Precious Metals Weekly

Group Economics
Macro & Financial Markets Research

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Goldilocks for now

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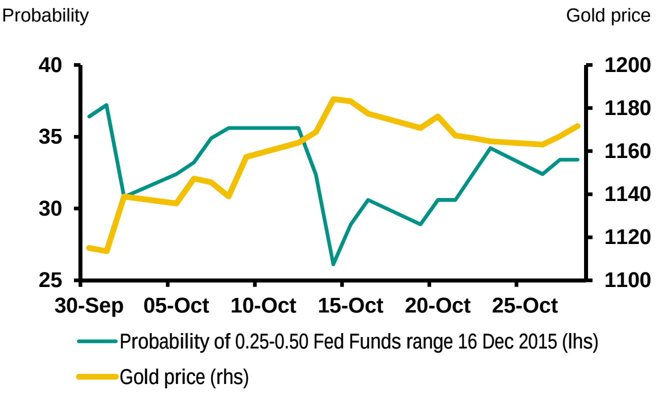
- **The usual suspects continue to support gold prices…**
- **…and they are all interrelated**
- **Supportive environment to remain in place for now**

The usual suspects continue to support gold prices…
Gold and to a lesser extent silver prices have commonly accepted drivers such as the direction in the US dollar, expectations about monetary policy in the US (if prices are denominated in US dollars), overall investor sentiment and jewellery demand. Over the recent years, the first three drivers have played an important role in explaining gold price behaviour. This is mainly because investor demand has taken a more prominent role and this demand is more fluid than jewellery demand.

The behaviour of gold prices this month can mostly be explained by these three factors that drive investment decisions in gold. Since the start of this month expectations of a Fed rate hike have been adjusted downwards, mainly because of weaker US employment report on 2 October and weaker US retail sales on 14 October. The graphs below show that investors scaled back expectations of a rate hike at the 16 December Fed meeting, which has supported gold prices (inverse relationship).

Fed rate hike expectations, gold price

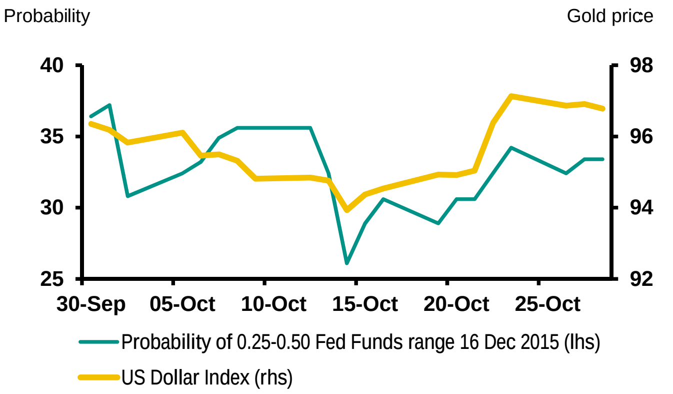


Source: Bloomberg, ABN AMRO Group Economics

...and they are all interrelated

It will come as no surprise that the other important forces that drive gold prices such as the direction in the US dollar and overall investor sentiment are affected by expectations about US monetary policy. This makes it an interrelated network of forces. The US dollar was negatively affected by lower expectations of a Fed rate hike this year as the graph below shows. This also supported gold prices.

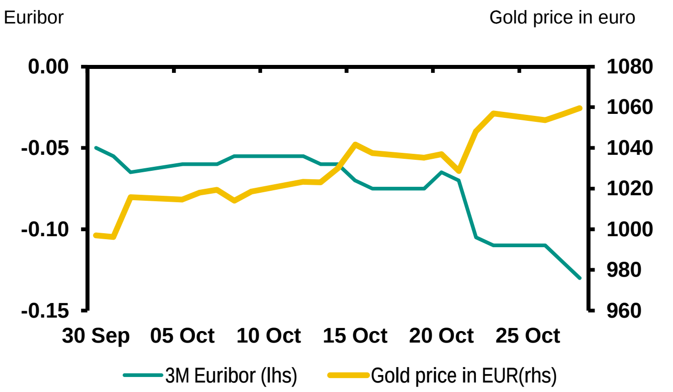
Fed rate hike expectations, US dollar



Source: Bloomberg, ABN AMRO Group Economics

The behaviour of investor sentiment is somewhat more complicated. There are four possible scenarios. For a start, there are periods that disappointing economic data are considered as good news because the likelihood of more monetary policy easing has increased. These periods of optimism are supportive for gold prices because monetary policy easing makes gold as a zero-to-low income asset more attractive (same for other precious metals). We have seen this reaction after the ECB meeting last week where ECB President Draghi signalled more monetary policy easing to come even with the possibility of a deposit rate cut. As a result, gold prices rallied considerably versus the euro.

Euribor, gold price in euro



Source: Bloomberg, ABN AMRO Group Economics

Moreover, there are also periods that disappointing economic data trigger general growth worries resulting a more risk averse behaviour. For gold prices this is also good news, because investors have a tendency to buy gold if investor sentiment deteriorates.

There are two scenarios that are not supportive for gold prices. Periods of better-than-expected economic data triggering expectations of less monetary policy easing (ECB, BoJ) and/or earlier-than-anticipated Fed rate hikes. The strong economic data provide confidence to investors so investor sentiment remains optimistic. This is the most negative scenario for gold prices. We expect the Fed to raise rates during the course of next year, so this gold price weakness will likely to play out in 2016. If expectations of rate hikes result in risk aversion, the downside in gold prices will be dampened.

Possible gold price reaction after the FOMC this evening

Expectations in financial markets about a possible rate hike by the Fed this year are low, but a Fed rate hike is not completely priced out yet. We don't expect the Fed to signal a rate hike in December. It will likely continue to focus on the uncertainty. As a result, financial markets will completely price out the possibility of a rate hike this year, supporting gold prices and weighing on the US dollar in the near-term

ABN AMRO precious metals forecasts

Changes in red/bold

End period	28-Oct	*Close 14*	*Mar-15*	*Jun-15*	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16
Gold	1,174	*1,185*	*1,184*	*1,172*	*1,112*	1,100	1,050	1,000	950	900
Silver	16.1	*15.7*	*16.6*	*15.7*	*14.5*	15.0	14.5	14.0	14.5	15.0
Platinum	999	*1,216*	*1,141*	*1,081*	*910*	900	875	850	900	1,000
Palladium	681	*798*	*736*	*674*	*652*	650	625	600	625	650

Average	*Q1 15*	*Q2 15*	*Q3 15*	Q4 15	2015	Q1 16	Q2 16	Q3 16	Q4 16	2016
Gold	*1,218*	*1,193*	*1,126*	1,106	1,170	1,075	1,025	975	925	1,000
Silver	*16.7*	*16.4*	*15.0*	14.8	16.0	14.8	14.3	14.3	14.8	14.5
Platinum	*1,194*	*1,129*	*993*	905	1,075	888	863	875	950	894
Palladium	*786*	*759*	*618*	651	700	638	613	613	638	625

Source: ABN AMRO Group Economics

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