

# FICC Research

## Commodities: Daily

### Focus: Lots of noise around long-term drivers



29 July 2010

Walter de Wet, CFA\*  
Walter.DeWet@standardbank.com

Leon Westgate\*  
Leon.Westgate@standardbank.com

- Focus: Lots of noise around long-term drivers — Until either interest rates start to rise or liquidity decline we believe gold's investment case remains intact. We have not seen any evidence yet that either of the two will move against gold.
- Looking at PGM, like base metals, they are increasingly following equities in recent days. As a result, short-term our focus remains on equity markets.
- Short covering activity has emerged across much of the base metals complex this morning, seeing the market spark into life after a moribund overnight trading session.
- The DOE crude oil inventory data was much more bearish than expected, with Crude stocks climbing 7.3 million bbl compared to expectations of a 1.7 million bbl decline. Aside from a knee-jerk reaction to the data, crude oil prices actually absorbed the news pretty well, with front month WTI closing the day virtually unchanged.

#### Commodity price data (28 July 2010)

##### Base metals LME 3-month

	Open	Close	High	Low	Daily change	Change (%)	Cash Settle	Change in cash settle	Cash – 3m
Aluminium	2,060	2,057	2,086	2,054	-3	-0.15%	2,045.00	24	-20.75
Copper	7,130	7,060	7,213	7,036	-70	-0.98%	7,091.50	96	-24.00
Lead	1,996	1,977	2,030	1,960	-19	-0.97%	1,975.00	15	-22.00
Nickel	20,799	20,550	20,945	20,370	-249	-1.20%	20,725.00	310	-71.86
Tin	19,500	19,330	2,042	19,325	-170	-0.87%	19,500.00	265	-30.20
Zinc	1,947	1,909	1,968	1,908	-38	-1.95%	1,907.00	24	-27.63

##### Energy

	Open	Close	High	Low	day/day	Change (%)
ICE Brent	75.98	76.16	76.23	75.86	0.10	0.13%
NYMEX WTI	76.89	77.13	77.23	76.78	0.14	0.18%
ICE Gasoil	639.75	642.00	642.00	639.50	3.50	0.55%
API2 Q3'10	92.60	92.60	-	-	0.00	0.00%
EUA Dec10	13.54	13.75	-	-	0.21	1.55%

##### Precious metals

	AM Fix	PM Fix	High bid	Low offer	Closing bid	Change (d/d)	EFPs
Gold	1,164.00	1,157.00	1,164.00	1,158.00	1,160.00	1.00	2.3/2.7
Silver	1,763.00	17.62	17.72	17.35	17.42	-0.21	-1.0/1.0
Platinum	1,540.00	1,535.00	1,542.00	1,536.00	1,535.00	0.00	1.5/3.5
Palladium	470.00	469.00	469.00	468.00	467.00	2.00	-0.5/1.5

Sources: Standard Bank; LME; BBG

### Focus: Gold — lots of noise around long-term drivers

Although gold has fallen sharply from the highs reached in June we believe gold will still head higher towards the end of the year despite the current price action. While we are seeing strong physical demand for gold already (*refer to our physical flow index in Commodities Daily 27 Jul'10*), we believe investment demand for gold will remain in place.

Liquidity (as we measure it when analysing gold) is ample and interest rates are low; as a result investment demand for gold is likely to remain in place. We view liquidity and interest rates as fundamental drivers for gold investment demand. We measure global liquidity as the US Fed balance sheet plus global foreign reserves holdings excluding gold. YTD, our measure of global liquidity is up 9.4%. The gold price is up 8% YTD.

As ETFs are accessed by institutional and retail investors, ETFs is an important vehicle for liquidity and low interest rates to be channeled into gold demand. Given the rise in liquidity it is not surprising that total ETF holdings now stand at 2030 tonnes — up from 1,800 tonnes at the start of May. Since the start of 2009, gold ETF holdings have increased almost 72%. Liquidations by ETF's have also proved to remain low with minimal liquidation in the face of heightened market volatility in the past two years.

Given the relationship between liquidity and commodities, we have found that gold specifically are the main beneficiary. In fact, gold has been shadowing global liquidity very closely (see graph).

While short-term, other factors such as equity price movements and currency moves influence the gold price, we believe these factors are not long-term drivers. For example, rising equities and

### Base metals

Short covering activity has emerged across much of the base metals complex this morning, seeing the market spark into life after a moribund overnight trading session. A stronger euro and firmer equities appear to be the main reason for the strength, with weak shorts, tempted into the market after prices stalled yesterday afternoon, heading for the exit.

