Technical Analysis: Gold

For uptrend to resume, price needs to recover back above 1250 soon.

| TECHNICAL ANALYSIS | GOLD| Technical Note

9 February 2015

Source: stockcharts.com

Gold's bearish candle breaking the 1250 seems bearish …

In our bottoming report, *Technical Analysis: Gold. Has Gold reached an intermediate bottom? Soon, if not **now***, we stuck out necks out and called a high probability bottom despite gold still being in a downtrend. We picked 1250 and 1350 as 1st and 2nd upside targets based on data available at that time. *Since then, gold surged to a high of 1307*, slightly more than halfway between our two targets. Since that high was made, the technicals looked promising as a bull flag was being formed in the last two weeks. However, gold dropped sharply on Friday after January jobs data beat expectations, seemingly re-instilling confidence in those that have been calling for the first Fed rate hike this year. The dollar surged as Treasury yields jumped, knocking the yellow metal to 3-week lows.

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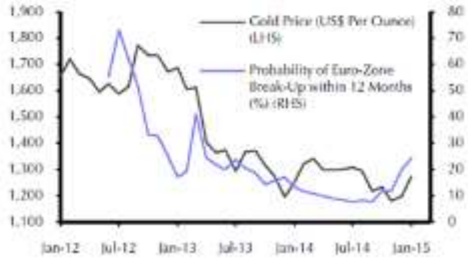
… but the media narratives can go either way.

At this part of the economic cycle, we believe we are technically *still* in a bull market, and any signs that reinforce this idea will be a *continued* headwind for gold prices, including the recent good job data in the US. However, at the same time, we note the long tailed upside risk as gold being triggered as a store of wealth as well as a safe haven. For instance, skepticism about the strength of the economy - pushing Fed rate hike expectations further into the future, or continued bigger than expected willingness by various central banks to keep easing monetary policies to fight off deflation, may cause investors to shift to gold to protect against devaluing currency. At the same time, with Greece at risk again to being kicked out from the Euro, will that cause more instability for the Euro? The chart by Sentix show that gold prices are correlated with the market's estimated probability of a Euro-Zone break up.



Sources: Sentix, Bloomberg

Technicals indicate a trading mentality at this point, with slight downside bias.

