

## Is this the start of a true upswing in prices, or a false start?

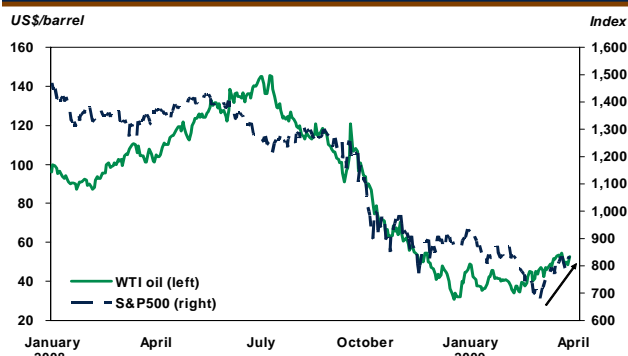
Stabilization of the commodity price indexes has given way to an increase of about 10% since March began. Industrial resources have done especially well, with oil prices going from US\$40/barrel to almost US\$55/barrel, and prices for some base metals up over 20%.

Although, in some cases, the recent increase is based on a few signs of improvement in the balance of supply and demand for raw materials, the price rebound is mainly due to psychological and financial factors. After being depressed for several months, investors have regained some optimism in the last few weeks, which favours risky assets (especially stocks and commodities) (graph 1). Gold's disappointing

performance is a good illustration of the trend reversal that is hurting safe haven securities. Moreover, the decision by several central banks, especially the Federal Reserve, to use quantitative policies (i.e. trying to stimulate the economy by creating an excess supply of money) is creating concerns about currency solidity and swelling commodities' appeal as a store of value.

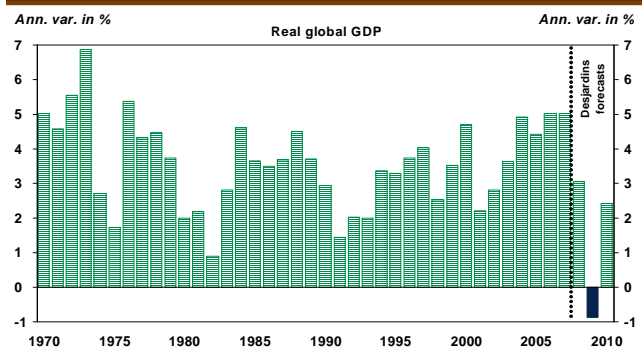
These financial factors could continue to sustain base product prices over the next few months. However, investors' recent optimism seems exaggerated, as the economic outlook is still deteriorating. The global economy should contract in 2009 for the first time since World War II, while 2010 is not promising to be a year of strong growth (graph 2). Demand for commodities will therefore remain very soft for several quarters, which should put new downside pressure on prices.

**Graph 1 – Commodities and the stock markets gained some altitude in the last few weeks**



Sources: Datastream and Desjardins, Economic Studies

**Graph 2 – A first contraction in the global economy**



Sources: International Monetary Funds, Consensus Forecasts and Desjardins, Economic Studies

