Commodity Futures Glossary

A Guide to the Language of the Futures Industry

There are many words and phrases which are part of the futures industry. These terms represent the "language" which is used by all participants to communicate specific and precise information. Everyone who is involved in this industry must have a clear understanding of at least some of the terms and their definitions.

This *Commodity Futures Glossary* contains numerous terms, many of which describe specialized trading techniques. Although you may not engage in these techniques, it is helpful to know what a new term means when you encounter it.

Although this glossary contains general definitions intended to raise your awareness, you should consult with your broker regarding the legal consequence of any term which applies to your trading activities.

A ***FREE*** Commodity Futures Trading Home Study Course is available at http://www.mi.verio.com/~twnorows

Abandon - The act of an option holder in electing not to exercise or offset an option.

Accrued Interest - Interest earned between the most recent payment and the present date but not yet paid to the lender.

Accommodation Trading - Non-competitive trading entered into by a trader, usually to assist another with illegal trades.

Actuals - The physical or cash commodity, as distinguished from commodity futures contracts. Also see *Cash Commodity, Spot Commodity*.

Add-on Method - A method of paying interest where the interest is added onto the principle at maturity or interest payment dates.

Adjusted Futures Price - The cash-price equivalent reflected in the current futures price. This is calculated by taking the futures price times the conversion factor for the particular financial instrument (e.g., bond or note) being delivered.

Alternate Delivery Procedure (ADP) - A contract delivery method that permits the buyer and seller, by agreement, to settle their delivery commitment independent of the exchange.

Against Actuals - Also see *Exchange for Physicals*.

Aggregation - The principle under which all futures positions owned or controlled by one trader (or group of traders acting in concert) are combined to determine reporting status and speculative limit compliance.

Allowances - The discounts (premiums) allowed for grades or locations of a commodity lower (higher) than the par (or basis) grade or location specified in the futures contract. Also see *Differentials*.

Approved Delivery Facility - Any bank, stockyard, ill, store, house, plant, elevator or other depository that is authorized by an exchange for the delivery of commodities tendered on futures contracts.

Arbitrage - The simultaneous purchase of similar commodities in the same or different markets profit from a discrepancy in prices. Also includes some aspects of hedging. Also see *Spread*, *Switch*.

Arbitration - The procedure of settling disputes between members, or between members and customers.

Asian Option - An option whose payoff depends on the average price of the underlying asset during some portion of the life of the option.

Assign - To make an option seller perform his obligation to assume a short futures position (as the seller of a call option) or a long futures position (as a seller of a put option).

Assignable Contract - One which allows the holder to convey his rights to a third party. Exchange-traded contracts are not assignable.

Associated Person (AP) - An individual who solicits orders, customers, or customer funds (or who supervises persons performing such duties) on behalf of a Futures Commission Merchant, an Introducing Broker, a Commodity Trading Advisor, or a Commodity Pool Operator.

Associate Membership - A Chicago Board of Trade membership that allows an individual to trade financial instrument futures and other designated markets.

At-the-Market - An order to buy or sell a futures contract at whatever price is obtainable when the order reaches the trading floor. Also called a *Market Order*.

At-the-Money Option - An option with a strike price that is equal, or approximately equal, to the current market price of the underlying futures contract.

Backpricing - Fixing the price of a commodity for which the commitment to purchase has been made in advance. The buyer can fix the price relative to any monthly or periodic delivery using the futures markets.

Backwardation - Market situation in which futures prices are progressively lower in the distant delivery months. For instance, if the gold quotation for February is $160.00 per ounce and that for June is $155.00 per ounce, the backwardation for four months against January is $5.00 per ounce. (Backwardation is the opposite of contango.) See *Inverted Market*.

Balance of Payment - A summary of the international transactions of a country over a period of time including commodity and service transactions, and gold movements.

Bar Chart - A chart that graphs the high, low, and settlement prices for a specific trading session over a given period of time.

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

Basis Grade - The grade of a commodity used as the standard or par grade of a futures contract.

Basis Point - The measurement of a change in the yield of a debt security. One basis point equals 1/100 of one percent.

Basis Quote - Offer or sale of a cash commodity in terms of the difference above or below a futures price (e.g., 10 cents over December corn).

Basis Risk - The risk associated with an unexpected widening or narrowing of basis between the time a hedging position is established and the time that it is lifted.

Bear - Someone who expects a decline in prices. The opposite of *bull*. A news item is considered bearish if it is expected to bring lower prices.

Bearish Opinion - A belief that the price of the commodity underlying the futures contract will decline and, therefore, futures prices will decline.

Bear Market - A period of declining market prices.

Bear Spread - The simultaneous purchase and sale of two futures contracts in the same or related commodities with the intention of profiting from a decline in prices but at the same time limiting the potential loss if this expectation is wrong. In the agricultural products, this is accomplished by selling a nearby delivery and buying a deferred delivery.

Bear Vertical Spread - A strategy employed when an investor expects a decline in a commodity price but at the same time seeks to limit the potential loss if this expectation is wrong. This spread requires the simultaneous purchase and sale of options of the same class and expiration date but different strike prices. For example, if call options are spread, the purchased option must have a higher exercise price than the sold option.

Beta (Beta Coefficient) - A measure of the variability of rate of return or value of a stock or portfolio compared to that of the overall market.

Bid - An offer to buy a specific quantity of a commodity at a stated price, subject to immediate acceptance.

Black-Scholes Model - An option pricing formula initially derived by F. Black and M. Scholes for securities options and later refined by Black for options on futures.

Board of Trade - Any exchange or association, whether incorporated or unincorporated, of persons who are engaged in the business of buying or selling any commodity or receiving the same for sale on consignment.

Board of Trade Clearing Corporation - An independent corporation that settles all trades made at the Chicago Board of Trade acting as a guarantor for all trades cleared by it, reconciles all clearing member firm accounts each day to ensure that all gains have been credited and all losses have been collected, and sets and adjusts clearing member firm margins for changing market conditions. Also referred to as clearing corporation. Also see *Clearinghouse*.

Book Entry Securities - Electronically recorded securities that include each creditor's name, address, Social Security or tax identification number, and dollar amount loaned, (i.e., no certificates are issued to bond holders, instead the transfer agent electronically credits interest payments to each creditor's bank account on a designated date).

Booking the Basis - A forward pricing sales arrangement in which the cash price is determined either by the buyer or seller within a specified time. At that time, the previously-agreed basis is applied to the then-current futures quotation.

Book Transfer - A series of accounting or bookkeeping entries used to settle a series of cash market transactions.

Box Transaction - An option position in which the holder has established a long call and a short put at one strike price and a short call and a long put at another strike price, all of which are in the same contract month in the same commodity.

Break - A rapid and sharp price change.

Break-Even Point - The price (or prices) at which a particular option or straddle will cover premium and transaction costs.

Broker - A person paid a fee or commission for executing buy or sell orders of a customer. In commodity futures trading, the term may refer to: (1) Floor Broker--a person who actually executes orders on the trading floor of an exchange; (2) Account Executive, Associated Person, Registered Commodity Representative or Customer's Man--the person who deals with customers in the offices of futures commission merchant; and (3) the Futures Commission Merchant.

Brokerage Fee - See *Commission Fee*.

Brokerage House - See *Futures Commission Merchant*.

Bucketing - Directly or indirectly taking the opposite side of a customer's order into the broker's own account or into an account in which the broker has an interest, without open and competitive execution of the order on an exchange.

Bucket Shop - A brokerage enterprise which *books* (i.e., takes the opposite side of) a customer's order without actually having it executed on an exchange.

Bull - Someone who expects a rise in prices. The opposite of *bear*. A news item is considered bullish if it portends higher prices.

Bull Market - A period of rising market prices.

Bull Spread - The simultaneous purchase of the nearby month, and selling the deferred month, to profit from the change in the price relationship.

Bull Vertical Spread - A strategy used when an investor expects that the price of a commodity will go up but at the same time seeks to limit the potential loss should this judgment be in error. This strategy involves the simultaneous purchase and sale of options of the same class and expiration date but different strike prices. For example, if call options are spread, the purchased option must have a lower exercise price than the sold option.

Bullish Opinion - A belief that the price of the commodity underlying the futures contract will rise and, therefore, futures prices will rise.

Bullion - Bars or ingots of precious metals, usually cast in standardized sizes.

Buoyant - A market in which prices have a tendency to rise easily with a considerable show of strength.

Butterfly Spread - A three-legged spread in futures or options. In the options spread, the options have the same expiration date but differ in strike prices. For example, a butterfly spread in soybean call options might consist of two short calls at a $6.00 strike price, one long call at a $6.50 strike price, and one long call at a $5.50 strike price.

Buy In - To cover or close out a short position. See *Offset*.

Buyer - A market participant who takes a long futures position or buys an option. An option buyer is also called a holder, or owner.

Buyer's Market - A condition of the market in which there is an abundance of goods available and hence buyers can afford to be selective and may be able to buy at less than the price that had previously prevailed. Also see *Seller's Market*.

Buying Hedge (or Long Hedge) - Hedging transaction in which futures contracts are bought to protect against possible increased cost of commodities. Also see *Hedging*, *Purchasing Hedge*.

Buy (or Sell) On Close - To buy (or sell) at the end of the trading session within the closing price range.

Buy (or Sell) On Opening - To buy (or sell) at the beginning of a trading session within the opening price range.

C & F - Cost and Freight paid to a point of destination and included in the price quoted. Same as C.A.F.

Calendar Spread - See *Interdelivery Spread* or *Horizontal Spread*.

Call - (1) A period at the opening and the close of some futures markets in which the price for each futures contract is established by auction; (2) Buyer's Call generally applies to cotton, also called *call sale*. A purchase of a specified quantity of a specific grade of a commodity at a fixed number of points above or below a specified delivery month futures price with the buyer allowed a period of time to fix the price either by purchasing a future for the account of the seller or telling the seller when he wishes to fix the price; (3) Seller's Call, also called *call purchase*, is the same as the buyer's call except that the seller has the right to determine the time to fix the price; (4) option contract giving the buyer the right to purchase the commodity or to enter into a long position; and (5) the requirement that a financial instrument be returned to the issuer prior to maturity, with principal and accrued interest paid off upon return.

Call Option - A contract that grants the purchaser the right, but not the obligation, to buy the underlying instrument at the specified strike price on or before the expiration date. The buyer pays a premium to the seller of the contract. A call option is bought with the expectation of a rise in prices (going long). See *Put Option*.

Call Rule - An exchange regulation under which an official bid price for a cash commodity is competitively established at the close of each day's trading. It holds until the next opening of the exchange.

Canceling Order - An order that deletes a customer's previous order.

Capping - Effecting commodity or security transactions shortly prior to an option's expiration date by depressing or preventing a rise in the price of the commodity or security so that previously written call options will expire worthless and the premium received therefrom will be protected.

Carrying Broker - A member of a futures exchange, usually a futures commmission merchant (FCM), through whom another broker or customer elects to *clear* all or some of their trades.

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

Carrying Charges - Cost of storing a physical commodity or holding a financial instrument over a period of time. Includes insurance, storage, and interest on the invested funds as well as other incidental costs. It is a carrying charge market when there are higher futures prices for each successive contract maturity. If the carrying charge is adequate to reimburse the holder, it is called a "full charge." Also see *Negative Carry*, *Positive Carry* and *Contango*.

Carryover - Grain and oilseed commodities not consumed during the marketing year and remaining in storage at year's end. These stocks are "carried over" into the next marketing year and added to the stocks produced during that crop year.

Cash Commodity - The physical or actual commodity as distinguished from the futures contract. Sometimes called *Spot Commodity* or *Actuals*.

Cash Contract - A sales agreement for either immediate or future delivery of the actual product.

Cash Forward Sale - See *Forward Contracting*.

