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Money still can be made in metals

Demand for copper, in particular, could continue to make investments appealing throughout next year

FINANCIAL FOCUS

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The case has been made for the value of investing in precious metals. It's time to understand that there are great opportunities in base metals as well, and specifically copper.

Copper is the most widely used industrial metal on planet earth. It is literally in virtually everything: your car, computer, air conditioner, refrigerator, freezer, flat-screen TV cell phone, etc. So as the rest of the world modernizes and industrializes, demand for copper is going through the roof.

Copper prices have increased 18 percent this year, reaching $8.725 per ton on the London Metal Exchange recently. This compares favorably to a 6.5 percent advance in the MSCI World Index of equities, a 6.9 percent return on Treasuries and a 16 percent gain for the Standard and Poor's GSCI Index of 24 raw-material futures.

To better understand this, China uses 40 percent of the copper produced in the world. At its current growth rate, China in 10 years will consume what the entire world uses today. This is what happens when a quarter of the world's population moves from stone huts into high rises.

The problem is that mining companies have failed to keep pace with burgeoning demand from the world's emerging markets. This is because "the major copper reserves that are being produced today come from 100-year-old mines – with few exceptions," said Freeport-McMoRan Copper & Gold Inc. Chairman James R. Moffett. Freeport is the second largest copper miner in the world and the largest listed producer. New deposits require 10 to 15 years to develop. Like gold, it is not something that can be brought on line quickly and easily.

Not only are new reserves becoming more and more difficult to find, but quality of ore is declining. This means that less metal is extracted from each ton of earth. Average ore grades declined to 1.1 percent this year from 1.6 percent in 1990, according to Brook Hunt, a researcher based in Guildford, England.

Production at Escondida, the world's largest copper mine, will drop by as much as 10 percent in the 12 months ending June 2011 because of the lower ore grades being extracted, according to Melbourne-based BHP Billiton – the largest shareholder and third biggest miner.

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The situation of copper can be likened to that of oil. We are not running out of it. We have simply run out of the easy-to-get, cheap stuff. As extraction and refining become more difficult, the product becomes more expensive. This upward price spiral is then exacerbated by steadily increasing demand from the world's developing economies.

Unlike the developed west, China, India, Brazil and others are not interested in being politically correct by way of conserving resources. They are simply interested in living longer and more comfortably. This means using more "stuff." To bring it back around, copper is used in all that "stuff."

Reasonably, I do not expect any decline in demand for copper through 2011. Consumption in China, India, Brazil and the Middle East could expand through 2015. That being said, the biggest threats to higher prices are: tightening Chinese monetary policy in response to the current Bernanke inflated asset bubble, and a worsening European debt crisis. However, these concerns have been extant for some time. Therefore, they may already be discounted by the market.

The demand for copper is driving shares of mining companies higher. Freeport-McMoRan climbed 36 percent in New York trading this year, beating the 9.8 percent gain in the S&P 500 Index more than threefold. It also resulted in JP Morgan and Black Rock launching exchange-traded products backed by the metal.

Folks who missed the high-tech boom of the late '90s and the housing market bubble ought to avoid being late to the metals decade. There's still time.

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