



28.11.13

Gold is 'crumbling' – or is it?

Precious metals look like continuing their losing streak this week, with gold prices down slightly on where they finished on Friday the 22nd November, when the London PM Fix came in at USD \$1246.25, with silver at USD \$19.93 on the same day.

With the metals trading at USD \$1237.25 for gold and USD \$19.69 for silver, they are both marginally down so far across this trading week.

Despite the fact that overall, prices haven't moved much this week, there's been no shortage of activity or commentary surrounding the precious metal market, with the gold market freezing again in response to a large sell order hitting the market when trading was particularly illiquid.

Earlier in the week, the Iran nuclear deal helped lead to sell off on Monday which pushed prices down below USD \$1230 at one point, and had many predicting a re-test of the USD \$1200 mark was soon on the cards.

Since then, we've seen conflicting US consumer confidence (some falling, some rising) alongside higher than expected house price growth in the US (according to the Case Shiller housing index), whilst in Europe we've heard even more talk about the potential for negative interest rates on the continent, as they try and fight their officially low inflation figures, stagnating economy and record high unemployment.

Overnight, we saw US durable good orders come at -2.0% (-0.1% ex autos which add a lot of volatility), the third month in the last four that it's fallen, and well below expectations, whilst mortgage applications also fell.

Whilst housing prices, as per my above comment on the Case Shiller housing index, have still been rising, mortgage applications are a critical barometer for the health of the US housing market, and whilst not plunging anymore, they are off the better part of 50% since bond yields starting moving higher when 'taper' talk started in Q2 this year. It's this reason that has led banks like Wells Fargo and Bank of America to lay off thousands of staff citing to financing/refinancing activity.

Indeed, [more trouble could be coming to the US housing market](#), with the number of institutional investors looking to purchase falling substantially (they've been a big part of the rally in home prices this past year or so), according to RealtyTrac, whilst the number of Americans falling behind on or missing payments on their home equity lines of credit again on the rise.

More positive news, it must be said, came from initial jobless claims in the US, which again fell, this time to 316,000, whilst the Chicago Purchasing Managers Index came in with a reading of 63.0, above consensus.

Whilst a reading of 63.0 would imply relatively robust growth, new orders fell, as did production. What did rise (significantly) was inventory build, off the back of 'expectations of higher demand', not actual demand you'll note.

Despite the, at best, mixed economic data coming out of the US, confidence (from an investors perspective) in the Fed and their ability to engineer a sustainable recovery and exit from QE eventually is still obviously very high, with [an appropriate headline from Zerohedge today](#) pointing out that the Dow, the NASDAQ, the S&P, the Russell, Bitcoin, and the US Debt are all hitting record highs.

With that in mind, it is little wonder investors aren't enthusiastic about bullion, with market sentiment still very bearish.

An article in [Business Insider this week](#) ran with the headline 'Gold is crumbling', hence the title of my report this week. It's an appropriate gauge of the overwhelming view of market participants towards gold today.

And whilst I don't believe the long-term bull market for metals is over, it must be acknowledged that the technical picture for gold is currently weak. The following chart, put together by the team at the Daily Reckoning, shows that since the start of the year, gold has been in a profound down trend.

As you can also see, every time gold has challenged that trend, it has failed, and turned lower:



The first of these instances was at around the \$1600 mark in early April, which was only a couple of weeks before the original price plunge which took gold down to the USD \$1320 region.

A bounce back to nearly USD \$1,500 was followed by an even more significant fall, placing gold below USD \$1,200 as the financial year ended.

Whilst technically gold is up in H2 2013 so far, as you can also see from the above chart, gold had a relatively strong rally in July and August, but couldn't break the downtrend around USD \$1430.

It once again attempted to rally in late October, but this time got turned back at around USD \$1350, and as we stand, obviously we are roughly USD \$100 lower today.

USD \$1,200 is going to be a key support line. Whilst the market did trade lower than this in late June, it was only for a couple of days.

If we do test USD \$1,200 in the next month or so, and it doesn't hold, then there is a good chance we'll see another clear out in precious metals, before we find a final bottom, possible around December of this year or January of 2014.

Note, I'm not predicting that this will happen, and in fact I think that the fact that so many people are expecting it to happen makes it somewhat unlikely, but forewarned is forearmed, and the bears are still in control of the market for the time being.

