

MACROCOSM

## Pushing On a Golden String

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**Donald Luskin**

**Buy the dip in gold. Global reflation remains the dominant strategic factor.**

It feels like gold is ripe for a short-term correction after a stellar run. But we say buy the dip, and we reaffirm our \$1500 price target (see ["Why Isn't Gold at \\$1500?"](#) December 10, 2008, and ["More Upside for Gold"](#) June 10, 2010). The strategic forces that have driven gold to new all-time highs

**Update to  
strategic view**

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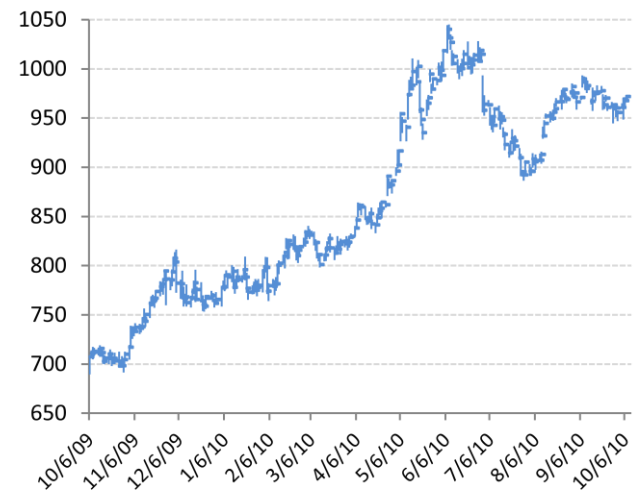
### Gold (US dollar)

Source: Reuters



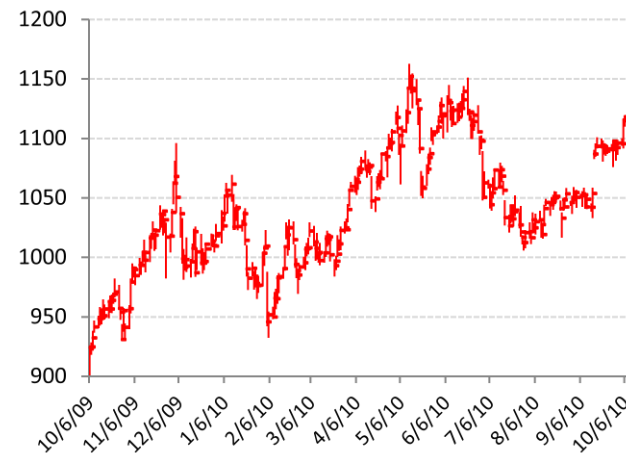
### Gold (euro)

Source: Reuters, TrendMacro calculations



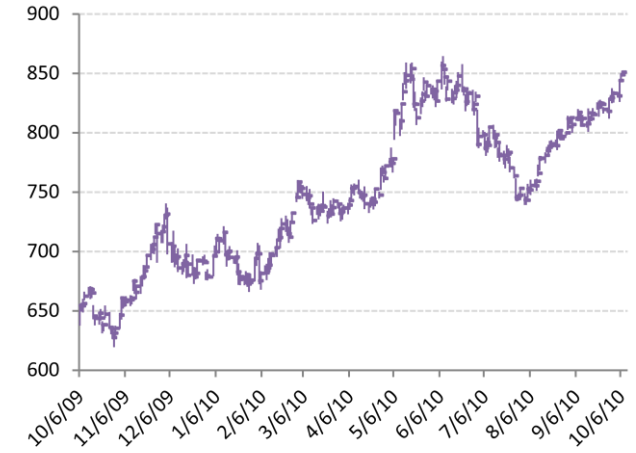
### Gold (yen)

Source: Reuters, TrendMacro calculations



### Gold (sterling)

Source: Reuters, TrendMacro calculations



remain in place, and we see no indication that they are going to change anytime soon.

- In the developed world's "expansionless recovery" there is "no exit" from recurring crises -- and "no exit" from the perceived duty of central banks to intervene by supplying additional liquidity.
- Even absent outright crises, the developed world's stagnant growth mandates ever-easier monetary policy in the face of high unemployment and low statistical inflation.
- Low statistical inflation not only gives central banks confidence to dare to run reflationary policies, but indeed goads them to do so in the belief that inflation is currently insufficient -- as the Fed [declared](#) at the September FOMC meeting (see "[On the September FOMC](#)" September 21, 2010).
- At the same time, the developed world is running low on official borrowing capacity, so monetary reflation is seen as the only hope for promoting growth -- and both fiscal and monetary authorities have their role to play in bringing it about.
- For treasury authorities, this means what Brazil's finance minister [calls](#) an "international currency war" of competitive devaluations, a "race to the bottom" chasing the goal of increased export volumes (see "[Gold is the Strongest Currency](#)" May 6, 2010).
- For monetary authorities at or near the zero-bound on overnight policy rates, this means continued quantitative easing and the use of overt inflation targets, both of which were [announced](#) by the Bank of Japan this week.

Whether or not any of this is effective in achieving relief from crises, greater export volumes, lower unemployment, high statistical inflation, or whatever else the world's central banks want or expect -- it will definitely keep propelling the price of gold and other monetary commodities higher.

- In an "expansionless recovery" in the wake of a world-historical credit crisis, newly created fiat money remains trapped in the clogged plumbing of the impaired banking system. So the central banks of the world are pushing on a string. But the excess quantity of money mandates the revaluation of money-substitutes such as gold, which becomes increasingly valuable measured in the unit of account of whatever currencies are being created in excess.
- At the same time, the "international currency war" is being waged to make developed world currencies (such as the US dollar) cheaper relative to emerging world currencies (such as the Chinese yuan). The consequence is that the emerging world will have more buying power to import strategic commodities such as gold, oil and copper, driving their dollar prices higher.

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## Bottom line

After a stellar run to new all-time highs, gold could be in for a short-term correction. But buy the dip, because the global reflationary forces that have propelled gold higher are all still very much in place. ▶

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## Update to strategic view

**GOLD:** After a stellar run to new all-time highs, gold could be in for a short-term correction. But buy the dip, because the global reflationary forces that have propelled gold higher are all still very much in place.

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