# CNBC

# Copper hits 3-year high as analysts debate whether it is overheating

- Copper futures rose above $3 a pound for the first time since November 2014.
- Analysts say copper can go higher as more speculators jump in, but it is getting overextended with a 19 percent gain year-to-date.
- Gold futures rose to $1,300 an ounce for the second time this year before falling back.
- The copper versus gold indicator is rising with copper prices, but it seems to be contradicting low bond yields, in what could be a sign that either the metals market is too upbeat or the Treasury market has it wrong.

Patti Domm | @pattidomm
Published 2:48 PM ET Tue, 22 Aug 2017    CNBC.com

Martin Leissl | Bloomberg | Getty Images

Copper has the wind at its back and is likely to keep moving higher, even though analysts see some reasons for caution.

Signaling stronger global growth, copper is up 19 percent year to dateand up 4.1 percent since the start of August. Copper futures for September rose above $3 a pound in U.S. trading Tuesday for the first time since November 2014. As copper rose, gold futures for Septemberalso briefly climbed above $1,300 an ounce for the second time this year, then slipped below $1,295.

Many are debating whether copper is overheated. At $3 a pound, "copper shows economic recovery that we haven't seen," said George Gero , managing director at RBC Wealth Management.

Copper and gold reflect two ends of the spectrum on the economic outlook but can move higher together.

Analysts say copper, used in manufacturing and construction, has been rising on momentum and bullishness for the global economy. Gold, a safe haven from risk, has been reacting to geopolitics such as recent tensions with North Korea and concerns about U.S. political dynamics. Gold moved higher after dovish comments in Federal Reserve meeting minutes released last week.

Palladium, a metal used in automobiles and electronics like mobile phones,also rose to a high not seen since 2001.

Now, investors are looking ahead to the Fed symposium at Jackson Hole, Wyo., where Fed Chair Janet Yellen and European Central Bank President Mario Draghi speak Friday. Inflation is a double-edged sword for gold, Gero said.

"If the central bankers see inflation, they're prone to hike, which is a short term negative for gold. If they don't see inflation that could be a short-term negative for gold. You're going to have a seesaw between politics and saber rattling from North Korea," said Gero, adding he expects to see gold climb above $1,300 an ounce after Labor Day, and it could then trade up to $1,320.

Copper on the London Metal Exchange was trading just above $6,600 a ton after hitting $6,642.50, its highest level since November 2014.

"I think it was a little expensive for a while," said Bart Melek, head of commodities strategy at TD Securities. "It can get more expensive. It looks to me like there's some momentum here." Melek said he would not be surprised to see it rise to $6,700 or $6,800 on momentum.

