The impact upon the economy of discouragement of futures trading

The most serious impact upon the economy, if futures trading were discouraged, would be loss of efficiency in marketing. The greater cost of marketing commodities would be borne by producers and consumers alike.

Another serious impact would stem from the fact that an increasing amount of international trade in commodities has been facilitated by our futures markets. The European or Japanese importer of our grains uses our markets increasingly. The exporters of tropical products to the United States also use our markets. Not only would this business be lost to the United States, but in some instances futures markets in other countries would pick up the business, possibly in addition to business now being done by our domestic commodity trade, which would be transferred to foreign markets. This would not only adversely affect our balance of payments, but would tend to undermine our world leadership in the organization and financing of commodity trade. If the needs of a trade which is international in scope are better served in other countries, the trade will shift to those countries. Last year the Chicago Board of Trade had $55 billion business volume, making it, as it has been for many years, the world's foremost commodity market. This distinction could pass to Liverpool or Rotterdam or Tokyo in the future if our markets are unduly restricted.

Conclusion

There is no doubt but what margin levels substantially higher than present ones would discourage hedging, force resort to other more costly marketing methods, and put futures markets out of business to the detriment of producers and consumers alike. Futures trading grew out of just the marketing methods to which the commodity trade would necessarily revert if the costs of futures trading were made arbitrarily prohibitive. It grew out of those methods as a refinement and improvement of them, in the very sense that it enables marketing at lower cost, which it can only provide with low margins aimed at protecting the clearing house. In the words of one banker who had had much experience financing the grain trade in the manner here illustrated, futures trading is "one of the major economic creations of all time."*

Supplementary statement on stock margin regulations

As supplements to general methods of influencing credit, selective methods, of which margin requirements are the most important, make it possible for the Federal Reserve to reach specific credit areas without imposing stronger general credit measures that might otherwise be appropriate. For example, if an unhealthy use of credit for stock market speculation develops at a time when credit for production and trade is expanding no more than would be considered normal, and when the application of general instruments of regulation (open market operations, change of discount rate and reserve requirements) might do more harm to the country's overall economic activity, the power of the Federal Reserve to regulate stock market credit can be invoked.

The Securities Exchange Act of 1934, Sec. 7. (a), under the heading "Margin requirements" says:

"For the *purpose of preventing the excessive use of credit* for the purchase or carrying of securities, the Federal Reserve Board shall . . . prescribe rules and regulations with respect to the amount of credit that may be initially extended and subsequently registered on a national securities exchange" (([2]) p. 399).

For initial extension of credit such rules and regulations must be based upon a certain standard set forth in the act, but the board is authorized to prescribe such requirements lower than the standard as it "deems necessary or appropriate for the accommodation of commerce and industry having due regard to the credit situation of the country," and such higher requirements as it may "deem necessary or appropriate to prevent the excessive use of credit to finance transactions in securities." (([3]) pp. 35–36.)

The control effected by margin requirements, although bearing directly on the lender, puts restraint upon the borrower and dampens demand. It can be

*Harry L. Wuerth, Vice President, Commerce Trust Company, Kansas City, Missouri, "A Banker Looks at Futures Trading," Proceedings of the Banking Seminar, Chicago Board of Trade, 1961.

[2] *Federal Reserve Bulletin*, June, 1934.

[3] *Annual Report* of the Federal Reserve Board, 1934.