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Market performance and macro factors

Gold report

Q4 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 Q4 2022

Gold price return in Q4
+9.8%

Gold return in 2022
-0.3%

Fed balance sheet remains high
$8.5 trillion

US Dollar index in Q4
-7.6%

Data: Bloomberg, as at 31 December 2022.

Market performance
Pages 03 – 09

The gold price rose sharply in Q4 to end the year only slightly lower than where it began. All major asset classes turned in a positive performance in the final quarter, with gold's return bettered only by that of Emerging Market equities.

Macro factors
Pages 10 – 15

The US Dollar was significantly lower in Q4, as the market priced in a change in Fed policy. Signs of a potential peak in inflation enabled the Fed to ease its rate hikes towards the end of the year, and the market is now expecting the central bank to shift its focus to battling the slowdown in the economy.

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 9.8% in the fourth quarter to end the year at $1,824. The precious metal retested recent lows at the start of the quarter before rebounding to June levels. The main catalyst was US inflation coming off its 40-year peak, leaving investors to begin factoring in a Fed pivot as the USD fell from its 20-year high. The strength of the Dollar had been one of the biggest headwinds to gold during the year.

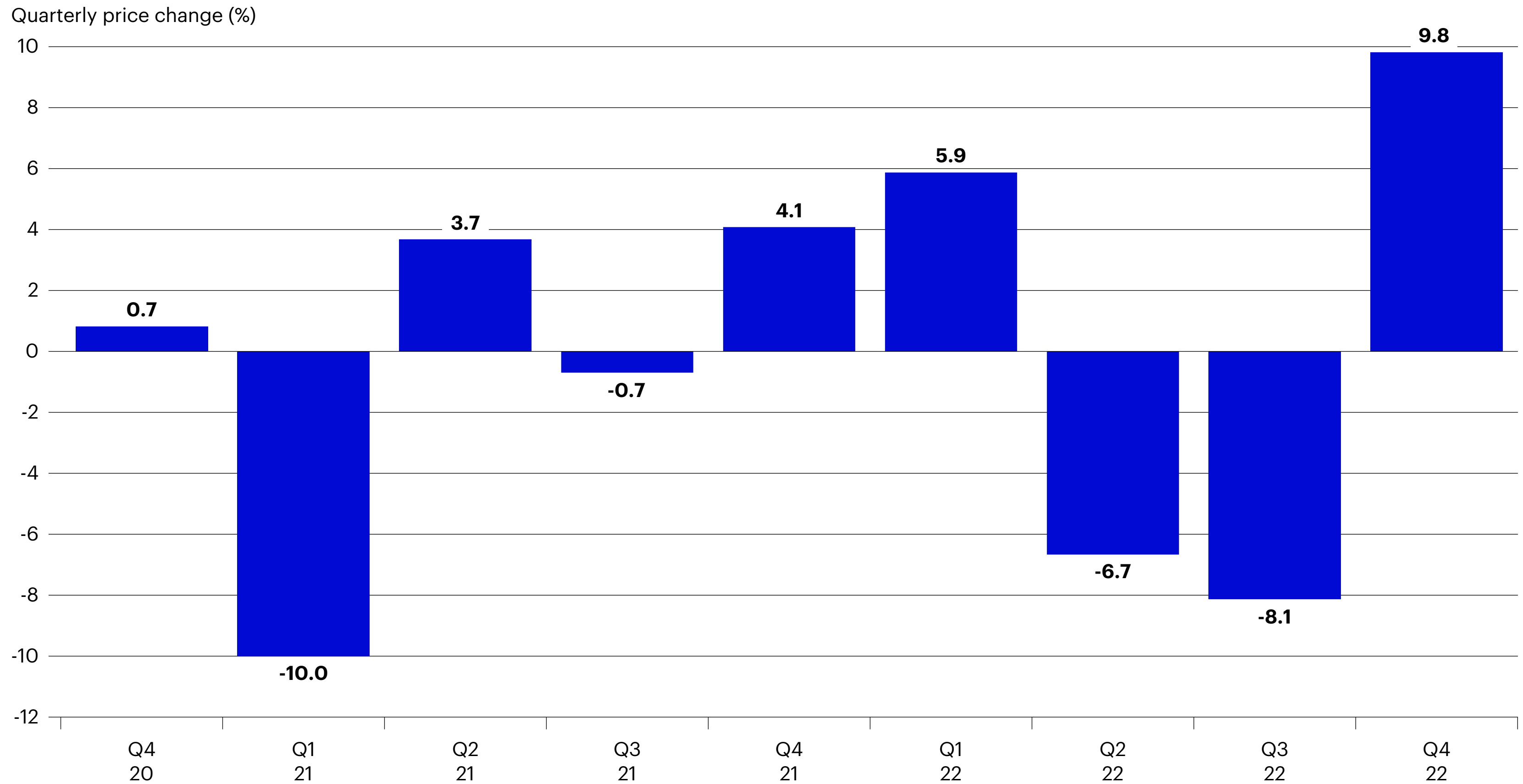
Gold price return in Q4

+9.8%

Past performance is not a reliable indicator of future returns. Bloomberg, in USD, from 30 September to 31 December 2022.

Quarterly price returns

Q4 2022 was the best quarterly return for gold since Q2 2020 when strong gold returns were also driven by a weaker USD. The performance in the most recent quarter was in sharp contrast to the previous six months when the Fed was fully immersed in looking to bring down inflation.



