CIRCULAR 091-22
August 2, 2022

REQUEST FOR COMMENTS

AMENDMENTS TO ARTICLE 12.5 OF BOURSE DE MONTREAL INC. TO MODIFY THE MINIMUM PRICE FLUCTUATION AND THE LAST TRADING DAY OF THE THREE-MONTH CANADIAN BANKERS' ACCEPTANCE FUTURES (BAX)

On July 11, 2022, the Rules and Policies Committee of Bourse de Montréal Inc. (the "**Bourse"**) and the Special Committee of the Regulatory Division of the Bourse approved amendments to the to the minimum price fluctuation (tick size) of the contract specifications for the Three-Month Canadian Bankers' Acceptance Futures (BAX).

Comments on the proposed amendments must be submitted at the latest on **SEPTEMBER 2nd , 2022**. Please submit your comments to:

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A copy of these comments shall also be forwarded to the *Autorité des marchés financiers* (the "**Autorité**") to:

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Please note that comments received by one of these recipients will be transferred to the other recipient and that the Bourse may publish a summary of such comments as part of the self-certification process concerning this file. Unless specified otherwise, comments will be published anonymously by the Bourse.

Appendices

You will find in the appendices an analysis as well as the text of the proposed amendments. The implementation date of the proposed amendments will be determined by the Bourse, in accordance with the self-certification process as established by the *Derivatives Act* (CQLR, chapter I-14.01).

Process for Changes to the Rules

The Bourse is authorized to carry on business as an exchange and is recognized as a self-regulatory organization ("**SRO**") by the Autorité. The Board of Directors of the Bourse has delegated to the Rules and Policies Committee of the Bourse its powers to approve and amend the Rules, the Policies and the Procedures, which are thereafter submitted to the Autorité in accordance with the self-certification process as determined by the *Derivatives Act* (CQLR, chapter I-14.01).

In its SRO capacity, the Bourse assumes market regulation and supervision responsibilities of its approved participants. The responsibility for regulating the market and the approved participants of the Bourse comes under the Regulatory Division of the Bourse (the "**Division**"). The Division carries on its activities as a distinct business unit separate from the other activities of the Bourse.

The Division is under the authority of a Special Committee (the "**Special Committee**") appointed by the Board of Directors of the Bourse. The Special Committee is empowered to recommend to the Board of Directors the approval or amendment of some aspects of the Rules of the Bourse governing approved participants. The Board of Directors has delegated to the Rules and Policies Committee of the Bourse its powers to approve or amend these Rules upon recommendation from the Special Committee.

AMENDMENTS TO ARTICLE 12.5 OF BOURSE DE MONTREAL INC. TO MODIFY THE MINIMUM PRICE FLUCTUATION AND THE LAST TRADING DAY OF THE THREE-MONTH CANADIAN BANKERS' ACCEPTANCE FUTURES

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I. DESCRIPTION

Bourse de Montréal Inc. (the "Bourse") hereby proposes to amend the minimum price fluctuation (tick size) of the contract specifications for the Three-Month Canadian Bankers' Acceptance Futures (BAX), such that the minimum price fluctuation for the third, fourth (the back "Whites"); the fifth, sixth, seventh and eighth (the "Reds"); the ninth, tenth, eleventh and twelfth (the "Greens") quarterly BAX contract months be increased from 0.005 index points (a half-tick) to 0.01 index point (a full tick). Additionally, the Bourse proposes to amend the last Trading Day of BAX contracts expiring after June 2024, from the third Monday of the contract month to the third Wednesday of the contract month, to better align with the exposure period of equivalent Three-Month CORRA Futures ("CRA") contracts.

In recent years, the Bourse implemented various tick size adjustments to accommodate market participants' needs (end users) including a gradual reduction on the BAX different contract months. As market conditions evolve, the Bourse is monitoring and re-evaluating its product specifications to make sure they are still appropriate and fulfill market expectations. The proposed increase in BAX tick size from half a tick to a full tick is particularly relevant in volatile market conditions, as experienced recently and is aimed at responding to the challenging liquidity in BAX markets. The proposed modification to the last Trading Day is, in that regard, a way to facilitate the transfer from BAX to CRA contract as the Canadian benchmark transition (from CDOR to CORRA) is accelerating. This change is considered minor but will allow a proper alignment of exposure periods between these two alternative products.

II. PROPOSED AMENDMENTS

The Bourse proposes to amend the minimum price fluctuation (tick size) of the BAX contract, such that the minimum price fluctuation for the third and fourth quarterly contract month (the back "Whites"); the fifth, sixth, seventh and eighth (the "Reds"), and the ninth, tenth, eleventh and twelfth (the "Greens") quarterly contract months be increased by from 0.005 index points (a half-tick), to 0.01 index points (a full tick). Therefore, the minimum price fluctuation for the ten most backdated quarterly contract months would be 0.01, representing $25.00 per contract.

Table 1: Proposed modifications to BAX minimum price fluctuation specification

Current Minimum price fluctuation specification	**Proposed** Minimum price fluctuation specification
0.005 = C$12.50 per contract for all contract months	**0.005, representing $12.50 per contract, for the six (6) nearest contract months: the two (2) nearest non-quarterlies (serials) and the four (4) nearest quarterly** 0.01 = C$25.00 per contract for all other contract months

Additionally, the Bourse proposes to amend the last Trading Day of BAX contracts expiring after June 28, 2024, from the third Monday of the contract month to the third Wednesday of the contract month, as detailed in the below table.

