Mercantile Exchange Nepal Limited
Invest - Trade - Earn
AN ISO 9001:2008 CERTIFIED EXCHANGE

MEX EXPRESS

A Smart Solution for Online Trading

www.mexnepal.com

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Message from Managing Director

Derivatives are subject to regulation which provides a safer environment for all market participations. *Regulations in broader term contain the following aspects:*

1. Proper agreement with adequate Risk Disclosure

2. Exchange Rules & Bye-laws

3. Government regulation

From MEX's side; to protect the market from any wrong doings; risk disclosure documents, agreements, AML policy and Exchange rules & bye-laws have been put into practice. Time and again we are urging government to regulate the futures market and consider the activities of market participants so as to protect the market integrity.

Government regulation brings uniformity in process of price discovery, clearing & settlement basics, taxation, permitted commodities market operation module, dispute settlement method posing an obligation among the stakeholders to act within certain boundary. Regulation of futures market is the need of an hour which helps to form a disciplined market. Only Commodity Exchange Act can address the process of conversion of consumption assets to investment assets.

Commodities Exchange is an exchange which ensures that each and every transaction is done accurately. For that purpose it has implemented the process of documentation, trading, clearing & settlement modules too. Settlement either through cash or physical delivery is imperative and needs to be addressed accordingly.

Overall exchange has to set a benchmark for pricing of commodities. By establishing the benchmark in pricing, an Exchange can serve the economic objectives as well.

In this scenario along with mushrooming investment in futures, antagonists who think of this market as an unattractive investment are also escalating. We should not leave any room for outsiders to complain as they are harming the overall objectives of the market. So, to protect market integrity we urge government to take necessary steps and come up with a regulatory body designed separately for the futures market.

- Dipendra Khatiwada

Warehouse Receipt Financing: A System to enhance agricultural-trade

Introduction to Warehouse Receipt

Warehouse receipts has been recognized as an important tool to provide the agricultural sector with increased flexibility in marketing decisions and also as a mechanism to obtain financing for farm operations. A warehouse receipt is a certification of legal ownership of a particular commodity that is stored in a specified location and is of a specified quality and condition, such that when the commodity is sold, the buyer can have the comfort, without physical inspection, that the product they have purchased will be available to them when required, in the condition outlined on the warehouse receipt. Warehouse receipts are practiced to provide benefits to smallholder farmers to enhance their participation in the broader market for agricultural products. Warehouse receipts are also an integral part of agricultural commodity exchanges as they allow trade to take place with "paper or receipts" rather than the physical commodity.

Concept of Warehouse Receipt Financing

Nepalese economy is largely based on agriculture. The agriculture sector contributes about 32 percent of the gross domestic product (GDP) employing over 66 percent of population. Therefore agriculture has always been considered as a backbone of Nepalese economy. However, the level of income in Nepal, especially in agriculture sector is very low by international standards. Agro trade in Nepal is usually done on the basis of visual inspection because there is lack of any system of grading and standardization of products. Therefore, small-scale farmers, who produce maximum percentage of Nepal's output, come to market with little information and unable to negotiate for better prices.

Now the time has come to form a system that coordinates better, links faster, which protects the interest of both sides of the trade. It is time for a sophisticated warehouse system to come into practice that will take Nepalese agriculture into the new Millennium. Moreover, practice of warehouse system as well as warehouse receipt will represent a new way of doing Traditional business, bringing global standards of efficiency and reliability to the old age of domestic agricultural trade. Warehouse system, will increase Nation's agricultural commodities share in trading. In the process of deposit of traded commodities in warehouse, firstly commodities will be sampled, weighed and graded using state-of-the-art technology equipment. Then the depositors will be provided with warehouse receipt issued

