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## WCU: Oil market turning attention to Opec and Saudi Arabia

By Ole Hansen

Hedge funds have accumulated the first net-short across key commodities and following six weeks of continuous selling the sector paused ahead of several critical event risks over the coming weeks. Continued focus on oversupply ahead of the December 4 Opec meeting kept oil under pressure, industrial metals received a boost from talk of Chinese production cutbacks while a rising dollar added further misery for precious metals.

**"They don't want to see oil below \$40 [when Opec meets] on December 4," says Ole Hansen at Saxo Bank, adding that he believes the kingdom is trying to make a "verbal intervention" in the market, as it has done in the past.**

**"This is all really about buying time," he adds. "Demand growth will eventually start to work off the glut, but there's no point going bankrupt in the meantime."**

Quote from today's *Financial Times*. [Click here](#) for complete article.

## King dollar reigns over us

The dollar continued its ascent and against the euro and touched its highest level since April. Traders both speculative and real money have been slow in jumping back on the long dollar train. However, speculation about additional stimulus being announced by the European Central Bank on December 3 in addition to the expected US rate hike on December 16, mean a continued rally into year-end seems increasingly likely.

Industrial metals received boost on news that the China nonferrous Metals Industry Association had asked the government to help prop up prices and to investigate a recent sharp increase in short selling of metals on the Shanghai Futures Exchange. The impact of such initiatives will probably prove limited as long the root causes of the weakness remain. These are declining demand, not least from China (the world's largest consumer), and a lack of production cutbacks by miners.

Codelco, owned by the Chilean state, and the world's biggest copper producer, recently stated that it would rather reduce margins than cut production. While the price of metals in dollars have fallen many producers have also seen a big reduction in production costs due to lower energy prices and falling local currencies. These developments have cushioned the impact of falling prices and helped prop up production thereby prolonging the current price slump.

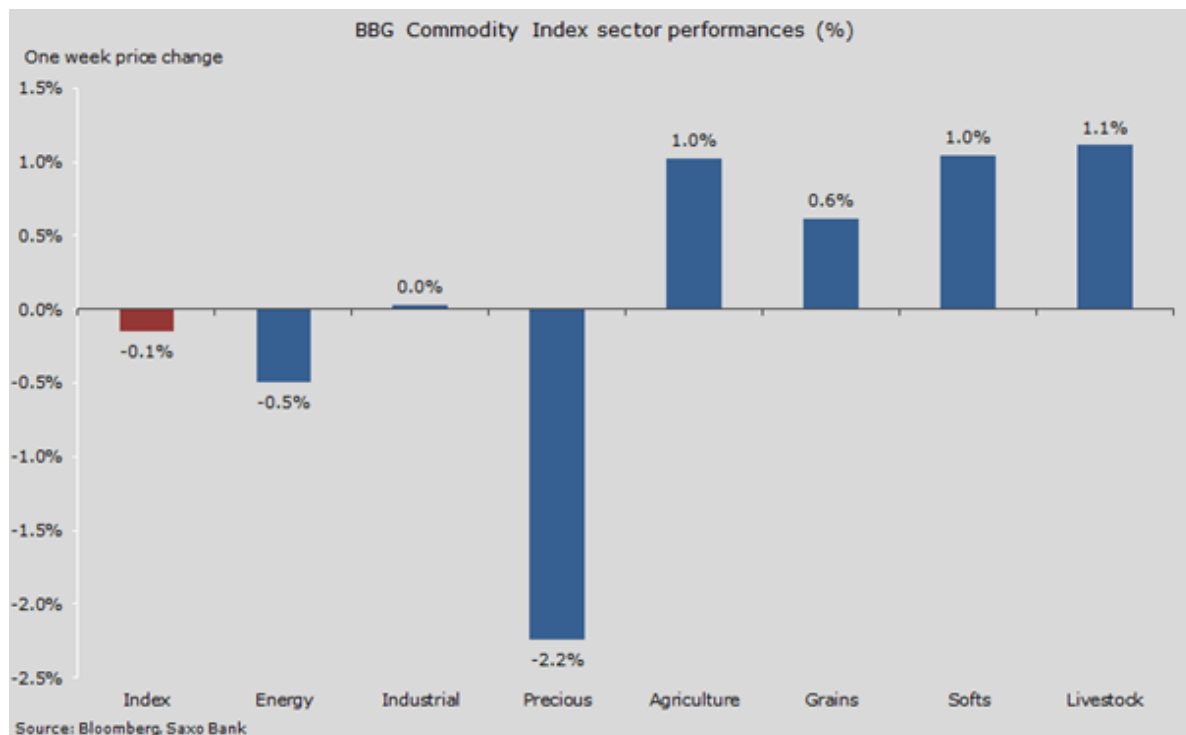
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The energy sector was mixed with gasoline rallying on strong demand around Thanksgiving while natural gas was heading for its biggest weekly decline since June. The weakness was driven by the 34th straight weekly rise in inventories as mild weather across the US north east continues to delay the beginning of the winter extraction period.

