Degussa Market Report

9 June 2022 Economics · Finance · Precious Metals

USD per ounce of gold

USD per ounce of silver

EURUSD

Source: Refinitiv; graphs by Degussa.

Precious metals prices				
	Actual (spot)	Change against (in percent): 2 W	3 M	12 M
I. In US-dollar				
Gold	1.848,8	0,2	-3,1	4,5
Silver	22,0	1,1	-10,0	-15,8
Platinum	1.006,1	5,3	-3,6	-6,2
Palladium	1.957,1	-0,3	-21,3	-29,6
II. In euro				
Gold	1.727,7	-1,1	1,6	15,8
Silver	20,5	-0,2	-5,6	-6,7
Platinum	940,2	4,1	1,1	3,7
Palladium	1.830,0	-1,5	-17,5	-21,9
III. Gold price in other currencies				
JPY	247.240,0	4,7	12,7	25,7
CNY	12.360,3	0,0	2,7	8,2
GBP	1.474,9	-0,2	3,7	15,3
INR	143.688,0	1,9	-0,3	9,2
RUB	111.666,9	1,7	-42,1	-13,5

Source: Refinitiv; calculations by Degussa.

OUR TOP ISSUES

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

INTEREST RATES RISE, “FINANCIAL REPRESSION” CONTINUES

The crushing issue of high inflation caused by central banks can no longer be downplayed. Public displeasure at the increasing currency devaluation has now forced monetary policy makers to act.

The US Federal Reserve (Fed) has raised its key interest rate to 1 percentage point. Many other central banks have also reacted – such as the Bank of England, the Central Bank of Australia, and the Central Bank of Sweden. Even the ponderous European Central Bank (ECB) now plans to raise interest rates at the beginning of the third quarter.

Does all this mean that there will be an "interest rate reversal"? The answer to this question is important for investors. Interest rates play an extremely significant role in economic and financial activity, especially in the price formation in asset and commodity markets.

The answer begins with a look at the fiat money system that is ubiquitous today. In the fiat money system, interest rates are not established in a "free market." Rather, the interest rate is determined in a "restricted market." Not only do Central banks dictate the short-term interest rate, but they now also have a firm grip on the long-term interest rate through the purchase of debt securities; in principle, if they want, they can determine the interest to the decimal place.

The interest rate is extremely important to the functioning of the fiat money system because fiat money is created by the central banks in close cooperation with the commercial banks, which lend money to consumers, producers, and governments without corresponding savings (renunciation of consumption) available. It amounts to creating money out of thin air.

Such an artificial supply of credit lowers the market interest rate below the level it would have been had the artificial supply of credit not occurred. The artificial suppression of interest rates initially causes an economic upswing, a boom.

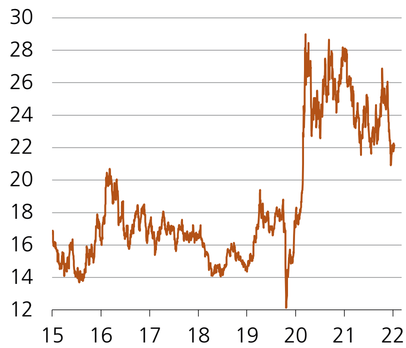
WE HAVE CHANGED OUR FORECASTS

The summary table on the next page shows our new precious metals price forecasts (see also the table on page 5). As can be seen, we now expect the price of gold to reach around 2.200 USD/oz until summer 2023 (which represents a 19 per cent upside potential from the current price), up from 2.100 USD/oz previously. The expected price of silver has remained bascially unchanged from our January 2022 estimate at around 28 USD/oz (implying an upside of 28 per cent from the current price). At the same time, however, we have lowered somewhat the expected platinum price to 1.070 USD/oz (suggesting an upside of 7 per cent

