Gold in pounds is at a new all-time closing high. I love it when a plan comes together.

Thanks Boris!

The UK government is finally negotiating like it knows what it is doing. Anyone who has ever haggled about the price of a car knows you have to be willing to walk away. Even if you have no intention of walking away and took an Uber because you intend to drive home, you still need the sales person to believe you are willing to walk away.

Otherwise you are begging to be taken to the cleaners. If the money is not in your pocket, it’s in there’s. If you don’t care enough to negotiate from a strong position, you are voluntarily paying more than you have to. Obviously, Theresa May is not much good at buying cars. Maybe Boris is.

The currency market believes he is and the pound fell out of bed at the end of July. It is back testing the levels it hit immediately after the Brexit referendum, as investors begin to take seriously the new administration’s determination to leave with or without a deal. The effort to retake the high ground and try to roll back the concessions made during negotiations over the last few years is laudable, even if ultimately fruitless.

The harsh reality is none of this is going to mean a thing to the eventual outcome of the negotiations. Johnson only has a majority of one seat in Parliament, following the Liberal Democrats’ success in the Brecon and Radnorshire by-election.

Under normal circumstances that kind of news would have caused the pound to rally since it removes some of the risk of a no-deal Brexit in fact gaining critical mass in Parliament.

However, the pound has not rallied meaningfully because Johnson has big plans. The biggest
A piece of news from the campaign trail is austerity is over. There is going to be money for everything. That is going to be achieved by blowing out government deficits to levels not seen since Gordon Brown was prime minister. Once more, the pound is to be used a political football and any semblance of support is now irrelevant.

If you have been reading my work for a while, you’ll know that I have written about this trend before. It is a significant one, so it bears repeating: a wave of new leaders are being elected across the world, making promises that can only be fulfilled by new and dangerous monetary policies.

So, let’s look at what Johnson is promising. 20,000 new police officers. Widening the tax bands for the top bracket from £50,000 to £80,000. That one will do nicely for those saving in ISAs. Increasing the threshold to begin paying national insurance to £12,500. Raise education spending to £5,000 per every secondary school pupil and £4,000 for every primary school pupil.

Free TV licences for the over 75s. Maybe even removing stamp duty on homes below £500,000. Full fibre broadband for the whole country by 2025. Six free trade zones and an increase in the minimum wage. Let’s call it at least £30 billion a year in additional spending.

You can see now why I refer to it as the campaign trail. Johnson is clearly stating that if it all goes to pot in October and he is forced to call an election, he aims to win by making big promises. You can be sure that the £50 billion coming back from the EU will be trotted out to support the spending plans. A 4% hike to government spending is nothing to sniff at and is something many southern European governments would salivate at.

Even if Johnson and the Conservatives/Brexit Party lose the next election, it is not as if the Labour Party/Liberal Democrats/Greens will suddenly develop an addiction to fiscal probity.

Consider that the New Green Deal being proposed by the “progressive” wing of the Democratic Party in the US is based on massive spending to shed reliance on fossil fuels while the UK’s Labour Party is proposing a “People’s QE” to fulfil every possible whim of voters. They are just as likely to be big spenders.

No one is under any illusion that the rise of populism and increasing polarisation of politics requires a response. No matter who is in power, the natural inclination of politicians is to spend.

The bigger the problem, the more they spend. It’s almost a natural law.

It’s not as if the UK doesn’t need spending. If anything, we probably need more spending, especially on key pieces of infrastructure. The devastation wreaked on Yorkshire from the flash floods are a clear signal that dams, roads and bridges need some urgent attention. That kind of infrastructure maintenance is also likely to gain cross-party support.

None of that is good for the pound, which is why is has not rallied to any meaningful extent following the by-election result. Nevertheless, these kind of sharp moves in the market do not last indefinitely. We are likely to see at least some consolidation so now is not the most opportune time to initiate new long positions.

Gold is money

The number one lesson to remember about investing in gold is it is volatile. That’s why it is such an interesting market. When it moves it really moves and we’ve just seen a great example of that with the run up in pounds.

However, it is also worth remembering that because it is volatile it is prone to short, sharp reversals. In a bull market these are buying opportunities. In the kind of sawtooth trends that gold and gold shares produce it is these occasional setbacks that produce the most attractive entry opportunities.