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

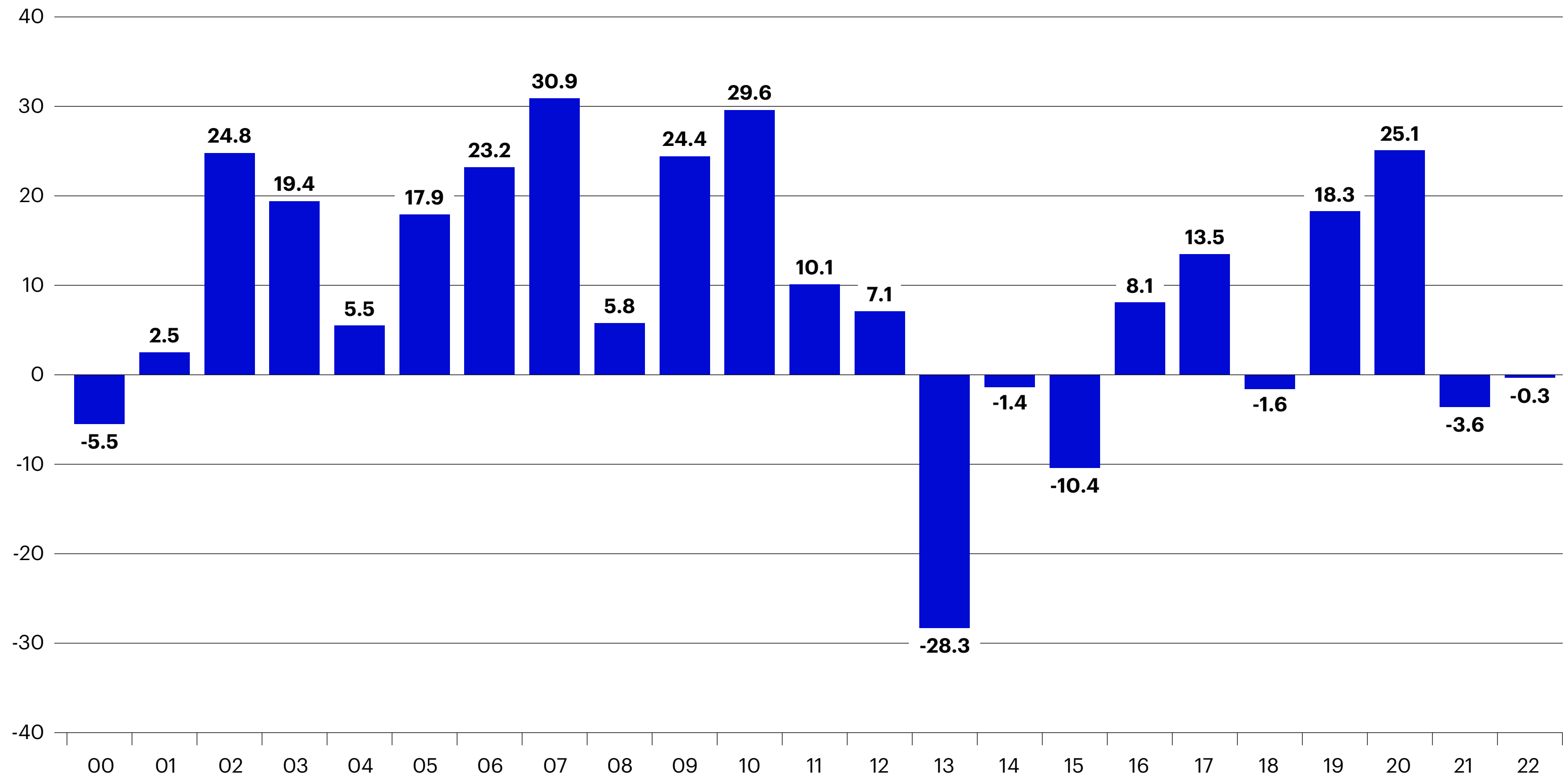
Annual price returns

The strong return in the final quarter meant, ultimately, gold delivered an almost flat performance for the year, returning -0.3% in 2022. Gold began the year with a strong Q1, benefitting from the outbreak of war in Ukraine (with gold perceived as a relative safe haven) before succumbing to its relative drawback of being a non-yielding asset against a backdrop of rising rates. Gold's broadly flat performance over the year is an improvement on the performance in 2021 when the metal returned -3.6%.

Gold return in 2022

-0.3%

Annual price returns (%)



