

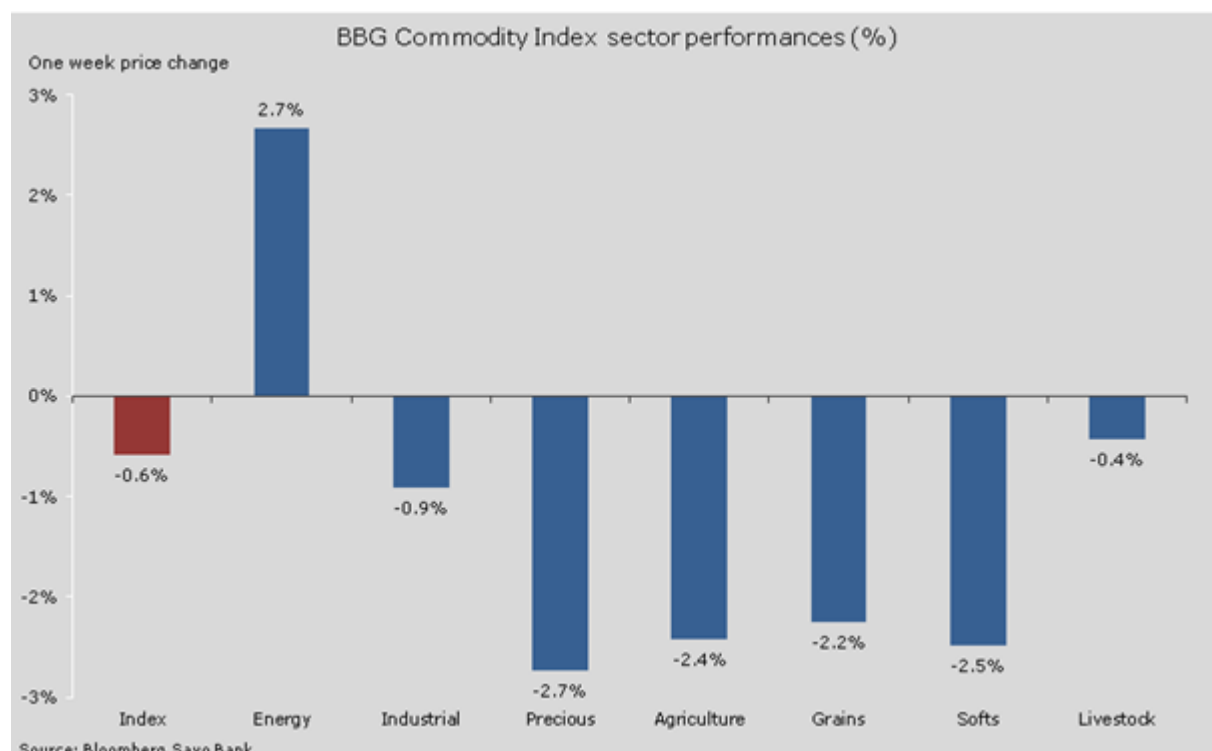


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Dollar's ascent piles pressure on commodities as polar vortex looms

Commodity prices remain under pressure across all sectors as the dollar continues to rise while rising supplies of many key commodities from energy through metals to food is not being met by an equal rise in demand. The outlook for global growth remains subdued, not least in Europe and China.

Several commodities from iron ore to crude oil and gold hit new lows as bears have taken control of the price action for now. The Bloomberg Commodity Index of 22 leading commodities touched a new five-year low before a dramatic rally in natural gas helped support a small recovery in the index.



Source: Bloomberg, Saxo Bank

The precious metal sector was the hardest hit for a second week in a row with both gold and silver continuing to be sold following the technical break below USD 1180/oz. on gold. Soft commodities were all lower, led by sugar on ample supply, while the strong dollar together with the removal of the Ebola premium saw cocoa drop to a six-month low.

Grains were also lower following five weeks of gains as record US supplies begin to hit the market. The UN's Food & Agriculture Organisation forecast that world grain reserves would reach a 15-year high during the 2014-15 period and this could weigh on the price of key crops such as corn and wheat.

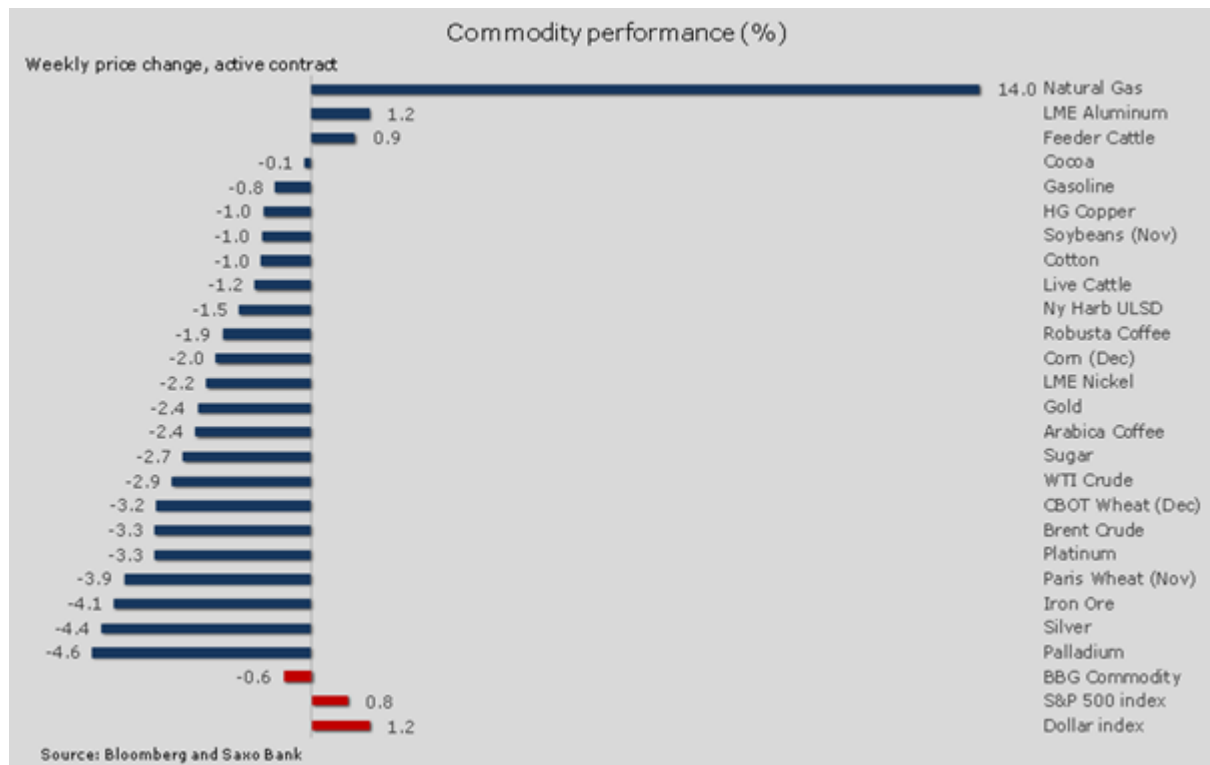
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Source: Bloomberg, Saxo Bank

The individual performance table gives a clear picture of the overall negative sentiment in commodities at the moment. All but a few suffered losses during the past week with natural gas being an almost extreme exception. Since October 28 the current futures contract for December delivery has rallied by almost one quarter as the early arrival of winter has brought back memories of the dramatic price spikes seen back in January when record gas demand drove inventories to a uncomfortably low levels.

A large blast of Arctic air or [polar vortex](#) is expected to hit the US next week and this could drive temperatures to at least 6 degrees Celsius below normal and sharply increase demand for natural gas, which heats around half the homes in the US. Most of the gas that was consumed during last winter's frigid weather has been replaced but the return of colder than normal weather so early in the season has raised concerns about a repeat of last winter.

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Return of the polar vortex? Planalytics, a business weather intelligence company, reckons the last one cost the US economy \$5bn. Photo: AccuWeather

Crude oil came under renewed selling pressure with supply continuing to rise faster than demand. OPEC, in its annual World Oil Outlook, reduced the forecast for how much the cartel need to supply all the way out to 2035 citing the ongoing shale boom, especially in the US, as the primary reason for cutting the outlook.

The price of both WTI and Brent crude oil, however, did manage to find some support as concerns about Libya's ability to maintain its recent production gains were highlighted after production from its biggest field was temporarily halted following an attack by militias. Meanwhile in the US, the weekly inventories rose by less than expected as refinery demand, against expectations, rose for the first time since September. This could be the first indication that the seasonal pick up in demand as begun.

The OPEC meeting on November 27 is going to receive a lot of attention considering the challenge the cartel is currently facing. OPEC is currently producing around 30.5 million barrels per day (bpd) as the International Energy Agency only expects some 29.3 million bpd will be needed throughout 2015. A cut of 1 million barrels per day is now increasingly required just to stabilise prices so lack of action carries the risk of sending oil down even further.

Another important date for oil markets and the near-term direction of the price is the November 24 deadline for reaching a deal between six major powers and Iran over its nuclear program. President Obama, who is in need of a success story following the defeat at the midterm election, has a strong incentive to push the negotiations towards a successful conclusion. The potential lifting of sanctions would trigger a sharp increase in exports from Iran as it would insist on reclaiming the market share that was lost when sanctions were imposed back in 2012.



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WTI crude has reached an important area of support ahead of the 2011 low at USD 75/barrel and although it remains stuck within a negative trend we believe that most of the selling could now be behind us. A meaningful recovery however can only happen when the current supply surplus begins to shrink, either through reduced supply and/or increased demand. So while we expect the price of WTI crude to remain above USD 75/barrel it will require a break above 80 dollars before short covering could take it back to resistance at USD 83/barrels.



Source: Saxo Bank

Gold traded in dollars continues to suffer from the adverse impact of a rising dollar and falling energy prices. As commodity prices falls so do the inflationary pressures. And in order to avoid the deflationary trap, increases in quantitative easing from the likes of the European Central Bank and the Bank of Japan further supports the dollar. This has now become a vicious circle from where gold and silver are struggling to escape and as a result both metals have fallen to their lowest level since 2010.

Gold's slide in the rout of Q2 last year was eventually halted by strong physical buying from China. So far there has been no sign of a similar pick up in demand with the spot price on the Shanghai Gold Exchange trading flat relative to London compared with a premium last month. Without a pick up in physical demand the bears are left in control leaving the upside potential limited as rallies will be viewed as a new selling opportunity.

Only a move back above USD 1180/oz could trigger a major round of short covering and signalling a move back towards a neutral stance. Attention is currently removed from the Swiss Gold referendum on November 30 as recent polls have indicating fading support for this initiative which otherwise could have provided a major boost to the price of gold.

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Ole Sloth Hansen is a specialist in all traded Futures, with over 20 years' experience both on the buy and sell side. Hansen joined Saxo Bank in 2008 and is today Head of Commodity Strategy focusing on a diversified range of products from fixed income to commodities. He previously worked for 15 years in London, most recently for a multi-asset Futures and Forex Hedge fund, where he was in charge of the trade execution team. He is available for comments on most commodities, especially energies and precious metals.

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