Ole Hansen: Commodities Are Back!

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Erik: Joining me now is Ole Hansen, head of commodity strategy for Saxo Bank. Ole has prepared a slide deck in association with today's interview.

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Ole it's great to have you back on the podcast, boy commodities, kind of forgotten it seems by most people in the macro world for the last few years, and all of a sudden Whammo, it seems as if the commodity sector overall has bottomed and reversed quite vigorously. Would you agree with that assessment? And how would you describe the macro drivers? What's going on here? Is it just a bump? Is it a dead cat bounce? Are we really seeing a secular return to a commodity bull market?

Ole: Well, hello Erik. And thank you very much for having me. You're absolutely right. I've been covering commodities in my current role for the past decade. And definitely the last six months, I haven't seen so many requests from clients looking for how to get exposure to the market. So it's obviously something that's suddenly attracting a lot of attention.

And I think rightfully so, because I think in order to understand where we are today, we obviously have to go back exactly almost a year to the peak of despair. When the pandemic started, more or less a year ago. We saw a massive collapse in demand, obviously, primarily hitting the oil sector. We saw producers step into to support the price. And that really set the the oil market on a recovery trend. If you look at the agricultural space, we seen China reemerging on the buy side and accelerating their buying of key products, such as soybeans and corn. They obviously had a Hawker that was decimated couple of years ago that's now rapidly being rebuilt, and they need massive amounts of corn and soybeans in order to do that. So that helped us well.

And then as we moved into the year, we will once again presented with a massive amount of stimulus, coordinated race to the bottom by central banks around the world, led by the majors, US, Europe, Japan, and the UK and suddenly money was basically for free. And stimulus was coming and again, we've seen the market react, suddenly starting to increase and to look for reflation and look for inflation hedges.

And I think there's a key time if you look over the past year, it was basically the beginning of November. We had the first vaccine announcements. And also we had Joe Biden winning the election in the US that kind of turbocharged the whole decarbonisation theme, green transformation. And we've seen some of the some of the commodities respond to that as well, because we had to have to remember that in order to turn green, we cannot turn green without many of these key raw materials.

So I think just to look at some of these amazing gains we've had on slide three in the deck, we've seen that these performance since early November. As I mentioned, we just basically got broad gains, basically apart from precious metals. And I think that's the one that stands out because and one would think that's surprised many because if this whole, or part of the rally was driven by reflation then why on earth has gold done as poorly as it has. And i think in order to understand that we need to see that recent yields have spiked with the spike that began back in January, and accelerated last week. It's simply a period that gold is struggling to put up a defense against.

But generally we're looking for stimulus, we're looking for banks to be supported over the coming years, we're looking for governments increasing spending. And that basically means a lot of money will flow into infrastructure and into the hands of consumers. And that will continue to, to lead growth in the market. And then just finally, I think very important, as well, one thing is that we're seeing a pickup, expecting a pickup in demand. Some of which we're seeing already, but also we're coming out of a decade where as you mentioned, the beginning commodities really not been invoked. It's not been in a sector where investments has gone to. People have been piling in money into the technology sector as well. And that basically leaves us with several of these markets, key markets with under investments and therefore also the risk of that we see supply basically not keeping up with demand over the coming years.

Erik: I find it very interesting given the narrative that at least I perceive in the market. It's really about stimulus and of course green energy is a big priority of the Biden administration and definitely infrastructure build up. That would say to me, okay, infrastructure build, I would expect the metals and industrial commodities to be the strongest. I would have expected the agriculture to kind of lag behind them because the story is not really about agriculture. It's more about government spending on infrastructure, and particularly the focus on green energy. But boy look at the grains and the softs in your chart here on page three. They're the only things that are or I should say, energy is the only thing that's outperforming grains and soft. any explanation or insight as to what's going on there?

Ole: Yeah, I think we have to boil that down to China. Chinese demand and whether we basically come out of, we've had four or five years where crop production around the world has been relatively unharmed by all the potential risk from climate change, especially in some of the key production areas in Russia, in the US, and in South America. And that's started to change ast year, we saw several moments of worries, which was related to the production. But then

clearly the massive amount of buying that came in from China also did its part so the rally has been driven primarily by corn and soybeans.

And this is really the bad type of inflation because that's the one that hurt, the one that that we can afford the least maybe we are now seeing country stands who complain about rising inflation, rising food costs. And just last month, when when we saw a spike in wheat prices after Russia introduced export taxes on wheat in order to maintain local supplies and keep domestic prices down. We saw wheat prices come within I think it was within 10% probably less than that of the peak we had back in 2011.

And obviously that was the one that partly led to the Arab Spring where we had food crisis in several countries. So we come from out of years of plenty suddenly into a market where we see see tight supplies. And we've got a slide later on as well, just highlighting how much that market has moved from contango for a number of years and now into quite a steep backwardation.

Erik: Let's talk a little bit more about precious metals and why they're underperforming here. Because, as you say, on one level, the narrative about governments, you know, spending a lot of deficit spending, printing money, debasing fiat currency, sounds like it ought to be really good for precious metals. Of course, it is easy to see that if you look directly at the observed values for real yields, they're increasing. This baffles me all that because yeah, I get it that Gold's enemy is increasing real yields. But it seems to me like inflation is just lagging.

And I would expect the market to look beyond this or look across this and say, look, you know, the inflation is coming at some point, that's going to offset those real yields. Gold's eventually going to move up. You'd expect people to be you know, buying the dip a little more aggressively. They're not, we're really seeing these real yields drag gold down hard. Would you agree with the way I've described it as to what's going on or what am I missing here?

Ole: I don't think you're missing anything, Eric. And we have the firm belief as well, that inflation is coming, and it is going to be higher then what the market is currently anticipating. But it also means that we've got breakevens now 10-year breakevens, just around 2.2%. And that could easily be a lot higher in 6 to 12 months. So it seems like it is just the market. They need the confirmation in order to respond to it. And also we know also how hedge funds react to primarily on momentum and technical signals.

And we've been in a downtrend trend now since August, so there's nothing in the price right now that's telling a fund to get back in the market. So they're sitting on the fence waiting for the breakout. I worked for a hedge fund in London for 10 years before I returned to Denmark in 2008. And I mean, we were missing, we would miss the bottom and we will miss the high but we will get involved when the when the signals were right. And right now there's absolutely no buy signal in the gold price. We probably need to see from this level, maybe even $100 higher before that start to emerge. But I think the narrative is the or the key drivers are still the real yields and the dollar.

And the big discussion right now is and we've been talking about this in our notes recently that we probably needed to see some pain before the gain because we need to see yields rise to a point where the FOMC starts to blink and potentially starts to talk about some kind of measures to cap the upside on yields. And obviously if that happens, right at the time when inflation starts to pick up, then obviously there's only one direction for real yields and that's back down again.

So I think the market didn't like the speed of the the change that we have had over the past week. We broke a key level $1760-65, that old band. And that basically just attracted some additional selling but we haven't broken any major level right now. I think the big line in the sand for me is the $1672-$1690 area. That's both the local lows we had may and June last year. But also it's 61.8% retracement of the whole rally we had from March up to August. So that really is a key area that needs to hold for now.

Erik: And if we were to see a close below that, if we were to break below, say $1680. What would that tell you? Does it mean the floodgates open? And we're all the way back down to $1350? Or what do you think happens at that point?

Ole: I would doubt it because I still firmly believe and still see a reason for holding commodities, holding precious metals in a portfolio. But it will obviously from a technical perspective further delay recovery and potentially also, obviously lower the eventual peak that we will reach. But it will attract some additional selling. But I think on that basis, we also just have to remember that as I mentioned, hedge funds have been cutting back exposure since almost since August last year. And their lens now is down to I think the lowest in almost two years. So the position that potentially needs to be adjusted further is not as great as we've seen in the past when we've seen some major breakouts.

Erik: Now the alternative explanation that some people have put some stock in is look what's really going on with gold is all about Bitcoin. What's happening is a significant number of investors who are concerned about fiat currency debasement who previously would have invested in gold are choosing Bitcoin instead or other cryptocurrencies. Have you guys done any analysis? Do you have any way of measuring whether that's going on? I mean, it sort of sounds plausible, but how do you measure that? Do you think that's what's happening?

