

Metals rally picks up momentum on energy crisis and inflation fears

Base metals are rallying amid an intensifying energy crisis, and heightened inflation fears are reigniting investor enthusiasm, especially for copper. Meanwhile, a stronger renminbi may be accentuating broader demand expectations for commodities from China



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The energy crisis shows little sign of abating and is taking a toll on metals production. We discussed this in our recent note on [aluminium](#) and [zinc](#). In Europe, both aluminium and zinc have seen increasing disruptions. Higher energy and carbon prices are a double whammy for Europe's producers, raising costs and squeezing margins.

The disruptions have been uneven among different metals, and the impact is not yet fully understood. So far, aluminium and zinc have been at the forefront of the energy crisis, mainly in Europe and China, with China's sector also troubled by the emissions control measures. LME zinc prices surged to more than \$3,700/t on Friday after an announcement of further cuts by Glencore at its European based operations; meanwhile, aluminium remains comfortably above \$3,100/t.

As for copper, the impact on the supply side has not been as big as that seen in aluminium and zinc. However, LME prices have returned to over \$10,000/t amid a decline in inventory and spike in spreads. The low inventory (as with zinc) was a long-standing feature even before the energy crisis struck, which has supported the metal against macro headwinds.

However, the energy crisis has added fuel to the inflation debate in Europe, and rising energy costs will certainly push headline [inflation higher for some time](#). Meanwhile, our US economist has pointed out that there are [cracks in the Federal Reserve's 'transitory' narrative](#) in terms of inflation.

Fears of inflation could increase demand for metals as there is a perception that they are a hedge against inflation, which is especially true for copper. In the meantime, a retreat in US real rates, along with the broad trade-weighted dollar index over the last couple of days, is also driving momentum.

Moreover, the recent stronger renminbi has accentuated the broader demand expectations for commodities from China and has led to the open of import arbitrage in some metals. The broad trade-weighted renminbi is up nearly 6%. The underlying mechanism may be partly linked to the ongoing power crunch in China and the policymaker mandates for major energy companies to secure energy supplies for this winter at any cost. Our FX team has more insights [here](#).