



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

435-912 647

IN REPLY
REFER TO: CED8-272

B-146770

March 20, 1978

The Honorable Frank E. Evans
House of Representatives

Dear Mr. Evans:

In your letter of March 2, 1978, you asked us to (1) review the effect of speculative short selling in the commodity futures markets on the cash prices of wheat and cattle, (2) review the pertinent literature dealing with speculative short selling, and (3) formulate a mathematical model of the subject matter.

As you know we are completing a year-long review of the Commodity Futures Trading Commission. Our review did not cover the effect, if any, of speculative short selling on the price of the underlying cash commodity. In response to your letter, however, we asked Commission officials whether they had performed any research in this area. They provided us with the enclosed copy of a March 7, 1978, paper on speculative short selling prepared by the Commission's Acting Chief Economist.

The Acting Chief Economist essentially concluded that speculative short selling is necessary to promote and maintain liquid (competitive) markets for futures trading. He also pointed out that futures prices are intrinsically related to cash prices and cannot override the basic conditions of supply and demand for any period of time. Restrictions on short selling would do nothing to change the fundamental supply/demand conditions, according to the Chief Economist, but would simply decrease liquidity and competition in the markets. On March 14, 1978, we advised your office of the conclusions reached by the Chief Economist.

We were advised that you would like to submit for our review material your office had received from a group of farmers who were dissatisfied with the present situation on speculative short selling. We would be happy to review the material and inform you of our observations, including whether we believe it would be useful or feasible for us to perform a review of speculative short selling. As part

of this effort, we may want to send a copy of the material to one of our economic consultants who assisted us in our review of the Commission's activities.

We hope that these arrangements will be satisfactory to you.

Sincerely yours,

(Signed) Elmer B. Stearns

Comptroller General
of the United States

Enclosure