



## Dow-Gold Ratio: Losing Its Shine?

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Risk Watchdog has always had a keen interest in relative value plays. One such view has been the multi-year compression in the Dow-Gold ratio (that is the Dow Jones divided by the price of spot Gold). Back in April 2006, I thought that gold would continue outperforming the Dow Jones, a trend that had started in late 2000. When I first thought of this, the ratio was trading around 20.7x and were targeting a move lower in gold's favour. I even chased the theme up again in this space in late November last year.

Fast forward to today, and the ratio is trading at a level of 10.3x as gold moved higher in 2007 and 2008 and the Dow Jones collapsed over the same period. This suggests that the decade-long trend remains firmly in place, and unless the ratio breaks out of the downtrend, gold will continue to outperform the Dow.

### The Short-Term View

However, regular readers of BMI's online service will know that I called a short-term reversal of this trend in late February, when the ratio was trading at 7.1x. I highlighted the potential for a move up in the Dow's favour first to 8.7x, and then to a level of 10.0x. This also coincided with a return of risk appetite to markets, which saw the Dow rally almost 50% since its March lows. Meanwhile, gold traded mostly sideways.

The question on my mind however, is whether the Dow-Gold ratio can break out of the long term downtrend. Unfortunately, I am a dog, not a clairvoyant, so I cannot answer this question. That said, any move above two-year trendline resistance around 10.5x would be a positive signal, and would suggest a move to multi-year resistance around the 13.0x area. Only a break of this level would be reason to believe that the downtrend would be over.