A 'Precious' Year Ahead

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Gold Is Ready To Shine, Time To Accumulate

- The COVID19 pandemic has unleashed the strongest response from the policy makers yet. The global appetite for excess monetary and fiscal support creates an excellent backdrop for Gold prices to move higher.

- We reckon that the excess monetary easing required to mop up the large proportion of Government debt, is creating a bigger financial debasement than the Global Financial Crisis of 2008. This is because Governments are over leveraged in comparison whereas private and household sector activity remains sluggish. Central Banks' key focus, brought about by lockdown led economic disruptions, is to help Governments raise resources. **This sets the tone for a larger debasement of all major currencies and are positive for Gold.**

- **While QE of this sort can effectively bail out Governments' debt, its impact on growth is likely to be limited.** In US, the velocity of M2 is lowest ever at 1.07, in contrast to 1.6 during the GFC

- To add to it, Gold's own supply and demand dynamics are favourably placed. While nominal gold prices are at record highs, real gold prices have not breached their previous highs-indicating more steam is left in the current cycle.

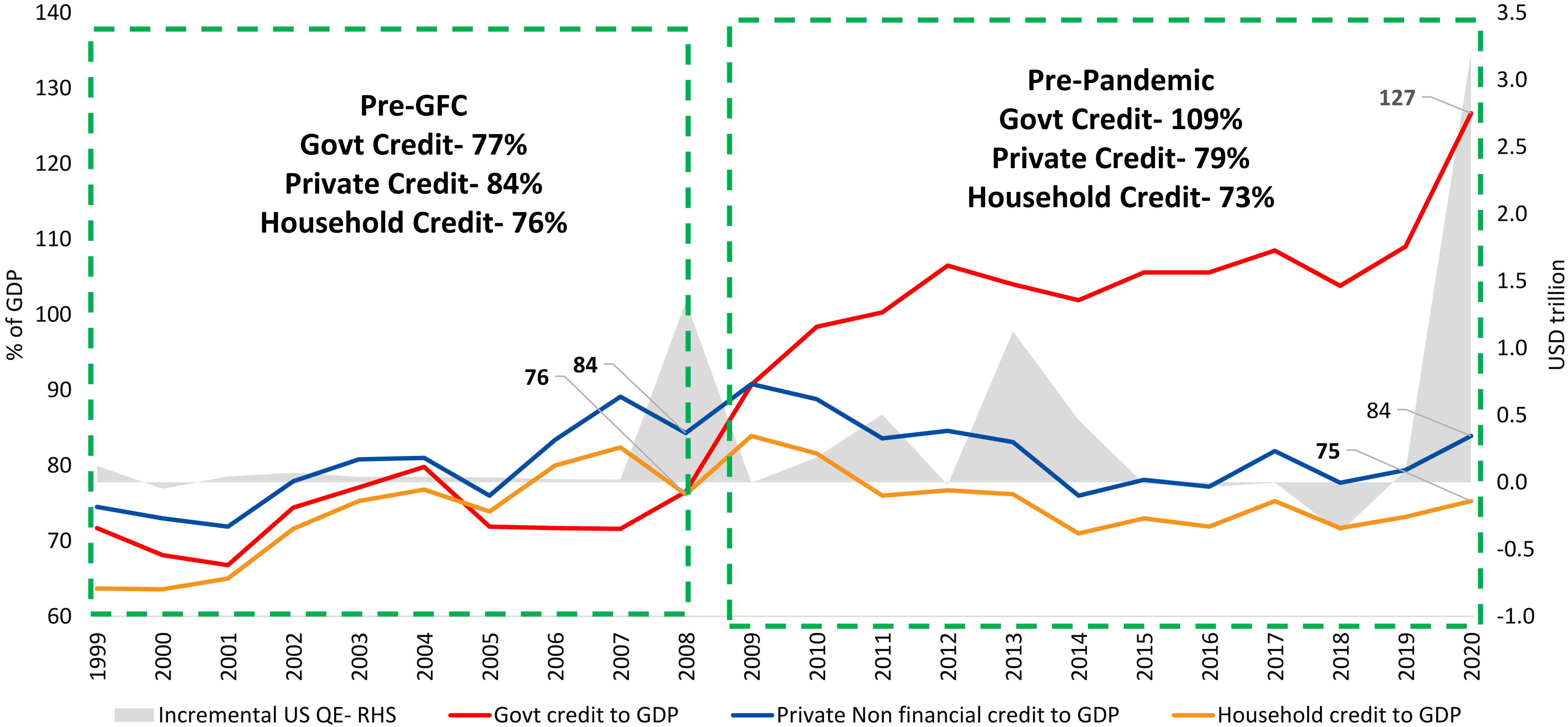
- **We believe that the possibility of a short term US Dollar rebound due to risk aversion should be utilized to add to Gold investments. We believe Gold prices can move towards 2600 to 2800 over the next few years. We suggest buying Gold now and on declines to $1750 / ounce**

High Government Debt + Unlimited QE = Dollar Debasement?

An unprecedented QE, to effectively keep the rates low and bail out high Government debt, creates a rationale for fiat currency debasement while the growth is expected to be low.

Appetite For QE is to Effectively Bail Out Government Debt

While the QE has been unprecedented, the credit picture is entirely different

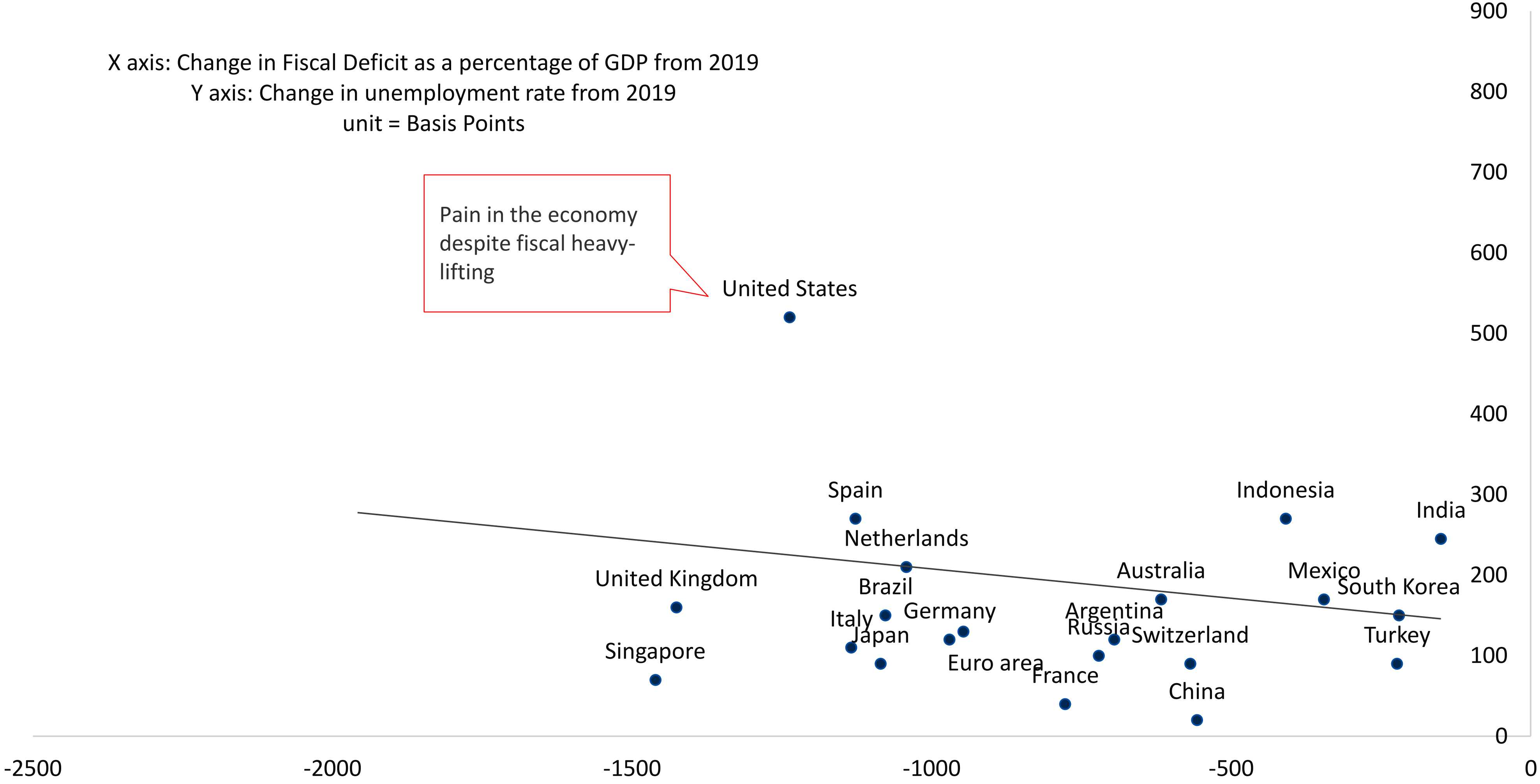


**credit numbers are for Advanced Economies*

Source: Bloomberg, Edelweiss Professional Investor Research

While The Impact on Growth is Limited

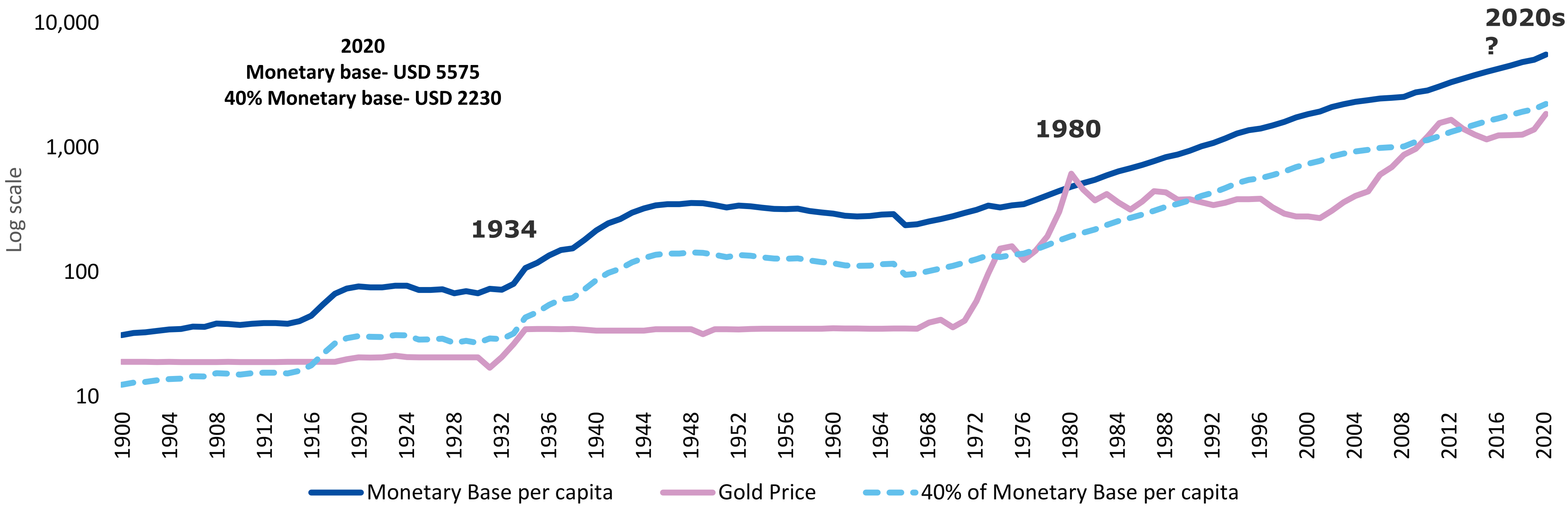
US has seen the highest fiscal increase but least impact on growth



