ABN·AMRO

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Precious Metals Watch

Georgette Boele, Precious Metal Strategist
Tel: +31 (0) 629 77 89 / georgette.boele@nl.abnamro.com

The stars seem to be aligned for gold prices

- **A new high in gold prices**
- **The stars seem to be aligned for gold prices**
- **Improvement in investor sentiment, aggressive monetary policy easing, ultra-low interest rates and fiscal stimulus have all supported gold prices**
- **We remain cautious and we expect another round of risk-off in financial markets to support the dollar and to trigger gold position liquidation**
- **But gold price weakness will probably be less severe than we had originally forecasted**
- **New gold price forecast for Q2 is USD 1,575 per ounce (was USD 1,300)**

We last published a Precious Metals Watch on 18 March. At that time, we expected more price weakness in the weeks and months ahead. Our main reasons were prolonged period of stress in financial markets resulting in safe haven demand for the dollar, and position liquidation in gold. We thought that the Fed was mostly done with easing monetary policy. Since 20 March gold prices have rallied in a spectacular manner. They have not only made up for the price weakness earlier in March, but even set a new high on 14 April (still far below the all-time of USD 1,921 on 6 September 2011).

Dramatic turn in events

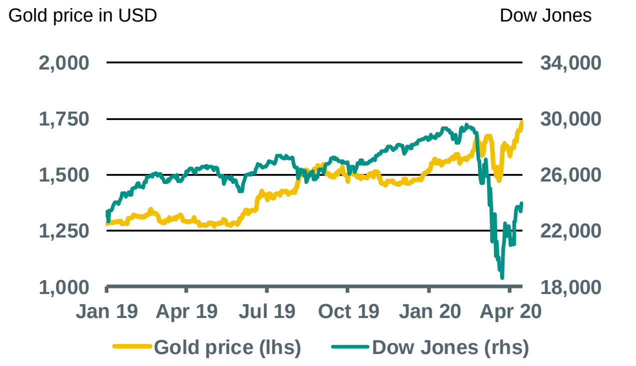
What are the reasons behind this dramatic turn in events? First, when gold prices were close to previous low around USD 1,450 per ounce, there were signs of a shortage in the physical gold market. Between 10 March - 20 March, the gold forward curve showed some backwardation, meaning that the spot price was above the futures price for the months of April, May and June. There could be several reasons for this sense of shortage. The temporary closing of three gold refineries in Switzerland could have been a reason for this. As a result, it was more difficult for investors to get their hand on physical gold.

Second, the level of USD 1,450 per ounce has been an important support in the past. As gold prices failed to move below this level after several attempts, investors became convinced that this was a good buying opportunity.

Third, the Fed used its full arsenal to fight the shortage in the dollar market and to support the economy. The Fed announced unlimited asset purchases to replace the previous $700bn commitment. This has driven the balance sheet much higher (see our Global Daily of 23 March) Other central banks have also eased monetary policy substantially. Aggressive monetary policy easing sounds like music to the ears of gold investors, especially as official rates and government bond yields are unlikely to rise substantially in the coming years and real yields to stay low or move even lower (see graph on the right below).

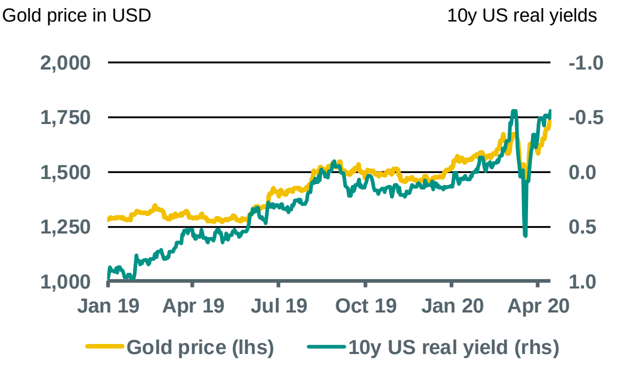
Fourth, the announced monetary and fiscal stimulus across the globe, combined with some improvement in the number of covid-19 casualties in countries that have been in lockdown have resulted in some optimism among investors. There is optimism among investors that we may have seen the worst of the covid-19 crisis and that the recession will be short-lived. It is likely that investors are looking past the seriousness of the near-term weakness in the economy, as in Q3 there is likely to be a snap-back in activity as government-imposed lockdown measures are scaled back. Gold prices have weathered well in a risk-on environment, so they have rallied in tandem with US stocks (see graph on the left below). As risk-off sentiment eased, the dollar has declined, and this has also been a support to gold prices.

Gold prices behave as a risk-on asset …



Source: Bloomberg, ABN AMRO Group Economics

… and move opposite to 10y US real yields



Source: Bloomberg, ABN AMRO Group Economics

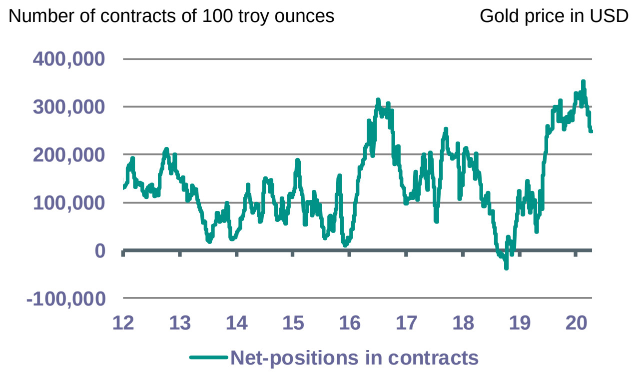
Are the stars aligned for gold prices?

The stars seem to be aligned for gold prices

1. Central banks have embarked on aggressive quantitative easing
2. It is unlikely that government bond yields will rise anytime soon
3. Official rates of central banks are close to zero
4. It is likely that the amount of government bonds in negative yielding territory will rise
5. Fiscal deficits will rise, and as yields won't go up investors will search for other assets

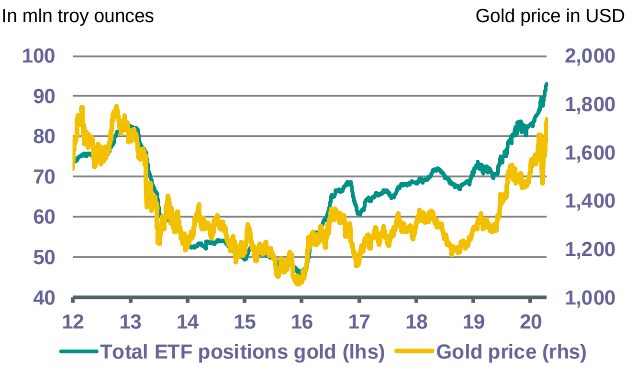
Does this mean that the sky is the limit for gold prices? Even though we recognise that the drivers are supportive for gold prices, we don't expect another strong rise in prices. In fact, we still expect another wave of risk-off to support the US dollar and to weigh on gold prices.

Speculative net-long gold positions still extreme …



Source: Bloomberg, ABN AMRO Group Economics

… as well as total ETF positions



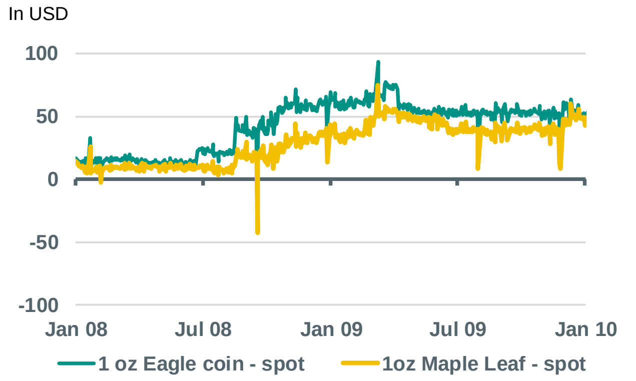
Source: Bloomberg, ABN AMRO Group Economics

As the graphs above show long positions in gold ETFs and in gold futures are still a crowded trade. We think that the position liquidation risk is still high, but probably less positions will be closed than we thought when we released our report on 18 of March. So, the decline in gold prices will likely be less substantial than we had previously forecast. Therefore, we have changed our forecasts to reflect the new reality. Our gold forecast for the end of Q2 is now USD 1,575 (was 1,300) and for the end of 2020 USD 1,700 (was 1,400).

Will investors re-evaluate the gold position they have?

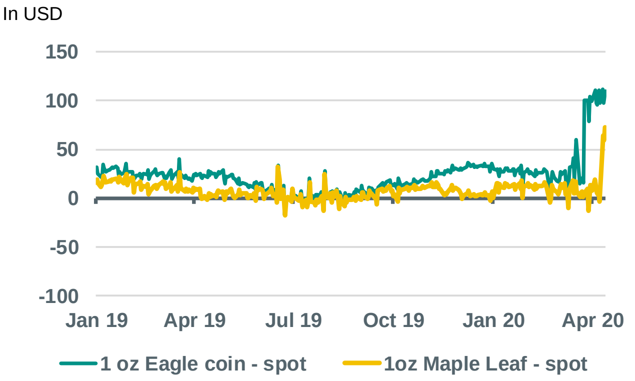
As my column on 9 December (A world with two gold prices?) shows are there several ways to invest in gold. An investor can buy physical gold, but the waiting times for delivery are between 8 to 12 weeks and the premiums are high. This means that it is more expensive to buy physical gold. The graphs below show that 1-ounce Golden Eagle and Maple Leaf coins are more expensive than spot (during the Global Financial Crisis and now).

Gold coins were more expensive during GFC …



Source: Bloomberg, ABN AMRO Group Economics

… and now as well



Source: Bloomberg, ABN AMRO Group Economics

An investor can also buy gold futures. For example, the CME has physically-delivered gold contracts. Not all investors have the opportunity to buy gold via futures. The gap between the future price of the near-term contract and the spot price is wider than usual. It appears that some larger investors have opted to buy gold (with physical delivery) via gold futures.

An investor can also invest in gold via ETFs (physically-backed, or not-physically backed), metal account gold and other gold products.

The argument to buy gold and the time horizon are crucial. Currently gold prices rise in a risk-on environment. So, investors buy gold because of monetary policy easing, because it is not negative yielding investment, and because the yield difference between gold and the US dollar has declined to almost zero. Gold is not rising because of safe-haven buying. So, as soon as we experience another wave of risk-off as we expect, it is likely that gold prices will decline again.

We also think that a lot of investors will re-evaluate the gold positions they have or the positions they would like to have. Does the investor want to speculate with the gold price in an environment of ultra-low interest rates and aggressive monetary policy easing? There are various ways to position for this. If an investor is worried about a collapse of the financial system or that fiscal deficits are unsustainable, this investor will likely opt for physical gold and is not that price sensitive. We think that investors will probably try to switch more into physical gold, meaning that the premium between physical gold (coins, bars but also futures with physical delivery) and the spot could remain high.

ABN AMRO Precious Metals' price forecasts

Changed in bold and red

New										
End period	**15-Apr**	**Dec-19**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**
Gold	1,721	*1,522*	*1,598*	**1,575**	**1,650**	**1,700**	**1,725**	**1,750**	**1,775**	**1,800**
Silver	15.48	*17.94*	*14.04*	**14.00**	**15.00**	**16.00**	**16.50**	**17.00**	**17.50**	**18.00**
Platinum	782	*974*	*731*	**700**	**750**	**800**	**825**	**850**	**875**	**900**
Palladium	2,203	*1,941*	*2,399*	**1,800**	**1,850**	**1,900**	**1,900**	**1,950**	**2,000**	**2,000**
Gold/silver ratio	111.2	*84.8*	*113.8*	112.5	110.0	106.3	104.5	102.9	101.4	100.0
Gold/platinum	2.2	*1.6*	*2.2*	2.3	2.2	2.1	2.1	2.1	2.0	2.0
Palladium /platinum	2.8	*2.0*	*3.3*	2.6	2.5	2.4	2.3	2.3	2.3	2.2
Average	**Q1 20**	**Q2 20**	**Q3 20**	**Q4 20**	**2020**	**Q1 21**	**Q2 21**	**Q3 21**	**Q4 21**	**2021**
Gold	*1,582*	**1,628**	**1,613**	**1,675**	**1,624**	**1,713**	**1,738**	**1,763**	**1,788**	**1,750**
Silver	*16.9*	**14.65**	**14.5**	**15.5**	**15.4**	**16.3**	**16.8**	**17.3**	**17.8**	**17.0**
Platinum	*903*	**726**	**725**	**775**	**782**	**813**	**838**	**863**	**888**	**850**
Palladium	*2,284*	**2,133**	**1,825**	**1,875**	**2,029**	**1,900**	**1,925**	**1,975**	**2,000**	**1,950**

Old										
End period	**15-Apr**	**Dec-19**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**
Gold	1,721	*1,522*	*1,598*	1,300	1,300	1,400	1,450	1,500	1,550	1,600
Silver	15.48	*17.94*	*14.04*	11.00	12.00	12.50	13.00	13.50	14.00	15.00
Platinum	782	*974*	*731*	600	650	700	750	800	850	900
Palladium	2,203	*1,941*	*2,399*	1,400	1,450	1,500	1,525	1,550	1,575	1,600
Average	**Q1 20**	**Q2 20**	**Q3 20**	**Q4 20**	**2020**	**Q1 21**	**Q2 21**	**Q3 21**	**Q4 21**	**2021**
Gold	*1,582*	1,375	1,300	1,350	1,398	1,425	1,475	1,525	1,575	1,500
Silver	*16.9*	11.3	11.5	12.3	12.9	12.8	13.3	13.8	14.5	13.6
Platinum	*903*	625	625	675	704	725	775	825	875	800
Palladium	*2,284*	1,450	1,425	1,475	1,633	1,513	1,538	1,563	1,588	1,550

Source: ABN AMRO Group Economics