Market performance and macro factors

Gold report

Q2 2021

Introduction

In the first part of our quarterly Gold Report, we review the performance of the gold price and touch upon other asset classes as well as explore significant macro factors, including bond yields, the US Dollar and inflation expectations.

Key facts from Q2 2021

Gold price increased

3.7%

in Q2 2021

On a 12-month basis, gold delivered an

-0.6%

return, leaving it as the second-worst performing asset, just ahead of US Treasuries

The yield on the US 10-year TIPS ended the quarter at

-0.88%

in Q2

US Dollar Index fell

-0.8%

in Q2

Data: Bloomberg, as at 30 June 2021.

Market performance

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The gold price recovered some of the ground it lost in Q1 as a spike in headline inflation and a dip in real bond yields supported the precious metal. Compared to other asset classes, gold was outpaced by equities in the quarter but fared better than fixed income, although all assets delivered positive returns in USD terms.

Macro factors

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Although headline inflation was markedly higher, the Federal Reserve's hawkish tone at its June meeting took some of the shine off gold.

Please note that we may refer to supply and demand dynamics in this commentary but will take a more in-depth look into these specific contributors in a subsequent report.

Quarterly price performance

The gold price increased 3.7% in the second quarter of 2021, recovering some of the ground lost in Q1. As inflation concerns rose and real yields fell, gold had a strong rally in the first two months of the quarter. The precious metal increased from just over $1,700 an ounce to a peak of $1,908 at the start of June, still well below the all-time high of $2,064 reached in August last year.

The unexpected hawkish tone struck by the Federal Reserve at the June FOMC meeting and the subsequent strengthening in the USD saw upward momentum in the gold price subsequently unwind, falling back sharply to end the quarter at $1,770.

Gold price increased

3.7%

in Q2

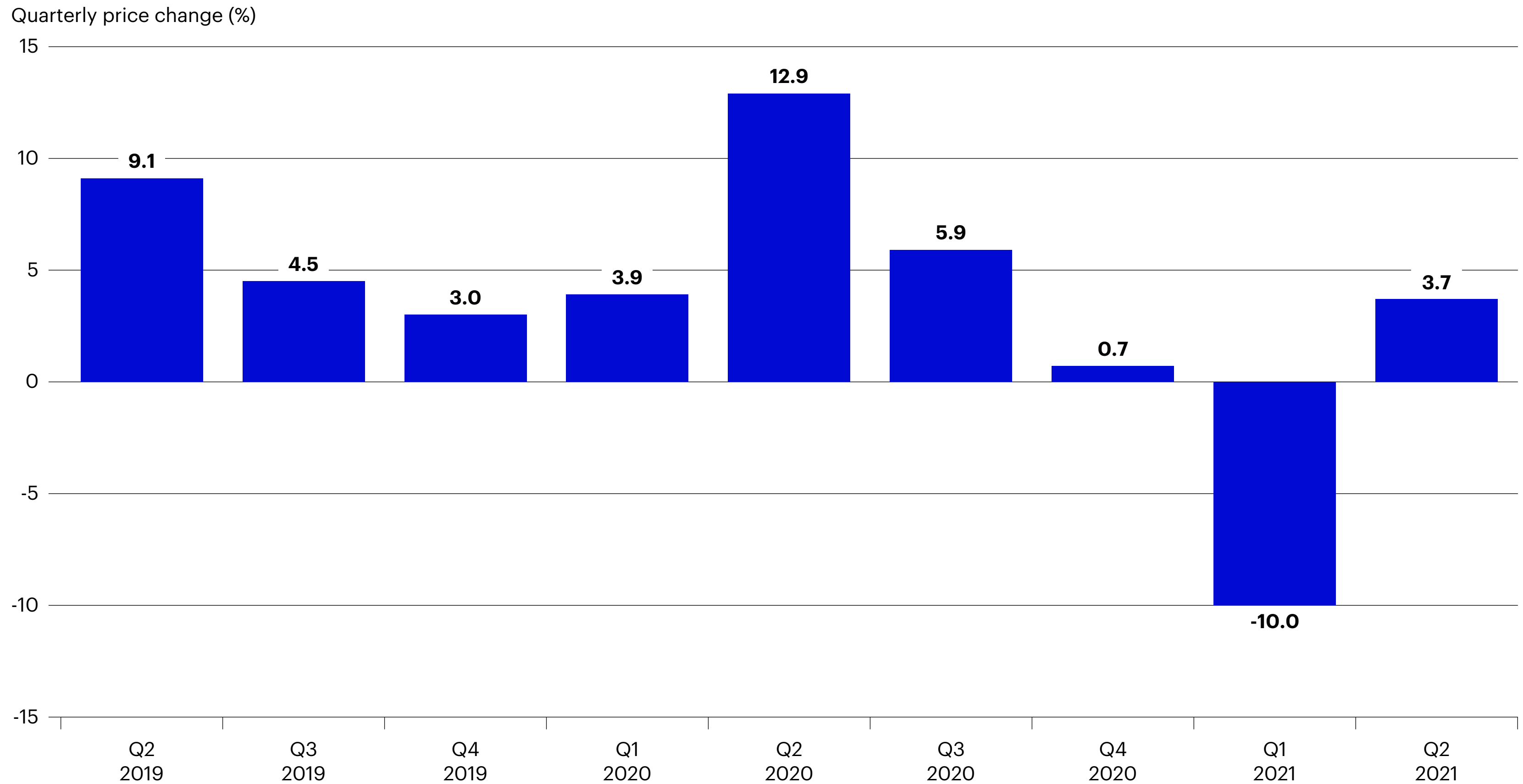
Past performance is not a reliable indicator of future returns. Bloomberg, in USD, from 31 March to 30 June 2021.

Market performance

Macro factors

Quarterly price returns

Although not able to hold onto all of its gains through Q2, gold still managed its best quarter since Q3 last year and the 3.7% return was a big improvement on the -10% decline in Q1.



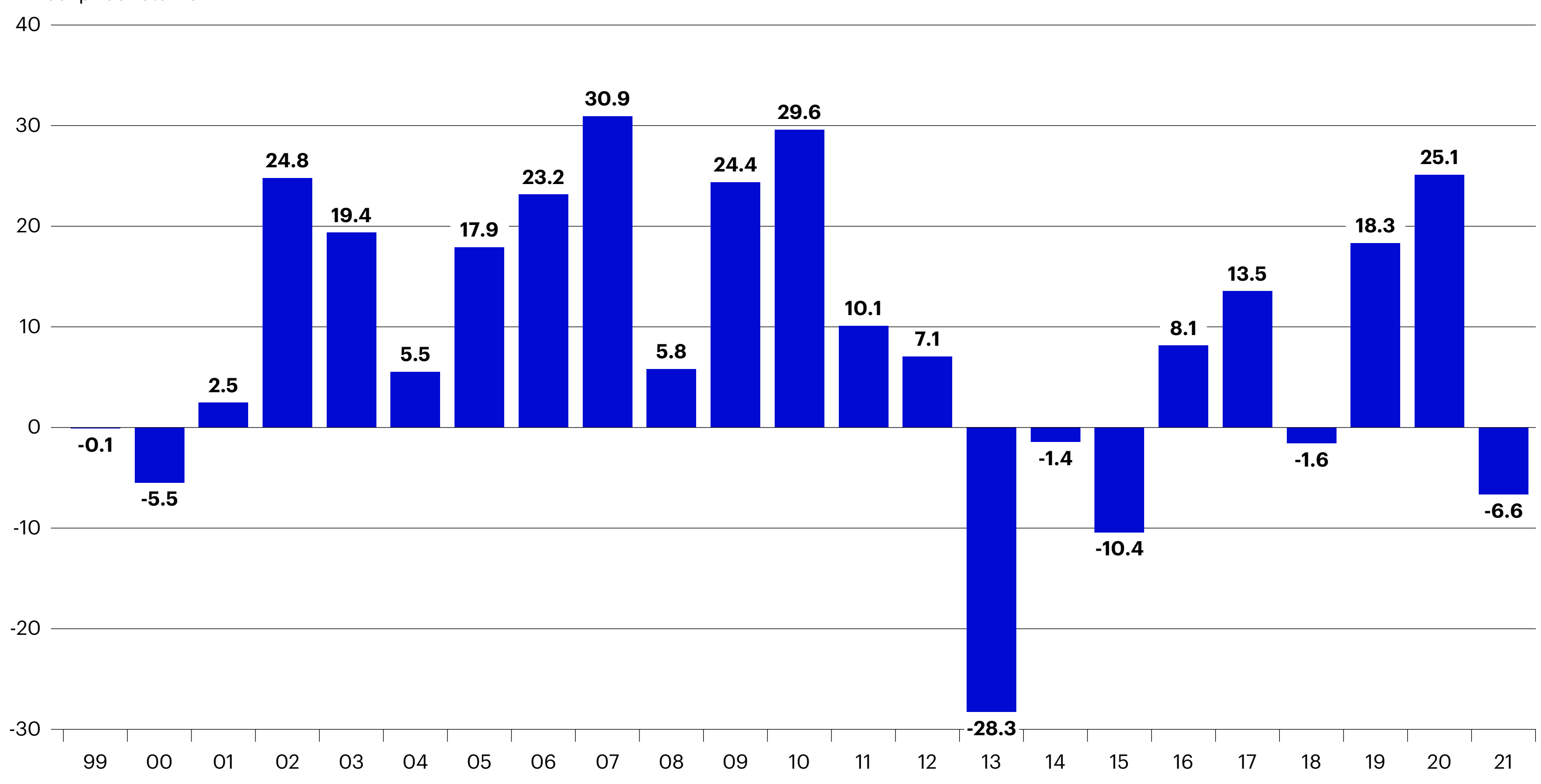
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 30 June 2021.

Annual price returns

The positive performance this quarter was not sufficient to overcome the poor start to the year. Year-to-date, gold has returned -6.6%.

While year-to-date returns are clearly down on recent years, 2021 is still ahead of 2013, when the gold price fell by a hefty 26.3% in the first six months and went on to end that year 28.3% lower.

Annual price returns*



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 30 June 2021. *2021 is YTD returns.

Asset class returns

Although every major asset class delivered a positive return in the quarter, Q2 again favoured risk assets. Commodity prices had a particularly strong quarter, rising 13.3%, boosted by notably higher oil and gas prices. Equities also performed well, led by global developed markets. In fixed income, both US Treasuries and investment grade credit recovered some of the previous quarter's losses, while high yield made further gains, hitting new all-time highs. Gold outperformed these fixed income sectors but lagged riskier assets.

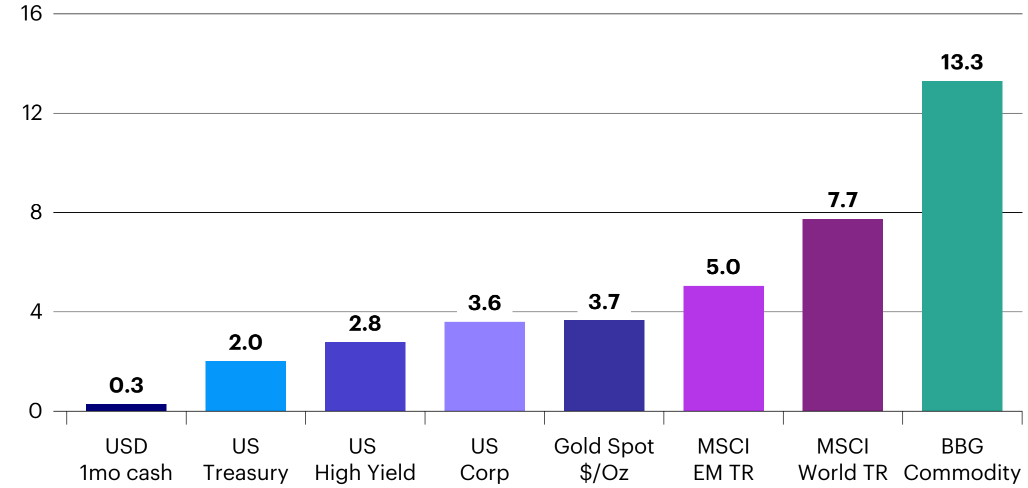
On a 12-month basis, gold has returned -0.6%, leaving it as the second-worst performing asset, just ahead of US Treasuries, which also delivered a negative return. The significant improvement in the macroeconomic outlook over the past year has underpinned very strong performance from risk assets, such as equities and commodities. High yield, the most risk-sensitive area of fixed income, has also delivered superior returns relative to the rest of the asset class.

