

ETFs Trade idea



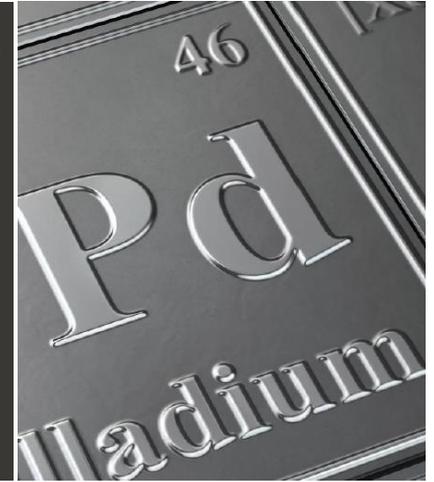
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Palladium on the move?

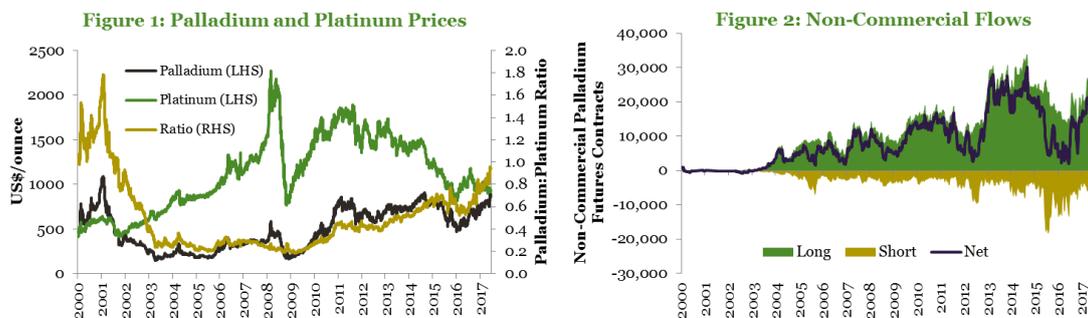
Trade idea – ETFS Physical Palladium (ETPMPD)

In this week's ETF Securities trade idea we examine the drivers behind palladium's recent price run (up 30% YTD) and look at whether it has further to go. We identify four key points to consider:

1. *Palladium's* major use is in autocatalysts used in emission reduction equipment in gasoline cars and its main suppliers are South Africa and Russia
2. Demand for gasoline vehicles is on the rise in key markets such as China and India and diesel demand is declining globally
3. Electric vehicle demand is yet to reach sufficient scale to impact *palladium* prices significantly
4. Speculative positioning in *palladium* is high, but not excessive



- *Palladium* is a metal used mainly in pollution abatement equipment. **Approximately 80% of palladium is used in autocatalysts** to reduce the emission of carbon dioxide and nitrogen oxides. There are higher loadings of *palladium* in gasoline cars than there are in diesel cars. Diesel cars have higher loadings of *platinum* (which performs a similar role to *palladium*, but is more suited to diesel engines which operate at lower temperatures). About 40% of *platinum* demand comes from autocatalysts.
- About 40% of mine supply of *palladium* comes from **South Africa** and another 40% comes from **Russia**. Historically, the Russian government had been selling its stockpiles of the metal, but there has not been any metal from this source since 2013. There is no transparent data on whether the Russian government has more stocks to sell.
- *Palladium* has **appreciated by 30.0%** in US dollar terms in 2017-to-date and, as shown in Figure 1, is approaching parity with *platinum* for the first time since 2002.



Source: Bloomberg data as at 20 June 2017

- Consumer preferences have tilted **towards gasoline vehicles away from diesel**, which accounts for much of the rise in demand for *palladium* relative to *platinum*. The automobile growth in markets like China, India and other emerging markets is a key area of strength. These are generally gasoline markets. These countries are also tightening emission standards which will increase the loading requirements of *palladium*. Established diesel markets like Europe are not seeing automobile growth on the same scale and regulatory fall-out from the emissions scandal and technological advancements have further tilted demand away from diesel.
- **Electric vehicles (EVs) are growing rapidly** from a small base. While electric vehicles account for less than 1% of global sales today, consensus estimates that it will rise to 4% by 2025. Most EVs do not contain *palladium* and so the growth of this type of vehicle will reduce a source of demand. We don't think that the growth of EVs will materially change the supply-demand balance for *palladium* in the next couple of years, but will do as the market continues to grow.
- **Speculative positioning** in the futures market is elevated, as shown in Figure 2. Net longs are above their 5 year historic average but are still well below 2013-2014 levels when concerns about mine supply were aggravated by strikes in South Africa.
- **Supply** is subject to abrupt changes. Mine closures due to strike activity, embargoes of exports from certain countries and recycling dependency on other metals are some of the examples of factors that cause supply disruptions. While changes in **demand** can be quite surprising, as we have seen with the rotation toward *palladium* (gasoline engines) from *platinum* (diesel engines) in light of the emission scandal, generally changes in demand are more gradual.
- Investors wishing to add *palladium* exposure to their portfolios may consider using **ETFS Physical Palladium (ASX Code: ETPMPD)**, the only ETP in Australia providing investors with physical exposure to the metal. *ETPMPD* offers holders a direct entitlement to *palladium* vaulted at HSBC in Switzerland with a management fee of 0.49% per annum.

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