Weekly Trends

PRIVATE CLIENT SOLUTIONS

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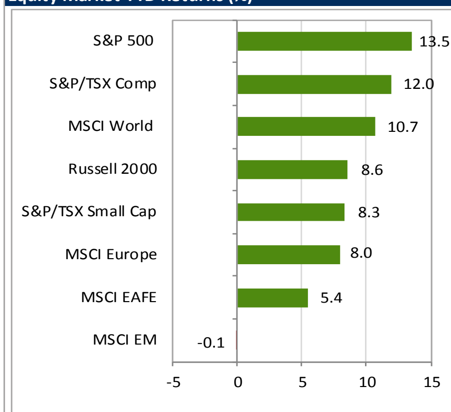
The Midas Touch

The inversion of the yield curve has grabbed investors' attention this week and for good reason. The 2yr10yr inversion has a good track record of calling US recessions and this is occurring at a time the global economy is struggling. In short, even with the inversion signal, history suggests neither a recession nor a potential peak in the market are immediate concerns.

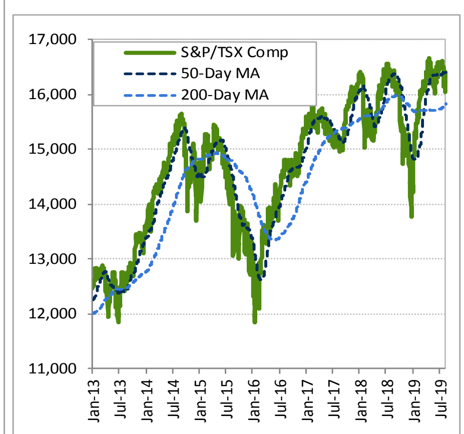
- In the midst of all of this, gold has gotten its groove back after spending the past few years struggling to break out of a rather large range. The commodity spent over three years trading between 1,120/oz and 1,370/oz, but thanks to the shift in global monetary policy this year, concerns about the fate of the global economy and greater geopolitical uncertainty, bullion put in a bottom late last year, sending the commodity through US$1,400/oz for the first time since 2013.
- While most investors view gold as a hedge against inflation, the commodity's performance is more closely tied to real rates – the difference between nominal yield and inflation. This can help explain gold's recent performance despite muted inflation and inflation expectations. With US nominal rates falling and nearing record lows, real rates have moved closer to zero and may in fact turn negative should nominal yields continue to fall.
- Gold continues to surge higher following the completion of its multi-year base in June. The commodity now faces its first major overhead resistance from 2011/2013 with previous support level at $1522/27. A phase of consolidation can be expected around these levels before the commodity makes a clear break to new multi-year highs.

Equity Market YTD Returns (%)



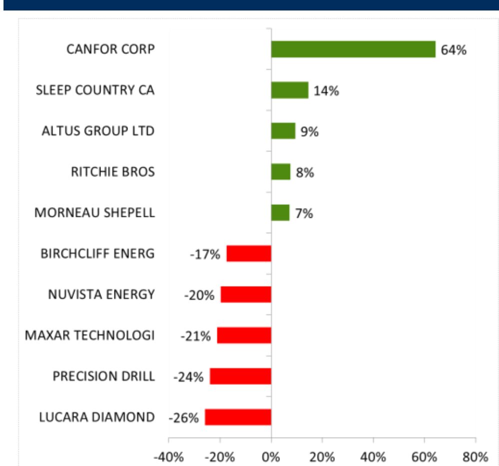
Canadian Sectors	Weight	Recommendation
Consumer Discretionary	4.2	Underweight
Consumer Staples	4.2	Overweight
Energy	16.1	Underweight
Financials	31.4	Overweight
Health Care	1.6	Underweight
Industrials	11.4	Market weight
Technology	5.5	Market weight
Materials	11.7	Market weight
Communications	5.8	Market weight
Utilities	4.6	Market weight
Real Estate	3.6	Market weight