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

Market performance

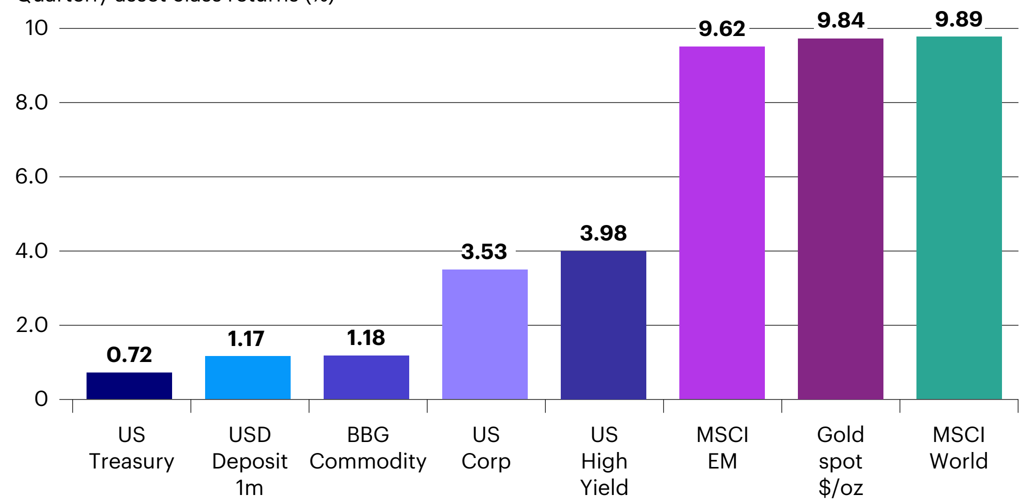
Macro factors

Asset class returns

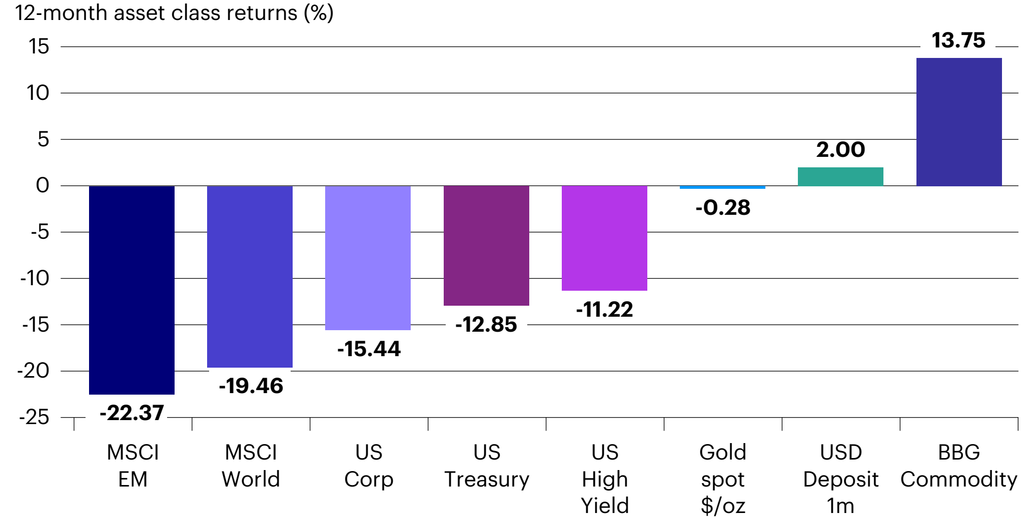
Gold and Emerging Market equities both benefitted from a weaker dollar in Q4 although all major asset classes generated positive returns in the quarter. As inflation seemed to have peaked in the US, the Fed slightly eased the magnitude of its rate hikes into year end and, as investors looked further ahead to the Fed pivoting, money came back into equities.

Performance did turn around in Q4 but not sufficiently to fully recoup earlier loses with the year closing with record falls in equities and fixed income. Higher discount rates saw equity multiples fall and China continued to struggle with Covid for most of the year. Higher rates also saw opportunities open up in fixed income with yields returning to levels not seen in over a decade in several cases. Unlike gold, commodities were able to hang on to their outsized gains from Q1 to be the top performer for the year.

Quarterly asset class returns (%)



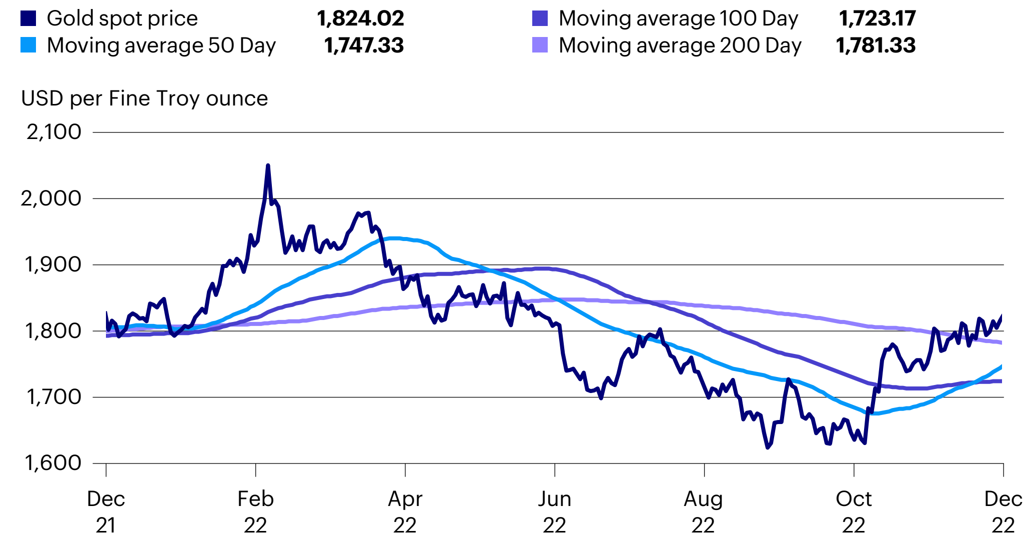
12-month asset class returns (%)

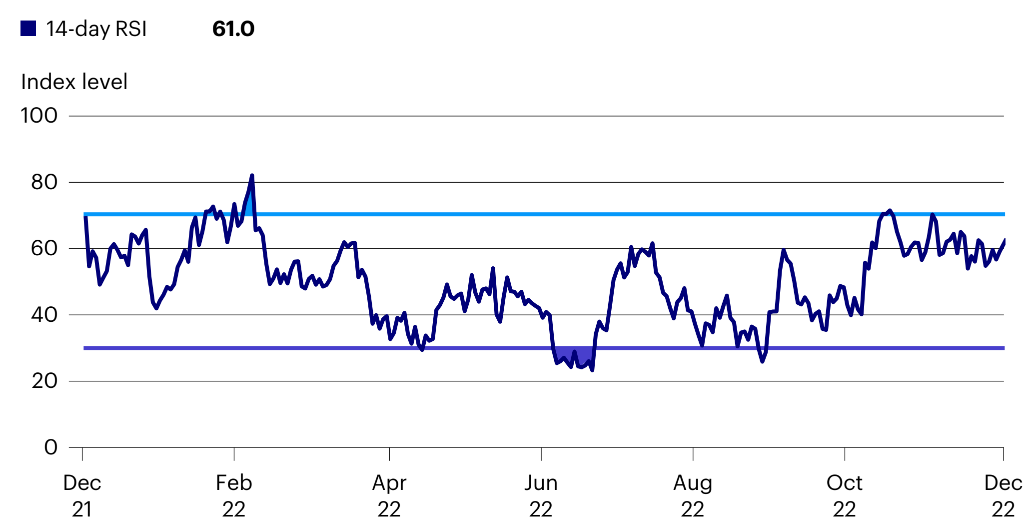


Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, as at 31 December 2022.

Relative strength of the gold price

The uptrend in gold over the quarter meant there was support for the metal at $1,725 as the 50-day moving average crossed the 100-day moving average. Should the recent trend continue, a clear buy signal could be triggered in the coming weeks using the longer-term moving averages. The rapid ascent of gold meant the metal did touch the overbought qualification at the start of the quarter before continuing on a steadier trajectory.

