



Investors and the Ag Markets – Where are They??

NGFA 113th Annual Convention

Eric Kolts



Perspective

**1980's: Bull Market for Bonds as Interest Rates Retreated;
Cash Equivalent Allocations**

**1990's: Revaluation of Future Corporate Earnings Coupled
with IT Revolution Produces Equity Bull Market**

2000-2001: Tech Bubble Burst

Unreasonable Investor Return Expectations

8% Return Expectation for Pensions

**2000-08: Search for Added Return not in Stocks and Bonds:
Alternatives**

Hedge Funds

Private Equity

Timber

Real Estate

Commodities



Commodities as an Asset Class

Demand from Emerging Economies

BRICs, Eastern Europe, Mid East, Asia

**Limited Investment in Infrastructure – Processing, Distribution,
Mining**

Inflation Hedging Characteristics

Short Term Supply/Demand Disconnects (Fundamentals)

**Academic Research Points to Viability of Commodities as a
Portfolio Diversifier**

**Diversification benefits place Commodities into Portfolio
Allocation Models**

**Commodity Indices allow Passive, Systematic exposure to the
asset class**

World's Biggest Floating Plasma??



Shanghai's Bund: Evident of China's Previous Global Role



Made in China

Distribution Facility

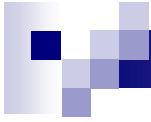


Pharma Manufacturing



Dubai Marina





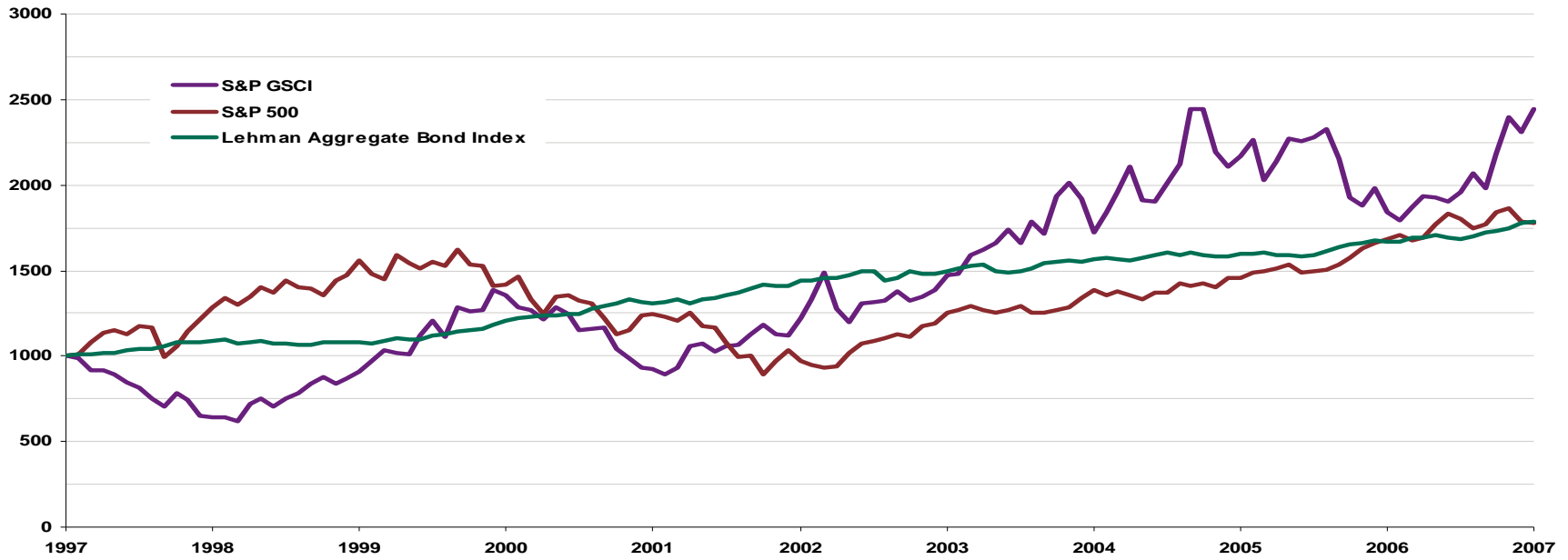
Dubai Palm



The Tallest Building in the World



Monthly 10 year Returns





Methods of Investing

Physical Commodities

Futures / Options

Funds

Mutual Funds

CTA's, Managed Futures

Hedge Funds

Listed: Funds (ETFs), Notes (ETNs), Commodities (ETCs)

