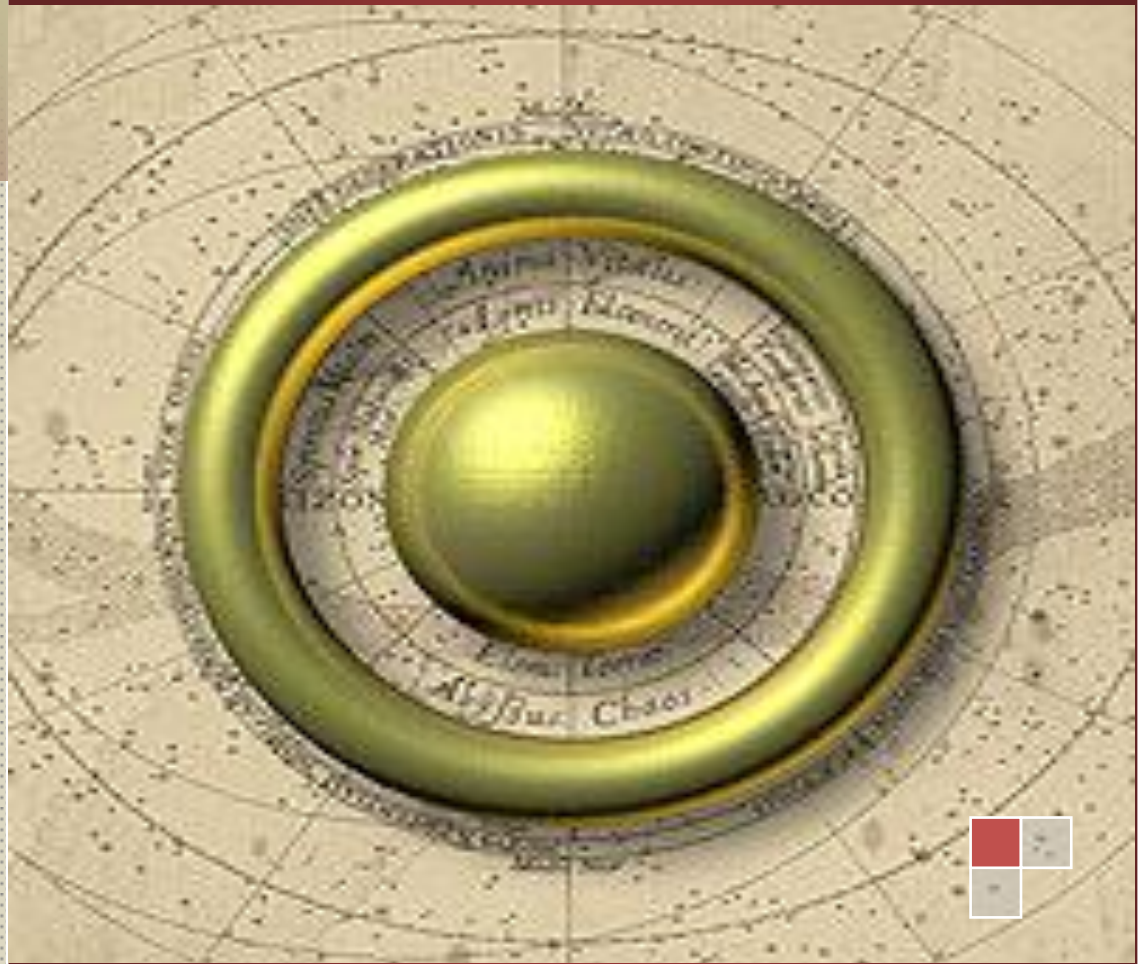


Apr '09

PRECIOUS METALS

GOLD
Q2 OUTLOOK



The downturn in the economies have resulted in reduction of interest rates to near-zero levels, buying back of debt, bailout of banks and expenditure worth trillions of dollars to infuse liquidity in the market. This has kept investors in mayhem with some investing in gold due to uncertainty hedge while others looking after the inflation hedge characteristics. Optimism over sooner economic recovery with some plans showing their effects, have resulted in rally in equity markets, reducing the appeal of gold. Prices may now witness correction and then rebound in later half of 2009.

