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Market performance and macro factors

Gold report

Q1 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 Q1 2021

Gold price decreased

-10%

in Q1 2021, its worst start to a year since 1982

On a 12-month basis, gold delivered an

8.3%

return, but that ranks it ahead of only cash and government bonds for the year

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

-0.63%

its highest in nine months

The first quarter of 2021 saw the US Dollar rise

3.7%

as relative economic momentum swung firmly in the US's favour

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.

Market performance

Macro factors

Quarterly price performance

Gold fell 10% in Q1 2021, its worst start to a year since 1982. It finished this most recent quarter at $1,708 per Fine Troy ounce, having dipped below $1,700 twice in March and returning to levels not seen since June. The metal's price did not breach $1,651, however, which would have put the metal into a technical bear market (20% below August 2020's all-time high).

The quarter's gold price weakness has been due primarily to rising nominal and real bond yields, which has also encouraged USD strength. Investors have been regaining their appetite for risk as the Covid vaccination programme rolls out and the economic growth outlook improves.

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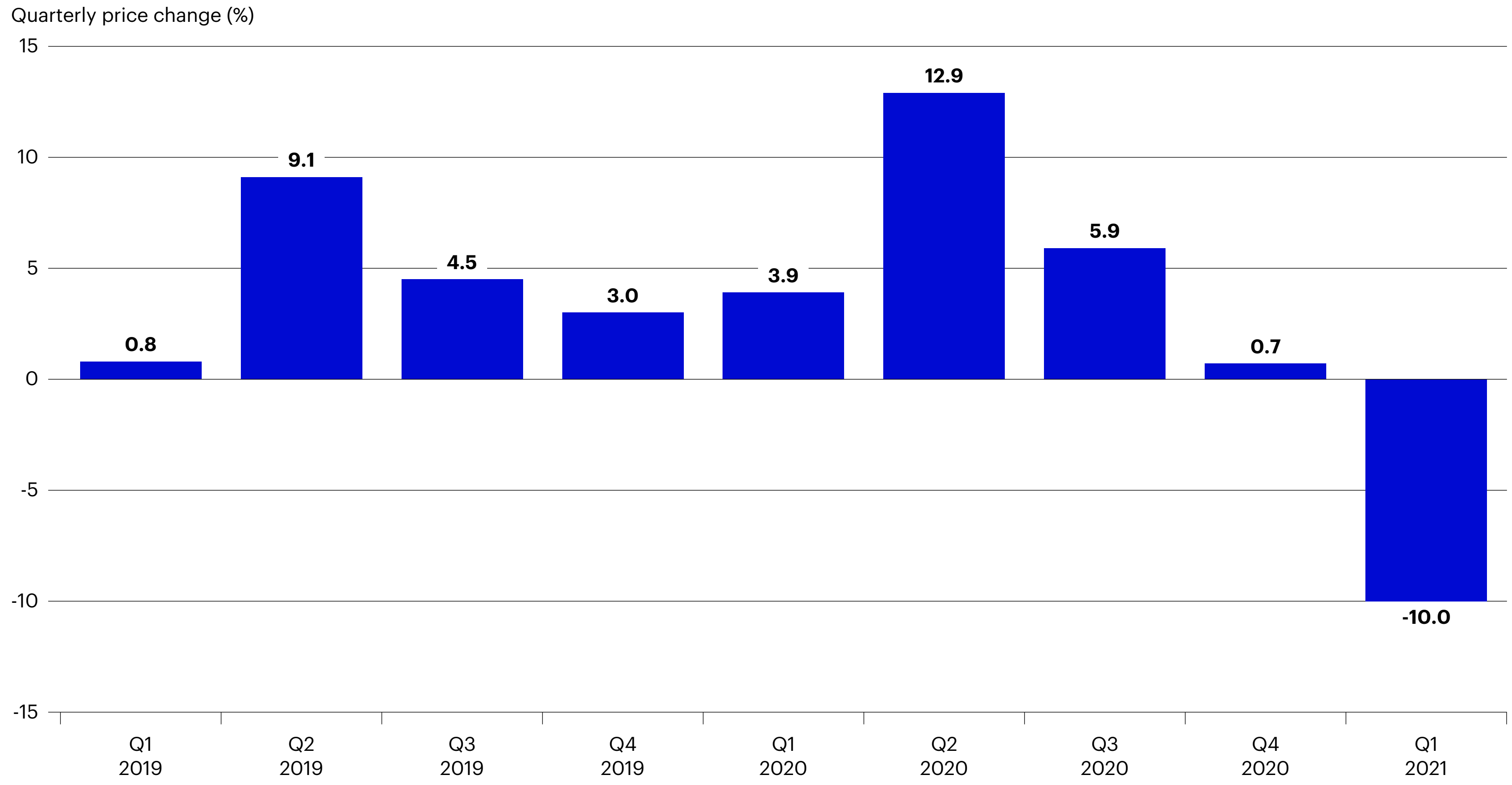
-10%

in Q1 2021, its worst start to a year since 1982

Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, from 31 December 2020 to 31 March 2021.

