Gold Plunges as Fears Over Inflation Fade

Metal’s 9.4% Drop on Comex Is Largest in 30 Years

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Gold posted its biggest one-day percentage drop in 30 years Monday as new signs of a global economic slowdown emerged and fears diminished that central banks' easy-money policies would stoke inflation.

Gold futures for April delivery fell $140.40, or 9.4%, Monday to a two-year low at $1,360.60 an ounce on the Comex division of the New York Mercantile Exchange. That extended their bear-market descent of more than 20% from their 2011 all-time high. Since Thursday, gold prices have declined by more than $203 an ounce, a record skid since the futures began trading in the U.S. in 1974.

The reversal comes as investors are grappling with signs the global economic expansion that began in 2009 is slowing.

The prices of industrial commodities ranging from copper to crude oil tumbled Monday, following news of softer-than-expected economic growth and industrial output in China. Adding to the gloom, the Federal Reserve Bank of New York issued a report showing manufacturing in the region barely expanding.

The Dow Jones Industrial Average marked its worst one-day point decline since Nov. 7, 2012, dropping 265.86 points, or 1.8%, to 14599.20. Declines in commodity-linked sectors such as mining and energy led the selloff, with Freeport-McMoRan Copper & Gold Inc. dropping 8.3%.

The market selloff continued in early trading Tuesday in Asia, with Japan down 1.3%, Korea down 0.5% and Australia down 0.8%. Gold also traded lower on the Tokyo Commodity Exchange, triggering circuit breakers because of steep price drops.

After posting 12 consecutive annual price rises, gaining more than 500% over that span, gold is suddenly being shunned by investors who once saw it as a way to generate outsized returns without the volatility and uneven performance in the stock, bond and real-estate markets.

"The trade is over," said Jason Tamayo, a 24-year-old U.S. Navy veteran who bought about $50,000 in gold—around 30 ounces—in October on the view the metal would continue to march higher amid worries about U.S. debt and the stability of the global economy. Mr. Tamayo said he sold his gold Friday, at a loss of $7,200.

The Japanese yen—which has lost almost a quarter of its value against the dollar since October, amid expectations the Bank of Japan would buy more assets in a bid to reverse years of falling prices—rose 1.6% in its sharpest advance since Feb. 25.

The gold rout stemmed partly from worries Cyprus and perhaps other nations may become sellers of the precious metal. Other price drags cited by traders included a sale recommendation on gold last week.
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The price of gold slumped to $1,400 an ounce in what appears to be panic selling after China's first-quarter growth came in lower than expected. Other markets were also hit, with silver and other commodity prices and currencies like the Australian dollar are falling too. Photo: Bloomberg

Gold by the Numbers
Gold continues its slide further into bear-market territory. According to the WSJ Market Data Group, as of Monday settlement, gold registered:

- Biggest one-day dollar decline since Jan. 22, 1980.
- Largest one-day percentage decline since Feb. 28, 1983.
- A year-to-date decline of 18.76%.
- Its second-largest dollar drop in Comex history.
- Down 13.02% over the past two sessions.
- Off 27.96% from its record settle high of $1888.70, hit on Aug. 22, 2011.

Gold falls to a two-year low on Monday. A gold-buying company in New York advertises in the city's jewelry district.

But the inflation hasn't arrived, despite all the money-printing by central banks. Consumer prices in the major developed economies are increasing at a less-than-2% annual pace; in the rest of the world, that is around 6%.

"Inflation has been remarkably quiet of late," the International Monetary Fund observed last week. "As long as inflationary expectations remain firmly anchored," it said, "fears about high inflation" shouldn't prevent central banks from pursuing their easy-money policies.

Gold Plummets, But Not at Jewelry Store

From Goldman Sachs Group Inc., and a growing view that stocks are better investments, due to continuing low inflation.

"Forced selling" by investors holding gold was also among the reasons stock and commodity markets tumbled Monday, said John Brynjolfsson, who runs the $1 billion hedge fund Armored Wolf LLC. Investors who borrowed to buy gold at higher prices could be forced to sell other assets to raise cash to meet margin calls—demands from brokers that they produce cash to cover the reduced market value of their positions.

After markets closed Monday, CME Group Inc., which operates the Comex gold market, increased the sums investors must pledge in order to trade gold futures. Exchange operators often raise so-called margin requirements at times of large market swings.

Flows out of the fund are likely to have been even higher Monday, traders said, after volume in the SPDR fund surged to an all-time high. Gold-backed ETFs can accelerate price declines in the metal as investors cash out, releasing physical gold into the market.

"I think what's happened is that gold, in the way it's traded, has transitioned," said Edward Lashinski, director of strategy and trading for the futures group at RBC Capital Markets. "It transitioned from a store of value into what now appears to be a bubble based on expectations of central-bank liquidity measures."

Gold's capitulation has been months in the making. The price hit a recent high in October and has been in decline since.

Over the past six years, central banks in the U.S. and Europe have printed extraordinary amounts of their currencies in an effort to resuscitate the world economy. Every new round of "quantitative easing," as it has been dubbed, was accompanied by loud warnings that the inevitable result of this easy money would be a surge of inflation.

That in turn, helped fuel a 116% increase since 2007 in the price of gold, the classic hedge against inflation, because its value tends to increase as the dollar weakens. Gold's performance stood out against sharp drops over that period in the value of U.S. stocks and houses.

Gold bugs proliferated. Steve Forbes, the onetime Republican presidential candidate, predicted in 2011 that loss of confidence in paper currency would force the U.S. to return to the gold standard after the 2012 election. Peter Hambro, chairman of London-listed Petropvlovsk PLC, which mines gold in Russia, was cited in a British newspaper as saying that a big U.S. bank sent a text message to him in the summer of 2011 saying that, if the Fed unleashed a third-round of money-printing and bond-buying (as it later did), gold prices would hit $5,000 an ounce.
The collapse of gold is provoking a chorus of "I told you so" from those long skeptical that the rise in the metal's price was a harbinger of inflation.

The recent drop in gold prices coincides with weakness in the prices of other commodities. That is seen by some as a signal the world economy—and China's, in particular—may be slowing.

Prices of energy, metals and other commodities are exquisitely sensitive to changes in demand, and thus are an important gauge of the pace of industrial activity around the world. Commodity prices fell sharply during the recession, rebounded for time, peaked in the spring of 2011, fell for about a year, and then turned up again in mid-2012.

Now, they seem to be back on the downward trend.

"We continue to see a slide in global commodity prices," economists at J.P. Morgan Chase & Co. told clients. "To the extent that the move reflects weakening demand, the signal is of decelerating global factory output."

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