

Commodity returns flat in June

Energy and metals support total commodity returns in June

On aggregate, commodity returns were flat in June, with the energy and metals sectors delivering a positive performance while precious metals and agricultural commodities posted losses. Overall, the MLCX TR index was flat at 0.01% for June, while the DJ-UBS TR index posted -1.90% and the S&P GSCI TR advanced 0.57%. Equities also experienced a flat month, with S&P 500 TR index at 0.20%, while the ML US Broad Bond index returned 0.61% in June.

How much money is tracking commodity index investments?

Following substantial withdrawals in 2H2008, investor money is starting to flow back into commodity indices on the back of rising prices and an incipient recovery in risk appetite. Our estimates put the total amount of money currently invested in commodity indices at about \$125bn, up from a trough of \$80bn in February.

Energy sector posts another positive month led by oil

In June, crude oil prices levelled out around \$70/bbl following the rally in May. Oil products also gained, leaving US nat gas as the only MLCX energy component in negative territory for June. In total, the MLCX Energy TR index returned 3.34%.

Industrial metals post gains, precious metals negative

Among the industrial metals, aluminium and nickel saw significant spot price increases over the month. The MLCX Industrial Metals TR index posted 5.31%, making it the best-performing sector in June. Meanwhile, the MLCX Precious Metals TR index fell -6.59% on the back of falling silver and gold prices.

Agricultural commodity prices decline in June

The agricultural sector saw sharp price drops in a number of commodities. The MLCX Grains TR index posted -16.20% in June on the back of severe drops in corn and wheat. The MLCX Softs TR index also declined -1.86% due to falling coffee and cotton, while the MLCX Livestock TR index was down merely -0.98%.

Table 1: Performance of main commodity indices and MLCX sub-indices

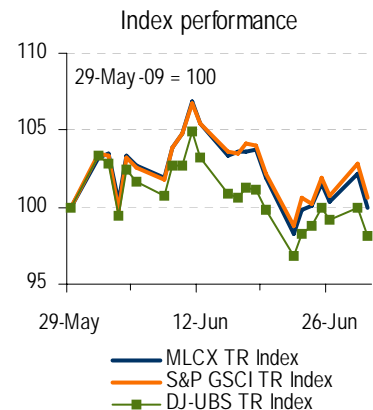
	Value on 30-Jun-09	Jun	YTD	YoY
MLCX TR	786.7889	0.01%	14.30%	-51.67%
S&P GSCI TR	4257.237	0.57%	6.55%	-59.68%
DJ-UBS (DJ-AIG) TR	245.722	-1.90%	4.62%	-47.08%
MLCX Energy TR	1204.4548	3.34%	18.59%	-60.66%
MLCX Ind Metals TR	295.8216	5.31%	33.46%	-40.60%
MLCX Prec Metals TR	268.4450	-6.59%	6.42%	-4.22%
MLCX Grains TR	83.3120	-16.20%	-11.80%	-47.05%
MLCX Livestock TR	241.1228	-0.98%	-12.19%	-30.31%
MLCX Softs TR	240.4990	-1.86%	19.23%	-6.23%

Source: Bloomberg, Banc of America Securities-Merrill Lynch

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Chart 1: Commodity index returns were flat overall for the month of June



Source: Bloomberg, Banc of America Securities-Merrill Lynch

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Refer to important disclosures on page 17 to 18.

How much money is tracking commodity index investments?

Historically, rising commodity prices have attracted flows

We argued in a recent publication that more speculation would benefit commodity markets by reducing inefficiencies found in commodity options and timespread prices ([Commodity Derivatives Insight, Jun 17th](#)). We also found statistical evidence that passive investor inflows into commodity markets tend to follow prices rather than the other way around. This evidence is consistent with the investor inflows into the commodity markets observed in recent months. With commodity prices bottoming out early in the year and steadily creeping higher, investors are starting to dip their toes again into the market.

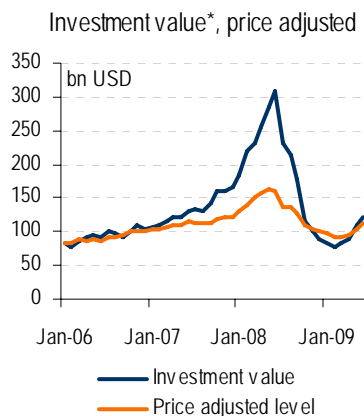
Still, index investment values are at mid-2007 levels

Our estimates put the total amount of money currently invested in commodity indices at about \$125bn or a level similar to that observed in mid 2007, down from a peak of \$300bn but up from a trough of \$80bn in February of this year. It is important to note that, while there has been some money inflow in 2009, much of the recent recovery value is due to a rebound in commodity prices (Chart 2).

Commodity investor flows into indices starting to pick up

Commodity futures are traded (1) for commercial hedging purposes, (2) by investors seeking to hedge inflation risks in their portfolios, and (3) by speculators willing to take on risk. Passive, rules-based commodity indices such as the S&P GSCI or the DJ-UBS are typically used by investors seeking to hedge inflation risks. Is there a way to estimate how much money is currently tracking commodity index investments? While no central registration exists, the U.S. Commodity Futures Trading Commission (CFTC) requires index traders to report their positions separately for certain agricultural commodities. These CFTC reports can be used to estimate total index investment into commodity markets under certain assumptions. We assume most of the index money invested has a composition similar to either the S&P GSCI or DJ-UBS index. We then derive the total amount invested from the agricultural index components (Chart 3). Of course, there are several moving parts here: spot price movements, roll returns resulting from the cost of carry, and actual money flowing in and out of indices. By accounting for spot price movements and roll returns, we can attribute the remainder to money flows (Chart 4).

Chart 2: Index investments have moved more due to price movements than money flow

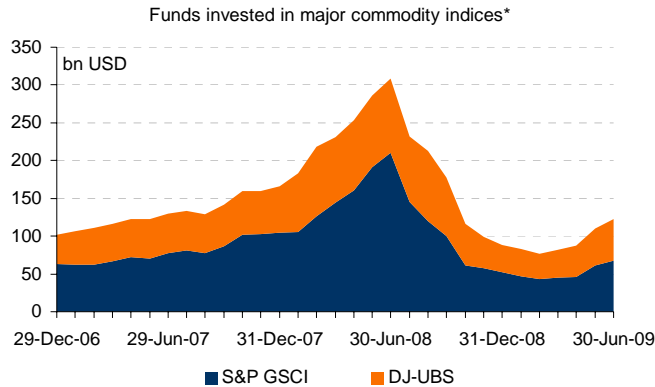


Source: CFTC, Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

* BAS-ML estimate of index investment level based on CFTC data

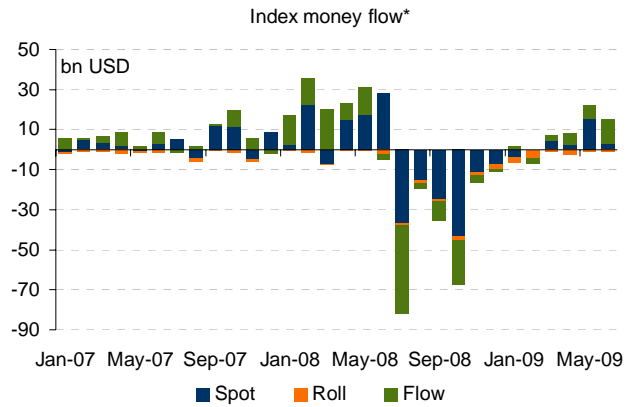
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Chart 3: Total index investments can be estimated from CFTC reported index positions in agricultural commodities



