Monday, September 26, 2016
GULF TIMES
BUSINESS

BANKING ON KNOWLEDGE

Monetary policy divergence drives commodity market volatility

By Dr R Seetharaman

Gold price posted the largest weekly gains since June on account of Fed holding rates and ended at $1337.56/ ounce. Silver also had surged and ended at $19.689/ounce. Gold has surged by more than 25% YTD and silver by more than 41% YTD respectively. The Fed put off a rate increase last Wednesday.

The US Federal Reserve was divided this month, with seven members opting to stick with rates as they are and three lobbying for a rise. Fed chairperson, Yellen had suggested that much of the discussion centred on which set of risks was greater: overheating the economy by delaying a rate increase now, or taking a chance that inflation will remain below its 2% goal by removing monetary accommodation too early. She played down concerns that the Fed's easy monetary stance was fuelling bubbles in the financial markets and

the economy. All eyes will now turn to the end of the year, by which time a majority of rate-setters currently expect an increase. The Fed's alteration in its monetary tightening plan this year has given boost to precious metals.

The oil prices declined by end of last week as Organisation of the Petroleum Exporting Countries (Opec) was unlikely to make any headway on a production freeze later this month. Oil prices fell 4% on Friday, paring weekly gains, on a report that Saudi Arabia did not expect an agreement at talks this week in Algeria among major crude exporters aimed at freezing production.

US oil drilling rig count was up on Friday by 2 to 418, according to Baker Hughes. Brent crude oil was at $45.98/ barrel by end of last week. US West Texas Intermediate (WTI) crude was at $44.56/ barrel by end of last week. WTI has surged by more than 20% YTD and Brent at more than 23% YTD respectively. Natural gas which had surged above $3/ MMBTU last week as hot weather reports keep stoking expectations for strong demand witnessed some correction and ended last week by $2.976/ MMBTU.

Nickel price is at 10615/tonne and has surged by more than 20% YTD this year as global stockpiles declined.

The Philippines, the world's largest shipper of mined nickel used in stainless steel, is carrying out an environmental audit and closing mines that don't meet international standards, curbing supply. Copper had fresh highs following the Federal Reserve's decision to keep rates accommodative and has ended at $4833/tonne by end of last week. It has surged by close to 3% YTD.

Aluminium price was also up after Fed's decision and concerns of supply in European market. It has surged by close to 9% YTD and ended last week at $1629.5/tonne.

The chances for lower corn prices increased after the USDA earlier this month pegged production at a record 15.1bn bushels on yields of 174.4 bushels an acre. Corn was at 3.36 USD/bushel by end of last week and had fallen by more than 12% YTD.

Higher soybean prices likely as incessant rains flood fields and the proliferation of fungal diseases including sudden death syndrome. Soya bean price was at 9.55 USD/bushel by end of last week and had surged by close to 10% this year. The Wheat price was at 4.04/bushel by end of last week and had fallen by more than 20% YTD on account of excess global supply.

Cocoa price has fallen by more than 10% YTD and is at $2852/tonne by end of last week amid demand concerns and improving global supply prospects, with outlook in western Africa improving. Coffee price has surged by more than 12% YTD and is at $151.40/ tonne by end of last week, however prices have fallen recently on bumper harvests due to benign weather, rising productivity in some larger producing countries. Sugar price has surged by more than 50% YTD and is at 22.70/ tonne by end of last week supported by tightening global sugar supplies.

The Fed continues to face dilemma on its monetary tightening which is giving some relief to commodity prices. However as the Fed resumes it monetary tightening the commodities may have to look beyond liquidity for their price support. The other major central Banks namely BoJ, BoE and ECB are still wondering when to pursue monetary easing or bring new monetary tools to revive economic growth as against the Fed which is planning its monetary tightening. The monetary policy divergence between central banks will drive commodity market volatility.

■ *Dr R Seetharaman is Group CEO of Doha Bank.*