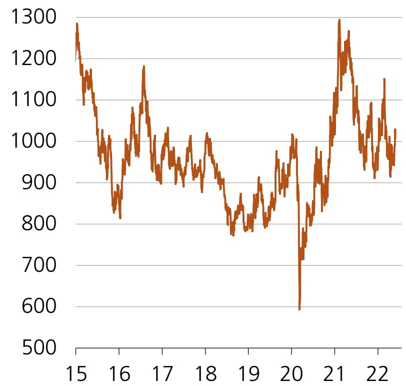
Precious metal prices (USD/oz), last seven years

(a) Gold

(b) Silver



(c) Platinum



(d) Palladium

Source: Refinitiv; graphs Degussa.

from the current price), while we left the expected palladium price basically unchanged (with an upside of 16 per cent from the current price). Underlying these estimates are two macroeconomic assumptions: (1) interest rates will remain lower than markets currently expect; and (2) inflation will remain higher for longer. Moreover, we expect that USDEUR will continue to trade lower in the coming months, dropping below parity.

Estimates for precious metal prices (USD/oz) until summer '23

	Gold	Silver	Platinum	Palladium
Market price 9 June 2022	1847	22,0	1004	1951
I. In US-Dollar	**2200**	**28,0**	**1070**	**2260**
Expected return (%) (1)	*19*	*27*	*7*	*16*
Upper range	2400	32	1280	2400
Lower range	1800	21	830	1650
II. In Euro	**2300**	**29,0**	**1100**	**2300**
Expected return (%) (1)	*33*	*41*	*17*	*26*
Upper range	2500	33	1300	2500
Lower range	1800	22	900	1700
Previous estimate from Jan. '22 in USD/oz:				
Market price January 2022	1840	24,1	1024	1999
Esimate for end '22	**2100**	**28,2**	**1175**	**2261**
Expected return (%) (1)	*14*	*17*	*15*	*13*

Source: Refinitiv; calculations and estimates by Degussa. Numbers are rounded.
(1) Estimated price againgst current market price.

The boom has an impact on the economic production and employment structure: Scarce resources are increasingly being invested in long-term, time-consuming projects and less in the production of consumer goods. The investment success and thus the continuation of the boom depend on interest rates remaining low or falling to even lower levels.

As long as the boom continues, everything seems to be working fine and properly: Companies seem to be doing everything right, they are making profits; borrowing is possible without major problems; workers can hope for higher wages and more job opportunities; tax revenues flow; stock market prices are climbing to new highs.

But debt is also growing in absolute terms and in relation to economic output. Consumer spending is financed "on tick", which essentially means capital consumption and no capital accumulation, and the government, in particular, borrows heavily to finance its spending, which normally contributes little to nothing to the productivity growth of the economy. Returns on many business investments lag behind the rise in debt, contributing to the increase in overall debt.

What happens when the central bank raises interest rates is obvious in the light of what has been said. When interest rates rise, people reduce their consumption and save more of their current income. Companies suddenly notice that profits are lower than hoped, new investments do not pay off contrary to expectations, they "flop". Projects are halted, liquidated, and jobs created during the boom are lost. In other words: The boom turns into bust.

This necessitates a reallocation and re-evaluation of the factors of production – tools, machines, labour, etc. It becomes clear that some of these factors have been wasted, i.e. channelled into unfeasible production methods with extremely low residual utilization (leaving behind ruins). Workers are also affected: human skills and abilities are no longer needed at previous levels, and workers have to reorient themselves and retrain – or drop out of the labour market.

Since all of this takes time, the economic rebalancing that such a bust entails does not usually come without a recession and unemployment. In a highly indebted economy, this is particularly painful.

Anyone who loses their income through unemployment, for example, has problems paying off their debt service on their home. Companies are under equal pressure to meet their interest and principal payments. Banks are affected by payment delays and defaults. If risk provisions are not sufficient to cover losses, the banks' meagre equity base will be depleted. Banks become cautious and reluctant to lend, and the flow of new credit and new money into the economy dwindles.

This, in turn, puts pressure on asset prices: stock and bond prices, as well as real estate and land prices, decline. The value of the collateral underlying bank lending dwindles. Banks require additional collateral from borrowers. If the borrowers cannot afford this, they are threatened with termination of the loan and slide to the brink of bankruptcy.

