Minutes

Heading:	Currency Derivatives Advisory Committee Meeting
Date:	Wednesday 19 March 2014
Time:	12h30
Venue:	Johannesburg Stock Exchange - Serengeti Conference Room

Present	Graham Smale	(Chairman)
	Gavin Betty	(Peregrine Derivatives – Conf. Call)
	Kobus Venter	(ABSA Bank)
	Justin Nichols	(ABSA Bank)
	Eben Karsten	(Matrix FM – Conf. Call)
	Steven Greenstein	(Investec Securities)
	Raymond Pretorius	(IRESS)
	Greg Kennelly	(Rand Merchant Bank)
	Philip Blom	(Rand Merchant Bank)
	Dianne Bates	(Rand Merchant Bank Clearing)
	Tom Anderson	(Standard Bank)
	Andre van der Merwe	(Standard Bank)
	Andrew Gillespie	(Tradition)
	Andre Koen	(JSE)
	Cindy Pillay	(JSE)
	Jacob Shayi	(JSE)
	Warren Geers	(JSE)
Apologies	Nicky Newton-King	(JSE)
	Alan Yates	(Investec Securities)
	Ross Hooper	(Reserve Bank)
	Woerie de Villiers	(Farmwise)
	Jan Badenhorst	(RMB)
Secretary	Brigid Gilbee	

Minutes:

No	Items	Action Item
1.	**<u>WELCOME</u>**: Mr. Smale welcomed the Committee members to the meeting and thanked them for their attendance at this meeting.	
2.	**<u>CONFIRMATION OF MINUTES</u>**: The minutes of the meeting of the Currency Advisory Committee held on 21 August 2013 were approved.	
3.	**<u>PROPOSED NEW MEMBERS AND RESIGNATIONS</u>**: Mr. Geers advised the Committee that a resignation from the Committee has been received from Mr. Andrew Bryson (Nedbank Private Wealth). It is proposed that Mr. Justin Kightley of Nedbank Capital be appointed to serve as a member of the Committee. The Committee **<u>AGREED</u>** that Mr. Justin Kightley should be appointed to serve as a member of the Currency Advisory Committee.	JSE to notify members accordingly – Cindy Pillay (CP)
4.	**<u>BLOCK TRADE RULE AMENDMENTS – 201 DOLLAR/RAND RULE</u>**: It was **<u>NOTED</u>** that the Market Regulation team are in consultation with members of the market in connection with proposed changes to the rules and directives for the reporting of various Report Only trade types. These changes cover not only Currency Derivatives, but also Bonds and Interest Rate Derivatives. The Market Regulation team will propose a final rule change as soon as this consultation process has been completed. Thereafter the rule change will be submitted to the Currency Advisory Committee for comment. After taking into account all comments received from the Trading and Advisory Committee, the JSE will consult with the FSB informally in relation to the proposed rule changes. The draft will then be submitted to the JSE Executive Committee for consideration and approval. Once this has been concluded, official changes will be submitted to the FSB. Should the rule be approved by the FSB, this will be communicated via the Government Gazette. The Rule and Directive will then become effective. Mr. Geers advised the Committee that in respect of the proposed rule and directive change, the JSE will create different reference fields on the reporting system. In these fields, the bank will capture the reason why they are doing a reported trade under the 201 Dollar / Rand rule. These trades will only be permitted between a bank and a professional counterparty (subject to certain criteria) and will not be permitted to take place between two brokers.	

	Mr. Kennelly confirmed that having reviewed the proposed rule change, he was satisfied that the change would address the potential risks that banks would be exposed to by not being able to book such trades. It was **AGREED** that once the proposed rule and directive changes have been discussed with the market and agreement has been reached on the changes, these should be circulated to members of this Committee for round robin approval which it is expected will be before the next Advisory Committee meeting.	
5.	**TRADE BUSTING RULES**: Reference was made to a draft document setting out the proposed trade cancellation and trade price adjustment rules, copies of which were circulated prior to the meeting and the content of which was **NOTED**. Mr. Shayi advised the Committee that the Market Regulation team have requested that the Committee review the proposed rule and submit any comments they may have in writing to the Currency Derivatives team as well as the Market Regulation Division at the following email addresses currencies@jse.co.za and surveillance@jse.co.za. Mr. Shayi advised the Committee that the proposed rule intends to indicate how the JSE will cancel trades and make trade price adjustments in the event that a particular party has made an error in inputting a trade. Reported trades will not be covered by the proposed rule. Mr. Smale indicated that with the change from the Securities Services Act to the Financial Markets Act which was promulgated on 3 June 2013, there was a six month window within which the JSE had to make any amendments which were required to be made to the JSE rules to ensure that these aligned to the Financial Markets Act. This period has been extended to the end of April 2014 and market notices have been sent out to market participants highlighting the implications that the required rule changes will have on the relevant rule books. In response to a question raised by Mr. Pretorius, it was **NOTED** that the JSE has ensured that there are a common set of principles, across the various markets applying to trade cancellations and trade price adjustments, however the parameters which apply in respect of these trades in the respective markets may differ. Mr. Pretorius suggested that the terminology applied in respect of these trades be standardised across the various markets (trade busting versus the cancellation of a trade). Mr. Geers indicated that this was the case and that the heading on the agenda mistakenly referred to trade busting instead of trade cancellations.	

