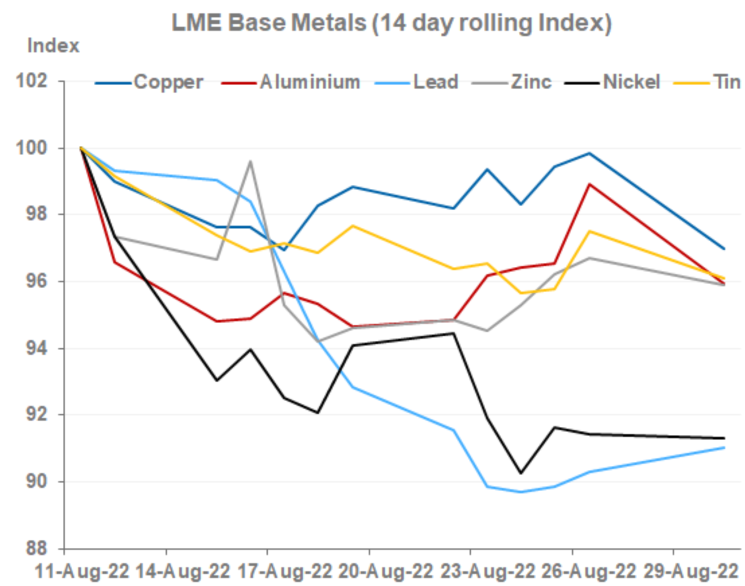
LME Metals Report

Written by Edward Meir – Commodity Research Group
Tel: 1-203-656-1143 • emeir@edfmancapital.com
WWW.EDFMANCAPITAL.COM

This commentary was written at 8:50 P.M. on September 1, 2022, US EST.



It was a brutal day for commodities on Thursday, with base metals, precious metals and oil prices all getting slammed. In the LME space, we saw a roughly 3% decline in copper and aluminum, with the latter closing at a 16-month low. Zinc got pounded as well, losing roughly 6.5% and rolling back practically all of August's advance in just the last two days. Nickel and tin were also very weak, off by roughly 4% and 8% respectively. There were several variables behind the declines, including a surging dollar that pushed higher on a spike in US interest rates, coupled with worrying developments out of China. On that latter point, yet another southwestern Chinese metropolis – Chengdu -- announced a lockdown of its 21.2 million people and instituted widespread COVID testing and movement restrictions – all this on account of 157 cases. Residents are being ordered to stay home from 6 p.m. onwards, with households allowed to send only one person to shop for necessities. Other major Chinese cities, including Shenzhen (15 million people) and Dalian (7 million), have stepped up restrictions as well. These measures are supposed to last only a few days, but that is what the residents of Shanghai were told before they endured a two-month ordeal. For now, businesses and industrial operations seem to be running, but we will be watching this space -- as will the markets.

Meanwhile, macro readings we got out of China overnight were uninspiring. The private sector CAIXIN survey showed factory activity contracting for the first time in three months in August as manufacturing PMI dropped to 49.5 from 50.4 in July. (This comes on the heels of China's official PMI out earlier in the week which dipped below 50). Sub-indices for new orders and export orders both fell into contraction territory as well, while manufacturers cut jobs for a fifth straight month. One bright spot was the ongoing drop in input prices, something we have been seeing pretty much around the world. In China's case however, the input decline ended 26 months of rising prices that have sharply squeezed profit margins.

In China’s real estate market, new home prices in 100 cities surveyed fell by a slight .01% from a month earlier, unchanged from July. Sixty-nine cities reported a fall in prices, compared with 47 in July. (Among all the Chinese statistics we have been following over the years, we find the home price index to be among the most dubious, especially lately as there hardly has been any meaningful price declines. China’s GDP estimates are a close second). Reuters also reports that new home sales by floor area fell 32% in August from a year earlier, about in line with the July decline.

With little sign of progress detected in China's real estate market, we have trouble seeing how base and ferrous metals could move substantially higher going into year-end, especially in view of additional COVID restrictions.