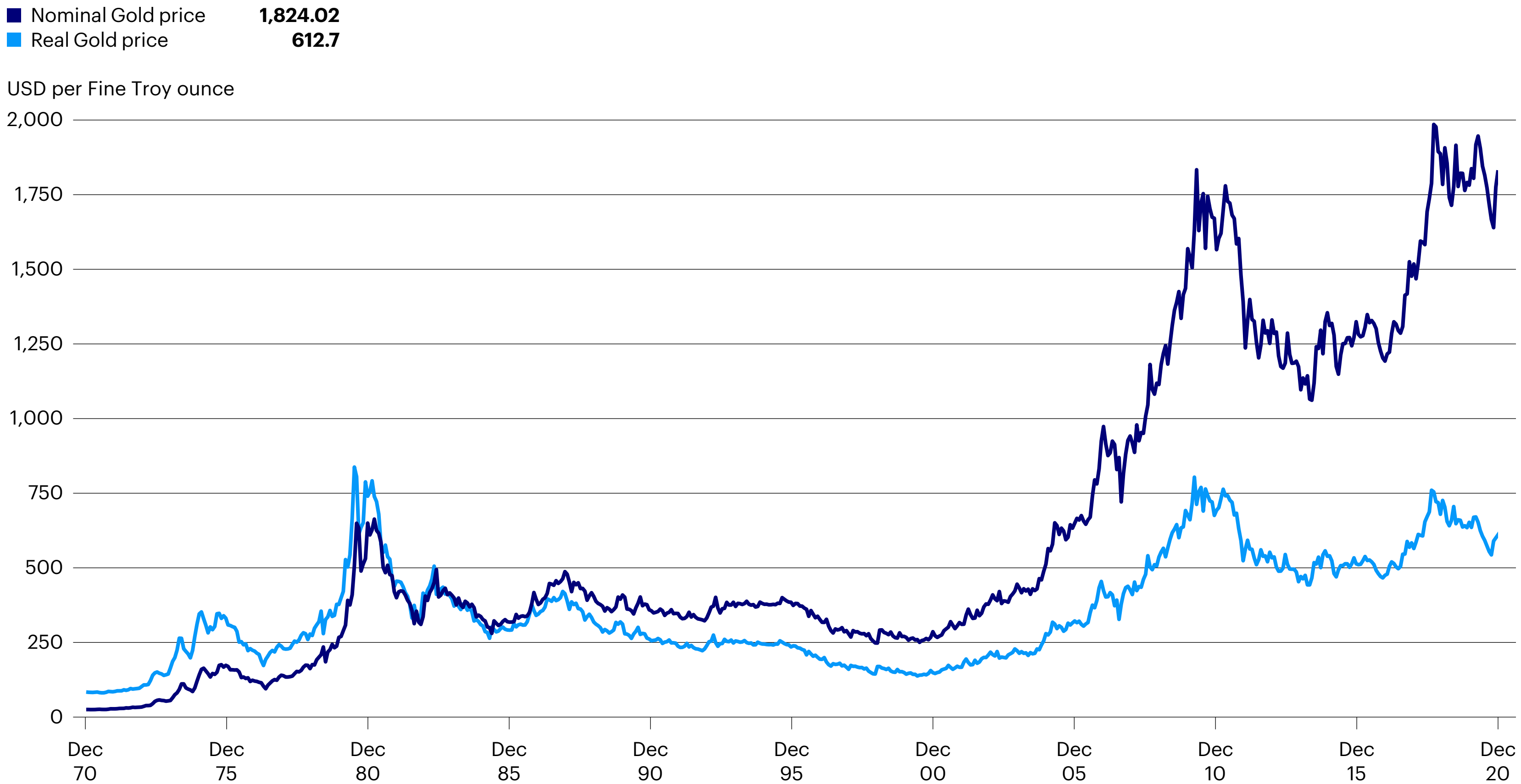




Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 December 2022.

Gold price return, nominal and adjusted for inflation

In real terms, gold returned 9.5% in the quarter as inflationary pressures in the US began to ebb slightly. To the end of November, US CPI was still running at 7.1% year-on-year meaning in real terms gold had returned around -7.0% for the year.



