



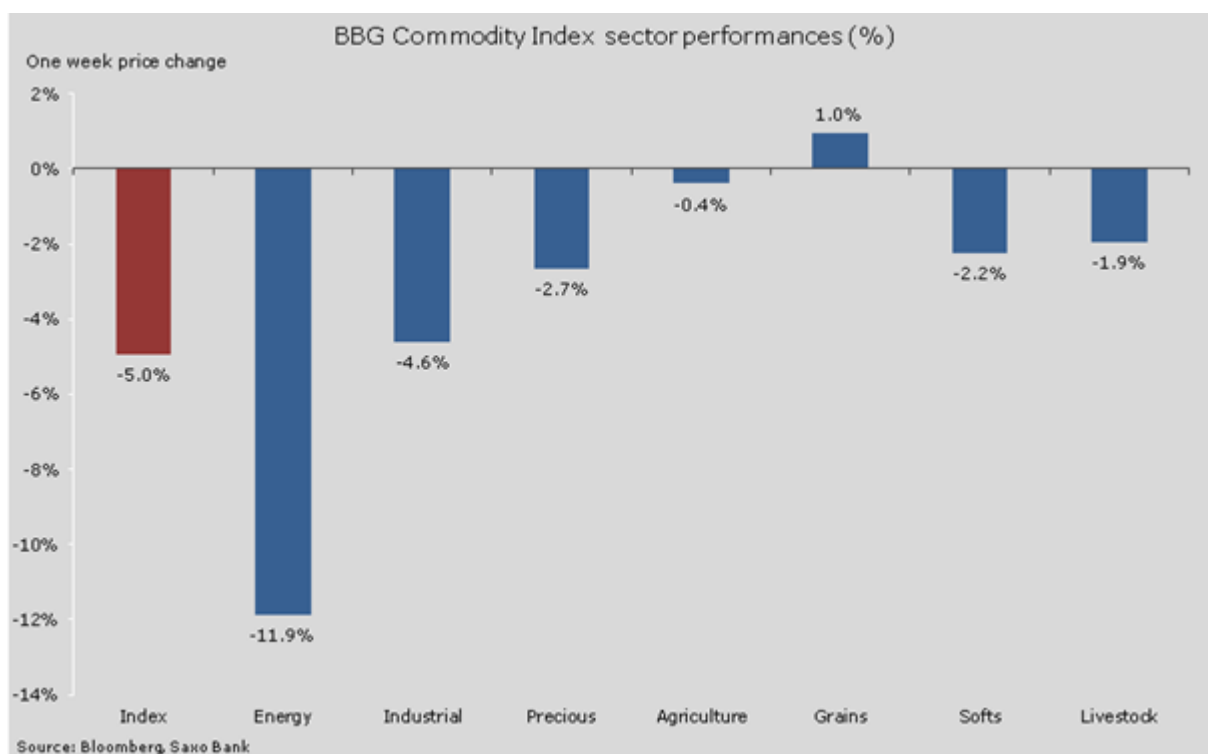
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Commodities take a breather after torrid November

Commodities have fallen to a five-year low, leaving producers of most raw materials with little to cheer about during the past month (and especially during the last week). Most notable was the accelerated selling that hit the energy market following last week's Opec meeting.

The cartel's unwillingness to cut production — thereby signalling a "battle" for market share against other, non-Opec producers — was the final straw, and it triggered a slump in oil prices to a new five-year low. A monthly collapse of this magnitude in Brent crude has only been seen on four occasions since 1988.

Industrial metals were the second-worst performer as the sharp declines in energy, together with weaker-than-expected manufacturing data from both China and Europe, had copper on the defensive. The break of key support on Friday triggered an extension to the lowest level in four years before a weaker dollar helped to stabilise the price. Having broken support, however, the risk of seeing further losses before support eventually gets re-established is rising.



