

# Commodities Exchange Center, Inc.

**COMEX<sup>®</sup>**



*New York  
Cotton  
Exchange*



# An Introduction to the Commodities Exchange Center

## Table of Contents

Commodities Exchange Center .....	3
FEATURE—What's All the Shouting About? .....	5
FEATURE—The Economic Role of Futures and Options ...	7
Tracing a Futures Transaction at CEC .....	8
CSCE, Coffee, Sugar & Cocoa Exchange, Inc. ....	10
COMEX, Commodity Exchange, Inc. ....	11
NYCE®, New York Cotton Exchange .....	12
NYMEX, New York Mercantile Exchange .....	13
FEATURE—Futures Trading: Should You Get Involved? ....	14







**CEC** In July 1977 four independent commodity exchanges opened a new trading floor in Four World Trade Center under the auspices of a service company called Commodities Exchange Center, Inc. (CEC). CEC manages the 26,500 square foot trading floor. CEC is also responsible for the vast computer network which disseminates futures and options price information, telecommunications, security, administrative and office services for the four member exchanges. The member exchanges are: Coffee, Sugar and Cocoa Exchange, Inc., Commodity Exchange (COMEX), New York Cotton Exchange (NYCE), and New York Mercantile Exchange (NYMEX). CEC occupies over 130,000 square feet in 4 World Trade Center that includes not only the trading floor but the exchanges' administrative offices, clearing associations, computer center and conference rooms.

## Tour Program

Each year thousands of people—school children, colleges, social organizations, trade related institutions, tourists—come to the CEC Visitors Gallery, located on the 9th floor of 4 World Trade Center, to view the excitement and activity on the trading floor. The Gallery is open to the general public Monday through Friday, 9:30 AM to 3:00 PM.

CEC also invites you and your group to join our tour program which offers a presentation on the history of commodity trading, an informative lecture explaining the activity conducted on the floor, followed by a question/answer period. Tours are conducted on a pre-arranged basis: 11:00 AM, 1:00 PM, and 2:00 PM, Monday thru Friday.

*Tours, which can be arranged for groups of 5-50, should be scheduled at least 1 week in advance of the date desired. Please call 212-938-2025 for more information.*





## What's All the Shouting About?

In observing the trading floor, what may look like chaos is actually a very orderly process of futures and options contract execution known as open outcry. Open outcry is a process common to all commodity exchanges in the U.S. The difference at the CEC is that four of those active exchanges are conducting trading within a jointly shared facility.

There's a very good reason why everyone is shouting and waving. They are required to do so. A commodities exchange is probably the best example of a true auction market, for all exchanges require that bids and offers be made by open outcry. When there are a hundred or more commodity brokers shouting at each other around a single trading location, the din is so great it is often difficult to hear individual voices, so brokers have their own sign language to be sure everyone in the trading ring understands what's going on. When you see a broker with his hand turned palm toward him, he is buying. If the palm is turned away from him, he is

selling. The number of fingers he extends indicates the number of contracts he would like to buy or sell.

Orders get to the trading floor the same way orders to buy or sell securities get to a stock exchange.

Somewhere in the world a customer gives an order to buy or sell to his broker who, in turn, transmits it to a telephone clerk on the CEC Floor. The order ticket is then time-stamped and relayed to a member in the appropriate trading ring, who will execute the trade if possible.

When a trade occurs, quantity, time, price and broker are noted on a card and confirmation is relayed back to the telephone clerk. The clerk then reports it to the originating broker who informs his customer that the trade has been completed. Meanwhile, an exchange reporter enters the trade details into the CEC data communications system. Any price variations from the last trade made are flashed instantaneously on the display boards that surround three sides of the trading floor.



# What's All the Shouting About?

*(continued)*

Simultaneously, the new price is displayed on video screens, and sent out to the press and to quotations systems throughout the world. The entire process, from initial order to confirmation to price display, usually takes less than a few minutes.

Those trading data confirmation cards are very important, for when trading ends for the day they must be submitted to the appropriate exchange clearing association. Customers' names need not appear on the cards as buyers or sellers. Only the name of the broker and the clearing association member, in whose name the trade was made, must be on the card.

