

Investors Get A Midas Touch

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Gold coins and gold bars on display at California Numismatic Investments, in Inglewood Calif. Gold has soared to record levels this year as investors... [View Enlarged Image](#)

Gold demand is strong during times of economic weakness and geopolitical uncertainty, which exists today.

"Gold is like a financial and monetary Geiger counter," said Jeff Clark, editor of Casey Research, an investment advisory firm. "It measures the health of your economy and money. It's the safe currency in times of trouble."

That trend has helped propel stocks of companies that mine gold and other precious elements. As of Friday, the gold, silver and gem mining sector ranked No. 12 among IBD's 197 Industry Groups, up from No. 104 a month ago.

1. Business

Gold and silver mining companies extract ore from the ground, which is then processed and sold at market prices.

The mining of gold is getting harder, while the grades of gold quality have declined. Fewer rich deposits have been discovered, putting constraints on future new supply.

Gold prices have been reaching new highs as investors accumulate bullion on fears of a worsening economic outlook. High levels of debt on government balance sheets and concerns that the global economy may be heading toward a double-dip recession are driving prices higher.

After reporting first-quarter results on April 27, Newmont Mining (NEM) CEO Richard O'Brien said sustained investor purchases of gold and healthy demand for gold jewelry from India and China are among the reasons it remains bullish on metal prices.

"Extra supply is not being pushed into the market, causing supply to tighten even further," he said in a conference call.

Mine supply will also remain constrained due to declining grades of global purchases, he said.

On the demand side, many developing economies are recovering faster than developed countries, especially in China and India, which are key markets for buying gold.

Name Of The Game: Mining companies earn a profit on the difference between the cost of producing an ounce of gold or silver and the price they get for it. The keys: acquiring the best properties and mining efficiently.

2. Market

The largest group of buyers today include finance-minded investors, banks and governments. The second-largest market is for jewelry. The third-largest purchasers are industrial companies that use it in their products.

The World Gold Council expects strong demand for gold this year, driven by jewelry purchases in India and China and investors in Europe and the U.S.

The average price for gold in the first quarter was \$1,109, up 22% from a year ago. Gold currently trades around \$1,200 per ounce.

Until a few years ago, jewelry demand accounted for most of the market. Now the bulk of demand is from investors. Investment demand nearly doubled in 2009 from 2007 to about 45% of the market, while jewelry demand fell from about 65% to about 44%. Industrial use is around 10%.

Investors bought 5.6 net tons of gold through exchange traded funds in the first quarter, bringing the total of gold to a record 1,768 tons worth \$63.4 billion at the quarter-ended gold price, according to WGC.

Gold ETFs trade on the major exchanges worldwide. They purchase and store large amounts of gold and issue shares that rise or fall with the price of gold bullion.

The biggest gold ETF is SPDR Gold Trust (GLD), which tracks the price of gold bullion. Market Vectors Gold Miners (GDX) follows an index of gold mining companies that include Barrick Gold (ABX) and Newmont.

Silver also has its slate of ETFs, including iShares Silver Trust (SLV) and Global X Silver Miners (SIL).

Investors can also buy gold coins such as the U.S. Treasury Department's American Eagle series.

A recent report by Bank of America Securities-Merrill Lynch forecasts average gold prices of \$1,200 per ounce this year, \$1,350 in 2011, and

Gold has been used in everything from ornamental toilets to dental fillings to home electronics, hoarded by investors in times of worry and adored as gifts.

"It's been in demand as a medium of value since the time of Sumerians roughly 3,000 years ago," said Thomas Winmill of the Midas Fund , which invests in securities of companies involved in mining, processing and distributing gold, silver and other natural resources.

"For one reason or another, people have sought to possess gold. It has extraordinary properties. It doesn't corrode or tarnish, it is very malleable and can be beaten into incredibly fine thinness and still maintain its connectedness."

Gold is also cold, hard cash in every corner of the world, no matter what the local currency is.

"Zimbabwe dollars are not universally accepted, but gold is — and always has been," Winmill said.

\$1,400 in 2012.

It also predicts that silver has further upside, with prices averaging \$18 per ounce this year, \$20.25 and 2011 and \$21 in 2012.

Winmill is even more bullish on gold prices.

"We believe gold is set up for a strong run and will end the year at \$1,400," he said.

3. Climate

Like all investments, the price of gold is driven by supply and demand.

"On the whole, the potential demand for gold far exceeds new supplies," said Winmill. "It can be hard to predict. The supply is still steady. The demand is the wild card."

In 2009, central banks and official institutions as a whole became net buyers rather than sellers of gold. Russia bought 8 tons of gold in the first quarter, and has been adding to its gold reserves for several years. Last year, China announced it had added 454 tons to its gold reserves since 2003, a 76% increase. China's demand for gold is set to double in tonnage within the next 10 years, according to the World Gold Council.

China has rapidly become a prominent gold market. Chinese gold consumption was more than \$14 billion in 2009, or 11% of global demand.

Central banks have been buying gold as a safe haven. The existence of gold reserves can increase public confidence in a central bank.

"Countries and central banks continue to buy gold," said Clark. "Its reputation as a safe haven is being increasingly recognized."

The U.S. has by far the highest gold reserves, followed by Germany, Italy, France and Switzerland.

4. Technology

Technology has played a key role in extracting gold and silver. Modern mining equipment and techniques enable miners to work faster and more efficiently.

As much as technology has benefited gold, the metal plays a crucial role in electronics, medical fields and other industries.

Gold is a well-established material in the electronics industry. Because of its unique physical and chemical properties, gold is expected to play a critical role in the development of nanotechnology.

Gold also sits at the core of many scientific and commercial breakthroughs to address problems ranging from treating cancer to combating climate change.

Other applications for gold in the technology field include fuel cells, solar cells, touch screens and high-density data storage and batteries.

5. Outlook

The World Gold Council expects strong demand for gold as rising public debt levels in the U.S. and Europe push investors to safe havens.

And if the economy does recover, jewelry demand could rise in the U.S. and Europe as jewelry sellers scramble to refill depleted inventories.

"What becomes clear is that gold's continuing upward price trend is anchored in solid fundamentals," Juan Carlos Artigas, World Gold Council investment research manager, said in a statement based on first-quarter results.

Upside: Events of the last few years have highlighted gold's advantage to central banks and investors, making widespread selling in the near future unlikely.

Risks: If governments solve their problem and economies stabilize, gold prices will likely fall.

"If economies get better and people believe they will get better, and if the dollar continues to be strong against (the) euro, and if inflation is less than expected — those are the risks of owning gold," Clark said.