MOTILAL OSWAL
Financial Services

Precious Metals Quarterly

8th April, 2024

Silver Story: 1 lakh and beyond!!!

Silver performance table- MCX	
Year	***%***
CY 2015	*-7*
CY 2016	*17*
CY 2017	*0*
CY 2018	*-1*
CY 2019	*20*
CY 2020	*46*
CY 2021	*-8*
CY 2022	*11*
CY 2023	*7%*
YTD 2024	*9.5%*

Source: Reuters

Silver has been witnessing sharp swings in prices over the last few quarters, influenced by a complex interplay of factors spanning economic data points, geopolitical tensions, and market-specific dynamics. Last year we did witness slower performance as compared to Gold however, returns of domestic silver looked better amidst the rise in basic custom duty and rupee depreciation. In this year, silver's journey on higher side was a bit delayed as compared to Gold but it caught the pace well and has posted ~9.5% gains YTD on domestic front.

Understanding the key drivers behind silver's recent move requires an analysis of:

1) Macro Economic Trends

2) Geo-political Development

3) Market Sentiment and Investment Behavior

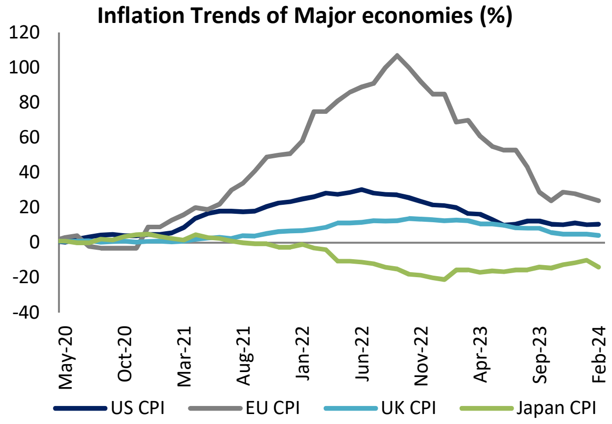
4) Industrial Penetration

5) Supply and Demand Dynamics

1. Macroeconomic Trends

Inflationary Pressures:

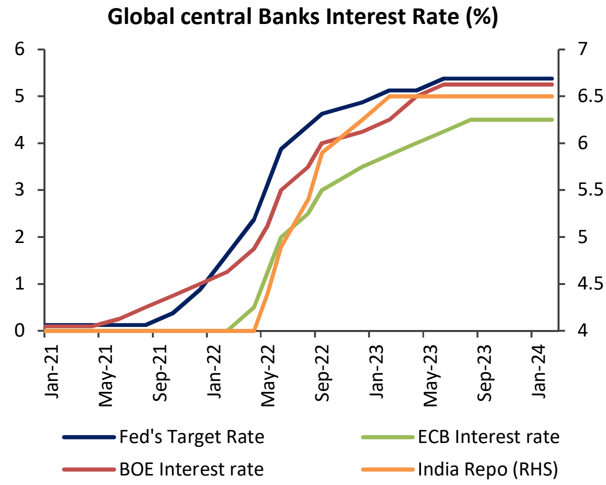
Inflation has been talk of town since the pandemic and still is responsible for any major triggers in Commodities segment. Since 2020, US Inflation has moved from almost 0% to 9.1% to now hovering around 3.0%, however Fed officials are not convinced with this ease off and are waiting for it to drop near its target of 2%. The inflationary pressures aggravated after the Russia –Ukraine war, with higher Food and Energy costs and increased supply side challenges. Fed officials fear that these challenges might surface again in the market; hence, they are taking their time in pivoting from the current monetary policy.



Source: Reuters

Central Bank Policies:

The Federal Reserve's decisions regarding its monetary policy stance and interest rates played a crucial role in shaping market sentiment towards all major assets including silver. Change in inflation as mentioned above influenced the interest rate decisions of major central banks. Major economies like US, UK, EZ, and India raised rates by more than 1700 bps from the end of 2021 to 2023, this led to sharp ease off in inflation.



Source: Reuters

Looking at the recent developments, after the Dec'23 Fed meeting market participants had started discounting an early rate cut in 2024, however Fed officials were quick enough to convey the change in tone to market participants. Fed officials mentioned that, US central bank will remain data dependent and will require more evidence for inflation to drop towards its target of 2%. They also said that it is too early to implement a rate cut and interest rate could remain higher for longer supporting an up-move in Dollar and US Yields.