This way, the inflationary regime can ultimately turn into a deflationary regime – in which the prices of goods fall across the board, and the economy falters. If there are no "opposing forces", such a development will even bring down the entire fiat money system. But there are "opposing forces".

It is important to know that the debt pyramid has been piled up under a regime of "financial repression" in recent years: Central banks have cut interest rates so much that they were (and still are) negative after inflation. Maturing loans were thus replaced by new loans with a negative real interest rate; and more loans were also taken out, also with negative real interest rates.

Therefore, it is understandable that especially highly indebted governments have very little interest in a monetary policy that increases interest rates and lowers inflation – because low interest rates, combined with high inflation, are exactly what public finances need: they reduce government debt at the expense of creditors and money holders.

An exit from such a "financial repression" would most likely trigger a major economic and financial, even political crisis, as the associated rise in real interest rates would cause a bust. So the key question is: What is the motive of the central banks? Their true motive is certainly not to keep consumer price inflation at the 2 per cent mark; otherwise, they would have raised interest rates long ago.

Rather, it is to be feared that central banks want higher inflation to defuse the precarious debt problems of their national economies. As mentioned before, this can be achieved if interest rates are kept low with inflation exceeding interest rates so that creditors and money holders get the short end of the deal. However, there is a problem: inflation must not get too high.

Because if that happens, there is a risk that people will literally "flee from money," and money threatens to lose its function altogether. Of course, governments don't want that. They need inflationary fiat money to conduct their redistributive policies.

If central banks want to pursue a policy of elevated inflation while at the same time preventing inflation from spiralling out of control, they have to bluff the public – giving the impression that they are determined to "fight inflation" (which, of course, they are to blame for).

While some smaller interest rate hikes might be needed, the question is: will the real interest rate, which has been negative for around 15 years, return back to positive territory? Doubts remain.

The elevated level of debt in the economies indicates that real interest rates can no longer return to "normal" levels. All the more so as there is a tacit consensus in the western world that free market forces must not challenge the "welfare state", financed with ever more debt and inflationary fiat money.

This mindset also supports those who want to impose their "great reset" and "great transformation" agenda on their fellow people. The fiat money system is a particularly powerful instrument not only for the state but also for the special interest groups who seek to use it for their purposes of manipulating economic and societal developments. They will not give it up lightly.

The strong political incentive to keep the fiat money system afloat suggests that central banks on both sides of the Atlantic will only tighten interest rates slightly; but that they will not abandon their inflationary policies; and that if the economy slows down, they will respond with even more debt, more money, and even higher inflation.

So even if interest rates rise, you as an investor should be aware that the financial repression continues. The purchasing power of official currencies will most likely continue to be heavily debased. It is a development that not only increasingly erodes the store of value function of the US dollar, euro & Co, it also threatens their means of exchange function.

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PRECIOUS METALS PRICES

In US-Dollar per ounce

	Gold		Silver		Platinum		Palladium	
I. Actual	**1849,4**		**22,0**		**994,7**		**1949,0**	
II. Gliding averages								
10 days	1851,4		22,0		976,5		2010,8	
20 days	1844,0		21,8		966,5		2005,7	
50 days	1890,5		23,2		966,0		2175,7	
100 days	1890,7		23,7		1005,6		2304,9	
200 days	1842,5		23,5		997,6		2138,9	
III. Estimates for summer 2023	**2200**		**28**		**1070**		**2260**	
(1)	*19*		*27*		*8*		*16*	
Band width	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1800	2398	21,0	31,0	830	1280	1650	2400
(1)	*-3*	*30*	*-5*	*41*	*-17*	*29*	*-15*	*23*
V. Annual averages								
2019	1382		16,1		862		1511	
2020	1753		20,2		878		2180	
2021	1804		25,5		1095		2422	

