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October 11, 2023

WisdomTree Europe

WisdomTree Commodity Outlook – Cycles, China and the Energy Transition

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October 2023

Commodity Outlook 2023/24

Cycles, China and the Energy Transition

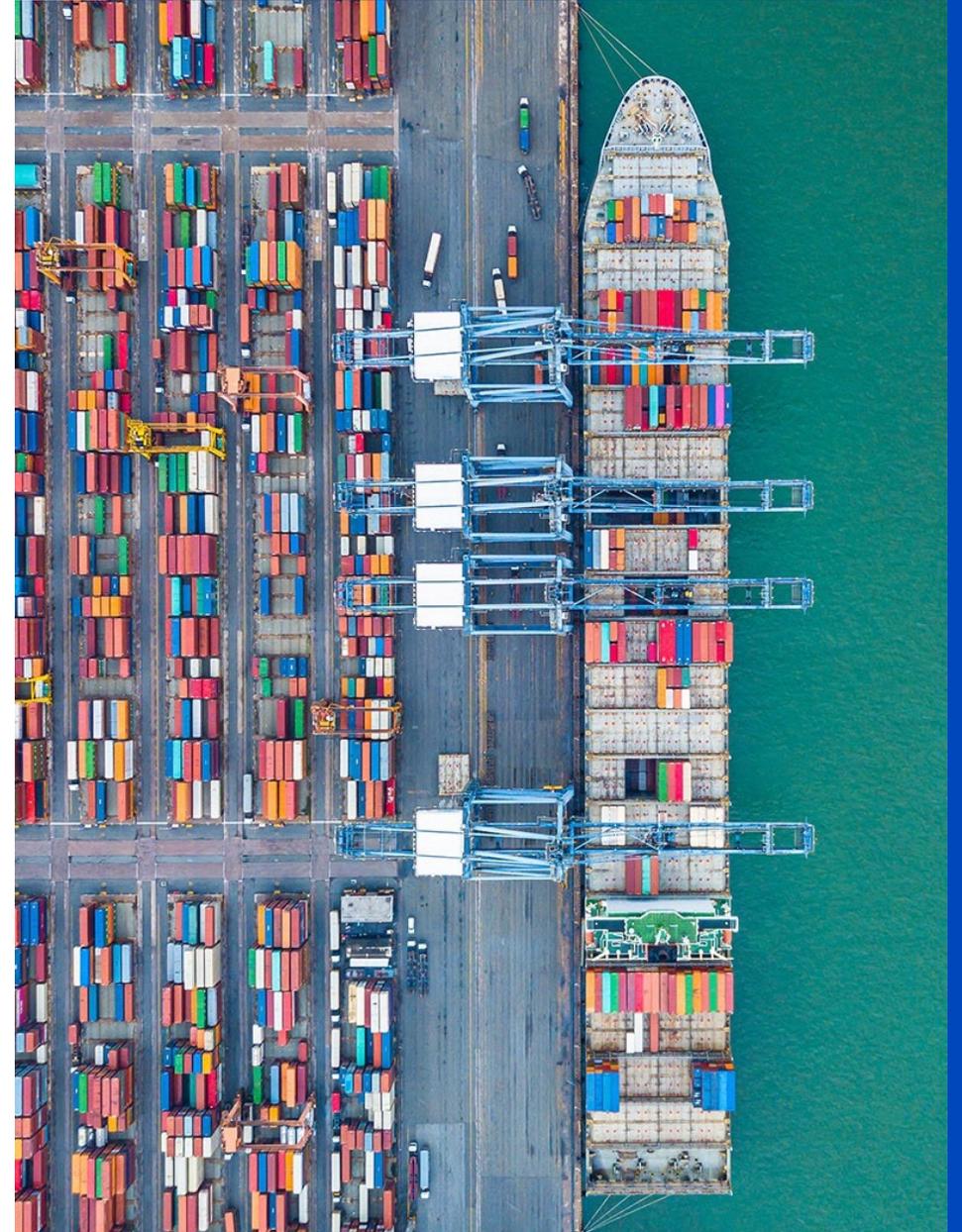




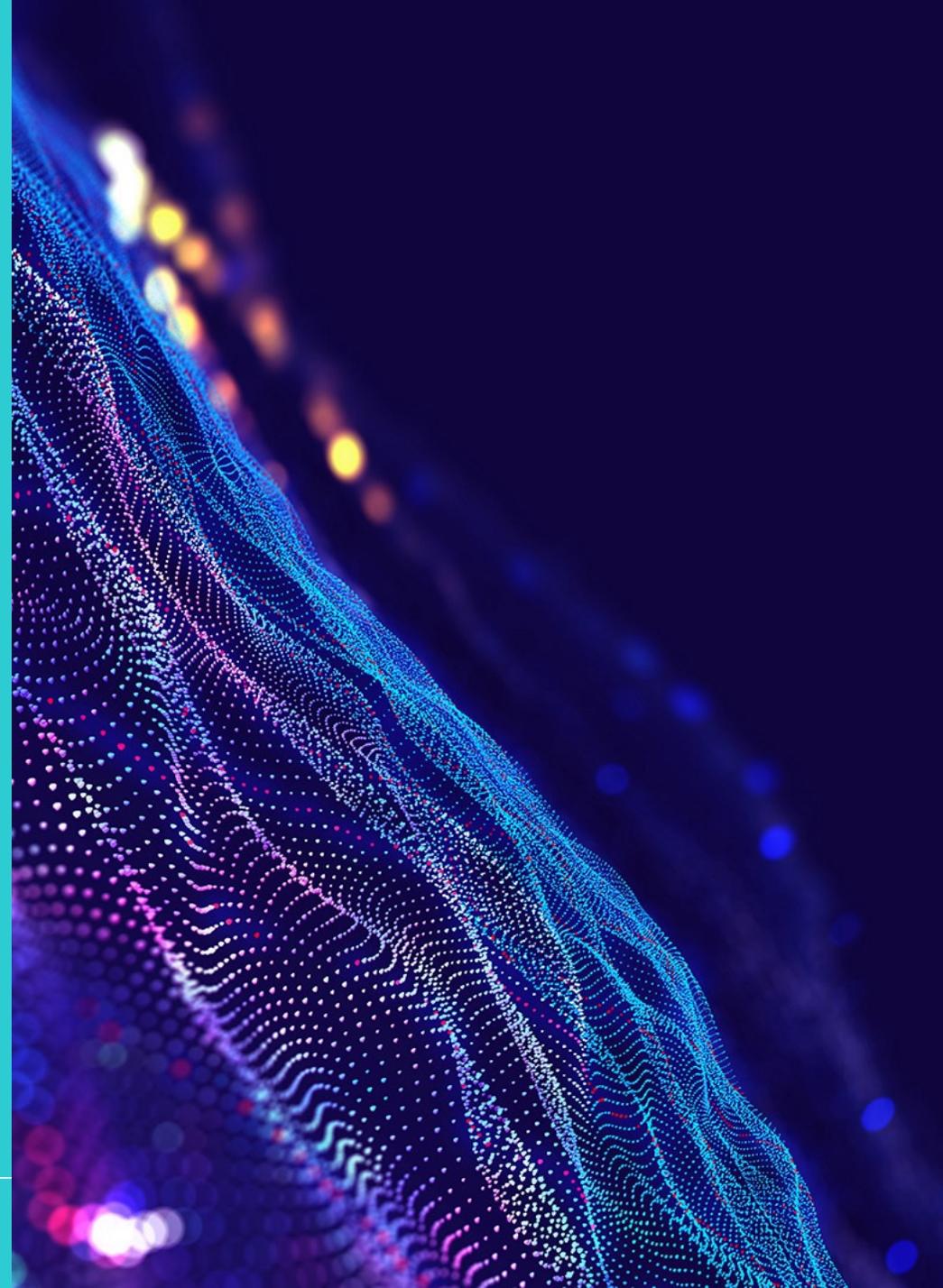
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1.

