

The Commodities Feed: USD surge holds complex back

Tensions in the Middle East continue to linger, however, comments from a Fed official and a surge in the USD yesterday held large parts of the commodity complex back



Energy – Red Sea tensions linger

Oil markets continue to trade in a fairly rangebound manner despite developments in the Middle East. The Houthis have attacked another commercial vessel in the Red Sea, while the US has carried out further strikes against the Houthis in Yemen. And more shippers have announced that they will be avoiding the region. A broader risk-off move seems to have held oil back after comments from a Fed official appear to question market expectations for as many as six rate cuts in 2024. The USD also rallied, while US treasury yields moved higher.

Red Sea disruptions also appear to be having an impact on middle distillate east-west arbs with them widening. Europe's reliance on middle distillates from the Middle East and Asia has grown since the Russia/Ukraine war, and obviously with developments in the Red Sea, shipments will be taking longer to get to Europe, offering relative support to European middle distillates.

Freezing cold weather conditions in the US has led to oil supply disruptions in the Bakken in North Dakota with as much as 650k b/d of production offline, which is around half of the state's output.

In addition, freezing conditions have also had an impact on refinery operations in Texas, with several refiners reducing run rates. Production declines in the Bakken has provided some upside to physical oil differentials for the region.

The EIA released its latest Drilling Productivity Report yesterday in which it forecasts that US shale oil production will fall by 2k b/d MoM to 9.68m b/d in February, while shale gas production is forecast to fall 187mmcf/day to 98.89bcf/day. Meanwhile, the number of drilled but uncompleted wells (DUCs) fell by 64 MoM to 4,374 at the end of December. Whilst drilling activity picked up slightly over the month, it was still lower than the pace of well completions.

US natural gas came under significant pressure yesterday with front month Henry Hub futures settling more than 12% lower. While large parts of the US are seeing freezing conditions, the weather forecast is for milder weather later this month. Meanwhile, in Europe TTF remains under pressure with the front month contract settling below EUR30/MWh for a second consecutive day. North West Europe is also expected to see milder weather from next week, whilst storage is around 79% full at the moment, well above the 5-year average of 67%. In the absence of supply shocks or demand spikes, prices are likely to remain subdued on the back of comfortable storage.

For the energy calendar today, OPEC will release its monthly oil market report, which will include its latest outlook for 2024. The report should shed some light on whether OPEC's numbers suggest the need to roll over current voluntary cuts into 2Q24. The API will also release US weekly oil inventory numbers. This release was delayed due to a public holiday in the US on Monday.

Metals – Copper falls on easing Fed rate-cut bets

Copper edged lower on Tuesday on increasing bets that the Fed may have to delay interest rate cuts after recent releases of mixed US economic data. Elevated rates and a stronger dollar have been a drag on metals in the past two years. We believe the Fed's interest rate path will continue to drive copper's short-term price outlook. Swaps markets are pricing in a 68% chance of a Fed rate cut by March, compared with 79% at the end of last week. But if US rates stay higher for longer, this would lead to a stronger US dollar and weaker investor sentiment, which in turn, would translate to lower copper prices.

We believe the short-term outlook remains bearish to neutral for copper demand and we do not foresee a substantial recovery in prices before the second quarter of the year, which should mark the starting point for Fed rate cuts, according to our US economist.

Author

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

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