GOLD

INVESTING GUIDE 2013

GOLD

Price Forecast 2013

PREDICTIONS AND ESTIMATES FROM MULTIPLE ANALYSTS

The Gold price forecast for the year 2013 has been covered by multiple analysts. Here is their consensus:
While the price of Gold has a gamut of forecast ranges for 2013, most experts remain bullish on the yellow metal for the year, though some have scaled back their estimates slightly over the past few months. A compilation of their predictions are listed below.

BANK OF AMERICA MERRILL LYNCH

In a December 2012 report, Bank of America Merrill Lynch stated that Gold would average $2,000 in 2013, with the metal climbing to $2,400 in 2014.

"Large-scale policy easing by the U.S. Federal Reserve and European Central Bank positions Gold as a useful hedge against global macro and inflation risks taking the commodity to $2000/oz levels", said the bank. The bank added that, "We have a six-month [Gold price] target of $2000 an ounce, but see scope as well for prices to rise to $2400 an ounce by the end of 2014. These targets reflect our view that the Fed will maintain mortgage purchases until the end of 2014 and will move to buy Treasuries following the end of Operation Twist in December 2012."

GOLDMAN SACHS

In December 2012, Goldman Sachs cut its three, six, and 12-month forecasts for Gold prices to $1,825, $1,805, and $1,800 an ounce respectively.

"We retain a positive view on the Gold market, but given Gold's outperformance during risk on intervals and our forex strategists' expectation for the dollar to strengthen beyond three months, we are revising down our forecast for 2013 modestly, to $1,815/oz," the bank said.

BARCLAYS CAPITAL

Barclays trimmed its 2013 price forecast for Gold by 2.5% in December 2012, but said that it still expects the metal to average $1,815 an ounce for the year.

"We retain a positive view on the Gold market, but given Gold's outperformance during risk on intervals and our forex strategists' expectation for the dollar to strengthen beyond three months, we are revising down our forecast for 2013 modestly, to $1,815/oz," the bank said.

BNP PARIBAS

BNP Paribas expects Gold to average $1,865 an ounce for the year.

"Market sentiment towards Gold has been much more uncertain in 2012 than was the case in previous years. Yet, we expect Gold to achieve a new record high in 2013 due to further monetary easing, less tail risk related to a breakup of the euro zone and ongoing support from physical demand," said BNP Paribas analyst Anne-Laure Tremblay in December.

UBS

Also in December, UBS maintained its 2013 price forecast for the yellow metal, stating that Gold would average $1,900 for the year.

According to analysts at UBS, "The chief driver of the Gold price is partly the short term uncertainty around US fiscal policy, but also the view that monetary authorities will keep their policy loose through the rest of next year." "The US Federal Reserve in its latest statement on interest rate policy has said that it will keep US rates near zero until the country's jobless rate falls closer to its historical average from the current higher level. The Fed will also continue its policy of quantitative easing, which effectively means printing money to force down the yield curve to stimulate growth through investment in the economy." "The Gold price should also benefit from similar open ended commitments by the European Central Bank, while the pending election in Japan could result in a significant policy shift at the Bank of Japan as it seeks to more aggressively stimulate the domestic economy."

HOW GOLD HAS PERFORMED IN 2012

During 2011, the price of Gold increased by more than 12% from the previous year, which marked the yellow metal's eleventh consecutive year of growth. The price of Gold at the start of 2012 was $1,536.20 per ounce. By December 21, 2012, the Gold price had increased – amid high volatility – to roughly $1,660.10, a gain of approximately 8.1% since the beginning of the year. Although Gold is on track to record its twelfth consecutive year of rising prices, the metal has slid about 7.9% since it hit its 2012 high of $1,791.75, on October 4, 2012. Gold's recent slide is partly due to the U.S. Commerce Department's latest report showing that U.S. GDP in the third quarter expanded at an annual rate of 3.1%, the fastest growth since late 2011.

Phil Streible, a senior commodity broker at R.J. O'Brien & Associates in Chicago told Bloomberg News, "The GDP number was better than forecast, so the thinking is that improving conditions in the economy might mean a light at the end of the tunnel on when the Fed will end QE3."

However, there are other important factors responsible for Gold's recent downturn. The metal is suffering from a typical decline in long trading activity as the year comes to a close. The Wall Street Journal recently noted that Gold traders tend to avoid holding large Gold positions in the last several weeks of any given year due to thin trading volumes and a scarcity of buyers and sellers that often enhance volatility and cause wide price swings. Profit taking is another important factor putting downward pressure on Gold prices. Money Morning Capital Wave Strategist Shah Gilani told FOX Business Network that Gold's large price move has to do with the metal becoming a trading vehicle.

"Gold has become a tradable asset class," explained Gilani. "It's no longer a hedge. It's no longer what it used to be. Investors are buying and selling Gold as they would any other commodity, as they would any stock, as they would any ETF, as they do Apple," stated Gilani. Just as investors are taking profits in other winning assets, they are doing so with Gold, which makes for more sellers than buyers ahead of the New Year.

The rise of the price of Gold appears set to continue as many investors are turning to Gold commodities to add stability to their portfolios.

CONTINUED FINANCIAL CRISIS IN 2013 MEANS HIGHER GOLD PRICES

Some of the key indicators putting upward pressure on Gold prices for 2013 are: the uncertainty following the long-term effects of the last-minute U.S. fiscal cliff aversion, increased monetary easing and currency debasing policies worldwide, rock-bottom interest rates, concerns over the financial stability of the euro zone, and diversification into bullion by central banks.

