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Portfolio diversification from precious commodities

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With risk aversion rising and the US imposing commodity-specific tariffs, some investors might be concerned about commodities exposure. We would instead urge investors to consider the fundamental supports for commodities as a whole, and the individual components. The asset class has the capacity to deliver decent diversification benefits for traditional bond-equity portfolios. With volatility likely to be elevated in the near term, gold remains a key portfolio hedge, while silver, copper and Brent crude offer volatility-selling opportunities to boost portfolio income.

Over the last two months, risk appetite has been eroding as the Trump administration's commitment to using tariffs as a policy tool became more apparent. This has accelerated over the last few weeks, with the VIX equity volatility index rising from under 15 to just below 30 earlier this week—levels seen just one other time in the last two years. The S&P 500 and MSCI All Country World Index are both down close to 9% and 5%, respectively, as markets grapple with the detrimental effects of tariffs on global growth. Given the pro-cyclical nature of many commodities, investors might be wondering if it would be prudent to stay away from this asset class.

Our answer would be a definite "no." While we acknowledge that in the near term, the intensification of tariff-related risk aversion from April might see the CMCI Composite Index fall in the near term, we actually remain positive on commodities overall over the year. Three key drivers stand out: increasingly expansionary fiscal policy (especially in Germany and China); rate cuts reviving manufacturing in 2H25 as tariff concerns ebb; and the fact that supply constraints remain in place. We highlight below some possible ways to utilize the potential impact on commodities to boost portfolio returns.

Taking exposure via an active commodity strategy. We are positive on commodities over the medium term. The asset class has the capacity to deliver decent diversification benefits for traditional bond-equity portfolios. We believe that an active commodity strategy can capture broad price trends on the asset class level as well as sector-specific developments from a demand-supply perspective. Our preferred approach is to go long in broader commodities indexes that include futures while shorting narrower commodities indexes without futures. This should allow investors to generate yield through the outperformance of the broader index, while also providing diversification benefits.

Metals to show their mettle. Both precious and industrial metals are attractive additions to portfolios in our view. Gold remains a key portfolio hedge against near-term uncertainty, but also against episodic bouts of risk aversion further out, which cannot be ruled out given the Trump administration's capacity for disruptive and unorthodox governance. Silver has lagged gold and is due for a catch-up, in our view, especially when a recovery in manufacturing takes place. Such a revival would likely also see copper—the highlight within industrial metals—outperform despite the prospect of tariffs. We would note that the US relies on imports for 40-50% of its domestic copper usage on account of its limited smelting and processing capacity. We continue to like gold as a portfolio hedge and maintain our USD 3000/oz price target for this year. In our risk case of prolonged universal trade tariffs, we see the gold price rising to USD 3,100-3,200/oz. We expect the price of silver to rise to USD 36-38/oz over the coming quarters and thus like selling the downside risks from USD 30.5/oz over the next three months for a yield pickup. We see copper moving toward USD 11000/mt by year-end and thus like selling the downside in copper below USD 9,150/mt over the next six months.

Brent crude oil offers volatility-selling opportunities. Although recent rhetoric from OPEC+ has been taken by the markets as an indicator of a potential increase in supply, we think the effective production increase will be smaller than the announced amount. Also, there is no indication that the group is fighting for market share and appears to be focused on supply management to keep the oil market in balance. On tariffs, US refineries are highly dependent on crude imports from Canada and Mexico, which means the potential supply constraints will be supportive of prices. Selling the downside price risks in Brent crude oil below USD 65/bbl over the next six months thus strikes a balance between our price outlook and near-term risks, in our view.

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