



## Gold Review

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Gold – Lets corner the market!

The Gold price looks to be stable at the top end of its current range. As we continue to support the Gold price trading higher it is important to revisit the reasons why we like the metal. Below is a briefing on the current issues affecting the Gold market next year and why we suggest the price of Gold will continue to strengthen during 2006.

**We are still tipping for the metal to trade towards US500 and possibly to US550 by the middle of next year. Below are several reasons why we think the fundamental news may corner the market into trading higher?**

Overall we can identify four major issues, which will affect the price of Gold during 2006: Production Deficits, US Inflationary/Economic concerns, Central Bank rhetoric changing and Fabrication demand continuing to expand.

- **Production Deficits** - One of the prime motivators for the price rise has been the yearly deficits in production. Last year global production according to GFMS fell to an eight-year low to 2,464 metric tons, this is the second decline in three years. The drop reflects a plunge in exploration spending after gold reached a 20-year low in 1999 and reserves became more difficult to find and develop. Overall production last year was down 5% and it is anticipated that production will continue to stagnate as exploration expenditures in the past 6 years have been slashed due to the low price of Gold in 1999. As an example spending fell to \$784 million in 2002 from a record \$2.96 billion in 1997. The trend is likely to be reversed as prices continue to trade higher, however, production from new mines will take time to come on track. Mine development can take up to twelve months plus before the first ingot is poured. The concentration of funds for exploration by major producers is also likely to be further reduced due to the recent trend from producers in resourcing projects. This trend sees major miners taking over existing smaller producers instead of exploring. The reason for this is that Gold reserves are known rather than adopting the hit and miss strategies for new deposits, as in the past. This trend further adds pressure on the supply side for the metal in the future, as no new supply is anticipated.
- **General US economic concerns caused by inflation.** The investor market remains cautious over inflation caused by the sustained increase in Oil prices.
- **Central Bank Activity** - The Washington Accord, continues today to limit the annual gold sales by Central Banks, however, some Central Banks (CB) are actually looking to purchase Gold. CBs such as Russia, South Africa and China are looking at the prospects of increasing the % share of foreign exchange that are backed up by gold. By comparison the US have 64% of foreign exchange reserves backed up by gold, whilst Russia has 3.6%, South Africa has 9.1% and it is reported that China has 1.1%. This is important from a stability point of view, in particular if you are an emerging economy. Of note is the Russian CB, which presently has 5% of its national reserve portfolio invested in gold, accordingly, they would like to hold 10% of gold in reserves. Russia presently has a reported 500 tons of gold in its reserves. If Russia looked to double its reserves it would consume all domestic production for three years. On the other side of the ledger, European CBs such as France and Germany are looking to sell off some reserves. Looking at the % of foreign exchange backed by gold for these CBs, France 56.4% and Germany 50.5% then potential sales are relatively small and really cannot be compared to the % s by Russia, South Africa and China. If CB policies are starting to favour Gold for stability of foreign exchange holdings then China is definitely light on. We would envisage that part of policy by the emerging economy would be for them to increase this reserve as a matter of course in looking to freeing up their currency.
- **Fabrication demand for Gold in particularly for jewellery** has as always fluctuated in line with seasonal demand such as the Indian wedding season and the general perception in the state of the global economic growth. Of note this year has been the continual support offered to the market by physical buyers on any dips. This year, in particular has seen a marked

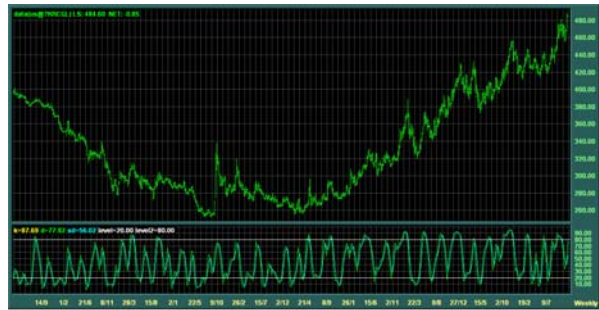
increase in physical demand. Gold jewellery off take rose 17% in the first quarter of this year in comparison to the same period last year. General demand for Gold last year saw fabrication demand increase by 5.7% with the noticeable pick up being from developing countries such as India, China and Turkey. Indian demand for the metal rose 47% last year and in China demand was up by 14%. Physical demand from China is a wild card for 2006, however, early signs so far from this year indicates continuing demand to be solid.

Given the fundamental picture for the metal continues to be solid. How does the technical picture stack up?

Technically, the market has been trending upwards since Jan 01. Weekly technicals both trend and momentum remain bullish. This falls in line with our fundamental view. The trend line on a monthly chart (below) indicates this as well. Any reversal of this trend currently needs to see 447 broken on a weekly basis then 380. As markets do not always move in a straight line we can assume that Gold is cheap again around the 450 level. As can be seen by the same chart, 500 is a huge psychological level. We would anticipate that the market will have a go at this level in the near future, hopefully this side of Christmas. Once this has been reached we will see a more drawn out correction that potentially will realise the 455 level. This should take us over the holiday period. A break of 450 sends our models in to a neutral to bearish trading pattern.

At the moment, on a short-term basis, we believe the market is over bought and see the potential for a pull back. This pull back will be healthy for Gold and will help it to gain momentum for the ultimate push though to 500. The last time it was at this level was Dec 1987 and February 1983. Each time it hit these levels we had significant corrections. As with any trading it is important to know the range and where we will be wrong. The immediate trading range is 488.50 – 480.50. If going long then look for dips back to 484, 480, 474, 468 and we will be wrong if 455 is broken on a daily basis.

### Weekly Bar Chart



### Monthly Bar Chart



### Strategy:

We continue to support the fact that Gold is midst a major bull market and believe, given the above that we will continue to see a structural change in the demand side of the equation into 2006. Therefore dips should be well supported. Best buying comes between 484 and 480. If this breaks then 474 is the next support level. Our models see a deeper correction if 455 is broken on a daily basis.

Please do not hesitate to call concerning any of the above. I can be reached on direct call 1300 660 734.

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