

Why Gold Bugs Should Be Praying for the Demise of Commodities

[Martin Pring](#) | December 30, 2020 at 06:30 PM

Last month, the gold price slipped down very closely towards its 12-month MA. This is not a perfect indicator, but most downside penetrations are followed by bearish action, so you could say that gold is at the crossroads. Chart 1 tells us that prices have bounced a bit since then, but the flattening action of the long-term KST in the lower window warns that there is not much margin for error.

I have always believed that the fortunes of the gold price have depended on swings in commodity prices. After all, if gold is a store of value, gold traders, like all savvy market participants, should anticipate future commodity inflation by bidding up the price of the yellow metal ahead of time, and vice versa. Another rationalization lies in the fact that gold tends to prosper when the trend of real interest rates is falling. That environment is usually one of weaker economic activity that is hostile to commodities.



Chart 1

Chart 2 sets the scene, as the CRB Composite in the upper window is compared to the ratio between it and gold. The actual relationship is featured in the middle window, and its KST in the bottom one.

The red arrows tell us when the KST peaks out - in other words, when the favorable trend for gold over commodities shifts in the direction of commodities. While this indicator only reflects relative performance, it's obvious from the solid green arrows plotted against the CRB that this is invariably positive for the CRB itself.

Since 1975, there has only been one exception, which took place in 1980. It culminated an unusual period when both gold and commodities had been exceptionally strong.

