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Germans lead gold rush frenzy

By Jack Farchy in London
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At the Rand refinery in South Africa, the phone has not stopped ringing this week.

Panicking German dealers and banks have been desperate to get their hands on krugerrands, the world's most popular gold coin.

"We have some extraordinary sales to German customers," says Deborah Thomson, the Rand treasurer. The refinery, which usually sells 2,000 coins to each customer at a time, says that last week it received an order from one German bank for 30,000 coins. Another bank requested 15,000 coins.

Frank Ziegler, head of precious metals at BayernLB, one of Germany's largest wholesale suppliers of gold, says: "People are buying krugerrands like crazy." The frenzy pushed gold prices to a nominal high of $1,248.95 a troy ounce yesterday while the euro price surged through €1,000 an ounce for the first time. Adjusted for inflation, however, gold prices are still a long way from their all-time high above $2,300 an ounce in 1980.

Although coins account for a small part of the market, they are one of the best indicators of investor sentiment towards the precious metal. And right now gold is in massive demand from investors who see it as the ultimate safe haven at a time of market turmoil and as one of the best hedges against a possible resurgence of inflation.

Other important factors are supporting prices: institutional investors are pouring billions into bullion-backed exchange traded funds; central banks have reversed 20 years of selling gold (and some, including the Chinese central bank, are buying it); and mine gold supply growth has stagnated.

Not all the factors are positive. India, the world's largest gold buyer and traditionally the best barometer of gold demand, is signalling that the rally could be near a peak. Ahead of the Akshaya Tritiya festival this weekend, when Hindus traditionally buy gold and gold jewellery for good luck, Mumbai dealers say customers are in short supply.

"Price makes a big difference," says Rajendra Gurjar, who runs a shop on Mumbai's wealthy Colaba Causeway. "We won't see many people coming in while prices are at these levels." Instead, Indians are buying cheaper silver.

Without the support of the traditional backbone of the gold market, some analysts believe bullion prices will soon fall.

But there is no indication that Germans are ready to stop buying. Panicked by the possible inflationary implications of this week's €750bn eurozone bail-out, they have been snapping up gold coins and small bars at a faster rate than in the aftermath of the Lehman Brothers bankruptcy.

The European Central Bank says its government bond purchases will be "sterilised" by operations to remove inflation risks. But Martin Siegel, manager of Westgold, a dealer of gold in Frankfurt, says people "are not as dumb as economists. They believe there is going to be inflation and are buying gold to protect themselves"."

German investors are notoriously wary about inflation. While few are old enough to remember the hyperinflation that wrecked Germany during the Weimar Republic in the 1920s, the episode remains etched into the national psyche: newsreel from the period has been running on the news in recent days.

The appetite for coins has been so intense that shortages are developing. "In the European market there is a shortage of krugerrands," says Mr Ziegler. As a result, the premium paid for krugerrands in the secondary market has risen from about 2 per cent to 6-8 per cent.

The interest has not been confined to coins and bars. ETFs, which hold physical gold and issue shares to investors, have also seen large inflows.

The world's largest, the SPDR Gold Trust, has increased its holdings by 50.5 tonnes in the past two weeks, more than in the first four months of the year.

Other funds have also been building their positions. Gijsbert Groenewegen, at Silver Arrow Capital, a New York-based precious metals hedge fund, says investors have been flooding into his fund "in swarms" in the past week.

Analysts and traders believe gold could rise even higher in the short term.

Philip Klapwijk, executive chairman of GFMS, the precious metals consultancy, believes that the current upward trend "could run a bit". Edel Tully, precious metals analyst at UBS, forecasts the gold price will hit $1,300 an ounce in the next month.

One bullish factor is the lack of physical gold, or scrap, being sold, despite the high prices. In Asia, where the gold market is especially sensitive to price, a surge in prices usually leads people to sell their old gold for scrap, boosting supply.

But that is not really happening yet. Afshin Nabavi, head of trading and physical sales at MKS Finance, a gold refining and trading company in Geneva, says: "Sales of scrap have picked up but not that much."

Additional reporting by James Wilson in Frankfurt, James Fontanella-Khan in Mumbai and Javier Blas in London