

Precious Metals: The dollar giveth, the dollar taketh away

A strong beat in Friday's US jobs report has furthered investor expectations of rising inflation and additional rate increases. The former continues to drive precious metals despite soaring yields whilst the latter is a potential headwind



Source: shutterstock

Inflation, Inflation, Inflation

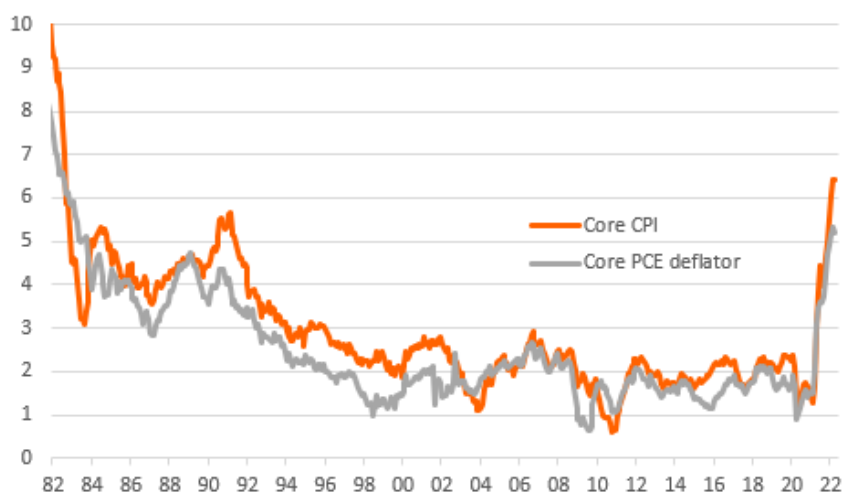
Inflation expectations have allowed gold to make gains this year despite surging yields. On Friday, the US jobs report showed wages grew 2.9% year-on-year in January, the fastest since 2009. The spread between the 10-year and the inflation-linked swap hit new highs on the news as the missing addition to low unemployment seemed to be finally picking up.

With equity valuations appearing vulnerable to higher borrowing costs, stock markets have since sold off significantly. Our FX strategists point out that the asset performance this week is the typical risk-off pattern that was seen in six of the seven instances of VIX spiking above 50% since 1990. The 10-year yield has come down 3bp from its Friday high along with the equity exodus. Funds have generally moved to risk-averse assets as the sell-off originated from within equity markets, not externally. So why then has gold's self-haven status disappointed?

In times of distress, gold can indeed fall with equities when sold to meet margin calls, but CFTC data shows longs held firm last week and only mild dips in open interest thereafter. Gold's relative stability might therefore add the perspective that distress is not the correct word. The ING team are calling it a "healthy correction". Equity valuations may have run ahead of themselves but the economic backdrop is solid.

Given this, it is the greenback that appears to have outshone gold's safe-haven appeal and has rebounded 1% against the Euro so far this month. Our FX team think this is temporary and fundamentals will revert towards a weaker 1.30 by year-end. This is not expected to be derailed whether its three or four rate hikes this year. But higher rates are indeed headwinds for the non-yielding precious metals. The jobs data and the dual addition of "further" in Fed commentary seem to have emboldened expectations of four rate hikes although our economists are sticking to three for now. The probability of March is now priced at an 84% certainty.

Inflation swaps diverge further after US jobs report



Market Fundamentals pick up in Q4

When flows settle down, fundamentals might yet have their turn to direct markets and seem to have improved in Q4. The World Gold Council (WGC) published its 2017 report yesterday. Ironically, amid the current volatility, gold investment demand was down 7% last year because of competition from equities and cryptocurrencies. However gold investment did start to come back in favour by Q4 as inflation themes emerged. We note ETF holdings were up 6% in H2 2017 but the 940koz level this year has almost halved since prices have peaked.

Jewellery accounts for over half of gold demand and increased 4% last year. China registered its first demand increase since 2013, a decent 3% that was spurred by a 6% pick up in Q4. India also had its strongest quarter for at least 17 years (which is in part the seasonal boost of the wedding season). Total year Indian jewellery demand recovered 12% from a low 2016 as the goods and services tax and demonitisation effects rolled over.

Silver and palladium behaving badly

If gold can be blamed for not rising through the equity turmoil then the steeper sell-offs in silver

and palladium- compared to the solely industrial metals- is more extreme still. Copper is down 1% month-to-date.