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

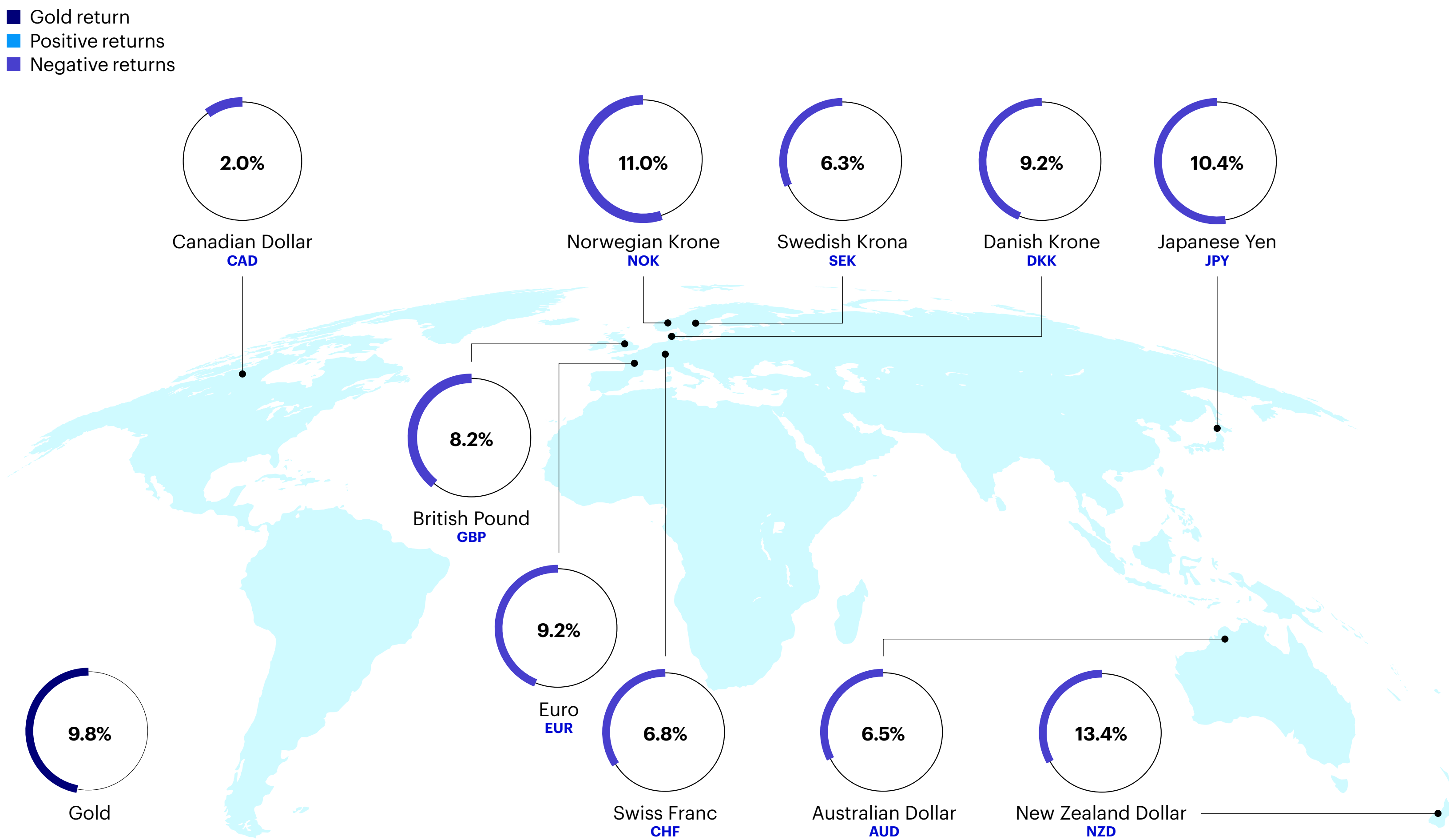
Market performance

Macro factors

G10 currencies

The US Dollar was weaker across all major currencies during the quarter as interest rate differentials widened on the expectation the Fed was closer to approaching its peak rate. In New Zealand, a further 1.25% of hikes is priced in over the coming six months whereas the Fed is expected to add 0.5% over the same period. The story is similar for most other countries with conditions expected to tighten further outside of the US. Also, the quarter saw additional (and unexpected) action by the Bank of Japan to relax its yield curve control, boosting the yen.

Q4 returns of gold and G10 currencies in USD (%)



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Gold price and real bond yields

The yield on the US 10yr TIPS was little changed quarter-on-quarter. At 10 basis points lower, it ended the quarter at 1.6%. Real yields did rally to 1.1% at the start of December but strong employment data and improving consumer sentiment on better inflation data gave real yields a boost as well as the upgrade to Q3 GDP estimates. Comparative data implies that real rates should be higher at this point of the cycle.

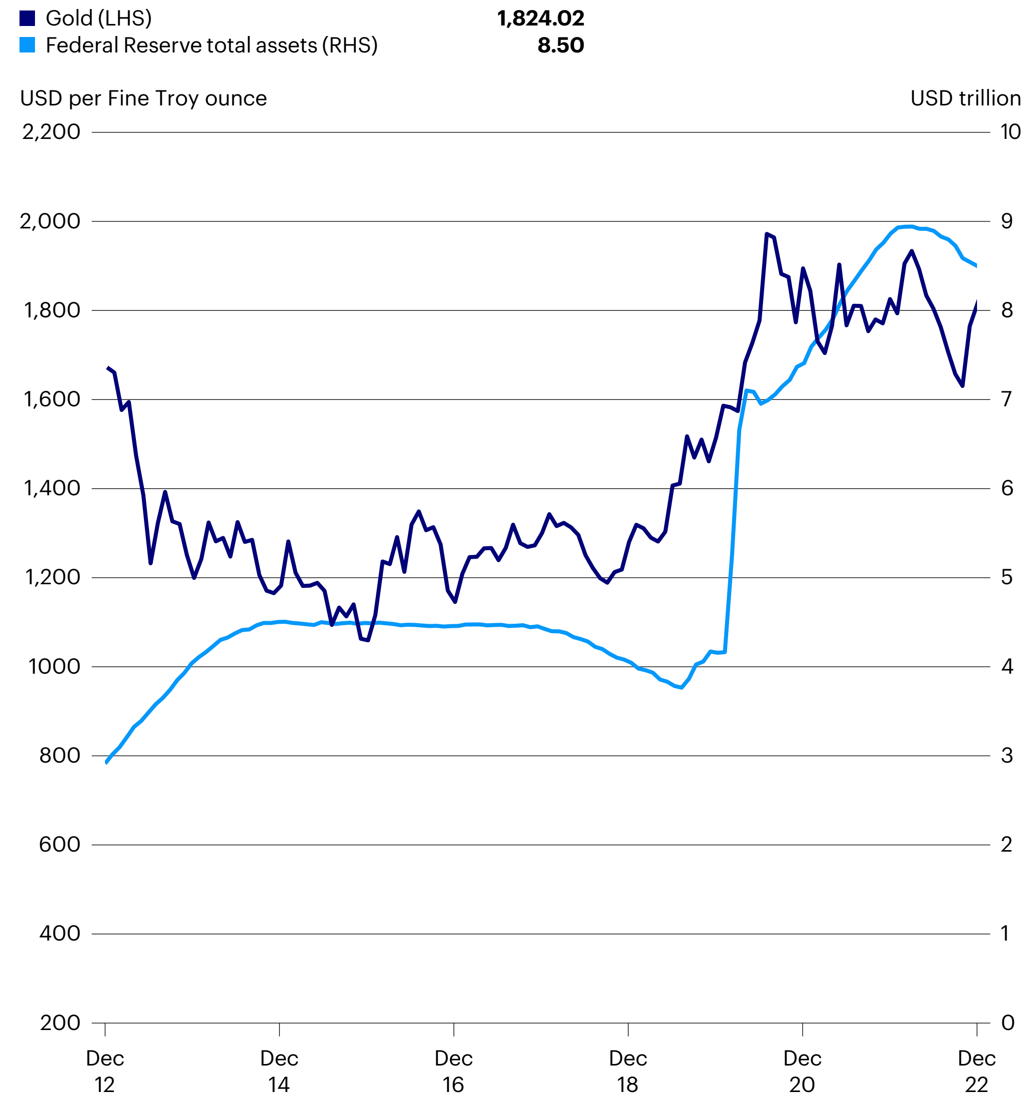
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 December 2022.