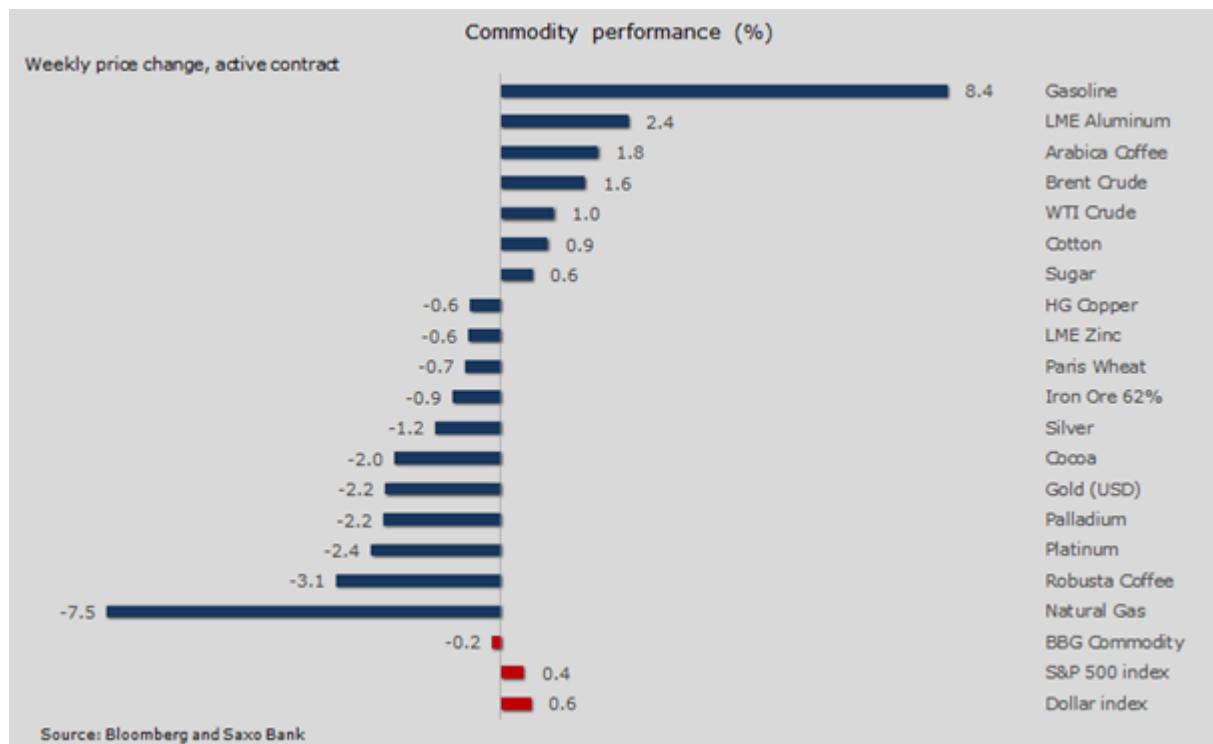
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WTI crude oil has settled into a \$40 to \$44 range with supply news continuing to limit the upside for now. US weekly inventories rose for a ninth straight week while Libya's attempt to reopen two of its biggest fields could lead to a doubling of its current production to 800,000 barrels per day.

