Commodities higher as bad news become good news for risk

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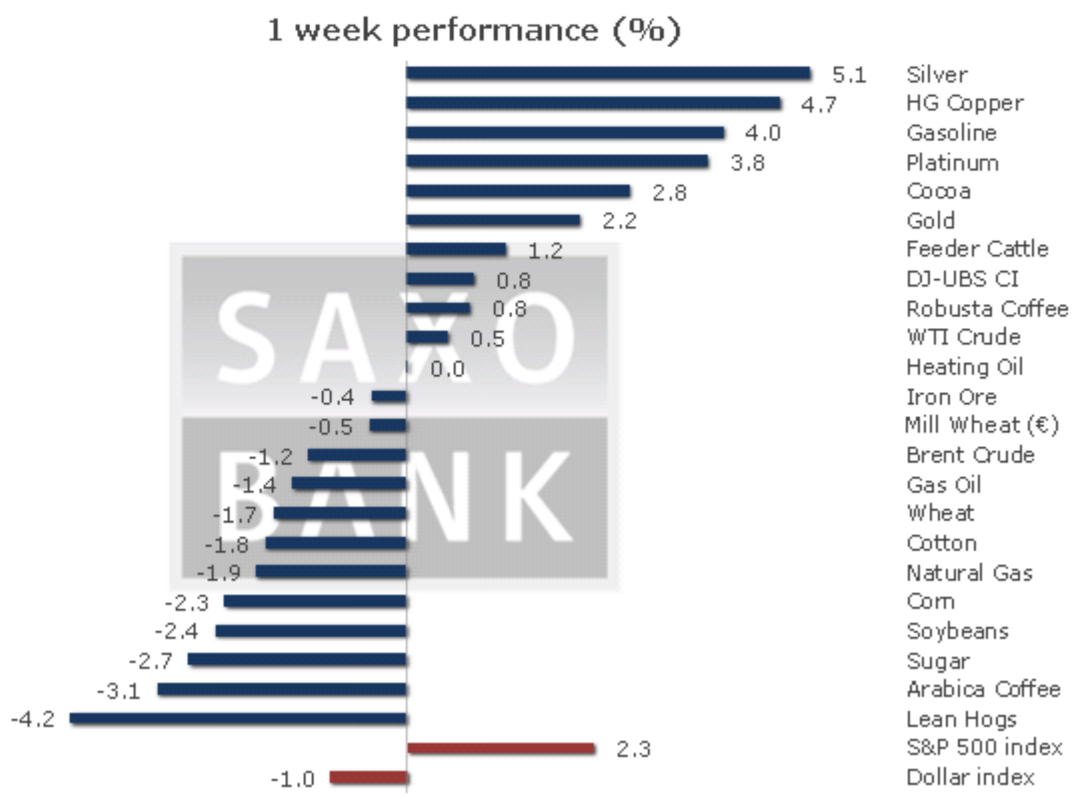
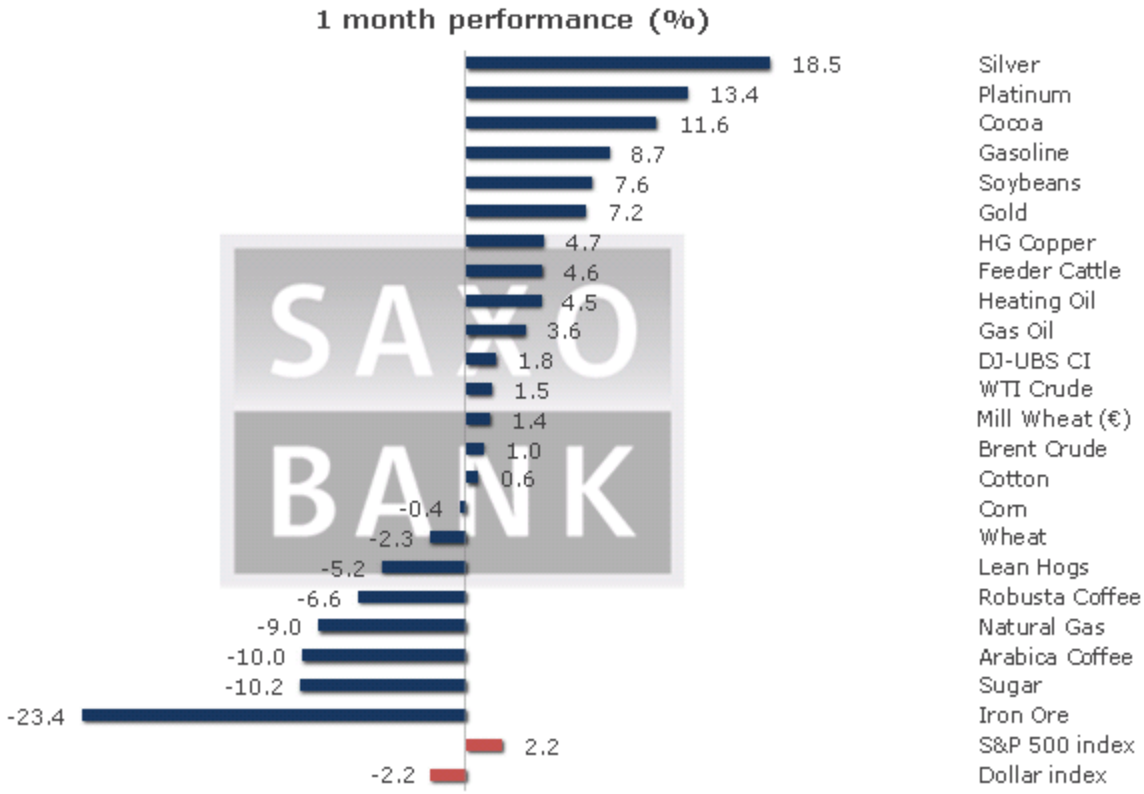
Commodities were generally higher and the dollar fell following the two major risk events; first the ECB and then the monthly US unemployment report. While the ECB delivered what was expected in terms of new initiatives to keep funding markets open to troubled economies the US jobs report was weaker than expected, once again proving that bad news is good news for the market as it helps raise expectations that additional stimulus will be announced at the US Federal Open Market Committee meeting on September 13.

