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SEPTEMBER 2024

Gold Stocks and Great Financial Bubbles
Just Early into a Multi-Year Bull Market
At Times Outperforming the S&P
And With a World-Scale Discovery: Fabulous Action

A Great Financial Bubble is a very exciting event for everyone from direct participants to looky-loos, including an enraptured media. Generated by human action with far too many participants thinking the Bubble is unique and enduring.

With five previous examples, gold's real price weakened a little as the Bubble climaxed. A page of charts follow.

Typically, with the Bubble's climax and collapse, gold's real price turns up as real base metal prices turn down. Major mining companies should be aware of these historically profound influences. Post-Bubble Contractions can endure for a couple of decades.

Bubbles are endearing – yes – but having occurred five previous times to 1929, each enjoyed a compelling mania before suffering a nasty collapse and sequel. Most participants get caught up in the "Now" and don't have the motivation to contemplate the full perspective.

As the saying goes: *"Every generation gets to invent sex, only every other generation gets to invent a Bubble"*.

Particularly, today as central bankers do not want to think there could be another such disaster as the 1929 Bubble. And consequent Horror Show. Moreover, Wall Street commentators during today's just as obvious excesses are reluctant to make the comparison.

And the stock market, which usually leads the economy by around seven months, no longer leads, but turns down, virtually with the economy. As policymakers are unaware of this, the S&P stays in the Leading Indicators.

It is worth including that with the 1929 Bubble the NYSE reached its best in that fateful September, as did the example that climaxed in 1873. Also, worth emphasizing is that the NBER determined that the economy peaked in October 1873 and reached its best in August 1929.

Indeed, motivation behind the Fed's formation in 1913 is fascinating. Then, influential bankers fully understood that a credit crisis triggered a recession. Which prompted the notion that a wisely-timed injection of credit would prevent a crisis and – Presto! – no more recessions.

In 1873, Walter Bagehot, the esteemed editor of *The Economist*, recorded the remedy in his book *Lombard Street*. He described the crisis as a form of "neuralgia" and the prescription was to artificially inject liquidity. Ironically, that Great Depression endured from the 1873 Bubble to 1895, when the next long expansion got underway.

Also, that summer, the New York Herald editorialized that the US would be more able to prevent a recession. It did not have a central bank and not being on a gold standard, the Treasury had virtually unlimited power to prevent recessions.

In the early 1880s, British economists began calling the prolonged weakness as the "Great Depression".

The preventative concept was called "Lender of Last Resort", which today is still highly regarded. It is outside the pale to note that there have been 18 cyclical recessions since the tout that they could not happen anymore. Ironically, as the recession, which was impossible, naturally ends, Fed Chairs have boasted that their liquidity injections prevented it from enduring into the foreseeable future.

That deliberate Fed tightening caused the Depression is taken apart by a practical editorial published by Barron's in July 1932. Indeed, the Fed had been injecting liquidity:

"***The Federal Reserve policy of cheapening credit through the purchase of government bonds has been unable to make a dent in the conservatism of borrower or bank lender, in short, every anti-deflationary effort has yet to provide positive results. The depression is sucking more and more bonds into its vortex***."

But it was not a "usual" crisis as following a Great Bubble a Great Depression is next on the schedule.

Further, neither 1929 nor our recent Bubble are unique.

The full list includes 1929 as Number Five, which was preceded by the example that climaxed in 1873.

Both were followed by Great Depressions as was the example that completed in 1825. Of course, the first one, the infamous South Sea Bubble climaxed in June 1720, and was followed by a severe Crash in the fall.

The amazing thing is that without any knowledge of past Bubbles the crowd, as well as policymakers, have been able to replicate the identifying features:

* Real Long Interest Rates Reverse to Rising
* Gold's Real Price Turns Up
* The Senior Currency Firms
* Copper's Real Price Declines

This is a methodical way of tracking the usual transition from boom to bust. Although only in an early stage now, they are close to the typical path.

The suggestion that Gold's Real Price can go up with a chronically firm dollar may seem improbable, but if it has happened it can happen. In dangerous conditions, the careful money goes to the most liquid items. Shorter than one-year Treasuries in the senior currency, offer outstanding liquidity which will provide a bid for the dollar. Of course, gold also offers liquidity which inspires a bid as well.

