A World Bank
Quarterly Report

http://www.worldbank.org/commodities

JULY 2016

Commodity Markets Outlook

From energy prices to food prices: Moving in tandem?

WORLD BANK GROUP

Q1
Q2
Q3
Q4

Executive Summary

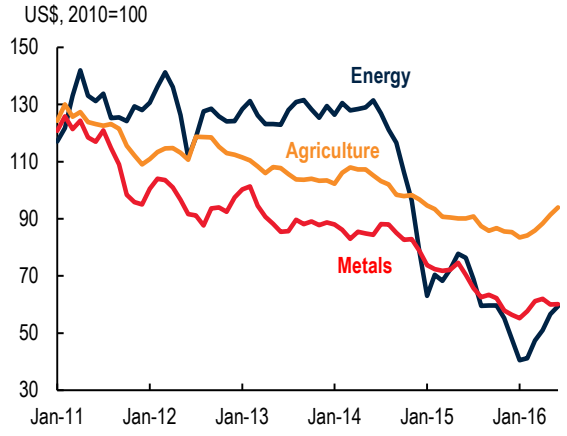
Most commodity price indexes rebounded in the second quarter of 2016, continuing their upward climb from January lows on improved market sentiment and tapering supplies. Oil prices jumped by more than a third due to supply outages and strong demand. Given this rebound and expected reduction in inventories during the second half of the year, the crude oil price forecast for 2016 is being raised to $43 per barrel (bbl) from $41/bbl in the April assessment, still a 15 percent drop from 2015. Metals prices are projected to decline 11 percent in 2016, a slightly larger drop than anticipated in April, mainly driven by an ongoing surplus in the copper market. Agricultural prices for 2016 have been revised slightly upwards due to weather patterns in South America, but are still expected to register a marginal decline from last year. A large upward revision for precious metal prices of more than 8 percentage points versus the April assessment reflects the increased demand for safe haven assets. For 2017, a modest recovery is projected for most commodities as demand strengthens and supply tightens. This issue of the Commodity Markets Outlook examines the implications of low energy prices for food prices. It finds that, given the energy-intensive nature of agriculture, high energy prices were an important driver of the post-2006 surge in agricultural prices. Over 2011-16, lower energy prices are estimated to account for up to one-third of the projected 32 percent decline in prices of grains and soybeans.

Trends. *Energy* prices leapt almost 30 percent in the second quarter of 2016 (Figure 1). Oil prices averaged $47.70/bbl in June, 37 percent above their first quarter average. The oil price rebound reflects a number of supply disruptions that removed up to 2.5 million barrels per day (mb/d) of production at peak during May and June, with large losses concentrated in Canada due to wildfires, and in Nigeria due to militant attacks on oil infrastructure. In addition, there were disruptions in other countries, including Kuwait, Iraq, and Libya. Declines in non-OPEC production, led by the United States, were partly offset by higher OPEC production, mainly from Iran. Global oil demand remained strong, albeit slowing. In contrast, natural gas prices were down 5 percent in the second quarter, particularly in Europe and Asia, due to weak demand and surplus supplies of liquefied natural gas (LNG). However, U.S. gas prices rose from their lows in March on stronger demand and higher exports. Coal prices rose 2 percent on tightening supply and strong demand in China.

Non-energy commodity prices rose 7 percent in the second quarter, led by agriculture, which was up 8 percent. Gains were concentrated in oils and meals (up 17 percent) due to poor harvests in South America (some grains and soybeans) and East Asia (palm oil). Other food commodity prices rose moderately. Metals prices rose 5 percent in the second quarter, with gains concentrated in iron ore, zinc and tin on production cuts and stronger demand. Precious metals prices rose 8 percent due to strong investor demand prompted by anticipation of delays in the normalization of monetary policy in the United States and growing concerns about global growth. Fertilizer prices fell almost 7 percent amid weak demand and surplus production capacity.

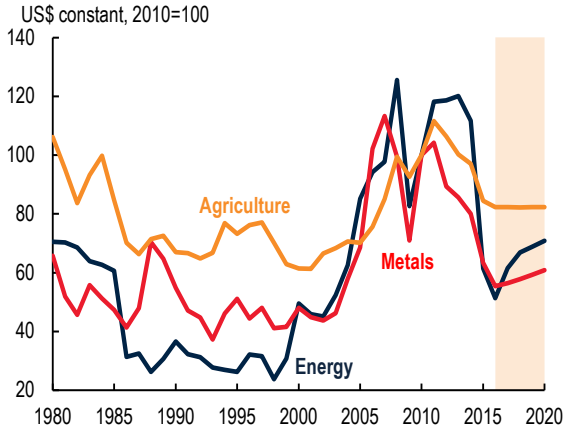
Outlook and risks. All main commodity price indexes (except food and precious metals) are expected to decline in 2016 (Figure 2) due to large supplies and, in the case of industrial commodities, weak growth prospects in emerging market and developing economies (EMDEs). However, the annual decline in prices is

1 Commodity price indexes, monthly



Source: World Bank.
Note: Last observation is June 2016.

