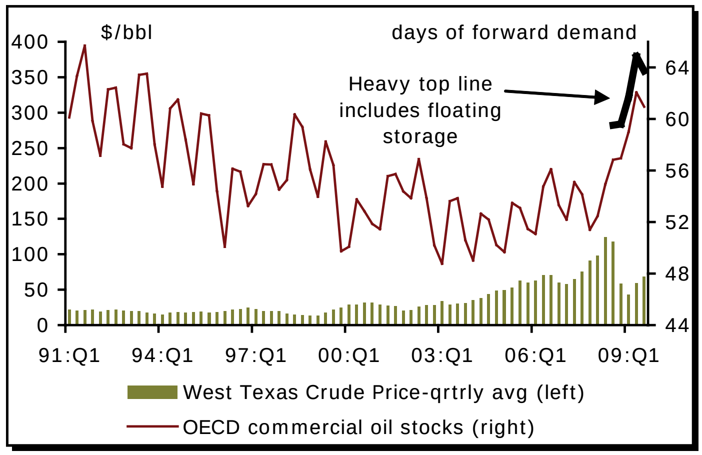
COMMODITIES OUTLOOK

After a spirited snapback, oil's rally appears to have run out of gas, easing by 10% recently from late October's one-year highs.The breakeven price for finding, developing and producing a barrel of crude doubled between 2004 and late 2008, according to producing-company data. While we believe that prices will climb appreciably further in the next decade, in step with marginal costs, the oil market appears to have gotten ahead of itself for now. Belying recent signs of momentum, OECD inventories and OPEC spare capacity are at or near decade highs. Demand in the US, still the world's largest consumer, also remains soft. We expect those realities, coupled with the demand effects of a not overly strong global recovery and above-trend efficiency growth, to hold WTI to an average $70/bbl next year, rising modestly to $80/bbl in 2011.

CO_2 abatement efforts could create longer-term opportunities for natural gas-fired power. The economics of shale gas, the dominant source of new North American supply, also don't work at prices as low as those seen recently. While that creates longer-term upside, record inventory levels and weaker US industrial demand will help to keep gas trading at an unusually larger discount to oil for the time being. We expect Henry Hub prices to average $5.50 next year and $6.50 in 2011.

Still-High Inventories Cast Doubt on Sustainability of Oil's Recent Gains



Gold gleamed for most of the fall. While we are staying with our positive longer-term forecast, several factors point to the risk of deeper correction in the interim. Speculative long positions are still measurably higher than they were before early 2008's appreciable sell-off. With the major industrial economies now operating a good 4% or so below capacity, the risk of material acceleration in inflation remains remote for now, even with faster monetary expansion. Central banks may well buy more gold, but the volumes are still conjectural.

While the global recovery is not shaping up to be a barnburner, the composition should be quite favourable for most key industrial metals. Softness in US non-residential construction will hurt demand from that sector but other heavy users like autos and homebuilding are stabilizing or on the mend. China's imports of key metals like copper have also held up well despite reported cuts in strategic stockpiling. That suggests observers may have underestimated the resilience of underlying demand. The full effect of ambitious infrastructure spending plans there will be felt in the quarters to come. Copper should benefit from grid expansion plans, recent mine interruptions and capacity delays due to the financial crisis, making the metal a preferred area for exposure.

Spot Commodity Prices

			Average				
		7-Dec	2007	2008	2009 (f)	2010 (f)	2011 (f)
Oil (WTI)	$/bbl	74	72	100	61	70	80
RBOB gasoline	$/gal	1.91	2.09	2.49	1.70	1.80	2.00
Heating Oil (NYH)	$/gal	1.96	2.03	2.86	1.62	1.95	2.10
Natural Gas (Henry)	$/Mn Btu	4.78	6.97	8.89	3.82	5.50	6.50
Gold	$/troy oz	1143	695	872	1150*	1050*	1100*
Copper	$/lb	3.16	3.24	3.16	2.29	3.25	3.50
Aluminum	$/lb	0.96	1.20	1.17	0.74	0.85	0.80
Nickel	$/lb	7.22	16.86	9.57	6.60	7.00	6.50
Zinc	$/lb	1.03	1.48	0.85	0.73	1.15	1.00

** end of period*