OCBC Bank

Friday, March 10, 2017

Weekly Commodities Outlook

Energy: Market-watchers were faced with higher crude oil production outlook by the US Energy Information Agency's (EIA) latest Short-Term Energy Outlook report (see table 1: Revised STEO Outlook). Importantly, crude oil supply growth into 2017 and 2018 is estimated to accelerate to 9.21 million barrels per day (bpd) and 9.73 million bpd, respectively, although crude oil prices are estimated to stay relatively unchanged to average $53.49/bbl this year.

Table 1: Revised STEO Outlook

	2018	2017	2018	2017
	March 2017 STEO		Feb 2017 STEO	
Crude Oil Supply (mbpd)	9.73	9.21	9.53	8.98
Change	*+0.20*	*+0.23*	-	-
Liquid Fuel Consumption (mbpd)	20.22	19.84	20.17	19.84
Change	*+0.05*	*no chg*	-	-
Price Outlook ($/bbl)	$56.18	$53.49	$56.18	$53.46
Change	*no chg*	*+$0.03*	-	-

Source: US Energy Information Agency

Elsewhere, sustained increase in US oil inventories print finally sent oil prices down by the most in more than a year yesterday. Empirically, US stockpiles rose to its record level of 528.4 million barrels for the week ended 3 March 2017, sending WTI to near its $50/bbl support handle overnight, while Brent followed suit to close at $53.11/bbl. However, should we look it holistically, the rise in crude oil inventories was seen in tandem with the fall in gasoline inventories (-6.6 million barrels to 249 million barrels), the lowest in 7 weeks while refinery utilisation rate was flat at -0.1%.

Still, WTI had fallen below its critical $50/bbl overnight on concerns over potential increases in US shale oil production. Specifically, energy giant Exxon Mobil had previously iterated its plans to commit $5.5 billion (1/4 of its total spending budget) to shale drilling in US Texas and North Dakota earlier this week. Joining Exxon Mobil are other producers including Hess Corp, Chesapeake Energy Corp, Continental Resources Inc and others which detailed their growth plans that would result in a steady supply of crude supplies through the next decade. Still, note that US producers recognise the potential consequence of oversupplying the market, in which they iterated that they "have a great responsibility not to do so." Elsewhere, also note that Libya halted oil shipments from two if its biggest oil ports and reduced production in some fields. The affected ports included Es Sider (Libya's largest oil port) and Ras Lanuf (third largest oil port), which

Commodities Futures

Energy	Futures	% chg
WTI (per barrel)	49.28	-1.99%
Brent (per barrel)	52.19	-1.73%
Heating Oil (per gallon)	1.530	-1.75%
Gasoline (per gallon)	1.624	-1.71%
Natural Gas (per MMBtu)	2.974	2.52%
Base Metals	**Futures**	**% chg**
Copper (per mt)	5,665.9	-0.85%
Nickel (per mt)	10,095	-0.54%
Aluminium (per mt)	1,855.8	-0.67%
Precious Metals	**Futures**	**% chg**
Gold (per oz)	1,203.2	-0.51%
Silver (per oz)	16.993	-1.53%
Platinum (per oz)	937.2	-1.30%
Palladium (per oz)	748.9	-3.04%
Soft Commodities	**Futures**	**% chg**
Coffee (per lb)	1.388	-0.93%
Cotton (per lb)	0.7663	-0.35%
Sugar (per lb)	0.1800	-2.17%
Orange Juice (per lb)	1.7675	0.94%
Cocoa (per mt)	1,931	-0.72%
Grains	**Futures**	**% chg**
Wheat (per bushel)	4.2600	-0.35%
Soybean (per bushel)	10.003	-1.06%
Corn (per bushel)	3.5975	-1.51%
Asian Commodities	**Futures**	**% chg**
Crude Palm Oil (MYR/MT)	2,990.0	-0.33%
Rubber (JPY/KG)	281.1	-2.56%

