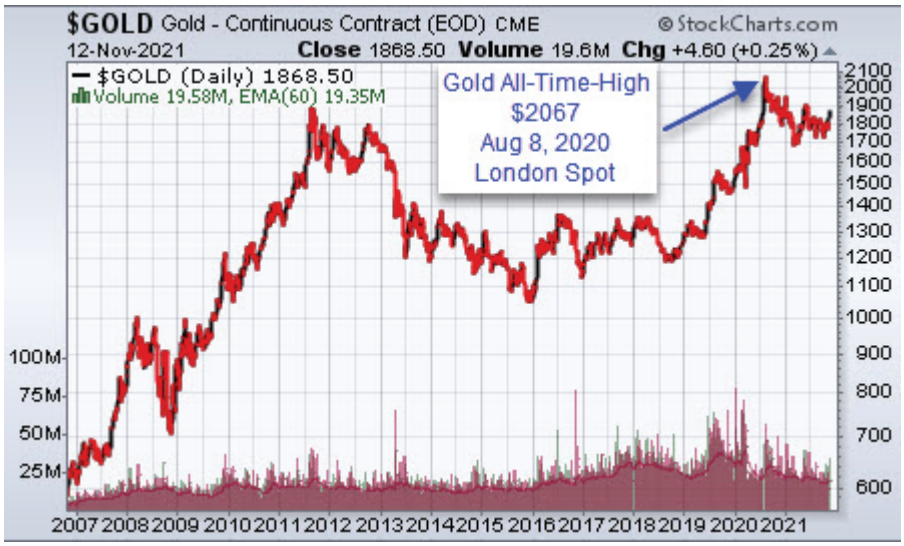
Thackray Report

Gold
Ready to shine?

November 15, 2021 Written by Brooke Thackray

Gold has been out of favor since mid-2020, but is starting to show some life ahead of its strong seasonal period that starts in late December.

Gold peaked in August 2020. Gold has had some ups and downs since last year. After a strong run from last 2018, gold reached an all-time-high of $2067 on August 8, 2020.



Inflation has been rising because of the reckless policy of the central banks and the governments. Together, they have over-stimulated the economy by increasing the money supply at a much greater rate than was required. A lot of investors ask, why has gold remained subdued in this situation?

There are a few theories on why gold has not benefited from rising inflation, including manipulation ahead of Basel III regulations being implemented in London at yearend, or Bitcoin is the new gold etc. I believe that investors have been so focused on buying the momo (momentum) stocks, they have put gold on the back burner. If gold is not moving, why invest in gold? As inflation roars higher, the stock market bounces around at all-time-highs and gold closes in on its seasonally strong period, the time to focus on taking a stake in gold could be fast upon us.

The price of gold is driven by a number of factors and the relative importance of the factors changes depending on the situation. Currently, the real interest rate has been the key driver of the price of gold. The strength of the US dollar has also played a role, but it has not made as much of an impact.

The graph below shows the price of gold versus the yield on the 10-Year Treasury Note versus the USD. It illustrates the different stages of gold's rallies and declines since late 2018. The movement in the yield on the 10-Year Treasury Note is used as a proxy for movement of real interest rates. The stages of comparison are:

❶ In the first stage, the price of gold rallied from just above 1200, to 2067. There are a few wiggles along the way, but generally as the yield on the 10-Year Treasury Note declined, gold rallied. The US dollar did not have a large impact on the price of gold. In 2019, the US dollar was flat. It rallied initially in the pandemic and then moved lower as the economy reopened. When the US dollar moved higher in early 2020, it only had a temporary effect on the price of gold.

