Innovations

Evolution of commodity market: effect of Covid-19 era

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Abstract
Evolution of commodity trading can be traced to the agricultural revolution of 8500 BC during which farmers and traders fashioned a means to secure prices of commodities against price fluctuations caused by weather, conflict, demand and supply gap. While the Egyptian Exchange was established in 1861, the Nigerian Commodity Market came on board not until 1990s. Nigeria has been the suppliers of raw materials to Western Europe and prices and conditions of trade dictated by them. The Covid-19 postmortem era has brought in new dimensions in Nigeria commodity marketing with global consequences of demand and supply shock, global energy crisis and US Dollar acceleration and squeeze. Consequently, the functioning system of Nigeria commodity marketing is bound to have several prongs, such as inadequate transport system, storage facilities and support ancilliary base. Hence, it is recommended for rejuvenation of the commodity market in general and agricultural sector in particular.

Key words: *evolution, commodity market, commodity market in practice, Covid-19 era*

"Evolution of Commodity Market: The Nigeria Perspective" unveiled the history of commodity market with special attention to Nigeria. Commodity trading is traced to the agricultural revolution of 8500 BC during which period farmers and traders fashioned a means to secure prices of commodities against price fluctuation caused by weather, conflict, supply and demand gap. Whereas the development and growth of modern commodity market started in 13th century in medieval Europe, trailed to Africa (Egypt) in 1861 and 100 years later (1961), the influence of commodity trading was felt on the shores of Nigeria. At the end of this paper, the reader will appreciate the trajectory of Commodity Market, Types of Commodity Market, Commodity Exchange (COMEX) in Africa, and its perspective in Nigeria with the underlying headings: COMEX in Practice, Institutional Framework, Need for COMEX in Nigeria, Benefits of COMEX in Nigeria and the underlying border-line of Conclusion and Suggestions.

Introduction

The business of commodity market has always been with us, perhaps in the most primitive pattern. In a series of efforts to reduce the risk in commodity prices, the forward pricing was evolved in the old cities of Middle Ease, India and China by the merchants who traded across the continents and also in the trade fairs of medieval Europe. A bill of exchange with the trusteeship of the goldsmith was developed in the medieval Europe and this served as a warrant for commodities to be traded forward in the 13th century.

The organized commodity market started in the United States in the 1850s and in Europe. The spread effect of the market to London "led to the establishment of the Royal Exchange in 1570, Garroways' Coffee House in 1670 and the London Commercial Sales Rooms in 1811"Shahabudin, 1989.

Although Shahabudin (1989) observed that futures market evolved in Europe, the actual futures practices started in Japan with rice traded forward. Agriculture is an occupation of uncertainty as the weather is unpredictable. In order to reduce the price risk inherent, the growers of rice sold their unharvested rice field in futures contract. In doing this, the farmer bore in mind the historical price and the likely price when the rice is delivered in future. Receipts were issued by the rice merchant in respect of the futures contract. This was the beginning of hedging.

Commodity trading can also be traced to the agricultural revolution of 8500 BC. During this period farmers and traders fashioned a means to secure prices of commodities against price fluctuation caused by weather, conflict, supply and demand gap. It was noted that trading evolution, excess supply and the quest of merchants to raise money while commodity was in storage formed the basis for futures agreement. The first recorded commodity futures trades was in the 17th century in Japan, although there was some evidence that rice was traded some 6000 years ago in China. (SEC Nigeria, 2019a).

Receipts were accepted as instrument of of credit between the European merchants and rice market in 1690 in Japan. This gave impetus to the rules governing the market today, such rules being "limited contract terms, standardized contracts, agreement on basic grades, clearing of contracts through clearing house, arbitration, etc" Shahabudin, 1989.

Commodity market is a market of speculation and to aggravate the rule of the game, deliveries of rice in Dojima Rice Market were not allowed and as a result, the spot price of rice off-shot the futures price. The state intervened and deliveries continued until when the market ceased to operate as a result of state intervention in the price of rice.