Cyclical recovery

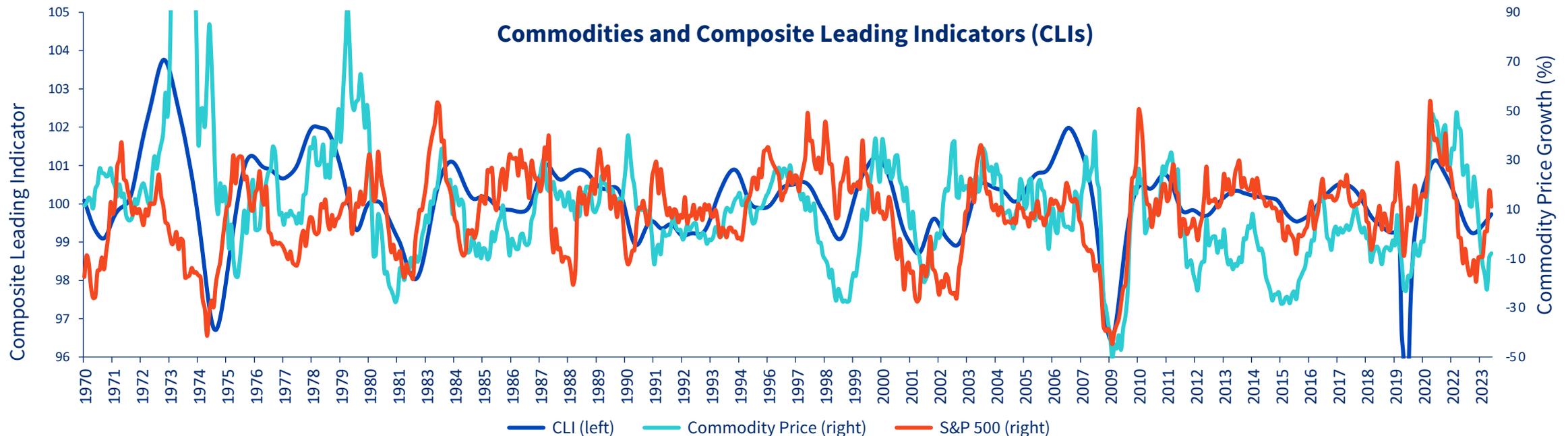


Leading indicators point to a turn in global economic cycle



Composite Leading Indicators bottomed out earlier this year

- Cyclical assets like equities have been recovering
- Commodities are beginning to turn



Source: Bloomberg, The Organisation for Economic Co-operation and Development, WisdomTree. January 1970 to July 2023. CLIs for G20 nations. The OECD system of Composite Leading Indicators (CLIs) is designed to provide early signals of turning points in business cycle

Historical performance is not an indication of future performance and any investments may go down in value.

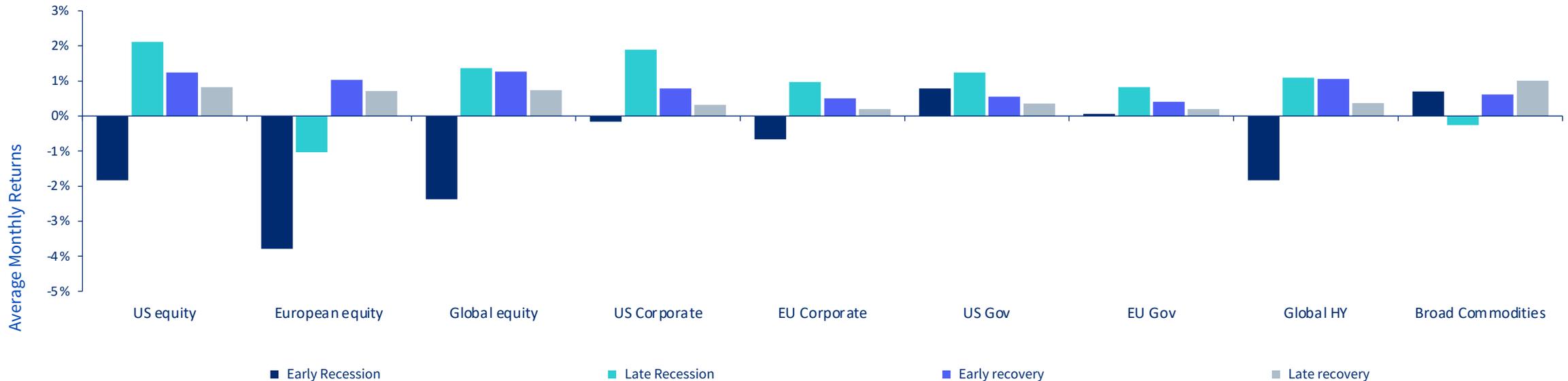
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Commodities are a late-cycle performer

The time for commodities is coming

- Historically, equities start to perform earlier in economic cycle (positive in late recession)
- Commodities tend to still post losses in late recession but pick up as the recovery starts
- Commodities perform even better in late recovery

Asset performance in different phases of economic cycle



Source: WisdomTree, Bloomberg, National Bureau of Economic Research, WisdomTree. January 1960 to June 2023. ‘Early’ is defined as the first half of an economic phase. ‘Late’ is defined as the second half of an economic phase. To account for different lengths of recessions and recoveries, monthly returns have been time weighted. Asset descriptions at the end. Historical performance is not an indication of future performance and any investments may go down in value.

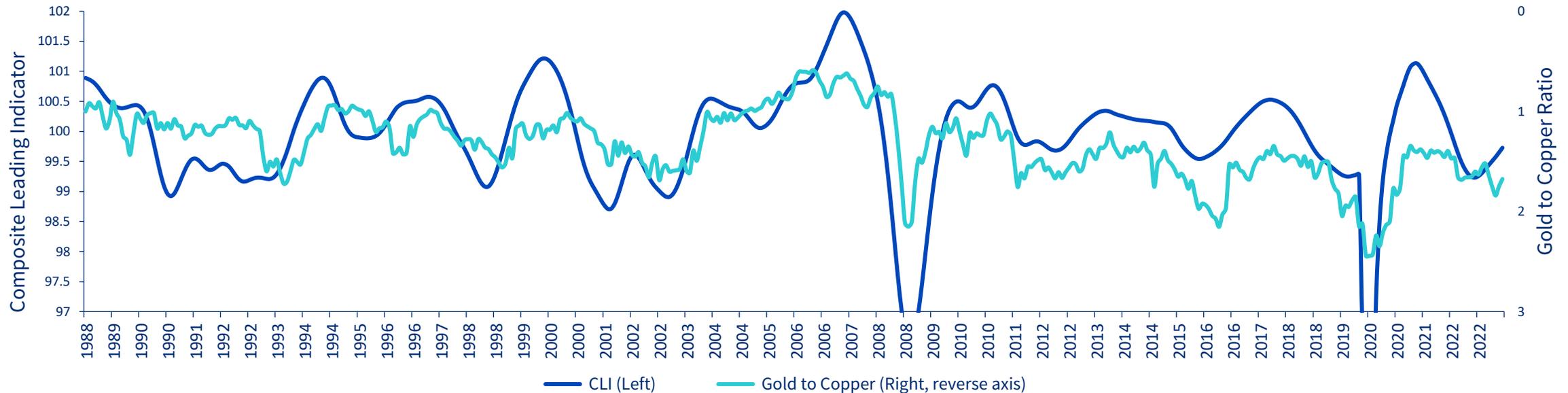
Commodity gains likely to shift from defensives, like gold, to cyclicals



Gold has been the best performing commodity in 2023 YTD

- Gold is a defensive asset and has done well in a time of economic, financial and geopolitical uncertainty
- But as we progress through the economic cycle, we expect cyclical commodities, like copper, to prosper

Cyclicals to gain favour over defensives as market turns



Source: Bloomberg, The Organisation for Economic Co-operation and Development, WisdomTree. December 1988 to July 2023. CLIs for G20 nations. Historical performance is not an indication of future performance and any investments may go down in value.

