



Commodity Investment Products and the Grain Complex

March 31, 2009

NGFA



Commodities as an Asset Class

- Inflation Hedge
- New Piece of the Portfolio Allocation
- Exposure to China and Emerging Economies
- Perception of Return $>$ or $=$ Stock, Bonds and Real Estate



CPI- Inflation

- The CPI was created after World War 1 for calculating cost of living adjustments to wages. Regular publication started in 1921. CPI's stated goal is to calculate what it costs to maintain a constant level of living defined as 'satisfaction' (or 'utility' in economics).
- This summary intends to break down the changes to the CPI and present an idea of how it has changed over the last several decades

All of Inflation's Little Parts

- Each month, the Bureau of Labor Statistics gathers 84,000 prices in about 200 categories — like gasoline, bananas, dresses and garbage collection — to form the Consumer Price Index, one measure of inflation.
- The categories are weighted according to an estimate of what the average American spends, as shown on the next page.



Interactive pie chart of CPI components:

http://www.nytimes.com/interactive/2008/05/03/business/20080403_SPENDING_GRAPHIC.html

An Average Consumer's Spending

Each shape below represents how much the average American spends in different categories. Larger shapes make up a larger part of spending.

Color shows change in prices from March 2007 to March 2008



ZOOM IN ZOOM OUT

Food and beverages 15%

The high price of oil is a factor that has made food prices rise quickly.

Miscellaneous 3%

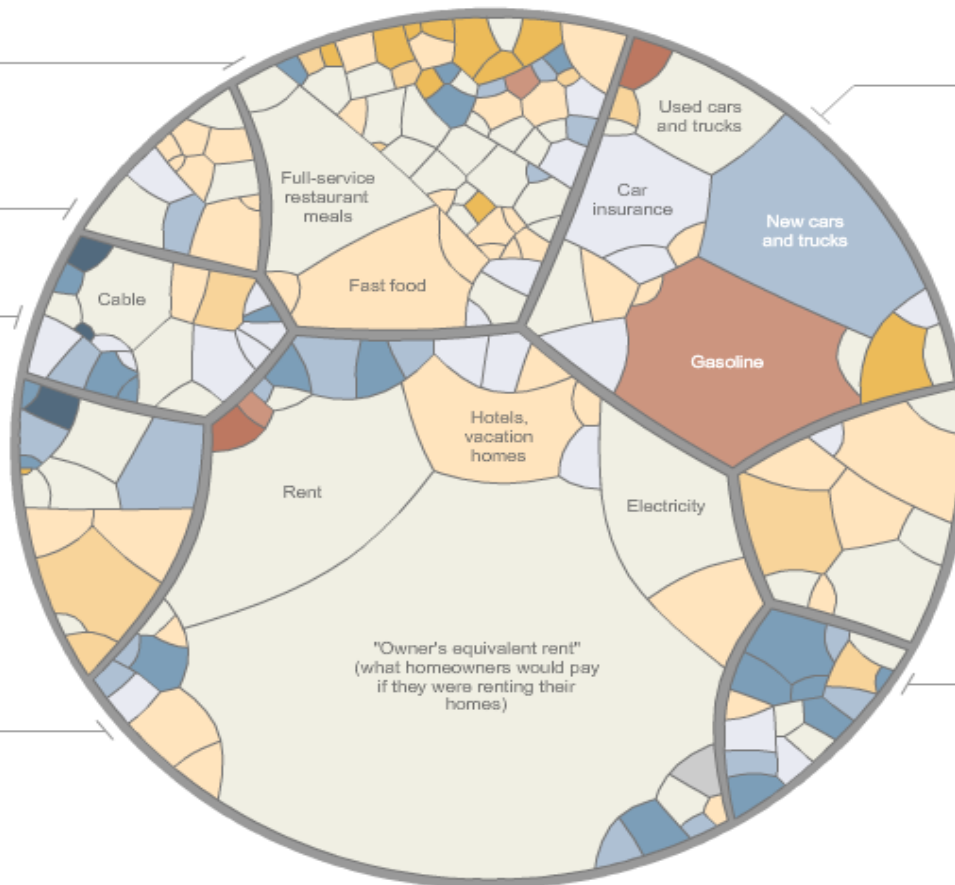
Recreation 6%

Education/Communication 6%

Cellphones were added to the index in 1997. Because the Consumer Price Index can be slow to add new goods, which are often cheaper, it may overstate parts of inflation.

Housing 42%

In the C.P.I., home ownership costs track rent prices more closely than housing prices. This means inflation may have been understated when home prices were rising faster than rents.



Transportation 18%

Gas is 5.2 percent of spending nationwide, but only 3.8 percent in the New York area.

Health care 6%

As a group, the elderly spend about twice as much of their budget on medical care.

Apparel 4%

The ratio of spending on women's clothes to that on men's clothes is about 2 to 1.

Source: Sources: Bureau of Labor Statistics; Michael Balzer, University of Konstanz (Germany) Matthew Bloch, Shan Carter and Amanda Cox/The New York Times

