The Insider Trader

Issue 39 January 2010

Markets at a glance

Trendspotter Signals *(click on links to obtain up to-date signal)*

Dow Jones (DJ)

S&P 500 (SP)

FTSE 100 (X)

DAX (DY)

£/US$ (BP)

US Dollar Index (DX)

Crude Oil (CL)

Gold (GC)

Coffee (KC)

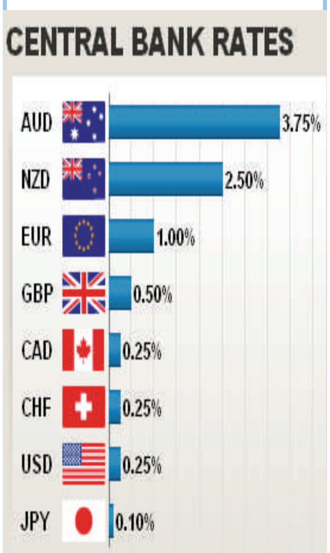
Orange Juice (OJ)

Sugar (SB)

Wheat

Cotton

Rough Rice



Commodities for 2010 which may surprise to the upside

My aim here to look at commodities that are not making big headlines but have the potential to surprise on the upside.

Last year our top market was Palladium with a 143% gain. We also made good money on Sugar (up 95%) and Platinum up 63%. Whilst these markets still look good the media has started to report on them more often which is normally a sign that the easy money has been made.

So in no order here are the three markets that I am looking for higher prices in 2010. The best way to back them would be to purchase Exchange Traded Commodities and to hold the position for at least 12 months. By buying outright you have no stops, margin calls or roll or issues. I hold all my Etfs in US$ however you can buy them in £.

Coffee (Arabica)
ETFS Coffee (LSE: COFF)
ipath DJ UBS Coffee Total Return (NYSE:JO)

Coffee is cyclical in nature as farmers shift to alternate crops or abandon their farms completely when prices are sustained below breakeven for extended periods of time. In 2001, coffee dipped below 50 cents. In 2003 I told the Business Editor of UK Sunday Newspaper that coffee would be a massive growth market and she would make more buying Coffee than buying shares, the price at that time was 60 cents. Today we are at 1.45 per lb and see prices heading to 2.00 within the next 12months which is a view not shared by the market.

The reasons that make me bullish:
New coffee drinkers in Asia. The new middle class have embraced the coffee culture .

US Coffee Monthly Chart continues in a long term uptrend. Whilst we may see a sell off overall the buyers will come in taking prices.

On my last trip to China I saw plenty of people at Starbucks and no they were not all American. True it's a still a luxury with many looking to buy cheaper coffee at street stalls and cafes but they were still buying coffee, remember less than 12 years ago you would struggle to get an Espresso in Shanghai, today I can get as good a coffee in Shanghai as I can in Italy.

A busy Starbucks coffee shop in Shanghai

Coffee sales continue to remain strong in the West and even in harder times many are reluctant to pass on their caffeine fix.

The crash in coffee prices in 1999 to 2000 saw many farmers go out of business and even today 10 years on many have not returned to farming Coffee.

For decades the world's coffee came from Brazil, Columbia and other South and Central American countries, exposing the industry to massive shocks when crop problems occurred. Now countries like Vietnam, India and Indonesia make up a significant supply, however some of these regions especially Vietnam have serious quality issues.

The two main types of coffee are Robusta which is traded on LIFFE in London and Arabica which is traded in the U.S. on ICE.

Robusta is basically the cheap blend and is the one that tends to be used in instant coffee and as an ingredient in other products. The better quality Arabica is harder to grow and the trees take longer to get the first yield.

Robusta coffee trees produce their first crops within about two to three years of being planted. Arabica trees require about four to five years to produce any fruit. So the farmer has an inducement to grow the faster growing variety to take advantage of upswings in the price of coffee. Also, the Robusta coffee tree can grow under a larger variety of environmental conditions than can the Arabica. It is more tolerant of cold and grows well in a wider range of altitudes.

