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Opening Teaser: (00:00)

Research @ Citi, Markets Edition

Dirk Willer (00:04)

Welcome to Research @ Citi, Markets Edition, where we break down Global Macro in 10 minutes or less. I'm your host, Dirk Willer, Citi's Global Head of Macro, and with me today is Alex Saunders, our Quant Macro Head.

Welcome to the show, Alex.

Alex Saunders (00:18)

Thanks, Dirk.

Dirk Willer (00:19)

We are recording this podcast at 9 a.m. on Monday, Oct. 20, 2025.

One of the most interesting market moves has been the relentless rally in gold, which is seen as an expression of the debasement trade. We will discuss the debasement risk and what investors should do about it.

Now let's start with the definition. At its core, the debasement trade is based on the fear that fiat currencies will be debased by either aggressive fiscal and/or monetary policy.

And of course, you can see how these fears can arise in the U.S. We have 6% fiscal deficits as far as the eye can see and there is a big debate about the independence of the FOMC, which also may be at risk.

But it's, of course, also a global story. Fiscal globally is a worry. And even on the central-bank independence side, it's not clear that it's just the Fed, as there are questions being raised post-election, for example, even in Japan.

Now, what is the classic expression of the debasement trade? It's obviously long gold, but it's also, if it's a U.S.-centric debasement, it would be short the dollar. And even if it's not, steeper curves would qualify. You know, if the central bank cuts interest rates below neutral, then the curve steepens. And if you cut for reasons that are not just driven by big growth, but for other reasons, then the curve should steepen even more.

You would also expect rising break-evens, i.e. rising inflation expectations, and maybe even long equities could be part of the debasement trade. So at this time, really only gold is working, which is very interesting. Equities are up, not because of debasement fears, but really because of the AI bubble.

You could say, fine, maybe the dollar shouldn't weaken because it's a global debasement issue that people worry about. But why is inflation not up and why is the curve not steeper?

Well, on inflation, you could argue maybe the risk is the U.S. labor market weakening and no one wants to be long inflation when the U.S. labor market hits a trap door. And that's certainly true. The other reason could be that markets are bearish on oil. And whenever you're bearish oil, you probably would not really rush to buy break-evens, at least at the short end of the curve. So all that is true. And maybe with the steepener, again, you could argue that this mentioning of a third mandate would eventually mean that the Fed will manage the back end of the curve lower in yield terms. And so, you know, you find a story for why it might be only gold, but it's a bit of a tortured story, we think. It does make us a bit nervous just how very narrow this debasement trade is at this stage.

But Alex, another debasement trade that has been lost in action really is crypto. What are you seeing there?

Alex Saunders (02:56)

Thanks, Dirk.

So Bitcoin is a potential debasement asset as well, often viewed as digital gold, given it has similar characteristics and a limited supply. The biggest difference is in the much higher equity beta, especially on the downside.

This came to the fore in the week just gone, Oct. 10, when crypto sold off with equities on renewed U.S.-China trade tensions. The correlations between Bitcoin and gold had been rising, which we view as a positive sign for that transition from a speculative asset towards the underlying debasement-type properties, only for those correlations to fall back.

In fact, after hours on the Friday, we saw a large sell-off in crypto futures markets as long positions were liquidated. This serves as a reminder that Bitcoin has more of a correlation with equities than gold, and it could have an impact on flows. That impact would present downside risk to our positive forecasts, especially if equity risks become more pronounced, given that Bitcoin trades above our anchor, which is based on user activity.

However, we still think there is a positive flow story given the change in regulatory backdrop, the early stage of adoption within financial institutions. ETF flows have been persistent and they represent newer investors. Futures liquidations are zero-sum, and between leveraged and likely existing crypto holders in our view.

So, the important point is that it's not obvious that we're really trading debasement. It's very interesting, but Dirk, what should we do about it?

Dirk Willer (04:33)

Yeah, that's a good question. So, we had a very narrow debasement trade here. And let's dig a little bit deeper into gold then. The price action is very interesting. I mean, essentially, gold traded sideways between April and late August. And the news flow that caused the breakout was first and foremost the Jackson Hole testimony, which suggested a more dovish Fed.

And that's just normal. Gold likes to rally into the first Fed cut. Gold likes lower rates, gold likes a weaker dollar, and all that was just textbook. But the interesting point is that both the rates and the dollar really got stuck after the first cut and gold kept going. And that is I think partly because the third mandate was discussed, which really led a little bit to this again, debasement fears.

But now the question is given that it's such a narrow debasement rate, who is catching up with whom? Will the other potential debasement trades get a bid or will gold get stuck?

And of course, there's a lot of news for us still to come about the Fed chair, about Lisa Cook, and that all will be important. But of course, the court case is next year's business most likely. So we think actually gold is really quite stretched and the rally probably has at some stage to at least pause.

If you look at the deviation of gold from its 200-day moving average, there are only seven instances since 2006 when it was more than 20%. Now it's almost 30%. And whenever that happens, you typically get actually a pullback in the order of 6% over the next one or two months. Currently, it's as extreme as in 2020. And so we do think things will eventually have to slow down.

Now, I think the only reason why we don't worry about valuation in gold is that there is no valuation. If it was a stock, people I think would start to worry a bit more. And at this stage, we do think actually you really have to risk-manage your gold position, really quite carefully. Make sure you have the appropriate sizing on ... and you know everyone likes a bull market and we like it too, but you really have to risk-manage it carefully, I think.

Alex, you did some work on positioning on gold as well. What are your thoughts on that front?

Alex Saunders (06:42)

So on the positioning side, asset allocators are long. They're increased positioning in the last update that we did and it's one of the biggest consensus trades out there — I say long gold together with short dollars.

Flow-wise, to your point, Dirk, the ETF flows ex-China really picked up post-Jackson Hole, and they've been positive since then. And then more recently, a bit more high-frequency, we see the rallies in gold being predominantly in Asian hours, and we see the China inflows on the ETF side picking up.

Dirk Willer (07:14)

Great. Thanks a lot, Alex. So, to sum it up, overall the debasement trade is based on a sensible narrative, but it's a narrative, not a fact so far. The debasement trade is also quite narrow, really just in gold, and that raises question marks to us. So, we do think you need to really risk-manage gold positions quite carefully.

Thank you very much for joining today. This episode was recorded on Oct. 20, 2025, and I'm your host, Dirk Willer. For more details, Citi clients can check out our report on the Citi Velocity portal. If you enjoyed the podcast, please leave us a review on your favorite podcast platform.

Next week's Research @ Citi Markets Edition will be hosted by Scott Chronert, Citi's Head of U.S. Equity Strategy. And be sure to watch out for our Research @ Citi podcasts, which you can view on the same channel.

The Macro Strategy Team will be back in two weeks' time. Stay sharp.

Disclaimer (08:07)

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