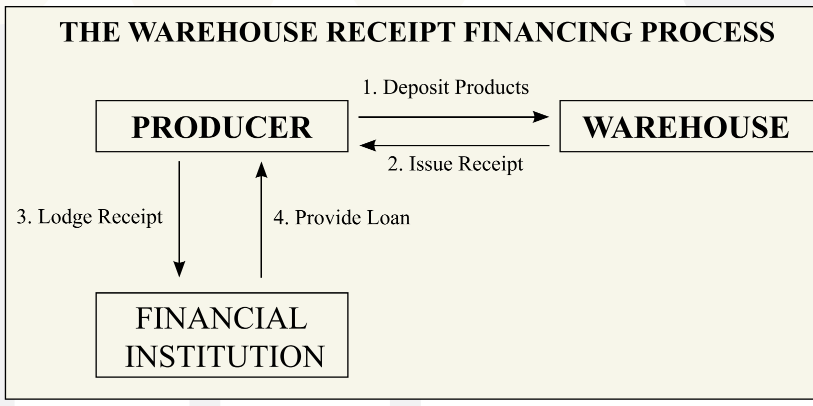
by warehouse operator followed by certification provided by government body in order to establish legal title to the deposited commodity.

Warehouse receipts provide an essential addition to the store of negotiable instruments in a country's financial sector. They can be especially useful in developing and transition of economies where new market instruments need to be created. Warehouse receipts are negotiable instruments backed by the underlying commodities, and also an integral part of the financial systems of most developed countries. The overall efficiency of markets, particularly in the agribusiness sector, is greatly enhanced when producers and commercial entities can convert inventories of agricultural raw materials or intermediary or finished products into a readily tradable device. Since warehouse receipts are negotiable instruments, they can be traded, sold, used as collateral to support borrowing, or accepted for delivery against a derivative instrument such as a futures contract in commodity exchange.

the financial institution, the producer (or farmer), and the warehouse. The farmer identifies a warehouse and takes his or her goods to the warehouse for deposit. The warehouse operator grades and classifies the goods and gives a receipt for storage of said goods to the farmer. The farmer then takes the receipt to the bank and, based on projections of the goods' market value, the bank gives the farmer a loan. The loan allows the farmer to spend it to finance expansion activities, pay off debts, or use it for any other reason. Warehouses can be either open to the farmer, allowing the farmer to withdraw produce at any time, or sealed, so the farmer cannot access produce until a predetermined date. If the produce is withdrawn, the farmer must repay the bank for the loan i.e. principal and interest and also any storage fees to the warehouse operator. Alternatively, the farmer may use the warehouse as a channel for selling the goods, in which case the goods are released to the buyer, the loan and fees are deducted from the selling price, and any remaining profits are released to the farmer.

Benefits of Warehouse Receipt

The warehouse receipt financing provides large benefits to various sectors. The practice of this system provides liquidity to the farmers as they can use it as collateral for taking loan. The farmers also get rewards from quality and grading of their products. It can help farmers for development of other productivity-enhancing agricultural services. The system will help for more efficient supply



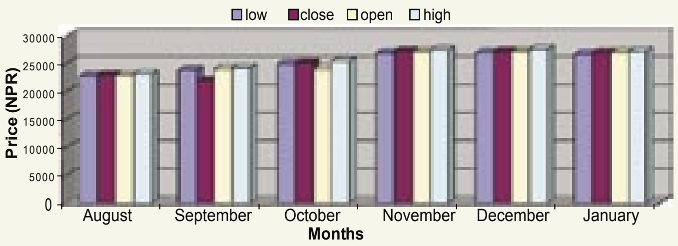
Warehouse receipt financing is the use of securely stored goods as collateral for loan. In this process the producer deposits a finished good or agricultural product in a warehouse where the producer receives a receipt certifying the deposit of goods of a particular quantity, quality, and grade. The farmer can use the receipt as a form of portable collateral to request a loan from a financial institution.

There are typically three parties involved in warehouse receipt financing:

chains of agricultural commodities. Many agricultural stakeholders can use it for better price-risk management. All this will result in higher returns to farmers, better service to consumers (involving lower prices, better quality and greater variety) and macro-economic benefits through a more healthy trade balance in agricultural commodities.

