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Market performance and macro factors

Gold report

Q3 2022

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 Q3 2022

Gold price return in Q3

-8.1%

Gold return, year to date

-9.2%

Fed funds rate

3.25%

at end of Q3

4.50%

at end of 2022 (current forecast)

US real yields

1.68%

Data: Bloomberg, as at 30 September 2022.

Market performance

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The gold price fell in Q3, the second-consecutive quarter of negative performance, as rising bond yields and the continued strength of the US dollar weighed on the precious metal.

Macro factors

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The Fed continued to raise interest rates during the quarter and is expected to increase rates further into year-end, as the central bank tries to bring down inflation, despite signs the economy is softening.

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

Gold ended September at $1,661, 8.1% lower than at the start of the quarter as US real yields and a yet stronger USD kept downward pressure on the gold price. The metal had three consecutive months of negative returns and fell to $1,622, its lowest price since March 2020, before recovering in the final days of the quarter when confidence in central banks took a knock.

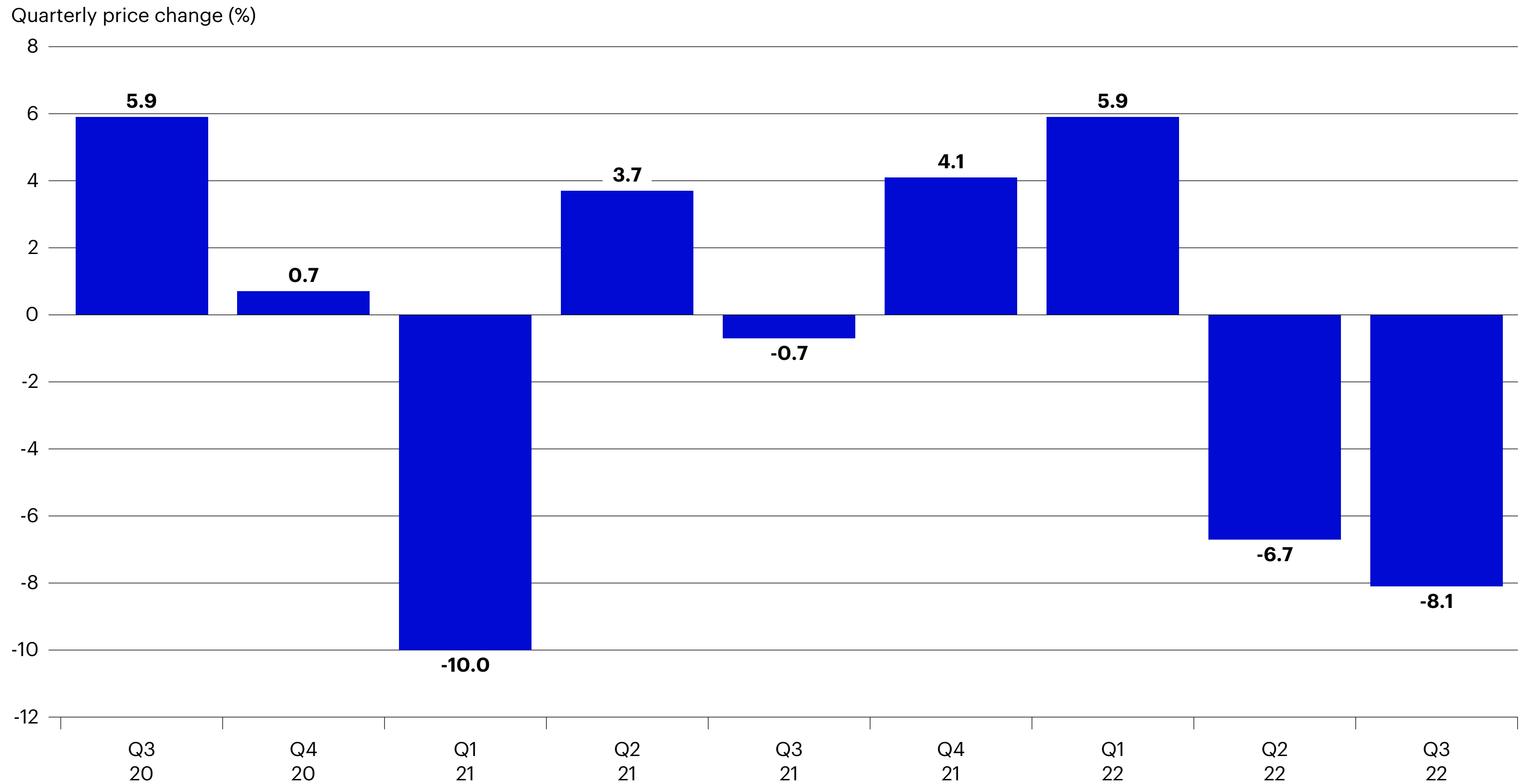
Gold price return in Q3

-8.1%

Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, from 30 June to 30 September 2022.

Quarterly price returns

This was the second consecutive quarter of negative performance for gold following its return of -6.7% in Q2. The 8.1% decline in Q3 was the metal's worst quarterly performance since Q1 2021 when it also struggled against rising real yields (on the back of the Covid-19 vaccine) and a stronger USD.



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 30 September 2022.

