Expansion of futures markets toward their full potential in the commodity world can be accelerated by making changes in the operation and development of the markets. The key to expansion is increased and improved speculation. Growth is dependent on the inflow of new equity capital and equity capital is synonymous with speculative capital. The expansion of speculation to greater direction of commodity production and inventory use is necessarily a move toward a closer approximation of the model of perfect competition. An increase in speculation results in an increase in competition and vice versa. The road to attainment of perfect competition is a rocky one because everyone involved, consciously or otherwise, seeks a noncompetitive shelter. The problem is to probe for weaknesses in the system and suggest changes that will increase speculation.

The moving force must be the markets themselves. They are the only neutrals in the contest. And they are only neutral to the extent that they include, in equal balance, all of the diverse elements of the commodity trade. There are fairly strong tendencies toward noncompetitiveness on the part of exchanges themselves. They have done a remarkably good job of maintaining balance of representation of the diverse interests of their members—democratic governance does work effectively in maintaining competitive balance. But exchanges tend to look inward and, in extreme cases, act as if they were private clubs. Exchanges must be operated in the best interests of the long run efficiency of the industries they serve. In the very long run, this goal is compatible with the self-interests of the exchange membership. The achievement of the semi-public utility role places a heavy burden of responsibility on the exchanges.
Why Markets Fail

The history of markets is replete with instances in which trade has dwindled to zero and in which the trade is so small that it is not significant to the commodity that it is designed to serve. The reasons for failure of markets are not readily apparent if they are at all ascertainable. The broad brush answer is that markets are not used when their use is not more profitable to existing and potential users than some other method of coping with financing and pricing problems. Markets in which there is a consistent upward bias so that short hedgers chronically lose money soon discourage hedgers. Markets with a chronic downward bias eventually get too expensive for longs to use whether the longs are commercials or speculators. Only the markets without discernible bias trade in large volume. In addition to chronic price bias is a lack of liquidity. If the prompt execution of orders requires appreciable price concession, up or down, use is soon judged to be too expensive. As the outside trade of commercials and speculators decreases, the attractiveness of the markets to the locals—the liquidity suppliers—decreases and the liquidity problem is further aggravated. Those markets that work, work well, but those that don’t work dwindle and disappear. Successful futures markets are zero sum games, equally attractive to longs and shorts. Five principal reasons for the dwindling and demise of markets can be pulled out of the history of market failure.

First, one market failed because it was legislated out of existence—onions. The Maine potato market has had some close calls from this kind of death.

Second, markets have lost their economic basis for existence. While there are instances of markets, pork bellies in particular, prospering without a large commercial or hedging base, we should continue to accept the general concept that the markets originate out of a need to shift risks and their size is determined by the amount of hedging use. When the need for use by hedgers decreases the markets decline and disappear. An outstanding example is the storage egg futures market. It developed and grew out of a need to shift price risks associated with inventory ownership. In time, technological developments in egg production resulted in the virtual elimination of the seasonality of production so that inventories were not built up. Year by year the size of inventory decreased and the build-up of open interest in futures almost exactly paralleled it. The market nearly went out of existence as the need for it declined toward zero. The storage egg contract was not suitable for hedging fresh eggs. The Chicago Mercantile Exchange gradually shifted to a fresh egg contract and this market has grown rapidly as the changing structure of the egg production industry has created an increasing need for the forward pricing of egg production.

A second example is the cotton futures market. For many years, the cotton futures market was one of the most active commodity markets. From 1955 on,
Market Development

Trade in cotton futures declined to the point of vanishing at New Orleans in 1964. With the exception of a brief flurry in 1968, trade at New York was very small until 1971. The overall decrease in trading was the direct consequence of the entry of the Federal Government into cotton merchandising. The cotton price program was operated in such a way that the Commodity Credit Corporation bought and sold most of the U.S. cotton at a very narrow range of prices, eliminating the need for hedging by cotton merchants. Until 1971, trading went the way of economic basis for merchant hedging. The unusual situation that developed in 1971 was a combination of a sharply reduced supply, a small prospective production and a crop scare. This stimulated great speculative and trade interest since it potentially removed the dominance of the Government in regulating prices.

When the general upheavals in commodities occurred in 1972, the cotton price, too, was ripped loose from its anchor in the government support system. There was an immediate and very large increase in the volume of trading and the size of the open interest.

Much of the increase in futures trading in the grain complex from 1972 onwards was the result of the disappearance of the government as a price making force. Should government programs again dominate agricultural prices there will be a decline in the need for, hence the amount of, futures trading.

Third, markets have failed because of weakness in contract terms that gave an advantage to either the buyers or sellers. If the contract terms are out of balance they enable either the buyer or the seller to squeeze the other so that one side chronically profits at the expense of the other. This is discouraging to the losers and, in due course, they refuse to play. A futures contract is a temporary substitute for a cash transaction that will eventually be made and it must reflect commercial standards and movement closely enough to avoid price distortion.

A turkey futures market was quite active in 1962 and 1963 but then dwindled rapidly. The terms of the contract permitted delivery of packaged and branded turkeys that were difficult for someone other than the packer to merchandise. It became a dumping ground for the surplus production of turkey packers, to the disadvantage of the longs.

Fourth, markets fail because they are boycotted by commercial interests. As we have seen, the development of an active futures market represents an increase in competition; it puts the commercials in a more competitive position. There is a marked and understandable tendency for the commercial interests in a commodity to oppose futures trading at its outset. After markets are developed the strongest supporters are the commercial users but they have to be forced into use by the superior risking and pricing efficiencies of the markets.

We should not want to suggest that the political hue and cry that resulted in the execution of the onion futures market was generated by onion dealers but we could not blame them had they been responsible. Their advantageous
monopolistic position was wrecked by the development of the market and restored with its demise.

Cottonseed oil futures trading was of major importance until 1963 but has since died out. The reasons are not clear and there are likely several but one important one seems to be a boycott by cottonseed oil producers and users. They can cover the bulk of their price level risks in soybean oil futures and work the differences between cottonseed and soybean oil prices to their own advantage. If they are to return they will have to be forced back by competition from speculators.

Fifth, markets fail to attract speculation. The short and long positions taken by hedging firms are almost never evenly balanced. Speculation is essential to the balancing of hedging positions and to liquidity. Hedgers are predominantly short. If sufficient speculative buying is not attracted, futures prices are unduly depressed, hedgers lose money, and discontinue use of the markets. Markets may be built on the need to shift risks and raise equity capital but it is certain that they cannot successfully exist without an adequate speculative interest.

These several reasons for failure of markets suggest that for a futures market to succeed there must be an economic need, the contract terms must be right, hedgers must be either attracted or forced in by competition, and there must be an active speculative interest. But the problem is not that simple: markets are built on commercial use and speculation is attracted but markets will not be used by commercials unless speculation is present. It is difficult to get markets off of dead center.

