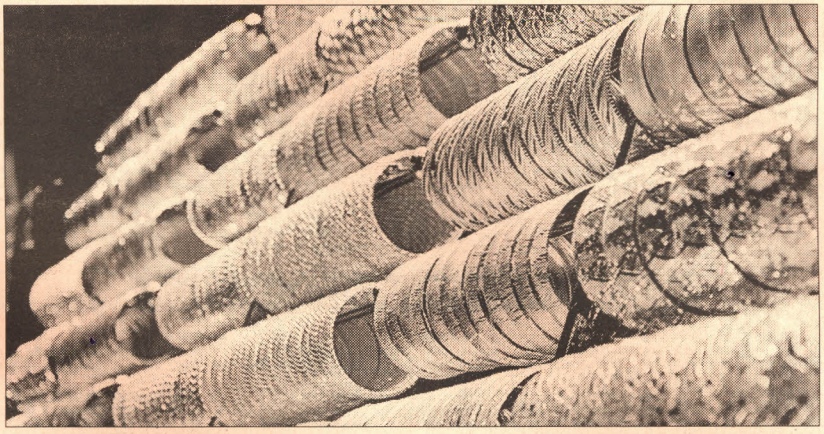
GOLD TRADE

MCX launches India's first commodity option product

Finance minister Jaitley says move a step towards formalisation of gold trade; NCDEX to start such trading in guarseed soon



FE BUREAU
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THE MULTI COMMODITY Exchange (MCX) introduced the country's first option product on Tuesday following recent policy changes, 14 years after India adopted modern derivatives trading in commodity futures in a big way.

Launching options trading in gold on the MCX platform on the day of Dhanteras, Union finance minister Arun Jaitley said allowing options trading was one of the steps towards formalising trade in the precious metal in a country where the bullion trade often done informally and therefore viewed with suspicion. "This marks a very important evolution in trading of gold itself. It hedges all risks by giving them (traders) the option of futures," Jaitley said.

The option contract, with gold (1 kg) futures as underlying, expiring on November 28, 2017 and January 29, 2018, for trading on MCX from Tuesday. NCDEX, the country's second-largest commodity exchange, has also got Sebi approval to start option in guarseed and will soon formally launch it. The primarily farm commodity bourse has already finalised contract specifications in guar option and started mock trading.

Earlier this year, regulator Sebi allowed the introduction of options, along with the existing futures contracts, to deepen the market. Options give the holder the right to buy or sell the underlying asset at expiration while a futures contract holder is obligated to buy or sell the underlying asset on a future date. The buyer of a commodity option pays a premium to the seller of the option for the right.

The Sebi move paved the way for a much wider basket of products and greater ability of farmers to hedge the risk of price fluctuations in their produce. Also, as market participants point out, the cost of trading in commodity options (both farm and non-farm items) will likely be only a fraction of that for trading in futures – less than a fourth in certain cases. Options could also lead to an enhancement of liquidity in the market, thus strengthening the price discovery process and reducing the trading costs. Since options carry limited downside risk, it could be a good tool for SMEs and farmers to hedge their commodity price exposures.

MCX chairman Saurabh Chandra said, "The introduction of options gives a strong impetus towards systematic development and transformation of commodity derivatives market in India, ushering in a new era in price risk management in response to stakeholder expectations." The exchange's managing director Mrugank Paranjape said options would "complement the existing array of commodity futures contracts and help in enriching the informational efficiency of the market's price discovery process".

Sebi formally notified the guidelines in June, allowing each exchange to start options trading in only one commodity initially upon meeting certain conditions (including the commodity has to be among the top five in terms of the exchange's turnover value of the previous one year).