Source: IMF, Bloomberg, Edelweiss Professional Investor Research

Investors Should Watch Out For Dollar Debasement

Approximately every 50 years, gold gets repriced upwards to account for fiat currency debasement

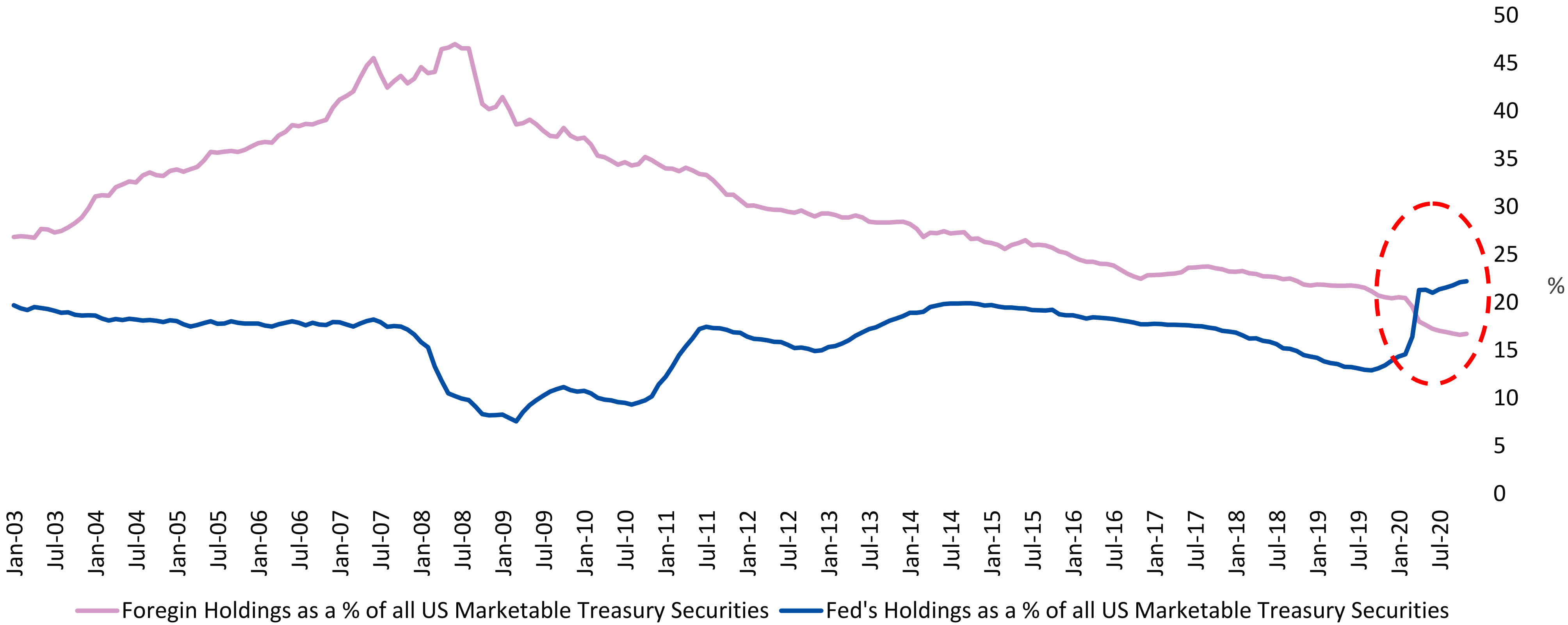


Source: St. Louis FRED, Bloomberg, Edelweiss Professional Investor Research

- With record global debt and MMT in place, there is more certainty that it is about time that Gold will reprice itself to account for dollar debasement. When faith in the modern monetary system is shaken, there is a tendency to shift towards hard assets, probably justifying why Central Banks across the globe have been net buyers of Gold bullions since the GFC

Fed is Now the 'Buyer' of Last Resort

Fed's share of holdings are now the highest in two decades

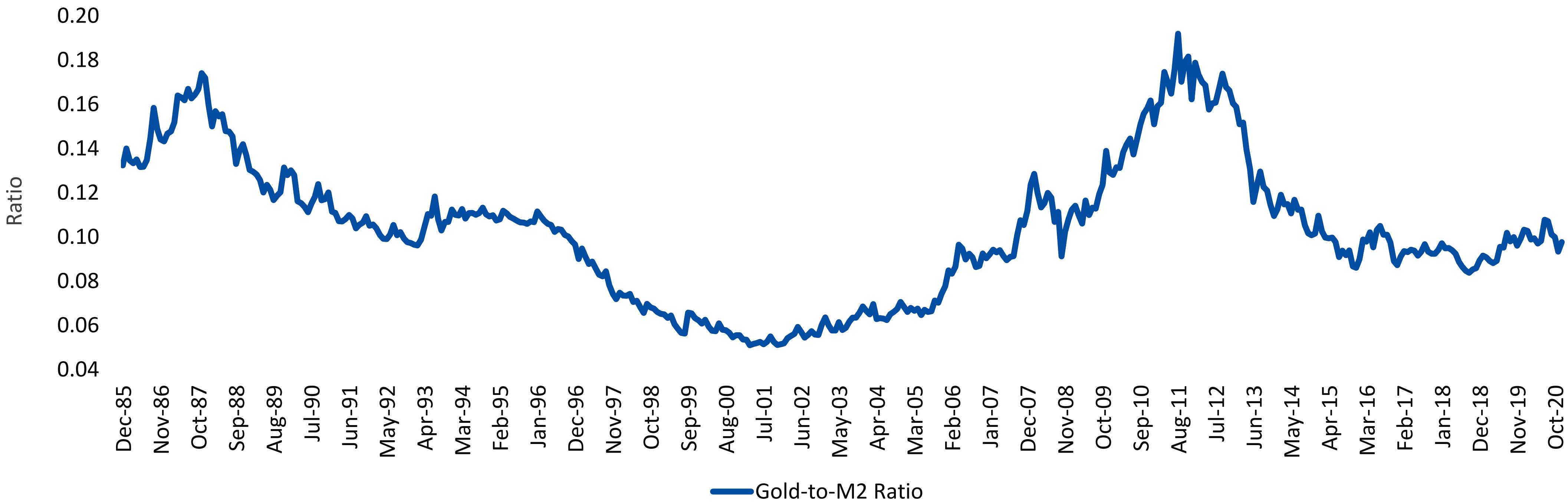


Source: Bloomberg, Edelweiss Professional Investor Research

- The fed has mopped up most of the debt while the demand otherwise remains sluggish, creating further rationale for fiat currency debasement.

Gold is Fairly Undervalued Relative to The Increase in Money Supply

Gold to money stock ratio is fairly low and is set to see an upside



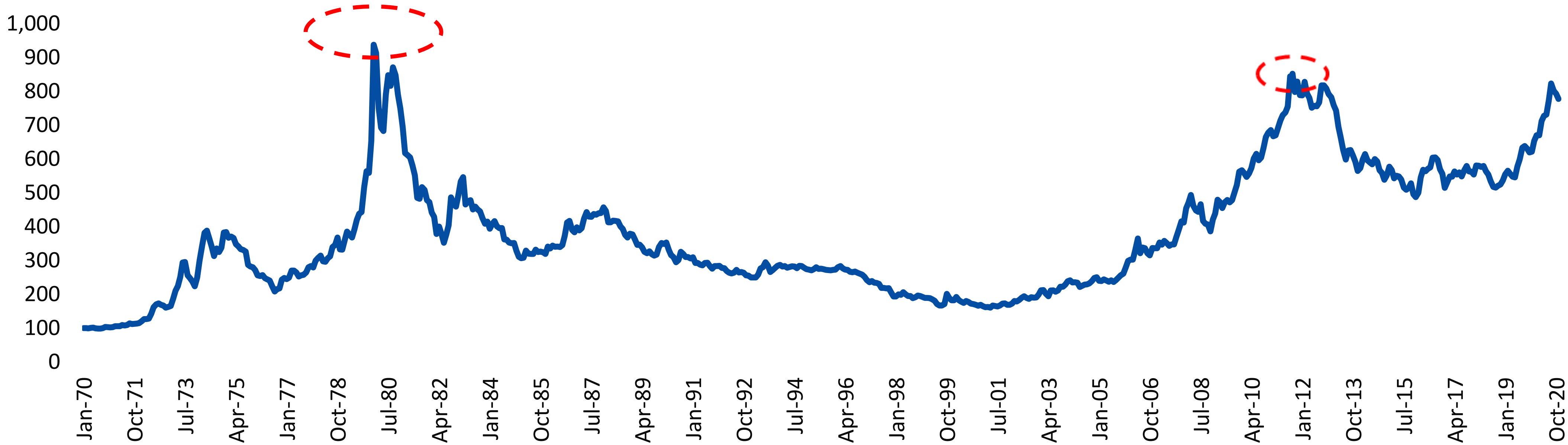
Source: St. Louis FRED, Bloomberg, Edelweiss Professional Investor Research

- While Gold has seen an uptick from increase in money supply, the current ratio is much lower than historic highs and points to a further upside.

