



## Myths and Realities, Surpluses and Deficits in Platinum and Palladium

by Paul Walker, CEO, GFMS

A week is a long time in the commodity markets these days. Six months is an eternity. It was only at the beginning of this year, as the power crisis and new safety regimes put strains on platinum production in South Africa, that some analysts were talking of half a million ounce deficits in that market. How circumstances have changed in the interim.

Firstly, South African production has turned out not to have been as dramatically affected by the power crisis as some had predicted (partially due to the fact that with

the lowest wholesale prices for electricity in the world, power was not necessarily being used that efficiently). Secondly, there have been marked demand side effects of higher prices, not least of all in the jewellery sector, where net demand has fallen sharply this year. But where will this leave the fundamental balances for platinum in 2008?

GFMS forecast that for the calendar year 2008, platinum will see a fundamental surplus of anything up to 150,000 ounces, and given the state of the global economy, one has to concede that the risks lie on the

downside (i.e. the surplus will get bigger). The move from deficit to surplus matters for platinum when viewed in the context of the above-ground stocks of the metal – at the beginning of this year, near market stocks of platinum in Zurich stood at less than 1.5 million ounces, much of this allocated into the ETF. Clearly, half a million ounce deficits with moderate stocks would have had an explosive price effect, and indeed, the price action in the first few months of the year indicated the market's belief that this would be unsustainable.

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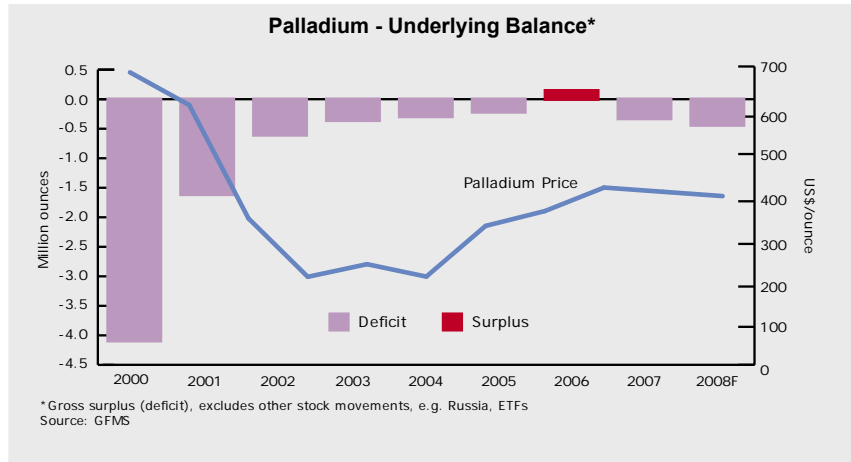
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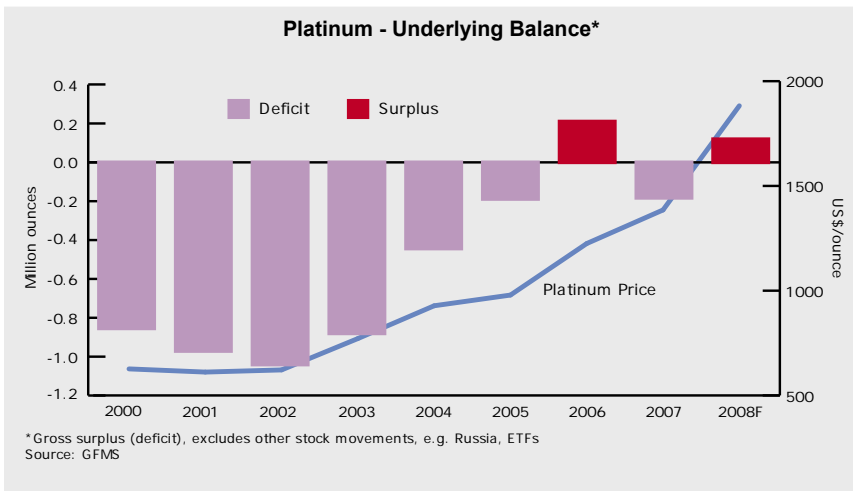
At this juncture it is worthwhile highlighting an important methodological point. GFMS analyse the PGM markets in manner that would be familiar to most base metals analysts. This involves looking at all of the supply and demand flows (mine production and scrap compared to actual use of the metal in fabricated products) and seeing whether this implies that above-ground stocks of the metal are required to meet real fabrication demand (a deficit), or that stocks have been added to (a surplus). The reason for platinum's price action over the past few years has been persistent underlying deficits in this market that has resulted in an ongoing run down of stocks. So what about palladium?



between platinum and palladium? It's all in the stocks, stupid!

