Commodity Challenge

Section 1: Introduction to Futures and Options Markets

Chapter 2: Cash and Futures Markets

Learning objectives

- The difference between a cash and futures markets, contracts and trading
- The difference between futures and forward contracts
- Types of orders

Key terms

Cash market: Anywhere that buyers and sellers meet to agree to terms of a contract.

Nearby market (aka "spot" market): The trading of cash contracts that call for immediate delivery.

Deferred market: The trading of cash contracts that call for later delivery (often months later), often called forward or "to-arrive" contracts.

Futures market: A commodity exchange where futures contracts are traded.

Market order: An order to buy or sell promptly at the first available bid or offer.

Limit order: An order placed to buy or sell a commodity at a specific price (or better).

Cash vs. Futures Trading

There are two types of grain markets where the trading of contracts occurs: **cash markets** and **futures markets**.

A **cash market** is where the trading of cash contracts occurs, involving the purchase or sale of the actual commodity for immediate or later delivery. A typical cash contract calls for immediate delivery in the nearby or "spot" market. A cash contract that calls for forward delivery is often called a **forward** or **to-arrive** contract.

Cash markets are informal and exist wherever a buyer and seller can agree to terms-at a local elevator office, over the phone, or through electronic platforms. Terms such as amount, quality, and timing are negotiated and unique to each contract. Cash contracts almost always end with physical delivery.

In contrast, **futures trading** occurs only on organized exchanges. Futures contracts are standardized, and the only negotiable term is price. Most futures contracts are offset before delivery and do not result in physical delivery.

Futures markets exist primarily for **price discovery** and **risk management**, while cash markets exist to physically move grain.

Know the difference between futures and forward contracts

Many people confuse "futures" and "forward" contracts, but they differ in important ways:

- **Futures contracts** are traded on organized exchanges.
- **Forward contracts** are cash contracts for future delivery, negotiated privately.
- Futures contracts are standardized; forward contracts are customized.
- Only about 1% of grain futures contracts end in delivery; forward contracts almost always end in delivery.

Types of Orders

To trade futures contracts-or many cash contracts-you must place an order.

Market Order

An order to buy or sell promptly at the first available bid or offer. Market orders usually fill near the most recent quote but can fill at less desirable prices in fast or thin markets.

Limit Order

A limit order specifies a price at which you are willing to buy or sell. In Commodity Challenge, this is the **“Set Price”** option. Limit orders offer more control but may not be filled.

All limit orders in Commodity Challenge remain active until filled or canceled.

Which contract should you buy?

When buying futures contracts to hedge grain, you must choose a delivery month. Corn and wheat typically offer five delivery months per year: **March, May, July, September, December**.

Example: If buying corn futures in April 2027, you may see:

- May ’27
- Jul ’27
- Sep ’27
- Dec ’27
- Mar ’28
- May ’28

Hedgers usually select the contract that aligns with expected delivery:

- Corn to be purchased in early June → hedge in **July** contract.
- Corn to be purchased in October → hedge in **December** contract.

Exercise #2

Place a market order and a limit order in the market.

1. Log into a game and place a **market order** to buy cash grain “At the market.” Note the cash price at the time of order placement. Compare the fill price to the quoted price.
2. Place a **limit order** to buy futures contracts. Note the futures quote at the time of order placement. Choose a realistic set price.
3. Check back later:
   a. Did the order fill?
   b. If not, will you wait for the market to reach your price or cancel and set a new price?

