The Commodities Feed: The need for a risk premium

The oil market has opened slightly stronger this morning and this is no surprise given recent developments in Russia. However, the failed move by the Wagner group suggests that any upside in prices will likely be limited

Source: Shutterstock

Energy - Russia instability offers limited upside to oil

It was shaping up to be an interesting opening for oil given developments in Russia towards the end of last week. However, the Wagner group's insurrection came to an end as quickly as it started thanks to a deal brokered by Belarus' Lukashenko. As a result, oil has only seen limited gains so far in early morning trading today with ICE Brent up a little over 1%. While the immediate supply risks have disappeared, the market will likely have to start pricing in a larger risk premium for oil given the growing instability in Russia. How much of a risk premium will really depend on how the aftermath of the failed insurrection is dealt with.

In the US, the oil rig count has continued to trend lower. The number of active oil rigs has fallen by 6 over the last week to 546, which is the lowest level seen since April last year. The rig count has fallen by 77 since mid-January and the slowdown in drilling activity will call into question how much supply growth we will see from the US. Falling drilling activity in the US will be welcome by OPEC+ members, as in theory, it should make their output policy more effective, though demand has been a big concern for the market which has more than offset the recent cuts seen from OPEC+ members.

The latest positioning data shows that speculators increased their net long in ICE Brent by 16,116 lots over the last reporting week to 190,386 lots. This move was predominantly driven by fresh buying with the gross long increasing by 12,996 lots. However, given the price action seen since the last reporting week, we are likely to have seen some of these longs liquidate already. The net speculative long in ICE gasoil increased by 12,250 lots to 16,191 lots over the week. This was largely driven by short covering. The gross short declined by 10,319 lots over the period. Refinery outages have been supportive for middle distillates in recent weeks and if these outages continue, there is room for further short covering.

There is very little on the agenda for energy markets this week with the exception of the regular weekly releases.

Metals – weather disruptions at Codelco mines

Codelco has halted some copper mining operations in central Chile due to heavy rains experienced last week. Mining activities at the Andina mine are currently suspended, while some operations were also stopped at El Teniente mine. The Los Bronces mine (located near the Andina mine) is also operating at a reduced rate. The copper LME cash/3m spread has moved deeper into backwardation, reaching US$18.74/t on Friday, reflecting concerns over a tighter prompt market.

The latest CFTC data shows that speculators increased their bullish bets in COMEX copper by 16,334 lots over the last reporting week, leaving them with a net long position of 23,258 lots (the highest since the last week of January) as of last Tuesday. The move was predominantly driven by short covering with gross shorts falling by 12,214 lots to 30,914 lots.

Authors

Warren Patterson
Head of Commodities Strategy
Warren.Patterson@asia.ing.com

Ewa Manthey
Commodities Strategist
ewa.manthey@ing.com