GFMS estimate that at the beginning of 2008, palladium above-ground stocks were sufficient to cover 10 months demand, and it is this factor, not any underlying surplus,

more importantly, what about future trends in palladium? Our view is that deficits are likely to persist into the future, so the key to answering this depends on how above-ground stocks are mobilised. Who owns it (in particular the loco-Zurich stocks), what was their average acquisition price, what's their reservation price, and will the Russians continue to sell from stocks?



Interestingly, the perceived wisdom in many quarters is that palladium is, in a fundamental sense, in surplus. For the record, GFMS data show that this is simply not true – echoing the title of this piece, therein lies the myth. As the accompanying graph shows, when the flows in the palladium market are correctly analysed, excluding flows from stocks, it becomes clear that with the exception of one year, since 1999 this market has been in deficit and at times very substantial ones too. So why such different price action

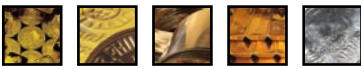
that explains why the prices of the metals have diverged so. To reinforce the point, when stock related movements are removed, palladium's underlying situation is not that dissimilar to platinum's, with many years of gross deficit.

So what about this year? GFMS believe that palladium will likely be in modest deficit this year, although as with platinum, the risks are that demand attrition due to a slowing global economy will see the market move towards balance. And perhaps



Dr Paul Walker is the Chief Executive Officer of GFMS, in addition to being responsible for gold, silver and PGM research

in East Asia, India and South Africa. He joined the company in 1995. After graduating with degrees in commerce and economics from the University of Cape Town, Paul worked as an economics researcher for a Member of Parliament in the UK House of Commons before joining the United Nations affiliated International Lead and Zinc Study Group, where he was involved in a wide range of economic studies and forecasts. He has a PhD in the application of mathematical optimization to large non-linear economic systems from the University of Nottingham in the UK.



## NEW AT GFMS

### GFMS Metals Consulting Will Release New Three Year Forecasting Service for the Base Metals

**GFMS Metals Consulting has launched a series of Quarterly Reports on the individual base metals that will analyse the prospects for the next three years. The first report on the copper market was published in July and will be shortly followed by similar forecasting services on the nickel (October), aluminium (November) and lead and zinc in December.**

We believe that a three-year time horizon is an ideal time frame in which to provide a realistic assessment of the prospects for the base metals industry. Beyond this

period, an ever-increasing number of assumptions have to be made about the timing of new projects, changes in the level of production costs, the likely economic and demand environment, fluctuations in the value of the major currencies etc. The Quarterly Forecasting Reports from GFMS Metals Consulting build on the success of the Base Metals Market Briefing, which provides regular analysis on the base metal markets. These new research reports are the most comprehensive and cost effective source of analysis on the medium-term prospects for individual base metals.

The new forecasting services

complement the services on the gold, silver and platinum group metals that are produced by GFMS. To get more information on these products contact:  
info@gfms-metalsconsulting.com.

**If you would like to purchase Quarterly Reports please contact Charles de Meester at [charles.demeester@gfms.co.uk](mailto:charles.demeester@gfms.co.uk) or [sales@gfms.co.uk](mailto:sales@gfms.co.uk)**

### GFMS Appoints Metals Analyst



Kirill Kirilenko joined GFMS on September 2008. He primarily works with Peter Ryan on Platinum and Palladium demand and assists Philip Klapwijk on investment activity research. Kirill holds a BSc in Finance and Banking from the St. Petersburg State University for Engineering and Economics – ENGECON, and PhD in Economics from the same university. Prior to GFMS, Kirill worked as a Market Research Analyst for a number of companies based both in the UK and Russia, including the precious metals refiner Johnson Matthey Plc.

