Executive Summary
Gold prices continue to trend lower, having retraced just over half the gains seen since the bull market began in 2001. There may well be more room on the downside as the US dollar strengthens and US monetary policy tightens.

Economic hardship and other factors are weighing on physical demand and strong returns in other markets mean investment demand for Gold is weak.

We would not be surprised if Gold prices fall further, but not much further. We expect physical demand to pick-up in 2016 and firmer prices should also instil confidence. We expect prices to continue to trade either side of $1,100/oz.

Introduction
Gold prices followed a similar pattern in 2015 as that mapped out in 2014, with prices rallying at the start of the year before heading lower as the year progressed. In late 2014 and early 2015, Gold prices rallied on the back of a combination of further central bank easing and a rise in geopolitical concerns over Ukraine and Greece. Monetary policy was seen to be easing as numerous central banks cut interest rates, which suggested a ‘race to the bottom’ as countries lowered interest rates to weaken exchange rates in the hope of boosting domestic growth through exports. Running in parallel to this was growing concern that the new Greek government would push Europe back into a crisis as talk of Greece exiting the euro re-emerged. The Ukraine/Russian standoff was also an issue. These led to a rally in Gold prices to $1,307.90/oz, from around $1,168/oz at the start of the year, and from the November 2014 low of $1,131.60/oz. The rally ended on 22nd January, when the ECB announced it would expand its asset purchase programme. Despite this being another form of quantitative easing (QE), the market saw this as yet another sign that policymakers would do all they could to prevent another crisis and that reassured markets, reducing investors’ need for safe-havens. The move was also a green light to the dollar, which was a negative for Gold. As a result, Gold prices started to fall again and despite some large counter-trend moves in March to April and August to early October, the downward trend has dominated with prices moving down to a fresh low at $1,052.80/oz, a level not seen since February 2010. The ups and downs in Gold during the remainder of the year have been caused by a combination of changing levels in market fear and how hawkish or dovish the Fed’s comments have been. China’s currency devaluation spooked the market, which led to a rally in Gold, while the switching stances of the Fed have led to significant rallies and corrections. Given that the dollar has rallied strongly since mid-2014 and Gold prices have sold off, both in anticipation of a rate rise, we cannot help but think the initial interest rates rise is already priced-in. As such, we feel 2016 will open a new chapter for Gold.
The Big Picture

The big picture is about to change, in that the fairly synchronised phase of global monetary policy easing since the financial crisis is now going to end as the US starts to normalise its monetary policy by raising interest rates. Other major economies, including the EU and China, look set to ease monetary policy further, so the global economy is likely to see greater divergence, which is bound to cause stresses to the financial system. At the very least, rising interest rates in the US and low rates in other economies are likely to lead to more capital flows and with that, political friction. These changes will come as no surprise to the market as they have been well telegraphed in recent years and accordingly there should be little initial reaction to a US rate rise, indeed we would not be surprised if some of the steam comes out of the markets with the recent trends correcting for a while – i.e. a pullback in the dollar and a rebound in Gold. There is precedent for this as highlighted by the market saying ‘buy the rumour, sell the fact’. But looking further forward, the changing US interest rate cycle could lead to a much stronger dollar down the road. The long term chart of the dollar index shows how much further the dollar could run.

At face value, if the dollar does continue to rise then we would expect Gold prices to come under further downside pressure and this is probably what the Gold price is discounting still. However, if the dollar rises, then that implies weakness in other currencies and investors in those countries may well look at Gold as a means to protect against their currencies being devalued. In addition, a rising dollar will make it harder for economies that have borrowed in dollars to service their debt, which would increase the risk of further fallout in emerging countries, which again could lead to a pick-up in demand for safe-havens. As such, we are not convinced that a continued run up in the dollar would necessarily mean weaker Gold prices, at least to begin with.

In the short term, we expect the dollar to consolidate once the initial US interest rate rise has been made and that may well lead to an upward correction in Gold prices. The emerging markets have had time to prepare for the US rate hike, so the initial reaction should be minimal, but once the first rise has been made the market’s attention will focus on when the second rise is likely and this could start to unnerve confidence in emerging markets and that we feel will underpin Gold prices, at least for a while. A second US rise is likely to be more dependent on US inflation and if inflation is seen to pick up then that could help underpin demand for Gold.