While the markets in futures were developed in Europe and Japan earlier, in USA it was known as "to arrive". But their system according to Shahabudin (1989), was full of loopholes and faults emanating from lack of standards, the receipts issued were not easily negotiable, unreliable deliveries, varied terms of payments and prices were common knowledge. Although the first coin grain was contracted in 1851, it was only after the establishment of Chicago Board of Trade that standardization of the market took place in 1859.

A commodity exchange market (COMEX) "is an organized market of buyers and sellers of various types of commodities" (Udoh, 1989). The commodities include both raw and processed agricultural produce and non-agricultural products such as minerals – metals, coal, gold and uranium.

Commodity Exchange in Africa

The Egyptian Cotton Exchange was established in 1861 in the city of Alexandra and it became one of the earliest commodity exchanges in the world. It played a key role in global trade, attracting users from the international community including Africa, Asia and the Americas. The exchange closed 100 years later in 1961 with the entry of the government as a player in the cotton trade (SEC Nigeria, 2019a).

As observed by SEC Nigeria (2019a), in a quest to deregulate their economies and open up the financial markets in the 1990s, African governments triggered their withdrawal from commodity trading which led to the establishment of commodity exchanges in a number of African countries with varying degree of success. Further, the African Union Abuja Treaty of 1991 identified the need for an African Commodity Exchange and provided some awareness and push for the set-up of commodity exchanges in the continent at the time. The concept of an African Commodity Exchange became one of the instruments of integration of the continent of African Union (AU). In West Africa, there was an attempt to create a regional exchange for food products following the adoption of Agricultural Policy paper by Heads of State in December 2001.

Types of Commodities Market

Broadly, commodities market can be classified into cash or spot market and the derivatives market (SEC Nigeria, 2019b). In the cash market, transactions are conducted for immediate delivery of physical commodities or securities while in the derivatives market delivery is at a future date (Fig.1). The derivative market is broadly categorized into the forward and futures markts. The futures market trades
in contract of commodities and financial instruments which are for future delivery but customized to the specifications of the transaction parties. They trade over-the-counter and not on an exchange.