### Internal Changes at GFMS



Nikos Kavalis, Senior Analyst with GFMS, who joined in September 2003 and has since worked in precious metals primarily assisting Philip Klapwijk on investment and official sector activity research, has moved to GFMS Metals Consulting, also part of the GFMS Group, to cover research in base metals.



# NEWS FROM THE FIELD

GFMS are unique in terms of time and effort spent on research worldwide. This new section "News From The Field" has been included in the Newsletter in order to provide you with the latest updates and news from the GFMS' precious metals research trips.

## Indonesian Jewellery Consumption Boosted by Rural Demand

by Cameron Alexander, Senior Analyst, GFMS

The health of Indonesia's jewellery fabrication industry, like that of countries in the South East Asian region, has suffered significantly in recent years as the gold price rally, inflationary pressures, and political uncertainty have fuelled a slowdown in jewellery consumption. However, in recent months there have been some positive signs for the besieged industry, providing some optimism for traders that they can ride out the high price environment to hopefully benefit when gold prices finally retreat. A recent field trip by Australia based GFMS analyst, Cameron Alexander, investigated the difficulties and modest successes the Indonesian fabricators are currently experiencing, and looked at the impact the price has had on the local markets.

To put the impact of the price rally on the local industry into perspective it is worth considering the significant decline recorded in Indonesian gold jewellery fabrication this decade. In 2001 for example, fabrication in fine gold terms reached almost 106 tonnes, while last year fabrication had slumped 41% or 43 tonnes from this point to below 63 tonnes. This rapid decline has been driven by several factors. Firstly, local jewellery consumption has fallen, with price the major culprit, though

a modernising economy has also seen consumer funds directed into household and personal electronics (mobile phones, for example). Secondly, the softening of export demand from the Middle East, easily Indonesia's largest jewellery export market, has also resulted in a downturn in fabrication volumes; while finally, an ongoing migration to low carat jewellery has resulted in a lower offtake of fine gold, as fabricators have increased the market share of both 9 and 10-carat jewellery in recent years.

Looking at 2008, fabrication volumes have again been hit hard as gold prices continued to surge with the local price peaking at over 300,000 rupiah per gramme in the first quarter. Further reductions in export demand as price sensitive Middle Eastern markets retracted added to the pain, with fabrication levels slipping a further 13% year-on-year in the first quarter and "just" 1% in the second quarter. Importantly, jewellery consumption, while weaker in the first three months, showed some resilience in the second quarter increasing by 6% year-on-year and recent research suggests consumption volumes have recorded modest gains in the third quarter as the severe price correction witnessed in September provided the impetus

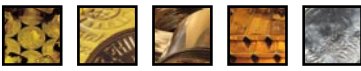
for an uptick in demand. This has been particularly beneficial to traders selling prior to the Islamic Ramadan period, which for many traders is normally the busiest time of the year.

While domestic sales have remained moribund in the larger cities where consumers on fixed incomes have felt the impact of rising food and energy costs, demand in rural areas has been boosted by higher commodity and agricultural prices, with higher earnings in these regions flowing through to a rise in jewellery sales. Moreover, robust sales have been reported in Kalimantan, Sumatra and across regional Java. The recent price rally back over \$900 is likely to again test consumption volumes, with recent reports from local Indonesian traders suggesting demand has fallen sharply in the last fortnight.



Cameron Alexander is an Australia based Analyst with GFMS and is responsible for research in South-east Asia, Australasia and the Gulf States in the

Middle East. Prior to his joining GFMS in December 2005, Cameron worked for over seven years with precious metals refiner AGR Matthey.



# PUBLICATIONS AND PRODUCTS

## GFMS Quarterly Three Year Gold Forecast - October 2008 Issue

**Against the backdrop of an escalating financial crisis, one of the key questions for the gold market, going forward, is what role will gold investment play? Will we see a sustained return of investment demand, which was so instrumental in gold realising its first quarter record? If so, will this be sufficient to see prices post new highs?**

**This is one of the central issues that will be addressed in the next edition of the *GFMS Quarterly 3-Year Gold Forecast*, which will be released on 17th October 2008.**

**The *GFMS Quarterly 3-Year Gold Forecast* will feature GFMS' expectations for the major supply and demand fundamentals as well as forecasts for the gold price under three different economic scenarios.**

Published four times a year, this report gives GFMS' independent insight into the latest developments and trends and offers a 3-Year forecast on supply, demand and the price for gold.