Equities are still near record highs and with dips just attracting fresh buying, the opportunity cost of holding Gold remains high, but a correction could be triggered in the aftermath of a US rate rise and when that happens it may well be the case that Gold looks like a relatively cheap safe-haven compared with an already stronger dollar and high priced treasury markets.

While the need to monetise Gold seems to have waned as confidence in the financial system has recovered, it seems that the bullish case for Gold will rely more on physical demand for Gold and here we feel the upwardly mobile Chinese and other Asian populations will remain important consumers of retail Gold in the long run. Countering that, we fear the novelty of ETFs, having been around for ten years, may have worn off. Over the past two years, ETFs have become a source of supply rather than demand, but they will remain a convenient vehicle to invest in Gold through when the market needs such a vehicle.
FACTORS DRIVING GOLD PRICES

The dollar

The inverse correlation between the dollar and Gold prices is crystal clear in the chart opposite and there have only been a few instances where Gold prices have been rising at the same time as the dollar has been rising, as seen in the boxes on the chart. The first one we would say was in 2005; the dollar turned higher as in late 2004 the US started raising interest rates as high oil and commodity prices were increasing inflationary pressures. Gold managed to rise in concert with the dollar rise as the dollar was rising on the back of inflation and the newly launched ETFs were attracting a lot of interest. The second box was in April to September 2011, which happened as safe-haven concerns rose over the debt situation in Europe at a time when geopolitical unrest in the Middle East and North Africa were raising inflation concerns on the back of rising oil prices.

In the short term, the dollar’s rise may have already discounted the first US rate rise, so we would not be surprised to see some consolidation in the dollar, but the trend in the dollar seems set to rise and that is likely to prove a headwind for Gold further down the road.

Opportunity cost

Bull markets in equities in recent years have flourished, especially as concern about the stability of the financial system has disappeared. As the equity bull market unfolded and record highs were set, the opportunity cost of holding Gold increased and investors rotated out of Gold and into equities, property and bonds. The slump in Chinese equity markets that unnerved markets around the globe in July and August led to a rally in Gold prices, but it was short-lived. We think, however, that with equities back in high ground, but with the market wary that tighter monetary policy in the US might cause headwinds for equities, Gold could be well placed to benefit if an equity correction gets going. The reason for this is that money coming out of equities will need to go somewhere and Gold prices have already corrected heavily over the past four years. You could argue that money would be more likely to go into the dollar and treasuries, but we would say their prices are already high. In addition, higher interest rates are likely to weigh on bond prices and falling bonds and equities could weaken the dollar as foreign investors liquidate.

Inflation and Deflation

One of the fears about QE was that it would lead to inflation, but that has not been the case. The US has used QE to stave off deflation, but even with a generally healthy recovery there is little sign of inflation picking up. China has in recent years been trying to cool inflation and that has now been achieved by deflating its housing bubble, but in doing so it is now suffering slower growth. Less concern about inflation in China and other Asian countries may well be a negative for Gold, as
households feel less need to buy Gold as a way to protect them from inflation. Japan’s QE has seen the economy switch from deflation to inflation, but it is struggling to see inflation take hold and the same is true in Europe to the extent that the ECB may have to increase its asset purchase programme, or lower deposit rates. So for now a lack of inflation seems to be troubling the global economy, while deflationary pressure remain present and low and falling oil/commodity prices are not helping. We do feel a return to higher oil prices would quickly feed through raising inflationary expectations. Generally, in deflationary periods you would expect government treasuries to do well as even a small yield is good in such an environment, but we would argue that Gold could also do well. If faced with deflation, we would expect the governments to do more QE and in turn that would likely debase currencies further, whereas although Gold would not pay a yield, it would stand a good chance of holding its value against currencies that are being debased. Once inflation does return, as we think it will as commodity prices recover in 2016, we expect some of the money flowing out of bonds to move into commodities.

De-hedging / hedging
At the start of the bull market for Gold in late 2001, which roughly coincided with the start of de-hedging, the total hedge book stood at 3,107 tonnes (99.9Moz). At the end of Q1’15, the hedge book stood at 193 tonnes, up from 129 tonnes in Q1’14, according to the Thomson Reuters GFMS. In recent years, as the hedge book shrunk, the level of de-hedging slowed and as it did it meant less support for Gold prices. In 2014, the hedge book increased by 103 tonnes, thereby adding to supply, but the increase was the result of two large hedges, which suggests no major shift in attitude towards hedging. Shareholders tend not to favour hedging. Most hedging done nowadays tends to be as part of a project financing deal. Looking forward, with the dollar likely to rise further as US interest rates rise, there is potential for lower Gold prices, perhaps to the $950-$1,000/oz area, and with prices then likely to be closer to producers’ production costs, there may well be a pick-up in hedging, probably via options.

Central Bank Activity
For many years, central banks were net sellers of Gold and in order to sell in an orderly manner and not to spook the market a Central Bank Gold Agreement (CBGA) was put into force to limit sales over a five year period. The first CBGA started on 27th September 1999 and ran for five years; it allowed for 2,000 tonnes to be sold and all of it was sold. The second agreement (CBGA-II) allowed for 2,500 tonnes to be sold and during that period 1,884 tonnes was disposed of; CBGA-III allowed for 2,000 tonnes, but only 207 tonnes was sold and the bulk of that was from the IMF. Given how little of the quota was filled under CBGA-III, the market was surprised that a fourth CBGA was signed, however it was and is now in effect, but only 6.8 tonnes were sold last year (27th Sept, 2013 to 26th Sept, 2014) and 3.4 tonnes were sold in the most recent year, ending 27th September 2015.

While sales under the CBGAs have dried up, other central banks, mainly in emerging markets, have been buying. In 2014, they collectively bought 590 tonnes and
in the first nine months of this year they have bought 426 tonnes, which annualised would equal 568 tonnes. Diversification seems to be the main driver with Russia consistently one of the larger buyers; it bought 144 tonnes in the first nine months of 2015, with Kazakhstan, Jordan, Ukraine, UAE and China also buying. China, after six years of not updating its reserves, has started to report its holdings on a monthly basis and has added 50.1 tonnes during the third quarter. Its reserves now stand at 1,708.5 tonnes, but that only represents around 1.6 percent of its total reserves.

**China’s Official Gold Holdings remain low**

In July, China updated data on the amount of Gold it was holding in official reserves to 1,655 tonnes, having last updated the record in April 2009, when it reported that it held 1,054 tonnes. China is now reporting monthly data and has been topping up its reserves each month. The increase in transparency was believed to have been in an effort to support its campaign to get the yuan included as one of the IMF’s reserve currencies, which it has now succeeded in doing. The fact that China is becoming a regular buyer of Gold should be viewed as a bullish development, we think, especially as Russia’s holding now accounts for some 13 percent of its total reserves, which may be getting near its upper limit. Russia’s buying has built up steadily; in 2008 it held just 2.5% of its reserves in Gold. With the US, Germany, Italy and France all holding over 60% of their reserves in Gold, there may well be room for China to step-up its purchases. If China were to have 10 percent of its reserves in Gold then it would mean holding 10,680 tonnes, which would put it at the top of the table in Gold ownership. With Gold prices under pressure and it being a buyers’ market, now may well be an opportune time for China to be buying. Generally, it is emerging market countries with Gold mining capacity that have been buying production, rather than countries buying in the open market.

**Oil and Gold**

Oil and Gold prices have tended to be positively correlated, although both commodities have been suffering weaker prices – oil prices have fallen more aggressively than Gold in the past year, although in 2011 to mid-2014, Gold prices were falling while oil was flat. As the Gold/oil ratio chart shows, oil prices are now relatively weak compared to Gold. With cheap energy prices now the lynchpin of inflation, any lasting rebound in oil prices could quickly pass through to inflation. In turn, that could pass through to Gold, firstly as a hedge against inflation and secondly as higher oil prices could increase concerns about economic growth and corporate costs, which could lead to stock market corrections, further boosting demand for gold as a safe-haven. It is well documented that these low oil prices are causing significant distress to oil producing countries,
especially those that still have their currencies pegged to the dollar. As such, we expect a rebound in oil prices next year.

