CRITICAL
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Your monthly guide to the latest information on the world's strategic metals

What's Your Silver Strategy?

After four days of an upward climb in mid-July when silver prices reached $40.55 per ounce, spot silver prices fell by $1.022 to reach $39.53 per ounce on July 19. Analysts are of the opinion that silver prices are reflecting the reactions of investors who are concerned about the approaching August 2 deadline for the US debt ceiling, the Eurozone debt and the US Federal Reserve hinting at a third round of quantitative easing (QE3). They agree that while the fall may just be a result of precautionary selling or profit taking, the long-term prospects for precious metals such as silver are promising since structural issues with debt and loose monetary policies are here to stay. In 2010, the price of silver increased by almost 80%.

When asked about the future of silver under current conditions, Jamie Greenough, an investment advisor with Global Securities Corporation, said, "I don't think that we have seen the high for the year." Reflecting on the fall in prices since April 25 when silver was traded at $49.79 per ounce, he added, "The CFTC absolutely slammed the market by raising margins, which took the wind out of the sails for silver. Now the silver market has had a chance to build a base, and finally digest the requirements. It appears that there is now a solid base for silver around the $35 per ounce level, and we are now seeing some appreciation."

Over the last one year, China has been importing silver in record quantities and trends indicate that it will continue to do so this year as well. In 2010, China imported a record 3,500 tonnes of silver and the strong demand shows no sign of slowing down. Industry, jewelry and investment are the three sectors accounting for the highest demand with industry constituting 70% of the demand.

Other than China, India has also shown an increasing demand for silver. The two nations are expected to show a 30% increase in the demand for silver this year. In 2010, India consumed about 2,800 tonnes of silver and consumption is expected to grow to 5,000 tonnes this year. In India, it is the rural sector that accounts for the highest investment in silver. Given the market uncertainties, investors in both nations are focusing on silver as a way to hedge market losses.

Considering the possibility that the current market trend of silver may replicate the pattern seen in the period between 1971 and 1980, Citigroup analyst Tom Fitzpatrick and two others wrote, "If the final rally in the last bull market repeated then we can expect $100 over the long term. While the high so far this year was at the same level as the peak in January 1980, we are not convinced that the long-term trend is over yet." They added, "The move down from the April high this year has come to an end and the double bottom is a good platform for a turn back up."

Metal dealers expect to see a huge rush for silver within the next month or so as investors collectively wake up to the fact that its long-term prospects are very positive. Usman Khalid, a supervisor at Toronto-based Gold Stock, said, "If I had my bet, I would definitely go with silver long-term. I think silver is under-valued, there's a big demand for it and it should go up." He added, "With physical silver you have the option of doing a lot of stuff, but with ETFs you just have it as an account. Physical silver you can use it as an investment, jewelry, or anything you like in any form." Khalid said that in spite of the price fall, silver is still the preferred metal instead of gold, for long-term investments in precious metals.

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Steel's Slow Rise

The World Steel Association reported a global steel production increase of almost 8% in June, y-o-y. China reported a y-o-y production increase of 11.9% in June, and a m-o-m production increase of 1.7%. The nation's slow economic period did not seem to affect its steel industry significantly. Analysts believe the government's incentives to steel makers for increasing production have borne the right results. The US, Africa, India, Japan and the Middle East also reported production increases but both Australia and Europe reported sharp falls in their y-o-y production in June. However, in a complete reversal, the China Iron and Steel Association (CISA) reported a 3.1% m-o-m production fall in early July.

The July figures have not dampened the potential for the future. As the construction sector continues its rapid growth, consumption during the first half of the year increased by 9%. In fact, China is expected to produce almost 729 million tonnes of crude steel this year. Social housing projects, high speed railway projects and water conservancy projects in addition to other infrastructure projects are expected to keep China's crude steel production levels at record highs over the next few months. Wang Dezhi, an analyst at Shanghai's Orient Futures, said, "Strong demand from social housing and infrastructure investments have driven long product mills to run at near 100% utilization rates, and the bull-run may extend to the coming months."

Asian steel makers are expected to report lower profits in the April to June quarter because of weak demand, high input costs, the natural disasters in Japan and tighter monetary policies in India and China. However, the third quarter is expected to be more fortunate for everyone as seasonal demand increases. The gains are not expected to be very high.

Chris Park, a senior credit officer with Moody's in Hong Kong, commented, "Persistent overcapacity in China, sizeable capacity expansion in Korea and longer term capacity increases in India, as well as a current glut in a sluggish Japanese market, should constrain price increases and trim margins."

Metals analyst Kamlesh Bagmar at Mumbai's Prabhudas Lilladher, recently said, "The demand environment has deteriorated substantially in the past quarter owing to elevated inflation and interest rates." Growing competition in hike capacity, and rising prices of iron ore and coking coke in India are expected to adversely affect the steel sector's bottom line.

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As Goes Steel...

Driven by the revival of the infrastructure industry, the increased demand for steel worldwide is driving the global manganese market as well. The demand is exceptionally high in the developing nations, with the Asia-Pacific region accounting for the highest consumption of manganese. Analysts are of the opinion that the region's demand is set to grow at 7.5–8% annually.

Other than the steel industry, which is the traditional user of manganese, the battery industry is also driving the manganese market. Lithium manganese batteries are expected to be the answer for the need for high capacity and low cost energy storage devices. Both factors are essential for the success of emerging technologies in areas such as renewable energy, consumer electronics, and electric vehicles. Jonathan Lee, Battery Technology and Materials Analyst for Byron Capital Markets, said that China produced 1.4 million tonnes of the metal in 2010 and non-Chinese production of electrolytic manganese was only about 34,000 tonnes. He added, "With electric vehicles, our estimates are by 2020, we see a need for 80–90 thousand tonnes [of manganese] for electric vehicles."

As manganese battery technology improves, the efficiency of electric vehicles is expected to improve as well. This will naturally increase the demand for both. Also, the potential of manganese based batteries in mobile technology is very high and that could lead to a much higher demand for manganese.

Nations have now turned their attention to the ocean floors and the Atlantic is being actively explored for minefields. Deposits of precious and rare metals have reportedly been discovered at a depth of about 4 kilometers on the ocean floor. The discoveries are naturally creating a great deal of interest among geologists. Vladimir Kryukov, director of Russia's Polar Marine Geological Prospecting Expedition (PMGRE) said, "China has already made a claim to this end, whereas France, Germany and England are actively engaged in searching for these ores that rank among such promising natural resources as manganese and cobalt. Russia, by the way, owns and explores a manganese field in the Pacific Ocean. Now we are preparing our bid to the UN concerning cobalt deposits."

The 20% export duty imposed by China electrolytic manganese has been creating more concerns than relief for Chinese authorities. China has been collecting the export duty January 2008 but recent reports indicate that certain quantities of the metal seem to be evading this duty and are being sold in Asian and European markets. This is creating a price pressure on the formally exported electrolytic manganese that has incorporated the export duty in its prices.

Another issue dogging China's electrolytic manganese sector is the fact that China's export records do not match the import records of Japan and South Korea. This mysterious phenomenon is causing Chinese exporters a great deal of anxiety since it substantiates the suspicion that large quantities of Chinese electrolytic manganese are successfully evading the export duty and taking advantage of the price difference.