Invesco

Market performance and macro factors

Gold report

Q1 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 Q1 2022

Gold price rose in Q1	Gold price return in past 12 months	US inflation at 40-year high at the end of February	USD strengthened in Q1
5.9%	13.5%	7.9%	2.8%

Data: Bloomberg, as at 31 March 2022.

Market performance

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Gold was one of the best-performing assets in Q1, rallying to within touching distance of its all-time high as Russia's invasion of Ukraine caused many investors to seek relative safe havens. Commodity prices were higher across the board, while credit and emerging market equities languished at the bottom of the quarterly performance table.

Macro factors

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The spike in commodity prices further increased what was already high inflation; year-on-year the US is now suffering a 40-year high. The Fed raised interest rates in March, and the market is now weighing up the odds of how much more tightening the central bank will be able to do this year considering current global conditions. Uncertainty and turmoil are at least partially countering the headwinds from higher interest rates, bond yields and the US dollar.

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 returned 5.9% in the first three months of the year, its best quarterly performance since Q3 2020, when the precious metal reached an all-time high. Gold began this latest quarter rather tamely but rallied strongly to within $11 of its record high. Despite then falling more than $100, the gold price ended the quarter at $1,937. The average daily price for the quarter was $1,879, compared to an average of $1,868 in Q4 2021.

Gold's rally this quarter was driven by the events unfolding in Ukraine as well as the uncertainty around the possible consequences of higher inflation pressures remaining for longer. The Federal Reserve began hiking interest rates with a 25 basis-point increase in March. Currently, the market is pricing in a further eight increases by the end of 2022.

Gold price rose in Q1

5.9%

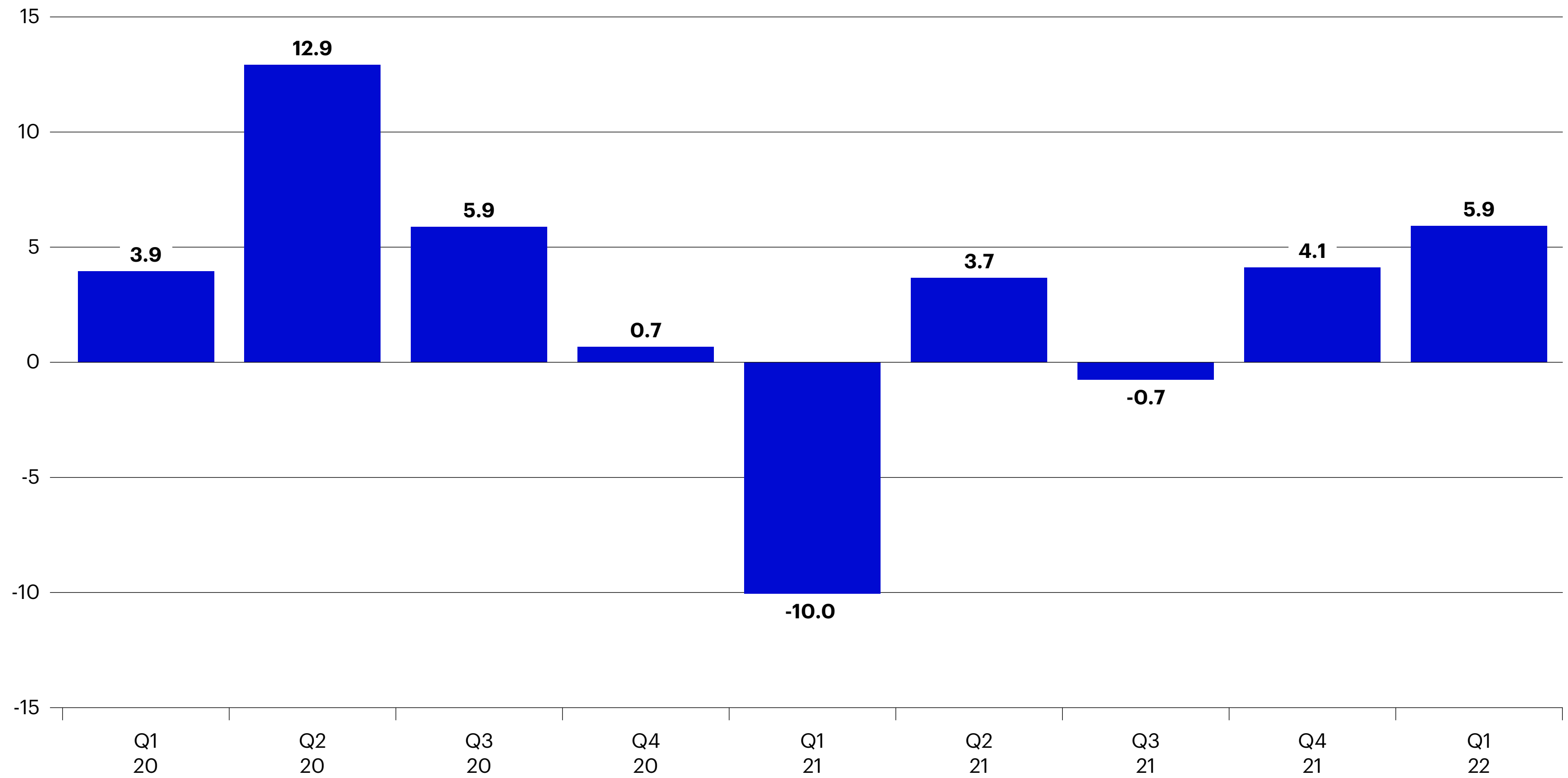
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, from 31 December 2021 to 31 March 2022.

Quarterly price returns

The 5.9% increase represents the strongest quarter for gold since Q3 2020, when it produced an equivalent return. Coincidentally, these were also the only periods in history when gold has broken through $2,000 an ounce.

This quarter marks the strongest start to a year for gold since 2017, when it gained 8.9% in Q1 of that year, and clearly much better than the 10.0% decline suffered at the beginning of last year.

Quarterly price change (%)



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 March 2022.