Technical Considerations	Level	YE Target
S&P/TSX Composite	16,037	15,600



Source: Bloomberg, Raymond James Ltd.
Sectors are based on Bloomberg classifications

S&P/TSX Top 5 Gainers/Laggards*



S&P/TSX Market Internals

Weekly Advance	109	43%
Weekly Decline	130	52%
Advance-Decline	-21	
New 52 wk high	8	3%
New 52 wk low	28	12%
No. Stocks Above 50-d	92	37%
No. Stocks Above 200-d	130	52%
Arms Weekly Index	0.98	Neutral
RSI (14-day)	35.6	Neutral
50-DMA	16,404	Downtrend
200-DMA	15,825	Uptrend

*Source: Bloomberg, Raymond James Ltd; * 5-day price return*

Inversion

The inversion of the yield curve has grabbed investors' attention this week and for good reason. The 2yr10yr inversion has a good track record of calling US recessions and this is occurring at a time the global economy is struggling. We discussed yield curve inversion at length in our August 2018 *Insights & Strategies: Yield!* and highlight an excerpt below:

"*… yield curve inversions have preceded all US recessions of the past but not every inversion has resulted in a recession. In fact, the timing between the inversion and the end of an economic cycle vary significantly. Since the 1960s, the timing between the initial inversion of the yield curve and a recession is between 6 and 24 months, with an average period of just under a year. More interesting is that in most cases, the performance of the stock market between inversion and recession has shown positive gains.*"

In short, even with the inversion signal, history suggests neither a recession nor a potential peak in the market are immediate concerns. While many of our recession indicators are neutral (or trending negative), the jobs market and US consumer remain bright spots, which lead us to believe that the probability of a recession is low at this time. Key to this call will be encouraging initial jobless claims, retail sales and consumer confidence in conjunction with other indicators not worsening. As we mentioned in our last week's *Weekly Trends*, "*we believe investors with a long-term time horizon should maintain a neutral weighting to equities. On balance, we're seeing both positive and negative factors in the market today, which supports our recommendation and we anticipate continued volatility throughout the remainder of the year given the push and pull of these factors that we identify in the table below.*"

Glass Half Full…

- ✓ Global central banks easing monetary conditions
- ✓ Inflation and inflation expectations well anchored
- ✓ Supportive US employment trends: job formation and wage gains
- ✓ Robust US consumer spending and confidence
- ✓ Credit conditions benign
- ✓ Corporate earnings per share growth slowing, but still growing
- ✓ US technicals supportive: S&P 500, DOW & Nasdaq achieved record highs in July
- ✓ Leading Economic Indicators positive

…Glass Half Empty

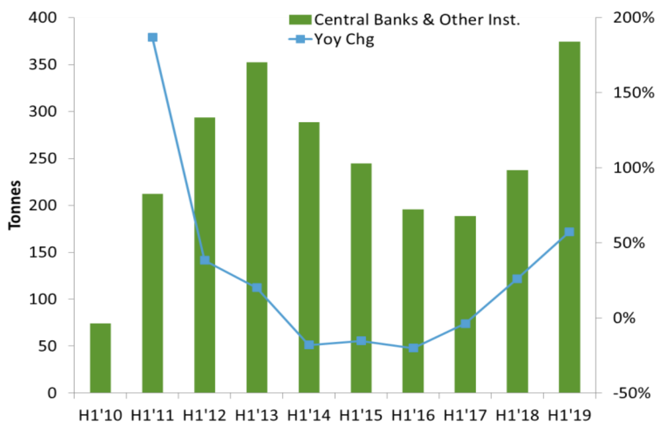
- ✗ Global economic momentum waning
- ✗ Global trade waning due to US/China trade tensions
- ✗ Geopolitical risks: EU political risks, Brexit, Middle East tensions
- ✗ Weak business investment and manufacturing activity
- ✗ Softening in US housing
- ✗ Yield curve inversion
- ✗ Risk-off assets rallying
- ✗ Some indication of US recession in next 12 months
- ✗ Global equities (ex. US) failing to achieve new highs

