

## **Glossary of Commodity Trading Terminology**

### **Actuals**

Also called cash commodity, this refers to the actual physical commodity, as distinguished from the futures contract based on the physical commodity.

### **Accumulation**

This occurs when traders in the market are in the process of adding to their existing positions.

### **Arbitrage**

This is the simultaneous purchase and sale of similar commodities in different markets to take advantage of price discrepancies. The two trades may be in different markets, exchanges, delivery months, or commodities. Also see Spreading.

### **Ask**

This is the opposite of bid and indicates the desire to sell a commodity. Also called offer.

### **Assign**

When an option buyer exercises the option, the seller is assigned either a long or short position opposite the purchaser.

### **Backwardation**

This is a futures market in which the relationship between two delivery months of the same commodity is abnormal.

### **Bar chart**

A chart that tracks the open, high, low, and closing prices.

### **Basis**

The difference between the current cash price of a commodity and the futures price of the same commodity. Unless otherwise specified, the price of the nearby futures contract month is generally used to calculate the

basis. Cash minus futures equals basis.

**Bear market**

A market in which prices are declining. A market participant who believes prices will move lower is called a "Bear." A news item is called bearish if it is expected to result in lower prices.

**Bear spread**

This term refers to the purchase of the nearby contract and the simultaneous sale of the deferred month of a commodity to profit from a change in price.

**Beginning stocks**

Also referred to as carryover. These are actual tangible commodity stocks not consumed during the previous year and that are carried over into the next crop year.

**Beta**

Refers to a measure correlating stock price movement to the movement of an index. Beta is used to determine the number of contracts required to hedge with stock index futures or futures options.

**Bid**

The opposite of offer, this is an expression of willingness to buy a commodity at a given price.

**Broker**

This is a company or an individual that executes futures and options orders on behalf of financial and commercial institutions and/or the general public.

**Brokerage fee**

Also referred to as a commission fee, this is the fee that a broker charges his customers for services rendered.

**Brokerage house**

Also referred to as a commission house, FCM, or wire house, this is an organization (or individual) that solicits or

accepts orders to buy or sell futures contracts or options on futures and accepts money or other assets from customers to support such orders.

**Bucket shop**

Describes a firm which buys an inventory of futures contracts and sells them to customers at prices other than those derived from the open outcry system used by the exchanges. This is an illegal activity.

**Bull market**

A market in which prices are rising. A market participant who believes prices will move higher is called a bull. A news item is considered bullish if it is expected to result in higher prices.

**Bull spread**

This term refers to the sale of the nearby contract and the simultaneous purchase of the deferred month of a commodity to profit from a change in price.

**Calendar spread**

See Spreading – horizontal

**Call option**

An option that gives the buyer the right, but not the obligation, to purchase (go long) the underlying futures contract at the strike price on or before the expiration date. The buyer of a call is considered bullish. Due to the nature of options, buying a call is less risky than buying an outright futures position.

**Carrying charge**

Also referred to as Cost of carry or carry, it is the cost of storage, insurance, and financial charges incurred by holding a physical commodity. In Interest Rate futures markets, it refers to the differential between the yield on a cash instrument and the cost of funds necessary to buy the instrument.

**Carry-out**

Also referred to as beginning stocks. These are commodity stocks not consumed during the previous year, and are carried over into the next crop year.

**Cash commodity**

A physical commodity, as distinguished from a futures contract, it calls for the delivery of the cash commodity during the delivery period.

**Cash market**

The marketplace where actual commodities are bought and sold, without the use of a futures market. Transactions in the cash market are negotiated privately, and are not subject to standardized regulations as in the futures market. See also forward contracts.

**Charting**

The use of graphs and charts in the technical analysis of futures markets to plot price movements, volume, open interest, or other statistical indicators of price movement.

**Churning**

Excessive trading that results in the broker deriving a profit from commissions while disregarding the best interests of the customers.

**Clear**

The process by which a clearinghouse maintains records of all trades and settles margin flow on a daily mark-to-market basis for its clearing members.

**Clearing member**

A member of an exchange clearinghouse responsible for the financial commitments of its customers. All trades of a non-clearing member must be registered and eventually settled through a clearing member.

