Daily European Wrap

GOLD: SUMMARY TABLE

	Tailwinds	Neutral	Headwinds	
	Overcrowded Inflation trade is merely a correction - it is NOT transitory. Real rates have aggressively shifted more negative providing a cornerstone foundation for precious. The Fed will wrongfoot the exit, and will need to do a lot more than talk (with 2x CPI >5%) to derail this inflation trade. Wage growth, bottlenecks that aren't alleviating, commodity inflation and businesses talking & passing on costs all point to not transitory inflation	**Limited macro fear/equity volatility** (VIX >20) is short-lived and doesn't upend the super complacent risk regime given aggregate amount of liquidity/cash in the system; gold is simply an equity inflation hedge that gets pulled up	Decreasing risk of **correlated dovish global Central Bank action** as growth & inflation surge. The Fed has provided a hawkish greenlight and some G-10 CBs have begun to taper.	
------> MORE BULLISH	**Aggregate positioning remains relatively underweight:** Net length COT at 7.8m oz (below 5yr average of ~11m oz), creating 2.5 longs per every short (5yr average is 3 longs/short). Very slow/stable outflows in ETFS (they still hold ~100mn oz). COT shorts are underweight (a risk they ramp up), but the larger generalist (FI, Equity) and macro investor remains underweight or unengaged. Overall, arguably underweight given relative overweighted ownership in other assets including other commodities	**Trading risk reward** in the near-term is neutral, after being net bearish (-$200/+$50 post FOMC) to being rather neutral (-$70 to $1750/new support, vs +$80 to $1900/recent peak)	**The poor performance of inflation hedges (Gold, Bitcoin)** is both perplexing and frustrating for potential longs, who're sticking to owning stocks a better inflation hedges. Relative to other high beta assets, Gold performs but doesn't outperform in sustainably low interest rate/low volatility environment. Stale longs quick to exit for better opportunities, providing an opportunity for fast money (COT) shorts to really reengage on Fed taper	------> MORE BEARISH
	Higher pace of Central Bank gold buying, diversifying against fiat/US$ and aggregate warlike era fiscal & monetary responses globally. Rather new entrants (Brazil), and larger purchases (Thailand) v constructive	**Return of physical support is shortlived;** given prices are $50 more expensive vs 2H June. China/London arb is ranging $0-$2 and rather flat/neutral as opposed to relatively stronger demand in June (as implied by imports). Indian and SE Asia is reemerging and only avid participants sub $1800/oz.	**Technically broken and still in no-man's-land** with perceived peak stimulus/inflation top in and a lot of ground to be regained. However, there will likely be more buyers >$1900 than $1800.	
<------ LESS BULLISH	**The Commodities thesis** (vs equities & bonds) is gaining traction given structural underperformance. **Portfolio asset allocation** potentially reconsidered given dramatic shift lower in yields offering little-no diversification benefits. Bitcoin is less of a viable/stable fiat currency, or equity inflation hedge & thus less of a detractor of Gold flows.	**Fed pivot** from behind to potentially ahead of the inflation curve. Cautious monitoring into Jackson Hole but the market it not as fearful as it was in 2013 and a repeat of largescale gold flush is very unlikely.	Large **dishoarding** from traditional physical Gold countries given price surge; **Gold Producers** well ITM across most metrics and can easily capitalize on rallies	<------ LESS BEARISH
	Catchup/rebound in European growth driving **EUR upside and rotation into European assets** is gaining traction as US-European reopening gap narrows & Fed reduces liquidity. Delta variant currently poses a threat to this thesis.	**US$.** Outlook on whether the $ continues into structural weakness or whether there's another squeeze up, is mixed. Given its reserve currency status & historical resilience into typical 'macro wobbles' (as Fed change in language will ramp up volatility), its still cheap. Technically contained.		
	Fiat currencies may be re-politicized in a **currency war as last of monetary policy tools redeployed**. The independence of CBs increasingly under threat from governments; skepticism growing around power of CBs to remove volatility & pump up asset prices amidst renewed risks	**Trade, Geopolitics, Politics**: no geopolitical bid given the lack of bullish/unpredictable headlines post Trump; the frequency of "off-calendar" geopolitical events/risks (Iran/Middle East/North Korea) is decreasing or a nonevent for assets. Multilateralism is clawing back		
	Unsustainable US **debt/fiscal** path (and globally!) with swelling twin deficits. A structural theme, but one which has taken a backseat to the Feds recent actions.			

Source: MKS PAMP Group

Given last weeks yield implosion, another hot CPI print, and the improvement in Golds risk-reward profile post hawkish FOMC (pretty bearish) to not now (leaning bullish), its worthwhile to revisit and update the bull/bear table (vs 3 weeks ago), with our thoughts and highlighting the main changes made (in purple).

The table is attached above or available here Gold Bull Bear Table

Changes:

- **Overcrowded Inflation trade is merely a correction - it is NOT transitory: Tailwind getting stronger.** Real rates have aggressively shifted more negative providing a cornerstone foundation for precious. The Fed will wrongfoot the exit, and will need to do a lot more than talk (with 2x CPI >5%) to derail this committed inflation trade.
- **Higher pace of Central Bank gold buying, also a stronger tailwind**: Rather new entrants (Brazil), and larger purchases (Thailand) v constructive
- **Physical demand/support downgraded from "tailwind" to "neutral"** given prices are $50 more expensive vs 2H June. China/London arb is ranging $0-$2 and rather flat/neutral as opposed to relatively stronger demand in June (as implied by imports). Indian and SE Asia is reemerging and only avid participants sub $1800/oz.
- **Fed pivot (hawkish stance) downgraded from "headwind" to "neutral":** the market is simply much less fearful than the post FOMC 2021, and especially vs 2013. Yield curve and price action implies there is no taper tantrum (quite the opposite), and there was no impending washout in gold and squeeze in USD.
- **Trading risk-reward in Gold has flipped** from being net bearish (-$200/+$50 post FOMC) to being currently neutral (-$70 to $1750/new support, vs +$80 to $1900/recent peak)
- **Aggregate positioning remains relatively underweight** vs equities & other commodities: Net COT underweight, ETF neutral and small outflows (albeit overweight). COT shorts are underweight (a risk they ramp up), but the larger generalist (FI, Equity) and macro investor remains underweight or unengaged.

New additions:

- **Headwind: The poor performance of inflation hedges (Gold, Bitcoin)** is both perplexing and frustrating for potential longs, who're sticking to owning stocks as better performing inflation hedges.

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