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American Bakers Association

Serving the Baking Industry Since 1897

COMMENT

January 17 2008

Mr. David Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre, 1155 21st St. NW
Washington, DC 20581

Received CFTC
Records Section
1/18/08

Re: Proposed "Revision of Federal Speculative Position Limits"
Federal Register, November 21, 2007; Page 65483

Dear Secretary Stawick:

The American Bakers Association (ABA) appreciates the opportunity to provide these comments for the record in response to the proposed revision of federal speculative position limits by the Commodity Futures Trading Commission (CFTC).

ABA is the leading advocate for the baking industry. It has been the voice of the baking industry since 1897, representing its members before the U.S. Congress, federal agencies, state legislatures, and international regulatory authorities. ABA tackles issues facing the baking industry and initiates positive reforms benefiting the industry and its customer, the consumer.

ABA member companies produce approximately 85% of all baked goods consumed in the United States. Membership includes large and small producers of all segments of grain-based foods, from bread and rolls to crackers, tortillas, sweet goods and other baked food items.

ABA commends CFTC for its continued efforts to safeguard participating market entities from unreasonable fluctuations within the commodity futures market. The commodities purchased and sold on the Chicago, Kansas City and Minneapolis Exchanges are vital to every ABA member. It is of the utmost importance that these markets maintain their availability to all participants and are protected against unwarranted market manipulation.

As stated in the *Federal Register* vol. 72, No. 224, "Speculative position limits have been a tool for the regulation of the U.S. futures markets since the adoption of the Commodity Exchange Act of 1936 (CEA)." The Act states that "excessive speculation in any commodity under contracts of sale of such commodity for future delivery…causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity, is an undue and unnecessary burden on interstate commerce in such commodity." The Commodity Futures Modernization Act of 2000 (CFMA) states the purpose of those limits is "to reduce the potential

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threat of market manipulation…the board of trade shall adopt limitations or positions accountability for speculators…"

ABA believes the current proposal to increase federal speculative position limits contradicts directives in both the CEA and CFMA, because such action could increase the threat of market manipulation and cause unreasonable fluctuations within the commodities market. ABA has identified three inherent concerns if speculative limits are increased: increased and unwarranted escalation of futures volatility and daily trading ranges; significant financial impact on small businesses that participate in the exchanges; and disproportionately allowing speculators the opportunity to significantly influence the price of commodities, especially wheat.

Increased and unwarranted escalation of futures volatility and daily trading ranges

Examining data compiled from January 2005 to December 2007, the daily average trading ranges for wheat at CBT for the last 12 months have increased 158% (from $0.06 to $0.16), KCBT 132% (from $0.06 to $0.15), and MGE 136% (from $0.06 to $0.14). Further analysis reveals that these ranges have increased even more dramatically over the last six months as compared to 2005 (CBT, 226%; KCBT 195%; and MGE 202%).

Implied volatility has also increased at an alarming rate. Since 2005, the daily volatility of the wheat pit at CBT has increased 34%, KCBT 29%, and MGE 17%. A similar pattern exists when looking at the average wheat futures market volatility within the last six months compared to 2005 (CBT 39%, KCBT 35%, and MGE 31%).

ABA believes these increases in both daily trading ranges and volatility are a result of the increase in speculative position limits implemented in 2005. Implementing a new increase could exacerbate this situation even more.

Significant financial impact on small businesses

ABA is also concerned small businesses could be adversely affected if speculative limits are increased. As stated in the *Federal Register* Vol. 72, No 224, "the Commission believes that raising limits would only impact large traders and thus, the action taken will not have a significant impact…on small entities." Since increasing speculative limits in 2005, the required wheat hedging margins at the CBT have increased 114% from the initial $700 per contract to the current requirement of $1500 per contract. During a nine day time span in October 2006, these required margins were raised by $450, a 56% increase due to the upward volatility of the wheat market. Any increase in hedging margins or the financial outlay necessary to satisfy margin calls requires businesses to shift monetary resources to this unanticipated requirement.

ABA contends that if speculative limits are increased as proposed, hedging margins will likely continue to increase, requiring small businesses to allocate more financial resources to this portion of their business to the detriment of their core business monetary needs. This could possibly force a country elevator, small flour miller or regional baker to alter their hedging strategies to the point where they will look at alternative hedging mechanisms or forego hedging in the agricultural futures market altogether. Either path could cause significant additional risk to the business owner.

Disproportionately allow aggregate traders the opportunity to significantly influence the price of commodities, especially wheat

ABA believes that increasing the speculative position limits for most commodities, especially wheat, could also increase the risk of a few speculators controlling large portions of the market. If these new speculative limits are enacted, a single speculative entity could purchase or sell over 20% of last year's soft wheat crop, over 7% of last year's hard wheat crop and over 16% of last year's spring wheat crop.

Based on recent data, CBT wheat futures open interest is approximately three times this year's U.S. soft wheat production. It is possible that if these new limits are imposed, CBT wheat futures open interest could balloon to five or six times the average U.S. soft wheat production. This increase in futures volume traded has the significant potential to raise the volatility above safe and equitable market levels. With these proposed increased limits, ABA believes that the wheat markets have the potential to be less competitive and efficient. Also, price discovery and risk functions could be jeopardized due to the potential for market manipulation by a relatively small number of speculators with a misappropriate market presence in the wheat futures.

Summary

ABA believes increasing the speculative position limits for commodities bought and sold on the Chicago, Kansas City and Minneapolis Exchanges would not be beneficial to the original producers and users of the physical product. This proposal moves away from the original intent of the exchanges, which was to allow commodity producers to sell their product to entities, including bakers, who use the physical product. This proposal, if enacted, could also increase market volatility, decrease market participation and create a situation where a few speculators could control major portions of the wheat market. Overall, ABA believes the proposed increase in speculative position limits will further fuel an already volatile commodity market and is not in the best interest of market users, including the baking industry and consumers.

ABA thanks you for your time and consideration of these comments on this issue of key importance to the baking industry. If you have any questions regarding ABA's position on this issue, please contact Cory Martin, Federal Government Relations Manager, at (202) 789-0300 / cmartin@americanbakers.org.

Sincerely,

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