AGE 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.

10/8/2020: Gold gathers for another surge

In the June edition of AGE's Gold Commentary, we alerted you that gold was poised for a record run above $2,000. In August, the market fulfilled those expectations, with gold setting a series of all-time highs that culminated in a new record of $2,069.

Silver's action has been even more impressive. After lagging gold for much of the past few years, silver surged an enormous 58% between early July and mid-August. Both metals are in strong demand as safe havens, but silver has been additionally supercharged by industrial demand as global economies have begun to recover from COVID-19 lockdowns.

Since then, both metals have corrected lower on profit-taking, which is normal after such epic rises, hitting cyclical lows during September. They have firmed up in recent weeks, but the markets remain volatile as we head into the home stretch of a momentous Presidential election.

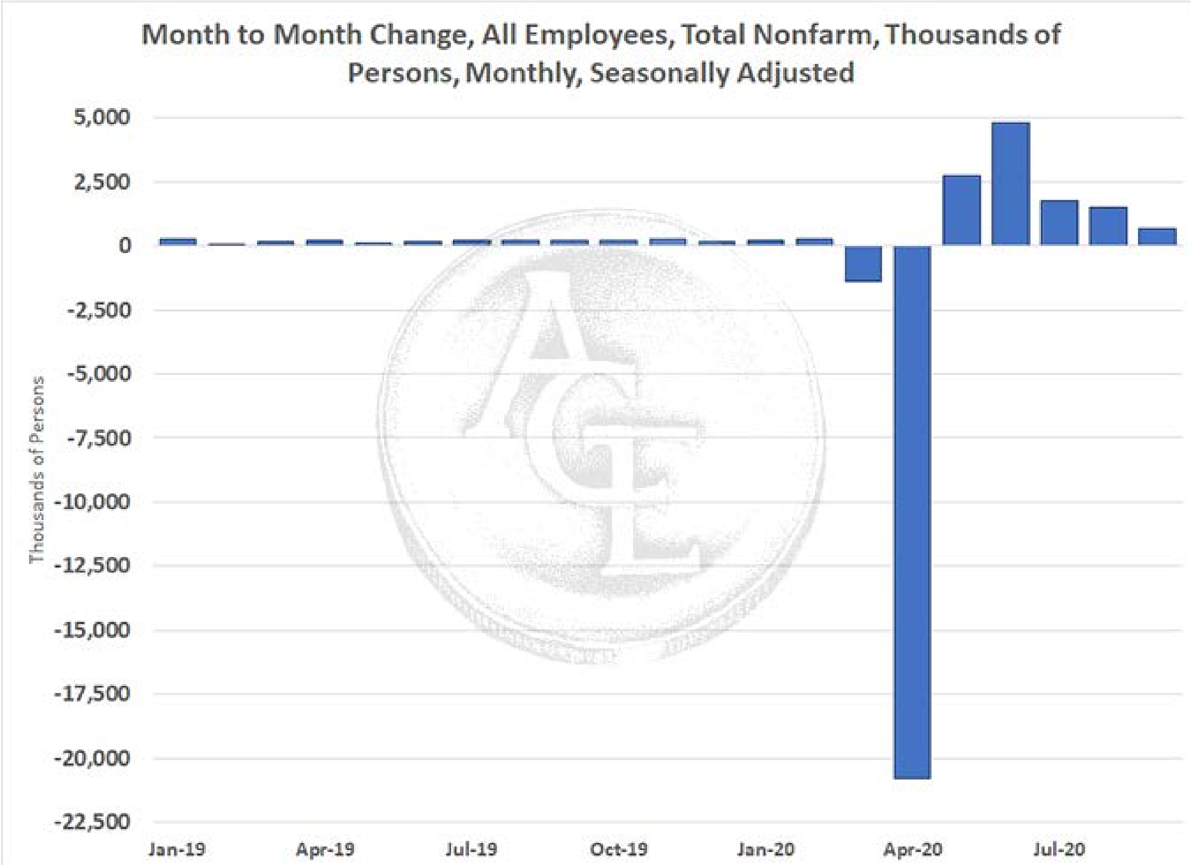
Still, the bullish fundamentals that propelled gold to record highs are very much in place. Unprecedented monetary easing by governments around the world; exploding debt and deficits at home; negative real interest rates; rising geopolitical tensions; and volatile stock markets--all these forces will continue to drive investors into safe havens as this tumultuous year unfolds.

While gold may seem expensive at current levels, it has the potential to move substantially higher. We believe gold is gathering itself for another surge and could easily push into a trading range of $2,200 to $2,500 within the next six to twelve months.

