Gold-to-silver ratio hits 50-year high

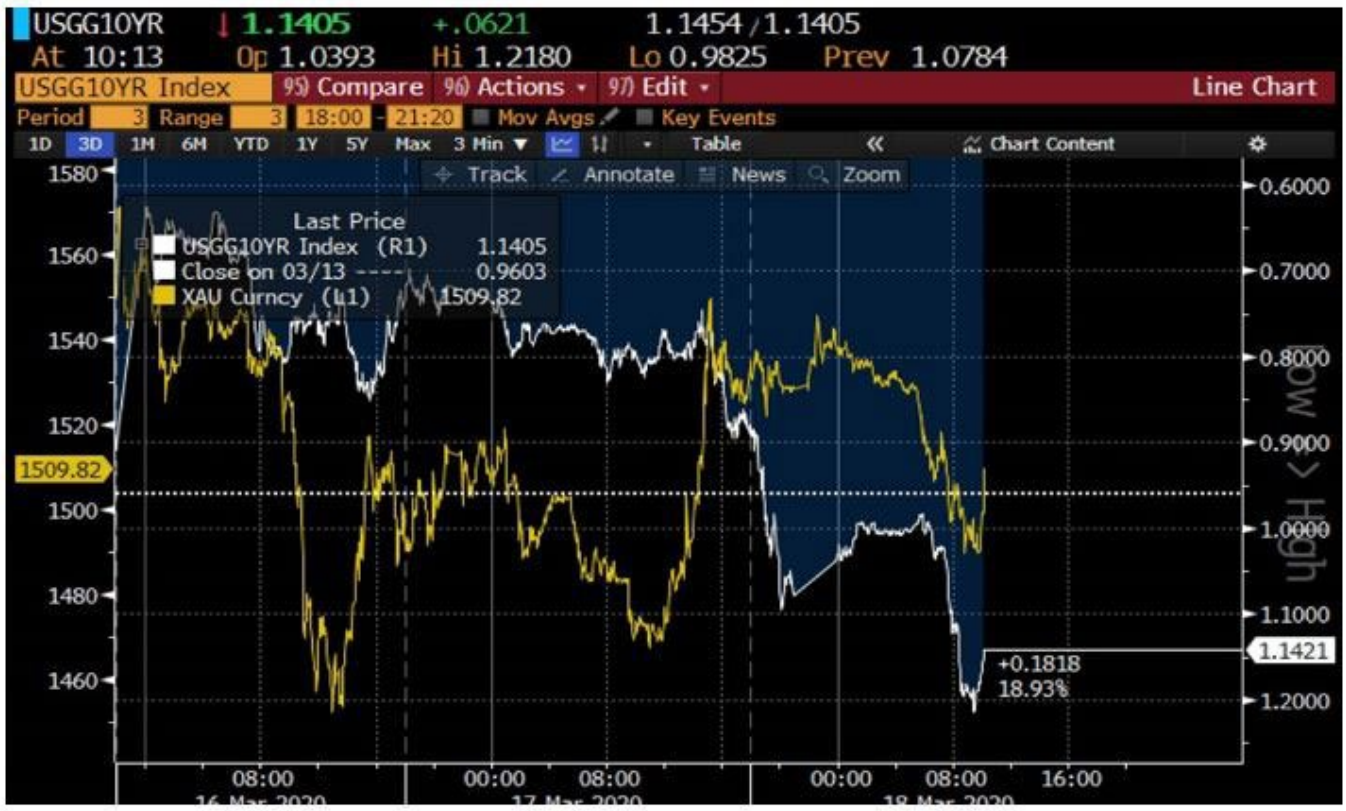
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Nitesh Shah

Head of Commodities and Macroeconomic Research, WisdomTree Europe

Gold, despite being a defensive asset that one might expect to rise in the current environment, is actually falling. That appears to be the result of the demand for liquid assets to meet margin calls in extreme violent declines in cyclical assets. The CBOE Volatility Index (VIX) has hit all-time new highs on 17/03/2020, highlighting just how violent the equity moves are. Treasury prices are also falling in line with gold – underscoring the view that this is liquidity driven (see Figure 1 below).

Figure 1: Gold (left, yellow), US Treasury Inflation Protected Securities, (right, white), 16-18th March 2020



Source: Bloomberg. 16/03/2020 to 18/03/2020. Historical performance is not an indication of future performance and any investments may go down in value.

The Federal Reserve's reinstatement of the Commercial Paper Funding Facility (CPFF), only provided temporary relief on 17/03/2020 as gold has resumed its downward moves on 18/03/2020 and central banks will likely need to provide more liquidity relief if this is to continue.

Silver is falling harder than gold in this environment, experiencing a double whammy. Its close correlation with gold is negative at the moment with liquidity concerns and its cyclical traits are also negative. The global manufacturing sector is suffering the worst declines since 2009 (based on Global Purchasing Managers Indices released on 2 March 2020), and by the time the next PMI data release comes it out, we could find we are experiencing the worst manufacturing decline on record. As a result, the gold-to-silver ratio has hit levels not seen before (Figure 2 below).

Figure 2: Gold-to-silver ratio 1970-2020

That indicates that silver is cheap relative to gold but if liquidity issues are resolved, we believe gold will start to perform very strongly and play its traditional role as a safe-haven asset. We also believe that silver will move in correlation with gold when gold turns. Given that silver is also driven by manufacturing trends, its gains will be capped and we think the gold-to-silver ratio could drop from the 120 range to 80 range which will still be very elevated by historic standards.
So, if gold ends the year around US$2000/oz, that indicates a silver price of US$25/oz (more than double today's price). Even if the gold-to-silver ratio only drops to 100 (and gold rises to US$2000/oz), we could get a silver price of US20/oz which would be a 60% rise from the price on 18/03/2020.

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