How Gold Got Its Groove Back

By Frank Holmes

CEO and Chief Investment Officer

U.S. Global Investors

Who says gold lost its appeal as a safe haven asset?

After five straight positive trading sessions, the yellow metal climbed above $1,100 on a weaker U.S. dollar, its highest level in nine weeks. The rally proves that gold still retains its status as a safe haven among investors, who were motivated this week by a rocky Chinese stock market, North Korea’s announcement that it detonated a hydrogen bomb on Wednesday and rising tensions between Saudi Arabia and Iran.

Here in the U.S., gold finished 2015 down 10.42 percent, its third straight negative year. Until the new year, sentiment appeared poor, and many gold bulls were finding it hard to stay optimistic.

But after the price jump this week, large exchange-traded gold funds saw massive inflows, confirming a shift in investors’ attitude toward the precious metal.

It’s worth remembering that about 90 percent of physical demand comes from outside the U.S., mostly in emerging markets such as China and India. In many non-dollar economies, buyers are actually seeing either a steady or even rising gold price. The metal is up in Russia, Peru, South Africa, Canada, Mexico, Brazil and many more.
Note the differences in returns between gold priced in U.S. dollars and gold priced in the Brazilian real, Turkish lira, Canadian dollar, Russian ruble and Indonesian rupiah.

**In 2015, Gold Performed Better in Non-Dollar Currencies**

Returns Priced in Local Currencies

![Chart showing gold performance in different currencies](chart)

Gold demand in China was very robust last year. A record **2,596.4 tonnes of the yellow metal**, or a whopping 80 percent of total global output for 2015, were withdrawn from the Shanghai Gold Exchange. As for the Chinese central bank, it reported adding 19 more tonnes in December, bringing the total to over 1,762 tonnes. Precious metals commentator Lawrie Williams points out, though, that China’s total reserve figure is widely believed to be “hugely understated,” meaning the central bank might very well have much more than we’re being told.

**Forget Interest Rates—Real Rates Are the Key Drivers of Gold**

Despite all the talk of rising interest rates in connection to gold, they’re not a dominant driver of prices. Sure, rising nominal rates have tended to make the metal less attractive, since it doesn’t pay an income, but the larger driver by far are **real** interest rates. When real rates drop into negative territory, gold has historically done well.

As a reminder, real rates, important for the Fear Trade, are what you get when you subtract the consumer price index (CPI), or inflation, from the 10-year Treasury yield. As of January 6, the 10-year yield was 2.18 percent, while the 12-month CPI for November—December data will be released later this month—came in at a barely-there 0.50 percent. Real rates, therefore, are running at a positive 1.68 percent, which is a headwind for gold.

That’s why we need inflation to pick up, because then gold would be more likely to rally.

Regardless, the World Gold Council (WGC) writes in its 2016 outlook that gold’s role as a diversifier remains “particularly relevant”:

> Research shows that, over the long run, holding 2 percent to 10 percent of an investor’s portfolio in gold can improve portfolio performance.

The reason for this is that gold has tended to have a low correlation to many other asset classes, making it a valuable diversifier. During economic contractions, for example, gold’s correlation to stocks actually decreased, according to data between 1987 and 2015.
For the last three years, gold has disappointed many because other investments, specifically equities, have seen such huge gains. But with global markets hitting turbulence, the yellow metal is looking more attractive as insurance against the currency wars.

I always recommend 10 percent in gold: 5 percent in gold stocks or an actively-managed gold fund, 5 percent in bullion and/or jewelry. It’s also important to rebalance every year.

This should be the case in both good times and bad, whether gold is rising or falling. As highly influential investment expert Ray Dalio said last year: “If you don’t own gold, you know neither history nor economics.”

USGI Among the First to Discuss the Significance of PMI as a Forward-Looking Indicator

Aside from real interest rates, gold prices are being challenged by weak manufacturing data around the world. China’s purchasing managers’ index (PMI) fell to 48.2 last month, down 0.4 points from the November reading. The Asian giant’s manufacturing sector spent a majority of 2015 in contraction mode, managing to rise above the key 50.0 level only once last year, in February.

China Manufacturing Still in Contraction Mode

Although fears of a Chinese slowdown are real, they’re largely overdone. Consulting firm McKinsey &
Company's Gordon Orr calls these fears a distraction, writing that “the country's economy is still massive—as are its potential opportunities.”

Something to keep in mind is that China recently approved a new five-year plan, its 13th since 1953. Although we won’t know exactly what’s in it until March, we do know that these plans have been good for economic growth in the past. It’s likely that interest rates will be trimmed even more to stimulate business, with more funding diverted to infrastructure and “green” initiatives.

Manufacturing around the world showed signs of deterioration in December as well. The JP Morgan Global Manufacturing PMI declined to 50.9 from 51.2 in November. The sector is still in expansion mode, but just barely.

Global Manufacturing Cools in December

The reading also fell below its three-month moving average in December, which, as I’ve shown many times before, can have a huge effect on materials and energy three to six months out.

