



**Statement of Justin Towery
Merchant Member**

Parkdale, Arkansas

On behalf of

USA Rice Federation

and

US Rice Producers Association

**Before the
Commodity Futures Trading Commission
Agricultural Roundtable
Washington, DC**

April 22, 2008

On behalf of the U.S. rice industry, we appreciate the Commodity Futures Trading Commission (CFTC) conducting a forum recently to discuss the current state of the futures market and to gather information and suggestions from market participants on possible ways to address this situation. Thank you for the opportunity for Mr. Justin Towery to participate in the forum. We would like to take this opportunity to provide some additional and more detailed suggestions in this regard.

As you know, the futures markets are intended to serve the primary roles of price discovery and risk management for producers and users of agricultural commodities. Unfortunately, for the last several months the markets have been volatile and unsettled, resulting in a divergence between cash and futures prices and significant increases in margin requirements. This has

been observed across almost all agricultural commodity contracts on the various exchanges, but we will focus our comments on the rice market and the Chicago Board of Trade rice contract.

There are a number of fundamental factors in the market that are leading to higher rice prices including: tighter global supply based on lower production due to weather events and acreage shifts to other crops and increased demand; increased costs of production; and increased energy costs that lead to higher storage and transportation costs. The presence of all these factors should lead to convergence of cash and futures prices, but we are experiencing a lack of convergence due in part to increased participation by speculators and commodity index funds in the market. Speculator participation is important to provide liquidity to the market, but there must be limits on participation. There have been instances of funds owning more of a crop on paper than will be produced during that crop year. This level of participation has hampered the price discovery role of the market, has damaged the cash market for rice, and has diminished rice producers' profitability.

We are concerned that this lack of convergence will continue as long as speculators and funds remain in the market to the current degree as unrestricted buyers. As a result, we will see fewer and fewer commercial marketers offering forward pricing opportunities due to the continued widening of the basis and greatly escalating margin requirements. Many commercial market participants have already exhausted their working capital and credit lines available for margin requirements and are therefore no longer in the market. This is particularly damaging to producers as they are no longer able to forward price their expected harvest, leaving them exposed to significant price risk. Producers are facing this price risk at a time of record high input costs. In fact, many producers are seeking to lock in their prices on input costs for the 2009 crop, but are unable to do the same for their expected crop production for 2009. Because of this, it is clear that the futures market is no longer performing one of its primary functions – hedging and price risk management.

In order to maintain the integrity of the market, it is important to provide increased transparency of market activities. **One specific action that we recommend the Commission take is to add rice to the weekly CFTC supplemental Commitment of Traders report. In doing so, the Commission should also consider reporting categories for speculators and funds that are separate from the traditional hedgers.** This would help to provide a more comprehensive view of what is occurring in the rice futures market.

We are of the opinion that the rice market is being “cornered” in a non-traditional sense – not by one market participant – but by the fact that hedgers can no longer afford to take short positions (sell) in the market while speculators and funds continue to take long positions (buy), creating a “demand” market in rice that is self-fulfilling.

We completely agree that margin requirements must be sufficient to insure performance, however we also suggest the Commission consider that only producers, processors, merchants (those that deal in the physical commodity) be considered hedgers for determining necessary margin requirements on this category of market participants. On the other hand, index, pension, and other funds not tied to the physical commodity should be considered speculators

with different margin requirements and separate limits imposed. Again, due to the increasing margin requirements resulting from increased market volatility, more and more market participants are exiting the market as their available capital and lines of credit are becoming increasingly stretched to the point they can no longer afford to hedge their price risks. **We suggest the Commission consider linking the margin requirement to both the price level and the amount of market volatility. While it is important to insure there is adequate margin to cover any default, we believe you should also consider a higher margin requirement for speculators than hedgers.**

Another recommendation we would like the Commission to review is the possible need for additional delivery points for rice and also consider raising the storage rates. Currently, the delivery system for rice is very limited and we believe adding delivery points would also help improve convergence. In addition we would urge the CFTC to review whether the use of cash settlement in the rice futures contracts would better serve producers, hedgers, and others using these vital markets.

In summary, we believe that the participation of speculators (funds) in the market is leading to increased volatility and therefore more oversight by the Commission, including increased market transparency, could help to address this problem. As the increased margin requirements, volatility, and lack of confidence cause more and more commercials to withdraw from the market, the divergence between cash and futures prices will only worsen. If and when the funds begin to withdraw from the market, we could be in store for a severe price correction that could lead to significant financial losses and instability, which could further prohibit participation by commercials and producers. **Speculators should be defined as those not tied to the physical commodity and we believe an excessive level of participation by speculators is at least partially responsible for the current market situation. In addition, increased speculative margin requirements and tighter position limits for speculators could also help improve the situation.** Otherwise, we believe the market will continue to be lacking in its ability to perform its two primary functions of price discovery and hedging. **The necessary steps must be taken to ensure that commercials can reenter the market and perform their role as hedgers for the physical commodity.**

We appreciate the opportunity to share these views and suggestions. We look forward to working with the Commission to help address the current market situation so that all in the rice industry can once again have confidence that the futures market will meet the industry's price discovery and risk management needs. **As the Commission reviews the current situation, if you find that any additional authority is needed to help address this situation, then we look forward to working with you and Congress to provide the necessary authority.**

Thank you again for the important role you serve in the regulation and oversight of the agricultural futures markets. If you have any questions or would like any additional information, please contact Mr. Reece Langley at the USA Rice Federation at 703-236-1471 or rlangley@usarice.com, or Mr. Fred Clark on behalf of the US Rice Producers Association at 202-448-9500 or fred@cgagroup.com.