Macro | FX Research and Strategy

Global

FX Flash

XAU: Near Term Consolidation; Prefer to Buy Dips

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Constructive on Gold Outlook Overall; Watch Yield for Warning

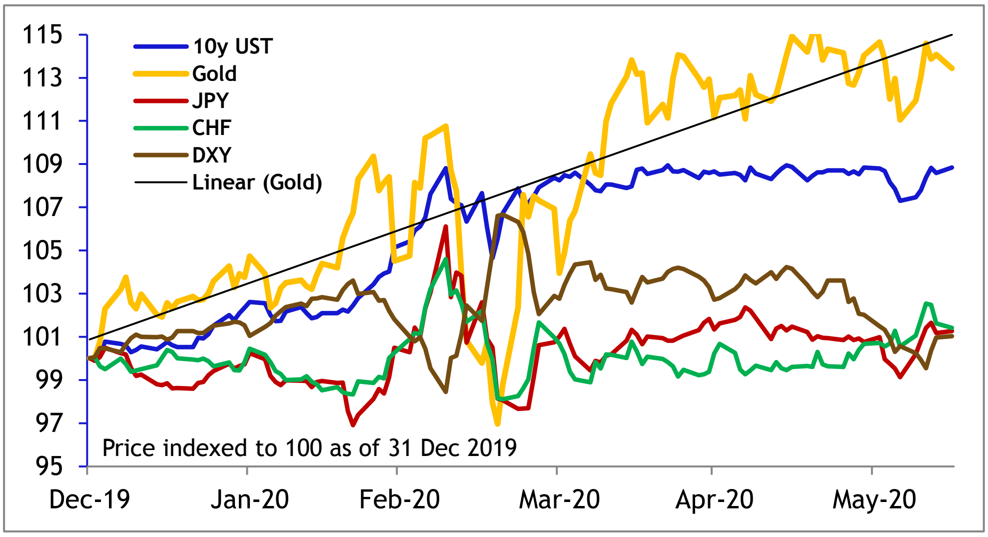
Gold has seen a massive run-up of >20% from its Mar lows and could potentially enter into a state of consolidation, from a price momentum and positioning point of view. We do not rule out near term decline towards 1691, 1675 levels if key support at 1713 is taken out. Bias remains to buy on dips.

Global growth is at risk of another downgrade *at the IMF* as there is a lot of concern about the path and shape of recovery given the possibility of a further decline in consumption, more job losses and risk of fresh wave of bankruptcies. *We* believe the sentiment could still remain cautious as economic reality sets in over the coming weeks and months and that central bank accommodation, low rates are likely to stay intact for longer. *This should continue to erode US rate advantage. Furthermore renewed fears of second wave covid infection, potential escalation of geopolitical tensions in Korean peninsula and sino-US tensions to some extent could still keep safe haven assets including gold somewhat supported.*

However if macro conditions turn out to better than feared, markets will start buying the growth story again, risk assets will continue to rally and cyclical-proxy FX will be beneficiaries, at the expense of a weaker USD (counter-cyclical factor). At this point, ***USD-Gold negative correlation could reassert, benefiting gold as USD eases***.

In light of the above, we remain constructive on the outlook of gold and favour buying dips. The biggest risk to our conviction is the rise in yields (when it happens).

