Sustainability of E-Business of Agro Commodities and the Role in Economic Growth of India

Payal Upadhyay[1] ● Keshav Gupta[2]

[1]Assistant Registrar, Mahirishi Arvind College, Kota
[2]Associate Professor, Satyawati College Eve. (University of Delhi)

Email Id: payalsharmaup@yahoo.co.in[1] ● k7gupta@gmail.com[2]

Abstract. The immense growth and sophistication of ICT have made the e-financial markets more efficient with greater information transparency and access. These markets play a major role in price discovery and serve a risk shifting function that can be used to lock-in prices in advance instead of relying on uncertain price developments in future. Apart from these basic functions e-financial markets have a number of indirect benefits like providing liquidity, speculative trade in a controlled environment, controlling black marketing and economic growth of the country.

Besides the well established fact towards the requirement of market based instrument, there is always been in doubt on the usefulness and suitability e-agro commodity futures contract especially in agricultural based economy like India. The Government has argued for continuation of temporary ban on futures trading in some essential commodities and expects the ban may rein in inflation expectations. The authors argued that banning futures is an illogical solution as it obstructs the sustainability development of a mechanism to regulate unhealthy speculation. The present study will critically examine the rationale behind the ban and study how logical the decision to impose it is.

Keywords: E-futures, Agro commodity, Sustainability, Economic Development

1 Introduction

E-commerce revolution from last decade has made an impact on the globe and as well in Asian country like China & India, the giants of Asia.

Through the successful implementation of E-commerce countries are growing rapidly by deploying economical resources. ICT has made communication cheaper, faster and effective. It provides easy access to Google the information draft it and uses it as per the requirement of the situation. it is a powerful sector has been a pioneer and a powerful catalyst in addressing the needs and interest of low income communities in developing countries but it was not always so. Only in the past twenty years or so has a self conscious appreciation for the ICT sector's role in expanding economic opportunity emerged. The rate of technological innovation in ICT has accelerated dramatically, and the sector today is orders of magnitude larger than it was 20years ago, and it encompasses a more diverse universe of players than ever before. Today, the sector includes hardware, software, the internet, telephony, and content, application and support service, provided by entities ranging from corporate giants to garage entrepreneurs to individual developers and open source networks. Relevant content and applications are integral parts of the value proposition. And the “network effects” is crucial technology only increases productivity when lots of people share access.ICT has become the foundation of every sector of every economy, everywhere.

Although various sector are contributory in the in the sustainable growth of a Nation. But in the country like India, where farming and agriculture is the biggest sector to contribute in the growth of Economy, requires some serious discussion to focus on it.

2. Sophisticated Growth of Information And Communications Technology (ICT)

India is No doubt developing as a strong nation in the world but still we require more sophistication in ICT to gear up. ICT has become the foundation of every sector of every economy. At the macro level, various studies have shown valuable, positive impacts on GDP from information technology, telecommunications and mobile telecommunications investment in both developed and developing countries. In developing countries, particularly into low income individuals and small enterprises, some factors impact the role of ICTs. In response, large ICT companies have begun to broaden their collaborative strategies to include actors outside the "business ecosystem" as traditionally conceived such as government agencies, non-governmental organizations, microfinance, institutions and social entrepreneurs to increase the value of their technologies and improve their economic opportunity impacts.

India having raw resources more then finished ones so it is important to develop and improve technological aspects to give away a strong medium of processed information to people working in diverse areas because India economy is more effected by the agriculture sector although manufacturing and service industries are also improving but major attribution to economical development and growth is by agriculture sector, so ICT in India requires more transparency to give away easy access to market players to operate smoothly and take decisions more wisely.

3. E-financial markets

In the recent year, the prices of the metal commodities like gold have been more volatile and the prices of some of the agricultural products like sugar, wheat, chana and metal products like gold have gone up. The uncertainty of commodity prices leaves a producer or trader open to the risk of receiving a price lower than the expected price for the commodity. The online future markets offer the price risk management (hedging) that helps in shifting the risk to speculators or traders who are willing to assume the risk. It gives a direct benefit to the hedger that try to minimise risk by taking opposite positions in the futures and cash markets. Future contracts allow speculative trade in a more controlled environment where monitoring and surveillance of the participants is possible. Hence, futures ensure transparency. The transparency benefits the producer, trader and consumer by spreading awareness about prices in the open market. For example, farmers use them to find out the prices of agricultural commodities and decide their cropping pattern, a jeweler uses them to buy gold for their future requirements and lock in the price. A biscuit manufacturer buys wheat in advance to avoid the imminent loss of margin on their final product. Futures also help in standardization of quality, quantity and time of delivery, since these variables are agreed upon by the participants and specified in the futures contract.