Cash Market - The place where people buy and sell the actual commodities, taking the form of: (1) an organized, self-regulated central market (e.g., a commodity exchange); (2) a decentralized over-the-counter market; or (3) a local organization, such as a grain elevator or meat processor, which provides a market for a small region.

Cash Price - The price in the marketplace for actual cash or spot commodities to be delivered via customary market channels.

Cash Settlement - Transactions generally involving index-based futures contracts that are settled in cash, based on the actual value of the index on the last trading day, in contrast to those that specify the delivery of a commodity or financial instrument.

Central Bank - A financial institution that has official or semiofficial status in a federal government. Central banks are the instruments used by governments to expand, contract or stabilize the supply of money and credit. They hold reserves of other banks, act as fiscal agents for their governments and can issue paper money.

Certified Stocks - Quantities of commodities designated and certified for delivery by an exchange under its trading and testing regulations at delivery points specified and approved by the exchange.

CFTC - See *Commodity Futures Trading Commission*.

CFO - Cancel Former Order.

Charting - The use of graphs and charts in the technical analysis of futures markets to plot trends of price movements, average movements of price, volume of trading and open interest. See *Technical Analysis*.

Chartist - Technical trader who reacts to signals read from graphs of price movements.

Cheap - Colloquialism implying that a commodity is underpriced.

Cheapest-to-Deliver - A method to determine which particular cash debt instrument is most profitable to deliver against a futures contract.

Chooser Option - An option which is transacted in the present but at a pre-specified future date is chosen to be either a put or a call option.

Churning - Excessive trading of an account by a broker with control of the account for the purpose of generating commissions while disregarding the interests of the customer.

Circuit Breaker - A system of trading halts and price limits on equities and derivative markets designed to provide a cooling-off period during large, intra-day market declines. The first known use of the term circuit breaker in this context was in the Report of the Presidential Task Force on Market Mechanisms (January 1988), which recommended that circuit breakers be adopted following the market break of October 1987.

C.I.F. - Cost, insurance and freight paid to a point of destination and included in the price quoted.

Class (of options) - Options of the same type (i.e., either puts or calls, but not both) covering the same underlying futures contract or physical commodity (e.g., a March call at strike price 62 and a May call at strike price 58).

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 - The procedure through which the clearing house or association becomes buyer to each seller of a futures contract, and seller to each buyer, and assumes responsibility for protecting buyers and sellers from financial loss by assuring performance on each contract.

Clearing Corporation - See *Board of Trade Clearing Corporation*.

Clearinghouse - An agency or separate corporation of a futures exchange that is responsible for settling trading accounts, clearing trades, collecting and maintaining margin monies, regulating delivery, and reporting trading data. Clearinghouses act as third parties to all futures and options contracts - acting as a buyer to every clearing member seller, and a seller to every clearing member buyer.

Clearing Margin - Financial safeguards to ensure that clearing members (usually companies or corporations) perform on the 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. See *Customer Margin*.

Clearing Member - A member of an exchange clearinghouse. Memberships in clearing organizations are usually held by companies. Clearing members are responsible for the financial commitments of customers that clear through their firm.

Clearing Price - See *Settlement Price*.

Clerk - A member's employee who is registered to work on the trading floor as a runner or phone person.

Close - The period at the end of the trading session officially designated by the exchange during which all transactions are considered made *at the close*. Also see *Call*.

Closing-Out - Liquidating an existing long or short futures or option position with an equal and opposite transaction. Also known as Offset.

Closing Price (or Range) - The price (or price range) recorded in trading that takes place in the final moments of a day's trade that are officially designated as the *close*.

Combination - Puts and calls held either long or short with different strike prices and expirations.

Commercial - An entity involved in the production, processing, or merchandising of a commodity.

Commercial Grain Stocks - Domestic grain in store in public and private elevators at important markets and grain afloat in vessels or barges in harbors of lake and seaboard ports.

Commercial Stocks - Commodity in storage in public and private elevators or warehouses at important markets and afloat in vessels or barges in harbors and ports.

Commission - (1) The charge made by a commission house for buying and selling commodities; (2) the CFTC.

Commission House - See *Futures Commission Merchant (FCM)*.

Commitments - Made when a trader assumes the obligation to accept or make delivery by entering into a futures contract. See *Open Interest*.

Commodity - An article of commerce or a product that can be used for commerce. In a narrow sense, products traded on an authorized commodity exchange. The types of commodities include agricultural products, metals, petroleum, foreign currencies, and financial instruments and index.

Commodity Credit Corp. - A branch of the U.S. Department of Agriculture that supervises the government's farm loan and subsidy programs.

Commodity Exchange Act - Federal act passed in 1936 establishing the Commodity Exchange Authority and placing futures trading in a wide range of commodities under the regulation of the government.

Commodity Futures Trading Commission (CFTC) - The Federal regulatory agency established by the CFTC Act of 1974 to administer the Commodity Exchange Act.

Commodity-linked Bond - A bond in which payment to the investor is dependent on the price level of such commodities as crude oil, gold, or silver at maturity.

Commodity Option - See *Option*, *Puts* and *Calls*.

Commodity Pool - An investment trust, syndicate or similar form of enterprise operated for the purpose of trading commodity futures or option contracts.

Commodity Pool Operator - An individual or organization that operates or solicits funds for a commodity pool.

Commodity Price Index - Index or average, which may be weighted, of selected commodity prices, intended to be representative of the markets in general or a specific subset of commodities (for example, grains or livestock).

Commodity Trading Advisor (CTA) - A person who, for compensation or profit, directly or indirectly advises others as to the value or the advisability of buying or selling futures contracts or commodity options. Advising indirectly includes exercising trading authority over a customer's account as well as providing recommendations through written publications or other media.

Concurrent Indicators - See *Lagging Indicators*.

Congestion - (1) A market situation in which shorts attempting to cover their positions are unable to find n adequate supply of contracts provided by longs willing to liquidate or by new sellers willing to enter the market, except at sharply higher prices; (2) in technical analysis, a period of time characterized by repetitious and limited price fluctuations.

Consignment - A shipment made by a producer or dealer to an agent elsewhere with the understanding that the commodities in question will be cared for or sold at the highest obtainable price. Title to the merchandise shipped on consignment rests with the shipper until the goods are disposed of according to agreement.

Consumer Price Index (CPI) - A major inflation measure computed by the U.S. Department of Commerce. It measures the changes in prices of a fixed market basket of some 385 goods and services in the previous month.

Contango - Market situation in which prices in succeeding delivery months are progressively higher than in the nearest delivery month; the opposite of "backwardation."

Contract - (1) A unit of trading for a commodity future or option; (2) An agreement to buy or sell a specified commodity, detailing the amount and grade of the product and the date on which the contract will mature and become deliverable.

Contract Grades - See *Deliverable Grades*.

Contract Market - (1) A board of trade or exchange designated by the Commodity Futures Trading Commission to trade futures or options under the Commodity Exchange Act; (2) Sometimes the futures contract itself (e.g., corn is a contract market).

Contract Month - See *Delivery Month*.

Contract Unit - The actual amount of a commodity represented in a contract.

Controlled Account - See *Discretionary Account*.

Convergence - The tendency for prices of physicals and futures to approach one another, usually during the delivery month. Also called a *narrowing of the basis*.

Conversion - When trading options on futures contracts, a position created by selling a call option, buying a put option, and buying the underlying futures contract, where the options have the same strike price and the same expiration.

Conversion Factor - A factor used to equate the price of T-bond and T-note futures contracts with the various cash T-bonds and T-notes eligible for delivery. This factor is based on the relationship of the cash-instrument coupon to the required 8 percent deliverable grade of a futures contract as well as taking into account the cash instrument's maturity or call.

Corner - (1) To corner is to secure such relative control of a commodity or security that its price can be manipulated; (2) In the extreme situation, obtaining contracts requiring delivery of more commodities or securities than are available for delivery.

Corn-Hog-Ratio - See *Feed Ratio*.

Cost of Carry (or Carry) - See *Carrying Charge*.

Cost of Tender - Total of various charges incurred when a commodity is certified and delivered on a futures contract.

Counter-Trend Trading - In technical analysis, the method by which a trader takes a position contrary to the current market direction in anticipation of a change in that direction.

Coupon (Coupon Rate) - The interest rate on a debt instrument expressed in terms of a percent on an annualized basis that the issuer guarantees to pay the holder until maturity.

Cover - (1) Purchasing futures to offset a short position. Same as Short Covering. See Offset, Liquidation; (2) To have in hand the physical commodity when a short futures or leverage sale is made, or to acquire commodity that might be deliverable on a short sale.

Covered Option - A short call or put option position which is covered by the sale or purchase of the underlying futures contract or physical commodities. For example, in the case of options on futures contracts a covered call is a short call position combined with a long futures position. A covered put is a short put position combined with a short futures position.

Crack - In energy futures, the simultaneous purchase of crude oil futures and the sale of petroleum product futures to establish a refining margin. See *Gross Processing Margin*.

Crop (Marketing) Year - The time period from one harvest to the next for agricultural commodities. The crop year varies slightly with each commodity (i.e., the marketing year for soybeans begins September 1 and ends in August 31. The futures contract month of November represents the first major new-crop marketing month, and the contract month of July represents the last major old-crop marketing month for soybeans.

Crop Reports - Reports compiled by the U.S. Department of Agriculture on various ag commodities that are released throughout the year. Information in the reports include estimates on planted acreage, yield, and expected production, as well as comparison of production from previous years.

Cross-Hedge - Hedging a cash market position in a futures contract for a different but price-related commodity (e.g., using soybean meal futures to hedge fish meal).

Cross-margining - A procedure for margining related securities options and futures contracts jointly when different clearing houses clear each side of the position.

Cross-Rate - In foreign exchange, the price of one currency in terms of another currency in the market of a third country. For example, a London dollar cross-rate could be the price of one U.S. dollar in terms of deutsche marks on the London market.

Cross Trading - Offsetting or noncompetitive match of the buy order of one customer against the sell order of another, a practice that is permissible only when executed in accordance with the Commodity Exchange Act, CFTC regulations, and rules of the contract market.

Crush Spread - In the soybean futures market, the simultaneous purchase of soybean futures and the sale of soybean meal and soybean oil futures to establish a processing margin. See *Gross Processing Margin*.

Curb Trading - Trading by telephone or by other means that takes place after the official market has closed. Originally it took place in the street on the curb outside the market. Under CFTC rules, curb trading is illegal. Also known as kerb trading.

Current Delivery Month - The futures contract which matures and becomes deliverable during the present month. Also called Spot Month. Daily Price Limits. See Limit Up, or Down).

Current Yield - The ratio of the coupon to the current market price of the debt instrument.

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. FCMs are responsible for overseeing customer margin accounts. Margins are determined on the basis of market risk and contract value. Also referred to as performance-bond margin. See *Clearing Margin*.

Day Order - An order that expires automatically at the end of each day's trading session if not filled. There may be a day order with time contingency. For example, an *off at a specific time* order is an order that remains in force until the specified time during the session is reached. At such time, the order is automatically canceled.

Daily Trading Limit - The maximum price range set by the exchange cash day for a contract.

Day Traders - Commodity traders, generally members of the exchange on the trading floor, who take positions in commodities and then offset them prior to the close of trading on the same trading day.

Day Trading - Establishing and offsetting the same futures market position within one day.

Dealer Option - A put or call on a physical commodity, not originating on or subject to the rules of an exchange, in which the obligation for performance rests with the writer of the option. Dealer options are normally written by firms handling the underlying commodity and offered to public customers, although the reverse may also be true.

Deck - The orders for purchase or sale of futures and option contracts held in the hands of a floor broker.

Declaration Date - See *Expiration Date*.

Declaration (of Options) - See *Exercise*.

Default - Failure to perform on a futures contract as required by exchange rules, such as failure to meet a margin call, or to make or take delivery.

Deferred Futures - The futures contracts that expire during the most distant months. Also called Back Months. See *Forward Purchase or Sale*.