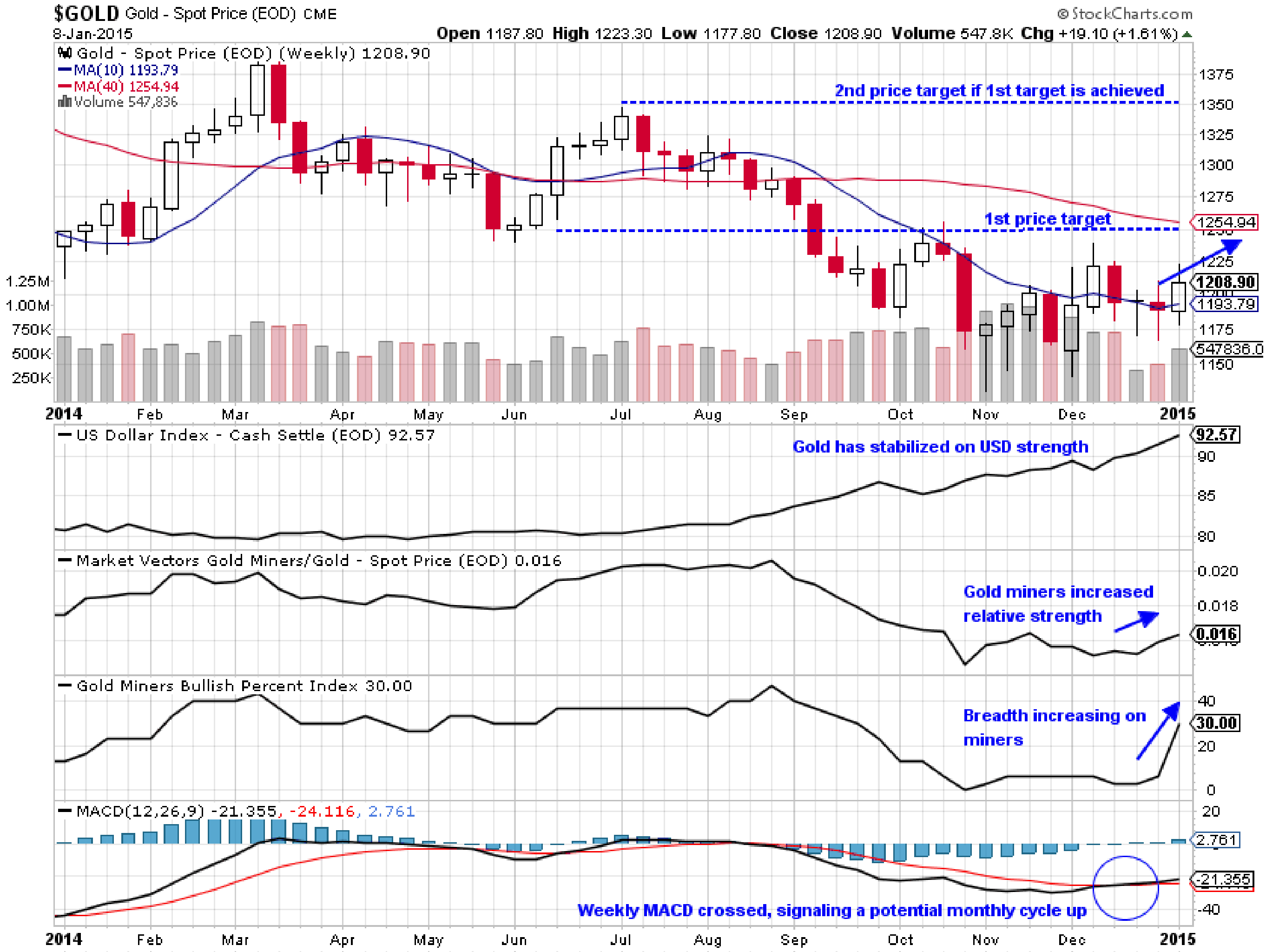
Friday's candle did quite a bit of technical damage, with RSIs and MACDs showing no sign yet of a reversal. However, gold price is sitting exactly on a significant support zone (1220-1240), if that zone breaks; price is likely to continue its short term down move as indicated by the daily MACD. On the other side of the coin, now is the moment of truth, for gold to resume its uptrend to the next technical target of 1350, it must recover its position above the 1250 support turned resistance soon. Hence, short term traders have to see which way price breaks out of due to gold being at an infection point. We also concede that the longer none of the tailrisks occur - Euro break up fears, or sputtering global economies that trigger more monetary easing - the greater the likelihood of a continued downtrend or consolidation.

Action:

For short term traders, look for support level of 1230 to break to trigger a sell, using 1180-1200 as a downside target, or oversold levels on the RSI. But, a convincing up-move to recover the 1250 level returns gold to an intermediate uptrend.

For the longer term investor, we think levels between 1000 and 1200 where we first wrote our first report is where the market views as cheap. Consequently, the closer it gets there, the more we can accumulate as a crisis or currency devaluation hedge.

The following is a summary of the main points of our 12 Jan 2015 report.



Recap from 12 Jan 2015: Gold down 33% since Aug 2012. Time to go contrarian?

The first signs of the death of gold started back when gold was pushing $1800 back in August 2012. Since then, gold prices have dropped all the way down to 3 year lows of $1130 as recently in November 2014 due to a combination of a strong USD, low levels of inflation, the increase of risk appetite and a strong US economy that was pushing investor cash into equities. Gold companies have made cuts over the past couple years, and have collectively taken billions of dollars in write-downs. According to PWC's Gold, silver and copper price report 2015, their industry survey shows that only 20% believe gold price will increase in 2015, 20% are neutral, and 60% think prices will decrease. Yet, in terms of technical analysis, the bottom of prices is always characterized by pessimism, is it time to go contrarian? We list a couple of technical factors that hint that strength in the market is building within a long downtrend:

1. **Improving underlying technicals.**

- **Gold priced has stabilized even through the USD has strengthened.** A rising USD usually applies downside pressure on commodities like gold. Resilience of gold price in view of the strengthening USD is akin to increasing tension on a spring that adds strength to the upside move when it eventually occurs in the future.
- **Though nascent, gold miners price and breadth are slowly increasing their relative strength.** Stock prices can sometimes be affected first before the actual move of

commodities as market participants are forward looking when making their investment decisions. The slight uptick adds encouragement to the bottoming view.