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2.

China woes



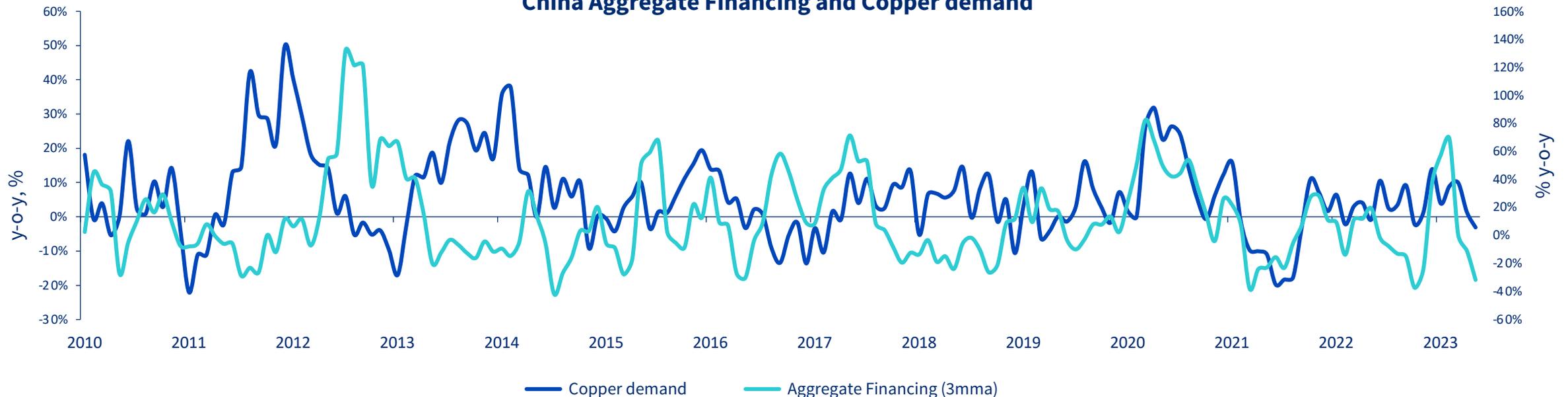
China's disappointment casts a dark cloud on commodities



China numbers disappoint

- China's post-COVID-19 reopening recovery has fallen short of expectations
- Aggregate financing to the real economy in July 2023 was at the lowest level since 2017, but August 2023 numbers picked up briskly
- Historically, metal demand in China has been strongly linked to financing conditions

China Aggregate Financing and Copper demand

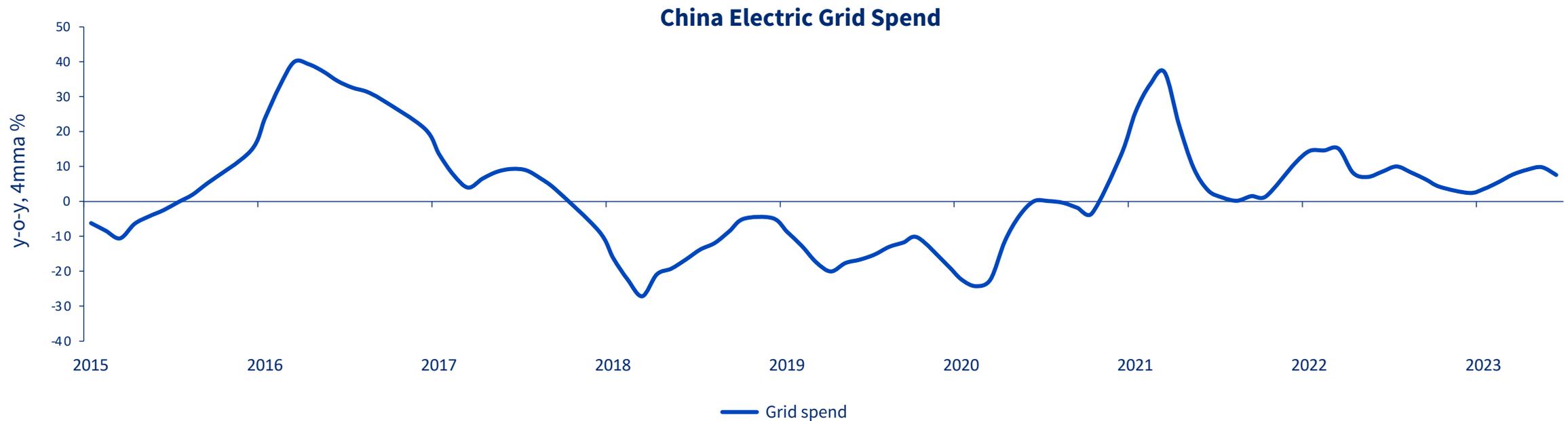


Source: Bloomberg, WisdomTree. January 2010 to August 2023. Combines old and new Total Social Financing measures to get a longer aggregate financing timeseries, but reader should be aware of definitional changes in 2018. Historical performance is not an indication of future performance and any investments may go down in value.

China's strategic planning may lend structural support

China grid spending on the rise

- Electric grid building is very copper intensive
- China is accelerating electric grid spending, taking advantage of relatively cheap copper prices and trying to catch up on net-zero commitments



Source: Bloomberg, WisdomTree. March 2015 to August 2023. 4 month moving average
Historical performance is not an indication of future performance and any investments may go down in value.

No Bazooka but a long list of piece-meal stimulus in China

Date	Measure
2 June 2023	State Council confirmed more support for Electric Vehicles, with details to follow later by The Ministry of Commerce (Mofcom) and The Ministry of Finance (MoF)
13 June 2023	10bps open market operations (OMO) seven-day reverse repo rate cut
15 June 2023	15 bps medium-term lending facility (MLF) cut
20 June 2023	10 bps loan prime rate (LPR) cut for both 1-yr and 5-yr
29 June 2023	State Council pledged to promote home decoration and home appliance consumption
30 June 2023	The People's Bank of China (PBoC) added RMB200bn relending quota to support agriculture, small to medium sized businesses and the private sector
7 July 2023	National Development and Reform Commission (NDRC) set up project-loan connection mechanism with 7 banks including policy banks to support investment
10 July 2023	PBoC The National Administration of Financial Regulation (NAFR) extended the 16 measures to support the property sector to the end of 2024
12 July 2023	Premier Li Qiang held a conference with major platform companies after PBoC and NAFR signalled an end to the regulatory revamp earlier on 7 July
12 July 2023	Mofcom issued a document supporting consumption of home appliances and decorations
14 July 2023	PBoC confirmed a soft but real cut on outstanding mortgage rates
19 July 2023	The Chinese Communist Party and State Council issued a joint document to support the private economy
21 July 2023	Ministries led by the NDRC issues a document to support consumption of electronics and autos
21 July 2023	State Council mentions support to old village redevelopment in mega/extra-big cities
24 July 2023	NDRC publishes a document to support private investment
27 July 2023	Ministry of Housing and Urban-Rural Development (MOHURD) hinted at more property easing, including lowering down-payment ratio and mortgage rate, tax and fee cuts for upgrade transactions
28 July 2023	Ministry of Industry and Information Technology (MIIT) issued an action plan to stabilise light industries
31 July 2023	NDRC issued a document containing 20 measures to restore and expand consumption
1 August 2023	NDRC unveiled detailed measures to bolster private economy
13 August 2023	State Council issues guidance to attract Foreign Direct Investment
15 August 2023	The first asymmetric policy rate cuts from the PBoC with 10pbs OMO rate cut and 15bps MLF rate cut
21 August 2023	10bps cut 1-year LPR and no change on 5-year LPR (disappointment relative to expectations)

