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Sell Gold as the US Fed is nearing another rate hike; External risks ease

Reco rate: Sell Gold at $1225 (spot)
Sell MCX Gold December at Rs29,230
Buy 45 lots of USDINR at spot price of Rs68.10

Key points

- In her first testimony after the US election, the Federal Reserve's Janet Yellen hinted: the Fed is close to hiking rates as the US economy gains traction
- Markets are optimistic on Mr Donald Trump's plan to stimulate the US economy through large fiscal spending
- US president-elect's plans of stimulating the American economy to lift interest rates
- Labor market condition in the US is improving
- US economy showed robust growth in 3QCY2016
- The Fed is likely to hike rates in December 2016
- The dollar index is at a 14-year high
- China is showing early signs of stabilising
- China's manufacturing PMI rises to over two-year high in October; new orders climb
- China's services sector grew at the fastest pace in four months as new business picked up
- European Union manufacturing sector is also showing some strength

Call:

On November 17, we initiated medium-term to long-term fundamental 'Sell' call in gold. We recommended selling gold at $1225 (spot) for the price target of $1150/$1100 (spot) with a stop loss (SL) of $1290. On the MCX, we recommended selling gold December contract at Rs29,230. We have advised hedging the currency risk by buying 45 lots of USDINR (spot) at Rs68.10.

Call rationale:

- The 'Sell' call in gold is based on the same factors that had prompted us to sell gold at $1348 on August 19. The report for the call wad released on August 26. The clients are advised to go through the report for the detailed analysis of both negative and positive factors for the yellow metal currently.
- We believe that the US Fed Reserve is heading towards another rate hike in December this year. The latest Yellen testimony on the US economic outlook on November 17 (her first after the US election) gave a clear indication that the US central bank policymakers are on the path to hike rates anytime soon, buoyed by improving labor market condition, rise in hourly earnings and increasing possibility of inflation inching toward the FOMC's 2% goal. All these factors lend weight to our assumption of a rate hike.

- Gold prices have lost more than $100 after the historic US election outcome on November 9, wherein Mr Trump surprisingly defeated Ms Hilary Clinton to become the 45th US president. Investors and money managers seem to be turning positive about Mr Trump's policies going forward. The US Dollar Index has risen to a 14-year high, which is indication of markets' confidence in the US president-elect.
- On the other hand, the external risks are also diminishing, as China's economy seems to be stabilising. The European PMI data has been encouraging too. In its latest monetary policy meeting held on November 3, the Bank of England (BOE) stated that it is ruling out any rate hike in the near term, as the Brexit event is likely to weigh less on on the UK economy than previously thought. The reduced external risk is another factor which supports the case for a rate hike by the Fed. Also, it would reduce the demand for safe haven assets like gold in the near term.

Risk to our call:

The major risk to our call would be the Fed taking for more time to assess the US economy, in which case a rate hike would be delayed.

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