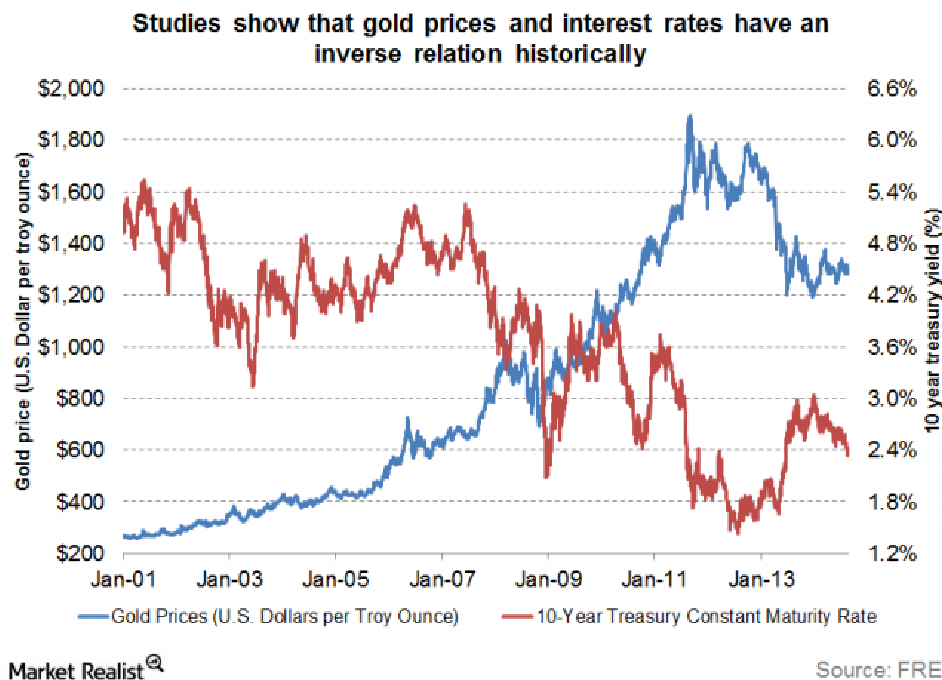
Why you should avoid commodities in a rising rate environment

By Russ Koesterich, CFA - Disclosure • BlackRock • Aug 27, 2014 1:55 pm EDT

Other commodities have suffered as well: Most agricultural commodities are down between 5% and 10% year-to-date, and oil prices have slid on less angst over Iraq and the Middle East. Among these various commodities, I remain particularly cautious of precious metals given their sensitivity to higher real rates.



Market Realist – The graph above shows the inverse relationship between gold and ten-year Treasury rates. Metals like gold (IAU) and silver (SLV) usually display an inverse relationship with interest rates, according to many academic studies.

According to a recent National Bureau of Economic Research essay by Claude Erb and Campbell Harvey, gold and ten-year Treasury (IEF) yields have moved inversely in the past decade. According to their econometric model, if the ten-year Treasury yield rises to 5%, gold (GLD) will fall to $471 an ounce. For gold to go up to $1,900 per troy ounce, Treasury yields will have to fall to below 1%. This is an unrealistic scenario in the context of rising rates.

Oil (USO) has recently slid based on easing geopolitical tensions. Yet the energy sector (XLE) still looks like a good investment due to the supply and demand dynamics of the market. Read more in our series Impact of Middle East tensions—oil prices and equity portfolios.

Read on to the next part of this series to learn where you should invest in a rising rate environment.