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GLOBAL BANKING AND MARKETS

Metal Matters April 2018

The precious metals' prices have diverged – Gold prices are holding up in high ground, Silver is holding in mid-ground, while the PGMs are trending lower as a correction unfolds.

- The increase in cross currents affecting global markets is helping to keep Gold prices elevated, while the more industrial precious metals are suffering more.
- Gold prices sold-off again ahead of the FOMC meeting, only to rally when the statement was not as hawkish as expected.
- Equity market jitters and trade tensions have provided some lift to prices, but not enough to see prices break higher.
- The fund long liquidation has run its course and fresh buying combined with further short-covering has lifted fund exposure.
- Gold's chart continues to look potentially bullish, but a move above the $1,366-1,388/oz area is needed to signal a breakout.

Silver prices continue to hold up relatively well considering further fund short selling – the market is looking vulnerable though.

- The funds are positioned for a sell-off; if this does not materialize then a short-covering rally would be likely to follow.

PGM prices are under significant pressure; sentiment appears to have turned decidedly bearish, especially for Palladium, but we see this as a correction, rather than the start of a bear market.

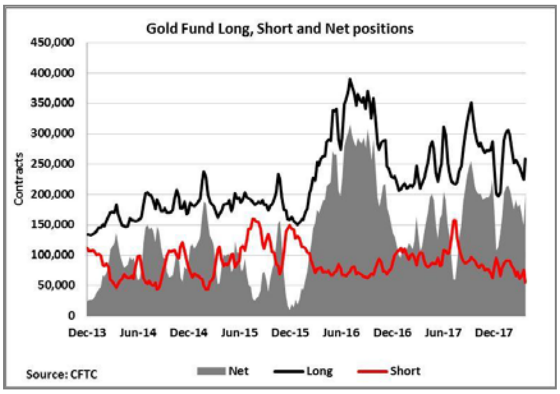
- We still expect concerted global growth and restricted supply to prompt restocking in the PGMs.

Less stable equity markets combined with trade tensions support firmer Gold prices

Gold's prices rebounded to $1,356.75/oz in late March, having been as low as $1,302.85/oz on 1st March. The weakness was part of a broad-based sell-off following President Donald Trump's announcement of plans to impose import tariffs on steel and aluminium. The knee-jerk downward reaction to the news was driven by traders taking risk off the table, which saw Gold prices sell off too, but the secondary reaction saw safe-haven buying emerge, leading to Gold prices rebounding to $1,340.60/oz by 6th March. As the initial trade war rhetoric died down, Gold prices drifted back to a low of $1,307.25/oz on March 20, which was the eve of the March Federal Open Market Committee (FOMC) meeting. Traders expected the FOMC statement to be more hawkish as the new Federal Reserve chair, Jerome Powell, had in earlier remarks sounded more hawkish than his predecessor Janet Yellen had. The FOMC statement, however, turned out not to be hawkish, with the Fed indicating three interest rate rises were likely in 2018, rather than the four the market had started to expect. This led to another sharp rally in Gold prices to $1,356.75/oz. Trading has since been choppy, reacting to a mixture of varying economic data and increased rhetoric over tariffs, especially between the US and China.

Gold has potential as outlook clouds over

Disappointing economic data, combined with prospects for trade wars with the US, has cast a shadow over whether concerted global economic growth will continue. The already rich bull market in equities may well have been able to extend further had global growth gained momentum, but with growth showing signs of slowing and trade disputes threatening to put the brakes on it, the outlook is not so bright. JP Morgan's global composite manufacturing PMI slipped to 53.4 in March, from 54.1 in February, 54.4 in January and a recent peak of 54.5 in December. Slower growth combined with the potential for trade wars is likely to prompt further risk reduction in equities and a pick-up in demand for safe-havens. In addition, with growth potentially set to slow down, US treasury yields have fallen which reduces the opportunity cost of holding Gold.

