TWO MARKET CONDITION:

CONTANGO AND BACKWARDATION

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Before investing in the future market, traders have to encounter various technicalities that may hassle their mind. As the armed soldiers target the goal before battle, like wise traders must have the assurance of winning the trade. During the commodity trading, traders encounter two market situations, i.e. contango and backwardation. Pricing of the future market is the main aspect to be understood by each and every trader. Generally we can see the future price to be higher than the cash price. The higher price is due to the various factor like demand and supply in cash market, interest rates, sentiment, dividend yield and transportation cost. Let's take the example of gold in cash future price, let's assume gold is Rs 32900 in cash market and the interest rate is 9% per annum and insurance and interest rates are 5% per annum. In this market situation the future price will be 34051.5 assuming this is three months contracts.

Under normal conditions, the future prices of the commodity are always higher than the cash or spot price due to the cost of carry incurred in it. When the future prices are higher than cash price then this type of market situation is known as contango.

If any market indicates that is in contango situation then it means there are surplus in the supply of commodity. When the future price is below the spot price then the situation is backwardation, for e.g. if there is very little lentil available for delivery, the price demanded for what little is available can be very high.

Some commodity experts believe that the backwardation is entirely abnormal and seldom exists. But it may happen especially in the case of perishable commodity. According to a report, gold went to backwardation, in 2nd December 2008, at the COMEX in New York, December gold future (last delivery: December 31) were quoted at 1.98% discount to spot, while February gold future (last delivery: February 27th 2009) were quoted at 0.17% discount to spot. This means that the gold basis had turned negative, and the condition of backwardation persisted for at least 48 hours. Some experts believe that gold is going to stable backwardation which means that gold is no longer for sale at any price due to the lack of supply.

Contango indicates the existence of a good or surplus supply of the commodity in the warehouse for immediate delivery where as backwardation indicates shortages of supply of commodity. Here the term basis is used to describe the numerical difference between cash price and future price, the negative basis is called under future and positive is over future and at the time of expiry of contract the basis will be zero. In a contango market where the future price is higher than the spot price this narrow of basis benefits the short hedgers, who sells the future price and buys the

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underlying commodity. If the basis widens it benefits the long hedger, who buys future and sells underlying physical commodity. The frequent change in basis is not good for the short selling because short selling is the selling of a commodity that the seller doesn't own, selling a commodity or equity by borrowing from other traders or brokers and after given time trader close the short by buying back the same number of commodity or equity and return them. So in changing basis price short selling is very thorny.

Normally the future price of gold is valued at premium. Which means the future price of gold is greater than spot price in aspect of supply. This is very good for the economy because the supply of gold is limited and the higher price trend leads people to hold less of physical gold. Backwardation of gold means shut down of the free flow in economic system and this type of backwardation affects dollar a lot because there is inverse relationship between gold and dollar, so if the gold price turns towards backwardation then the present price of gold rise by decreasing the value of dollar which is not very good for US economy. Despite to this crude oil remains in backwardation in some case which means the price of future crude oil seem lower than the spot price, because the holding or storage cost is high. The future or forward premium will usually be quoted as a percentage of the underlying price. Gold is nearly always in a contango, but the backwardation may exist during price compress, but it rarely happens.

The two market condition contango Vs backwardation is very important for the commodity hedgers and speculators. The fact in the year 1993, the German company Metallgesellschaft lost 1 billon dollar because there expert team developed the hedging system under backwardation but they didn't anticipate a shift to contango situation.

In agro products like corn, wheat or oil, backwardation effect can be seen. Backwardation occurs in agro because the farmers or the commodity producer always try to lock their price from uncertainty of price movement. These people are not willing to sell their crops in uncertainty and always try to accept the current price assuming it as a high price to lock a sure profit. This is why the backwardation exist because there is low probability of supply of commodity in future, so the price of spot trend high than in near future. Let's take an example of Nepalese farmer of black cardamom, they have been observing prices of it, say the present spot price for immediate delivery is Rs 5000 per kg, but the farmers are not having much confidence of future increase in price of this commodity. Therefore, they lock the present spot price, in this situation the spot price is higher than future price, and this is one of the way how market turns contango to backwardation.

