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"Global commodity outlook by the World Bank and its highlights"

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Global commodity outlook by the World Bank and its highlights

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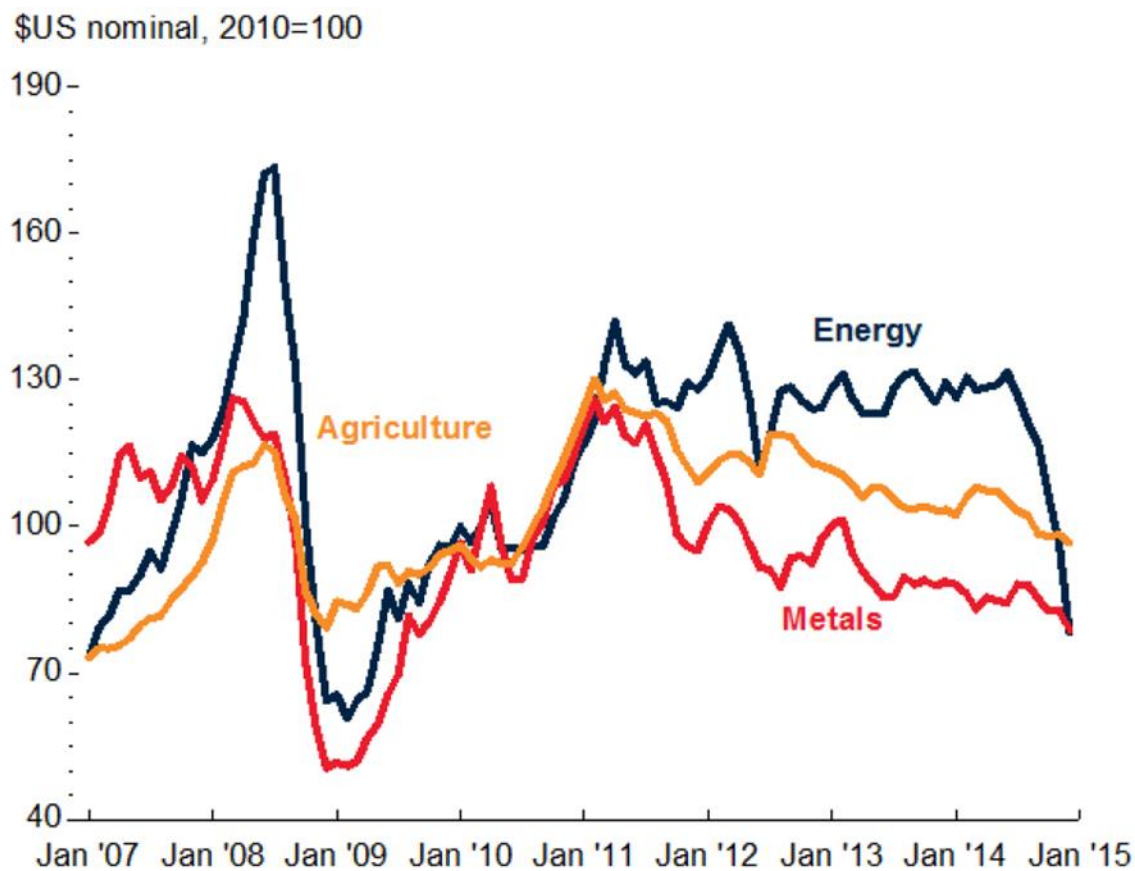
Commodity price indices

The World Bank noted that, although the energy price index experienced the largest drop in 2014Q4 (mostly due to oil), all three industrial commodity price indices (energy, metals and minerals, and agricultural raw materials) have experienced nearly identical declines from their 2011Q1 peaks: 37, 36, and 35 percent lower as of December 2014.

Figure 1. Commodity price indices



Source: World Bank.

And the Bank is also predicting that the commodity prices to continue decreasing in 2015 (Table 1). The forecast is based on the baseline scenario, which assumes no further deterioration in the global macroeconomic environment and OPEC abstaining from any form of supply management.

