Degussa Market Report

17 August 2018 Economics · Finance · Precious Metals

USD per ounce of gold

USD per ounce of silver

EURUSD

Source: Thomson Financial.

Precious metals prices				
	Actual (spot)	Change against (in percent): 2 W	3 M	12 M
I. In US-dollar				
Gold	1.174.0	-3.2	-8.1	-9.1
Silver	14.6	-5.2	-11.1	-14.0
Platinum	774.5	-6.3	-12.1	-17.2
Palladium	883.5	-2.9	-10.8	-3.0
II. In euro				
Gold	1.031.5	-1.6	-6.2	-4.6
Silver	12.8	-3.6	-9.2	-9.7
Platinum	680.7	-4.9	-10.0	-13.3
Palladium	776.0	-1.5	-8.8	1.4
III. Gold price in other currencies				
JPY	130.088.0	-3.6	-7.9	-10.4
CNY	8.088.8	-2.4	-1.7	-4.9
GBP	922.5	-1.1	-4.4	-2.9
INR	82.297.0	-1.0	-5.3	-1.6
RUB	78.313.6	2.0	-3.3	4.7

Source: Thomson Reuters; own calculations.

OUR TOP ISSUE

This is a short summary of our fortnightly ***Degussa Marktreport****.*

US Dollar and Gold – Is This Time Different?

On 13 August 2018, the price of gold fell below 1.200 USD/oz, declining to a 1.5 year low. What to make of this move? It seems that several factors have been at work in triggering the gold price decline. At the same time, it does not seem too far-fetched to think that the current market price of gold is now well below its *true value*, and so the chance for the gold price to go up outweighs the risk of a further drop by quite a margin. Here is why:

Given recent market uncertainty – amongst other things due to the Turkish Lira crisis and other emerging market currencies being affected by the turmoil – investors have substantially increased their demand for the Greenback. It does not only serve as a "safe haven" currency, but it also offers a positive interest rate (e.g. 2-year US bills offering a yield of around 2.6 per cent). In the international context, this is a rather attractive combination from an investor's point of view.

What follows is an appreciating US dollar and – as its flipside – a decline in the price of gold in US dollar terms. In fact, investors seem to be convinced that the Greenback is the currency to hold, and that the US dollar can outshine the 'gold currency'. This, however, appears to be a questionable proposition. For the end of the Fed's hiking cycle might be closer than the market expects. The reason lies in the growing international US dollar indebtedness.

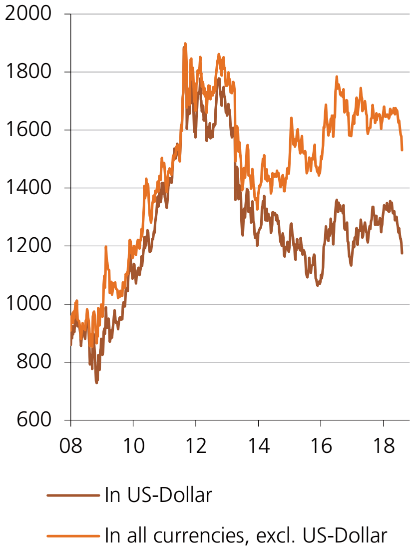
In the period of extreme low US interest rates, many foreign borrowers – in particular, those from emerging market economies – have taken on US dollar denominated debt. An appreciating US dollar causes them quite some trouble: It increases the costs of serving their debt. What is more, it makes rolling-over maturing US dollar debt more difficult: Lenders become hesitant to renew loans, and if they do, they can be expected to charge higher interest rates.

Deterioration in credit availability and the cost of funding undoubtedly has the potential of unhinging the credit-driven boom in many emerging market economies. This, in turn, is most likely to also have negative consequences for the developed economies around the world, including the United States of America. To cut a long story short: It seems that the Fed's room for manoeuvring is quite limited, much more constrained than many market observers might expect.

Due to the high dependence of many economies around the globe on the US dollar, the Fed can no longer gear its monetary policy to the needs of the US economy alone. It can no longer ignore the consequences its monetary policy is most likely to have on other economies around the world. While the US economy may well need higher interest rates, many countries will have significant problems coping with US borrowing costs going up.