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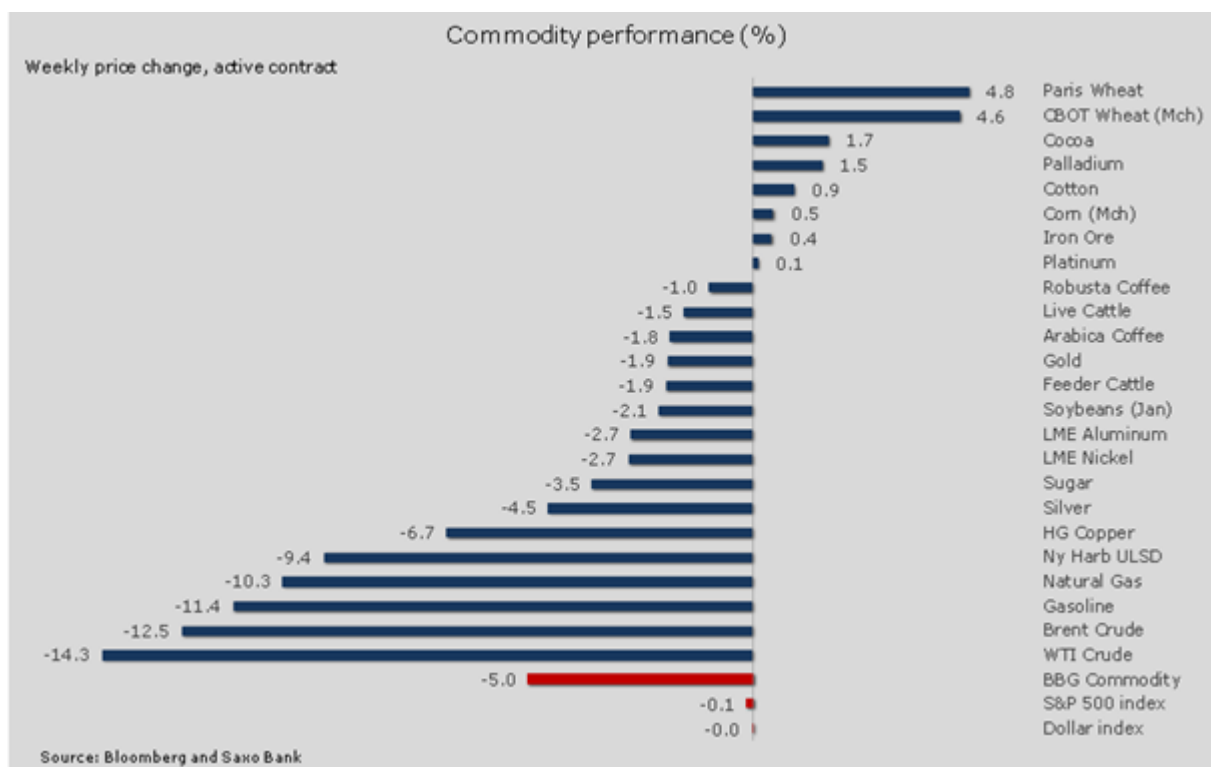
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Precious metals finally got the Swiss gold referendum out of the way and the resounding "No" initially triggered a selloff in which silver reached a five-year low. Sellers, however, were forced to cover shorts as the combination of a weaker dollar and signs of physical demand in Asia helped trigger a major short squeeze in both metals.

This squeeze was, again, felt heavily in silver as low liquidity helped trigger a Monday trading range of more than 13%. The sector could still struggle as attention returns to the diverging action between the US Federal Reserve and other central banks, as well as the continued downward pressure on inflation caused by lower commodity prices.

December has arrived, and with it we could increasingly see low liquidity moves triggering higher levels of volatility. Traders are increasingly moving into a defensive mode where profits are being protected and losses are less tolerated than they are during any other time of the year.

The strong recovery in gold and silver on Monday was a good reflection of this attitude, and commodities that feature extreme positioning one way or the other could find themselves at the receiving end of counter-moves.



The energy sector and the ongoing price slump continue to attract most of the attention in commodities. Last Thursday's surprise decision by Opec to do nothing in terms of cutting supply has sent crude oil prices into a tailspin as the battle for market share in an oversupplied market continues.

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Following a torrid November (which yielded the biggest monthly losses in almost six years), December kicked off with similarly weak trading, with crude oil futures slumping to a new five-year low before establishing a bid supported by both oversold conditions and a weaker dollar.

The impact of a prolonged period of lower energy prices should positively impact the global economy over the next six to nine months as a massive redistribution of money from producers to consumers increases consumer confidence and reduces input cost for manufacturers.

The winners are likely to be the biggest consumers (such as the USA, China and India), while the losers can be found among producers such as Russia and Venezuela, where a lack of investment and diversification leaves these countries exposed to the sharp reduction in government revenues.

The US shale industry: what to look out for?

