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International: 1-877-888-2565

USA: 1-888-888-2565



**GLOBALWAX LLC**

One Bethany Rd. Suite 74  
Hazlet, NJ 07730 U.S.A

Phone: 732-888-1900 • Fax: 732-888-0900  
Email: [info@globalwax.net](mailto:info@globalwax.net)

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## **Palm Oil Bouncing Off Highs While Crude Tries to Gain Momentum; Chinese Paraffin Inches Higher**

**Palm Oil** (prices in Malaysian Ringgit (RM) per MT, \$ value based on most recent exchange rates)

Crude Palm Oil (CPO) has had been in a very volatile uptrend since bottoming out last November near RM1,400/mt (\$378), closing Friday at RM1,972 (\$532), an increase of about 40%. Fundamental factors of steady demand and dwindling inventories has help maintain this rally through 2009 but as the price chart indicates, currently CPO is in a very tight RM100 consolidated range between RM2,025 (\$547) and RM1,925 (\$519) with the uptrend losing a lot of steam. On a technical basis, we expect CPO to break out of this tight range over the next couple of weeks which will give greater indication of future market direction. In the short-term we see continued price volatility in this tight range and will wait for the consolidation to resolve on its own on a price spike either up or down. Due to the several factors outlined below, we believe it is very likely that this breakout will be to the downside with a potential retrace in CPO back to the RM1,750 (\$472) area.

Despite decent demand for CPO helping to support this rally, current economic conditions cannot support such price levels and demand should weaken as the global economic recession continues to spread. One key problem in CPO pricing of late is that there are still very tight supply issues with respect to palm oil which is still keeping prices up and may lead to some more price spikes just over RM2,000. However for the longer-term, we see several factors that will not support prices to remain at these levels for long.

First, as noted above, global demand will continue to fall and take off some of the price and supply pressure from palm. Second, palm oil's discount to soybean oil has dropped considerably from over \$400 to close to \$100 over the past 6- months and there



should be less and less palm for soy substitution as there was in the past. Unless CPO drops in price, it will become uncompetitive with soybean oil. Third, CPO has gone against the trends in soybean oil and crude oil and made recent highs while both soybean oil and crude oil have been testing their lows in February of this year. The fundamental factors pushing CPO of late have shown a decoupling of the correlation between CPO and crude oil to some extent. This makes CPO as a bio-diesel less and less attractive. There just does not seem to be enough global demand, economic growth or interest in bio-fuels with crude at current low levels, to push palm that much higher.

Overall, we have a nice consolidation range forming on CPO and in the short-term, tight supply issues in Asia will help keep CPO prices at current levels and we may see some price spikes back to the RM2,000 – RM2,100 range (\$540 - \$566). However, for the longer-term, we believe the fundamentals cannot sustain CPO at these prices and we expect a distinct breakout to the downside and a move in the next 3 – 4 months to the RM1,600 – RM1,700 range (\$432 - \$459). We will continue to monitor the price chart to catch any breakout from the current range.

### Crude Oil (\$ per barrel)



After making new lows in mid-Feb, Crude Oil began a steady climb back into the upper \$40s. Price action has been quite volatile as a result of various forecasts trying to assess the effects of the global recession on global demand in 2009. Despite the spreading global recession and cuts in 2009 demand forecasts, oil has been forming a V-bottom base in trying to find price support. Some of this has been buying a result of OPEC cutting back production and people trying to predict the bottom in this recession. Many countries have cut back demand but the

supply of oil is still greater than current demand in the short-term and we are not convinced that economic conditions have changed enough to support the sharp price increase from \$38 to almost \$48 a barrel over the past month.

Crude Oil is moving higher in a tight price channel and we feel that we could see crude back in the low \$40s in the next few weeks with a fear that it will breakout and possibly re-test those February lows. The economic data and global demand as of yet does not support price increases back to the \$50s so we are wary of this rally and would not put much faith into it unless we were able to break out of this channel into the low \$50s and stay there for more than an intra-day price spike. We believe the next short-term move in oil is back to the \$42-\$44 range and longer-term projections are more difficult to ascertain given the lack of clarity in future direction of the U.S. economy and government stimulus effects.

## Soybean Oil (\$ per pound)

Soybean oil continues to struggle even with CPO and crude oil pushing higher the past few weeks. Soy has been bouncing against \$0.30 price support the past month and we think that it will once again dip in the upper \$0.20s as continued weak demand from the global recession puts a short-term ceiling on prices. In general changing weather patterns in the U.S. and Argentina, the two largest producers of soybeans, will cause some price volatility but we see a general pricing range between \$0.29 and \$0.32 for a little while longer as the market looks for some directional guidance in the global economy.

However, just as with CPO and crude oil, soybean oil is also facing reduced demand and downward pricing pressures and we expect this to continue and are watching closely any move below \$0.29. A strong close below these levels could mean new lows over the next month or two. Given current market conditions, we feel new lows are more likely.



## Chinese Paraffin Wax (\$ per MT FOB)

The past year or so has seen some of the most volatile price swings in Chinese paraffin wax ever with prices dropping over 50% from last Fall to the beginning of this year. As the global economic crisis worsened and the price of oil collapsed, and China ramped up inventories to record levels just as demand dropped sharply, the fundamentals were in place for a staggering crash in the price of all grades of Chinese paraffin wax. Recently, we have seen some support forming in pricing and a positive turn in some of the fundamentals.

After building up excessive inventories during last year's price surges, most Chinese refineries cut back production drastically and dropped prices rapidly to move product. Currently, refineries are operating at about 30% and demand has picked up since the beginning of the year. Most of the excess inventory has been moved and supplies are actually tightening a bit across some grades which has led to price increases of \$40 to \$50 off of earlier lows for most grades. With inventories reduced to more normal levels and some increases in demand, we expect Chinese paraffin to continue to show price stabilization with additional price increases to come in small increments as inventory levels will be maintained lower to avoid the oversupply problems faced at the end of last year.

Crude oil has shown price support as well which should also help price stabilization in Chinese paraffin. We would like to stress, however, that recent price movements in Chinese paraffin are still predicated on supply/demand issues and even if

crude oil slips back as we fear, Chinese paraffin should hold current pricing levels. The big question mark right now is how far and wide the current global economic crisis will spread and to what extent which could affect future demand. For this reason we do not expect Chinese refineries to ramp up production too quickly so that they do not overshoot demand and hurt their pricing power. Even outside of China, many refineries around the world have extended their recent shutdown periods for maintenance to reduce production levels and supply while moving excess inventory.

Based on these factors, we expect Chinese paraffin to continue to hold current prices across all grades with possible future price increases in the coming weeks as supply conditions continue to tighten. Demand has started to pick up slowly and should continue to do so as long as the global economic crisis does not take a turn for the worse.

If you have any questions or comments about this report or are interested in price quotes on any products, please contact:

***Philip Budwick***  
***GLOBALWAX LLC***  
***Tel 202 365 8328***  
***pbudwick@globalwax.net***