XAU/USD Report

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Trading and Research

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Basic Information

Current XAUUSD Price	$2049.18
Previous Close	$2028.71
Min. Day's Range	$2028.71
Max. Day's Range	$2062.28
1-Year Change	8.03%

Chart info

Figure 1:U.S. Inflation Rate(2023)

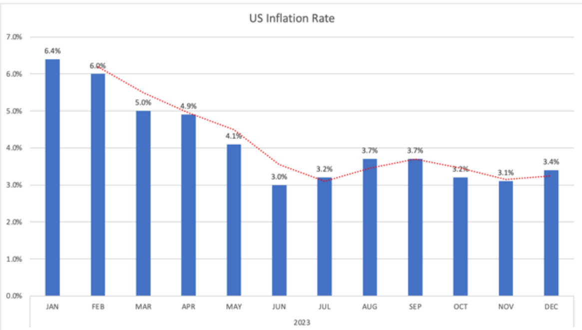
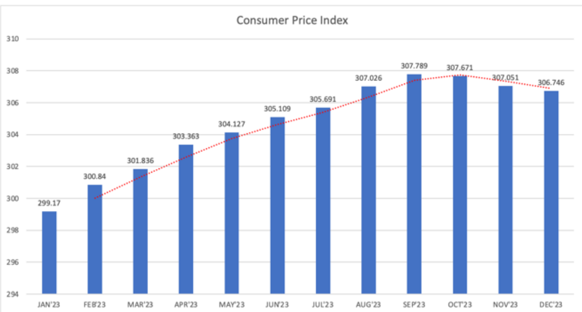


Figure 2: Consumer Price Index(CPI)



Executive Summary

In 2024, gold becomes a major focus amid economic uncertainties and geopolitical complexities. The allure of gold, deeply rooted in its historical role as a safe-haven asset, takes center stage as investors seek stability in the face of heightened market volatility. This positioning as a store of value becomes pivotal in contributing to the upward trajectory of gold prices. Central to the optimistic outlook is the sustained demand for gold from central banks, notably exemplified by the unwavering interest of developing markets. The 2023 Central Bank Gold Reserve Survey signals a positive trend, with a notable 24% of central banks planning to augment their gold reserves in the coming year. This, coupled with a 10-point increase from 2022, reflects a growing confidence in gold's enduring appeal as a strategic reserve asset. Additionally, a significant 71% of surveyed central banks foresee an uptick in global reserves, further solidifying the positive sentiment surrounding gold.

Technical analysis serves as a powerful lens, unveiling a robust uptrend for XAUUSD. The convergence of key indicators, including the MA200 trend line, a Golden Cross Formation, and strategic rejections at crucial Fibonacci levels, fortifies the bullish stance. For traders thinking about buying XAUUSD, the risk-reward ratio is excellent at 1:6.22, making it a compelling opportunity. This ratio, carefully calculated to balance potential returns and associated risks, adds a layer of confidence to the investment strategy. Zooming out to the broader economic canvas, concerns about a potential economic slowdown and recession risk become pivotal factors in bolstering gold's positive sentiment. The metal's established reputation as a hedge against economic downturns aligns with the prevailing cautious market sentiment in 2024.

This strategic outlook rests on the synergy of multiple factors, including the traditional safe-haven appeal of gold, sustained central bank demand, and robust technical indicators supporting a bullish trajectory. The convergence of these three elements, coupled with a vigilant risk management approach, forms the cornerstone of the presented strategic outlook, emphasizing the potential of XAUUSD as a resilient and attractive investment choice for the discerning investor in the financial landscape of 2024.

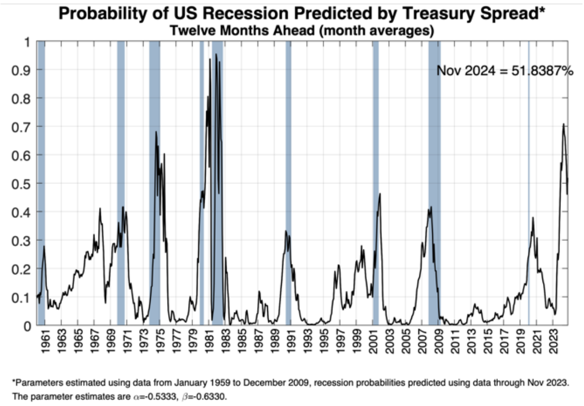
Market Overview

U.S. inflation is seemingly experiencing a downturn(Figure1), but the Consumer Price Index (CPI) (Figure 2), conceals this trend. WisdomTree's alternative inflation metric, substituting real-time housing metrics for shelter inflation, indicates a rate of 1.4%, sharply contrasting with the official 4.1% headline inflation reported by the Bureau of Labor Statistics (BLS).

