Our Weekly Paid Newsletter

Richard Cluver Predicts

In our 37th year of service to the investing public of South Africa

Volume: 37 - Issue: 13

05 April 2024

From a low of $1 998.20 on February 14, the gold price soared to $2 288 this week, a gain of 14.5 percent in the past seven weeks.

When last I drew readers' attention to the phenomenon on March 11, the dollar gold price had just completed a nine percent surge to peak at $2 190.80. Inevitably it fell back marginally to a March 18 low of $2 149.20 as it consolidated this new high. But since the 22nd it has been gathering strength for another sharp increase which effectively confirms that the marketplace no longer believes the world's inflation problems are behind us….or worse that a monetary crisis of significant proportions lies ahead of us which might be the consequence of unrestrained global debt.

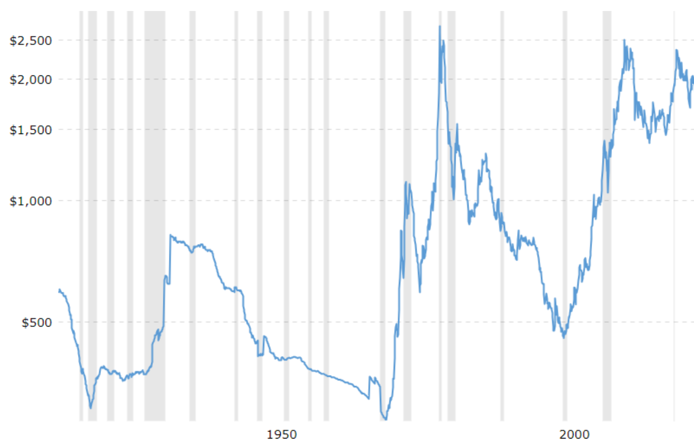
The flight into inflation hedges like gold - and more latterly cryptocurrencies which have the added advantage of being able to cross borders at a touch of an Internet button while remaining opaque to governments desperately seeking new ways to fund their collapsing budgets – possibly implies a beginning of panic that the world's monetary system might soon begin to unravel.

So let's start with the proofs of what is happening. On the left below I have graphed the gold price in US$. In the middle Bitcoin which has risen from a low of $16 408 in January 2023 to a current $71 536 and, more recently on the right the price of Brent crude oil up from a December 23 low of $73.78 to a current $88.43.

There are many others and so it is important to emphasise that these sudden increases do not happen by accident. They represent a world deeply concerned about the value of the money they have traditionally resorted to for all their global transactions, the once almighty greenback Dollar