	Mr. Pretorius queried whether the proposed trade cancellation and trade price adjustment rules would have any systems impact. Mr. Shayi indicated that there should not be any system impacts as a result of the introduction of these rules. Mr. Pretorius indicated that should this change, lead time will be required to enable such changes. Mr. Geers specifically requested that Market Makers review the proposed rules in detail to ensure that they are satisfied that these rules cater for their requirements.	
6.	**LISTING AND TRADING OF AFRICAN CURRENCY PAIRS**: It was **NOTED** that following the Advisory Committee meeting held in March 2013, it was concluded that banks would be interested in being Market Makers for African Currency pairs if there was a demand for the product. Since the last discussion, there has been an increase in the market appetite for trading African Currency Pairs. As is the standard for the listing of new Currency Pairs, the exchange will only list a pair if there is a committed trade behind a deal and will make Mark-to-Market prices available as long as the incumbent is in existence. The secondary requirement would be commitment from the banks to make prices available on spot and forwards as per the current process. Mr. Geers indicated that previously the JSE listed the Botswana Pula and as a result of no interest in the product, it has been suspended and is no longer available for trading. Mr. Geers queried whether members of the Committee would be interested in trading African Currency Pairs. Mr. Gillespie of the Committee indicated that in his view there was demand for such an offering and that it would be strategically important for the JSE to pursue and to ensure the listing of African securities takes place on the JSE rather than on other African exchanges. Mr. Greenstein suggested that the contract lengths in respect of these products be kept to shorter periods to mitigate potential reputational risk in the event of an issue being experienced in trading these products. Mr. Greenstein suggested that only near contracts be considered initially to enable the JSE to assess the liquidity of such contracts. Mr. Geers indicated that this would be the case. Mr. Greenstein indicated that from an authorised dealer perspective there is the ability to hedge firm and ascertainable NDF's. He explained that if a broker is hedging a future they may need to do a hedge with an NDF. This would however require specific SARB clearance.	

	Mr. Greenstein suggested that discussions take place with National Treasury to ensure that an African Future can be hedged with an African NDF. Mr. Geers indicated that when this was discussed with the Reserve Bank, they advised that the JSE could list any Currency Pair (even African Currency Pairs) and did not raise any issues in respect of NDF's. It was however **AGREED** that the JSE should review the SARB application process to determine whether this catered for NDF's and non-NDF's. Mr. Geers advised the Committee that currently, all Mark-to-Market and fixing is done at 17h00. If the JSE is asked to use a 12h00 fix, trading will happen after the fixing. It was suggested that the central bank fix be used as a reference. The Committee **AGREED** with this approach. It was **NOTED** that interest has been expressed in currencies from Keyna, Zambia, Nigeria, Botswana and Mauritius. It was **AGREED** that Mr. Geers should send a document to members of the Committee on work that the JSE has done in respect of margining of African Currency Pairs. Mr. Geers suggested that instead of inverting these currency pairs, the nominal should be changed. Mr. Geers indicated that previously the requirement came from the hedge fund industry to invest currency pairs. It was **AGREED** that Currency Pairs should not be inverted to Rand and the nominal should rather be increased. It was **AGREED** that a market notice should be sent out indicating that the JSE will continue to list Currency Pairs on condition that there is open interest in the contract. If there is no open interest in a particular contract, it will be suspended until the JSE is advised that there is a requirement for such a contract to be listed again.	JSE - Warren Geers (WG) will review the SARB application process. WG to circulate margin requirements to the committee for review. WG to send market notice of suspension of non-trading currency pairs.
7.	**RISKS ASSOCIATED WITH HIGH OPEN INTEREST**: It was **NOTED** that March 2013 was a record month for the Currency Derivatives market with the overall highest Open Interest ever held of 4.2 million contracts. Specifically looking at the 17 March 2014 expiry, running up to the close out, on 3 March 2014, there was an open interest of over 1,622,980 million contracts in the US Dollar/Rand contract. The current close-out process is for a period of five minutes, where ten iterations of the arithmetic average of the underlying traded spot price is taken every thirty seconds. The concern is mainly around the possible occurrence of the large open interest not being rolled to the next expiry and rather left to close out.	

