CAIRNS WEALTH MANAGEMENT

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Macro Memo

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Has Gold Lost Its Luster?

Recent Price Action

Just two and a half years ago gold began an eye-catching move, breaking through previous price resistance at $2000 per ounce. In January of this year, it surged to more than $5500 before retreating to roughly $4000. Such dramatic moves, both higher and lower, naturally raise questions. Has gold lost its appeal as an investment? Does the recent decline signal that the long-term rise in hard assets is coming to an end? Or is there a deeper explanation behind gold's recent weakness? We address these questions in this month's Macro Memo.

Some Background Information

If we are to understand the reasons behind both gold's rise in price over the last three years as well as its more recent pullback, we should understand gold's relationship to fiat currencies, and more specifically its relationship to the dollar.

Historically, gold has served as a hedge against inflation. Currency debasement is not a new phenomenon; it goes back to at least the Roman Empire. A well-documented example occurred in the1st century AD under Emperor Nero.[1] The silver denarius, which was originally nearly pure silver, was steadily diluted with copper and bronze to finance military campaigns and lavish state projects (doesn't that sound familiar?). By the 3rd century AD, the denarius contained less than 5% silver and was essentially a bronze disc with a thin silver wash.

The same phenomenon continues today, via persistent federal deficits. "Printing" new money to cover the excess spending has the same effect as diluting the silver of the Roman denarius. The mechanics differ, but the result is the same: each unit of currency buys less over time. Over the centuries, investors have protected the purchasing power of their wealth by owning real, physical assets that the government can't unilaterally dilute, like gold. The more a currency is debased, the more currency it takes to purchase the same ounce of gold.

Another reason gold moved higher was the expectation for lower interest rates. Physical gold does not pay interest, so when interest rates are low, especially when they are lower than inflation (negative real rates) gold is a more attractive asset to own. However, when interest rates are higher, and real rates are positive, gold becomes less attractive and is often sold and replaced by higher yielding investments.

Since the Global Financial Crisis (GFC) in 2008, and increasingly since 2022, foreign central banks have moved towards holding more of their foreign exchange reserves (savings) in gold and less of them in dollars. But why? The answer, we believe, is that the United States has broken a commitment.

Since the mid-1970s, the "petrodollar" arrangement has placed the U.S. dollar at the center of global oil and commodity trade. The petrodollar agreement was an agreement to price and to sell all oil in U.S. dollars. Because oil is the "master commodity" (nothing happens without energy) countries, in turn, always needed dollars. This made the dollar the **global reserve currency**; it was needed by virtually all countries to buy essential economic inputs. By default, the US Treasury Bond became the **global reserve asset** (savings vehicle) because it was essentially the dollars those countries would need to buy commodities, but with an interest rate.

However, as it was replacing the gold standard, the petrodollar agreement hinged on a key promise: the United States would keep the dollar "as good as gold for oil." Otherwise, if this promise were not upheld, the United States would have the singular ability to inflate away (debase) the savings of other foreign countries. Fed Chairman Paul Volker honored the "good as gold for oil" commitment in the late 70s and early 80s by increasing interest rates substantially to defend the value of the dollar. But when hard times rolled around again with the GFC, the US failed this commitment and went down the path of extraordinary monetary policy, which debased the value of the dollar. As a result, foreign Central Banks have since sought out a reserve asset which holds its value relative to the debasing dollar; as the chart below shows,[2] they chose gold, the asset they held prior to the petrodollar. This choice echoed a famous quote of J.P. Morgan in a 1912 Congressional testimony, "Gold is Money. Everything else is credit.[3]"

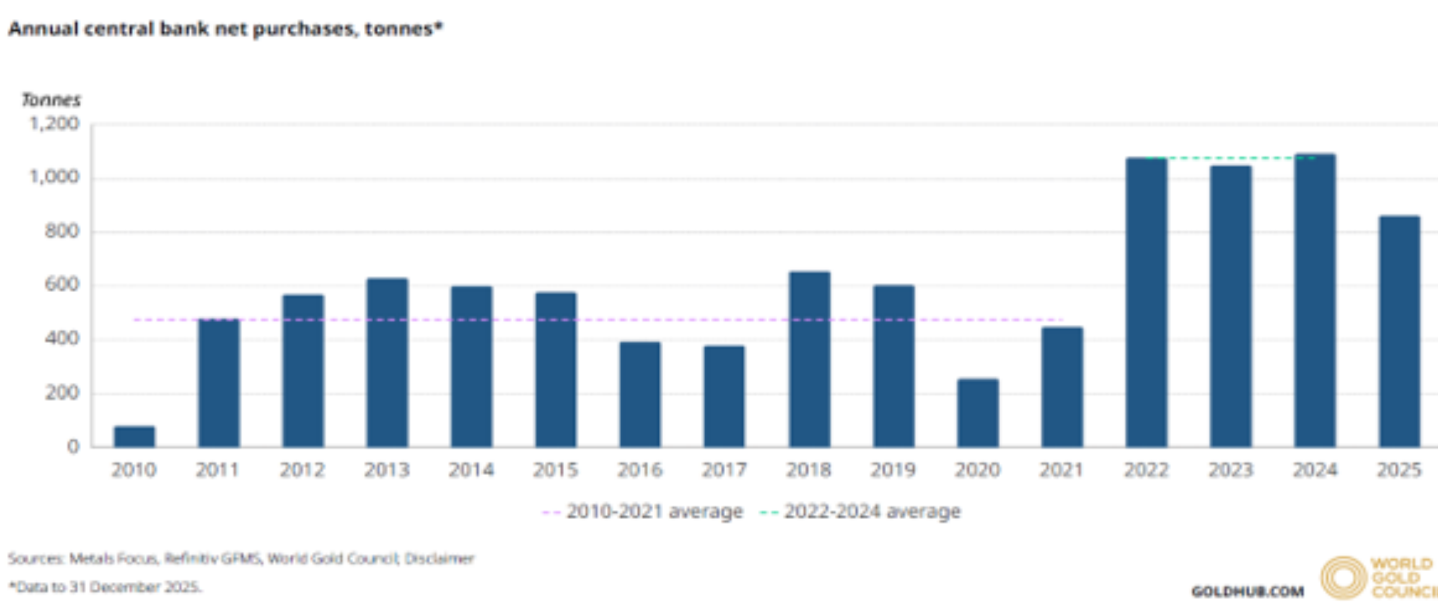
The conversion of their reserve assets from US dollars to gold accelerated in 2022 after the US seized Russian foreign reserves in response to their invasion of Ukraine. Foreign governments realized the US could do the same to them if they ever ran afoul with US policy and therefore sought a savings vehicle with no counterparty risk.