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

Deliverable Grades - The standard grades of commodities or instruments listed in the rules of the exchanges that must be met when delivering cash commodities against futures contracts. Grades are often accompanied by a schedule of discounts and premiums allowable for delivery of commodities of lesser or greater quality than the standard called for by the exchange. Also referred to as *contract grades*.

Delivery - The transfer of the cash commodity from the seller of a futures contract to the buyer of a futures contract. Each futures exchange has specific procedures for delivery of a cash commodity. Some futures contracts, such as stock index contracts, are cash settled.

Delivery Commitment, Buyer's - The written notice given by the buyer of his intention to take delivery against a long futures position on delivery day.

Delivery Commitment, Seller's - The written notice given by the seller of his intention to make delivery against the short futures position on delivery day.

Delivery, Current - Deliveries being made during a present month. Sometimes current delivery is used as a synonym for nearby delivery.

Delivery Date - The date on which the commodity or instrument of delivery must be delivered to fulfill the terms of a contract.

Delivery Instrument - A document used to effect delivery on a futures contract, such as a warehouse receipt or shipping certificate.

Delivery Month - The specified month within which a futures contract matures and can be settled by making or accepting delivery. Also referred to as *contract month*.

Delivery, Nearby - The nearest traded month. In plural form, one of the nearer trading months.

Delivery Notice - The written notice given by the seller of his intention to make delivery against an open short futures position on a particular date. This notice, delivered through the clearing house, is separate and distinct from the warehouse receipt or other instrument that will be used to transfer title.

Delivery Option - A provision of a futures contract which provides the short with flexibility in regard to timing, location, quantity, or quality in the delivery process.

Delivery Points - Those locations designated by commodity exchanges where stocks of a commodity represented by a futures contract may be delivered in fulfillment of the contract.

Delivery Price - The price fixed by the clearing house at which deliveries on futures are invoiced--generally the price at which the futures contract is settled when deliveries are made.

Delta - A measure of how much an option premium changes, given a unit change in the underlying futures price. Delta is often interpreted as the probability that the option will be in-the-money by expiration.

Delta Margining - An option margining system used by some exchanges for exchange members and/or floor traders which equates the changes in option premiums with the changes in the price of the underlying futures contract to determine risk factors on which to base the margin requirements.

Delta Value - The expected change in an option's price given a one-unit change in the price of the underlying futures contract or physical commodity.

Deposit - The initial outlay required by a broker of a client to open a futures position, returnable on liquidation of that position.

Devaluation - A formal and *official* decrease in the value of a country's currency, typically by that country.

Diagonal Spread - A spread between two call options or two put options with different strike prices and different expiration dates.

Differentials - Price differences between classes, grades, and delivery locations of various stocks of the same commodity.

Discount - (1) The amount a price would be reduced to purchase a commodity of lesser grade; (2) sometimes used to refer to the price differences between futures of different delivery months, as in the phrase *July at a discount to May*, indicating that the price for the July future is lower than that of May; (3) an option is trading at a discount if it is trading for less than its intrinsic value.

Discount Basis - Method of quoting securities where the price is expressed as an annualized discount from maturity value.

Discount Bond - A bond selling below par.

Discount Method - A method of paying interest by issuing a security at less than par and repaying par value at maturity. The difference between the higher par value and the lower purchase price is the interest.

Discount Rate - The interest rate charged on loans by the Federal Reserve Bank.

Discretionary Account - An arrangement by which the holder of an account gives written power of attorney to someone else, often a broker, to make trading decisions. Also known as a *managed* or *controlled account*.

Distant or Deferred Delivery - Usually means one of the more distant months in which futures trading is taking place.

Dominant Future - That future having the largest number of open contracts.

Double Hedging - As used by the CFTC, it implies a situation where a trader holds a long position in the futures market in excess of the speculative limit as an offset to a fixed price sale even though the trader has an ample supply of the commodity on hand to fill all sales commitments.

Double Top -or- Double Bottom - Prices reaching their 12-month high or 12-month low two times. The second top or bottom may be used as a new number one point or may be considered the three point in a 1-2-3 formation.

Dual Trading - Dual trading occurs when: (1) a floor broker executes customer orders and, on the same day, trades for his own account or an account in which he has an interest; or (2) an FCM carries customer accounts and also trades, or permits its employees to trade,in accounts in which it has a proprietary interest, also on the same trading day.

Duration - A measure of a bond's price sensitivity to changes in interest rates.

Early Exercise - The exercise of an option contract before its expiration date.

Ease Off - A minor and/or slow decline in the prices of a market. ECU - See *European Currency Unit*.

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.

Efficient Market - A market in which new information is immediately available gratis to all investors and potential investors. A market in which all information is instantaneously assimilated and therefore has no distortions.

EFP - Exchange for Physical. See *Exchange of Futures for Cash*.

Elliot Wave - (1) A theory named after Ralph Elliot, who contended that the stock market tends to move in discernible and predictable patterns reflecting the basic harmony of nature; (2) in technical analysis, a charting method based on the belief that all prices act as waves rising and falling rhythmically.

Equilibrium Price - The market price at which the quantity supplied of a commodity equals the quantity demanded.

Equity - The residual dollar value of a futures, option, or leverage trading account assuming it were liquidated at current prices.

Eurocurrency - Certificates of Deposit (CDs), bonds, deposits, or any capital market instrument issued outside of the national boundaries of the currency in which the instrument is denominated (for example, Euro-Swiss francs, Euro-Deutsche marks, eurodollars, eurodollar bonds, or eurodollar CDs).

Eurodollars - U.S. dollars on deposit with a bank outside the U.S., and consequently, outside its jurisdiction. The bank could be either a foreign bank or a subsidiary of a U.S. bank.

Eurodollar Bonds - Bonds issued in Europe by corporate or government interests outside the boundary of the national capital market, denominated in dollars.

Eurodollar CDs - Dollar-denominated certificates of deposit issued by a bank outside of the United States, either a foreign bank or U.S. bank subsidiary.

European Currency Unit - The official unit of account of the European Monetary System. It is a combination or basket of the currencies from the twelve European Community countries: the Deutsche mark, French franc, British pound sterling, Irish pound, Italian lira, Belgian franc, Dutch guilder, Luxembourg franc, Greek drachma, Spanish peseta, Portuguese escudo, and the Danish krona.

Even Lot - A unit of trading in a commodity established by an exchange to which official price quotations apply. See *Round Lot*.

Evening Up - Buying or selling to offset an existing market position. See *Liquidation*.

Exchange For Physicals (EFPs) - A technique where a physical commodity position is traded for a futures position.

Exchange of Futures for Cash - A transaction in which the buyer of a cash commodity transfers to the seller a corresponding amount of long futures contracts, or receives from the seller a corresponding amount of short futures, at a price difference mutually agreed upon. In this way the opposite hedges in futures of both parties are closed out simultaneously. Also called EFP (Exchange for Physical), AA (Against Actuals) or Ex-Pit transactions.

Exchange Rate - The price of one currency stated in terms of another currency.

Exchange Risk Factor - The delta value of an option as computed daily by the exchange on which it is traded.

Exercise - The action taken by the holder of a call option if they wish to purchase the underlying futures contract, or by the holder of a put option if they wish to sell the underlying futures contract.

Exercise an Option - To enter the futures market at the strike price.

Exercise Price - See *Strike Price*.

Exotic Options - Any of a wide variety of options with non-standard payout structures, including Asian options and Lookback options mostly traded in the over-the-counter market.

Expanded Trading Hours - Additional trading hours of specific futures and options contracts at the Chicago Board of Trade that overlap with business hours in other time zones.

Expiration Date - The date on which an option contract becomes void. At a specified time on the expiration date, the option can no longer be exercised or sold. For example, an option on a March futures contract expires in February but is referred to as a March option because its exercise would result in a March futures contract position.

Ex-Pit Transactions - Trades executed, for certain technical purposes, in a location other than the regular exchange trading pit.

Extrinsic Value - See *Time Value*.

Face Value - The amount of money printed on the face of the certificate of a security; the original dollar amount of indebtedness incurred.

Federal Funds - Member bank deposits at the Federal Reserve; these funds are loaned by member banks to other member banks.

Federal Funds Rate - The rate of interest charged for the use of federal funds.

Federal Reserve System - A central banking system in the United States, created by the Federal Reserve Act in 1913, designed to assist the nation in attaining its economic and financial goals. The structure of the Federal Reserve System includes a Board of Governors, the Federal Open Market Committee, and 12 Federal Reserve Banks.

Feed Ratio - A ratio used to express the relationship of feeding costs to the dollar value of livestock. These serve as indicators of the profit margin or lack of profit in feeding animals to market weight. See *Hog/Corn Ratio* and *Steer/Corn Ratio*.

Fictitious Trading - Wash trading, bucketing, cross trading, or other schemes which give the appearance of trading. Actually, no bona fide, competitive trade has occurred.

Fill or Kill Order - A customer order that is a price limit order that must be filled immediately or cancelled.

First Notice Day (FND) - 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 who they have been matched up with.

Fix, Fixing - See *Gold Fixing*.

Floor Broker - Any person who, in or surrounding any pit, ring, post or other place provided by a contract market for the meeting of persons similarly engaged, executes for another person any orders for the purchase or sale of any commodity for future delivery. This person must be an exchange member and also trade for his own account under certain conditions.

Floor Trader - An exchange member who executes his own trades by being personally present in the pit or place for futures trading. See *Local*.

F.O.B. (Free On Board) - Indicates that all delivery, inspection and elevation or loading cost involved in putting commodities on board a carrier have been paid.

Forced Liquidation - The situation in which a customer's account is liquidated (open positions are offset) by the brokerage firm holding the account, or, in the case of leverage accounts, by the leverage transaction merchant, usually after notification (margin calls), because the account is undercapitalized.

Force Majeure - A clause in a supply contract which permits either party not to fulfill the contractual commitments due to events beyond their control. These events may range from strikes to export delays in producing countries.

Foreign Exchange - A foreign exchange market where foreign currency is bought and sold for immediate or future delivery.

Forward - In the future.

Forwardation - See *Contango*.

Forward Contract - A cash transaction common in many industries, including commodity merchandising, in which a commercial buyer and seller agree upon delivery of a specified quality and quantity of goods at a specified future date. A price may be agreed upon in advance, or there may be agreement that the price will be determined at the time of delivery.

Forward Market - Refers to informal (non-exchange) trading of commodities to be delivered at a future date. Contracts for forward delivery are *personalized*, (i.e., delivery time and amount are as determined between seller and customer).

Forward Months - Futures contracts, currently trading, calling for later or distant delivery. See *Deferred Futures*.

Forward Purchase or Sale - A purchase or sale between commercial parties of an actual commodity for deferred delivery.

Free Crowd System - A system of trading, common to most U.S. commodity exchanges, where all floor members may bid and offer simultaneously either for their own accounts or for the accounts of customers, and transactions may take place simultaneously at different places in the trading ring. Also see Board Broker System and Specialist System.

Frontrunning - With respect to commodity futures and options, taking a futures or option position based upon non-public information regarding an impending transaction by another person in the same or related future or option.

Full Carrying Charge, Full Carry - See *Carrying Charges*.

Fundamental Analysis - A method of anticipating future price movement using supply and demand information. See *Technical Analysis*.

Fungibility - The characteristic of interchangeability. Futures contracts for the same commodity and delivery month are fungible due to their standardized specifications for quality, quantity, delivery date and delivery locations.

Futures - A term used to designate all contracts covering the sale of commodities for future delivery on a commodity exchange. See Futures Contract.

Futures Commission Merchant (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. Also referred to as *commission house* or *wire house*.

Futures Contract - A legally binding agreement to purchase or sell a commodity for delivery in the future: (1) at a price that is determined at initiation of the contract; (2) which obligates each party to the contract to fulfill the contract at the specified price; (3) which is used to assume or shift price risk; and (4) which may be satisfied by delivery or offset.