In recent months, the pace of piece-meal policy announcements have intensified



Source: Government announcements, various media



3

El Niño returns



El Niño impacts weather and thus crop growing conditions and energy demand

The World Meteorological Organization (WMO) forecasts that there is a 90% probability of the El Niño event continuing during the second half of 2023.

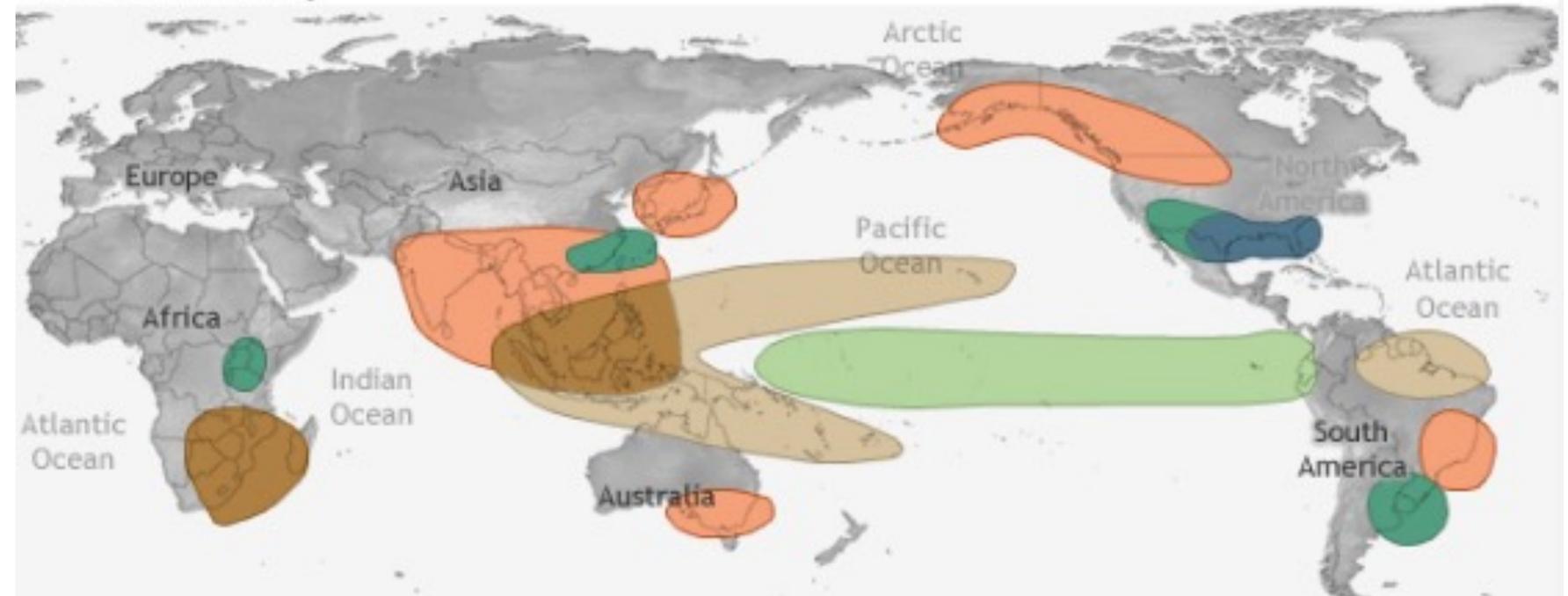
What is the El Niño phenomenon?

The El Niño Southern Oscillation (ENSO) is an oceanic-atmospheric phenomenon whose origins lie in abnormal variations in surface water temperatures in the Central and Eastern Pacific (Latin American coast).

When El Niño starts picking up – trade winds slow down and the warm water near Asia starts moving back eastward across the Pacific, reaching the coast of South America. The drift in warm water also moves evaporation and rain such that southeast Asia and Australia tend to get drier while Peru and Ecuador tend to see more precipitation.

El Niño typically picks up over the summer and shows its strongest effects over the winter in the Northern Hemisphere.

EL NIÑO CLIMATE IMPACTS December-February



Source: World Meteorological Organization (WMO) , National Oceanic and Atmospheric Organisation (NOAA).

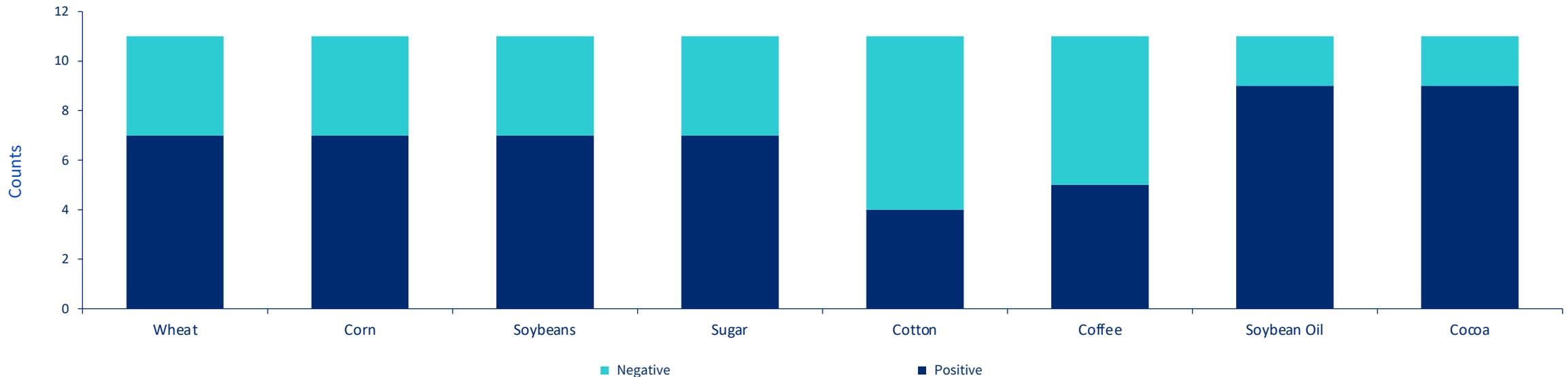
El Niño could be another catalyst for commodity price gains

El Niño has generally been price-positive for agricultural commodities



- In 8 of the last 11 occurrences, wheat, soybean oil and cocoa traded higher by an average of 14%, 6% and 16% respectively, 6 months after the El Niño started
- In 9 out of the past 11 occurrences, soybean oil and cocoa traded higher

Price performance 6 months after start of El Niño



Source: National Oceanic and Atmospheric Organisation (NOAA), Bloomberg, WisdomTree, data from January 1963 to July 2023. Based on the last 11 El Niño episodes since 1963 for all commodities. Historical performance is not an indication of future performance and any investments may go down in value.