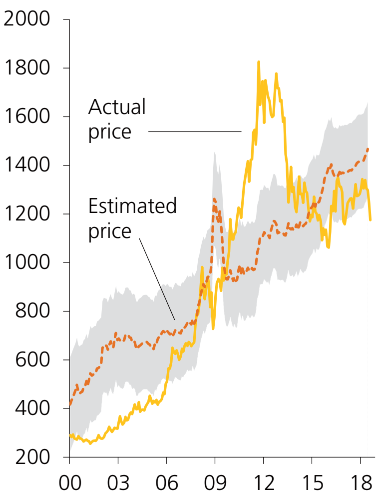
As soon as the financial markets find out that the Fed cannot continue its US economy-centred monetary policy, there is a decent chance that the reserve currency status of the US dollar will be critically reviewed. Because the question is:

Gold price per ounce
in US dollars and all world currencies (excl. the US dollar)*
January 2008 to August 2018



Source: Bloomberg; own calculations. *Calculated from the gold price (USD/oz) and the nominal trade weighted exchange rate of the US dollar. The timeline was indexed at 5 September 2011 with a value of 1.900.

Current gold price is well below its ‚estimated value'
Gold price (USD/oz), actual and estimated [1]



Source: Thomson Financial; own calculations. [1] Period: January 1972 to July 2018. Explanatory variables: US money stock M2, US short-term real interest rate and corporate credit spread. Grey area: standard error.

What does it mean if the Fed's monetary policy has to increasingly factor in the financial and economic needs of the 'global economy'? The answer? The currently unshakable belief in the Greenback's safe-haven status will lose some of its shine.

The Fed's monetary policy would become, more than ever, a 'bail-out policy' for the rest of the world, that is coming to the rescue of foreign borrowers who have overstretched themselves by taking on US dollar debt. Printing great amounts of money and providing it at artificially low interest rates would become the hallmark of the 'new Fed policy'. Hardly an outlook to inspire investor confidence in the Greenback's store of value function.

In fact, the current inflow into the US dollar seems to disregard the consequences this will have on the international credit system and, as a result, the Fed's monetary policy. The uncomfortable truth is that keeping the global credit system going, the Fed will have to churn out more fresh money, provided at artificially low interest rates.

Now you may ask: What is going to happen if the Fed ignores the consequences its policy has for much of the rest of the world? If it keeps raising interest rates according to the needs of the US economy? Well, the 'day of reckoning' would presumably not be long in coming. If the Fed's monetary policy tightening tanks the boom of other economies around the world, the US economy is unlikely to escape the mess – and the Fed will have to reverse course.

Against this backdrop, investors are unlikely to get happy betting on the US dollar as the one and only 'safe-haven currency'. In fact, from the viewpoint of the savvy investor, the 'gold currency' will have a role to play because the purchasing power of the yellow metal cannot be debased by central banks' monetary policy. On top of that, gold does not carry a default- or credit-risk as time and savings deposits undeniably do.

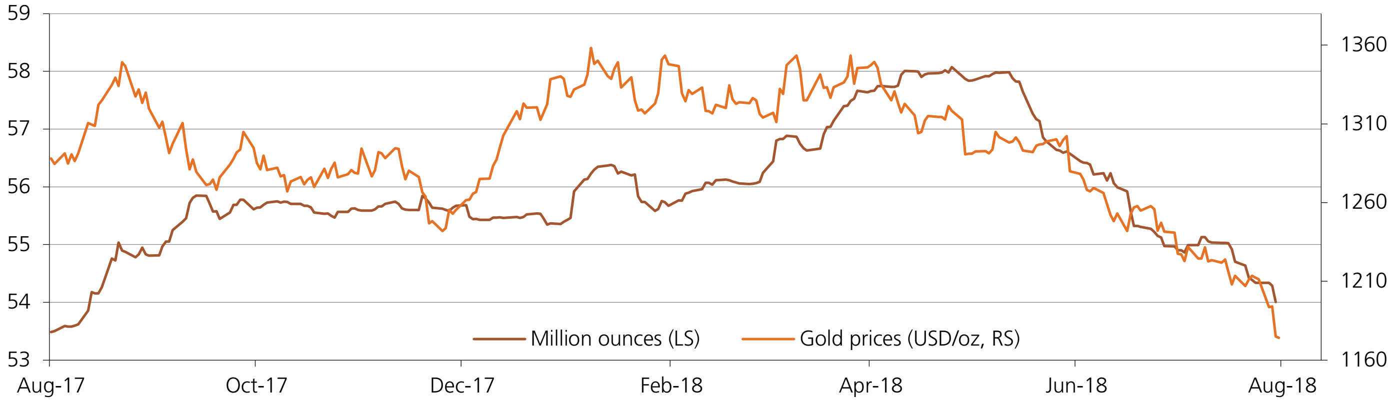
Current price action in financial markets clearly suggests that investors do not fear inflation or systemic default risks. This, however, appears to be grossly underestimating the true risk profile in the global credit and monetary architecture and it may well explain why there has been a sell-off in gold in recent days. However, there are good reasons to conclude that the sell-off has gone too far and that it has pushed the price of gold well below its 'true value'.