Gold: An Outperformer amongst Safe Haven Peers



Source: Bloomberg, Maybank FX Research & Strategy

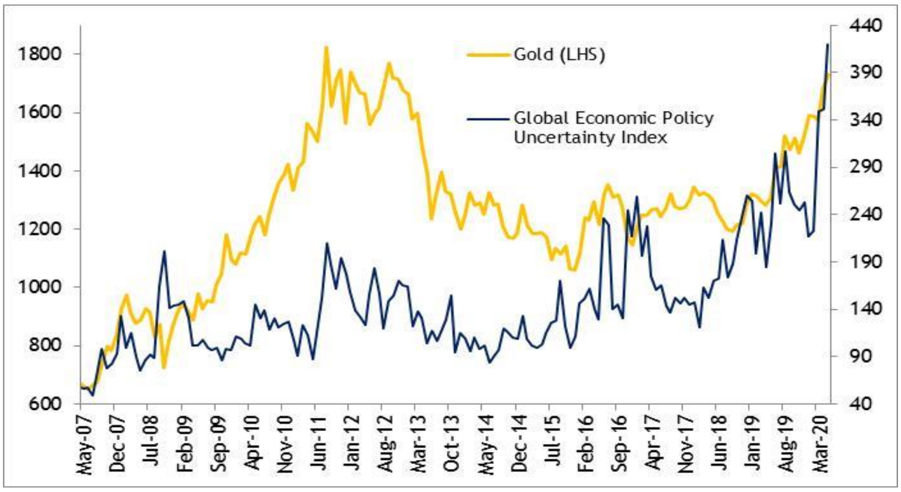
Grim Economic Prospects Enhance Gold's Appeal

Gold has continued to trade higher this year, outperforming most traditional safe haven assets, including USTs, JPY and CHF. COVID-19 pandemic and its ensuing global economic lockdowns, border restrictions and social distancing measures have been cited as the main fear factor for fuelling demand for safe-haven assets, including gold. Back in Apr-2020, the IMF even made one of its most bearish economic assessment - projecting global growth to be -3% for 2020, a 6.3ppts downward adjustment from Jan-2020 forecast making the great lockdown the worst recession since the Great Depression and far worse than the Global Financial Crisis.

And just 3 days ago, the IMF said it may again downgrade its pessimistic outlook for the global economy. At the 7th Asian Monetary policy forum (12 Jun), IMF Chief Economist Gopinath said there is a lot of concern about the path and shape of recovery given the possibility of a further decline in consumption, more job losses and risk of fresh wave of bankruptcies.

Despite the gradual re-opening of many economies, we believe the sentiment could still remain fragile as economic reality sets in over the coming weeks and months. Border restrictions and social distancing measures remain in place for now, and that means travel and consumer spending would still be curbed. Job losses remain one of the biggest worries. On a global scale, the International Labour Organisation (ILO) projected job losses of up to 305mn globally (up from earlier estimates of 195mn due to prolongation and extension of lockdown measures). Fed Chair Powell also weighed in, saying there is great uncertainty about the future given unknowns about the coronavirus and whether people will feel comfortable resuming their previous day-to-day activities absent a vaccine. He added that "my assumption is that there will be a significant chunk, well into the millions who don't get to go back to their old job, and, in fact, there may not be a job in the industry for them for some time".

Continued Rise in Uncertainty to Keep Gold Prices Supported



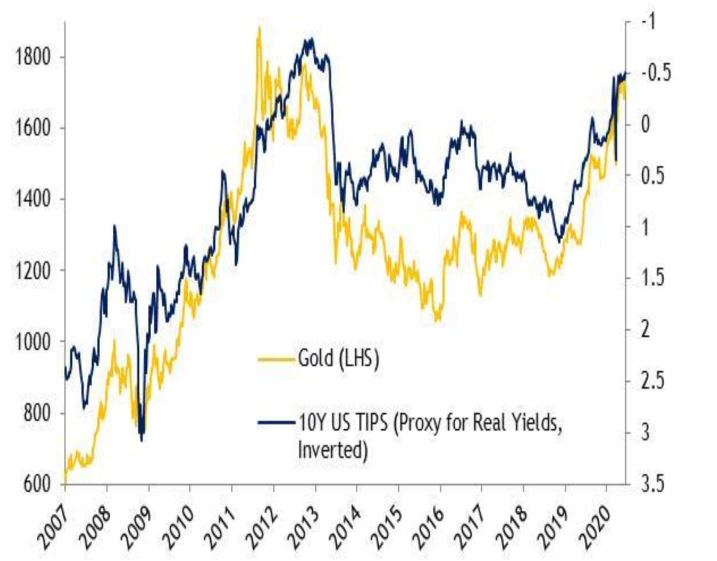
Note: Economic Policy Uncertainty index constructed from 3 types of underlying components including (1) newspaper coverage of policy-related economic uncertainty; (2) number of federal tax code provisions set to expire in future years; (3) disagreement among economic forecasters as a proxy for uncertainty
Source: Baker, Bloom & Davis, Bloomberg, Maybank FX Research & Strategy

Eroding US Rate Advantage and Policy Accommodation to Support Gold

The rise in gold is also consistent with the decline in both nominal and real yields (adjusted for inflation). Central banks around the world including ECB, Fed have pledged to keep monetary policy accommodative, including rates at record low for longer as well as the use of unconventional policy tools including expanding balance sheet to support growth. It is not likely this policy stance will change anytime soon given that economic growth outlook remains bleak. As such gold can still expect to stay supported, especially in an environment of emerging risk factors.