We were one of the earliest investment firms to monitor this important economic indicator closely and bring it into public, everyday discourse. (From what I can find, the first time we wrote about it was in January 2009, as it applied—wouldn’t you know?—to China.) Today, I hear and read about the PMI on the radio and in newspapers as often as I do more common economic indicators such as GDP and unemployment rates.

That’s a testament to the sort of cutting-edge analysis we do and pride ourselves on here at U.S. Global Investors.

Looking Ahead in the New Year

Until we see global synchronized growth with rising PMIs, we remain cautious going forward. A constant source of hope is the Trans-Pacific Partnership (TPP), which, when ratified sometime this year, will eliminate 18,000 tariffs for 25 percent of global trade.

We also anticipate more stimulus programs this year around the world. Lately we’ve experienced strong fiscal drag as more and more regulations and taxes impede progress that not even cheap money has been able to offset. A 2014 report by the National Association of Manufacturers (NAM) revealed that federal regulations in the U.S. alone cost businesses more than $2 trillion a year. To ignite growth, G20 nations should commit themselves to cutting red tape.
A good model for such a task is Canada’s “One-for-One Rule,” introduced in April 2012 during former Prime Minister Stephen Harper’s administration. The rule mandates that when a new or amended regulation is introduced, another must be removed.

However it’s accomplished, regulatory burdens placed on businesses must be reduced.

For more in-depth analysis, consider subscribing to my award-winning CEO blog, Frank Talk.

**Index Summary**

- The major market indices finished down this week. The Dow Jones Industrial Average lost 6.19 percent. The S&P 500 Stock Index fell 5.96 percent, while the Nasdaq Composite fell 7.26 percent. The Russell 2000 small capitalization index lost 7.90 percent this week.

- The Hang Seng Composite lost 7.11 percent this week; while Taiwan was down 5.33 percent and the KOSPI fell 2.23 percent.

- The 10-year Treasury bond yield fell 15 basis points to 2.12 percent.

---

**Domestic Equity Market**
Strengths

- The utilities sector was the best performer amid a down week, falling 0.40 percent versus an overall decline of 5.96 percent for the S&P 500 Index.
- Time Warner was the best-performing stock for the week, increasing 10.05 percent. Several key pieces of news, including impressive subscriber growth and new advertising techniques, helped drive Time Warner's stock gains.

Weaknesses

- The materials sector was the worst performer for the week, falling 7.82 percent versus an overall decline of 5.96 percent for the S&P 500 Index.
- Williams Companies was the worst-performing stock for the week, falling 20.97 percent. The company’s debt was cut to junk by Moody’s, fueling a downward spiral for the stock.
- In an interview in The Economist, Deputy Crown Prince Mohammed bin Salman Al Saud of Saudi Arabia said that the kingdom might consider selling shares in the state-owned oil giant, Saudi Aramco. Suffering from a low oil price, the Saudis appear to be looking to fill a growing budget hole.

Opportunities

- With the deepest and most liquid equity market and the strongest economy, the U.S. could weather the recent bout of volatility relatively better than other developed markets.
- The information technology sector has been hit the hardest over the past month. A rebound in the market could see this sector outperform.
- A positive retail sales report next Friday could be a catalyst for consumer discretionary stocks.

Threats

- With profit margins historically elevated, this could cast a shadow over relative earnings prospects.
- The valuation of the U.S. market is less attractive than many other developed markets. The cyclically-adjusted price-earnings ratio (CAPE) for U.S. non-financial stocks is above its historical average, unlike many other markets.
- The selloff in high-yield corporate bonds widened the divergence from U.S. equity prices and earnings multiples. High-yield bond movements often precede periods of poor equity returns.
The Economy and Bond Market

Strengths

- U.S. December non-farm payroll rose to 292,000 jobs. Solid payroll growth was accompanied by upward revisions to prior months, which added an additional 50,000 jobs to the tally.

- The unemployment rate for December held steady at 5 percent.

- The Institute for Supply Management (ISM) Non-Manufacturing Index dipped to 55.3 in December from 55.9 in November, but held well above the neutral level of 50.

Weaknesses

- The ISM Manufacturing Index slipped to 48.2 in December, the lowest level in six years. It was weighed down by a strong dollar and weak global demand.

- Construction spending fell 0.4 percent month-over-month (MoM) in November, down from a 0.3 percent MoM gain in the prior month. (It was initially revised lower from a 1.0 percent MoM gain). This was below the expected 0.6 percent MoM gain.

- China's manufacturing sector remains in contraction. The Caixan Purchasing Managers' Index, a privately compiled survey of small and medium-sized firms, contracted for the tenth straight month in...
December, falling to 48.2. The official PMI, compiled by the government and focusing on larger state-owned businesses, contracted for a fifth consecutive month, with a 49.7 reading.