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# ENERGY

## OPEC's cuts and hopes of seeing the economy stabilizing are supporting crude prices

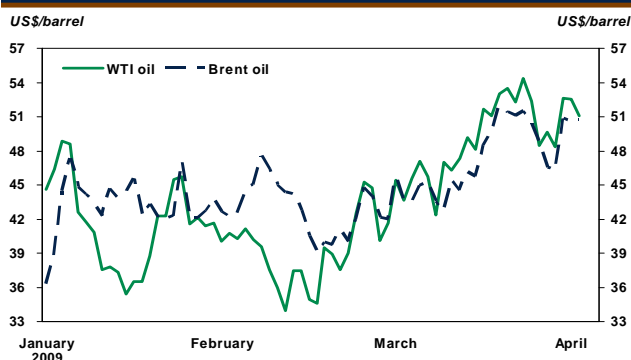
### OIL

- After stabilizing at around US\$40/barrel early this year, oil prices shot up in March, reaching a peak of almost US\$55 that dates back to November 2008. This price surge is based on a number of factors, including a tighter supply, soft U.S. dollar and even some encouraging signs from demand. The recent appreciation put an end to the distortions that had been affecting WTI (West Texas Intermediate) oil. The WTI price has thus returned to just over the Brent oil price (graph 3).
- One very good development for oil prices is how quickly supply has adjusted to the collapse in prices. Members of the Organization of Petroleum Exporting Countries (OPEC), especially Saudi Arabia, have cut their production by about four million barrels a day since last July. The Organization decided not to change its quotas at the March meeting, opting to focus, for now, on even tighter compliance with the limits that have already been set. The OPEC supply cuts should soon get the global oil market back into equilibrium, particularly as production elsewhere in the world remains disappointing. The International Energy Agency (IEA) has cut to zero its forecast for non-OPEC supply growth for 2009. The increase in crude inventories, which had accelerated in the last few months, could come to an end shortly (graph 4).
- Some signs of stabilization or at least a slowing in the decline in U.S. demand for oil products also played a role in the recent rise in crude prices. In particular, in the United States, demand for gas is almost unchanged since the beginning of the year compared with the same time last year. This tends to confirm that the drop in U.S. oil demand will be smaller this year than it was last year.
- Although the United States is the biggest oil consumer, we must not overlook the rest of the world. There, the latest developments are not nearly as good for crude prices. In fact, the global recession is bringing consumption down sharply almost worldwide (graph 5). The latest statistics thus confirm a rapid slide in demand in Europe and Japan.

### GASOLINE

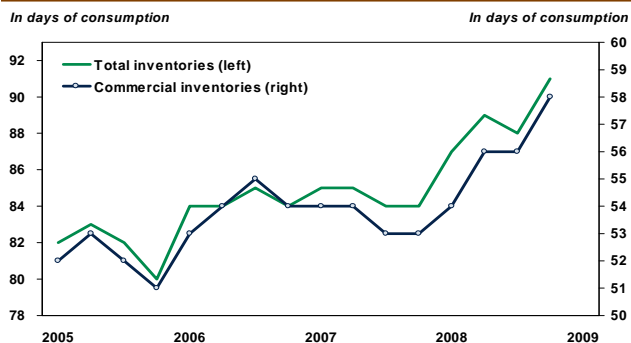
- The up trend in gas prices that began last January was supported by March's surge in crude prices. This allowed prices at the pump in the United States to go back over US\$2 a gallon in the last few days (graph 6). Demand from American drivers has almost stabilized and this, combined with the refineries' fairly limited output, has brought gas inventories down slightly, which is helping fuel prices go up. However, this trend is not yet solidly established, as the latest weekly statistics show inventories going up. In this economic context, another increase in gas prices would be surprising and could make demand decline, as we had seen in the first half of 2008.

Graph 3 – Oil prices come up and distortions wane



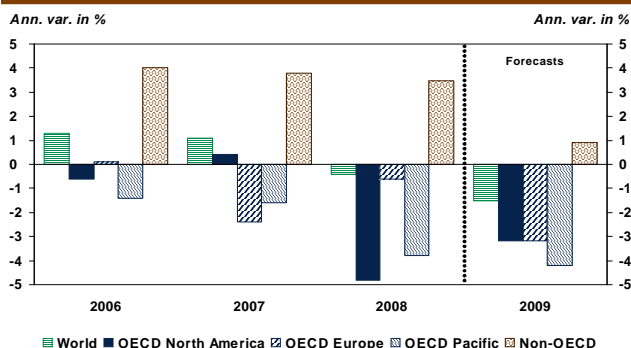
Sources: Datastream and Desjardins, Economic Studies

Graph 4 – The rise in OECD oil inventories could wind down



Sources: International Energy Agency and Desjardins, Economic Studies

Graph 5 – Generalized pullback of oil demand in 2009



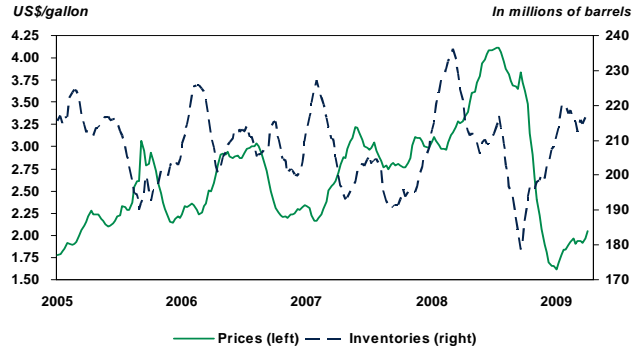
OECD: Organisation for Economic Co-operation and Development  
Sources: International Energy Agency and Desjardins, Economic Studies

