

Commodity Spotlight Precious Metals

20 April 2012

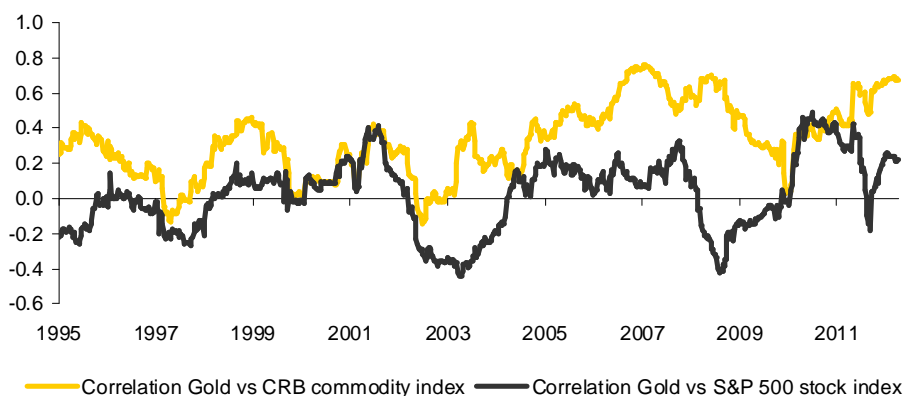
Prices squeezed in short term, increasing in long term

Gold is currently behaving more like a risky asset class and less like a safe haven, partly due to the increasing number of speculators. However, the price is likely to regain its former peaks by the end of 2012 as a result of its return to a store of value, low interest rates and the appetite for gold in China. Silver, platinum and palladium are currently under pressure due to their industrial characteristics, but should also increase again over the course of the year.

So far this year gold has behaved more like a risky asset class and less like a safe haven. This is based on the high correlation of gold with commodities and equities. The rolling 52-week correlation of weekly changes from gold with commodities, measured by the CRB Commodity Index, is currently at a high level of 0.67. And the correlation of 0.22 with the S&P 500 stock index - although low in absolute terms - can be described as historically high (chart 1). The correlation has become much stronger since the massive price decline of last September. We attribute this to the increasing number of speculators in the gold market. Even though it had resumed its safe haven status again for a short time recently, gold is likely to continue to be affected by macro factors and the atypical pattern of behaviour will probably persist in the short term. It is not therefore surprising either that gold has not benefited recently from the resurgence of the sovereign debt crisis in the eurozone - risk premiums for Spanish and Italian government bonds have risen sharply.

Since the fluctuations in the gold price since the beginning of the year have not been accompanied by significant changes in ETF holdings, speculative financial investors are likely to be mainly responsible. This is evident from the CFTC statistics on the market positioning of those speculative financial investors. In the first two months of the year they had increased their net long positions by two thirds to just over 177 thousand contracts - the highest level since the beginning of September 2011 -, only to reduce them by 41% again in the following six weeks (chart 2, page 2). The price reacted accordingly: while in the first period evaluated there was an increase of 12%, in the second period there was a decline of 7%. Obviously there are still too many "shaky hands" on the market that need to be "flushed out". Only when the market has settled down is the gold price likely to resume its long-term upward trend.

CHART 1: Currently high correlation between gold and commodities and equities



Source: Bloomberg, Commerzbank Corporates & Markets

Commerzbank Forecasts 2012

	Q2	Q3	Q4
Precious metals			
Gold	1650	1750	1900
Silver	32	35	38
Platinum	1600	1700	1850
Palladium	675	750	850

USD per troy ounce

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Bloomberg: CBIR

Weak demand for gold in India due to strike...

On the fundamental side two main aspects have prompted investors to act. On the one hand, news from India raised fears that the increase in import duties on gold might lead to a sharp decline in physical demand in what was until recently the country with the highest gold consumption in the world. For the announcement by the Indian finance minister of the tax increase triggered a three-week nationwide strike by gold jewellers in the country. According to the All India Gems & Jewellery Trade Federation, around 90% of the 300,000 jewellers in the country took part in the strike. The Bombay Bullion Association (BBA) therefore expects gold imports of only 125-150 tons in the first quarter. It also expects a figure of only 150 tons in the second quarter, compared to 250 tons in the previous year. And in full-year 2012 imports are likely to reach 700-800 tons. This would be 17-28% less than last year. The gold price could therefore lose what has so far been an important supporting factor for a short time.