Opportunities

- Various Federal Open Market Committee (FOMC) members will deliver speeches next week, and investors should look out for clues as to how renewed market volatility will factor into their plans to gradually lift interest rates this year.
- The one-month reading of the University of Michigan Sentiment Index remains above the three-month trend. If this holds, next Friday’s release should be a boost to consumer confidence.
- The one-month reading of U.S. retail sales remains above the three-month trend. Next Friday’s release of December retail sales will be an important gauge of retail consumption during the holiday season.

Threats

- The lack of participation among younger-age cohorts suggests that a meaningful pick-up in broad-based wage growth might still be several months away.
- 2015 ended with a major sea change for U.S. fixed-income markets, with the Federal Reserve finally pulling the trigger on liftoff after seven years of zero percent interest rates. However, the fundamental issues that plagued bond markets throughout last year have not gone away. Additionally, The U.S. yield curve saw a bear flattening for the calendar year 2015. This is the first bear-flattening that has occurred over a calendar year since 2005, when the Fed was in the midst of a rate hike cycle.
- The Chinese market turbulence and poor policy communication and implementation have negatively affected global risk assets. Little clarity over the authorities’ willingness to stabilize the currency will continue to pose a major risk to Chinese and global risk assets. On the macro front, the Chinese external trade released on Wednesday will help monitor how the Chinese slowdown is impacting the global economy.

Gold Market

Since the start of the year, spot gold closed at $1,104.16, up $42.74 per ounce, or 4.03 percent. Gold stocks, as measured by the NYSE Arca Gold Miners Index, jumped 5.49 percent. Junior miners underperformed seniors for the week as the S&P/TSX Venture Index traded down 2.09 percent. The U.S. Trade-Weighted Dollar Index slipped 0.22 percent since last Thursday’s holiday extended week.

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
<th>Survey</th>
<th>Actual</th>
<th>Prior</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan-08</td>
<td>U.S. Change in Nonfarm Payrolls</td>
<td>200k</td>
<td>292k</td>
<td>211k</td>
</tr>
<tr>
<td>Jan-14</td>
<td>U.S. Initial Jobless Claims</td>
<td>275k</td>
<td>--</td>
<td>277k</td>
</tr>
<tr>
<td>Jan-15</td>
<td>U.S. PPI Final Demand YoY</td>
<td>-1.0%</td>
<td>--</td>
<td>-1.1%</td>
</tr>
</tbody>
</table>

Strengths

- Gold opened the year with very a strong gain, climbing 4.02 percent, as rising sectarian tension between Saudi Arabia and Iran ratcheted up; North Korea announced the testing of its first hydrogen bomb; and twice on separate trading days, Chinese markets fell 7 percent, the maximum amount Chinese authorities allowed them to decline. This sent shock waves through financial markets leading investors to seek out safe haven assets once again. In 2015 gold fell 10 percent, putting in three consecutive years of negative returns, its longest losing streak since 2000. Billionaire George Soros reiterated the precious metals’ status on Thursday by stating, “Global markets are facing a crisis and investors need to be very cautious.”
- This week ZeroHedge pointed out a move in gold that many sell-side experts previously warned would never be able to happen again. On Thursday the publication shared a chart showing the precious metal finally broke out above the $1,100 resistance level, an encouraging sign going against a deluge of
predictions calling for nothing but lower gold prices.

- U.S. imports of gold jewelry rose to a seven-year high in October of last year, while platinum jewelry surged by more than 60 percent after precious metals prices dropped to multi-year lows, according to calculations from Thomson Reuters.

**Weaknesses**

- The worst performing precious metal for the week was palladium, falling 12.11 percent, likely on weak manufacturing data out of China and its prospects for car sales to grow at a slower rate.

- In Paradigm Capital’s 2016 Gold Sector Outlook, the group reviews 2015 share price performance by tiers — developers, seniors, and royalty companies. They noted the “biggest surprise” came from the royalty companies. The report states that royalties didn’t have the best 2015, going on to explain that the recent poor performance has only happened during three out of the last 12 years.

- Top gold forecaster Bernard Dahdah, of French investment and bullion bank Natixis, predicts that the yellow metal will drop through $1,000 per ounce in the first three months of 2016, according to an article on BullionVault. He states the move will primarily be driven by the “expected path of interest rate hikes” from the Federal Reserve, and even believes the price could gradually decline to end 2016 at $950 per ounce.

**Opportunities**

- According to HSBC’s analysis of the Federal Open Market Committee’s (FOMC’s) minutes, the median Fed projections show total PCE inflation and core PCE inflation expected to rise to 1.6 percent by the end of the year. The FOMC inflation target is at 2 percent, as seen in the chart below. The Globe and Mail outlines four specific investment regimes defined by growth and inflation: 1) In high growth and high inflation, real estate and resources do best, 2) In high growth and low inflation, growth stocks outperform, 3) In low growth and low inflation bonds shine, and 4) In low growth and high inflation most stocks underperform, but gold does best! With so many central banks targeting higher inflation, to deflate their debts, be careful what you ask for.

