

There has been significant volatility in markets recently with string of negative macroeconomic developments. The fear of default of Greece debt leading to a banking crisis in France and Italy, slowing growth in developed market, tight monetary policy stand in emerging nations causing contraction in manufacturing to service sector- all pointing towards a double dip recession.

Commodities- mostly industrial commodities which are directly linked to a global growth has a fear of demand slowdown. "Hot Money" which is also a major factor for asset price appreciation is likely to get a blow if any banking crisis hit the Euro zone. The low rate regime that lead to a "V" shaped recovery of the global economy has also causes significant appreciation of commodities from past two years.

Now we are at a critical juncture where all major economic data releases from the EU and US suggest a possible negative reading of growth as early as Q1 2011. The austerity measures that have been taken by European Nations will dampen the long term growth story. Countries such as France, Italy, Greece, Portugal, and Ireland will see significant impact on growth due to cut in fiscal spending. In a recession or a downturn, it is believed that fiscal spending revives economic activity through multiplier effect. Apart from the political deadlock between EU nations on bailout fund norms may lead to further worsening of situations.

Gold which is regarded as a flight of safety rose to a fresh historic high of \$1920 an ounce on 6th September along with other safe assets like US T Bills, German Bund and UK Gilt. Now, even Gold prices are under pressure on fear of a banking crisis in the Euro zone which may be resulted from default of Greece Sovereign debt.

Exposure to Greece debt by Institutions

Company	Exposure (Bonds and Bills)	Business
Marfin	€2.3 billion	Marfin Investment Group is a Greek investment company
Societe Generale	€2.9 billion	Global Financial Service
Commerzbank	€2.9 billion	Global Financial Service
Generali	€3.0 billion	Italy's largest insurance company.
Hellenic Post bank	€3.1 billion	Hellenic Post bank is a Greek savings bank.
Dexia	€3.5 billion	Diversified Belgian financial services company.
Alpha Bank	€3.7 billion	Greece's second biggest bank.
ATE Bank	€4.6 billion	Greek commercial bank
BNP Paribas	€5.0 billion	Global Financial Service
Bank of Greece legacy loans	€6.0 billion	
FMS	€6.3 billion	German bailed out banks Depfa and Hypo Real Estate
Euro bank EFG	€9.0 billion	Greek bank, ranking the country's third largest.
Piraeus Bank	€9.4 billion	Greek bank with a presence in Eastern Europe.
The National Bank of Greece	€13.7 billion	

Date collected from various website for reference

From bullion perspective, a banking crisis may lead to a healthy correction in prices. The long term fundamental of Gold as alternative currency and safe haven investment is intact while drying up of liquidity due to redemption pressure may lead to some long liquidation of fund houses as well as from retailers. The same situation was observed during 2008 subprime crisis when gold prices dropped to \$680 an ounce from a high of \$1032.40 an ounce. However, in the long term such as for next 2-3 years gold will remain attractive for investment. Silver which is mostly used in industrial sector may see additional pressure on prices.

Short-term View on commodities

In case of base metals, Copper prices are expected to drop despite supply cut due to strike in producing nations. Mine workers throughout the developing world have downed tools in recent months, demanding a greater share of mining profits at a time metals are fetching high prices on international markets. Chile's 2011 copper production will likely total 5.4 million metric tons, virtually flat from last year, state copper commission said. Cochilco lowered its forecast of 5.7 million tons due to production stoppages at some of the Andean nation's largest mines because of labor strikes and severe weather. Despite supply tightness, the demand is expected to slowdown from major consuming nation such as China. China apparent consumption has been on a decline. Usage from China was down by 6% in Jan-June 2011. The net imports from China have declined by 40% in first half of the year compared with corresponding period previous year.

In other metals such as Zinc where bank financing deals have been blocking almost 60% of Zinc in LME warehouse may see some pressure in prices if a banking crisis hits. Zinc with soft fundamentals is expected to see surplus till 2012, market expects. In such as situation, Zinc prices remain depressed in the short term.

In energies, Crude oil is prices are also expected to see declines. Already prices have fallen almost \$35 a barrel from the high posted during May 2011 as geo-political risk premium reduced. Recently, OPEC sharply revised down its forecast for world oil demand for this year and expected consumption would remain weak in 2012. The group slashed its global oil demand forecast by 150,000 barrels per day for 2011 and by 40,000 barrels per day for 2012.

Oil supply issue has been addressed as Saudi Arabia and other Gulf producers raised output this summer to make up for the loss in Libyan exports. To compensate the loss of output of 1.6 million barrels a day from Libyan crude, Saudi raised output above 9.8 million barrels a day by June from around 9.1 million in February. OPEC's 12 member countries expect Libyan oil production to recover enough to reach one million barrels a day within six months.

So all in all a major correction in commodities such as metals and energy is underway and on an average we may see prices dropping at least 15-20% from September level. In case of Gold, correction may be mild and long term investors may look for bargain buying.

While taking from the Indian perspective, the decline may be limited with depreciation of Indian rupee v/s the US dollar. The USDINR has gained over 13% from past three month and likely to reach fresh historic levels such as 52 in next 3-5 months.

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