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GLOBAL BANKING AND MARKETS

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Metal Matters March 2018

The precious metals' prices were under pressure in February as US monetary talk turned more hawkish and as the broader markets suggested sell-offs that dragged Gold down too.

- Dips in Gold prices continued to be short-lived and underlying spikes lower highlight good bargain hunting. Support has been evident ahead of $1,300/oz.
- There are a number of cross currents flowing through the Gold market but even the bearish ones could potentially turn out to be bullish for Gold if investors need to park money in safe-havens.
- With prices appearing capped on the upside, funds have taken profits but there has been little pick-up in short selling. This suggests funds/investors are not bearish per se.
- The Gold chart continues to look bullish with prices well placed to break out of a multi-year base.
- Low jewellery demand has been the weak link for Gold; we wait to see if concerted global growth spurs jewellery demand.

Silver prices have held up surprisingly well considering the funds have turned net bearish for the first time in 15 years.

- ETF investors have been buying, suggesting the funds' bearish stance runs the risk of creating an oversold condition.

PGM prices have corrected lower; we see this as being part of the general weaker tone in industrial metals.

- We expect concerted global growth and restricted supply to underpin the overall bullish trends in the PGMs.

Gold prices have been under pressure, but dips continue to attract buying

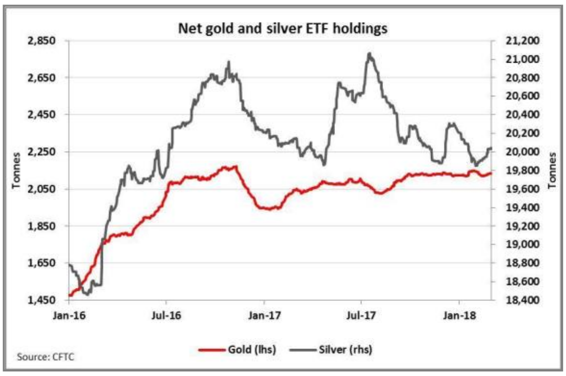
Gold's prices are consolidating above $1,300/oz; this after the early February rebound ran out of steam in mid-February at $1,361.80/oz, falling short of the late-January peak of $1,366.15/oz. It appears Gold prices have run into resistance in high ground, with the recent peaks all hovering below the all-important July 2016 high at $1,375.25/oz. The climate for Gold has been quite diverse of late with rising US Treasury bond yields, a more hawkish Fed and reduced geopolitical tensions all negative factors for Gold, while the potential for corrections in equity and bond markets and trade wars are potentially bullish factors.

Higher treasury yields a headwind

US ten-year treasury yields have climbed to 2.95 percent, up from 2.4 percent at the start of the year and a low of around 2.05 percent in September last year. Despite this headwind, Gold prices have managed to extend gains to levels not seen for 17 months, although in more recent weeks the fact yields have approached the 3 percent level does seem to have capped bullishness. But higher yields are a double edged-sword for Gold. On the one hand, they increase the opportunity cost of holding Gold, while on the other hand, higher yields could prompt profit-taking in equities/bonds and raise fears of a recession, which could increase investors' demand for safe-havens.

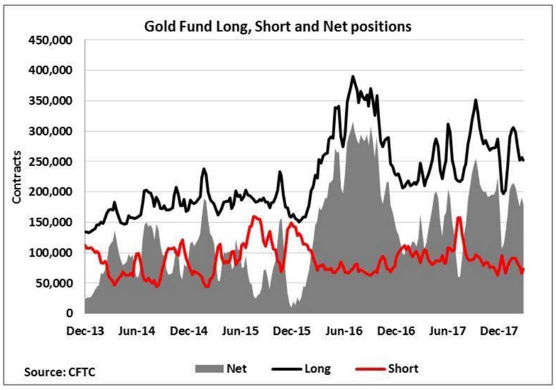
New Fed chair starts on a hawkish note

Jerome Powell took over the Federal Reserve chair from Janet Yellen and his first comments were more hawkish than the market was expecting. This lifted treasury yields, led to a stronger dollar and sent jitters through equity markets around the world. As is often the case, when markets first become jittery all markets can sell off, but for Gold there is often a secondary reaction that is bullish as those taking risk off the table look to buy safe-havens while the turbulence lasts. So, while Gold prices sold off sharply from $1,336/oz to $1,302.85/oz between 27th February and 1st March (during which time the Dow Jones fell 1,500 points, a drop of 6 percent), prices have since rebounded to $1,332/oz. Another potential supporting factor is the increased chance of a trade war between the US and its trading partners after President Donald Trump imposed tariffs on steel and aluminium.