Not all exchange members have clearing association membership, but every trade must be verified and guaranteed by the clearing association members. Consequently, every floor trader is required to clear his transactions with a clearing member or is himself a member of one or more of the clearing associations at the CEC.

A clearing association exists to facilitate the flow and transfer of funds resulting from its member firms' transactions, and to serve as a guarantor of contract performance. In other words, the brokerage firm, after executing a trade, deals exclusively with the clearing association which, in effect, acts as the seller to every buyer and buyer to every seller.

The clearing association membership is comprised of the larger brokerage houses and trading firms acting jointly to guarantee the contract obligations of each clearing member.

Behind all the trading floor activity is an army of producers, processors, manufacturers, importers, exporters, bankers, researchers, institutional investors, brokers, economists, governments, and individual speculators. All have their own particular economic purpose for being involved in the day-to-day price movements of the vital commodities that are being bought/sold on the floor of the Commodities Exchange Center.

And that's what all the shouting is about.

# The Economic Role of Futures and Options

Futures and options are generally traded by two types of traders: hedgers and speculators. The hedgers, who represent commercial interests, use futures and options markets to offset and manage price risk. Speculators trade futures and options as an alternative or additional investment vehicle to stocks, bonds and other financial instruments. Speculators seek to profit by assuming the price risk that hedgers wish to avoid. Speculators add liquidity to the markets and help futures and options markets perform their two major economic functions: (1) risk shifting and (2) price discovery.

## RISK SHIFTING

Commercial interests, or hedgers, use commodity markets to shift—or more properly manage—the price risk to which they are exposed in their commercial dealings. Hedging involves taking an equal but opposite futures position to one's cash position. For example, a seller of a commodity, such as a farmer, can reduce the risk of falling prices by selling a futures contract. In

case of a drop in price, the farmer would offset the cash market loss when he sells his crop with a futures market profit. Likewise, a manufacturer who needs to buy raw materials in the future for processing can buy a futures contract to reduce the risk that raw material prices will increase before he makes his cash market purchase.

## PRICE DISCOVERY

Futures and options markets provide a competitive price setting mechanism for commodities and financial instruments. Futures and options markets absorb information, allowing prices to be efficiently derived, thereby assuring that both buyer and seller receive the best prevailing price at any point in time. Therefore, properly functioning futures and options markets increase the competitiveness of cash markets by maximizing the information flows of one central market where the forces of supply and demand determine price.



# Tracing Futures and Options Transactions at CEC

An exchange is a membership organization which provides the physical facilities used for futures and options trading within established rules and regulations that are designed to provide standard and equitable treatment for all participants in the market.

All domestic commodity exchanges are regulated by the Federal Government through the Commodity Futures Trading Commission (CFTC).



**1** Your commodity broker transmits your order to the CEC trading floor via telephone or teletype.



**2** Incoming orders are recorded on trading slips which are immediately passed to a floor broker standing at the appropriate trading ring.



**3** Orders are executed by open outcry between floor brokers standing in the trading rings. Open outcry trading involves continued voicing of bids to buy and offers to sell between brokers who also use hand signals to assist communications between one another.



**4** Exchange reporters, stationed among the floor brokers in each ring, are responsible for transmitting the prices of all trades (using hand signals) to a clerk stationed in a rostrum overlooking each ring. The data is then immediately entered into the central CEC computer.



**5** Computer-actuated wallboards instantly display transaction prices to all trading floor brokers and telephone clerks.

All trading data is immediately available to you or your broker via private price quotation vendors who provide CEC data through video terminals or personal computers.

National and international news wire services further distribute CEC trading data, which is published daily by major trade and financial publications.



## Coffee, Sugar & Cocoa Exchange, Inc.



Today, the Coffee, Sugar & Cocoa Exchange, Inc. (CSCE) is the world's leading marketplace for futures and options trading in these international commodities. In existence since 1882, the CSCE has provided a marketplace where the worldwide forces of supply and demand determine the prices of three globally significant agricultural commodities.

