

21st July 2016

****SALES DESK COMMENTARY****

Rising dollar, abatement of Brexit fears, and US economy to place downward pressure on gold. Sell gold equities in short-term.

US dollar resumes upward trajectory as Brexit fears abate

- The Bloomberg US Dollar Index (DXY) has rallied 3.9% to 97.1 since late June. This has been driven by the continued robustness of the US economy; political polls favouring Hillary Clinton likely to be elected President rather than wild-card Trump; the likelihood of the Fed to continue on its modest and staggered tightening; and the abatement of Brexit fears.
- The last point is the most salient. The exaggerated negative economic scenarios that the markets and media feared in the days immediately post Brexit have now largely dissipated. Even the FTSE is now up 12% from its post Brexit low.

Gold price has rallied too, gold equities even more so

- Gold has nicely rallied this year to date - up 26% - chiefly on the realisation that the Fed's tightening of cycle rates would be less aggressive than thought. This corresponded with a weakening in the US Dollar index. Since Brexit, the gold price has ticked up 5.5%. Much of this was driven by the flight to safety in lieu of the uncertainty that the referendum result engendered. Australian gold equities as measured by the ASX All Ordinaries Gold Index rose even higher by 16.2%, the market clearly believing that the gold price has further to run.

US\$ Gold Price vs US Dollar Index



Source: Bloomberg.

Tipping point reach – sell gold equities

- The chart above shows the plot of the US Dollar Index (DXY) vs the US\$ gold price over the past two years. The striking point of the chart is the inverse correlation between the dollar and gold which has held fairly firm, at least until the end of June.
- Post Brexit the gold price and dollar have both enjoyed rallies, but we believe this cannot continue. We believe it is gold that will need to retrace its gains. The markets realise now that Brexit, while a shock and representing a degree of some uncertainty for Britain's economic future, won't completely derail its economy nor totally disrupt the EU. The Fed will continue its softly-softly "goldilocks" tightening policy – not too much and not too frequently. The bull market will continue on the path laden with globally low rates, providing corporates with easy money. Fears such as Brexit and Italian bank debt provide just a little bit of nervousness required to stop the Fed tightening with abandon. Investors need to watch the DXY as any catalyst for a sell-off in gold.

Recommendation: Sell gold equities in short-term

- We believe that in this environment the gold price will now struggle, and contract probably back to US\$1,200/oz. This is negative for gold equities, which are mostly already trading above their NPVs, factoring in gold price well north of spot. We recommend investors sell gold stocks in the short-term.

Foster Stockbroking Pty Ltd
A.B.N. 15 088 747 148 AFSL No. 223687
Level 25, 52 Martin Place, Sydney, NSW 2000 Australia
General: +612 9993 8111 Equities: +612 9993 8100 Fax: +612 9993 8181
Email: contact@fostock.com.au
PARTICIPANT OF ASX GROUP

Foster Stockbroking recommendation ratings: Buy = return >10%; Hold = return between –10% and 10%; Sell = return <-10%. Spec Buy = return > 20% for stock with very high risk. All other ratings are for stocks with low-to-high risk. Returns quoted are annual.

Disclaimer & Disclosure of Interests. Foster Stockbroking Pty Limited (Foster Stockbroking) has prepared this report by way of general information. This document contains only general securities information. The information contained in this report has been obtained from sources that were accurate at the time of issue. The information has not been independently verified. Foster Stockbroking does not warrant the accuracy or reliability of the information in this report. The report is current as of the date it has been published.

In preparing the report, Foster Stockbroking did not take into account the specific investment objectives, financial situation or particular needs of any specific recipient. The report is published only for informational purposes and is not intended to be advice. This report is not a solicitation or an offer to buy or sell any financial product. Foster Stockbroking is not aware whether a recipient intends to rely on this report and is not aware of how it will be used by the recipient. Investors must obtain personal financial advice from their own investment adviser to determine whether the information contained in this report is appropriate to the investor's financial circumstances. Recipients should not regard the report as a substitute for the exercise of their own judgment.

The views expressed in this report are those of the analyst/s named on the cover page. No part of the compensation of the analyst is directly related to inclusion of specific recommendations or views in this report. The analyst/s receives compensation partly based on Foster Stockbroking revenues, including any investment banking and proprietary trading revenues, as well as performance measures such as accuracy and efficacy of both recommendations and research reports. Foster Stockbroking believes that the information contained in this document is correct and that any estimates, opinions, conclusions or recommendations are reasonably held or made at the time of its compilation in an honest and fair manner that is not compromised. However, no representation is made as to the accuracy, completeness or reliability of any estimates, opinions, conclusions or recommendations (which may change without notice) or other information contained in this report. To the maximum extent permitted by law, Foster Stockbroking disclaims all liability and responsibility for any direct or indirect loss that may be suffered by any recipient through relying on anything contained in or omitted from this report. Foster Stockbroking is under no obligation to update or keep current the information contained in this report and has no obligation to tell you when opinions or information in this report change.

Foster Stockbroking and its directors, officers and employees or clients may have or had interests in the financial products referred to in this report and may make purchases or sales in those the financial products as principal or agent at any time and may affect transactions which may not be consistent with the opinions, conclusions or recommendations set out in this report. Foster Stockbroking and its Associates may earn brokerage, fees or other benefits from financial products referred to in this report. Furthermore, Foster Stockbroking may have or have had a relationship with or may provide or has provided investment banking, capital markets and/or other financial services to the relevant issuer or holder of those financial products.

For an overview of the research criteria and methodology adopted by Foster Stockbroking; the spread of research ratings; and disclosure of the cessation of particular stock coverage, refer to our website <http://www.fostock.com.au>.