Market Insight

Gold Outlook to Q4 2024: From one high to the next

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Despite the lack of institutional investor interest in the metal, gold had a fantastic year in 2023, reaching a new high of $2078/oz on the London Bullion Market Association (LBMA) afternoon fixing on 28 December 2023 and in terms of intra-day prices reached an even higher $2135/oz on 4 December 2023. Spot gold prices closed the year up 14.6% (LBMA afternoon fixing, 29 December 2022 – 29 December 2023). While reaching a nominal high, in real terms (netting off inflation) gold is still 15% below the August 2020 level (that marked the previous nominal high). Gold significantly outperformed US Government Bonds (up 4.0% over the same period based on the Bloomberg US Treasury Index). In contrast to 2022, bond and US Dollar headwinds eased toward the end of the year, allowing the metal to gain.

Speculative positioning in the gold futures went through a wide range, topping at 226k contracts net long in May 2023 and falling to just 60k contracts net long in October 2023. However, positioning ended the year close to its intra-year high at 217k contracts, indicating that investor sentiment toward the metal is improving markedly alongside the price rally. Meanwhile, central bank demand for the metal looked like it was on track to match the 2022 all-time highs (latest data from World Gold Council shows that central banks bought 799.6 tonnes in the first three quarters of 2023, compared to 699.8 tonnes in the first three quarters of 2022). As we look to 2024, further compression in bond yields and a softening US Dollar will likely override the slowing support from inflation, driving gold to another new high.

Many metal prices rallied in late December 2023 on hopes that the Federal Reserve will start cutting rates as early as March 2024. However, the release of the US Federal Reserve Open Market Committee minutes from the 12-13 December meeting in early January 2024 showed that the central bank is not in as much of a hurry as the market thought. All the US Dollar depreciation from 18 December 2023 to 27 December 2023 has been reversed in the first week of 2024. The bond market is now pricing in a cut by May 2024, rather than March.

Looking at economists' median expectations for 2024, the first rate cuts are likely to be delivered in Q2 2024 and we could see a total of 100 bps reduction by the year end. However, the resilience of the US economy continues to surprise most analysts, with latest job numbers looking very robust and unemployment figures falling toward the end of 2023, after a small increase in the first eight months of the year.

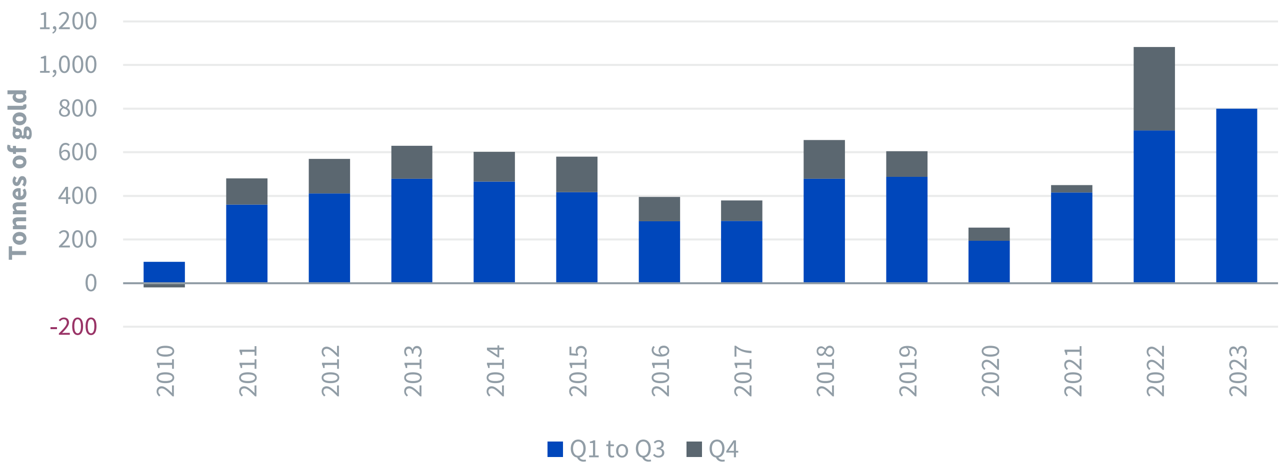
Against this backdrop, the Federal Reserve may not offer forward guidance as quickly as the market has been hoping for in order to give itself maximum flexibility to respond to data as it becomes available.

