

Obama/Bernanke policies ultimate gold price drivers

With U.S. government policy aimed at turning deflation into inflation, Rick Mills believes gold will be one of the major beneficiaries.

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COQUITLAM, BC (AHEAD OF THE HERD) -

Investors are starting to realize that gold is a storehouse of value and a safe haven in times of turmoil. Gold's price has risen because of the abuse and mismanagement of our monetary and currency systems - throughout history, gold has always shone the brightest when trust breaks down, confidence falls and fear climbs.

Latest demand statistics from the World Gold Council:

- Total gold demand in Q2 2010 rose by 36% to 1,050 tonnes
- Investment demand posted a rise of 118% to 534.4 tonnes
- With the return of demand for consumer electronics, industrial demand grew by 14% to 107.2 tonnes, compared to Q2 2009

The Dow on gold's terms is telling everybody something important is happening. I published "Silver, Two of Seven" just three weeks ago, in that article I included the following:

"In 2000 gold made its \$260 per ounce low, in January 2000 the Dow was 10,900

10,900 / \$260 per ounce = 41.9 ounces to buy the Dow

Today at 10,447 DJII and \$1,250 gold it's 8.53 oz to buy the Dow."

As I write this, the Dow:Gold Ratio is $10,447 / \$1250 = 8.35$ oz. Chart from earthlink.com



After being the best performing major asset of the last decade, is the price of gold going to continue higher?

On January 21st 1980 gold closed at US\$850 an oz. According to Adam Hamilton of Zeal Intelligence, who uses the Consumer Price Index to recast historical gold prices into today's inflated dollars. The gold price today would have to be US\$2358 to match gold's nominal high in 1980. So according to Mr. Hamilton's figures we aren't even close to receiving full value on our gold. And not surprisingly Tier One gold producers aren't either.

According to Michael Curran, an RBC Dominion Securities analyst, the average discounted gold price among North American Tier 1 producers is \$915 an ounce - gold is currently trading at US\$1250 an oz.

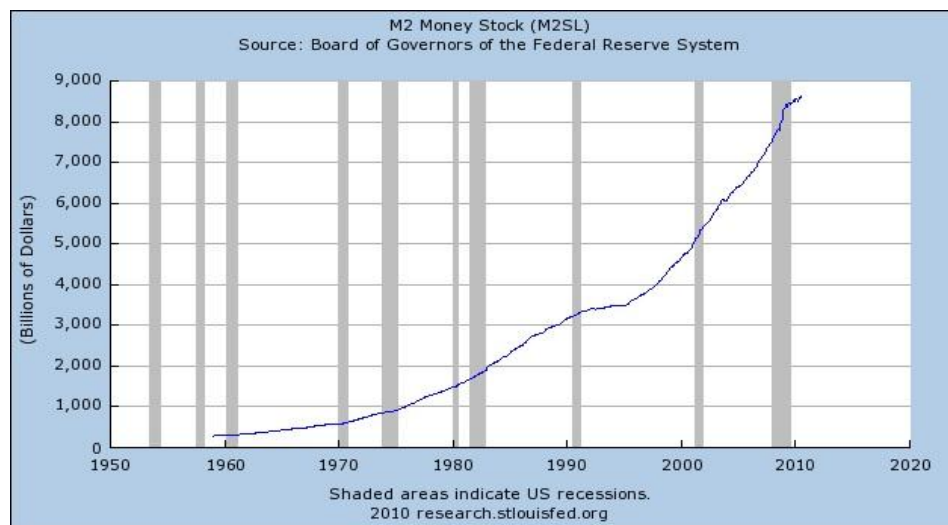
There presently exists today reasonable, sound, and at least as far as I'm concerned, convincing arguments, that both gold and gold stocks, or at least Tier one producers, are undervalued.

Considering the seasonally strong period for gold and gold stocks is right around the corner, they might be even more undervalued than we think.