Eroding Nominal Rate Advantage Supports Gold Prices

Depressed Real Yields for Longer Suggest Gold Prices Can Maintain Altitude



Source: Bloomberg, Maybank FX Research & Strategy

Emergence of Risk Factors Reinforce Support for Gold Prices

1. **Renewed fears of second wave covid infection.** Globally, several states in US, Beijing, Seoul have reported sharp spikes in newly infected cases. In particular, Beijing reported a fresh cluster and shut down its largest fruit and vegetable supply market early last Sat that was linked to it, along with the lockdown of nearby residential area. The virus was detected amongst business owners and their equipment (including a chopping board used by a seller of imported salmon, according to Global Times). 45 people tested positive and were asymptomatic.

2. **Geopolitical tensions in Korea peninsula not to be under-estimated.** Over the weekend, North Korean leader's sister Kim Jo Yong said that it is "high time" to break relations with South Korea and warned that the next move in retaliation for S.Korea's failure to stop activists sending anti-regime leaflets into its territory will be entrusted to the military. Pyongyang said its military is considering re-entering DMZ. South Korean authorities conveyed an emergency meeting in response and had issued a statement saying it was assessing the current situation "sternly". Further escalation (though not our base case for now but a risk

to watch) in geopolitical tensions in the peninsula could catch markets off-guard, weigh on sentiment and re-fuel demand for safe haven assets, including gold.

3. **Sino-US tensions at Risk of Escalation.** This may be a lesser risk for now as tensions this episode (in May) relates more to sanctions instead of trade and have since receded. But we do not rule out the risk of escalation especially going into 2H as US Presidential Elections come near and Trump could ramp up its China bashing rhetoric to shore up its approval ratings. Recall that back in 2018-19 when US-China trade war flared up, threatening global growth and sentiment, gold had rose then.

Historical Negative Gold-USD Correlation Should reassert itself and Benefit Gold as USD Eases Further

Some of the commonly cited relationships between Gold & other FX include:

- Negative correlation with USD (DXY): Gold is priced in USD, and a softer USD increases demand for "cheaper" Gold.
- Positive correlation with THB: Thailand is a regional gold trading hub. Sales of gold tend to rise when gold prices are on the rise, and this supports the THB when proceeds are exchanged back to THB.

We take a closer look at how these relationships are shifting.

52-Week Rolling Correlation of Returns in Gold vs USD, THB

Source: Bloomberg, Maybank FX Research & Strategy

Gold & THB: Positive Correlation Slowly Dissipating

52-week moving correlation between returns in Gold and THB changes has been positive but declining over time. Part of the structural decline could be due to actions by the central bank. In Thailand, the central bank is increasingly trying to avoid a scenario whereby "gold gains =>

THB gains". Last year, it allowed Thai investors to trade gold in foreign currencies, and to keep FX proceeds from gold investment in their accounts, without having to exchange back to THB. Recently, BoT also identified gold trading as an undesired channel of THB appreciation and commented that it will scrutinize such activities. On net, THB may increasingly receive less support in an environment of Gold appreciation.