Reviewing Q1 2009

The start of the year was in positive trend as the increasing uncertainty and the panic stricken markets withheld the support for bullion prices. This report comes in sequel to the yearly update wherein fundamental outlook of high prices was underway. The investment avenue for bullion took the forefront during the Q1 2009 as the global economy slipped into grave recession. The spiraling crisis, with the bleak economies has resulted in the sell off of major asset classes. The liquidity crunch witnessed has drained out resources of investment in most of the assets.

The beginning of the year was promising for bullion as it mostly traded high reaching the pinnacle at \$1007.7 in the month of February. The cascade of poor economic numbers in conjunction to the spiraling crisis and the recession stricken economies have helped support the momentum in gold prices. Few significant economic events have taken place in this quarter which were very prominent in determination of the future of the global economies. The U.S presidential election, billion dollar stimulus plans, deepening recession, G-20 meeting were to name a few.

Prices gained as uncertainty was high in the market due to weak economic data and lack of detailing by the US Treasury Secretary in regard to the new bank bailout plan. Final estimates of -6.3 % U.S gross domestic product Q4, highest unemployment of 8.5% since 1992, record-low consumer confidence, and declining personal income and spending in the US also contributed to the rise in bullion prices. Demand for gold as an inflation hedge grew after the US Congress passed the mammoth \$787-billion stimulus package. Moreover, the financial crisis, which has resulted in a recession in most developed nations, prompted some investors to buy gold.

Prices surpassed the \$900-mark after the U.K economy recorded a second consecutive negative economic growth (-1.5% in Q4, the steepest since 1980), confirming the recession in the region, and the Royal Bank of Scotland posted its biggest loss. Record-low U.S housing starts, building permits, consumer confidence also supported the uptrend in gold prices. There on prices breached the crucial psychological levels of \$1,000/troy ounce and tested a monthly high of \$1,007.70 levels

Interestingly, prices of gold and dollar displayed a positive correlation in February, recording multi-month highs of \$1,007.70 and 1.2455 levels (against one euro) respectively. This is because gold is regarded as a safe haven during economic uncertainty and the dollar is treated as a safe currency due to liquidity tightening. Historically, prices of gold and dollar are negatively correlated due to their distinct asset characteristics. However, given the current economic emergency, both these assets are being considered as a safe haven.

Investment in the SPDR Gold Trust has increased phenomenally as the investor sought the safe refuge in term of uncertainty. In this year alone, the funds in the SPDR Gold Trust have reached a

record high of 1127.68 metric tonnes surpassing the national reserves of Switzerland. For the year 2009, funds climbed at an astounding rate of 44.53% as the participation in these funds gains significance with the surge in bullion demand.

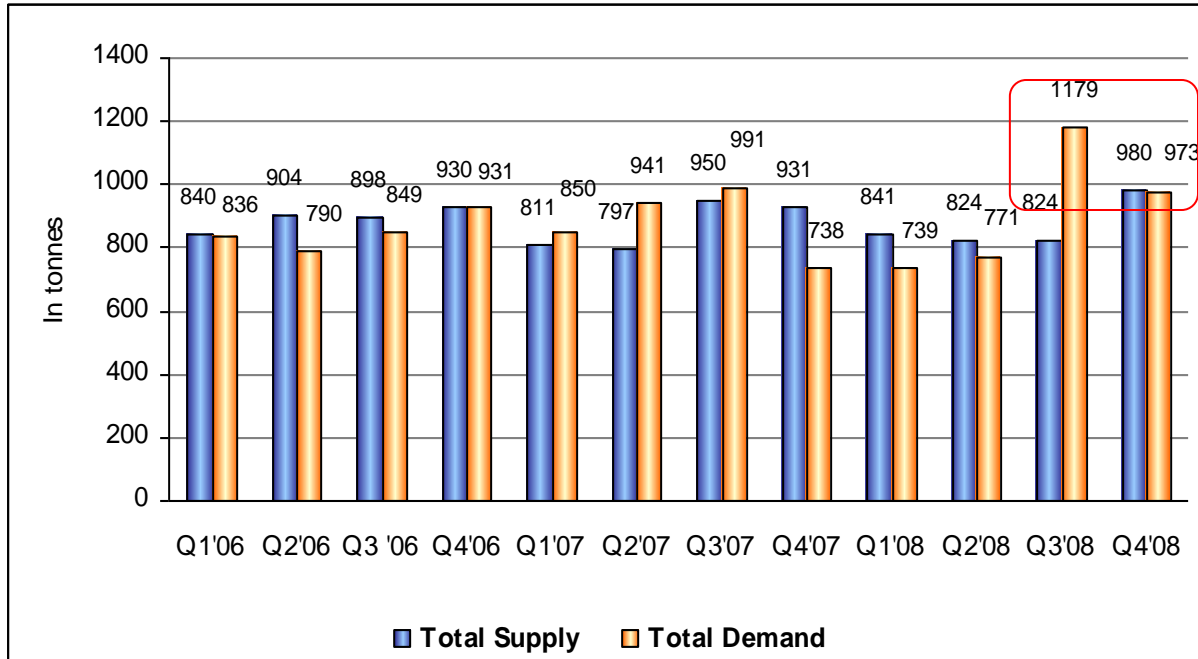
What experts say?

