Risk Management Policy- Commodity Derivatives

Introduction:

The Reserve Bank of India (RBI) has allowed banks to offer commodity derivative products through their subsidiaries which are currently dealing in financial products, that is, securities. Accordingly SBICAP Securities Limited (SSL) is in process of obtaining membership of Exchanges which are offering Commodity derivatives for trading on its trading platform so as to offer its customer a complete product basket. Client registered with SBICAP Securities Limited (SSL) can register for trading in Commodity derivatives segment.

Following broad risk management tools will be used to manage the risk in the commodity market

1. **Margin requirement**:- At the time of any order entry, checks are performed to ensure margin sufficiency. Margin is the minimum Client margin required to enter into a position. Margin will be specified in terms of percentage of the order value. Different types of margins will be charged for commodity derivatives which are

    - **VaR margin:** VaR is the value at risk. SSL will use the VaR margin which is provided by the exchanges as base for taking any new positions in commodity derivatives.

    - **Extreme Loss Margin (ELM):** ELM margin is charged to cover the loss in situations that move beyond the coverage of Initial Margin.

    - **Additional Margin:-** Additional margins are margins which are charged over and above the normal margin. It includes Tender margin, special margin, concentration margin, delivery/devolvement margin etc.

2. **Exposure Limit**: Exposure limit is the net value of position a client can enter into at any given point in time on that day. This is proposed to be the same as current limit applicable for Equity/Equity derivatives.

3. **Client Margin:** Total Deposit of the client with SSL. This includes Ledger balance and value of collateral.

4. **Haircut**: SSL accepts collateral (i.e. shares) from client towards the margin requirement. However, shares carry risk of volatility. Hence a haircut, which is the **perceived risk** on the price of the security, is applied to the total value of the security for arriving at the perceived **risk free** value of the collateral.

A. **Approved Collateral:** Approved list of collateral includes list of Mutual Funds / Bonds / NCDs and any other tradable securities including securities forming part of the approved list of securities as published by exchanges, from time to time, which is taken as part of approved list of securities as per SSL risk management policy.

Risk Management and Exposure Policy for Commodity Derivative Segment

It is proposed that a standard policy will be followed for all the clients trading in Commodity derivative segment through SSL

Segment	Forms of Margin	Criteria	Haircut	Multiplier	Margins charged
Commodity Derivatives	Ledger	Clear Credit Balance in the ledger of the client maintained with SSL	N.A.	1 time	Margin as Prescribed by the Exchange
	Collateral	After Haircut Value of Approved Collateral.	SSL approved list	1 time	

Note:

a. SSL Approved list: The policy applicable for Equity/Equity derivatives on approved list of securities will also be applicable for commodity derivatives.

b. Mark to Market losses should be collected on T+1 day.

B. Monitoring Process:

Risk Team shall monitor the positions / debits of the client vis-a-vis the client margin available with SSL. Following process / reports which are currently generated for other segments will also be used to monitor the risk associated with the commodity trades.

a) Carry Forward Debit:

Daily at the beginning of the day (BOD), ageing report will be generated. This report will contain details of the amount recoverable from the client (debits of client) with total valuation of shares available with the client. SSL reserves the right to sell these shares in case of default by client.

Available margin of the client will be monitored every morning and separate alerts will be sent to the branches, where available margin falls below 10% (i.e. total value of shares is less than 110% of the debit). Position of these clients will be monitored closely and shares will be sold (to the extent of debit) if client fails to clear the debit.

b) Intraday and derivative Positions:

Mark to market loss on the positions will be monitored by risk department and positions will be squared off where mark to market loss for the client exceeds 70% of client margin.

c) **Margin shortfall for commodity derivatives**:

Risk Management System will square off the positions in cases where margin is in shortfall than that required as per regulations.

All Intraday positions for Clients will be auto squared off before 30 minutes from the close of Agri/non-agri market as the case may be or any other time as deemed fit by RMS based on market conditions and volatility

d) **Position limits:-**

- **Client level:-** Client Level Position Limit in any commodity will be allowed as specified by the exchange. If client exceeds the Client Level Position Limit in any commodity of the exchange, then RMS will square off the excess position and inform the same to the concerned Branch / department.

- **Member Level:-** Member Level Position Limit in any commodity should be maintained as specified by the exchange. If Member Level Position Limit exceeds in any commodity , Member will put in square off mode in that commodity position. Accordingly, position of client will be square off immediately on "last in last out basis"

e) **Compulsory Delivery:-**

In case of commodity derivatives contracts which are compulsory delivery contracts, the Long and Short position may convert into delivery. In order to mitigate the risk of unwarranted delivery,

- The client should roll over / close the existing positions **3** trading days before the start of tender period (T-3) till 12.00 noon. For e.g. If tender period starts from 11th October, 2018, clients can close / roll over till 8th October 12.00 noon.

- SSL will start squaring off all open positions post T-3rd working day --- 12.00 noon. Note that this is irrespective of margin availability

- In case square off cannot be done (e.g. Due to lack of liquidity or any other reason), then such contracts may be physically settled and will have to be settled by the client by paying requisite obligations as per the physical settlement rules. SSL may impose additional margin, if any, in such cases to cover the obligation which would be debited in the ledger, on a case to case basis

Risk Management System will review the above risk measure with reference to physical delivery based on the market conditions and clients requirement in future, as and when required.