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Cotton Exchange Building, 2nd Floor, Cotton Green, Mumbai - 400 033
Phone: 3006 3400 Fax: 2370 0337 Email: cai@caionline.in
www.caionline.in

Technical Analysis

Price outlook for Gujarat-ICS-105, 29mm and ICE cotton futures for the period 26/09/17 to 31/10/17

(The author is Director of Commtrendz Research and the views expressed in this column are his own and the author is not liable for any loss or damage, including without limitations, any profit or loss which may arise directly or indirectly from the use of following information.)

We will look into the Gujarat-ICS-105, 29mm prices along with other benchmarks and try to forecast price moves going forward.

EXPERT's Column

Shri Gnanasekar Thiagarajan
Director, Commtrendz Research

As mentioned in the previous update, fundamental analysis involves studying and analysing various reports, data and based on that arriving at some possible direction for prices in the coming months or quarters.

Some of the recent fundamental drivers for the domestic cotton prices are:

- Cotton futures edged higher as the uneven monsoon seemed to have affected the kharif output. Hopes of an increase in MSP has also added to the sentiment. New crop prices have steadied or rather improved following reports of slight delay in arrivals due to the recent rains across most of India. There seems to be a shortfall in current physical cotton stock, especially of good quality cotton.
- The world's top cotton buyers, all in Asia, are flocking to India to secure supplies after fierce storms in the US, the biggest exporter of the fibre, affected the size and quality of the crop. Hurricanes Harvey and Irma caused widespread damage to the crop in Texas and Georgia, major cotton producing states, with the effects more widespread in Texas.
- The total production is expected to be about 2.5% less than last year despite more sowing area, due to poor rain in some of the main growing areas. This has also fuelled the uptrend.
- Notwithstanding the crop damage due to floods in Gujarat, the largest cotton producing state, India's cotton output in the forthcoming 2017-18 season starting October is seen increasing by 10-15 per cent on rise in acreage across the country.

Some of the fundamental drivers for International cotton prices are:

- ICE cotton futures fell one percent on Tuesday as concerns of crop damage in major producing regions in the United States faded, amid a stronger dollar. The damage across south Texas from Hurricane Harvey seems to be less than originally estimated. The U.S. Department of Agriculture's weekly crop progress report on Monday showed that 60 percent of the crop was in good or excellent condition as against 48 percent for the corresponding week a year earlier.

- The domestic cotton prices are expected to decline by October or November, when arrivals of new kharif crop begin in full swing. According to the U.S. Department of Agriculture estimates for 2017-18, global cotton production at about 120.8 million bales, is expected to be 13 per cent more than in the previous season, as farmers shifted from other crops to cotton due to more attractive prices.

- The speculators cut net long positions by 6,019 Contracts to 62,786 in the week upto September 19, Commodity Futures Trading Commission data showed on Friday.

Technical indications have turned bearish as expected. After moving in a broad range of 11,800-12,200 /qtl range, prices have dropped sharply. As cautioned earlier, prices are still finding it difficult to sustain and push higher and could be vulnerable for a drop in the coming months they fail to find momentum. With the cap at 12,750-800, we can expect prices to edge lower towards 11,000/qtl.

As mentioned previously, indicators are still in a neutral state and prices could remain range bound for a while till some clear directional clues are obtained. We see support now in the 11,000 / qtl range followed by more important support at 10,800/qtl range now. It looks like prices could stage a rebound higher to 11,700-800 levels before resuming the decline lower again. The indicators are extremely oversold indicating a possible upward correction in the coming weeks.

MCX October Contract Continuation Chart

The MCX benchmark October cotton chart as mentioned earlier shows signs of an

intermediate bottom around 17,740 levels. A recovery to 19,000 levels materialised. Prices have corrected lower, but managed to hold supports around 18,000 levels so far. While this support holds, we expect prices to edge higher once again towards 18,700 where strong resistances are seen. Once above here it could even aim for 19,000 in the coming sessions. Close below 18,000 could revive bearish hopes for 16,850-17,000 subsequently.

We will also look at the ICE Cotton futures charts for a possible direction in international prices.