Indra Kasula
Assistant Manager
Research & Development Department

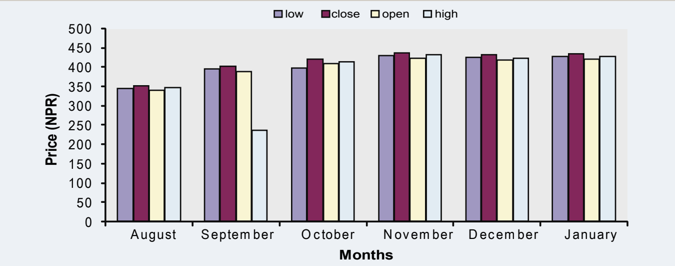
Gold Chart



Gold Data

Months	Low	Close	Open	High
August	22,780.01	22,937.35	22,953.87	23,118.56
September	23,871.60	21,853.12	24,040.41	24,261.25
October	24,978.01	25,211.23	24,073.89	25,381.79
November	26,936.80	27,279.13	27,240.56	27,418.11
December	26,950.04	27,203.31	27,298.29	27,559.88
January	26,715.21	26,952.60	26,979.23	27,193.84

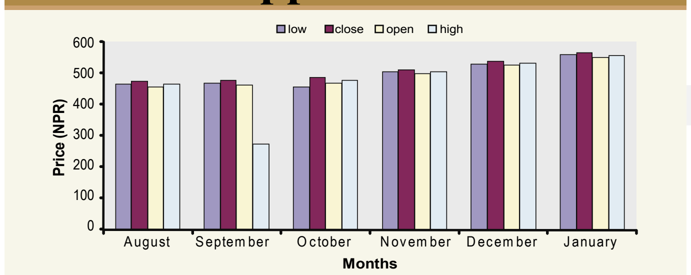
Silver Chart



Silver Data

Months	Open	High	Low	Close
August	346.17	352.57	340.95	346.89
September	395.92	403.48	390.02	338.47
October	398.23	422.38	409.41	415.79
November	430.22	437.52	424.76	432.4
December	426.57	432.18	419.72	424.85
January	429.57	435.47	422.62	428.77

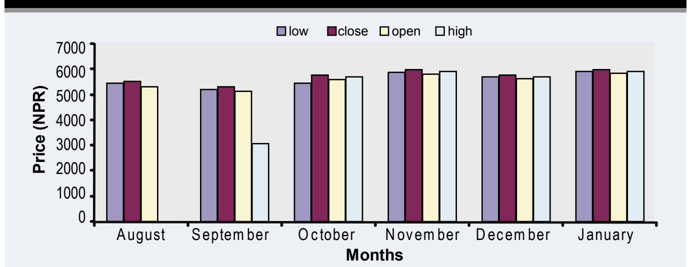
Copper Chart



Copper Data

Months	Open	High	Low	Close
August	462.81	472.97	455.63	465.10
September	466.91	475.17	459.78	273.46
October	454.52	484.11	467.29	476.75
November	501.95	509.93	496.99	503.57
December	528.21	535.04	524.00	529.82
January	556.59	564.92	547.74	554.41

Crude Oil Chart



Crude Oil Data

Months	Open	High	Low	Close
August	5428.54	5515.43	5319.18	5421.78
September	5198.39	5291.62	5110.82	3068.13
October	5438.15	5776.29	5593.57	5699.01
November	5882.04	5981.82	5794.65	5886.53
December	5676.34	5762.28	5612.89	5682.07
January	5920.95	5976.30	5830.88	5892.07

Know your Commodities

Gold Futures Contracts

Commodity Symbol	: GOL
Exchange	: MEX
Trading Hours	: 4:15 AM-2:45 AM
Contract Size	: 1 Kg (Regular) 200 Grams (Mini)
Contract Months	: FEB, APR, JUN AUG, OCT, DEC
Price Quote	: NPR/10 grams
Tick Value	: 241 (Regular) 48.2(mini)
Quality specification	: Refined Gold .995 fineness

Gold Futures

Gold has long been prized for its beauty, resistance to chemical attack, and workability. Since it occurs as a native metal, it has a relatively low melting point, and is malleable; early man easily separated it from rock and cast or hammered it into beautiful designs. Gold is used in jewelry, scientific apparatus, dentistry, and photographic processes. The ever-growing demand for jewelry and the rareness of gold hence determined its price. In return, the high price made gold an ideal store of wealth.