**Demand**

Gold demand amounted to 4,424 tonnes in 2014, according to the World Gold Council (WGC), of which jewellery absorbed 56 percent, industry 8 percent, coin and bar investment 23 percent and central banks buying 13 percent. In the first three quarters of 2015, each area has continued to take up roughly the same percentage of total demand, totalling 3,243 tonnes, which annualised would equal 4,323 tonnes. The main swing factor in demand in recent years has been whether the ETFs have been net buyers or not. From 2013 onwards, ETFs have been net sellers, so they have been a factor of supply, but between 2004 and 2012, ETF buying was a major contributor to demand. In 2014, excluding ETFs that were net sellers, demand for Gold fell 17.8 percent compared with 2013, as demand dropped across all sectors. In the first three quarters of 2015, demand is down just 1.9 percent, with demand down in most sectors other than for coins and bars, an area showing growth of ten percent.

**Jewellery demand**

Jewellery accounts for the majority of global Gold use and historically accounts for around 80 percent of Gold demand. The bull market in Gold prices that started to accelerate in 2005 when prices started to move up above $500/oz did start to negatively affect demand, with jewellery demand as a percentage of total demand falling to 43 percent in 2011. The percentage drop coincided with the pick-up in demand from ETFs, but even on a tonnage basis less metal was being consumed, with demand dropping to 1,817 tonnes in 2009 from an average of 2,636 tonnes in the period 2000 to 2008. Needless to say, this was not just price orientated; the financial crisis curbed spending on luxury items too. The recovery in jewellery demand in 2013 was primarily driven by a surge in demand from China, with Hong Kong and the Middle East also seeing a pick-up. Since 2013, the pullback in demand has come about for a number of reasons. China destocked in 2014, after seeing rapid gains in 2013, but the massive bull run in equities then diverted discretionary spending towards investing in the stock market, where no doubt much was lost in the correction. India’s demand dropped as the government raised the import tariff in 2013, which remained in place in 2014 and last year uncertainty over the election held buyers back too. The Middle East wealth effect has been hit by lower oil revenues and the economic crisis in Russia has seen demand drop too. These are all external reasons for the fall in demand and that is why jewellery demand has for a change not been particularly price elastic. Another reason weighing on demand to some extent is that many Asian countries would view buying jewellery as an investment as well as an adornment, so the downward spiralling price may well have kept buyers on the sidelines. All the above factors, however, are likely
to mean there is a degree of pent-up demand for jewellery, so once a base is thought to be in place buying may well recover.

In 2014, global demand for jewellery fell 8.1 percent, to 2,383 tonnes; in the first three quarters of 2015, it has dropped 1.8 percent, according to WGC data. Our basic economic view is that the slowdown in China is expected to halt next year and that will be followed by a slow recovery as the service sector continues to grow and investment in the One Belt One Road mega project gathers momentum. In turn, this is likely to boost personal income and we would expect a recovery in broader based consumer spending, with disposable income not just going into the stock market. A stronger China should help lift global growth especially in emerging markets and, as the pie-chart opposite shows, stronger growth in these areas should be good for jewellery demand as the world (ex-Europe and the Americas) accounts for 88 percent of jewellery demand, with China consuming 33 percent and India 25 percent.

Indian demand for Gold, and thereby jewellery, has been affected by numerous cross currents in recent years mainly at the hands of government intervention which raised import taxes and restricted imports, having the effect of lifting premiums sharply at a time when world Gold prices were falling. Despite all the disruptions that have caused some large month-on-month swings in demand and imports, it appears that jewellery demand has held up relatively well, and that lower prices have led to good demand and restocking. In 2014, Indian jewellery demand for Gold was 604 tonnes, off just 2 percent on 2013, and in the first three quarters of 2015, jewellery demand was 480 tonnes, compared with 459 tonnes in the same period in 2014, showing a rise of 4.6 percent.

