Irrational Exuberants, Liquidity Providers, or Both?

The Role of Speculators in Futures Markets

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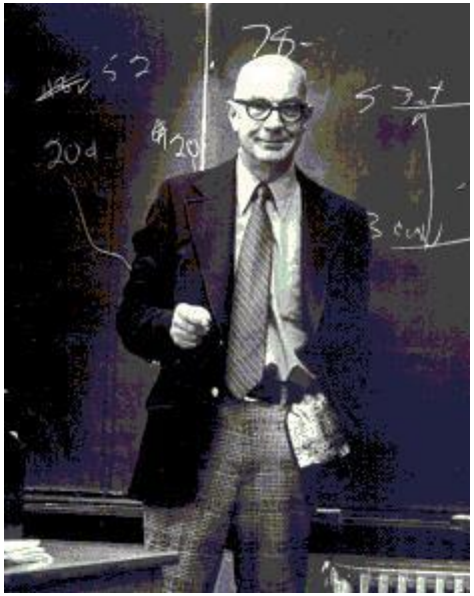
Speculators are Necessary

“The warehousemen are large scale operators who have skill and money. Only the professional speculators are equipped to oppose them; the effective competition in the storage market is provided by the large scale speculators.”

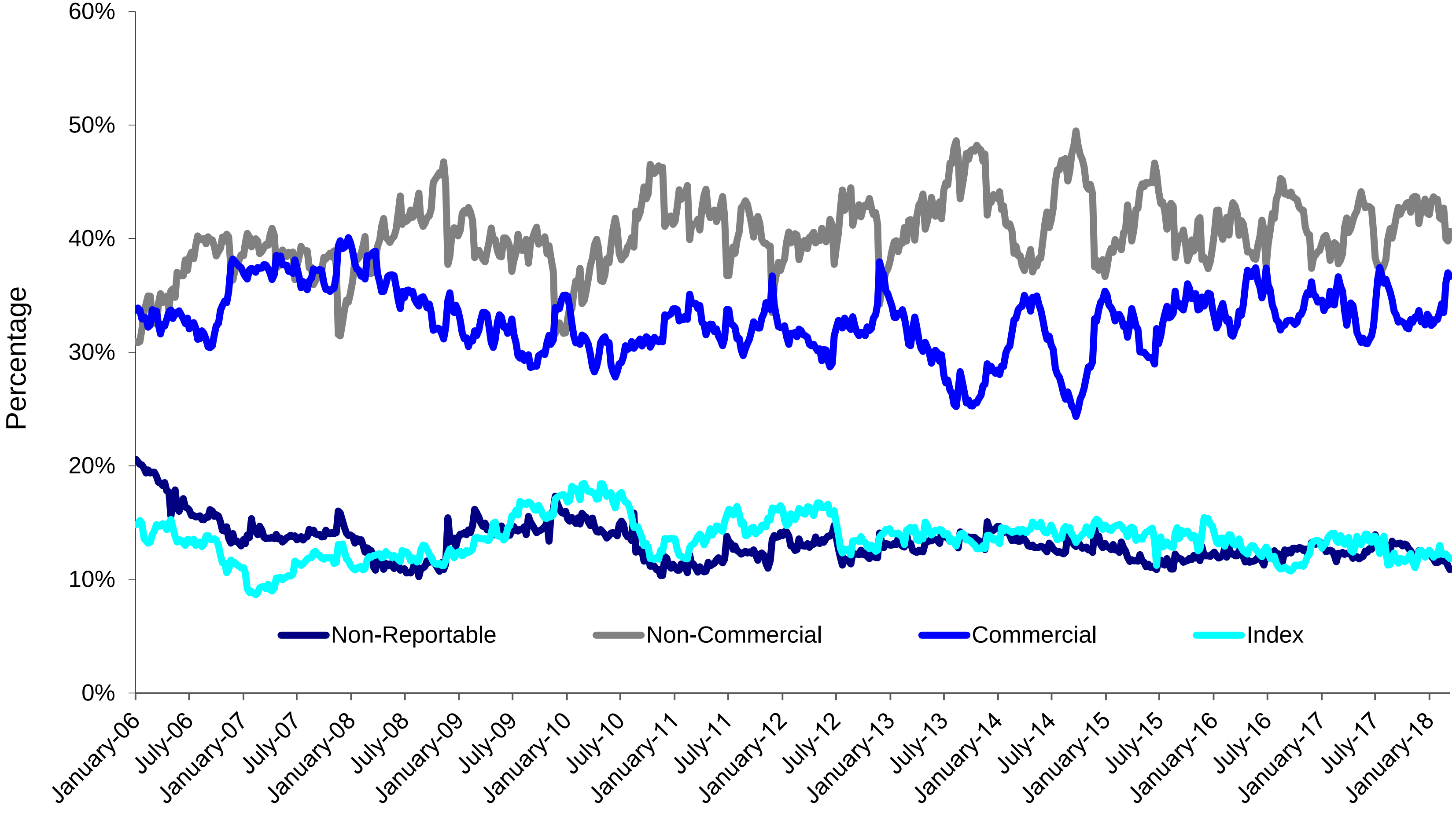
-- **Tom Hieronymus**

The University of Illinois