Real Gold Prices Have Been Higher

While nominal Gold prices are at record highs, real Gold prices have been higher

Inflation Adjusted Gold Index (Base = Jan 70)



Source: St. Louis FRED, Edelweiss Professional Investor Research

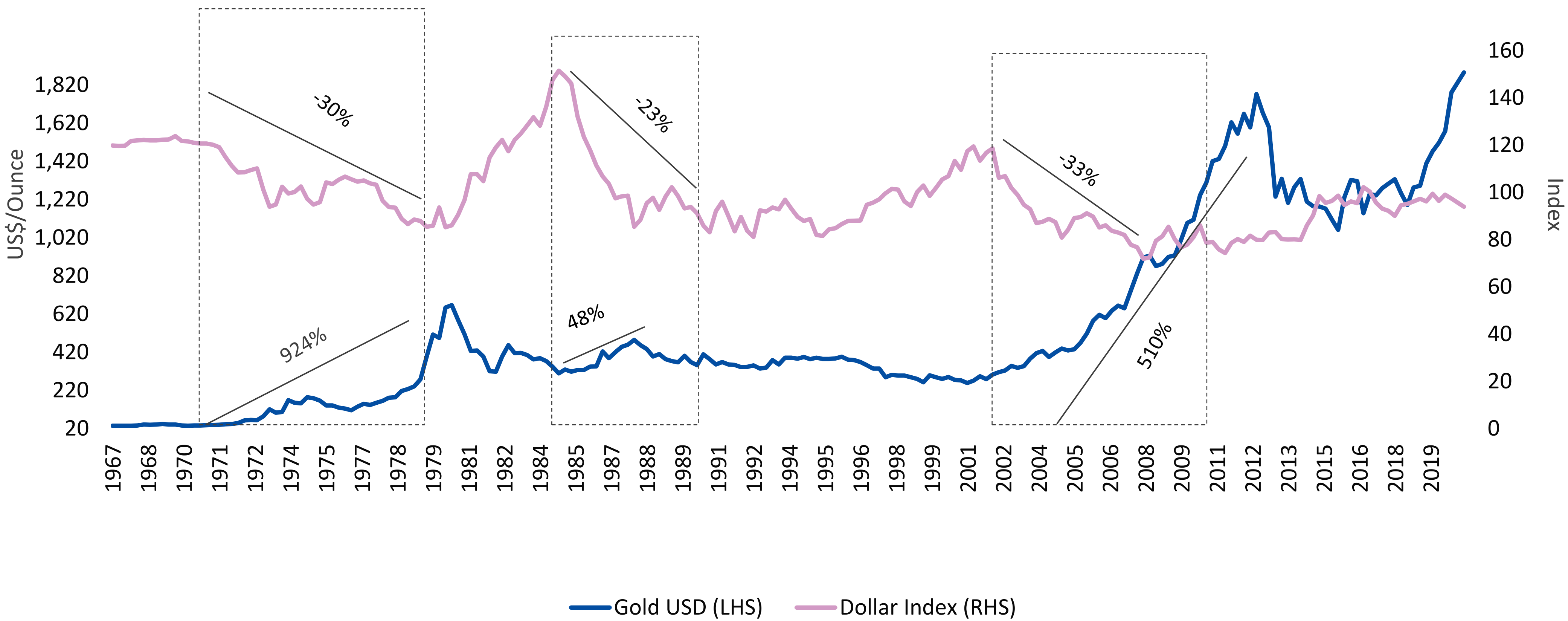
- **Real gold prices are pointing at further upside**

US Dollar to trend downwards

After an immediate bounce, US dollar will trend downwards leading to an upside in Gold prices

Gold Prices Will Gain Asymmetrically From Dollar Weakness

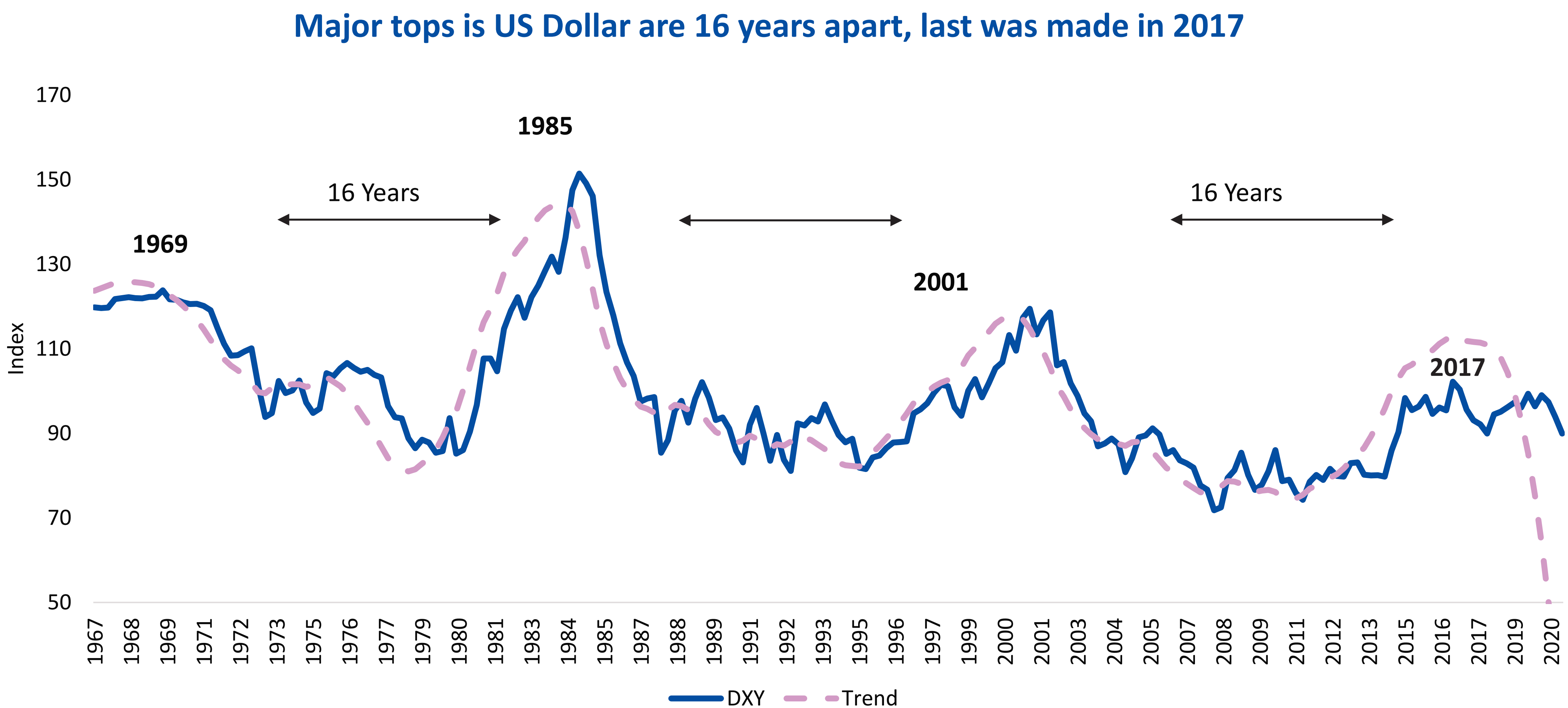
Historically, for every 10% dip DXY, Gold Prices go up by 15%



Source: Bloomberg, Edelweiss Professional Investor Research

US Dollar Index is likely to remain softer after an rebound in H12021. Moreover the worldwide currency debasement should favour Gold prices across countries, including India.

A Short Term Dollar Rebound But a Long Term Weakness Ahead

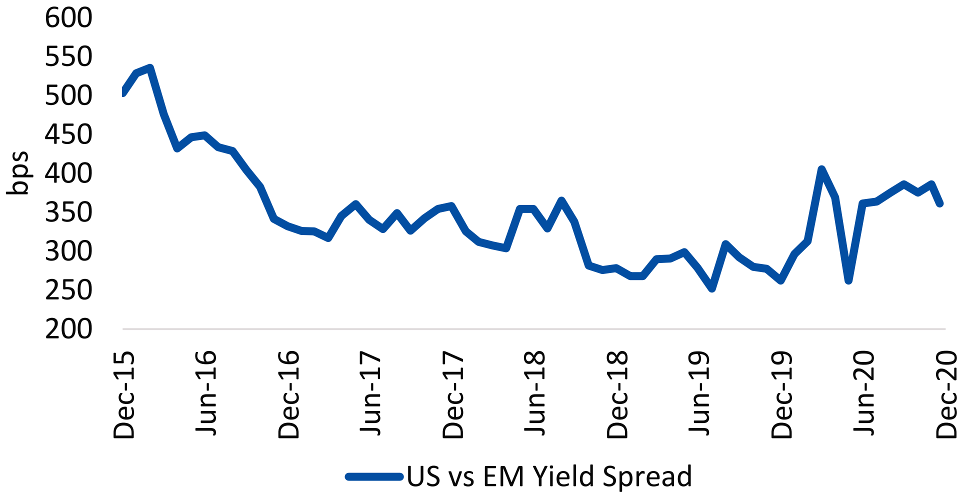


Source: Bloomberg, Edelweiss Professional Investor Research

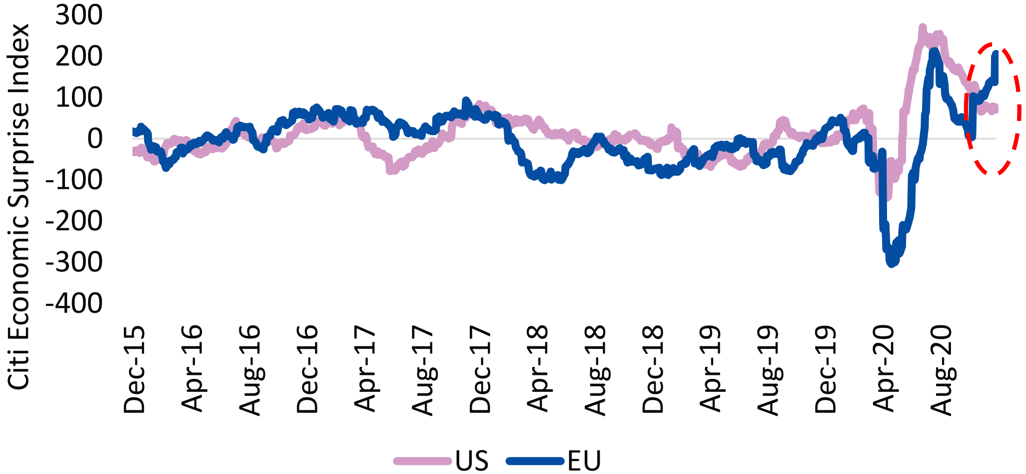
The Dollar weakness that is yet to play out will reflect in further upside to Gold prices. Risk aversion and rebound in US Dollar should be utilized to add to Gold positions at lower levels.

