Feature Interview

The Markets, Trading Systems, Dad and Other Adventures

Philip Gotthelf
Publisher, COMMODEX® System

BY RUSSELL WASENDORF, SR.

Philip Gotthelf may be one of ***SFO***'s most interesting and unusual interviews to date. The bow-tied publisher of the longest-running daily futures trading system published anywhere – the COMMODEX System – is a trader, renowned analyst, author, speaker and educator, among other endeavors. He further has achieved an enviable reputation for uncanny accuracy where the markets are concerned.

Perhaps Gotthelf's most notable forecast was prior to the October "Crash of '87," but then there were also highly consistent currency predictions ever since the early days of currency futures' inception. He has an extraordinary record of foreseeing interim and long-term interest rate moves and has called tops and bottoms in meats, grains, sugar, precious metals and coffee. So, here we have a commodity guy who can leverage his wisdom into tangible results. Yet, he makes mistakes like everyone, because even the very talented can be drawn into second-guessing what, in retrospect, may have been the perfect market call. Sound familiar?

In the interview that follows, he makes some macro predictions on the markets, harkens back to his early days of trading, admitting that there were foibles, and speaks with great love and admiration for his father, Edward, the inventor of COMMODEX. As he says privately, "My father was extremely colorful; much more than I am." Well, perhaps. But the interview shows that, with Philip Gotthelf, the apple doesn't fall far from the tree. For traders and traders-to-be or for those that are merely "students" of the markets, there is something to be learned from this remarkable man.

RW: *Our August/September issue looks at trading systems – pros, cons and guidelines when making choices. It's not surprising then that I should be talking with **you** since COMMODEX is the oldest futures trading system in existence. Plus, I think your personal trading experiences will offer some excellent insight for **SFO** readers. Let's begin by talking about how COMMODEX began. I know it started in the 1950s, and your father, Ed Gotthelf, who I knew and for whom I had great respect, was the mover and shaker behind the operation.*

PG: My father created the COMMODEX system, traded with it from '56 to '59 and published it in 1959. But he actually started trading back in the 1920s, obviously without the benefit of the system he created. He was in his early twenties when he first got the trading bug, and then he was hired to write the treatise on commodity trading when the government was developing the Commodity Exchange Authority (CEA). He actually had a very colorful past. In fact, in 1950, he was accused of cornering the egg market, and he pleaded no contest. And people said, "Why would you plead no contest, if you weren't guilty?" But the reason is very clear; this was the McCarthy era. He said, "The government was not fun to do business with back then." So, he basically tried to get out from whatever it was they were accusing him of and move on.

RW: *But your father was also in the publishing business, which led to some natural tie-ins to publishing COMMODEX.*

PG: Interestingly, he also was an advertising guy. And, the story goes that my father's advertising agency was hired to advertise a newsletter called "Commodity Futures Forecast," which purportedly was going to tell people how to trade. So, he handled advertising for the newsletter in the ***Herald Tribune***, the ***New York Times*** and the ***Wall Street Journal***. Through the advertising, several thousand people became interested in the service, and that was good. But when my father went to the guy to have him pay the bill, the owner decided he didn't want to do the newsletter after all. And the bill wasn't going to be paid, so my father became the publisher of "Commodity Futures Forecast." After that, he became very successful because there were very few services for commodities back then.

RW: *Can you tell our readers the basis for the COMMODEX system and how it evolved?*

PG: My father, who was trading at the time, found that his psyche went in cycles where he was trading very effectively and then times where he wasn't quite able to focus on what was happening in the market because some other thing was playing in his head. He had seats on exchanges and would go down to the New York Merc or, if he was in Chicago, he'd watch Board of Trade action. He likened the action to bidding on a painting of a master artist at an auction. So, if all the bidders wanted a Picasso, their hands would be up and flailing with prices going higher. Assume the bid starts at $1,000, goes to $1 million and, finally, at $7-1/2 million, you and I are the *only* guys with our hands up. Obviously, the two of us could keep bidding until it went to $100 million. But it's getting close to the top. So, when you buy the painting for, let's say, $8 million, who could you sell it to?

RW: *You've eliminated every seller and every buyer at that point. I assume that you're getting to the point about COMMODEX.*

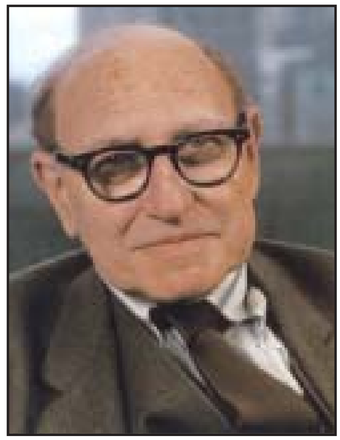
PG: Yes, and you're right. Maybe you could sell it to me, but since I wasn't willing to offer the auctioneer $8 million, the best price you could hope to get out of me would be my last bid, which was probably $7-1/2 million. This is where COMMODEX comes in. My father said the situation of the last bidder defines an overbought market; it was very intriguing because we hear these concepts bandied about all the time. No one ever sought to explain the dynamics behind an overbought market. It means you're the last guy or the last group of traders with the highest bid or bids. You're stuck there, and nobody behind you is going to pay a price anywhere near what you just paid, so the next trade has to be lower. Therefore, traders should want to sell an overbought market.

