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This gold price fall is a bad omen

Speculation on the cause is rife but one thing is certain – gold's special place in finance means there will be repercussions

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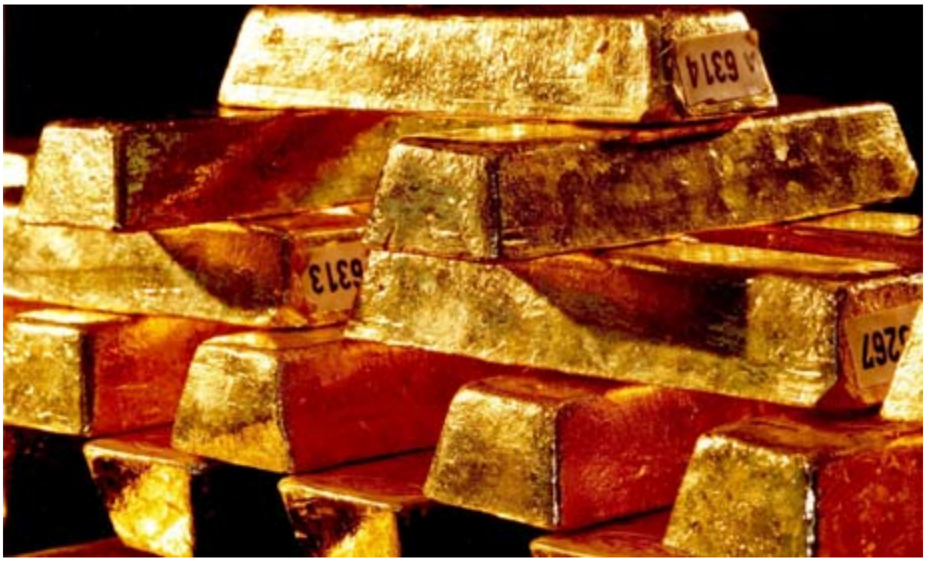

'The gold bugs – who think gold provides a more real basis of value than currencies created at the flick of a switch – see the price fall as an opportunity to buy gold more cheaply.' Photograph: EPA

After years of attracting strong demand from fearful investors, a crash in gold prices on Monday caught the financial world on the hop.

In London the price was officially "fixed" at $1,395 per troy ounce, down 9.2% from Friday. Eight hours later on the New York market, the price for immediate delivery was down 9.1% from Friday at $1,365 an ounce. Most other commodity prices fell in gold's wake. By Monday evening Brent oil fell below $100 a barrel for the first time since July 2012.

The sudden collapse of gold left brokers and bloggers scratching their heads for explanations. Whatever the cause, it must be big to have such an impact. And gold's special place in finance means there will be repercussions.

This is another marker of the fragility of financial markets, as the chosen strategy of quantitative easing fails to revive the real economy. It serves to remind us that the world economic crisis is far from over, just as the Cyprus bailout did for the eurozone. There has already been a steady decline since 2011 in commodity prices, in which eight years of "supercycle" have surely ended. As commodities are physically traded products, they are a better indicator of the real state of the economy than this year's stock market bubble.

Speculation on the cause of the gold rout is rife. It seems to have started in a big placing of "short sale" orders in New York on Friday – said to be either 400 or 500 tonnes, depending on the source. This is not actual gold but contracts for future sale. Nevertheless it is a huge amount, each tonne worth around $45m on Friday morning.

Who did it? Paul Craig Roberts, former US assistant treasury secretary, asserted it was a "concerted effort" by the Federal Reserve to "scare people away from gold and silver by driving down their prices" and get them to buy dollars instead. A more prosaic explanation was that a hedge fund wanted to force prices down.

Alternatively, Italy's central bank was selling, prompted by Cyprus's decision to sell 10 tonnes of gold reserves after the bailout. Among Asian brokers it was linked with Japan's recent decision to embark on its own form of quantitative easing.

There had been warnings in the air. Before Monday's sell-off, gold prices fell 13% this year, and its sister metal silver by 20%. Last week influential banks including Goldman Sachs recommended investors to sell – also a co-ordinated move by the Fed, in Roberts' view.

Meanwhile, the Bitcoin virtual currency's price rose 10 times to $130 from the start of the year – another sign of investors' reluctance to hold conventional currency assets.

The gold bugs – who think gold provides a more real basis of value than currencies created at the flick of a switch – see the price fall as an opportunity to buy gold more cheaply. They have suspected many official conspiracies to force prices down during the metal's meteoric rise from $260 per ounce 12 years ago to $1,747 in October 2012. By March 2013 the London price fell back to a monthly average of $1,593.

However, it is salutary to recall the last big boom and crash in gold and silver prices. It immediately preceded the commodity price collapse and recession of the early 1980s.

Although history does not repeat itself, the financial and real economies are more connected than they seem. Then too there was a big global debt overhang and the Fed was desperate to retain confidence in the dollar. There are good reasons to think this gold price fall could also presage worse to come.