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## Investors Abandoning Copper, Cotton, Crude

By **JERRY A. DICOLO**

The commodities market is shrinking.

Amid plunging prices and soaring volatility, investors and traders reduced bets on 13 key commodity contracts by 19% in 2011, according to a Wall Street Journal/Dow Jones Newswires analysis of U.S. Commodity Futures Trading Commission data. The data show so-called open interest, or the number of futures and options contracts outstanding in each commodity.

### Rush for the Exits

Outstanding contracts to buy or sell 13 key commodities declined last year.



Source: U.S. Commodity Futures Trading Commission  
The Wall Street Journal

The exodus was the biggest in at least 12 years, outpacing the flight seen in 2008 during the financial crisis, the data show. And it came from a range of commodities—from crude oil to copper to cotton.

Investors of all stripes bolted for the exits, including hedge funds and producers and consumers of raw materials. Index funds and other investment products often used by retail investors also showed outflows in the last months of the year, according to Barclays Capital.

The price swings of 2011, led by worries about Europe's debt troubles and fears China would slam the brakes on its economy, have cast doubts about whether the decadelong commodities rally can continue. Investors had flocked to the commodities markets, chasing gains driven by growing developed and emerging economies. Small investors were also able to join the game, as commodity-focused mutual funds and exchange-traded funds sprang up.

"Commodities were a one-way bet," said Rich Saultanian, co-president of NUS Consulting Group,

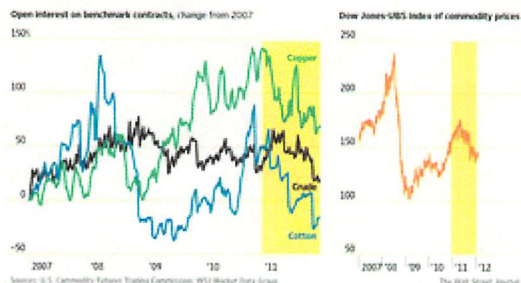
which helps companies manage their energy costs through hedging. He says clients dialed back hedging activities in 2011 after years of oil- and energy-price swings, and that many are skeptical that hedging their future needs is a safe bet: "It's not so simple any longer."

Open interest in 13 key commodities dropped to 8.7 million contracts at the end of last year, from 10.7 million contracts at the end of 2010, according to the data.

The collapse of commodity-trading firm MF Global Holdings in October also likely contributed to the decline, analysts say, as positions held by MF customers were liquidated.

#### Anatomy of a Fall

Outstanding contracts to buy or sell commodities, including crude oil, cotton and copper, shrank in 2011 amid price volatility and widespread declines.



While there is no direct link between market activity and prices, declines in open interest have previously preceded the end of a price surge. In 2011, prices of oil, copper and cotton dropped after open interest peaked. And, even though commodities broadly rose Thursday, the data show prices typically don't have a sustained rebound until open interest halts its declines.

John Hummel, chief investment officer of AIS Futures Management in Wilton, Conn., which manages \$400 million in assets, cut the size of his commodities wagers in half over the past few months, after his computer algorithm told him the market was getting too risky.

"Some of the statistics on commodities suggest there is an extreme level of pessimism and disinterest," Mr. Hummel said. Though he thinks the apathy may suggest prices have reached a bottom and could be set to rise, the sizes of his positions aren't increasing yet.

"That's where we still are until we get a green light to bump it up," Mr. Hummel said, referring to his algorithmic program.

Some analysts say investors could soon step back into the market, especially if the rally that began earlier this month gains momentum.

A resolution to the debt situation in Europe or confirmation U.S. economic growth is accelerating would help reset commodities to a trajectory of rising prices, potentially encouraging investors to get back in the market, said Michael McGlone, senior director of commodities at Standard & Poor's, which operates the S&P GSCI index. "We all know how this will change," Mr. McGlone said. "Once you get something that looks like a substantial trend...then, there will be more interest for longer-term holdings."

CME Group Inc., operator of the main U.S. commodity exchanges, acknowledged the overall use of products to bet on commodities had fallen but said the decline in open interest for benchmark contracts had outpaced that of the broader commodity market.

Natural gas bucked the trend, with open interest growing 24% last year, as investors ramped up bets on lower prices. Other energy markets didn't fare as well. Open interest in crude-oil futures and options fell 29% from March to the end of the year, to 2.2 million contracts, the lowest since May 2007.

In November, futures and options for copper fell to 112,431 contracts, the lowest since June 2009 and 33% below the all-time high hit in December 2010. Cotton fell to a two-year low of 180,303 contracts in November, a 61% drop from its recent high of 459,691 contracts in November 2010.

After an uptick in the beginning of the year, investor flows into commodity-focused ETFs, index funds and certain other products fell \$4.1 billion in the final three quarters of 2011, according to a report by Barclays Capital. That reduced inflows to \$15 billion for the year—the smallest amount since 2002—and well down from the \$67 billion of 2010 and \$77.1 billion in 2009.

Investors pulled \$14.4 billion from commodity index funds alone, Barclays said.

"We believe commodity investment flows will rebound in 2012, but will not go back to the very high levels reached in 2009-10," the Barclays analysts wrote.

Some investors are still reeling from 2011 and may take a while to return to the market, said Tim Evans, an analyst at Citi Futures Perspective in New York. "When you look at the price volatility here, that can chew traders up," Mr. Evans said. "After a while, you get the idea that you should cut down on the total size of your position, or maybe you should trade elsewhere."

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