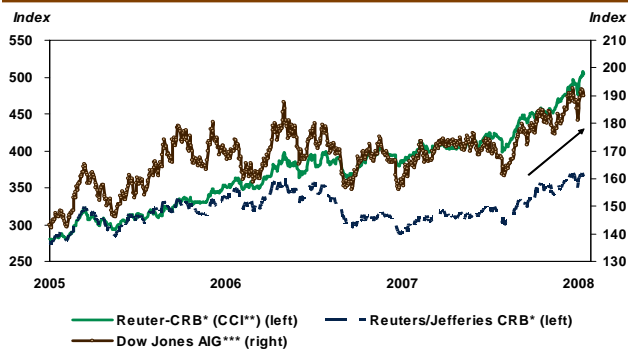


## Commodities stand up to the darkening economic outlook

Commodity prices have continued to advance overall in the last few weeks, despite proliferating indications that global economic growth will slow substantially in 2008, and that the United States could soon slip into a recession. Problems with the production of some commodities and strong demand from speculators are the main factors buoying raw materials prices, allowing the major indexes to hit new peaks in the last few days (Graph 1).

Graph 1 – Another increase in commodity price indexes



\* Commodity Research Bureau; \*\* Continuous Commodity Index; \*\*\* American International Group.  
Sources: Datastream and Desjardins, Economic Studies

Oil prices, however, have been affected by the deterioration in the economic situation, as concerns about demand growth, especially in the United States, and a surge in inventories

brought the price of a barrel of WTI (West Texas Intermediate) below US\$90. The price of natural gas, on the other hand, has continued to advance, staying on its usual seasonal trend.

Contrary to the other commodities, investors often use precious metals as safe-haven assets. It is therefore no surprise that they are doing well in the current context, especially as monetary authorities' energetic action to rein in the economic slowdown through major injections of liquidity is supporting demand for these metals. Moreover, production stoppages at South Africa's mines gave gold and platinum prices an extra boost.

It is much more surprising to see industrial metals prices hold and even climb when the global economy is losing momentum. This is mainly due to serious production problems, fairly low inventories, and a medium-term outlook that is still positive given infrastructure development in emerging countries, particularly in India and China.

Less affected by the economic situation, the outlook in demand for grain remains positive overall, which has triggered further substantial increases in a context where stocks are very low and supply growth is weak.

**François Dupuis**  
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Economist

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**NOTE TO READERS:** The letters **k**, **M** and **B** are used in texts and tables to refer to thousands, millions and billions respectively.

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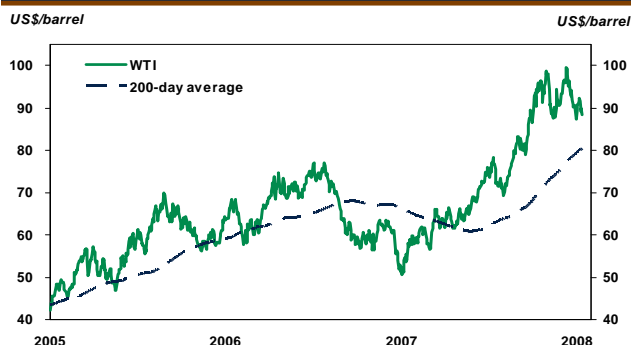
# ENERGY

