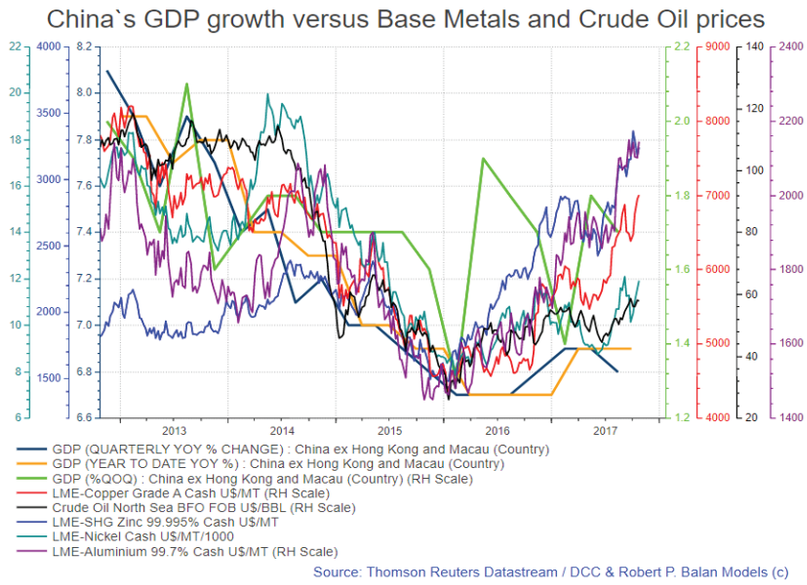
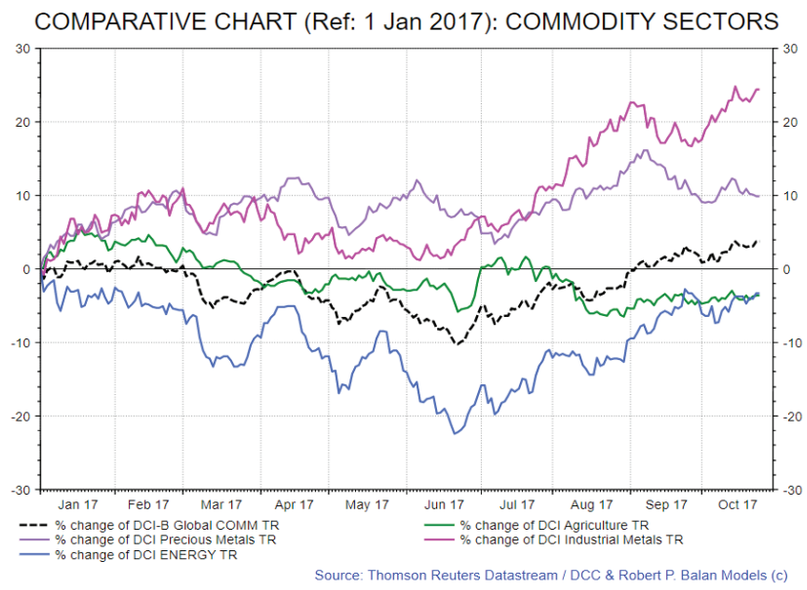
8 / China´s Communist Party Congress provided a strong boost for medium-term outlook in commodities

China represents (and comprises) the demand side of the fundamental equation for commodities as an asset class. With a circa 1.4 billion population (more than 18.5% of the world›s inhabitants), and a steady (although lately flat) economic growth, **China can make or break commodity prices. Recent history can provide proof: double-digit Chinese GDP growth in 2011-2012 boosted many industrial raw materials prices to all-time highs during the period. A deceleration in the Chinese economy in late 2015 and early 2016 caused the prices of these commodities to decline to multi-year lows**. As the country´s economic growth fell below the 7% level for the first time in many years, copper price fell to a low of $4342/MT in January 2016. Crude oil, abetted by copious Saudi Arabia output, also fell to $26.05/bbl in February 2016. At the same time, the Chinese domestic equity market moved to the downside as economic growth in the nation declined to the lowest level since 2010.





That was a severe takedown from an economy that hit a growth of almost 14.50% in 2008, just before the Great Financial Crisis. Apparently, China finally caught up with the maxim that it is a lot easier to achieve double-digit growth levels when the GDP is at a low level than when China´s economy has climbed to the world´s second largest. It became challenging for China to maintain a double-digit growth rate in a larger economy, and that became apparent in 2016 when GDP rose to almost $16.5 trillion, and GDP annual growth remained moored near 6.7%. The Chinese leadership recognized that fact, and in 2016, President Xi Jinping introduced a policy recognizing the «new normal» pertaining to the slowing growth rates. That set the stage for lower but stable rates of economic growth and expansion for the coming years.

The Communist Party of China last week convened for the first time since 2012 to give President Xi another term as leader, appoint new leadership and set the future course of the nation. In the lead up to the Party Congress, many raw materials prices moved sharply to the upside when it became apparent that Mr. Xi would consolidate power further, meaning that China would remain on course for stable and steady growth over the next five years at least. Commodities markets take cues from events in China because of their huge consumption – and the resource markets saw the outcome of the CCP assembly as good news. And indeed, it was.

The positive jolt to the market came at a time when commodities have already risen off the lows in June in the wake of the reflation wave led by the recovery in oil prices. The oil recovery was accompanied by impressive gains in industrial resource materials -- base metals were up 24.42% as a sector through the first nine months of 2017, and some continue to go to higher levels as we come close to the end of October. The base metal sector, as testament to the Chinese Effect, has been the best performer in the general commodities asset class, followed by the precious metal sector. Base metals (DCIIMTR) outperformed the general commodity

The euphony of Mr. Xi´s plans for China`s future has been pleasing for commodities, but in the final analysis, the nitty-gritty lies in the status of China-based leading short-term indicator for base metals. And that leading indicator is flashing somewhat red in the short-term. In line with our outlook for a short-term risk off environment in the financial markets, the TSF indicator (which leads base metals by 9 months), is indicating the possibility of a correction into December. **However, there seems to be a sound basis for another reflation wave into late Q2 2018. That synchronizes with the outlook we have been laying out at the Capital Observer – a seasonal, Christmas rally from early December, which may extend to late Q1-Q2 2018 for cyclical assets.**