In other words, gold has become cheap (and undeservingly so) – which might be painful for those currently holding gold but offers an excellent opportunity for those who want to build up their gold positions. In any case, it appears that we are right in the middle of a situation in which market prices do not reflect 'true values': The stock market seems to be expensive, and gold is too cheap. And history taught us that over- and undervaluations will be corrected over time.

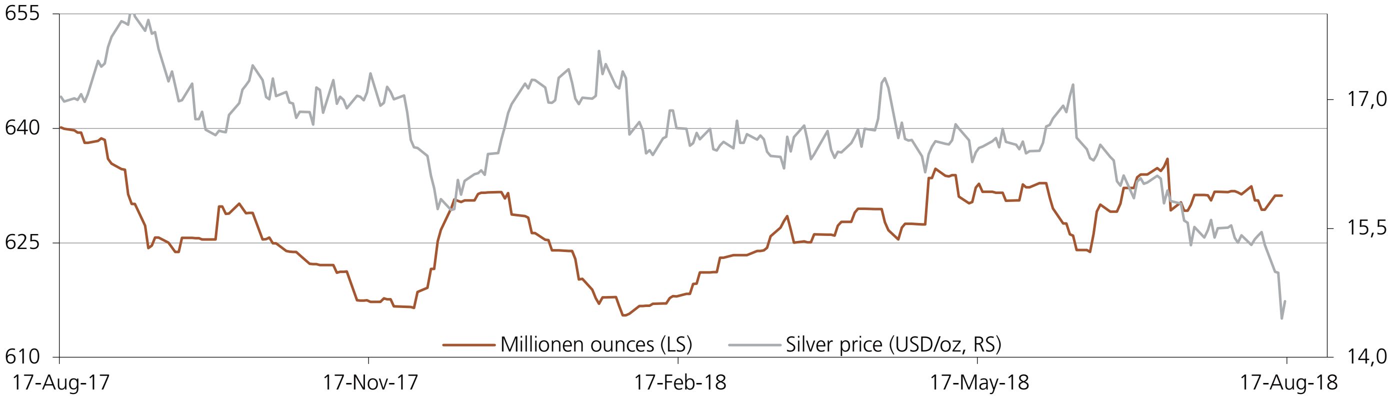
This brings us back to the relation between the US dollar and gold. We might have entered a phase in which the US dollar – an unbacked paper currency – is no longer, and for political-economic reasons can no longer, serve as the world's only reserve currency. If this assessment is true, or even half-true, going forward, the price of gold can be expected to move higher by quite a margin; perhaps much higher than most people expect under current conditions.

Precious metals prices and ETF holdings

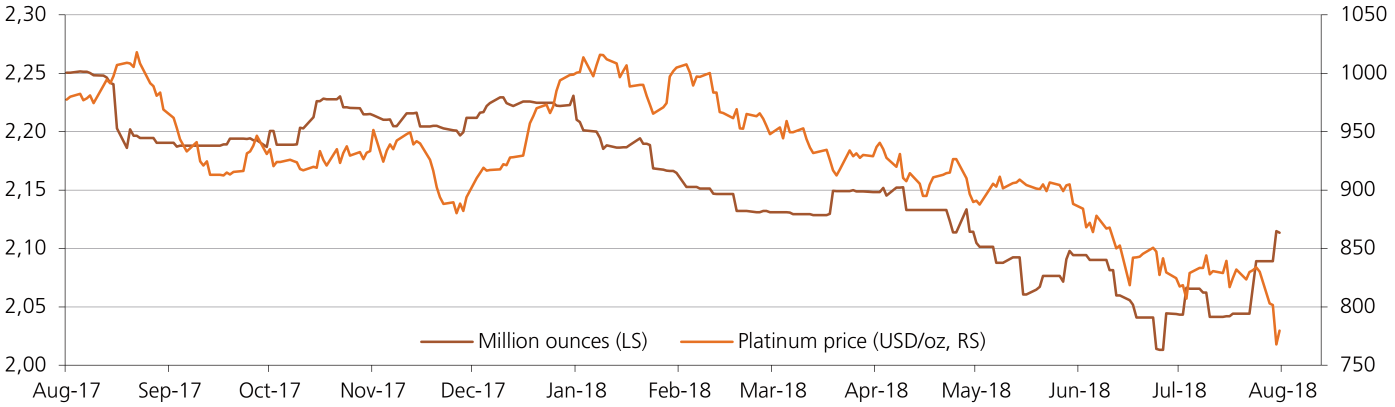
Gold ETFs (million ounces) und gold price (USD/oz)



