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| ***THE BHAR REPORT***  [*robinbhar@outlook.com*](mailto:robinbhar@outlook.com) *https://www.rbmc.world*  The Week in the Markets  Week of 10 July 2020 – Number 26   |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | | *Weekly price change* | S&P 500 | Shanghai | US 10-YR | DXY | $/CNY | WTI | Gold | LMEX | LME Cu | LME Al | LME Ni | LME Zn | LME Pb | LME Sn | | *Last* | 3,142 | 3,383 | 0.57% | 96.7 | 7.00 | $38.6 | $1,807 | 2,798 | $6,379 | $1,664 | $13,201 | $2,156 | $1,830 | $17,340 | | *Change w-o-w* | **0.2%** | **7.3%** | **-0.10** | **-0.6** | **-1.0** | **-3.7%** | **1.8%** | **3.7%** | **5.7%** | **2.7%** | **2.4%** | **5.4%** | **3.6%** | 3.0% | |  |
| Macro Themes As of 10 July, about 12.3mn **Covid-19** cases have been confirmed worldwide, and the death toll has surpassed 555k, according to Johns Hopkins University data. The **US** is seeing renewed rise in cases and it is affecting reopening, while there are clusters requiring local containment measures in Australia, South Korea, Japan, UK, and Switzerland. Nevertheless, the situation remains precarious (see **Chart 1**). Shares in **China** outperform again as inflation data point to higher demand and its currency the renminbi has strengthened passing the important seven to the USD marker for the first time since March, reaching 6.98 to the USD.  Global **stock markets** continue to go from strength to strength higher despite spikes in Covid-19 cases forcing cities across the world to roll back reopening plans (see **Chart 2**). But investors appeared to take the setbacks in their stride, focusing on economic data (US jobs report and manufacturing/services PMIs) and hopes of more stimulus. The most likely outcome for the coming months is that stock markets tick higher because of massive stimulus from central banks, generous government spending and unwillingness globally to lock down as thoroughly as in March in order to avoid further economic damage. The most likely outcome, at a 50% probability, is that there is no second wave and that we have a V-shaped or, more likely, a U-shaped economic recovery instead. This would imply either an instant economic recovery, which should see stock markets maintain their momentum, or a recovery by the end of the year. Either way, downward pressure on stock markets should be minimal.  We have seen the low point in global economic **activity** and the most extreme lockdowns. Economies continue to reopen; healthcare systems are able to manage any new outbreaks and a second round of lockdowns is prevented. However, what is certain is there could be considerable volatility, particularly in the coming months if case numbers rose. Governments would be less willing to implement full lockdowns in the future in order to limit economic pain.  **Central banks** are on standby to do more if necessary. For the **Fed**, large-scale asset purchases and a weakening USD (due to a rising budget deficit, financed with QE) appear sufficient for now in arresting domestic deflation pressures. Already, the huge pandemic response from the Fed has prompted concerns about long-term financial stability, and whether an open-ended programme of buying Treasury debt will encourage the government to maintain hefty levels of spending in the coming years. The Fed may want to shrink its balance sheet once the world gets back to normal, but this looks difficult, especially if fiscal policy ramps up in 2021, as expected. Importantly, inflation expectations remain contained, given the likelihood that the economic output gap sparked by shutdowns will not close for several years. Precious Metals Spot **gold** has broken above $1,800/oz thereby succeeding what it failed to do on two previous occasions, most recently in 2012. With **silver** at the same time breaking resistance at $18.40/oz the path towards higher prices has now opened up. The break could now signal an extension for gold towards the 2011 record high at $1,920/oz while silver could take aim at the next level of resistance just below $19/oz followed by $19.65/oz. The combination of high gold prices, especially in local currency terms, and economic uncertainty has prompted weaker physical demand (mainly jewellery demand in India and China) but has been more than offset by investment demand. Investors continue to diversify into gold bullion **coins** and **bars** in vaults globally and into gold-backed **ETFs**, with holdings at a record 3,621t (see **Chart 3**). All regions saw net inflows during June, with North American funds accounting for the lion’s share - accounting for 80% of global net inflows. The economic and geopolitical