

Commodity weekly Fuel tightness and gold demand support recovery

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Key Points:

- Commodities head for their first weekly gain in three, with all sectors advancing despite persistent macroeconomic headwinds.
- Oil remains far from normalisation, as recovering Gulf crude exports contrast with soaring freight costs, constrained refining capacity and tight distillate markets.
- Gold investors look beyond rising yields, with resilient ETF demand, renewed Chinese buying and mounting fiscal concerns supporting demand.
- El Niño threatens to become a major commodity driver, increasing agricultural supply risks while potentially reducing heating demand in parts of the Northern Hemisphere.

The Bloomberg Commodity Total Return Index is heading for its first weekly gain in three, rising a modest 1.7% and lifting its year-to-date advance to 35%. Despite headwinds from elevated bond yields, a stronger dollar and concerns about global growth, all sectors have contributed. Energy leads with a 2.8% gain, followed by metals, both precious and industrial metals, and softs all returning around 1.1%.

Beneath the broad advance, significant differences remain. Diesel and natural gas have outperformed crude oil, highlighting continued supply constraints despite recovering Middle East exports. Gold has shown resilience following a challenging period of rising real yields, while industrial metals have benefited from China's return after Golden Week. Meanwhile, a strengthening El Niño is raising weather-related risks across agriculture.

Looking ahead, seasonality may offer some support. Over the past ten years, the final quarter has, on average, delivered positive returns for both the Bloomberg Industrial Metals and Precious Metals indices. While last year's particularly strong fourth quarter has a significant influence on the averages, the period has nevertheless produced more positive than negative monthly returns. Past performance, however, is no guarantee of future returns.

Oil: Recovering crude exports mask a market far from normalisation

Brent crude holds above USD 100 per barrel, having retreated from Thursday's high near USD 106 after President Trump ruled out attacking Iran ahead of the US midterm elections. The announcement raises hopes of a period of relative calm, potentially allowing Gulf crude exports to remain elevated, provided further escalation can be avoided.

However, recovering exports should not be mistaken for a return to normal market conditions. Shipping costs remain exceptionally high, while significant refining capacity across the Middle East remains unavailable. As a result, the global market continues to face tightness and elevated prices for refined products, particularly middle distillates used in diesel, jet fuel, heating oil and some marine fuels.

The disruption is illustrated by the physical crude market. On Thursday, Dated Brent traded at a premium of around USD 31 to December Brent futures, highlighting strong demand for immediately available North Sea barrels. Meanwhile, tanker freight costs from the Middle East and the US to Asia have reached levels that can make long-haul shipments prohibitively expensive. For some refiners, obtaining crude at an economically viable delivered price has become a greater challenge than physical availability.

With more than 10% of global refining capacity reportedly curtailed, NY ULSD and London gasoil futures have returned towards USD 200 per barrel, rising 8% and 9.6%, respectively, this week. Gulf product exports remain well below pre-war levels, leaving global markets heavily dependent on alternative suppliers.

The G7 announcement of a 100-million-barrel release of crude and diesel initially provided relief, but its impact faded as the market recognised that much of the volume represented an acceleration of previously agreed releases rather than additional supply. Strategic reserves, moreover, cannot repair damaged refineries or restore disrupted distribution networks. China's expected resumption of fuel exports following Golden Week may offer some relief, but volumes remain insufficient to close the wider supply gap.

Looking ahead, crude prices could ease further if geopolitical tensions subside and Gulf exports continue recovering. However, a cornered Iran is potentially a dangerous Iran, and relatively unsophisticated weapons can threaten commercial shipping and undermine confidence in Gulf transit routes. Even isolated drone or missile attacks could trigger renewed risk aversion, lifting insurance and freight costs while threatening regional exports. The risk of sudden flare-ups is therefore likely to maintain a sizeable geopolitical risk premium, even during periods of relative calm.

A sustained normalisation will require a meaningful recovery in refinery operations, lower shipping costs and a rebuilding of depleted product inventories. Until then, diesel and other middle distillates are likely to remain under pressure as Northern Hemisphere winter demand approaches.

Gold: Investors look beyond the immediate pressure from rising yields

Gold recovered towards USD 4,200, heading for its strongest weekly performance since early August despite a difficult macroeconomic backdrop. Surging US Treasury yields and a stronger dollar recently pushed bullion to a two-month low, before a well-received 30-year bond auction and some easing in oil prices helped trigger a recovery.

More importantly, investment demand has remained remarkably resilient throughout the bond-market selloff. World Gold Council data show global gold ETF holdings reaching a record 4,256 tonnes following inflows of 67 tonnes in September and 120 tonnes in August, despite the recent price correction.