**NATURAL GAS**

- Natural gas is still posting one of the worst performances among all commodities. Prices continued to slide quickly in March. They dropped over 10%, taking the price to US\$3.60 per MMBTU (Million British Thermal Unit), a low that dates back to 2002 (graph 7). Since the year began, natural gas is down nearly 35%. Soft demand from the industrial sector and the substantial increase in American output in 2008 could keep gas prices low over the near term. The large supply of liquefied natural gas in the international market is also a drag on prices.
- While natural gas's extremely low price may be justified by the current supply-demand balance and by high inventories, we think that the market is making a mistake in overlooking developments in future supply. Drilling activity is still dropping at an unprecedented pace and everything suggests that U.S. production will begin a down trend as of mid-2009. If the price remains at this level for several months, gas surpluses will quickly disappear, and risks of a shortage could re-emerge as of 2010. The futures curve shows that the market also thinks that this price level cannot be sustained over the medium range (graph 8).

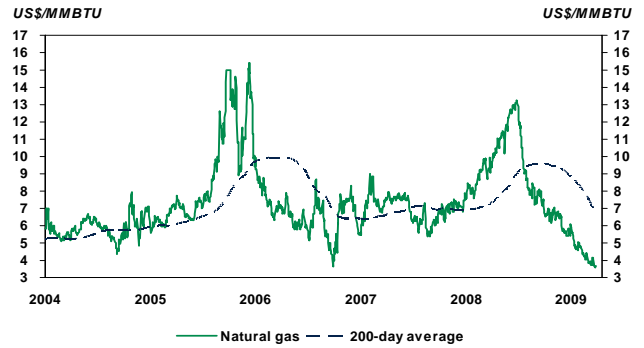
**Forecasts:** Despite the recent rebound in oil prices, we think it is still too early for a true bull trend to start. Our economic scenario calls for the global economy to contract sharply in 2009, followed by a modest recovery in 2010. Demand for oil will therefore remain very low, limiting the rise in prices. However, the cyclical low of US\$30.80/barrel may well not be tested again. Prices could instead fluctuate around US\$45 over the next few months, given the substantial cuts to output by OPEC nations. We thus expect oil to be at an average price of US\$48 a barrel for all of 2009 and US\$65 in 2010. Natural gas prices could remain weak for several more months, given soft demand, but the spectacular tumble in drilling operations promises a big surge over the medium range.

**Graph 6 – Gas prices and inventories**



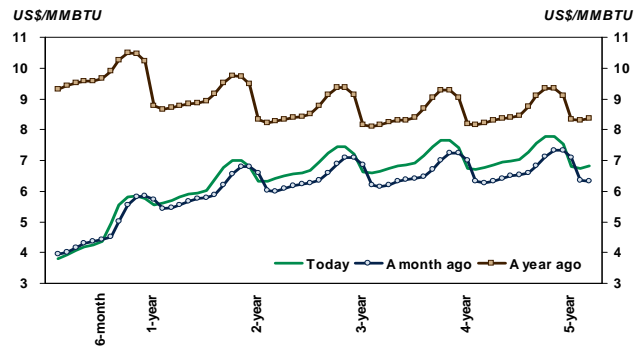
Sources: Energy Information Administration and Desjardins, Economic Studies

