

What a commodity trader does

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A commodity trader buys raw materials where they are produced and sells them where they are consumed. The simplicity of this description conceals a business of considerable complexity. The trader transforms commodities in three dimensions. In space, it transports them from the mine, the oil field or the farm to the smelter, the refinery or the mill. In time, it stores them from the moment of production to the moment of consumption, while it transforms their form by blending, processing or grading them to meet the specifications of the buyer.¹ The trader earns a margin on each of these transformations by knowing more about the markets, the logistics and the counterparties than its competitors.

The physical trader differs from the financial speculator. It takes delivery of the goods, charters the ships, arranges the storage, inspects the quality and issues and receives the documents. It also bears the risks of the physical chain: that the cargo is lost or damaged, that the buyer does not pay, that the seller does not deliver, that the goods do not meet the specification, that the ship is detained or that the port is closed. Against the price risk, the trader hedges on the futures exchanges, above all the London Metal Exchange for metals, the Intercontinental Exchange for oil and the Chicago exchanges for agricultural products. Its profit therefore depends on the margins of the physical business and on its skill in managing the difference between physical and futures prices.²

The margins of the physical trade are thin, often a fraction of a per cent of the value of the goods. The trader's profit therefore depends on volume, on the efficient use of capital and on the ability to exploit moments of market dislocation. At such moments, when prices diverge between regions, between delivery dates or between grades, a trader with the goods in the right place at the right time can earn exceptional returns. The years after 2022 were such a moment: when the Russian invasion of Ukraine disrupted the markets for energy, grain and metals, the trading houses

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earned record profits. The extraordinary profits of the energy and commodity traders of Geneva from 2022 onwards were large enough to raise that canton's payments into the national fiscal equalisation significantly.³

1 Notes

1. Craig Pirrong, "The Economics of Commodity Trading Firms", white paper, University of Houston, March 2014, research financially supported by Trafigura, bauer.uh.edu (PDF): "Commodity trading firms are all essentially in the business of transforming commodities in space (logistics), in time (storage), and in form (processing)." For the history of the industry see also Javier Blas and Jack Farchy, *The World for Sale* (2021). ↩
2. Craig Pirrong, "The Economics of Commodity Trading Firms", white paper, University of Houston, March 2014, research financially supported by Trafigura, bauer.uh.edu (PDF): hedging on futures markets "involves the exchange of flat price risk for basis risk", the risk of changes in the difference between the price of the commodity hedged and that of the hedging instrument. The allocation of the exchanges by commodity group in the text is general market knowledge and not taken from this source. ↩
3. fairer-nfa.ch, "Die Ausgleichszahlungen steigen 2026 stark an": Geneva's increase stems from extraordinarily high profits of energy and raw material trading companies from 2022 onwards. ↩

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