BULLSEYE Highlights

Commodities

Stocks and bonds, which represent the ownership and debt of a company, are financial instruments or "paper" assets. Commodities, on the other hand, are considered "real" assets because they are tangible items that can be consumed. For example, we use oil to heat our homes and to produce gasoline to fuel our cars. And we use agricultural products, such as corn or cotton, to produce food and clothing. Where financial assets are typically valued at their net present value based on dividends, earnings or income potential, commodities are often valued by the basic laws of supply and demand.

The perception among many investors is that commodities are always riskier than stocks. As with most investments, commodities do have inherent risks; some that are unique to the asset class. However, a Yale study of commodity returns between 1959 and 2004 showed that investor perceptions were inaccurate. This study was re-examined ten years later and was found to remain accurate. In addition to validating commodities as a necessary asset class, the study found that commodity futures and stocks have similar historical returns and volatility. The study also showed that the correlation of commodity returns with stocks and bonds is low, especially over longer holding periods. The original study describes that the diversification benefits were best when they were needed most; when stocks earned below-average returns due to equity market. During times of inflation and recessions, commodity returns were generally positive, whereas stock and bond returns generally disappointed. And despite the methods used by many indexes, rebalancing commodity futures annually, or not at all (buy and hold), outperformed monthly rebalancing.

Commodities have become increasingly more popular in recent years as investors seek additional ways to diversify their portfolios. This popularity has led to the creation of several investment products tied to indexes that offer access to commodity exposure. But the construction and calculation methodology varies widely from one index to the next.

Commodity Index Construction

Index	Sector Weights	Components & Weights	Contracts & Roll Frequency
Bloomberg Commodity Index	Energy 29.84% Precious Metals 17.02% Industrial Metals 15.48% Grains 23.66% Softs 8.89% Livestock 5.12%	22 Components; Rebalanced in January on price % basis; Annual weights defined in June by committee	Near-Term: Contracts dated 1-3 months out Rolled monthly
S&P Goldman Sachs Commodity Index	Energy 63.56% Precious Metals 3.59% Industrial Metals 8.79% Grains 11.54% Softs 4.16% Livestock 8.37%	24 Components; Weights based on 5 year world production, rebalanced annually	Near-Term: Contracts dated 1-3 months out Rolled monthly
Longview Extended Commodity Index	Energy 25.98% Precious Metals 24.48% Industrial Metals 7.49% Grains 12.32% Softs 18.30% Livestock 11.44%	16 Components; Initially market-weighted; weights float with maximum limits	Long-Dated: Contracts dated 15-18 months out Semi-annual and annual rolls

Source: Bloomberg as of 12/31/2015

Commodity indexes use vastly different component allocations, investment methodologies, and rebalancing frequencies which can lead to large differences in performance. Some indexes are less diversified than others and some overweight specific sectors, such as energy or precious metals. But a well constructed commodity index can provide an additional layer of diversification through a better balance of exposure to noncorrelated components within the index itself.

Something that separates commodity returns from those of stocks and bonds is the inherent return generated from inflation. When the markets expect inflation, bonds generally drop in price as interest rates often rise. Many people would think stock prices could drop as well if the cost of materials used to create products begins to rise. Yet a commodity index might be expected to rise in response to higher prices for raw materials. This response to inflation expectations actually provides the rationale for a low correlation between a commodity index and stocks and bonds.

The case for including commodities in a portfolio is simple—exposure to the asset class may help diversify a portfolio from some unexpected events. As with any asset class, nobody can predict with certainty when to put commodities to work in a portfolio. Therefore, investors may want to consider commodity exposure as an ongoing allocation to their portfolio. Commodities have historically produced returns that are competitive with equities, but often at different times. Remember that commodities, as a stand-alone investment, do have specific risks that are unique to the asset class. But as a diversification component, commodities may also provide long-term benefits due to their historically low correlation with other asset classes such as stocks and bonds.

Commodity Index Performance

As of 12/31/2015	Bloomberg Commodity Index	S&P GSCI	Longview Extended Commodity Index	Stocks (S&P 500)
2000	31.84%	49.74%	9.06%	-9.10%
2001	-19.51%	-31.93%	-15.67%	-11.89%
2002	25.91%	32.07%	20.17%	-22.10%
2003	23.93%	20.72%	15.12%	28.68%
2004	9.15%	17.28%	26.04%	10.88%
2005	21.36%	25.55%	41.53%	4.91%
2006	2.07%	-15.09%	11.41%	15.79%
2007	16.23%	32.67%	28.31%	5.49%
2008	-35.65%	-46.49%	-25.36%	-37.00%
2009	18.91%	13.48%	20.20%	26.46%
2010	16.83%	9.03%	24.39%	15.06%
2011	-13.32%	-1.18%	-2.23%	2.11%
2012	-1.06%	0.08%	2.80%	16.00%
2013	-9.52%	-1.22%	-9.65%	32.39%
2014	-17.01%	-33.06%	-15.11%	13.69%
2015	-24.66%	-32.86%	-18.97%	1.38%
3 Years	-17.29%	-23.71%	-14.66%	15.13%
5 Years	-13.47%	-15.18%	-8.98%	12.57%
10 Years	-6.43%	-10.56%	-0.03%	7.31%
Bear Market Apr 2000-Mar 2003	8.29%	7.73%	2.53%	-16.09%
Bull Market Apr 2003-Mar 2006	15.90%	18.78%	29.50%	17.22%
Financial Crisis Jan 2008-Dec 2009	-12.53%	-22.07%	-5.28%	-10.74%
Risk (10-year)	18.09%	23.77%	17.86%	15.00%
Correlation vs S&P 500 (10-year)	0.50	0.50	0.46	1.00

Source: FactSet and Bloomberg as of 12/31/2015

The Bloomberg Commodity Index, S&P GSCI, and Longview Extended Commodity Index are all benchmarks for broad-based commodity exposure. The S&P 500 Index, shown as a proxy for stock investments, is a widely known broad-based equity index. Index returns assume reinvestment of all dividends and do not reflect any management fees, transaction costs or expenses. The indexes are unmanaged and are not available for direct investment. **Standard Deviation** (Risk) is a statistical measurement of volatility based on historical returns. **Correlation** measures how closely two securities' movements are associated, ranging from 1.0 (highly correlated) to -1.0 (inversely correlated).

Past performance is not indicative of future returns. *The information shown herein is for illustrative purposes only and should not be used as a predictive measure for the future return expectations of any investment. The information is subject to change or revision without notice, should not be construed as a recommendation of any specific security or investment product, and was prepared without regard for specific circumstances and objectives of any individual investor.* ***All investments involve risks, including the potential for loss of principal.*** *Nontraditional and alternative investments may involve additional risks specific to the asset class. Before investing in any financial product, always read the prospectus and/or offering memorandum for product-specific risks.*

AD-032316