STILL HEADING DOWN:
EMERGING STOCK MARKETPLACES AND COMMODITIES
 October 7, 2013

The Notorious B.I.G. "Mo Money Mo Problems" song raps:
"What's goin on?
I don't know what, they want from me
It's like the more money we come across
The more problems we see"

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CONCLUSION

From the end of the Goldilocks Era in mid-2007 to the depths of the worldwide economic crisis in late 2008 and early 2009 and onward through the ensuing global recovery up to now, "overall" emerging stock marketplaces and commodities "in general" generally have traveled together. The emerging stock marketplace and commodities domains have been in a sideways to bearish trend since their spring 2011 peaks. In the wake of Federal Reserve Board tapering talk, they established interim lows in late June 2013. Yet despite the notable rally since then, in recent weeks they probably have resumed their interrelated downtrends. These bear moves probably will continue. Within the commodities realm, the tumble of the petroleum complex is especially noteworthy.

TABLE TALK

In the table below, Morgan Stanley's "MSCI Emerging Stock Markets Index" (MXEF on Bloomberg) represents emerging stock marketplaces. For commodities "in general", review the broad S+P Goldman Sachs Commodity Index.

The bull and bear adventures and timing relationships between emerging stocks and the broad GSCI are not perfect. However, in recent years they have been rather close. Since the peaks in spring 2011, note the pattern of lower and lower highs as the downtrends have proceeded.

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Of course not all emerging stock marketplaces are alike or move in the same fashion. Not all commodities voyage in the same direction, or in the same direction at around the same time.

In various ways, a great number of variables influence emerging stock marketplaces and assorted commodities. Emerging marketplace equities and commodities are not financial islands. Trends in stock marketplaces of advanced nations such as the United States (picture the S+P 500) entangle with those of emerging marketplaces. Levels and movements in interest rate territories, whether in emerging lands or in advanced ones such as the United States, influence both international stock marketplaces and commodities. Currency fluctuations, especially US dollar ones, likewise are very relevant to emerging and developed nation equities as well as commodities in general. The current US government spending and debt limit showdown has worldwide implications.

Despite the deficit spending actions of politicians around the globe and the highly accommodative monetary actions by central bankers (such as the Federal Reserve Board's sustained rock-bottom Federal Funds rate and its gargantuan money printing festivals) emerging marketplace equities (unlike the S+P 500 so far) and commodities gradually have fallen lower.

What do the sideways to down movements in emerging stock marketplaces and commodities suggest for worldwide economic growth? Aren't emerging nations supposed to be one of the key engines of prosperity for the rest of the world? These emerging nations in general probably have less robust economic growth than many believe. The sideways to down trends in emerging stocks and commodities, particularly the slump in recent weeks, warns that the divergence between them and the S+P 500 probably will not continue for much longer. In that regard, note the high in the S+P 500 to date was on 9/19/13 at 1730, alongside one in the MXEF that day at 1028; the broad GSCI top around 675 on 8/28/13 preceded these by about three weeks.

Given China's importance to worldwide economic growth and to commodities in general, the table includes China's Shanghai Composite stock index. Admittedly, the Shanghai Composite does not fully reflect all China-related equities. For example, Hong Kong's stock index is relevant. And clearly the Shanghai Composite's downtrend does not mirror China's real GDP growth. Yet China's stock stumble, particularly since mid-2011 (and arguably over a year or so before that) nevertheless aligns itself with drops in emerging marketplace stocks in general and in the broad GSCI. Perhaps China's past growth trajectory and its prospects are not as glorious as many assert. See "Another Marketplace Tapering Tale: the China Story" (9/9/13).

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	Emerging Stocks/ MXEF	**China Stocks/Shanghai Composite**	**Broad GSCI**
2008/2009 Major Low	446 (10/28/08) 471 (3/3/09)	1665 (10/28/08)	306 (2/19/09)

[From several years ago up to the present, many marketplace turns in the S+P 500 have occurred around the time of those in the MXEF and the broad GSCI. The S+P 500 established a major low on 3/6/09 at 667. Recall that the S+P 500's major peak on 10/11/07 at 1576 and its subsequent final top at 1253 on 5/19/08 neighbored MXEF pinnacles at 1345 on 11/1/07 and 1253 on 5/19/08. In this timing context related to the final 2008 peaks in stocks, recall the broad GSCI's major summit at 894 on 7/3/08.]

Spring 2010 Top	1051 (4/15/10)	3181 (4/15/10)	556 (5/3/10)

[Highs in the Shanghai Composite at 8/4/09's 3478 and 11/24/09's 3361 preceded its 2010 elevation. S+P 500 high 4/26/10 at 1220.]