As mentioned earlier, December active month is indicating a mixed picture with a bearish bias. As cautioned earlier, any unexpected rise and close above 72.50c could see further upside to 75c followed by 78c. Strong resistance was seen around 75c and it failed to follow-through higher from there, leading to a loss of confidence. Our favoured view is mildly bullish initially for 69-71c levels again, followed by a break below 67c, opening the way for further declines to 63-64c levels. Only an unexpected close above 73c could revive bullish hopes.

CONCLUSION:

Both the domestic and international prices are unable to see follow-through upside momentum. The technical picture presently is neutral with some mild indications of bullishness which could be temporary. Only a rise above 73c could revive bullish hopes again. The international prices indicate some near-term strength, but the medium-term picture looks very bearish, while the domestic prices look benign.

For Guj ICS supports are seen at 11,200 /qtl followed by 11,000 /qtl, and for ICE Dec cotton futures at 67c followed by 64c. Failure to follow-through higher above 12,500 /qtl has weakened the bullish picture in the domestic markets, while in the international markets prices are indicating a possible bearish turnaround. As we have been maintaining, though international markets could potentially change direction and push higher, but the technical picture is indicating prices to edge lower to 64c on the downside and the domestic prices to edge lower around 10,800/qtl levels in the coming weeks after a minor recovery upwards. We still maintain the same view in this update as well.

Rainfall Distribution (01.06.2017 to 24.09.2017)

Sr. No.	State	Day 24.09.2017				Period 01.06.2017 to 24.09.2017			
		Actual (mm)	Normal (mm)	% Dep.	Cat.	Actual (mm)	Normal (mm)	% Dep.	Cat.
1	Punjab	1.5	4.7	-68%	LD	385.0	475.7	-19%	N
2	Haryana	6.3	3.2	97%	LE	341.8	450.6	-24%	D
3	West Rajasthan	0.0	1.2	-100%	NR	365.6	259.6	41%	E
	East Rajasthan	0.0	2.7	-99%	LD	566.0	607.2	-7%	N
4	Gujarat	0.0	3.6	-100%	NR	798.8	658.2	21%	E
	Saurashtra & Kutch	0.0	2.5	-100%	NR	646.3	468.2	38%	E
5	Maharashtra	1.2	6.4	-81%	LD	991.1	972.9	2%	N
	Madhya Maharashtra	3.1	6.9	-54%	D	830.2	692.9	20%	E
	Marathwada	0.0	6.4	-100%	NR	640.0	650.5	-2%	N
	Vidarbha	0.0	4.1	-100%	NR	727.0	932.2	-22%	D
6	West Madhya Pradesh	0.0	4.3	-100%	NR	740.1	858.9	-14%	N
	East Madhya Pradesh	0.2	3.5	-93%	LD	792.1	1033.0	-23%	D
7	Telangana	0.2	5.9	-96%	LD	616.7	725.6	-15%	N
8	Coastal Andhra Pradesh	6.0	6.2	-4%	N	620.1	543.2	14%	N
	Rayalseema	2.4	5.7	-57%	D	459.3	368.4	25%	E
9	Coastal Karnataka	0.0	9.9	-99%	LD	2497.9	3021.8	-17%	N
	N.I. Karnataka	3.0	6.8	-56%	D	456.2	470.3	-3%	N
	S.I. Karnataka	0.1	6.4	-99%	LD	576.4	625.5	-8%	N
10	Tamil Nadu & Pondicherry	0.4	4.1	-90%	LD	373.5	289.6	29%	E
11	Orissa	1.8	6.5	-73%	LD	1018.5	1116.3	-9%	N

L. Excess, Excess, Normal, Deficient, L. Deficient
Source : India Meteorological Department, Hydromet Division, New Delhi

COTTON EXCHANGE MARCHES AHEAD

Madhoo Pavaskar, Rama Pavaskar

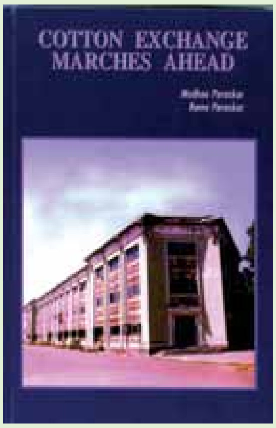
Chapter 6

March To Freedom - II

(Contd. from Issue No.18)

Regulation of NTSD Contracts

Although unlike as in several other commodities, trading in the n.t.s.d. contracts in cotton is not prohibited, such contracts can be entered into at present only between, through or with the members of the associations recognised by the Central Government under Section 6 of the F.C.(R) Act. Earlier the n.t.s.d. contracts in cotton were regulated only in Mumbai. But following the suspension of futures trading in the commodity during the mid-1960s, such regulation was extended to the rest of the country in February 1969. Since then, besides the East India Cotton Association, seven associations in the country have been recognised for buying and selling of cotton against n.t.s.d. contracts. These are (1) The South India Cotton Association, Coimbatore, (2) The Central India Cotton Association, Ujjain, (3) The Cotton Association, Indore, (4) The Ahmedabad Cotton Merchants Association, Ahmedabad, (5) The Central Gujarat Cotton Dealers' Association, Vadodara, (6) The Southern Gujarat Cotton Dealers' Association, Surat and (7) The Andhra-Pradesh Cotton Association, Guntur. The recognition granted earlier to the Northern India Cotton Association, Bhatinda, was suspended in September 1995.



The n.t.s.d. contracts in Indian cotton (full pressed, half pressed or loose) having brought under regulation throughout the country, trading in such contracts can commence only after the Forward Markets Commission (FMC) grants the necessary permission for the specific varieties of cotton and for the periods prescribed. These permissions are granted by the FMC from time to time every year, depending on the picking and marketing seasons for the different varieties. Such permissions restrict the contracts to a maximum period of six months in advance of their maturity. In other words, neither are all the varieties of cotton lint permitted to be traded simultaneously through the n.t.s.d. contracts, nor are such contracts permitted for delivery and payment of price beyond six months at any time. For some time, this period was restricted to just three months, though later the six month period was restored on representation from the Cotton Exchange. Again, the members of not all the associations are allowed to trade in all the permissible varieties. While the members of the East India Cotton Association and the South India Cotton Association are permitted to transact business in n.t.s.d. contracts for all the varieties grown in the country at different times of the year, the members of other recognised associations are allowed to trade in only the local varieties grown in their respective States or their neighbouring regions.

All the seller members of the recognised associations are required to report fortnightly to the FMC, through their respective associations, the details of all the n.t.s.d. contracts entered into by them. When the seller is a non-member, the buyer member is required to report. When both are non-members, the member through whom the contract is entered into needs to report. These reports call for details of not only the contracts entered into during the reporting fortnight, but also the performance of the contracts which matured during that fortnight.

Since a n.t.s.d. contract in cotton is a forward contract between two parties in which cotton of specific grade and description has to be delivered at a specific location during a pre-determined future period at a pre-determined price, neither the buyer nor the seller can transfer such contract to a third party nor can they settle it mutually without giving or receiving either the delivery of physical goods or the documents of title thereof, which documents, in turn, are also not transferable by the buyer. To put it more succinctly, the buyer must either receive the physical delivery of goods of the quality as specified in the contract, or use the delivery order or any other document of title to goods received from the seller against such contract, for the sole purpose of taking the possession and ownership of the physical goods. Similarly, the quality, the location and the delivery period cannot be renegotiated once the contract is entered into. In other words, the specific performance of a n.t.s.d. contract in accordance with its terms is obligatory on both the buyer and the seller.

Crisis of 1994

The definition of ready and n.t.s.d. contracts by the F.C.(R) Act and their regulation in cotton have really put the private cotton trade in strait-jacket.

There is little room for any manoeuvrability in these contracts. Their absurd rigidity actually led to a serious crisis in November 1994 when the cotton prices of the varieties grown in the Punjab and Rajasthan skyrocketted, following the unexpected crop failure and the resulting downward revision of the crop estimate for the region from 50-55 lakh bales to 35-40 lakh bales. The prices of most varieties rose so sharply that the ginners in most of the North Indian mandies were unable to meet their earlier commitments against the n.t.s.d. contacts to the mills as well as to the merchants in and outside the region. This had a cascading effect and the merchants who had bought on the n.t.s.d. contracts from the ginners, in turn, were unable to fulfill their subsequent sales against similar contracts with the mills. Several contracts were dishonoured, and in some cases deliveries were effected only after the stipulated time-frame. Finally, under pressures from the ginners, the outstanding n.t.s.d. contracts were unilaterally settled by the Northern India Cotton Association, Bhatinda, at rates much below the prevailing prices in the spot market, resulting in heavy losses to the buyers.

