

## MINUTES

**HEADING: JSE EQUITY TRADING ADVISORY COMMITTEE MEETING**

Date: 06 September 2016  
Time: 11:00 to 13:00  
Venue: JSE, Serengeti Boardroom - 9th Floor

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Ms Donna Nemer (Chairman, JSE) (DN)  
Ms Valdene Reddy (Business Owner, JSE) (VR)  
Mr Warren Geers (WG)  
Mr Gregori Nicola (GN)  
Ms Adele Hattingh (AH)  
Ms Pumelele Sibisi (PS)  
Mr Merlin Rajah (MeR)  
Mr Mark Randall (MR)  
Mr Peter Redman (PR)  
Mr Tshwantsho Matsena (TM)  
Ms Leanne Parsons (LP)  
Mr Brett Kotze (BK)  
Present: Mr. Zweli Vonya (ZV)  
Ms Maria Dalle Ave (MdA)  
Mr Neil Cohen  
Mr Matthew Rattray  
Mr Cameron Macklin  
Mr Carlyle Whittaker  
Mr Mike Ray  
Mr Alec Schoeman  
Mr James Stewart  
Ms Kelebogile Motjale  
Mr Sandile Sibanyoni  
Ms Erica Bruce  
Mr Ockie Raubenheimer , standing in for Muneer Ismail  
Ms Adriana Weilbach, standing in for Derek Hompes

Mr Conrad Africa, standing in for Jackie Tetlow (Dial in)  
Mr Dharmesh Gangaram, standing in for John Slettevold (Dial in)  
Mr Alphonso Raats (Dial in)  
Mr Tshepo Maseko (Dial in)  
Mr Warren Chapman (Dial in)  
Mr Rudolph Botha (Dial in)  
Mr Shiran Samuel (Dial in)  
Ms Sunette Mulder (Dial in)  
Mr Harry Ioannou (Dial in)

Mr Earl Owen

Apologies: Mr Philip van der Merwe  
Mr Tristyn Naidoo  
Mr Peter Koutromanos

Distribution: Equity Trading Advisory Committee

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### **1. WELCOME, APOLOGIES & NEW MEMBERS**

DN welcomed everyone to the third Equity Trading Advisory Committee meeting for 2016.

### **2. CONFIRMATION OF PREVIOUS MINUTES**

The minutes of the TAC meeting held on 9 May 2016 were confirmed and accepted as correct.

### **3. INFORMATION SERVICES**

LP informed the Advisory Committee (AC) about the JSE's restructuring, leading to her being the Director of Information Services. The division encompasses Business Intelligence, Equities and Bonds Indices, Valuations, Corporate Actions, Market Data and Colocation. The responsibility of BDA has moved to Post Trade Services and the Trading and Market Services falls under TJ Matsena.

LP's new role is mainly about improving and streamlining the operational processes; produce elegant analytics based off the JSE's internal data, compliant with international standards. LP informed the AC about the non-resident statistic issue that was mentioned within the media during July alluding to fact that it was an internal human error. The JSE is engaging with an independent entity, PWC to help review the non-resident statistic issue;

audit and advise on checks and balances regarding data governance. She concluded by saying that the JSE takes the data that is being produced seriously. A question was raised on reliability of the checks that JSE has implemented to ensure the data issue does not happen again. LP responded saying that the JSE is confident that the current data is correct and they have put further measures in place to ensure it remains correct going forward.

The AC suggested that the JSE should create a centralized reporting system where all client issues raised can be forwarded to and be taken seriously without delay by the customer service center. DN thanked everyone who reported the error to the JSE.

#### **4. FTSE/JSE INDEX UPDATE**

MR provided the committee with feedback with regards to rule changes related to Equity Indices. These rule changes were published on the 31 August 2016 and are effective from the 19 September 2016.

MR went on to explain that one of the biggest changes to the All Share Index is a change to the free float eligibility of inward listed companies. Companies such as Glencore and South 32 which were formerly not part of the All Share Index, will now be included. MR explained that this is due to the fact that previous rules stated that in order for a company to be included in the index, a minimum number of shares in the South African register which ranged from 5-15 %, depending on size of the company, were required. However, that rule will now be relaxed to a minimum of 1% free float on the local register.

