

The Gold Rush

With the economic slowdown in the U.S. many investors are left pondering on the best means by which to preserve their wealth. The declining U.S. dollar, rising fuel prices, decreasing payrolls and the drop in home prices has without a doubt left investors contemplating alternative avenues to protect themselves in the wake of economic uncertainty. One such alternative is that of investing in gold. The precious metal is being turned to by investors as a safe haven amidst the economic turmoil currently being experienced in the U.S. Investors however, should tread cautiously as the price of this valuable commodity is very sensitive to political and economic events and trading in this market entails substantial risks. This coupled with the fact that gold prices have recently soared to record highs suggests that investors need to also bear in mind that this upward surge in prices is not guaranteed to continue.

Gold futures reached as high as \$1,001.50 an ounce on March 13, surpassing the \$1,000 an ounce level for the first time. At the time of writing this article (March 17), gold futures for April delivery rose \$3.10, or 0.3 per cent, to \$1,002.60 an ounce on the New York Mercantile Exchange. Last year the price of gold increased 32 per cent and for the year, gold is up 20 per cent as at March 14.



Source: *Global Insight, WGC (Fig 1)*

Regarded as a symbol of wealth and an integral part of world history, gold today is easily accessible to the average investor. Today individuals can invest in this precious metal through various means: gold coin and bullion, gold exchange traded funds, gold futures, and by investing directly in mining companies to name a few.

While gold coins and bullion can be purchased directly from a dealer, the emergence of sophisticated financial instruments such as exchange traded funds and futures, allow an investor direct exposure to the valuable commodity. Gold Exchange Traded Funds (GETFs), which track the price movements of gold, are traded on the major stock exchanges and are usually referred to

as Exchange Traded Gold. Some of these major stock exchanges include The Australian Securities Exchange (ASX: GOLD), The London Stock Exchange (LSE: GBS), The New York Stock Exchange (NYSE: GLD) and The JSE Limited (JSE: GLD), previously Johannesburg Securities Exchange, which is the only full services securities exchange in South Africa.

	Product Name	Total Tonnes	Total Ounces	Total Value
New York Stock Exchange Arca (NYSE Arca) AND Singapore Exchange (SGX)	StreetTRACKS Gold Shares	652.48	20,977,756	US\$ 20,869m
London Stock Exchange (LSE) AND Euronext Paris AND Borsa Italiana AND Frankfurter Wertpapierbörse (Deutsche Börse)	Gold Bullion Securities	112.85	3,628,164	US\$ 3,623m
Australian Stock Exchange (ASX)	Gold Bullion Securities	19.57	628,793	US\$ 628m
Johannesburg Securities Exchange (JSE)	New Gold Debentures	28.24	908,036	US\$ 903m

Source: *Exchange Traded Gold (Fig 2)*

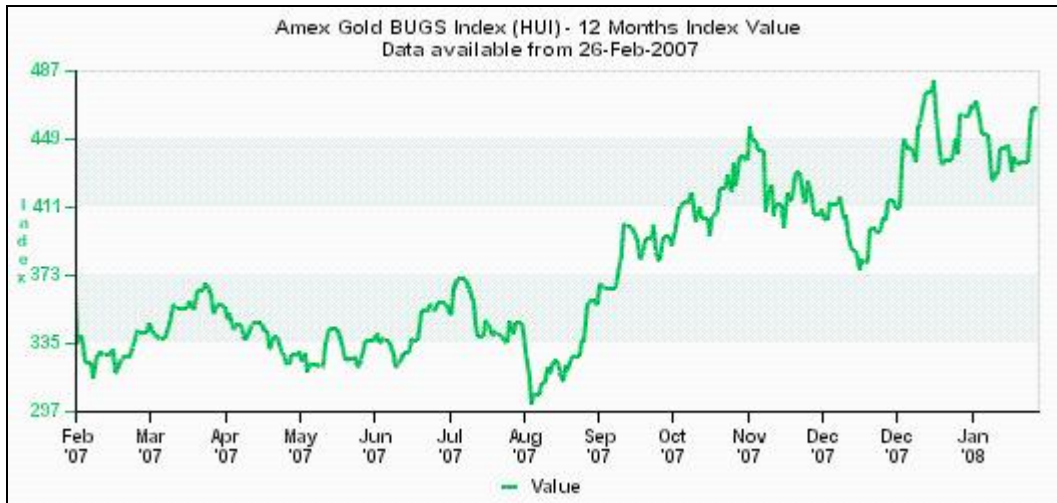
On March 17, the StreetTRACKS Gold shares (GLD) gained 0.47 per cent to US\$99.17, and the Luxor Gold Bullion Securities (GBS) advanced 1.19 per cent to US\$99.58.