Source: CFTC, Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research
* BAS-ML estimate of index investment level based on CFTC data

Chart 4: We estimate money flow by calculating differences in investment levels, adjusted for spot price movements and roll returns



Source: CFTC, Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research
* BAS-ML estimate of index money flow, based on CFTC data, using S&P GSCI and DJ-UBS spot and roll return

Exchange traded products, funds are reflected in indices

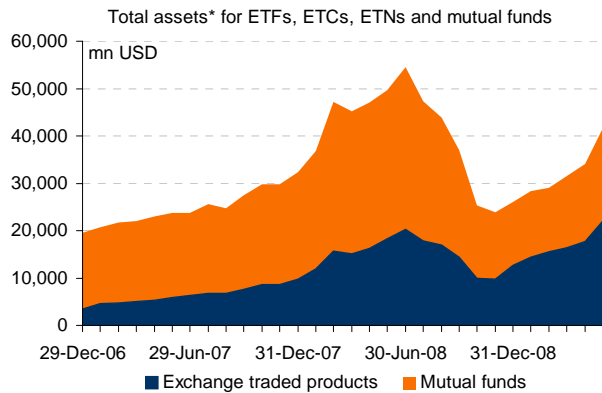
Other methods to gain passive commodity exposure include buying exchange traded funds (ETFs), commodities (ETCs) or notes (ETNs). These instruments have characteristics generally similar to that of a passive index. In addition, a number of asset managers offer exposure to commodities through actively managed mutual funds that try to outperform a major commodity index. Broadly speaking, we estimate the exchange traded products and mutual funds experienced lesser and later withdrawals in 2008, even in relative terms. We estimate investments at their peak hit a combined value of \$55bn, and they currently stand at a value of approximately \$40bn (Chart 5). Of course, these vehicles are typically either explicitly or in practice a form of commodity index and the hedges behind them will generally be reported to the CFTC as index investments. Thus, they generally form part of, rather than add to, the investments illustrated in Chart 3.

We have excluded physically-backed funds from the sample

Still, it is important to differentiate between those investor products backed by commodity futures, e.g. the US Oil Fund, and those backed by physical quantities of the underlying commodity, as the SPDR Gold Trust. Physically backed funds can account for large investment values, as is the case of the SPDR Gold Trust with \$35 billion total assets. However, these instruments do not translate into positions in commodity futures and we have excluded them from the sample below. Total assets under management for both exchange traded products and mutual funds are publicly reported and can be aggregated (Chart 5). Again, as these levels incorporate spot price movements, by accounting for price changes we can construct an estimate of money inflows into these investment vehicles (Chart 6). As is the case with passive commodity index investments, inflows into commodity products have been positive in the last few months.

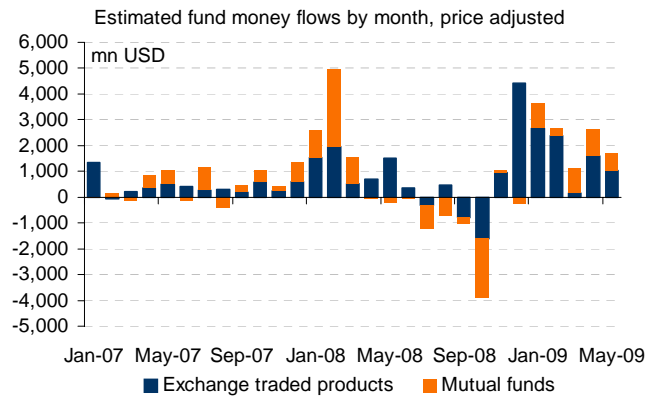
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Chart 5: Exchange traded products backed by futures continue to attract investor interest...



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research
* In our estimates we include 222 ETFs/ETNs/ETCs (excl physically backed ETFs) and 60 funds.

Chart 6: ...and have seen money inflow for most months, experiencing only limited redemptions in 2H2008



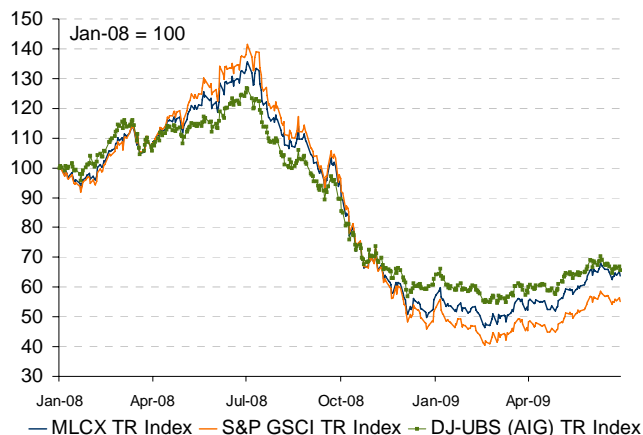
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

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Commodities Portfolio

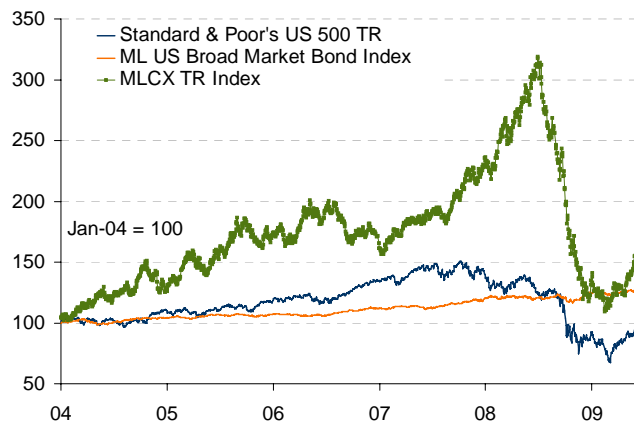
The Merrill Lynch Commodity index eXtra

Chart 7: Total Return Commodity Indices performance



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 8: Commodities and other asset classes performance



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Table 2: Total Return Commodity Indices performance

Benchmark	S&P GSCI	DJ-UBS
MLCX alpha* relative to benchmark	5.73%	3.71%
MLCX beta* relative to benchmark	0.90	1.21
MLCX correlation with benchmark	99.10%	94.74%
Average tracking error**	4.92%	11.77%

Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Based on performance from 31-Dec-2007 to 30-Jun-2009

* Alpha and beta coefficients are annualised intercept and slope coefficients of a linear regression of MLCX TR daily log-returns on the benchmark's daily log-returns.

** Average tracking error is the annualised residual standard deviation of a linear regression of MLCX TR daily log-returns on the benchmark's daily log-returns.

