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MACRO TOPICS

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POLICY: AS UP-TO-DATE AS GRANDMA'S TELEPHONE CHAIR

The topic of discussion at Jackson Hole this week should be: has monetarism run its course?

Japan publishes its monthly economic report this week while German PMIs are published on Wednesday followed by the Business Climate Index on Thursday. Investors and corporates will look for signs that monetary policy is supporting activity and growth. US home sales and house price monthly data are also published on Wednesday – key indicators for the health of the trans-Pacific container shipping market. US new jobless claims data are published on Thursday.

So when the governors of the US Federal Reserve gather in Jackson Hole this week, they will have a good stock of data to ground their discussions. They may nonetheless feel like they are staring into a policy abyss; namely, where do they go from here?

Stock market movements early in the week suggest that a buoyant tone may be struck, and that Governor Yellen will give an indication that interest rate increases are on the way. However, deflation still stalks the global economy, the US consumer remains belligerently pessimistic, labour participation rates are growing more slowly than actual employment rates (i.e. many people have stopped looking for work altogether) and wage inflation is of no great concern. So why raise rates?

It is becoming increasingly obvious that loose monetary policy is no longer effective in promoting growth. The ECB first introduced negative interest rates in mid-2014. The Bank of Japan implemented them in February 2015. Neither the Eurozone nor Japan have seen their economies reflate. Negative interest rates are encouraging corporates to hoard cash, slowing down the movement of money through the economy. Even my bus-conducting grandfather knew that money, like the buses, was made to go around. Mohamed El-Erian of Allianz covered the same ground with more sophisticated vocabulary last week when he declared that, "the collateral damage of negative interest rates far exceeds the benefits."

The US bucked the trend in December 2015 when, after numerous delays, it increased rates. The Fed's problem now is not just that there is little cause to increase rates now, but also that, when the next recession inevitably arises, it may have little room to cut rates and little cause to do so knowing that loose monetary policy has patchy, inconsistent and debatable benefits. The economic question that should be on the agenda this week is not "is monetary policy working?" but "has monetarism run its course?"

After the USD and DM were taken off the gold standard in 1971, the Bretton Woods system (implemented in 1945) was declared dead by 1973. Liberal democracies thereafter focused on interest rate policy as the main lever of economic growth. Monetarist shock therapy was applied to the Western industrial economies (including Japan), then the tiger economies of South East Asia, leading to the globalised system that China was able to take such great advantage of with its vast and cheap labour force. The party came to an end of course with the burst debt bubbles of 2008.

The global economy is now a very different shape to the economy of 40 years ago, just as the world of 1971 was different from that of 1945. It should therefore, be no surprise to anyone that the economic management techniques of the pre-digital age should be as redundant as a telephone with a rotary dial. But while we all now have smartphones, we continue to work in an economy built from 1970s vintage blueprints.

Perhaps the disgruntled populations of the liberal democracies and more volatile regions aren't being populist, stupid or irresponsible. Perhaps they sense that the time has come for deeper political and economic reform to create economic models and institutions as modern and as smart as our phones. One conclusion is clear: mainstream political parties offering more of the monetarist status quo are about as up-to-date as grandma's telephone chair.

DRY CARGO: WHEAT AND RUSSIAN EXPORT DUTIES

As this year's harvests are well under way, bumper harvests and low wheat prices put stress on farmers.

Over the past five years, the wheat markets have seen the price of the commodity fall significantly. Prices for hard red winter wheat No. 2 FOB from the US Gulf have slid to below USD 5 per bushel, from over USD 10 per bushel in the latter half of 2012. This drop corresponds to rising global wheat output over the same period, and more importantly ending stocks which are projected to grow to 622.1 Mn tonnes for the 2016/17 harvest, up from 454.95 in the 2012/13 harvest. The increase in ending stocks indicates that global supply has outstripped global demand growth over the same period, something which has made life very difficult for farmers as margins fade away.

In Russia, mid-August is when the hard red winter harvest ends and when the spring harvest kicks off and, according to the Russian Agriculture Ministry, this year is one for the record books. This year's crop is expected to yield no less than 110 Mn tonnes, up 2 Mn from the last record year in 2008 and, given the favourable weather, the ministry may raise estimates by 3-6 Mn tonnes. Russia is expected to export 25-30 Mn tonnes of wheat in the current marketing year which started on July 1.

However, for the farmers, the good harvest is dampened by the weak value of its produce, which is why, on Friday, Russian news agencies could report that according to a senior official at the Agriculture Ministry, a proposal to reduce the floating wheat export tax currently in place to zero until 1 July 2017 has been put forward. Rather than eliminating the duties all together, the proposal sent to the Russian government suggests lowering the tax level rather than abolishing it.