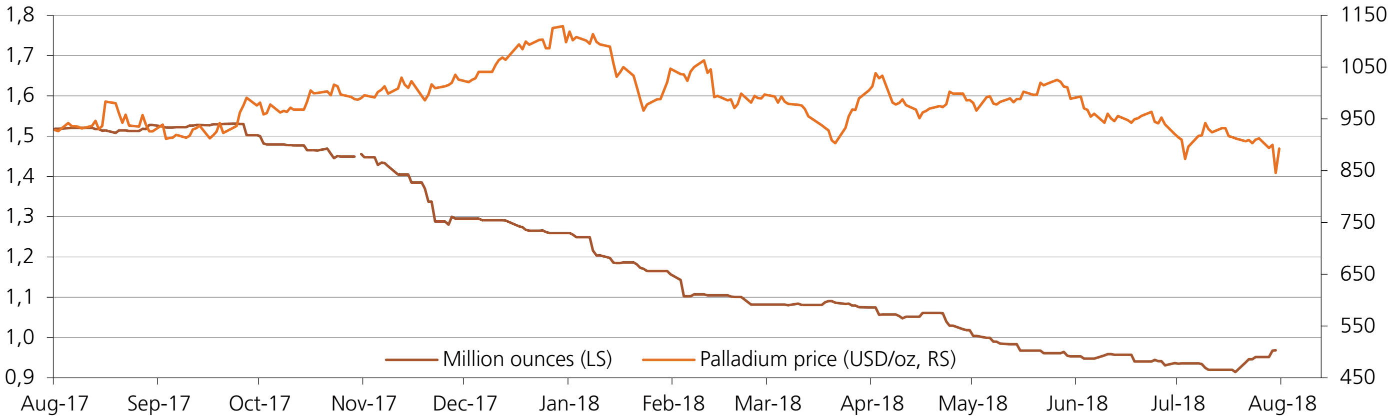
Silver ETFs (million ounces) and silver price (USD/oz)



Platinum ETFs (million ounces) and platinum price (USD/oz)



Palladium ETFs (million ounces) and palladium price (USD/oz)



Source: Thomson Financial.

Precious metals prices

In US-dollar

	Gold		Silver		Platinum		Palladium	
I. Actual	1175.3		14.6		780.2		893.0	
II. Gliding averages								
5 days	1193.9		15.0		800.8		888.8	
10 days	1203.6		15.2		815.7		898.7	
20 days	1213.8		15.3		823.0		910.1	
50 days	1242.8		15.9		843.7		939.7	
100 days	1279.7		16.2		878.4		958.8	
200 days	1294.6		16.4		917.3		993.2	
III. Bandwidths for 2018	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1248	1472	16.0	21.0	936	1048	1033	1261
(1)	*6*	*25*	*9*	*43*	*20*	*34*	*16*	*41*
IV. Annual averages								
2014	1260		19.1		1382		800	
2015	1163		15.7		1065		706	
2016	1242		17.0		985		617	
2017	1253		17.1		947		857	