Separate Accounts (OTC Swaps, Options)

Structured Products

Retail, HNW, Institutional



Sources of Commodity Index Returns

Collateral Yield: Non leveraged investments produce cash return.
US T-Bills used for Total Return calculations

Risk Premium (Roll Yield): Hedgers expect to pay investors for absorbing future spot price risk. The futures price will be offered at a discount to the *expected spot price*

Unexpected Price Changes: *Realized return* is the *expected return* (collateral + risk premium) +/- *unexpected* changes in spot price



Commodity Index Providers

S&P

DJ-AIG

REUTERS / JEFFERIES

DEUTSCHE BANK

ROGERS

DIAPASON

BARCLAYS

BACHE COMMODITIES

MORNINGSTAR

MERRILL LYNCH

BLOOMBERG / UBS

DEUTSCHE BOERSE

JPMORGAN

BNP PARIBAS



Commodity Indices

Indices differ by:

Components

Roll Scheme

Weighting Methodology

Rebalance Convention

Indices smooth cyclicalities of individual commodity price movements

CME Corn May 2009





COMEX HG Copper May 2009





Commodity Index AUM 2008

S&P GSCI Commodity Index

2007 \$85

2008 \$30+

Dow Jones AIG Commodity Index

2007 \$45

2008 \$15+

Others (DBLCI / RICCI)

2007 \$15+

2008 \$10

Total for Index Investments ~\$55+B (62% Decrease)



Historic AUM Linked to Commodity Indices

S&P GSCI Commodity Index

2000	\$4-6B
2005	\$50
2006	\$60
2007	\$85
2008	\$30

Dow Jones AI Commodity Index

2003	\$500M
2005	\$20B
2006	\$30
2007	\$45
2008	\$15

DBLCI / RIC1 / RJ-CRB / UBS CMCI

2005	\$4-5B
2006	\$10+
2007	\$15+
2008	<u>\$10+</u>

Total for Index Investments **\$55+**



Commodity Index Evolution

Classic commodity indices (long only, front of curve)

DJAIG, SPGSCI, RJCRB, RIC1, DBLCI

2nd generation commodity indices (utilize futures curve)

