

# **MCX ISF Presentation**

## **Price Risk Management in Cotton & Kapas**

**9<sup>TH</sup> JANUARY, 2024**

**INDO AGRI FOOD FEED INTERNATIONAL, MAHABALIPURAM, CHENNAI**

There are different type of Commodity Market:

**Spot Market:** bought & sold for cash and the delivery takes place immediately.

Physical contracts for cotton are not standardized and specific to each transaction (volume, quality, location, etc).

**Forward Market:** The trading takes place directly between the buyer & seller.

Terms such as Qty, Quality, Delivery date and price and negotiated between buyer & Seller (two person only).

**Futures Trading:** Future trading in commodities results in transparent and fair price discovery due to the large scale participation from all entities associated with the value chains involved.

Future market/ financial markets have uniformed standard contracts:

1) Delivery location/place, 2) Delivery procedures, 3) Quantity (Lot size), 4) Quality (like length, mic, moisture, trash, grade) and 6) Price etc

## Did you Know?

The first organized futures market – Bombay Cotton Trade Association was started in 1875. Trading in certain commodities was stopped in 1960's and 1970's and resumed only in 2002-03.

## What is Commodity Exchange ?

- In simple terms, a commodity exchange is a market place where various commodities are electronically traded
- Commodities are traded in standardized futures contracts with a expiry date
- Exchanges are regulated by SEBI
- Exchange has no role in pricing of futures contracts
- Buyers and sellers determine the price

## What is the need of Commodity Futures Exchange ?

- A future exchange provides future price signals
- Fair Price Discovery
- Price Risk Management/Hedging
- In the absence of price signals, one has access only to current prices.
  - a) he can not plan for the future and
  - b) policy makers would not be able to prepare for future plan.

# ACTIVE COMMODITY FUTURES IN INDIA

## BULLION

Gold, Silver,  
Diamond



## ENERGY

Crude Oil  
Natural Gas

**SEBI has notified 91 commodities, where exchanges may launch derivative contracts**

## METALS & ALLOYS

Aluminium, Copper, Lead  
Nickel, Zinc, Brass, Steel

## AGRICULTURAL

**Grains:** Barley, Maize, Wheat



**Spices:** Black Pepper, Cardamom,  
Coriander, Jeera, Turmeric



**Fibre:** Cotton (Bales), Kapas, Raw Jute



**Oil Complex:** Castorseed, CPO,  
Soybean, Soyoil, RBD Palmolein



**Others:** Guarseed, Guargum, Mentha  
Oil, Isabgul, Rubber, Sugar



## COMMODITIES TRADED AT EXCHANGE

### PRECIOUS METALS



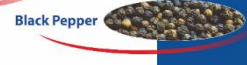
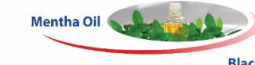
### BASE METALS



