Commodities Strategy

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Commodities' contrasting outlook: Gold's momentum, metals' caution, oil's equilibrium

- **Higher gold prices are sustainable due to strong underlying drivers.**
- **Following a sharp rally, we are now cautious on silver and copper.**
- **We expect Brent crude to trade between USD55/bbl and USD70/bbl.**
- **We look at why commodity ETFs do not always track their underlying's prices.**

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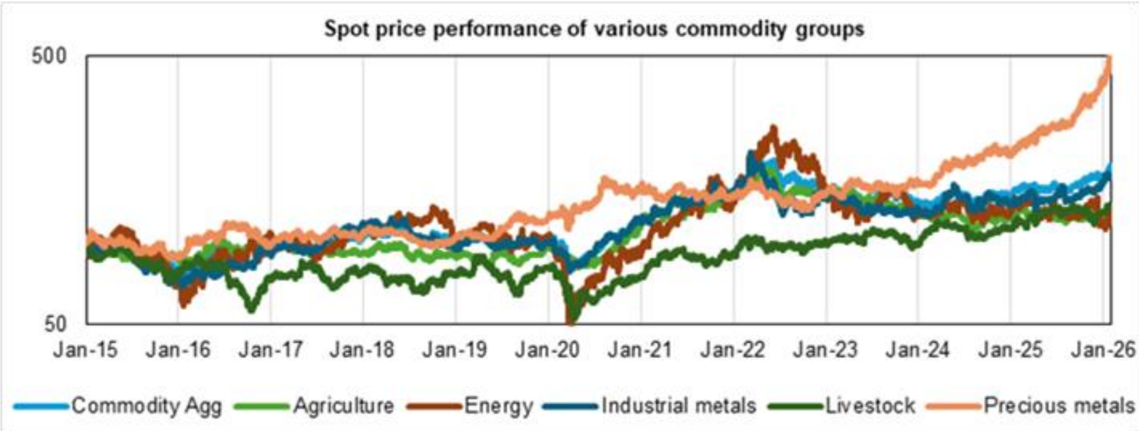
Gold (positive view): Supported by tight physical markets and liquidity-stress.

Gold continues to demonstrate exceptional resilience, breaking above USD5,500/oz amid a pronounced liquidity squeeze in London. The price action is not simply speculative exuberance; it reflects a structural tightening in the physical market and a broader macro backdrop that remains highly supportive. Gold has benefited from a combination of constrained liquidity, elevated premia, and persistent investor demand. The London market, in particular, has experienced ongoing stress, with liquidity thinning and physical availability tightening – conditions that historically amplify upside moves during periods of macro uncertainty. The broader precious-metals complex has been influenced by similar dynamics, but gold stands out because it is less exposed to industrial demand softness and more leveraged to financial market stress. While silver and other industrial metals could be pulled into volatility driven by manufacturing weakness, gold has been buoyed by its role as a macro hedge. The rally in gold has occurred despite subdued global PMIs and weak manufacturing activity across the US, Europe, and China – reinforcing the view that gold's drivers are decoupled from cyclical demand and instead anchored in liquidity, risk hedging, and strategic allocation. Speculative inflows into metals have been significant, but gold's move is not solely a positioning story. Unlike copper, where speculative length has reached record levels, gold's rally is supported by genuine physical tightness. Exchange inventories remain low, and the liquidity squeeze in London has pushed prices higher as market participants compete for immediate delivery. This is consistent with historical episodes where gold rallies sharply when physical availability tightens. Furthermore, the broader commodity complex is experiencing supply-side constraints, geopolitical uncertainty, and shifting trade dynamics – all of which reinforce gold's strategic role. Geopolitical tensions involving Iran, Venezuela, and Russia, as well as structural changes in OPEC+ and global energy markets. These developments increase the appeal of gold as a portfolio stabilizer. Other metals – particularly copper and aluminium –are experiencing volatility driven by inventory dislocations, financing flows, and speculative positioning. Gold, by contrast, benefits from these cross-market stresses without being directly exposed to industrial demand weakness.

Overall, the combination of tight physical markets, liquidity stress, geopolitical uncertainty, and broad investor demand supports a constructive outlook for gold. The most recent breakout above USD5,500/oz is consistent with these underlying dynamics, and the structural backdrop suggests that gold remains well-positioned to retain its strength.

