AGE's Gold Commentary

AGE Gold Commentary is our regular report analyzing trends in precious metals and rare coins. We monitor domestic and international markets and extrapolate from our 30 years in metals to place current events into a hard asset perspective. View archives.

12/9/2019: Gold's quietly spectacular 2019

Source:

Sputtering expansion
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Gold is enjoying a quietly spectacular 2019. Following its breakout to a six-year high of $1,560 in September, the metal has been consolidating gains of 14% for the year so far. It's on course for its best annual percentage rise since 2010, during the throes of the financial crisis.

The main drivers behind gold's remarkable performance have been slowing growth and uncertainty over trade policies, which have combined to stoke demand for safe-haven assets despite the headwinds—and headlines—generated by record-high US stock markets. As a result, bond yields have plummeted as investors worldwide have piled into government securities and gold. We expect these important fundamentals to persist and even accelerate in 2020.

Sputtering expansion

The US economic expansion is sputtering in key areas. Manufacturing has been in outright contraction for the past four months, according to ISM surveys, hitting a 10-year low in September as tariffs and slowing global growth stifle demand for US exports and curtail business investment.

Although it constitutes only 12% of the economy, manufacturing is widely considered the leading forward indicator of economic health. Cyclical in nature, the sector is highly responsive to changes in the outlook for trade, business investment, and corporate profits—all of which have softened this year.

Perhaps more alarming, weakness in factories has begun to spill into the much larger services sector, which is around 77% of the economy. Representing 400 non-manufacturing industries like healthcare, food service, and finance, the ISM services index has slowed in two of the past three months. And while this crucial sector continues to expand, its trend has been sharply lower since hitting a 13-year high in late 2018.

Certainly, the economy had some bright spots this year. The job market has shown remarkable resilience, with a whopping 266,000 new jobs added in November after a couple months of soft hiring. The unemployment rate is down to 3.5%, the lowest since 1969. Consumer spending and retail sales have also been solid, as rising real estate and stock market values create a sizable wealth effect for many American households.

Falling indicators

In fact, consumer spending has almost single-handedly kept the US economy from slipping in into recession. Comprising around 70% of GDP, spending has increased for the eight straight months, including a 2.9% rise in Q3. It's been the main reason GDP growth has held between 2% to 3%, which is considered healthy if not robust.

But household spending has moderated in Q4, in part because of trade uncertainty. And consumer confidence, which projects spending patterns out six months in advance, has fallen for the past four months, according to Conference Board data, suggesting Q1 of 2020 will not be so strong.

Casting a further shadow on early 2020, the Index of Leading Economic Indicators, a weighted gauge of 10 drivers of growth, has fallen for three straight months, posting negative six-month growth for the first time since 2013.

The Fed is projecting GDP growth of 2.3% for 2019, substantially below last year's tax-cut-fueled 2.9% increase and lower than 2017's rise of 2.4%. The Conference Board is projecting 2020 growth at just 2%.

Add simmering trade wars, geopolitical tensions in the Middle East and Hong Kong, Brexit turmoil in the UK and EU, and a tumultuous US election season on the way, and safe havens are looking awfully attractive for 2020.

All these factors are taking their toll on investor sentiment. When overvalued equities finally roll over, and risk appetite turns into risk aversion in a big way, the flood gates will open toward protective assets. Along with government bonds, gold should to be a primary beneficiary.