Table 3: Commodities and other asset classes performance

From 31-Dec-03 to 30-Jun-09	Annual return	Vol	Sharpe ratio
Standard & Poor's US 500 TR	-1.43%	22.94%	-16.67%
NASDAQ 100 STOCK INDX	0.12%	25.22%	-9.02%
MSCI Daily TR Gross EM USD	13.46%	24.98%	44.30%
ML US Broad Market Bond Index	4.48%	4.10%	50.89%
MLCX TR	7.64%	26.21%	20.05%
S&P GSCI TR	-1.01%	28.67%	-11.86%
DJ-UBS (DJ-AIG) TR	1.03%	20.60%	-6.60%
3-month T-bill returns (risk-free)	2.39%		

Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

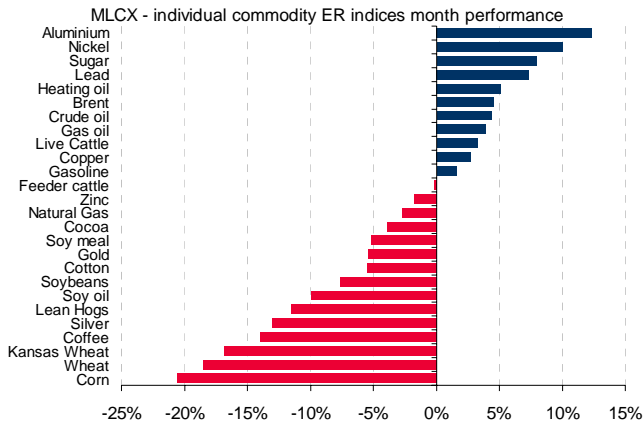
Annualised performance based on daily returns from 31-Dec-2003 to 30-Jun-2009

Since January 2004, commodities have broadly outperformed traditional equity indices, but there has been diverse performance among commodity indices. Specifically, the MLCX TR index outperformed the Standard & Poor's US 500 TR index by 9.07% on average during the last five years. However, the same comparison for the S&P GSCI TR index yields 0.42% and for the DJ-UBS TR index the relative performance is 2.46%. In the time period, EM equities and the ML US Broad Market Bond index fared better than commodity indices, primarily due to the recent correction to commodity prices.

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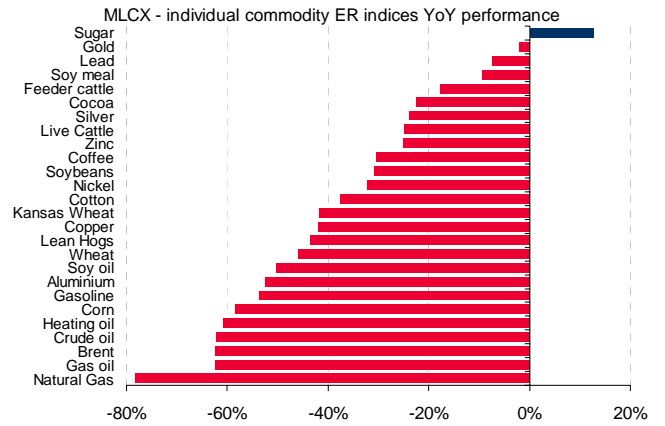
MLCX sub-indices

Chart 9: Performance for the month of June



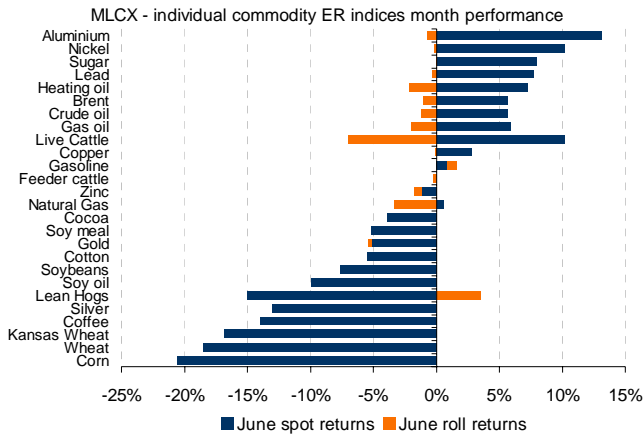
Source: Banc of America Securities-Merrill Lynch Commodity Research

Chart 10: Performance year-on-year (YoY)



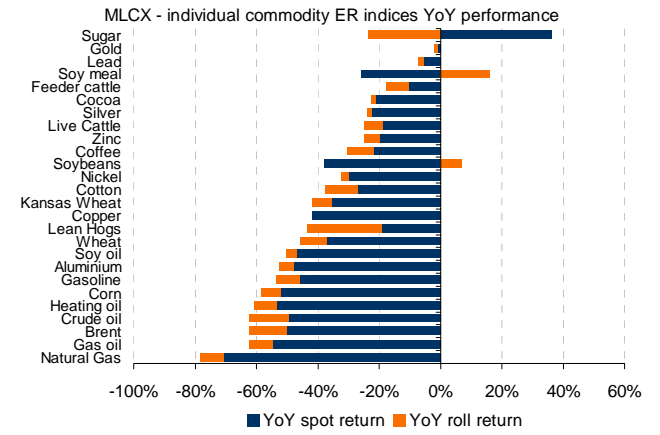
Source: Banc of America Securities-Merrill Lynch Commodity Research

Chart 11: Spot and roll returns for the month of June



Source: Banc of America Securities-Merrill Lynch Commodity Research

Chart 12: Spot and roll returns year-on-year (YoY)

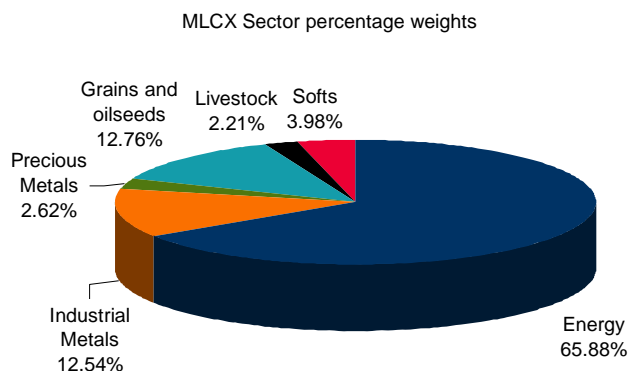


Source: Banc of America Securities-Merrill Lynch Commodity Research

Weights and contracts

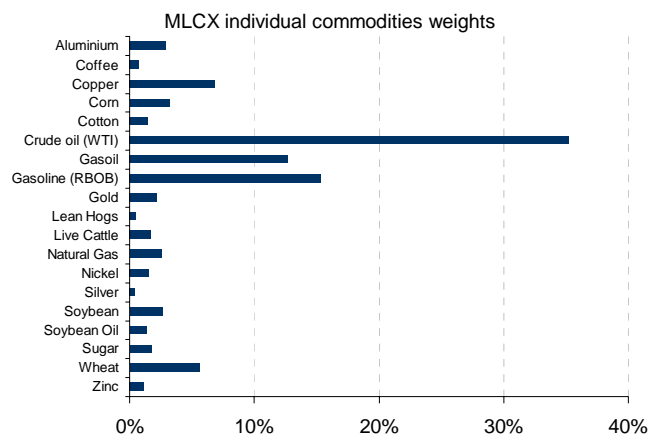
The Merrill Lynch Commodity index eXtra

Chart 13: Sector weights in the MLCX



Source: Banc of America Securities-Merrill Lynch Commodity Research

Chart 14: MLCX individual commodities weights



Source: Banc of America Securities-Merrill Lynch Commodity Research

Table 4: MLCX contracts

Contracts rolling in or constant for July	Contracts rolling out for July	Weight, end of June
Aluminium LAV9	Aluminium LAU9	2.95%
Coffee KCZ9	Coffee KCU9	0.74%
Copper LPV9	Copper LPU9	6.84%
Corn C Z9	Corn C U9	3.21%
Cotton CTZ9		1.47%
Crude Oil (WTI) CLV9	Crude Oil (WTI) CLU9	35.28%
Gas oil QSV9	Gas oil QSU9	12.72%
Gasoline (RBOB) XBV9	Gasoline (RBOB) XBU9	15.34%
Gold GCZ9		2.23%
Lean Hogs LHV9		0.55%
Live Cattle LCV9		1.67%
Natural Gas NGV9	Natural Gas NGU9	2.54%
Nickel LNV9	Nickel LNU9	1.60%
Silver SIZ9	Silver SIU9	0.39%
Soybean Oil BOZ9		1.32%
Soybean S X9		2.64%
Sugar SBV9		1.77%
Wheat W Z9	Wheat W U9	5.60%
Zinc LXV9	Zinc LXU9	1.15%

