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Focus Commodity

Commodities: trade wars escalate

In May, optimism quickly faded as U.S.-China trade talks abruptly stopped and the threat of more tariffs became a reality. Moreover, trade tensions heightened also between the U.S. and other important trade partners, like Mexico and the European Union. We now envisage a gloomier baseline scenario for commodity prices, as we rule out any short-term improvement in the U.S.-China trade dispute and expect that trade tensions will become a structural market feature.

Crude oil: frequent swings in market sentiment

Over the next months, the markets will probably continue to focus their attention alternatively from concerns about escalating trade tensions to fears for supply disruptions. In our opinion, physical markets' fundamentals and geopolitical risks may prevail over global macroeconomic and political concerns. In our baseline scenario, OPEC will not break and therefore the current output cuts implemented by OPEC+ will continue.

Precious metals: gold benefits from rising uncertainties

The global outlook is turning positive for gold: monetary policies are becoming more accommodative and low interest rates in the main economies are reducing the opportunity cost of holding precious metals and improving the risk/return profile of gold investments. Moreover, political and geopolitical tensions will probably remain high. This context should favour gold through investors' demand for safe havens and Central banks' quest for diversification.

Industrial metals: political risks prevail

The key risks weighting on the sector are related to macroeconomic and political factors that could prevail over the good fundamentals. In particular, concerns about weakening global growth and escalations in U.S. and China's trade war are expected to limit the upside potential of industrial metals' prices up in the short and medium term. Longer term, we are very positive on the complex as prices should increase in the next 3-5 years to incentivize investments in mining.

Agricultural commodities: an effective diversification tool

This year, agricultural goods proved their effectiveness as a diversification tool in financial portfolios. In most cases, cereals and softs' performances reflect the underlying supply and demand fundamentals and expectations about weather conditions. Softs' prices, in particular, are in most cases little influenced by concerns related to the U.S.-China trade war and are therefore less vulnerable to the frequent swings of market sentiment between risk-on and risk-off.

June 2019

Quarterly Outlook

Intesa Sanpaolo
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Macroeconomic and
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Prepared on the basis of the information available as at 19.06.2019 (except otherwise indicated)

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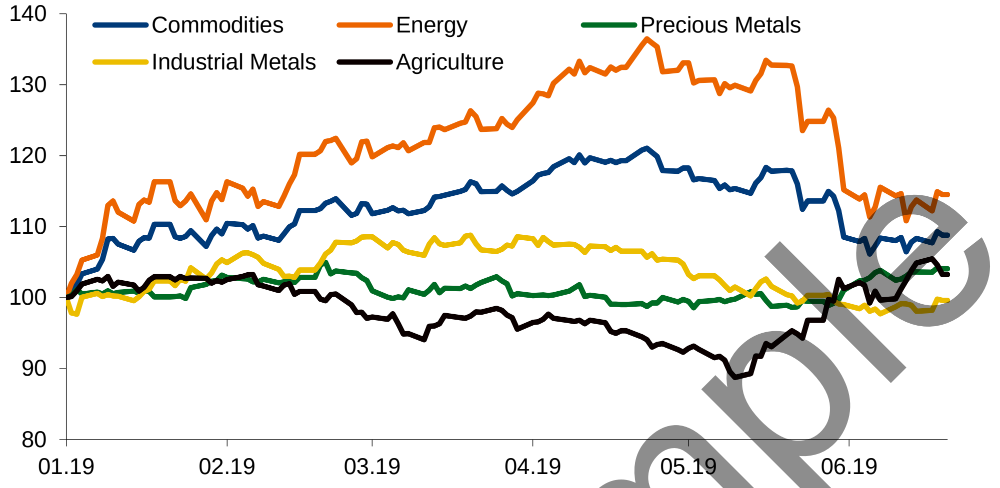
In May, optimism quickly faded as U.S.-China trade talks abruptly stopped and the threat of more tariffs became a reality. Moreover, trade tensions heightened also between the U.S. and other important trade partners, like Mexico and the European Union. We now envisage a gloomier baseline scenario for commodity prices, as we rule out any short-term improvement in the U.S.-China trade dispute and expect that trade tensions will become a structural market feature.

Year-to-date performance of commodity indices



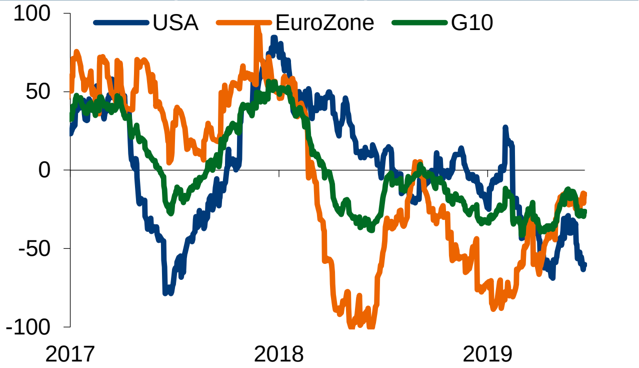
Source: Intesa Sanpaolo chart from Bloomberg data

Commodities benefited from a bright 1Q: concerns about the U.S.-China trade war were easing, with all the parties expressing optimism about progresses in high-level talks; central banks reassured the global markets that liquidity would remain abundant; most commodities benefited from tightening physical markets due to a mix of structural and exogenous factors. For instance, industrial metals' prices have been supported by the very low level of investments in productive capacity implemented over the past years, a structural market feature. Crude oil prices have been mainly sustained by exogenous events: output cuts implemented by OPEC+ and Canada; U.S. sanctions against Venezuela and Iran; clashes in Libya.

Then, the positive price trend came to a halt **in the 2Q**, when **optimism quickly faded as U.S.-China trade talks abruptly stopped and the threat of more tariffs became a reality**. Moreover, trade tensions heightened also between the U.S. and other important trade partners, like Mexico and the European Union. In Europe, political risks remain significant with an increased probability of a no-deal Brexit happening as early as in the 4Q19.

Moreover, during the past months, **macroeconomic data missed expectations in most areas and concerns about a weakening global growth intensified**. Therefore, we had to revise downwards our forecasts on regional and global growth and more downward revisions to macroeconomic forecasts could be announced over the next months, if political tensions do not ease.

Citi Economic Surprise Index, developed countries



Source: Intesa Sanpaolo chart from Citi, Bloomberg data

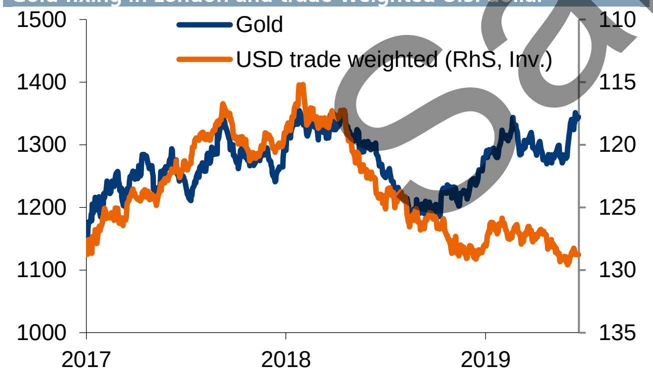
Citi Economic Surprise Index, emerging countries

Source: Intesa Sanpaolo chart from Citi, Bloomberg data

We also had to revise our forecasts about monetary policies in the U.S. and Europe. We now expect that the Fed will cut its benchmark interest rates by 25bp in 2019 and by further 25bp in 2020. The ECB is now forecasted to remain on hold up to the end of 2020, although it will probably implement more expansive measures to provide an adequate liquidity to the system.

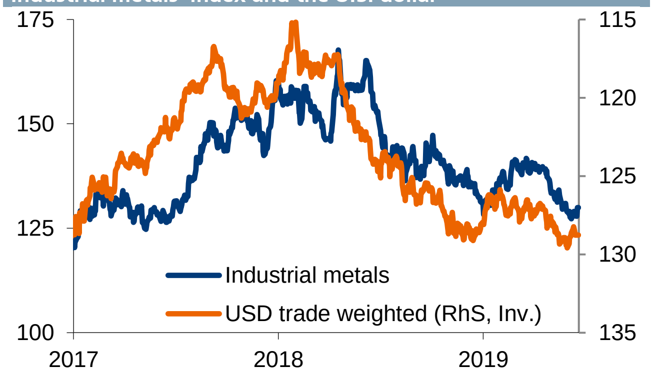
As a consequence, the trade weighted U.S. dollar may modestly depreciate over the next months. A flat or weaker U.S. currency is usually beneficial to the commodity complex due to the traditionally negative correlation between these assets. However, in this market phase the dollar effect could be easily offset by a negative market sentiment, probably depressing the main cyclical assets, including energy and industrial commodities. Indeed, we think that **once again the market sentiment will become the main driver in commodity prices, as we suspect that the main focus on financial markets will become political and geopolitical risks**.

Gold fixing in London and trade-weighted U.S. dollar



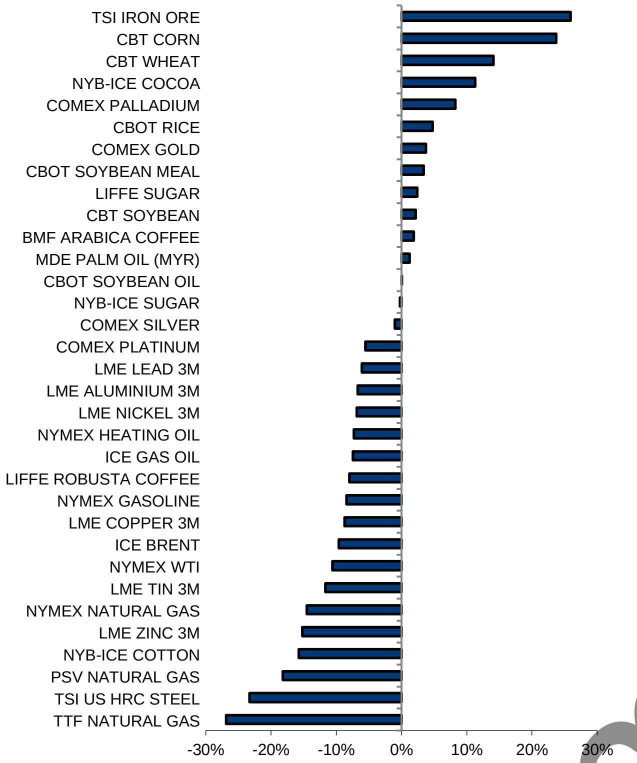
Source: Intesa Sanpaolo chart from Bloomberg data

Industrial metals' index and the U.S. dollar



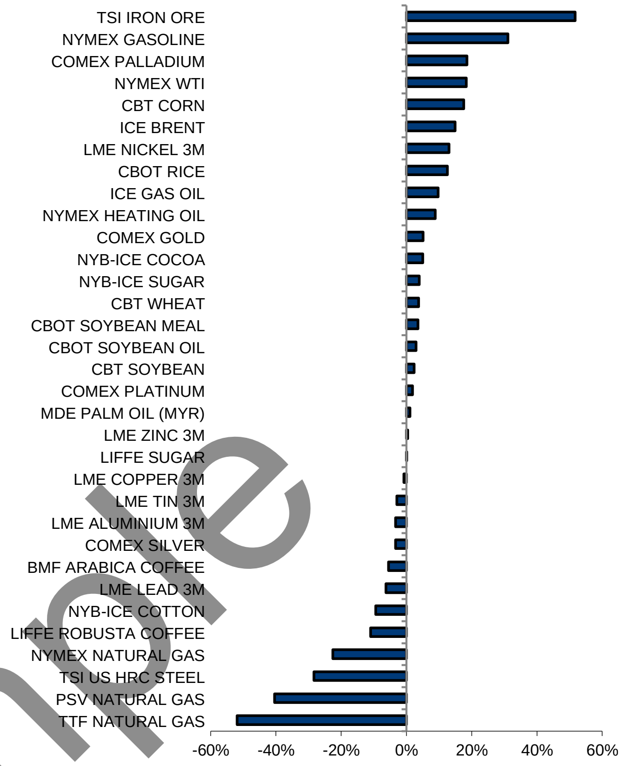
Source: Intesa Sanpaolo chart from Bloomberg data

2Q19, QTD performances as at 19.06.2019



Source: Intesa Sanpaolo chart from Bloomberg data

2019, YTD performances as at 19.06.2019



Source: Intesa Sanpaolo chart from Bloomberg data

Assumptions underlying our baseline scenario

We now envisage a gloomier baseline scenario for commodity prices. We had to rule out any short-term improvement in the U.S.-China trade dispute, and we now expect that **trade tensions will become a structural market feature**.

- We think that **the U.S. will introduce tariffs on the remaining Chinese imports** worth about 300 billion dollars and that **China may retaliate** by imposing trade limits on goods perceived as strategic for some core industries, like technology and defence. Both the economies will suffer, although China would bear the most negative impact in terms of reduction in potential growth. In several industries, the global supply chains may be disrupted, with possible negative impact on other areas, including Europe. We had an anticipation of the severe and far-reaching consequences of U.S. tariffs and sanctions in the steel sector: now, steel prices in Europe are cheaper than in China, the world biggest producer, as Chinese and Turkish steel exports have been diverted to the old continent. Despite the safeguard clauses, the European market is in oversupply amid abundant imports and weak domestic demand. The biggest losers are European steel mills, negatively affected by low prices and rising input costs, on the back of the stellar rally recorded by iron ore prices after the dam disaster in Brazil and weather-related disruptions in Australia.
- We currently assume that **the U.S.-Mexico dispute over immigration controls will not turn into more limits to regional trade**. We think that the new USMCA[1] deal will be probably ratified and that U.S. tariffs on aluminium and steel imports from these two countries will be probably removed.

[1] USMCA: United States, Mexico, Canada Agreement, replacing the previous NAFTA.

- At the moment, **we do not include in our baseline scenario the introduction of U.S. tariffs on European and Asian vehicle imports**. However, this issue will be discussed ahead of the November deadline and will probably fuel volatility in market prices. The significant threat of trade limits on the automotive sector represents the biggest downside risk weighting on our commodity outlook.

Also, **geopolitical risks are here to stay**. We assume that several dossiers will be frozen as long as the U.S.-China relationship does not improve: **Venezuela and North Korea** are the most evident examples.

In the Middle East, tensions escalated after the U.S. did not renew their waivers to the biggest importers of Iranian crude. **Iran threatened to scale down its commitments under the 2015 JCPOA nuclear deal** next July, if European and Asian signatories do not restart crude imports and restore financial ties. Over the past weeks, all the parties involved tried to smooth the tone, expressing their desire to avoid military confrontation in the area.

Over the next months, the level of tensions will remain high, but we assume that Iran will not abandon the nuclear deal and that possible negative accidents (like sabotage attacks from unknown sources in the Hormuz Strait or terrorist attacks to sensitive targets) will not be so severe to lead to an embargo against Iran nor to open military confrontation with a Saudi-U.S. coalition. However, **unpredictable events may start a series of unstoppable retaliations leading to the break of diplomatic relationships, and Iran relinquishing its OPEC membership is now relevant** (we attribute a 10% probability to Iran abandoning OPEC over the summer in our scenario analysis).

Within this framework, **the role of Russia in the Middle East becomes even more critical** in several issues. Concerning the oil policy, the cohesion inside the OPEC+ could break, if Iran expresses its desire to retire its membership in retaliation against Saudi's higher exports offsetting lower Iranian exports, and if Russia pushes to abandon the current deal, in order to satisfy Russian producers wishing to profit more from relatively high prices.

Forecasts for the commodity universe

Energy. We still think that, over the next months, crude oil prices will remain in a broad range and will trade most of the time between 60 and 75 dollars. Upward pressures will be triggered by geopolitical risks and OPEC+ pledges to maintain the global market in balance. Downward pressures will be caused by concerns about trade tensions, a fragile global growth and weakening global crude demand. Volatility may still have an important impact on price movements. For gas, we forecast that prices will increase both in the U.S. and in Europe thanks to a seasonal pick-up in demand.