**Clearinghouse**

An agency or separate corporation of a futures exchange, it is responsible for settling trading accounts, collecting and maintaining margin monies, regulating delivery, and reporting trade data. The clearinghouse becomes the buyer to each seller and the seller to each buyer, and assumes responsibility for protecting buyers and sellers from financial loss by assuring performance on each contract.

**Closing price**

Settlement price; the price of a commodity that is settled at the end of any trading day. The exchange

clearinghouse determines a firm's net gains or losses, margin requirements, and the next day's price limits, based on each futures and options contract settlement price. If there is a closing range of prices, the settlement price is determined by averaging those prices.

### **Commission fee**

Also referred to as a brokerage fee. The fee that a broker would charge his customers for his services.

### **Commodity**

Any good that is tradable on an exchange. A good or item of trade or commerce.

### **Commodity Futures Trading Commission (CFTC)**

A federal regulatory agency created in 1974 by the Commodity Exchange Act. This is the agency that oversees commodity futures trading in the U.S. and regulates the futures exchanges, FCMs and their agents, floor brokers, and traders, among others.

### **Commodity pool operator (CPO)**

An individual or organization engaged in a business such as an investment trust, who solicits or accepts funds from customers for the purpose of commodity trading on a commodity exchange. CPOs generally deal with commodity pools, funds, or managed accounts, and must be registered with the CFTC.

### **Commodity trading advisor (CTA)**

An individual or organization who advises others of commodity trading recommendations for a profit. CTAs must be registered with the CFTC.

### **Congestion**

Occurs when a market is trading sideways, awaiting new information before continuing or reversing a trend.

### **Contract**

A legally enforceable agreement between two or more parties for performing, or refraining to perform, some specified act. For example, delivery of 40,000 pounds of live cattle at a predetermined time, place, price, and grade.

**Contract month**

Also referred to as delivery month. The month in which a futures contract expires, requiring either settlement or delivery.

**Convergence**

A term referring to the tendency of cash and futures prices to come together (as in, the basis approaches zero) as the futures contract nears expiration.

**Cost of carry**

Also referred to as carrying charge or carry. These are costs, including storage, insurance, and other financial charges, incurred by holding a physical commodity. In interest rate futures markets, it refers to the differential between the yield on a cash instrument and the cost of funds necessary to buy the instrument.

**Covering a position**

In futures trading this phrase means to offset your original position. Whatever is sold must eventually be bought back, and vice versa.

**Crop (marketing) year**

Time span from harvest to harvest for agricultural commodities. The dates of each crop year vary slightly with each agricultural commodity. For example, the marketing year for soybeans begins September 1 and ends August 31.

**Crop reports**

Compiled and released throughout the year by the U.S. Department of Agriculture on various agricultural commodities. Information in the reports includes estimates on planted acreage, yield, and expected production as well as comparison of production from previous years.

**Crush spread**

The purchase of soybean futures and the simultaneous sale of soybean oil and meal futures.

**Customer margin**

Within the futures industry, financial guarantees required of both buyers and sellers of futures contracts and sellers of options contracts to ensure fulfilling of contract obligations. Futures Commission Merchants (FCMs)

are responsible for overseeing customer margin accounts. Margins are determined on the basis of market risk and contract value. Also referred to as a performance-bond margin. Financial safeguards to insure that clearing members (usually companies or corporations) perform on their customers' open futures and options contracts. Clearing margins are distinct from customer margins that individual buyers and sellers of futures and options contracts are required to deposit with brokers.

**CWT**

Hundredweight. Descriptive of meat markets. Prices used are multiplied by a hundred to get actual price of the animal.

**Daily trading limit**

The maximum price range that a contract trades within during one day.

**Day traders**

Speculators who take positions in futures or options contracts and liquidate them prior to the close of the same trading day.

**Deferred (delivery) Month**

The more distant month(s) in which futures trading is taking place, as distinguished from the nearby (delivery) month.

**Delivery**

The actual transfer of the physical commodity from the seller of a futures contract to the buyer of the contract. Each futures exchange has specific procedures for delivery of a cash commodity. Financial contracts, such as stock and currency indexes, are settled in cash.

**Delivery month**

Also referred to as contract month. The month in which a futures contract expires, requiring either settlement or delivery.

