Bullion Weekly

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Bullish

- Further unrest in financial markets
- Geopolitical tensions rise over Iran
- Potential for safe-haven buying

Bearish

- If equities fall, bullion may sell off initially
- Safe-haven buying to support dollar
- Potential for profit-taking

Outlook

Short Term	Consolidate gains	$1,000/974
Medium Term	Move up to tackle highs at	$1,032.50
Long Term	Set new highs above	$1,050

Last Week:

- Markets again seemed a little unsure on direction as risk appetite flip-flopped in reaction to economic data - particularly US employment numbers - news headlines and speeches from finance officials ahead of the G7 meetings. Month- and quarter-end book-squaring was also a feature, with equity markets as a whole finishing lower, with both the Dow and S&P500 down 1.8% on the week. The CRB Index and Dollar Index both posted slight gains, up 0.9% and 0.25% respectively.
- While gold and silver continued to reflect both risk sentiment and the dollar, both metals were rangebound. Gold traded in a $25 range across the week, spending Monday, Tuesday and early Wednesday at $985-$998 before reclaiming the $1,000 level as sentiment picked up. Gold rose 5.25% in September and 8% across the third quarter; silver posted a 12.5% gain in September and 22.5% in the third quarter.
- Near-record prices continue to dampen demand from the jewellery sector. The Bombay Bullion Association announced gold imports of 35-40 tonnes in September, down 77% on the previous year. Imports could drop to zero in the last quarter, one official suggested, while prices remain close to all-time highs and farmers contend with disastrous drought conditions. Gold imports into Turkey, the world third-largest consumer, tumbled 94% year on year in September to just 1.7 tonnes. Silver fared no better, with imports at just 0.9 tonnes. But the tone is not uniformly negative – rising geopolitical tension towards Iran could spur demand from neighbouring areas in the coming weeks.

The Week in Numbers NYSE-Liffe (mini-sized contracts)

Gold Dec	Mon 28	Tue 29	Wed 30	Thu 01	Fri 02	Week*
High	998.10	997.30	1010.60	1011.20	1008.80	1011.20
Low	987.00	985.90	992.70	998.70	987.20	985.90
Close	994.20	994.10	1009.30	1000.20	1004.40	13.00
Silver Dec						
High	16.328	16.310	16.705	16.820	16.490	16.820
Low	15.750	16.016	16.171	16.332	15.910	15.750
Close	16.195	16.180	16.672	16.437	16.237	0.166

* week's high, week's low & change on week

The Week Ahead:

The dollar is expected to be the primary driver of bullion but a sell-off in equities could dominate events should one start. Bearish economic data last week has continued to change the tone of the equity and commodity markets - investors are seemingly mulling the increasingly splintered global recovery narrative that has been at the heart of the broad rally since March.

Further weak data could begin to test the mettle of the equity bulls and test the correlations between gold, the dollar and equities, we believe.

If equities sell off, we would expect bullion to initially suffer but the secondary reaction would probably be bullish for bullion as safe-haven demand increases. Indeed, risk-averse investors have seemed to be favouring the yen over the dollar as their safe-haven currency choice in recent weeks.

In turn, this could soften the downside risk for bullion as it may limit the extent of a rebound in the dollar.

Date	Economic Agenda	Expected	Previous
Tuesday 6th Oct	IMF Meeting		
	UK GDP		0.20%
Wednesday 7th Oct	Japan L.I.	83.4%	82.5%
	IMF Meeting		
	EU GDP	-0.1%	-0.1%
	US Crude Oil Inventories		2.8M
	US Consumer Credit	-10.2 B	-21.6 B
Thursday 8th Oct	Japan Eco Sentiment	42.5	41.7
	BoE interest Rates	0.50%	0.50%
	ECB Interest Rates	1.00%	1.00%
	US Initial Jobless Claims	543K	551K
Friday 9th Oct	Fed Chairman Bernanke speaks		
	ECB Trichet speaks	0.10%	-1.5%
	US Trade Balance	-32.7B	-32.0 B
	FOMC Members speak		

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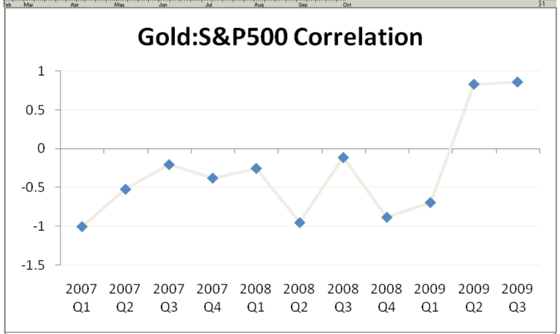
Focus - Gold seen as vulnerable but only temporarily

Financial markets remain close to multi-month highs as the broader macroeconomic picture continues to improve, with the IMF suggesting the world economy is on the "verge of recovery".