Ole: I've heard that for a long time now. And obviously, it is a very valid discussion. I just struggle to see Bitcoin as a, well you can't call it a safe haven, but a place to park your money because the volatility is just simply too great. When you see 30% moves up and down in no time that basically means, I think for someone who wants to preserve their wealth, it just simply is too volatile. But no doubt it's attracting a lot of attention. And if you are a paper investor, not physical investor in the goldmine, just looking for direction. Then silver comes into that category as well being a high beta gold. Then clearly the Bitcoin, or the whole coin area has offered great opportunities. But boy, also a lot more volatility.

Erik: Let's move on now to the Green Revolution. Certainly with the shift to the Biden administration, we've got a clear message that there's going to be more focus in the United States on something that, frankly, the rest of the governments around the world were already focused on. Which is climate change, and in general, being more environmentally conscious.

Moving on to page five of your slide deck now, what does this mean in terms of commodities, which commodities will benefit from a green revolution?

Ole: Several of them and we'll start with the most quick one. So obviously, the rare earth metals, they are still going to be in strong demand. And that's potentially could become a geopolitical punchball over the coming years. But the one that obviously has attracted most of the attention and most of the imagination from investors is copper. Because it is the metal that's required for the whole electrification process. We've seen China obviously come up with a 2060 plan for that area. Europe is already on route, we still wait to see what comes out from the Bible administration.

But there's obviously a clear expectation that the demand for Copper towards that transformation is going to pick up over the coming years. And from a Copper perspective, from a price perspective, it can't really happen at a worse time because the pipeline in terms of new production coming online over the coming years is pretty weak. And that basically means we're starting the year 2021 with inventories already at very low level for this time of year. So it is a market where there's a lot of potential for for higher prices, and one where we are probably likely to see a new record price. It is also of the metals, probably one that got the biggest amount of liquidity. Also basically meaning that from a speculative perspective has become very popular.

We saw just recently, news from China that one of the big whales out there accumulated $1 billion worth of copper in just four days after the Chinese New Year. These positions obviously does create some some nervousness if we are seeing a short-term pause or consultation in the market. But so far, copper we've seen a small correction this week so far, just like all we haven't come close to break any key levels and something like copper could easily drop 10-15% and still only just return to the uptrend, that has been put in place since March of last year.

So there is still probably in the short-term some risk if we continue to see yields move up there by seeing the volatility move up both in bonds and in stocks that could trigger some periods of deleveraging just like we saw last year. And obviously deleveraging, at this moment in time, could potentially have an impact on some of these commodities, where there's been quite a lot of pent up demand from speculative investors.

Erik: Speaking of speculative investors, let's talk a little bit more about copper in that context. This is a tough one for me Ole, because on the one hand, I couldn't imagine a better bull market argument than we have right now for copper in the long term because we've got to accept that this electric vehicle revolution is real, and every single electric vehicle needs something like 10 times more copper than a conventional vehicle that takes to produce.

What most people don't even consider is that we really are going to need to rebuild the entire electric distribution grid in order to charge all of those electric vehicles. That's more copper. And we're also contemplating infrastructure spending for the sake of stimulating the economy. That's more copper. You just couldn't ask for a stronger argument. But boy, you couldn't ask for a more crowded trade either. Could you? What are you telling clients? Is it too late to get in on this? Did you wait for the pullback? I mean, I've been waiting for a big pullback, there haven't been any big pull backs.

Ole: I think at this moment in time, we are urging caution not because what's happening in in copper or in some of the commodities where fundamentals are sound, but just the outside markets, because commodities are not an isolated island. Because these days, it's not just purely producers and consumers that meet to discuss prices. There's a lot of so called paper demand involved as well. And these are impacted by developments elsewhere.

And we just saw that over the past week here that after the bond spike that we have already seen some mild profit taking that hit the market. I think there's still the risk that we haven't seen the end of the rally in yields just yet. And on that basis, urging some caution here. And as you also said, could easily see it drop quite significantly without even change the bullish uptrend that we have had in place since the low last year.

Erik: Ole you mentioned rare earths earlier. I just like to clarify what is the reason that you see it? Is it because of their use in windmills and electric motors or why do you see the rare earths as being so important?

