Gold Monitor

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Murenbeeld & Co.
Subscription research for the gold business.

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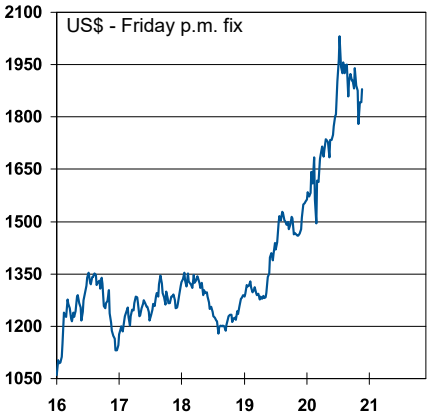
GOLD PRICE

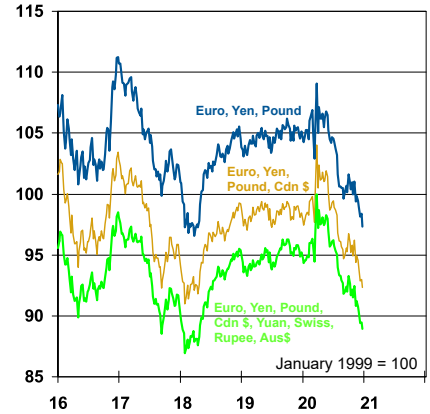


Source: Bloomberg, Murenbeeld & Co.

	Dec-14	Dec-15	Dec-16	Dec-17	Dec-18
Gold - 2nd Fix	1831.15	1850.65	1851.95	1890.75	1879.75
Gold - COMEX	1828.70	1852.30	1856.10	1887.20	1885.70
Silver - HH	2390.50	2449.90	2495.30	2587.80	2586.70
Platinum - NYME	1015.60	1039.30	1035.40	1050.10	1041.50
Crude Oil - NYME	46.99	47.62	47.82	48.36	49.05
CRB Bridge - NYBOT	162.24	163.02	163.86	165.49	166.45
US $ Index (EFXR0C)	98.01	97.64	97.35	96.90	97.24
Fed Funds (Overnight)	0.09	0.09	0.09	0.09	0.09
US 10-Year TIPS Yield	-1.01	-1.03	-1.03	-1.03	-1.03
TSX Global Gold Index	304.12	311.96	317.92	327.64	322.34
S&P 500	3647.49	3694.62	3701.17	3722.48	3709.41

Source: Bloomberg, Murenbeeld & Co.

US DOLLAR INDEX



Source: Bloomberg, Murenbeeld & Co.

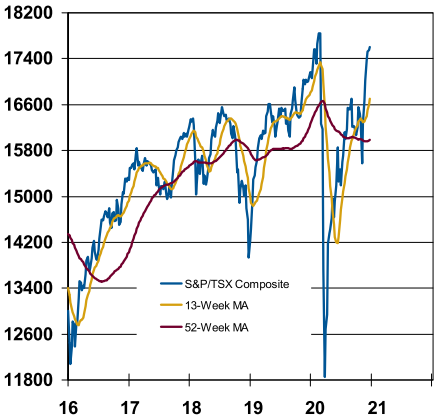
Review

by Martin Murenbeeld

It was a good week for gold; the Friday/Friday pm fix rose $37.75 but since Monday was a down day for gold the weekly chart below suggests something closer to $60 is a more accurate assessment of the price rise this week.

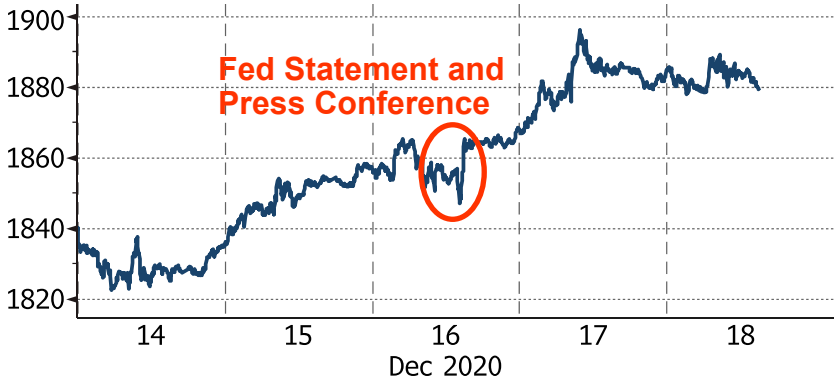
The Fed met this week (discussed below); the statement and Powell's press conference had a positive impact on gold. So did the news mid-week that *Congressional leaders closed in on a roughly $900 billion coronavirus relief deal that includes another round of direct payments to households …* (WSJ 12/16). No deal was reported at the time of writing, however; a new sticking point appears

