Commodity

- Commodity means primary agricultural products
- Basic good used in commerce
- Used as inputs in the production of other goods or services

Commodity Market

- Marketplace for buying, selling and trading raw or primary products.
- Two types – Soft commodities and hard commodities
- History dates back to 4500 BC and 4000 BC
- Physical delivery of commodity once the trade is executed

Types of commodity Market

- Precious Metals E.g. Gold, silver, copper etc.
- Agro commodities E.g. Wheat, corn, chilli, turmeric
- Energy commodities E.g. Crude oil, gas
- Soft commodities E.g. Coffee, coco
- Live stock commodities E.g. Pork, cattle

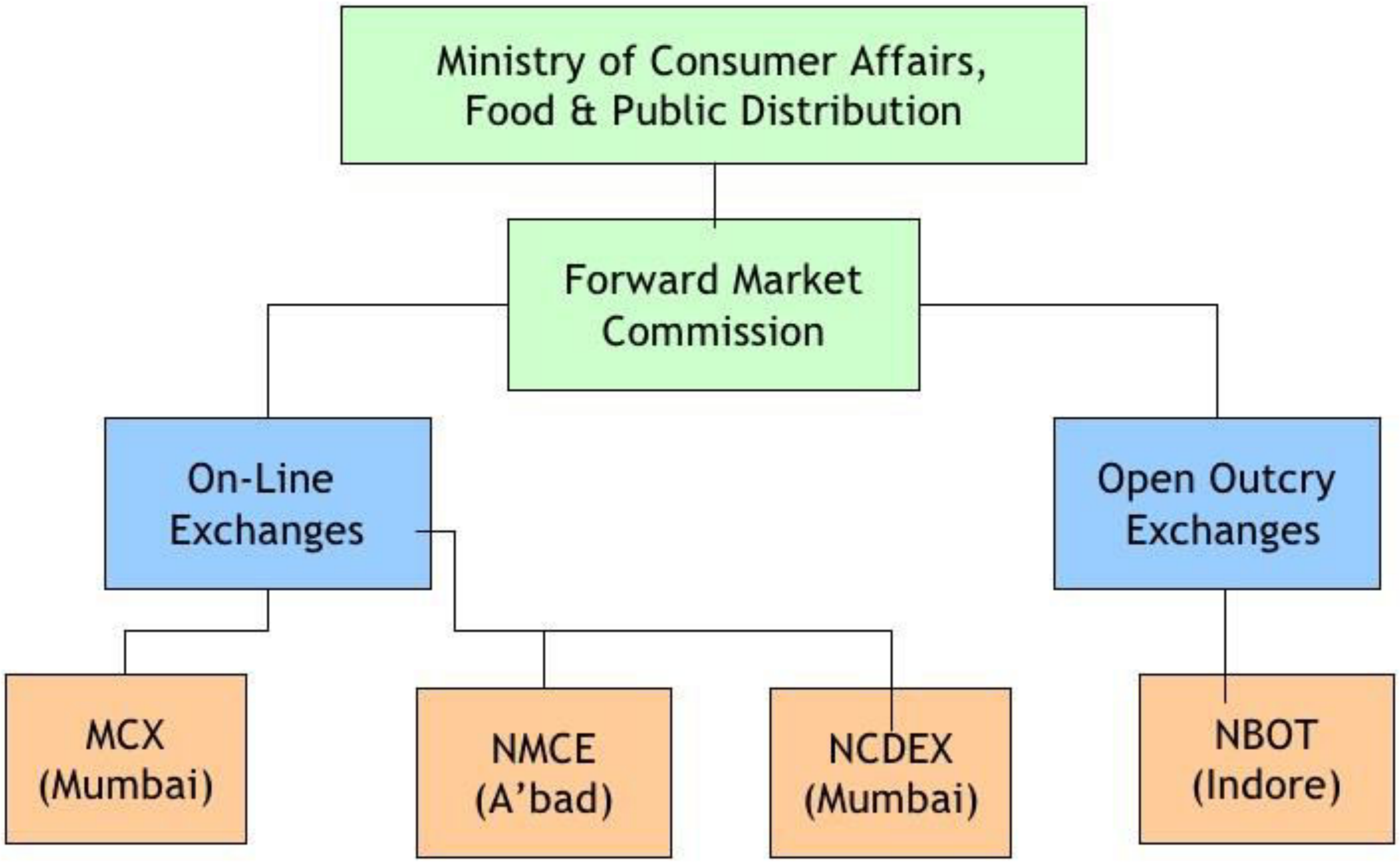
What are tradeable commodities?