Market performance

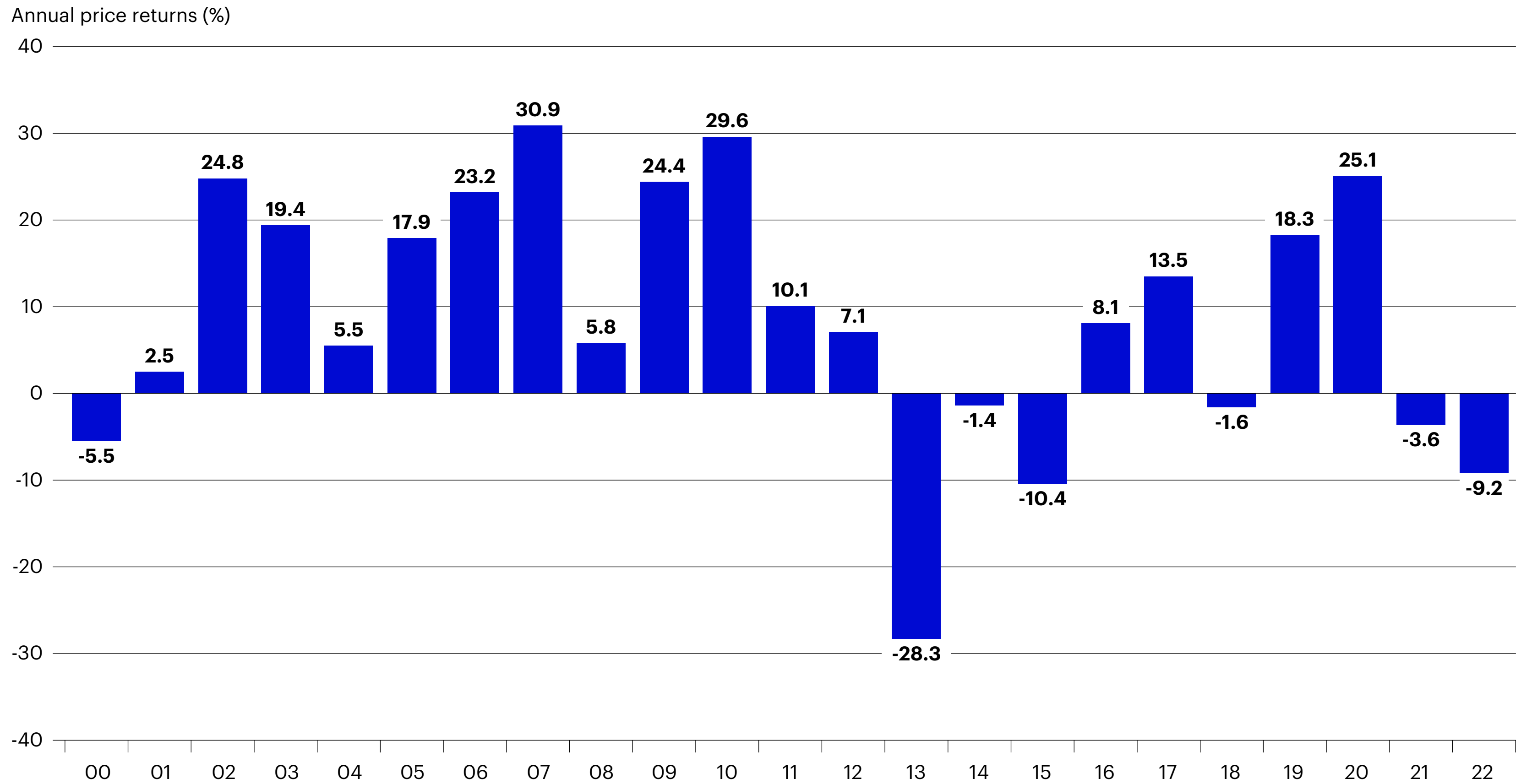
Macro factors

Annual price returns

Further poor performance means that year-to-date gold has returned -9.2% and current forecasts for the macroeconomic environment suggest continued headwinds in the near term as the Fed continues to emphasise its focus is on managing inflation down, even if there are signs that the US economy is beginning to soften.

Gold return, year to date

-9.2%



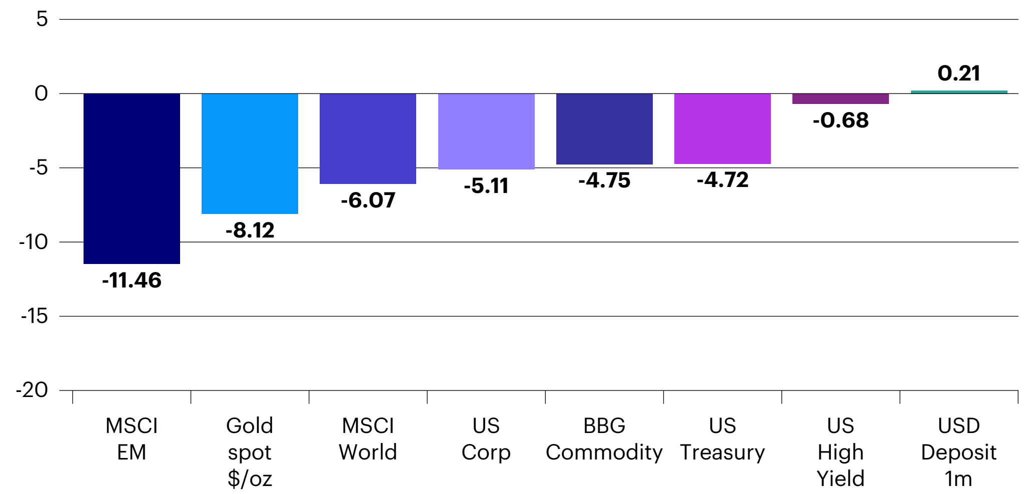
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD. 2022 is for the year to 30 September 2022.