Gold price and Fed balance sheet

The Fed's balance sheet continued to shrink through the quarter by a further $244 million, taking it back to October 2021 levels of $8.5 trillion. The reduction, and therefore tightening effect, has been below expectations. The Fed does need to consider liquidity issues as it continues its quantitative tightening programme but falling bank reserves are a factor, too; this may bring a premature end to the balance sheet reduction in 2023.

Fed balance sheet remains high

$8.5 trillion



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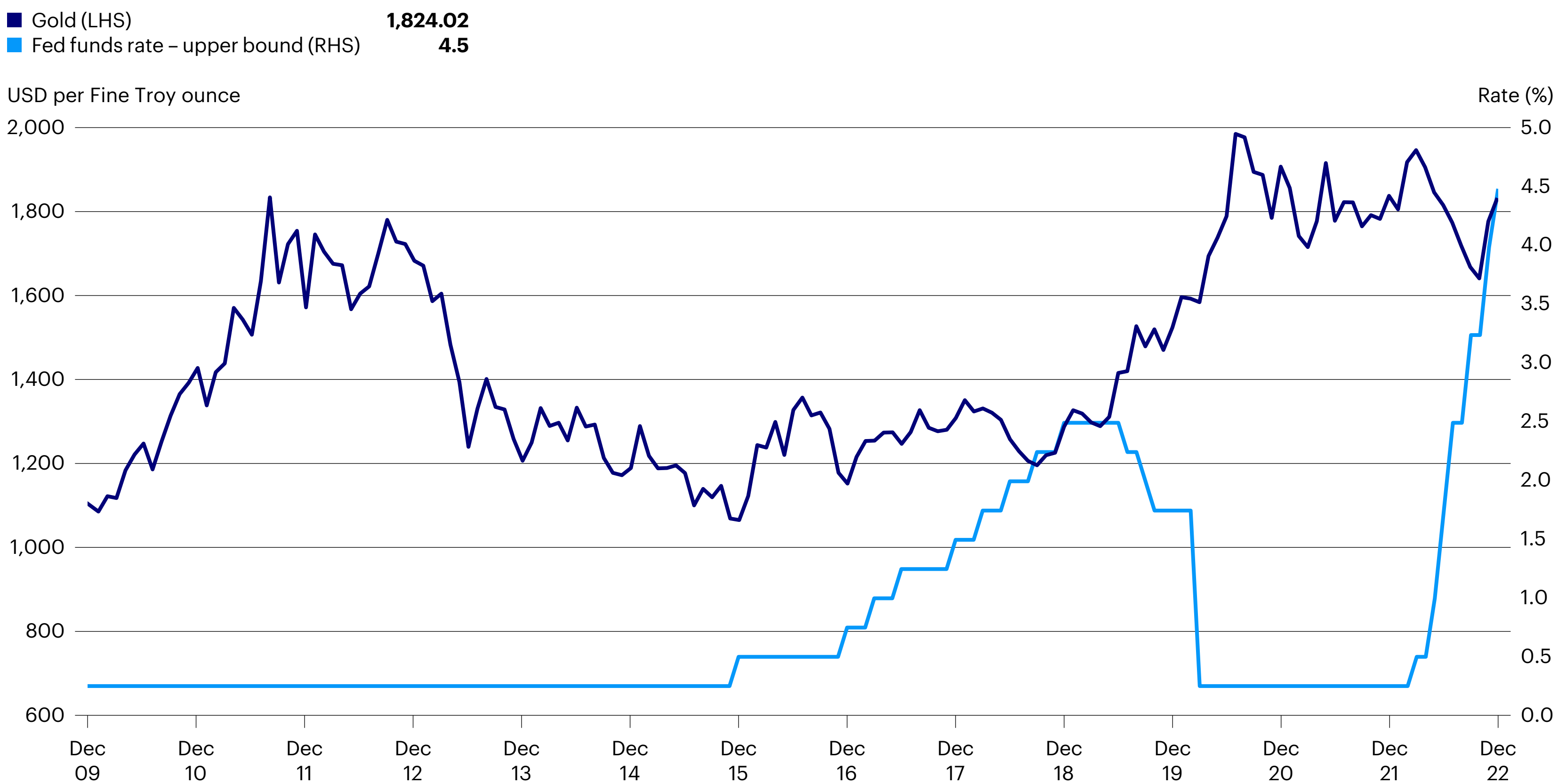
Market performance

Macro factors

Gold price and US interest rates

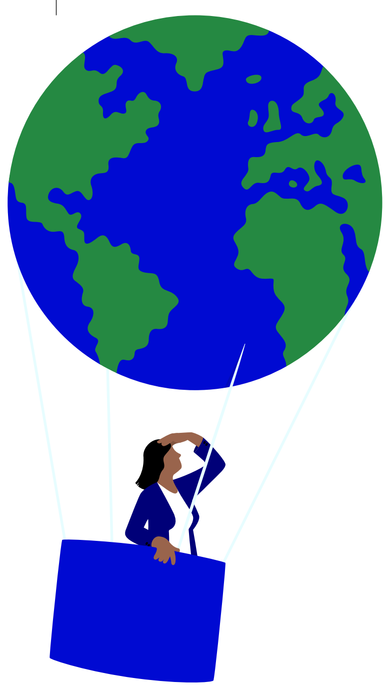
The Fed funds rate was further increased this quarter as the Fed continued its battle with the high inflation backdrop. Despite the 1.25% increase in the policy rate, gold still made gains over the quarter as investors looked to when the Fed would reach its peak rate. The dot plot in December did provide a talking point with the markets not supporting the Fed's projected path of rates being above 5% at year-end 2023. The Fed does need to signal commitment to its fight against inflation, but questionable tactics may provide some upside for gold.