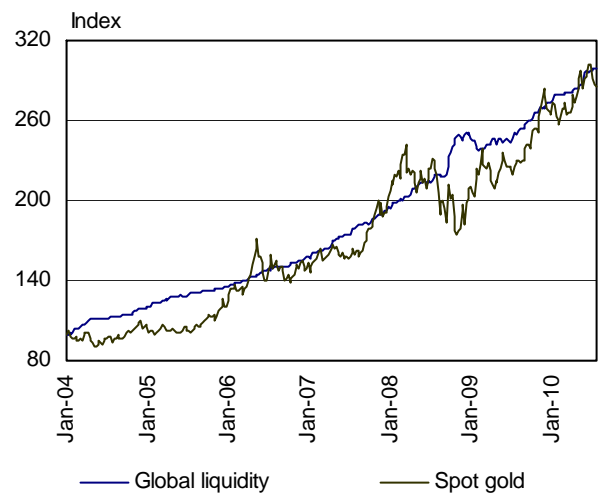
Copper looked to have run out of steam during Wednesday afternoon, absorbing the worse than expected US data but failing to push higher. In the face of stronger equity markets and a weaker dollar this morning however, prices have continued to push higher with short covering activity exacerbating the rally.

In China, although the SHFE-LME copper arbitrage ratio has dropped to 7.84, overnight volumes were far from exceptional with only light arbitrage activity emerging. Rather than dictating copper prices for the day ahead, as is the case when China is in the driving seat, the SHFE market appears to be on the defensive for the moment, reacting to the previous day's price activity on the LME. Of note, physical SHFE copper is trading at around a \$30 discount to the SHFE front month contract, suggesting physical demand has dried up in the face of stronger prices.

In contrast to copper, there has been mounting SHFE-LME arbitrage interest in Zinc over the past couple of days. LME volumes remain subdued however, while price-wise the metal has been dominated by short covering heading into the early afternoon.

Nickel inventories have started to edge higher over the past couple of days, with this morning seeing headline stocks climb 444 mt. That said, on-warrant stocks actually fell 6 mt, with fresh warrant cancellations in Asia and Europe offsetting the increase. Seasonally speaking, August through December typically sees rising LME inventories. Stable or increasing stocks over the balance of the year are therefore to be expected, with further sustained inventory draws a bullish signal instead.

### Gold vs. global liquidity



Source: Standard Bank

a rising gold price between 2003 and 2007 are not consistent with an argument that gold should fall when equities rise over a longer time horizon. Equities also rose since mid-2009 and gold pushed higher at the same time.

Until either interest rates start to rise or liquidity decline, we believe gold's investment case remains intact. We have not seen any evidence yet that either of the two will move against gold. When we see this evidence will reconsider our longer-term view on gold. Our target for gold remains \$1,300 on a six month horizon.

By Walter de Wet

By Leon Westgate

## Precious metals

Gold's technical outlook has not changed since yesterday — technically the metal looks bearish below \$1,176. At the same time we are seeing increased physical demand as the gold price push lower. The bear trend from the \$1,264.90 high could extend to \$1,140 and possibly \$1,125. However, we remain constructive on gold on a 6-month horizon (refer to the Focus section).

Looking at PGM, like base metals, they are increasingly following equities in recent days. As a result, short-term our focus remains on equity markets. However, we also look at EM FX for PGM price direction. Although currencies in general have become irrelevant to commodity price moves in recent days, we look at EM FX for further indication of market sentiment towards risk. EM FX in general is stronger since the start of the week which is consistent with increased risk appetite. This should support PGM prices.

Longer-term we believe our fundamental view (based on cost-curve analysis) that platinum and palladium below \$1,500 and \$420 respectively provide good value is growing in support. The recent factor in support of this view is a strong ZAR and adds support on the downside for PGM prices. A stronger ZAR puts more pressure on SA platinum producers' revenue stream. The ZAR/USD exchange rate has strengthened from \$8.00 in May to below \$7.30 this morning.

Platinum support is at \$1,520 and \$1,508, resistance at \$1,554. Palladium support is at \$463 and \$457 and resistance at \$476 and \$484. We see silver support at \$17.40 and \$17.15. Resistance for silver is at \$18.05 and \$18.45.