RW: *But how do you measure that?*

PG: That's precisely the question that created COMMODEX. My father wondered, "How do I measure these hands?" In stocks, you can't have an accumulation because if I own IBM and I sell it, then the buyer owns IBM. With a fixed number of shares, for every seller there's a buyer and vice-versa. But in commodity markets, there's an actual accumulation taking place. Open interest can rise and, as it rises, money enters the market. Every time you have an increase in open interest, you also have an increase in margin. The light went on in his head, and he said, "I can measure the hands going up in this auction pit by determining how much open interest is increasing or decreasing, relative to how much margin is coming into the market." So, he came up with some simple formulas. If open interest goes up by ten and the market goes up by a buck, how much money has entered the market? Ten bucks. If the open interest goes up by one, but the price goes up by ten, how much money has entered the market? Ten bucks. So, he says, "I can measure in commodities how much money is entering the market, and I know whether it's long or short by the price direction. That's how I'm going to formulate COMMODEX." From about 1953 to 1956 he was busy with a bunch of guys with their Freden mechanical calculators and their little visors on, calculating all of the stuff and trying to get the correlations to work.

RW: *And, again, without the computers, it must have been a laborious procedure.*

PG: It was very similar to a game of chess. It was an intuitive feel that you had from the market, plus the observations of the chessboard that told you where you should move your pieces – an intellectual exercise. And, I believe it's one of the reasons COMMODEX has survived so long – because it's not simply a back-tested series of experiments where you're saying, let's try this, let's try that. It was an intellectual exercise in analyzing markets to determine how these markets function and how that function reflected in the statistics. Price, obviously, gives you the direction. Volume is the velocity. You can liken that to the speed with which people would raise their hands, and the open interest was the money that's coming into the market. And, if no money is coming in, you can't take it out. So, obviously, he wanted to have as much money entering a market, and that's how we came up with the COMMODEX index values. Each day, COMMODEX measures accumulation or distribution on a scale from -10 (strong selling) to +10 (strong buying). Then, a composite of Daily Index values is calculated to determine if a trend exists. The composite called the Trend Index that measures on balance accumulation or distribution on a scale from -100 to +100. This also acts as an oscillator where extreme values signal overbought or oversold conditions. Price up, volume up, open interest up, depending on the speed and velocity, can yield a +10. Price down, open interest up, volume up, -10. Minus ten is an accumulation of short positions. Plus ten is an accumulation of long positions. It's that simple. By correlating the Daily and Trend Indices, he (my father) developed trading rules. Buy when the Daily Index gets to a certain point and exhibits certain behavior in conjunction with the Trend Index. Sell when it gets to the same point in the opposite direction. These rules are explained as part of the COMMODEX service.



Edward Gotthelf, creator of the COMMODEX System

RW: *Or, perhaps as important, if there's no accumulation, simply sit back and don't do anything.*

PG: That's right. It is one of the rare systems that has a neutral stance. If there's no trend, don't do anything. So, he started publishing COMMODEX every day while he was trading. At the time, I think he was the largest trader on the books of Bache. [***Editor's note****: In 1981, Prudential Insurance Company of America acquired Bache & Co. The name changed to Prudential-Bache Securities in 1981 and then to Prudential Securities in 1991.*] But when you're that successful, there's always someone who assumes there's something amiss. So along came the CEA that had looked at his marvelous trading record and said, "There's no way this guy can be that good." So they issued a cease-and-desist order and told him that COMMODEX constituted inside information.

RW: *How did the CEA determine that?*

PG: What they basically were saying was that because the system was so accurate and because he had access to it before the public (i.e., subscribers), COMMODEX was, in effect, an inside barometer. But they didn't say he couldn't use it. He could either trade and *not* publish or publish but *not* trade. It's 1960, which is still, basically, slightly post-McCarthy era. No one knew what authority the CEA had. So, he said, "Alright, I'll publish." If he had said, "I'll trade," you'd be looking at another Bill Gates.

RW: *So, then, tell me about your route to involvement in COMMODEX.*

PG: The COMMODEX thing was very intriguing to me, and computers were just becoming generally available. But first, I went to Lehigh University. I was a music major. However, after getting a D in music appreciation, I figured that if I couldn't appreciate it, I certainly couldn't make a career of it. So, I played guitar in coffeehouses to earn extra money. I finally decided to get serious and switched to the business school to major in economics and finance and minor in statistics. I got out of college, was unemployable during the recession and missed Vietnam by one day. So, I needed a job. At that time I was offered $200 a week to be a stock analyst. I decided to work with my dad.