**Inflation Has Been Below the FOMC’s 2-Percent Target**

Looking back on their 2015 strategy, UBS says last year’s rise in volatility was just the beginning of a dramatic rise in cross-asset volatility. In the group’s macro-view this week, UBS stated that the large cap-driven U.S. indices, as well as Japan and European small and mid-caps, are “the last men standing” at 2015’s close. In 2016 UBS expects these markets to top out also, falling into a full-size bear market which, worst-case-scenario, would last into early 2017. UBS noted with equities predicted to roll over, investors should consider owning gold for better diversification.

- Over the past two years, nearly 50 percent of global gold demand has come from Chinese and Indian
markets – with particular buying strength on dips in the renminbi or the rupee, according to RBC Capital Markets. The group continues to look to increasing global market volatility to allow gold to regain its safe haven status. In addition, lack of exploration and capital investment spending should lead to a reduced supply.

**Threats**

- This year began with a rocky start, points out BMO Private Bank, as Chinese policymakers struggled to stabilize the Shanghai Composite after disappointing manufacturing data showed economic contraction in China. According to the BMO’s current market update, as we move further into 2016 “investors increasingly believe that central bank ‘puts’,” are not as effective as they once were.

- ZeroHedge points out that 2016 marks a presidential election year (which usually have a bullish track record), but also marks the eighth year of president Obama’s term. A closer look at this cycle shows a divergence between a normal election year and the eighth year of a term – since 1920 (more or less) all eighth years of a term were amongst the worst for market performance.

- Julien Garran of MacroStrategy Partnership believes that deteriorating private debt conditions, tightening liquidity, declining returns and slowing growth have now entered a “self-reinforcing cycle in the U.S.” As credit and returns deteriorate, Garran says corporates will no longer be able to justify gearing up to do buybacks. In 2013, 60 percent of Garran’s sample could justify buybacks, and now only 35 percent make the grade.

**Frank Talk Insight for Investors**

January 6, 2016
**Franco-Nevada: Royalty of the Gold Industry**

January 4, 2016
**Hope for the New Year: 3 Asset Classes for 2016**

December 28, 2015
**Christmas Edition: 2015 in Review**

A blog by Frank Holmes, CEO and Chief Investment Officer

**Energy and Natural Resources Market**

**Strengths**

- Natural gas prices reached a seven-week high as U.S. inventories declined for a sixth consecutive week, and weather patterns signal a return of winter temperatures to much of the U.S. Midwest.

- Gold miners were the best performers this week as the yellow metal benefited from its safe-haven status amid rising tensions between Iran and Saudi Arabia. The release of lower-than-anticipated eurozone inflation data for December provided additional support to gold prices.

- The best performing stock for the week in the broader natural resource space was Barrick Gold. The Canadian miner rose with gold prices and outperformed its peers for the week. Barrick made significant strides to shore up its balance sheet last year by selling assets and retiring significant portions of its debt.

**Weaknesses**

- U.S. crude production edged higher in December and is now at a four-month high. This increase offset OPEC production falling 170,000 barrels per day in December, reaching a seven-month low. Still, OPEC output remained significantly above earlier quota levels, exacerbating the global oversupply condition.

- Industrial metals miners were the worst performers this week on concerns that metals are oversupplied as growth wanes in China, the biggest buyer of commodities. Copper declined the most in at least seven weeks after a weak China purchasing managers’ index (PMI) reading.
• The worst performing stock for the week in the S&P Natural Resources Index was Anglo American. The London-based miner led a slump in mining equities as concerns over commodity prices continuing to slump took front page after China fixed its currency lower. Anglo American is one of the most indebted miners with nearly $20 billion in debt.

Opportunities

• The weighting on the “FANG” stocks (Facebook, Amazon, Netflix and Google) in the S&P 500 Index surpassed that of the S&P 500 Energy sector. A report by Macro Risk Advisors observes that in June 2014, energy was 10.5 percent of the S&P 500 by market cap; since then, it has shrunk to around 6.5 percent. The extreme opposite behavior of these two components over the last six months may suggest that a short-term correction could take place.

The Four FANGs’ Market Capitalization Now Exceed S&P 500 Energy Sector
Market Capitalization as a Percentage of S&P 500

- U.S. petrochemical producers should benefit from a looming shortage of ethylene and polyethylene in Asia, similar to that of last year, as already high utilization rates are curtailed by the “heavy” turnaround season. In a report, Bernstein analysts expect Dow Chemical and Lyondell to benefit the most.

- Mohamed El-Erian, former CEO and co-CIO of PIMCO, suggests the commodity space may be setting up for a multi-year recovery. In his opinion, the price collapse is likely to force asset disposals. In this readjustment process, a supply-side correction should trigger a rebalancing from record short and underweight positions in the commodity space to a more balanced position.