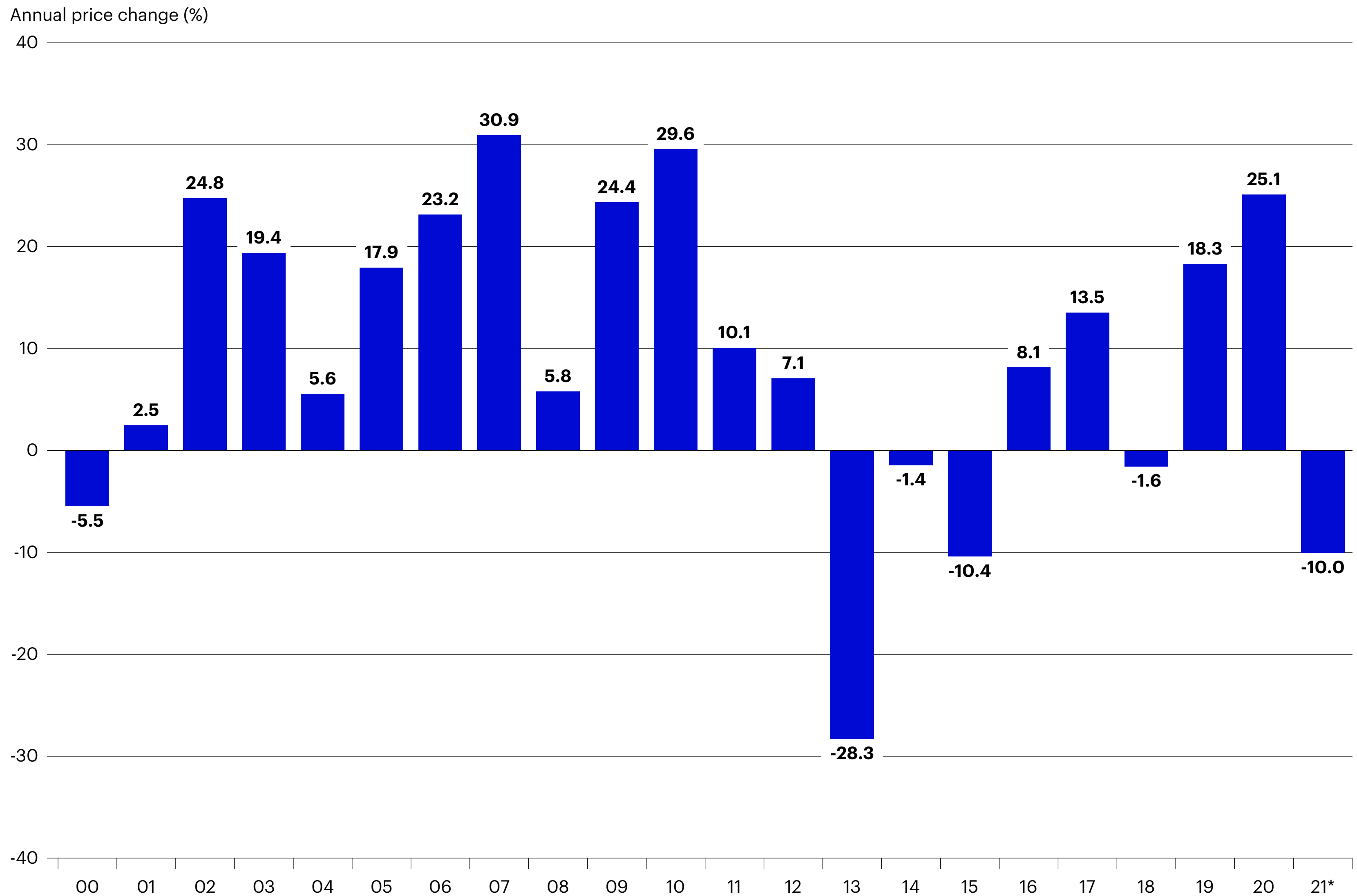
Quarterly price returns

The first quarter of this year saw three consecutive months of negative returns. Q1 was the first negative quarter since Q3 2018 and the worst quarterly performance since Q4 2016. In terms of bad starts to the year, you have to go back to 1982, when gold returned -19.5%, for a more inauspicious start to a year.



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 March 2021.

Annual price returns



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 March 2021. *2021 is YTD returns.

Market performance

Quarterly price performance

Quarterly price returns

Annual price returns

Asset class returns

Relative strength of the gold price

Gold price return, nominal and adjusted for inflation

G10 currencies

Macro factors

Gold price and real bond yields

Gold price and negative-yielding debt

Gold price and US interest rates

Gold price and inflation expectations

Gold price and the US Dollar

Gold price and economic risks

Asset class returns

In a risk-on quarter, gold performed poorly compared to other asset classes, despite underlying weakness in government bonds and investment grade credit, with the former having their worst quarter at a global level since 1987. Broad commodities generated the strongest returns as economically sensitive commodities, such as oil and copper, gained from heightened expectation of a robust economic recovery. Equities also had a good quarter.

On a 12-month basis, gold delivered an 8.3% return, but that ranks it ahead of only cash and government bonds for the year. Gold has fallen down the performance table as the bear market numbers of Q1 2020 rolled off and risk assets this quarter rallied strongly.

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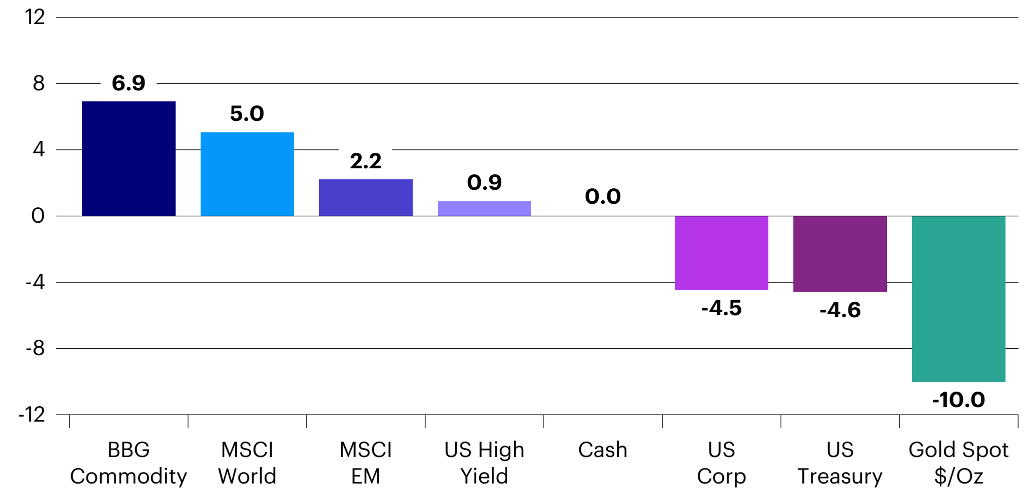
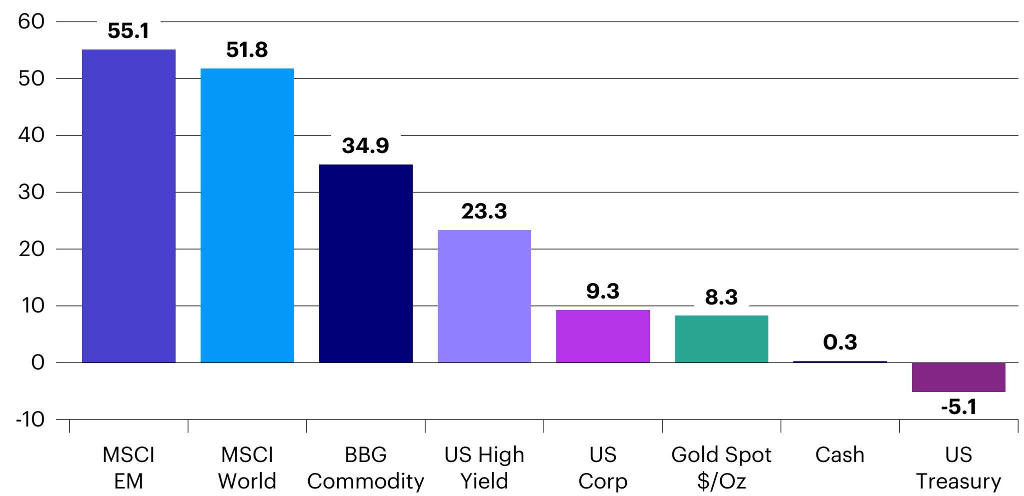
Quarterly asset class returns (%)