On a 12-month basis, gold delivered a

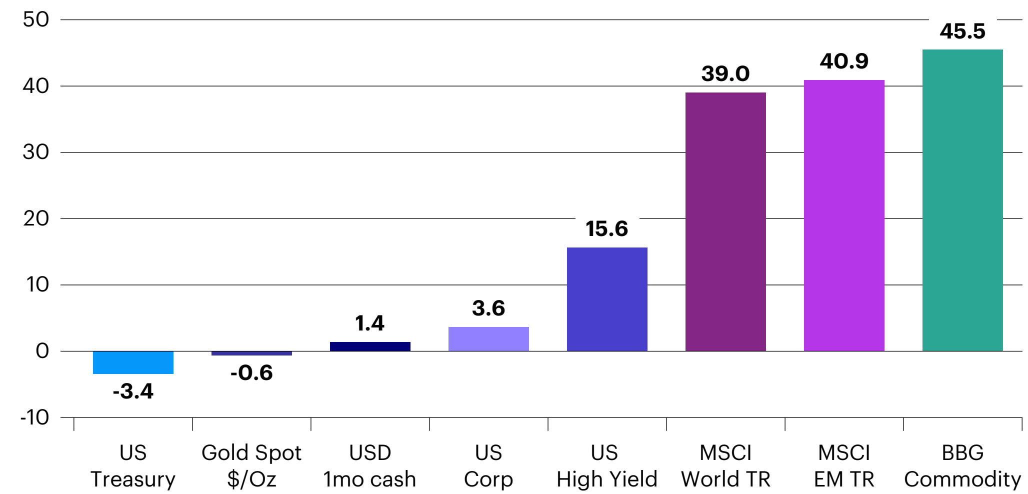
-0.6%

return, leaving it as the second-worst performing asset, just ahead of US Treasuries

Quarterly asset class returns (%)



12-month asset class returns (%)

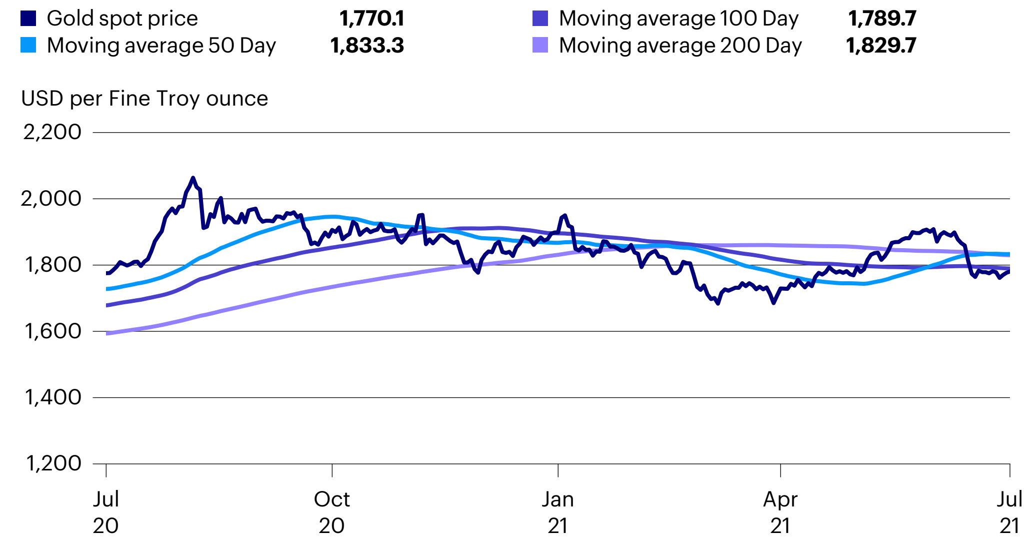


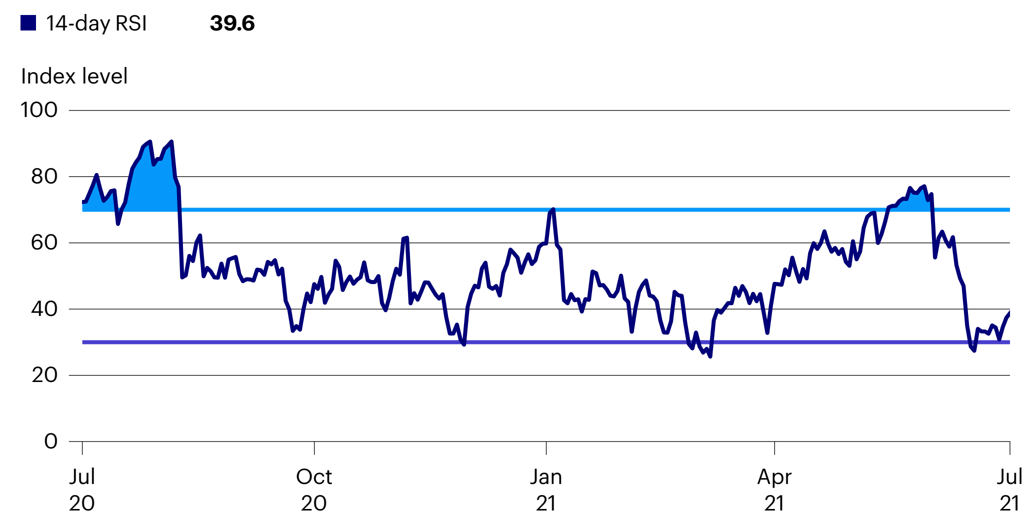
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 30 June 2021.

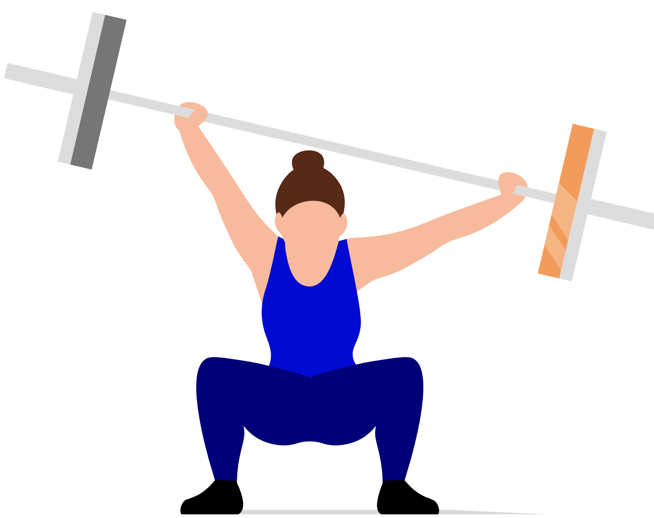
Relative strength of the gold price

Moving averages provided support to the higher gold prices as the shorter 50-day measure crossed the 100-day measure creating a buy signal.

However, the gold price has been particularly volatile this quarter, triggering both overbought and oversold signals within a matter of weeks in June. On the 14-day relative strength indicator measure, it is currently hovering close to oversold levels (30).







Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 June 2021.

