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The properties of commodity spot and futures-markets

The ongoing debate about food commodity speculation began when food prices spiked in recent years (especially in 2008) and thus lead to food crisis in many developing countries. Since these price spikes coincided with increasing investments in commodities, many non-profit organizations (NGOs) and some political parties blame investors for rising food prices. As a result, a stricter regulation of commodity investments is demanded in the hope of banishing further price spikes. In Switzerland a political party went even further and aims to ban investments in food commodities at all. Unfortunately, the role of investors in commodity markets is often misunderstood, since futures (derivative) markets seems to have a complex or even mysterious mechanism and their economic and social benefits appear doubtful.

The purpose of our presentation is to give basic knowledge of the functioning of commodity futures markets and addresses the following issues: first, we differentiate the physical (spot) market form the derivative (futures) market. Second, we describe the relationship between spot and futures prices and how futures prices may affect spot prices and vice versa. Third, we highlight the important role of inventories as a buffer against supply and demand shocks. Based on this explanation, we attempt to answer the question, is speculative investor demand able to increase or push commodity spot prices? Furthermore, the term “speculation” will be defined and why a distinction must be made to “manipulation”. With the presented basic knowledge, embedded in the current grain-market environment, people will be able to form their own judgment regarding this controversial and emotional topic.