MR added that two new benchmark indices have been introduced and are designed for funds looking for a performance benchmark. The first index introduced is a Large Cap index which is based on global gross company size. This index has no regard for free float when selecting constituents and is designed to capture 85% of the market. The second index introduced is a Large & Mid-Cap index which is designed for funds that struggle with the tail of the All Share Index and are looking for something with fewer smaller companies. This index targets 96% of the market, unlike the All Share Index which targets 99% of the market. It cuts out around 50 companies from the tail as a result.

MR mentioned that the rules to how companies are selected for the Top 40 index have also changed. Previously, companies were selected on gross total market capitalization but this rule has changed and companies are now ranked on investable/free float market capitalization.

As a result of the aforementioned change, the index has seen a 2% increase in total representation. The weighting of the top 5 largest companies has come down by 2% whilst the smallest 5 companies' weightings have increased; thus improving tradability.

MR concluded by telling the committee that the index review will be completed on 30<sup>th</sup> November 2016 and the implementation of the changes will take place in December 2016.

A request was then made for MR to give insight as to how the SABMiller delisting would be treated. MR explained that the delisting will be treated as an immediate acquisition as it does not fall under the index quarterly review period. He then added that treatment of cash acquisitions in the Top 40 index is to delete the company that has been delisted and replace it with the next largest company.

MR was requested to confirm the changes that will be made to the SWIX 40 index. The SWIX40 index will be selected and ranked according to SWIX net market capitalization and as a result the constituents will divert from the Top 40. The Spar group for example is being added to the SWIX 40 and not the Top 40 index. This however makes the DTOP a better proxy for the SWIX All Share.

## **5. EQUITY MARKET BILLING FOR EQUITY MARKET ENHANCEMENTS**

DN mentioned that through market consultation, she understood there was a need for enhanced market functionality to assist traders in executing trades with minimal impact from HFT/Algos. The functionality provided tried to provide the market with alternate execution capabilities whilst still retaining market quality.

When looking at the pricing for the enhanced order/safe haven functionality the JSE looked at international exchanges' billing structures and found that many of these exchanges charge significantly more for this type of offering. Typically though, their lit functionality does start off at a lower base which was taken into consideration. DN reiterated that this new enhanced functionality is used on a voluntary basis.

VR discussed the new functionality of ITAC 1a in detail:

- The CPX sessions will be rolled out to the other trading segments within the market. This is not new functionality as it is currently in existence in ZA01.
- The Central Order Book Cross is new functionality that will allow for a single member to cross a buy and sell, the only dictate is that it needs to cross within the spread. Clients would see a trade come out as a XT, so clients can program their algorithms to ignore it, as it's volume they would have not been able to participate in.

- The pegged hidden orders is an enhancement of the JSE's current hidden order functionality, however the JSE now allows for the pegging of orders to best bid, best offer or mid-point, giving participants a better chance of finding one another. This functionality does however have a size requirement. Central order book orders will take preference over pegged hidden orders, which still protects the integrity of the lit book.
- MRS (minimum reserve size) in ZA01 has been reduced from 20% ADV (Average Daily Volume) to 15% or R50 million notional (whichever the lesser). MRS in ZA02 and ZA06 has also been reduced from 20% ADV to 15%. ZA03 will remain at 150% ADV. This was to cater for the top 40 stocks to be more accessible to the pegged hidden orders or EOD volume auction sessions. This is open to a review after 3 months to see if this size is too small or too large.
- The last piece of new functionality is the End of Day volume auction; it is typically our safe haven auction. There is a MRS requirement however no MES requirement. It will be a 5 minute session starting at 17:10. There will be neither visibility of indicative uncrossing size nor any post trade visibility of overhang; therefore it will be completely dark. Members would only see one print at the closing price of what has gone through the market. Limit orders will not be required to meet the MRS requirements.

In terms of the pricing, most exchanges do charge a premium for dark or safe haven functionality. VR unpacked several international exchanges' pricing. The JSE had to look at ensuring there was no arbitrage between the lit book and hidden orders and did not feel comfortable increasing the bps, but rather opted to remove the cap.

DN mentioned that the challenge was to price this in a way which would convey the intentions the JSE have, which is to offer additional execution flexibility without suffering the unintended consequences of pulling liquidity away from the lit book.

The committee was happy that the JSE proceed on the no cap fee. Should there however not be much take-up with the new functionality, the committee would review pricing after a few months.

## 6. JSE PROJECTS UPDATE

### 6.1. T+3

BK advised the committee that moving from T+5 to T+3 had been a huge success and provided the following averages:

- Between 55% and 60% of trades are being committed to by trade day (T).