The good news is that with the consolidation many gold shares have undergone there is now a clear rationale for a breakout and some adjustment to buy-up-to levels. More on that later.

Moving on, the pound is not the only currency gold has been rallying against. It has been breaking out to new recovery highs and, indeed, breaking records in a whole host of currencies.
One of the clearest confirmatory signals we are in a new bull market is that gold is appreciating when compared to most other currencies as well. In the last month gold has hit new all-time highs when denominated in the Argentinean peso, Australian dollar, Brazilian real, British pound, Canadian dollar, Chilean peso, Colombian peso, Indonesian rupiah, Indian rupee, Mexican peso, Malaysian ringgit, Nigerian naira, Norwegian krone, Pakistani rupee, Swedish krona and South African rand. This is not an exhaustive list but I think you’ll get the message.

There are two big takeaways from this list.

The first is of course that gold is a monetary metal and it is therefore going to do best when it is valued like a currency. The secret to happiness in the currency markets is matching the strongest with the weakest. That’s where the biggest trends evolve and you have scope for the biggest moves.

Right now, gold is among the strongest currencies in the world. That is why it deserves a place in every portfolio, everywhere.

It’s this last point that really needs to be driven home. The investment portfolios and bank balances of more than half the world’s population are being devalued as we speak. If gold is breaking out to new all-time highs in the currencies billions of people handle every day, it is a major signal something is happening we need to pay attention to.

Open a newspaper and you’re likely to see a running total for the quantity of debt that has a negative yield. It touched $14 trillion at the end of July but that is likely to be out of date by the time you read this.

What is particularly interesting is that the primary currencies where negative yields are evident are not listed in my list of countries where gold is making new all-time highs above.

Gold has not, yet, made a high when denominated in the euro, Swiss franc or Japanese yen. It is definitely trending higher when measured in these currencies but their relative strength is noteworthy, so what is going on?

The bond paradox

Bond yields go down when prices go up. For bond yields to go negative, bond prices have to go up a lot. Every bond issued by the German and Swiss governments has a negative yield. That means investors are willing to pay those governments for the chance to own their debt.

It’s an extraordinary set of circumstances but what it means is money is flowing into those markets in an attempt to profit from a massive momentum trade. All that money is helping to support those currencies on a relative basis.

This is the paradox of the debt markets. The biggest debtors, the companies and governments with the most debt outstanding tend to have the most liquid bonds.

One of the biggest concerns of bond traders is not whether the bond is going to default but whether they will be able to sell it later to realise a profit. That ensures the biggest positions are always in the bonds of the biggest debtors. By contrast the bonds of the most creditworthy issuers are not nearly as liquid because there is so little risk, they don’t merit big trading positions.

It’s not that there is no risk in the German, Swiss or Japanese bond markets. Quite the opposite in fact. The reality is these kinds of momentum moves don’t end well.

They look like the strongest thing in the world for as long as they last but when they end, the rush for the exits makes them look like the worst thing in the world. It’s literally as if Mr. Muscle turns into Mr. Bean.

Right now, the bubble is still expanding because investors are willing to bet that the central banks of the world are so terrified of a recession, they will do whatever is necessary to prevent one.

The European Central Bank (ECB) has basically committed itself to an interest rate cut in September. Since the ECB’s main refinancing operations rate is currently 0%, which represents a clear departure from anything that approaches normal monetary policy.

Deposit rates in the EU are already negative but the lending rate is currently positive. A quarter point cut would take that lending rate negative.
The European economy is not yet in recession but Germany is very close to contracting. As a globally oriented major exporter it is suffering most from the slowdown in global growth and the trade war.

The ECB is facing a difficult position. The fiscal austerity regime forced member governments to take on private sector debts to avoid the entire banking system from going bust. The pressure that has put sovereign finances under and the resulting drop in living standards has been one of the root causes of populism blossoming in almost every country in Europe.

From a decade of experience, we know what quantitative easing (QE) is good for. It is wonderful at inflating asset prices but not much else.