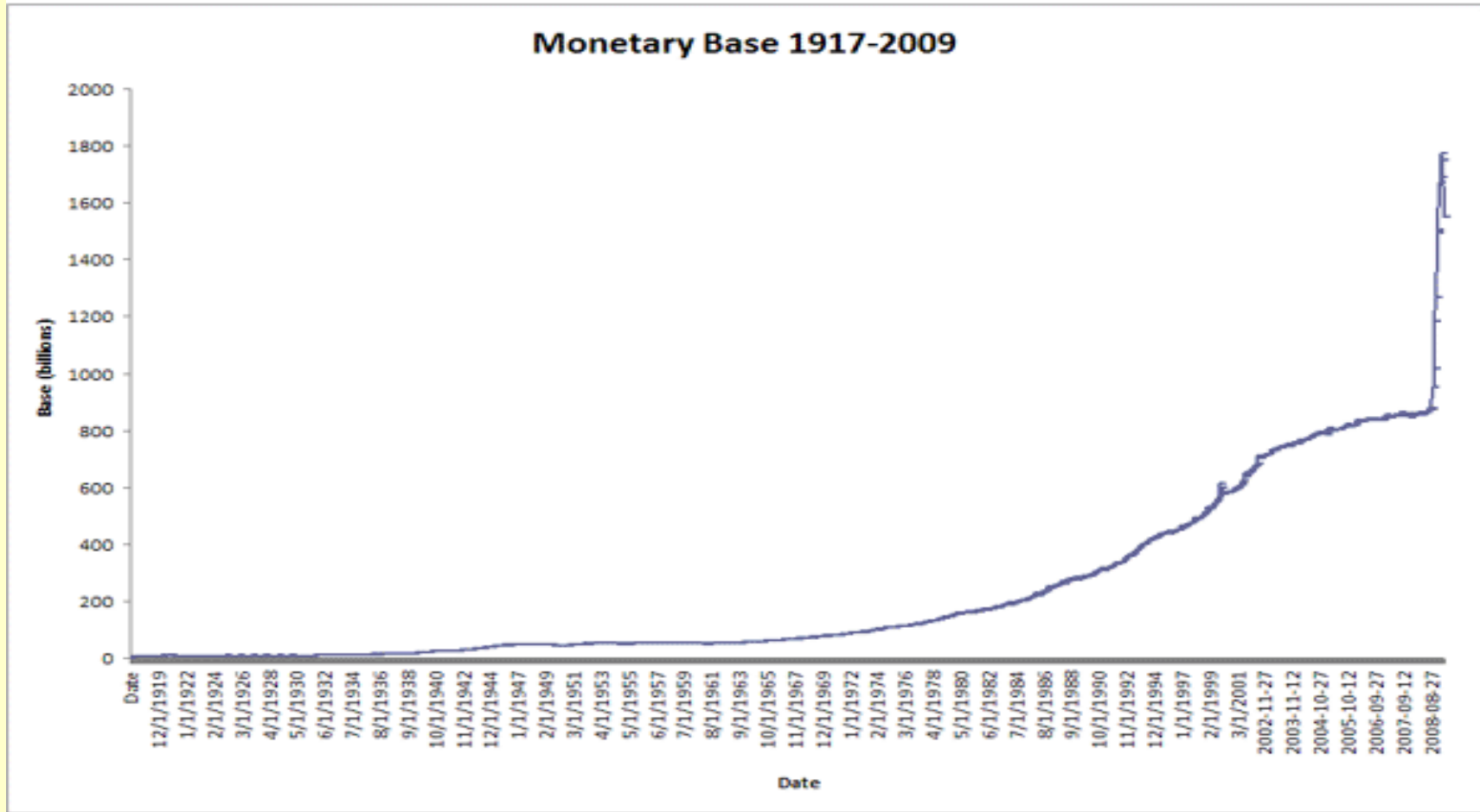


Some real-time and future expected inflation barometers:

- TIPS spread over 10 yr treasuries (use IEF/TIP ETFs)
- Money supply, (MZM, M3-M0 - although Japan in 1990's was a setback for this barometer given you had double **digit increases in M3 occurring contemporaneously with deflation**)
- ERCI Future Inflation Gauge (has stat significant predictability of Fed Fund rates)
- Eurodollar futures
- Hourly wages (wages are estimated to be 60-70% of total costs in US)
- Commodities
- Currencies relationships
- Treasury curve



US Dollar Monetary Base 1917-2009

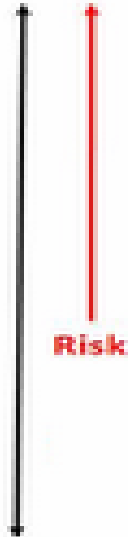




Money Supply Definition

Money Supply

Delay, Decay,
Intermediation



Risk

Immediacy

M3 = M2 + CD's > 100,000 + Money Market Accounts for Institutions
+ Short Term Repo Agreements + EuroDollars

Eurodollar deposits are dollar-denominated deposits held at foreign offices of banks worldwide. The definition of Eurodollar broadened significantly from its inception. We "think" it is the non-conspiratorial reason why the Fed stopped publishing M3, as its calculation became increasingly difficult.

M2 = M1 + Savings Deposits + CD's < 100,000
+ Money Market Accounts for Individuals

M1 = M0 + Checking Deposits + Traveler's Checks
+ Debit Card Accounts

Fedsters are cautioned that since 1994, the level and growth of M1 have been depressed by small-currency programs that reduced transactions deposits (demand deposits and other checkable deposits) in response to calls for M1 overnight to reduce banks' non-fed reserves.

