Precious Metals Weekly

Group Economics
Macro & Financial Markets Research

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Gold the attractive risk asset

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- **Gold is the attractive risk asset…**
- **…and it will likely continue doing so**
- **Furthermore, gold prices are relatively low**
- **However, a sharp deterioration in sentiment will likely weigh on gold**
- **Lower supply of gold will also support prices**

Gold the attractive risk asset

Intuitively, investors would say that this can't be true that gold behaves like a risk asset. In fact, gold is currently often behaving as a risk asset. Of course the pricing out of Fed rate hikes has been a clear positive for gold prices because it is an asset that doesn't pay coupon or dividend like bonds or equities. In an environment that investors need to go longer on the curve in fixed-income (especially sovereign bonds) to avoid having negative interest rates and that major central banks will likely cut interest rates further into negative territory, gold prices receive considerable support. Gold prices are in this environment attractive. The new risk-on trade appears to be long gold as most currencies and some assets are not attractive. In addition, the low gold price makes gold a relatively safe bet in comparison to other assets. However, there is one major downside to this. If investor sentiment were to deteriorate sharply (crisis or panic), it is likely that gold prices will suffer because assets with the highest liquidity are in demand. Going forward, we expect that the action by central banks will improve investor sentiment in financial markets. As a result, gold will continue to receive support as a risk-on asset. The negative relationship between gold prices and equity volatility (VIX) at times signals that gold behaves as risk-on asset.

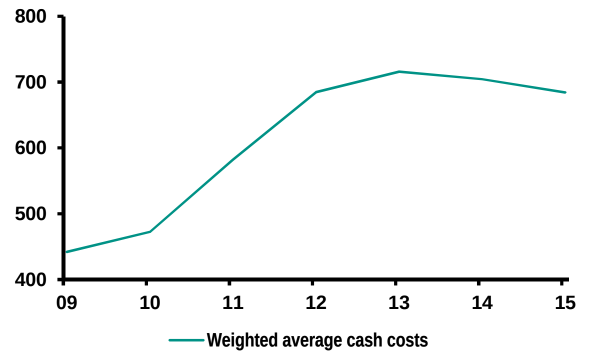
Lower gold supply will also be supportive…

Another factor to support gold prices is lower supply. In general, average cash costs to mine gold are still below the current level in gold prices. Since 2013, these costs have come down (see graph below). This is because of low oil prices and lower domestic costs because of sharp currency depreciation of countries that mine gold. The all-in sustainable cash costs have also come down but are at higher level and much closer to the current price of gold. The all-in sustainable costs also take into account royalties, taxes, overhead and other costs. The harsh conditions that miners currently face have triggered a sharp restructuring wave. This will, over time, result in lower supply of gold and other precious metals. As a result of lower supply, prices will receive support especially if demand is also picking up.

Meanwhile, market dynamics have turned positive for precious metals. We now expect higher prices this year because of more monetary policy easing, the Fed remaining on hold, less upside on the US dollar and an overall improvement in investor sentiment towards precious metals.

Weighted average cash costs

Weighted based on production



Source: Bloomberg, company reports

ABN AMRO precious metals forecasts

Changes in red/bold

End period	24-Feb	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17
Gold	1,251	*1,061*	1,200	1,225	1,250	1,300	1,300	1,300	1,300	1,300
Silver	15.5	*13.9*	15.0	15.5	16.0	16.5	17.0	17.5	18.0	18.5
Platinum	954	*894*	950	975	1,000	1,050	1,075	1,075	1,100	1,200
Palladium	496	*562*	525	550	575	600	625	650	675	700

Average	Q1 16	Q2 16	Q3 16	Q4 16	2016	Q1 17	Q2 17	Q3 17	Q4 17	2017
Gold	1,131	1,213	1,238	1,275	1,214	1,300	1,300	1,300	1,300	1,300
Silver	14.4	15.3	15.8	16.3	15.4	16.8	17.3	17.8	18.3	17.5
Platinum	922	963	988	1,025	974	1,063	1,075	1,088	1,150	1,094
Palladium	543	538	563	588	558	613	638	663	688	650

Source: ABN AMRO Group Economics

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