Investment Strategy Update

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Dr. Copper has good news for you, and bad news for the dollar

- **The industrial metal is trading close to its highest in two years as investors seem to be hoping for more infrastructure spending and a strong recovery next year.**
- **The metal is up 10.1% so far this year, while nickel has gained 7.8% and iron ore has rallied 38.4% in US dollar terms in the same period.**
- **The move may also reflect general expectations for the US dollar to continue to weaken.**
- **China, the biggest consumer of these metals, is contributing to the rally as it stockpiles commodities.**
- **The FAB AAC remains underweight equities while favouring gold and investment-grade debt.**

Investors call it ‘doctor’ because copper has often been a good way of predicting future economic growth. If that ability is confirmed, then there is good news ahead.

The price of a ton of copper in the London Metals Exchange has rallied 46.4% since its recent low on 23 March and is now up 10.1% for the year-to-date, outperforming the S&P 500 in that timeframe. What is even more heartening in terms of future growth expectations is the fact that copper is not alone in its gains.

Iron ore, perhaps an even more cyclical metal, is up 38.4% year-to-date in US dollar terms, while nickel has gained 7.9% in the period. Such a strong rally of these metals would normally be a precursor to a lot more demand ahead, suggesting significant spending in construction and infrastructure for years to come.

Some of those expectations can be justified by predictions of future fiscal stimulus being targeted at new infrastructure. After nearly a decade of negative investment in roads and bridges, G-10 economies could really use this.

The other part of the explanation is probably coming from forecasts of more housing construction as record low interest rates across the globe prompt more real estate investment. Some of that has already started to be seen, with US housing starts in July jumping to 1.5 million, 60.2% higher than April, and one of the highest monthly prints since 2007.

China, the biggest consumer of industrial metals, is also helping to fuel the rally. Home price appreciation in the country accelerated in August, increasing the interest in residential construction. Perhaps more important, Bloomberg recently reported that the country is increasing its state reserve stockpiles of commodities too.

Copper is up 46.4% since 23 March as investors look at strong growth next year

Amid all this potential additional demand, there is little by way of new supply, as five years of a commodities bear market have translated into less investment in production. This adds pressure to price expectations for metals.

Aside from all this, however, industrial metals may also be signaling something else: that investors expect the US dollar to continue to weaken. Most commodities are still traded in dollar terms, and some investors (particularly in China) use them as a way to hedge against local currency fluctuations. They also tend to move in the opposite direction of the dollar. Indeed, the Federal Reserve is widely expected this week to indicate it will continue to add liquidity to the system, which weakens the dollar. And Dr. Copper would know that.

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