S&P/TSX COMPOSITE INDEX



Source: Bloomberg, Murenbeeld & Co.

Gold Price
Last 5-days



Source: Bloomberg, Murenbeeld & Co.

to be a Republican push *to insert a measure that would restrict the Federal Reserve's ability to establish the types of emergency lending programs that it authorized in March to curb an emerging financial panic … That step would go beyond an earlier proposal to revoke $429 billion provided to the Treasury to backstop losses in the Fed lending programs* (WSJ 12/18).

We'll see, but a relief bill should be signed shortly; both Congress and the Administration want something signed before Christmas recess! Meanwhile, the dollar and the 10-year TIPS yield declined marginally over the course of the week, which helped gold now that the 22-day rolling correlations have turned negative again.

Fed Meeting

The statement following the Fed meeting was not significantly different from the previous statement, but it notably stressed that: *The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range* ***until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time.*** *… the Federal Reserve will continue to increase its holdings of Treasury securities by at least $80 billion per month and of agency mortgage-backed securities by at least $40 billion per month* ***until substantial further progress has been made toward the Committee's maximum employment and price stability goals****…* (bolding added).

The statement and Powell's press conference following the meeting were widely interpreted to be quite dovish, particularly so in light of the fact that vaccines are now being distributed and that the economic outlook for 2021-H2 has accordingly improved.

FT (12/16) – ***Powell preserves his dovish credentials at tricky moment for Fed*** *… In a delicate balancing act, the Fed chairman held off on a big boost to the central bank's asset purchases but introduced guidance that will keep them in place for a longer timeframe. This preserved Mr. Powell's dovish credentials and the sense that the Fed remains in the fight for the long term, soothing investors …* (bolding added).

WSJ (12/16) – ***Fed Reinforces Plans to Provide Open-Ended Stimulus to Spur Recovery*** *… The [SEP: economic] projections show most officials thought they would hold short-term rates near zero* ***for least three more years*** *despite a somewhat more optimistic economic outlook than they had in September, before drug makers had developed highly effective Covid-19vaccines … Many officials projected* ***such low rates would be needed even though they projected inflation would be at the Fed's 2% target and unemployment would fall below 4% by the end of 2023.*** *Those projections reflect a change in the central bank's framework adopted this summer that took* ***a more relaxed view toward inflation*** *…* (bolding added).

Peter Boockvar (*The Boock Report with Peter Boockvar*, 12/16) – *Jay Powell could not have been more dovish. In fact, the dovishness was oozing out everywhere. We are now rolling out a vaccine and he talked about how he could provide more accommodation by doing more QE or extending out maturities ….*

No surprise here – we fully expected the Fed to maintain *pedal to the metal* well into 2021, if not right through 2022. The Fed has frequently mentioned the damage to the labor market resulting from the pandemic, and often noted that many participants currently unemployed or under-

