PERCENTAGE PLAY
Actionable insights

NUMERA ANALYTICS

EMBRACING UNCERTAINTY

Outperforming the market requires accurately estimating opportunities and risks: it's about identifying favourable odds through probability analysis. ***Percentage Play*** *offers high conviction calls based on our cutting-edge probability forecast models.*

THIS WEEK'S PLAY: LONG ALUMINIUM PRICES

THE OPPORTUNITY: A shift in US economic policy calls for some inflation protection. Aluminium is an excellent hedge, and stands to benefit from a tighter balance as production in China hits a government-imposed ceiling on capacity.

THE ACTION: We find a near 80% chance that LME aluminium prices rise by double digits this year to over $2850. Investors can act on this dynamic via the specialized DBB ETF, or with call options on COMEX or LME futures.

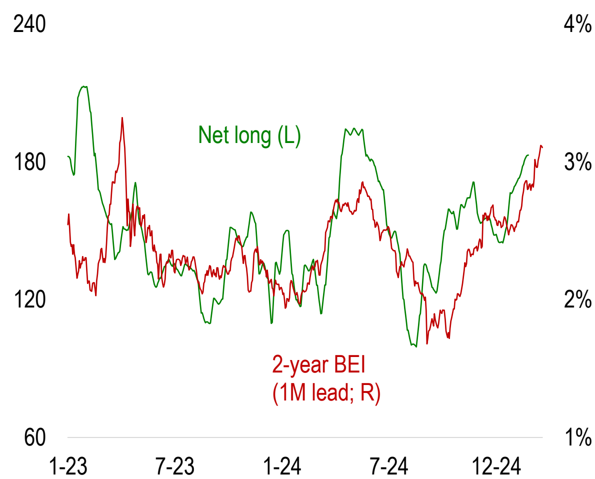
No lightweight bet – As we have discussed in recent publications, President Trump's protectionist agenda increases near-term inflation risks by fueling inflation expectations. Even if this does not prompt a reversal in Fed policy, we find that adding some inflation protection via hard assets improves the risk-reward profile of multi-asset portfolios.

But while alternatives often provide protection, their hedging ability varies markedly over time. Last month, we conducted a study evaluating the hedging ability of 60 competing assets. Within commodities, we found that oil and base metals are usually the most reactive to inflation shocks, especially when driven by demand-side factors.

Across metals, aluminium (Al) has the best hedging capabilities, consistently exhibiting a positive correlation to inflation surprises. In line with our findings, investor demand for the lightweight metal has picked up this year, amid a resurgence in breakeven inflation (F1).

Yet even if Al usually benefits from sticky inflation, its hedging ability depends crucially on valuations and market fundamentals. Last year, prices rose 4.7% in real terms, versus flat growth in all base metals. One important source of support was resilient global demand, which based on our models lifted prices by nearly 7% (F2).

F1: Investment demand is on the rise
Net long Al positions vs. breakeven inflation

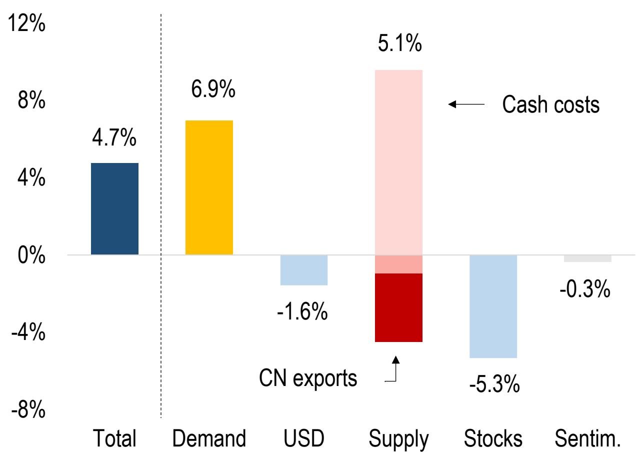


Takeaway: Net long positions on aluminium in the LME and SHFE have picked up since late 2024, partly reflecting policy uncertainty (including worries over higher inflation). Source: LME, SHFE, Department of Treasury.

This, in turn, reflects a clear advantage in its end-use exposure. While most metals depend heavily on building construction in China (down 23% last year), aluminium relies primarily on transportation equipment and increasingly on electrification. Strong EV production in China and rapid growth in solar and power infrastructure last year translated in consumption growth of around 3.5% in full-year 2024, compared to e.g. a 3.2% decline in steelmaking.

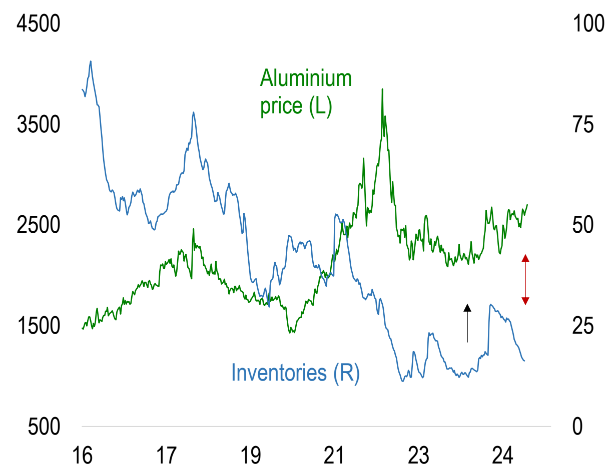
In addition, notice from F2 that Al prices faced significant upward pressure from raw material costs. The key driver, in this respect, were disruptions in the supply of bauxite in Australia and Guinea, causing alumina costs to double. Bauxite shortages hit smelter margins, particularly outside China, where alumina makes up 40%+ of cash costs.