Core inflation, utilizing real-time metrics, aligns closely with the Federal Reserve's target at 2.1%. In contrast, the BLS reports shelter inflation at 8% over the past 12 months, while our alternative metric suggests a mere 0.5% increase in shelter prices. This singular adjustment could significantly reshape the Fed's inflation narrative, indicating that additional rate hikes may be unnecessary. Despite this alternative perspective, the Federal Reserve's dot plots imply that members(12) of the Federal Open Market Committee (FOMC) anticipate further rate hikes, posing an increased risk of recession.

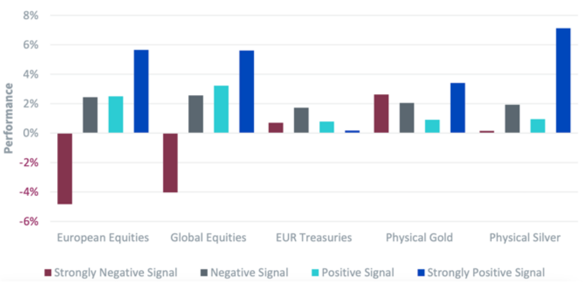
Conversely, central banks in other developed economies show no indications of concluding their respective hiking cycles. The European Central Bank (ECB) maintains a hawkish stance, signalling additional hikes. ECB President Lagarde acknowledges "significant progress" but cautions against declaring victory. Simultaneously, the Bank of England (BoE), responding to persistent upside inflation surprises, has surprised the market with 50 basis point hikes. While Europe's inflation metrics may not mirror the U.S. distortions, the extended and unpredictable nature of monetary policy lags suggests that the swift pace of rate hikes could exert a considerable impact once these lags are considered.

Figure 3: The Federal Reserve Bank of New York's Recession Probability Model



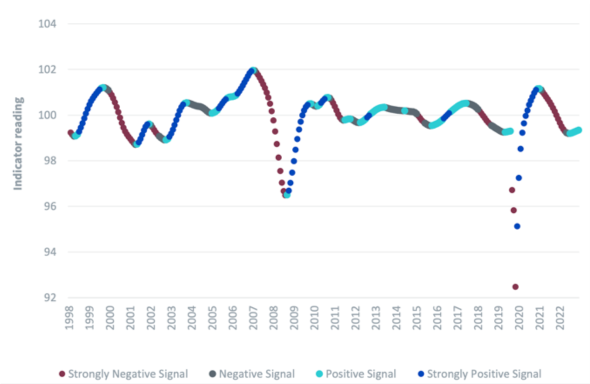
Source: Federal Reserve Bank of New York

Figure 4: Gold Prices in different phases of economic cycle



Source: Wisdom Tree, Bloomberg, Organisation for Economic Cooperation and Development

Figure 5: Composite leading indicator of economic conditions



Source: Wisdom Tree, Bloomberg, Organisation for Economic Cooperation and Development

Recession Risk Rising

Amidst increasing recession risks, investors may consider turning to gold as a defensive asset. One key indicator of recession risk, derived from yield curve inversions, suggests a 52% likelihood of the U.S. economy entering a recession by mid-2024 (Figure 3). The Federal Reserve Bank of New York model, known for its historical accuracy in predicting recessions, presents a compelling warning signal that is challenging to overlook.

Gold as a Defensive Asset

Gold often exhibits strong performance during periods of economic stress. As illustrated in (Figure 4), when composite leading indicators (Figure 5) take a notable negative turn, gold tends to show positive performance, contrasting with the negative trends observed in equities. Furthermore, gold tends to outperform Treasuries, which are traditionally considered competing defensive assets. This pattern underscores gold's role as a valuable hedge during times of economic uncertainty.

Central Bank Gold Demand

Central bank gold demand, having reached a historic peak in 2022, continues to demonstrate robust momentum. In Q1 2023, official sector gold buying achieved a new first-quarter record, although slightly lower than the levels observed in Q3 2022 and Q4 2022, as illustrated in Figure 6. Notably, in April 2023, Turkey's central bank sold 81 tonnes of gold – a seemingly technical move rather than a shift in gold buying policy. The sale aimed to meet strong demand for bars, coins, and jewellery in the domestic market, spurred by a temporary partial ban on gold bullion imports enacted to mitigate the economic impact of the February 2023 earthquake. According to a YouGov poll sponsored by the World Gold Council, central banks in developing markets express an intention to augment their gold reserve holdings while reducing their holdings in US dollars.