Another medium for investors interested in trading in the yellow metal is that of futures. A futures contract is an agreement between two parties for the delivery of an underlying commodity in the future at a specified price. In gold futures contracts, the price is quoted in dollars and cents per troy ounce and the minimum price fluctuation (tick size) is 10 cents per troy ounce.

On the Chicago Board of Trade there are two gold futures contracts: a 100 troy ounce contract and a mini contract of 33.2 troy ounces of gold. Thus if gold is trading at \$1,000 an ounce, the value of a 100 troy ounce futures contract is \$100,000 (100 ounces x \$1,000) while the mini contract would be valued at \$33,200 (33.2 ounces x \$1,000).

On the New York Merchantile Exchange Comex Division there are also two gold futures contracts available: a 100 troy ounce contract and a mini contract of 50 troy ounces. The tick size on the mini contract traded on the NYMEX is 50 cents per ounce.

As previously mentioned, one means by which investors can enter the gold market is by investing directly in mining companies. The American Stock Exchange's Gold BUGS Index (HUI) represents a basket of 15 of the largest gold mining companies that do not hedge their gold positions beyond a year and a half into the future. This Index is up 24 per cent this year. Three of the Index's components, Randgold Resources Limited (GOLD), Barrick Gold Corporation (ABX) and Agnico-Eagles Mines Limited (AEM) have seen substantial increases over the last year. GOLD, which conducts gold mining operations in the gold regions of Africa is up 90 per cent year on year; ABX the largest bullion miner increased 53 per cent while AEM, owner of Canada's biggest gold deposit, rose 79 per cent.



Source: American Stock Exchange (Fig 3)

Another index, the CBOE Gold Index which is composed of 10 companies involved primarily in gold mining and production is also up 24 per cent for the year.

So what makes this lustrous metal so attractive? Investors look towards the gold market for a number of reasons. Investing in gold is considered to be an effective hedge against inflation and a depreciating U.S. dollar. Extensive research from various economists has shown that, over the long term, gold has preserved its purchasing power in times of rising inflation (as evidenced in the U.S. in the 1970s). This is because investors upon realizing that their money is losing value, look to position their portfolios in assets that have in the past maintained its value, such as gold, thereby boosting the demand for the precious metal.

With regards to a declining U.S. dollar, gold becomes cheaper and hence more appealing to global investors who hold currencies that have appreciated relative to the U.S dollar. This in turn creates greater demand for the precious commodity.

To further substantiate this claim, a study conducted in January 2006 by GFMS Limited, on behalf of the World Gold Council, examined how effective commodities would be as a hedge against fluctuations in the U.S. dollar and whether this ability varied across different commodities. The study comprised of 22 different commodities and the analysis revealed that gold is the strongest hedge against the dollar particularly during times of a weakening dollar.

If not for any of the reasons mentioned above, investing in alternative investment vehicles, such as commodities, offers diversification to investors' portfolios.

Given the considerable risk associated in gold trading and the expertise needed to succeed in this market, I caution you to seek the advice of your investment advisor before venturing in this market.

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