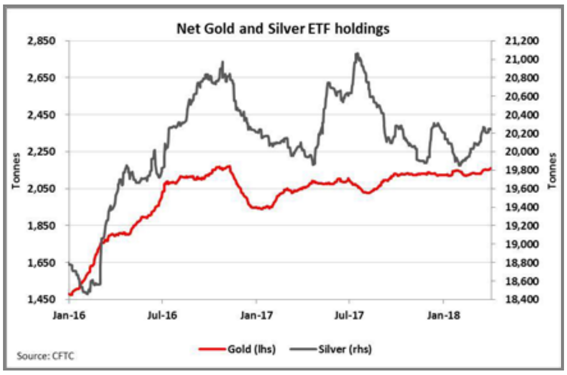


Funds turn buyers again on Comex

The net long fund position (NLFP) has up until recently been declining, but this has mainly been a result of stale long liquidation, as seen by the drop in the black line in the chart above. But, while the longs have cut exposure (until recently); shorts have not been getting bearish, as seen by the declining red line. This has suggested longs have grown impatient as Gold prices have failed to break higher, but lack of upside has not encouraged bears to increase exposure. More recently, fund longs have started to increase exposure again. The gross long fund position has climbed to 259,032 contracts as of 27th March, from a recent low of 223,882 contracts. The NLFP has returned to 203,354 contracts from a low of 148,731 contracts on 20th March. This latest change was driven by 35,150 contracts of fresh buying and 19,473 contracts of short-covering.

Investors increase exposure to ETFs

Holdings in Gold ETFs are edging higher with investors adding 18.5 tonnes in March. Holdings now stand at 2,162 tonnes, up some 39 tonnes so far this year. Holdings averaged 2,068 tonnes in 2017. Given the lukewarm investor interest in Gold ETFs, it may be that the market is waiting for prices to break higher above the $1,366-$1,388/oz resistance area before increasing exposure.



Gold rangebound as big picture is mixed

While Gold prices have picked up some safe-haven interest on the back of trade war concerns and jittery equity markets, some geopolitical developments are expected to ease the need for safe-haven demand. Talk of summits between the US and North Korea and between the US and Russia, as well as constructive developments between some of the Arab majors and Israel, all point towards some easing in geopolitical tensions. With Gold prices rising last year on the back of tensions over North Korea, any concrete positive developments in this area could weigh on Gold prices. That said, Saudi Arabia's positive stance towards Israel may well increase tensions with Iran, who have said the Saudi move is a 'big, unforgivable mistake'. Any increased tensions between Saudi Arabia and Iran may well play out in the oil market, which in turn could be another supportive factor for Gold prices, if higher oil prices boost inflation fears. So, for now, there seem to be numerous cross currents flowing through the Gold market that are likely to keep prices rangebound until further developments unfold.

Dollar and US interest rates

Given rising US interest rates, many investors have been surprised by the weakness in the dollar. It seems that the run-up in the dollar from 2014 to late 2016 was in anticipation of tighter US monetary policy, so when interest rates actually started to rise it was already in the price – a classic example of 'buy the rumour sell the fact'. However, now that dollar, basis the dollar index, has undergone a 15 percent correction from the highs, it may be that continuing tighter monetary policy starts to support the dollar again, especially if global (and particularly US) growth resumes. If the dollar does start to rise again then that may put a cap on Gold prices, although if industrial commodity prices resume their upward trends, then Gold prices may be able to rise in tandem with the dollar and commodity prices.

Technical – This weekly chart of Gold prices shows a potential large 'W'-shaped base formation with prices being capped by the resistance line ($1,365.50/oz) that runs along the top of the pattern. The chart picture has not changed much so far this year, but the ascending triangle does favour an eventual upside break. Prices are also holding above the 20-week moving average, although the stochastics are not looking that bullish, suggesting the market is not in a hurry to push higher. Each move above $1,366/oz, $1,375/oz and $1,388/oz would be a step further towards breaking higher.

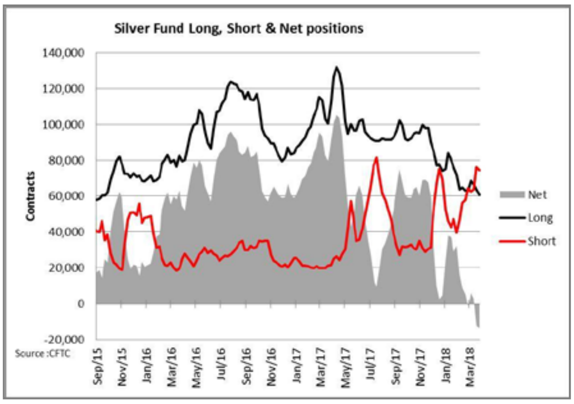
Summary – There are a lot of cross currents flowing through the Gold market, but on balance Gold prices are holding up well and that suggests underlying sentiment is firm. We expect dips to remain well supported.