**Graph 7 – Natural gas prices**



Sources: Datastream and Desjardins, Economic Studies

**Graph 8 – Natural gas futures**



Sources: Bloomberg and Desjardins, Economic Studies

# BASE METALS

## Will Chinese demand be enough?

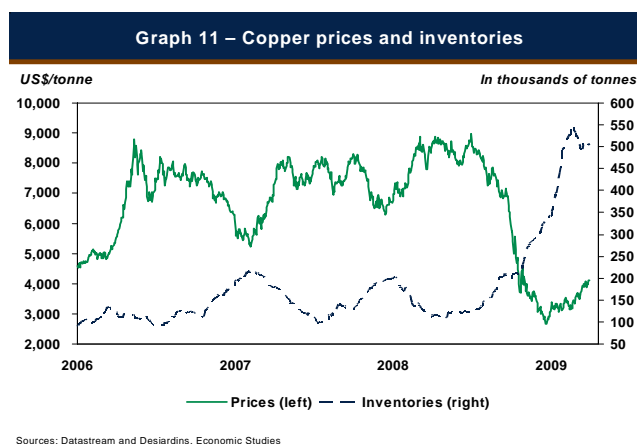
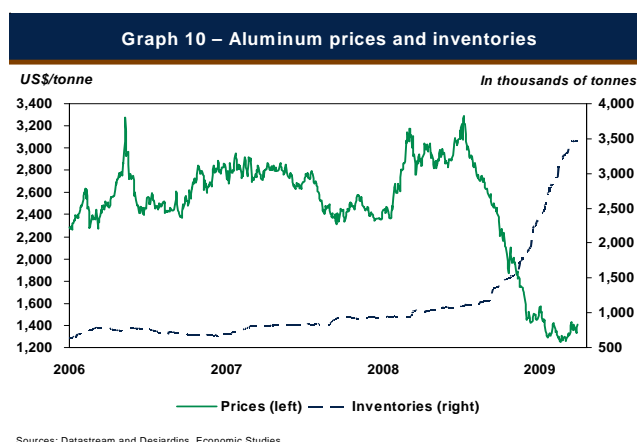
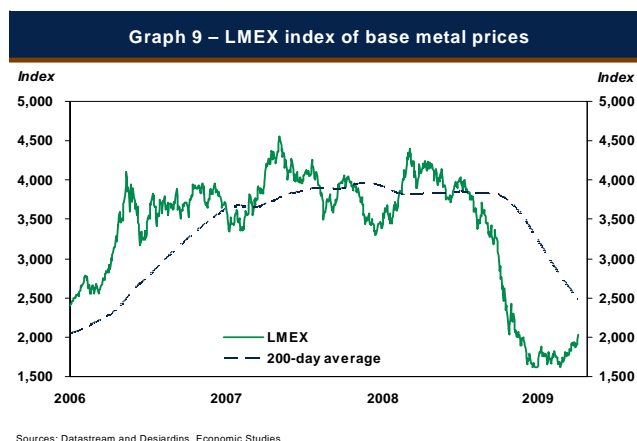
March was a very good month for industrial metals, with the LME (London Metal Exchange Index) advancing by more than 10% (graph 9). This substantial gain is due to strong Chinese demand, a few economic indicators that were better than expected, and to financial factors, especially the greenback's depreciation and renewed investor optimism. However, the LME index rebound obscures some diverging trends in prices for various base metals. Given that the economic environment is very difficult, especially for the construction and automotive sectors, the recent rise seems very fragile.

### ALUMINIUM

- Aluminum is still one of the industrial metals with the most obvious difficulties. Although it edged up in March, aluminum's price is still close to its cyclical low, and below the breakeven points of most smelters. There is still a clear imbalance between global supply and demand, as inventories are mounting rapidly (graph 10). One sizeable problem is that, to date, production cuts by the major international aluminum plants have been more than offset by the increase in Chinese output. The first signs that the American housing market is stabilizing are good news for aluminum, but activity will remain very soft in this sector for several more quarters. The news from the auto industry remains very negative for this metal.

### COPPER

- Copper prices stole the show in March, posting an approximate 20% gain and crossing back over US\$4,000 a tonne. A number of developments helped this metal, but the most important one was certainly February's record for Chinese imports. Purchases by Chinese authorities and the gap between prices in this country and elsewhere in the world are behind the surge in imports that helped bring copper inventories down in mid-March (graph 11). However, it remains to be seen if China will actually use all of this copper, or simply stockpile it, which seems more likely at this point. Copper demand also remains very low worldwide, and inventories have recently edged up, which could put downside pressure on the metal's price. As copper is especially sensitive to financial factors, its price could remain volatile over the next few months as the American dollar and stock markets could keep casting about for a real direction.