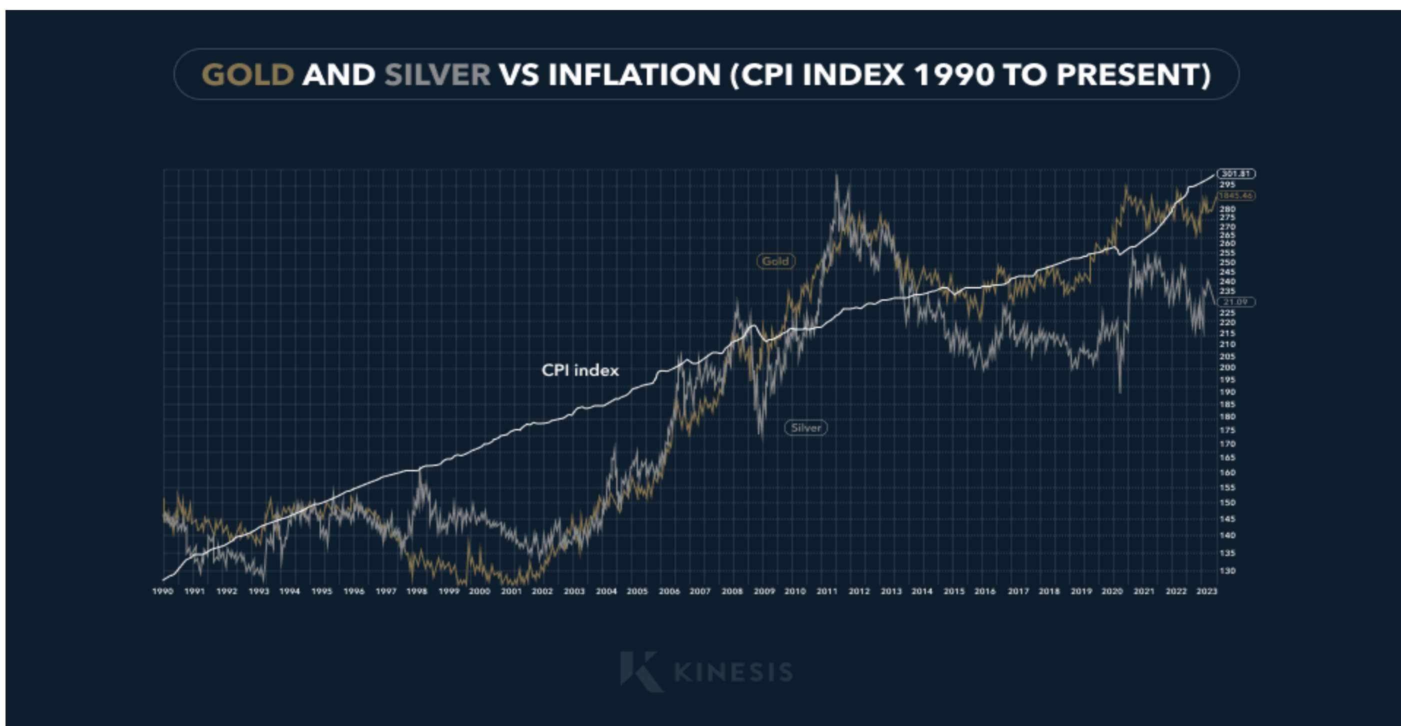
which, by universal agreement at the Bretton Woods meeting in 1946, became the world's reserve currency at a then fixed exchange rate of $35 a fine ounce.

If you care to work it out for yourself, the increase of the gold price from $35 to the current $2 288 over the past 75 years implies that the US inflation rate, which measures the effective erosion of the buying power of the Dollar against this ultimate store of monetary value, has been a compound annual average rate of 5.3 percent. Official US inflation figures, however, suggest that at least for the past 50 years, inflation has averaged only 3.8 percent.



So something does not quite add up. Part of the problem lies in the fact that the gold price has not risen in a clean straight line as the graph on the right of the past 110 years illustrates. Clearly such price volatility implies that the US government, via its agency the US Federal Reserve, has not done a very good job of maintaining the value of the dollar through some quite dramatic inflationary periods.

But, if we turn to the chart below, courtesy of the St. Louis Fed's FRED database which shows the prices of gold and silver vs. the CPI since 1990 suggesting that over the last 32+ years, gold has been reasonably well correlated with the US rate of inflation.



Readers need to be reminded that there was a bull market in precious metals between 1980 and late 2000 during the period of the 'Volcker Shock' when runaway inflation last threatened to overwhelm the world's monetary system. But as investor concerns receded once inflation was brought back under control, the graph shows that, between 1995 and 2001, gold and silver underperformed the CPI index. Then from 2001 to mid-2011, both metals significantly outperformed the CPI. So one might conclude that in the medium-term the gold price more adequately telegraphs the hopes and fears of the marketplace than it does long-term inflationary trends. In the long term however, it should be completely accurate. So something is wrong with US CPI measurement!