This divergence suggests investors are looking beyond the immediate opportunity cost of holding a non-interest-bearing asset. While rising real yields traditionally weigh on gold by increasing the attraction of bonds, persistently elevated borrowing costs also carry longer-term consequences that could ultimately support bullion.

Two potential, albeit still unlikely, scenarios may help explain this continued interest.

In the first, high borrowing costs eventually undermine economic activity, exposing weaknesses in heavily leveraged sectors. A slowdown or recession would likely trigger renewed demand for government bonds, lower real yields and eventually easier monetary policy, supporting gold.

In the second, growth proves more resilient, but elevated yields increasingly strain public finances. With

government debt exceeding annual economic output in several major economies, rising debt-servicing costs could eventually force policymakers to intervene to stabilise bond markets. Such intervention, particularly if it undermines confidence in monetary discipline, could strengthen demand for gold as a store of value.

Neither outcome is inevitable, and further increases in real yields remain a near-term risk, while a roll-over may offer fresh support. Nevertheless, continued ETF accumulation suggests some investors are positioned for the potential consequences of elevated borrowing costs rather than simply responding to current interest-rate movements.

China's return from Golden Week adds another potentially supportive factor, coinciding with the start of a seasonally stronger period for physical gold demand. Indian festival and wedding-related buying traditionally provides additional fourth-quarter support. While elevated prices may restrain jewellery demand, renewed investment buying could challenge recent attempts by short sellers to push prices lower.

Industrial metals: China returns, but high prices challenge demand

Industrial metals have posted modest gains, led by copper and zinc, both rising around 1.9%. China's return from Golden Week has restored physical market activity, but the immediate demand picture remains mixed.

Copper inventories monitored by the three major futures exchanges have risen to just above one million tonnes, with COMEX accounting for approximately 71% of the total. Shanghai stocks increased following the holiday, while LME inventories declined, highlighting the uneven distribution of available metal.

Meanwhile, elevated prices are discouraging Chinese downstream consumers, many of whom remain reluctant to purchase beyond immediate requirements. Although the fourth quarter often brings renewed industrial activity and restocking, sustained gains will depend increasingly on evidence of stronger end-user demand rather than supply concerns alone.

Agriculture: El Niño threatens a growing weather shock

Agriculture has contributed to the weekly recovery, with gains across grains and soft commodities led by soybean meal, cotton, soybeans and sugar. An increasingly important development is the rapid strengthening of El Niño. The traditional Oceanic Niño Index reached 2.2°C for July–September, compared with approximately 1.7°C at the same stage of the powerful 2015–16 event, which subsequently peaked at 2.6°C. The latest NOAA outlook points to a high probability of an exceptionally strong event developing towards year-end.

Sugar is particularly exposed, with excessive rainfall potentially disrupting Brazilian harvesting while hotter and drier conditions threaten production in India and Thailand. Coffee production in Brazil and Southeast Asia also faces changing rainfall patterns, while heavy rains in West Africa have disrupted cocoa transportation and deliveries.

For grains and oilseeds, the impact will depend on the timing and geographical distribution of rainfall anomalies, making regional weather forecasts increasingly important.

El Niño also carries implications for energy demand. A potentially milder winter across parts of the Northern Hemisphere could reduce heating requirements and weigh on natural gas consumption, although regional weather patterns remain uncertain. The longer the event strengthens, the greater the risk that weather-related disruptions become a more dominant driver of commodity prices into 2027.

Outlook: Physical constraints remain a key uncertainty

The importance of physical tightness is illustrated by the chart above showing one-year implied roll yields across major commodity futures. In a balanced market, futures would normally trade in contango, with prices for later delivery higher than those for immediate delivery, reflecting financing, storage and insurance costs. With the US one-year overnight indexed swap (OIS) rate currently at 4.47%, this helps explain why several industrial and precious metals trade in modest contango, with negative implied roll yields broadly reflecting funding costs.

By contrast, a positive roll yield indicates backwardation, where buyers pay more for immediate delivery than future supply. The higher the yield, particularly when it exceeds funding costs, the stronger the indication of physical tightness and the premium attached to securing prompt supply. This remains particularly pronounced across energy markets, most notably in NY ULSD and London gasoil, where one-year implied roll yields exceed 25%. Such extreme backwardation highlights why recovering crude exports have yet to translate into normal conditions across the wider energy market.

For now, commodities remain caught between economic headwinds that threaten demand and physical constraints that support prices. Whether recovering crude exports translate into improved refinery output, whether gold continues to attract investment despite elevated yields, and how China's demand and El Niño develop will be critical in shaping the outlook for the final quarter and beyond.

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