

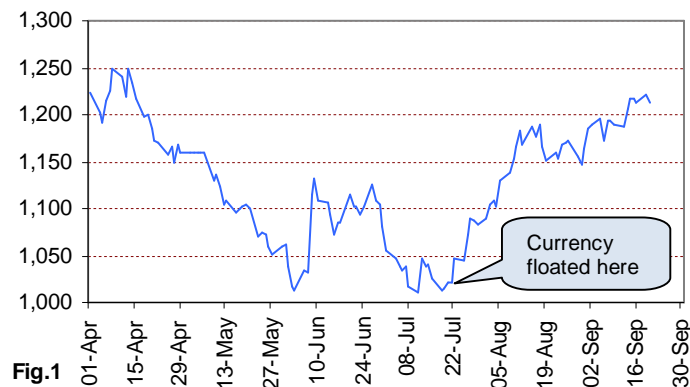


THOUGHTS ON LONG-ONLY COMMODITY INVESTING – Part 2 – SEPTEMBER 2005

You may recall that on 21st April this year, we published our views on passive, long-only investing in the commodity markets. In our note, we outlined our concerns on the Chinese economy, our concerns that many investors were focusing on accessing commodity markets via commodity indices, our concerns on the extent of asset allocation into commodity futures (open interest), and our fears of a short-medium term severe price retracement. Five months later, we thought it might be worthwhile to see how markets have performed.

CHINA

Our previous report highlighted the poor performance of the Shanghai stock market, and mentioned various anecdotal “man on the ground” comments regarding the true state of the economy. In our view, this underlying weakness seemed at odds with the rampant bullishness of many market commentators, who viewed China increasingly as “buyer of the last resort” of commodity markets.



Notwithstanding the abandonment of the currency peg on 21st July, nothing much has changed. After further weakness, the stock market has bounced (see Fig.1). The stock market is currently some 20% off the lows (though only 3% higher than 21st April).

Clearly the currency change appears to have been a catalyst, though whether this heralds a substantial change in sentiment remains to be seen. More technical analysts may conclude that the recent rally has been no more than a “dead cat” bounce off of the triple bottom and psychological number of 1000.

Time of course will tell, but our people on the ground there are no more bullish than they were back in April. Reuters recently (15th Sep) reported that “(The) Chinese government’s cooling measures are reining in growth in demand”. They also noted that “...prices have stayed stubbornly soft this September, normally the season when orders pick up following a summer lull. Traders estimate that this month’s demand ...has fallen as much as 20 percent from a year ago” and “supply remains abundant, supported by unexpectedly high August imports and by increased domestic shipments.” We remain cautious.

OPEN INTEREST

Our previous report indicated that the 14 markets we track were some 800,000 contracts, or 22% over-long (4.4m vs. “fair value” of 3.6m). Notwithstanding the continued rise in open interest in these commodities (to 4.7m), the “over long” position has remained fairly flat at around 23% (900,000 contracts) – see Fig.2.

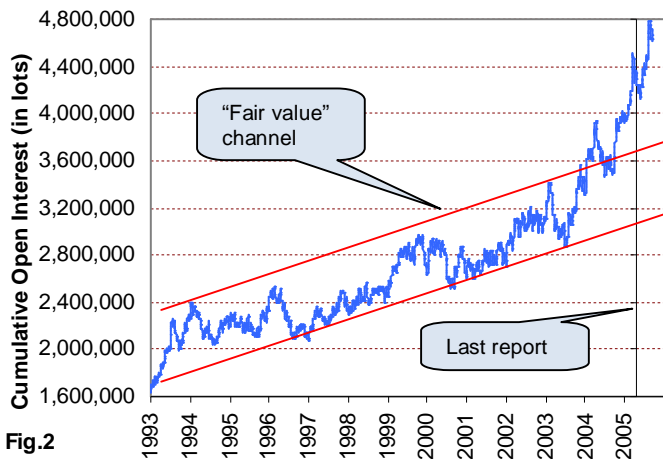


Fig.2

As in our previous report, this rise of some 300,000 contracts has coincided with a rise in the CRB index (see Fig.3), and the correlation here has remained strong at >95%. We interpret this as further evidence of fresh long positions, and we remain concerned that long positions established in recent months are increasingly vulnerable to a short-medium term negative price shock.

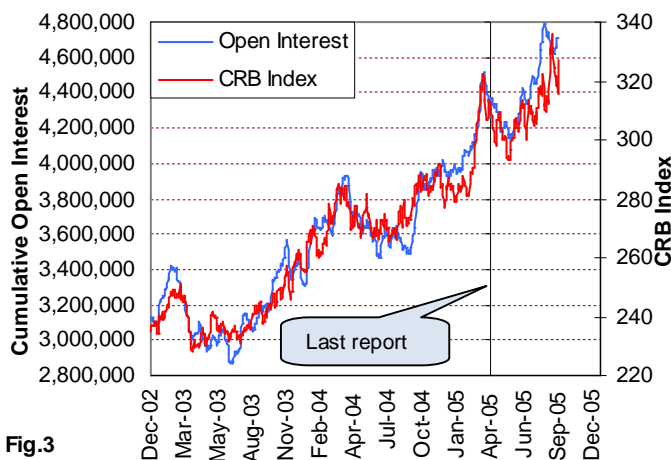


Fig.3

Supporting this, Michael Lewis, global head of commodities research at Deutsche Bank suggested recently (20th September) that those looking to invest in commodity indices

"...may now have missed out on the opportunity".