Slowing recovery

The US economy has improved substantially since the spring when government-imposed shutdowns triggered the deepest economic contraction since the Great Depression. Manufacturing, retail sales, consumer spending, and the housing market have all rebounded remarkably. But the momentum of these gains is slowing, and overall activity remains stuck at around 80% of its pre-pandemic level, according to most metrics. Meanwhile, the coronavirus rages on.

Perhaps the single most-important measure of economic health is job creation. While the labor market enjoyed sharp rebounds in May and June after the staggering loss of 20.7 million jobs in April, the pace of gains has steadily declined since. The government's Nonfarm Payroll Report for September showed 9.37 million people who had jobs in February remain out of work today because of COVID-19.



And the layoffs keep coming. Disney is cutting 28,000 jobs. Allstate, the nation's fourth largest insurer, is reducing its workforce by 8%. Royal Dutch Shell is laying off 9,000 workers. United Airlines and American Airlines have both said they will furlough or eliminate a total of 31,000 employees if they do not receive another government bailout, and soon. The Regal movie theater chain just announced they are shutting down all their 536 locations and furloughing roughly 40,000 employees. Many of these are likely to be permanent job losses, all announced in just the past two weeks.

And small businesses are suffering even more. According to Yelp, permanent business closures have surged from about 40,000 in March to almost 70,000 today.

Monstrous debts and deficits

Congress has flooded the economy with $4 trillion in aid, but it has not been enough, and consumers are starting to feel the pinch. Once Federal unemployment support of $600 per week ended in July, personal income dropped 2.7% in August. Meanwhile, savings has turned sharply negative, indicating consumers are supplementing lower incomes by dipping into savings. With consumer spending accounting for roughly 70% of GDP, this trend is unsustainable for economic growth.

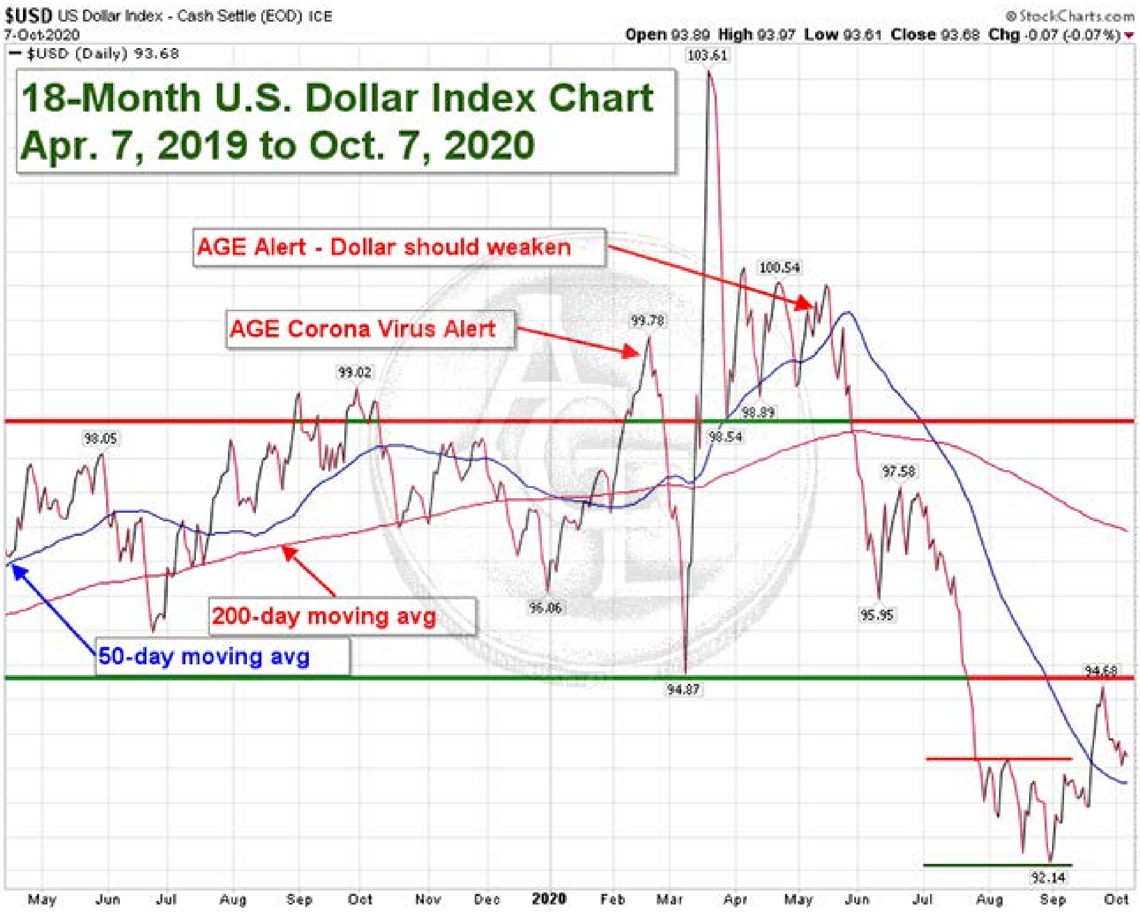
It will probably take years for the economy to recover fully from COVID-19, just like it did after the financial crisis of 2009. Now as then, the debt and deficits we incur to mitigate the damage will take even longer to be overcome. Large deficits typically create headwinds for GDP growth and can undermine investor confidence in the US. This kind of change in sentiment is ultimately reflected in the value of the dollar, and that is bullish for gold in the longer term.