Threats

• The pressure on commodities in the first week of the year has been attributed to the People’s Bank of China (PBOC) lowering the fixing for the Chinese yuan. Recent history shows the correlation between lower CNY fixings and commodities is very strong, as depicted in the chart below. Fundamentally this is sensible, since a lower CNY makes commodity imports more expensive for China, the world’s biggest user of energy, metals and grains.
Global manufacturing PMI slipped back to 50.9 in December, crossing below its three-month moving average of 51.1 as output, exports and new orders all eased lower. China, India, Brazil and Russia all reported PMIs below 50 as manufacturing output in emerging markets remains in contraction. With PMIs having shown to be among the best predictive tools for commodity prices, the outlook for the first few months of the year has turned more challenging.

Agricultural chemical producers are under pressure as potash prices continue to fall. Global potash volumes shrunk last year as farmers delayed purchases following double-digit drops in corn and soybean prices which pressured farmer economics. U.S. potash prices are at the lowest since September 2007, after falling 29 percent in 2015.

**China Region**

**Strengths**

- In Guangzhou, the capital of Guangdong province, the residential real estate market surged in sales volume. According to Colliers International, a global property service provider, sales of commodity housing rose 34 percent year-over-year to more than 7 million square meters in 2015.

- The Chinese yuan stabilized on Friday after Thursday's surprise devaluation spooked investors and helped contribute to a large selloff in Chinese equities.

**Weaknesses**

- Caixin China Manufacturing PMI came in at 48.2, missing expectations of 48.9 and signaling continued contraction in the Chinese manufacturing sector. Services PMI fell to 50.2, down from 51.2 last month, just barely expanding. Overall, though, the lower numbers in Manufacturing and Services led the Caixin China Composite PMI to fall to 49.4.
The Shanghai Composite Index lost 6.86 percent on Monday. The same index lost more than 7 percent on Thursday. In both cases, Shanghai dragged world equity indices and sentiment lower, and the Shanghai Composite is already down about 10 percent year-to-date.

The World Bank issued a press release lowering its expectations for 2016 global growth to 2.9 percent. The World Bank expressed concerns over an “anemic recovery in emerging markets,” specifically citing slower projected growth in China. While there were no earth-shattering data in the press release, the timing—coming in tandem with Thursday’s selloff—added to the negative sentiment.

Opportunities

- Expectations for some manner of forthcoming Chinese policy aimed at stabilizing the stock market have increased since the Chinese government suspended Shanghai’s new and heavily-criticized stock market circuit breaker system, which was employed in both Monday and Thursday’s heavy selloffs. If widespread international chatter of the Chinese government purchasing stocks in the open market on Friday is indeed true, then the Chinese government has perhaps “bought” itself a window of time this weekend to deliver a thoughtful, pragmatic response and attempt to reassure investor sentiment.

- Contrarian investors may see opportunity amidst the sharp selloffs that marked the start of 2016.

- The beginning of the Chinese New Year is now only one month away. As the Year of the Monkey approaches, it could bring positive domestic Chinese sentiment and instill some sense of urgency to any potential Chinese government actions undertaken on behalf of market stability in the meantime.

Threats

- China’s ban on large institutional sellers that was set to expire today was left partly unresolved. The Chinese government’s makeshift solution to reassure investors over their fears of looming large share sales came in the form of a three-month extension against sales by holders of positions larger than 5 percent, with the caveat that a maximum of 1 percent of shares can be sold if the seller files 15 days ahead of time. Needless to say, some uncertainty remains.

- The week brought to the forefront again philosophical and economic questions over Chinese government policies and the pace of reform and movement toward a freer market. In the short term, volatility can always be exacerbated.

- Claims that North Korea may have tested a powerful hydrogen bomb cast an eerie geopolitical shadow over the week’s otherwise overwhelmingly economic focus, adding to negative sentiment in Asia and posing a particular diplomatic headache for China, which has repeatedly stressed that it can rein in North Korea and bring the defiant, isolated East Asian country back to the nuclear negotiating table.
Emerging Europe

Strengths

- Ukraine was the best-performing market this week, gaining 2.1 percent. It was a short trading week as Ukraine’s PFTS Index was closed on Thursday and Friday in observation of Orthodox Christmas. During the holidays, the leader of Russia-supported separatists in the Luhansk region in Eastern Ukraine ordered the release of captured troops.

- The Ukrainian hryvnia was the best-performing currency this week, gaining 2.8 percent against the U.S. dollar. Budget revenue rose 50 percent year-over-year to 481 billion hryvnia in the first 11 months of 2015. December inflation declined to 43.3 percent from 46.6 in the prior year.

- Health care was the best-performing sector among Eastern European markets this week.

Weaknesses

- Greece was the worst-performing market this week, losing 7.19 percent, led by big weekly declines in Alpha Bank and National Bank of Greece. The Mediterranean country has begun working on pension reform and plans to vote on it by early February. According to the proposals that were sent to lenders on Monday, all six main pension funds will be merged into one and future pensions could be cut up to 30 percent.