	This only gives members the limited time period of five minutes to exit the position and at one point in time, this exposure could have been R17,5 billion, which could have an impact on the underlying spot market. Mr. Geers suggested that members of the Committee discuss any potential measures which the JSE should take to avoid the risks associated with high open interest. A suggestion was raised to potentially increase the close-out period but it was agreed to leave the process as is. Extensive discussion ensued and the Committee **AGREED** that in respect of high open interest, there is no risk mitigation which is expected to be pursued by the JSE. It was **AGREED** that during June 2014, if any concerns are raised by market participants, the JSE will send an email to market participants indicating that they should be aware of their positions.	
8.	**INTEGRATED TRADING AND CLEARING PROJECT (ITaC)**: As previously communicated, the JSE has set a strategy for 2017, key elements of which involve integrated trading and clearing. The JSE has concluded the analysis and made decisions to embark on a strategic journey to transition all Derivatives markets and the Interest Rate market across to a single new trading system and a single new clearing solution. This extensive programme of work for all of the markets will be phased in over a number of years. The JSE still needs to satisfactorily conclude contract negotiations with the potential vendors. All of the Derivatives markets and the Interest Rate market will take at least three years to transition, commencing with the replacement of the Equity Derivatives trading and clearing platforms. Planning of the various project phases will be done in such a way that the change can be digested by both the JSE and its clients. The JSE is firmly of the view that this strategic journey is critical to the JSE enhancing the quality of its products and services to the South African and Global financial community. Ongoing engagement with market participants will take place in respect of this project. Mr. Geers indicated that it is of utmost importance for all participants to understand the implications of this project including prime brokers, clearing members. This is particularly true in respect of API connections as new connections will need to be developed when the new system is implemented. It is anticipated that the JSE will no longer provide front-ends when the new system is implemented.	

Mr. Geers indicated that once the process has been defined and agreed on, engagement will take place with all members of the Committee from a business perspective to ensure that the impact to each entity is as limited as possible.

Mr. Pretorius queried whether the trading and the clearing platforms would be two separate platforms. Mr. Smale confirmed that this would be the case. Both the trading and clearing platforms will be implemented simultaneously for each market that goes live.

9. **BILLING MODEL REVIEW**:

Mr. Geers advised the Committee that it is the JSE's philosophy that as liquidity increases, the JSE will attempt, where possible, to decrease its prices. As a result, the team is currently exploring new billing models to assist trading participants. No fees will be altered or changed until consultations have taken place with trading and clearing members.

Once the majority of participants are satisfied with the new fee methodologies, the JSE's Executive Committee will need to agree and ratify the proposed new fee structures. Market participants will however be provided with notice of the new billing model once this has been approved.

10. **CURRENCY FUTURES STATISTICS**:

Ms. Pillay provided the Committee with an overview of the current statistics relating to Currency Futures as follows –

Year	Volume Traded	Value Traded
Jan – March 2013	5 038 087	R47 131 297 682
Jan – March 2014	10 040 908	R114 650 800 224
% Increase	**99%**	**143%**

11. Ms. Pillay provided the Committee with an overview of the current statistics relating to Currency Options as follows –

Year	Volume Traded	Value Traded
Jan – March 2013	2 574 424	R17 101 540 271
Jan – March 2014	2 356 021	R31 274 593 876
% Increase	**-8%**	**83%**

Ms. Pillay provided the Committee with an overview of the current statistics relating to Currency Futures and Options as follows –

Year	Volume Traded	Value
Jan – March 2013	7 612 511	R12
Jan – March 2014	12 396 929	R145
% Increase	**63%**	**127%**

	It was **<u>NOTED</u>** that a record day in terms of Currency Derivatives was realised on 12 March 2014. The market had its best single day performance since its inception on this day with value traded of R36 billion.	
12.	**<u>GENERAL</u>**: <u>Close Out Methodology</u>: Mr. Geers indicated that concern has been raised around the difference in the close out methodology for all other Currency Pairs compared to that of the US Dollar/Rand contract. The current process is as follows – <u>US Dollar Rand</u>: 10 iterations, arithmetic average of the underlying traded spot price taken every thirty seconds for a period of five minutes, commencing at 09h55 and ending at 10h00 New York time. <u>All Other Currency Pairs</u>: 10 iterations, arithmetic average of the foreign cross (e.g. NZD/USD) mid-price (of the bid and offer) taken every thirty seconds and crossed at every iteration with the USD/ZAR price for a period of five minutes, commencing at 09h55 and ending at 10h00 New York time. Mr. Geers queried whether members of the Committee felt that the same logic and methodology that applies in respect of the US Dollar/Rand pair should apply to the Euro/Rand. The suggestion was raised to use the last traded price. <u>Super Derivatives versus Bloomberg</u>: Mr. Geers advised the Committee that Super Derivatives charge in a completely different manner to the way in which Bloomberg charges. The Post Trade Services team feels that it would be more prudent to continue with Super Derivatives until such time as the new Integrated Trading and Clearing Platform is implemented at which stage this decision can be revisited if required.	