Asset class returns

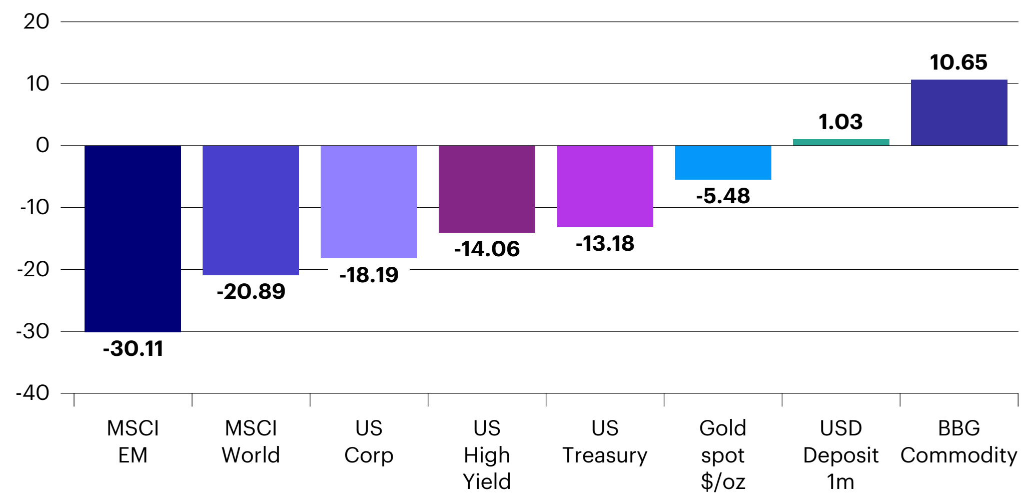
The most recent quarter continued the trend of Q2 with all major asset classes delivering negative returns. The Fed has been raising rates since March, making deposit rates increasingly positive although obviously still far behind inflation. Unsurprisingly, emerging market equities and gold came in at the bottom of the rankings as the US dollar has continued to strengthen on the back of widening interest-rate differentials.

On a 12-month basis, gold has returned -5.5% whereas the wider commodities complex still shows a positive return of 10.6%. The broader commodity performance is likely to continue to fade as we move further away from Russia's' initial military actions in February. Rising inflation has been difficult for most investments, directly and in the anticipation of higher rates. US dollar strength coupled with concerns over Chinese growth has caused emerging market equities to underperform.

Quarterly asset class returns (%)



12-month asset class returns (%)



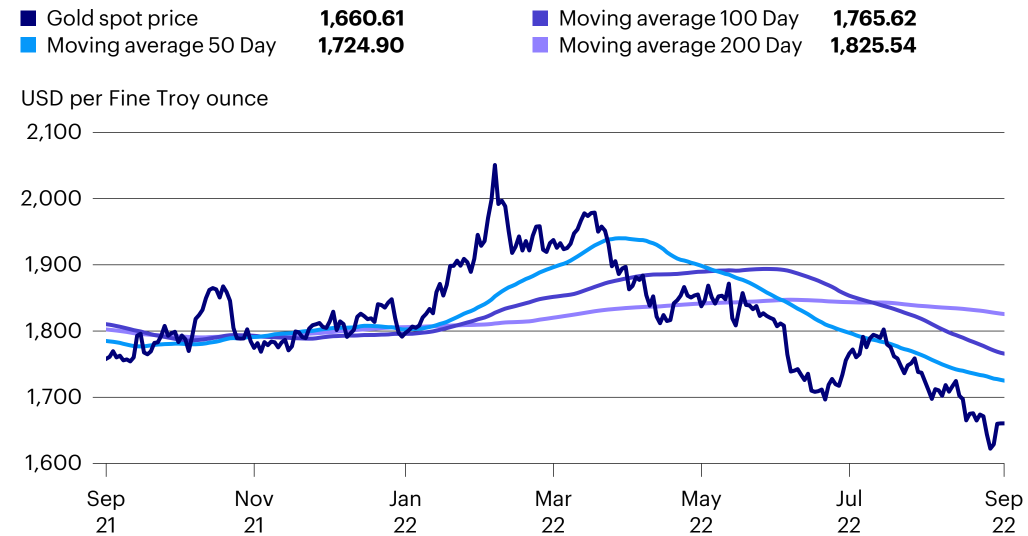
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 30 September 2022.

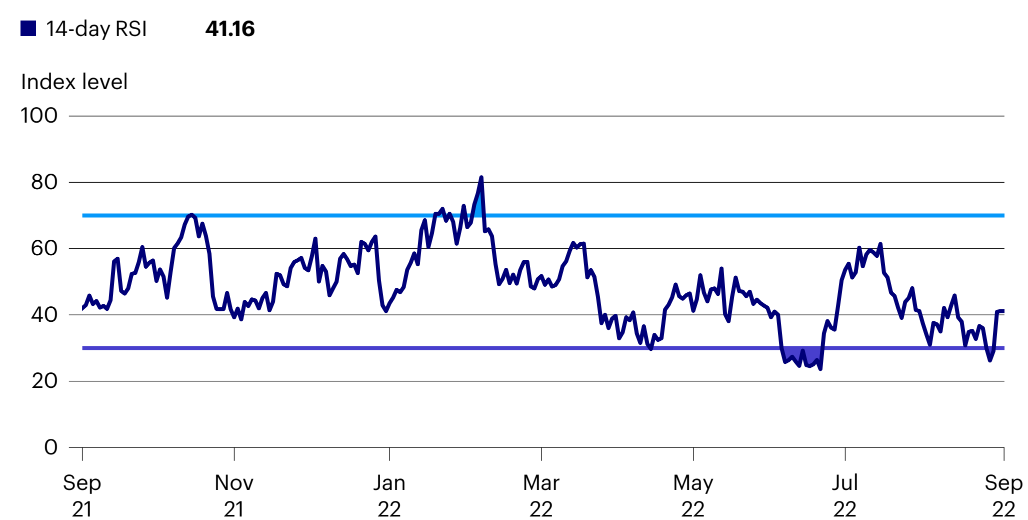
Market performance

Macro factors

Relative strength of the gold price

Gold's technicals worsened during the quarter as the shorter moving averages (both 50- and 100-day) crossed the 200-day moving average. At the start of July, when the 50-day crossed the 200-day series, gold sold off sharply into oversold territory on the 14-day relative strength index. Gold rebounded before sliding into oversold territory again at the end of the quarter, then rallying on Bank of England market interventions.

