witnessed in recent years as gold typically only gained significant ground when the dollar, the word's reserve currency, was losing value. Stage Two is driven by global investment demand which makes gold decouple from the dominant currency and rise on its own fundamental merits in all currencies simultaneously. Finally, Stage Three can ignite near the end of a secular bull when a popular speculative mania drives gold vertical into a blowoff top.

Chart 16. Relative dollar and relative gold



Source : Zeillc, 2005.

Our following chart 16, which proved extremely useful for timing the major gold uplegs and corrections in Stage One, compares the Relative Dollar to Relative Gold. To compute these series, each currency is divided by

17) World Gold Council, Spot Gold in a Range of Currencies, December 12, 2005.

its own 200-day moving average and then the resulting multiples of these 200dmas are plotted over time. these relative readings have accurately shown us when gold uplegs were overbought and dollar downlegs were oversold. But the character of this venerable indicator has suddenly changed. As you see in the chart, think of both gold and dollar charts flattened along a common horizontal 200dma line running at 1.00. The well-established gold and dollar synchronized pirouette seems to be spiraling apart in recent months.[18)]

Prior to mid-spring 2005, gold tended to be strong when the dollar was weak and vice versa. Major gold uplegs, illustrated here by gold soaring above its 200dma to higher rGold multiples, only occurred when the dollar was suffering major downlegs, falling below its 200dma to lower rDollar multiples. If you consider the blue (upper rGold) and red (lower rDollar) lines in a general sense, they could almost be inverted mirror images[19)].

Both gold and the dollar generally stretched away from their respective 200dmas simultaneously to advance their opposing secular moves. And once these secular moves reached sentiment extremes both currencies would contract back to their 200dmas simultaneously in counter trend moves. This tendency was so well defined in Stage One that gold traders could time trades based solely on the dollar's rhythms.

But check out the last couple calendar quarters on this chart. Starting in spring, the dollar was roaring forward in its greatest bear-market rally in its entire bear to date. If the Stage One relationship between the dollar and gold had held, gold should have been crushed as the dollar surged for beyond its 200dma that usually caps its major bear rallies.

While gold was initially compliant and retreated back to its 200dma in early 2005 as the dollar approached its own, once the rDollar went above 1.00 gold refused to fall any farther. Indeed gold even started rallying as the dollar continued blasting higher, quite uncharacteristic behavior for a Stage One gold bull. While it is still a bit too early to make emphatic prognostications, it sure looks like gold is decoupling from the dollar and transitioning to Stage Two.

The stunning gold trading action in early 2005 certainly appears to confirm a fundamental change in gold's relationship with the dollar. Gold's entire September surge was independent of the dollar's behavior. Investors were bidding up gold for other reasons than just dollar weakness. This is very important as it is exactly what we should expect in Stage Two. Gold rises independently in all currencies regardless of the dollar's machinations.

To get an idea of just how unique such a dollar-independent gold surge is, examine the past major rGold rallies in this chart. Every single prior one occurred only, when the rDollar was falling in its own trading band, when the dollar was sinking rapidly under its own 200dma. In Stage One it is dominant-currency devaluation that is the primary of gold, not investment demand. The decoupling starts slowing with frequent relapses back to Stage One behavior. But as this transition matures more and more time is devoted to Stage Two independence. Stage

---

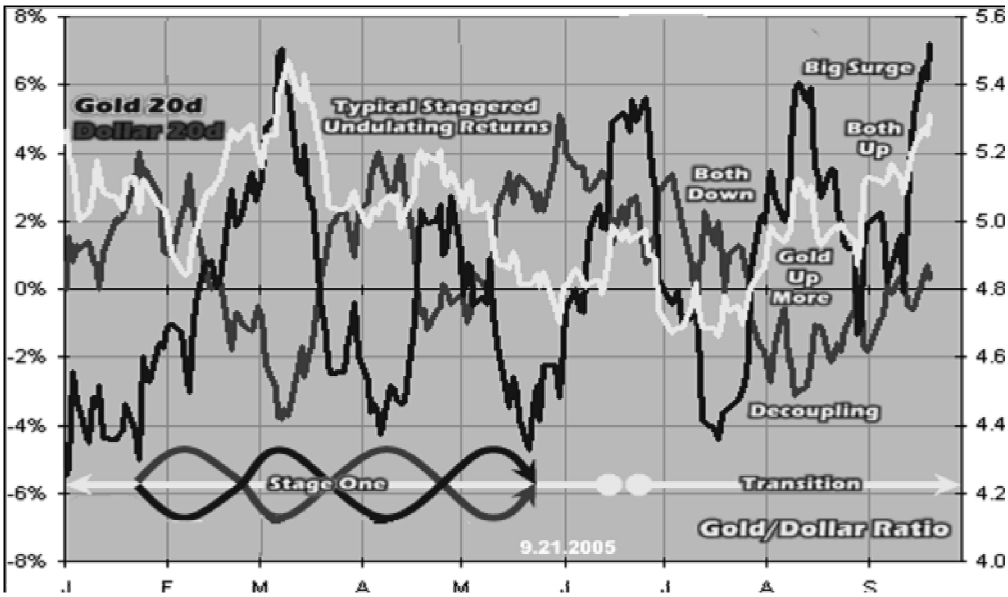
18) Hamilton Adam, Gold Bull Stage Two, Zeillc, September 23, 2005.
19) Hamilton Adam, Relativity, Zeillc, October 1, 2004.

