

Bullish

- Good support evident at \$1,074
- Sovereign debt concerns continue
- Strong economic data could point to inflation

Bearish

- Dollar rebound continues
- Further risk reduction seems likely
- Buyers sitting on the sidelines

Outlook

Short Term	Build a base	\$1,050/1,075
Medium Term	Move back above	\$1,162
Long Term	Target	\$1,250-1,500

Last Week:

- Commodity and equity markets corrected further last week amid mounting concerns of EU members defaulting on credit obligations. In addition, speculation intensified that the rapid pace of economic expansion in China could force the People's Bank to tighten fiscal policy to ward off the formation of so-called asset bubbles.
- The corrections led equity and commodity markets to their worst monthly performance for some time – the Dow fell 360.7 points, its worst since February 2009, while the CRB Index saw its largest drop since December 2008, down 17.7 points.
- Dollar strength and the broad correction in investor risk appetite pressured gold to its lowest since November at \$1,074.20 but it held above support at \$1,071, closing the week down one percent at \$1,079. Silver fell to a three-and-a-half-month low of \$16.01 as support at \$16.74 failed, triggering stop-loss selling. The metal fell five percent on the week, closing down \$16.19 and pushing the AU/AG ratio to 67.31, its highest since mid-August.
- Data on funds showed sizeable corrections in speculative holdings last week. Silver and gold both endured their largest weekly drop since August 2008, with the net long in gold down 106 tonnes while 1,126.5 tonnes was cut from the net long in silver.
- China is set to maintain its position as the world's largest gold producer after an 11.3-percent rise in output, data for 2009 showed. Output increased to a record 313.98 tonnes, statistics from the China Gold Association showed.

The Week in Numbers NYSE Liffe US						
Gold Feb	Mon 25	Tue 26	Wed 27	Thu 28	Fri 29	Week*
High	1103.80	1103.00	1102.00	1095.30	1089.90	1103.80
Low	1092.90	1085.20	1083.50	1073.20	1075.90	1073.20
Close	1096.70	1098.20	1084.50	1083.70	1082.90	-6.80
Silver Mar						
High	17.255	17.255	16.930	16.731	16.364	16.364
Low	17.008	16.347	16.446	16.065	16.051	16.051
Close	17.151	16.848	16.449	16.198	16.241	-0.728

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

The Week Ahead:

Volatile trading looks set continue this week as efforts by finance ministers from the EU PIIGS – Portugal, Ireland, Italy, Greece and Spain – has done little to underpin the euro, which closed below 1.39 on Friday for the first time since July.

Traders and investors will continue to monitor the newswires closely for signs of positive action to bolster the eurozone currency. But Friday's solid growth reading from the US could see the dollar extend its rebound, with the euro testing chart support at 1.3755-1.3820 and the dollar index testing the psychological 80 mark.

A busy line-up of economic data will also drive direction (see table), with the focus in the early part of the week lying with manufacturing with the release of Chinese, EU and US PMI. Other data includes US ADP Employment change on Wednesday and Non-Farm Employment data on Friday.

Market participants will also look closely at the rate announcements and particularly the strength and tone of accompanying statement from the RBA, the Bank of England, the ECB and the G7 meeting at the weekend.

Date	Economic Agenda	Expected	Previous
Tuesday 2nd Feb	German Retail Sales	1.1%	-1.1%
	Eu PPI	0.0%	0.1%
	US Pending Home Sales	0.6%	-16%
Wednesday 3rd Feb	Eu Final PMI	52.3	52.3
	EU Retail Sales	0.4%	-1.2%
	US ADP Employment Change	-41K	-81K
	US ISM Non manufacturing PMI	51.3	49.8
Thursday 4th Feb	ECB Rate Decision	1.0%	1.0%
	US Initial Jobless Claims	461K	470K
	US Non Farm Productivity	5.3%	8.1%
Friday 5th Feb	Japan Leading Indicators	93.7%	90.7%
	US Employment Report	20K	-85K
	US Unemployment	10.0%	10.0%
Saturday 6th	G7 Meeting		

Focus – It's all about the dollar

January proved to be a month of two halves for gold, with the metal initially buoyant as improving economic indicators increased systemic risk appetite before sentiment soured as fears of EU default intensified, while speculation increased that China could soon be forced to apply the brakes on its resurgent economic rebound.