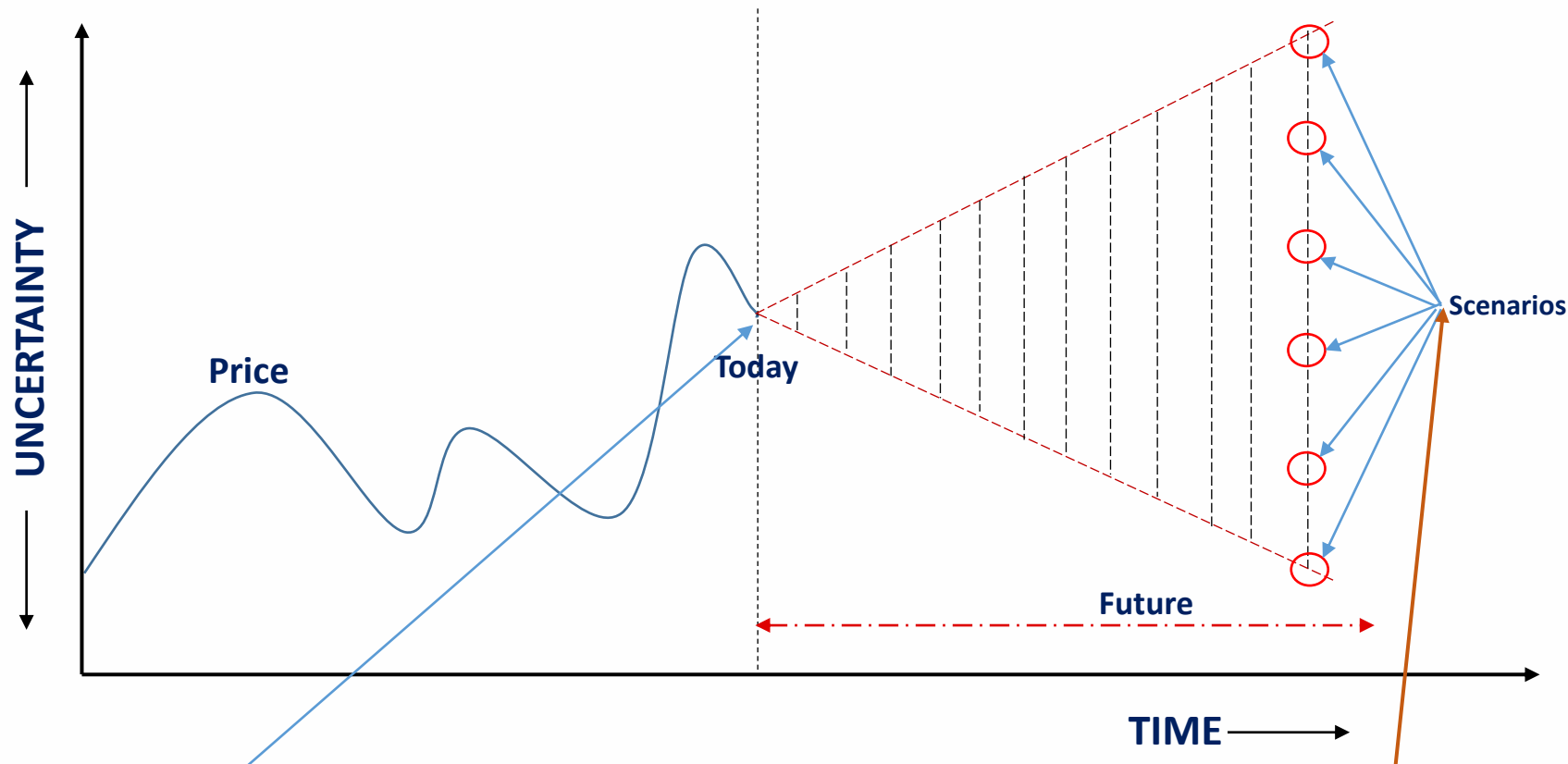
### ENERGY



### AGRI



# WHAT IS COMMODITY PRICE RISK/HEDGING ?



Producer or Consumer or any Value Chain Participant/Commodity Stakeholder at “Today” is not aware of what might happen in the future.

There could be favourable / unfavourable scenarios in the time unknown (i.e. Future). Hence, it is a necessary to Hedge “Today” and be locked-in at a desired / current price level.

- Taking a position in the futures market that is opposite to a position in the physical market
- Reduces risks associated with unpredictable changes in price
- The objective behind this mechanism is to offset a loss in one market with a gain in another

## HEDGERS

- Corporates
- Farmers
- Producers & Consumers
- Intermediaries in Spot Markets
- Merchandisers
- Importers & Exporters
- Foreign Hedgers (EFEs)

**Transfer  
of  
Risk**

## INVESTORS

- Speculators
- Arbitragers
- AIF (CAT III)
- Mutual Funds
- Portfolio Management Services



### DID YOU KNOW ?

HEDGE | DISCLOSE | BE COMPLIANT - LISTED ENTITIES TO DISCLOSE COMMODITY PRICE RISK & HEDGING ACTIVITIES IN ANNUAL REPORT (SEBI-LODR)

