SKYLAR Capital Management

April 27, 2020

Submitted Via Email

TO: Hon. Pat Roberts, Chairman
U.S. Senate Committee on Agriculture, Nutrition, & Forestry

Hon. Collin C. Peterson, Chairman
U.S. House Committee on Agriculture

Hon. Dr. Heath P. Tarbert, Chairman and Chief Executive
U.S. Commodity Futures Trading Commission

Terrence A. Duffy, Chairman and Chief Executive Officer
CME Group

FROM: William O. Perkins, III
Skylar Capital Management LP

RE: Market Participation Limits Impair Liquidity and Magnify Price Volatility

My name is William O. Perkins, III, and I am the founder and CEO of Skylar Capital Management LP ("Skylar"), a commodity pool operator registered with the U.S. Commodity Futures Trading Commission ("CFTC"). Founded in 2012, Skylar operates a hedge fund with over $100 million in assets under management. Further, Skylar is an active trader in and an important provider of liquidity to the U.S. energy derivatives markets. Prior to starting Skylar, I spent the first part of my career as a derivatives trader at other physical and financial U.S. energy trading firms after graduating with an electronic engineering degree from the University of Iowa. In this letter, I explain that the recent extreme volatility in oil futures contract prices has been due in large part to unnecessary restrictions and artificial limitations imposed by the CME and CFTC that force financial trading firms like Skylar to exit the market during the time period in which liquidity is needed most. The dramatic moves in oil futures prices on April 20 and 21 was unfortunate for many reasons – not least of which is because it was avoidable. Congress must urge the CFTC to ensure that responsible risk taking financial

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firms are able to participate in markets, and not unnecessarily restricted or artificially restricted, when their liquidity is needed most.

On the afternoon of Monday, April 20, 2020, I and the rest of the market watched with suspended disbelief as the price of CME's NYMEX May 2020 WTI Crude Oil futures contract, which had opened the trading session at a price just under +$18 per barrel, plunged in a flash crash to a completely irrational and shocking closing price of approximately -$37 per barrel. While many experienced traders expected the possibility that prices for the May 2020 contract could go modestly negative at some point, there is no rational or logical explanation for the price to have gone all the way to -$37 per barrel. That price level did not reflect any version of the reality of supply and demand in underlying physical markets—instead, it reflected a broken derivatives market structure where ready-and-willing buyers were forced to stand on the sidelines due to artificial limitations placed on market participation by the CME and the CFTC, either directly or via related restrictions imposed by brokers. Perhaps even more bizarre (but not unexpected to those forced to sit on the sidelines), the same contract rebounded the next day to settle at approximately +$10 per barrel. By my very rough estimate, if the CME and CFTC had permitted financial trading firms to freely participate in the market on these two days, these prices swings would have been dramatically reduced.

When the global benchmark contract for oil fluctuates in $50 swings two days in a row, something is broken—very broken. In fact, the status of that contract as the "global benchmark" is brought into question. While a lot of physical crude traded at negative prices on April 20, that is only because many physical pricing conventions have methodologies ultimately tied to the NYEX crude contract. Where that contract fails, due to a forced lack of liquidity, all of those pricing methodologies have to be re-evaluated. Producers cannot be stuck flowing crude into pipelines at negative prices, in locations that have plenty of capacity and demand, just because the NYMEX contract experiences a flash crash.

Nonetheless, the CFTC continues to pursue policies and rules that will compel exchanges to increasingly force critical liquidity out of the derivatives market at the times they are needed most. For example, *see* the CFTC's current proposal to impose a sweeping new regime of Federal position limits restrictions to twenty five different agricultural, energy, and metals derivatives markets. Rather than solving existing problems, these rules would only

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further restrict financial firms from trading during the time periods in which liquidity is most critical. This liquidity, provided by financial trading firms and hedge funds like Skylar, is essential to balance, check and smooth the otherwise uncontrollable trading that can occur when only commercial firms and unsophisticated trading participants are active in a market. It is imperative that the CME, the CFTC, and Congress move as quickly as possible to eliminate existing impediments and avoid pursuing any new rules, limits, or other restrictions that shut down ready and willing market participants at the very times when their liquidity is crucial to efficient and transparent markets.

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I stand ready to provide additional information and to answer any additional questions that may assist the CME, CFTC, or the Committees and their staff in considering this letter.

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Sincerely,

William O. Perkins, III
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