4

Oil outlook

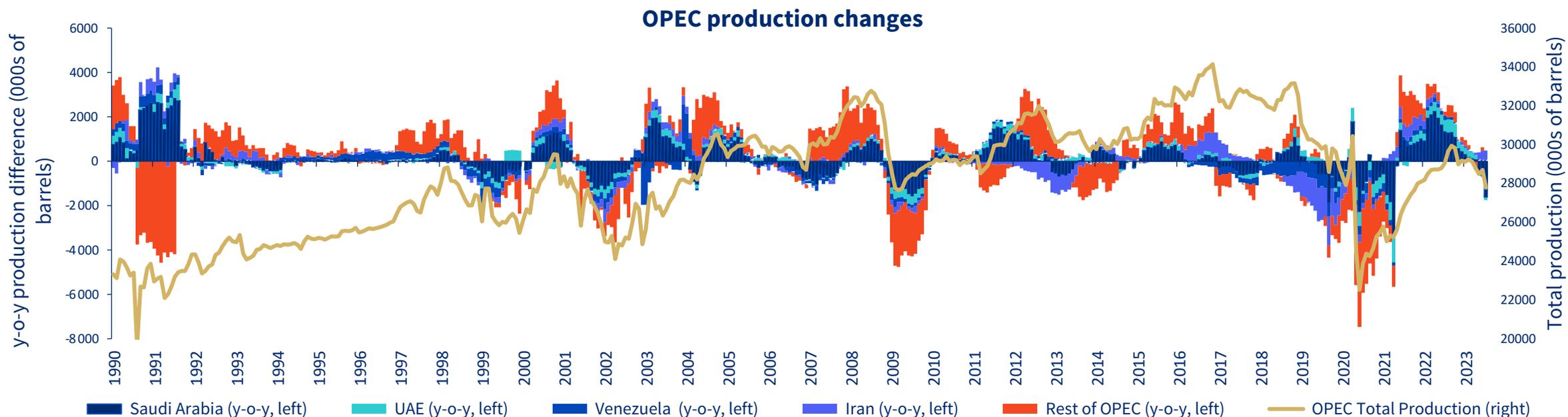


Oil markets are tightening as OPEC slams on the brakes

Organization for Petroleum Exporting Countries (OPEC) aggressively cuts back on production.



- Most OPEC countries are still struggling to keep up with their quotas
- Saudi Arabia made massive voluntary cuts
- OPEC's allies, like Russia, are also cutting back aggressively



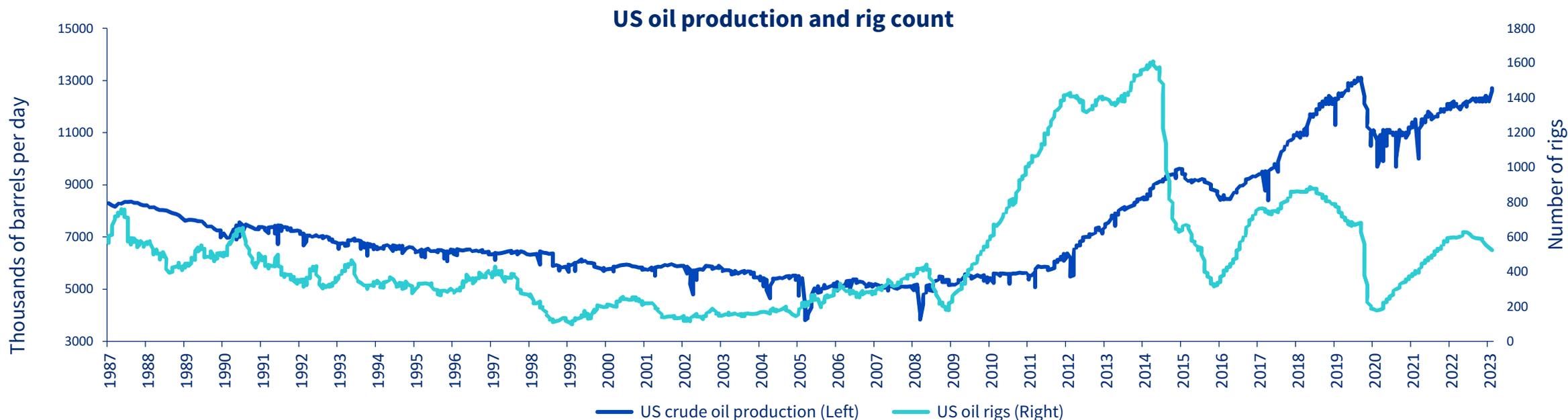
Source: Bloomberg, WisdomTree. January 1990 to July 2023. Historical performance is not an indication of future performance and any investments may go down in value.

US oil production rising despite rig counts contracting

Despite rigs in operation declining, US oil production keeps rising



- US's lead over Saudi Arabia and Russia keeps widening as it expands production while the latter contract

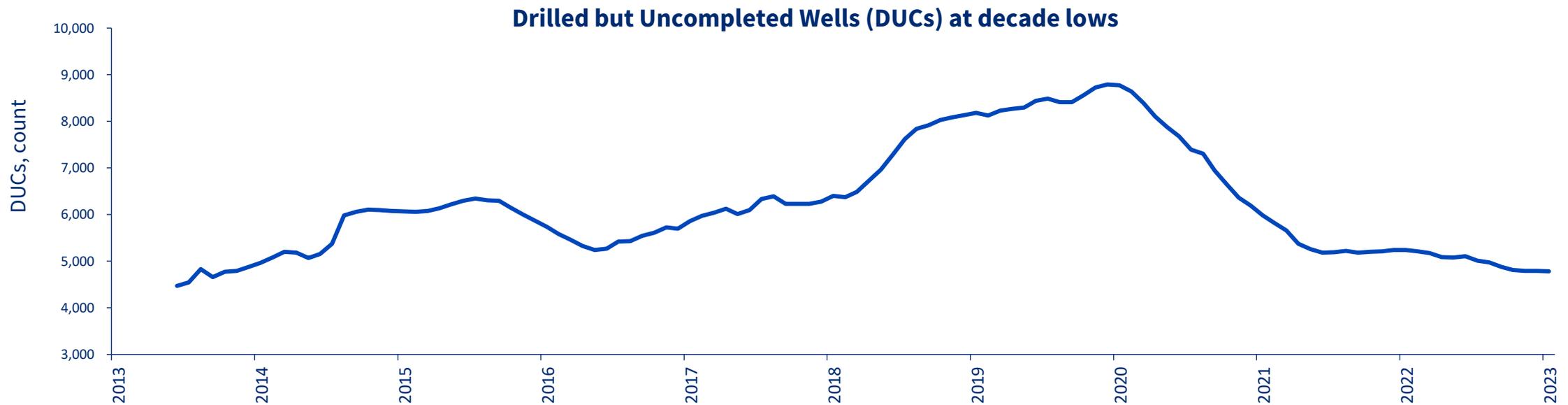


Source: Bloomberg, Energy Information Administration, WisdomTree. July 1987 to July 2023. Historical performance is not an indication of future performance and any investments may go down in value.

US production fuelled by wells drilled in the past

We question how long US production can keep rising

- Drilled but uncompleted (DUCs) wells are often opened when financing conditions are tighter, and demand looks less certain
- That requires less new drilling
- Given DUCs are finite, using past drilling to increase current production cannot last forever



Source: Energy Information Administration, December 2013 to July 2023. Historical performance is not an indication of future performance and any investments may go down in value.