## The pullback by crude prices could continue

### OIL

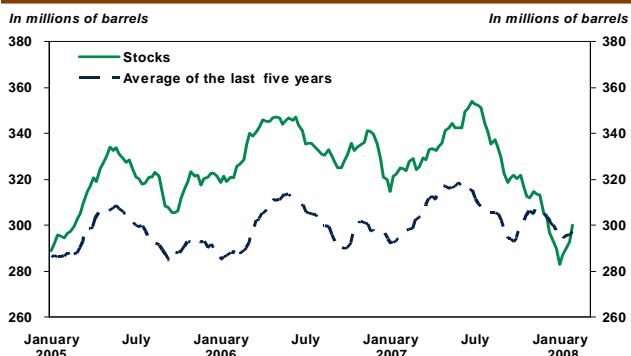
- After briefly reaching US\$100 early this year, the price of oil per barrel has oscillated downward in the last few weeks. It seems increasingly clear that the global economy's slowdown will put the brakes on growth in demand for oil, easing fears of a shortage. Also, geopolitical tensions seem to have eased as U.S. intelligence agencies have concluded that Iran's nuclear program was inactive. Despite some passing surges, the price per barrel thus dropped back below US\$90 at the beginning of the month (Graph 2).
- The recent decline by oil prices convinced OPEC (the Organization of Petroleum Exporting Countries) to keep production steady at its meeting on February 1. OPEC welcomed the moderation in oil prices, but is trying to stave off a precipitous tumble by prices akin to the one that occurred at the end of 2006. It appears that OPEC will look at all the options at its next meeting on March 5. The evolution in prices and oil inventories, as well as the outlook for global growth will have a major influence on its decision to increase, maintain or cut quotas.
- After posting eight straight weekly declines at the end of 2007, U.S. crude oil inventories have shot up since the year began to return to almost normal levels (Graph 3). The risks of a shortage in the United States in the near future are minimal, as U.S. gas inventories are very elevated.
- Globally, the latest data still attest to a market that is still tight, with declining inventories, but, as is occurring in the United States, some easing in demand is likely in early 2008.
- The oil futures curve flattened further in the last few weeks, as the drop in the current WTI price was stronger than in longer-term prices (Graph 4). It thus seems that investors believe oil prices could stay high over the medium term, close to US\$90. This outlook is based on the assumption that Asian nations will continue to see sharp increases in oil consumption over the coming quarters.

Graph 2 – Price of oil per barrel



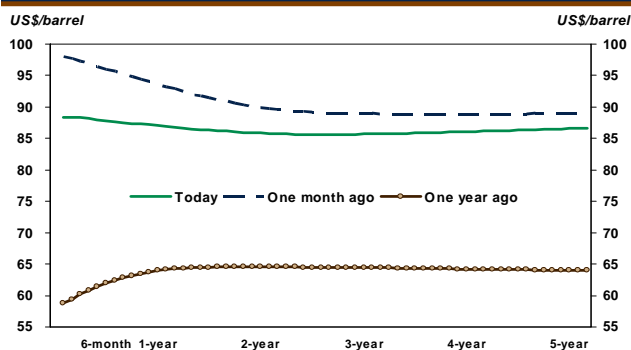
Sources: Datastream and Desjardins, Economic Studies

Graph 3 – U.S. crude inventories



Sources: Energy Information Administration and Desjardins, Economic Studies

Graph 4 – Oil futures



Sources: Bloomberg and Desjardins, Economic Studies

## NATURAL GAS

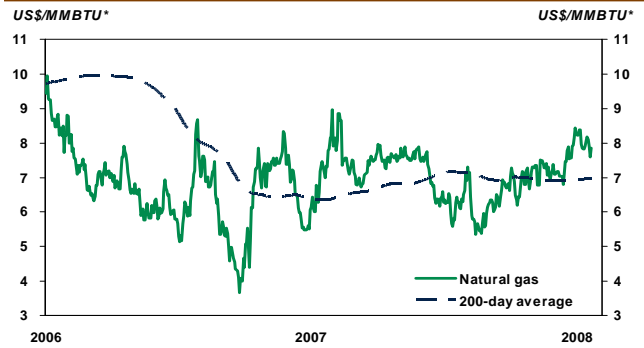
- The price of natural gas was very volatile in January, going from US\$7.50 per MMBTU (Million British Thermal Unit) early in the month to close to US\$8.50 in mid-January, then dropping just below US\$8.00 in the last few days (Graph 5). These big price fluctuations mainly reflect the changing weather in the United States, and the impacts of the weather on gas inventories. Despite a record plunge in the last week of January, U.S. inventories are still 3.9% higher than the average for the five previous years.
- Beyond substantial weekly variations, the price of natural gas has been on the rise overall for several months now, in line with the usual seasonal trend (Graph 6). Seasonal effects will become increasingly negative for gas prices in the next few months, however, especially as of April when the injection period normally begins.
- After having evolved downward since 2001, U.S. natural gas production began to grow again in 2007, and this trend should continue this year as major projects have come on line in the last few months. The increase in output will help keep the U.S. market well supplied, restricting natural gas' short-term appreciation potential. In exchange, it would be surprising to see liquid gas imports increase as sharply as in 2007 as higher international prices and greater demand from other countries will reduce the U.S. market's allure for gas exporters.