Market performance

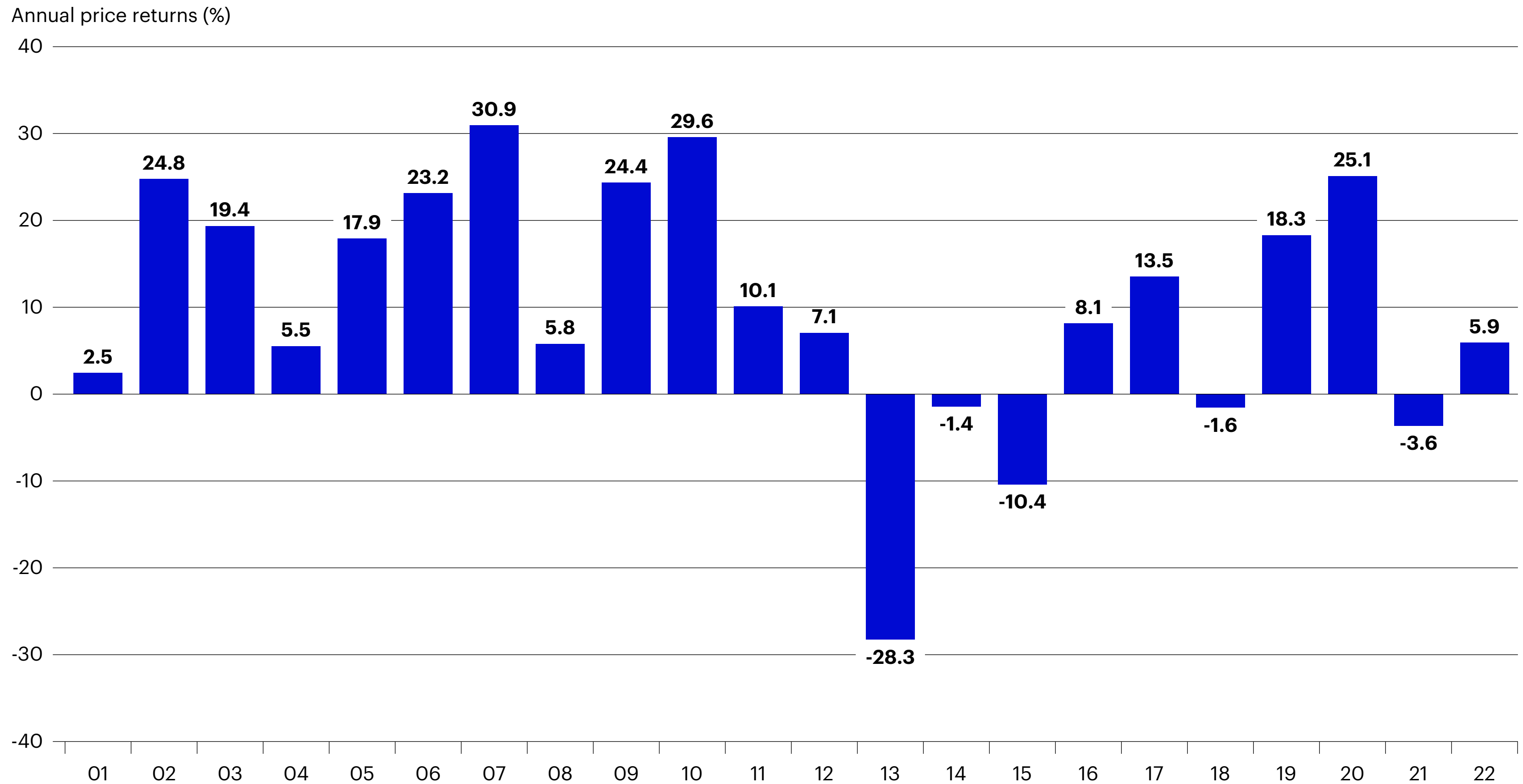
Macro factors

Annual price returns

For the 12 months to the end of March 2022, gold increased 13.5%. This reflects both the sustained build-up of inflation pressure over the past year as well as, more recently, the increased geopolitical instability including, but not limited to, the Russian invasion of Ukraine.

Gold price return in past 12 months

13.5%



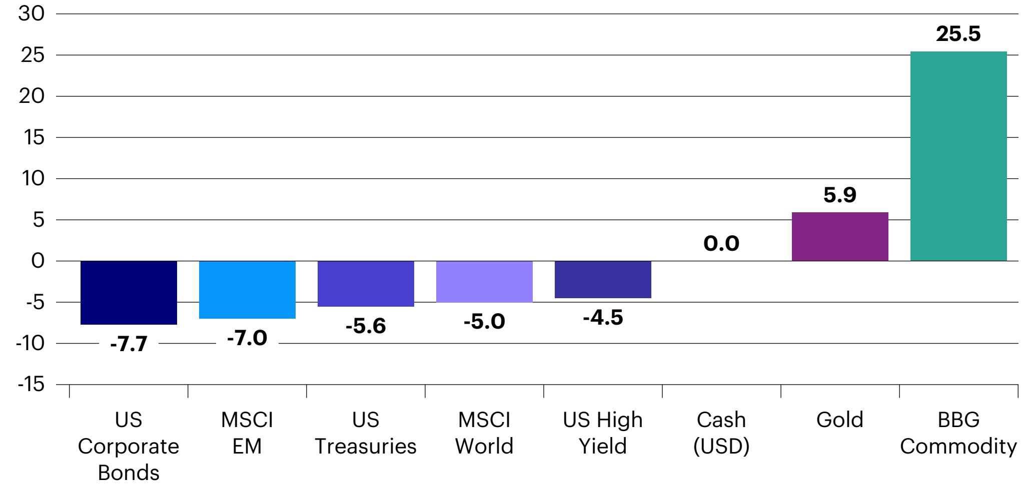
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 March 2022.

