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Gold and the Out of Whack Economy

by The Mogambo Guru

"In case you were wondering, China actually kicked our American butt a long time ago, as China 'surpassed the United States as the world's second largest gold producer in 2007 with 270.491 tons of output.'"

I am always looking for some extra money with which to buy gold, and if I am ever successful without actually getting a job, I intend to buy some right away, as Bob Moriarty at 321Gold.com has taken a look at the XAU gold equities index compared to gold, and finds that a recent ratio of 0.182 means that today "is the most negative ratio of gold shares to gold in the last five years. This week the ratio got even more negative with the ratio plunging to 0.176. People simply hate gold shares."

As a result, he says, "Since most profitable investors use contrarian opinion, the ratio is a screaming buy signal for both gold and gold shares."

Mark O'Byrne, Executive Director of Gold and Silver Investments and writing at MoneyWeek.com prefers his statistics on the fundamental side, and even so, agrees with this analysis and says so in an essay titled "Why Gold and Silver are Table-Thumping Buys."

He says that "Gold production is stagnating, and output in the leading gold producing countries continues to fall year on year, despite higher gold prices leading geologists to wonder whether we may have or may soon have reached the point of 'peak gold' production. The world's biggest producer - South Africa - produced nearly 1000 tonnes of gold in 1980. This was down to 264 tonnes last year, the lowest since 1932."

Even China is getting into the gold mining thing, as Chinainfoworld.com reports that "China Tops the World in Gold Output", which is something that I did not expect. In fact, "The China Gold Association announced that China's gold output was expected to reach 300 tons in 2008, surpassing that of South Africa and making China the world's largest gold producer."

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As a result, Mr. O'Byrne concludes, "Gold and silver are cheap vs. many commodities and oil", especially considering that "the long-term average gold-to-oil ratio is 15 to 1, or 15 barrels of oil to one ounce of gold".

Today, he notes, the gold-to-oil ratio is down in the low 7's, which is Very, Very Low (VVL). "At the higher end of the scale," he reminds us, "gold has traded at over 30 times a barrel of oil."

It is eerily similar, only more striking, with the oil-to-silver ratio! Silver is a screaming bargain!

With a sly smile, I realize he knows that I cannot calculate these kinds of things, so he helpfully adds "Should there be a classic reversion to the mean average of 4.4 in the ratio of ounces of silver per barrel of oil, then silver prices would rise to $30 per ounce! And silver is selling at less than half that price right now!"

With a burst of Mogambo Interpretive Thinking (MIT), I conclude that if there is one thing that you can count on in this crazy world, it is like Bill Bonner here at The Daily Reckoning once so famously said: "Things that are out of whack tend to get back into whack", which I extrapolate to mean that things that sell for half their value end up costing full price.

So if now is not the time to buy gold and silver, when things are so seriously out of whack, then when is? Hahaha! Exactly!