12-month asset class returns (%)



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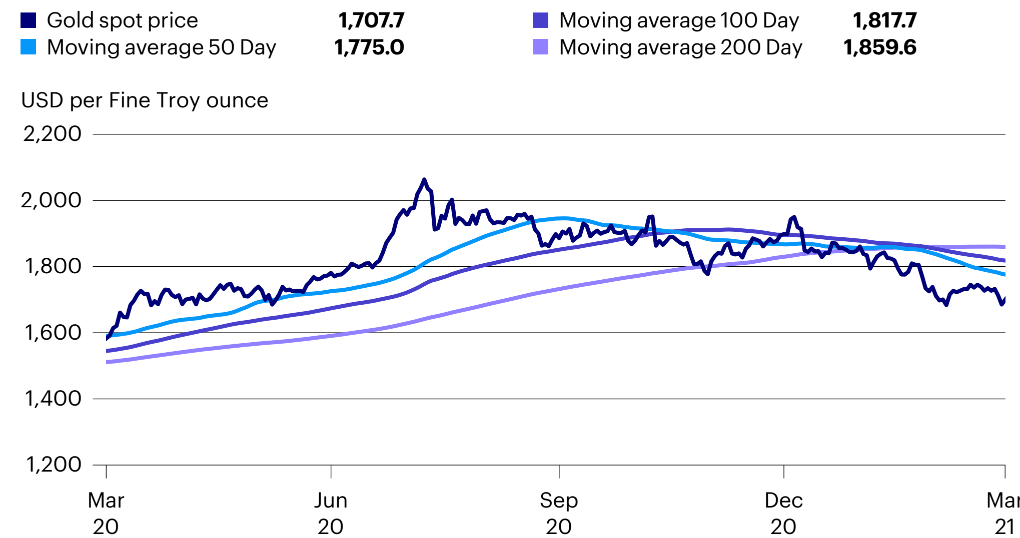
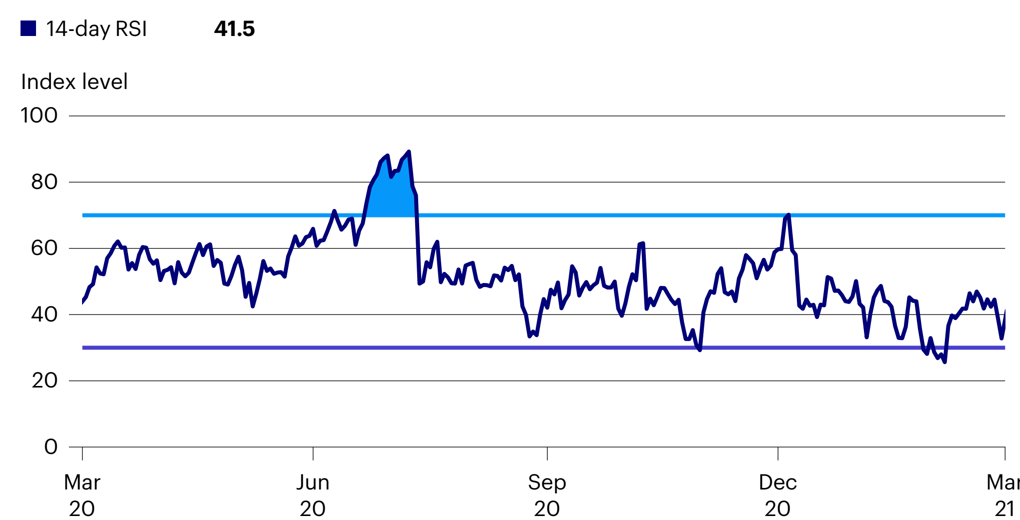
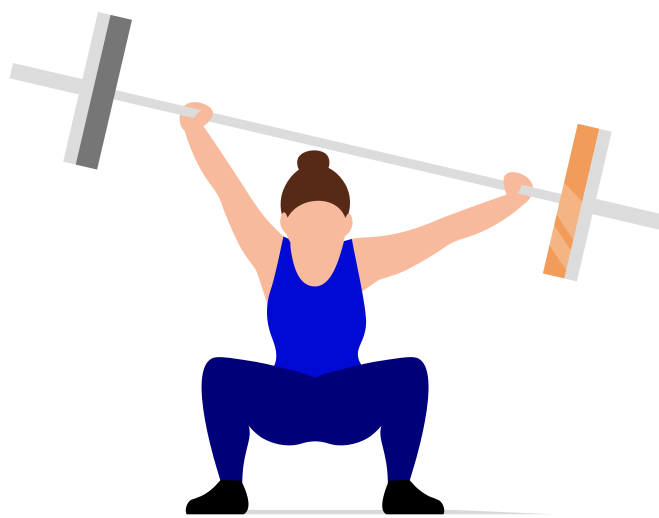
Relative strength of the gold price

The pace of gold selling in the quarter meant there were several days where the metal dropped into oversold territory. The moving average (MAV) chart shows that the 50-day MAV, having already crossed the 100-day series in Q3 2020, continued its negative momentum, falling below the 200-day MAV at the end of January 2021, known in technical terms as the 'death cross'.

Stabilising bond yields and some easing in USD strength helped gold recover off its lows, but there would likely need to be a sustained deterioration in the economic outlook for technical signals to become unanimously positive on gold.