Exhibit 1: Precious metals have diverged from other commodities quite substantially in recent years



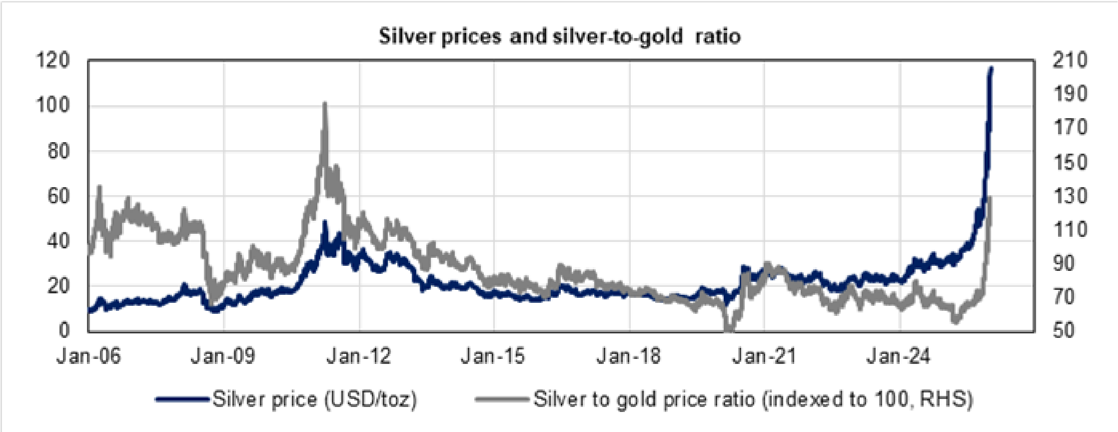
Source: LSEG Workspace, and ADCB Asset Management

Silver (cautious view): Strong price action but vulnerable to industrial weakness

Silver has rallied sharply, trading above USD115/oz, but the underlying market dynamics warrant caution. Unlike gold, silver is heavily exposed to industrial demand, and the macro indicators across major economies remain subdued. Manufacturing PMIs in China, the US, and Europe have been flat or contracting, reflecting weak activity in metals-consuming sectors. This is particularly relevant for silver, given its dual role as both a precious metal and an industrial input. Industrial demand in China has softened across multiple sectors, including grid spending, construction, and consumer products. These categories are significant contributors to silver demand, especially in electronics and photovoltaics. The slowdown in China's grid investment is particularly important, as it has historically been a major driver of silver consumption. The weakness in US manufacturing, as reflected in the ISM survey, further underscores the fragility of industrial demand. At the same time, speculative inflows into metals have been substantial, with more than USD30bn entering base metals markets in 2025. While silver is not explicitly broken out, the broader pattern of speculative activity suggests that part of silver's rally may be driven by positioning rather than fundamentals. This raises the risk of a pullback if macro conditions fail to improve materially or if speculative length unwinds. Physical tightness has been more pronounced in gold than in silver. While silver has benefited from the broader precious-metals rally, its industrial exposure makes it more vulnerable to cyclical softness. The divergence between gold's liquidity-driven rally and silver's industrially-sensitive fundamentals suggests that silver may face headwinds if global demand weakens. Inventory levels across metals have risen in some regions, particularly in the US, where copper and other metals have accumulated due to tariff-related flows. The broader trend of rising inventories and weak demand across industrial metals suggests that silver's industrial component may be at risk.

In summary, while silver has exhibited strong price momentum, the underlying fundamentals – weak industrial demand, speculative inflows, and rising inventories – justify a cautious stance. The metal may continue to benefit from precious-metals sentiment, but its industrial exposure introduces downside risks that gold does not share.