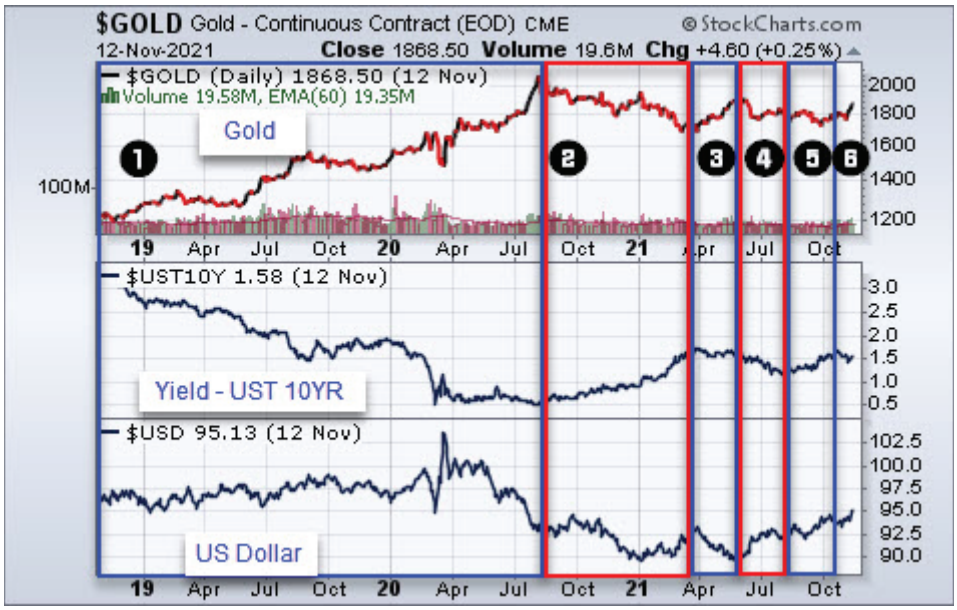
❷ In stage two, gold declined and the yield on the 10-Year Treasury Note moved higher. At the same time, the US dollar moved lower. The move higher in yield on the Treasury Note had a much larger impact than a weaker US dollar.

❸ In stage three, gold moved higher as the yield on the 10-Year Treasury Note moved lower and the US dollar moved higher. Once again, the move in the yield on the Treasury Note had a larger impact than the US dollar.

❹ In stage four, gold declined as the yield on the 10-Year Treasury Note moved lower and the US dollar rallied. In this stage, the move in the US dollar had a greater impact than the move in the yield on the 10-Year Treasury Note.

❺ In stage five, gold was fairly stable as the yield on the 10-Year Treasury Note rose and the US dollar also increased in value. The fact that gold increased in value when its key drivers were trying to push it lower is a positive sign for gold and indicates that the positive sentiment for gold is increasing.

❻ In stage six, so far gold has been rallying as interest rates have been declining and the value of the US dollar has been decreasing. Lower interest rates and investors getting concerned about inflation have helped to push the price of gold higher.

