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COMMODITIES UPDATE

REP-019
MARKET VISTA

Reeling from global economic fragility

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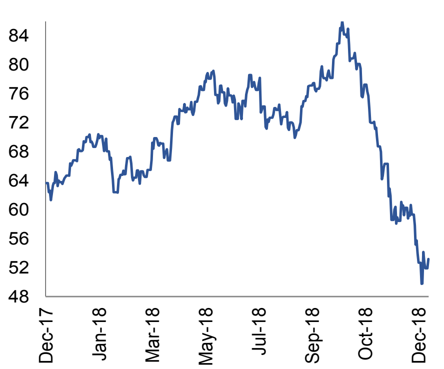
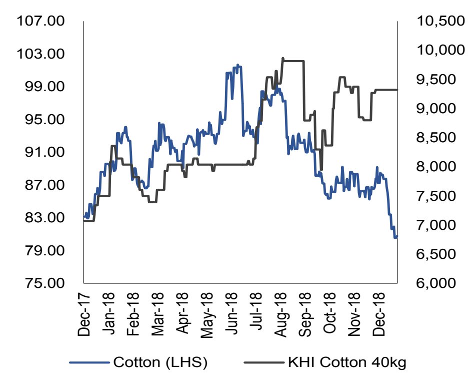
- **Global industrial activity indicators, particularly PMI reads from China, USA and the EU, and consumer confidence slippages indicate a fragile end to CY18, laying the groundwork for CY19 to be a volatile year for global commodity markets, reflected in the TRJ Commodity index sliding 6.6%MoM for Dec'18.**
- **On a broad note, fuel and energy-linked commodities witnessed weakness (Arab Light/International Urea Prices down ~11/12%MoM) during Dec'18, as most other Hard (CRC/HRC Steel price -5.6/3.5%MoM) and Soft (Cotton/FAO dairy/FAO sugar indices moved -6/-3/-2%MoM) commodity classes were unchanged or exhibited muted moves**
- **Lower global oil prices endows room for enhanced global commodity consumption, while subduing expectation surrounding aggressive monetary tightening as inflationary pressures subside, all the showcasing implications on global commodity prices from possible US$ weakness**
- **Political uncertainty coupled with a shift to populist policies (EU, US) and erosion in global rule-making/enforcement bodies, remain major stressors for international commodity markets. The limited and unstable nature of commodity prices offer the GoP a window to enact impactful policy actions (circular debt clearance, oil pricing, gas reforms, additional RLNG arrangements) addressing structural deficiencies, a long time in the making.**

Brent (US$/bbl)



Cotton Price (Usc/lb)



Source: KCA, Bloomberg & AKD Research

Impending developments could support Crude prices: Arab Light/Brent prices averaged US$58.82/56.48/bbl moving -10.5/-9.0%MoM, where sustained weakness was largely a repercussion of possible warning signs emerging in slower than expected global macro-data points. These included weak PMI data from China (below no-growth mark), US (Dec PMI slowed the most since Oct'08) and the EU coupled, fueling fears of depressed demand throughout 2019. On the back of weak expecations, major OPEC suppliers have asserted their willingness to cut supply further from levels agreed in Dec'18 meeting (1.2mn bps between OPEC and NOPEC members). That said, near term upsides could arise from US stating their unwillingness to extend waivers for Iranian oil exports (after re-imposition of sanctions) and successful outcome from ongoing US-China trade negotiations.

Cotton price stability inherently unstable: International cotton prices witnessed a mixed trend in Dec'18 with prices touching a peak of USc89.2/lbs (+3.1% vs. Nov'18), before falling 9.4% (Dec'18 end: USc80.8/lbs) there-on. The prices surged on concerns over drought in Northern

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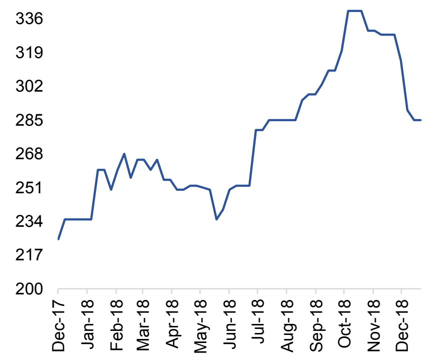
India (Gujrat received 40% less rainfall vs. long term avg.). However, the spike was short-lived as sluggish demand particularly from China triggered build-up in inventories, prompting cuts. Locally prices remained stable at PkR9324/40kg where most of the mills remained on the sidelines with buying activity restricted to stock replenishment. International Cotton Advisory Committee (ICAC) forecasts cotton prices to trend upwards in 2019 directly related to the fall in production and growth of demand, which would cause a contraction in worldwide stocks.

