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What are spreads all about?

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An **intra-commodity spread** is long one future and short another. Both have the same underlier, but they have different maturities. An **inter-commodity spread** is a long-short position in futures on different underliers, both typically have the same maturity. Spreads can also be constructed with futures traded on different exchanges (**inter-exchange spread**). Typically this is done using futures on the same underlier, either to earn arbitrage profits or, in the case of commodity or energy underliers, to create an exposure to price spreads between two geographically separate delivery points. For speculators, spread trading offers reduced risk compared to trading outright futures. This is because the long and short futures that comprise a spread are usually correlated, so they tend to hedge one another. For this reason, exchanges generally have less strict margin requirements for futures spreads.

How can you make money trading spreads?

By playing a spread one may want the spread to widen or for the spread to narrow. With a spread, you follow the relationship, or difference between the contracts, without having to pick a market direction. When you trade an outright futures position there is only one way that you can make money. If you buy, the market must go up and if you sell, the market must go down. With a spread trade, you can make money whether the markets move higher or lower. If the side you bought goes up more than the side you sold, you make money. If the side you bought goes up and the side you sold remains even, you make money. If the side you bought does not move and the side you sold goes down, you make money. If the side you sold goes down more than the side you bought, you make money. Finally, if the side you bought goes up while the side you sold goes down, you stand to profit even more. Of course, in the above scenarios if the reverse of what is described above happens, you would lose money. As far as I know, there is no trading method that is risk free. However, spreads add flexibility and versatility to a trader's arsenal, and generally with less risk. The key here is to find a spread that has a favorable risk/reward dynamic which should be at least 3:1.

What I like about spreads.

The exchanges recognize that spread trades have **lower volatility** and usually present less risk than a straight futures trade. This is reflected in **lower margin** requirements. Spreads do not count on a particular market to go up or down; rather, it is the **price relationship** between two markets that determines the success of the trade. Spreads trend and swing well; and their chart pictures respond to the standard tools of **technical analysis**. When you consider that spread **trading opportunities** include not only the commodity, but also the number of contract months available to trade, plus the potential for inter-market and inter-exchange spread trades, the possibilities are vast. Some benefits are using spreads as an alternative to using protective stops, legging in and out of spreads, and entering a spread as a defensive measure to reduce or avoid the catastrophic effects of a lock limit move against you. Seasonal and other patterns are evident in spreads and it is very satisfying to maintain and manage successful trades lasting weeks and even months at a time. (**Staying power**)

What I do not like about spreads.

Not all spreads are recognized by a given exchange as carrying lower risk. Hence, there may be **no reduction in the margin requirements**. Learning the concept of "widening" and

"narrowing". The confusion is created because when you enter a spread trade it can be done at either a positive or negative price. Additionally **pricing spreads, orders and liquidity can sometimes be confusing**. Pricing spreads can be difficult when doing "inter-market" or "inter-exchange" spreads. Some commodities are priced differently and have different units of measure and contract values. The **absence of stops** may also be a disadvantage to certain traders. A spread trade involves **two futures transactions** plus the commissions and fees that go with them.

The Best Spread I have seen in some time.

Long Corn / Short Wheat

Wheat has traded at a \$3.00 premium to Corn twice in history (*presently above \$5.00*); in 1974 and 2007. The average spread between wheat and corn over the last 30 years is \$1.00-\$1.50. With corn demand expected to expand for 08/09 and prices likely to climb to avoid a loss in planted acreage to other crops, corn needs to move to higher levels. With wheat prices currently at a record high price these prices are likely to attract a significant jump in wheat planted acreage much like corn did last year (*the result corn lost \$1.00 in the futures market in 60 days or a \$5,000 move per contract*). What is most attractive is the risk/reward dynamic which we currently view as 5:1.

Contact us at 888-920-9997 or via e-mail at <http://www.mbwealth.com/contact.html> for further details.

Matthew Bradbard is from New England and studied Finance at Northeastern University & the University of Sydney. He has been a member of the NFA since 2000.

Matthew Bradbard founded and remains President of MB Wealth Corporation. Subsequent to establishing MB Wealth, he worked at various brokerages over his tenure in commodities. Matthew Bradbard has helped identify and develop several trading strategies in numerous commodities markets for his clientele. He has always been a hands-on broker with proficiency in fundamental as well as technical analysis. Over the years he has cultivated relationships with floor traders, farmers, grain marketers, and end users.

His trading decisions are based largely on technical analysis with an emphasis on position trading, identifying trending commodities, and capitalizing on volatile movements both on the long and short side. Fundamentals are also a major consideration; with the wild weather patterns and insatiable demand from emerging markets like India and China for raw materials need always be considered. He expects the secular bull market in commodities to continue for years to come.

Matt strives to offer an informed perspective, helping clients to limit their emotions and greed though executing a logical trading plan. You can reach him at 888-920-9997 or via email at contact@mbwealth.com. You can also obtain a timely market commentary and trading strategies from Matt in his Weekly Commentary issued every Monday. If you wish to get on MB Wealth's distribution list email us at contact@mbwealth.com. For a limited time Matt is also willing to review current Commodity Portfolios to give you his unbiased opinion on open positions as well as the overall environment on Commodities and what he feels is next to come.

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perhaps most importantly what is on our radar. It is very important to stay informed when trading commodities especially when utilizing leverage because in some instances the days, hours, even minutes make a difference.

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Are you as diversified as you should be? What sectors are you invested in?

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