Wg | Weekly Gold Commentary | 2013

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MAIN TOPICS

- Gold prices rebound.
- Fed holds interest rate.
- Global equities fall.
- Japan credit rating downgraded.

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The price of gold rebounded strongly last week after the US Federal Reserve announced that it will not be raising interest rates.

Gold prices rebound after Fed announcement.

After trading close to the $1100 an ounce level at the beginning of the week, the price of yellow metal traded as high $1143.10 an ounce as and settled the week at $1139.90 per ounce.

In what has become the most highly anticipated meeting of the Federal Open Market Committee (FOMC), the Fed announced that it was going to maintain its current policies, and left the policy rate at 0.125%. Yet, the accompanying statement and the economic projections came in more dovish than expected. The Fed showed concerns over the negative impacts of the recent global financial market volatility, as well as rapid slowdown in China and other emerging markets, on growth and inflation outlook.

In her press conference, Fed Chairwoman Janet Yellen made it clear that the U.S labour market is close to full employment, and that she's reasonably confident that the inflation rate will drift back up to around 2% eventually.

While gold prices were given a boost on Thursday and Friday, after the Fed announced that it will not be raising interest rates, the U.S dollar tumbled but later staged a strong recovery towards the weekly close. However the greenback still closed the week as the second weakest major currency, after Euro. The dollar index dipped to as low as 94.06 last week but recovered to close at 94.86.

The central bank's cautious comments about the outlook for the global economy sent shudders through global markets, and prompted a global sell-off in equities.

European markets were harder hit than the UK, with the weaker dollar pushing the euro higher and causing concern for European exporters. The FTSE 100 finished 82.88 points or 1.34% lower at 6104.11 while Germany's Dax dropped 3.06% to 9916.16. France's Cac closed 2.56% lower at 4535.85, Italy's FTSE MIB fell 2.65% to 21,514.90 and Spain's Ibex ended 2.57% lower at 9847.2.

In the U.S., stocks tumbled on Friday to their biggest one-day loss in two weeks. The Dow Jones Industrial Average closed down 291.7 points or 1.75% to 16,383 points. The S&P 500 lost 32.09 points to 1,958.11 and the Nasdaq fell 66.72 points to 4,827.23 points.

Seven years ago on September 15, 2008, the US government's total debt was $9.6 trillion. Today it's over $18 trillion... and once they raise the debt ceiling (which is inevitable) the debt will rise overnight to over $19 trillion--twice as much in seven years.

In 2008 the entirety of the Fed's balance sheet was just $924 billion. And the total of its reserves and capital amounted to $40 billion, roughly 4.3% of its total assets.

Today the Fed's balance sheet has ballooned to $4.5 trillion, nearly 5 times as large. Yet its total capital has collapsed to just 1.3% of total assets. And, its assets are things like US government bonds.

Over the last several years the Fed has essentially printed trillions of dollars and which it has used to buy US government bonds. This has all been done at almost zero interest rates. Currently the Fed is holding some $4.5 trillion worth of existing bonds, most of which they purchased when interest rates were basically zero.

So what happens if the Fed raises rates? The market value of their entire bond portfolio will fall.

And given the razor-thin capital the Fed has in reserve, they can only afford a tiny 1.3% loss on their bond portfolio before they too become insolvent.

Meanwhile, with inflation near zero, the yen plunging, the economy contracting and debt rising as the population ages, Japan's debt crisis is deteriorating quickly.

According to the International Monetary Fund, public debt will increase to about 247% of gross domestic product next year.

Japan's credit rating is cut.

Recently S&P cut Japan's credit rating, announcing that Japanese debt is now rated lower than that of China and South Korea, two of its major trading partners. Japan's bonds are barely worth the paper they're written on.

"We believe that the government's economic revival strategy — dubbed 'Abenomics' — will not be able to reverse this deterioration in the next two to three years," S&P said in a statement. "Economic support for Japan's sovereign creditworthiness has continued to weaken."

As I have mentioned countless times, the level of debt created by the major central banks around the world is not sustainable, and it seems that the governments of Europe and Japan are already teetering on the brink of massive defaults.

Demand for physical gold and silver in August and September has been exceptionally strong as investors seek a safe-haven from market turmoil, as the global economy slows down and as it becomes clear that the Federal Reserve and central banks generally are slowly losing credibility and ultra-loose monetary policies are set to continue for the foreseeable future.

At the same time the traditional months of strong demand from Asia are now ahead of us which will add even greater demand for gold in the coming weeks. In India, gold demand will reach its peak later than usual this year as Diwali falls in the second week of November.

Premiums for physical gold in China have risen from $4 per ounce to as high as $6 this indicating very strong demand in China. As do withdrawals from the Shanghai Gold Exchange.

However, this robust demand for physical gold has been obscured by the ongoing shenanigans of the bullion banks and their persistent selling of futures contracts on the Comex. For now, the paper or electronic market continues to set the price of the yellow metal creating a distorted perspective of the real situation. But rising premiums and delays for popular bullion products suggests that this continual price suppression will soon give way to a more realistic price discovery reflecting real world supply and demand.

TECHNICAL ANALYSIS

Gold prices rebounded strongly from the $1100/oz. level to break above the 50 day MA. I believe we will see prices continue to trade with an upward bias in the medium term.

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