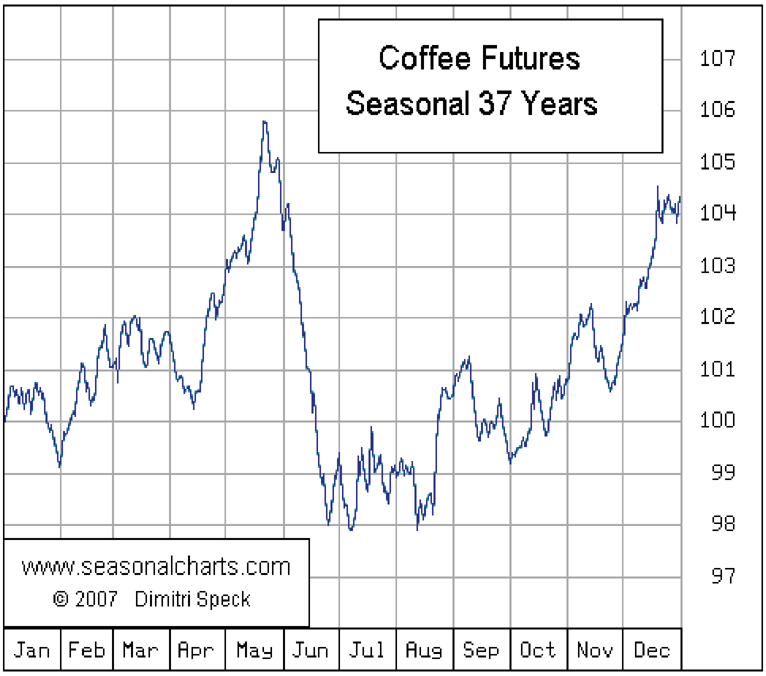
The temptation for farmers is to pass off Robusta as Arabica and get a better price is an understated problem. The ICO (International Coffee Organization) is trying to clean up the business and in 2002 passed a resolution to help farmers improve the overall quality. For this to work and for farmers to make the effort they need a higher and more stable price.

Kraft, Nestlé, Procter & Gamble, and Sara Lee are the "Big 4" roaster companies that buy about 50 percent of all the annual production of coffee. Many still blame the big roasters for screwing the farmers down which in turn caused the crash.

Whilst Brazil may report a better than expected 2010 crop many other regions may come up short including Columbia and Vietnam.

The forward futures market is currently pricing in a 4 to 5 cent premium for December 2010 Coffee which is not excessive pointing to a marketplace which does not expect too many surprises in 2010, as we know markets make big moves when no one expects them.

Seasonal coffee patterns remains strong into May and then sells off June/July.



Lean Hogs
ETFS Lean Hogs (LSE: Hogs)

Right now I cannot find anyone that has anything good to say about Lean Hogs (Pork) which makes me even more bullish.

The Lean Hogs market had been in a down trend for many years however it had a final death blow last year when "Swine flu" which had little to do with Pork hit the media. After hitting a crash low price of 50 cents prices have since bounced back to 65 cents but are still at historically low prices.

Unlike stocks which can go to 0 commodities have an intrinsic value. If Lean Hogs become so cheap then farmers go broke then supply increases short term as more come to slaughter (that's the pigs not the farmers) but then you have a gap which can be years between new farmers reopening and starting to breed again. Another problem facing all agriculture is the lack of financing for feed and fertilizer. The general sense from my sources in the farming world is of fear and survival rather than expansion which means lower supply going forward.

Now let's look at demand.

Pork is still a very cheap product and manufactures and restaurants will continue to look for ways to cut costs and use more pork products. McDonalds are well aware of this and the McRib which is a barbeque pork product is making its way back on the menu. In the past it's been on and off menus and was taken off the US menu in 2006 but is set for comeback