This report is the result of rigorous analysis of key market dynamics such as fabrication demand, mine production (feeding off GFMS' proprietary mines database), investor trends, exchange and speculator (hedge fund) activity, producer hedging, central bank activities, and macro economic factors including GDP growth, interest and exchange rates.

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### Scenarios

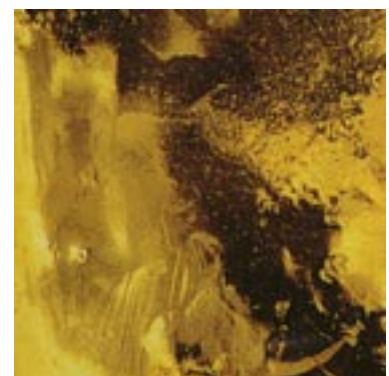
The forecast is provided under three alternative scenarios for the world economy: The Base Case scenario represents GFMS' expectations of global economic growth, energy prices and exchange rates over the forecasting period, while the

Low GDP and High GDP variants provide alternatives based on more pessimistic and more optimistic outlooks for the world economy respectively.

### Availability and Annual Fee

The Quarterly 3-Year Gold Forecast is available for an annual fee of £5,450 or can be purchased in a package along with the Quarterly 3-Year Silver and Platinum and Palladium Forecasts for £9,950 pa.

**For further information please contact Charles de Meester at [charles.demeester@gfms.co.uk](mailto:charles.demeester@gfms.co.uk) or [sales@gfms.co.uk](mailto:sales@gfms.co.uk)**





## Gold Survey 2008 - Update 1 Released on 17th September

**GFMS Gold Survey 2008 - Update 1** was released on 17th September in London during the 5th GFMS Precious & Base Metals Seminar. The launch took place at Trinity House, London with a total of 110 delegates attending. The presentation was given by GFMS' Chairman, Philip Klapwijk, who revealed the most recent developments in the gold market and provided a thorough and comprehensive interim analysis of these changes. The conclusions were published in various leading media sources, including the Financial Times, Thomson Reuters, Dow Jones Newswires, Les Echos, etc.

**Gold Survey - Update 1** is a comprehensive report, which just in 40 pages, identifies the most important economic, sociopolitical and market-specific issues facing the gold market.

Gold Survey - Update 1 provides data and commentary on the essential supply and demand fundamentals, comments on how they shaped the market in the first half of the year and how they could do so moving forward.



### Main features

- Supply and demand statistics for the first half of the year and second half forecasts.
- Review of main developments in mine production, costs, hedging, scrap supply, fabrication, investment and central bank activity.
- Commentary on price movements and indications on what to expect looking forward.



Please contact Elena Patimova to purchase or to find out more information about Gold Survey 2008 - Update 1. The publication is available both as a hardcopy and an electronic version.

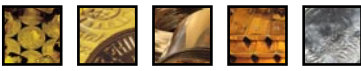
Email: [elena.patimova@gfms.co.uk](mailto:elena.patimova@gfms.co.uk) or phone + 44 (0) 20 7478 1750\*

Online: <http://shop.gfms.co.uk>

\* Omit (0) when dialling from outside the United Kingdom.

**Gold Survey 2008 - Update 1** can be ordered individually or as part of the following "discounted packages":

- Gold Package
- Precious Metals Package
- Precious Metals Package Plus



# EVENTS

## GFMS Precious & Base Metals Seminar - The Highlights

London, 17<sup>th</sup> September 2008

GFMS and sister company GFMS Metals Consulting held their 5<sup>th</sup> Precious & Base Metals Seminar in London on 17<sup>th</sup> September. This GFMS seminar is unique as it assesses the prospects for all the precious and base metals in a special one-day event. The seminar looked at specific issues that are affecting the individual markets as well as general factors that have impacted the entire metals sector. International experts in the area, including representatives from the Venezuelan and Philippines central banks, joined GFMS' in-house analysts in these presentations.

### Precious Metals Session

A highly informed and engaging range of speakers gave the precious metals presentations at the seminar.