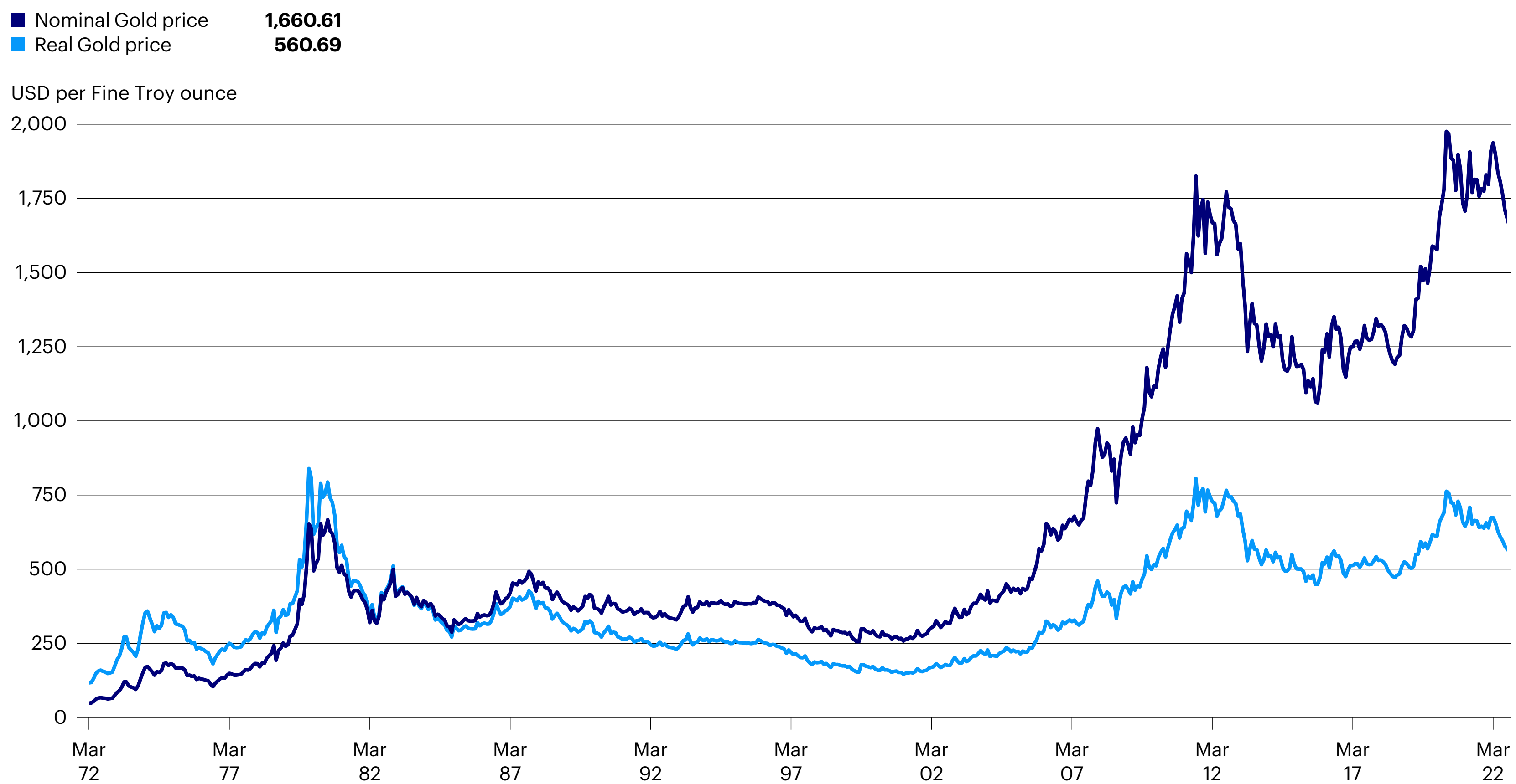




Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 September 2022.

Gold price return, nominal and adjusted for inflation

Although year-on-year inflation data remains strong in the US, the month-on-month picture shows that recently there has been a plateauing. For gold this means that the relative real return performance is showing signs of near-term stabilisation also falling -8.1% in Q3. On a 12-month basis, gold has returned -12.5%.



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 September 2022.