Global Pork Prices

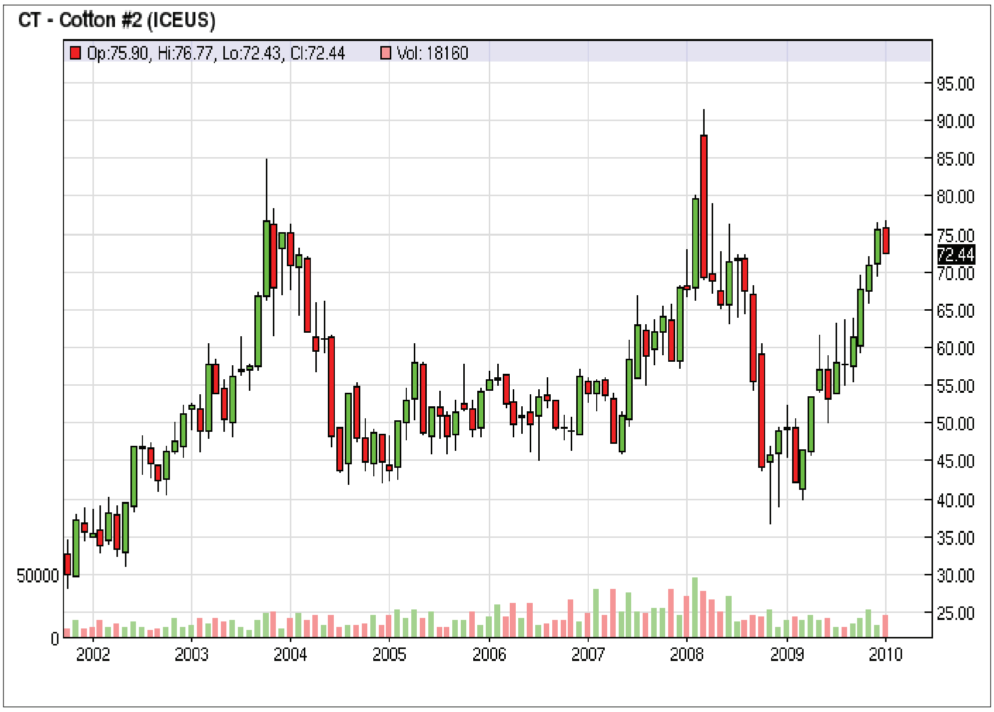
Whilst I see higher demand for pork coming from China that does not help the US as the majority of Pork in the USA is consumed internally. Primary markets for U.S. pork products are Japan (which accounts for about one-third of U.S. exports), Mexico, and Canada. The primary competitors of the United States in foreign markets are Canada, Denmark, and Brazil

So overall I see higher Lean Hog prices as demand picks up but supply does not, **<u>I don't recommend buying futures or spread betting nor do I recommend trying to short term trade as the swings and trading limits are not for everyone.</u>**

I suggest just buying the ETF and forgetting about it. I am well aware that the ETF is not perfect and that tracking errors and rolling futures can distort the market (just look at UNG which does a terrible job at tracking Nat Gas) but I still think ETF Hogs will give you an exposure to gains. Looking for 30% plus gain up to the 90 cent level

Cotton ETFS LSE: COTN
ipath DJ UBS Cotton Total Return (NYSE:BAL)

Lets start by saying I am already long cotton and have been since April 09 so this is not a new trade for me and currently up around 40%. Cotton can be a wild market anyone that was with me back in March 2008 will remember we had a 35% up move and a 35% down move all in 4 weeks which then promoted a CFTC to investigate and it also caused the collapse or subsequent mergers of many Cotton trading houses. The warning and lesson is invest with risk capital only.



Cotton has become a bit of a forgotten market as the global recession diminished demand for end-user cotton products and the shift in Texas towards corn production reduced planted acreage in some areas.

China and Indian remain the biggest growers with the USA coming 3rd.

The whole US cotton growing business is extremely controversial and is kept alive by US government subsidies. The World Trade Organisation have already sanctioned the US and urged them to stop paying farmers, so far this has been ignored however Africa and Brazil are stepping up the campaign and want to see higher prices.

Consolidation of farms, migration from cotton supply to agricultural production and crop problems in Texas all setup a potential bull run this year. I expect cotton to see prices in the 90s before the year is out.

Many looking at Cotton will say is this a repeat of 2008? Whilst no one can be sure I see getting back to 90 as a gradual supply/demand move up rather than a spike and bust.

Risk Warning
All trading and investing involves risk and you should only invest what risk capital that you can afford to lose. These trading ideas are based on buying Exchange Trading Funds outright, should you decide to spread bet then other risks will be present. Only speculate with money you can afford to lose. Spread betting may not be suitable for all readers, therefore ensure you fully understand the risks involved. Past performance is not necessarily a guide to future performance. Ultimately all investment decisions are made by you. Insider Trader does not advise when to open or close a transaction. If you choose to open a transaction it is based on your own judgement and research and at your own risk. It is the responsibility of visitors to this Site to ascertain the terms of and comply with any local law or regulation to which they are subject.