

Bullish

- Bargain hunting has emerged
- Sovereign debt concerns continue
- A base seems in place

Bearish

- Fund longs liquidate, while shorts are building
- Dollar rebound continues
- Market remain nervous

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:

- Markets remained in volatile mood last week, with risk sentiment swinging backwards and forwards on news headlines related to the European Union. But despite the intraday fluctuations, market sentiment appeared to improve modestly across the week as EU leaders announced they would take "determined and co-ordinated action" to support Greece's efforts to regain control of its finances.
- In addition, the People's Bank of China made the surprise decision on Friday to increase bank reserve requirements a further 50 basis points to 16.5 percent. This is the second increase this year as the central bank tries to stem growing concerns about the formation of asset bubbles given the economy's rapid rebound.
- This led the Dow to gain 0.85 percent across the week, despite closing below 10,000 on February 8. Support for Greece also bolstered the euro, which gained 0.5 percent against the yen but lost ground to the dollar, slipping 0.4 percent. The dollar index straddled the 80 level for much of the week, closing unchanged at 80.24.
- As has been a theme for some time, gold again proved more resilient in times of dollar strength, finding good support from investment demand as well as physical buying ahead of Chinese New Year celebrations. Gold ended the week up 2.4 percent at around \$1,091 per ounce, with EUR/gold reclaiming the 800 mark and nearing all-time highs early this week. The correlation between gold and the EUR/USD cross consequently stood at 0.68 from 0.97 in the prior week. Silver posted a similar 2.75-percent gain over the week; the AU/AG ratio levelled out.
- Data for the week to the February 6 showed another substantial cut in speculative longs and a build in shorts.

The Week in Numbers NYSE Liffe US

Gold Apr	Mon 08	Tue 09	Wed 10	Thu 11	Fri 12	Week*
High	1074.10	1083.80	1082.80	1098.30	1094.10	1098.30
Low	1061.90	1063.80	1063.50	1073.20	1078.20	1061.90
Close	1065.70	1077.20	1076.20	1094.60	1089.60	36.30
Silver Mar						
High	15.300	15.575	15.612	15.712	15.688	15.300
Low	14.953	15.050	15.100	15.200	15.224	14.953
Close	15.082	15.437	15.300	15.590	15.446	0.611

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

The Week Ahead:

Greece's sovereign debt crisis will no doubt continue to drive the bullion markets this week. European financial ministers are meeting on Monday and Tuesday to thrash out a bailout plan. While some form of rescue package is now likely, the real issue is whether the markets will perceive this bailout as substantial enough to allay fears of Greece's debt spreading to other peripheral EU countries.

A great deal of US data is due this week and, with markets already on edge, any figures that confound expectations could exasperate risk aversion already present in the markets. The rescue package and the economic data remain two of the central themes to this week but we note more chatter about the possibility that China will revalue the yuan, which would be another major turning point for the markets, making Chinese imports cheaper, which would probably be bullish for commodities. All in all, while we think there is good upside potential for bullion in the medium term, we remain wary in the short term should this stronger tone prove to be just a bear market flag.

Date	Economic Agenda	Expected	Previous
Tuesday 16th Feb	EU ZEW Economic Sentiment	42.6	46.4
	Empire State Manufacturing	17.0	15.9
	TIC Long Term Purchases	50.3B	126.8B
Wednesday 17th Feb	US Housing Starts	0.58M	0.56M
	US Industrial Production	0.7%	0.6%
	FOMC Minutes		
Thursday 18th Feb	US PPI m/m	0.8%	0.2%
	China CPI	2.2%	1.9%
	Initial Jobless Claims	445K	440K
	Philly Fed Manufacturing	17.2	15.2
	CB Leading Indicators	0.6%	1.1%
Friday 19th Feb	Japan All Industries Activity	0.3%	0.1%
	EU Manufacturing PMI	52.8	52.5
	US CPI	0.2%	0.1%

Focus – Euro faces big questions despite rescue package

"Euro area member states will take determined and coordinated action, if needed, to safeguard financial stability in the euro area as a whole. The Greek government has not requested any financial support."

Those were the words used by EU President Herman Van Rompuy after last week's summit to discuss Greece's debt issues. The decision to support Greece prompted a rebound in risk sentiment over the week but the lack of details on exactly how EU members will support Greek debt, which is expected to hit 290 billion euros (\$394 billion) this year, raised suspicions that Germany, Holland and the creditor states of Northern Europe still cannot agree on the terms of any bailout. And rather than acting directly, Germany and the like are more likely to provide support through state banks or sovereign wealth funds.

EU officials have been relatively quick to act to avoid contagion but while the decision to help Greece may relieve the immediate pressure it will only throw the spotlight on the next troubled states such as Portugal, Spain and Italy. And it is this debt domino that has raised serious questions over the euro both as an entity and particularly as a reserve currency alternative to the dollar. We have previously touched on how US debt has led the dollar to lose its appeal and, with other traditional reserve currencies facing similar problems, there could be a broader shift away from fiat currencies in the making.