Multiple Factors Are Aligning For Dollar Weakness Ahead

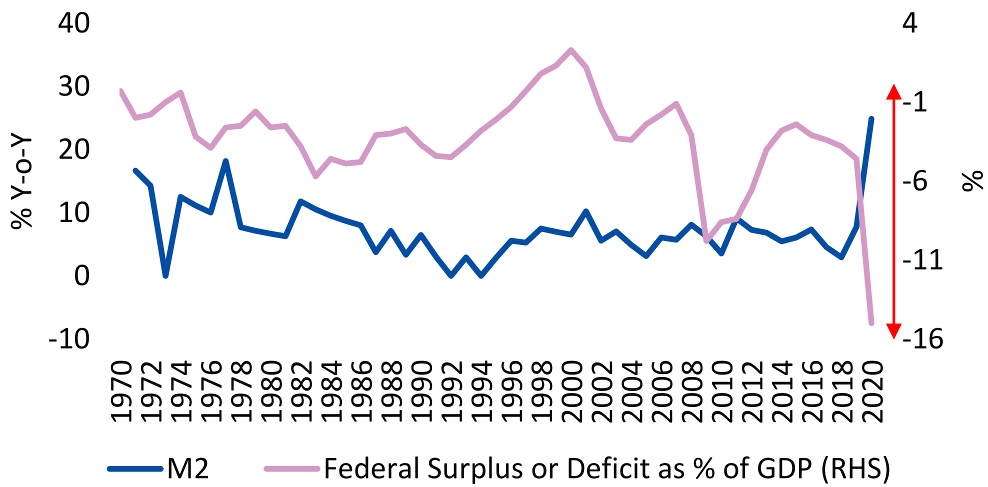
US and EM yield spread is widening…



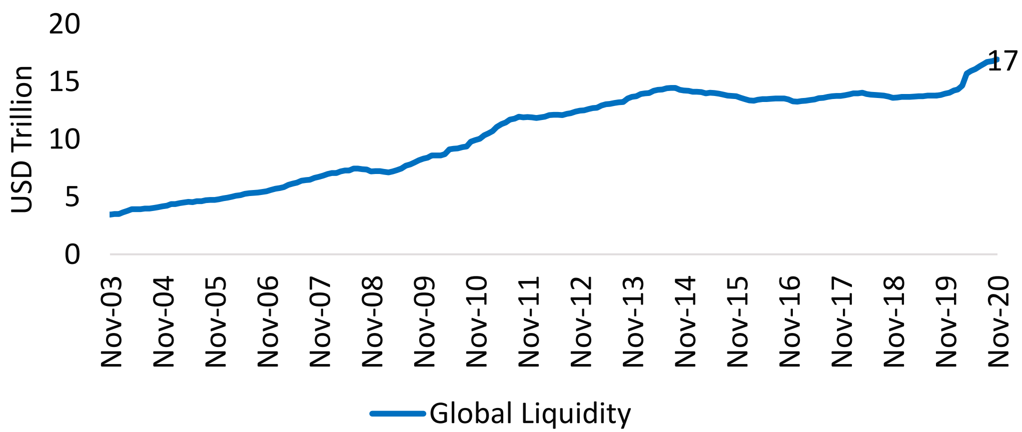
Economic surprises are faring better in EU



Modern Monetary Theory is in play..



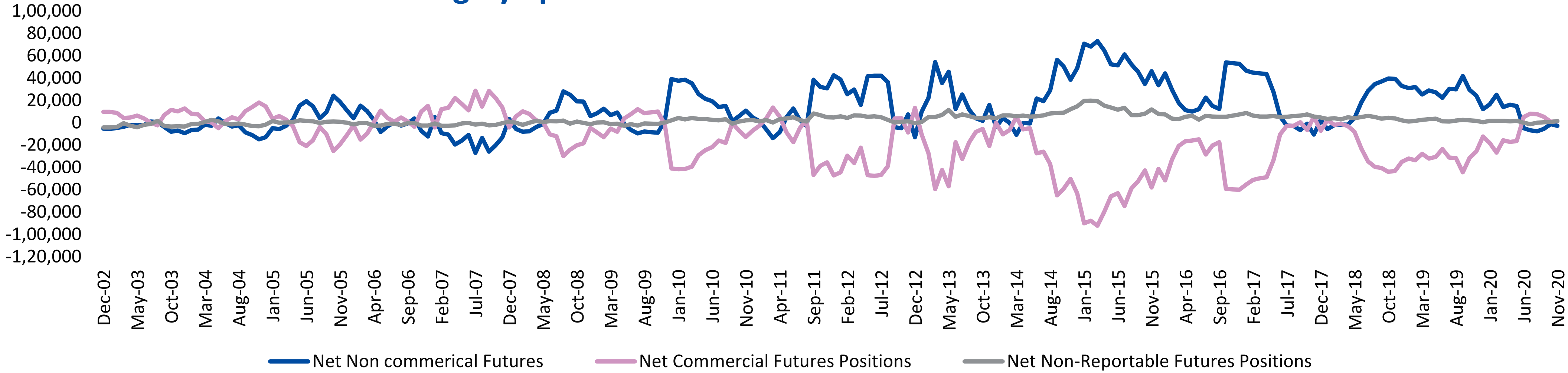
..Global Money Supply is making fresh highs

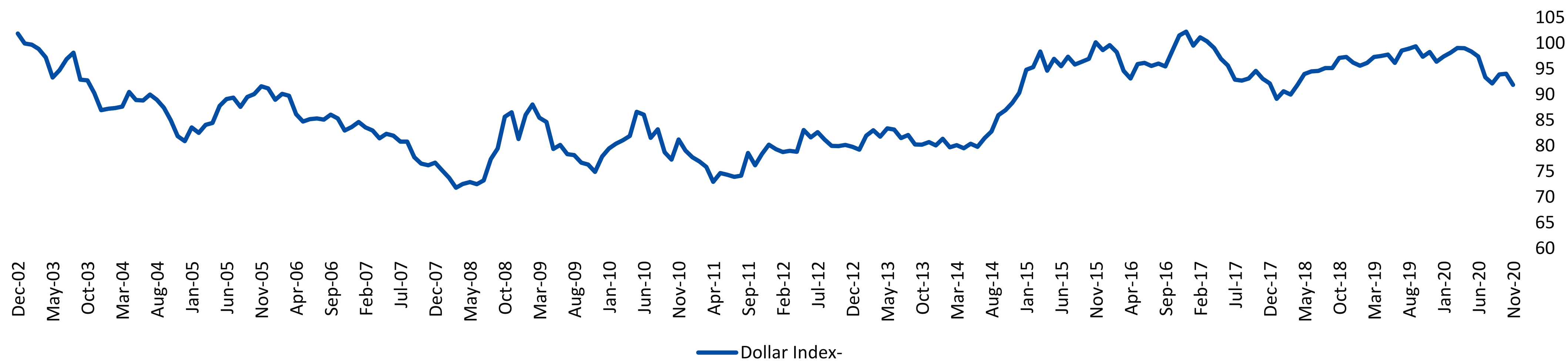


Source: St. Louis FRED, Bloomberg, Edelweiss Professional Investor Research

A Short Term Dollar Rebound Can Give Opportunity For Buying Gold

US Dollar Positioning By Speculators Indicates Short Term Exhaustion And A Rebound



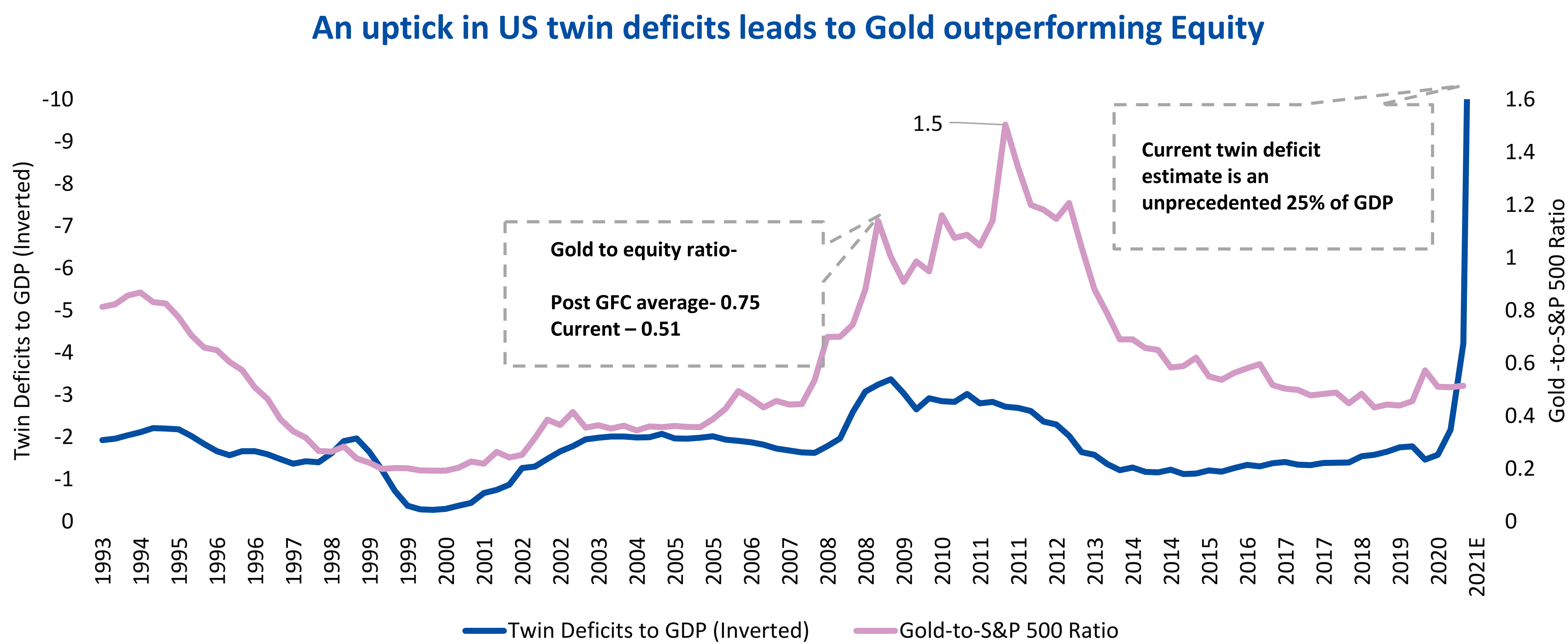


Source: Bloomberg, Edelweiss Professional Investor Research

Cross asset class points at potential for Gold

While equities and debt are significantly overvalued, it is Gold’s turn to shine.