The Percentage of Open Interest by Category

Breakdown of Corn OI Holders, while Variable, is Range Bound



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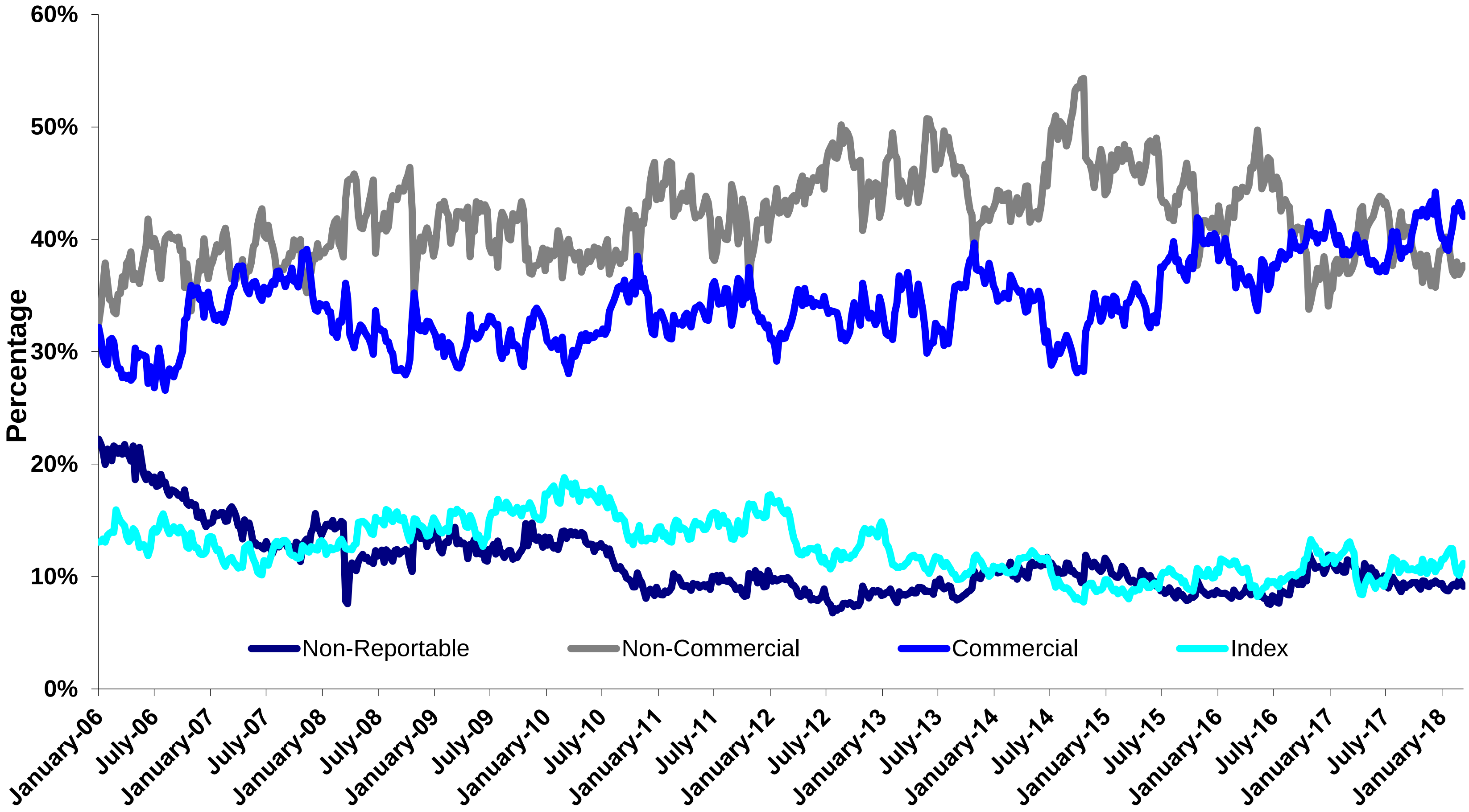
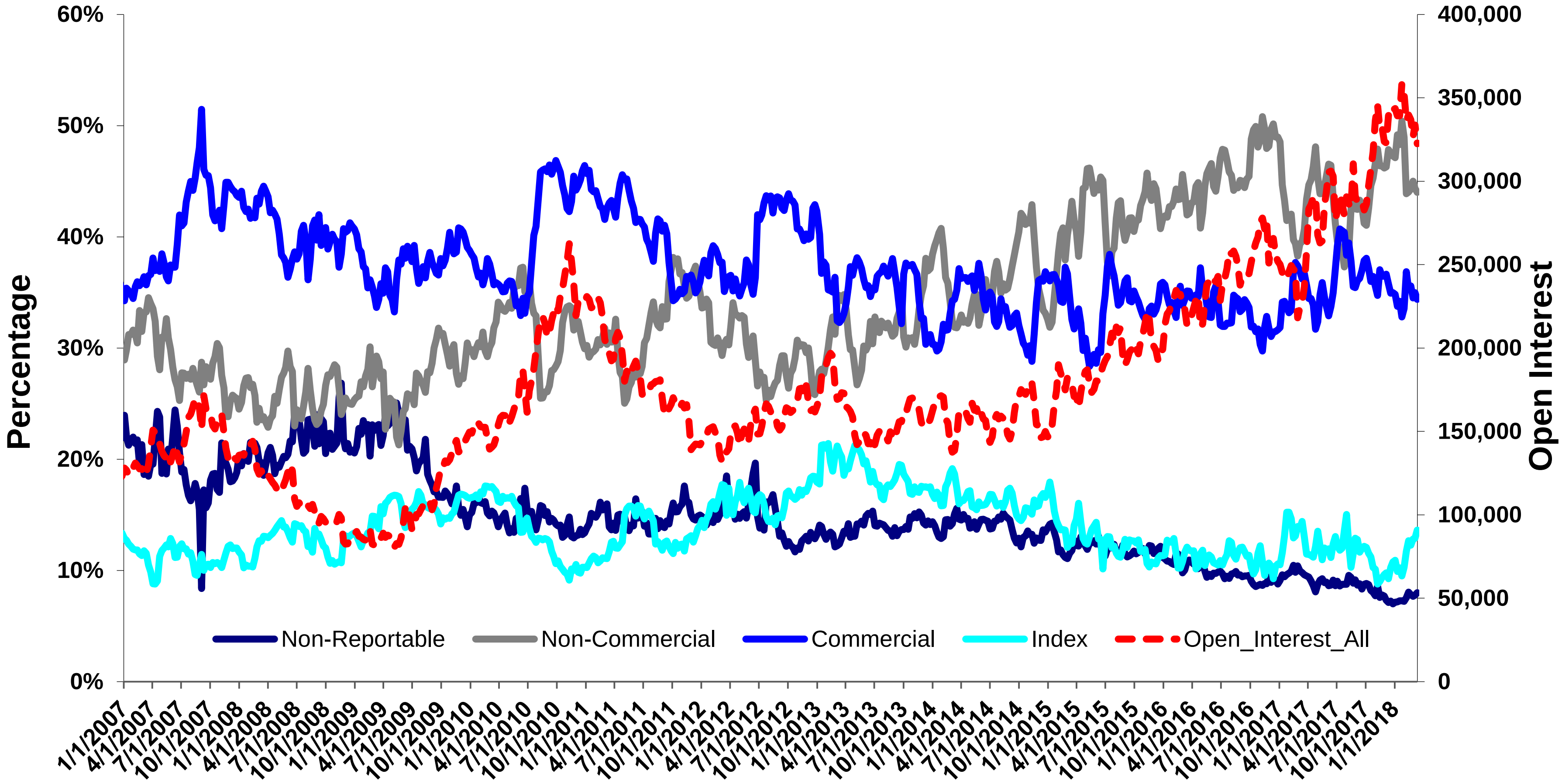
The Percentage of Open Interest by Category