ETF investors remain committed

Despite the weaker Gold prices in recent weeks, investors in ETFs are not reducing exposure. Holdings stand at 2,130 tonnes - the range so far this year being 2,120-2,149 tonnes, while holdings averaged 2,068 tonnes in 2017.



Net long fund position declines

Although the net long fund position (NLFP) on Comex has fallen in recent weeks (down to 178,718 contracts on 27th February from 214,684 contracts on 23rd January), the position remains fairly elevated. In mid-December, ahead of the expected US interest rate rise, the NLFP had dropped to 107,068 contracts. As the chart shows, most of the weakness has come from long liquidation, rather than from short-selling. At 73,263 contracts, the gross short position remains low, as shown by the red line on the chart above. This suggests that some investors have grown tired of waiting for Gold prices to push higher and have taken profits, but the lack of any meaningful increase in the gross short position suggests investors are not that bearish.

Return of jewellery demand
Gold demand from the jewellery industry increased four percent to 2,136 tonnes in 2017, which was the first annual increase since 2013. With more concerted global growth now underway, we expect demand in this sector to continue to recover. The average offtake by the jewellery industry in the years 2013 to 2015 was 2,537 tonnes, which means there is considerable room for demand to recover. Jewellery demand in 2016 was particularly hard hit in India, as it had been in China between 2014 and 2016. In India a string of government regulations and restrictions hit demand, but with the country now becoming accustomed to the new regulations, we expect demand to recover. It recovered 11.5 percent in 2017, but at 562 tonnes was still 10.7 percent below the average seen between 2010 and 2015. In China, economic hardship combined with the government's anti-corruption drive of recent years has hit demand, but it showed signs of recovering in 2017, rising 3% to 647 tonnes, but that was still down from the average of 906 tonnes seen between 2013 and 2015. With China and India's middle classes growing at a fast pace and with global economic growth recovering, we expect a boost in spending on luxury items. This is especially so in China, where investment in property is being restricted.

Gold looks a good insurance
Having Gold as part of a commodity basket also makes sense as it offers a degree of insurance should either the broader market suffer a correction, or geopolitical issues escalate – the latter looks less likely at present, but we remain concerned that North Korea's 'olive-branch' gestures may be seen as the country playing for time as it strengthens its nuclear power. Market-wise, we have seen more jittery equities and the VIX index, showing volatility in the S&P, has itself become more volatile with a surge to 37; it has recently been oscillating either side of 20 after months of moving sideways either side of 10. The pick-up in volatility may be a pre-cursor to an equity market correction.

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 stochastics have turned lower again so buying pressure is low, but support is being found from the higher of the two up-trend lines and prices look well placed to challenge overhead resistance again. Each move above $1,366/oz, $1,375/oz and $1,388/oz would be a step further towards breaking higher.

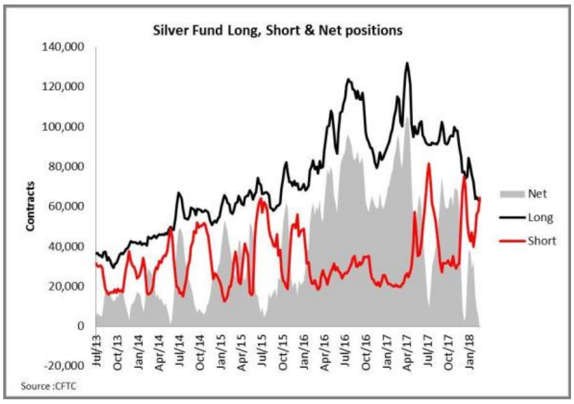
Summary – There are a lot of cross currents flowing through the Gold market, but on balance Gold prices are holding up well and that suggests underlying sentiment is firm. Gold could be in a win-win situation; it could continue to benefit from concerted global growth, while if broader markets look set to correct it could also benefit from increased safe-haven demand.