Source: Bloomberg, OCBC Bank

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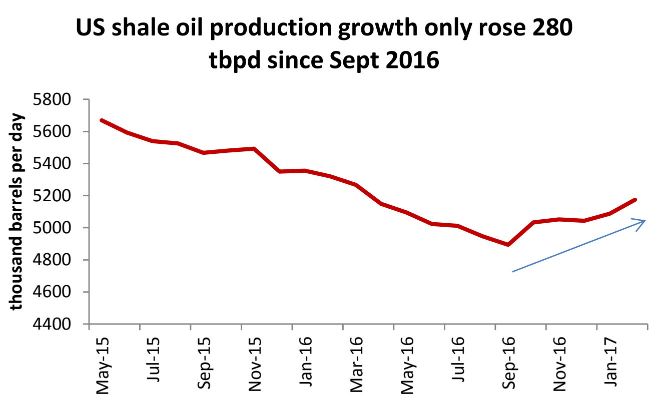
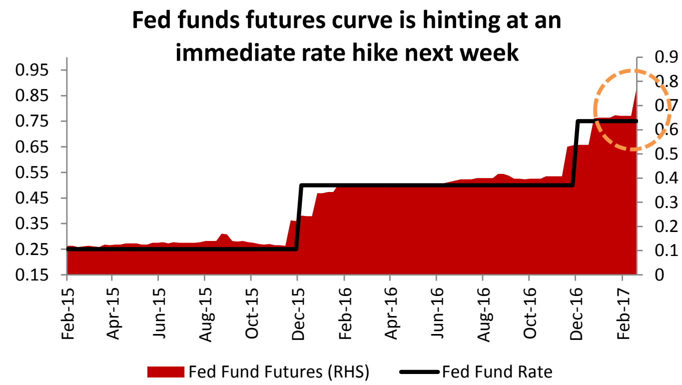
closed on security issues on militias takeover. Given the clashes, Libya's oil production had fallen to 650 thousand barrels per day (bpd), and may fall further if the ports stay shut, according to official comments.

Addressing the recent fall in oil prices, we think that the recent decline is most likely an over-reaction (with unnecessary concerns perhaps) over oversupplies. Indeed, there are signs of potentially higher US oil production, led by higher US oil rig counts and higher shale production. However, the increase in total US oil production was 56 thousand bpd in the first week of March. Moreover, the increase in shale oil production was a mere 86 thousand bpd in February 2017. Elsewhere, we reiterate that the reading of US total oil stocks must be accounted together with gasoline stocks and refinery utilization rates in order to have a holistic (and accurate) view of US supply and demand environment; note that US refinery utilization rates have repeatedly fallen from its high of 93.6% seen earlier this year to a recent 85.9% in March, thus explaining the surge in US crude oil stocks. Moreover, gasoline stocks fell to its the lowest in 7 weeks, suggesting that US energy demand remains robust.



Source: Bloomberg, US EIA, OCBC Bank

Precious Metals: All eyes are on next week's FOMC meeting on 15th March. Essentially, the Fed Fund futures curve suggests that market-watchers are pricing in another rate hike (+25bps). Consequently, the dollar index has been strengthening over the week. As we reiterate, gold prices have been a function of the dollar, and the relatively strengthening of the greenback over the last week has dragged gold prices lower. Moreover, should we refer to Yellen's latest speech at Chicago over the weekend, the Fed chair had dropped an arguably strong hint that "a further adjustment of the federal funds rate would likely be appropriate" in March.

