ABC BULLION. EDUCATION

06.02.14

Markets in turmoil as we await US jobs report

Another seesaw week for precious metal investors, with gold largely range-bound between USD $1240 and USD $1275. Trading overnight was particularly volatile, with a run up to USD $1275 followed by a pullback below USD $1260, where we are this morning.

All up gold traded in a USD $25 range, and seems to have built at least temporary support at USD $1250.

Silver also had a positive run, and is now trading just below USD $20 and $19.91 per ounce, up 3% on the week in USD terms.

Australian dollar gold is currently sitting at $1413, as a rally in the AUD to over $0.89 USD following the Reserve Bank's decision to hold interest rates steady kept a lid on prices for domestic investors.

Whilst it has been disappointing not to see gold hold onto its gains in its various attempts to push higher in the last few days and weeks, especially in light of equity market falls and a plethora of relatively disappointing economic data, investors need to be patient.

Chinese New Year celebrations may have also been a factor, although Asia will be back in action on Friday, which might add some extra bids to the market.

Certainly gold investors will be much happier with their holdings YTD compared to equity investors, with broader asset markets still in turmoil.

The Nikkei, which led the way up this year is now working in reverse, -13% YTD, the Dow and SP500 in the US are now -6.7% YTD and -5.1% respectively, the Euro Stoxx 50 is -4.5% and domestically, the ASX 200 is -5.3% and in some danger of testing the psychological 5,000 point level if this unwind gets any more serious.

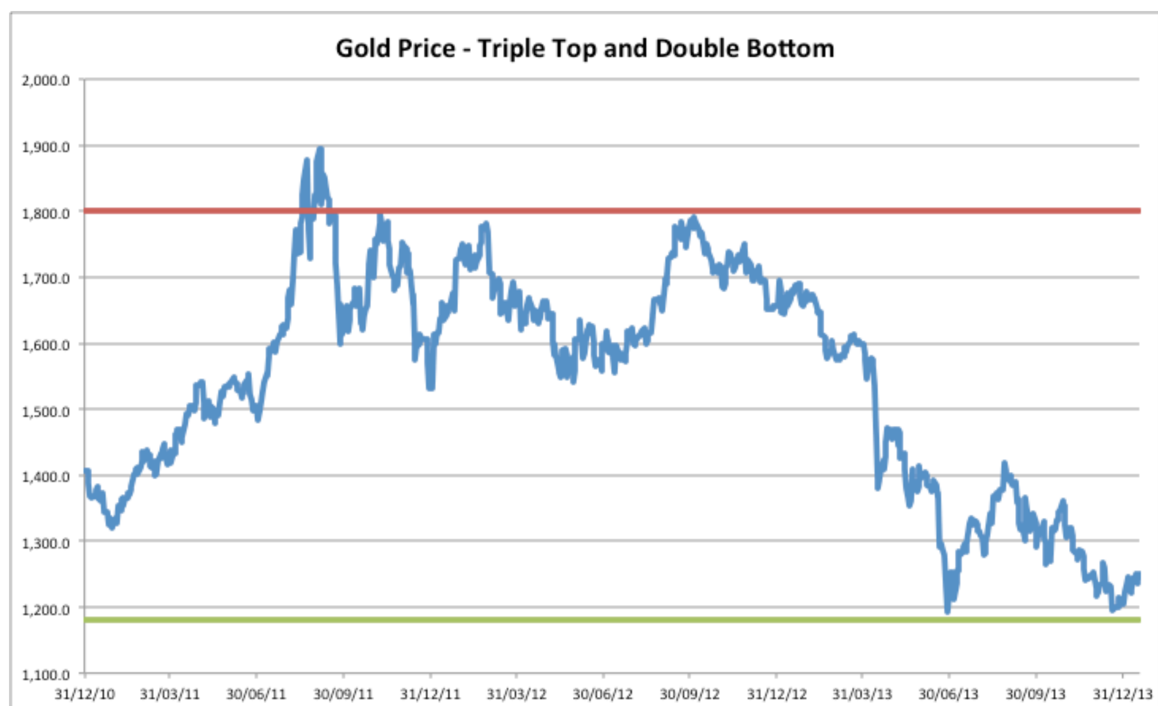
Whilst no once can be 100% certain which way stocks will go from here, and I certainly don't like to see anyone lose money in any investment, I do see a lot of risk out there, and I think the following article is worth a read, particularly as many of you will have money in a traditional superannuation fund, with a large allocation to stocks and which tend to perform in a manner that is highly correlated to the broader equity market.

On a shorter term note, I'd expect plenty of traders to be squaring away positions over the next 24 hours in the lead up to the non-farm payrolls report.