The ECB itself has been pretty clear in its statements that it does not think QE is going to cure the eurozone's ailments. Depressing government bond yields across the region is a bonus for bond investors and risk takers but it robs savers by depriving them of a positive carry on their deposits. It also kills banking margins and since the banks are loaded with bad debts that are more than a decade old, they have no capacity to lend.

Mario Draghi upbraided EU governments for not doing more in terms of fiscal stimulus at the policy meeting press conference in July. However, the eurozone is so wedded to fiscal austerity that they cannot bring themselves to admit it is killing the economy and represents an existential threat to the long-held dream of a pan-European federal state.

Without even the potential for fiscal stimulus, the full onus for supporting the eurozone economy rests with the ECB – and QE, negative interest rates and other extraordinary measures are the only tools at its disposal.

It is looking very likely that the ECB is about to kickstart its QE programme again. That is going to increase the quantity of euros in circulation and put downward pressure on the currency. That's a good reason to think that gold's appreciation in euro is going to continue.

The ECB might not be willing to consider fiscal stimulus, but the rest of the world is now going full steam ahead. The US led the way by pivoting almost seamlessly from QE to fiscal stimulus at the end of 2017.

The UK is about to embark on its own version of fiscal stimulus with the new PM's plans. Australia is cutting rates, lowering taxes and easing restrictions on the housing market. China has been running a fiscal deficit in the order of 4% of GDP for the last year and this year is likely to be even wider.

**The Fed to pull the MMT trigger?**

What they are now seeing in the US is that fiscal stimulus needs to be supported by the central bank if it is to stimulate the economy.

When the US government started its fiscal stimulus, through the Trump tax cuts, the Federal Reserve started reducing the size of its balance and raising interest rates. That policy of quantitative tightening (QT) resulted in US economic growth slowing down and the stockmarket taking fright at the prospect of the Fed creating a recession. Many investors concluded that the best of the benefits from the fiscal stimulus are behind us so they started pricing in a recession.

July was a pivotal month for that conclusion. First the Democrats and Republicans agreed to suspend the debt ceiling until 2021 and set spending levels $320 billion above the previous peak.

That's going to take the deficit to $1 trillion a year going forward. It effectively provides an additional $2.7 trillion in additional discretionary spending over the next two years. Not only does this represent an important new stimulus but it effectively takes the issue of the debt ceiling off the newsmagazine until well after the next presidential election.

The original Trump tax cut represented a stimulus of about $2.3 trillion but spread over ten years. The big kicker for the stockmarket was the tax holiday corporations received for repatriating foreign earnings which they used to boost dividend payments and stock buybacks. The new spending bill is considerably larger than the Trump tax cut.

A week later, the Fed cut interest rates and more importantly brought forward the timing
negative, they are not as negative as in Europe. The Bank of Japan and the Shinzo Abe government have never stopped their QE programmes but they are not accelerating them either.

The market seems to be concluding the Japanese monetary and fiscal authorities risk being overtaken by events. That suggests it is only a matter of time before Japan also recommits to additional stimulus.

What all this tells me is we are going to see gold continue to trend higher in the currencies for countries that are now sporting negative yields.

Trade war fallout = good for gold

That was a long first point, so how about the second?

I might have caught your attention that the majority of currencies gold is breaking out against are also commodity producers or commodity traders. The last commodity bull market peaked in 2011 and that thrashed the value of commodity exporters.

The Brexit referendum did the same for the pound. That resulted in gold holding its value in these currencies a lot better than it did against the US dollar, euro or yen.

I favour the Continuous Commodity Index or what is also referred to as the “old CRB” because it is unweighted and therefore gives a more representative perspective on what is going on in the commodities sector.

What is particularly interesting right now is that while gold is breaking on the upside, the vast majority of industrial resources’ prices are breaking downwards. The index has been trending downwards for more than a year and hit new reaction lows at the beginning of the month.

The trade war between the US and China has a lot of moving parts. One of the biggest takeaways is it is falling most acutely on China. That is a problem for a lot of emerging markets and commodity producers. They do more business with China than the US, so if China’s economy is slowing, it’s a problem.

China’s economy is slowing and more importantly it is already doing a lot to support it. China’s fiscal stimulus is larger than that of the US. The total of its corporate, income and sales takes are below the US’s. It is aggressively cutting reserve requirements at its banks and cutting the interbank lending rate.

