Global Macro Research | US

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MF Global Daily Report

COMMODITIES | ENERGIES

Energy

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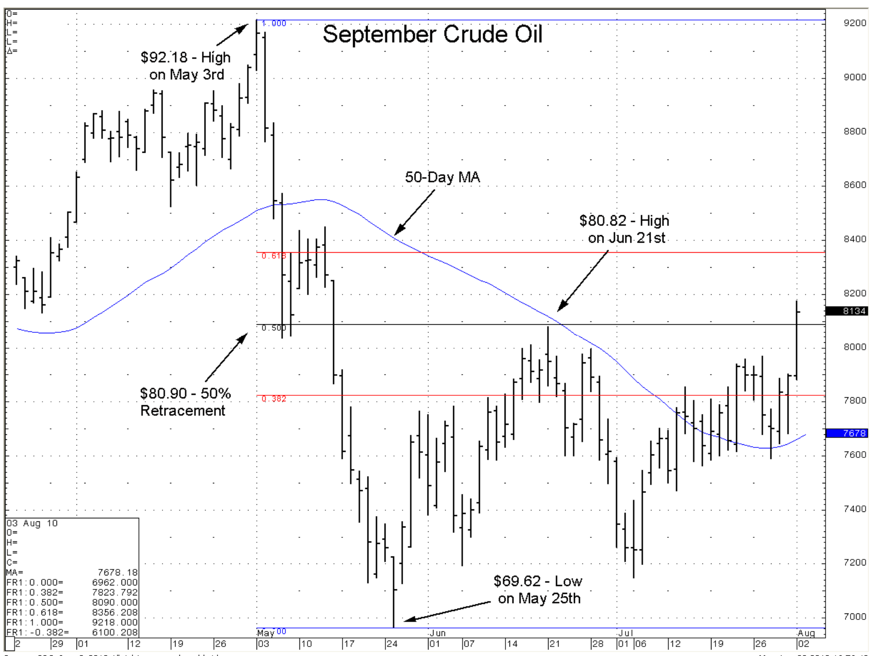
Price Outlook

Crude oil prices are expected to move slightly higher in today’s trade, with the market potentially holding in an $80.82-$82.00/bbl range. Support will come from technical factors, strength in the stock market, and from tropical storm concerns. Pressure will be offered by signs of weak energy demand in the U.S. and high levels of oil stocks. We had favored buying CLU0 at $77.00 in our 3M report published yesterday, but the recommendation’s price target of $81.00 has already been achieved. We favor only buying NGV0 now at $4.65, targeting $5.30 and risking $4.50.



Yesterday’s trade made an impressive breakout above the Jun 21st peak at $80.82 and ended up closing near the day’s high itself. The action appears extremely favorable from the technical perspective, especially when combined with last Wednesday’s test and hold at key support from the 50-day MA. The technical action would now suggest that an advance toward the 62% retracement of the May 3rd-May 25th downtrend at $83.55 would be in order, although as we discuss below, we don’t believe that prices are fundamentally valued that high. Support could also come from strength in the stock market, where the S&P 500 futures are approaching key resistance at 1,135. We think that because stocks have been well respecting the head & shoulders bottom pattern as well as other patterns recently, that a hold at 1,135 is possible, and could tie-in with oil peaking around $82.00-$83.55 in the next couple days.

We can’t get very bullish on energies at this time because of supply and demand issues. OPEC’s spare capacity is currently around 5.6 mb/d and OPEC compliance with its quotas is around 50%. Even though Chinese demand continues to increase, OPEC and non-OPEC supplies have the ability to meet extra demand for the foreseeable future. Weekly EIA data shows U.S. demand that’s 325 kb/d below a peak made in early-Jun, despite a five-year average which typically gains 77 kb/d between early-Jun and now. Similarly, U.S. stocks of crude oil, gasoline, and distillates are a combined 76.7 MB above their five-year averages, which is the highest divergence since Oct '09. The negative argument also focuses on the health of the U.S. economic recovery, which has changed its tone nearly every data. Weak GDP numbers on Thursday turned into positive manufacturing data on Friday and yesterday. With payrolls due out Friday, the tone could easily change back to bearish in just a few days.

TRADE: Buy: NGV0 at $4.65, target $5.30, risk $4.50

Upcoming Energy Events

Tue - API Weekly Stats 4:30 pm EST
Wed - Oil Inventories 10:30 am EST
Thu - Natural Gas Inventories 10:30 pm EST
Oct 14th - Next Ordinary OPEC Meeting

Global Economic & Dollar News

The dollar fell throughout the trading day yesterday, with pressure offered by in increase in risk appetite. The ISM manufacturing PMI beat expectations, and high yield debt outperformed treasuries.

