The SA Bullion Gold Report

Q2 2013

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Date: 18th July 2013

Table 1: Gold Performance to 30 June 2013 (% per annum)[1]

	Quarter[2]	1 Yr	2 Yr	3 Yr	5 Yr	10 Yr
Gold in US Dollar	-25.4	-25.4	-11.0	-1.4	5.1	13.2
Gold in Rand	-20.3	-9.5	7.3	8.0	10.3	16.4
Gold in Euro	-26.6	-27.5	-6.2	-3.3	9.2	11.7

[1] Based on LBMA Afternoon Fixes
[2] not annualized for periods of less than 1 year

Table 2: Quarter-End Gold Prices and Exchange Rates[1]

	Gold in US$/oz	R/$ rate	Gold in R/oz	$/€ rate	Gold in €/oz
30 June 2003	346.00	7.5	2,598.45	1.15	302.05
30 June 2004	395.80	6.2	2,458.81	1.22	324.92
30 June 2005	437.10	6.7	2,917.05	1.21	361.74
30 June 2006	613.50	7.1	4,375.33	1.28	480.72
30 June 2007	650.50	7.1	4,587.33	1.35	481.49
30 June 2008	930.25	7.8	7,282.13	1.58	589.21
30 June 2009	934.50	7.8	7,305.13	1.41	664.89
30 June 2010	1,244.00	7.6	9,443.93	1.23	1,012.70
30 June 2011	1,505.50	6.9	10,321.86	1.45	1,040.07
30 June 2012	1,598.50	8.2	13,123.35	1.27	1,260.45
30 June 2013	1,192.00	10.00	11,881.85	1.30	914.39

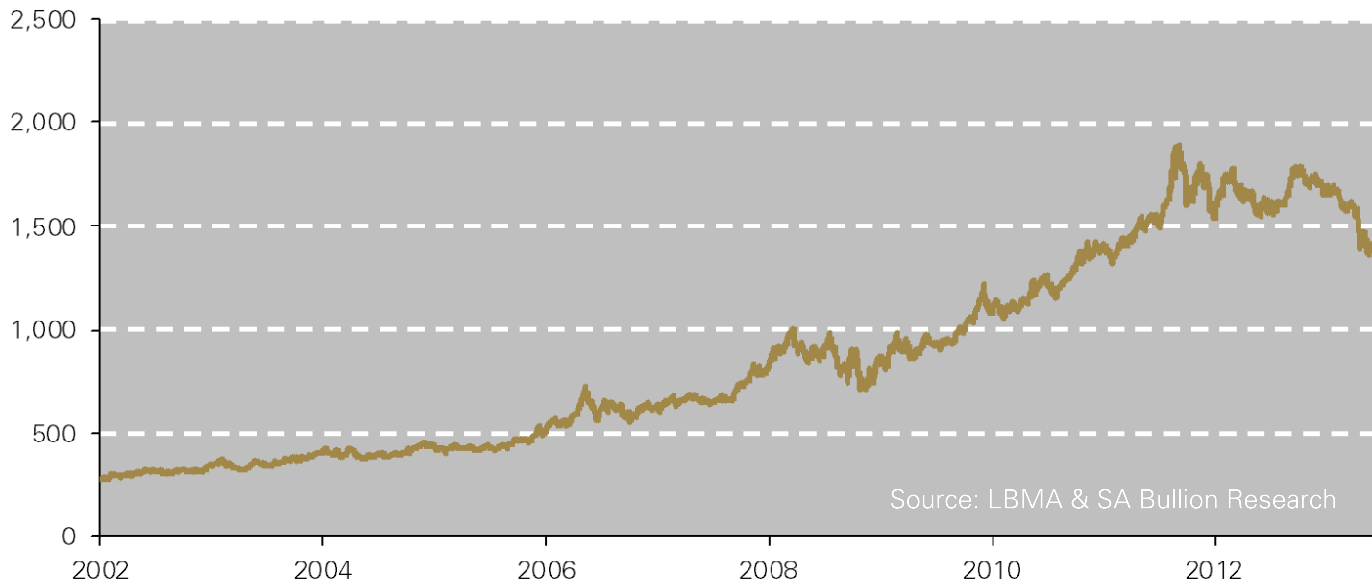
Note 1: Gold prices in US$ and € are LBMA Afternoon Fix prices
Note 2: Gold price in Rand from Rand Refinery
Note 3: Gold prices at time of writing—$ 1,297.25; R 12,731.99; € 987.47

Table 3: Calendar Year Performance of Gold

	% US Dollar	% ZA Rand	% Euro
2003	19.9	- 6.7	- 0.3
2004	4.6	- 11.7	- 2.9
2005	17.8	32.6	35.7
2006	23.2	37.0	10.2
2007	31.9	27.9	18.9
2008	4.3	41.1	9.7
2009	25.0	- 0.4	21.1
2010	29.2	16.1	38.2
2011	8.9	33.0	12.6
2012	8.3	13.6	6.2
2013 year to date	-28.1	-15.4	-27.0

Q2

Figure 1: Ten-Year Chart of Gold Price in US Dollar [LBMA PM Fix]



Gold Price Action in the First Quarter

The second quarter of 2013 was the worst quarter for gold in more than a decade. In US Dollars the gold price lost one-quarter of its value and put the gold price back to where it was three years ago. In South African Rand the price retrenchment was dampened by Rand weakness to result in a loss of one-fifth of value – putting the gold price back to where it was two years ago.

Almost all of the gold price losses were incurred in the first three weeks and the last two weeks of the quarter. In round numbers, gold went from $1,600/oz to $1,400/oz in the first three weeks of April, and went from $1,400/oz to $1,200/oz in the last two weeks of June.