With that kind of stimulus, one would assume that the economy would be firing on all cylinders but that is not the case. The trade war is taking a toll. At the same time the government is trying to unwind leverage in the property market because it is deeply
fearful of a housing crash.

Defaults are a new thing in China but that also means they represent a complete unknown. It is literally impossible to know what the natural default rate is when everyone has been borrowing, without ever worrying about repayments, for about 40 years.

I'm in China right now and I look forward to reporting on my impressions of the health of the economy. One thing we do know is that the price of gold in renminbi crossed the psychologically important CNY10,000 level in July, suggesting investor interest is picking up.

One thing we know for sure is the Chinese government is buying, and on a regular basis, as it attempts to insulate the currency from the trade war.

Russia and Poland have also both been big buyers. Poland is noteworthy because it does not have a domestic gold mining industry so it is making the purchases purely to insure itself against a calamity. Considering the deteriorating relationship, the country has with the EU, those actions are not surprising. Russia buying gold to insure itself against sanctions is not exactly new but it is an important source of demand.

It's not only governments which are buying gold. Investors are also boosting their holdings and that is driving the uptrend in total holdings of exchange-traded funds (ETFs) which now stand at almost 75.6 million ounces or 2,650 tonnes.

Investors are one of the most important sources of new demand for physical gold. That is also driving the continued outperformance of gold shares relative to the gold price.

“Investors are also boosting their holdings and that is driving the uptrend in total holdings of exchange-traded funds (ETFs) which now stand at almost 75.6 million ounces or 2,650 tonnes.”

As the outlook for gold continues to improve, I am adjusting the buy-up-to limits on a number of our portfolio positions:

- **Shanta Gold** has posted three consolidations this year and each has latest a few months. However, the pace of the advance is picking up and the share looks primed for another leg on the upside. Therefore, I am raising the buy-up-to price to 10p.

- **Hochschild Mining** is performing very much in line with silver so it paused in late July as the silver price pulled back. This is exactly what I meant when I said precious metals are volatile. I regard this pullback as a buying opportunity and am now raising the buy-up-to price to 230p.

- I am expecting **Polymetals’** earnings to be flattered by the recent strength in underlying metal prices so I am raising the buy-up-to price ahead, of the 24 August earnings call, to 1,070p.

- I believe the recent setback we have seen in platinum is temporary in nature and therefore I am raising the buy-up-to price on Sibanye Gold to $5.50.

- I am not raising the buy-up-to price on **Newcrest** because the price is accelerating and therefore susceptible to volatility.

For the same reason I am not recommending anyone add to the position in gold when denominated in pounds just yet. There is too much risk of the pound bouncing to make that a wise trade at this time.

Now, what other gold miners are looking interesting right now that we can buy?

**This week’s recommendation:**

**BUY McEwan Mining (MUX)**

Rob McEwen did something back in 2000 that had never been done before and is still a very rare endeavour. He gave away Goldcorp’s geological data. Generally, miners see their drilling data as proprietary and are very jealous of who has access to it.
However, McEwen had been at an MIT conference in 1999 where people were talking about how the internet could be used as a collaborative resource. He used Linus Torvalds and his success in building the Linux software operating system as an example.

McEwen decided to crowd source a solution to Goldcorp's drilling needs. The Red Lake mine had been a serial underperformer but the company's geologists were convinced the property's primary ore body was deeper underground. They had no idea how to find it though.

Subsequently, a challenge was launched for anyone who wanted to enter – to find the best drilling site. The prize of C$575,000 attracted more than 1,400 contestants from all over the world. More importantly, the success of the subsequent drilling operations turned Goldcorp from a minnow into a major gold producer.