- The Russian ruble was the worst-performing currency this week, losing 3.7 percent against the dollar. Russia’s currency and its stock market are highly correlated with the price of oil. Brent crude oil declined 10.6 percent this week and is trading near 12-year lows.

- The utilities sector was the worst performer among Eastern European markets this week.

Opportunities

- The eurozone’s purchasing managers’ index (PMI,) a key measure of manufacturing activity, registered at 53.2 in December, above the earlier flash estimate of 53.1 and the November reading of 52.8. A reading above 50 indicates expansion while a reading below 50 represents contraction. Manufacturing data for Poland, Hungary, the Czech Republic, Turkey and even Greece was reported above 50. Russia’s PMI, however, dropped below 50, from 50.1 to 48.7.

- The World Bank is raising GDP expectations for Romania to 3.6 percent in 2015 and 4 percent for the years 2016-2018, above the earlier consensus of 3.7 percent. The bank forecasted faster economic growth on the back of successful reforms, ultra-competitive labor costs and improving corporate governance.

- The MSCI Emerging Markets Index slumped 6.9 percent this week, the most since September 2011. Following this week’s drop, developing nation stocks trade on average at 10.5 times projected 12-month earnings, near the cheapest since September and a 30 percent discount to advanced country shares in the MSCI World Index, according to data compiled by Bloomberg.

Threats

- Hungarian Prime Minister Viktor Orbán visited Poland this week for a meeting with former Poland Prime Minister Jaroslaw Kaczynski, a day before his visit with United Kingdom Prime Minister David Cameron. Kaczynski, chairman of the newly-elected Eurosceptic party, has been expressing his admiration for the Hungarian leader and his policies that seek to affirm national sovereignty over the
Brussels bureaucracy. When Orbán came to power in 2010, he rewrote Hungary’s fundamental laws and taxed foreign-dominated sectors. In recent weeks, Poland has come under a lot of criticism from euro-members after Mr. Kaczynski’s party rewrote the rules governing the country’s top court, making it harder for the constitutional court to rule against legislations.

- HSBC expects Russia’s economic outlook to remain poor this year. Analysts predict its GDP to contract 1 percent this year followed by a 4 percent decline in 2015, assuming oil prices to be almost 10 percent lower on average. Russia’s economic growth is highly dependent on oil prices, and with the recent Brent selloff, further economic weakness is anticipated.

Russia's December inflation came in well above expectations at 0.21 percent month-over-month and 8.8 percent year-over-year versus market consensus expectations of 8.5 percent. The main reason behind the higher inflation was again food prices. Inflation could reach 9.5 percent in January.

Leaders and Laggards

<table>
<thead>
<tr>
<th>Index</th>
<th>Close</th>
<th>Weekly Change($)</th>
<th>Weekly Change(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>DJIA</td>
<td>16,346.45</td>
<td>-1,078.58</td>
<td>-6.19%</td>
</tr>
<tr>
<td>Index</td>
<td>Close</td>
<td>Monthly Change($)</td>
<td>Monthly Change(%)</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>--------</td>
<td>-------------------</td>
<td>-------------------</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>1,922.03</td>
<td>-121.91</td>
<td>-5.96%</td>
</tr>
<tr>
<td>S&amp;P Energy</td>
<td>417.77</td>
<td>-30.67</td>
<td>-6.84%</td>
</tr>
<tr>
<td>S&amp;P Basic Materials</td>
<td>252.23</td>
<td>-21.41</td>
<td>-7.82%</td>
</tr>
<tr>
<td>Nasdaq</td>
<td>4,643.63</td>
<td>-363.78</td>
<td>-7.26%</td>
</tr>
<tr>
<td>Russell 2000</td>
<td>1,046.20</td>
<td>-89.69</td>
<td>-7.90%</td>
</tr>
<tr>
<td>Hang Seng Composite Index</td>
<td>2,806.71</td>
<td>-214.76</td>
<td>-7.11%</td>
</tr>
<tr>
<td>Korean KOSPI Index</td>
<td>1,917.62</td>
<td>-43.69</td>
<td>-2.23%</td>
</tr>
<tr>
<td>S&amp;P/TSX Canadian Gold Index</td>
<td>141.77</td>
<td>+12.24</td>
<td>+9.45%</td>
</tr>
<tr>
<td>XAU</td>
<td>47.10</td>
<td>+1.80</td>
<td>+3.97%</td>
</tr>
<tr>
<td>Gold Futures</td>
<td>1,103.80</td>
<td>+43.60</td>
<td>+4.11%</td>
</tr>
<tr>
<td>Oil Futures</td>
<td>32.96</td>
<td>-4.08</td>
<td>-11.02%</td>
</tr>
<tr>
<td>Natural Gas Futures</td>
<td>2.48</td>
<td>+0.14</td>
<td>+6.03%</td>
</tr>
<tr>
<td>10-Yr Treasury Bond</td>
<td>2.12</td>
<td>-0.16</td>
<td>-6.83%</td>
</tr>
</tbody>
</table>