Precious metals. Prices will probably be well supported by political tensions and volatility in risky assets. However, we still expect that in the foreseeable future gold will trade for most of the time within a 1,250-1,400 dollar range. We assume that gold could trade well above the level of 1,400 dollars only if serious concerns about global growth intensify and trigger a new spike in risk aversion and a consequent fall in cyclical assets, including global equities, energy and industrial commodities. We favour palladium to platinum due to the ongoing trends in the automotive sector.

Industrial metals. A bearish market sentiment, fuelled by trade tensions and concerns about a weaker than expected growth in China, exerts a deep negative impact on industrial metals' prices. We think that the upside potential in this complex remains very limited, as long as the markets focus on political risks. However, we maintain our forecasts that prices should significantly increase in the next 3-5 years, as industrial metals are endowed with the strongest fundamentals in the commodity complex: most metals are expected to record deficits in both 2018 and 2019, global stocks are declining, low prices discourage secondary supply and investments were low during the past years.

Agricultural commodities. Most agricultural goods recorded important price swings over the past months amid weather-related risks and concerns about supplies. U.S. crops are influenced by trade tensions with China and by the US Government's pledges of more subsidies to those farmers affected by Chinese tariffs. Soft commodities, like coffee, are expected to be less influenced by global political tensions, as prices should follow more closely their fundamentals. Therefore, soft commodities are perceived as an interesting diversification tool.

Price forecasts for the main commodities

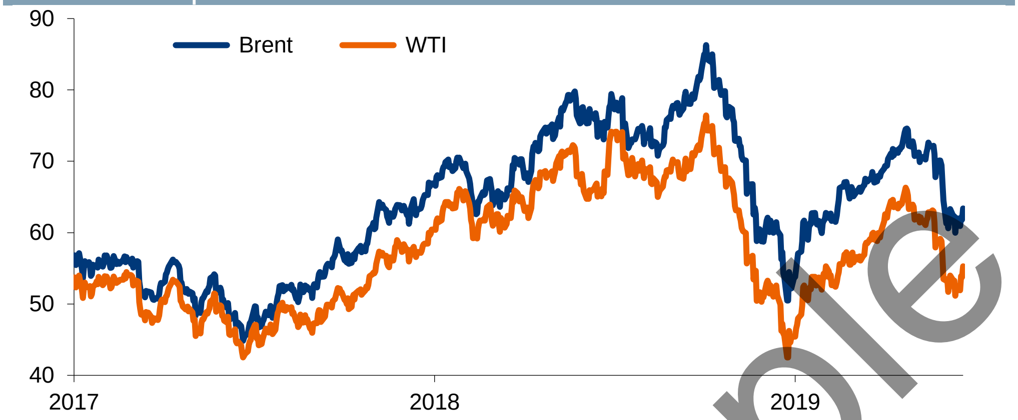
As at 17.06.2019		3Q19	4Q19	2019	2020	2021
CO1 Comdty	ICE BRENT	67.0	70.0	67.2	70.0	70.0
CL1 Comdty	NYMEX WTI	58.0	62.0	58.4	64.0	66.0
NG1 Comdty	NYMEX NATURAL GAS	2.3	3.0	2.7	3.0	3.0
GOLDLNPM Index	LME GOLD	1,350	1,325	1,321	1,300	1,325
SLVRLND Index	LME SILVER	15.0	15.2	15.2	16.0	16.25
PLTMLNPM Index	LME PLATINUM	800	800	815	800	800
PLDMLNPM Index	LME PALLADIUM	1,450	1,480	1,436	1,550	1,600
LMCADS03 Comdty	LME COPPER 3M	6,000	6,000	6,079	6,000	6,300
LMAHDS03 Comdty	LME ALUMINIUM 3M	1,800	1,800	1,823	1,800	1,920
LMNIDS03 Comdty	LME NICKEL 3M	12,500	12,500	12,416	13,000	14,000
LMZSDS03 Comdty	LME ZINC 3M	2,500	2,500	2,578	2,500	2,600
LMPBDS03 Comdty	LME LEAD 3M	1,800	1,800	1,882	1,800	1,880
LMSNDS03 Comdty	LME TIN 3M	19,500	19,500	19,894	19,500	19,750
SCO1 Comdty	SGX IRON ORE	90	85	89.1	82.0	77.0
NASS000C Index	TSI US HRC STEEL	500	530	584	550	550
JBO1 Comdty	LME SCRAP	300	300	303	300	300
JBP1 Comdty	LME REBAR	468	465	469	463	460
C 1 Comdty	CBOT CORN	450	460	421	480	490
W 1 Comdty	CBOT WHEAT	500	500	494	500	500
S 1 Comdty	CBOT SOYBEAN	900	900	892	900	940
KC1 Comdty	NYB-ICE ARABICA COFFEE	100	105	100	110	115
DF1 Comdty	LIFFE ROBUSTA COFFEE	1,400	1,450	1,437	1,525	1,600
SM1 Comdty	CBOT SOYBEAN MEAL	310	310	310	300	300
BO1 Comdty	CBOT SOYBEAN OIL	28.0	28.0	28.4	28.0	28.0

Source: Intesa Sanpaolo estimates. Iron: one-month futures contract listed on the Singapore stock exchange and based on a basket of reference prices published by the Steel Index. Steel: The Steel Index: index calculated as the weighted average price paid for US hot-rolled coil steel trades

Crude oil: frequent swings in market sentiment

Over the next months, the markets will probably continue to focus their attention alternatively from concerns about escalating trade tensions to fears for supply disruptions. In our opinion, physical markets' fundamentals and geopolitical risks may prevail over global macroeconomic and political concerns. In our baseline scenario, OPEC will not break and therefore the current output cuts implemented by OPEC+ will continue.

Brent and WTI oil prices



Source: Intesa Sanpaolo chart from Bloomberg data

During the 2Q19, crude oil prices recorded significant swings, following frequent oscillations in the market sentiment and switches between risk-on and risk-off moods. The markets often move their focus from concerns about escalating trade tensions and their negative impact on global economic growth and commodity demand to fears for supply disruptions, especially related to geopolitical risks.

Physical markets' fundamentals tightened over the past months amid the ongoing output decline in Venezuela, U.S. sanctions against Iran, production cuts in Canada and OPEC+ countries and unexpected contamination problems along the Druzhba pipeline transporting Russian crude to Eastern Europe.

The data published in June by the U.S. Energy Information Administration (EIA) show that the planned output cuts and the several supply disruptions pushed the global market in deficit. In fact, the EIA forecasts that this year demand will surpass supply by about 0.3 million barrels per day (mb/d).

However, non-OPEC output growth is expected to remain exceptionally strong both in 2019 and 2020, rising much quicker than total consumption. Therefore, even assuming a rollover of the current OPEC+ deal and unchanged U.S. sanctions against Iran and Venezuela, the market will probably come back into surplus next year, with an estimated oversupply of about 0.3 mb/d.

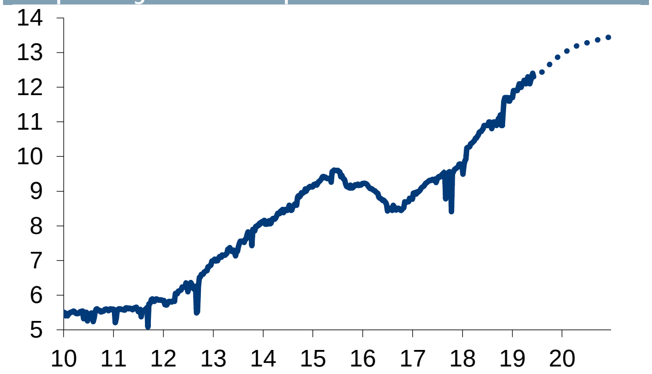
Supply and demand estimates published by U.S. EIA in June 2019

Estimates published in June 2019 in mb/d	Global Demand	Non-OPEC Supply	U.S. Supply	LNG OPEC Supply	Crude OPEC Supply	Call on OPEC crude*	Market balance**
2018	99.9	63.4	11.0	5.3	32.0	31.2	0.7
2019	101.1	65.5	12.3	5.2	30.2	30.4	-0.3
y/y change	1.2	2.2	1.4	-0.2	-1.8	-0.8	
2020	102.6	68.1	13.3	5.0	29.7	29.5	0.3
y/y change	1.4	2.6	0.9	-0.2	-0.4	-1.0	

Note: (*) Call on OPEC crude = World Consumption – Non-OPEC Supply - OPEC LNG supply; (**) Market balance = OPEC crude supply - Call on OPEC crude. Source: Intesa Sanpaolo chart based on US EIA data

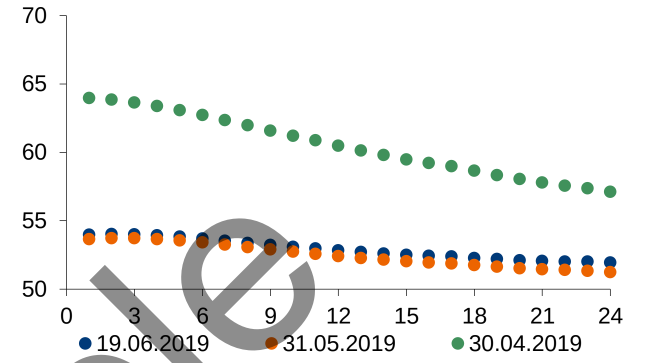
The shape of the forward curves reflects the strength of U.S. output growth: the front-end of the WTI curve is in contango, signalling a very well supplied domestic market, where infrastructural constraints limited takeaway capacity from shale basins toward the Gulf Coasts. However, these bottlenecks are likely to ease as of mid-2019 thanks to pipelines' capacity expansion and flow reversals. On the contrary, the Brent curve is in backwardation, reflecting the combined impact of ongoing output cuts, U.S. sanctions and supply disruptions.

Exceptional growth in U.S. production



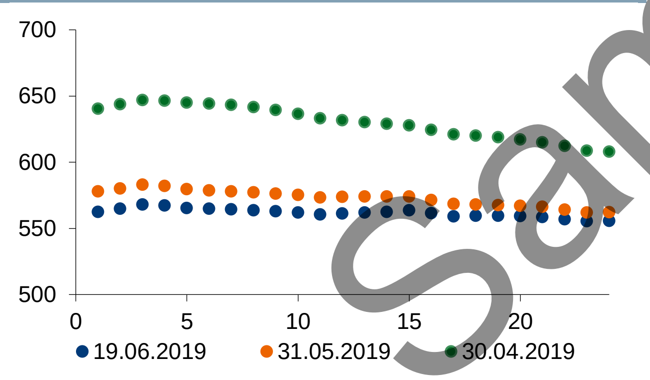
Source: Intesa Sanpaolo chart based on U.S. EIA data

WTI forward curve



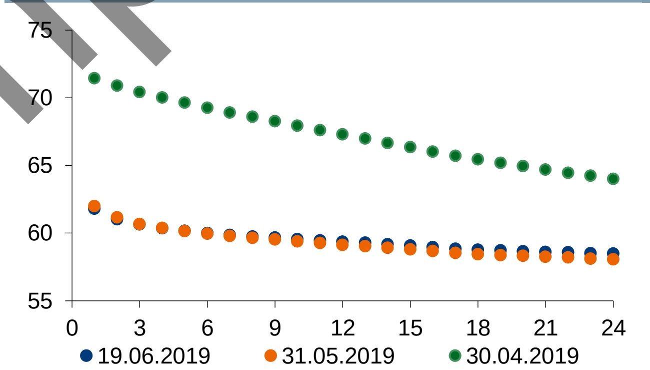
Source: Intesa Sanpaolo chart based on Bloomberg data

Gasoil forward curve



Source: Intesa Sanpaolo chart based on Bloomberg data

Brent forward curve



Source: Intesa Sanpaolo chart based on Bloomberg data

In our opinion, the next months will be crucial for the OPEC's own future. On the one hand the strategy to reduce the cumulative output didn't bring the hoped results, as it didn't halt shale output growth nor helped anchoring prices at the level preferred by Saudi, i.e. close to their fiscal breakeven oil price in a USD 70-90 range. On the other hand, higher tensions in the Middle East are weakening OPEC's internal cohesion.

Over the past weeks, several sabotage attacks were reported near the Strait of Hormuz and Yemen's Houthi rebels were more actively targeting Saudi infrastructures.

The current geopolitical framework is also complicated by the serious risk of Iran abandoning the nuclear deal, irremediably compromising its relationships with western countries, and by the strength of the U.S.-Saudi relationship.

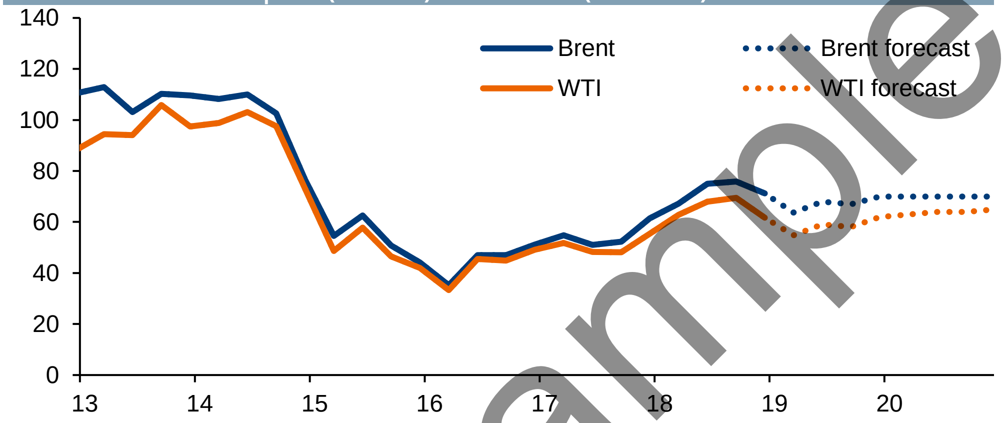
In our opinion, such unusual level of political tensions could force actors to deviate from the preferred paths and lead to undesired consequences. In particular, if tensions between Saudi Arabia and Iran do not ease, OPEC unity could break, and its role may become less relevant.

Apparently, the first cracks in OPEC+ also emerged, as Russia often threatened to abandon the deal. On the contrary, Saudi confirmed their desire to roll over the output limitations at least till the end of the year.

In our baseline scenario, we forecast that crude prices will frequently swing in a broad range over the next months. We see the level of USD 50 as a strong support for Brent. This level could be reached, only if political tensions intensify and macroeconomic data disappoint in the main consuming countries. We see the level of USD 85 as a strong resistance for Brent. This level may be broken, only if geopolitical risks in the Middle East translate into severe concerns about security of supply and flow disruptions through the Strait of Hormuz.

We currently forecast an average Brent price of USD 67 over 3Q19 and of USD 70 in 2020. In fact, we think that physical markets' fundamentals and geopolitical risks may prevail over political concerns related to trade war. Obviously, our forecasts are based on the assumption that OPEC+ will maintain the current output cuts at least till mid-2020.