# COTTON HEDGING ILLUSTRATION

## Cotton Producers/Stockists – Locks in Price

Date	Physical	Futures
January – 2024	Holding Stock	Sell Futures
March- 2024	Sales at ruling price	Buy Futures

Time	Spot Price (Rs./candy)	Futures Price (Rs./Candy)	
January	55,000	Sell 1 lot of March	56,500
March	54,000	Buy 1 lot of March	55,500
Result	Loss of Rs 1000/candy	Gain of Rs 1000/candy	

Thus, the FPO or ginner protected himself from falling prices in the spot market with an effective selling price of Rs 55,000 per candy.

## Cotton Exporter/Spinners – Locks in Price

Date	Physical	Futures
January – 2024	Has to purchase cotton	Buy Futures
March- 2024	Buys at ruling price	Sell Futures

Time	Spot Price (Rs./candy)	Futures Price (Rs./candy)	
January	55,000	Buy 10 lots of March	56,500
March	56,000	Sell 10 lots of March	57,500
Result	Loss of Rs 1,000 per candy	Gain of Rs 1,000 per candy	

Thus, the exporter or spinners protected himself from rising prices in spot market with an effective buying price of Rs 55,000 per candy.



- **Weather Conditions:** Climate related events, such as droughts or hurricanes, can impact cotton yields and subsequently affect prices.
- **Global Demand:** Changes in consumer demanding for cotton products influence prices in the market.
- **Prices ruling in the international markets**
- **Forex rates**
- **Geo-Political factors – Global and Indian**
- **Trade policy and Regulations:** Tariff & Non-Tariff Barriers including taxes, quota
- **Economic Factors:** Economic conditions e.g. recession, inflation
- **Commodity - specific events & statistical releases –**
  - Demand & Supply Scenario (Global as well Domestic)
  - Inventory Levels

