Press Release **Singapore, London, Nice, October 25, 2011**

EDHEC-Risk Institute study sheds new light on commodity investment and financialisation of commodity markets

A number of policy-makers have blamed the decade-long rise in commodity prices and recent market volatility on the growing influence of financial investors and called for new regulation restricting their participation in commodity markets. Market financialisation has also led investors to worry about higher integration between commodity and traditional financial markets weakening the portfolio benefits of commodity investment.

EDHEC-Risk Institute Professor Joëlle Miffre addresses these concerns in a study released today entitled "Long-Short Commodity Investing: Implications for Portfolio Risk and Market Regulation", produced with market data and support from CME Group.[i]

The study first examines the performance and risk characteristics of long-only commodity index investments favoured by passive investors and of long/short commodity strategies of the kind implemented by hedge fund managers.

Over 1992-2011, strategies involving going long and short in commodity futures based on signals such as momentum, term structure or hedging pressure are found to dominate investment in long-only commodity indices, in terms of raw as well as risk-adjusted performance.[ii]

The low correlations of long-only and long/short commodity portfolios with equities and bonds confirm the strategic role of commodity investments as diversifiers of both equity and fixed income risks. While the correlation between long-only commodity portfolios and equities has risen sharply since the downfall of Lehman Brothers, long/short investing continues to offer excellent diversification benefits.[iii] Overall, long/short investing is found to be a better diversifier of equity risk and long-only investing a better diversifier of fixed income risk. However, the diversification benefits of long-only investing are unequivocally reduced in times of financial stress (correlations with equities and bonds rise), while long-short commodity portfolios are found to provide a partial hedge against extreme risks in equity markets (correlations fall when the volatility of equities rises) and to better withstand turbulence in fixed income markets.

The study then confirms the financialisation of commodity markets and investigates whether the increased participation of long/short investors has caused changes in the volatility of their portfolios or in the correlation between their returns and those of traditional assets. The tests performed find very little to no evidence to suggest that these investors have had such a destabilising role.[iv]

These results on the performance and risk characteristics of long-only and long/short commodity investing have important practical consequences for investors that are considering or have implemented commodity investment programmes. The new evidence on the financialisation of commodity futures market and the impact of long/short investing challenges the assumptions of a politically charged debate and will be of relevance not only to regulators and industry associations but also to investors that need to factor social responsibility considerations into their investment decisions.

Download: "Long-Short Commodity Investing: Implications for Portfolio Risk and Market Regulation"

EDHEC–Risk Institute	EDHEC Risk Institute—Europe	EDHEC Risk Institute—Asia
393 promenade des Anglais BP 3116 - 06202 Nice Cedex 3 France	10 Fleet Place - Ludgate London EC4M 7RB United Kingdom	1 George Street #07-02 Singapore 049145

Contact:

For further information, please contact **Séverine Anjubault**:

Tel.: **+33 (0)4 93 18 78 63** – E-mail: **severine.anjubault@edhec-risk.com**

About EDHEC-Risk Institute

EDHEC-Risk Institute is part of EDHEC Business School, one of Europe's leading business schools and a member of the select group of academic institutions worldwide to have earned the triple crown of international accreditations (AACSB, EQUIS, Association of MBAs). Established in 2001, EDHEC-Risk Institute has become the premier European centre for financial research and its applications to the industry. In partnership with large financial institutions, its team of 66 permanent professors, engineers and support staff implements six research programmes and eleven research chairs focusing on asset allocation and risk management in the traditional and alternative investment universes. The results of the research programmes and chairs are disseminated through the three EDHEC-Risk Institute locations in London, Nice and Singapore.

EDHEC-Risk Institute validates the academic quality of its output through publications in leading scholarly journals, implements a multifaceted communications policy to inform investors and asset managers on state-of-the-art concepts and techniques, and forms business partnerships to launch innovative products. Its executive education arm helps professionals to upgrade their skills with advanced risk and investment management seminars and degree courses, including the EDHEC-Risk Institute PhD in Finance.

www.edhec-risk.com

About CME Group

As the world's leading and most diverse derivatives marketplace, CME Group (www.cmegroup.com) is where the world comes to manage risk. CME Group exchanges offer the widest range of global benchmark products across all major asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, energy, agricultural commodities, metals, weather and real estate. CME Group brings buyers and sellers together through its CME Globex® electronic trading platform and its trading facilities in New York and Chicago. CME Group also operates CME Clearing, one of the world's leading central counterparty clearing providers, which offers clearing and settlement services for exchange-traded contracts, as well as for over-the-counter derivatives transactions through CME ClearPort®. These products and services ensure that businesses everywhere can substantially mitigate counterparty credit risk in both listed and over-the-counter derivatives markets.

[i] The extant academic literature has focused on the conditional correlations between long-only commodity portfolios and traditional assets; its overwhelming conclusion is that it is not possible to empirically link investments in commodity futures and commodity futures prices. This study extends the literature by looking at the potentially unsettling role of long-short investors on price volatility and cross-market correlation.

[ii] Over the period, the mean excess return of the Standard and Poor's Goldman Sachs Commodity Index (S&P-GSCI) equals 0.64% per year, that of the long-only equally-weighted portfolio of the twenty seven commodities in the study is 4.28% and the average mean excess return of the long-short portfolios equals 7.99% when only one type of signal is used and 9.03% when two signals are used in combination. The Sharpe ratios of the long-short portfolios range from 0.2711 to 0.6302 and average out at 0.5093. The equally-weighted portfolio has a Sharpe ratio of 0.0529 and the S&P-GSCI a Sharpe ratio of 0.1965.

[iii] The mean in the average conditional correlations of the S&P500 index relative to long-short indices stands at a mere 0.0559, while that relative to long-only indices equals 0.5402.

[iv] This conclusion is based on Granger-causality tests and holds irrespective of whether investors are labelled as "non-commercial" in the CFTC Commitment of Traders report or "professional money managers" (i.e., CTAs, CPOs and hedge funds) in the CFTC disaggregated Commitment of Traders report.