Gold Statistics	2014	2015	2016	2017	Q4 2017	Q1 2018	Feb-18	Mar-18
London Prices (US$/oz)								
AM fix	1266.34	1162.49	1248.16	1257.85	1276.51	1330.72	1333.78	1325.56
Pm fix	1266.20	1161.30	1248.34	1257.13	1274.35	1329.29	1331.53	1324.66
Average	1266.27	1161.89	1248.25	1257.49	1275.43	1330.00	1332.66	1325.11
Parity prices								
Australian - A$/oz	1,403	1,544	1678.88	1645.14	1,659	1,638	1,528	1,709
South Africa Rand/kg	440,562	474,410	589,051	537,559	558,876	510,684	505,955	504,168
Japan Y/g	4,146	4,355	4,203	4,370	4,463	4,464	4,459	4,354
India Rupee/oz	77,077	74,310	83,721	81,767	82,499	85,492	85,796	86,079
COMEX - futures contracts								
Stocks ('000oz)	8,203	7,422	8,962	8,860	8,970	9,151	9,134	9,062
Vol (million contracts)	40.52	41.76	51.84	72.80	20.47	14.11	6.08	8.04
OI ('000 contracts)	380	418	550.71	479.85	511	518	500	500
CFTC (futures only data)								
Net Spec position Long (Short)	98,265	88,022	201,250	163,493	166,887	198,919	178,718	203,354
TOCOM								
Stocks ('000oz)	146	127	120	73	60	57	65	57
Volume ('000 contracts)	8,744	7,928	8,540	5,750	1,524	1,544	849	695
OI ('000 contracts)	88	94	88	87	98	101	108	105
Other Indicators								
FT Au Mines Index	1,409	1,061	1,579	1,521	1,472	1470	1,410	1,424
Dow Jones Index	16,837	17,524	18,062	21,990	24,113	25,094	25,029	24,103
US$ Index	83.0	96.7	97.1	96.0	93.3	89.9	90.7	90.0
Gold Bullion Imports, tonnes (exports)								
Dubai	136	118	~					
China	1297	1610	1,281					
India	776	949	582					
Italy	103	~	~					
Japan	-80	-107	~					
Singapore	284	~	~					
South Korea	24 ~		~					
Taiwan	22	30	28					
Turkey	102	49	106					

Data: Financial Times; Bombay Bullion Association; LBMA; TOCOM; COMEX; CFTC, REUTERS
Figures are period averages unless marked by *, indicating the period end. OI= Open Interest on the exchange
~ = data not available yet, *italics* = estimates

Silver prices set to become volatile – will a sell-off, or a short-covering rally follow?

Silver prices remain range bound, with supply evident above $16.80/oz and buying providing support below $16.20/oz. Prices are generally mirroring Gold prices and have so far avoided following the PGM prices, which have broken below support. One interesting observation is that investors in Silver ETFs continue to buy, while the funds trading Silver futures on Comex have increased their net short position. Given this it is surprising that Silver prices have not broken lower as have the PGMs.



ETF investors buy Silver

As the chart in the Gold section shows, Silver investors continue to favor Silver, buying 209 tonnes in March thus increasing their holdings to 20,240 tonnes, this after a low of 19,851 tonnes in early February.

Funds increase short exposure

While investors have been adding to positions, the funds have become increasingly bearish, with the Net Short Fund Position (NSFP) climbing to 13,657 contracts from 1,508 contracts in late February. Before the shift to being net short in late February, the last time the market had been net short was in March 2003, which was near the start of the bull run in bullion prices. Given the growing NSFP, there is increased risk of Silver prices falling further, but if that does not unfold, then in time a short-covering rally could provide energy on the upside. The gross short position stands at 74,329 contracts; the peak was 81,400 contracts in July last year, while the average since 2008 has been 21,564 contracts, which highlights how large the short position is.

Silver - a precious or industrial metal?

While Silver prices are holding up better than the PGMs, suggesting its precious metals/safe-haven attributes are helping it, it does seem to have been under pressure of late on the back of the weakness seen in the base metals. Overall, we think Silver's industrial outlook is strong as we move into a significantly broader electrical world; as such, we are surprised by how bearish the funds are.

Technical – Silver prices remain under pressure in that most of the trading since early February has been done below the 20-week moving average, but support is still holding around $16.20/oz and the underlying up trend line seems to be providing support too, at least so far. The stochastics are, however, in low ground, so a break lower could still be seen.

Summary – Fundamentally we remain bullish for Silver prices and the fact the market has had to absorb considerable selling and shorting from the funds suggests there is still buying interest around. Given the size of the gross short position, if prices do not break lower, then there may well be a counter move to the upside driven by short-covering.

Silver Statistics	2014	2015	2016	2017	Q4 2017	Q1 2018	Feb-18	Mar-18
London Prices (US$/oz)								
Daily Fix	19.08	15.71	17.10	17.05	16.70	16.77	16.66	16.47
Parity (London) prices								
Japan (Y/g)	70.31	58.92	57.46	59.27	58.44	56.29	55.74	54.12
India (Rupee/oz)	1,312.5	1,004.7	1,147.5	1,109.5	1,080.4	1,078	1,072.5	1,069.9
COMEX – futures contracts								
Stocks (Moz)*	178.9	171.6	162.1	210.8	237.4	253.8	251.8	262.7
Vol (million contracts)	13.7	13.5	17.0	23.0	5.8	4.0	2.2	1.8
OI ('000 contracts)*	155.8	169.6	188.8	191.6	169.9	191.8	148.0	229.1
CFTC (Futures Only Data) non-commercial								
Net Positions *	19,307	31,269	69,366	56,301	33,731	4,639	- 1,508	- 13,657
TOCOM								
Stocks (Moz)*	0.2	0.16	0.16	0.18	0.11	0.14	0.13	0.14
Futures Vol ('000 contracts)	86.1	62.6	61.1	20.6	4.5	4.1	2.4	1.8
Futures OI ('000 contracts)*	4.5	3.1	3.3	1.8	1.6	1.9	2.1	2.2
Other Indicators								
Gold/Silver ratio*	67.6	74.4	73.0	74.3	76.8	79.5	79.6	81.3
Silver Bullion Imports (tonnes)								
USA	3835	5464	5956					
Japan	1688	1560	1833					
India	5819	7954	2793					
Italy	796	843	675					
Hong Kong	948	839	659					
China (exports)	1369	2054	-137					

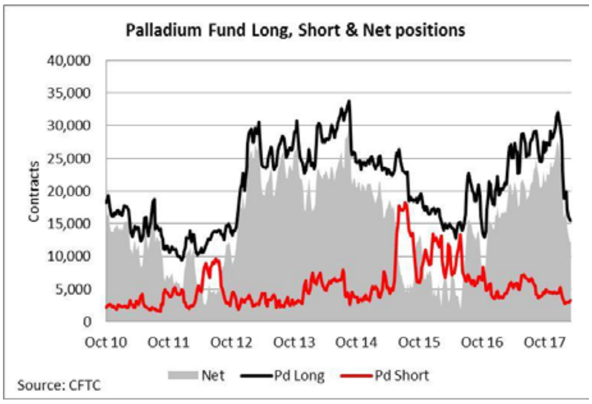
* figures are period averages unless marked; ~ not available yet, *italics* = estimate.

PGM prices are correcting, funds and investors take profits into the sell-off

Palladium prices have slumped to $915/oz having reached a high of $1,140/oz on 15th January, a drop of 19.7 percent. Platinum prices that only started to rally in December have over the past few months given back 78 percent of their gains. Platinum prices peaked at $1,029.50/oz in late January, having rallied from a low of $873/oz in mid-December, but have since dropped to $907/z, a fall of 11.9 percent.

What has hit sentiment?

It may be that high expectations for electric vehicles (EV) have dampened sentiment, or the slower growth outlook for global vehicle sales this year. If the former, then we would say the market is jumping well ahead of the fundamentals. Although the EV revolution is underway, it is starting from a very low base and it is likely to be many years before EVs lead to a reduced demand for PGMs from the auto industry. With auto emission legislation still tightening, the PGM loadings are likely to increase overall demand. However, we are not so surprised that Palladium prices have fallen more than Platinum prices, as we have expected for some time now that Platinum would increasingly start to be used in autocatalysts for petrol engines as manufacturers seek to reduce dependency on Palladium, with its tighter fundamentals.