Breakdown of Soybean OI Holders, while Variable, is Range Bound but Tending Commercial



The Percentage of Open Interest by Category

Breakdown of KC Wheat OI Holders, while Variable, Commercials are Range Bound while Non-Commercials are Tending Up at the Expense of Index & Non-Reportable Positions



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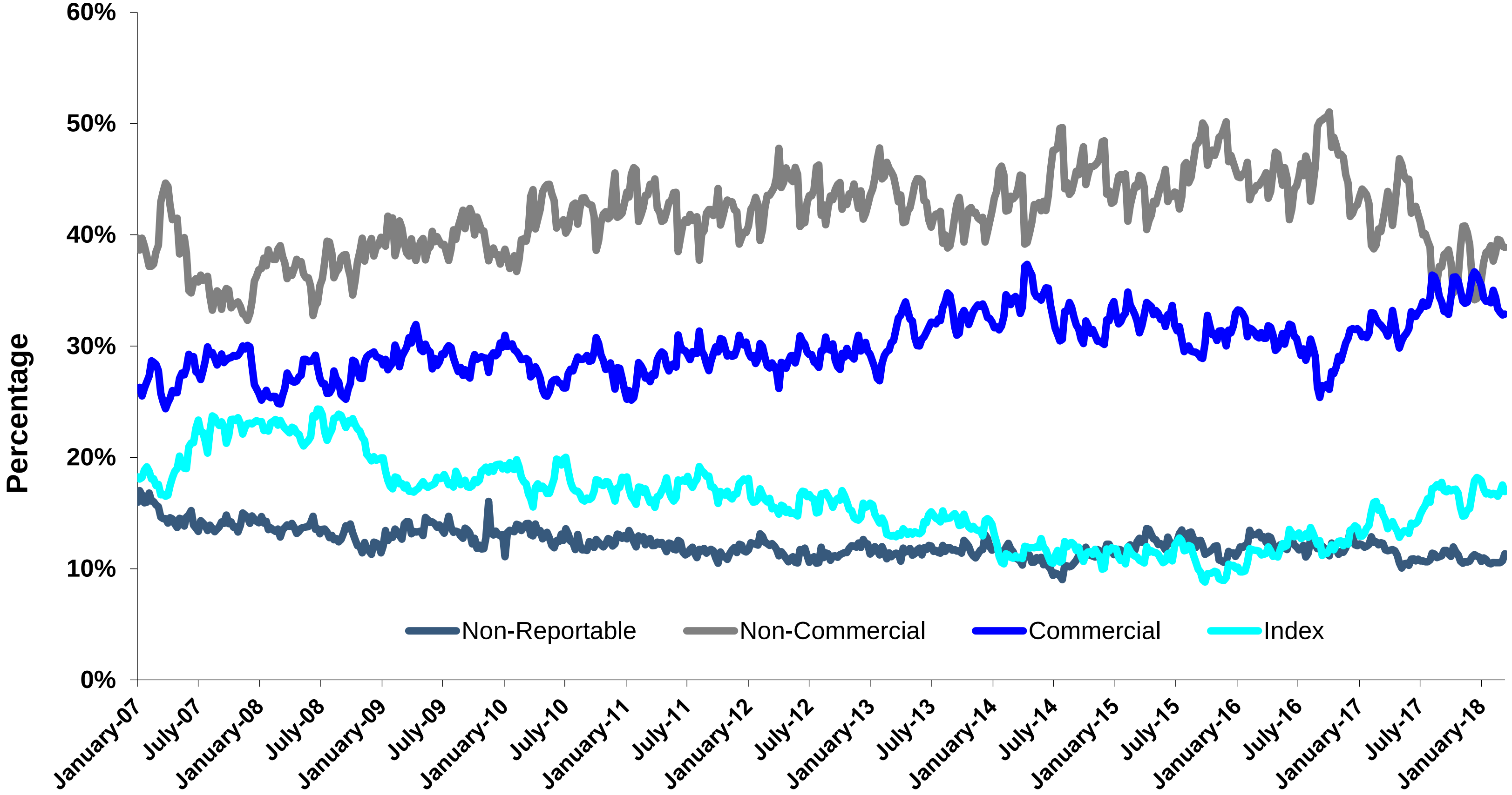
The Percentage of Open Interest by Category