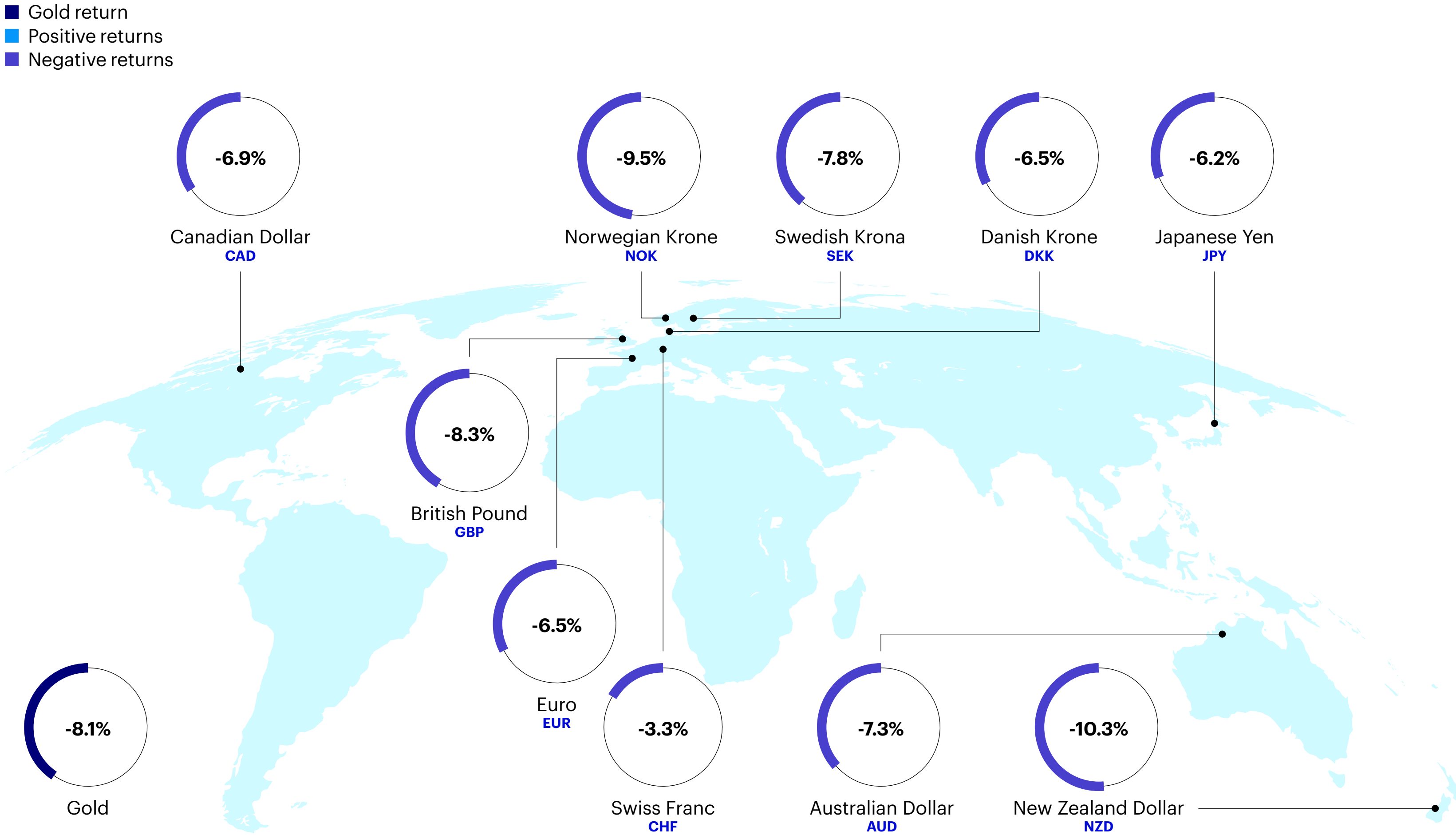
Market performance

Macro factors

G10 currencies

All major currencies were weaker against the USD in the quarter as the Fed added a further 150 basis points to its policy rate. The traditional currency 'safe havens' of the Swiss franc and Japanese yen were the better currency performers in Q3, returning -3.3% and -6.2% respectively. This is despite the Bank of Japan maintaining its rate at -0.1% (where it has been since 2016). All European central banks now have positive policy rates as the Swiss National Bank raised its rate to 0.5% from -0.25% in September and the ECB ended the quarter with its deposit rate at 0.75% having started Q3 at -0.5%. As gold is non-yielding, it has struggled to compete.

Q3 returns of gold and G10 currencies in USD (%)



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Market performance

Macro factors

Gold price and real bond yields

US real yields strengthened noticeably over the quarter, to 1.68%, the highest for 13 years, as markets priced in further rate hikes by the Fed. This was based on the continuous message from the Fed that it was going to pursue its fight against inflation until the job was done, suggesting yields will remain elevated for the foreseeable future. That the US has also embarked on quantitative tightening over the past few months is also a boost to real yields as inflation expectations are falling back to their long-term averages.

US real yields

1.68%

Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 September 2022.

Gold price and Fed balance sheet

Since September, the Fed has begun reducing its balance sheet runoff to its maximum of $95 billion per month, as announced in May. At the end of the quarter, the Fed balance sheet was $8.8 trillion, slightly higher than at the end of 2021. Liquidity has given rise to concerns about the Fed ending its quantitative tightening programme early, the central bank itself expects the programme to run for several years but still exit at a much higher level than pre-pandemic. Gold may benefit from any Fed-induced liquidity issues.

Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 30 September 2022.

