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AFR Bulletin: The CFTC's Proposed Rule on Position Limits

Financial speculation on commodities like oil and food is driving up consumer prices from the gas pump to the grocery store. To bring it under control, we need workable position limits. But the verdict is in – the CFTC's proposal needs to be strengthened to do the job. Below are links to comments from Main Street businesses that use commodity markets to hedge their legitimate business risks, as well as public interest organizations concerned about the impact of excessive speculation. The comments all agree on two key points:

- The past decade has seen a massive increase in speculative interest in U.S. commodity markets, which has had a major impact on volatility and prices.

- The "concentration limits" for individual traders proposed by the CFTC will not be effective in limiting this speculation. We need an overall limit on total speculation.

A Massive Increase In Commodity Speculation Has Impacted Prices And Volatility

Some speculation in commodity markets is healthy, to provide liquidity. But recently financial speculation has exploded far beyond historical levels. Real economy hedgers of business risk have traditionally constituted the great majority of commodities market interest, but today speculators are responsible for over two-thirds of activity in many markets. A recent Goldman Sachs report implies that speculation is responsible for $21 to $27 of the current cost of a barrel of oil – a speculation premium of about 20 percent. Speculation has an especially pronounced effect on volatility, which drives up the cost of risk management for commodity producers.

The comment letter that Better Markets submitted on the CFTC position limits proposal contains extensive research and documentation of this increase in speculation and its impact on prices. A comment from Professor Michael Greenberger, a former director of the CFTC's Division of Trading and Markets, also describes the growth in speculation and its effects. Other comments testify to the impact of speculation in specific markets from diesel fuel (the American Trucking Association) to agriculture (Food and Water Watch and the family farmers of the National Farmers Union).

The CFTC's Individual Trader Limits Are Not Enough – We Need To Limit Overall Speculation

The CFTC rule would limit any one trader's spot month position to 25 percent of the total financial interest in a commodity. While limiting individual trader positions does restrict the ability of a single trader to manipulate the market, it does not limit the total market speculation. Many different traders holding an interest of up to 25 percent of the market will still permit total speculative interest to remain enormously in excess of business-related hedging interest.

Comments from all the organizations cited above, as well as Americans for Financial Reform and Public Citizen, the Air Transport Association, the Petroleum Marketers Association of America, and Maryknoll all call for the imposition of a cap on **total** commodities speculation, not just individual trader positions. Such a cap should limit the speculative activities of large passive investors (such as commodity index funds), and be set at a level that would allow sufficient liquidity for hedgers without causing excessive price volatility.