Wealth Enhancement®

Gold Beyond the Myths: What Really Moves the Market

Gold has long fascinated investors, especially during times of economic uncertainty. But does it truly live up to its reputation as a hedge against inflation or a safeguard against fiscal instability?

Historical Roots of Gold and Inflation

There is a psychological factor rooted in history that drives most of the inflation hedge narrative. Those roots stem from a Global economic agreement made in New Hampshire in 1944.

Following World War II and the Bretton Woods Accord, gold was pegged to the dollar at $35 an ounce and other currencies were pegged to the dollar. Bretton Woods created a gold standard around the world which stabilized global currencies where economies were completely devastated. At the time, most of the gold reserves were held in the United States, so the system was manageable. European countries could borrow dollars, rebuild their economies, sell product to the United States, repay the dollars, and use profits to build gold reserves.

Trade deficits led to more dollars being exported. Gold was exported overseas as dollars were used to redeem bullion. As inflation pressures built, gold left Fort Knox at accelerating rates as the $35 peg became more and more irrational. Like a bank run, the fear was that a system that had too many dollars chasing too little gold. These events culminated in the Nixon shock in 1971 which led to floating exchange rates, and by 1980 gold had risen to over $600 an ounce.

These events left a lasting impression on those who lived through that experience of the ‘60s, ‘70s, and ‘80s. However, statistical evidence shows that gold’s relationship with inflation is unstable save for that initial shock. Sometimes it is positively correlated and sometimes negative, making it hard to justify inflation as a reason to be in gold.

Federal Budget Deficit and the Dollar: Does Gold Benefit?

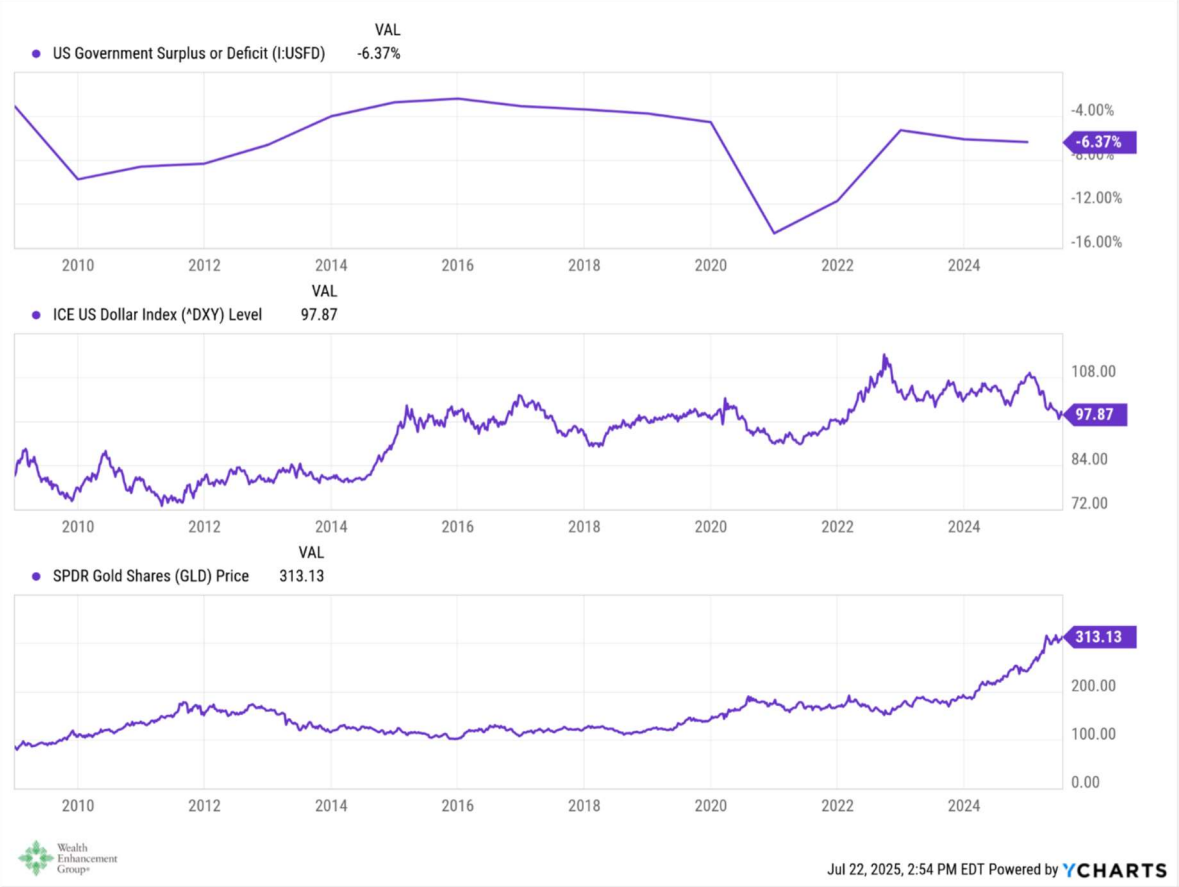
The logic behind the “deficit/gold” theory is that persistent overspending by the Federal Government would weaken or “debase” the dollar. Since gold cannot be printed and is finite it would be a better store of value in a worst-case scenario.

