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COMMODITY PRICES TO DROP SHARPLY IN Q1... BUT WILL BOUNCE BACK BY YEAR-END

- TD Economics' Quarterly Economic Forecast, released earlier this week, contained a significant deterioration in the global economic outlook. Given that a credible solution is nowhere in sight, the sovereign debt crisis in Europe will likely intensify in the coming months. We suspect that Eurozone leaders and the European Central Bank will ultimately contain the crisis before it spreads into a global calamity, but not without some casualties. We believe Greece will default during the first half of the year, while the region as a whole will slide into a renewed recession – contracting by about 1.2%.
- While we expect a global financial crisis to be averted, financial stress and economic weakness in Europe will drag down growth in both the emerging markets and the advanced world. Overall, we project global economic activity to essentially stall next year, with growth of only 2.5%. The weakness will be concentrated in the first half of the year.
- Economic growth in key commodity-consuming countries, including China (+7.8%) and the U.S. (+1.9%), will be subpar in 2012, with a significant deceleration in activity occurring during the first two quarters. Investor confidence will also continue to deteriorate in the coming months. As a result, we have downwardly revised our commodity price forecast, with substantial declines expected in the first quarter.
- The good news is that we expect prices to bounce back strongly in the latter part of the year as economic conditions stabilize or improve. Accordingly, the annual average and Q4/Q4 forecasts mask some of the extreme weakness that we are predicting in commodity prices during the first half of the year.
- The accompanying tables contain our revised commodity price forecasts. The sectors that will be impacted most by this slowdown in global economic activity are energy and metals, as was the case during the 2008-09 recession.
- We now foresee WTI crude oil prices sliding to the low US$80s early in the year, before rebounding back above the US$100 per barrel mark in Q3. This pales in comparison to the US$30 per barrel prices that we saw during the last recession. However, this projected slowdown is not expected to be as pronounced, and geopolitical tensions in the Middle East will likely put a floor under how far prices will fall.
- Of all the base metals, copper is the most closely tied to economic growth given its use in construction and manufacturing. As such, the metal has been downgraded the most. We now expect copper prices to sink 12% in the first quarter, averaging US$3.00 per pound. Aluminum is projected to slide 13% in Q1, while nickel and zinc will drop 10% and 11%, respectively. The sizable drop in prices will set the stage for an even greater rebound, likely by the third quarter.

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- Despite its safe haven status, gold will also lose some ground in the near term, as investors will flock to U.S. Treasuries. We forecast gold prices to average US$1550 in the first quarter of 2012, before rebounding strongly next year, due in part to further quantitative easing by central banks in the U.S. and Europe. Similarly, we expect silver prices to slide to US$27 in Q1, but to head into 2013 at around US$44.
- We have scaled back our forecast for agricultural prices in 2012, reflecting weaker near-term demand from emerging markets and lower investor confidence. Nonetheless, prices will still remain elevated relative to historical averages.
- Forestry prices were downgraded only slightly in 2012, as the outlook for the U.S. housing market remains largely intact.
- Overall, the majority of the revisions are hidden in the quarterly profiles, with the rankings remaining largely the same as our previous forecast. We continue to expect precious metals to be a top performer in 2012, while the forestry sector will be slow to recover.
- Of course, there are risks to this forecast should the events in Europe play out differently than what we are forecasting. Either way, the volatility in commodity markets seen in recent months is going to persist until conditions in the Eurozone have at least stabilized.

COMMODITY PRICE FORECAST SUMMARY

	2011			Q4			Annual Average		
	Q1	Q2	Q3	2011F	2012F	2013F	2011F	2012F	2013F
FORESTRY									
LUMBER	297.47	267.91	265.16	262.00	290.00	330.00	273.14	270.00	310.00
PULP	967.16	1019.04	1000.50	925.00	925.00	960.00	977.93	908.75	950.00
NEWSPRINT	640.00	640.00	640.00	640.00	695.00	715.00	640.00	671.25	710.00
ENERGY									
OIL	94.02	102.60	89.70	93.00	102.00	105.00	94.83	95.00	103.75
NAT GAS	4.18	4.37	4.12	3.70	4.15	4.75	4.09	4.00	4.50
COAL	127.51	120.65	121.72	115.00	110.00	101.00	121.22	105.00	95.00
PRECIOUS METALS									
GOLD	1384.98	1506.96	1700.89	1714.00	2100.00	1700.00	1576.71	1856.25	1850.00
SILVER	31.80	38.59	38.88	32.80	44.00	28.00	35.52	36.44	32.50
NON-PRECIOUS METALS & MINERALS									
ALUMINUM	113.40	118.37	108.83	98.00	108.00	106.00	109.65	102.00	108.00
COPPER	437.89	415.50	407.89	340.00	415.00	370.00	400.32	381.25	380.00
NICKEL	12.20	11.03	10.00	8.30	8.85	8.25	10.38	8.65	8.51
ZINC	108.69	102.13	100.98	90.00	108.00	117.00	100.45	96.50	110.00
URANIUM	68.25	56.57	52.06	50.00	66.00	68.00	56.72	61.00	67.50
AGRICULTURE									
WHEAT	11.68	12.75	10.30	10.10	10.05	10.55	11.21	9.63	10.33
BARLEY	193.82	211.90	204.95	210.00	220.00	230.00	205.17	210.00	223.25
CANOLA	607.80	619.58	594.29	530.00	595.00	610.00	587.92	548.75	600.00
CATTLE	110.80	111.28	114.81	122.00	123.00	126.00	114.72	117.00	124.50
HOGS	86.03	94.10	93.42	89.00	90.00	96.00	90.64	86.00	93.25

