5 Reasons Gold May Have Finally Hit Bottom

Description

Over recent months gold has taken a severe mauling, with its price hitting its lowest point since April 2010 only six weeks ago on the back of a resurgent U.S. dollar and declining oil prices.

But since then, gold has rallied 8% and there are signs its price will climb higher. Let me explain why.

1. China continues to accumulate record amounts of gold

Total gold imports to China are up with both the lower gold price and seasonal demand driving higher overall purchases. This burgeoning demand now sees physical settlement volumes for the country's largest gold exchange, the Shanghai Gold Exchange, up by 15% for the year-to-date when compared to the equivalent period in 2013.

With China's government expected to implement a plan opening up access to gold imports and reducing the premium for Chinese buyers, this strong growth in demand can only continue.

China is already the world's largest consumer of gold and I expect this to remain the case. China's government remains intent on hoarding gold, while an increasingly wealthy middle-class continues to drive demand higher.

2. Global central bank demand for gold remains strong

Growing economic and geo-political uncertainty continues to drive central bank demand for gold as nations seek the protection and diversification it offers. During the third quarter 2014 a number of countries again boosted their gold reserves, with the largest buyer being Russia, which purchased 55 tonnes followed by Kazakhstan with 28 tonnes.

For the same period, central bank sales of gold remained meagre and the World Gold Council expects this strong central bank buying to continue, further underpinning the gold price.

3. A number of countries are repatriating gold

While the Swiss gold initiative failed to pass a popular vote last month, other nations have commenced their own gold repatriation programs. The Netherlands repatriated 3.9 million ounces of gold during November, while Belgium is investigating repatriation of its gold reserves. Germany also implemented its own repatriation program last year, though it appears to have lost momentum at this time.

This highlights growing concerns among governments about rising global instability and their desire to have greater control over their gold reserves as a means of protecting themselves from a new global financial crisis.

4. Major institutional investors are buying gold

Ray Dalio, who runs the world's largest hedge fund, Bridgewater Associates, has allocated 7.5% of his portfolio to gold. This has seen him make some big bets on beaten down gold miners, boosting his stake in **Goldcorp Inc.** (TSX: G)(NYSE: GG) by US$6 million and **Barrick Gold Corp.** by US$4 million during the third quarter.

Another hedge fund manager, Donald Smith, in the same period bet US$17 million on struggling **Kinross Gold Corp.** and boosted his total investment in **Yamana Gold Inc.** to US$236 million.

These and other institutional investors are obviously seeing bright prospects ahead for gold and clearly are not expecting its price to decline, indicating the rally is set to continue.

5. Global gold supplies are declining

According to the WGC, third-quarter gold supplies declined 7% year-over-year, despite marginally increasing mine supply. This was because recycled gold supplies for the same period plunged a massive 25%.

The WGC also expects growing mine supply to wane as miners hold off on the development of major projects because of the uncertainty surrounding the gold price. According to the WGC, year-on-year growth from projects that came online over the last few years had a diminishing impact on the cumulative supply of gold.

Clearly with demand set to rise, a constrained supply situation will help to further boost the price of gold.

What should investors do?

While I certainly don't advocate "betting the house" on a contrarian play in gold, investors should consider allocating a proportion of their portfolio. This will allow them to take advantage of the rebound in gold prices while hedging against further economic and geo-political uncertainty.

I believe the best way to do this is by investing in Goldcorp, which continues to attract the attention of Wall Street because of its solid balance sheet, high quality assets, and growing gold production.

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