

Introduction to **WORLD OF COMMODITIES**





Introduction to Commodities

Commodity trading brings a basket full of diverse avenues for investment, away from the traditional avenues of Equity, Bonds and Real Estate. Based on the historical data, adding commodities exposure to your existing portfolio helps you increase the returns while lowering the risk.

Things you need to know while trading in Commodities

- Commodity Derivatives in India are primarily traded on three exchanges namely NSE, MCX & NCDEX
- Both options and futures are available on various commodities
- MCX is primarily known for its trading in Non-Agricultural commodities and NCDEX is the flag bearer of Agricultural commodities
- Commodities are primarily divided in to Precious Metals, Industrial Metals, Energy and Agricultural commodities
- Recently various commodity indices were launched for those who want to invest in commodities market at sectorial level
- Most of commodities except energy commodities are settled by physical delivery on expiry of contract
- Motilal Oswal offers dedicated and high level of services of accessing commodities.

PRECIOUS METALS

CONTRACT SPECIFICATION							
BULLIONS METAL	GOLD	GOLD MINI	GOLD GUINEA	GOLD PETAL	SILVER	SILVER MINI	SILVER MICRO
Lot Size	1KG	100GMS	8GM	1GM	30 KG	5 KG	1 KG
P&L/Lot (₹1 change)	100	10	8	1	30	5	1
Traded Contract	Feb, April, June, Aug, Oct, Dec	Jan to Dec (Every Month)			Mar, May, July, Sept, Dec	Feb, April, June, Aug, Nov	
Options Availability	✓	✓	✗	✗	✓	✓	✗

*Source - Multi Commodity Exchange

- o Gold and silver are considered as a safe haven asset, and are benefited during times of uncertainty and risk
- o Both are non interest paying assets and are considered as hedge against inflation
- o Silver being precious metal is also considered an Industrial metal and hence movement in base metals also impact the price movement in Silver
- o Broader economic environment, inflation, interest rates and liquidity drives the prices of precious metals
- o Along with uncertainties, economic data points also give a direction to the metal prices
- o India and China are biggest consumers of gold, hence Demand – Supply related data becomes important to focus
- o As both precious metals are imported any movement in Rupee and any changes in import duty shall also impact the price movement of both Gold and Silver.



CONTRACT SPECIFICATION

TRADED CONTRACT	CRUDE	NATURAL GAS
Lot Size	100 Barrels	1250 mmbtu
Multiplier	100	1250
Traded Contract	Jan To Dec	Jan To Dec
Options Availability	✓	✓

*Source - Multi Commodity Exchange

Key Fundamentals:

- o Crude Oil, Natural Gas, Coal, Electricity and other fuels are part of energy basket
- o Energy consumption is the back bone of any economy and the ups and downs of economic growth impact demand for these commodities
- o Supply side fundamentals are the biggest drivers of price over short term
- o Organization of Petroleum Exporting Countries (OPEC) along with Russia and USA controls the supply of crude across the world
- o Shipping & logistics along with geo-politics also impacts the price movement over short term
- o Inventories of USA and other developed countries is also one factor to watch out. USA released their stocks of crude products every Wednesday which moves markets

Crude oil demand is closely correlated to global economic growth. Hence, economic data from major consumers like the US, Europe and China play a major role in determining prices. The OPEC supplies nearly 40% of world oil; hence, its production is very closely watched. Data from the US is closely watched as it has turned largest producer of shale oil.

Base Metals

CONTRACT SPECIFICATION					
TRADED CONTRACT	COPPER	NICKEL	ZINC	LEAD	ALUMINIUM
LOT SIZE(REGULAR)	2.5MT	1.5MT	5MT	5MT	5MT
P&L/Lot (₹1 change)	2500	1500	5000	5000	5000
TRADED CONTRACT	JAN TO DEC	JAN TO DEC	JAN TO DEC	JAN TO DEC	JAN TO DEC
EXPIRY	LAST WORKING DAY OF THE MONTH AT 5:00 PM				
Options Availability	✓	✓	✓	✗	✗

*Source - Multi Commodity Exchange

Key Fundamentals:

- Copper has been considered the economic activity barometer; it is widely used in Infrastructure, consumer durables and automobile industries, and the trend in copper depicts how economies are faring
- Nickel is primarily used in making stainless steel which has varied uses also Electric car batteries are made of Nickel which will attract strong demand in future
- Aluminium is refined from one of the widely available minerals called bauxite. This metal has the largest quantity of inventory and has uses in a wide array of industries
- Lead is one of the smaller metals and is widely used in the manufacturing of batteries. The automobile industry plays a key role in the price discovery of this metal
- Zinc is widely used for galvanizing, which protects the steel from external elements, galvanized steel is used in the construction and automobile industries
- LME inventories are released every day and one on the common factor moving the prices. Any sharp drop of rise in inventories have an impact on prices. Shallow inventories indicate higher demand lending support to prices, while higher inventories indicate lower offtake and negative for prices
- Globally, metals move largely in Sync with how the Chinese economy fares or how the US dollar reacts and China is not only the largest producer but also the largest consumer of most industrial metals, and as a hub of global manufacturing activity, it's economy plays a critical role in sentiments of metal markets
- Global macro-economic conditions, especially construction, housing and automobile industry, play an important role. Therefore, the numbers relating to these industries have high importance to these metals. Hence traders should keep a close eye on these sectors.

Economic Data Point Impacting Commodities

Event	Definition	Country	Frequency	Importance	Impact
GDP	Gross Domestic Product measures the overall growth of the economy	US	Quarterly	High	Base metal, Gold, Crude
		China			
		Euro zone			
		UK			
		India			
Non-Farm payrolls	Measures the change in number of people employed during previous month, excluding the farming industry	US	Monthly (First Friday)	High	Base metal, Gold, Crude
Unemployment rate	Measures the percentage of total work force that is unemployed and actively seeking employment during previous month	US	Monthly (First Friday)	High	Base metal, Gold
Inflation	Measures the change in price of goods and services from perspective of the consumer	US,	Monthly	High	Base metal, Gold, Crude
		China,			
		Euro zone,			
		UK,			
		India			
Crude Monthly Report	OPEC and IEA monthly report covers major issues affecting world oil market and outlook for crudeoil market in coming years	US	Monthly; (Source: International Energy Agency & Organization of Petroleum Exporting Countries)	High	Crude
Crude Inventory Data (EIA/API)	The Energy Information Adminstration (EIA) crudeoil Inventories measures weekly change in number of barrels of commercial crudeoil held by U.S. firms.	US	Weekly (Every Wednesday)	High	Crude
Natural Gas Inventory Data	The Energy Information Adminstration (EIA) Natural Gas storage report measures change in number of cubic feet of natural gas held in underground storage	US	Weekly (Every Thursday)	High	Natural Gas

Economic Data Point Impacting Commodities

Event	Definition	Country	Frequency	Importance	Impact
Rig count	Showcases the number of active drilling rigs. The active rig count act as a leading indicator of demand for oil products	US	Weekly (Every Friday)	High	Crude
Service & Manufacturing PMI	Measures the activity level of purchasing managers in services & Manufacturing sector	US	Monthly	High	Base metal, Gold, Crude
		China			
		Euro zone			
		UK			
		India			
Imports & Export	Import/Export data measures any good or service brought/sold from one country to another country	US	Monthly	High	Base metal, Gold
		China			
		EU			
		UK			
		India			
Industrial Production	Measures change in total value of output produced by manufactures, mines and utilities	US	Monthly	High	Base metal, Gold, Crude
		China			
		Euro zone			
		UK			
		India			
New Home Sales	Measures annualized number of new single family homes that were sold during the previous month.	US	Monthly	High	Base metal, Gold,
LME Warehouse Stocks	Shanghai Future Exchange gives weekly update regarding base metals inventory change in its warehouse	US	Daily at 1.30 PM India time & 2.30 PM during day light saving	Low	Base metal
Shanghai Stocks	Shanghai Future Exchange gives weekly update regarding base metals inventory change in its warehouse	China	Weekly (Every Friday)	Low	Base metal
Automobile Sales	Shows number of vehicle sold in previous month, showcasing demand of Automobiles in the market	US	Monthly	Low	Base metal
		Euro zone		Low	
		India		Low	
		China		High	

CONTRACT SPECIFICATION

Commodity	Exchange	Price quotation	Lot size	P&L / lot (₹ 1 change)	Approx Margins%*
Mentha Oil	MCX	1 KG	360 KG	360	10
Turmeric	NCDEX	100 KG	5000 KG	50	10
Steel	NCDEX	1000 KG	10000 KG	10	15
Castor	NCDEX	100 KG	5000 KG	50	10
Castor Oil	NCDEX	10 KG	2000 KG	200	10
Cocudakl	NCDEX	100 KG	10000 KG	100	10
Dhaniya	NCDEX	100 KG	5000 KG	50	10
Guargum	NCDEX	100 KG	5000 KG	50	10
Guarseed	NCDEX	100 KG	5000 KG	50	10
Jeeraunjha	NCDEX	100 KG	3000 KG	30	10
Chana**	NCDEX	100 KG	10000 KG	100	-
Soybean**	NCDEX	100 KG	5000 KG	50	-
Wheat**	NCDEX	10 KG	10000 KG	100	-
CPO**	NCDEX	10 KG	10000 KG	1000	-
Refined Soy Oil**	NCDEX	10 KG	5000 KG	500	-

*Margin are subject to change as per exchange guidelines

**Agri Commodities are not currently trading on exchange

*Source - Multi Commodity Exchange

*Source - National Commodity & Derivatives Exchange Limited

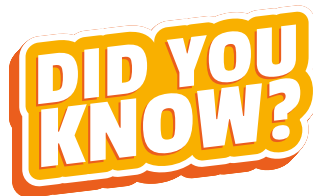
Introduction to **Commodity Options:** (BIG Opportunity like Equity Options)

- o In an options transaction, the purchaser pays the seller (the writer of the option), an amount for the right to buy (in case of “call” options) or for the right to sell (in case of “put” options). This amount is known as the “**Option Premium**”.
- o **Premium is the cost of the option paid by the buyer to the seller.** Since the buyer is paying the premium to the seller, he has the **right to exercise the option** when it is favourable to him but no obligation to do so.

Rights and obligations summarized			
Party	Long (Buy)	Counterparty	Short (Sell)
Call Buyer	Right to Buy	Call Seller	Obligation to Sell to call buyer
Put Buyer	Right to Sell	Put Seller	Obligation to Buy from put buyer

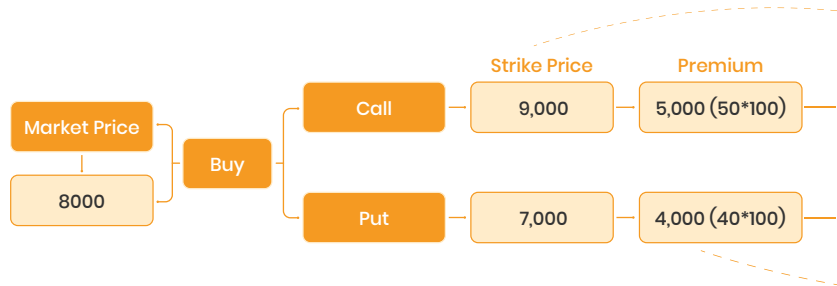
Risk & Reward in Commodity Options		
Position	Maximum Risk	Maximum Reward
Long Call	Limited to premium	Unlimited
Short Call	Unlimited	Limited to premium
Long Put	Limited to premium	Unlimited
Short Put	Unlimited	Limited to premium

Commodity Options On Futures



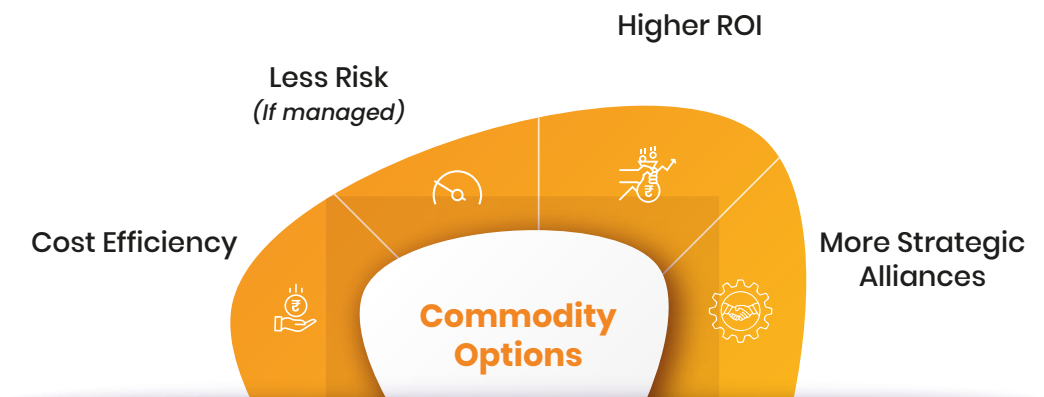
- o Commodity options in India devolve into Commodity Futures. That means, buyers of commodity options would get a right to have a position in underlying commodity futures on expiry.
- o Therefore, the underlying for a commodity options contract is a commodity futures contract of a specified month traded on the corresponding exchange