The Uptick in Twin Deficits Indicates Gold's Outperformance

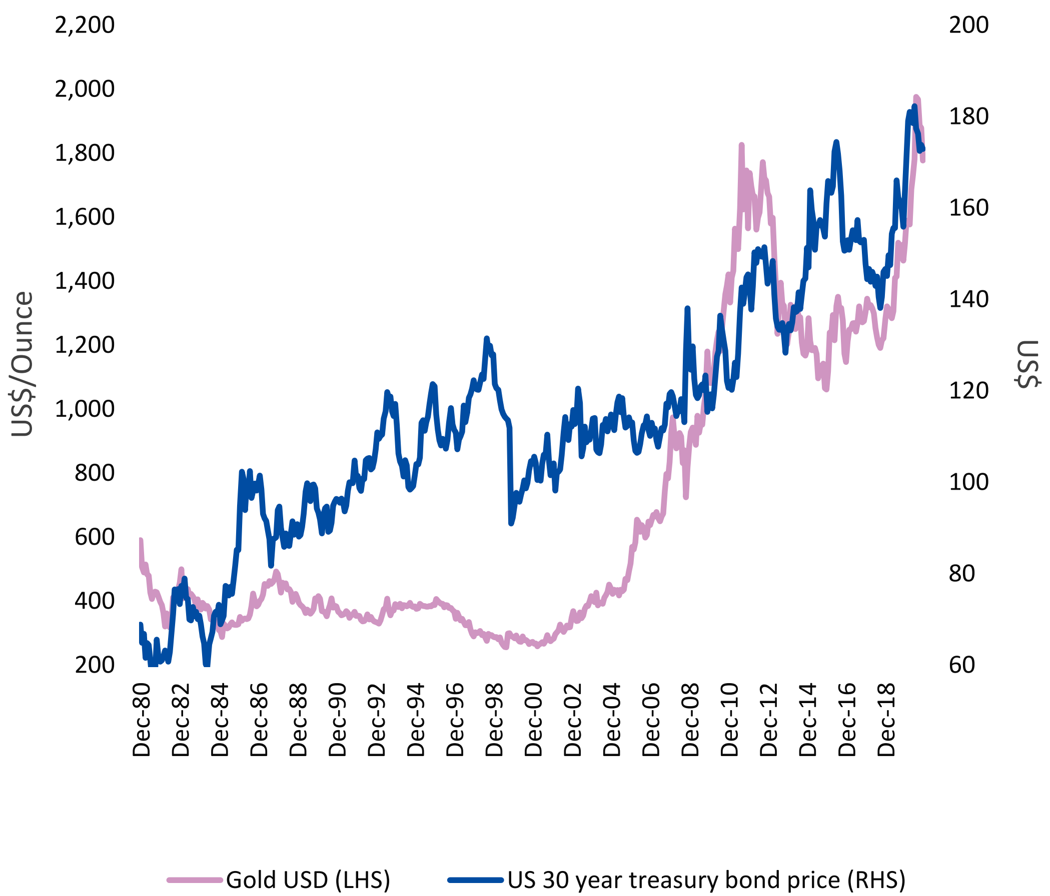


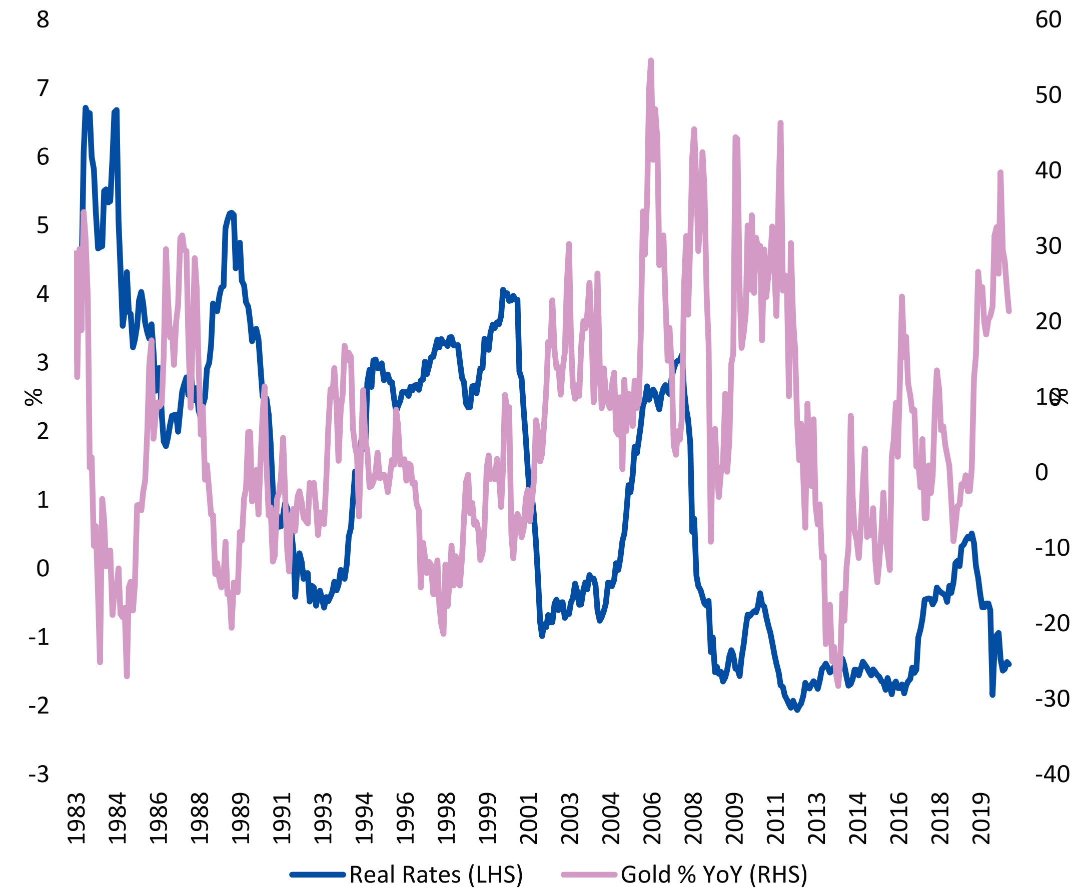
Source: St. Louis FRED, Bloomberg, Edelweiss Professional Investor Research

Gold has done well in time of fiscal easing and more so when is it coupled with a current account deficits widening. This year will be historic in taking the twin deficits to the unprecedented 25% of GDP.

Gold Moves in Tandem With The Debt Market

Higher bond prices and lower rates from the QE will provide further support to Gold prices

