

The Commodities Feed: Oil price caps and halted gas flows

There is plenty going on in energy markets at the moment, which should keep prices volatile. The market has largely ignored the G-7 agreeing to a Russian oil price cap, instead focus is on today's OPEC+ meeting. In addition, supply concerns in the European natural gas market have grown once again, with Nord Stream gas flows not resuming



Energy - OPEC+ likely to keep output targets unchanged

G-7 nations agreed on a price cap for Russian oil at the end of last week. This is an idea that has been pushed for several months now by the US with the hope that it would offer some relief to the oil market. However, looking at the price action since the announcement (prices have moved higher), it is pretty clear that the market is not convinced that the cap will work. The idea of the cap is to allow buyers to access G-7 and EU insurance and shipping services for Russian oil, if the price is at or below the price cap. However, there are still a lot of obstacles and unknowns regarding the cap. Firstly, EU members will have to accept the proposal and changes will need to be made to the sanctions package. It could be difficult getting all member states to agree to this latest proposal. Secondly, and even if all EU members agree to the cap, G-7 nations need to ensure that buyers are willing to take part in the price cap plan to make it effective. This means that larger buyers such as China, India and Turkey would need to take part. There is no guarantee they will,

particularly after Russia has said that it will not supply any country who follows the price cap. In addition, a big unknown is what price level the cap will be set at. It is pretty clear that it will need to be set above Russian production costs, otherwise there is little incentive for Russia to maintain production at current levels. Finally, monitoring and enforcing the price cap will be a significant challenge as well.

While there is plenty of uncertainty over Russian flows, there is also quite a bit of uncertainty over OPEC+ output policy and what the group will decide today at its monthly meeting. Previous comments from the Saudi energy minister suggested that the group may have to cut output due to a dislocation between the physical and paper markets. Several OPEC producers have since echoed these comments. However, we believe that OPEC+ will leave output targets unchanged for next month. It is difficult to justify cutting output when the market is trading near US\$100/bbl. In addition, Russia is reportedly against cutting output as it sends the wrong signal to the market about the supply and demand picture. Furthermore, it would make more sense for OPEC+ to wait for further clarity on Iranian nuclear talks before taking any action. These talks appear to have taken a turn for the worse, with the US saying that Iran's latest response was "not constructive".

Finally, we are likely to see further volatility in the European gas market this week. And this is after gas flows along the Nord Stream pipeline did not resume over the weekend, following maintenance. Gazprom claims that an oil leak at the Portovaya compressor station means that the Nord Stream pipeline will be fully shut down "until the operational defects in the equipment are eliminated". Prior to last week's maintenance, Nord Stream was operating at only 20% of capacity. The halting of flows means that Europe will lose close to 1bcm of natural gas supply per month. The market will now likely become increasingly nervous about flows via Ukraine as well as TurkStream. What is clear is that the more Russia reduces gas flows to Europe, the less leverage they have over Europe.

Metals - more supply woes for aluminium

While most industrial metals ended lower on Friday, LME aluminium managed to eke out a small gain due to persistent supply risks (especially from Europe and China as the power crisis lingers). As per the latest reports, Dutch aluminium smelter Aldel is going to suspend its remaining capacity due to high energy prices and a lack of government support. The smelter has an annual production capacity of 110kt for primary aluminium and 50kt for recycled aluminium. Meanwhile, there are some concerns that Yunnan province in China could see some similar power rationing to what has been seen in Sichuan province, due to lower hydro power output. Yunnan province is home to a large amount of aluminium smelting capacity, which stands at around 5.6mtpa, accounting for 12.7% of China's total installed aluminium smelting capacity according to Shanghai Metals Market.

Novelis Inc. joins the list of industrials trying to avoid exposure to Russian metal since the invasion of Ukraine. A new tender issued for 2023 supply to its European plants specifies that no metal of Russian origin would be allowed as part of any deal. Existing Novelis contracts won't be affected by the new conditions and would allow the supply of Russian metal.

The latest CFTC data shows that speculators increased their bearish bets in COMEX copper by 3,544 lots over the last reporting week, leaving them with a net short position of 8,312 lots as of last Tuesday. Moving to precious metals - speculators decreased their bullish bets in COMEX gold by 9,600, to leave them with a net long of 20,726 lots at the end of the last reporting week.

Agriculture – speculative interest in corn remains high

It was another week of strong buying interest from speculators in CBOT corn as adverse weather in the US and parts of Europe is keeping current crops in poor condition and is weighing on supply prospects. CFTC data shows that money managers increased net longs in CBOT corn by 39,251 lots over the last week, with them holding a net long of 221,467 lots as of 30 August. The move higher was predominantly driven by fresh longs, with the gross long position increasing by 30,446 lots.

Meanwhile, the managed money net long in CBOT soybeans fell by 2,670 lots over the week to 101,801 lots last week, whilst the managed money net short in CBOT wheat declined by 3,822 lots over the week, to leave net shorts at 22,247 lots.

Ukraine has increased exports of agricultural products to around 5mt in August according to Ukraine's Ministry of Infrastructure, which has been driven by a ramping up of shipments through sea ports. Ukraine reportedly shipped around 1.7mt of product through the three ports that opened after the Russia-Ukraine deal, around 1.6mt through the Danube port, and rest by rail and road. Ukraine aims to increase exports to around 8mt in September.

Author

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.