Source: Banc of America Securities-Merrill Lynch Commodity Research

Commodity Alpha

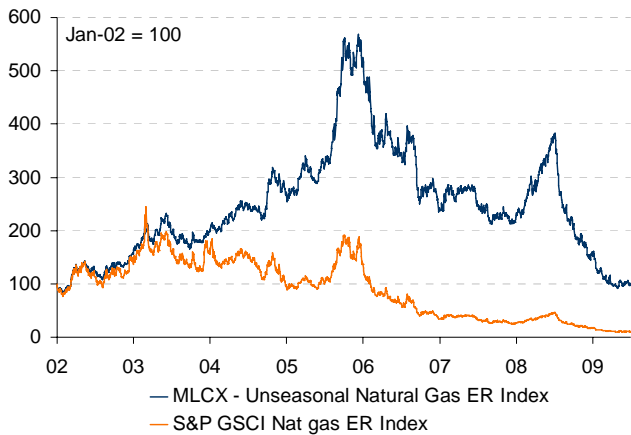
Long ML Unseasonal Natural gas ER Index - short S&P GSCI Natural gas ER Index

Table 5: Trade performance

LONG	MLCX - Unseasonal Natural Gas ER Index
SHORT	S&P GSCI Nat gas ER Index
Since launch on 17-Oct-06	13.28%
June	3.67%
May	-3.83%
YoY	3.93%
Worst month since Dec-2001	-33.01%
Best month since Dec-2001	23.62%
Annualised volatility of last 3 months	29.14%

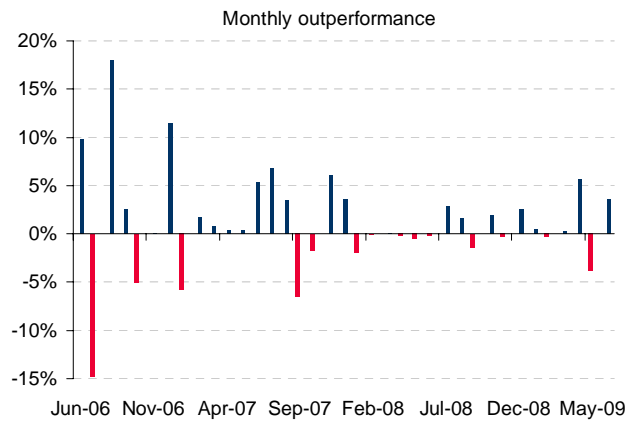
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 15: Indices historical performance



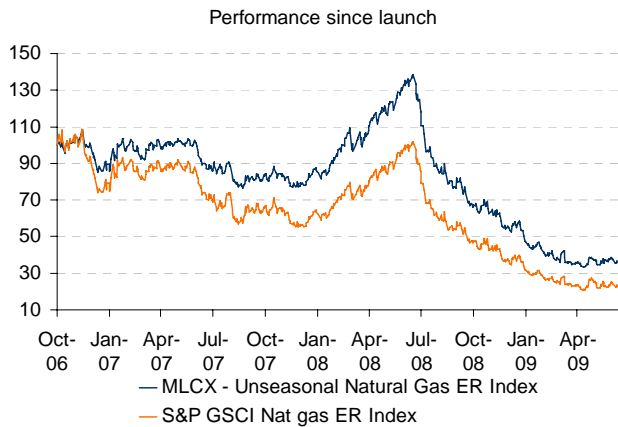
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 16: Monthly ML Unseasonal Nat gas outperformance



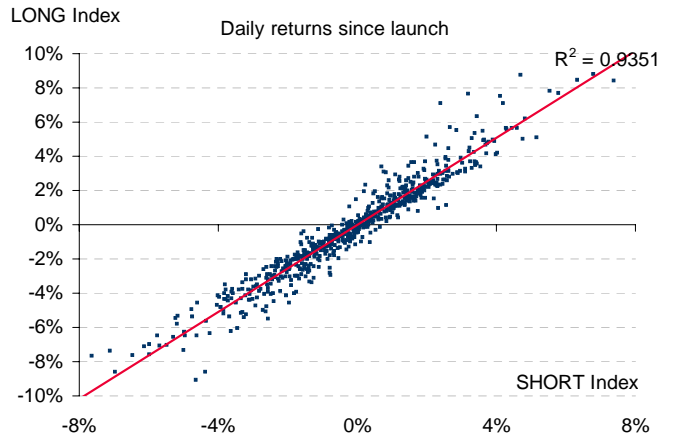
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 17: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 18: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

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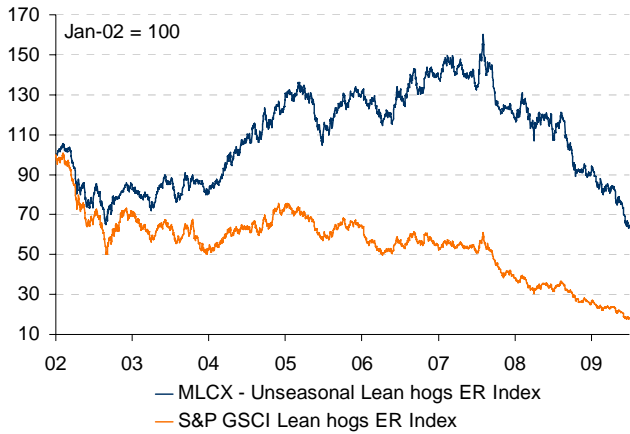
Long MLCX Unseasonal Lean hogs ER Index - short S&P GSCI Lean hogs ER Index

Table 6: Trade performance

LONG	MLCX - Unseasonal Lean hogs ER Index
SHORT	S&P GSCI Lean hogs ER Index
Since launch on 01-Jun-07	11.79%
June	-1.78%
May	-1.65%
YoY	1.26%
Worst month since Dec-2001	-6.73%
Best month since Dec-2001	10.66%
Annualised volatility of last 3 months	10.70%

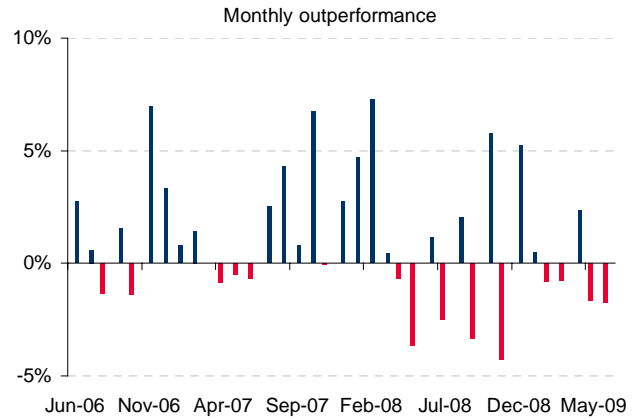
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 19: Indices historical performance



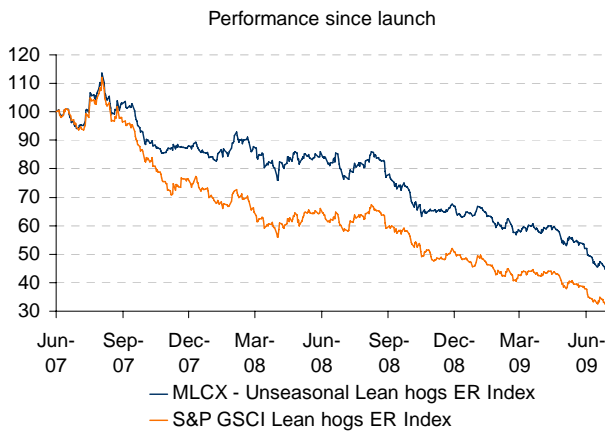
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 20: Monthly MLCX Unseasonal Lean hogs ER outperformance