THE EURO ZONE CRISIS DRIVES GOLD PRICES

In its recent bi-annual report on the world economy, the Organization for Economic Cooperation and Development (OECD) warned that the world economy is in danger of another contraction if euro zone and U.S. policymakers fail to restore confidence by resolving their fiscal problems. “After five years of crisis, the global economy is weakening again,” said Pier-Carlo Padoan, the OECD’s chief economist. “The risk of a new major contraction can’t be ruled out.”

The Paris-based think tank stated that the euro zone’s fiscal and banking crisis remains the greatest threat to the global economy, and that the currency area might not survive in its current form. “The euro area, which is witnessing significant fragmentation pressures, could be in danger,” added Mr. Padoan.

“We don’t think the euro-zone crisis is over yet. Fragility in the euro area remains, and the negative feedback loop between banks and sovereigns is still there.” Mr. Padoan added that citizens’ growing frustration with austerity measures and their consequences could also create serious problems within the region, stating that, “Rising unemployment could trigger reform fatigue and social resistance.” Sluggish growth in the euro zone is a major concern, with the OECD expecting the economies of Greece, Italy, Portugal, Slovenia and Spain to contract again in 2013. The composite purchasing managers’ index, or PMI, for the currency area also remains in contraction, with data indicating that the recession deepened during the third quarter of 2012. Should one or more members leave the euro zone, the effects would be far-reaching and Gold prices would certainly rise as investors scramble for a safe haven. Even if this doesn’t occur, the euro zone is a long way from resolving its sovereign debt issues and the uncertainty in the region will continue to favorably affect the yellow metal.

“The euro area, which is witnessing significant fragmentation pressures, could be in danger,” added Mr. Padoan.

THE FISCAL CLIFF AND U.S. MONETARY EASING POLICIES

While GDP in the U.S. surpassed expectations for the third quarter of 2012, American policymakers took until the last minute to come up with a deal to evade the country’s fiscal cliff. Reaching an agreement allowed the country to avoid the expected extraction of about $600 billion from the economy at the start of 2013.

However, Steven Englander, a fixed-income strategist at Citigroup, wrote in a note to clients that “The process was so chaotic and the outcome so unsatisfactory that we are likely to see a further U.S. downgrade at some point.” Even after avoiding the fiscal cliff, the U.S. debt is currently a staggering $16.358 trillion, and congress must also agree to raise the debt ceiling. There is no question that the current debt level coupled with sagging corporate earning reports by U.S. companies over the last last quarter of 2012 will weigh heavily on the U.S. economy and renew Gold's role as an attractive safe haven investment. The Federal Reserve recently announced that it would keep a key short-term interest rate at 0.25%, and also that it will buy $45 billion in additional treasurys every month, on top of the $40 billion of mortgage-backed securities it already purchases, taking the total size of its quantitative easing program to $85 billion a month.

The Fed's recent policies which lower the value of the US dollar may trigger a cycle of currency wars with the emerging world, much like what occurred with QE1 in 2008 and QE2 in 2010. Tension has been increasing on an international scale, as many wealthy countries enact monetary easing policies which directly devalue their currency. A lower currency is good for industry on a national scale as it allows the country to be more competitive as an exporter.

Over the final two months of 2012, three of the world's largest central banks, namely the U.S. Federal Reserve, the European Central Bank and the Bank of Japan, embarked on a new round of monetary easing. This involves printing money and lowering the long-term interest rates in order to stimulate the economy.

The combination of lowered interest rates and monetary easing are likely to result in increased inflation and a devaluation of the dollar, both of which put upward pressure on Gold prices.

CENTRAL BANKS TO CONTINUE PURCHASING GOLD IN 2013

A number of the world's most prominent Gold experts are expecting central banks to continue to play a very supportive role in underpinning the rise in the Gold market in 2013.

In recent years, central banks - the long-time nemesis of the Gold sector – have done an about-face to become its biggest supporters. And this shift promises to retain momentum in 2013 with the prospect of a new era of net buying continuing to fuel robust demand for bullion.

According to data compiled by the World Gold Council, the world's central banks purchased more than 500 tons of Gold in 2012, up from 465 tons in 2011. It is the highest level recorded since central banks became net buyers of the precious metal in 2009, after 20 years of continued net sales. Central bank Gold buying has become a driving force of the Gold market today. Only a few years ago the central banks were net sellers of Gold under a long-standing inter-bank agreement. But lately they have been among the biggest buyers to protect against weaker currencies and the potential for faster inflation. The Bank of Korea recently announced that its Gold reserves rose by 14 metric tons, a 20% jump in total holdings to 84 tons. Brazilian holdings expanded 14.7 metric tons in November to 67.2 tons, doubling the country's reserve since August. Brazil bought 17.2 tons in October after adding 1.7 tons in September, the first increase since 2008. Kazakhstan expanded their Gold reserve by 7.5 tons last months, while Russia and Belarus's holdings increased by 2.9 and 1.4 tons respectively during the month.

"Central banks, particularly in the emerging economies, are looking to increase the proportion of Gold in their reserve assets," Alexandra Knight, an analyst at National Australia Bank Ltd., said from Melbourne. "That will drive prices of Gold because they can be quite significant purchases." The proportion of Gold as a share of total reserves is much smaller in emerging economies than advanced countries, and there's probably going to be a continued push to increase the amount of metal held, Knight added. The U.S., Germany, Italy and France hold more than 70% of their reserves in Gold, according to data from the producer-funded WGC. The share in Brazil, the largest emerging economy after China, is 0.8%, the data show.