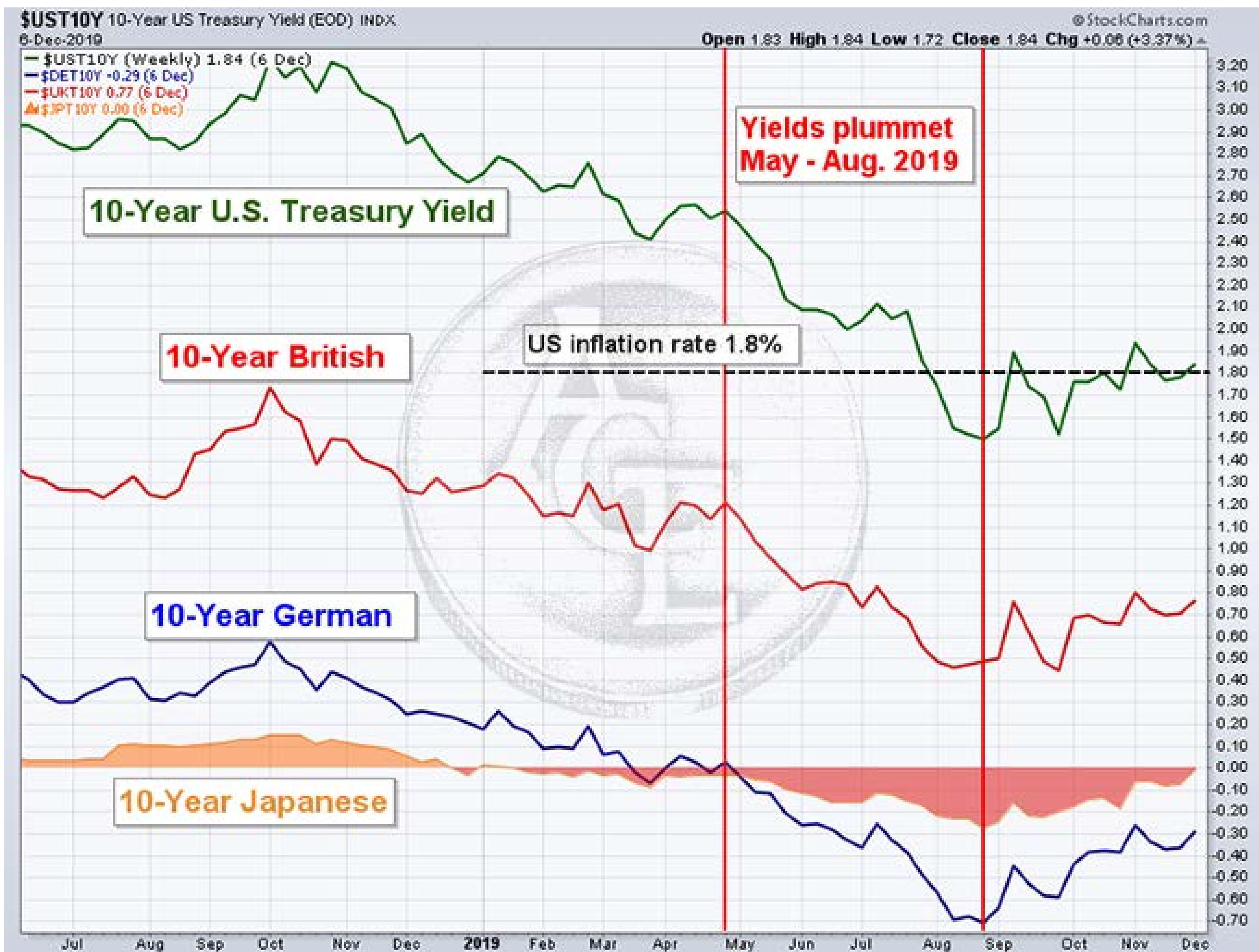
Bullish charts

Bond yields

Plummeting government bond yields were a major catalyst for gold's breakout to new cyclical highs this summer. Simply put, both gold and Treasurys climb a wall of worry. But when yields on bonds fall near or below the inflation rate, gold becomes even more attractive.

With inflation hovering around 2%, bond yields must be 2% or higher for investors to enjoy real returns on their investment. When yields fall below the rate of inflation, real yields become negative.

Gold thrives in a low or negative real yield environment, becoming more attractive than bonds for two main reasons. First, negative real yields reduce the opportunity cost for holding gold instead of bonds, since gold provides no yield itself. So, money that might otherwise move in to Treasurys for safety finds its way to gold instead. Second, gold typically preserves purchasing power by rising with inflation, whereas the value of regular Treasury bonds is eroded by inflation when it begins to accelerate.



If you look at the chart above, you'll see just how far the yields on major global bonds fell from their October 2018 highs to their late August 2019 lows. What started as a decline in October 2018 turned into a rout in May 2019.

As trade wars intensified and the global economic slowdown accelerated, investors rushed to the safety of bonds, locking in the highest yields possible. The more buyers of bonds there are, the lower their yields fall, and this chart reflects that buying surge.

Between May and late August 2019, the US 10-year T-bill yield plummeted 1%, from 2.5% to 1.5%. This is a huge drop in a very short time for the biggest bellwether bond in the financial universe. British, German, and Japanese 10-year notes all fell sharply as well.

The Federal Reserve's abrupt reversal on interest rates further pressured bond yields and boosted gold. In July, the Fed cut interest rates for the first time in 10 years, hoping to inoculate the US economy against fallout from trade wars. Although Fed Chair Jerome Powell dismissed it as "a midcycle adjustment," the cut was rapidly followed by two more in the next few months. Powell recently said rates will stay this low for the foreseeable future.

Lower rates are a very bullish development for gold. They pressure the dollar by making it less attractive to foreign exchange investors seeking higher yield. A weaker dollar, in turn, supports gold and other commodities by making them less expensive overseas. In addition, the rate cuts helped to push yields on government bonds near or below inflation, creating the negative-real-yield conditions that make gold even more attractive.

Since bottoming in August, yields have rebounded somewhat, stabilizing on optimism about a possible US-China trade pact. But yields are still sharply lower than six months or a year ago. Today, the 10-

year Treasury yield is virtually equal to our current rate of inflation, which means no real yield at all, which is a bullish environment for gold.