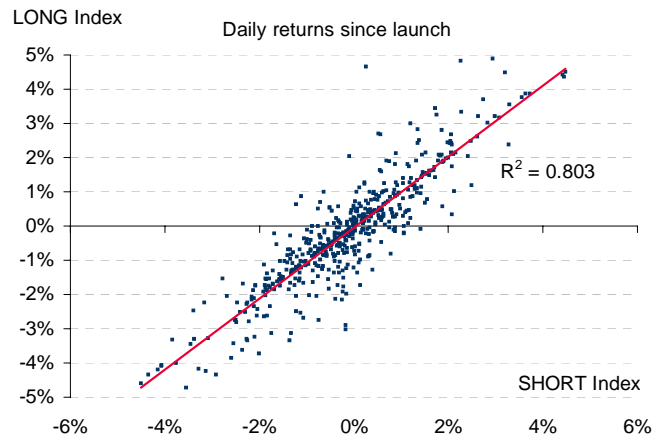
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 21: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 22: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

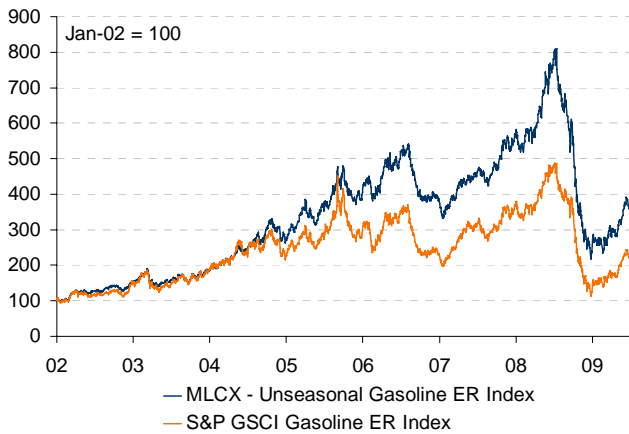
Long MLCX Unseasonal Gasoline ER Index - short S&P GSCI Gasoline ER Index

Table 7: Trade performance

LONG	MLCX - Unseasonal Gasoline ER Index
SHORT	S&P GSCI Gasoline ER Index
Since launch on 01-Jun-07	9.95%
June	2.10%
May	-6.36%
YoY	-0.29%
Worst month since Dec-2001	-15.32%
Best month since Dec-2001	9.69%
Annualised volatility of last 3 months	10.45%

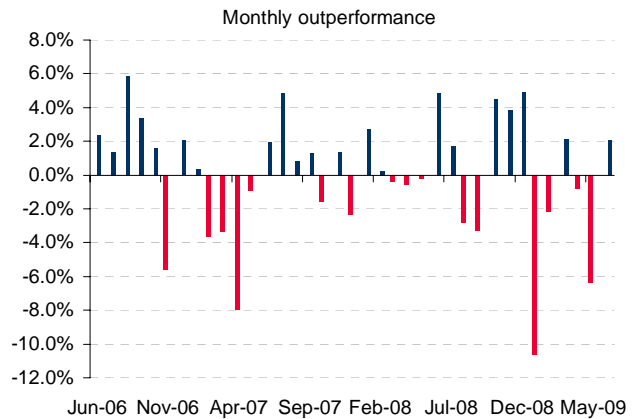
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 23: Indices historical performance



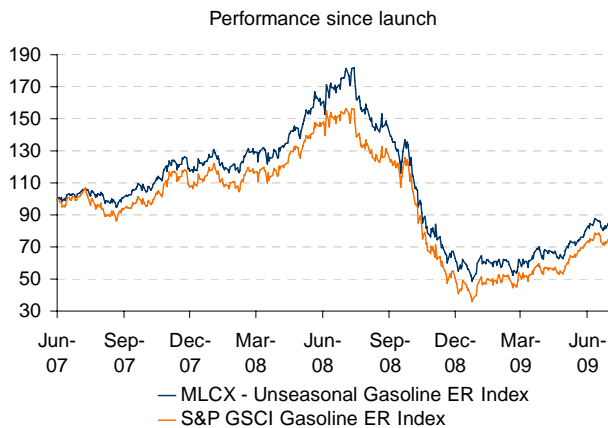
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 24: Monthly MLCX Unseasonal Gasoline ER outperformance



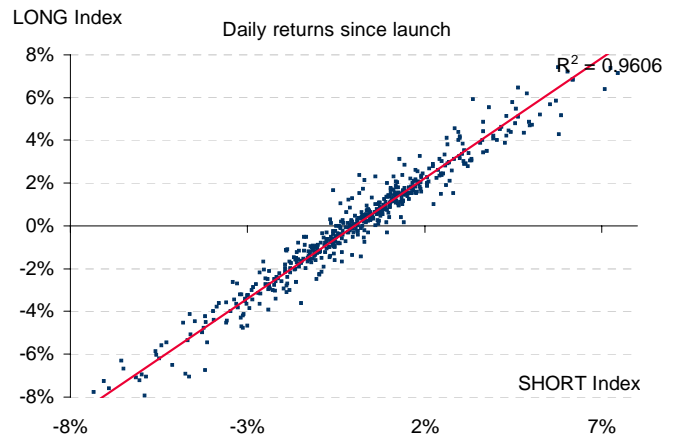
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 25: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 26: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

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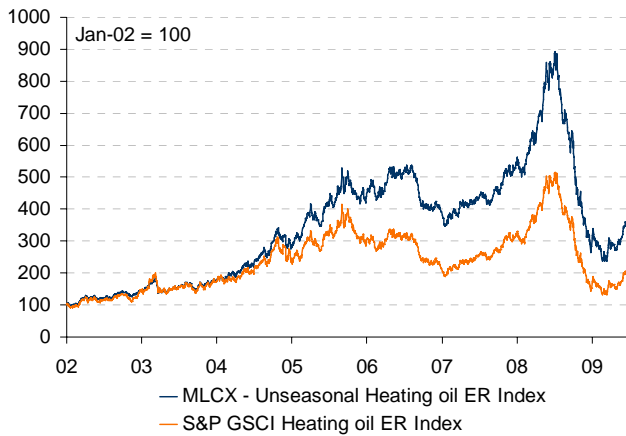
Long MLCX Unseasonal Heating oil ER Index - short S&P GSCI Heating oil ER Index

Table 8: Trade performance

LONG SHORT	MLCX - Unseasonal Heating oil ER Index S&P GSCI Heating oil ER Index
Since launch on 01-Jun-07	1.16%
June	0.14%
May	-2.66%
YoY	0.81%
Worst month since Dec-2001	-15.34%
Best month since Dec-2001	7.01%
Annualised volatility of last 3 months	7.38%

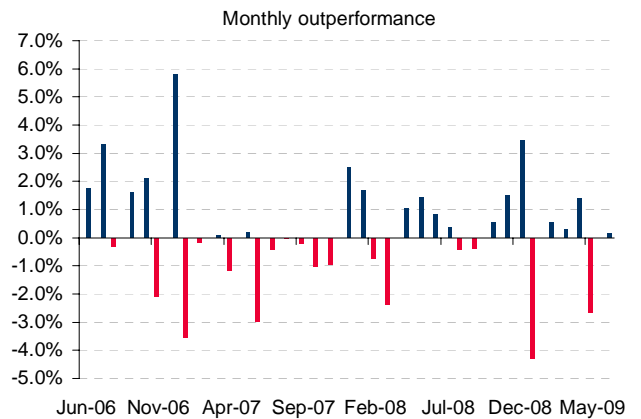
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 27: Indices historical performance



