HSBC Global Research

25 November 2022

Gold Special

Raising our forecasts

Commodities
Gold

Global

- We are raising our average gold price forecasts for 2023 and 2024 to USD1,813/oz and USD1,750/oz, respectively
- A peaking in the USD and likely weakness in 2023 as well as an eventual end to the Fed's rate hike cycle are gold bullish
- Strong central bank and coin & bar demand is expected to continue in 2023 and buoy prices; ETF demand likely to rise

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Raising the gold bar

While the logic we presented in the *November Currency Outlook: It has peaked* (11 Nov 2022) and our last *Gold Outlook: Force Fed lower* (6 Oct 2022) remains broadly intact, the more recent changes in sentiment in the forex and fixed income markets, most notably the USD fall, triggered a gold rally that we had previously expected would come later, from Q2 2023. The impact of a potentially weaker USD earlier in 2023 than anticipated, combined with a peak in Fed tightening policy, are the main catalysts that lead us to modestly revise higher our gold forecasts.

We leave our **average price forecast for 2022** unchanged at USD1,770/oz. We raise our **average price forecasts for 2023 and 2024** to USD1,813/oz and USD1,750/oz from USD1,701/oz and USD1,675/oz, respectively. We leave our **long-term forecast** unchanged at USD1,600/oz. We anticipate a trading range of USD1,650-1,900/oz in 2023 and year-end prices of USD1,790/oz for 2023 and USD1,750/oz for 2024.

USD is key

Historically, USD levels have exerted a significant influence on gold, and normally gold trades inversely with the USD. USD strength, which reached levels not seen in decades, played a key role in gold weakness for most of 2022. The USD has been buoyed by three drivers (hawkish Fed, slower economic growth, and risk aversion), according to HSBC FX research. The apparent change in the USD's fortunes – which is occurring a little earlier than we had anticipated – set off the recent gold rally and alters the timing for further likely gold gains in 2023.

The USD has performed undeniably well since mid-2021, but the key forces that propelled it to multi-decade highs may be losing steam (see *Currency Outlook: It has peaked*, 11 Nov 2022). The global economy has been weakening since mid-2021 and there is a strong association between a strengthening USD and weak global economy. That said, the pace of decline has been slowing, suggesting the low point of the cycle could be approaching, especially relative to very bearish consensus expectations. USD rates remain elevated compared to other currencies, but terminal rate expectations may already have peaked, especially if US inflation shows further signs of subsiding. This could reduce rate volatility, thereby undercutting the USD. The combination of a bottoming in global growth dynamics alongside an eventual stabilization in yields may provide a better backdrop for risk appetite. This in turn could remove another leg of USD support, conclude the FX team, and thus aid gold.

The Fed can still restrain gold

HSBC economists are forecasting a federal funds rate of nearly 5% by February 2023 (see *FOMC Multi-Asset Outlook: Five is alive*, 2 Nov 2022). According to HSBC Rates strategists, a higher-for-longer Fed narrative could push up recent trading ranges for rates if FOMC policymakers stay hawkish (see *Fixed Income Asset Allocation: Calling the relatives*, 9 Nov 2022). Two-year note yields should have support in the 4.5% area and near-term resistance in the 4.75% area. A continued hawkish Fed could see the two-year yield move to over 5.0% over time. For the 10-year note, a hawkish Fed could mean a near-term range of 4.0-4.3% with the bearish trend pointing to a move to 4.5% or more over time. Although some easing in inflation pressures have called the pace of Fed rate increases going forward into question, recent comments from Fed officials confirm further tightening. Fed tightening could remain an important negative for gold at least into Q1 2023.

Physical rules

A feature of the institutional investment market has been strong selling, notably heavy liquidation in the ETFs, prompted by hawkish Fed policies and a strong USD. Heavier than anticipated selling leads us to revise lower our forecast for ETF liquidation for this year to a decline of 80t from a decline of 40t previously, followed by a forecast build of 150t next year from 165t previously, as USD weakness and the end of the Fed rate hike cycle encourages demand.

The outlook for underlying physical demand for bar & coins remains strong. Retail demand, spurred by ongoing inflation concerns and geopolitical and financial markets risks, is likely to continue to stoke demand globally. This stands in contrast to institutional demand which, as evidenced by ETF liquidation, has been negative this year. This component of consumption may be key in supporting prices in 2023. The sharp increase in central bank demand in Q3 leads us to increase our forecast for official sector purchases for 2022 to 725t from 475t previously. We also increase our 2023 forecast for official sector purchases to 550t from 450t previously.

Conclusion

We believe the likelihood that the USD has peaked and expected further strong official sector and coin & bar and jewellery demand present compelling arguments for higher gold prices in 2023 and beyond. That said, until the end of the Fed's rate hike cycle is complete, and institutional demand for gold increases, prices may be constrained. This leads us to look for weakish prices in early 2023 with increases more likely as the year unfolds.

Disclosure appendix

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