Application of several market-based instruments to deal with the commodity price risk basically focuses on the introduction of derivatives viz. futures and options contract on several commodities. In other words, it is widely proposed to setup an efficient derivative market for commodities to strengthen the commodities market. It is internationally appreciated that if the derivative markets function adequately and without manipulation, some of the important policy goals regarding price volatility of agricultural commodities can be addressed in a market oriented manner. The basic need to trade in commodity derivatives in general and commodity futures in particular arises for Hedging. Hedging can be represented as just taking a required amount of counter position (Buy or Sell) in a standardized futures contract against the corresponding position (Sell or Buy) of the related underlying commodity. This counter positions in the futures contract help to offset the loss expected to incur from the adverse price movements of the underlying commodities. Therefore, it is very important to develop futures and other forms of derivative trading in all commodities more especially, those which are vulnerable to large and erratic price fluctuations. Commodity futures also help in discovering the future prices of underlying commodities. This anticipation of commodity prices as on some future dates makes the underlying spot market stronger and vibrant. Therefore, commodity futures market is expected to have a built-in Mechanism for stabilizing commodity prices which are otherwise prone to fluctuate in response to any swing in the demand and supply forces. But at the same time, it is also important to ensure that the commodity futures market is free from any manipulations, which otherwise lead to price distortion and resist the market from performing an effective price discovery function. The surveillance mechanism has to be robust which can uncover any kind of manipulations and nip it in the bud.

The present study has exhibited that the spurt in commodities prices like gold and the so called inflationary pressure on commodities like –wheat, sugar, and chana remained there even after the introduction of ban because the prices had gone up not because of the futures markets speculation but because of the basic demand supply mismatch.

4. History of Commodity Derivatives Market in India

Commodity derivative trading in India has a long history extending over more than a century. Its first futures market for cotton started at Mumbai in year 1875.Subsequently futures trading had started for oilseeds (Mumbai, 1900), jute (Calcutta, 1912),wheat (Hapur, 1913) and bullion (Mumbai, 1920).The markets underwent rapid growth between the two World Wars. Before the outbreak of the Second World War, a large number of commodity exchanges and trading of futures contracts in several commodities such as cotton, jute, oilseeds, groundnut, wheat, rice, sugar, silver and gold, flourished at various locations all through the country. But during the Second World War, the Defense of India Act, 1943 was invoked to prohibit futures trading in some commodities. An opinion emerged that speculative trading in commodity markets have helped in inflationary pressures in these commodities.

Futures trading were initiated again on 16 diverse commodities after independence, on the recommendation of the Forward Market Commission (FMC). However, the growing status of commodity futures market in India again could not last for long. Owing to agricultural shortages and rising prices, and a growing apprehension that speculative activities on commodities through futures trading may fuel inflation in Indian economy, central government again banned futures trading in most of the commodities. Even if the Dantwala Committee (1966) recognized the benefits of commodity trading even at the time of commodity scarcity, the recommendation were ignored by the governmental authorities. This banning process continued till end 70s, followed by formation of Khusro Committee in the year 1980. Khusro committee also supported the revival of futures trading in most of the major commodities including even potatoes and onions. The ban on all other commodities still continued with the misconception that speculative futures trading destabilize the prices of commodities. During the new era of liberalization in 1990s, the government appointed another committee in 1993 under the chairmanship of Prof. K.N. Kabra to have a reconsider the necessity of commodity futures in Indian economy. The Kabra Committee (1994) recommended the reintroduction of futures trading in a wide number of commodities and also the up gradation of existing commodity exchanges to facilitate futures trading at the International level. The actual reform started after the intervention of international bodies followed by the submission of World Bank – UNCTAD report in the year1997. The international pressure made the Government of India implement the majority of the recommendations of Kabra Committee (1994). This eagerness to stimulate commodity futures trading in India not only led to recognizing and strengthening of various regional commodity exchanges, but also to build up national level multi –commodity exchanges. Accordingly four national level multi-commodity exchanges (MCX, NCDEX, NMCEX, and ICEX) were recognized for online futures trading which started their operations since the year 2003. Therefore, the year 2003 is considered to be a turning point in the history of Indian commodity futures market .After the initiatives of the electronic trading at multi commodity exchange and NCDEX the gold became major attraction in these market.

