

THE RUSSIA-UKRAINE CONFLICT & THE POTENTIAL IMPACT ON GOLD

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At the time of writing, many [commodity](#) prices are rallying on the news. Oil, natural gas, wheat, corn, palladium, aluminum and nickel are all trading higher, including gold. While other commodities have rallied in the past year, gold has been sitting in the shadows. Gold is often thought of as a geopolitical hedge instrument.

Geopolitical risk is an inherently difficult thing to quantify. Quantifying the relationship between an asset price and geopolitical risks is even more difficult. Looking back at periods when there has been a perception of elevated geopolitical events, it is hard to say that asset prices have behaved in a consistent manner. Any positive or negative price movement needs to be viewed in the context of broader economic activity at the time.

Nevertheless, we can point to some geopolitical case studies that have shown a very strong positive reaction from gold. The table below gives four examples where gold has significantly outperformed equities in the aftermath of a geopolitical shock.

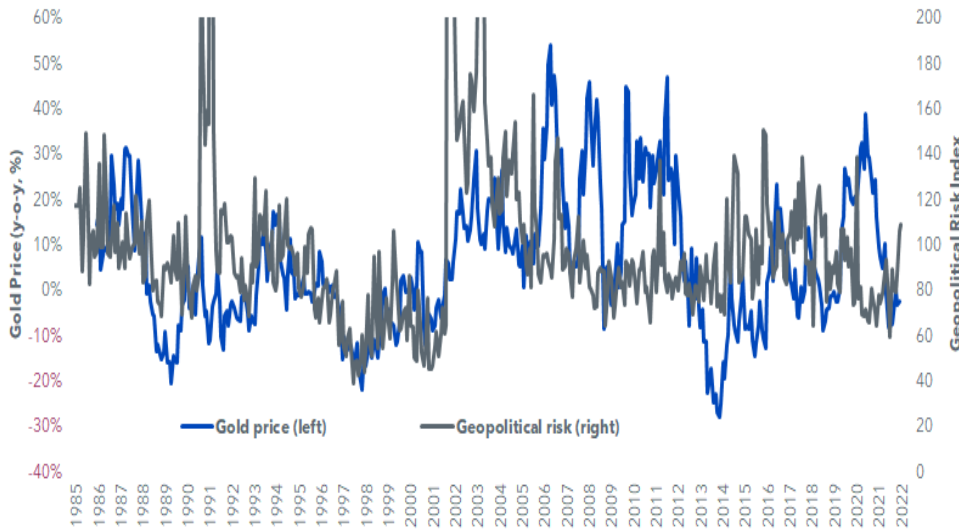
	Event Date	1-Yr Forward Gold Price Change	1-Yr Forward Equity Price Change	Relative Gold Outperformance
Yom Kippur War	6-Oct-73	47.40%	-42.00%	89.40%
Nixon's Resignation	9-Aug-74	14.90%	4.40%	10.50%
9/11 Terrorist Attack	11-Sep-01	16.90%	-15.10%	32.00%
Paris Bombings	13-Nov-05	33.50%	17.60%	15.90%

Sources: WisdomTree, Bloomberg. Gold is based on Bloomberg spot prices and equities is based on the S&P 500 Index. S&P 500 Index: market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the U.S. economy. Past performance is not indicative of future results. You cannot invest directly in an index.

Notwithstanding the difficulty in quantifying geopolitical risk, we use the Geopolitical Risk Index developed by the [Federal Reserve](#) Board's Dario Caldara and Matteo Iacoviello, which is based on automated text-search results of the electronic archives of 10 newspapers. Plotting their series against gold yields some interesting results.

- Immediately before the buildup to the Gulf War (1990), gold prices were quite depressed. It seems the buildup ignited gold prices.
- Immediately before the 9/11 terrorist attacks in the U.S. (2001), gold was depressed. The attacks seem to have ignited gold prices. The Iraqi war soon after (2002) kept gold well supported.

Gold and Geopolitical Risks



Sources: WisdomTree, Bloomberg, Economic Policy Uncertainty (Geopolitical Risk Index by Dario Caldara and Matteo Iacoviello), January 1985 to January 2022. Scale on right axis capped at 200 to allow for better visualization of the gold trend.

We believe most people would agree that gold price behavior in 2021 was disappointing, with the backdrop an elevated level of [inflation](#). Our models indicate that gold should have been trading close to \$2,500/oz in January 2022 when inflation in the U.S. was running at 7.5%.¹

Could the beginning of a war in Ukraine act as a catalyst for gold in a similar way to the noted events in 1990 and 2001?

¹ Other relevant inputs to our model for this January gold price calculation include: [dollar basket \(DXY\)](#) at 96.5, U.S. [10-year Treasury yields](#) at 1.78%, net speculative positioning on gold futures contracts at 245,782 (source: Bloomberg, 31/01/22)

Important Risks Related to this Article

Nitesh Shah is an employee of wisdomTree UK Limited, a European subsidiary of wisdomTree Asset Management Inc.'s parent company, wisdomTree Investments, Inc.

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DEFINITIONS

Commodity: A raw material or primary agricultural product that can be bought and sold.

Federal Reserve: The Federal Reserve System is the central banking system of the United States.

Inflation: Characterized by rising price levels.

DXY Index: Weighted geometric mean of the dollar's value compared only with basket of 6 other major currencies, Euro, Japanese Yen, Pound Sterling, Canadian Dollar, Swedish Krona, and Swiss Franc.

10- Year Treasury: a debt obligation of the U.S. government with an original maturity of ten years.