

Commodities: The dawn of a new supercycle?

DIGITAL ENGAGEMENT TEAM

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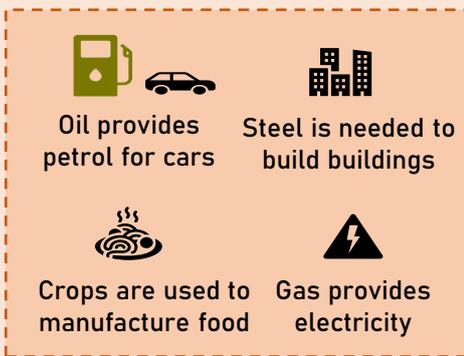
TRADING MATTERS SERIES: NEWS FOCUS

The summary and impact of a major news event

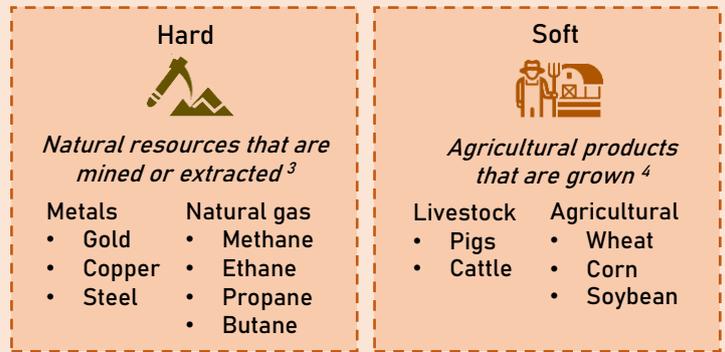
Summary of commodities

Commodities are raw materials used in the production of other goods and services, ranging widely from food to furniture to gasoline or petrol.^{1,11}

Commodities are the building blocks² of the economy. Prices of commodities can affect the operational cost of businesses, who may then decide whether to pass on these costs to consumers!



Commodities can be classified into hard and soft commodities³



Commodities & Inflation

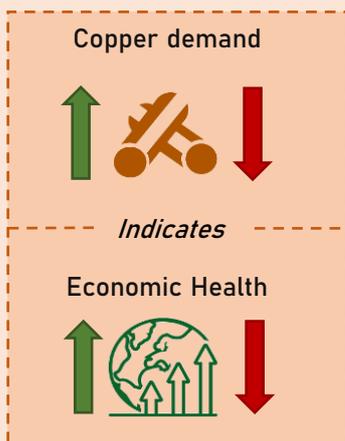
When commodities rise in price, the costs of basic goods and services generally increase.⁵ Here's an example⁶:



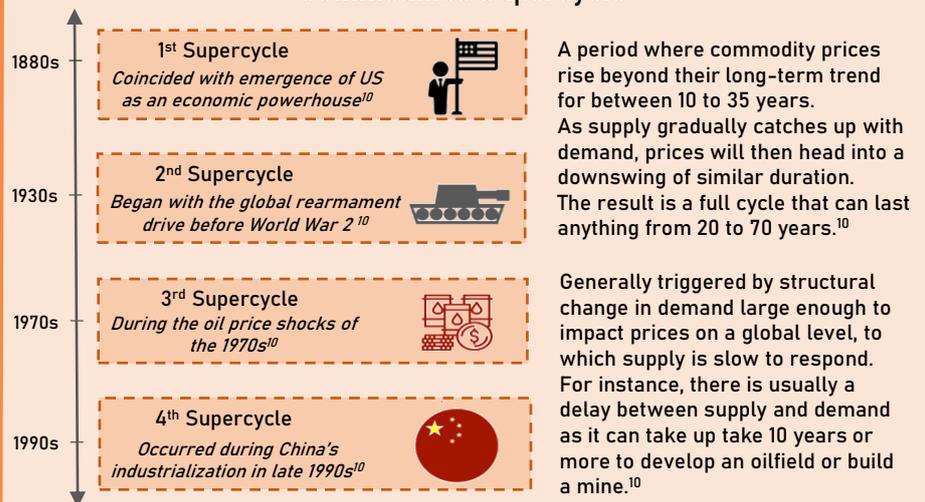
Commodities are a good hedge⁷ against cost-push inflation, where price increase largely results from higher costs of production.⁸

