

**MINUTES OF THE JULY 19, 2023 MEETING OF THE
U.S. COMMODITY FUTURES TRADING COMMISSION'S
AGRICULTURAL ADVISORY COMMITTEE**

The Agricultural Advisory Committee (“AAC”) convened for a public meeting on Wednesday, July 19, 2023, at 9:00 a.m., at the U.S. Commodity Futures Trading Commission’s (“CFTC” or “Commission”) Headquarters Conference Center, located at Three Lafayette Centre, 1155 21st Street., N.W., Washington, D.C. The meeting consisted of one panel and a presentation. The panel discussed ways to improve access to futures markets. The presentation addressed Mississippi River disruptions to grain flows and markets.

AAC Members in Attendance

Scott Herndon, Field to Market, AAC Chair
Buddy Allen, American Cotton Shippers Association
Joe Barker, National Council Farmer Cooperatives
Chris Betz, Michigan Agri-Business Association
Robbie Boone, Farm Credit Council
Layne Carlson, Minneapolis Grain Exchange
Gerald Corcoran, Futures Industry Association
Patrick Coyle, National Grain and Feed Association
Ed Elfmann, American Bankers Association
Edward Gallagher, National Milk Producers Federation
Thomas Haag, National Corn Growers Association
H. Thomas Hayden, Jr., Commodity Markets Council
Jered Hooker, American Soybean Association
Bryan Humphreys, National Pork Producers Council
Jeff Lloyd, Archer Daniels Midland
Michelle Mapes, Green Plains Inc.
Mark McHargue, American Farm Bureau Federation
Cynthia Nickerson, U.S. Department of Agriculture/Office of the Chief Economist
Michael Ricks, Cargill
Bella Rozenberg, International Swaps and Derivatives Association
Derek Sammann, CME Group
Troy Sander, National Cattleman’s Beef Association
Liam Smith, Futures Industry Association, Principal Traders Group
Curt Strubhar, Grain and Feed Association of Illinois
Wes Uhlmeyer, Demeter Logistics
Hayden Wands, American Bankers Association
Ryan Weston, American Sugar Alliance
Jason Wheeler, USA Rice Federation

CFTC Commissioners and Staff in Attendance

Rostin Behnam, Chairman and AAC Sponsor
Christy Goldsmith Romero, Commissioner

Summer K. Mersinger, Commissioner
Caroline D. Pham, Commissioner
Swati Shah, Special Counsel, Division of Market Oversight, and AAC Designated Federal
Officer (“DFO”)

Invited Speakers in Attendance

Gerald Corcoran, Futures Industry Association
Curt Strubhar, Grain and Feed Association of Illinois
Layne Carlson, Minneapolis Grain Exchange
Susan Olson, Action Intel

I. Opening Remarks

Ms. Shah called the meeting to order. Chairman Behnam, the AAC Sponsor, gave opening remarks. He recognized fellow Commissioners, Ms. Shah, the DFO, and Mr. Herndon, the AAC Chair, and all participating attendees for their service. He then outlined the two main topics of discussion for the day: (1) improved access to markets and (2) the Mississippi River disruptions.

On access to markets, Chairman Behnam noted that the Committee has been concerned about the trend of higher concentration in the agricultural markets and fewer points of access for smaller end users. He stated that the CFTC’s goal is to investigate why these trends are happening and to work with commercial end users to reverse them. He also emphasized that since futures markets provide important risk-management options, providing fair and open market access is a top priority for the CFTC. Regarding the Mississippi River, Chairman Behnam noted that it represents a key artery for American agriculture – thus to maintain its effective function is paramount, acknowledging that while there are climate-related variables beyond the CFTC’s control, the agency is willing to work with other U.S. agencies to address challenges and arrive at solutions.

Commissioner Goldsmith Romero echoed Chairman Behnam’s remarks about the importance of the AAC in helping the CFTC understand the challenges facing farmers and producers. In particular, Commissioner Goldsmith Romero was interested in hearing about developments in Mississippi River barge traffic, acknowledging that extreme weather such as record rain and melting snowfall would lead to flooding and lock closures, barge shipping problems, disruptions in the deliveries of grain, soybeans, and fertilizer, thus detrimentally impacting the livelihood of farmers and producers. She emphasized that the CFTC is fully committed to working closely with farmers and producers to find sustainable solutions.

Commissioner Mersinger followed by sharing a personal anecdote about her father, a farmer in South Dakota. She described how this year’s drought is the worst he has seen in his 60 years of farming, then went on to discuss the broader impact of the drought – how it disrupts barge traffic, reduces grazing land for livestock, and places a higher demand on feedstock, therefore creating a deleterious effect on the agriculture industry and the broader economy as a whole. Commissioner Mersinger then highlighted the importance of derivatives markets during

times of economic hardship, explaining that that the CFTC's job as regulator is to ensure that these markets function well in their role of providing sound price discovery and hedging tools.

