

FICC Research

Commodities: Daily

Focus: Base metals stocks vs. spreads



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Focus: Base metal stocks vs spreads With copper inventories starting to come under pressure, and with the physical copper market expected to tighten up amid the global economic recovery, the copper forward curve looks set to shift into a pronounced backwardation over the next few months. In contrast, aluminium looks set to remain in a fairly stable contango.

- We don't yet believe that gold can break out of the \$1,150 – \$1,100 range in which it has been since the second week of December. But downside support is increasing..
- For WTI we remain wary of the rise in speculative length. Non-commercial net long positions reached 10.4% of open interest (OI) in January. Average speculative length as a percentage of OI over the past two years was only 4%. Currently, speculative interest stands at 8.1% of OI — up from 7% last week. However, with the Fed's decision to keep monetary policy accommodative, the bias remains in favour of a higher crude oil price.
- The base metals have continued to climb this morning on the back of the Fed announcement, with sporadic short covering exacerbating the gains in some of the metals. Overall however, volumes across the complex are pretty tame.

Commodity price data (16 March 2010)

Base metals LME 3-month

	Open	Close	High	Low	Daily change	Change (%)	Cash Settle	Change in cash settle	Cash – 3m
Aluminium	2,248	2,259	2,252	2,225	31	0.49%	2,208.00	-8	-33.20
Copper	7,375	7,405	7,383	7,300	90	0.41%	7,330.00	-140	-33.50
Lead	2,222	2,221	2,226	2,200	17	-0.05%	2,185.00	-66	-28.13
Nickel	21,975	21,900	21,975	21,520	450	-0.34%	21,300.00	-500	-55.00
Tin	17,600	17,555	17,700	17,550	50	-0.26%	17,500.00	-50	-79.00
Zinc	2,301	2,307	2,309	2,261	33	0.28%	2,254.00	-76	-29.50

Energy

	Open	Close	High	Low	day/day	Change (%)
ICE Brent	80.92	81.39	81.47	80.53	0.86	1.06%
NYMEX WTI	82.04	82.45	82.56	81.72	0.75	0.91%
ICE Gasoil	675.25	677.25	678.50	672.00	5.00	0.74%
API2 Q1'10	74.75	75.20	-	-	0.45	0.60%
EUA Dec10	13.11	12.84	-	-	-0.27	-2.06%

Precious metals

	AM Fix	PM Fix	High bid	Low offer	Closing bid	Change (d/d)	EFPs
Gold	1,113.25	1,124.75	1,128.90	1,108.75	1,122.40	16.70	-.2/2
Silver	-	17.57	17.46	17.14	17.34	0.26	0/2
Platinum	1,620.00	1,624.00	1,628.00	1,620.00	1,625.00	13.00	-0.5/1.5
Palladium	462.50	467.00	473.00	463.00	471.00	-3.00	0/2

Sources: Standard Bank; LME; BBG

Please refer to the disclaimer at the end of this document.

Focus: Base metal stocks vs. spreads

With copper inventories starting to come under pressure, and with the physical copper market expected to tighten up amid the global economic recovery, the copper forward curve looks set to shift into a pronounced backwardation over the next few months. Looking at the relationship between copper stock levels and time spreads (see Fig. 1), the 3-15 month backwardation really starts to emerge as on-warrant stocks approach the 400 kt mark (currently at 500 kt), before flaring out as on-warrant stocks approach 200kt.

The recent surge in copper open interest, particularly around the Dec-11 date - currently on a par with 3-month open interest - suggests that some participants are perhaps borrowing the far-dated spreads in anticipation of a tighter market, rather than taking an outright directional view.

In contrast to copper, the far-dated aluminium curve looks set to remain in a fairly stable contango. The 3-15 month spread only starts to shift towards backwardation when on-warrant inventories slip below ~1.5 Mt (see Fig. 2). With over 4.2 Mt of on-warrant stocks in LME warehouse at the moment, and given the current low interest rate environment, the current contango may draw even more material into LME warehouses.