Spring/Summer 2010 Low	850 (5/25/10)	2320 (7/2/10)	459 (5/25/10)

[S+P 500 lows on 7/1/10 at 1011 and 8/27/10 at 1040.]

Spring 2011 Peak	1212 (4/27/11)	3067 (4/18/11)	762 (4/11+5/2)

[In the Shanghai Composite, a top on 11/11/10 at 3187 arrived before April 2011's plateau. The S+P 500 attained an important interim top at 1371 on 5/2/11.

Since spring 2011, the S+P 500 of course has achieved notable new peaks, whereas the MXEF and the broad GSCI have not. Yet even since spring 2011, many key turns in the S+P 500 have taken place around the time of those in emerging stock marketplace s and commodities.]

	Emerging Stocks/ MXEF	China Stocks/Shanghai Composite	Broad GSCI
Autumn 2011 Bottom	824 (10/4/11)	2307 (10/24/11)	573 (10/4/11)

[Recall the S+P 500 trough at1075 on 10/4/11.]

Early 2012 Top	1085 (2/29/12)	2478 (2/27/12)	717 (3/1/12)

[The S+P 500 made a minor top 4/2/12 at 1422. The MXEF later reached an interim high on 9/14/12 at 1018, as did the S+P 500 that day at 1475. Compare the time of the GSCI's 699 high on 9/14/12. Keep in mind that these September 2012 elevations in the MXEF and the broad GSCI stood beneath their early 2012 ones.]

[Despite the worldwide economic revival since around early 2009, the MXEF not only has not come close to its 2007 major peak and never breached its May 2008 final top. Its January 2013 high at 1083 did not surpass its 2/29/12 one at 1085. The broad GSCI has not come close to its 2008 plateau.]

June 2012 Low	877 (6/4/12)	1960 (6/25/13)	556 (6/22/12)

[S+P 500 low 6/4/12 at 1267. Major low in US Treasury 10 year note 7/25/12 at 1.38 percent.]

[Note the sharp rise in the UST 10 year note yield from 11/16/12's 1.55pc, 12/6/12's 1.56pc, and especially 5/1/13's 1.61pc. The recent high is about 3.01pc (9/6/13).]

November 2012 Low	968 (11/16/12)	1950 (12/4/12)	622 (11/5/12)

[S+P 500 low 1343 on 11/16/12.]

Early 2013 Summit	1083 (1/3/13)	2445 (2/18/13)	682 (2/13/13)

[The MXEF made another high close to that one, on 5/9/13 at 1065. Compare the Shanghai Composite's one on 5/29/13 at 2334. Initial high in the S+P 500 was 5/22/13 at 1687.]

June 2013 Low	878 (6/25/13)	1850 (6/25/13)	605 (6/24/13)

[This GSCI bottom occurred slightly later than one at 596 on 4/18/13. S+P 500 low 6/24/13 at 1560.]

Recent High Late Summer 2013	1028 (9/19/13)	2270 (9/12/13)	675 (8/28/13)

[The S+P 500's high to date is 1730 on 9/19/13. A five percent fall gives about 1644, a 10pc one about 1557.]

PEEKS AT PETROLEUM

Petroleum constitutes an important part of the broad GSCI and many other commodity indices. The petroleum story and its supply/demand situation are important components for the emerging marketplace growth theme. However, note the late summer 2013 reversal of the petroleum bull move that began around a late June 2013 take-off point. In addition, the overall worldwide petroleum situation is bearish. Weakness in various corners of the oil marketplace in recent weeks suggests that commodities "in general" probably will continue to venture lower over the next few months. So what does the historically close association between trends in emerging stock marketplaces and commodities in general suggest? The renewed bear trend in petroleum since late summer 2013 indicates that the MXEF will continue to drift lower as well.

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Within the worldwide petroleum complex, scan the price action of several noteworthy crude and product members. They remain beneath their 2011 (or 2012 peaks), and thus in a sideways to down trend. After rallying in late June 2013 (compare the broad GSCI and the MXEF) they resumed their declines in late summer/early fall 2013.

Brent/North Sea crude oil (nearest futures continuation) established a major high on 12840 on 3/1/12. This generated a double top, for it rested only about one percent above the highs at 12702 on 4/11/11 and 12670 on 4/28/11. Its 2/8/13 high was 11917. Compare the timing of NYMEX crude oil tops. What about quite recently? Although Brent soared from 9967 on 6/24/13, it has fallen about ten dollars from its recent high on 8/28/13 at 11734.

What about NYMEX crude oil (nearest futures continuation)? Its summit is 5/2/11’s 11483. Several months ago, after making a low on 4/18/13 at 8561, this marketplace accelerated upward from 9267 on 6/24/13. Its recent high is 8/28/13’s 11224, the date of the Brent and broad GSCI tops.

