Ind. Jn. of Agri.Econ.
Vol.64, No.3, July-Sept. 2009

RAPPORTEURS' REPORTS

Futures Market in Indian Agriculture and Its Impact on Production and Prices

Rapporteur: J.N. Dhankhar*

I

INTRODUCTION

Indian markets have recently thrown open a new avenue for retail investors and traders to participate in commodity derivatives. Earlier, retail investors could have done very little to actually invest in commodities such as gold and silver – or oilseeds in the futures market. Except for gold and silver, there was practically no retail avenue for punting in commodities. However, with the setting up of three multi-commodity exchanges in the country, retail investors can now trade in commodity futures without having physical stocks/commodities. They are the Multi Commodity Exchange (MCX), the National Commodity and Derivatives Exchange (NCDX) and the National Multi Commodity Exchange (NMCE). Commodity futures contract and the commodity exchanges are regulated by the Government under the Forward Contracts (Regulation) Act, 1952 (FCRA).

The nodal agency to regulate the future market is the Forward Markets Commission (FMC), situated at Mumbai, which functions under the aegis of the Ministry of Consumer Affairs. The two major economic functions of a commodity futures market are price risk management and price discovery. Among these, the price risk management is by far the most important, and is the crux of a commodity futures market.

The Economic Survey and the recent budget proposals are in favour of the growth of Commodities Market. The 2008-09 Economic Survey has also suggested lifting the ban on some commodity futures contracts. The Government has banned trading in rice, urad, tur futures indefinitely and suspended sugar futures till December 31, 2009. The budget has also removed CTT (Commodities Transactions Tax) on the commodities trading.

The survey suggested the need for taking shot electronic trading to agricultural produce marketing committees across India. The two largest commodities exchanges in India are Multi Commodity Exchange (MCX) and the National Commodities and Derivatives Exchange (NCDEX) have already started electronic spot exchanges.

*Dean, ICFAI Business School, Jaipur – 302 019 (Rajasthan) and Former Executive Director, Jaipur Stock Exchange Ltd., Jaipur.

However, there are more than 7500 APMCs (mandis) in the country where trading still takes place in physical form. Therefore, it is suggested that the existing electronic spot exchanges can also involve APMCs for increasing the scope of electronic trading. Futures market in Indian agriculture has a definite and significant impact on production and prices of various agricultural commodities.

II

REVIEW OF PAPERS

The papers received under the theme are grouped into three categories, i.e.,

(a) Agricultural Commodity Futures Markets – Production and Prices - Six papers

(b) Growth of Commodity Futures, Subsidies, Globalisation perspective, Future Role in Indian Economy etc. - Four papers

(c) Role and marketing of individual commodities in different states including price behaviour and contract farming etc. i.e. - Seven papers

Agricultural Commodity Futures Market Production and Prices

K. Elumalai *et al.*, has starts with the introduction that price discovery is very efficient in futures market than spot market. Through hedging, farmers can mitigate the price risk that they may face in the spot market with volatile prices. It is argued that futures trading affect the spot market by increasing price volatility in the spot market. They have also given the findings about the impact of futures trading on agricultural commodity prices made by Dr. Abhijeet Singh, Chairman of the Spot Committee in March, 2007. Their paper has concluded to assess the futures and spot price linkages using Johnson Co-integration Analysis and Vector Error Correction Model. On price discovery, the significant co-efficient of atleast one error, correction term confirm the results of co-integration between futures and spot prices.

Naveen P. Singh *et al.*, have explained in their paper, how efficient are futures market operations in mitigating price risk. They have used the co-integration technique in the present study to analyse the long run relationship between spot price and futures price. In their study, the variation in the spot and futures prices as measured by co-efficient of variation was found to be higher in case of urad, chana, zeera and wheat. In this study, an attempt has been made to look into the mechanism of movement in spot and futures prices for various cereals, pulses, oil seeds and major cash crops in India.

M.S. Jairath’s study examines the growth and composition of Indian Agricultural Commodity, Trading Systems and settlement of performance of futures market. The study also suggests that there exist huge opportunities for each stake holders of futures trading, i.e., farmers for what to grow and when to sale and Government fixing minimum support price (MSP) or for intervention prior to the crisis. For improving the performance of futures markets in India, he suggests that awareness at various levels for creating efficiencies, starting trading in operation market etc.

Tata Rao Dummu concludes that India is one of the top producers of a large number of commodities. The market has made enormous progress in terms of technology, transparency and the trading activity. He suggests that the pricing and price risk management should be left to the market forces rather than trying to achieve these through administered price mechanism.