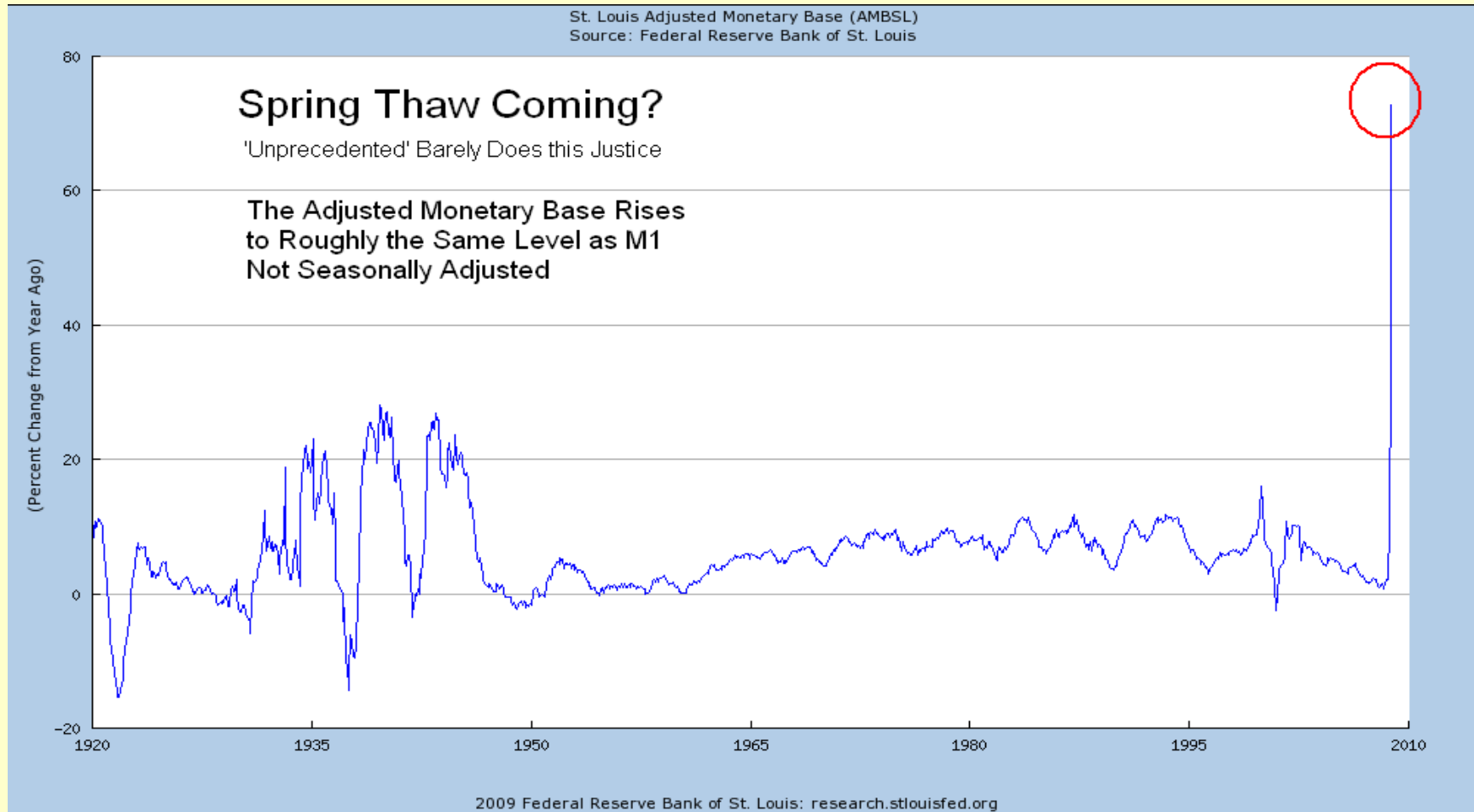
M0 or Monetary Base

Currency and Coins in Circulation
and in Federal Reserve Banks

Note: The **Monetary Base** is the sum of currency in circulation outside Federal Reserve banks and the U.S. Treasury and deposits of depository financial institutions at Federal Reserve banks. The **Adjusted Monetary Base** equals the Monetary Base and the reserve adjustment magnitude (RAM). **AMB** is an index that measures the effects on a central bank's balance sheet of its open-market operations, discount window lending, unsterilized foreign exchange market intervention, and changes in statutory reserve requirements. The Fed believes that this index is important because the long-run path of a monetary economy's price level is primarily determined by the path of the central bank's balance sheet, adjusted for the effects of changes in statutory reserve requirements.



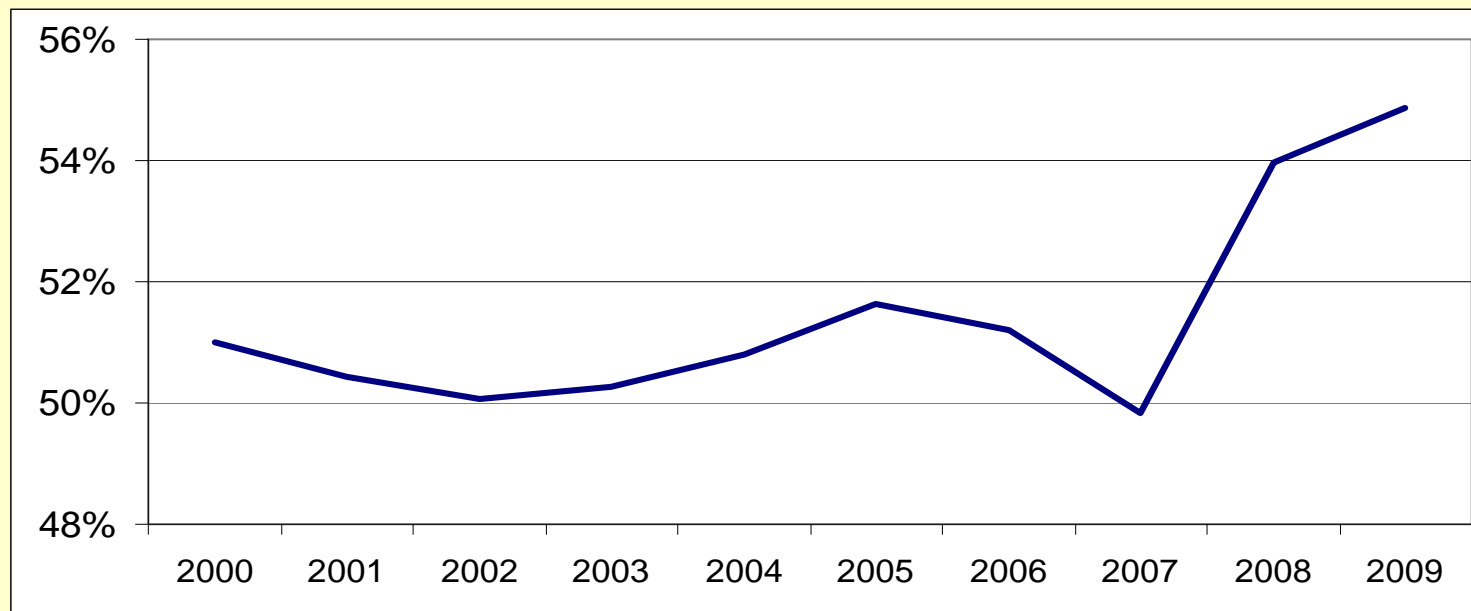
M1=Cash and Other





China

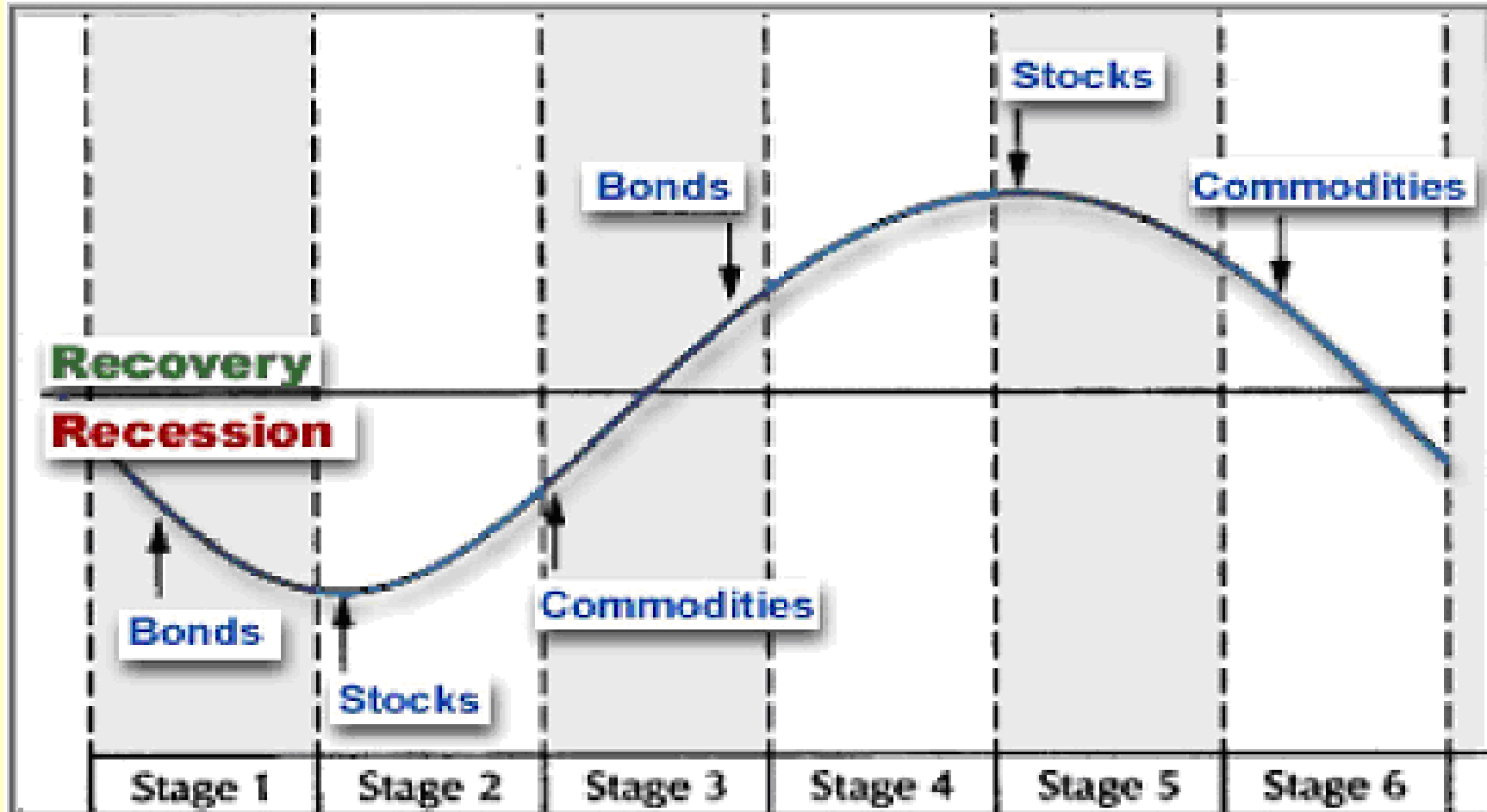
Hog Supply (as a % of Total World Hog Supply)



