H1 2022 Gold and Silver Market Review and Outlook

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Transcript

Shree Kargutkar: Hi, everyone. This is Shree Kargutkar. I'm the managing director at Sprott Inc. and the portfolio manager at Sprott Asset Management. Today, we'll be reviewing the performance as well as the events that occurred in the gold and silver space through the first half of 2022. The first half of the year was marked by volatility for investors across all asset classes. The Russia-Ukraine conflict created a tremendous amount of uncertainty for investors around the world.

Inflation, which was a big issue entering 2022, accelerated even further. As a result, central banks around the world have adopted an extremely hawkish tone, punctuated by supersized interest rate

heights that we've all been witnessing over the past few months. These factors have led to a wholesale liquidation of virtually every single asset class and the sell-off that we saw in equities, in particular, picked up steam through the second quarter of the year. The S&P 500 declined by 20%, and the Nasdaq saw a decline of 29% through the first six months of the year.

Investors typically buy gold to protect against these types of uncertainties and this type of volatility that we've been experiencing through the first half of 2022. Through the first half, gold actually was an asset class that held itself relatively steady. Although it declined by just over 1% over this timeframe, the theme of deglobalization has continued to play out. One of the most important monetary events that occurred for gold came on the outset of the Russian invasion of Ukraine, both the US and the eurozone effectively froze the Russian reserves that were held in US dollar and euros and effectively cut off Russia from accessing two-thirds of the reserves that it had accumulated.

This obviously did not go unnoticed by central banks around the world. Many central banks have been working to reduce their exposure to the US dollar as well as to the euro for the past few years. As a result of the action of both the ECB, as well as the Fed, when they froze Russia out of their respective currencies, gold bullion as a reserve asset started to gain importance, and as a reserve asset, gold, because it does not have any type of counterparty risk, has seen it's importance get magnified for the past few months.

Through the first half of 2022, central banks around the world were busy buying gold. They actually grew their gold reserves by 270 tons in the first six months. Out of the 270 tons, 180 tons were actually purchased in the second quarter of this year. While gold health study through the first half, this was a very, very opportune buying opportunity for central banks around the world, just to diversify themselves away from fiat currencies like the US dollar, like the euro, for example.

Silver, on the other hand, unfortunately, did not far as well as gold did. It declined by 13% through the first half of the year. While silver demand has benefited greatly from its expanding use and the photovoltaic industry for making solar panels, it has fallen out of favor as far as investors are concerned. This is best observed when you look at the ETF holdings, for example. Through the first half, silver ETF suffered large liquidations, and over 100 million ounces of silver were actually sold by silver ETF.

We also saw a similar activity of liquidation on the long side occur in the silver futures market. This has precipitated into larger declines that we saw for silver versus gold, but this is not all bad news, the way we look at it, the combination of the selling we have seen in the silver futures market, as well as a massive sell-off we saw in the silver ETF front, seem to point us towards a potential event which we refer to as a capitulation. We think that investors in silver, in particular, have likely capitulated through 2022. This presents a very good entry point for investors that are interested in getting exposure to silver bullion.

Let's talk briefly about precious metal equities. While gold held its own through the first half, precious metal equities suffered significantly more. We think and we know that this is more a function of price rather than profitability because the profitability of the precious metal miners continues to be strong. As I had touched on earlier, the price of gold has held in relatively well through the first half of the year, and the cost of the inputs for these miners has not really changed all that much, so the profitability of these miners has remained strong as a result.

The price declines that we have seen has been as a result of multiples getting cheaper, and price

have gotten cheaper while the profitability has more or less remained the same for many of these companies. The NYSE Arca Gold Miners Index, which has a combination of gold and silver miners in it, currently trades near multiple of around 5.7 times EV/EBITDA, which is among the lowest readings we have seen over the past decade or so. With gold hovering around $1,800 and silver around $20, many companies in our portfolio continue to generate fairly strong cash flows and will continue to do so.

In summary, I'll just end off by saying that this year has been an unkind one for investors, virtually. Every single asset class, with perhaps the one exception being gold and precious metal equities and silver bullion unfortunately, have suffered large price declines. As I speak, the entire precious metal complex is oversold especially when it relates silver bullion as well as the lowest precious metal equities. As it relates to precious metal equities, valuations are near tenure lows.

The current setup has all the classic hallmarks of capitulation like I pointed out before. Prices have moved lower while underlying fundamentals have improved for gold and silver. Central banks and smart investors are already positioning themselves into precious metals, and looking ahead, we are quite excited by the upside not only in precious metals but also in particular precious metal equities.

If you have any questions about gold, silver, either on the bullion side or on the equity side, and the precious metals complex, please reach out to your Ninepoint advisor for more details. Thank you.

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