The Midas Touch

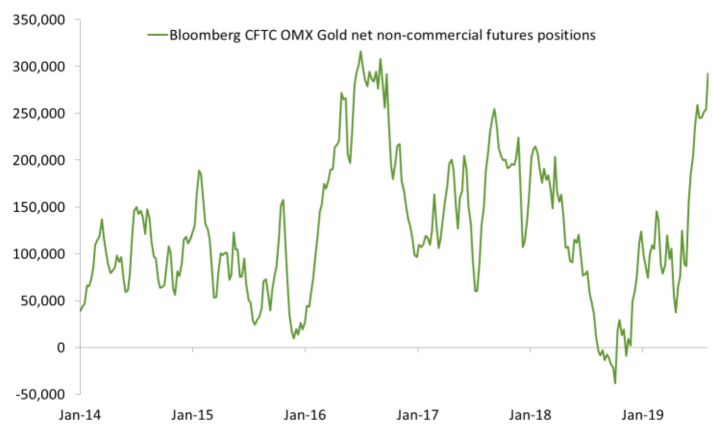
In the midst of all of this, gold has gotten its groove back after spending the past few years struggling to break out of a rather large range. The commodity spent over three years trading between 1,120/oz and 1,370/oz, but thanks to the shift in global monetary policy this year, concerns about the fate of the global economy and greater geopolitical uncertainty, bullion put in a bottom late last year, sending the commodity through US$1,400/oz for the first time since 2013. With gold completing a multi-year base and the tailwinds from monetary policy and increased economic uncertainty, we see bullion prices moving higher from current levels.

Demand for bullion can be seen from central bank purchases, healthy ETF inflows and speculators increasing their allocation to the precious metal. In the first half of 2019, central banks purchased a record 374.1 tonnes, ETFs and other investment vehicles ramped up purchases by 77% yoy and speculators have also been building positions in the commodity.

Central Banks Bullion Purchases on the Rise



Speculators Building Their Positions



Source: Bloomberg, Raymond James Ltd.

While most investors view gold as a hedge against inflation, the commodity's performance is more closely tied to real rates – the difference between nominal yield and inflation. The real rate can be calculated using any number of maturities, but for our purpose we use the US 10-year yield less the 10-year breakeven inflation rate. Comparing gold prices to real rates over the past 19 years (see chart on next page) we see a very strong negative correlation of -0.90. This suggests that gold prices advance when real rates are falling since lower rates reduce the opportunity cost of holding non-yielding gold.

This can help explain gold's recent performance despite muted inflation and inflation expectations. With US nominal rates falling and nearing record lows, real rates have moved closer to zero and may in fact turn negative should nominal yields continue to fall.

There are a number of facts pulling US nominal yields lower, including recession concerns (mentioned above) and the significant divergence between US and global bond markets. While the global bond market has a value of US$56 trillion, there are now some US$15 trillion, or 27% of the market, trading with negative yields. In fact, long-term bond yields for the major economies are at their lowest level in history, lower even than the level set during the most severe economic environments witnessed over the past 150 years.

Market participants have even begun to ponder whether the US bond market may also turn negative amid the Fed easing cycle, persistently soft inflation and demographics that hinder economic output. Surprisingly, former Federal Reserve Chairman Alan Greenspan this week says he would not be surprised if US bond yields turn negative. Of course, we have a ways to go before rates flip to negative as the US 10 year treasury yields is 1.60%, around 30 bps above its record low of 1.3%. Nonetheless, gold looks more attractive in periods when real yields decrease.

US Real Rates Approaching Zero

Negative Yielding Bonds & Gold

Source: Bloomberg, Raymond James Ltd.

What's the Chart Saying?

Gold continues to surge higher following the completion of its multi-year base in June. The commodity now faces its first major overhead resistance from 2011/2013 with previous support level at $1522/27. A phase of consolidation can be expected around these levels before the commodity makes a clear break to new multi-year highs. Given the backdrop that we've outlined above, our core tendency is the belief that bullion could make a clear break on its way to retest its previous highs.