The high rise in prices in Q1 has adversely affected the jewelry demand for the yellow metal. With prices flaring up towards the \$1007.07 per troy ounce in February left most of the consumers to trim down consumption. The demand has been price sensitive in markets such as India and Turkey which was the most hit during this term of high rise in prices. In fact, Indian imports of gold in the month of February and March remained near to zero compared to the previous year's figure of 23 and 60 tonnes in 2007. The jewelry demand in fact is the top notch use of the yellow metal. This constitutes of about 70% of the total demand of the metal followed by investment and industrial demand.

According to GFMS gold survey 2009, total fabrication demand for gold dropped by 7% to 2,850 tonnes in 2008, its lowest level since 1988. Most of the decline in demand was due to the jewellery sector. The principal reasons for this were high and volatile gold prices, together with the downturn in the global economy. The Indian market was the worst affected in terms of volumes while U.S jewellery consumption fell by nearly one-third last year to its lowest level in GFMS' 20-year series. The only bright spot was seen in China where investment-related demand contributed to a notable rise in jewellery offtake. The largest drop for other fabrication occurred in electronics, a result of the economic downturn leading to depressed orders and supply chain de-stocking.

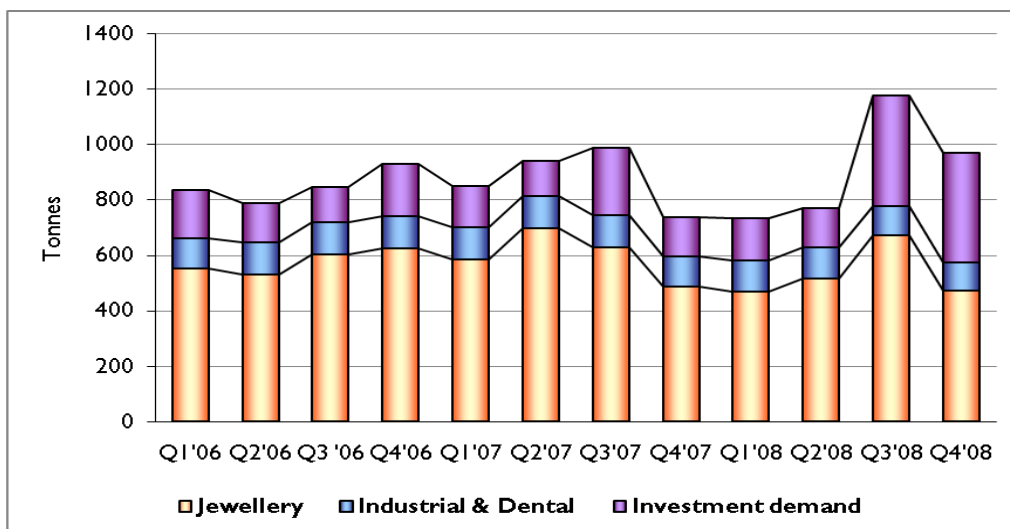
The survey also points out that implied net investment demand in 2008 gained by nearly 76%, with a significant amount of support arising from record inflows into gold ETFs during the year. Official coin minting hit a two-decade high, climbing by over 40% on the back of demand in North America and Europe.

Scrap supply increased by 27% to over 1,200 tonnes in 2008 due to rising gold prices and the economic downturn.