Market performance

Macro factors

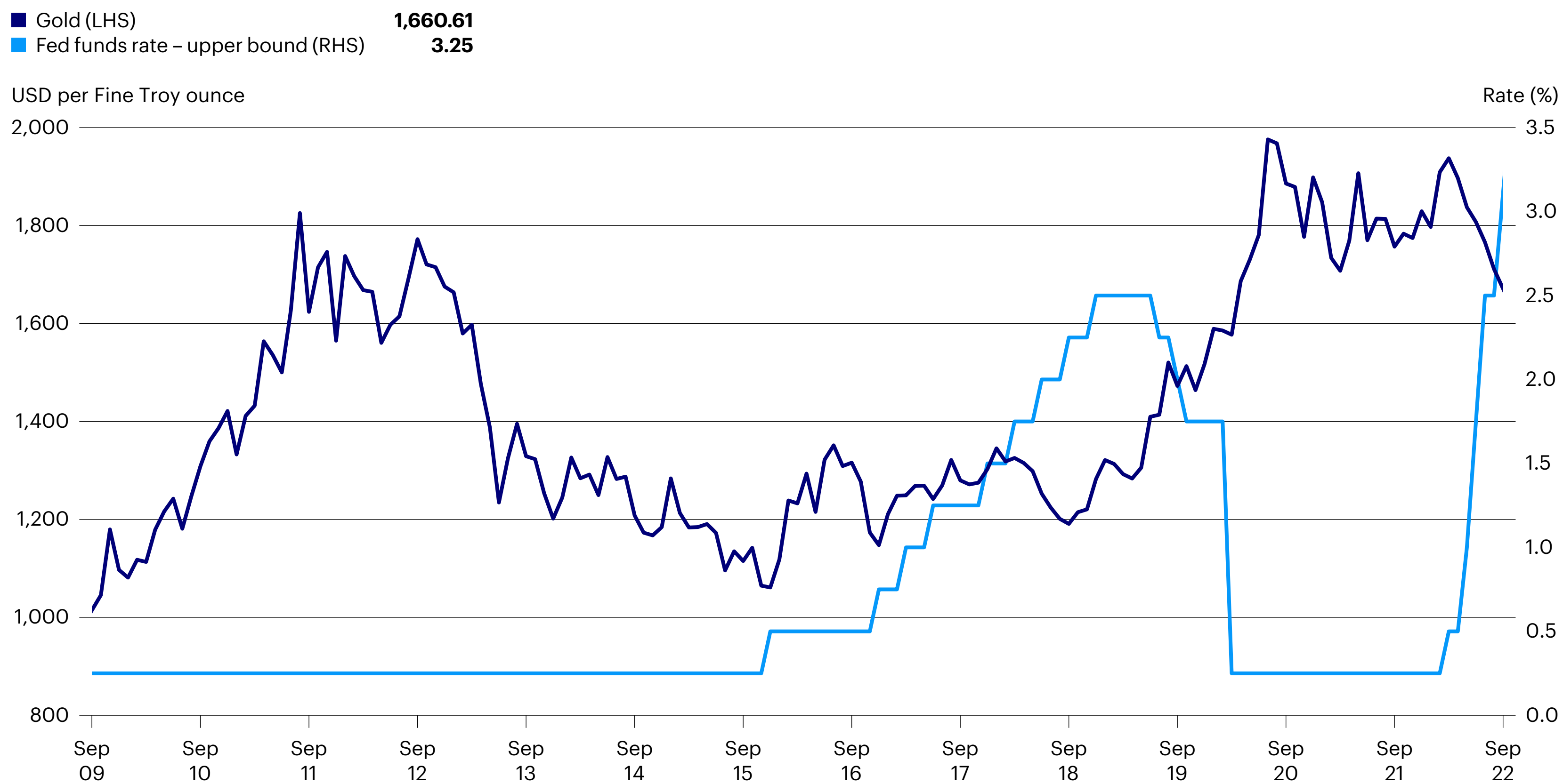
Gold price and US interest rates

The Fed funds rate ended the quarter at 3.25%, having added 75 basis points (bps) both at the July and September meetings. Current forecasts are for a further 75 bps to be added at the November meeting and 50 bps at the December meeting, meaning the US' policy rate would be at 4.5% at year end. Stronger labour market data is keeping year-end 2023 estimates above 4.5% (having peaked at 4.75% in Q1 2023), despite softening in other economic series.

Fed funds rate

3.25%
at end of Q3

4.50%
at end of 2022 (current forecast)