Breakdown of Live Cattle OI Holders, while Variable, Range Bound



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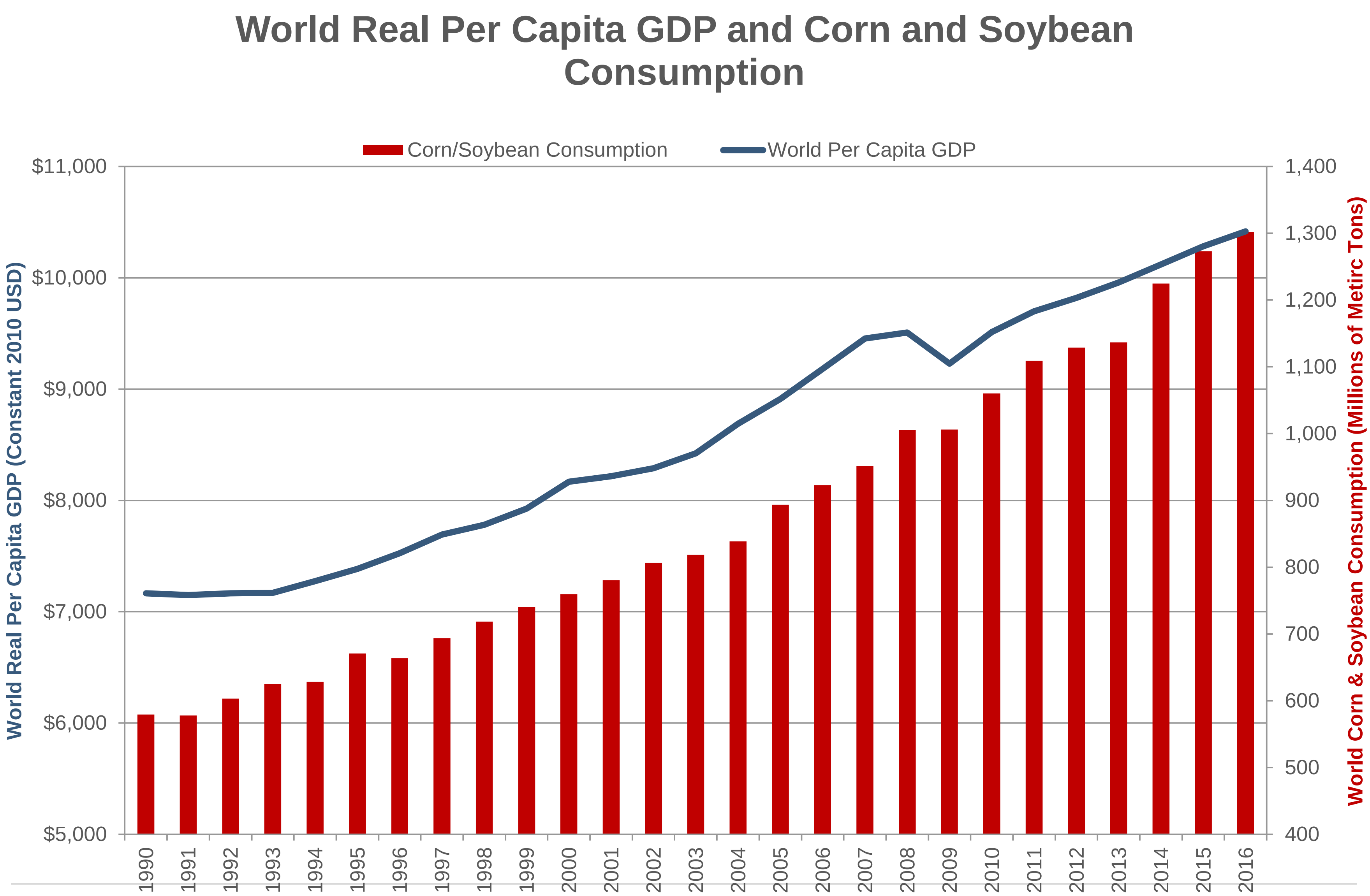
Market Growth from all Participants is to be Expected



Informa Economics Study

Background: This study was commissioned in May, 2008 by the CME Group for the benefit of a consortium of futures exchanges. Work was completed in October, 2008.

Purpose: Analyze data available from the CFTC on large trader reporting to evaluate any index fund or managed money impacts on market liquidity, volatility, price discovery and convergence.

Data: The CFTC provided a subset of information regularly collected for the *Commitments of Traders* report. In addition to the normal categories of traders, the CFTC also identified accounts that are associated primarily with index trading and managed money. The dataset began on January 1, 2005 and ended on June 30, 2008.

General Finding: After a lengthy and detailed analysis of the data provided, Informa found very little evidence that index funds and managed money were routinely detrimental to any of the studied markets. All of the trader groups displayed instances of non-optimal behavior (including small traders), but none were consistently harmful to the studied markets.

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Do Index Traders cause Distortions

- The number of index positions has increased significantly
- Senate PSI report concluded that index investment overpowered delivery mechanism resulting in higher wheat futures prices compared to wheat cash prices (poor convergence)
- Etienne, Irwin, and Garcia (*AJAE,* 2015) found limited futures price explosiveness (about 2% of the time) and any price bubble effects on commodity futures prices were small and short-lived
- Areal, Balcombe, and Rapsomanikis (*EARN* ,2016) and Li, Chavas, Etienne, and Li (*J. Agric. Econ.,2017)* fail to find discrepancies alleged in the PSI report
- Petzel (Testimony before CFTC, 2009) Argues large index long positions requires large commercial short positions which results in larger than otherwise stocks and higher value of storage
- Irwin, Garcia, Good, and Kunda (*AEPP*, 2011) and Garcia, Irwin, and Smith (*AJAE*, 2015) however, find no significant impact of index positions on Corn, Soybean, Wheat, and KC Wheat spreads