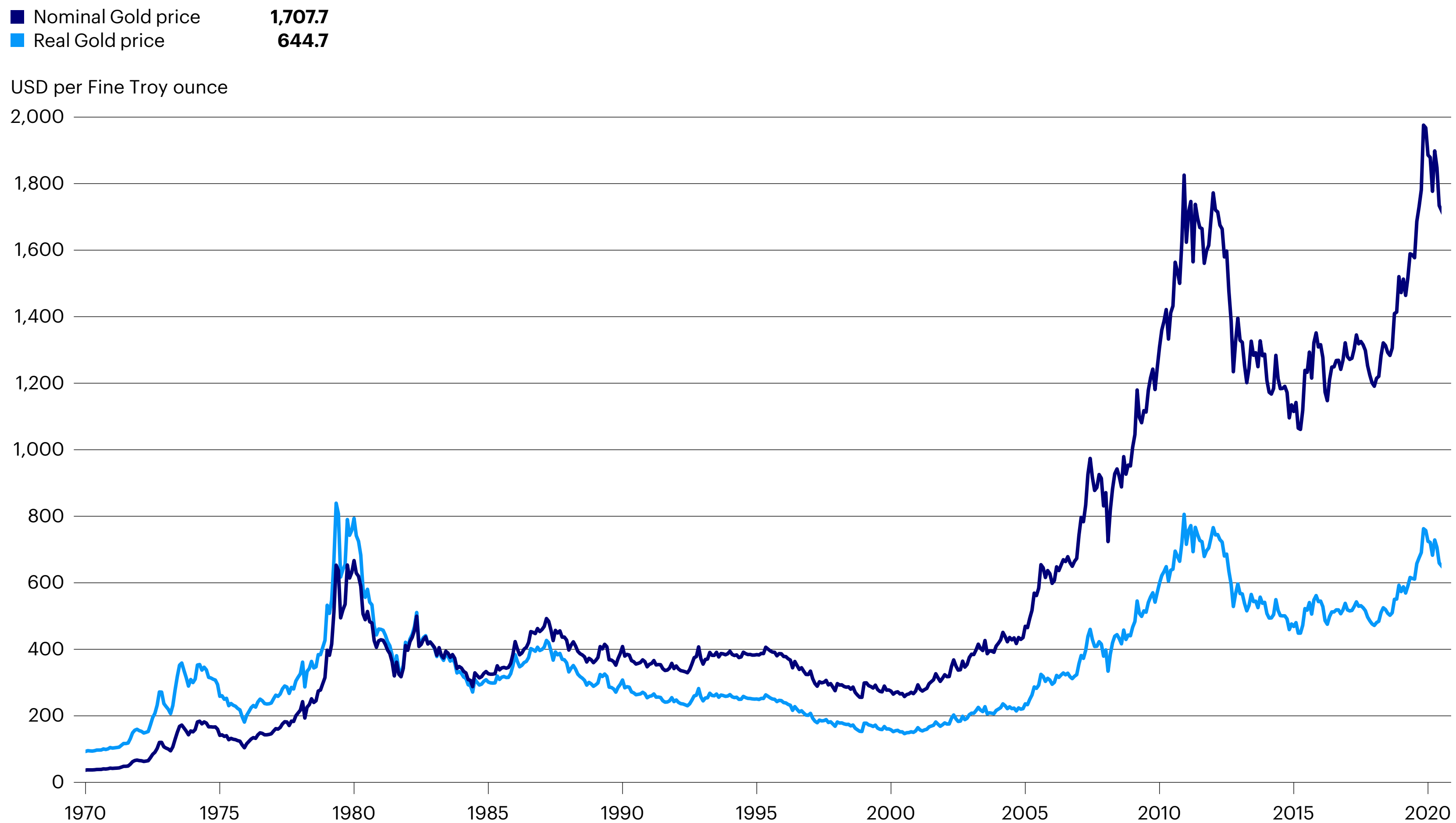




Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 March 2021.

Gold price return, nominal and adjusted for inflation

With the outlook for economic growth improving, the attention now turns to inflation. US CPI increased 1.7% in the first three months of the year – the largest quarterly increase in a decade – but gold did not assume the inflation-hedge often associated with it. In real terms, gold fell by 11.5% over the quarter.



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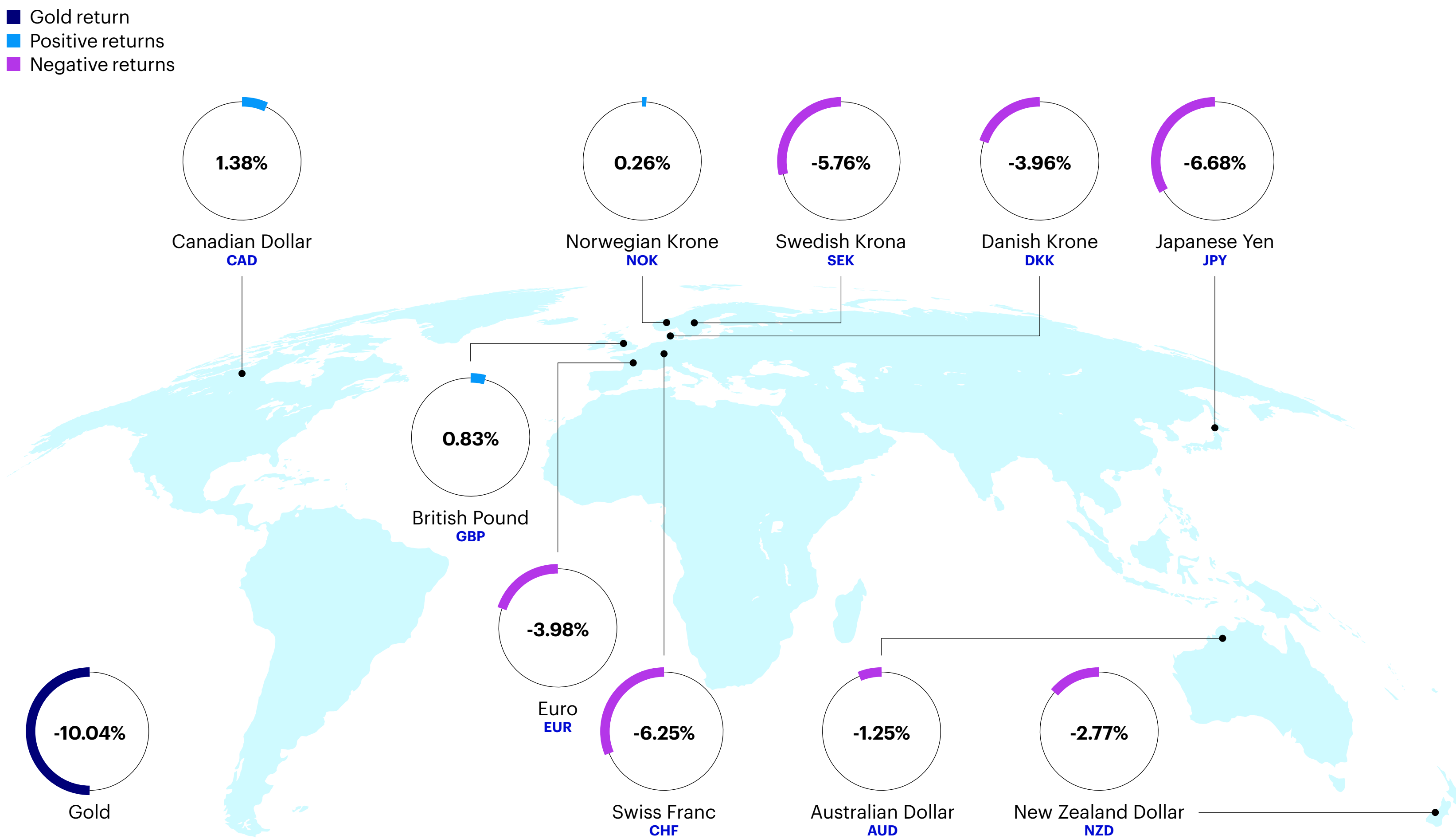
G10 currencies

After a number of weak quarters, the US Dollar performed well during Q1 2021, rising against most of the G10 currencies. Fiscal-policy-driven upgrades to the US economic outlook, good progress on the rollout of the vaccination programme, rising interest differentials and an unwinding of short positions underpinned the gains. Perhaps unsurprising given the quarter's risk-off environment, the Japanese Yen and Swiss Franc saw the weakest returns.