RW: *Did you think you could improve on the COMMODEX system?*

PG: Yes, I thought I might be able to do that. So I spent the better part of my senior year in a special project with this fellow who's internationally known for statistics, named Dr. James Greenleaf. We formulated ways of improving the system from a money management standpoint, but we never could consistently improve upon its performance. If it was a short-term market, you could use shorter averages for measuring the price directions, but as soon as you adjusted your model for that, it turned out to be a longer trending market, and you'd have to change the model. By the time you did that, it was back to a shorter.

RW: *As I recall, the correlations were fantastic.*

PG: The system had a remarkable correlation of the long average and the short average that took into account just about every kind of condition. So, that was helpful. But, we found out that COMMODEX had an 85-percent accuracy entering the market. In other words, eight-and-a-half times out of ten, if COMMODEX said buy, prices went up. If it said sell, the prices went down before the signal was closed out. But, it only had a 33-percent efficiency, capture ratio, so if the bonds went from zero to a $1,000 on average, COMMODEX would only take $333 out of that move. That's a big loss of profitability. Still, it's a pretty good way of making money in commodities, but everybody was curious about how we could improve the efficiency.

RW: *You didn't want to leave that much on the table.*

PG: No. So, we developed statistical models to determine when the 66-percent move was going to mature and to what extent it was going to mature. That was the only major improvement that I made in the possible implementation of the system. Problem was, there were still no real computers in the late-'70s, so all of this calculating of profit objectives based on probability had to be done manually. By the time you did your calculations manually, sometimes your profit objective was here and gone, and you were sitting there wondering what was happening. So, my father used to say, "It has to work in the physical world." By the way, are you old enough to remember Paragon?

RW: *Sure, and thanks for asking.*

PG: That was first of the Hewlett-Packard calculators. It seemed to outperform COMMODEX a hundred dollars to one. I was so intrigued that I ended up finding somebody who was trading on the Chicago Board of Trade who had one of these Hewlett-Packards. I watched this guy. This thing was taking a half-cent to a penny out of beans. And of course, it was logging all of these wonderful $50 trades, not including commissions. And by the time you wrote your order, time-stamped it, called it down to the floor, it was all over. You'd lost. But the Paragon system *looked* so good because it was not trading in the real world. My father and I got a big chuckle out of that, so we left Paragon alone and just kept on working on our product.

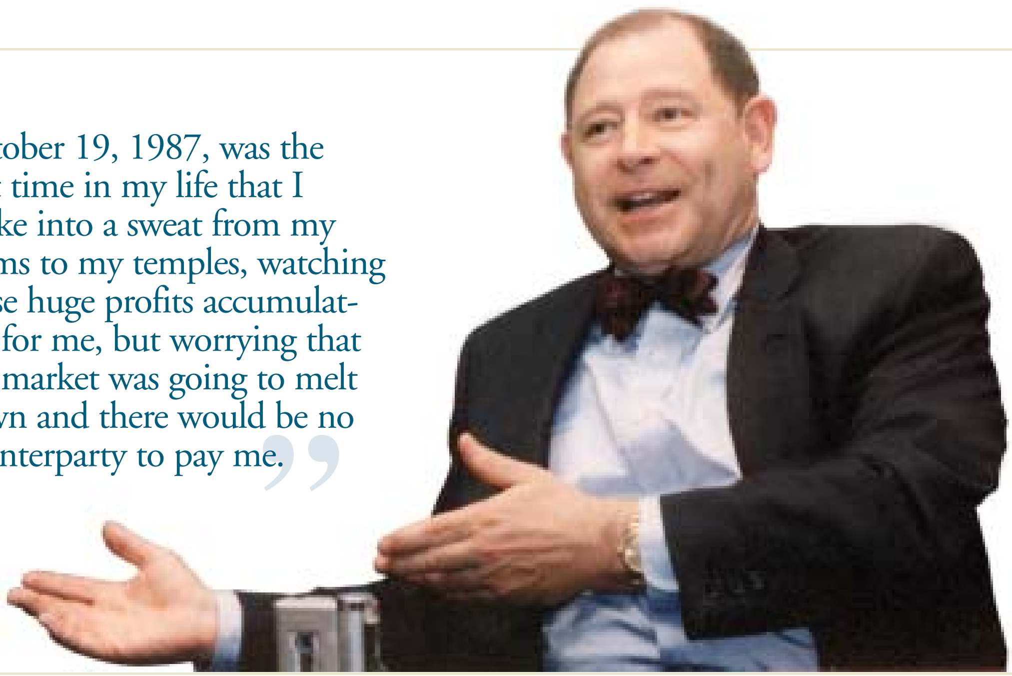
RW: *I'm going to go back to something that you alluded to earlier. One of the greatest problems that most systems have is that they constantly need to be adjusted in order to fit whatever the current market conditions are. They work under certain kinds of market conditions, and they stop working under other kinds of market conditions. Your system has a tendency, because of the principles on which it's built, to be self-optimizing, and you don't have to constantly tweak it.*