Money managers have accumulated a record short futures position in Brent and WTI crude and, just like when this last happened back in August, the shorts have helped put the brakes on the selloff with positions now already geared towards lower prices. In August, the similar sharp rise in bearish bets helped trigger a 25% rally in just three days and with this in mind the selling has now slowed despite news from the market continuing to be non-supportive.

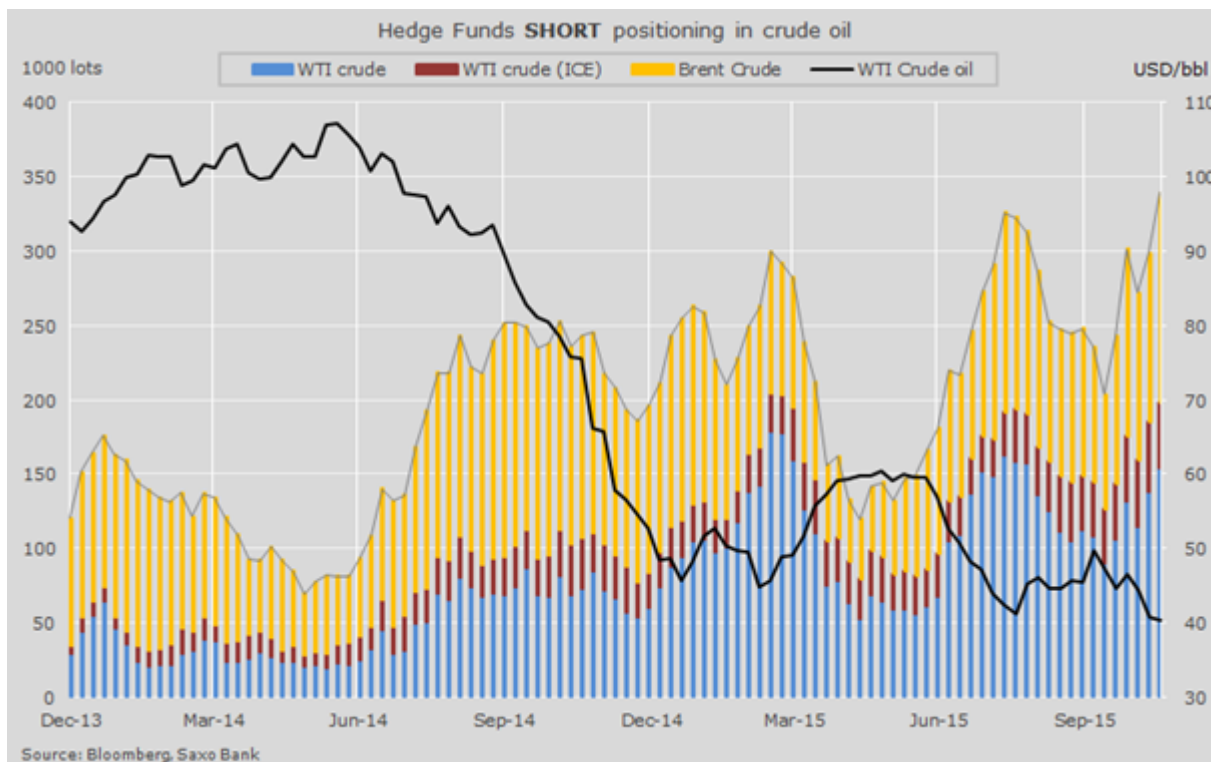
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### Crunch summit in Vienna

On December 4 Opec meets in Vienna for the first time since October and multiple issues will be discussed on and off the official agenda. Since October the price of Opec's crude oil basket has fallen by another 10% to the lowest since the 2009 recession.

Non-Opec supply, meanwhile, remains stubbornly high with US production having plateaued above 9 million barrels per day. A continued drop in the number of oil rigs operating across the US should however provide some comfort in the belief that additional production cuts will be seen during the coming months.