Gold & USD: Negative Correlation in Returns Intact

52-week moving correlation between returns in Gold and USD (red line) has remained persistently negative in recent years. We note that the Fed is unabashedly pumping dollars into financial markets via its asset purchase programmes and this could continue for some time—emerging consensus is that Covid-led drags on the US labour market could take years to dissipate. Concerns over ballooning Fed balance sheet and widening US fiscal deficit could lead to a softening bias in the dollar while intensifying the appeal of "real" assets, including gold. **Appeal of gold could remain intact for some time.**

We highlight there are 2 aspects of the USD - (1) an "international" role due to US being the world's reserve and payment currency (for a lack of better alternative) and (2) as a proxy of its domestic factors. If risk of second wave covid infection turns into a global risk phenomenon. Then USD broad weakness, USD-gold negative correlation story will have to be put on hold as doubts over economies reopening will come to the fore again. USD, JPY, CHF and EUR (to some extent) and **gold will be better bid on risk aversion.**

But if covid second wave concerns turns out only to be a scare, then markets will start buying the growth story again, risk assets will continue to rally on and cyclical-proxy FX will be beneficiaries, at the expense of a weaker USD (counter-cyclical factor). At this point, **USD-Gold negative correlation could reassert, benefiting gold as USD eases.**

- USD (domestic) weakness bias owing to US still covid epicentre and risk of second wave infection, slump in US data, eroding rate advantage, massive and increasing Fed's balance sheet amid QE, deteriorating twin deficits, chatters of reserve diversification or reallocation away from USD and potential political risks in the lead up to US Presidential elections in Nov 2020.

Gold Shines in Crisis and Maintains Allure in Recovery

Given the high extent of uncertainty in markets now, we also turn to the behaviour of Gold in past "crises", defined as periods of sharp fall in S&P 500 Index.

	Crisis Phase (% Chg, Pre-crisis vs. Trough)			Recovery Phase (% Chg, 6 Mths from Trough)		
Event	**S&P 500**	**Gold**	**USD (DXY)**	**S&P 500**	**Gold**	**USD (DXY)**
2002 Crisis - Last Phase of IT Bubble	-33.6	9.2	-9.1	11.5	2.1	-6.3
2007-09 Financial Crisis	-56.5	23.3	14.0	50.2	7.9	-12.4
2011 US Debt Ceiling Woes	-16.4	1.4	7.3	25.8	1.4	-0.1
2015-16 Chinese Equity Turbulence	-14.2	3.5	0.3	19.5	7.4	0.3
2018 Global Growth Concerns	-19.7	5.7	2.5	24.1	12.2	-0.5

Source: Bloomberg, Maybank FX Research & Strategy

There are two characteristics of Gold that we like here.

(i) Gold has been a steady haven asset in uncertain times. Over crisis periods, returns have always been positive, even as it has varied across episodes.

(ii) Even in the recovery phase (defined as 6 months post equity troughs), Gold has always managed to retain/improve on gains. This is important as it is hard to identify market troughs definitively till after the event. Ideally, price action should not reverse too quickly (for haven assets) in recovery periods.

Gold Performance in various FX (in % terms)