PG: Right now, for example, we're going through a period of trending markets at the Board of Trade [***Editor's note:*** *This interview was in late May 2003*]. We just went up 12 cents in soybeans this morning, and COMMODEX is going to do extremely well when you have trending markets. When you have a whipsaw market, COMMODEX has the ability to go neutral. So, it's not going to get hurt as much as systems that are always either long or short. In other words, if your price is above, let's say, a 21-day moving average, or an 18. So, you're over the 18-day moving average and you're long. And it goes below the 18-day moving average and you're short. And heaven forbid you're experiencing what heating oil and crude oil markets are doing where the moving averages converge on top of each other in a straight line while the market makes multi-thousand dollar swings like a Chinese ping-pong tournament. You might as well just write checks to the boys on the floor. But, the fact is that COMMODEX has the ability to avoid the bulk of this type of erratic movement. That's not to say that we don't have difficult periods.

RW: *Well, certainly all systems go through bad periods. And there's no such thing as perfect or we'd all be billionaires.*

PG: The problem that you encounter when you have systems with good periods and bad periods, COMMODEX included, is that there's a psychological influence. For example, you get involved with trading, and the first thing that happens is you lose 50 percent of your equity over the course of four, five, six weeks, so you become discouraged. So, you stop trading before you get to the period of time when you're potentially going to do well. This is a bit of gallows humor among brokers using COMMODEX to guide clients, which is that when the broker is doing well, his clients are not. And when the clients are doing well, he's not. Why? Because when brokers are generating higher commissions, COMMODEX is trading in and out of shorter-term positions. There are likely to be stop-outs or close-outs that don't have a substantial profit or generate losses. When COMMODEX is in a period like this past month, the commissions are very slow because COMMODEX can hold a position for weeks and even months. Just out of curiosity, do you remember when sugar was trading at 4-1/2 cents?

"October 19, 1987, was the first time in my life that I broke into a sweat from my palms to my temples, watching these huge profits accumulating for me, but worrying that the market was going to melt down and there would be no counterparty to pay me."



RW: *Sure.*

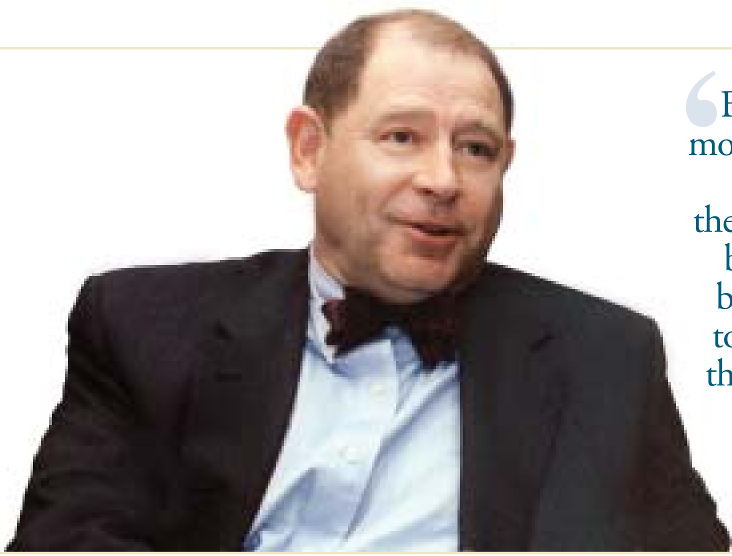
PG: Back then, I rationalized that sugar would not be rolled out into the streets for free, so I bought a few contracts. Of course, COMMODEX sold short. The market dropped from 4-1/2 cents to 4 cents, and I bought more while COMMODEX enjoyed a half-cent profit. At 3 cents, COMMODEX has a 1-1/2 cent gain while I'm in the hole. I averaged down. The end is obvious. I placed my stop at 2.55 cents because I was going broke. I believed the bottom was at 2.52 cents, so I was stopped out. Meanwhile, the market finally turned around, and COMMODEX exited with a 2-1/2 cent profit, or $2,550, went long at 3.01 cents and rode the uptrend to about 16 cents. This proves the difficulty of following a system that can fly in the face of logic – one that dictates a commodity is simply too low or too high.