Urea Middle East Granular (US$/MT)

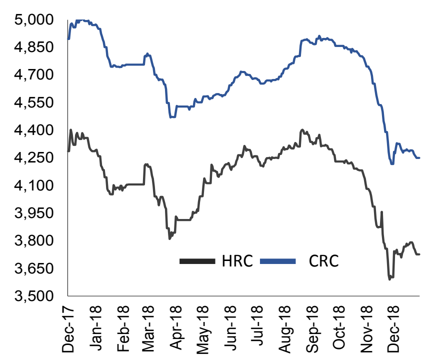


Source: Bloomberg & AKD Research

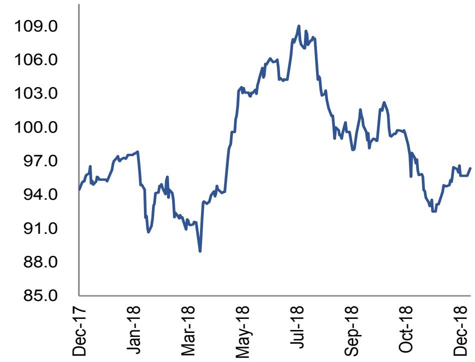
Oversupply keeps Urea lower: Urea prices trended lower in Dec'18 avg. at US$286.6/MT vs. US$325.8/t in Nov'18 due to lackluster international demand. Domestic prices observed an opposite trend (+4.0%MoM) where the manufacturers benefitted from the peak demand season. International urea prices are likely to recover in the short run driven by declining Chinese exports and increasing import demand from the U.S., Europe and Turkey. India is expected to announce another tender in early 2019, though the requirement this time could be much smaller than last (Last tender 750kT). On the domestic front, future price trend is dependent on the Government's decision on GIDC where any cut in this regard would potentially have direct impact on urea prices.

China's import policy to dictate coal prices in CY19: The benchmark Richard's Bay Spot price averaged US$95.4/mt for Dec'18 up 0.8%MoM. Overall, Richards bay average at US$98.5/mt in CY18, highest in last seven years, as Chinese imports were recorder at a four year high of 281.5mn tons. Moving forward, the demand is expected to slow down as China tightens the restrictions on cement and steel industry in a bid to counter high pollution levels during winters. On the flip side, the increased demand amid re-stocking ahead of Chinese New Year can support demand. While in the long run, Chinese govt. has asked its utilities to keep the imports below 2018 level amid abundant local supplies and lower electricity demand growth.

Steel price (CNY/MT)



COAL Price (US$/MT)

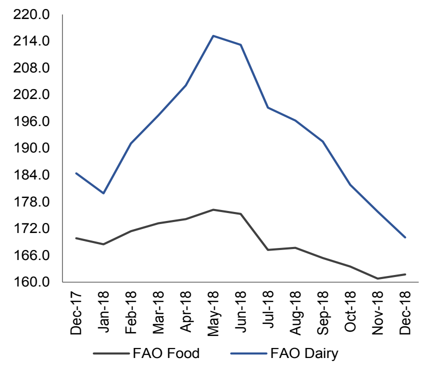


Source: Bloomberg & AKD Research

Steel – soft demand weighing on prices: Steel prices continued their decline in Dec'18 where Rebar/Billet prices declined by 9.8/6.1%MoM while CRC/HRC witnessed a decrease of 5.6/3.5% MoM amid soft demand. Looking ahead, winter restrictions on steel plants will provide support to prices, in our opinion, as Govt. has asked to cut the production levels by at least 30% after 'orange' level smog alert was issued in at least nine cities in China's industrial hub of Hebei, Shandong, Henan and Shanxi. While a recent statement by China's state minister stating that China will strictly prohibit the expansion of steel plants along with the increase in funding for infrastructure projects by Chinese govt. can potentially provide further boost to the prices.

Food prices continue heading down: FAO food index remained tepid, averaging 161.7pts vs. 161.6pts in Nov'18, taking CY18 average to 168.4pts (-3.6%YoY). This weakness was directly imposed through sliding in sugar, vegetable oil, meat and dairy prices sub-indices throughout CY18. Sugar prices were particularly pressured as production from India and slowing demand from ethanol producing countries (as oil prices slide) led to a global glut. Increased export supplies was the major culprit inhibiting Dairy prices as well.

FAO Index



Source: FOA & AKD Research

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Neutral	**> 13% to < 19% expected total return**
Sell	**< 13% expected total return (Rf: 13%)**

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Buy	**> 20% upside potential**
Accumulate	**> 5% to < 20% upside potential**
Neutral	**< 5% to > -5% potential**
Reduce	**< -5% to > -20% downside potential**
Sell	**< -20% downside potential**
Not Rated	**No investment opinion or recommendation**

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- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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