Opinion: Soybeans are better for you than corn
By Mark Hulbert
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Favor commodities whose spot prices is higher than the next nearby futures

CHAPEL HILL, N.C. (MarketWatch) — Those of you interested in a commodity-trading strategy might consider betting on soybeans over corn in coming months.

That's because the spot soybeans contract is trading for a higher price than comparable contracts expiring in the near future, while just the opposite situation prevails for corn. If these two commodities adhere to the historical pattern, a trader investing in soybean futures will beat the one in corn.

This greater profit would be realized when the contract you hold approaches expiration and you roll it over to the one whose expiration comes next. If that next contract is trading at a lower price, as currently is the case with soybeans, you pocket the difference as profit. But if that contract is trading at a higher price, your so-called “roll return” will be negative.

Sounds too easy, doesn’t it?

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But, historically, roll return has been the source of almost all of the profits from investing in commodities, according to a study that appeared a decade ago in the Financial Analysts Journal: The Tactical and Strategic Value of Commodity Futures, by Campbell Harvey, a Duke University finance professor, and Claude Erb, a former commodities manager at fund manager TCW Group. (The two recently updated that study, with similar results.)

To illustrate the benefit of focusing on roll returns, the researchers constructed a hypothetical portfolio that, each month between July 1992 and May 2004, invested in the six commodities that were then trading most like soybeans is today and shorting the six most like corn currently. This portfolio’s return was 2.6 percentage points per year better than it would have been had it invested equally in all commodities.

Even better, this hypothetical portfolio was 23% less volatile, or risky, than the equally-weighted portfolio. As a result, its risk-adjusted performance was more than four times better.

To be sure, as Prof. Harvey stressed in a recent email, these results reflect an average over many years, and the roll return wasn’t always positive when investing in commodity futures similar to soybeans today (or negative for commodities similar to corn today). So there is no guarantee that you will do well by investing in soybean futures or that you will do better than if you had invested in corn futures.

Another qualification: The pattern the researchers documented applies primarily to futures contracts tied to real assets (such as grains and industrial metals) rather than to financial instruments (like stock market averages, currencies, and even gold). So focus on real assets if you want to try your hand in coming months at basing a commodity trading strategy on various commodities’ term structures.
If you aren’t inclined to trade directly in commodity futures, an alternative is to invest in exchange-traded funds that themselves do so — such as the Tecurium Soybean Fund SOYB, +1.39% and the Tecorium Corn Fund CORN, +0.96% .

One possible trade right now, for example, would be to invest in the soybean ETF while shorting an equal dollar amount of the corn ETF.

That hedge will make money even if soybeans go down, so long as they don’t fall as much as corn does.

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