Q1 returns of gold and G10 currencies in USD (%)



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Gold price and real bond yields

A rapid rise in the real yield in US Treasuries from their all-time low (-1.1%) at the start of January was a key driver in a weaker gold price during the quarter. Expectations of a strong US economic recovery on the back of the recent approved pandemic relief packages, a supportive monetary policy stance from the Federal Reserve and good progress on the rollout of the vaccination programme all helped push real yields higher. An increase in bond yields increases the opportunity cost of holding gold, given it is a non-income-paying asset.

The yield on the US 10-year TIPS ended the quarter at -0.63%, its highest in nine months, and the positive momentum is expected to continue as the US economy returns to something close to normality in the coming quarters.

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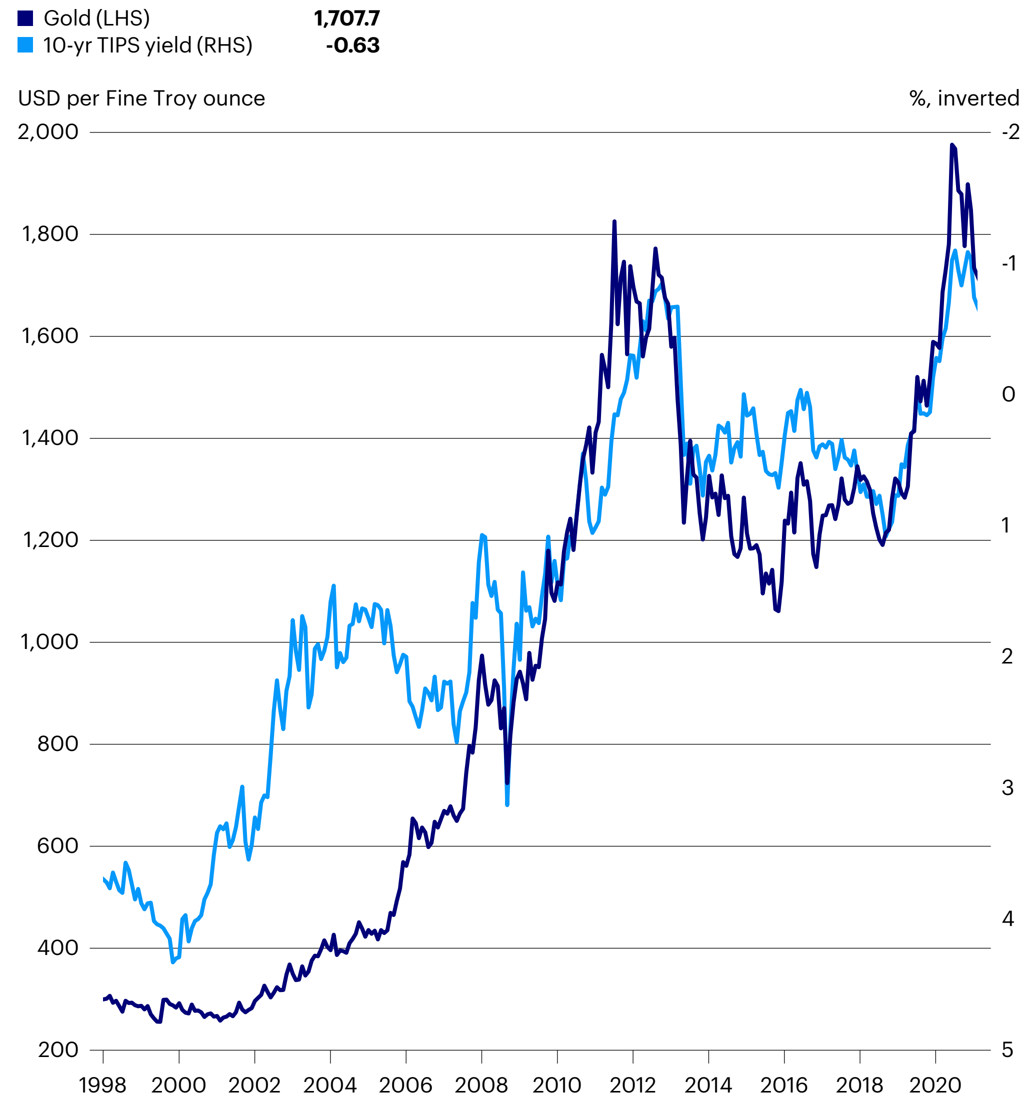

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Market performance

Macro factors

Gold price and negative-yielding debt

The stock of negative-yielding debt globally, while still elevated, fell from just over $17.8 trillion to around $13.4 trillion. At just over 20%, this is still a significant portion of the Bloomberg Barclays Global Aggregate Index of investment grade debt.

All countries with negative policy rates, notably Japan and the Eurozone, are still able to issue short-term government debt with negative yields, while even in longer-dated maturities, countries such as Germany continue to see yields firmly in negative territory. Currently, the majority of the negative-yielding debt globally is denominated in either Euro (66%) or Yen (30%).