**Philip Klapwijk**, GFMS' Executive Chairman, presented the latest findings from Gold Survey 2008 - Update 1, which was launched at the seminar. A detailed account of global gold supply and demand, both during the first half of this year and the outlook for the final six months, can be found in the report. In addition, Philip discussed the outlook for gold prices, in the light of the recent commodity sell-off. Philip pointed out that GFMS expected the gold price to rally further during the fourth quarter on the back of investors flooding back into the market, largely on the basis gold being regarded as a safe haven from ongoing financial turmoil. In essence, gold's monetary attributes were expected to trump its commodity ones, with the yellow metal therefore forecast to outperform by some margin other commodities.

The **Gold Survey 2008 – Update 1** presentation was followed by a speech from **Eli Sanchez**, Head of the Gold Department of the **Venezuelan Central Bank (BCV)**. In his presentation "The Role of Venezuelan Central Bank in the Domestic Gold Market", he highlighted that the BCV continues to maintain substantial gold reserves, which can be augmented by purchases in the domestic market from local producers. Mr Sanchez also stated that the BCV is considering a range of alternative initiatives to increase its participation in the domestic market, including the possible development of gold financial products.

**Maria Ramona Gertrudes Santiago** of the **Philippines Central Bank** started her presentation "Gold and Reserves Management at the Philippines Central Bank" saying that the Philippines is ranked among the world's top-20 gold producing countries. For the last five years, local gold production, currently carried out at eight mines, has been measured in the range of 35 to 39 tonnes per year. About 80% of the metal output is being produced by small scale miners and sold to the Philippines Central Bank. In recent years, the majority of gold produced has been exported, mainly to Hong Kong.

In his presentation, "Oil price: Speculative Bubble or Structural Shift", **Mark Lewis** of **Energy Market Consultants** provided some insights into the oil market. The presentation began with a brief review of the oil demand / supply trend in the past, citing the importance of fundamentals on the

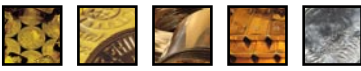
oil price. However, the rising oil price in the first half of 2008 and the recent price slide were driven by more sentiment than fundamentals. Mr Lewis concluded that the oil market was going through a period of major change, being driven by a number of factors, such as demand growth drivers moving to emerging economies, supply drivers shifting to national oil companies and reduced "market management" from OPEC.

**Philip Newman** of **GFMS**, discussed "The Impact of Metal Prices on Jewellery Demand". Given the recent historic price highs in the gold market, the presentation compared the response of western-style and traditionally price sensitive markets to this development. In this regard, it was noteworthy to see an adverse reaction in many western markets, but largely initiated by the retail trade, who looked to reduce their use of gold, in an attempt to limit retail price increases. Jewellery demand in the price sensitive countries has also been hit, but here the response has primarily come directly from consumers. Mr Newman also discussed the impact of prices in the silver and PGM jewellery markets, details of which can be found in the main presentation, available on GFMS' website.

**Paul Walker** of **GFMS** presented the paper entitled "Platinum and Palladium Deficits and Surpluses – Past, Present and Future". (A summary of Paul's paper is provided at the beginning of this Newsletter).

**Paul Burton**, Managing Director of **GFMS World Gold**, gave a paper entitled "Investing in the Gold Sector: Bullion or Barrick?". He noted in his presentation





## China Mining Congress & Expo 2008: Join in Celebrating the 10<sup>th</sup> Anniversary



**GFMS agreed to participate as a media partner of the China Mining Congress & Expo 2008 that will be held at Beijing International Convention Center on 11<sup>th</sup> - 13<sup>th</sup> November 2008.**

China Mining Congress is hosted by the Ministry of Land & Resources, China and supported by domestic & international governments, associations as well as organizations including the World Bank Group, the China Mining Association, the Australian Embassy and the Canadian Embassy.

As one of the world's top four mining events and the biggest Asian platform for mining exploration and exploitation, the event provides an important channel for communication and exchanging information among global mining enterprises, while

building relationships.

After a very successful event last year, China Mining Congress & Expo is now approaching its 10th anniversary. More than 3000 registered delegates, 300 exhibitors and 30 sponsors from 45 countries and regions participated in last year's China Mining Congress & Expo. With a larger exhibition space and more conference streams we are expecting even more attendees of the world wide mining community to celebrate the 10th anniversary of China Mining Congress & Expo in this year.