He also noted that;

"Today is not the best time to go into a traditional commodity index".

ANALYST FORECASTS

In our last report, we showed high, low and mean price forecasts by a variety of market analysts. These forecasts are compiled and published annually by Reuters. The table below shows initial forecasts and subsequent accuracy levels for the year to date:

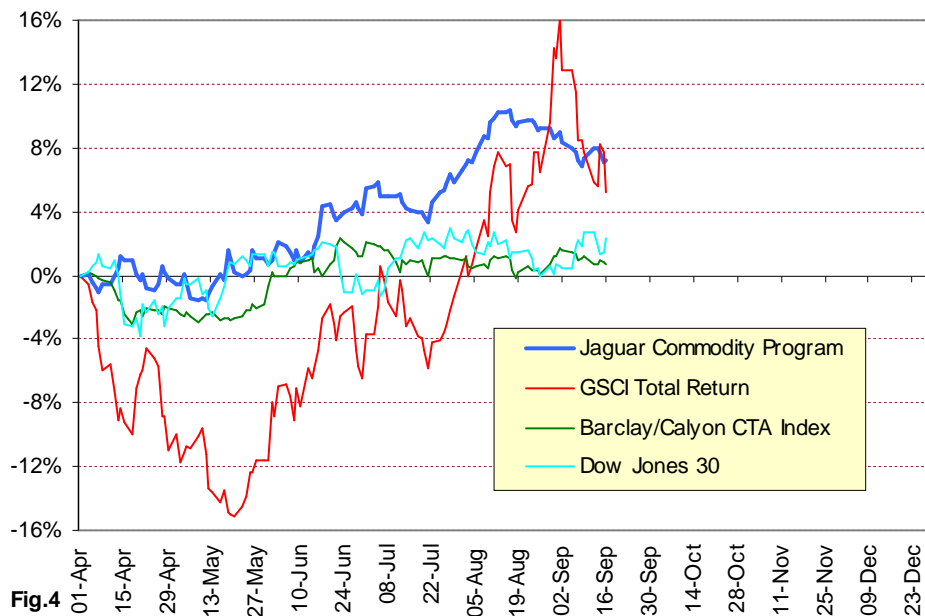
2005 FORECASTS	CLOSE 2004	MEAN	FORECAST	ACTUAL *	CHANGE	MARGIN OF ERROR
COPPER	3,280	2,729	-17%	3,456	+5%	22%
ALUMINIUM	1,964	1,779	-9%	1,839	-6%	3%
NICKEL	15,205	13,027	-14%	15,525	+2%	16%
ZINC	1,270	1,177	-7%	1,290	+2%	9%
LEAD	1,056	842	-20%	951	-10%	10%
TIN	7,765	8,062	+4%	7,738	0%	4%
GOLD	438	434	-1%	430	-2%	1%
SILVER	6.82	6.56	-4%	7.05	+3%	7%
CRUDE	43.45	45.12	+4%	55.10	+27%	23%
			-7%		+2%	11%

*ACTUAL prices are; LME=average cash, PRECIOUS=average LBMA fixes, Crude=average front month NYMEX WTI

Clearly this year has proved a little turbulent, with prices to date averaging significantly higher than forecast. Notwithstanding unforeseen events (Hurricane Katrina, inconclusive elections in Germany etc), it seems as though many have got this year wrong with forecasts being almost entirely too pessimistic (the exception being tin). We find it difficult to believe that all of these analysts can be so wrong on a fundamental analysis basis – and we believe that their error has instead been in under-estimating the huge wave of investment in commodity indices. In our view this confirms that recent price action has been driven by speculative elements rather than fundamentals.

CONCLUSION

In the last five months, markets have fallen back and subsequently made new highs as fresh waves of speculative/investment cash have continued to crash on the shores of Commodity Island. Open interest has continued to rise. China remains at the forefront of most demand conversations. Yet the fears that we outlined back in April remain, and if anything have grown. While we acknowledge that the supply situation is uncertain in some sectors (metals and energy), we remain more fearful that the demand situation is seriously worse than estimated, and deteriorating. So we reiterate our belief that investments in commodities should not rest SOLELY in long-only index products, but should instead be (at least partially) diversified among actively managed programs. Nevertheless, Fig.4 below demonstrates that an investment in our Commodity Trading Program would have yielded a higher return than that of an investment in the GSCI Total Return Index, and would have substantially outperformed the Barclay/Calyon CTA Index;



PERFORMANCE ANALYSIS –			
Jaguar Commodity Trading Program vs. Goldman Sachs Commodity Total Return Index vs. Barclay/Calyon CTA Index vs. Dow Jones Industrial Average			
1 st April to 16 th September 2005			
	Return	Volatility (30d)	Max.Draw (Daily)
Jaguar Commodity	= +7.22%	6.67%	-3.15%
GSCI Total Return	= +5.24%	29.03%	-15.09%
Barclay/Calyon CTA Index	= +0.64%	5.40%	-3.32%
Dow Jones 30	= +2.28%	9.33%	-5.06%