MONEY MORNING
YOUR GUIDE TO FINANCIAL FREEDOM

How to Profit As Copper Becomes the "New Gold"

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The Statue of Liberty is one of the most recognizable American icons in the world.

And as she towers 305 feet above Ellis Island, what's Lady Liberty wearing? Copper – 60,000 pounds of it.

Clearly, copper's big in art. It's also a key metal that keeps the world economy humming. Copper consumption has grown at an average annual rate of 4% since 1900. China and India – which some analysts describe as the combined market of "Chindia" – where one of every three human beings resides, needs loads of this element to meet its modernization requirements for electricity and infrastructure.

Copper is also used in today's currency, where most U.S. coins are actually 92% copper, and 8% nickel.

MONEY MORNING PROMISE

Keith Fitz-Gerald's promise to all new *Money Morning* Readers.

But there's no denying that, given the choice, nearly everyone prefers gold. It's valuable, it's seductive and it's mystical.

Ancient kings fought wars to amass it. Yet, for thousands of years, its most enduring role has arguably been in the form of money – as a store of value.

That's because fiat-paper-currency experiments have never lasted, and always ended badly.

Increasingly, followers of the Austrian School of Economics are nostalgic for gold to regain its former glory, perhaps "backing" a new international currency.

But despite gold's much longer history as true money, copper – the much humbler metal – could be positioning itself to upstage gold.

China's Paper Mountain

If copper is to replace gold as the world's most-valuable metal, China will play a huge role. With all its uses – from hybrid cars to an electricity grid – copper may become both an inflation hedge *and* a strategic asset.

Today, China sits atop a paper Everest, with foreign-currency reserves worth more than $2.4 trillion. No public financial institution boasts that degree of financial-asset firepower. Of that total, more than $800 billion is held in U.S. debt.

A war chest of this size serves as a great insurance policy during tough economic times. The trouble is that China is painfully aware of the damage that U.S. dollar inflation will inflict on that massive hoard of greenbacks.

During a visit to New York last February, Luo Ping, a director general at the China Banking Regulatory Commission said: "We hate you guys. Once you start issuing $1 to $2 trillion… we know the dollar is going to depreciate, so we hate you guys, but there is nothing we can do."

That's not completely true. There are some things that China is already doing. China recently announced an increase in its official gold reserves to 1,054 tons, an increase of 76% from 2002 levels. China accomplished this without a single purchase on global bullion markets. How? By quietly becoming the world's largest gold producer, then buying up all that it produced. (And, that's not the only commodity China's stockpiling, check out **this report**.)

Red Gold to Back a New Currency?

I expect China will continue to covet gold. But with such a large reserve in dire need of both diversification and securitization, this emerging global superpower of 1.3 billion citizens has set its sights on other tangibles. Let's face it, the gold supply is small, and China needs resources of *all* kinds.

So it makes perfect sense for Beijing to trade holdings it has too much of – like U.S. Treasuries, for example – for assets China needs more of, like copper. There are multiple benefits to this strategy, too: Not only is China swapping a holding whose value is declining (dollar-based holdings) for a tangible asset whose value is on the rise (copper), it's also getting (in copper) an asset that's central to its ongoing infrastructure build-out.

Yet some believe that China's actions reflect a new strategy, since this acquisition binge goes way beyond national consumption requirements. And with a full war chest, that buying could be sustained for some time.

Copper could be used to back a currency, but it's also necessary for the modernization of China, and even in the next wave of automobile technologies – both electric and hybrid – an industry this nation could lead.

China's share of the copper market is a world-dominating 38%. Clearly, its 2009 record import levels helped vault the copper price by 226%, from its January slump of $1.50 per pound to a recent high near $3.40 per pound.

As China was buying hand over fist in early 2009, copper prices began to rebound. London Metals Exchange (LME) statistics underscore that copper stockpiles were raided from February until mid-July.

What happened next, however, was both surprising and counterintuitive.

As copper stocks continued to rise in the second half of 2009, the price of copper rose, as well – zooming from $2.50 a pound to about $3.40. The last time copper stockpiles were above 500,000 tons, the metal's price was $1.50. So copper at $3.40 was looking quite overbought considering current stock levels.

Dr. Copper's Diagnosis

Commodities traders often refer to this all-important non-ferrous metal as "Dr. Copper." Its price and supply/demand characteristics are widely assumed to reflect the health of the world industrial economy, hence its "Ph.D. in Economics."

Given that reputation as an excellent barometer, it's tough to understand just what's keeping copper prices high at a point in which the *risks* of a double-dip recession worldwide are exceeded only by the *fears* of one.

So what's propping up copper prices? For one thing, hedge funds are taking physical positions in the metal, rather than through futures contracts, due to concerns the Commodity Futures Trading Commission (CFTC) will bring in position limits.

What's more, China's State Reserves Bureau has purchased large amounts of copper, pushing the nation's year-over-year imports up by 63%.

The Longer-Term View

I am convinced that we are still relatively early in a secular commodity bull market. In fact, with the modernization of Chindia and numerous other less-developed nations, I expect this bull market will be one for the record books. Fundamental demand coupled with inflation will push resource prices to unimaginable heights.

But that doesn't mean – in the intermediate term – that copper hasn't gotten ahead of itself. Look for its price to weaken somewhat before the price of the metal resumes its upward trajectory.

Even if a new international commodity-backed currency were to emerge, it's likely that copper will only be *one* of its underlying components.

For now, copper will continue to be overwhelmingly used in industry and infrastructure, with 75% of output going into electrical applications.

From my vantage point, gold will remain the ultimate form of money, while copper will retain its Ph.D. in Economics.

That's why I'm not expecting copper thieves to steal Lady Liberty's dress and melt it down, but I do expect copper to become increasingly valuable as our secular commodity bull rages on.

The last question investors need to answer is a simple one: How do I profit from this trend? If you're looking for a simple way to play copper directly, check out the iPath DJ AIG Copper TR Sub-Index (NYSE: JJC) Exchange-Traded Note. This ETN tracks the price of Copper High Grade Futures Contracts traded on the New York Commodities Exchange.