TABLE 1. Nominal price indices actual and forecasts (2010 = 100)

	Actual					Forecast		Change		
	2010	2011	2012	2013	2014	2015	2016	2013/14	2014/15	2015/16
Energy	100	129	128	127	118	70	75	-7.2	-40.5	6.4
Non-Energy	100	120	110	102	97	92	93	-4.6	-4.9	0.6
Metals	100	113	96	91	85	80	81	-6.6	-5.3	1.2
Agriculture	100	122	114	106	103	98	98	-3.4	-4.8	0.4
Food	100	123	124	116	107	103	103	-7.2	-4.2	0.2
Grains	100	138	141	128	104	100	101	-19.0	-3.7	0.6
Fats and oils	100	121	126	116	109	101	102	-6.0	-7.1	0.5
Other food	100	111	107	104	108	107	107	4.3	-1.0	-0.6
Beverages	100	116	93	83	102	96	95	22.2	-5.6	-1.4
Raw Materials	100	122	101	95	92	86	88	-3.6	-6.0	2.1
Fertilizers	100	143	138	114	100	98	98	-11.6	-2.1	-0.8
Precious metals	100	136	138	115	101	98	98	-12.1	-2.9	-0.7
Memorandum items										
Crude oil($/bbl)	79	104	105	104	96	53	57	-7.5	-44.8	7.1
Gold ($/toz)	1,225	1,569	1,670	1,411	1,266	1,240	1,225	-10.3	-2.0	-1.2

Source: World Bank.

The World Bank has lowered the energy and metal indices for 2015 significantly from the commodity from its outlook in October 2014. The Bank forecasted that energy price index to decrease to 70, 33% lower than the previous outlook. This is mostly due to the oil price drop, which the Bank assumes to average $53/bbl in 2015, 45 percent lower than 2014.

Metal price index was also revised down from 87 to 80, 8% lower than its previous outlook of October 2014. The World Bank expects metal price to decline 5.3 percent in 2015 on top of last year's 6.6 percent decline. A moderate decline is also expected in **precious metal prices** as institutional investors view them less attractive "safe haven" investment vehicles; reduced demand by China and India will also contribute to the weakness.

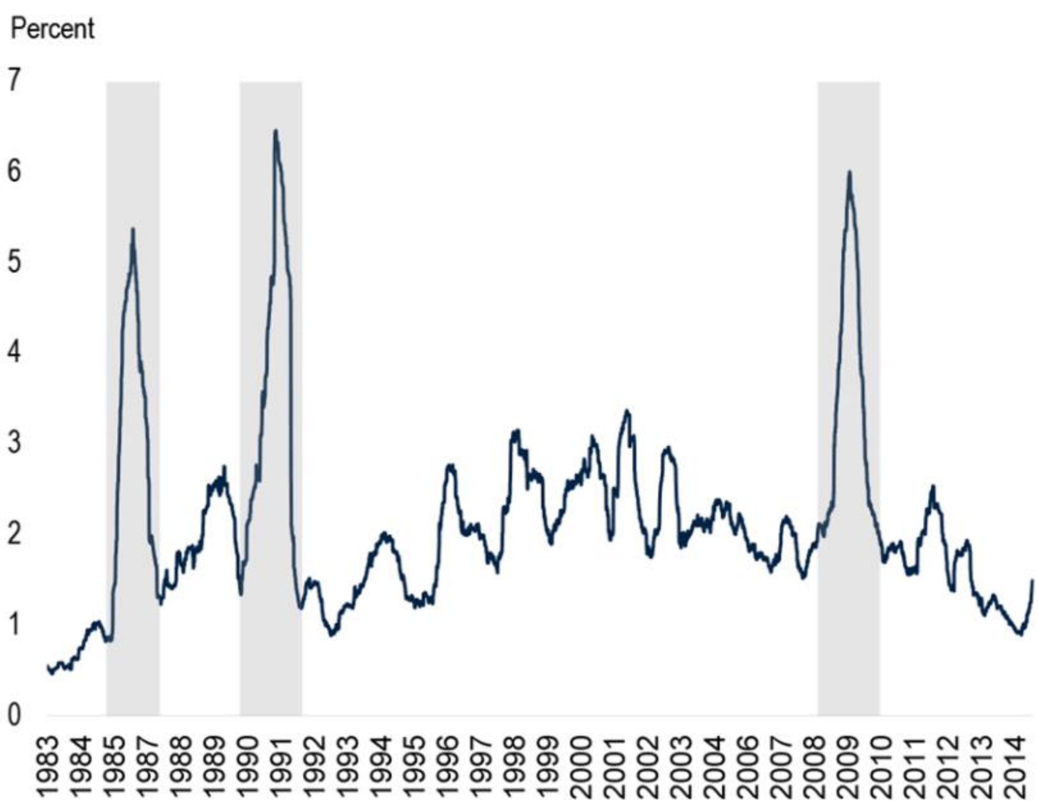
Special focus: Putting the recent plunge in oil prices in perspective

The plunge in oil price has been given special focus this time. The World Bank has concluded that the following main forces have pressed the oil price down: revisions of supply and demand expectations combined with the change in OPEC's objectives, receding geopolitical risks and U.S. dollar appreciation. If the low oil price persists (which actually the WB assumes would happen) it will push other commodity price down.