Therefore, the suggestion to the traders is to consider both the market condition, i.e. contango and backwardation before doing commodity spot and/or future trading.

GOLD V/S PLATINUM HURDLES

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If you turn the pages of history you will find that Platinum is considered one of the most precious of the precious metals' category. But, there are some ways to differentiate the characteristics of the "Rich Man's Gold". Platinum in the past had always led the other precious metals in a secular commodities bull run accompanied by palladium. Beside, platinum is considered having maximum volatility on the upside move as well as the downside move compared to the movement of gold. Since many years during the normal phase of price rise of precious metals, platinum always managed to enjoy a few dollars premium over gold price. Looking at the price history you will observe that the platinum & gold spread always widen up considerably among the precious metal group whenever there is a strong bull market. In the past two decades, platinum and gold spread managed to reach above 200 USD. But during the recent time the big question mark has come that whether Platinum is really a 'Rich Man gold' or not, as the Gold prices appreciated more than the price of the platinum in per troy ounce. At the current juncture the gold price is higher than the platinum price by almost 120 USD per troy ounce. Before we make some conclusion lets discuss some facts about them:-

Platinum: - Platinum is a white metal which is used in jewelry items almost in its pure form (almost 95% pure). Platinum is bright and white in luster and long wearing in nature. Due to this characteristic of platinum it does not require to be rhodium plated which is done in the process of making white gold. Platinum has more density then gold due to which a Platinum ring always feel heavier than a gold ring. Though in the past, platinum was more expensive than gold, a platinum ring always used to be more costly than white gold ring. If we have a close look at the World Annual Production of Platinum we will find that the World annual supply of platinum is just a mere 130 tons only- indeed scarce!

Gold: - Pure Gold is a bright yellow color metal. Its density is less than that of platinum. Among its physical characteristics it's soft, shiny luster, malleable, ductile and good conductor in nature. Its yellow color luster is traditionally considered attractive because it does not oxidize in air or water. It is among the least reactive metal thus it frequently occurs in nature in a free elemental form as nuts or grains in rocks or as dust in alluvial deposits. Rarely does it occur as compounds among the Minerals. As a compound it occurs with tellurium

Gold are used for making coins, medals, arts, design, jewelry and also used for the dental purpose & fabrication Industry. Gold is also the standards for monetary policies since the beginning of the human history. Later on in the late 20th century, it was supplanted as the fiat currency. Gold is also linked to a wide variety of symbolisms and ideologies. As of 2009 figure it's estimated that a total of 165,000 tonnes of gold have been mined in human history which is equivalent to 5.3 billion troy ounces. Of the total gold mined almost 54% is used purely for jewelry, 42 % of it is used for the purpose of investment and remaining 4 % used for industrial purposes. Many people around the world hold gold in form of bullion bars and coin which is used as a financial tool to hedge against inflation, currency devaluation or economic problems.

Thus after knowing about both platinum and gold it's good to know, how much of a relationship do these metals really have. At the current scenario gold is the talk of the town as its popularity is growing as the safe haven of investment during wild economic crisis. But with regards to platinum, one can hardly hear of this metal as the average investor knows very little about this metal, although it is on the same playing field as gold. As both Platinum and gold are definitely on the same level field as both of them are categorized as precious commodities. In the powerful secular bull markets which is supported by strong long-term fundamentals we observed that the Platinum's bull gathered momentum around the same time as gold's, in 2001, and we

