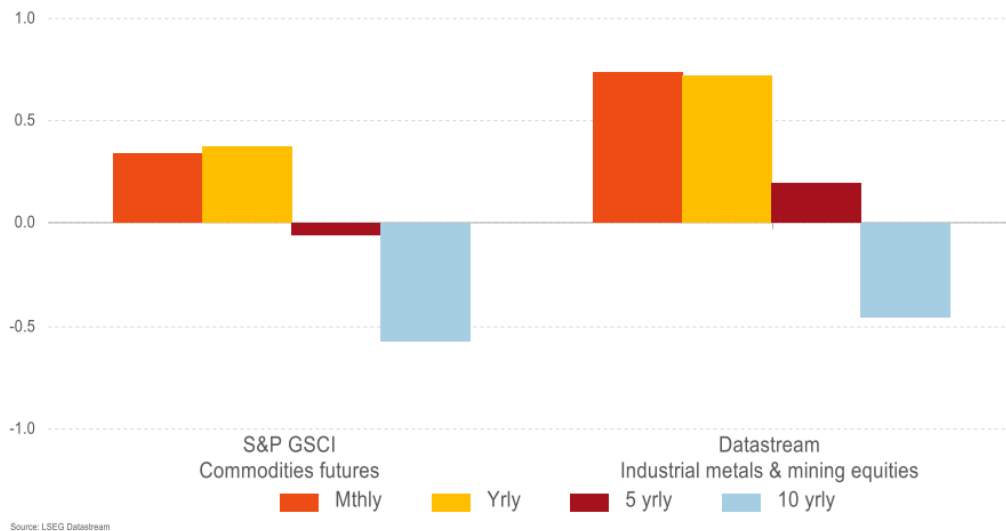


## Why now is the time to consider commodities

Commodities have a key role to play in portfolios given their performance is linked to geopolitical developments, decarbonisation, inflation and currency movements.

“The primary key reason is the diversification benefits,” said Chris Trevillyan, Director Investment Strategy, Frontier Advisors, pointing to the way commodities are often negatively correlated with the US dollar and equities.

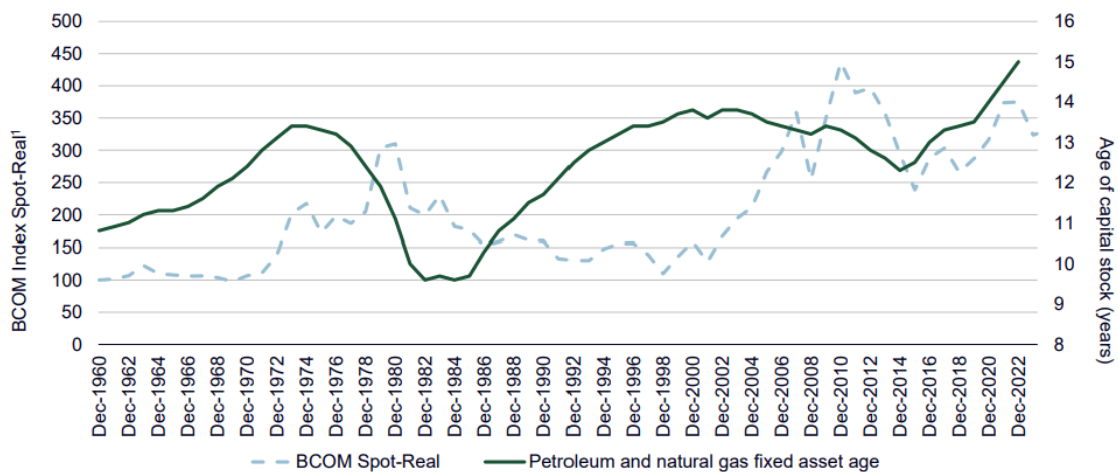
Correlations MSCI World versus commodities 2000 to 2024



The commodities cycle may be entering a new investment phase although the index is also volatile and moves through long cycles, which means investors “need to be nimble but you need to be prepared in advance to be able to be nimble,” according to Trevillyan.

### The commodities cycle

We believe we are entering an investment phase



1 Indexed to 100 December 30, 1960. BCOM = Bloomberg Commodity Index.  
Source :TDAM Estimates, Bloomberg Finance L.P., Bureau of Economic Analysis. As of March 29, 2024.

Canadian-based Hussein Allidina, Managing Director, Head of Commodities at TD Asset Management said commodities also played a role in portfolios when inflation was strong.