Commodities have to fulfill the following criteria to be traded in the commodity market:

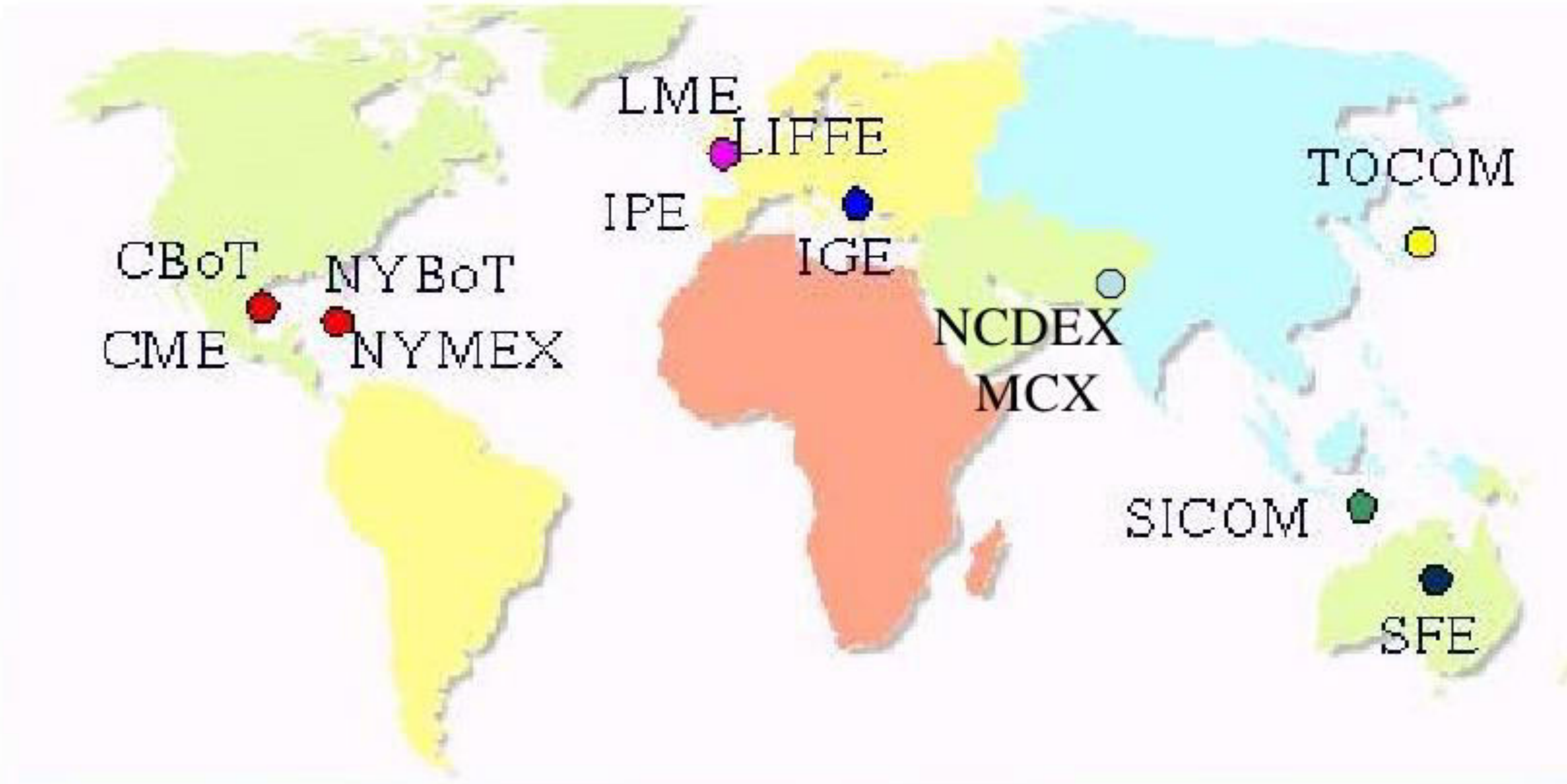
1. Tradeable – viable to carry out exchange
2. Deliverable – physically deliverable
3. Liquidity – must have a demand & supply

"Commodities have become an attractive investment in recent years, even for those who may not know much about them but would like to participate in the profit potential from dramatic price advances posted by energy, grains, metals and other commodities, lifting them to the highest overall levels in more than 30 years."

Structure of Market In India



World's Major Commodities Exchanges



Commodities Segment wise (MCX & NCDEX)

COMMODITIES

Metals
- Gold
- Silver
- Steel
- Copper
- Zinc
- Nickel
- Lead & Aluminium

Oilseed Complex
- Crude Palm Oil
- Mustard Seed
- Castor Seed
- Refined Soy Oil

Energy
- Brent crude
- Sweet Crude oil
- Furnace oil

Softs
- Cotton
- Sugar
- Gur

Agri. Comm.
- Pepper
- Guar Seed
- Soy Bean
- Jeera
- Chilli
- Turmeric
- Etc…..

Why Commodities?

- Commodities are easy to Understand and have positive correlation with Inflation.
- The Commodity market are global in nature , hence less risk for manipulation.
- Every commodity have separate market in Itself and hence many such market is simulated at one single screen. The trend in one commodity not necessarily have correlation with the trend of other.
- Historically Commodities have outperformed the Stock Market .
- Diversification through a different asset class.
- Low Margins – 4% - 10% only

Opportunities in the Commodity Futures

(1)**Speculation:**

It facilitates speculation by providing opportunity to people, although not involved with the commodity, to trade on the views in the movement of commodity prices.

(2)**Hedging:**

For the people associated with commodities, the Futures market can provide an effective hedging mechanism against price movements. For example an oil-seed farmer may go short in oil-seed futures, thus ‘locking’ his sale price and in the process hedging against any adverse price risks.

- Also, there is a saying that ‘Gold, is the safe haven’. Thus, gold can be used as a hedging tool against other investments.

(3)**Arbitrage:**

Traders may exploit arbitrage opportunities that arise on account of different prices between the two exchanges or between different maturities in the same underlying.

(4)Two Way Market Opportunities. Traders will benefit in a Bull or Bear market

(5)**Spread Trading**

- Inter Commodity (Gold /silver, guar seed/guar gum)
- Intra Commodity Spreads (calendar Spreads)

(6)Lower margins compared to Equity Markets, gives scope to higher exposure.

Benefits of Commodities Futures Trading

- Additional Investment/Trading opportunity
- Diversification of Portfolio – Asset Class
- Lower Margins – High leverage for traders
- Hedging/ Arbitrage opportunities
- Additional trading opportunity after 3.30 PM

Trading Strategies

Pure Trading

Speculators in the futures market can use different strategies to take advantage of rising and declining prices. The most common are known as **"Going Long," "Going Short"**

As an Investment

Investors can build and Diversify their Portfolio

Alternative Ideas

Calendar Spread trading

Spreads involve taking advantage of the price difference between two different contracts of the same commodity

Arbitrage Opportunities

Inter Exchange (NCDEX & MCX)

Spot -to- Futures

Some Major International Commodity Derivatives Exchanges

Sr. No	Name and Address	Contract Traded
1.	Chicago Mercantile Exchange (CME)	Butter, Milk, Diammonium Phosphate, Feeder cattle, Frozen Pork bellies, Lean Hogs, Live Cattle, Non-fat Dry Milk, Urea, Urea Ammonium Nitrate, etc.
2.	New York Mercantile Exchange (NYMEX)	Light Sweet Crude Oil, Natural Gas, Heating Oil, Gasoline, RBOB Gasoline, Electricity, Propane, Gold, Silver, Copper, Aluminum, Platinum, Palladium, etc.
3.	London International Financial Futures and Options Exchange (LIFFE)	Cocoa, Robusta Coffee, Corn, Potato, Rapeseed, White Sugar, Feed Wheat, Milling Wheat, etc.
4.	Chicago Board of Trade (CBOT)	Corn, Soybeans, Soybean Oil, Soybean meal. Wheat, Oats, Ethanol, Rough Rice, Gold, Silver, etc.
5.	London Metal Exchange (LME)	Aluminum, Copper, Nickel, Lead, Tin, Zinc, Aluminum Alloy, North American Special Aluminum Alloy (NASAAC), Polypropylene, Linear Low Density Polyethylene, etc.
6.	New York Board of Trade (NYBOT)	Cocoa, Coffee, Cotton, Ethanol, Sugar, Frozen Concentrated Orange Juice, Pulp etc.

7.	Tokyo Commodity Exchange (TOCOM)	Gasoline, Kerosene, Crude Oil, Gold, Silver, Platinum, Palladium, Aluminum, Rubber, etc.
8.	Sydney Futures Exchange (SFE)	Greasy Wool, Fine Wool, Broad Wool, Cattle, etc.
9.	Dubai Gold and Commodities Exchange (DGCX)	Gold, Silver, Fuel Oil, Steel, Freight Rates, Cotton, etc.
10.	Bursa Malaysia Berhad	Refined Bleached Deodorized Palmolein, Crude Palm Oil, Palm Kernel Oil, etc.
11.	Winnipeg Commodity Exchange	Canola, feed Wheat, Western Barley, etc.
12.	Dalian Commodity Exchange	Corn, Soybean, Soybean Meal, Soy Oil, etc.
13.	Zheng Zhou Commodity Exchange (CZCE)	Wheat, Cotton, Sugar, etc.
14.	Central Japan Commodity Exchange	Gasoline, Kerosene, Gas Oil, Eggs, Ferrous Scrap, etc.
15.	Shanghai Futures Exchange (SHFE)	Copper, Aluminum, Natural Rubber, Plywood & Long Grained Rice
16.	Brazilian Mercantile and Futures Exchange	Anhydrous Fuel Alcohol, Arabica Coffee, Robusta-Conillon Coffee, Corn, Cotton, Feeder cattle. Live Cattle, Soybean, Crystal Sugar, Gold, etc.
17.	Kansai Commodity Exchange	Soybean, Raw Sugar, Raw Silk, Shrimp (frozen). Coffee, Corn, Azuki beans (Red), etc.
18.	Osaka Mercantile Exchange	(Ribbed Smoked Sheets) RSS3, (Technically Specified Rubber) TSR20, Nickel, Aluminum, Rubber Index

19.	Singapore Commodity Exchange	Coffee, Rubber (RSS1, 2, 3)
20.	Tokyo Grain Exchange (TGE)	Corn, Soybean Meal, Soybeans, Red Beans, Coffee, Sugar, Raw Silk, Vegetables, etc.
21.	Intercontinental Exchange (ICE)	Brent Crude Oil, Coal, Electricity, Emissions, Gas Oil, Heating Oil, Gasoline (RBOB), Natural Gas, WTI and all the futures contracts of its subsidiary - The international Petroleum Exchange (IPE)

In October 2005, MCX and London Metal Exchange (LME) announced the signing of a licensing agreement that will allow the MCX to launch futures contracts in non-ferrous metals using LME prices as the basis of settlement. MCX has also signed a Memorandum of Understanding (MoU) to explore areas of cooperation and business opportunities with the goal of assisting and benefiting the underlying producers, end-users and investors in their commonly traded products by maximizing the application of International best practices for price risk management and exchange operations that could mutually benefit the exchanges.

Key Shareholders of MCX

- Financial Technologies (India) Ltd.
- State Bank of India
- National Stock Exchange of India Ltd. (NSE)
- National Bank for Agriculture and Rural Development (NABARD)
- HDFC Bank
- Fidelity International
- Bank of India
- Union Bank of India
- Bank of Baroda
- State Bank of Indore
- State Bank of Hyderabad
- State Bank of Saurashtra
- SBI Life Insurance Co. Ltd.
- Canara Bank

Role of Banks in Commodity Markets

Financing of agriculture poses certain special risks for banks and so, banks need to mitigate these risks in order to ensure effective credit delivery to the agricultural sector. One of the key risks for banks is the commodity price risk. The volatility in the prices of agricultural commodities may cause severe loss to the farmer who may be unable to repay his dues to the bank. If the prices collapse, the distress in the farming community can be widespread and security obtained by the bank may have very limited usefulness, Commodity derivatives can mitigate these risks to a certain extent. The issue has been examined in greater detail later in the report.

A well-established system of issuance of Warehouse Receipts is a pre-requisite of an efficient market in commodity derivatives. Warehouse Receipts are also useful to the farmer in securing timely finance from banks at economical rates.

In terms of Section 8 of the Banking Regulation Act, 1949, no banking company shall directly or indirectly deal in buying or selling or bartering of goods except in connection with realisation of securities given to or held by it, or engage in any trade or buy, sell or barter goods of others. For this purpose, "goods" means every kind of movable property, other than actionable claims, stocks, shares, money, bullion and spices and all instruments referred to in clause (a) of sub-section (1) of Section 6 of the B.R. Act, 1949. Thus, while bullion is specifically permitted for trading under the Act, banks are prohibited

Physical Share certificate