DBLCI-OY, UBSCMCI, JPMCCI, MLCX

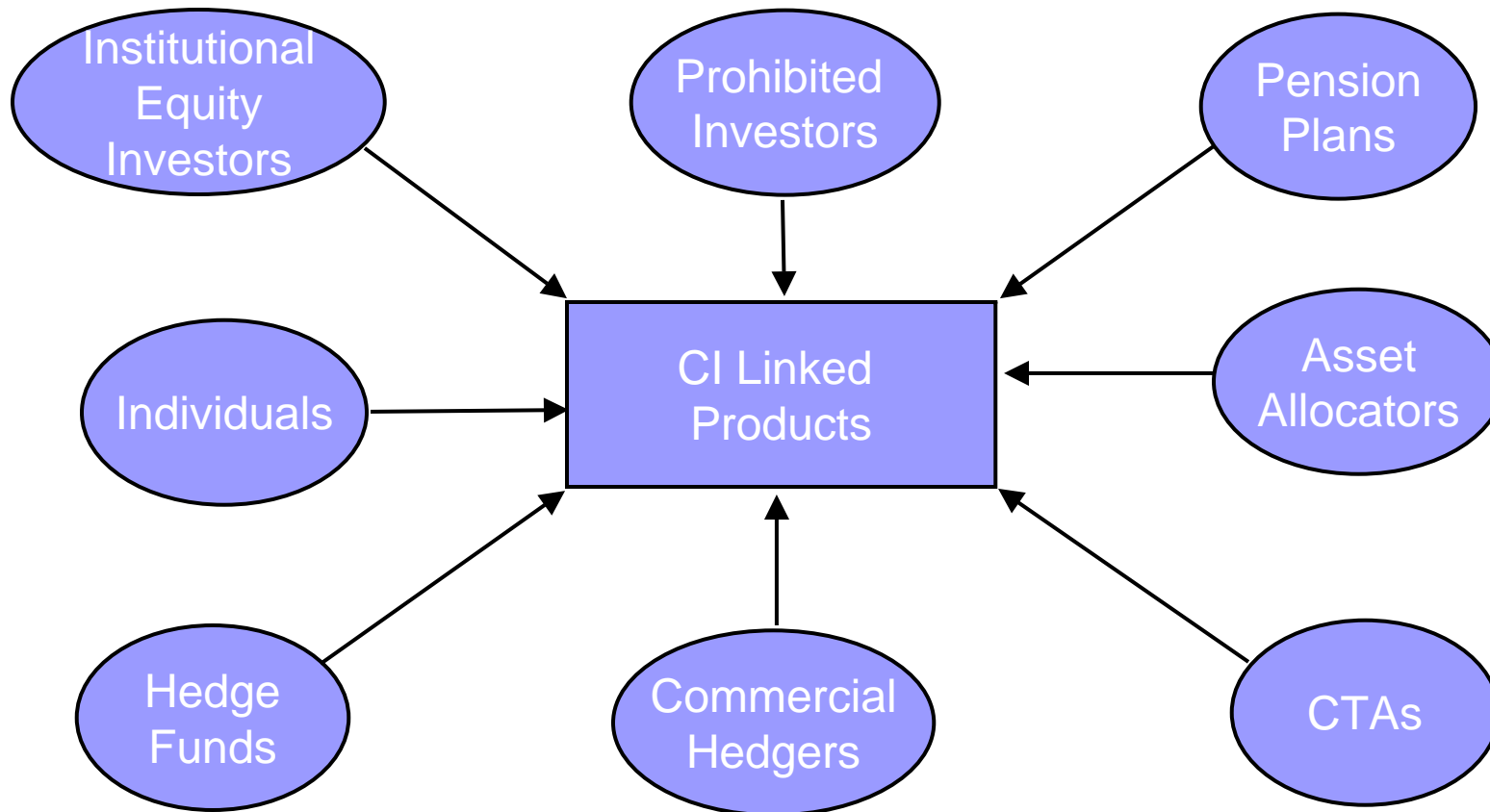
DJAIG & SPGSCI Forwards

Commodity strategy indices

JPM IGAR, UBS Comm-PASS, BarCap CORALS

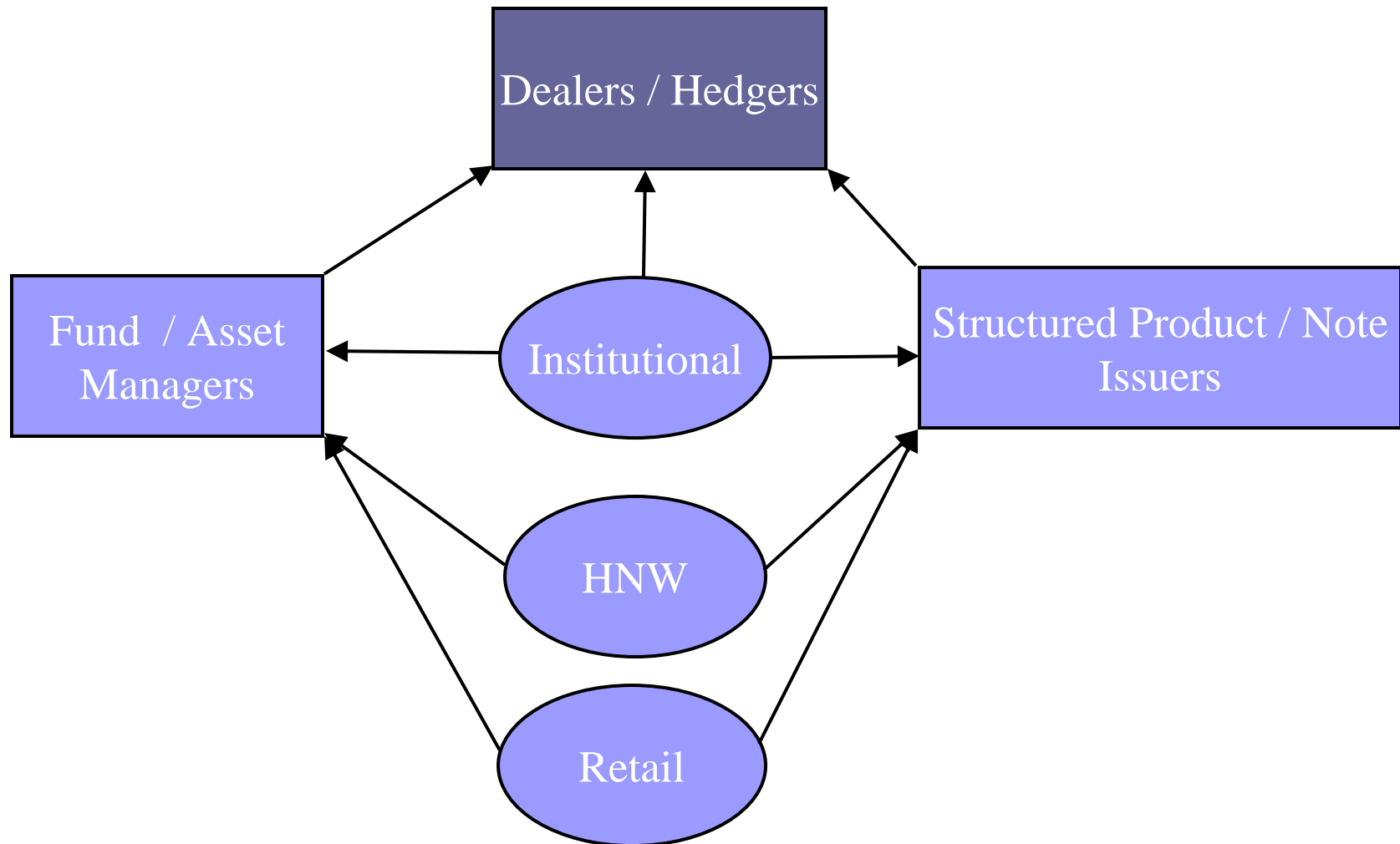
S&P DTI Series

Commodity Index Customer Type



Mutual Funds, Futures, ETFs, ETNs, Structured Products

Commodity Index Customer Model





What Happened Last Year?

2008 ~ Smooth Sailing!!





Ag Investment Drivers for 2008

Population growth, urban expansion

since 1900, population doubled, water usage 6X

Developing countries wealth creation

BRICs, Mid East, Central Europe, LatAm

Small % change means large absolute #s due to population size

Bio-fuel applications (new source of demand)

Rising input costs (energy, fertilizer)

Low inventories

Limited land & water availability per capita

Threats of Nationalization, possibility of inventory building

Food is a major political issue



2008 Unfolds.....

Q1

Strong Institutional Inflows

Thematic Investing continued, 1H08

Development of “newer” markets

Growing popularity of Alpha products (all of '08)

Q2

Dramatically higher prices

Food riots

Protectionism, national actions (export restrictions)

Regulatory uncertainties dominated the headlines

...Getting a Little Rougher.....





Downdraft.....

2H08

Credit freeze in inter-bank money markets

Demand Destruction, particularly in
energy markets

Extreme price moves

High volatility environment

**Massive de-leveraging across all asset
classes**

Help is on the way (!?)...





Now What?

Population growth continues

Limited land & water availability per capita

Threats of Nationalization, possibility of inventory building

Food is a major political issue

Will developing countries economies turn the corner?

OECD countries must recover first

Is consumption recession proof?

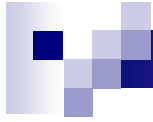
Demand for feedstock & ethanol (gov't subsidies & directives)

Attractive price points?

What effects of trade protectionism, global supply uncertainty?