Exhibit 2: Silver-gold ratio has risen to its highest level in 15 years



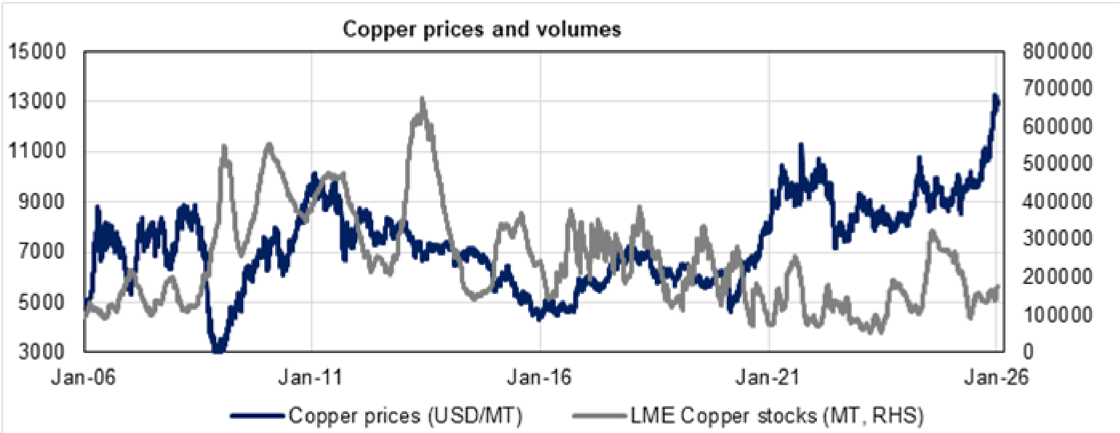
Source: LSEG Workspace, and ADCB Asset Management

Copper (cautious view): Speculative rally on fragile fundamentals

Copper prices have surged above USD13,000/t, but the rally is being driven primarily by speculative inflows rather than fundamental tightness. Goldman Sachs notes that the latest copper rally has been “largely driven by speculative inflows,” with more than USD30bn entering base metals markets in 2025. Both COMEX and LME net speculative length are at or near record levels, indicating that positioning is stretched. At the same time, copper fundamentals have softened. Ex-US inventories have risen, global visible stocks are trending higher, and China’s refined copper demand contracted sharply in Q4 2025 (-12% YoY). This is a critical signal, as China accounts for more than half of global copper consumption. Global copper inventory is rising ahead of the usual post-Lunar New Year restocking cycle, suggesting that the market is not as tight as prices imply. Copper’s physical market indicators are weakening. Import arbitrage windows in both the US and China remain closed, indicating that physical buyers are not incentivized to pull material into their markets. Copper cathode premiums in China have been more resilient than during the 2024 buyer strike, but they remain subdued relative to historical norms. On the supply side, global refined copper supply is expected to rise, with China’s share of global production exceeding 50% for the first time in 2026. Mine supply disruptions have eased, and soaring prices are incentivizing increased scrap flows and production growth in regions such as the DRC. Goldman Sachs has recently increased its 2026 refined copper surplus forecast to 300kt, up from 160kt previously. Copper’s forward curve has been volatile, with periods of deep backwardation driven by liquidity dislocations rather than genuine tightness. CME warehouse financing deals remain highly profitable, encouraging the accumulation of inventories in the US. This dynamic has distorted global flows and contributed to the appearance of tightness in ex-US markets.

Given these factors – speculative positioning, weakening demand, rising inventories, and increasing supply – a cautious view on copper is warranted. While near-term prices may remain elevated due to positioning and liquidity dynamics, the fundamental backdrop suggests vulnerability to correction.

Exhibit 3: Copper has broken out of our expected range in recent days despite no change in underlying drivers