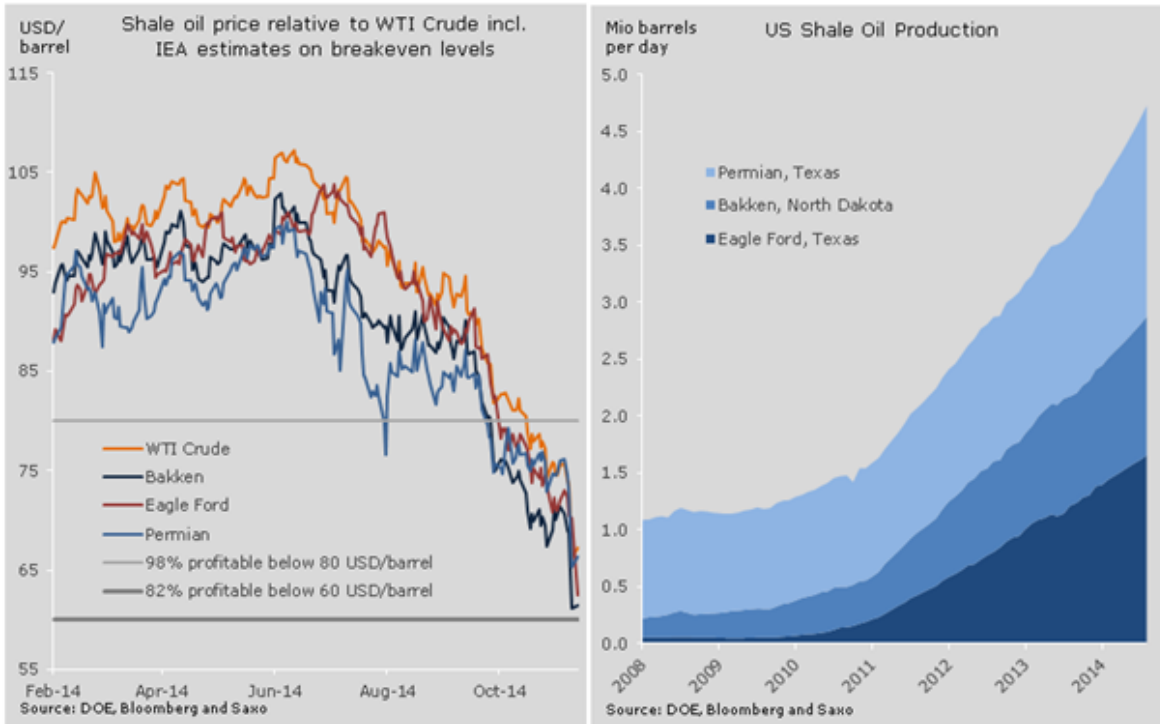
With Opec signalling its willingness to endure some pain in order to put pressure on other producers — not least the US shale oil industry — the focus naturally shifts to the US for clues as to how the industry there is dealing with deteriorating prices.

US crude oil production is running at its highest level since at least 1983, and given the current oversupply in global markets, traders will be looking for clues as to how production data develop over the coming weeks and months.

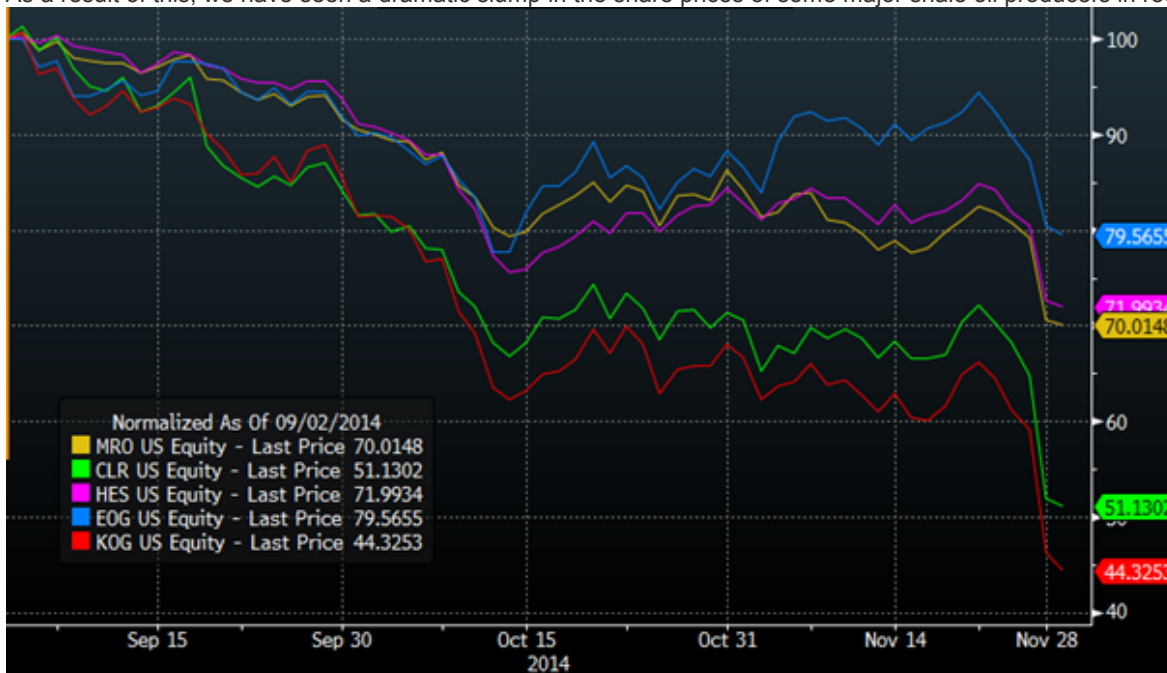
US shale oil production from the three major production areas currently accounts for almost half of the country's total output. The prices that producers from these areas receive are discounted to WTI crude with the infrastructure struggling to keep up with the ongoing increase in production. The chart below shows that shale oil prices are rapidly approaching the \$60 per barrel mark, below which only 82% of producers will manage to break even.