## NICKEL

- Soft demand continues to dominate the nickel market, even in China, as there is nothing to augur an increase in stainless steel output at this point. Overall, the metal's price remained below US\$10,000/tonne in March and even fell temporarily below US\$9,500 (graph 12). Production stoppages are still not enough, as inventories continue to rise.

## ZINC

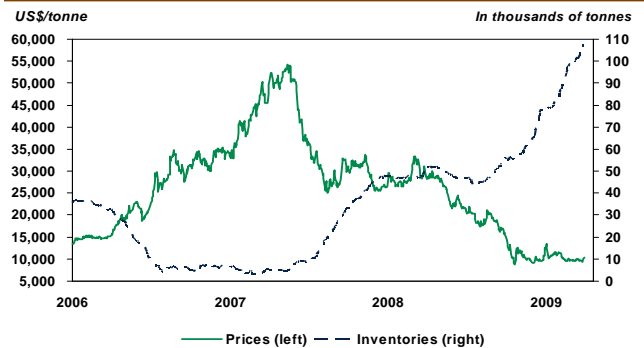
- Like copper, zinc prices benefited extensively from record Chinese imports. After two months, Chinese zinc imports are up 632% from the same time last year. The significant gap between international and Chinese prices goes a long way to explain the huge influx of zinc into China. Extraordinary Chinese demand reined in the rise in inventories and allowed zinc prices to go up 20% in March; prices reached about US\$1,300 a tonne (graph 13).

## TIN AND LEAD

- Tin prices remained low in March, fluctuating between US\$10,000 and US\$11,350 a tonne to end the month less than 5% above the cyclical low set at the end of 2008 (graph 14). Tin inventories continued to rise in March, as soft global demand is still winning out over the limited supply.
- Despite the problems in the global auto industry, lead prices jumped by almost 25% in March, reaching US\$1,270 a tonne, about one third higher than it was at the start of the year. Like copper and zinc, the gain is primarily due to a spectacular surge in Chinese imports and a break in inventory growth in March. Lead prices could remain highly volatile.

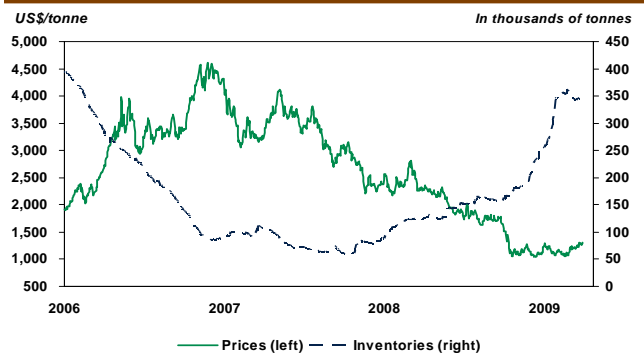
**Forecasts:** Given the weak global economy, base metal product prices will remain very sensitive to signals from China. If recovery plans are implemented quickly and unprecedented metal imports continue, prices could hang onto their recent gains and even appreciate further. However, we have some serious doubts about the Chinese economy's soundness; instead, we think that this recent «demand» primarily represents restocking and arbitrage that, by supporting Chinese producers, could expand the surplus in the global base metals market. In our opinion, the metals that shot up in March could have their gains erased in the next few months; overall, prices should stay close to their cyclical lows until the end of the year.