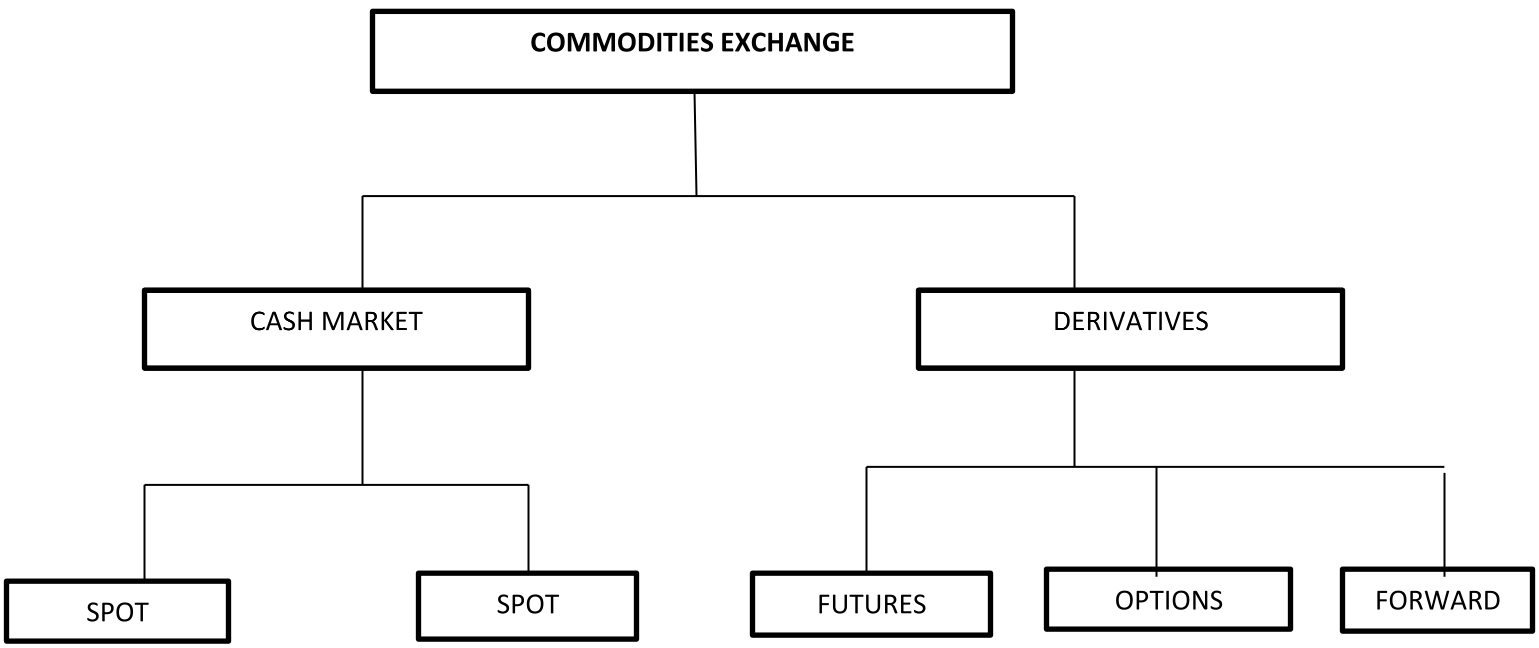

Fig. !: Types of Commodities Market
Source: SEC Nigeria, 2019b

The Nigeria Perspective

In modern sense, commodity exchange is relatively new in Nigeria but is as old as the Nigerian nation. The arrival of white man on the shores of Nigeria boosted trade. The white man for their industries in
England bought raw materials such as palm produce, rubber, cocoa, and groundnut which were not readily available but had been sighted and which were delivered in the future date. No tickets were issued to the buyers but for identification purposes, marks were made on the palm or rubber trees or on the farm as the case may be. The business which was conducted through agents was on verbal trust and was characterized by

lack of generally acceptable measure of value, standardization and establishment of documented ownership in the futures contracts.

In this era of higher productivity, marketing assumes greater importance as an economy becomes increasingly commercialized, leading to urbanization and consequently to urban wage earners. As noted by Issa, Fapojuwo & Bidoli (2011), excess production from the farm must be disposed of in order to earn some income with which the farmer can purchase other goods and services not produced by him. In a higher perspective, commodity exchange becomes necessary as marketing includes all stages of operation which aid the movement of commodities from the farm to the end users, This includes assemblage of goods, storage, transportation processing, grading as well as financing every stage of the operation (Adegeye & Dittoh, 1985).

At independence, Nigeria faired well as an agricultural nation, deriving 70 per cent of its foreign exchange from agriculture and it was food crops sufficient. There were regional marketing boards, such boards being Palm Produce Marketing Board in the East, Cocoa Marketing Board in the West and Groundnut Marketing Board in the North to procure and market these produce overseas. And later there was Rubber Marketing Board in the Mid West.

The disequilibria and maladjustment of macroeconomics of industrialised nations caused global recession in the 70s while the prices of secondary goods were on the high side, prices of primary goods dampened. The recession coupled with neglect of agriculture, worsened the Nigerian economy vis-à-vis the balanxe of payment position. The natural hazards of erosion, drought and insect infestation according to Udoh (1989) disturbed the ecological system which resulted to a further acute commodities shortages and price escalation.

From food surplus to food deficit nation. This is the trend of Nigerian agricultural development. It has a chequered history with years of boom crops being succeeded with years of lean crops often in a more serious and destabilizing intensity despite huge government investment in agriculture. Because of this, observed Udoh (1989), "given the needs of the manufacturing sector on the one hand, and the social and political consequences of a free-wheeling system especially in food production on the other, agriculture must cease to be left to the forces of nature to regulate, but must be brought within the modernizing influences of science and technology that have elevated it else where to the level of predictability".

In the same vein, any such policy mix must be one that must accommodate the secular growth of agriculture, ensure the income of the farmers, surplus food supply and adequate manufacturing inputs as raw materials as well as ensuring "all season-availability of food at prices that will obliterate once for all the off and non-season produce dichotomy" (Udoh, 1989) in Nigeria.