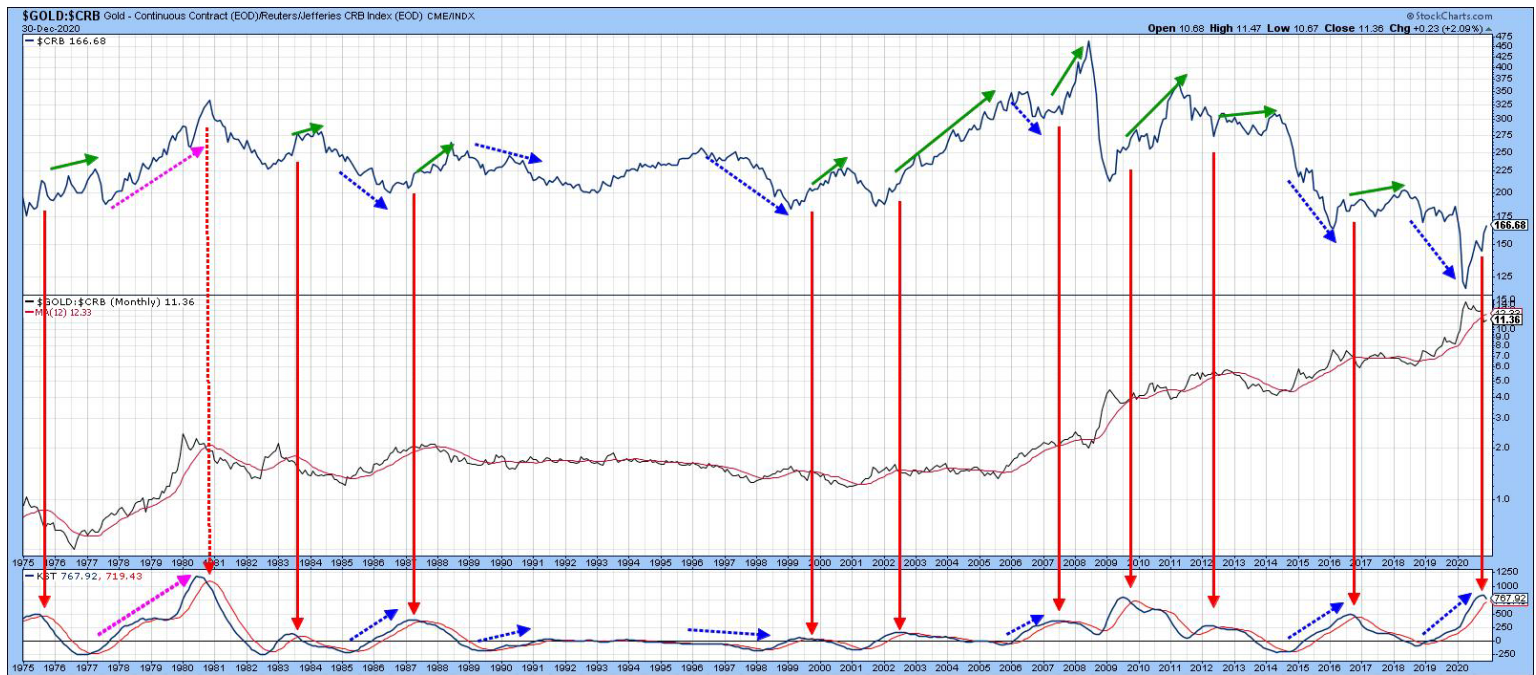


Chart 2

The blue arrows tell us that, when the KST is in a rising phase, this is normally bearish for commodities in an absolute sense. The two fuchsia-colored arrows indicate that, in a really strong commodity market, commodities can still rise even when they are underperforming gold.

The ratio itself recently crossed below its 12-month MA, but, more importantly, its long-term KST has peaked out from a high level. Based on eight of the nine precious signals, that should be very positive for the CRB Composite, *but what of gold?*

Chart 3 reverses the relationship, where the Gold Trust ETF (GLD) is compared to the ratio and the Bloomberg Commodity ETN, the DJP. There are several things to note.

First, the ratio and gold price generally move in the same direction. *Second*, this relationship often, but not consistently, leads the GLD, as flagged by the red dashed arrows. *Third*, it's occasionally possible to construct trendlines for both series - their joint penetration then serving as timely buy and sell signals for the gold price.

The most recent signal of this nature was triggered in October, as both series violated red trendlines and subsequently fell.



Chart 3

Chart 4 shows a recent action in greater detail.

The first thing to notice is the negative divergence between the GLD and ratio that took place earlier this year. Also, **the ratio has already dropped below its 200-day MA, which is certainly not supportive of higher gold prices.**

Finally, December has seen the gold price recover towards its bear trendline. *However, the ratio has been weaker.* That could all be cleared up with a joint upside trendline violation. At the moment, though, the trend of gold versus commodities is bearish, which is negative for gold itself. By the way, if you want to update this chart to see whether those upside breakouts do in fact materialize, simply click on it when more data is available.



Chart 4

Bottom line: if gold is to stand a real chance of moving higher, it needs to outperform commodity prices, and that would initially involve breaking through those two down trendlines in Chart 4.

To Hedge or Not to Hedge?

Another relationship that should concern gold traders is the ratio between the Gold Bugs and the Gold Share Index (\$HUI/\$XAU). The Gold Bugs Index is focused on gold miners who do not hedge their production, the implication being that they benefit far more than unhedged miners during bull markets but suffer more when prices fall. Because of this, the \$HUI has a tendency to outperform the \$XAU during bull markets and vice versa, as it is reflective of swings in confidence amongst gold share traders.

Chart 5 compares the GLD to that ratio. The numbers 1-3 represent examples where it has been possible to construct two trendlines and observe their joint violation. Important reversals in trend followed.

A fourth setup appears to be forming currently, as the ratio has already severely violated its 2018-2020 up trendline. The GLD price has not yet confirmed, so it's premature to head to the exits. However, the red dashed arrows are pointing up a massive 4-year negative divergence, as the price has broken out to new highs and the ratio to a record low.

Once again, it's important to note that the trend for gold is still favorable, but red flags are appearing.