*US oil production has stabilised but the continued drop in number of oil rigs should eventually trigger a renewed decline*

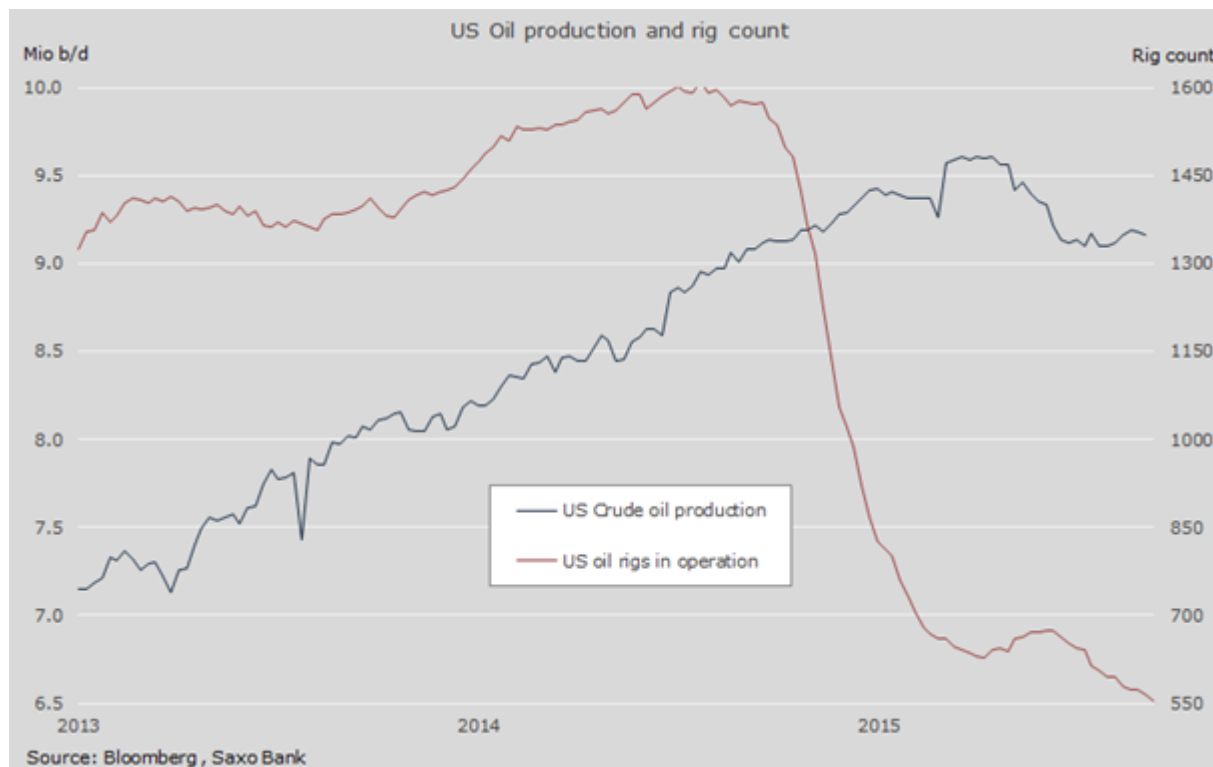
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Saudi Arabia, the architect of the current strategy of pump and dump, has received increased criticism from within the cartel. Not least from its poorer members who are all suffering from dwindling income and the inability to increase production any further Saudi officials have been seen changing their tone in recent statements and the latest which highlighted its desire to work with other producers to ensure price stability have sparked speculation about a surprise announcement next Friday.

The value of Opec's daily production has slumped by \$2 billion per day compared with the average seen between 2011 and 2014. So while Opec can claim success in terms of stimulating global demand the negative economic impact on its members has been tremendous.