Two major influences on the gold prices are the major financial upheavals and inflation fears. Financial crisis tends to be a major reason for the increase in gold prices. A case in point being the Dubai World crisis that happened in November, 2009. In the last week of November, the Dubai government announced it was planning to ask creditors to freeze repayment of debt worth billions of dollars of two of its flagship firms - Dubai World and real estate developer Nakheel. It has USD 60 billion in liabilities and will seek a six-month standstill on its debts with all lenders. The news shocked global markets. The debt, though not major, has shocked investor sentiment that had taken the oil-exporting Gulf region to be a safe haven during the financial crisis. The immediate effect was for investors to shun risk and flee to safety. That benefited the U.S. dollar and U.S. government debt, which suddenly became very attractive amid all the turmoil. This in turn affected the immediate demand for gold and it's price level.

The second is the influence of inflation. In times of high inflation, wealthy investors tend to flee to the gold as a safe haven asset. However, this influence has been reduced due to the management of gold prices by the central banks. Gold prices and USD tend to move in opposite direction. This negative correlation isn't perfect but tends to hold over longer periods of time.

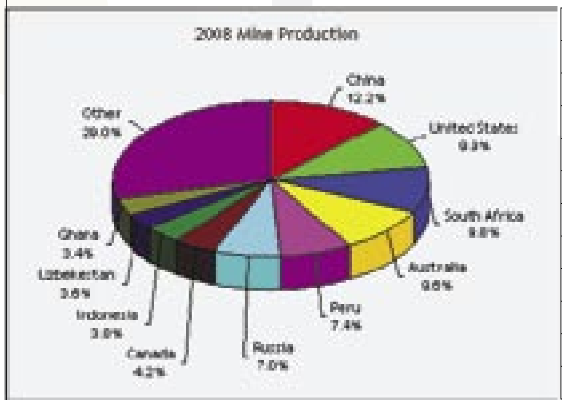
Some quick facts about gold:

• In 1980, gold reached $800 per ounce, the all-time highest market value for gold. Adjusted for inflation, this would be more than $2200 per ounce today.

• For several decades, the United States government made it illegal to own gold bullion. This was initiated by President Roosevelt in 1933 to fight severe deflation and the ban lasted till President Nixon lifted it in 1972.

• South Africa has been a major gold producer since 1880s and it is estimated that about 50% of all gold ever produced has come from this nation. While, during the early 1980's it produced about 1000 tonnes, the output in 2007 dropped to just 272 tonnes.

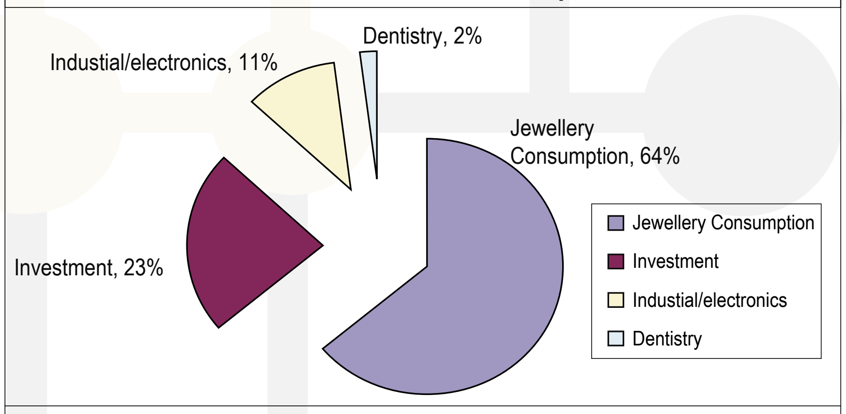
Total Gold Production



China	288 mt
United States	234 mt
South Africa	232 mt
Australia	225 mt
Peru	175 mt
Russia	163.9 mt
Canada	100 mt
Indonesia	90 mt
Uzbekistan	85 mt
Ghana	81 mt
Other	660 mt
Total	2356 mt

Total Annual Production of Gold in 2008.
Source: http://www.goldsheetlinks.com/production.html

Breakdown of Gold Consumption



Source: http://www.goldsheetlinks.com/production.html

• The United States is credited with having the largest holdings of gold. According to a recent estimate (Dec 2009), it has 8,133.5 tons of gold.

