

Cover story

# In uncertain times, gold beckons again



***"In uncertain times, gold beckons again"***  
**By John Waggoner, USA TODAY, August 15, 2002**

Violence in the Middle East. A drop in the value of the U.S. dollar on world currency markets. The worst bear market since the Great Depression. In short, it's a glorious time for the gold market — the best since 1999, when a computer glitch threatened to leave the world living on bartered corn and rainwater.

The worst brings out the best in the precious metal:

Gold has spiked to \$314 an ounce, from a three-year low of \$256 in April 2000.

Mutual funds that invest in gold-mining stocks have soared 37% the past 12 months, vs. a 23% loss for the Standard & Poor's 500-stock index. Investors have poured \$650 million into gold funds this year — so much that some funds, such as Vanguard Precious Metals, have closed their doors to new investors. The gains have sparked a new gold rush. The U.S. mint sold 48,000 gold Eagles in July, 60,500 ounces in all, up 20.6% from a year earlier.

"July sales were up 50%," says Michael Byrd, president of Austin Rare Coins, which sells gold bullion as well as collectible coins. "We're having a Y2K kind of year." Fervent gold investors believe the government is desperately trying to squash gold prices and prop up the stock market. "The last thing they need is a gold rush," says Doug Casey, editor of International Speculator, a gold-oriented newsletter. He thinks gold will win out. "Gold is like a coiled spring," he says. He predicts it will top \$1,000 an ounce.

Gold is a direct bet against the monetary system: Gold investors figure an ounce of gold is always worth something, even if the government is in shambles and currency is worthless. For two decades, the powerful U.S. economy kept the dollar strong and gold prices low. But lack of confidence in the financial system and the specter of more terror attacks are pushing gold prices up — and individuals back into the gold market.

Gold dealers report that business hasn't been better since, well, December 1999, when Y2K fears were at their height and gold popped to \$318 an ounce. "Through June of this year, we've sold as much gold as we did in 2001," says Carl Wright, president of International Precious Metals in Brookeland, Texas.

"We've had retail customers buying 200, 300 ounces every other week," says Michael Kramer, head gold trader at Manfra Tordella & Brookes in New York City. "Every few days, we do a couple of large trades — couple thousand ounces. I don't remember the last time it was this busy."

But most gold transactions are private, so there's no way to tell exactly how much gold has changed hands this year. Privacy is a big reason people buy gold. Cash purchases greater than \$10,000 have to be reported to the government, but you can buy an unlimited amount by check. Once purchased, gold can't be tracked by anyone, including the Internal Revenue Service. "Many of my clients' wives don't even know about their purchases," says Kevin Boulais, president of Atlantic Rare Coins in Mason, N.H.

Why are investors racing for gold?

Shaken trust. Clark Peterson, 54, was a public relations officer for a military recruiting office in the Murrah Federal Office Building in Oklahoma City in April 1995, when a bomb ripped into it, killing 168.

"I'm a survivor," he says. He has been buying gold for a couple of years. And the collapse of Enron deepened his suspicion of corporate accounting. "When I see big boys like that go kerplunk, all I can say is that a lot of others have been dishonest with the books," he says. Gold coins have solid value, he says. "With a stock, I'm not in control of how a firm handles itself," Peterson says.

Shaken dollar. For many years, foreign investors rushed to dollar-denominated investments, such as U.S. Treasury bills, when war or bad economic news made the world seem dangerous. But this year, a falling U.S. economy and an open-ended war on terror has forced the dollar lower on world markets, prompting many investors, including foreign buyers, to purchase gold instead.

Shaken savers. Many gold buyers are simply looking for an alternative to the stock market, or the 2% to 5% they could earn in money market mutual funds, bank CDs and bonds. "We've seen a lot of new buyers come in, including my stockbroker and my sister," says Marc Watts of Gaithersburg (Md.) Coin Exchange.

But many newcomers to gold investing run the risk of doing the same thing they did in the stock market: buying just because the price is rising. "It's a funny thing — they don't want to buy gold when it's at \$250 an ounce," says Leon Hendrickson, a gold dealer in Winchester, Ind.

Some think the rise in gold prices comes from a fall in confidence in the entire monetary system, not just the stock market and corporate accounting.

The government recalled and melted its gold coins in 1933. The dollar has been backed only by the government's good word since 1973, when the country came off the gold standard. The value of the dollar today is a reflection of the world's belief in the U.S. economy. When confidence in the dollar is low, people start buying gold. To gold fans, the fall of the dollar and the rise of gold is a long-awaited — and frequently predicted — vindication of the gold standard.

