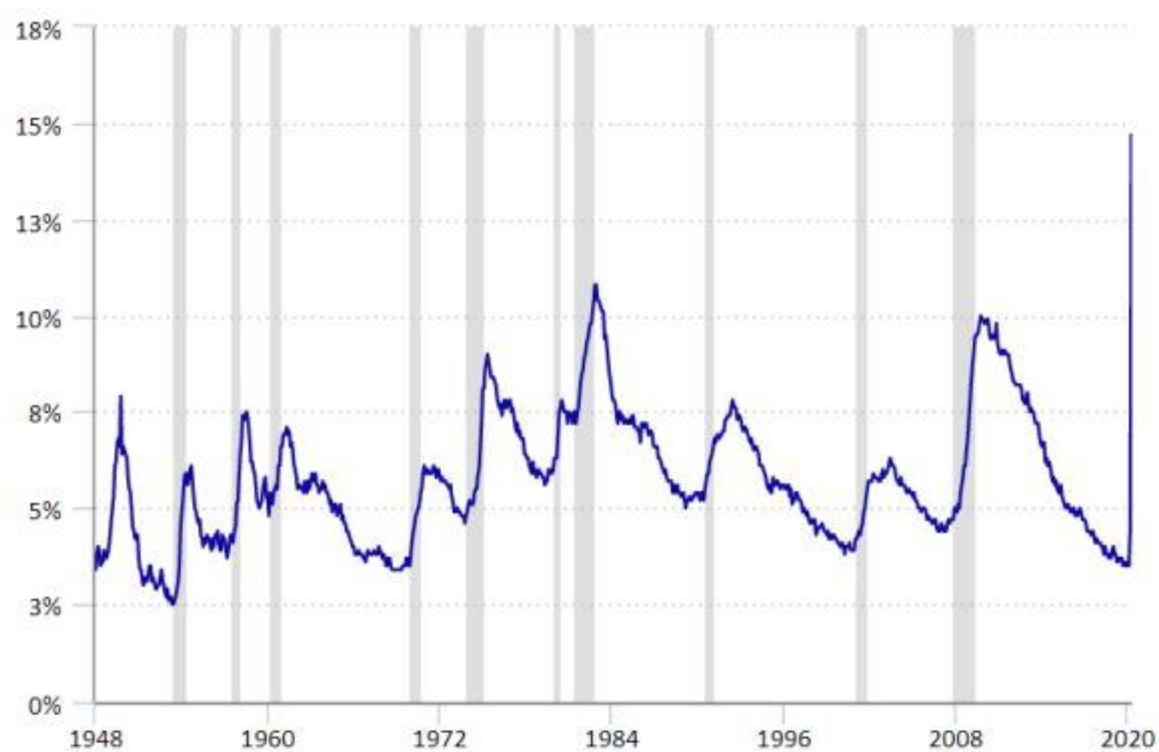
Gold - Special Report

September 25, 2020 FAT-GEQ-065

On track to retest record highs

The onset of the COVID-19 pandemic during the months of March and April 2020, dealt a harsh blow to the US economy. Lockdowns became the norm and the disruptions to business were serve and this was quickly manifested in a surge in US unemployment to record levels. The following chart show the long-term US unemployment rate:

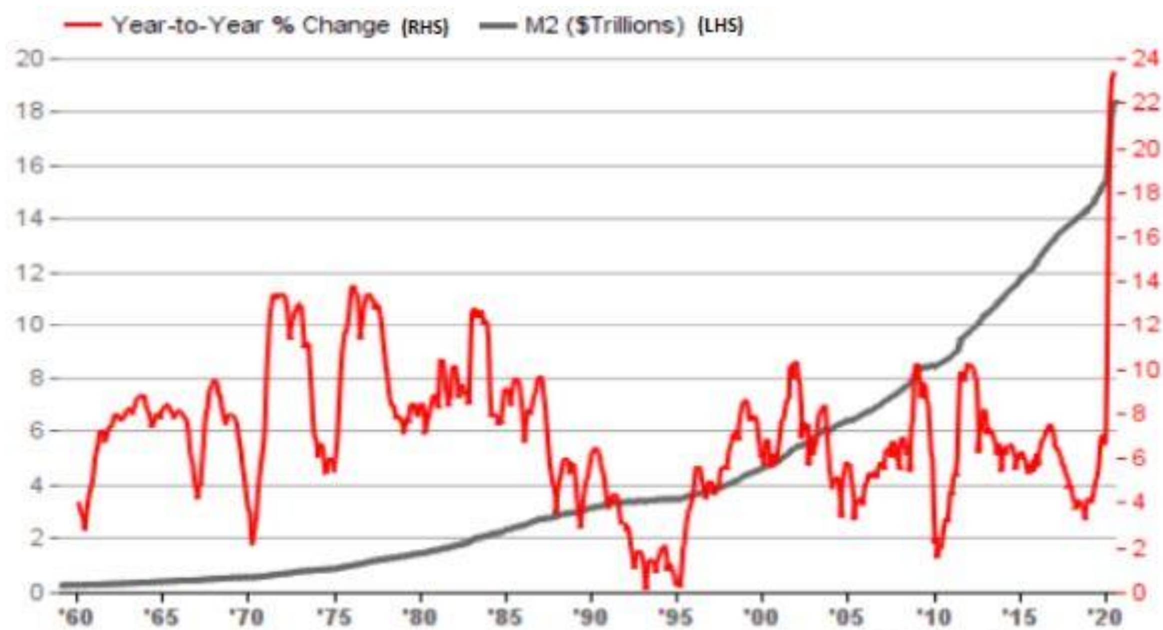


Source: US Bureau of Labor Statistics

With especially the US service sector hit hardest, as hospitality and tourism shutdown. Unemployment, as Members can see hit a **record** 14.7% for the month of April 2020 and in people terms 15.9 million workers hit the unemployment lines, **swelling the total to 23.1 million unemployed.**

The US government response to this reading was predicable with stimulatory programmes amounting to US$10 trillion and counting, rolled out. <u>The COVID-19 programmes were, unlike the Global Financial Crisis (GFC) counterparts, directed to the unemployed.</u> Much of the GFC programmes went to shoring up the financial sector and especially the banks before filtering into infrastructure funding.

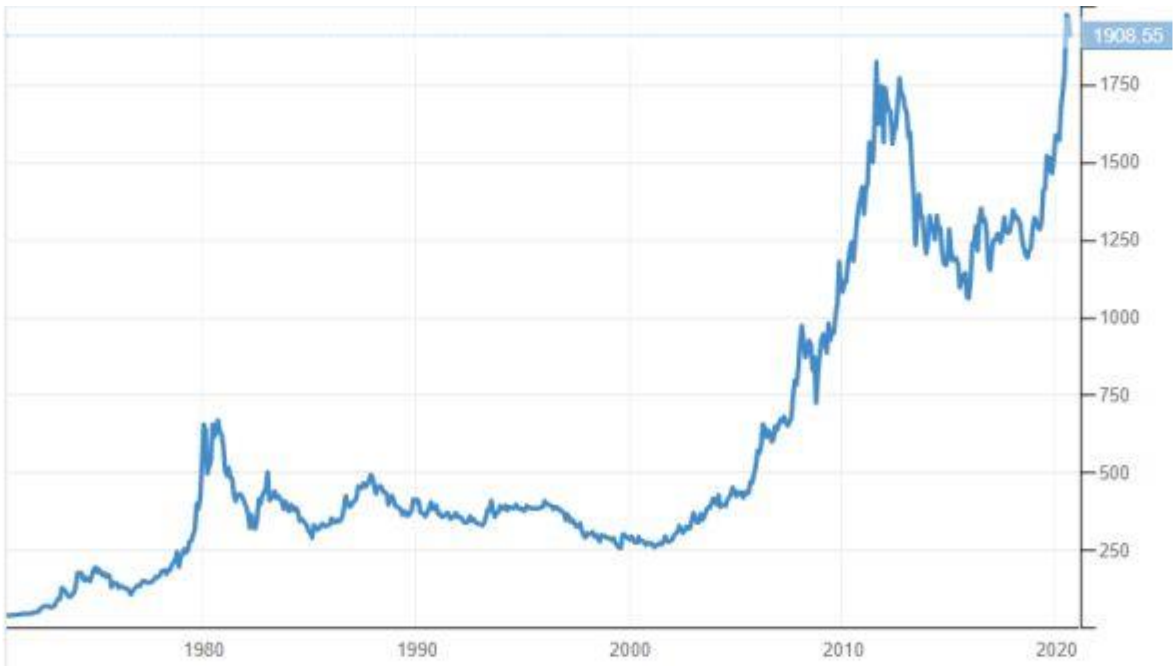
The upshot of the COVID-19 stimulatory programmes going directly to the unemployed as wage supplements, was a surge in US money supply. The following chart shows US M2 money supply:



Source: Shadowstats

We have espoused over the years in our daily communiques that fiat currencies devalue as governments pump more dollars into their economies. **The US Dollar has not been immune and has come under pressure as, with the implementation of these COVID-19 stimulatory packages, US money supply swelled.**

A weakening US Dollar has been a boon for gold over 2020, with the price hitting new records as it broke the US$2,000 an ounce barrier. The following chart shows the US Dollar gold price:



Source: tradingeconomics

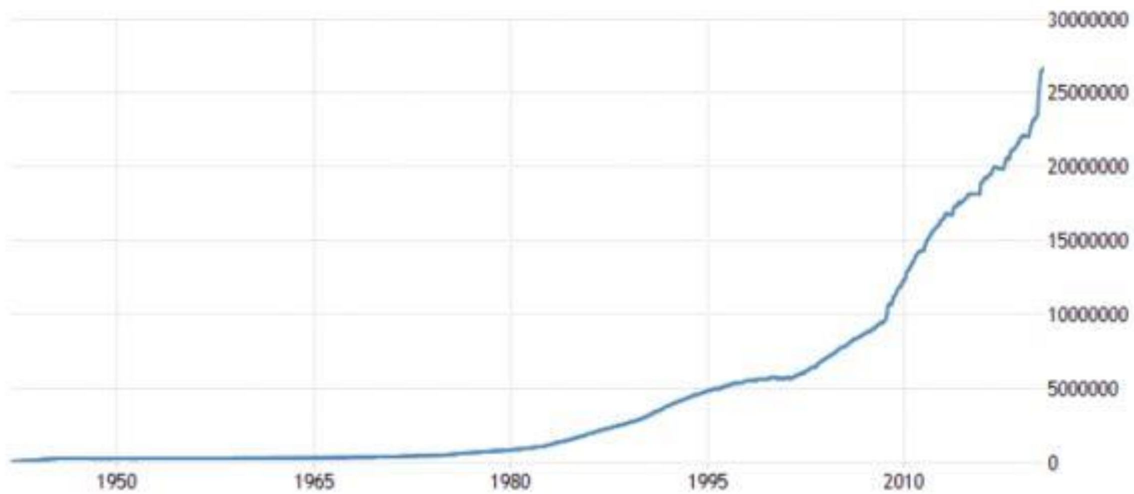
At its recent price peak, we flagged again in our daily communiques, caution as a likely broad risk off correction was brewing and gold having hit a record US$2,051 an ounce has now settled back at US$1,872 an ounce.

So, is the correction over?

Certainly, the first wave of stimulatory action by the US government is now in the gold price. There is more however to come, as the COVID-19 pandemic is not under control and continues to exert pressure on the US economy. The US Congress is already in talks around a further US$1.5 trillion of stimulatory initiatives and **our expectation is for further programmes to follow, this is while COVID-19 remains unchecked.** Only a successful vaccine may break this cycle, with the timing and efficacy of such a vaccine is unknown for now; **one will come to market.**

So, the first stimulatory wave that pushed the gold price to a record will still in our view provide a modest tailwind for the gold price, over the remainder of 2020. The US Dollar will remain under pressure as more dollars come into the economy.

A second tailwind for the gold price goes hand-in-hand with the stimulatory programmes, with the US debt pile burgeoning. The following chart shows US debt:

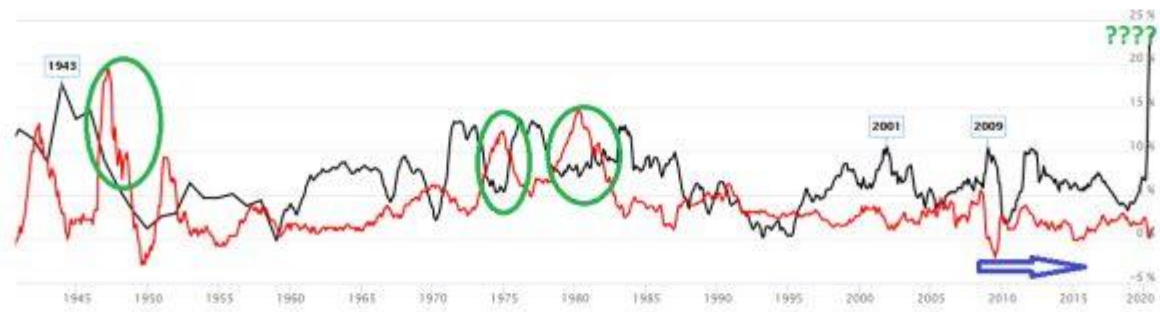


Source: tradingeconomics

Already at record levels and fast approaching US$27 trillion, we expect the pile will continue to grow, as the two political parties' line up programmes to sweeten the electorate. **The US government either Republican or Democrat** (post the election), and certainly the Democrats have signalled on going government spending programmes, will continue to **"Splash the government cash."**

The swelling debt pile now stands at some 107% of gross domestic product, and as this number grows will weaken the US Dollar. The Federal Reserve (Fed) will likely remain on the back foot and maintain an easy monetary stance to support US interest rates. **Already, the Fed's focus has shifted away from inflation as its primary concern to managing employment.** We view the growing debt pool as being a constant weight on the US Dollar going forward.