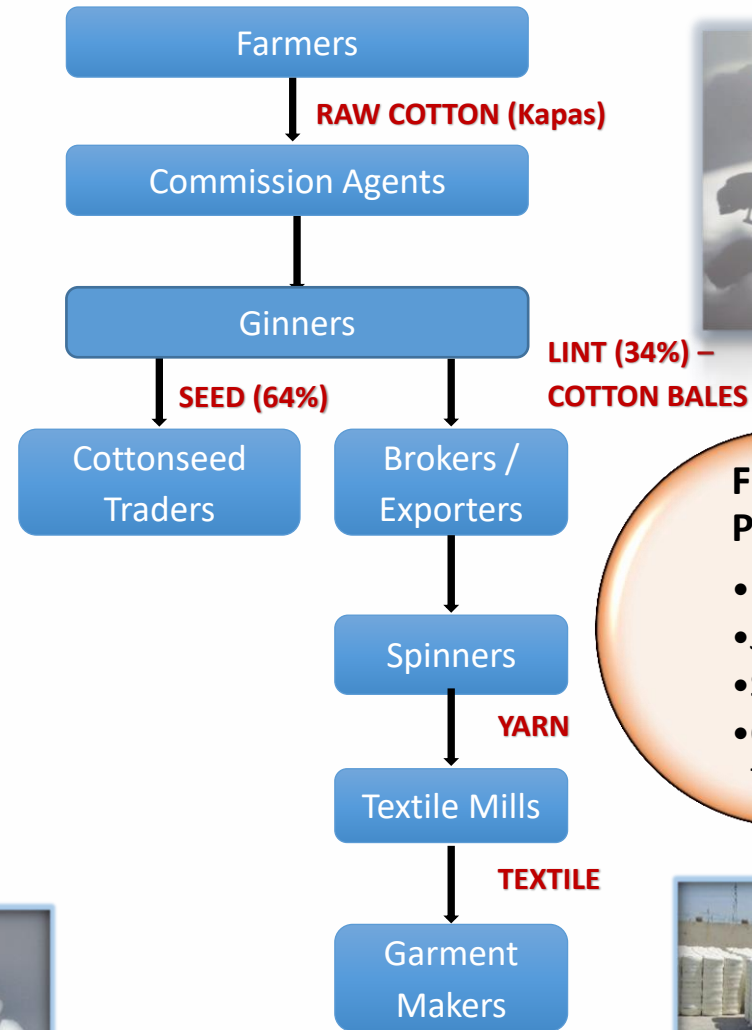


## DID YOU KNOW ?

YOU CAN DIVERSIFY YOUR PORTFOLIO WITH COMMODITIES DERIVATIVES - BULLION | BASE METAL | ENERGY | AGRI

# VALUE CHAIN & MCX COTTON CONTRACT SNAPSHOT

- Approximate Indian market size : ₹ **1,01,830 Crores**  
(Prodn 343 lakh bales (CY 2022-23) and Avge Price Rs 29,688/bale, 1st Oct to till 30<sup>th</sup> Sep)
- Annualized price volatility in 2022-23: 15.20% & exposure to price risk: ₹ **15,478 Crores**
- At MCX
  - Delivery more than **21 lakh bales** (1 bales = 170Kgs) (till December'23)
  - **More than 80%** correlation with ICE prices
  - Contract specifications covers **more than 70%** of cotton grown in India
  - The market operational both morning and evening - **price discovery** when global markets are active
- Exempted from paying **Commodities Transaction Tax**



# 29 MM COTTON CONTRACT SPECIFICATION

Parameter	Specification
Price Quote	Rs./ Candy
Trading & Delivery Unit	48 Candy (100 bales)
Tick Size	Rs. 20
Contract Months	Bi-Monthly – April, June & August (for current season only), Next Season onwards: Nov, Jan, Mar, May, Jul and Sep
Expiry Date	Last trading day of month
Delivery Logic	Compulsory Delivery
Maximum Allowable Open Position	<p><b>At Client level:</b> 9,600 Candy (20,000 bales) <b>At Member level –</b> 96,000 Candy (2,00,000 bales).</p> <p><b>For Near Month Delivery:</b> <b>At Client level:</b> 2,400 Candy (5,000 bales).</p> <p><b>Near month member level position limit shall be one fourth of the overall member position limit.</b></p>

STAPLE LENGTH (mm)	
<b>Basis: 29.00 mm</b>	No Premium on or above 29 mm
<b>Below 29 upto 28</b>	Discount of 1%
<b>&lt; 28.00</b>	Rejects

RD VALUE and +b	
<b>Basis</b>	75
<b>&lt; 75 up to 74</b>	1% Discount
<b>&lt; 74 to 73</b>	1.5% Additional discount
<b>Below 73</b>	Reject
<b>+b</b>	Upto 10.20 accept and above 10.20 rejects

STRENGTH
<b>Minimum 28 Gtex</b>

TRASH	
<b>2%&lt;= Trash &lt;3%</b>	Premium :1:1
<b>Of 1</b>	0.5
<b>Basis</b>	3 %
<b>&gt; 3 up to 4%</b>	Discount 1:1
<b>&gt; 4%</b>	Reject

MOISTURE	
<b>Basis</b>	<b>9%</b>
Accept upto 10%	1:1 Discount
Above 10%	Reject

MICRONAIRE	
<b>3.7 to 4.6</b>	No Premium / Discount
<b>Below 3.7 upto 3.5</b>	0.5% Discount
<b>Above 4.6 upto 4.9</b>	0.75% Discount
<b>Below 3.5 &amp; Above 4.9</b>	Rejects

