

PORTFOLIO DIVERSIFICATION OPPORTUNITIES

Futures  
Group



A Case for Managed Futures.



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on-line trading | systems | managed futures | forex



# Managed Futures: Portfolio Diversification Opportunities

## INTRODUCTION

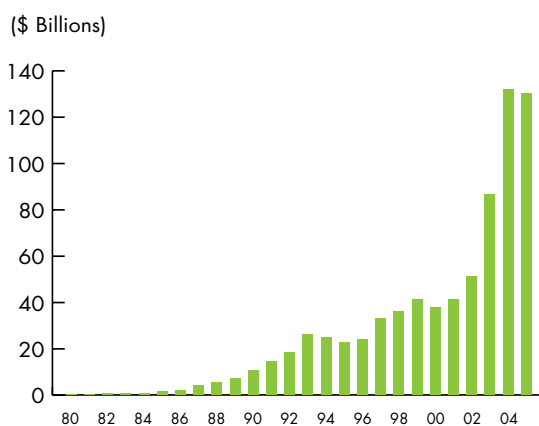
The term managed futures describes an industry made up of professional money managers that manage assets on behalf of their clients. These money managers are referred to as Commodity Trading Advisors, or CTAs. Using the global futures markets, they implement their systems to take positions based on expected profit potential.

Managed futures investments have been used by individual investors for more than 20 years. More recently, institutional investors such as pension funds, banks, endowments, trusts and family offices have incorporated managed futures as one segment of a well-diversified portfolio.

As an asset class, managed futures is increasingly being recognized as an important investment alternative that may potentially enhance the returns and lower the overall volatility of a diversified investment portfolio.

## GROWTH OF MANAGED FUTURES\*

(January 1980 - December 2005)



\*Source: Barclay Trading Group

## THE VALUE OF DIVERSIFICATION

Today, a variety of academic research and evidence demonstrates the potential benefit of incorporating managed futures to create better balance to a stock and bond portfolio.

The general conclusion is that diversification of non-correlated asset classes, such as the introduction of managed futures to an investment portfolio, can both reduce portfolio risk and enhance overall portfolio performance.

The concept of Modern Portfolio Theory, introduced by Nobel Prize-Winning economist Harry Markowitz in 1952, showed how to measure the risk of various securities and how to combine them in a portfolio to get the maximum return for a given risk.

This theory was further advanced by the work of Harvard professor Dr. John Lintner in 1983 who concluded, "...The combined portfolios of stocks (or stocks and bonds) after including judicious investments in appropriately selected sub-portfolios of investments in managed futures accounts...show substantially less risk at every possible level of expected return than portfolios of stocks (or stocks and bonds) alone".

## A WORD ABOUT RISK

Futures investments are speculative, do involve a high degree of risk and are not suitable for everyone. An investor can potentially lose more than their initial investment in individually managed accounts. Certain managed futures accounts or funds may be leveraged, and performance can be volatile. In addition, managed futures accounts or funds may be subject to substantial fees. Before considering any investment, investors should always obtain and read thoroughly the appropriate disclosure document or offering memorandum for additional information on the risks associated with this type of investment.

# The Concept of Non-Correlation

## NON-CORRELATION

Although trading in futures may be highly volatile and risky, adding managed futures as a component to a diversified investment portfolio may actually decrease volatility and increase returns in a portfolio as a whole.

The graph to the right compares the correlations between managed futures, domestic bonds and domestic & international stocks.

## MARKET DIRECTION

Another way to evaluate the relationship between managed futures and stocks is to consider the frequency with which they move, or do not move, in the same direction. Over the period from January, 1980 through December, 2005:

- In nearly 50% of those months managed futures moved in an opposite direction from stocks.
- In 35% of those months both managed futures and stocks posted positive returns.
- In only 17% of those months did both managed futures and stocks move lower.

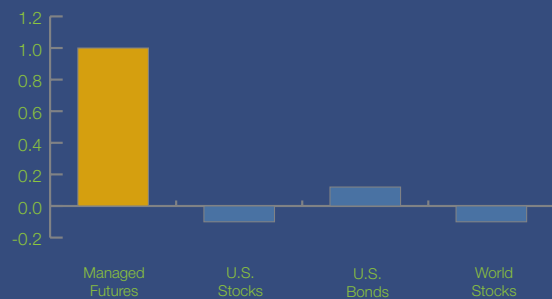
Data:

Managed Futures: CISDM Managed Futures Index; U.S. Stocks: S&P 500 Index; U.S. Bonds: Lehman Brothers Aggregate Bond Index.