In our First Quarter 2013 report I set out in detail the reasons for the price collapse in the period of 1 April to 21 April (even though this was post-quarter end). There were chiefly four reasons, related to: a report by Goldman Sachs, the implosion of Cyprus, disappointing Chinese growth and a big-money, manipulated trade in the US derivatives market.

We will discuss the last two weeks of June below.

Gold Price Action post-Quarter End

On 30 June gold was priced at $1,192 (The London Bullion Market Association PM Fix). At time of writing the Wednesday 17 July PM Fix was posted at $1,297.25, representing an 8.8% recovery in these 17 days.

Review of the last two weeks in June

Ben Bernanke, Chairman of the US Federal Reserve Board (the "Fed") made a pronouncement in mid-June regarding US economic recovery and a tapering-off of the quantitative easing ("QE") program "later this year". The current QE3 program entails Fed purchases of treasuries and Mortgage Backed Securities to the extent of $85 billion per month in order to engineer low long term interest rates so as to save the US economy.

Fed-talk prompted panic in financial markets as money-managers felt wrong-footed with respect to QE-tapering (i.e. a winding-down of central bank monetary stimulus). In typical fashion the market over-reacted and responses were to dump bonds (10 Year Treasuries went from a yield of 1.5% to 2.5%), dump emerging market (EM) currencies, dump gold and scramble for US Dollars. The rout in bonds, EM currencies and gold was shocking, to say the least. On 16 June gold was priced at $1,391.25. By 30 June gold was knocked down to $1,192.00, fully 14.3% lower in a mere two weeks.

As an indication of EM currency depreciation, note that the South African Rand lost 10.2% of its value against the Dollar in just 91 days (i.e. the second quarter).

Commentary

The Fed was wildly over-optimistic at the time of Ben Bernanke's mid-June comments. If QE3-tapering requires the official rate of unemployment (the rather questionable U3 Series) to first come down to 6.5% then we would argue that QE3-tapering is a long way off. If QE3-tapering requires economic growth to first show strength and sustainability then we would again argue that QE3-tapering is a long way off. We shall take a look at these arguments.

Unemployment

According to the US Bureau of Labor Statistics (BLS), the official rate of unemployment stood at 7.6% at end-June. This figure is the same as that at the end of the previous quarter, but down from 8.4% a year earlier, which in itself would seem to indicate a considerable turnaround and the likelihood of 6.5% being reached in the not too distant future. This is however, not the true picture of US unemployment and is an overly rosy portrayal of reality. The U-3 series (i.e. the 'offical' rate) is highly manipulated. The ratio of unemployed workers to total labour force has been decreasing **BUT,** this because in the U-3 Series the BLS reduces the number of unemployed workers, not necessarily because they have been finding jobs, but because the BLS re-categorizes those people unemployed for more than six months as no longer unemployed. (Magically they disappear!) Essentially, those unemployed people who have suffered long term unemployment are no longer regarded as unemployed – they are regarded as having left the labour force out of choice.

A truer picture of unemployment is found in the U-6 Series which captures the long term disillusioned and underemployed workers. The U-6 unemployment rate currently stands at 14.3%. Even worse than the previous quarter-end figure of 13.8%! Better still is to look at not the **unemployment** picture but rather the opposite – the **employment** picture. With the greatest fiscal stimulus and monetary stimulus in the history of humankind, the number of employed workers has gone from 143.2 million to 144.8 million in the last year (a change of 58.9 to 59.0 in percentage terms). Hardly a picture of a robust recovery!

A note to you, our dear client. The US regulators have trumpetted the creation of 182,000 new jobs per month for the last year. Bear this in mind: the US population of 310 million is adding more than 200,000 people to the labour force each month! In order to stand still and have no further employment deterioration, the number of employed US workers must increase by at least 200,000 per month. (I hope you didn't choke on your coffee!!)

A final word on unemployment: we are great fans of the work of Shadow Government Statistics. The economists at Shadow Stats dissect the numbers so as to produce unadulterated statistics. They report that the actual unemployment rate is currently 23% and climbing.

Economic Growth

The Fed is obsessed with house price increases as a leading indicator of economic growth and it would appear that US house prices have bottomed and in some areas have turned up. We think this obsession is mistaken. [At this point it is probably as well to point out that the Fed is more commonly wrong than right]. To illustrate our point: the mid-June Bernanke comments caused a bond market collapse when yields went from 1.5% to 2.5% almost overnight. Bearing in mind that new mortgages are tied to the long bond rate it becomes self-evident that new entrants into housing (mortgages specifically), are faced with much stiffer mortgage servicing costs. If anything is a growth inhibitor this is it.

The point of QE-tapering, or simply the perception of imminent QE-tapering, comes as a hammer blow to long bonds but also to the servicing costs of debt of all descriptions. This effect will be felt in the business world (for corporate debt) and in the public sphere (for government debt) as well. The growth-inhibition effect is profound – worldwide. We strongly believe that the whole world in general, as well as the US in particular, faces a very fragile and dangerous future given decades of over-investment in capacity, massive over-leverage and the structural threat of deflation. For years we have been saying that the Fed is pushing on a string. We say this still.

In Closing

The US Fed has little ammunition left with which to fight this dangerous economic war. The weapons of stimulus and interest rate policy have been abundantly used and at best have helped very little. At worst, they have created aberrations for which we will all pay dearly at some future time.

The Fed's last major source of ammunition cannot get spent. And that is: Words! The Fed is strategically using word-choice and the media to provide encouragement so as to engender confidence, and from that, they hope…self-fulfilling prophecies. We are cynics and are more concerned with reality than with the wishful guidance of the Fed. For this reason we believe that hedging our bets and having some of our savings in gold makes sense. Maybe more so now that gold is so much cheaper and gold miners are being put out of business!

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