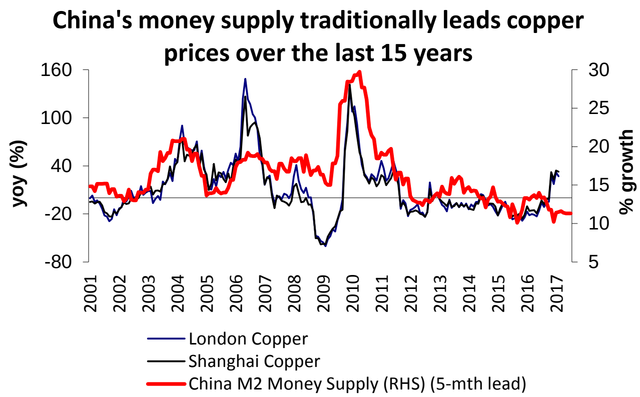


Source: Bloomberg, OCBC Bank

More importantly, the immediate question now, is the climate we may face after the rate hike comes to pass. For that matter, we recognise that current gold weakness is chiefly driven by the increased likelihood for a rate hike to materialize next week. However, market-watchers would then be left wondering (again) on when is the next rate hike into the year. **Coupled with the sustained uncertainty over European-centric political elections and the lack of clarity over US President Trump's trade and fiscal policies, the current fall in gold prices may be short-lived.**

Base metals: In a twist of events, some reprieve in copper production in the world's largest and second-largest copper mine were seen over the week. Copper prices fell sharply to print $5,660/MT this morning, down from a $6,000/MT handle seen in early March. Specifically, BHP Billiton had announced its intent to employ "contractors' help to try to get production going". Moreover, given that Friday (today) marks the 30-day mark, a time period where BHP Billiton can submit new contract offers to employ new workers, market-watchers will likely eye closely on such a move which would quickly allow the resumption of copper production. Elsewhere, Freeport-McMoRan Inc is said to resume copper concentrate production on 21st March at its Grasberg mine. Still, the mine is still not allowed to export copper concentrate given new export regulations.

Elsewhere, in the latest China's National People's Congress (NPC) meeting, China plans to cut 150 million tons of coal and 50 million metric tons of steel in 2017. Furthermore, it plans to cut money supply (M2) and aggregate social financing growth rate to 12%, down from a previous outlook of 13.0% in 2016. Relating this back to commodity demand in China, we note that the reduction in steel production would consequently mean lower demand for steel-making materials including metallurgical coal (or coking coal) and iron ore. Moreover, China's money supply growth traditionally leads copper prices (although correlation has broken down of late given supply issues in Chile and Indonesia), as copper was previously used as a tool to secure financing (or better known as copper financing). A such, the recent announcements by China's NPC meeting may lead to more bearish behaviour in base metal prices into the year.



Source: Bloomberg, LME, SHFE, OCBC Bank

Agriculturals: Crude palm oil prices continue to range-trade around its MYR3,000/MT handle over the week, suggesting a relatively quiet palm oil space amid an absence of news indicating stronger production into the year. Elsewhere, market-watchers had little news to trade on, except for Malaysia's stronger palm oil exports at +0.27% yoy (the first positive print since Oct 2016.

However, the key factor that could have given palm oil futures a lift is seen from emerging signs of another El Nino phenomenon in 2017. Specifically, the US National Weather Service's Climate Prediction Center indicated that La Nina conditions had disappeared as early as February 2017, and El Nino conditions could once again play out later this year. Note that the El Nino conditions seen in 2015/6 had dragged Asian palm oil production lower, resulting in elevated crude palm oil prices over the same period. Still, weather experts pencil in a mere 50% chance for El Nino to occur this year.

In other developments, note that Malaysia had highlighted its move to standardize crude palm oil export duty with Indonesia. Note that the CPO export duty was raised to 8.0% in March this year, up from 7.5%, and the mismatch in CPO export duty had led to a discount of between US$15 to US$30 per tonne in various palm oil products, according to Borneo Post. Moreover, the Malaysian government reportedly allocated MYR50 million for research and development in order to improve the safety and quality of Malaysian palm oil and its products, according to Plantation Industries and Commodities Minister Datuk Seri Mah Siew Keong, adding that Malaysia is still in the process of increasing productivity and sustainability of palm oil.

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