Gold is primarily used for making jewellery and is a significant consumption area. Investment forms the second bigger consumption area followed by use in industrial and electronics and then dentistry.

Factors influencing gold prices:

Demand and supply

As with other commodities, demand and supply affects the price of gold. During the wedding season in India and the Chinese New Year, two of the world's top gold consuming nations, the demand for gold increases. This in turn increases the price of gold.

State of the American economy, world economy

The state of the American economy, the world's biggest economy as well as the state of the world economy also affects gold. Interest rates of a country, particularly, interest rate policy of USA as well as ECB (European Central Bank) monetary policy affects their respective currencies which in turn affects the price of gold.

Major announcements:

Major announcements by big international organizations also affect the price of gold. Recent examples being the announcement of IMF (International Monetary Fund) to sell its reserve gold holdings and the subsequent announcement by Reserve Bank of India to purchase some of that excess holdings.

Conclusion:

Gold is a popular investment option and a very volatile market. Because of its volatility, good income can be generated as well. However, the reverse is also true that one can suffer significant losses because of this volatility. Thus, an investor needs to study the market carefully taking into account, the various factors that can affect gold like announcements, seasonal trends etc.

Controlling Risk Exposure

One of the important elements of commodity futures trading is to have the discipline to exit losing trades. Many novice traders in Nepal have fallen into the trap of holding on to their positions for too long in a trade, hopefully anticipating for a market trend reversal. However, this does not happen and they end up spiraling deeper and deeper into greater losses. Eventually they have no choice but to exit the market with a huge portion of their capital being wiped out.

This would not have occurred if they had implemented risk control strategies typical of experienced commodity futures traders. Appropriate stop losses should be calculated and put into place at the point when the trade is initiated. Evidently, stop losses are part of a trading plan. Once a stop loss is hit, traders exit their trades with minimal or acceptable losses, and subsequently move on to the next trade. The trader should be well aware of his risk tolerance levels when he enters a trade. He must understand that not all of his trades will turn out favorably, and that there is a probability for winning and losing each time.

Subsequently, the next question now would be, how would a trader identify the right stop losses to

place? The trader should utilize technical analysis methods to pinpoint technical barriers which are great locations to place stops. However, he should be careful against placing stops within a trading range, support and resistance, as this will result in being stopped out prematurely. Thus, it is strongly advisable to place stop losses beyond the trading range.

There are instances where a large number of commodity futures traders identify the same stop loss points. But there are also instances when that different sources of information may calculate different trading ranges. In these cases, it may be a good idea to identify stops at different locations by adopting different methods of analysis.

Another aspect of commodity futures trading would be the maximum percentage of capital that a trader should risk in each trade. The general contention in international practice is that a trader should not risk more than 5% of his capital in each of his trades. In fact, 1% to 2% would be preferable risk levels for each trade. Any percentage higher than this will result in relatively huge losses when a trade goes wrong. In these circumstances, a trader could get wiped out in no time if he is on a losing streak. Thus, with a lower risk level, a trader would still have adequate capital to make a comeback should his trades turn out to be losses.

Finally, any commodity futures trader should analyze his past losses to determine the causes of failure. This way, he shall be able to learn from his mistakes and avoid making repeating them again. At times, traders who have been suffering from a losing streak should take a break from trading in order to regain their emotional stance before going into the market again.

SR Bajracharya
Director
Futures Fortune Pvt. Ltd.
MEX Membership Code: 28

Nepal's Commodity Futures Market: Prospects & Challenges

Dr. Manoj Shahi, CFA

Nepal entered the world of organized automated commodities futures trading with the start of Mercantile Exchange Nepal Limited (MEX) operations from January 2009. Within a span of 12 months, MEX has been able to clear trades whose average daily traded value in the month of December 2009 was about 9 times greater than Nepal's Stock Exchange. Despite this achievement, Nepal's automated futures market is at its infancy whose growth and sustainability will require concentrated efforts by concerned stakeholders to give it positive momentum.