Futures-equivalent - A term frequently used with reference to speculative position limits for options on futures contracts. The futures-equivalent of an option position is the number of options multiplied by the previous day's risk factor or delta for the option series For example, 10 deep out-of-the-money options with a risk factor of 0.20 would be considered 2 futures-equivalent contracts. The delta or risk factor used for this purpose is the same as that used in delta-based margining and risk analysis systems.

Futures Exchange - A central marketplace with established rules and regulations where buyers and sellers meet to trade futures and options on futures contracts.

Futures Price - (1) Commonly held to mean the price of a commodity for future delivery that is traded on a futures exchange. (2) The price of any futures contract.

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

GTC - See *Good Till Cancelled*.

Ginzy Trading - A trade practice in which a floor broker, in executing an order--particularly a large order, will fill a portion of the order at one price and the remainder of the order at another price to avoid an exchange's rule against trading at fractional increments or "split ticks." In re Murphy, [1984-86 Transfer Binder] Comm. Fut L. Rep. (CCH) at pp. 31,353-4 (Sept. 25, 1985), the Commission found that ginzy trading was a noncompetitive trading practice in violation of Section 4c(a)(B) of the Commodity Exchange Act and CFTC Regulation 1.38(a).

Give Up - A contract executed by one broker for the client of another broker that the client orders to be turned over to the second broker. The broker accepting the order from the customer collects a wire toll from the carrying broker for the use of the facilities. Often used to consolidate many small orders or to disperse large ones.

Globex - An international after-hours electronic trading system for futures and options that allows participating exchanges to list their products for trading after the close of the exchanges' open outcry trading hours. Developed by Reuters Limited for use by the Chicago Mercantile Exchange (CME) and the Chicago Board of Trade (CBOT), Globex was launched on June 25, 1992, for certain CME and CBOT contracts. Various MATIF (Marche a Terme International de France) contracts are scheduled to begin trading in early 1993, and, at this writing-- August 1992, several New York and European exchanges have expressed an interest in participating in Globex.

Going Long - Someone who expects a futures price to increase over a given period of time can seek to profit by *buying* futures contracts. The futures contract can later be sold for the higher price, yielding profits. Because of *leverage*, the gain or loss may be greater than the initial margin deposit.

Going Short - Someone who expects futures prices to decline. They would *sell* futures contracts in the anticipation of lower prices, and the hope of later being able to buy back identical and offsetting contract at a *lower* price, yielding profits. It differs from going long is in the sequence of the trades. Instead of first *buying* a futures contract, you first *sell* a futures contract. If, as expected, the price declines, a profit can be realized by later purchasing an offsetting futures contract at the lower price. The gain per unit will be the amount by which the purchase price is below the earlier selling price.

Gold Certificate - A certificate attesting to a person's ownership of a specific amount of gold bullion.

Gold Fixing (Gold Fix) - The setting of the gold price at 10:30 AM (first fixing) and 3:00 PM (second fixing) in London by five representatives of the London Gold Market. See *London Gold Market*.

Gold/Silver Ratio - The number of ounces of silver required to buy one ounce of gold at current spot prices.

Good This Week Order (GTW) - Order which is valid only for the week in which it is placed.

Good Till Cancelled Order (GTC) - Order which is valid at any time during market hours until executed or cancelled. See Open Order.

Grades - Various qualities of a commodity.

Grading Certificates - A formal document setting forth the quality of a commodity as determined by authorized inspectors or graders.

Grain Futures Act - Federal statute which regulated trading in grain futures, effective June 22, 1923; administered by the U.S. Department of Agriculture; amended in 1936 by the Commodity Exchange Act.

Grain Terminal - Large grain elevator facility with the capacity to ship grain by rail and/or barge to domestic or foreign markets.

Grantor - The maker, writer, or issuer of an option contract who, in return for the premium paid for the option, stands ready to purchase the underlying commodity (or futures contract) in the case of a put option or to sell the underlying commodity (or futures contract) in the case of a call option.

Gross Domestic Product - The value of all final goods and services produced by an economy over a particular time period, normally a year.

Gross National Product - Gross Domestic Product plus the income accruing to domestic residents as a result of investments abroad less income earned in domestic markets accruing to foreigners abroad.

Gross Processing Margin (GPM) - Refers to the difference between the cost of a commodity and the combined sales income of the finished products which result from processing the commodity. Various industries have formulas to express the relationship of raw material costs to sales income from finished products. For example, the difference between the cost of soybeans and the combines dales income of the processed soybean oil and meal. See *Crack* and *Crush*.

GTC - See *Good Till Cancelled Order*.

GTW - See *Good This Week Order*.

Haircut - (1) In determining whether assets meet capital requirements, a percentage reduction in the stated value of assets. (2) In computing the worth of assets deposited as collateral or margin, a reduction from market value.

Hardening - (1) Describes a price which is gradually stabilizing; (2) a term indicating a slowly advancing market.

Heavy - A market in which prices are demonstrating either an inability to advance or a slight tendency to decline.

Hedge - A position in a commodity for which there is an offsetting position.

Hedge Ratio - Ratio of the value of futures contracts purchased or sold to the value of the cash commodity being hedged, a computation necessary to minimize basis risk.

Hedger - An individual or company owning or planning to own a cash commodity (corn, soybeans, wheat, U.S. Treasury bonds, notes, bills, etc.) and concerned that the cost of the commodity may change before either buying or selling it in the cash market. A hedger achieves protection against changing cash prices by purchasing (selling) futures contracts of the same or similar commodity and later offsetting that position by selling (purchasing) futures contracts of the same quality and type as the initial transaction.

Hedging - Taking a position in a futures market opposite to a position held in the cash market to minimize the risk of financial loss from an adverse price change; a purchase or sale of futures as a temporary substitute for a cash transaction that will occur later. Someone that make purchases and sales in the *futures* market solely for the purpose of establishing a known price level – weeks or months in advance – for something they later intend to buy or sell in the *cash* market (such as at a grain elevator or in the bond market). Hedgers willingly give up the opportunity to benefit from *favorable* price changes in order to achieve protection against *unfavorable* price changes. For example, an option purchased opposite a position in the futures market.

High - The highest price of the day for a particular futures contract.

Hog/Corn Ratio - The relationship of feeding costs to the dollar value of hogs. It is measured by dividing the price of hogs ($/hundredweight) by the price of corn ($/bushel). When corn prices are high relative to pork prices, fewer units of corn equal the dollar value of 100 pounds of pork. Conversely, when corn prices are low in relation to pork prices, more units of corn are required to equal the value of 100 pounds of pork. See *Feed Ratio*.

Holder - An individual who pays the option seller a premium for the right to buy (in the case of a call) or sell (in the case of a put) the underlying instrument at the specified strike price on or before the expiration date. See *Option Buyer*.

Horizontal Spread - The purchase of either a call or put option and the simultaneous sale of the same type of option with typically the same strike price but with a different expiration month. Also referred to as a *calendar spread*.

Hybrid Instruments - Financial instruments that possess, in varying combinations, characteristics of forward contracts, futures contracts, option contracts, debt instruments, bank depository interests, and other interests. Certain hybrid instruments are exempt from CFTC regulation. See Commission Rule 34.1(b).

Index Arbitrage - The simultaneous purchase (sale) of stock index futures and the sale (purchase) of some or all of the component stocks which make up the particular stock index to profit from sufficiently large inter-market spreads between the futures contract and the index itself.

Initial Margin - Customers' funds put up as security for a guarantee of contract fulfillment at the time a futures market position is established. See *Original Margin*.

In Sight - The amount of a particular commodity that arrives at terminal or central locations in or near producing areas. When a commodity is *in sight*, it is inferred that reasonably prompt delivery can be made; the quantity and quality also become known factors, rather than estimates.

Intercommodity Spread - The purchase of a given delivery month of one futures market and the simultaneous sale of the same delivery month of a different, but related, futures market. See *Spread*.

Interdelivery Spread - The purchase of one delivery month of a given futures contract and simultaneous sale of another delivery month of the same commodity on the same exchange. See *Spread*.

Interest Arbitrage - The process where foreign debt instruments are purchased to profit from the higher interest rate in the foreign country over the home country. The operation is profitable only when the forward rate on the foreign currency is selling at a discount less than the premium on the interest rate. See *Interest Rate Parity*.

Interest Rate Futures - Futures contracts traded on fixed income securities such as U.S. Treasury issues or CDs. Currency is excluded from this category, even though interest rates are a factor in currency values.

Interest Rate Parity - The formal theory of interest rate parity holds that under normal conditions the forward premium or discount on a currency in terms of another is directly related to the interest differential between the two countries. For example, the forward rate discount (or premium) on Swiss Francs in terms of dollars would equal the premium (or discount) of interest rates in Switzerland over (or under) those in the U.S. This theory holds only when there are unrestricted flows of international short-term capital. In reality,numerous economic and legal obstacles restrict the movement, so that actual parity is rare. See *Interest Arbitrage*.

Intermarket Spread - The sale of a given delivery month of a futures contract on one exchange and the simultaneous purchase of the same delivery month and futures contract on another exchange.

Internal Financing - Using the profit from one contract to finance the margin on another.

In-The-Money Option - Describes an option with intrinsic (positive) value if exercised. A call option is in-the-money if its strike price is below the current price of the underlying futures contract. A put option is in-the-money if its strike price is above the current price of the underlying futures contract. See *Intrinsic Value*.

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

Introducing Broker (IB) - A person or organization that solicits or accepts orders to buy or sell futures contracts or commodity options but does not accept money or other assets from customers to support such orders.

Inverted Market - A futures market in which the relationship between two delivery months of the same commodity is abnormal. That is, the nearer months are selling at prices higher than the more distant months; a market displaying *inverse carrying charges*, characteristic of markets with supply shortages. See *Backwardation*.

Invisible Supply - Uncounted stocks of a commodity in the hands of wholesalers, manufacturers and producers which cannot be identified accurately; stocks outside commercial channels but theoretically available to the market.

Job Lot - A form of contract having a smaller unit of trading than is featured in a regular contract.

Kerb Trading or Dealing - See *Curb Trading*.

Lagging Indicators - Market indicators showing the general direction of the economy confirming or denying the trend implied by the leading indicators.

Large Order Execution (LOX) Procedures - Rules in place at the Chicago Mercantile Exchange that authorize a member firm which receives a large order from an initiating party to solicit counterparty interest off the exchange floor prior to open execution of the order in the pit and that provide for special surveillance procedures. The parties determine a maximum quantity and an "intended execution price." Subsequently, the initiating party's order quantity is exposed to the pit; any bids (or offers) up to and including those at the intended execution price are hit (accepted). The unexecuted balance is then crossed with the contra-side trader found by the LOX procedures.

Large Traders - A large trader is one who holds or controls a position in any one future or in any one option expiration series of a commodity on any one contract market equaling or exceeding the exchange or CFTC-specified reporting level.

Last Notice Day - The final day on which notices of intent to deliver on futures contracts may be issued.

Last Trading Day (LTD) - According to the Chicago Board of Trade rules, the final day when trading may occur in a given futures or option contract month. Futures contracts outstanding at the end of the last trading day must be settled by delivery of the underlying commodity or securities or by agreement for monetary settlement.

Leading Indicators - Market indicators that signal the state of the economy for the coming months. Some of the leading indicators include: average manufacturing workweek, initial claims for unemployment insurance, orders for consumer goods and material, percentage of companies reporting slower deliveries, change in manufacturers' unfilled orders for durable goods, plant and equipment orders, new building permits, index of consumer expectations, change in material prices, prices of stocks, change in money supply.

Leaps - Long-dated, exchange-traded options.

Leverage - The ability to control large dollar amounts of a commodity with a comparatively small amount of capital. See *margin*.