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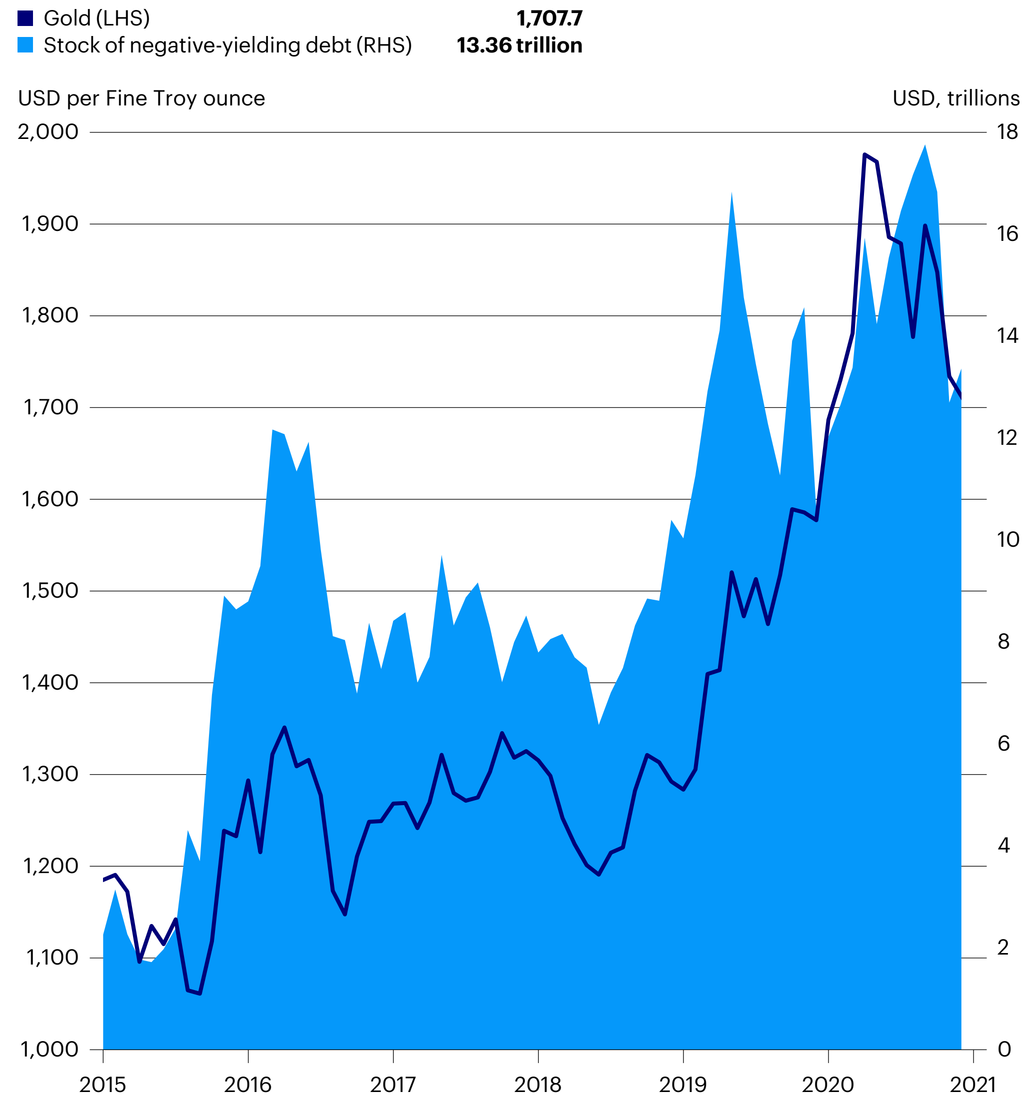

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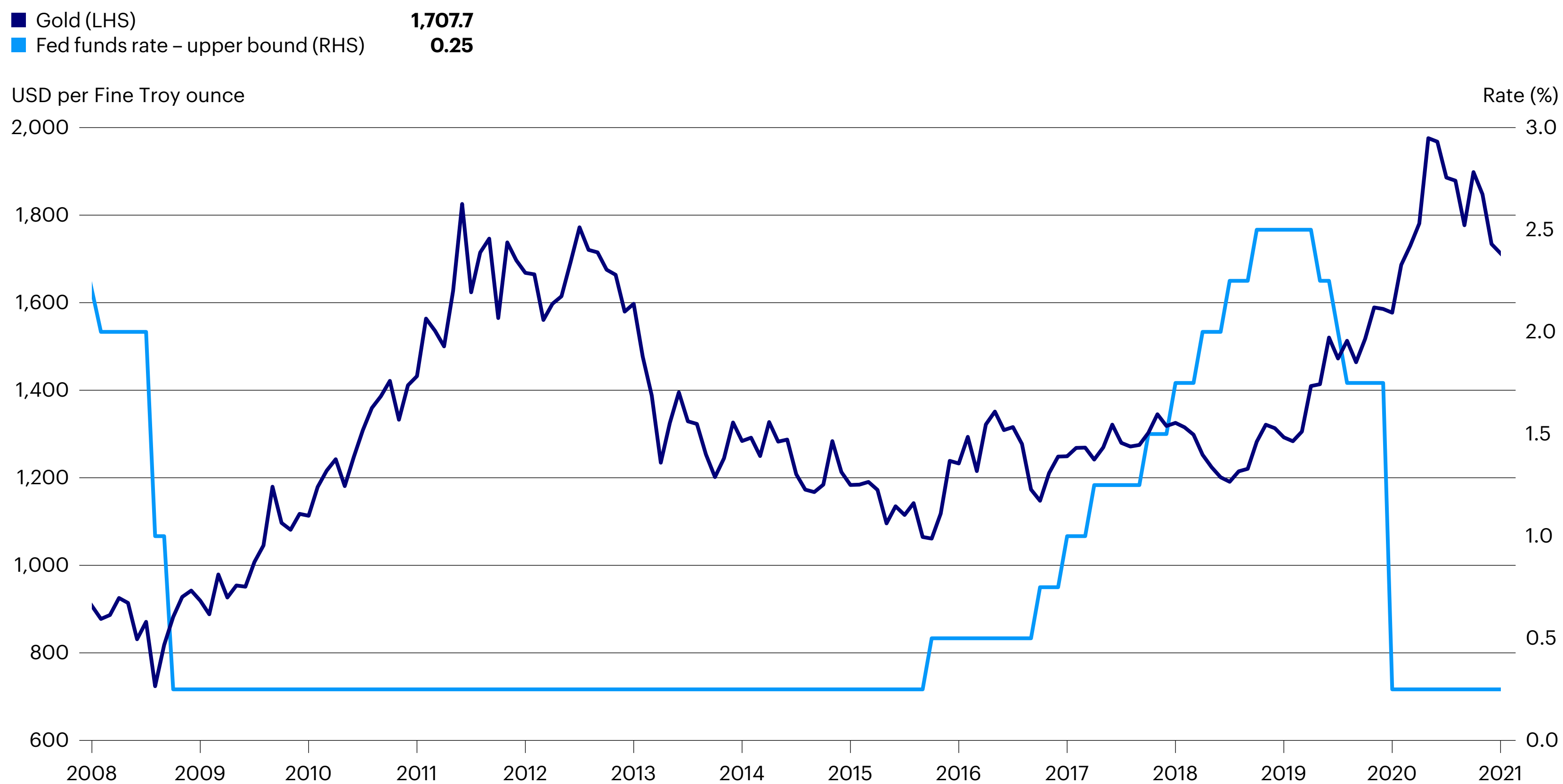
Market performance

Macro factors

Gold price and US interest rates

The Fed Funds rate may have remained at 0.25% in the quarter, but there was considerable speculation about the timing of the next rate hike, reflected in the rise of longer-dated bond yields. The market expects the first rate increase to occur in 2022. However, while the latest dot plot released in March showed more members of the Federal Reserve seeing a rate hike in 2022, a clear majority still forecast the Fed Funds rate remaining unchanged until the end of 2023. With the Fed apparently dispelling speculation of an earlier rate hike, gold was granted a slight reprieve from its downward trajectory at the end of the quarter.