Graph 12 – Nickel prices and inventories



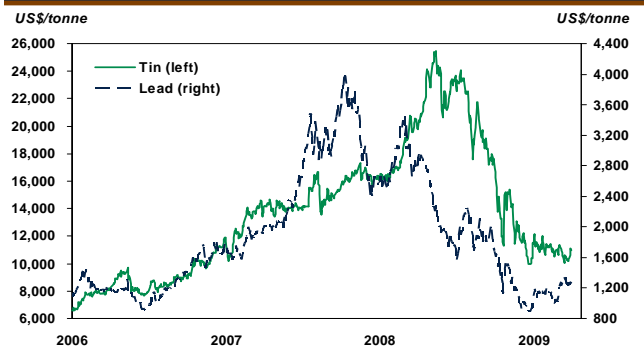
Sources: Datastream and Desjardins, Economic Studies

Graph 13 – Zinc prices and inventories



Sources: Datastream and Desjardins, Economic Studies

Graph 14 – Tin and lead prices



Sources: Datastream and Desjardins, Economic Studies

# PRECIOUS METALS

## Gold's price is casting about for a direction

A number of contradictory trends led to substantial fluctuations in precious metal prices in the last few weeks. Extreme risk aversion, which had boosted prices for safe haven securities early in the year, eased in March, taking precious metal prices down. The central banks' increasingly bold quantitative policies are giving the metals' prices some support, however.

### GOLD AND SILVER

- Speculative demand for gold continued to rise in February, even driving its price over US\$1,000 an ounce during trading on February 20. Once again, this level could not be sustained and the price quickly fell. The downturn steepened in March, as investors started to turn back to riskier assets, including stock. Gold's price thus fell back below US\$900/ounce (graph 15). The news that the Federal Reserve was instituting a true quantitative policy temporary made gold bounce back over US\$950 on March 19. However, the possibility that the International Monetary Fund (IMF) will sell some of its gold reserves to bolster its income send the price of gold back under US\$900 an ounce. Silver was better able to hang onto its gains (graph 16).

### PLATINUM AND PALLADIUM

- Platinum and palladium prices continued to rise in March. Platinum is now up over 25% since the year began, taking it back over US\$1,100 an ounce, while palladium is up by just over 20% (graph 17). In our opinion, the rise primarily reflects the fact that the correction in the second half of 2008 went too far. The auto industry's problems—with President Obama now considering a bankruptcy for GM or Chrysler—limit these metals' potential for gains over the short term.

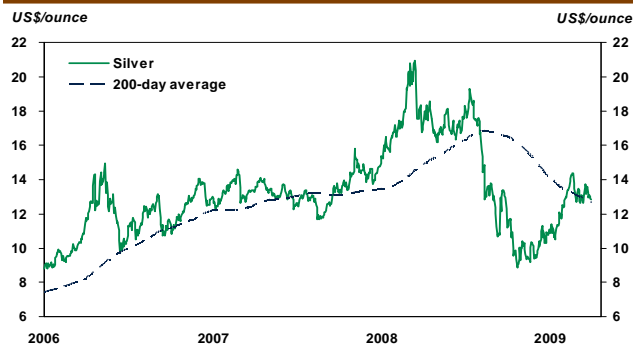
**Forecasts:** Precious metal prices will remain highly volatile for the next few months. This could well allow the price of gold to finally cross its historic record, US\$1,012 an ounce, especially if renewed pessimism drives investors toward safe haven securities. It will be hard to maintain this level all year, and the price of gold should be in the neighbourhood of US\$940 an ounce on average in 2009. Prices for other precious metals, which the industrial sector uses more, will remain well below cyclical peaks.

Graph 15 – Gold prices



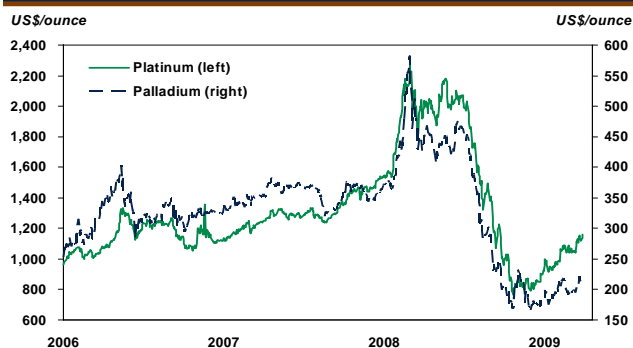
Sources: Datastream and Desjardins, Economic Studies

Graph 16 – Silver prices



Sources: Datastream and Desjardins, Economic Studies

Graph 17 – Platinum and palladium prices



Sources: Datastream and Desjardins, Economic Studies

# AGRICULTURAL COMMODITIES

## The contraction in supply is confirmed

After several weeks of relative calm, the agricultural sector learned of American planting intentions for 2009 at the end of March. The impact of the drop in prices and tightened credit on the cereal supply was confirmed; U.S. farmers plan to reduce the acreages devoted to the three main cereals (wheat, corn and soybeans) by 2.3% (graph 18). The lower-than-forecast seeding intentions made cereal prices rise (graph 19).

