Wg Weekly Gold Commentary 2013

Rand Refinery (Pty) Ltd, Refinery Road, Industries West, Germiston, 1401, South Africa
P.O. Box 565, Germiston, 1400, South Africa, Tel: +27 (0) 11 418 9000
Fax: +27 (0) 11 418 9231 www.randrefinery.com Email: gold@gold.co.za

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MAIN TOPICS

- Gold prices trade at five year lows.
- US Fed offers little news on a rate hike.
- The Greek debt crisis continues.
- Demand for physical gold soars.

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Gold prices managed to recover slightly on Friday as the dollar fell after the release of weaker-than-expected U.S. data. However, prices remained on course for their biggest monthly decline in more than two years.

Gold prices remain under pressure.

After breaking below the key psychological support level of $1140 an ounce, the price of gold has found some support at around $1190 an ounce. But, investor sentiment towards gold remains largely negative as market participants believe that the Federal Reserve will soon raise interest rates.

Investor confidence in gold was shaken last week when bullion prices tumbled to a 5-1/2-year low of $1,077 on July 24 mainly on the back of selling pressure from record futures shorting. The metal has lost 6.4% so far this month, its steepest decline since June 2013.

The prevailing general consensus on gold is overwhelmingly bearish, with virtually everyone convinced it is headed lower. And, once again the narrative being used is that gold yields nothing, thus it is not worth owning. Also, the belief that higher interest rates will be bearish for gold prices seems to have permeated main stream media.

The Federal Open Market Committee (FOMC) concluded another policy meeting last week. Its latest statement on monetary policy did not offer much guidance to investors on when to expect the much anticipated “rate hike.”

As widely expected, the U.S. central bank's Open Market Committee kept its key funds rate near zero. There had been some anticipation the FOMC would provide at least few code words indicating that it was ready to move, but in the post-meeting statement, there was no mention of the timing of such a move.

Some analysts expect the Fed to raise rates in September, while others are anticipating the announcement in December.

The Fed characterized economic growth as moderate but said inflation indicators "remain low." The committee noted that "business fixed investment and net exports stayed soft." However, the FOMC characterized job gains as "solid," something the market interpreted as perhaps hawkish for the future of rate hikes and keeping September in play for a move.

The Fed is under great pressure to raise rates. Doing so would be a confirmation that its policies have solved the current economic problems. Prolonged low rates are dangerous. They distort markets, build bubbles, and tend to spawn harmful inflation. So Fed chief Janet Yellen and her group of policy makers want to hike rates.

At the same time, by them procrastinating, illustrates the concerns the Fed has about current economic uncertainties that remain, from Greece and China to America’s own struggling recovery.

The Fed had not raised interest rates in more than nine years and had been keeping its key funds rate near zero since late 2008, in an effort to stimulate growth into an economy suffocated during the financial crisis and the accompanying Great Recession.

In addition to keeping rates low, it had instituted three rounds of quantitative easing. Since late 2008, the Fed has expanded the monetary base approximately five-fold. It has gone from just over $800 billion to $4 trillion. This is unprecedented in the Fed's 100-year history. It has also been the main driving force that pushed S&P 500 upwards by around 210%.

While it is difficult to predict when the Fed will raise rates from near-zero levels, when it does, the move will see a gradual rise, which should cap moves across stock, bond and currency markets. But, big prices swings are still likely as investors track economic data to position themselves for a September, December or even 2016 rate increase.

On Friday, moments after the release of the U.S. employment-cost index, a measure of workers' wages and benefits also known as ECI, the dollar sank as much as 1.7% against the euro before paring most of the losses later in the day.

Despite Friday's selloff, the dollar rose 1.4% against the euro for the month of July.

Even though the financial crisis in Greece has not been resolved and while the story has faded from news media the saga continues. Recently the International Monetary Fund (IMF) stated that Greece's high debt levels and poor record of implementing reforms disqualify the country from a third IMF bailout of the country, raising new questions over whether the fund will join the EU's latest financial rescue.

The determination, presented by IMF staff at a two-hour board meeting on Wednesday, means that while IMF staff will participate in bailout negotiations currently under way in Athens, the fund will not decide whether to agree a new programme for months — potentially into next year.

That delay could have significant repercussions, particularly in Germany, where officials have long said it would be impossible to win Bundestag approval for the new 86 billion euro bailout without the IMF on board.

Demand for physical gold surges.

While, the bullion banks persist with their frequent bear raids on the gold price, the current lower price has once again led to a surge of buying of gold coins and bars across the globe. Both the Wall Street Journal and Reuters reported on how bullion dealers have been seeing a spike in demand for gold coins and bars in India and China and indeed Europe, Australia and the U.S.

The U.S. Mint – which ran out of Silver Eagles earlier in the month due to unexpectedly high demand – has sold 170,000 ounces of Gold Eagle coins in July. This compares with a mere 21,500 ounces sold in May and 76,000 in June. It represents the highest level of monthly demand in over two years

According to the Wall Street Journal, demand during July in India surged dramatically. July is typically a quiet month for gold sales as farmers, who make up the bulk of the population, allocate their cash towards cultivation.

"Gold's plunge to five-year lows this week has prompted a swift rise in demand from jewellery retailers in China and India, the world's top consumers of gold, leading to a doubling of premiums paid on physical gold," reports the WSJ.

The article goes on to quote an Indian jeweller:

"Until now, the gold demand was very low because of the season. Demand has picked up noticeably as the common man thinks prices have bottomed out."

Meanwhile, Chinese investors have been allocating money to gold following the bursting of China's equity bubble.

Interest in gold *"had waned in recent months as investors flocked to the soaring stock market."* The surge in demand has caused a doubling in the premiums paid for gold. Demand for investment type "gold biscuits" has "shot up" this week, according to a Hong Kong based jeweller. *"Our sales are up by 20% to 30% compared to average sales in previous months."*

The Perth Mint in Australia has also seen a sharp rise in demand for gold coins. In June, sales were up 37% on the same month last year with the mint clearing 21,962 ounces.

"Sales in July already matched that level earlier this week and appear to be gaining momentum," said Ron Currie, sales and marketing director.

The Perth Mint sells coins and bars internationally and is seeing strong demand in the U.S. and EU.

With the continued uncertainty in the global financial system, investors purchased record Gold coins in July. Many individuals are becoming more concerned about the fragility of the financial system and the experience of the Greek people in not being able to access bank accounts and even cash in safety deposit boxes has been a reminder of what can happen in the banking system.

Market participants are now awaiting the next U.S employment report. The nonfarm payrolls report due on Friday is expected to show 215,000 new jobs were added in July, in line with the recent trend of strong employment growth. Some traders played down the importance of the wage report, saying that the two job reports ahead of the September Fed meeting will weigh more heavily.

Meanwhile gold at five-year lows remains a compelling investment despite all the bearish reports issued by most of the major banks including Goldman Sachs, Citibank, UBS, Morgan Stanely and HSBC.

TECHNICAL ANALYSIS

The price of gold remains oversold. For the moment it seems to be building support at around $1190/oz.

About the author: David Levenstein is an independent precious metals market commentator with more than 30 years' experience.