Looking forward into 2016, we expect demand for Gold jewellery in India to remain strong, especially as prices remain near multi-year lows. The big unknown, however, is whether the various Indian Gold schemes launched by the government will be successful in souring Gold from domestic hoards, which could reduce the amount of Gold imported. India in recent years has imported between 700-900 tonnes of Gold per year, so if this were to fall significantly it could have a big impact on the global supply and demand balance.

It is estimated that some 22,000 tonnes of Gold is held in India, some of which the government wants to monetise via the Gold Monetisation Scheme (GMS), where private holdings of Gold will be lent to the Scheme, interest will be paid and final repayment can be either in Gold or rupees. GMS could then lend or sell the Gold to gold consumers, such as jewellery fabricators. The government is also launching the Sovereign Gold Bonds (SGB) Scheme whereby investors can buy a bond and the return will be linked to the price of Gold. Whether the schemes are successful remains to be seen, they have got off to an embarrassingly slow start with just 400 grammes lent to the Scheme since it started on 5th November. As such, the government is likely to have to offer more in the way of incentives and we feel it is likely to take considerable time before they have a marked impact on imports and the global market.

Globally, given the significant price weakness, we expect demand from the jewellery industry to grow as jewellery retailers and consumers take advantage of these multi-year lows. In regions where jewellery is seen as an investment, it may well take a price recovery to spur a pick-up in demand. We are still very bullish for demand in China and Asia in general as the middle classes grow. The middle class in China is now estimated to be around 590 million strong, which is larger than the population of
Investment demand

One of the big changes in investment demand in recent years has been that net redemptions have outpaced buying in ETFs, which means ETFs are now more to do with supply than demand. This leaves only demand for bars and coins in the investment category. Holdings in ETFs peaked in January 2013 at 2,647 tonnes; they have since fallen steadily to a low of 1,511 tonnes – see chart below. Investor interest in ETFs started to wane as the Fed first started to talk about reining in QE, as if this was the signal that the financial markets were no longer at risk so there was less need for safe-havens. There have been a few periods that have seen ETF holdings rise, but they have not lasted, but then neither have the counter trend rallies. The big test will be if ETF holdings pick up once an uptrend returns – we think they will as they still provide a convenient way for retail and institutional investors to trade Gold. As such, ETFs should act as a good barometer as to whether investor interest is returning.

In 2013, the strong rise in demand for investment bars and coins led to a shift in physical Gold from the West to Asia. As ETF holdings were sold, the large bars were re-refined into smaller bars and coins that are popular in Asia and the Middle East. Out of the increase in global demand for investment bars and coins, 94 percent was seen in Asia. In 2014, demand for coins and bars dropped 41 percent, with the ban on imports of small bars in India hitting demand, at the same time as Chinese demand was weaker following the surge in imports in 2013 and as the stock market was attracting most investors' interest. For now, with Gold prices falling and the opportunity cost of holding Gold high, we feel demand may remain subdued. That said, prices falling from these already relatively weak levels may well start to boost bargain hunting and that is also likely once prices start to turn higher. Although the equity market may be strong and there are few concerns about the integrity of the financial system, the world still may have to come to terms with the mass of debt that has accumulated since the financial crisis. This, we think, is likely to underpin demand for investment Gold and in times of stress we would expect bouts of demand to be strong, especially when prices are considered relatively low.

The Futures market

The net long fund position (NLFP) has been volatile, with numerous large swings in the NLFP as seen by the shaded area on the chart. There was a big swing up to 157,000 contracts in late
October, driven by a belief the Fed would delay a rise to 2016, but that has been reversed recently as the Fed has become more hawkish. Generally the fund shorts have been more active than the longs – the longs were active early in the year with the gross long position climbing to 238,000 contracts; it then averaged 187,000 contracts between February and mid-October, before ramping up to 233,000 contracts in late October. As we head into December, the gross long position is mid-range, while the gross short position is elevated so there may not be that much more selling energy should the Fed raise rates. The combination of weak prices, a relatively large gross short position and the fact a rate rise is likely to be well and truly priced in, suggest the market is vulnerable to another short-covering rally.

