2023 November Economic Update

Market Optimistic as Inflation Appears Under Control and Markets Expect Rate Rise Cycle to End

1. CPI Overview – Falling Energy Prices and Consumer Weakness Keep Inflation at Bay

	Dec-23		For reference only	
	MoM CPI	CPI YoY	High	Low
Sensitivity Forecast	-0.10%	2.99%	3.20%	2.66%
	0.00%	3.10%	3.30%	2.76%
	0.10%	3.20%	3.40%	2.86%
	0.20%	3.30%	3.51%	2.96%
	0.30%	3.41%	3.61%	3.07%
	0.40%	3.51%	3.71%	3.17%
	0.50%	3.61%	3.81%	3.27%
Base-case Scenario	**0.00%**	**3.10%**		

Earlier this month, the Bureau of Labour Statistics released the inflation data for October 2023. Year-on-year inflation was at 3.2%. This was sharply lower than 3.7%, which was the level in the previous two months.

A key factor in this decline was from falling energy prices as the price of oil fell from US$94 a barrel to below US$80. However, the continued rise in shelter costs increased by 0.3% for the month which partly offset the benefits of lower energy costs. That said, the cost of shelter rose less compared to the 0.6% spike in September.

Our prediction for inflation this month, due for release on 12th December, is for the month-on-month CPI to remain flat. This equates to 3.0%-3.1% year-on-year rise in the CPI. We expect the price of oil remains at these levels. Our research has shown that the MoM CPI rises by at most 0.1% when the price of crude oil drops by more than 5%, as you can see below:

	Period	Crude Oil Average Price	MoM %	MoM CPI	
2023	Nov	78.03	-8.70%	0.00%	**~estimated**
	Oct	85.47	-3.46%	0.00%	
	Sep	88.53	8.80%	0.40%	
	Aug	81.37	7.40%	0.60%	
	Jul	75.77	7.77%	0.20%	
	Jun	70.31	-1.91%	0.20%	
	May	71.67	-9.42%	0.10%	
	Apr	79.13	7.88%	0.40%	
	Mar	73.35	-4.78%	0.10%	
	Feb	77.03	-1.56%	0.40%	

Jan	78.25	2.18%	0.50%

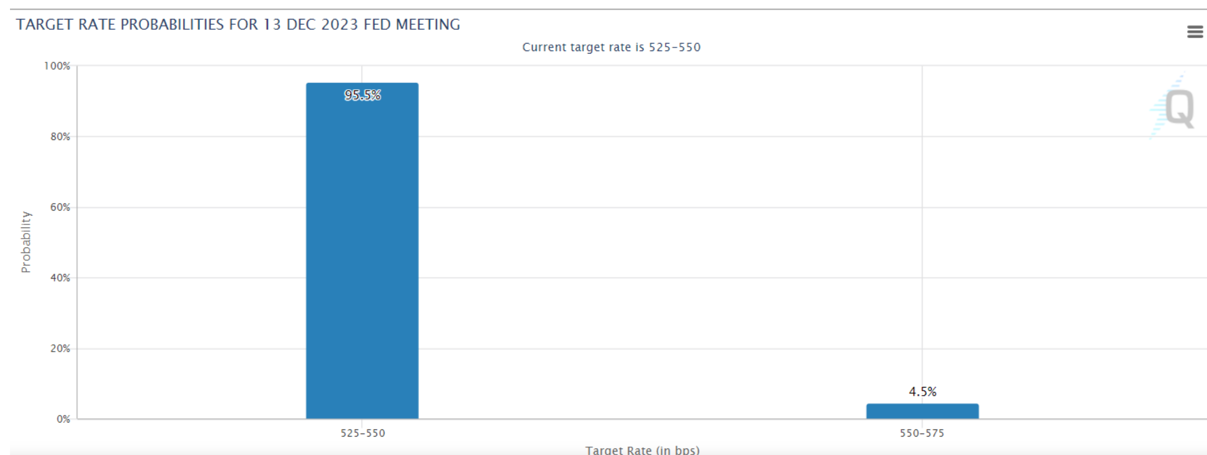
While this is a better outcome than what we saw for most of last year, it is not optimal given the pressures of rising living costs on the public. However, at such levels, we expect that the US Federal Reserve is less likely to see the need for further rate rises, even moving on timing its first rate cut.

For now, we see a drop in the year-on-year CPI from 3.7% to 3.2% as a good indicator that headline inflation is under control. We expect the headline CPI to stay around this level, even falling slightly in the near future.

However, we hold a different view regarding the core CPI. The US Federal Reserve tried to claim that core CPI is difficult to control as the price of oil plays a key role, something that the Federal Reserve notes it cannot control. Therefore, we expect that core CPI will remain elevated at 3.7%-4% for some time.

For this reason, the market expects that the Federal Reserve will likely choose to begin cutting rates in the second half of 2024, unless something drastic happens to the global financial markets beforehand.

The figure below shows the market's expectation for what the US Federal Reserve will do in the next scheduled meeting on 13th December 2023:



The most likely outcome is for the Federal Funds Rate to remain at 5.25-5.5% after this meeting, although we will focus our attention on the comments made in the press release.

