Commodities and Energy

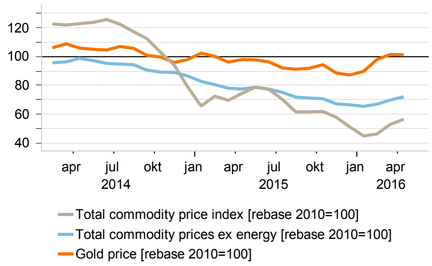
Less tailwind in commodity markets

- Rapid drop in oil production and increased demand
- Rising metal prices when China stimulates again
- Global inflation turns higher – less pressure on central banks

Swedbank's Total Commodity Price Index rose in April by 6.7% in USD terms, continuing its recovery after bottoming out in January. While the index has risen by 24% in recent months, it is still has a way to go to reach last year's level (20% lower). Energy commodities saw the biggest rise. Since mid-January oil prices have risen by just over 90% to nearly USD 50 a barrel at the time of writing, which has pushed food prices higher as well. Cyclical industrial metals have also showed signs of recovery, though the trend differs by metal. Zinc has risen more than nickel, which remains under pressure from large inventories.

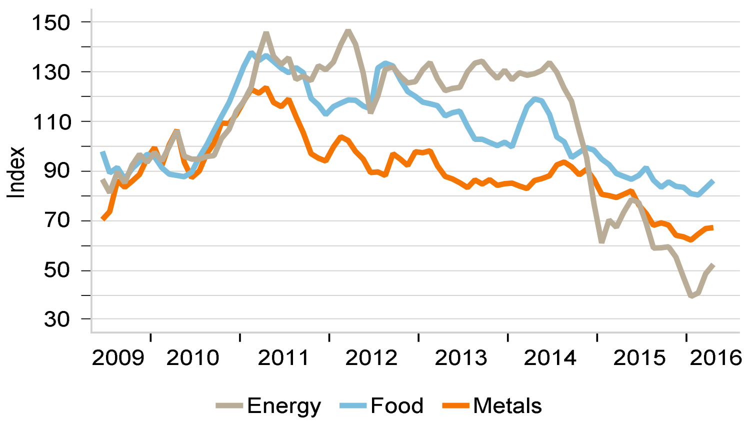
Prices of precious metals (gold and silver) have resisted the price drop better than other commodities. The 20% rise in gold since the beginning of the year may be partly due to uncertainty overshadowing the global economy with many political risks and more expansionary monetary policy. A cautious Federal Reserve and weaker USD have supported gold prices at the same time that several central banks have increased the gold exposure in their currency reserves.

Commodity Price Index and gold price, 2010=100



Source: Swedbank Research & Macrobond

Swedbank's Commodity Price Index, 2010=100



Source: Swedbank Research & Macrobond

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Oil market in balance 2016

Falling oil production outside OPEC and rising demand, not least from emerging markets (China and India), will push oil prices higher this year and in 2017.

Lower oil production and increased demand

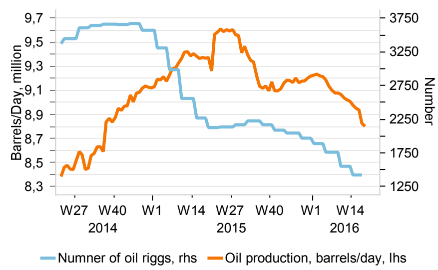
Crude oil prices have risen significantly during the year, from USD 25 a barrel in January to just over USD 48 at the time of writing, up just over 90%. The average price for the first five months of the year is USD 38, however, due to the low levels at the beginning of the year. The increase during the winter and spring is driven by both lower production and continued growth in global demand, not least from emerging economies led by China and India. The IEA (International Energy Agency) has repeatedly revised its global consumption estimates higher for this year and next despite that the global growth outlook has been pushed lower, but where low oil prices may have stimulated stronger demand.

At the same time that demand for crude oil is growing, production outside OPEC has fallen. In the US it has dropped by 800 000 barrels a day, from 9.6 million barrels a year ago to 8.8 million today. This is happening at the same time the number of oil rigs is dropping and more oil companies are struggling with declining profitability. Tighter financial conditions may limit utilization of existing rigs even if prices rise. Within OPEC, production continues to increase, a trend that's expected to continue going forward, not least due to the oil dependence of these countries and their growing fiscal deficits. In April production was 33 million barrels a day, driven by Iran, which has raised production faster than expected (3.5 million barrels in April). Iran will play an increasingly important role in the market. Officially, it doesn't want to slash production until it can recover its previous market share. It will be interesting to see whether previous tensions persist at OPEC's June 1 meeting, especially between Saudi Arabia and Iran, and whether the meeting will include Russia. In April valiant efforts were made to freeze oil production within OPEC together with Russia, but they failed when Saudi Arabia backed out.

