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Investment Demand Forecast to Drive Prices Towards $480/oz in the Fourth Quarter

Investment demand from funds and private investors in Europe and North America was generally lacklustre during the first half of the year. The important exception to this was fund activity on the Comex, which at times resulted in substantial long positions in futures being temporarily established. In the third quarter to-date buy-side interest has been maintained on the New York exchange, with the non-commercial net long, for example, reaching a record level in August. There have even been signs of "western" investment demand stirring outside the exchange - demand for gold via exchange traded funds, for example, has risen in recent weeks.

Even though in the short run GFMS expect some reduction in funds' net long positions on Comex (and for this to have a negative impact on prices), the general trend in investment demand is expected to become increasingly more positive as we move into the fourth quarter. Indeed, not only should Comex continue to see a high level of demand from fund longs but also that investors more generally will increase their exposure to gold, in particular via Over-The-Counter market instruments.

The reasons for expecting an important pick-up in investor demand are several. First, investors will be encouraged by the fundamental support for gold from fabrication demand and to a lesser extent de-hedging, which has allowed the market to absorb a significant increase in supply from central bank sales without the price moving lower. A higher floor should be interpreted as providing a good platform for a rise in the price. Second, the US dollar is likely to come under renewed pressure as more attention is paid to its poor and deteriorating fundamentals as opposed to short term interest rate differentials. Third, other competing assets - namely bonds and, especially, stocks - are unlikely to do well under the probable scenario of lower US and world GDP growth. Fourth, and related to the previous point, investors are expected to increase their exposure to so-called "alternative assets". This could well benefit gold both directly via outright purchases of the yellow metal and indirectly through funds buying commodity indices that include gold. Fifth, inflation concerns are mounting due to the ongoing impact of $70/barrel crude and striking rises in oil product prices in the wake of Hurricane Katrina. And, finally, the global political environment arguably remains supportive, with for example the United States and its allies bogged down in Iraq and the crisis over Iran's nuclear ambitions becoming more serious.

Given the small size of the market, an inflow of even a few billion dollars of fresh money into gold would have a meaningful impact on prices. For the reasons cited above, GFMS believe that the probability of this will grow as we move into the fourth quarter. Growing investment demand is therefore forecast to drive prices to new highs for the rally-to date before year-end.

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Gold Survey 2005 - Update 1 provides a thorough and comprehensive interim analysis of the most recent developments in the global gold market. In just 40 pages, *Update 1* identifies the most important economic, socio-political and market-specific issues facing the gold market.

The publication can be ordered from GFMS for £205 or US$375 / €315 per copy. For orders and to receive further product information please contact Ms L. Perrard on: Tel: +44 (0)20 7478 1777, Fax: +44 (0)20 7478 1779, Email: sales@gfms.co.uk, Web Site: www.gfms.co.uk

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