	USD	EUR	GBP	JPY	AUD	NZD	CAD	CHF	SGD	MYR	IDR	THB	PHP	KRW	CNY	HKD	Average
2001	2.5%	8.6%	5.2%	17.9%	12.4%	9.2%	8.9%	5.6%	9.0%	2.5%	10.1%	4.4%	5.7%	6.4%	2.4%	2.4%	7.1%
2002	24.8%	5.8%	12.7%	12.6%	13.2%	-0.9%	23.1%	4.0%	17.3%	24.7%	7.4%	21.7%	29.6%	12.6%	24.8%	24.8%	16.1%
2003	19.4%	-0.6%	7.6%	7.7%	-10.9%	-4.5%	-1.5%	6.9%	17.0%	19.4%	12.3%	9.7%	23.7%	20.0%	19.4%	18.8%	10.3%
2004	5.5%	-1.9%	-1.7%	1.0%	1.7%	-1.7%	-2.2%	-1.9%	1.3%	5.5%	16.2%	3.7%	6.8%	-8.4%	5.5%	5.7%	2.0%
2005	17.9%	35.0%	31.4%	35.4%	25.4%	24.2%	14.1%	36.0%	20.3%	17.3%	25.0%	24.2%	11.3%	15.1%	15.0%	17.8%	22.9%
2006	23.2%	10.4%	8.2%	24.3%	14.5%	19.3%	23.4%	14.2%	13.7%	15.0%	12.7%	6.5%	13.7%	13.4%	19.1%	23.4%	15.9%
2007	30.9%	18.5%	29.2%	23.0%	18.1%	20.3%	12.2%	21.8%	22.6%	22.8%	36.9%	10.1%	10.2%	31.8%	22.5%	31.3%	22.6%
2008	5.8%	10.4%	43.9%	-14.1%	31.7%	39.9%	29.1%	-0.3%	5.0%	10.4%	27.4%	23.1%	21.6%	42.3%	-1.1%	5.1%	17.5%
2009	24.4%	21.4%	12.2%	27.5%	-2.6%	-0.3%	7.5%	20.5%	22.2%	24.0%	3.9%	19.8%	21.0%	14.5%	24.4%	24.4%	16.5%
2010	29.6%	38.6%	34.1%	13.0%	13.5%	20.0%	22.7%	17.0%	18.3%	15.2%	23.3%	16.5%	22.5%	25.4%	25.0%	29.9%	22.8%
2011	10.1%	13.7%	10.6%	4.3%	10.3%	10.5%	12.7%	10.5%	11.2%	14.0%	11.0%	15.7%	10.8%	13.8%	5.3%	10.0%	10.9%
2012	7.1%	5.2%	2.4%	20.8%	5.2%	0.5%	4.0%	4.4%	0.9%	3.4%	13.7%	3.7%	0.2%	-1.9%	5.9%	6.8%	5.1%
2013	-28.3%	-31.0%	-29.5%	-12.9%	-16.4%	-27.7%	-23.2%	-30.0%	-25.6%	-22.8%	-7.9%	-23.1%	-21.3%	-27.9%	-30.1%	-28.1%	-24.1%
2014	-1.4%	11.8%	4.5%	12.0%	7.6%	3.9%	7.8%	9.7%	3.1%	4.9%	-0.9%	-1.1%	-2.2%	0.8%	0.7%	-1.6%	3.7%
2015	-10.4%	-0.2%	-5.3%	-10.0%	0.4%	2.3%	6.7%	-9.7%	-4.1%	9.7%	-0.2%	-1.8%	-6.1%	-3.7%	-6.2%	-10.5%	-3.1%
2016	8.1%	11.8%	29.1%	5.2%	9.5%	6.6%	5.0%	9.9%	10.8%	13.5%	5.7%	7.9%	15.0%	11.5%	16.7%	8.2%	10.9%
2017	13.5%	-0.7%	4.1%	9.8%	4.7%	11.2%	6.6%	8.6%	4.4%	2.4%	13.9%	2.8%	13.8%	-0.1%	5.5%	14.8%	7.2%
2018	-1.6%	3.1%	3.8%	-4.6%	9.0%	3.7%	6.4%	-0.8%	0.3%	0.2%	4.4%	-2.2%	3.2%	2.8%	3.8%	-1.7%	1.9%
2019	18.3%	21.0%	13.9%	17.2%	18.9%	18.0%	12.7%	16.5%	16.8%	17.1%	13.6%	8.9%	14.4%	22.7%	20.5%	17.7%	16.8%
YTD 2020	14.6%	15.4%	21.7%	13.5%	18.4%	22.7%	19.8%	13.9%	19.9%	20.9%	20.3%	22.0%	14.0%	21.4%	16.8%	14.0%	18.1%
Average	10.7%	9.8%	11.9%	10.2%	9.2%	8.8%	9.8%	7.8%	9.2%	11.0%	12.4%	8.6%	10.4%	10.6%	9.8%	10.7%	10.1%