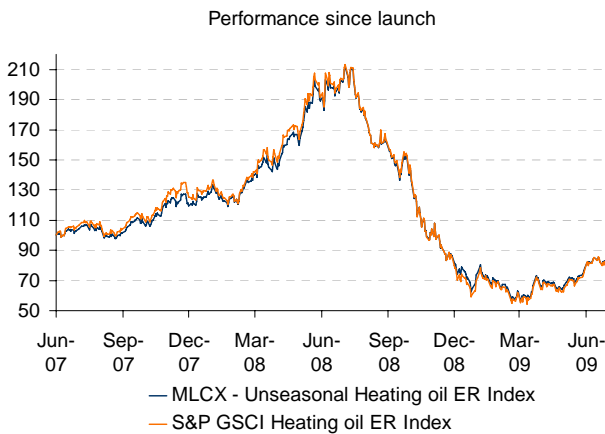
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 28: Monthly MLCX Unseasonal Heating oil ER outperformance



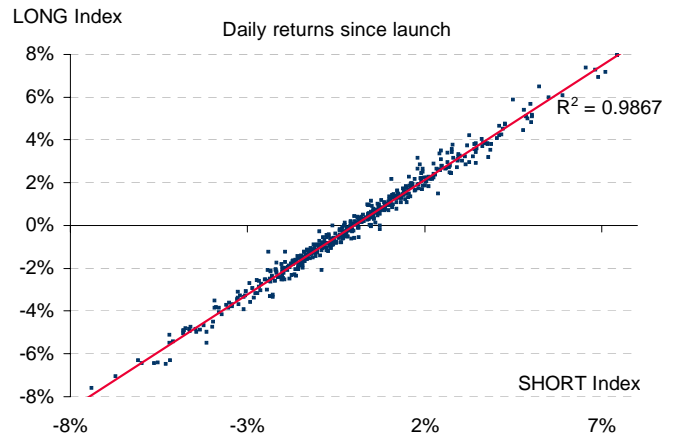
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 29: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 30: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

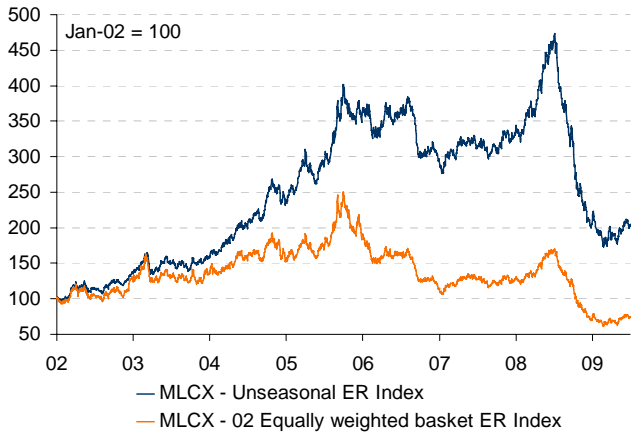
Long MLCX Unseasonal ER Index - short MLCX 02 - Equally weighted basket ER Index

Table 9: Trade performance

LONG	MLCX - Unseasonal ER Index
SHORT	MLCX - 02 Equally weighted basket ER Index
Since launch on 01-Jun-07	6.72%
June	1.22%
May	-4.10%
YoY	-0.43%
Worst month since Dec-2001	-10.92%
Best month since Dec-2001	9.48%
Annualised volatility of last 3 months	6.33%

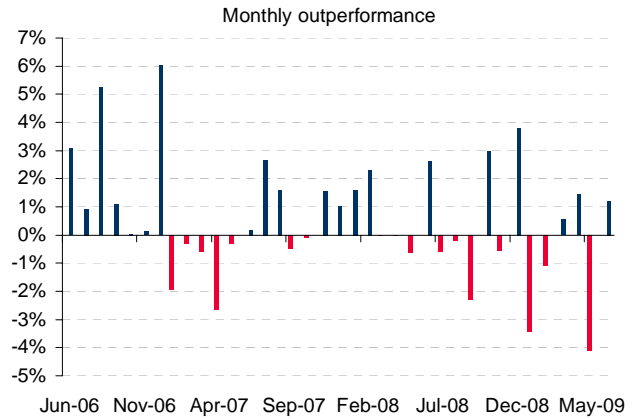
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 31: Indices historical performance



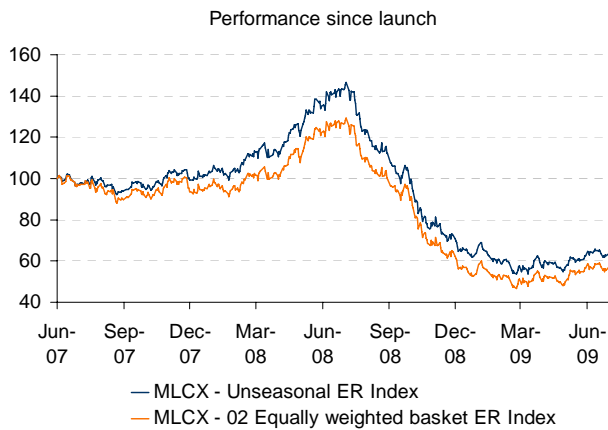
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 32: Monthly MLCX Unseasonal ER outperformance



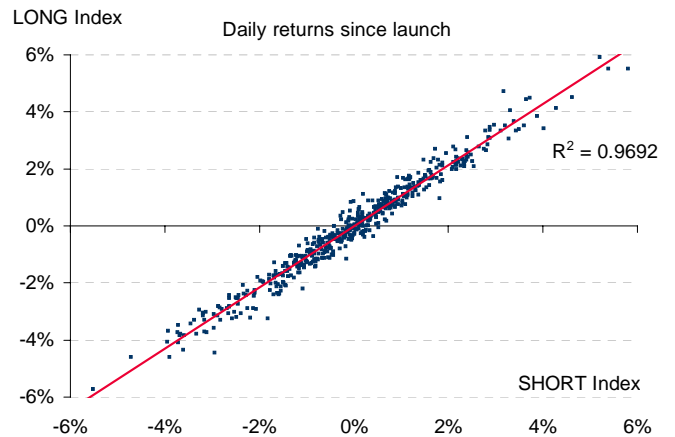
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 33: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 34: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

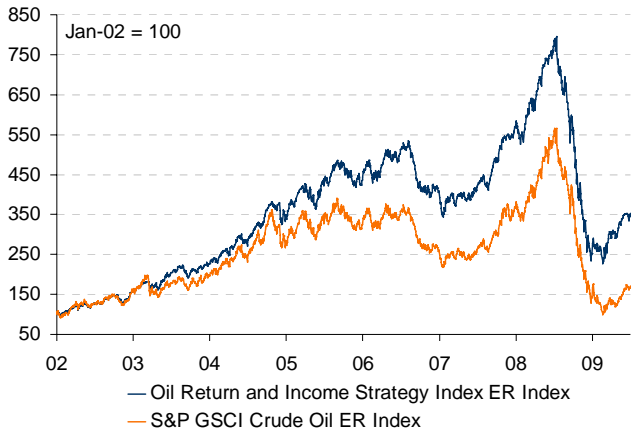
Long MLCX Oil RIS ER Index - short S&P GSCI Crude Oil ER Index