In the recent meet, the Fed kept the rate unchanged, but raised expectations for three rate cuts this year. It was surprising to see that the Fed raised their Core inflation and GDP forecast to 2.6% and 2.1% for this year, Fed Governor Powell also mentioned that they will continue to be data dependent as inflation is still sticky. According to the dot plot, Fed expect three rate cuts of at least 75bps in this year and the next, influencing 100bps fall in Dollar index and triggering a sharp move in safe haven assets. We are seeing something similar once

Fed Projections(%)

Years	Core Inflation	Growth	Unempl-oyment	Fed Funds Rate'
2024	2.60	2.10	4.00	4.60
2025	2.20	2.00	4.10	3.90
2026	2.00	2.00	4.00	3.10

Source: Bloomberg

again, wherein market participants are discounting a rate cut three months from now, but Fed officials comments and economic data points are suggesting the opposite.

The probability chart has been a big signal showing change in sentiment regarding the US interest rates for the future meetings. Post the Mar'23 Fed meeting the probability for March meeting showed 70% chance for a rate cut in the month of June, however, after sticky inflation and labour market data bets dropped to around 50%. Any change in sentiment and probability for June Fed meeting would trigger significant volatility in the market.

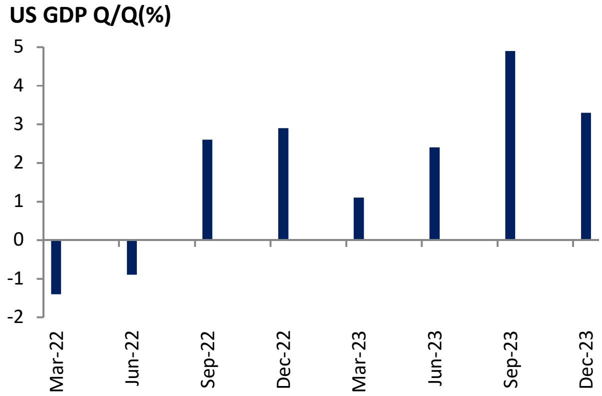
Target Rate probabilities for Fed Meetings

Meeting Date	475-500	500-525	525-550
May'24	-	3%	97%
June'24	1.8%	61.8%	36.4%
July'24	21.7%	54%	24.3%

Source: CME Fed Watch-Tool

Economic Data Releases:

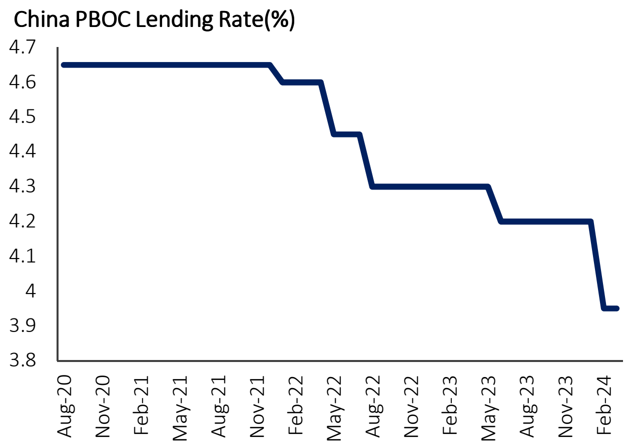
Economic data releases in Q1'24, such as GDP figures, employment reports, and manufacturing data, provided insights into the pace and trajectory of the global economic recovery. Economic numbers are a bit mixed, not conclusive enough for the Fed to pivot from the current monetary policy path. Positive economic indicators supported industrial demand for silv er; however, ease off in the concerns regarindg slower demand dented the safe haven appeal for gold and silver. US inflation cooled less than expected in February to 3.2% YoY, Core inflation a measure, which strips out the volatile food and energy prices, was reported at 3.8% YoY in February. US PPI was also higher from the expectations, suggesting caution regarding overall inflationary pressures. Following the numbers, the two-year Treasury, which moves with interest rate expectations, recently rose significantly around 4.65%,increasing fears regarding delay in rate cut.



Source: Reuters

Betting on China:

Economic number from China is very important to keep an eye on, with property sector distress, stimulus measures from PBoC, industrial metals are witnessing sharp swings and this could influence volatility in Silver as well. The concerns of China are quite opposite from the rest of the world - China is struggling to pick up its growth, it is in a deflationary scenario, is continuously pumping money in market and loosening its monetary policy. There could be a scenario that China stabilises in the H2'24, we could possibly witness major economies struggling to pick up pace on the back of higher debt, labour market trouble and impact of higher interest rate. This could again initially keep the gains for silver in check and later support the rally as a safe haven asset.



Source: Reuters

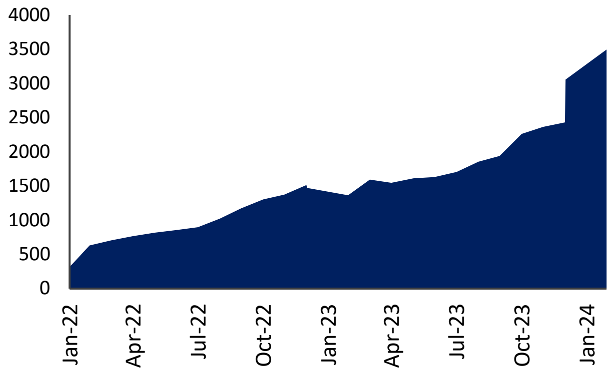
2. Geopolitical Uncertainties

Geopolitical tensions have continuously built in risk premium in the market, we have continuously seen year after year, since 2020, some or the other black swan has hit markets and supported the precious metal pack. In 2022, we had the Russia –Ukraine war, last year we saw a conflict between Israel and Hamas group, expectations for a tussle between Russia and Ukraine is building up supporting the safe haven assets. Geopolitical risks, including conflicts, geopolitical tensions, and geopolitical uncertainty, heightened market volatility and drove demand for silver as a perceived safe investment. The UN Security Council did try to intervene and pass a resolution demanding a ceasefire between Israel and Hamas for the first time since the war began. This resolution also calls for the immediate and unconditional release of all hostages held by Hamas. However, the resolution did not hold much value, as the attacks continue.

3. Market Sentiment and Investor Behavior

Speculative trading activity and investor sentiment have not a played a significant role in shaping silver is price movements since quite a long time. Even if the speculative positions have seen rapid flicks, it has failed to influence silver prices; similarly, ishares ETF flows have also not been very impressive, affecting the overall sentiment. However, inflows in the domestic ETF and the Imports on for the metal has seen a significant jump. In just two months of 2024, silver imports have crossed 2500 tonnes giving a boost to the sentiment.

AUM of Indian Silver ETF (in Cr)



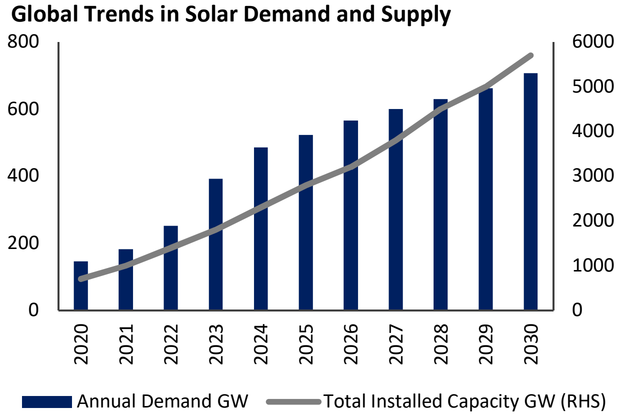
Source: MOFSI, ACE

4. Green Tech advancement:

The Silver Institute estimates 2023 demand from silver used in photovoltaics (PV) at around 161 million ounces, up from 140 million ounces in 2022, and representing about 13% of total global silver demand. This demand is, of course, expected to continue to increase to reflect the growth of solar installations as one of the main sources of renewable energy globally. By 2028, International Energy Agency estimates that solar photovoltaics (PV) will account for about 13% of total global electricity capacity, up from approximately 5% of capacity. The implications for silver is that increasing solar PV demand over the next five years and beyond is unlikely to be matched by an increase in supply.

A more than doubling of solar PV capacity by 2028 should translate to more than twice the PV demand for silver. Annual global supply of silver has been relatively unchanged over the past 10 years, as primary silver deposits hard to find. Thus, this growing demand from solar applications and other green technology is substantial to an industry that is inelastic when it comes to the supply side.

Global Trends in Solar Demand and Supply



Source: Sprott

Global P.V. installations significantly exceeded initial market expectations in 2023, with new capacity additions forecast to reach another record high this year. Silver offtake should also benefit from the technological breakthrough that has brought new, higher-efficiency N-type solar cells (with higher silver loadings) into mass production. In the automotive industry, greater use of electronic components and investment in battery charging infrastructure will continue supporting silver offtake.