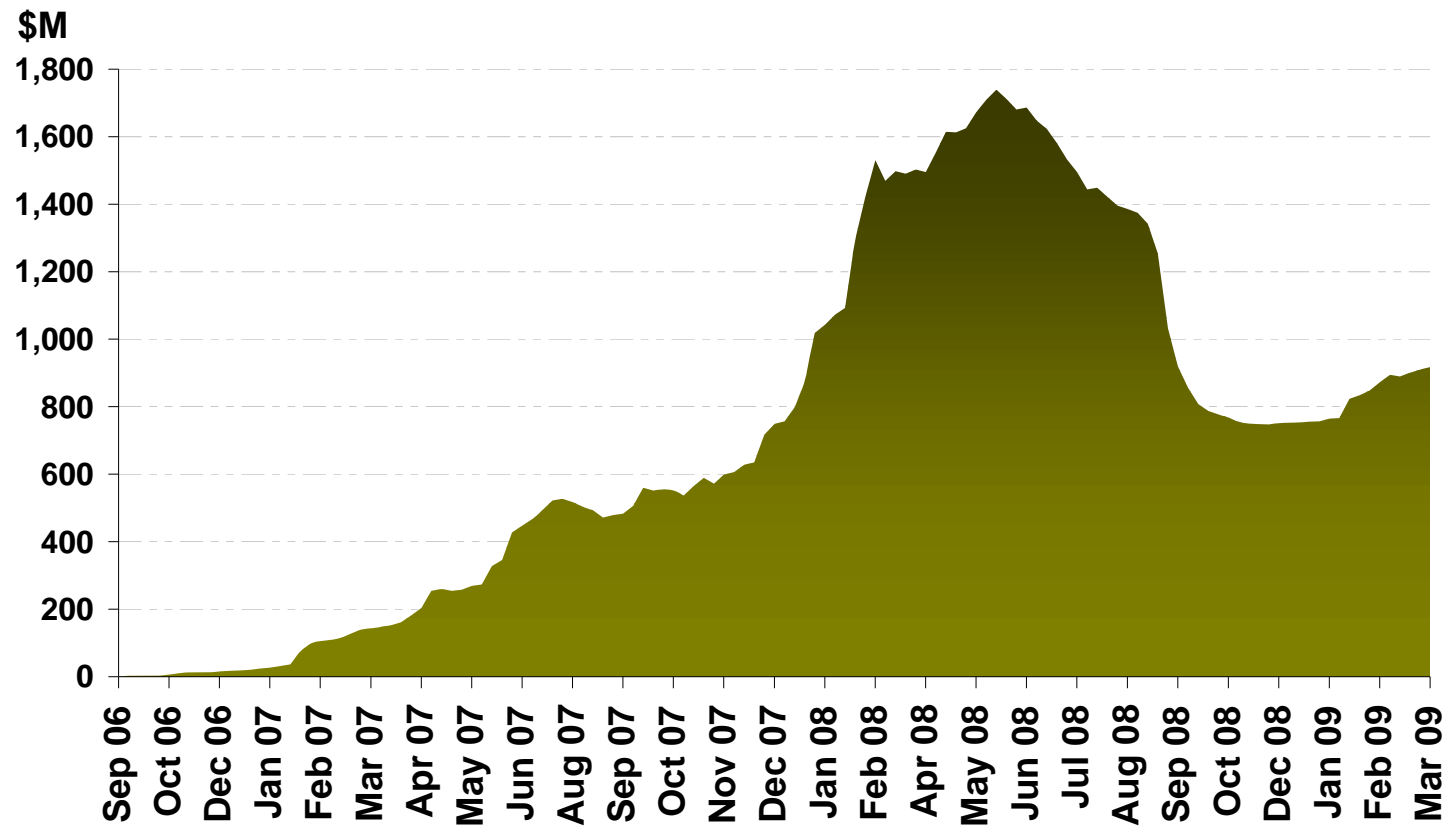
What effects of credit shortage & under-investment in new technology, producer financing constraints

Will input prices rise?