On March 7, 1882, the CSCE was founded as the Coffee Exchange of the City of New York by a group of young coffee merchants reacting to a crisis in their trade. In the wake of uncontrolled speculation and tremendous oversupply that led to the collapse of the market in 1880, they sought to rebuild the coffee trade by establishing the first orderly market for trading of coffee futures.

The Exchange added the trading of sugar futures in 1914, and subsequently changed its name to the New York Coffee & Sugar Exchange, Inc. in 1916. A few years later, in October of 1925, the New York Cocoa Exchange was founded, establishing the world's first marketplace for cocoa futures trading. In September of 1979, the Coffee & Sugar Exchange, Inc. and the New York Cocoa Exchange merged, forming the Coffee, Sugar & Cocoa Exchange, Inc.

In 1982 the CSCE was the first U.S. futures exchange to originate trading in options on futures contracts with the introduction of options on world sugar futures. This market has subsequently grown to become the Exchange's second most active contract.

In March of 1986, the CSCE launched an options contract on its cocoa futures, and in the fall of the same year, opened the coffee options market.

In 1987 the Exchange instituted the World White Sugar contract which requires the delivery of refined sugar.

In 1989 the CSCE expanded its presence in the world's markets by offering a futures contract based on a new International Market Index,<sup>SM</sup> (IMI<sup>SM</sup>) thus continuing its 107 year tradition in the international marketplace.

Detailed brochures about each of the Exchange's contracts are available, free of charge, upon request.

*For further information on the Coffee, Sugar & Cocoa Exchange, Inc. and for brochures about coffee, sugar and cocoa futures and options and the IMI, please contact: Communications Department (212) 938-2966; Statistical Information (212) 938-2843; Membership Information (212) 938-2807 or 1-800-HEDGE-IT.*

## Commodity Exchange, Inc.

COMEX

Commodity Exchange, Inc. (COMEX), founded on July 5, 1933, is a product of a merger of four older exchanges, the National Metal Exchange, the Rubber Exchange of New York, the National Raw Silk Exchange and the New York Hide Exchange. COMEX has been an important part of the overall growth of futures trading for more than 50 years.

COMEX is the world's most active metals market and is among the largest commodity futures exchanges in the world. As the dominant exchange for gold futures and options trading, COMEX is a major force in the world gold market. In addition to its prominence in international gold trading, COMEX is the dominant world market for silver and copper futures and options and is the only U.S. exchange to offer trading in aluminum futures.

In its continuing effort to meet the ever-changing needs of the industry, COMEX recently changed its copper futures and options and aluminum futures contracts to high-grade (minimum purity standards) metals. The Exchange also upgraded its trade matching and processing system. The previously used manual procedure for submitting trade data to the Exchange

has been completely automated and responsibility for trade submission has been shifted to clearing members. In addition, COMEX announced plans for an interactive hand-held transaction entry system to accurately record trades in our markets. The system will be feasibility tested in 1990. During testing the hand-held device will be modified to meet the day-to-day needs of COMEX traders. When fully implemented it will bring the speed, accuracy and audit trail enhancements of an automated system to the liquidity of open outcry trading.

COMEX will continue to provide an open and freely-competitive marketplace for the trading of futures and options contracts, tailoring its markets to meet the needs of the industry and develop in conjunction with changes in prevailing regulatory, economic and financial conditions.

*For further information and brochures about COMEX futures and options, please contact: The Marketing Department (212) 938-7921; Statistical Department (212) 938-2937; Exchange relations (212) 938-2936; Member Services (212) 938-2924.*



## New York Cotton Exchange



Founded in 1870 by a group of cotton brokers and merchants, the New York Cotton Exchange (NYCE®) is the oldest commodity exchange in New York. The Exchange consists of 450 members which represent either commercial users, commission houses or themselves. Since its founding, the Exchange has been an integral part of the cotton industry and today is the world's premier marketplace for cotton futures and options trading. The Exchange has also introduced several new innovative products and will continue to respond to the increasingly sophisticated demands of a global financial marketplace.