For detailed contract specifications, please refer latest Exchange circulars

# KAPAS CONTRACT SPECIFICATION

Parameter	Contract Specification
Price Quote	Rs./ 20 Kg
Trading & Delivery Unit	4 MT (200 maund of 20 kg)
Tick Size	50 Paise
Contract Months	Mar, April and Nov
Delivery Logic	Both Option
Maximum Allowable Open Position	<p><b>At Client level - 1,80,000 MT</b>  <b>At Member level - 18,00,000 MT</b>                      or 15% of the market wide open position whichever is higher.</p> <p><b>For Near Month Delivery:</b>  <b>At Client level: 45,000 MT.</b>  <b>At Member level - 4,50,000 MT</b> or                      15% of the market wide open position whichever is higher.</p>

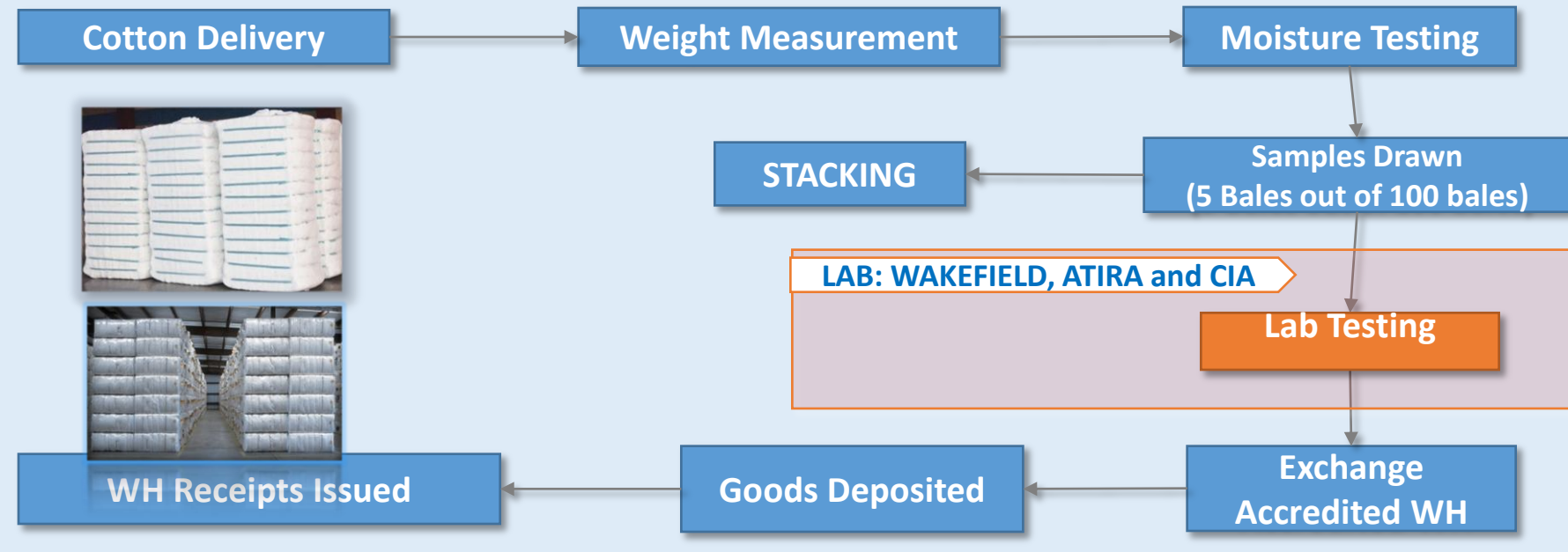
Quality Specification	
Staple Length (Raw Cotton)	Basis: 29 mm
Outturn	Minimum 34%
Trash Content	Maximum 3%
Microniare	3.6-4.8
Strength	Minimum 29 G Tex
Moisture	Maximum 8%

# DEPOSIT PROCEDURES FOR COTTON

WSPs (Yamada logistic, Shri Shubham Logistic, Star Agri and Steinweg Sharaf Pvt Ltd. )

For Warehouses details -

<https://www.mcxcl.com/warehousing-logistics/Overview>



## Delivery Centers

Rajkot (basis Centre)