Back in 2000 the idea of crowdsourcing drilling information was nothing short of visionary. That's what McEwen is: a visionary.

| His target for the end of this year is $1,700. When Newmont Gold's acquisition of Goldcorp closed earlier this year it was one of the biggest gold mining mergers in history. That's why my ears pricked up when McEwen said in an interview with Kia Hoffman of Oreninc last week that he expects his new venture McEwen Mining to grow large enough to be an S&P 500 company. |
| The only way that objective is going to be achieved is through significant discoveries of new gold. The company is a producer but that is only a fraction of the ambition of the management team. |
| C$575,000 attracted more than 1,400 contestants from all over the world. More importantly, the success of the subsequent drilling operations turned Goldcorp from a minnow into a major gold producer. |
| The company is also spending $18 million this year at its Timmins properties in Canada where a similar drilling at depth operation is underway. |

Goldcorp's success was in securing properties that had high grade gold at depth. That is exactly what McEwen Mining is also looking to achieve. It's how a minnow turns into a major.

McEwen has stated the company is in the market for mergers. In the meantime, it has been buying property in Nevada, along the Carlin Trend and in Canada along the Timmins Trend. The Gold Bar property in Nevada achieved first pour in May. It expects 42,000 ounces this year at an all-in sustaining cost of $975.

However, the biggest point is the company has $15 million in spending planned for this year to try and confirm deeper mineralisation at the property, which is a feature common to other Carlin Trend properties. If that is successful, it will transform the prospects for the mine. The company is also spending $18 million this year at its Timmins properties in Canada where a similar drilling at depth operation is underway.

One of the primary arguments against investing in the company is the short mine life of some of its primary assets. However, it is also worth remembering that the reason the company owns these assets is because it believes it can radically extend mine life through additional drilling.

That is the optionality an investor is taking by opening a position in the shares. You are betting on a miner with a solid history of game-
Here is a rundown of the company’s principle assets from its website:

The Black Fox mine in Timmins, Canada which is one of the best mining jurisdictions in the world; the San José mine in Santa Cruz, Argentina (49% interest); the El Gallo Fenix project in Mexico where they have recently extended the mine life an additional 12 years; the Gold Bar mine in Nevada which is targeting production in early 2019; and the massive Los Azules copper project in Argentina which is advancing towards development.

The primary point that is now supporting the share is that the weather issues which inhibited supply in the 1st and 2nd quarters are now behind it. The company expects better results in the second half with feasibility studies from the previous drilling operations expected.

One of the reasons to own the share is the company has a beta of 3 relative to the gold price. That tells us this is a company that is highly leveraged to the gold price.

If the price continues to rise, it can be expected to go up three times more than the rise in the gold price. The other side of that equation is that if the gold price declines, the share would fall three times more than the gold price.

The reason for investing in gold shares is to get leverage to the gold price so this is one of the primary reasons I am recommending you buy this share.

One of the reasons the share has such high beta is because of its relatively high all-in sustaining cost of production, which is currently at $1,034. The higher the gold price goes, the quicker the company goes into a sustainably profitable position.

One important point to be aware of is the growing position the company has in copper production. Its 51% interest in the Los Azules mine is costing $2.6 billion to produce but that should be paid back within three years of production starting. With a 30-year mine life the internal rate of return, after tax, is 20%. The share has rallied over the last ten weeks to break its more than 18-month downtrend. In that regard it is trading much more like a silver stock than a gold stock and it does not have substantial silver assets in addition to its gold.

I rate the share a buy up to $3.50 and my 18-month target is for the share to at least retest its peak from 2016, which was $6.

Action to take: Buy McEwen Mining Inc
Ticker: MUX US
Market cap: $698 million
52-week high/low: $2.44/$1.23
Price as of 13.08.2019: $1.89
Buy up to: $3.50

“The reason for investing in gold shares is to get leverage to the gold price so this is one of the primary reasons I am recommending you buy this share.”
The Gold Stock Fortunes Portfolio

### Gold plays

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<th>Price Then</th>
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### Precious Metal plays

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### Risk warning

General – Your capital is at risk when you invest. You can lose some or all of your money, so never risk more than you can afford to lose. Past performance and forecasts are not reliable indicators of future results. Commissions, fees and other charges can reduce returns from investments.

The Financial Conduct Authority does not regulate certain activities, including the buying and selling of commodities such as gold. This means that you will not have the protection of the Financial Ombudsman Service or the Financial Services Compensation Scheme.

Small cap shares - Shares recommended may be small company shares. These can be relatively illiquid meaning they are hard to trade and can have a large bid/offer spread. If you need to sell soon after you bought, you might get back less that you paid. This makes them riskier than other investments.

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