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Investment Services

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Market Commentary

<u>Curious: whether or not there is going to be enough demand to justify higher prices?</u>

Crude prices saw a back and forth movement for this week, trending in the price range of $37-$41 showing indecision in the markets. Price action is under pressure against a backdrop of rising Covid cases, which could be dragging down fuel demand. At times this week, the market also reacted to the extremely weak U.S. Dollar, which made the dollar-denominated asset more attractive to foreign buyers. The number of Americans filing for unemployment benefits hit 1.416 million last week, unexpectedly rising for the first time in nearly four months. Meanwhile, U.S. business activity increased to a six-month high in July. U.S. companies, however, reported a drop in new orders as new cases spiked across the country.

Markets saw some enthusiasm after a bullish tone when European Union announced the approval of the recovery fund and this news led to investors ignoring a surprise build in U.S. crude oil inventories and a worsening of pandemic cases could cap fuel demand. In India, road fuel sales fell in the first half of July as virus lockdowns occurred in several cities, and the Chinese city of Urumqi locked down some areas amid fears of another outbreak in the country.

There are already signs the spread of the infection has all but cancelled the demand boost from the driving season this year: while many expected a pickup in demand for fuels spurred by the pandemic as people chose their cars over airplanes, this has failed to materialize.

Broadly speaking, lower crude oil prices stem from a whopping 9% plunge in world oil demand expected this year due to a screeching halt in economic activity amid the lockdown. This has primarily contributed to a supply-demand imbalance of 9.8-Mbpd penciled in by OPEC for 2Q-2020. Looking forward, however, the cartel of major oil producers have optimistic projections for world oil demand to recover during the second half of 2020 and into 2021. Both the IEA and EIA anticipate global oil demand to increase in the months

Crude Oil			
Exchange	MCX	NYMEX-WTI	ICE-Brent
Open	3155	41.06	43.27
Close	3072	41.29	43.34
1 Week Chg.	-83	0.23	0.07
%change	-0.03%	1.33%	0.46%
OI	1256	453308	263495
OI change	879	9665	-120058
Pivot	3091	41.21	43.34
Resistance	3136	41.75	43.90
Support	3028	40.74	42.79

Natural Gas		
Exchange	MCX	NYMEX-NG
Open	137.5	1.784
Close	138.9	1.81
1 Week Chg.	1.4	0.02
%change	1.02%	1.35%
OI	4379	17719
OI change	49.10%	84.18%
Pivot	138.0	1.79
Resistance	141.1	1.84
Support	135.9	1.76

Front Month Calendar Spread		
Exchange	MCX	NYMEX($)
1st month	20	0.16
2nd month	55	0.19

WTI-Brent spread$	
1st month	0.44
2nd month	0.38

ahead as well according to their respective monthly oil reports.

Supply:

OPEC+ overproducers pose risk to recent oil price gains:

With oil prices back above $40/b, the OPEC+ alliance plans to relax its crude oil production quotas by about 2 million b/d in August but says the new volumes will not flood the market. The move looks to ease OPEC+ production cuts from 9.7-Mbpd to 7.7-Mbpd on the net. As such, a bearish risk facing crude oil price action emerges with OPEC+ set to unwind prior supply cuts and relax oversight of standing output quotas.

In fact, some of the production rise will be offset by so-called compensation cuts that countries that violated their quotas in May and June will have to implement in the next few months. Meanwhile, U.S. rig count an early indicator of future output, fell by two to an all-time low of 251 in the week to July 24.This was indicated by OPEC+ delegates who backed an agreement solidified by Saudi Arabia and Russia to increase the group's crude oil output by 2-million barrels per day starting next month.

However, energy firms added one oil rig in the first weekly increase since March. U.S. shale has been unprofitable for years and has almost no chance of growth with prices at $40 per barrel. In that sense, prices need to move above USD 50/bbl at some point relatively soon in order to stabilize supply. On the EIA front, data showed that crude oil inventory saw a build of 4.9Mbpd with a 1.8-MB decline in gasoline stockpiles and an average of 9.1 Mbpd in gasoline production for last week. This suggests demand for the fuel is indeed improving, despite the improvement being an uneven one. In distillate fuels, the EIA reported a 1.1-million-barrel inventory build, compared with a modest decline of 453,000 bpd a week earlier.

Demand:

Demand for oil products in key Asian markets continues to show signs of recovery. South Korea's domestic gasoline demand rebounded to 7.81 million barrels in May from 6.58 million barrels in April. In Japan, weekly domestic gasoline shipments were estimated to have risen above the pre-crisis level of 4.72 million barrels in recent weeks.

However, Japanese and South Korean industry refiners in both countries are cautious about not over committing to crude procurement. Meanwhile, Chinese refiners are wary of tilting the supply-demand balance as expected severe floods and heavy rain could curb transportation and industrial fuel demand this month.

OPEC+ output unwind is not so good for one large segment of the industry for the downstream segment (refiners) as they prefer cheap oil prices and demand for refined products. Gasoline demand has picked up, indeed, but growth is weaker than hoped for. For jet fuel, this demand pickup has been nonexistent. This has forced refiners to shift their production to more gasoline and distillate fuels. This, however, has led to excess supply of middle distillates.

