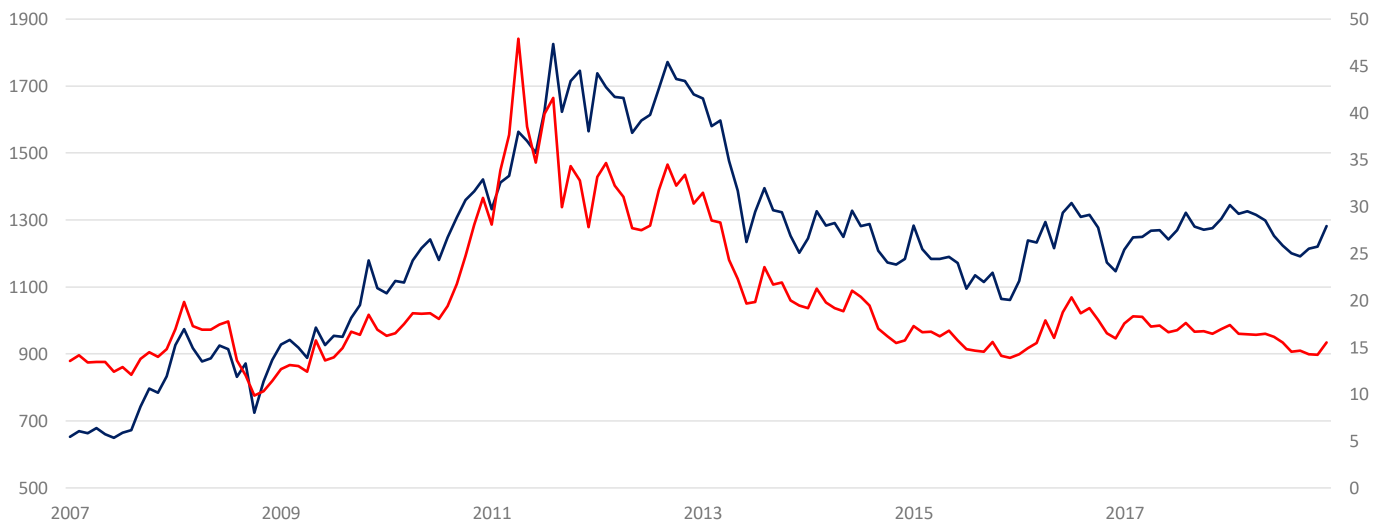
Precious Metals an Asset Class for These Times

The allure of gold has both fascinated and captivated humanity for eons. Given the current unparalleled challenges faced by the global financial system, precious metals deserve the same focus and close attention. During 2019, sentiment towards precious metals fluctuated as investors reacted to the ever-changing geopolitical landscape and economic outlook. Set against this backdrop some technical analysts believe that the pattern of substantial gains and subsequent downside correction is the continuation of a longer-term trend which indicates a strong advance in 2020, and beyond. We agree. We see short-term pullbacks in the gold price as an opportunity to initiate new positions or add to existing holdings.

Chart 1: Gold and Silver prices (USD per ounce)



Source: Bloomberg

Below we highlight three factors which we believe are vital in driving meaningful gains for precious metals.

Negative Interest Rates

The global financial system has, in the recent years, faced unprecedented challenges, which have been met with extraordinary measures by major central banks. Declining consensus forecasts for economic growth, most recently exacerbated by the trade war between the United States and China, and the continuous expansion of global debt, has forced central banks to cut policy rates to zero, and then negative. During 2019 the global market value of negative-yielding debt peaked at US$17 trillion. Despite declining from this level, the sum still increased by over 50% during the year. By common consensus, where lenders have to pay a borrower to accept their money then it has reached the extreme point of absurdity, being devoid of any real commercial logic. Historically, periods of declining real US $ interest rates have been positive for gold.

Chart 2: Value of global negative yielding debt (USD trillion)