environment remains supportive for gold investment, with most of the existing gold demand drivers still relevant. The **opportunity cost** of holding gold remains low, as continued central bank activity keeps interest rates low or negative, while several countries continue to experience high levels of tension/unrest. Gold is glistening, but the more industrial precious metals - silver, platinum, and palladium - are faring worst due to the global recession and the substantial decline in manufacturing activity. At the end of 1H20 gold was 17% higher than at the beginning of the year, while silver was essentially flat (+0.2%). The most industrial of the precious metals, the **PGMs**, were far more downbeat - **platinum** fell by 16% and **palladium** by 18.7%. Both metals registered modest gains w-o-w on the back of a rising gold price but should continue to underperform as they are in over-supply.    **Base Metals**  **Copper** has extended gains to move close to its pre-Covid-19 highs of January, as firm demand in China and mine disruptions in Chile attract speculative money – LME spec **net long** is now 11% of contracts. No doubt momentum and trend following CTA’s are buying into strength, while other investors are long of the metal, the most macro driven base metal, to express their bullish view on the global economy. While current copper prices may not appear justified by weaker physical demand it can also be argued that a copper price consistently below $6,000/t could affect new investment in supply required to avert sizeable market deficits from emerging in the mid- 2020s. Given the long lead times needed to bring new mines into production (~5-10 years), higher copper prices are needed to incentivize mining companies to give the go-ahead to uncommitted projects sooner rather than later. **Chart 4** shows where in the copper price cycle since 2009 project approvals were announced. Metals prices are tracking closely the fortunes of the stock market, which makes sense given the uncertain economic outlook and the influx of massive liquidity into financial markets. It will take some time for metals to decouple from stock market trends and react to the micro fundamentals (supply, demand, and inventories), as real underlying economic data lags by several months. Should the economic outlook stay grim then metals prices are likely to stop rising and start falling, but they will most likely take their cue from the stock market. **LME stocks** and their trends have been a barometer of global surplus/deficit in metals markets but have proved less useful in analysis of price action as more metal has migrated to cheaper off-market storage, often tied to **financing deals** (**aluminium** has been favoured). **Off-warrant** metal stockpiles are a significant multiple of reported and highly visible LME stocks. With metals usage collapsing in recent months, the size of these inventories will give a key insight into the depth of the industry’s demand crisis. Rising open interest on the LME suggests physical supplies have increased lately and there are other signals that the off-exchange stock build this year is massively dwarfing the increase on the LME (+620kt, or 38%, since March). The LME is compelling warehouses to report off-warrant tonnages and aggregate data is to be published starting 9 July. It is clear to the LME that, over recent years, a shift has occurred from on-warrant to off-warrant storage. The consequent reduction in market transparency has caused specific concerns to users of the LME’s trading market. In particular, the fact that warranted stock may now represent only a small portion of warrantable metal has been cited as causing technical tightness in the futures market, which is not justified by the fundamental conditions of broader physical metal supply. Charts with moving averages are shown on **The Backpage**.   C Dashboard – What You Need to Know  *Source: Federal Reserve Bank of St. Louis, Trading Economics*Charts of the Week **Chart 1. A precarious situation**    *Source:* *J.P. Morgan Asset Management*  **Chart 2. Global stock markets rallying**      *Source: Trading Economics, RBMC* Charts of the Week **Chart 3. Gold ETFs: Holdings and monthly flows**        *Source: World Gold Council, IMF, RBMC*    **Chart 4. Copper price consistently below $6,000/t could affect new investment**    *Source: CRU, industry reports, RBMC* The Backpage – Industrial Metals   *Source: LME, LBMA, LPPM, RBMC*  ***For more commentary see my blog on*** [***www.rbmc.world***](https://d.docs.live.net/a109b31e324e793e/Documents/Work/Britannia/www.rbmc.world)  ***Comments, suggestions, and feedback are welcomed*** | |