The Three Phases of a Gold Bull Market

RICHARD RUSSELL DESCRIBES THE THREE PHASES OF A GOLD BULL MARKET AND NOTES HOW THIS BULL MARKET IS DIFFERENT BECAUSE THE U.S. DOLLAR IS COLLAPSING.

Richard Russell on bull markets

Richard Russell has been editing his Dow Theory Letters since 1958 and brings great wisdom to the markets. Here are his thoughts on bull markets and the ongoing gold and silver bull market from his March 13, 2007 Remarks, which come with a subscription to Russell’s Dow Theory Letters, $250 a year.

Russell deals primarily with the stock market, but he became a gold bull in 2000, the timing of which illustrates Russell's insight into the precious metals markets. He was also a gold bull in 1970s. For more about Russell’s Dow Theory Letters, visit www.dowtheoryletters.com.

There are four kinds of gold or non-gold people (1) They know nothing about gold and never even think to ask. (2) They know a little about gold, but can't afford to buy any. (3) They trade small amounts of gold, but as soon as gold moves up or down 5 dollars or more, they sell it or are stopped out. (4) the so-called "gold bugs," the small minority who understand gold and money and adhere to a policy of accumulating gold.

I'm in category number 4. But let me give you my reasons.

The great majority of investors don't understand bull markets or the concept of the primary trend. When the primary trend of an item turns up -- whether it be stocks, commodities, agriculturals, precious metals -- we call that a bull market. There are small, medium and large bull markets. Once the primary trend of a category turns bullish, there's no way of knowing beforehand, how big the coming bull market is fated to be -- nor exactly what path the bull market will take.

We do know that in major bull markets there are psychological or sentiment phases. The first phase of a bull market is the accumulation phase. This is the early phase where informed investors accumulate an item because they know the item is underpriced or that the item is underused or simply not understood.

The second phase of a bull market, usually the longest phase, sees the professionals, the funds, the big money, the smartest of the public, taking positions in the item. The second phase tends to be characterized by many reactions, corrections, adverse news events that cause the public to dump the item.

The third phase of a bull market is the speculative phase, Here we see rising volume, the wholesale entrance of the public, accompanied by news and endless hype by the Wall Street "experts." People who wouldn't touch the item during the first and second phases, are now enthusiastic buyers. The third phase sees systematic distribution by the early first phase buyers. Third phase buying can easily turn to hysteria and madness. Towards the end of the third phase, we see hints of the beginning of the next primary bear market.

Question -- Do all bull markets progress as described above?

Answer -- Almost all major bull markets do. It's a judgment as to whether an ongoing bull market is fated to become a major bull market or not. There's no definitive answer to that question.

Now I want to talk about the current bull market in gold. This is a bull market that began in August 1999 with gold priced at 252 an ounce. Gold is the most emotional of all items -- loved by much of mankind, hated by certain elements including governments and central banks. Because gold is real money, and because gold is collected, traded and accumulated by millions of people the world over, gold bull markets tend to be BIG bull markets.

The gold bull market that started in 1999 has already taken gold up 291% to a high of 734 recorded in May of 2006. But what's so interesting about the ongoing gold bull market is that neither the public nor the funds have entered the picture. In fact, most people really have no idea that gold is in a primary bull market, this despite that fact that since 1999 gold has consistently outperformed the Dow and the S&P.

I believe that the gold bull market is now in its very early second phase. Informed investors have already established healthy positions in gold. I think that a very minor sector of the investing public has now taken some kind of a position either in gold or gold stocks or a gold ETF or a gold fund. Nevertheless, it's still unusual today to find an individual who has any kind of a position in gold.

Gold has been in a corrective phase ever its May high of last year. This backing-and-filling has served to discourage many Johnny-come-lately and in-and-out traders. Meanwhile, gold remains in what I consider its "bargain phase" below 734. But what about the future?

This is important. Almost all BIG bull markets (and I believe gold is in one) ultimately move into a third speculative phase. I believe this phase lies ahead for gold, maybe a year or so, maybe three, four or five years out. It doesn't matter -- in my opinion, the longer the time elapsed prior to the entrance of the third phase, the bigger the third phase for gold is fated to be. But before entering the third phase, we have to complete the second phase. The second phase, from the looks of it, may has quite a while to go before it is completed. Question -- how many of your friends own any gold?

My thinking is that when gold finally moves into its third phase, we may see one of the most speculative third phases in history. I believe we will see gold in the thousands of dollars. I believe we will see one of the most emotional bull market third phases in history. People will look back on the year 2007 and wonder what the world was thinking about with gold selling for $650 US dollars, dollars that were created out of thin air, fiat dollars which could be created by central banks in any quantity in at any time.

At any rate, that's the way I see this sluggish, unexciting, slowly-moving gold bull market here in 2007. I lived through and profited during the gold bull market of the 1970's. That bull market was based on inflation fears. This bull market when it moves into its third phase will be based on fear of the viability of the dollar and all fiat money. This bull market is fated to be much bigger than the bull market of the 1970's.