Wg Weekly Gold Commentary 2013

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MAIN TOPICS

- Gold prices bounce back.
- China devalues the yuan.
- Eurozone agrees on a new bailout for Greece.

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Gold prices rebounded from recent lows last week after China devalued the Yuan. The price of the yellow metal broke back above the $1,100-per-ounce level on safe-haven demand from investors concerned about China's devaluation of the yuan.

Although prices have drifted lower from the weekly high, it was a positive week for the international gold price which settled the week at $1113.70 an ounce.

China devalues its currency.

The global financial markets were rattled last week when China shocked the world last Tuesday with a surprise devaluation of its yuan currency, sending gold prices sharply higher.

Last Tuesday, the People's Bank of China (PBoC), set the mid-point reference exchange rate for the yuan against the U.S dollar at 6.2298 which was tantamount to a devaluation of around 1.9%. And, on Wednesday, China cut the yuan's value against the dollar for the second consecutive day, roiling global financial markets and driving expectations the currency could be set for further falls.

The daily reference rate that sets the value of the Chinese currency against the greenback was cut by an additional 1.62% to 6.3306 yuan, from 6.2298 on Tuesday.

The combined drop is the biggest since China set up its modern foreign exchange system in 1994, when it devalued the yuan by 33%t at a stroke.

It is also a bigger change than the 2.1% rise when China unpegged the yuan, also known as the renminbi (RMB), from the dollar in 2005.

The double move has been widely viewed as a way to boost China's exports by making them more competitive amid a collapsing stock market, rapidly decelerating economic growth, plunging exports and price deflation.

Analysts said the move could also delay an expected US hike in interest rates and even threaten a currency war as other countries come under pressure to devalue as well.

The PBoC dismissed claims that it is trying to engineer a 10% fall in the yuan as "groundless", saying in a statement the exchange rate movements were normal and "there is no base for continued depreciation". However, I doubt that this is going to be the case and I expect to see more action from the Chinese central bank. As I have always mentioned, and let me state it once again, don't trust a central bank governor or financial leader. Do you remember what happened in Switzerland?

Meanwhile, China's yuan tumbled to a four-year low against the US dollar while Malaysia's ringgit headed for the biggest drop since 1998, extending an eighth week of declines as falling oil prices and political turmoil spur capital outflows.

The ringgit dropped 2.1% to 4.0985 per dollar on Friday, extending this week's retreat to 4.2 percent.

The Turkish lira has fallen to a record low against the U.S. dollar following the breakdown of talks aimed at forming a new government while the South African Rand plunged to fresh 14-year lows against the dollar on Friday, and was at its weakest ever against the pound, hit by worries about the local economy and prospects of imminent US policy tightening.

The threat of wage strikes in the gold sector has foreign investors concerned about the on-going situation in the country. Apart from extraordinary high level of corruption in the country Africa's most developed but ailing economy, is also grappling with its worst electricity crisis since 2008. And, the unions continue with their unrelenting demands for higher wages amid an already precarious situation in the mining sector.

The rand stumbled to a session low of R12.8895 against the dollar, the weakest it has been since December 2001. It also fell to an all-time low of 20.1071 versus the pound, according to Thomson Reuter's data.

Meanwhile, the International Monetary Fund (IMF) hailed the move taken by China and issued the following statement. "The new mechanism for determining the central parity of the renminbi announced by the [People's Bank of China] appears as a welcome step as it should allow market forces to have a greater role in determining the exchange rate."

The IMF also pointed out that the latest move would not have any direct implications regarding the ongoing review of the IMF's SDR basket. But, a more market-determined exchange rate would facilitate SDR operations in case the renminbi were included in the currency basket going forward," the IMF stated.

Before China devalued its currency, the IMF issued a report suggesting that Beijing would have to wait another year before its yuan (or renminbi) currency is given world-reserve status via inclusion in the IMF's SDR basket.

The Chinese government wants the IMF to include the yuan in the basket of currencies that comprise the IMF's reserve assets that are known as special drawing rights. By doing so the yuan would be acknowledgment as an international currency together with the U.S. dollar, the euro, the Japanese yen, and the British pound.

While some analysts view the yuan devaluation as the next chapter in the current global currency war, the move was seen as largely bullish for gold. Although gold gets more expensive priced in yuan as the currency is devalued, with gold still such a culturally engrained store of value, China's citizens might turn to it anyway, especially those Chinese investors who have suffered from the stock market blowout and who are now fearful of further yuan depreciation/devaluation.

The bad news for the U.S. is that a weaker yuan means the dollar gets stronger and that will hurt the American export and manufacturing sectors even more intensely.

A strong dollar is something that the U.S, economy can't afford, and thus the yuan devaluation will now raise many questions about whether the Fed can still seriously consider raising rates this year.

Eurozone finance ministers agree on a new bailout for Greece.

After months of acrimonious debates, finally, the Eurozone finance ministers have agreed on a new bailout deal for Greece after Athens backed the plan.

European Commission President Jean-Claude Juncker said the deal sent a message "loud and clear" - Greece will stay in the Eurozone.

The agreement demands tax rises and more tough spending cuts in return for Greece's third bailout in five years.

The deal means new loans of up to €86bn ($95bn; £61bn) will be made available over the next three years.

The first tranche will be of €26bn - €10bn to recapitalise Greek banks and €16bn in several instalments, the first of which - €13bn - will be made by 20 August, when Greece must repay about €3.2bn to the European Central Bank (ECB).

Announcing the "comprehensive and ambitious reform package", Eurogroup chairman Jeroen Dijsselbloem said: "All the intense work of the past week has paid off.

The deal rules out any "bail-in" of depositors' savings in Greek banks.

IMF managing director Christine Lagarde said the deal was "an important step forward" but stressed again that Greek debt was "unsustainable" and that relief would be needed.

Although, the price of the yellow metal has fallen some 40% since the all-time high in 2011, with investors and futures market participants cutting their bullish exposure, the fundamentals for owning it have never been more compelling.

TECHNICAL ANALYSIS

It appears that a bottom has been posted for the most recent correction in gold prices. I expect to see further sideways action before the upward momentum continues

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