<u>THE METALS MARKETPLACE GAME: TOUCHING BASE</u>
(c) Leo Haviland March 16, 2015

In the film "Full Metal Jacket" (Stanley Kubrick, director), a US colonel emphasizes: "It's a hardball world, son."

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CONCLUSION

Base metals such as aluminum, copper, lead, nickel, and tin capture far fewer headlines than the alluring stars of the petroleum complex. Nevertheless, base metals play an important position in the global economic game. Base metals are very significant not only to the economies of emerging/developing countries (think of China), but also to numerous so-called advanced nations. Despite assorted twists and turns, base metals "in general" (use the London Metal Exchange's base metal index, "LMEX", as a benchmark) have been in a bear path since early 2011. The renewed price meltdown in base metals over the past several months underscores recent and probable future slowdowns in real GDP growth rates in developing nations such as China. However, as emerging and developed nations closely interconnect in today's international economy, base metal weakness probably also points to reductions in future output rates for advanced nations.

In the 2007-09 global economic crisis era and its aftermath up to the present, many significant trend changes in base metals, gold, the broad Goldman Sachs Commodity Index (and the petroleum complex), and the emerging marketplace stocks arena "in general" have occurred around roughly the same time.

The broad real trade-weighted United States dollar's trend does not lock base metals prices, or those of any other playground, into a particular pattern. Nevertheless, the gradual strengthening of the dollar since mid-2011 roughly intertwines with the large bear move in base metals, gold's bloody stumble since its September 2011 peak, and monumental declines in the broad GSCI (and the petroleum complex).

Emerging marketplace stocks in general, like benchmarks for base metals and commodities in general, have slumped in recent months. Further declines in the LMEX and the broad GSCI, especially when accompanied by US dollar rallies, will be a bearish warning sign (confirmation) for emerging marketplace stocks. Further noteworthy erosion in emerging marketplace stock prices likewise will be ominous for stock marketplaces of advanced nations.

DIGGING IN

Metallica sings in "The Unforgiven": "Won't see what might have been".

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Of course supply/demand situations for assorted commodities vary. Analysts also differ in their perspectives regarding a given commodity, relationships between commodities, and the links between commodities and other marketplaces such as currencies, interest rates, and stocks.

Not all commodities or commodity sectors travel exactly alike. Copper does not precisely mirror crude oil. Often price patterns (or important turning points within them) dramatically differ. Price trends of various individual commodity marketplaces (or commodity marketplace fields such as the petroleum complex or base metals) apparently may converge or diverge relative to each other. Also, one commodity arena may seem to lead or lag another. In addition, convergence/divergence and lead/lag perspectives and issues exist between commodities "in general" (or any given commodity) and other realms such as stocks, interest rates, and currencies.

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China is a huge consumer of base metals. The Financial Times (3/11/15, p20) says China's steel industry accounts for about 70 percent of seaborne iron ore demand. Iron ore recently crumbled under $60/tonne for the first time since 2009. China's copper imports last month fell to their lowest level since 2011 (Financial Times, 3/11/15, p20). China even has deflation fears; noting the nation's producer price index's year-on-year tumbles (4.8pc in February 2015), the FT declares: "worries remain that the world's factory floor is heading for outright deflation" (3/11/15, p4).

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The London Metal Exchange Index (LMEX) presents a helpful overview of base metals in general. Six primary non-ferrous metals constitute the LMEX. The index includes aluminum (42.8 percent), copper (31.2pc), lead (8.2pc), nickel (2.0pc), tin (one pc), and zinc (14.8pc).

To unearth trends for commodities "in general", many marketplace players avidly study the broad S&P Goldman Sachs Commodity Index ("GSCI"). The GSCI alloy contains LMEX elements; it has aluminum, LME copper, lead, nickel, and zinc (no tin). However, their percentage dollar weights add up to 6.7 percent of the 2015 GSCI. Compare the petroleum complex's bulky 68.1 percent GSCI share (Brent/North Sea crude oil grabs 24.7pc, NYMEX crude 24.5pc). Because base metals represent a paltry percentage of the broad GSCI, and although base metals and the GSCI often to some extent manifest similar trends, the GSCI is not always a close proxy to the base metals complex.

Incidentally, gold is 2.4pc of the GSCI, silver about .3pc. So base metals plus precious metals combined equal only 9.5pc of the broad GSCI.

