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The Sharp Perspective

OUR MONTHLY COMMENTARY

SHARPS PIXLEY LTD BULLION BROKERS LONDON

Gold continuing to set fresh record highs, seemingly oblivious to the growing headwinds

- The buying is so determined that it has so far not been influenced by the sharp rebounds in the US dollar and the US treasury yields
- But, geopolitical risks have escalated with North Korea sending troops to help Russia fight in Ukraine and as Iran joins the fighting in the Middle East…
- …so far the war has not targeted the Middle East oil industry
- Funds have reduced their exposure slightly, but ETF buying continues with holdings increasing for the sixth month in October – there seems potential for significantly more buying given the growing risks the world faces
- China has been a stronger buyer of gold over the past two years, high prices and a rebounding equity market may lead to rotation from gold to equities
- There is much talk that gold is being bought as de-dollarisation gathers pace amongst central banks, but central bank purchases have been slowing this year, suggesting this is not the main driver

Silver has for so long lagged gold, but that seems to be changing now

- Silver prices are up 46.5% since the beginning of the year, gold prices are up 35%
- Chinese stimulus and weaker US monetary policy will boost industrial production, which bodes well for silver demand

PGM prices also rally on prospects for better industrial demand

- PGMs to benefit as battery electric vehicle uptake slows, meaning demand for auto catalysts holds up stronger for longer
- Palladium saw oversized gains compared with platinum in October, as the US was trying to sanction Russia palladium

KEY TAKEAWAYS

- Gold pushing ahead in uncharted waters…
- …strong momentum means it is managing to ignore current headwinds
- Is the latest run away in price last-minute hedging against the US election? We don't think it is due to de-dollarisation as central bank purchases have slowed in recent months
- Markets rarely travel in such straight lines for so long, so there is growing risk of a correction
- That said, the overall bullish case for gold remains strong as the geopolitical situation is deteriorating with North Korea now helping Russia in Ukraine and Israel and Iran attacking each other. On top of that US debt looks to grow even more and if de-dollarisation does eventually gather pace then that would become a major headache for the US, especially with its ability to run such a large deficit
- Silver prices have started to play catch-up, and prices are still 32% below their 2011 record high
- Lower US interest rates and Chinese stimulus, to boost demand for industrial precious metals.

Gold's upward price momentum pushes through mounting headwinds

The persistence of the rally in gold prices is remarkable, with the latest high being $2,790.90 per oz, up 5.9% from the end of September's level of $2,635 per oz. This puts the year-to-date gain at 35%. The rally has significant momentum and that can be a strong driver in its own right. While many of the bullish drivers are known about and are justified, questions are being raised as to why gold prices are still rising given the headwinds the market faces. Has another structural driver emerged, that of de-dollarisation? While everyone is intrigued by a conspiracy theory it seems unlikely that de-dollarisation is the main driver now. Central banks have been taking more interest in gold in recent years, if anything the pace of buying has slowed in recent months, which is what you would expect given the strong price rise. Therefore, the slowdown in central bank buying does not support the idea that there is a surge in de-dollarisation buying, which raises the question what is causing buyers to chase prices higher so aggressively? Chasing prices higher is often done by those in destress, so it maybe that some large-scale OTC option trades are at play, and delta-hedging has become the consistent source of buying – this would help explain why some of the more usual correlations with the dollar and US treasury yields have broken down.

Slower central bank buying puts a question mark over de-dollarisation

While central banks are still buying gold, the pace has slowed. Last year, central banks added 1,037 tonnes of gold to their reserves, this followed a record amount of 1,082 tonnes in 2022. In the first three quarters of 2024, central bank buying totalled 694 tonnes, according to the World Gold Council and with the People's Bank of China (PBoC) not reporting any additions to its gold reserves since May, it seems likely that central banks net purchases will be considerably lower this year than last. It could be that other sovereign wealth funds are buying and the purchases are not being reported, but that remains to be seen.