But while gold is some distance from its December peak above \$1,220 per ounce, it has been well supported by strong scale-down buying from investors and the physical sector in the run-up to the Lunar New Year celebrations. And – importantly – it has held key chart support around \$1,073 despite continued dollar strength and deeper corrections across commodities and equities.

The relationship between gold and the dollar is not always a straight correlation, as we said last week, with gold generally proving more resilient to downside pressure in times of dollar strength. The fact that gold has held such an important technical level is a clear example of this relationship as well as the pent-up demand below the market, which we believe is attributable to several factors including: economic uncertainties among EU member states, the unknown effects of quantitative easing and what impact its reversal will create and – perhaps the greatest fear now deflation has abated – inflation.

Clearly, the short-term outlook for gold is slightly murky and the risk of being pulled along by a deeper broad-based correction remains; however, we believe that it is now fair value and will remain underpinned by growing investment demand.

Other observations

- The combined gold ETFs position dropped 2.05t last week
- The combined silver ETFs position climbed 45.6t last week
- The net fund long gold position dropped 2,056 contracts
- The net fund long silver positions dropped 7,232 contracts

Technical Analysis - Gold

Gold prices have again tested support between \$1,071 - the peak from October last year - and \$1,074. A breach of \$1,070 support would target the 50% Fibonacci retracement level at \$1,045. The stochastics are down in the weak zone so further weakness cannot be ruled out but a rebound now also looks quite likely. A move above \$1,090 followed by \$1,105 would look increasingly constructive. We would start to favour the upside again on a positive cross in the stochastics and on a move above \$1,105 but would remain wary should the rebound turn into another 'dead-cat' bounce.

Should a rebound falter before overcoming \$1,105, we would expect a drop to the \$1,050-\$1,045 area, which might provide a downside trading opportunity.

Technical Analysis – Silver

The sell-off in silver continued last week, with prices pulling back towards the 50% Fibonacci retracement line at \$15.96. Below there is support at \$15.75 – the lows from September 2009.

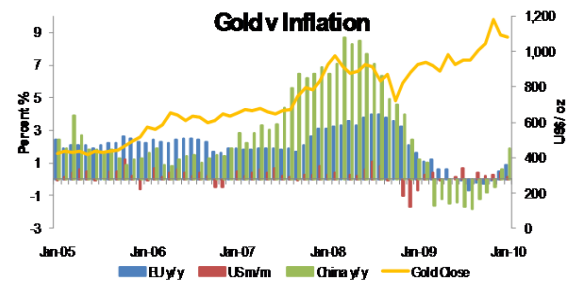
The stochastic indicators have fallen to very low levels so a base may well be found between \$16.00 and \$15.75, in which case look for upside a rebound back towards \$17.00. Resistance is seen at \$16.45, \$16.75 and \$17.98.

We would turn bullish on a rebound through \$16.45 as long as the stochastics had crossed higher by then.

Conclusion – Given the strength of the dollar's rebound, further weakness in bullion cannot be ruled out but support between \$1,074 and \$1,071 seems formidable. If a base now builds above \$1,071, bargain hunters may well grow in confidence. And if equities continue to correct, we would expect some rotation out of equities and into safe havens, especially with currencies also under pressure.

Trader Talk:

"The euro can fall further. Sovereign debt risk will continue to be a key theme. The stresses created by the fiscal situation in Greece won't go away quickly" - Neil Mackinnon, economist at VTB Capital



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