RW: *Most people don't realize that they're their own worst enemies when it comes to trading the markets. That's where a system comes into play and becomes important. But let's back up a little bit. There are some people that call your system a techno-fundamental system. Why?*

PG: When you have a purely technical model, it's usually based upon price alone – things like chart patterns, moving averages and various price formulations. A fundamental change in the market generally influences participation as well as price. For example, diagnosis of mad cow disease in Alberta may drop cattle prices. There's a fundamental change in the prospects for the cattle market leading to massive herd liquidations. We conclude cattle will sell cheaper, and those liquidations should be reflected in a rising short side open interest and falling prices, which would trigger COMMODEX's selling short. So, the fundamental condition of the market is reflected in the way COMMODEX interprets the market, whereas if the price were just falling in general, you wouldn't know the cause or the extent to which people are participating in the declining market. Are people going to give up red meat altogether because of mad cow disease? Not likely. So, today's glut becomes tomorrow's shortage. That condition will be reflected by long-side accumulation. The fundamentals are reflected by our model.

RW: *I discovered when I was doing a little bit of research for this interview that you and I made similar recommendations. I was writing a newsletter at the time, "Futures Factors," which you probably know. On October 9, 1987, you and I both told our customers to go short. This was ten days before the October 19 crash in the stock market where it dropped 500+ points. Of course, we both looked pretty smart at that time, but the truth is that we probably had no idea that it was going to be that extensive. But the market indications that we were using, though ours were different, were looking at similar type factors. Just a couple of years ago, on September 11, was your system short the financials?*

PG: Yes, I looked for some fundamentals, and here's what I came up with. It's likely Al Qaeda was selling short in anticipation of 9/11. It is similar to what took place during the Falkland War, when COMMODEX bought gold on



"Boomers are going to be pulling money out of the stock market for education or retirement while these Xers are just getting ready to begin families, build homes and buy Porsches. They're not going to be investing in anything other than consumer goods. So, where do you make up that deficit between the 30 million babyboomers and the gen Xers?"

a very subtle accumulation. We didn't know who was doing the accumulating, just that the indicators reflected an accumulation. It turned out to be Argentine generals who were busy buying gold in anticipation of the price going much higher once they invaded the Falkland Islands. With 9/11, we didn't know there was going to be an attack, but we *certainly* knew that the markets were reflecting something changing prior to that event. I'm not sure even bin Laden expected to see the complete destruction of the World Trade Center, because if you looked at his infamous videotape, he said it surpassed his wildest dreams.

RW: *Which was quite different than October 19, 1987, obviously.*

PG: On that Monday, October 19, when COMMODEX was watching the most spectacular one-day percentage move in the S&P contract – I think we had a $90,000 profit in the S&P by the close of that day. I personally was short the market and panicked. October 19, 1987, was the first time in my life that I broke into a sweat from my palms to my temples, watching these huge profits accumulating for me, but worrying that the market was going to melt down and there would be no counterparty to pay me. So, at approximately $50,000 into that move, I left $40,000 on the table. I got out, and I wanted to go to cash so badly that I wanted them to wire the money to the bank. And I was worried about what bank they were going to wire the money to. So, there again, was the disciplined and blissfully ignorant trader who held through Monday and Tuesday and made a huge profit. I wanted to be safe and in cash or even gold, which was a very bad thing to buy back then. The illiquidity from the overall crash evaporated money to buy gold, so gold went down. But that's the personal interpretation coming into play. They say, "OK, Philip Gotthelf is an expert in the market. He wrote a book on precious metals and on currency trading, on energy trading, so he should know better." Yet, that personal knowledge can influence me in incorrect ways.

RW: *Well, frankly, you knew too much. But, let's take a little detour here because that brings up the point about an entirely new market that has come about – single stock futures – which is really taking the securities market and applying the principles that we use successfully in the futures market. Have you been using your system to analyze single stock futures?*

PG: Well, the volume and open interest aren't stellar yet. But we fully anticipate being able to apply the same formulas, because the markets are the markets. They all operate the same way. These are still part of a bid-and-ask marketplace. One negative to single stock futures is the argument existing before the '87 crash, which was if you hedge stock portfolio exposure with futures, you defeat the investment purpose of gaining price appreciation commensurate with your risk. So, if you eliminate the downside and upside, all you're going to get is dividends. The same logic thwarts single stock futures. Of course, we know proper timing allegedly lifts a stock hedge when prices trend higher. You try replacing your hedge when the market is looking overbought or unstable.

RW: *To me and to a number of my colleagues, it's one of those products that really hits on a market need, but it just hasn't* ***begun*** *to reach its potential yet. I believe it will, especially because there are market makers standing ready to take on the orders. It's different than a typical futures contract where you need lots of volume to get in and out of the market at a decent price.*

PG: Single stock futures represent the permutation of four things — the stock itself, the futures, the put and the call. These four vehicles present *multiple* strategies that can yield profits that previously didn't exist. They're synthesized by this creation of a single stock futures contract. The standard procedure is to hold IBM in expectation of appreciation. While you hold IBM, you can sell a call. If you're called away, you're happy because you've made profits from where you sold that call to the strike, and you make the call premium. Take all that cash and buy your IBM back. People think they've lost the IBM, but they haven't. They get cash.

