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PRECIOUS METALS

RON WILLIAM PRESENTS HIS VIEWS ON THE GOLD MARKET AFTER ITS STEEP SLIDE FROM ALL-TIME HIGHS.

Gold remains bearish after its dramatic 20% price decline, which helped confirm the extreme overbought conditions (marked by DeMark™ indicators), perfectly timed into a key cycle peak, ahead of that all-important $2,000 glass-ceiling.

The "perfect storm" of bearish technical signals was magnified by the CME's recent 55% increase in margin requirements on COMEX futures contracts that helped squash the largest of gold-bug positions. A series of margin hikes (in a short timeframe at trend extremes) can lead to major highs (similar to silver's historic crash in late April which was precipitated by an 84% margin increase as it accelerated into its historic $50 level).

Figure 2 – A historical parallel to 2008, when gold tested its formidable psychological $1,000 level, which led to an 8-month price consolidation that exhibited a volatile 34% drawdown.

Source: Bloomberg Finance LP.

Figure 1 – Gold's daily chart with DeMark Signal and Key Trigger Levels

Source: Bloomberg Finance LP.

It may have also created a conundrum for academic experts that gold's capitulation still took place despite increased safe-haven flows after the Swiss National Bank's unprecedented intervention on the EUR/CHF rate and heightened worries on the European Union debt crisis.

The key lesson here is that despite gold's seductive "haven" qualities, investors are witnessing another exception to the rule, when gold can fall in value during periods of economic and political uncertainty. This is an important wakeup call to the financial community that gold, like every other market, is still governed by mass-psychology, which ultimately becomes overcrowded.

Moreover, the current macro bearish environment is rather similar to 2008, when gold tested its formidable psychological $1,000 level. Following a temporary price spike, the gold market embarked on an 8-month consolidation and lost up to 34% in value, before resuming its long-term uptrend. Back then and perhaps now, the primary driver was a big liquidity squeeze where investors and traders were forced to scale down their portfolios after a profitable bull run on popular "risk" markets.

In price terms, gold's latest 20% bearish slide is still worth less than the largest average drawdown measured since the start of the yellow metal's long-term bull market in 1999. There is heightened risk of a much larger decline if we confirm a weekly close beneath $1,600 and $1,534 (200-day moving average), which has not been breached in 3 years! A number of "bargain hunting" trend-followers will be watching this benchmark "line in the sand" for repeat support or a potential big squeeze lower.

Figure 3 – Gold's long-term bull-channel highlighting key cycle peaks.

Source: Bloomberg Finance LP.

Speculative liquidity flows are of concern after another peak that has triggered a test of a critical downside structural level. Over two years of sizeable long gold positions will be under threat if this area breaks down. This would place gold's bullish macro drivers temporarily on ice as the market shifts to a large technical unwinding of overcrowded positions.

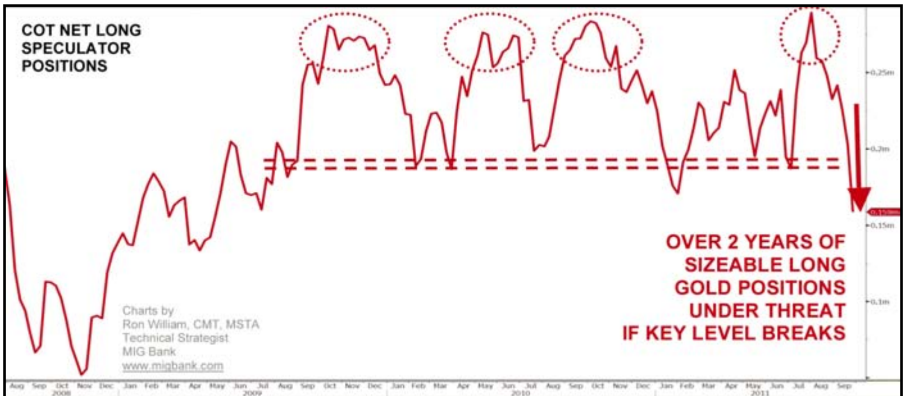

Figure 4 – Gold's COT NET Long Speculator positions

Source: Bloomberg Finance LP.

A sustained close beneath $1,530 would unlock a fast avalanche (wave IV) decline toward $1,300 with lower scope potential into the $1,040 to $1,000 zone (trend-channel floor-psychological). Remember this would still be consistent with gold's long-term bull-market cycle and offer a unique buying opportunity into its "grand-finale" rise that is likely to commence by mid-2012.

> "The U.S. dollar, which is in a polar opposite technical setup, may benefit from this domino flight to safety..."

Until then, growing economic and political turmoil will force investors to scramble for more attractive safe-havens. The world is running out of safe places to hide money with the Swiss authorities leading a currency war against the CHF haven status, Japan still vigilant of their strong JPY (around historic WWII levels) and commodity currencies mean reverting from trend extremes.

In a relatively weak beauty contest, the U.S. dollar, which is in a polar opposite technical setup, may benefit from this domino flight to safety effect, coupled with gold's potential decline and unwinding of global risk appetite. Investors will be forced elsewhere with capital always searching for the most attractive home (especially during uncertain times). Technical projections suggest the DXY may gain up to 30% from very oversold price conditions which are currently mean reverting from record net short liquidity flows and bearish sentiment extremes. **FJ**

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Figure 5 – U.S. Dollar Index long-term chart from 1980

Source: Bloomberg Finance LP.