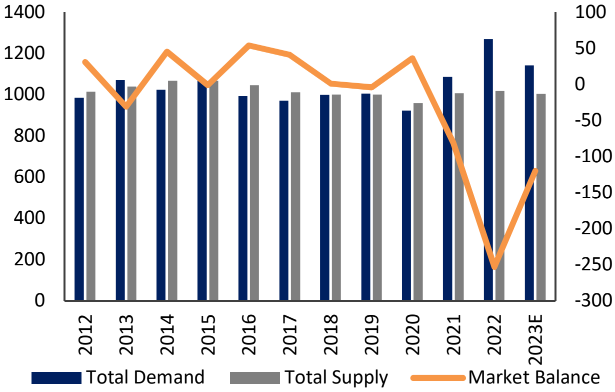
5. Supply and Demand Dynamics

Supply Factors:

Silver supply faced several challenges that affected market dynamics, like operational disruptions at mines, environmental regulations constrained production levels in key silver-producing regions.

Total global silver supply is forecast to grow by 3% in 2024 to an eight-year high of 1.02 billion ounces, entirely led by a recovery in mine output. Silver mine production in 2024 is projected to rise 4% to 843 Moz, the highest level since 2018. In contrast, silver recycling is expected to edge lower, with volumes likely to drop by 3 percent to a three-year low. Lower jewellery and silverware scrap supply will account for most of this year's losses.

Global Silver Demand , Silver and Market Balance



Source: Silver Institute

By-product silver output from base metal mines is forecast to decrease as community and government disputes led to some mine closures in 2023, particularly in South America. Furthermore, there is an impending risk to silver output from zinc mines that may continue to face mine suspensions due to weak zinc prices.

Demand Factors:

Global silver demand is forecast to reach 1.2 billion ounces in 2024, which, if achieved would be the second-highest level recorded. Stronger industrial offtake is a principal catalyst for the rising global demand for the white metal, and the sector should hit a new annual high this year.

Data from silver institute suggest that, Global silver demand is expected to rise 1%, pushed higher by the continued strength of industrial end-uses and a recovery in jewelry and silverware demand. Silver industrial fabrication is forecast to post a 4% rise in 2024 to a record 690 million ounces (Moz), building on the all-time highs achieved last year. In line with the trend in recent years, the photovoltaics (P.V.) and automotive industries will remain key drivers of growth this year.

On the demand side, silver benefited from robust industrial demand, particularly in sectors such as electronics, solar energy, and healthcare. The global economic recovery, coupled with increased investment in renewable energy infrastructure, drove demand for silver in various industrial applications. Furthermore, the resurgence of manufacturing activity in major economies contributed to higher silver consumption in sectors like automotive and consumer electronics. Jewellery demand is expected to record a 6% rise, and India will contribute the bulk of gains this year. This follows a sharp pull back in 2022 when Indian demand weakened after a post-COVID surge in 2021.

**We are expected receive fresh demand and supply forecast from the silver institute by the end of this month.*

Conclusion:

Safe haven assets are currently assessing the Fed's interest decision and geo-political risks. There definitely are some headwinds, which could keep prices weighed down like the industrial activities, China's recovery, ease off in the early rate cut scenario, persistent strength in Dollar Index strength. On other hand, factors like, *fall in Dollar Index and US Yields, expectation of a deficit, loose monetary policy, boost in industrial metals, Green-Tech advancement, geo-political uncertainty and fears regarding slower global growth, could trigger safe haven buying in Silver.*

Fed's interest rate decisions and China's recovery are two big factors that market is currently discounting and could continue to support prices in the long run. It is important to note that Gold has seen a significant rally and silver has also now started to catch up its pace. The recent rally is coupled with the up move in industrial metals. Silver being a hybrid metal (Precious + Industrial) and a high beta commodity, the pace on either side is always higher than Gold; we believe this year we could see silver matching or outperforming Gold's pace. As per the factors mentioned above, the current underlying tone in silver is very strong, and the metal has a tendency to surprise everybody by the sheer pace of price move. *We are seeing a reasonable uptrend in price and it would be difficult to time weather it is just the beginning of the big swing in silver that we have been anticipating, or another deception.*

***We continue to be strongly positive in Silver over the next few months, but will it be a straight upside or with volatility is difficulty to time. We advise to be invested in silver and keep adding on dips towards Rs. 75,000 for a medium to long term upside towards Rs. 92,000 followed by Rs. 100,000*.**

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