- End of day T +1 has 99.99% of committed trades.
- The JSE still has zero failed trades.

No problems occurred during the migration week from T +5 to T+ 3.

The JSE has been getting positive feedback from market participants about the move to T +3. BK advised that he has been getting calls from some brokers informing him the move has allowed them to automate some manual processes leading to the amount of work being done in far shorter period of time. The South African market has been receiving global accolades due to the move to T +3.

BK also told the committee that there have been a couple of close calls due to dual listed stocks and he will be joining Strate in their London roadshow to address some of the pain points that have been identified since T + 3.

BK reiterated that as much as the JSE is currently seeing zero failed trades, the JSE's failed trades appetite still sits at 5%.

## **6.2. ITAC**

TM advised the committee that a planned dress rehearsal was the previous Saturday. Everything went according to plan in terms of the client accessibility network but there were a couple of issues especially from clients housed in the colocation centre. There were also some issues identified internally but by the time the dress rehearsal was completed all identified issues had been sorted out. To be sure that everything works correctly, another dress rehearsal has been planned for that coming week albeit an optional one but the JSE has reached out to all clients in colocation and they have consented to come in on the Saturday. Overall from an ITAC 1A point of view go-live is still the weekend of the 24 September 2016.

TM further advised the committee that as part of the 1A code drop a couple of issues had been identified:

- One of the issues is that the current design will reject a spread that is less than 1 cent. This will be rectified after go- live. TM did advise that it only affects shares that have a spread of half a tick and that it does not affect BDA.
- The second issue relates to the cross trade. When the JSE initially designed the functionality, the conversation about circuit breakers kicked in. At the time a call was made that because the orders do not reside in the central order book, if the price point is outside the circuit breaker levels the initial design was to allow the trade. However, after market consultation and worries about market quality, the JSE will now reject the order and the member will have to get a price that is within the circuit breaker before

they can re-submit it. This will not be an issue for most of the shares; it might be an issue for the lower end of ZA02. TM advised that a market notice will be sent out to the market advising on this change.

TM provided an update on Project 1B and 1C, the replacement of the derivatives and currency market technology. The project is progressing however there are some challenges related to integration. The JSE remains bullish that it will make the set timelines of late Q2 to early Q3 next year and will keep the market abreast as the project progresses.

TM further advised the committee that the JSE will be hosting a software provider showcase both for clearing and trading.

## **7. CLOSING AUCTION COMPARISON**

Closing Auctions across different markets were compared in trying to understand if there are any dictates around commitments to the closing auction. The exercise was to also see if there are any facets of other markets that the JSE could look to adopt.

NYSE, TSX and NASDAQ operate their closing auctions similarly to the JSE in that orders can be placed, amended and cancelled throughout the trading day. The exchanges would then publish an order imbalance after which traders are not allowed to remove orders already placed; they are however allowed to place orders that are opposite to the imbalance.

Hong Kong Stock Exchange does not allow for orders to be placed during continuous trading hours. The exchange calculates a reference price which is done in the last minute of continuous trading by taking the median of 5 snapshots of trades 15 seconds apart for every instrument. Once the reference price has been calculated members have a 5 minute window period where they can place, amend or cancel auction orders. The auction orders placed must be within 5% of the reference price of the stock. Post the order entry period is a further 2 minutes referred to as the no-cancellation period where only orders that are within the best bid and offer spread from the previous session are allowed. The auction will then have a 30 seconds random end time.

Brazil BM&BOVESPA operates what is referred to as a committed auction; orders can be placed, amended and cancelled during continuous trading hours. Once the closing auction begins market participants are not allowed to make amendments to orders unless they are to contribute to price improvement.

The JSE, LSE and SIX allow for orders to be placed, amended and cancelled during continuous trading as well as during the auction period.

A comparison of closing auction activity versus continuous trading reveals that the JSE's closing auction in 2015 contributed an average of 17% of the daily value traded. This is in line with the auction activity in the European and UK markets and with US markets at around 9%.

There has been a steady increase in the JSE's closing auction activity in the past few years, with the closing auction contributing 12% of the day's average value traded. This was before the introduction of colocation in 2014. At present the closing auction contributes about 18% to the day's value traded.