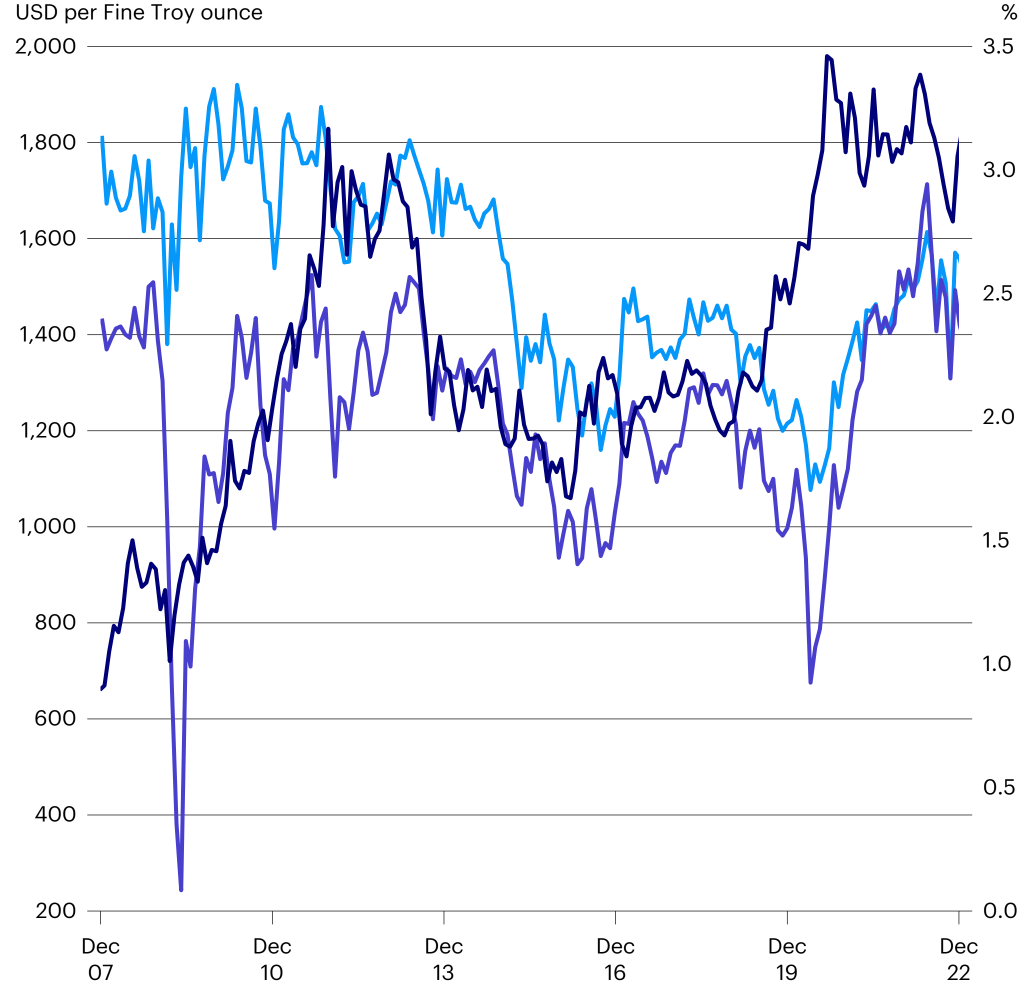
Past performance is not a reliable indicator of future returns. Source: Bloomberg, in USD, to 31 December 2022.

Gold price and inflation expectations

Inflation expectations ended the quarter slightly higher than where they began as some sectors showed better progress towards lower inflation. Although goods and housing-related inflation have fallen, other services inflation is stubbornly high, and hours worked in the services sector still shows remarkably high demand. Inflation is forecast to fall mid-2023 at a pace that is synonymous with recession. If this does not transpire, inflation expectations may well increase again.



Gold (LHS)	**1,824.02**
USD Inflation Swap Forward 5Y5Y (RHS)	**2.60**
US Breakeven 10 Year (RHS)	**2.30**