Economists and politicians have debated the wisdom of taking the U.S. off the gold standard for decades.

"It was a mistake," says Jack Kemp, a former New York congressman and secretary of Housing and Urban Development. A floating-rate currency system has led to disasters in Latin America and other developing nations, he says. "We need to get a distinguished group together to rebuild the monetary system."

Rep. Ron Paul, R-Texas, says the legacy of leaving the gold standard has been a 30-year bout of inflation manifested in different ways, such as increased debt. "The Federal Reserve is inflating like crazy," he says. His solution — which he has no illusions about becoming law — is to legalize gold as an alternative currency.

Few mainstream economists agree with the idea of returning to the gold standard. "It's a stupid idea," says David Wyss, economist for Standard & Poor's. A currency tied to gold means the government can't stimulate the economy in a recession. And just as floating-rate currencies tend toward inflation, gold-based currencies tend toward deflation.

But some deeply distrust the government's ability to manage the economy. To them, gold's ability to protect against inflation has become an item of faith. In theory, gold prices will rise along with inflation. But the price of gold has fallen from \$875 in 1980, while inflation has risen an average 3.8% a year.

"Gold languished for so long that it looked like soggy cereal," says Mark Bass, a financial planner in Lubbock, Texas.

Why has gold fallen? Some say the Federal Reserve and other central banks have deliberately pushed down the price to maintain faith in paper currency.

"Government intervention in the gold market was at the heart of the Clinton administration's strong-dollar policy," says J. Taylor, editor of J. Taylor's Gold and Technology Stocks newsletter.

Adds Paul: "There has been a concerted effort by the government to discredit gold."

To newsletter editor Casey, it's inevitable that gold will triumph in the end. "The dollar is an unsecured liability of the U.S. government, and the government is bankrupt," he says. "It's an IOU of nothing." To Casey, gold is the answer because it's always worth something — and it can't default. His prediction:

Gold isn't going through the roof — it's going to the moon.

Gold fans argue that the yellow metal is good in any situation, even if the economy sinks into a period of falling prices, as it did during the Great Depression.

"Gold is best looked at as a crisis hedge," Casey says. "If your bank won't let you get your money out, it's best to have something of value in your hand."

But gold fans have argued for a monetary collapse ever since the country went off the gold standard. It hasn't happened yet. There's an element of apocalypse in hard-core gold literature. Buy gold, it implies, and the world can fall apart — but you'll still have your money.

Those looking to gold as a cure for all the world's financial ills should remember that gold can be every bit as risky as stocks. Plenty of people who bought gold at \$800 an ounce are still down by 60% — and even more when you consider what they could have earned in a bank CD in the meantime. Central banks are still selling gold and can push the price down sharply. And when gold prices get high enough, mining companies can reopen mines that were unprofitable when gold was at \$260 an ounce, but quite profitable at \$350.

Even ardent gold supporters recommend it be used in moderation as a kind of insurance against utter catastrophe. For example, Taylor predicts the Dow Jones industrial average will plunge to 5,000, and that real estate prices will collapse, too. It would be a disaster on nearly every level — except for gold. Taylor is selling his house and investing 10% to 20% in gold bullion coins. A financial catastrophe would push up the price of gold enough to offset losses elsewhere.

Nearly all advisers say that gold is best used as disaster insurance, not as your sole portfolio holding. Owning gold does involve special problems — like what to do with it once you own it, particularly if you value your privacy. In a small town, you can't walk into the bank with a bag of gold coins "without everyone knowing what you have," rare coin dealer Byrd says.

And what if you think your bank will be out of business when you need it most? "Some people bury it," says coin shop owner Watts. "It's kind of weird, to work hard to accumulate wealth and then hide it."

If you hide gold, you have to worry about someone finding it or stealing it. Even if you put it in a safe-deposit box, the cost of storage and insurance will eat away at your gains.

Most coin dealers say that if you buy rare coins, buy them for their intrinsic beauty and collectible value first. Gold investor Peterson acknowledges that his gold bet is more than a little speculation. "If you look at the history of coins, they do shoot up at times," he says. "When they get to the point where they just go wild, you have to get out."

Investors have felt gold's allure for centuries. These days, the allure is its store of value, if only in comparison with the stock market. "I've had farmers, businesspeople, people from all walks of life" as customers, says gold dealer Hendrickson. They might not be able to sell real estate or stocks quickly, but they can call Hendrickson and turn gold into cash. "It's always worth something."