MINUTES

Heading:	Currency Derivatives Advisory Committee Meeting
Date:	17 February 2016
Time:	11h00 – 13h00
Venue:	Johannesburg Stock Exchange - Serengeti Conference Room

Attendees

Warren Geers	Chairperson
Justin Nichols	ABSA
Woerie De Villiers	Farm Wise
Elaine Mabiletsa	JSE
Donna Oosthuyse	JSE
Brett Kotze	JSE
Paul Du Preez	JSE
Terrence Saayman	JSE
Alex Comninos	JSE
Andrea Maisel	JSE
Andre Koen	JSE
Athandile Maswili	JSE
Justin Kightley	Nedbank
Gavin Betty	Peregrine (Conf. Call)
Greg Kennelly	RMB (Conf. Call)
Dianne Bates	RMB Clearing
Jan Badenhorst	RMD (Conf. Call)
Tom Anderson	Standard Bank
Andrew Gillespie	Tradition (Conf. Call)

Apologies

Philip Blom (RMB), Nongcebo Mthembu (SARB), Ross Hooper (SARB), Kobus Venter (ABSA), Garith Botha (Standard Bank), Steven Greenstein (Investec), Jayson Gordon (Standard Bank Clearing).

No	Items	Action Item
1.	**WELCOME** The Chairperson, Mr. Warren Geers, chaired the proceedings. He welcomed all members present and declared the meeting open at 11h00.	
2.	**CONFIRMATION OF MINUTES** The previous minutes were adopted as a true reflection of the meeting held.	
3.	**ACTION ITEMS FROM PREVIOUS MEETING MINUTES** Mr. Geers reported that there were no open items from the previous advisory committee meeting.	
4.	**PROPOSED NEW MEMBERS AND RESIGNATIONS** • Mr. Geers welcomed the new Currency Derivatives trading members; Kaon Capital and Constellation Capital. • Mr. Geers announced the resignation of Eben Karstens from Matrix from the advisory committee and thanked Mr. Karstens for his contribution and participation over the past years.	
5.	**FEEDBACK: CLOSE-OUT AUCTION** • Mr. Geers stated that the Close-Out Auction was successfully and efficiently executed. • Mr. Geers mentioned that all the banks that took part in the close-out auctions did not encounter any issues with the close-out process. • Mr. Geers shared the results from the 3 auctions: AUCTION 1 — • 75 000 contracts filled AUCTION 2 — • 27 838 contracts filled AUCTION 3 — • 0 contracts filled • Mr. Geers stated that there were requests from the banks to introduce the Euro and Pound in the close-out auction. • Mr. Kennelly expressed concern that if the participant is long Euro/Rand and short Dollar/Rand they would have to do an all-or-nothing since it poses a complexity given different types of contracts. • Mr. Nichols stated that the process went well on their side. He recommended an auction be done for Euro/Dollar to negate the complexity raised by Mr. Kennelly. • Mr. Geers stated that the exchange would have to get dispensation from the	

	Reserve Bank to implement an auction for the other currencies as currently the dispensation is only for the USD/ZAR contract. • Mr. Geers stated that the exchange would investigate how to include EUR and GBP in the auction taking into consideration the challenge raised by Mr. Kennelly and suggestion from Mr. Nichols. This would not be considered for the March close-out. • Mr. Geers thanked the market makers for their participation and ensuring the success of the currency derivatives close-out auction and to Mr. Koen and the team for their work in the process.	
6.	**NEW PRODUCTS/ INSTRUMENTS** ***Contracts listed*** • Mr. Geers mentioned that the Hong Kong/Rand futures contract was listed on the 14th of January 2016. • The Botswana Pula/Rand was listed; however, the obligation to trade the instrument was not fulfilled by the trader. • Mr. Geers stated that if the contract is not traded within the next three months it will be suspended, however, in the interim, daily valuations and margining will continue to be done. ***Request For Quote (RFQ) Demo*** • Mr. Geers mentioned that the demonstration of the RFQ functionality was shown to the banks and they are comfortable with it. • The RFQ is presently available for trading Currency Futures and not for options. • Mrs. Mabiletsa took the committee through the RFQ demonstration with the help of Mr. Petersen. • Mr. Nichols stated that the issue with the responder screen enabling the requestor's trading side for quoting is wrong and won't work for the market. • Mr. Geers noted the member's concern and mentioned that this matter will be looked into for correction. • Mr. Nichols asked if auto-quoting is possible and stated that connecting via API should enable price streaming for RFQs. ***Forward Forward FX*** • The *FWDFWD* contracts are predominantly bank to bank dealings and the instrument will be traded at a contract size of $1,000,000.	