Source: World Gold Council

Figures released by World Gold Council shows that gold demand remained strong during Q4 2008 with total identifiable demand was up 214.7 tonnes (26%) on the levels of Q4 2007. The organization said that the biggest source of growth in demand for gold, during Q4 and 2008 as a while, was investment demand. Identifiable investment demand reached 399.0 tonnes in Q4, up from 141.4 tonnes in Q4 2007, a rise of 182%. Demand in 2008 was 64% higher than in 2007, equivalent to an additional inflow of \$US15.2bn. Taking into account implied investment, which includes the more speculative side of the gold market, total investment was \$US10.1bn higher than in 2007. Due to global economic slump, Industrial and dental demand declined 10% relative to year-earlier levels while the electronics sector demand was also been hit hard.



Source: World Gold Council

Meanwhile gold supply in Q4 2008 was up 5% relative to year-earlier levels and year-on-year it declined by 1%. Lower net central bank sales were partly offset by slightly higher mine production, reduced levels of producer de-hedging and sharply higher levels of scrap. Net central bank sales in 2008 totalled 279 tonnes, down from 501 tonnes in 2007.

| Supply | Q1'07 | Q2'07 | Q3'07 | Q4'07 | Total 2007 | Q1'08 | Q2'08 | Q3'08 | Q4'08 | %Chng Q4 08 Vs Q4 07 | Total 2008 |
|-----------------------|-------|-------|-------|-------|------------|-------|-------|-------|-------|-------------------------|------------|
| Mine production | 590 | 613 | 640 | 630 | 2473 | 550 | 589 | 634 | 634 | 0.6 | 2407 |
| Net producer hedging | -94 | -197 | -82 | -74 | -447 | -128 | -126 | -63 | -45 | | -362 |
| Total mine supply | 495 | 416 | 558 | 557 | 2026 | 422 | 463 | 570 | 588 | 5.6 | 2043 |
| Official sector sales | 72 | 154 | 178 | 97 | 501 | 80 | 86 | 42 | 71 | -26.8 | 279 |
| Old gold scrap | 243 | 227 | 215 | 277 | 962 | 339 | 275 | 211 | 320 | 15.5 | 1145 |
| Total supply | 811 | 797 | 950 | 931 | 3489 | 841 | 824 | 824 | 980 | 5.3 | 3469 |
| Demand | | | | | | | | | | | |
| Jewellery | 586 | 698 | 630 | 488 | 2402 | 472 | 519 | 672 | 475 | -2.7 | 2138 |
| Industrial & Dental | 116 | 118 | 117 | 110 | 461 | 111 | 112 | 108 | 99 | -10.0 | 430 |
| Investment demand* | 148 | 125 | 244 | 141 | 658 | 153 | 140 | 399 | 399 | 183.0 | 1091 |
| Total Demand | 850 | 941 | 991 | 739 | 3521 | 736 | 771 | 1179 | 973 | 31.7 | 3659 |

* Investment demand includes demand from bar & retail coin investment, ETFs & similar and other retail investment

Source: World Gold Council & KCTL research

Is gold-dollar repeating history?

Since January 2009, the world's two major financial instruments, gold and dollar, have once again began moving in tandem. The last time they moved together was between May and November 2005. Traditionally, the long-term trend for gold and dollar has been inversely correlated because the yellow metal is considered as just another form of currency. Although gold is not "money" in the true sense of the term, it tends to move like one. As a result, gold is often regarded as an alternate asset class compared to, say, assets denominated in US dollars. In such a scenario, it is often observed that when the greenback depreciates in the foreign exchange market, bullion prices will generally increase in dollar terms. Similarly, if the dollar strengthens, gold prices usually fall.

