Precious Metal Markets

The conflicting health of markets in platinum and palladium look sets to continue, as evidenced by *Platinum 2003*, Johnson Matthey's latest market review of supply and demand for the platinum group metals (PGMs). Gold, meanwhile, continues to mystify. By **GUY ISHERWOOD**

MUCH ATTENTION OF late has been focussed on the bullion sector. The price of gold has followed patterns that were largely predicted in the last edition of this magazine (*Commodities Now, March 2003*). The pre-war run-up began in December with a peak reached in February (up to US$ 385 oz). The subsequent US dollar price fall (precipitated by the expected success of troops in Iraq) and rise once again, (precipitated largely by the fall in the value of the US dollar) have left many scratching their heads as to the future direction of the yellow metal.

The safe-haven demand factor is still in play. Hostilities are far from over. Some say they have only just begun. Perhaps there are more risks now than, say, post September 11th. The world remains a dangerous place and gold may well be being valued accordingly. But is it?

Andy Smith of Mitsui Global Precious Metals Research sees it thus: "Dollar weakness should raise all dollar-priced commodity lifeboats, provided the world outside the US doesn't appreciate itself into recession. But enough theory. In practice, the gold market seems to have usurped 'dollar weakness' as its own private correlation."

While the dollar exchange rate has a real bearing on the gold price – particularly of late we are told – experience tells us that it has only limited explanatory power compared with war and terror. "Position gold in this pall of semi-professional pessimism if you like. Since it surrendered six weeks before a missile war fired in anger in Iraq, might it, equally presciently, be the first beneficiary of an 'unpeace'?" says Smith.

Platinum Group Metals

Compared with gold, forecasting PGM prices should be a walk in the park. Experience over the last 2-3 years, however, has left many unimpressed.

Platinum prices moved up smartly in the latter half of last year, pacing gold to a large extent. Like gold, prices declined as warring success became a reality. Prices remain strong and most market forecasters see platinum maintaining its current trading range. Palladium, on the other hand, is still suffering from the fall-out of serious market disruptions over a number of years. Palladium prices plunged in April to an average of US$166 oz. Analysts are in sharply disagreement over palladium's near term prospects.

Here, we review the findings of Johnson Matthey's just issued *Platinum 2003* report for an insight into future supply and demand trends for platinum and palladium.

Platinum Highlights

- Demand for platinum grew by 5% in 2002 to a new high of 6.54m oz.
- Buoyant retail sales of platinum jewellery in China, despite higher prices, lifted total jewellery purchases by 9%.
- Auto industry purchases of platinum were limited by the use of stockpiled metal by some companies, but consumption of the metal in autocatalysts grew strongly.
- Industrial demand for platinum increased by 2%; the main contribution to the growth came from higher demand for catalysts from the chemical industry.
- Supplies of platinum increased by just 2% as sharply higher output in South Africa was balanced by a drop in sales from Russia.
- The widening deficit between supply and demand was reflected in the platinum price, which rose by 24% to finish the year at US$598.

Platinum

Demand for platinum grew by 5% to 6.54m oz. in 2002, driven by another strong year of sales to the Chinese jewellery market and by greater use of platinum in autocatalysts, say Johnson Matthey in the *Platinum 2003* report. Supplies of platinum failed to keep pace with demand, rising by less than 2% to 5.97m oz. and as a result, the deficit in the platinum market widened to 570,000 oz. last year.

Consumption of platinum in autocatalysts grew by 17% during 2002. Further growth in sales of diesel cars, rising light vehicle output, tighter emissions regulations, and greater use of platinum based catalysts (at the expense of palladium) all contributed to its higher use. But purchases of platinum by auto manufacturers increased by less than 4% to 2.61m oz. as many satisfied a significant proportion of their platinum needs from stocks.

Jewellery demand, (the other significant use for the metal) grew by 9% in 2002 to 2.83m oz. Fabrication of platinum jewellery in China climbed impressively again – demand rising by 14% to 1.48m oz.

Industrial demand for platinum increased by 2% to 1.59m oz. led by demand for platinum based catalysts from the chemical industry. Reduced investment in new manufacturing capacity caused a fall in purchases of platinum by the glass industry, while demand from electrical applications, such as computer hard disks, weakened slightly.

Net demand for platinum coins and bars from the investment sector edged lower in 2002 – with higher prices in the second half of the year depressing sales of new products.

Matthey expect platinum demand to flatten out this year.

Palladium Highlights

- Palladium demand slumped by almost 30% in 2002 to 4.78m oz., the lowest level for nine years.
- Heavy use of inventories and the effects of thrifting reduced palladium purchases by the auto industry by 39% to 3.08m oz.
- Purchases of palladium for electronics increased by 6% but remained substantially below consumption due to a further reduction of inventories.
- Demand for palladium used in dental alloys recovered by 3% – the metal's weaker price enabled palladium alloys to regain market share in the US and Japan.
- Palladium demand in the remaining other applications grew by 12%, led by higher jewellery alloy production in China and Japan.
- Supplies of palladium dropped steeply to 5.25m oz. as Russia continued to restrict sales. Despite this, the market remained in surplus and the price dropped by more than US$200 to a low of US$222.

South African supplies will rise and Russian supplies will remain stable. However, the overall increase in supply is unlikely to close the gap with demand and physical availability of the metal will remain tight. Platinum is expected to trade in the US$590– 690 range over the rest of 2003.

Palladium

After a torrid 2002 and early 2003, the price of palladium is expected to improve throughout this year as less use of inventories by both the auto and electronics industries results in net metal purchases, say Matthey.

Consumption of palladium on autocatalysts declined last year as thrifting programmes and greater use of platinum based autocatalysts took effect. In contrast, demand from the electronics sector improved as the use of inventories subsided. But substitution of palladium by nickel in the capacitor industry continued. In total, palladium demand in 2002 slumped by almost 30% to 4.78m oz.

Russian shipments of palladium fell sharply in response to the weaker market but production of the metal in all other regions expanded. As a result, the market remained oversupplied.

Autocatalyst demand for palladium slumped to 3.08m oz. in 2002, a drop of almost 40%. Demand for palladium in other applications, however, advanced by 12% to 610,000 oz.

> Palladium demand in 2002 slumped by almost 30% to 4.78 million oz. <

Production of jewellery alloys containing palladium increased, while demand for palladium-based chemical catalysts was broadly flat. Purchases of palladium for use in petroleum refining catalysts were also positive following net sales of the metal back to the market the previous year.

Supplies of palladium slid by 28% last year to 5.25m oz. as Russian shipments were cut back to levels not seen since 1990. In the face of weak demand, and in an effort to support the palladium price, Russian sales were restricted to just 1.93m oz. – less than half the 2001 total and some distance below the level of production. A significant proportion of Norilsk's palladium output was used to repay a long standing government loan and Gokhran has stated that it made no sales from the state stockpile during the year.

Shipments of palladium from South Africa, however, climbed to 2.16m oz., rising in line with growing platinum output. Palladium production in North America also increased substantially in 2002, nearing 1m oz. as expansions at Stillwater Mining and North American Palladium took effect.

Consequently, despite Russian efforts to bring supply more in line, the palladium market remained substantially in surplus. Liquidity was further increased as the US Defence National Stockpile Center (DNSC) sold more than 324,000 oz of palladium over the year.

Although US auto companies will continue to consume stockpiled palladium this year, the rate of inventory use will be substantially lower compared to last. As a result, global purchases of metal will grow significantly but will remain a long way short of the 6.75m oz. purchased in 2001, according to Matthey.

Despite the increase in purchases, consumption of palladium in autocatalysts will fall further. The effect of continuing projects to thrift palladium by auto companies will be felt this year and average loadings are expected to decrease. Programmes to replace palladium based autocatalysts with platinum based alternatives on some vehicle models, however, have largely run their course and will have little further impact on palladium demand. Indeed, given the substantial discount in the price of palladium to platinum, some auto manufacturers are already preparing to migrate a proportion of their autocatalyst systems back towards greater use of palladium.

Inventories of palladium and components in the electronics sector have largely been run down to normal working levels and stock use is not expected to affect palladium purchasing in 2003. Demand for the metal will therefore increase and should be more closely aligned with consumption. However, nickel based MLCC will take additional market share from palladium components and overall demand for palladium is likely to remain below 1m oz.

Continuing price weakness should enable palladium based dental alloys to make further small gains in market share in North America and Japan, but the combined increase in demand will be small in context of the overall palladium market. Output of palladium from South Africa will grow substantially in 2003 as the expansion of platinum mining continues.

Meanwhile, sales of Russian metal are likely to exceed last year's low. Norilsk Nickel has reported some success in signing new supply contracts with consumers, while comments from the Ministry of Finance suggest that sales of metal from government stocks may resume this year. Disposals of palladium are also continuing from the US DNSC, although as of the end of April there were less than 160,000 oz left in the stockpile.

In summary, even though demand for palladium is forecast to improve in 2003, it is likely to be once again outstripped by supply and the market will remain in surplus. Matthey expect the recent price weakness to persist, with palladium trading between $120 and $180 over the next six months ■

Guy Isherwood is Editor of *Commodities Now* magazine.
www.commodities-now.com