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"Why Some Commodity (and Financial) Futures Contracts Succeed and Others Fail: A Survey of Relevant Research"

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Why do some futures contracts succeed and others fail? Although the U.S. futures markets have evolved in a trial-and-error fashion, a survey of relevant research suggests key elements have determined whether particular futures contracts succeeded or failed. This knowledge could be useful for new financial centers as they build successful futures markets. This paper shows that there are three elements that determine whether a futures contract succeeds or not:

1. There must be a commercial need for hedging;
2. A pool of speculators must be attracted to a market; and
3. Public policy should not be too adverse to futures trading.

"Non-Renewable and Intermittent Renewable Energy Sources: Friends and Foes?"
FAERE Working papers WP 2015.02

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This paper studies the links between non-renewable and intermittent renewable energy sources in the production of electricity. We argue that the relationship between the price of natural gas and investments in solar and wind capacity is non-linear and can be represented by an inverted-U shape. Hence, for relatively low natural gas prices, the two modes of production are substitutes. After a price threshold is reached, the two are complementary. A theoretical model explains this as the trade-off resulting from two forces: the input price differential of these two modes of production and the risks related to the unpredictable nature of renewable energy. Using U.S. state-level data from 1998 to 2012, we find that this relationship is robust to various empirical specifications.
"Expecting the Unexpected: Emissions Uncertainty and Environmental Market Design"  
NBER Working Paper No. w20999

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We analyze the demand for emissions allowances and the supply of allowances and abatement opportunities in California's 2013-2020 cap and trade market for greenhouse gases (GHG). We estimate a cointegrated vector autoregression for the main drivers of greenhouse gas emissions using annual data from 1990 to 2011. We use these estimates to forecast business-as-usual (BAU) emissions during California's program and the impact of the state's other GHG reduction programs. We then consider additional price-responsive and price-inelastic activities that will affect the supply/demand balance in the allowance market. We show that there is significant uncertainty in the BAU emissions levels due to uncertainty in economic growth and other factors. Our analysis also suggests that most of the planned abatement will not be very sensitive to the price of allowances, creating a steep abatement supply curve. The combination of BAU emissions uncertainty and inelastic abatement supply implies a high probability that the price of allowances in California will either be at the price floor, or high enough to trigger a safety valve mechanism called the Allowance Price Containment Reserve (APCR). We estimate a low probability that the price would end up in an intermediate range between the price floor and the APCR. The analysis suggests that cap-and-trade markets, as they have been established in California, the EU and elsewhere may be more likely to experience price volatility and extreme low or high prices than is generally recognized.

Institutional subscribers to the NBER working paper series, and residents of developing countries may download this paper without additional charge at www.nber.org.

"Impact of Supply Chain Transparency on Sustainability Under NGO Scrutiny"  

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Companies are increasingly held accountable for social and environmental sustainability violations committed by their contract suppliers. Government regulation, buyers developing codes of conduct and increasing auditing effort, and additional independent auditing by Non-Governmental Organizations (NGOs) are all important tools in addressing supply chain sustainability issues. In this paper we study the potential use of supply chain transparency as another effective tool. In particular, we study whether the buyer should reveal her supplier list, knowing that revealed suppliers could face a different level of NGO scrutiny than the unrevealed ones. Using an analytical model we incorporate the strategic interactions among a buyer, her suppliers, and the independent NGOs. We are able to characterize their equilibrium actions and find conditions under which the buyer finds it beneficial to reveal her supplier list, and discover different reasons for the buyer to do so. An important finding is that supply chain transparency -- either the buyer's voluntary revelation of her supplier list, or government's mandate for the buyer to
disclose violations -- can lead to better supply chain sustainability, but we also discuss the possibility that more supply chain transparency may lead to lower supply chain sustainability. We offer conditions and intuitive explanations for such findings.

"Risk Spillover in the Commodity Market: Is There Any Financialization Effect?"

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This paper investigates the change in risk transmission mechanism between commodities as a result of the financialization of the commodity market. Relying on intra-day price observations for 25 commodities traded in the US market, the time series of realized variances/covariances is constructed. Risk spillover is then measured by mean of a recently introduce multivariate realized volatility model, the Wishart Autoregressive model (WAR). Risk transmission between commodities belonging to the same sector (Energy, Grains, Soft, Livestock and Metals) has been volatile in the last 10 years and has particularly increased for Energy, Precious Metals and between agricultural commodities and Oil.

This finding is shown to have a profound effect in terms of hedging ratios, optimal portfolio weights and ultimately on the diversification benefits the commodities as asset class were associated to.

"Inventory Control and Intermediation in Global Supply Chains"
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The paper develops a simple theoretical model of inventory control in global supply chains. It identifies a role for intermediaries in managing inventory, and shows that inserting an intermediary as an additional link in a supply chain is profitable when demand volatility is high. It also provides conditions under which the intermediary handling inventory is located in the exporting versus the importing country. Trade liberalization in the form of less lumpy trade is shown to expand the role of export and import intermediaries but to have potentially negative effects on the volume of international trade and social welfare in the importing country.

"Maize Price Volatility: Does Market Remoteness Matter?"

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This paper addresses the role of market remoteness in explaining maize price volatility in Burkina Faso. A model of price formation is introduced to demonstrate formally that transport costs between urban and rural markets exacerbate maize price volatility. Empirical support is provided
to the proposition by exploring an unusually rich data set of monthly maize price series across 28 markets over 2004-13. The methodology relies on an autoregressive conditional heteroskedasticity model to investigate the statistical effect of road quality and distance from urban consumption centers on maize price volatility. The analysis finds that maize price volatility is greatest in remote markets. The results also show that maize-surplus markets and markets bordering Côte d’Ivoire, Ghana and Togo have experienced more volatile prices than maize-deficit and non-bordering markets. The findings suggest that enhancing road infrastructure would strengthen the links between rural markets and major consumption centers, thereby also stabilizing maize prices.