Macro Market Insights

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Robert Levy
MA (Economics)
Director
rlevy@bordergold.com
(604) 535-3287
www.bordergold.com

Global Slump

There have been an increasing number of factors that have begun to put pressure on global financial markets. Just over the past week the International Monetary Fund once again revised lower their outlook for growth, and cited that the global recovery was relatively uneven between different geographic regions. This triggered yet another down move in energy markets, which translates to pressure on a number of smaller commodity based economies (like Canada) and emerging market economies. As well, the Fed released minutes from their September meeting midweek and cited concerns over a stronger US dollar, which led investors to briefly question the timing of the Fed’s tightening schedule. Finally, manufacturing data out of Germany signalled the Eurozone’s perhaps only remaining beacon of light may too be headed for recession.

The aforementioned reasons could all be factors that three years ago would be used to explain higher gold prices. That they are not today gives reason to believe that there will remain attractive buying opportunities in the months to come. Ultimately investors’ appetite for precious metals is not yet there. Gold, as we have witnessed, is not performing as its typical safe haven asset for capital, and part of the reason may still be tied to a loss of confidence following a year when the asset class of precious metals were nearly decimated and gold lost close to 30 percent. In a global environment where investors where holding gold for its relative stability, this traumatizing event would inevitability lead many to seek a safe harbor elsewhere.

The forward looking question though is can gold outperform the US dollar? As the IMF outlines in their most recent report, we remain in an unbalanced global recovery. As North American economists look to whether the US and North American economies can “go at it” alone, with 60 per cent of US exports destined for Canada and Mexico, the IMF, with a more international focus, is left to ponder whether US growth is strong enough to support the rest of the world. The scenario though with the United States acting as the leader and the first to step forward from accommodative monetary policy is the reason for the US dollar strength.

As we witness outside the US, Europe is at a near standstill and recent data seems to point to being on the cusp of a German recession. Brazil, who was once the poster child of the emerging market economies (the B in BRIC) is ahead of Germany now actually in a recession. Analysts continue to call for a slowdown in China as their GDP growth retreats from once double digits to below 7.5 per cent. Passing on the debate of whether the landing will be soft or hard, their demand for the world’s resources at this point seem to be tapering off. This leads to commodities. We remain plagued with the uncertainty of where this global supply glut can meet a slumping demand.

Gold cannot behave like a commodity forever. Unfortunately, it seems it will until investor confidence is restored in its ability to act as a relatively stable asset that’s uncorrelated with most other markets, making it that ideal hedge. And as has been most often the case with the precious metal, its shine is revealed after its bigger moves rewarding those already holding it. Right now, however, it maintains it’s near perfect negative correlation to the US dollar, and any dollar strength is inevitability bad for gold in the near term.

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Happy Thanksgiving to our Canadian customers!