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Commodity focus switches from Syria to the FOMC

Fear about a Western military strike on Syria waned considerably this week as representatives from Russian and US governments sat down to hammer out a deal that could remove Syria's chemical weapons. As a result, oil markets drifted lower while gold went into a tailspin, not least due to the increased focus on the Federal Open Market Committee meeting on September 17 to 18, when the US Federal Reserve is widely expected announce the beginning of the tapering its massive asset purchase programme.

Energy, industrial and in particular precious metals sectors all fell driven by the two above-mentioned factors, but also due to lingering doubts about the continued economic recovery following lower-than-expected production data in Europe and the recent slowdown in US job creation. The agriculture sector was mixed, with soybeans and corn going their separate ways, while three of the top performers were soft commodities, such as orange juice, sugar and coffee.

Crude oil lower but uncertainties persist

With the risk of an imminent US air strike on Syria now much reduced oil prices gave back some of the risk premium that had been building over the past few weeks. As a result, Brent crude saw its first weekly drop in five weeks but still managed to re-establish support ahead of USD 110/barrel, which represents the average price over the past couple of years. Although Syria now poses less of a risk of upsetting the balance in the Middle East, which produces 35 percent of all global oil supplies, some tough negotiations are ahead and therefore the situation could easily escalate again and cause renewed supply concerns.

In terms of supply concerns, a port strike in Libya continues to support oil prices. Daily production has dropped from 1.3 million barrels just a few months ago to 300,000 per day currently. This has led to a tightening in the global oil market despite Saudi Arabia pumping oil during August at the fastest rate in 32 years. This has put oil stocks in OECD countries under some pressure with its inventory of crude and refined products dropping to the lowest level in two years compared with the long-term average for this time of year.

A monthly report this week from The International Energy Agency (IEA) also helped to keep a floor under oil prices. The IEA raised its 2014 global growth demand for crude oil to 1.1 million barrels per day. It expects the overall macroeconomic outlook to continue to improve but also mentioned that the slowdown in emerging economies during the last quarter may have a negative impact if it carries on into the new year.

An expected seasonal slowdown in demand as we head towards October should help rebuild inventory levels and depending on when Libyan oil again begins to flow the price of crude may eventually move lower as we head towards the fourth quarter. A price move back below USD 110/barrel carries the risk of further long liquidation by hedge funds which could result in the price overshooting to the downside.

Gold and silver falls hard as tapering looms

Gold fell the most in nine weeks as geo-political tensions eased and FOMC stimulus speculation rose. The sell-off was given a technical boost on Thursday once the triple line of defence in the USD 1,350/oz area gave way and the sell-off was only halted when technical support ahead of 1,300 caused some profit taking ahead of the weekend. The move lower was driven by momentum traders such as hedge funds,who during August had sharply increased their net-long exposure to gold. As this increase was primarily driven by short covering the change towards more negative sentiment left many funds with ample room to re-instate short positions into a falling market.

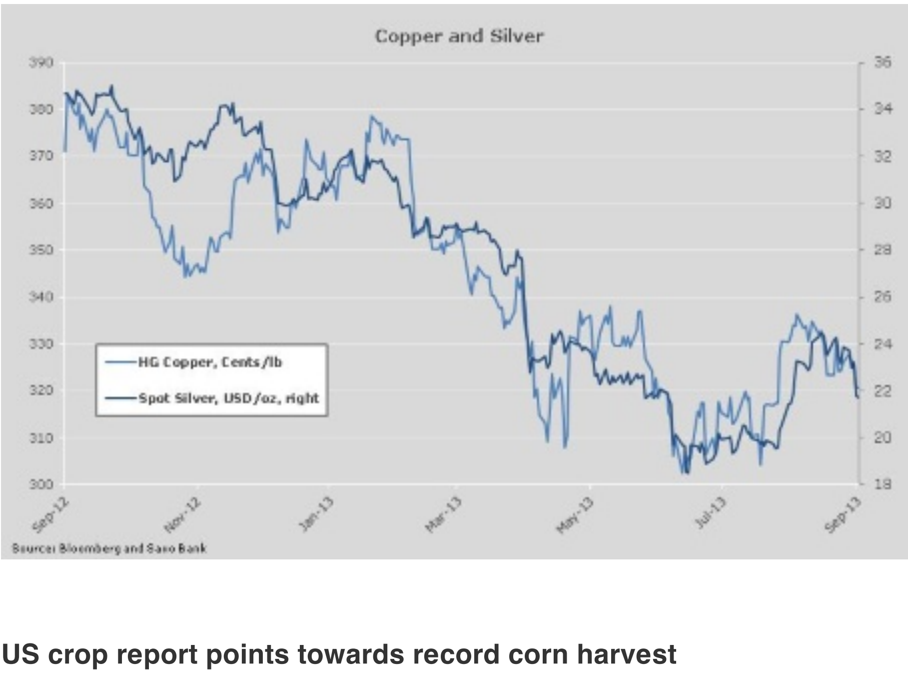
Uncertainty surrounding the impact of next Wednesday's expected announcement from the Fed carries the risk of keeping precious metals on the defensive until then. But even though tapering will commence there could be an argument that much of this announcement has already been priced into gold at the current levels and as a result a relief rally following the announcement cannot be ruled out. Such a rally would most likely need the support from falling government bond yields where the US 10-year yield is hovering just below three percent after rising more than one percent since tapering was first mentioned in May by Fed chairman Ben Bernanke.

Holdings of gold in Exchange Traded Products are on track for a second week of net reductions which also highlights the continued lukewarm attitude by institutional investors. This important investor segment is required to change sentiment as physical demand alone will not be enough to drive prices higher at this stage.

The technical levels to look out for now in gold is support at 1,277, a break below which could signal a move to a new low for the year. A move through resistance at USD 1,360/oz is required to change the sentiment back to neutral before key resistance at 1433.8, the August 28 high.

Copper effect on silver

Silver has reacted to the same news that drives gold with some added weakness coming from continued profit-taking in copper. The December contract of HG Copper (HGZ3) has moved to the lower end of its 3.20-3.40 USD/pound range as the outlook for demand has been questioned following some weaker than expected economic data lately. It was the copper rally in August which helped kick off a major rally in silver (and gold) and as we now see a reversal silver has been struggling and sold off harder than gold.



US crop report points towards record corn harvest

The monthly crop report for August from the US Department of Agriculture painted a very different picture for corn and soybeans. While US farmers will harvest a record 13,843 million bushels of corn this summer, thereby helping global inventories to rise to a 12-year

Corn prices fell on the news while soybeans rallied to the highest close so far this year, not far from the psychological level of USD 14/bushel. As a result the price ratio between November Soybeans and December Corn has reached a level above three for only the second time in five years. Such an elevated level is being viewed as unsustainable from a substitution point of view as consumers may switch to corn at the expense of soybeans.