In Euro

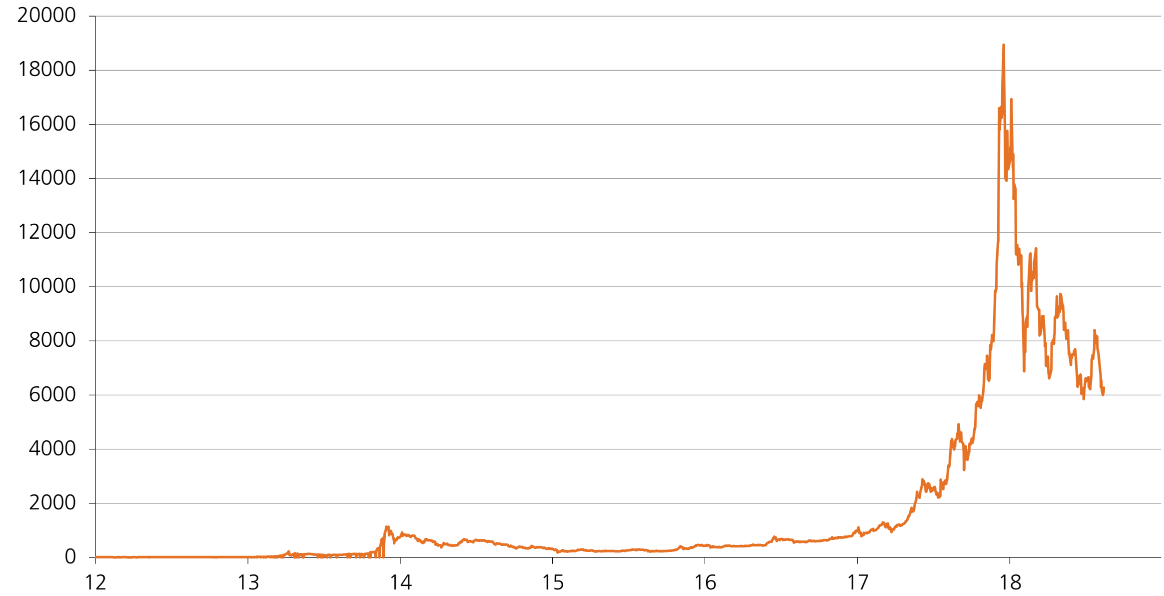
	Gold		Silver		Platinum		Palladium	
I. Actual	1032.0		12.8		685.0		784.1	
II. Gliding averages								
5 days	1048.7		13.1		703.3		780.6	
10 days	1048.1		13.2		710.2		782.5	
20 days	1048.0		13.2		710.5		785.7	
50 days	1068.0		13.6		725.0		807.5	
100 days	1082.5		13.7		742.9		811.3	
200 days	1081.5		13.7		766.0		829.8	
III. Bandwidths for 2018	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1080.8	1274.2	13.8	18.2	810.4	907.6	894.1	1091.7
(1)	*5*	*23*	*8*	*41*	*18*	*32*	*14*	*39*
IV. Annual averages								
2014	945		14		1035		601	
2015	1044		14		955		633	
2016	1120		15		888		557	
2017	1116		15		844		760	

Source: Thomson Financial; own calculations and estiamtes.

(1) Estimated return against actual price in percent.