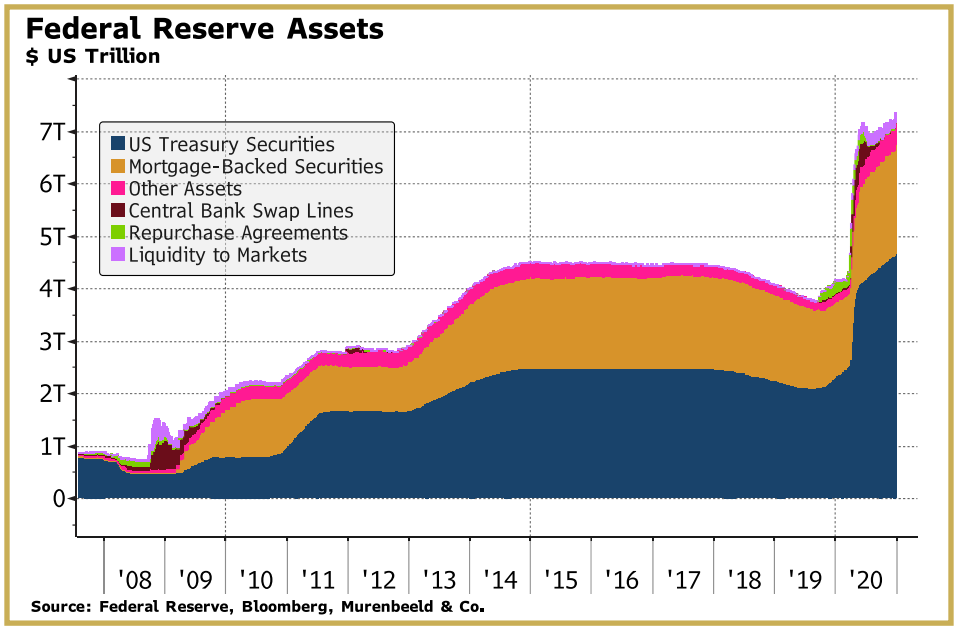
employed will not be returning to their previous jobs. The Fed has constantly referred to *maximum employment* in all its public statements, and its forward guidance suggests inflation will be allowed to exceed 2% for an extended period of time.

The dot-plot spreadsheet we use to track Fed participants' FF-rate projections is included below. It shows, see the December 2020 panel, that the weighted-average of the FF-rate projections (i.e., of what each participant believes to be the appropriate FF-rate for year-end) is essentially unchanged through 2022, and is no more than 13 basis points higher at the end of 2023.

You just can't get lower than that – I mean as it stands the Fed simply doesn't expect to raise rates until late 2023 at the earliest! That's dovish indeed!

And not to be overlooked from a gold perspective, the real FF-rate (the nominal rate of .25% less inflation) is expected to stay around -1.5-1.6% through 2023. If this isn't positive for gold, I don't know what is.

The chart of the Fed's balance sheet highlights what has happened this year to date. With at least $120 billion



FOMC Projections for Federal Funds Rate

	June 2020					September 2020						December 2020					
Target FF Year-end	Target FF Year-end	2020	2021	2022	Long Run	Target FF Year-end	2020	2021	2022	2023	Long Run	Target FF Year-end	2020	2021	2022	2023	Long Run
0.00	0.00					0.00						0.00					
0.25	0.25	17	17	15		0.25	17	17	16	13		0.25	17	17	16	12	
0.50	0.50			1		0.50				2		0.50			1	3	
0.75	0.75					0.75			1	1		0.75				1	
1.00	1.00					1.00						1.00					
1.25	1.25			1		1.25						1.25				1	
1.50	1.50					1.50				1		1.50					
1.75	1.75					1.75						1.75					
2.00	2.00				1	2.00					1	2.00					1
2.25	2.25				3	2.25					3	2.25					3
2.50	2.50				9	2.50					9	2.50					9
2.75	2.75				1	2.75					1	2.75					1
3.00	3.00				2	3.00					2	3.00					2
3.25	3.25					3.25						3.25					
3.50	3.50					3.50						3.50					
3.75	3.75					3.75						3.75					
FOMC	FOMC	17	17	17	16	FOMC	17	17	17	17	16	FOMC	17	17	17	17	16
FF-Rate	FF-Rate					FF-Rate						FF-Rate					
W-Ave	W-Ave	0.25	0.25	0.32	2.50	W-Ave	0.25	0.25	0.28	0.38	2.50	W-Ave	0.25	0.25	0.26	0.38	2.50
Median	Median	0.10	0.10	0.10	2.50	Median	0.10	0.10	0.10	0.10	2.50	Median	0.10	0.10	0.10	0.10	2.50
Headline PCE	Headline PCE	0.80	1.60	1.70	2.00	Headline PCE	1.20	1.70	1.80	2.00	2.00	Headline PCE	1.20	1.80	1.90	2.00	2.00
Core PCE	Core PCE	1.00	1.50	1.70	-	Core PCE	1.50	1.70	1.80	2.00	-	Core PCE	1.40	1.80	1.90	2.00	-
Real FF	Real FF	-0.55	-1.35	-1.38	0.50	Real FF	-0.95	-1.45	-1.52	-1.62	0.50	Real FF	-0.95	-1.55	-1.64	-1.62	0.50