The current duty formula is half of the customs' price less 6,500 rubles (USD 102) per tonne, but not less than 10 rubles per tonne. The current price of Russian wheat basis the Black Sea is around USD 168 per tonne.

The primary purpose of this proposal is, of course, to protect the farmers, struggling to break even in the current glut, and simultaneously protect the nation's strategic food production capabilities. By lowering the current trade barrier, it is hoped that Russian wheat will become more attractive to international buyers, particularly as bumper harvests in the US also has led to plentiful supply of low-cost wheat.

Whether or not this will have any significant impact on tonne-mileage is questionable, yet a combination of large volumes of low protein content wheat coming out of the US, only suitable for feed grain, and horrendous harvests in Europe and South America, may result in some of that trade redirecting to the Black Sea region.

Sources: Affinity Research, Reuters

GAS: NORTH AMERICAN GAS STOCKS RISING SLUGGISHLY

Slowing stocks of natural gas could indicate the start of a rebalancing in the US.

The US EIA has reported that US natural gas stocks increased by around 22 billion cubic feet (BCF) for the week ending 12 August. This is smaller than many anticipated, with Reuters and Bloomberg expecting additions of between 25-35 BCF. After being traded down at USD 2.63 per MMBtu just before the EIA's statement, gas prices rose slightly on the news to USD 2.65 per MMBtu. This is a difference of around 35 cents from last year, having been priced around USD 3.03. Overall, stockpiles remain around 11 per cent higher than their levels a year ago, at around 3.339 TCF, and 14 per cent higher than the five-year average.

Although stockpiles have been rising, they have done so at a sluggish rate. According to Reuters, stockpiles have been rising slower for the last 17 weeks compared to previous years. The main reason has been that the warmest June, July and August on record have compelled the population to keep their air conditioners running cool. The availability of cheap gas has ensured that power producers choose to burn natural gas rather than other fuels.

The continued drive for natural gas for power generation over its coal counterpart will see CO_2 levels from natural gas top coal this year. This has mainly been down to cheap gas, and coal production falling to its lowest levels in 30 years. Despite this rise in CO_2 from natural gas, overall carbon intensity in the US has declined. Many states in the US have now successfully made the switch from coal to gas and many still seek to continue this trend. Michigan now has decided to shut down more of its coal-fired power plants by 2020 and will build up two new natural gas-fired power plants, totalling 170 MW. However, many states still understand that to lower CO_2 levels, one must change further. Those states now reliant on natural gas now seek to diversify their portfolio to include renewables as a lack of fuel diversity can be problematic. Especially if prices were to rise.

Even with low gas prices, the US natural rig count rose again by two this week up to 83. Although good news for producers, this is still far from its peak at 1,606 rigs in September 2008 and down 94 per cent in total. As the rig rate correlates significantly with the natural gas price, the slower inventory build-up could be good news. If the market starts to balance out and the uptake of cheap gas continues to draw on stocks, this could result in higher gas prices. Good news for producers and drill rigs, but potentially bad news for US LNG exporters seeking to compete with worldwide low gas prices.

Sources: Reuters, Bloomberg, Oil voice

CONTAINERS: PLANS… AN INVITATION TO DISAPPOINTMENT

Ports around the world are postponing their plans to expand their container cargo handling capacity.

DP World, the Dubai-based port and terminal operator, announced on Thursday that the planned expansion of container handling capacity at Jebel Ali, its flagship port, will slow down despite the company's increased profit reported in first-half of 2016.

According to the chairman and chief executive, the "challenging market conditions of 2015 have continued into 2016 with currency volatility, weak commodity prices and geopolitical issues contributing to uncertainty in domestic demand". As the global throughput growth remained "weak", DPW decided to delay capacity expansion at Jebel Ali. A slight volume decline in 2016-H1 in the port (at 7.4 million TEU, down by 6 per cent) supported DPW's decision to postpone the planned 1.5-million-TEU expansion of the new Terminal 3 next year. The development of the new Terminal 4 will slow down as well, linked to the "softer market conditions". DPW targets to operate its Jebel Ali ports at high utilisation. As mentioned in its latest earnings statement, the medium-term outlook still looks positive in the lead up to EXPO 2020, to be hosted in Dubai.

