Bullion Weekly

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8th February 2010

Bullish

- Big picture remains bullish for gold
- Sovereign debt concerns continue
- Lower prices likely to attract more buying

Bearish

- Dollar rebound continues
- Further risk reduction seems likely
- Fund longs liquidating while shorts are building

Outlook

Short Term	Build a base	$1,040/1,075
Medium Term	Move back above	$1,130
Long Term	Target	$1,250-1,500

Last Week:

- Investors continued to shun risk last week as eurozone debt fears worsened while key US payrolls data missed expectations, showing a loss of a further 20,000 non-farm jobs compared with a forecast increase of 10,000. In addition, speculation of a Chinese rate increase bubbled away in the background while the Reserve Bank of Australia surprised many by keeping interest rates unchanged, prompting speculation that the country's financial officials are concerned that the economic recovery in the region could stall.
- The absence of detailed plans to tackle the Greek debt situation, coupled with broad negativity towards the EU PIIGS, weighed heavily on the euro across the week – it fell 1.5 percent or two big figures against the dollar and almost three percent against the yen. European equities came under similar pressure, with the benchmark STOXX 50 Index falling 5.25 percent. Their US counterparts fared better, with the Dow posting a weekly fall of just 0.5 percent and closed above the psychologically important 10,000-point level; however, the VIX volatility index staged a sharp increase, jumping 20 percent midweek.
- Gold and silver began the week in an upbeat tone, tracking to highs of $1,125 per ounce and $16.95 per ounce respectively on Wednesday as the dollar softened and the euro briefly reclaimed 1.4000. The mood changed on Thursday, however, as the market reacted negatively to ECB President Jean-Claude Trichet's interest rate speech. Further pressure emerged below $1,070 as technical support at $1,073 failed, triggering stop-loss orders and eventually pushing gold to a three-month low of $1,044.50 and silver a five-month low of $14.65.
- Despite the price correction, jewellery demand remains sluggish, with Turkey reporting imports of just 60 Kg of gold (well below the average of 11-20 tonnes) and 1.1 tonnes of silver in January.

The Week in Numbers NYSE Liffe US

Gold Apr	Mon 01	Tue 02	Wed 03	Thu 04	Fri 05	Week*
High	1108.90	1119.80	1126.80	1111.80	1069.00	1126.80
Low	1077.40	1099.70	1107.60	1058.70	1044.50	1044.50
Close	1105.00	1117.70	1112.10	1064.20	1053.30	-29.60
Silver Mar						
High	16.681	16.794	16.907	16.350	15.358	15.358
Low	16.095	16.589	16.285	15.206	14.660	14.660
Close	16.669	16.759	16.327	15.330	14.835	-1.379

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

The Week Ahead:

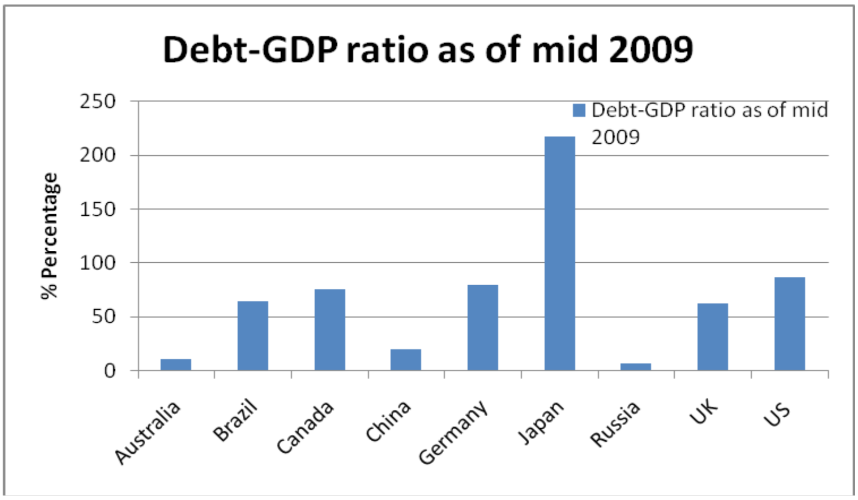
Nervous market sentiment and increasing risk aversion will continue to play a dominant role in shaping markets this week.

European economies are now under intensive market scrutiny and, unless they can instil some confidence, the euro may slip further, potentially piling more downside pressure on bullion. But given the size of the fall in bullion last week, we think the precious metals have a decent chance of consolidating during the first half of the week. With the important data due out on Thursday and Friday, we think that trading will become more volatile at that stage.

Overall, while there is some upside potential for gold, we think the greater risk remains to the downside, at least until the market starts to worry about holding dollars again.

Date	Economic Agenda	Expected	Previous
Tuesday 9th Feb	China New Loans		380B
	IBD/TIPP economic Optimism	49.3	48.8
	US Whole Sale inventories	0.5%	1.5%
Wednesday 10th Feb	US Trade Balance	35.7B	-36.4B
	UK GDP Estimate		0.3%
	Chairman Bernanke Speaks		
	Crude Oil inventories		2.3M
Thursday 11th Feb	China CPI	2.2%	1.9%
	US Retail Sales	0.4%	-0.3%
	Initial Jobless Claims	458K	480K
Friday 12th Feb	EU Flash GDP	0.4%	0.4%
	EU Industrial Production	0.3%	1.0%
	CB Leading Indicators		0.9%
	UoM Consumer Sentiment	74.7	74.4
	UoM inflation Expectations		2.80%

Focus – The dollar is up on safe-haven demand - but is it really so safe?



