

**August 29, 2006**
**„Stronger for longer“ ?!**

On the LME nickel market, one record high chases another. For the first time the 3 months quote has touched the 30,000.00 USD/mt mark. The cash price had already climbed over this hurdle since the premium for spot delivery had risen considerably due to the presumed shortage of nickel. At times the backwardation (cash to 3 months) was up to USD 5,650.00/mt. The backwardation for one day (“tom-next”) traded at USD 1,000.00/mt prompting an intervention by the LME in an attempt at calming the market. Since the 18th August 2006, the maximum limit for the backwardation for a single day is now USD 300.00/mt. Calculating a backwardation of 90 days (cash to 3 months) there could be a theoretical maximum value of USD 27,000.00/mt (premium on the 3 months quotation!). The idea behind this market regulation is to try to ensure that the holders of market controlling long positions do not exploit their dominant role by trying to force holders of short positions, not being able to deliver physically, to close out their positions by asking for higher than justified premiums. But then again, just what is justifiable in a market with an artificial shortage? USD 300.00/mt per day?

It is interesting to note that according to a report published by the LME each trading day, 50 to 80% of nickel warrants (secured LME nickel stocks) are to be found held in one hand. In another standard report of the LME, also from the 25th August 2006 (Futures Banding Report), it is mentioned that 20 to 30% of due long positions in Nickel for the November date, i.e. 15th November, are in the control of one market participant alone. This means that between 11,000 mt and 17,000 mt with a market value, at today’s rates, of around USD 328 to USD 528 million are held in one hand. From this example the dominating presence of single market participants on the LME can be clearly seen. In this scenario even the impartial observer must query quite critically the functionality of the price mechanism of the LME. But in the end even that does not help very much.

A possible third way between the two camps, that of the proponents of the super cycle and those awaiting for the bubble to burst, has been put forward by the head of Rio Tinto, Leigh Clifford. He too doubts the super cycle, but does admit that we are dealing with quite a robust and long bull phase. The reasons for this lie especially in the missed exploration of further stock repositories in the “weak” years. With his description “stronger for longer” but not “stronger for ever” he hits the nail on the head.

The summer “silly season” with little news provides an opportunity to look into topics for which normally there is no time. This should however not be like when 2nd or 3rd rate politicians get hold of subject matter and fill the media with their nonsense, for on the sidelines there are indeed interesting matters to report.

Liquidity for a company is a blessing, for it protects against the inability to pay and so against insolvency. That liquidity can also be a risk factor was a point raised in an article in the “Handelsblatt” at the beginning of this year. The relevance of this article has become more acute since the beginning of the year. The main point of the article was that speculative bubbles – in the judgement of many analysts seen also in the metal markets – are often the result of exorbitant liquidity supplies. There is the danger that speculators react irrationally since high liquidity tries to seek investments with high returns. This can however only be attained with a correspondingly high level of risk. Reasons for such high levels of liquidity lie mainly in the historically low levels of interest rates of the central banks, in the considerable national savings of the Asian boom countries and in the record revenues of the oil and raw material producing countries. Should these surplus funds flow uncontrollably into the capital and commodity markets, then there is the danger of a new speculative bubble evolving, as reported already by the Handelsblatt. If commodity rates of today are compared to those at the beginning of this year, then the impression is that this has already happened. The 3 months nickel price, today quoted at just under USD 30,000.00/mt, dealt on 3rd January 2006, the first dealing day of the year on the LME, at between USD 13,400.00/mt and USD 13,900.00/mt. It is not now falling rates which are the best argument for investors to invest in commodities, for not only are long maintained valuation factors ignored, but also fundamental market data is pushed more and more into the background. Finally in this connection a correction is being threatened by inflation, for the central banks are now starting to look more closely and seriously at this phenomenon.

**LME (London Metal Exchange)**

**LME Official Close (3 month)**

August 29, 2006			
	Nickel (Ni)	Copper (Cu)	Aluminium (Al)
Official Close 3 Month Ask	29.500,00 USD/mt	7.430,00 USD/mt	2.480,00 USD/mt

**LME stocks in mt**

	July 24, 2006	August 29, 2006	Delta in mt	Delta in %
Nickel (Ni)	5.448	5.808	+ 360	+ 6,61%
Copper (Cu)	97.300	124.125	+ 26.825	+ 27,57%
Aluminium (Al)	731.650	718.300	- 13.350	- 1,82%