



Why Palladium Will Continue to Outperform Silver and Gold

Description

The precious metal palladium has rallied about 25% since the start of the year, and is currently hovering near a 13-year high. The metal's year-to-date performance has trumped silver and gold, but the current high price may cause some investors to fear that the rally is about to lose steam. However, a close examination of the palladium market's supply/demand fundamentals quickly reveals how more upside could be in store.

Supply constrained

When comparing palladium to gold and silver it is immediately obvious that palladium has higher supply constraints. The majority of the world's palladium comes from just two countries, Russia and South Africa, and recently both regions have been grappling with instability.

South Africa's production has been unreliable for years due to power outages, labour disputes, and the fact that the region's mines are aging and therefore have inconsistent output.

Russia's supply issues include uncertainty in palladium availability and geopolitical concerns. Russia amassed stockpiles of palladium during the Cold War, and in the years since the country has willingly released some of the metal from its supplies whenever a market deficit became an issue. Recently, the country has stopped doing this. Russia is not transparent with its palladium supply data, leaving analysts to speculate that the country is not releasing more supplies because they have been exhausted.

While the country still holds impressive palladium reserves, its current political situation is cause for concern. It is currently under economic sanctions, and while those sanctions do not directly target palladium they are causing some impact on pure sentiment. There is also the potential for steeper sanctions to directly impact Russia's palladium sector.

Growing demand

Palladium is benefiting from strong demand thanks to an improving global economy and new interest in the metal as an investment.

Palladium is a chameleon. It is both a precious metal and an industrial metal. While an improving global economy erodes the value of traditional precious metal investments, palladium prices actually benefit from higher industrial demand in times of economic growth. Silver and gold also have industrial demand components, but not to the same degree as palladium.

In addition, palladium is seeing fresh interest from investors, which has resulted in the creation of a few physically backed palladium ETFs. These ETFs remove even more supply from the market, acting as another catalyst for palladium prices.

Multi-year deficit expected

The supply challenges and demand outlook discussed above have put the market in a deficit, and this deficit will linger for at least a few years. Standard Bank's Walter de Wet expects that palladium will be in a deficit of two million ounces this year, 1.3 million ounces in 2015, and 1.8 million ounces in 2016. Until more supply comes online, prices have every right to continue to ascend given the forecast for a prolonged deficit.

How to profit

The key to finding a palladium investment that can actually benefit from industry fundamentals is to find one whole operation outside of South Africa and Russia; with about 80% of the world's palladium coming from those two countries, the options are limited.

Surprisingly, the best pick for investors looking for a Canadian miner with access to palladium is actually primarily a gold miner. **Franco-Nevada Corporation** ([TSX: FNV](#))([NYSE: FNV](#)) is a gold-focused royalty stream company that holds interests in platinum group metals. The company's ownership of assets outside of South Africa and Russia, the Stillwater Complex and the Sudbury basin in Ontario, is a differentiating factor, and thus leaves it well positioned to benefit from the palladium market's positive fundamentals without being negatively impacted by the current supply chain challenges.

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