



CUSHIONING THE RISKS OF COMMODITIES

By David Greising

For years, John Beviacqua, 50, believed that buying stocks was the smart, safe way to invest for retirement. But after the 1987 crash erased more than \$15,000 of his portfolio, the chief financial officer for data processing firm RCG/Pro-Access decided to rethink his strategy. Today, he has 45% of his portfolio in an investment he considers even smarter and safer than stocks: commodities funds.

That's right. Although commodities—or futures, to use the more modern term—are notoriously risky if you trade them yourself, Beviacqua and a growing horde of investors are putting their faith in professionally managed funds. These investments give individuals access to the potentially lucrative-yet volatile-futures markets for as little as \$2,000. "People are afraid of commodities. I'm afraid of commodities," says Beviacqua. "But not with a good manager out there."

THE RECORDS OF TOP TRADING ADVISERS

Firm	Annualized return for 5 yrs. *	Worst 2-month period	Assets under management (in millions)
ROEMER WEATHER Des Moines, Iowa	95.81%	-31%	\$13
RED OAK COMMODITY ADVISORS Saddlebrook, N.J.	81.38	-2	77
LOGOS TRADING Chicago	73.01	22	28
HOLLINGSWORTH TRADING Giddings, Tex.	72.27	-3	50
SCHEIDER MANAGEMENT Albany, Conn.	58.76	-12	20

*Compound annual total return

DATA: BARCLAY TRADING GROUP LTD.

Even with professional management, though, futures funds are highly speculative. In most cases, investors are advised to place no more than 5% to 10% of their total portfolio in such funds, and they should be able to withstand heavy losses of principal. Commodities are also not a game for people who need instant access to their money, such as retirees dependent on a steady income stream. Careful investors can protect themselves to some extent by choosing managers with long, proven track records. They can even turn to guaranteed funds that offer lower rates of return but pledge to refund the investor's original outlay, no

matter what the trading results.

A lot of investors think the possible rewards are worth the risks. Futures funds have attracted more than \$21 billion, nearly three times as much as they contained before the 1987 stock market crash, according to the Managed Futures Assn. That's still only a fraction of the \$350 billion in stock mutual funds, but the dollars keep flowing in.

For most of this year, funds have traded miserably, losing more than 10% of their value. But they turned around smartly in June, when fund managers found moneymaking opportunities in

currencies and interest rates. "Some managers who have been taking a beating over the last few months are currently seeing 10% and 12% returns," says Leon Rose, publisher of *Managed Account Reports*, a newsletter that tracks fund performance. "This only bodes well for the commodity funds," he says. Still, perhaps more than other investments, commodity performance is difficult to predict because the markets move so quickly and the funds trade in such a variety of products.

LOSS LIMIT. Futures funds offer a number of advantages. Investors get the huge potential upside of buying commodities, but unlike speculators who often buy futures on margin, their losses are limited only to the amount they actually invest. They get an investment vehicle that typically moves independently of stocks. That can be an enticing feature at a time when the stock market's gearshift appears stuck between neutral and reverse. They also can get an attractive performance record, with a number of fund managers posting an annual return of 15% or more over the last 10 years, says *Managed Account Reports*. Stock prices, meanwhile, have appreciated by about 14% per year during that period.

Mainstream brokerage firms such as Merrill Lynch, Dean Witter Reynolds, and Shearson Lehman Brothers have all backed funds in recent years with low costs of entry. But those investors willing to risk a bit more can choose another option: private placements available to groups of 35 or fewer people who can each put up a minimum of, say, \$5,000 to \$150,000. Pension funds and other institutions have started buying into managed funds, but it still remains a business dominated by retail investors who supply more than two-thirds of the money and put less than 10% of their investment capital into commodities.

Choosing the right fund requires some work, such as perusal of offering documents that typically run more than 200 pages. The most important investor checkpoint is the name of the trading adviser—the person or people who actually make trading decisions. The trading adviser's history should show a record of reasonable profits, losses of no more than 25% in any given year, and a consistent growth in assets under management. For example, Sjo Inc., which manages more than \$50 million in fund assets, specializes in futures on foreign financial instruments. In the last three years, Sjo has shown a 61% compounded annual return, posted a one-month loss no bigger than 14.5%, and done no worse than a 26% gain in any one year.

REASONABLE FEES. Sometimes, the trading adviser's impact can be hard to determine because the fund managers hire more than one. "It's become fashionable to have 8 or 10 trading advisers involved in one fund," says John Alban Jr., president of Pragma, a trading advisors firm. "Sometimes it's hard to know who's doing what to whom."

Fees charged by the brokerage firm and the trading adviser should be reasonable—say, a 4% up-front sales load, a 1% guaranteed management fee, and an incentive fee of 1% to 3% of trading profits. And conditions for withdrawal of funds, or "redemptions," should be clearly stated and allow investors to receive their money in a timely manner.

THE CONTRACTS BEHIND THE FUTURES FUNDS

AGRICULTURALS

Range from soybeans to wheat to pork bellies to orange juice. Prices tend to move based on weather, trade policy, consumption, and international crops.

CURRENCIES

Investors speculate on the future value of the dollar vs. German marks, Japanese yen, Swiss francs, and others.

ENERGY

Crude oil, heating oil, and gasoline are the most popular. Weather, wars, and inflation make these markets move.

INTEREST RATES

Sensitive to all manner of economic news and to actions by the world's central banks. Eurodollar futures are tied to short-term rates charged on funds deposited overseas. Treasury bond futures are tied to the U.S. government's 30-year bond.

PRECIOUS METALS

Silver, gold, platinum. One of the sleepest games around in recent years. May take a resurgence in inflation to wake them up.

STOCKS

Available on the Standard & Poor's 500 or other stock indexes. Enable fund managers to bet on the future course of a big basket of stocks in a single leveraged transaction.

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Unlike open-end mutual funds, in which investors can buy or sell shares on an ongoing basis as market conditions change, most commodity funds are closed-end. Once the funds start trading, new investors are no longer welcome. That means investors must make their decision about buying into a fund up front, based on the past performance of the trading advisers. Investors in private pools can sell their stakes, but arranging such transactions can be a touch-and-go proposition. Some investors prefer funds that target particular sectors of the commodity markets. Funds that concentrate on currencies and on shifts in interest rates in foreign countries have been popular lately. Dean Witter, for example, recently raised \$68 million for its Global Perspective Portfolio, and Shearson is currently raising money for its F1000 Guarantee Fund XIX. But many fund managers believe that targeted funds unnecessarily limit trading options. "From our perspective, we are futures traders, whether it's currencies, grains, interest rates, metals, or whatever," declares Alan Kaufman, senior vice-president of Mt. Lucas Management, an investment firm based in Princeton, N. J.

ERRATIC PERFORMANCE. Whatever their target, all commodity funds are likely to show an erratic performance that can be unsettling. Indeed, it's not uncommon for funds to shut down after losing all or most of their investors' money. "A higher degree of volatility is assumed," declares Sol Waksman, president of Barclay Trading Group, a Fairfield (Iowa) brokerage firm that tracks the performance of trading advisers. "If investors can't handle it, they should stay away from commodity funds."

Instead, those people might consider guaranteed funds, which promise a return of principal, despite market conditions. The pledge is possible because trading advisers invest about two-thirds of the fund assets in low risk instruments such as zero-coupon bonds or Treasuries. The other third goes into the commodities markets to boost the fund's overall yield. Cost for such a promise? Less money for trading means less risk of loss--and less opportunity for double-digit gains.

Reminder: We do not guarantee your investment success.

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