Economic Indicators

U.S Non-Farm Payroll(NFP)

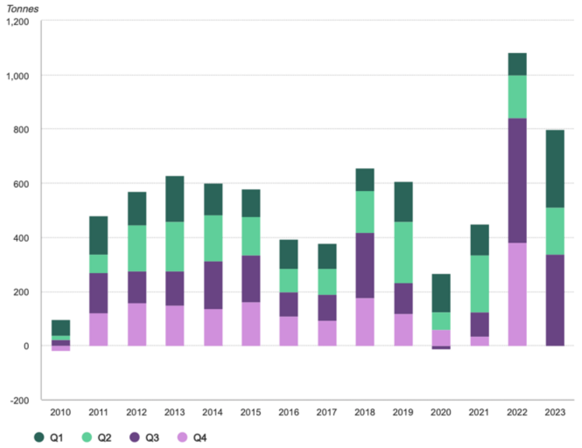
The NFP report(Figure 7), a monthly indicator of the US labor market's health released by the Bureau of Labor Statistics, reflects the net change in US employment, excluding farm, non-profit, and private household workers. Highly influential across the US Dollar, equities, Treasuries, and gold markets, the NFP report stands as a pivotal and market-moving data point.

On 08/12/2023, the US Bureau of Labor Statistics (BLS) revealed that Nonfarm Payrolls (NFP) in the US saw a rise of 199,000 in November, exceeding market expectations of 180,000 and surpassing October's increase of 150,000. This indicates a consistent increase in job creation over the months, suggesting a growing economy.

In market dynamics, the Federal Reserve's rate-hiking phase appears concluded, signalling a potential rate cut in 2024. On 14 Dec, dovish remarks from Fed Chair Powell further cemented this outlook, with traders now indicating a 71% probability of a 25-basis point cut by March 2024.

Should overall US economic data, including the NFP report, disappoint, it could reinforce expectations of a Fed interest rate cut in Q1 2024, potentially weakening the dollar. Conversely, a stronger-than-expected jobs report may postpone rate cut expectations, offering an opportunity for the dollar to stabilize.

Figure 6: Central Bank's rising demand for gold



Source: Metals Focus, World Gold Council

Figure 7: Non-Farm Payrolls

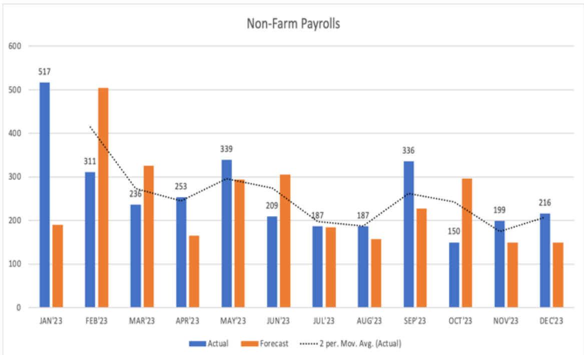
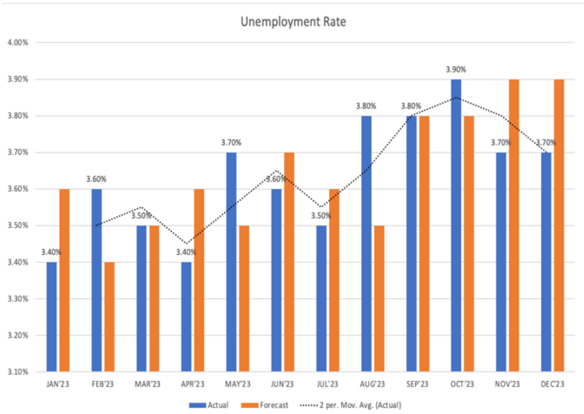


Figure 8: Unemployment Rate



Unemployment Rate

In November 2023, the unemployment rate in the United States fell to 3.7%(Figure8), reaching its lowest point since July and surprising the market, which had expected it to remain unchanged at 3.9%. This reversal from the recent upward trend, which saw a near two-year high in October, contradicts signs of a slowing labor market. The decrease was accompanied by a reduction in the number of unemployed individuals by 215 thousand to 6.291 million, while the count of employed individuals witnessed a significant increase of 757 thousand to 161.969 million. Notably, the decline in the unemployment rate persisted despite a marginal rise in the labor force (0.1 percentage point to 62.8%), with the employment rate also seeing a 0.3 percentage point increase to 60.5%.

