Investment Management Perspectives

Reflecting on the Decade's Worst Investment

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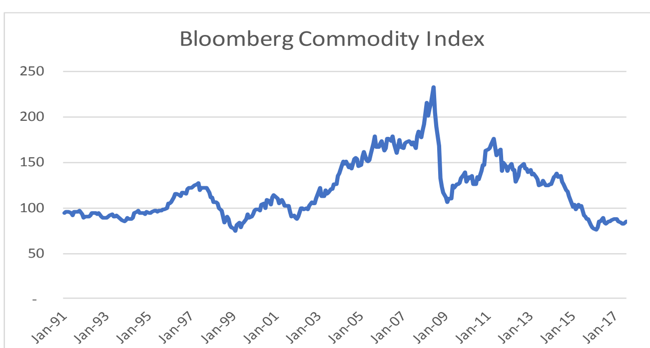
What is one of the worst investments you could have made 10 years ago? The first rumblings of the financial crisis started in August 2007 with BNP Paribas suspending withdrawals from three money market funds. Over the next 18 months the entire global financial system came close to collapsing. It is estimated that wealth[1] in the United States alone declined by 22% (around $14 trillion[2]).

What is your guess?[3] Las Vegas real estate? You would still be down 25%. How about a financial stock ETF with a large weighting to the bailed-out banks? You would have made 12%. Or maybe an index tracking stocks of homebuilders? You would have made a surprising 71%. Nope, the worst performing investment we found (by a wide margin) was commodities.[4] If you invested in commodities 10 years ago, your investment would still be down 50% today.

	Aug. '07 - Aug. 17	
Asset Class or Index	Cumulative Return	Value of $100
Bloomberg Commodity Index	-50.2%	$49.84
Case Shiller Las Vegas Home	-25.3%	$74.66
Case Shiller NYC Home	-8.9%	$91.06
Financial Select Sector SPDR Fund	12.3%	$112.29
iShares MSCI Emerging Markets ETF	18.5%	$118.53
iShares Core U.S. Aggregate Bond ETF	50.4%	$150.42
SPDR S&P Homebuilders ETF	70.9%	$170.87
iShares iBoxx $ High Yield Corporate Bond ETF	75.3%	$175.27
SPDR Gold Trust	81.9%	$181.87
iShares Russell 2000 ETF	101.7%	$201.67
SPDR S&P 500 ETF Trust	105.9%	$205.86

What made commodities such a terrible investment for the past 10 years? A lot of it was the relatively high starting price. The chart below shows the index over the past 30 years.

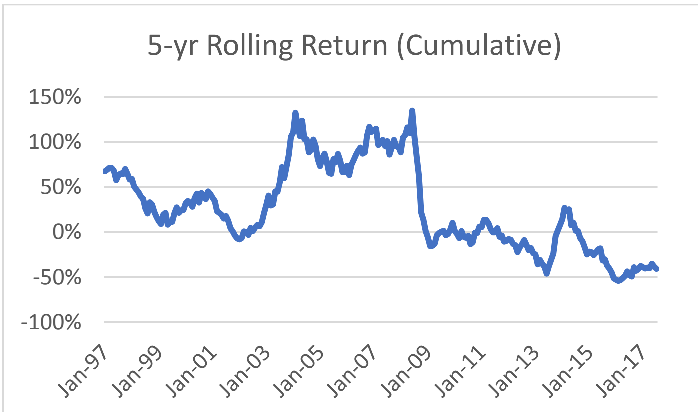


[1] Includes homes as well as financial assets like stocks and bonds.
[2] "The global financial crisis and American wealth accumulation" John Makin 2013 & "The Crisis of Wealth Destruction" Roosevelt Institute 2010 & "IMF Survey: Households Hit Hard by Wealth Losses" Petya Brooks 2009
[3] One caveat is that we are only tracking investments that you could have made in 2007 that are still trading today. Probably the correct answer for the worst investment you could have made would be subprime mortgage bonds.
[4] For assets that pay interest or dividends we assume reinvestment of those dividends.

In August 2007 the index was at one of its highest levels ever. Stories were being written about the coming shortage of commodities. Investment into new sources of supply was very high. There is a saying regarding commodities: high prices will cure high prices. End users adjust and producers make investments so that the price level eventually reverts to more normal levels with time.

From the elevated level in August 2007, the index briefly spiked but fell sharply and bottomed in February 2009 (along with almost every other financial asset). From this low, the index had a strong rally (along with most other assets) but in April 2011 commodity prices decoupled from equities and other financial assets and began what is now a six-year bear market. It is not unusual for commodities to behave differently than stocks (or bonds). Since 1991, the correlation between commodities and stocks has been 0.3 and for bonds 0.0.

What is unusual is the extended period that commodities have been a bad investment. The current level of the index matches the lows of the late 1990s and the 5-year rolling returns from investing in commodities is one of the worst in the past two decades.



We have no insight as to the 'appropriate' level for commodity prices but it wouldn't surprise us if we see a positive reversion over the next five years.

Graph Source: FactSet 2017

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