Brent and WTI: historical prices (solid line) and estimates (dotted line) in USD/barrel



Source: Intesa Sanpaolo estimates, Intesa Sanpaolo chart based on Bloomberg data

Price estimates for Brent

As at 18.06.2019	3Q19	4Q19	2019	2020	2021	2022
ICE BRENT	67.0	70.0	67.2	70.0	70.0	68.0
Median, Bloomberg	70.0	70.0	67.8	68.0	67.0	68.0
Forward Curve	59.6	58.9	62.4	58.3	57.8	58.1

Source: Intesa Sanpaolo chart from Bloomberg data

Price estimates for WTI

As at 18.06.2019	3Q19	4Q19	2019	2020	2021	2022
NYMEX WTI	58.0	62.0	58.4	64.0	66.0	64.0
Median, Bloomberg	62.0	62.3	61.0	61.6	62.9	63.8
Forward Curve	58.9	52.2	55.3	51.7	51.1	51.4

Source: Intesa Sanpaolo chart from Bloomberg data

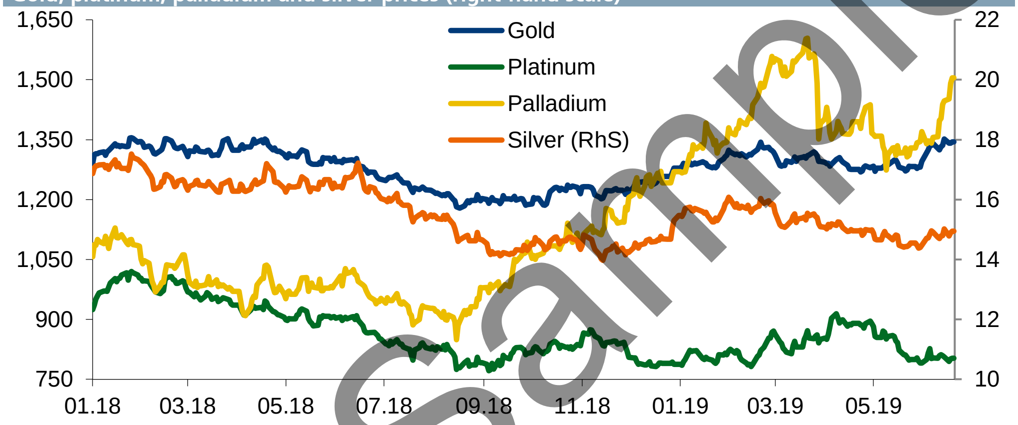
Precious metals: gold benefits from rising uncertainties

The global outlook is turning positive for gold: monetary policies are becoming more accommodative and low interest rates in the main economies are reducing the opportunity cost of holding precious metals and improving the risk/return profile of gold investments. Moreover, political and geopolitical tensions will probably remain high. This context should favour gold through investors' demand for safe havens and Central banks' quest for diversification.

The prices of most precious metals are marginally higher than the levels prevailing in early January. The best performances have been recorded by palladium, in structural deficit, and gold, driven by Central banks' strong demand, investors in developed markets and consumers in emerging markets.

We think precious metals will remain well supported also during the next months, as the main Central banks will pursue accommodative monetary policies and the trade weighted U.S. dollar is expected to modestly depreciate. However, the upside potential for gold and silver prices is limited by low inflation risks, absent severe episodes of stress on financial markets.

Gold, platinum, palladium and silver prices (right-hand scale)



Source: Intesa Sanpaolo chart from Bloomberg data

Gold

The global outlook is turning very positive for gold: monetary policies should become more accommodative, with the Fed expected to cut interest rates over the 2H19 (probably as early as in the 3Q19) and next year, and the ECB committed to maintain negative rates at least up to mid-2020 and to provide adequate liquidity in the Euro Zone through more targeted easing. These pledges significantly contributed to the gold rally recorded so far in June, as low interest rates in the main economies are reducing the opportunity cost of holding precious metals and improving the risk/return profile of gold investments.

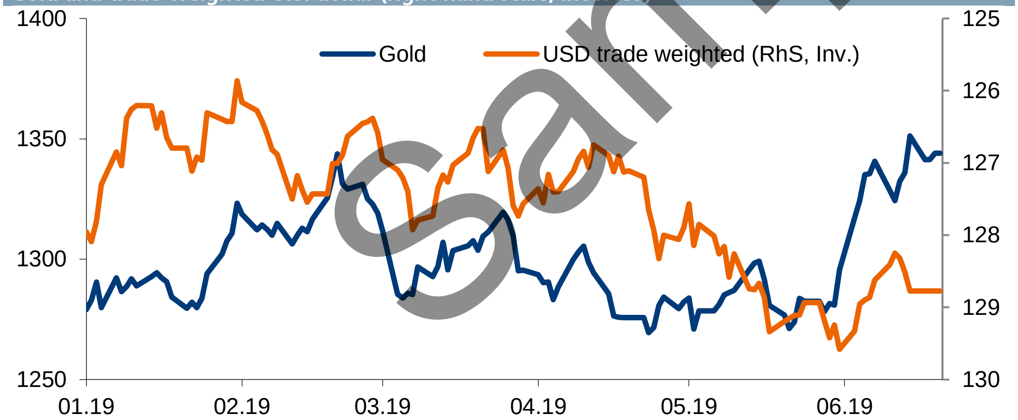
Moreover, in June political and geopolitical risks escalated, and tensions will probably remain high at least till the end of this year. This context will favour gold through two main transmission channels:

- Political uncertainties and the several risks weighting on the global macroeconomic framework (Brexit, trade tensions and geopolitical risks, especially in the Middle East) will support investors' appetite for gold as a safe-haven asset and an important diversification tool in financial portfolios. In fact, over the past quarters we often noticed a significant positive correlation between gold and U.S. policy uncertainty during periods of heightened concerns. For instance, U.S. policy uncertainty indexes peaked in early 2019 (as gold price did) and then declined toward more comfortable levels in April (and gold followed). Over the next months, we forecast uncertainty to remain an important feature in U.S. policy, at least concerning trade policy, and it could add volatility to gold prices.
- Central banks in several important emerging markets will continue their efforts to de-dollarize their official reserves. The trend is especially clear in those countries that are more negatively affected by U.S. tariffs and sanctions, like China, Russia and Turkey.

In our baseline scenario, we expect gold price to remain high over the 3Q19, probably trading most of the time above the level of USD 1,325 an ounce and remaining above the strong ceiling of USD 1,400 for a limited period. We currently forecast an average gold price of USD 1,350 over 3Q19, of USD 1,325 in 4Q19 and of USD 1,300 in 2020. Risks on our forecasts are skewed to the upside. Overall, we think that gold is currently one of the best tools for investors looking for capital protection.

Our forecasts also point toward a weakening of the trade-weighted U.S. dollar over the next months. If the traditionally negative correlation between the U.S. currency and gold holds, a weaker dollar would be positive for gold prices.

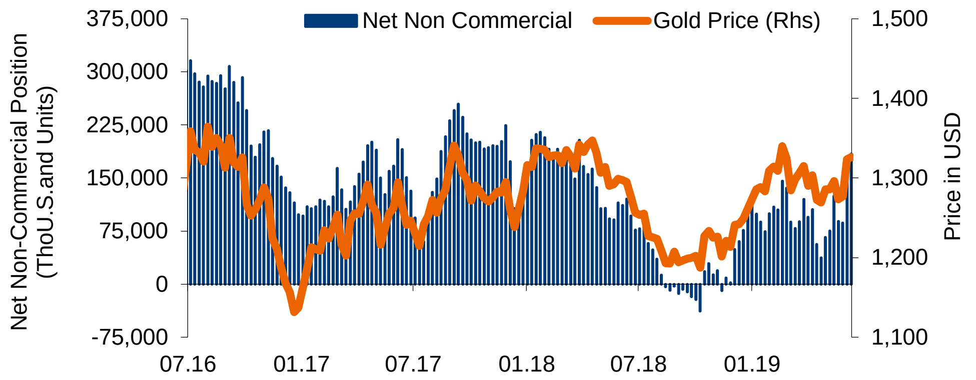
Gold and trade-weighted U.S. dollar (right-hand scale, inverted)



Source: Intesa Sanpaolo chart from Bloomberg data

The analysis of net non-commercial positions recorded by the U.S. Commodity Futures Trading Commission (CFTC), usually held by money managers and speculators, indicates that as market expectations toward monetary policies became more dovish, financial operators expanded their net long positions on gold reaching the highest level since April 2018.

Gold (right-hand scale) and speculative positions

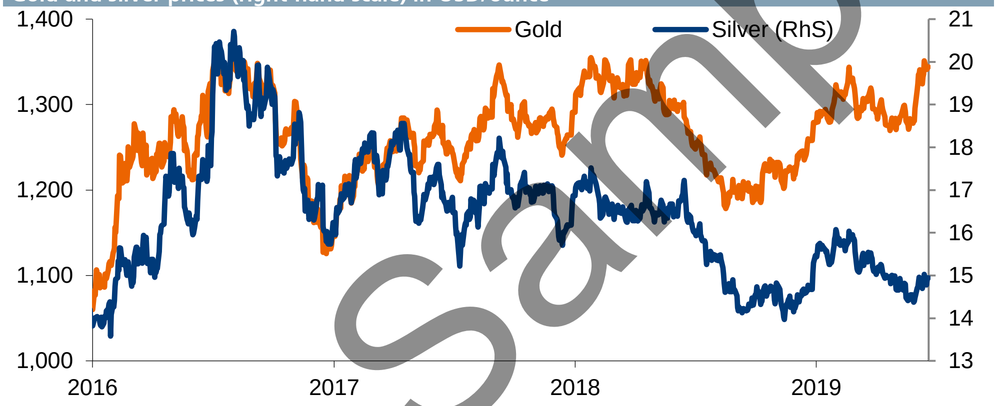


Source: Intesa Sanpaolo chart from U.S. CFTC and Bloomberg data

Silver

So far this year, silver recorded the worst performance among precious metals. The trend of systematic underperformance of silver against gold has been in place since 2011, excluding the temporary reversal in 2016. Therefore, the gold/silver ratio is close to a record high.

Gold and silver prices (right-hand scale) in USD/ounce



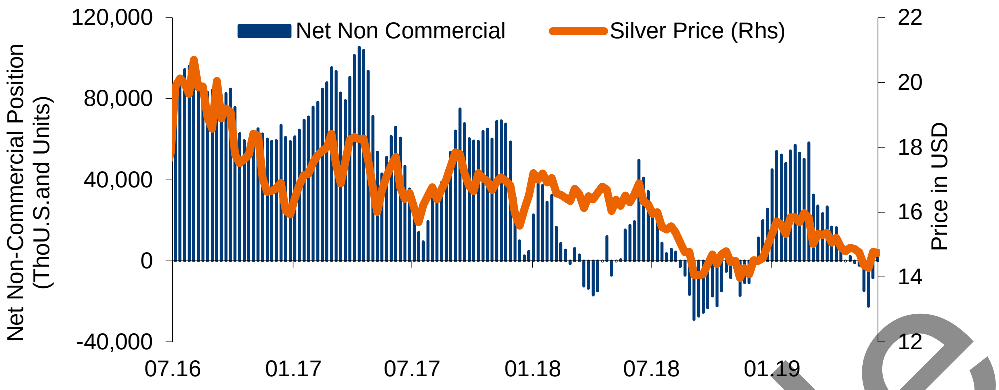
Source: Intesa Sanpaolo chart from Bloomberg data

Gold/silver ratio

Source: Intesa Sanpaolo chart from Bloomberg data

As a consequence, net non-commercial positions in silver, monitored by the U.S. CFTC and held by money managers or hedge funds, turned again negative at the end of April. In our opinion, if political tensions persist over the summer and gold prices remain high, we expect investors' renewed interest in silver. Therefore, silver prices will likely rebound, driven by short covering and demand for safe-haven assets.

Silver (right-hand scale) and speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC and Bloomberg data

We currently estimate an average price of USD 15.0 an ounce for 3Q19 and a modest increase towards an average price of USD 15.2 for 4Q19. We then forecast an average price of USD 16.0 in 2020. As seen in the latest round of liquidation of net-long speculative positions, the level of USD 14.0 represent a very strong support.

We see limited downside risks in our forecasts, as we think that silver is undervalued relative to gold, while silver fundamentals remain strong, with a market expected in deficit in 2019 on the back of robust demand from the electronic and energy sectors. In the longer term, silver should overperform gold, as both industrial and investment demand gain strength.

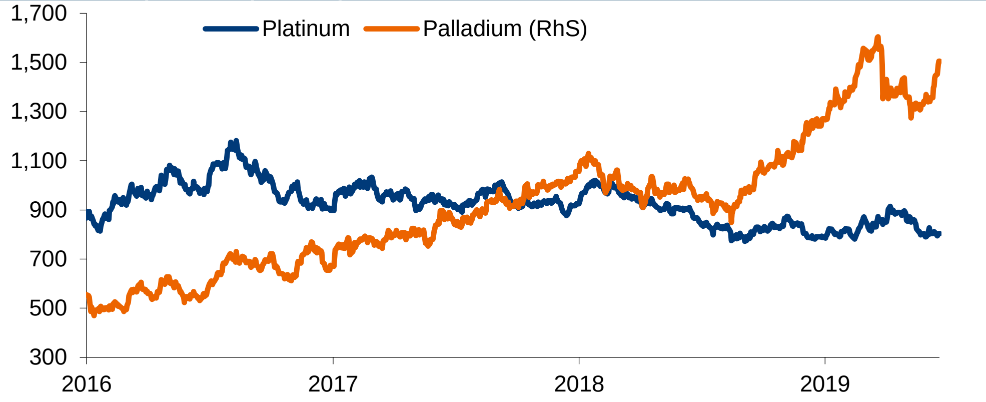
Platinum and palladium

As precious metals, platinum and palladium aren't usually considered safe-haven assets, as their industrial usage in the automotive sector often prevails over the dynamics of financial markets.

Therefore, our preference of palladium over platinum is explained by physical markets' fundamentals: platinum is expected to record a small market surplus in 2019, while palladium is forecast to record a market deficit for the eighth consecutive year. Moreover, palladium deficit is widening against constrained mine output growth in South Africa and Russia.

On the consumption side, platinum demand is expected to remain structurally weaker than palladium one due to the ongoing reduction in diesel vehicles' market share compared to gasoline vehicles amid tightening emission regulations in Europe and China. The penetration of hybrid and electrical vehicles is also further eroding diesel's market share.

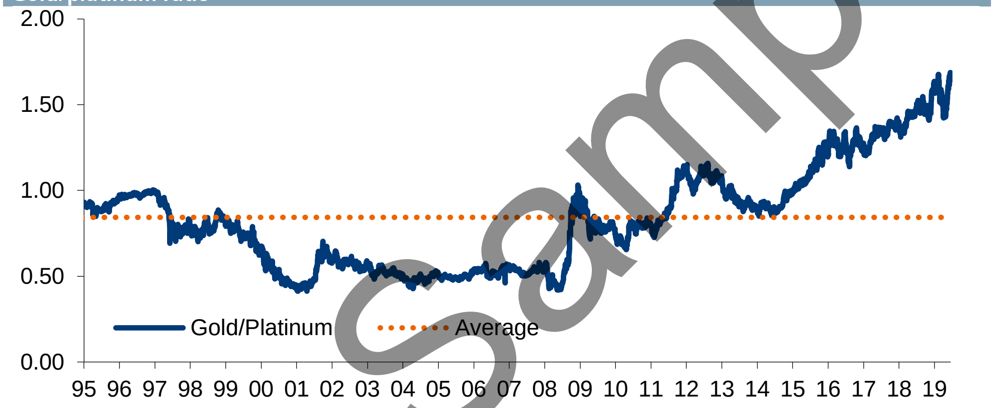
Platinum and palladium prices (right-hand scale) in USD/ounce



Source: Intesa Sanpaolo chart from Bloomberg data

We currently estimate an average platinum price of USD 800 an ounce for 3Q19 and the same average in 2020. We assume platinum prices will remain in a wide trading range, but the upward potential is limited due to the structural changes in the global automotive sector. As a consequence, the gold/platinum ratio should remain far from its historical average.

