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Public Policy Economics

KEY INSIGHTS

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Predicting Gold Prices with the Keybridge U.S. Momentum Monitor

Key Insights

- Our analysis shows that the Keybridge U.S. Economic Momentum Monitor can be used as a predictive tool by investors to forecast movements in gold prices.
- An examination of historical data indicates that higher Momentum Monitor values precede periods of falling gold prices, and lower Momentum Monitor values precede rising gold prices.
- Transforming the Momentum Monitor into quartile scores lends itself to an easily interpretable signal of movements in gold prices over the next 6 months.

Keybridge's U.S. Economic Momentum Monitor is predictive of gold price movements.

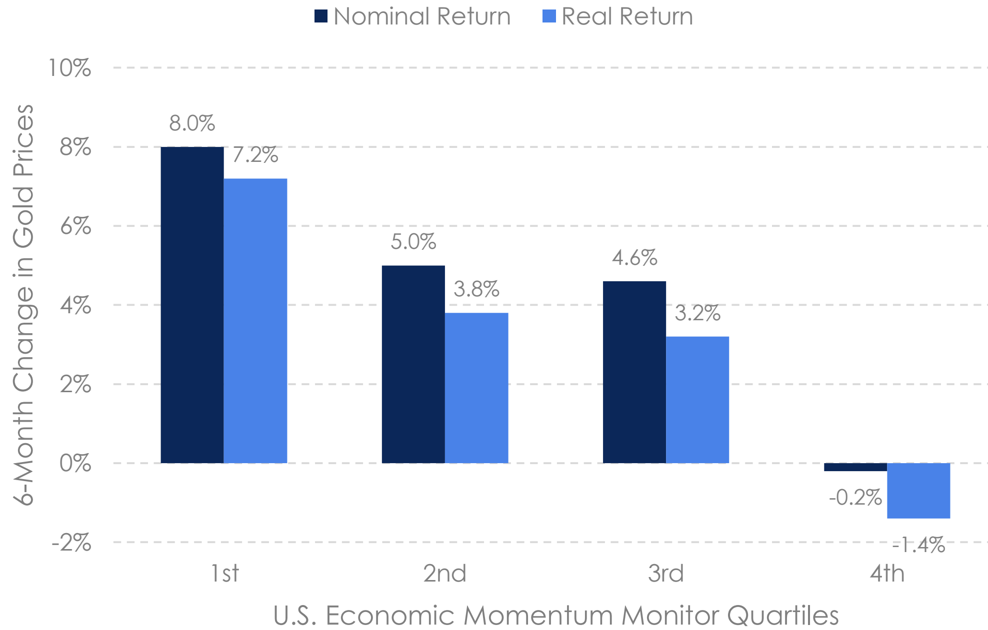
Investors typically use gold as a hedge against slower economic growth and rising inflation. As with any asset class, timing is critically important to profitable investing in gold. However, it is notoriously difficult to forecast changes in gold prices. As Warren Buffet said, "the problem with commodities is that you are betting on what someone else will pay for them in six months." While predicting short-term volatility in gold prices is extremely difficult even for the most sophisticated investors, Keybridge has developed an analytical tool that is statistically proven to identify shifts in U.S. economic growth, and in turn, is also useful in anticipating the level of gold prices in 6-months.

Predicting Gold Prices with the Keybridge U.S. Momentum Monitor

More optimistic readings of the U.S. economy are associated with falling gold prices.

Based on an analysis of data from 1995 to 2013, we found that the Keybridge U.S. Economic Momentum Monitor is a statistically valid predictor of future gold prices. Figure 1 (below) shows that, when the U.S. Economic Momentum Monitor is broken into quartiles, a clear pattern in future gold prices emerges. Specifically, higher Momentum Monitor Index readings predict low to negative returns on gold prices over the subsequent 6 months; and low Momentum Monitor Index readings predict higher 6-month returns on gold. For example, when the Momentum Monitor Index reading is in its first quartile, the average increase in gold prices over the next 6 months is 8.0% (7.2% in real terms); when the Index is in its 4th quartile, the average change in gold prices over the subsequent 6 months is -0.2% (-1.4% in real terms). These results are consistent with the traditional view of gold as a "safe haven" asset during times of slow economic growth, and vice versa.

Figure 1. 6-Month Return on Gold by Momentum Monitor Quartile



Source: Macrobond Financial, Keybridge analysis

Differences in gold prices are statistically significant with a high degree of confidence.

Upon further inspection, an analysis of variance ("ANOVA") shows that the differences in returns are statistically significant at a 99% confidence level. In other words, the differences in the average 6-month return on gold for each Momentum Monitor Index quartile are meaningfully different and not overly-influenced by a few outliers.

Figure 2. U.S. Economic Momentum Monitor & Gold Price ANOVA

Source	SS	df	MS	F	Prob > F
Between groups	0.2208	3	0.0736	7.09	0.0001
Within groups	2.2416	216	0.0104		
Total	2.4623	219	0.0112		
Bartlett's test for equal variances: chi2(3) = 2.5537 Prob>chi2 = 0.466					

The Keybridge U.S. Economic Momentum Monitor can be an effective tool for gold investment strategies.

This relatively straightforward analysis shows that the U.S. Economic Momentum Monitor Index can be a useful tool for setting gold investment strategies. This is just one of many applications of Keybridge's Momentum Monitors that can be implemented into a broader investment strategy. For more information on Keybridge's Momentum Monitors, investment analysis tools, and asset allocation advisory services, contact us at: info@keybridgedc.com.