Seven reasons why gold should surge

Commentary: And how to play the move

I believe gold about to surge to $700 ... then $800 and potentially higher. Here are seven reasons why ...

1. China can't get enough gold
According to the China Gold Association, China's gold production hit 19.9 metric tonnes in January, up 25.7% from a year earlier. At this rate, China should produce 260 tonnes this year. And it's STILL not enough to meet Chinese demand - it falls about 100 tonnes short.
And the gap may be even BIGGER! This is "The Year of the Golden Pig," in the Asian calendar, and many Chinese buy gold to celebrate. China's 2006 gold consumption grew by an amazing 17%, and the Shanghai Gold Exchange reports that gold trading volume 72.83% in January.

2. Two India gold ETFs are launching
The first gold ETF in India is Benchmark Mutual Fund's Gold BeES. It launched on February 15. The second gold ETF in India is rolling out now, launched by UTI Mutual Fund. The new ETF is called, naturally enough, UTI Gold Exchange Traded Fund.
According to Rajesh Bhojani, President of Marketing for UTI Mutual Fund, about 30% of the gold market in India is investors. I wonder what the new gold ETF will do to that percentage?

3. Existing gold ETFs are pumping up demand
We already know what gold ETFs have done here in the U.S. When the StreetTRACKS Gold Shares gold ETF (GLD) started in November of 2004, it held about 100 tonnes of gold and gold traded at around $450 per ounce. Now, there are 476 tonnes and gold is trading around $650 per ounce. That's not a coincidence. The Gold Shares gold ETF and other gold ETFs around the world make it easier than ever for people to invest in gold. Why? Because there are several advantages of investing in GOLD ETFs:

- **No hassles of safety**
- **No resale concerns**
- **Quality Assurance**
- **No making charges**
- **More tax efficient in absence of wealth tax and long-term capital gains tax**
- **Despite the recent sell-off in markets of all types, the amount of gold held by the GLD barely budged (down 2.2% from its peak). I expect U.S. investors to start adding again, and that will drive prices even higher.**

4. Investment demand is booming
Reuters reports that worldwide investment demand for gold should remain at historically high levels this year, with investors continuing to buy large volumes of gold in bullion, coin and jewelry. CPM's 2007 Gold Yearbook

report predicted investors would likely add another 39.7 million ounces to their gold holdings in 2007, after investing 43.5 million ounces in 2006. I believe this estimate of demand is too conservative. See reasons 1 through 3 for why.

5. Central bank gold stockpiles have swooned to a 60-year low
The International Monetary Fund (IMF) reports that the amount of gold held by central banks and other government organizations declined for the eighth straight year in 2006. Bullion holdings were 867.6 million ounces last year, down 1.2% from 2005, the lowest since 1948, according to the World Gold Council.
The Russian Central Bank was the only one to make purchases last year, up 3.8% to 12.91 million ounces, according to the IMF. Speaking of China, it is still holding 19.29 million ounces in December -- unchanged since 2001. But here's some interesting news: China is setting up a managed fund to handle its more-than $1 trillion in currency reserves. This will be Asia's biggest government controlled fund. China has to do something -- 70% of its currency reserves are in the U.S. dollar and the greenback could get creamed as China's currency, the renminbi (or yuan) appreciates. China is already losing money on the deal, writing off $3.4 billion in exchange-rate losses in 2006.
In short, China needs to invest in something other than dollars. A smart move would be to buy more gold for its central bank reserves. Even a small move in this direction would send gold soaring.
What's more, central bank gold sales fell to 11.4 million ounces in 2006, down from 20.6 million ounces in 2005. If this trend continues, that will also boost the price.

6. Miners can't find new deposits fast enough
Analysis by Metals Economics Group shows exploration budgets increased to almost $7.13 billion in 2006 -- the fourth consecutive annual increase since the bottom of the exploration cycle in 2002 and the highest total since MEG began these reports in 1989. MEG analyzed budgets for 1,624 companies (using a $100,000 cutoff), which MEG estimates covers about 95% of worldwide commercially oriented nonferrous expenditures. Adding in the other 5% of companies gives total expenditures for commercial nonferrous metals exploration of $7.5 billion. That blows past the previous high of $5.2 billion in 1997 to set a new pinnacle of global nonferrous exploration.
So where is all this gold? Well, it takes time to bring new gold mines online ... and the big 'n' cheap-to-mine deposits have already been found. Meanwhile, production at existing but long-worked mines is grinding down. As a matter of fact ...

- **South Africa's gold output fell nearly 8% in 2006 from 2005. It is now at its lowest level since 1922!**
- **U.S. gold output for last year declined slightly from 262 tonnes to 260 tonnes.**
- **Australian production fell 4.5% to 251 tonnes.**
- **Peruvian gold production fell to 203 tonnes from 207 tonnes.**
- **Russian gold output dropped to 152 tonnes from 156 tonnes**

- **Canada's gold production fell a whopping 11% to 104 tonnes.**

Bottom line: Big gold producers are finding it tough to replace their reserves. That's why we saw huge mergers last year. Yamana merged with RNC Gold ... Glamis Gold bought Western Silver ... Goldcorp merged with Glamis ... Barrick bought Placer Dome.
Heck, just look at mine supply. Despite the price of gold rising for years, supply from mines is actually going DOWN. Since mine supply doesn't cover demand, where does the rest come from? From scrap, central bank gold sales and stockpiles, all of which are being depleted. And that is a recipe for much higher prices.

7. Gold charts show opportunity
Take a look at a weekly chart of gold. You can see that gold is channeling higher. The rate of ascent is INCREASING. It is at the BOTTOM of the channel now. It appears that gold is presenting the best buying opportunity since January. The next big move will likely be over $700 per ounce. And if we have a breakout, all bets are off.
Those are seven good reasons why I think gold will head higher. I could give you a lot more.