F2: High availability capped 2024 returns
Drivers decomp. - Real LME Al prices - 2024



Takeaway: Last year, Al prices benefited from resilient global demand and a sharp rise in bauxite and alumina costs. However, gains were paired back by high global availability and a strong USD. Source: Numera Analytics.

F3: Market balance has now tightened
LME Al price vs. inventory days of supply



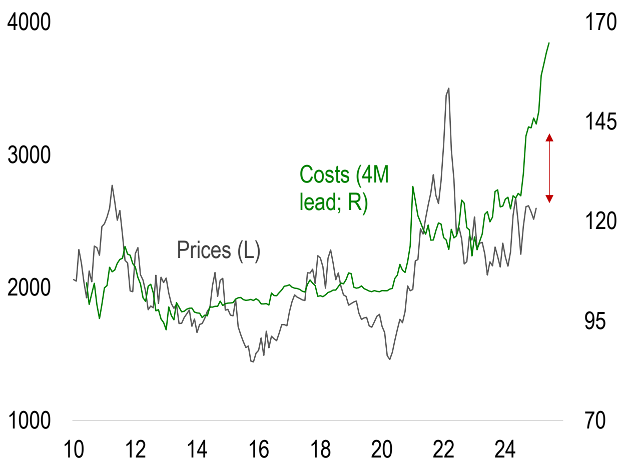
Note: Chart compares LME primary aluminium prices against LME and SHFE warehouse inventories relative to global Al consumption (the inventory DOS series is indexed to 2015=100). Source: LME, Numera Analytics.

Yet despite higher manufacturing costs, global availability increased last year, resulting in higher exchange inventories (F3). This reflected double-digit growth in CN aluminium exports, enabled by two factors: Firstly, heavy rainfall allowed the restart of 1.1M MT of capacity in Yunnan, after hydropower shortages prompted temporary shuts. Secondly, a 13% export tax rebate encouraged smelters to direct tons abroad, increasing global supply.

Following strong output growth last year, CN production is only 2% below the 45M MT ceiling set by Beijing in 2017 in the hopes of curbing oversupply and GHG emissions. In a context of strong transportation and green energy demand, this cap could easily result in shortages in 2025, especially considering the government has eliminated the VAT rebate for aluminium products this year, discouraging offshore sales (themselves 10% of global supply).

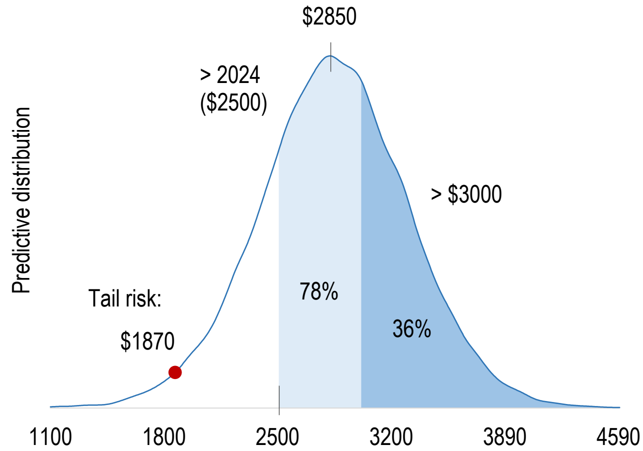
Besides a tighter balance, Al prices should continue to rise in response to high alumina costs, even if these have eased since January in anticipation of capacity additions in India and Indonesia. As we can see in F4, cash costs lead prices by around 4 months, so the recent cost normalization should not have a material near-term impact.

F4: Smelters facing major cost pressures
LME aluminium price vs. CA cash cost index



Takeaway: Costs of producing primary aluminium in Canada are up 30% YoY due to a sharp rise in bauxite and alumina prices. Cash costs lead spot LME prices by around 4 months. Source: LME, Numera Analytics.

F5: Aluminium prices should rise further
LME aluminium price outlook - Dec. 2025



Takeaway: There is a 78% chance that LME aluminium prices are higher than in 2024 this year, and a 36% probability that prices break above $3000. Should prices fall, the worst potential outcome is a $800 drop to $1870. Source: Numera Analytics.

F5 shows our year-end outlook for LME prices, as derived from a recently developed probability forecast model. The framework controls for a combination of macro and market-specific drivers, featuring leading indicators in an effort to limit errors in prediction. The model identifies a 78% chance that prices will trade above 2024 levels, as a tight CN balance more than offsets any downside risk from weaker demand in the US now that tariffs have taken effect.

Even if prices are already up 6% this year, the framework still identifies considerable upside, expecting prices to rise by at least the same extent for the remainder of 2025 to over $2850. For non-specialized investors, a simple way to gain Al exposure is via the thematic DBB ETF, which has a 90% correlation to aluminium prices on 12M holdings.

Alternatively, funds with an active use of derivatives could directly go long on aluminium via COMEX or LME futures. The forward curve is in slight backwardation, increasing the appeal of call options. For instance, an at-the-money call on COMEX May '25 futures has a 64% probability of execution, with expected gains of 160%. Like any leveraged trade, expected losses are also high, but at -60% it makes for an attractive risk-reward balance.

In case you missed it ...

- **Commodity Outlook** (13/02): Drill, baby drill?
- **Global Asset Allocation** (20/02): Protecting against inflation risk

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