- Total Chinese Hog Production: **1,062,000,000!**
- US Production, by comparison, is 150,000,000
- China had a 4.5% increase in 2008 = 48,000,000 hogs
- Based on the latest arable land and population data from the World Bank, China must feed 9.1 persons for each hectare of arable land, whereas the United States needs to feed only 1.7 persons.



Timing the Business Cycle





A Reason for Commodity Index Funds

Stock, Bond and Individual Commodity Futures Performance over the Business Cycle, 7/1959 – 3/2004*

Avg. Monthly Annualized % Returns					Phase Avg.			
Data Series	Starting Date of Data Series	Overall Avg.	Expansion Avg.	Recession Avg.	Late Expansion	Early Expansion	Early Recession	Late Recession
Inflation	07/01/59				4.6%	3.6%	7.6%	5.4%
S&P Total Return	07/01/59	11.1%	13.1%	1.7%	10.4%	18.1%	-15.5%	17.3%
Corporate Bonds TR	07/01/59	7.7%	7.2%	12.1%	3.6%	11.5%	-2.9%	25.7%
Eq. Wtd Futures TR	07/01/59	11.0%	13.4%	0.9%	16.9%	7.4%	4.3%	-1.7%

Inflation is Highest during a recession??

1959 -2004 * Yale Study on Commodities

Gorton, Gary and Rouwenhorst, K. Geert Facts and Fantasies about Commodity Futures 2004



Commodity Cycles

1959 -2004 * Yale Study on Commodities

Avg. Monthly Annualized % Returns					Phase Avg.			
Data Series	Starting Date of Data Series	Overall Avg.	Expansion Avg.	Recession Avg.	Late Expansion	Early Expansion	Early Recession	Late Recession
Eq Wt Spot	07/01/59	8.7%	10.8%	-2.0%	12.3%	7.7%	0.1%	-3.7%
Eq Wt Energy Futures	11/30/78	19.2%	14.7%	-0.8%	17.1%	6.0%	5.4%	-7.8%
Eq Wt NonEnergy Futures	07/01/59	10.2%	10.2%	-12.9%	15.7%	7.2%	1.8%	0.5%
Eq Wt Industrial Metals Futures	07/01/59	15.4%	18.4%	6.3%	27.2%	3.5%	15.7%	-29.8%
Eq Wt Industrial NonMetals Futures	01/05/60	7.7%	10.9%	-14.9%	13.5%	8.7%	-5.4%	-13.4%
Eq Wt Precious Metals Futures	11/06/63	9.4%	11.5%	-8.7%	17.9%	2.3%	0.1%	-10.5%
Eq Wt Animal Products Futures	09/19/61	11.8%	15.1%	-7.7%	17.9%	9.0%	-3.6%	5.8%
Eq Wt Other Food Futures	07/01/59	9.9%	6.4%	20.3%	11.7%	14.3%	15.7%	0.2%
Eq Wt Grain and Products Futures	07/01/59	8.0%	7.1%	0.4%	9.8%	5.1%	-2.8%	11.3%
Natural Gas Futures TR	04/05/90	16.4%	11.3%	-31.0%	10.3%	5.2%	-15.6%	-21.5%
Crude Oil Futures TR	04/04/83	19.1%	13.1%	4.5%	12.1%	4.4%	26.3%	
Unleaded Gas Futures TR	12/04/84	21.0%	14.4%	4.4%	13.1%	3.2%	23.6%	
Heating Oil Futures TR	11/15/78	16.4%	12.5%	6.1%	14.4%	3.0%	15.6%	
Live Cattle Futures TR	12/02/64	13.2%	15.2%	1.3%	16.9%	11.1%	-1.1%	-2.7%
Lean Hogs Futures TR	03/01/66	15.0%	15.1%	2.0%	19.5%	16.3%	-10.8%	5.2%
Wheat Futures TR	07/01/59	4.5%	6.8%	-4.6%	7.1%	6.2%	-14.3%	2.4%
Corn Futures TR	07/01/59	3.6%	5.0%	-5.2%	6.0%	2.7%	-17.3%	
Soybeans Futures TR	07/01/59	11.5%	14.0%	3.8%	14.2%	6.9%	-3.9%	
Soybean Oil Futures TR	11/27/62	14.0%	11.4%	32.4%	9.4%	9.5%	37.2%	
Aluminum Futures TR	06/01/87	5.8%	4.3%	1.1%	4.6%	-0.6%	5.6%	-3.8%
Copper Futures TR	07/01/59	16.1%	18.7%	-6.0%	28.8%	2.3%	11.3%	-21.6%
Zinc Futures TR	01/03/77	9.3%	9.6%	-6.4%	11.9%	3.3%	-8.6%	-1.7%
Nickel Futures TR	04/23/79	16.6%	14.8%	-3.4%	14.1%	3.4%	6.9%	-11.2%

Energy Underperforms During late Recession

Grains and Oilseeds do better then other commodities In a late recession



Commodity Cycles Cont

Avg. Monthly Annualized % Returns					Phase Avg.			
Data Series	Starting Date of Data Series	Overall Avg.	Expansion Avg.	Recession Avg.	Late Expansion	Early Expansion	Early Recession	Late Recession
Lead Futures TR	02/01/77	8.4%	9.2%	-16.6%	11.6%	2.6%	-16.0%	-9.7%
Tin Futures TR	07/03/89	2.7%	2.9%	-5.5%	-2.0%	1.5%	-1.3%	-5.1%
Silver Futures TR	11/06/63	7.3%	8.9%	-1.0%	13.9%	-2.0%	-1.1%	-0.2%
Platinum Futures TR	03/05/68	10.7%	14.1%	-11.7%	16.3%	5.0%	-2.5%	-20.2%
Cotton Futures TR	01/05/60	9.9%	13.1%	-4.7%	11.0%	17.3%	-4.6%	-3.0%
Coffee Futures TR	01/03/73	14.6%	12.1%	5.5%	4.9%	22.7%	21.2%	-11.4%
Cocoa Futures TR	07/01/59	9.3%	13.2%	5.9%	8.0%	19.0%	18.6%	-2.5%
Lumber Futures TR	10/02/69	6.5%	9.7%	-12.6%	15.5%	0.0%	-7.0%	-23.6%
Propane Futures TR	09/01/87	25.2%	18.4%	-0.3%	11.1%	7.4%	16.5%	-14.8%
Butter Futures TR	09/05/96	18.0%	6.7%	-14.8%	7.0%	0.0%	9.4%	-9.9%
Milk Futures TR	01/11/96	9.8%	6.4%	-10.4%	3.8%	0.4%	6.3%	-2.7%
Orange Juice Futures TR	02/01/67	10.7%	11.1%	-24.1%	19.6%	12.3%	-22.1%	-2.4%
Rough Rice Futures TR	09/02/86	-0.2%	9.1%	-10.6%	0.2%	0.8%	-7.8%	-6.8%
Soybean Meal Futures TR	07/01/59	14.6%	16.5%	-0.5%	22.4%	7.5%	-13.5%	4.6%
Feeder Cattle Futures TR	11/30/71	9.6%	8.0%	2.6%	11.8%	6.4%	-3.8%	0.4%
Palladium Futures TR	01/03/87	15.6%	14.3%	-1.2%	21.1%	9.8%	-19.2%	-13.3%

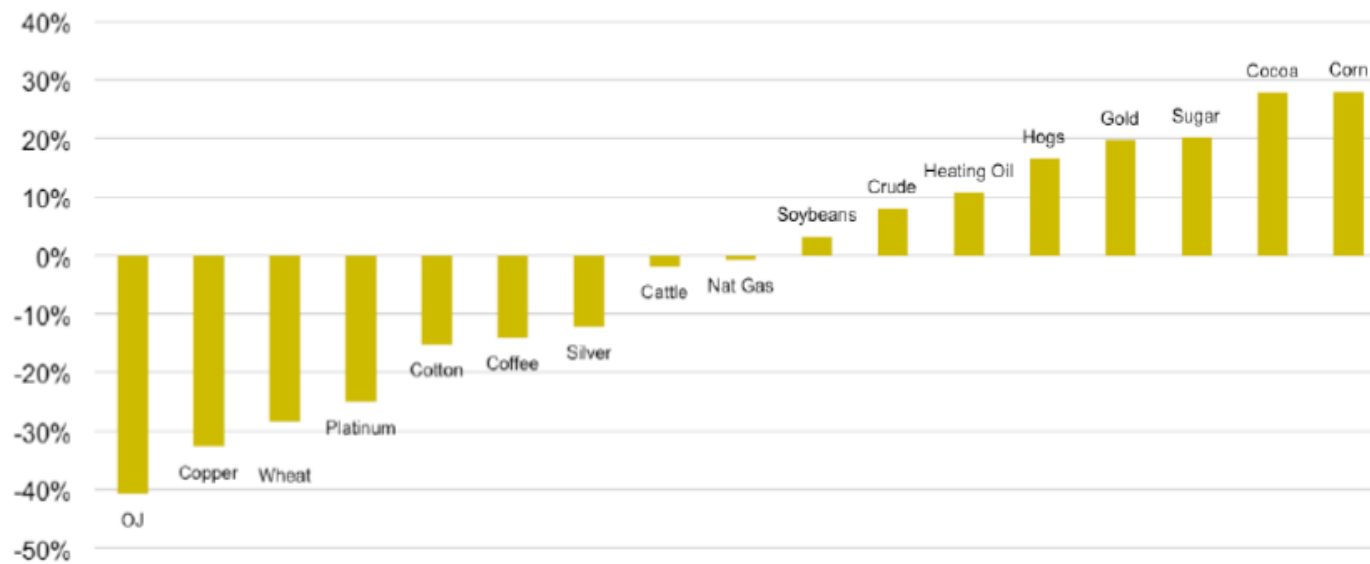
1959 -2004 * Yale Study on Commodities



Commodity Cycles Cont

Not All Commodities Move in Tandem...

Trailing 12 Month Commodity Performance - 10/8/08

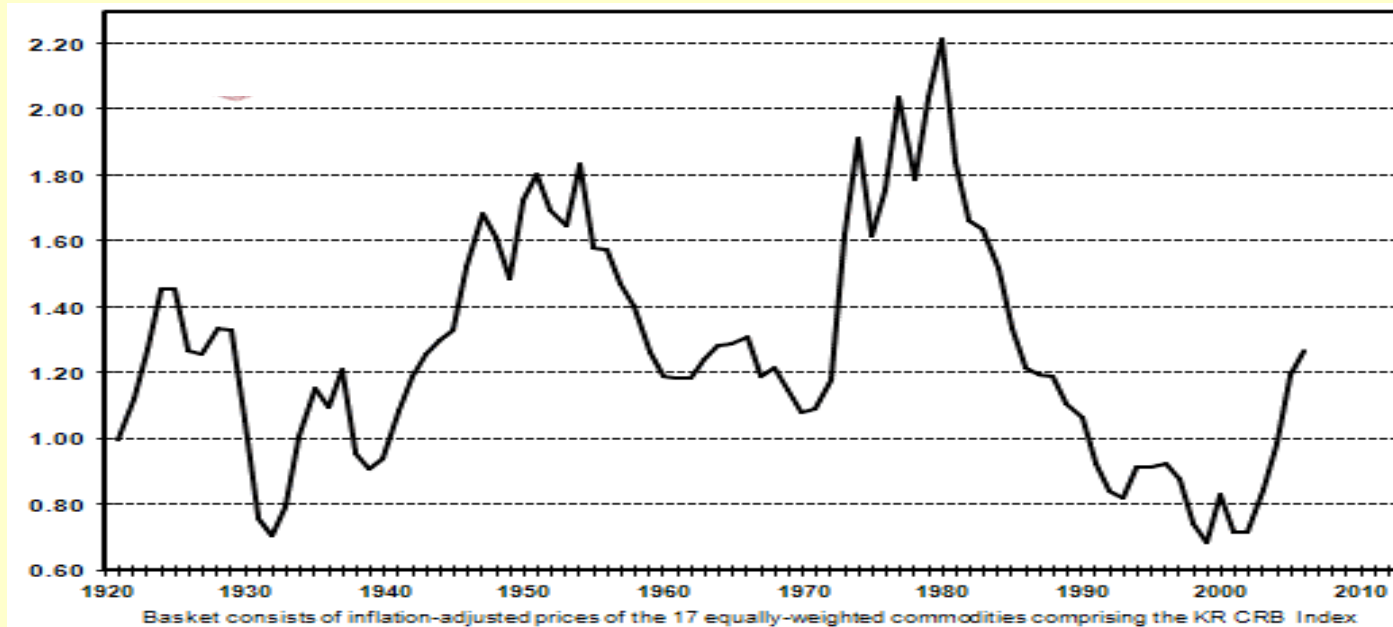




Commodity Cycles Cont

	1999-2003	2004-2007	2008-2009	1999-2009		Down years
Energy	303.45%	71.87%	-61.21%	168.94%		-37.12%
Ags	-26.73%	18.86%	-36.58%	-44.76%		-20.93%
Livestock	9.23%	10.63%	-31.41%	-17.11%		-11.93%
Industrial	45.53%	164.04%	-50.94%	88.51%		-23.09%
Precious	52.01%	98.96%	7.78%	226.00%		2.76%
Energy	303.45%	71.87%	-61.21%	168.94%		-37.12%
Non-Energy	20.01%	73.12%	-27.79%	63.16%		-13.30%

