Market Update 11th February 2010

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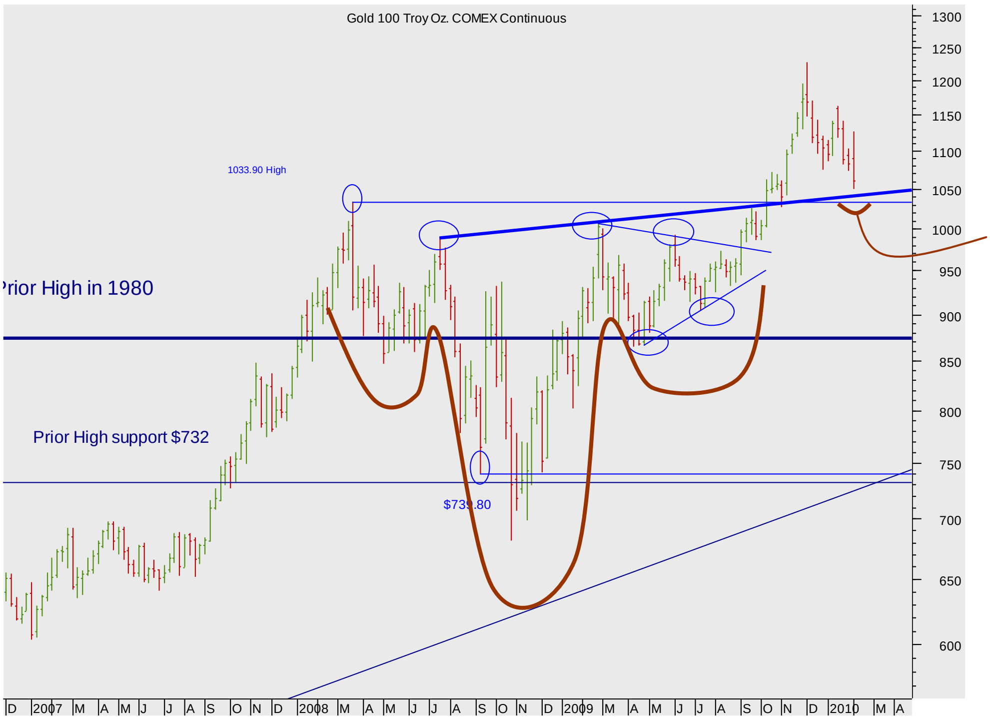
Are the Gold bears broken? It's not clear.

The Technical Trader's view:



WEEKLY CHART

The pull-back to the massive support from the prior High at 1033 has almost made it.

The long run Neckline was a little higher than there at about 1042 or so.

Like many others we have been watching it and wondering: did that pull-back get close enough for bulls to buy for the bounce – since we remain wedded to the medium term bull pattern and target of very much higher? About 1350 in fact.

Look closer.

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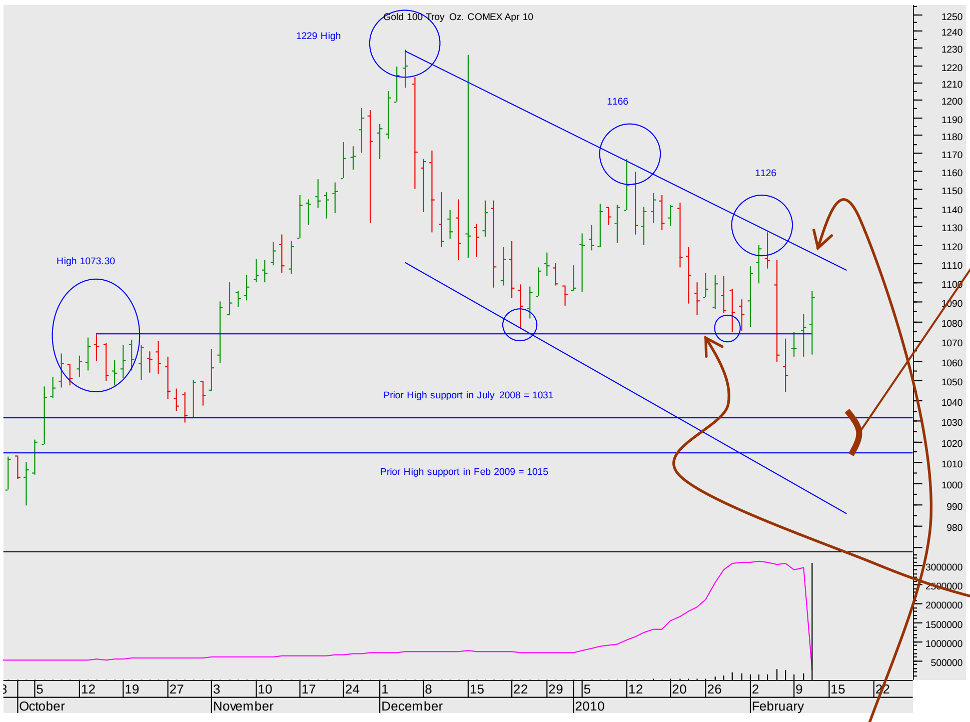

DAILY CHART

Well, it got pretty close to 1033. And in the April 10 contract there was a band of support from Prior Highs at 1031-15.

<u>That wasn't quite tested either.</u>

But the market has bounced. Rather impressively, you might say, surging (as Gold does) through the resistance from two prior lows above the market at1073-5 or so.

<u>But we are not totally convinced.</u>

There is a falling diagonal well-established above the market at 1110. Now, lacking a Reversal pattern at the supports, we would require a close above that diagonal before buying. Completing a bull falling wedge.

The Macro Trader's view:

The Gold market continues to frustrate both Bulls and Bears. Although the highs were made in early December 2009, the long drawn-out retreat has been orderly. And on two occasions the market has attempted to re-establish the underlying Bull trend.

What lies behind the price action?

We judge gold is in a consolidation phase. Since gold made the high last December the Dollar has enjoyed a period of strength. Initially this was driven by improving data, and has been aided on several occasions by spikes in risk aversion.

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The current leg of the Dollar rally, Gold weakness, is again due to risk aversion. This is currently centered on the Sovereign risk concerns provoked by Greece and other weak peripheral Euro zone members.

But the question begs asking: if Sovereign risk deterioration is behind recent price action in currencies, stocks and Bonds, why is Gold not rallying hard?

Because of the nature of the Euro zone, traders are unable to sell national currencies for Greece et al because they no longer exist, but what they have been doing is selling Greek, Spanish and Portuguese Government Bonds and Buying Bunds. This has caused yield spreads to widen out sharply and has caused the Euro to weaken against mainly the Dollar and the Yen as fears of a Greek default have increased.

So traders are buying the Dollar more as a default consequence of wishing to sell the Euro. But a stronger Dollar usually equals a weaker Gold market.

At some point traders will stand back, re-assess and recognize that the fiscal health of the US isn't any better than the Euro zone countries currently being targeted. What so far makes the difference between US debt and that of Greece is confidence. The US has a long history of honouring its obligations. As the world's largest economy by a margin, with the Dollar the World's sole reserve currency, traders/investors are giving the US the benefit of the doubt over the management of its government finances.

But that can only be stretched so far and the credit rating agencies have begun flagging risks. Obama continues to forecast large budget deficits which are piling up the national debt and although he has said he wants to halve the deficit by the end of his Presidential term, so far his actions don't match that aspiration.

So the Dollar buying may come to an end. And it may yet begin to be sold. If the Euro zone does manage to calm the current crisis, traders will refocus. The UK and US could yet find their bond markets and currencies coming under renewed pressure and that would lift gold.

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Seven Days Ahead

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