Source: Federal Reserve, Murenbeeld & Co.
(**How to read the table**: Each column indicates the number of Fed participants who feel the accompanying FF-rate (upper bound) is the appropriate rate for year-end.
For example, at the December 2020 meeting all 17 participants deemed 0.25% to be the appropriate FF-rate at year-end 2020, and year-end 2021.
A similar analysis holds for 2022 year-end, 2023 year-end, and the Long Run.

to be added to the balance sheet each month ($80 billion in Treasuries and $40 billion in MBS) it will rise another $1.44 trillion over the next 12 months, and possibly also over the 12 months thereafter. Indeed, the Summary of Economic Projections – SEP – does not suggest many Fed participants see anything that could be described as *maximum employment* before 2023-end!

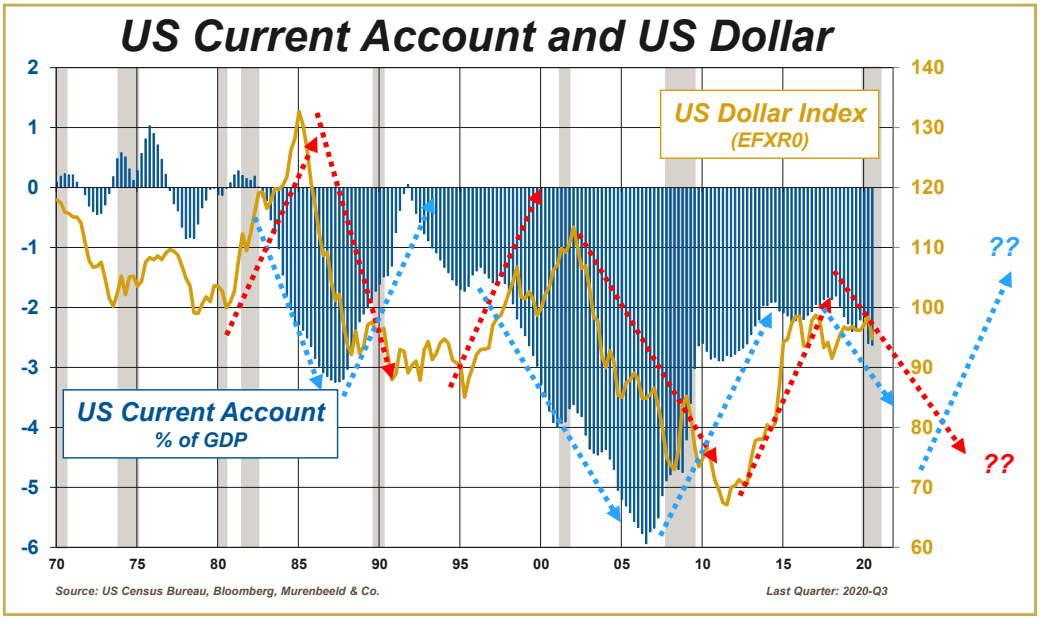
The outlook for Fed policy is also not particularly constructive for the dollar, although other central banks are also in highly stimulative mode. Add the Biden's predisposition to expand the US budget deficit significantly (which is not to say the Trump Administration was so penny-pinching given the deficit data), and on top of negative interest rates we should have a weaker dollar helping gold out too.