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

There's little evidence that federal deficits weaken the dollar. For example, the DXY (dollar) index rose from near 90 to around 108 during the hyper deficit pandemic spending (-14.67%) of the CARES act. Despite the surges in the deficit and dollar, the GLD ETF stayed around $170 a share.

Contrast that with the post financial crisis period: GLD nearly doubled from $87 in 2009 to $157 at the beginning of 2012. If gold were reacting purely to a weakening dollar, you'd expect a sharp drop in the DXY, but it only slipped modestly from 85 to 80. Additionally, the deficit got larger at the beginning of the financial crisis, but it was narrowing during gold's bull run from -10% to -8%. These inconsistencies challenge the idea that deficits and dollar weakness reliably drive gold prices.

More recently we have seen gold scream higher. GLD has gone from $187 at the beginning of 2024 to $313 as of this writing. The deficit is getting larger and the dollar is weaker over that time frame, but likely not enough to explain to burst in gold.



Supply and Demand Dynamics of Gold

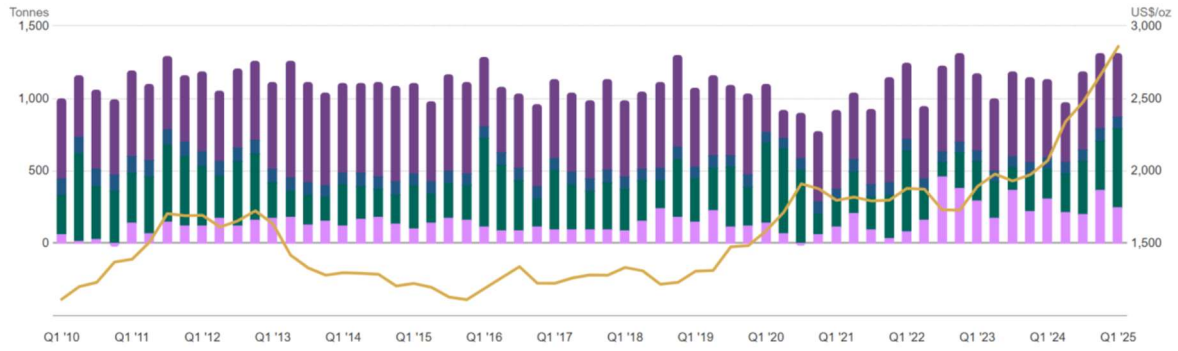
Supply

The amount of gold that has been mined only increases by about 1.5% a year with modest and reasonably predictable increases in costs of production.

Demand

1) ~7% of gold demand is attributable to industrial use.
2) ~45% of mined gold is used for jewelry and vanity.
3) ~20% is held at central banks globally.
4) ~The remainder is mostly held for investment purposes.

Jewelry fabrication has trended down as the recent price of gold has ballooned. Industrial use has risen just modestly. However, the investment portion has risen.



Data as of 31 March, 2025
Sources: ICE Benchmark Administration, Metals Focus, Refinitiv GFMS, World Gold Council; Disclaimer

Gold Demand & Supply by Country | World Gold Council

We can see that there was a rapid increase in demand from central banks following the invasion of Ukraine in Q1 2022. At the same time, the United States restricted Russian use of the SWIFT system effectively freezing reserve assets. In response, it logically follows those central banks turned to gold and other assets as more reliable reserves. Additionally, it looks like the price momentum has led to 5.5 times more investment since the beginning of the rally.

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

Since central banks and investor momentum have driven the demand and price for gold recently it has become a very unpredictable asset to me.

For example:

1) If a war started in 2022 kicked off this trend would a cease fire reverse trend?
2) Could central banks start to sell down gold to buy their own currency?
3) Could central banks use gold to fund necessary imports?
4) If central banks began to sell would investors follow suit in a momentum reversal?

Finally, would any of the answers to these questions be knowable and transparent? The following questions make gold a hard asset to hold right now despite the recent great performance.

Gold as a Currency: When it Makes Sense

I view gold as a global currency with a perpetually zero interest rate. It has historically been a store of value, and as we saw with the central bank reserves, it still seems to be. When global interest rates are high and rising, all things equal, I would expect gold to weaken. When interest rates are low and falling, all things equal, I would expect gold to strengthen.

From the summer of 2019 to the end of 2020, I held GLD in our strategies. The ECB rate was negative and stable. The Japanese rate was near zero and stable. The Canadian rate was low and stable, and most importantly, the US Fed Funds rate was falling. Gold subsequently followed suit.

Conclusion: What Has Moved Gold and How to Allocate

Gold’s role as an inflation hedge is often overstated, largely due to a dramatic historical episode that continues to shape investor psychology. Recent price surges are frequently linked to fears about inflation and federal deficits, but the evidence for that connection is weak. The more compelling drivers have been increased central bank buying and investor momentum. With so many variables influencing gold, the key is to have a clear, consistent rationale for owning it that helps you enter and exit the asset confidently.

This information is not intended as a recommendation. The opinions are subject to change at any time and no forecasts can be guaranteed. Investment decisions should always be made based on an investor's specific circumstances. Investing involves risk, including possible loss of principal.

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

Wealth Enhancement®

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.