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As a result of this, we have seen a dramatic slump in the share prices of some major shale oil producers in recent weeks.



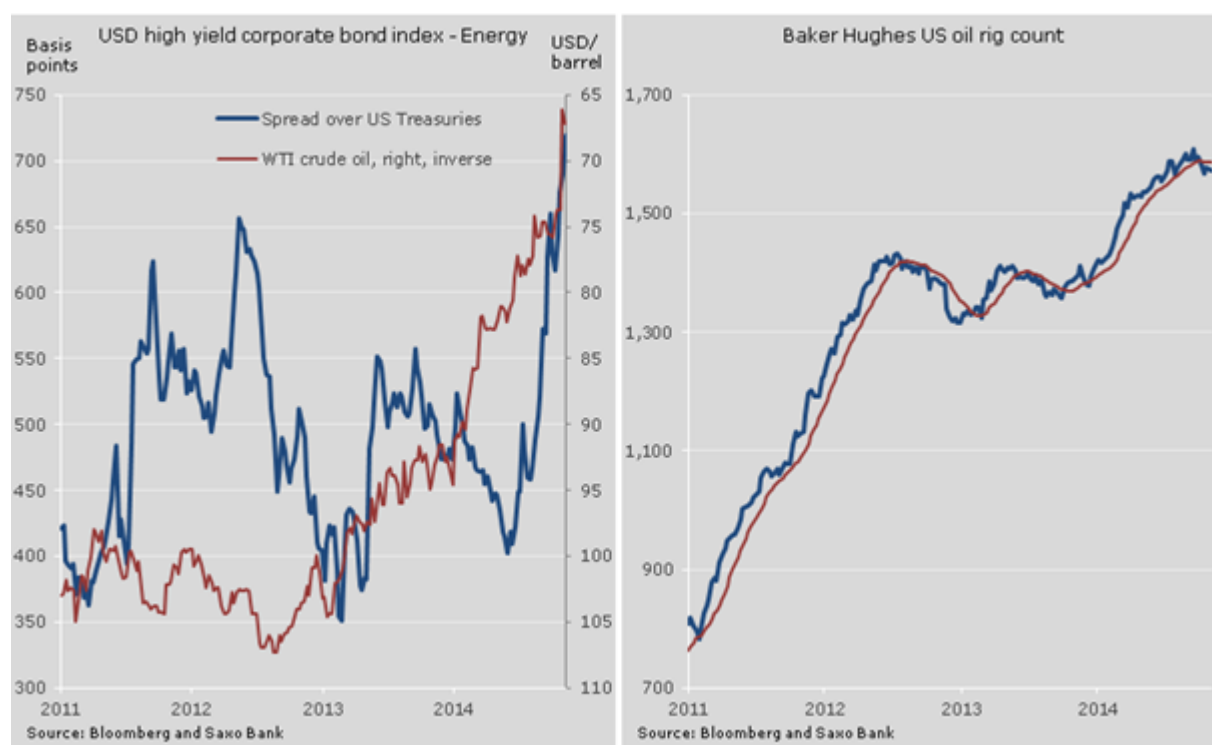
Source: Bloomberg



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Going forward, the market will be looking towards smaller energy companies (not necessarily those mentioned above) and their ability to attract continued financing. The cost of borrowing for this sector has been on the rise for a while, and the US high-yield corporate energy bond index is currently priced almost 725 basis points above US treasuries.

Additional clues as to whether a slowdown in production is happening will come from the weekly oil rig count, which has seen a fall during the past couple of weeks.



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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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