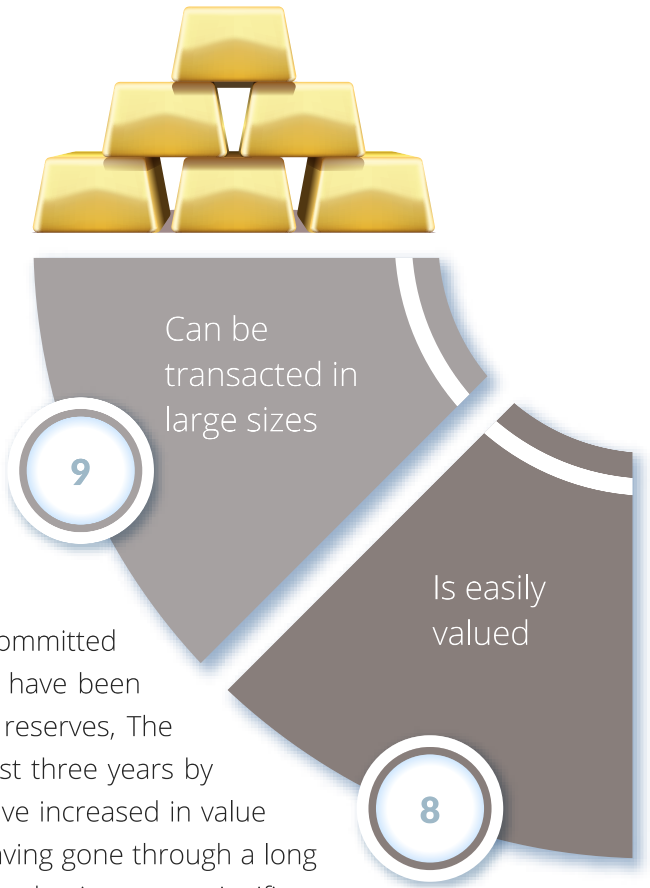
Source: Bloomberg

Currency Devaluation

Historically, a strong currency was a symbol of national pride, especially among the political leadership and popular press; however, the desire for this emblematic status has now been almost entirely reversed. Indeed, most central banks and national governments have entered into a competitive devaluation, with a race to the bottom of purchasing power. During 2019, President Trump made multiple references or statements of intent and desire to devalue the US Dollar. Furthermore, the likelihood of the devaluation race becoming full-blown currency 'wars' arguably increased in 2019, as the Trump administration formally labelled China as a currency manipulator, after the People's Bank of China allowed the yuan to fall to more than an eleven-year low versus the US Dollar.

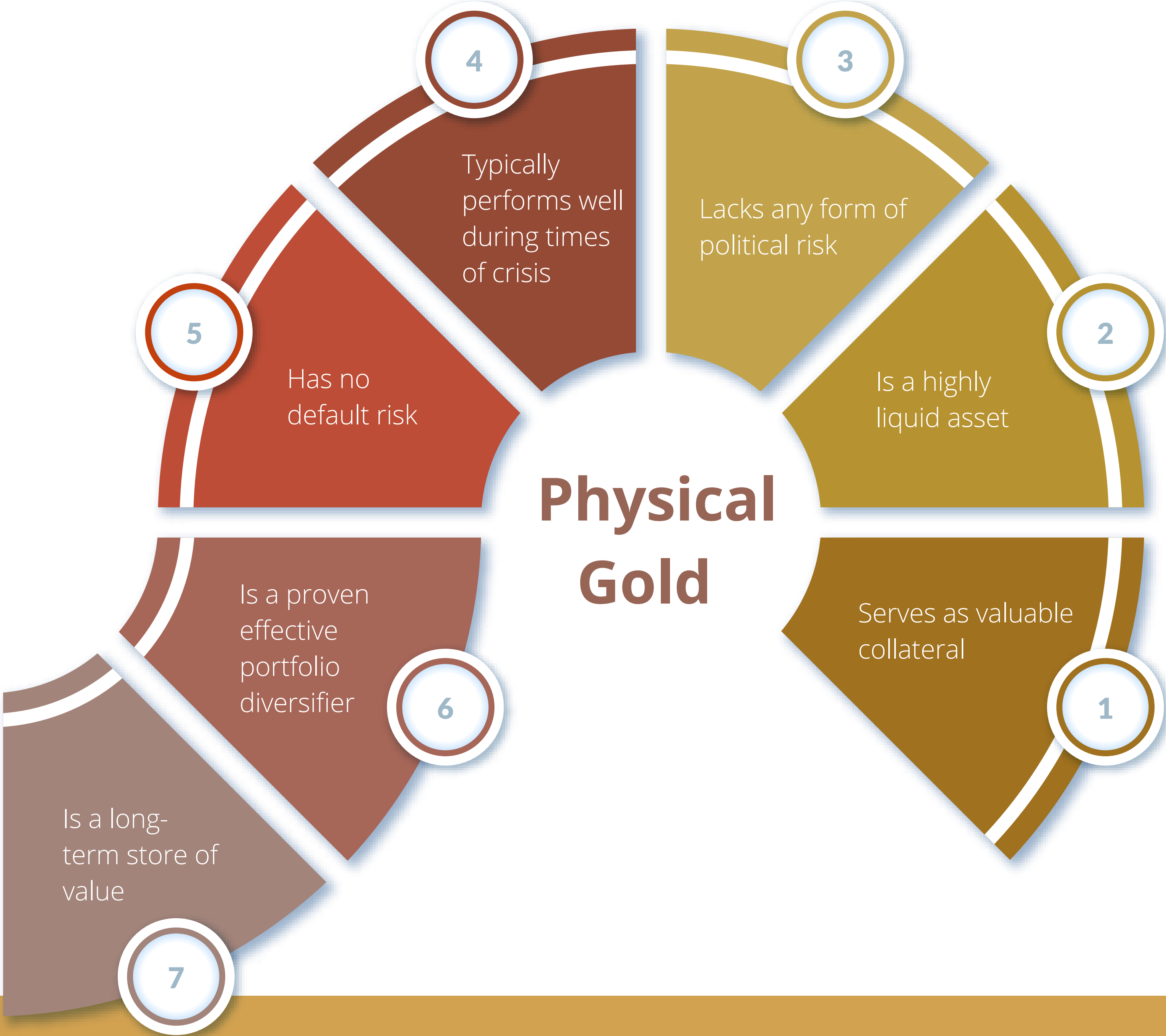
Meanwhile many financial analysts also interpreted the Swiss National Bank's (SNB) 2019 intervention in the currency market to weaken the Swiss franc as a further sign of these potential currency wars. The SNB took the stance that they were acting "to keep the attractiveness of Swiss franc investments low and ease pressure on the currency." In such a scenario of active devaluation, we believe that investors will view gold as a better store of value. Investors need only look at Argentina to understand that extreme outcomes can happen when there is a complete loss of confidence in fiat currency. Over the past five years, the price of gold in Argentine Peso's has risen more than 750%. Over ten years, the price change is over 1,800%! By way of reference, in US Dollar terms, the price of gold has risen 28% over ten years and in Japanese Yen terms by just over 55%.