Gold/platinum ratio

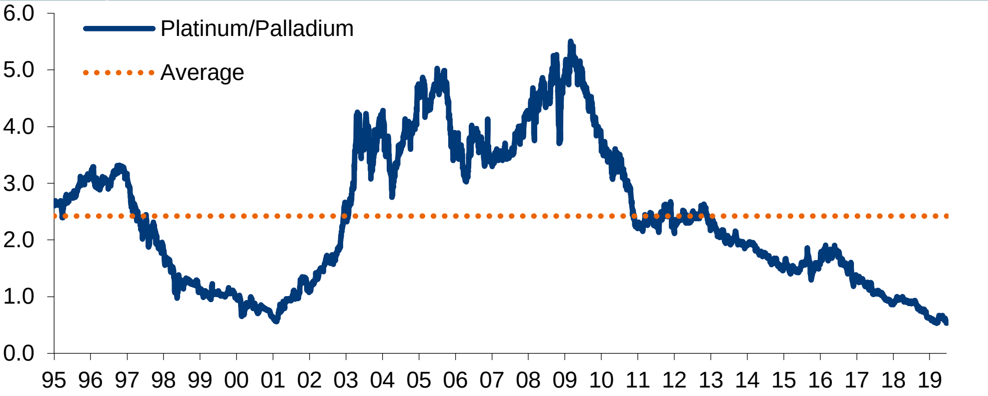


Source: Intesa Sanpaolo chart from Bloomberg data

We estimate: an average palladium price of USD 1,450 an ounce for 3Q19 and of USD 1,550 in 2020. We expect that prices could reach new record highs in 2020 amid positive fundamentals.

Therefore, the platinum/palladium ratio should further decrease over the years, further increasing the distance from its historical average.

Platinum/palladium ratio

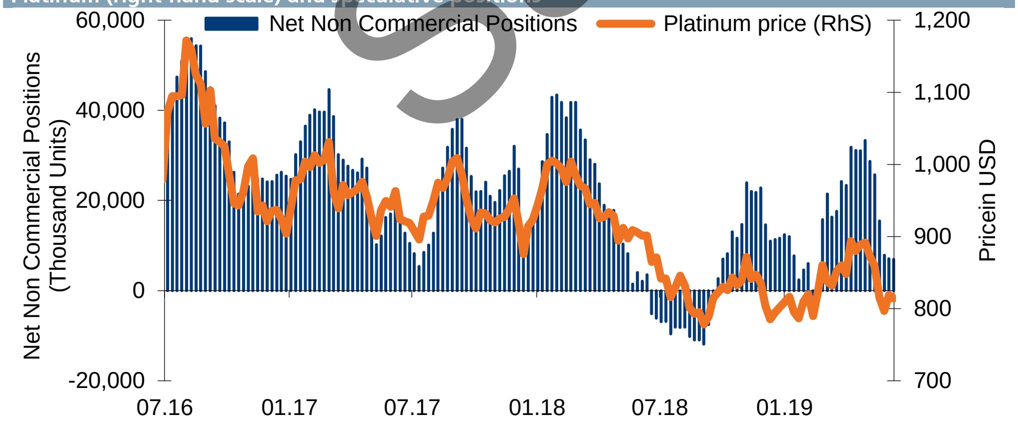


Source: Intesa Sanpaolo chart from Bloomberg data

We see the threat of U.S. tariffs on vehicle imports as the biggest downside risk weighting on our baseline scenario for platinum and palladium. Indeed, in the event of new trade limitation, global vehicle sales could slow down as higher uncertainty about trade flows, coupled with important shifts in technology, could further discourage vehicle purchases, especially in urban areas in developed markets. Consequently, estimates about palladium and platinum consumption would be revised downwards and prices would inevitably decline.

U.S. CFTC figures show that money managers and hedge funds are currently positive on both metals, although the positioning is apparently less volatile on palladium than on platinum. For instance, in the 1Q we noticed a quick accumulation of net long positions on platinum, driven by rising platinum prices and by a positive sentiment toward precious metals in general. Then, in the 2Q we recorded a sharp liquidation of net long positions, driven by lower prices and the perception that global market remains well supplied. We expect more liquidations of long positions, as investors should revert toward a neutral or negative exposure.

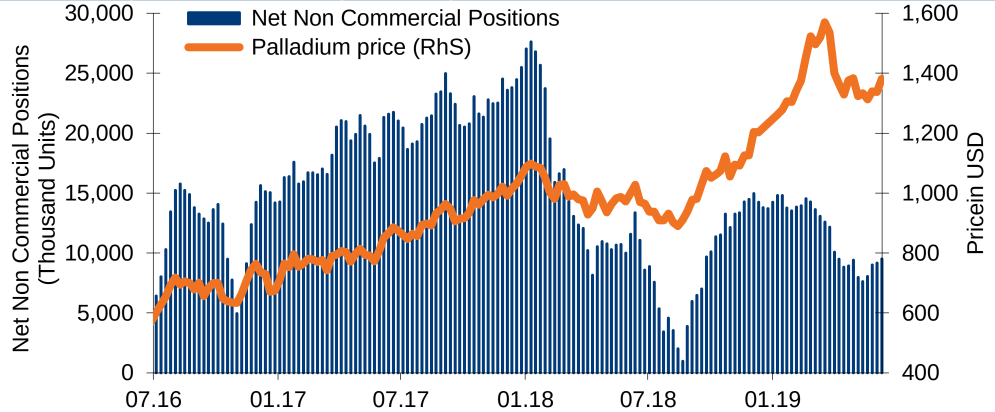
Platinum (right-hand scale) and speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC and Bloomberg data

On the contrary, net long speculative positions on palladium have been more stable despite the impressive price swings recorded by the metal. We expect that investors will expand their long positions on palladium over the next months, contributing to a gradual increase in palladium prices.

Palladium (right-hand scale) and speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC and Bloomberg data

Forecasts for precious metals

Price forecasts estimated by Intesa Sanpaolo

As at 17.06.2019		3Q19	4Q19	2019	2020	2021
LBMA GOLD	in USD/oz	1,350	1,325	1,321	1,300	1,325
	in EUR/gr	38.38	37.51	37.54	35.81	35.42
LBMA SILVER	in USD/oz	15.0	15.2	15.2	16.0	16.25
	in EUR/gr	0.43	0.43	0.43	0.44	0.43
LBMA PLATINUM	in USD/oz	800	800	815	800	800
	in EUR/gr	22.74	22.65	23.16	22.04	21.39
LBMA PALLADIUM	in USD/oz	1,450	1,480	1,436	1,550	1,600
	in EUR/gr	41.22	41.90	40.81	42.70	42.77

Source: Intesa Sanpaolo estimates

Gold price forecasts: comparison with the market and consensus, in USD/oz

As at 17.06.2019	3Q19	4Q19	2019	2020	2021
LBMA GOLD	1,350	1,325	1,321	1,300	1,325
Median, Bloomberg	1,330	1,350	1,323	1,375	1,324
Forward Curve	1,350	1,372	1,332	1,377	1,398

Source: Intesa Sanpaolo and Bloomberg data

Silver price forecasts: comparison with the market and consensus, in USD/oz

As at 17.06.2019	3Q19	4Q19	2019	2020	2021
LBMA SILVER	15.0	15.2	15.2	16.0	16.25
Median, Bloomberg	16.0	16.1	15.6	16.3	16.0
Forward Curve	15.2	15.3	15.2	15.4	15.8

Source: Intesa Sanpaolo and Bloomberg data

Platinum price forecasts: comparison with the market and consensus, in USD/oz

As at 17.06.2019	3Q19	4Q19	2019	2020	2021
LBMA PLATINUM	800	800	815	800	800
Median, Bloomberg	873	893	860	890	920
Forward Curve	796	820	816	823	N.A.

Source: Intesa Sanpaolo and Bloomberg data

Palladium price forecasts: comparison with the market and consensus, in USD/oz					
As at 17.06.2019	3Q19	4Q19	2019	2020	2021
LBMA PALLADIUM	1,450	1,480	1,436	1,550	1,600
Mediana, Bloomberg	1,263	1,200	1,320	1,150	1,313
Forward Curve	1,489	1,487	1,461	1,437	N.A.

Source: Intesa Sanpaolo and Bloomberg data

EUR/USD forecasts: comparison with the market and consensus, in USD/oz					
As at 17.06.2019	3Q19	4Q19	2019	2020	2021
EUR/USD	1.13	1.14	1.13	1.17	1.20
Mediana, Bloomberg	1.13	1.15	N.A.	1.21	1.22
Forward Curve	1.13	1.14	N.A.	1.17	1.19

Source: Intesa Sanpaolo and Bloomberg data

Industrial metals: political risks prevail

The key risks weighting on the sector are related to macroeconomic and political factors that could prevail over the good fundamentals. In particular, concerns about weakening global growth and escalations in U.S. and China's trade war are expected to limit the upside potential of industrial metals' prices in the short and medium term. Longer term, we are very positive on the complex, as prices should significantly increase in the next 3-5 years to incentivize investments in mining.

Among the main commodity sectors, industrial metals benefit from the strongest fundamentals. For most non-ferrous metals, inventories are low, markets are expected in deficit this year, and investments in expansion capacity are often perceived as insufficient to satisfy long-term demand growth.

The key risks weighting on the sector are related to macroeconomic and political factors, which could prevail over the good fundamentals. In particular, concerns about weakening global growth and escalations in U.S. and China's trade war are expected to limit the upside potential of industrial metals' prices up to the end of 2020. Longer term, we are very positive on the complex, as prices should increase in the next 3-5 years to incentivize investments in mining.

During the next months, industrial metals' markets will probably be influenced by both exogenous factors and metal-specific fundamentals.

Among the most important exogenous drivers, we highlight:

- Political tensions, now a permanent market feature. Further negative events (no deal Brexit, tariffs on vehicle imports) remain the biggest downside risk to our forecasts;
- Macroeconomic scenario: we envisage a weaker than earlier expected growth, but fiscal and monetary policies are supportive and commodity demand is still growing;
- U.S. dollar: in 2019, the expected moderate weakening of the U.S. dollar could represent a boon for metals' prices.

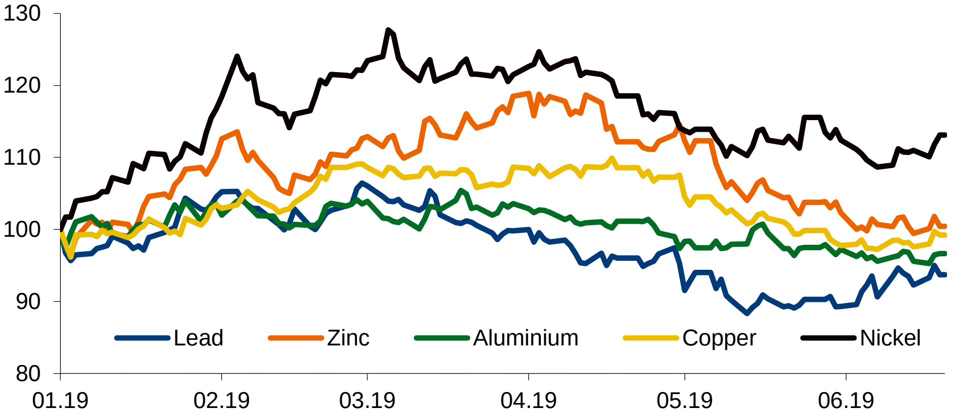
Among the most significant metal-specific fundamentals, we highlight:

- Policies in China: the positive impact of pro-growth policies may be crucial to offset the negative impacts from U.S. tariffs;
- Investment cycle: after years of shrinking capital expenditures, we still witness little appetite for large-scale investment plans and a preference for a shareholder-friendly attitude;
- Political risks are a serious threat amid resource nationalism, labour negotiations, safety and environmental concerns.

Moreover, several industrial metals are now perceived as interesting tools in strategic asset allocation, thanks to the big themes of electric vehicles' (EV) penetration and global warming, which implies more extreme weather events and a higher risk of unexpected supply disruptions.

3-month copper, aluminium, nickel, zinc and lead futures quoted on the LME are used as benchmarks for price forecasts and targets.

Year-to-date performances of the main industrial metals (LME 3-month futures)



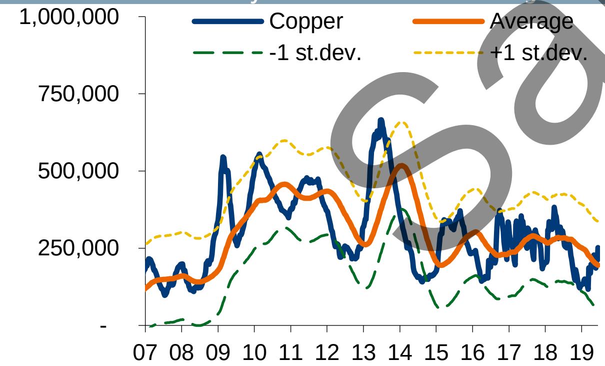
Source: Intesa Sanpaolo chart from Bloomberg data

Copper

Among industrial metals, copper is the most influenced by financial and macroeconomic factors. Political risks related to the trade war had a negative impact on copper prices, despite tight physical markets.

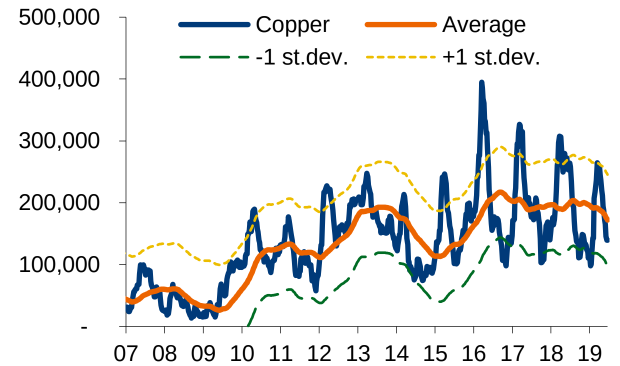
In fact, copper fundamentals are good, as the refined market should record deficits in both 2019 and 2020 and global stocks remain in a comfortable range. Longer term, demand growth will probably be driven by increasing volumes requested by power and automotive industries, while insufficient investments in capacity expansion significantly constrain supply growth.

Inventories monitored by the London Metal Exchange



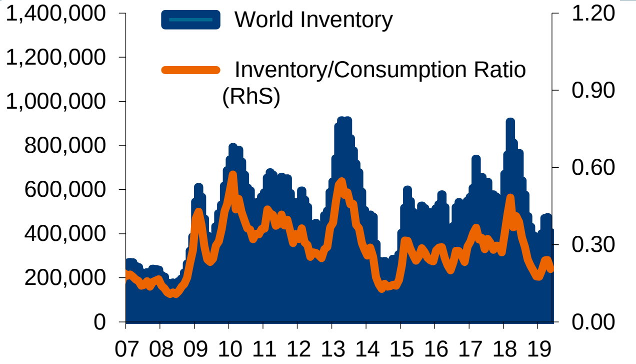
Source: Intesa Sanpaolo chart from Bloomberg data

Inventories monitored by the Shanghai Futures Exchange



Source: Intesa Sanpaolo chart from Bloomberg data

Stock-to-global consumption ratio



Source: Intesa Sanpaolo chart from LME, WBMS data

Prices of the 3-month futures on the LME

Source: Intesa Sanpaolo chart from LME data

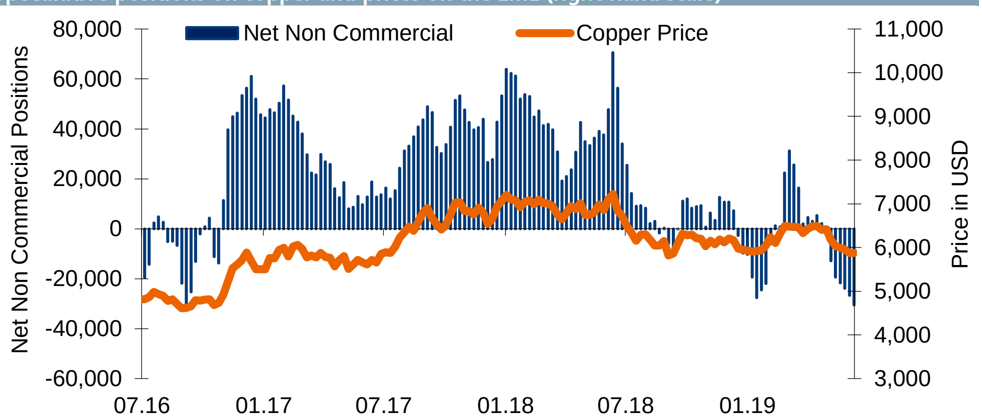
The latest semi-annual forecasts published in April by the International Copper Study Group (ICSG) suggest that the copper market will remain in deficit in 2019, although the shortage is expected to be smaller than in 2018: a deficit of about 189 thousand tonnes this year vs. a deficit of about 399 thousand tonnes last year. On the contrary, the deficit is expected to widen further in 2020 to 250 thousand tonnes.