One gradually fades into Stage Two over a transitional time.

Our next chart 17 also highlights this evolving transition between the stages. It records the absolute 20-trading-day returns achieved in both gold and the US Dollar Index so far in 2005. We chose 20d returns because most calendar months run 20 to 21 trading days, so this is like looking at how much gold and the dollar have returned on a rolling-month basis continuously. This alternative perspective also reveals the transition underway.

The yellow line(we can see it on the screen) overlaid on the gold and dollar 20d returns is the gold/US Dollar Index ratio. It shows which currency has the balance of power at any given time. When this ratio is falling the dollar is outperforming gold, and when it is rising gold is outperforming the dollar. It provides a reference point off of which to frame the 20d returns we have witnessed in the dollar and gold, 2005.

Chart 17. Dollar and gold 20d returns



Source : Identical with Chart 15.

Prior to mid-June the dollar and gold returns were offset as we have come to expect in Stage One. When the dollar was doing poorly gold was thriving and vice versa. A stylized version of this relationship is rendered in the lower-left corner of this chart. It looks like a series of offset sine waves where gold is almost totally dependent on the short-term fortunes or lack thereof in the dollar.

Other than the brief gold spike in March, there really is a lot of parity in these 20d returns. When the dollar is up 4%, for example, odds are gold will be down about 4%. There was a strong, though not airtight, tendency for the gains/losses in gold to be very similar in magnitude to the losses/gains in the dollar.

This parity behavior establishes a hard empirical baseline from which we can judge the uniqueness of this apparent Stage Two transition. The breakdown of Stage One protocol looks to have started in. This pivotal event does indeed appear to be catalytic in broadening the group of international investors buying gold.

While early June looked normal, the 20d returns of both gold and the dollar started falling into July. The serpentine offset relationship that looks like a sideways version of the serpents entwining the medical symbol caduceus started to fail. In August Stage One behavior kind of returned but gold was up far more than the dollar was down, +6% compared to -3%. And so far in September both currencies are up but gold’s 7% surge utterly dwarfs the dollar’s flat month-over-month returns.[20)]

Granted several months is not much data to discern a major secular development, but you have to admit that gold’s behavior in recent months really looks like it is decoupling from the dollar’s dominating influence. Rather than gold just mechanically offsetting the dollar at a similar magnitude, lately gold has been doing whatever it wants regardless of the dollar’s own behavior. It looks like it is gradually achieving Stage Two independence!

Just as great secular gold bulls unfold over more than a decade, the transitions between their three stages are not instant but a gradual fade.

Ⅴ. Summary of main conclusions

In the week ending December 16, 2005, gold ran up to $540/oz and thudded back to $500. The question on most everyone's mind now is what is next for gold & where do things go from here?

Right now gold is trying to support at $500. It will likely pause or bounce off of that number for a few days before slipping back down below it. The long-term picture, however, looks even more bullish than ever. Our gold world view is long-term bullish as we believe gold is going higher, and is in a massive secular bull market that ought to gallop higher for many more years, perhaps a decade 2006 should be a huge year for gold. Bull markets usually come in three stages. The first stage being when insiders and professionals invest in the market. The second stage is when the general public and financial media recognizes that the bull market is real. The third stage is the mania stage when people feel what not only is the bull market real, but it is a must own situation. Gold is entering it now.

Even though the gold bull market is now going on it's fourth year, up until the past few months it got very

20) Hamilton Adam, Global Gold Breakouts, Kitco, December 22, 2005.

little attention in the press. The only people really participating in it were a select group of gold insiders, so called "gold bugs" and a few investment professionals who also understood the gold trend. Now, hedge funds start to flock into the gold market and commentary in the main stream press is now recognizing that gold is going up. The only thing we know that gold is going up and the viewers should buy some if they want to make money. We can say that gold isn't a great long-term, but is going up because demand for gold is growing. Gold is going to keep going up, we analysed a confluence of factors seem to be feeding gold's rising and the typical shape of a Secular gold bull --- gold bulls' three stages. Through the study here, we found that gold market is already in the Stage Two --- decoupling from the dollar or transitioning to Stage Three.