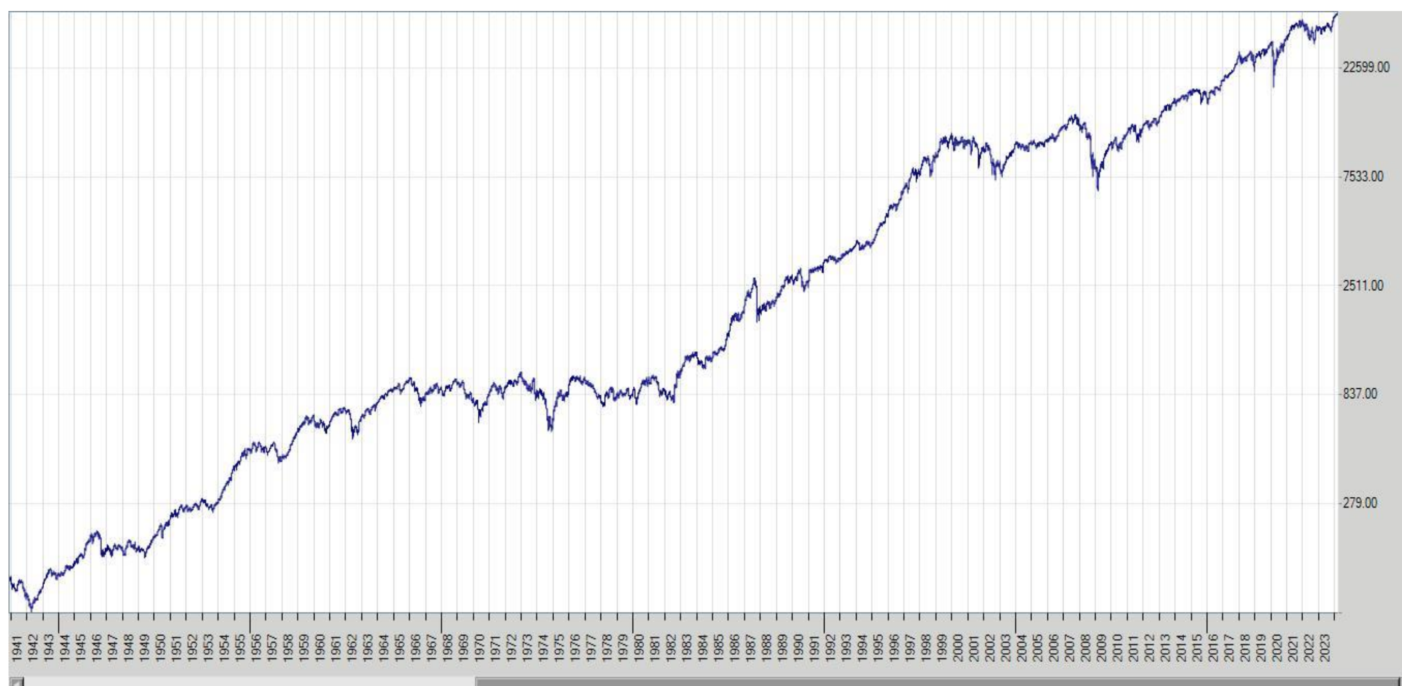
That being so, it is hardly surprising that the market has been growing increasingly concerned about the value of the dollar because, using 2001 as our base calculation, the graph on the right shows that gold has since then been rising in value at compound 9.7 percent annually– and furthermore some 50 percent higher than the 75-year average rate of 5.3 percent – and furthermore it has offered a reasonable overall straight line fit. So it is clear that the correlation between gold and US inflation is not entirely precise.

Obviously as the world's ultimate store of wealth, it rather echoes investor sentiment more accurately than it does US core CPI. But there can be no questioning the fact that over the long term it accurately tells us the extent of Dollar inflation and this explains why many analysts have serious doubts about US CPI methodology. Clearly too, US inflation is a whole lot worse than the US Government would try to convince us!

That being the case, gold might actually be a better indicator of impending trouble than we imagined!