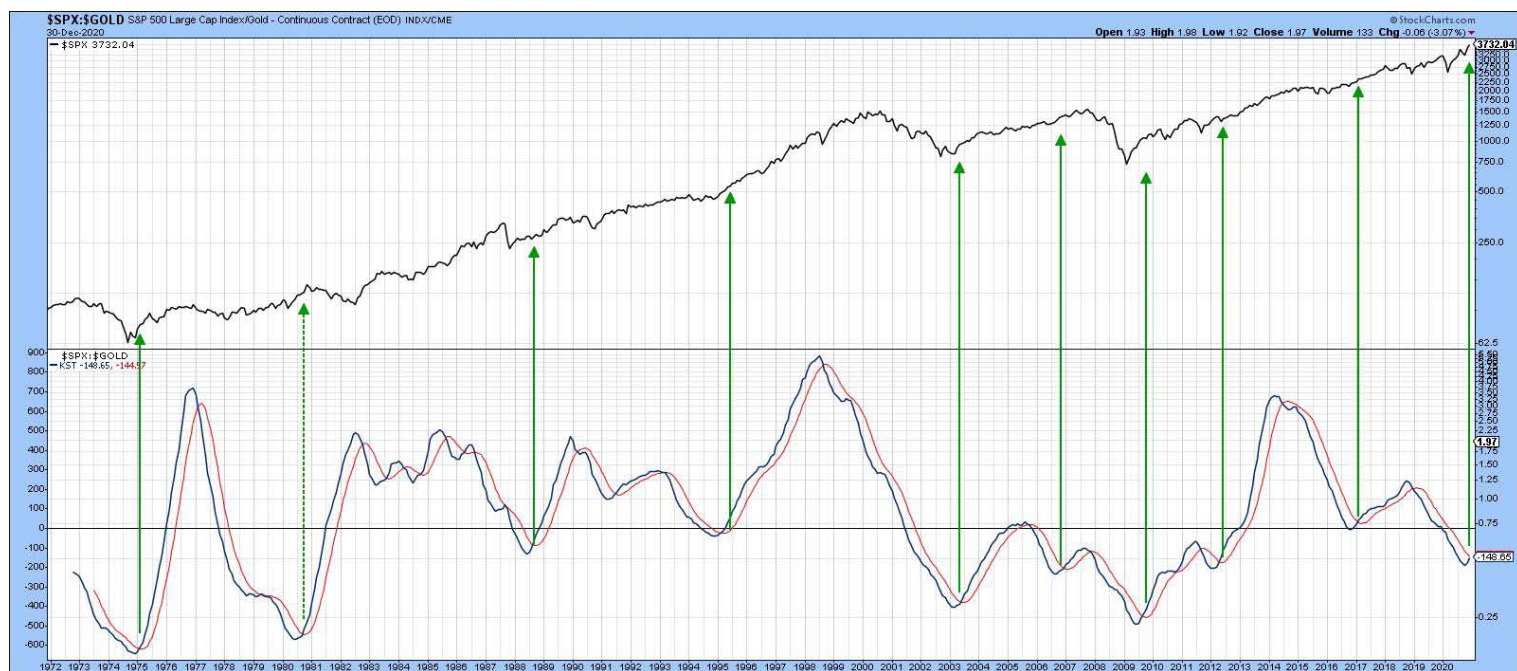


Chart 5

Stock/Gold Ratio is Starting to Favor Stocks

That said, there is a silver lining should the price of the yellow metal start to slip with stocks outperforming gold, as that would be a bullish sign for stocks in their own right.

For instance, the lower window features the long-term KST for the stock/gold relationship. The arrows show sub-zero buy signals since the 1970s. All, except the 1980 signal, were followed by substantially higher equity prices. December has seen the KST hook up for what will likely be another positive signal.



On that optimistic note, Happy New Year, everyone.

Good luck and good charting,

Martin J. Pring



About the author: [Martin Pring](#) is one of the most prominent names in the industry. A master technical analyst and educator extraordinaire, he is the award-winning author of numerous books on Technical Analysis, including [Introduction to Technical Analysis](#) and [Technical Analysis Explained](#). The latter is now used by several international technical societies for training and for several decades was one of the three core books for Level 1 CMT certification with the Market Technicians Association. Translated into over 7 languages, the book is, as quoted by Forbes, *"widely regarded as the standard work for this generation of chartists"*.