COMMODITY PRICE FORECAST SUMMARY: % CHANGE									
	2011			Q4			Annual Average		
	Q1	Q2	Q3	2011F	2012F	2013F	2011F	2012F	2013F
FORESTRY									
LUMBER	11.1%	-9.9%	-1.0%	-2.1%	10.7%	13.8%	-3.3%	-1.1%	14.8%
PULP	-0.6%	5.4%	-1.8%	-4.9%	0.0%	3.8%	2.6%	-7.1%	4.5%
NEWSPRINT	0.0%	0.0%	0.0%	0.0%	8.6%	2.9%	5.6%	4.9%	5.8%
ENERGY									
OIL	10.5%	9.1%	-12.6%	9.3%	9.7%	2.9%	19.4%	0.2%	9.2%
NATURAL GAS	10.0%	4.5%	-5.6%	-2.6%	12.2%	14.5%	-6.7%	-2.3%	12.5%
COAL	18.0%	-5.4%	0.9%	6.4%	-4.3%	-8.2%	22.5%	-13.4%	-9.5%
PRECIOUS METALS									
GOLD	1.3%	8.8%	12.9%	25.3%	22.5%	-19.0%	28.8%	17.7%	-0.3%
SILVER	20.0%	21.4%	0.7%	23.7%	34.1%	-36.4%	75.8%	2.6%	-10.8%
NON-PRECIOUS METALS & MINERALS									
ALUMINUM	6.6%	4.4%	-8.1%	-7.9%	10.2%	-1.9%	11.2%	-7.0%	5.9%
COPPER	11.7%	-5.1%	-1.8%	-13.3%	22.1%	-10.8%	17.1%	-4.8%	-0.3%
NICKEL	13.9%	-9.6%	-9.3%	-22.5%	6.6%	-6.8%	5.0%	-16.7%	-1.6%
ZINC	3.5%	-6.0%	-1.1%	-14.3%	20.0%	8.3%	2.4%	-3.9%	14.0%
URANIUM	18.7%	-17.1%	-8.0%	-13.0%	32.0%	3.0%	21.7%	7.5%	10.7%
AGRICULTURE									
WHEAT	31.1%	9.2%	-19.2%	13.4%	-0.5%	5.0%	48.0%	-14.1%	7.3%
BARLEY	10.9%	9.3%	-3.3%	20.1%	4.8%	4.5%	31.8%	2.4%	6.3%
CANOLA	11.8%	1.9%	-4.1%	-2.5%	12.3%	2.5%	30.1%	-6.7%	9.3%
CATTLE	10.4%	0.4%	3.2%	21.5%	0.8%	2.4%	20.8%	2.0%	6.4%
HOGS	20.7%	9.4%	-0.7%	24.9%	1.1%	6.7%	19.9%	-5.1%	8.4%

MEASURES & QUOTED PRICES ($ is US$ unless stated otherwise;
C$ prices converted to US$ using daily C$/US$ exchange rate).

FORESTRY*

Lumber: Random Lengths' Framing Lumber Composite ($/1000 Bd Ft)
Pulp: NBSK, delivered in east U.S. ($/mt)
Newsprint: New York ($/mt)

ENERGY**

Oil: Domestic Spot Market Price: West Texas Intermediate, Cushing ($/Barrel)
Natural Gas: Henry Hub, LA ($/mmbtu)
Coal: Austr. Therm ($/mt)

PRECIOUS METALS**

Silver: Cash price: Silver, Troy Oz, Handy & Harman Base Price ($/Troy oz)
Gold: Cash Price: London Gold Bullion, PM Fix ($/Troy oz)

NON-PRECIOUS METALS & MINERALS**

Aluminum: LME Aluminum, 99.7% Purity: Closing Cash Price (Cents/lb)
Copper: LME Copper, Grade A: Closing Cash Price (Cents/lb)
Nickel: LME Nickel: Closing Cash Price ($/lb)
Zinc: LME Zinc: Closing Cash Price (Cents/lb)
Uranium: Ux U308 ($/lb)

AGRICULTURE*

Wheat: Srping,14%Protein: Minneapolis ($/bu)
Barley: Canada: Cash Prices: Feed Barley: Lethbridge: Grade 1 CW (C$/mt)
Canola: Canada: Cash Pr: Canola: Instore Vancouver: Grade 1 Canada NCC (C$/mt)
Cattle: Live Cattle Futures Price: 1st Expiring Contract Open (Cents/lb)
Hogs: Lean Hogs Futures Price: 1st Expiring Contract Open (Cents/lb)

Sources: WSJ, FT, Ux Weekly, Random Lenghts, Pulp & Paper Weekly, GlobalCoal, Comtex, WCE, FRBNY / Haver Analytics.
* Forecasts by TD Economics; ** Forecasts by TD Securities