In detail, world mine production is expected to marginally grow in 2019 (+0.2% y/y) to 20.6 million tonnes, but to expand by 1.9% y/y in 2020 to 21.0 million tonnes. World refined production is forecast to increase by 2.8% to 24.8 million tonnes in 2019 and by 1.2% to 25.1 million tonnes in 2020. World apparent refined usage is expected to increase by 1.9% in 2019 to 25.0 million tonnes and by 1.4% to 25.3 million tonnes in 2020.

Looking at higher frequency data, the latest monthly report published in May by the ICSG confirmed that the global market of refined copper is tight, when excluding seasonal distortions related to the Chinese Lunar New Year.

Copper is especially vulnerable to speculative flows. As a matter of fact, net commercial positions recorded by the U.S. CFTC reached an historical peak of net longs in June 2018, turned into a net short in August, for the first time since October 2016, and then oscillated between net long and net short. Speculative positions on copper are now net short and if our pessimistic outlook is right, they could remain negative in the foreseeable future.

Speculative positions on copper and prices on the LME (right-hand scale)



Source: Intesa Sanpaolo chart from U.S. CFTC data

In our baseline scenario, we currently forecast that copper prices will trade around an average level of USD 6,000 per tonne from the 3Q19 up to the end of 2020, as in our opinion political concerns related to the trade war and a slowdown in China will prevail over positive fundamentals.

In our opinion, risks to our forecasts are skewed towards the upside, as several years of deficit are raising production costs and marginal producers are often located in more difficult areas and provide lower-grade and higher-cost supplies. Given the insufficient level of investments in additional capacity recorded over the past decade, we expect that the copper market will remain in deficit over the coming years, and when political risks ease prices will increase to incentivise new supply.

In the most bullish scenario of easing trade tensions and of a consequent resumption of positive market sentiment, market fundamentals would become the main driver of industrial metals' prices. In such benign environment, in our opinion copper prices may trade in a higher range of about USD 6,400-7,000.

Aluminium

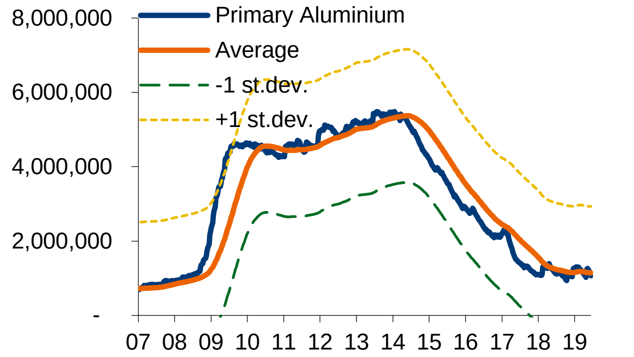
After the huge price swings recorded in 2018 and driven by political risks, U.S. tariffs on aluminium imports and U.S. sanctions against Russia, so far this year aluminium has been following the industrial metals' complex. In fact, the 1Q19 rally was driven by easing concerns about U.S.-China trade tensions and the 2Q19 drop was caused by the unexpected introduction of further U.S. tariffs on Chinese imports, by revived tensions between U.S. and Mexico and by stronger fears about the slowdown in global growth.

According to our model, the aluminium market recorded deficits in both 2017 and 2018, when the impact of supply-side reforms in China on the aluminium smelting sector was sharper, curbing the country's oversupply. Now, the global market is expected to remain close to balance or in small deficit over the whole 2019 and 2020. In fact, global supply is expected to rise over the next months due to new planned capacity additions in China and in the Middle East and to restarts of idled capacity in the U.S.

The signals coming from global stocks currently show that the global market has been in modest deficit over the last months, as inventories in the LME-monitored warehouses and the stock-to-consumption ratio are declining to their lowest levels in a decade.

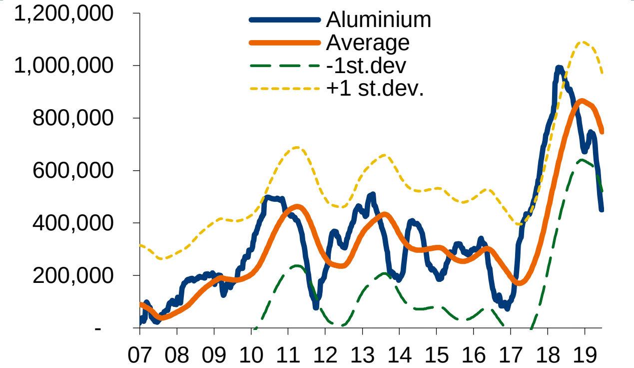
In our baseline scenario, aluminium prices may trade around an average level of USD 1,800 per tonne from the 3Q19 till the end of 2020, as in our opinion political concerns related to the trade war and a slowdown in China will probably depress prices in all the industrial metals' complex. In the most bullish scenario of easing trade tensions and positive market sentiment toward cyclical assets, we forecast that aluminium prices could increase and trade in a higher range of about USD 1,900-2,000.

Inventories monitored by London Metal Exchange



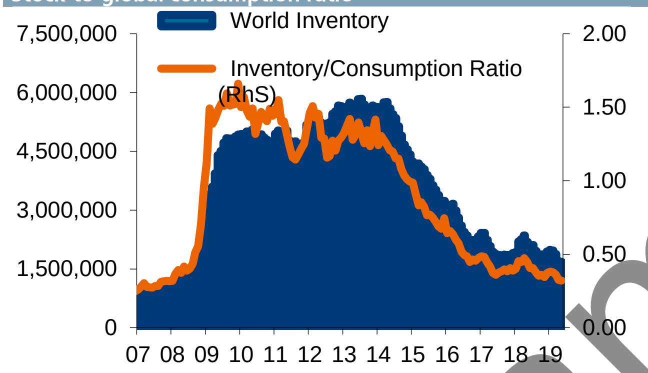
Source: Intesa Sanpaolo chart from Bloomberg data

Inventories monitored by Shanghai Futures Exchange



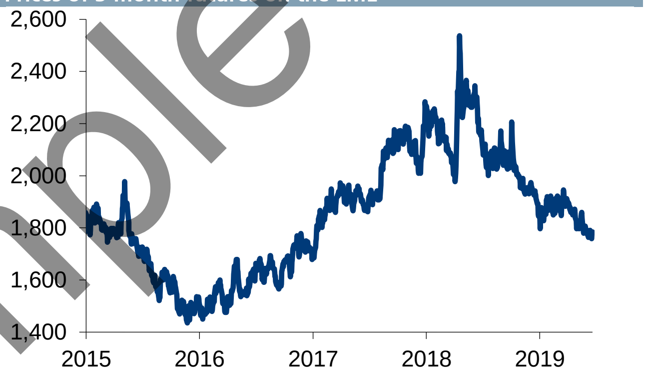
Source: Intesa Sanpaolo chart from Bloomberg data

Stock-to-global consumption ratio



Source: Intesa Sanpaolo chart from LME, WBMS data

Prices of 3-month futures on the LME



Source: Intesa Sanpaolo chart from LME data

Nickel

Nickel recorded the best year-to-date performance among industrial metals thanks to its fundamentals, perceived as stronger than those of other non-ferrous metals. In fact, the market is expected to remain in structural deficit over the foreseeable future due to a resilient global demand for stainless steel and strengthening consumption from new applications, especially related to nickel-based batteries for electric vehicles and energy storage.

In the last semi-annual outlook published in May, the International Nickel Study Group (INSG) forecasts that the global nickel market will record a deficit of about 0.08 million tonnes in 2019, a fourth consecutive year of undersupply after posting a big deficit of 0.15 million tonnes in 2018 and a shortage of 0.11 million tonnes in 2017.

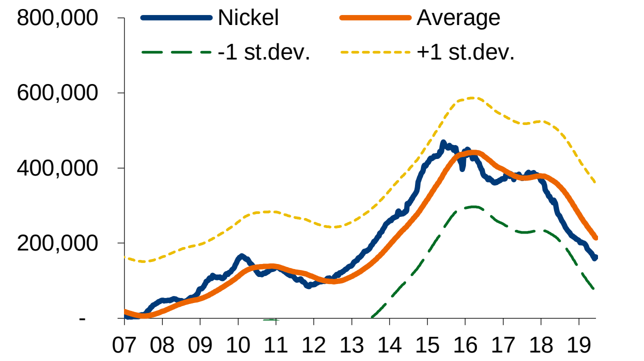
In fact, according to INSG estimates, global primary nickel production will grow from 2.18 million tonnes in 2018 to 2.38 million tonnes in 2019. However, we warn that the global nickel supply chain remains extremely vulnerable to the risk of further unexpected government interventions in the Philippines and Indonesia. World nickel usage is expected to grow from 2.33 million tonnes in 2018 to 2.46 million tonnes in 2019.

The decline in LME stocks has continued over the recent months. Inventories reached the lowest level in more than six years and the ratio between stocks and consumption is now at the lowest level since early 2013, confirming that the market is tight.

In our baseline scenario, we forecast an average nickel price of USD 12,500 for 3Q19 and 4Q19 and an average nickel price of about USD 13,000 in 2020, assuming unchanged mining regulations in South-East Asia. Currently, we are more bullish on nickel prices than on other industrial metals due to its strong fundamentals and the ongoing technological changes affecting nickel demand on both physical and financial markets. As a matter of fact, nickel is benefitting from a strong interest from financial investors thanks to the electrification trend.

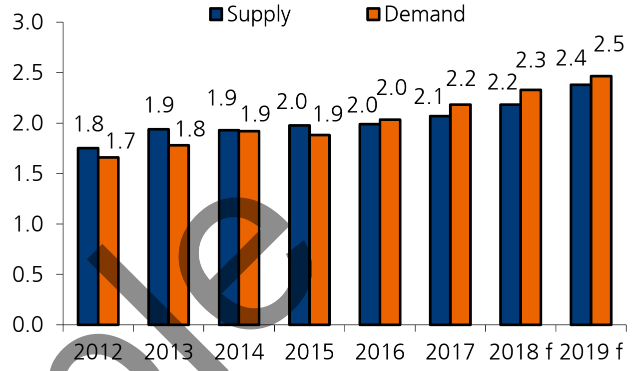
In the most bullish scenario of easing trade tensions we forecast that nickel prices could increase and trade in a higher range of about USD 13,000-14,000.

Inventories monitored by London Metal Exchange



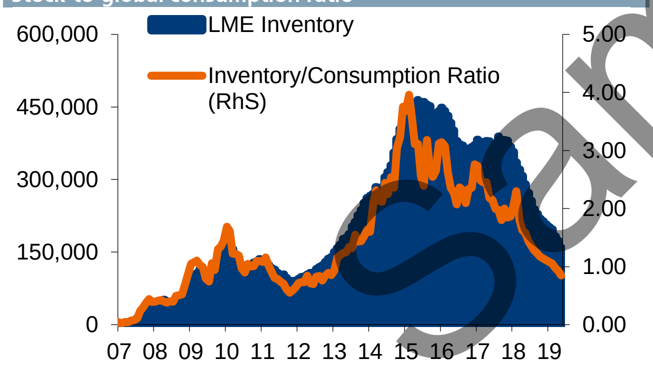
Source: Intesa Sanpaolo chart from Bloomberg data

INSG world supply and demand estimates



Source: Intesa Sanpaolo chart from Bloomberg data

Stock-to-global consumption ratio



Source: Intesa Sanpaolo chart from LME, WBMS data

Prices of 3-month futures on the LME

Source: Intesa Sanpaolo chart from LME data

Zinc

Zinc's year-to-date performance is flat, as the price increases posted in the first months of 2019 were offset by the heavy losses recorded since April. As for other industrial metals, swings in market sentiment have been the driving force behind zinc movements.

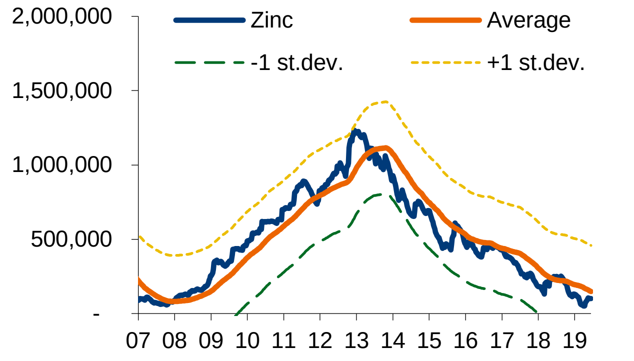
Zinc fundamentals are still positive this year, although weaker than in 2017 and 2018 due to the significant increase in global output planned this year. In the last semi-annual outlook published in May, the International Lead Zinc Study Group (ILZSG) forecasts pointed to a supply shortage of 121 thousand tonnes in 2019, the lowest deficit in four years.

According to ILZSG estimates, global primary zinc production will grow by 6.2% y/y to 13.5 million tonnes in 2019, driven mainly by an expected 29% increase in supplies from Australia. World refined zinc metal output may expand by 3.6% to 13.7 million tonnes in 2019, due to a 5.3% y/y growth in China. World zinc usage is expected to rise by a tiny 0.6% to 13.8 million tonnes in 2019.

Coherently, the data from warehouses monitored by the LME and SHFE Exchanges show that inventories are continuing their declining trend. The ratio between stocks and consumption, an indicator of the market's state of health, is still at the lowest level in more than 10 years.

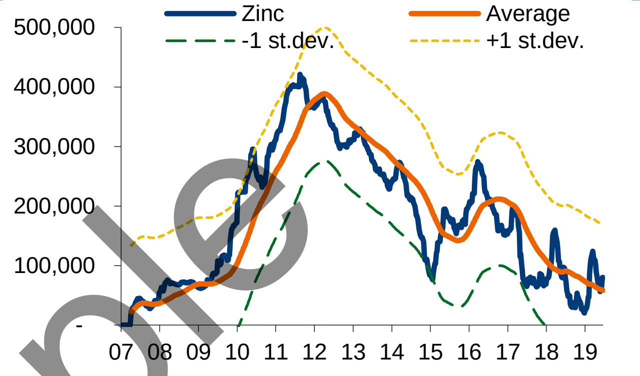
In our baseline scenario, zinc prices may trade around an average level of USD 2,500 per tonne from the 3Q19 up to the end of 2020, as in our opinion political concerns may constrain industrial metals' prices. In the most bullish scenario of easing trade tensions we forecast that zinc prices could increase and trade in a higher range of about USD 2,800-3,000.

Inventories monitored by London Metal Exchange



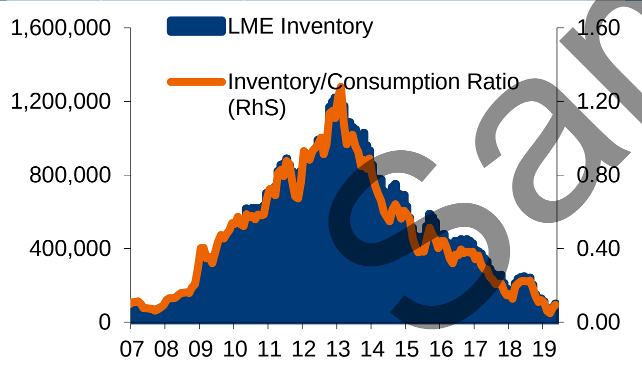
Source: Intesa Sanpaolo chart from Bloomberg data

Inventories monitored by Shanghai Futures Exchange



Source: Intesa Sanpaolo chart from Bloomberg data

Stock-to-global consumption ratio



Source: Intesa Sanpaolo chart from LME, WBMS data

Prices of 3-month futures on the LME

Source: Intesa Sanpaolo chart from LME data

Lead

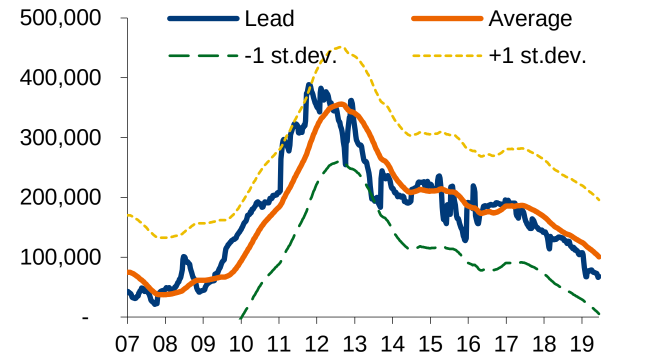
Lead fundamentals are the weakest in the industrial metals' complex. According to the latest figures published in May by the ILZSG, the lead market will come back in surplus after two years of deficit. The oversupply is estimated at 71 thousand tonnes in 2019.