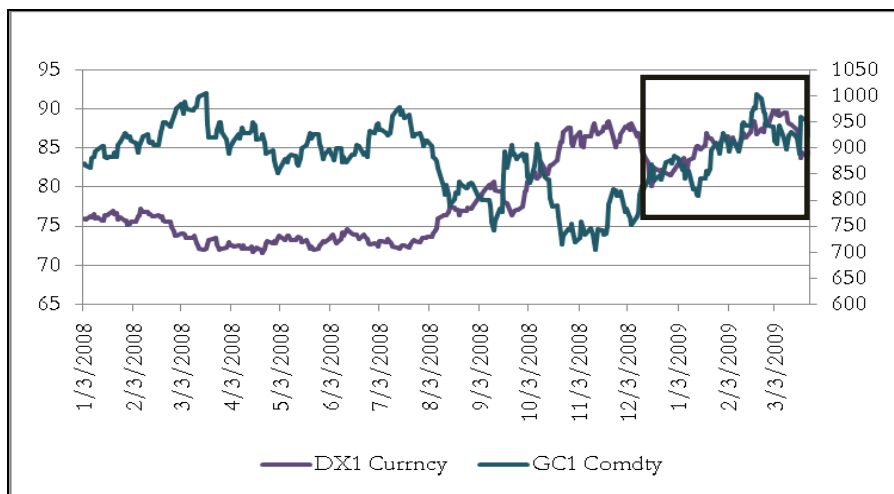
The recession has now created two categories of asset classes. We can call one category as safe-haven assets, while the other can be referred to as economic barometer instruments. A safe-haven instrument is one that attracts a lot of investment demand during economic and financial uncertainty. On the other hand, economic barometer instruments are associated with the performance of an economy, say, for example, equities, consumption goods, among others. In the current scenario, both these categories of asset classes are mutually exclusive—that is, if economic barometer instruments rise when, say, banks in the US post profits, the price of safe-haven instruments tends to decline. Conversely, if recession is expected to deepen in the coming months, the price of safe-haven assets would increase while equity stocks tend to fall.

Meanwhile, the correlation of gold with other asset classes has also changed in recent months. For instance, gold and crude oil used to move in tandem earlier when oil rallied in the first half of 2008. Now, however, they are quite un-correlated. The positive correlation could be attributed to the inflation hedge demand for the yellow metal, fuelled by crude oil prices as the latter skyrocketed to peak levels of \$147.27 in July 2008.

However, as circumstances changed in the wake of global recessionary fears, both gold and crude oil showed an inverse relationship. The falling crude price was an indicator of falling demand and global slowdown underway, which prompted investors to move to safe-haven assets like gold. Likewise, as the economic scenario in the Euro-zone and Japan deepened, the dollar shared a whole new relationship as a safe-haven asset with gold, and started moving in tandem with each other.

Moreover, gold and equity markets, which used to move together earlier, are now inversely correlated. That is because when the economy was growing earlier, inflation and investment demand for gold remained high. On the other hand, given the economic downturn and weak stock markets, gold prices have surged due to its appeal as an alternate asset class. In fact, as we go to press, global stock markets have risen by about 25% from its lows on March 9, and, needless to say, bullion prices have taken a beating during the same period, further underlining the inverse correlation.

