Macro Market Insights

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Sizing Up Gold's Rally

Gold had its best single day performance since September of 2013 on Thursday of this week. It begs the question, what contributed or led to the 50-dollar rally as it was not triggered by a single piece of economic news, geopolitical action, or policy announcements. One thing that is clear, however, is there has been a shift in investor sentiment and speculators no longer feel as comfortable with their short positions in the futures market. The advances on Thursday, made largely on the back of technical trading confirm this.

Wednesday brought the typical FOMC announcement, to which gold coincidentally has become accustom to not react to. It was perhaps Janet Yellen's comments during her press conference later on Wednesday that pre-empted the weak dollar trade that in turn was positive for precious metals. Despite the Fed continuing their pace of tapering their monetary stimulus, it was the outlooks for the Fed Funds Rate that were analogous to comments from the IMF earlier last week, that low rates will ensue until at least the beginning of 2017.

The closest piece of contradictory evidence to this is that North American economies, particularly the US and Canada, are beginning to see signs of inflation. Still nowhere near levels that would prompt policy response as of yet, but it's been the lack of inflation that's been the concern of both Bank of Canada and the US Fed, thus these drastic upticks have caught their attention. To give context, in the US, core inflation has been 2 per cent or above in 10 of the 65 months since the recession of 2008. A few consecutive months like we've seen certainly don't make a trend; it's the fact that key components like rising food and energy prices could very well be sustained.

And it is the rise in energy prices, triggered by geopolitical concerns that have been another positive for gold. Tensions around violence in Iraq have investors worldwide keeping a close eye on crude oil prices. As crude prices elevate to higher levels, consumers face higher energy costs and that means less expenditure elsewhere. Gold once again is participating in a fear trade, which history tells us in not usually sustainable for the market on its own, but paired with other factors could be a different story.

The materialization of an increase in the rate of inflation (which investors who questioned the Feds experimental policies have been waiting for since the onslaught of quantitative easing) provides support for metal prices in here. The question becomes will it last, or once again be more transitory in nature.

It's difficult to try and forecast this rally and the strength and breadth of it. But one thing is for sure, the move in gold this past week was impressive, and if conditions continue to manifest as they were, this rally could be for real.

As per usual, it's a wait and see game.