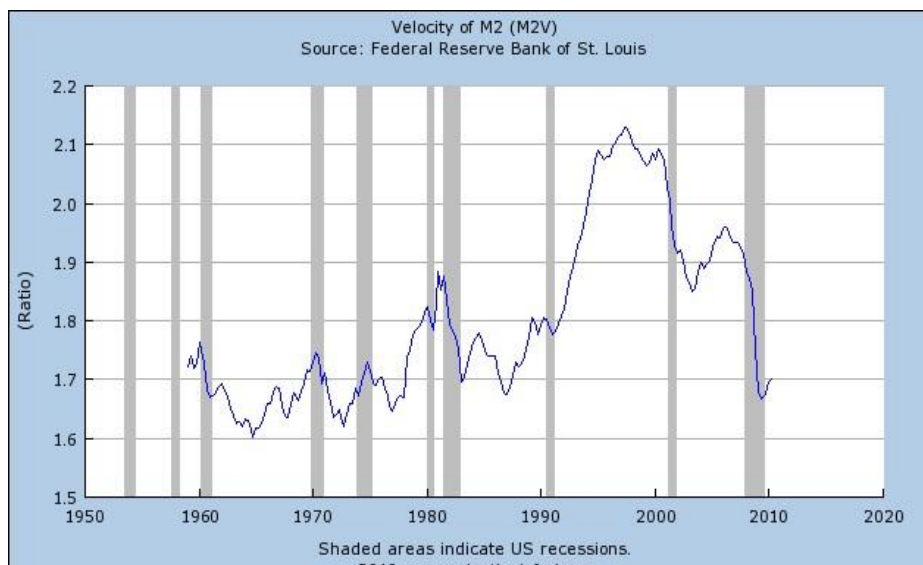
Current head of the Federal Reserve is Ben Bernanke, he's an economist and a student of the Great Depression.

Bernanke thinks he knows how to turn deflation into inflation - throw massive amounts of cash at the economy and don't worry about the dollar's value, not yet anyway. Just get all that money out there and deflation will disappear and in its place will be very much welcomed, by the government anyway, inflation.

And this is exactly what is happening today, massive cash injections to stimulate practically every sector of the economy.



What's interesting at this point of the game is to look back in time a bit and realize how Ben "Helicopter" Bernanke got his nickname. He once made light of the fact that to combat deflation, if worst came to worst, he could always throw money out of a helicopter. What he was getting at was, if previous efforts had failed, and they mostly have (at best all he can claim is 'it could be worse'), if the American consumer had retrenched, wasn't spending but was saving money (and paying down debt), banks weren't lending and businesses weren't borrowing and growing (creating jobs) - much like conditions today - then to stimulate spending he, Bernanke, would literally throw money out of a helicopter to consumers and get them spending again. All this new money being spent would cause the wanted inflation in a great enough amount to reverse deflation.



When we talk about the velocity of money, we are speaking of the average frequency a dollar is spent. If nobody is spending money the velocity is zero.

There's a lot of ways the Fed could get this accomplished (buying stocks, guaranteeing mortgages), and some of these methods are starting to be employed, with debt relief/forgiveness being on top of the list. The Fed realizes a lot of money is trapped in bank coffers and isn't going to be loaned out to businesses and individuals (instead the banks take the free 0 percent money from the Fed, leverage it 10:1, and buy US Treasury Bonds at 4 percent interest). They also understand that you can lead a horse to water but can't make him drink, meaning you can shovel money to the consumer but till he's comfortable with his level of debt he'll pay off that debt and then and only then, spend.