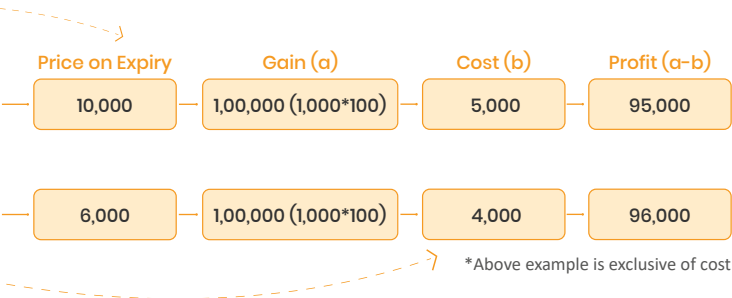
Commodity Options Scenario Analysis



Advantages of Options Over Futures

- o **Less Risk:** Long option positions are less risky than futures and short option positions
- o **Less Expensive:** Generally, option premiums are smaller than futures margins
- o **More Leverage:** A large array of premiums available to options traders
- o **Higher ROI:** Handsome returns on investment in options buy as compared to futures
- o **Cost Efficiency:** Trading cost of option is much lesser than trading in futures





Trading Cost Comparison

Crude Oil Futures

CONTRACT SPECIFICATION	
Contract Size	1 Lot
Buy Price	8000
Sell Price	8010
Quantity	1 Lot
Total Turnover (Buy+Sell)	16,01,000
Turnover Charges (0.0028%)	44.83
SEBI TAX (0.00005%)	0.80
GST (18%)	8.21
Stamp Duty (0.002%)	16.00
CTT (0.01% - Sell Side)	80.10
Total Cost	149.94

Crude Oil Options

CRUDE OIL Option Contract Trading Cost	
Strike Price	8000
Buy Price	100
Sell Price	120
Quantity	1 Lot
Total Turnover (Buy+Sell)	22,000
Turnover Charges (0.05%)	11.00
SEBI TAX (0.00005%)	0.02
GST (18%)	1.98
Stamp Duty (0.003%)	0.30
CTT (0.01% - Sell Side)	1.20
Total Cost	14.51

** Trading cost may change as per exchange & regulatory guidelines

*Source - Multi Commodity Exchange

*Brokerage to be added as per actuals



➤ Commodity Indices:

- o Portfolio diversification (low correlation to stocks)
- o Access to a basket of commodities
- o No delivery, settled in cash on expiry
- o No need to select one commodity but benefit from broader trend
- o Lower risk, as a basket is less risky than any individual commodity
- o Asset allocation, strategies and long term investing
- o Smaller lot size reduces risk and lower capital requirement.

CONTRACT SPECIFICATION			
Specification/contract	MCX BULDEX	MCX METLDEX	MCX ENRGDEX
Indicative Price	15,000	21,000	8,000
Lot Value	7,50,000	11,00,000	10,00,000
Multiplier	50	50	125
Traded Contract	JAN TO DEC	JAN TO DEC	JAN TO DEC

*Source - Multi Commodity Exchange

> Weightages

Index	Constituents	Weights 2022
MCX BULDEX	Gold	63.70%
	Silver	36.30%
MCX METLDEX	Copper	39.74%
	Nickel	25.21%
	Zinc	14.34%
	Aluminium	16.12%
	Lead	4.59%
MCX ENRGDEX	Crude Oil	51.07%
	Natural Gas	48.93%

*Source - Multi Commodity Exchange

*Above weightages are subject to change annually





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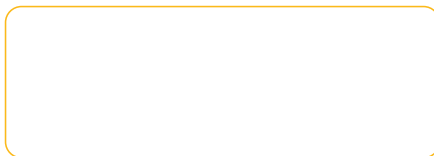
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