However, changing course at this stage when non-Opec production remains stubbornly high should ensure a no change decision as anything else could be viewed as an unwelcome defeat to Saudi Arabia. Discussions about how to handle next year's production increase from Iran, and the potential doubling of output from Libya within weeks, will undoubtedly lead to an interesting discussion among the ministers. One thing is certain. Oil traders will be glued to their screens next Friday while journalists and analysts will be busy trying to decipher all the unofficial comments that are picked up outside the conference room.

The combination of a surprise announcement (however slim) and the extended short position currently seen in the futures market should keep the downside risk remaining limited to \$40 for WTI and \$43 for Brent ahead of the meeting. We still view the \$40 to \$50 area as the most likely area of trading during the coming months. However, a seasonal build in US inventories during the first quarter, combined with increased production from Libya and Iran, will keep the short-term risk skewed to the downside.

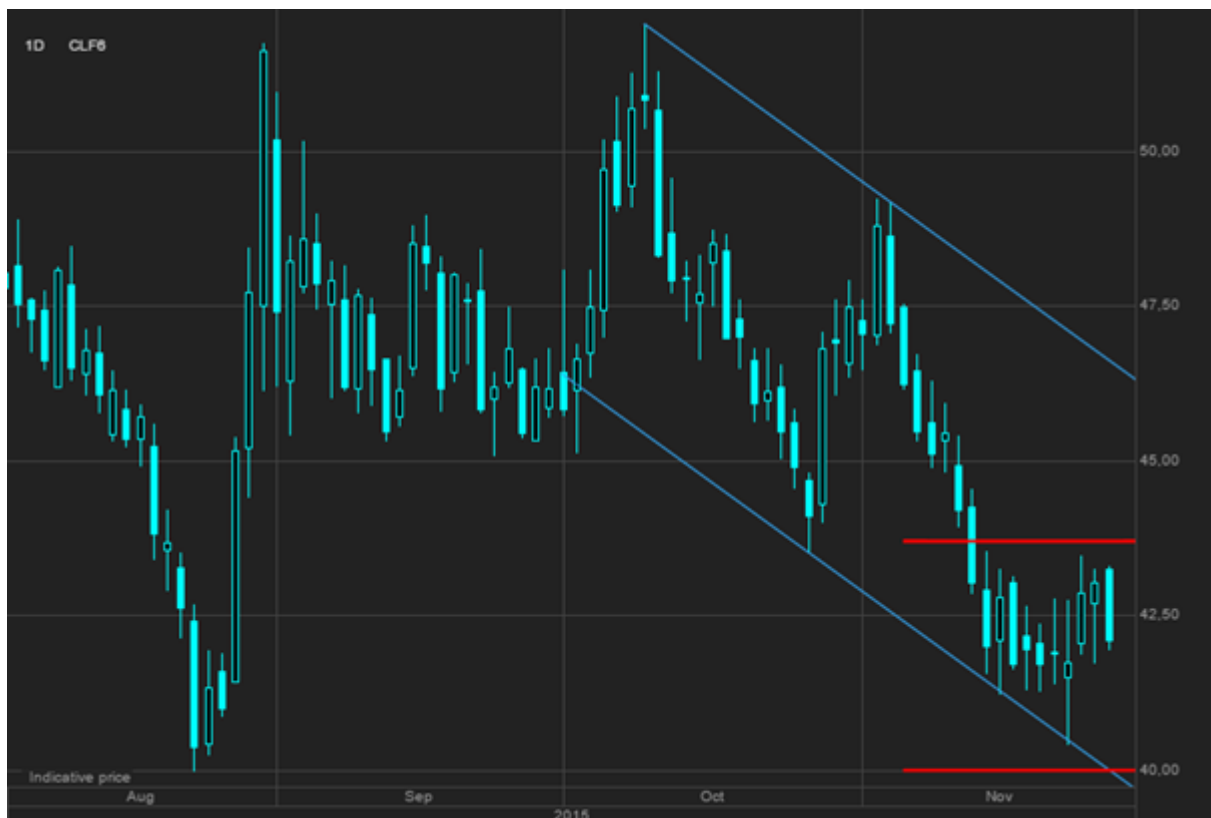
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Source: SaxoTraderGO

### **Dollar and FOMC focus sending gold lower**

With US interest rates poised to rise, the dollar seemingly on an endless journey higher and most global commodities plumbing multi-year depths, it's no wonder that gold, too, is in trouble. Even the latest spike in geopolitical tensions over Turkey's downing of a Russian jet has failed to invigorate the metal, a traditional refuge in troubled times.