Chinese iron ore futures got hit hard overnight, losing more than 4% basis October futures. Rebar prices fell more than 1%, while stainless steel values were down by roughly half a percent. There were 1%-3% declines in coking coal and coke.

In the currency markets, the general dollar index tacked on almost a full point to reach 109.66, a twenty-year high. The yen was the biggest casualty, trading above 140 and this could very well prove to be the new floor for the currency. The Euro ended down by a whole cent at 99.45, while sterling collapsed below 1.15 at one point, a two-year low.

The surging dollar, the spike in US interest rates and the moderating inflation picture hit the precious metals group hard on Thursday. Gold lost roughly $19/ounce as it briefly broke below $1700/ounce before finishing the day at $1709. Technical support, according to chartists, is not evident until $1675/ounce and we easily could get there given the current rate of decline and the generally bearish environment for the precious metal. Silver dropped $0.25 to end at $17.63, while platinum was off $19 to finish at $807, although it too, breached the $800 at one point. Palladium got smacked, losing 3% to finish at $2005.

In the energy space, crude oil prices lost more ground on China concerns and general recession fears. Brent settled down $3.28 at $92.36 a barrel, while WTI fell $2.94 to $86.61/barrel. "Western-world oil demand, as well as China's, is stagnant, while supplies are expanding incrementally, largely on the back of the U.S. shale boom," a Julius Baer analyst told Reuters. In fact, US output rose to 11.82 million bpd in June and is now running at its highest level since April of 2020. We should add that there has been no stoppage in Russian crude oil exports either and it also looks possible that Iranian barrels could be added into the mix in the event of a nuclear deal, all further headwinds for crude pricing.

Separately, the Chairman of Lukoil — who spoke out against Russia's invasion of Ukraine — died after apparently falling out of a hospital window, this according to TASS. It must have been a very slippery window he was peering out of; that's about the only thing we can think of.

US equity markets opened sharply lower on Thursday, but stocks managed to pare their losses by the close. NASDAQ was the exception, finishing with a modest decline after being weighed down by rising US rates and news that the Biden administration was going to impose export bans on certain chips going to China. This impacted the shares of a number of chip producers, notably Nvidia and AMD. The S&P-500 more broadly is now down about 6% during the past five sessions, its longest losing streak in nearly two months.

Macro data out of the US showed that the ISM manufacturing reading for August was unchanged from July's level at 52.8%, but both monthly readings are at their lowest levels since June 2020. The August report did show new orders and a backlog index rising by about 2%-3%, but the overall production index was down nearly 3%. Importantly, the input price index plunged nearly 8 points to 52.5% from 60. In May, this reading was a sizzling 82% and so the decline bodes well for inflation readings going forward.

Friday of course, brings us the key August nonfarm payroll reading. Economists polled by Reuters see a jobs increase of 300,000, with outliers closer to 400,000. We are hoping for a "poor number" as that would lead to a much more positive response in a number of markets and could hasten a Fed pivot on rates-- now indefinitely postponed judging from Chairman Powell's recent remarks. Meanwhile, labor data released on Thursday showed weekly jobless claims filings dropping to a two-month low and August layoffs falling as well, but the longer-term continuing claims number is ticking higher. Currently, traders expect a 73% chance of a third straight 75 basis point increase in rates. The 10-year ended Thursday's session up 13 basis points and ended at a two-month high of 3.26%, while two-year yields jumped to a 15-year high of 3.511%. Let's see what Friday payroll report brings us. We present market indications below:

Copper: $7596, down $27
Aluminum: $2313, up $18
Zinc: $3235, down $24
Lead: $1914, up $13
Nickel: NA
Tin: $20,660, down $400
Gold: $1709, UNCH
Silver: $17.69, up $.03
Platinum: $810, up $4
Palladium: $2013, up $17
WTI: $87.69, up $1.08
US 10-year: 3.26%
Euro: .9950
Sterling: 1.1550
Yen: 140
Dollar Index: 109.54, down .13
NASDAQ futures: up 6
Dow futures: down 32
S&P futures: down 2