## URANIUM

- After having stabilized at close to US\$90 a pound at the end of 2007, the price of uranium has come back to US\$75/pound in the last few days (Graph 7). Recent news are not favourable, as immediate demand remains disappointing and the supply is being inflated by a jump by production in Australia and Kazakhstan, and by an agreement that will allow U.S. firms to buy Russian uranium as of 2011.

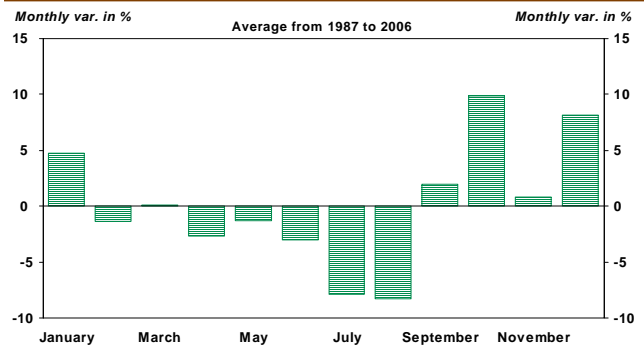
**Forecasts:** Our forecasts for energy prices hold overall. The price of oil per barrel should continue to retreat toward US\$80 in the first half of 2008, then return to a rising trend after that. In keeping with its usual seasonal trend, the price of natural gas will retreat as of the spring and even before that if temperatures turn out to be relatively warm until winter ends in the United States.

Graph 5 – Natural gas prices



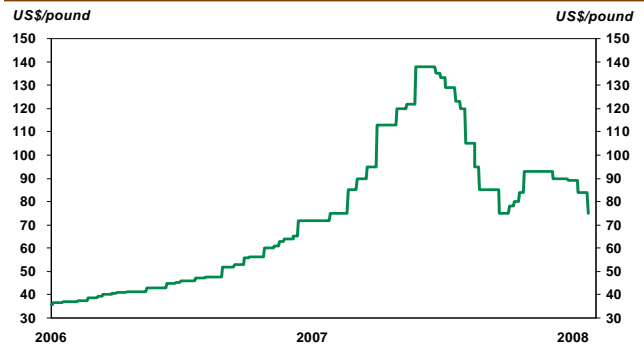
\* Million British Thermal Unit.  
Sources: Datastream and Desjardins, Economic Studies

Graph 6 – Seasonal effects on natural gas prices



Sources: Consensus Economics and Desjardins, Economic Studies

Graph 7 – Uranium prices



Sources: Datastream and Desjardins, Economic Studies

# BASE METALS

## Will prices stand up to the economic slowdown for long?

After having fallen substantially in the second half of 2007, base metals prices showed surprising resilience in the face of further darkening by the economic situation in the last few weeks. It remains to be seen whether low inventories, strong Chinese demand, and production problems will be enough to help metals prices remain impervious to slowing global economic demand for a while.

### ALUMINIUM

- Contrary to the downward trend seen in the last few months, the price of aluminium jumped by over \$300 a tonne in the last few days, reaching US\$2676/tonne (Graph 8). The increase is mainly due to production problems in China, the world's biggest aluminium producer. China is having a very harsh winter and major power outages are promising further production losses at Chinese smelters. As a result, the aluminium surplus forecast for 2008 could be smaller than previously expected.
- Despite Chinese producers' problems, it would be surprising to see aluminium prices pick up as inventories continued to expand and are enough to meet demand. Also, the U.S. housing sector's slowdown has accelerated again (Graph 9); this, combined with global economic growth that has been revised downward, will limit demand for aluminium. In exchange, high production costs, especially for electricity, will limit the potential for this metal's price to decline.

### COPPER

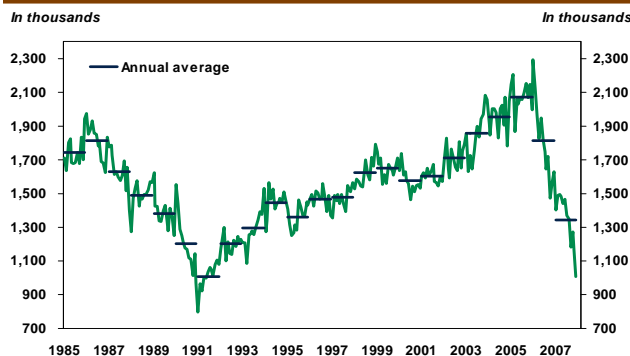
- China's harsh winter and power supply problems in China and Africa, where other countries are dependent on the electricity produced by South Africa, have also put the brakes on copper production in the last few weeks, although the impact is not as big as with aluminium. These production problems, combined with a decline by already very low copper inventories, have allowed the metal's price to advance somewhat in the last few weeks (Graph 10). However, the economic slowdown is continuing to influence the price of copper, and could well take it back below US\$7,000/tonne soon.