Predictions about Gold's ascendancy are not just being validated by central bankers. Since the financial crisis, there has also been a buying frenzy among many of the world's multi-billion dollar hedge funds, as well as plenty of other institutional investors and of course legions of individual speculators. All have been buying in record amounts. And most are venturing into the Gold sector for the very first time.

Similarly, Gold-backed Exchange Traded Funds (ETF's) are attracting ever-increasing numbers of rattled investors, who view Gold as the ultimate hedge against a weakening US dollar and continued instability in the US economy. The prospect of a continuation of low interest rates for some time to come is also adding to Gold's universal appeal.

Flows into ETFs may total 200 metric tons this year, from 175 tons in 2012, Barclays Plc said in a Nov. 8 report. That's 4.6% of total physical supply of 4,323 tons this year, according to Bloomberg calculations based on Barclays' figures.

With banks worried about the outlook for the financial sector, sales by the world's central banks promises to be even lower next year than they have been in 2012. Given the damage done to other paper assets that were formerly considered secure, there will be greater risk aversion among central banks, boosting Gold's status within central bank reserves. The shift in central bank Gold transactions in 2013 shows no signs of abatement, and is one where major sovereign investors (state-owned investment funds), are increasingly hedging against an ailing dollar in favor of bullion.

A key reason why central banks want to hold onto Gold is the instability of their most common reserve asset, the dollar. Gold traders are paying close attention to reports from Beijing that China is attempting to boost its Gold reserves to around 4,000 tonnes to diversify away from paper currencies. Should this be true, it could lead to a significant material change for the Gold price.

China is the world's largest Gold producer, but the metal only represents 2% of the central bank's total asset portfolio. As the nation's economy continues to grow, they will certainly increase the amount of Gold in their portfolios.

"When comparing China to the U.S., it would seem that in China, gold asset allocation can only go in one direction," Chairman David Gornall told the association's annual conference in Hong Kong. "The country has only 2% of its reserves in the form of gold compared with the U.S. at 75%."

The International Monetary Fund (IMF) was the major seller of Gold in 2009-2010, after the executive Board approved the sale of 403.3 metric tons of Gold (12.97 million ounces), which amounted to one-eighth of the Fund's total holdings of Gold at that time. However, in December 2010, the IMF concluded its limited Gold sales program.

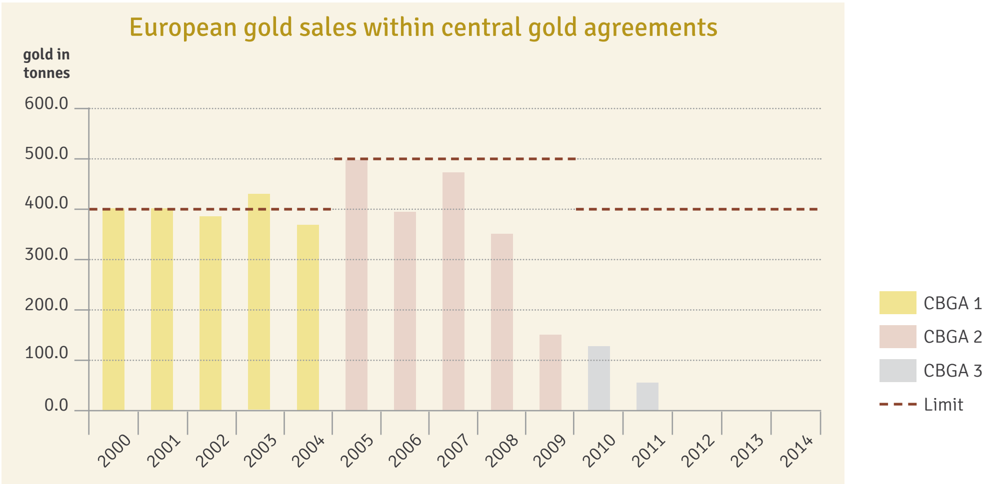
Central bank officials the world over have woken up to the fact that their predecessors acquired Gold reserves in the first place to stave off currency devaluations. And that impetus is once again taking on a heightened importance against a backdrop of "continued economic and currency uncertainty, and inflation concerns." This is the conclusion of a report by the London-based World Gold Council. The report adds:

"In the official sector, we expect to see a continuing trend of central banks diversifying their dollar exposure in favor of the proven store of value represented by Gold."

There are plenty of other Gold-hungry central banks elsewhere in the world, especially in Asia, that may not wait to see if Gold drops much further before they act.

CENTRAL BANKS: EUROPEAN IMPACT

Sales of Gold by European central banks has substantially decreased over the last couple of years as political and economic crises have increased the appeal of bullion as a "safe" reserve asset. The Central Bank Gold Agreement, which began in September 1999, permits signatories to sell 400 tonnes of Gold collectively per year. However, in 2010 European central bank signatories only agreed to sell a gross 1.1 tonnes of Gold during the year, the lowest annual sales since the agreement began. Total Sales in the last year of the agreement (which spanned from September 2010 to September 2011) reached 53.3 tonnes, due to the additional 52.2 tonnes of Gold sold by the IMF as part of its limited Gold sales program.