Bullion Prices Breakout of Multi-year Base

Source: stockcharts.com, Raymond James Ltd.

How to Play

If you believe gold prices have entered a new bull phase, there are a couple ways to play it, but your investment strategy may depend on your tolerance for risk. The first choice one must make is whether to invest in the commodity itself or the producers of the commodity. The most efficient, and easiest, way to gain broad-based exposure to either one of these categories is via an ETF. Below we highlight some commodity-linked and equity offerings available in the marketplace today.

Canadian-listed Gold Products

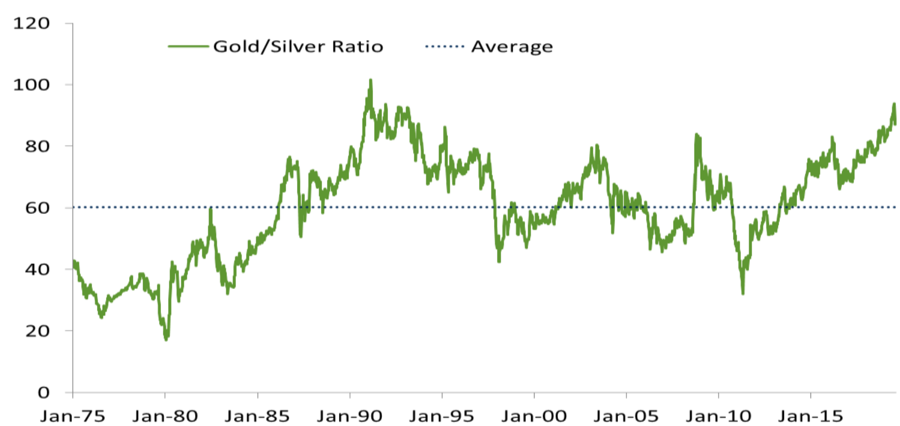
- Horizons gold ETF (HUG-T)
- ishares gold bullion ETF Hedged (CGL-T)
- Canadian Gold Reserves ETR (MNT-T)
- BMO Junior Gold Miners ETF (ZJG-T)
- US Global GO Gold & Precious Metal Miners ETF (GOGO-T)

US-listed Gold Products

- SPDR Gold Trust (GLD-US)
- iShares Gold Trust (IAU-US)
- VanEck Vector Gold Miners ETF (GDX-US)
- VanEck Vector Junior Gold Miners ETF (GDXJ-US)

For risk-averse investors wanting to gain exposure, individual equity exposure through senior gold producers and royalty streamers may provide participation while offering less volatility. Risk tolerant investors may wish to focus on junior producer as they generally provide greater leverage to bullion prices. Another option is to consider silver plays. This is a particularly attractive option given the gold/silver ratio is near an extreme. The ratio has averaged 60.2x over the past 44 years, but currently stands at an elevated level of 88.3x. A reversion to the mean could see silver prices significantly outperform bullion.

Gold/Silver Ratio



We screened for Canadian precious metals producers with a market cap greater than $250 mln and sort the table below based on the 10-year weekly correlation to bullion prices.

Company Name	Ticker	Market Cap ($mln)	Weekly Correlation to Gold*	YTD Return
Wheaton Precious Metals Corp	WPM	$15,794	0.676	33.9%
Barrick Gold Corp	ABX	$42,678	0.647	32.6%