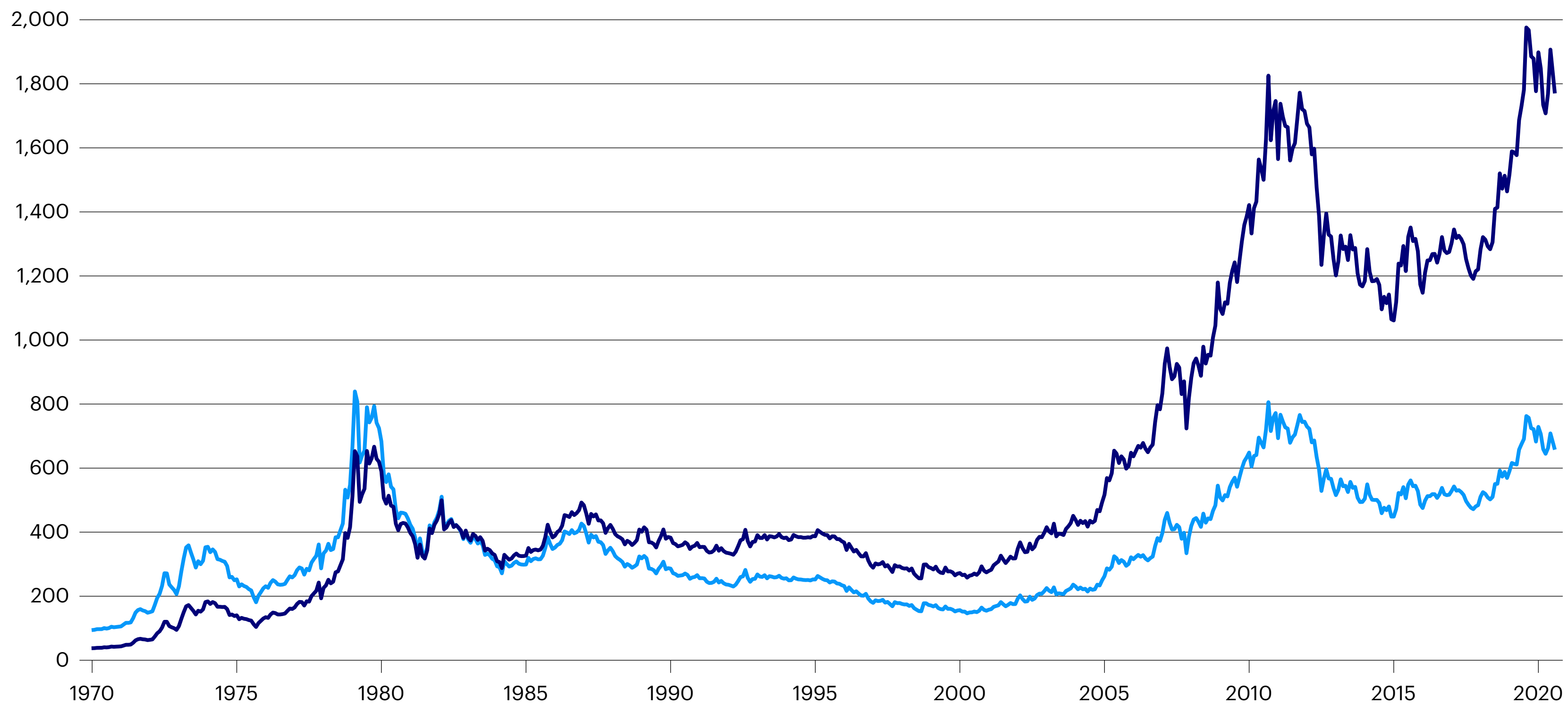
Gold price return, nominal and adjusted for inflation

Adjusting for the US headline Consumer Prices Index (CPI), gold returned 2.0% for the quarter. On an annual basis, the sharp rise in CPI to 5.0% year-on-year was its highest level since 2008 and resulted in a -4.8% return for the gold price in real terms.

Inflation is currently one of the key factors that gold observers are monitoring, especially regarding the Federal Reserve's expectations beyond the immediate term. The majority of the US rate-setting committee still considers the high level of inflation as temporary.

Nominal Gold price	**1,770.1**
Real Gold price	**657.6**

USD per Fine Troy ounce



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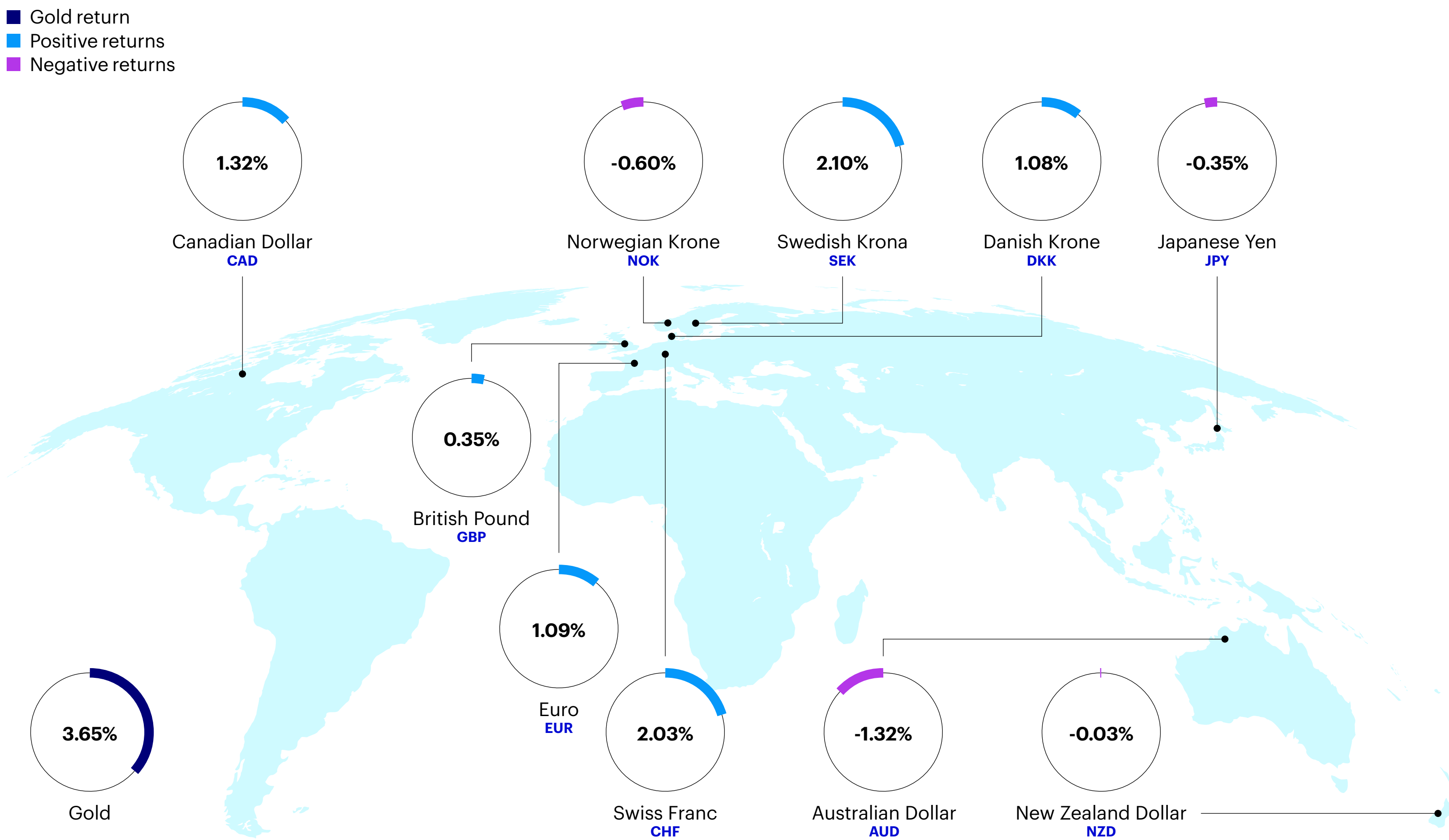
G10 currencies

Although the US Dollar had its strongest month for over a year in June on the back of the hawkish Federal Open Market Committee (FOMC) meeting, it was not enough to offset earlier weakness. For the quarter as a whole, the greenback was down against many major G10 currencies, such as the Euro and Sterling.

Q2 returns of gold and G10 currencies in USD (%)



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Gold price and real bond yields

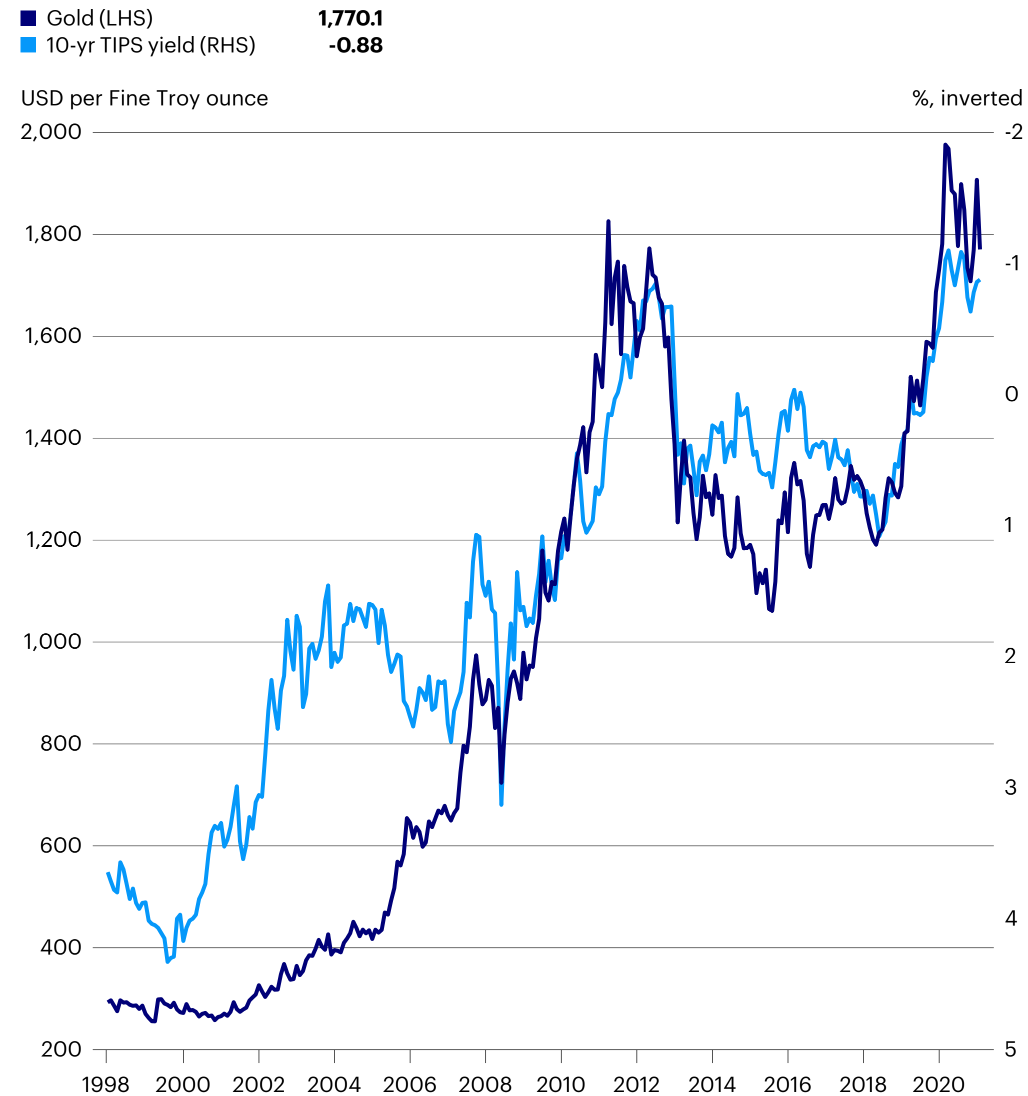
During the quarter, the gold price benefitted from lower real yields with the 10-year TIPS falling to -0.88% from -0.63%. A decrease in bond yields reduces the opportunity cost of holding gold, given it is a non-income-paying asset.

Economic growth continues to be strong reflected in the hawkish turn of the FOMC at its latest meeting and despite inflation risk still seen as transitory. With the 10-year Breakeven Inflation rate broadly unchanged during the quarter, the decline in the 10-year US Treasury yield from 1.74% to 1.47% was largely driven by lower real yields.