Bitcoin, performance of various asset classes

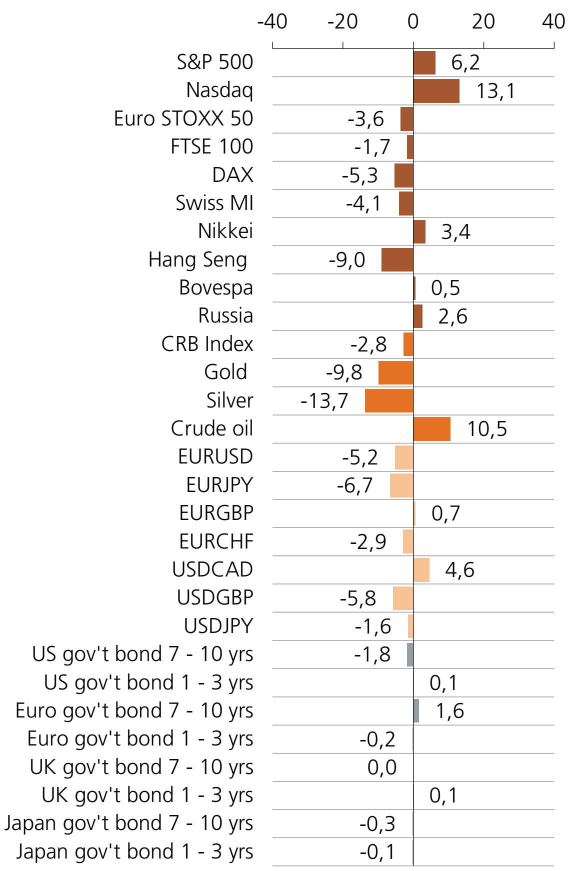
Bitcoin in US dollars



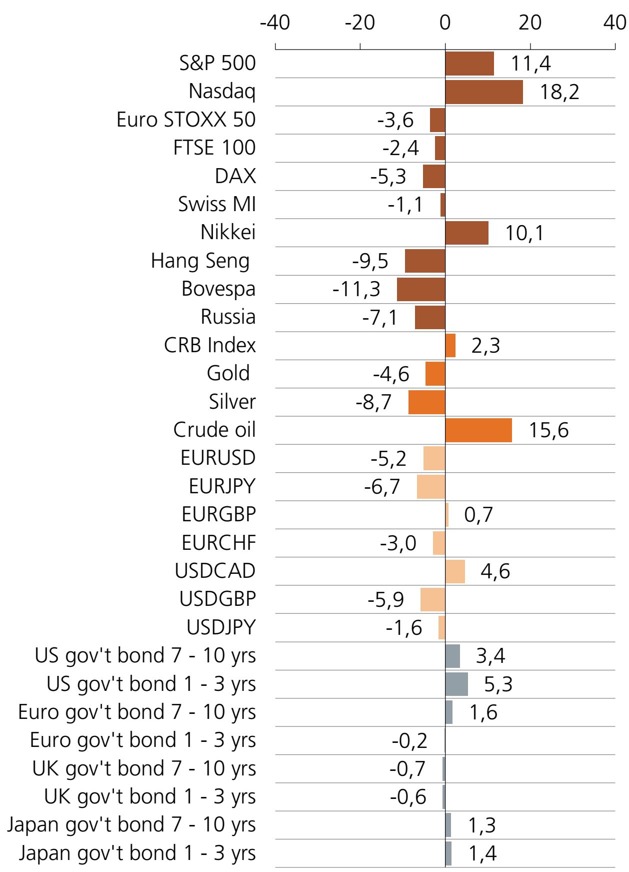
Source: Thomson Financial.

Performance of stocks, commodities, FX and bonds

(a) In national currencies



(b) In euro



Source: Thomson Financial; own calculations

Articles in earlier issues of the *Degussa Market Report*

Issue	Content
17 August 2018	The US dollar And Gold – Is this Time Different?
20 July 2018	Not All Is Well In Financial Markets
22 June 2018	Euro-Banks In Trouble. A Case for Gold
8 June 2018	Demand for Gold ETFs up Despite Higher Interest Rates
25 May 2018	Mind The Interest Rate
11 May 2018	Mr Buffett on Gold – Viewed Differently
27 April 2018	Moving Towards Higher Gold Prices
13 April 2018	The Risk of a Currency Crisis
29 March 2018	Walking the Tightrope
16 March 2018	Gold, Interest Rates, And Money
2 March 2018	Gold in Times of Boom and Bust
16 February 2018	The Fed Makes The Stock Market A Risky Place
2 February 2018	Central Banks Put a Safety Net Under Financial Markets
19 January 2018	Chances And Risks For Investors in 2018
21 December 2017	New Competition: Gold and Crypto Currencies Against Fiat-Monies
8 December 2017	It Is Just Another Inflationary Boom
24 November 2017	There Is, And Will Be More, Inflation
10 November 2017	Calm Markets: The Great Mystery
27 October 2017	The Interest Rate Becomes A "Crash Factor"
13 October 2017	The Great Complacency
29 September 2017	The German Election Outcome Might Turn Up The Heat On The Euro
15 September 2017	A Case for Gold in the Investment Portfolio
1 September 2017	On the Intrinsic Price of Gold
18 August 2017	Gold in Times of Boom and Bust
4 August 2017	The Underpriced Risk
21 July 2017	The Fed Remains on Course – to Trouble
7 July 2017	Gold And The Blockchain
23 June 2017	The Super-Bubble in Danger
9 June 2017	Trapped in Boom-and-Bust
26 May 2017	The Make-Believe World of Fiat Money
12 May 2017	The Fed Will Likely Chicken Out on Planned Rate Hikes
28 April 2017	Central Banks Will not Dare to Take Away the Punch Bowl
13 April 2017	The Gold Price Rise Tells Us: The Crisis Isn't Over Yet
31 March 2017	ECB Negative Interest Rate Policy Will Come to an End
17 March 2017	The Fed's Half-Hearted Attempt of Monetary Tightening
3 March 2017	ECB Flirts With Higher Inflation. The Case For Gold
17 February 2017	Gold Gains Ground vis-a-vis the US-Dollar
3 February 2017	Gold Insures Against Risks Lurking in the Financial System
20 January 2017	The Year of Change
20 December 2016	Gold Rather Than Euro