Leverage Contract - A contract, standardized as to terms and conditions, for the long-term (ten years or longer) purchase (long leverage contract) or sale (short leverage contract) by a leverage customer of a leverage commodity which provides for: (1) participation by the leverage transaction merchant as a principal in each leverage transaction; (2) initial and maintenance margin payments by the leverage customer; (3) periodic payment by the leverage customer or accrual by the leverage transaction merchant to the leverage customer of a variable carrying charge or fee on the initial value of the contract plus any margin deposits made by the leverage customer in connection with a short leverage contract; (4) delivery of a commodity in an amount and form which can be readily purchased and sold in normal commercial or retail channels; (5) delivery of the leverage commodity after satisfaction of the balance due on the contract; and (6) determination of the contract purchase and repurchase, or sale and resale, prices by the leverage transaction merchant.

Life of Contract - Period between beginning of trading a particular futures contract and the expiration of trading. In some cases this phrase denotes the period already passed in which trading has already occurred. For example, *The life-of-contract high so far is $2.50*. Same as Life of Delivery or Life of the Future.

Limit (Up or Down) - The maximum price advance or decline from the previous day's settlement price permitted during one trading session, as fixed by the rules of an exchange. See *Daily Price Limits*.

Limits - Stated in terms of the previous day's closing price plus and minus so many cents or dollars per trading unit. Once a futures price has increased by its daily limit, there can be no trading at any higher price *until the next day of trading*. Conversely, once a futures price has declined by its daily limit, there can be no trading at any lower price *until the next day of trading*. For some contracts, daily price limits are eliminated during the month in which the contract expires.

Because prices can become particularly volatile during the expiration month (also called the *delivery* or *spot* month), persons lacking experience in futures trading may wish to liquidate their positions prior to that time. Because of daily price limits, there may be occasions when it is not possible to liquidate an existing futures position at will.

Limit Move - A price that has advanced or declined the permissible limit during one trading session, as fixed by the rules of a contract market.

Limit Only - The definite price stated by a customer to a broker restricting the execution of an order to buy for not more than, or to sell for not less than, the stated price.

Limit Order - An order to buy or sell a futures contract at the specific price you state (or better), as contrasted with a market order which implies that the order should be filled as soon as possible.

Liquid - A characteristic of a security or commodity market with enough units outstanding to allow large transactions without substantial change in price. Institutional investors are inclined to seek out liquid investments so that their trading activity will not influence the market price.

Liquidate - Selling (or purchasing) futures contracts of the same delivery month purchased (or sold) during an earlier transaction or making (or taking) delivery of the cash commodity represented by the futures contract. See *Offset*.

Liquidation - The closing out of a long position. The term is sometimes used to denote closing out a short position, but this is more often referred to as covering. See *Cover*.

Liquidity - How easy it is to get out/in a market at a reasonable price close to your specified exit/entry price. Two useful indicators of liquidity are *volume of trading* and *Open Interest* (the number of traders willing to buy and sell).

Liquid Market - A market in which selling and buying can be accomplished with minimal price change.

Local - A member of a U.S. exchange who trades for his own account and/or fills orders for customers and whose activities provide market liquidity. See *Floor Trader*.

Locked-In - A hedged position that cannot be lifted without offsetting both sides of the hedge spread). See Hedging. Also refers to being caught in a limit price move.

Lock Limit - The event when prices have risen or fallen by the maximum daily limit, and there is presently no trading in the contract. It may not be possible to execute your order at *any* price. A market may be lock limit for more than one day, resulting in substantial losses to you when you find it impossible to liquidate losing futures positions.

London Gold Market - Refers to the five dealers who set (fix) the gold price in London: Mocatta & Goldsmid, N. Rothschild & Sons, Johnson Matthey, Sharps Pixley, and Samuel Montagu & Co.

London Option - A generic term sometimes used to describe options on physical commodities or on futures contracts traded abroad (typified by options on London commodity markets). These options, which often had nothing whatsoever to do with legitimate foreign markets, gained notoriety--prior to their ban in the United States in 1978--because of the sales practices and fraud allegations associated with the American dealers who sold them.

Long - (1) A market position which has been established through the purchase of an option or future and for which no offsetting sale has been made; (2) a market position which obligates the holder to take delivery; (3) one who owns an inventory of commodities. See *Short*.

Long Hedge - Purchase of futures against the fixed price forward sale of a cash commodity. See *Purchasing Hedge*.

Long the Basis - A person or firm that has bought the spot commodity and hedged with a sale of futures is said to be long the basis.

Lookback Option - An option whose payoff depends on the minimum or maximum price of the underlying asset during some portion of the life of the option.

Lot - A unit of trading. See *Even Lot*, *Job Lot*, and *Round Lot*.

Low - The lowest price of the day for a particular futures contract.

Maintenance - A set minimum margin (per outstanding futures contract) that a customer must maintain in his margin (trading) account.

Maintenance Margin - A sum usually smaller than, but part of, the original margin (security deposit) that must be maintained on deposit at all times. If customer equity in any futures position drops to or under the maintenance margin level, the broker must issue a call for the amount of money required to restore the customer's equity in the account back to the original margin level. See *Margin*.

Managed Account - See *Controlled Account*, *Discretionary Account*.

Managed Futures - Represents an industry comprised of professional money managers known as commodity trading advisors who manage client assets on a discretionary basis, using global futures markets as an investment medium.

Margin - The amount of money or collateral deposited by a customer with his broker, by a broker with a clearing member, or by a clearing member with the clearinghouse, for the purpose of insuring the broker or clearinghouse against loss on open futures contracts. The margin is not partial payment or a purchase. (1) Initial margin is the total amount of margin per contract required by the broker when a futures position is opened; (2) Maintenance margin is a sum which must be maintained on deposit at all times. If the equity in a customer's account drops to, or under, the level because of adverse price movement, the broker must issue a margin call to restore the customer's equity.

Monetary deposit to buy/sell a futures contract. Leverages your resources. Small deposit amount purchases large commodity value. The smaller the margin in relation to the value of the futures contract, the greater the leverage. The high leverage can produce large profits in relation to your initial margin. Conversely, if prices move in the opposite direction, high leverage can produce large *losses* in relation to your initial margin. You must clearly understand the concept of leverage as well as the amount of gain or loss that will result from any given change in the futures price of the particular futures contract you would be trading.

The margin required to buy or sell a futures contract is solely a deposit of good faith money that can be drawn on by your brokerage firm to cover losses that you may incur in the course of futures trading. It is like money held in an escrow account. Margins are typically 5% of the current value of the futures contract.

There are two types of margins: *Initial* margin and *maintenance* margin.

Initial margin (sometimes called *original* margin) is the sum of money that the customer must deposit with the brokerage firm for each futures contract to be bought or sold. When profits accrue on your open positions, the profits are added to the balance in your margin account. When *losses* accrue, the losses are deducted from the balance in your margin account.

If and when the funds remaining available in your margin account are reduced by losses to below a certain level - known as the *maintenance* margin requirement - your broker will require that you deposit additional funds to bring the account back to the level of the initial margin. See *Clearing Margin*, *Customer Margin*.

Margin Call - A demand by the brokerage firm for additional funds to bring margin deposits up to a required minimum level, because of adverse price movement. You will be required to keep an amount equal to the maintenance margins in your open account. If you are unable to do so, your position will be liquidated.

Market Correction - In technical analysis, a small reversal in prices following a significant trending period.

Market-If-Touched (MIT) Order - An order that becomes a market order when a particular price is reached. A sell MIT is placed above the market; a buy MIT is placed below the market. Also referred to as a board order.

Market-on-Close - An order to buy or sell at the end of the trading session at a price within the closing range of prices. See *Stop-Close-Only Order*.

Market-on-Opening - An order to buy or sell at the beginning of the trading session at a price within the opening range of prices.

Market Order - An order to buy or sell a futures contract or option at the prevailing market price when the order reaches the floor of the exchange. Considered a day order. See *At-The-Market*.

Mark-to-Market - Daily cash flow system used by U.S. futures exchanges to maintain a minimum level of margin equity for a given futures or option contract position by calculating the gain or loss in each contract position resulting from changes in the price of the futures or option contracts at the end of each trading day.

Maturity - Period within which a futures contract can be settled by delivery of the actual commodity.

Maximum Price Fluctuation - See *Tick*, *Limit Up*, *Limit Down*.

Minimum Price Contract - A hybrid commercial forward contract for agricultural products which includes a provision guaranteeing the person making delivery a minimum price for the product. For agricultural commodities, these contracts became much more common with the introduction of exchange-traded options on futures contracts, which permit buyers to hedge the price risks associated with such contracts.

Minimum Price Fluctuations - Smallest increment of price movement possible in trading a given contract.

Momentum - In technical analysis, the relative change in price over a specific time interval. Often equated with speed or velocity and considered in terms of relative strength.

Money Market - Short-term debt instruments.

Money Supply - The amount of money in the economy, consisting primarily of currency in circulation plus deposits in banks. M1 U.S. money supply consisting of currency held by the public, traveler's checks, checking account funds, NOW and super-NOW accounts, automatic transfer service accounts, and balances in credit unions. M2 U.S. money supply consisting M1 plus savings and small time deposits (less than $100,000) at depository institutions, overnight repurchase agreements at commercial banks, and money market mutual fund accounts. M3 U.S. money supply consisting of M2 plus large time deposits ($100,000 or more) at depository institutions, repurchase agreements with maturities longer than one day at commercial banks, and institutional money market accounts.

Moving Average Charts - A statistical price analysis method of recognizing different price trends. A moving average is calculated by adding the prices for a predetermined number of days and then dividing by the number of days.

Municipal Bonds - Debt securities issued by state and local governments, and special districts and counties.

Naked Call - See *Naked Option*.

Naked Option - The sale of a call or put option without holding an offsetting position in the underlying commodity.

Naked Put - See *Naked Option*.

National Futures Association (NFA) - An industrywide,industry-supported, self-regulatory organization for futures and options markets. The primary responsibilities of the NFA are to enforce ethical standards and customer protection, screen futures professionals for membership, audit and monitor professionals for financial and general compliance rules and provide for arbitration of futures-related disputes.

Nearby (Delivery) Month - The futures contract month closest to expiration. Also called *spot month*.

Negative Carry - The cost of financing a financial instrument (the short-term rate of interest), when the cost is above the current return of the financial instrument. See *Carrying Charges* and *Positive Carry*.

Negative Yield Curve - See *Yield Curve*.

Net Position - The difference between the open long contracts and the open short contracts held by a trader in any one commodity.

NOB Spread - Note Against Bond. A futures spread trade involving the buying (selling) of a Treasury note futures contract and the selling (buying) of a Treasury bond futures contract.

Nominal Price (or Nominal Quotation) - Computed price quotations on futures for a period in which no actual trading took place, usually an average of bid and asked prices.

Notice Day - According to Chicago Board of Trade rules, the second day of the three-day delivery process when the clearing corporation matches the buyer with the oldest reported long position to the delivering seller and notifies both parties. See *First Notice Day*.

Notice of Delivery - A notice that must be presented by the seller of a futures contract to the clearinghouse. The clearinghouse then assigns the notice and subsequent delivery instrument to a buyer. Also Notice of Intention to Deliver.

Notional Amount - The amount (in an interest rate swap, forward rate agreement, or other derivative instrument) or each of the amounts (in a currency swap) to which interest rates are applied (whether or not expressed as a rate or stated on a coupon basis) in order to calculate periodic payment obligations. Also called the notional principal amount, the contract amount, the reference amount, and the currency amount.

Number 1 Top - The highest price paid for a commodity in the last 12-months.

Number 1 Bottom - The lowest price paid for a commodity in the last 12-months.

Offer - An indication of willingness to sell at a given price; as opposite to bid.

Offset - Taking a second futures or options position opposite to the initial or opening position. See *Cover*, *Liquidate*.