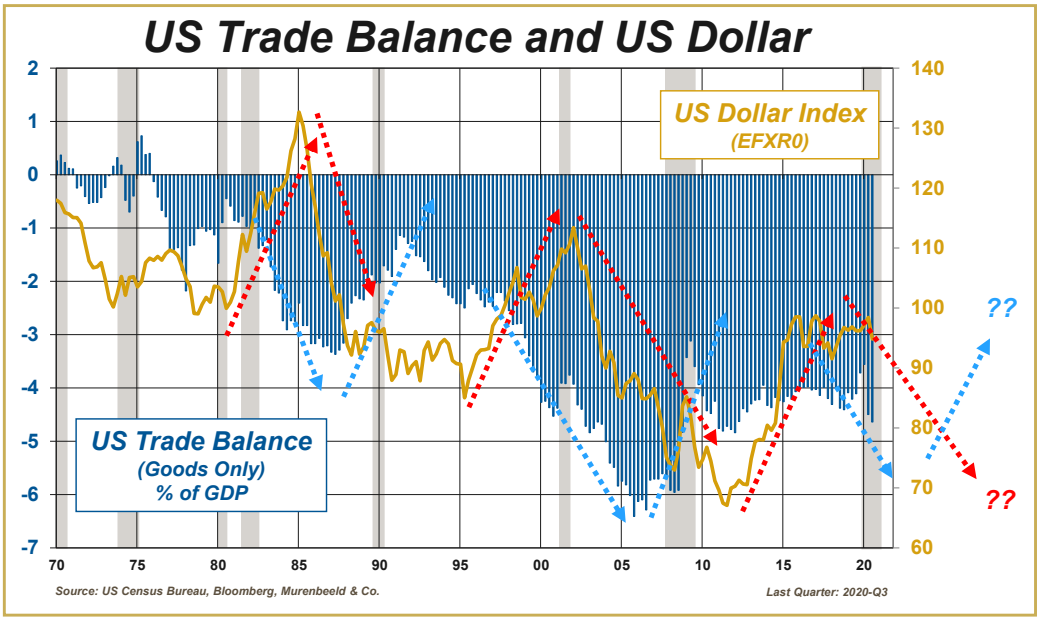
The Dollar and US Trade

We had a question this week on our argument last week that a dollar decline will help rebalance (i.e., reduce) the US trade deficit. The questioner noted it often appears that when the dollar declines, the US trade deficit simply keeps on rising. So, is our argument indeed correct?

Without getting into the economic/theoretical details of US trade deficits we simply want to highlight here trends in the US current account and trade-in-goods deficits with trends in our US dollar index – an index identical to the DXY. (There are many economists who argue that a lack of domestic savings and large US budget deficits will of necessity mean large US trade deficits – which is an ex-poste truism but sheds little light on the currency dynamics of the deficit. Those dynamics have been discussed often in this report.)

BTW, the CA deficit for 2020-Q3 was released this





morning and widened 10% to nearly $180 billion, which is just short of $720 billion on an annualized basis. Not an insignificant deficit!

The red arrows in both charts denote periods when the US dollar is rising or falling. The dollar rose strongly in the 1995-2001 period for example, and then declined strongly in the 2002-2008 period.

Did this rise and decline, and other rises and declines, have a visible impact on the US CA/trade deficits?

The answer is yes! But we must note that the impact of the dollar on the deficit is often delayed; trade flows do not respond rapidly to currency changes for a multitude of reasons, including the time necessary to substitute from overseas suppliers to domestic suppliers (part of the *J-Curve* effect). There are also other factors which make the visual relationship in these two charts murkier; the two most important ones are *recessions* (during which the US trade deficit often declines simply because US consumers import less) and more recently the increase in US domestic *oil production* (higher domestic production – shale – has seriously reduced US annual trade deficits over the last 10 years, independent of the dollar's ups and downs).

But look at the blue arrows, which denote periods when the CA and trade deficits rise and decline; the blue arrows tend to match up quite well with the red arrows – with the expected lag.

As it stands currently, we expect US deficits to rise for several more years as a result of the recent surge in the US dollar (i.e., from 2012 to 2018-2020). But then, assuming the dollar declines over the next 4-5 years (which we expect), the US deficits should start to decline again.