Asset class returns

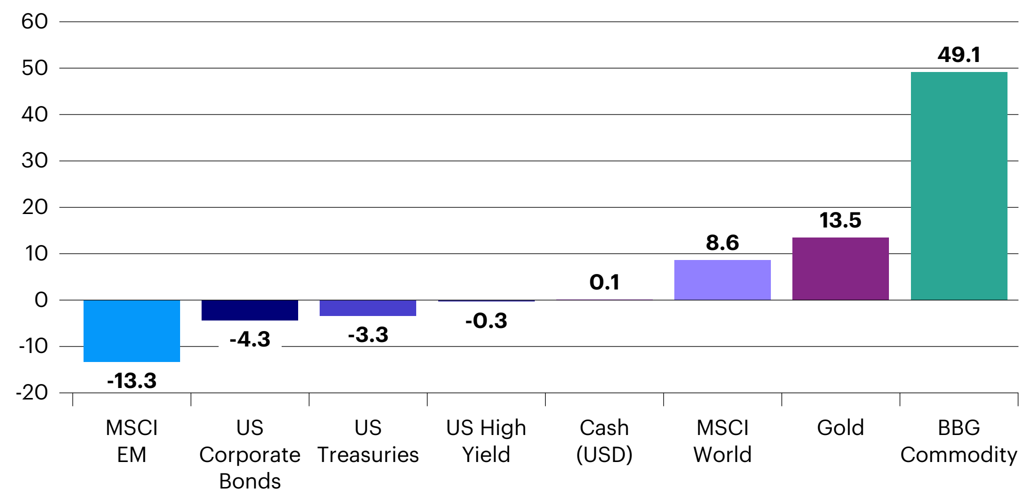
Markets were dominated by the events in Ukraine causing a spike in commodity prices, which were already prevalent in 2021. Gold also benefitted from the uncertainty generated as risk assets fell out of favour, specifically emerging market equities, before having to contend with the rate hike by the Fed, finally confirmed at 25 basis points. Concerns about the economic growth outlook, in large part owing to inflation and the management thereof, as well as the rate hike meant credit had the toughest quarter.

At the end of last year, emerging market equities were already struggling from the combined effects of a stronger US dollar and base effects. Continued poor performance into this year, concentrated in eastern Europe but also concerns on China's outlook, cemented emerging market equities as the biggest underperformer over the past 12 months. Commodities were the only asset class to outperform gold both in the most recent quarter and the past year. The performance of the commodities basket has been on a broad basis from energy to softs.

Quarterly asset class returns (%)



12-month asset class returns (%)

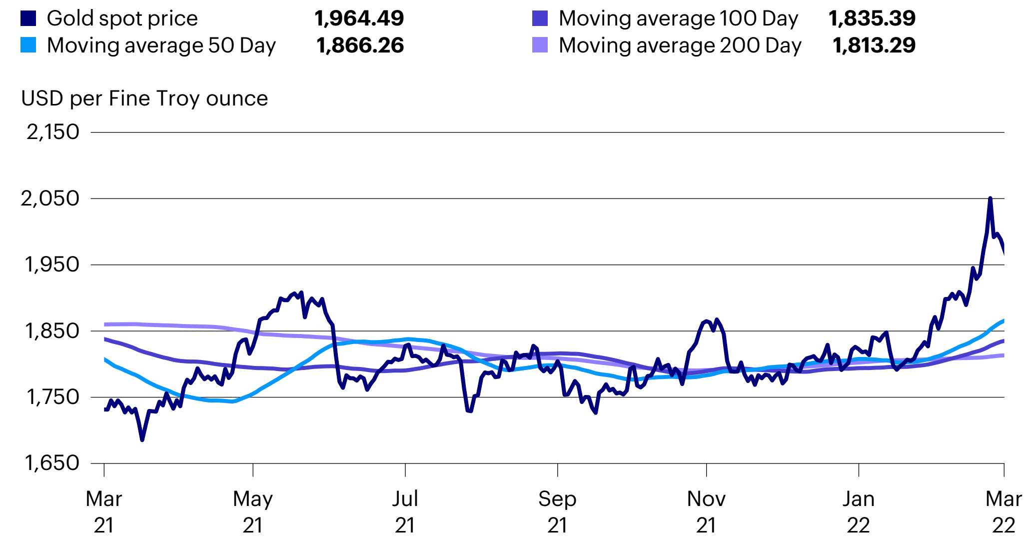


Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 March 2022.

Relative strength of the gold price

Following the "golden cross" signal in Q4 (defined as the crossing of the 50-day moving average (MAV) above the longer-term MAV measures), gold rapidly broke away from its moving averages at the start of the year, rallying towards the all-time high of August 2020.

The rapid rise in the gold price into the start of March did trigger an overbought signal as the metal broke above $2,000. As implied by the Relative Strength Index in the bottom chart, gold appeared to be overbought for eight days during the quarter before falling back.



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 March 2022.

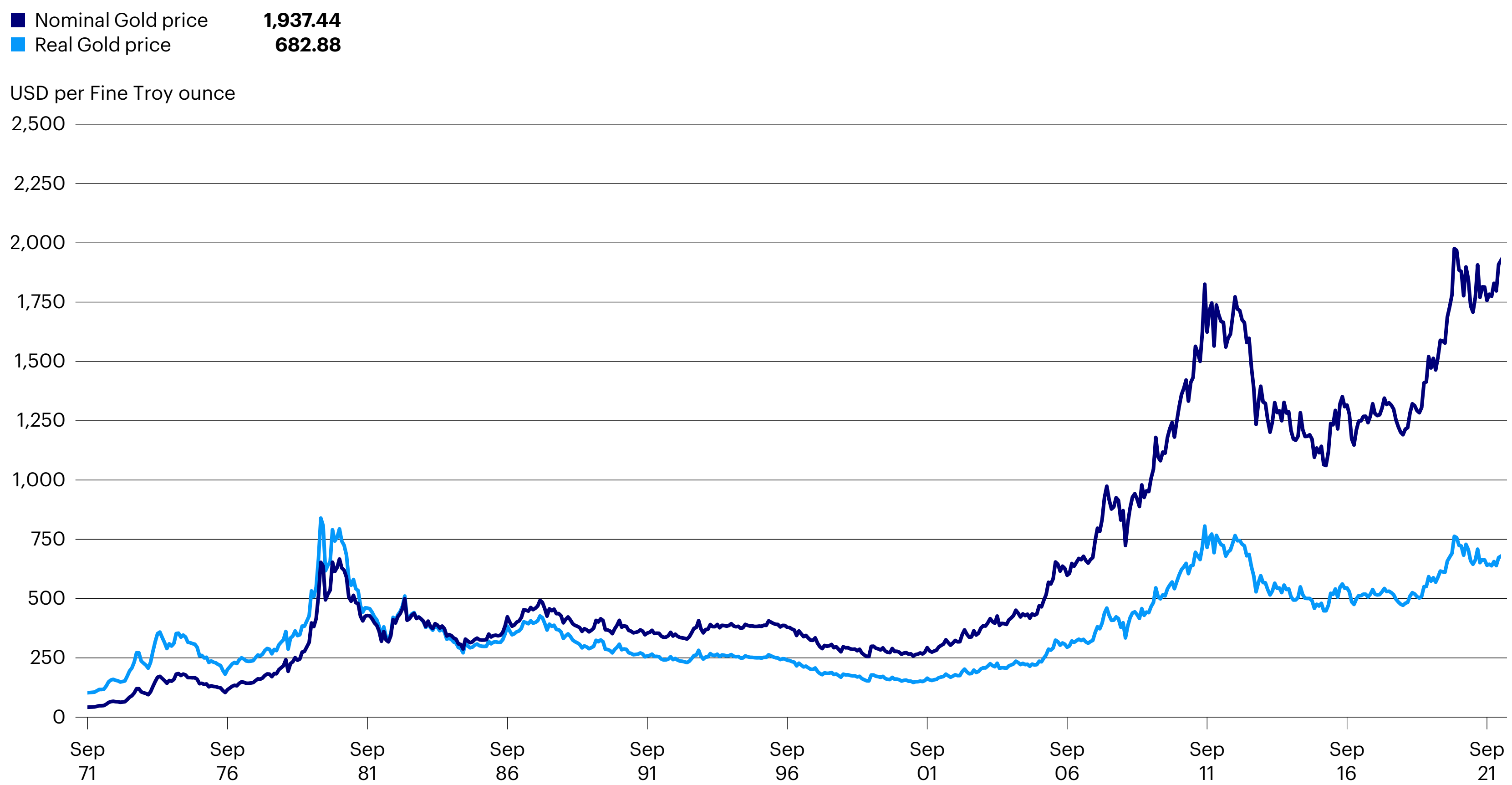
Gold price return, nominal and adjusted for inflation

