LouisDreyfus
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November 5, 2009

Dear Sir/Madame:

Subject: CME proposal for Variable Storage Rate on Chicago wheat futures

This letter is addressed to the CFTC in regards to the CME proposed changes to Chicago wheat futures in their attempt to solve issues related to convergence. Louis Dreyfus Commodities is a major exporter and merchandiser of US Wheat and has been an active participant in the CME's wheat futures contract.

It is our belief that the Variable Storage Rate (VSR) proposal put forth by the CME is unique and will likely help in achieving the ultimate goal of convergence, but in order to have a timely impact it must be enacted swiftly. We would also point out the VSR is not an end all solution and may prove as only another tool addressing the convergence issue and masks the more fundamental problems with the wheat futures contract.

The industry has seen soft wheat diverge from futures during the last 2-3 years and unfortunately it has left many questioning the function of the CME contract as a risk management tool. After years trying to fix the convergence issue and finding that all prior fixes have in fact not led to a remedy, we believe the CFTC should not accept a proposal that allows implementation against the September contract. The very essence of this "fix" is to prompt convergence through a punitive and incremental penalty; therefore, a September implementation will not have any impact until 2011. The industry simply cannot continue to have such a severe disparity between cash and futures. The uncertainty in cash values has left many elevators and commercial companies unsure of where to bid farmers for new crop wheat supplies. In some areas it has even resulted in farmers choosing not to grow wheat due to the fact they cannot find a forward price. We have witnessed numerous industry meetings, CFTC meetings, and committees formed to study and attempt to address the damaging results of this convergence problem. It appears very clear that precedence is set for the CFTC to take emergency action in this matter.

VSR could have some important implications on convergence by providing even greater incentives for elevators to be purchasing SRW inventories against a possible further increase in storage rates. The fact that storage rates are set by the exchange and not allowed to fluctuate prevents the nearby futures contract from moving lower to where cash prices are trading. VSR helps address this problem by allowing storage rates to be dictated by the market. However, it is imperative that these changes happen quickly in order to prevent an even great convergence problem when the US harvests next year's crop. Waiting over a year to implement a possible solution to the Chicago wheat contract is simply unacceptable.

In addition to the discussion about VSR we feel it is important that the CFTC is again made aware that the disparity in the wheat market is largely brought upon by the ever growing presence of index funds in the commodity arena. The problems in Chicago wheat are unique because it is the only market where index funds own an inordinate amount of annual production and total supplies. The table below shows how significant this ownership is vs. other the other grain markets.

INDEX FUND OWNERSHIP VERSUS ANNUAL PRODUCTION

	Index Fund Size		Annual Production	
Commodity	# contracts (1,000 ckts)	Bushels owned (million bushels)	2009 Production (million bushels)	Index Fund % ownership of Annual Production
Wheat (SRW)	173,000	865	404	214%
Corn	354,000	1770	13,103	14%
Soybeans	154,000	770	3,250	24%

As one can see the index funds control more than twice the annual production of SRW. Some academics have argued that this does not distort the marketplace because the index funds never consume or take delivery of this product, but this conclusion is incorrect. The fact that they are always present in the marketplace is exactly what causes the types of distortions seen in the wheat market over the last 3-4 years.

The index fund length in the wheat market essentially points out that there must always be more than 2 years of annual production hedged (an offsetting short position) to accommodate this index fund length. Essentially index fund length is artificial demand which in turn leads to artificial price supports. These artificial price supports prevent US wheat from competing globally leaving US basis levels trading at severely weak levels. US inventories are forced to build to very large levels as the market attempts to find a balance between US Soft wheat supplies and this artificial index fund demand.

The table also shows that similar problems could easily develop in other markets if ownership were to continue to rise and index funds were to own a larger share of annual production in other commodities. It is our belief that the academic studies put forth by the CME have largely been flawed as you cannot simply study the changes in index fund positions versus price changes. The real effect of index fund ownership is that fact that it is long lasting and static meaning every year the market must find a way to accommodate this new piece of demand.

For the reasons outlined above a contract change such as VSR will certainly have an impact on convergence in SRW. It creates greater incentives for elevators to bid and store SRW stocks. The changes also allow for storage rates to become a better reflection of the market and over time allow the nearby futures contract to decline towards cash values. However, early implementation is critical as the market needs to determine the impact of these changes prior to handling new crop supplies. We would suggest the proposed contract be implemented on the March, 2010 futures contract. Additionally, we feel the CFTC needs to consider the impact of the index fund and the role they have played in the convergence problems seen with the Chicago wheat contract as well as the risk that problems develop in other commodity markets.

Sincerely,

Steve Campbell
Vice President
Louis Dreyfus Commodities