Graph 8 – Aluminium prices and inventories



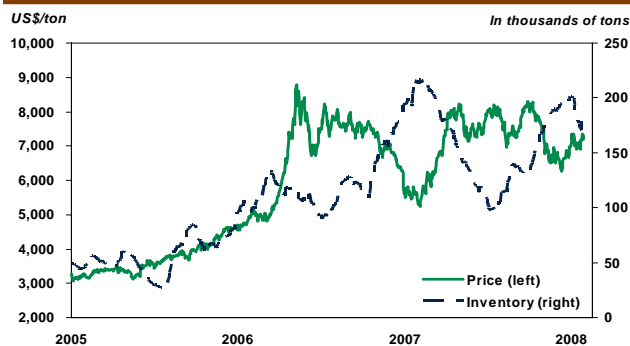
Sources: Datastream and Desjardins, Economic Studies

Graph 9 – U.S. housing starts



Sources: Census Bureau and Desjardins, Economic Studies

Graph 10 – Copper prices and inventories



Sources: Datastream and Desjardins, Economic Studies

## NICKEL

- As expected, nickel's climb to just under US\$30,000/tonne early in the year did not last and the price has come back to the neighbourhood of US\$27,000/tonne in the last few weeks (Graph 11). Despite some recent stabilization, nickel inventories are very high and further declines in China's stainless steel production do not augur any imminent recovery by demand for nickel. On the other hand, China's power problems are also limiting nickel production there. Over the medium term, some recovery by demand for stainless steel seems probable, but rapid growth by global nickel output should limit price growth.

## ZINC

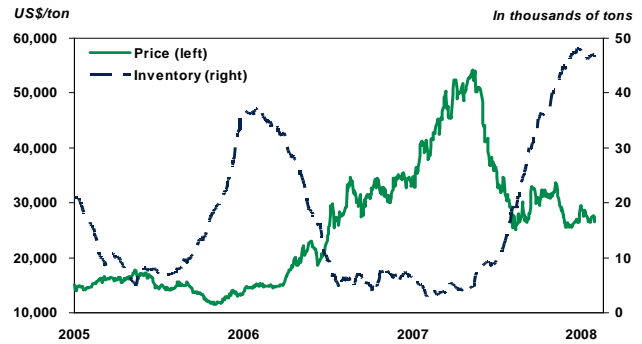
- The price of zinc has been fairly stable since the year began, generally staying below US\$2,500/tonne (Graph 12). It could be hard to stay at this level as the expected increase in inventories has now begun and should continue for the next two years, as a substantial surge in zinc output will result in a major surplus of this metal.

## TIN AND LEAD

- Tin's price has continued to show major resilience and even came close to US\$17,000/tonne lately (Graph 13), when inventories fell somewhat. The problems facing Indonesian producers and a drop in Chinese exports could support prices and keep the tin market in a slight deficit situation this year, despite soft demand growth.
- Lead has climbed back over US\$2,700 a tonne in the last few days. Strong demand from Asian countries is continuing to support lead's price, with some problems still limiting production. Global growth by lead output should accelerate this year, however, which would put the metal back into a slight surplus situation after the deficit recorded last year.

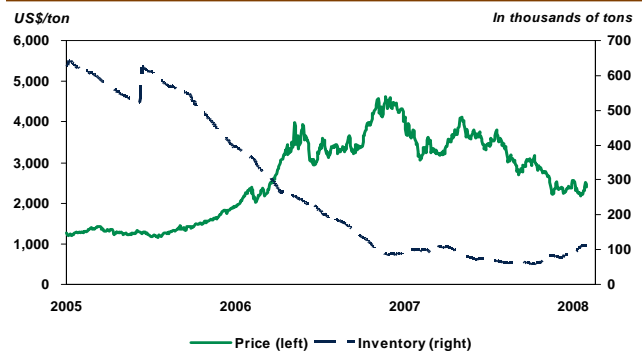
**Forecasts:** We continue to expect the global economic slowdown to cause prices for industrial metals to go down. However, the decline will be small as long as Asia's economies, especially China's, are not contaminated by the U.S. economy's difficulties.

