

EXCHANGE TRADED FUNDS

The launch of two sets of physically-backed Exchange Traded Funds (ETFs) in Europe in 2007 injected some vigour into the physical investment market for platinum and palladium. While many larger investors had already been able to gain exposure to the prices of these metals, these funds have allowed others to invest, from private individuals to pension funds.

The ETFs which were launched were entirely backed with physical metal in that each investment in a new share in the ETF was balanced by the purchase of the appropriate amount of either platinum or palladium by the ETF. While investors maintain these positions, this metal is held off the market, leading to physical demand (in contrast to the leveraged and short funds later launched which have no impact on the physical market).

With more than two years of history since the launch of these funds, it is now possible to understand ETF investor behaviour to some extent. The Swiss-based fund appears to have attracted a buy-and-hold type investor looking for longer term profits. Indeed one of the larger initial investors in the Swiss funds was a pension fund.

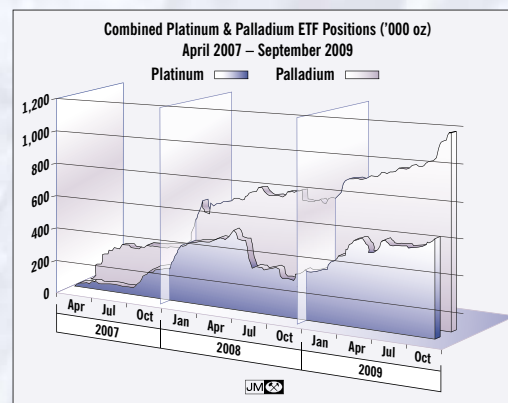
The launch of Exchange Traded Funds has provided investors with another route to gain leverage to movements in metal prices.



By contrast, in London, positions appear to be significantly more fluid with investors speculating on shorter term price movements. Although these investors may be willing to hold metal for the longer term, this has not been seen to date. What has been seen is a rapid increase in total metal holdings at times of rising prices and weighty sales as the price falls or as the value of other investments has fallen, necessitating the liquidation of these positions to cover losses incurred elsewhere. Our relatively positive outlook for the prices of both metals in 2010 suggests that net investment flows into the ETFs could again be substantial.

In April 2009, the launch of a US-based physically-backed fund was proposed. This is currently in the process of attempting to gain approval from the relevant licensing authority. In the USA, the existence of the liquid NYMEX futures market already provides a route for investors to gain exposure to the price of platinum and palladium. However, the US Federal Trade Commission has spent much of this year investigating excessive speculation in the futures markets for energy. The possibility remains that it will seek to impose limits on futures positions in other commodities, making an ETF a more attractive investment vehicle for larger investors. For private individuals, the smaller minimum holding of an ETF (likely to be 0.1 ounces compared to the 50 ounces of a NYMEX contract) may make an ETF the more practical option.

Further details on these funds were filed with the US authorities in October 2009 but they have not yet



received approval. If they were to be approved, we believe that they could readily generate additional physical investment of perhaps 200,000 oz of each metal in the first year of operation.

A cross-listed version of the London platinum and palladium funds started trading on the Tokyo Stock Exchange in August. In Japan, there is a considerable history of individuals investing in platinum either in physical form, through accumulation plans – where a set amount of Yen is invested per month with the combined positions of all investors then used to buy platinum bars – or via TOCOM futures. The launch of these funds might therefore have been expected to generate substantial interest from the investment community. However, the lack of a domestic sponsor and the ready availability of these other investment routes have meant that investor activity has been light so far.

2009 did also see the creation of Australian platinum and palladium funds early in the year. To date, there has been less than 5,000 oz of interest in either metal, perhaps unsurprisingly since Australian investors are already heavily exposed to the commodity sector.

After substantial net redemptions of platinum and palladium ETF holdings in the second half of 2008, investors returned in the first three quarters of 2009.