

Memorandum

Date: 19 June 2023

Subject: Proposed amendments to the JSE Derivatives Rules – Exchange for Risk Trade

Dear Member,

Transactions in the agricultural commodity market sometimes include the off-book negotiation and execution of a trade in futures contracts between two parties which is then reported to the JSE trading system, in conjunction with the simultaneous execution of an equivalent, but opposite, over-the-counter (OTC) derivative transaction in the same underlying commodity. The objectives of this activity can include, inter alia, hedging, price and/or credit risk management, as well as physical delivery, and cash or liquidity management.

Members will be aware of the off-book trade criteria in derivatives rule 7.115, which specifies the types of transactions that may be validly reported to the JSE trading system. One of these transaction types - the Exchange for Risk (“EFR”) Trade - described in rule 7.115.1.3, is defined in the derivatives rules as a type of EFRP (“Exchange for Related Positions”) where two trading members, a trading member and a client, or two clients, enter into an agreement whereby the parties unwind an existing OTC derivative contract between them by concluding an off book transaction in commodity futures which replaces the OTC derivative contract, and report the futures transaction to the JSE trading system.

The current EFR definition in the derivative rules only contemplates a specific scenario, where the parties unwind or close out an existing OTC derivative transaction or contract between them, and simultaneously report an off-book futures trade to replace the OTC trade.

The JSE Market Regulation Division has recently received a request from a market participant to expand the scope of the current EFR definition in the derivative rules to accommodate situations where the parties to an EFR, depending on their objectives, need to execute or enter into a new OTC derivative transaction between them, in the same underlying commodity, and simultaneously report an opposite off-book futures trade to the JSE trading system.

The JSE Market Regulation Division has done research into the equivalent rules on other commodity exchanges, such as the Chicago Mercantile Exchange (CME), and is confident that the proposed amendments to the JSE derivatives rules, as reflected in Annexure A, are compatible with the EFR rules on those exchanges.