**Delta**

A measure of how much an option premium changes, given a unit change in the underlying futures price.

**Demand, law of**

The relationship between product demand and price.

**Discretionary account**

A type of futures account where the customer gives his broker power of attorney to trade his account without notification prior to a trade. Also referred to as a controlled or managed account.

**Distribution**

This occurs when traders in the market are taking profits.

**Econometrics**

The application of statistical and mathematical methods in the field of economics to test and quantify economic theories and the solutions to economic problems.

**Equilibrium price**

An economist's term. When referring to commodities, the market price at which the quantity supplied of a commodity equals the quantity demanded.

**Eurodollar time deposits**

U.S. dollars on deposit outside the U.S., either with a foreign bank or a subsidiary of a U.S. bank. The interest paid for these dollar deposits generally is higher than that for funds deposited in U.S. banks because the foreign banks are riskier—they will not be supported or nationalized by the U.S. government upon default.

**Exchange for physicals**

Also referred to as against actuals or versus cash. The exchange of physical commodities for cash. Generally used by hedgers.

**Exercise**

The action taken by the holder of a call option if he wishes to purchase the underlying futures contract or by the holder of a put option if he wishes to sell the underlying futures contract.

**Exercise price**

The price at which the futures contract underlying a call or put option can be purchased (if a call) or sold (if a put). Also referred to as the strike price.

**Expiration date**

Options on futures generally expire on a specific date during the month preceding the futures contract delivery month. For example, an option on a January futures contract expires in December but is referred to as a January option because its exercise would result in a January futures position.

**Exports**

The amount of a domestically produced commodity sold to foreign buyers.

**Fibonacci**

Sequence of numbers constructed by adding two numbers to arrive at a third.  $1+1=2$ ,  $2+1=3$ ,  $3+2=5$ ,  $5+3=8$ ,  $8+5=13$ , and so on. 1, 2, 3, 5, 8, 13, 21, 34, 55, 89, 144....

**Fill or kill (FOK)**

An FOK order is to be either filled immediately or cancelled, and may result only in a partial fill if any.

**First notice day**

According to Chicago Board of Trade rules, the first day on which a notice of intent to deliver a commodity in fulfillment of a given month's futures contract can be made by the clearinghouse to a buyer. The clearinghouse also informs the sellers with whom they have been matched up.

**Floor broker (FB)**

An individual who executes orders for the purchase or sale of any commodity futures or options contract on any contract market for any other person.

**Floor trader (FT)**

An individual who executes trades for the purchase or sale of any commodity futures or options contract on any contract market for such individual's own account.

**Forward (cash) contract**

A cash contract in which a seller agrees to deliver a specific cash commodity to a buyer sometime in the future. Forward contracts, in contrast to futures contracts, are privately negotiated and are not standardized.

**Full carrying charge market**

A futures market where the price difference between delivery months reflects the total costs of interest, insurance, and storage.

**Fundamental market analysis**

The study of supply and demand factors that affect price movements in the markets. Weather patterns, war, government activities, discoveries, etc., all have effects on market movements.

**Futures commission merchant (FCM)**

Also referred to as a brokerage house, commission house, or wire house. An individual or organization that solicits or accepts orders to buy or sell futures contracts or options on futures and accepts money or other assets from customers to support such orders.

**Futures contract**

A standardized agreement to buy or sell a set quantity and quality of a commodity at a predetermined place and time at a price discovered on an exchange floor. The terms of these agreements are set by the exchanges.

**Futures exchange**

A marketplace with established rules and regulations where buyers and sellers, or their brokers, meet to trade futures and options on futures contracts. The Chicago Mercantile and New York Stock Exchange are examples.

**Gamma**

A measurement of how fast delta changes, given a unit of change in the underlying futures price.

**Good 'till cancelled**

An order that remains on the books until the customer cancels it. Otherwise all orders are day-orders by default.

**Government National Mortgage Association (GNMA)**

A government organization which issues guaranteed certificates backed by VA and FHA mortgages.

**Gross processing margin**

The difference between the price of a raw material and its products.

**Hedger**

An individual who either owns or plans to own a cash commodity and is concerned that the cost of the commodity may change before either buying or selling it in the cash market.

