

A generational opportunity for commodities?

News of vaccines coming in will likely prompt other big pharma companies to announce their successes as we move towards Christmas. Whilst that's going to be a big boost to newspaper headlines for households across the world, I think on Wall Street, each new entrant announcing their success will lose a little market elasticity in terms of reaction size as investors move to a more pragmatic and measured approach to buying into the COVID relief rally.

Whilst a more measured response is not as exciting as markets ripping higher, it's exactly this measured tone of investor reaction which we want. It shows the market is thinking about its next move carefully and with clarity. Markets ripping higher only increases the risk of them ripping lower again in pretty short order. Not only is this tiring for everyone, it can often leave investors back at the start when all is said and done.

With Carnival, the cruise line, up some 40% in a day I find it hard to believe stocks like this will remain ahead of the pack this time next year. So where do we think the measured opportunities lie in 2021, akin to our call on gold bottoming out in 2018?

An interesting opportunity we think has potential for next year is raw commodities, or "raw materials". Most who cut their teeth in 2008 know there is a relationship between the printing of money (and thus its debasement), and the subsequent attractiveness of real world assets such as raw materials.

The poster child of this movement is gold, and boy have we seen the yellow metal rally this year. Simply speaking, if a government or central bank can print money ad infinitum it ceases to hold its value. So conversely, assets where you cannot create infinite supply such as raw materials, become more attractive to investors as both alternate forms of currency and a safe haven.

For those of you who need a quick reminder, from 2008 to 2010 the level of QE injected into the US totalled in the region of $2.2 trillion. The total QE bill for 2020's COVID bailout has been over $5 trillion. All in all, the FED's balance sheet now stands in excess of $7 trillion. So yes, there has been money printing on an industrial scale, and yes, the equity markets historic rally this year is largely down to this single massive intervention. But one just has to look at the rally in gold to see just as voracious demand for real world assets. Confusing? You bet.

Historically, there is also a negative correlation between commodities and the dollar as there is with gold. This is primarily because the dollar remains the base currency of the world, and a currency in which many commodities are priced. Naturally, when the dollar falls in value, international buyers can use the opportunity to buy more commodities with the same amount of capital, thus increasing the demand which pushes the price higher.

We believe the investment case for commodities in 2021 has the potential to be as attractive as our call on gold which we invested into in 2018 when the price was at a generational low, and then rode the trade all the way up to the highs where we now see clients making some 30-40% in gains. The key to this specific asset class rallying will be linked to a sustained recovery in global growth and consumption.

With global demand on the up, a COVID vaccine in circulation, shipping containers full once again and the potential for a cooling in tensions between China and the US, the stage is set for a pickup in global demand. This feeds into demand for raw materials which gets boosted by a weaker dollar as inflation and interest rate expectations start to replace the "lower for longer" narrative from the FED.

With gold already shooting for the moon, we know the appetite for real world assets holds true, yet commodities remain at a 50 year low to equities and gold. Much in the same way as gold did to equities in 2018 when we decided to start buying in. All in all, to us, this would suggest an investment into the raw commodity theme looks primed as a nice way to capture the positivity which we could see taking hold of markets in 2021.

But, make no mistake, we are fully aware of the myriad of macro risks which lie just under the surface of 2021's positivity. TAM's portfolios have just as many defensive investments as they do commodity style "risk on" investments, ensuring clients are not only poised for the upside but prepared for the downside. At the end of the day, diversification remains king.

If you would like to discuss our portfolios or current positioning further please do not hesitate to contact us.

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