



Tocqueville Gold Strategy Investor Letter Third Quarter 2016 Investor Letter

BY JOHN HATHAWAY ON *OCTOBER 12, 2016*

During the third quarter of 2016, gold and gold mining shares consolidated in a narrow range following substantial gains in the first half of the year. On a year to date basis (9/30/16) gold bullion rose 24% while most gold mining shares gained 3x-4x the gold price.

During the first few days of October, the gold price broke sharply lower beneath the consolidation range of the third quarter. The decline in gold accelerated after breaking through technical support zones clustered around \$1300/oz. in only a few days. High frequency and short term momentum traders piled on as they typically do when technical support is breached. Intense short selling by these players accelerated the market decline. Bearishness has replaced the euphoria and overconfidence that dominated only a few months ago in early July. It must be remembered that these short term gyrations reflect synthetic or paper trading, which we have discussed frequently over the past two years, and is almost completely disconnected from flows of physical metal.

Long term, we don't think this washout signals a structural change in gold's outlook; it may have been a clean-out of weak holders as prices recalibrate lower towards physical support from Asian buyers. The correction of the past few days coincided with an absence of Chinese buyers due to the "Golden Week" holiday there. "With China (by far the largest buyer of physical gold) closed, the markets were open for

rampant manipulation, which is exactly what happened as several billion dollars in paper assets were dumped.” (Zero Hedge Oct. 9, 2016) As noted in the October 10 Belkin report, “who sells \$22 billion of gold for maximum market impact over a very short period of time? The global monetary cabal (central banks, BIS) have a long history of suppressing gold prices because a rising gold price discredits their legitimacy. But never mind, gold is still up 18% year to date ...even after last week’s intervention.” As the charts below show, this intervention was very similar to the previous two years. Paper losses inflicted by synthetic speculators during Golden Week were recouped in the subsequent trading sessions.



Source: ZeroHedge.com

To us, it looks like a bull market shakeout triggered by worries over rising interest rates and perceived lack of action by central bankers, especially in Europe, to expand monetary stimulus in response to a growing banking crisis at Deutsche Bank, Unicredit, etc., all orchestrated with virtually no physical gold being transacted. We would expect to see a sharp reduction in speculative COMEX long positions over the next few weeks as confirmation that the shakeout has run its course.

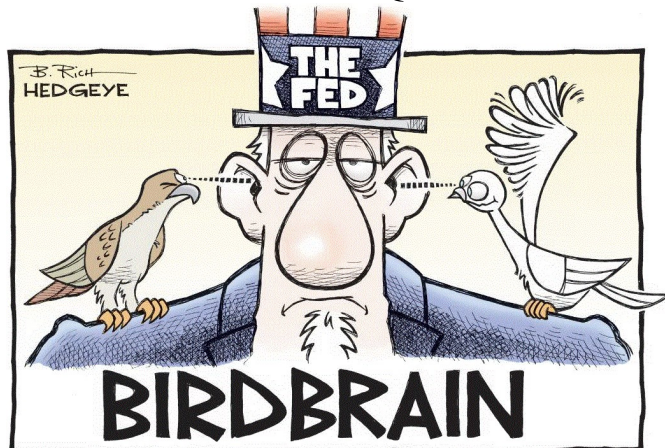
One must ask whether anything has really changed in terms of the investment rationale for gold. In our opinion, gold began a second leg of a long term bull market at the end of 2015. Bull market shakeouts are a regular feature of longer term price advances and serve to restore the component of doubt necessary to reconstruct the wall of worry characteristic of all bull markets.

In our opinion, systemic risk continues to grow in a stealthy manner and is only manifested episodically, as in the current European banking crisis and in the fragmentation of the political consensus that was once the foundation for the Eurozone and the euro itself. Investors in gold should find reassurance in the palpable decay of investor confidence in central banking and radical monetary policy. There is scant reason, in our opinion, to expect waning confidence to revive. In fact, there is substantial evidence to suggest that ultralow

interest rates, ballooning fiscal deficits in Western democracies, and competitive currency devaluations are jelling into a negative feedback loop for global economic growth. We believe the most likely macroeconomic scenario for years to come is a Japanese like twilight zone that oscillates between feeble growth and periodic downturns.

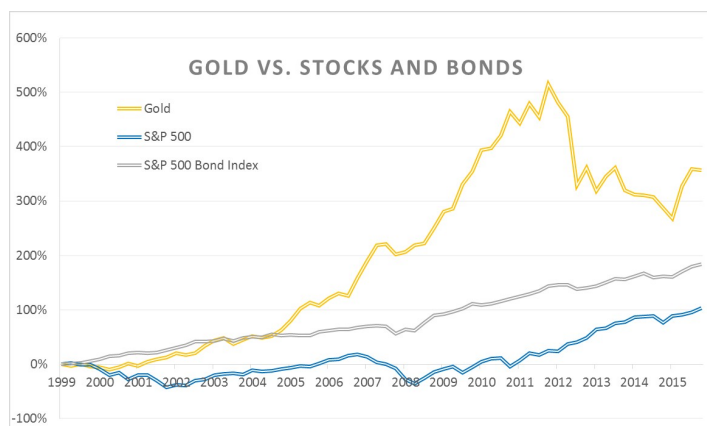
In our opinion, numerous catalysts are aligning to stoke broader interest and a renewed advance in gold prices:

- Spreading loss of confidence in central banking, both from investors and policy insiders. Trial balloons to eliminate cash, ramp up fiscal deficits, and push nominal interest rates below the zero bound seem to proliferate. Commentary in main stream financial media openly questions the efficacy of ultralow interest rates and QE to stimulate economic growth.



- Interest rates appear set to rise on a schedule not orchestrated by the Fed but by the financial markets. Both political candidates favor fiscal stimulus that will inflate deficits at a time when non US buyers of treasuries, a principal source of demand in recent years, have been in a liquidation mode for the past twelve months. In our opinion, a continuation of rising interest rates will lead to steep capital losses for holders of low to negative yielding sovereign debt, and cause considerable collateral damage to equities.
- Global gold mining production, in our opinion, appears locked into an irreversible decline for the next 5 to 10 years. Because exploration has slowed sharply, there are fewer new deposits to mine. Industry reserve life is dwindling. Barriers to new mine construction seem more formidable than at any time for the past twenty years.
- The US economy is cruising at stall speed on a best case basis and more likely teetering on recession. Should interest rates rise at this precarious juncture, monetary policy, perceived to be in a tightening mode, could be forced into another phase of QE or even more radical measures.
- Gold is extremely under owned in Western investment portfolios. Because supplies of above ground stocks normally available to satisfy Western investment demand have been severely depleted by flows to Asian investors, the price dynamics could be explosive.
- Gold has enjoyed a stealth bull market since the advent of radical monetary policies around 2000. As the chart below shows, gold has been the best performing asset class since then, a fact that is completely unrecognized by main stream media and conventional investors. The painful correction

from 2011 to year end 2015 camouflaged gold's strength and explains why most investors remain complacent as to systemic risk, intellectually understanding the unsustainability of radical monetary policy but unmotivated to seek gold's protection.



It seems unlikely that the long term erosion of investment confidence, the onset of a secular bear market in financial assets, and further advances in the stealth bull market for gold will take place in a linear fashion. There are bound to be shakeouts and fake outs along the way to camouflage the underlying reality that the global financial system as we know it is in extremis. We also believe that the current sharp correction in the precious metals complex is a setup for another major advance toward new highs in metal and share prices. We therefore recommend taking advantage of current weakness to build or establish new positions.

Tocqueville Gold Monitor

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