

WHO'S WHO IN THE FUTURES MARKETS

The Commodity Exchange

A commodity exchange is an organization that formulates rules for the trading of commodity futures contracts, provides a place to trade and/or an electronic trading platform and supervises trading practices. Its members are people whose business is trading. The exchange establishes the terms of standardized contracts that are traded subject to Commodity Futures Exchange Commission (CFTC) approval. It also disseminates price and market information and provides the mechanics to guarantee contract settlement and delivery.

CME Group

CME Group, the world's largest and most diverse financial exchange, does not buy or sell contracts, nor does any financial exchange. It hosts trading conducted through one of the more than 3,100 CME Group members.

CME Clearing

Virtually eliminating counterparty credit risk, CME Clearing acts as the counterparty to every trade – the buyer to every seller and the seller to every buyer. CME Clearing matches and settles all trades, collects and maintains performance bonds, regulates delivery and provides data reports – ultimately guaranteeing the creditworthiness of every transaction that takes place in CME Group's markets. This safeguard is the cornerstone of a market that has not suffered a default in more than 100 years. Performance bond/margin deposits are required at each level in the clearing process –

customer to broker, broker to clearing firm, clearing firm to clearing house. The performance bond is a

good-faith deposit that represents the minimum amount of protection against potential losses. CME Clearing handles more than 90 percent of all futures and options contracts traded in the United States. This requires management of the substantial exposure that results from guaranteeing the performance of each of nearly 2.2 billion contracts annually.

Futures Brokerage Firms

A futures brokerage firm places orders to buy and sell futures or options contracts for its customers: companies and individuals. Everyone who trades has to have an account with a brokerage firm. The brokerage firm conducting customer trades with the Exchange is either a clearing member of CME Group or a firm registered with a clearing member. All trades are settled through clearing firms, who interact through CME Clearing. The brokerage firm places orders for customers, collects performance bond monies, provides basic accounting records, disseminates market information and counsels customers in futures and options trading strategies. These firms charge a commission on transactions they conduct.

Traders

The traders are individuals or companies that buy and sell contracts on an exchange via a form of public auction. All bids and offers are made publicly so each trader has a fair chance to buy and sell. There are different categories or types of traders. Some are private speculators, called locals. Some locals are called scalpers because they make their living by buying and then quickly selling, or selling and then quickly buying, hoping for more profits than losses at the end of the day. Other locals are day traders, who buy and sell throughout the day, closing their positions before the end of trading; and position traders, who take relatively large positions in the market and may hold their positions for a day or longer. The second class of traders are the brokers who act as agents for customers who are individuals and companies. Brokers are paid a fee for executing customer orders.

Speculators

Speculators are people or firms who try to make money by buying and selling futures and options. They speculate that prices will change to their advantage. They don't intend to buy or sell the actual commodities. Speculators take on market price risk and provide liquidity.

Hedgers

People or firms who use futures and/or options as a substitute for buying or selling the actual commodities are called hedgers. They buy or sell contracts to offset the risk of changing prices in the cash markets. Hedgers transfer risk to speculators.

Key Points

1. Commodity exchanges provide the location, electronic marketplace and rules for trading.
2. CME Clearing acts as the seller to every buyer and the buyer to every seller. It also is the central depository of required good-faith deposits (performance bonds) that act to guarantee contract performance by all parties.
3. Everyone who trades futures must have an account with a futures brokerage.
4. Hedgers transfer risk to speculators, who take on risk in pursuit of profit.