**Hedging**

The process of transferring risk of loss, due to adverse price movement, by taking an equal but opposite position in the futures market as their position in the cash market. Hedgers use many different trading strategies in the futures markets, to protect their business from adverse price changes.

**High**

The highest price of a market for a certain time frame.

**Holder**

Also referred to as the option buyer. The purchaser of either a call or put option. Option buyers receive the right, but not the obligation, to assume a futures position.

**Initial margin**

The amount of money, set by an exchange, which a customer must have deposited in his futures account at the time he places an order to buy or sell a futures contract.

**Intrinsic value**

The amount by which an option is in-the-money. See also options.

**Introducing broker (IB)**

A person or organization that solicits or accepts orders from customers to buy or sell futures contracts or options on futures. The IB receives a commission for this service and can offer trading advice when needed.

**Inverted market**

A futures market in which the price relationship between two delivery months of the same commodity is inverted.

**Last trading day**

All outstanding futures contracts must be settled in cash or by delivery on the last trading day of the contract month.

**Leverage**

This term is the basis for the futures market and describes the act of purchasing or selling a futures contract with a much smaller sum of money than the contract is worth. However, when you enter into a leveraged position in the market you are still responsible for the entire contract value, whether you profit or not.

**Limit order**

A limit order sets a limit on the price and/or the time of execution. For example, a buy limit order would be placed below the market and executed at or below the market.

**Liquidity**

Refers to a market that allows quick and efficient entry or exit at a price close to the last traded price. This ability to liquidate or establish a position quickly is due to a large number of traders willing to buy and sell. The market is said to flow like liquid, or have liquidity. Conversely, a market with little trading volume is said to be illiquid. A volatile market has little liquidity.

**Long**

A person who is buying the physical commodity or who has bought the futures or option contract. To go long soybeans, or to hold a long position, means that you have purchased the contract, anticipating a price increase.

**Long hedge**

Buy hedge. To purchase a futures contract with the intent to protect against a possible price increase of cash

commodities that will be purchased in the future. At the time the cash commodities are bought, the futures position(s) are closed with the sale of the futures contract(s). Converse of short hedge.

**Low**

The lowest trading price of the day, week, or month for a futures contract.

**Maintenance margin**

The minimum dollar amount that must be kept in a customer's margin account. These amounts are set by the exchanges.

**Managed futures**

Represents an industry comprised of professional money managers, known as commodity trading advisors, who manage client assets on a discretionary basis.

**Margin**

The amount of money that must be deposited by the customer prior to the purchase or sale of a futures contract. This money acts as earnest money or a performance bond. Margin for options on futures contracts is required only when selling or writing a call or put, not on the purchase.

**Margin call**

If, due to adverse price swings, the amount of loss in a customer's account is greater than the amount of margin required by an exchange, the customer would receive a margin call. This requires the customer to either bring his account balance back to the initial margin level or to liquidate his position.

**Market order**

An order to buy or sell that does not specify price. This order is to be filled at the best possible price, as soon as possible. These orders generally take precedence over all others.

**Market value-weighted index**

A stock index in which each stock is weighted by market value. A change in the price of any stock will affect the index in proportion to the stock's respective market value. The S&P 500 is an example of a value-weighted index.

**Marking to market**

A daily process to debit or credit a margin account based on the close of that day's trading session.

**Moving averages (MA)**

A lagging technical indication tool that adds up the previous closes and divides by the number of days it tracks. Examples include: 10, 100, and 200-day MA.

**National Futures Association (NFA)**

A self-regulatory group, organized under the CFTC, whose purpose is to enforce ethical standards and customer protection rules, screen futures professionals for membership, audit and monitor professionals for financial and general compliance rules, and provide arbitration of futures-related disputes. Similar to the NASD, National Association of Securities Dealers.

**Nearby (delivery) month (Spot month)**

The contract month closest to expiration.

**Offer**

Opposite of bid. Indicates the desire to sell a commodity. Also referred to as ask.

**Offsetting a position**

The reversal of an original position. For example, to offset the purchase of a futures position, one would sell the same contract month of the same commodity at a later date.