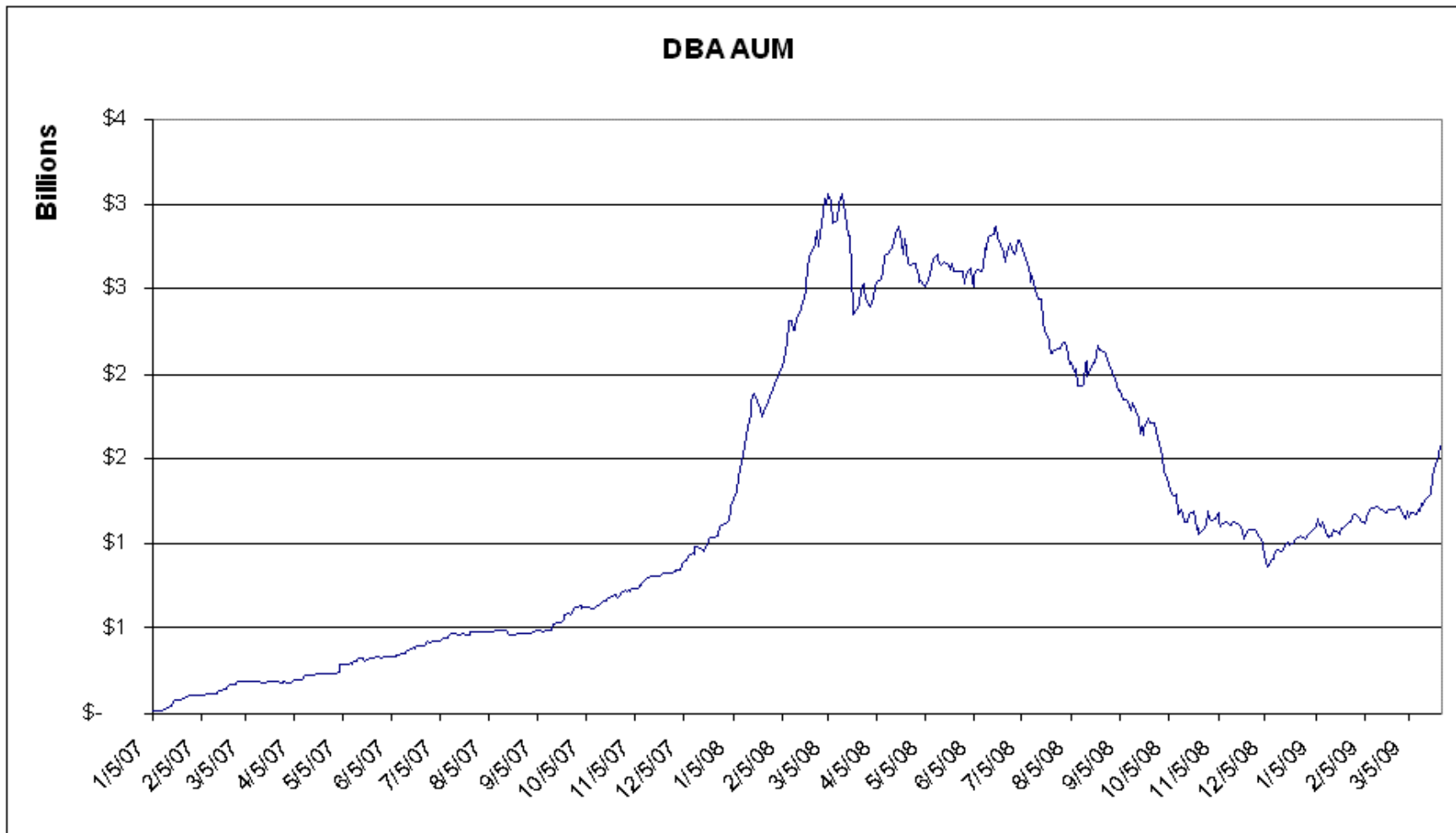
What of Investors?

Strong Rebound of Flows into ETF Securities' Long Agriculture ETCs (Cumulative Flows)

