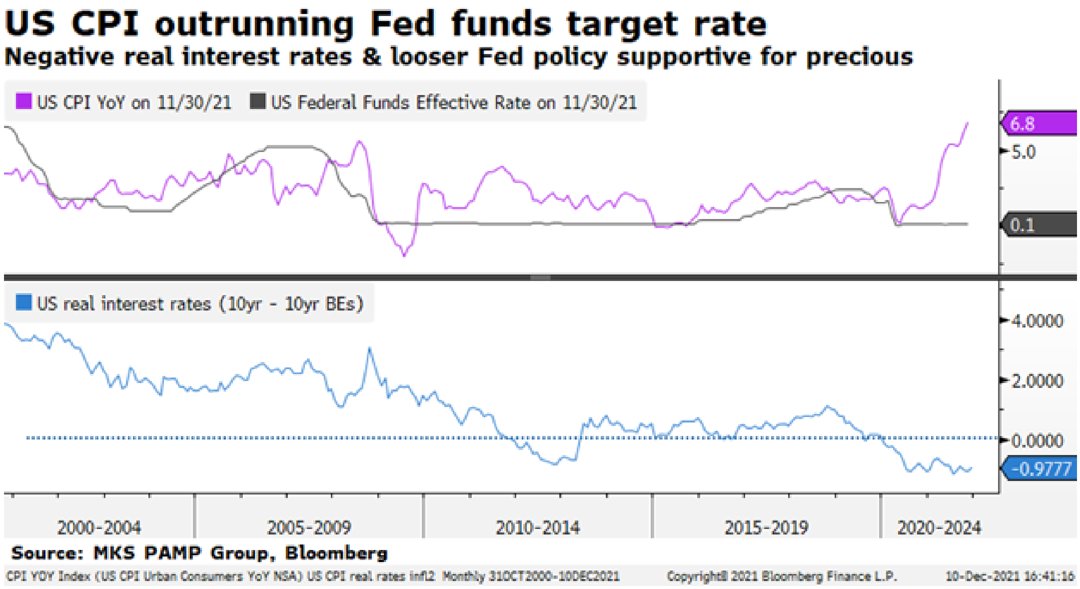
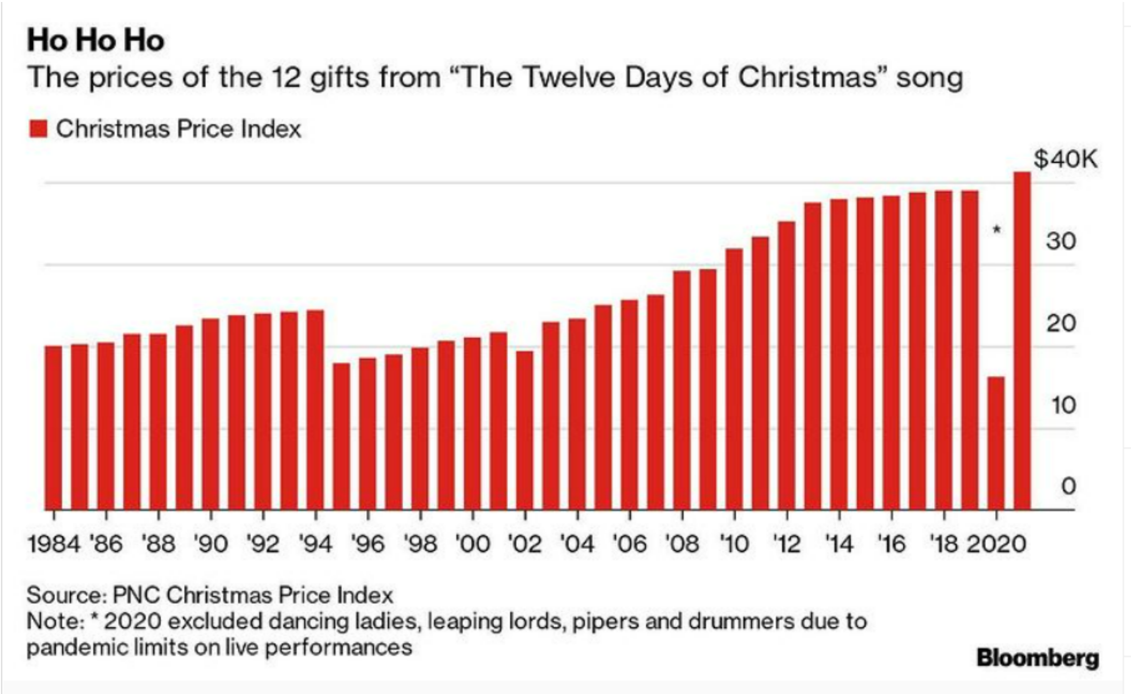
CPI & Gold





Part 2: The numbers came pretty much spot on versus expectations. CPI YoY at 6.8% with core CPI YOY at 4.9%. The kneejerk reaction in 10yr yields (down though 1.5%) and gold up ~$10+ signals that those levels were already baked in and prepositioned for (on the shortside, *the irony* – but see note below). So on a short-term basis, there isn't anything in todays report for gold bears to sink their teeth into. **The bigger issue is that todays US number is its highest in 40yrs, core CPI (ex energy) is very strong near 5%, and real average hourly earnings are negative (so wages are not keeping pace with inflation metrics which becomes a sticky political issue).**

In addition, a few other CPI prints this week put in some significant headlines; Germanys inflation rose at its fastest almost 30yrs, Mexicos inflation hit 21yr high, Brazils CPI at its highest in 18years, Czech/Norway inflation hit a 13yr high. Ha, even Japan (!) saw PPI inflation at its highest since 1980 (which is squeezing firms as, for now, they have not passed on costs to consumers).