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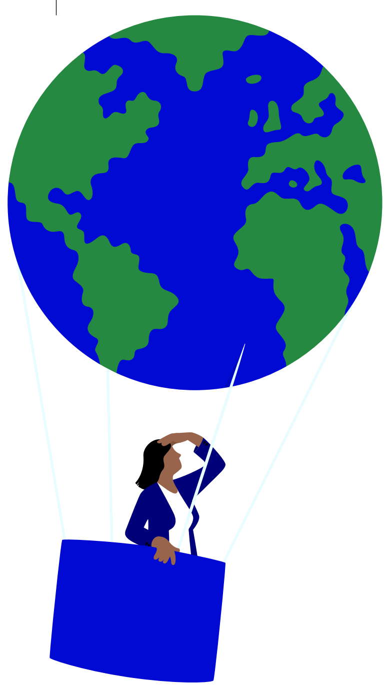
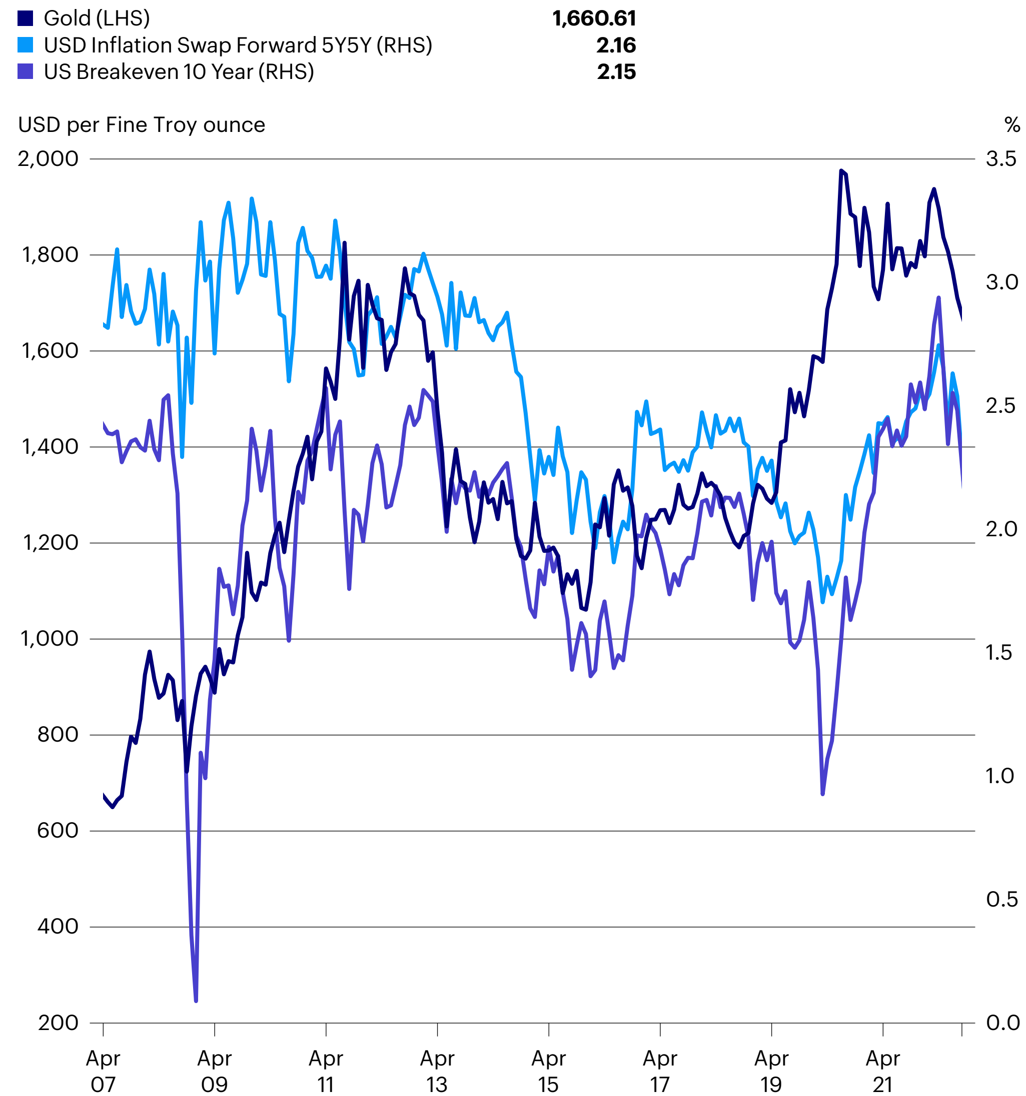
Gold price and inflation expectations

Inflation expectations have fallen back to 2.2%, a clear roll over from the peak in April of this year (2.9% for the 10yr breakeven and 2.7% for the 5y5y swap), albeit still above the long-term average. That expectations are falling is a signal that markets have confidence that the Fed will manage inflation down in the future albeit in the nearest-term inflation remains elevated as recession risk has risen.





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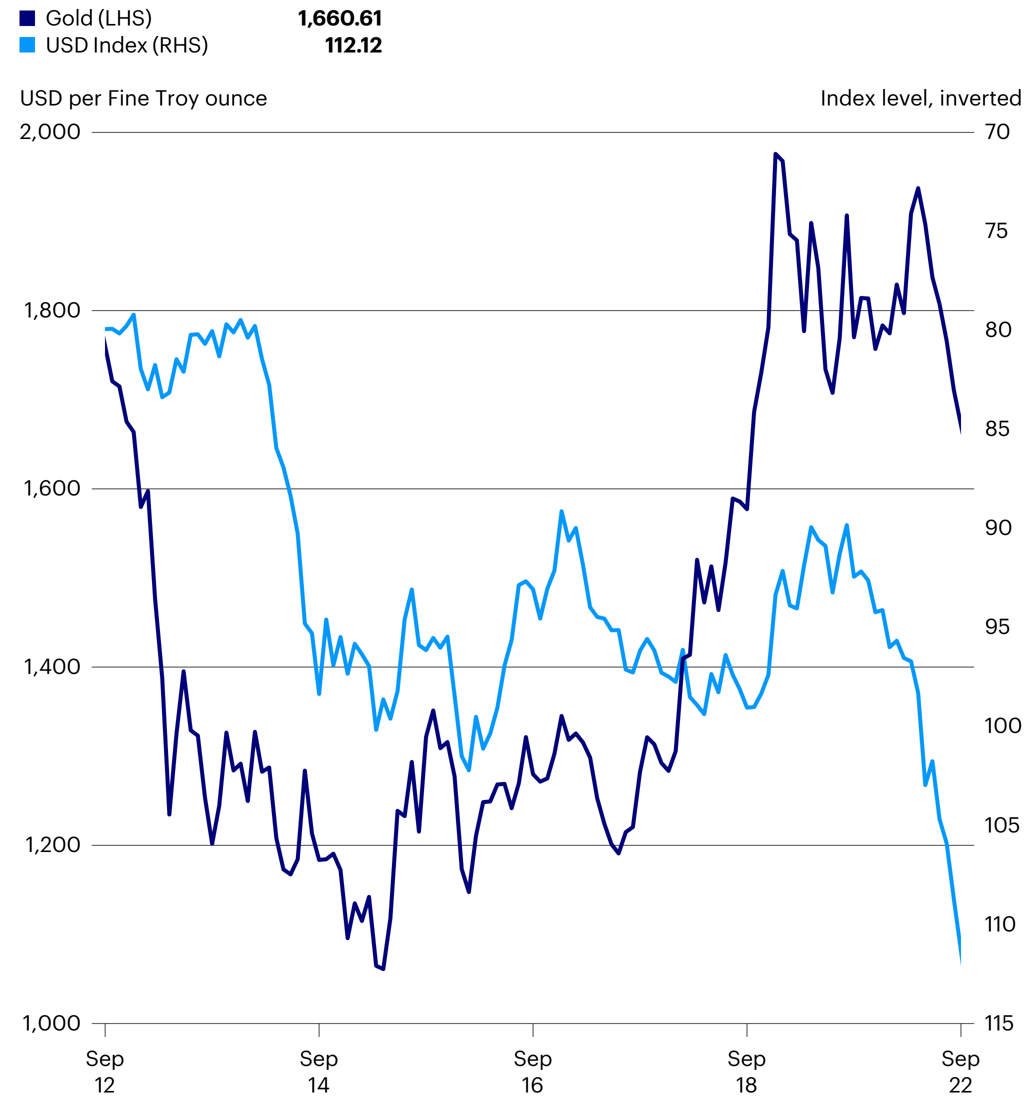
Market performance