Source: IMF International Financial Statics and European Central Bank

According to Natalie Dempster, Director of Government Affairs, "European central banks' appetite for Gold sales has dissipated since the onset of the financial crisis. During periods of such intense economic and financial market turbulence Gold adds much needed stability to a central bank's reserves. This is also evident from the behavior of emerging market central banks over the past two years who have accumulated significant additional volumes of Gold. As a whole, central banks are now large net buyers of Gold having re-evaluated their reserve asset management policies and we expect them to remain so for the foreseeable future."

GOLD INVESTMENT STRATEGIES

While most analysts remain bullish on Gold in 2013, there is an obvious wide range of predictions for the coming year on the pricing of precious metals. Some investors will choose to play it safe by steering clear of this investment altogether. Others may trade the futures market while others will speculate on companies that derive their income based on the commodity. Many will use options for increased leverage and to manage risk. Regardless of methods used to play the Gold market, investors will no doubt be carefully keeping abreast of the changing price forecast for 2013 to aid their decision-making.

BATTLE OF THE "SAFE HAVENS"

The continuing uncertain economic picture is likely to remain a catalyst for Gold to perform well as a "safe haven." In particular, what may continue to give the Gold price the major boost that some economists expect could be the wholesale dumping of US assets by investors (especially China) around the world, as they lose patience with the US economy. In 2007 Professor Willem Buiter, one of the world's top economists and a former member of the UK's Monetary Policy Committee for the Bank of England predicted: "There will before long (my best guess is between two and five years from now) be a global dumping of US dollar assets, including US government assets. Old habits die hard. The US dollar and US Treasury bills and bonds are still viewed as a safe haven by many, but this may not continue for long" We are seeing this happen now, and Gold is the beneficiary. The faster the dollar falls, the steeper the rise in Gold price, in dollar terms at least. In other words Gold will ultimately win the battle of the "safe havens" and reign supreme as the de-facto currency of choice.

Immediate factors that may positively impact the Gold price:

I. Geopolitics: The chronic problems in the Middle East, with Iran, Afghanistan, Pakistan, Syria and other potential flashpoints boost the price of oil – usually a positive for Gold.

II. Physical delivery requests are mounting at the COMEX (commodity) futures exchange, which could well result in an immediate shortage of Gold. The futures market looks about to break down, giving control of the Gold price back to the physical market where available stocks are low.

III. Gold preserved value through the credit storm of 2009, and increased in value through 2012. Investors are becoming increasingly concerned about the bubble in the bond market and Sovereign debt. In the investment cycle the next step could be a bond crash and a flight to precious metals.

Source: www.kitco.com

THE GOLD SUPPLY

Supply is another major issue. It is commonly acknowledged that going into 2013, Gold mining supply worldwide has failed to grow during the recent bull market in Gold – and failed badly. Global Gold mining output peaked nearly 9 years ago in 2003. Consequently, many commentators believe that Gold can only continue to rise given its scarcity.

According to Barrick Gold Corp.'s (NYSE: ABX) CEO, the industry as a whole spent a record $8 billion in 2011 to explore for gold. And even with such massive resources on the hunt for this precious metal, discoveries are declining. Bloomberg reported that in 1991 there were 11 gold discoveries, yet in 2011 there were only three.

Gold mining supply Worldwide has failed to grow during the last 7 years leading to an increase in demand and prices.

Gold dealer reports an "unprecedented" shortage of metals

A surge for demand in Gold and silver has resulted in an unprecedented shortage of the metals for retail investors in recent days, according to Gold and Silver Investments, a Dublin-based firm that allows retail investors to speculate on movements in the value of precious metals. As the Gold and Silver supply deteriorated over the past few years, Gold and silver have now become only easily accessible in the primary market, which consists of central banks and other major traders of the precious metals. According to Gold and Silver Investments this situation is "absolutely unprecedented," and that shortages are likely to drive up the costs of Gold and silver in the secondary market: "This did not happen even in the 1930s and the 1970s, and will result in markedly higher prices."

FIVE FACTORS TO CONSIDER WHEN INVESTING IN GOLD

I An investment in Gold should be based on macroeconomic considerations. If the investor expects or fears rising inflation, destabilizing deflation, a bear market in stocks or bonds, or financial turmoil, Gold should do well and exposure is warranted.

II Understanding the internal dynamics of the Gold market can be helpful regarding investment timing issues. For example, the weekly position reports of commodity trading funds or sentiment indicators offer useful clues as to entry or exit points for active trading strategies. Reports on physical demand for jewelry, industrial, and other uses compiled by various sources also provide some perspective. However, none of these considerations, non monetary in nature, yield any insight as to the broad market trend. The same can be said for reports of central bank selling and lending activity. Central banks are bureaucratic institutions and in their judgments they are essentially market trend followers.

III A reasonable allocation in a conservative, diversified portfolio is 0 to 3% during a Gold bear market and 5% to10% during a bull market.

IV Equities of Gold mining companies offer greater leverage than direct ownership of the metal itself. Gold equities tend to appear expensive in comparison to those of conventional companies because they contain an imbedded option component for a possible rise in the Gold price. The share price sensitivity to a hypothetical rise in metal price is related to the cash flow from current production as well as the valuation impact on proven and probable reserves.