Omnibus Account - An account carried by one futures commission merchant with another futures commission merchant in which the transactions of two or more persons are combined and carried in the name of the originating broker rather than designated separately.

On Track (or Track Country Station) - (1) A type of deferred delivery in which the price is set f.o.b. seller's location, and the buyer agrees to pay freight costs to his destination; (2) commodities loaded in railroad cars on track.

OPEC - Organization of Petroleum Exporting Countries, emerged as the major petroleum pricing power in 1973, when the ownership of oil production in the Middle East transferred from the operating companies to the governments of the producing countries or to their national oil companies. Members are Algeria, Ecuador, Gabon, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, the United Arab Emirates, and Venezuela.

Open Contracts - Contracts that have been bought or sold and are still outstanding, not having been delivered upon offset. See *Open Interest*.

Opening Price (or Range) - A range of prices at which buy and sell transactions took place during the opening of the market.

Opening - The period at the beginning of the trading session officially designated by the exchange during which all transactions are considered made *at the opening*.

Open Interest - The total number of futures contracts long or short outstanding in a delivery month or market that have been entered into and not yet liquidated by an offsetting transaction or fulfilled or satisfied by delivery. Open interest of 1,000 means 1,000 buyers and 1,000 sellers on that date.

Open Market Operation - The buying and selling of government securities (treasury bills, notes, and bonds) by the Federal Reserve.

Open Order (or Orders) - An order that remains in force until it is cancelled or until the futures contracts expire. See Good Till Cancelled and Good This Week orders.

Open Outcry - Method of public auction for making verbal bids and offers in the trading pits or rings of futures exchanges.

Option - A commodity option is a unilateral contract which gives the buyer the right (but not the obligation) to buy or sell a specified quantity of a commodity at a specific price within a specified period of time, regardless of the market price of that commodity. Also see *Put* and *Call*. Enables option buyers to participate in futures markets with known risks. Options make it possible to speculate on increasing or decreasing futures prices with a *known and limited risk*. The most that the buyer of an option can lose is the cost of purchasing the option (known as the option *premium*) plus transaction costs. There are two types: *put* and *call* options.

Options can be most easily understood when call options and put options are considered separately, since, in fact, they *are* totally separate and distinct. Buying or selling a call in no way involves a put, and buying or selling a put in no way involves a call.

The buyer of a *Call Option* acquires the right *but not the obligation* to purchase (go long) a particular futures contract at a specified price at any time during the life of the option. Each option specifies the futures contract which may be purchased (known as the "underlying" futures contract) - and the price at which it can be purchased (known as the "exercise" or "strike" price). One reason for buying call options is to profit from an anticipated *increase* in the underlying futures price. A call option buyer will realize a net profit if, upon exercise, the underlying futures price is *above the option exercise price* by more than the premium paid for the option. Or a profit can be realized if, prior to expiration, the option rights can be sold for more than they cost. While the option buyer has a limited *risk* (the loss of the option premium), the *profit potential* is reduced by the amount of the premium.

A *Put Option* conveys the right to *sell* (go short) a particular futures contract at a specified price. Put options can be purchased to profit from an anticipated price *decrease*. Again, the most that a put option buyer can lose, if wrong about the direction or timing of the price change, is the option premium plus transaction costs.

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. Also referred to as the *holder*.

Option Grantor - The person who originates an option contract by promising to perform a certain obligation in return for the price of the option. Also known as *Option Writer*.

Option Premiums - The price to acquire the option; the sum of money that the option buyer pays and the option seller receives for the rights granted by the option. Three variables influence the option premium:

<u>The option's exercise price</u>, or more specifically, the relationship <u>between the exercise price</u> and the current price of the underlying futures contract. An option that is already worthwhile to exercise (known as an "in-the-money" option) commands a higher premium than an option that is not yet worthwhile to exercise (an "out-of-the-money" option).

The length of time remaining until expiration. An option with a long period of time remaining until expiration commands a higher premium than an option with a short period of time remaining until expiration because it has more time in which to become profitable. Said another way, an option is an eroding asset. Its time value declines as it approaches expiration.

The volatility of the underlying futures contract. The greater the volatility the higher the option premium. In a volatile market, the option stands a greater chance of becoming profitable to exercise.

Selling Options. Who *sells* the options that buyers purchase? Options are sold by other market participants known as option writers, or grantors. Their sole reason for writing options is to earn the premium paid by the option buyer. If the option expires without being exercised (which is what the option writer hopes will happen), the writer retains the full amount of the premium. If the option buyer exercises the option, however, the writer must pay the difference between the market value and the exercise price.

Option Seller - The person who sells an option in return for a premium and is obligated to perform when the holder exercises his right under the option contract. Also referred to as the *writer*.

Option Spread - The simultaneous purchase and sale of one or more options contracts, futures, and/or cash positions.

Option Writer - See *Option Seller*.

Original Margin - The amount a futures market participant must deposit into his margin (trading) account at the time they place an order to buy or sell a futures contract. See *Initial Margin*.

Out-Of-The-Money Option - A term used to describe an option that has no intrinsic value. The strike price is above (in the case of a call) or below (in the case of a put) the underlying instrument's price. For example, a call at $400 on gold trading at $390 is out-of-the-money by $10.

Out Trade - A trade which cannot be cleared by a clearinghouse because the trade data submitted by the two clearing members involved in the trade differs in some respect (e.g., price and/or quantity). In such cases, the two clearing members or brokers involved must reconcile the discrepancy, if possible, and resubmit the trade for clearing. If an agreement cannot be reached by the two clearing members or brokers involved, the dispute would be settled by an appropriate exchange committee.

Overbought - A technical opinion that the market price has risen too steeply and too fast in relation to underlying fundamental factors. Rank and file traders who were bullish and long have turned bearish.

Overnight Trade - A trade which is not liquidated on the same trading day in which it was established.

Oversold - A technical opinion that the market price has declined too steeply and too fast in relation to underlying fundamental factors. Rank and file traders who were bearish and short have turned bullish.

Over-the-Counter (OTC) Market - A market where products such as stocks, foreign currencies, and other cash items are bought and sold by telephone and other means of communications.

Overvalued - Describing an instrument trading at a higher price than it logically should. Normally associated with the results of options price predictions by mathematical models. If an option is trading in the market for a higher price than the model indicates, the option is said to be overvalued.

P&S (Purchase and Sale Statement) - A statement sent by a commission house to a customer when any part of a futures position is offset, showing the number of contracts involved, the prices at which the contracts were bought or sold, the gross profit or loss, the commission charges, the net profit or loss on the transactions, and the balance.

Paper Profit or Loss - The profit or loss that would be realized if open contracts were liquidated as of a certain time or price.

Par - (1) Refers to the standard delivery point(s) and/or quality of a commodity that is deliverable on a futures contract at contract price. Serves as a benchmark upon which to base discounts or premiums for varying quality and delivery locations. (2) In bond markets, an index (usually 100) representing the face value of a bond. For example, a bond selling at par is worth the same dollar amount it was issued for or at which it will be redeemed at maturity.

Parity - Par Rate.

Path Dependent Option - An option whose valuation and payoff depends on the realized price path of the underlying asset, such as an Asian option or a Lookback option.

Pay/Collect - A shorthand method of referring to the payment of a loss (pay) and receipt of a gain (collect) by a clearing member to or from a clearing organization that occurs after a futures position has been marked-to-market. See Variation Margin.

Payment-in-Kind - Refers to an alternative to cash payments to producers of various commodities under the U.S. Department of Agriculture acreage control program authorized by Congress in 1985. The payments consisted of generic certificates which could be exchanged for commodities held in government warehouses or redeemed for equivalent monetary value.

Pegged Price - The price at which a commodity has been fixed by agreement.

Pegging - Effecting commodity transactions to prevent a decline in the price of the commodity so that previously written put options will expire worthless, thus protecting premiums previously received.

Performance Bond Margin - The amount of money deposited by both buyer and seller of a futures contract or an options seller to ensure performance of the term of the contract. Margin in commodities is not a payment of equity or down payment on the commodity itself, but rather it is a security deposit. See *Customer Margin* and *Clearing House*.

Pit - The area on the trading floor where futures and options on futures contracts are bought and sold. Pits are usually raised octagonal platforms with steps descending on the inside that permit buyers and sellers of contracts to see each other.

Point - A measure of price change equal to 1/100 of one cent in most futures traded in decimal units. In grains, it is 1/4 of one cent; in T-bonds, it is one percent of par. See *Tick*.

Point-And-Figure - A method of charting which uses prices to form patterns of movement without regard to time. It defines a price trend as a continued movement in one direction until a reversal of a predetermined criterion is met.

Point Balance - A statement prepared by futures commission merchants to show profit or loss on all open contracts by computing them to an official closing or settlement price, usually at calendar month end.

Point Value - A point is the minimum basic price unit of a commodity established by the exchange. It is based on the futures contract size.

Pork Bellies - One of the major cuts of the hog carcass that, when cured, becomes bacon.

Portfolio Insurance - A trading strategy which attempts to alter the nature of price changes in a portfolio to substantially reduce the likelihood of returns below some predetermined level for an established period of time. This can be achieved by moving assets among stocks, cash and fixed-income securities or, with the advent of stock index futures contracts, by hedging a stock-only portfolio by selling stock index futures in a declining market or purchasing futures in a rising market. The objective is to create an exposure similar to that of a stock portfolio with a protective purchased put option.

Position - A market commitment, either long or short, in the form of one or more open contracts. A buyer of a futures contract is said to have a long position and, conversely, a seller of a futures contract is said to have a short position. Also, *in position* refers to a commodity located where it can readily be moved to another point or delivered on a futures contract. Commodities not so situated are *out of position*. Soybeans in Mississippi are out of position for delivery in Chicago, but in position for export shipment from the Gulf.

Position Day - According to the Chicago Board of Trade rules, the first day in the process of making or taking delivery of the actual commodity on a futures contract. The clearing firm representing the seller notifies the Board of Trade Clearing Corporation that its short customers want to deliver on a futures contract.

Position Limit - The maximum number of futures contracts one can hold as determined by the Commodity Futures Trading Commission and/or the exchange upon which the contract is traded. Also referred to as *trading limit*.

Position Trader - An approach to trading in which the trader either buys or sells contracts and holds them for an extended period of time, as distinguished from the day trader, who will normally initiate and offset a futures position within a single trading session.

Positive Carry - The cost of financing a financial instrument (the short-term rate of interest), where the cost is less than the current return of the financial instrument. See also *Carrying Charges* and *Negative Carry*.

Posted Price - An announced or advertised price indicating what a firm will pay for a commodity or the price at which the firm will sell it.

Premium - (1) The price of an option, paid by option buyer to option seller, for the right to buy or sell the underlying instrument at the specified strike price on or before the expiration date. Determined competitively on the exchange floor. (2) The additional payment allowed by exchange regulation for delivery of higher-than-required standards or grades of a commodity against a futures contract. (3) In speaking of price relationships between different delivery months of a given commodity, one is said to be "trading at a premium" over another when its price is greater than that of the other. (4) In financial instruments, the dollar amount by which a security trades above its principal value. See *Option Premium*.

Price Basing - A situation where producers, processors, merchants or consumers of a commodity establish commercial transaction prices based on the futures prices for that or a related commodity (e.g., an offer to sell corn at 5 cents over the December futures price). This phenomenon is commonly observed in grain and metal markets.

Price Discovery - (1) The process of determining the price level for a commodity based on supply and demand factors. (2) The "generation" of information about "future" cash market prices through the futures markets.

Price Limit - The maximum advance or decline from the previous day's settlement permitted for a contract in one trading session by the rules of the exchange. See also *Variable Limit*.

Price Limit Order - A customer order that specifies the price at which a trade can be executed.

Price Manipulation - Any planned operation, transaction or practice calculated to cause or maintain an artificial price.

Price Movement Limit - See *Limit Up*, *Limit Down*.