Aluminium is however being impacted by the prevalence of warehouse rent deals. These deals essentially tie-up material and leave the nearby market feeling tighter than it should be, given reported inventory levels. This has also resulted in elevated physical premiums. The impact of these deals, and a gradual recovery in demand has seen the 3-15 month contango tighten slightly compared with 2008 and 2009, though the impact is relatively small.

Looking ahead, the two main factors powerful enough to break the current aluminium stock situation are either; an increase in interest rates - making the returns gained by playing the contango less competitive; or a structural shift upwards in terms of real demand. With neither of these scenarios likely to occur in the near future, the farther dated portion of the aluminium forward curve looks set to remain fairly stable for the time being.

By Leon Westgate

Base metals

The Fed pledged to keep interest rates exceptionally low for an extended period last night, essentially meaning money will remain cheap. The announcement saw equities and commodities rally strongly, though the impact on the dollar has been relatively small. The base metals have continued to climb this morning, with sporadic short covering exacerbating the gains in some of the metals. Overall however, volumes across the complex are pretty tame.

BHP Billiton has halted production at its Kwinana nickel refinery in Western Australia due to a lack of hydrogen. There are no details yet with regards to lost production, with the company reportedly using the shutdown to undertake maintenance at the refinery. The news gave nickel an additional boost when it hit the headlines this morning, however prices have since run out of steam after trading back above \$22,000, and are currently drifting sideways heading into the afternoon.

Copper and aluminium have also ran out of momentum, with copper looking to consolidate above \$7,500 and aluminium struggling to push above \$2,290. Looking ahead to this afternoon, the metals will likely take direction from the US equity markets.

By Leon Westgate

Fig 1: On Warrant Copper Stock vs 3mth-15mth Spread

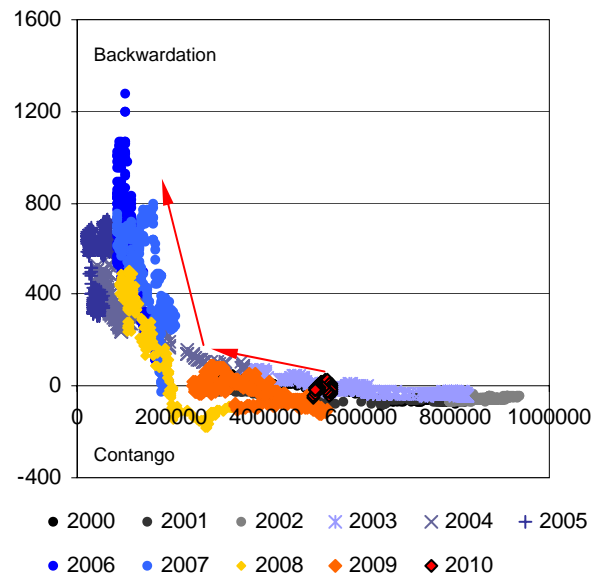
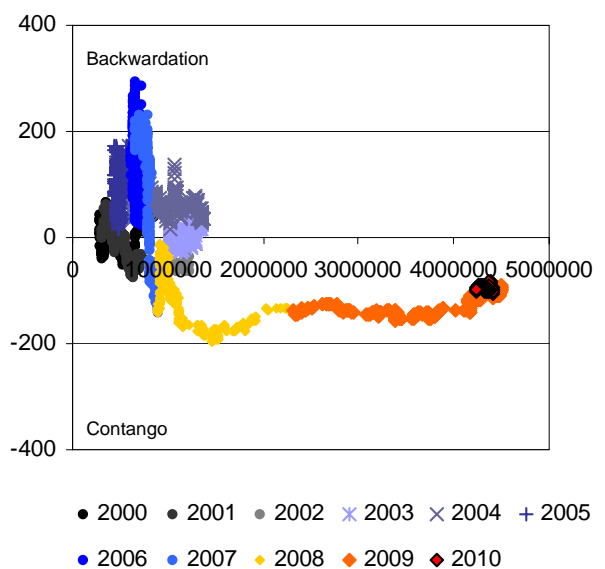