The big drop in investment in the global oil industry and rising demand for crude are expected to lead to a smaller surplus in 2016-17. The market could find a balance as soon as the second half of the year after a surplus of 2 million barrels a day last year. In the US, investments in the sector have fallen significantly, and according to the consulting firm IHS prospecting for new oil sources has dropped to the lowest levels in 60 years. IHS warns that the lack of new sources could eventually lead to a growing oil shortage.

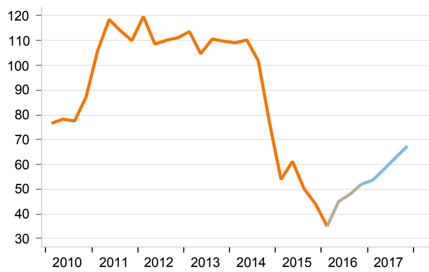
We estimate an average oil price of USD 45 a barrel in 2016, before it reaches just over USD 60 next year. This implies a price of just over USD 50 by the end of this year and nearly USD 70 by the end of 2017. Expectations of higher oil prices may generate higher production, however, due to which the price gain may be more modest than we forecast, especially next year.

US oil production



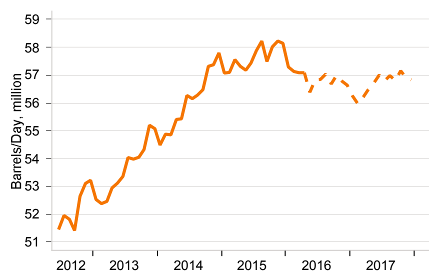
Source: Swedbank Research & Macrobond

Swedbank's oil price forecast



Source: Swedbank Research & Macrobond

Oil production outside OPEC acc. to EIA



Source: EIA

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Metal prices have bottomed out

Metal prices stabilized at low levels. Production cutbacks and lower inventories are initially driving up prices.

Shrinking inventory levels

Prices of industrial metals seem to have bottomed out and are slightly recovering in 2016, though from low levels. In April Swedbank's price index for non-ferrous metals rose by 0.6% in USD terms compared with March, the third month in a row that prices increased. Zinc and aluminum and to some extent copper have seen the clearest increases, while nickel prices are still under pressure from significant oversupply. Nickel stocks are still record high, while stocks of zinc and copper have decreased in the wake of production cutbacks by the mining industry to meet weaker global demand for metals.

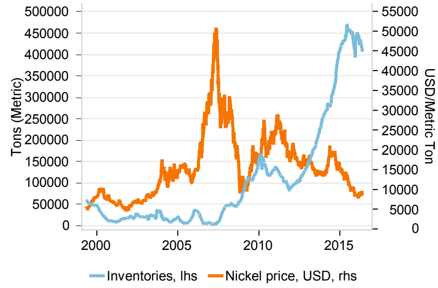
The price of iron ore, which bottomed out in January at USD 40 per ton, has since risen markedly to nearly USD 70 per ton in April before retreating to USD 55 per ton. Steel prices have also risen in 2016. This increase rests on shaky ground, however. Overcapacity is still significant at the same time that new production capacity for iron ore is increasing, with a risk that prices could continue to fall in the short term. At the same time demand is being squeezed lower Chinese steel consumption in the wake of its declining investments. Both the US and EU are highly critical of the slow pace of the Chinese steel industry's consolidation, and instead the global market has been flooded with cheap Chinese steel. On the other hand, a major cutback by the Chinese steel industry could lead to lower demand for iron ore and probably lower prices

The World Steel Association estimates in its April forecast that global consumption will drop by 0.8% in 2016 after declining by 3% in 2015. Next year consumption is expected to rise again, while it continues to shrink in China to 42% of the global market from nearly 50% in 2013.