Primary Dealer - A designation given by the Federal Reserve System to commercial banks or brokers/dealers who meet specific criteria. Among the criteria are capital requirements and meaningful participation in the Treasury auctions.

Primary Market - (1) For producers, their major purchaser of commodities; (a) in commercial marketing channels, an important center at which spot commodities are concentrated for shipment to terminal markets; and (b) to processors, the market that is the major supplier of their commodity needs. (2) Market of new issues of securities.

Prime Rate - Interest rate charged by major banks to their most creditworthy customers.

Principals' Market - A market where the ring dealing members act as principals for the transactions they conclude across the ring and with their clients.

Producer Price Index (PPI) - An index that shows the cost of resources needed to produce manufactured goods during the previous month.

Program Trading - The purchase (or sale) of a large number of stocks contained in or comprising a portfolio. Originally called *program* trading when index funds and other institutional investors began to embark on large-scale buying or selling campaigns or *programs* to invest in a manner which replicated a target stock index, the term now also commonly includes computer aided stock market buying or selling programs, portfolio insurance, and index arbitrage.

Prompt Date - The date on which the buyer of an option will buy or sell the underlying commodity (or futures contract) if the option is exercised.

Public - In trade parlance, non-professional speculators as distinguished from hedgers and professional speculators or traders.

Public Elevators - Grain elevators in which bulk storage of grain is provided for the public for a fee. Grain of the same grade but owned by different persons is usually mixed or commingled as opposed to storing it *identity preserved*. Some elevators are approved by exchanges as *regular* for delivery on futures contracts.

Pulpit - A raised structure adjacent to, or in the center of, the pit or ring at a futures exchange where market reporters, employed by the exchange, record price changes as they occur in the trading pit.

Purchase and Sale Statement - See *P&S*.

Purchasing Hedge or Long Hedge - Buyer futures contract 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 open futures position is closed by selling an equal number and type of futures contracts as those that were initially purchased.

Put Option - A contract that grants its purchaser the right, but not the obligation, to sell (go "short") the underlying instrument at the specified strike price on or before the expiration date. Also see *Call Option*.

Pyramiding - The use of accrued profits on existing positions as margin for additional contracts to increase the size of the position, normally in successively smaller increments.

Quick Order - See *Fill or Kill Order*.

Quotation - The actual price or the bid or asked price of either cash commodities or futures contracts.

Rally - An upward movement of prices following a decline. Same as Recovery.

Random Walk - An economic theory that price movements in the commodity futures markets and in the securities markets are completely random in character (i.e., past price is not an indicator of future price).

Range - The difference between the high and low price of a commodity during a given period.

Ratio Hedge - The number of options compared to the number of futures contracts taken in a position necessary to be a hedge; that is, risk neutral.

Ratio Spread - This strategy, which applies to both puts and calls, involves buying or selling options at one strike price in greater number than those bought or sold at another strike price.

Reaction - The downward price movement tendency of a commodity after a price advance.

Recovery - An upward price movement after a decline. Same as *Rally*.

Regular Warehouse - A processing plant or warehouse that satisfies exchange requirements for financing, facilities, capacity and location and has been approved as acceptable for delivery of commodities against futures contracts. See *Licensed Warehouse*.

Replicating Portfolio - A portfolio of assets for which changes in value match those of a target asset. For example, a portfolio replicating a standard option can be constructed with certain amounts of the asset underlying the option and bonds. Sometimes referred to as a *Synthetic Asset*.

Repurchase Agreement or (Repro) - An agreement between a seller and a buyer, usually in U.S. government securities, in which the seller agrees to buy back the security at a later date.

Reserve Requirements - The minimum amount of cash and liquid assets as a percentage of demand deposits and time deposits that member banks of the Federal Reserve are required to maintain.

Resistance - In technical trading, a price area where new selling will emerge to dampen a continued rise. The level above which price has difficulty penetrating. Also see *Support*.

Resting Order - An order to buy at a price below or to sell at a price above the prevailing market that is being held by a floor broker. Such orders may either be day orders or open orders.

Resumption - The reopening the following day of specific futures and options markets that also trade during the evening session at the Chicago Board of Trade.

Retender - In specific circumstances, some contract markets permit holders of futures contracts who have received a delivery notice through the clearing house to sell a futures contract and return the notice to the clearing house to be reissued to another long; others permit transfer of notices to another buyer. In either case, the trader is said to have retendered the notice.

Retracement - A reversal within a major price trend.

Reverse Crush Spread - The sale of soybean futures and the simultaneous purchase of soybean oil and meal futures. See *Crush Spread*.

Reversal - A change of direction in prices.

Reversal Stop Order - An order that not only offsets your current futures position (long or short), but actually enters you in that market on the opposite side.

Reverse Conversion - With regard to options, a position created by buying a call option, selling a put option, and selling the underlying futures contract.

Riding the Yield Curve - Trading in an interest rate future according to the expectations of change in the yield curve.

Ring - A circular area on the trading floor of an exchange where traders and brokers stand while executing futures trades. Some exchanges use pits rather than rings. See Pit.

Risk Factor - See *Delta Value*.

Risk/Reward Ratio - The relationship between the probability of loss and that of profit. This ratio is often used as a basis for trade selection or comparison.

Roll-Over - A trading procedure involving the shift of one month of a straddle into another future month while holding the other contract month. The shift can take place in either the long or short straddle month. The term also applies to lifting a near futures position and re-establishing it in a more deferred delivery month.

Round Lot - A quantity of a commodity equal in size to the corresponding futures contract for the commodity. See *Even Lot*.

Round Turn - A completed transaction involving both a purchase and a liquidating sale, or a sale followed by a covering purchase.

Rules - The principles for governing an exchange. In some exchanges, rules are adopted by a vote of the membership, while regulations can be imposed by the governing board.

Runners - Messengers who rush orders received by phone clerks to brokers for execution in the pit.

Sample Grade - In commodities, usually the lowest quality of a commodity, too low to be acceptable for delivery in satisfaction of futures contracts.

Scale Down (or Up) - To purchase or sell a scale down means to buy or sell at regular price intervals in a declining market. To buy or sell on scale up means to buy or sell at regular price intervals as the market advances. Scalper - A speculator on the trading floor of an exchange who buys and sells rapidly, with small profits or losses, holding his positions for only a short time during a trading session. Typically, a scalper will stand ready to buy at a fraction below the last transaction price and to sell at a fraction above, thus creating market liquidity.

Scalp - To trade for small gains. Involves quickly establishing and liquidating a position within the same day, hour or minute.

Scalper - A trader who trades for small, short-term profits during the course of a trading session, rarely carrying a position overnight.

Scalping - The practice of trading in and out of the market on very small price fluctuations. A person who engages in this practice is known as a scalper.

Secondary Market - Market where previously issued securities are bought and sold.

Security - Common or preferred stock; a bond corporation, government, or quasi-government body.

Security Deposit - See *Margin*.

Security Deposit Call - A demand for additional cash funds because of adverse price movement. See *Maintenance Margin*.

Seller's Call - See *Call*.

Seller's Market - A condition of the market in which there is a scarcity of goods available and hence sellers can obtain better conditions of sale or higher prices. Also see *Buyer's Market*.

Seller's Option - The right of a seller to select, within the limits prescribed by a contract, the quality of the commodity delivered and the time and place of delivery.

Selling Hedge (or Short Hedge) - Selling futures contracts to protect against possible decreased prices of commodities. Also see *Hedging*.

Series (of Options) - Options of the same type (i.e., either puts or calls, but not both), covering the same underlying futures contract or physical commodity, having the same strike price and expiration date.

Settle - See *Settlement Price*.

Settlement - The act of fulfilling the delivery requirements of a futures contract.

Settlement Price - The last price paid for a commodity on any trading day. The exchange clearinghouse determines a firm's net gain 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. Also referred to as *settle* or *closing price*.

Sharpe Ratio - A measurement of trading performance calculated as the average return divided by the variance of those returns; named after William P. Sharpe.

Shipping Certificate - A negotiable instrument used by several futures exchanges as the futures delivery instrument for several commodities (e.g., soybean meal, plywood, and white wheat). The shipping certificate is issued by exchange-approved facilities and represents a commitment by the facility to deliver the commodity to the holder of the certificate under the terms specified therein. Unlike an issuer of a warehouse receipt who has physical product in store, the issuer of a shipping certificate may honor its obligation from current production as well as from inventories.

Shock Absorber - A temporary restriction in the trading of stock index futures which becomes effective following a significant intra-day decrease in stock index futures prices. Designed to provide an adjustment period to digest new market information, the restriction bars trading below a specified price level. Shock absorbers are generally market specific and at tighter levels than circuit breakers.

Short - (1) One who has sold futures contracts or plans to purchase a cash commodity. (2) Selling futures contracts or initiating a cash forward contract sale without offsetting a particular market position. (3) The selling side of an open futures contract; a trader whose net position in the futures market shows an excess of open sales over open purchases. See *Long*.

Short Covering - See *Cover*.

Short Hedge - See *Selling Hedge, Hedging*.

Short Selling - Selling a futures contract with the idea of purchasing it at a lower price at a later date. The speculator expects the market to decline. This market position is known as a short position.

Short Squeeze - See *Squeeze*.

Short the Basis - The purchase of futures as a hedge against a commitment to sell in the cash or spot markets. See Hedging.

Small Traders - Traders who hold or control positions in futures or options that are below the reporting level specified by the exchange or the CFTC.

Soft - A description of a price which is gradually weakening. Also refers to commodities such as sugar, cocoa, and coffee.

Soften - The process of a slowly declining market price.

Sold-Out-Market - When liquidation of a weakly-held position has been completed, and offerings become scarce, the market is said to be sold out.

Speculative Bubble - A rapid, but usually short-lived, run-up in prices caused by excessive buying which is unrelated to any of the basic, underlying factors affecting the supply or demand for the commodity. Speculative bubbles are usually associated with a *bandwagon* effect in which speculators rush to buy the commodity (in the case of futures, *to take positions*) before the price trend ends, and an even greater rush to sell the commodity (unwind positions) when prices reverse.

Speculative Limit - See *Position Limit*.

Speculative Position Limit - See *Position Limit*.

Speculator - A market participant who tries to profit from buying and selling futures and options contracts by anticipating future price movements. Speculators assume market price risk and add liquidity and capital to the futures markets.

Split Close - Term which refers to price differences in transactions at the close of any market session.

Spot - Usually refers to a cash market price for a physical commodity that is available for immediate delivery. Also refers to a maturing delivery month of a futures contract.

Spot Commodity - (1) The actual commodity as distinguished from a futures contract; (2) sometimes used to refer to cash commodities available for immediate delivery. Also see *Actuals or Cash Commodity*.

Spot Delivery - Immediate delivery.

Spot Month - See *Nearby (Delivery) Month*.

Spot Price - The price at which a physical commodity for immediate delivery is selling at a given time and place. Same as Cash Price. See *Cash Price*.

Spread (or Straddle) - The price difference between two related markets or commodities. The purchase of one futures delivery month against the sale of another futures delivery month of the same commodity; the purchase of one delivery month of one commodity against the sale of that same delivery month of a different commodity; or the purchase of one commodity in one market against the sale of that commodity in another market, to take advantage of and profit from a change in price relationships. See also Arbitrage, Switch. The term spread is also used to refer to the difference between the price of one futures month and the price of another month of the same commodity. A spread can also apply to options. It involves buying one futures contract and selling another futures contract. The purpose is to profit from an unexpected change in the *relationship* between the purchase price of one and the selling price of the other. When the spread (price difference) between the two contracts *widens* to become greater than the difference between the two prices, profits are taken by *selling* the lower priced contract and *buying* the higher priced contract. If the spread *narrows*, the result is a *loss*. Spreads involve the *purchase* of one futures contract and the *sale* of a different futures contract in the hope of profiting from a widening or narrowing of the price *difference*. Because gains and losses occur only as the result of a *change* in the price difference - rather than as a result of a change in the overall level of futures prices - spreads are often considered more conservative and less risky than having an outright long or short futures position.