Commissioner Pham commended the AAC for studying ways to improve agricultural participants' market access, acknowledging that futures commission merchants ("FCMs") have often cited challenges to the business model, such as the high costs of technology and compliance. She also noted that the implementation of the standardized approach to counterparty credit risk (SA-CCR) under Basel III has led to higher capital requirements for customer clearing, which may have discouraged certain FCMs from offering clearing services to end users. She warned that the continued consolidation of the clearing ecosystem could pose problems for agricultural hedgers and create systemic risk by amplifying the consequences of a major provider's failure or withdrawal, and concluded by affirming the CFTC's commitment to alleviating market access issues.

Ms. Shah then proceeded with the roll call and turned the meeting over to AAC Chair Herndon, who introduced Mr. Corcoran, Mr. Strubhar, and Mr. Carlson as speakers for the panel on the role of FCMs and participants' access to the futures markets.

II. Panel: Improving Access to Futures Markets

Mr. Corcoran, representing the FIA, began by thanking the Commission for the opportunity to discuss the role of FCMs in providing farmers and ranchers with access to futures markets. He noted that FCMs play a critical role in the agricultural end user community by providing a central point of access for futures exchanges and clearinghouses, maintaining checks and controls, collecting margins, guaranteeing clients' obligations, and contributing to default funds. Mr. Corcoran then discussed the decline in the number of FCMs providing clearing services to customers. He attributed this decline to mergers and acquisitions, the impact of the 2008 Financial Crisis, the cost of keeping up with technology and capital requirements. He also noted that there are several barriers to entry for new FCMs, including the high cost of connecting to exchanges and building necessary technology infrastructure.

However, Mr. Corcoran believed that the existing FCM network is strong and does provide farmers and ranchers with equal access to the marketplace. He highlighted the critical role of introducing brokers (IBs) within this vast network, in connecting small and medium-sized end users with risk management tools in the futures and derivatives markets. The FCMs in turn play a quasi-SRO role in supervising and managing the IBs' regulatory compliance.

Mr. Corcoran also discussed the importance of education in the end user community. He noted that FCMs offer education about trading strategies, including courses about hedging with agricultural futures. Mr. Corcoran then highlighted the growing importance of financial risk management and hedging tools, not just for farmers and ranchers, but also for energy companies that turn crops into biofuels. He observed that these developments may lead to more participation in agricultural markets by enticing current FCMs to enter these markets or expanding their existing commitments. In conclusion, Mr. Corcoran reiterated FIA's

commitment to providing educational access to the general public and particularly the agricultural community.

Next, Mr. Strubhar, who heads an IB firm, Advanced Trading Inc., expressed concerns about the shrinking number of FCMs willing to take on IB business. He noted that this is an issue for his clients, who often prefer to maintain multiple FCM relationships as a risk mitigation strategy. Thus, Mr. Strubhar had misgivings about the potential for a direct clearing model, which he did not think would be suitable for midsize to smaller entities relying on FCMs for risk management. He believed the auto-liquidation model proposed by FTX is equally problematic for hedging purposes.

Mr. Strubhar concluded by remarking that the shrinking number of FCMs is an economic rather than a regulatory issue, and that his firm would be open to the possibility of forming a new FCM designed for smaller entities if the economics justify it. However, he noted this would likely mean a change in the capital model and a decrease in efficiency for farmers, ranchers, and smaller grain trading companies.

As the last speaker, Mr. Carlson expressed support for open and diverse market access, acknowledging the concern of the agricultural community about the reduction of market access due to increasing consolidation of the FCM and IB industries. He explained that MGEX has flexible rules to ameliorate the access issue since the Exchange does not require FCMs to be clearing members in order to access its markets. This means that FCMs can choose to clear their customers' trades through another clearinghouse. He also noted that MGEX compliance rules and financial requirements are not necessarily more burdensome for FCMs than those imposed by the CFTC and other industry players. Mr. Carlson concluded his remarks by affirming the concept of open access as well as urging for a pragmatic shift, noting that while having multiple local FCMs to choose from is desirable for an end user, if that's not feasible then there are well-qualified FCMs, regardless of location, to address a farmer's risk management concerns.

AAC Chair Herndon thanked the speakers and opened the floor for questions and comments. Mr. Sammann expressed his appreciation for the speakers' remarks on the needs and interests of the end user community. He said that small farmers and ranchers form the core backbone of CME Group's global commodities franchise and that they need to have open access to CME markets. He also emphasized CME Group's dedication to educating farmers and ranchers on the benefits of using the derivatives markets as risk management, citing several examples of CME Group's grassroots efforts, such as scholarships for state fairs and 4-H clubs, educational resources for trading communities, and a strong relationship with the National Association of Farm Broadcasters.

