Gold price drivers – all roads lead to West Africa

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The price of gold is influenced by a combination of supply, demand and investor sentiment. That seems simple enough, yet the ways in which these factors work together is sometimes counter-intuitive.

Correlation with inflation

Two economists, Claude B. Erb, of the National Bureau of Economic Research, and Campbell Harvey, a professor at Duke University’s Fuqua School of Business, have studied the price of gold in relation to inflation.
AUTHOR: Dean Cunningham, Director at Micofin

They conclude that when inflation rises, gold is not necessarily significantly impacted. So, if inflation is not the driver, fear of inflation must be, combined with the associated impacts on currencies and economic activity.

Supply

Unlike oil or coffee, the gold consumed today is largely above ground. Though there are some industrial uses for gold, this hasn’t increased demand as much as jewelry or investment.

Central banks

In times when foreign exchange reserves are large and the economy is growing, a central bank will look to reduce its holdings; unlike bonds or even money markets, gold generates limited return.

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One exception is China which has been a net buyer for some time, likely due to the extent that it is regarded as a source of diversification from the dollar.

Portfolio considerations

Gold has been seen as an insurance policy over short time horizons. This often does well but its inclusion should be viewed alongside risk, return and correlation features of the wider portfolio to achieve optimal diversification.

Retaining value

Many authors, including Erb and Harvey have concluded that purchasing power of has stayed fairly constant and largely unrelated to market prices.

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We see it as tangible, movable and acceptable around the world as a currency. Many investors are looking
If you're looking at gold prices, it's probably a good idea to look at how well the economies of certain countries (particularly China, the UK and US) are doing. As economic conditions worsen, the price will (usually) rise.

- Technically - The gold price has been showing bullish signals and has recently broken out, with some commentators looking as high as US$2 000/oz and even $5 000/oz.
- Trade Wars - Key players with divergent views, opinions and ideologies have been disrupting years of global trade. What looks like a move away from integrated global trade and towards increasingly segmented markets could be a key contributor to a rising gold price.

The US-China trade war has been blamed for a lack of growth.

Manufacturing has been hit hard, with orders dropping and prices rising on the back of increasing tariffs imposed by the two countries. Talks have stalled repeatedly and the IMF believes this has already cost the global economy billions. A move by investors to safe-haven assets is possible.

**Gold forecast for 2020**

After an impressive nine months, gold has already increased from $1 270/oz in July to $1 574/oz in January 2020. At this stage, short-term volatility in the gold price seems to be driven by geopolitical and economic circumstances, but this can change significantly and rapidly.

We expect long-term, strong demand, with the World Gold Council reporting that demand in mid-2019 was up 8% year-on-year we expect 2020 to be an interesting year for the metal.

Many of the drivers behind gold’s recent rally are still ongoing. Most have no resolution in sight and the unpredictable way in which they end will likely have a significant impact on the gold price outlook.

In the words of:
• Commerzbank: We see the ongoing steep rise in the gold price as an expression of the high-risk aversion among market participants. Gold is quite clearly still in demand as a safe haven in the current market environment.”

• Neils Christensen for Kitco News: “We are entering another leg of the bull market where there is greater investor acceptance of stocks as attractive assets but at the same time, they acknowledge the higher risks,” …I think it is natural that at this point in the bull market, investors become interested in gold.”

• Holmes and US Global Investors see gold at $5 000/oz and $10 000/oz, respectively. Based unprecedented money printing will continue, with ultra-loose monetary policy undertaken by central banks to flood the economy with money.

In the short- to medium-term, gold remains a key component for diversification within any portfolio; buy on any pull-back and continue to monitor market risk and sentiment.

**Where to go**

The focus is West Africa, now producing over 330 tpa, with some 220 exploration or near-term producers and operators, investors have an ideal environment in which to invest into.

**Read more about mining in West Africa**

There has been a significant increase in investment in existing and new gold mines of late. So, says Barry Beylefeld from Azmet Technology and Projects, a multi-disciplined engineering design and project management company with a strong eye in Africa.

“We have seen a significant rise in demand for technical skills and services to improve existing operations by considering new technologies and optimising certain unit operations and recommissioning mothballed companies based on the current higher gold prices in the region,” he says.

Key players include AngloGold Ashanti, Barrick Gold and Newmont Goldcorp all have mines in the region, and Newmont recently completed an expansion project in Ghana.

Most of West Africa’s deposits have yet to be found and mined, according to Oumar Toguyeni, IAMgold’s vice-president for the region.
About the author:

Over the past years Dean Cunningham has been the orchestrator of a number local and international transaction in the mining, downstream and energy and utilities sectors - coupled with Micofin and its strategic partners’ (Wood, Practara, NEXUS Intertrade and Africa House) objectives to take skills, technology and capital to Africa, with a firm understanding of doing the work and creating jobs here at home.

Project destinations include the Middle East (Phase 1 completed) and the production of dololime and magnesium metal, supplying construction materials in Mozambique, the formation of a logistics company to move both own and third-party products and the treatment of waste material into high value saleable materials for the battery sector.

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