The post independence agricultural policy has always bounced from one development formular to another. In this sector, one can count more than a dozen formulae in the spirit for food sufficiency – Land Army, Price Control and Decontrol, Agricultural Credit Guarantee Scheme, Green Revolution, Rural Infrastructure, Better Life for Rural Women and others. But quite unfortunately that "while a lot of effort has been concentrated on production, the problem of organized marketing has not been given enough attention" Makinde, 1989.

The government at its inception established marketing boards but these marketing boards failed to address the issue of the problems of marketing. They rather served as clearing house for raw materials in respect of British industries in England which dictated the commodity boards prices. The commodity boards have since been abolished, thus leaving the agricultural produce to the fate of laissez faire.

Instead of the market forces to improve the price level, "the current loose system has been found to be more dangerous to the economy of the country in several quarters" observed Makinde, 1989.

As a series of efforts to improve the agricultural performance and increase the standard of living of the citizenry, the government has come yet with another policy of Commodity Exchange (COMEX). But it is argued that the Nigerian problem is not one of policy but one of management. In all sincerity, if COMEX is to be managed as the demised commodity boards, the failure could be more disastrous in the SAP era.

Commodity Market in Practice

The COMEX poses new challenges to financial houses, manufacturers and exporters. These challenges centre on the management and the management is not more than those who participate in the commodity market. Commodity exchange is also known as future market exchange (FME). According to Issa, Fapojuwo & Bidoli (2011), commodity exchange is a market institution which provides physical or virtual venue that brings together buyers and sellers to trade through a group of registered brokers.

Tracey-White (2003)as cited in Issa, Fapojuwo & Bidoli (2011), a corn farmer can sell a future contract on his corn which will not be harvested for several months and guarantees the price he will be paid when he delivers. A breakfast cereal producer buys the contract now and guarantees the price will not go up when it is delivered. This protects the farmer from price drop and the buyer from price rise. Speculators and investors on the other hand, buy and sell the futures contracts in attempt to make profit and provide liquidity to the system. However, according as Tracey-White (2003), due to the leverage provided by the exchange to traders, those participating in commodity futures trading face substantial amounts of speculative risk.

Features of the Commodity Exchange:

Commodity exchange market which deals with agricultural goods is unlike the stock market which deals in intangible goods. Akinyosoye (2005) has highlighted some form of similarities that exist between commodity exchange and the stock market as contained in Issa, Fapojuno & Bidoli (2011):

- They are composed of traders who are authorized to buy and sell futures contracts for the public commission of fee.
- There is a trading floor where buyers and sellers meet.
- There is a governing board or council which sets and enforces the rules for orderly transactions.
- There is a clearing house which facilitates trading and delivery of commodities.
- Exists also is the floor and trading "pits" where actual trading is made.
- f) There is the communications network, which links brokers throughout the world to the traders in the pits.

The commodity trading floor is a physical place which represents a worldwide market. There are many commodity exchanges in the world where over 50 commodities are traded. Importantly, commodity exchanges are located in cities that are major transportation centers and through which substantial portions of the products move. These locations are well connected by modern communications systems (Issa, Fapojuno & Bidoli, 2011).

The Participants

Under the rule, there are a number of recognized participants in COMEX. According to Makinde (1989) such participants are the producers, bankers, commodity exchange market, brokers, jobbers and the end users. In the exchange, there is no direct exchange between the

producer and the end-user. In between is the broker via the jobber. The Commodity Exchange Council (COMEXCON) is the objective arbiter.

The producer (farmer), in order to subscribe to the exchange market must be a big-time farmer and he must solicit for the services of experts and even if the farmer is a trained agriculturist, "he must employ a farm manager and pay for professional services of a management team which include agronomy, farm accounting, standard management, soil tests, post production management and marketing" Makinde, 1989. Though these services are optional, they are necessary for any successful agriculturist.