China Mining Expo has been held successfully for the past four years, with China Mining Congress held at the same time also welcoming its 10th anniversary ceremony. Conferences, exhibitions and featured events, as the three core

content of China Mining Congress & Expo, are contributed to greater world appeal and influence of China Mining Congress & Expo with its emerging distinctive manner. China Mining Congress & Expo not only collects tremendous information stream, capital stream and technology stream, but also provide a convenient channel for domestic and international mining companies for a purpose of economic and trading cooperation and communication between China and the world.

China Mining Congress & Expo has grown to be a matured community of gathering East Asia and international professionals in the mining sector. However, China Mining Congress & Expo will continue to impel the constant development of global mining economy with its cohesive effect and core impact. We confidently believe that China Mining Congress & Expo 2008 is going to build a wider stage for a better dialogue communication and cooperation opportunity for governments, enterprises and all circles from each country.

**For more information about China Mining Congress & Expo 2008, please visit the website: [www.mining-expo.com/en](http://www.mining-expo.com/en) or [www.china-mining.com](http://www.china-mining.com).**



# MARKET COMMENTARY

## Futures Volumes Rocket as the Financial Sector Struggles

by Rhona O'Connell, Managing Director, GFMS Analytics

The gold and silver price falls slithered to a halt on 11th September after 8½ weeks in which gold shed 25% and silver gave up 45%. The falls were slightly more prolonged in the PGM sector, with platinum and palladium bottoming on 17th September, having fallen by 47% and 51% respectively.

With the spiralling tensions in the financial markets, trading in the metals markets in the second half of September has been extremely choppy as all eyes have been on the consternation in Washington as the debate rages over the content of a bail out programme. Trading volumes in the New York futures metals contracts soared on 17th and 18th September as the news broke of the imminent rescue of insurance giant AIG and it was on the 17th that gold started pouring into the Exchange Traded Funds, particularly the SPDR® Gold Shares in New York, which added 111 tonnes in one week. While the average gold trading volume on COMEX from the July downturn had averaged 540 tonnes daily, the turnover on the 17th and 18th of September was an average of 1,055 tonnes, the highest since the 22nd of January this year, when the equity markets were under pressure and Federal Reserve cut the fed funds target rate by 75 basis points.

The significance of the problems at AIG in particular rested on the fact that as it was a triple-A rated insurer, virtually every financial market participants including some central banks had exposure to AIG products in one form or another. As such it fell firmly into the category of "too big to fail".

After falling as a result of both a flight from commodities as well as being sold through distress, gold has turned higher in response to "safe haven" buying, and silver has shown some price strength on gold's coat tails. Platinum and palladium have also taken a few tentative steps on an upward path, but the spectre of a faltering automotive industry and doubts over the prospects for jewellery purchases have rendered the recovery in these metals rather more subdued.



*Rhona O'Connell is a recognised authority in the metals markets with over 20 years' experience as an analyst in the metals*

*sector. Rhona is the managing director of GFMS Analytics and ROC Consultancy an independent consultancy specialising in metals markets analysis and comment. The specialist areas constitute gold silver platinum and palladium looking at the markets themselves in the context of the economic political and financial environments while considering also the performance of other asset classes and related mining activities.*



## Investing in the Gold Sector: Bullion or Barrick?

by Paul Burton, Managing Director, GFMS World Gold

Gold stocks are generally considered to be leveraged to the gold price based on the notion that a gold share is an option on a higher gold price, but do they perform better than the metal in practice?

### 3-year findings

Barry Cooper of CIBC World Markets recently completed an analysis, using normalised share prices, which shows that between two points in time (Q1.05 and Q2.08) gold has grown more than Barrick Gold. The interrelationship has not been constant throughout the period as sometimes Barrick has outperformed gold price and other times it has lagged considerably.

Overall, gold increased at an annualised percentage of 23%, whereas Barrick increased by 19%, with an underlying correlation of 97% between the two.

Another major, NYSE-listed Newmont Mining, for the first half of the period

showed far superior returns to the gold price (and Barrick), but since Q3.06 it has been a much weaker performer.