IV Bullion or coins are a more conservative way to invest in Gold than through Gold mining shares. In addition, there is greater liquidity for large pools of capital. Investing in the physical metal requires scrutinizing the custodial arrangements and the creditworthiness of the financial institution. It is also advisable not to mistake the promise of a financial institution to settle based on the Gold price, for example by a "Gold Certificate" or a "Structured Note" (i.e. a derivative). Instead, be adamant on actual physical possession of the metal. Insist on possession in a segregated vault, subject to unscheduled audits, and inaccessible to the trading arrangements or financial interest of the financial institution.

Holding precious metals in a portfolio can provide distinct benefits in the form of speculative gains, investment gains, hedging against macroeconomic and geopolitical risk and/or wealth preservation. Successful investing is about the diversification and management of risk. In layman's terms this means not having all your eggs in one basket. Some exposure to Gold should be included in all diversified portfolios. In the same way that every major Central Bank in the world continues to maintain huge reserves of Gold bullion so too should private investors invest, save and own Gold. A good rule of thumb would be a minimum allocation of around 10% to Gold and related Gold-investments such as Gold miming companies or Exchange Traded Funds (ETFs).

Diversification

Gold is a unique asset class and was possibly the first asset class to exist. Gold has been a store of wealth, a currency and a commodity for thousands of years. Furthermore, there is a growing body of research, which supports the notion that Gold is treated by investors as a unique asset class and fluctuates independent of both other asset classes and some macroeconomic indicators such as GDP and inflation. A number of studies overseas and one recent study by PriceWaterhouseCoopers in Australia have all found that Gold is insignificantly or negatively correlated with the major portfolio asset classes.

International research

The body of research studying the statistical benefits of holding Gold bullion in a portfolio is slowly growing. Roy Jastram wrote the cornerstone piece of this research in 1977: The Golden Constant—The English and American Experience 1560-1976. Jastram's book investigated the price and purchasing power of Gold over time and during different periods such as inflationary and deflationary times. He concluded that Gold bullion has held its purchasing power parity with other commodities and intermediate products over the very long term. In this study, the use of commodities as a basis of comparison enabled construction of a long-dated index which represented a CPI-style index (CPI did not exist 400 years ago). In 1998, Harmston (another financial historian) updated Jastram's research, while also looking at the relationship between Gold bullion and other asset classes. Harmston's study covered the US (from 1796), Britain (from 1596), France (from 1820), Germany (from 1873) and Japan (from 1880). Harmston ran a series of regressions and showed that there was a positive relationship between the annual movements in bonds and T-bills with the annual movements in the Dow Jones Industrial Average Index (DJI) for the period 1968 to 1996. Over the same period, Harmston found that Gold bullion had a negative relationship with the DJI.

What does this mean for the investor?

Many consider it an accepted practice in the finance industry that assets with low or negative correlation can decrease portfolio risk and expand the efficient frontier (see Markowitz theory on portfolio analysis). This gives rise to a problem for most investors because most stocks are relatively correlated with one another and most bonds are relatively closely correlated with each other. Savvy investors, therefore, are required to find investments that are not closely correlated to stocks or bonds and include these in their portfolios as a hedge. One of the main benefits from investing in Gold bullion is that it is either negatively correlated or independent from other asset classes or financial and macroeconomic measures. Many alternative assets exist, perhaps with low correlation to the major asset classes. However, in contrast, to most of them Gold bullion is highly liquid, fungible, easily stored and requires no management. Research suggests that Gold is one of the best asset classes for diversification.

Why Gold is better than cash

Rightly or wrongly, investing in Gold is often compared to investing in cash. This is in part because Gold has been used as money for thousands of years and often it trades like a currency although it also has some of the traits of a commodity. Regardless of how you choose to categorize it, Gold is often considered a currency. The summary below clears up some common misperceptions about Gold, relative to cash, and shows that, when the concerns of the average persons with respect to cash are taken into account, Gold comes out on top.

Defining Gold versus Cash

When Gold is compared to cash, most people don't realize that there are two main different ways of holding Gold bullion in a bank account: (1) allocated Gold, and (2) unallocated Gold. Using this terminology, cash on deposit at a bank is technically "Unallocated Cash". Therefore, one should compare unallocated Gold to cash on deposit. However, lets proceed with comparing Allocated Gold to Cash on Deposit as most people who think of Gold, think of it sitting in a vault, and not being lent out and therefore not collecting a return.

Allocated Gold is not lent out

One of the main reasons you keep money in the bank is that it (hopefully) pays a rate of return (the interest rate). Modern finance theory tells us that in simple terms, the greater the risk, the higher the potential return. Cash on deposit earns a rate of return because the bank lends out your cash – in effect you have loaned the bank your own cash. That is why you earn interest on it. The bank lends out this money at some multiple (in some countries in excess of 10 times) greater than its total deposits. You have just taken a risk on: (1) the banks credit worthiness and, (2) that the bank has made a good decision to lend out this money. The more money the bank lends out, or the higher the credit risk of the person/institution to whom the bank has lent the money, then the more risk you have taken on by depositing cash at the bank. The only control you have over this risk is by not keeping your cash on deposit with the bank. This is similar to unallocated Gold: it is lent out to a 3rd party, often to a multiple of what is actually on deposit, and it earns a rate of return which is called the lease rate. By comparison, allocated Gold is not lent out, does not carry any credit risk on the bank or a 3rd party, and therefore does not earn any income. Indeed, allocated Gold may bear a holding charge to cover the costs of storage and insurance.