The order-to-trade ratio pre-colocation was at 19.9 and is currently at 15.8. With the introduction of colocation the total market quality has improved. The ratio is however much higher if we were to consider colocation in isolation. Colocation makes up about 30% the market's value traded.

Exchanges around world have changed the way they operate during continuous trading hours with the introduction of slow orders or speedbumps to their markets. They have however not made any changes to the way in which their auctions operate.

Although the JSE does not have any dictates as to how to trade in the closing action, its closing auction activity ranks high among global norms.

It was noted that in the first five minutes of futures closeout the auction price swings, as it seems traders place misleading orders only to correct them in the last five minutes. At present traders are afraid to disclose their full hand in the closing auction and thus only place their orders in parts.

The JSE will monitor activity in the new functionality to see if the noise in the closing auction might move to the EOD volume and provide feedback after 6 months of activity.

## **8. REGISTERED OFFICER NEW REQUEST FORM AND PROCESS**

MdA mentioned that as part of onboarding of the dealers, registered officers and traders, MdA's team investigated how they could standardize the actual process, improve operational efficiencies and maintain a consistent customer experience.

The current trader onboarding process takes up to 48 hours, whereas on the derivative market dealer onboarding could take up to 3 weeks, with the exception of the IRC market. In preparation for ITAC Readiness, MdA's team identified an opportunity to finalize one standardized process.

The current process for Equity Derivative and Commodity Derivatives registered officers and dealers registration requirements include:

- Registration form
- Obtain Surveillance Clearance
- 10 Business Day market notification
- Internal membership forum approval
- JSE Executive Approval
- If any concerns raised at any point in the process a Surveillance investigation is launched

Whereas in the Equity Market, trader registration requirements only include:

- Registration form
- Obtain Surveillance Clearance
- Internal membership forum approval

Within the derivative markets, dealers are required to complete a checklist to answer questions relating to:

- Their involvement in Disciplinary / Arbitration actions
- Criminal record
- Insolvency, etc.

Answers are not verified/vetted by the JSE Market Regulation as it is a duplication of the member's due diligence during their recruitment process.

Equity market traders do not have to complete the same questions.

In order to harmonise the process across the markets, the JSE Derivatives and IRC rules were amended, aligning the principles already in place in the Equity Market. The rules are currently being reviewed by the Registrar where it is anticipated that finalization will be reached by end September.

The JSE Executive will no longer accept or reject applications for the registration of traders and officers or issuance of market notice. In addition, the 10 day submission of objections or comments in respect of the person

registered will fall away. The internal membership forum will also be replaced with the Registered Officers Approval Committee which consists of the JSE Capital Markets trading heads, Market Regulation and the TMS Client Data team who will collectively consider the application for approval.

A consolidated application form for the registration of registered officers and traders has been developed, which is available via the JSE website. Phase one consists of a portal scheduled for go-live in early October, whereas Phase two will allow for logon, electronic submission and verification and is scheduled for go-live shortly thereafter.

The entire application process will now take up to three days to complete.

## **9. GENERAL**

### **9.1. STRATE**

DN mentioned to the committee that this item was raised by a committee member. An issue has arisen between the JSE, Strate and some members with regard to billing. Discussions have been taking place between the JSE, Strate and affected members. The discussions have led to directive BI to be suspended. DN thanked a committee member who raised the issue and that more consultations will take place around the issue.

A committee member mentioned that from an industry perspective there are two issues around the new rules for directive BI and that there might be a big commercial impact. The committee member did acknowledge that the JSE is busy changing its rules and that there is ongoing consultation between JSE, Strate and members.

### **9.2. MARKET STRUCTURE/NEW EXCHANGES**

DN mentioned that this agenda item had also been raised by a committee member. DN mentioned that with the FSB granting new licenses for new exchanges there have been questions about policy issues and market structure issues such as:

- Whether a national best bid and offer will exist;
- Whether a consolidated tape will exist; and
- Whether there would be rules around best execution.

With two exchanges being recently granted licenses, DN mentioned that the JSE had been approached by one of its members to raise the possibility of having a workshop. The workshop would include the new exchanges, the FSB and committee members about what the common understanding will be regarding market structure and to debate some of the above mentioned issues. Committee members agreed with the proposal.

DN said that it is for the common good that a workshop is set up and she will pass on the proposal to the JSE's CEO and ask that she reach out to the FSB regarding the possibility of having the workshop.

**DN thanked everyone for their commitment and for attending the meeting.**

**Meeting closed at 1pm**