The current state of Nepal's commodity futures market is characterized by trading of cash-settled futures contracts on global-based commodities by speculative investors in an unregulated environment. There is no organized spot exchange, no physical delivery of traded commodities, no participation by true economic users, and no regulatory oversight whatsoever. Why the government has been moot in regulating a market which has grown to be 9 times the size of the domestic stock exchange in such a short period of time is a question probably they can only answer. Currently speculative investors in Nepal's market are accruing the benefits of a bull market but should markets suddenly turn south causing some investors to get badly burned, it may create a negative image on the commodity futures market as a whole which may be difficult to shake off thereby damaging its growth prospects. Steps must be taken immediately to better manage and regulate this market so that it can provide positive impetus to the growth of the underlying commodity markets and thereby the development aspirations of the country.

The last few years have seen a tremendous growth in the volume of contracts traded in global commodity exchange markets reaching 1,871 million contracts in 2008 compared to only 712 million contracts in 2004. The share of commodities trading in organized exchanges has grown from 8% in 2004 to 10.6% in 2008 when 17.6 billion futures and options contracts were traded. Asia has been a key growth market for futures especially those related to agriculture commodities. In 2008, Chinese exchanges accounted for seven of the top ten agro-based commodity contracts traded worldwide in terms of volume.

Commodity futures markets exist in most countries because they serve a specific purpose in the economy. Futures markets provide three key benefits. First they help in the price discovery mechanism of underlying commodities. Second they provide instruments than can be used to manage the price exposure of underlying commodities. Third they permit investors to use commodities as an asset class to diversify their investment portfolios.

By creating benchmark contracts on high-volume physically traded commodities which are quoted and settled on a daily basis by buyers and sellers, futures markets take the pricing power away from scrupulous traders and give more transparency to the whole pricing mechanism. Like commodities are then priced off the benchmarks giving more structure to the broader underlying markets. End users (farmers, wholesalers, manufactures, processors, retail consumers, and others) can use these benchmark prices to manage their own operations providing support to the commodity market as a whole.

In the absence of commodity futures markets, end users are limited in the tools available to them to manage the price exposure of the commodities their livelihoods depend on. The farmer may be able to sell his crop forward to a physical trader but the benefits may accrue to the trader rather than the farmer due to the non-transparency of where the price will be at the time of the harvest. With futures market, the farmer has a better idea of the path the price will take based on which he can deal with the physical trader. Alternately he can use the market itself to lock in the price now for delivery or settlement during harvest time. Similarly other end-users such as processors who need to purchase the commodity can use the markets to hedge their price exposure. These hedging and price risk management options that futures market provide allow end-users to worry less on where the prices will be and concentrate more on their core operations generating greater efficiency.

For investors, whether they are retail or institutional, commodity futures provide a vehicle whereby they can allocate some of their funds to investment in commodities. Commodities have little correlation with other asset classes such as stocks and bonds, thereby allowing investors to gain greater return for the same level of risk. Commodities as an asset class like real-estate provide a mechanism whereby investors can hedge against inflation risk.

Besides bringing more structure to the underlying commodity markets, futures markets also help in integrating the physical market to the financial market. Through the use, trading and financing of warehouse receipts written against stored commodities in regulated warehouses, users can bring liquidity in the physical commodity market that would otherwise not be possible. In addition, the exchanges can help bring in needed revenues to the government through capital gains tax similar to that used in other financial markets.

