BCOM Index Quarterly Commodities Update
Second Quarter of 2019

Executive Summary

The Bloomberg Commodity Index Total Return declined 1.19% in the second quarter of 2019. Natural Gas fell 16.18% as warmer-than-average temperatures in April and then milder temperatures for the rest of the period in most areas of the continental US reduced heating and electricity generation needs. US natural gas inventories experienced one of the fastest paces of builds in history over the quarter. Cotton decreased 14.22%, as concerns mounted that China may not take delivery of all of the US cotton it committed to purchase after trade talks deteriorated in May. In addition, the US Department of Agriculture (USDA) revealed higher-than-expected planted cotton acreage for the 2019-2020 season due to beneficial weather, increasing production estimates. Lean Hogs weakened 13.88%, mostly in the second half of the quarter, after China indicated that the African swine fever outbreak among its hog population had been contained, weighing on China's import expectations. The USDA also reported an increase in domestic frozen pork inventories in May and growth in US hog herd sizes as the US-China trade war continued to put pressure on demand. Corn rose 14.92% due to decreased supply forecasts. Severe storm conditions in the US Midwest and Great Plains caused significant planting delays as the pace of plantings slowed and shortened corn's growing season. Chicago Wheat gained 14.03% as heavy rainfall in the US Midwest increased the risk of fungus growth, potentially decreasing US crop yields and the production of futures deliverable-grades of wheat. In addition, as corn prices rose, more wheat was diverted to making animal feed at a lower cost. Coffee increased 10.63% as adverse wet weather in key coffee-producing regions in Brazil disrupted the harvest and reduced supply expectations for the current season. Third quarter forecasts of cold temperatures impacting Brazil's coffee regions also threatened the quality of the current season's crop while also putting next season's crop at risk, further supporting prices.

Quarterly Commentary

The Bloomberg Commodity Index Total Return was negative for the quarter, with 14 out of 23 constituents posting losses. Livestock declined 11.01%. In addition to Lean Hogs, Live Cattle fell after USDA data revealed declining US beef exports throughout the period. China, one of the largest buyers of Brazilian beef, removed its temporary ban on beef imports from the South American nation after Brazil was able to verify that a case of mad cow disease did not spread throughout its food chain. In addition, China's cold storage facilities at major ports were reported as nearing capacity by the end of the period. Both situations reduced US beef export expectations. Industrial Metals fell 7.23%, led lower by Zinc, after inventories tracked by the London Metal Exchange rose for the period. The International Lead and Zinc Study Group also revised data to show a market surplus during January and February this year. Base metals declined broadly as the US-China trade war continued to weigh on demand prospects as trade negotiations halted in May. Energy decreased 4.56%, led lower by Natural Gas. WTI and Brent Crude Oil also fell as concerns around the global growth outlook weighed on the demand for crude oil and petroleum products. Agriculture increased 4.50% as some gains in grains and Coffee were offset by losses in Cotton. Precious Metals rose 7.15% as continued uncertainty surrounding US-China trade negotiation translated into a slower global growth trajectory. That, paired with statements from central banks that implied they were preparing to resume easier monetary policies, raised the demand for Gold as a store of value.

Market Outlook

The Group of 20 Summit in Japan provided an avenue for world leaders to improve both trade and political relationships, particularly between the US and China, as other nations affected by the trade war become more vocal about their reaching a trade agreement. The US and China entered into a temporary truce to prevent an escalation of tit-for-tat tariffs while also allowing for negotiations to resume, which has caused market participants to become cautiously optimistic that a near-term trade deal may be reached. Reduced barriers to trade would be beneficial to commodity demand as companies are increasingly delaying capital investments amid the uncertainty. Russia also announced at the G20 Summit that it agreed with Saudi Arabia to extend the crude oil production cut agreement through year end and potentially into the first quarter of 2020. How strictly all participants will be at adhering to the agreement remains a concern as some participating nations, such as Nigeria, face growing political and financial constraints. So far, a majority of the participating nations to the OPEC+ agreement have met or exceeded production cut quotas over the past year and a half, exemplifying their commitment to supporting crude oil prices. However, the biggest risk to the agreement's effectiveness rests outside of the group's control. A question remains on how much more will US shale producers continue to grow production and make up for the shortfall.

Beyond policy risk, weather continued to impact the planting and growing seasons of key crops. Per the National Oceanic and Atmospheric Administration, soil saturation levels for a large part of the US Midwest remained abnormally moist to excessively wet in late June. The heavy rainfall has forced farmers to plant a higher percentage of their fields at the same time, increasing the concentration risk to plantings if additional adverse weather (con't)

conditions appear, especially during the key summer growing season. Meanwhile, European wheat faced a heatwave by the end of the period, which may also impact output expectations. In addition, a delayed monsoon season in India, a country which tends to oscillate between a net consumer and a net exporter of sugar, may also impact sugarcane production. If dry conditions persist in India, then there may be less sugar supplies available for trade.

Economic indicators seem to be losing some momentum, adding to the evidence that the ongoing trade conflict between the US and China has impacted growth expectations broadly. In the US, unemployment remained at 3.6% in May. However, the US Purchasing Manager's Index reading weakened to 50.5 in May. A reading below 50 would indicate a contraction. The same reading for the Eurozone fell to 47.7, potentially threatening the region's job market as its manufacturing industry was impacted by reduced factory activity. China's Caixin/Markit Manufacturing PMI reading remained at 50.2 for May as well, as exports fell. In response to these data points, central banks prepared to potentially take action. The Fed announced it was prepared to cut short-term interest rates, with two to three rate hikes priced in this year as of the end of the period. ECB President Mario Draghi announced the central bank will consider cutting interest rates in the near future in an effort to counteract an economic slowdown. China may also implement more stimulus measures in an attempt to reduce the pace of the weakening following special bond issues released earlier in June. As central banks continue to adjust policies to accommodate growth in the latter stages of an expansionary cycle or even in early contractionary periods, the appeal of commodities as an asset class is increased as a business cycle diversifier.

Bloomberg Commodity Index TR Performance through June 30, 2019

	Weight as of Quarter End	QTD Total Returns
Energy	31.23%	-4.56%
Agriculture	29.41%	4.50%
Livestock	5.51%	-11.01%
Industrial Metals	17.32%	-7.23%
Precious Metals	16.53%	7.15%
BCOM Index Total Return	**100.00%**	**-1.19%**

Sources: Credit Suisse Asset Management, LLC, Bloomberg

Performance Notes:
The Bloomberg Commodity Index Total Return is a composite index of commodity sector returns, representing an unleveraged, long-only investment in commodity futures that is broadly diversified across the spectrum of commodities. The returns are calculated on a fully-collateralized basis with full reinvestment. Excess return reflects relative performance versus the benchmark (+/-).
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