Bloomberg

Hedge Funds Raise Bullish Bets on Commodities

By Debarati Roy - Jan 3, 2012

Speculators increased wagers (.MMLOSH) on rising commodity prices by the most since August 2010 on signs that sustained economic growth will drive a rebound in raw materials from their first annual slump since the recession.

Hedge funds and other money managers increased combined net-long positions across 18 U.S. futures and options by 18 percent to 536,907 contracts in the week ended Dec. 27, Commodity Futures Trading Commission data show. Soybean holdings jumped more than ninefold and those for corn reached a five-week high. Speculators trimmed bets on declining prices for copper, cocoa, wheat, and soybean oil and meal.

While the Standard & Poor's GSCI Total Return Index of 24 commodities declined 1.2 percent last year, it rallied 12 percent from a 10-month low reached in October on mounting optimism about growth. Confidence among American consumers rose in December to the highest level in eight months and pending sales of existing homes jumped in November for a second month. More than $3.3 trillion was added to the value of global equities since Oct. 4, data (WCAUWRLD) compiled by Bloomberg show.

"The U.S. is certainly putting the floor on commodities," said James Paulsen, the chief investment strategist at Minneapolis-based Wells Capital Management, which oversees about $330 billion of assets. "Data out of the U.S. flies in the face of recession. More and more people are saying: 'Maybe things are not that bad.'"

Quarterly Rally

The S&P GSCI Total Return Index rose 9 percent last quarter, snapping two consecutive three-month drops. The MSCI All-Country World Index of equities rose 6.7 percent, the most in a year. The U.S. Dollar Index (DXY), a measure against six trading partners, gained 2.1 percent, the second straight quarterly advance, while the yield on 10-year Treasuries slid 2.1 percent, Bloomberg Bond Trader prices show.

Twelve of the 24 raw materials tracked by the S&P GSCI rose last week. Gains were led by wheat traded in Kansas City, which surged 6.2 percent. Cotton climbed 5.2 percent. Silver, cocoa, oil in New York and heating oil rose at least 2 percent today.

On a total return basis, commodities lost 1.2 percent last year, the first annual drop since 2008, as Europe's debt crisis escalated and China's economic growth cooled. Money managers have cut bets on higher prices by 65 percent since this year's high in April. More than $10 trillion has been wiped off the value of global equity markets since May 1 as markets were roiled by concern that the world would tumble into recession.

Precious Metals

Investors withdrew $936 million from commodity funds in the week ended Dec. 28, according to data from EPFR Global, which tracks investment flows. Gold and precious-metals outflows accounted for $688 million, while $248 million was withdrawn from other commodities, said Cameron Brandt, the director of research at the Cambridge, Massachusetts-based research company. Inflows totaled $12.8 billion last year, of which $8.1 billion was into bullion (.GLDTONS), EPFR said.

"We have seen people reducing risks, and the future of commodities largely depends on whether Europe and U.S. can avoid a recession," said Nic Johnson, who helps manage $30 billion in commodity assets at Pacific Investment Management Co. in Newport Beach, California.

Commodities plunged 46 percent in 2008 as the collapse of Lehman Brothers Holdings Inc. triggered the worst global recession since World War II. Prices rebounded 13 percent in 2009 and 9 percent in 2010 as governments around the world flooded markets with money to shore up growth.

'Finding a Bottom'

"News from Europe continues to remain depressing, while U.S. economic reports are getting better and better, and people think we will find the bottom for most of the commodities soon," said Michael Smith, the president of T&K Futures and Options in Port St. Lucie, Florida.

The U.S. expanded at a rate of 1.8 percent this year and will probably grow 2.1 percent in 2012, according to the median of 70 economist estimates compiled by Bloomberg. Fewer Americans filed applications for jobless benefits in the four weeks through Dec. 24 than at any time since June 2008, according to figures from the Labor Department on Dec. 29.

Goldman Sachs Group Inc. said in a Dec. 1 report that the world probably will avoid a recession and maintained its "overweight" allocation to commodities, predicting a 15 percent return in the next 12 months. A close balance between supply and demand across raw materials "could drive a strong price rebound in early 2012," Barclays Capital said last month.

Farm Bets

A measure (.AGLOSH) of 11 U.S. farm goods showed speculators increased bullish bets in agricultural commodities by 35 percent to 273,677 contracts. That's the biggest gain since July 2010.

Soybean wagers surged to 23,683 from 2,575 a week earlier, the CFTC data show. Prices jumped 6.8 percent in December, the biggest monthly gain since August. Corn holdings (.MMCANET) climbed 18 percent to 148,653 contracts, the highest since Nov. 22.

Lower-than-average humidity and dry soil will curb crop development in Argentina and southern Brazil through at least Jan. 7, according to T-Storm Weather LLC, a forecaster in Chicago. Nineteen of 25 traders surveyed by Bloomberg expect corn to advance this week.

A La Nina weather pattern is similar to the 2008-2009 growing season, according to T-Storm. In that period, there was at least a 30 percent plunge in Argentina's grain and oilseed production, a 13 percent decline in Brazil's corn output. The La Nina phenomenon typically brings heavier rainfall in Asia and drier weather in South America.

"The headlines out of Europe have not gotten any worse, and the U.S. economy is improving, so in general the story for commodities can only get better," John Stephenson, who helps manage $2.6 billion at First Asset Management Inc. in Toronto, said in a telephone interview.

To contact the reporter on this story: Debarati Roy in New York at droy5@bloomberg.net

To contact the editor responsible for this story: Steve Stroth at sstroth@bloomberg.net