The exodus from riskier assets by speculative and investment players in recent weeks has prompted a surge in demand for the dollar and US Treasury assets. The euro is now down 4.6 percent in the year to date against the dollar compared with 3.2 percent at the end of January, while the dollar index reclaimed the 80 mark over the week for the first time since mid-July. The latest data from the CFTC has also shown a significant increase in speculative euro shorts, which are at their largest since September 2008.

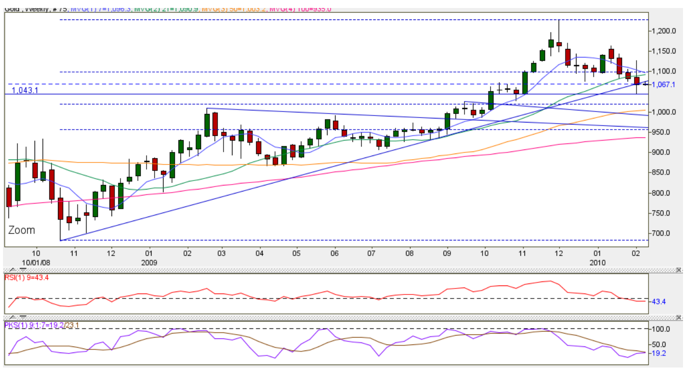
But this return to the dollar as a safe haven may not prove the best choice in the long run either. To quote the crooked police colonel in the James Bond film Quantum of Solace – who takes his blood money in euros – "the dollar isn't what it once was".

Indeed, fiscal deficits are not only a European worry – the US could lose its 'AAA' rating, ratings agency Moody's warned, if its finances fail to improve after the government upped its debt ceiling to $14.3 trillion. Despite Treasury Secretary Tim Geithner's vehement defence of America's 'AAA' rating, this could prove a serious concern to investors large and small and could send huge shock waves through the currency and bond markets. Central banks are already looking to diversify their portfolios and, given the high levels of debt (see chart), we expect this to increase. The trouble is that, with other nations in a similar or worse situation, alternatives are in short supply.

While we expect that most will view the dollar as the least-bad option, we may also see a shift back to hard assets – and gold in particular. Given the current correction, we could see another groundswell of interest such as that of 12 months ago.

Other observations

- Net fund long positions in gold drops 1,755 contracts, as short position builds
- Net fund long position in silver drops 6,192 contract - longs contract, shorts build
- The combined gold ETF position rose 0.45t; the silver ETF position dropped 26.6t



Technical Analysis - Gold

Gold closed negatively last week, forming a thick spinning bottom formation. Although this pattern can often signal a potential short-term bottom, we think that it is more likely to indicate some consolidation.

Gold closed below the long term up trendline [$1,073] last week, which is bearish, and has found some resistance from this trendline today. It also closed below the 23.6% Fibo line (Oct '08 low-Nov '09 high). Next support is at the 38.2% Fibo level [$1,018]. Although the stochastics look bearish, the K% line is near the top of the weak range and is trending just below the D% line.

Overall, we are neutral-negative. We would look to turn bearish ion a drop below $1,043 a close below $1,064 again but would turn bullish if prices close above $1075.

Technical Analysis – Silver

Silver closed negatively last week for a fourth consecutive week. It has traded within a small range this morning, which could be indicative of some short-lived consolidation.

Silver closed below the long- and medium-term up trendlines [$16.18-$15.74] last week, which was bearish, but found support from the 100-week moving average [$14.66] and a long-term internal down trendline [$14.64]. The stochastics and the RSI look bearish.

Overall, given the size of the drop, we think silver has the potential to consolidate above $14.66-$16.44 but we still believe that the greater risk is still to the downside.

Trader Talk:

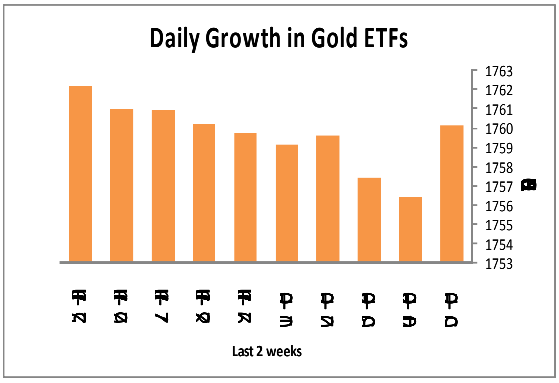
"Sometimes markets seem to defy logic. Recently, we have seen a 'rush to safety' back into the US dollar. But what is safe about the US dollar when the national debt of the US is approaching $12 trillion, unemployment is at 9.7 percent and the economy is not booming?" – David Levenstein

Market Drivers

Euro

Euro extends its decline against the dollar, highlighting dollar strength

That said, we think it is euro weakness driving the dollar rather than dollar strength



Lower prices attracts scale-down buying

Despite the fact that there has been little liquidation in ETFs, it is interesting to note that lower prices are now attracting buying as opposed to further profit-taking

Oil

Oil prices are in retreat, with prices breaking the up trend line.

This suggests a general retreat in commodity prices.

Gold Silver Ratio

The leap higher in the gold/silver ratio shows how silver has fallen faster than gold has.

If the correction continues, expect the ratio to widen further.

Conclusion – Gold has broken below support and therefore may become volatile for a while as traders become accustomed to the new trading range. For now, the dollar seems set to strengthen further, which may weigh on bullion prices but, given sovereign debt concerns and with selling across other markets, we would expect money to move into gold again at some stage before long. The dollar may be rising as carry trades are unwound but the market is likely to remain wary of becoming comfortable with the dollar and, as such, gold is likely to benefit.

To learn more about trading gold and sliver on NYSE Liffe US
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