Table 10: Trade performance

LONG	Oil Return and Income Strategy Index ER Index
SHORT	S&P GSCI Crude Oil ER Index
Since launch on 22-May-06	22.56%
June	-4.54%
May	-11.51%
YoY	14.49%
Worst month since Dec-2001	-11.51%
Best month since Dec-2001	16.74%
Annualised volatility of last 3 months	23.08%

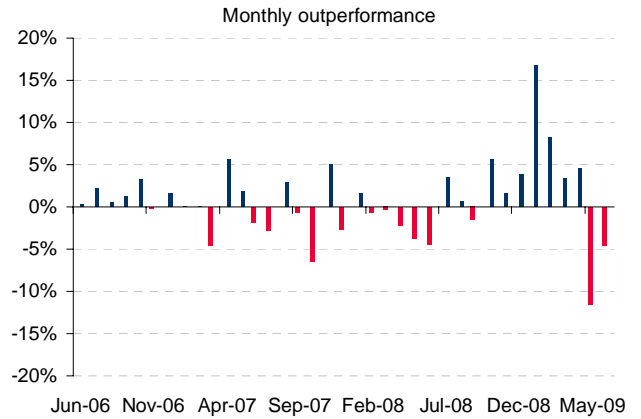
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 35: Indices historical performance



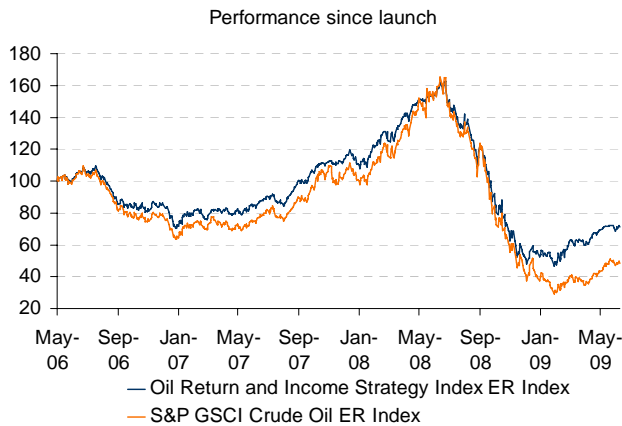
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 36: Monthly MLCX Oil RIS outperformance



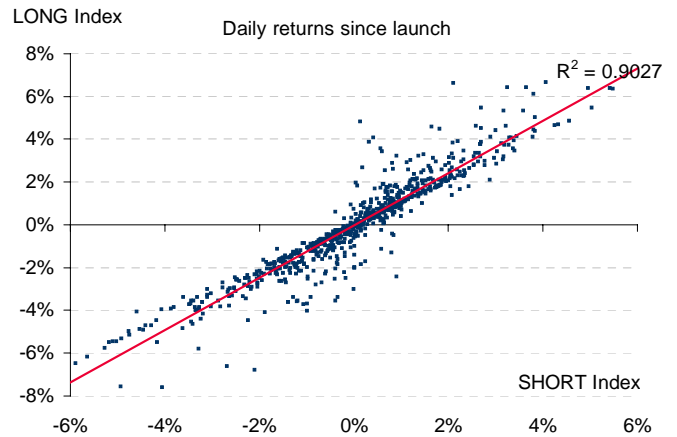
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 37: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 38: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Long MLCX ER Index - short S&P GSCI ER Index

Table 11: Trade performance

LONG SHORT	MLCX ER Index S&P GSCI ER Index
Since launch on 21-Jun-06	16.54%
June	-0.56%
May	-0.68%
YoY	7.96%
Worst month since Dec-2001	-4.93%
Best month since Dec-2001	4.76%
Annualised volatility of last 3 months	5.05%

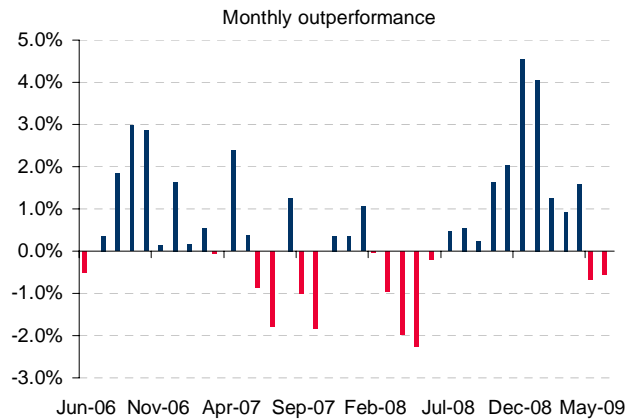
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 39: Indices historical performance



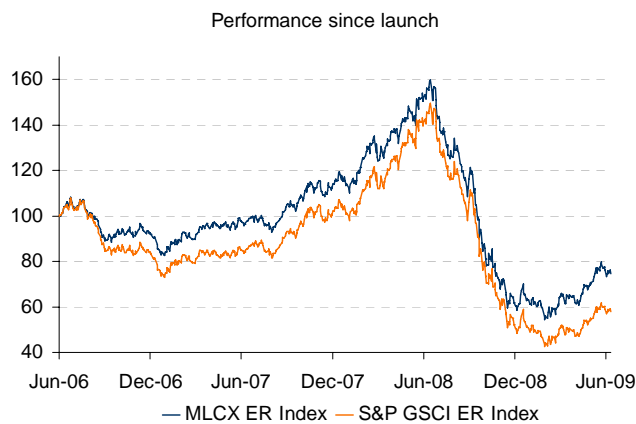
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 40: Monthly MLCX ER outperformance



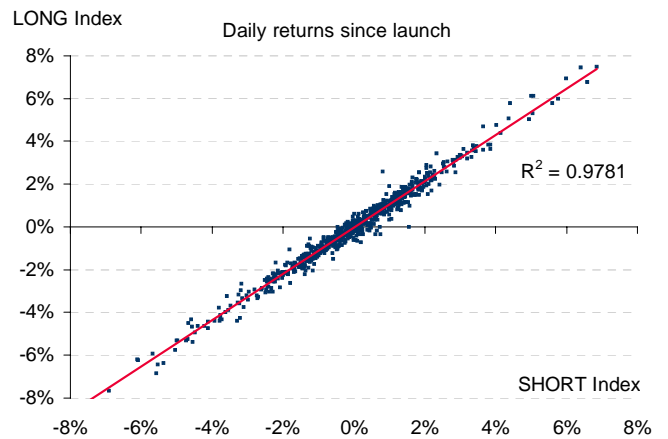
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 41: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 42: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

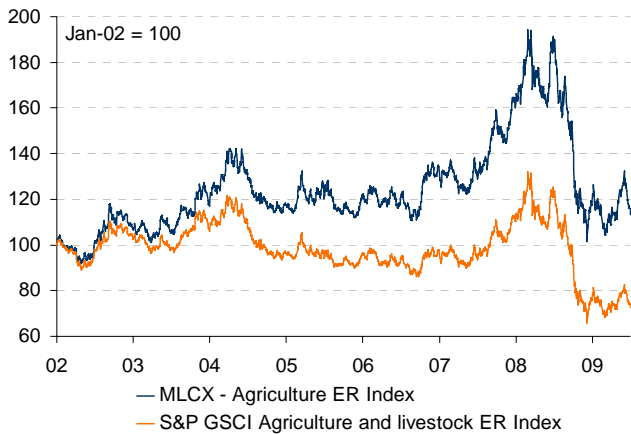
Long MLCX Agriculture ER Index - short S&P GSCI Agriculture and livestock ER Index