The crisis of November 1994 clearly established that the rigidity of n.t.s.d. contracts as defined at present and their regulation in cotton had served little purpose. The Forward Markets Commission did not renew the recognition granted to the Northern India Cotton Association, Bhatinda, but could do very little to ease the situation. Had the contracts been allowed to be flexible and not under regulation, buyers and sellers could have arrived at mutual settlements voluntarily, without much hue and cry, considering the unavoidable difficulties faced by both. But as the contracts did not allow any manoeuvrability for fear of otherwise infringing the law, buyers sought to demand their pound of flesh, which sellers were unable to satisfy. That led to an unprecedented crisis, violating the sanctity of contracts in the process, from which the market for the n.t.s.d. contracts in cotton has still not recovered.

As it is, there appears to be a world of difference between the delivery contracts, both ready and n.t.s.d., as permitted in India and those executed and performed in other countries. As the World Bank report on futures markets in India observes, "Forward trade between two parties is quite common in other countries, but in contrast to India, considerable flexibility is normally built into these contracts. For example, a seller is normally allowed to deliver products of comparable quality if his/her own production has fallen short. Contracts can be liquidated ("washed out"), with final payment between buyer and seller (representing price movements over the life of the contract) taking the place of contract delivery. Postponements are not a real problem, with premiums or discounts on the original price often directly calculated from futures market prices". With the envisaged globalization of India's commodity trade by A.D.2005 under the rules of the World Trade Organization (WTO), of which India is a member, time is now ripe for the Government of India to modify the present absurdly rigid definitions of the ready and n.t.s.d. contracts to make them more flexible so as to fall in line with the actual practices prevailing internationally.

Discrimination Against Trade

While regulating the n.t.s.d. contracts in cotton, the Central Government has exempted all such contracts entered into by the government organizations and the public sector bodies like the Cotton Corporation of India and the Maharashtra State Co-operative Cotton Growers' Marketing Federation which implements the monopoly procurement scheme in Maharashtra. The discrimination against the private sector cotton trade is obvious insofar as it is still denied the right to compete with the public sector agencies on equal footing.

The export and import contracts for deferred shipments are also exempted from the n.t.s.d. contract regulations. This is denying the domestic private sector cotton trade a level playing field vis-à-vis not only the public sector and State agencies, but also the overseas importers and exporters. It is patently unfair to discriminate between the overseas sales and purchases and the domestic sales and purchases for distant deliveries. If overseas suppliers can sell foreign cotton freely to Indian spinners for shipments beyond 11 days, and likewise if foreign buyers can purchase Indian cotton on deferred shipment basis, there seems little rationale in regulating the domestic sales and purchases of cotton through n.t.s.d. deals by mills, merchants and ginners in the country.

Interestingly, the Commodity Exchange Act of U.S.A. which also regulates futures markets in that country excludes "any sale of any cash commodity for deferred shipment or delivery" from the term "future delivery", and thereby exempts all contracts akin to our ready, n.t.s.d. and t.s.d. contracts from the ambit of regulation under that Act. As a matter of fact, the n.t.s.d. contracts for the sale and purchase of goods in India are even otherwise subject to the provisions of the Indian Contract Act, 1872 and the Sale of Goods Act, 1930. These legislations have extensive provisions for the performance of such contracts by way of delivery and payment. The parties to the delivery contracts can take easy recourse to these Acts to seek their enforcement. There is no reason for the government to intervene in their performance through arbitrary regulation under the F.C.(R) Act.

Shrinking Market for NTSD

Surprisingly, the total volume of n.t.s.d. contracts in cotton traded at all the recognized associations, as reported to the Forward Markets Commission, has scarcely exceeded 20 lakh bales a year. After the 1994 crisis, the market has actually shrunk to 10 lakh bales, or even less, if one were to believe the transactions as reported by the members of the recognised associations. The business in n.t.s.d. contracts as a proportion to the corresponding cotton crop seems to have fallen even more sharply from nearly 16 per cent in 1992 to around 5 per cent, or even less, at the dawn the New Millennium.

