

TALK TO AN EXPERT: Jeffrey Christian Makes The Case For Precious Metals



Jeffrey Christian

Jeffrey Christian is the Managing Director and founder of CPM Group, a leading commodities market research, consulting, asset management, and investment-banking firm. Widely considered the world's foremost authority on the markets for precious metals, Mr. Christian is also a respected authority on copper, foreign exchange markets, and other commodities. Among his publications is the definitive book on commodities and trading, "Commodities Rising".

Global Resource Reference: You used to be a journalist. What questions does the journalist in you ask about this market upset? Who were the important players in the problem and who will be a part of the solution?

Jeffrey Christian: That's a tough question. The fact of the matter is governments around the world are rolling out infrastructure projects. China and the U.S. have been the most prominent, but India has announced them, as have the European Union, Britain, Russia. All those projects are going to take steel, concrete, copper, a lot of them are going to take aluminum. I think you can't really necessarily say it's down to one or two big players because one of the things we're seeing over the last six or eight years is a reduction—however small—in the hegemony of the United States' economy. It's still the prime mover in the world economy but it has lost mar-

ket share, and the decisions of a lot of other people are more important than they used to be.

Also, I think the governments of the world have learned a lot from the last great depression, and so they're being much more forceful, which means we should avoid the worst conditions we saw in the period from the 1870s to the 1930s.

We'll see where this new US government takes us. I like what they're saying so far about spending on infrastructure and jobs. I'm a little upset that Congress is insisting on tax cuts as part of this program because that's a really ineffective way to use government borrowed money to rebuild the economy. Infrastructure projects, schools, rebuilding bridges and building light rail transit would be a much better investment of the government's money.

GRR: Are you short or long on commodities and equities right now?

JC: We have many clients who have an enormous portion of their assets under management in cash and they're waiting to reinvest. The recovery could be relatively fast and fierce, just like the decline was: You could have a v-shaped selloff and recovery if a lot of this money gets redeployed. Some of this will start to reappear in the second quarter, but I think most will wait until the second half of 2009 and maybe even early 2010.

Platinum:

GRR: The near death experience of the big three automakers in America has become a problem for the platinum sector. Auto demand is at lows not seen in decades. And yet production of platinum is also down, with mines shutting and putting upward pressure on price. Can you clarify some of the mess for us?

JC: Our view is that the market probably will be in a large surplus this year, and then maybe it will start to contract next year as the auto industry recovers. There are two long term trends to watch. One is that auto sales on a global basis have been rising sharply until 2008 and probably will resume growing at a relatively sharp rate once the recession is behind us. On a worldwide basis the auto industry will continue to be a strong source of demand for platinum

group metals. In the US, the auto market is kind of saturated, so it remains to be seen what's going to happen. Virtually every driving age adult is accommodated with a vehicle, so the US actually could see its auto markets downshifted to a much lower sustained basis. That's probably not going to happen because there's so much economic incentive on the part of just about everybody to have people buying cars. So I think there will be a recovery in the US, but what you have to watch for is that US consumers could buy far fewer cars in the future than they have in the recent past even as the global auto market expands.

GRR: What is your outlook for platinum in 2009?

JC: We expect the price of platinum to be relatively low this year, maybe \$950 on an annual average basis, and then next year we could see a relatively healthy rebound. We wouldn't be surprised to see \$1,300 next year.

GRR: Platinum Exchange traded funds were a new offering last year. Do these investment funds affect the market in terms of dumping product as ETFs try to recoup some cash flow?

JC: Yes. One of the things we've seen on the exchange traded funds was this massive build-up in demand for platinum for the ETFs where they went from 50,000 ounces in late 2007 to around 500,000 ounces in July and then they sold off and came to about 250,000 ounces. So they sold about half of their platinum. So the platinum ETF has been much more volatile compared to palladium, gold or silver where a lot of ETF investors have been buying ETFs and not selling.

GRR: Are you keeping track of which mines are going on care and maintenance?

JC: North American Palladium and Stillwater are the most significant guys who have gone on care and maintenance. We've also see some cutbacks in South Africa, and you have seen a reduction in palladium production in Norilsk, which is probably going to continue for at least a couple more years.

GRR: North American Palladium is an interesting one to look at because going on care and maintenance at Lac des Iles hasn't

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really affected their share price as much as one may have thought.