RW: *Interesting viewpoint. I'm going to make a 180-degree turn here. Someone who used to speak at seminars for me once said that he feels that most people trade the futures markets for entertainment. Agree or no?*

PG: Absolutely. I'll give you an example. A guy in his eighties came to me and he said, "I had six million dollars in my pension fund, and it's now at two and a half. I heard I can make it back in the commodity markets." I discover he's 84 years old, married, in good health and took a big hit in the market. I asked if he had ever taken a cruise, and he says, "No, but, how do *you* make money if *I* go on a cruise?" I said, "I don't, but, why do you need more money? You're 84 years old. Take your money and spend it! That's my recommendation." The guy says, "Okay." I didn't send him account forms, nothing. About six months later, I get a call from him – "You remember me?" I say, "Yes. Didn't I tell you to go on a cruise?" He says, "Heck, I took that cruise – best time I ever had, but I want to trade." So, he opened a $10,000 account and dropped it down to four, put in another six, and dropped it down again. I called him saying, "You know, you're not trading properly." He says, "Don't bother me. Can't you see I'm having fun?"

RW: *Well, that really creates a dilemma because you've really got a combination of circumstances. One* *circumstance is where people are affected by their psychology, and that is always detrimental to their trading, or usually is, unless someone is masochistic and they really…*

PG: …are having fun.

RW: *Right. And if you think about it, if you're really having fun, usually that's when you're making money, and making a lot of money affects your psychology and then you become holier than thou. You believe you know everything there is to know in the world. That, of course, is when you become the most vulnerable.*

PG: Not only that, but we in the futures industry have created an aura about commodity trading vis-à-vis Hillary Clinton going from $1,000 to $100,000, and the $700 million made by Warren Buffett while George Soros makes a billion dollars trading currencies. So, someone opens an account. Let's say he has $10,000, and at the end of the year he's got $12,500, a 25-percent return after commissions. Not a bad year, but the individual thinks, "What good is $2,500? My wife can spend that in five minutes. Heck, she can spend it in three!" Yet, the same person's other money is in Treasuries earning two-and-a-half percent. Is he happy with that? My point is how do we get commodities into the same risk/reward parameters as stocks and bonds? How do you get people to divorce themselves from the sensational and become practical, so that they're satisfied when they get 15- and 20-percent returns? If you take a system like COMMODEX and you trade it for an entire year with $50,000, at year-end you could be at $60,000 – you've done well, but not according to most people. Why? Because they read about a CTA who took the same $60,000 and turned it into $120,000.

RW: *I heard it through the grapevine that you, individually, are pretty good at predicting markets.*

PG: Some people think so. In March of 2000, I did an interview with CNBC's Ron Insana, he asked me what I thought of the market, and I said, "I think it's over." He said, "Are you crazy? It just made a new high." Based on what I'd seen, I thought the market was going to crash between then and April. I believe you and I think alike since we're from the old school. All I did was watch the last quarter of '99 when the Dow Jones went down and the Nasdaq went up. This told me people were finally getting out of the Dow Jones stocks they had accumulated for the past 50 years, and they were going into the speculative Nasdaq, which was the classic definition of the bubble. I concluded they had large capital gains taxable in April. What could they pay with? They had to sell something, and that was going to be their Nasdaq stocks because none of these guys thought through the consequences of having to "pay the tax piper." In late March, a small article in the ***Wall Street Journal*** appeared indicating how tax burdens were taking investors by surprise. Sure enough, between March and April we saw the first down leg down in the Nasdaq, Dow and S&P 500. I wasn't a genius; my father was much smarter than me – recall that I thought sugar was cheap at 4 1/2 cents. The question is, can you make money with my macro-predictions? Yes, if you've got Warren Buffet's deep pockets. But, it's tough for me to say that I'm as good as COMMODEX in terms of consistency, because my predictions are very broad and general.

RW: *Well, let's make a broad prediction. What do you think interest rates are going to do?*