Table 12: Trade performance

LONG	MLCX - Agriculture ER Index
SHORT	S&P GSCI Agriculture and livestock ER Index
Since launch on 21-Jun-06	16.58%
June	-2.32%
May	2.38%
YoY	0.91%
Worst month since Dec-2001	-2.35%
Best month since Dec-2001	3.35%
Annualised volatility of last 3 months	4.42%

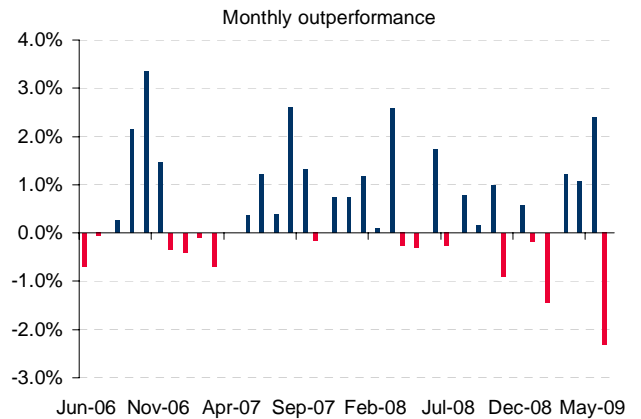
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 43: Indices historical performance



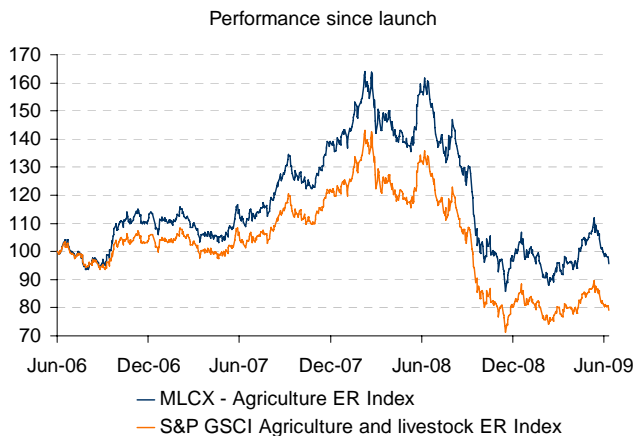
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 44: Monthly MLCXAG ER outperformance



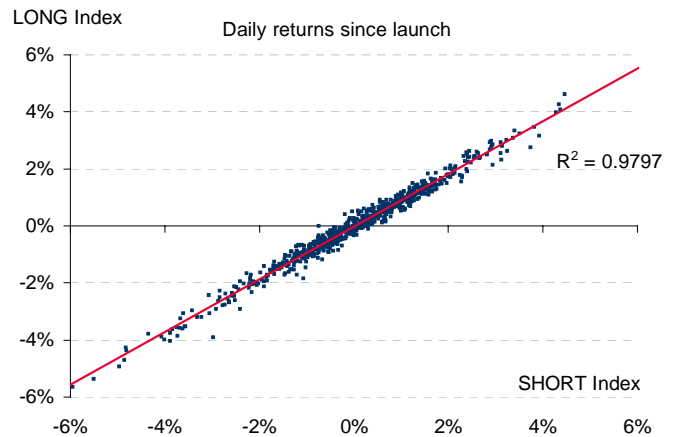
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 45: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 46: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

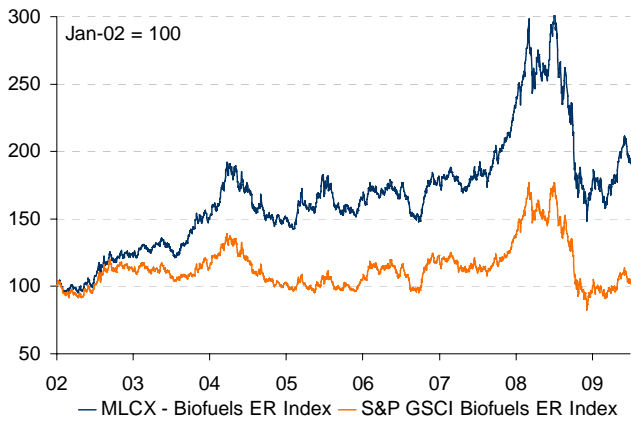
Long MLCX Biofuels ER Index - short S&P GSCI Biofuels ER Index

Table 13: Trade performance

LONG	MLCX - Biofuels ER Index
SHORT	S&P GSCI Biofuels ER Index
Since launch on 01-Oct-07	10.75%
June	0.21%
May	2.23%
YoY	4.91%
Worst month since Dec-2001	-3.67%
Best month since Dec-2001	6.32%
Annualised volatility of last 3 months	8.62%

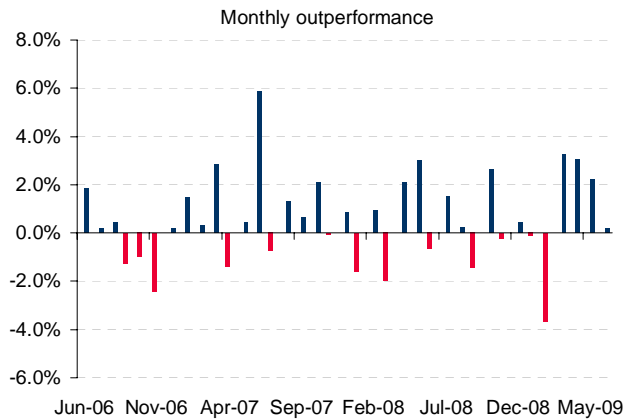
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 47: Indices historical performance



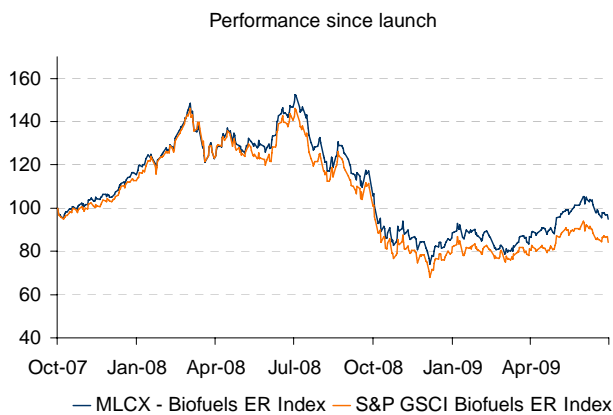
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 48: Monthly MLCXAG ER outperformance



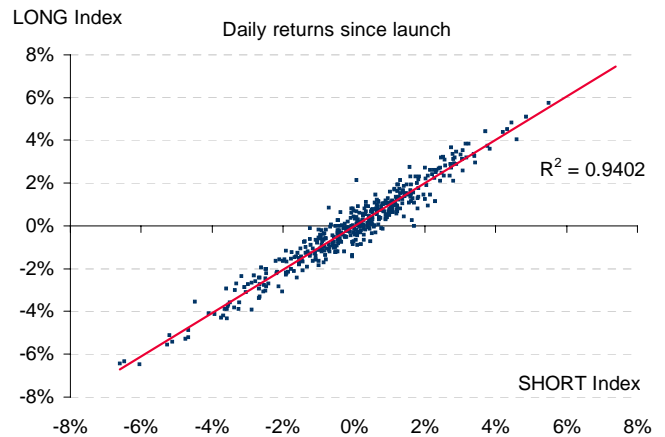
Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 49: Performance since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

Chart 50: Correlation between the two legs since launch



Source: Bloomberg, Banc of America Securities-Merrill Lynch Commodity Research

01 July 2009

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