

Commodity exchanges

Recent international experience

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Theoretical Rationale

- Stimulate market transparency and price discovery
- Make collusion harder on account of anonymity
- Moderate price volatility and bubbles
- More accurate price information to stakeholders

Commodity Exchanges in Developing Countries

- Early commodity exchanges Brazil and Argentina, Malaysia (palm oil)
- **1990s African wave** Kenya, Uganda (government/donor support), South Africa, Zambia, and Zimbabwe (private sector led)
- **Continued into the 2000s.** Malawi, Nigeria, and Ethiopia (donor support plus own revenue).
- **New wave.** Rwanda RCX (2013), Tanzania, Nigeria (Abuja)

The Puzzle

- Most failed or exist only on paper. For example, Kenya, Malawi, Nigeria, Uganda, Zambia (3)) and Zimbabwe. (Sitko and Jayne, 2012; Rashid, et al 2010; Tollens 2006; Robbins, 2011; Makhebi Kundu 2014)
- Only a few succeeded. Ethiopia, Malaysia, Thailand, and Brazil (PPP), China (Government; domestic market oriented), South Africa

Why have so many commodity exchanges failed?

- Despite international donor support (\$ 24 million for ECE, for example).
- Despite theoretical benefits and some empirical evidence of positive impacts.

Features of the exchanges

- Commodity exchanges either grow into heavily traded institutions or fail completely
- Small, thin markets. Only 2.7% of total marketed volume of maize, soybean and wheat is traded in the exchanges. Forty thousand tonnes in a year.
- Hence not financially sustainable. JSE agriculture trading division SAFEX US\$100 million /day, none of the rest attained this scale. Trade in ZAMACE \$78 mill over 4 years in ZAMACE. Malawi made US\$ 18,000 in year as revenue.

Features of the exchanges

- No floor trading in many exchanges . Around 68% of the US\$78 million trade (between 2007 and 2011) occurs bilaterally off-line and is reported to ZAMACE later (Sitko Jayne, 2012).
- Many are just MIS services (KACE, MACE), others WFP P4P (Uganda UCE, MACE, now ZAMACE) (Robbins, 2012)
- ECX considered successful but grain trading failed, legal restrictions mandate all commodity exports have to go through the exchange (e.g., coffee). Heavy handed approach, stocks of coffee confiscated.(Rashid, 2010)

Key observations (1)

- Some commodities are better candidates than others (maize, wheat, soybeans).
- Higher probability of success where wholesale markets absent but large trading volumes exist.
- Context influences outcomes - deeply entrenched relationships can have the opposite result of predicted outcomes.
 - anonymity breeds non-compliance and opportunistic behavior
 - the potential for conflict of interest among brokers; trade diversion to outside-Exchange transactions
 - more collusion rather than less the potential for market manipulation in a thinly traded market
 - the high fixed costs that are imposed on actors trading in a thin market.

Key observations (2) Other actors, other challenges

- the limited success in attracting *financial institutions'* *commitment* to commodity exchanges and poor link with financial markets.
- Where *heavy government intervention in price policy* exists, commodity exchanges tend to flounder.
- *Macroeconomic stability* in Zimbabwe, *Election violence* Kenya (2006)

Further,

- Expand the number and type of actors (limits to this)
- Third party quality and certification services (South Africa is apparent exception)

Policy implications

- Focus on the nuts and bolts of grain market development, market fundamentals rather than financing exchanges directly (information, credit, infrastructure).
- Decentralization of efforts (e.g, Malawi, earlier, Kenya) - take the market to the farmer

India is often used as an example.

Parallels, Contrasts and Lessons?

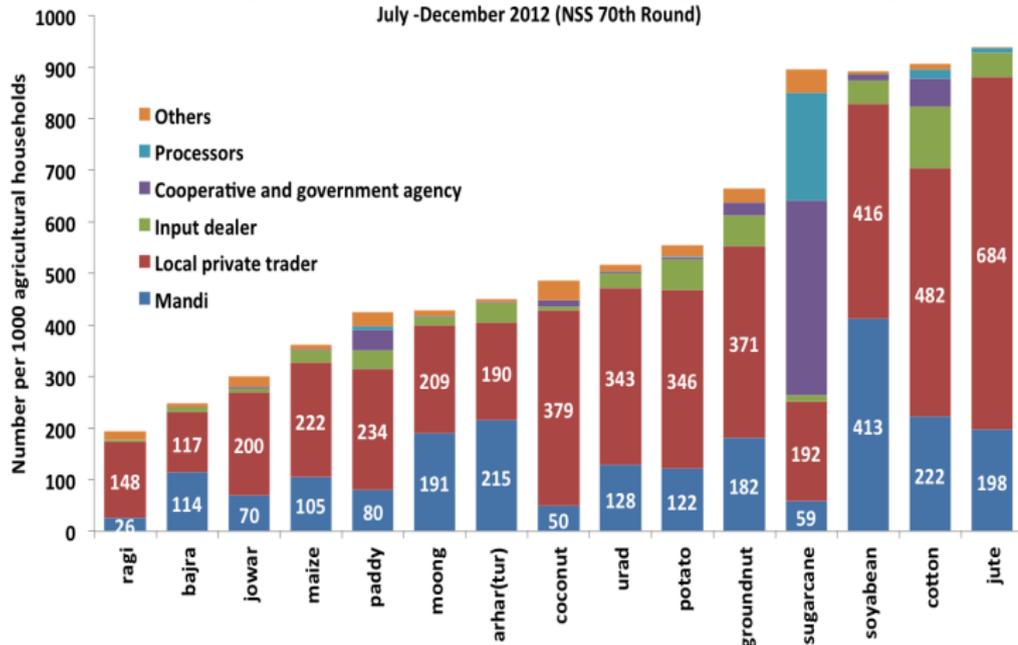
Contrasts

- Financially sustainable from the start; macroeconomic stability
- Unification links mandis - decentralized, but warehouse-based sales.
- But, entrenched system - brokers/ commission agents, etc., risk of trade exiting mandi
- Capacity and framework for farmers to get organized for marketing (arecanut)
- Credit plays a critical role.

Similarities

- Success in markets with large arrivals , simple quality parameters.
- Enforcement issues, trust based transactions.
- Mandi is not the most important interface for many commodities

Number per 1000 of agricultural households reporting sale for selected crops
July -December 2012 (NSS 70th Round)



Percentage distribution of quantity sold by agency for selected crops

July- December, 2012 (NSS, 70th Round)