Odd how gold ignores dollar strength

Gold prices normally have an inverse relationship with the dollar and with US treasury yields, but this has clearly broken down in October. Between June and September, the Dollar Index fell to 100, from 106, a drop of 5.7% and gold prices climbed 13.8% to $2,675 from $2,350, but in October the Dollar Index has rebounded to 104.50, a 4.5% rise, while gold has continued to climb, adding another 4.3%. The same is true with US treasury yields, higher yields are a headwind for gold prices as they raise the opportunity cost of holding gold, but the rise in gold prices in October has happened as the ten-year treasury yield has rebounded to 4.25 percent, from 3.74 percent at the start of October. The fact these price series are out of sync, suggests some out of the ordinary drivers are present – one likely being the uncertainty over the US election.

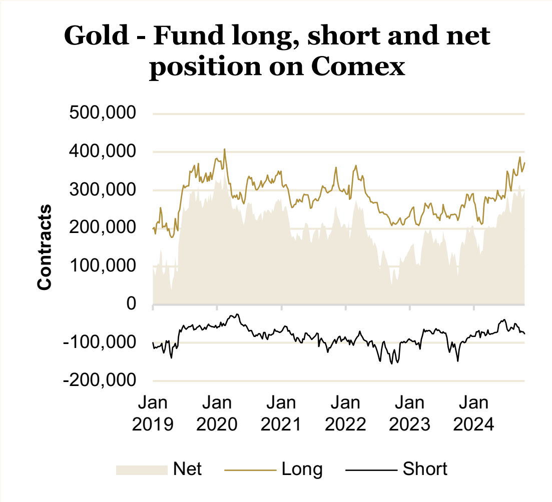

CHART 1

Funds – light profit-taking

The recent fund performance is not supportive of the rally. The overall fund position remains significantly long, but the net long fund position has eased slightly to 296,204 contracts, down from the recent peak of 315,390 contracts on September 24. This has happened as longs have cut exposure by 15,759 contracts to 371,813 contracts, while shorts have increased their exposure by 3,427 contracts to 75,609 contracts. The net long position has been trending higher for over a year now, but the recent peak at 315,390 contracts was still 12% below the record high of 353,649 contracts seen in February 2020, when the pandemic was starting to gather momentum.

ETF investors continue to accumulate

ETF investors continue to buy gold, buying around 34 tonnes in the first four weeks of October. Since turning net buyers in May, average monthly purchases have been 25.7 tonnes. Holdings stood at 3,234 tonnes, up from April's low of 3,080 tonnes. Holdings are still 17.4% below the all-time peak of 3,915 tonnes, seen in October 2020. Given concerns about US debt and the possibility that an alternative BRICS payment system may emerge in time, which could cause debt financing issues for the US, it would not be surprising to see ETF holdings rise further. In a way, it is surprising that with many western equity indices at record highs, suggesting corrections could lie ahead, and the uncertainty over the US election, that interest in ETFs has not been stronger.

Jewellery demand fell 27.5% to 400 tonnes, while demand for bars and coins climbed 27% to 282 tonnes. While high prices are weighing on jewellery demand, there is a distinct possibility that with the government stepping up its stimulus efforts, which are focused on supporting property sales and the stock market, that there may be some rotation out of gold into the relatively weak equity market. This is especially so given the gains gold investors will be sitting on. Gold disinvesting could make the already weak physical market, due to weak jewellery demand, even weaker. The World Gold Council reported in its Q3 Gold Demand Trends that "high prices have taken their toll on tonnage, producing one of the weakest y-t-d totals in our quarterly dataset back to 2000". In India, the WGC estimates that gold demand is likely to be the lowest since 2020.