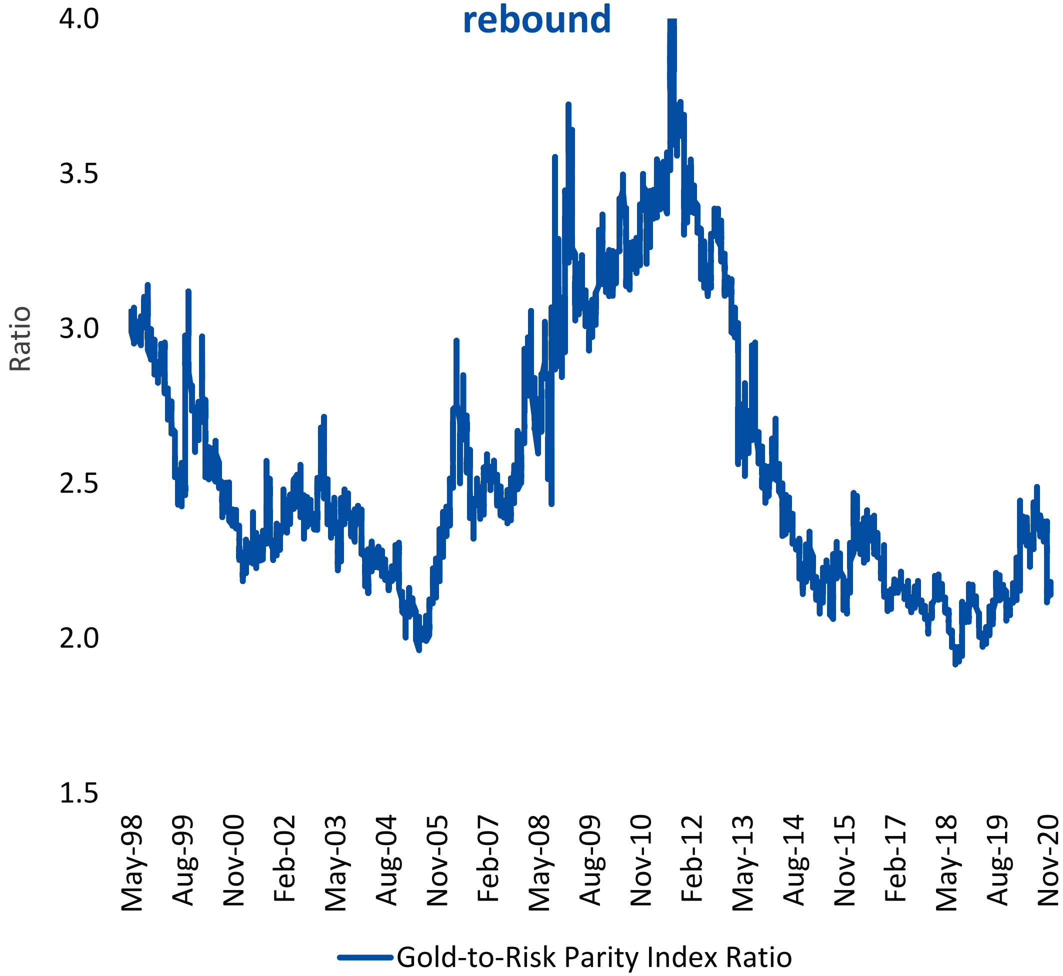




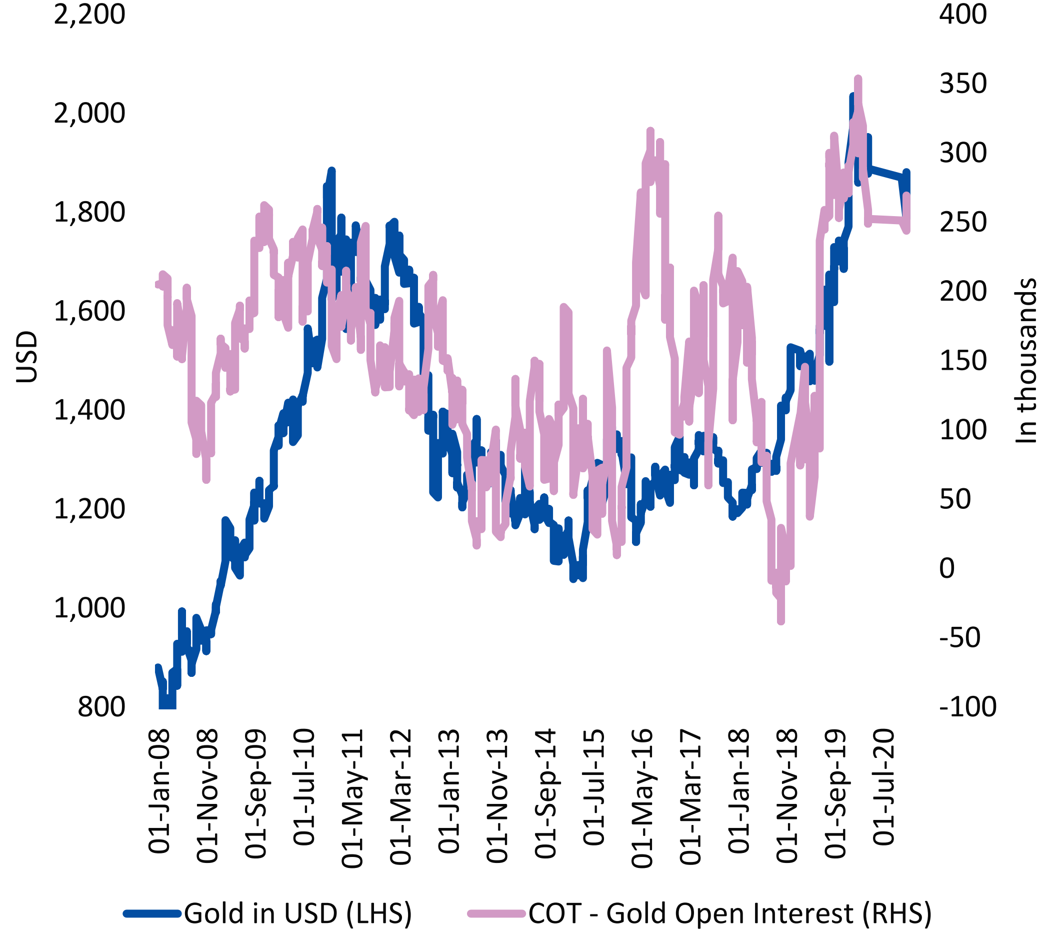
Source: Bloomberg, Edelweiss Professional Investor Research

Risk Ratios And Open Interest Are Indicating Bullish Formations

Gold to Risk Parity ratio has been trending downwards since 2011 but after recent double bottom is set to rebound



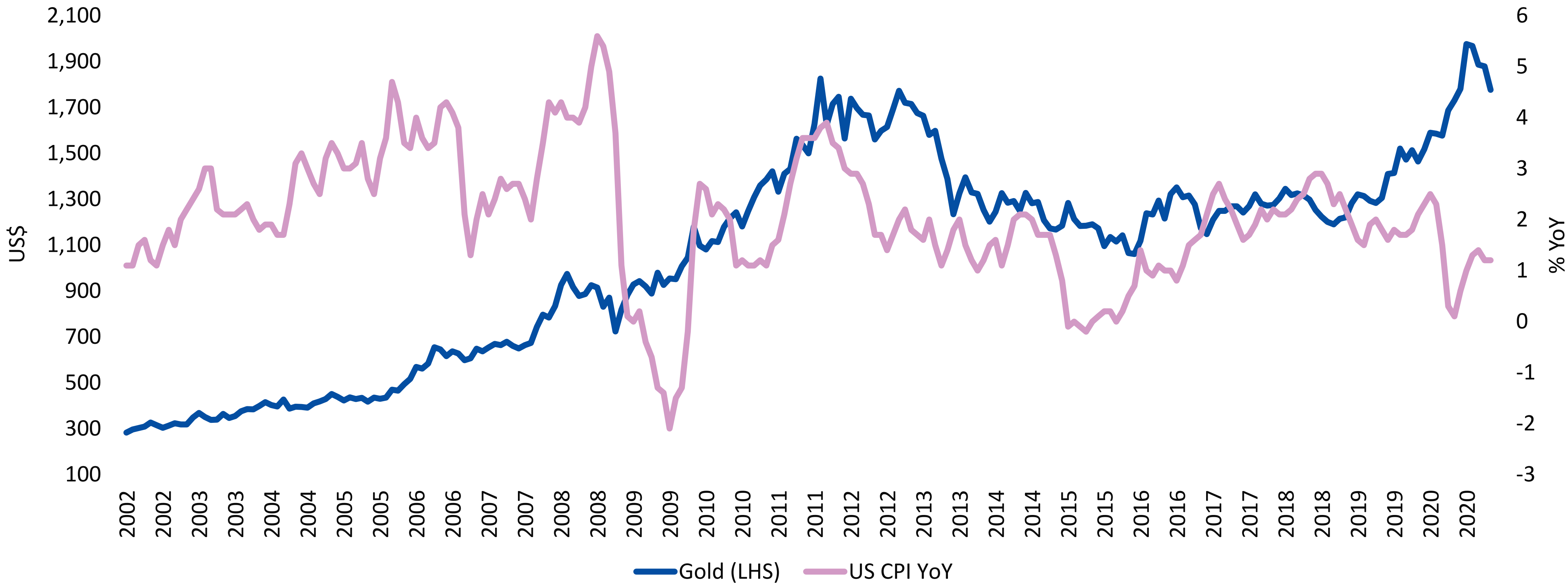
Open Interest has also risen upwards



Source: Bloomberg, Edelweiss Professional Investor Research

Gold Has Recently Done Well in Low Interest Scenario

Gold's run seems to have little correlation with inflation recently



Source: Bloomberg, Edelweiss Professional Investor Research

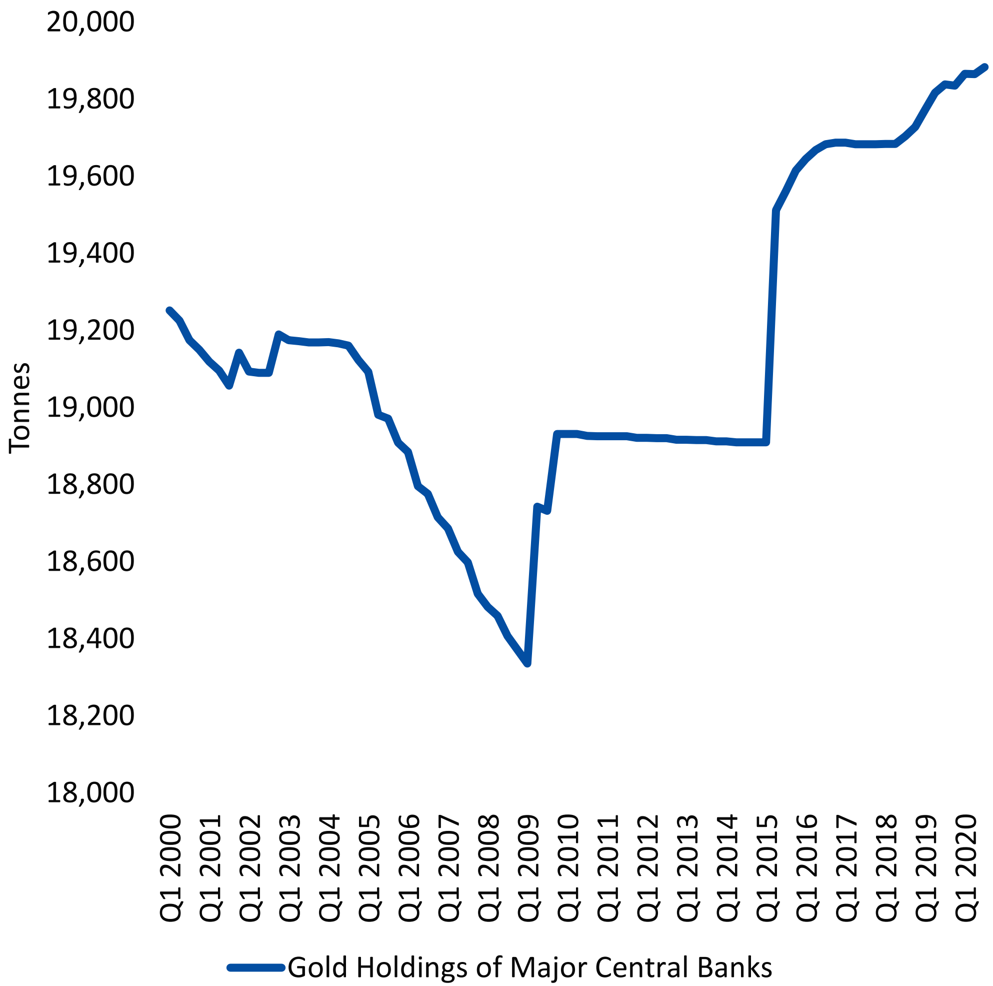
- While our base hypothesis remains that higher QE but lower growth is unlikely to sustainably ignite inflationary pressures, any uptick will rather play in Gold's favour.