These markets are national on-line markets and supposedly play a major role in price discovery ensuring an integrated price structure throughout the country. They also serve a risk shifting function that can be used to lock-in prices in advance instead of relying on uncertain price developments in future. Apart from these basic functions e-financial markets have a number of indirect benefits like providing liquidity, speculative trade in a controlled environment, controlling black marketing. The present study has attempted to critically examine the increasing trade volumes due to online future markets since its existence in November, 2003 and their impact on inflation of India.

With rising prices, the functioning of futures markets came under suspicion during 2006–07 and the government ordered a ban on futures contracts for 6 commodities like Urad, Tur, Wheat and Rice to avoid the abnormal rise in their prices. Followed by this, Sugar, Oil, Rice and Potato were also added to the banned list in 2007, but were subsequently allowed for trading in 2008. The Indian Government again banned future trading in Chana, Potato and Soya oil in May 2008. The ban on sugar was lifted in 2009 .As against the argument of Price Discovery, Hedging of Price Risk, Risk Sharing, etc. as the important functions of futures market; several arguments are offered against the unbridled trade in the commodity future market in India leading to price inflation.

The critics have widely pointed out that in the presence of any future bad news in the market, the speculators tend to hoard the concerned commodities and hence artificially drive up the prices. As a result of these speculative activities of major market players, the volatility of the underlying spot market for those commodities also increases sharply. Unlike as claimed, the trading opportunities are generally monopolized by large traders/farmers, and give a little space for others to take part in the commodity market. For example, recent onion price kike is owing to a very few traders.

5. Objectives of the Study

The objective of the study is to examine the impact of online trading of agro commodities like wheat, sugar and chana .and their role in economy including measure like Inflation. Inflation is said to be triggered by the futures trading. The price rise of wheat, sugar and chana during this period has become the cynosure of Indian commodity derivatives. We have undertaken the study from a secondary data of prices, volumes, Inflation, collected from Thompson Reuters, MCX, and NCDEX. The study aims to show commodities and its online trading is again a blessing in disguise for shifting the risk rather than fuelling the pure speculation and causing inflationary pressures on these prices. The daily prices of these commodities have been used for the time series analysis.

The exact period may vary for different commodities, depending on the availability of trading information. If there is any missing observation, due to non-trading, in any day and in any of the market, the common practice is to remove that specific interval (s) from the sample and therefore has been applied here also.

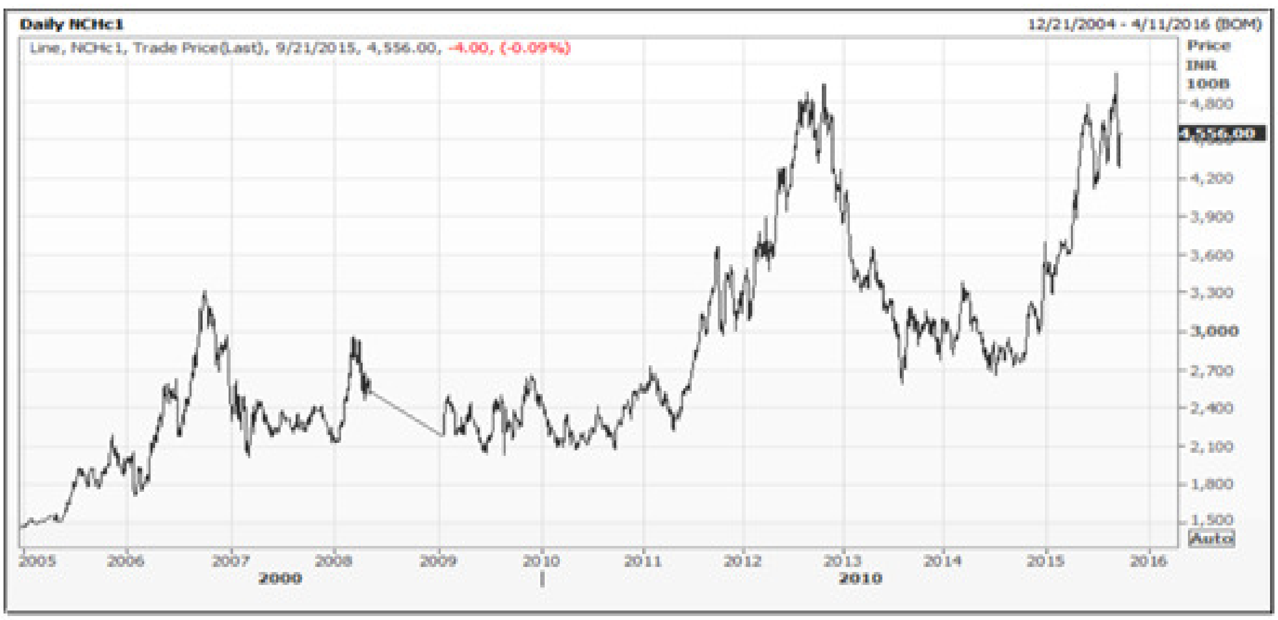
6. Results and Discussion

For common man India wheat, sugar and chana are basic prices which if they happen to go up disturbs the common household budget. Similarly, investors of India, gold are a prized asset, cherished as both an adornment and an investment. For the government, gold is a major contributor to the current account deficit, a challenge that needs to be addressed. It is estimated that at least 2.5 million people are employed by the gold industry and, according to Price Waterhouse Coopers, gold boosts economic output in India by at least $30 billion per annum. Indian gems and jewelry has been fastest growing industries in the country and a leading foreign exchange earner.

Domestic and international prices of Wheat during last ten years

Domestic and international prices of sugar during last ten years

Domestic and international prices of chana during last ten years



A closer look at the prices of sugar during the last 10 years clearly indicates that the price rise continued even during the ban period and even after the lifting of the ban on its trading in the futures markets. During the period the prices are also a reflection of the international price too with a strong correlation.

7. Conclusion

The present study has exhibited that even though the inflationary pressure on commodity, especially agricultural commodities, prices have gone up sharply after the introduction of commodity futures contracts, the destabilizing effect of the futures contract is casual in nature and tends to vary over a long period of time. Even if the spot prices of few agricultural commodities in India destabilized during the post commodity futures period, it is very difficult to come out with a categorical statement regarding the un-usefulness and irrelevance of futures contract in commodity, especially on essential agricultural commodities.

Even though the inflationary pressure on commodity, especially agricultural commodity, prices have gone up sharply after the introduction of commodity futures contracts, the destabilizing effect of the futures contract is casual in nature and tends to vary over a long period of time.

The price rise of most of these commodities is mirror image of the international prices with strong correlation existing between these prices. In fact World food prices have seen a significant rise during the current decade. The rise in prices was particularly sharp during 2007 through mid-2008 reflecting higher demand and low stocks. Prices of all major food items like rice, wheat, maize and edible oils increased more than doubled during the period 2005 to 2008. Prices have, however, eased significantly since July 2008 on the back of improved supply prospects, particularly for oilseeds and grains in major producing countries.

Since the government of India have posted certain temporary ban on essential commodities, marketers assume that it is highly risky and volatile situation to work under so they usually steps themselves involving in uncertain environment.

Indian government requires to rethinking on the issue to resolve the pressure from e-financial market and ancillary markets associated with e-agro commodity sector to give free passage to Indian e-agro commodities for more effective contribution in developing Indian economy.

Government requires examining the present situation and future expectations and should find certain way to dissolve the ban on certain commodity and to ensure the market players to provide more risk free environment to work with in otherwise unhealthy speculation will develop illegal practices and kill the fairness of economic market.

Government should redefine the accessibility to its banned area and try to improve the bar to certain limits. So that stops hindering the economic development of country

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