After a 3.8% plunge on Friday, the gold/silver ratio briefly hit above 80 for the first time since early 2016. The ratio has risen from 75 since Q4 2017 as silver has lacked gold's investor appeal as an inflation hedge. ETF silver holdings are down 3% since June 17 compared to +4% inflows for gold. Commitment of trader data shows longs are back to December rate hike lows and on Friday's sell-off, the open interest rallied 6% which suggests investors are rebuilding shorts. Over half of silver usage is industrial so given our positive outlook for the global economy, the gold/silver ratio should not be at Great Financial Crisis levels, and we expect a move back towards 70 by year-end. Silver's fundamentals are turning as the silver institute expects robust demand to create a mild deficit this year after a 32.2Moz surplus last year.

Gold-to-Silver Ratio at GFC highs

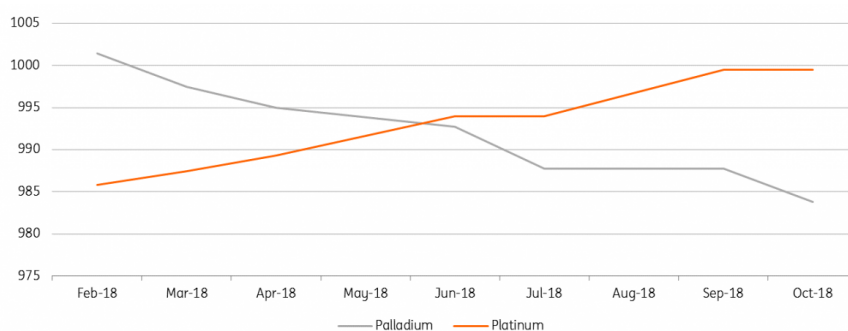


Source: Bloomberg, ING Research

Platinum-Palladium heading back to parity?

Palladium continues to see profit-taking after its 53% rally in 2017 and the CME contract managed money longs reduced by 7% last week. The platinum-palladium ratio has recovered to 0.98 from its 0.86 lows and the forward curve is expecting platinum to be back on top by July. Through the Friday sell-off, Palladium backwardation briefly narrowed but quickly returned which is keeping this an expensive ratio for investors to short. The funds continued to add length to platinum last week with the longs now up 70% since the start of the year.

Forward Curve Puts Platinum back on top by July



Source: CME, ING Research

Author

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania
tiberiu-stefan.posea@ing.com

Marine Leleux
Sector Strategist, Financials
marine.leleux2@ing.com

Jesse Norcross
Senior Sector Strategist, Real Estate
jesse.norcross@ing.com

Teise Stellema
Research Assistant, Energy Transition
teise.stellema@ing.com

Diederik Stadig
Sector Economist, TMT & Healthcare
diederik.stadig@ing.com

Diogo Gouveia
Sector Economist
diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux
Sector Strategist, Financials
marine.leleux2@ing.com

Ewa Manthey
Commodities Strategist
ewa.manthey@ing.com

ING Analysts

James Wilson
EM Sovereign Strategist
James.wilson@ing.com

Sophie Smith
Digital Editor
sophie.smith@ing.com

Frantisek Taborsky
EMEA FX & FI Strategist
frantisek.taborsky@ing.com

Adam Antoniak
Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Senior Editor and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Oleksiy Soroka, CFA

Senior High Yield Credit Strategist

oleksiy.soroka@ing.com

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist

sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy

gerben.hieminga@ing.com

Nadège Tillier

Head of Corporates Sector Strategy

nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland

charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist

+31(0)611172684

laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist
raoul.leering@ing.com

Maarten Leen
Head of Global IFRS9 ME Scenarios
maarten.leen@ing.com

Maureen Schuller
Head of Financials Sector Strategy
Maureen.Schuller@ing.com

Warren Patterson
Head of Commodities Strategy
Warren.Patterson@asia.ing.com

Rafal Benecki
Chief Economist, Poland
rafal.benecki@ing.pl

Philippe Ledent
Senior Economist, Belgium, Luxembourg
philippe.ledent@ing.com

Peter Virovacz
Senior Economist, Hungary
peter.virovacz@ing.com

Inga Fechner
Senior Economist, Germany, Global Trade
inga.fechner@ing.de

Dimitry Fleming
Senior Data Analyst, Netherlands
Dimitry.Fleming@ing.com

Ciprian Dascalu
Chief Economist, Romania
+40 31 406 8990
ciprian.dascalu@ing.com

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr

Iris Pang
Chief Economist, Greater China
iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research
+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com