Two key NYMEX crude oil intramarket spread relationships parallel this August 2013 peaking in flat price NYMEX crude oil. Increasing backwardation (or less contango) often is connected with a bull charge in outright (flat) prices. For example, note the NYMEX December 2013 less December 2014 crude oil spread. It made a trough on 4/16/13 at 130 backwardation. This spread rallied sharply, spiking up from 6/24/13’s 517. Note the day of its 1428 (over fourteen dollars a barrel) high- 8/28/13. It now is around nine dollars.

What about the current front two months spread, the actual November 2013 less December 2013 contracts? After peaking at 176 per barrel, it has cratered to around thirty cents.

The United States Gulf Coast regular gasoline and diesel marketplaces are crucial refined product benchmarks. The USGC regular gasoline (spot, cash) established a key pinnacle on 5/10/11 about 343.3. Gasoline made another top on 4/3/12 at 330.7, as well as one on 2/15/13 at 314.1. Note its 2013 slump after its rally from its 6/25/13 take-off point around 254.7. It reached a high on 7/12/13 at 298.5, and since has collapsed under its June 2013 floor, touching 244.5 on 10/2/13.

As for USGC diesel (ultralow sulfur), recall its 4/8/11 high at 334.7, as well as its tops close to but still under that one, 2/26/12’s 333.2 and 2/12/13’s 329.1. Note how that like USGC gasoline, USGC diesel flew higher after late June 2013 (from 6/26/13’s 280.2 low (which hovered above 4/17/13’s 272.0). It made a high on 8/28/13 at 318.4, but since has slipped to 10/1/13’s 288.2 depth.

The substantial decline in US Gulf Coast refining margin (“crack”) spreads since late 2012 arguably reflects a relatively weak American (and worldwide) economy. The USGC regular gasoline crack spread high (crude oil is NYMEX nearest futures continuation) was nearly $42 dollars per barrel (8/27/12 high at 4187, settlement basis versus NYMEX crude oil first futures continuation; 3990 on 10/5/12). It then made a lower high on 2/22/13 at $35.69; compare this first quarter 2013 top with that made in the MXEF (and Shanghai Composite) and the broad GSCI. This gasoline crack made a low at 1026 low on 6/27/13 (close to 12/13/12’s 1006). Yet despite soaring up to 8/21/13’s 1732 height, it has crashed down dramatically to around a dollar.

As for the USGC diesel (ultralow sulfur), recall its major high on 10/11/12 around 4610 (over 46 dollars per barrel). Like the gasoline crack (and the MXEF and broad GSCI), the USGC diesel crack made another high during first quarter 2013, at 4134 on 2/8/13. It collapsed to a low of 1792 on 7/10/13. Though the diesel versus crude oil refining margin rebounded to 2454 on 8/21/13 (compare the August 2013 high in the USGC gasoline crack), it has edged lower since then (10/2/13 low about 1934).

As a footnote to the weakness since around late August in the petroleum complex (including the NYMEX intramarket spreads and the USGC crack spreads, note gold's high 1428 on 8/28/13 (nearest futures continuation), which followed a late June 2013 low (6/28/13 at 1179).
As for the LME's base metal index (LMEX), keep in mind it remains under its minor high of 3226 reached 8/16/13.

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The supply/demand situation of the worldwide petroleum marketplace appears somewhat bearish.

According to the International Energy Agency, end 2Q13 industry-held OECD stocks represented 58 days of forward demand (Table 5, "Oil Market Report", 9/12/13; next release 10/11/13). OECD inventories built 8.0mm barrels in July, but there was a counter-seasonal draw of over 14.0mm barrels in August (page 1). However, OECD inventories, even if they have slipped a day (or even two) from the 58 day level of end 2Q13, are at least around normal.

What days coverage does the crucial US marketplace display? Based on Energy Information Agency data (9/27/13) total commercial inventory (crude and products combined) relative to recent consumption (the four week average of total products supplied, not estimated forward demand) equals 59.2 days coverage. The 1996-2012 end September days coverage average is 54.1 days, so 9/27/13's level is well above average. Also, the current total days coverage is fairly close to the record end September high for 1996-2012, September 2012's 61.8 days. The end October days coverage average is 52.7 days; the high for end October is 2012's 59.6 days.

Crude oil and various petroleum products of course may vary in their days coverage trends and apparent adequacy relative to demand. Nevertheless, in regard to the USGC gasoline and diesel crack spread collapses from around October 2012, keep in mind the lofty September and October 2012 days coverage for crude and products combined. Compare the recent 2013 collapses in crack spreads in regard to current days coverage (as well as September and October 2012's total days coverage).

As current US overall days coverage is thus on the high side, it currently therefore probably is so to some degree for the overall OECD as well. Euroilstock end August 2013 days coverage for crude and feedstocks was 44.2 days, a record high for the 1998-2013 period (no refining run data before 1998), and well beyond the end August average of 38.3 days.