Ole: Its component is used to in so many different appliances and from, as you mentioned, from breaks in terms of very, very powerful magnets to the arms industry as well. So the thing about rare earths is that they're not actually that rare, but no one really wants to refine them apart from China and the States. And that means that the rare earths are being produced around the world but shipped to China in order to be processed. And that is obviously given China quite a big scene in this market. And one day we were starting to see breaking potential breaking down a little bit. A couple of new major companies has been established over the past year. And obviously I live in Denmark, we Greenland is part of Denmark and I think there's going to be an increase focus on Greenland. Trump obviously offered to buy it a couple of years ago, was turned down by the Prime Minister, but I think there's going be a lot of focus on Greenland from a rare earth mining perspective.

Erik: Returning to page five, what else in terms of the Green Revolution should we be thinking about in terms of commodity trends,

Ole: I think to other metals, which I like and which we obviously follow quite closely. That's silver, because the solar panel, and then also Platinum because of the increased regulations in terms of emissions from vehicles. Especially recently in China. And we've seen Platinum as a

major winner since November, where it was trading at a discount of around $1100 to gold. Now that discount has narrowed close to $500. And there's even the potential for that discount to evaporate over the coming years. Because again, demand staying robust. One thing is industrial. Obviously another one is financial paper demand.

Then we have to look at the supply side which is quite limited, primarily deriving from South Africa. So Platinum I think the reason why it hasn't really been caught on that well is because it's just a tiny metal. It's a factor, multiple factors smaller than the gold market, smaller than silver. And it basically means that it is one of those trades where when it gets too crowded you want to get out the door. It is simply too small. And that creates some volatility.

But just like palladium had a phenomenal run in recent years, it looks like the time has now switched to platinum. And then there are emerging signs that some of the producers, they have the emission control systems, they are starting to switch to platinum. So platinum is one, silver is going from the increased use of the solar panel together with the investment demand, which has also been quite strong over the past couple years.

Erik: What about battery metals that are used in producing electric vehicles?

Ole: They'll be part of it as well. I tend to focus primarily on the metals that we can trade. Some of them are a little bit more quirky, but anything that, any metal that is used in the electrification process, as in batteries clearly will continue to be in demand until potentially new discoveries are made in new battery technology. But for now, as we say we can't turn green without getting some stuff out of the ground first.

Erik: Moving on to page six, this is the slide that scares me a bit Ole. It reads hedge funds have accumulated a record long exposure. I hate to say it but hedge funds are kind of known as the dumb money in the commodity business. Usually when they accumulate a record long exposure, it means the markets topping, is that the case here?

Ole: Well, it's most certainly a signal that they're looking for even higher prices. And I think the phrasing, the dumb money is clearly because they're always the one having the biggest position when the market turns. They are the most exposed on the long side when the market suddenly flips around. But obviously what we have to remember as well that hedge funds trade on momentum, they're looking for the big moves. And having been long since, well have been long, aggressively since August last year that they have obviously reaped a lot of rewards for that so they will take some pain if we do see a correction. But I think also it means that the pain threshold for many of these positions are quite substantially lower then where the current market levels are. So we need to see, I think a major change in the technical or the fundamental outlook in order to really rip into that that long.

But I think the that potentially you could be most worried about is the agricultural position. because what we have to remember is if you want to produce more copper, it can take you 5 to 10 years from the decision is made to copper is coming out of the ground. If you're having a

strong year in terms of crop prices, farmers, and anecdotally, I'm a farmer boy myself, grew up in one. And if we had a good year, and we had a good production, we didn't go on holiday to Mauritius, we bought a new tractor instead. And that basically because we want to constantly improve production. And that basically means we could expect weather permitting a strong response in terms of crop production, this coming season. So I think the next few months, as we enter the US, the US planting season and the growing period, that could be quite critical for the agricultural space. So that's probably one that because of the cycles are so much shorter that could potentially be most exposed.

Erik: And on page seven, you're saying that this cycle involves broader exposure than previous buildups? Why is that? What is it that's getting exposure that wasn't getting exposure before.