According to ILZSG estimates, global primary lead production will grow by 1.8% y/y to 4.8 million tonnes in 2019, driven mainly by an expected increase in supplies from China and India. World refined lead metal output may expand by 2.5% to 11.9 million tonnes in 2019 because of a 14% y/y increase in Australia. World lead usage is expected to rise by 1.2% to 11.9 million tonnes in 2019.

The data from warehouses monitored by the main commodity Exchanges show that inventories fell at the LME network but rose at the SHFE. The ratio between stocks and consumption, an indicator of the market's state of health, is about stable and close to the lowest level in more than 10 years.

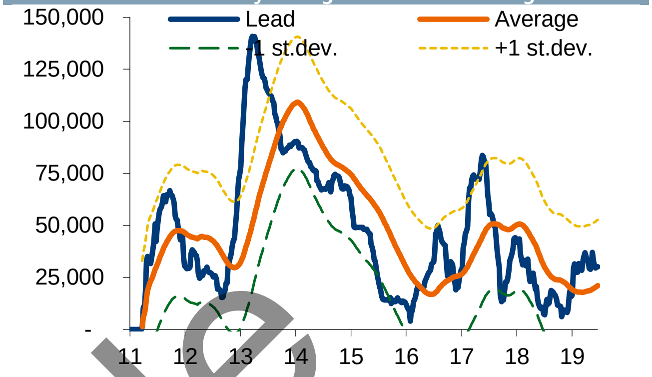
In our baseline scenario, lead prices may trade around an average level of USD 1,800 per tonne from the 3Q19 up to the end of 2020, as in our opinion political concerns may limit industrial metals' prices. In the most bullish scenario of easing trade tensions we forecast that lead prices could moderately increase and trade in a higher range of about USD 1,900-2,000.

Inventories monitored by London Metal Exchange



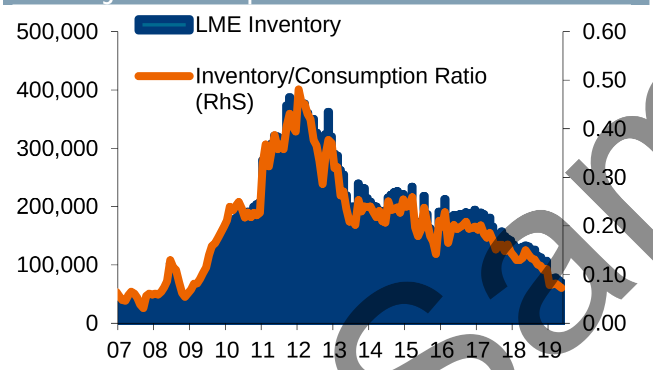
Source: Intesa Sanpaolo chart from Bloomberg data

Inventories monitored by Shanghai Futures Exchange



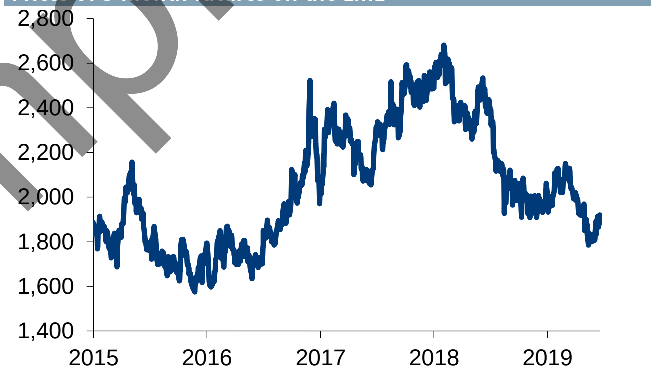
Source: Intesa Sanpaolo chart from Bloomberg data

Stock-to-global consumption ratio



Source: Intesa Sanpaolo chart from LME, WBMS data

Prices of 3-month futures on the LME



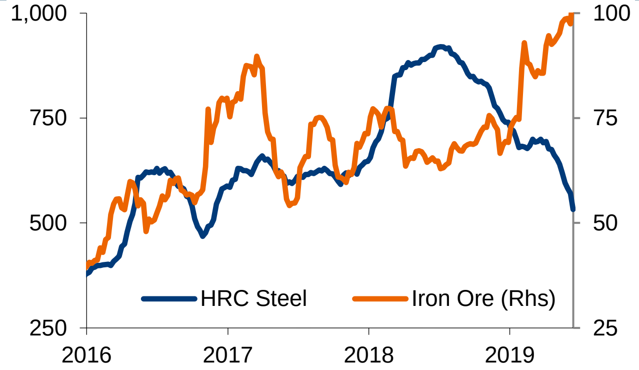
Source: Intesa Sanpaolo chart from LME data

Iron ore and steel sector

In our baseline scenario for iron ore, taking as a benchmark the one-month future contract listed on the Singapore Exchange, based on a basket of reference prices published by The Steel Index, we estimate an average price of USD 90 per tonne for 3Q19, an average price of USD 85 per tonne for 4Q19 and an average price of USD 82 in 2020. We expect that Australian supply will respond to high prices, easing the current market tightness. Moreover, despite high prices, stocks at Chinese ports remain high.

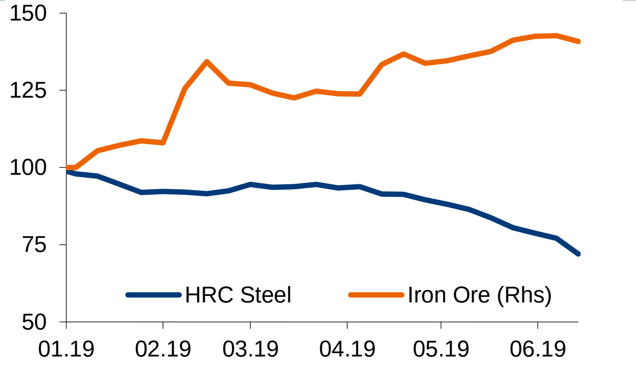
We see a stronger than expected increase in exports from Australia and Brazil and a deeper than expected slowdown in steel production in China as the main downside risks for our forecasts.

Steel and iron ore prices (right-hand scale) in absolute terms…



Note: Steel= TSI U.S.A Domestic Hot Rolled Coil (FOB Midwest mill) in USD/ton. Iron ore= 1-month futures contract listed on the Singapore Exchange in USD/tonne. Source: Intesa Sanpaolo chart from The Steel Index (TSI) figures

… and YTD returns (Dec. 2018=100)



Source: Intesa Sanpaolo chart from The Steel Index figures and Singapore Exchange

Concerning the steel sector, we forecast a decline in U.S. steel prices, while European benchmarks are forecast to remain about flat.

We consider as a benchmark for U.S. steel the index published by The Steel Index, calculated as a weighted average of the prices paid for U.S. hot-rolled coil. We now estimate an average price of USD 500 per tonne for 3Q19 and an average price of USD 550 for the whole 2020. In our baseline model, U.S. steel prices should return to a lower average, as both domestic output and imports are expected to increase over the next quarters.

We consider the new LME contracts on scrap and rebar as a benchmark for European steel. We now estimate for LME scrap an average price of USD 300 per tonne for 3Q19 and the same average in 2020. We envisage for LME rebar an average price of USD 468 per tonne for 3Q19 and of USD 463 for the whole 2020. In fact, European prices are expected to remain close to the current depressed levels amid oversupply and weak domestic demand.

At a global level, we see the future balance of the Chinese market as a significant factor of uncertainty. In particular, in the event of worsening Chinese economic growth, a slowdown in the country's steel demand would lead to an increase in Chinese exports, with clear downside effects on international prices.

Chinese exports of steel in millions of tonnes

Source: Intesa Sanpaolo chart from Bloomberg data

Forecast prices of industrial metals						
As at 17.06.2019		3Q19	4Q19	2019	2020	2021
LMCADS03 Comdty	LME COPPER 3M	6,000	6,000	6,079	6,000	6,300
LMAHDS03 Comdty	LME ALUMINIUM 3M	1,800	1,800	1,823	1,800	1,920
LMNIDS03 Comdty	LME NICKEL 3M	12,500	12,500	12,416	13,000	14,000
LMZSDS03 Comdty	LME ZINC 3M	2,500	2,500	2,578	2,500	2,600
LMPBDS03 Comdty	LME LEAD 3M	1,800	1,800	1,882	1,800	1,880
LMSNDS03 Comdty	LME TIN 3M	19,500	19,500	19,894	19,500	19,750
SCO1 Comdty	SGX IRON ORE	90	85	89.1	82.0	77.0
NASS000C Index	TSI US HRC STEEL	500	530	584	550	550
JBO1 Comdty	LME SCRAP	300	300	303	300	300
JBP1 Comdty	LME REBAR	468	465	469	463	460

Note: Iron ore= 1-month futures contract listed on the Singapore Exchange and based on a basket of reference prices published by The Steel Index. Steel= The Steel Index, index calculated as the weighted average of prices paid for US hot rolled coil steel transactions. Source: Intesa Sanpaolo estimates

Agricultural commodities: an effective diversification tool

This year, agricultural goods proved their effectiveness as a diversification tool in financial portfolios. In most cases, cereals and softs' performances reflect the underlying supply and demand fundamentals and expectations about weather conditions. Softs' prices, in particular, are in most cases little influenced by concerns related to the U.S.-China trade war and are therefore less vulnerable to the frequent swings of market sentiment between risk-on and risk-off.

So far this year, performances in the agricultural complex have been mixed: corn and wheat recorded a good price rally in 2Q19 amid unusually unfavourable weather conditions in most areas, while soybeans were little changed amid ongoing concerns about the U.S.-China trade war.

Among soft commodities, cocoa and sugar have been positive so far this year, while coffee is still recording negative performances. In particular, Arabica prices sank to the lowest level in 13 years on the back of concerns about an abundant Brazilian crop.

In general, agricultural goods proved their effectiveness as a diversification tool in financial portfolios. In most cases, cereals and softs' performances reflect the underlying supply and demand fundamentals, whose expectations are heavily affected by forecasts about weather conditions. Softs' prices, in particular, are in most cases only marginally influenced by concerns related to the U.S.-China trade war and are therefore less vulnerable to the frequent swings of market sentiment between risk-on and risk-off.

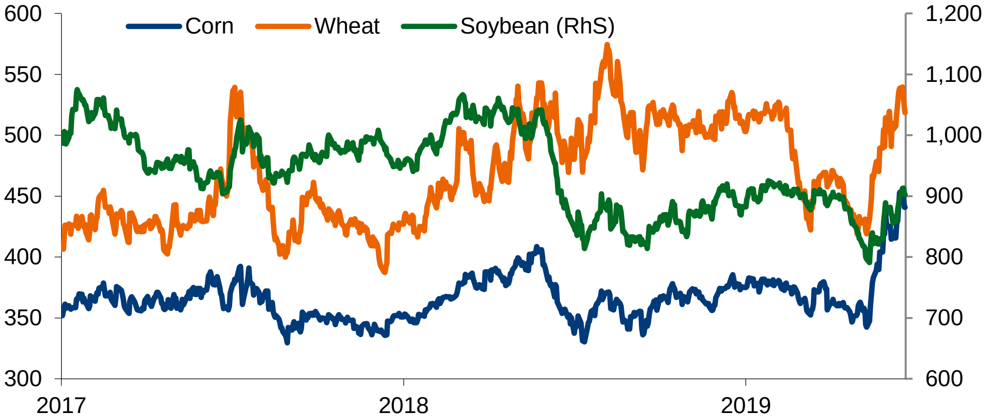
Over the past quarters, the most serious threats to cereals' crops were dry weather in South America during the southern hemisphere's summer and unusually wet weather in North America during the northern hemisphere's spring. In particular, the U.S. corn belt suffered from prolonged floods which delayed (and in most cases derailed) planting.

During the next months, we expect that volatility will remain a prominent market feature in the agricultural complex. Especially cereal prices may be heavily influenced by expectations about weather conditions. So far, adverse weather in the U.S. is supporting corn, wheat and soybean prices. However, the rapid diffusion of the African swine fever in China could lead to more downward revisions to estimates about global animal feeding and represents the main threat to our baseline scenario.

In our scenario, characterized by ongoing political tensions and the threat of a worse-than-expected economic slowdown, softs could in fact come back in the spotlight as an interesting diversification tool for investors.

We consider the futures listed on the Chicago Board of Trade for corn (CBOT Corn), wheat (CBOT Wheat) and soybeans (CBOT Soybean) as benchmarks for cereals, while our benchmarks for coffee are the Arabica futures listed in New York on the NYB-ICE Exchange and the Robusta futures listed in London on the ICE Exchange.

Corn, wheat and soybean prices (right-hand scale), in dollar cents per bushel



Source: Intesa Sanpaolo chart from Chicago Board of Trade data

Corn

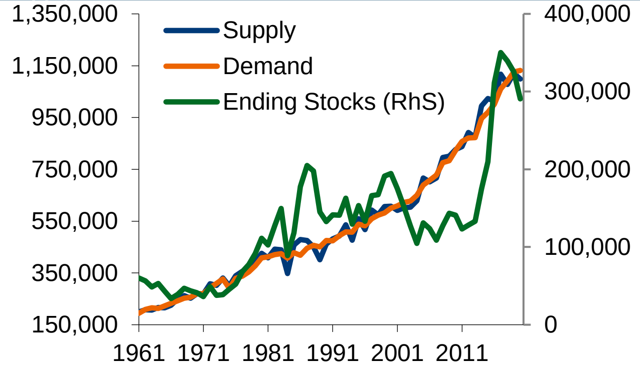
So far this year, corn has been the cereal most negatively affected by adverse weather conditions. The global corn market is now expected to record a large deficit in the 2019/20 season. It would be the third consecutive year of deficit and the widest since 1988/89. As a result, the stock-to-consumption ratio, an indicator of how well supplied the market is, should decrease further, reaching the lowest level since the 2014/15 season.

The monthly World Agricultural Supply and Demand Estimates (WASDE) report, published by the U.S. Department of Agriculture (USDA) in June, estimates that in the 2019/20 season global corn production should decrease by 1.9% y/y, while global consumption is expected to remain about stable at an historical high. In volume terms, the global production of corn is forecast to decrease to 1,099 million tonnes (revised downwards from 1,134 million tonnes last month). Global consumption is expected to remain stable at 1,134 million tonnes (vs. the first estimate of 1,145 million tonnes formulated in May).

Ending stocks are thus expected to decline by 10.7% y/y, reaching 291 million tonnes (revised downwards from 315 million tonnes in the first estimate published in May). Consequently, the stock-to-consumption ratio should fall to 25.6% (from 27.5% expected last month) from 38.7% in the previous season.