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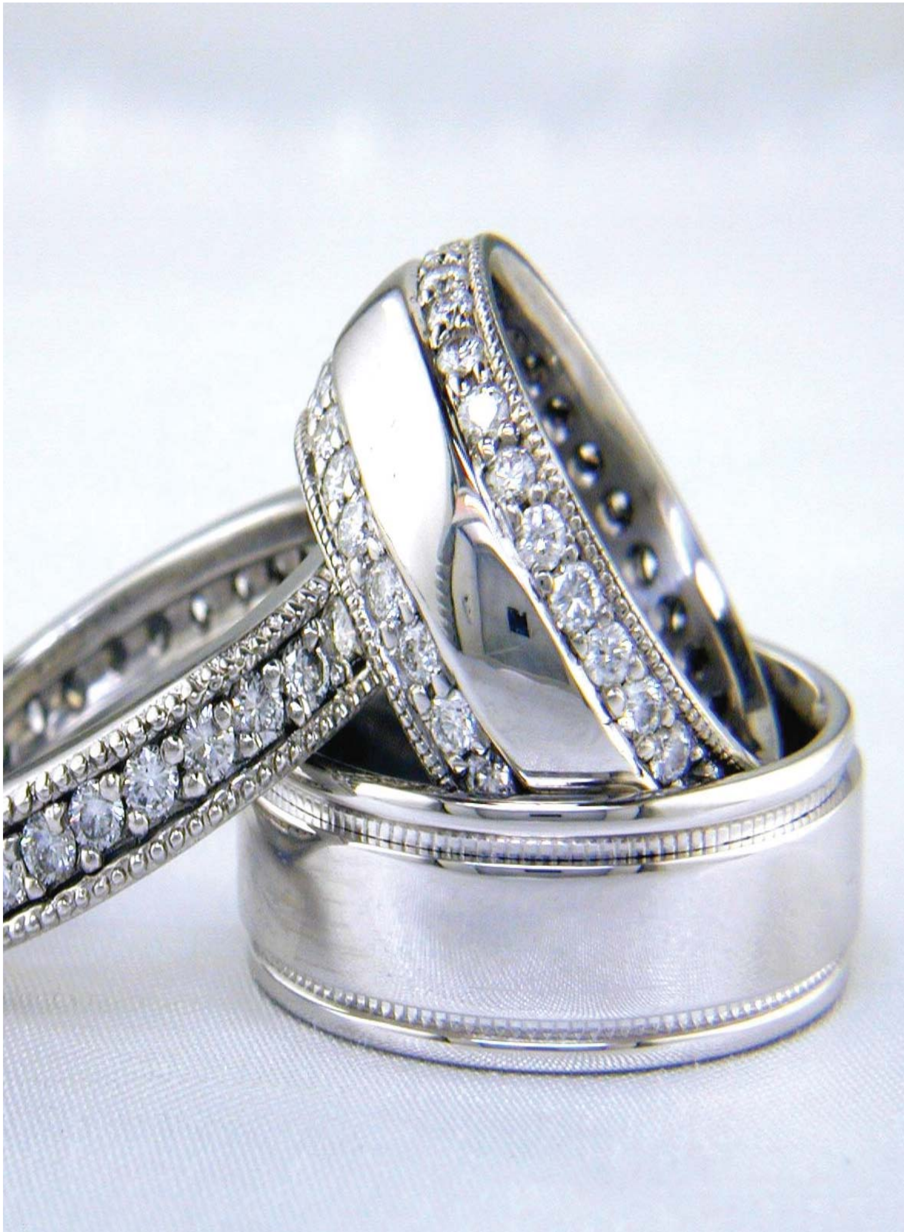
saw a gain of 448% compared to its 2008 high. In fact, measured by historic price movement, platinum is more precious than gold as the former made a historic high of $2273 in March 2008.

But currently i.e. 11/11/2011 Platinum is at 1611 USD level where as gold is higher than platinum by USD 150 i.e. at 1761 USD Level.

