



## **The impact of populism, the supercycle and gold as insurance – PAM Insight roundtable**

22/09/2016 by: Tristan Blythe, Group Editor

*On Tuesday 20 September 2016, PAM Insight (publishers of thewealthnet) co-hosted a roundtable discussion with ETF Securities, entitled 'Where are we in the commodity super cycle?'. Participants were Stephen Ford, investment director at City Asset Management; StJohn Gardner, head of investment management and co-chief investment officer at Arbuthnot Latham; Fahad Kamal, senior market strategist at Kleinwort Benson; Ian Williams, chief executive of Charteris Treasury Portfolio Management; Chris Wyllie, chief investment officer at Connor Broadley; as well as James Butterfill, head of research and investment strategy at ETF Securities.*

There are a number of trends driving the world economy and affecting the price of commodities, a roundtable hosted by PAM Insight and ETF Securities heard. Some of these factors have increased the appeal of holding gold in portfolios.

Populist politics is one factor that James Butterfill, head of research and investment strategy at ETF Securities, told participants will shape the economy.

For the purposes of the discussion populism was defined as an overt political strategy to “pander to the masses” rather than necessarily acting in the best interest of a nation. It typically touches on points of inequality, migration and low wages. There tends to be an “outsider” to the traditional political elite which destabilises the incumbent dominant parties.

“We think QE has caused populism through rising inequality,” explained Mr Butterfill. “In turn populism fuels inflation. This is due to increased government infrastructure spend widening national deficits as well as rising minimum wages leading to increased consumer spending. This will be a longer term theme around the world.”

Populist forces do not need to gain power in order to influence the establishment and to have populist policies. Mr Butterfill cited the example of Hillary Clinton responding to Donald Trump by increasing her pledges to spend on infrastructure.

Mr Butterfill said he did not feel that the commodities cycle is easy to determine over long time horizons. Rather, economic fundamentals and infrastructure determine long term rises in prices, furthermore historic big falls in commodity prices are closely correlated to major wars, such as the American Civil war and the two World Wars.

Ian Williams, chief executive of Charteris Treasury Portfolio Management, however takes a different view and believes there is a 20 year cycle between

peaks and troughs. “If it bottomed in 2000 we think that it is a correction and the commodity cycle will peak around 2020,” he said.

StJohn Gardner, head of investment management at Arbuthnot Latham, pointed out that historical time periods on charts cannot be the determinant of the next commodities uplift. Commodity prices are a function of general global growth, the fundamentals (such as production/consumption trends) of each commodity and in some cases sentiment (particularly in the case of precious metals). It should also be noted that different factors affect different types of commodities in particular political risks in countries that have a concentration of commodity production (e.g. platinum in South Africa) or weather predictions in the case of agriculturals.

One fundamental factor that drives commodities prices is how much nations around the world are investing in infrastructure, both from private and public funds. Mr Butterfill said much has been made of China spending less on infrastructure and that India will overtake it as the top infrastructure spending nation. He said this was overplayed and while this may happen in the future it will not be for some considerable time. He cited McKinsey data which suggests India will increase its spend but from a low basis. Africa is also expected to invest considerably more in infrastructure. If these developing nations have the aim of having as developed an infrastructure as Europe, the UK and the US they will need to invest heavily.

Mr Williams added that when considering these underlying fundamentals there tends to be too much emphasis on the demand side. He suggested more attention needs to be paid the supply side.

“A large part of the pricing of a commodity is often explained by supply,” he said. “For example, global oil demand increases every year. What caused the big price collapse was not a change in demand – the cause was the emergence of American shale on the market. This led to much more oil being supplied and resulted in a fall in price.”

An increase in supply, for example in industrial metals, also can occur due to higher levels of capital expenditure. Mr Williams said this happened in the recent past and mining companies had overestimated the demand. They are now bringing supply down to levels to meet demand. “This is a feast/famine market,” he said. “It has a history of expanding to much in the bull cycle and contracting too much in the bear cycle. You go from gluts to shortages.”

One commodity set that is impacted by additional factors, and is treated differently to the others, is precious metals – and in particular gold. The price of this is also affected by the financial services sector and the semi-currency role it can play in portfolios.

“Mood is very important for gold,” said Fahad Kamal, senior market strategist at Kleinwort Benson. “Gold price shifts daily depending on perception and mood. It is extremely sensitive to this – more than any other asset.”

Stephen Ford, investment director at City Asset Management, said that the current situation means the safe haven status of gold has made it an attractive asset for portfolios.

“With negative real rates you are charged to hold cash. There a number of forward risks in the world, such as the fifth largest economy re-negotiating its relationship with the EU. The insurance angle of gold is extremely interesting. We are adding to the money supply at incredible rate, so having something to hold that may devalue more slowly and cost less to hold is attractive.”

Chris Wyllie, chief investment officer at Connor Broadley, agreed that negative interest rate made a case for holding gold, however he added that there is a chance that what is behind the negative rates could change. “Gold does well in times of negative real yield,” he said. “We could be entering a time when the arithmetic behind the negative real yield shifts. In particular, if populism does lead to higher inflation, we could have higher interest rates and higher inflation. The real yield will remain negative as a result, but this is a different scenario to one of negative interest rates.”

Mr Kamal said that if this argument is believed the question still remains as to how much gold should be held in a client’s account.

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