The Exchanges

What steps should markets take to accelerate expansion? As a general proposition they need to recognize their role as semi-public utilities whose purpose is to serve their outside trade—speculators and commercials. To the extent that exchange governance is weak in this recognition, the faults seem to lie with too much control by the locals who are present every day and too little by the members who represent the outside trade. There are many members of the exchanges who belong only to get reduced commission rates and who never go near the markets nor participate in the affairs of the exchanges. Some improvement might result from a change in the commission structure so that it would be less favorable to members. The exchanges should consider having more than one class of membership with different voting rights for each. Some would benefit from turning more control over to paid administrators. But in the main, improvement must come from enlightened membership and is a slow process.

Contract Terms. The purposes of futures trading are other than exchange of title. In instances in which delivery has been extensively made and taken markets have failed. In broad context, the purpose of futures trading is to
enable specialized speculation; to separate the speculative functions from production, processing, storing, merchandising, etc. Thus, the theoretically perfect futures market is one on which delivery is neither made nor taken. The market must protect the speculator from having to procure and make delivery and from having to accept and merchandise delivery. At the same time the contract must be commercially real, representing and pricing actual commodities as they exist and are used in ordinary commercial activity. The rights and obligations of delivery must be inviolate. The contract must be so readily deliverable and so easily takable that neither party has reluctance to make or take and, thus, no desire to make or take delivery. Delivery is made and demanded to test markets and to force price relationships into line but the better the contract, the less this occurs. When it is possible to distort prices or price relationships by making or taking delivery, there is a fault in the contract that is in need of correction.

The existence of a futures market with its obligation to make and take delivery should not distort the flow of the commodity in its ordinary marketing channels. The pricing system, of which futures trading is a part, must adapt itself to the physical marketing problems, not vice versa. The objective of contract delivery terms should be to sample the flow of the commodity, test it for its value in exchange, and return it to stream.

The writing of futures contracts is difficult and the terms of the contracts need to be continually revised to maintain balance between buyers and sellers. Changing the terms of contracts is not simple. It takes agreement on the details by the committee of diverse interests that is appointed by the exchange. A soybean meal committee properly includes processors, feed manufacturers, merchants, and exporters. Each member is torn between loyalty to his company's advantage and service to the industry. As a result, changes are difficult to bring about. Once trading in a delivery month is authorized the terms of the contract cannot be changed for that delivery. Thus, there is always a lengthy transition often involving two different contracts for a particular month. The existence of two contracts in a commodity at one time is confusing to speculators and makes basis operations difficult for commercial users. It is avoided as much as possible.

Exchanges must have supervisory control of delivery. The clearing house is finally responsible for the fulfillment of delivery terms—that payments is made, that quality is appropriate, that delivery is made on time, and that warehouse receipts or ownership certificates are bona fide. This results in a tendency for delivery on contracts to be restricted to locations and to firms that can be supervised with a minimum danger of fraud, default, or contract violation. The supervisory requirement also makes contract change difficult.

Contract terms must be kept as simple as possible in the interest of the position of speculators. The speculators are not merchants and so are at a disadvantage when they must make or take delivery. From the individual speculator's point of view the solution is simple—stay out of the delivery
month. However, this does not solve the problem of contract balance. Except as contract terms are kept simple and delivery restricted, speculators are put at a disadvantage and the long side of the market is weakened.

With this set of thoughts we have set up a contradiction. In the interest of representativeness we have argued for wide open delivery but in the interest of balance between speculators and commercials, we have argued for restricted delivery. Given this choice we will side with restricted delivery, for delivery terms have been too long modified and watered down to prevent market congestion. The futures contract, hence the futures price, should represent the top quality commercial commodities that are traded in substantial volume. If the standard trading grade of soybeans is U.S. No. 1 the futures contract should require U.S. No. 1. If the premium location and the place of the largest volume movement of soybeans is Gulf Ports, the Gulf should be the delivery point. If the standard item of commerce is strictly fresh eggs, the contract should specify strictly fresh eggs. The key consideration is that a readily merchantable commodity be placed in the hands of longs on delivery.

The long term preoccupation of the markets and of the government in connection with delivery terms has been the prevention of corners, squeezes, and price distortion associated with limited deliverable quantities and qualities at delivery points. The rules have been repeatedly relaxed to permit delivery of less than contract quality at approximate market discounts, delivery in high-rate warehouses, furnishing of minimum freight billing on delivery, and the suspension of trading before the end of the delivery month. Nearly every modification has been made in the direction of strengthening the position of the shorts versus the longs—the position of the commercials versus the speculating public.

Too restricted delivery terms can lead to congestion and price distortion although, as we saw in the last chapter, the danger of this tends to be exaggerated. The solution is simple: allow off grade, out of position delivery at punitive discounts. If the usual cash market discount of No. 3 corn is 2 cents under No. 2 let it be delivered at a 4 cent discount, etc.

That these suggestions for tightening up delivery are designed to strengthen the position of speculators does not mean that they are disadvantageous to normal hedging operations. They would be useful in preventing the putting of off grade commodities out of position for the purpose of creating an abnormally wide basis or distorting futures prices downward. This goes back to the notion that a short side distortion is easier to engineer and profit from than a long side distortion. A tightening up of delivery terms would tend to regularize price relationships, both over space and over time because it would make contracts more concisely representative of commodities traded. Normal price relationships are essential to out of delivery position hedging.

Promotion. During most of their existence the main objectives of the exchanges in their relationships with the public has been to keep a low profile.
The general negativeness toward futures trading led exchanges to feel that any image was bound to be bad and so the less image the better. They fought their political battles in smoke-filled rooms. A marked change occurred immediately following World War II when some of the exchanges, particularly the Chicago Board of Trade, began to develop educational programs. The Board celebrated its centennial in 1948 with a big bash, including extensive publicity. It took the position that if it had survived 100 years, it was a useful institution and the story should be told. It, and other of the exchanges, have continually sponsored symposia, seminars, research fellowships, educational films, and tours since that time. In addition the exchanges publish informational booklets and classroom materials. Most of this effort has been directed toward the educational system, particularly colleges. The objective is to introduce the subject matter into curricula and have it presented in a favorable light. Interestingly, the primary motivation appears more image building than promotion of new business. Exchange members truly believe that futures trading is a very useful institution and feel badly about the generally unfavorable image that it has so long had. The extent of success and direct effects of these programs is not measurable but the extent of general knowledge about futures trading is greater and the image is more favorable than it was in 1948. There remains a long way to go.

Beginning about 1960 some exchanges undertook more direct promotional programs. These were aimed at commercial interests, primarily smaller processors, country elevators, and, more recently, livestock producers. As new commodities are introduced, the exchanges make major efforts to acquaint the relevant trades with the nature and uses of futures markets. The objective is to teach firms how to use futures in connection with their businesses. This effort is useful in the introductory phases but the job is far greater than the resources of the exchanges permit; the bulk of the work must be done by the people who get revenue from trade—the commission houses.