It is clear that well organized futures commodity markets can play a significant role in the overall development of a country's economy. For Nepal, given the two-year history and looking at how commodity markets have prospered in other countries, the prospects for the growth of commodity futures market looks good. The challenge is to maintain the positive momentum by creating a viable and sustainable spot market with physical delivery on commodities more closely aligned with the needs of the domestic

MEX Highlights

Expedient Securities Pvt. Ltd, MD. Mr Kanhaiya Ghiraiya being awared for Best NCM in Quality Services to the clients category

Futures Fortune Pvt. Ltd. Director, Mr. Shashi Raj Bajracharya being awarded for Best NCM in Compliance Category

Morning Star Investment Services Pvt. Ltd. MD, Joseph Adhikari being Awarded the for Best NCM contributing for the growth & development of futures market

Unicorn Investment Pvt. Ltd. Director, Amit Agrawal being awarded for Best NCM in Emerging NCM category

Article of Manoj shahi contd…

market, a prerequisite for the better function of derivative markets. The market faces some serious bottlenecks in achieving this goal. These include a legal regulatory vacuum; under-invested enabling infrastructure including roads, energy, irrigation, and warehouses; lack of skilled human resource; and lack of general awareness by users on the merits of using organized exchanges.

So what can various stakeholders do to help this fledgling market gain positive momentum? Obviously, the government has a strong role to play.

In many countries such as Kenya and Thailand, governments have played a very pro-active role in establishing commodity exchanges. Here in Nepal, there is an urgent need to provide a regulatory framework for the market. We have the benefit of looking at other countries and adopting best practices. There is an immediate need for a commodities act and the establishment of a regulator. Different countries have different modalities and there is no right or wrong modality. In China, the same regulator provides oversight to both the stock and futures market whereas in India, there is a separate commission that provides oversight to the futures market. Whatever modality we choose the regulator must have the necessary resources and power to regulate the market. Some of the key issues the regulatory framework needs to address are (a) the appointment of a regular, (b) the requirements for opening of exchanges including the number of exchanges to permit operations, (c) requirements for being market makers including the role of financial institutions, (d) what standardized commodities to permit trading, (e) disclosure requirements for exchanges and market makers, (f) anti-money laundering and code of conduct to prevent unethical trading practices, and (g) the use of Indian exchanges by market-makers to off set exposures not able to be managed by local exchanges.

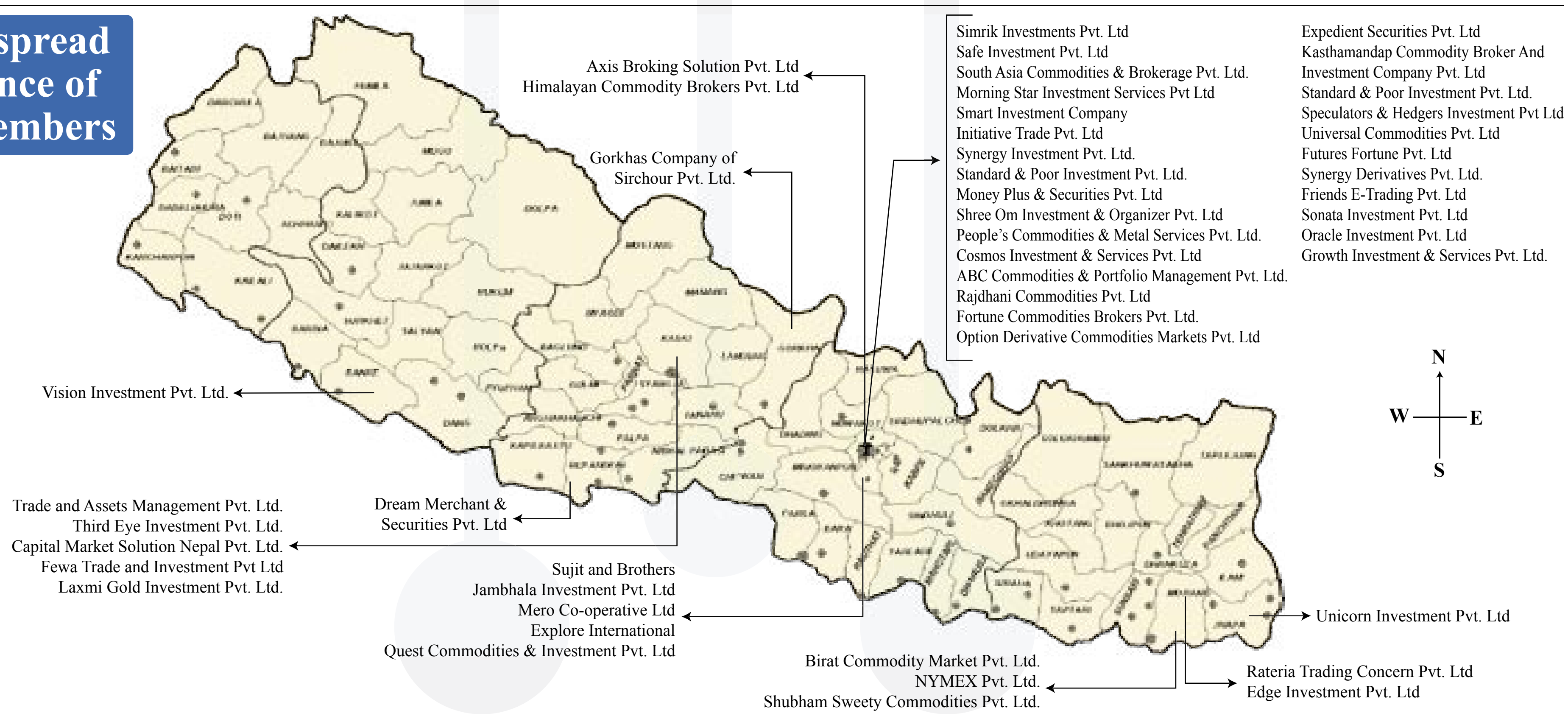
The government can provide significant boost to the commodity market by further investing in enabling infrastructure that promotes the growth of underlying commodities market. These include investments in energy, irrigation, transportation and warehousing infrastructure that have a direct impact on the manufacture, movement and storage of commodities. In the short term, the government can help facilitate storage of commodities by enabling the use of its existing warehousing facilities at affiliated organizations such as the Nepal Food Corporation, National Trading Limited and Salt Trading Limited. Some of these investments in enabling infrastructure could be done in public/private partnership modalities which the government seems to be keen on promoting. Other important roles, the government can play are setting standards for commodities, providing incentives for investment in agriculture and other commodities, and educating the general population on the merits of using commodities exchanges.