US 10-year TIPS yield fell to

-0.88%

in Q2



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Market performance

Macro factors

Gold price and negative-yielding debt

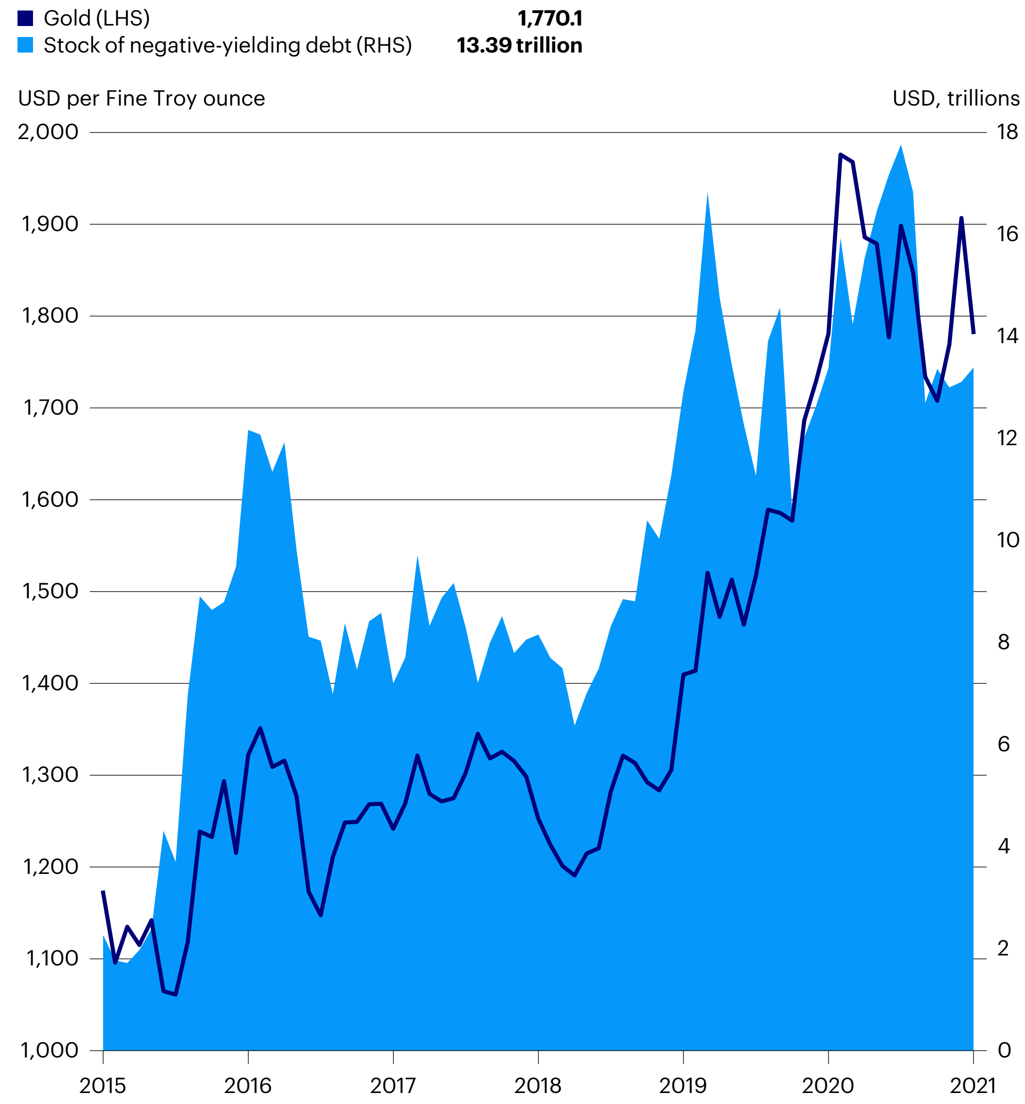
The gold price continues to be supported by the low yields on offer in many fixed income markets. The stock of negative-yielding debt was $13.4 trillion at the end of Q2, broadly unchanged over the quarter and constituting around 20% of the Bloomberg Barclays Global Aggregate index of investment grade debt. Euro (63%) and Yen (34%) denominated bonds make up the bulk of this exposure with government and government-related debt just under 85% of the total. The remainder is in corporate (8%) and securitised (7%) debt.

Amount of negative-yielding debt globally

$13.4 trillion

20%

of aggregate bond index

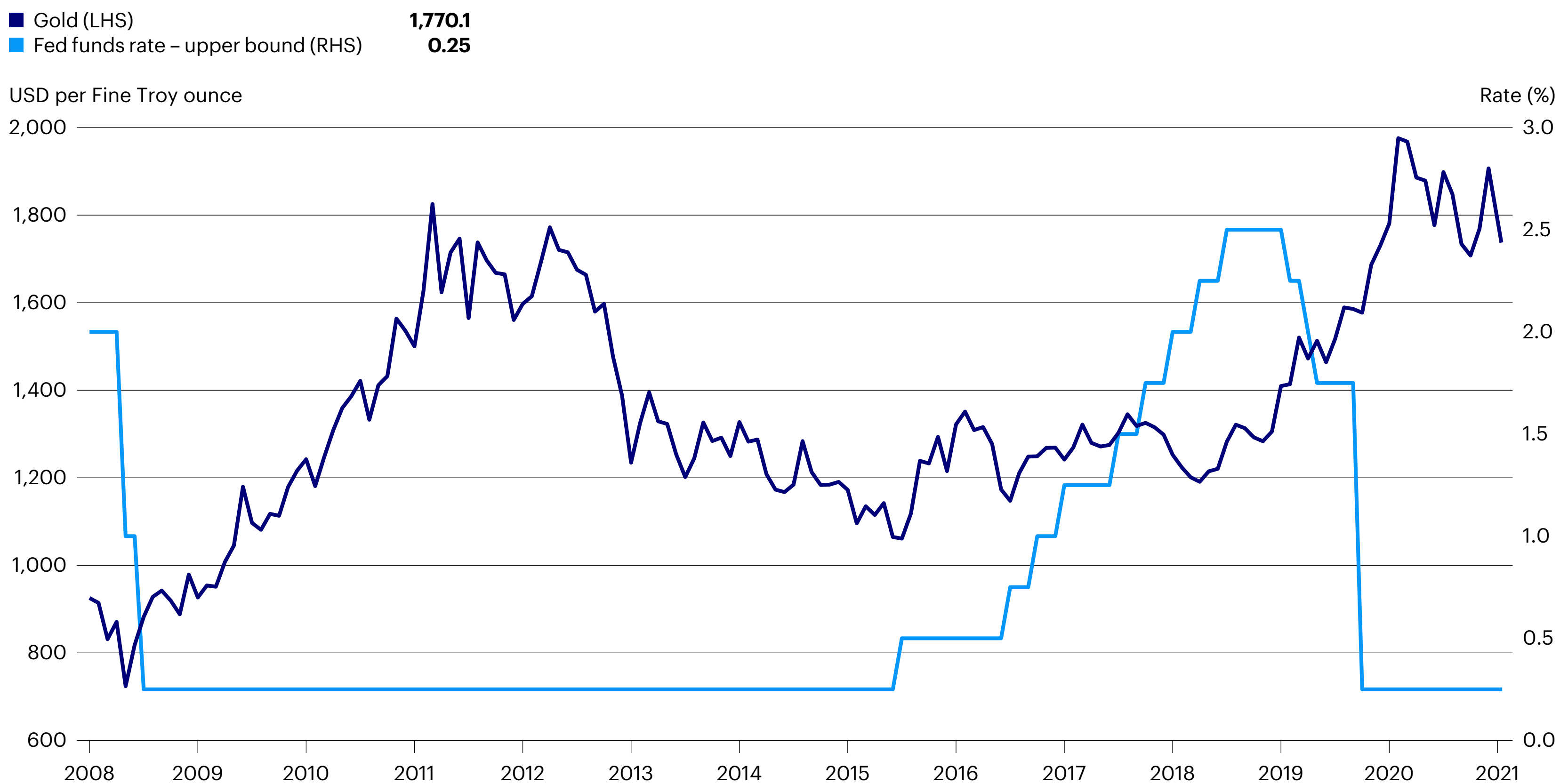


Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 June 2021.

Gold price and US interest rates

The Fed Funds Rate remained at 0.25% in the quarter, although a surprisingly hawkish tone was set at the June FOMC meeting. The dot plot of rate expectations now has two rate hikes in 2023 from none in March. This is more in-line with market expectations where the first hike is now priced in towards the end of 2022.

An announcement on tapering of the Fed's asset purchase programme is expected in Q3, potentially at the Jackson Hole Symposium in August. A more aggressive policy stance from the Fed could weigh on gold's prospects.



