OCBC TREASURY RESEARCH

Weekly Commodity Outlook

14 January 2020

Commodity	Market Roundup & Opinion	Likely Price Direction
Crude oil	**Concerns over the US-Iran geopolitical tensions** have abated since the past week and prices have come off. Brent touched a high of $68.91/bbl and has sunk to $64.20/bbl as of last Monday. What is interesting is crack margins have been all over the place since the start of the year, with the mid-distillate cracks (heating oil, jet fuel, gasoil) dropping rapidly since the start of the year. Meanwhile refinery swaps on gasoline and HSFO are climbing (with HSFO still lingering deep in the red possibly due to IMO 2020-led restructuring efforts among bunkers). The mid-distillates are typically a sign of industrial strength and the rapid decline in the crack margins may be a signal that economic recovery is facing road bumps. **Separately, CFTC bets show a 16-month high of 567k net long contracts as of last Tuesday**, which we expect to have fallen since given the decline in oil prices. What is significant about that level is that it is the first time net longs have crossed the mid of the 24-month range of net spec positions (500k) since April last year, when Brent traded in the low $70/bbl range. **Short-term we expect the market to continue correcting** after last week's spike and the weaknesses seen in refinery margins. The early Chinese New Year is also expected to continue suppressing demand for now. Beyond this month, we think the risks of US-Iran tensions and improving global economic activity should continue to present upside risks to crude oil prices.	↓
Soybeans	**Hog stock in China recorded a gentle turning point in November**, rising from 202.3mn to 206.4mn heads, suggesting that a bottoming out might be in sight for the industry plagued by the ASF. Official reports have said that Chinese hog production is expected to recovery gradually through this year and return to normal by 2021, which is consistent with the turning point observed. Customs data show China buying 9.5mmt of soybeans in December, bringing the grand total in 2019 to 88.5mmt – based on USDA data, we estimate that US beans probably accounted for 30% of that 9.5mmt imports (~2.85mmt), which is higher than the current Q4 average of 25.6%. With hog stock expected to recover, a US-China trade deal to be signed this week and crush margins decently attractive at 138 RMB/mt, the base for a continued rally in soybeans remains firm in our opinion.	↑
Palm	**Palm prices touched a high of 3134 RMB/mt last Friday** but appear to have consolidated within a tight range since the start of 2020. The market continues to look heavily overbought in our opinion and we maintain our belief that selling pressure may set in by early Q2, when the dwindling in MPOB stocks start to rebound (possibly by February or March, according to our estimates). Prices of crude palm oil are at a rich premium compared to gasoil and soyoil – a return to even the lower range of normal for both spreads appears to be $100/mt for gasoil and $50/mt for soyoil. Translating that into ringgit terms at prevailing exchange rates mean a possible correction on palm prices of about 200-400 MYR/mt. Current factors, however, continue to provide hurdles for the correction to occur, especially with India's purchase of palm oil from Malaysia now thrust into the spotlight. Edible oilseed stock position in India is currently at a 5-year low; whether the country continues to buy from Malaysia or even at a premium from Indonesia, India's buying look set to persist for now.	→

Cotton	**The January WASDE report** showed little changes in US stock position, with export expectations at 16.5mil bales and production dipping a slight 100k bales due to a decline in harvested acreage estimates. World production is revised down to 120.5mil bales from 121.1mil bales, while domestic consumption remains largely unchanged, which led to a drop in global stock expectations. With logistics in Australia expected to be a challenge for the foreseeable future (with production expected to be easily near record low), the burden of cotton exports now falls squarely on Brazil in Q2 and Q3. Any signs of drought in Brazil cotton areas during this growing season could send cotton prices higher.	→
Iron Ore	**Iron ore prices climbed to an intraday high of $97.50/mt** last week and attempted another breakout today after data from China showed imports totalled 101.3mmt – close to the record volume of 102.8mmt. Interestingly, Steelhome port inventories of iron ore fell last week to 127.9mmt. The lack of a big increase in port stock despite the record import volume last month suggests the commodity is facing organic demand from steel millers, restocking early for post Chinese New Year consumption. Steel manufacturing parity is positive at about 294 RMB/mt, with steel prices unlikely to drop as Chinese authorities continue to clamp down on highly pollutive steel mills. Consistent with our Commodity Outlook report in early December, we maintain our view that iron ore might return to $100/mt in the short-term.	↑
Gold	**Gold surged to a six-year high of $1574/oz** last week as US-Iran tensions ran high. It has since rescinded to $1548/oz. Gold prices ran strongly ahead of US 10Y yields in this episode of geopolitical tensions, which led us to earlier believe that the rally might have been overdone. We maintain that view and with 10Y yields having risen back to 1.85% after falling briefly below 1.8% last week, gold looks expensive in our opinion and we think it might continue its recent correction back to the $1500/oz level. Implied vols on 1M gold have also fallen back below 10% after spiking to as high as 12.8% last week, which lends further strength to our hypothesis that gold's buying may see weakening interest.	↓

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