Fig 2: On Warrant Aluminium Stock vs 3mth-15mth Spread



Sources: Standard Bank, LME

Precious metals

Gold has reached higher. The \$1,100 level has been offering very strong resistance and, after failing to break below this level, the appetite to short gold may now be declining. We believe that Fed's decision to keep monetary policy accommodative should provide gold more downside support.

We don't yet believe that gold can break out of the \$1,150 – \$1,100 range in which it has been since the second week of December. But downside support is increasing. We have seen increased physical buying interest for gold on approach of \$1,100. Still, while we believe that support for gold is growing, range-trading remains our preferred strategy: sell into rallies, and buy the dips. When we change strategy, it will be to buy the dips and then staying long gold. Support is at \$1,116 and \$1,101, resistance at \$1,134 and \$1,140.

Platinum is higher, so is palladium. We are looking for platinum to test resistance at \$1,640. ETF activity in both platinum and palladium has been fairly muted in recent days. Total ETF platinum holdings now stand at 927,124oz. However, we expect platinum demand from ETFs to remain robust. This should continue to move platinum metal further away from the market. While resistance is at \$1,640, support is at \$1,610. Palladium has rallied to \$475. Support is at \$460 and resistance at \$480.

Silver support is at \$16.20 and \$16.90, resistance at \$17.60 and \$17.75. As with gold, we believe that silver will remain range-bound.

We are looking with keen interest at the oil market today. Should the DOE inventory report be bullish, we expect all commodities to enjoy good buying. Precious metals should also benefit.

By Walter de Wet

Energy

With the Fed's decision to keep monetary policy accommodative, the bias remains in favour of a higher crude oil price.

US DOE crude and product inventory data: in the headline numbers, we saw a drawdown in gasoline and distillate inventories last week. With increasing attention on gasoline, and less on distillates as we head into spring in the northern hemisphere, another draw in gasoline could see WTI retest the \$84/bbl level. An inventory draw in Cushing could assist to push prices higher. Expectations are for a 1.1m bbls build in crude inventory, while product inventory should decline by 1m and 1.3m bbls for gasoline and distillates respectively.

We remain wary of the rise in speculative length. Non-commercial net long positions reached 10.4% of open interest (OI) in January before prices declined from \$84 to \$70. Average speculative length as a percentage of OI over the past two years was only 4%. Currently, speculative interest stands at 8.1% of OI — up from 7% last week.

While we believe the global economy is recovering, we believe there could be a correction before the next move higher for crude. WTI front-month support is at \$80 and \$78.30, resistance at \$83.50 and \$84.00.

The focus is on OPEC. As the oil price has increased, OPEC's compliance with its officially targeted cut of 4.2m bpd has slipped to just 53% of this amount. Based on forecasts from tanker tracker Oil Movements, OPEC's crude oil shipments are expected to fall to 23.20m bpd in the four weeks to 27 March, down from 80k bpd to 27 bpd. This decline in shipments concurs with seasonal trends. OPEC meets in Vienna today to discuss its production policy. We expect no change to the production targets.

By Walter de Wet

Base metals

Daily LME stock movement (mt)

Metal	Today	Yesterday	In	Out	One day change	YTD change (mt)	Cancelled warrants (mt)	Cancelled warrants (%)	Contract turnover
Aluminium	4,546,025	4,537,775	14,175	5,925	8,250	-82,875	305,225	6.71	158,246
Copper	525,575	528,050	50	2,525	-2,475	23,250	21,600	4.11	123,915
Lead	170,375	170,300	75	#N/A N/A	75	23,875	12,200	7.16	28,980
Nickel	158,364	158,382	588	606	-18	354	3,684	2.33	35,098
Tin	23,730	23,600	160	30	130	-3,035	685	2.89	14,037
Zinc	540,400	539,700	1,000	300	700	52,350	3,175	0.59	77,117