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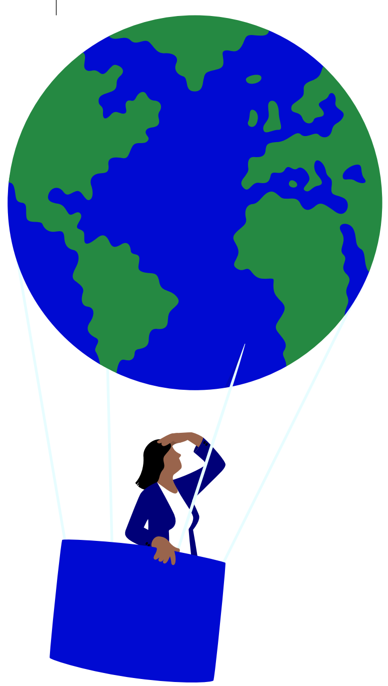
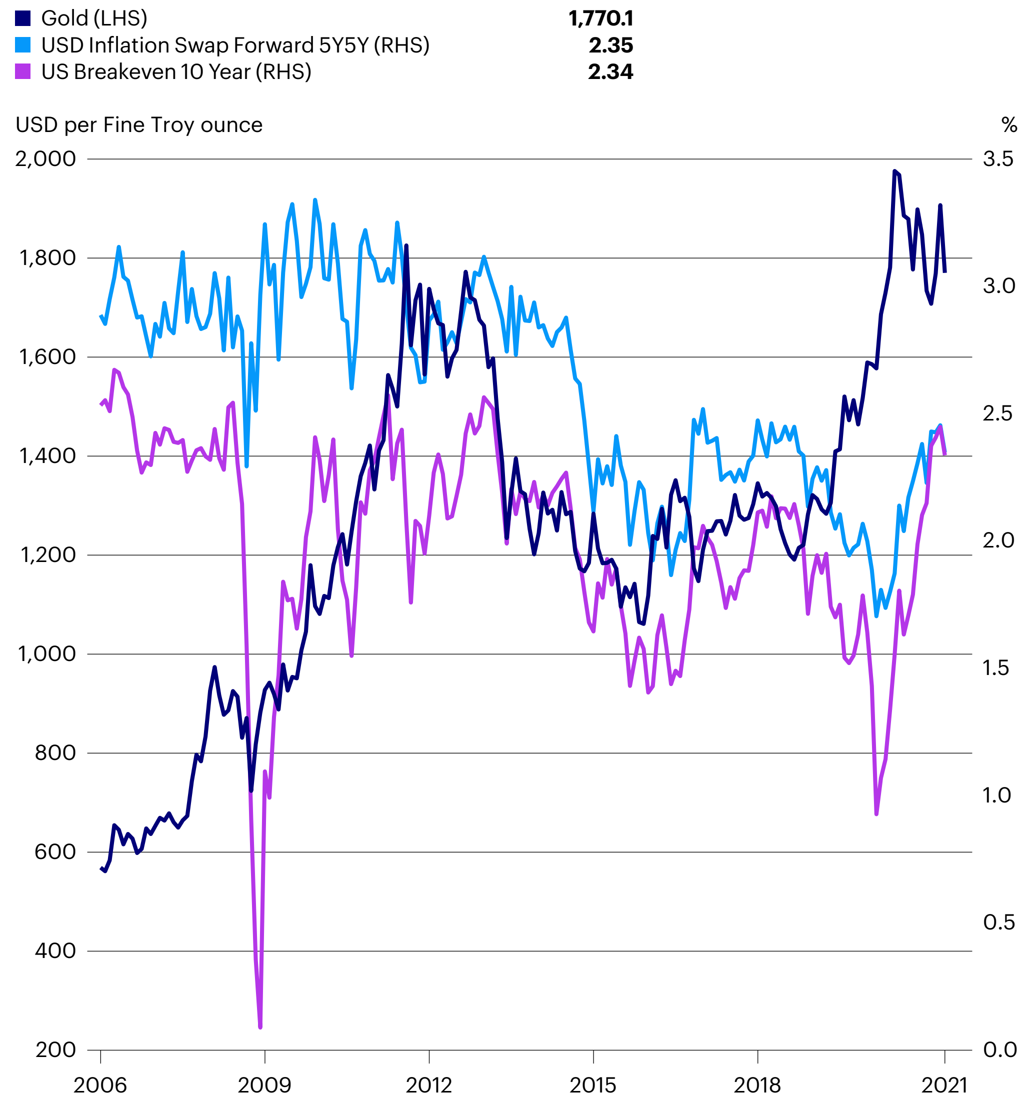
Gold price and inflation expectations

Market measures of inflation expectations ended the quarter slightly lower, but still well above the pandemic-related lows of March last year. 10-year US Breakeven Inflation fell to 2.34% from 2.37% and the 5y5y USD Inflation Swap also edged lower from 2.43% to 2.35%. While US Headline CPI rose from 2.6% to 5.0% during the quarter, its highest level since 2008, the lack of reaction in market inflation expectations reflected the fact that higher inflation has already been largely discounted and, more importantly, an expectation that any rise is likely to be transitory in nature.