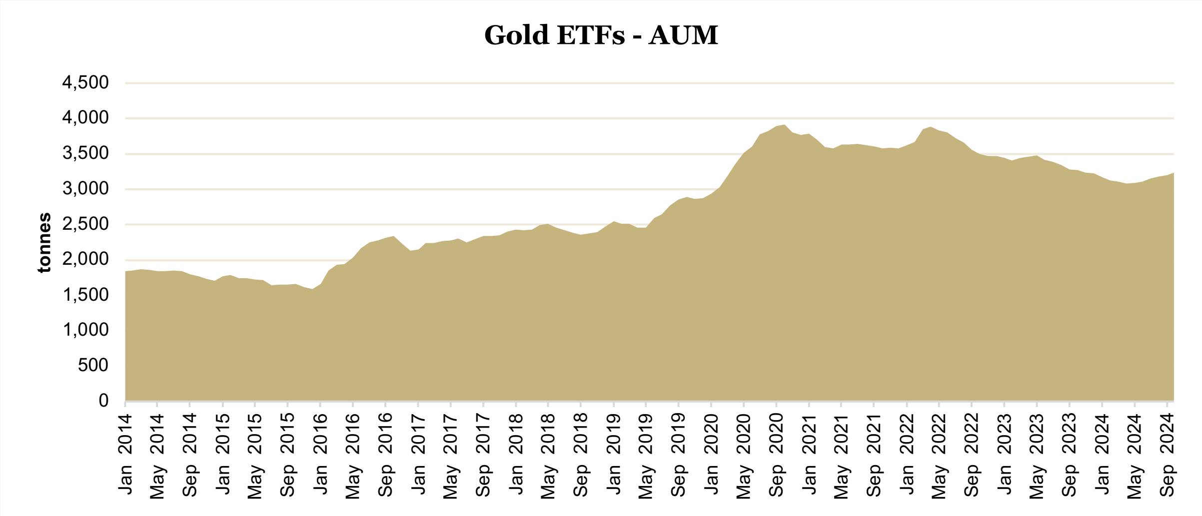

CHART 2

Cooler wind from China

China's appetite for gold has cooled this year, compared with the strong performance in 2023, when the troubled property market and falling equity prices left investors with few alternatives. In addition, with the yuan weakening, gold provided a much-needed investment vehicle. The PBOC was an aggressive buyer. Chinese gold reserves climbed to 2,235 tonnes at the end of 2023, up from 2,010 tonnes at the end of 2022. In the first three quarters of 2024, the country's gold consumption fell 11% to 741 tonnes, according to the China Gold Association.

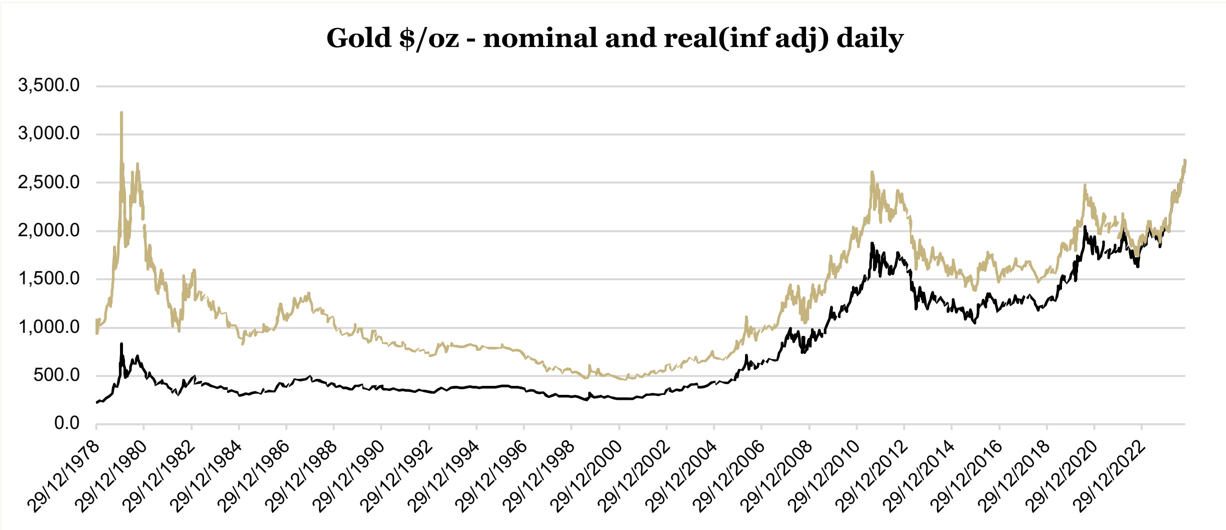

CHART 3

SUMMARY

The high price in 1980 was $850 per oz, which would be equivalent to around $3,200 per oz today. This seems to be why expectations are running high for prices to move up towards that level. While the overall long-term outlook is bullish with global debt growing, geopolitical risks escalating (North Korean involvement in Ukraine and Israel/Iran attacks) and potential for de-dollarisation one day; right now the headwinds do seem to be mounting and momentum on its own may not be enough - markets rarely go up in such a straight line for such a long time.