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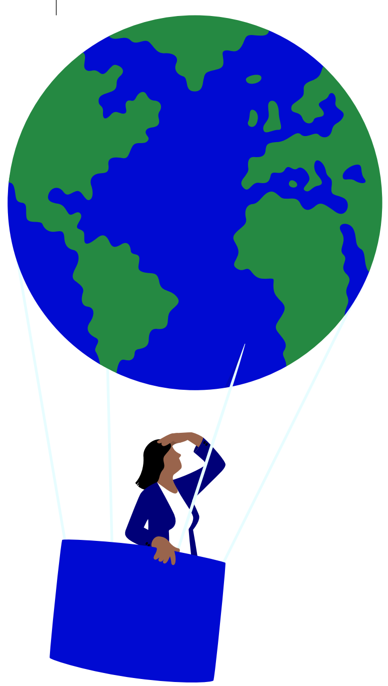
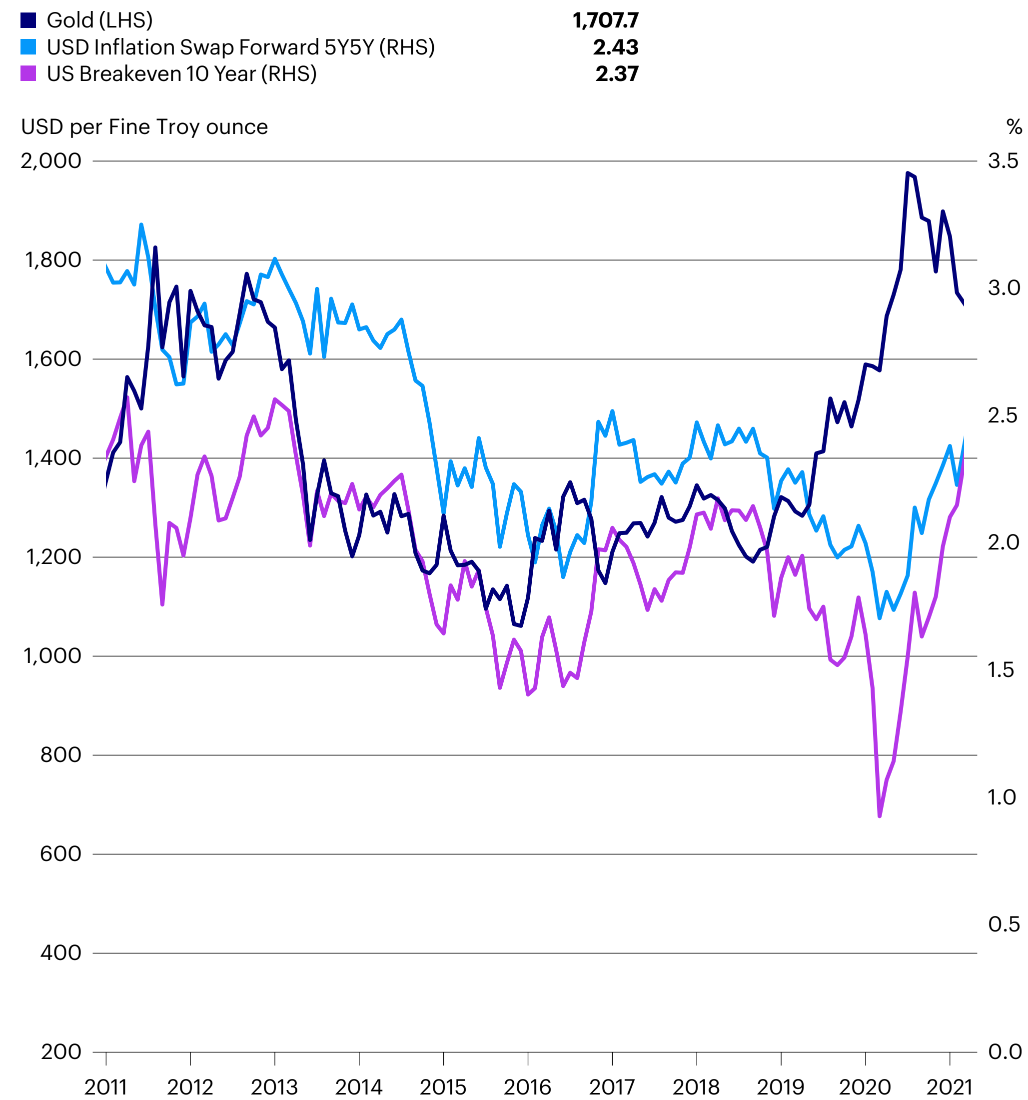
Gold price and inflation expectations

Markets are pricing higher inflation expectations with the US 5y5y inflation swap ending the quarter at 2.4%, having been at 1.7% a year earlier. US breakeven inflation has made an even sharper move, with the 10-year at its highest level in eight years, up to 2.3% from 0.9% over the past 12 months.

Despite higher expectations for inflation, gold has not moved in response. It may be that, as with the Fed, the market is waiting for inflation to come through in the data or that investors no longer see it as the inflation-hedge it was once perceived to be, particularly when the rise is inflation is expected to be relatively contained.





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Gold price and the US Dollar

After an extended period of weakness during 2020, the first quarter of 2021 saw the US Dollar regain some of its losses, rising 3.7%, as relative economic momentum swung firmly in the US's favour. Being short the USD was very much a consensus view, so an unwinding of some of these short positions, against a backdrop of the increasing yield attractions of the US Treasury market, also helped support the greenback.

