

Back to future(s)?

Kaushik Basu calls for clean line on futures trading in agri-commodities

The Congress has been always ambivalent about futures trading in agricultural commodities. Unlike the BJP and CPI(M), which have openly come out against futures trading in the commodity market, the Congress has not taken an unequivocal stand. It is prone to succumbing to pressures whenever things go out of hand. Trading in sugar futures was suspended till June 2010 when prices began to rise in May last year. Earlier, futures in *urad* and *tur* were suspended in January 2007.

Under commodity futures trading, participants trade on futures contracts to hedge their risks against adverse price movements. A futures contract is an agreement between two parties to buy and sell a specified quantity of an asset at a future date at an agreed price.

The Congress ambivalence may be partly due to the fact that agriculture and food minister Sharad Pawar, a favourite punching bag of the Congress, is a known votary of futures trading. The ambivalence is reflected in the government line articulated in Parliament, which does not give a clean chit to futures trading, but adds that agri-commodities in which there are no futures trading have also shown sharp acceleration in price rise.

Now, chief economic advisor to the finance ministry, Kaushik Basu, the new star on the UPA's economic policy-making firmament, has taken an unequivocal line and articulated the need for a clear policy on this sensitive issue. Recently, he said futures trading in commodities allows efficient price discovery and will not fuel inflation.

"Rice, *urad* and *tur* are other commodities in which futures trading have been suspended, but the prices of these commodities



Basu: calling for a clear policy

rose subsequently. You cannot link the two (commodity futures and inflation)... The reason why I am personally in favour of allowing futures trade in commodities is because it is not going to make inflation worse," Basu said at a seminar.

The UPA had even set up a committee in 2007 to investigate if there was any link between rising prices and futures trading. The committee, led by Planning Commission member Abhijit Sen, had concluded, "...No strong conclusion can be drawn on whether introduction of futures trade is associated with decrease or increase in spot price volatility."

Subsequently, Planning Commission deputy chairman Montek Singh Ahluwalia had endorsed the committee's findings. "I don't support the notion that futures market creates inflation. We should not look at banning futures trading as this market plays an extremely important

role in price discovery. Banning futures trading will be contrary to real economic rationale," Ahluwalia had said. This stance was at variance with that of the Left parties that had demanded a blanket ban on futures trading in essential commodities, as it was inflationary. The Left was then propping up the UPA.

Experts say that the policy flip-flop has discouraged the development of a sound futures market in agri-commodities, which Basu felt was extremely important for many stakeholders to take a position to manage price risk. However, he added it should not be left unregulated as there are possibilities of people getting cheated. The oversight of the commodities market has been a matter of debate, with some experts arguing it should be regulated by the stock market watchdog SEBI.

Futures trading is regulated by the Forward Markets Commission, which is under the jurisdiction of the ministry of consumer affairs, food and public distribution. The Forward Contracts (Regulation) Act, 1952 does not prohibit futures trading in any commodity. At present, 106 commodities are notified for forward trading.

With inflation expected to come down by April following good agricultural production, it remains to be seen whether the UPA will pick up the courage to resolve this policy dilemma. Basu, on his part, feels that the government's storage and release mechanism of foodgrains needs to be improved to manage prices. "We need to give much more thought on foodgrains management to protect the most vulnerable section of the population... I think this mechanism can be improved by bringing the private sector into play. The government should not be the only agent that is trying to take this risk on its shoulders," he said.

He pointed out that from January, the government has been releasing foodgrains in smaller stocks and some of the downward pressure on food prices is probably due to this fact and this mechanism is managed better – but is still not good enough. That's where the private sector can come in.

♦ RAKESH JOSHI