2. Outlook on Gold and Crude Oil – 2023 December performance should improve as conditions are more favourable for gold mining companies

We have updated our website now to include price charts for gold, silver, gold stock indices and other key metrics.

You can find these on our website at https://goldfund.com.au/price-charts.

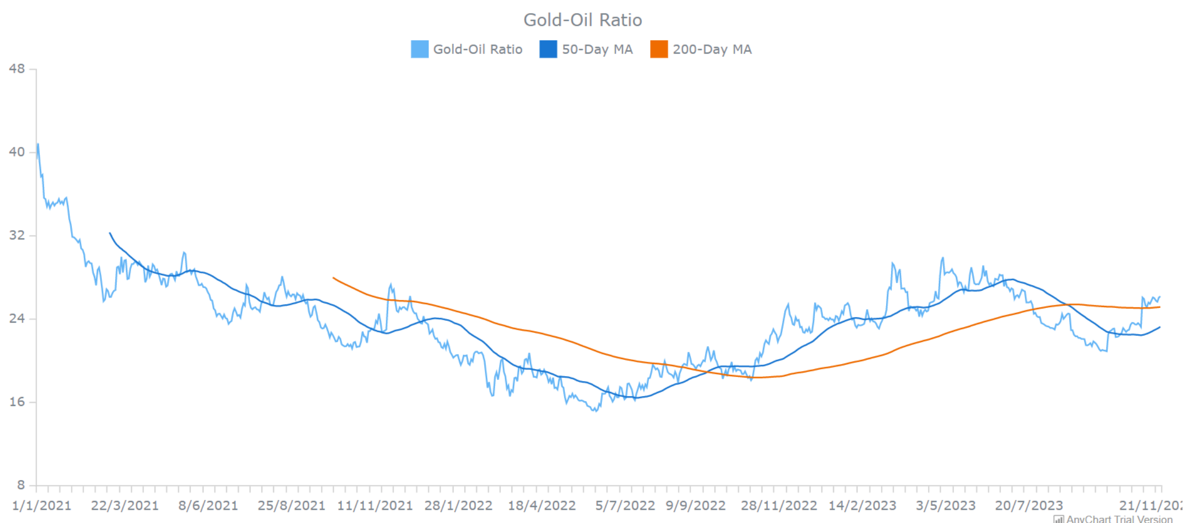
Here is our commentary regarding the recent performance and outlook on gold and crude oil, and how this will affect gold mining companies:

- **Gold**. Technically, gold remains one of the strongest hedge to inflation over the past year. The 200-day moving average currently sits at US$1,930 an ounce. The good news is that gold has managed to trade above this level consistently in the past half a year.

  For the 2023 December quarter, we project that gold will likely trade within the US$1,930 – $2,100 level. This is because the market currently expects the US Federal Reserve to keep rates steady, with a possibility of one more rate rise. This is what drives the US Dollar Index to remain relatively strong, thus holding gold back.

  We expect a strong bull run for gold mining companies to occur once gold price breaks $2,100. This will likely happen if the Federal Reserve cuts rates earlier than expected or a market panic sparks a flight to safety to gold.

- **Crude Oil**. The price of crude oil fell significantly in October after staging a bullish run for several months from June to September. The rising price of oil was a major stumbling block for gold producers seeking to ramp up operations to pre-2020 levels. With oil trading now in the US$75-80 range, operating conditions are likely to improve for gold producers this quarter. We do not expect, however, that oil will fall below US$70 at this stage.



- **Gold-Oil Ratio.** We base our predictions on how gold producers will perform in the next two quarters using this ratio. Our research has proven this is an effective leading indicator. The gold-oil ratio has staged a significant improvement from below 21 at the end of September to over 25 at the start of November as oil suddenly dropped below US$80. At such levels, we are expecting gold producers to operate more profitably and will report this in the 2023 December quarter. If this trend continues, it might even flow through to the 2024 March quarter.

3. ASX Gold Index – Our recommendation is to ACCUMULATE

- **ASX Gold Index**. Favourable moves in both the price of gold and crude oil are setting up gold producers to deliver better results in the coming quarters. This will help bring about a rally in this space, which has experienced a bearish trend since April.

  Currently, we see that the market has not priced these in. The ASX Gold Index currently trades at around 6,500-7,000 points, which is around 15% higher from its recent lows. With the gold-oil ratio rising by 25% since September, this should set the scene for the ASX Gold Index to rise above the 7,000 point resistance level and trade at 7,300 points into early 2024. All this depends on gold producers announcing marked improvements in their production, costs and cashflow generation.

To conclude, here are our key findings and recommendations:

- **December year-on-year headline CPI figures – 3.0%-3.1% (70% probability) and 3.2% (30% probability)**
- **Expect at most one rate rise to come, though this could change if the economy deteriorates quickly.**
- **Gold likely to trade between US$1,930-2,100 an ounce in the coming months. A break above US$2,100 could spark a major gold stock bull market.**
- **Crude oil trading at current levels of US$70-80 a barrel is favourable to gold producers. However, we do not expect the price to drop below US$70 at this stage.**
- **Accumulate ASX gold producers given current favourable conditions, which the market has not fully priced in.**