It is challenging to estimate the levels and days coverage of non-OECD inventories. However, the sufficient OECD days coverage alongside the downward trend in key petroleum price signposts (especially Brent/North Sea) following their late summer 2013 highs suggests that non-OECD oil stockpiles probably are adequate.

According to IEA estimates, the call on OPEC crude oil has drifted lower. In 2012, the call was 30.4 million barrels per day, with 2013's 29.9mmbd (Table 1). However, the IEA states that July 2013 OPEC crude production was 30.8mmbd, with August 2013's 30.5mmbd (Table 3). The 3Q13 call on OPEC crude oil is 30.3mmbd, with 4Q13 at 29.6mmbd. The call on OPEC crude in calendar 2014 is 29.2mmbd (with 1Q14 at 28.8mmbd and 2Q14 at 28.7mmbd). Thus if OPEC keeps production at its July and August 2013 levels, worldwide inventories probably will build by quite a bit, a bearish development.

One reason for decreasing demand for OPEC crude oil has been the jump in OECD supply, especially from the "Americas" category, which includes the US. Supply from this region increases from 2012's 19.9mmbd to about 20.8mmbd in 2013, mounting in 2014 to 21.7mmbd (IEA, Table 1).

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Interruptions of petroleum supply (recall recent troubles from Libya, Nigeria, Syria, and elsewhere) help to underpin oil prices. The Israel/Palestine issue remains far from solved. Iraq has had civil conflict.

Fears regarding an escalation of the Iranian nuclear situation have supported petroleum prices. Yet recently there have preliminary steps toward resolving the Iran nuclear issue, a bearish signal for oil prices. "US says it is ready for talks with Iran" (Financial Times, 9/16/13. p3), "Iran to show 'flexibility' at talks" (FT, 9/18/13, p6), "Iran Moves to Mend Ties With West" (NYTimes, 9/18/13, pA10), "Iran Said to Seek a Nuclear Accord to End Sanctions" (NYTimes, 9/20/13, pp A1, 10).

Of course it remains an open question as to how much actual progress will be made. In any event, this recent (even if slight) easing of tensions makes it less likely that America (and probably Israel) will launch an attack on Iran's nuclear facilities in the near future.

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The most current (9/24/13) net noncommercial long ("NCL") position in the NYMEX Commitments of Traders for NYMEX petroleum complex (crude oil, heating oil, and RBOB/gasoline combined, futures and options positions combined) is very large. (The 9/24/13 date provides the most recent data due to the US government shutdown resulting from the federal budget and deficit ceiling impasse.) As of 9/24/13, the gross noncommercial long position is 574,000 contracts. The net NCL total is about 411,000 contracts; and that net NCL position represents about 12.9pc of the total open interest.

Highs in the NYMEX petroleum complex's net NCL and of the net NCL as a percentage of total interest often linked fairly closely in time to peaks in outright prices for that complex (and its parts). For nearly ten years (since September 2003), the net noncommercial position of the NYMEX petroleum complex has never been net short. Thus lows in the net NCL position (a relatively low net NCL) often have been associated with marketplace bottoms in the NYMEX oil complex. (In the more distant past, there sometimes was a large net NC short position around price lows.) Of course other oil marketplaces such as Brent are relevant to this noncommercial net long issue.

The recent peak in the gross noncommercial long position for the NYMEX petroleum complex was 7/30/13's 670,000 contracts; this was a record total. The net NCL long that week was about 468m contracts. That was only slightly below the net NCL high of 472m on 7/23/13, which also established a new record. The net NCL position as a percentage of total open interest on 7/30/13 was extremely high, over 14.5 percent. It thus was the highest net NCL percentage for nearly 10 years (since 3/2/04's 15.4pc). The 7/30/13 net NCL total likewise was large, about 14.2 percent of total open interest. Compare the 14.2pc net NCL on 2/28/12 (and its 456m net NCL) as well as the nearly 14.4pc net NCL on 2/5/13 (445m net NCL one week later on 2/12/13).

These late July 2013 very high net NCL and net NCL as a percentage of total open interest levels for the NYMEX petroleum complex are fairly close in time to the recent tops in nearest futures continuation crude oil (8/28/13 at 11224), RBOB/gasoline (7/19/13 at 316.3), and heating oil (8/29/13 at 319.3).

The most current (9/24/13) net noncommercial long position in the NYMEX Commitments of Traders for NYMEX petroleum complex fell from its recent peak, as have prices in the NYMEX petroleum complex over the past several weeks. Further liquidation by the net noncommercial long group (whether labeled as speculators or investors) could, all else equal, have a substantial bearish impact on oil prices.

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