We have reports of modest demand for bars/ingots and coins. The US mint, for example, has sold 50,000 one-ounce Eagles so far this month compared with 85,000 in January. ETF demand is also rather stale, with holdings in the SPDR fund down 5.5 tonnes in the month to date as improving equity sentiment draws demand. But should EU worries resurface, we expect share values to come under pressure again swiftly, at which point we expect demand for gold to jump – as it did this time last year.



Other observations

- Net fund long positions in gold drops 28,650 contracts
- Net fund long position in silver drops 7,512 contract
- The combined gold ETF position rose 4.8t; the silver ETF position climbed 81t



Technical Analysis - Gold

Gold closed above the primary long-term up trendline [\$1,079] last week, which was positive in the short term. Both the RSI and the stochastics look constructive. As such, we remain neutral-positive for now but gold must close above the 23.6% Fibo [\$1,103] to maintain bullish momentum.

Doing so would give it an upside target of \$1,125-\$1,140. But should gold fail to close above \$1,103, we think it has a chance of retesting weakened trendline support from the primary up trendline [\$1,079].

If gold breaches below \$1,079, we would suggest that it would target \$1,062-\$1,045-\$1,027-\$1,018.

Technical



Analysis – Silver

Silver closed positively last week but still failed to close above the long-term primary up trendline, which is bearish. There are two important sets of Fibonacci retracement levels on the charts: the first at the 2008 high-2008 low and the second at the 2008 low-2009 high. Both sets indicate that a close below \$15.53-\$15.27 this week could force silver back to \$13.98-\$14.15 to find long-term support.

The stochastics look bearish and the RSI is not much more positive. With this in mind, we are neutral on silver and would turn negative on a breach of \$15.27-\$15.00. But we would be prepared to turn positive on a close back above \$15.75.

All in all, we think there is some bullish potential in the very short term but the downside risk is far greater.

Trader Talk:

"If the Chinese economy crashes, it will be a disastrous environment for commodities" - Marc Faber

Market Drivers

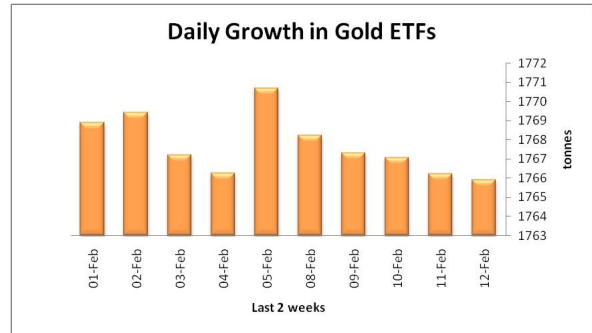
Euro



Euro has extended its decline against the dollar, highlighting dollar strength.

Former resistance from March and May 2009 is now providing some support but this is being tested. If support breaks, expect bullion to drop further.

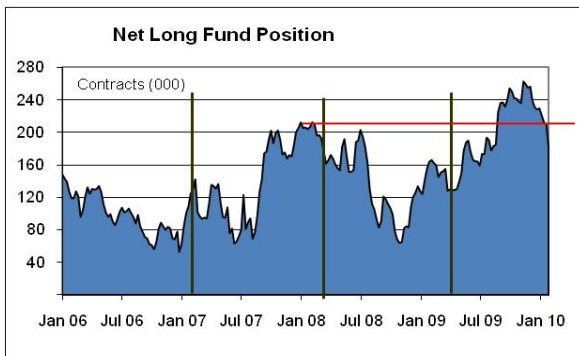
ETFs



Investors continue to cut their exposure to gold but, interestingly, there is some buying into silver ETFs

The gold/silver ratio (see chart below) shows that silver has corrected more than gold has.

Funds



The net fund position is dropping quite sharply as longs liquidate and shorts add to their positions. Longs cut their exposure by 23,273 contracts while shorts added 5,377 contracts.

Gold Silver Ratio



This chart suggests that you get more 'bang for your buck' with silver rather than with gold.

If prices continue to rally, expect the ratio to drop again.

Conclusion – Gold's rebound looks encouraging - it may be that the downside correction has now run its course but we would remain on high alert as it could be that prices are just bouncing, having become oversold. Although we remain bullish overall on gold, we feel the profit-taking by the funds could spill over to ETF investors and we would not be surprised to see equities correct further too. All of this could initially prompt further bullion weakness, although the secondary reaction to selling in other asset classes would probably again be bullish for gold and, to a lesser extent silver. As such, we would run with these rebounds while they last but be on the lookout for the rebounds to falter, in which case the recent lows could be retested and even extended.

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