

Commodity Ratios: The Investing Truth They Reveal

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As gold prices near new highs, some are calling gold's skyrocket success a bubble. However, informed investors are seeing it differently; gold is not much more expensive than its 1980 levels, even despite runaway growth in the money supply over the past 30 years.

Gold's High and Silver's Ratio

As we well know, gold and silver often trade within a reasonable ratio to each other, ranging anywhere from 15:1 to 70:1. Currently, the ratio is near its highs at 66:1 and is now more than four times higher than its historical low. While gold may have traveled too high too quickly, silver looks even better as time progresses.

Other Ratios

There are plenty of other ratios that come into play than just the gold to silver ratio. One popular ratio is the Dow:gold ratio, as well as the oil:gold ratio.

Recently, the oil to gold ratio has become more mainstream, mostly due to economic issues that have largely thrown the Dow:gold ratio off its course. The gold to oil ratio is very important for silver investors, as well as gold and oil investors, because it helps establish a baseline for what current prices should be, allowing silver investors to extrapolate their own numbers.

Oil to Gold Ratio

The oil to gold ratio is more volatile than others, mostly due to the fact that they tend to rise and fall in tandem in the long term; however, short term divergence in price changes has a lasting impact on the ratio. For instance, although gold and oil are both inflationary plays, gold was as high as \$870 an ounce and rising at the start of 2009, while oil prices were coming off their lows in the \$40 per barrel range. This short term fluctuation pushed the ratio well off its course, despite the fact that both should trend in the same general direction.

Regardless, gold and oil often retain a healthy ratio of anywhere between 8 barrels to 30 barrels of oil per 1 ounce of gold. Currently, the ratio resides at an extremely healthy 15:1, right in line with historical averages, showing that neither gold nor oil is bubbling. In fact, they are about as average in price as history has allowed.

Silver: The Common Denominator

Having already established that neither gold nor oil is in a bubble, it is now time to add silver into our mathematical mix. Although gold appears expensive when compared with the historical average of silver prices, it is not that gold is overpriced. Rather, silver is easily underpriced compared to both gold and oil and should be well poised for a rally.

It is commonly understood by investors that gold, silver and oil are all inflation hedges; thus, for institutional investors, each is interchangeable. However, profits generated from each are not always proportional, as often times the prices of one can diverge from each other, creating better

profit potential in one commodity as opposed to another. In the present case, silver remains the best anti-inflationary investment, being undervalued both to gold and silver – all while maintaining the same positive fundamentals.

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