So far so good; the efforts relate to general education and trade use. In the 1960’s the more touchy area of promotion of speculation was introduced. This has been done on a modest scale with documentary type films and newspaper and magazine advertisement. It has been circumspect, not suggesting speculation but only inviting further inquiry. This development raises two questions: To what extent should the exchanges promote commodity speculation by the public? And what are the obligations to the public in teaching them to speculate in a way that will give them a reasonable chance of success? A lot more speculation than existed in 1976 is needed and its quality needs to be improved. Exchanges should not be reticent in calling attention to the merits of commodity speculation. Their only guideline should be the fact that futures trading is a zero sum game minus commission. Again the size of the task is beyond the resources of the exchanges and should be mainly left to the people who collect commissions. The main role of the exchange should be the development of
educational materials for the use of others in teaching the public how to speculate.

**Control of Commission Houses.** The bulk of the job of promotion, development, and improvement of speculation is and will continue to be done by commission houses. It is important that their behavior be especially circumspect. All of the exchanges need to review their rules as they apply to commission house customers, particularly speculators, and develop sets of rules and supervisory procedures that will assure high professional standards of performance by commission houses.

The control of the activities of commission houses vis-à-vis their customers is difficult. When a small commission house holds membership in only one exchange or concentrates its activities in the commodities of one exchange it is easy to control. Large exchanges are able to control the behavior of commission houses because of the importance of trading on the large exchanges to the houses. But much of the match-up is small exchange and large, multi-exchange commission houses. Here, the ability of the exchanges to control is inherently weak. Exchanges are dependent on commission houses for volume. Commission house customers go to the exchanges and commodities that the houses recommend. A boycott of or failure to support an exchange by several major houses can be ruinous to an exchange. It is sometimes thought that large commission houses have more than optimum power in the governance of small exchanges.

**High Cost of Overhead**

Prior to 1973 all commodity exchanges prescribed minimum commission rates that commission houses had to charge customers. They did not establish maximum rates but this was not of consequence because the minimum was invariably the maximum. They prescribed nonmember rates, member rates which were usually one half of nonmember rates, floor rates which were about 10 to 15 percent as large as member rates, and scratch rates for trades made in pits at one price by scalpers that were but a fraction of the floor rates. In addition they prescribed the fees that brokers were paid. In 1972 the Department of Justice brought action against the Chicago Board of Trade under Anti-Trust law for price fixing. There followed class action suits against numerous exchanges and commission houses. In 1973 an agreement was reached by which fixed commissions would be gradually phased out by early 1978. The first step was to make commissions on trades of 25 contracts or more negotiable, then six months later, trades of 20 contracts or more become negotiable, etc.

The change is not complete at the time of this writing nor is the effect on commission houses to date known. In general, commissions have been increased with inflation. The increase has not been uniform. Houses that provide a minimum of services for customers or that specialize in larger accounts have tended
to forego increases in the rates charged. Full service houses that handle smaller accounts have increased the most.

The fixed commission charge per contract was not economically rational—no fixed price ever is, else it would not be fixed. The charge for a two contract trade was $60 and $300 for a ten contract trade, but the cost was not five times as great. Brokerage and clearing fees were greater and the order transmission and accounting costs were greater if the larger transaction was offset in installments but there was no way for the cost difference to be $240. Inactive accounts that trade in one or two contracts per year are much more expensive per contract than active accounts. Some accounts call registered representatives incessantly and request large amounts of information, publications, etc., while others only use the commission house to take and execute orders and keep accounts. There is a tremendous range in profitability of accounts.

We can only speculate about the eventual impact of decontrolling commission rates. Some combination of several things will likely occur. First, the per contract rate will be reduced for large trades and increased for small trades. Competitive rates will become cost rational.

Second, commission rates may eventually be tied to some concept of annual volume of business done. Most of the cost of an account is fixed. The accounting procedure, the rendering of monthly statements, the furnishing of market letters, the research overhead are not directly proportionate to the volume of business done. The time that a registered representative must spend in opening and servicing an account is not directly proportional to volume. Small accounts often take more time than large accounts. One problem that commission houses encounter is that customers sometimes trade with more than one house to get a variety of opinions and move from house to house frequently. A system of charging one amount for the first 100 contracts in a given year, and a lesser amount for succeeding trades on a scale down may evolve. It would be cost and reward rational.

Third, there will be an unbundling of services. Clients that want only execution and accounting will be able to obtain it at lower rates. Clients that want, in addition, market letters and advice will pay more, and clients that want full service including business operational programs will be able to get it but will pay more.

Fourth, commissions will be related to customer success. This can take different forms. One could be quite indirect in that houses who can show good results obtained by customers can command higher commissions than others. Some houses may go directly to relating commissions to results.

Fifth, there probably will be an increase in nonmember Futures Commission Merchants. With fixed commission rates, the only incentive that many members had for owning memberships was reduced rates. With fully negotiated rates some merchants will not have incentive to belong to exchanges. This will raise
Market Operation

problems that exchanges have in exercising control over the way that commission house customers are handled.

**Commissions Can Be Costly.** One lesson learned from the look at trading results in Chapter 13 is that commission charges are large in relation to the total amount of money that changes hands—the slot in the table drains a lot of money out of the game. If the objective is to maximize the amount of speculation and the amount of equity capital generated by the system, the cost of operating the game must be held at a minimum.

When compared to the total value of the commodity represented by the contract, commissions are small; $40 per contract when corn is $2.50 per bushel is .3 of one percent and $40 per contract of soybeans worth $5.00 is only .16 of one percent—impressively small numbers. They are much larger numbers when compared to minimum margin requirements. When the commission is $40 and the margin requirement for corn is $1000 and for soybeans $2000, the commission charge is 4 and 2 percent respectively—much less impressive.

Commission charges are small when compared to the size of price changes that regularly occur in commodities. A 3/4 of a cent change in the price of a bushel of corn covers the cost of commission as does .06 cents per pound of soybean oil, etc. Speculators show little concern about the cost of commissions and the volume of their trading does not seem to be affected by commission rates. But, as we saw, they should be concerned. They cannot afford to trade for small price moves because commission charges tip the profit—loss odds against them. A one cent profit on 50,000 bushels of corn is a net profit of $100 while a one cent loss is a net loss of $900. Prospective moves have to be fairly large before a speculator who pays full commission can intelligently participate; the fine tuning of the market is left to the people whose cost of trading is small.

