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Gold May Rise for Sixth Year as Hedge Funds Diversify (Update3)

Jan. 4 (Bloomberg) -- Gold prices may extend gains for a sixth year in 2006 as hedge funds buy the precious metal to diversify from stocks, bonds and currencies.

The price of bullion may rise 18 percent to average \$525 an ounce, up from \$445 last year, according to the median forecast of 29 analysts, traders and investors surveyed by Bloomberg News.

Hedge funds and other large speculators more than tripled their net long positions, or bets prices will rise, in New York gold futures in the past five months. Investors are buying the metal because of concern over inflation, the U.S. budget and current account deficits and the dollar.

"It's all about fund diversification, that's the bottom-line," said Peter Hillyard, head of commodities sales in London at ANZ Banking Group. Investors have been heavily dependent on equities, bonds and currencies."

Gold for immediate delivery reached a 24-year high of \$541 an ounce on Dec. 12 in London. The metal traded at \$532.78 an ounce at 10:48 a.m. London time today.

Investors are buying gold because it's outperforming stocks and bonds. Gold rose 90 percent in the five years to the end of 2005, while the Standard & Poor's 500 Index returned 2.7 percent with dividends reinvested. An index of Treasuries maturing in two years or more returned about 30 percent including interest reinvested, Merrill Lynch & Co. indexes show.

A sixth year of gains would be the longest winning streak since central banks allowed the price of gold to find its own level in the free market in 1968.

Hedge Funds

Hedge fund managers and other large speculators held net-long positions totaling 154,522 contracts in gold futures on the Comex division of the New York Mercantile Exchange as of Dec. 27, figures from the U.S. Commodity Futures Trading Commission show. That compares with 49,022 contracts held as of July 26.

Bullion is a top trading pick for 2006, Goldman Sachs Group Inc., the third-biggest securities company, said in a Dec. 19 report, citing concern over inflation, currency values and the U.S. trade deficit.

Prices of the precious metal may climb to \$600 this year, Marty McNeill, a trader at R.F. Lafferty & Co. in New York, said.

"It's a long-term thing," said McNeill, 63, who witnessed gold's last bull market as a trader, when the metal peaked at \$873 in 1980. "Oil's going to stay high so you've got inflationary pressure. That's going to work in gold's favor."

Gold may rise as high as \$850 an ounce within 18 months as a weakening dollar boosts the metal's appeal as an alternative investment to U.S. assets, Paul Walker, chief executive of London-based research group GFMS Ltd., said in an interview.

Weaker Dollar

The dollar will weaken as `` more attention is paid to its poor and deteriorating fundamentals, such as the twin budget and current account deficits," Walker said Dec. 8.

The U.S. posted a record budget deficit of \$412.5 billion in fiscal 2004. The shortfall narrowed to \$318.6 billion in fiscal 2005. The deficit in the current account, the broadest measure of trade because it includes income from investments and transfer payments, widened to a record \$668 billion in 2004 from \$520 billion the previous year, according to Bloomberg data.

Buying by central banks could push gold up to as much as \$560 this year, said Graham Birch, who helps manage \$8.5 billion in mining assets for Merrill Lynch Investment Managers Ltd., the world's biggest investor in gold stocks.

`` Countries with big trade surpluses, such as China and some in the Middle East, have too many dollars. They may think about gold as a reserve diversifier," he said.

Russia's central bank said in November it may double its gold reserves. Central banks in South Africa and Argentina have also said they may increase their gold holdings.

Central banks, mainly in the U.S. and Europe, hold almost 20 percent of the world's gold supply as a reserve asset.

Production

Gold production in 2004 had its biggest decline since the 1940s. It was little changed in the first half of last year at 1,172 metric tons, according to GFMS. South Africa, the world's top producer, produced 15 percent less in the third quarter, the biggest drop in at least nine years.

Demand for the metal in the first half of last year rose 10 percent to 2,034 tons, buoyed by jewelry consumption, according to GFMS. Demand in India, the world's biggest consumer of gold jewelry, rose 47 percent. Gold jewelry sales gained 14 percent in China and the Middle East, GFMS said.

`` The coming year, according to Chinese tradition, will be a good year for weddings," Paul Law, financial controller of Luk Fook Holdings International Ltd., a Hong Kong-based jeweler, said in an interview on Dec. 21. `` People will try to buy more gold jewelry."

Company	Gold	Silver	Palladium	Platinum
ABN Amro	\$510	\$8.60	\$275	\$900
Adrian Day's Asset Management	\$530			
A.G. Edwards & Sons	\$475			
Angel Commodities Broking	\$540	\$10		
ANZ	\$520			
Barclays	\$465	\$7.10	\$220	\$910
CPM Group	\$471	\$8.18	\$247	\$896
Dan Chesler	\$550			
GFMS Analytics	\$520			
Goldman Sachs	\$515			
James Turk	\$580			
John Licata	\$560			
JPMorgan	\$558		\$220	
Logic Advisors	\$540			
Kotak Securities	\$555	\$9.50		
Macquarie	\$516	\$8	\$265	\$925
Merrill Lynch	\$525		\$250	\$975
Midas Management Corp.	\$666			
Mitsubishi Intl. Corp.	\$520			
MKS Finance	\$500	\$8	\$250	\$850
NAB	\$532			
Numis	\$475		\$204	\$800
Narrondass Manordass	\$525			
Paul Yusem	\$574			
Prospector Asset Management	\$485			

RBC	\$540	\$9		
SocGen	\$515	\$8	\$233	\$925
Tiberius	\$550	\$9.10	\$240	\$850
UBS	\$520	\$6.40	\$185	\$911

2006 Forecast: (Median)	\$525	\$8.18	\$240	\$905
2005 Average:	\$445.39	\$7.32	\$202.26	\$897.63
% Gain (Loss)	18%	12%	19%	1%

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