Graph 11 – Nickel prices and inventories



Sources: Datastream and Desjardins, Economic Studies

Graph 12 – Zinc prices and inventories



Sources: Datastream and Desjardins, Economic Studies

Graph 13 – Tin and lead prices



Sources: Datastream and Desjardins, Economic Studies

# PRECIOUS METALS

## More new records

The tough economic and financial context continues to favour precious metals prices. Gold and platinum capitalized on the problems in South Africa's mines to reach new peaks.

### GOLD AND SILVER

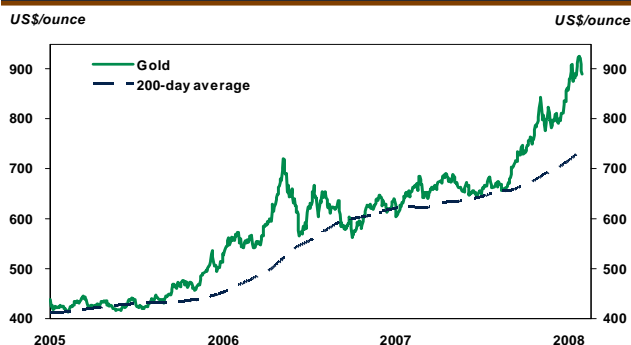
- The stock market problems, growing likelihood of an U.S. recession, and substantial monetary easing from the U.S. Federal Reserve have continued to prod investors to turn to gold. Combined with production stoppages owing to power supply problems at major South African mines, this climate pushed the price of gold over US\$925/ounce at the end of January (Graph 14). The news of renewed output at some mines, a rising U.S. dollar and technical factors, however, took the price of gold back toward US\$900/ounce in the last few days. Gold's price will continue to be highly dependent on investor demand, as everything indicates that high prices will lead to new declines by demand for jewellery.
- The price of silver got a boost from the surge by gold prices, temporarily rising above \$17/ounce in early February (Graph 15). The strong surge in mining output this year will, however, lead to substantial silver surpluses, putting downward pressure on silver prices.

### PLATINUM AND PALLADIUM

- The power supply problems in South Africa, where almost 80% of the world's platinum is produced, will help to deepen the global platinum deficit in 2008. Combined with the favourable precious metals context, this put the price of platinum at a record peak of over US\$1,800/ounce (Graph 16). Although the global palladium market is seeing major surpluses, the metal's price capitalized on platinum's surge to jump to over US\$400/ounce.

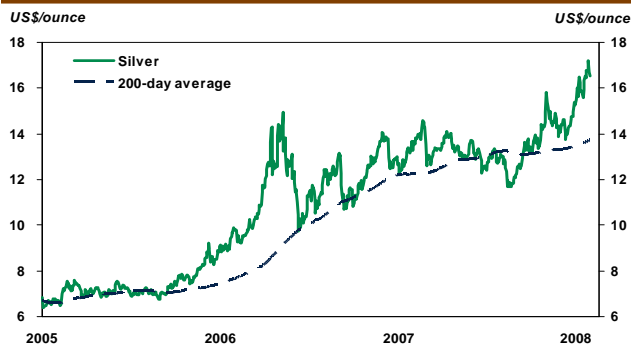
**Forecasts:** Strong demand from investors looking for safe-haven assets will continue to buoy precious metal prices in the first half of 2008, especially as monetary authorities will lower their key rates again to support economic growth. The major financial demand, however, exposes gold to a decline by prices at year's end or next year, when the economic situation improves.