Conference Board(CB) Consumer Confidence

Conference Board (CB) Consumer Confidence(Figure 9)measures the level of consumer confidence in economic activity. It is a leading indicator as it can predict consumer spending, which plays a major role in overall economic activity. Higher readings point to higher consumer optimism.

In December, the Consumer Confidence Index by the Conference Board witnessed a substantial surge, marking the most significant monthly increase in almost three years. The index rose impressively from November's revised 101.0 to 110.7, surpassing the anticipated forecast of 103.8. This surge suggests a notable improvement in consumers' perception of economic conditions and their expectations for the future.

It implies a robust increase in consumer confidence, which can have widespread implications for the economy. Strong consumer confidence often translates to increased consumer spending, a key driver of economic growth. In the context of the foreign exchange market, this positive sentiment could potentially be seen as a bullish factor for the USD, as it may attract foreign investment and contribute to the overall strength of the currency.

Purchasing Manager Index(PMI)

The Manufacturing Purchasing Manager's Index(PMI)(Figure10) measures the activity level of purchasing managers in the manufacturing sector. A reading above 50 indicates expansion in the sector; below 50 indicates contraction. Traders watch these surveys closely as purchasing managers usually have early access to the data, which can be a leading indicator of overall economic performance.

Non-Manufacturing PMI

The ISM Non-Manufacturing Purchasing Managers' Index (NMI)(Figure11), also referred to as the ISM Services PMI, serves as a composite indicator for assessing the overall economic condition of the non-manufacturing sector. Calculated from diffusion indexes with equal weights for key indicators such as Business Activity, New Orders, Employment, and Supplier Deliveries, the NMI offers insights into sectoral expansion or contraction. A reading above 50 percent signifies growth, while below 50 percent indicates contraction. Compiled from monthly responses by over 370 purchasing and supply executives across 62 industries, representing nine divisions based on Standard Industrial Classification (SIC) categories, the report provides a diversified and GDP-aligned perspective on economic trends in the non-manufacturing sector.

Figure 9: CB Consumer Confidence

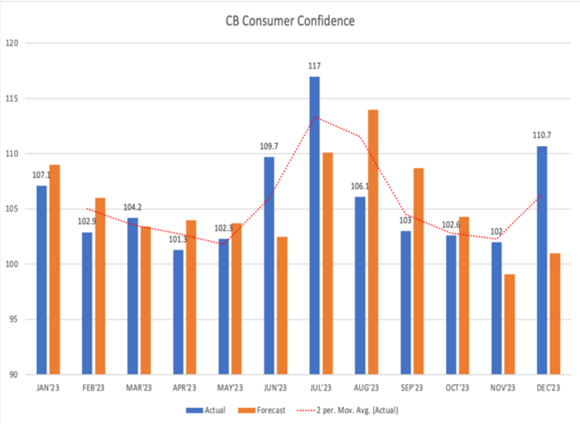


Figure 10: Manufacturing PMI

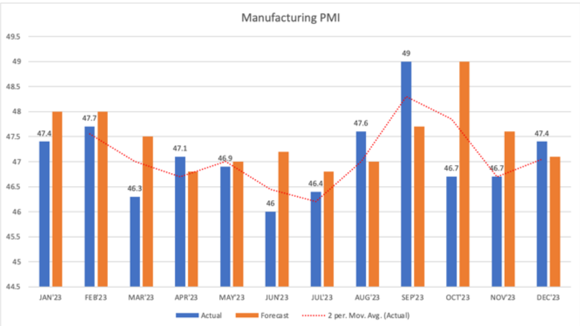


Figure 11: NMI

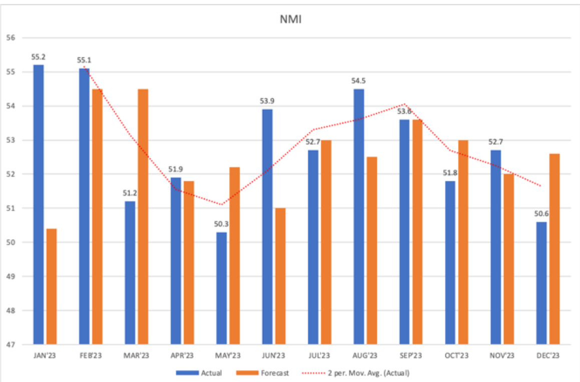


Figure 12: XAUUSD Weekly Chart

Source: TradingView

Gold Price Outlook

In 2023, gold proved resilient, hitting a two-year high above $2100 in December with a year-to-date gain of 17.67%. Market sentiment leaned towards the potential conclusion of the current tightening cycle, amplified by escalating geopolitical tensions in the Middle East and Ukraine.