	• A forum will be held with the participants in the 1st week of March 2016. ***African Currency*** • The JSE was awarded the *FOW* International Awards 2015: Most Innovative New Contract for the African Currency suite. • Mr. Geers stated that there have been some issues with the listed African Currency futures. He stated that the banks are having difficulty making prices for these instruments which poses as a challenge to the exchange, as there are participants who want to trade the African currencies however there are no prices available for them to trade. • The issue that some banks face is that they are unable to price the instruments because the underlying currency is not trading which makes it difficult for pricing of the futures. • Mr. Gillespie stated that pricing exists for the Zambian Kwacha except the prices are wide. He also mentioned to the committee that there has been an interest for the Ugandan shilling and Malaysian rupee and that he will submit a request for listing once there is a firm order from the client.	
7.	**INCENTIVE BILLING** • Mr. Geers highlighted that volatility seen in December 2015 impacted the pricing and spread levels in the currency futures market. He mentioned that for the dollar contract, banks had to make prices 200 bps wider than required and even wider on the other currencies. • Mr. Geers added that the way the model was designed is around monitoring the futures spread and not the futures over and above the underlying spot spread. • Mr. Geers advised that he has been to see the banks to solicit their feedback on how to go about fixing the model and making it appropriate. • Mr. Nichols and Mr. Anderson both articulated the inappropriateness of the spread as a requirement and qualifying criteria. • Mr. Anderson stated that time on-screen and quantity is a more relevant requirement. • Mr. Geers stated that the exchange would look into removing the spread as a requirement. • Mr. Geers mentioned that the market makers have enjoyed a 55% reduction in booking fees irrespective of whether they met the obligations or not. • Mr. Anderson highlighted that the use of Reuters as a benchmark for price discovery	

	is becoming less relevant. • Mr. Kightley added that most market makers are making use of other platforms for pricing which are not discoverable by the exchange. • Mr. Geers stated that the JSE relies on Reuters for one impartial view of the price levels. • Mr. Anderson raised the concern of doing 10 iterations over 5 minutes on Reuters and that in six months' time one can get two iterations where nothing trades on Reuters. • Mr. Geers added that potentially there could be a two-tier mark-to-market for the liquid and illiquid contracts. • Mr. Geers added that there needs to be an internal discussion at the exchange on what to do to mitigate the dependency of the exchange on Reuters. • Mr. Kennelly pointed out that the downside of the incentive model is that when a market maker is not on-screen for 2 or more days they will not qualify which does not incentivize them to make prices for the rest of the month since they already do not qualify for the month. • Mr. Geers mentioned that the concerns raised by the participants will be considered carefully and the incentive billing measuring components remodeled. • Mr. Geers also added that he would meet with the four banks to get their views, to redesign the model and to come up with an appropriate solution. • It was agreed that the spread level would be removed as a qualifying criteria in the incentive model, pending a final discussion with the Head of Capital Markets and explore the impacts on IT systems. ***Iteration Process*** • Mr. Geers touched on the iteration process and asked the participants what their views are especially now that the auction process is implemented at close-out. He asked whether the 5 minute iteration period should be prolonged or shortened. • It was agreed at the advisory that 5 minutes is adequate.	
8.	**TAKING A TURN AND COMMISSIONS - GIVE UP TRADES** • Mr. Comninos reported that the exchange is continuing to investigate solution options to assist the market in the processing of commissions for agency trades • Mr. Comninos stated that after initially expressing reservations to the proposal to facilitate commissions via JSE Clear daily processes, the clearing members are now	

	largely on board with the process • The initial solution considered involved integration with the deal management module of the new clearing system to be delivered in ITaC. Other potential solutions include an alternative solution in the new clearing system and the FIA technology platform which is widely used by the broker community abroad. • Mr. Comninos mentioned that as soon as the investigations are completed the exchange would engage the participants and create a forum to discuss further.	
9.	**<u>ITAC UPDATE</u>** • Mr. Geers requested that the participants make their teams aware of the changes that will be implemented with ITAC and take note of all correspondence sent out regarding ITAC and updates. • Mrs. Maisel advised the committee that the Currency Derivatives falls under Project 1 Phase 1 C. • Mrs. Maisel mentioned that the draft API was sent in December and the final API document will be sent out at the beginning of March 2016 as well as the connectivity details and requirement for the test and production environment • The CTS test environment will be available June/July 2016 • Mrs. Maisel advised that the team is currently busy with the Internal Technical Integration and so far it is going well. • The Currency Derivatives go-live will follow 2 months after equities however if testing goes well these dates will be revised. • Mr. Comninos added that deal management will be facilitated on *Cinnober* on the clearing system and the specifications will come out at least 12 months before go-live however the specifications will go out to the market within the first quarter of 2016.	
10.	**<u>MARGINING: J-SPAN PARAMETERS</u>** • Mr. Du Preez explained to the committee how the margining framework works. • Mr. Du Preez stated that on the clearing system each contract is loaded with an absolute Initial Margin (IMR). • The clearing system will apply a Calendar Spread Margin (CSMR) on a standard currency contracts with the same short name. • However on an Any-Day and standard currency futures combination, the system detects that the codes and names are not the same and does not apply the CSMR but instead applies a Series Spread Margin (SSMR), making the initial margin higher	