Gold Statistics	2014	2015	2016	2017	Q3 2017	Q4 2017	Jan-18	Feb-18
London Prices (US$/oz)								
AM fix	1266.34	1162.49	1248.16	1257.85	1277.96	1276.51	1332.81	1333.78
Pm fix	1266.20	1161.30	1248.34	1257.13	1277.84	1274.35	1331.67	1331.53
Average	1266.27	1161.89	1248.25	1257.49	1277.90	1275.43	1332.24	1332.66
Parity prices								
Australian - A$/oz	1,403	1,544	1678.88	1645.14	1,637	1,659	1,676	1,528
South Africa Rand/kg	440,562	474,410	589,051	537,559	540,737	558,876	521,928	505,955
Japan Y/g	4,146	4,355	4,203	4,370	4,393	4,463	4,581	4,459
India Rupee/oz	77,077	74,310	83,721	81,767	82,069	82,499	84,600	85,796
COMEX - futures contracts								
Stocks ('000oz)	8,203	7,422	8,962	8,860	8,707	8,970	9,258	9,134
Vol (million contracts)	40.52	41.76	51.84	72.80	19.95	20.47	9.16	6.08
OI ('000 contracts)	380	418	550.71	479.85	512	511	554	500
CFTC (futures only data)								
Net Spec position Long (Short)	98,265	88,022	201,250	163,493	178,157	166,887	214,684	178,718
TOCOM								
Stocks ('000oz)	146	127	120	73	67	60	67	~
Volume ('000 contracts)	8,744	7,928	8,540	5,750	1,233	1,524	796	849
OI ('000 contracts)	88	94	88	87	92	98	91	108
Other Indicators								
FT Au Mines Index	1,409	1,061	1,579	1,521	1,566	1,472	1,576	1,410
Dow Jones Index	16,837	17,524	18,062	21,990	22,096	24,113	26,149	25,029
US$ Index	83.0	96.7	97.1	96.0	92.9	93.3	89.1	90.7
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 hold up quite well considering funds turn net bearish

Silver's firm start to the year has waned; prices peaked at $17.703/oz in January, up from a low of $15.623/oz on 12th December, but have slipped to a low of $16.755/oz in early March. The 20-day moving average is trending lower, but dips below $16.20/oz have tended to be short-lived. One interesting development is that funds trading on Comex have turned net bearish for the first time since April 2003.



Funds turn net short

The net fund position (NFP) has dropped to short 1,508 contracts; as the shaded area on the chart shows, the NFP has been increasingly volatile since it peaked at long 105,515 contracts in April last year. What is noteworthy is that the funds have become increasingly bearish on the back of persistent long liquidation as well as recent short-selling. Generally, when the net long fund position (NLFP) has got low, short-covering has followed. The gross short position has a habit of being volatile, but perhaps more worrying is the strong downward trend in the gross long position as can be seen by the falling black line. This suggests investors are losing interest in Silver's upside potential. While the fund position has turned bearish, prices have held up relatively well, which suggests a degree of positive divergence. If prices end up finding support then that could prompt short-covering, especially as the gross short position is already relatively high.

ETF investors are buyers

The pullback in Silver prices from recent highs, combined with rebounds off the price dips below $16.20/oz, have attracted ETF investor interest with holdings rising to 20,044 tonnes, up from 19,853 tonnes at the end of January (see the chart in Gold section). The fact ETF investors are buying and the funds trading futures are becoming less bullish and more bearish is another sign of divergence.

Electrification of the world

The world seems to be moving towards being driven more by electricity whether it be electric vehicles (EV), alternative energy generation or the 'internet of things', and Silver should benefit as a result. Photovoltaic cells and many of the small electrical devices used both in the internet of things and in the sensors being fitted to EVs use Silver, even if in tiny/small amounts, but collectively these all add up.

Technical – Silver prices are under pressure in that most of the trading since early February has been done below the 20-day moving average, but support is evident below $16.20/oz and the underlying up trend line seems to be providing support too. The stochastics have also recently turned higher again.

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 buying interest around to absorb the selling. We would be on the lookout for a short-covering rebound before too long.

Silver Statistics	2014	2015	2016	2017	Q3 2017	Q4 2017	Jan-18	Feb-18
London Prices (US$/oz)								
Daily Fix	19.08	15.71	17.10	17.05	16.83	16.70	17.17	16.66
Parity (London) prices								
Japan (Y/g)	70.31	58.92	57.46	59.27	57.87	58.44	59.03	55.74
India (Rupee/oz)	1,312.5	1,004.7	1,147.5	1,109.5	1,081.2	1,080.4	1,090.2	1,072.5
COMEX – futures contracts								
Stocks (Moz)*	178.9	171.6	162.1	210.8	216.5	237.4	247.0	251.8
Vol (million contracts)	13.7	13.5	17.0	23.0	6.2	5.8	2.2	2.2
OI ('000 contracts)*	155.8	169.6	188.8	191.6	192.3	169.9	198.2	148.0
CFTC (Futures Only Data) non-commercial								
Net Positions *	19,307	31,269	69,366	56,301	44,441	33,731	29,081	- 1,508
TOCOM								
Stocks (Moz)*	0.2	0.16	0.16	0.18	0.16	0.11	0.13	~
Futures Vol ('000 contracts)	86.1	62.6	61.1	20.6	3.8	4.5	1.6	2.4
Futures OI ('000 contracts)*	4.5	3.1	3.3	1.8	1.8	1.6	1.4	2.1
Other Indicators								
Gold/Silver ratio*	67.6	74.4	73.0	74.3	75.8	76.8	77.7	79.6
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					

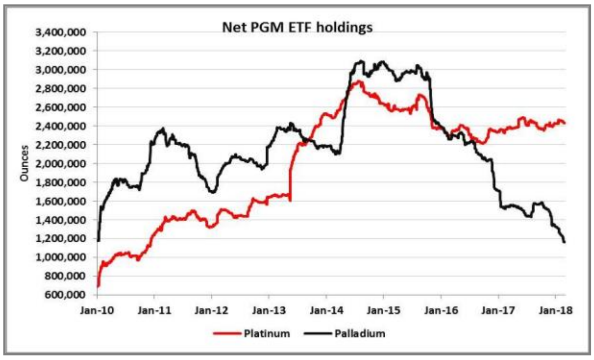
* figures are period averages unless marked; ~ not available yet, *italics* = estimate.

PGM prices correct in line with weaker sentiment across metals

Palladium prices set a high of $1,140/oz on 15th January, but have since corrected to $960/oz (a drop of 15.8 percent) and prices are recently quoted at $980/oz. Platinum prices put in a strong rebound in December and January, running up to $1,029.50/oz, but they have more recently been consolidating around the $965/oz level. At Palladium's price peak, its premium over Platinum prices was $138/oz; it has since fallen to a $25/oz premium – we think this signals the start of some convergence that will be driven by Platinum gaining some market share from Palladium in the manufacture of autocatalysts for petrol vehicles. We expect the prospects for growing shortages of Palladium to lead auto manufacturers to reduce their dependence on Palladium for future vehicle models. This may help offset the negative implications of increased anti-diesel sentiment, which has recently been given a further boost as German courts said older diesel vehicles could be banned from cities.

South African miners face rising costs

The South African rand has strengthened in recent months and that has been helped by the political changes, but the stronger rand will put further pressure on South African miners as they will receive less rand when they sell their metal in dollars.The rand has climbed from an average over the past six months of 13 to the dollar to 11.75 to the dollar - an increase of ten percent.

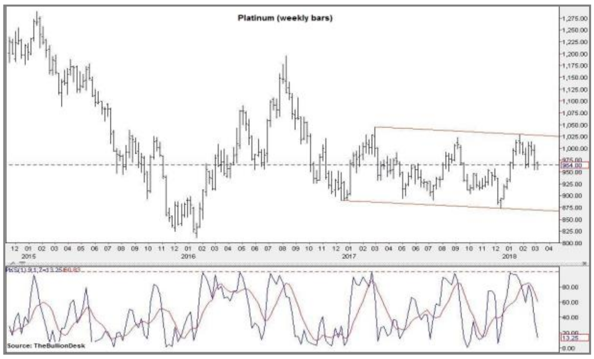


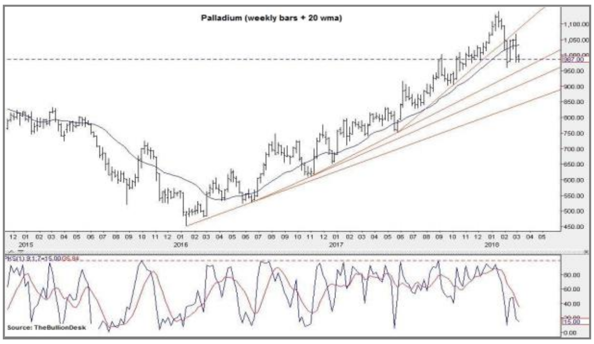
ETF investors continue to cut Pd exposure

Investors holding Palladium in ETFs continue to cut exposure with holdings dropping to 1.16 million ounces (Moz), down from 1.330 Moz at the end of 2017. Given a bullish outlook, it is not inconceivable that investors start buying Palladium again – that would reduce supply and increase demand, which could have a bullish impact on prices. Interest in Platinum ETFs is subdued with holdings standing at 2.427 Moz, the range this year being 2.423 - 2.464 Moz. Generally, investment in PGMs is probably suffering on the back of the EV story, but we think PGM demand from internal-combustion-engined vehicles will continue to rise for many a year.

Funds bullish on Pt, take profits on Pd

Funds trading Nymex Platinum have increased long exposure and cut short exposure this year with the net long fund position (NLFP) rising to 41,751 contracts from 16,313 contracts at the end of 2017. For Palladium, the NLFP has dropped to 16,983 contracts from 24,498 contracts over the same period, while the gross long position has fallen by around 33 percent.





Technical & Summary - Both PGM prices have run into resistance and sentiment across the metals has turned less bullish. This is likely to lead to further consoliation, but concerted global growth and supply restraints are likely to keep PGM prices underpinned and bullish overall.

PGM Statistics	2014	2015	2016	2017	Q3 2017	Q4 2017	Jan-18	Feb-18
London Prices (US$/oz)								
Platinum	1,390	1,060	976	949	953	921	988	991
Palladium	809	692	611	869	901	992	1,095	1,023
Rhodium	1,180	953	694	1,101	1,077	1,477	1,706	1,848
Japanese Parity Prices (Y/g)								
Platinum	4,519	3,965	3,278	3,298	3,275	3,221	3,396	3,315
Palladium	2,636	2,587	2,050	3,020	3,097	3,472	3,766	3,423.96
South African Parity Prices (Rand/kg)								
Platinum	466,074	417,839	444,891	391,696	388,728	389,038	373,134	362,711
NYMEX Stocks ('000oz)								
Platinum	195.8	138.8	205.1	215.0	214.0	194.6	178.8	186.0
Palladium	347.4	134.0	71.1	50.2	47.0	49.6	40.7	43.0
CFTC Futures Only Data Long / (short) non-commercial								
Platinum	35,840	24,585	31,817	24,302	23,972	21,430	42,916	41,751
Palladium	22,276	12,080	8,765	20,660	21,134	23,565	26,663	16,983
Tocom - Platinum								
Stocks ('000oz)	46.6	53.8	57.1	47.1	46.1	54.2	52.2	~
Vol (Million contracts)	4.6	3.9	2.9	2.5	0.4	0.6	0.3	0.2
OI ('000 contracts)	72.6	69.7	52.7	56.8	60.2	55.0	45.3	46.4
Tocom - Palladium								
Stocks ('000oz)	3.2	5.4	11.1	3.6	3.1	1.0	0.8	~
Vol ('000 contracts)	77	63	30	32	5.5	9.3	3.3	4.7
OI ('000 contracts)	2.0	1.8	1.1	1.4	1.6	1.4	1.3	1.4
Other Indicators (US$/oz)								
Pt-Au spread	115	-100	-253	-320	-341	-355	-343	-366
Pt-Pd spread	568	245	369	59	30	-77	-29	-18
Platinum Bullion imports (kg)	2014	2015	2016	2017		2017		
USA	141,413	238,740	201,412	431,277		~	(Jan)	
Japan	32,684	47,283	44,786	42,986		3,181	(Jan)	
PalladiumBullion imports (kg)	2014	2015	2016	2017				
USA	92,400	82,500	88,800	86,000		~	(Jan)	
Japan	58,429	57,223	58,860	59,492		4,642	(Jan)	

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

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