

## Precious metals: Gold soars

The yellow metal has risen along with bond yields as inflation looks set to turn



Source: shutterstock

### Market update

The dollar's demise has reinvigorated speculative flows into precious metals, with platinum in front. Rising yields are offset by inflation expectations and currency reigns king with room for more upside as our FX team expects more pain for the dollar.

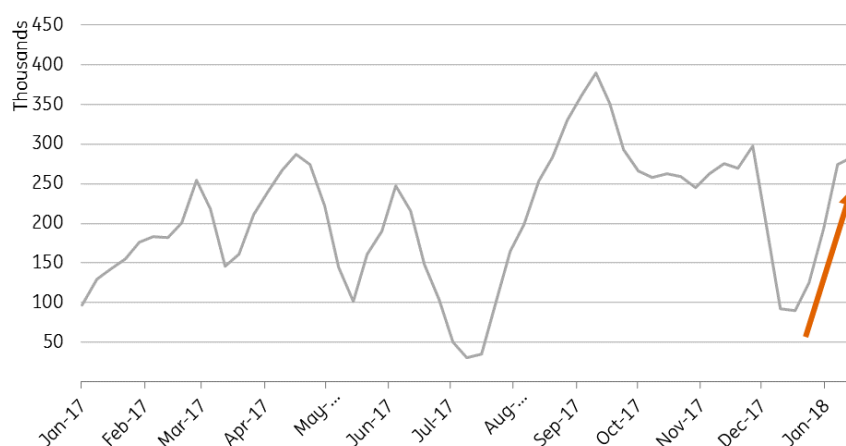
### Money managers return to precious metals en masse

Managed money net longs across precious metals have surged 284k lots in the last month, a more than two-fold increase which more than reversed the steep sell-off in early December. On a relative basis, platinum positioning has swung the most, from net short 10% of open interest to 23% net long. In turn, prices have surged 16% from mid- December. Whilst the platinum-palladium ratio has reversed, palladium shorts are flat, suggesting traders sought a leveraged oversold precious position rather than to short the ratio. Speculative gold flows also outperformed open interest and have further to go before looking stretched. Longs represent 39% of open interest compared to the highs of 48% seen in 2017. Open interest had a slight dip on Monday suggesting

some profit taking but outside of futures, there has also been a net 852koz of inflows into gold ETFs. The dollar's demise is the clearest driver for the precious rally and for further upside. The dollar index is down 3% year-to-date and our FX team sees more pain ahead. In their view, the prospects for Europe are better than the US, where any tax stimulus will be short-lived. That's expected to push EUR/USD to 1.30 by year-end. For perspective, gold's three-month 6.4% gain in dollar terms is only 1.3% in EUR. But the yellow metal rose across currencies last month, highlighting the strong flows.

## CME managed money net long position in precious metals

Includes positions in CME gold, silver, platinum and palladium futures



Source: Bloomberg

## In face of rising yields

The precious metal's rally is all the more impressive in the context of surging bond yields. The US 10-year has reached 2.66%, the highest since 2014, and the two-year is closing the gap at 2%, a level not seen since 2008. Gold as a non-yielding asset should really be losing favour but it's not. The missing ingredient is inflation. The US CPI in December came in at a fairly lacklustre 2.1% but our economists believe all the ingredients are there for US inflation to turn: Wages set to grow, a low dollar, high commodity prices, and one-off factors like unlimited mobile data will soon drop out of annual comparisons. The market, it seems, is of the same mind, with inflation-linked swaps staying flat through the yield surge. With inflation follows rate hikes, and the market is already pricing in a 70% probability of a March increase, with next week's meeting probably a non-event. Our FX team, however, thinks that such increases have little chance of changing the dollar's downward trajectory: please see "[The logic of Fed tightening = A stronger USD is so 2014](#)".

## Platinum prices up

Platinum prices are up 18% from the December bottom and the platinum-palladium ratio has improved from its historical low of 0.85x to a slightly higher 0.92x. As said at the outset, traders have piled into platinum longs without any corresponding palladium short because they were looking for the oversold leverage to the precious complex. Those who do think the price ratio should revert still struggle to hold the position because of a costly backwardation in palladium markets. Concerning the auto catalyst demand, European vehicle sales had a strong 2017, up 3.4% but with a disappointing 4.9% year-on-year drop in December. Counting against the Pt-Pd

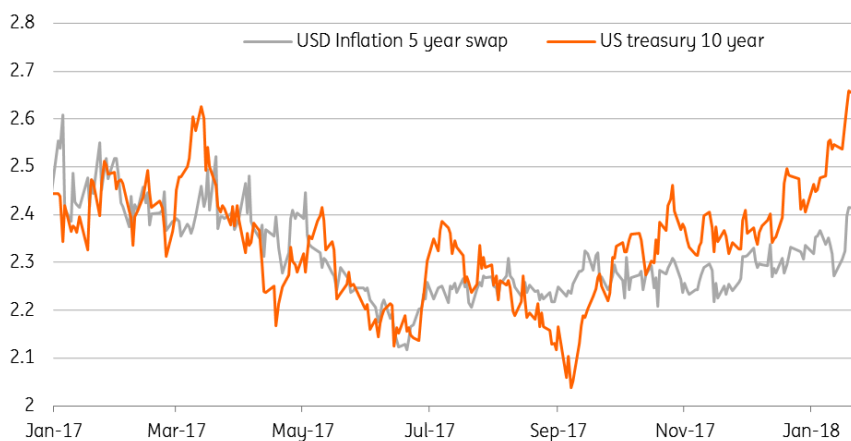
ratio, the ACEA has confirmed that palladium-friendly gasoline sales have started to dominate sales this year. The World Platinum Investment Council estimates a 2% YoY drop in auto catalyst demand this year followed by a further 1% next year.

**18%** Platinum prices growth  
from the December bottom

## Indian budget this week

The dollar and inflation expectations are driving these markets but when flows settle down, fundamentals will play their part. India's gold imports were down 7% YoY for the Oct-Dec whole wedding season and even with the December comparison inflated from last year's demonetization curbs. Local press reports suggest that commerce could push for a reduction in import duties but given the recent implementation of the goods and services tax and widening trade deficits this is unlikely.

## Inflation-linked swaps much flatter than yields



Source: Bloomberg

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