A third tailwind for the gold price over the remainder of 2020 and beyond, has been the most elusive, and that is inflation. We expected inflation to appear post the GFC and the stimulatory programmes introduced to counter the crisis; it did not (the purple arrow in the following chart). The following chart shows US M2 money growth and inflation:

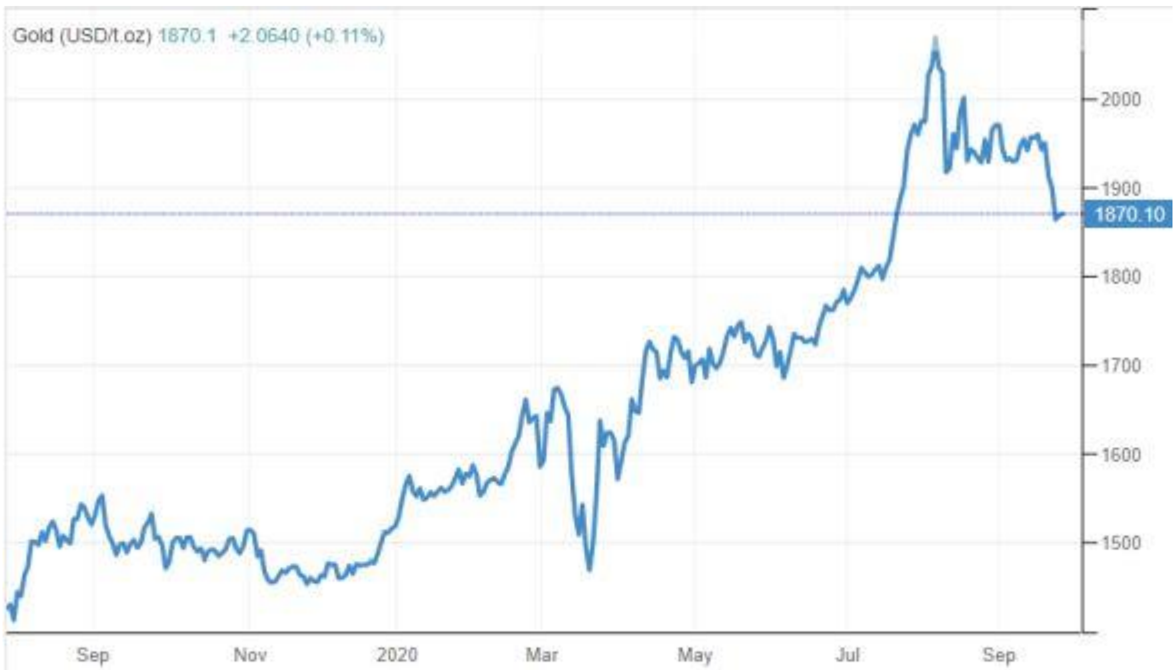


Source: Longtermtrends

Again, in our daily communiques we have raised the spectre of inflation being a distinct problem in the future and it is not without reason. **As Members can see from the above chart, there have been prior periods when US M2 has spiked and offset but following came inflation (green ecliptics in the above chart).** Again, as Members can see during the GFC, US M2 shrank and recovered but was other wisely relatively stable across the GFC years, as was inflation.

Certainly, the most recent surge in M2 growth to a record 23.3% (green ???? in the above chart), we believe, will bring inflation down the track. As we have quoted in our daily communiques, **the famous economist Milton Keynes once said, "everywhere inflation is a monetary phenomenon."** Members may have noted from the prior chart that the inflationary peak is relative to the surge in M2 growth. We are not suggesting that inflation may hit 23.3% in the US, but any higher levels above the consistent lows of the 21st century, will be harmful, <u>and once out of the bottle, it may be difficult to get it back in.</u>

Overall, the first wave of stimulatory spending has been a real tailwind on the gold price, pushing it to record highs. **As pressure comes out of the US economy, as data reads such as unemployment recede from record highs, the correction in the gold price may have already passed.** The following chart is a 12-month gold view:



Source: tradingeconomics

We certainly expect the stimulatory programmes will continue to have a positive influence on the gold price going forward, albeit less pronounced than the first wave. Such programmes will remain in place while COVID-19 continues to grip the economy. The US debt pool will be a constant source of agitation for investors for an extended period of time and we are perhaps contrarian when it comes to inflation.

We will persist with our end-year price forecast for gold in the range of US$1,925 to US$2,000 an ounce. We will however when looking into 2021 be likely moving the range higher. With the gold price now trading around US$1,872 an ounce and given our view of a second and third tailwind for gold, we will be quiet accumulators of gold stocks.

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