Gold rose post print toward $1800 , which was a mix of **1) short-term short paper positioning exiting (expecting a stronger number and a much hawkish Fed); that thinking is also evident in US equity futures rallying strongly into the US equity open 2) the view outlined below that it's a goldilocks**

print VS expectations (not on an historical basis) for bulls; just enough inflation for Gold to play its part as a hedge, while not enough to *accelerate* a Fed taper significantly. Leveraged investors may remain sidelined into yearend (due to uncertainty around FOMC and the Feds outlook) but the headline fear this 40yr print will induce, should aggressively ramp up a mix of retail coin/bar precious demand.

Overall, “transitory” has been one of the worst (inflation) calls by the Fed and both knocks the Feds credibility AND raises the risk of a major policy mistake; the latter would be enormously harmful to peoples livelihood. **When the Fed acknowledges we have an inflation problem, its then more likely a greenlight for Gold, than simply dismissing it…**

Looking forward, the Northern Hemisphere winter (read energy concerns, Omicron/variant overhang, Asias Zero-Covid policy) will ensure these inflation stats remains lofty for a couple few months, as supply chains continue to be pressure tested. However, inflation should start to become “transitory” fall, simply by virtue of base effects toward the middle of next year; that doesn’t mean theres no inflation, it just implies prices have risen and remain high…. *(sigh)*

1. Graph 1 shows the gap between Fed Funds rate and CPI, which is eye catching; it would’ve been hugely bullish Gold historically, but currently, US equities is the preferred play for easier US monetary policy. And while there is just no sustained macro fear (US equities dips aggressively bought, VIX tops short-lived), the equity backdrop becomes much trickier next year into a Fed taper/transition period. With more equity market volatility, and with new variants (this is an endemic, not a pandemic - read persistent stagflation), gold should win over flows.
2. Graph 2 is a a light-hearted take on the BLS CPI; its the Annual PNC Christmas Price Index which measures the average change in prices consumers pay for procuring True Love's “12 perfect gifts” at Christmas.

Part 1:
Gold is currently on track for its worst weekly run since 2009 (*credit to Bloomberg reporting*) before todays all important CPI data. Some would argue, what does gold know…. *(i.e: its going to be a big CPI beat which will further accelerate the growing hawkish narrative).* The news cycle around the vaccine remains rather mixed for gold; theres the view that its over 4x more transmissible than delta & countries are imposing further curbs (eg: UK, HK), vs continued evidence from S.A that despite case jumps, hospitalizations remain manageable.

We’ve argued, its mostly all about the Fed cycle & inflation, and this new variant has NOT given Powell reason to pause/lean dovish. That’s translated into a massive pricing of rate hike expectations; already over the next 18 months, the market expects 4x rate hikes (and one can never rule out a surprise 50bp knock). Graph 1 highlights this together with the move in real 10year rates (Gold favorite influencer).

Expectations are for a 6.8% YoY increase (core 4.9% YoY) which is already much higher than last months 6.2% print. **However, the whisper no. and thus market positioning is arguable even higher** as October-November were months of broader inflationary pressures (higher energy prices, escalating supply-chain bottlenecks, higher rents, etc). Thats somewhat visible in gold positioning (200K oz was added to Agg Oi over the past 2days on price pressures suggesting fresh shorts, not long liquidation). **A much higher print ramps up political pressure on the Fed to end tapering sooner, and provides impetus for hawkish paper shorts to press gold into another event risk (FOMC next week) and yearend.** The structural bullish point that the Fed/Powell will face political pressure, is NOT playing out in Gold; very few structural drivers are relevant right now. Besides, Powell has shown he can stand up to criticism (to Trump!) very well, so certainly can face backlash from the Dems, while trying to uphold a reputation (he cant go down as the Fed Chair who did nothing in the face of persistent inflation) *But I digress…* So, **a goldilocks print - not too hot, but not too cool - VS expectations (so say 6-7%), is likely the best bullish backdrop for any Gold bulls to participate on dips; its just enough inflation for Gold to play its part as a hedge (especially now that crypto is seemingly at dangerous technical levels after the recent washout), while not enough to accelerate a Fed taper.**

Graph 2 highlights Golds past kneejerk/daily reactions to the monthly CPI print, since inflation starting its rear is head (May 2021). Theres been 7 CPI prints over 4%, and the number has decently beat expectations 5 out of these 7 times (Nov print of 6.2% vs 5.9%exp, Oct, July, June & May prints). Takeaways:

- ON average, Gold is up ~0.5% 6 hours on after these past 7 PCI prints. i.e.: there seems to be a lot of preemptive shorts/positioning that unwinds on the fact (CPI release).
- The kneekjerk reaction within 1hr after the most recent prints (Nov + Oct which saw decent beats off higher bases) was wrong and should be faded.
- The Sept & Aug prints which were pretty much on point, saw gold trade mildy positive/bid into the close
- Gold prices currently ($1770) are heading into this CPI at its 2nd cheapest level (the August 11th CPI print for July was when Gold was its cheapest at $1730). 5/7 of the last CPI prints occurred when Gold was >$1800.
- After putting in massive technical failures recently (trendline resistance nicely broken across both futures & OTC), Golds now revisiting trend support (extending back to 2019) at a key moment/event risk. Graph 3.

Sooo… despite gold putting in its 4th week of declines and risk/reward not really in in its favor being short (eg: -$20/+$50 to $1750/$1820), I'm super respectful of 1) technicals *(what can't go up must go down)*, 2) lack of liquidity around event risk (CPI, FOMC), yearend and reduced physical demand (allowing paper shorts to push…), 3) growing hawkish Fed narrative, IF CPI 'allows' for that. It's a tactical view…. Stagflation (a core longer-term bull view) has yet to be fast tracked into asset classes at the moment