**OPEC**

Organization of Petroleum Exporting Countries. Included are Algeria, Ecuador, Gabon, Indonesia, Iran, Iraq, Kuwait, Libya, Qatar, Saudi Arabia, The United Arab Emirates, and Venezuela.

**Open interest**

The total number of open contracts which have not yet been offset.

**Open outcry**

A method of trading on an exchange floor, using oral bids and offers, that ensures fairness and integrity for both buyers and sellers. Every price, bid or offered, must be verbal. Commodity futures prices are “discovered” by open outcry.

**Opening price**

The first traded price of the session for a given commodity. See also closing price.

**Options**

An option on a futures contract gives the purchaser the right, but not the obligation, to buy or sell the underlying futures position. The buyer of an option must pay a premium to the seller. Only the buyer can exercise the right to own the underlying futures position. (There are many books that explain options and their terminology in greater detail.) Call buyers are bullish and think the market will rise. Put buyers are bearish and think prices will decline. The sellers of options can make money in a rising market (put sellers), or a falling market (call sellers), and even a sideways market when the options expire worthless. The risk involved in buying options, other than the market going the wrong way, is that from the day you purchase an option it is a dying entity.

**Assign**

When an option buyer exercises the option, the seller is assigned either a long or short position opposite the purchaser.

**At-the-money**

An option whose strike price is equal or approximately equal to the current market price of the underlying futures contract.

**Exercise**

The action taken by the holder of a call option if he wishes to purchase the underlying futures contract, or by the holder of a put option if he wishes to sell the underlying futures contract.

**Exercise Price**

The price at which the futures contract underlying a call or put option can be purchased (if a call) or sold (if a put). Also referred to as the strike price.

**Expiration date**

Options on futures generally expire on a specific date during the month preceding the futures contract delivery month.

**Holder**

The purchaser of either a call or put option. Option buyers receive the right, but not the obligation, to assume a futures position.

**In-the-money**

A call is in-the-money when its strike price is below the market. A put is in-the-money when its strike price is above the market.

**Intrinsic Value**

The amount by which an option is in-the-money.

**Out-of-the-money**

Having no intrinsic value. Not in-the-money. Futures contract price has not yet reached the strike price.

**Premium**

The price that a buyer of an option pays to the seller for the right to buy or sell the underlying futures position.

**Spread**

The simultaneous purchase and sale of an option contract. There are many different strategies for spreading.

**Strike price**

The price at which the futures contract underlying a call or put option can be purchased (if a call) or sold (if a put). Also referred to as the exercise price.

**Time value**

The probability that an option will move in-the-money before it expires.

**Writer**

The individual who sells the option to the buyer, for a premium.

**Original margin**

The amount of money set by an exchange which a customer must have deposited in his futures account at the time he places an order to buy or sell a futures contract.

**Perishability**

The time frame in which a commodity is able to be used or consumed. Perishable commodities are corn, hogs, and anything else that might spoil or become unusable.

**Pit**

The area on the floor of an exchange where futures trading occurs via open outcry.

**Pit broker (floor broker—FB)**

An individual who executes orders for the purchase or sale of any commodity futures or options contract on any contract market for any other person.

**Portfolio**

The group of investments held by an investor.

**Position**

The commitment which a buyer gives the seller, or vice versa, when entering the market. If one buys into the market, he is said to have taken a long position. Conversely, if one sells the market, he has taken a short position.

**Position limit**

The maximum number that a customer can hold at any given time. These limits are set by the exchanges or the CFTC. Also referred to as a trading limit.

**Position trader**

A trader who holds a position for a longer period of time. The opposite of a day trader or scalper.

**Price discovery**

The act of generating information about future prices through the open outcry system of the commodity futures market.

**Price range**

The range of prices between the day's high and low.

**Profit taking**

In an upward rally, a market might pause briefly due to Longs closing their positions, or taking profits, before continuing the rally.

**Pyramiding**

Purchasing additional contracts with the profits earned on open positions. There are many methods of pyramiding.

**Purchase and sell statement**

A statement issued by the commission house that includes information regarding quantities, prices, commissions, dates and times, and profit or loss of all transactions in a customer's account. P&S statements are issued each time a transaction occurs.

**Rally**

The sharp upward movement of a price.

**Range**

The difference between two prices on a chart.

