



The Next Six Months

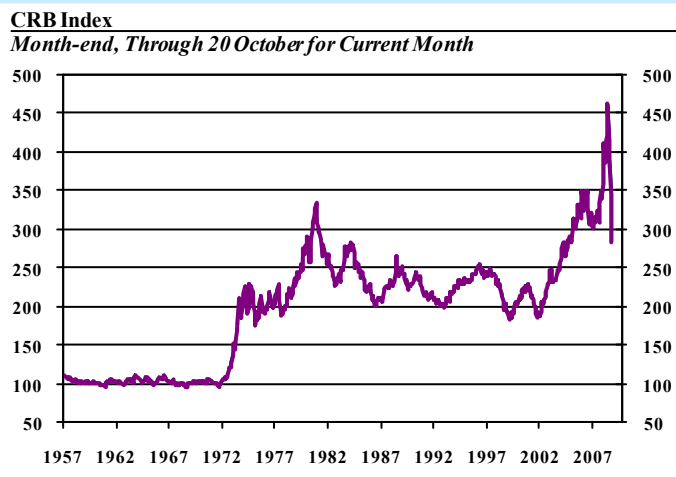
The next six months may well be critical for commodities markets, in establishing their price directions and in broadcasting the most likely course of supply, demand, and prices for the next two to five years.

At present the markets are overwhelmed by uncertainty about demand levels, the potential for financing future supply, and economic and global political conditions. By April of next year, the outlook should be expected to be clearer for a number of trends on which the longer term outlook for commodities prices and market trends rest. These factors include market fundamentals, including supply, industrial demand levels, and investment patterns.

It is possible that the macro-economic and political environment that presents itself to the commodities markets will be just as confusing and unpredictable in six months as it is now. The world tends not to move in black and white terms, but rather in shades of gray. However, the degree of uncertainty in so many economic, financial, political, and market trends at present is at a statistically extreme level, and it does seem that things should be sorted out somewhat better in six months than they are in late October 2008.

The Fundamentals for all commodities are likely to be more clearly defined by then.

Fabrication or consumption demand has been weakening in recent months. More important, demand is seen as being weak by investors. By April, there may be signs of the U.S. and global economies bottoming out and moving toward recovery. Demand for many commodities, including base metals and energy commodities, actually could hold up better than is expected in late 2008, and is likely to respond more forcefully than expected now. Demand could come to be seen as having been dampened down by the recession, deferred, but not destroyed. This view is based on the fact that final demand for many goods and services will remain strong on a global basis in the long run. The worldwide move toward modernization and greater consumption of everything from housing and automobiles to consumer durables and services is likely to be seen as being strong on a long-term basis, beyond the next few quar-



ters, than the present consensus market view. In economic jargon, the secular upward shift in the fabrication demand curve for most commodities may come to be seen as being more durable than presently is thought.

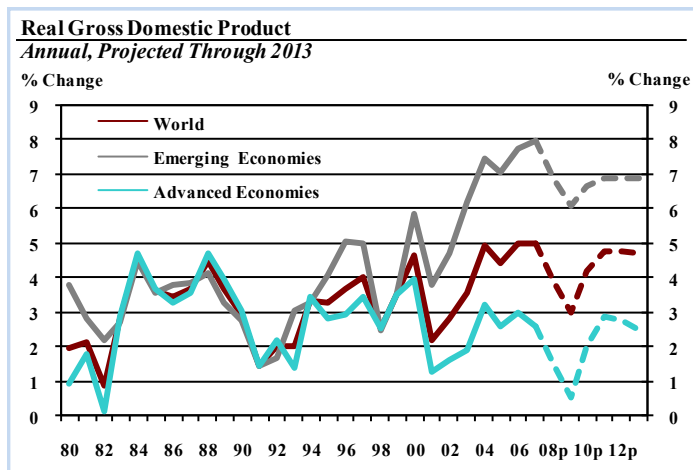
Supply meanwhile will have suffered from the current absence of project financing and low prices. Supply responses to the higher prices and higher real demand for commodities has been slow over the past few years. It will be even slower in the medium term, now that the financing for many new operations and expansions has dried up, at least today. Longer term, financing will be available once again, but it is likely to be more expensive and harder won than it had been over the past few years. This will mean an even slower supply response than has been the case up to now, and tighter balances between supply and demand.

Investment demand also most likely will be seen as not having entirely disappeared six months from now, but will be reorganizing for continued investment interest in commodities as portfolio assets. Most investors that have been interested in commodities remain interested in commodities. They have moved their money to the sidelines right now, as they have across all financial markets. There has been some redemptions and liquidations at commodities oriented funds, but much of the money is still there. At some point investors will begin to re-deploy their assets. A good part of this re-allocation should be expected to be into commodities and commodities investments.

Economics and Political Environment

The financial, economic, and political outlook also should be much more clearly defined by the second quarter of 2009.

At present the consensus among mainstream economists seems to be that the recession will last two to three quarters, into the second quarter of 2009. By the second half of 2009 economic recovery is projected by the International Monetary Fund and others to take hold and be more apparent. April, six months from now, may be a bit too early to expect confidence, if not exuberance, to return to the financial marketplace. By then, however, it may be clear that the U.S. and world economies are experiencing a recession, and are not teetering on the brink of a depression the likes of which the world has not seen since the 1930s. By then, the financial market rescue efforts of governments worldwide should have begun to bear tangible fruit.



The current **political** environment also presents a great deal of uncertainty for investors and businesses. By April political trends should be more clear. The next six months will incorporate both the period between the U.S. election and the inauguration in late January, which will be critical insofar as it will reveal likely political and economic policies to be pursued. It also will include the first 100 days of the next U.S. Administration, which will provide markets a fair reading of what to expect both of the new Administration and its ability to move initiatives through Congress.

The political uncertainties limiting investment decisions for corporations and investors alike are not limited to those of the U.S. election. There are great uncertainties

related to the future of peace or war throughout the Middle East, which weigh heavily on both the energy markets and, by extension, all investment decisions. At present there are mixed signals throughout the region, presenting signs of the potential for widespread war, or lasting peace. By April the world should have a better idea of which way the region is tilting, between these two extremes.

Political conditions in Russia and other former Soviet republics have been unsettled recently. With the passing of the baton to a new U.S. Administration, there will be an opportunity for the governments of Russia and the other former Soviet republics to reposition themselves, or not. This, too, will be clarified to some extent over the first four months of 2009.

Other political conditions, from Europe to Pakistan, including China, North Korea, Venezuela, and other countries, also may have moved toward a more readily identifiable trend forward over the next two quarters, allowing for increased predictability, and thus a more confident investment posture, by April.

Outlook

One of the investment strategies CPM Group historically has employed has been to not try to pick the absolute bottoms and tops of markets, but rather to wait until a major turn in markets has been confirmed over a brief period of time. The gold market bottomed out in February 1985, for example, but we waited for prices to rise around 10% over the next 12 months before issuing a buy recommendation.

This time may be different, and investors and businesses may not want to wait so long for such a confirmation. The turn in prices back toward higher levels, especially for base metals and energy commodities, could be very fast. There is so much money piled up in cash and Treasuries, with its owners waiting to re-allocate these funds when their confidence in the economic outlook for the world has been restored. Because of this build up of un-deployed wealth, when the turn comes it could be a rapid appreciation off of the floor for many commodities prices. If one waits for the first 5% or 10% of the recovery before investing, one may well miss the first 30% of the upward revision in prices – when it comes.

CPM Group has updated its corporate brochure. To learn more about the full range of financial advisory, research, and consulting services we provide, [click here](#).

