Precious metals

Cautiously optimistic

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FLASH NOTE

SUMMARY

- Gold may perform rather well in 2023 despite US real rates being significantly less supportive than in previous years. Our 12-month projection stands at USD1,880 per troy ounce.
- Silver could outperform gold in 2023 should our scenario of an economic recovery in the later part of 2023 prove to be correct. While we are cautious on the short term, our 12-month projection is at USD25.0 per troy ounce.
- Platinum looks more attractive than palladium as its usage in the car industry is less at risk than palladium. We see scope for a structural outperformance of platinum relative to palladium. Our 12-month estimate stands at USD1,150 per troy ounce for platinum, whereas our 12-month estimate for palladium is at USD1,700 per troy ounce.

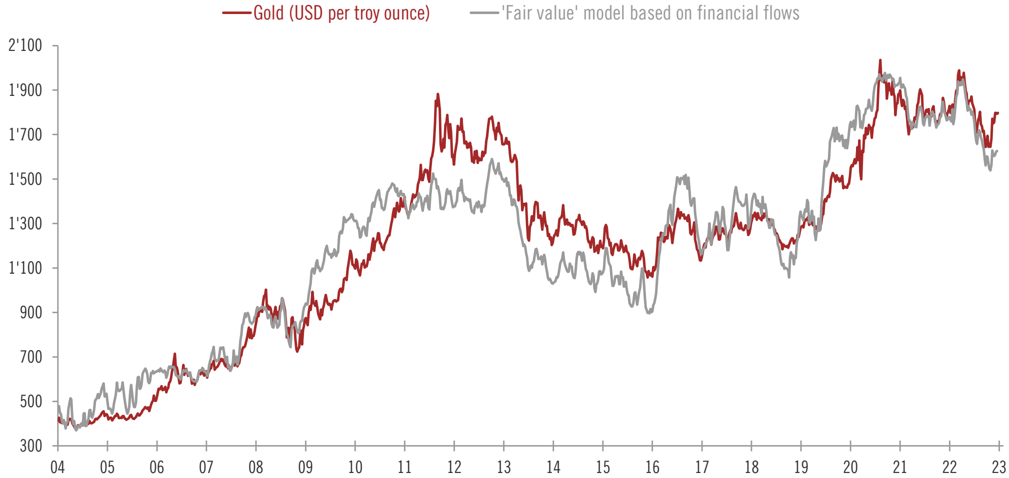
GOLD IN AN ENVIRONMENT OF POSITIVE REAL RATES

Gold price is mainly driven by investment demand. A key driver of investment demand is the opportunity cost of holding this non-yielding asset. Given the recent surge in the US 10-year real interest rate (from roughly -1.1% in March to as high as +1.7% in November), such cost has significantly increased and may penalise gold relative to US treasuries that are also proven safe assets.

While US real rates may not move much higher than their current levels (1.5% on 22 December), they are likely to remain well into positive territory in 2023, which would make gold price expensive relative to real rates alone. That said, investment demand is also driven by the trend in the US dollar, the fear of high inflation and global uncertainties. On that front, ongoing elevated uncertainties (both economic and geopolitical) and an expected decline in the greenback should provide some support to the yellow metal. While a decline in inflation could erode the attractiveness of gold as a hedge against inflation, the relatively high level of inflation and the impact its decline may have on the Fed's monetary stance should act as significant offsets.

Adding in support from central bank demand, gold price could do rather well against the US dollar despite the end of extremely low opportunity costs to hold gold linked to negative real rates. Our three-month projection stands at USD1,700, while the 12-month one is at USD1,880 per troy ounce.

Chart 1: Gold looks expensive relative to financial flows



Source: Pictet Wealth Management, Bloomberg Finance L.P., 23 December 2022

SILVER MAY FACE SHORT-TERM HURDLES

Silver has been strong in the past months rising from USD17.9 in early September to as much as USD24.2 on 20 December. While positioning in the futures market suggests some short covering, stabilising ETF demand (after months of decline) and strong Indian imports (likely from pent-up demand after disruption from covid-19) have led to a strong outperformance of silver relative to gold.

Still, with the price of silver relative to gold now close to its long-term average, positioning in the futures market back to historically neutral territory and limited scope for physical demand to keep up the recent pace, the momentum in the price of silver is likely to deteriorate. An economic downturn in major economies would likely exacerbate downward pressure on prices. As such, we would be cautious on the short term and stick to our three-month projection at USD20.0 per troy ounce.