Graph 14 – Gold prices



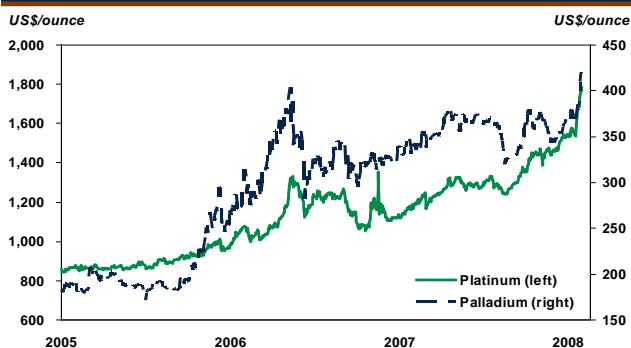
Sources: Datastream and Desjardins, Economic Studies

Graph 15 – Silver prices



Sources: Datastream and Desjardins, Economic Studies

Graph 16 – Platinum and palladium prices



Sources: Datastream and Desjardins, Economic Studies

# AGRICULTURAL COMMODITIES

## Grain prices continue to rise

Overall, grain prices continued to advance in the last few weeks, with low stocks and an encouraging outlook for growth in demand for corn and soybeans is prompting numerous investors to bet on further appreciation.

### WHEAT

- The disappointing harvests in the last few years and plummeting U.S. inventories are continuing to support wheat prices. The news of a smaller than forecast increase in winter wheat planting and a tumble by Canadian inventories helped the price per bushel go over US\$10.5 (Graph 17). Unlike the other grains, wheat is not benefiting from an increase in consumption, while global demand should fall off a little more this year.

### CORN

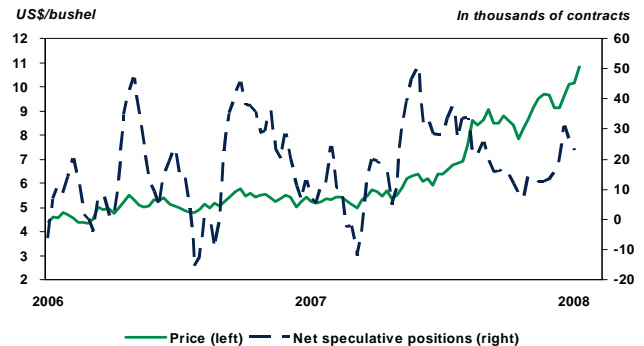
- The surge by corn prices continued in the last few weeks, allowing the price per bushel to go near US\$5 (Graph 18). The U.S. Department of Agriculture (USDA) has revised its projections and it now seems that, despite the major surge in production during the last harvest, global corn stocks are still declining. This shows how strong demand for this product is thanks to such things as increased ethanol production.

### SOYBEAN

- Soybean price has continued to set new records, surging over US\$12.50 a bushel in the last few days (Graph 19). The drop in global production (as American farmers have opted to shift to corn) has reduced soybean stocks, while demand continues to grow. In particular, Chinese soybean consumption has grown by an average of 12% a year in the last decade, with a resulting explosion by soybean imports there.

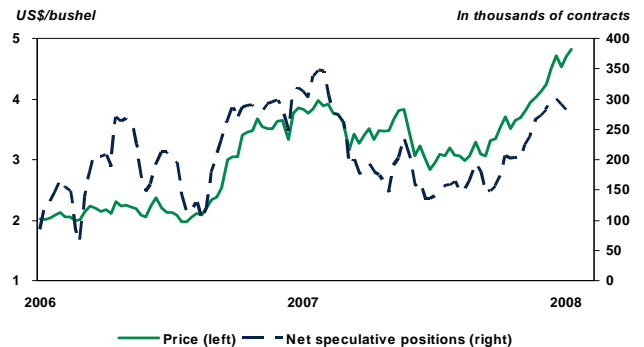
**Forecasts:** The problems that global grain output is having in meeting demand could lead to further price increases this year. The less positive developments by demand for wheat could make this grain underperform this year, unless the weather hits the harvest hard again this year.

Graph 17 – Wheat prices and speculation



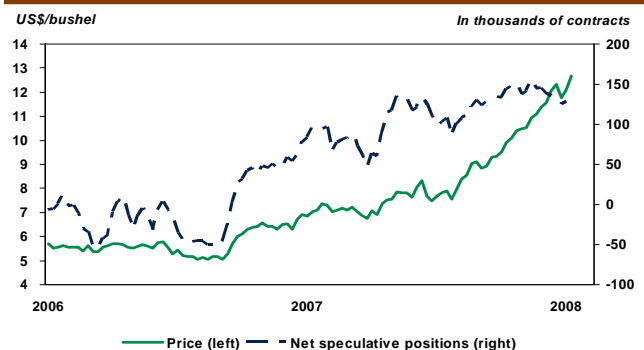
Sources: Datastream, Bloomberg and Desjardins, Economic Studies