The Degussa Marktreport (German) and the Degussa Market Report (English) are available at:
www.degussa-goldhandel.de/de/marktreport.aspx.

Disclaimer

Imprint
Marktreport is published every 14 days on Fridays and is a free service provided by Degussa Goldhandel GmbH.
Deadline for this edition: 17 August 2018
Publisher: Degussa Goldhandel GmbH, Kettenhofweg 29, 60325 Frankfurt, Tel.: (069) 860068-0, Fax: (069) 860068-222
E-Mail: info@degussa-goldhandel.de, Internet: www.degussa-goldhandel.de
Editor in chief: Dr. Thorsten Polleit
Degussa Market Report is available on the Internet at: http://www.degussa-goldhandel.de/infothek/marktreport/

Degussa

GOLD UND SILBER.

Frankfurt Headquarters
Kettenhofweg 29 · 60325 Frankfurt
Phone: 069-860 068 – 0 · info@degussa-goldhandel.de

Retail buying and selling outlets in Germany:

Augsburg (shop & showroom)**:** Maximiliansstraße 53 · 86150 Augsburg
Phone: 0821-508667 – 0 · augsburg@degussa-goldhandel.de

Berlin (shop & showroom)**:** Fasanenstraße 70 · 10719 Berlin
Phone: 030-8872838 – 0 · berlin@degussa-goldhandel.de

Frankfurt (shop & showroom)**:** Kettenhofweg 29 · 60325 Frankfurt
Phone: 069-860 068 – 100 · frankfurt@degussa-goldhandel.de

Hamburg (shop & showroom)**:** Ballindamm 5 · 20095 Hamburg
Phone: 040-329 0872 – 0 · hamburg@degussa-goldhandel.de

Hanover (shop & showroom)**:** Theaterstraße 7 · 30159 Hanover
Phone: 0511-897338 – 0 · hannover@degussa-goldhandel.de

Cologne (shop & showroom)**:** Gereonstraße 18-32 · 50670 Cologne
Phone: 0221-120 620 – 0 · koeln@degussa-goldhandel.de

Munich (shop & showroom)**:** Promenadeplatz 12 · 80333 Munich
Phone: 089-13 92613 – 18 · muenchen@degussa-goldhandel.de

Munich (Old Gold Centre): Promenadeplatz 10 · 80333 Munich
Phone: 089-1392613 – 10 · muenchen-altgold@degussa-goldhandel.de

Nuremberg (shop & showroom)**:** Prinzregentenufer 7 · 90489 Nuremberg
Phone: 0911-669 488 – 0 · nuernberg@degussa-goldhandel.de

Pforzheim (refinery)**:** Freiburger Straße 12 · 75179 Pforzheim
Phone: 07231-58795 – 0 · pforzheim@degussa-goldhandel.de

Stuttgart (shop & showroom)**:** Kronprinzstraße 6 · 70173 Stuttgart
Phone: 0711-305893 – 6 · stuttgart@degussa-goldhandel.de

Retail buying and selling outlets around the world:

Zurich (shop & showroom)**:** Bleicherweg 41 · 8002 Zurich
Phone: 0041-44-40341 10 · zuerich@degussa-goldhandel.ch

Geneva (shop & showroom)**:** Quai du Mont-Blanc 5 · 1201 Genève
Phone: 0041-22 908 14 00 · geneve@degussa-goldhandel.ch

Madrid (shop & showroom)**:** Calle de Velázquez 2 · 28001 Madrid
Phone: 0034-911 982 900 · info@degussa-mp.es

London Sharps Pixley Ltd. (member of the Degussa Group)
Phone: 0044-207 871 0532 · info@sharpspixley.com