



FLASH REPORT: GLOBAL RESOURCES

Portfolio Update

Natural resource related investments rallied sharply in May. While there are few signs of a meaningful global economic recovery, there are continuing indications that the worst may be behind us. As a result, markets are rallying on “less bad news.” This is not necessarily a case of excess optimism, rather an acknowledgement that last year’s sharp decline in resource investments was, to some extent, due to panic selling by global investors. At some point, financial markets generally, and natural resource markets in particular, will need some true good news to sustain any rally.

The one spot of true economic acceleration continues to be China. It is the only economy that is growing. Like most emerging markets, China uses more natural resources per unit of GDP than developed markets. So any report of increased economic activity boosts commodity prices. All commodity imports to China, especially base metals, have rebounded from the lows of the winter.

The most interesting news lately has been in the oil markets. Oil is a perfect bellwether for commodities; it is basically global (with modest differences for regional grades and markets) and used in all countries for transportation fuel. Crude oil rose almost 30% in May and is now up 49% for the year. The primary way to invest in oil is by trading oil futures.

Commodity investors and commodity index funds should be doing great, a real source of return when the major equity indices are still struggling to maintain positive performance for the year. However, this has not been the case. Even though oil prices are up almost 50% for the year through May 31, products linked to oil futures are only up marginally. OIL, the index linked note to the Goldman Sachs Crude Oil Index, is only up 3.1% this year. See Table 1.

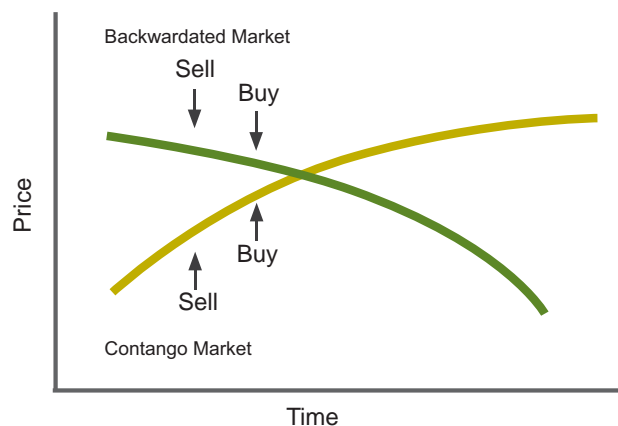
TABLE 1: OIL SPOT VS. OIL FUTURES

	YTD
Cushing Crude Oil Spot Price	48.68
Dow Jones AIG Crude Oil	-1.59
S&P GSCI Crude Oil Return Index	3.14

Source: Bloomberg; to 5/31/09

What could account for this incredible discrepancy between spot prices (those that we see on TV and in the papers) and the actual return to investors? The shape of the futures curve – its *term structure* to be more formal – specifically the phenomenon called *contango*, when prices for a commodity are higher in the future than current spot or nearby contracts. Contango, and the opposite condition (*backwardation*) are represented in Chart 1. When markets are in contango, there is a constant headwind on futures traders, who must effectively sell contracts when they expire and then rebuy them at higher prices. This rolling of a

CHART 1: CONTANGO AND BACKWARDATED MARKETS



contract represents a gain in the price of oil, but it does not translate into a return for investors¹. Markets in contango do not automatically cause investors to lose money. However the gain in spot prices will be reduced by the degree future prices exceed current ones. Commodity related stocks are not impacted by contango, though this is no guarantee that they will outperform spot market prices.

Newgate's Portfolio still has less than 40% allocated to energy stocks. We have increased allocations in exploration and production industries, purchasing several new positions. Generally all energy stocks rose in May, with the servicing and drilling sector having the best performance, up over 17% during the month.

Base metals prices such as copper and zinc rose in May and have had double digit returns year to date. Aluminum is the exception, with prices down due to global oversupply. Mining companies had high returns, with the HSBC Global Mining Index

up 18.3% and the S&P 500 Steel Index up 11.8%. We reduced positions in many base metals companies, selling into the recent strength. Steel is now 5.3%, down from over 10% a few months ago. We also have 5% allocated to transportation companies, both shipping and rail, that forecast some strength coming back into the global economy. Valuations in this sector have increased along with prices, and we may need to see earning increases before becoming more bullish.

The sector with the greatest return in May was agriculture. Coffee, wheat and soy futures were all up double digits in May. Agriculture, with a focus on fertilizers, represents over 20% of the Portfolio. We also own seed companies and have reintroduced the livestock related ETNs to the Portfolio. We believe that this sector has both safety (agriculture is less economically sensitive) and growth (population is rising) characteristics. ♦

¹Newgate published a report on the impact of contango, available on our website, www.newgatecapital.com.

Any opinions expressed are subject to change without notice, and any statements of fact have been obtained from, or are based on, sources considered reliable, but no representation is made by Newgate as to their completeness or accuracy. There is no assurance that estimates/forecasts will be realized. The indexes are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. This material does not constitute investment advice and should not be viewed as a current or past recommendation or a solicitation of an offer to buy or sell any securities or to adopt any investment strategy. Investing entails risks, including possible loss of principal. Past performance is no guarantee of future results. To the extent the investments depicted herein represent international securities, you should be aware that there may be additional risks associated with international investing involving foreign economic, political, monetary and/or legal factors. International investing may not be for everyone. These risks may be magnified in emerging markets. © 2009 Newgate Capital Management LLC