The bank owns your cash

If you deposit allocated Gold with an institution, you own the Gold. You can turn up to the bank and demand your Gold to be delivered to you. It is like holding it in your own safety deposit box. Cash on deposit, on the other hand, is not owned by you. It is owned by the bank and therefore if your bank went into bankruptcy, then all cash on deposit with the bank would be shared amongst its creditors (unless it is bailed out by the government or through insurance). Having cash on deposit means that you rank as an unsecured creditor of the bank. Furthermore, if everyone demanded all their cash from the bank at the same time, there would not be enough cash to pay people. In small amounts, you can usually demand your cash, however even insignificant cash cannot be paid on demand.

Gold is always accepted

Provided that Gold has its authentication verified, Gold has always been accepted. It has been used as a store of wealth and as a currency for many thousand years. And as Alan Greenspan said in May 1999:

"Gold still represents the ultimate form of payment in the world ..Gold is always accepted."

In contrast, cash is not always accepted. A central bank can withdraw a note at any time, Gold however, is accepted anywhere in the world. It can be a currency without borders. Cash has borders and this is most pronounced when the government is unstable, the currency is not liquid or the government is printing too much money.

Gold is relatively scarce

Without getting too deep into the debate as to whether Gold has scarcity value, it is worth pointing out that Gold Fields Minerals Services (GFMS) estimate that only about 150,000 tons of Gold has ever been mined. At a Gold price of US$700/oz, this values the total world Gold stock at US$3.36 trillion. To put this in context, the total cash stock (M1 money - being cash & checkable deposits) in the United States is approximately US$1.3 trillion. Knowing that money exists in every country and how that money is multiplied, the implications are that Gold is scarce, relative to cash.

Gold is produced, money is printed

Gold forces discipline; Gold's production process from exploration through to the minting of Gold bars can take as long as 30 years, but let's say that it generally takes 10 years. Compare this to cash, which can be printed at will by each of the world's governments. On this subject, consider the remarks by the then Governor Ben S. Bernanke (of the Federal Reserve Board), before the National Economists Club, Washington, D.C., November 21, 2002: "Like Gold, U.S. dollars have value only to the extent that they are strictly limited in supply. But the U.S. government has a technology, called a printing press (or, today, its electronic equivalent), that allows it to produce as many U.S. dollars as it wishes at essentially no cost. By increasing the number of U.S. dollars in circulation, or even by credibly threatening to do so, the U.S. government can also reduce the value of a dollar in terms of goods and services."

Gold is more than an investment. It is a diversification and risk management tool –essential for a balanced portfolio.

GOLD OWNERSHIP: BULLION OR STOCKS?

Assuming you have already decided to own Gold to diversify your overall portfolio, you may then ask the following question. What form of Gold should I purchase? Should I buy physical metal such as bullion coins or bars, or would mining stocks be better? It is often recommended by portfolio managers to own a combination of both physical metal and mining shares to maximize performance, and minimize risk. Owning physical metal enjoys certain advantages over owning the mining stocks and vice-versa, but a combination provides the best way to protect and grow a portfolio in difficult and uncertain financial times. Gold investors must choose for themselves how to split up their Gold allocation. It is important for investors to be certain that the Gold items they own are the ones that will best serve their purposes. While each investor's circumstances are different, the discussion that follows should give some ideas on how to best divide Gold holdings. What are the differences between owning physical metal and owning stocks? The obvious difference is risk. On the investment pyramid of risk, physical ownership of Gold would be on the lowest tier (least risk) with cash and life insurance, while ownership of Gold mining shares would be classified on the second or third tiers (higher risk) depending on whether you own shares relating to a major Gold producer or a junior mining company. In general terms, owning physical metal is more of a "saving", whilst owning mining shares would be considered more of an "investment". There is an increase in risk when investing in stocks. However, with increased risk comes greater opportunity for return. Thus both should be considered. A second factor to remember is that a Gold mining share is not Gold. It is a company stock first and then secondly can be construed as Gold. A Gold mining share is NOT a substitute for the physical metal. It represents a claim against potential Gold deposits in the ground and not the actual Gold itself. Stock ownership often has inherent risks that are associated with investing in company stock. Stocks often represent debts, liabilities, risks – monetary, environmental, political, etc. Physical Gold is an asset, the only financial asset that is not simultaneously someone else's liability. Owning physical Gold is essentially risk-free as long as you retain possession. Obviously its value can go up or down according to market fundamentals/fluctuations, but you can hold it securely in your hands. Physical Gold does not need cash flow or management to insure its ultimate survival. During a bull market in Gold, the physical metal prices will go higher, but the Gold mining shares are leveraged to the physical price. In other words, as the price of Gold rises, profits from mining stocks rise even more in percentage terms. Generally, over the longer term, the share prices of the major Gold producers rise by a factor of two to three times more than the price of Gold. Successful early stage junior mining and exploration companies can rise by a factor of 5 to 10 times more than the price of Gold. The reason for this leverage is that a rising Gold prices do not have any effect on the cost of production. Therefore, for companies that are already profitable, incremental revenues received from selling Gold at a higher price flow straight to the bottom line. A price rise also increases the value of "in the ground" reserves without capital investments. For mining companies that are not profitable, a rise in the Gold price can suddenly lift them into profitability. Any potential investors would need to consider what their objectives are for considering Gold before they can correctly decide what class of items to purchase. Some people who are more savings oriented, tend to emphasize owning the metal, while others who are looking to make a big return would tend to emphasize the mining stocks. Mining stocks can produce spectacular returns at times, but can also exhibit volatility.

Gold has been used as money for a thousend years. Even today, it remains the ultimate currency.

