
Friday, May 11, 2012

In a trading pattern that has become all too familiar, the resurgence of Eurozone concerns, and poor US economic data sent investors sprawling back to safe haven assets, while equity indices and commodities prices fell. Gold especially, saw its new milestone, with futures plunging below its psychologically important level of \$1,600/oz, the lowest since Dec 2011. With technical indicators continuing to point towards lower prices at least in the short-term, the market sentiment on the bullion had slowly turned from bullish to severely bearish in the past 2 weeks. However, despite the recent lackluster gold performance, we remain unfazed over our long term year-end expectation of \$1,800/oz with fundamentals continue to point towards higher gold prices in the medium to long term.

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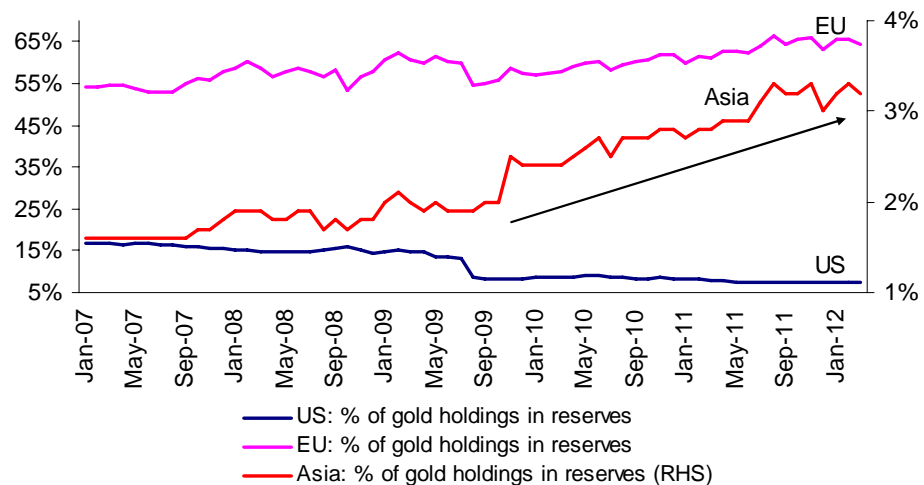