Commodities & Economic health

Some commodities like Copper are relied upon as a barometer of global economic health due to widespread applications in industrial production and electrical equipment.⁹



Commodities Supercycle



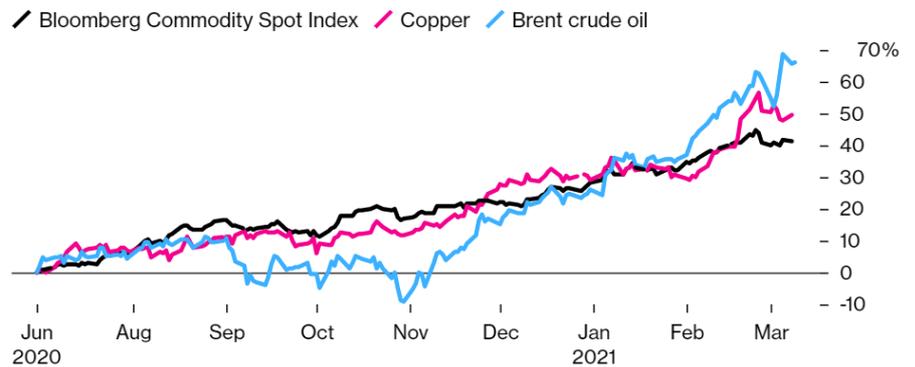
Why is the attention on commodities all of a sudden?

Commodity prices have come a long way since the days of virus-induced lockdowns in April 2020, when oil prices plunged and briefly even went negative.¹² In recent weeks, commodities have seen a broad and powerful rally, with the Bloomberg Commodity Spot Index rising in May 2021 to the highest since 2012.^{13,15}

Hedge funds have piled into what's become the biggest bullish wager on the asset class in at least a decade, with analysts from JPMorgan and Goldman Sachs amongst others anticipating a potential "supercycle" as the global economy rebounds and the world pulls out of the pandemic.^{14,15} However, against this backdrop of a global recovery and commodities boom, fears that this could cause higher inflation have also started to creep in.¹⁴

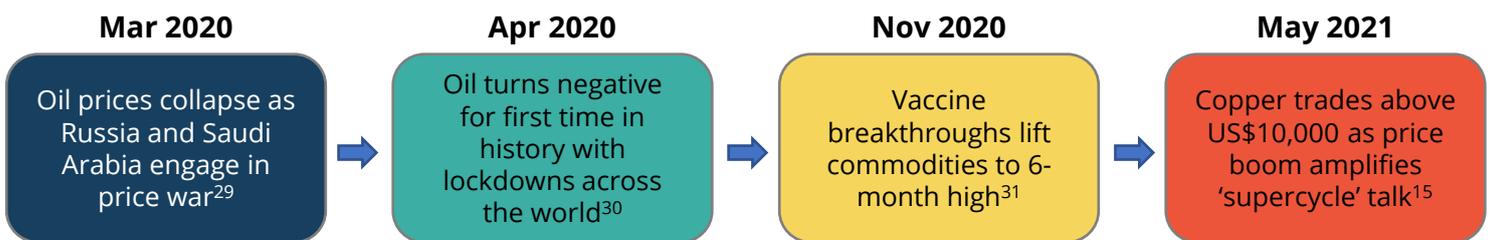
Up and Up

Commodity and energy prices have soared since late 2020



Source: Bloomberg. Chart shows percentage changes

Timeline of Commodities since 2020



How do commodity prices affect the macro environment and stock market?

Commodity prices affect both the broader macro environment, as well as specific stocks and sectors.