### 10-year findings

The following table shows the performance of gold and the XAU

INDEX	1 SEPT 98	1 SEPT 08	
<b>GOLD (US\$/oz)</b>	<b>279</b>	<b>822</b>	<b>+ 195%</b>
XAU	51	139	+ 173%
BARRICK	20.55	35.00	+ 70%
NEWMONT	14.31	42.93	+ 200%

stock index as well as the two largest gold producers over the 10-year period commencing 1<sup>st</sup> September 1998.

While gold has posted an impressive 195% rise in ten years, the XAU has grown slightly less, by 173%. However, once again Barrick has underperformed the gold price, this time substantially.

### Conclusions

In the 1990s it was common wisdom that investors bought gold shares for their optionality on a gold price rise. However, the empirical evidence of the last three and ten year periods, based on the XAU and the individual performance of Barrick Gold and

Newmont Mining, shows that the relationship has changed and gold stocks often underperform the gold price.

The reasons for the loss of the gearing effect are perhaps how the market perceives the production growth prospects for specific gold companies and the impact of hedging strategies.

#### GFMS World Gold publications and services:

- The subscription-only quarterly, World Gold Analyst, has proved to be an indispensable tool for busy mining executives, analysts, investment bankers and private and institutional investors around the world for over 50 years.
- An occasional series of investment reports into gold exploration and development in specific regions of the world.
- We also undertake independent research into companies producing or exploring for precious metals worldwide.

**World Gold Analyst is a subscription-only publication. Annual subscription rates are £375 (US\$750) for the combined hardcopy and PDF and £245 (US\$490) for the PDF alone.**

For more details or to request an invoice, please contact Elena Patimova at [elena.patimova@gfmsworldgold.com](mailto:elena.patimova@gfmsworldgold.com) or +44 (0)20 7478 1777.



**Paul Burton** graduated as a mining engineer from the Camorne School of Mines in 1988 and spent almost twenty years working in the South African gold mining industry. He has been editor of World Gold Analyst since early in 2008. He is an established speaker on the international conference scene and is Chairman of the FTSE Gold Mines and Committee. He holds an MSc in Mineral Economics and an MBA from the University of the Witwatersrand. Recently Paul Burton took the position of Managing Director of newly established GFMS sister company - GFMS World Gold.



## Zinc – a Sign of Things to Come in the Base Metals?

by Neil Buxton, Managing Director, GFMS Metals Consulting

Zinc prices were the first to peak and the first to decline in this bull market. In early October, the LME cash quote was around \$1,550/tonne compared to the bull market peak of \$4,620/tonne in November 2006. The massive decline in prices has come about despite only a relatively modest deterioration in the visible fundamentals. For example, zinc inventories are still only around 160,000 tonnes compared to 700,000 tonnes earlier in the decade after the end of the "dot.com" boom. July ILZSG data shows a surplus of around 77,000 tonnes over the first seven months. Driving this increase is the 9.9% rise in mine production, although the slowdown in demand was also noteworthy. Output in Australia at 864,000 tonnes and Peru at 917,000 tonnes, represented significant contributions, and correspond to y-o-y increases of 4.7% and 5.9% respectively. In addition, the shift towards full capacity at operations in San Cristobal has allowed Bolivian output growth to surge 89%, as production reached 193,000 for the first seven months.

### Chinese refined production steady

Latest figures from Antaike show Chinese total refined zinc output over the Jan-Aug period up 9.4% y-o-y, to reach 2.59m tonnes. Whilst up on last year, Chinese refined output has thus far been slow to respond to the significant increases in concentrate output both domestically

and elsewhere. Refined output could be boosted however as three of China's major producers – Zhuzhou, Yuguang Gold and Dongling Group – announced the activation of a combined 280,000 tonnes per year of new capacity in August. Total global refined output for the January-July period increased just 4% y-o-y according to ILZSG. Asia saw the most impressive growth, where, excluding China, the region saw growth of 10% y-o-y. European growth was largely stagnant at +1.2% y-o-y and the Americas saw a decline of 0.5%.

### China remains net importer of zinc

Although refined zinc imports slipped 18.4% from July to reach 25,589 tonnes in August, total refined zinc imports swelled to 125,499 tonnes over the first eight months, an increase of 36.9% y-o-y. Rather than being indicative of any shortage in the domestic market, it is believed that it represents an exploitation of the SHFE/LME price differential. On the export side, it seems the cancellation of the export rebate has had a negative impact as refined zinc exports slipped to 4,765 tonnes in August. Total exports over the first eight months are down 78.4% on last year, standing at 50,952 tonnes.