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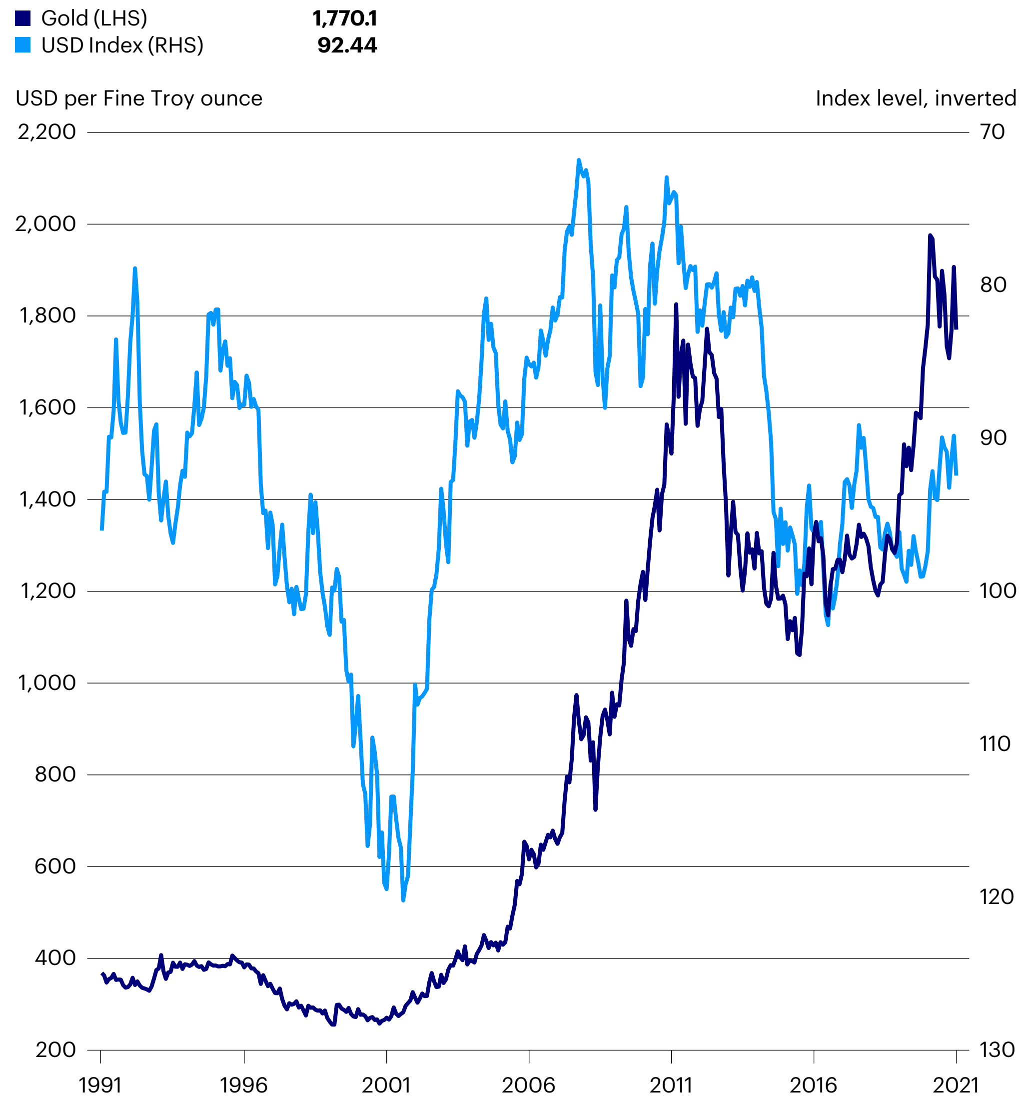
Gold price and the US Dollar

The second quarter was a roller-coaster for the US Dollar. At its quarterly low in late May, the USD Index was down -3.9%, but since then has rallied strongly, boosted by the hawkish FOMC meeting to end the quarter -0.8%. Moves in the USD were reflected in the gold price, providing a boost in the first two months of the quarter, then weighing on it towards the end.

US Dollar Index fell

-0.8%

in Q2



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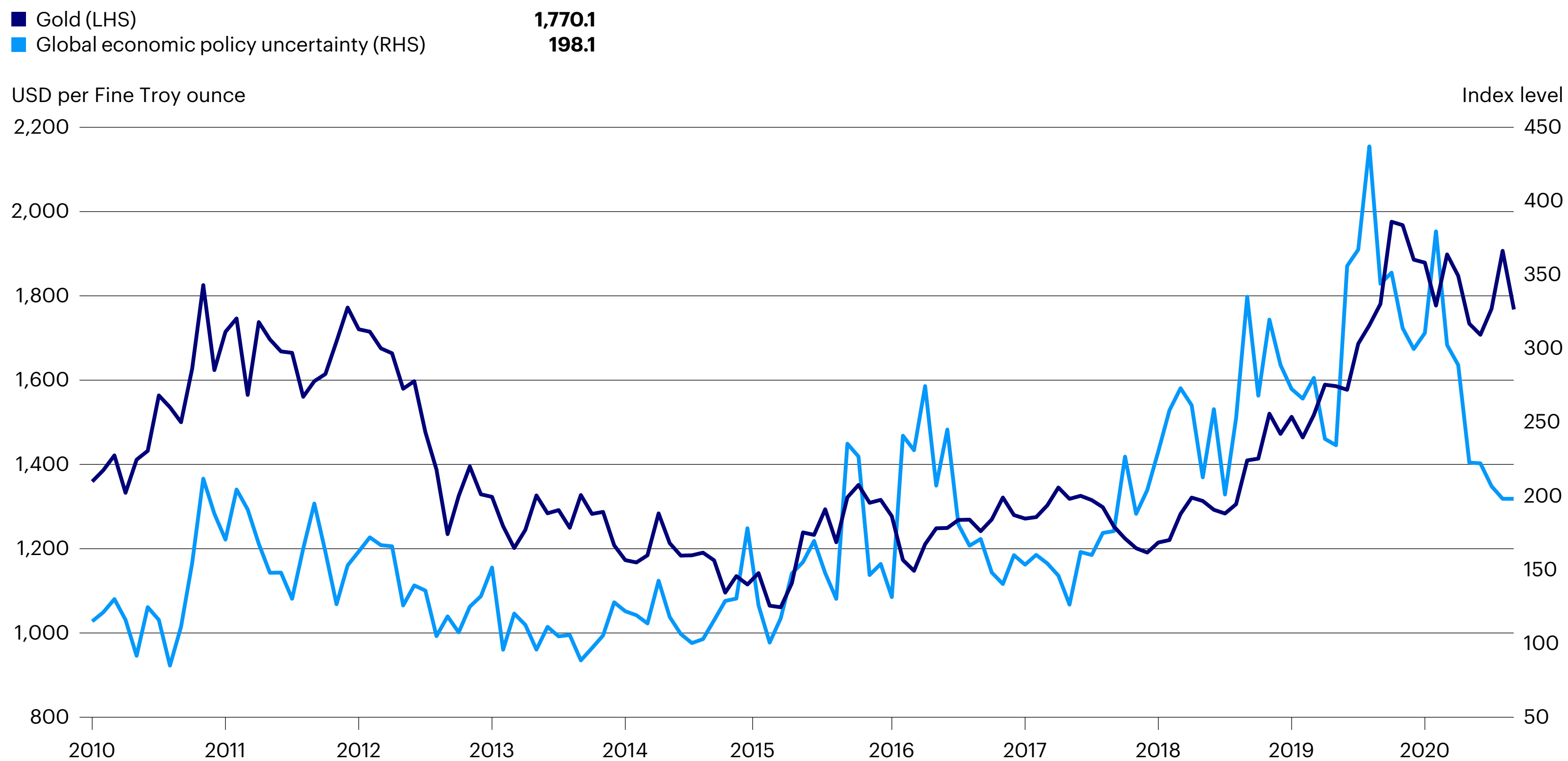
Gold price and economic risks

As the vaccination programme rolled out globally and virus containment measures eased, global economic policy uncertainty declined further during the quarter. It is now at its lowest level since Q3 2018. Declining economic uncertainty is not generally supportive for the gold price.



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Contributors

Michael Joynson
Head of Market Insights
michael.joynson@invesco.com

Emma McHugh
Strategist, Market Insights
emma.mchugh@invesco.com

David Scales
Senior ETF Investment Editor
david.scales@invesco.com

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Data as at 30 June 2021, unless otherwise stated.

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