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JULY 28, 2009

Traders Blamed for Oil Spike

CFTC Will Pin '08 Price Surge on Speculators, in a Reversal From Bush Findings

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By IAN THE JEANNE DUGAN and ALISTAIR MACDONALD

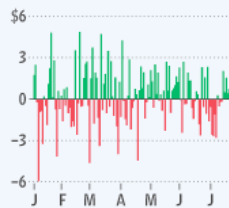
The Commodity Futures Trading Commission plans to issue a report next month suggesting speculators played a significant role in driving wild swings in oil prices -- a reversal of an earlier CFTC position that augurs intensifying scrutiny on investors.

In a contentious report last year, the main U.S. futures-market regulator pinned oil-price swings primarily on supply and demand. But that analysis was based on "deeply flawed data," Bart Chilton, one of four CFTC commissioners, said in an interview Monday.

The CFTC's new review, due to be released in August, adds fuel to a growing debate over financial investors who bet on the direction of commodities prices by buying contracts tied to indexes. These speculators have invested hundreds of billions of dollars in contracts that were once dominated by producers and consumers who sought to hedge against oil-market volatility.

Ups and Downs

Daily change in the price of oil, in dollars a barrel



Source: Thomson Reuters

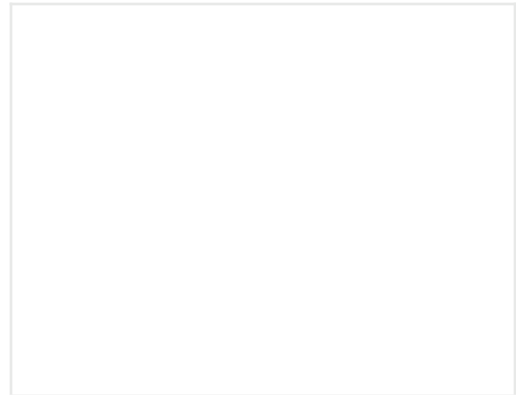
The review also reflects shifting political winds. Under Chairman Gary Gensler, appointed by President Barack Obama, the CFTC is departing from the more hands-off approach it took under its previous head, a George W. Bush appointee. The agency is widely expected to adopt new rules to limit the amount of investments in commodities by big institutions betting on their direction purely for financial gain.

The agency didn't make available preliminary figures from the report and declined to discuss the previous data.

Speculators have been a lightning rod of criticism from politicians world-wide, who worry that rising oil prices could damp the recovery potential of their recession-hit economies. Many lawmakers and regulators say they want to ensure that speculators don't make it more costly for consumers to access heating oil, food and other essentials.

These decision makers don't present a united front. The U.K.'s Financial Services Authority has found no evidence that speculators are behind big oil-price swings, people familiar with the matter said Friday. This view, made by the overseer of one of the world's biggest financial markets, contrasts with an opinion piece published in The Wall Street Journal two weeks ago, by French President Nicolas Sarkozy and U.K. Prime Minister Gordon Brown, who said governments need to act to curb "dangerously volatile" oil prices.

In the U.S., the CFTC begins public hearings Tuesday to determine whether to limit speculative investments in commodities. Congress also is weighing whether to give the CFTC the authority, under a broader proposal to revamp financial regulation, to regulate commodities investments that occur off traditional exchanges. Byron Dorgan, a North Dakota Democrat, has called on the CFTC to curb "oil speculators looking for a quick buck at the expense of American consumers."



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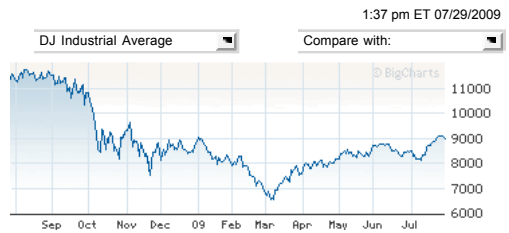
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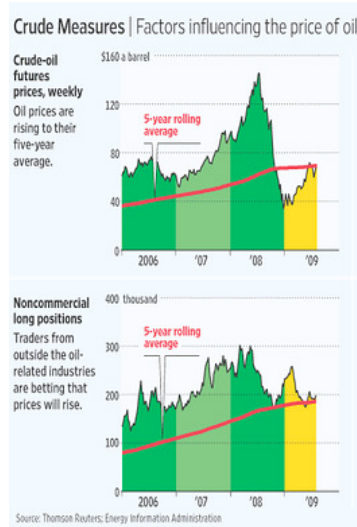
years. Those who want to bet on commodities prices have increasingly put their money in indexes that track the value of futures contracts, in which investors promise to pay a certain amount in the future for oil and other commodities. As of July 2008, financial investors had about \$300 billion riding on these indexes, roughly four times the level in January 2006, according to the International Energy Agency, a Paris-based watchdog.