Investing in managed futures is speculative, involves a high degree of risk, and is not suitable for all investors. Past performance is not necessarily indicative of future results.

## CORRELATION ANALYSIS

(January, 1980 Through December, 2005)

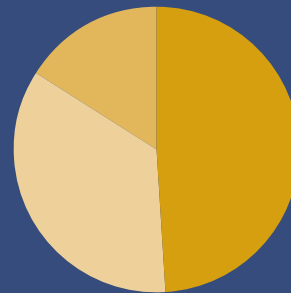


## DIRECTION OF MONTHLY RETURNS

(January, 1980 Through December, 2005)

54 Months = 17%  
Both Down

150 Months = 48%  
Opposite Directions



108 Months = 35%  
Both Up

# The Value of Diversification

## THE ABILITY TO PROFIT IN VIRTUALLY ANY ECONOMIC ENVIRONMENT

In addition to improving overall portfolio returns, managed futures has the ability to perform well in a variety of economic climates, including inflation and periods of down stock markets.

One reason for this is that managed futures trading advisors have the ability to take advantage of price trends in either direction. For example, during periods of inflation, commodities such as gold, silver, oil, and grains tend to do well.

## ACCESS TO GLOBAL MARKETS

The establishment of global futures exchanges allow managed futures trading advisors to diversify their trading systems by participating in over 50 different markets worldwide. These include currencies, stock indices, financials, agricultural products, precious metals, and energy products.

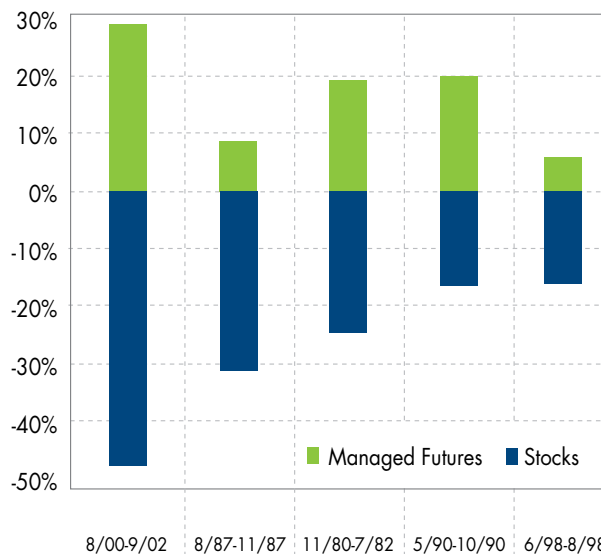
Thus, managed futures trading advisors have a variety of opportunities for profit potential and risk reduction through an array of non-correlated markets.

## MANAGED FUTURES VS. STOCKS DURING STOCK MARKET DRAWDOWNS

(January, 1980 Through December, 2005)

The following chart shows the comparison between the performance of managed futures and stocks during the five worst declines in U.S. Stocks as represented by the S&P 500 Index. This chart demonstrates the historical non-correlation between these two asset classes for the stated period of time.

| Aug. 2000 - Sep. 2002 |                 |                |
|-----------------------|-----------------|----------------|
| S&P 500               | Managed Futures | Net Difference |
| -46.28%               | 28.12%          | <b>74.40%</b>  |
| Aug. 1987 - Nov. 1987 |                 |                |
| S&P 500               | Managed Futures | Net Difference |
| -30.17%               | 8.46%           | <b>38.63%</b>  |
| Nov. 1980 - Jul. 1982 |                 |                |
| S&P 500               | Managed Futures | Net Difference |
| -23.80%               | 18.68%          | <b>42.48%</b>  |
| May 1990 - Oct. 1990  |                 |                |
| S&P 500               | Managed Futures | Net Difference |
| -15.84%               | 19.42%          | <b>35.26%</b>  |
| Jun. 1998 - Aug. 1998 |                 |                |
| S&P 500               | Managed Futures | Net Difference |
| -15.37%               | 5.76%           | <b>21.13%</b>  |



Data:

Managed Futures: CISDM Managed Futures Index; U.S. Stocks: S&P 500 Index; U.S. Bonds: Lehman Brothers Aggregate Bond Index.