As markets recalibrate, gold may lose some of the steam that it gathered in late 2023 and dip in Q1 2024. However, as rate cuts start to become communicated, gold will likely rally and as cuts are actually implemented gold could reach a new all-time new high of $2,210/oz by the end of the year.

Central bank demand for gold

Central bank demand for gold in 2022 was the strongest on record and in the first three quarters of 2023, that source of demand was on track to beat 2022 levels. Although high hurdles to beat, 2024 demand could be in the same region. Non-G7 countries are buying gold at a record pace to diversify their foreign exchange holdings. The events of 2022, when Russia's central bank assets in G7 currencies were frozen, spooked many other central banks. Falling foul of the G7 geopolitical alliance has a deep cost and in order to mitigate the risk, central banks are accumulating the pseudo-currency that no other central bank controls: gold.

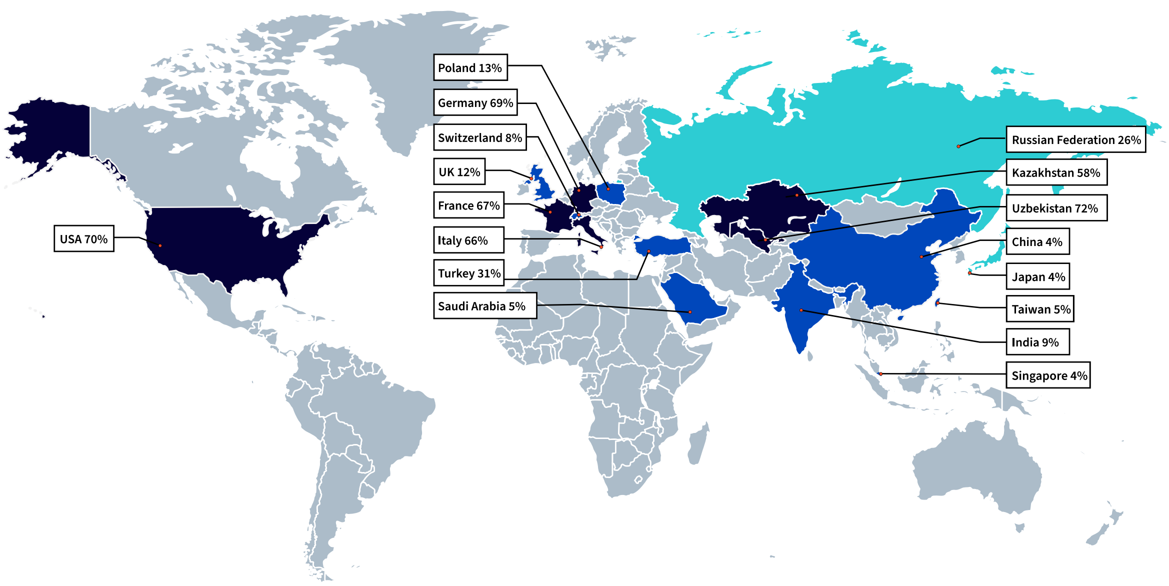
Central Bank Gold Demand



Source: WisdomTree, World Gold Council, Q1 2010 to Q3 2023. **Historical performance is not an indication of future performance and any investments may go down in value**

Looking at some of the biggest central bank purchasers of gold in recent years – China, Poland, Turkey – they still have a relatively low amount of gold as a proportion of total foreign exchange. So, we believe that these central banks could keep buying gold at the current pace for many years and still not reach the levels held by the US, France, Germany and Italy.