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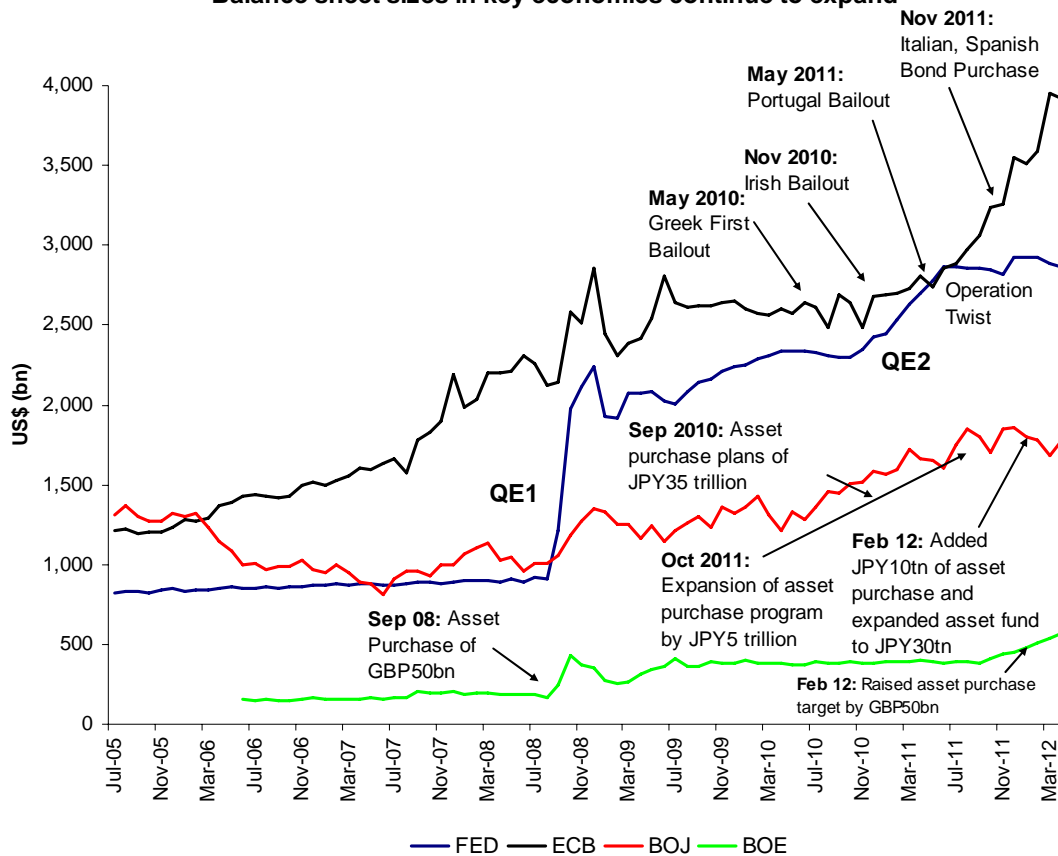
In our view, the most important factor for higher gold prices is potentially higher gold demand from key gold consumers: India and China. In a recent move, the Indian government had decided to withdraw the additional 1% duty on gold jewellery previously proposed in the Budget, bowing to pressures from a 6-week strike from gold retailers. With gold imports plunging to 30 – 35 tons in April, as compared to 90 tons a year ago, we expect gold demand to pick up on the resumption of businesses ahead of a new wedding season in September. Likewise, China's gold imports from Hong Kong had surged more than six-fold in 1Q12 to 135.53 metric tons, according to Bloomberg news. Moving away from Asia, central bank's interest in gold has also picked up, illustrated by gold buying from Mexico (+541k ounces) and Russia (+532k ounces) in March.

