<u>COMMODITY INDEX INVESTMENT AND US STOCK TRENDS</u>

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In the war movie "The Dirty Dozen" (Robert Aldrich, director), Major John Riesman declares: "I never went in for embroidery, just results."

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<u>OVERVIEW AND CONCLUSION</u>

The CFTC statistics on Index Trader long and short positions for 12 agricultural commodities (CIT Report) offer a snapshot of buy-and-hold "investment" over some version of the long run. From 2007 to the present, the CFTC has provided this information as part of its weekly Commitments of Traders data. Though the CFTC does not provide Index Trader ("IT") data for other marketplaces, many commodity investors desire a diversified portfolio of commodity "assets", often acquiring a package via indices such as the broad S+P Goldman Sachs Commodity Index ("GSCI"). Consequently the IT position levels (futures and options combined) and trends within the IT agriculture sector probably roughly represent the IT situation throughout the entire commodity universe. Keep in mind that within the IT presentation for agriculture, the IT clan is not "commercial" for CFTC purposes. Within the CIT Report, Index Traders also stand outside the "non-commercial" category; many marketplace observers casually label this noncommercial element "speculators".

The net Index Trader position for each of the 12 commodities has always been substantially net long. The net IT position percentage relative to total open interest for the various commodities differs, in some cases substantially: cocoa, corn, cotton, live cattle and wheat net long IT percentages are not the same. In any event, the average net long IT position for the 12 commodities combined from 2007 to the present is about 24.8 percent of total open interest (3/12/13's is about 23.7pc). Thus the commodity buy-and-hold for the long run alternative investment community is a very important factor within the commodity arena.

Moreover, notable changes in the net long IT positions for the combined dozen marketplaces, offer insight into (helps to confirm) overall commodity price trends. A substantial addition over time to net IT positions is a bullish sign for the commodities sector, whereas a significant slash in these net IT positions warns of (or confirms) a bear trip. Of course since net IT positions and their changes are only one factor influencing commodity price level and trend, players should not be dogmatic regarding the role and predictive potential of this marketplace indicator.

Since mid-2008, commodities "in general" (use the broad GSCI as a benchmark) in recent years often have traded in patterns somewhat similar to those in United States stocks (S+P 500). Substantial bull (bear) moves in US equities find parallels in those in the commodity domain. Therefore stock marketplace congregations should monitor IT position levels and trends.

Yet recall 2007-08. American stocks peaked in October 2007, about nine months before the one in commodities. Only after the final stock summit in May 2008 did equities and commodities trade closely together. The current longer run relationship probably also reveals divergence, but with the commodity peak to date arriving well in advance of one in the S+P 500. See "Commodities and US Stocks: Convergence and Divergence" (1/28/03).

The net long IT position since early February 2013 has started to decline, as have prices in the broad GSCI and in the great majority of commodities, although stocks have remained robust. Admittedly IT data availability beginning in 2007 does not constitute an extensive history. One should interpret it in relation to commodity (and especially) stock trends with caution. However, given the frequent parallels of important commodity and stock trends since mid-2008, further notable slumps in the net long IT position alongside price falls in the broad GSCI will warn (help to confirm) that price divergence between the commodities and American stocks will cease. If so, and thus as occurred in spring 2008 and thereafter, stocks and commodities probably will begin to fall together. A boost in net IT positions conversely would be bullish for the S+P 500.

INDEX TRADER LENGTH and S+P 500 TRENDS

The S+P 500 attained its major peak 10/11/07 at 1576. Agricultural Index Trader net length, which had been about 1.29 million contracts on 1/30/07, had climbed to an open interest of about 1.41 million contracts on 10/9/07. Although the S+P 500 began to slump, the net long IT position continued to increase (as did the broad GSCI), reaching its high of 1.78mm on 5/13/08. The broad GSCI plummeted a few weeks thereafter (7/3/08 plateau at 894).

The S+P 500 reached its abyss 3/6/09 at 667, with the broad GSCI major low not long before, on 2/19/09. Many on the buy-and-hold commodities for the long run teams scrambled frantically for the exits after mid-2008. The low in net IT length, about 923 thousand contracts, occurred 3/10/09.

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The net IT total mounted higher, reaching 1.62mm contracts 5/4/10. The broad GSCI peaked at 556 on 5/3/10, a few days after the S+P 500 one at 1220 on 4/26/10. Though the net IT position did not fall much (low 1.45mm contracts 6/8/10), that fall occurred alongside stock and commodity tumbles.

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Over the next several months, the net IT position high of 1.633mm (8/10/10) was around that of 5/4/10. However, this did not coincide with a very important commodity or equity summit. It fell to about 1.41mm on 2/15/11.

But recall what happened after this. The IT net length then edged up to about 1.53mm contracts. Notably, the timing of this elevation approximately matched that of highs in the broad GSCI (762 tops on 4/11/11 and 5/2/11) and a key S+P 500 one (5/2/11 at 1371). In addition, as the IT net longs slashed their positions, commodity and stock prices crashed. The net IT long depth was about 1.30mm contracts on 10/4/11, the same day as the broad GSCI bottom (at 573) and the S+P 500 1075).