Inflation in the US is now at a 40-year high, with CPI at 7.9% year-on-year at the end of February 2022. In comparison, over the same 12-month period, gold returned 10.1%, exemplifying gold's property of being a potential hedge against unexpected and high inflation.

US inflation at 40-year high

7.9%

at the end of February

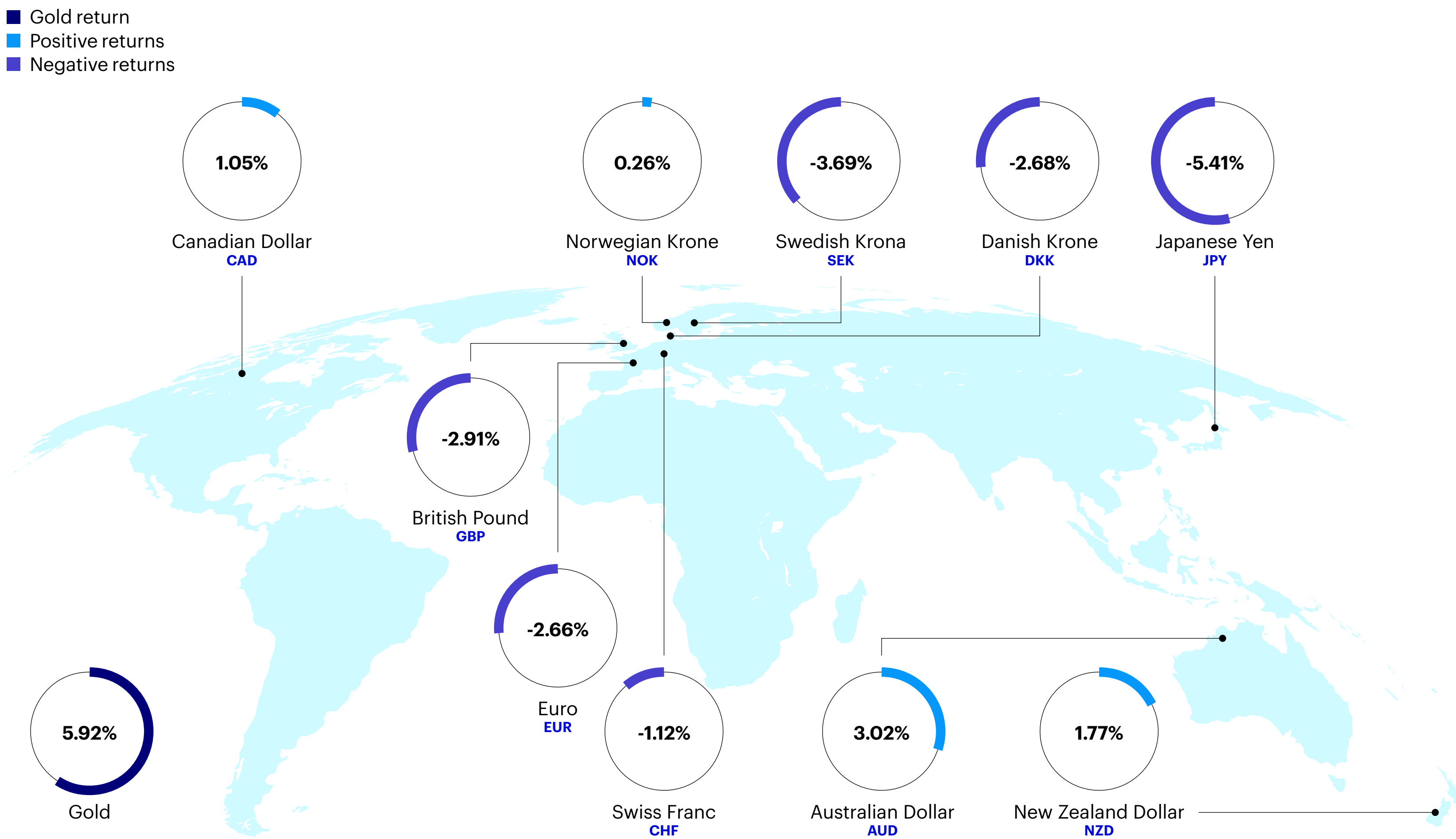


Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 March 2022.

G10 currencies

Gold outperformed all G10 currencies during the quarter. Those currencies backed by natural resources (AUD, CAD, NOK) unsurprisingly posted positive returns against the USD, even though we saw the Fed take the initial step on its rate hiking path. Central bank moves put the spotlight on interest rate differentials and yen underperformance.