Figure 3: Current scenario—Dollar-gold correlation



Source: KCTL Research

Table 1: Gold correlation trend with other asset classes

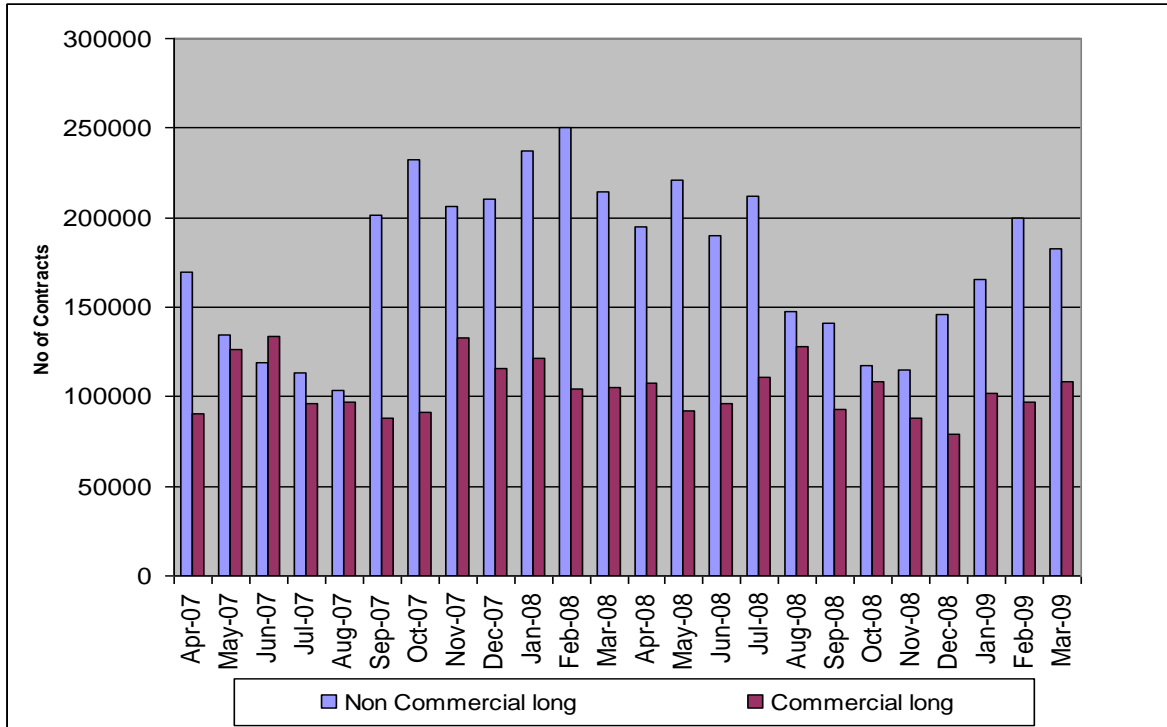
| Particulars | 2007 | 2008 | 2009* |
|--------------|-------|-------|-------|
| Crude oil | 0.91 | 0.58 | -0.04 |
| Dollar Index | -0.92 | -0.84 | 0.61 |
| EUR/USD | 0.94 | 0.82 | -0.67 |
| Dow Jones | 0.42 | 0.66 | -0.62 |
| FTSE | 0.18 | 0.64 | -0.52 |
| Hang Seng | 0.90 | 0.69 | -0.40 |

*Data as of March 18, 2009.

Source: KCTL Research

Commodity Futures Tarding Commission report

The commodity futures trading commiosn provides with the status of the open positions which act as a guage of the market activity. The participants are divided into Commercial and Non Commercial positions which help attain an insight into the pulse of the market. In the Q3 andQ4 of 2008 a decline in the commercial and the Non commercial longs was seen, due to the credit crunch, which lead to the major sell off in the market. Nevertheless the spiralling crisis brought back investment demand into the market and the total longs were seen to mark an increase in Q1 of 2009 indicating a rise in participation.



Source: bloomberg & KCTL Research

The good and bad news of Q1 2009

The weakening economies have invited a range of measures by the governments in order to stall the economy from further downfall. The central banks across the globe have spent trillions of dollars and slashed interest rates to near zero in order to lubricate the stagnant consumer spending. Many of the economies stuck with falling industrial activity, contracting growth rates and the spiraling crisis seem to turn to grave. With the governments pumping in more money into the market and demand being blindly absent, the fear of global deflation has caught up. Following are the few significant economic measures taken during the first quarter 2009 affecting the bullion market:

- ❖ US bailout package of \$787 billion comprising of about 35% tax cuts.
- ❖ Bank rescue plan of \$500 billion with an addition of \$500 billion, if required

- ❖ Obama's budget for fiscal 2010 amounted to \$3.5 trillion, and it was aimed at overhauling the country's education and healthcare system. The budget was approved by the US House and the Senate.
- ❖ Obama pledged up to \$275 billion to help stem home foreclosures and finance private investors to buy illiquid loans and securities held by banks.
- ❖ The Federal Reserve planned to add a further \$1.15 trillion to its balance sheet and G20 nations pledged to use their full fiscal and monetary firepower to combat the economic crisis.
- ❖ The US Federal Reserve keeping its key interest rates unchanged at 0.25% and announced a massive \$1.15 trillion quantitative easing program to buy debts, bonds and long-term treasuries, helped boosting demand for the precious metals.
- ❖ The Fed Chairman pointed out that he sees a US recovery beginning in 2010 as long as there is enough political will to take its costly rescue plan to its logical conclusion.
- ❖ The U.S Treasury, Federal Reserve and Federal Deposit Insurance Corp., said that they will provide private investors with financing to buy illiquid loans and securities held by banks.
- ❖ The European Central Bank (ECB) reduced its main refinancing rate by 125 basis points to 1.25%.
- ❖ G20 Meet arrives at a figure of \$1.1 trillion, with increased regulation of hedge funds and the financial sector, and shoring up the resources of the IMF and the World Bank to help them facilitate the finances of some of the poorer countries in the current scenario.
- ❖ Global equity markets rallied by around 25% since their March 9th lows
- ❖ Financial services majors, Bank of America, JPMorgan and Citicorp stated that they had operated profitably in the first two months of 2009.
- ❖ China implemented the second allocation of its \$586-billion stimulus package
- ❖ US unemployment rose to 25-year high of 8.5% and gross domestic product shrank by 6.2% in Q4 2008.