Separately, these investors may buy derivatives, not directly traded on futures exchanges, that let them make contrary bets to offset their risks.

Crude-oil prices surged in July 2008 to a record \$145 a barrel, then dropped to about \$33 in December. Oil now trades at around \$68 a barrel.

Proponents of index speculation say these parties have added liquidity to markets. They blame price gyrations on supply and demand and say attempts to regulate speculation are foolhardy and could drive investors to less-regulated venues.

CME Group, the world's largest commodities exchange, said in a statement that it hasn't seen "any empirical evidence that index funds and speculators distort prices, as has been widely alleged."



shifting nature of commodities trading in recent years. Before the mid-1990s, these markets were dominated by entities that had physical dealings with the underlying commodity, and "speculators" who often took the opposite position, providing liquidity to markets.

But a new group of investors has emerged in recent

The exchange's chief executive, Craig Donohue, said: "We are deeply concerned that inappropriate regulation of these markets will cause market participants to move to dark pools and other unregulated markets, causing irrevocable harm to the entire U.S. economy." Dark pools are private markets where large orders are transacted.

Last year, CFTC Chief Economist Jeffrey Harris told a House Agriculture subcommittee: "The economic data shows that overall commodity price levels, including agriculture commodity and energy futures prices, are being driven by powerful fundamental economic forces and the laws of supply and demand." Mr. Harris didn't return a call to comment.

The acting CFTC chairman at the time, Bush-appointed Walter Lukken, told the House Agriculture committee that CFTC's economists "did not find direct evidence that speculation was driving up prices." Mr. Lukken, now an executive at the New York Stock Exchange, declined to comment.

In preparing its 2008 report, the CFTC sought information from swaps dealers about their off-exchange derivatives transactions. CFTC commissioner Mr. Chilton -- who was appointed by Mr. Bush and now awaits confirmation of his reappointment under Mr. Obama -- said the data the agency gathered was incomplete, with some players providing partial or no information.

Mr. Chilton dissented from the 2008 CFTC report, saying the agency's conclusions didn't go far enough. He expressed doubt about the amount and type of data received, which he called limited and unreliable. "We didn't have all the information we should have," he said. "And we gave it to Congress anyway, and we spun it."

The agency began shifting under Mr. Gensler, its new chairman. During his confirmation process earlier this year, Mr. Gensler said he believed speculation was partly behind the surge in commodity prices.

Mr. Chilton said the new report will contain a more-thorough analysis of the investors in contracts tied to oil and other commodities, and reveal cases in which single traders hold massive market positions. "We now have multiple sources,

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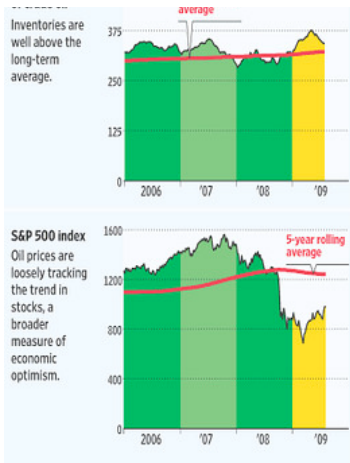
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Meantime, the U.K.'s FSA has been examining whether speculation has driven big oil price swings in recent months. The FSA is leaning toward the conclusion that the moves have more to do with uncertainty over the direction of economic growth than speculation, according to the people familiar with the matter.

The FSA has no jurisdiction over U.S. markets. But it oversees ICE Futures Europe, one of the largest global energy exchanges, which is based in London.

The FSA doesn't believe that limiting the size of trading positions would be "beneficial" for the market. Still, it concedes it doesn't have a "full explanation" as to why it the market has moved as it has.

—Carolyn Cui and Kara Scannell contributed to this article.

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