Other factors contributing to the increase in gold's price included momentum driven investment flows from speculators and gold's role as a hedge, or safe-haven investment, from global conflicts, trade disputes, and currency instability.

So, What Happened?

Central Banks Used Reserves

A major contributor to the recent pullback in gold prices is the closure of the Strait of Hormuz. Once the strait was closed, oil prices skyrocketed to well over $100 per barrel. They currently remain more than



40% higher than they were in the 4th quarter of 2025. As mentioned earlier, globally oil trades primarily in dollars. Therefore, oil importing nations must obtain additional dollars to satisfy their energy needs.

The logical source for those additional dollars would be to sell US Treasury bonds. However, as also mentioned earlier, foreign central banks have been reducing their holdings of Treasuries. When those holdings are depleted, the next most likely asset to sell is gold. Gold is highly liquid and also trades globally in US dollars.

Turkey is an excellent example of this. In March of this year, immediately following the beginning of US/Iranian hostilities, Turkey sold nearly 90% of its US Treasury holdings for roughly $14 billion.[4] To satisfy the remainder of its need for dollars Turkey sold or pledged approximately 58 tons of gold, worth roughly $8 billion.[5]

They are not making a strategic shift away from gold, the country still owns over $120 billion of it.[6] Rather, Turkey is making use of its savings in times of financial stress. We often refer to our personal savings as our "rainy day fund". Well, for much of the global economy, especially emerging market countries who import most of their energy[7], closure of the Strait of Hormuz counts as a rainy day.

Gold is not failing as a reserve asset; instead, it's acting like one.

Interest Rates Moved Higher

The day before hostilities began with Iran, the US ten-year Treasury yield was 4%. In response to the spike in oil prices, at the time of this writing it is over 4.6%. This increase in yields creates more competition for investment dollars from gold, which pays no current yield.

Retreat of Momentum Speculators

Momentum speculators are trend followers. They care far less about what asset is trending than they do over the fact that, whatever that asset happens to be, it is trending. Once that trend breaks, the speculators move on to another asset that is trending. The retreat of these speculators is evident in the net flows of dollars in and out of gold ETFs. After experiencing very strong inflows of new money in the second half of 2025, gold ETF flows turned decisively negative in the first half of 2026, resulting in the weakest first half since 2013.[8]

What Now?

The combination of these factors created the environment for gold prices to pull back, but the question now is, does gold still make sense as an asset for investors? We believe that it does.

This memo began by discussing factors that supported gold's move above $5500/ounce. Inflation via monetary debasement, expectations for lower interest rates, central bank demand, momentum driven speculation, and geopolitical uncertainty are all still trends supporting the potential for gold to move meaningfully higher.

- According to the Congressional Budget Office (CBO), the US will continue to debase the dollar via structural fiscal deficits for at least the next ten years.[9] This is bullish for gold prices.

- For every energy importing emerging market country forced to use their gold reserves to raise dollar liquidity, there were multiple central banks eager to buy them. We expect the need for these emerging markets to utilize their gold reserves to abate in coming months. As their trade balances return to positive territory, we believe they will once again be buyers of gold as their preferred reserve asset.

- Once gold begins to demonstrate price recovery, momentum driven speculators are very likely to return.

- As for geopolitical uncertainty, it's hard to believe the world is moving toward unified peace. We believe gold will remain a hedge against conflicts and disputes.

Gold has stood the test of time as a reliable store of value for investors. But the last few months have shown that it is not risk-free; it can be volatile. Your investment objectives and time frame will determine how gold may fit into your investment plans, and to what extent it might. If you would like some guidance through the thought process, we would welcome the conversation.

[1] https://www.investopedia.com/terms/d/debasement.asp

[2] Sources: Metals Focus, Refinitiv GFMS, World Gold Council. Retrieved from: www.gold.org/goldhub/research/gold-demand-trends/gold-demand-trends-full-year-2025/central-banks [Online Resource]

[3] https://www.investmentoffice.com/Observations/Macro_Observations/Gold_Is_Money_Everything_Else_Is_credit.html

[4] https://news.metal.com/newscontent/104013906-why-countriesare-selling-their-gold-%E2%80%93-and-whats-really-behind-it

[5] ibid.

[6] ibid.

[7] This group includes India, Indonesia, Thailand, the Philippines, Egypt, Pakistan, Vietnam, and South Africa

[8] https://www.gold.org/goldhub/data/gold-etfs-holdings-and-flows

[9] https://www.cbo.gov/publication/62105

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