Ole: But I think we can just combine slide 6 that we just talked about and slide 7 because this is the table I produce on a weekly basis based on the data from CFTC. And if you look back in the previous spikes we had in terms of positioning from funds in 14 and 17 and 18, it was primarily driven by the energy market. A strong build up in energy exposure. But this time around, we can see that agricultural spaces are really participating quite aggressively. I think we're close to a record long. If you look at some of the main crop commodities that are agricultural commodities.

So I'm highlighting in the table here, but if you look down in the net, which is highlighted with a red line. You see we've got long positions across the board. There's not that often we don't see, one or two or more commodities where there's net short held. But the fundamental drivers just simply been so strong that we're seeing net long positions across the board. I think also, we have to remember that a lot of investments are handled through investment funds, ETFs which buy into some of these major tracking funds, tracking some of the big providers of commodity indices, like the S&P, GSCI, and the Bloomberg Commodity Index and for every dollar you invest into these that money almost has to be spread out across the whole sector. So, if you are seeing strong index buying of some of these commodity index funds via the ETFs, it will have a positive impact on on most of these commodities.

Erik: Ole let's move on to page nine because I think you're making a really important point here about role yields in a contango market as we had in crude oil after the crash. Boy, you're really have to believe in the market in order to invest in the front month contract as you're losing ground every single month. As you roll that contract forward, you get a worse and worse price. Now we get a better and a better price as we move into structural backwardation. How is that, I personally follow the crude oil market most closely. Is that happening across other commodities? And what does it mean in terms of I would think it would bring more confidence and more investment into the sector.

Ole: Absolutely, Erik, and I think we just if you just go back one slide to slide eight, this just basically highlight what has been going on now for the past six months, across the commodity space. You're absolutely right, we come out of a decade where we seen ample supplies almost

across most commodities. We have had pockets of tightness, which has led to brief periods of backwardation, but generally it's been a decade of plenty.

Basically, we had the massive Bull Run during the first 10 years of this millennium creating a lot of excitement about the sector, a lot of investments going into the market and there's a supply suddenly starts to be beefed up the demand growth that didn't catch up with the increase in supply and that led to almost a decade, at least in the last six years where we see ample supplies and that's reflected in the in the curves because as people normally say, "the curve doesn't lie". If it's in backwardation, it does indicate that someone is prepared to pay a payoff to get immediate delivery.

And looking at the left graph on slide eight, you can basically see how the roll yields. If you take this, it's kind of non-scientific, but you take the average roll yield of 25 commodities, excluding natural gas because it's a bit of a beast on his own. But for the first time last year, the end of last year, we can see that the average roll yield moved into backwardation for the first time since 2014. That is a major change. And it is one if you are a passive long investor in commodities, you would have been suffering for the last six years from negative roll yields. But now we can see it's basically jumped to at least a decade high. We are close to 5% that you get as a passive role by holding along the basket of 25 commodities for a year.

And if you look on the right hand side, we can see where the big changes has occurred. The light blue is where we were 12 months ago. And the dark blue is where we are today. And you can see for now the big change has really been in the agricultural space, especially the soybeans and corns where we are now suddenly looking at roll yield returns of more than 1% on a monthly basis. A year ago, it was hovering around negative 5%. But generally, there's not that many commodities left where we don't have a positive carry on. And that really does matter.

And that takes us back to slide nine instruments Erik, with the roll yields because for the past five years. If you just look at the spot contract, and you look at where the spot contract is trading today relative to five years ago, well it doesn't look too bad. But you obviously have to remember that these contracts, they have to be rolled on a monthly basis and with a contango in place for so long, you are basically rolling yourself out of money. And that basically means that the Bloomberg Commodity Index, which is a bit more broad, we can look at that a little bit later. It has seen the gap of around 40% and a gap of around 45-43% on the S&P which is a bit more heavy in energy. And that has now started to turn around and if I had a broader chart just for the last six months, we could see how suddenly that it started to reverse.

Erik: Ole some of our listeners, myself included are commodity traders who trade the futures markets directly. But that's not for everybody. One of the things that may not be clear to our listeners, I'm not sure if from this slide on page nine is. What this chart is really telling you is that whole business about how you know commodity traders tell you don't buy the ETFs you get killed by the contango, don't do it. Don't do it.

