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Last week's S&P 500 Index: +4.3%

Super cycle

Key takeaways

- We believe commodities began a new bull super cycle in March 2020.
- The recent pullback has given us an opportunity to upgrade commodities to favorable from neutral.

What makes the world economy go round? Commodities. Think about it. Every day consumers use commodity products. Putting gasoline in your car? How about stopping by the grocery store to find something to prepare for dinner tonight? Most of us turn to a variety of commodities on a daily basis for survival. The prices of oil and agricultural products might be set by the global markets, but we feel the effects of shortages or surpluses right in our own backyards (and wallets).

Consumers know the price of oil, and, therefore, gasoline, has skyrocketed since the depths of the COVID pandemic in March 2020. The same thing has happened with prices at the grocery store for beef, chicken, and grain-based products. The prices of many other commodities including industrial metals like copper, aluminum, and iron ore have also risen dramatically over the last two years. As a result, the Bloomberg Commodity Index (BCOM), our preferred commodity price gauge, surged 130% from March 2020 into early June 2022. We held a favorable rating on commodities for the two years ending in March 2022 but reduced positions as we felt prices had become extended.

We have written often in this weekly piece, especially since the pandemic lows in the equity market, about seeking potential opportunities that arise during periods of uncertainty and downdrafts in the markets. We often encourage longer-term investors to seek opportunities during market corrections. From mid-June through mid-July, the BCOM pulled back nearly 18%. We feel this pullback offers a buying opportunity. This recent downside reversal represents what we believe to be a consolidation period within a longer-term uptrend. Looking ahead through the current period of economic headwinds and likely a moderate economic recession, we look for the global economy to eventually stabilize and regain some strength should continue to feature commodity supplies that fall short of demand. Even with the recent pullback in gasoline and crude oil demand, prices remain well above year-ago levels. As a result, we have recently upgraded commodities to favorable from neutral.

From a portfolio perspective, we have chosen to increase tactical allocation to commodities by decreasing exposure to large-cap U.S. equities. We continue to hold a most favorable or overweight rating on U.S. large-caps, but given the proximity of the S&P 500 Index to our year-end target range, we feel the upside for large-cap domestic equities is somewhat limited in the near term and a portion of the funds would be better allocated to commodities.

Our longer-term view of commodities remains positive. We believe commodities began a new bull super cycle in March 2020. Commodity bull super cycles are periods of strong commodity performance, often lasting a decade or longer. It is typical for a commodity bull super cycle to experience bouts of falling or consolidating prices while the long-term trend remains higher. We believe the recent pullback in the BCOM represents an opportunity to upgrade our guidance on commodities to favorable, in line with our bull super cycle view.

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Definitions

Bloomberg Commodity Index is comprised of 22 exchange-traded futures on physical commodities and represents 20 commodities weighted to account for economic significance and market liquidity.

S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the US stock market.

An index is unmanaged and not available for direct investment.

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