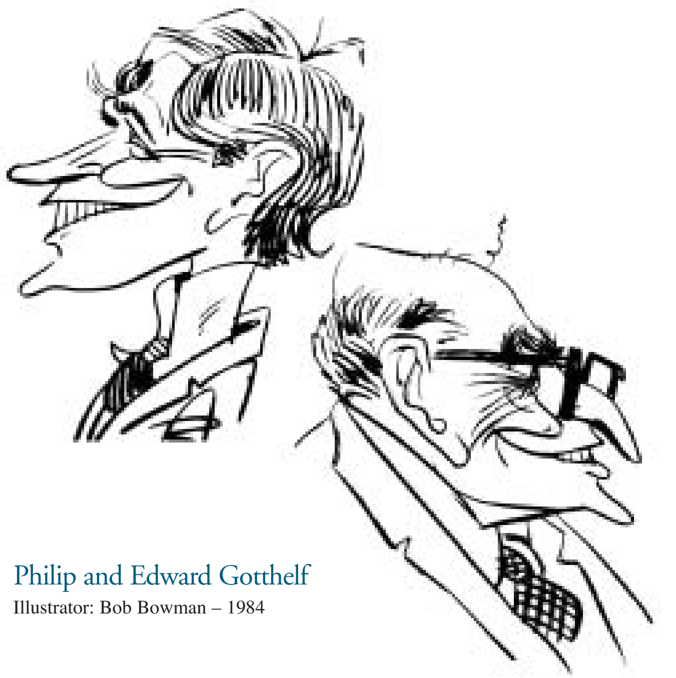
PG: I think interest rates are probably going to hover around the same area. Maybe, even if the Fed kicks the interest rates down, I think that's being taken into consideration. If I were involved in the cash bond market, I'd be lightening up, because there really is too much downside exposure. You've got very, very low yields. You've got nothing but a limited potential for lower interest rates. So, my prediction is that we're pretty much at the end of the downtrend in interest rates and the uptrend in principle values. That's my prediction based solely upon levels. Does that mean that the bond market won't go to 121? No. It's possible that it can go that high. I'm simply saying conditions tell me, from a macro-portfolio standpoint, that I don't want to be heavily weighted in bonds anymore.

RW: *What about the equities market*?

PG: Again, macro-prediction. A television anchor named Consuelo Mack interviewed me, and we discussed demographics. I said that demographics don't look good for the stock market because there are 30 million more of us baby-boomers than there are of generation Xers. Boomers are going to be pulling money out of the stock market for education or retirement while these Xers are just getting ready to begin families, build homes and buy Porsches. They're not going to be investing in anything other than consumer goods. So, where do you make up that deficit between the 30 million baby-boomers and the gen Xers? That's just the topic to be discussed by the big money managers. Oops, there I go with another broad prediction. We're going to have a lackluster stock market until such time as our government gooses it with something extraneous, outside of the scope of normalcy – a proposal for privatization of Social Security, for example, or some way to inspire people to put money into the market via tax incentives. Other than that, I don't see corporations doing remarkably better. I don't see consumers spending. I see a big hole.

RW: *Do you see deflation?*

PG: I see the possibility of monetary deflation or an even worse scenario with monetary deflation and a cost-push inflation similar to the Nixon era stagflation. What was stagflation based upon? — high energy prices forced upon us by OPEC, a disaster in the grain markets based upon the corn blight of 1971, followed by the Russian wheat "robbery" of '72, and then cost-push inflation throughout the period, despite all the fiscal policy and all of the monetary policy we tried to put in place. Mother Nature was the culprit that froze coffee in 1975 and 1985. Mother Nature caused problems with the sugar market in '74, in the grains in '73 and the meats in the late-'70s. So, how do you program against Mother Nature? You can't. Yet, I generally see a deflation because OPEC has been busted by Operation Iraqi Freedom, and technology has removed threats like corn leaf blight. Vietnam has become a formidable coffee producer, and pigs breed faster than rabbits.



Philip and Edward Gotthelf

Illustrator: Bob Bowman – 1984

RW: *What you described is a period of time from approximately 1972-1980 when if one market wasn't making record highs, another market was. Like when soybeans rose above $12.50 or…*

PG: Just before the teens, right?

RW: *Yes. I had a friend in the soybean pit at that time. He said that when the market hit the all-time record high of $12.90, the pit went absolutely silent. That, of course, gives you an indication when there's not another buyer, similar to your father's early thoughts. By the way, who specifically uses COMMODEX?*

PG: We have small traders who are trying to learn about commodities as well as long-term subscribers who tend to be professionals with brokerage companies, registered reps, banks, agricultural and energy companies – just about anybody who's trading physical commodities has a need for COMMODEX. We break it down to two basic audiences – speculative and industrial. Speculators are traders and, to some extent, hedgers, because they actually do speculate. Industrial users are people who get a feel for the interest rate markets, even if they don't trade interest rates in the futures – banks, brokerage companies, other financial institutions. They get a feel for energy or currencies. We've had very good success. The worst period for COMMODEX sales was probably three years ago when we had great profits, but nobody was interested in commodities. Why should I trade commodities…

RW: *…when I can make a fortune in the stock market?*

PG: Absolutely correct. We suffered in the last few years of the Clinton administration because stocks were doing so well. Were it not for hardcore subscribers – for example, if we had been just another new newsletter – we would have gone out of business.