In the following table, data for the broad real trade-weighted US dollar ("TWD") is from the Federal Reserve Board (H.10; monthly average; March 1973=100). Morgan Stanley's "MSCI Emerging Stock Markets Index" ("MXEF") represents emerging stock marketplaces.

TIMING MAY NOT BE EVERYTHING (BUT IT IS SOMETHING)

Iron Maiden, "Age of Innocence":
"I feel I've lost my patience with the world and all
And all the politicians and their hollow promises
And all the lies, deceit and shame that goes with it
The working man pays everything for their mistakes".

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	2011 High	Recent Low	2007-08 High	Crisis Era Low
LME (Base Metals) Index (LMEX)	2/4/11; 4478 (4/8/11; 4469, 7/26/11; 4339)	1/29/15; 2667	5/4/07; 4557 (3/5/08; 4400, 7/2/08; 4038)	12/24/08; 1614

[The LMEX has degraded 40.4 percent from its February 2011 summit to its late January 2015 low.

Note that the LMEX's lofty May 2007 pinnacle preceded major highs in the broad GSCI, MXEF, and S+P 500 (10/11/07; 1576) and the broad real trade-weighted dollar's bottom. However, the LMEX's March and July 2008 secondary tops occurred close in time to the major low in the TWD, the final high in the S+P 500 (5/19/08; 1440), and the broad GSCI's peak. The LMEX's December 2008 major low occurred near in time to the crucial turns in these marketplaces.

Other important LMEX interim tops after its 2011 peak include: 2/9/12 at 3820, 9/14/12 at 3609, and 2/4/13 at 3614.

Recent collapse points are 7/24/14's 3316 (which was before the OPEC oil meeting) and 11/21/14's 3150. The fall since July and November 2014 (and the absence of a significant rally since then) indicate slowing worldwide real GDP growth (and arguably especially in China).

The LMEX's 3/13/15 close at 2720 hovers not far from January 2015 depth.]

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[Iron ore (delivered to China), an important segment of the base metal complex, peaked 2/17/11 at 191.7 (alongside the LMEX major high; an interim high on 5/5/11 at 183.0 followed). It since has plummeted to 57.6 (3/11/15), a crushing seventy percent fall from February 2011.]

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[Silver's spike from its 10/28/08 bottom at $8.46 transported it up to 4/25/11's top around $49.80 Other important tops include 8/22/11's $44.06, 2/29/12's $37.48, and 10/1/12's $35.36; compare those in the LMEX. Silver recently tripped lower from 1/21/15 $18.49 height.]

	2011 High	Recent Low	2007-08 High	Crisis Era Low
Gold	9/6/11; 1921	11/7/14; 1130	3/17/08; 1034	10/24/08; 688

[Other important tops from a few years ago include 11/8/11's 1804, 2/28/12's 1793 (close in time to the LMEX one), and 10/3/12's 1795.

Undermined in part by the long bull ascent for the broad real trade-weighted dollar, gold since its September 2011 plateau has turned out to be more fragile than many expected. Gold's tarnished fall from its 2011 top to its November 2014 low is 41.2 percent, about the same as the 2011-present 40.4pc LMEX bear move. The current gold price near 1160 neighbors its November 2014 low.

Gold's recent collapse points are 7/10/14's 1347 high (close in time to the LMEX's) and 1/22/15's 1308.

Gold's 2008 major low occurred a few weeks prior to the LMEX's trough, and alongside the major lows in China's Shanghai Composite stock market index (10/28/08 at 1665) and the MXEF.

A comprehensive analysis of gold pricing and trends also would consider it in non-dollar terms.]

	2011 High	Recent Low	2007-08 High	Crisis Era Low
Broad GSCI	4/11+5/2; 762	1/29/15; 372	7/3/08; 894	2/19/09; 306

[The GSCI suffered a 51.1pc hammering from its 2011 peak to its January 2015 low. It nowadays uneasily rests above its 2/19/09 major bottom at 306. The 3/13/15 GSCI level around 393 stands rather close to its January 2015 floor.]

Other significant plateaus in the slump following 2011's major high: 3/1/12 at 717, 9/14/12 at 699, 2/13/13 at 682; compare the timing for those in the LMEX. See also 8/28/13's 675 height.

