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Gold expert still predicts strong gold market

Sydney, 16 December 2016 – VanEck's gold expert, Joe Foster, believes despite the decline in the gold price since the US election outcome, the outlook for gold is strong based on a number of significant obstacles facing the US economy.

Mr Foster, Portfolio Manager for VanEck's gold equities strategy, said, "The markets have gone into fantasy mode since the US presidential election. US stocks have reached new all-time highs, the US dollar has soared, copper has had a parabolic rise and interest rates are up substantially while gold has tanked. All of these strong moves indicate the market is pricing in a rosy scenario in which projected Trump tax cuts, infrastructure spending and regulatory reforms ignite robust economic growth that enables the Federal Reserve to normalise rates.

"This outlook works against safe haven assets like gold and bonds. While we are hopeful for such an outcome, it will be very hard, if not impossible, to achieve in reality," Mr Foster said.

According to Foster, there are a number of obstacles that pose an imminent risk to the rosy scenario that is currently priced into markets which are outlined below:

- **Extreme debt levels** – Aggregate household, business, and government liabilities currently total 250% of GDP. At such debt levels, servicing and/or reducing debt take priority over spending and investment. The 2016 fiscal deficit was US$523 billion, 2.9% of GDP. The total government deficit amounts to 77% of GDP and the Congressional Budget Office (CBO) projects it will reach 85% in 2026. The Wall Street Journal estimates of the cost of the Trump tax plan range from US$3.5 to US$6.2 trillion over 10 years, which would boost government Debt/GDP to over 100%, according to the Tax Policy Center.
- **Late cycle constraints** – At over seven years, this economic expansion is the 4th longest since 1902. Pent-up demand for big-ticket items might be exhausted. Trends in a number of leading indicators are following past late cycle trends. The risk of recession in the next four years appears to be increasing.
- **Fed tightening** – Tightening policies are inherently designed to bring slower growth. Rising rates are also an impediment to the housing and auto markets.
- **Infrastructure limitations** – Mr Trump plans US$1 trillion of infrastructure spending over 10 years, however, we have already seen how little impact President Obama's 10 year US$860 billion "shovel ready" infrastructure program launched in 2009 has had on the economy.
- **US dollar strength limits growth** – As the US dollar strengthens, it becomes a drag on exports and industrial growth.
- **Fully valued stock market** – The S&P 500 Index is up 229% in a bull market that is over seven years old with lofty P/E (price-to-earnings) valuations of 20x.

Mr Foster said, "It doesn't seem the current market is accounting for the challenges the Trump administration faces. The market response to the US election is, in our opinion, all based on expectations, not fundamentals. Markets have also lost sight of the potential risks that radical monetary policies globally pose to financial well-being. We believe that at some point sentiment will evolve to reflect these inherent risks.

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“It is impossible to predict the catalyst that shifts market psychology but it could come soon after the 14 December Fed rate announcement, as happened last year. Until a catalyst emerges and as long as bullion ETP outflows continue, gold is likely to struggle. However in the longer term, our conviction remains for a strong gold market.

“A couple of points of historic interest: The S&P 500 Index, the Dow Jones Industrial Average and the Russell 2000 Index hit new all-time highs at the same time in November. The last time this happened was 31 December, 1999. The best election to inauguration stock market performance in history was with Herbert Hoover, who was sworn in on March 4, 1929. Both of these events occurred just prior to monumental stock market crashes,” Mr Foster said.

To view Joe Foster’s full commentary go to VanEck Australia’s blog site https://www.vaneck.com.au/blog/gold/

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