In 1966, the Exchange built on its agricultural expertise and expanded its product line through the formation of the Citrus Associates of the New York Cotton Exchange, Inc., an affiliate of the Exchange, where frozen concentrated orange juice futures and options are traded.

In 1985, the Exchange entered the explosive arena of financial futures and options through the creation of the Financial Instrument Exchange (FINEX®) division. Several

innovative futures and options contracts are traded on FINEX® including U.S. Dollar Index<sup>SM</sup> (USD<sup>®</sup>) futures and options, Five Year U.S. Treasury note (FYTR®) futures and options, Two Year U.S. Treasury note (2YTN®) futures and European Currency Unit (ECU) futures. Several of these financial contracts have proved to be among the most successful new contracts to be introduced in recent years.

In 1988, the New York Futures Exchange (NYFE), a subsidiary of the New York Stock Exchange, became an affiliate of the NYCE® and moved its trading operations to the NYCE® quadrant. NYFE's financial products include futures and options on the NYSE Composite Stock Index as well as the CRB Futures Price Index.

*For further information and brochures on NYCE® futures and options, please contact: the Marketing Department (212) 938-2702; FINEX® (212) 938-2634; Statistical Department (212) 938-2668; and Membership Information (212) 938-2666. For further information on NYFE futures and options, please contact (212) 656-4949.*

## New York Mercantile Exchange



A little more than a decade since the launch of its heating oil futures contract in 1978, New York Mercantile Exchange (NYMEX) has become the world's leading risk management forum for the energy industry. In the process, it has also become the third largest futures exchange in the U.S..

The NYMEX energy complex is comprised of heating oil, gasoline (1981), crude oil (1983), propane (1987), residual fuel oil (1989) and natural gas futures contracts, along with options on crude (1986), heating oil (1987) and gasoline (1989). Trading volume continues to climb, and the crude oil contract is the world's most actively traded futures contract on a physical commodity.

NYMEX's success has not been limited to energy. The Exchange's hi-tech metals contracts—platinum and palladium—continue to attract broad trader interest. Growing investor participation, new industrial applications and a dynamic marketplace have made NYMEX platinum and palladium futures key financial instruments for hedgers and traders alike.

As the next century rapidly approaches, NYMEX is poised to meet tomorrow's risk management challenges. By developing new and innovative products and seeking the technology to export its liquidity to every corner of the globe, the New York Mercantile Exchange will maintain and enhance its status as a worldwide futures industry leader.

*For further information about NYMEX contracts contact the Marketing Department at (212) 938-2879. For membership information contact Membership Services at (212) 938-2225. For up to the minute statistics on all NYMEX contracts call Fastfacts, the NYMEX 24-Hour Hotline at (212) 938-0064.*



## Futures and Options Trading: Should You Get Involved?

The late Will Rogers offered perhaps the best advice to people who wanted to invest in the stock market. The famous cowboy/comedian said: "Buy low and sell high, and if it don't go up...don't buy it."

His seemingly foolproof advice doesn't necessarily apply to commodity futures markets. In commodities, it's just as important to sell high and buy low, because even "if it don't go up," you may still be in a position to make a profit on a market decline. It's as easy to sell a futures contract as it is to buy one, and profit is possible either way.

Unlike stocks or bonds, you cannot buy a commodity futures contract and put it away for years, or will it to your heirs. Every futures and options contract has a relatively short life span, and if not offset with an opposite transaction, or expiration in the case of an option, ends with ultimate delivery or acceptance of delivery of the commodity, financial instrument, or cash equivalent. The objective, from a speculator's standpoint, is to get into the market at the right time, at the right price, and get out of the market at a better time and price before the contract's maturity or delivery date. The life of a futures contract is generally less than 24 months, and you have a choice of several contract months near and distant from which to choose.

Individual market participants are called speculators—a term that is

often misunderstood. Speculator is not a bad word. It is derived from the Latin *speculari*: to watch and observe. Wise speculators do just that. They watch price movements, observe supply and demand, monitor commercial activity in the market, evaluate the factors affecting price, and then make their buy or sell decisions using "risk capital"—money that they can afford to lose. In effect, speculators do everything possible to minimize risk and maximize profits, without endangering their financial base.

