

**GOVERNMENT OF INDIA
CONSUMER AFFAIRS, FOOD AND PUBLIC DISTRIBUTION
LOK SABHA**

UNSTARRED QUESTION NO:3233
ANSWERED ON:30.11.2010
FUTURES TRADING IN COMMODITY
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Will the Minister of CONSUMER AFFAIRS, FOOD AND PUBLIC DISTRIBUTION be pleased to state:

- (a) whether futures trading in a commodity is a mechanism for price assessment and price risk management;and
(b) if so, the details and the implications thereof?

Answer

MINISTER OF THE STATE IN THE MINISTRY OF AGRICULTURE AND MINISTER OF THE STATE IN THE MINISTRY OF CONSUMER AFFAIRS, FOOD AND PUBLIC DISTRIBUTION (PROF. K. V. THOMAS)

(a): Yes Madam.

(b): The futures trading in commodities is allowed in accordance with the provisions of the Forward Contracts (Regulation) Act, 1952 for performing two important economic functions, i.e., price discovery and price risk management.

The price discovery role of futures market is extremely valuable to the real sector of the economy in terms of planning business activity and for allocating commodity price risk. The price signals emanating from the market help various stakeholders in the commodities sector, viz., farmers, producers, processors, manufacturers, exporters etc. to plan their business strategies and use the futures markets to mitigate their price risks arising out of potential unfavourable price movements in the future.

The second important function performed by the commodity futures market is that of price risk management. Price Risk management is the process by which commodity market participants from the real sector, viz., producers, processors, exporters, importers etc. protect their businesses from adverse price changes in the future (which could dent the profitability of their business), by hedging their price risks in the commodity futures market. The price risk in the spot market is offset in the commodity futures market by taking an equal but opposite position in the futures market. Hedging benefits all participants like farmers, livestock producers, traders and merchandisers, food processors, feed manufacturers, exporters and importers.

Thus, by performing the two important economic functions of price discovery and price risk management, the commodity futures market serves as an important adjunct to the commodity spot market. It also helps policy makers to realign policies to meet likely shortage or surplus situation in a given commodity in the near future.