

VOLATILE TIMES AHEAD



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IN A NUTSHELL

- We believe that strategically risks to global demand will weigh on oil prices as concerns over global trade and shrinking industrial production have a negative impact on global GDP growth.
- While there is some progress in trade negotiations, we are cautious whether this can translate into better fundamentals for agricultural products. In our view, it is becoming evident that China will only purchase as much soybeans and pork as it needs to satisfy domestic demand, irrespective of the promises it might make.
- In the near term, the recently calming trade-war rhetoric limits the gold-price upside. Longer-term, uncertainty in the economy due to geopolitical events, global growth and trade policy is likely to drive the gold price higher.

With an uninspiring macroeconomic outlook and 'low rates for longer,' we turn again to the traditional safe-haven asset: gold [for more details on our asset-class positioning please go to [DWS CIO View Quarterly "Ready for sideways trading" as of 9/12/19](#) and [DWS Multi-Asset View Americas as of 10/11/19](#)]. Bad news is good for gold investors but perhaps not even they would have dared dream at the beginning of the year that both the European Central Bank (ECB) and the U.S. Federal Reserve (Fed) would return to expansionary monetary policy. Gold has therefore been able to set off on another good run. At the beginning of September, it reached 1,557 U.S. dollars per troy ounce, its highest since early 2013 – still some way short, however, of its above 1,800 dollar peaks of 2011. It was not only declining real interest rates that drove the gold price. Brexit uncertainty, geopolitical conflicts in the Middle East and the Sino-American trade conflict have all supported the yellow metal. And for now they seem likely to continue doing so. Although Washington and Beijing are again engaged in negotiations, a final agreement seems unlikely in the near future. The upcoming elections in the United States are not likely to reduce market volatility either. Gold demand is the key, with the price chiefly determined by what financial investors are willing to pay. Global central banks, especially Turkey, but also China and Russia, have stocked up on the yellow precious metal in recent years, although China and Russia less so recently. For these three central banks, greater independence from the U.S. dollar is likely to be a further incentive to increase their gold inventory, not least because of the threat of further sanctions by the United States. Will gold be

tamed? Perhaps not. But at least in the short term some progress in trade talks and perceived lower geopolitical risks might limit its upside.

What about other precious metals? Palladium remains well supported, not only by Fed and ECB monetary policy and supply deficits, which potential strikes in South Africa might exacerbate further. The fact that substitution of palladium by platinum in automotive applications looks less likely than previously thought is supportive on the demand side as well.

While palladium benefits from supply deficits, oil is back again from supply concerns to demand worries. The supply shock from a major drone attack on Saudi oil infrastructure at Abqaiq and Khurais only had a short-lived effect. We see shrinking industrial production and risks to global demand as more serious for oil. Actually, the supply side looks healthier. Brazil, Norway and the United States could potentially add 1.6 million barrels per day to oil production next year. We therefore believe prices are more likely to fall than rise. Any balance will depend on Saudi Arabia's willingness to reduce production capacity to offset decelerating global demand. In the short term, however, elevated geopolitical risks and U.S.-China trade negotiations may keep oil prices volatile.

In agricultural commodities, China is experiencing food-price inflation due to the African-Swine-Flu epidemic¹, which has decimated hog parcels. Additional tariff exemptions from China on lean hogs as well as on U.S. soybeans are

¹ A highly contagious viral disease of wild and domestic pigs.

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supportive of prices. Despite substantial purchases of soybeans and pork by China over the previous few weeks, lean hogs and soybeans are still underperforming, however. And we don't believe that China will purchase more agricultural goods than needed to satisfy domestic demand despite any commitments in a preliminary deal. But we continue to monitor for additional purchases of these commodities through November. Supply shortages might be a positive catalyst for prices as data showed harvest of soybeans and corn signifi-

cantly behind historical averages, increasing the potential for frost damage the longer the harvest is delayed.

Meanwhile, the fundamental outlook for sugar is improving as sugarcane is increasingly diverted toward ethanol production in Brazil. We are closely watching the developments as the low sugar/ethanol mix² in Brazil begins to tighten the market.

GLOSSARY

Brexit is a combination of the words "Britain" and "Exit" and describes the exit of the United Kingdom of the European Union.

A **central bank** manages a state's currency, money supply and interest rates.

The **European Central Bank (ECB)** is the central bank for the Eurozone.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

Monetary policy focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

The **real interest rate** is the nominal interest rate adjusted for inflation as measured by the GDP deflator.

The **U.S. dollar (USD)** is the official currency of the United States and its overseas territories.

The **U.S. Federal Reserve**, often referred to as "**the Fed**", is the central bank of the United States.

Volatility is the degree of variation of a trading-price series over time. It can be used as a measure of an asset's risk.

² The amount of cane that is diverted to biofuel versus sweetener.

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