The prospect of a firming dollar and rising real prices for gold can't be imagined by orthodox gold commentators.

All five previous Great Bubbles climaxed and suffered an Autumnal Crash and four out the five were followed by Great Depressions that prevailed for a couple of decades.

The 1772 Bubble was not followed by a lengthy depression in the commercial regions of the world. Perhaps too many wars were waged by England and France.

The following charts display Gold's Real Price through each Bubble. This shows the key reversal, and the typical full increase was some 1.7 times. That was on annual averages, making it practical to look for a double over the next couple of decades.

For perspective: On buying the S&P in 1929 it took until late 1958 to break even.

Investors should consider seriously reducing both sides of the 60/40 portfolio and positioning good grade corporate bonds that mature in three to four years.

Mining companies could consider selling base metal production and expanding gold operations. There is an index of Base Metal Miners, which set a big high in 1872 at 400 and twenty years later it was around 50.

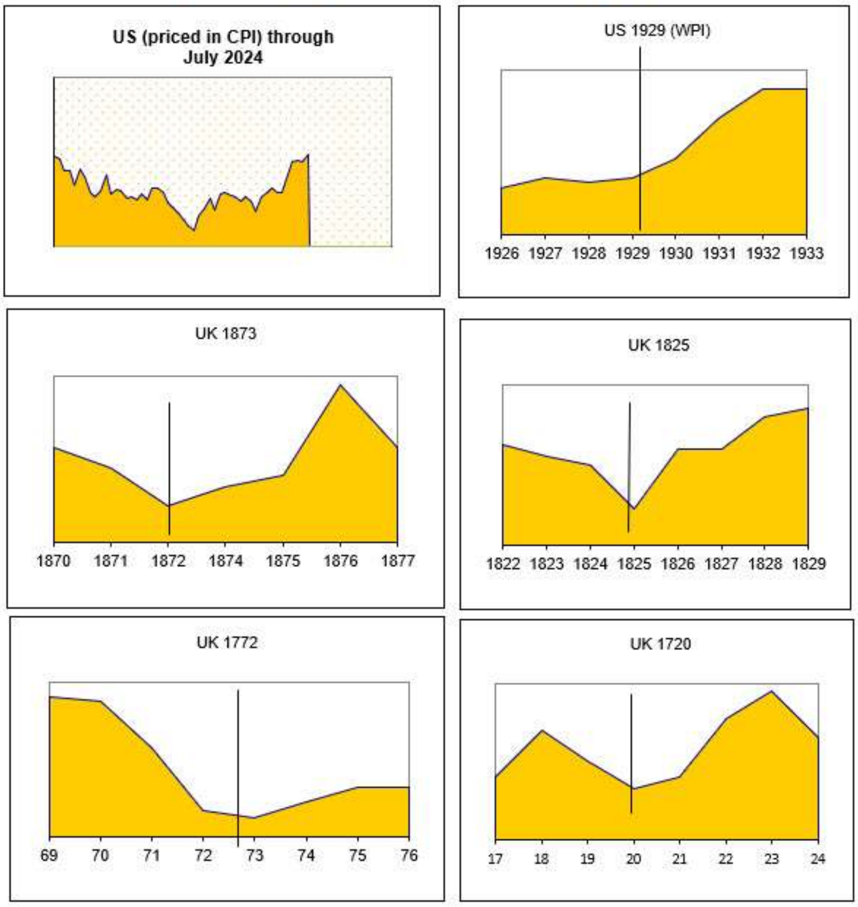
In the gold sector, it was around 1879, when George Hearst wrote to his fellow Homestake directors. The advice was that neither they nor their heirs should ever sell their stock. Operating until 2002, it produced some 43 million ounces of gold and many more of silver. It became one of the longest-trading stocks on the NYSE.

While the action now in Golds has become overbought, it is in the early stages of a long bull market.

The following pade of charts shows gold's real price through all Bubbles:

Deflated Price of Gold

Senior Currency: All Six Great Bubbles



Over the many years of the Post-Bubble Contraction, the typical increase in the Real Price has been almost a double. Making gold mining increasingly profitable. At times the sector could outperform the S&P.