So might Wall Street share prices offer a better correlation with inflation? After all, investors putting up hard-earned savings for shares in corporate America would surely wish to be at least compensated over time for any inflationary losses in the buying power of the Dollar and similarly expect to share in the productivity gains made by the companies they invest in. That must surely be a more reliable measure than the somewhat arbitrary choice of CPI basket ingredients which, for example controversially leaves out big ticket items like house prices and home rentals: perhaps because their inclusion might produce numbers that are rather worse than their politician employers would want to see.

Logic says that the Wall Street average must surely represent the sum of inflation and US aggregate productivity? Below I have thus offered a graph of the world's oldest share market index, the Dow Jones Industrial Average dating back to 1944. Reading off the numbers shows that the Dow bottomed at 131.30 in July 1944 and currently stands at 39 868 which suggests that the Dow has grown by a compound annual average of 8.38 percent since that Bretton Woods meeting.



But if the gold price obviously represents the ultimate store of monetary value and, periods of monetary uncertainty aside, what might account for the difference between the official inflation rate of 3.8 and the long-term gold price gain at a compound annual average rate of 5.3 percent?

Logically it might be represented by the average gain in US GDP. So, if you assume that over long periods the gain in value of Wall Street shares might logically represent the sum of GDP gains and the inflationary loss of value of the US$. Then inflation's long term 3.8 percent plus gold's 5.3 gives us 9.1 which gives us a 0.72 percent absolute error factor. That is just too big a number!

So let's take another tack. According to World Bank records, the official average GDP growth rate of the US between 1961 and the present has been 1.9 percent and, if you take that number away from the average Wall Street share price gain of 8.38 you get 6.48 percent which is closer to the long-term gold price average of 6.07 to imply a slightly better correlation.

For some that could be enough evidence to believe that official US numbers somewhat understate the real inflation problem.

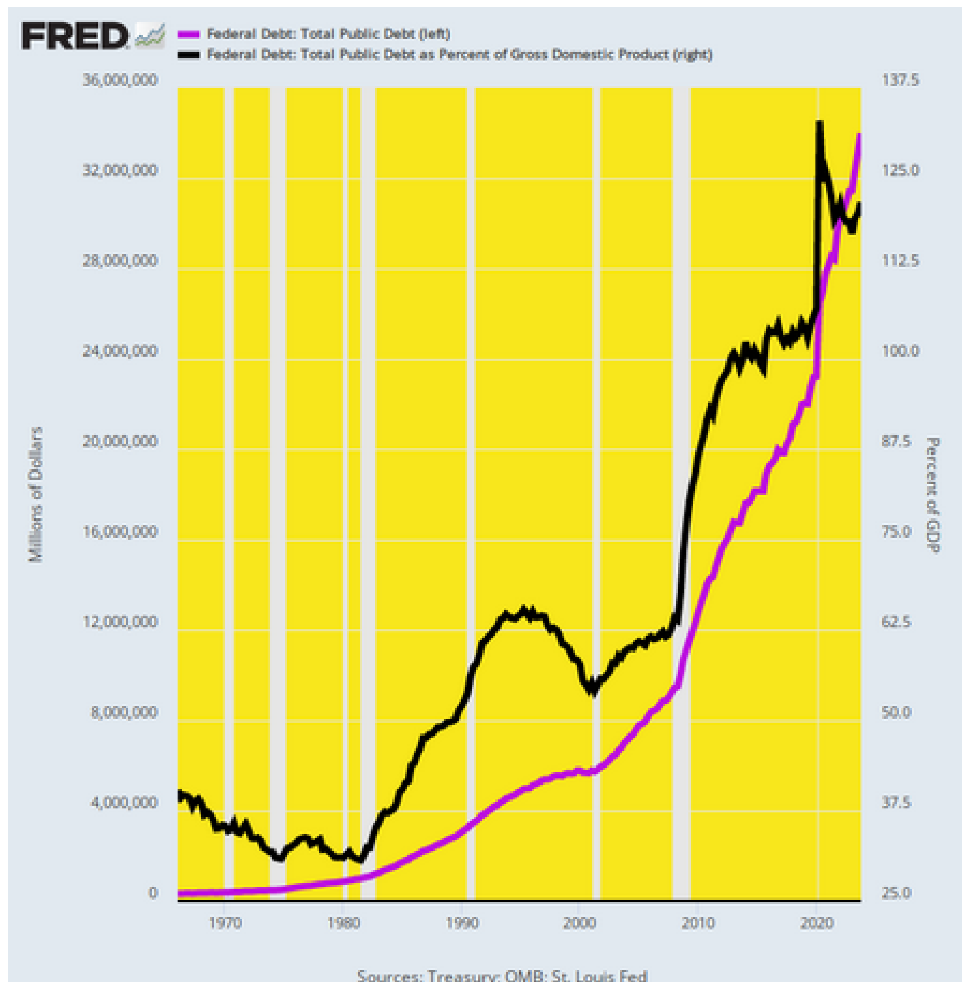
Furthermore, since the recent gold price average gain has been an annual 9.7 one could perhaps conclude that something more has been at play for the past quarter century: indeed, the fact that for the past quarter of a century during which the gold price increase has been rising at compound 9.7 percent compared with its long-term average of 5.3 – an 83 percent rate increase – makes it clear something dramatic is happening.