Spreading - The simultaneous buying and selling of two related markets in the expectation that a profit will be made when the position is offset. Examples include: buying one futures contract and selling another futures contract of the same commodity but different delivery month; buying and selling the same delivery month of the same commodity on different futures exchanges; buying a given delivery month of one futures market and selling the same delivery month of a different, but related, futures market.

Squeeze - A market situation in which the lack of supplies tends to force shorts to cover their positions by offset at higher prices.

Steer/Corn Ratio - The relationship of cattle prices to feeding costs. It is measured by dividing the price of cattle ($/hundredweight) by the price of corn ($/bushel). When corn prices are high relative to cattle prices, fewer units of corn equal the dollar value of 100 pounds of cattle. Conversely, when corn prices are low in relation to cattle prices, more units of corn are required to equal the value of 100 pounds of beef. See *Feed Ratio*.

Stock Index - An indicator used to measure and report value changes in a selected group of stocks. How a particular stock index tracks the market depends on its composition; i.e., the sampling of stocks, the weighting of individual stocks, and the method of averaging used to establish an index.

Stock Market - A market in which shares of stock are bought and sold.

Stop-Close-Only Order - A stop order which can only be executed, if possible, during the closing period of the market. See also *Market-on-Close Order*.

Stop Limit Order - A variation of a stop order in which a trade must be executed at the exact price or better. If the order cannot be executed, it is held until the stated price or better is reached again.

Stop-Loss Order - A price order to exit a market at a specified price. A Stop-Loss order will always be an order to do the opposite of an open position. If you are long (bought) you place a stop-loss order to sell. If you are short (sold) you place a stop-loss order to buy.

Stop Order - An order placed with the broker to buy or sell a particular futures contract at the market price if and when the price reaches a specified level. Stop orders are used to limit the amount of losses if the futures price moves against your position. Stop orders are also used to *protect profits*. A sell stop is placed below the market, a buy stop is placed above the market. Sometimes referred to as *Stop Loss Order*.

Straddle - Strategy whereby a trader simultaneously buys an equal number of calls and puts at the same strike price level. See *Spread*.

Strangle - Strategy whereby a trader buys a call and buys a put at different strike prices and/or for different contract months. An option position consisting of the purchase or sale of put and call options having the same expiration but different strike prices.

Street Book - A daily record kept by futures commission merchants and clearing members showing details of each futures transaction, including date, price, quantity, market, commodity, future, and the person for whom the trade was made.

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 *exercise price*.

STRIPS - Separate Trading of Registered Interest and Principal Securities. A book-entry system operated by the Federal Reserve permitting separate trading and ownership of the principal and coupon portions of selected Treasury securities. It allows the creation of zero coupon Treasury securities from designated whole bonds.

Strong Hands - When used in connection with delivery of commodities on futures contracts, the term usually means that the party receiving the delivery notice probably will take delivery and retain ownership of the commodity; when used in connection with futures positions, usually means positions held by trade interests or well-financed speculators.

Support - In technical analysis, the place on a chart where the buying of futures contracts is sufficient to halt a price decline. Also see *Resistance*.

Suspension - The end of the evening session for specific futures and options markets traded at the Chicago Board of Trade.

Swap - The exchange of one asset or liability for a similar asset or liability for the purpose of lengthening or shortening maturities, or raising or lowering coupon rates, to maximize revenue or minimize financing costs. In securities, this may entail selling one issue and buying another; in foreign currency, it may entail buying a currency on the spot market and simultaneously selling it forward. Swaps may also involve exchanging income flows; for example, exchanging the fixed rate coupon stream of a bond for a variable rate payment stream, or vice versa, while not swapping the principal component of the bond.

Swaption - An option to enter into a swap (i.e., the right, but not the obligation, to enter into a specified type of swap at a specified future date.

Switch - Offsetting a position in one delivery month of a commodity and simultaneous initiation of a similar position in another delivery month of the same commodity, a tactic referred to as *rolling forward*. Also see *Arbitrage*.

Synthetic Futures - A position created by combining call and put options. A synthetic long futures position is created by combining a long call option and a short put option for the same expiration date and the same strike price. A synthetic short futures is created by combining a long put and a short call with the same expiration date and the same strike price.

Systematic Risk - Market risk due to price fluctuations which cannot be eliminated by diversification.

Taker - The buyer of an option contract.

T-Bond - See *Treasury Bond*.

Technical Analysis - An approach to forecasting commodity prices which examines patterns of price change, historical prices, rates of change, and changes in volume of trading and open interest, without regard to underlying fundamental market factors.

Technical Rally - A price movement attributed to conditions developing from withing the futures market itself. These conditions include changes in open interest, volume and extent of recent price movement.

Ted Spread - The difference between the price of the three-month U.S. Treasury bill futures contract and the price of the three-month Eurodollar time deposit futures contract with the same expiration month.

Tender - To give notice to the clearing house of the intention to initiate delivery of the physical commodity in satisfaction of the futures contract. Also see *Retender*.

Terminal Elevator - An elevator located at a point of greatest accumulation in the movement of agricultural products which stores the commodity or moves it to processors.

Terminal Market - Usually synonymous with commodity exchange or futures market, specifically in the United Kingdom.

Theta - The derivative of the option price equation with respect to the remaining time to expiration of the option. A measure of the sensitivity of the value of the option to the passage of time.

Tick - The smallest allowable increment of price movement for a contract. Familiarize yourself with the tick size for whatever futures contracts you plan to trade. You will need to know how a price change of *any* given amount will affect the value of the contract. See *Point*.

Time Limit Order - A customer order that designates the time during which it can be executed.

Time-of-Day Order - This is an order which is to be executed at a given minute in the session. For example, *Sell 10 March corn at 12:30 p.m.*

Time Spread - The selling of a nearby option and buying of a more deferred option with the same strike price.

Time-Stamped - Part of the order-routing process in which the time of day is stamped on an order. An order is time-stamped when it is (1) received on the trading floor, and (2) completed.

Time Value - The amount of money option buyers are willing to pay for an option in the anticipation that, over time, a change in the underlying futures price will cause the option to increase in value. In general, an option premium is the sum of time value and intrinsic value. Any amount by which an option premium exceeds the option's intrinsic value can be considered time value. Also referred to as *extrinsic value*.

To-Arrive Contract - A transaction providing for subsequent delivery within a stipulated time limit of a specific grade of a commodity.

Trade Balance - The difference between a nation's imports and exports of merchandise.

Trade Option - A commodity option transaction in which the taker is reasonably believed by the writer to be engaged in business involving use of that commodity or a related commodity. See Commission Rule 32.4.

Trader - (1) A merchant involved in cash commodities; (2) a professional speculator who trades for his own account.

Trading Limit - See *Position Limit*.

Transaction - The entry or liquidation of a trade.

Transfer Trades - Entries made upon the books of futures commission merchants for the purpose of: (1) transferring existing trades from one account to another within the same office where no change in ownership is involved; or (2) transferring existing trades from the books of one commission merchant to the books of another commission merchant where no change in ownership is involved. Also called *Ex-Pit Transactions*.

Transferable Option (or Contract) - A contract which permits a position in the option market to be offset by a transaction on the opposite side of the market in the same contract.

Transferable Notice - A term used on some exchanges to describe a notice of delivery. See *Retender*.

Treasury Bills - Short-term U.S. government obligations, generally issued with 13, 26 or 52-week maturities. See *U.S. Treasury Bill*.

Treasury Bonds (or T-Bond) - Long-term obligations of the U.S. government which pay interest semi-annually until they mature or are called, at which time the principal and the final interest payment is paid to the investor. See *U.S. Treasury Bond*.

Treasury Notes - Same as Treasury Bonds except that Treasury Notes are medium-term and not callable. See *U.S. Treasury Note*.

Trend - The general direction, either upward or downward, in which prices have been moving.

Trendline - In charting, a line drawn across the bottom or top of a price chart indicating the direction or trend of price movement. If up, the trendline is called bullish; if down, it is called bearish.

Underlying Commodity - The commodity or futures contract on which a commodity option is based, and which must be accepted or delivered if the option is exercised. Cash commodity underlying a futures contract.

Underlying Futures Contract - The specific futures contract that is bought or sold by exercising an option.

Underlying Instrument - The contract or commodity that a call option purchaser has the right to buy, or put option purchaser has the right to sell.

U.S. Treasury Bill - A short-term U.S. government debt instrument with an original maturity of one year or less. Bills are sold at a discount from par with the interest earned being the difference between the face value received at maturity and the price paid.

U.S. Treasury Bond - Government-debt security with a coupon and original maturity of more than 10 years. Interest is paid semiannually.

U.S. Treasury Note - Government-debt security with a coupon and original maturity of one to 10 years.

Variable Price Limit - A price limit schedule, determined by an exchange, that permits variations above or below the normally allowable price movements for any one trading day.

Variable Limit - According to the Chicago Board of Trade rules, an expanded allowable price range set during volatile markets.

Variation Margin - During periods of great market volatility or in the case of high-risk accounts, additional margin deposited by a clearing member form to an exchange.

Vault Receipt - A document indicating ownership of a commodity stored in a bank or other depository and frequently used as a delivery instrument in precious metal futures contracts.

Versus Cash - See *Exchange for Physical*.

Vertical Spread - Buying and selling puts or calls of the same expiration month but different strike prices.

Visible Supply - Usually refers to supplies of a commodity in licensed warehouses. Often includes afloats and all other supplies *in sight* in producing areas.

Volatility - A measure of the degree to which price fluctuations have occurred in the past or can be expected in the future. Commodities which are subject to frequent large price changes are said to be highly volatile.

Volatility Quote Trading - Refers to the quoting of bids and offers on option contracts in terms of their implied volatilities rather than as prices.

Volume - The number of contracts traded during a specified period of time. Often the total transactions for one trading day.

Warehouse Receipt - A document certifying the existence and availability of a given quantity and quality of a commodity in storage in a licensed warehouse that is recognized and commonly used for delivery purposes as the instrument of transfer of ownership in both cash and futures transactions.

Warrant - An issuer-based product that gives the buyer the right, but not the obligation, to buy (in the case of a call) or to sell (in the case of a put) a stock or a commodity at a set price during a specified period.

Warrant or Warehouse Receipt for Metals - Certificate of physical deposit, which gives title to physical metal in an exchange approve warehouse.

Wash Sale - Transactions that give the appearance of purchases and sales but which are initiated without the intent to make a bona fide transaction and which generally do not result in any actual change in ownership. Such sales are prohibited by the Commodity Exchange Act.

Wash Trading - Entering into, or purporting to enter into, transactions to give the appearance that purchases and sales have been made, without resulting in a change in the trader's market position.

Weak Hands - When used in connection with delivery of commodities on futures contracts, the term usually means that the party probably does not intend to retain ownership of the commodity; when used in connection with futures positions, the term usually means positions held by small speculators.

Wild Card Option - Refers to a provision of any physical delivery Treasury Bond or Note futures contract which permits shorts to wait until as late as 8:00 p.m. on any notice day to announce their intention to deliver at invoice prices that are fixed at 2:00 p.m., the close of futures trading, on that day.

Winter Wheat - Wheat that is planted in the fall, lies dormant during the winter, and is harvested beginning about May of the next year.

Wire House - See *Futures Commission Merchant (FCM)*.

Writer - The issuer, grantor, or maker of an option contract. See *Option Seller*.

Yield - A measure of the annual return on an investment.

Yield Curve - A chart in which the yield level is plot on the vertical axis and the term to maturity of debt instruments of similar creditworthiness is plotted on the horizontal axis. The yield curve is positive when long-term rates are higher than short-term rates. However, yield curve is negative or inverted.

Yield to Maturity - The rate of return an investor receives if a fixed-income security is held to maturity.