Metal commodity prices are steered in large part by the Chinese economy, which accounts for 40-50% of global consumption. The current rebalancing of the Chinese economy has led to less commodity-intensive growth. Industrial production is growing a more modest 5-6% on an annualized basis at the same time that lower investment growth is reducing the demand for commodities. The plans of Chinese authorities to launch infrastructure investments of 4.7 billion yuan (about 6.7% of GDP) over a three-year period may give metal prices a boost. This is a bigger investment program than the one in 2008/09 in the wake of the financial crisis, but this time the program is less focused on the housing sector and less commodity intensive. Instead, the priority will be infrastructure investment.

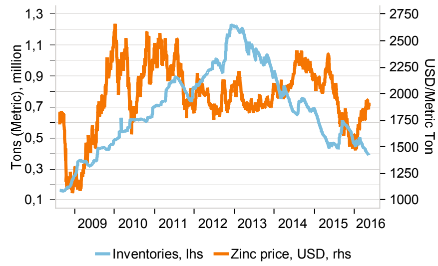
We expect prices of industrial metals, excluding iron ore, to rise over the course of the year but not reach last year's levels, with the average price down 5-7%. For 2017 we estimate that prices will rise by 8-10% on average, driven by both lower metal production and increased demand.

Nickel, USD and million tons



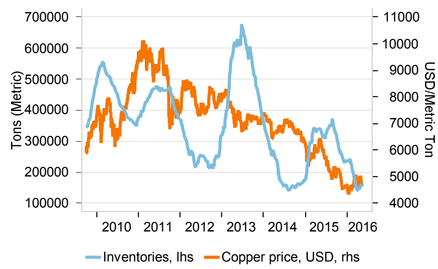
Source: Swedbank Research & Macrobond

Zinc, USD and million tons



Source: Swedbank Research & Macrobond

Copper, USD and million tons



Source: Swedbank Research & Macrobond

Iron ore price, USD

Source: Swedbank Research & Macrobond

Oil lifts food prices

Large inventories and strong production are limiting the rise in food prices. Higher production costs due to higher oil prices are raising the pressure on prices, however.

Continued high grain production

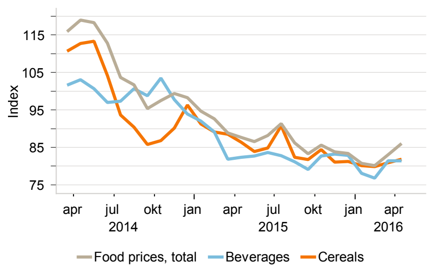
Global food prices rose in April by 3.6% in USD terms compared with March. It has mainly been the higher prices of oilseeds such as soy beans and rapeseed that have driven the increase due to drought in the southern hemisphere (El Nino), while grain prices have been fairly stable. The food market is facing large inventories after good harvests in recent years, especially of grain. This is expected to continue this year against the backdrop of the Food and Agriculture Organization's (FAO) latest forecast on global grain production, which estimates 2 526 million tons, in line with last year's level.

Higher oil prices in 2016-17, in accordance with our forecast, mean more expensive costs for food producers, whose biggest costs are fuel and fertilizer (around 40% of US wheat growers' variable costs). We expect that rising production costs will eventually generate higher grain prices, especially where fuel/fertilizer use is highest. Rising oil prices are also expected to lift the price of rapeseed oil, an oilseed that correlates closely with oil. Since rapeseed oil is an alternative to crude for use as a fuel, the price of rapeseed tends to rise along with oil prices.

Global inflation turns higher

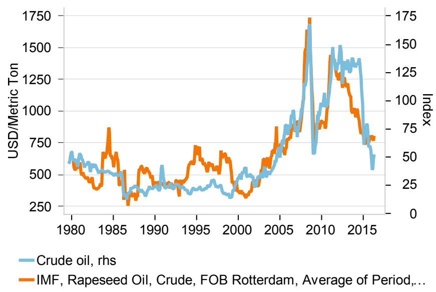
The restraining effect of commodity prices on global inflation is expected to fade as commodity markets stabilize. This also eases pressure on central banks and reduces the need for further monetary stimulus. The clearest impact will come through higher oil prices. The restraining effect of energy prices on global inflation will fade during the second half of the year when oil prices are compared with the low levels at the end of last year. On the other hand, other commodities are expected to have less impact on inflation as long as overcapacity in the market continues.