Some other items to consider:

I Physical Gold ownership does not pay dividends. Mining stocks can pay dividends when profitable.

II Physical Gold ownership has protected investors during periods of economic depression, wars and political unrest. Mining stocks could be negatively affected in such times as stock markets may be closed or adversely affected for a time.

III Physical Gold can be used for barter or purchasing life sustaining items during crisis times. Mining shares would be harder to use for such purposes.

WHY INVEST IN JUNIOR & EXPLORATION COMPANIES?

Leverage is the simple answer. It is not uncommon for early stage junior mining and exploration companies (hereafter, Juniors) to experience huge gains (10 times or more) very quickly as news of a discovery is made. Consider the following facts: In the mining world, it is no secret that the majority of economic mineral deposits are found by the junior mining companies or prospectors. There are several reasons for this. Junior explorers are not slow-moving bureaucracies like many established and large resource companies (hereafter "Seniors"). This makes Juniors able to make fast decisions both in the boardroom and in the field. Seniors generally have a different role to play, namely, to fund and place into production deposits discovered and developed by Juniors. But perhaps chief amongst the most important reason Juniors tend to make most discoveries is that they are hungry and entrepreneurial, in other words: the talent, motivation and dedication of their management team. Exploration is, to some extent, a creative enterprise. It is often said in the mining business, that if an exploration geologist finds a mine it is likely that he will find others. It is a fact that fewer than 5% of all exploration geologists will ever have the credit of a discovery that leads to a mine, which proceeds to the production stage. This is because those few select, gifted explorers who find numerous mines, seem to possess a sixth sense that moves them to succeed in this area. Most of the true and successful leaders in mineral exploration are geologists that don't necessarily fit into the corporate culture. They are field geologists who do not generally sit behind desks, stare at computer monitors and talk on the phone, preferring instead to be out in the field. Whilst the majority of geologists may have a firm grip on the theory of mineral exploration, they cannot take it to the next level to unravel Mother Nature's secrets. As is often the case Juniors are managed by men and women who have had success working for both Senior and other Junior companies. So why would someone want to be a director of a junior mining company that has no revenue and sometimes not even a decent salary to offer? It is the potentially huge rewards that can come when a discovery is made that attracts the top talent of the mining sector into the Juniors. In other words, they want to work for themselves and get the big payoff, instead of earning a nice salary with some kudos if they made the discovery whilst working for a Senior company. In a major mining company, a successful exploration geologist who made a significant discovery might get a pat on the back and a new credenza, if they're lucky. As part of a junior mining company, the geologist who made that same discovery might profit considerably from the $10 million, $20 million, or a $100 million capital gain from any discovery made on the part of their efforts. In the life cycle of a mining share, it is the exploration phase that provides the biggest move (leverage) in share price. The best and brightest ´´mine-finders´´ of course know this and are highly motivated to search the world over to make a new discovery. When they do, the monetary rewards are substantial, for both the management team and its investors. Over the last few years, very little major corporate mining money has been going into the search for new deposits. Exploration expenditures declined drastically from 1997 into 2001 as the brunt of the bear market took its toll. Since then, we have seen the start of what looks to be a major bull market in the precious and base metals. Exploration budgets are cranking up again as the search for new deposits is greatly needed to replenish depleting reserves. With this renewed interest in exploration, demand for good exploration companies is increasing in the capital markets and the junior mining sector is once again showing spectacular gains. As the spot prices of the minerals continue to rise, we are also likely to see an exponential rise in the share prices as additional capital comes their way. Richard Russell (a prominent writer on mining and commodities investments), has this to say about the current bull market in precious metals: "..I believe that fortunes will be made in the years ahead by those who are now establishing major positions in Gold and Gold shares. These primary moves last longer than anyone thinks possible – and they take the items higher than anyone thinks possible. We are now in a primary bull market in Gold. I believe Gold (and very probably silver) will make fortunes for those who now take major positions in the precious metals"

Huge Leverage

The increase in the mineral prices not only focuses more attention on the sector, but also causes even more money to be spent on exploration thereby increasing the probability of finding new deposits. It also increases the value of any potential discovery through leverage. Mineral deposits are gauged, in financial terms, by the ``Net Present Value of Future Cash Flows`` formula should the deposit be mined. Say for example we find a million ounce deposit of Gold and an engineering study suggests it could be mined over ten years at a cost of $250 an ounce, including capital. For the purposes of the example let's assume Gold is at the unrealistically low level of $350 an ounce. Lets also assume a 10% discount rate (over 10 years) and we find that the deposit would be worth roughly $70 million. However if the Gold price were to increase to $400 an ounce (a 15% increase) the value of the same Gold (with the same parameters) increases to $100 million (almost 50%). That is over 300% leverage to the Gold price. Increases, obviously, have an increment benefit.

Suggestions for Gold Investors

Options for acquiring Gold can take several forms. Investors interested in Gold may want to consider investments in Gold producing companies either as an alternative to or along with any bullion type of investment. Improved sentiment towards precious metals is producing an equity financing boom for Gold companies, from substantial producers to junior explorers. There is a tremendous demand for Gold shares at the moment. The Gold price is rising and many astute investors are turning to the smaller Junior Gold mining companies that enjoy a debt free history, un-hedged production and large reserves still to be mined. Many investors feel these smaller mining companies will continue to reflect the movement of Gold as it continues to advance, albeit without the unnecessary risks attributed to investments in both the bullion and futures markets. While Gold continues to rise, the search is on to find these Juniors still in an early stage of growth. In addition, a race is on by the Seniors to take over smaller mining companies holding proven reserves, and investments in Seniors which have recently acquired large reserves should also be considered. With the expectation of aggressive returns, however, great attention must be paid to the technical factors of: yields, testing results, reserves and operational cost(s).