View from fundamentals

Given that gold is now positively correlated with the dollar, many question whether the yellow metal has decoupled from the greenback? However, before one can jump to conclusions, we would like to point out that this positive correlation is purely a temporary phenomenon. We do not expect gold to decouple from the dollar as gold is also regarded as an investment asset or rather an alternate asset class, thus inevitably related to the currency market, especially the dollar.

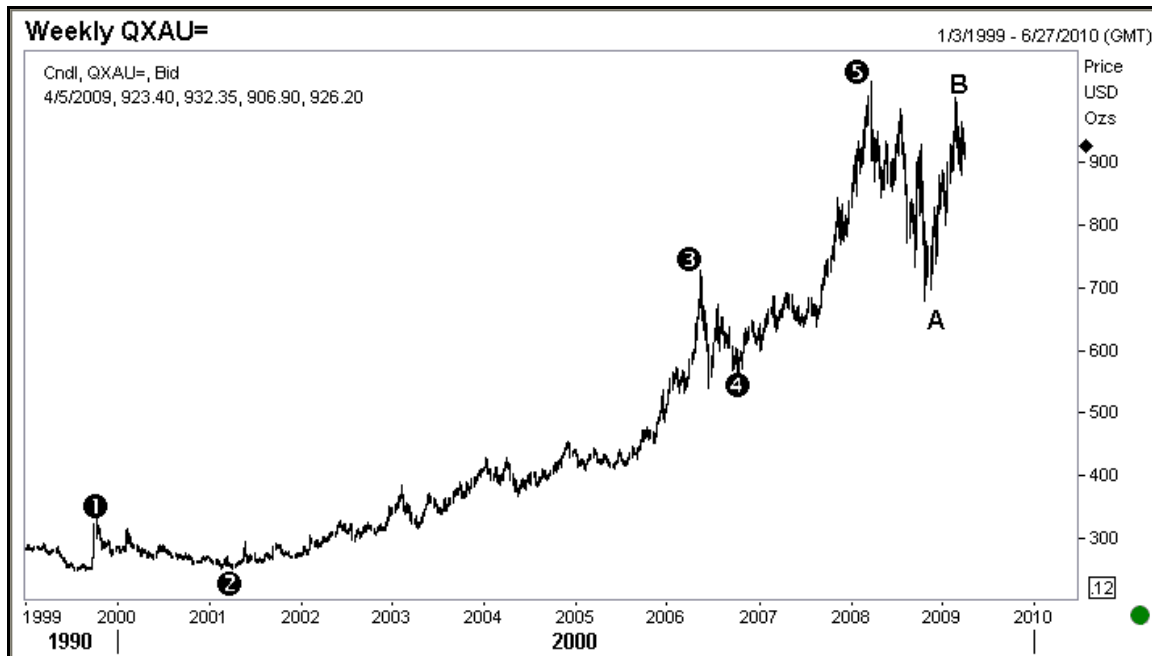
Trillion dollars spending by government across the world is likely to fuel the inflation in the economy. However this will be in a medium to long term, say for after one or two quarters. In the current situation, host of measures are taken up by several countries in order to protect their economy from further downturn. International Monetary Fund (IMF) now expects the global economy will grow by 0.5% in 2009, its lowest rate since World War II. The advanced economies are expected to record a negative growth of 2% while emerging and developing economies is estimated to grow by 3.3%.

Investor's sentiment about the market is likely to improve after the recent spat of economic revival measures. Equity markets have moved higher sharply from the recent lows as optimism grows that worst of the financial crisis may be over soon. Money markets have started easing as global central banks cuts interest rates to record lows. Currently LIBOR 3-month USD stands at 1.31% when compared to peak level of 4.82% in 2008.