By December 10, gold prices surged an impressive 26.69% in Q4, surpassing the crucial $2000 per ounce level(Figure 12). Trading within an ascending wedge since June 2022, the metal hints at a potential move towards the May high above $2075 with sustained momentum. Conversely, $1999 acts as a key support level for potential pullbacks.

Looking to 2024, the positive outlook for gold endures, underpinned by consistent factors driving its appeal. Gold's trusted status as a wealth preserver during economic challenges gains prominence, and the anticipated economic slowdown in 2024 is expected to further elevate gold's position as a safe-haven asset.

Sentiment Analysis

Following the NFP announcement, the US Dollar exhibited strength against other currencies(Figure 13). As of 06/01/2024, the US Dollar Index has surged by 1.19% for the day, standing at 102.070.

The Consumer Sentiment Index(Figure 14), a key leading indicator, reflects consumer sentiment and future behavior. A decline in sentiment often coincides with increased saving and reduced spending. Integrated into the Leading Indicator Composite Index, a decrease in consumer sentiment signals potential economic sluggishness. The notion of a negative correlation between gold prices and consumer confidence is intriguing, as gold is often sought as a safe-haven asset during economic uncertainty. However, gold prices are multifaceted, influenced by geopolitical events and central bank policies. While consumer sentiment is valuable, a comprehensive analysis considering broader market dynamics is essential.

Technical Analysis

Strategy Analysis

1. Trend Direction

- Analysing both the weekly(Figure 12) and daily charts(Figure 15)reveals a clear uptrend for XAUUSD. The price consistently maintains a position above my SMA200(Simple Moving Average), a crucial trend line.

- Furthermore, the occurrence of a golden cross between two of my moving averages solidifies the confirmation of the uptrend. Based on these indicators, I am inclined to consider a LONG position.

2. Moving Average Convergence Divergence(MACD)

- Examining the daily chart, the MACD has consistently indicated a bullish signal since 1964, and its momentum continues to present a favourable buy signal for traders considering a LONG position.

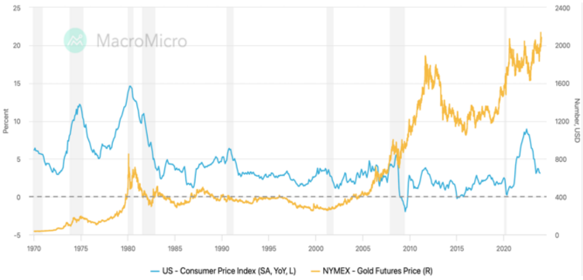
3. Fibonacci Retracement

- Examining the Fibonacci retracement, notable rejections occurred at the 0.618 and 0.5 levels, recognized as the golden zone, providing traders with strategic points to set their buy limits.

Figure 13: US Dollar Index

Source: TradingView

Figure 14: US-CPI vs Gold Price



Source: MacroMicro.me

Figure 15: XAUUSD Daily Chart

Source: TradingView

Entry Analysis

1. Entry Point

- Entry point is estimated to be around $2026.77 - $2007.26, which is in range of the psychological levels of the market at 0.809 and 0.736 levels.

- This range is positioned above the SMA of 26, which acts as the support zone for the entry point.

2. Target Zone

- Utilizing the Fibonacci retracement technique adds a dynamic touch to identifying the take-profit zone. Through the strategic placement of two Fibonacci retracements on distinct waves, the chosen profit zone unfolds within the enticing range of 2242.95-2348.59, perfectly aligning with the intriguing Fibonacci 1.618 levels.

3. Risk-Reward Ratio

- Underpinned by a thorough analysis and meticulous setup, a defined risk-reward ratio of 1:6.22 stands as a pivotal metric. This ratio plays a crucial role in evaluating the expected return against the associated trade risk.

Disclaimer: