# Limits on futures trading could boost gas prices, expert says

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Proposals to reign in wallet-draining gasoline prices by curbing speculation in oil markets would likely increase costs at the pump instead of trimming them, a University of Illinois economist says.

Scott Irwin argues congressional efforts to curb trading by speculators is a "misguided witch hunt" that ignores the root of America's energy problem – a finite global oil supply that has been stretched thin by surging demand in China, India and other developing countries.

"We need to have a real national debate about issues related to both the demand side and the supply side of our energy use. That's what we need to be focusing on, not speculators," said Irwin, an agricultural and consumer economics professor who testified this month before a House committee considering limits on speculation in futures markets.

The Senate voted unanimously this week to move ahead on legislation to curtail speculation in oil futures markets, which Irwin contends would be a step backward in the battle against $4-a-gallon gasoline prices.

"If the markets become overregulated, they become less efficient mechanisms for transferring risk from parties who don't want to bear it to those that do, creating added costs that ultimately get passed back to consumers," Irwin said.

Dozens of proposals have surfaced to scale back speculation that has exploded in oil markets over the last few years. Billions of dollars have been pumped into oil futures and related over-the-counter derivative contracts, which supporters of trading limits contend has artificially inflated oil prices by 20 to 50 percent.

Irwin maintains that speculation accounts, at most, for a small part of the recent spike in oil prices, based on a recent study of commodity futures markets he conducted with Southern Illinois University agribusiness economist Dwight Sanders.

The study shows that a surge in trading by commodity firms has offset the dramatic rise in speculation, maintaining a market balance of buyers and sellers.

"The bottom line is that the balance between hedgers and speculators in our commodity markets today is very much within historical norms for these markets going back to the 1940s," he said. "We argue that when there's a buyer and a seller, the market will balance itself."

Another key, Irwin says, is that investments by speculators largely amount to "side bets" on the price of oil and other commodities. "They rarely buy and hold physical tanks of crude oil. That's where the price is set," he said.

He says history is dotted with misguided attacks on speculators, including a 50-year-old ban on onion futures trading that producers are seeking to repeal even as limits are being mulled for oil markets.

"We have been here before and we have made now well-documented mistakes in trying to over-regulate markets, so let's not make the same mistake again," said Irwin, who has studied the impact on speculation on commodity futures for nearly 25 years.

Ironically, Irwin says his earlier research dealt with cases where speculators were blamed for driving down farm commodity prices.

"That says something all by itself," he said. "In all big market cycles, when prices are very low, the natural sellers such as farmers will start screaming that speculators are the problem. And when prices are really high, the natural buyers in the market – consumers and processors – are the ones screaming."

"There's a tendency to look for a scapegoat, and speculators are the convenient scapegoat," he said. "But, really, it's a supply and demand issue."

Source: University of Illinois at Urbana-Champaign

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