Mr. Allen agreed with the previous speakers and thanked the committee for taking up this important topic. He said that ACSA represents a wide range of cotton market participants, from large agri-businesses to small country cotton gins, noting that access to FCM services varies depending on each market participant's size and sophistication. Specifically, Mr. Allen indicated that large self-clearing commercial entities have different needs than mid-size commercial entities that may not have the capital to perform these services internally. He also

said that local producers may rely on merchandisers to perform risk management services on their behalf. In addition, he disclosed that, due to a lack of experience and other factors, hedging is done less by farmers today than it used to be decades ago, and he expected this trend to continue.

Mr. Gallagher commented on the challenges faced by dairy farmers in accessing FCM services. While smaller dairy farmers have easy access to risk management programs through the USDA, he explained that farmers-owners from larger dairies depend on a complex aggregation program designed by the Dairy Farmers of America that involves aggregating milk production from a variety of farms and using forward contracts to manage risk. He said that as the FCM industry consolidates, there are fewer entities interested in handling business from large dairies. Overall, Mr. Gallagher agreed with the other speakers that education is paramount, and that he has been working with his organizations to educate its members on the importance of consistently using risk management tools to protect their financial well-being.

Mr. Coyle commented that the NGFA has been concerned about the FCM consolidation trend and its potential impact on market access. He said that the NGFA has not seen a critical lack of access yet, but there is some concern that the trend could continue and lead to problems in the future. Mr. Coyle indicated that the NGFA is monitoring the situation and will continue to advocate for equal competition and market access for all market participants.

Mr. McHargue commented that farmers are increasingly looking to merge crop insurance products with hedging options to get full coverage. Since it has become more difficult for individual farmers to be experts in all aspects of agriculture, he reported that farmers are collaborating more frequently with other producers, co-ops, and other industry groups, to help them gain a holistic and symbiotic view of risk management.

Chair Herndon then solicited comments from Chairman Behnam and attending Commissioners. Commissioner Goldsmith Romero asked Mr. Corcoran if he envisions any sign that may halt or reverse the trend of declining FCMs. Mr. Corcoran said that the trend seems stable, as he does not see market participants exiting the FCM space, but that the barrier to entry is very high, especially with the compliance requirements that have been put in place since the 2008 Financial Crisis. Mr. Corcoran further acknowledged that since the agricultural futures markets are very competitive, commission rates can be driven down to a level that makes it unattractive for some FCMs to expand into agriculture. Mr. Corcoran concluded by saying that there is still plenty of access for farmers and ranchers today, but it could become a problem if more FCMs exit the network.

Chairman Behnam followed up on Mr. Corcoran's and Mr. Strubhar's comments about the economics of the FCM business. He asked Mr. Strubhar about the impact of higher interest rate on the FCM business model and whether that has changed his view on starting a new FCM. Mr. Strubhar said while the higher interest rate has made some FCMs more robust and efficient, it has also increased the cost of capital for new FCMs. While not inclined to start a new FCM, Mr. Strubhar said he is still open to this idea if existing FCMs continue to stay strong and are willing to take on new clients and other IBs. Chairman Behnam then commented on the role of education for both agricultural producers and their intermediaries as a way to improve market

access. He proposed the CFTC can play a role in this area by incentivizing IBs on the benefits of offering futures market services to producers.

Mr. Corcoran agreed with Chairman Behnam and the other speakers that education is important to ensure that producers have access to futures markets. He said that the futures industry has a platform called Futures Fundamentals that can be used to promote education to IBs. In addition, Mr. Corcoran said while the number of IBs has declined significantly over the past fifteen years, those who have decided to remain in the industry are “top-notch.” Finally, Mr. Corcoran posited that FCMs should not rely on interest income as a primary source of revenue since such income is not as important to FCMs as it once was because customers are now more likely to invest their money elsewhere.

Commissioner Mersinger then asked if there have been any partnerships between the futures industry and community banks to educate farmers and ranchers about hedging and risk management. Mr. Strubhar replied that his IB firm conducts regular meetings with community banks and other entities to provide education on hedging and market fundamentals. He also commended the CFTC for a joint conference with Kansas State University a few years ago to educate industry participants, and hoped that the CFTC would resume this program in the near future. In addition, Mr. Strubhar also commended the NGFA and the State Grain and Feed Association for their instrumental speakers’ programs on hedging and risk management.

Mr. Sammann agreed with Mr. Corcoran and Mr. Strubhar that risk management education is important to farmers and ranchers. He said that the Futures Fundamentals coalition is a good example of how the industry can work together to provide education to all market participants. Mr. Sammann also noted that there are two parts to this education: content and distribution. While CME Group can provide content, it would need the support of other industry partners to distribute that content to farmers and ranchers. Mr. Sammann also said he would be interested in hearing the Commission view on how the agency can promote access of relevant educational programs.