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



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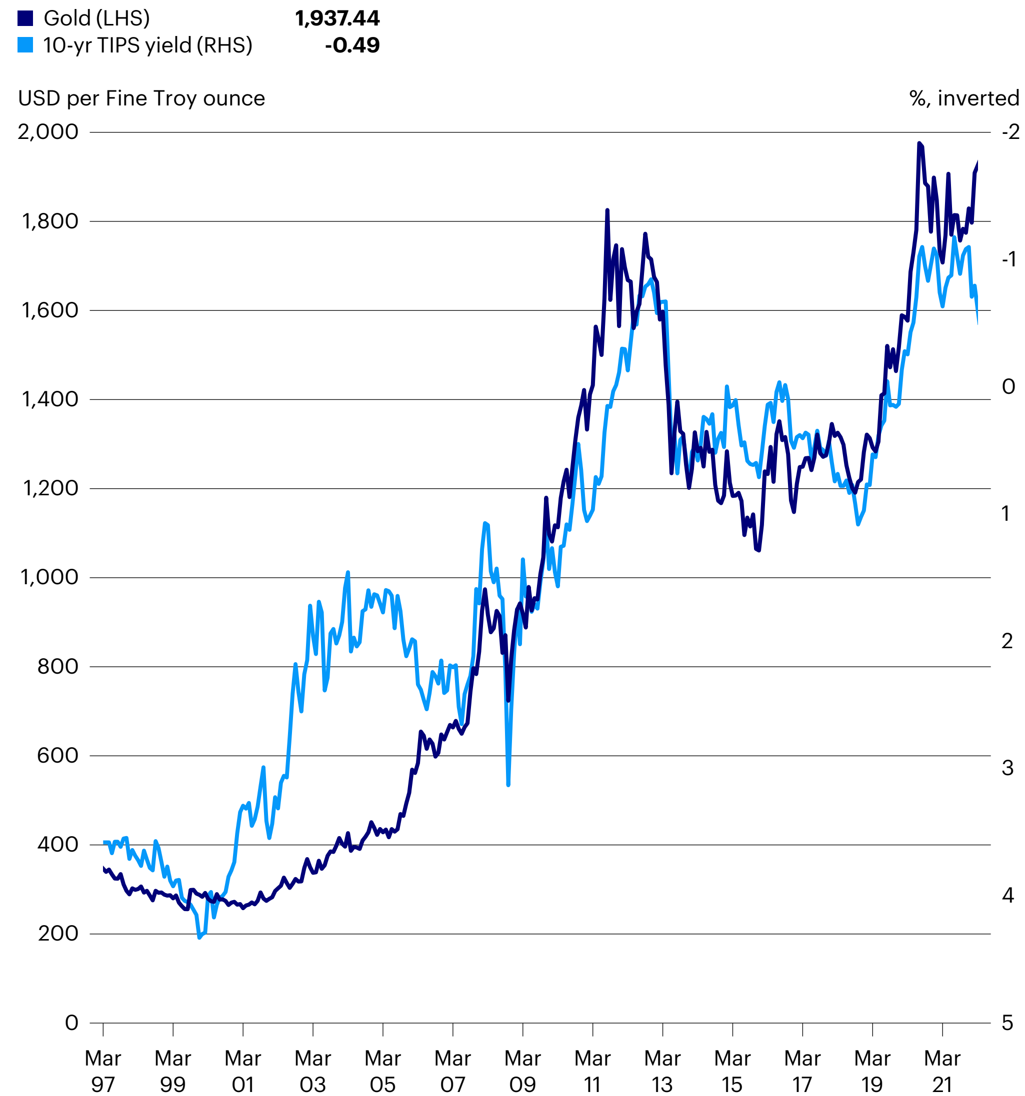
Gold price and real bond yields

Having started the year at -1.1%, real yields ended the quarter at -0.49%, with the increase in the Fed funds rate being the key driving factor. Although yields were higher, gold was also able to deliver strong returns, contrary to the long-term relationship as geopolitical risk saw investors turn to the perceived "safe haven" of the precious metal.



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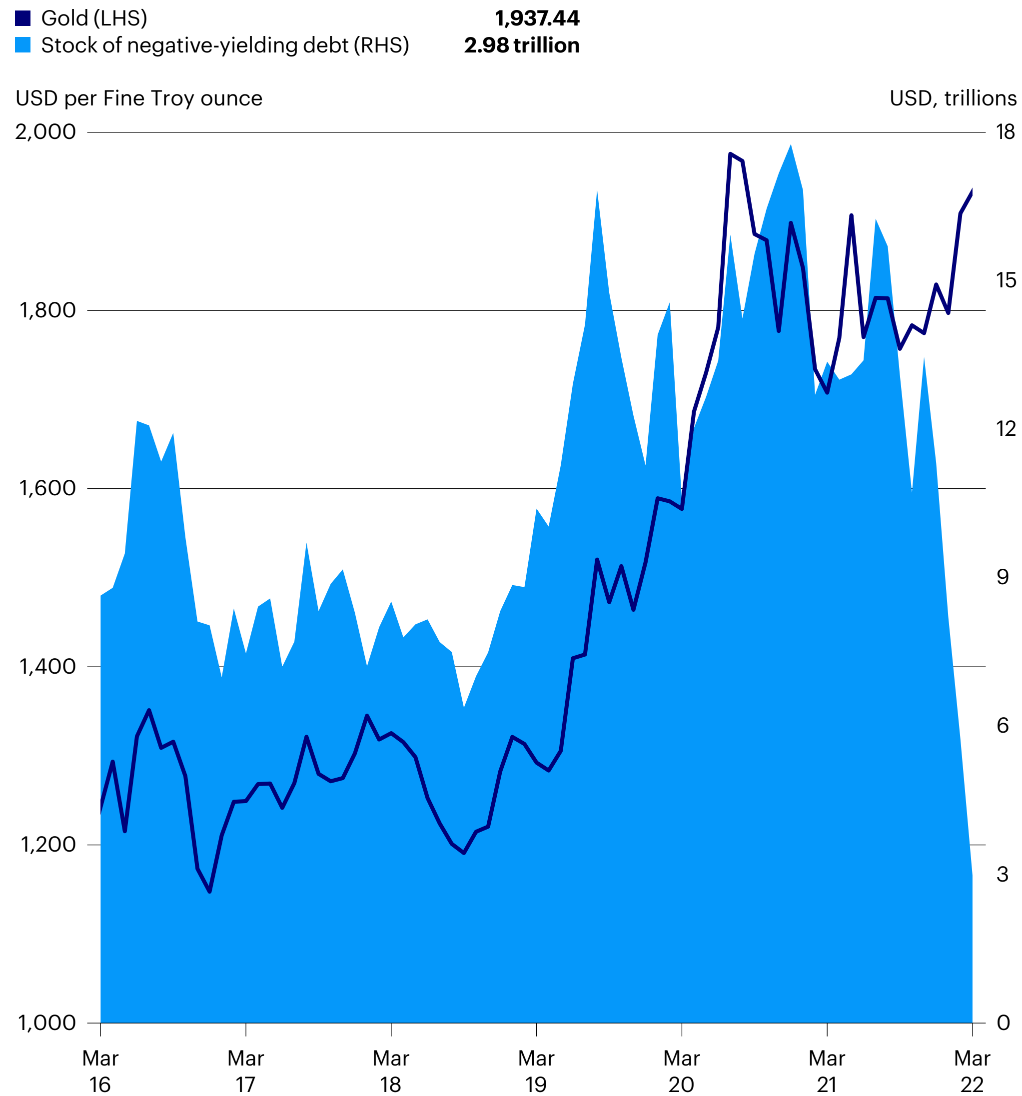
Market performance