Gold's lost shine is dramatically illustrated by the current state of the market which has seen an exceptionally sharp fall in longs. Right now Comex gold futures are net short by 9,000 lots (900,000 ounces) – nearly as low as back in late July when the market was short of 11,300 lots.

The magnitude of gold's fall from grace is one thing but what's really remarkable is the speed at which it occurred: as recently as late October there were longs of 121,000 lots (12.1 million ounces).

In other words, the reversal was both sizable and sudden, occurring as it did inside three weeks and that's one of the most aggressive reversals we have seen in a long time.

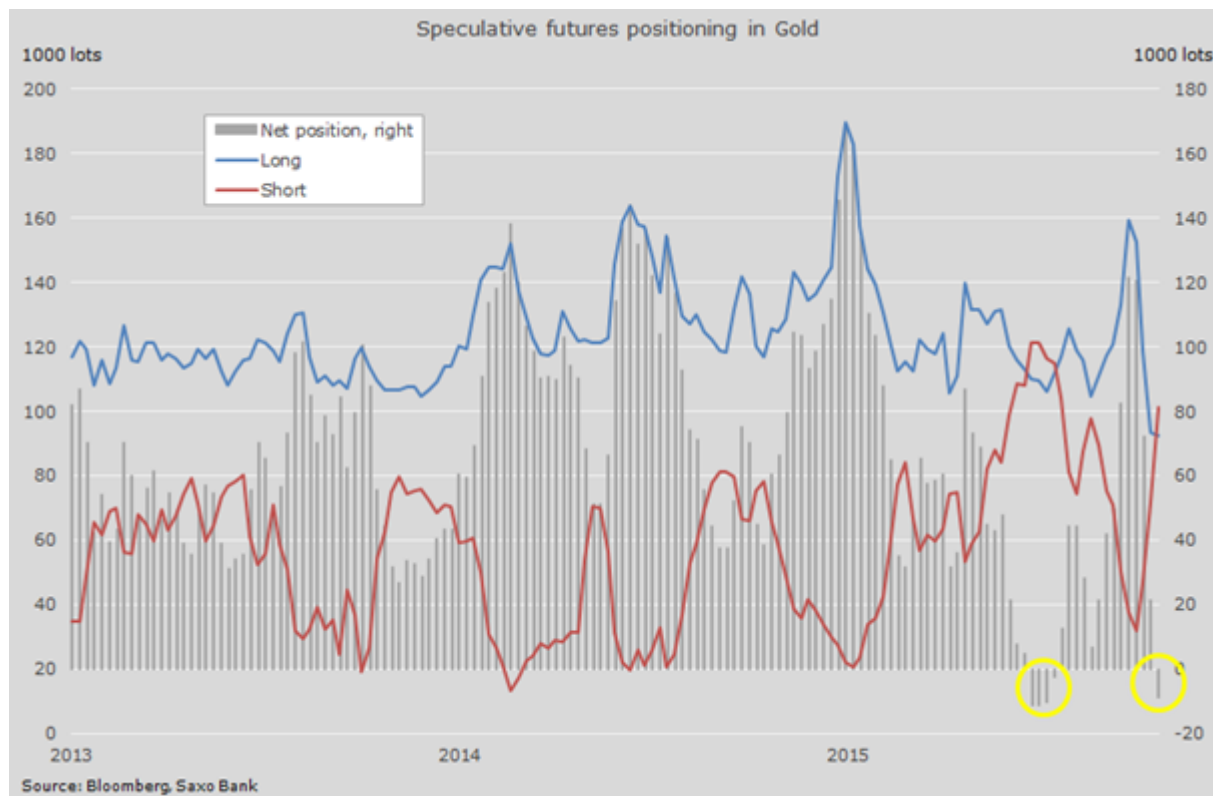
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Gold traders have by now fully priced in a US rate hike in December but what the market hasn't yet worked into the price is the impact higher rates will have on the dollar. Both speculative and real money investors have been slow in re-building sizable dollar longs and that could see the greenback strengthen further during the coming weeks.