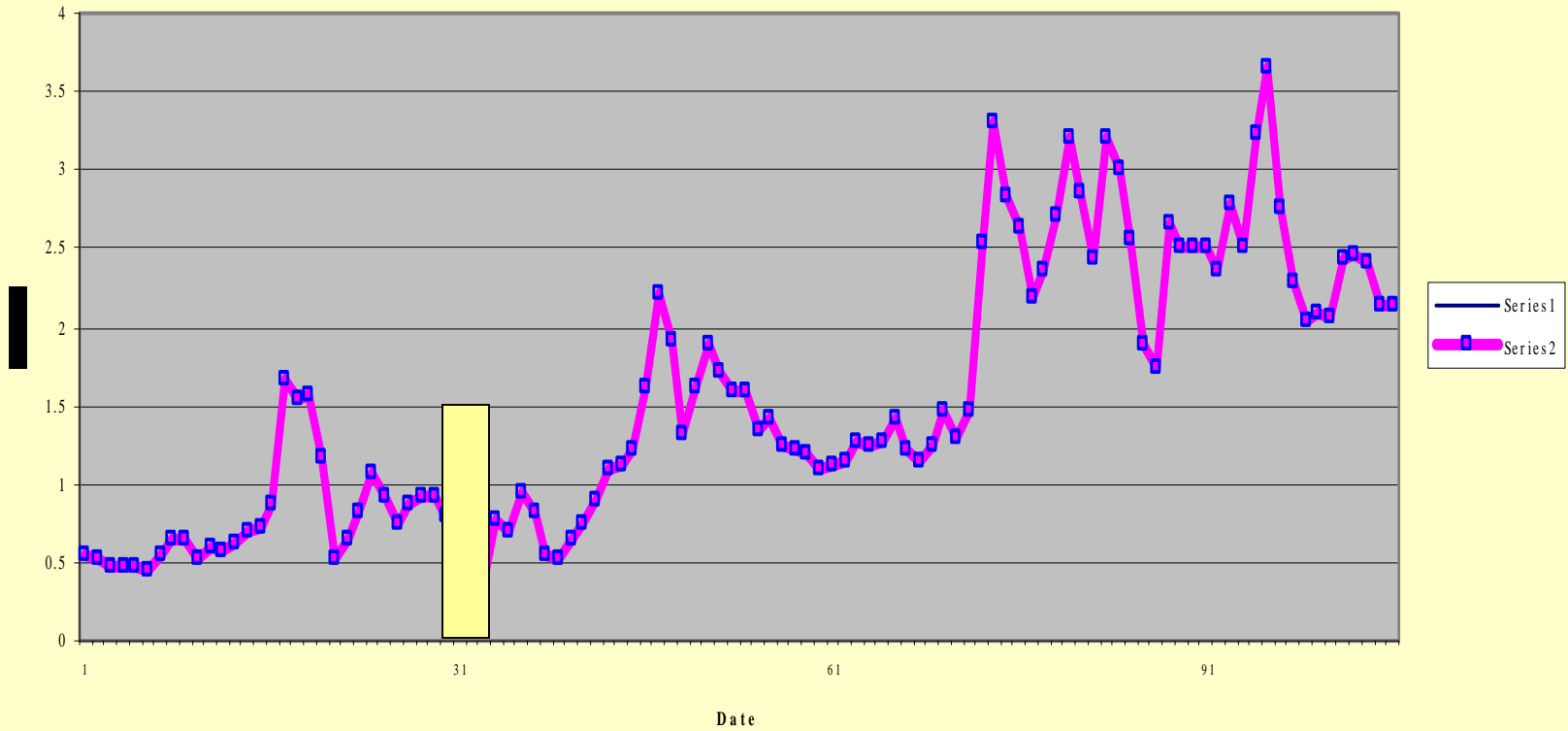
Commodity Prices in Constant Dollars seem Cheap?





Historical Corn Prices 1901-2006

Historical Corn (hlc)