Let's look at the charts.

US Dollar Index

As you can see in the US Dollar index chart below, the dollar plummeted and then rebounded in March as COVID surged and the economy went into lockdown. We saw a similar knee-jerk low and then high in the dollar in 2009, as the global financial crisis unfolded.

The initial reaction following a sudden shock is to sell everything, creating an initial downdraft in most markets. Afterwards, value buyers can bid the markets back up. But more importantly, money from weaker economies can pour into the US seeking safety. When foreign investors seek haven, primarily in US government bonds, they must first buy dollars. This transactional demand is what created the rebound spike in the dollar in 2009 and again in 2020.



After the March spike up to 103.61, the dollar corrected lower as the economic damage caused by shutdowns in April and May steadily increased, undermining our economic fundamentals. We anticipated back in May that the US economy would likely underperform for a while, which was why we said in our mid-May Gold Commentary that the dollar would weaken. Indeed, the dollar plummeted--from just over 100 in mid-May down to the bottom of the chart at 92.14 in September.

The buck's recent rebound to as high as 94.68 reflects another wave of foreign investment as the pandemic re-emerged in Europe in September. But the bounce has been relatively short-lived, as COVID-19 has started resurging here, too. The dollar has declined from its short-term high of 94.68, which coincides with the upside resistance red and green line on the chart. The most recent dollar weakness buoyed the gold price back above $1,900 over the last two weeks.

Technically, the dollar will encounter upside resistance at just under 95, at the major green and red support/resistance line, and enjoy major support at 92, where it found support in early September. If the dollar breaks below 92, it should find technical support at 88.50. A break below 88.50 could take it substantially lower. It all depends on the relative strength or weakness of the US economy going forward.

Gold

The gold market has been turbocharged by dollar weakness since early July. As the dollar fell precipitously from just over 97 in early July to under 93 in early August, gold surged from just under $1,800 to its new all-time high of $2,069 in early August, as you can see on the chart below.

Profit-taking then pressured gold into a lower trading range of $1,925 to $1,980, where it held until mid-September, when the dollar's rebound pushed it below its 50-day moving average. This move under the 50-day moving average increased the technical selling pressure on gold, pushing it from $1,940 to as low as $1,866. Once again, though, the dollar weakened, and gold rebounded over $1,900.

In the short-term, gold remains in a downtrend, as indicated by the parallel blue lines on the chart, holding in a range from $1,870 to $1,925. A move above $1,925 will meet resistance at $1,950, the 50-day moving average. A push past $1,950 will mean the current correction is ending. If gold falls below support at $1,870, the next level of major support is $1,820.

It bears repeating that the three primary drivers of higher gold in today's market are negative real interest rates, surging US debt and deficits, and weakness in the dollar. All three have room to drive gold substantially higher in coming months and years.

While nominal interest rates are theoretically already almost as low as they can go, real interest rates (that is, adjusted for inflation) could fall further into the negative, especially if the overvalued stock markets falter and bonds rally hard again. Negative real rates are bullish for gold because they remove the opportunity cost for holding the metal instead of bonds.

Our national debt will certainly continue to climb at an abnormally high rate, accelerated whenever the next stimulus bill is passed by Congress. Fed Chair Powell warned this week that the US faces a weak recovery without sufficient government aid and that too much stimulus would not be a problem. That means cheaper money is coming.

And the dollar is therefore precarious. Deeper easing by the Fed would further debase the currency, potentially driving investors elsewhere. More fiscal stimulus could have the same effect. At certain point, the ever-expanding debt could raise questions about the government's ability to meet its obligations--and by extension, the dollar's fitness to be the global reserve currency.

Add in trade tensions with China, tumultuous domestic politics, and the uncertain course of the pandemic itself, and gold has seldom been in a better position to fulfill its traditional role as currency of last resort.