Mundra

Kadi

Jalna

Yavatmal

Adilabad

Indore

Approximate cost for giving delivery of 100 bales or 48 Candy	1 lot (48 Candy or 100 bales)
Sampling & Assayer's charges (Rs 3500 for 100 bale without GST)	Rs. 3500*
Unloading & Stacking at Warehouse ₹30/bale approx.	Rs. 3,000
Warehouse charges @ ₹2.85 / bale / day including insurance charge.	285 / day
Standard Deduction	(based on month of deposit)

Procedure for Deposit at the warehouse: Prior intimation of minimum one working day is required by way of entry "deposit request" into CDSL Commodity Repository Ltd. ("CCRL") application and intimation to sampling agency for making arrangements for sampling.

\* Minimum 2 lots should be deposit on the same day. In same warehouse.

MCX Cotton Delivery	
Season (Oct-Sept)	Qty (Bales)
2011-12	80,500
2012-13	1,54,700
2013-14	71,500
2014-15	1,87,600
2015-16	83,400
2016-17	96,200
2017-18	1,86,600
2018-19	3,98,500
2019-20	2,35,975
2020-21	3,13,450
2021-22	2,50,075
Oct'22	2,450
Nov'22	23,075
Dec'22	18,625

Stocks as on January 05, 2024	
Stock eligible for Exchange Delivery	2,496 candy (5,200 bales)
Stock in process for eligibility	
Storage Capacity	

Stock position in the accredited warehouses -  
<https://www.mcxcl.com/warehousing-logistics/stock-position>

- Can take sowing decision based on next season futures prices – Next season futures get launched on MCX platform before sowing season starts (on 1st May).
- New season cotton contracts (Nov and January contracts) would be available from 1st May onwards.
- Sell futures to lock-in price at exchange platform - Farmers would remain more or less unaffected by any upside or downside movement in price till the time of harvest.
- Efficient price discovery ensure competitive price to participants.
- Good liquidity & depth in future contracts provide easy entry & exit at minimum impact cost
- Exchange guarantee counter party risk - Good delivery and payment are assured by the exchange
- Enhances credit worthiness and ability to borrow

Approximately 500 kg of Kapas required for making 1 bale cotton (170 kg lint)	
Kapas Price (assumed)	7000 ₹ / 100 Kg
50,000 Kg Kapas Price (to make 100 bale cotton)	$(7000 * 500) = 35,00,000$ ₹
Ginning Charge (Charge to convert raw Kapas to bale cotton)	1000 ₹ / bale
Ginning Charge for 100 bales	$(1000 * 100) = 1,00,000$ ₹
<b>Total Cost (Kapas + Ginning charge)</b>	<b><math>(Rs\ 35,00,000 + Rs\ 1,00,000) = Rs\ 36,00,000</math></b>
Cotton Candy Price	Rs 57,000/candy or 27,360/bale
Cotton Candy cost for 48 candy (100 bales)	$(57,000 * 48) = 27,36,000$ ₹
Cotton Seed Price	30 ₹ / kg
Price of Seeds out of 50,000 Kg Kapas*	$(50,000 * 0.64 * 30) = 9,60,000$ ₹
<b>Total Value (Cotton bale + Cotton Seed)</b>	<b><math>(27,36,000 + 9,60,000) = 36,96,000</math> ₹</b>
<b>Profit (Total Value – Total Cost)</b>	<b><math>(36,96,000 – 36,00,000) = 96,000</math> ₹</b>



Sr. No.	Activities for utilization of fund	Subsidy/Reimbursement to the extent
a)	Assaying charges	100%
b)	Warehouse rent/storage charges	100%
c)	Cost of Bags, drums, etc.	100%
d)	Transportation cost	50%
e)	Funding of Cost of Mark to Market	100%
f)	Broker Fee	100%
g)	Repository related fee	100%
h)	Mandi Tax	100%
i)	Cleaning, drying and sorting charges	50%
j)	Clearing corporation fees	100%
k)	Any other activity as may be permitted by SEBI	100%



FPO'S CAN GET THE BENEFITS FOR QUANTITY ASSAYING, REPOSITORIES, BROKER (PRAGATI) WAREHOUSE REIMBURSEMENT REIMBURSED

- Choose the Member Broker
- Fulfill KYC at Broker level
- Arrange for minimum initial margin requirement
  - Update yourself on Mark-to-Margin requirements
- Know Exchange regulations and byelaws
- Select the commodity/ product to trade
- Read the Dos and Don'ts
- Know and distinguish among:
  - Brokerage and Transaction Charges
  - Margins, Taxation and Stamp Duty
  - Default Penalties and Arbitration



## DO'S

- Trade only through **Registered Members** of the Exchange.
- **Visit Exchange web site** for Members Details to check if the member is registered with Exchange
- Fill standard '**Know Your Client**' (KYC) form before you commence trading
- **Update your mobile number** and/or email id with your broker
- Insist with your **Broker to upload your mobile number** and/or email-id in the Exchange UCC database.
- Insist on getting a **Unique Client Code (UCC)** and ensure all your trades are done in UCC
- Insist on reading the standard '**Risk Disclosure Document (RDD)**' & '**Rights & Obligation of Investor**'

## DON'TS

- Do not be influenced by indicative returns or promises made
- Do not get carried away by luring advertisements, rumors, hot tips
- Do not make payments in cash/take any cash towards margins and settlement
- Do not sign blank DPs while furnishing securities deposits
- Do not pay brokerage in excess of the rates prescribed by the Exchange

SEBI has launched New Investor website  
Visit; <https://investor.sebi.gov.in>



Scan QR Code to  
Participate in Survey



Dive into Money Matters to grasp Personal Finance concepts.



Educational Resources, related to investments, including securities market



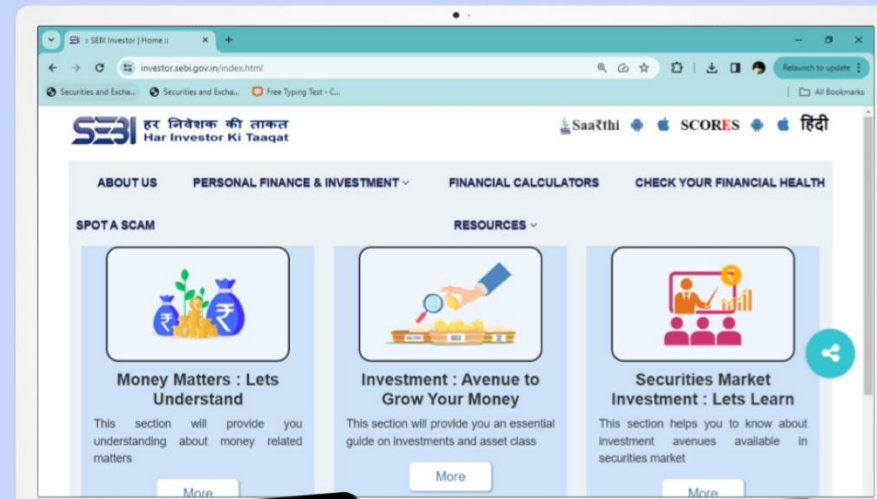
Access a range of Financial Tools and Calculators.



Evaluate your Financial Health with the easy check.

Join on a journey of informed decision-making and confident participation in the securities market.

UNLOCK THE **WEALTH OF KNOWLEDGE**  
AT THE SEBI INVESTOR WEBSITE  
*Empower yourself in the world of investing*



TO VISIT THE SEBI  
INVESTOR WEBSITE,  
SCAN THE QR CODE



# THANK YOU

Disclaimer: The Contents do not constitute professional advice or provision of any kind of services and should not be relied upon as such. MCX does not make any recommendation and assumes no responsibility towards any investments / trading in commodities or commodity futures done based on the information given in the website and any such investment / trade are subject to investment / commercial risks for which MCX shall not be responsible. If financial, investment or any other professional advice is required, please seek advice of competent professionals.