In our cursory look at the results of speculation in Chapter 13 we noted that the difference between profit and loss for the regular traders was commission paid. Other studies have shown much the same thing. Commissions are a large cost in a zero sum game. It grinds up a lot of speculative capital. There would be more speculative capital available if the cost of commissions were less. This does not mean that profits are inordinately large—they are not. It does mean that commodity speculation can be increased more readily if the cost of commission can be reduced. It can be done in two ways. First, by reducing the frequency of turnover of positions held by speculators. They would choose positions more judiciously and hold on to them longer. Were this to be accomplished they would probably be more successful, not only because of lower commission costs, but because one of the most serious faults that speculators have is over-trading. They tend to continually trade, which puts them in competition with professional locals and, in that game, they have little chance of success.

Second, by increasing the size of the capital units controlled by one person whether an individual trader, a registered representative, or a commodity trading
Market Development

pool. The arithmetic of being a registered representative is illustrative of the principle. Registered representatives typically get one third of the commissions they generate. If the average account generates one dollar of commission for each dollar of average value—which is not far from the current industry standard—the RR must control an average of $90,000 to have an income of $30,000. But if he controls $360,000 he can have the same income by trading the accounts only one fourth as actively. To reduce the activity would not mean that the money would be kept less fully invested but only that it would be turned over less often.

There are two powerful forces that work against a reduction of turnover. RR’s are predominantly paid by the contract. This is a strong incentive to encourage activity. Commission houses have the same incentive.

Second, commission house customers have a built-in bias toward over-trading. They are unhappy if they do not have a position. They tend to want to grab a quick profit rather than wait for the whole of a situation to develop. They take larger positions than their available capital justifies and so are forced to take numerous small losses.

The operation of commodity pools is relatively new and the best methods of operation are not known. One thing that seems to be evolving is that they are more successful, as they hold a large proportion of their capital in reserve and as they are able to filter out the price static that surrounds markets as they make major moves.

Commission House Operation

The rudiments of commission house operation were discussed in Chapter 3. The objective here is to explore some ways in which improvements in commission house operations can contribute to increased and improved participation in futures trading. The remarks are necessarily critical because they deal with changes. This should not be construed as a negative attitude toward the commission house industry as it now operates; they do a generally conscientious and competent job.

The commission houses are the primary instruments for expansion and improvement for they are the firms that gain revenue from growth. They are the ones who have the money needed for promotion of trading and the training of traders. They must bear a heavy burden of responsibility for achievement of the aggregate goal of market growth. This requires far-sighted operation and willingness to forego short-term gains in the interest of long-term gains and the general welfare of the industry.

The basic objective of commission houses must be to get traders to succeed; if the "how to" chapters in Part III of this volume are correct, to get traders to operate as recommended there. The primary emphasis is on speculators, not on
the larger and successful speculators but on the smaller and unsuccessful speculators. It is a challenging task because futures trading is a zero sum game in which traders try to take each other's money; the rate of failure must, by the terms of the game, be high.

Commission houses must play a major role in the development of new markets and the expansion of undertraded markets by seeking out the best speculative opportunities and guiding speculators to them.

Speculators tend to be vain and greedy. They enter markets because they have heard of someone who has made a lot of money from a little very quickly. They are after a fast buck, fail to understand what the game is about, and are not aware of the work, discipline, and patience that is required for a reasonable chance of success.

Speculators fail to grasp the basic concept that speculation is about forecasting prices of commodities that move in commercial channels. They depend too much on the advice of other people and, as a result, fail to make progress in developing forecasting skills. In their quest for action they frequently go outside their own areas of competence and trade in commodities they know nothing about. Few speculators appear to have any concept of money management. They trade for quick returns from soybean or cocoa price changes rather than for returns on invested capital with objectives that are established in relation to the risks they are willing to take.

Finally, few speculators understand how to admit error and take their losses before they are put out of the game. Part of the reason for this is that account executives are loath to say, "I blew it; take your lumps and let's try again.", part stems from the natural optimism that is required if one is to enter the game, and part from the misguided notion that losses are only "paper" until a trade is closed.

This is the assortment of errors and suicidal tendencies that commission houses must cope with if they are to develop a new breed of improved speculators.

*Training Registered Representatives.* The registered representative is the place where the system meets its lifeblood—the commission house customers. The success of markets is dependent on outside trade. Commission house earnings depend on the generation of commissions by RR's. The long run growth and development of futures trading will depend on the effectiveness with which RR's perform. Being an RR is a complex job requiring skill and a good working relationship with the house. As the futures trading industry expands there will be need for an increasing number of RR's. The structure of the commission house industry and the method of compensation has not been conducive to the development of effective RR's. In the mid 1960s a centralized examination was developed that one must pass to solicit business for commodities traded on major exchanges. But it does not require much knowledge or training. Some
commission houses have established training programs but they are usually fairly brief. In the main, all that is required is that one be willing to undertake a job that is compensated on a piece work basis.

Training programs need to be developed that will adequately prepare people for securing and handling customer accounts. Ideally, these should be based on the curricula of universities. Cooperation between the commission house industry and the colleges is necessary in development of such curricula, for the knowledge and teaching of commodities and futures trading is limited. A training program should be broad, including not just the specifics of actual trading, order transmission, and contract terms but also the study of commodity price behavior, investment portfolio management, and psychology.

Compensation of RR’s. Alterations or changes in the compensation system should be considered. Football coaches get fired when teams lose too often and get raises and new automobiles when teams win. Perhaps this should be the system for RR’s; pay them bonuses when their assigned or recruited customers win and fine them when their customers lose. "But where are the customers’ yachts?" is an old joke in the securities brokerage industry. One commodity house has a Yacht Club to which the RR’s whose customers have been the most successful are admitted. There is special compensation to the members.

There needs to be incentive for performance and performance is the generation of commissions. But there is need for the industry to take a longer view. It needs a compensation system that does not put undue short run financial pressure on its employees. RR’s must have time to develop a clientele that has a reasonable chance of success.

Selection and Control of Customers. Houses vary in the standards that they apply in accepting customers. Some only want to know if the prospect has an initial margin although even the most nondiscriminating try to see that the man is not playing with the rent money. At the other extreme, some houses require complete financial and income statements and limit the amount that can be put into commodities to the amount that they judge the prospect can afford to lose. There are all gradations. Note that these standards are based on the cynical attitude that the customer is probably going to lose money.

What is needed is a more positive approach. Commission houses should aggressively seek out people who need but are not currently using futures in connection with cash commodity businesses and people who have a reasonable probability of success as speculators. They need to do some serious study of the factors affecting customer success and methods of identification of speculative talent. Even the best of football coaches lose if they don’t have the horses and most spend more time recruiting than coaching.

Control of customers is both important and difficult. The two worst faults that speculators have is letting losses get too large and letting success go to their heads so that they overtrade. It is difficult to stop a man from letting his losses
run as long as he produces adequate margin money. Houses can watch closely and advise, and they can put teeth in their advice by raising margins for individual customers. This latter course is apt to cost the house a customer but no customer is better than a losing customer. Forcing customers to accept losses is also dangerous because the house doesn’t know what is going to happen to the price. They may succeed in forcing a loser out just at the time that the price turns around. There is no weapon other than moral suasion to slow down a customer who holds a hot hand. The best course is to try to prevent his getting really clobbered when his hand turns cold.

*Training Customers.* More resources need to be put into the training and management of customers. The houses should get to know customers well, evaluate their forecasting skills, and help establish their investment objectives. This requires not only a flow of information and advice about positions but a continuous flow of the rationale behind the advice. The goal must be the development of competent, specialized, commodity analysts.

Finally, the name of the game is money. Customers need to be taught how to establish investment objectives and how to manage money in the ever changing profit-loss picture so that they have the best shot at success.

*The Problem of Taxes.* Under Internal Revenue Service regulations commodity futures contracts are capital assets. When traded in connection with a cash commodity business, gains and losses are treated as ordinary income. When traded by speculators they get capital gain and loss treatment. Gains on long positions held less than six months are taxable at ordinary income rates. Gains on long positions held for more than six months are long term so that only half of them are taxed. All gains on short positions are taxable as ordinary income, regardless of the length of time held. Only $1,000 of losses are deductible from ordinary income. This set of rules reduces the available speculative capital and results in some modifications of trading activity that may not be economically productive.

Suppose that two speculators, whose marginal income tax rates are 50 percent, take opposite market positions; one long, the other short. Suppose that the price goes down so that one loses $20,000 and the other makes $20,000. Suppose further that these are the only transactions that each makes in the year. The winner will pay $10,360 in taxes and the loser will have his income tax reduced by $480. $9,880 is taken out of the game by the government when there is no real gain or loss. The government is an interesting partner in commodity speculation, taking an increasing share of winnings and refusing to participate beyond the most niggardly way in losses. It is a "heads I win, tails you lose" game.

It is doubtful that many people are discouraged from speculating in commodities out of tax considerations, but tax treatment lends incentive to trading in ways that will postpone taxes and sometimes provide long term rather than short term gain. Tax modification can be accomplished by spreading, and the most
popular spreading vehicle at this time (1976) is silver futures. Tax spreading may turn out to be the primary economic use of gold futures trading. The silver market has never been cross-sectioned but a cross section of the open interest would doubtless reveal a high proportion of spreads. The open interest typically declines sharply each January.

When an individual makes some money trading commodities his first objective is to spread it into the next year. He takes offsetting positions in futures deliverable in the next tax year with the long positions more than six months forward, say short June and long August silver. If the price goes up, so that short side loss equals his previous gain, he realizes the loss by buying June and offsets his long August position with a short position in October. He now has no taxable income in the current year but a locked in position value that can be realized the next year. If the price stays up long enough the gain becomes long term, only half is taxable. If a long term doesn't work out the whole process can be repeated the next year, etc., until it does. Careful operators can carry gains forward for quite long periods.

Experienced speculators try to carry gains forward because of the ever present possibility of loss. Suppose that one year a trader in a marginal 50 percent bracket makes $20,000 of short term gain. He pays $10,360 in taxes. The next year he loses $20,000 but from this he can recover only $480 from savings in taxes on other income. He can carry the loss forward to be used in the third or fourth year when he again wins but in the meantime his trading is handicapped by a capital shortage. Better to pay taxes later than sooner.

Traders often lose money trying to extend gains from short-term to long-term. Tax considerations bias traders toward the long side. They result in trading that would not otherwise occur, some of which is not productive in rationalizing commodity price.

This tax structure does not make sense and should be modified *in the interest of preserving speculative capital*. The whole futures trading industry supports long term capital treatment. But such treatment is questionable. No futures contract is a long term capital asset in the sense that a farm or factory is a capital asset. Commodities aren't capital; they are goods. If this is the case, then losses on positions should not have capital treatment but should be permitted to be offset by income from other sources.

A change from capital asset to ordinary income treatment would still result in capital loss because of the graduated tax structure but the loss would be much less. A trade of the long term treatment on long positions held over six months for other income offset of losses would be a net gain for the industry, both of the amount of speculative capital and rationality of trading. This is a loophole, through which good speculative money is drained into government, that should be closed.
Index

Accounts
hedging, 64
trade vs. speculative, 61
Alfalfa meal, 189, 233
Alsike futures, 11
Animal by-product feed ingredients, 189, 233
Anticipatory hedging, regulation of, 329
Apple futures, 19
Barley futures, 11, 18, 23, 201, 233, 334
Basis
cash and price relationship in storage markets and, 151-66
defined, 152
hedging off purchases on weak, 181
importance of, to primary producers, 206-7
tables and charts of, as hedging tools, 184
Beans futures, 12-13
Beef futures, 18, 19, 24, 26, 134, 296
Bids, making, 34
Blair Stewart study, 256-58, 301
Bone meal, 189
Bran futures, 25
Brewers dried grains, 189, 233
British Pound futures, 25
Broiler futures, 18, 19, 21, 24, 201
market performance of, 303
mechanics of trade in, 41, 63
price relationships of, 145, 147
regulation of trade in, 333
Bucket shops, 89-93
Brokers, 52-53
Butter futures, 19

Canadian Dollar futures, 25
Candy manufacturers, 241-43

Capital
equity financing and pyramiding of, 135-36
speculation and allocation of, 279-82
speculation and management of, 267-69
tax reforms needed to preserve speculative, 361
Carrying charges
in cash and price relationships, 154-60
in nonseasonal markets, 164-66
Cash commodity trading, regulation of, 318-19
Cash forward contracts, 32-33, 218-19
Cash grain merchants, 192-93
Cash and futures price relationships, 148-72
artificial distortions in, 171-74
basis of, in storage markets, 151-66
hedging and, 148-51; see also Hedging
over space, 170-71
temporal price relationships in nonstorage markets, 168-70
Cash prices, tables of, as hedging tools, 184
Cash sales
ahead of harvest, 179-80
during marketing season, 180
Cash transactions, futures contracts as substitutes for, 107
Cattle futures, 4, 18, 19, 21, 24, 25, 41
beef futures, 19, 24, 26, 134, 296
equity financing of, 133-35, 137
market performance of, 296-97, 301, 308
mechanics of trade in, 108
price relationships of, 166-69
primary producers and, 204-6, 213-15
regulation of trade in, 333
speculation in, 145, 147, 249
Cereal grain futures, see Grain futures
Charges, see Carrying charges
Clearing corporations, 43-44
Clearing House, 35, 43-47

effects of speculation on, 250-51
Clover futures, 11
Cocoa futures, 4, 11, 12, 18, 19, 27, 109
market performance of, 301
mechanics of trade in, 58
as raw material, 241, 242, 249
speculation in, 274
Coconut oil futures, 18, 296
Coffee futures, 18, 27, 109
Commission houses (commission merchants), 64-60
agreements with customers by, 55-56
independence vs. advice from, in speculation, 278-79
market development and control of, 354
market development and operation of, 357-61
operational objectives of, 59-60
services provided by, 56-59
types of, 54-55
Commissions, costs of, 356-57

Commodities
in production, speculation in, 145
See also Stored commodities; Traded commodities; and specific commodities futures

Commodity advisors, 344
Commodity Exchange Act (1936), 314-15
1968 amendments to, 315
Commodity Futures Trading Act (1974), 315-18
Compensation of RRs, 359
Competition
between scalpers and pit traders, 53-54
workings of, 95-99
Competitive markets, 95-106
regulation of, 104-6
Contingent orders, 63
Contract terms, 36-40, 350-52
Contracts, see Futures contracts
Copper futures, 18, 25, 27
Copra, 233
Corn futures (and by-products), 12, 18, 23-25, 356
anatomy of January 27, 1967, market of, 109-19
development of trade in, 73-76
equity financing of, 133-37
exporters and, 198
hedging in, 179, 180, 182, 183, 185
ingredient merchants and, 189
interior merchants and, 188
market performance of, 296, 303
mechanics of trade in, 32, 40-43, 64, 64, 66
price relationships of, 153-55, 159-61
primary producers and, 201, 206-13, 219
as raw material, 233, 234, 238-41
regulation of trade in, 329-31, 334, 335, 341-42
risk shifting in, 107-8, 119-26
speculation in, 145, 249, 250, 256-57, 270-71, 274, 277, 279, 284
terminal elevators and, 197
Corn wet millers, 238-43
Costs, overhead, 354-57
Cotton futures, 18, 22, 24, 26, 109, 249, 348-49
development of trade in, 77-78
manipulation and regulation of, 326
market performance of, 296
regulation of trade in, 313, 319, 334
Cottonseed futures (and by-products), 11, 19, 23, 201, 233, 238, 293, 331, 334, 350
Country elevators, hedging by, 178-86
Cross hedging
by feed manufacturers, 236
regulation of, 331-32
Crude oil futures, 18
Currencies, 18, 25
Customers, 60-68
commission houses' agreements with, 55-56
getting to be, 61-62
kinds of orders placed by, 62-64
margin requirements for, 64-68
number and identity of, 60-61
selection, control and training of, 359-60
Delivery
contracts settled by, 41
defered, 32
delivery months, 39-41
in cash and price relationships, 152-54
trading stopped in, 39-40
delivery points, regulation of, 339-42
Deutschemark futures, 25
Direct hedging by feed manufacturers, 235
Discretionary orders (T.Y.T. orders; Not Held orders), 63-64
Disputes, settlement of, on exchanges, 17-18
Dual trading, regulation of, 342-44
Dutch Guilder futures, 25
Egg futures, 18, 21, 23, 25, 100, 203
development of trade in, 78-80
equity financing of, 133
market development of, 348, 352
market performance of, 296
mechanics of trade in, 41, 46
price relationships of, 166, 167
regulation of trade in, 334
risk shifting in, 108
speculation in, 145, 147
Equity financing, 130-37
attraction of speculators to, 136-37
process of, 131-35
pyramiding of capital and, 135-36
Exchanges, 9-18
defined, 10
development of, 10-12
financing of, 15
foreign, 12-13
Exchanges (Cont.)
governance of, 14–15
market development and, 350–54
membership of, 15–17
objectives of, 13–14
separateness of, 13
settlement of disputes on, 17–18
See also Volume of trading
Exporters, 197–99

Failure of markets, 348–50
Federal guaranteed Mortgages futures (GNMA), 18
Feed manufacturers, 233–38
Feed futures, see specific commodity futures used in feed manufacturing; for example: Corn futures
Fiber futures, 18
See also Cotton futures; Wool futures
Financial instruments
of equity financing, 130–31
See also Futures contracts
Financing
of exchanges, 15
of risk shifting, 291–97
See also Equity financing
Fish oil, 19
Fishmeal, 189, 201, 233
Flax futures, 11
Flaxseed futures, 12, 18, 201, 334
Floor traders, 51–52
Flour millers, 222–27
Foods futures, 18; see also specific foods futures
Forecasting
market performance and, 303–10
speculation and, 255, 269–74
Foreign exchanges, 12–13
Forest products futures, 18, 19, 24, 25, 137
Forward contracts
cash, 32–33, 218–19
historical development of, 75–77, 85, 91–92
French Franc futures, 25
Frozen shrimp futures, 19, 23
Fundamental approach to speculation, 275–78
Futures contracts, 31–33
settlements of, 41–47
as standardized agreements, 10
as substitutes for cash transactions, 107
terms of, 36–40, 350–52
See also Forward contracts
Futures trading
dynamics of, 22–30
interest in, 3–7
process involved in, 33–35; see also specific aspects of trading; for example: Commission houses; Futures contracts

Gold futures, 18, 19, 25, 247, 317
Government control, see Regulation
Grain futures, 4, 11, 18–19
cash grain merchants and, 192–93
exporters and, 198–99
hedging in, 176–79, 181–83
interior merchants buying, 187
market development of, 349
mechanics of trade in, 36, 37, 39, 46
price relationships of, 152–53
primary producers and, 201, 203
regulation of trade in, 313–14, 334–36, 341
terminal elevators and, 195–96
See also specific grains futures
Grain Futures Act (1922), 313–14
Growing crops, establishing price of, 207–11

Ham futures, 18, 19, 23
Hayseed futures, 11
Heating oil futures, 18, 19
Hedging
cash and price relationships and, 148–51
on corn futures market (Jan. 27, 1967), 110–11
by country elevators, 178–86
defined, 244, 328–29
details on, 175–78
by feed manufacturers, 235–38
markets as risk-shifting mediums and, 292–93; see also Risk shifting
open interest and, 119–29
regulation of, 328–33
speculation and, 254–55
tools for, 184
Hedging accounts, margin requirements for, 64
Hedging exemptions, 329
Hide futures, 11, 19
Historical development, 71–94
of bucket shops, 89–93
of corn and wheat futures trading, 73–76, 85, 91–92
of cotton futures trading, 77–78
of egg futures trading, 78–80
of regulation, 312–18
of soybean futures trading, 80–83
of speculation, 83–89
Hog futures, 18, 21, 25, 109
market performance of, 296, 297
price relationships of, 167
primary producers and, 203, 206, 215–17
regulation of trade in, 331, 333
speculation in, 145, 147
Industrial fuel oil futures, 18, 19
Information
generation of, 101–4
risk shifting and position, 108–9
Ingredient merchants, 189–92
Integrated merchants, 199–200
Interim price variations, market performance and, 300–3
Interior merchants, 186–89
Japanese Yen futures, 25
Judgment, speculative, 143-44
Lard futures, 19, 24, 238
Large speculators, regulation of position size of, 337-38
Later performance, contracts calling for, 31-32
Limit moves, 38-39
Limit orders, 62
Linsed meal, 19, 233
Livestock futures (and by-products), 18, 19, 21, 201, 203, 217-18, 340
See also specific types of livestock
"Long" records, as hedging tools, 184
Lumber futures, 25
Manipulation, regulation of, 321-28
Margin requirements
clearing house, 45
commission houses, 64-68
regulation of, 319-21
Market development, 347-61
exchanges and, 350-54
market failures and, 348-50
operation of commission houses and, 357-61
overhead costs and, 354-57
Market orders, 62
Market performance, 289-310
forecasting, 303-10
price variability and, 297-303
in risk-shifting financing, 291-97
Marketing, plans for, of primary producers, 205-6
Markets
failure of, 348-50
forecasting ability of, 255
function of, 7
nonseasonal, 164-66
nonstorage, 166-70
as risk-shifting mediums, 292-93
specific uses of, by primary producers, 207-18
storage, 151-66
See also Competitive markets; Volume of trading
Meatscraps, 19
Membership of exchanges, 15-17
Merchandizers, 187
Merchants, see specific types of merchants
Mercury futures, 27
Metal futures, 11, 18, 109; see also specific types of metal
Mexican Peso futures, 25
Middlings futures, 24, 26
Millers
corn wet, 238-41
flour, 22-27
Nonseasonal markets, carrying charges in, 164-66
Nonstorage markets, temporal price relationships in, 166-70
Normal backwardation, theory of, 293-94
Not Held orders (T.Y.T. orders; discretionary orders), 63-64
Oats futures, 12, 18, 19, 23-25, 85, 233
primary producers of, 201, 212
regulation of trade in, 334, 340
risk shifting in, 108
speculation in, 256-57
Observers, function of, 35
Offers, how offers are made, 34
Oilseed futures (and by-products), 4, 18, 189, 201, 233
One price principle, 152
One time traders, speculation by, 261
Onion futures, 19, 32, 116, 142, 294-95, 298, 300-1
Open contracts, defined, 42
Open interest, 42-43
hedging and, 119-29
risk shifting and, 108-9
Open orders, 63-64
Opposite (offsetting), transactions, contracts settled by, 41-42
Orange juice futures, 18, 19, 26, 109, 137, 249, 258
equity financing of, 137
market performance of, 296
mechanics of trade in, 37-38
primary producers and, 201
speculation in, 147
Orders
types of, 50, 52, 62-64
See also Spreads
Out trades, defined, 44
Overhead costs, 354-57
Palladium futures, 18, 19, 26, 301
Palm oil futures, 18, 296
Partial hedging, regulation of, 300-31
Peanuts, 19, 201, 233
Perfect competition, workings of, 98-99
Permissible price changes, contract terms and, 37-38
Petroleum futures, 18, 19, 26, 247
Pit, described, 33-34
Pit traders, 49-51, 53-54
Plantinum futures, 18, 19, 26, 166
Plywood futures, 18, 19, 24, 137
Pool operators, 344
Pork bellies futures, 9-10, 18, 19, 23, 25, 100
market development of, 348
market performance of, 293, 296, 301
mechanics of trade in, 41, 46, 52, 63
price relationships of, 153, 166
regulation of trade in, 318-19
risk shifting in, 108, 127-29
speculation in, 249, 258, 271
Position information, risk shifting and, 108-9
Position size, regulation of, 333-39
Potato futures, 18, 19, 21, 25, 26, 201, 249
  failure of market of, 348
  market performance of, 296
  regulation of trade in, 334
  risk shifting in, 109, 116
Price relationships
  effects of changes in, 175
  See also Cash and price relationships
Prices
  communication of, 35
  contract terms and permissible price changes, 37–38
  effects of changes in levels of, 175
  of growing crops, establishing, 207–11
  market performance and variability in, 297–303
  of sold crops, delaying, 212–13
  of stored commodities, establishing, 211–12
  tables of cash, as hedging tools, 184
Pricing
  hedging to defer, 181–82
  as key to competition, 98
  See also Speculation
Primary producers, 201–20
  importance of basis to, 206–7
  marketing plans for, 205–6
  pitfalls common to, 219–20
  purposes of trading for, 202–5
  specific uses of markets by, 207–18
Procurement by feed manufacturers, 235
Producers, see Primary producers
Promotion, market development through, 352–54
Propane futures, 18, 26
Provisions, 11, 85; see also specific pork products
Public, the, protection of, 344–45
Pure competition, 98–100
Random walk school, opposed, 275–76
Rapeseed futures, 19
Rationing and supply, 141–42
Raw materials users, 221–45
  candy manufacturers as, 241–43
  corn wet millers as, 258–41
  feed manufacturers as, 233–38
  flour millers as, 222–27
  generalizations on, 243–45
  regulation of raw materials, 332–33
  soybean processors, 227–33
Reasonableness in margin requirements, 67
Records, long and short, as hedging tools, 184
Registered representatives (RRs), 58–59, 344, 358–59
Regular traders, speculation by, 261–63
Regulation, 311–46
  competition and, 96
  of competitive markets, 104–6
  of delivery points, 339–42
  of dual trading, 342–44
  of hedging, 328–33
  historical development of, 312–18
  of manipulation, 321–28
  of market operations, 318–21
  philosophy of, 345–46
  of position size, 333–39
  to protect the public, 344–45
Reserves, speculation and maintenance of, 142–43
Resting orders
  brokers and, 52
  pit traders’ handling of, 50
Ring, described, 34
Risk shifting, 107–29
  on corn futures market (Jan. 27, 1967), 109–19
  financing of, 291–97
  markets as risk-shifting mediums, 292–93
  open interest, position information and, 108–9
  See also Hedging
RRs (registered representatives), 58–59, 344, 358–59
Rubber futures, 11, 12, 27, 109
Rye futures, 12, 19, 23–25, 85, 201, 256–57, 334
Sales, see Cash sales
Scale orders, 63
Scalpers, 47–48, 53–54
Scrap iron futures, 19
Seasonal prices, market performance and, 299–300
Selective hedging by feed manufacturers, 236–38
Services provided by commission houses, 56–59
Short records, as hedging tools, 184
Silver futures, 18, 19, 24, 27, 164–66, 258, 274, 301, 317, 332
Silver coin futures, 18, 19, 25, 26, 58, 317
Sold crops, delaying prices on, 212–13
Sorghum futures, 18, 24–25, 129, 201, 233
Soybean futures (and by-products), 12, 18, 19, 21, 22, 24–25, 238
devolution of trade in, 80–83
hedging in, 179
ingredient merchants and, 189–91
market development of, 350, 352, 356
market performance in, 293, 296, 303
mechanics of trade in, 35–37, 41, 52, 58, 63
price relationships in, 161, 164
primary producers and, 201, 212, 213
processors of, 227–33
as raw materials, 233, 234, 237
regulation of trade in, 319, 330–32, 334, 335, 339, 340
risk shifting in, 108, 116
speculation in, 142, 249, 274, 279
terminal elevators and, 197
Space, cash and price relationships over, 170–71
Speculation, 137–47, 246–88
for commodities in production, 145
commodity futures as medium for, 247–50
consequences of, 145–47
controversy over, 138–41
hedging and, 151; see also Hedging
historical development of, 83–89
Speculation (Cont.)
how to speculate, 263-65
results of, 255-63
rules of the game for, 250-55
on stored commodities, 141-44
Speculative accounts, trade accounts vs., 61
Speculators
attraction of, to equity financing, 136-37
on corn futures market (Jan. 27, 1967), 110-11
regulation of position size of large, 337-38
Spreads, 65
basis and, 159-60
regulation of, 332-33
tables of, as hedging tools, 184
Standardized contracts, 33
Steer futures, see Cattle futures
Stewart, Blair, study by, 256-58, 301
Stop limit orders, 62-63
Stop loss orders
brokers and, 52
pit traders’ handling of, 50
Stop orders, 62
Storage hedges, 179
Storage markets, 151-66
Stored commodities
establishing price of, 211-12
speculation in, 141-44
Sugar futures, 12, 18, 27, 109, 241, 242, 301
Sunflower seeds (and by-products), 19, 201, 271
Swiss Franc futures, 18, 25
Taxes, 360-61
Technical approach to speculation, 275-78
Temporal price relationships in nonstorage markets, 166-70
Terminal elevators, 193-97
Texas hedge, 186
Textile yarn futures, 12; see also Cotton futures;
Wool futures
Time, cash and price relationships over, 154-60
Time contracts, historical development of, 74, 76, 79-80
Time orders, 63
Timothy futures, 11

'To arrive' contracts, historical development of, 75
Tomato paste futures, 23
Trade accounts, speculative vs., 61
Traded commodities, 18-22
common characteristics of, 19-22
See also Volume of trading and specific commodities futures
Traders, types of, 47-54
Trading with the flow orders, 49
Trading with the market, 49, 51
Trailing stop orders, 63
Training
of customers, 359-60
of RRs, 358-59
Turkey futures, 18, 349
T.Y.T. orders (Not Held orders; discretionary orders), 63-64

U.S. Treasury bill futures, 18
Uranium futures, 247

Volume of trading
on all markets combined (1961-75), 28-29
in cereal grains (1884-1974), 23
market performance and, 295-97
U.S. annual (1961-75), 24-27

Warehousemen, see specific types of warehousemen
Wheat futures, 4, 10, 12, 18, 19, 23-25, 233
developing of trade in, 73-76, 85, 91-92
flour millers and, 222-27
market performance of, 296, 308
mechanics of trade in, 52, 64
price relationships of, 153
primary producers of, 201, 212
regulation of trade in, 322-24, 329-31, 334, 340, 341
risk shifting in, 108, 116
speculation in, 249, 256-57, 279, 282
terminal elevators and, 196, 197
wheat millfeeds, 19, 23, 189, 233, 331
Wool futures, 18, 23, 26, 109
2. Futures trading is a remarkably close approximation to the classical economic concept of pure competition. The established, high volume markets, nearly meet the tests for perfect markets. They are not planned with these concepts in mind, but evolved into this form out of the crucible of market forces.

3. The markets are mainly about the pricing of commodities, which is speculative. Hedging, in its standard context, is often a nonsense term. Equal and opposite is still speculative. In addition, a high proportion of "hedged" positions are taken with a "view of the market."

4. Futures markets are investment media. They are financial markets, and futures contracts are financial instruments. The markets generate equity capital from the speculators and, as furnishers of capital, the speculators play a significant role in the direction of economic processes.

5. Much of the regulation of markets is misdirected. Much of the alleged manipulation and price distortion hasn't really happened. When prices have been distorted, the guilt has usually been misplaced. Market dominance is more apt to be accomplished by hedgers than by speculators, and regulation has generally restricted speculation and decreased competition. The markets are relatively free of monopolistic influences but a preoccupation with price distortion has hampered market growth and development.

6. The futures markets that work, work well indeed. These are the visible ones. But, rather more markets do not work than do. There is need for much more speculation of a higher quality than now exists.

This book is a tribute to the people who trade in commodities, both commercial interests and speculators. They are a fascinating group of sportsmen who try to run a good game and who play to win. This is the story of their activities, but in a broader sense, this book is a tribute to a competitive economic system that is not only highly productive of goods and services, but more importantly, contributes so much to liberty and the excitement of a life style.
ABOUT THE AUTHOR

Dr. THOMAS A. HIERONYMUS is among the world's leading authorities in the areas of commodity futures trading and price analysis. He has been a Professor of Agricultural Economics at the University of Illinois since 1949 and has written extensively for both academic and business consumption. His services as an expert are in continuous demand by government agencies, commodity exchanges and commercial interests.

His activities, concurrent with University duties, include cooperative research and consultative work with the Economic Research Service, Commodity Stabilization Service, and the Foreign Agricultural Service of the U.S. Dept. of Agriculture. He has served as chairman of the Educational Advisory Committee of the Chicago Board of Trade and on the Education Committee of the Chicago Mercantile Exchange. He has participated in numerous seminars and symposia for these exchanges as well as for the Minneapolis Grain Exchange and the New York Coffee and Sugar Exchange.

Dr. Hieronymus's stature in the commercial world also is evidenced by his popularity as a speaker. He has made repeated appearances before the Commodity Clubs of New York and Chicago, the American Feed Manufacturers Association, American Soybean Association, National Association of Margarine Manufacturers, American Farm Bureau Federation, American Meat Institute, and numerous other national, state and regional commodity associations. Most of the papers of these presentations have been published in national publications. In addition to his courses on futures trading, marketing and prices at the University of Illinois, he has taught adult courses to groups of farmers, merchants, warehousemen, processors and bankers.

From his consulting experience with processors, merchants and commission houses, he gained the first hand knowledge that enabled him to tell the story of the markets, as they are, warts and all, with clarity and good humor.

ABOUT THE PUBLISHERS

It is appropriate that this book by a leading authority on futures markets should be published by the world's leading publisher of commodity books and services. Commodity Research Bureau, Inc., has been serving the commodity trades, commission houses and their customers since 1934. Publications include the famed COMMODITY YEAR BOOK, published annually, MODERN COMMODITY FUTURES TRADING, FORECASTING COMMODITY PRICES, FASTEST GAME IN TOWN, COMMODITY CHART SERVICE, FUTURES MARKET SERVICE, DAILY COMMODITY COMPUTER TREND ANALYZER, and OTHER SPECIALIZED COMMODITY PUBLICATIONS. Complete information is available from the publishers on request.