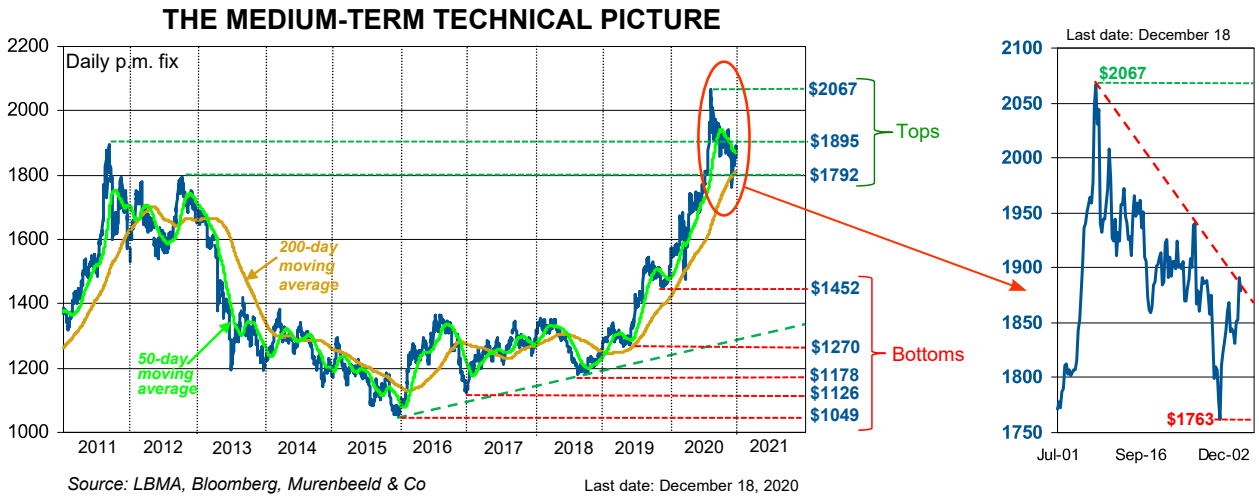
In short, we are very much of the view that a reduction in US external deficits (which of necessity implies a reduction in US trading partner surpluses) requires a decline in the US dollar's exchange rate with other important currencies – the renminbi, SE Asian currencies, the yen, and the euro.

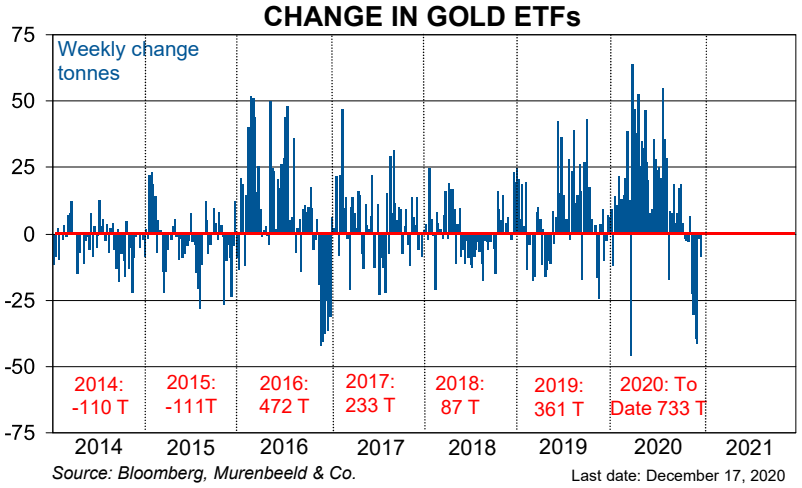
Other policies would also help to reduce global imbalances. For example, the latest report from the US Treasury to Congress on *Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States*, which looks for potential predatory trade policies abroad, notes among its 69 pages that: *China should take decisive steps to further rebalance its economy and allow for greater market openness by implementing structural reforms to reduce state intervention, strengthen household consumption growth, and permit a greater role for market forces* (i.e., China should allow foreign access to domestic markets and boost consumption to soak up domestic output as well as bring in more imports).

The Treasury report did not discuss what domestic fiscal policies the US might adopt to help reduce global imbalances – which is a whole other issue.