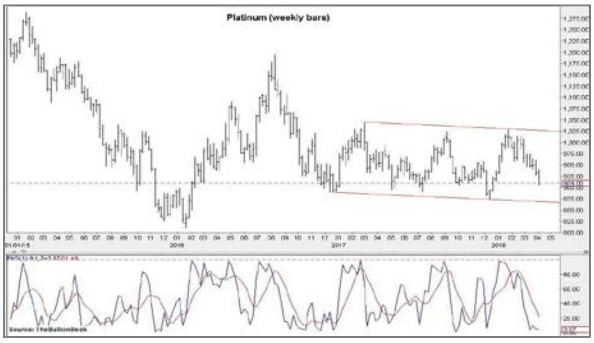


Funds cut exposure at a fast pace

The Net Long Fund Positions (NLFP) on the Nymex Platinum and Palladium contracts have fallen in recent months. On Platinum, the NLFP ramped up in December to peak at 41,753 contracts on 30th January, but has since fallen to 28,039 contracts. The fund action has tracked the price action. For Palladium, the NLFP peaked at 27,614 contracts on 9th January, but has since dropped to 12,047 contracts (see chart opposite). In both metals, it has been long liquidation that has led to the drop in the NLFP.

ETF investors reduce exposure

Investors in Platinum ETFs have been slowly reducing exposure; by the end of March, holdings stood at 2.413 Moz, down from 2.426 Moz at the start of the year. For Palladium, holdings ended March at 1.146 Moz, from 1.331 Moz at the start of the year.



Technical & Summary - Both PGM prices are trending lower and the near 20 percent correction in Palladium prices signals a possible bear market. The correction in Palladium prices is not surprising given the price gains in recent years and it looks as if Platinum prices are being pulled down in line with the weaker prices in Palladium and industrial metals generally. The fundamentals for both metals do not look bearish, and Palladium's strong fundamentals remain in place, so we would expect dip buying before too long to provide support.

PGM Statistics	2014	2015	2016	2017	Q4 2017	Q1 2018	Feb-18	Mar-18
London Prices (US$/oz)								
Platinum	1,390	1,060	976	949	921	978	991	955
Palladium	809	692	611	869	992	1,035	1,023	987
Rhodium	1,180	953	694	1,101	1,477	1,826	1,848	1,925
Japanese Parity Prices (Y/g)								
Platinum	4,519	3,965	3,278	3,298	3,221	3,283	3,315	3,138
Palladium	2,636	2,587	2,050	3,020	3,472	3,478	3,424	3,243
South African Parity Prices (Rand/kg)								
Platinum	466,074	417,839	444,891	391,696	389,038	362,060	362,711	350,336
NYMEX Stocks ('000oz)								
Platinum	195.8	138.8	205.1	215.0	194.6	183.4	186.0	185.3
Palladium	347.4	134.0	71.1	50.2	49.6	41.8	43.0	41.6
CFTC Futures Only Data Long / (short) non-commercial								
Platinum	35,840	24,585	31,817	24,302	21,430	37,569	41,751	28,039
Palladium	22,276	12,080	8,765	20,660	23,565	18,564	16,983	12,047
Tocom - Platinum								
Stocks ('000oz)	46.6	53.8	57.1	47.1	54.2	56.3	53.9	56.3
Vol (Million contracts)	4.6	3.9	2.9	2.5	0.6	0.5	0.2	0.3
OI ('000 contracts)	72.6	69.7	52.7	56.8	55.0	50.6	46.4	60.0
Tocom - Palladium								
Stocks ('000oz)	3.2	5.4	11.1	3.6	1.0	0.9	0.9	0.87
Vol ('000 contracts)	77	63	30	32	9.3	7.6	4.7	2.9
OI ('000 contracts)	2.0	1.8	1.1	1.4	1.4	1.4	1.4	1.4
Other Indicators (US$/oz)								
Pt-Au spread	115	-100	-253	-320	-355	-374	-366	-412
Pt-Pd spread	568	245	369	59	-77	-16	-18	-2
Platinum Bullion imports (kg)	2014	2015	2016	2017		2018		
USA	141,413	238,740	201,412	431,277		11,712	(Jan)	
Japan	32,684	47,283	44,786	42,986		6,122	(Jan-Feb)	
PalladiumBullion imports (kg)	2014	2015	2016	2017				
USA	92,400	82,500	88,800	86,000		7,172	(Jan)	
Japan	58,429	57,223	58,860	59,492		9,709	(Jan-Feb)	

~ = data not available yet, *italics* = estimates

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