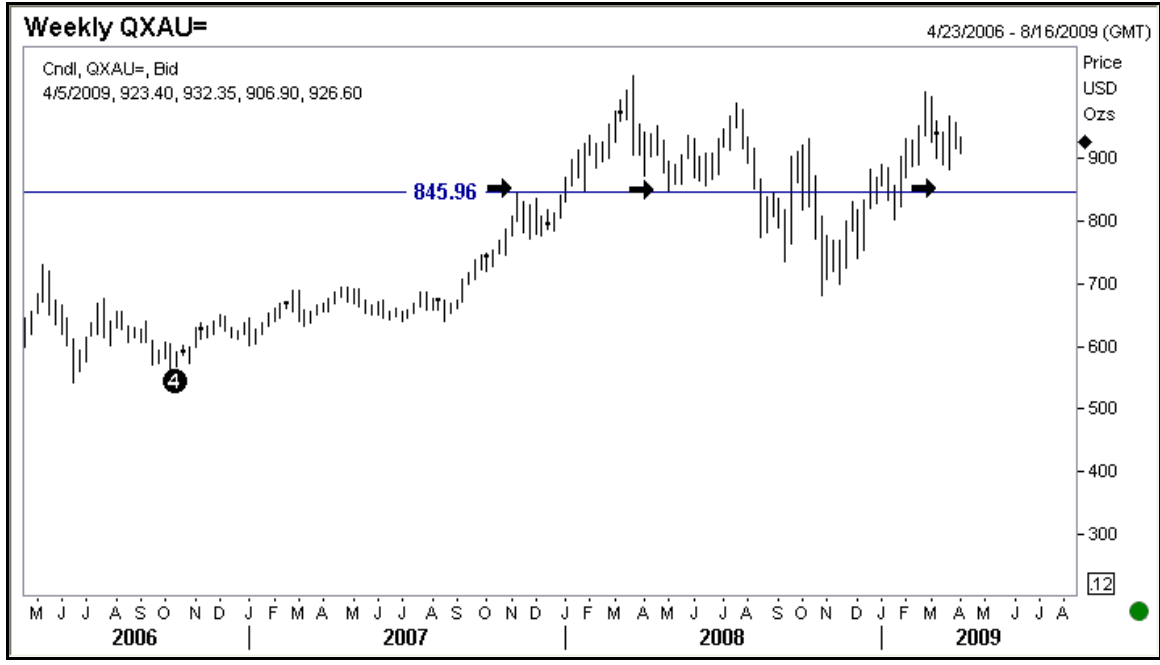
On the demand front, the extent of jewelry demand will depend upon the gold prices. World Gold Council says that while western markets are expected to continue to struggle, dips in the gold price could trigger bouts of buying in some non-western markets, similar to what was seen in both Q3 and Q4 2008. Central banks sales of gold have been low in last quarter while market now speculates that IMF may sell gold in addition to its sale of 403.30 tonnes in April 2008. More selling of gold may increase supply and reduce the liquidity pressure in the market, driving gold prices lower.

Considering all these factors, we expect gold prices to witness correction in Q2 2009 and are then likely to rebound by the year end.

View from technical's



Since 2000 till today, spot gold have been moving higher somewhere around \$250 and made a lifetime high of \$1033 levels. The price move of gold has been justified by Elliot wave principle. If the psychological behaviors' of investors are correct, then market needs to take a brief correction.



Above chart says, on break of \$882-890 range, market can slip to \$845 (various highs and lows in the weekly chart)



Market is moving in a trend channel. Break out and one weekly close below the trend line would confirm the fall towards \$845



Zigzag or indecisive consolidation move of gold prices after the lifetime high of \$1033



Now, in the daily chart, prices are firmly holding above the trend channel. Moreover, a Head & Shoulder pattern is seen forming with the neck line support at around \$880 levels. On break of \$880, it can fall to \$845 and then \$800-780 levels.

At this juncture, no analysts could say the Head & shoulder pattern is likely to make a neckline break out.

In the 1st chart, we have said end of Wave-B, means a sharp corrective WAVE-C is awaited. May be this would be confirmed only at the break of neck line support of Head & Shoulder pattern.

Our stance: Break below \$880, can drag the prices to \$800-780 range.

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