It appears that there is gross under-reporting and even non-reporting of business in n.t.s.d. contracts. It is hard to believe that over 95 per cent of the cotton production is at present sold by way of ready delivery contracts, entailing delivery and payment within 11 days. For one thing, following the fear of inviting disciplinary or penal action in the event of either defaults or settlement of the contracts otherwise than by giving or receiving actual deliveries, it seems that not all the n.t.s.d. contracts in cotton are reported by the members of the recognised associations. It is also likely that quite a few such contracts have remained unreported, when neither the buyers nor the sellers to such contracts are members of any of the recognised associations. Incidentally, merchants and mills may also be entering into such contracts as ready delivery contracts by suitably adjusting the contract dates to avoid the cumbersome regulating requirements and reporting procedures.

Need for Deregulation

There is no doubt that the regulation of delivery contracts in cotton has failed miserably, without securing any economic gain to any section of the cotton economy, or even the nation at large. And having allowed futures trading, it is time for the authorities to free the delivery contracts in cotton from the needless shackles of regulation under the F.C.(R) Act. As Mr. Suresh Kotak, the present erudite President of the Cotton Exchange, observed cogently in his illuminating speech at the 75th Annual General Meeting held on September 16, 1997, "In the emerging scenario of larger crop sizes, increased exports of raw cotton and resumption of futures trading, it is imperative that action is taken to resolve these problems in order that we can turn a new leaf in cotton trading and make it smoother and more efficient." Emphasising that n.t.s.d. contracts are genuine merchandising contracts, Mr. Kotak pointed out that "several committees had gone into this question and without exception they recommended that these contracts be left outside the purview of regulation".

In the same speech, Mr. Kotak also brought out vividly the hurdles, procedures and bottlenecks that delay the delivery of goods and the payment of price beyond 11 days as stipulated for ready delivery contracts and argued that "there is no particular sanctity about 11 days", which period "had been decided arbitrarily and needs to be changed when realities on the ground warrant the same". He therefore strongly pleaded for "amending the definition of ready delivery contract so as to provide for at least 30 days, instead of the present 11 days."

The cotton trade also desires that the existing definitions of ready and n.t.s.d. contracts in the F.C. (R) Act need to be amended so as to make such contracts more flexible by mutual agreement between the contracting parties in order to bring them on par with similar contracts traded internationally. Simultaneously, with the revival of futures trading, the prohibition on "on call" contracts in cotton also needs to be lifted, as such contracts known as "executable orders" or "price to be fixed contracts" are common internationally. After all, the envisaged globalization of the cotton economy under the World Trade Organization charter necessarily presupposes, albeit implicitly, that the contracts traded globally should be allowed to be traded by the cotton trade in Indian as well.

In fact, to elucidate its arguments cogently and educate the authorities on this issue of ready and n.t.s.d. contracts, the Cotton Exchange commissioned a small study on the subject and brought out in its Platinum Jubilee Year a detailed brochure on 'Ready & N.T.S.D. Contracts – Need for Liberalization'. The brochure was released on October 27, 1997 at one of the Platinum Jubilee functions of the Exchange held at Ahmedabad by the renowned champion of cotton farmers in Gujarat, Mr. Sanat Mehta, Former finance Minister of that State, who was the Chief Guest on the occasion, and who strongly supported the recommendations made in the brochure.

Midas Touch

The Cotton Exchange seems to be lucky in having Mr. Suresh Kotak at the helm of its affairs at present. After several decades of strenuous struggle, it was surprisingly during his short stint so far that selective credit controls were abolished, futures trading in cotton permitted, and even export liberalization was announced. Verily, Mr. Kotak is born with Midas Touch. It would therefore not be astonishing, if his Midas Touch soon brings about the deregulation of delivery contracts also. That would be the crowning end to the heroic march to freedom began by the Cotton Exchange more than three decades and a half back.

UPCOUNTRY SPOT RATES

(Rs./Qtl)

Standard Descriptions with Basic Grade & Staple in Millimetres based on Upper Half Mean Length [By law 66 (A) (a) (4)]							Spot Rate (Upcountry) 2016-17 Crop SEPTEMBER 2017					
Sr. No.	Growth	Grade Standard	Grade	Staple	Micronaire	Strength /GPT	18th	19th	20th	21st	22nd	23rd
1	P/H/R	ICS-101	Fine	Below 22mm	5.0-7.0	15	9561 (34000)	9476 (33700)	9476 (33700)	9533 (33900)	9533 (33900)	9448 (33600)
2	P/H/R	ICS-201	Fine	Below 22mm	5.0-7.0	15	9842 (35000)	9758 (34700)	9758 (34700)	9814 (34900)	9814 (34900)	9729 (34600)
3	GUJ	ICS-102	Fine	22mm	4.0-6.0	20	7930 (28200)	7930 (28200)	7930 (28200)	7845 (27900)	7817 (27800)	7817 (27800)
4	KAR	ICS-103	Fine	23mm	4.0-5.5	21	9223 (32800)	9223 (32800)	9223 (32800)	9223 (32800)	9223 (32800)	9223 (32800)
5	M/M	ICS-104	Fine	24mm	4.0-5.0	23	10236 (36400)	10179 (36200)	10179 (36200)	10179 (36200)	10179 (36200)	10123 (36000)
6	P/H/R	ICS-202	Fine	26mm	3.5-4.9	26	11023 (39200)	10882 (38700)	10798 (38400)	10517 (37400)	10517 (37400)	10432 (37100)
7	M/M/A	ICS-105	Fine	26mm	3.0-3.4	25	9673 (34400)	9673 (34400)	9561 (34000)	9561 (34000)	9561 (34000)	9561 (34000)
8	M/M/A	ICS-105	Fine	26mm	3.5-4.9	25	10123 (36000)	10123 (36000)	10039 (35700)	10039 (35700)	9954 (35400)	9926 (35300)
9	P/H/R	ICS-105	Fine	27mm	3.5.4.9	26	11192 (39800)	11051 (39300)	10967 (39000)	10691 (38000)	10691 (38000)	10601 (37700)
10	M/M/A	ICS-105	Fine	27mm	3.0-3.4	26	10208 (36300)	10208 (36300)	10123 (36000)	10039 (35700)	10039 (35700)	9983 (35500)
11	M/M/A	ICS-105	Fine	27mm	3.5-4.9	26	10601 (37700)	10461 (37200)	10320 (36700)	10236 (36400)	10179 (36200)	10151 (36100)
12	P/H/R	ICS-105	Fine	28mm	3.5-4.9	27	11276 (40100)	11135 (39600)	11051 (39300)	10770 (38300)	10770 (38300)	10686 (38000)
13	M/M/A	ICS-105	Fine	28mm	3.5-4.9	27	11304 (40200)	11164 (39700)	11023 (39200)	10967 (39000)	10967 (39000)	10939 (38900)
14	GUJ	ICS-105	Fine	28mm	3.5-4.9	27	11164 (39700)	11023 (39200)	10995 (39100)	10967 (39000)	10967 (39000)	10967 (39000)
15	M/M/A/K	ICS-105	Fine	29mm	3.5-4.9	28	11670 (41500)	11529 (41000)	11389 (40500)	11389 (40500)	11332 (40300)	11304 (40200)
16	GUJ	ICS-105	Fine	29mm	3.5-4.9	28	11501 (40900)	11360 (40400)	11304 (40200)	11304 (40200)	11248 (40000)	11248 (40000)
17	M/M/A/K	ICS-105	Fine	30mm	3.5-4.9	29	11923 (42400)	11838 (42100)	11698 (41600)	11698 (41600)	11698 (41600)	11670 (41500)
18	M/M/A/K/T/O	ICS-105	Fine	31mm	3.5-4.9	30	12232 (43500)	12148 (43200)	12007 (42700)	12007 (42700)	12007 (42700)	11951 (42500)
19	A/K/T/O	ICS-106	Fine	32mm	3.5-4.9	31	12766 (45400)	12654 (45000)	12513 (44500)	12513 (44500)	12513 (44500)	12485 (44400)
20	M(P)/K/T	ICS-107	Fine	34mm	3.0-3.8	33	14904 (53000)	14763 (52500)	14763 (52500)	14622 (52000)	14622 (52000)	14622 (52000)

(Note: Figures in bracket indicate prices in Rs./Candy)