Gold Stocks: The Wide Angle View

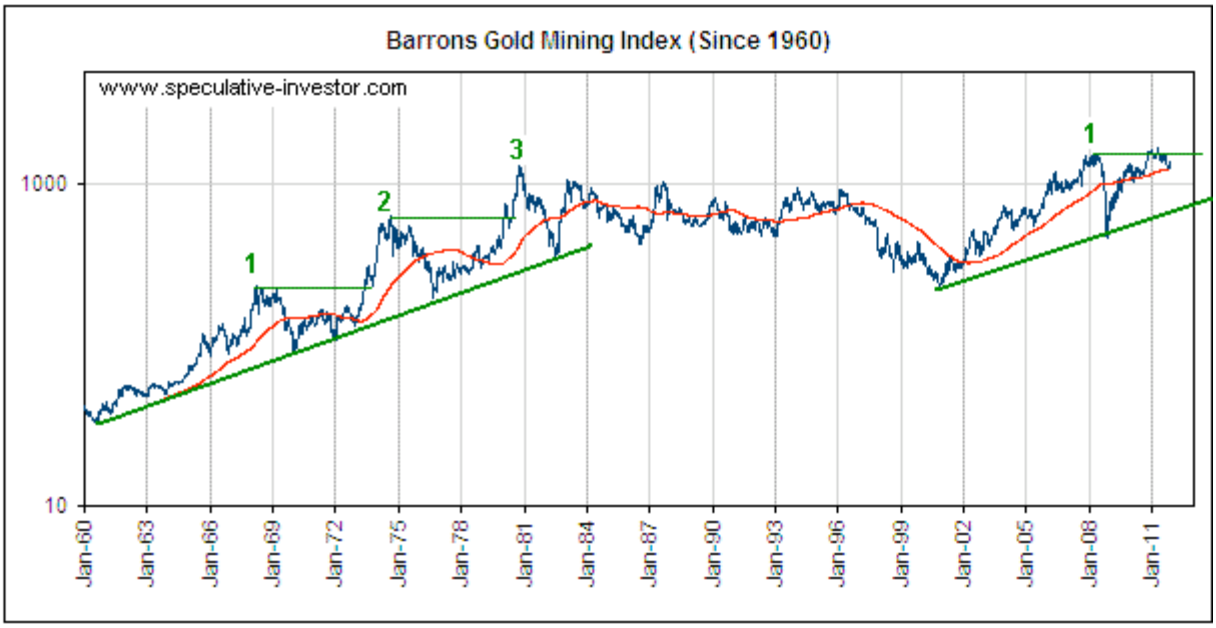
Below is an excerpt from a recent commentary at www.speculative-investor.com.

Gold stocks, as a group, did poorly in 2011. They did very well during 2009 and 2010, although the strong 2009-2010 performance was partly a reaction to the dismal 2008 performance. If we step back we see that despite experiencing some huge swings, they have essentially gone nowhere since March of 2008. In other words, long-term holders of gold stocks have now spent almost 4 years treading water in rough seas.

If past is prologue, the gold sector's performance over the past few years is encouraging. We say this because if we step even further back we see that the current long-term bull market is continuing to evolve in a similar manner to the long-term bull market that extended from the early-1960s to 1980. In particular, with reference to the following weekly log-scaled chart of the Barrons Gold Mining Index (BGMI) we see that:

1. The previous bull market had three major upward legs separated by huge corrections back to a long-term trend-line (drawn in green on our BGMI chart). The new bull market appears to have completed the first major upward leg and the first huge correction back to the long-term trend-line (the trend-line under the current market is drawn parallel with the earlier one to help make the point that the long-term pace of advance is roughly the same in both cases). In terms of time it now appears to be about half way into the second major upward leg, although in terms of price it is probably less than half way. This is because a disproportionately large percentage of a multi-year up-leg's price gain usually occurs during its final 6 months.

2. After the 60s-70s bull market reached the top of a major upward leg (the points labeled 1 and 2 on our BGMI chart), more than 5 years elapsed before there was a decisive break to a new all-time high. If the current market does something similar then there won't be a decisive break into new all-time-high territory prior to the second quarter of 2013. The point, here, is that the gold sector's seeming inability over the past 12 months to embark on a powerful new upward trend is consistent with what happened during the previous long-term bull market.



Now, we shouldn't blindly assume that the current long-term bull market will continue to track the earlier long-term bull market. Real-time analysis is required at each step along the way, because the current market could end up doing better or worse than the earlier one in response to contemporary fundamental developments. We are simply trying to show that the frustration being experienced by today's holders of gold stocks was most likely also experienced by holders of gold stocks at a similar stage of the 60s-70s bull market. In fact, the level of frustration could have been higher back then because this time around the BGMI was quicker to recoup the losses incurred during its first major correction.

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