Gold Statistics

	2020	2021	2022	2023	Q2 2024	Q3 2024	Sep-24	Oct-24
London prices								
$/oz	1,769.97	1,799.87	1,801.17	1,942.99	2,337.69	2,476.21	2,567.62	2,690.07
£/oz	1,378.80	1,308.41	1,457.43	1,562.57	1,852.42	1,904.12	1,942.41	2,060.81
€/oz	1,549.38	1,308.41	1,457.43	1,796.32	2,067.61	2,253.43	2,311.78	2,467.35
Parity prices								
Australian - A$/oz	2,544	2,393	2,589	2,924	3,547	3,697	3,795	4,007
South Africa Rand/kg	29,352	26,519	29,139	35,952	42,780	44,455	45,216	47,237
Japan Y/g	189,104	197,644	241,248	273,806	364,369	368,858	367,555	402,676
India Rupee/oz	131,445	133,434	142,184	160,596	195,010	207,405	215,167	226,046
COMEX - futures contracts								
Stocks ('000oz)#	38,157	33,805	23,180	19,191	16,505	17,112	17,112	17,133
Vol (million contracts)*					15.89	14.84	4.13	4.45
OI ('000 contracts)#					448	528	528	569
CFTC (Futures Only Data) non-commercial								
Net Positions#	268,872	213,157	136,880	207,718	246,229	315,390	315,390	296,204

Figures are period averages unless marked by *, indicating total in the period, or #, indicating value at the end of the period.

~ = data not available yet, *italics* = estimates, OI= Open Interest on the exchange

Silver, poor man's gold, is outperforming gold this year

Silver has underperformed gold in many ways since gold's major uptrend got underway in 2019, when prices broke out of the 2013-2019 base. By mid-2020, gold had set a fresh record high, as it has done so many times since, while silver has lagged. Even after silver's strong performance during the pandemic, it then spent most of 2021 to early-2024 drifting and below the pandemic highs. But that has now changed. Indeed, while silver still seems to be underperforming gold in that silver has not got anywhere near setting a fresh record high (the high was $49.81 per oz in April 2011), it has outperformed gold this year. Silver prices have rallied 46.5%, compared with gold's 35% rally.

CHART 4

Funds increase net long exposure

The funds trading Comex silver have increased the net long position to 66,355 contracts, up from 62,198 in late-September. The longs have added positions and the shorts have been covering. Note, the trend in short-covering is stronger than the trend in fresh buying, with the gross long position at 82,139 contracts, still well below the high of 111,282 contracts seen in July 2019. This suggests the funds are still not fully convinced about being bullish.

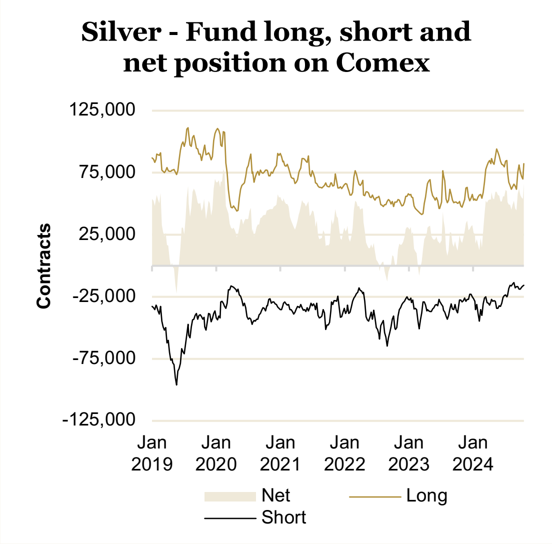

CHART 5

Physical tailwinds, financial headwinds

The latest up leg in silver was spurred by traders anticipating a large US interest rate cut in September and was then further fuelled by China's stimulus measures. Both will be good for industrial demand and with silver's wide use in many high-tech applications, this bodes well for silver demand. In addition, high gold prices impact gold jewellery demand, opening opportunities for silver jewellery demand. But, like for gold, the stronger dollar and higher treasury yields are headwinds, but perhaps less so for silver as investors are likely to see silver as having catch-up potential to gold. This is for three reasons: As mentioned above, silver prices are still 30% below the record high, the gold/silver ratio is at 1:82, the long-term ratio, since the gold standard was abandoned in the 1970s, is 1:65, suggesting that at today's gold price silver could be trading around $43 per oz and if China's stimulus works, then physical industrial demand will grow.

TECHNICALS – UPSIDE BREAKOUT

With the bull market starting in early March, at around the $22.50 per oz level, the first up leg ran up to May's high at $32.50 per oz, it then consolidated with prices falling back to $26.46 per oz in August, before pushing higher again with the move above $32.50 per oz establishing a fresh 12-year high. The first leg ran for $10 per oz, so far the second leg has climbed $8.40 per oz.

SUMMARY

Despite silver already outperforming gold this year, silver still seems to have more catching up to do and the tailwinds to do so. That said, should gold sell-off, silver is bound to follow, but that may then be seen as an even better opportunity to get involved.

Silver Statistics

	2020	2021	2022	2023	Q2 2024	Q3 2024	Sep-24	Oct-24
London Prices (US$/oz)								
Spot London price	20.55	25.14	21.73	23.39	28.86	29.42	30.01	32.41
Parity (London) prices								
Japan (Y/g)	2,196	2,761	2,911	3,296	4,500	4,389	4,296	4,852
India (Rupee/oz)	1,526	1,864	1,715	1,933	2,408	2,464	2,515	2,724
COMEX - futures contracts								
Stocks ('000oz)#	396.5	355.7	299.0	253.9	255.7	305.1	305.1	308.6
Vol (million contracts)*					7.20	5.09	1.52	1.76
OI ('000 contracts)#					155.3	144.7	144.7	155.1
CFTC (Futures Only Data) non-commercial								
Net Positions#	54,779	26,458	31,027	31,863	50,836	62,188	62,198	66,355
Other Indicators								
Gold/Silver ratio#	1:72	1:78	1:76	1:86	1:86	1:82	1:82	1:82

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PGMs put in strong performances – driven by better demand prospects

At the highs in late-October, palladium and platinum prices were up 24.3% and 7.5% respectively since the end of September, extending the rebounds off the summer lows. As industrial precious metals, they look set to benefit from the lower US interest rates, as they do from China's stimulus measures. In addition, some pushback against the adoption of battery-only electric vehicles in favour of plug-in hybrids and hybrid vehicles has rekindled interest in the metals as it means demand for auto-catalysts is likely to be stronger than earlier feared. Palladium's out performance over platinum seems to be for two reasons - reports that the US is pushing G7 economies to put sanctions on Russian palladium and due to the funds being net short of the metal. While the US might want sanctions on Russian palladium, it is unlikely the G7 economies with domestic auto industries would want to impose further costs on their manufacturers who are already facing difficult times. Take for example, Germany's VW who has warned it may have to close three factories in Germany.

Funds behind the rally

The funds have been a bullish factor in both PGMs, but as with silver, the buying has come more from short-covering than from fresh buying. This is particularly pronounced on the palladium chart, seen by the steepness of the rise in the lower black line, while the top line shows long's cutting positions. On the platinum chart, the long position has tended to oscillate sideways, while the black line showing the short position has been trending higher, indicating short-covering. During October, the net short palladium position has dropped to 5,080 contracts, from 6,733 contracts at the end of September and a peak of short 13,244 in June. For platinum, the net long position has climbed to 34,876 contracts, up from 24,401 at the end of September and a recent low of 1,388 contracts in early-September.

China to launch PGM futures contracts

China's Guangzhou Futures Exchange is planning to launch PGM futures contracts early next year, which will provide local companies with hedging tools to manage risk in yuan. With the metals used widely in the auto industry as well as in the jewellery industry, this should lead to a more efficient supply chain that should enable more competitive pricing, which in turn should boost demand. Russia also announced it would launch futures contracts too.