% of foreign reserves in gold

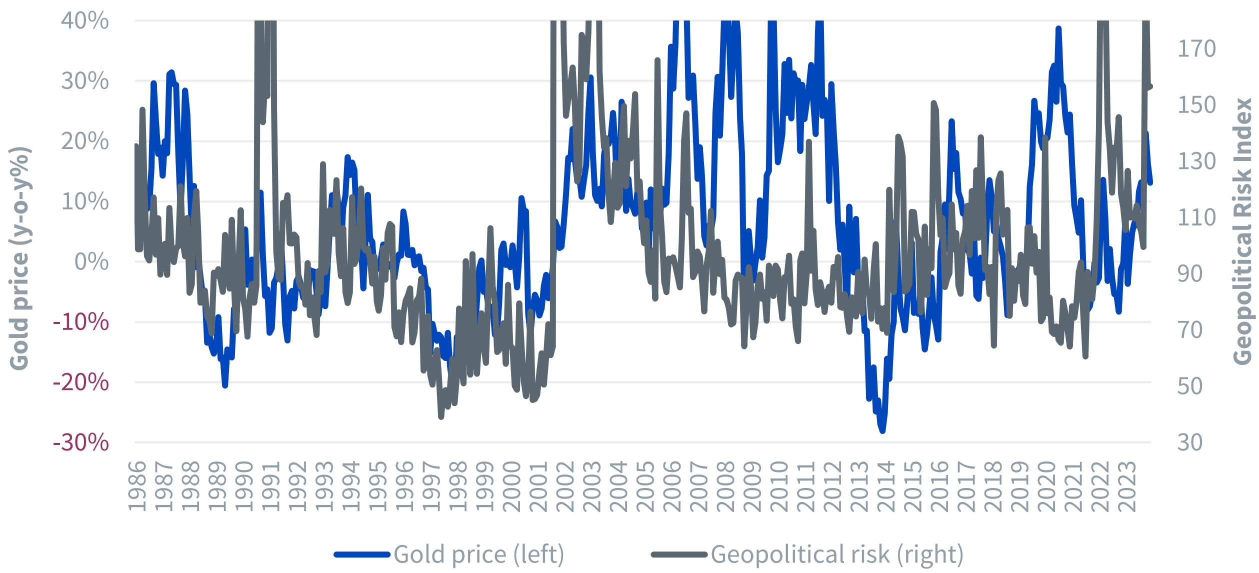


Sources: WisdomTree, World Gold Council, IMF, as of November 2023. **Historical performance is not an indication of future performance, and any investments may go down in value.**

Geopolitical risk and gold

Although geopolitical risk seems to have calmed down a little since October 2023, when the Israel-Hamas war broke out, this source of risk still remains elevated. In December 2023, Houthi attacks on ships in the Red Sea highlighted that tensions in the Middle East are not simply confined to Israel-Gaza. Chinese President Xi Jinping used his annual new year address to the nation to sound a warning to Taiwan's voters, days ahead of the island's presidential election (January 13 2024). He said "reunification" of Taiwan and China was a "historical inevitability". He added that "compatriots" on both sides of the Taiwan Strait must share in the glory of "national rejuvenation". Many analysts had thought the prolonged war in Ukraine would be a deterrent to Xi in pursuing annexation of Taiwan, but recent rhetoric from Xi indicates that risk is still on the cards.