Macro factors

Gold price and the US Dollar

The USD continued to strengthen as the Fed continued to add rate hikes as expected and more than other central banks: the ECB added 125bps and is 58% of the USD (DXY) index; Japan's rate was unchanged and is 14% of the index; the Bank of England added 100bps and is 12% of the index. The Bank of Canada added 175bps to its policy rate in the quarter, the only central bank in the USD index (9%) to hike more than the Fed, but CAD still weakened against the USD. The USD also benefitted from political events in the UK and Italy in September.



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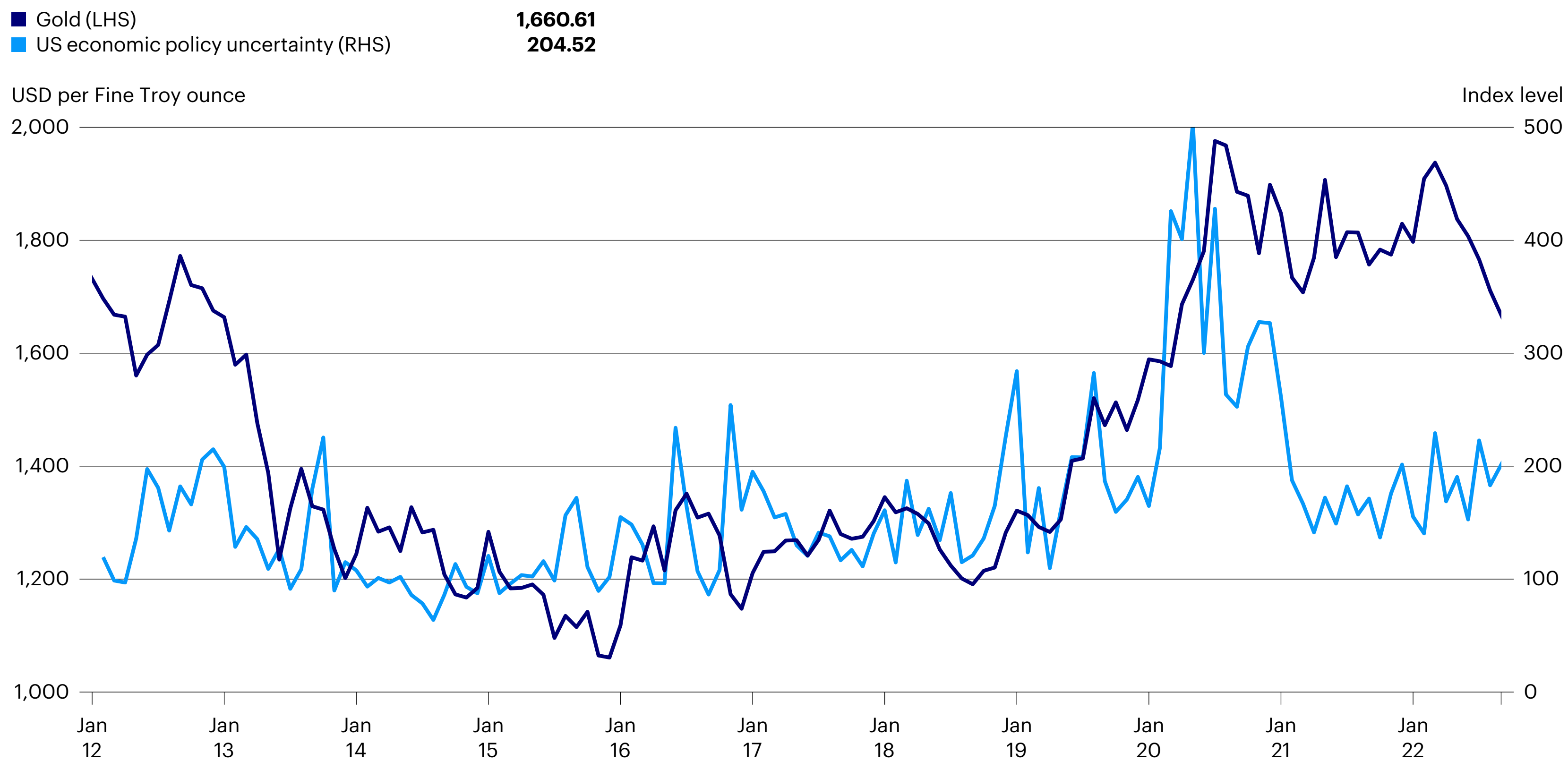
Gold price and economic risks

US economic uncertainty has been trending higher through 2022 as the Fed has been tightening economic conditions but also Biden signed the Inflation Reduction Act into law in Q3 2022. Previously titled the Build Back Better plan, the reworked Inflation Reduction Act is expected to reduce the US deficit by up to $300 billion over the course of the following 10 years covering areas from health to climate change.



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Data as at 30 September 2022, unless otherwise stated.

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