Gold

Since peaking in early September at $1,560, gold has been in a slow corrective phase as traders took profits from its big run-up. We believe this phase is now ending. Over the last six years, each December has brought profit-taking or speculative selling of gold as traders and hedge funds close out their yearly books. With gold already rebounding off November lows and demand picking up, this traditional year-end selling may have already occurred.

With all the uncertainty afoot in geopolitics and the global economy today, gold has strong short-term support at $1,450. Technically, this was gold's upside resistance level in August before it broke out above $1,550. When markets make such big moves, the previous ceiling often becomes the new floor, and this is what we are seeing in gold. Upside resistance will be found at the 200-day moving average at $1,488, which gold was testing last week. The next resistance level is the short-term top of $1,560.

Moving into early 2020, we see gold trading in a range from $1,475 to $1,550, with the bias to the upside. Gold under $1,500 is a buy in the current market. Under $1,475, of course, it is an even better value.

Silver

After hitting a short-term low of $14.32 in late May, silver surged a whopping 36% in three short months to as high as $19.55 in late August. Since then it has settled into a new, higher trading range of $16.95 to $18.50.

As many of you know, silver is more volatile than gold and tends to overreact at the top and the bottom of its short-term price cycles. Today, the price has been pulled below its recent range by year-end profit-taking, speculation in the futures markets, and hopes for a US-China trade deal. This correction in the silver price is overdone, in our opinion, and has created outstanding value under $16.95.

As you can see on the one-year price chart above, silver was trading in a range from $14.30 to $16.20 for the first half of the year, then jumped to a much higher range from $16.95 to $18.50 in the summer. This sharp surge left a gap in the range from $16.20 to $16.95. Silver fell under $16.95 briefly in November but recent pressure has silver backfilling this gap once again. We continue to see short-term support for silver at $16.60, and major support at $16.20. To the upside we see resistance at $17.60 and again at $18.50.

In November we said, "we would like to buy silver closer to $16.20," but we didn't get the chance. In the current environment, silver under $16.95 looks like a good buy; under $16.50 looks like a great buy. In fact, we think it's only a matter of time until this consolidation phase ends and silver punches back above $16.95 into its higher trading range.

Low premiums on physical gold

As you probably know, demand for physical gold in the US wanes during times of stock market peaks. When demand drops, premiums can fall, and this is exactly what has happened over the last 18-months.

With gold breaking out to new cyclical highs this summer, demand for physical gold surged. Premiums have started to rebound in earnest but remain unusually low for pre-1933 US gold coins, and classic European gold coins. Both sectors offer unusually good opportunities for what we call the "double

play" of rising gold value along with rising collector premiums based on scarcity. Supplies of these coins are limited to what has survived the ravages of time from mintages long ago. Modern bullion coins, by contrast, are minted in virtually unlimited numbers each year and offer no premium for scarcity.

Pre-1933 US gold coins

In classic pre-1933 US gold coins, we continue to advocate the highest quality, lowest premium coins you can buy, with the lowest overall survival rates. We specifically recommend the following coins as the best values for popularity, price, and scarcity in the current market.

$20 Liberty MS64

$20 Saint-Gaudens MS65

$10 Liberty MS64

$10 Indian MS64

Bulk gold buyers looking for lower prices, albeit with less upside potential, should consider the same coins one grade lower. Given previous track records, current pricing, their historical premiums over their intrinsic gold content, all these coins are offering outstanding value today.

Classic European gold coins

For bulk gold buyers we also highly recommend Swiss "Helvetia" 20 franc and French "Rooster" 20 franc gold coins in Brilliant Uncirculated grade. Like their historical US counterparts mentioned above, these trading-sized gold coins have premiums today that are absurdly low. With gold content of just a little less than one-fifth of an ounce (.1867 oz per coin), they are much cheaper per ounce today than their modern bullion equivalents, like quarter-ounce or tenth-ounce US Gold Eagles and Canadian Maple Leafs.

With special pricing on Swiss "Helvetia" 20 francs and French "Rooster" 20 francs, we're offering them at substantially lower premium than the manufacturing cost for those modern fractional coins. For overall value in bulk gold, they simply cannot be beat. While supplies last.

Year-end inventory specials

Finally, as a Texas corporation, we are taxed on our inventory at the end of the year. We would rather pass savings on to you than pay those taxes! For our regular clients, please ask your dedicated market expert what else we can offer that's not on special. For newer clients, you may not realize that only a portion of what we routinely trade is listed on our web site. We have a deeper inventory than you may realize. Again, one our market specialists will be happy to help you with unpublished specials.

In closing, we would like to thank all of you for another great year. We sincerely appreciate your business and the relationships we have built with you over the last two decades.

Happy Holidays and here's to a fantastic 2020!

Sincerely,

Dana Samuelson
President