Gold 22% Rally to Record Seen by Eric Sprott: Commodities

Bloomberg News

By Liezel Hill - Jul 12, 2012 9:44 AM ET

Gold will climb to a record by yearend as the global economy slows from the weight of too much debt, says Eric Sprott, the founder and chairman of Canadian fund manager Sprott Inc. (SII)

"I just can't imagine the demand for gold is going down," he said in a July 9 interview at Bloomberg's Toronto office. "I don't personally see a solution to the problem that we're in, the financial leveraging issue that we all have where everybody wants to shed debt and there's no buyers."

Gold, which had advanced for 11 successive years, is almost unchanged so far in 2012.

Gold, which had advanced for 11 successive years, is almost unchanged so far in 2012. Photographer: Guenter Schiffmann/Bloomberg

July 3 (Bloomberg) -- Ben Davies, co-founder of Hinde Capital Ltd. and manager of the Hinde Gold Fund, talks about the outlook for gold prices. He speaks with Adam Johnson on Bloomberg Television's "Street Smart." (Source: Bloomberg)

Sprott's company manages funds investing mainly in gold, silver, and precious-metals equities. He expects bullion will rise as investors seek the safest assets while governments spend to stimulate their economies, increasing chances that inflation will accelerate.

Gold, which had advanced for 11 successive years, is little changed so far in 2012. It's 19 percent lower than the record $1,923.70 an ounce traded on Sept. 6 in New York after investors favored buying the dollar amid Europe's escalating debt crisis.

The metal "should go to new highs before yearend, that would be my guess," said Sprott, 67. "Gold has blown away every financial market in the world since 2000, let's not forget that."

Rallying to a record would mean gold climbing at least 24 percent on the Comex in New York, where bullion for August delivery fell 1.2 percent to $1,557.30 an ounce at 9:41 a.m. Futures gained 2.4 percent in 2012 through June, the smallest first-half increase since 2007.

'Fundamental Problem'

Sprott declined to make a specific price prediction. Future highs are "indefinable" because they will depend on decisions by policy makers, he said.

Sprott has previously made predictions that were accurate, or largely so. He said in May 2011 that gold might rise to $2,000 that year. In March 2008 he said banking stocks would collapse. Bear Stearns Cos. was sold to JPMorgan Chase & Co. later that month and Lehman Brothers Holdings Inc. filed for bankruptcy in September.

Governments including the U.S. don't have the resources to meet their obligations, Sprott said.

"We have a fundamental problem in the sovereign and banking system in the world," Sprott said. "Probably nobody has any conception of how bad it is."

Minsky Moment

Central banks can either print money, which would help lenders, or “deal with the Minsky moment,” he said. The term was named after the late U.S. economist Hyman Minsky, whose Financial Instability Hypothesis argues that capitalist economies first trigger waves of credit expansion and asset inflation and then credit contraction and asset deflation.

“Minsky said that if you expand your economy by increasing debt, there comes a point where the productive engine can’t deal with the debt,” Sprott said. “I’ve thought that there will be many, many Minsky moments for many banks and countries.”

Sprott is a qualified accountant who started his investment career as an analyst at Merrill Lynch & Co. He founded his current company before selling Sprott Securities, now Cormark Securities Inc., to its employees in 2002. He owns 55 percent of Sprott Inc. according to data compiled by Bloomberg.

His company, which also offers wealth-management and consulting services, had C$9.7 billion ($9.5 billion) under management as of March 31, mostly through its Sprott Asset Management unit.

Gold Equities

Sprott Inc. fell 2.1 percent to C$4.75 at 9:49 a.m. in Toronto, valuing it at C$805.8 million. The company has declined 53 percent since its May 2008 initial public offering.

Sprott has lauded gold and gold stocks since at least 2001. The company began offering its own products for investors who want to own bullion in March 2009. Sprott Inc.’s Sprott Hedge Fund has returned about 391 percent since its inception in 2000, according to data compiled by Bloomberg.

Gold equities, which have lagged behind gains in the metal, will probably “do well” when gold prices rise, Sprott said. The stocks “can’t get a sustained recovery until gold has a sustained recovery,” he said.

The NYSE Arca Gold BUGS (HUI) Index, which comprises 16 gold mining companies, has fallen 27 percent in the past 12 months, compared with a 0.3 percent decline in gold in New York. Toronto-based Barrick Gold Corp. (ABX) and Vancouver-based Goldcorp Inc. (G), the world’s two most valuable miners of the metal, have dropped 23 percent and 35 percent respectively in the period.

Gold Standard

To be sure, gold-mine production is increasing, which will be negative for prices, said ***Pawel Rajszel***, a Toronto-based investment analyst at ***Veritas Investment Research***.

“Supply is growing faster than demand can keep up with, and as a result you are going to see prices slowly but gradually fall,” ***Rajszel*** said. “Obviously there’s a bunch of short-term fluctuations that can happen, but I think over the long term you will see gold prices fall.”

The metal averaged $1,613 in the second quarter. It will average $1,721 in the third quarter and $1,802 in the fourth, according to the average of 23 analysts’ estimates compiled by Bloomberg.

The debt crisis “should be incredible for gold,” said Sprott. He said the world may eventually return to the gold standard.

“Ultimately, if there’s a currency crisis, which one could argue we are in the throes of it right now, how do sovereigns and banks back things up? What do you back it up with?” he said. “I can imagine that the most logical thing is gold.”