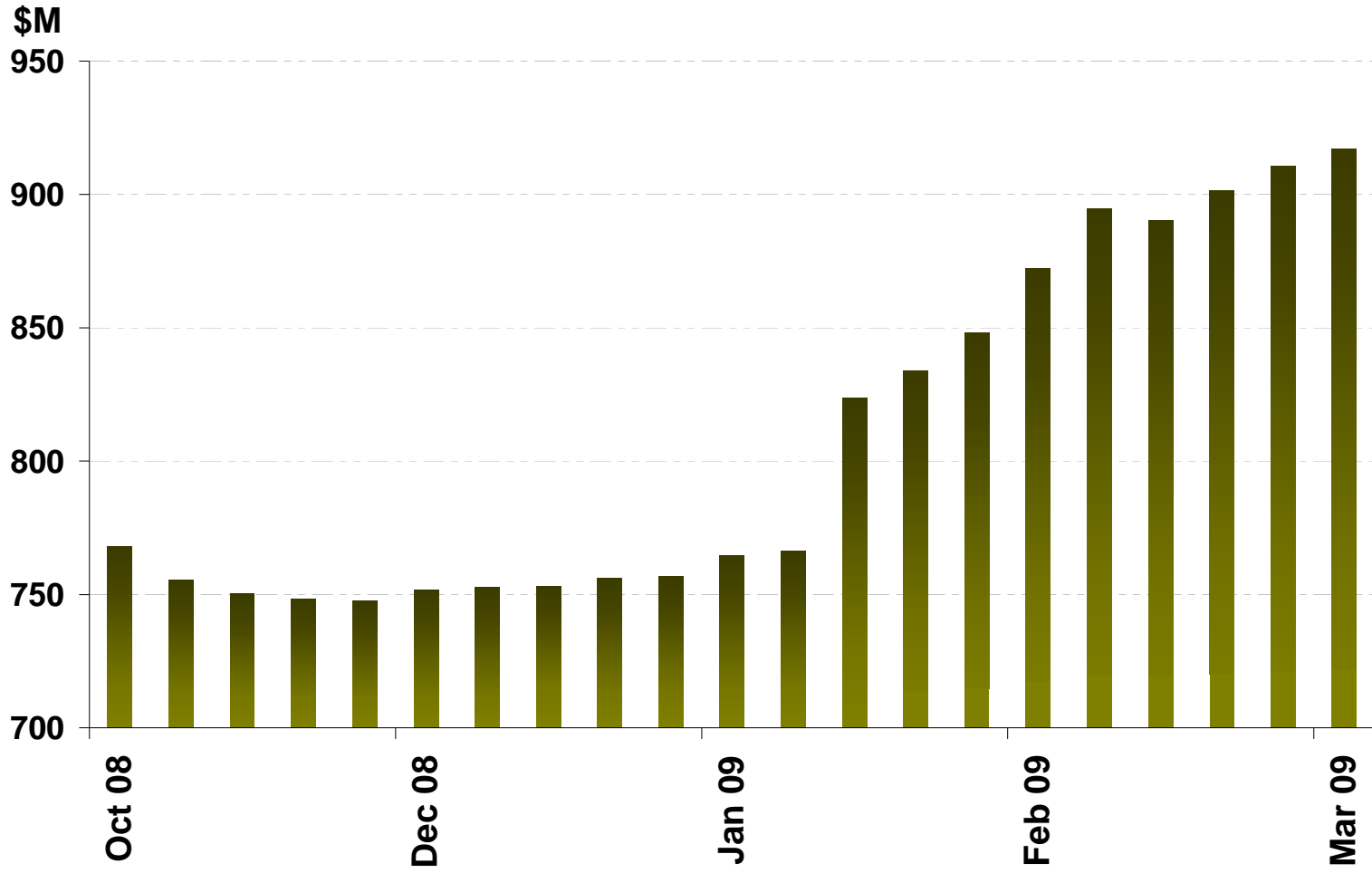


Source: ETF Securities

PowerShares DB Ag Fund



Net Cumulative Flows into Long Agriculture ETCs



Source: ETF



DBA Volumes



The Regulatory Question



© Daniel Forster



Regulatory / Statutory Risks - USA

Senate

The Prevent Excessive Speculation Act (Levin)

Impose speculation limits in Energy & Ag markets

Close “swaps loophole” regulate OTC market

Close “LDN loophole” apply spec limits to foreign exchanges

Allow hedgers to exceed limits

Impose OTC clearing via exchanges

House

The Derivatives Markets Transparency and Accountability Act (Peterson)

Impose spec position limits

Apply to non-US exchange positions as well



Regulatory / Statutory Risks - EUR

Monitor:

Committee of European (EC) Securities Regulators (CESR)

European Regulators' Group for Electricity and Gas (ERGEG)

Market Abuse Directive (Directive 2003/6/EC aka MAD)

Insider dealing and market manipulation

Legally binding disclosure obligations & sanction mechanisms

FSA (UK)

Testimony to Treasury Select Committee re: regulation of oil markets



Crystal Ball...

Commodities are an accepted asset class, though there's still a long way to go

Institutional investors are still in, just lower volumes

Commodity investing is a sensitive issue for some institutional investors

Flows will return upon price increases

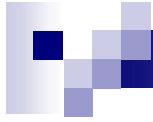
Retail investor flows to exchange traded products

Question of hedge fund involvement

Credit / financing issues

New money will go to index linked (beta) products

Active managers will benefit from legacy investors increased allocations



Thanks!!

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