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Gold Reaches For Highs Not Seen Since 1980

By Jon Nadler

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Gold prices staged an explosive rally on the last trading day of the week, making Monday's half-hearted attempt at a correction a distant memory. Growing apprehensions about Iran and Turkey took center-stage in the consciousness of investors today. The backdrop of a feeble dollar (77 on the index has now broken) and the assumption that the Fed will cut rates once again next week contributed to the boldness among gold bulls.

Price gains remained robust during the trading session despite massively overbought conditions, record open interest and large net speculative long positions. When it comes to warfare (possible, or actual), the price premia that gold is capable of bearing can be counted on quite reliably. The metal has surged more than \$100 since the beginning of September and it did so without any meaningful pullbacks, to date. Some see a replay of 1980 taking place here. We see very active funds, largely ignorant mainstream investors, and a (sure-to-come) surge of trend-following late entrants lured by the headlines that gold will likely make over the weekend.

Spot prices closed on day's highs, gaining \$16.50 to \$783.50 bid, as market participants continued to focus on not only the set of harsh US sanctions levied against Iran yesterday, but also on Tehran's sharply defiant response to the imposition of same. In the interim, more Turkish troops were seen massing on the Iraq border and that fact also added to the volatile geopolitical mixture that has had speculative-minded bullion buyers afire.

Most observers have little doubt that crude oil supplies would encounter some form of disruption, were some direct conflict in the region to, in fact, take the place of the present, loud, saber-rattling. As a result, we saw new records being carved out in that market as well (at over \$92 per barrel). Silver also picked up some safe-haven buyers and gained 32 cents to \$14.14

while platinum gained \$9 to \$1454.00 per ounce, on its own supply worries.

"I don't think I've ever seen such an explosive market without a major correction," said Phil Flynn, senior trader at Alaron Trading Corp. in Chicago. "There is a combination of factors that continue to send prices higher and we've run out of bearish news." Mind you, that was an observation that Mr. Flynn made about the oil market earlier today to Bloomberg. However, you can safely take his quote and apply it in equal measure to the gold market at this time.

One of the factors that ought not to be ignored at this juncture is the emerging possibility of an economic recession in the US and its related (and likely) effects on markets - including commodities. Consider for example the findings of the San Francisco Chronicle which reports that:

"More than \$23.6 billion in California housing wealth will evaporate if real estate prices continue to decline and foreclosures on subprime home loans soar, according to a new congressional report that indicates the fallout from the national mortgage crisis is worsening. Nationally, some 2 million homes representing \$71 billion in housing wealth - coupled with \$32 billion in depressed values on nearby homes - and \$917 million in property tax revenue are at risk."

This state of affairs has led some economists to raise the "R"-word flag at the top of the lookout towers. Jon Haveman, a former senior economist with the president's Council of Economic Advisers, observes that:

"Things are getting exponentially worse," said Haveman, a principal at Beacon Economics in San Rafael. Home prices "have only now started to drop. They have a ways to go."

Haveman expects the housing slump to touch off a recession by the beginning of next year, because more than 70 percent of U.S. spending is by consumers.

"There's been a dramatic increase in consumer spending fueled by the housing market," he said. "Now that housing prices are going down, (consumers are) going to have to reorient their household portfolio. They're going to have to start saving because their retirement isn't going to come out of the house. And they have to stop consuming because there's no more cash in their house."

Such potential outcomes cannot but ultimately impact base and precious metals consumption in the world's largest economy. The US is the second largest consumer of gold after India. While gold may ultimately still benefit from a reorientation of investment priorities, the initial stages of a contractive phase in the economy could have an adverse effect on the value of everything.

Volatile conditions will persist as the stampede continues without serious pause. This surge remains a speculative and largely fund-driven bet and it requires a strong physical and financial

constitution for any participant. Conditions could turn on a dime. The prospect of a \$50-\$75 move in either direction should not be discounted as we navigate through largely uncharted and very turbulent waters. Some portion (possibly large) of such moves may well take place within a single session on the market floor. Look for bid/ask spreads to widen, if nothing else. However, surely, you may look for much else, as well.

Mr. Nadler's gold market commentaries on the gold market are quoted on a regular basis by the mainstream U.S., Canadian, and global financial media including MarketWatch, Forbes.com, and Associated Press to name a few. His expertise is in the area of consumer education in precious metals.