### A supply response has begun to emerge

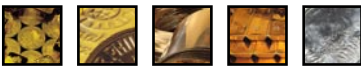
A series of Australian mines have struggled recently as low prices have squeezed margins. Intec Ltd's

Hellyer zinc mine, Teck Cominco's Lennard Shelf, CBH's Endeavour and Perilya's Broken Hill operation have all been forced to either close or cut production. The latest casualty is OZ Minerals Ltd, the world's second largest zinc miner, which has announced cuts of 50,000 tonnes effective from 2009 at its Golden Grove mine in Australia.

**To receive GFMS Metals Consulting's latest projections on the zinc market, contact: [info@gfms-metalsconsulting.com](mailto:info@gfms-metalsconsulting.com)**

GFMS Metals Consulting has launched a series of Quarterly Forecasts on the individual base metals that will analyse their prospects for the next three years. The first report on the copper market - the **Quarterly 3-Year Copper Forecast** - was published in April, and will be shortly followed by similar forecasting services on the nickel, zinc, lead, aluminium and tin markets.

**Please contact Charles De Meester at [charles.demeester@gfms.co.uk](mailto:charles.demeester@gfms.co.uk) for further information.**



## Steel: Is It Time to Panic?

by Neil Buxton, Managing Director, GFMS Metals Consulting

It is undoubtedly crisis time for financial institutions – is it crisis time for steelmakers? At the moment, the noises coming from major steelmakers such as ArcelorMittal are that this is a momentary dislocation of supply and demand, which with a little judicious assistance from supply restraint in the final quarter, will be overcome by early 2009. On the whole we agree – prices went too high over the second quarter, excessive supply hit the market in the third quarter just as demand slowed and prices came back down.

There is now a supply response in effect to the low prices – in China, the CIS and North America in particular. This should bring back supply back into line with demand relatively quickly as there was little build-up in inventory prior to the summer period and therefore the huge surge in Chinese exports over Q3 should be absorbed over Q4 and leave the market in approximate balance by the end of the year. Nevertheless, the scale of the financial crisis will have knock-on effects on the real economy in 2009 and we have revised down our forecasts for the next 12 months. We continue to forecast a bounce-back in flat product pricing during Q1 and Q2 next year as purchasing returns from low levels, but are forecasting weakness for the second half of the year, as production then catches up and fundamental demand continues to deteriorate. Without any major demand stimulus, prices are unlikely to reach the highs seen in the previous cycle. However, the recent change in price resulting in a

downturn to marginal cost levels (at least for the marginal supplier – the Chinese) has stimulated a supply response. This leads us to suspect that prices could trade in the range of \$750-1,000/tonne for HR coil on an fob international market basis over the next twelve months.

### Long product prices are marked down aggressively

September was a dismal month for emerging market exporters, as constant price reductions failed to interest consumers. CIS, EU and Turkish billet prices dropped another \$200/tonne over the month. We expect no relief in October either with prices potentially falling another \$100/tonne before we hit rock-bottom with billet at \$420/tonne fob CIS and around \$450/tonne for Turkish exporters.

For those producers such as in the US, which left prices higher, they will have to take the pain in October to re-align domestic prices with international ones and price cuts should be in the region of \$300/tonne at least. This will hurt margins, but these are now down across the globe and will fall further in October. If they try to hold prices higher, imports will come in and leave them sitting on inventory as demand continues to dwindle, hurting even more in 2009.

Nevertheless, we still expect the market to hit bottom in October, and while purchasing may be in “drips and drabs” early on, there will be the requirement to feed still strong demand in the Middle East and other

emerging markets in Q1. We expect purchasing to come back in greater volumes in November and the price turnaround by the end of the year and early into Q1 could be just as quick on the way back up – \$200/tonne a month is not inconceivable. Production cuts are required to make this a quick turnaround and northern European and US mills have not really reacted so far, while some CIS suppliers can ride their low-cost base down further and still make a margin.

### To receive our detailed forecasts on the flat and long products

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