From a macro perspective:



Commodities have a huge impact on the cost of living, as they affect the price of fuels, power, food and construction projects.¹⁴ A spike in commodity prices could fuel fears of inflation, pose risks to corporate profit margins and complicate the broader macro-outlook as it may lead policy makers to reconsider and taper any stimulus that could affect markets.¹³



Commodities shape terms of trade, exchange rates and ultimately the politics of commodity-dependent nations like Canada, Brazil, Chile and Venezuela.¹⁴ The Arab Spring uprisings in Egypt a decade ago and recent social unrest in Pakistan triggered in part by increasing food and fuel costs also shows how politically sensitive this issue can be.¹⁶ The recent deterioration in China-Australia relations and potential disruption to commodity trade also highlights the often intertwining relationship between commodities trade and international relations.¹⁷



Raw materials and especially industrial metals are often seen as indicators of economic activity, as they indicate prospects for increased demand.¹⁸ In recent months, copper, a bellwether industrial commodity, has surged to trade above US\$10,000 for the first time since 2011.^{15,21} Other metals from iron ore to nickel have also rallied, boosted by rapidly tightening physical markets and prospects for rebounding economic growth from the pandemic.^{14,18}

From a sector & stock-specific perspective:



Metals
& Mining

Bloomberg Intelligence highlights commodity-heavy equities and currencies of countries like Brazil, Mexico, South Africa, Malaysia and Indonesia as particular beneficiaries of a commodities boom.¹³

The recent commodity surge has seen shares of metals producers soar on optimism on the mining sector's earnings outlook, balance sheets and margins.^{18,19} Some of the world's biggest miners such as Freeport-McMoRan, Anglo-American, BHP and Rio Tinto have hit decade or record highs, propelled by metal prices and profits.^{19,20} Both BHP and Rio Tinto have also paid out record dividends, as has Glencore.²⁰

Why do some people say we're at the start of a new commodities "supercycle"?

Here are some reasons why some traders and analysts expect that a new "supercycle" – a prolonged period of high prices generally seen at times of global change – has kicked off.^{15,20}



Economic Recovery

Rapid economic recoveries in the world's largest economies such as China, Europe and the US have stoked demand for metals, food and energy, as well as more cars, electronics and infrastructure.^{15,21}



Government Spending

Contributing to the economic recovery are government stimulus measures that are fueling prospects for resurging demand.¹⁹ Potential infrastructure plans from US President Joe Biden have also lifted the sector, as materials such as iron and copper could play a part in infrastructure plans that lean green.²²



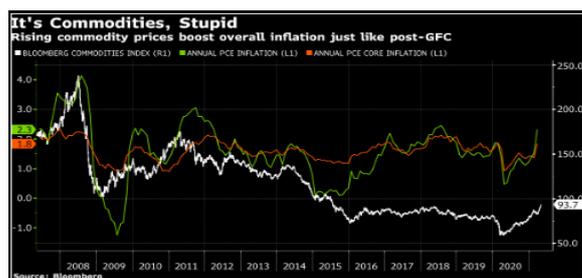
Use in Green Technologies

Raw materials needed for green technologies have also been swept up in the current rally.^{15,22} Global efforts to decarbonise will require vast amounts of copper and other materials like lithium and rare earths to create millions of electric car batteries, wind turbines, electric cabling and other green technologies.^{15,20}

Not all analysts remain as bullish on a "supercycle" outlook however, citing the current price rally as part of a business cycle upswing rather than a supercycle.¹⁵

How have central banks and governments reacted to the rising commodities prices?

Generally, a rise in commodities prices can lead to a movement in currencies, interest rates increases and a corresponding decline in bond prices.²³ Recently however, central banks seem to have been successful in attempts to keep the economy running hot while ignoring the inflationary pressures of surging commodities,²⁵ as the recent spike in commodities prices did not seem to elicit some of the classic responses in currencies and bonds.²⁴ Indeed, we have seen that surging commodities prices are boosting inflation now,²⁶ with the April 2021 consumer price index posting its biggest month-over-month gain since 2009.²⁷



