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INTERVIEW: Midas' Winmill: U.S. Fiscal Issues, Negative Rates To Propel Gold Higher Again

By Allen Sykora of Kitco News
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Tom Winmill

(Kitco News**) -** The veteran portfolio manager of a gold mutual fund looks for the precious metal to recover this year on worries about U.S. government spending and continued negative real interest rates.

Tom Winmill, president and chief executive officer of Midas Funds, said he sees potential for gold to return to $1,900 an ounce by year-end. Winmill is the portfolio manager for the Midas Fund (MIDSX) and Midas Perpetual Portfolio (MPERX).

Gold has slid so far this year, with many investors feeling more comfortable about the economy and willing to turn to so-called risk assets, including the broader equity market, with the Dow Jones Industrial Average repeatedly hitting record highs in recent sessions. Further, this is a period of slower seasonal demand for gold jewelry, before this picks up in the second half of the summer, Winmill explained.

Nevertheless, he continued, if gold were to fall back toward $1,500 an ounce, he suspects that fabricators will be replenishing supplies in anticipation of the normal pick-up for jewelry demand in the third quarter.

Meanwhile, for the longer term, he said there are still monetary and fiscal issues in the world's largest economy – the U.S. – that are likely to underpin gold. "Those are the biggest inescapable factors going forward," Winmill said.

Massive deficit spending is continuing despite worries about the automatic spending cuts referred to as sequestration, he said. Meanwhile, interest rates remain negative, meaning the yield is below the rate of inflation.

There have been some worries among hard-asset investors about when the Federal Reserve might begin to peel back its ultra-loose monetary policy. The Federal Open Market Committee's statement after the January meeting said rates would remain "exceptionally low" as long as unemployment remains above 6.5% and inflation below 2.5%. The jobless rate in February fell to 7.7%.

"We don't see that the growth in the U.S. economy is going to lead to substantially lower unemployment," Winmill said, also commenting that a stronger dollar may help limit any inflationary pressures.

"We think the monetary side is probably going to stay about where it is, with the factor of negative real interest rates," he said. "That typically favors hard assets. So on the longer term, we're bullish."

He suggested there is increasing risk in historically high equity markets and ultimately there could be some disappointment, meaning investors may turn back to gold. "This is a great time, we think, to pick up gold and mining equities."

Winmill described current policies of the U.S. as "inherently unstable" with some sort of resolution necessary.

Until then, "we think investors of whatever stripe should consider owning some kind of gold in their portfolio for liquidity and as insurance," Winmill said. Yet, the metal also does not provide a return other than rises in price. So at the same time, he cautions against being heavily overweight in gold.

Uncertainties such as those surrounding the U.S. are among the factors that are leading many central banks to increase their gold holdings, particularly those in emerging-market nations, Winmill later added.

"My feeling is if the sequestration is lifted and it's business as usual to spend money and incur deficits…we're going to see a lack of confidence in the dollar and more central banks trying to add gold as a percentage of their reserves," Winmill said. "That is going to be very, very bullish for the gold price."

Midas Looks At People, Projects And Pricing When Picking Stocks

Investors who favor gold may want to consider holding mining shares as well, since historically they have tended to move more than the metal itself, Winmill said. To choose mining shares, Midas uses what he terms the "three P's" – people, projects and pricing.

As for people, "you want to find management teams that have experience and shown success -- in either that company or prior companies – who are good stewards of shareholders' money and that they respect the notion of not just returning capital but getting preferably double-digit returns on capital," he said. He advised investors to look for management teams with discipline and who would not touch deposits unless they are convinced they would be profitable.

Meanwhile, investors must also carefully scrutinize projects, since most deposits probably are not financially attractive, he said. “There are some great deposits out there, and those should be focused on,” Winmill said. But, he conceded, these are difficult to find. He favors looking for those in politically safe jurisdictions and prefers to stay away from those that require the cutting edge of technology for extraction.

“We try to stay in the middle of the fairway and compromise toward the safer side,” he said. “In the gold-mining business, I’d rather have a longer payout in a safer jurisdiction that may have a lower margin of return than the opposite, where there are more risks and any one of those varied risks could lead to a negative situation.”

These potential risks could be political, extraction-related or geologic, including potential for tremors, and strikes. “Be a little bit on the defensive side,” Winmill said.

Pricing refers to attempting to find stocks that appear to offer the greatest value.

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