Yamana Gold Inc	YRI	$4,229	0.635	39.2%
Franco-Nevada Corp	FNV	$23,330	0.62	30.9%
Agnico Eagle Mines Ltd	AEM	$18,648	0.607	43.2%
Premier Gold Mines Ltd	PG	$476	0.603	40.4%
Endeavour Silver Corp	EDR	$473	0.601	17.0%
IAMGOLD Corp	IMG	$2,111	0.595	-10.0%
B2Gold Corp	BTO	$4,896	0.592	21.1%
Detour Gold Corp	DGC	$4,218	0.591	107.5%
First Majestic Silver Corp	FR	$2,825	0.578	73.2%
Fortuna Silver Mines Inc	FVI	$824	0.573	2.8%
Kinross Gold Corp	K	$8,204	0.569	48.9%
SSR Mining Inc	SSRM	$2,576	0.569	28.5%
Pan American Silver Corp	PAAS	$4,755	0.559	14.6%
Alamos Gold Inc	AGI	$3,641	0.556	90.3%
Sandstorm Gold Ltd	SSL	$1,486	0.541	32.8%
OceanaGold Corp	OGC	$2,166	0.535	-29.9%
Alacer Gold Corp	ASR	$1,677	0.531	125.8%
Endeavour Mining Corp	EDV	$2,948	0.525	20.1%
Silvercorp Metals Inc	SVM	$831	0.521	72.5%
Great Panther Mining Ltd	GPR	$324	0.513	7.2%
SEMAFO Inc	SMF	$1,704	0.508	72.7%
Novagold Resources Inc	NG	$3,009	0.506	70.7%
Asanko Gold Inc	AKG	$287	0.505	46.0%
MAG Silver Corp	MAG	$1,403	0.503	62.4%
Eldorado Gold Corp	ELD	$1,860	0.496	192.8%
Seabridge Gold Inc	SEA	$1,169	0.496	4.9%
New Gold Inc	NGD	$903	0.477	48.6%
Osisko Gold Royalties Ltd	OR	$2,329	0.473	37.0%
Dundee Precious Metals Inc	DPM	$894	0.471	39.2%
Golden Star Resources Ltd	GSC	$408	0.458	-13.7%
Torex Gold Resources Inc	TXG	$1,654	0.458	49.3%
Sabina Gold & Silver Corp	SBB	$497	0.447	38.2%
Centerra Gold Inc	CG	$3,485	0.446	103.2%
Americas Silver Corp	USA	$362	0.445	96.9%
Continental Gold Inc	CNL	$879	0.44	92.4%
Teranga Gold Corp	TGZ	$585	0.434	35.0%
Pretium Resources Inc	PVG	$3,144	0.433	47.3%
Argonaut Gold Inc	AR	$448	0.43	60.9%
Victoria Gold Corp	VIT	$408	0.376	33.8%
China Gold International Resources	CGG	$608	0.365	-2.8%
Gran Colombia Gold Corp	GCM	$268	0.356	98.2%
Wesdome Gold Mines Ltd	WDO	$986	0.348	63.0%
SilverCrest Metals Inc	SIL	$655	0.326	90.5%
TMAC Resources Inc	TMR	$701	0.294	-9.5%
Roxgold Inc	ROXG	$431	0.293	43.8%
Osisko Mining Inc	OSK	$975	0.216	16.6%
Kirkland Lake Gold Ltd	KL	$12,918	0.203	73.0%
North American Palladium Ltd	PDL	$846	0.18	34.5%
Gold Standard Ventures Corp	GSV	$325	0.156	-31.6%
New Pacific Metals Corp	NUAG	$386	0.142	86.9%
Novo Resources Corp	NVO	$404	0.122	-8.9%
Leagold Mining Corp	LMC	$688	0.068	39.6%
Equinox Gold Corp	EQX	$965	0.067	49.0%
Maverix Metals Inc	MMX	$693	0.063	32.6%
K92 Mining Inc	KNT	$531	0.059	198.8%

Lundin Gold Inc	LUG	$1,760	0.049	58.3%
Orla Mining Ltd	OLA	$306	0.044	57.1%
Sierra Metals Inc	SMT	$313	0.034	-20.7%
Centamin PLC	CEE	$2,532	N/A	17.8%
McEwen Mining Inc	MUX	$887	N/A	-2.0%
Newmont Goldcorp Corp	NGT	$41,954	N/A	17.5%
Perseus Mining Ltd	PRU	$864	N/A	89.7%
Average				46.1%

Source: Bloomberg, * weekly 10 year correlation

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