### Where does one start?

Launch your own investigation by contacting and questioning experienced futures brokers. Select a brokerage house on the basis of its depth in futures trading services. It should have good communications facilities, not only with its customers but with its floor brokers at the exchange. The firm should also have research ability to keep abreast of factors affecting market fluctuations as well as training programs for its account executives who are in contact with the customer.

Once you have decided on a firm, evaluate your account executive as well. He should be knowledgeable about the markets in which you are most interested. Not many keep abreast of every futures market every day, but a good broker knows where to get information his customers need and is able to intelligently discuss your position in the market. The sophisticated speculator isn't merely

buying and selling. He may also be using spreads and arbitrage, and he's concerned with the tax aspects of his trading. The broker you choose should be familiar with these market techniques.

Placing an order to buy or sell a commodity contract is critical to success. The speculator must become familiar with the different types of orders and the way instructions should be given to his broker to assure prompt execution.

### Time and price are the two key elements of every order.

Unless otherwise specified, an order will remain in effect only on the day placed. However, an "open order" can be placed and will remain in effect until it is executed or cancelled (also termed "good 'til cancelled" orders). You can specify executions "on-the-opening" or "on-the-closing" of the market or designate a specific time for an order to be executed.

Price is the other element of strategy. Orders to buy or sell "at the market" are executed at the best possible price when the order is received on the exchange floor. But a trader may designate a specific price for the order and run the risk of not having it filled if the market never reaches that point while assuring himself of a better price (than prevails at the time the order is placed) if it is filled.

There are a number of ways to place orders, market orders, limit orders, stop orders, spread orders, combination orders and more. A knowledgeable broker will provide specific educational materials and will assist your investigation into all aspects of futures trading.

### How can one learn more about commodity speculating?

Many books have been written on that subject, and most commodity brokerage firms and commodity exchanges will supply you with informative literature. Seminars and other educational programs for prospective speculators are popular.

Obviously, no one can guarantee success in futures or options markets, anymore than success can be assured in the stock market, real estate, oil exploration or any other risk-oriented investment activity.

If anyone is interested in commodity speculating, the first question to ask is "can I afford to speculate in commodity futures or anything else?" Put simply, speculate only with risk capital money not necessary to maintain your established lifestyle. If you have adequate insurance, sufficient savings for emergencies, and a portfolio of sound stocks or bonds, you may have a good financial foundation. If your fundamental financial obligations are met, you could consider futures and options trading.



Be certain that you aren't undercapitalized. Commodities markets often change rapidly and one of the prerequisites for success is the ability to take losses. Many of the most successful commodity traders have low batting averages when comparing winning and losing trades, but score on the home run. They are accustomed to acting quickly, cutting losses to a minimum while letting favorable trades run as long as possible for maximum profit. Thus, while a successful futures trader may have more losing than winning trades, the size of his profitable trades more than offsets his losses.

Market price fluctuations determine profits or losses. However, the tremendous leverage available to futures traders has the greatest impact on the capital invested. Initial margin requirements vary from broker to broker but average about 10% of the full value of a contract. This relatively small capital outlay makes small price changes into dramatic profits or losses.

Speculators, as a rule, avoid having to make or take delivery of the physical commodity by liquidating their contract position prior to its maturity month.

Conversely, the market may move against them during the same period, but a prudent speculator will have placed a "stop loss" order with his broker in order to liquidate his position when the price of the commodity drops to his established stop point. This strategy may minimize losses and preserve remaining risk capital for use in other trades. Speculators who do not liquidate positions as the market moves against them can expect to receive a "margin call" from their broker to cover the potential loss. Also, a trader may request the return of surplus margin funds that build up in his account when the market is moving in his favor.

There are no magic formulas. Speculators will take losses, but the smart trader can still profit greatly.



**COMMODITIES EXCHANGE CENTER, INC.**  
*Four World Trade Center*  
*New York, N.Y. 10048*  
*(212) 938-2000*

100M690