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Up and Down Wall Street
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This Time, Gold Bugs May Have a Point

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Illogical dumping raises questions about causes of the metal's sharp decline.

Stocks are for lovers and gold is for haters. That's how one especially supercilious strategist (is there another kind?) sizes up the two markets, and it's clear he's been feeling the love lately. Stocks are at new highs in the U.S. and many other venues, while Japan's market is strapped to a rocket ship, all propelled by money fresh off the printing presses of the world's central banks.

Fans of the yellow metal, meanwhile, are feeling rather battered and bruised these days from the beating they've taken over the past month or so and, indeed, for more than a year and a half. Given all the quantitative easing—which is how money-printing is referred to in polite company these days—one would think gold would be getting a little love (or a facsimile of the same that cash can sometimes provide.)

It's not just the likes of the Dow industrials or the S&P 500 at record levels; money is sending all manner of stuff soaring. Last week's auctions at Christie's in New York marked the beginning of "a new era" in the art market, the auction house declared, with nearly a half-billion dollars' worth of 20th-century works being snapped up by bidders who coveted them as much as stores of value as pieces of art. How else to explain Jackson Pollock's drip painting, Number 19, 1948, going for a record $58.4 million, about twice the $25 million-to-$35 million it had been expected to fetch?

And the superrich again are falling over themselves in yet another round of "can you top this" in buying up trophy homes. It isn't just Russian oligarchs looking to get their wealth out of the country by snapping up Manhattan condos in the tens of millions, or newly minted South American millionaires swooping into Florida to buy properties at knock-down prices that are even bigger bargains in devalued dollars. Howard Stern reportedly is buying a Palm Beach house for a tidy $52 million, yet another sign of a surfeit of money over taste these days.

But with all this dough being thrown around promiscuously at every so-called asset class—as indulgences such as mansions and art have come to be

classified, even if they really are forms of conspicuous consumption—why doesn't gold get any ardor? After all, for reasons probably buried deep within the human genome, the precious metal has been sought for thousands of years as an object of adornment and, most importantly, a store of value.

That value has been battered of late, with massive outflows from gold-related exchange-traded funds, notably the SPDR Gold Trust (ticker: GLD.) For a brief time, it actually was the world's biggest ETF, eclipsing the SPDR S&P 500 (SPY), just before gold hit its high of about $1,900 an ounce in September 2011. Indeed, it has been the flight from "paper gold"—ETFs and futures or options contracts—that has sent the metal tumbling, from a recent high of $1,800 last October, to around $1,700 at year end, and about $1,600 as recently as the end of March. That was just before the market plunged—or was pushed—into a virtual free-fall in mid-April that slashed the price by more than $200 an ounce in just two sessions. So extraordinary was the 9.4% collapse on April 15, wrote Howard Simons of Bianco Research at the time, that the odds against such a move were 20 trillion to one—"a lower probability of occurrence than randomly selecting a [particular] $1 bill out of pile of singles representing the U.S. national debt."

These improbable moves have made gold bugs suspicious, which isn't unusual. Folks who own gold do so because they don't trust the status quo, especially when it comes to government-issued paper money. But just because you're paranoid doesn't mean somebody isn't out to get you. They point to bursts of selling on Friday, April 12, which resulted in prices plunging by more than 5%, and to dumping that resumed the following Monday in Asia, early in the day when markets are illiquid. That culminated in a 9% collapse by the time the New York market had settled. But a seller who wanted to unload a large position at the optimal price would have done precisely the opposite—liquidate as discreetly as possible. Instead, sellers dumped the equivalent of more than 300 tons of the metal in staccato-like blasts during those sessions.

THE SUSPICIOUS SELLING resumed this Friday, with the equivalent of 17 tons sold on the New York Comex in two bursts in the morning, according to market sources. And the declines continued after the settlement of futures trading in the early afternoon as the SPDR Gold Trust ETF slumped a total of 2.25% on the day, to close at 131.07, below the April 15 close of 131.31. (The ETF represents a bit less than 1/10th of an ounce of gold.) The current-month May futures contract plunged 1.6%, or $22.20, to $1,364.90 an ounce on the Comex.

