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Prices Reach the Danger Level

By ANNA RAFF | MORE ARTICLES BY AUTHOR

As the Egyptian crisis helps push commodities to record highs, investors need to think twice before jumping in.

Article Comments

DJ-AIG Commodity Indexes

Protests on the streets of Cairo are sowing panic about food supplies and the security of oil-transit routes. Record and multiyear highs in commodities abound.

Cotton continues to break post-Civil War records. Sugar futures are at their highest in more than three decades. Brent crude oil, the European benchmark, traded above $100 a barrel for the first time in two years. Grains are also at their highest prices since 2008, when records were set.

The sheer force of the momentum across the asset class is enough to pull in fresh investment-and that is worrisome. Even though diversification into alternatives such as commodities continues to gain traction, prudent investors should hold back for now. Simply put, prices may be getting toppy.

That isn't to say that they won't rise further. They might. But when price charts cause vertigo, it's probably time to stay away. U.S. cotton is certainly on a dizzying ride: After breaking through $1 a pound in late September, it hit a record $1.8122 last week.

It's a well-worn adage that timing is everything in investing. It's especially important when putting money into commodities and other alternative investments, says Todd Walker, a managing director at Oppenheimer and author ofthe recently published book *Wave Theory for Alternative Investments.* "You can avoid losing a lot of money by going in at the right time," Walker says.

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Gold's recent behavior shows the dangers of investing at record highs.

Gold futures have come down nearly 5% since settling at $1,422.90 anounce on Jan. 3, a record and nearly double the price at the trough in October 2008. Itdoesn't make much sense to buy in while those who doubled their money, or close to it, are taking it off the table.

Those who argue gold prices will continue to rise point to its growing acceptance among different kinds of investors. However, markets that are deeper and more liquid will attract both buyers and sellers. Financial innovation and the increasing sophistication of exchange-traded funds means that going short, or betting on price declines, will become just as easy as going long in commodity markets. That is reason enough to avoid treating the metal as a one-way bet. 1.

For those interested in adding exposure to raw materials, the challenge is rooting out the underperforming ones. Natural gas might be an option. Despite its bearish fundamentals

-an onslaught of supply from U.S. shale formations and lagging demand growth-natural gas looks more attractive from a wave-theory perspective. It hit its all-time high of $15.427 per million British thermal units in December 2005 and scraped a seven-year low of $3.206 in August 2009. Futures trade around $4.50 on the New York Mercantile Exchange.

"The point is, you avoid putting too much at the peak or too little at the trough," Walker says.

Investors with time horizons that are longer than a month or a quarter don't have to time the extremes exactly. There's opportunity to take measured bets once a wave up or down is well underway.

COPPER FUTURES GAINED 20.55 cents per pound last week, or 4.7%, to settle at $4.5710, a record on the Comex division of the New York Mercantile Exchange. The metal was helped by a drop in the U.S. unemployment rate reported Friday, and talk that demand still would outpace supply this year was also supportive.

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