THE FUNDAMENTAL REASONS TO INVEST IN GOLD: A RECAP

I Global Currency Debasement

The US dollar is fundamentally and technically very weak and could fall dramatically. However, other countries are very reluctant to see their currencies appreciate and are resisting the current fall of the US dollar. Thus, we could be in the early stages of a massive global currency debasement, which may see tangibles, and most particularly Gold, rise significantly in price.

II Invest Demand

Many experts believe that, when the retail investing public recognizes what is unfolding, they will seek an alternative to paper currencies and financial assets and this will create an enormous investment demand for Gold. Under such circumstances, it may be prudent to own both the physical metal and select mining shares.

III Financial Deterioration in the US

In the space of a few years, the United States Federal Government budget surplus has been transformed into a yawning deficit, which has all the signs of persisting. At the same time, the current account deficit has reached levels which historically portend continued weakness in the United States.

IV Dramatic Increases in Money Supply in the US and Other Nations

US authorities are concerned about the prospects for deflation given the unprecedented debt in the US. Fed Governor Ben Bernanke is on record as saying the Fed has the ability to issue new currency and will use it to combat deflation if necessary. Other nations are following in the US's footsteps and global money supply is accelerating. Historically, this can create a very "Gold friendly" environment.

V **Existence of a Huge and Growing Gap between Mine Supply and Traditional Demand**

Gold mined is roughly 2500 tons per annum, and traditional demand (jewelry, industrial users, etc.) has continued to exceed this by a considerable margin for a number of years. Some of this shortfall has been filled by Gold recycling, but selling from various Central Banks has been a primary source of above-ground supply.

VI **Mine Supply is Anticipated to Decline in the Next Two to Three Years.**

A combination of traditional demand continuing to exceed mine supply, buying prompted by ongoing worldwide economic weakness, and an expected decline in mine supply, may very well lead to greater mid-term shortages. Mine supply will contract in the next several years, irrespective of Gold prices, due to a shift away from high grading (which was necessary for survival in the sub-economic Gold price environment of the last decade), and the natural exhaustion of existing mines, and environmental pressures on cleaner mining processes.

VII **Large Short Positions**

To fill the gap between mine supply and demand, Central Bank Gold has been mobilized primarily through the leasing mechanism, which facilitated producer hedging and financial speculation. Some evidence suggests that between 10,000 and 16,000 tones (perhaps as much as 30-50% of all Central Bank Gold) is currently in the market. This is owed to the Central Banks by the bullion banks, which are the counter party in the transactions.

VIII **Low Interest Rates Discourage Hedging**

Interest rates are low. With low rates, there isn't sufficient impetus to create higher prices in the out years. Thus there is incentive to hedge and Gold producers are not only not hedging, but are reducing their existing hedge positions, the resultant effect of which is removing Gold from the market.

IX **Rising Gold Prices and Low Interest Rates Discourage Financial Speculation on the Short Side.**

When Gold prices were continuously falling and financial speculators could access Central Bank Gold at a minimal leasing rate (0.5 – 1% per annum), sell it and reinvest the proceeds in a high yielding bond or Treasury bill, the trade was viewed as a lay-up. Everyone did it and now there are numerous stale short positions, which must be filled with actual purchases. However, these types of trades now no longer make sense with a rising Gold price and declining interest rates.

In the mining World, the majority of Gold deposits are found by junior mining companies. They provide better leverage and potential for long term investors.

Investors interested in Gold may also want to consider investments in Gold producing companies.

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XIV The Central Banks are nearing an Inflection Point when they will be Reluctant to Provide more Gold to the Market.

Far Eastern Central Banks who are accumulating enormous quantities of US Dollars are rumored to be buyers of Gold to diversify away from the US Dollar.

XV Gold is Increasing in Popularity

Gold is seen in a much more positive light in countries beginning to come to the forefront on the world economic scene. Prominent developing countries such as China, India and Russia have been accumulating Gold. In fact, China with its 1.3 billion people recently established a National Gold Exchange and relaxed control over the asset. Demand in China is expected to rise sharply and could reach 500 tons over the next few years.

XVI Gold as Money is Gaining Credence

Islamic nations are investigating a currency backed by Gold (the Gold Dinar). The new President of Argentina proposed, during his campaign, a Gold backed peso as an antidote for the financial catastrophe which his country has experienced, and Russia is talking about a fully convertible currency with Gold backing.

XVII Limited Size of the Total Gold Market Provides Tremendous Leverage

All the physical Gold in existence is worth somewhat more than $1 trillion US Dollars while the value of all the publicly traded Gold companies in the world is less than $100 billion US dollars. When the fundamentals ultimately encourage a strong flow of capital towards Gold and Gold equities, the trillions upon trillions worth of paper money could propel both to unfathomably high levels.

CONCLUSION

Gold is under-valued, under-owned and under-appreciated as an investment tool. It is most assuredly not well understood by most investors. At the beginning of the 1970's when Gold was about to undertake its historic move from $35 per oz to $800 per oz in the succeeding ten years, the same observations would have been valid. The only difference this time is that the fundamentals for Gold appear to be better.