For COMEX, the agriculturist needs some large sum of money. Every commercial bank in Nigeria is mandated to give at least 15% of its portfolio to agriculture and the Nigerian Agricultural and Cooperative Bank has credit cell known as Agricultural Credit Guarantee Scheme Fund (ACGSF). The exchange market is conducted according to the set rules and regulations of the Commodity Exchang Council._All the participants are professionals, hence, they operate within the bounds of the rules and the regulations. Some of the function of the Council are (Makinde, 1989): price regulation, evaluation, monitoring, corporate image making, export promotion, information and data management, counseling and research and market development.

Unlike the open market, sales and purchases in COMEX must be conducted through a broker. The broker is an expert and he occupies a special position in the market. Auxilliary to brokers are the jobbers who are knowledgeable men in their cognate area of commodities in both agriculture and other commodities. The brokers, jobbers and others must be accredited by the COMEX after meeting all the accreditation requirements and fulfilling the COMEX rules and regulations.

There are two sets of users – the industries sourcing for raw materials and the merchants, purchasing for futures market. In recent times, since the inception of structural adjustment program (SAP), some industries have backward integration, having their own field and process base, commodity examination and valuation. The understanding of the tools used in COMEX will be be useful in this regard.

Mechanics of COMEX

Although the buyers and sellers may be experts in their own particular lines, they are likely to be amateurs on the commodity exchange. Transactions in the market are either spot or forward or futures. In spot transaction, cash is paid and delivery is also made. No risk ia involved. But in others, there are risk transferring mechanisms known as forward and futures contracts. While the forward contract is the delivery of the specified commodity in some later date at fixed price, futures market permits trading in various grades of commodity to protect hedger sellers from being cheated by speculator buyers who may insist on the delivery of a particular grade in small quantity (Lall,1982). The risk may be avoided through the process of hedging.

Hedging

Hedging is motivated by the desire to reduce risk. There are two categories of hedgers in the futures markets – the short hedger and the long hedger. The short hedger purchases commodities in the cash market and simultaneously sell the same in the futures market. In other words, he is long (buy) in the spot market and short (sell) in the futures market. The actual practice is that as soon as the short hedger purchases cash, he simultaneously sells forward and repurchases futures contracts. In this way , he hedges the prevailing futures price (Akinyosoye, 1989).

Long hedges deliver a specific quantity of a commodity at a later date at a price – and who do not now have the stocks to fulfill his commitments. The hedger in this respect hedges against the risk of price rise for fulfilling the contract. There are also speculators in COMEX who anticipate to profit from future price market. While speculator is interested in making profit when he is not prepared to take or make delivery, the hedger makes profits, takes and makes delivery.

Institutional Framework

For a workable COMEX , there is every need for a strong in-built institutional framework. Since SAP, the government is re-accessing its role in the economy. From its policies so far, it is obvious that it has a role reversal between itself and the private sector. It restricts its activities (President Babangida, 1989) to the traditional role of providing infrastructure, social amenities and regulations whereas Nigerians must use the infrastructure and social amenities to, within the policy framework develop an economy in which everybody can achieve his maximum potential.

Policy Framework

The experience of government in business in this country is one of disappointment, hence the role of government in COMEX is regulatory and advisory: establishing COMEX by law; setting up a commodity exchange council (COMEXCO) as the apex regulatory body; providing adequate food buffer stocks independent of COMEX; providing credit lines to private sector for infrastructure such as rail/truck transportation; storage facilities; grain silos, and other backward linkages.

Transport Network

There must be readily available registered transporters for adequate movement of commodities. It is expected that storage technology can be developed provided the market is large enough for the transport division of the COMEX which must be subscribers of equity.

Strong Manufacturing Base

A strong manufacturing base is a sine quo non for a commodity exchange market. Since they are the purchasers of the raw materials, they are on the other hand, the providers of fund. With the price of raw materials for future deliveries confirmed prior to production, long-term planning and investment in plant equipment can be made.

Roles of Insurance Companies and Banks

The insurance companies are in position to render services, such as farm, burglary abd fire policies. They should also be in the business of hedging farm produce by buying and selling in both cash and futures markets. The roles of banks are eminent. Inasmuch as they provide funds for most of the transactions, they are expected to establish brokers' cell in their major branches and all transactions must be submitted on behalf of the customers by brokers. The cell will serve as a pool of resources of buyers and sellers in both cash and futures markets.