Macro factors

Gold price and negative-yielding debt

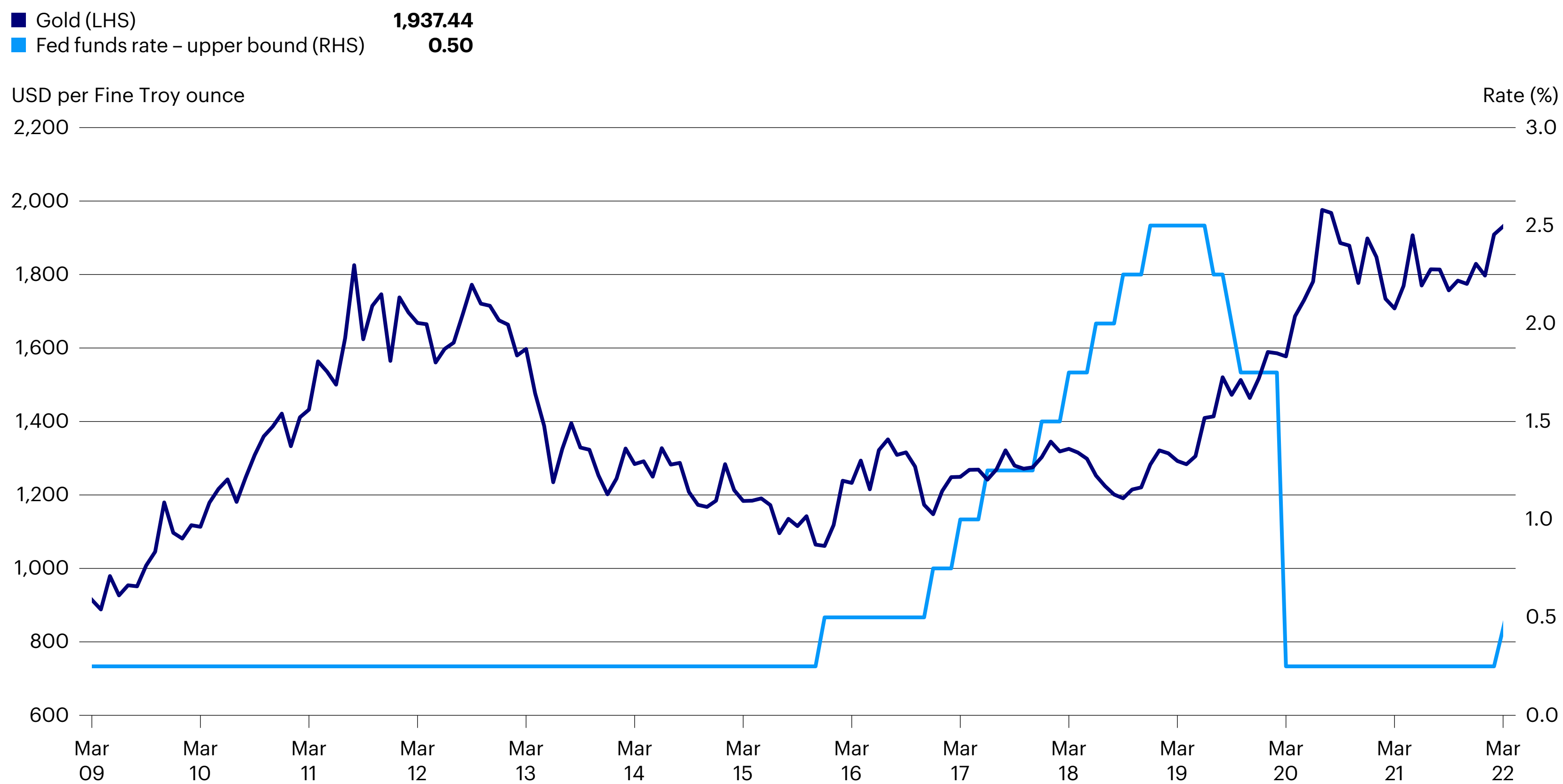
With the Fed embarking on its well-flagged rate-hiking cycle, the stock of negative-yielding debt has fallen away. At the end of March, total stock stood at $3.0 trillion, a fall of $8.3 trillion quarter-on-quarter, as we saw the US 10year Treasury rise to 2.3% from 1.5% and credit spreads widen by 25 basis points over the same time horizon. This is the lowest level of negative-yielding debt since October 2015. The European Central Bank, Swiss National Bank and Bank of Japan, however, still hold negative policy rates, and government debt constitutes the majority of the index of negative-yielding debt (79.1%) with government-related securities a further 12%.



Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 March 2022.

Gold price and US interest rates

The Fed raised rates in March, for the first time since December 2015, with another eight hikes priced in for year-end by the futures market. The March dot plot caught the markets offside by registering more rate hikes than anticipated and because of this, and the Fed's strong tone on tackling inflation, the markets sharply re-evaluated its positioning; a case of "Don't fight the Fed" perhaps. Higher rates in the US would be expected to create a headwind for gold, albeit this needs to be weighed against global events.