JC: I think it's a combination of things. First of all, their share price already was hammered pretty low. Also, they didn't have a lot of speculative short term institutional investors in there the way some other mining stocks did, so they didn't suffer from deleveraging. Also, just before they went on care and maintenance, they brought in this new fellow, Bill Biggar coming out of Barrick (TSX, NYSE:ABX), and he knows what he's doing. One of the first things he did was to put the mine on care and maintenance, and state the need to preserve cash and think carefully about the company's future. So I think people look at the company and say here's a company that's got new, good management, smart guys, that's taken the right steps at the right time, that has cash, and that has an attractive mine that will come back on stream at the right time...plus the fact that it's got George Kaiser [Ed: Net worth \$12 billion last year] as its major shareholder, means this could be one of the more interesting mining vehicles going forward.

GRR: Say I'm a stock broker, looking to invest in Platinum, and to guide my clients. What would you counsel me to do right now?

JC: One of the things we're seeing is people buying the ETF because it's a way to get at the physical platinum. One of the reasons why they were interested in the physical metal is because they saw the South African mining companies as having problems, as well as the North American producers. Then the ETFs came along and they found that here was a very easy way to buy. So a lot of people are looking at the ETFs still as a way to buy platinum and palladium. For a lot of our clients that does make sense. Personally I go into physical platinum be-

cause I will do futures for them on a short term basis. But the ETFs are probably the most attractive approach.

Palladium:

GRR: What impact is changing demand having on the fundamentals for palladium?

JC: Well, right now what you've got is you've had a big decline in price because of fabricators pulling back. Part of that has to do with the increased importance that the auto industry plays, but the electronics industry has also been hammered pretty hard, and was hammered with a lag relative to auto demand. So what you're seeing now is some build up in palladium inventories. Investors have caught on and they're getting away from the palladium market. Our view is that the palladium market might have a little more downside, but from the perspective of a year or two from now,

it's probably very attractive.

GRR: From close to 600 dollars per ounce to almost 200 per ounce. There must be some good opportunities right now in terms of palladium investments.

JC: I agree. We've made the point to our clients who are institutional investors that the entire platinum group complex is an attractive place for investment. You know, ruthenium, iridium and rhodium are very difficult to invest in, so we don't advise them on those unless they hire us to manage their positions for them. I think the entire platinum metals complex from the perspective of two or three years out is probably extremely attractive.

GRR: If I'm not mistaken, Russia controls the majority of world supply. What does that mean for North American explorers and producers?

JC: It doesn't really scare or concern me. There's a lot of people worrying that the Russian government has large inventories

of palladium. I don't believe that their inventories are that large, and I don't believe that they have been the seller in recent selloffs. We haven't seen the government in Russia sell from its stockpile since around 2001 and we don't think that we will, so we're not concerned about that. We've been telling people that we're more concerned about the fact that you have even more metal now in the hands of institutional investors and high net worth individual investors, and those guys would be more inclined to sell their inventories than the Russian government.

Gold & Silver:

GRR: You told me last year: "The fact that the financial markets are so much larger than the gold market means that even small changes in investor attitudes toward gold have this dramatic effect in the price of gold." There must be a lot at play here, because investors on one hand have been spooked out of a lot of investments, and yet gold is often perceived as a safe haven. Are the two nullifying each other to some extent and keeping the price of gold buoyant?

JC: They are to some extent. First off, since we spoke a year ago gold went up to a record price and then came back down. But if you look at gold in euro terms it's still very close to its March peak. One of the things that you're seeing is that gold prices have held up much better than industrial commodities. That makes sense, because gold is not an industrial commodity—it's a financial asset. You have seen enormous buying of gold worldwide. The other thing that you saw starting in September was this massive liquidation of leveraged gold positions—futures, options, gold-linked notes written by banks—and that is what caused the price of gold to fall as much as it has over the last six months. But that's a temporary thing. The physical market will always ultimately trump the paper market.

GRR: You believe that demand is the major determining factor of gold price. Where is demand at today?

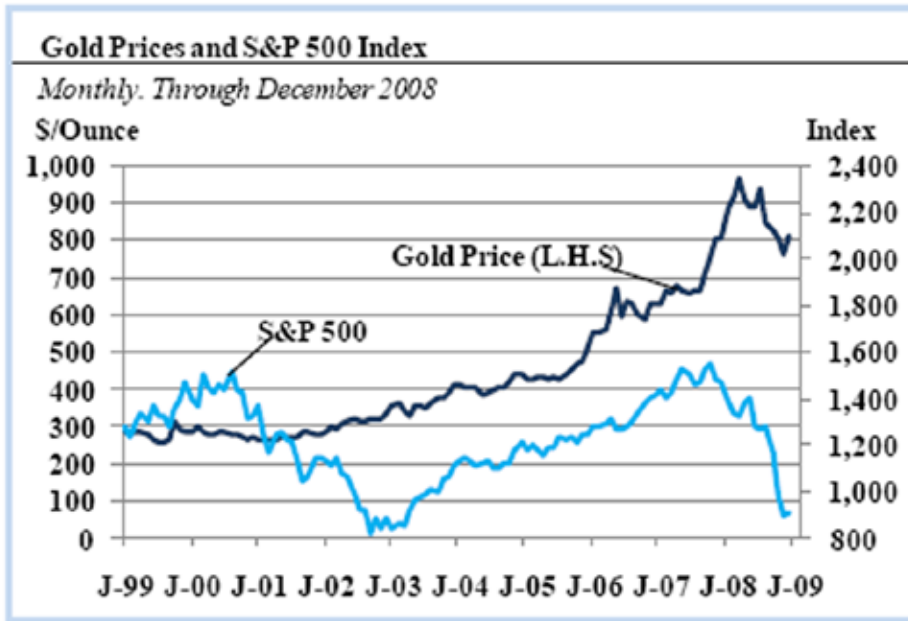
JC: The key demand thing to look at is the investment demand, and we have seen very strong investment demand for seven years, which continued in 2008. We're working right now to come up with our figures for

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how much demand did in fact rise or fall in 2008 from 2007 levels. There are indications that it may have been somewhat lower last year than in 2007. Regardless, gold demand from investors was at very high levels and in the third quarter it was at historic-

ter, as you say, and demand is the same or growing, don't we see—

JC: —a higher price. Yes. Mine production is only a part of supply, and another thing that you're seeing on the supply side is in-



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ally high levels. I mean, we probably saw unprecedented levels of gold demand from investors around the world in 2008.

GRR: You have also said that mines will continue to produce in spite of price changes, except in extreme cases. Is today an extreme case?

JC: We're in the process of reviewing our supply/demand figures and coming out with our Gold Yearbook for 2009. One of the things that we have been saying for a couple years now is we thought that mine production would continue to expand over the next ten years. But over the next five years you might see flat, maybe lower, or very small increases in mine production because of a couple things. One is the financial freeze up. The economic crisis that hit us over the past year has been much more destructive of supply and the pipeline of future supply than it has been of demand. There are some very interesting projects that will still come on-stream, but there are a number of others that are being delayed or deferred indefinitely... partly because of lack of financing; partly because of volatility in gold prices.

GRR: But if supply is slashed by a quar-

creased scrap recovery because people are selling their old jewellery because of high prices. But the other thing you're seeing that's bullish is central banks selling less gold than they used to, and that's probably a long term thing that's going to continue. The gold market has been absorbing about 14 or 15 million ounces of gold per year from central bank sales for the last 20 years, and that's probably behind us now. Central banks have sold the gold they wanted to. They still have about 970 million ounces in their coffers, but they're showing increased interest in keeping what they've got.

GRR: And this means that there are some very good investment deals out there. Particularly as small companies merge or are swallowed up.

JC: I agree, yes. And that's one of the things you're going to see. You're going to see some consolidation, some people who cannot hang on, and you will see the stronger companies will buy out the weaker companies.

GRR: There was a lot of excitement as gold pushed through \$1,000 per ounce last year. Will we see that again in the next 12 months?

JC: I wouldn't be surprised to see it. It would have to be pushed by investor fears. If you have continued problems in the economic environment, say GM comes along in March and says, "We've spent your \$10 billion and we still don't have a viable plan to go forward," and Citibank is breaking up, corporations are having further problems, and final demand across the economy is not recovering, you could see another wave of investor fears that could easily drive the gold price higher.

GRR: Unlike gold, silver has had a humbling year as it wrestled with \$20 per ounce only to be pushed back down to the \$10 to \$12 range. What factors have pushed silver to its present price?

JC: Silver demand was rising very strongly in addition to investment demand. As we saw in gold you also had industrial demand for silver rising strongly. Then the economic slowdown hit the industrial demand and institutional investors were deleveraging again in the paper markets. Also, silver's a much smaller market than gold, so its price tends to be more volatile as a result of its lower liquidity.

I have this game that I play with producers and consumers of silver. I ask them what they think the average price of silver was last year. The answer is \$14.97 per ounce. But very few people think that. Most people guess \$11 or \$12. So, there's an under appreciation of the strength that silver prices exhibited last year. And there's an under appreciation of where the price today is.

GRR: So what sort of a year can we look forward to for silver?

JC: A pretty volatile year still. I wouldn't be surprised to see the price rise. We wouldn't be surprised to see the price at \$13, \$15, maybe even \$18 or \$20 at some point on a spike in the first half of this year, and then it will probably come and we're thinking when it comes off it might come down to \$11 or \$12 per ounce, maybe not even that low, because the silver market's still fundamentally tight. It's a much smaller market, less liquid than gold, it doesn't have the inventories lying around that the gold market has. **GRR**