	than it would have been had the spread involved only two standard currency futures contracts with the same short name e.g. ZAUS. • A committee member asked whether the J-Span is across asset classes for the Currency Derivatives and Interest Rates Derivatives market, and Mr. Du Preez advised that it does not currently. • Mr. Gillespie queried why the JSE is 200% more expensive than CME and ICE when it comes to the initial margin on the Dollar Rand. • Mr. Du Preez stated that when the IMR model was changed a couple of years ago the JSE did take into consideration how it compares to other exchanges however it was very risky for the exchange to base the initial margin on what other clearing houses were doing. • Mr. Du Preez added that the structures of the clearinghouses are not similar, and that the JSE has fully segregated client accounts whilst other clearing houses may not have. • Mr. Gillespie advised that it is hard to convince an international client to bring their business to the JSE when the IMR is about 200% more when compared with an international counterpart such as ICE. • The committee member queried if it is possible for the exchange to put out a discussion document or article to the public domain explaining why the JSE is charging more initial margin than other exchanges. • Mr. Saayman stated that it will be more valuable to have a one-on-one with the participant to show them how the initial margin is determined and what is considered, however the exchange is happy to put a document together for the parties interested. • Ms. Oosthuyse suggested the discussion document include benchmarks comparing the methodology that is being used by the JSE and other exchanges. • Mr. Betty queried if the exchange foresees an increase in the initial margin going forward. • Mr. Du Preez stated the exchange tries to maintain stable IMR and not to have margin surge rapidly when there is volatility. • Mr. Saayman added that the volatility witnessed in December has been factored in the prevalent margin levels at the exchange and does not anticipate margins increasing to the levels which they did in December 2015.	Mr. Du Preez

Add-On Margin

- The JSE will implement a framework whereby the JSE will stress-test each account every day; observe the P&L under the stress-test scenario; compare it to the initial margin, and when the difference exceeds a threshold of R250 million (half the size of the default fund), the excess will be applied as an additional initial margin.
- The worst case stress scenario for the interest rate derivatives market is currently a curve shift of roughly 150 bps, mainly driven by the events observed in December 2015.
- In the IRC market there is currently no account that is impacted by add-on margins.
- On the issue of non-cash collateral, Mr. Du Preez mentioned that the delay in implementation of the add-on framework was due to participants believing it is not fair to implement such a framework without an opportunity being given to participants to pledge non-cash collateral against the exposure.
- The rule changes to allow for non-cash collateral have been drafted, and the legalities surrounding the implementation examined. The rules will be circulated for public consultation.

11. <u>CURRENCY DERIVATIVES STATISTICS</u>

- Mrs. Mabiletsa provided the committee with a 2015 review of the Currency Derivatives market.

Currency Futures and Options				
Period	Deals	Contracts Traded	Value Traded	Open Interest
2014	46 955	44 634 070	R 516 200 008 974.31	3 601 849
2015	60 514	45 168 690	R 603 975 857 052.10	3 332 297
% Change	29%	1%	17%	-7%

- In terms of the product split, Currency Futures make up 71% of all contracts traded and the Standard Option makes up 20% of the total market.
- There was a significant increase in African Currency Futures contracts. The total contracts traded in 2014 were 170 747 and in 2015, 875 117. This is also owed to the fact that African Currency Futures were introduced late 2014
- Mr. Geers commented on the remarkable growth in the Currency Derivatives market and thanked the committee members and participants for the value they bring to the market.

12. <u>GENERAL</u>

- Mr. Anderson requested an update on the RAIN contract.
- Mr. Geers stated that the value of the RAIN contract index has gone up and there

	has not been a demand to trade the instrument. Mr. Geers also added the exchange can offer the RAIN contract to the market if there is a demand and if market makers are willing to price it. • Mr. Anderson advised that Standard Bank would be willing to make prices for the RAIN contract. • Mr. Koen added that the contract is currently being marked-to-market and that the exchange needs to republish the weightings and margin it. • Mr. Geers stated that the exchange is prepared to look into restoring the RAIN contract to the market.	
13.	**<u>CLOSE</u>** • Mr. Geers asked the committee for their final remarks. • He thanked the committee for attending the Advisory meeting. • The meeting adjourned at 12h45	