But if Biden wants smaller trade deficits, more made-in-America goods and services, and higher domestic employment, he should start by getting other countries to revalue their currencies!

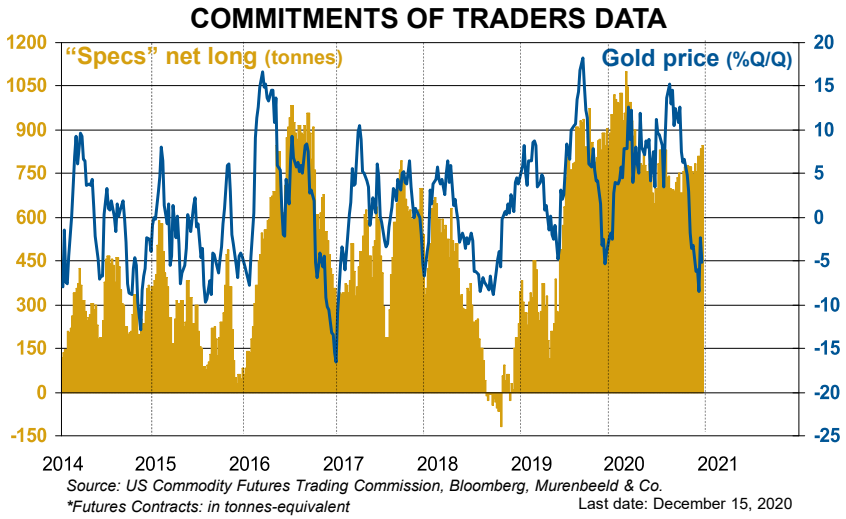
And the bi-product of this will be a higher US dollar price of gold!



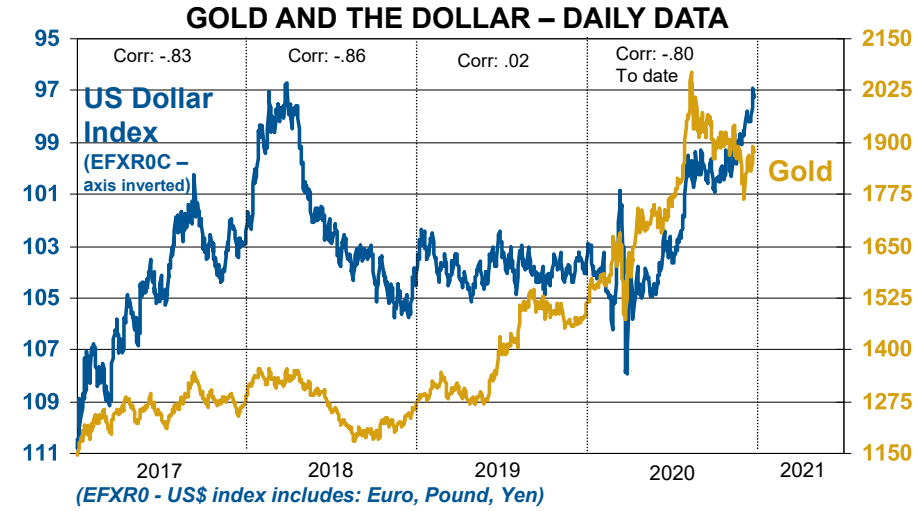


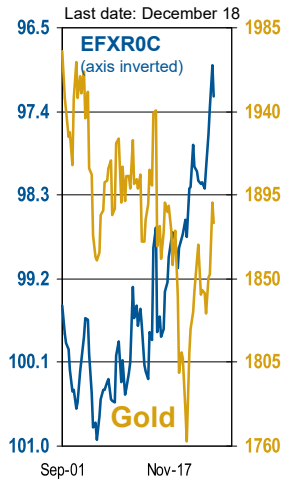
The technical picture has improved! Gold has broken its downtrend line and with gold's correlations with the dollar and TIPS yields negative again we expect gold to do better in coming weeks.