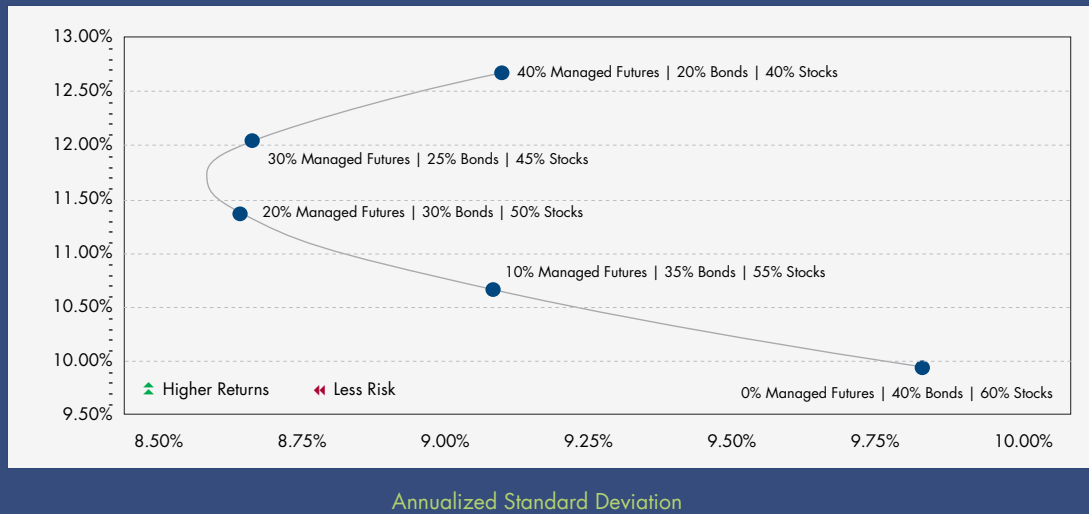
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# Balanced Performance

## THE EFFECT OF DIVERSIFYING A TRADITIONAL PORTFOLIO INTO MANAGED FUTURES

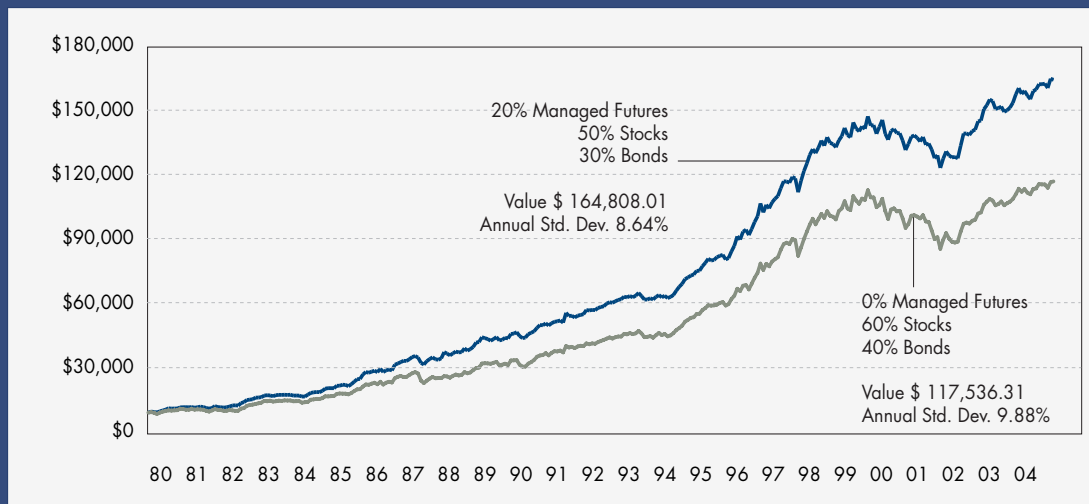
(January, 1980 Through December, 2005)

Compounded Annual Returns



## VALUE OF INITIAL \$10,000 PORTFOLIO VS. A TRADITIONAL STOCK AND BOND PORTFOLIO

(January, 1980 Through December, 2005)



Data:

Managed Futures: CISDM Managed Futures Index; U.S. Stocks: S&P 500 Index; U.S. Bonds: Lehman Brothers Aggregate Bond Index.

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# Summary of Benefits

## **WHO INVESTS IN MANAGED FUTURES**

- Public Pension Funds
- Corporate Pension Funds
- Corporate Treasurers
- Insurance Companies
- Foundations, Endowments and Trusts
- Funds of Funds
- Family Offices
- Proprietary Bank Capital
- Central Banks
- Governments
- Individuals

## **BENEFITS OF MANAGED FUTURES**

- Provides direct exposure to international financial and non-financial asset sectors
- Offers a means to gain exposure to risk and return patterns not easily accessible with investment in traditional stock and bond portfolios
- Reduces portfolio risk
- Ability to profit in different economic environments
- Global Diversification
- Timely Portfolio Diversification
- May be just as profitable during declining stock, bond and real estate investments

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