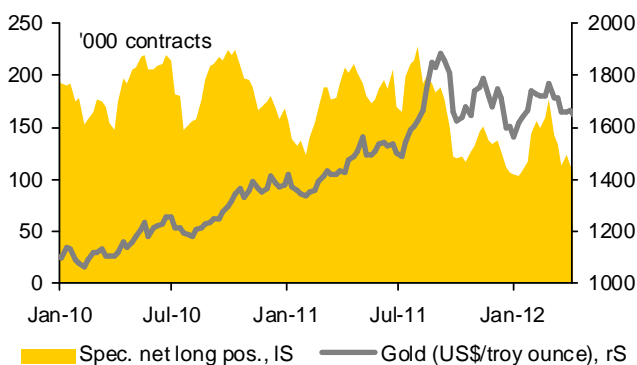
...offset by "appetite for gold" in China

On the other hand, the "appetite for gold" in China still does not seem to be satisfied. The Census and Statistics Department in Hong Kong thus reported gold exports of 39.7 tons to China in February. This was 20% more than in January. Last year gold exports from Hong Kong to China had already increased by 260% year-on-year to 428 tons. If the pace of the first two months of the year continues, exports will be even higher in 2012. Since China itself does not publish such data, the information provided by the Hong Kong authority gives a good indication of Chinese demand for gold. Hong Kong is also still regarded as the gateway to China, which makes the data even more important. High Chinese demand for gold could also balance out the lower demand in India and could also be an indication that demand from India is being transferred to other Asian countries. According to an estimate from the World Gold Council, China is likely to overtake India this year as the biggest gold consumer in the world. Given the growing middle class and increasing wealth as well as the gradual opening up of the gold market to private investors, demand for gold in China has grown very dynamically in recent months. The Chinese central bank is also likely to steadily increase its gold reserves. Despite the expansion of domestic gold production last year to a record level of 361 tons (chart 3), China is reliant on imports and thus even takes supply out of the world market.

Upward trend expected to resume in medium to long term

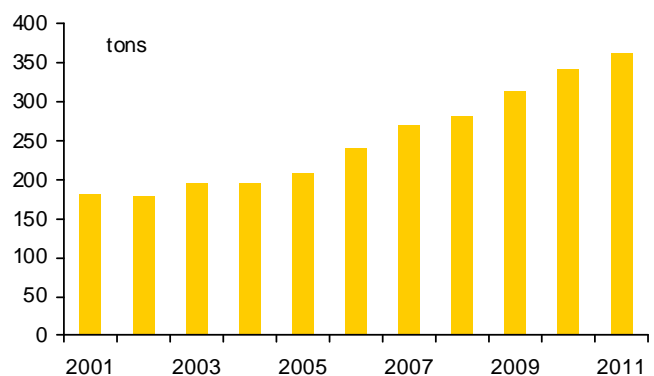
In the short term, gold could come under further pressure as a result of the high correlation with the risky asset classes and the heightened risk aversion of investors. The fact that a further quantitative easing of monetary policy in the US is now regarded as less likely also remains a negative factor. We would not therefore rule out a temporary price decline to below the level of USD 1,600 per troy ounce. However, its safe haven status should prevail in the medium to long term and gold should resume its upward trend. The sovereign debt crisis in the eurozone is therefore far from solved and is continuing to smoulder. Concerns about inflation and the high level of interest from the central banks could help gold to move back towards its all-time peak of USD 1,900 per troy ounce by year-end.

CHART 2: Gold recently influenced by financial investors



Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 3: Gold production in China expanding further



Source: WBMS, Commerzbank Corporates & Markets

Silver:

Financial investors driving silver price

Silver has also remained on a roller coaster ride so far this year. After a price increase of almost 25% in the first two months of the year, it has fallen again by just over 8% since the end of February. As with gold, this has probably been mainly caused by speculative financial investors. In the same periods they initially increased their net long positions sixfold to almost 30,000 contracts, and subsequently reduced them again by more than a half within four weeks. In contrast, in a press release, the Silver Institute attributed the increase in the silver price mainly to investment demand. This includes ETF investors and demand for coins.

In contrast, ETF investors holding back

However, in the first quarter, ETF investors - who are regarded as having a longer-term investment horizon - adopted a fairly reserved stance with regard to silver in contrast to platinum and palladium, consequently failing to provide any real support for the silver price. The silver ETFs tracked by Bloomberg reported inflows of only 2.7% or 459 tons in the first three months of the year. At a total of 17,753 tons as of the end of March, holdings of silver ETFs were however at their highest level since the beginning of May 2011 (chart 4).

After a strong start to the year, the pace of demand for coins is slowing

Demand for silver coins, which had already absorbed a proportion of the sales by speculative financial investors and ETF investors last year, gained significant momentum again at the beginning of the year. The U.S. Mint alone sold 6.11 million troy ounces (or around 190 tons) of silver coins in January. This represented the second highest level ever achieved. However, the pace slackened visibly in the two subsequent months, and US coin sales were therefore down by almost 20% on the previous year's level in the first quarter of 2012 at 10.1 million troy ounces (around 315 tons).

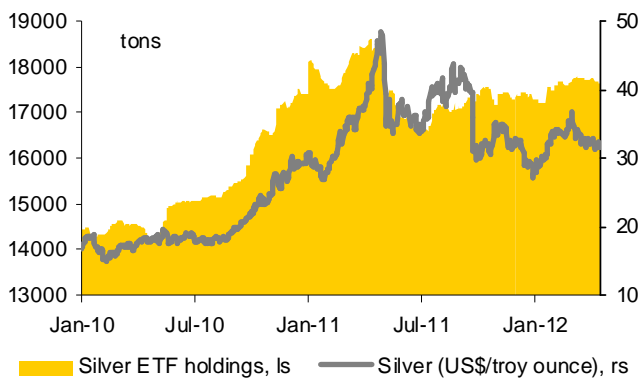
Silver demand declined in 2011 for the first time in three years

As the Silver Institute reported jointly with GFMS in the recent "World Silver Survey", demand for silver fell last year by 3.2% on the year to 1.04 billion ounces owing to the sovereign debt crisis in the euro zone. This was the first decline in three years. Whilst demand from industry dropped by 2.5% to 486.5 million ounces, demand for bullion as well as for coins and medals reached new record highs. Similar to gold, silver was apparently regarded at least as something of a safe haven last year, the high volatility notwithstanding. Demand in the segments of jewellery, photography and silverware declined, however (chart 5).

Price rise expected in second half

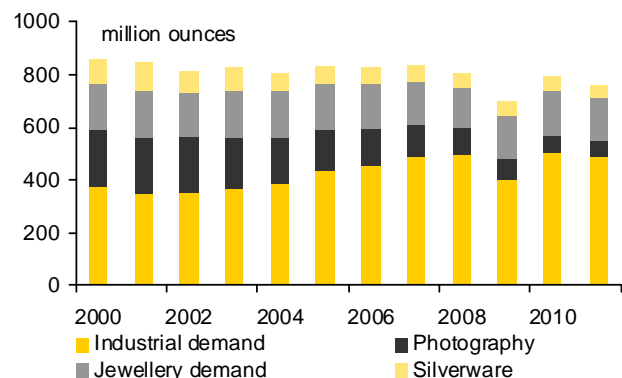
We still expect the price of silver to increase this year. The recent slip in the price to below the level of USD 32 per troy ounce in particular is likely to attract bargain-hunters. The capital preservation character of silver could also move more centre-stage again, since the sovereign debt crisis in the eurozone has only eased superficially and is continuing to smoulder. Silver should also be supported by the currently high gold/silver ratio of 52, since silver is relatively cheap compared to gold. In general, thanks to its hybrid character – capital preservation and participation in an economic upturn due to its mainly industrial uses - silver should remain attractive and in demand. We therefore expect the price to increase to USD 38 per troy ounce by year-end. However, like gold, the lion's share of the price increase should be in the second half.

CHART 4: Influence of the silver ETFs has decreased



Source: Bloomberg, Commerzbank Corporates & Markets

CHART 5: Sovereign debt crisis affects demand for silver



Source: Silver Institute, Bloomberg, Commerzbank Corporates & Markets

Platinum:

Platinum much cheaper than gold at times

The price of platinum has increased by 17% or about USD 240 since the beginning of the year despite the recent price decline, and was trading at around USD 1,640 per troy ounce at the end of the last quarter. At the end of February, a 5-month peak of USD 1,737 per troy ounce was even reached for a short time as a result of the euphoria in the equity and commodity markets, but also due to a strike in South Africa (see below). This was also attributable to the relative attractiveness of platinum compared to gold. Since trading in platinum started on stock exchanges in 1987, platinum has almost always been more expensive than gold, but since September 2011 it has been continuously cheaper. At its peak, the price differential between these two precious metals even exceeded USD 216 in favour of gold. This attracted bargain-hunters banking on a convergence of the price difference. Gold has also been increasingly replaced by platinum in the jewellery industry. Consequently, platinum has recovered strongly against gold and was intermittently even more expensive than gold again in mid-March.

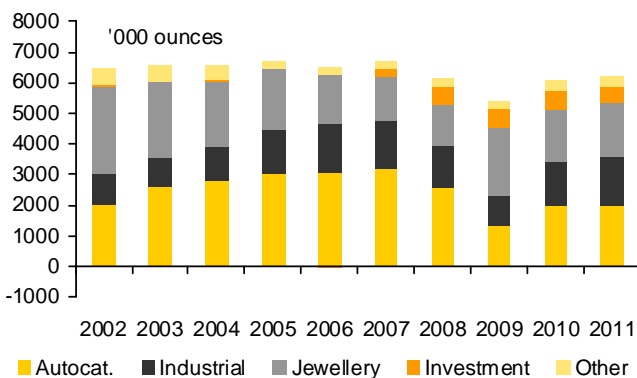
High demand from the jewellery industry

The fact that platinum has recently been used increasingly in the jewellery industry does not seem to be a temporary phenomenon. In recent years - excluding 2009 - the proportion of jewellery demand to total demand has increased on a net basis. Whereas, according to figures from Johnson Matthey, almost 22% of demand for platinum came from the jewellery industry in 2007, in 2011 the figure was almost 29% (chart 6). After the automobile industry, the jewellery sector is thus the second most important demand component for platinum. This trend has been mainly driven by China. Last year the country accounted for more than two thirds of global jewellery demand with 1.69 million troy ounces. Given the increasing wealth of the Chinese population, the signs are that this trend will continue in future years. In addition to China, demand for platinum also seems to be increasing in India. Platinum is becoming increasingly popular, particularly with young women. However, in absolute terms, India played an insignificant role in the global market last year with total demand of 93.2 thousand ounces.

Vehicle sales subject to very wide regional variations

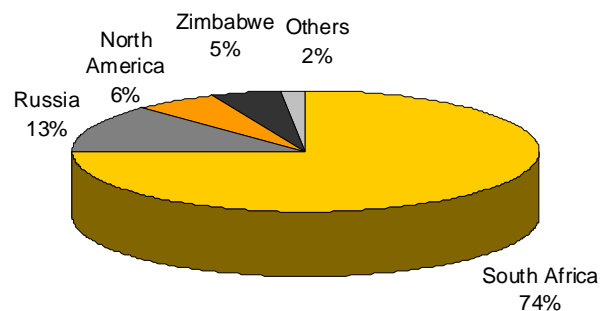
The automobile industry - where platinum and palladium are used to produce autocatalysts - is, in turn, currently experiencing difficult conditions, with regional variations. After a weak start to this year, automobile associations expect at best a stagnating market in the EU. According to figures from the European Automobile Manufacturers' Association (ACEA), new vehicle registrations declined by 8.3% in the first two months of the year compared to last year. However, the comparison is distorted somewhat, since in France for example, car sales were supported in the previous year by a scrappage premium. Nevertheless, car sales throughout the EU declined by 1.7% last year to 13.11 million units. The German Association of the Automotive Industry (VDA) takes a slightly more pessimistic view of the West European market in 2012 and expects car sales to decline by 5% to 12.1 million units. However, this should be offset by stronger than expected growth in the US - +8% to 13.7 million units. The Chinese car market is also set to grow by 8% in 2012, and a growth rate of 10% is expected in India. The Japanese car market is recovering very rapidly from the natural disasters of last year. All in all, the VDA expects moderate growth of 4% in car sales to 68 million units on a global basis. The growth rate last year was still 6%.

CHART 6: Jewellery industry becoming more important again



Source: Johnson Matthey, Commerzbank Corporates & Markets

CHART 7: Platinum market heavily dependent on South Africa



Source: Johnson Matthey, Commerzbank Corporates & Markets

Investors focusing more strongly on platinum again

After the large-scale sales of platinum by both short-term and long-term oriented financial investors last year, the trend has reversed again since the beginning of this year, providing additional support for the price. Net long positions therefore expanded by 44% to 16.3 thousand contracts in the first three months of the year. And the platinum ETFs tracked by Bloomberg also showed inflows of more than 107 thousand ounces in the first quarter. Last year investment demand accounted for 8% of total demand. Here too, the price attractiveness compared to gold is likely to have played a role.

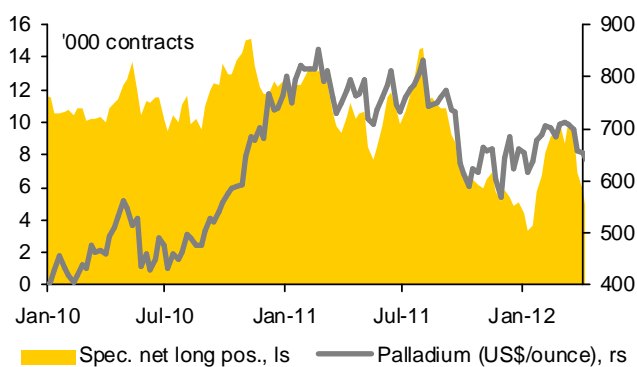
Supply reduced by protracted strike in South Africa

On the supply side, the focus shifted back to latent risks again in the last quarter: for in South Africa, which with a market share of 75% is by far the biggest platinum producer in the world (chart 7, page 4), there was another lengthy strike. Workers in the largest platinum mine in the world, Rustenburg, went on strike for several weeks. The mine operator Impala Platinum, which is one of the largest in the country, consequently "lost" around 100 thousand ounces of production. After a court declared the strike to be illegal and Impala Platinum subsequently dismissed 17,200 workers, violent riots took place involving deaths and injuries. Production only resumed at the beginning of March after a six-week shutdown. However, this did not mean that the conflict has finally been resolved. The mine operator is still negotiating with the unions on workers' wages and the strike could therefore be resumed at any time. The strike has also once again demonstrated the power of the unions in South Africa. However, there is obviously not always agreement between the various unions. Smaller upcoming unions are therefore attempting to attract members away from the largest union in the country, the National Union of Mineworkers, and to implement their own ideas - a dangerous development which could increase the danger of more strikes in future.

Expected supply deficit should support platinum price

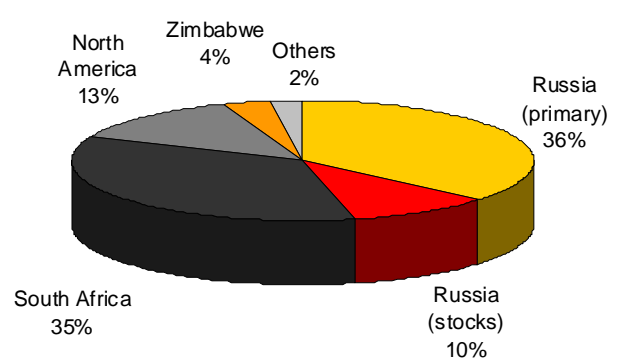
Since it is doubtful to what extent the "lost" production can be made up over the course of the year, and further strikes cannot be ruled out, in our view the global platinum market could already show a supply deficit again this year. In its last interim report in November, Johnson Matthey was still anticipating a moderate surplus. However, its next report, which will be published in May, is likely to include revisions as a result of the strike-related production losses and robust demand. We still expect prices to rise over the course of the year and platinum to reach around USD 1,850 per troy ounce by year-end.

CHART 8: Financial investors exerting pressure on palladium



Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 9: Sales of Russian reserves so far a major element in palladium supply



Source: Johnson Matthey, Commerzbank Corporates & Markets

Palladium:

Although the trend in palladium has been broadly in line with that of platinum, it has come under greater pressure in recent weeks and, in terms of the price trend, has lagged well behind the other three precious metals which are traded on stock exchanges. Below the line there was a decline of 0.1% in the first quarter to USD 654 per troy ounce.

Palladium influenced by financial investors

The reversal of the trend in the behaviour of financial investors in relation to palladium was even more marked than for platinum. From the beginning of the year to mid-March net long positions virtually doubled to 10 thousand contracts. However, bets on rising prices have been reduced significantly since then, exerting major pressure on the price (chart 8, page 5). The palladium ETFs tracked by Bloomberg have shown inflows of 243 thousand ounces. This has thus already partly offset the extremely weak investment demand, particularly in the second half of 2011. In 2010, the proportion of investment demand to total demand amounted to 14% on a net basis and thus more than platinum (11%). In 2011 the proportion was even negative, i.e. financial investors have sold more platinum than they have bought, thus helping to expand the supply.

Palladium more heavily dependent on the auto industry than platinum

In terms of demand from the automobile industry, palladium is essentially subject to the same risks and opportunities as platinum. The difference is that palladium is mainly used in the production of autocatalysts for petrol engines, while platinum is mainly used in autocatalysts for diesel engines. Palladium is also more heavily dependent on the automobile industry than platinum, since it accounts for a significantly higher proportion (66%) of total demand on a net basis (i.e. taking account of recycling) than platinum (32%). One benefit of palladium is the absolute price advantage, so that producers of autocatalysts for cars replace platinum with palladium whenever possible. From a technical perspective this can be achieved in up to 25% of cases.

Concerns about sale of Russian reserves

On the supply side, palladium is not as heavily dependent on South Africa - which is the second largest producer in the world with a market share of 35% - but consequently all the more dependent on Russia. Russia was the biggest supplier of palladium last year with 3.45 million ounces (46% share). In addition to mining production, the sale of Russian state reserves of 750 thousand ounces played a major role here (chart 9, page 5). And this is the factor which raises the largest number of question marks and concerns. It is generally accepted that the volume of reserves sold will be significantly lower this year, the question is only, how much lower? In February the Russian news agency RIA Novosti quoted an employee of the Finance Ministry as stating that Russia will not sell any more significant volumes of its state-owned palladium reserves. This would remove an important source of supply from the market.

Palladium prices expected to increase

The supply deficit already expected by Johnson Matthey this year in the global palladium market is likely to be significantly higher again without the sale of the Russian state reserves. Last year the market would already have been only in balance without the sale of the reserves. We therefore expect prices to increase over the year and palladium to reach around USD 850 per troy ounce by year-end.

At a glance

TABLE 1: Our forecasts

	Quarterly average								Yearly average			
	19/04/12	Q1 12	Q2 12	Q3 12	Q4 12	Q1 13	Q2 13	Q3 13	Q4 13	2011	2012	2013
Gold	1643	1691	1650	1750	1900	1950	1900	1950	2000	1575	1750	1950
Silver	31.8	32.7	32.0	35.0	38.0	42.0	42.0	45.0	50.0	35.5	34.5	45.0
Platinum	1580	1612	1600	1700	1850	1950	1900	2000	2100	1725	1700	2000
Palladium	665	684	675	750	850	900	875	950	1000	730	740	930

Quarterly average, based on spot prices Source: Commerzbank Corporates & Markets, Bloomberg

TABLE 2: ETF holdings (weekly data)

	Date	Holdings	Total Net change			% change.		Comments
			1 week	1 month	1 year	1 year		
Gold ETFs (in '000 ounces)	13.04.12	77050.3	-33.6	-438.3	7547.4	10.9	Gold relatively stable, outflows from silver and platinum, inflows in palladium	
Silver ETFs (in '000 ounces)	13.04.12	566874.7	-1619.8	-4186.9	-25797.4	-4.4		
Platinum ETFs (in '000 ounces)	13.04.12	1385.9	-6.3	-7.2	12.4	0.9		
Palladium ETFs (in '000 ounces)	13.04.12	1908.5	4.4	29.2	-322.9	-14.5		

Source: Bloomberg, Commerzbank Corporates & Markets

TABLE 3: COMEX inventories (weekly data)

	Date	Holdings	Total Net change			% change.	
			1 week	1 month	1 year	1 year	
Gold (in '000 ounces)	13.04.12	10993	-323.5	-418	-3	0.0	
Silver (in '000 ounces)	13.04.12	141594	2075	9364	39076	38.1	
Platinum (in '000 ounces)	13.04.12	198	-0.2	21.8	73	58.2	
Palladium (in '000 ounces)	13.04.12	591	-1.4	-6.6	73	14.0	

Source: Bloomberg, Commerzbank Corporates & Markets

TABLE 4: History

Current	% change					history							
	USD per troy ounce	1 week	1 month	y-t-d	y-o-y	Q110	Q210	Q310	Q410	Q111	Q211	Q311	Q411
Gold	1643	-0.9	-0.4	5.1	9.4	1100	1200	1225	1375	1400	1500	1700	1675
Silver	31.8	0.9	-1.0	14.2	-29.7	17.0	18.5	19.0	26.5	32.0	38.5	39.0	32.0
Platinum	1580	-0.1	-4.5	12.9	-12.2	1575	1625	1550	1700	1800	1775	1775	1525
Palladium	665	3.3	-4.0	1.6	-12.4	440	495	495	680	790	760	750	630

Source: Bloomberg, Commerzbank Corporates & Markets

TABLE 5: World Official Gold Holdings (monthly data)

Country	tonnes	Country	tonnes
USA	8,133.5	Switzerland	1,040.1
Germany	3,396.3	Russia	879.2 (-3.8)
IMF	2,814.1	Japan	765.2
Italy	2,451.8	Netherlands	612.5
France	2,435.4	India	557.7
China	1,054.1	ECB	502.1

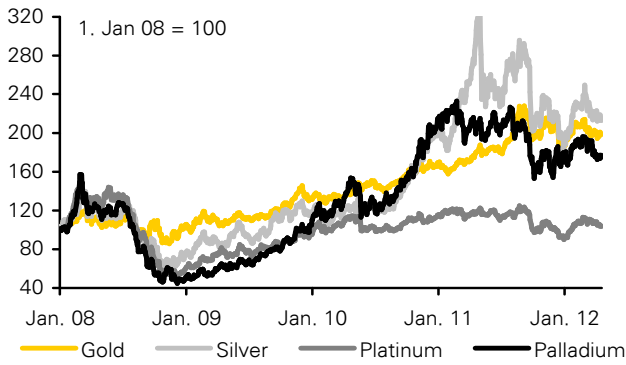
Source: World Gold Council, Commerzbank Corporates & Markets

TABLE 6: Upcoming Events

25 April	USA	FOMC meeting
1 May	USA	Vehicle sales April
3 May	EUR	ECB meeting
15 May	USA	Inflation data April
16 May	EUR	New car registrations April
16 May	EUR	Inflation data April

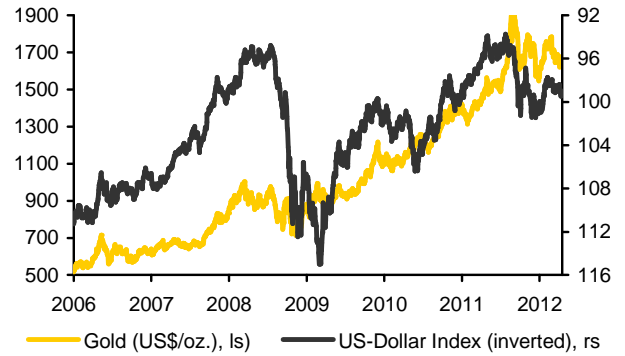
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 10: Precious metals since 2008 (01/01/08 = 100)



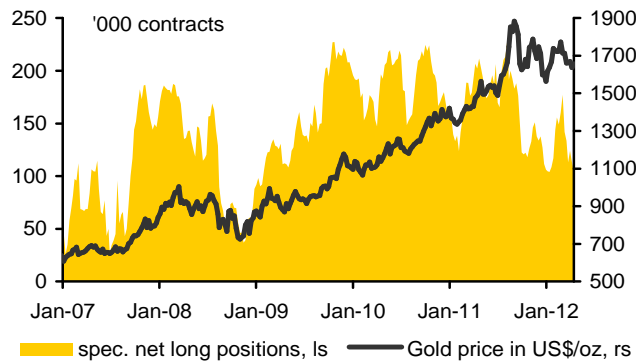
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 11: Gold versus US dollar



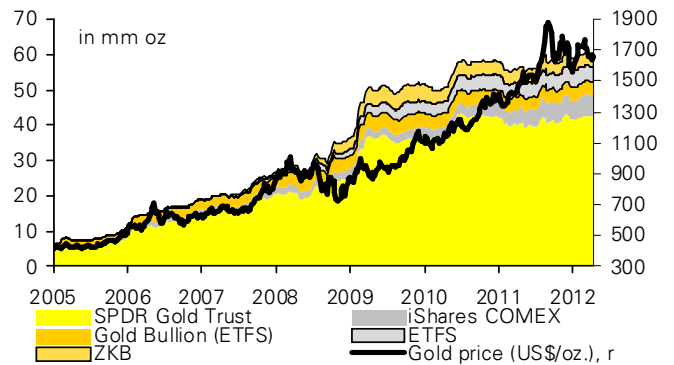
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 12: Net long positions of money managers (Gold)



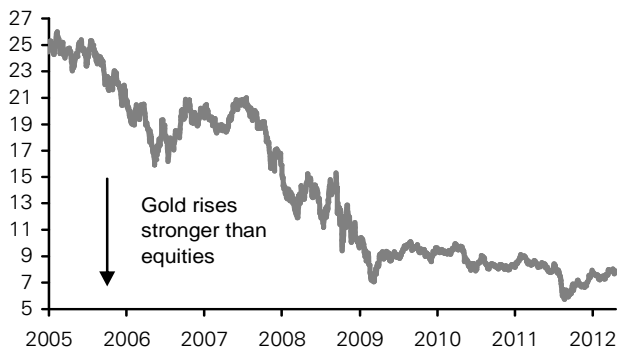
Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 13: Gold: ETF volume



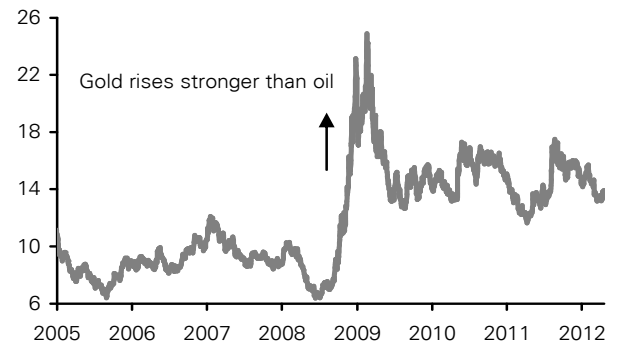
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 14: Dow/Gold ratio



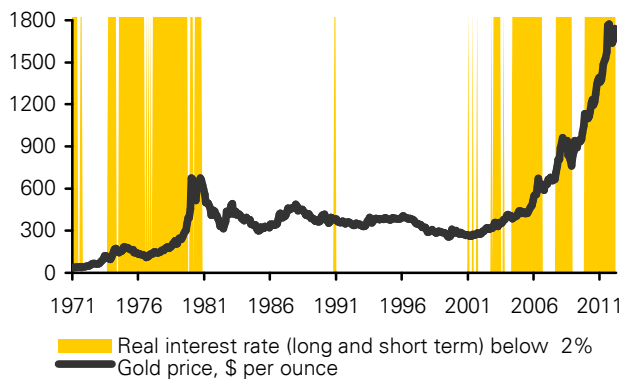
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 15: Gold/Oil ratio



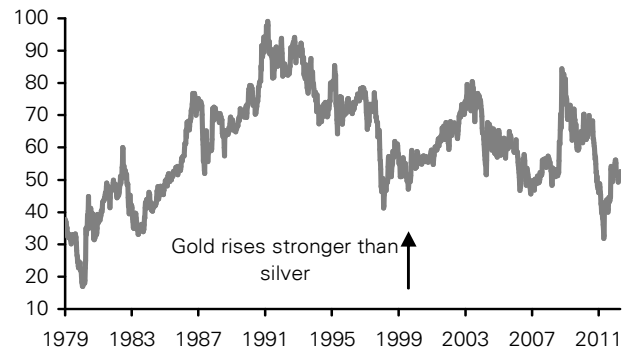
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 16: Gold price and real interest rates



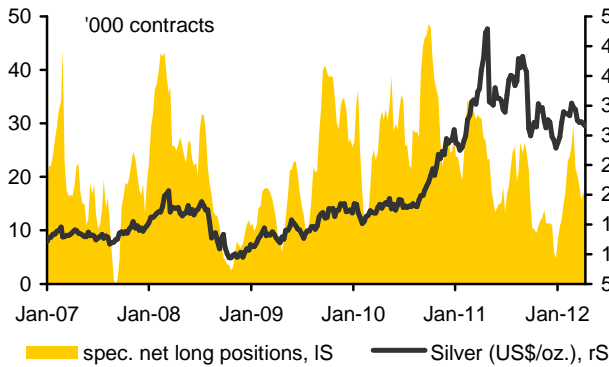
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 17: Gold/Silver ratio



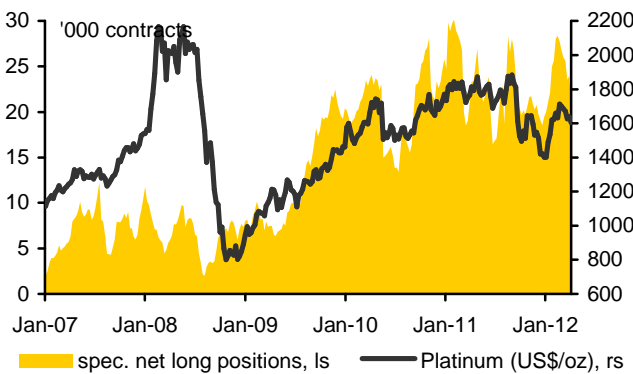
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 18: Net long positions of money managers (Silver)



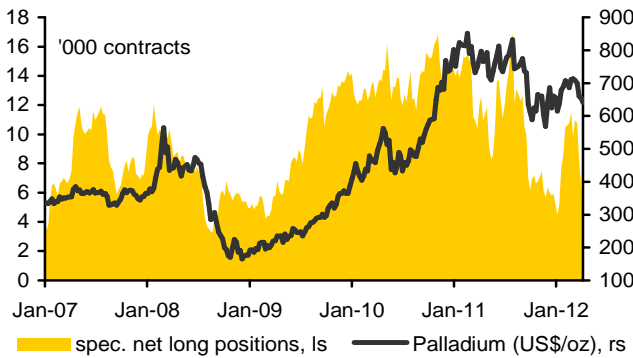
Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 20: Net long posit. of non-commercials (Platinum)



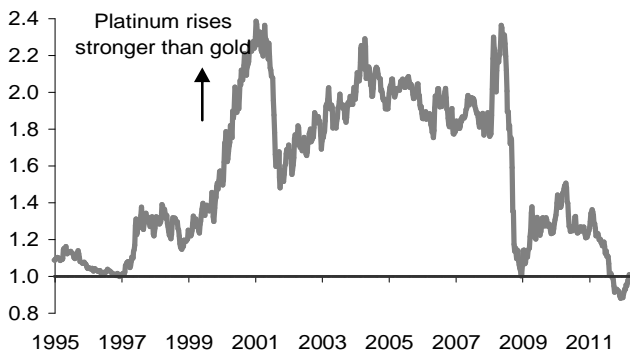
Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 22: Net long posit. of non-commercials (Palladium)



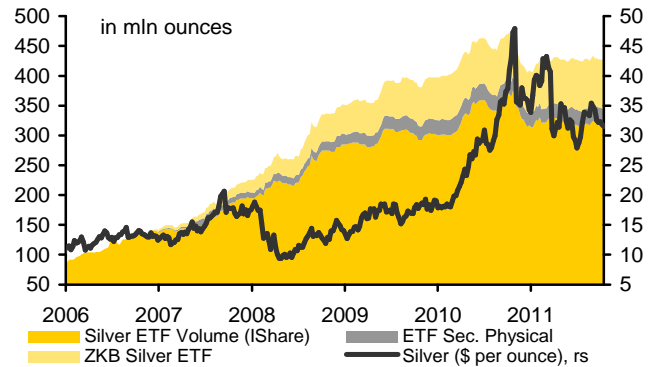
Source: CFTC, Bloomberg, Commerzbank Corporates & Markets

CHART 24: Platinum/Gold ratio



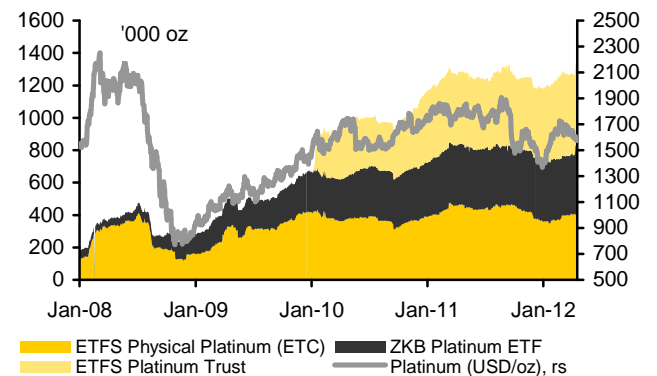
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 19: Silver: ETF volume



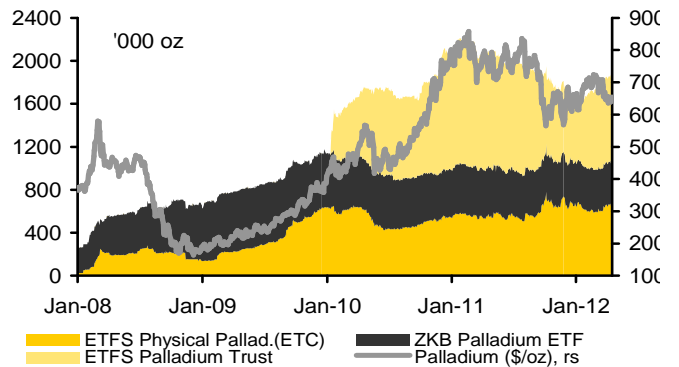
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 21: Platinum: ETF volume



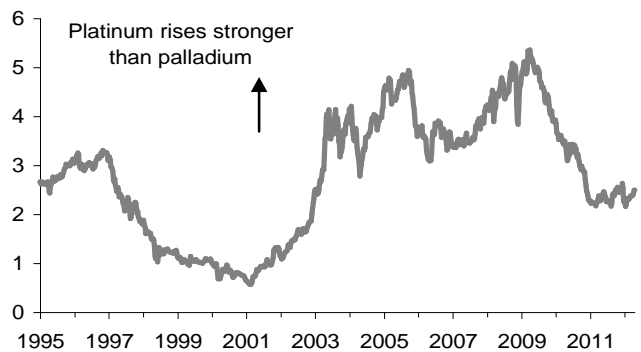
Source: Bloomberg, Commerzbank Corporates & Markets

CHART 23: Palladium: ETF Volume



Source: Bloomberg, Commerzbank Corporates & Markets

CHART 25: Platinum/Palladium ratio



Source: Bloomberg, Commerzbank Corporates & Markets

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