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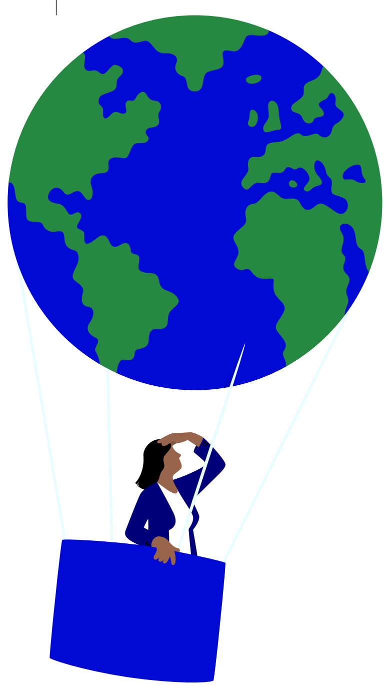
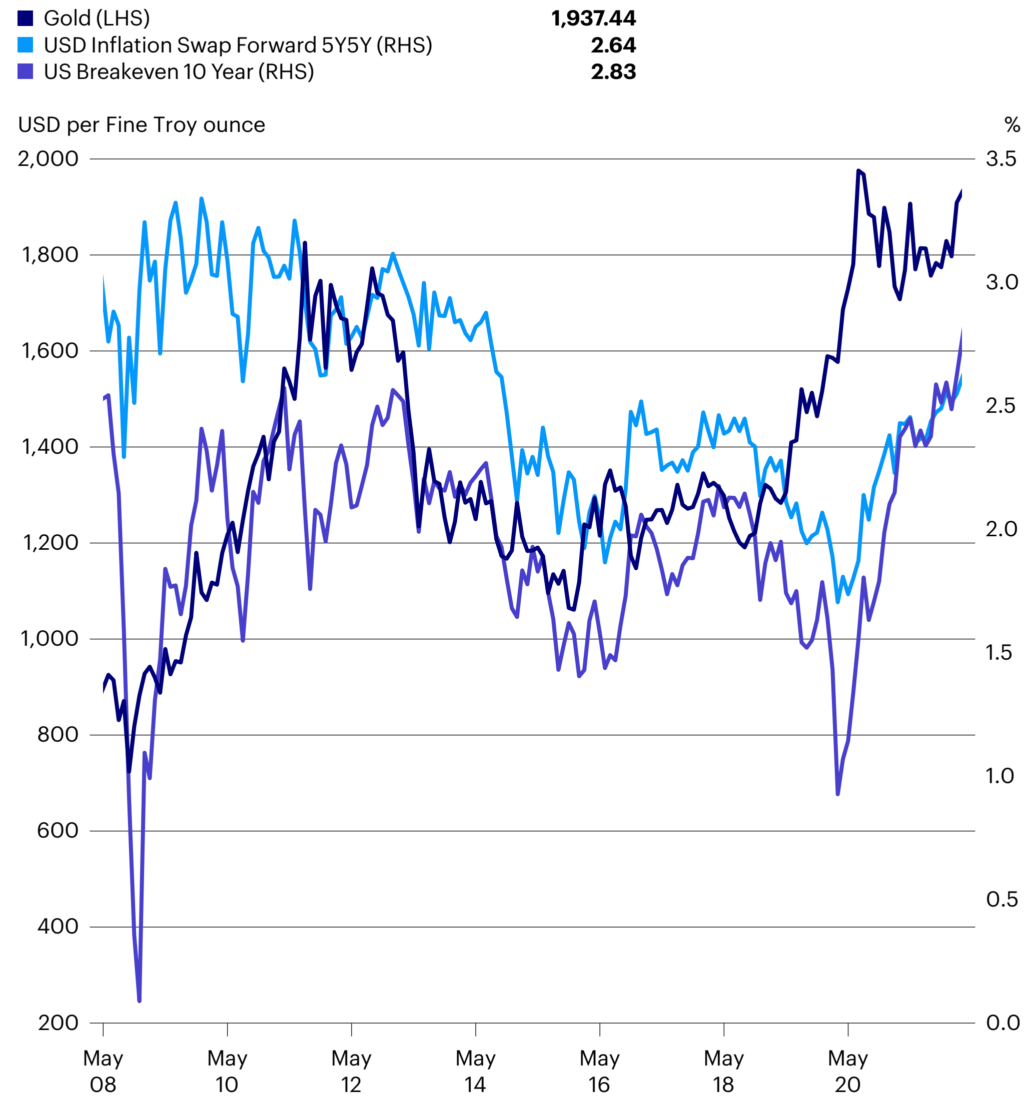
Gold price and inflation expectations

The unexpected military action in Ukraine caused commodity prices to spike and had immediate consequences on inflation expectations. Typically, gold is a beneficiary of unexpected inflation, and inflation expectations had already been rising. Inflation is now expected to endure at higher levels than previously expected. What will be crucial for gold is the credibility of central banks in being able to manage this price instability. Perceived mismanagement may provide support to gold.