Gold may well remain under pressure until the Federal Reserve Open Market Committee meeting on December 16 but we might see a rally thereafter. So while gold may finish the year close to \$1,100/oz the real test will be during the first quarter of next year. Ahead of the FOMC meeting we could see gold trade in a range between \$1,040– \$1,090/oz in December. On a three to six month perspective it might drop as low as \$1,000/oz before clawing its way back towards \$1,250/oz by the end of next year.

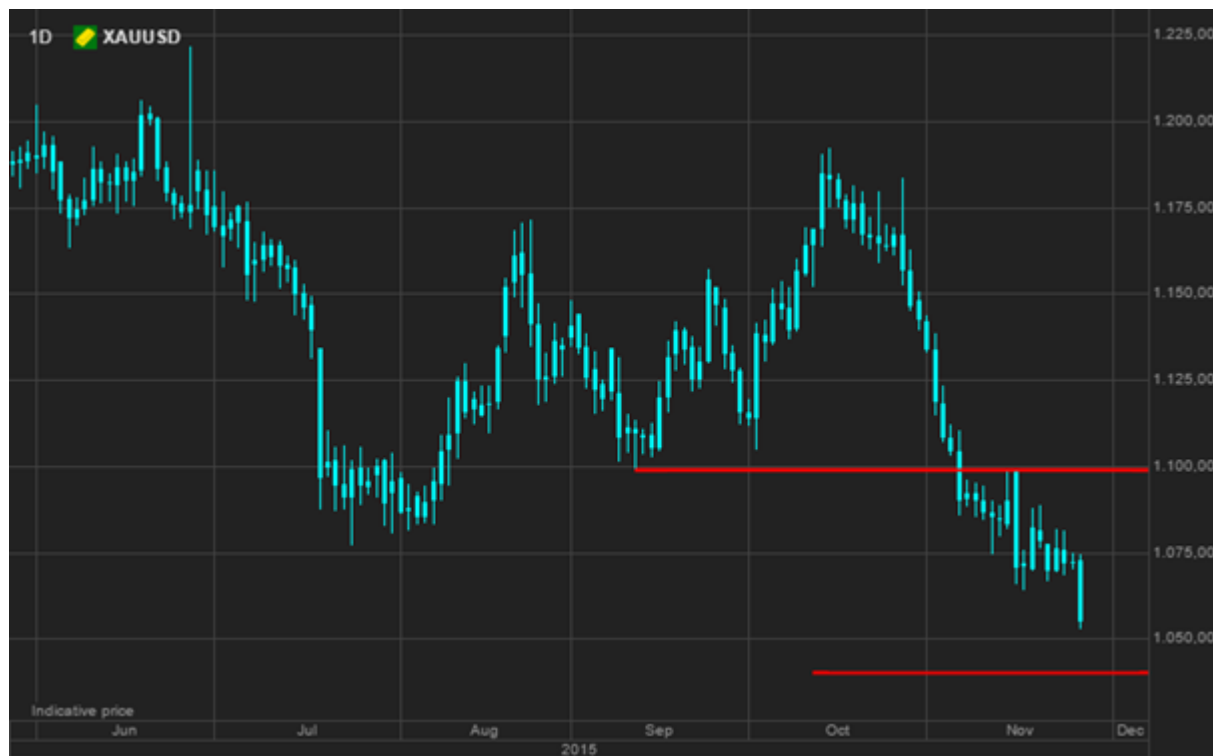
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*Ole Sloth Hansen is a specialist in all traded Futures, with over 20 years' experience both on the buy and sell side. Hansen joined Saxo Bank in 2008 and is today Head of Commodity Strategy focusing on a diversified range of products from fixed income 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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