- **Japanese PM Kan** said that tackling deflation and fiscal reform are urgent, and that the gov't and BOJ share the same goals.
- **BOJ's Shirakawa** said that the economy is picking up but that the level of economic activity is low.
- **Chinese NBS PMI** was 51.2 vs. 52.1. The HSBC PMI was 49.4 vs. 50.4.
- **South Korea's Exports** from July 1-20 were +49.3% y/y to the U.S., and +56.9% to the EU.
- **Eurozone MFG PMI** was 56.7 in July vs. 55.6 previously.
- **UK MFG PMI** was 57.3 vs. 57.6 previously.
- **Goldman Sachs** predicted that the UK will grow faster than the U.S. and Eurozone in 2011, in a Sunday Times article.
- **HSBC's Earnings** were +4.5% after first-half earnings doubled from a year ago and bad debts fell. BNP Paribas +4.3% after beating expectations and posting lower loan loss provisions.
- **Ex-Fed Greenspan** said that the slowing economic recovery feels like a quasi-recession, and that the economy might contract again if home prices decline.
- **U.S. Construction Spending** was +0.1% vs. -0.5% expected and vs. -1.0% previously (revised down from -0.2% previously).
- **ISM MFG PMI** was 55.5 vs. 54.2 expected. Prices paid were 57.5 vs. 57.0 previously while employment was 53.5 vs. 58.5.
- **Fed's Bernanke** said that there's a considerable way to go before a full recovery takes place and that job growt is still insufficient to reduce unemployment materially. Said he expects consumer spending to pick up in coming quarters from a modest pace, but that the slow recovery in jobs is weighing on household confidence. He anticipates inflation to remain subdued over the next couple of years, and inflation expectations to remain stable.
- **Climate Envoy Todd Stern** said that the U.S. is sticking to its climate change commitments despite the setback on the Senate's climate legislation. Said the U.S. is committed to reducing emissions by 17% by 2020 from 2005 levels.

Commitment of Traders Jul 20th-Jul 27th
Net non-commercial (large funds) (Legacy Report)

	Net Position	Change	Price Change
Crude Oil	44,313	+8,168	+$0.06
ICE WTI	29,321	+8,978	+$0.06
Heating Oil	13,109	-2,300	-2.53c

Gasoline	48,252	+7,031	-1.54c
Natural Gas	-154,103	+1,877	+8.5c

Energy News Stories

- **Japanese LNG Imports** rose 9.5% in the six months through Jun to 34.68 mln metric tons from 31.65 a year earlier. That put imports at a new record.
- **Indonesia's Oil Production** fell 2.48% or 20,700 b/d in Jul due to technical problems. Output was 813,000 b/d vs. 833,700 b/d in Jun.
- **The NHC** is watching a storm halfway between Africa and the Leeward Islands. With a 90% chance of tropical storm formation. The NHC upgraded the system to Tropical Depression 4 yesterday morning.
- **BP** conducted a test of its static kill process yesterday evening, and if successful, will conduct the kill today. The operation should take 33-61 hours, according to BP.

ANALYSIS

EIA Oil Inventory Preview

The EIA is expected to report oil inventories this week that unwind a significant portion of last week's gain. A build of 7.3 MB was reported last week, due mainly to a 1.18 mb/d surge in imports. We believe that the import jump may have caused a larger increase than was justified, since the API reported a 1.67 mb/d increase in imports but only a 3.1 MB build in crude stocks. API data suggest that EIA oil stocks are 4.4 MB too high, presenting another downside risk. Refinery utilization is likely to decline, as demand isn't strong enough to justify operating rates that are 0.5% above the five-year average. Gasoline demand typically increases sharply in Aug before falling precipitously in Sep. Such opposing influences on utilization and demand should lead to a decline in gasoline stocks of 1.5 MB and a below-normal rise in distillates of 1.0 MB. Another downside risk for distillates comes from the API, which suggests that EIA distillate supplies are 5.2 MB too high.

EIA Inventories - w/e July 30th							API Inventories		
	Actual	Market Estimate	MFGR Estimate	Five-Year Average	Last Week		Converge with EIA	Actual	Previous
Crude Oil		-1.0 MB	-4.0 MB	-0.6 MB	+7.3 MB				+3.1 MB
Gasoline		-0.7 MB	-1.5 MB	-1.9 MB	+0.1 MB				+0.9 MB
Distillates		+1.1 MB	+1.0 MB	+1.9 MB	+0.9 MB				+0.4 MB
Utilization		-0.6%	-0.5%	+0.3%	90.6%				87.4%
Natural Gas		+35 bcf	+34 bcf	+51 bcf	+28 bcf				

*The API convergence figures are the amounts that EIA data need to change in order to match the previous day's API figures

Geopolitical Tensions/Developments

Iran: Iranian President Ahmadinejad called on U.S. President Barack Obama on Monday to face him in a televised one-on-one debate to see who has the best solutions for the world's problems.