5.

Gold outlook



Gold defying bond headwinds....



Gold vs real rates (Treasury Inflation-Protected Securities yield)



Source: WisdomTree, Bloomberg, 01/03/2023 – 22/09/2023

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...and strong Dollar headwinds



Gold vs Dollar Basket



Source: WisdomTree, Bloomberg, 02/01/2023 – 22/09/2023

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...but institutional flows into gold exchange traded products remain negative



Gold held in exchange-traded products



Source: WisdomTree, Bloomberg, 01/01/2015 – 22/09/2023

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...and institutional sentiment remains muted

Net speculative positioning in gold futures



Source: WisdomTree, Bloomberg, 01/04/2015 – 22/09/2023

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Retail demand, however, is very strong especially in emerging markets



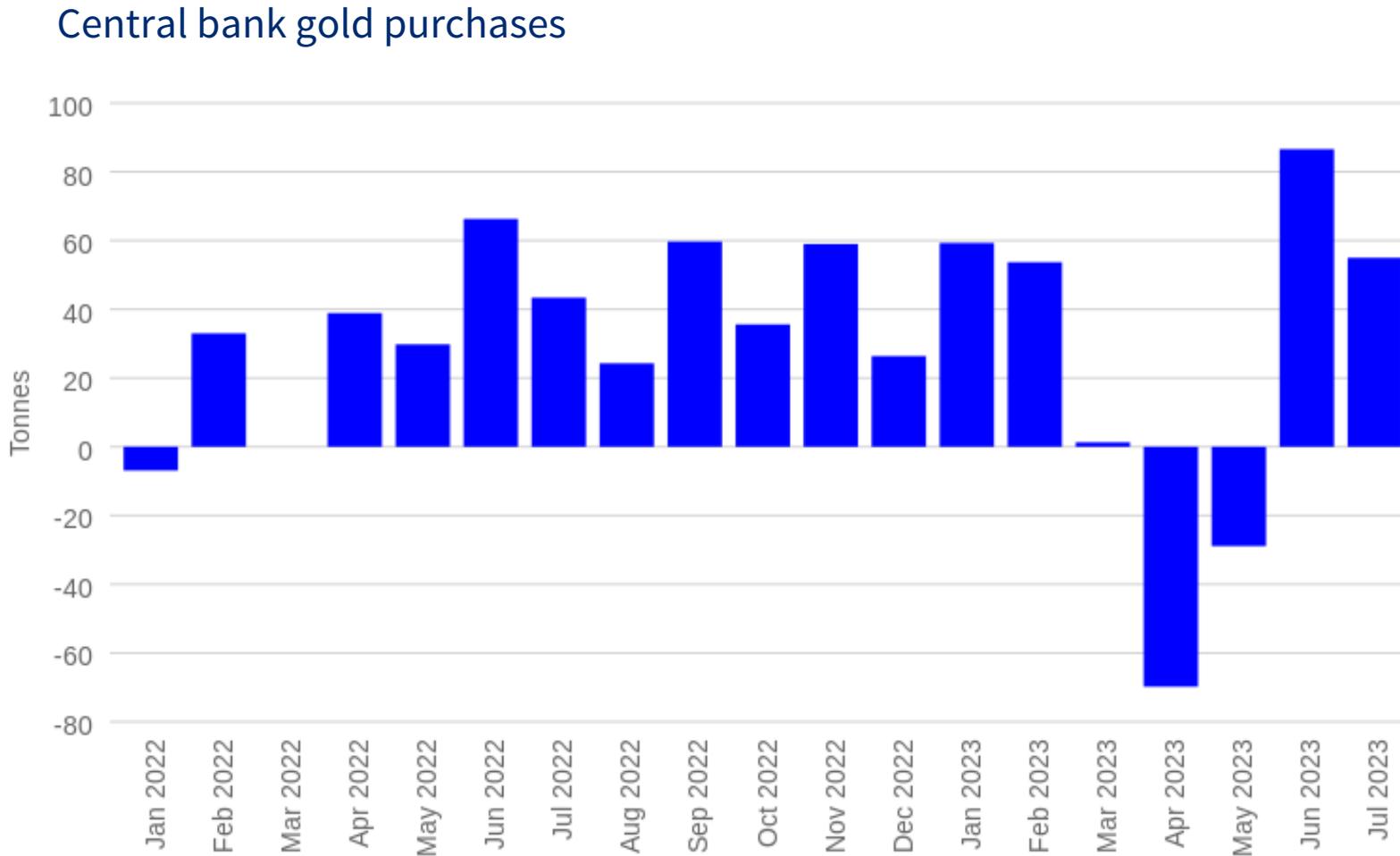
Shanghai Gold Premium



Source: WisdomTree, Bloomberg, February 2010 – September 2023. 30-day moving average.
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Central banks are continuing to buy at record levels



Source: WisdomTree, International Monetary Fund, World Gold Council. January 2022 – July 2023.
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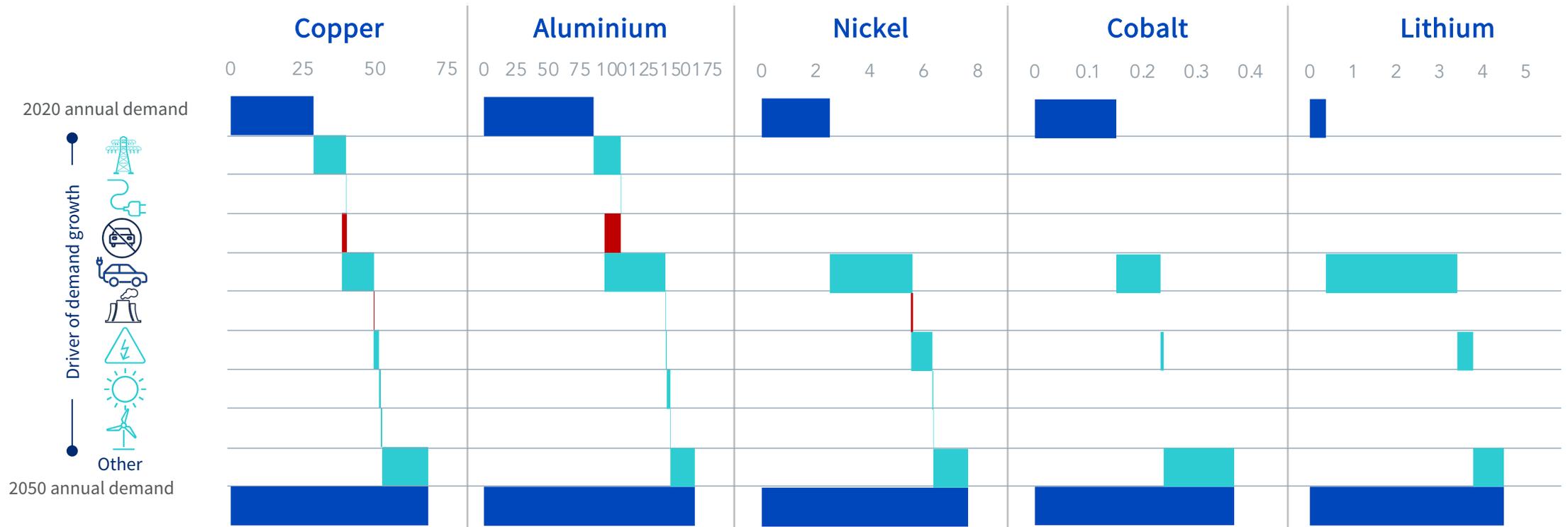


6.