Exchanges such as MEX can take additional steps to provide more backbone to the commodity futures market. They need to introduce commodity futures contract more tailored to the domestic needs of the economy with particular emphasis in agriculture commodities with physical delivery so true economic players can benefit from the exchanges. This will require exchanges to be thorough on their research and involve all participants in the value chain of the commodities being considered for listing. Exchanges also need to be pro-active in (a) educating potential users of the merits of using the contracts offered in their exchanges, (b) creating a strong self-regulatory environment including the establishment of a proper code of conduct for market participants and a proper dispute resolution mechanism with enforcement capabilities to build trust in the market, (c) creating more transparency on the trading operations of their contracts, (d) providing better price discovery process both on the spot and futures market through robust collection and dissemination of price information, (e) taking steps to ensure they have a strong and skilled human capital, technical competency and internal controls to manage their operations effectively, and (f) working with the government in creating the necessary legal and enabling infrastructure to promote the growth of the underlying commodities market. Existing exchanges seem to be aware of these issues and appear to be actively trying to pursue them.

Globally financial institutions are very active in the trading of commodities in futures exchanges. This is because some of the products and services such as commodity based loans and deposits, they provide have a commodity component giving them exposures which they need to manage. They also have a robust risk management mechanisms compared to other players that make them ideal choices in the roles of market-makers in commodities related trading. Certainly financial institutions and in particular well capitalized banks in Nepal have a role to play in the sustainable development of organized commodity exchange markets. Besides the normal activities of providing and managing segregated trading accounts, they can be involved as market makers, operators of warehouses and clearing of contracts in particular those related to precious metals, financing and trading of warehouse receipts, and by providing access to the commodity markets to the general public through the use of commodity linked structured deposits and to borrowers through commodity linked financing.

Nepal's organized commodity futures market has begun to take shape. The prospects are good and the challenges and bottlenecks are equally great. Where it goes from here will depend on how the various stakeholders in the market interact with each other to deal with the challenges and bottlenecks to take it forward.

Wide spread presence of our members



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