R. Ramakrishna and Jayasheela's paper is on impact of futures trading on spot market and price discovery of futures market. The paper does not make any reference of futures fundamental on commodity futures. Their study concludes that the hedge is effective for the Nifty stock index futures whereas it is not effective in the case of stock futures. This study shows that there is casual relationship between spot price and futures.

Nilabhja Ghosh and Sangeeta Chakrabarti's paper on agricultural prices and futures trading and interaction and transfer of news, use the times series analysis method to achieve the objective. Their paper concludes the relationship between the futures market and the spot market in determining prices as a subject having close interaction between the two markets. They have illustrated this point with the help of statistics.

Arimandan Singh *et al.*, have made assessment of the problems in Indian agricultural commodity futures. They have highlighted that the objectives cannot be achieved unless the deficiencies are removed and difficulties are solved.

Growth of Commodity Futures, Subsidies, Globalisation Perspective and Futures Role in Indian Economy

Madhusudan Ghosh's paper is on growth and efficiency of Commodity Futures in the Indian liberalised agriculture and R.B. Singh and Vinod Kumar have submitted a paper on the impact of agricultural subsidies and procurement prices on production and income distribution in India. M.M. Rajput *et al.*'s paper on Globalisation of Indian Commodity Futures Market have covered the perception from international point of view. Swami Prakash Srivastava and Bhawana Saini have explained in their paper about the commodity futures market and its futures role in Indian economy. Paper writers of this group have made good efforts to highlight various issues related to Indian agriculture directly or indirectly.

Role and Marketing of Individual Commodities in Different States Including Price Behaviour and Contract Farming

A.R. Verma has discussed in his paper on Marketing and Constraints of Hybrid Cotton in Khandwa District of Madhya Pradesh. Bhag Chandra Jain and Hari Om Sharma have submitted papers on ‘Futures Market of Maize Cob in Raipur District of Chhattisgarh’ and ‘Economic Viability of Different Marketing Channels of Soyabean in India’ respectively. Anil Kumar discusses in his paper about ‘An Imperative Empirical Scenario of Price-Behaviour of Groundnut in Markets of Uttar Pradesh’. Arvind Awasthi and Abhishek Mishra have submitted a paper on ‘Rationality, Social Responsibility and Market Failure: A Case of Futures Trading of Wheat in India’. A.K. Gauraha and K.N.S. Banafar have discussed in the paper on ‘A Study on Contract Farming of Mentha in Chhattisgarh’. Subhash Chandra, R.C. Srivastava, B. Ganesh Kumar and others have submitted a paper on ‘Marketed Surplus and Price Spread of Milk in Bay Islands – Micro Level Analysis’.

III

ISSUES AND PROBLEMS

The commodities markets have developed at a fast pace within a short time span in our country but they cannot compete in the matter of stability and transparency with the international commodity exchanges. In fact it is the process of refining and re-refining methods, policies, procedures, acts and provisions to establish a system of fair trade for all the people who are directly or indirectly related with the commodities market. There are many issues which have arisen within the system of commodities market and the economy of the country also. India being an agricultural dominated country cannot ignore the commodities market structure of other industrialised countries of the world. It has a wider social and economic impact because majority of the people in India are dependant upon agriculture.

IV

ISSUES FOR DISCUSSION

1. Trading related issues
2. Institutional involvements,
3. Tax structure vis-à-vis speculative income
4. Physical Vs Electronic settlements
5. Social issues – fluctuations in commodity prices affecting directly the producers (farmers) as well as the end consumers.
6. Educating farmer’s inspite of various positive affects of commodities trading at exchanges. Its benefits are not available to the original producers i.e. farmers.

Intermediaries always tried to speculate the price which in turn leads to the consumer's bearing higher cost of commodities. The shortage of some of the important commodities and rising prices are not only affecting the consumers but also the commodity exchange players/members. One of the major objectives of including the essential commodities like wheat, rice, sugar and other items in the forward and futures trading is to benefit the producers but the result is big farmers and speculators only get benefit.

The intent and decisions of the government as mentioned in the Budget 2009-10 shall go a long way in transforming the Indian agricultural sector, developing our spot markets and mandis and ultimately lead to better and efficient price discovery for the agri commodities.

This would lead to a steady growth in the agri commodity futures volumes on the exchanges, as awareness about the benefits and close interplay between the spot and the futures markets shall help market participants to face the challenges of price volatility and manage the risks effectively on the Indian commodity exchanges. When this happens all across the country, then I believe we could achieve the status of a developed market where the benefits of growth reach out to all the stake holders, i.e., producers and the ultimate consumers.