SUPPLY
Gold supply to the market can come from six sources: mined output, scrap sales, official government sales, producer hedging, redemptions from ETFs and private stocks. If India’s Gold Schemes work then a flow of Gold from private hoards may well become an important factor of supply, although we do not expect this to happen in a hurry. With Gold prices having been falling for four years, mine supply is likely to suffer in the years ahead as mining companies have cut back on development-stage projects. In 2014, mine supply totalled 3,138 tonnes, supply from scrap was 1,168 tonnes, producer hedging added 104 tonnes and 183 tonnes of metal came from ETFs, so total supply was 4,593 tonnes. Official Gold sales dried up in 2010.

Mine supply increased 2.2 percent to 3,138 tonnes in 2014, according to WGC, as new mines and expansions, commissioned when Gold was in a bull market, saw production ramped up. Growth in mine output in 2014 was slower than in the preceding five years when it averaged four percent. In the first nine months of 2015, output was 2,364 tonnes, up 2.4 percent compared with the same period in 2014. Looking forward, low prices are likely to see some higher cost mines close and a cut in development budgets and capital expenditure is likely to delay the start-up of new mines. Although mine production is expected to drift lower, supply to the market from producers could increase if they start to do more forward hedging as that would require the borrowing of metal, which is then sold to form a hedge. The practice of forward hedging on a large scale ended in 1999; in the seven years before that an average of 280 tonnes, some 10 percent of mine output, was hedged each year. In 2014, 104 tonnes of producer hedging was seen, which represented 3.3 percent of mine production. In the first three quarters of this year there has been some hedging, but it has been more than countered by de-hedging. The 20 tonnes of hedges that were put on in the third quarter were done by a few producers to lock-in cash flow. So despite four years of falling prices it does not look as though the appetite to hedge has returned. Whether this changes if prices look set to fall, to stay down for longer and to start to encroach on producers’ all-in sustaining costs remains to be seen. It is one thing for shareholders not to like producers hedging away profit potential, but quite another issue to hedge the bottom line to avoid losses or possible closure.

The forward price curve for Gold on Comex shows a contango with $4/oz difference between December 2015 and December 2016, widening out to a $12/oz difference between December 2020 and December 2021 – so not a lot of contango to take advantage of for nearby hedging, but five-year forward gold prices are $58/oz higher than current prices.
In recent years there have been some interesting trends where Gold production has been growing; generally it has become more diverse, with China, Mongolia, Canada, Russia, Dominican Republic, Mexico and the Democratic Republic of Congo seeing strong growth, while South Africa and Indonesia have seen output fall. China’s Gold production has taken off in recent years, with output rising to 462 tonnes in 2014, an increase of 5.3, and up 35 percent compared with 2010. The country overtook South Africa as the world’s largest producer in 2007 and has not looked back since. South Africa was the world’s 6th largest producer in 2014, it was overtaken by Peru who became the fifth largest producer, with the US, Russia and Australia now the fourth, third and second largest producers respectively.

In 2015, it looks as though mine output will increase slightly, judging by the performance so far this year, but we would expect lower prices and producers’ efforts to cut costs to lead to lower production in 2016 – we expect it to drop three percent.

Scrap

Gold supply from scrap tends to be price elastic, as can be seen from the chart. It is all-important as it accounts for a significant proportion of supply, although it does vary depending on Gold prices and economic hardship. Scrap supply shot higher in 2009 and 2010, as the combination of high prices and economic hardship led to a surge of old Gold coming out of the woodwork, enticed out not only by record high prices, but all also widespread and high profile advertising campaigns. Scrap accounted for around 22 percent of supply in the early 2000’s; it accounted for 40 percent in 2009, but has since slipped and has slipped more so since prices have started to trend lower. In 2014, 1,247 tonnes of supply came from scrap, which was down from a peak of 1,728 tonnes in 2009. In the first nine months of 2015, 857 tonnes of scrap has gone into supply; annualised that is around 1,142 tonnes, which would make up 26.6 percent of supply. With a lot of old scrap sucked out of the system since 2009, much of which had probably accumulated over many decades, we would be surprised if there was much old scrap remaining. As such, scrap may not be as price elastic on the upside as it was in the 2008 to 2012 period. For 2016, we expect scrap supply to remain around the same level as this year.