**Monthly Performance**

<table>
<thead>
<tr>
<th>Index</th>
<th>Close</th>
<th>Quarterly Change($)</th>
<th>Quarterly Change(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>DJIA</td>
<td>16,346.45</td>
<td>-1,145.85</td>
<td>-6.55%</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>1,922.03</td>
<td>-125.59</td>
<td>-6.13%</td>
</tr>
<tr>
<td>S&amp;P Energy</td>
<td>417.77</td>
<td>-37.97</td>
<td>-8.33%</td>
</tr>
<tr>
<td>S&amp;P Basic Materials</td>
<td>252.23</td>
<td>-32.74</td>
<td>-11.49%</td>
</tr>
<tr>
<td>Nasdaq</td>
<td>4,643.63</td>
<td>-379.23</td>
<td>-7.55%</td>
</tr>
<tr>
<td>Russell 2000</td>
<td>1,046.20</td>
<td>-99.67</td>
<td>-8.70%</td>
</tr>
<tr>
<td>Hang Seng Composite Index</td>
<td>2,806.71</td>
<td>-200.07</td>
<td>-6.65%</td>
</tr>
<tr>
<td>Korean KOSPI Index</td>
<td>1,917.62</td>
<td>-30.62</td>
<td>-1.57%</td>
</tr>
<tr>
<td>S&amp;P/TSX Canadian Gold Index</td>
<td>141.77</td>
<td>+9.80</td>
<td>+7.43%</td>
</tr>
<tr>
<td>XAU</td>
<td>47.10</td>
<td>-0.11</td>
<td>-0.23%</td>
</tr>
<tr>
<td>Gold Futures</td>
<td>1,103.80</td>
<td>+27.30</td>
<td>+2.54%</td>
</tr>
<tr>
<td>Oil Futures</td>
<td>32.96</td>
<td>-4.20</td>
<td>-11.30%</td>
</tr>
<tr>
<td>Natural Gas Futures</td>
<td>2.48</td>
<td>+0.42</td>
<td>+20.17%</td>
</tr>
<tr>
<td>10-Yr Treasury Bond</td>
<td>2.12</td>
<td>-0.10</td>
<td>-4.60%</td>
</tr>
</tbody>
</table>

**Quarterly Performance**

<table>
<thead>
<tr>
<th>Index</th>
<th>Close</th>
<th>Quarterly Change($)</th>
<th>Quarterly Change(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>DJIA</td>
<td>16,346.45</td>
<td>-738.04</td>
<td>-4.32%</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>1,922.03</td>
<td>-92.86</td>
<td>-4.61%</td>
</tr>
<tr>
<td>S&amp;P Energy</td>
<td>417.77</td>
<td>-88.41</td>
<td>-17.47%</td>
</tr>
<tr>
<td>S&amp;P Basic Materials</td>
<td>252.23</td>
<td>-25.03</td>
<td>-9.03%</td>
</tr>
<tr>
<td>Nasdaq</td>
<td>4,643.63</td>
<td>-186.84</td>
<td>-3.87%</td>
</tr>
<tr>
<td>Russell 2000</td>
<td>1,046.20</td>
<td>-119.15</td>
<td>-10.22%</td>
</tr>
<tr>
<td>Hang Seng Composite Index</td>
<td>2,806.71</td>
<td>-285.03</td>
<td>-9.22%</td>
</tr>
<tr>
<td>Korean KOSPI Index</td>
<td>1,917.62</td>
<td>-101.91</td>
<td>-5.05%</td>
</tr>
<tr>
<td>S&amp;P/TSX Canadian Gold Index</td>
<td>141.77</td>
<td>+1.61</td>
<td>+1.15%</td>
</tr>
<tr>
<td>XAU</td>
<td>47.10</td>
<td>-8.94</td>
<td>-15.95%</td>
</tr>
<tr>
<td>Gold Futures</td>
<td>1,103.80</td>
<td>-53.00</td>
<td>-4.58%</td>
</tr>
<tr>
<td>Oil Futures</td>
<td>32.96</td>
<td>-16.67</td>
<td>-33.59%</td>
</tr>
</tbody>
</table>
Natural Gas Futures 2.48 -0.02 -0.96%
10-Yr Treasury Bond 2.12 +0.03 +1.24%

U.S. Global Investors, Inc. is an investment adviser registered with the Securities and Exchange Commission ("SEC"). This does not mean that we are sponsored, recommended, or approved by the SEC, or that our abilities or qualifications in any respect have been passed upon by the SEC or any officer of the SEC.

This commentary should not be considered a solicitation or offering of any investment product.

Certain materials in this commentary may contain dated information. The information provided was current at the time of publication.

Some links above may be directed to third-party websites. U.S. Global Investors does not endorse all information supplied by these websites and is not responsible for their content.

All opinions expressed and data provided are subject to change without notice. Some of these opinions may not be appropriate to every investor.