“The performance of that portfolio in environments where inflation is volatile and elevated, tends to be negative,” Allidina said. “By introducing commodities, the derivative, into your portfolio – you don’t need a material allocation because the beta or the responsiveness to inflation is higher than what you would get from many other asset classes.”

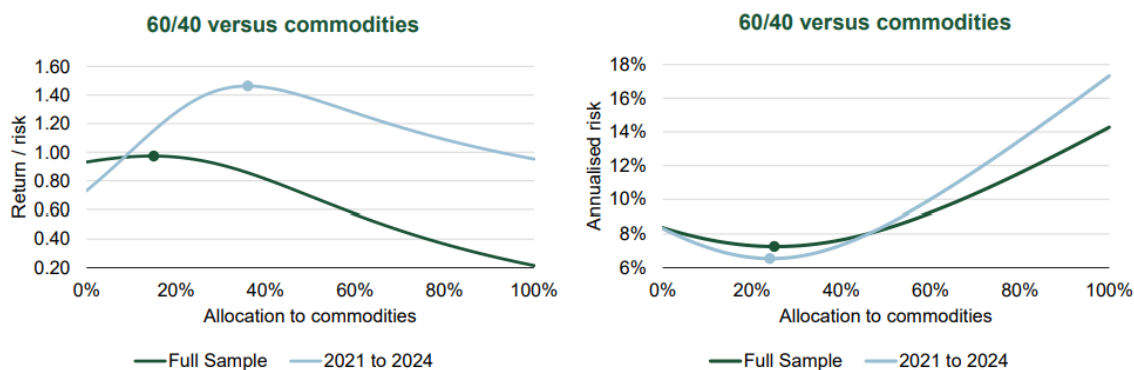
It was one reason why the Ontario Teachers’ Pension Plan – where Allidina previously worked – made its first allocation to commodities in the late-1990s.

“Their perspective was, we have this allocation because in certain macro environments, most of everything else we own underperforms,” he said. From 2013-2020 that ‘insurance’ was expensive, but in 2020-2021 it paid off.

“If you’re making a strategic allocation to commodities, timing it is difficult and if you have that steady allocation through time, the data shows that it pays off.”

### Allocating to commodities is additive

#### Adding 5% to commodities within a Balanced Portfolio adds to return and lowers volatility



Source: Bloomberg, MSCI, TDAM. Data from Jan-1978 to Apr-2024. Equities are represented by 50% S&P/ASX 300 Index, 25% MSCI World ex Australia Index (Unhedged), and 25% MSCI World ex Australia Index (Hedged to AUD). Bonds are represented by 40% Bloomberg AusBond Composite 0+ Yr Index, 40% Bloomberg Global Agg Index (Hedged to AUD), and 20% Bloomberg Australia Bank Bill Index. Commodities are represented by the Bloomberg Commodity Index (AUD). The risk-free rate used for the calculation of the Sharpe ratio is represented by the Bloomberg Australian Bank Bill Index. The markers represent the optimal allocation to commodities. Each portfolio is rebalanced quarterly with no transaction cost. The allocation to commodities is sourced pro rata from equities and bonds. The 60/40 portfolio is comprised of 60% equities and 40% bonds and is rebalanced quarterly. Constant volatility portfolios are scaled to match the volatility level of the 60/40 over the same period. Inflation beta is calculated by regressing quarterly asset returns on quarterly changes in seasonally-adjusted YoY inflation.

Commodities are also strongly related to the net zero 2050 energy transition. The energy sector comprises 58.5 per cent of the S&P GSCI commodities futures index followed by agriculture (18.7 per cent) and livestock (10.5 per cent), industrial metals (7.7 per cent) and precious metals (4.7 per cent).

Jennifer Wu, Managing Director – Global Head of Sustainable Investing, based in JP Morgan Asset Management’s UK Office said commodities were critical in the transition to net zero. Renewable energies such as solar, wind, hydro, and batteries will require minerals such as copper, aluminium, lithium, cobalt, nickel, and graphite.

“We’re looking at a transformative opportunity – we cannot get to net zero without these minerals. But how to invest when and where is going to be a balancing act because of some of the risks.”

Lithium mining has raised issues about [environmental damage](#) in countries such as Chile and Argentina. [Amnesty International](#) has raised human rights issues with cobalt mining practices in the Democratic Republic of Congo, which produces more than two-thirds of the world’s supply.

**At a time when a range of factors, from technological advancement to significant geopolitical upheaval, are impacting markets across the world, investors are naturally re-thinking their approach to traditional sectors and asset allocations. Get in touch with Frontier’s Capital Markets and Asset Allocation Team to learn more about our analysis.**