Gold Fundamentals Are Well Aligned

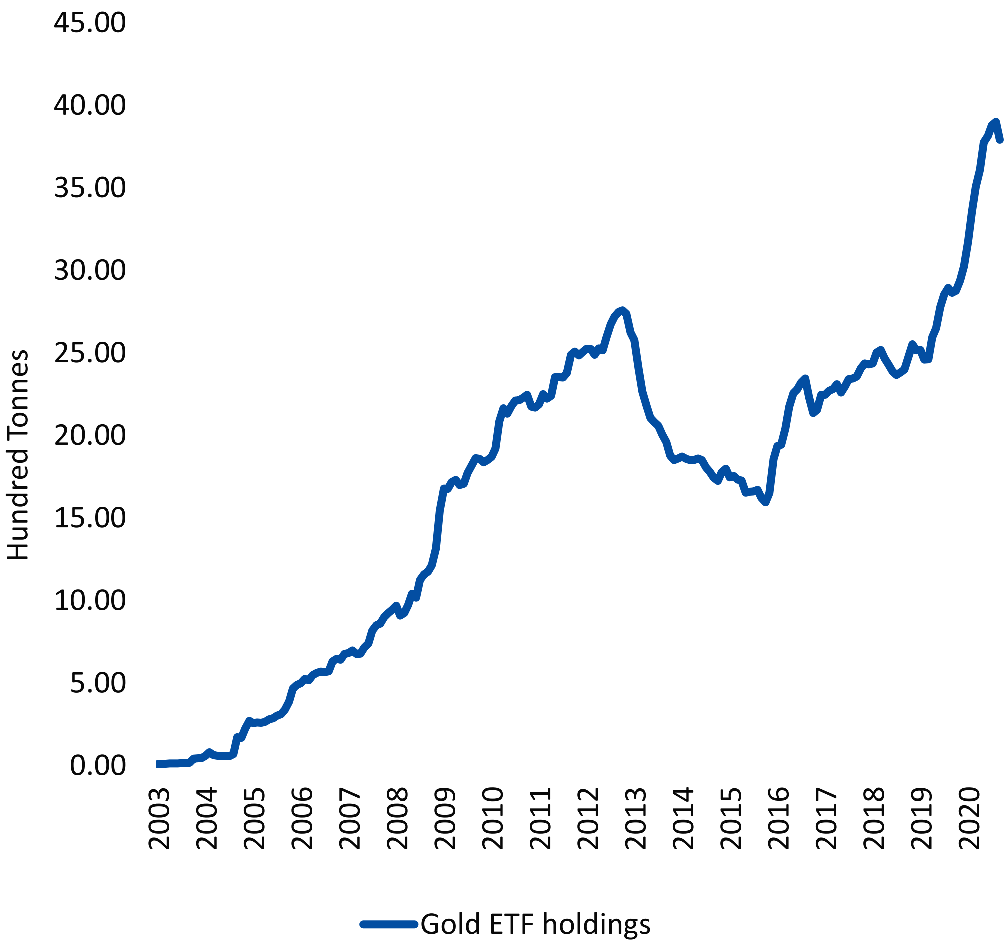
Gold has the demand support while supply is unlikely to substantially go up. Coupled with mining clock, there's significant upside on cards.

There is a Demand Support For Gold

Central Banks' holding for Gold is at record high…



..and so is investment demand



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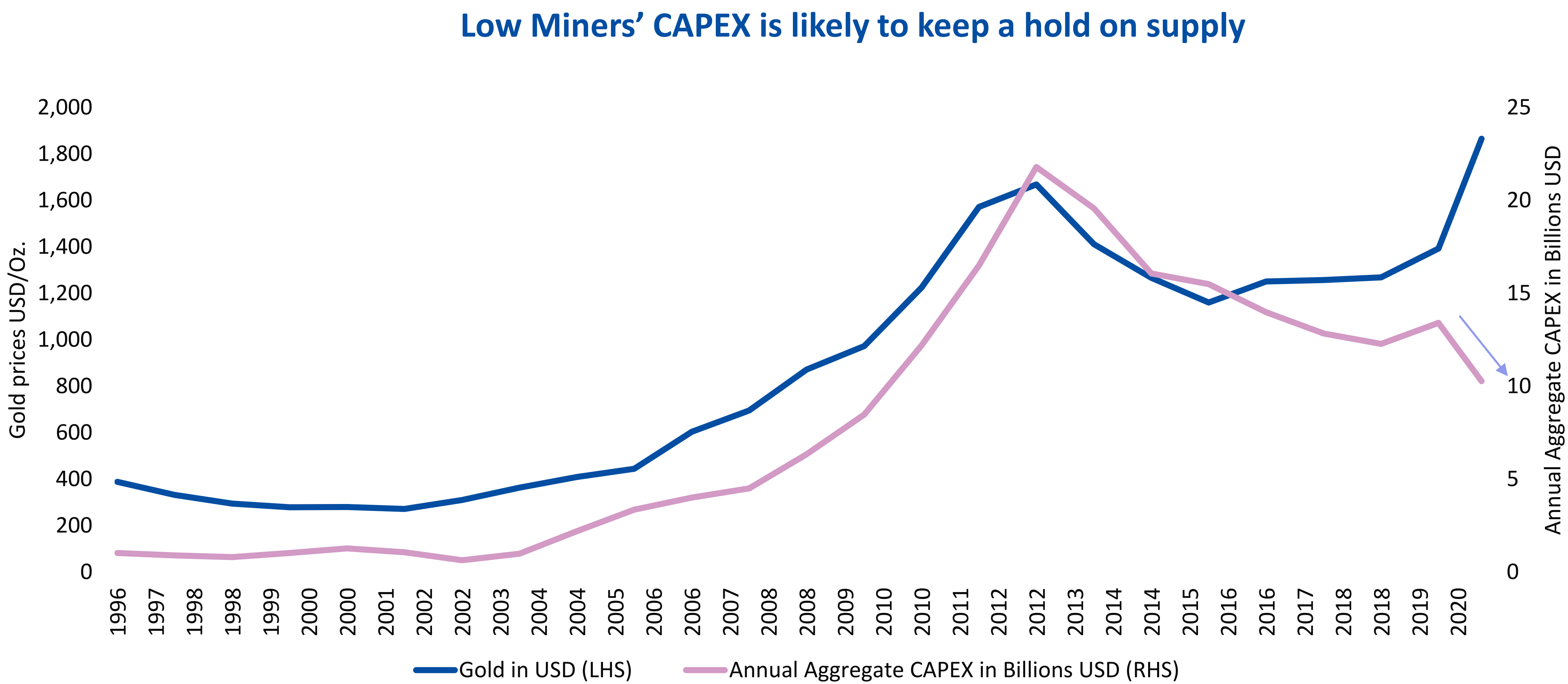
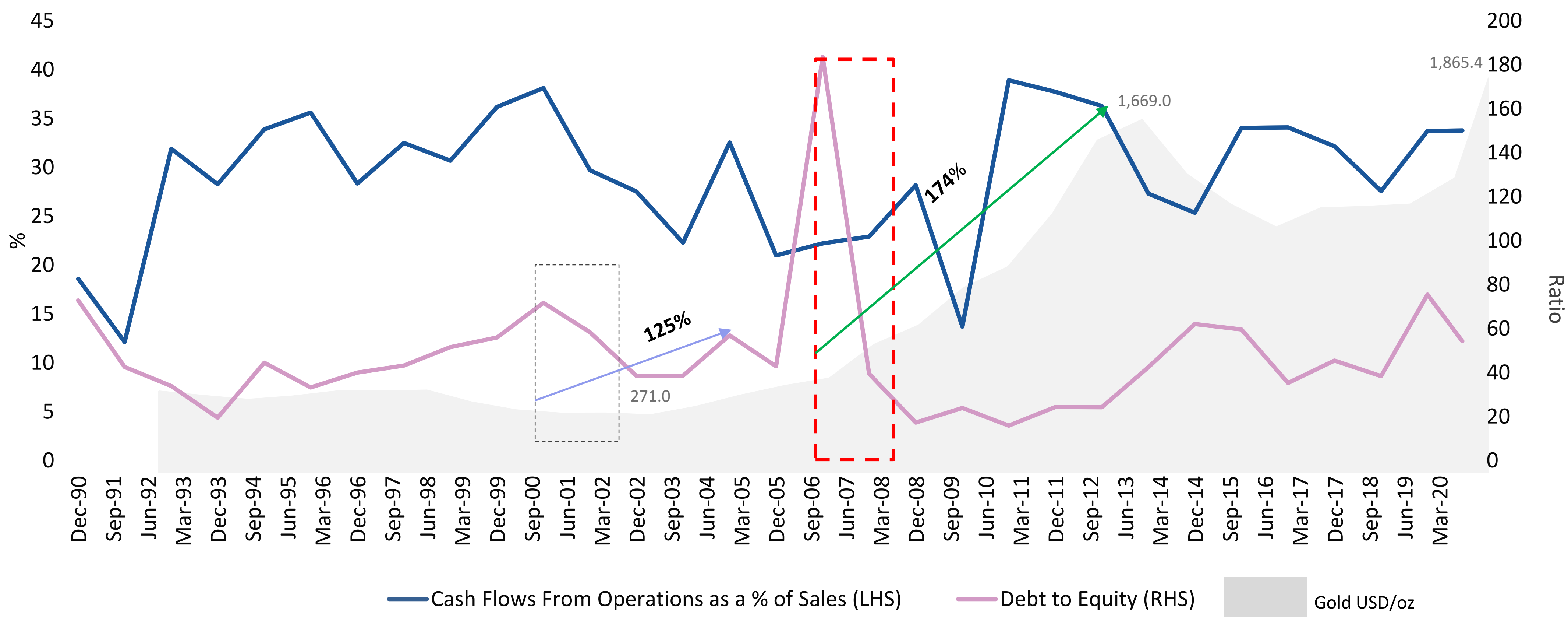
While Supply is Unlikely to Go Up