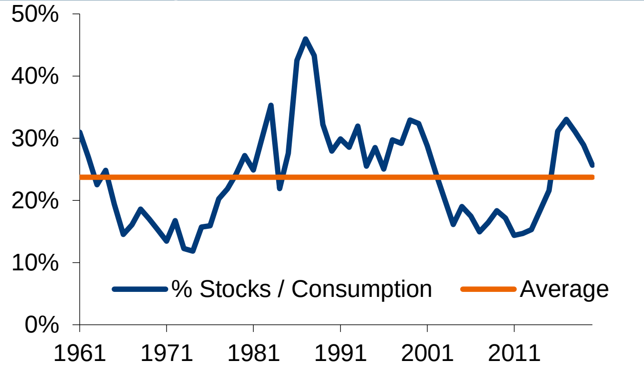
Currently, we estimate an average price of USD 450 cents a bushel for 3Q19 and of USD 480 cents for 2020. In fact, we expect corn to trade most of the time in the USD 400-500 cents range. In the short-term, the main themes on the corn market are weather conditions in the biggest producing regions and distortions related to U.S. subsidies to the farmers negatively affected by lower Chinese imports. In the longer term, concerns about global demand could prevail, especially if the epidemic of African swine fever in China is not contained.

Supply and demand (in thousand tonnes)



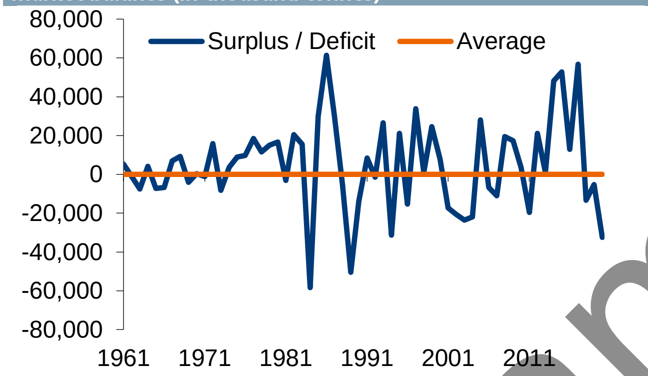
Source: Intesa Sanpaolo chart from USDA data

Stock-to-consumption ratio (%)



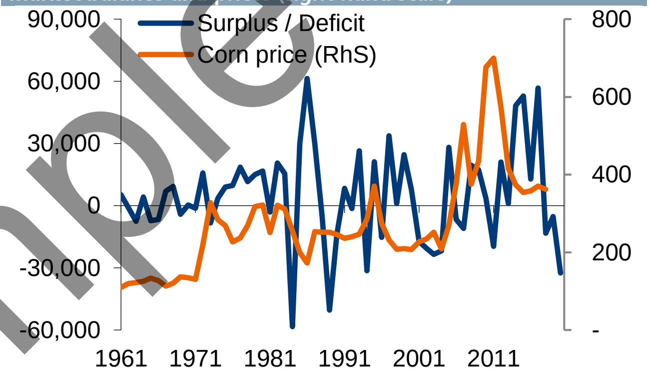
Source: Intesa Sanpaolo chart from USDA data

Market balance (in thousand tonnes)



Source: Intesa Sanpaolo chart from USDA data

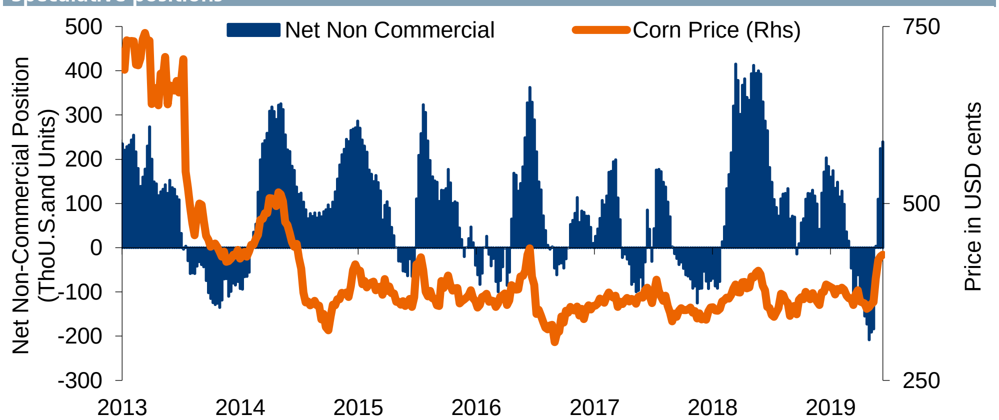
Market balance and prices (right-hand scale)



Source: Intesa Sanpaolo chart from USDA data

According to data from the U.S. CFTC, the net non-commercial positions held by money managers and investors recorded huge swings over the past months. Speculators are now net long and their net exposure is the widest since January due to weather concerns and bullish revisions to USDA estimates.

Speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC data

Wheat

In the 2019/20 season, the global wheat market is expected to come back in surplus, after recording its first deficit in six years in the previous season, as global supplies are forecast to grow quicker than total demand. Moreover, the surplus would be the widest since the 2015/16 season. The stock-to-consumption ratio may therefore increase to the second-highest level ever recorded, or the highest level since the season 1968/69.

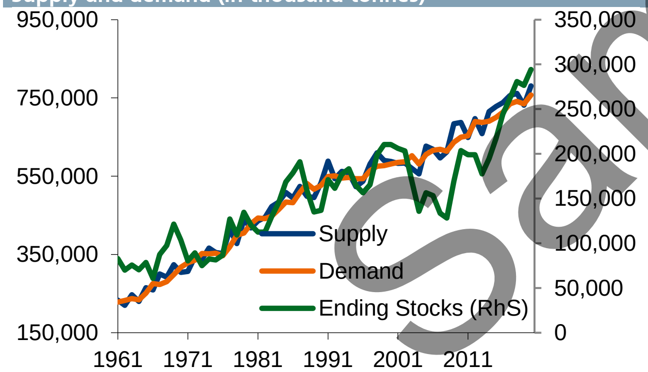
In the WASDE report for June, global wheat consumption is expected to expand by 3.7% y/y to 763 million tonnes (up from 760 million tonnes in the first estimate published in May), a new historical record and the highest level since the 2017/18 season.

The USDA estimates that the 2019/20 season may see a 6.7% y/y increase in global wheat production to 781 million tonnes (revised upwards from 778 million tonnes in the first estimate of May), also a new historical record and the highest level since the 2017/18 season.

Ending stocks are thus expected to increase by 6.4% y/y to 294 million tonnes (revised upwards from 293 million tonnes in May), a record high. The stock-to-consumption ratio is therefore forecast to widen to 38.6% in 2018/19 (unchanged from May), the highest ratio in more than 50 years, from 37.6% in the 2018/19 season.

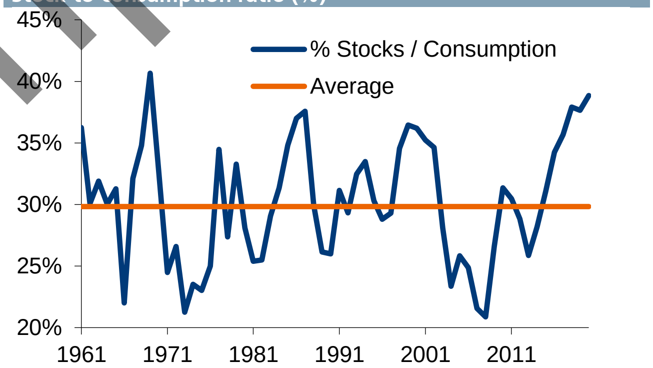
In our baseline scenario, we estimate an average price of USD 500 cents a bushel for 3Q19 and the same average price for 2020. We think wheat prices are well supported by adverse weather conditions in the U.S., as both acreage and yields may be negatively affected by wet and cooler than usual conditions. Downside threats weighting on our forecasts are the risks of more downward revisions to consumption estimates and the level of global inventory well above its historical average both in absolute terms and relative to world consumption.

Supply and demand (in thousand tonnes)



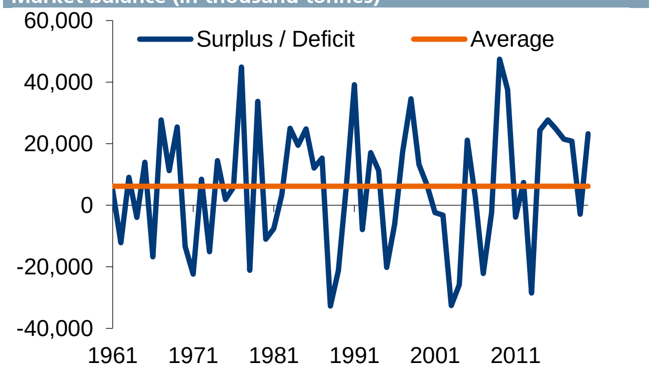
Source: Intesa Sanpaolo chart from USDA data

Stock-to-consumption ratio (%)



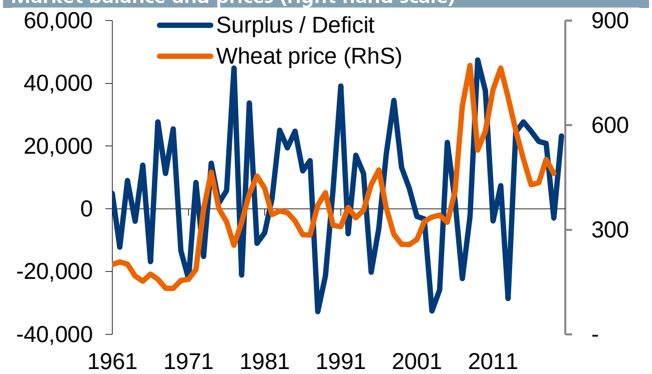
Source: Intesa Sanpaolo chart from USDA data

Market balance (in thousand tonnes)



Source: Intesa Sanpaolo chart from USDA data

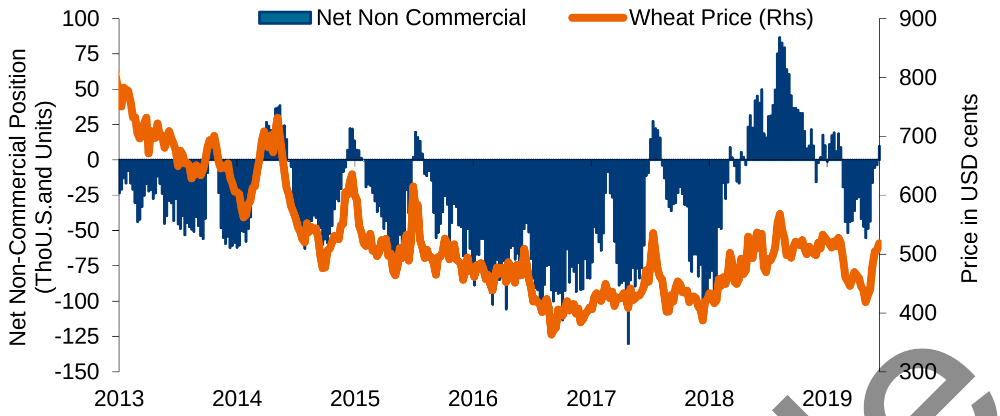
Market balance and prices (right-hand scale)



Source: Intesa Sanpaolo chart from USDA data

The speculative positions remain net short, but net levels are now closer to neutrality as the price rally triggered short covering. We expect that speculative positions will continue to be driven by market prices reflecting the physical market's fundamentals. In fact, wheat is less exposed than corn and soybeans to the trade disputes between the U.S. and China.

Speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC data

Soybeans

So far, soybeans have been the cereal most hit by trade tensions between China and the U.S.: China is the world's biggest consumer and importer of soybeans and the U.S. were China's main supplier. During the past months, Brazilian soybeans gained market shares on the Chinese markets. Even in the rosiest scenario of easing trade tensions, we think that China's purchases from Brazil will remain structurally higher than during the previous years, as in our opinion the global supply chain has been permanently altered.

In its June report, the USDA forecasts that soybean production may decline by 1.8% y/y to 355 million tonnes (slightly down from the first estimate of 356 million tonnes formulated in May).

Global consumption is expected to grow by 2.3% y/y and hit a new record of 355 million tonnes (unchanged from May).

Consequently, global inventories are expected to decrease by 0.1% y/y to 113 million tonnes in the 2018/19 season (little changed from last month). The stock-to-consumption ratio is thus expected to decrease to 31.7% (revised downwards from 31.8%) vs. 32.5% recorded in the previous season.

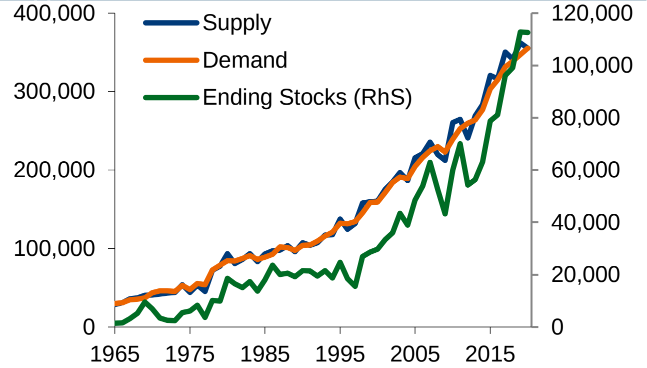
Regarding soybean products, the fundamentals for both soybean meal and soybean oil remain constructive in the 2019/20 season.

The stock-to-consumption ratio for soybean meal is expected to fall to 5.1% in 2019/20 from 5.4% recorded in the previous two seasons. In June, the USDA estimated that ending stocks should decrease by 3.6% to 12 million tonnes in the 2019/20 season (unchanged from May).

The stock-to-consumption ratio for soybean oil is also expected to decline 6.1% in 2019/20 from 6.4% in the previous season. The USDA estimates that ending stocks will decline to 3.5 million tonnes in the 2019/20 season (unchanged) from 3.6 million tonnes in the 2018/19 season.

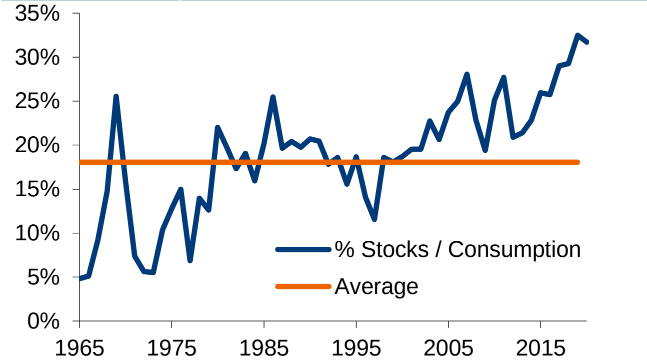
Currently, we estimate an average price for soybeans of USD 900 cents a bushel for 3Q19 and the same level for 2020. Trade tensions may continue to fuel volatility in soybean prices, as in the short term the market will focus on developments in the trade war, uncertainty about U.S. soybeans' yields and distortions related to U.S. subsidies to farmers.