Communication

Lack of market information system inhibits marketing. For efficient COMEX, a good sum of investment is needed in both communication system and computer, hard and softwares.

This is because the participants in COMEX need up to date information on the movement of prices and adequate data on commodities via standardization, quantity and quality.

Food Industry

While the food processors buy their raw material from the market, the processors of cash crops such as vegetable oils, and cocoa beans and butter will be the suppliers of contracts into the market. The futures contracts for yam, wheat and corn flour and fruit juice will help to boost the market for food processors.

Covid-19 Postmortem Effect in Nigeria

Covid-19 ushered in orchestrated slowdown of the economy through the burden of high inflation, tighter commodity and financial market conditions, US Dollar strength, supply chain pressures and pressure from central bank pivot (The Orchestrated Slowdown, 2022).

In the sequential supply-side shocks, it is eminent that global markets have accelerated into a fundamentally new macro super-cycle of Covid-19 following three sequential shocks to the global

economy and policy regime in recent years. This new macro and geopolitical landscape is fundamentally less stable, less predictable and more inflationary. These are practically visible in Nigeria commodity market as well as the financial market. Suffice it to say that in 2020, global Covid-19 crisis infested demand shock and supply shock whereas in 2022 as a carryover of Russia-Ukrain crisis, global energy crisis and US Dollar acceleration and squeeze intensified. The degree of disruption of Covid-19 can be imagined from Table 1: The New Macro Supercycle (The Orchestrated Slowdown, 2022).

Table 1: The New Macro Supercycle

From	To…
The Great, Moderation	The Great Instability
Lower rates, Volatility suppression	Higher rates and structural volatility
Secular Stagnation	Secular reflation
Surplus global production capacity	Global Labor shortages
Deficient aggregate demand	Disruption in global supply
Monetary and Fiscal	Monetary and fiscal tightening
Currency wars (‘’race to the bottom’’)	“Reverse” currency wars
Lighter government regulation and free trade	Increased government activism & policy intervention

Source: The Orchestrated Slowdown, 2022.

We have remained suppliers of raw material to Western countries. In the past and even now, they have always dictated prices of these commodities. Observed Ndubuisi (1989), while prices of imported goods are on the increase, the prices of primary produce have dampened and this has caused macroeconomic disequilibrian in the developing countries. Writes Udoh (1989), "Our competitive advantage in today's competitive world seems to be agriculture and raw materials".

However, he concludes "because of the excessive manipulation of the forces of demand and supply by more established commodity and foreign exchange markets, we have watched helplessly as the producer prices of our commodities, minerals and raw materials continue to lose value precipitously thereby continuing to force on us a lower standard of living" and loss of purchasing power. This alone is a strong case to establish a COMEX.

Monetary Instrument: Just as the policies on foreign market is used by the central bank to equilibrate the economy, the same instrument can be used in commodity exchange for the good health of the economy. But in so doing, the following objectives must be born in mind (Udoh, 1989):

- The market for internal food crops must be inward looking for the betterment of the people.
- The buffer stock system of the commodity exchange clearing Banks (CECB) must be a major policy instrument used for equitable distribution of prices and goods.
- Government grain reserves and the buffer stocks must be used to ensure that producer prices are more than the production costs..
- The structure of the market should ensure nation wide coverage with Nigerian owned commodity broker companies.
- Such markets in Lagos, (Aba) and Kano should be export zones and businesses conducted in foreign currencies.
- Economic Community of West African States (ECOWAS) and the environs are potential markets and they should be encouraged to come in using Camerron, Ghana and Cote d'Ivoire as delivery points for cocoa.