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Market performance

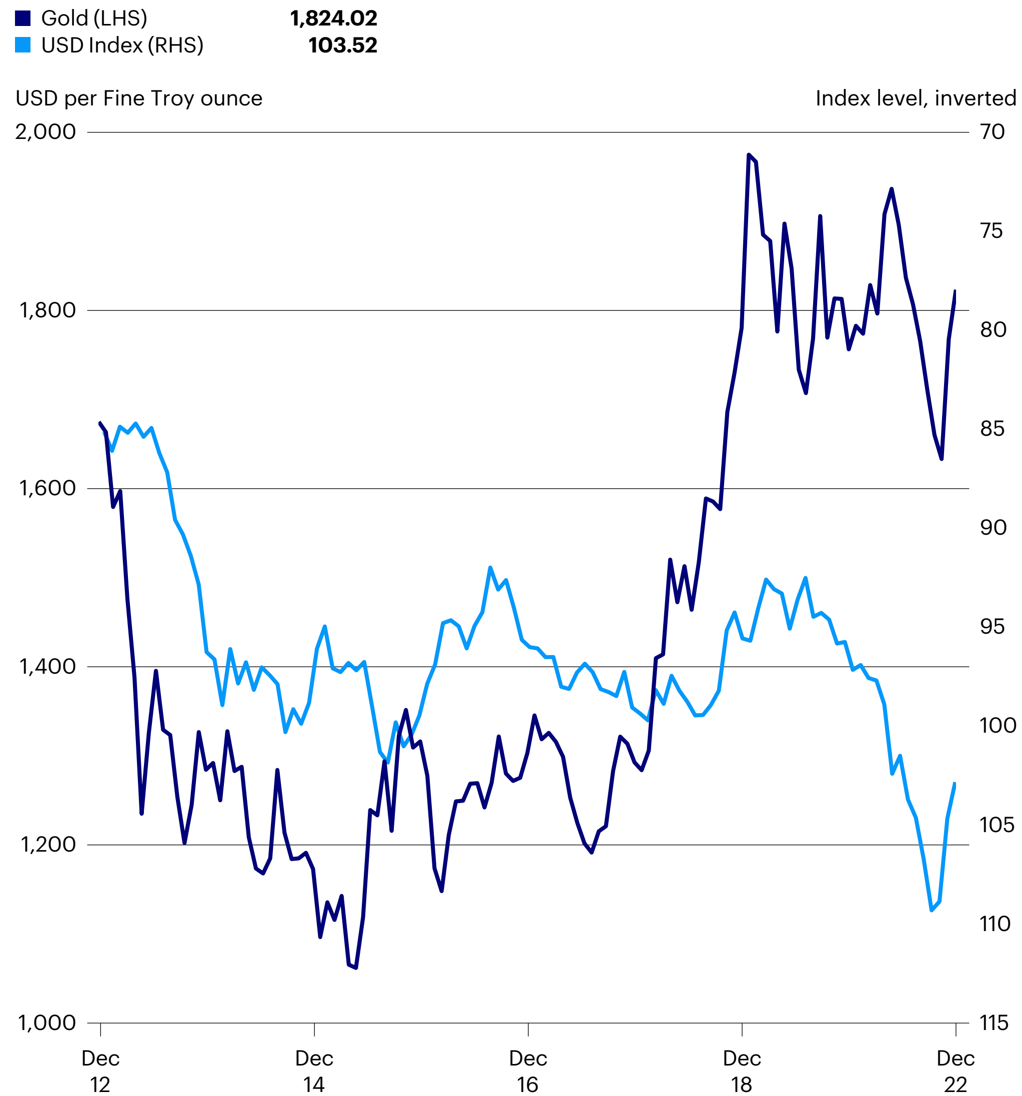
Macro factors

Gold price and the US Dollar

Expectations that the Fed will pivot over the coming months caused the Dollar to fall from its 20-year high, which was the key reason for gold's strong performance over the quarter. The USD (DXY) index fell 7.6% in Q4 2022 as the US ranks lowest in the list of major countries' projected rate hikes in 2023. If the Fed proves correct in its forecast of rates remaining above 5% into the end of 2023, this would be a positive for the USD and a negative for gold.

US Dollar index in Q4

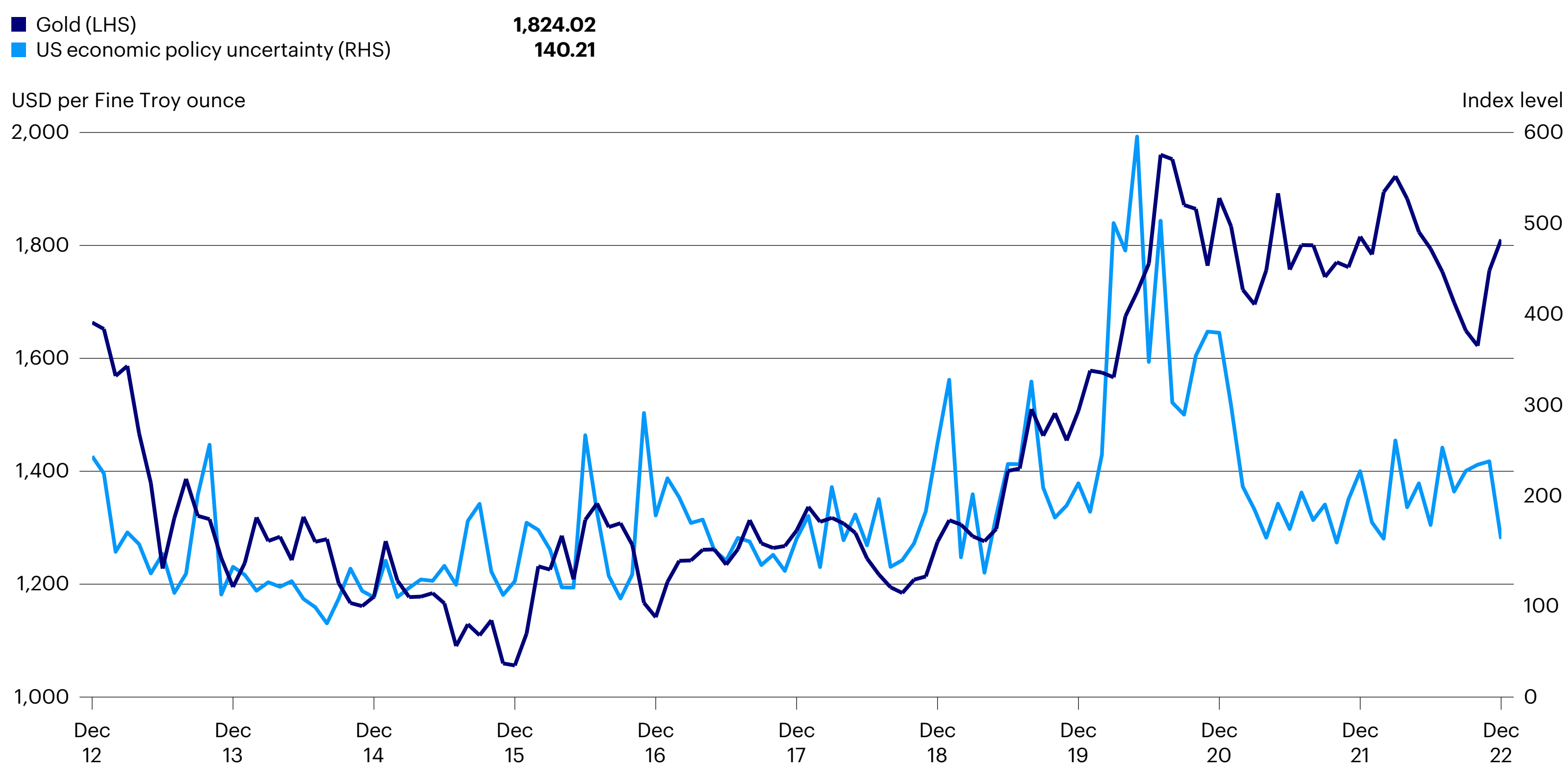
-7.6%



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

Gold price and economic risks

US economic policy uncertainty turned down sharply at the end of the year, disconnecting from the higher gold price. Economic uncertainty had been increasing gently recently but has not had an influence on the price of gold. Potential for a shock this year is most likely around monetary policy but there are other possible sources relating to a US recession and political risk. Any such shock could result in the two variables re-joining.



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Contributors

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 31 December 2022, unless otherwise stated.

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