In Euro per ounce

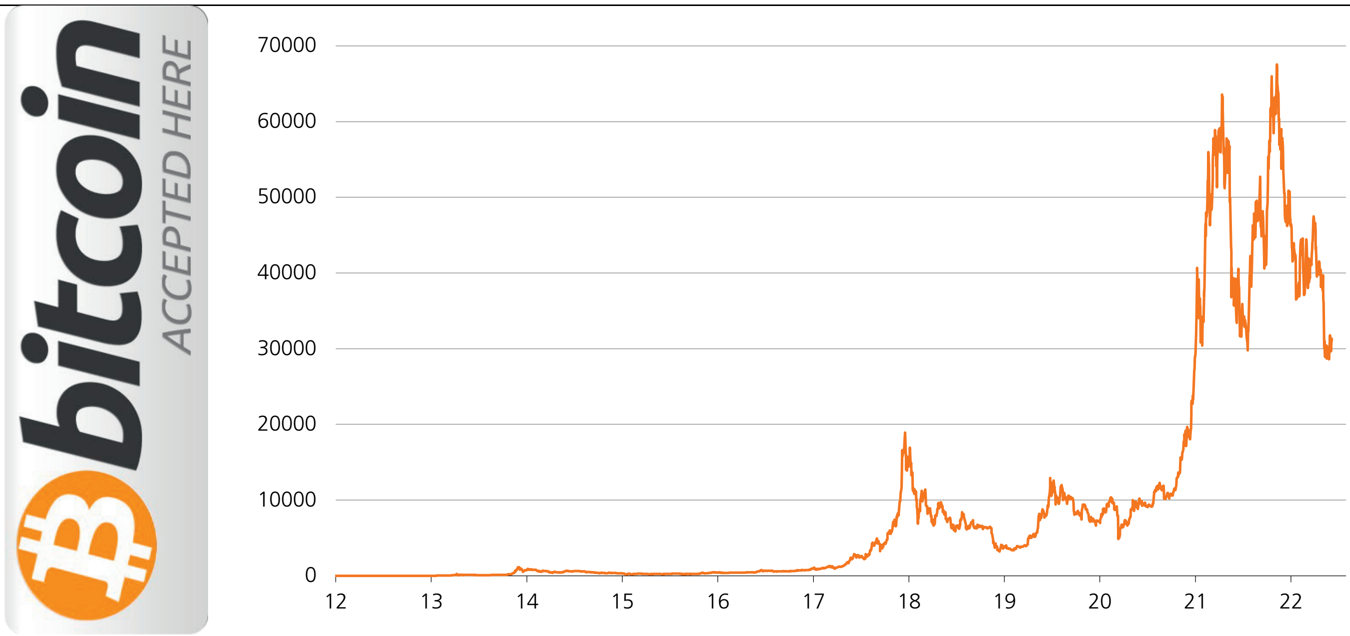
	Gold		Silver		Platinum		Palladium	
I. Actual	**1726,6**		**20,5**		**928,6**		**1819,6**	
II. Gliding averages								
10 days	1728,1		20,5		911,5		1876,9	
20 days	1735,8		20,5		909,7		1888,0	
50 days	1765,4		21,6		902,2		2031,0	
100 days	1728,0		21,7		918,2		2104,4	
200 days	1644,6		21,0		889,5		1909,6	
III. Estimates for summer 2023	**2281**		**29**		**1110**		**2344**	
(1)	*32*		*41*		*19*		*29*	
Band width	*Low*	*High*	*Low*	*High*	*Low*	*High*	*Low*	*High*
	1867	2487	21,8	32,1	860	1320	1710	2480
(1)	*8*	*44*	*6*	*57*	*-7*	*42*	*-6*	*36*
V. Annual averages								
2019	1235		14		770		1350	
2020	1535		18		769		1911	
2021	1519		21		921		2035	

Source: Refinitiv; calculations and estimates Degussa. Numbers are rounded.

(1) On the basis of actual prices.