### WHEAT

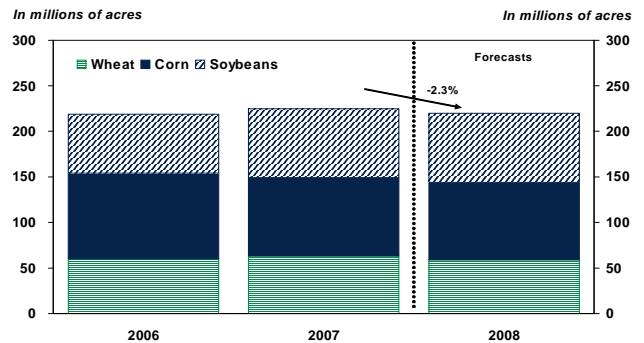
- The forecast 7% decline in wheat acreage in the United States in 2009 allowed the cereal's price to climb above US\$6.00 a bushel. However, we must not forget that this decline in planting follows on a record wheat harvest that helped to substantially replenish stocks (graph 20). Overall, the worldwide wheat market seems to be relatively balanced, which should allow the price to stay close to current levels or appreciate slightly in the next few months.

### CORN AND SOYBEANS

- The price of corn has stayed below US\$4.00 a bushel since the year began. The drop of just 1.2% in corn planting intentions is slightly less than had been forecast: it is thus not good news for this cereal's price. The recent rise in gas prices, however, appears to be enough to get ethanol production back in gear and thus support corn demand. The price of soybeans held around US\$9.00 a bushel over the last few weeks. Despite its lower fertilizer intensiveness and relatively sustained demand, especially in China, U.S. farmers decided to increase the crop area dedicated to soybeans by just 0.4%, compared with a forecast increase of about 6%. Soybean stocks could thus continue to pull back, which could soon drive prices higher than US\$10 a bushel.

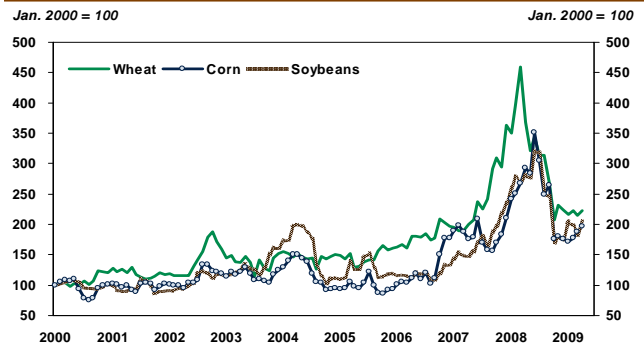
**Forecasts:** The drop in planting intentions confirms the cereal supply's response to the substantial price declines. The potential for further price declines therefore appears limited; we are instead expecting prices to climb gradually in the next few quarters. Now that the planting intentions are out, the factor to watch is the weather, which could have a substantial impact on agricultural output and prices.

Graph 18 – Planted acreages in the United States



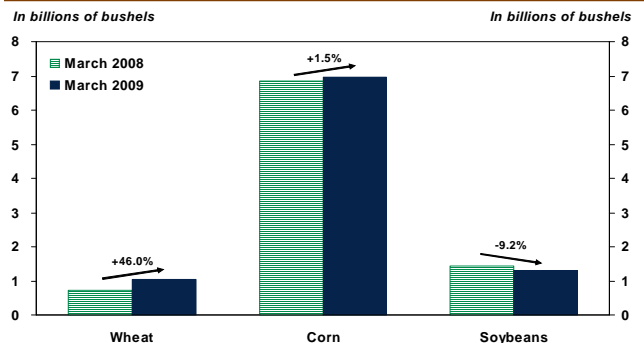
Sources: U.S. Department of Agriculture and Desjardins, Economic Studies

Graph 19 – Is the low point for cereal prices behind us?