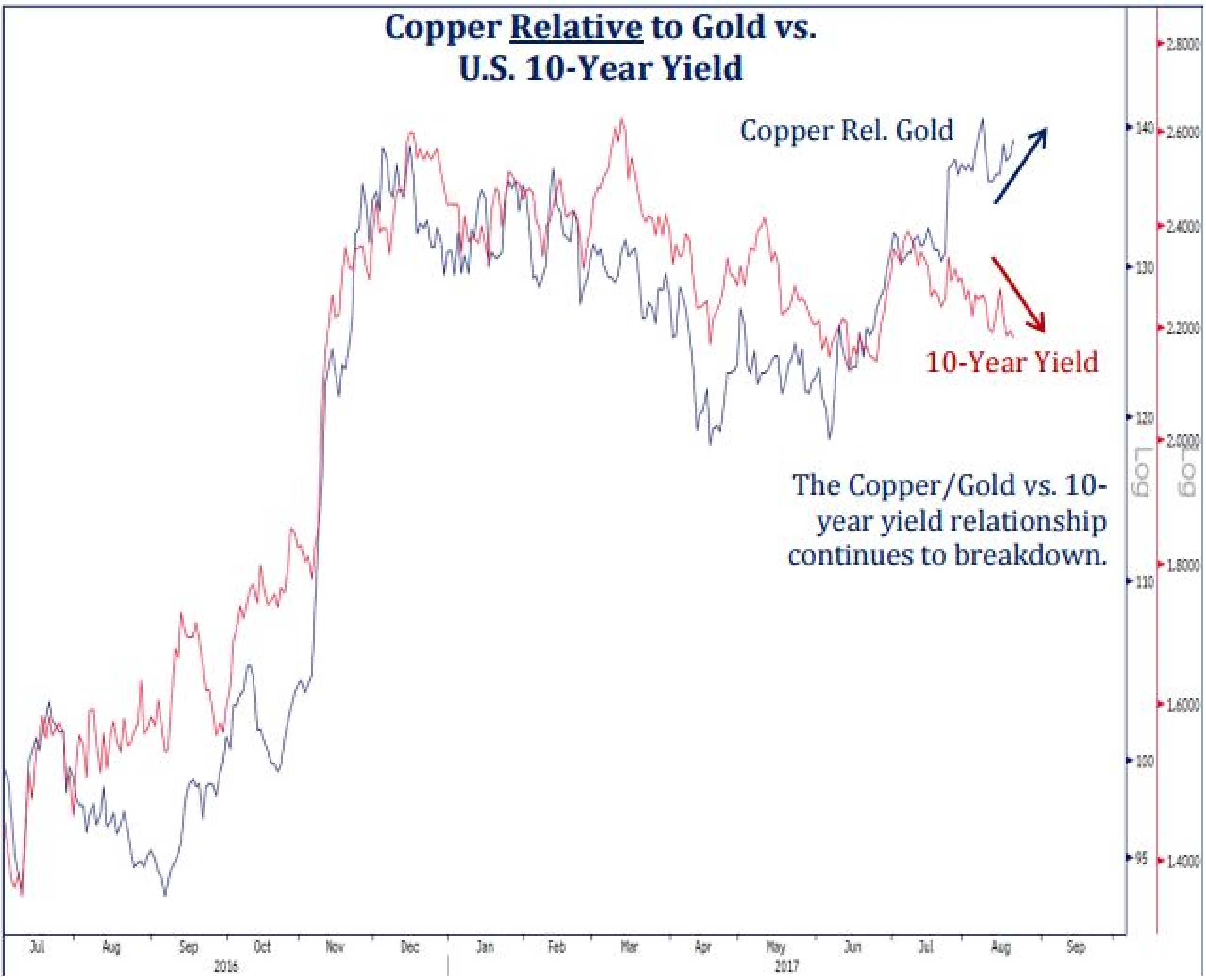
Barclays called the recent copper rally "puzzling." They said supply disruptions have increased and the market is in a deficit, with mined production set to decline this year if those disruptions continue. Those factors and the fact that China has defied expectations for a slow down have helped push copper higher.

"Yet something seems off about this recent rally, and we still remain skeptical of its strength and duration," wrote Barclays' Dane Davis. "We think that this is a market that is overreacting to short-term conditions and ignoring several warning signs."

New projects in Africa, Panama and Chile will boost supply from 2018 to 2020, Davis wrote, and demand in China is slowing and expected to continue to slow.

Strategas Research points out there is a technical dilemma when looking at the popular copper versus gold relationship and bond yields. As copper outperforms, copper versus gold has moved higher, but it has diverged from its normal relationship with the 10-year Treasuryyield. Industrial metals leading is a positive sign for the risk environment and reflects global growth, but super low yields indicate the opposite is at play.

"It's a game of saying who is right here?" said Strategas Research technical analyst Todd Sohn. "Relationships can break down. Copper is outperforming gold. I don't think it's getting ahead of itself but perhaps the relationship [with the yield] is breaking down. Sometimes these things just de-correlate."




*Source: Strategas Research*

Sohn said it may take a jolt like a stock market selloff to bring the relationship back together. Or the Fed could become more convincingly on track to raise interest rates, and that would move yields higher.

"I don't think the move in copper is bad. We look at momentum as a good thing. The overbought condition is reinforcing that the trend is higher," said Sohn.

Gold broke out last Friday to its highest level since the day after the November election on geopolitical worries, a weaker dollar, easy monetary policy and concerns about the effectiveness of President Donald Trump.

"The price of gold is an economic and political barometer of the well being of the world," said Gero. He said depending on what happens, it could eventually reach $1,400, but he expects to see it trade for now between $1,300 and $1,320.

Gero said U.S. politics could be a bigger driver after Labor Day because of the budget and debt ceiling talks in Congress, as well as the potential for tax reform this year. Congress needs to pass a new budget by Sept. 30. That is also when the U.S. is expected to hit the limit, or ceiling, on how much it can borrow.

Gero said the Fed helped drive the gold rally when the market read a dovish bent in the minutes of its last meeting, released last Wednesday afternoon. He said buyers immediately drove gold ETFs higher. Gold followed the ETFs higher, driven in part by worries about the terrorist attacks in Spain last Thursday.

The Fed's comments in the minutes included concern about low inflation, and that reaffirmed some market views that the central bank will not be in a hurry to raise interest rates this year. But the Fed is expected to move forward with plans to unwind its balance sheet this fall, which means it will be buying fewer bonds, potentially driving real interest rates higher.

Patti Domm CNBC Markets Editor