Chinese refiners, the one that pushed prices higher by higher imports in April are now cutting processing rates and this is a worrying sign. China has been stocking up on dirt-cheap crude since the early days but if imports are rising more quickly than local fuel demand, then this storage space would be filling up, reducing Chinese buyers' appetite for crude.

With the depressed demand, refinery overcapacity has emerged and global refining capacity is 3 Mbpd higher than necessary, and if the downstream industry is to regain its profitability, this needs to be cut by the end of next year. Currently, some 1.4 Mbpd in refinery capacity is under threat of closure between 2022 and 2023 in Europe alone.

Natural gas prices continued to show strength as the bankruptcy has led to plenty reduction in supply down a bit, and at the same time we also have plenty of hot temperatures in the United States to drive up demand. Tropical storm Hanna has now formed in the Gulf of Mexico and is headed directly for the Texas coast. There are some natural gas installations that will be impacted by the storm and any disruption would support prices. However, LNG tankers loading on the US Gulf Coast and delivering to East Asia are continuing to slow steam to their destinations in search of better netbacks in the fall.

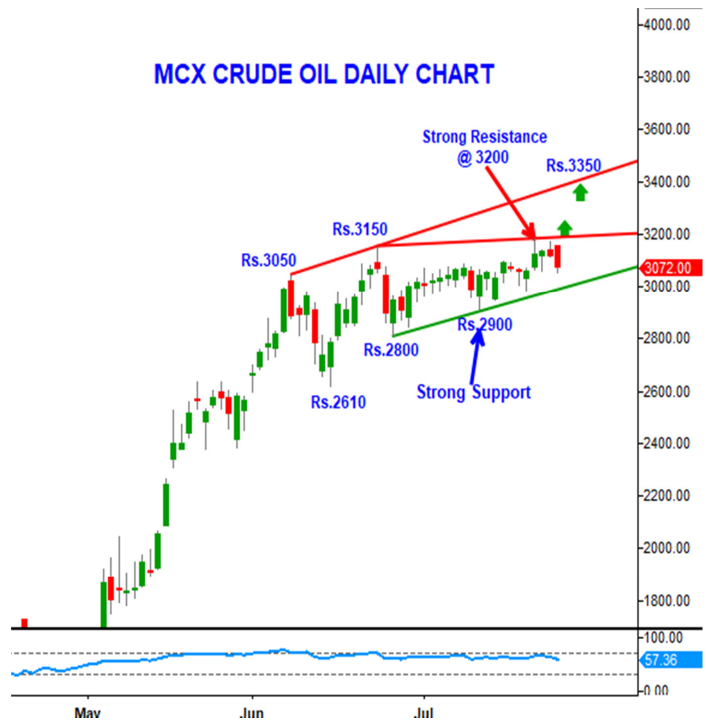
Outlook:

Oil prices could see a near-term correction if a recovery in fuel demand slows further, especially in the United States. There's a huge concern that after the stimulus checks run out, there's going to be a pullback in retail sales and definitely a pullback in travel by car if people are not going to be working. Major gasoline-guzzling states like Texas and California are facing resurgence in cases, squashing demand, while the OPEC+ alliance is preparing to unleash crude oil back into the market next month. It's unclear what happens next. Oil prices have become trapped between two main competing market narratives, negative coronavirus news and the fact that oil prices are unsustainably low. Oil prices have been trapped at $40 as these two forces battle and the move from current price levels is expected to be downwards.

Meanwhile, market participants may focus on second quarter GDP data releases due next week considering the elevated chance for volatility as GDP growth rates might garner notable attention as the US and EU are two of the world's biggest economies and consumers of crude oil. On the other hand, a swarm of equity earnings anticipated next week, not to mention the potential for coronavirus vaccine news, could cause fluctuations in risk appetite and crude oil price action as well.

Technical Views

Crude Oil



MCX Crude Oil continued to trade in a narrow range last week and closed almost unchanged at Rs.3072 level. Going ahead the commodity has got strong short term support at Rs.2900 level and short-term trend is likely to remain bullish as long as the it is trading above the support zone. On the higher side crude oil is likely to face stiff resistance at Rs.3200 level and daily close above the same is likely to result in further bullish momentum in the commodity. If it manages to give daily close above Rs.3200 level then it is likely to test higher resistance of Rs.3350 levels. The counter has got good intermediate support in the range of Rs.3000-3020 levels and any dips towards the same should be used as an opportunity to buy the commodity. However if crude oil manages to break the support level of Rs.2900, then there is high probability that it may give further downfall till Rs.2600 level. However 14-period RSI is sustaining above 50 mark which is signalling strength in the prices of the commodity. Thus Buying on dips towards intermediate support zone is thus advised. Major Support for Nymex crude oil is placed at $37.50 level whereas critical resistance is placed at $43.50 level.

Natural Gas

MCX Natural gas traded on a positive note last week and closed higher by approximately 4.99% at Rs.138.90 level. MCX natural gas has been consolidating in a triangle pattern (visible in the adjacent chart) and trend is likely to be established once the commodity breaks out of the consolidation zone. On the higher side the commodity is having strong resistance at Rs.150 level while major support is placed at Rs.124 level. If the commodity manages to break Rs.150 level then it is likely to gather more bullish momentum and is likely to test Rs.165 - 180 levels on the higher side. However if it gives the breakdown of consolidation zone then it may give further down fall till Rs.110 - 95 levels. Thus consolidation is expected to continue till the breakout or breakdown takes place.

For any details

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