Well, it's changed buying the ETFs is a good idea now. When you have structural backwardation, so for people who are not trading the futures directly, which ETFs? How do you pick one? Let's take a look at page 10.

Ole: Absolutely. And you're absolutely right. There's no doubt that the market structure has changed and suddenly it's not no longer a drag and but it's also important to note that there are many different indices out there but I've just highlighted two of the biggest that's being tracked, being shattered by billions of dollars of investment from funds around the world and through ETFs in the most regions.

But what you have to be aware of is that the S&P historically has always been very weighted towards the energy sector. You can see that on both the pies and also on the the chart on the left and on the right that the energy sector is something like 54% of the total exposure in the S&P GSCI. That is obviously important because if you are an energy bull and you think that's where the biggest pull is going to come from, well then that's the one you should look at. But at the same time, you also just put a few more eggs in your basket just to spread your risk a bit. So that could be a good idea.

But if you are more inclined to look at the first of all looking at those where we've seen these big moves towards backwardation and thereby roll yields. And you're also looking at a broader inflation hedge, that is probably the Bloomberg Commodity Index that you need to focus on because they are set up to more or less track one third from each of the main sectors: energy, metals and agriculture.

And if we for instance, as we talked about the trends of green transformation, if the metal space is really going to be where a lot of the focus is going to go into continuously also from the fact that again the metal space is not, you cannot just bring supply back online. If prices go high enough in the oil market, the shale, shale oil production will increase, no doubt because there's money to be made. But the metal space will be the one that's least reactive to increase demand. And that means that's probably where the price potential are the greatest. So just be aware that there are different compositions, but that also means they are different ways to conserve individual preferences.

Erik: Let's move on to page 11 because I want to come back to this question of precious metals and real yields. I think our listeners understand from previous shows that real yields are super important to precious metals. What's been baffling me is it feels like the market just can't see what to me is obvious, which is yeah, real yields are increasing because nominal yields are increasing. The nominal yields increasing with no inflation ain't gonna last, it's gonna change. But it seems like the market doesn't want to look past what's in front of us right now. How do you make sense of this? And what do you think comes next? How much longer does this real yield induced, temporary cycle down in gold continue?

Ole: It will until we start to reset our inflation expectations, or we start to see yields break high enough in order to force some kind of response from the Federal Reserve because as you can see, on this one, on this slide here on the on the right hand side. The yields are, the nominal yield is a factor, is the sum of the inflation and the real yields and what we have seen over the past, well, over the past year or so you probably even longer that breakevens has slowly been creeping higher to reflect high inflation expectations going forward. But over the last few months, it's almost plateaued.

And during that time, that means basement as nominal yields rose, it was real yields that had to give and they were rising almost in line with nominal yields. So we need to see the so it's all about inflation. If we're whether we're right or wrong that inflation is going to be play a bigger part than the market is currently pricing in. I think the word that could really turbocharge precious metals would be yield curve control.

Ole: I think there's a lot of arguments for and against. One thing is that Australia go in and then Japan go in and cap the upside on the yields. But the world's reserve currency and the USA, I think it's basically if they're capping yields, they're almost giving the government a blanket check to spend, because they're just going to keep the yields of financing that prevent financing rates from moving higher. But at the same time, I think it's too early for yields to move dramatically higher.

So if we do see some kind of an attempt to curb yields then real yields are likely to go lower if our expectations for inflation, that inflation would be higher than what we're seeing it right now. If that comes to fruition, then that would be your next move in gold. And potentially that could be three that could be six, six months out in the future. So I think gold right now is very much a patient game.

Erik: Now let's play devil's advocate and look at the other side of this of how we could be wrong here. Let's suppose that somehow you and I and a whole lot of other smart people just got this inflation call completely wrong and we're just going for deeper deflation. I suppose one side of the argument would be well that really spells bad news for gold because if you saw no inflation at all, and yields continued to back up on a nominal basis, well that would really just do a number on the real yield.

The other side of that, though, is well, wait a minute, if you really saw deflation. Then this backing up of nominal yields would probably reverse. Is that a safe bet? Or is there a scenario where this really turns summer for gold?