Green arms race



The energy transition could be the largest driver of metal demand



Transmission
 Charging infrastructure
 Internal combustion vehicles
 Electric vehicles
 Other power
 Energy storage systems
 Solar generation
 Wind generation

Source: Wood Mackenzie, 2023. Forecasts aligned to 1.5 degree scenario. Data presented in Millions of Tonnes. Negative growth in red. Forecasts are not an indicator of future performance and any investments are subject to risks and uncertainties.

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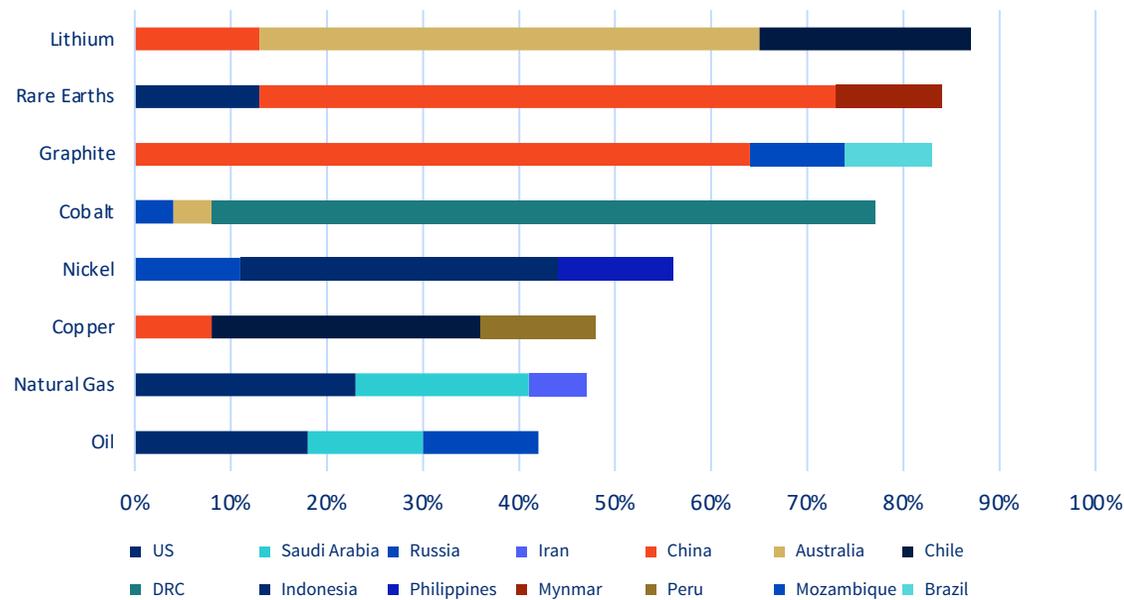
Sourcing critical raw materials will remain a challenge for the energy transition



Extraction resources are geographically concentrated

Weaning away from hydrocarbon resources is a challenge because metal mining is even more geographically concentrated than oil and gas

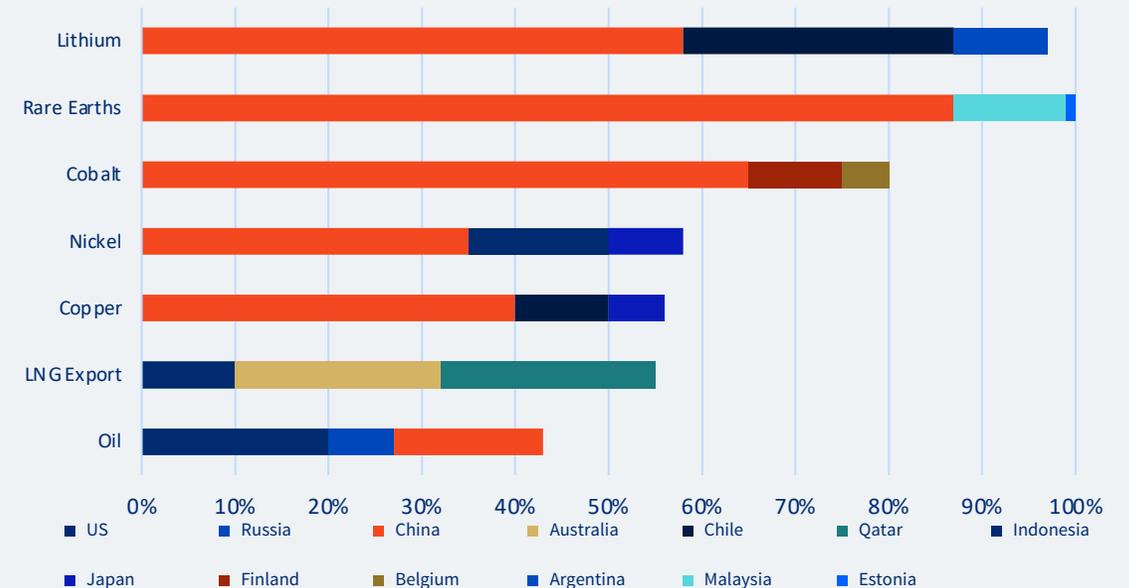
Top 3 Extraction Countries, Market Share



Processing resources are even more geographically concentrated, with China dominating

China dominates in every metal processing value chain

Top 3 Processing Countries, Market Share



Source: International Energy Agency, WisdomTree, 2021. LNG = liquefied natural gas; US = United States; DRC = Democratic Republic of Congo. Historical performance is not an indication of future performance and any investments may go down in value.

Green arms race

Inflation Reduction Act

The 2022 Inflation Reduction Act (IRA) in the USA aims to spur investment in domestic green technology. The majority of the \$394 billion in energy and climate funding in the IRA is in the form of tax credits with strings attached to local sourcing and processing.

REPowerEU

The European Union launched REPowerEU, an ambitious plan to reduce EU dependence on fossil-fuel imports and accelerate the green transition.

In July 2023, the European Investment Bank (EIB) increased the financing targets by 50% to €45 billion until 2027. This additional financing is expected to mobilise over €150 billion in new green investments, helping Europe cut its carbon emissions to net zero by 2050.

Critical Raw Material Act

New legislation currently being discussed by the European Union tripartite to onshore more of the supply chain (see next slide)



Sources: Data from The White House (2022) and The European Investment Bank (2023).