Graph 18 – Corn prices and speculation



Sources: Datastream, Bloomberg and Desjardins, Economic Studies

Graph 19 – Soybean prices and speculation



Sources: Datastream, Bloomberg and Desjardins, Economic Studies

### Table 1 Commodities

	Spot price		Previous data			Last 52 weeks		
	Feb-6	-1 month	-3 months	-6 months	-1 year	High	Average	Low
<b>Index</b>								
Reuter-CRB* (CCI**)	506.7	485.0	458.8	419.1	394.0	507.7	430.6	393.0
Reuters/Jefferies CRB*	364.1	366.2	355.6	312.3	301.1	370.2	326.7	298.9
Dow Jones AIG***	190.7	189.8	184.9	167.5	165.5	192.5	174.9	161.1
<b>Energy</b>								
Crude oil (US\$/barrel)	87.1	97.9	94.0	72.1	58.9	99.6	76.1	56.6
Gasoline (US\$/gallon)	3.0	3.1	3.0	2.8	2.2	3.2	2.9	2.2
Natural gas (US\$/MMBTU****)	7.9	7.5	7.2	6.1	9.0	9.0	7.1	5.4
Uranium (US\$/pound)	75.0	90.0	84.0	123.0	75.0	138.0	100.4	75.0
<b>Precious metals</b>								
Gold (US\$/ounce)	904.6	858.0	823.3	671.7	653.1	926.8	723.1	639.6
Silver (US\$/ounce)	16.5	15.3	15.0	13.1	13.7	17.2	13.7	6.4
Platinum (US\$/ounce)	1,813.0	1,545.0	1,472.0	1,294.0	1,186.0	1,813.0	1,351.9	1,165.0
Palladium (US\$/ounce)	417.0	372.0	376.0	364.0	342.0	420.0	359.0	320.0
<b>Base metals</b>								
Aluminium (US\$/ton)	2,591.3	2,446.5	2,580.8	2,607.5	2,814.5	2,920.5	2,603.3	2,316.3
Copper (US\$/ton)	7,180.5	6,990.3	7,469.0	7,790.3	5,355.5	8,300.5	7,263.3	5,225.3
Nickel (US\$/ton)	26,405.0	29,512.5	31,547.5	29,227.5	39,895.0	54,150.0	36,241.4	25,052.5
Zinc (US\$/ton)	2,383.8	2,562.5	2,767.3	3,412.5	3,189.8	4,119.8	3,107.3	2,179.8
Tin (US\$/ton)	16,677.5	16,547.5	16,812.5	16,162.5	11,872.5	17,297.5	15,027.0	11,872.5
Lead (US\$/ton)	2,795.0	2,662.5	3,785.0	3,250.5	1,614.5	3,977.5	2,682.4	1,577.5
<b>Agricultural commodities</b>								
Wheat (US\$/bushel)	10.83	9.50	8.43	6.55	5.19	10.83	7.21	4.97
Corn (US\$/bushel)	4.83	4.38	3.70	3.00	3.76	4.85	3.60	2.82
Soybean (US\$/bushel)	12.67	12.03	9.93	7.67	7.03	12.67	8.73	6.78
CRB* Livestock index	433.7	411.8	425.7	459.6	382.5	468.3	431.8	382.5

\*Commodity Research Bureau; \*\* Continuous Commodity Index; \*\*\* American International Group; \*\*\*\*Million British Thermal Unit.  
Note: Currency table base on previous day closure.

### Table 2 Commodities prices: History and forecasts

	2006	2007	2008 <sup>f</sup>	2009 <sup>f</sup>
Annual average				
WTI* oil (US\$/barrel)	66	72	Target: 80 (range: 76 to 92)	Target: 87 (range: 75 to 95)
Natural gas Henry Hub (US\$/MBTU**)	6.73	6.97	Target: 7.75 (range: 6.75 to 8.50)	Target: 8.50 (range: 7.50 to 9.25)
Gold (US\$/ounce)	604	697	Target: 875 (range: 825 to 950)	Target: 775 (range: 700 to 880)
CRB*** index—base metals	606	868	Target: 850 (range: 800 to 950)	Target: 900 (range: 840 to 1,000)

f: forecasts

\* West Texas Intermediate; \*\* Million British Thermal Unit; \*\*\* Commodity Research Bureau.

Sources: Datastream and Desjardins, Economic Studies