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The S+P 500 achieved another interim top on 4/2/12 at 1422, about a month after the broad GSCI’s 717 height of 3/1/12. Note that this GSCI level as well as the subsequent key high on 9/14/12 at 699 remained under the GSCI’s 2011 pinnacles around 762. The high in net IT was about 1.54mm (on 3/27/12 and 4/3/12).

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The S+P 500 established an important low 6/4/12 at 1267, with the GSCI’s a couple of weeks later, 556 on 6/22/12. However, net IT length indeed declined from its 3/27 and 4/3/12 levels to reach 1.47mm on 6/5/12 (also 1.47 on 7/3/12); it kept falling after early July 2012, reaching 1.39mm on 8/14/12 and 9/11/12.

The mid-September IT net length low contrasted with interim tops in the broad GSCI (9/14/12 at 699) and the S+P 500 (also 9/14/12 at 1475). This underlines that one should not be dogmatic about the trend in net IT length and prices in commodities in general or US equities.

Maybe speculators in commodities significantly increased their positions, whereas the IT group did not? In that regard, note that the NYMEX petroleum complex (benchmark crude oil, heating oil, and RBOB; futures and options combined)net noncommercial long position rose from around 247 thousand contracts on 6/26/12 to 413m on 9/18/12.

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In any event, net IT length climbed modestly over the next few months, reaching a high around 1.49mm contracts on 2/5/13 (1.48mm 2/12/13). It has eroded slightly since then to about 1.42mm as of 3/12/13. Although this fall since early February has been modest, note that the February 2013 net IT length remains under the 5/4/10, 4/26/11, and the 3/27-4/3/12 net IT highs, and that these net IT highs also were associated with commodity price tops. In addition, underline the recent interim minor tops around early to mid-February 2013 in numerous individual commodities as well as commodity indices.

Admittedly IT history does not extend back decades, and its correlation with commodity and US equity trends is not perfect. Yet the analysis above is rather suggestive. So assume net IT net length continues to ebb lower and that this widespread commodity price weakness since February 2013 persists. Then from this perspective, despite the S+P 500's magnificent bull run since March 2009 and its recent high on 3/15/13 at 1564, the S+P 500 accordingly becomes increasingly likely to suffer a significant price decline.

FEBRUARY 2013: AN ARMADA OF COMMODITY PRICE TOPS

As part of the major longer run downtrend that exists for commodities in general, note the assortment and timing of minor tops made in early 2013 in several commodity indices and in numerous particular commodity marketplaces.

Commodity or Commodity Index	Date + Level of Recent High in 2013
Broad Goldman Sachs Commodity Index (GSCI)	2/1/13 at 681.5 and 2/13/13 at 681.7
Dow Jones- UBS Commodity Index	2/1 at 143.7
Goldman Sachs US Agriculture Spot Index	2/1 at 469.7
Gold	1/17/13 at 1698, collapse from 2/17/13 at 1682 (though has edged up since 2/21's 1555)
Silver	1/22/13 at 3248, then 2/11 at 3153 (3/1 low at 2796)
LMEX (London Metal Exchange base metals index)	2/4/13 at 3614
Steel (LME, three month forward)	2/20 at 310
Iron Ore (delivered to Qingdao, China)	2/20 160.8
Coal (ARA/Northwest Europe, delivered)	2/11 at 91.25
Coal (US, Appalachian, NYMEX nearest futures)	2/21 at 60.48
Rubber (Tocom, in Yen terms)	2/6 at 314.2

Brent/North Sea (ICE, nearest futures continuation)	2/8/13 at 119.17
NYMEX crude oil (first futures)	1/30 at 98.24 and 2/13 at 98.11
OPEC crude oil basket	2/13 at 114.94
US Gulf Coast regular gasoline	2/15 at 3.14
USGC diesel (ultralow sulfur)	2/12 at 3.29
USGC high-sulfur (3.0pc) residual fuel	2/8 at 101.38

NYMEX natural gas (nearest futures continuation) represents an exception to these February 2013 commodity tops, rallying sharply from lows on 1/2/13 at 3.050 and 2/15/13 at 3.125.

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One should supplement this overview of US stocks, commodities, and Index Traders with actions by the Federal Reserve Board (and other central banks), the US fiscal situation and Treasury (and other US and international) interest rate trends (recent high of the UST 10 year on 3/8/13 at 2.09 percent.), currency (particularly US dollar) levels and fluctuations, outlooks regarding the reemergence of the European (worldwide) economic crisis (not just Cyprus), and so forth.

Anyway, underscore three additional February 2013 data points in regard to the February 2013 timing in commodities "in general", Index Trader statistics, and the S+P 500. The Euro FX peaked against the US dollar 2/1/13 at 1.3711. Gurus underline the importance of the China economic growth story to bull moves in much of the commodity complex. China's stock marketplace is not a perfect proxy for overall Chinese economic growth. However, it should not be overlooked. The Shanghai Composite's recent minor high was 2/18/13 at about 2445; note the timing of the minor low in the renminbi, 2/20/13 at 6.249. The recent peak in the NYMEX petroleum complex net noncommercial long position was about 445m contracts on 2/12/13 (a very elevated 14.3 percent of total open interest; the pc of total open interest on 2/5/13 was nearly 14.4pc). As of 3/12/13, net noncommercial longs at NYMEX had fallen to about 357m (around 11.4pc of total open interest).

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