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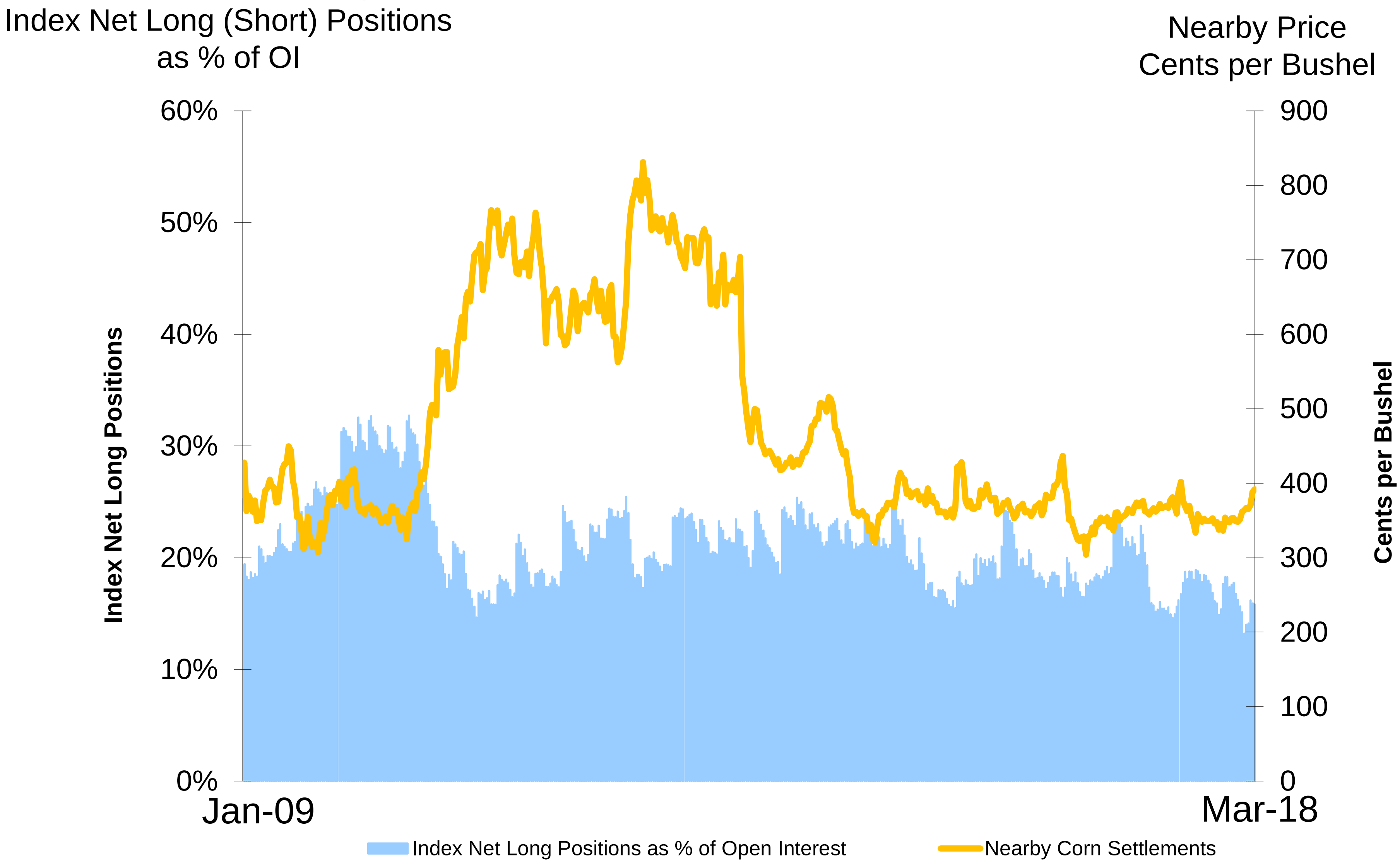
Index Fund Net Long Positions Vary Independently and Often Inversely to Futures Market Prices



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