Over the longer term, we see silver as capable of outperforming gold based on improving industrial demand. Besides a potential global economic recovery in the later part of 2023, the structural demand linked to the energy transition should bring some strong long-term support to silver price. Our 12-month estimate stands at USD25.0 per troy ounce.

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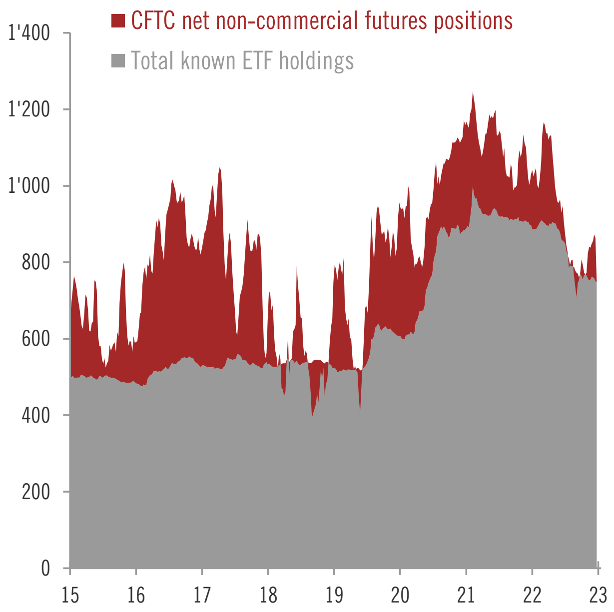
PLATINUM TO OUTPERFORM PALLADIUM

We think that the recent outperformance of platinum relative to palladium has further scope. Apart from the fact that platinum price is still at a decades-low level, market balance for palladium is likely to deteriorate over coming years. Part of the reason comes from the increasing share of electric vehicles (EV) within overall car sales. As palladium demand stems almost entirely from autocatalyst demand (ca. 85%), the decline in market share of the internal combustion engine car is a clear threat for palladium price. As Russia is a large producer of palladium, risks of disruptions remain a key source of uncertainties. At this stage, there are no signs of any decline in Russian production relative to previous years, which has weighed on the price of palladium.

Autocatalyst demand represents slightly less than 40% of platinum demand. While a decline in such demand is negative for platinum price, the emergence of fuel cell electric vehicles could counterbalance its impact as platinum is key to this technology. That said, it may take years before such demand leads to meaningful increase in demand. Besides autocatalyst demand, platinum is used in jewellery and in industry. In particular, platinum is positively correlated to gold price (as a potential substitution of gold jewelery), which makes it somewhat less volatile than palladium.

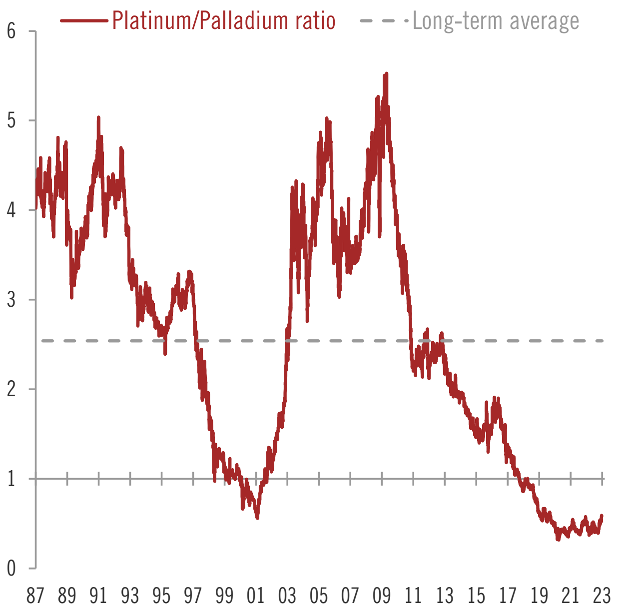
Overall, we see the price of palladium as particularly expensive and see limited upside. On the contrary, platinum looks rather cheap and even if it may take time to see its market balance improve meaningfully, platinum's outlook looks significantly brighter than palladium. Our 12-month estimate stands at USD1,150 per troy ounce for platinum, whereas our 12-month estimate for palladium is at USD1,700 per troy ounce.

Chart 2 : Silver ETF and futures flows



Source: Pictet Wealth Management, Bloomberg Finance L.P., 23 December 2022

Chart 3: Platinum/palladium price ratio



Source: Pictet Wealth Management, Refinitiv, 23 December 2022

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