The Bank pointed out that recent development in global oil markets took place against the backdrop of longer-term strong supply growth, especially from unconventional oil in the United States, and to a lesser degree Canadian oil sands and the production of biofuels. During the second half of 2014, the 2014 and 2015 oil production outlook for the United States was revised upwards several times, global oil demand forecasts, on the other hand, have been revised downwards repeatedly, consistent with the fragile recovery of the global economy. These revisions were not that unique, what makes the adjustments in 2014H2 important, is that they unfolded alongside a number of other significant (predominantly supply driven) forces in commodity markets, as mentioned above. The World bank names it a 'perfect storm'.

There have been only three occasions since 1984 (when oil futures contracts were introduced) when the price of oil dropped by 60 percent or more in any seven-month period. First, during 1985-86, when the West Texas Intermediate nearby futures contract (WTI was the world oil price barometer at the time) declined by 67 percent from $31.72/bbl (November 20, 1985) to 10.42/bbl (March 31, 1986). Second, in 2008, when Brent nearby futures contract (today's world price indicator) declined by 75 percent from $146.08/bbl (July 3, 2008) to $36.61/bbl (December 24, 2008). Third, during 2014-15, when the Brent nearby futures contract declined by 60 percent from $115.06/bbl (June 19, 2014) to 46.77/bbl (January 13, 2015).

Figure 2. Oil price volatility



Source: World Bank.

Note: Price volatility is the standard deviation of daily changes in prices (over a 125-day window).

The World Bank concluded that the oil price collapse of 2014 share hare two key similarities with the 1985/86 price collapse. On the technology front, there was a boom in unconventional oil production on both occasions. On the policy front, the drop in oil prices in both episodes coincided with OPEC's movement toward targeting market share rather than prices. Given the condition of the large production capacity is still in place and OPEC officials' statement that the cartel will not act even if prices decline to $20/bbl, the price of oil is not likely to recover in 2015, even in 2016.

Metals

The decline in prices resumed in 2014Q4, with the World Bank metals price index falling 6.5 percent (q/q). Both base metals (down 4.7 percent, q/q) and iron ore (down 18 percent q/q) contributed to the decline. The steep drop in iron ore prices, down for the fourth consecutive quarter, reflects expansion of low-cost producers, particularly Australia and Brazil, in an oversupplied market. For the whole of 2014, iron ore, copper, lead, and tin prices all fell. The declines in iron ore and tin markets are driven by supply issues, while those for copper and lead were dominated by weak demand, namely by China.

Metal prices are expected to decline by more than 5 percent in 2015 (which comes on top of last year's 6.6 percent drop) as new supplies will be coupled with weaker demand by China. Specifically, iron ore is expected to decline the most in 2015 (-22 percent), followed by tin (-8.6 percent), copper and nickel (-5.3 percent each). Zinc and aluminum prices are expected to gain 1.8 and 3 percent respectively.

The key risk on metals prices would be a sharp slowdown in the Chinese economy. However, a sharp slowdown of the Chinese economy remains a low probability scenario at present, according to the bank.

The precious metal index fell to a four-year low in November, with platinum, gold and silver down 7, 10, and 20 percent for the year, respectively. Precious metal price weakness will persist in 2015, with the index averaging 3 percent lower as institutional investors consider these commodities as less "safe haven" holdings, and to fall an additional 1 percent in 2016.

Summary

We have reviewed price forecasts of selected minerals in 2015, released by the World Bank in January 2015 along with the Commodity Markets Outlook and compared with the price forecast at the previous October 2014 edition.

Table 2. Changes of the forecast of selected commodities (in nominal US dollars)

Commodity	Forecast of January 2015 edition		Forecast of October 2014		Difference (%)	
	2015	2016	2015	2016	2015	2016
Coal, Australia ($/mt)	67	69.7	75	77.2	-11%	-10%
Crude oil, avg ($/bbl)	53.2	56.9	95.7	96.6	-44%	-41%
Copper ($/mt)	6500	6529	6880	6872	-6%	-5%
Iron ore ($/mt)	75	78	105	107	-29%	-27%
Gold ($/toz)	1240	1225	1240	1225	0%	0%

Source: World Bank

The table 2 shows that the World Bank has lowered its price forecast of 2015 for the commodities that are important to Mongolia and it is not likely to recover fully in 2016 either. As we repeatedly stated before, along with other researchers, 2015 will be the tough year for Mongolia, especially when Mongolia is extremely vulnerable to the external factors. Predictions of international organizations on commodity market and fragile economic recovery of the world are not new; however they keep lowering their expectations, which are not good news for Mongolia. Therefore, we still keep concluding that Mongolia should watch very carefully the negative impacts from the external market.

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