2 Commodity price indexes, annual



Source: World Bank.
Note: Shaded area denotes price forecast (2016-20).

smaller than forecast in the April 2016 *Commodity Markets Outlook* (Table 1). Energy prices are expected to fall 16 percent, with average oil prices projected at $43/bbl in 2016 (compared with $41/bbl in the April assessment). This implies marginally higher prices for the second half of 2016, as the oversupply in the oil market diminishes. Downside risks to the energy price forecast include higher-than-expected output and further weakening in EMDE growth. Supply disruptions among key producers could lead to higher prices.

Non-energy commodity prices are expected to drop 4 percent in 2016, 1 percentage point less than forecast in the April assessment. Agricultural prices have been revised up 2 percentage points, but are still projected to average marginally lower in 2016 than in 2015. The outlook reflects adequate supplies for most commodities but also takes into account reduced harvests in South America (especially Brazil) due to dry weather conditions. Agricultural commodity prices are also expected to be dampened by lower energy costs and plateauing demand for biofuels. Although the food price index is expected to grow only moderately next year, there is considerable dispersion among its key components: Grains and beverages are both projected to fall 4 percent and raw materials by 2 percent, while oils and meals are expected to increase 3 percent. Upside risks to agricultural price forecasts include the likely intensification of La Niña (unusually cold weather in the equatorial Eastern Central Pacific Ocean), which could affect some food commodities, such as maize in the United States and wheat in Australia. Downside price risks reflect increased agricultural subsidies, which would encourage greater supply of food commodities. Fertilizer prices are projected to retreat 18 percent in 2016 due to surplus capacity, weak demand, and low natural gas prices, used as feedstock to the production of some fertilizers.

Metals prices are projected to decline 11 percent in 2016, which follows last year's 21 percent drop, due to weak demand prospects and new capacity coming on line. The largest declines are for nickel and copper, amid surplus supply, while the zinc market is expected to tighten with the closure of large mines. Downside price risks for non-energy industrial commodities include further slowdown in China and currency depreciations in key suppliers. Precious metals prices are projected to rise 8 percent in 2016 on stronger safe-haven buying and deepening concerns about global growth prospects.

Special Focus on the implications of low energy prices for food prices. Energy prices declined 45 percent in 2015 and are projected to drop another 16 percent in 2016. Since agriculture is energy intensive, lower energy prices reduce the cost of producing food commodities. Lower energy prices can ease policy pressures to encourage production of biofuels, which have been a key factor behind the growth of food commodity demand over the past decade. Indeed, energy prices were an important driver of the post-2006 surge in agricultural prices. During 2011-16, energy price changes are estimated to contribute about one-third to the projected 32 percent decline of grain commodities and soybeans prices.

TABLE 1 Nominal price indexes (actual and forecasts) and forecast revisions

	Price Indexes (2010=100)						Change (%)		Revision[2]	
	2012	2013	2014	2015	2016f[1]	2017f[1]	2015-16	2016-17	2016f	2017f
Energy	128	127	118	65	54	66	-16.4	22.2	1.9	3.4
Non-Energy[3]	110	102	97	82	79	81	-4.1	2.1	0.8	0.7
Agriculture	114	106	103	89	89	90	-0.7	1.5	2.4	2.2
Beverages	93	83	102	94	90	89	-4.2	-0.3	0.4	0.5
Food	124	116	107	91	91	93	0.4	1.6	3.4	3.1
Oils and meals	126	116	109	85	87	89	2.7	2.3	5.2	4.8
Grains	141	128	104	89	86	88	-3.7	2.6	1.4	1.3
Other food	107	104	108	100	101	101	1.0	0.2	2.9	2.7
Raw Materials	101	95	92	83	82	84	-1.7	2.3	1.1	1.0
Fertilizers	138	114	100	95	78	80	-18.0	2.0	-4.6	-4.2
Metals and Minerals	96	91	85	67	60	62	-11.0	3.6	-1.8	-2.0
Precious Metals[3]	138	115	101	91	97	95	7.5	-2.0	8.3	7.3
Memorandum items										
Crude oil ($/bbl)	105	104	96	51	43	53	-15.2	23.7	2.0	3.2
Gold ($/toz)	1,670	1,411	1,266	1,161	1,250	1,219	7.7	-2.4	100.0	87.1

Source: World Bank.
Notes: (1) "f" denotes forecasts. (2) Denotes revision to the forecasts from the April 2016 report (expressed as change in index value except $/bbl for crude oil, and $/toz for gold). (3) The non-energy price index excludes precious metals. See Appendix C for definitions of prices and indexes. Figures may not match due to rounding.