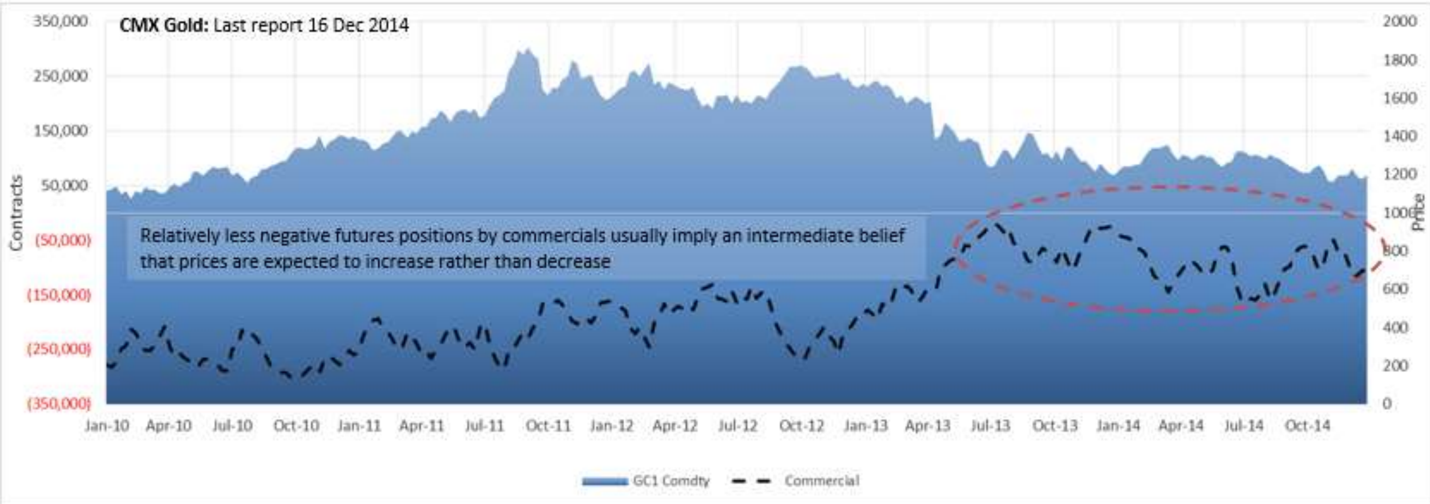
- **The bullish cross of the weekly MACD imply a potential upturn**. Unless price deteriorates sharply, causing technical damage that reaffirms the downtrend, the bullish cross implies at least a short term upturn, and a potential intermediate upturn that may last 1-2 months.

2. Gold commercials are hedging less at current prices.

Based on the Commitment of Trader's report, "commercials" are defined as entity that is commercially engaged in business activities hedged by the use of the futures or option markets. Commercial positions are usually more long term in nature and less speculative. The net futures position, since gold broke below 1400 in Apr 2013, has been significantly less negative as compared to prior years. This leads me to believe on a fundamental level, gold prices should start to see stability as the commercial market is not viewing current future prices for gold as expensive, hence they are hedging a lot less.

3. Since June 2014, high yield bonds have been on the downtrend.

Although the S&P500 has been on an uptrend, the iBoxx High Yield Corporate Bond Fund has actually decreased by 3% since June 2014. The divergence shows increasing risk within the system, which is coherent with recent geopolitical happenings such as the sharp fall in oil prices increasing the probability of defaults on oil exporting nations and oil producers with high cost of lifting. Any increase of perceived risk may cause increased gold prices capital looking for flights to safety.



Source: Bloomberg

However, we do note that gold is technically on a downtrend, and based on the market psychology of reflexivity or the feedback loop of cause and effect, downtrends can go on longer than expected. That said, based on the reasons above, we note underlying strength appearing within this downtrend. We are sticking our necks out with this call, as technically speaking, there is still no weekly upside breakout signal and trends tend to continue, yet we cannot ignore the improving underlying technical strength. Gold is also a crisis hedge if crude oil continues to fall in price, creating geopolitical instability.

We think there is a good chance gold's price should firm up again around current levels or maybe slightly lower. If gold cycles up, the first upside target is likely 1250. A successful break above this level signals completes a reverse head & shoulders pattern that started in Sep 2014 and implies a **further technical upside target of 1350.**

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