


## Commodities - End of Bull?



Commodities, as measured by the Standard & Poor's GSCI index of 24 raw materials, had their fastest 30-day decline to mid-August, slumping 21%, after peaking July 3, according to Bloomberg. This phenomenon reinforced the view that the global economy has been weakening, not just the US economy. However, commodities are still in their seventh year of gains, fueled by demand led by China and India and disruptions to mine and farm supplies. On the other hand, the California Public Employees' Retirement System (Calpers), the largest US pension fund, which oversees \$239 billion, said early this year it may raise commodity investments 16-fold to \$7.2 billion through 2010. In fact, supply constraints have pushed some commodities from the recent bottom levels. Corn and soybeans have rebounded as reduced crop yields push US stockpiles to near five-year lows. Corn and soybeans, down

as much as 37% from their peaks, gained the past two weeks as delayed plantings threaten to reduce US yields and on concern export tax protests may disrupt supplies from Argentina, the second-largest exporter of corn and third-largest of soybeans. That would strain world cereal stockpiles that the United Nations' Food and Agriculture Organization says are near a 30-year low. With regard to metals, copper, after plunging as much as 20% from its \$8,940 a ton record on July 2, has rebounded from a six-month low as output fell at BHP Billiton, the world's biggest mining company. Xstrata, the fourth-largest nickel refiner also said the suspension of its Falcondo operations in the Dominican Republic may last four months. The operations produce 29,000 tons of nickel a year, or about 2% of world primary nickel production. In addition, supply constraints

come at a time of sustained demand in China and India, home to a third of the world's population. Over the past two weeks, it was speculated that China might spend as much as 400 billion yuan to stimulate the economy and ease monetary policy. As a matter of fact, Chinese factory and property spending accelerated through July, fueled by rebuilding after the Sichuan earthquake. Exports surged and retail sales growth was the most since 1999. Chinese demand may also increase as factories shuttered for the Olympics reopen. The economy expanded 10.1% in the three months through June. Moreover, India, which could emulate China in demand for raw materials, will grow 7.7% in the year to March, a government panel said Aug. 13. 

## Microscope

In the past, farmers grew their crops and then brought them to market in the hope of selling their commodity of inventory. Without any indication of demand, supply often exceeded what was needed, and unpurchased crops were left to rot in the streets. In the mid-19th century, grain markets were established and a central marketplace was created for farmers to bring their commodities and sell them either for immediate delivery or for forward delivery to hedge price risk. The latter contracts, forwards contracts, were the fore-runners to today's futures contracts. In fact, this concept saved many farmers from the loss of crops and helped stabilize supply and prices in the off-season. Today's commodity market is a global marketplace not only for agricultural products, but also currencies and financial instruments such as Treasury bonds and stock futures. It's a diverse marketplace of farmers, exporters, importers, manufacturers and speculators. Modern technology has transformed commodities into a global marketplace where a Japanese farmer can match a bid from a buyer in Europe. Therefore, commodities prices affect everyone in the world.



### MARKET BRIEFING

#### YTD % (local curr)


<b>US DJ</b>	11,628 (-12.3%)
<b>Nasdaq</b>	2,414.71 (-9%)
<b>Euro Stoxx 50</b>	3,312 (-24.7%)
<b>HSI</b>	20,392 (-26.7%)
<b>Japan NK225</b>	12,666 (-17.3%)
<b>China Shanghai Composite</b>	2,405 (-54.3%)
<b>Singapore</b>	2,723 (-21.4%)
<b>India BSE30</b>	14,401 (-29%)
<b>Brazil BOVESPA</b>	55,850 (-12.6%)
<b>Aus All Ord</b>	5,010 (-22%)
<b>US-10yr Bond</b>	Yield 3.87%

As at 22/08/08


## Insight: "Commodities"

A commodity is anything for which there is demand, but which is supplied without qualitative differentiation across a market. One of the characteristics of a commodity good is that its price is determined as a function of its market as a whole. Well-established physical commodities have actively traded spot and derivative markets. Generally, these are basic resources and agricultural products such as iron ore, crude oil, coal, ethanol, sugar, coffee beans, soybeans, aluminum, rice, wheat, gold and silver. There are two types of commodities: hard and soft commodities. A hard as metals,

commodity is a commodity such crude oil, or coal. This term generally refers to commodities that are mined, rather than grown. Gold is a traditional commodity. Demand for gold, traditionally used as

an inflation hedge, is up 20% yoy, driven by a combination of market nervousness, dollar weakness, the rising US trade deficit, geopolitical uncertainty, and middle eastern petrol dollars. As commodity-play, gold mining shares are one of good choices. But they are extremely volatile. As a rule of thumb, for every 1% movement in the gold price, there is a 3-5% swing in share price, because any price movement in the metal drops straight into the profit margin and transforms the value of the reserves. Consequently companies that have done the best are those with the largest reserve divisions. 

## A-Z Financial Tools

**Zero-investment portfolio** is a portfolio of zero net value established by buying and shorting component securities, usually in the context of an arbitrage strategy. The utilization of arbitrage to protect the overall value of the financial portfolio creates a situation where the investor is protected from the shifts in the investment market that can occur without warning. 



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Call 2268 6308  
Email: [insider@ibccapital.com](mailto:insider@ibccapital.com)

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