Gold – 100 reasons to sell

Any dispassionate review of gold and silver prices for this year can only come to one conclusion, and that is that nothing has worked for gold in 2013

- The Federal Reserve increased QE in December 2012 and has maintained the \$85 billion a month pace all year, yet the gold price has fallen.
- The Bank of Japan have undertaken a monetary policy stimulus even greater than the Federal Reserve in respect of the size of their economy, and the gold price has fallen.
- Cyprus confiscated depositor funds from its banks, and the gold price has fallen
- Geopolitical tensions have risen, most notably in Syria, and the gold price has fallen

The list goes on and on. Nothing has worked for gold this year, and with the market still operating in the belief that not only will QE be tapered next year, but also that the global economy is heading toward 'escape velocity', the consensus opinion is that nothing will work for gold anymore, and its glory days ended in 2011 and are not coming back.

Whilst worrying in the short-term, the lack of love towards precious metals should be hugely encouraging for investors, especially those with the conviction to be a contrarian, and those that have the appropriate time-frame in mind as regards investing in bullion.

And the reason for that is simple, and it comes down to having the humility as an investor to realise that in all likelihood, we, as individuals, aren't possessing any major insight the rest of the market isn't also aware of.

A gentleman by the name of Bob Moriarty, who runs the website www.321gold.com.au was once [quoted as saying words to the effect of](#) *"if you can count 100 reasons why you should buy something, sell it. If you can count 100 reasons to sell something, buy it."*

The logic, whilst it might appear confusing on the surface, is incredibly simple to understand. If you can think of 100 reasons to buy something, so can everyone else, so they've probably already bought it, meaning there are in all likelihood only sellers left.

The opposite is also true. If you can think of 100 reasons to sell something, so can everyone else, and they've probably already sold it, meaning there are most likely only buyers left.

That is a very accurate reflection of what the market is thinking about gold right now.

There are 100 reasons most people can think of to sell gold.

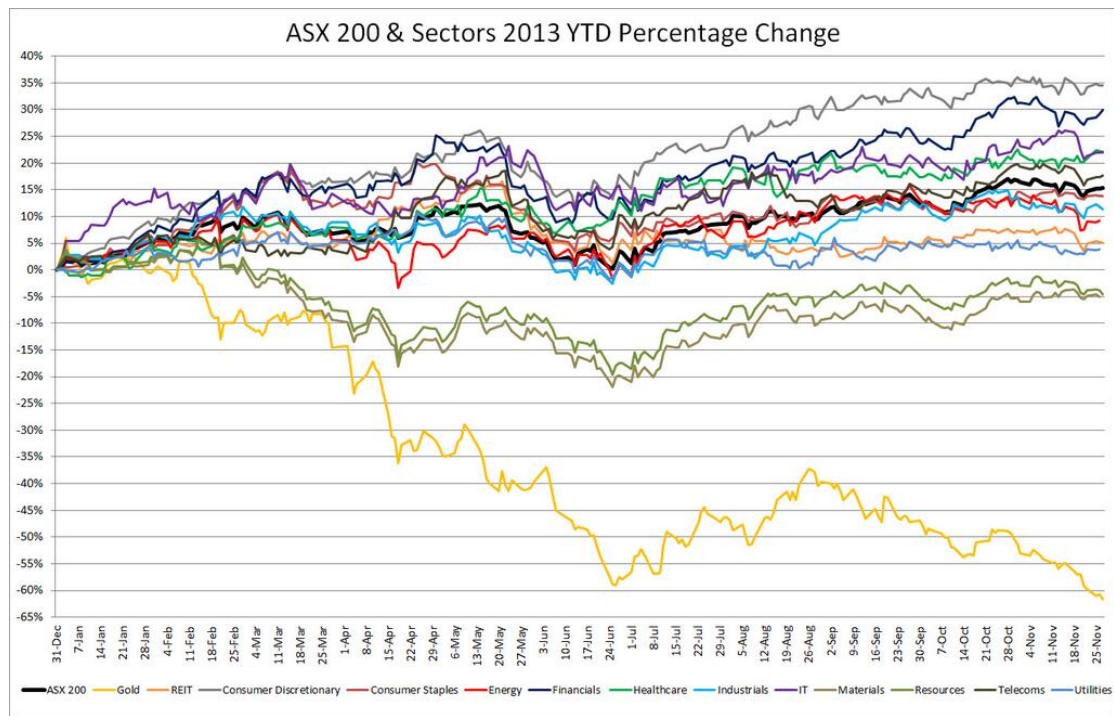
I'm buying.

