The Commodities Feed: Rising treasury yields hit the complex

Your daily roundup of commodity news and ING views

Energy

Oil did not like the spike in US treasury yields and the rallying USD yesterday, with ICE Brent settling down almost 7% on the day. Pressure has continued this morning, with the market trading below US$63/bbl. Timespreads have also come under pressure with the prompt Brent spread now trading in a backwardation of around US$0.22/bbl, having traded at US$0.67/bbl at the start of this month. WTI prompt spreads are even weaker, with the prompt timespread moving deeper into contango. The large US crude oil builds that we have seen in recent weeks as a result of refinery outages are likely the key driver behind this spread weakness.

From a fundamental perspective, there was little behind yesterday's move. The market is becoming increasingly nervous around some countries in Europe imposing Covid-19 related restrictions once again, and in doing so raising concerns for the demand outlook. The European gasoil crack appears to reflect these worries as well, with the prompt crack trading down to the lowest levels seen since November last year, breaking below US$4/bbl at one stage yesterday.

There has also been a disconnect between the physical and the paper market for quite some time now, with the physical market weaker than the futures suggest. Chinese buying has been softer in recent weeks while growing Iranian flows have not helped. So there seems to be an element of the futures market falling back in line with the physical market.

Metals

Rising treasury yields and dollar strength has kept the metals complex under pressure. New waves of Covid-19 in some European countries, along with a setback in the rollout of vaccines in the UK has also hit market sentiment. In the very short term, metals appear to be struggling to find direction.

The latest trade data show Chinese imports of unwrought aluminium and aluminium products soared by 151% YoY to total 455kt over the first two months of the year, largely as a result of arbitrage flows. We are expecting that March imports will remain elevated, with an open arbitrage window. Turning to exports, and alumina exports over the same period totalled 20kt, down 27% YoY.

Finally, SMM reported that China's plan to restrict carbon emissions would result in reduced output levels from zinc smelters in northern China. It is estimated that about 2% of the nation's monthly zinc production would be hit as result next quarter. As of now, the output cuts are not huge. However, if restrictions were prolonged, it could tighten supply in north China. Currently, Inner Mongolia's smelters are expected to reduce zinc output by 32kt (-20%) in 2Q21. Zinc output in Inner Mongolia stood at around 160kt during the second quarter last year.

Agriculture

The latest trade data from China Customs confirmed very strong imports of grain over the first two months of the year. A recovery in the herd stock, along with Beijing's commitment to the phase-1 trade deal with the US, has been supportive for agricultural imports into China. Corn imports increased 414% YoY to 4.8mt over the first two months of the year, a record amount at this stage of year. Similarly, wheat imports increased by 265% YoY to total 2.48mt over January and February.

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