Silver

After lagging gold in price appreciation from the summer of 2019 until July 2020, silver played catch up with a vengeance this summer. The metal gained an astonishing 58% in July, surging from $18.50 an ounce to as high as $29.26 an ounce in six weeks before hitting price resistance.

Since that peak, price action has been choppy and volatile as silver oscillated between $26 and 28.50 an ounce. As many of you know, silver is more volatile than gold, and tends to make bigger percentage moves. Silver has clearly lived up to this reputation over the last several months.

When any market moves so far so fast, it is bound to encounter pressure from speculative profit-taking. So, when silver stalled in mid-September at $28.65, selling pressure ramped up, driving it sharply down to $23 before support was found. This profit-taking coincided with dollar's rebound. Since then silver has settled into tighter trading range of $23 to $24.50, largely tracking with gold's inverse relationship to the dollar.

When both gold and silver make big moves higher, they tend to take two steps forward and one step back. Silver's recent pullback to just above $23 is a clear example.

In the short term, if silver can breach resistance at $24.50, it will find upside resistance at $26. Support is at $23, and below that, at $21. Given the market fundamentals we've been discussing, a sharp break lower is unlikely. We would view silver under $23 as a major buying opportunity.

Modern Bullion

We are happy to report that, after the most extreme supply squeeze in 10-years, gold and silver bullion coins and bars are flowing again from world mints and private manufacturers. Still, production at the various mints remains somewhat inhibited by COVID-19. Social distancing is difficult to achieve in these facilities, and supply lines can still be interrupted with no advance notice.

As a result, coins and bars are shipping immediately but premiums remain somewhat elevated. Premiums for gold bullion are 0.5% to 1% higher than pre-pandemic while premiums for silver are $0.50 to $3.00 per ounce higher than normal, depending upon the manufacturer.

Adding to the potential for disruption, the end of the production year is approaching, when mints will cease making 2020 coins and prepare for the 2021 issue. This transition can create a production hiccup of anywhere from two weeks to a month, depending upon the mint. If another demand surge occurs during the transition, premiums and delays could easily ramp up once again.

We highly recommend that you take advantage of today's lower gold and silver bullion prices and near-normal premiums to add to your positions. Remember, Chairman Powell said more stimulus is better than less stimulus. This means more money printed out of thin air, and debt that just keeps growing.

Pre-1933 US gold coins

The surge in gold has lifted premiums on pre-1933 US gold coins from all-time lows back towards their 10-year moving averages. The double-play of rising intrinsic metal value and rising collector premiums has paid off handsomely for our customers. We actively placed as many classic, pre-1933 US $20 and $10 gold coins as we could over the last several years, expecting this outcome. Thank you to those who took our advice, and congratulations.

But there are still plenty of good values to be found in this sector. With the gold correction over the last six weeks, premiums have relaxed a bit in some areas. Supply lines have been somewhat refilled after being severely constrained in August due to demand completely overrunning existing market supplies of these vintage, limited availability coins.

For more speculative buyers we recommend $20 Liberty MS64 and $10 Indian MS64. These coins are far scarcer than most others overall and they are leading the numismatic market higher. This scarcity provides greater leverage to the market when demand is high. In fact, their premiums have been consistently expanding since March 2020 from all-time lows, and they still have plenty of room to rise.

A true sleeper today is the $10 Liberty in MS65 grade. This is by far the scarcest of the gem-quality $10 and $20 gold coins. Why it is being overlooked in the current market is anyone's guess. This coin is a contrarian's dream today.

For more conservative buyers, we recommend $20 Saint-Gaudens MS64 and $20 Liberty MS62. These coins track more closely with the gold price, yet their scarcity gives them additional leverage that gold bullion cannot offer. Gold's price corrections over the past month have compressed their premiums again somewhat, making them two of the best values for bulk buyers in the current market.

AGE is the only company that regularly analyzes, updates, and publishes price and premium charts for pre-1933 US gold coins on the web. Our inhouse analyst and senior account manager, Matt Warden, has done a remarkable job of picking the best of the best values in pre-1933 US gold coins each month. We are all grateful for Matt's excellent work.

That's it for now. Please stay safe!

Sincerely,

Dana Samuelson
President

P.S. -- AGE will once again be attending and participating in the annual New Orleans Investment Conference next week, only it will be virtual this year. If you want to see who will be presenting, and it is an impressive list of speakers, below is a link with all the information. And you can watch the entire conference from the convenience of your own home or office.

I'll be on the Precious Metals Panel and will also be giving a gold market update.

2020 New Orleans Investment Conference