Precious Metals Outlook

Group Economics
Financial Markets Research

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Positive, but wait to step in

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- **Precious metal prices have rallied strongly**
- **Long term outlook for gold, silver and platinum is positive**
- **But wait for a correction to position for higher prices**
- **Palladium prices have risen exponentially**
- **We expect a correction moving prices back to a more sustainable path**

Introduction

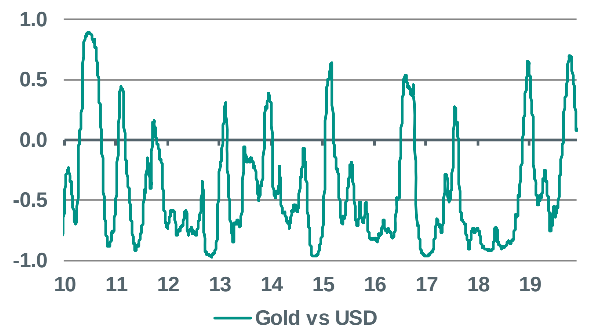
Precious metal prices have had a very strong year. Palladium had a stellar performance, rising by more than 47%. Gold and silver rose substantially above our year-end forecasts of USD 1,400 and US 18 per ounce, respectively, and platinum prices rallied to levels just below USD 1,000. Our view for palladium was completely off. Where we had expected a decline of USD 200 over the year in a volatile ride, prices rallied substantially barring three periods of sharp sell-offs in March, August and November. Gold prices were supported by a general shift in monetary policy of major central banks from tightening to a new round of easing, a decline in government bond yields, an increase in the amount of negative yielding government bonds, weakness in the Chinese yuan, uncertainty on global growth and global trade front, and Brexit uncertainty. When gold prices became somewhat expensive, silver and platinum caught up. Palladium prices have mainly rallied on supply shortages at the front end of the curve, amid higher palladium loadings in car catalysts in anticipation of more stringent emissions regulations in China and Europe. What do we expect for precious metals for 2020 and 2021?

Positive on gold, but wait for position clearing before buying

We are positive on the gold price outlook for the longer-term. First, easy monetary policy and low interest rates are here to stay. Central banks remain keen to support growth and/or to reach their inflation target. In the near-term we expect growth in the eurozone to remain weak and the economic situation in the US to deteriorate. We expect the ECB to cut the deposit rate by 10bp and to increase the pace of QE asset purchases in Q1 (not expected by the market), and the Fed to cut rates by 25bp in Q1 (the market expects a later cut). Overall, we expect US real yields to decline. These factors should support gold prices. Second, the outstanding amount of negative yielding government bonds will probably grow; while gold has no yield, it is at least not paying negative rates. So this will support gold prices. Third, we expect the US dollar to weaken modestly because of a deterioration in longer-term fundamentals and weakness in near-term cyclical dynamics. Gold tends to rally when the dollar declines, and we think this relationship will hold in the coming years.

A weaker US dollar …

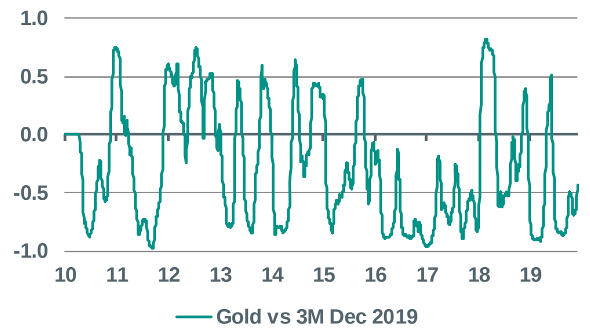
90-day rolling correlation



Source: Bloomberg, ABN AMRO Group Economics

… and lower US interest rates to support gold

90-day rolling correlation

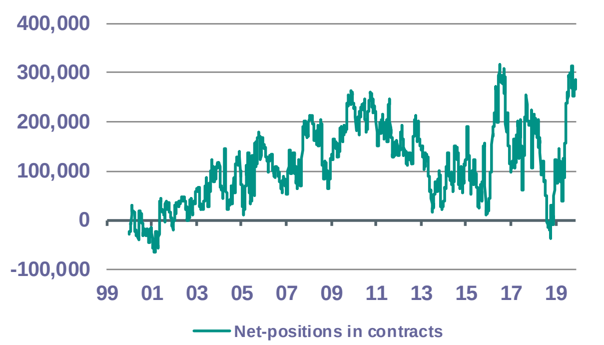


Source: Bloomberg, ABN AMRO Group Economics

Even though the longer-term outlook looks solid, we expect substantial price weakness in the coming weeks and months. Some may argue that gold prices are already USD 100 lower compared to the high set this year. So why do we expect more weakness now? For a start, investors are still massively positioned for higher gold prices. Net-long positioning in the futures markets are extreme, and ETF positioning is at a high (see graphs below). These positions currently hang over the market and prevent prices from moving substantially higher, because every uptick in prices is used to take profit on existing positions. As a result, the downward pressure on prices increases. For now, the break-out and support level of USD 1,450 has held, but as soon as this floor is taken out, prices will probably drop substantially. If it is a quick wash-out of positions, the sell-off could stop around USD 1,400 per ounce. If the sell-off is more aggressive, prices could even drop to USD 1,350 per ounce. The 200-day moving average comes in around USD 1,400 per ounce. A weekly break and close below this level will result in a deterioration of the longer-term technical outlook. It is important not to try to catch a falling knife. We prefer to wait until the sell-off has materialised and prices have stabilised before stepping in again.

Net-long speculative gold positions are extreme …

In contracts

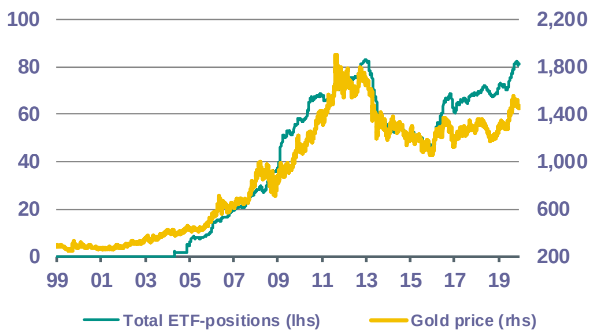


Source: Bloomberg, ABN AMRO Group Economics

… and total ETF positions are also at a high level

In mln

Gold price USD/ounce



Source: Bloomberg, ABN AMRO Group Economics

Moreover, developments on the trade front will probably have a mixed impact on Chinese gold demand. We expect some pick-up in jewellery demand, but lower investment demand from China.

Silver to follow gold

We expect silver prices to follow gold prices with some lag, while the price action will likely be more volatile. We are also optimistic on the longer-term outlook for silver because of the arguments already mentioned above for gold. In addition, silver prices will probably be more supported if global growth and global trade start to stabilise and improve somewhat. In the near term, we also expect weakness in prices as is the case for gold. There are several reasons for this. First, investors also have excessive long silver positions, and position liquidation could be brutal for silver prices, especially if this comes at a time of weaker economic data and uncertainty on the trade front. We think that an aggressive sell-off in silver prices in the coming months will be an opportunity to position for higher prices later in 2020.

Platinum prices to recover during 2020

We expect platinum prices to be relatively resilient in the near-term and to recover during 2020. Global catalyst demand accounts for around 40% of global platinum demand. As a result, platinum prices react more to developments in the car sector and to the outlook for global growth and global trade. During 2020 we expect a stabilisation and some improvement in the global trade and global growth outlook, and this should support platinum prices. Meanwhile, more stringent car emission regulation results in more platinum content for car catalysts. We think that most of the expectations on lower diesel demand is reflected in the price, even though we think that the trend for lower diesel demand will probably continue (which is widely anticipated). Alongside a modest improvement in demand for catalytic converters, we also expect industrial demand and jewellery demand to rise somewhat. The modest rise in industrial demand is in line with our view of some improvement in the manufacturing sector during 2020. The latter reflects higher consumer spending in China.

Platinum is cheap compared to gold …

Source: Bloomberg, ABN AMRO Group Economics

… and cheap compared to palladium

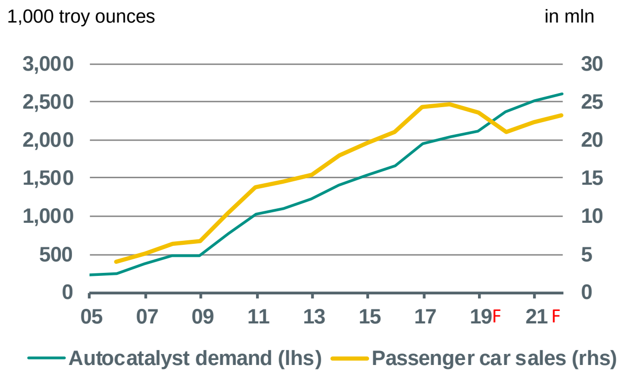
Source: Bloomberg, ABN AMRO Group Economics

Since 2016 the price of palladium has almost tripled, while platinum was out of favour. This pushed the platinum/palladium ratio into extreme territory – levels not seen before. This year, gold and platinum prices have rallied, and this has kept the platinum/gold ratio at an all-time low. So, platinum prices are cheap relative to both palladium and gold (see graphs above). Taken together, platinum is a cheap precious metal and will probably have some higher demand during 2020 supporting our outlook for a price recovery.

Are palladium prices in bubble territory?

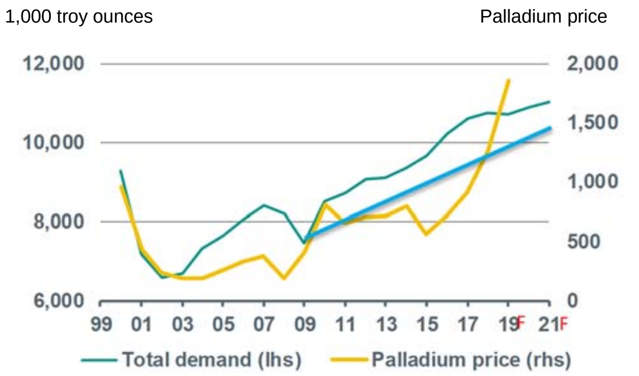
The palladium market has experienced a pronounced supply shortage at the front-end of the curve. This is the result of inventory dynamics, as well as higher palladium demand for car converters to meet the more stringent emission standards in China and Europe in the future. Even though car sales in China have declined year-on-year, Chinese palladium demand for catalysts has probably risen because of the higher loadings (see graph on the left below). Do these higher loadings and higher industrial demand justify the exponential palladium price increase seen since 2015? We don't think so. We have factored in higher palladium loadings for Chinese and European cars, higher global car sales and higher industrial demand in our new demand calculations. We have also considered what the annual marginal increase in demand and in the palladium price were since 2000. If prices were to move in line with demand from 2009 to 2021, palladium would be just below USD 1,500 per ounce at the end of 2021. We continue to think that palladium price increases are not justified by the fundamentals, and that prices will fall back. We have adjusted our price forecasts to USD 1,450 per ounce by end-2020, and USD 1,500 per ounce by end-2021.

Chinese car sales vs China auto catalyst demand



Source: Thomson Reuters Datastream, GFMS, ABN AMRO Group Economics

Palladium price is still too expensive



Source: Thomson Reuters Datastream, GFMS, ABN AMRO Group Economics

ABN AMRO Precious Metals' price forecasts

End period	10-Dec	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
Gold	1,463	1,400	1,400	1,500	1,550	1,600	1,650	1,700	1,725	1,750
Silver	16.64	15.50	16.00	16.50	17.25	18.00	18.50	19.00	19.50	20.00
Platinum	901	900	950	1,000	1,050	1,100	1,150	1,200	1,250	1,250
Palladium	1,891	1,650	1,600	1,550	1,500	1,450	1,450	1,475	1,475	1,500
Average	**Q1 20**	**Q2 20**	**Q3 20**	**Q4 20**	**2020**	**Q1 21**	**Q2 21**	**Q3 21**	**Q4 21**	**2021**
Gold	1,400	1,450	1,525	1,575	1,500	1,625	1,675	1,713	1,738	1,688
Silver	15.8	16.3	16.9	17.6	16.6	18.3	18.8	19.3	19.8	19.0
Platinum	925	975	1,025	1,075	1,000	1,125	1,175	1,225	1,250	1,194
Palladium	1,625	1,575	1,525	1,475	1,550	1,450	1,463	1,475	1,488	1,469

Source: ABN AMRO Group Economics

Find out more about Group Economics at: **https://insights.abnamro.nl/en/**

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