Food prices, 2010=100



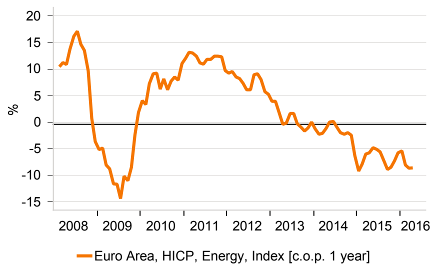
Source: Swedbank Research & Macrobond

Rapeseed oil and crude oil prices



Source: Swedbank Research & Macrobond

Energy prices in eurozone, y/y (%)



Source: Swedbank Research & Macrobond

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Swedbank's Commodity Price Index

Swedbank Commodity Index			- US$ -
Basis 2000 = 1oo			18-05-16
	2.2016	3.2016	4.2016
Total index	**136,8**	**155,9**	**166,3**
Per cent change month ago	3,4	14,0	6,7
Per cent change year ago	-35,1	-22,8	-22,3
Total index exclusive energy	**163,7**	**172,0**	**179,4**
Per cent change month ago	2,8	5,0	4,3
Per cent change year ago	-17,8	-10,1	-5,0
Food, tropical beverages	**180,6**	**188,6**	**192,9**
Per cent change month ago	-1,1	4,5	2,3
Per cent change year ago	-13,5	-4,4	-1,6
Cereals	**168,8**	**170,9**	**173,0**
Per cent change month ago	-0,4	1,2	1,2
Per cent change year ago	-10,3	-8,6	-5,2
Tropical beverages and tobacco	**193,1**	**204,7**	**204,7**
Per cent change month ago	-1,7	6,0	0,0
Per cent change year ago	-13,8	-0,6	-1,2
Coffee	**111,8**	**117,7**	**117,9**
Per cent change month ago	0,7	5,3	0,2
Per cent change year ago	-20,8	-7,4	-8,5
Oilseeds and oil	**161,1**	**165,5**	**180,5**
Per cent change month ago	0,0	2,7	9,1
Per cent change year ago	-15,0	-10,9	0,0
Industrial raw materials	**158,9**	**167,2**	**175,5**
Per cent change month ago	4,1	5,2	4,9
Per cent change year ago	-19,1	-11,7	-6,0
Agricultural raw materials	**130,1**	**131,9**	**135,3**
Per cent change month ago	1,7	1,4	2,6
Per cent change year ago	-9,7	-5,6	-1,6
Cotton	**59,4**	**50,0**	**61,6**
Per cent change month ago	-3,9	-15,8	23,2
Per cent change year ago	-6,0	-20,0	-5,2
Softwood	**116,4**	**116,1**	**117,4**
Per cent change month ago	2,2	-0,2	1,1
Per cent change year ago	33,9	30,7	27,1
Woodpulp	**792,1**	**789,7**	**789,4**
Per cent change month ago	-0,2	-0,3	0,0
Per cent change year ago	-12,5	-10,8	-8,3
Non-ferrous metals	**157,6**	**162,7**	**163,7**
Per cent change month ago	4,0	3,3	0,6
Per cent change year ago	-19,4	-15,9	-16,7
Copper	**4595,5**	**4948,0**	**4851,0**
Per cent change month ago	3,0	7,7	-2,0
Per cent change year ago	-19,4	-16,5	-19,5
Aluminium	**1535,6**	**1531,6**	**1564,3**
Per cent change month ago	3,8	-0,3	2,1
Per cent change year ago	-15,6	-13,6	-13,9
Lead	**1771,6**	**1808,0**	**1729,0**
Per cent change month ago	7,6	2,1	-4,4
Per cent change year ago	-1,8	1,3	-13,5
Zinc	**1711,0**	**1804,0**	**1851,0**
Per cent change month ago	13,2	5,4	2,6
Per cent change year ago	-18,6	-11,1	-16,1
Nickel	**8309,5**	**8704,0**	**8853,0**
Per cent change month ago	-2,0	4,7	1,7
Per cent change year ago	-42,8	-36,7	-30,7
Iron ore, steel scrap	**236,0**	**270,0**	**311,3**
Per cent change month ago	7,9	14,4	15,3
Per cent change year ago	-29,1	-11,5	9,4
Energy raw materials	**124,8**	**148,8**	**160,6**
Per cent change month ago	3,8	19,2	7,9
Per cent change year ago	-42,1	-28,1	-28,8
Coking coal	**195,4**	**198,7**	**195,7**
Per cent change month ago	2,7	1,7	-1,5
Per cent change year ago	-24,9	-18,4	-12,5
Crude oil	**121,6**	**146,5**	**159,0**
Per cent change month ago	3,9	20,5	8,5
Per cent change year ago	-43,1	-28,6	-29,5

