August 31, 2020

Dear Commissioners and Commission Staff:

Thank you for the opportunity to submit comments regarding the Chicago Mercantile Exchange's (CME) Request for Approval: Amendments to Daily Price Limits Rule of the Live Cattle and Feeder Cattle Futures Contracts (CME Submission No. 20-352).

The CME Feeder Cattle Futures specify cash settlement based on cash transactions of steers between the weight of 700 and 899 pounds. These feeder cattle are destined for finished feeding operations. Thus, their prices are derived heavily from their ultimate price as finished, fed, live cattle. The CME is right to recognize their derived demand in formally linking the Feeder Cattle Futures' daily price limits as a ratio of the Live Cattle Futures' daily price limits.

Within the submission, CME states: "Limit settlements can inhibit price discovery and can hinder market participants when entering, exiting, and/or rolling positions." There are few good hedges for liquidity providers in the cattle contracts. Given the economic connectivity of feeder cattle and live cattle, their futures' markets are reasonably correlated. It is imperative that liquidity providers and commercials be able to intra-commodity hedge/spread between live cattle and feeder cattle futures.

The ratio of the proposed daily price limit is far too small relative to the live cattle daily price limit. The Feeder Cattle Futures contract is specified by an average 800-pound steer contract. Steers of this weight routinely average 1400 to 1450 pounds at finished weight. This means that a $1/cwt change in the live cattle price equates to an approximate $14.25/head value change. That $14.25/head change in live cattle equates to a $1.78/cwt change in feeder cattle price (14.25/8=$1.78). This is a 1.78:1 ratio. The submission uses a 1.25:1 feeder cattle/live cattle ratio. The current static daily price limits (1.5:1 ratio) are closer to the economic realities of derived demand than the submission proposal. In a formal linking of the two product's price limits, the ratio should be 1.75:1, but at the very least 1.5:1. If the ratio is implemented at 1.25:1, it will deter liquidity providers from being able to intra-commodity hedge and spread between the correlated markets. This is an opposite consequence to CME's stated intent of these proposed variable price limits.

Thank you again for the opportunity to share these comments. Please contact me if you would like to discuss them further.

Sincerely,

Joe Kovanda
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