Metals Strategy: Gold Floors & thinking (part 2)

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Part 1 provided a quick update on the macro-economic backdrop as it relates to the monetary/fiscal policy response & the fluid global growth profile. Metals Strategy Macro Update And Floors-17032020.pdf

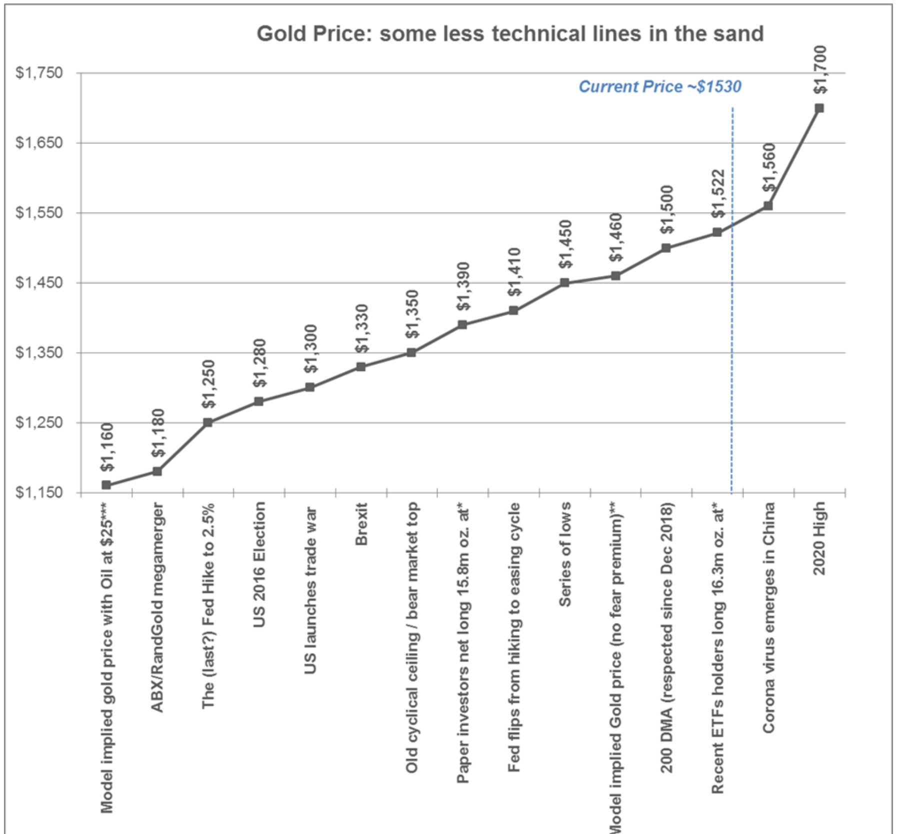
Part 2 below applies that new thinking to Gold and outlines some price levels and positioning.

- The recent aggressive global CB action ensures a stronger and more bullish longer term platform (Gold should wake-up to the impending global over indebtedness, restrained growth, more experimental CB polices and income supporting programs / helicopter drops resulting in dilutive currencies and historically low real rates). The stimulus backdrop has emerged the past few days and is growing, but the greenlight needs to stem from a reduction in panic selling across all assets, a dial back in peak fear (which is contingent on US' case numbers/flattening the curve); **Golds' goldilocks is mild equity volatility / macro fear, not Armageddon.**

- **This recent peak-to-trough price action - capitulating $250 in days, alongside risk, highlights the similarities to 2008, in which broader liquidity/credit issues and largescale wealth destruction are much larger than golds fundamentals** *(which are currently very weak with physical dialing back and CB demand potentially reducing their pace of buying, or selling).* Despite the numerous calls for Gold to act up as a fear hedge (which its done but failed to hold), past historical analysis helps explains why Gold will perform *relatively* well, but it will be tough for it to diverge and breakout on *extreme* equity volatility and oil flush outs. See Februarys Metals Note outlining 5 core reasons which all still apply and the Oil vs Metals Note.

- Chart 1 below outlines some 'less technical' price points to consider. **The recent tentative hold around $1450 is a constructive development, perhaps marking that the indiscriminate selling is nearer the end,** at the very least some decent buying & conviction has emerged. And while Gold remains a liquidity asset that is still vulnerable to an evolving health & economic crisis and contingent on where risk and credit markets are heading (chart 2 matches up 2008 price action vs COVID price action), **fair prices should be HIGHER than before COVID-19 emerged, i.e.: above $1560 in medium-longer-term.**

Chart 1:



* weighted average price, net COT managed money and ETF investors who added to Gold holdings since the collapse of trade agreement (May 2019), are long at
** See Gold Fear Premium Regression results as of March 17 2020
*** See Oil vs Metals note dated March 11 2020
Source: Bloomberg, Scotiabank Commodities Strategy

Chart 2:

Source: Scotiabank Commodities Strategy, Bloomberg
GOLDS Comdty (GOLD SPOT $/OZ) COVID vs 2008 Daily 15JUL2008-31DEC2010 Copyright© 2020 Bloomberg Finance L.P. 17-Mar-2020 13:40:43

- Similarities to 2008 are correct in that Gold hasn't reacted as safehaven but rather any traditional source of liquidity; however theres better economic similarities to the sudden economic stop of 9/11 (2008 was a financial crisis, not a sudden-stop shut-in of global activity). Regardless, graph 2 aligns Golds peak in summer 2008 to the current $1700 **highlighting a short-term warning sign IF risk markets deteriorate much further (unlikely given proactive stimulus measures!) → Golds current unwinding is only ~1/3rd of what it did into Lehman; a 30% decline from $1700 puts pricing at $1240.** Positioning also shows that ETF and COT investors together own 107m oz (which is currently a lot cleaner given the $250 unwind but data is COT data is lagged and ETF data arguably stale); that is over 2x the leverage/firepower of positioning exhibited in 2008, in which over 15mn oz (or 30% of total positioning) was offloaded. *We will update positioning similarities on Friday in which nos will be a lot more insightful.*

Chart 3:

		Gold		
	Net COT Contracts	**ETF oz**	**Net COT oz**	**Total oz**
3/10/2020	210,185	86,939,008	21,018,500	**107,957,508**
COVID positioning > GFC positioning				**2.2x**
GFC				
7/15/2008	168,906	31,522,515	16,890,600	48,413,115
9/15/2008	44,367	28,513,068	4,436,700	32,949,768
Difference	(124,539)	(3,009,447)	(12,453,900)	(15,463,347)
% Change	-73.73%	-9.55%	-73.73%	-31.94%

Chart 4:

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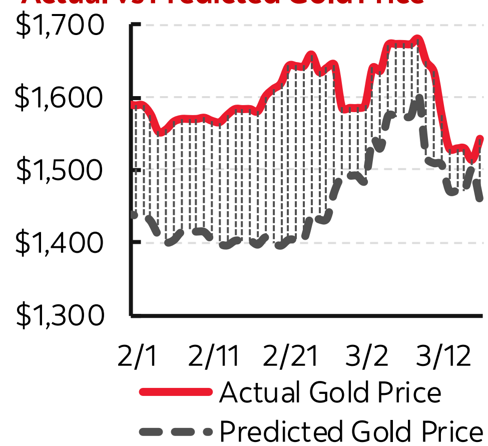
Gold Fear Premium Daily Report

Tuesday, March 17, 2020

Regression Results			Current Prices		
Intercept	$	2,218	Gold Price	$	1,543.51
US10Real	$	(227)	US10Real	$	0.10
DXY	$	51	DXY	$	99.69
USDJPY	$	(14)	USDJPY	$	107.27
USDEUR	$	(4,324)	USDEUR	$	0.91
USDGBP	$	(367)	USDGBP	$	0.83
R Squared		83.83%			

Actual vs Predicted Gold Price



Source: Scotiabank Commodity Strategy (Metals), Bloomberg

Predicted Prices & Premium		Prediction Share Of Estimate	
Gold Price	$ 1,458.03	Intercept	152.13%
Fear Premium	$ 85.48	US10Real	-1.48%
		DXY	346.63%
		USDJPY	-105.99%
		USDEUR	-270.39%
		USDGBP	-20.91%
		Total	100.00%

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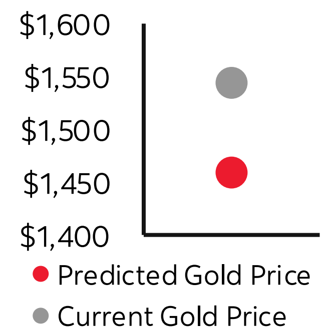
Prices as of 17-03-2020

Fear Premium



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