Over the past seven sessions, the metal has shed over $100, or more than 7%, all but wiping out the rebound after the stunning mid-April collapse. That slide

had sparked a wave of bargain-hunting in physical gold around the globe, especially in Asia, where it was suddenly seen as cheap at the marked-down prices. The markets for paper gold and the actual metal thus showed a marked contrast in sentiment. The latter was eager to buy what the former dumped, something that makes you say 'hmmmm.'

There were a number of other curious aspects to the latest plunge in the GLD (everybody in the market refers to the big exchange-traded fund just by its ticker.)

Barron's options guru, Steve Sears, reports heavy buying in the GLD weekly put option with a 132 strike price that expired Friday. That option, which would have expired out of the money—and thus worthless—wound up solidly in the money after the ETF's drop.

Back in February, Sears began to pick up signs of increased GLD put buying and in his Striking Price column just before the big break ("A Hot Potato That Glitters," April 8), he suggested the purchase of weekly puts that paid off hugely the following Friday.

While the gold bugs point to this mysterious, concentrated dumping on big down days, it's clear that large-fund managers both followed and led the retreat in gold by selling their holdings of GLD. That's what our exchange-traded fund maven, Brendan Conway, pointed out Friday in his Focus on Funds blog on Barrons.com. He noted that Commerzbank's commodity strategists had found that 75% of redemptions of GLD came from institutions, based on their quarterly filings with the Securities and Exchange Commission.

NORTHERN TRUST (NTRS) WAS THE biggest seller, liquidating the equivalent of 910,500 ounces, followed by BlackRock (BLK), with 428,500 ounces. In contrast, the iShares Gold Trust (IAU), the smaller ETF representing 1/100th of an ounce of gold and favored by individuals, saw lesser outflows.

At the same time, the options action has been weighted heavily to the put side, which has had the gold crowd on anxious alert.

Farallon Capital, the San Francisco hedge-fund operator founded by Democratic Party rainmaker Tom Steyer, listed in its first-quarter 13F filing 600,000 GLD put options, which sent ripples through the market. With each contract representing the right to sell 100 shares, that would have equaled 60 million shares of GLD, worth more than $900 million at quarter-end.

In actuality, the options position was equivalent to 600,000 shares of the ETF, as a revised filing indicated. A fund spokesperson said that the put designation "was put in the wrong column." Still, the fund listed a roughly similar amount of both calls and puts in its year-end 13F filing, evidently betting on a breakout either way. The latest data show it squarely on the short side of gold.

Gold bugs spy an agenda in all the concerted selling to discredit the metal and burnish the allure of stocks and bonds. The evidence remains circumstantial in that regard, but shouldn't be dismissed. The huge bouts of selling are irrational for a profit-maximizing investor.

Be that as it may, will the slide continue or is a rebound looming?

Charles Nenner, who heads the research firm bearing his name, watches recurring market cycles. Nenner, who advises hedge funds and sovereign-wealth funds, calls the current swoon a correction in gold's long-term bull market, from which he recommended temporarily exiting at $1,900 an ounce at the top in September 2011.

Now, Charles looks for a bottom sometime in June—but there could be another spill before then. The risk, he warns, is that gold tumbles to $1,284. So, don't try to bottom-pick just yet.

(As an aside, Nenner also recommended the sale of Apple (AAPL) at $700 last September. In case you've been doing a Rip Van Winkle since then, the stock closed Friday at $433.26.)

The last time gold was held in such low esteem was during the fin de siècle dot-com bubble. It's feeling as if we're partying like it's 1999 with darlings like Tesla (TSLA) doubling in the past month or so, and analysts playing "can you top this" with their price targets for Google (GOOG) as it soars past $900 and seemingly heads to quadruple digits.

I guess you could say love is in the air.

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