From: Pradyumna Upadrashta <pradsu@gmail.com>
Sent: Thursday, February 18, 2010 7:13 PM
To: secretary <secretary@CFTC.gov>
Subject: Regulation of Retail Forex | 10:1 leverage is a VERY bad idea

To:
Mr. David Stawick, Secretary Commodity Futures Trading Commision
1155 21st Street, N.W., Washington, DC 20581

Dear Mr. Stawick:

The proposed CFTC legislation to limit leverage limits to 1:10 in the forex markets will be disastrous for the US forex market. Currently, a minimum leverage of 100:1 is required to be marginally profitable on currency trades. A typical currency does not fluctuate more than 100 pips (basis points) over the course of a day of trading. By constraining leverage further, this movement is constrained to about 10 pips - it is guaranteed that traders will be barely able to break even at this level. I believe strongly that this will not only stifle the US forex market, but will cause an exodus of larger traders to foreign brokerages, while simultanesouly restricting access for smaller traders that will not have the ability to migrate.

The concept of leverage has been much maligned in the public eye of late due to the widespread misconception that it was leverage that caused the recent financial crisis. It was never the leverage which caused the crisis - but rather, an inability to price illiquid securities in a relatively insulated OTC market place. In a highly liquid and well capitalized global market such as forex, where over $1.4 trillion dollars change hands on a daily basis, a trader's account is marked-to-market virtually instantaneously as market prices are constantly updated to reflect prevailing supply/demand. There is absolutely ZERO risk of a systemic credit failure or a "run on margin" as a trader's account is automatically closed out (margin called) when a broker-dealer determines that there are insufficient funds. All forex trading accounts are settled continuously (or at least at the end of a market "day"), preventing an account from imploding beyond the original margin requirement - this precludes the ability of traders to "break the bank" ever. In the highly illiquid derivatives market this is not the case, since often the market value of a derivative security cannot be readily determined. In forex, all quoted prices are highly responsive to supply/demand in the broader market.

This new 10:1 leveraging rule is pure political posturing and does not have any basis from a risk management or regulatory point of view.

I do hope that such an unfair legislation will never come to pass, or you can be absolutely certain that the US forex market will come to a grinding halt. It was bad enough when they reduced leverage from 400:1 to 100:1, but reduction to 10:1 is unsustainable and no trader will be able to make a profit, and no market maker will be able to offer a sufficiently attractive commission structure to entice traders to deal with US brokers - it is mathematically impossible to operate profitably at those levels. By reducing leverage down to 10:1, the CFTC is effectively amplifying the cost of a trade by 10x, making any and all forex trading in the US impossible. On top of that, this new leverage increases the risk of a trade 10x as well. Consider that whereas at 100:1 leverage, I risk $1000 for every $100K of currencies traded, that now I have to risk $10,000 for every $100K of currencies traded. This new rule has effectively placed 10x more of my personal capital at risk. There will be (should be!) a mass exodus to foreign markets if this legislation passes.

I would like to stress the point that the practical impact of leverage in a forex account is NOT the same as leverage in other markets. It is absolutely unfair to treat them in the same manner - it is not only irresponsible, but it draws serious concern as to whether the regulators understand what it is they are regulating, when they "throw the baby out with the bath water". It is even more unfair to punish the entire trading community for the acts of a few large irresponsible banks. It was stupid to have repealed glass-steagal to begin with, and this new piece of legislation is nothing but politically self-serving. The volcker rule of re-instating a separation between banking and proprietary trading is a step in the right direction. Reducing forex leverage is undeniably a step in the wrong direction.

These illogical and irrational developments in regulation are deeply concerning to everyone in this industry; instead of bringing stability, this may wipe out the industry altogether. I am writing this letter to URGE the CFTC and other concerned regulatory bodies to reject this nonsensical piece of reactionist/populist legislation outright.

As a small trader, I know that I cannot afford to trade under these new regulations, and am seriously thinking about finding a broker elsewhere that can give me better options. I'm very concerned with the bludgeoning approach to regulatory reform that is being practiced right now, when a scalpel is what is required.

I'm not certain how much my input is valued, but there it is, for what its worth. I am certain that there is an entire community that feels the same way. I am guessing that asking CFTC to re-instate the 400:1 leverage allowance is too much.

Respectfully,
A very concerned citizen/trader/investor.

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