Which takes me to the fact that US debt graph has now become parabolic! US columnist David Stockman has just posted the fact that: "The Federal debt has been recently increasing by $1 trillion every 100 days. That's $10 billion per day, $416 million per hour.

"In fact, Uncle Sam's debt has risen by $470 billion in the first two months of this year to $34.5 trillion and is on pace to surpass $35 trillion in a little over a month, $37 trillion well before year's end, and $40 trillion some time in 2025. That's about two years ahead of the current CBO (Congressional Budget Office) forecast.

"On the current path, moreover, the public debt will reach $60 trillion by the end of the 10-year budget window. But even that depends upon the CBO's latest iteration of Rosy Scenario, which envisions no recession ever again, just 2% inflation as far as the eye can see and real interest rates of barely 1%. And that's to say nothing of the trillions in phony spending cuts and out-year tax increases that are built into the CBO baseline but which Congress will never actually allow to materialize.

"So when it comes to the projection that the 2034 debt will come in at just $60 trillion, we'll take the wonders any day of the week. The fact that it will likely be much higher also means that the Washington UniParty's prevailing fiscal policy path will lead to $100 trillion of public debt sometime in the early 2040s. And that means, in turn, that annual interest expense will then be greater than the entire federal budget during 2019."



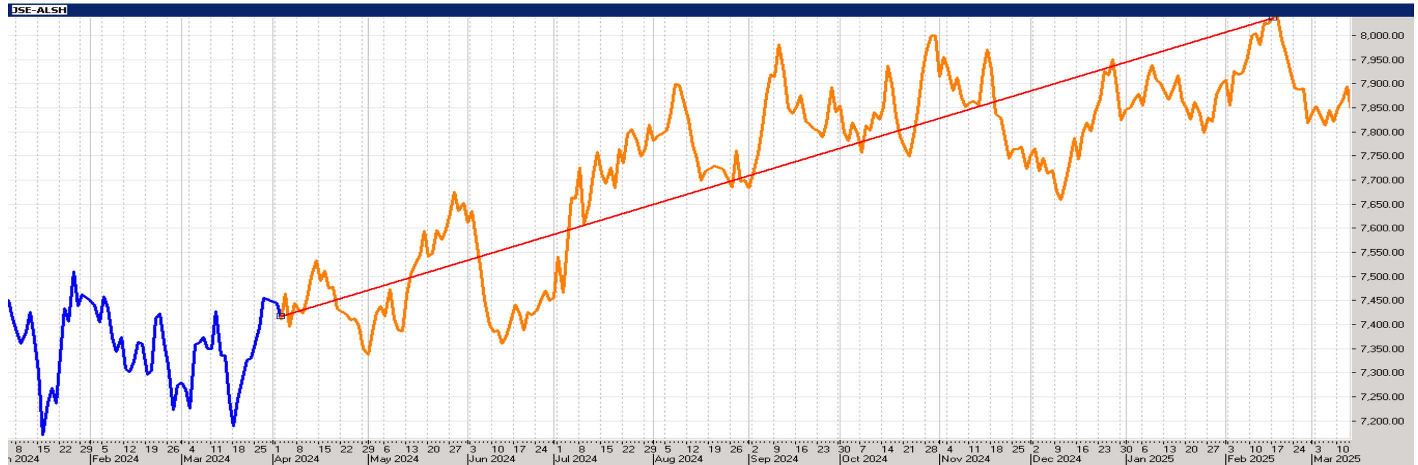
The crisis is clearly upon us…and note the US is not the most indebted country. Japan's debt is 214.27 percent of its GDP and China is estimated to be more than double that.