The broad-based DJ-UBS commodity index reached the highest level since March as gains were recorded in both metal groups and energy. The agriculture sector ran into some selling, primarily driven by coffee and sugar, which both reached the lowest levels in two years. Copper one of the surprise performers hit the highest level since May on raised hopes that additional stimulus will help growth and demand. Gasoline was another winner as the recent hurricane Isaac helped trigger a drop in US inventories to a 33-month low as some refineries along the Gulf Coast had been forced to shut down production temporarily.



Source: Bloomberg and Saxo Bank Strategy & Research

Monthly performance if preferred:



Source: Bloomberg and Saxo Bank Stategy and Research

Crude oil looking for the next driver

The confirmation of the ECB bond buying programme and weak US jobs report helped stocks to rally but had limited impact on both WTI and Brent crude oil as they continued to be range-bound with traders reluctant to take prices much higher at this stage as the possibility of a release from Strategic Petroleum Reserves (SPR) continues to linger. A stubbornly high price for US gasoline, which is trading close to the highest level of the year, is unnerving the US administration and it was reported that a meeting with oil experts had been held as it considers a release, potentially much larger than the one seen following the war in Libya in 2011.

Near-term price risk skewed to the downside

Brent crude has now spent one month confined in a range between 111.65 USD/barrel defined by its -day moving average and resistance at 116.60 USD/barrel. The failure to move higher in recent weeks, despite stimulus speculation and a weaker dollar, combined with slowing momentum, leaves the near-term risk skewed to the downside, not least considering the amount of speculative buying that has been witnessed in recent weeks. A great amount of investors in recently established new speculative longs will have to reconsider their positions on a move below the 200-day moving average.

The option market is also pointing towards a greater need to protect downside risk with out-the-money (OTM) put volatility being almost four percent costlier than OTM calls, after having seen a rise of five percent during the last week.

Brent Crude, first month cont., USD/barrel – Source: Saxo Bank

Copper jumps on China prospects

Sentiment in the depressed industrial metal markets has improved with copper reaching the highest level in almost four months on a combination of supporting news which could help improve demand and lower levels of available stock. Hopes that Europe will begin to recover following the newest initiative from the ECB and China's approval of a multi-billion dollar infrastructure programme drove the market higher. This was the kind of news that the depressed sector had been looking for and speculative traders have been busy reducing the gross short position which has remained elevated since May.

High Grade Copper, first month cont. Cent/lb. – Source: Saxo Bank

Gold and silver continue higher as stimulus seems assured

Gold continued to build on its recent strength and rose to a six-month high above 1700 USD/oz. as additional quantitative easing in the US moved a step closer following the weak jobs report. Silver as usual jumped the most and also reached the highest level since March and its 18 percent rally during the last month makes it the best performing commodity during this period.

With positive momentum now back after several months of sideways trading we have seen hedge funds and other leveraged investors jumping back into gold and silver. In just two weeks the net long position in gold has risen by 40 percent and for now these new longs are comfortable in the money and therefore do not pose any near-term threat of long liquidation, especially as long as the 200-day moving average at 1,641 USD/barrel is not threatened. Options traders had up until the ECB meeting been paying up for call volatility, but as we head into next week's FOMC meeting put volatility has seen most of the bidding, which indicates some near-term nervousness about a potential correction following the strong push higher.

Spot Gold, USD/oz. – Source: Saxo Bank

Grain markets await US crop report

Attention in grain markets has switched to September 12 when the United States Department of Agriculture will release its monthly World Agriculture Supply and Demand estimates (WASDE). During the week we saw the price of soybeans come under mild selling pressure after having made a new record high as recent rainfall over the US Midwest has improved harvest prospects.

Wheat prices initially held back following news that US exports were struggling to compete with those of Russian origin but the market remains unconvinced that Russia will be able to continue to export throughout this marketing year, following a drought this summer which has resulted in a lower grain production this year compared with 2010, when export restrictions were implemented, something Russia has said will not happen this year.

The price of corn has just like that of soybeans eased off recently but there have been no major attempts on support at 7.85 USD/bushel. The WASDE report is expected to show a further cut in 2012/13 production compared with the USDA's August estimates and this continues to apply upside pressure on prices in order to ensure enough rationing to preserve global stock levels.

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