**By Walter de Wet**

## Energy

The DOE crude oil inventory data was much more bearish than expected, with Crude stocks climbing 7.3 million bbl compared to expectations of a 1.7 million bbl decline. Aside from a knee-jerk reaction to the data, crude oil prices actually absorbed the news pretty well, with front month WTI closing the day virtually unchanged. This morning has seen crude prices trade sideways to lower, with the weaker dollar having little impact on prices.

Aside from the headline crude oil figures, the DOE inventory numbers for gasoline and distillates were more positive, climbing by 91 k and 938 k bbl respectively, and significantly below expectations. Cushing stocks climbed by 66 K bbl, also way below the 985 k increase seen last week.

In other news, OPEC's crude oil output increased in July, gaining 0.3% or 80,000 bbl/day, to 29.24 million bbl/day. In terms of compliance with quota levels, the figure fell to 52.9% from 53.6% in June.

The German power market remains a key driver of coal prices, with the wider global markets having little impact. Overall however the markets are quiet, winding down early ahead of the traditionally quieter summer period. API2 for Q4-10 was unchanged yesterday, finishing at \$92.60, while Cal-11 posted only a \$0.15/mt gain. API4 was similarly uneventful, with Q4-10 also unchanged and Cal-11 up only \$0.25/mt

**By Leon Westgate**

## 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	4,390,625	4,395,125	4,400	8,900	-4,500	-238,275	233,350	5.31	135,233
Copper	411,525	411,425	2,800	2,700	100	-90,800	35,650	8.66	86,876
Lead	183,825	183,350	600	125	475	37,325	4,150	2.26	32,630
Nickel	116,778	116,334	678	234	444	-41,232	4,824	4.13	22,808
Tin	15,050	15,155	25	130	-105	-11,715	835	5.55	6,041
Zinc	619,725	619,725	850	850	0	131,675	21,475	3.47	62,324

### Shanghai 3-month forward prices

### COMEX active month future prices

Metal	Open	Last	1d Change		Open	Close	Change	Change (%)
Aluminium	15,440	15,400	-15	Ali Jul'10	-	-	-	-
Copper	56,100	56,230	660	Cu Jul'10	325	324.65	0.10	0.03%
Zinc	16,200	16,240	190					

### ZAR metal prices (28 July 2010)

	Aluminium	Copper	Lead	Nickel	Tin	Zinc	ZAR/USD fix
Cash	15,120	52,286	14,452	150,064	142,537	14,125	7.3435
3-month	15,422	53,480	15,038	152,130	145,533	14,572	7.4537

## 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)	84.50	0.00	85.68	-0.38	86.00	-0.29	87.65	-0.20	-	-
Gasoil 0.1% Rdam (\$/mt)	642.00	3.50	647.75	3.25	651.25	1.00	664.25	-1.50		
NWE CIF jet (\$/mt)	687.08	-0.34	693.82	-2.84	699.92	-2.41	718.11	-1.12		
Singapore Kero (\$/bbl)	85.23	-0.25	86.28	-0.33	87.00	-0.24	89.00	-0.18		
3.5% Rdam barges (\$/mt)	418.02	-0.46	424.25	-1.75	423.50	-1.75	429.75	-1.50		
1% Fuel Oil FOB (\$/mt)	456.52	-0.40	460.25	-0.50	461.25	-0.25	470.00	0.50		
Sing FO 380 Cargo (\$/mt)	100.15	-349.60	100.15	-349.60	100.15	-349.60	100.15	-349.60		
Sing FO180 Cargo (\$/mt)	446.45	-0.34	449.75	-1.00	450.25	-1.50	457.75	-1.75		

### Thermal coal

	Q3-10	Q4-10	Q1-11	Cal 11	Cal 12
API2 (CIF ARA)	92.60	0.00	94.70	0.20	96.50
API4 (FOB RBCT)	89.50	0.00	91.60	0.50	93.00

## Precious metals

Forwards (%)	1-month	2-month	3-month	6-month	12-month
Gold	0.37200	0.44600	0.48200	0.54200	0.60000
Silver	0.70833	0.70833	0.73500	0.77667	0.78500
USD Libor	0.31563	0.38906	0.47500	0.68794	1.06438

Technical Indicators	30-day RSI	10-day MA	20-day MA	100-day MA	200-day MA	Support	Resistance
Gold	44.67	1,181.35	1,193.26	1,183.50	1,149.12	1,150.00	1,176.00
Silver	46.46	17.79	17.92	18.09	17.67	17.40	18.00
Platinum	48.53	1,528.82	1,524.22	1,606.80	1,545.04	1,535.00	1,565.00
Palladium	51.82	459.93	455.45	482.50	440.06	465.00	485.00