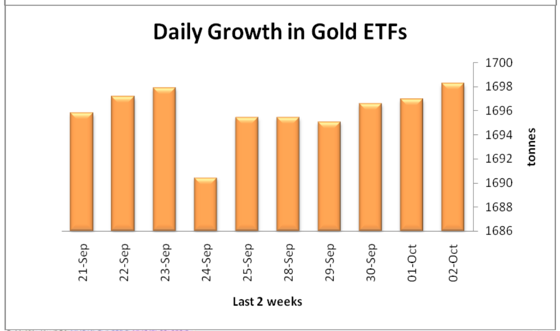
But some signs of fatigue have been emerging in recent weeks, particularly as to the sustainability of an economic recovery in the US after housing sales lagged behind forecasts, durable goods fell 2.4% in August compared with an increase of 4.8% in the previous month and the end of the car scrappage programme has hit auto sales, with September figures down 22.7% year on-year. Deflation fears have also risen but, as we have said previously, gold should perform well in both an inflationary and deflationary environment.

Given the rise in bearish sentiment, we think equities could be readying for a correction lower as investors curb their risk exposure and return to safe-haven assets. While gold traditionally comes under this category, it has been moving more in line with risk sentiment in recent months – as shown in the accompanying chart, with gold and the S&P 500 moving towards a very strong correlation.



Given this correlation, the scale of speculative/fund longs built since the end of August, the relatively mild influx of ETF investment demand and low physical interest gold is also looking vulnerable. But we believe that any dip will be short-lived, with some substantial pent-up demand lurking below the market.

First, the inflation/deflation argument will probably prompt strong bargain-hunting from investors. Second, the dip will also draw interest from producers, keen to continue their dehedging programmes, and the jewellery wholesale sector ahead of the festival season. Third, central banks may also use any price correction to increase their holdings.



Other observations

- Combined gold ETF holding climbed 2.8 tonnes last week
- Combined silver ETF holding fell 2.8 tonnes last week
- Fund net long position dropped 16.7 tonnes

Technical Analysis - Gold

Gold closed bullishly last week, forming a bullish Harami reversal pattern. It opened above $1,000 this week, which is bullish. The stochastics have improved but the K% line needs to cross over the D% line and move into the strong buying range to become bullish. The RSI looks positive too.

Gold prices are well supported by the 5WMA [weekly moving average] for now. We are neutral to bullish this week and would become positive if gold can close above $1,008 this week with the stochastics having crossed higher. Support: $996-$991-$985-$983-$973. Resistance: $1008-$1011.98- $1020-$1024- $032.

Technical Analysis – Silver

Silver closed neutrally last week but in doing so formed a bullish Doji Harami reversal pattern. Looking at the chart, silver is in a downside flag formation. This is will be negative for the metal until it can close over the upper flag line [$16.63].

The stochastics are presently neutral, as is the RSI, while the 5WMA [$16.44] is causing resistance. Overall, we are bullish in the medium term and neutral in the short term, expecting a trading range of $16.75-$15.70. Support: $16.03-$15.91, $15.70-$15.20. Resistance: $16.44-$16.63-$16.77-$17.00.

Conclusion – Gold is leading the precious metals and, having got within $8 of the record highs, the market is not surprisingly consolidating. The big picture remains bullish for gold: as well as the continuing concerns in the financial markets, geopolitical issues have also resurfaced over Iran's nuclear ambitions. But although we remain bullish in the medium term, we feel an equity market correction is unfolding, which is likely to encourage risk reduction across the board. Such a move is likely to take bullion down with it initially; however, any retreat is likely to be short-lived as it is likely to attract dip buying.

Trader Talk:

"Markets have gone up too much, too soon, too fast… I see the risk of a correction, especially when the markets now realize that the recovery is not rapid and V-shaped but more like U- shaped" Professor Nouriel Roubini

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