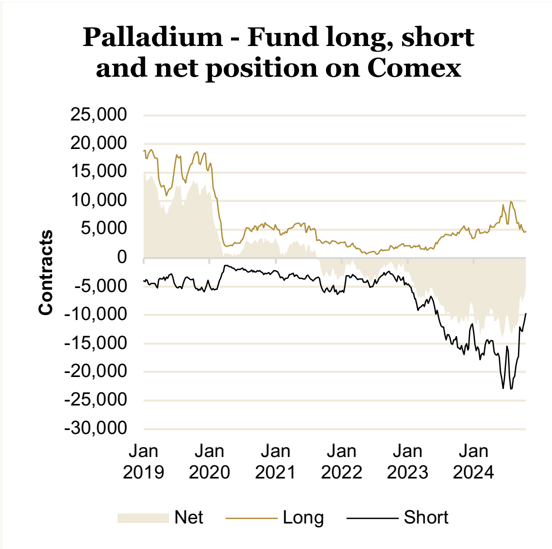

CHART 6

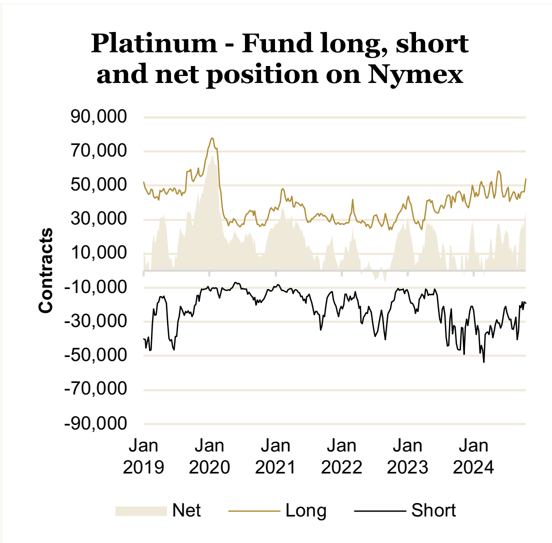

CHART 7

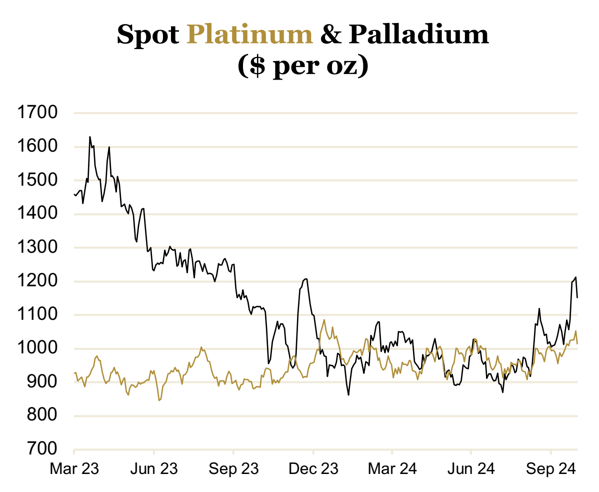

CHART 8

SUMMARY

The fundamentals for the PGMs have improved in that the demand outlook is brighter and prices had earlier got back to levels that were threatening supply cutbacks, suggesting bases are now in place. Palladium looks best placed to see further gains given the funds are still net short, but platinum should benefit as platinum jewellery offers a cheaper alternative to gold jewellery.

PGM Statistics

	2020	2021	2022	2023	Q2 2024	Q3 2024	Sep-24	Oct-24
London Prices (US$/oz)								
Platinum	884.49	1091.24	961.24	966.88	980.94	963.32	964.17	999.67
Palladium	2197.06	2398.86	2108.33	1338.69	972.46	958.21	1018.67	1069.44
Japanese Parity Prices (Y/g)								
Platinum	94,499	119,829	128,748	136,253	152,928	143,728	138,021	149,641
Palladium	234,734	263,419	282,390	188,648	151,514	142,703	145,823	160,084
South African Parity Prices (Rand/kg)								
Platinum	14,668	16,078	15,551	17,891	17,956	17,302	16,979	17,554
NYMEX Stocks ('000oz)								
Platinum#	623.10	482.00	167.20	206.20	174.84	144.97	144.97	139.39
Palladium#	138.1	95.2	53.4	36.7	34.7	39.3	39.3	38.5
CFTC (Futures Only Data) non-commercial#								
Platinum	25,829	4,469	24,666	23,662	18,322	24,401	24,401	34,876
Palladium	2,714	-3,109	-2,206	-7,801	-11,685	-6,733	-6,733	-5,080
Other Indicators (US$/oz)#								
Pt-Au spread	-816	-858	-747	-1,056	-1,353	-1,666	-1,666	-1,756
Pt-Pd spread	-1,295	-966	-723	-113	2	-12	-12	-128

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