Asia interest in gold continues to rise


Source: CEIC, OCBC BANK

Meanwhile, low interest rates in the G7, especially in the US where interest rates will probably stay accommodative till 2014, while a potentially expanding balance sheet size in the ECB, Fed, BOJ and BOE may allow for more upside in gold prices. In particular, we believe that the mid-June FOMC meeting will be key in influencing gold prices, given that Operation Twist is set to cease in end-June and additional monetary stimulus may be introduced should US employment numbers remain less than satisfactory for a sustained period. Additionally, Fed Chairman Bernanke had previously reassured that the Fed “remain prepared to do more as needed to make sure that this recovery continues and that inflation stays close to target” and reiterating that additional bond buying is still “very much on the table” in his last FOMC meeting.

Balance sheet sizes in key economies continue to expand



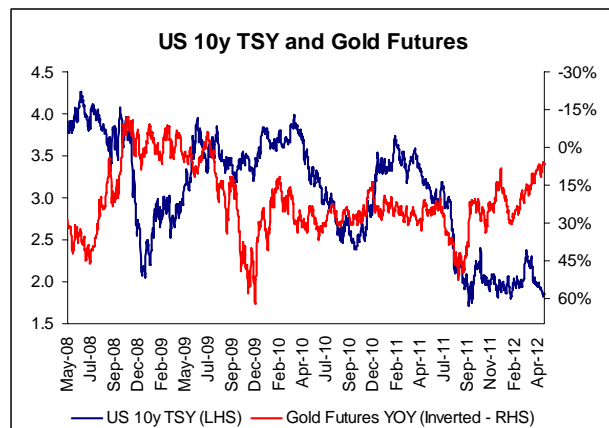
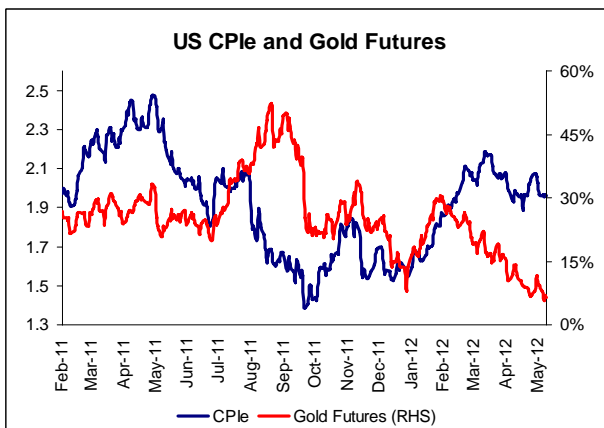
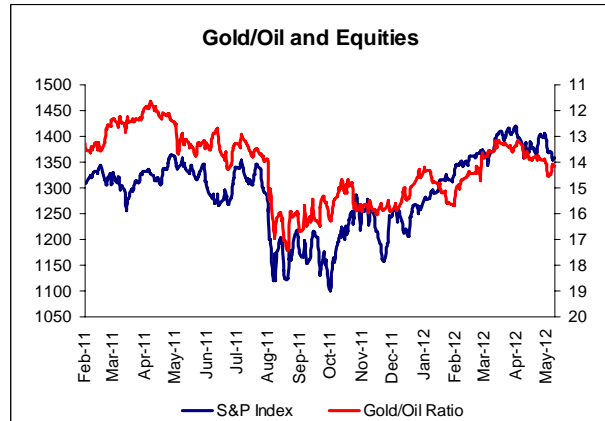
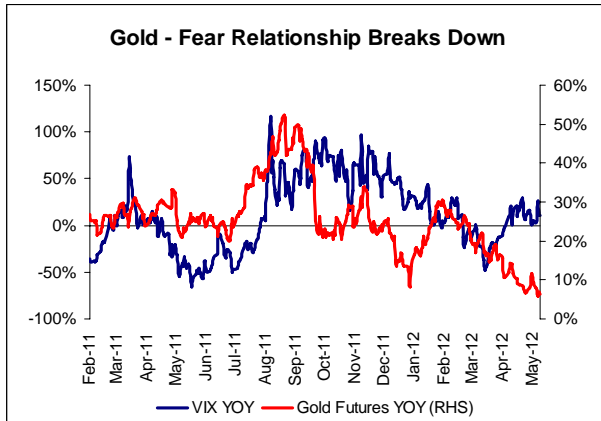
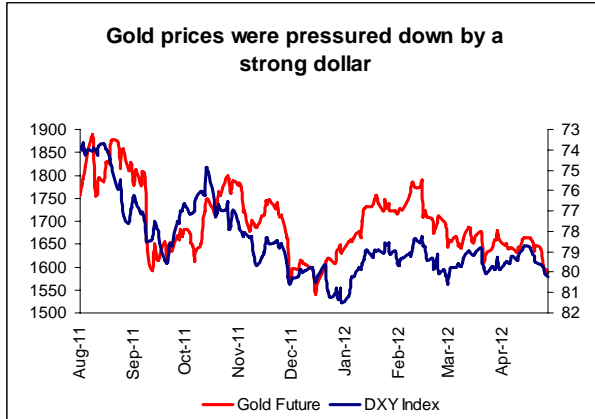
Source: Bloomberg, OCBC BANK

Despite the fall in gold prices below its psychological important level of \$1,600/oz, we remain constructive on gold demand and gold prices. However in the short-term, we may see further downside in gold prices due to sustained risk-off sentiments due to renewed Eurozone concerns, with immediate strong support at \$1,522/oz. We then expect a quick recovery above its 200-day moving average in 3Q12 and look for gold to close above \$1,800/oz at end-year.

Appendix

OCBC Gold Forecast

\$/oz	2Q12	3Q12	4Q12
Gold	\$1,650	\$1,740	\$1,830



Source: Bloomberg, OCBC BANK

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