Platinum bulls have not yet tested its highs while gold has blown through its own and managed to make all time historic highs in 2011. But what I believe is that it can be easily explained that when you consider the usage of these metals then through simple economics it explains that the precious-metals story has played out in recent years.

With continued supply strain on the mining fronts for both platinum and gold, it is the activities on the demand side of the economic scale that have of course been the big price drivers. And as anyone with a pulse is fully aware, the current global recession has radically altered the demand for virtually all goods and services. If the Investment appetite further increases for these metals added by demand which continue to grow and economy continues then platinum will quickly move to a deficit environment. And this will of course stimulate prices to move more higher in the days to come. Thus we can expect that platinum prices to move higher once again as strong fundamentals are holding it back. So the conclusion is that we could see platinum prices moving higher once again against gold and platinum would be first hitting the USD 2300 mark before gold.



GOVERNMENT AND REGULATORY BODY: THE INTRICACIES DISCUSSED

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No market functions in a blankness. In order to be proficient, the market requires a dynamic, unwavering support from the government. Government with different role: a role of oversight, finding those who try to influence or manipulate the markets to their own benefit and guarantee the inviolability of contracts; and a facilitating role, providing the necessary legal and regulatory framework. Markets need the government - the only problem is that over regulation should be avoided.

Over regulation results in the lack of understanding on the functioning and purpose of Commodity Exchanges. Well knowledge of this market is very essential. This market, if they function well is an image of physical markets. Presently we have few well-placed companies or a dealer who knows about the supply and demand conditions of the physical market. Through the functioning of futures market, these trade secrets are made visible for the whole people. It's only the commodity exchange that can bring the message to

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the government about the state of demand/ supply, whether they are good or bad. But if bad they should not be blamed for this.

Inadequate understanding of the role and significance of commodity exchanges to the economy of the country can certainly lead to policies that harm the exchanges and their users. Exchanges can function only with support of government, with a framework regulated by government. Government need to come with such a policy for exchanges so that direct and indirect investors or users can rest assured. Government should facilitate or enable the working of exchanges through a provision of appropriate legal and regulatory framework.

Taking into account the large potential benefit of commodity exchanges for a country's economy, governments must provide a proper regulator for these markets.

The major part of investor protection is transparency and information. The investor needs to gain confidence by getting complete transparent view of the market and its function, as well as the right to information must be assured. In this provided circumstances the investor can better evaluate the possible risks and rewards of their deal and protect their benefits.

Total Capital market is directly linked with peoples hard earn money, so the managers of the fund must be enough competent and resourceful to manage the public fund.

Furthermore if current licensed holders didn't meet the new capital requirement by regulators, then they should allow winding down its business without doing any loss to its customers.

The regulator should set least standards for all the market participants. The market intermediaries should follow and refer to rules and ethic of business which guarantee the investor satisfaction.

Recently Brazilian Securities, Commodities and Futures Exchange which is one of the world's largest exchanges in market capitalization and its self regulatory organization installed a hi-tech surveillance system of Nasdaq OMX to monitor trading abuses and manipulations of all the participants in this field. Such steps from the regulators are to ensure the safety of the investors and traders, and only regulatory body can do to an extent.

Before deciding the rule's and regulation for the market, regulators must sit together with all the participants and discuss the various issues which may directly or indirectly impact whole the market area. Regulators are the watch guard who should be able to lead the market to function efficiently and should never step down in any circumstances.

The upcoming commodity regulation must address the trading operational requirement of the business, additional it should allow exchanges to design their own contracts which will enhance the competitive advantages of the Nepalese commodity derivatives.

Most of the eminent commodity exchanges of Nepal are interested in developing the facility to offer physical delivery. In upcoming act the power and duties of exchanges, clearing house, Non-clearing brokers as well as right of the clients must be clearly mentioned, and finally the regulatory requirements should include adequate defend against money laundering policies, but all this will be just a fantasy without proper regulation knowledge and ideas.