For the past few years, the mainstream media has mocked gold bugs whenever it has mentioned the gold trend. Now it is recognizing that the trend is real. This is also a sign that we are beginning Phase Two of the gold bull market. However, Phase Three will come when the mainstream media and the general public comes to see gold as a "must own" hedge. Anyway, 2006 is going to bring the biggest move in gold that we've seen yet, fortunes are going to be made.

BIBLIOGRAPHY

Anikim. A., Gold- the Yellow Devil, International Publishers, N. Y., 1983.

Allen, G., Gold, History from Ancient Times to the Present Day, New York, 1965

Bernstein, Peter L., The Power of Gold : The History of an Obsession, John Wiley & Sons, 2000

Beck Rachel, In Turbulent Times, Gold Becomes Hot Commodity, Contra Costa Times, December 21, 2005.

Blakemore, K., The Book of Gold, Stein & Day, 1971

Boyle, R.W., The Geochemistry of Gold and its Deposits, Geological Survey of Canada, 1979

Buranelli, Vincent, Gold, an Illustrated History, Dembner Enterprises, 1979.

Busschau, W.J., Measure of Gold, Central News Agency, 1949

Cartright, A.P., The Gold Miners, Purnell & Sons, 1962

Desebrock, Nigel, Gold Refiners and Bars Worldwide, Grendon International Research Pty. Ltd., 1991

Friedberg, R., Gold Coins of the World, The Coin and Currency Institute, 1971

Green, Timothy, The Gold Companion : The A-Z of Mining, Marketing, Trading and Technology, Rosendale Press, 1997

Hahn, Emily, Love of Gold, Lippincott & Crowell, 1980

Halliday, J.S., The World Rushed In : The California Gold Rush Experience, Gollancz, 1984

Hamilton Adam, Gold Bulls' Three Stages, Zeal, 2004
Hamilton Adam, Global Gold Highs, Zeal, 2005
Ivosevic, Stanley W., Gold and Silver Handbook, Ivosevic, 1984
Jastrom, Roy W., The Golden Constant：The English and American Experience, 1560-1976, John Wiley & Sons, 1977
Kettell, Brian, Gold, Ballinger Press, 1982
Klapwijk, Philip, Gold Survey 2001, Gold Fields Mineral Services, 2001
Kutz, Kenneth J., Gold Fever, Gold Fever Publishing, 1987
Lassonde, Pierre, The Gold Book, Penguin Books, 1990
Paul, R.W., Californian Gold, Harvard University Press, 1947
Puddephatt, Richard J., The Chemistry of Gold, Elsevier Scientific Publishing Co., 1978
Rapson, W.S., and Groenewald, T., Gold Usage, Academic Press, 1978
Robbins, P. and Lee, D., Guide to Precious Metals and Their Markets, Kogan Page, 1979
Rose, Sir. T.K., and Newman, W.A.C., The Metallurgy of Gold, 7th Edition, 1937
Sarnoff, P, Trading in Gold, Woodhead-Faulkner, 1980
Shinn, C.H., The Story of the Mine：As Illustrated by the Great Comstock Lode of Nevada, University of Nevada Press, 1980
Vaughn David, What Next for Gold?, Kitco, 2005
Swanson Mike, Gold Corrction and Phase Two, Kitco, 2005
White Ben, Gold's New Luster Puzzles Traders, Washington Post, November 30, 2005
Wise, Edmund M., Gold：Recovery, Properties, and Applications, Van Nostrand, 1964
青柳守城(あおやぎもりま), 金の知識, 東洋經濟新聞社, 昭和 57.
荒木信義(あらきのぶよし), 円·ドル·金, 日本關稅協會, 昭和 61.
稲葉豊實(いなだとよみ), 金と投資, 日本工業新聞社, 昭和 54年.
崎川範行(さきかわ のり やき), 金の 雜學, ブル-バックス, 1989.
第一商品, それからの 金価格, 現代書林, 1988.
高橋靖夫(たかはしやすお), 金投資入門, KKベストセラ-ズ, 昭和 54.
增田義郎(ますだよしお), 黃金郷に憑かれた人々, NHKブっ久ス, 平成元年.
松村善太郎(まつむら ぜんたろう), 金と SDR, 日本經濟新聞社, 昭和 44.
三宅義夫(みやけ よしお), 金, 岩波書店, 1968.
山下義男(やました よしお)外 3人, 金の 經濟がわかる本, ダイヤモンド社, 昭和 56.
プレジデント, 金の 常識, プレジデント, 1981.
www.eagletraders.com

www.goldinstitute.org

www.gold.org

www.the-privateer.com

www.anygoldnow.com

www.goldsheetlinks.com

www.kitco.com