Central Bank Buying



While the recent trend for global central banks has been to pressure interest rates to extreme lows, many have been increasing their holdings of gold on their balance sheets. When central banks were questioned by the World Gold Council for their 2019 survey to rank the relevance of factors underpinning their decision to invest in gold, both emerging and developing economy central banks put "long-term store of value" and "lack of default" in first and second position respectively. The central banks of advanced economies, however, cited "historical position" as their primary reason. In recent times the most committed countries, in percentage terms, to increasing their gold reserves have been Russia and China. In a concerted effort to reduce its US Dollar reserves, The Bank of Russia has cut its holdings of US Treasuries over the past three years by over 88%. In contrast, over the same period, its gold reserves have increased in value by over 75%. Russian gold reserves now total over US$107bn. Having gone through a long hiatus between October 2016 and December 2018, China is also buying more significant quantities of the precious metal again, raising reserves to over 1,948 tonnes. Although China is the world's largest producer of gold, its overall gold stores have been anaemic compared to its competitors, especially in the context of the size of its economy. According to the World Gold Council today the People's Bank of China (PBoC) has just 3% of its reserves in gold compared to 9% for the UK, 20% for Russia, 63% for France and 77% for the United States. We expect the PBoC to be a persistent buyer of gold from both domestic and international sources in the coming years. Should China continue to accumulate bullion at the current rate over 2019, it will probably eclipse Russia as the top buyer of the precious metal. Furthermore, we also believe the trend to diversify balance sheet risk by increasing gold and reducing the influence of the US Dollar as a reserve asset to continue. Without question, the dynamics of emerging economy central banks accumulating reserves as net buyers will play a crucial role in the directionality of the gold market for years to come.

For today's investor, the allure of gold and other precious metals is in their many attractive attributes, especially when viewed in the context of their total wealth (see exhibit below).



We believe gold and other precious metals, play an important role in investment portfolios and believe there is more upside to come in years ahead.

Investment in precious metals can act as insurance policy against untoward issues in the near and long term. A world of ever declining real rates, currency devaluations, trade disputes, tensions in the Middle East, political uncertainty, and debt levels showing no bounds, is a world made for gold and silver.

Contribution from Aurian

Disclaimer

This update has been produced using both internal and external data with the aim to provide information. However, this is not intended to form professional advice nor should it be relied upon as such and before taking any particular action, specific and personal advice should be obtained.

While The Fry Group uses reasonable efforts to obtain information from sources which it believes to be reliable, we make no representation that the information or opinions contained in this report are accurate, reliable or complete. The information and opinions contained in this update are subject to change without notice.

The Fry Group of companies comprises of Wilfred T Fry Ltd – Taxation Consultants, Wilfred T Fry (Executor and Trustee) Ltd, The Fry Group (H.K.) Ltd, The Fry Group (Singapore) Pte Ltd, The Fry Group (Belgium) SA, Wilfred T Fry (Personal Financial Planning) Ltd – Dubai Branch, and Wilfred T Fry (Personal Financial Planning) Ltd ('PFP'). The last company is authorised and regulated in the UK by the Financial Conduct Authority (FCA number 114402) and is also passported under EU regulations. The Fry Group (H.K.) Ltd is licensed to conduct investment advisory and asset management in Hong Kong by the Securities & Futures Commission (SFC; CE Number: ATY965) and is licensed as an insurance broker by the Insurance Authority (IA;Licence Number:FB1207).The Fry Group (Singapore) Pte Ltd is authorised to act as a financial adviser by the Monetary Authority of Singapore - licence number FA100057. The Fry Group (Belgium) SA is regulated in Belgium by the FSMA (Reg. No. 23345 A) and is also passported under IMD EU regulations. Wilfred T Fry (Personal Financial Planning) Ltd – Dubai Branch is regulated by the Dubai Financial Services Authority (licence number F005071).

The Fry Group
since 1898