Sources: Datastream and Desjardins, Economic Studies

Graph 20 – U.S. cereal stocks



Sources: U.S. Department of Agriculture and Desjardins, Economic Studies

### Table 1 Commodities

	Spot price	Percentage return since				Last 52 weeks		
	Apr. 6	1 month	3 months	6 months	1 year	High	Average	Low
<b>Index</b>								
Reuter-CRB* (CCI**)	371.9	5.8	-2.7	-10.0	-29.5	614.6	448.9	323.2
Reuters/Jefferies CRB*	224.5	7.1	-7.5	-27.5	-43.2	473.5	322.1	200.3
Dow Jones AIG***	111.8	5.6	-9.4	-25.9	-45.4	238.0	161.4	102.0
<b>Energy</b>								
Crude oil (US\$/barrel)	51.1	12.1	5.1	-41.9	-50.8	145.7	85.3	30.8
Gasoline (US\$/gallon)	2.04	5.3	21.0	-41.5	-38.1	4.11	2.94	1.61
Natural gas (US\$/MMBTU****)	3.74	-5.4	-38.7	-45.8	-60.2	13.27	7.77	3.58
<b>Precious metals</b>								
Gold (US\$/ounce)	870.4	-7.7	2.9	0.8	-3.9	995.2	868.0	710.8
Silver (US\$/ounce)	12.4	-7.8	14.4	9.9	-28.9	19.3	13.7	8.9
Platinum (US\$/ounce)	1,150.0	7.4	20.4	17.0	-42.2	2,182.0	1,354.2	763.0
Palladium (US\$/ounce)	224.0	10.6	21.1	13.1	-48.9	475.0	288.3	164.0
<b>Base metals</b>								
Aluminium (US\$/ton)	1,447.5	12.0	-7.7	-34.4	-49.1	3,291.3	2,211.4	1,253.3
Copper (US\$/ton)	4,330.3	17.3	30.0	-24.1	-49.9	8,982.5	5,819.0	2,667.5
Nickel (US\$/ton)	10,775.0	10.2	-19.7	-25.2	-62.5	30,000.0	16,280.4	8,807.5
Zinc (US\$/ton)	1,340.5	9.5	4.7	-11.8	-41.2	2,362.3	1,550.1	1,041.0
Tin (US\$/ton)	11,062.5	-2.5	-9.0	-33.6	-44.5	25,497.5	16,701.1	9,950.0
Lead (US\$/ton)	1,311.5	10.4	12.8	-18.7	-54.9	2,952.5	1,637.6	877.5
<b>Agricultural commodities</b>								
Wheat (US\$/bushel)	6.30	5.1	-9.7	3.2	-41.6	10.78	7.35	4.87
Corn (US\$/bushel)	3.84	12.1	-3.5	3.1	-31.9	7.11	4.55	2.72
Soybean (US\$/bushel)	9.85	14.1	-0.8	15.1	-19.1	16.19	11.05	7.60
CRB* Livestock index	311.4	3.0	-2.5	-33.4	-32.5	565.8	421.7	267.1

\*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

	2007	2008	2009f	2010f
Annual average				
WTI* oil (US\$/barrel)	72	99	Target: 48 (range: 40 to 60)	Target: 65 (range: 50 to 80)
Natural gas Henry Hub (US\$/MMBTU**)	6.97	8.84	Target: 5.00 (range: 4.00 to 6.00)	Target: 6.50 (range: 5.00 to 8.00)
Gold (US\$/ounce)	697	872	Target: 940 (range: 875 to 1,000)	Target: 1,000 (range: 850 to 1,100)
LMEX*** index—base metals	3,847	3,377	Target: 1,900 (range: 1,500 to 2,300)	Target: 2,300 (range: 1,750 to 3,500)

f: forecasts; \* West Texas Intermediate; \*\* Million British Thermal Unit; \*\*\* London Metal Exchange Index.  
Sources: Datastream and Desjardins, Economic Studies