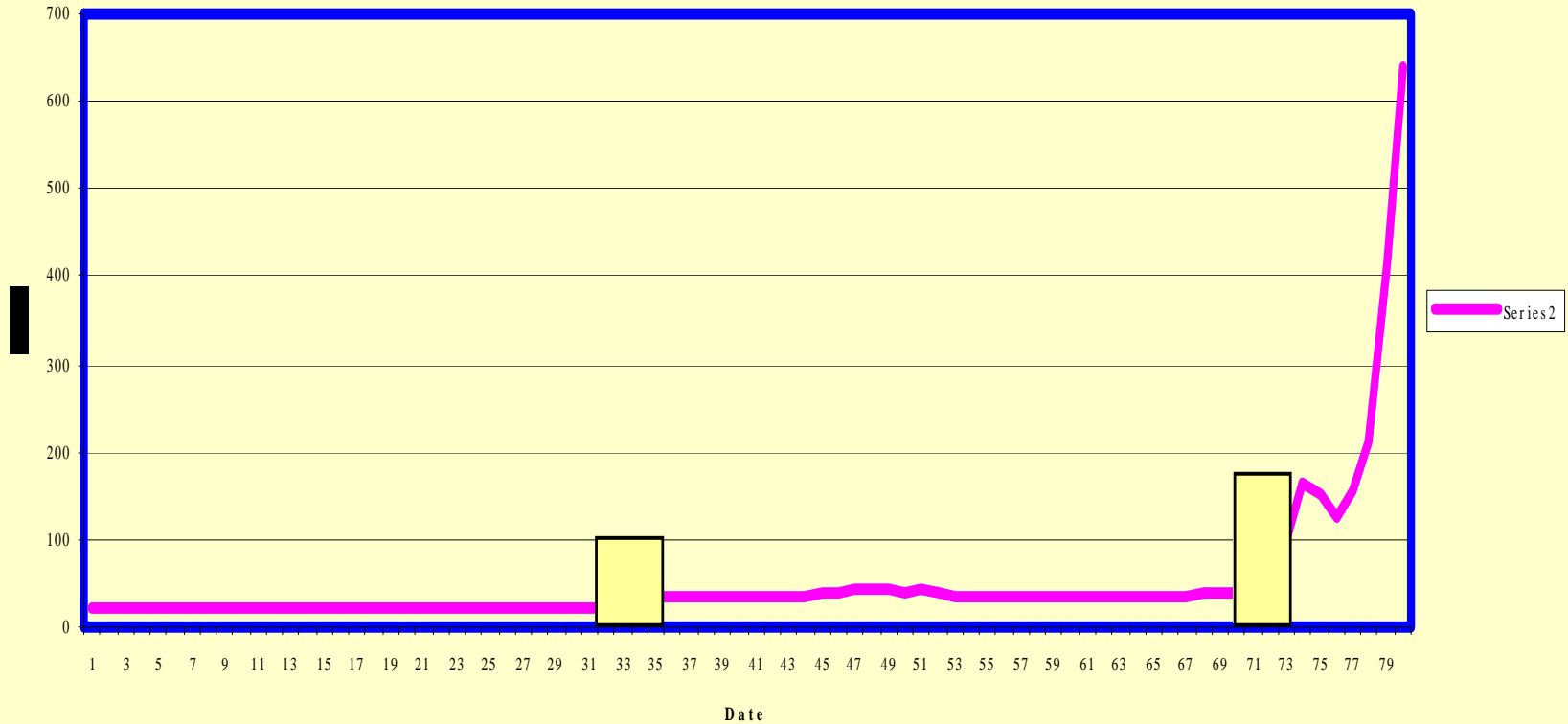




70% devaluation in 1934 Gold went from \$20.67 and ounce to \$35

Gold 1901 -1980

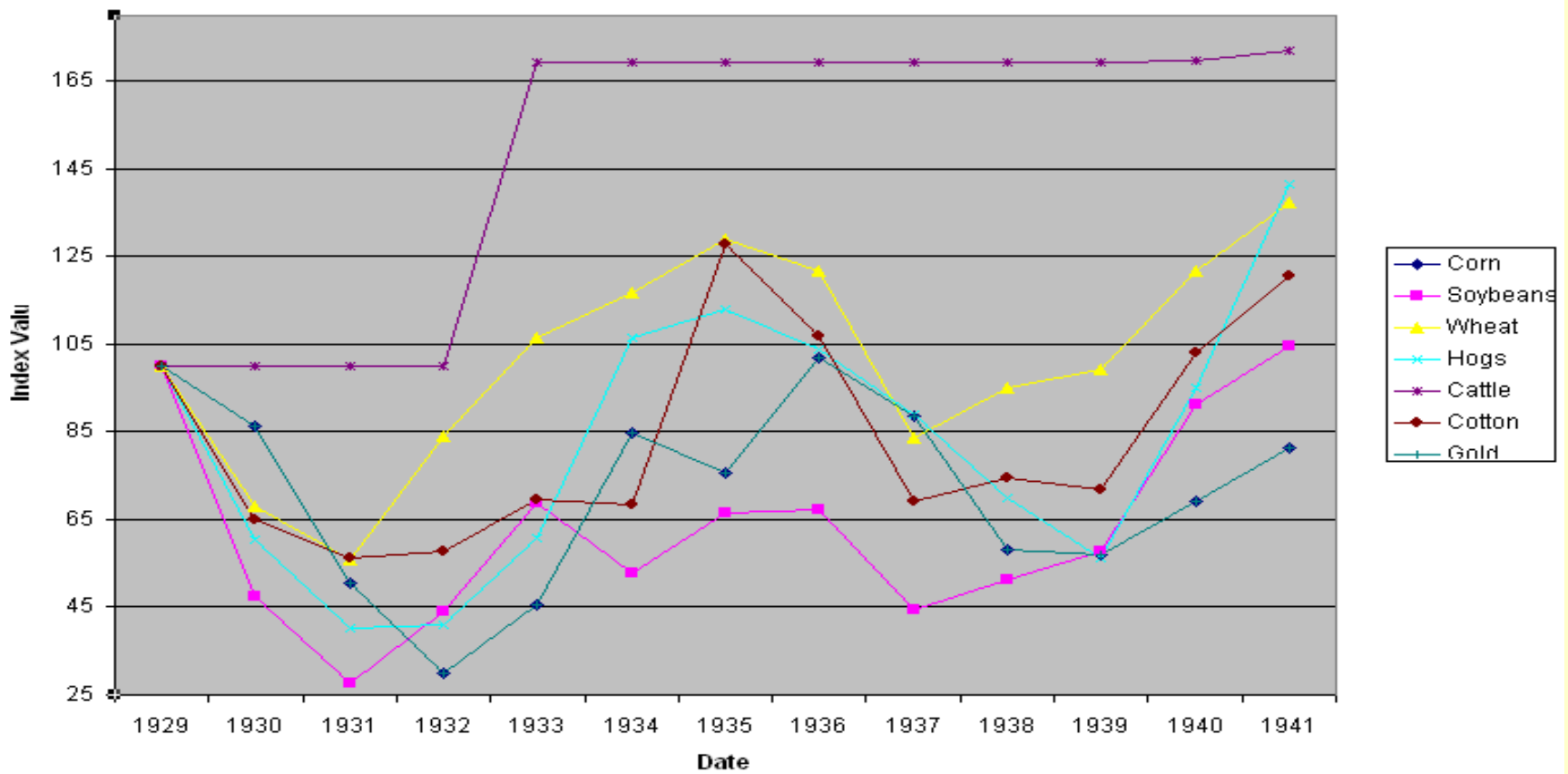
Gold 1901-1980





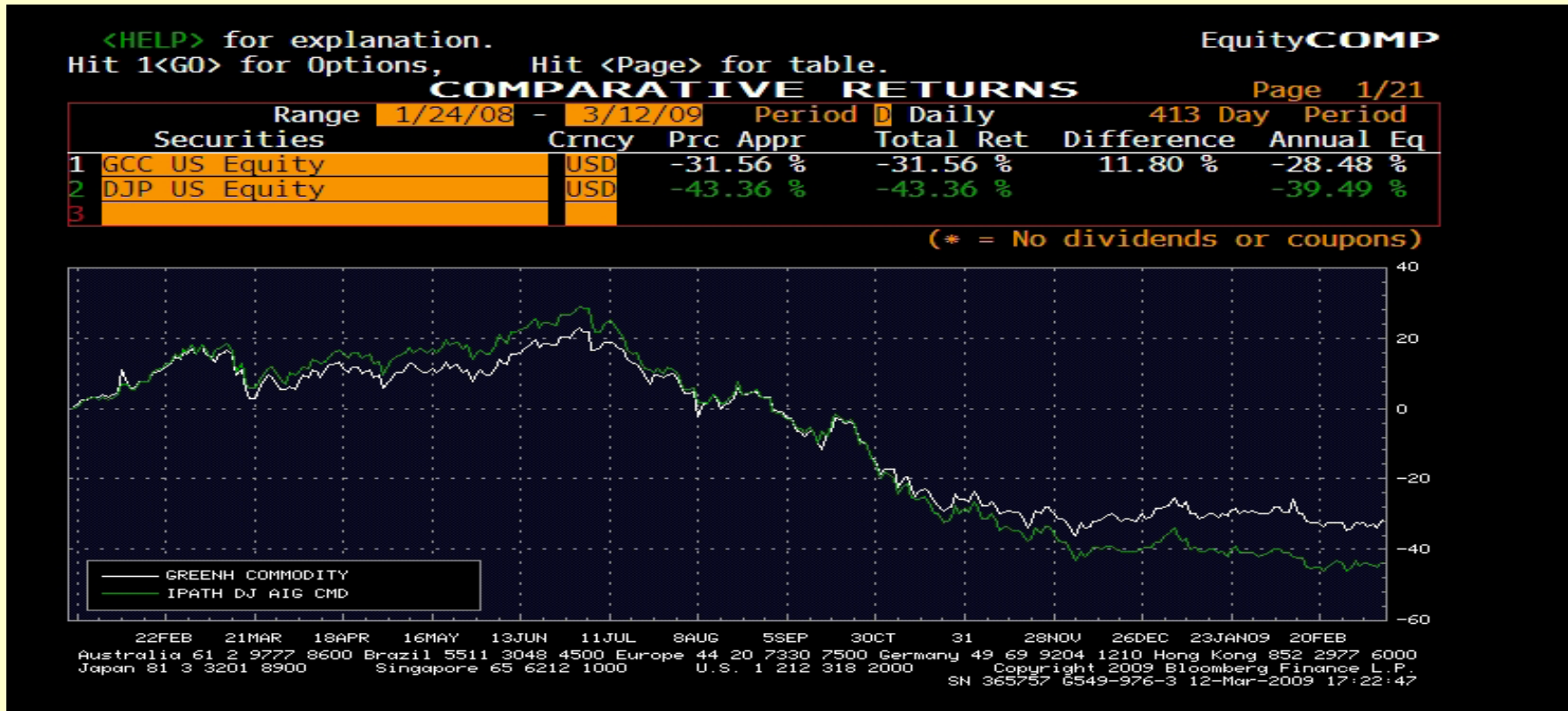
Commodity Cycles Cont

Agri Commodities 1929 - 1941





Funds Move Further Out on the Curve

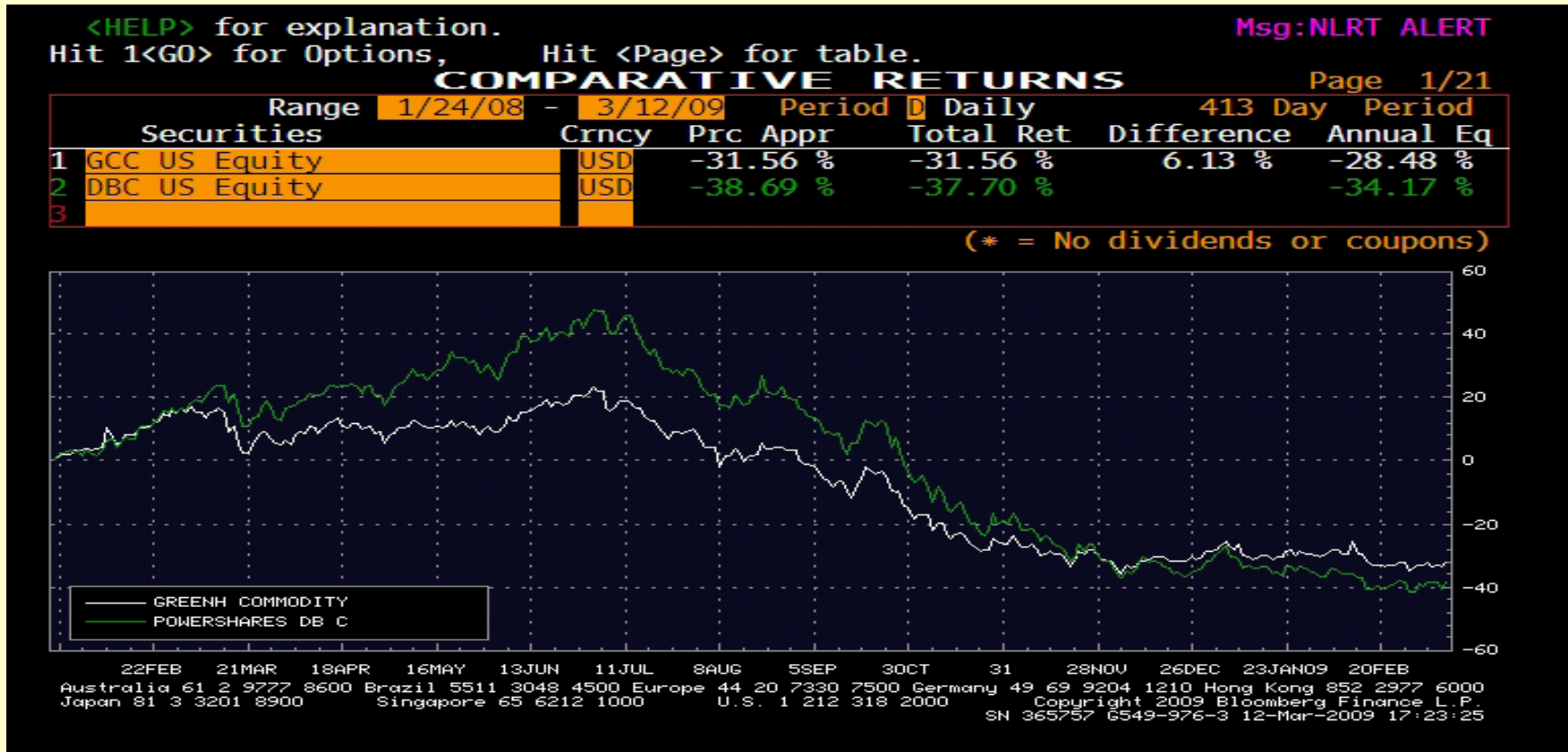


Good News: Wider Carries out further on the curve!

Bad News: More of a chance for inverse moves to the curve



Picking the Curve



All hedgers should understand Who, Where / When, Why and What of the market participants that systematically roll rebalance etc on certain dates.



Owning Physical

- Gold ETF 40 Billion in Physical Gold.
- i.e., Grain Repos Good for Both Parties (Forward Contracts?)
- Could Position Limits force the marketplace into more physical ownership?
- Rep. Collin Peterson (House Ag Committee Chairman) “Commodity Markets Transparency and Accountability Act 2008”- Only Bona Fide Hedgers get Hedger status for position limit exemption.
- Hedge Funds buying Grain Elevators i.e. “White Box”
- Hedge Funds, Institutions Buying other related Agriculture and transportations assets:
 - Bulk Cargo Ships
 - Barges
 - Railcars
 - Farmland



Conclusion

- Best way to own is to own the producing asset. (Because of Carrying Cost)
- Increased appetite for MLPS & REITS.
- Funds move further out on the curve. (Because of Carrying Cost)
- New investors come into commodities everyday.
- New investors and products will and should work with the commercial space (Grain Companies) to share their exposure. What seems like a threat could be a great opportunity for the bottom line of grain companies.
- Watch out for Currency Intervention Price vs. Fundamentals