Shanghai 3-month forward prices

Metal	Open	Last	1d Change
Aluminium	16,770	16,780	135
Copper	59,280	59,660	1,300
Zinc	18,735	18,840	380

COMEX active month future prices

Metal	Open	Close	Change	Change (%)
Aluminium	Ali Mar'10	-	-	-
Copper	Cu Mar'10	337	341.90	5.40
Zinc				

ZAR metal prices (16 March 2010)

	Aluminium	Copper	Lead	Nickel	Tin	Zinc	ZAR/USD fix
Cash	16,319	54,176	16,149	157,428	129,343	16,659	7.3910
3-month	16,989	55,689	16,703	164,697	132,021	17,350	7.5204

Energy

Energy futures pricing	Price Change		Price Change		Price Change		Price Change		Price Change	
	1-month forward	2-month forward	3-month forward	6-month forward	1-year forward					
Sing Gasoil (\$/bbl)	86.88	-1.37	89.50	2.46	89.41	2.54	90.25	2.28		
Gasoil 0.1% Rdam (\$/mt)	677.25	5.00	676.25	5.75	676.75	6.50	687.00	6.75		
NWE CIF jet (\$/mt)	705.57	9.92	720.75	20.32	724.08	19.91	737.39	17.53		
Singapore Kero (\$/bbl)	86.41	-1.11	89.55	2.51	89.91	2.64	91.40	2.35		
3.5% Rdam barges (\$/mt)	444.01	10.55	445.00	11.25	447.75	10.75	452.75	9.75		
1% Fuel Oil FOB (\$/mt)	462.76	9.84	468.00	11.75	473.00	10.00	488.00	9.75		
Sing FO 380 Cargo (\$/mt)	464.25	12.25	467.00	11.25	469.00	11.00	472.50	10.25		
Sing FO180 Cargo (\$/mt)	470.98	10.54	472.50	11.75	475.00	11.00	480.25	10.00		

Thermal coal	Q2-10		Q3-10		Q4-10		Cal 10		Cal 11	
API2 (CIF ARA)	75.20	0.45	78.40	0.90	81.50	0.60	90.15	0.00	100.50	-0.45
API4 (FOB RBCT)	82.50	0.15	83.00	0.50	84.20	0.30	88.20	0.00	95.50	-0.45

Precious metals

Forwards (%)	1-month	2-month	3-month	6-month	12-month
Gold	0.22200	0.23000	0.23600	0.32200	0.49400
Silver	0.54000	0.54400	0.55400	0.56600	0.60600
USD Libor	0.23563	0.24650	0.26088	0.40125	0.87175

Technical Indicators	30-day RSI	10-day MA	20-day MA	100-day MA	200-day MA	Support	Resistance
Gold	50.69	1,119.28	1,116.03	1,116.62	1,044.89	1,085.00	1,120.00
Silver	53.17	17.18	16.69	17.25	16.21	16.30	16.90
Platinum	60.49	1,598.25	1,565.37	1,491.72	1,370.57	1,550.00	1,600.00
Palladium	59.21	463.86	448.67	401.54	340.13	435.00	470.00

Active Month Future	COMEX GLD	COMEX SLV	NYMEX PAL	NYMEX PLAT	DGEX GLD	TOCOM GLD	CBOT GLD
	Feb'10	Mar'10	Mar'10	Apr'10	Feb'10	Dec'10	Feb'10
Settlement	1,112.10	17,2750	464.75	1,615.80	1,112.00	3,246.00	1,112.30
Open Interest	507,046	112,813	23,045	36,417	1,331	106,720	2,513
Change in Open Interest	-13,001	-1,205	531	275	0	339	66

Date: 16 March 2010

Sources: Standard Bank; LME; Bloomberg

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