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INTERVIEW

Indian agricultural commodity derivatives market — In conversation with S Sivakumar, Divisional Chief Executive, Agri Business Division, ITC Ltd.

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Abstract Though the agricultural sector contributes significantly to the Indian economy, it faces several bottlenecks, one of those being the antiquated laws governing agricultural marketing and price discovery, leading to low price realization by Indian farmers. In India, six national level exchanges offer commodity derivatives contracts on commodities, with some having electronic spot exchanges to facilitate spot trading of commodities. However, farmers' participation in these exchanges has been poor. ITC-ABD, one of the largest aggregators and exporters of Indian agri-commodities, has started using these exchange platforms to hedge price risk. With experience of over three decades in the agricultural sector, Mr. S. Sivakumar has a deep understanding of the commodity markets and the needs of Indian farmers. This interview aims to get an insight into his views on increasing farmers' participation in commodity derivatives trading and more importantly, to understand ITC-ABD's commodity hedging strategy.

Context note

Preparatory to the interview with Mr. S. Sivakumar, Divisional Chief Executive, Agri Business Division, ITC, the context note provides a brief overview of the different aspects of the Indian agricultural market and the Indian commodity derivatives market. The ITC Agri Business Division's venture into commodity hedging through exchanges predominantly revolves around soyabean and soyaoil price risk management. Hence, in addition to the Indian agricultural market and commodity derivatives market, this context note also introduces the soyabean and soyaoil market in India.

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Indian agricultural market

India's agricultural production has improved significantly since independence. India is now a major producer of many agricultural commodities, fruits, and vegetables. According to the Ministry of Agriculture annual report (2013–2014), India ranks within top two global producers of rice, wheat, sugarcane, cashewnut, pepper, cotton, jute, spices, potato, tomato, and tea. As per the Department of Animal Husbandry, Dairying & Fisheries annual report (2013–2014), India is also the world leader in milk production and ranks third in egg production. Agriculture contributes to the Indian economy in many significant ways. It provides employment to around 51% of the total population. Data provided by the Planning Commission of India indicates that in 2013, agriculture contributed 14% of the total GDP, and agricultural exports accounted for 11% of the total exports from India.[1] According to the Agricultural & Processed Food Products Export Development Authority (Apeda, 2013) report, total export of agricultural commodities and value-added products stood at USD 37,029 million in 2012–13, which grew at 13.6% over the previous year. This report also mentioned companies such as Dabur, Godrej, ITC, Parle, Amul, Haldiram, Marico, Alok Industries, Nestle, Cargill, Pepsico, and Danone as major agro exporting companies from India.

In spite of its significant contributions to the Indian economy, Indian agriculture suffers from several weaknesses. India's agricultural yield is among the lowest in the world. Timely arrival of monsoon and the quantum and distribution of rainfall are crucial for farm output, as almost 55% of the area under cultivation depends on rain. Even areas with irrigation facility are under severe strain as overuse of groundwater has led to fall in groundwater level. Every year India loses huge amounts of agri-produce due to lack of adequate warehousing and cold storage facilities. Answering a Right to Information (RTI) query in 2013, the Food Corporation of India (FCI), which procures majority of wheat and rice produced in India, reported that as much as 1,94,502 tonnes of food grain was wasted during 2005–2013 due to inadequate storage facility (The Economic Times, 2014).

Warehouse facilities for agricultural commodities in India

Availability of warehousing is not only crucial for storage of food grains, but it also provides an opportunity for farmers to get higher price realization. Lack of adequate warehousing facilities forces farmers to sell during harvest period at low prices. According to a Planning Commission report (2011), the total warehousing capacity in India is about 108.75 million tonnes (Table 1).

During 2010–11, the total food grains and pulses production stood at 244.49 million tonnes (Reserve Bank of India Statistics [2]). Even if one were to consider that the total production of food grains and pulses is spread over the Kharif and Rabi seasons, and discounting any storage requirements for fruits and vegetables, there is a gross shortfall in total warehousing capacity.

Table 1 Warehouse storage capacities (2010–11).

Name of organization/sector	Storage capacity (in million tonnes)
Food Corporation of India (FCI)	32.05
Central Warehousing Corporation (CWC)	10.07
State Warehousing Corporation (SWC)	21.29
State Civil Supplies	11.30
Cooperative sector	15.07
Private sector	18.97
Total	108.75

Data Source: Planning Commission of India Report (2011) titled "Report of Working Group on Warehousing Development & Regulation for the Twelfth Plan Period (2012–2017)".

To increase warehousing capacity, the Government of India (GoI) introduced the Warehousing (Development & Regulation) Act 2007 and set up the Warehousing Development & Regulatory Authority (WDRA) in 2010. The GoI also made warehouse receipts negotiable in 2011, under which, ownership of warehouse receipts can be transferred between buyers and sellers without physically transferring the underlying goods. This reduces handling costs by eliminating avoidable additional transportation. Since its inception in 2010, the WDRA has already registered 365 warehouses and has permitted issuance of negotiable warehouse receipts (NRWs) for 115 agri-commodities and 26 horticulture commodities. In the 2013–14 budget, the GoI allocated INR 5000 crores to the National Bank for Agriculture and Rural Development (NABARD) for providing loans to companies as well as to individual entrepreneurs for augmenting warehousing, cold storage, and cold chain infrastructure. Recently some private players such as National Bulk Handling Corporation, Star Agriwarehousing and Collateral Management Limited, and Guru Warehousing Corporation have started creating new warehouses. Notwithstanding these positive developments, availability of adequate warehousing facilities continues to be a bottleneck.

Spot market for agricultural commodities and agricultural produce market committees (APMCs)

Physical trading of agricultural commodities in India falls under the jurisdiction of the state governments. Each state has its own Agricultural Produce Market Committee

[1] Planning Commission of India "Gross Domestic Product (GDP) from Agriculture and Allied Sector and its Percentage Share to Total GDP(1954-55 to 2014-15)" available at http://planningcommission.nic.in/data/datatable/data_2312/DatabookDec2014%2043.pdf.

[2] Reserve Bank of India Statistics on "Agricultural Production in India" available at http://dbie.rbi.org.in/DBIE/dbie.rbi?site=statistics.