Benefits of Commodity Exchange

According to Makinde (1989) the benefits of commodity exchange are important to the economy. Some of them are:

- They promote economic growth by fostering the development of both soft and hard commodities to industry by efficiently linking commodities to industry which could improve industrial output and profitability. A thriving commodities trading can facilitate industrialization of the economy and improve tax revenue.
- They create employment and raise the living standard of the farming community as opportunities are provided for better access to marketing, access to market price and other important information.
- They can serve as platform for small holder farmers to be brought into the financial succor as they are exposed to financial services such as bank deposit and credit facilities, thereby fostering the much needed financial inclusion.
- They engender economic **diversification**. This is more so for an economy like Nigeria which is branded as a mono product economy for foreign exchange earnings. For an agrarian economy like Nigeria, with sound mineral deposits, developing the commodities market remains a potent way to diversify the economy and increase the tax base.
- They improve the attractiveness of agribusiness and foster agricultural production as farmers and end users benefit from the use of the exchange
- As platform **and** transparent pricing mechanism is provided for trading solid minerals, activities in the sector could go up and more investment attracted with multiplier effect on the economy.

- They provide rules and regulations which bring about order to the market. This in turn forces and encourages producers including the farmers and traders to meet the ethical and quality standards of the market. By efficiently linking buyers and sellers in sufficient number, commodity exchanges create liquidity and facilitate price stability which aids decisions and trades.
- Through grading and standardization of commodities, commodity exchange promotes high standards of quality thereby boosting export as confidence is strengthened in the quality of commodities exported through the exchange.
- They provide a ready market for the sale of commodities and incentivize the use of storage facilities, such as warehousing which helps to minimize post-harvest losses.
- By efficiently linking buyes ans sellers in sufficient number, commodity exchange creates liquidity and facilitates price discovery which further boosts commodity trading. Market information such as price, quantity and quality are regularly made available to facilitate exchange efficiently and effectively.

Other Benefits of Commpdity Market

Other benefits of commodity exchange accrued to the Nigerian economy according to SEC Nigeria (2019b are):

- Through the provision of price and other information transparency as well as better access to market, they reduce the exploitation of small holders farmers by intermediaries. This enhances values to farmers, improves their well-being and encourages farming activities.
- Commodity exchanges provide risk management tools, enabling hedge against possible adverse development in the future prices of commodities. Such facilities help industries plan by providing against adverse price fluctuations .price and supply certainties. Farmers use the market to hedge their commodities
- They promote agricultural produce financing and development of warehouse receipts which enables farmers of all categories borrow against the commodities in the warehouse.
- Commodity exchange provides price benchmark for non-xchange traded markets such as the over-the-counter (OTC) market.
- Through the use of warehousing, commodity exchange helps to ensure continuous supply of commodities regardless of the season. This guarantees raw materials for the industry at all times, reducing risk of production disruption as well as storage and production costs.
- Commodity exchanges can also assist in moderating consumer price because of their ability to drive up agricultural production.
- Commodity exchange provides opportunity for regularization of commodities through the warehouse receipt system which can also be used as collateral to unlock finance from financial institutions.
- The commodity exchanges provide opportunities for investment in the commodities value chain such as warehousing, brokerage and logistics.
- They promote the development of derivative markets as derivative instruments are developed with the attendant benefits such as permitting farmers and others to hedge their farm products.
- And finally, a thriving commodity exchange market can contribute to moderating and reducing illegal mining of solid mineral products as the exchange tracks and records the origin (source) of all commodities traded on its platform.

Conclusion and Suggestion

The medieval Europe had the trace of futures market in the 13th century. With all vagaries along the way, it was only in 1880 that the Sugar Market came to be in London as a Terminal Market. The forward market which started with rice market was developed in Japan and the market ceased to operate when rice became a controlled item in Japan. The first forward contract which was dated March 13, 1851 in USA came to a perfect market only in 1859. The Nigerian commodity market is on the experimental stage. It is to the laissez faire and with moderate regulatory devices, it will be a success having having experienced the trajectory of Covid-19.

Commodity market is an innovation in the Nigerian economic system. In its functioning system, it is bound to be subject to several prongs. One of such prongs is lack of infrastructure such as storage facilities, adequate transport system, support anciliary base, standardization and measures, communication, trained manpower and regulatory framework.

On the whole, the need for commodity market should not be overemphasized. Tracing the chequered history of agriculture, the several government policies and the activities of the buyer cartels in Europe, there is every need to rejuvenate the commodity market in general and the agricultural sector in particular in Nigeria.

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