The Q&A portion concluded. Chair Herndon then introduced Dr. Olson as the speaker for the presentation.

III. Presentation: Mississippi River Disruptions to Grain Flows and Markets

Dr. Olson indicated her presentation would illustrate the recent disruptions to the lower Mississippi River as it relates to grain flows and markets. Dr. Olson then discussed the data sources she had collected to create her metrics, including automatic vessel tracking data, USDA data, geospatial data, and data from the American Commercial Barge Line Association.

Dr. Olson then introduced the metrics employed in her research: tow direction and turn time. Tow direction shows whether a tow is going southbound to New Orleans or northbound up the river. Turn time measures how long it takes a tow to travel from Vicksburg to New Orleans and back. She also discussed other metrics that she has been tracking, such as tow count, river gage data, Vicksburg spot barge freight, CBOT soybean futures, and export inspection volumes.

Then Dr. Olson presented data on the effects of Hurricane Ida in 2021 and the 2022 drought on the Mississippi River barge freight market. She showed that both events led to elevated barge freight rates, reduced tow count, and longer turn times. Specifically, the soybean futures spread widened during the period of time when Hurricane Ida disrupted the Mississippi River. This suggested that the market was expecting higher prices for soybeans at delivery because of the higher transportation costs in hazardous weather. Equally serious were the disruptions caused by low water levels on the Mississippi River in 2022, since they created two main categories of disruptions: (1) navigation/bottleneck issues, and (2) barge fleet access issues. Dr. Olson explained how the drought led to a significant reduction in the number of towboats that were able to transit the river, as the reduced river channel size made it difficult for towboats to navigate and for barges to be loaded and unloaded. She thus established that the drought, like Hurricane Ida, caused elevated barge freight rates due to the higher cost of transporting grain via the river route. Dr. Olson also demonstrated that these climate-related disruptions have had a significant impact on grain exports, although the trend has begun to reverse in 2023.

Chair Herndon then opened the floor for discussion. Mr. Haag thanked Dr. Olson for her presentation and expressed concerns about the low water levels on the Mississippi River in Minnesota. He said the barges have begun to transport less goods due to low-level water, which will likely hurt the timely shipment of grain and other commodities in his state.

Mr. Ricks worried that the competitive nature of the global agricultural market is making the low water conditions on the Mississippi River even more problematic for US farmers. In the past, the US was the price setter for agricultural commodities, so US farmers could pass on some of the added costs to consumers. However, since today the US is often not the primary supplier of agricultural commodities, buyers can easily switch to suppliers from South America. This means that US farmers would have to absorb the added costs, which can significantly reduce their profits.

Mr. Allen agreed with the previous commenters that the low water levels on the Mississippi River are a problem. Acknowledging that river infrastructure is critical, and that the US is behind on investment in dredging, he supported advocacy efforts to increase investment in dredging.

Mr. Herndon then solicited comments from Chairman Behnam and attending Commissioners. Chairman Behnam asked Dr. Olson if she envisions any measurable shifts in the way the market or infrastructure has responded to weather events of the past decade, and whether these changes have made the agricultural industry more resilient to climate disruptions, or have these disruptions been so unique that it would be difficult to generalize about trends in either market or infrastructure.

Dr. Olson responded that it is difficult to gauge the market's response to weather events because each event, while may seem frequent, still poses distinct and irregular patterns. From a lay perspective, however, Dr. Olson observed that it is remarkable how quickly the industry was able to recover from Hurricane Ida. She indicated that she would like to devote further research to the issue and respond to the AAC as appropriate.

Commissioner Goldsmith Romero then asked Dr. Olson how extreme weather events, such as the spikes in temperature and precipitation seen in past years, could be used in market forecast. Dr. Olson responded that the AAC's next task is to develop reliable models to illustrate the duration of both weather-related events and their impact on the markets. She acknowledged that this is a complex task, as there are many overlapping factors that can affect the markets. However, a rigorous scientific approach could be achieved by separating data into training and testing sets, so a model can be thoroughly trained on historical data before being exposed to new input. This helps to ensure the model's reliability.

Commissioner Mersinger reiterated Mr. Allen's point that river management is a complex issue with many stakeholders. She concluded that the federal government has an important role to play in investment decisions that can strengthen river infrastructure and improve freight navigation down river.

IV. Closing Remarks

Chair Herndon thanked all participants. Ms. Shah recognized Chairman Behnam, who gave brief closing remarks.

Ms. Shah adjourned the meeting at 10:48 a.m.



10/30/23

Scott Herndon
AAC Chair

Date