Source : SWEDBANK and HWWA-Institute for Economic Research Hamburg

Swedbank Commodity Index			- SKr -
Basis 2000 = 1oo			18-05-16
	2.2016	3.2016	4.2016
Total index	**126,1**	**141,3**	**146,6**
Per cent change month ago	2,6	12,1	3,7
Per cent change year ago	-34,1	-24,5	-27,1
Total index exclusive energy	**150,9**	**155,9**	**158,1**
Per cent change month ago	1,9	3,3	1,4
Per cent change year ago	-16,6	-12,0	-10,8
Food, tropical beverages	**166,4**	**171,0**	**170,1**
Per cent change month ago	-1,9	2,7	-0,5
Per cent change year ago	-12,3	-6,5	-7,6
Cereals	**155,6**	**154,9**	**152,5**
Per cent change month ago	-1,2	-0,4	-1,6
Per cent change year ago	-9,0	-10,6	-11,0
Tropical beverages and tobacco	**178,0**	**185,6**	**180,4**
Per cent change month ago	-2,5	4,2	-2,8
Per cent change year ago	-12,5	-2,8	-7,3
Coffee	**103,0**	**106,7**	**103,9**
Per cent change month ago	-0,1	3,6	-2,6
Per cent change year ago	-19,6	-9,4	-14,1
Oilseeds and oil	**148,5**	**150,0**	**159,2**
Per cent change month ago	-0,8	1,0	6,1
Per cent change year ago	-13,7	-12,8	-6,1
Industrial raw materials	**146,5**	**151,6**	**154,7**
Per cent change month ago	3,3	3,5	2,0
Per cent change year ago	-17,9	-13,7	-11,8
Agricultural raw materials	**119,9**	**119,6**	**119,3**
Per cent change month ago	0,8	-0,3	-0,3
Per cent change year ago	-8,4	-7,7	-7,6
Cotton	**54,7**	**45,3**	**54,3**
Per cent change month ago	-4,7	-17,2	19,8
Per cent change year ago	-4,6	-21,8	-11,1
Softwood	**107,3**	**105,2**	**103,5**
Per cent change month ago	1,4	-1,9	-1,7
Per cent change year ago	35,9	27,8	19,3
Woodpulp	**730,1**	**715,9**	**695,9**
Per cent change month ago	-1,0	-2,0	-2,8
Per cent change year ago	-11,2	-12,7	-14,0
Non-ferrous metals	**145,3**	**147,5**	**144,3**
Per cent change month ago	3,2	1,5	-2,2
Per cent change year ago	-18,2	-17,7	-21,9
Copper	**4235,8**	**4485,5**	**4276,3**
Per cent change month ago	2,1	5,9	-4,7
Per cent change year ago	-18,2	-18,3	-24,5
Aluminium	**1415,4**	**1388,4**	**1379,0**
Per cent change month ago	2,9	-1,9	-0,7
Per cent change year ago	-14,4	-15,5	-19,2
Lead	**1632,9**	**1639,0**	**1524,2**
Per cent change month ago	6,7	0,4	-7,0
Per cent change year ago	-0,3	-0,9	-18,8
Zinc	**1577,1**	**1635,4**	**1631,7**
Per cent change month ago	12,2	3,7	-0,2
Per cent change year ago	-17,4	-13,0	-21,3
Nickel	**7659,2**	**7890,4**	**7804,1**
Per cent change month ago	-2,8	3,0	-1,1
Per cent change year ago	-42,0	-38,0	-35,0
Iron ore, steel scrap	**217,5**	**244,8**	**274,4**
Per cent change month ago	7,0	12,5	12,1
Per cent change year ago	-28,1	-13,5	2,7
Energy raw materials	**115,0**	**134,9**	**141,5**
Per cent change month ago	3,0	17,2	4,9
Per cent change year ago	-41,3	-29,6	-33,1
Coking coal	**180,1**	**180,1**	**172,5**
Per cent change month ago	1,9	0,0	-4,2
Per cent change year ago	-23,8	-20,2	-17,9
Crude oil	**112,1**	**132,8**	**140,1**
Per cent change month ago	3,0	18,5	5,5
Per cent change year ago	-42,3	-30,2	-33,8

Source : SWEDBANK and HWWA-Institute for Economic Research Hamburg

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