It will be the last major news report for the week, with the market desperately looking for a strong print. Another disappointing read and the odds of a 'tapered taper' from the Fed will only rise.

Could a triple bottom be coming for gold?

A triple bottom in markets is where an asset class or stock hits the same price three times, only to bounce higher in price. This typically occurs over a period of many weeks or months, and is the exact opposite of a triple top, where prices hit what turns out to be a ceiling three times, only to turn lower at this critical price point.



The chart above, which shows USD gold prices since the start of 2011, highlights clearly what proved to be a 'triple top' in gold (at USD $1800), which was formed over roughly a year after gold's initial run to USD $1900.

As you can see, gold prices tested USD $1800 three more times, and failed at all three attempts, before turning decisively lower in April last year.

Looking at the green line at the bottom, and we can now see clearly the 2 times that gold has 'bottomed' so far, with prices just below USD $1200.

Whilst there is no guarantee that the bottoming process for gold will mirror the cyclical topping process, which began occurring back in 2011, it should give investors encouragement that even if we see another test of USD $1200, there is nothing to fear, especially if gold can hold that level.

This chart should also encourage bullion investors to be patient. The triple top process took place over a 12-month period. If the same were to happen on the downside, it would indicate that gold could well trade in and around the USD $1200 range for some time.

This shouldn't necessarily detract investors from adding to positions now, as I have been personally, but I'm not doing that in the expectation of immediate upside fireworks (although it would be nice).

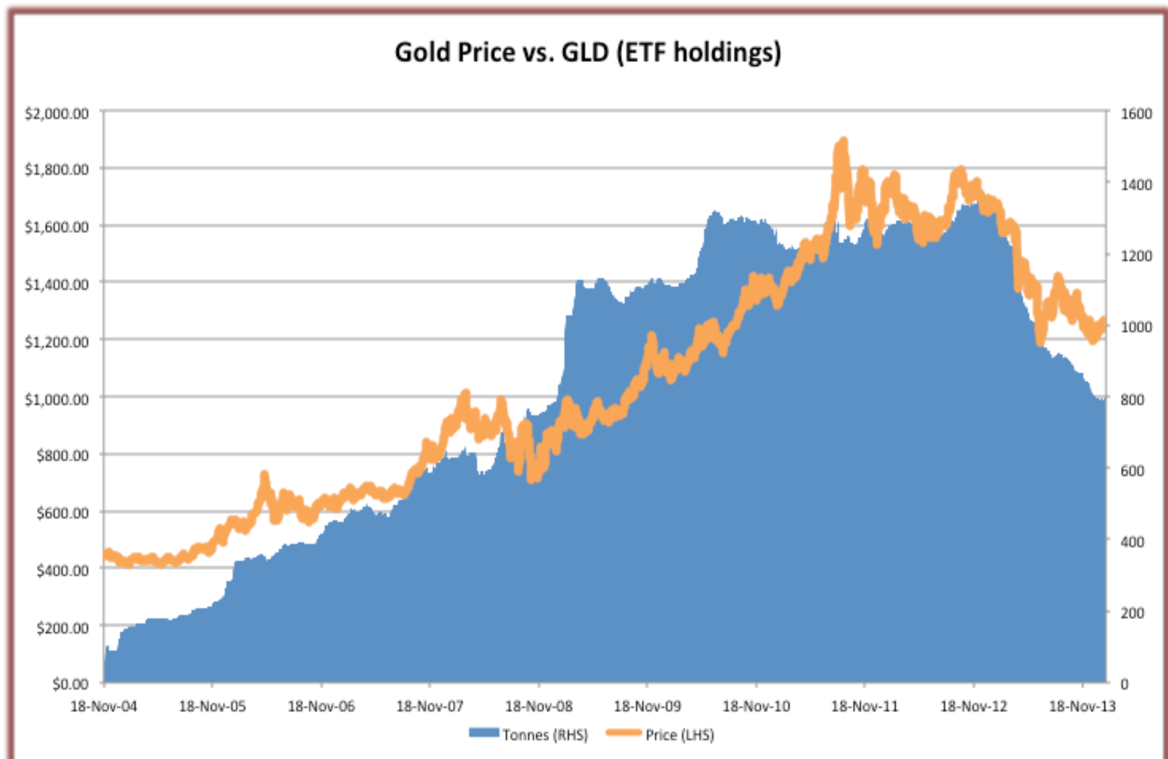
ETF flows more constructive

In other gold-price-related news, ETF holdings look to have finally found a base, with redemptions largely drying up. This is not unexpected in the face of falling equity markets, as for now at least, there is no incentive to rotate away from bullion and into 'risk assets'.

