INTERNATIONAL
Herald Tribune

Around the Markets: Chicago traders beat firms in predicting job growth

By Daniel Kruger
Bloomberg News
Tuesday, March 6, 2007

NEW YORK: Burt Gutterman, who began trading soybean futures 35 years ago, said markets in Chicago had helped him make money betting against economic forecasts made by the world's biggest securities firms.

Options on the Chicago Mercantile Exchange that let traders bet on fluctuations in U.S. job growth have been about 6.8 percent more accurate since April 2004 in anticipating monthly changes than the average of forecasts from Wall Street firms that trade U.S. Treasury securities with the Federal Reserve, CME data show.

"In this business you're only as good as your performance," said Gutterman, chief executive at Sangamon Trading, a commodity trading adviser in Chicago. "We've been fortunate to make some money on it."

The Chicago exchange generates a consensus estimate for U.S. job growth based on the weighted average of options purchased by traders. The contracts have emerged as critical tools for Treasury bond traders like Gutterman in trying to anticipate the effects of U.S. employment reports. Three of the six biggest changes in benchmark Treasury prices since January 2006 have come on employment report days.

The payroll figure is usually released the first Friday of the following month. The February report will be issued Friday. The popularity of the jobs auction has prompted exchanges to expand the use of derivatives tied to other economic reports as traders become less reliant on the views of economists.

"The market has some nice ways of aggregating existing data," said Justin Wolfers, a professor of economics at the University of Pennsylvania's Wharton School of Business in Philadelphia, who has studied the contracts and found them more accurate than forecasters.

The derivatives, created by Goldman Sachs Group and Deutsche Bank for clients in 2002, have a better track record than the firms' economists. Primary dealer forecasters have misjudged changes in nonfarm employment by 69,300 jobs on average since 2004.

Economists led by Jan Hatzius at Goldman Sachs missed the payrolls number by an average of 67,600 from April 2004 through last month. Joseph LaVorgna, chief U.S. economist at Deutsche Bank Securities in New York, was off by an average of 75,400 jobs. Brian Jones of Citigroup misjudged the amount by 84,600 jobs, on average, during the same period.

"Your average economist has to get his forecast out in advance," said Jones at Citigroup. "Traders get to incorporate any information that's available right up to the report."

Hatzius of Goldman declined to comment. Jones of Citigroup also said that the Labor Department revises the figures monthly because of the difficulty in gathering the data immediately.

"I believe in the wisdom of crowds," LaVorgna said. "The auctions can reflect more easily because it's a market and prices can move on the latest piece of information."

"There's no direct accountability for each number at those firms, like there is for us," said Gutterman of Sangamon, who began trading soybeans on the Chicago Board of Trade when they still used chalk boards to record prices.

Employers in the United States probably added 100,000 workers to their payrolls in February, according to the median forecast of 59 economists. The unemployment rate was steady at 4.6 percent, they predicted.

Traders can purchase options on the payroll data the day before and day of the release and from 3 p.m. to 4 p.m. New York time the two days before the report. The options offer hedge fund managers, traders and bankers a way to make money on their forecasts or hedge against market losses.

"It gives you the latest, best idea of what the number will be," said Ray Remy, head of fixed-income trading in New York at Daiwa Securities, one of the 21 primary dealers. "Because of the volatility there's the potential to make money, so you want to be involved."

Notes: