The Farmer's Perspective of Commodity Futures in India- The Road Ahead

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The process of economic liberalisation in India began in 1991. As a part of the process, several capital market reforms were carried out by the capital market regulator Securities and Exchange of India. One such measure was to allow trading in equities-based on stock exchanges in the year 2000. This step proved to be a shot in the arm of the capital market and volumes soared within three years. One of the favourite quotes about trading in this connection comes from trading psychology expert Mark Douglas. As he opines, most of us are not willing to take financial risks as we think. "Most people like to think of themselves as risk takers, but what they really want is guaranteed outcome with some momentary suspense to make them feel as if the outcome had been in doubt. The momentary suspense adds the thrill factor necessary to keep our lives from getting too boring."

The success of the capital market reforms motivated the government and the Forwards Market Commission (the commodities regulator) to kick off similar reforms in the commodities market. Thus almost all the commodities were allowed to be traded in the futures market from April 2003. To make trading in commodity futures more transparent and successful, multi-commodity exchanges at national level were conceived and were allowed to start futures trading in commodities on-line.

WHAT IS FUTURES' TRADING?

Before going into the intricacies of commodity futures, let us understand what futures' trading is all about.

Futures trading is an agreement between a buyer and a seller obligating the seller to deliver a specified asset of specified quality and quantity to the buyer on a specified date at a specified place and the buyer, in turn, is obligated to pay to the seller a pre-negotiated price in exchange of the delivery. In futures trading ,the contracting parties negotiate on, not only the price at which the commodity is to be delivered on a future date but also on what quality and quantity is to be delivered and at what place. "Futures Contract" is a highly standardized contract with certain distinct features.

INDIA AND AGRICULTURE

In India, agriculture has traditionally been an area with heavy government intervention. Government intervenes by trying to maintain buffer stocks, they try to fix prices, they have import-export restrictions and a host of other interventions. Many economists think that we could have major benefits from liberalisation of the agricultural sector. In this case, the question arises about who will maintain the buffer stock, how will we smoothen the price fluctuations, how will farmers not be vulnerable that tomorrow the price will crash when the crop comes out, how will farmers get signals that in the future ,there will be a great need for wheat or rice. In all these aspects, the futures market has a very big role to play. Agriculture requires investments; farmers spend money on fertilisers, high yielding varieties, etc. They are worried when making these investments that by the time the crop comes out, prices might have dropped, resulting in losses. Thus a farmer would like to lock in his future price and not be exposed to fluctuations in prices.

Futures trading perform two important functions: price discovery and hedging of price risk in a commodity. Presently, futures' trading is permitted in 41 commodities in India. These include *pepper* (domestic and international), *turmeric, gur, castor seed, hessian, jute, sacking, cotton, potato, castor oi*l (international), *soyabean* (oil and cake), *kapas, RBD palmolein, sugar* and *tea*. The futures market allows producers and consumers of each product to engage in risk management. Indeed, that is why the futures exchanges were developed. A farmer wanting to be sure of a price for a product would sell a contract for future delivery at a price agreed to now. By doing so, he or she, would remove the risk that prices on the delivery date would be lower.

The present shift is as much towards better systems as away from the existing agricultural policy which protected and promoted the sector through procurement and controlled prices. "In view of the fiscal pressure and that of WTO (World Trade Organization) to reduce direct support to agriculture under the Agreement on Agriculture, there is a policy shift towards a market-oriented approach," explains the report of the Inter-ministerial Task Force on Convergence of Securities and Commodity Derivative Markets headed by Wajahat Habibullah, Secretary,

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Department of Consumer Affairs. A look at commodity exchanges will give an idea about their scope. In the US, the Chicago Mercantile Exchange, over and above basic commodities, deals in a basket of products based on equity indices, interest rates, weather and energy. In the UK, commodities, equities and interest rates are traded on the London International Financial Futures and Options Exchange. So, for Indian exchanges, the potential is huge. And they are poised for growth.

In fact, the size of the commodities markets in India is also quite significant. Of the country's GDP of Rs 13, 20,730 crore (Rs 13,207.3 billion), commodities related (and dependent) industries constitute about 58 per cent. At the end of the June 2007, the various commodities across the country clock an annual turnover of Rs 1, 40,000 crore (Rs 1,400 billion). With the introduction of futures trading, the size of the commodities market grows many folds here on. The global commodity trade is about three times the size of equities. But it is nowhere as hot in India. Commodity futures are fast spreading into rural India at a much faster pace than capital market operations. Seeing the immense potential and response from rural India, some companies have begun to pay increased attention to commodity futures markets.

COMMODITY FUTURES AND GROWTH

After a 40-year ban, commodity Futures was reintroduced in India 4 years ago. In 2003, the government gave four entities the nod to set up nation-wide multi-commodity exchanges. Again, expansion of permitted list of commodities under the Forward Contracts (Regulation) Act, 1952 was also allowed. Ever since the go-ahead given by the Forward Markets Commission regarding Commodity futures Trading in emerging markets in 2003, the futures market in commodities has seen vigorous growth. It is in this context, necessary to examine the benefits accruing to the Indian farmer from the futures market. The availability of futures market has emerged as an important source of information to farmers, thanks to the revolution in audio-visual media. Even when the farmers are not exchange users, they are more aware of prices of what they produce, the likely prices a few months ahead and the related variables. If discussions in village tea shops are any pointer, farmers are using such price information to get better deals in the village marketplaces. Knowledge thus becomes a source of empowerment for farmers.

The gradual evolution of commodity market in India has been of great significance for our country's economic prosperity. In the Indian commodity market there are so many varieties of products including agricultural products like rice, wheat, cattle etc; energy products like coal, petroleum, kerosene, gasoline; metals like copper, gold, silver, aluminum and many more. There are some delicate commodities also such as sugar, cocoa, and coffee, which is perishable, so cannot be put in stock for long time. Commodities have gained importance with the development of commodity futures indexes along with the mobilization of more resources in the commodity market.

At present, 25 commodity exchanges are in operation in India carrying out futures trading in as many as 81 commodity items. Most of these exchanges are regional and commodity specific exchanges. During 2003, National Multi Commodity Exchange (NMCE) status has been accorded to four commodity exchanges, viz., National Multi Commodity Exchange (NMCE), Ahmedabad, National Board of Trade (NBOT), Indore, National Commodity Derivative Exchange (NCDEX), Mumbai and Multi Commodity Exchange (MCX), Mumbai. India's commodity futures markets witnessed a whopping 37.3 per cent increase in trade in value terms during the financial year 2005-06. The total value of trade increased to Rs 21, 34,000 crore, according to the Forward Markets Commission (FMC). In the previous fiscal, the value of trade stood at Rs 5, 72,000 crore. The three national multi-commodity exchanges-National Commodity and Derivative Exchange of India (NCDEX), Multi Commodity Exchange of India (MCX) and National Multi-Commodity Exchange of India Ltd (NMCE) together accounted for 94 per cent of the trade in futures. The NCDEX share was Rs 10, 46,000 crore and MCX Rs 9, 62,000 crore. FMC did not give figures for the Ahmedabad-based NMCE. India is an agrarian economy where the agricultural sector provides employment to approximately 60 per cent of the population and contributes 25 per cent to the GDP of the country. Policies must be oriented towards enabling Indian farmers to prosper.

The total agriculture exports from was around 10.95 per cent in the year 2005-06. There has been decline in agricultural imports. The agricultural imports decreased from Rs 22057.49 crore (Rs 220.57 billion) in 2004-05 to Rs 21025.54 crore (Rs 210.26 billion) in 2005-06. The share of agricultural imports to the country has remained steady around 3.33 per cent. The turnover of commodity exchanges in 2006-07 financial year is likely to touch a whopping Rs. 37 lakh crore (Rs 37 trillion), according to the data from Forward Markets Commission. The following figure shows the top commodity futures traded at the end of March 2007.

Figure 1.0 Top Commodity Futures at the end of March 2007

SHOOTING STARS	
Top commodity futures traded across exchanges	
Commodity	Value of futures traded (Rs. crore)
Gura seed	129,522.98
Silver	116,267.99
Soy oil	101,527.66
Gold	62,784.85
Mustard seed	19,422.46
Castor seed	14,327.34
Guar gum	13,412.08
Pepper	8,334.28
Gur	7,891.49
Rubber	2,745.84
Crude oil	1,900.14
Cotton	779.16
Other metals	618.22
Jute	91.74

Source : Forward Markets Commission

(Source: www.fmc.gov.in/cdf/ff.htm 2007)

The data from the apex commodity regular in India showed that the total turnover of all the 23 national and regional bourses stood at Rs 35,08,856 crore (Rs 35,088.56 billion) till March 15 of 2006-07 fiscal. Agriculture exports, on the other hand, have shown an increasing trend. India's agricultural exports have increased from Rs 398.63 billion in 2004-05, to Rs 498.03 billion in 2005-06. However, during the current year (April-September 2006), the value of agricultural exports was worth Rs 28157.52 crore (Rs 281.58 billion) compared to Rs 21673.25 crore (Rs 216.73 billion) for the corresponding period of last year, registering a growth of 29.91 per cent. Export of marine products, oil meals, rice, wheat, tea, cashew and sugar dominates India's agricultural exports. There has been a surplus in agricultural trade over the years. The trade surpluses in terms of value have been Rs 17805.82 crore (Rs 178.06 billion) in 2004-05, and Rs 28777.38 crore (Rs 287.77 billion) in 2004-06 respectively. The surplus is continuing during the current year and is worth Rs 17025.74 crore (Rs 170.26 billion).

India being a Commodity based economy where two-third of the one billion population depends on agricultural commodities, surprisingly has an under developed commodity market. Unlike the physical market, futures markets trades in commodity are largely used as risk management (hedging) mechanism on either physical commodity itself or open positions in commodity stock. For instance, a jeweler can hedge his inventory against perceived short-term downturn in gold prices by going short in the future markets.

The United States Department of Agriculture (USDA) has released its annual outlook and prospects for major agri products in the month of September 2007. There is a cautionary note to be attached to the numbers as it is necessary to read between them. While the absolute numbers are important for different years, the changing projections in September over August reflects the changing perceptions which need to be taken into account more seriously as they also affect price movements. Further, the changes in stocks are critical because falling stocks have an impact on the price levels.

The commodity futures market size is expected to reach more than double by 2010 to Rs 12,00,000 crore and create additional employment avenues for one lakh persons, industry body ASSOCHAM has said. The Indian commodity futures market is poised to touch more than Rs 12 lakh crore by 2010 as against the current size of Rs 5.5 lakh crore, the chamber said in a release.

COMMODITY FUTURES AND FARMERS

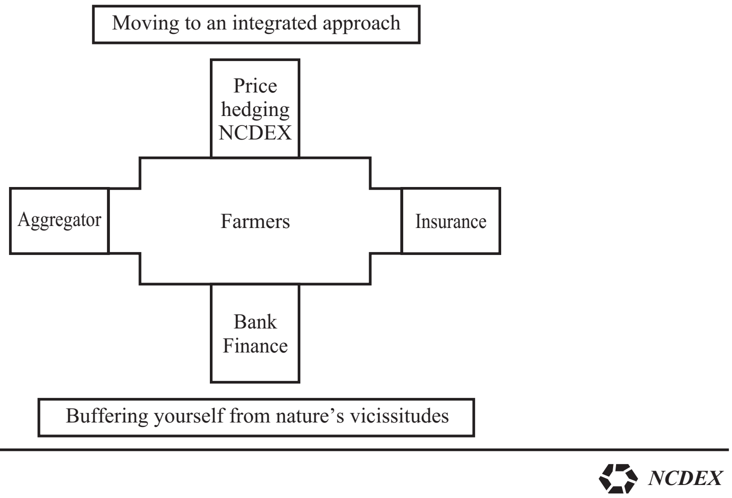
In the developed world, the majority of farmers use futures and options in commodity derivatives and even recognised agents quote spot market prices benchmarked to the commodity derivatives' contract prices. The derivatives exchanges are currently under fire for allegedly becoming speculators' dens responsible for driving up prices of basic essentials consumed by the common man. The question everybody is asking is how is futures trading in commodities benefiting farmers as this was the premise behind the liberalisation envisaged by the National Agriculture Policy of 2000, which led to the re-introduction of futures trading. Currently, only 25-30 per cent of the price paid by the consumer is actually realised by farmers. The rest of the proceeds get appropriated by a long chain of intermediaries. In the US, farmers' share is between 60 and 65 per cent, and in the case of the Amul experiment, it is as high as 90-92 per cent of the final consumer price.

The initiatives of NCEDX have helped farmers in betterment of their positions in the futures market. Farmers on the NCDEX- promoted exchange will also be able to set the base price for their produce and trade non-standard grades through an electronic national auction process. In the mandi, once the farmer brings his produce to the market, he finds his realisations affected by cartelisation of traders who purchase from him. NCEDX has planned to make warehousing facilities available at delivery centres, where the farmer can bring in the produce and have it graded and stored. Further, it also arranges for banks to lend against such stock that is properly warehoused and graded to help him realise some cash upfront without entering into a forced sale at low prices. As a result, the farmer may also end up realising a better price. The bargaining power of farmers will go up if there is a transparent alternative available as currently, they are the most exploited party in the value chain. After totting up a daily turnover of Rs 11,500 crore, India's two leading commodity derivatives exchanges are taking the magic of screen-based transparent price discovery to the spot markets for agricultural produce. The aim is to rationalise the value chain of agriculture so that farmers get a much larger share of the final price the consumer pays.

Futures trading should normally help farmers plan their cropping pattern, based on forward prices on the exchanges. However, in a country like India, the ability of farmers to switch from one crop to another based on forward prices is rather limited. For processors and traders faced with the risk of adverse price movements, futures' trading is a boon. They can buy or sell futures contracts and lock in their profits or margins. Hedgers and speculators impart liquidity to the market. Small farmers have benefited directly from futures trading. At the same time, they have reaped huge benefits indirectly as trading terminals helped a nationwide price discovery mechanism.

Farmers can adopt an integrated approach which favours them, one as follows:

Figure 1.1 An Integrated Approach



(Source: http://www.NCDEX Research Reports /Dec0406/indepth01.asp)

Awareness amongst the large farmers can bring them directly into the futures market. Even though farmers may not be directly participating in large numbers in the futures markets, the benefit of transparency in futures platform as regards price discovery accrues to them. The experience in rubber and pepper has been extremely positive and the farmers have definitely benefited. Since the farmers could sell in futures contracts, they can now opt for increased production using appropriate methods such as usage of rain guards, etc.

Commodity futures trading in India started some hundred years ago. Then because of shift in economic policies, almost the entire commodity futures trading got banned. In the last decade, this has gradually come back to life and is offering various services to farmers.

SOME BENEFITS THAT ACCRUE TO FARMERS IN FUTURES MARKET

If the peasants are farming some crop now and are very much concerned that price will crash by the time the crop comes in, then if there is futures market, they will have the option to sell their products in it. As price in the future markets are fixed; farmers selling products in the future markets get rid of their worries about the unexpected price fall. This helps them to take the risk of innovations, by using new high yielding varieties of seeds, fertilizers and new techniques of cultivation.

Futures Market will act as a smoothing agent between the present and future commodity market. If the price, which is going to prevail in future, is high compared to what it is now, then the arbitragers would like to buy the commodities now to sell those in future. The reverse process is also true. So the existence of a futures market is always good for any economy. It opens up a new opportunity to people to protect themselves from unexpected risks.

Future Markets also serve as a low cost, highly efficient and transparent mechanism for discovering prices in the future by providing a forum for exchanging information about supply and demand conditions. The hedging and price discovery functions of future markets promote more efficient production, storage, marketing and agro-processing operations and help in improvement in overall agricultural marketing performance.

After verifying the quality and grade of the produce, the farmer stores his produce in these warehouses. He can visually ascertain the prevailing spot price as also the futures prices in various languages on the monitor.

The farmer can decide to sell at the current price, in which case he gets the full amount in cash. Or, if he decides to sell at any convenient future date, he gets an advance of about 70-75 per cent of the current price and also a warehousing receipt, which is a negotiable instrument. On expiry of the contract date, the holder of the warehousing receipt is assured of getting the contracted price. The farmers have no difficulty understanding the scenario and would rather transact through the futures market.

There was a time when the farmer was not aware of futures trades when speculations could have been taken place. When the futures market is truly opened to farmers, it takes on an entirely different aspect.

The farmer produces various types of crops and the existing socio-economic and political framework makes it difficult for him to change the form of his produce through value-addition / processing and also to make his produce available in another location where the prices may be better. The farmer is well aware of the fact that the immediate post-harvest prices are low and it will rise in three to four months. But he cannot wait to take advantage of this price rise.

At the same time there are traders and consumers who need the farmers' produce in other locations at a specified time in the future. Here comes the futures market which matches the offers to sell with the bids to purchase with an objective to avoid costs of transport and storage. For the first time, farmers can choose the price at which they want to sell their produce. So it facilitates price discovery and risk-cover with greater certainty.

A number of traders deliver Mentha oil in MCX warehouse, obtain a warehouse receipt, pledge such warehouse receipt with the bank and obtain bank loan. For availing such loan, the trader need not have risk balance sheet or income tax file, because banks finance on the commodity itself and not on balance sheet. Banks are also comfortable to finance, because they get a real time benchmark price for MTM purpose and they also feel safe, if stock is lying in commodity exchange warehouse.

Traders and stockiest feel safe, if they are completely hedged against price fluctuation in a futures market. They keep on buying and accumulating stock, without bothering about price crash, if they have sold a futures contract against their physical stock. Though farmers benefit in many ways, there are several pre-harvest and post-harvest concerns that need to be addressed.

Pre-harvest Concerns of the farmers: These include Choice of crop**,** Cobweb syndrome**,** Influence of MSP**,** Grades and standards**,** Price risk **,** Volumetric risk**,** Yield dependent on monsoons**,** Credit availability limited**,** Crop failure and Default on crop loans

Post-harvest conundrums of the farmers: These include when to sell the commodity? Spot market or futures market? Where to sell? Choice of the closest mandi or the one offering best price? If selling in futures market, then how to tide over financial requirements in interim period? Warehousing facilities. How to access the commodity futures market?

POSITIVE IMPACTS OFFUTURES MARKET ON THE EXPORTERS:

They get raw material continuously throughout the year and so, they are able to run their factories round the year. Earlier, in most of the years, crude mentha oil was available for 7-8 months only, and so the factories were virtually closed for 3-4 months in a year, due to non- availability of raw material.

In futures market, they get an alternative channel for procurement of raw material. It has been seen practically during last 2 years that during February to May, when availability of mentha oil in physical market is poor being off season, exporters have lifted huge stock from MCX warehouse by buying futures contracts.

The exporters can cover themselves by buying futures contracts against their uncovered export commitment.

Today, all the leading exporters of Mentha Oil hedge their position on MCX futures, which is a benchmark for real benefits of MCX futures contract to the physical market traders.

Exporters can negotiate better with overseas buyers showing them MCX futures prices. Earlier, there was no benchmark price available and so, the exporters were not able to quote any referanceable price while negotiating with the overseas buyer.

POSITIVE IMPACTS OFFUTURES MARKET ON THE COUNTRY:

Increase in export earnings as a result of increase in size of export as well as price realization.

Increase in employment due to development of a number of ancillary activities such as warehousing, quality certification, laboratories for GLC testing, etc.

Availability of structured bank finance against warehouse receipts.

Bridging the rural urban divide due to reduction in spread between farmers' realization and price realized by exporters.

The powerful tool, futures market breaks the market power of the farmers by its nature of transparent, electronic exchange with nationwide access which brings in new players. Physical proximity to the market becomes a non-issue once an electronic exchange is in operation. Also when both the trader and the farmer know the futures price, it is harder for the farmer to get cheated. Futures' trading is about planning; it is about taking control of uncertainty. A farmer who sells goods at a future harvest date, at a locked-in price, is in a fundamentally superior position in terms of planning. *Banning futures trading is about forcing people to not plan for the future.* The sensible strategy is to address the genuine difficulties of market design, regulation and supervision, so that futures' trading is able to play its full role in a mature market economy.

BRIGHTER SIDE- ACASE STUDY OF MENTHAOIL

Scientists can discover high yielding species of seeds and plants, while electronic markets can create transparency, price efficiency, reduction in spread and expansion of market size. A combination of scientific discoveries and successful commodity futures market leads to unprecedented and overwhelming growth in the GDP contribution of a commodity as has been proved in the case of Mentha Oil.

The Masauli, Barabanki and Muradabad areas of UP, were known for cultivation of opium prior to independence. After imposition of prohibition on opium cultivation in that area, farmers of the locality did not have any cash crop other than sugarcane. Subsequently, during 1980s, CIMAP, the premier agricultural research institute based in Lucknow, came out with Mentha crop and endeavored to develop this crop as a significant cash crop in that area. Even after continuous efforts, till 2004, the area under cultivation for Mentha oil was hardly ranging around 1.50 lakh hectare.

After commencement of futures trading in April 2005, the entire eco system of Mentha Oil got a big boost. It is evident from the following table:

Table 1.0 Growth of Mentha Oil -June 2007

	2003	2007	Increase / decrease
Area under cultivation	1.50 lac hectare	2.40 lac hectare	60 % increase
Production of Mentha Oil	17000 MT	32000 MT	88 % increase
Export of Mentha Oil	13000	25000 MT	92 % increase
India's share in world production	75 %	90 %	25 % increase
India's share in world trade	70 %	75 %	5 % increase
Average export realization	$ 10 per Kg for mentha powder	$ 15 per Kg for mentha powder	50 % increase
	$11 per Kg for mentha crystal	$ 17 per Kg for mentha crystal	55 % increase
Total size of export	Rs. 650 crores	Rs. 1100 crores	69 % increase

(Source: http://www.business.headlinesindia.com)

Benefits to farmers from trading in Mentha oil:

Increase in price realization: The average price realized by the farmer prior to introduction of futures trading was Rs. 300-350 per Kg. Now, he realizes Rs. 500 to Rs 550 per Kg.

Increase in profit margin: The direct cost of production for the farmer works out to be around Rs 150 to 200 per Kg. As the price realization increased from Rs 300 to Rs 500, profit per Kg has also increased from Rs 150 to Rs. 350. Hence, profit per Kg is more than doubled.

Availability of Continuous market system: Prior to commodity futures era, most of the farmers used to sell their entire production during arrival season (June-July every year). Stockiest used to create inventory by buying from the farmers during such period and to sell to exporters at higher price during off season. In 2007, production is at least 30 % higher than last year, but arrivals during June July is less, which shows that farmers are holding oil. Farmers are aware that MCX trading is operational across the year, and hence they will be able to sell anytime during the year. Hence, the alternate market system created by MCX has increased holding capacity of the farmers.

Price transparency: MCX price is known to the farmers, even at remote locations. Now, they sell their produce considered MCX price in mind and hence are able to get Rs 500 and above per Kg.

Therefore, it can be seen that, ensuring inclusive growth, farmers are able to enjoy piece of cake originating out of boom in Mentha Oil Economy. But leaving this commodity aside, let us examine some of the initiatives taken up by the Government of India in elevating the status of commodity futures trading in the country as such.

GOVERNMENT POLICY AND FUTURES' TRADING

Government of India, in 2002-2003, has demonstrated its commitment to revive the Indian agriculture sector and commodity futures markets. The Prime Minister's Independence Day address to the nation on August 15, 2002, which enlisted nation-building initiatives, included setting up of national commodity exchange among important initiatives. Some of the policy initiatives are as follows:

Government of India, in early 2003, has given mandate to four entities to set-up nation-wide multi-commodity exchanges. National level exchanges would make availability of futures contracts across nation in the most effective manner through technology and at the same time would improve the risk management systems to improve and maintain financial integrity of futures markets in the country.

The permitted list of commodities under the Forward Contracts (Regulation) Act, 1952. This has effectively translated into futures trading in any commodities that can be identified. This would make available risk management mechanism for all commodities where such a demand exists but never made possible in the past.

Abolition of 11 day restriction on spot market transactions would effectively mean unhindered forward contracting among the constituents of commodity trade value chain.

The Non-Transferable Specific Delivery (NSTD) contract is removed from the purview of Forwards Contracts (Regulation) Act.

The Government is protecting the interests of the poor Indian farmers by procuring crops at remunerative prices directly from the farmers without involving middlemen in between. This way Government maintains sufficient buffer stocks and at the same time provides the farmers safeguard against the fluctuating food crop prices.

OTHER INITIATIVES

A ***European Commission-financed study***, released in Paris in the last week of Septmeber2007, is any indication, the agriculture policies in India were the most disastrous. The countries studied consist of three large developing ones (Brazil, India and South Africa), four formerly planned economies (Bulgaria, Romania, Russia and Ukraine) and China, which combines some features of both the groups. The new study is by the inter-governmental think tank of 30 rich industrial countries, the Organisation for Economic Cooperation and Development (OCED), and is financed by the European Commission.

The Green Revolution in India, brought about large gains in production but in recent years, food crops in particular have reached a plateau with deteriorating land quality and water shortages posing serious problems for future increases in output, the report said. India has only 4 per cent of world water resources for 16 per cent of the population and the lack of water is a serious issue. To tackle quality related problems, the exchanges offer premiums and discounts depending on quality of produce on offer. Farmers will also have the option of subjecting

their produce for testing before delivery to the warehouse or on delivery and obtain a receipt. The warehouse receipt is expected to help farmers to raise short-term finance.
Farmer Finance program at Centre for Development Finance (CDF), focuses on identifying major bottlenecks in farmer's productivity and providing sustainable financial solutions to overcome these bottlenecks as well as building knowledge base for the sector. Farmer Finance projects aim to strengthen the rural credit delivery system and fill the existing gaps by prototyping new financial products in agriculture/farmer finance.
Reviewing government support to agriculture in India, it can be said that their support to agriculture is dominated by market price support and input subsidies, the least efficient and most distorting ways of providing agricultural assistance. Besides, the share of MPS and input subsidies in total support has been growing. Such measures misallocate resources and are not well targeted to specific outcomes.

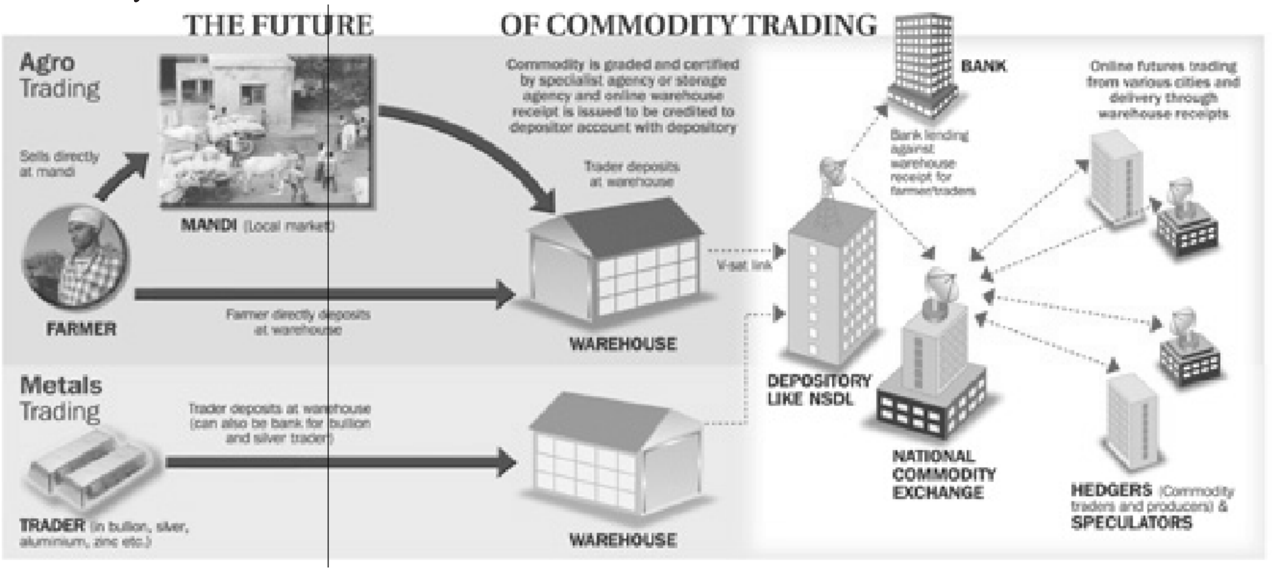
THE ROAD AHEAD

The case in India seems that there are too many commodity exchanges competing with each other for the same products.

The future is that India will go the American way, and each exchange will specialise in certain commodities and that focus will enable them to deliver the best possible values to the stakeholders. Instead of trying to introduce all the commodities, focusing on a few in which they have a competitive advantage will take them to a higher level of growth in terms of volume. In fact, there are clear signals already in the market place.

To compare Indian Markets with the US exchanges, and if we take the total volume of the NYSE and NASDAQ and the total volume of commodities exchanges in the US, the commodities turnover is much higher than the stock market turnover. In fact, the turnover on just one of the leading commodity exchanges viz. CME is $333.7 trillion while the NYSE and NASDAQ combined turnover is only $8.285 trillion. If this is taken as an indication, the commodities futures trading turnover will increase manifold in India too.

FMC and the National Commodity Exchanges are in the process of identifying organisations with rural connectivity and knowledge of futures trading to reach the benefits of futures to the farmers directly or indirectly.



(Source: http://www.businessworldindia.com/sep1503/indepth_commodity.asp)

Commodities trading with global linkages should be allowed for reforming the exchange. These suggested reforms, if executed, will undoubtedly transform the commodities exchanges as such reforms would not only enhance depth but would also increase the liquidity in the market.

Brokers engaged in commodity futures / derivatives trading should be extended the exemption from 10% TDS condition.

Loss arising from speculation in commodity futures trading should be allowed to be set off against business profit.

FMC is looking at various aggregation models so as to develop a policy on aggregation of farmers for participation in the futures market. The various measures adopted by FMC would fructify at the grass root level and that in the coming years this market will see greater participation direct and indirect by farmers and other supply chain functionaries.

Mutual funds, Financial Institutions and Foreign Institutional Investors should be allowed to participate in commodity futures.

Stamp duty on futures contracts should be rationalised. 'Warehouse Receipt' system should be introduced

CONCLUSION

The availability of futures market has emerged as an important source of information to farmers, thanks to the revolution in audio-visual media. Even when farmers are not exchange users, they are more aware of prices of what they produce, likely prices a few months ahead and related variables. If discussions in village tea shops are any pointer, farmers are using such price information to get better deals in the village market places. Knowledge has become a source of empowerment for farmers. Commodity Exchanges in India are expected to contribute significantly in strengthening Indian economy to face challenges of globalisation. Indian markets are poised to witness further developments in the areas of electronic warehouse receipts (equivalent of dematerialized shares), which would facilitate seamless nationwide spot market for commodities. Amendments to Essential Commodities Act and implementation of Value-Added Tax have facilitated easier trading in commodities. Also the increased interest from the international players in the Indian Commodity Markets is quite obvious.

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