



भारतीय रिजर्व बैंक
RESERVE BANK OF INDIA

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May 28, 2015

The Chairman and Managing Director/Chief Executive Officer
All Scheduled Commercial Banks
(Excluding Regional Rural Banks)

Dear Sir / Madam,

Hedging of Commodity Price Risk - Creating awareness among borrowers

Banks provide a number of credit facilities to customers engaged in activities related to agriculture. One of the prominent, *albeit* indirect, risks in this sector is that of volatility in agricultural commodity prices. Generally, this risk is more pronounced in cases where agricultural borrowers do not hedge the underlying agri-commodity price risk. Hedging of the agri-commodity price risk is beneficial to both the borrowers and the banks and, hence, it is desirable that a risk management culture is fostered amongst the stakeholders including agri-borrowers and banks.

2. Presently, hedging tools including derivatives are available in the Indian market, but these are not being used extensively due to lack of awareness of the products or their inherent complexity.

3. With a view to developing strong risk management capabilities to manage agri-commodity price risk, it is felt that banks should encourage hedging by the agri-borrowers by creating awareness amongst them regarding the utility and benefits of hedging through agri-commodity derivatives. At the same time, banks must keep the sophistication, understanding, scale of operation and requirements of their agri-borrower in mind while advising on the availability and use of these instruments.

4. To begin with, banks may encourage large agricultural borrowers such as agricultural commodity processors, traders, millers, aggregators, etc., to hedge their commodity price risk. The hedging can be through agri-commodity derivative products available on recognised exchanges in India. Banks may educate their customers about the suitability and appropriateness of using these products for hedging specific exposures so that these customers can take an informed decision, lessening the scope for mis-selling of these derivatives.

Yours faithfully,

(Sudarshan Sen)
Chief General Manager-in-Charge