Source: Bloomberg

However, the narrative seems to be changing as hints of monetary policy tightening are beginning to show.²³ According to Bloomberg, some Federal Reserve officials are now open to the idea of tapering bond purchases if the rapid progress of the economy continues.²⁷ Elsewhere, the central banks of Canada and Norway have indicated that they are considering withdrawing monetary accommodation.²⁴

The government of China has also recently decided to implement measures to rein in commodities prices, including raising export tariffs, canceling export rebates, stockpiling of certain commodities as well as strengthening market regulation to target malicious trading.²⁸

Companies in the Mining Industry

Below are the top companies based on Market Cap in their respective segments and geographical locations

Anglo American PLC
(AAL LN)

Market Cap:
USD \$55.97bn

BHP Group Ltd
(BHP US)

Market Cap:
USD \$173.33bn

Glencore PLC
(GLEN LN)

Market Cap:
USD \$58.91bn

**Freeport
McMoran Inc**
(FCX US)

Market Cap:
USD \$59.68bn

Vale S.A.
ADR
(VALE US)
Market Cap:
USD \$112.13bn

Source: Bloomberg, as of 28 May 2021 (11am SGT)

BHP Group Ltd (BHP US)



- Largest mining firm in the world by market cap (Bloomberg)
- Deals primarily in iron ore, metallurgical coal and copper (Bloomberg)
- Its South Flank iron ore project, one of the world's biggest new mine, has recently started production (Bloomberg, Reuters)

Vale S.A. ADR (VALE US)



- World's top producer of iron ore in 2020 (NS Energy) and largest producer of nickel (Vale)
- Most valuable company in Latin America reported as of 28 Apr 2021 (The Rio Times)
- Reported first quarter 2021 earnings on 26 Apr 2021, beating estimates (Reuters)

Anglo American PLC (AAL LN)



- World's largest platinum producing company (Statista) with production in iron ore, metallurgical coal, copper, nickel and diamonds as well (Bloomberg)
- Their thermal coal business spin-off, Thungela Resources Limited is expected to list on London Stock Exchange on 7 June 2021 (Reuters)

Freeport McMoran Inc (FCX US)



- World's largest public copper miner based upon 2021 estimated production (Seeking Alpha)
- Operates the Grasberg mine, which is the third-largest gold mine in the world (Reuters)

Glencore PLC (GLEN LN)



- Largest mining company in the world by revenue (NS Energy)
- Involved in various metals like copper, cobalt, nickel and iron ore as well as energy products like coal and oil (Yahoo! Finance)
- Recently partnered with battery material supplier Umicore to trace cobalt using blockchain technology (Reuters)

Companies in the Mining Industry

Below are the top companies based on Market Cap in their respective segments and geographical locations



Source: Bloomberg, as of 28 May 2021 (11am SGT)

Rio Tinto Ltd (RIO AU)



- World's second largest mining company by market cap (Statista)
- World's third largest mining company by revenue (NS Energy)
- Involved in various minerals and metals such as iron ore, aluminum as well as copper (Bloomberg)

China Shenhua Energy Co Ltd (1088 HK)



- The largest state-owned mining company in China and the world's largest coal mining enterprise (Mining Global)
- Produces various coal products as well as operating electricity generation, railway transportation and other businesses (Bloomberg)

Fortescue Metals Group Ltd (FMG AU)



- Fourth largest iron ore producing company in the world in 2020 (NS Energy)
- Also engages in exploration ventures in various countries such as Ecuador, Argentina, Colombia and Kazakhstan for minerals including copper, gold and lithium (NS Energy)

Zijin Mining Group Co Ltd (2899 HK)



- Largest gold miner in China (Caixin Global)
- Also involved in copper, lead, zinc, silver and iron products (Investopedia)
- Acquired Qulong Copper, the largest copper mine in China, back in 2020 (SMM News)

Jiangxi Copper Co Ltd (358 HK)



- Fifth largest mining company by revenue in 2020 (NS Energy)
- Largest copper producer in China (Metal Bulletin)
- Reported highest quarterly net profit since 2014 on 27 Apr 2021 (Nasdaq)

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