Ole: I think if we are wrong on inflation, then the reasons for having a portion of gold in your portfolio starts to be reduced. And could have an impact. But I think at the same time if it's happening in a scenario where yields just continue to move higher, do you really want to be long bonds? Where you're losing losing capital, you obviously will get repaid your full investment. But from an investment perspective, continuous rise in yields is really not an environment that from

an investment perspective is going to gain much from during that period. So I think that the risk is obviously there.

But looking at the tightness that we're seeing in across the world, and obviously, commodities are up a lot. Freight rates are three, four or five times higher than they are normally. There's a lot of congestion there. So I think we are just literally weeks if not few months away from businesses bonds to pass on the higher prices to consumers because they have to go somewhere to pass on the the cost. We're seeing PPI rising in China. China's being a major exporter of consumer goods and that will have an impact as well on price pressures. So yeah, it is obviously healthy to be the devil's advocate. But it's just very difficult to see a scenario where inflation is not going to move higher and potentially even surprise to an accelerated extent.

Erik: Moving on to page 12, copper prices have more than doubled since their march lows and hey, the pandemics not even over yet. Once the pandemic is over, does that mean we're headed toward a triple?

Ole: Well, I suppose there's this old saying that the best cure for high price is high price. The question is, if that's still valid when it comes to something like copper. And if you look at where it's used, I suppose in electric car manufacturers. Even though its price goes up, it's still a relatively a small part of the total cost of the car. But how much further can it go? Well it really, if we are having a major supply deficit, then in theory, the price can go a lot higher and we will certainly not rule out that we're going to eclipse the record highs that we saw in 2011.

I think the biggest risk to copper in the short-term is probably China because we're seeing some weakness in some of the data, credit impulse is slowing and that could indicate that the impact of the massive spending that they did last year, potentially is starting to fade a little bit. I put in on the slide you can see the copper and its relationship to the Chinese Renminbi, so if we do see a period of remember weakness, so that potentially could also just take the top out of copper and then create that pullback that you've been looking for.

And we have to remember, if you look at China, they consume roughly around 50% of the global mined copper, and they probably hold what around 5% of the global reserve. So they are obviously a key driver. But I think what will carry Copper higher will not be China, it will be the electrification of the world which we will see to an increased extent both in Europe and in the US.

Erik: Moving on to page 13, green transformation and its relationship to correlations in commodities.

Ole: Yeah, that's a little bit of a quirky one. Because, again, you can always find a chart that suits your narrative, but I think this one is quite interesting. This is just basically looking at the copper-gold ratio relatively two the 10-year bond yields in the US. And you can see that to me is pretty much a correlation that has been playing out for the past 10 years at least and you could

probably could go even further back. But what we noted since the load last March and accelerating during the past six months is how we're seeing the dislocation.

First of all, copper has been rallying faster than gold. So the ratio has been going higher, but at the same time it's also rallied faster than the pickup we have seen in US yields. And the question is really whether that is due to the green transformation that we are seeing a shift in demand patterns for copper which basically means that it can command a higher price going forward relative to other assets that it did in the past.

Or it could just basically be telling us at this stage that it is too high relative to gold or yields needs to go even higher. So there are three variables here that could move. I think the scenario that could be really quite fascinating what would be the again if we see some kind of a Yield Curve Control because then the yields will stop rising at the same time, we potentially could see the copper-gold ratio come down because gold will start to reclaim some of the lost ground. But for now, there's a dislocation indicating that either copper is too expensive or yields are too low. Or we basically have a new world where the green transformation is going to cater for much more copper demand that we've seen in the past.

Erik: Let's move on to my own favorite topic of crude oil. Boy, you know, it seems to me we're almost up to 65, spot 65, which was the kind of double top at the end of 2019. And then January of 2020. I'm not sure if we break through that. What's next, there's not a whole lot of obvious resistance levels up there. What do you make of this market? Are we nearing a top? Or are we just beginning?

Ole: I think we're nearing a near-term top before we eventually move higher again. I think the fact that we have rallied what almost 30%, since Saudi Arabia curbed production back in January, that obviously highlights the importance of supplies being kept away from the market. So the rally we've seen so far has been a supply or lack of supply driven rally. Now obviously, we expect that they will be replaced by a demand driven rally going forward. Once we all get the COVID Cloud start to lift and we can get back on planes and back in the cards and start to be more mobile.