Supply and demand (in thousand tonnes)



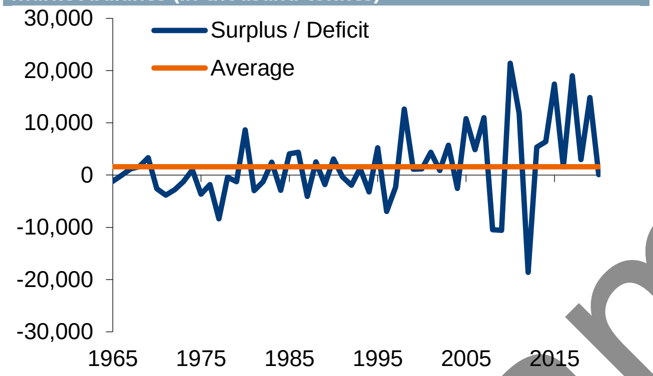
Source: Intesa Sanpaolo chart from USDA data

Stock-to-consumption ratio (%)



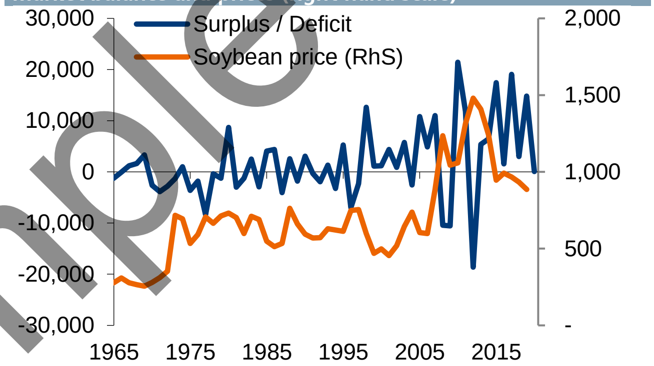
Source: Intesa Sanpaolo chart from USDA data

Market balance (in thousand tonnes)



Source: Intesa Sanpaolo chart from USDA data

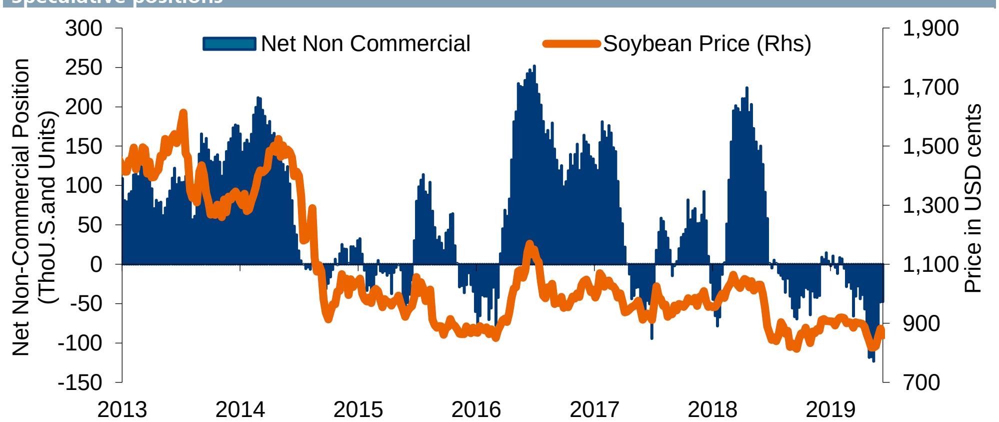
Market balance and prices (right-hand scale)



Source: Intesa Sanpaolo chart from USDA data

U.S. CFTC figures show that money managers and hedge funds have further reduced their financial exposures towards soybeans due to fears related to political risks and they remain net short on soybeans. We expect that speculative positions will still be net short over the next months, even if weather concerns could fuel limited movements of short covering.

Speculative positions



Source: Intesa Sanpaolo chart from U.S. CFTC data

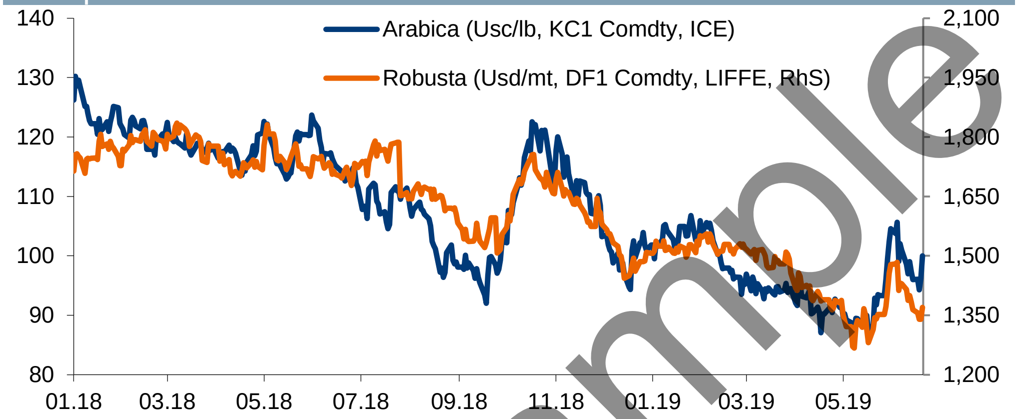
Coffee

Over the past quarters, Arabica and Robusta prices recorded significant swings. During the first four months of 2019, downwards pressures prevailed amid concerns about a very well supplied market. In fact, the global coffee market had recorded big surpluses both in the 2017/18 (an oversupply of 4.2 million bags vs. a total output of 165.5 million bags) and the 2018/19 seasons (an oversupply of 3.4 million bags vs. a total output of 168.0 million bags, a new record high).

Moreover, consensus estimates are pointing toward a big crop in Brazil in the 2019/20 season: despite Arabica trees are entering in their off-year in the biennial production cycle, probably this crop will be the highest ever recorded in the low phase of the production cycle.

As a consequence, Arabica traded in mid-April at the lowest levels in 13 years.

Coffee prices



Source: Intesa Sanpaolo chart from Bloomberg data

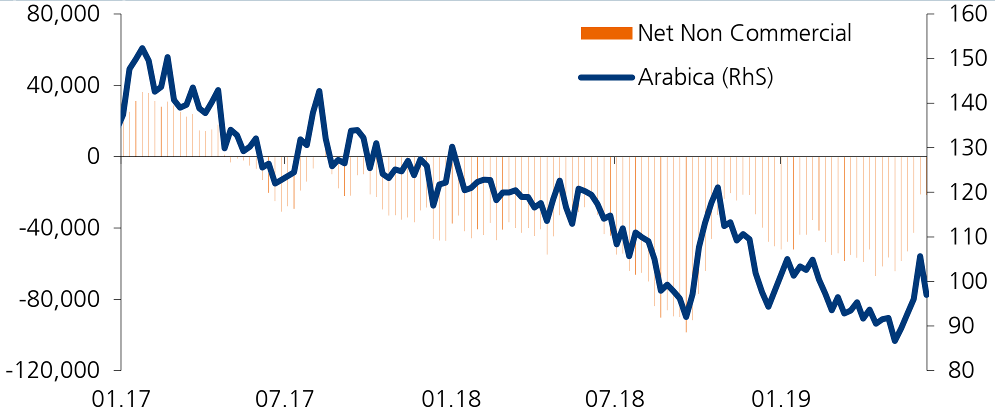
Then, optimism prevailed, and coffee prices rose, with Arabica leading Robusta amid weather-related risks and an appreciating Brazilian Real.

Coffee fundamentals marginally improved as the second official estimate of the Brazilian coffee crop, published on May 16th by the Brazilian Companhia Nacional de Abastecimento (CONAB), showed that the 2019/20 crop will probably be lower than earlier expected. CONAB now expects that Brazil may produce 50.92 million bags in the current season vs. a first estimate published in January of about 52.5 million bags (the central point of the CONAB's 50.5-54.5 million bag range). This would correspond to a 17.5% y/y drop in total coffee output.

CONAB now expects that Brazil may produce 37.0 million bags of Arabica in the current season, close to the central point of the CONAB's first estimate of a 36.1-38.2 million bag range. It would correspond to a 22% y/y drop in Arabica output. Still, it would be the second highest level ever recorded for the Brazilian Arabica harvest in an off-year after the 2013/14 season.

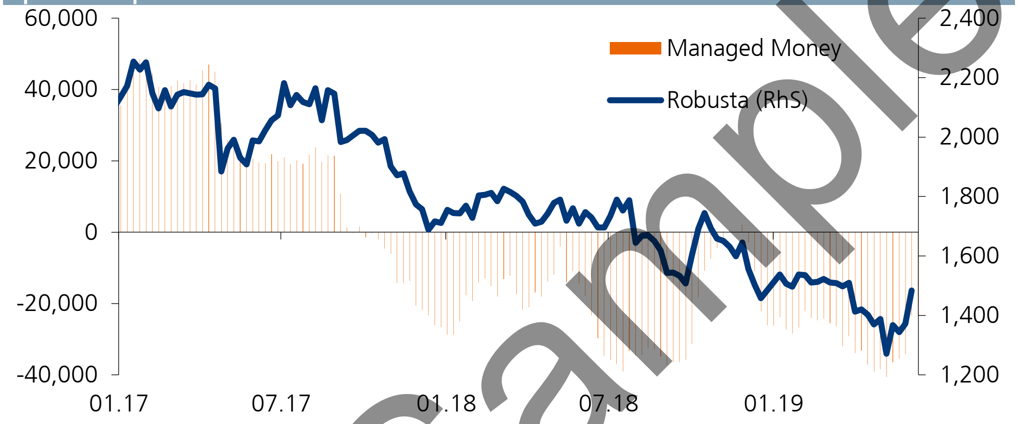
CONAB now estimates that Brazil may produce 14.2 million bags of Robusta in the 2019/20 season, well below CONAB's first estimate of a 14.4-16.3 million bag range. It would correspond to a 2% y/y drop in Robusta output. Still, it would be the second highest level ever recorded for the Brazilian Robusta harvest after the 2018/19 season.

Speculative positions on Arabica



Source: Intesa Sanpaolo chart from U.S. CFTC data

Speculative positions on Robusta



Source: Intesa Sanpaolo chart from U.S. CFTC data

Data from the U.S. CFTC show that price swings have been amplified by speculative positions, as money managers and hedge funds are very interested in a market trading at low historical levels and relatively isolated within trade tensions and global political concerns.

Currently, we estimate an average price for Arabica of USD 100 cents in 3Q19 and of USD 110 cents for 2020, and an average price for Robusta of USD 1,400 cents in 3Q19 and of USD 1,525 cents for 2020. We are very positive on coffee as according to our estimates market prices lower than USD 100 on Arabica do not fully cover production costs in several areas. The biggest threats weighting on our baseline outlook are weather-related risks and unexpected currency movements, especially related to the Brazilian Real. In fact, forex dynamics affect the competitiveness of the world's biggest producers and often influence export flows.

Price forecasts for cereals and coffee

As at 17.06.2019		3Q19	4Q19	2019	2020	2021
C 1 Comdty	CBOT CORN	450	460	421	480	490
W 1 Comdty	CBOT WHEAT	500	500	494	500	500
S 1 Comdty	CBOT SOYBEAN	900	900	892	900	940
KC1 Comdty	NYB-ICE ARABICA COFFEE	100	105	100	110	115
DF1 Comdty	LIFFE ROBUSTA COFFEE	1,400	1,450	1,437	1,525	1,600
SM1 Comdty	CBOT SOYBEAN MEAL	310	310	310	300	300
BO1 Comdty	CBOT SOYBEAN OIL	28.0	28.0	28.4	28.0	28.0

Source: Intesa Sanpaolo estimates

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Appendix

Analyst Certification

The financial analysts who prepared this report, and whose names and roles appear on the first page, certify that:

(1) The views expressed on companies mentioned herein accurately reflect independent, fair and balanced personal views;

(2) No direct or indirect compensation has been or will be received in exchange for any views expressed.

Specific disclosures

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Valuation Methodology

This document has been prepared in accordance with the following method.

Macroeconomic Data

Comments on macroeconomic data are prepared based on macroeconomic and market news and data available via information providers such as Bloomberg and Thomson Reuters-Datastream. Macroeconomic and interest rate forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated econometric models. Forecasts are obtained using analyses of historical-statistical data series made available by the leading data providers and also on the basis of consensus data, taking account of appropriate connections between them.

Forecasts in the Energy Sector

Comments on the Energy Sector are prepared based on macroeconomic and market news and data available via information providers such as Bloomberg and Thomson Reuters-Datastream. Unless otherwise stated, consensus estimates come from the leading international energy Agencies, primarily the IEA (International Energy Agency – which deals with this sector on a global scale), the EIA (Energy Information Administration – an institute that deals specifically with the US energy sector) and OPEC. Forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated models.

Forecasts in the Metals Sector

Comments on the Metals Sector are prepared based on macroeconomic and market news and data available via information providers such as Bloomberg and Thomson Reuters-Datastream.

Unless otherwise specified consensus estimates on precious metals come mainly from GFMS, the long-established forecasting agency based in London. The forecasts cover gold, silver, platinum and palladium. Forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated models.

Unless otherwise stated, consensus estimates for industrial metals come mainly from Brook Hunt, an independent forecasting agency which has prepared statistics and predictions on metals and minerals since 1975, and from the World Bureau of Metal Statistics (WBMS), an independent research body on the global market of industrial metals which publishes a series of monthly, quarterly and annual statistical analyses. Forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated models.

Forecasts in the Agricultural Sector

Comments on the Agricultural Sector are prepared based on macroeconomic and market news and data available via information providers such as Bloomberg and Thomson Reuters-Datastream.

There are several consensus estimates on agricultural products. Each individual country has its own internal statistics agency that estimates and forecasts crops, production capacity, the product supply quantities and, above all, the amount of land available for cultivating a particular product, in both absolute and percentage terms.

At an international level, the main agencies are: the USDA (United States Department of Agriculture) which, in addition to providing data on the US territory, also deals in general with the grain industry worldwide through the FAS (Foreign Agricultural Service); the Economist Intelligence Unit of the Economist Group which deals with all agricultural products on a global scale; and CONAB (Companhia Nacional de Abastecimento), the Brazilian Government agency that deals with agriculture (with a particular focus on coffee) and which also provides some insight into the entire South America.

Forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated models.

Technical levels

Comments on technical levels are based on market news and data available via information providers such as Bloomberg and Thomson Reuters-Datastream. Interest rate technical level forecasts are prepared by the Intesa Sanpaolo Research Department, using dedicated technical models. Forecasts are obtained using analyses of historical-statistical data series made available by the leading data providers and also on the basis of consensus data, taking account of appropriate connections between them. There is also a further in-depth study linked to the choice of appropriate derivatives that best represent the sector or the specific commodities on which one intends to invest.

Recommendations

Negative Outlook: a Negative Outlook recommendation for a sector is a wide-ranging indication. It not only indicates deteriorating price conditions of the indices or futures that best represent the commodity in question (thus the reduction of a price performance), but it also implies the deterioration in the forecasts on production, weather and input supplies (like water or energy) that characterize these sectors more than other financial instruments.

Neutral Outlook: a Neutral Outlook recommendation for a sector is an indication that includes a multitude of aspects. It indicates that the combination of price forecasts of indices and futures and all the conditions of production, weather and input supplies (like water or energy) will lead to a sideways movement in prices or inventories or production capacity, recording, therefore, void or minimum performances for the sector under examination.

Positive Outlook: a Positive Outlook recommendation for a sector is an indication covering a wide range of areas. It not only indicates net improvements in price conditions of the indices or futures that best represent the commodity in question (thus a positive price performance), but it also implies the improvement in the forecasts on production, weather and input supplies (like water or energy) that characterize these sectors more than other financial instruments.

Frequency and validity of forecasts

Market indications refer to a short period of time (the same day or the following days, unless stated otherwise in the text). Forecasts are developed over a time span of between one week and 5 years (unless specified otherwise in the text) and have a maximum validity of three months.

Disclosure of potential conflicts of interest

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In particular, the description of the measures taken to manage interest and conflicts of interest – related to Articles 5 and 6 of the Commission Delegated Regulation (EU) 2016/958 of 9 March 2016 supplementing Regulation (EU) No. 596/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the technical arrangements for objective presentation of investment recommendations or other information recommending or suggesting an investment strategy and for disclosure of particular interests or indications of conflicts of interest as subsequently amended and supplemented, the FINRA Rule 2241, as well as the FCA Conduct of Business Sourcebook rules COBS 12.4 - between the Intesa Sanpaolo Banking Group and issuers of financial instruments, and their group companies, and referred to in research products produced by analysts at Intesa Sanpaolo S.p.A. is available in the "Rules for Research " and in the extract of the "Corporate model on the management of inside information and conflicts of interest" published on the website of Intesa Sanpaolo S.p.A., webpage https://www.group.intesasanpaolo.com/scriptIsir0/si09/studi/eng_doc_governance.jsp along with a summary sheet on the website of Banca IMI S.p.A. webpage https://www.bancaimi.com/en/bancaimi/chisiamo/documentazione/normative.html. This documentation is available to the recipient of this research upon making a written request to the Compliance Department, Intesa Sanpaolo S.p.A., Via Hoepli, 10 – 20121 Milan – Italy.

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