*"The Committee is prepared to provide additional monetary accommodation through **unconventional measures** if it proves necessary, especially if the outlook were to deteriorate significantly."* Ben Bernanke, Chairman of the Federal Reserve

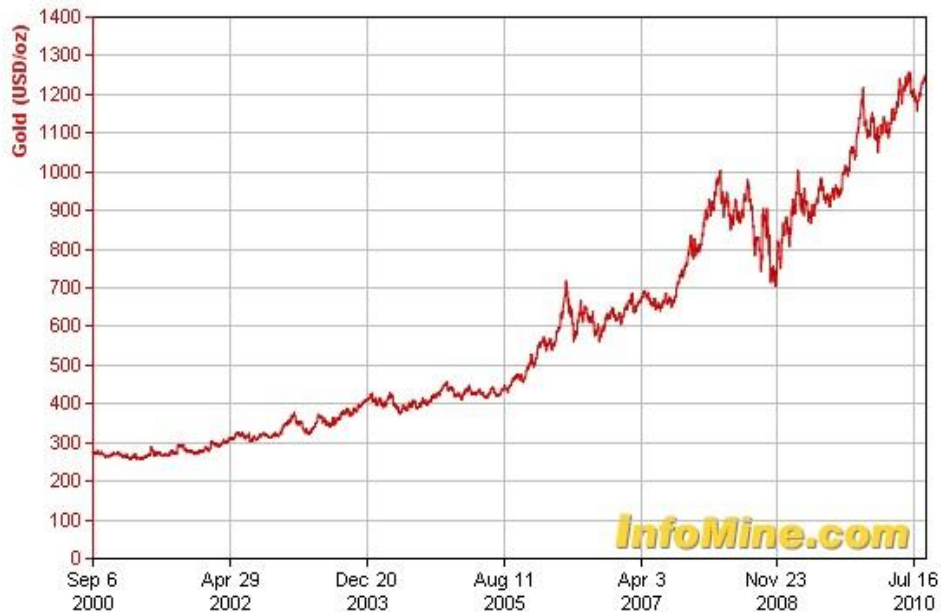
The next round of stimulus, and there will be another round, is going to be aimed squarely at consumers - dropping money out of helicopters.

Money will, it's a matter of when not if, begin to flow and circulate through the economy again. I believe we're heading, over the next few years, to a very inflationary environment.

The real threat facing us today, in my opinion, is the coming rise in prices, for all things, caused by the ongoing world-wide increase in the monetary base. I'm not sure how long it will take for all the money creation to work its way through the pipeline but this author definitely believes its coming. With U.S. President Obama promising trillion dollar deficits for years to come (estimates from the White House predicts the budget deficit will reach a record \$1.47 trillion this year - the government is borrowing 41cents of every dollar it spends. Next year's budget deficit is predicted at \$1.42 trillion, that's 37 cents of borrowing for every dollar spent), with all exporting countries trying to keep their currencies weak to make their exports competitive and with Bernanke throwing money out of helicopters - once my anticipated inflation starts it isn't going to stop anytime soon. I believe when investors wake up to this fact we'll see a flood of money, a virtual herd of investors, stampeding into all things gold.

It presently would be very hard to mount an argument against gold being clearly the winning major investment of this decade.

GOLD
10 YEARS (Sep 6, 2000 - Sep 5, 2010)



With the price of gold at US\$1250 it's definitely living up to its oft proven history of acting as a safe haven in times of turmoil.

But what happens to our gold investments when "deflation" turns to inflation? Does gold serve us as well in an inflationary environment as it's serving now?

Gold shines brightest in inflationary times. The ongoing deflationary scare could be a buying opportunity for gold but especially for those undervalued gold company shares.

History proves the greatest leverage to a rising gold price is gold mining stocks.

I think gold juniors are going to be the most rewarding, the most lucrative way to garner the huge rewards from the coming freight train rush to gold. Those golden tracks are being laid today using the world's currencies as ballast - when your cash is trash your gold is shining.

There will be fierce merger and acquisition (M&A) competition for the juniors with stable safe gold ounces in the ground by producers having to replace their reserves in an extremely competitive environment. There aren't very many decent sized deposits, ones over two million ounces, left in politically stable countries.

Monetary and fiscal authorities around the world are setting us up for an inflationary cycle. This will be the ultimate driver of the gold bull market going forward.