Overall, with mine output expected to be falling slightly next year and with scrap supply expected to remain stable, Gold supply is likely to drop marginally in 2016. That could change if mining companies start to hedge more, or if redemptions from ETFs gather pace again, neither of which we expect; indeed we would not be surprised to see ETFs edge higher as Gold prices stabilise.
Technical Outlook

Although Gold prices continue to move lower, downward momentum has slowed and prices seem to be finding support below the 50 percent Fibonacci retracement line of the 2001 to 2011 rally. Prices have been trading in a falling wedge on the chart as seen by the red dotted lines, but in recent months prices have breached the lower boundary. These breaches could be false downward breakouts, or a sign that support is being eroded, in which case a drop down to the $1,000/oz would likely follow. A move down to the $1,000/oz still seems likely, as this would take prices back to the level where they were trading ahead of the financial crisis. A move back to that area may well mean Gold has rid itself of all the support it got from QE – at least psychologically. The high before the financial crisis was $1,032.60/oz in March 2008, the low to date has been $1,152.80/oz. On the upside the 20 month-moving-average is at $1,198/oz, this line has done a good job at capping rallies since July 2014, so we would continue to look for resistance around that line and at the top of the wedge pattern that is at $1,127/oz.

Forecast & Conclusion

Gold prices peaked in 2011, so they have now been in a bear market for four years and although it feels as though prices have fallen a long way, a look at the chart above shows prices are still relatively high, compared with where they were in 2005-2007. Interestingly, prices have now all but given back all the gains seen during the period of QE, so it may be that the sideways-to-down trading range of late is the market consolidating after the excesses of all the liquidity that was thrown at markets after the financial crisis. Indeed, as the financial markets have survived the crisis the need for Gold as a safe-haven has been reduced – the redemptions in the ETFs highlight that. With other markets booming, notably equities and bonds, the opportunity cost of holding Gold has proved too high, so it is not surprising that investment money has rotated out of Gold.

Recent years have also seen a lot of economic hardship, high levels of youth unemployment in Europe, the Arab spring and unrest in the Middle East, slower growth in China and falling commodity prices, which have all meant global growth has slowed. In turn, it stands to reason that consumers have had less to spend on luxury items such as jewellery, especially when jewellery will also have faced competition from ‘must haves’ such as smart phones. With jewellery accounting for 60 percent of Gold demand, we should not be surprised that demand has suffered, especially as investment demand has been lacking too.
Looking forward, we do expect the global slowdown to halt and for growth to pick up steam in 2016, which should lead to better demand for all aspects of Gold. Even investment demand may recover if prices are seen to have put in a base and start to edge higher. To get more bullish for Gold, we feel investors would need to become worried about their wealth again; it could be a stock market correction, or higher interest rates could start to focus investors’ minds on the huge levels of debt that have been created since the financial crisis. The chart above shows US debt, but it is the debt in other countries that is denominated in US dollars that may become a problem if US rates rise at a faster pace than expected. Generally, as Gold prices have already undergone a major, long-lived correction it may be that investors see Gold as offering a safe-haven again if needs arise and in such circumstances Gold and the dollar could rise in tandem.

On balance, we feel there is not much call for a safe-haven at present and while that has been the case, Gold’s fortune has been dependent on physical demand, which for numerous reasons has been weak. We feel lower prices will lead to some opportunistic buying and other markets will undergo corrections before too long and when they do then we expect Gold will benefit. Once Gold’s downward trend is widely considered to be over, then we would expect all types of Gold buyers to step off the sideline and back into the market. We still expect China, at both the government and retail levels and with its rapidly growing middle class, to be a long term bullish factor for Gold, but also feel Gold still has potential to offer a safeguard against how governments decide to reduce the debt mountain.

In our Gold Forecast Report last year, we expected Gold to trade in a $1,050 to $1,400 range; for 2016 we would look for a $950 to $1,280 range.
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