Is the world's monetary system or, more precisely its governance systems, now verging on collapse? Well you need to be the judge of that. But the sudden gains being made by global inflationary hedges ARE signaling something close to panic!

Meanwhile The Daily Maverick reported yesterday week that: "Fed chair Powell reiterated that the central bank will take a wait-and-see approach before reducing borrowing costs. However, his views that recent inflation figures did not "materially change" the overall picture offered support for risk assets.

"In recent days, traders had scaled back their rate-cut expectations amid signs of economic resilience and a more cautious tone from a drumbeat of Fed officials. That has led to scepticism on whether Powell and his colleagues would be able to deliver on the central bank's projection of three rate reductions this year."

Meanwhile, ShareFinder's projection – see graph below - of the JSE All Share Index continues to see rising share market optimism rising from May 2 right up to Election Day and then sharply reversing until June 14 followed by at least eight months of strong gains. I interpret that as two weeks of post-election uncertainty followed by a coalition consequence that fills South Africans with a new spirit of confidence since the projected market gains are likely to outstrip ShareFinder's projections for most global markets – twice those projected for Wall Street!



The month ahead:

New York's SP500: I correctly predicted the beginning of weakness which is likely to continue until now ahead of a brief recovery to April 11 and then another decline to the end of April ahead of a volatile recovery to a new market high in mid-August.

Nasdaq: I also correctly predicted the down-turn which I still expect to last to approximately May 10 followed by gains to the end of July ahead of a long decline to the end of the year.

London's Footsie: I correctly predicted a brief reversal ahead of a short gain starting today until May 27 and then another drop to June ahead of two months of gains. Thereafter I see a long drop to December.

France's Cac 40: I correctly warned about the start of a long decline beginning this week and likely to last to early July when two months of gains should begin ahead of another extended decline to Christmas.

Hong Kong's Hangsen: I correctly predicted the start of weakness until early April which is but a brief moment in an extended recovery into the New Year.

Japan's Nikkei: I correctly predicted the start of a lengthy sideways trend with the next up-trend only starting in late August to the end of the year.

Australia's All Ordinaries: I correctly warned of weakness ahead of a volatile recovery likely to begin in mid-May. But from until late July I again sense weakness right through to next February.

JSE Top 40 Index: I correctly predicted weakness but this week's gains came sooner than expected. But I continue to see a volatile recovery until the end of October.

ShareFinder JSE Blue Chip Index: I correctly predicted the imminent end of current weakness and, though there is likely to be another short dip from April 18 to the end of May, I see volatile gains until late September with further interim weakness between July 10th and August 23.

Rand/Dollar: I correctly predicted weakness though it ended sooner than I expected. Long term I see gains well into the New Year with the next brief weakness between April 24 and June 11.

Rand/Euro: The current gains are likely to be over by the 10th with protracted weakness thereafter**.**

The Predicts accuracy rate on a running average basis since January 2001 has been 87.19 percent. For the past 12 months it has been 92.57 percent.

Published by ShareFinder International
http://www.sharefinderpro.com
richard@rcis.co.za