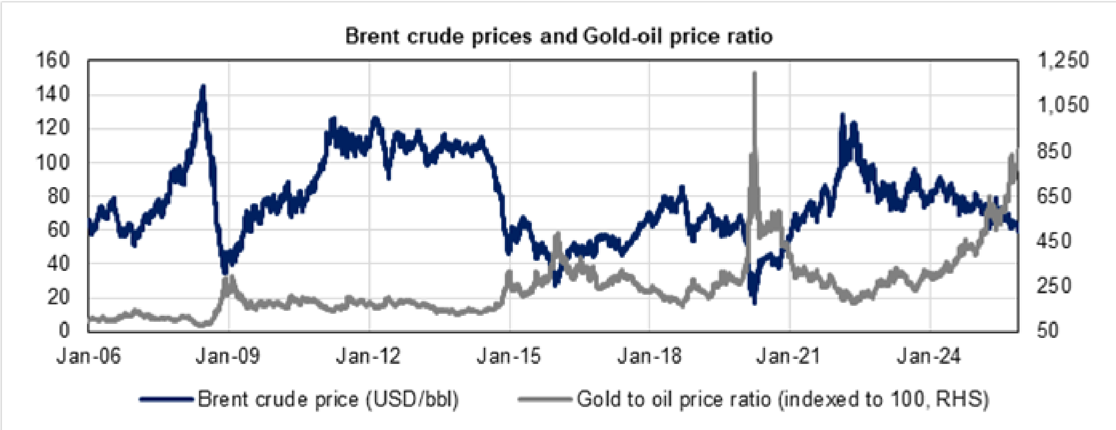


Source: LSEG Workspace, and ADCB Asset Management

Oil (neutral view): Geopolitical noise but fundamentally range-bound (USD55–70/bbl)
Global oil markets are shaped by geopolitical tensions, shifting trade flows, and structural changes within OPEC+. Despite the headlines – US strikes on Iran, Venezuela's political transition, and evolving sanctions – the underlying supply-demand balance points to a range-bound market, consistent with USD55–70/bbl Brent. BofA Global Research forecasts a +2mb/d surplus. Demand growth is expected to be modest (~1mb/d YoY), while non-OPEC supply continues to expand, particularly in the US, Canada, and Brazil. OPEC+ is expected to increase crude supply by 300kb/d in 2026, while US crude and NGL output stabilizes before rising slightly in 2027. Geopolitical developments – such as the US intervention in Venezuela and sanctions and potential military actions on Iran – may influence near-term volatility but are unlikely to shift the structural balance. Venezuela's production could rise gradually, but meaningful recovery requires USD50-100bn in investment and several years of rebuilding. Iran's production has increased in recent years despite sanctions, and floating inventories have risen, suggesting that supply remains available even under tighter enforcement. China's strategic crude inventory build-out adds another layer of support to near-dated prices, but this is offset by the broader surplus. Further, China has accumulated more than 100 days of forward import coverage, reducing the urgency of incremental buying. On the product side, diesel markets remain tight due to sanctions, drone strikes, and slower refining-capacity growth, but gasoline and other products are more balanced. This supports cracks but does not fundamentally alter crude pricing.

Overall, in our view, oil prices will remain anchored within a broad USD55–70/bbl range over the next 12 months, with geopolitical events creating short-term volatility but not altering the medium-term surplus.

Exhibit 4: Gold to oil ratio has risen to its highest level since 2020, but we find this relative mov reasonable



Source: LSEG Workspace, and ADCB Asset Management

Why commodity ETFs do not always move like the commodities they track.
Commodity ETFs often offer clean, efficient exposure to raw materials, but their performance frequently diverges from the spot market. The gap is not a flaw in the product – it is a function of market structure. Most commodity ETFs do not hold the physical asset. Instead, they obtain exposure through futures contracts, which behave differently from spot prices. When the futures curve is in contango – with forward prices trading above the current spot – ETFs are forced to “sell low and buy high” as they roll expiring contracts into longer-dated ones. This creates negative roll yield, a persistent drag that can materially erode returns relative to the underlying commodity. Periods of backwardation can temporarily reverse this effect. When near-term futures trade above longer-dated contracts, ETFs roll into cheaper positions, effectively “buying low and selling high.” This generates positive roll yield, allowing ETFs to outperform spot. However, backwardation is typically episodic, often driven by supply disruptions, inventory shortages, or seasonal dynamics. As a result, the tailwind is neither stable nor predictable. Beyond curve structure, tracking error further widens the divergence. Management fees, collateral returns, liquidity constraints, and replication choices all influence ETF performance. Futures markets also react to storage bottlenecks, supply shocks, and market stress in ways that spot markets do not. The 2020 oil dislocation – when futures briefly traded negative while spot remained positive – highlighted the structural limitations of futures-based exposure. Physical commodity ETFs, such as those backed by gold, track more closely but still incur storage, insurance, and operational costs that create a small but persistent lag.

In summary, commodity ETFs are effective tools for gaining exposure, but they are not perfect substitutes for spot commodities. A sound strategy requires understanding roll dynamics, curve shape, and the sources of tracking error to set realistic expectations and avoid unintended performance surprises.

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