Gold stocks are the most hated asset class on the planet

Whilst anyone who's been an investor in either physical gold or silver has seen their portfolio take a hit this year, spare a thought for those who've concentrated their precious metal exposure into gold stocks.

The chart below shows the sector returns on the ASX200 for the year so far, and as you can see, gold stocks have suffered an incredible fall in value, with the sector as a whole down roughly 60%.

No miner (or explorer) has been spared, with even the heavyweight of the sector, Newcrest Mining, trading below \$8.00, down 65% from where it started the year.



Source: ASX 200

A chart like this helps to highlight a key mantra regarding investing in this sector, and that is that one must not confuse investing in physical precious metals with investing in mining companies that produce (or explore for) gold.

If anything, 2013 has reminded us that, as stand alone assets, gold and silver are volatile. This is doubly so for gold mining companies, and with them you have added risks (political, operational, financial, management etc.)

This is not to say one shouldn't have any money in this sector (or indeed any other asset class), but it does highlight that when it comes to those looking for long-term wealth protection, physical precious metals are a superior investment.

For the record, the best performing sector of the year has been consumer discretionary (think JB HiFi and the like), which has rallied strongly even through our retail sector has been struggling all year.

The overall rally in the stock market has been the major factor behind superannuation funds returning over 15% YTD, a subject [covered in Money Minute on the Today show this week](#).

The Money Minute excerpt is [actually worth a watch](#) as it talks about how dominant the major companies on the ASX are in terms of the overall market, and the fact that all the major funds do is try and beat the index.

Talk about being dammed with faint praise!

Pay attention to Karl's comment at the end regarding fees too.

Gold demand in China

As many would be aware, demand for gold in China has reached incredible levels, with recorded imports to the mainland from Hong Kong running at 855 tonnes in the year to September, and on track to reach 1000 tonnes for the year.

However, this number understates overall demand with evidence suggesting up to a fifth more bullion has gone into China via other routes, and of course, the official stats don't show purchases mainland Chinese make when visiting Hong Kong on business or as tourists.

Whilst hard to estimate, Chow Tai Fook, the world's largest jewellery chain, [reported a 92% jump in profit](#) in the last year, as demand for gold has exploded.

What's also fascinating is the very evident transfer of wealth (gold) from West to East, as hundreds of tonnes of gold are shipped from London to Switzerland, where they are re-refined into kilo bars, and then shipped on to Asia.

As Scott Morrison, Chairman of gold refiner Metalor stated; *"We see huge flows of gold in and out of Switzerland, an inflow of large bars, which we convert to smaller bars. From April to August, we saw very large volumes from all our refineries headed to Asia"*, whilst Argor-Heraeus, a Swiss refiner, [stated that 70% of their kilo bar production](#) was being shipped to China.

This is the gold that ETF holders and the like have been divesting this year, in their belief (erroneous in my view) that the gold bull market is over. They will find it hard to get it back at anywhere near today's prices as Chinese investors will not be selling this gold any time soon.

Make no mistake about it, whilst many precious metal analysts spend a lot of time talking about the need to own physical gold and silver as the ultimate hedge against what might broadly be defined as the decline of the developed western world, the precious metal story is also very much a way to profit from the tailwind that is the rising prosperity of the East.

The Chinese know the chart below, and know they'll need tens of thousands of tonnes of physical gold if they want to be the next global economic powerhouse:



Source: Classical Numismatic Group

Unlike the game we all played as children, in the real world of global finance, precious rock beats worthless paper, hands down. It always has, it always will.

The unprecedented movement of physical gold from West to East has only just begun.

Until next week,



Jordan Eliseo
CHIEF ECONOMIST

ABC Bullion

This publication is for education purposes only and should not be considered either general or 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 of a licensed financial adviser. Performance is historical, performance may vary, past performance is not necessarily indicative of future performance.