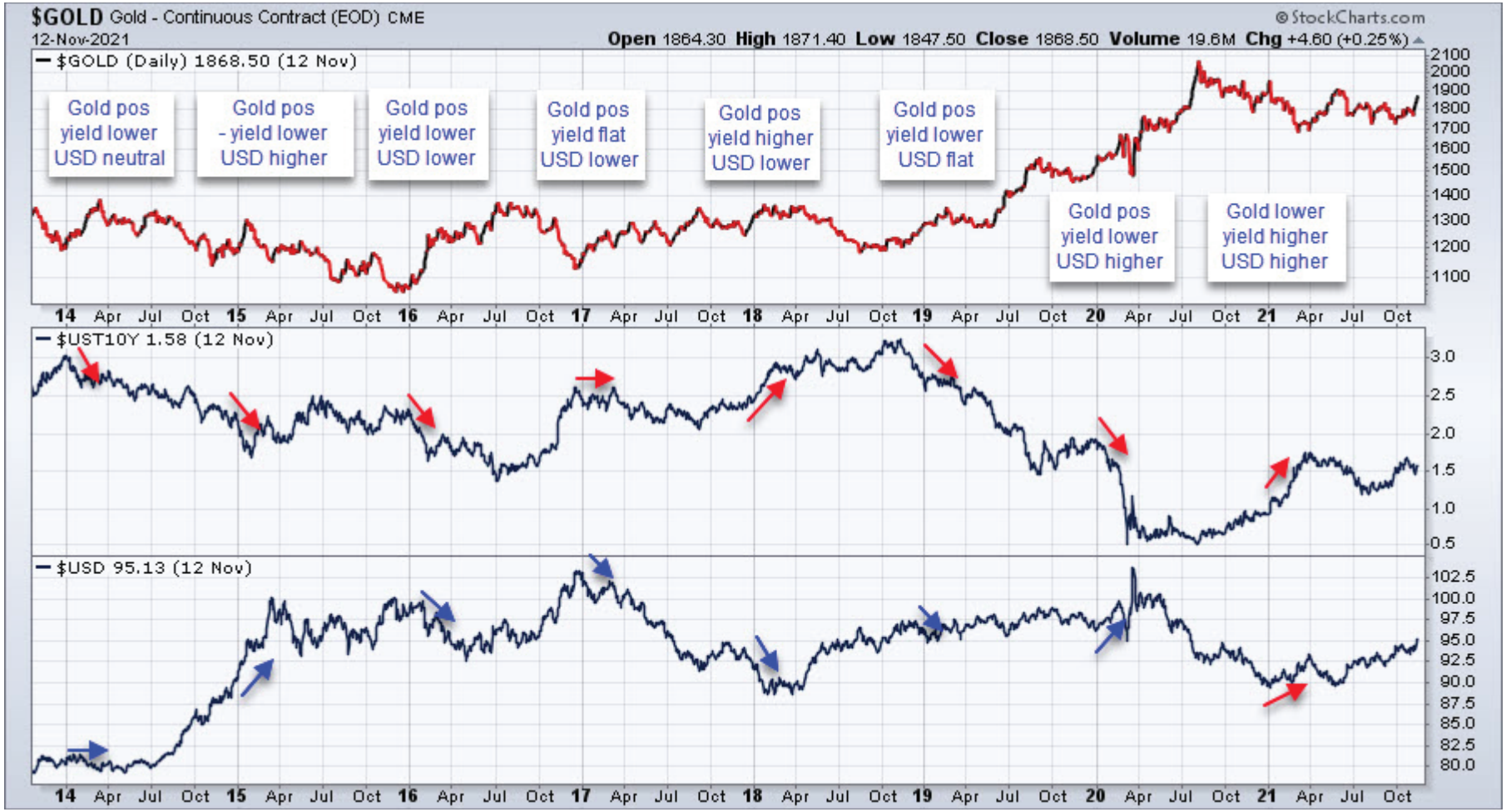


Overall, the graph above illustrates that interest rates are a key driver in the price of gold. The US dollar plays an important roll in determining the movement of gold, but it has not been as strong as interest rate movement. This could change in the future. The movement in the US dollar is becoming more influential, but it still does not have the same impact as interest rate movement.

Gold Q4 Interim Bottoms - 2013 to 2020

Since 2013, gold has put an interim bottom every year in Q4. Although the official seasonal period for gold starts in late December, most bottoms in recent years were created in November. Recently, the price of gold has been rallying on higher inflation than expected.

Gold Performance in January vs Yield on 10-YR Treasury Note vs US Dollar



Gold has been positive in every January from 2012 to 2020 (in 2021 gold was negative in January). January 2021 was the only time that both the yield on the 10-Year Treasury Note was rising and the US dollar was strengthening against world currencies.

Influence of US dollar and Yield on 10-Year Treasury Note

As shown in the graph (Gold Performance in January vs Yield on 10-Year Treasury Note vs US Dollar), gold was able to perform well from 2013 to 2019 in the month of January even when the US dollar or the yield on the 10-Year Treasury Note was rising moderately. When both variables increased in tandem, for example in 2020, gold was negative in January. Investors should monitor the current situation for a rising US dollar and rising yields putting a damper on gold performing well in its strong seasonal period.

Seasonality of gold

Gold has a strong seasonal period from December 27 to January 26. It can extend its run past late January under favorable conditions. The main reason that gold performs well at this time is from increased demand from Chinese buying. In recent years, China has battled India for the largest amount of retail purchases of gold. The Chinese tend to purchase a lot of gold early in the year for gifts, leading up to Chinese New Year. This tends to drive the price of gold higher starting in December and into January.

In the last few years, when gold has corrected in Q4, it has represented a good buying opportunity, mostly in November. This year, gold might have already put in its interim bottom in late September. Nevertheless, a pullback from current levels could still present an opportunity late in the year. Overall, conditions are still favorable for gold at this time of the year.

It is possible for gold to continue to run past the end of its seasonal period in late January, especially if it has support from macro variables such as interest rates declining and/or the US dollar declining.