

## Market Notice

**Number:** A1873  
**Date:** 20 September 2013

### Proposal to introduce Short-Dated New Crop (SDNC) Options to the SA Market

South African grain and oilseed market participants have been using put options and related derivative strategies for more than 15 years to lock in a floor price for their grains. While these strategies are quite popular they come at a cost that at times can be prohibitive.

Short-Dated New Crop (SDNC) options provide convenient alternative strategies for those trading new season crops in that producers can experience the benefits of hedging with options at reduced cost and without having to take a futures outright position.

#### How Short-Dated New Crop options work

The South African new crop season for Maize begins on the 01 May each year, with new crop main hedging month being July. SDNC options will all reference the new crop main hedging month, but will expire earlier than the traditional new crop options. Because of the shorter time value, these options will have reduced premiums while effectively allowing grain market participants to manage price risk during the critical growing period.

The underlying futures contract for, say, maize will be July and there will be two contract months listed for each product (i.e. white and yellow) and their expiry methodology will be consistent with the usual expiries for old crop options, namely 5 business days before month end.

In our illustration in the table below there are two options expiries of Dec13 and Mar14 that would reference the July14 WMAZ underlying futures. The Dec13 SDNC option will expire as at 12h00 on 23 December 2013 and the Mar14 SDNC option will expire as at 12h00 on 25 March 2014.

The JSE will determine the final mark-to-market (mtm) value for July14 contract in accordance with the daily mtm process and **WILL NOT** move the option expiration process earlier as we would do with old crop option close outs. If the SDNC option expires in-the-money, the JSE will book a report-only trade and create a relevant futures position in the July14 WMAZ expiry for each long and short position holder.

We propose that, initially, only white and yellow maize SDNC options be listed in October 2013, followed by oilseeds and wheat options being listed upon demand as demonstrated in the table below:

Short-Dated New Crop Option	Underlying Futures	Short-Dated New Crop Option Contract Months
White Maize	July 2014	December 2013, March 2014
Yellow Maize	July 2014	December 2013, March 2014
Sunflower seeds	May 2014	October 2013, January 2014



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Soya bean	May2014	October 2013, January 2014
Wheat	December 2014	July 2014, September 2014

### Salient Features and Benefits

- The underlying futures contracts are the same as those for standard options contracts and are July White and Yellow Maize, May Sunflower seeds and Soya beans and December Wheat.
- There are two option contract months listed for each commodity and the option expiries coincide with the standard expiry dates, namely 5 business days prior to the expiry month
- Short-dated new crop options expire earlier than standard options but are identical to standard options in all other respects
- Premiums will typically be lower than the standard new crop options because of reduced time value
- Hedgers with inherent interest in the respective underlying commodities can use these short-dated new crop options to manage price risk during the critical growing season at reduced costs
- Because they reference the same underlying futures contracts as standard options, they allow arbitrage opportunities with calendar spreads, as well as serial and standard options
- They offer new opportunities to trade high impact events on new crop markets, such as SAGIS and Crop Estimates Committee reports or change in weather outlook

### Comparing Short-Dated and Standard Options on July14 WMAZ

The table below shows standard at-the-money July14 2100 WMAZ put with Short-Dated New Crop 2100 put options on July14 WMAZ futures.

	Dec Short-Dated New Crop 2100 Put (Exp 23/12/13)	March Short-Dated New Crop 2100 Put (Exp 25/03/14)	Jul Standard 2200 Put (Exp 24/07/14)
July14 WMAZ Futures			
Price on 18/09/2013	2100	2100	2100
Option Premium (R/ton)	96	139	181
Min Selling Price (R/ton)	2004	1961	1919
Protection Period (number of days)	84 days	176 days	297 days

### Comparing Short-Dated and Standard Options on “Greek” Sensitivities

Because SDNC options reference the same underlying futures contract as the standard new crop options, they allow the novice market participants with additional opportunities to trade the “Greeks.” Consider the sensitivities of the following “Greeks”:

**Theta.** Theta is defined as the change in the price of option for 1-day decrease in the remaining time to expiration. Theta decays exponentially as options approach expiration. Thus the time decay of the SDNC options as it approached expiration is much more rapid than the longer-dated standard option of the new crop.

**Gamma.** Gamma is the change of the options delta for one-point change in the price of the underlying. Gamma increases exponentially as options approach expiration. SDNC options have a much higher Gamma than the longer-dated standard options on new crop.

**Vega.** Vega is the change in the value of an option for a 1% increase in implied volatility. Vega decreases exponentially as options approach expiration. The SDNC options have a much lower vega than the longer-dated options on new crop, which also explains the lower option premium for the SDNC options.

### Contract Specifications

	Short-Dated New Crop Maize Options	Short-Dated New Crop Oilseeds Options	Short-Dated New Crop Wheat Options
Underlying Contract	July WMAZ and YMAZ contracts nearest to option expiration	May SUNS and SOYA contracts nearest to option expiration	December WEAT contract nearest to option expiration
Symbols	WMNC and YMNC	SUNC and SYNC	WENC
Strike Price Interval	R20	R20	R20
Tick Size	As per the current contract which is 1 cent per ton		
Daily Price Limits	Same as the daily price limits applicable to standard and serial options		
MTM Process	In accordance with the normal daily mtm process		
Contract Months	December and March	October and January	July and September
Exercise	The buyer of SDNC options may exercise the option on any business day prior to expiration. Option exercise results in an underlying futures position. Options in-the-money on the last day of trading are automatically exercised by the JSE and a report-only position booked.		
Expiration	Unexercised SDNC options shall expire at 12h00 pm on the last day of trading.		
Trading Hours	9H00 to 12h00 CAT, Monday to Friday		
JSE Fees	R12/contract (VAT Incl) All options that expire in the money will not be charged a fee together with the corresponding new crop futures position. However when closing out the futures position a JSE fee will apply		

Market participants are kindly requested to take a look at the proposal above and provide any comments that you feel need to get to our attention. Specifically, please confirm:

1. If you see value in SDNC options
2. If you would be interested being a price maker for this products
3. Whether or not you agree with the proposed expiry months

We will appreciate any comments reaching our offices on or before 04 October 2013.

Sincerely,

A handwritten signature in black ink, appearing to read 'Chris Sturgess', written in a cursive style.

**Chris Sturgess**

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