RW: *How many subscribers do you have?*

PG: We generally go from 10,000 down to 6,000 up to 10,000. In all honesty, I don't think there are more than 10,000 people out there. Frankly, I'd be happy at 3,000 subscribers. I would say our *core* list probably is fewer than 5,000. The only time we lose one of them is if they die. If they get fired or move from Chase to Citibank, they subscribe at the new location. Right now, we're on an upswing. Everybody wants to trade commodities. Everybody wants COMMODEX. Unfortunately, our competitors were decimated by the same three-year period we suffered through – they don't exist, so we're picking up a lot of business. Plus, who's got a record going back to 1959? COMMODEX is not a new kid on the block or a black box. Anyone can subscribe and test it before they invest. If it doesn't work, you won't renew or extend. If COMMODEX had not worked since 1959, it would no longer exist. COMMODEX is a publication; therefore, subscribers can trade anywhere they like – electronic, discount, full-service. Our brokerage affiliate, EQUIDEX Brokerage Group, Inc. also helps those who need assistance with a guided account program.

RW: *In your personal trading, do you establish long-term positions and then trade short term as well?*

PG: I do all kinds of crazy things. I'm one who will readily confess that I have fun. Win, lose or draw—I have fun. Something you'll appreciate because you were around in 1978 was when the Hunt brothers were cornering the soybean market and *not* silver. COMMODEX had a long signal on the July beans, and they were up limit practically every day. It was the first real sensational move since earlier in the '70s. And my boat is getting bigger. I put on my nice huge position, and I was very proud of myself because I was just out of college a few years. I'm this kid making a fortune in the bean market, and I come into work one day, and COMMODEX says get out. And, I look at the screen, and it's limit up. So, I called the floor and asked what's going on? Same thing. No offers, all bids. The system probably will get back in, I think. So, I go out to lunch and when I get back, the screen shows beans down two limits, $0.60. I don't know about you, but the first thing *I* did was tap the screen to see if it was broken. Then I get the bead of sweat in my lifelines, throbbing of the temples, and I finally get up the courage to call the floor. And I ask what's going on. Ooohhh— the exchange put a liquidation only on the July soybean contract because the Hunts were trying to corner it. I'm having a heart attack now. I know what that means. But I publish COMMODEX, and COMMODEX gets out…at the top. *The top!* People are calling me saying, "Well, that's a pretty damn good system. You must be so rich." Yet, here I am – losing limit, limit, limit. My boat's shrinking or even sinking. Talk about feeling like a jerk. But, I was young. I needed a good market beating.

RW: *So, you were young and probably headstrong. But your father had to teach you something about trading that helped, didn't he?*

PG: Sure, my father and I put on a bull bean spread—long July and short November. July was already over November, which was an inverted spread—what they call a backwardation now. In my day, spreads were normal (i.e., near under far) or inverted (near over far). Now, the spreads are contango, which I thought was some kind of dance, or a backwardation which spell checker rejects every time. We took $0.60 out of the July - November bull spread and my father exclaimed, "Look at the spread in August!" The August is $0.90 cents over September. He says, "Why would anybody hold an August bean at that kind of premium when cash beans are going to be coming out of the ground toward the end of August? Farmers planted early that season. Let's reverse the spread—we'll do the bear spread." We put on a $100,000

"I can measure in commodities how much money is entering the market, and I know whether it's long or short by the price direction. That's how I'm going to formulate COMMODEX."

spread, and it goes from $0.90 to $0.95 and from $0.95 to $1.00…$1.00 to $1.05. My father keeps saying, "Put more on!" Finally we're coming up on August, and we're going toward first notice day. He says, "Don't worry, you're short August." So, not only does my boat not exist any more, I can't even afford an inner tube. Sure enough, as we came into August, the spread narrowed by chunks of 10 and 20 cents a day. Well, when it came into about $0.50 cents, I said "That's it for me. I can't take it any more," and I pulled out despite my father's protestations that it was going to go to a normal market with the August at a discount to September. He stayed in with this big grin on his face; sure enough, it went a nickel August under September. I made good money, but he made more. Great experience. Great trading experience. But, understand, this was not based upon COMMODEX.

RW: *What about when you trade on the COMMODEX system?*

PG: If I traded purely the COMMODEX system, I'd do extremely well. But, I don't like to trade my own account when we are guiding customers. It can appear to be a conflict of interest if my personal trading is better than my clients'.

RW: *One final question, Phil. You've seen the futures markets change radically over the years. What's your take on how electronic markets have benefited the individual trader?*

PG: Electronic trading and platforms are marvelous for many traders. The drawback is they can be mesmerizing… hypnotic! They can be all consuming and detract from work, play and social interaction. Still, this progress has placed enormous power into the hands of individuals who can trade with the same acumen as professionals. I strongly believe electronic trading will create a powerful and positive expansion of futures and related options trading. It's a very exciting time to be involved in these markets.

RW: *I agree. With that, let me thank you for a very interesting interview. I think our readers will gain a great deal from it.*

PG: I've enjoyed it as well, Russ.

Russell Wasendorf, Sr., is chairman and CEO of PFG, Inc., a futures commission merchant. He also heads Wasendorf & Associates, Inc., a research firm that is devoted to trader education. He has authored five books, and his sixth book is scheduled for release soon.

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