Gold and geopolitical risk



Source: Dario Caldara and Matteo Iacoviello's Geopolitical Risk Index based on a tally of newspaper articles covering geopolitical (war) tensions, Bloomberg, WisdomTree. January 1986 – December 2023. **Historical performance is not an indication of future performance and any investments may go down in value.**

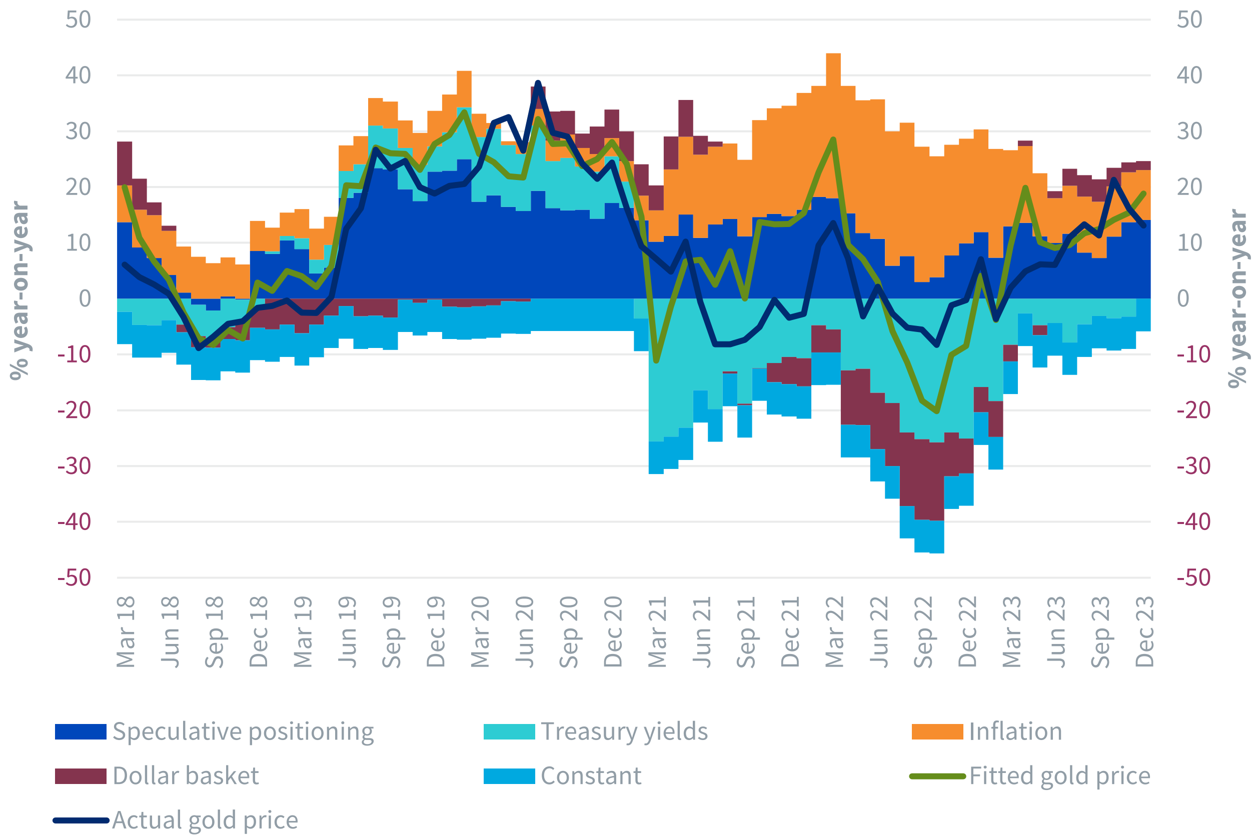
Gold look-back

We can use WisdomTree's quantitative gold model[1] to find out what had driven gold prices in 2023. In contrast to previous years, while bond yields were still rising for most of the year and indeed hit the highest levels since 2007 in October 2023, the incremental change was not as large as in previous years. By the end of 2023, bond yields were about the same level as at the end of 2022. Thus, the headwind against gold was dulled. That allowed the relatively elevated levels of inflation to boost gold prices. Also, while the US Dollar was firm, the USD basket depreciated over the previous year, once again providing gold some relief.

Lastly, sentiment towards gold, based on speculative positioning in gold futures, while appearing somewhat depressed in October 2023, improved markedly by the end of the year. In December 2023, gold posted a fresh new high because of these factors coming together. Our model indicates that gold could have risen even further in December 2023, after a few months of actual gold prices outpacing the model. However, the model and actual prices ended the year a lot closer than in April 2023, when the discrepancy was a notable.

1. See our model described in [Gold: how we value the precious metal]

Gold price attribution



Source: Bloomberg, WisdomTree price model, data as of December 2023
The fitted gold price is the price the model would have forecast. The constant does not have economic meaning but is used in econometric modeling to capture other terms. It can be thought of as how much gold prices would change if all other variables were set to zero (although that would be unrealistic). **Historical performance is not an indication of future performance and any investments may go down in value**

Gold outlook using WisdomTree's forecasts model

Using the same model, we can produce gold forecasts consistent with several macroeconomic scenarios.

Consensus

Our consensus scenario takes Bloomberg's Survey of Professional Economists average views on inflation, US Dollar and Treasury yield forecasts. Consensus is looking for inflation to continue to decline (although to remain above the central bank target), US Dollar to depreciate and bond yields to continue to fall. Consensus is based on Federal Reserve rate cuts commencing in Q2 2024 and ending the year a full percentage point lower.

Without a consensus forecast on gold sentiment we reduce speculative positioning to a conservative 75k, which is below the long-term average of 111k since 1995 and down considerably from the end of 2023 levels (217k contracts net long). The risk is clearly to the upside on positioning this year if a recession or financial dislocation risks materialises or geopolitical tensions escalate. Gold is a highly sought after asset in times of economic, financial and geopolitical stress, and these triggers could drive sentiment towards the metal even higher.

In the consensus case scenario, gold reaches US$2,210/oz by Q4 2024, piercing through previous all-time nominal highs (US$2,078/oz on 28 December 2023). However, in real terms this does not reach the all-time high, which was reached in January 1980. In fact, it would be 36% below that level.

Bull Case

In this scenario the Federal Reserve provides forward guidance as soon as the January Federal Open Market Committee (FOMC) meeting and starts delivering rate cuts in Q1 2024. It acts pre-emptively to ward off recessionary risk. That recessionary risk is a deflationary force and investors look to gold as a hedge against adverse economic and financial outcomes. The effects are that the US Dollar depreciates much more quickly and bonds yields fall to 3% by the end of the year, while inflation falls more aggressively.

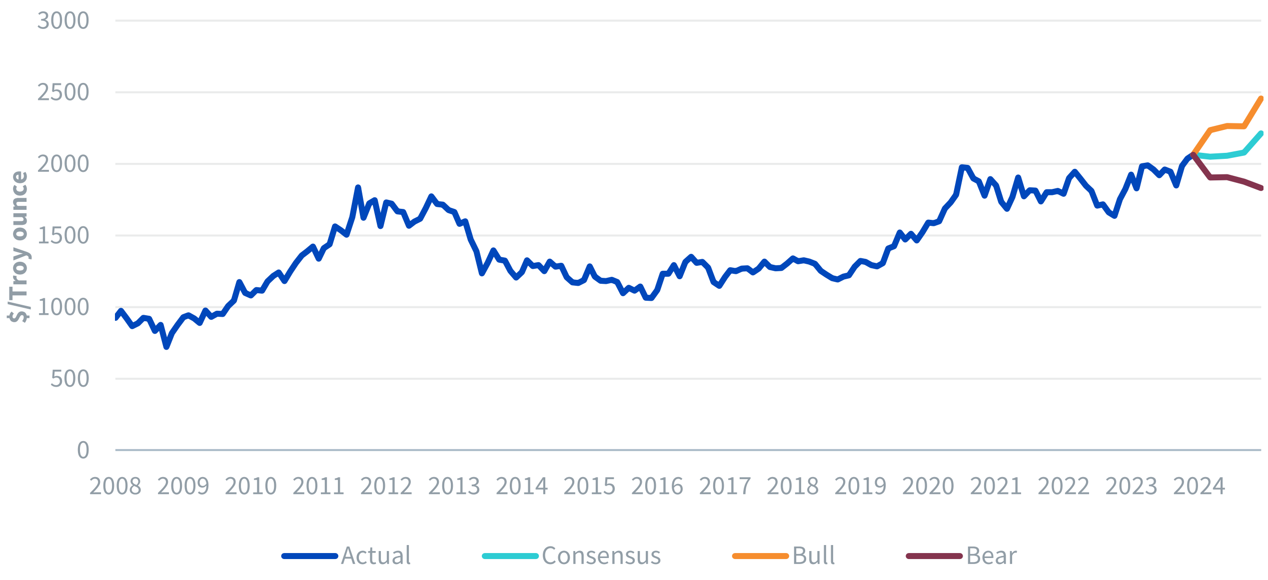
In this scenario, gold could reach US$2,455/oz. That would be 18% higher than the all-time nominal high (reached in December 2023) and about 29% below the real all-time high of January 1980.