DPW's net profit for Jan-Jun reached USD 608 Mn (was USD 405 Mn in 2015), with revenues of USD 2.1 Bn, up by 10.2 per cent y-o-y. Non-organic activities, such as acquisitions (of Jebel Ali Free Zone in the UAE, Prince Rupert's Fairview Terminal on the Canadian Pacific Coast and the new container terminal at Yarimca in the Turkish Marmara Sea), brought some of this growth. Excluding these additions, net profit increased by 4.3 per cent, with an organic revenue growth of 2.5 per cent, as the company's total container volumes were up by 2.5 per cent y-o-y due to improved by growth in Europe and India, while conditions in Australia and Latin America remained "challenging".

Elsewhere, Jakarta port finally opened its new container terminal, the NPCT-1 or New Priok Container Terminal One, a month later than originally planned, as the operational license was so far not approved for undisclosed reasons.

The terminal is the first of a series to be developed in the new outer areas of Jakarta Port, known as Tanjung Priok. With an annual handling capacity of approximately 1.5 million TEU, an overall berth length of 850 metres and a depth alongside 16 metres, the terminal had trial operations already since May, with the 1,732-TEU "SINAR SUMBA". Commercial operations started with a call by the 1,618-TEU "UNI-PERFECT", a ship trading for Evergreen on the "TMI" service connecting Singapore, Thailand, Indonesia, and Malaysia.

A joint venture between the Indonesia Port Corporation, the Japanese Mitsui and NYK Line, and PSA International of Singapore, the terminal has four ULCS-sized ship-to-shore gantries and 20 RTG yard cranes. The number of quay cranes will double at a later stage. The need for extra cargo handling capacity was more than obvious as volumes grew rapidly, but more recently Jakarta's throughput has been suffering significant losses after 2013's all-time high. However, the port is expected to further expand in the longer term.

Acting as an Indonesian gateway and as a transhipment hub for the Indonesian archipelago, the port could compete with Singapore, Port Kelang and Tanjung Pelepas, but the port's last direct connection to Europe was CMA CGM and CSCL's "Sunday Express", closed 10 years ago.

Sources: Alphaliner

TANKERS: THRIVING AND SURVIVING

Production appears set to rise throughout Opec, while Chinese exports surge.

It is a testament to Opec's influence on the oil market, on the eve of its latest informal gathering to discuss an output freeze, that much of this page will be devoted to a number of its members.

Exports from Iraq are set to rise by 150,000 bpd – around 5 per cent – within the next few days after an agreement was reached between the state-run Northern Oil Co. (NOC) and the Kurdistan Regional Government (KRG). The Baba Gorgor, Jambour, and Khabbaz fields, which are owned by the NOC, halted production following a payment dispute with the KRG, which controls their export pipeline. Test pumping was conducted last week, and the NOC is aiming to return output to 150,000 bpd this week.

Over in West Africa, it was on Sunday announced that a conditional ceasefire was reached between militant group the Niger Delta Avengers and the Nigerian government. A number of militant groups have been carrying out attacks on Nigeria's oil infrastructure, but the Avengers are the most prominent and high profile. As a result of the attacks, Nigeria's crude oil production has fallen from around 2.3 Mn bpd to 1.56 Mn bpd. In order for Nigeria to meet its production target for the year, the country will have to produce an extra 1.1 Mn bpd.

Iran is likely to prove a stumbling block to a production freeze yet again. An Iranian press official has declared it unlikely that Iranian crude production will have risen to sufficient levels to cooperate with rivals by the time the meeting takes place in late September. In April, Iran claimed that output would have to rise to between 4 and 4.2 Mn bpd in order for it to consider participating in the deal. Production has risen since then, but it has stagnated at around 3.6 Mn bpd.

Market share very much remains at the forefront of Iran's thinking. Iranian Oil Minister Bijan Zanganeh recently revealed that negotiations on an oil swap with Russia are ongoing. The maximum capacity for a swap is 150,000 bpd, with the prize being that Iran would effectively have extra barrels available for export, which would likely be destined for the Persian Gulf. Moreover, production from the West Karun oil field is set to rise by 60,000 bpd to 280,000 bpd. Following on the heels of Saudi Arabia's near-record June exports, it would appear that, even if there is the intention to freeze output, Opec's members want their output as high as possible when the time comes.

Of further concern are China's growing exports. In July, China exported 1.53 Mn T of diesel and 970,000 T of gasoline. Year-on-year, these are rises of 182 per cent and 145 per cent respectively. This revelation will do nothing to alleviate concerns over the current glut, while also revealing an alarming drop-off in domestic demand. Refining margins are falling under heavier pressure, which may encourage Chinese refineries to reduce runs, resulting in a fall in crude demand.

Sources: Reuters, WSJ, FT

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