That's obviously the narrative at a time where as well, the US producers are more suddenly become more responsible, more interested in passing money back to the investor than just going all out on the drilling, drilling for craziness. So that's I think the narrative. But I think we also just have to see there was quite a significant amount of demand from Asia. During the past six months, I've read a few reports now over the past 48 hours that some of that demand is starting to slow from Asia, from refineries there.

We're seeing India contemplating lowering taxes on fuel, because prices are just simply getting starting to get too high. Inflation is getting uncomfortably high. So we are ready at this level Stan to see the potential impact on some of the major consumers around the world. So I think the narrative that we are seeing. We are going to see a return in demand to where we came from a

bit more than a year ago, that's going to hold truth because even though we are seeing, even though we see the green transformation and electrical vehicles and so on.

We will still have a growing population in parts of the world where demand growth is where most of the demand growth is coming from. So it will still take a number of years before we see a peak in in oil demand and into that we are seeing a US shale oil sector which has become bit more prudent than it's been in the past. The lack of investment because of the sector is just not attractive for many investors these days. And that's the whole ESG, that's something that's impacting mining companies as well. That the availability of finance is not as great as it has been, that will eventually drive the price higher. But I think I've got a sound, bit of sound skepticism at these current levels.

And as you can also see, on slide 14, we clearly need to see a more optimistic view coming in from OPEC, IEA and EIA ever since August last year they have been downgrading their demand growth forecast for 2021 on a monthly basis down to around five and a half million barrels of growth this year. And as we recall, OPEC+ still has around 7 million that they can unleash onto the market, not strong growth in the US so that will still be below the previous peak. But generally, I think the rally in oil has potentially not much further to rally at this time. I think it's going to be a little bit more difficult to come by. But as we move into 2022, I could easily see it move higher.

Erik: Ole, you mentioned agriculture previously, anything you want to add here on page 15?

Ole: Just the one I've mentioned before that we've gone from years of plenty to tightening supply. The one-year roll is now across the agricultural sector that's really where you'll find the biggest roll. We also find the biggest speculative long so I'm just as I mentioned earlier, I'm a bit cautious for the coming months because we are getting into a massively important planting season in the US which could really set the tone for the prices into the summer. But we starting the year on a very strong footing.

Erik: And Uranium, a subject near and dear to many of our listeners hearts. The price of the URNM ETF is more than doubled. Since we first discussed it here at macro voices What's going on?

Ole: I think the realization that we can simply not move to a less carbon intensive energy supply without uranium, wind, and solar is obviously an important part of the mix. But we need some base load and that base load is really sorely missing. We've seen that in recent incidents. And that basically means that I think uranium is becoming less of a bad word than it was back when I was young in the 70s and the 80s. The technology has moved on.

So I think it will come back, we already are seeing quite a big growth in the number of new reactors primarily in Asia. But I think what is pretty certain is that if Uranium or U3O8 stays at these current levels, we're going to run into a massive deficit because it's just simply not

profitable enough for the mining companies to beef up production. So I think uranium sector is one that I I want to have an exposure to over the coming years.

Erik: Ole, I can't thank you enough for a terrific interview. Before I let you go, though, we have a broad audience here, mostly institutional family offices, high net worth investors, but there's also a retail component. You guys are one of the most respected commodity advisors in the institutional space, but I believe you also have some retail offerings as well. Tell people how they can find out more about what you do at Saxo Bank.

Ole: Well, for those of you who doesn't know, Saxo Bank is basically a platform we offer access to more than 35,000 markets, or tradable products around the world. We got clients in more than 170 countries. So we operate in multiple legal jurisdictions and in multiple languages. And if you want to follow us from the strategy team. We are relatively active on Twitter, you can find me @Ole_S_Hansen. And otherwise, if you can take a look at analysis.saxo and if I should just highlight two daily publications. It's our podcast where we try to stick our neck out on a daily basis. Just what's moving it, where we see the market go next. And also just a quick take that we put out early in the European hours just to summarize what's been going on overnight.

Erik: Well Ole, I can't thank you enough Patrick Ceresna and I will be back right after this message from our sponsor.