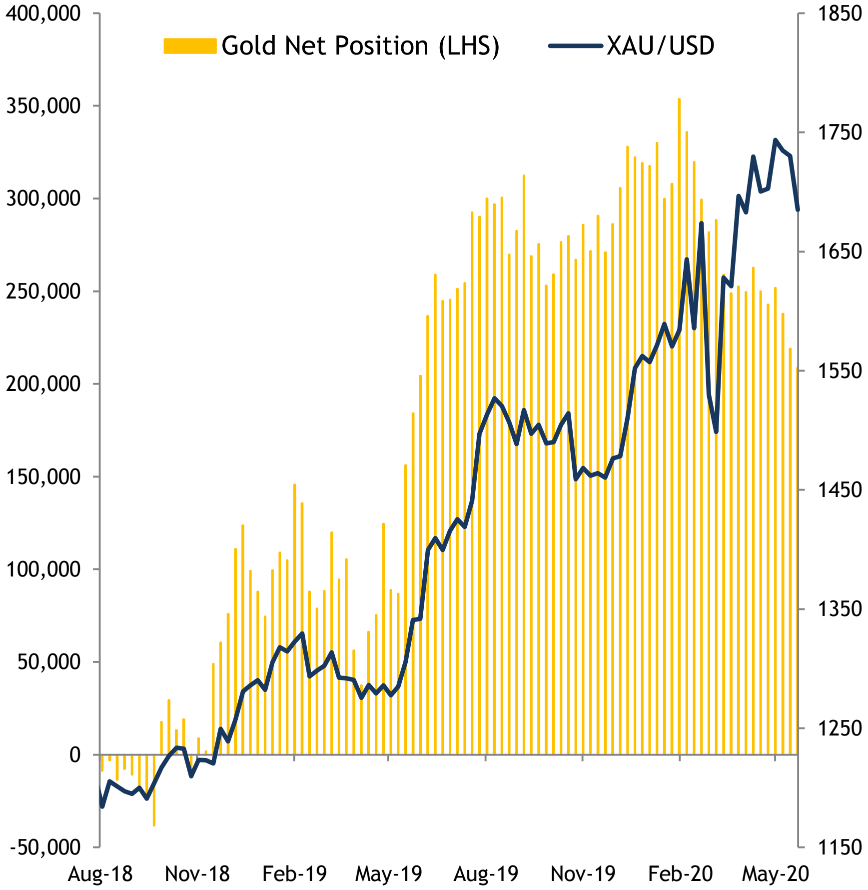
Note: YTD 2020 as of 1 Jun 2020
Source: Bloomberg, Maybank FX Research & Strategy

Apart from measuring gold prices and performance in USD terms (the standard market convention), we dwell further into gold performance against other FX majors and AXJ FX, since 2001 on calendar basis. For instance XAUSGD cross is up 19.9% when measured between 31 Dec 2019 close and 1 Jun 2020 close (refers to gold strengthened 19.9% in SGD terms).

A look across the past 20 years or so show that Gold outperformed most currencies (on average terms). The average annual performance for gold against most currencies from 2001 to (YTD) 2020 is 10.1%. Except for specific periods in 2013 when gold lost by an average of ~24% and in 2015, where gold fell slightly on average by ~3%. We attribute the declines in gold prices to episodes of rising treasury yield - which forms our biggest risk to our constructive outlook on gold prices.

Gold Positioning: Overcrowded Longs Pose Risk of Long Squeeze

According to the latest Commitment of Traders (COT) data released by Commodity Futures Trading Commission (CFTC) last Fri, the non-commercial gold futures contract (proxy for speculative positioning and large hedge funds), showed a weekly decline of 10,421 contracts to a net position of 208,613 contracts, nearing its 1-year low. Further trimming of stale long gold positions could accelerate the easing of gold prices in the interim.



Source: CFTC Positioning, Maybank FX Research & Strategy

XAUUSD: Losing Momentum in the Interim; Enters Into State of Consolidation; Buy Dips Preferred

XAU has seen a sharp run-up of >20% since Mar low to a high of 1765 (18 May). Since then, XAU has drifted lower. Last seen at 1730 levels. Bearish divergence on RSI (weekly chart) is potentially emerging while on the daily chart, momentum and RSI are not indicating a clear bias for now. Immediate support at 1713 (50 DMA) before 1691 (23.6% fibo retracement of Mar low to May high). A stretch towards 1675 (lower bound of the horizontal trading band, 1645/50 levels (38.2% fibo, 100 DMA) should not be ruled out. We expect XAU to consolidate in the interim and trade a range of 1675 – 1755 till it breaks. Constructive bias intact. Resistance at 1755 (upper bound of horizontal band) before 1765. Decisive break above 1765 could open room for move into 1900 territories.

XAU (Daily): State of Consolidation; Watch the Band

Source: Bloomberg, Maybank FX Research & Strategy

XAU (Weekly): Potential Bearish Divergence on RSI

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