The broad GSCI's initial key drop-off point several months ago was 6/23/14's 673 (compare the high in OPEC's crude oil basket, 6/20/14 at $110.48). The broad GSCI then wandered lower, collapsing after 10/29/14's minor high at 549 (blasting under the key lows of 10/4/11 at 573 and 6/22/12 at 556) and the late November 2014 OPEC meeting. In their 11/27/14 meeting, OPEC oil ministers decided to maintain their production quotas.]

	2011 High	**Recent Low**	**2007-08 High**	**Crisis Era Low**
MXEF	4/27/11; 1212	12/17/14; 906	11/1/07; 1345 (5/19/08; 1253)	10/28/08; 446

[Note also interim MXEF highs such as 2/29/12's 1085 and 1/3/13's 1065, not far in time from those in the LMEX.

Like the LMEX and the broad GSCI, the MXEF has not exceeded its 2011 peak. December 2014's MXEF low crashes 25.2 percent beneath late April 2011's high.

Emerging marketplace stock fans lament the MXEF's slide from an interim top at 1104 on 9/14/14, attained only several weeks after the LMEX's July 2014 base metals one. It retreated further from 11/27/14's lower interim high at 1018 (recall the OPEC petroleum meeting) The MXEF has not surpassed its September and November 2014 elevations, despite festive rallies to new highs by the S+P 500 (and European equity benchmarks such as the Stoxx Europe 600 stock index).

The MXEF's 3/13/15 close at 940 is only a modest advance above its 12/17/14 low.]

	2011 Low	**Recent High**	**2007-08 Low**	**Crisis Era High**
TWD	July 2011; 80.5	Feb 2015; 93.2	Apr 2008; 84.2	March 2009; 96.9

[The TWD's 15.8 percent bull move from its record low of July 2011 to February 2015 surpasses its 15.1pc ascent from April 2008 to March 2009 during the global economic crisis.

As the broad real trade-weighted US dollar marched sideways in a narrow range following its July 2011 major trough, it established a minor high in June 2012 at 86.2. September 2014's TWD 86.6 broke over June 2012's resistance. Keep in mind this September TWD breakthrough occurred in between LMEX interim tops of 7/24/14 at 3316 and 11/21/14 at 3150.

Here's a warning bell for watchers of various financial and commodity marketplaces. During the broad real TWD's bull move during 2007-09's worldwide economic disaster, it made a notable jump from September 2008's 88.8 to October 2008's 93.9. Around that time, the dreadful crisis accelerated. The February 2015 TWD level stands close to October 2008's elevation. The broad real TWD average for March 2015 to date, based on available nominal TWD statistics, probably has moved even nearer to October 2008's height.

The Euro FX cross against the US dollar established a new low in its bear trend at around 1.046 on 3/13/15.]

EXTRA INNINGS

The recent strength in the broad real TWD alongside softness in base metal prices (as well as feebleness in gold and the broad GSCI) signals slowing real GDP growth rates. The TWD probably will remain strong. Recent lows in base metals, gold, and the broad GSCI probably will be broken.

Obviously it is much easier for "investors" and other marketplace competitors to own large (valuable) quantities of financial instruments such as securities than a similar dollar value stockpile of physical base metals. It is easier to buy and hold (or hoard) equities or US 10 year Treasury notes than copper. Sustained interest rate yield repression and floods of money printing by the Federal Reserve Board and its allies have helped to create a marvelous golden age for stock benchmarks such as the S+P 500 and the Stoxx Europe 600. Many ask: "Where should we put our money when interest rate yields are so low?" Weakness in the LMEX (and broad GSCI) and glittering strength in the TWD warns that the golden age for stocks probably will not last much longer.

Unlike the LMEX, gold, and the broad GSCI, the S+P 500 has soared over fifty percent beyond its 2011 summit (5/2/11 at 1371). Like the LMEX, gold, and the broad GSCI, emerging stock marketplaces in general (MXEF) remain under their spring 2011 peaks. Yet despite this sharp difference in trends relative to 2011 between the S+P 500 and commodities in general and the MXEF, the S+P 500 and these marketplaces often have since made many price turns in the same overall direction at roughly the same time (as they did for several years prior to 2011). In addition, the MXEF, like the LMEX and other commodity benchmarks, has slumped in recent months (9/14/14 high). Further declines in the LMEX and the broad GSCI, especially if accompanied by continued US dollar strength, will be a bearish warning sign for emerging marketplace stocks. Renewed significant feebleness in emerging marketplace stocks likewise would be ominous for those of advanced nations.

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