Precious Metals Monthly: Platinums time to eek out an outperformance

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Summary:

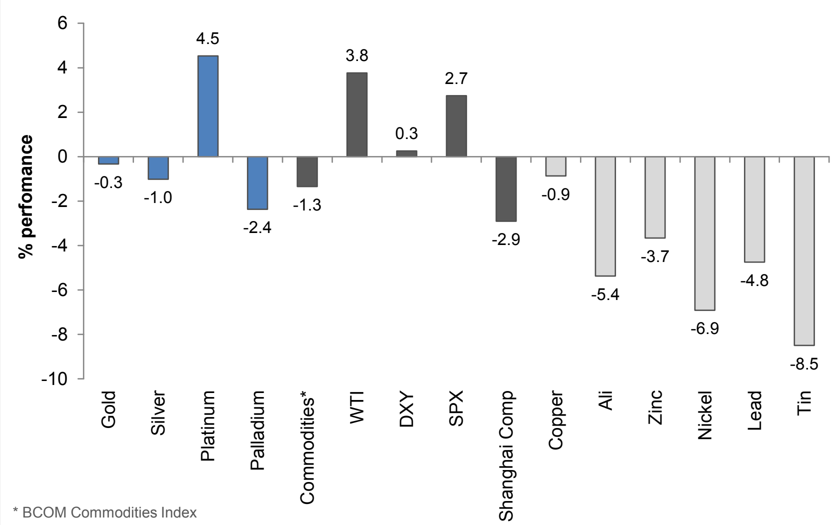
GOLD finished April almost unchanged, unable to fully escape $1300 in either direction, which is a fair performance given the moderately stronger $, the lack of persistent macro fear and buoyant US equities prices. Despite the unwind of both speculative (COT) and ETF investor interest (a total of 6.3m oz exited), the fall in real rates during April promoted CB and OTC buying; we continue to believe that it wont take just 1 attempt to break the cyclical range earmarked by $1350 as Gold remains a 2nd-tier investment while it awaits for a $-negative or vol-positive catalyst to evolve.

SILVER: The Gold/Silver ratio remains very elevated near the top end of a long-term range due to fact that Silver is no longer poor mans gold (with nominal Gold prices well below $1500) while it also fails to attract the steady Central Bank inflows seen in Gold. Overall, the longer Silver remains near its cyclical floor around $15, AND the longer price volatility is contained, the better chance it has of attracting and inducing new technologies and end-use demand. We continue to believe the Gold/Silver ratio will remain lofty at 82-86; tactical opportunities exist with small curve tightening (which could inject a some CTA short covering) but large breakouts are limited, when Gold is <$1350, as the investment case for Silver is absent, for now

PLATINUM was able to break through the $880 technical inflection point in early April, but any price extension wasn't possible as it contended with a Gold reversal (at $1310), the unwind of supply-side fear length (AMCu, Eskom), and further headwinds from weak European data. Platinum should post a (smaller) surplus next year, which *could* swing into deficit if European growth (and thus diesel/auto sales) rebound and investor interest remains persistently strong.

PALLADIUM prices whipped around $1400, tormenting anyone looking for a sustained trend outside of its $1300-1450 comfort zone. With Palladium prices (and forwards) probing the bottom of its YTD range, there are destocking changes occurring that will put to test just how *much tighter* global environmental standards are in the face of structurally weaker global auto sales (global vehicle sales fell by 4.7% y/y in March for a 7th consecutive month of YoY declines)

Metals performances vs the rest, April 2019



* BCOM Commodities Index

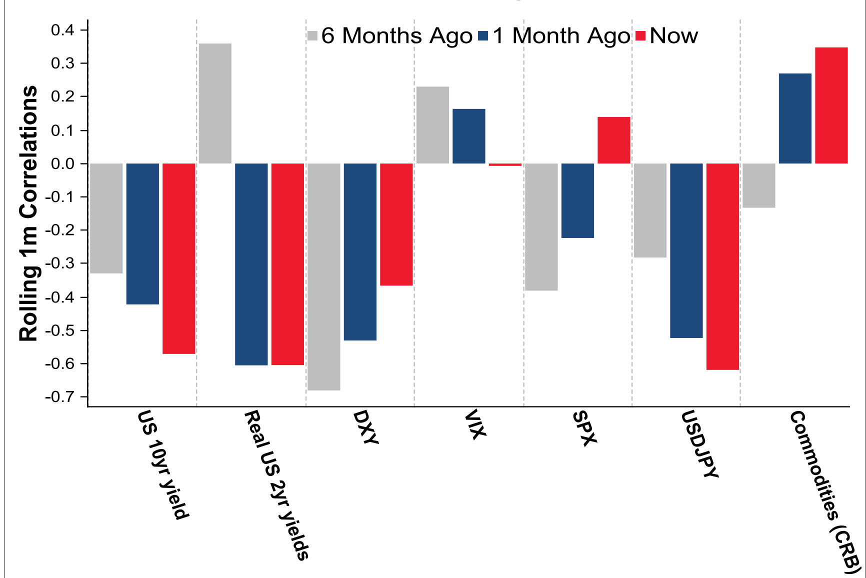
Source: Scotiabank Commodities Strategy

GOLD finished April almost unchanged unable to fully escape $1300 in either direction, which is a fair performance given the moderately stronger $, the lack of persistent macro fear and buoyant US equities prices. Despite the unwind of both speculative (COT) and ETF investor interest (a total of 6.3m oz exited), the fall in real rates during April promoted CB and OTC buying; we continue to believe that it wont take just 1 attempt to break the cyclical range earmarked by $1350 as Gold remains a 2nd-tier investment while it awaits for a $-negative or vol-positive catalyst to evolve. Our original overarching 2019 investment theme - long volatility, short politics and short the $ (which is best expressed by being long Gold) - drastically changed the past 2months. Gold should do well in a low (and falling) real rate environment—together with the JPY, real rates are its preferred driver (box 1) - but unless theres some macro fear and complacency is shattered, its tough to see Gold really outperform (i.e.: >$50 repricing) on a tactical basis.

The confirmed 'Fed pause' which prompted expectations that the Fed cuts rates this year given tame inflation (at the end of April rate cut expectations were 64%) was somewhat offset by the DXY technically trading rather bid into key resistance area at 97/98. Structural bearish-$ arguments (MMT, political polarization, deficits, a Fed pause etc) have not yet had an impact on the $, and overall any technical breakouts are false starts (graph 1). That creates the core backdrop for range bound commodity prices which mirrors the stalemate macro environment markets are in for now (policymakers—led by the Fed—are on hold, China easing has become much less responsive/accommodative, Brexit and trade deal deadlines were extended, May/summer is coming…)

The notable flows in April were ETF outflows. These erased all the 'gains' in Q1 and resulted in net 2019 outflows, as recession fears withdrew and the $ threatened a key technical break. This stood in contrast to the plethora of reports around strong Central Bank inflows (CBs bought ~146t of Gold in Q1, the highest Q1 purchase since 2013). The pace of April ETF outflows more than offsets the 2019 monthly pace of all CB inflows in Q1. And while CB buying from EM CB and the usual candidates (China, Russia, India etc) is supportive for Gold, it's a well-known fact and almost baked into $1250-1300 prices. Only CB purchases from new regions and/or a significant ramp up in the pace of usual suspect purchases, is mildly bullish Gold. Total Global ETFs stand at 70m oz, with UK ETF holdings at all-time highs (due to Brexit concerns), Chinese & European funds holdings falling (slowly), but US outflows accelerating. If US equities sustainably break into new highs theres a structural threat of further (US) ETF redemptions which will make $1350 an even tougher nut to crack. Overall, while the combination of Indian, Chinese and CB demand provides a well-respected floor around $1270-1280 for now, the investment environment needs a jolt before Gold can wake up from its sleepy range; that's certainly not unheard of — Gold tends to perform when no one is looking…

Macro assets driving Gold...



* Real 2 year yields = 2 Treasury yields- 2yr Breakevens

Source: Macrobond, Scotiabank Commodities Strategy

DXY Bull flag - cant break decidedly outside of flag
… complacency indicator

Source: Scotiabank Commodities Strategy

DXY Curncy (DOLLAR INDEX SPOT) DXY bull flag Daily 11MAR2017-07MAY2019 Copyright© 2019 Bloomberg Finance L.P. 07-May-2019 11:23:00

Silver:

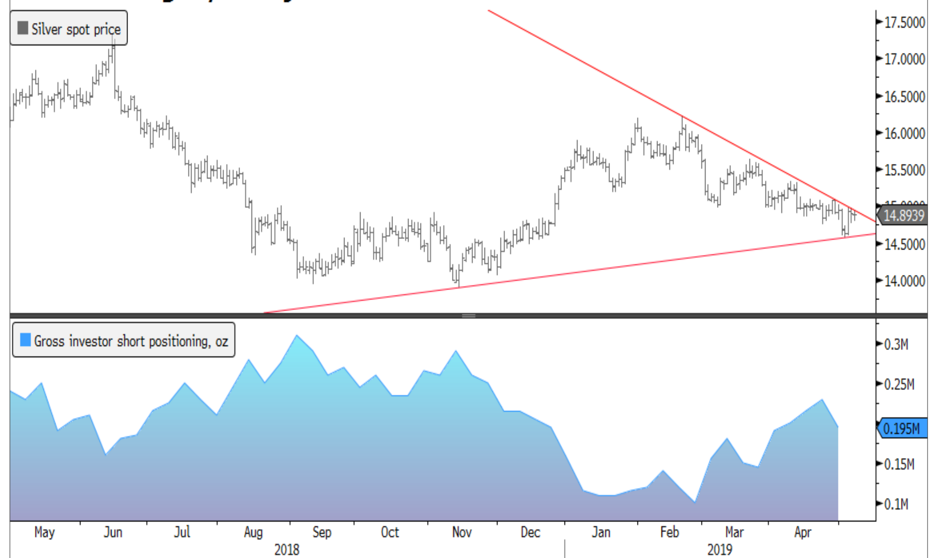
Silver posted another monthly loss in April (of 1%), as it struggled to find the typical investor buying given persistently saturated supplies solidifying a firm technical ceiling (that has now shifted down to $15.30 from $16.20).

Visible exchange inventories (COMEX & SHFE) broadly stabilized around record highs in April. However since the accumulation has halted which is somewhat loosely connected with Silver forward rates tightening up incrementally, its a small constructive step signaling that industrial end-users are restocking. ETF inflows remained broadly stable above 500m oz, but COT shorts ramped up positioning in April, taking gross shorts to almost 200m oz, and providing a sliver of hope for a quick tactical repricing higher on any convincing technical break (graph 1).

With Silver supply due to expand in 2019 (primarily due to higher productions from Gold/Silver mines in Americas and lead/zinc operations in Oceania) and the lack of new industrial uses/technologies and fresh investment inflows, its tough to foresee a sustainably higher Silver price in the upper teens. TCs (treatment charges for concentrate base metals), especially for zinc, have increased considerably this year, underlying the raw material availability (including Silver).

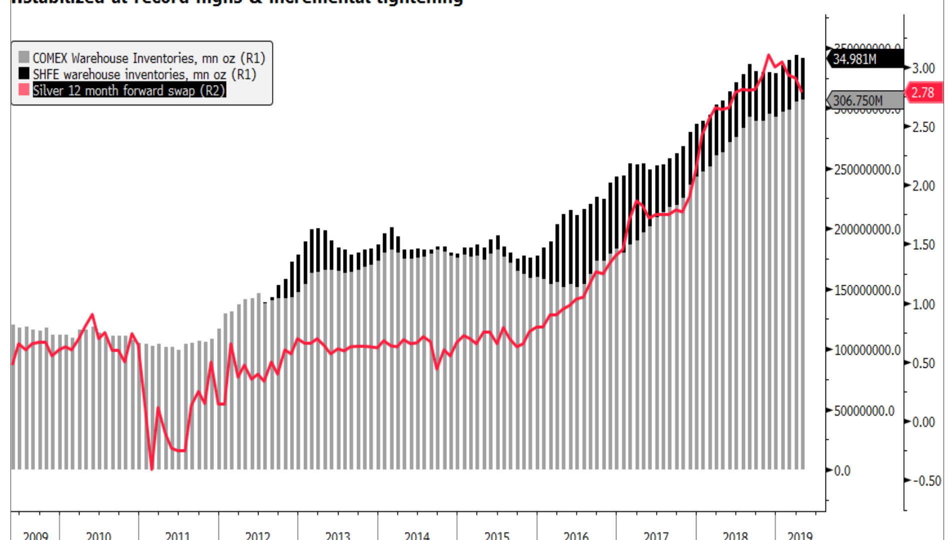
The Gold/Silver ratio remains very elevated near the top end of a long-term range due to fact that Silver is no longer poor mans gold (with nominal Gold prices well below $1500) while it also fails to attract the steady Central Bank inflows seen in Gold. Overall, the longer Silver remains near its cyclical floor around $15, AND the longer price volatility is contained, the better chance it has of attracting and inducing new technologies and end-use demand. We continue to believe the Gold/Silver ratio will remain lofty at 82-86; tactical opportunities exist with small curve tightening (which could inject a some CTA short covering) but large breakouts are limited, when Gold is <$1350 as the investment case for Silver is sidelined, for now.

Silver...wedged, heavy but short



Source: Bloomberg, Scotiabank Commodities Strategy
SILV Comdty (SILVER SPOT $/OZ) silv tech Daily 01MAY2018-07MAY2019 Copyright© 2019 Bloomberg Finance L.P. 07-May-2019 11:38:36

Exchange Silver inventories vs 12mo forwards
..stabilized at record highs & incremental tightening



Source: Scotiabank Commodities Strategy, Bloomberg
COMXSILV Index (Comex Silver Inventory Data) comex shfe silv stocks2 Monthly 09 Copyright© 2019 Bloomberg Finance L.P. 07-May-2019 14:14:30

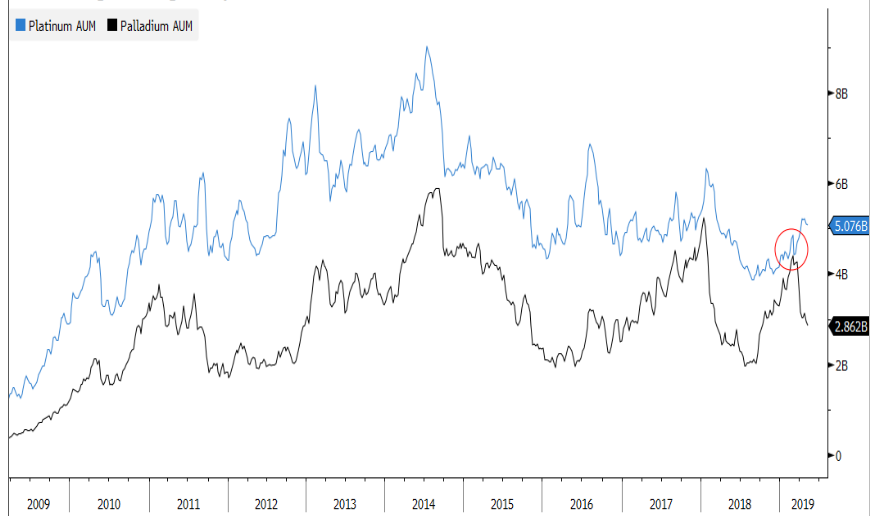
PGMs

Platinum was the precious outperformer in April, posting 4.5% gains vs Palladiums 2.3% fall (extending the large ~11% loss seen in March).

Platinum was able to break through the $880 technical inflection point in early April, but any price extension wasn't possible as it contended with a Gold reversal (at $1310), the unwind of supply-side fear length (AMCu, Eskom), and further head-winds from weak European data (European car sales in March fell by 3.9%, a 7th monthly fall that is likely to extend given continuing Brexit uncertainty). There is, however, further compression in the Platinum-Palladium spread (Platinum has shifted from a $600 discount vs Palladium, to $450, in the past month) and the longer this trend continues, the more it will bolster and support the theory that substitution is occurring, albeit incrementally. While its large key sectors (auto & jewelry) remain weak spots for platinum, the introduction of Euro 6d emissions legislation and RDE testing conditions (2020) could ensure OEMs hedge out increased platinum loadings, while other smaller industries (electronics & chemical) are also growing. Versus Gold, Platinum prices seem to have somewhat stabilized around a $400 discount, signaling that the marginal investor (ETF or COT) has not fully committed. In fact, in April, Platinum ETF holders actually liquidated 45K oz (minor vs the massive inflows seen in Q1'19). Overall, platinum should post a (smaller) surplus next year, which could swing into deficit if European growth (and thus diesel/auto sales) rebound *and* investor interest remains persistently strong.

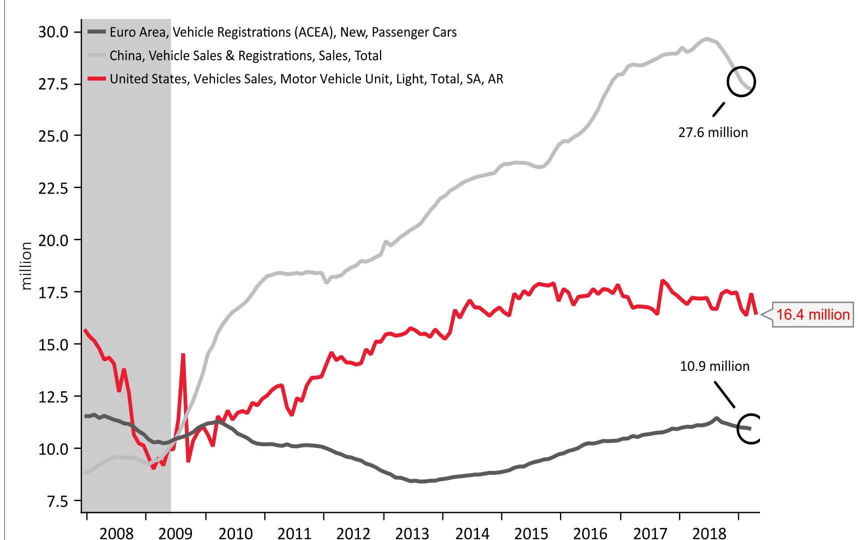
Palladium prices whipped around $1400, tormenting anyone looking for a sustained trend outside of its $1300-1450 comfort zone. With the persistent decline in lease rates (as borrowing demand trends change) and several Asian holidays in April, liquidity and traditional rationale has been further complicated; further declines in ETF holdings (-66K oz in 1month) is now being cited as a key source *fuelling* increased metal availability (not driving the tightens as was the case 3 months ago). Nonetheless, the structural deficit this year should be somewhat alleviated by additional metal from SA where WIP material was accumulated in 2018 and scrap supply; any further power cuts from Eskom will impact the timing of this built up inventory creating the much feared short-term bottlenecks. Overall, with Palladium prices (and forwards) probing the bottom of its YTD range, there are destocking changes occurring that will put to test just how *much tighter* global environmental standards are in the face of structurally weaker global auto sales (global vehicle sales fell by 4.7% y/y in March for a 7th consecutive month of YoY declines)

AUM in Palladium just cant quite overtake Platinum
*ETFs and gross long COT positions



Source: Scotiabank Commodities Strategy, Bloomberg

Light Vehicle Sales, seasonally adjusted in the US, China, Europe



Source: Macrobond, Scotiabank Commodities Strategy