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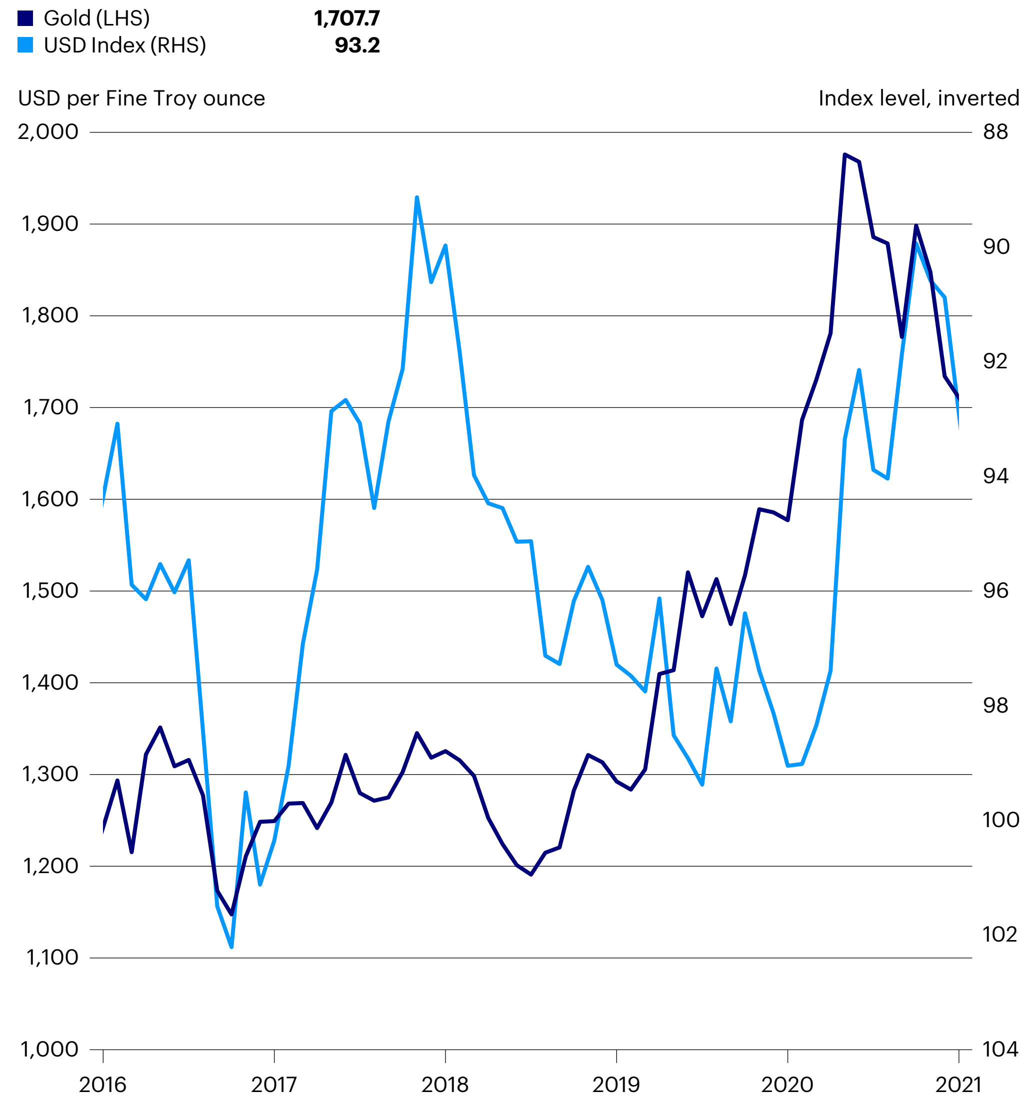

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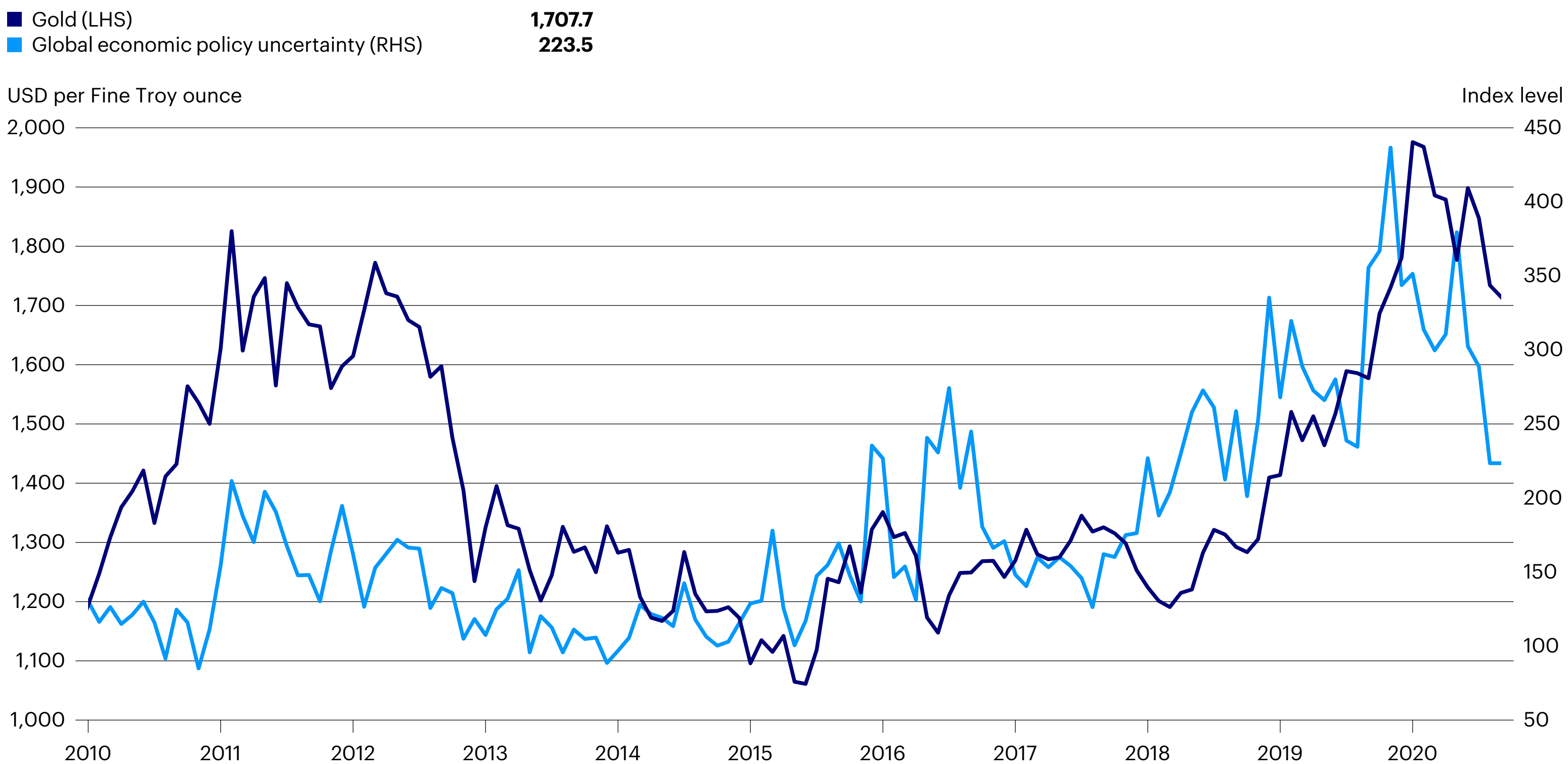
Gold price and economic risks

Global economic uncertainty fell materially in the first quarter, returning to pre-pandemic levels. Policy uncertainty has continued to recede (outside of the 2020 US election period) since it peaked in May of last year.

As the largest economies have begun to show signs of recovery, supported by continuing fiscal and monetary stimulus and the vaccination programme rollout, it is hardly surprising to see the level of uncertainty decline. A clearer outlook reduces the attraction of assets such as gold, which have historically provided a safe haven during periods of heightened uncertainty.



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Data as at 31 March 2021, unless otherwise stated.

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