BITCOIN, PERFORMANCE OF VARIOUS ASSET CLASSES

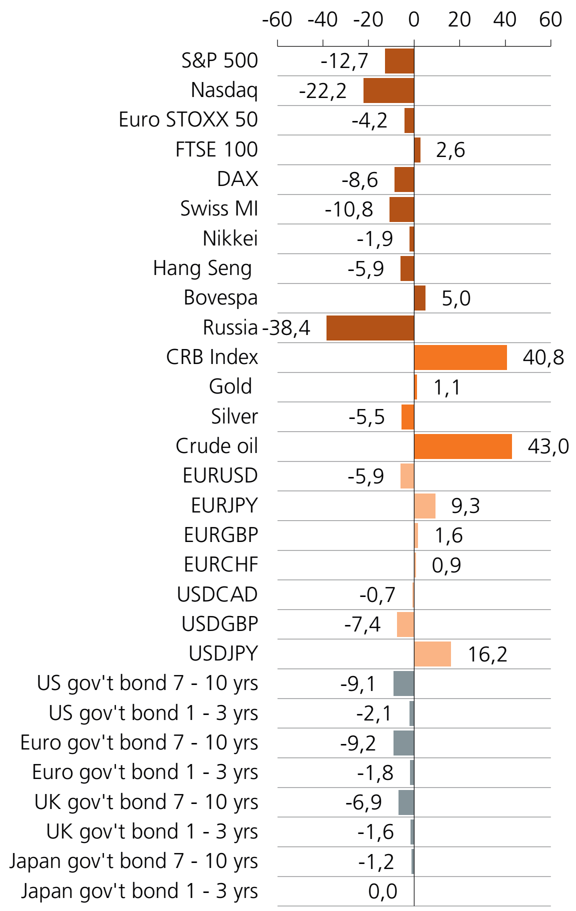
Bitcoin in US dollars



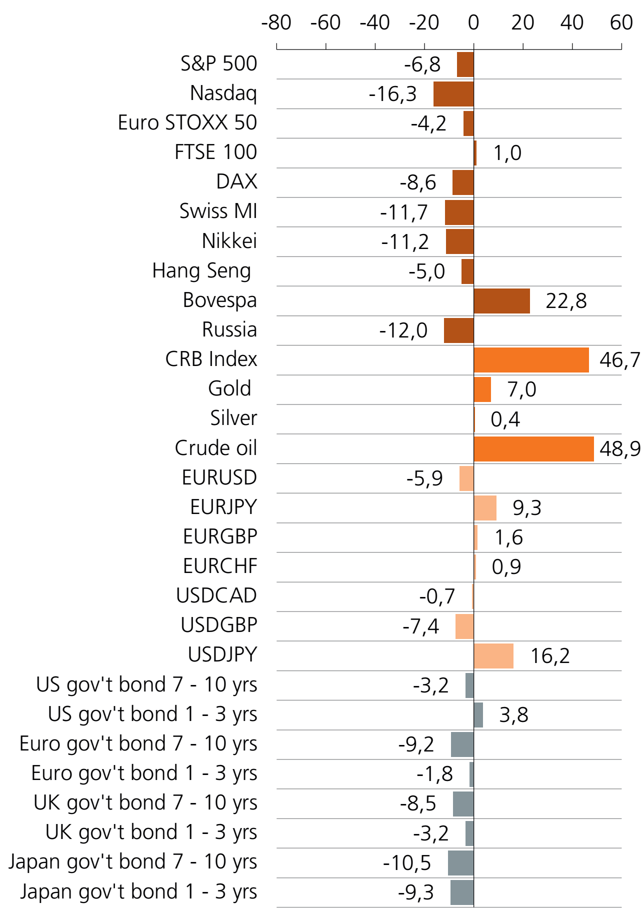
Source: Refinitiv; graph by Degussa.

Performance of stocks, commodities, FX and bonds

(a) In national currencies



(b) In euro



Source: Refinitiv; calculations by Degussa.

Articles in earlier issues of the *Degussa Market Report*

Issue	Content
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14 April 2022	Do You Know What Inflation Really Is? Then Hold Gold And Silver
31 March 2022	How Not To Get Battered
17 March 2022	There is no Return to Normality. The Case for Gold and Silver
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17 February 2022	The Inflation beast is bigger than you think it is
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