

*Gold production has been in decline since it peaked in 2001. Exploration costs have climbed and gold producers have stopped investing*

After all, since the crisis kicked off in August 2007, gold prices are up 7 per cent. That contrasts with a 40 per cent drop in the S&P 500 index. In sterling terms, gold has risen 46 per cent since August 2007.

Taking a longer view, the gold price has risen fourfold since its low in 1999 of about \$250 an ounce when the UK government decided to sell a large chunk of its gold reserves. It crept above \$300 an ounce in 2005, the first time since the early 1980s, and it has been rising pretty steadily since then on general expectations of rising global demand for commodities and rising inflation. In March, gold peaked at more than \$1,030 an ounce.

The bulls maintain that gold and jewellery will come into their own as (portable) safe havens during turbulent times and cite recent evidence from the World Gold Council that consumer demand for gold coins and bars has reached the highest level for more than a decade.

The WGC calculates that consumers spent more than \$6.5bn in buying more than 232 tonnes of gold coins and bars in the

third quarter of 2008, representing an increase of 121 per cent in volumes in a year. It was the strongest quarterly increase since the mid-1990s. At the same time, in India, the world's largest gold jewellery market, demand rose 29 per cent to 178.5 tonnes in a year, with consumers apparently taking advantage of lower prices ahead of October's Diwali festival.

The gold bugs insist these are not short-term factors. The gap between supply of gold and demand will only widen when confidence is revived in the world's banks and the financial system and worries about inflation pick up again.

"Gold will always be subject to price volatility, but it will never lose its physical or 'real' value," says Julius Baer, the private bank.

Gold production has been in decline since it peaked in 2001, it points out. Exploration costs have climbed and gold producers have stopped investing. Very few new gold reserves have been developed since the 1990s and even when new deposits are discovered, new gold mines take decades to get up to speed to plug the gap between supply and demand.

As Graham Birch from BlackRock, says: "You now have to sink a shaft three miles deep at the cost of billions and it takes 10 years for the mine [to start producing ore]." ■



**SILVER SERVICE**

Silver prices react to much the same influences as gold and, though silver tends to attract less emotional attachment it has been used for millennia to back currencies.

Since the time of Themistocles in Athens (circa 500BC) and through much of the western world, India and China, monetary units were often fixed with reference to silver.

Nevertheless, the metal is seen as more of an industrial metal than gold and prices are volatile. Until the rise of digital cameras, photography accounted for about a quarter of silver usage for film. The use of the metal in items such as electrical appliances and medical products has increased since 2001.

Like gold, silver prices have been soaring for the past three years. Although silver has never got back to the levels seen in the 1980s, when prices rose from about \$5 to more than \$35 as speculators tried to corner the market, it reached \$20 earlier this year. Like other commodities it fell back sharply this autumn and currently trades at close to \$10 an ounce. However, there are plenty of silver bulls who argue that it, like gold, is a safe haven and can only rise in value amid economic gloom. ■

**GOLD BULLS COUNTER** that the recent price weakness is merely a correction after a strong run. They blame the price weakness on troubled hedge funds and traders who had been using gold to bet on rising commodity prices and are now cashing in on the stronger dollar.



*All that glitters: valuing gold as an investment is reasonably straightforward - in contrast to precious stones*