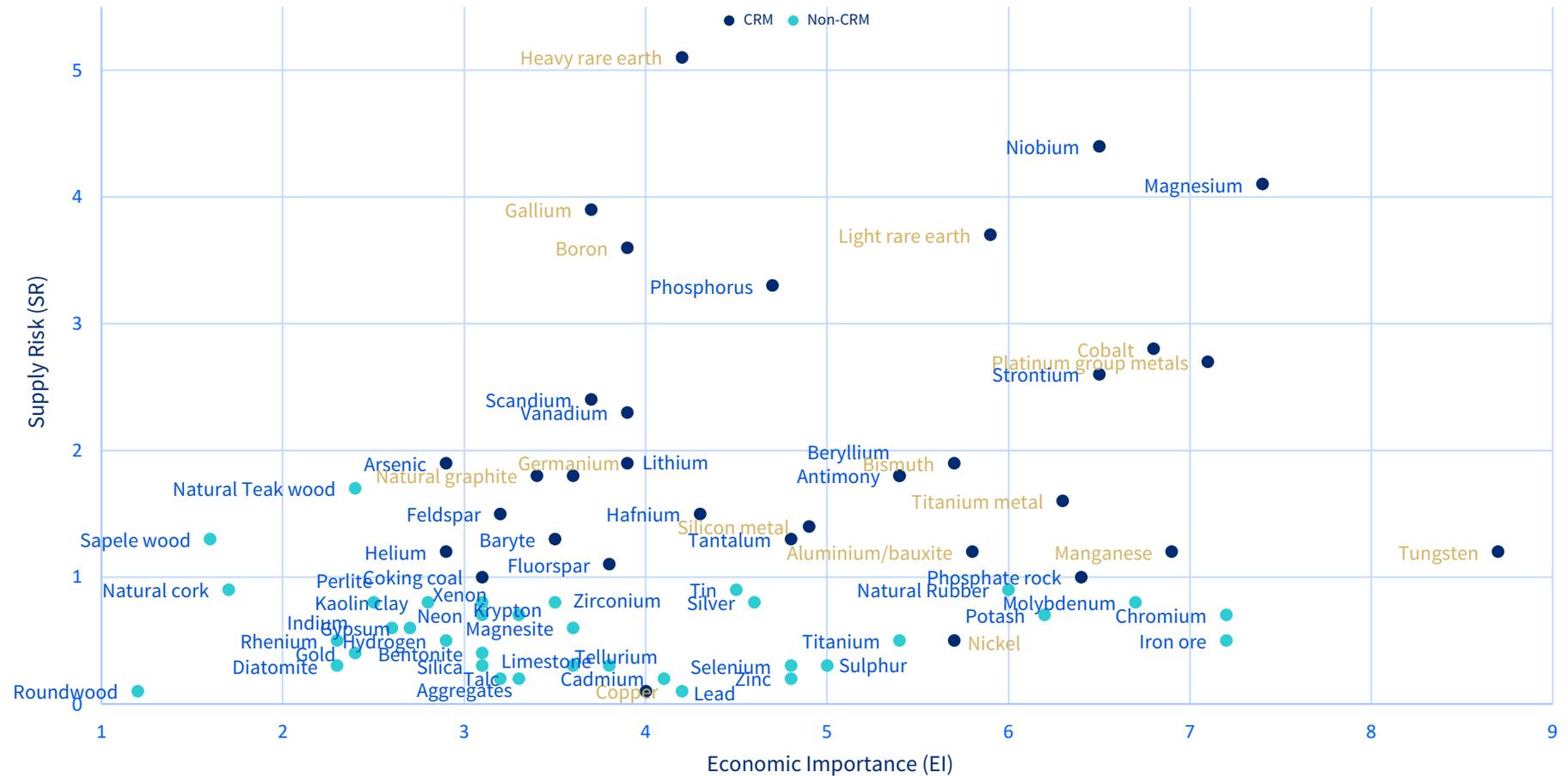
European Union prepares for local sourcing



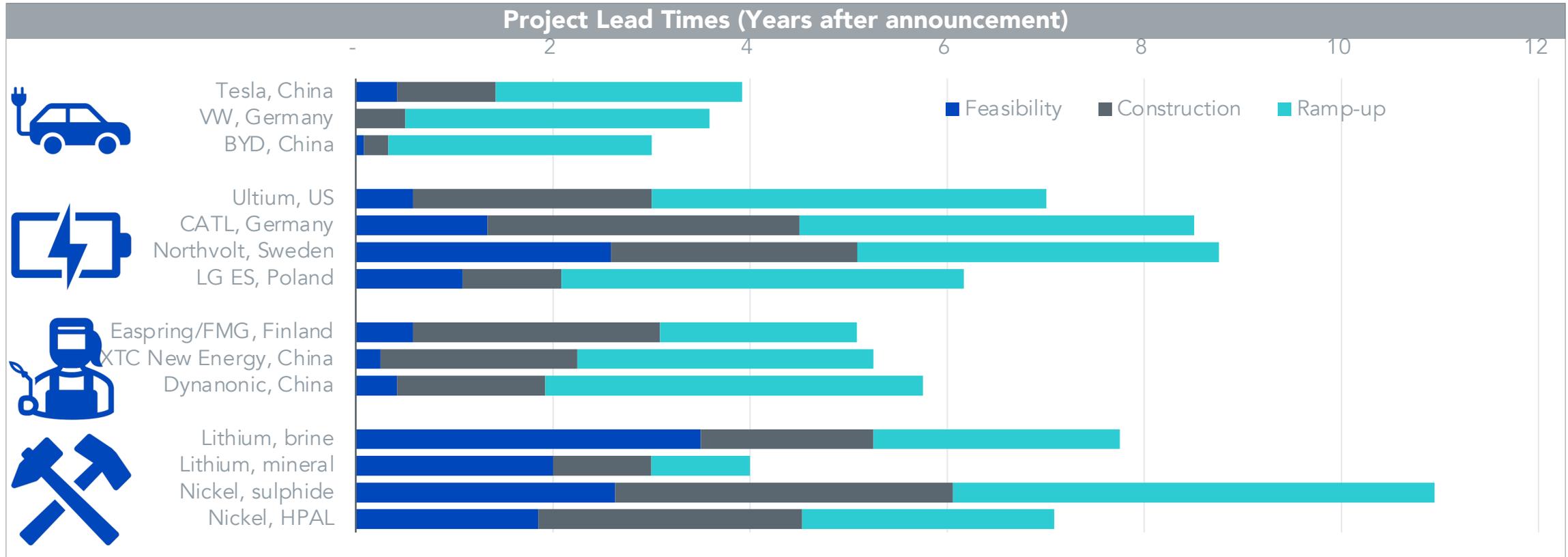
Critical Raw Material (CRM) Act

The European Commission's Critical Raw Materials Act proposal sets hard targets for domestic capacities in Strategic Raw Materials by 2030. The European Council's counter-proposal sets even higher targets (Council's proposals in parenthesis):

- at least 10% of the EU's annual consumption for extraction
- at least 40% (50%) of the EU's annual consumption for processing
- at least 15% (20%) of the EU's annual consumption for recycling
- no more than 65% of the EU's annual consumption from a single third country



Long lead times for projects



Source: Wood Mackenzie, based on historical examples of timelines

HPAL = High Pressure Acid Leaching

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Electric vehicles



Batteries



Cathodes



Raw material extraction

Resource nationalisation

- Chile (second largest lithium producer, with largest lithium reserves) has threatened to nationalise the industry
- Chile is also the largest copper producer in the world and has mining royalties to bring its mining taxes to highest level in world

Knowledge gaps

Significant knowledge gaps are likely to inhibit rapid production of raw material processing and mining capabilities



Reshoring/onshoring

IRA, CRM Act are examples of efforts to bring more supply chain production close to the consumer market

Tit-for-tat trade restrictions

China will restrict the exports of gallium and germanium - used in semiconductors and electric vehicles

Questions

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Asset descriptions



Asset	Index	Bloomberg code
US equity	S&P 500 Total Return Index	SPXT Index
European equity	EURO STOXX 50 Net Return EUR	SX5T Index
Global equity	MSCI World Net Total Return USD Index	NDDUWI Index
US Corporate	Bloomberg U.S. Corporate Investment Grade	LUACTRUU Index
EU Corporate	Bloomberg Euro-Aggregate: Corporates	LECPTRUH Index
US Gov	Bloomberg US Government Bond	LUAGTRUU Index
EU Gov	Bloomberg Euro Government	H02001US Index
Global HY	Bloomberg Global High Yield	LG30TRUH Index
Commodities	Bloomberg Commodity Total Return	BCOMTR Index

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