Source: Bloomberg, Edelweiss Professional Investor Research

‘Mining Clock’ Has Turned Favourably

The cash flow has jumped while the deleveraging is in place



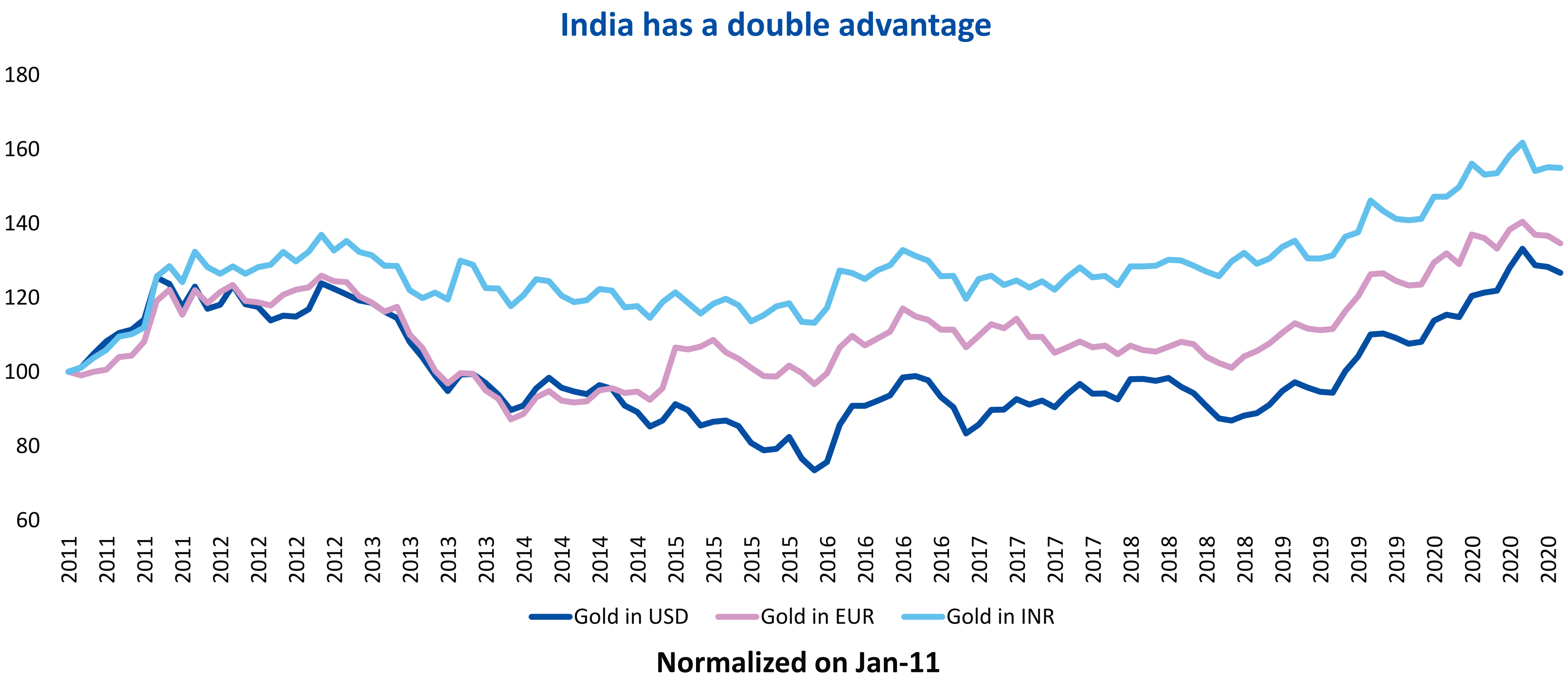
Source: Bloomberg, Edelweiss Professional Investor Research

Mining clock indicates the cyclical point based on the financials of corporates, and turn in leveraging cycle coupled with increase in cash flows, point at an upside in the Gold prices

Gold in INR is a win-win

Gold in Rupee terms will benefit from both currency depreciation and uptick in dollar prices- as has been the case in past

Gold in INR Has Historically Outperformed



Source: Bloomberg, Edelweiss Professional Investor Research

Owing to weaker currency, Gold in INR has historically outperformed.

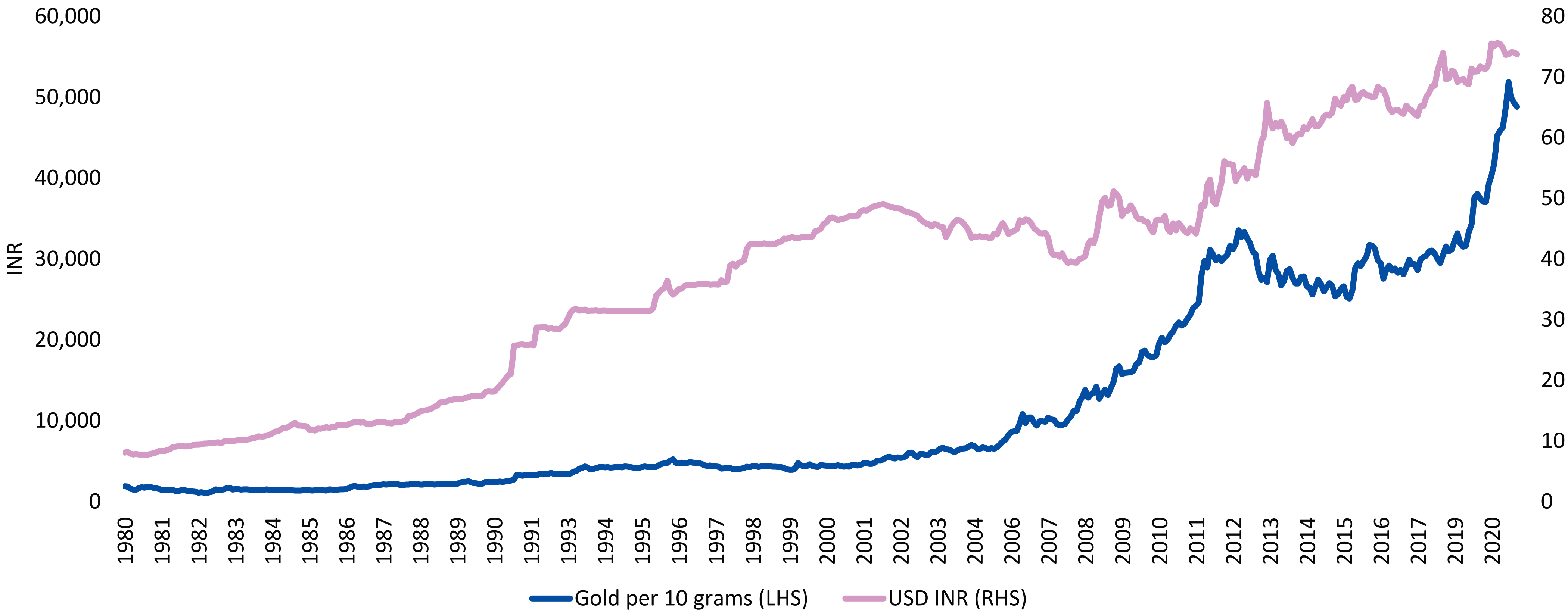
In Real Terms, Gold is Yet to Reach Its Highs

Adjusted for inflation, Gold has not surpassed its 2011 highs in USD and INR terms

Source: Bloomberg, Edelweiss Professional Investor Research

Lower Inflation, Weaker Currency Ahead?

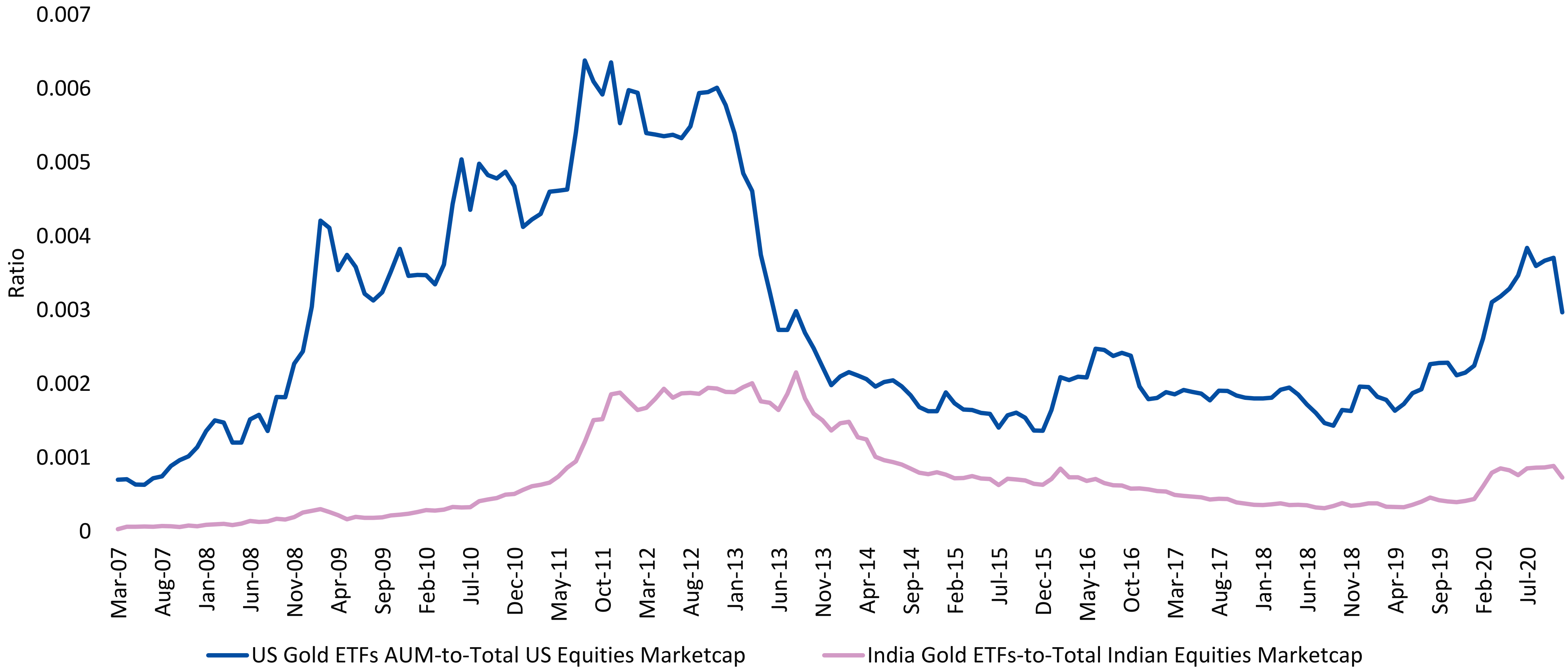
Indian inflation has started to trend downwards, coupled with high REER and widening trade deficit could lead to weaker currency



Source: Bloomberg, Edelweiss Professional Investor Research

India's Gold ETF Market is Underpenetrated But Growing

Flows to Gold ETF could increase significantly from here



Source: Bloomberg, World Gold Council, Edelweiss Professional Investor Research

Strategy

- **Gold has entered a multi year bull run. Over the next few years our initial targets are placed at $2600 to 2800 per ounce.**
- **In H1 2021 we expect volatility, a US Dollar bounce back and an ideal opportunity to add to Gold positions.**
- **Gold should be bought at $1850 and half the positions below $1750 over the next few months. Since asset prices are fairly volatile we suggest investors should utilize this period to add to positions in a staggered manner.**
- **In India, investors can participate through variety of instruments. We suggest to allocate to Gold ETFs with corresponding US Dollar price strategy listed above.**
- **We expect Gold in INR to touch INR 70,000-75000 per 10 gm in the near term.**

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