Holdings may change daily. Holdings are reported as of the most recent quarter-end. The following securities mentioned above were held by one or more accounts managed by U.S. Global Investors as of 9/30/2015:
Alpha Bank AE,
Amazon.com Inc.,
Dow Chemical Co,
Facebook Inc.,
Google Inc.,
LyondellBasell Industries NV,
Time Warner Cable Inc.

The Dow Jones Industrial Average is a price-weighted average of 30 blue chip stocks that are generally leaders in their industry.
The S&P 500 Stock Index is a widely recognized capitalization-weighted index of 500 common stock prices in U.S. companies.
The Nasdaq Composite Index is a capitalization-weighted index of all Nasdaq National Market and SmallCap stocks.
The Russell 2000 Index® is a U.S. equity index measuring the performance of the 2,000 smallest companies in the Russell 3000®, a widely recognized small-cap index.
The Hang Seng Composite Index is a market capitalization-weighted index that comprises the top 200 companies listed on Stock Exchange of Hong Kong, based on average market cap for the 12 months.
The Taiwan Stock Exchange Index is a capitalization-weighted index of all listed common shares traded on the Taiwan Stock Exchange.
The Korea Stock Price Index is a capitalization-weighted index of all common shares and preferred shares on the Korean Stock Exchanges.
The Philadelphia Stock Exchange Gold and Silver Index (XAU) is a capitalization-weighted index that includes the leading companies involved in the mining of gold and silver.
The U.S. Trade Weighted Dollar Index provides a general indication of the international value of the U.S. dollar.
The S&P/TSX Canadian Gold Capped Sector Index is a modified capitalization-weighted index, whose equity weights are capped 25 percent and index constituents are derived from a subset stock pool of S&P/TSX Composite Index stocks.
The S&P 500 Energy Index is a capitalization-weighted index that tracks the companies in the energy sector as a subset of the S&P 500.
The S&P 500 Materials Index is a capitalization-weighted index that tracks the companies in the material sector as a subset of the S&P 500.
The S&P 500 Financials Index is a capitalization-weighted index. The index was developed with a base level of 10 for the 1941-43 base period.
The S&P 500 Industrials Index is a Materials Index is a capitalization-weighted index that tracks the companies in the industrial sector as a subset of the S&P 500.
The S&P 500 Consumer Discretionary Index is a capitalization-weighted index that tracks the companies in the consumer discretionary sector as a subset of the S&P 500.
The S&P 500 Information Technology Index is a capitalization-weighted index that tracks the companies in the information technology sector as a subset of the S&P 500.
The S&P 500 Consumer Staples Index is a Materials Index is a capitalization-weighted index that tracks the companies in the consumer staples sector as a subset of the S&P 500.
The S&P 500 Utilities Index is a capitalization-weighted index that tracks the companies in the utilities sector as a subset of the S&P 500.
The S&P 500 Healthcare Index is a capitalization-weighted index that tracks the companies in the healthcare sector as a subset of the S&P 500.
The S&P 500 Telecom Index is a Materials Index is a capitalization-weighted index that tracks the companies in the telecom sector as a subset of the S&P 500.
The NYSE Arca Gold Miners Index is a modified market capitalization weighted index comprised of publicly traded companies involved primarily in the mining for gold and silver.
The Consumer Price Index (CPI) is one of the most widely recognized price measures for tracking the price of a market basket of goods and services purchased by individuals. The weights of components are based on consumer spending patterns.
The Purchasing Manager’s Index is an indicator of the economic health of the manufacturing sector. The PMI index is based on five major indicators: new orders, inventory levels, production, supplier deliveries and the employment environment.

The University of Michigan Confidence Index is a survey of consumer confidence conducted by the University of Michigan. The report, released on the tenth of each month, gives a snapshot of whether or not consumers are willing to spend money.

The PFTS index is a benchmark index of PFTS Ukraine Stock Exchange, Ukraine’s leading bourse.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. MSCI World Index is a capitalization weighted index that monitors the performance of stocks from around the world.

The ISM manufacturing composite index is a diffusion index calculated from five of the eight sub-components of a monthly survey of purchasing managers at roughly 300 manufacturing firms from 21 industries in all 50 states.

The ISM Nonmanufacturing index based on surveys of more than 400 non-manufacturing firms’ purchasing and supply executives, within 60 sectors across the nation, by the Institute of Supply Management (ISM). The ISM Non-Manufacturing Index tracks economic data, like the ISM Non-Manufacturing Business Activity Index. A composite diffusion index is created based on the data from these surveys that monitors economic conditions of the nation.

The Shanghai Composite Index (SSE) is an index of all stocks that trade on the Shanghai Stock Exchange.

The cyclically adjusted PE ratio (CAPE) is a modification of the PE ratio to account for the effect on profits of the economic cycle.

The article references the investment theory of an investment as insurance against a separate market event that could negatively affect performance of an investment. The reference does not guarantee performance or a safeguard from loss of principal by investing in that asset.