Bear case

In the bear case, we maintain an inflation scenario in line with the bull case, i.e. a recessionary/deflationary scenario arises but the Federal Reserve is reluctant to cut rates. Possibly justifying its lack of action due to the labour market not weakening enough and not wanting to be premature in declaring a victory over the inflation battle. Bond yields rise back to November 2023 levels as the Federal Reserve telegraphs that it will not cut rates anytime soon, while the US Dollar appreciates. For the sake of playing out a scenario, we cut speculative position to 50k net long on the assumption that investors are attracted to higher yields in the bond market. However, we acknowledge that if investors see the Federal Reserve making a policy mistake, positioning could indeed rise as they hedge themselves with gold.

In this scenario, gold could fall to US$1,830/oz, retracing prices back to February 2023 levels.

Gold price forecast



Source: WisdomTree Model Forecasts, Bloomberg Historical Data, data available as of close December 2023.
Forecasts are not an indicator of future performance and any investments are subject to risks and uncertainties

	Consensus			
	Q1 2024	Q2 2024	Q3 2024	Q4 2024
Inflation forecast	2.9%	2.8%	2.5%	2.3%
Nominal 10-year yields forecast	4.07%	3.95%	3.84%	3.80%
US$ exchange rate forecast (DXY)	102.8	101.9	100.8	99.4
Speculative positioning forecast	75,000	75,000	75,000	75,000
Gold price forecast	US$2,050/oz	US$2,055/oz	US$2080/oz	US$2,210/oz

Source: WisdomTree. Bloomberg Survey of Professional Economists. December 2023. **Forecasts are not an indicator of future performance and any investments are subject to risks and uncertainties**

	Bull			
	Q1 2024	Q2 2024	Q3 2024	Q4 2024
Inflation forecast	2.0%	2.0%	1.0%	1.0%
Nominal 10-year yields forecast	3.70%	3.50%	3.10%	3.00%
US$ exchange rate forecast (DXY)	100	98	96	94
Speculative positioning forecast	200,000	200,000	200,000	200,000
Gold price forecast	US$2,235/oz	US$2,265/oz	US$2,265/oz	US$2,455/oz

Source: WisdomTree. Bloomberg Survey of Professional Economists. December 2023. **Forecasts are not an indicator of future performance and any investments are subject to risks and uncertainties**

	Bear			
	Q1 2024	Q2 2024	Q3 2024	Q4 2024
Inflation forecast	2.0%	2.0%	1.0%	1.0%
Nominal 10-year yields forecast	4.60%	4.35%	4.25%	4.15%
US$ exchange rate forecast (DXY)	104	105	106	107
Speculative positioning forecast	50,000	50,000	50,000	50,000
Gold price forecast	US$1,900/oz	US$1,900/oz	US$1,875/oz	US$1,830/oz

Source: WisdomTree. Bloomberg Survey of Professional Economists. December 2023. **Forecasts are not an indicator of future performance and any investments are subject to risks and uncertainties**

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