Indeed, the largest gold ETF GLD has actually seen some inflows of late, recording an increase of 125,328 ounces (roughly 4 tonnes) in their total holdings. ETF flows were one of the major drivers of the gold price last year, alongside Indian government restrictions and taxation on the importation of gold, and the voracious appetite shown by China.

As a barometer for Western investors and their attitude toward gold investment, they highlighted very clearly that most hedge funds and institutional asset managers saw the gold bull market as being over, with a preference to chase the stock market instead.

But with ETF holdings now many hundreds of tonnes lower than they were 12 months ago, the market looks far more constructive today. The 'weak hands' are gone, leaving predominantly stronger hands and long-term holders in possession of the metal.



Indeed as you can see from the chart above, GLD holdings are now back at around 800 tonnes. Last time holdings were this low was in early 2009, when the gold price was closer to USD $800, not the USD $1250 it's at today.

What's more, with holdings that low, it's safe to say that any of the excess froth that might have built up in gold heading into 2011, be it those fearing imminent hyper-inflation or an immediate 'moon-shoot' for gold with prices to hit $10,000, is now and well truly gone.

I see this as being a very bullish development going forward, and any change in demand from Western investors looking to come back into the market via GLD and other ETFs will be very positive for sentiment, although I'd always be buying physical metal itself.

Economic data wrap – Australia, the US, Japan and Europe

There has been plenty of economic data out this week, with some notable developments, starting in Australia with the RBA decision to hold rates at 2.50%. Whilst this was expected, it was the dropping of their 'easing bias', which surprised the market, as many were expecting their next interest rate move to be down (I still do).

Nevertheless, the changed tone saw the AUD rally strongly, and is pushing back toward $0.90 against the USD, a level the RBA has called 'uncomfortably high' in the past. They really are stuck between a rock and a hard place wanting to promote rebalancing here but fearing a property bubble, particularly in Sydney.

We also saw PMI and PSI reads, which were both below 50, indicating that both our manufacturing and services industries are struggling, whilst building permits fell, which doesn't bode well for construction.

The ABS also released their Job Search Experience Survey, which showed that the median duration of unemployment has hit a decade high. Not good in an environment where job ads are still weak and higher unemployment is on the cards.

Turning to Europe, and overnight we saw a truly dismal retail sales report, which fell -1.6% in December, more than 3 times the expected fall of -0.5%. Markit Services PMIs for Germany and Europe also missed expectations, whilst Italy and Spain's remained in contractionary territory. On a brighter note, manufacturing services in Europe generally beat expectations

Eurozone business investment is still falling though, and is currently at a modern era low of 18.9%, nearly 2% below where things fell to in the aftermath of the dotcom bubble. Private sector loans fell by over 150 billion euros in the past quarter.

All this makes the ECB rate decision overnight incredibly important, with many expecting Draghi to announce further stimulus plans.

Turning to Japan, and the big news was that Japanese real wages are back at the lows experienced during the GFC, which coincides with the lowest level they've been at in more than 15 years. Alongside a Nikkei that is now plummeting, it's leading more people to question the sense of Abenomics, which so far doesn't seem to have got much traction turning the actual economy around.

In the USA, the ADP employment report showed 175,000 Americans getting a job in the private sector last month, well below both the prior 3- and 6-month averages, which came in at 230,000 and 205,000 jobs respectively. Services PMIs and ISM non-manufacturing PMIs held up strongly, but the biggest 'miss' of the weak came Monday night Australian time, when the ISM manufacturing PMI came in at 51.3, well below expectations.

More concerning with the report were some of the sub-sectors, with new orders falling over 13 points, the largest plunge since 1980, whilst the employment component also weakened noticeably.

Between now and the weekend, look out for Australian retail sales and the overnight decisions by the ECB and the BoE, whilst in the US it will be all about the non-farm payroll report.

This number has confounded analysts of late, so it wouldn't be a surprise to see a number that is either much higher or much lower than market consensus, which is currently suggesting 185,000 job additions in the USA last month.

Until next week,

Jordan Eliseo
CHIEF ECONOMIST

ABC Bullion

This publication is for education purposes only and should not be considered either general of personal advice. It does not consider any particular person's investment objectives, financial situation or needs. Accordingly, no recommendation (expressed or implied) or other information contained in this report should be acted upon without the appropriateness of that information having regard to those factors. You should assess whether or not the information contained herein is appropriate to your individual financial circumstances and goals before making an investment decision, or seek the help the of a licensed financial adviser. Performance is historical, performance may vary, past performance is not necessarily indicative of future performance.