Active Month Future	COMEX GLD	COMEX SLV	NYMEX PAL	NYMEX PLAT	DGCX GLD	TOCOM GLD	CBOT GLD
	Aug'10	Sep'10	Sep'10	Oct'10	Aug'10	Jun'11	Aug'10
Settlement	1,169.20	17.5950	474.50	1,541.70	1,165.50	3,285.00	1,165.10
Open Interest	560,066	117,370	20,201	28,971	1,273	109,585	2,574
Change in Open Interest	-9,049	-826	-367	-217	31	-717	-66

Date: 27 July 2010

Sources: Standard Bank; LME; Bloomberg

## Disclaimer

### Certification

The analyst(s) who prepared this research report (denoted by an asterisk\*) hereby certifies(y) that: (i) all of the views and opinions expressed in this research report accurately reflect the research analyst's(s') personal views about the subject investment(s) and issuer(s) and (ii) no part of the analyst's(s') compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed by the analyst(s) in this research report.

### Conflict of Interest

It is the policy of The Standard Bank Group Limited and its worldwide affiliates and subsidiaries (together the "Standard Bank Group") that research analysts may not be involved in activities in a way that suggests that he or she is representing the interests of any member of the Standard Bank Group or its clients if this is reasonably likely to appear to be inconsistent with providing independent investment research. In addition research analysts' reporting lines are structured so as to avoid any conflict of interests. For example, research analysts cannot be subject to the supervision or control of anyone in the Standard Bank Group's investment banking or sales and trading departments. However, such sales and trading departments may trade, as principal, on the basis of the research analyst's published research. Therefore, the proprietary interests of those sales and trading departments may conflict with your interests. **Please note that one or more of the analysts that prepared this report sit on a sales and trading desk of the Standard Bank Group.**

### Legal Entities:

To U. S. Residents

Standard New York Securities, Inc. is registered with the Securities and Exchange Commission as a broker-dealer and is also a member of the FINRA and SIPC. Standard Americas, Inc is registered as a commodity trading advisor and a commodity pool operator with the CFTC and is also a member of the NFA. Both are affiliates of Standard Bank Plc and Standard Bank of South Africa. Standard New York Securities, Inc is responsible for the dissemination of this research report in the United States. Any recipient of this research in the United States wishing to effect a transaction in any security mentioned herein should do so by contacting Standard New York Securities, Inc.

To South African Residents

The Standard Bank of South Africa Limited (Reg.No.1962/000738/06) is regulated by the South African Reserve Bank and is an Authorised Financial Services Provider.

To U.K. Residents

Standard Bank Plc is authorised and regulated by the Financial Services Authority (register number 124823) and is an affiliate of Standard Bank of South Africa. The information contained herein does not apply to, and should not be relied upon by, retail customers.

### General

This research report is based on information from sources that Standard Bank Group believes to be reliable. Whilst every care has been taken in preparing this document, no research analyst or member of the Standard Bank Group gives any representation, warranty or undertaking and accepts no responsibility or liability as to the accuracy or completeness of the information set out in this document (except with respect to any disclosures relative to members of the Standard Bank Group and the research analyst's involvement with any issuer referred to above).

All views, opinions and estimates contained in this document may be changed after publication at any time without notice. Past performance is not indicative of future results. The investments and strategies discussed here may not be suitable for all investors or any particular class of investors; if you have any doubts you should consult your investment advisor. The investments discussed may fluctuate in price or value.

Changes in rates of exchange may have an adverse effect on the value of investments. This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. Members of Standard Bank Group may act as placement agent, advisor or lender, make a market in, or may have been a manager or a co-manager of, the most recent public offering in respect of any investments or issuers referenced in this report. Members of the Standard Bank Group and/or their respective directors and employees may own the investments of any of the issuers discussed herein and may sell them to or buy them from customers on a principal basis. This report is intended solely for clients and prospective clients of members of the Standard Bank Group and is not intended for, and may not be relied on by, retail customers or persons to whom this report may not be provided by law. This report is for information purposes only and may not be reproduced or distributed to any other person without the prior consent of a member of the Standard Bank Group. Unauthorised use or disclosure of this document is strictly prohibited. By accepting this document, you agree to be bound by the foregoing limitations. Copyright 2010 Standard Bank Group. All rights reserved.