**Resistance**

A technical trading term used to describe an upper level on a chart in which prices have difficulty penetrating to the up side. The converse of resistance is support.

**Scalper**

A trader who rarely holds a position over a long period of time, but completes many small-profit trades daily. Scalpers trade more frequently than position and day traders and generally more often.

**Sell-off**

Describing the sharp decline of prices. Many factors will cause this.

**Settlement price (closing price)**

The price of a commodity that is settled at the end of any trading day. The exchange clearinghouse determines a firm's net gains or losses, margin requirements, and the next day's price limits, based on each futures and options contract settlement price. If there is a closing range of prices, the settlement price is determined by averaging those prices.

**Short**

A person who is selling the physical commodity or who has sold the futures or option contract. To go short soybeans, or to hold a short position, means that you have sold the contract, anticipating a price decrease.

**Short hedge**

Sell hedge. To sell a futures contract with the intent to protect against a possible price decrease of cash commodities that will be sold in the future. At the time the cash commodities are sold, the futures position(s) are closed with the purchase of the futures contract(s). Converse of long hedge.

**Speculator**

A market participant who does not own or plan to own a physical commodity, but attempts to profit from price change by entering the market. Speculators assume the price risk for hedgers, who seek to reduce risk. Speculators provide liquidity, and without them the futures market would be extremely volatile.

**Spot month (Nearby)**

The contract month closest to expiration.

**Spreading**

The purchase of a futures contract and the sale of another with the intent to profit from price change. Some examples of spreads are:

**Inter-commodity**

Between two similar commodities, such as the crack spread—buying crude oil and selling gasoline and heating oil futures.

**Inter-market**

Same commodity, different markets. Such as buying Chicago wheat and selling Kansas City wheat.

**Intra-market**

A spread within a market, such as buying March corn and selling May corn.

**Horizontal (calendar) spread**

Buying and selling calls or puts with the same strike price but in different expiration months.

**Vertical (price) spread**

Buying and selling calls or puts in the same expiration month but with different strike prices.

**Stock index futures**

Futures contracts that are based upon stock market indexes such as the S&P 500 or the Dow Jones Industrial Average. These contracts, upon expiration, are settled in cash.

**Stop order**

An order that becomes a market order when a certain price is reached. A buy stop is placed at the intended price level, and is initiated if the market trades or is bid at or above that price. If the market trades or is offered

at or below a sell stop, it becomes a market order to sell. A person might place a stop order to buy or sell a contract in hopes of maximizing profits or minimizing losses.

**Strike price**

The price at which the futures contract underlying a call or put option can be purchased (if a call) or sold (if a put). Also referred to as the exercise price.

**Supply, law of**

The relationship between product supply and its price.

**Support**

A technical trading term used to describe a lower level on a chart in which prices have difficulty penetrating to the down side. The converse of support is resistance.

**Technical market analysis**

The use of historical charts in anticipation of future price movements. Technicians compose charts from data such as historic prices, trading volume, open interest, and more to predict and profit from price trends. There are many methods of technical trading. See also charting.

**Tick**

The smallest allowable increment of price movement for a futures contract.

**Time stamp**

Orders that is placed with a broker that are stamped with the time and date at: (a) the time the broker places the order; (b) the time the order goes to the floor; (c) the time the order is filled; and (d) the time the broker receives confirmation of the fill. This process helps to ensure the validity of each order. The broker also stamps orders that do not receive a fill at the end of the day (unless GTC).

**Trading limit**

The maximum numbers that a customer can hold at any given time. These limits are set by the exchanges or the CFTC. Also referred to as a position limit.

**Up-tick**

A tick up. A tick higher than the previous one, required in securities to sell short.

**Variation margin**

At times of extreme market volatility, additional margin money might be required of traders and must be posted within the specified time frame, or the position(s) will be liquidated.

**Volatility**

The term used to describe a condition in a market where prices are moving rapidly, and in a volatile fashion. The opposite of a liquid market.

**Volume**

The total number of transactions in a day.

**Wire house**

Also referred to as a brokerage house, commission house, or FCM. An individual or organization that solicits or accepts orders to buy or sell futures contracts or options on futures and accepts money or other assets from customers to support such orders.

**Yield**

The return provided on an investment.