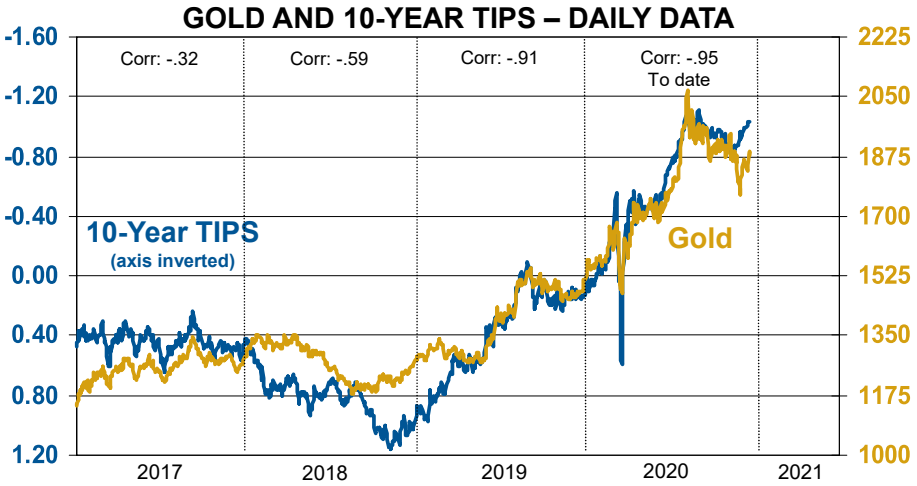
ETF demand remained modestly negative this week ...

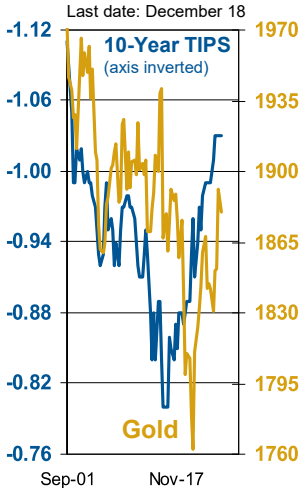


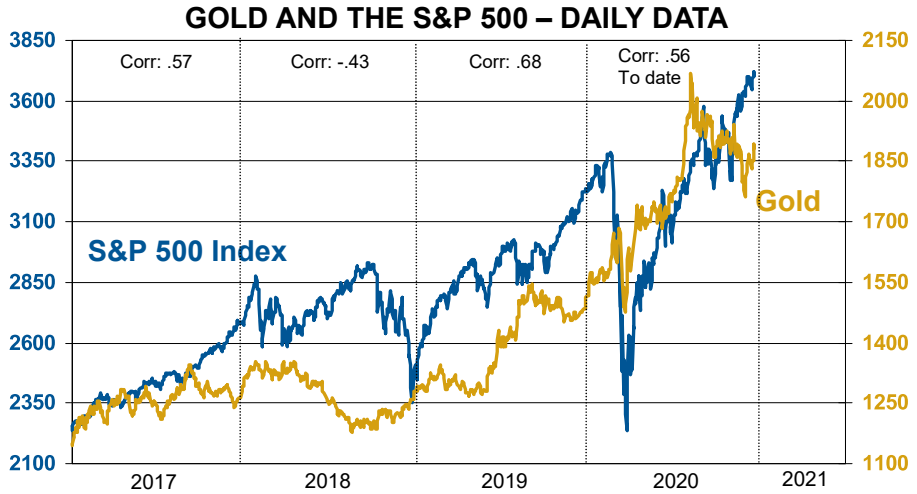
... but the net-long "spec" position on COMEX continued to rise modestly in the week through Tuesday.

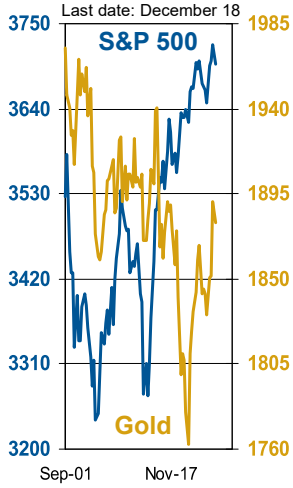












Source: Bloomberg, Murenbeeld & Co.

Good news! The 22-day rolling correlations of gold with the dollar and with the TIPS yield have turned negative again, suggesting these relationships are returning to normal.