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Market performance

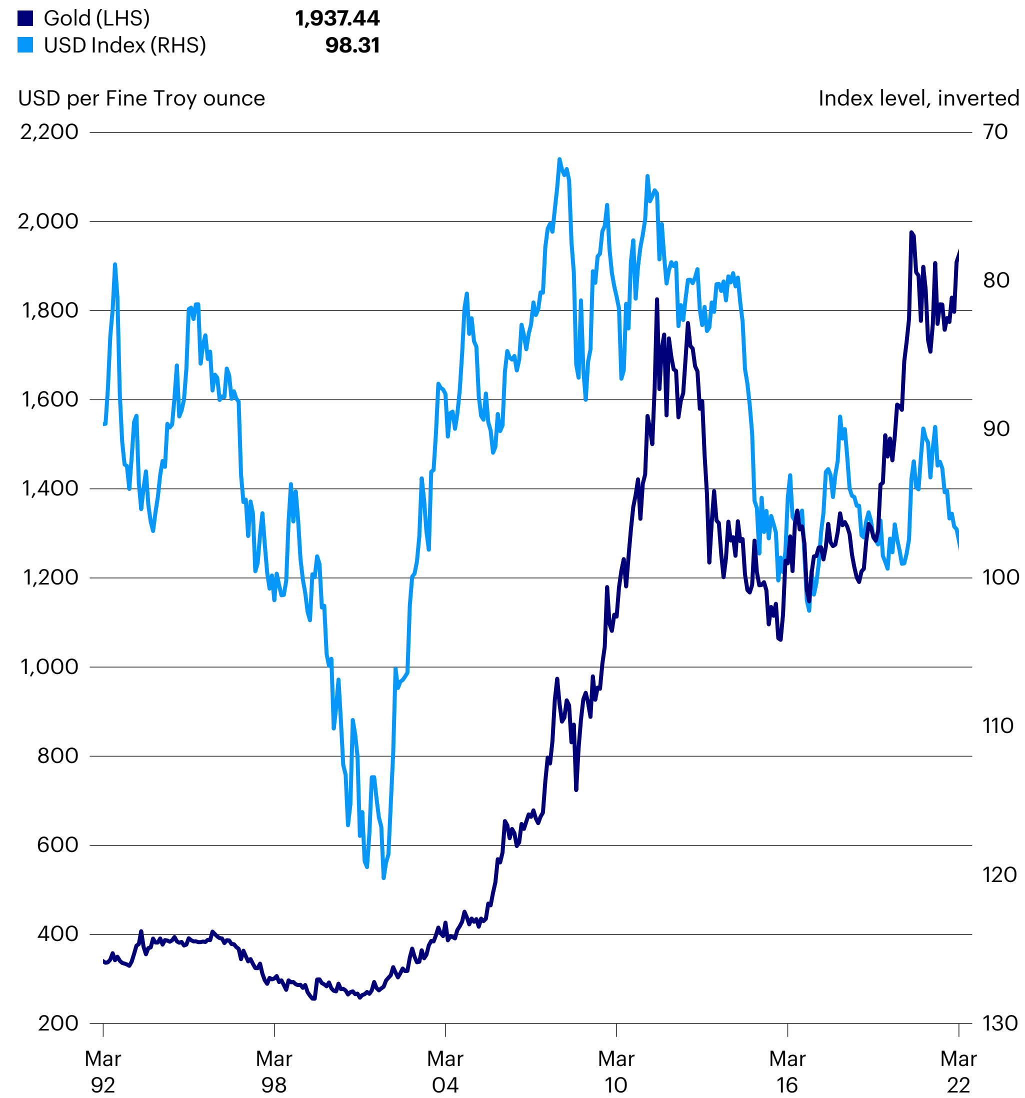
Macro factors

Gold price and the US Dollar

The USD index increased 2.8% on the quarter, running against the general relationship of stronger USD / weaker gold. The dollar increased not only as investors retreated to safe havens but also as the Fed began to raise rates, attracting investors' seeking higher yields. A relatively strong outlook for the USD will be supported by greater interest rate differentials, which is usually not a strong outlook for gold. As the chart shows, however, there are more powerful factors at play right now.

USD strengthened in Q1

2.8%



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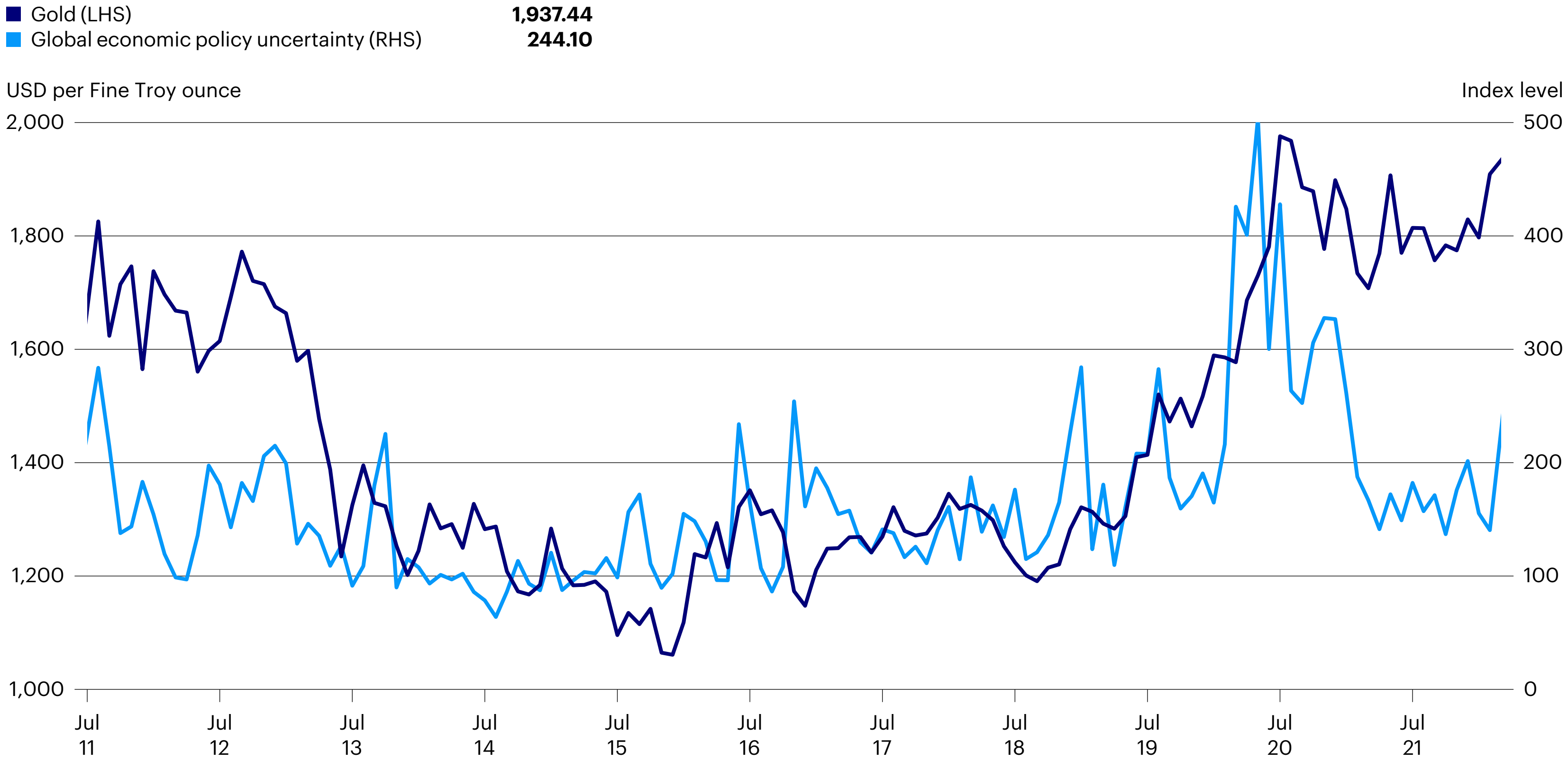
Market performance

Macro factors

Gold price and economic risks

Speculation over the number of Fed rate hikes this year has seen a spike in the economic uncertainty measure for the US. In the past, this has been a positive for gold but given the uncertainty captured here is just how many hikes the Fed can implement – without giving the US economy a hard landing – it may not be as dependable as it has been in the recent past.



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Data as at 31 March 2022, unless otherwise stated.

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