Table 2: Proposed modifications to BAX Last Trading Day specification

Current Last Trading Day	Proposed Last Trading Day
Trading of Canadian Bankers' Acceptance Futures ceases at 10:15 a.m. (Montréal time) on the second London (Great Britain) banking day preceding the third Wednesday of the Settlement Month.	**For contract months expiring on or before June 28, 2024**: Trading of Canadian Bankers' Acceptance Futures ceases at 10:15 a.m. (Montréal time) on the second London (Great Britain) banking day preceding the third Wednesday of the Settlement Month. **For contract months expiring after June 28, 2024:** Trading of Canadian Bankers' Acceptance Futures ceases at 10:15 a.m. (Montréal time) on the third Wednesday of the Settlement Month.

III. ANALYSIS

a. Background

When the BAX contract was introduced in April of 1988, the minimum price fluctuation (tick size) for all contract months was established at 0.01 index points (a full tick). In February of 2002, the Bourse reduced the minimum price fluctuation to 0.005 index points (a half-tick) for the three nearest listed contract months (the first quarterly BAX contract month and the two serial BAX contract months) as a greater level of granularity was in the best interest of the market.

In September 2014, at the request of market participants, the Bourse extended the minimum tick reduction to the second, third and fourth BAX quarterly futures contract months (the "Whites"). Based on an extensive market participant survey, the Bourse extended again the implementation of half-tick to the fifth, sixth, seventh and eighth BAX quarterly futures contract months (the "Reds") in March 2018. Finally, in September 2020, the Bourse applied the minimum price fluctuation change to the ninth, tenth, eleventh and twelfth quarterly BAX contract months (the "Greens").

Unfortunately, considering existing market conditions, short-term interest rates, volatility standards and industry commitments towards risk-free benchmark rate (CORRA), the liquidity for the BAX has been quite limited in recent months. The Bourse contends that the reasons cited for the change in 2014 and 2018 no longer apply in today's market environment. A wider tick would result in a higher minimum bid-ask spread, increasing the profitability of market making thereby encouraging liquidity. The higher trading costs, typically considered a negative factor, would still benefit users' transition towards CORRA futures. The latest statistics on the BAX market evolution are presented in tables 3 and 4.

Table 3: BAX contract average daily volume ("ADV") by contract year

Year	BAX Whites	BAX Reds	BAX Greens
2017	81 832	32 187	1 829
2018	81 398	32 666	1 545
2019	82 032	34 867	1 891
2020	60 623	28 704	2 045
2021	55 734	47 246	7 875
2022 (March YTD)	56 104	21 692	1 580

Source: Montréal Exchange

Table 4: BAX Average Bid / Offer spread by contract year[1]

BAX Whites	0.0065
BAX Reds	0.0116
BAX Greens	0.0382

Source: Montréal Exchange

Various benefits support the recommended increase:

1) Market quality improvement: Increasing the tick size is expected to provide a better balance between liquidity at each price point and optimal spreads. The Bourse believes that the current tick size level is causing liquidity misbalances and may not offer, in the current environment, the right tradeoff between promoting liquidity and fair transaction costs. In a context of increased short-term interest rate volatility, a wider tick size would offer a more stable pricing structure. With increased order size and number of orders at best price levels (increased depth), the foreseen augmentation should enhance market stability and improve the overall BAX market depth.

2) Market participation support: Having a full tick minimum price fluctuation unit would potentially increase the number and diversity of market participants. It is expected that increasing the minimum tick size will re-ignite and broaden participation from active traders who provide essential liquidity to this sector of the listed Canadian yield curve. Both hedgers and speculators are key to the health of the BAX, and it is crucial to ensure that each group makes up a sustainable proportion of the overall market. A healthy futures market needs a diversified mix of market participants and trading strategies.

3) BAX structure optimization: From an economic perspective, the Canadian short term interest rate (STIR) market has been experiencing a sharp (and historic) steepening since October 2021. The tightening monetary policy from the Bank of Canada and the multiple

[1] Statistics reflect the regular trading hours (from 6 a.m. to 4:30 p.m ET) between November 1, 2022 and May 31, 2022.

past and projected rate hikes suggest that the highly volatile period in the BAX market may persist for some time. Given this context, the importance of having competitive bid-ask spreads is essential.

4) Strategic measure and transition to CORRA: A full tick is deemed more costly, especially considering the market environment where the bid/ask spread is lower for comparable products in OTC markets.[2] Ultimately, the increase is viewed as a strategic incentive as higher trading costs encourage a faster transition to CRA, which has a smaller tick size.[3]

5) New covered trade functionality:[4] The Covered Trade functionality can be used to achieve the simultaneous execution of combinations that would incur significant execution risk if "legged" individually. Expanding the minimum width of the bid-ask spread would only contribute to the risk of slippage when executing these combinations individually. Therefore, a functionality (such as Covered Trade) that eliminates execution (slippage) risk becomes more advantageous to use in the context of a full tick in the BAX market.

The Bourse has conducted extensive consultations with market participants to gauge their interest in an increased minimum price fluctuation in BAX Whites, Reds and Greens. The participants' feedback was centered around the principal benefits summarized above.

The CRA contract was introduced in June 2020 to support the transition efforts initiated by the Canadian Alternative Reference Rate working group (the "CARR"). The CARR was created in 2018 to identify and pursue a new Canadian Dollar risk-free rate benchmark that is robust, reliable and resilient to market stress and manipulation (consistent with IOSCO principles[5]). The CARR quickly identified CORRA as the primary alternative benchmark to CDOR, and has since worked on ways to facilitate the transition in the Canadian market. In May 2022, Refinitiv, the benchmark administrator of CDOR, published a notice stating that the calculation and publication of all tenors of CDOR would permanently cease after June 28, 2024. As a result, the Bourse expressed its commitment to support the transition efforts[6] and is determined to make the necessary adjustments to its product offering.

Based on the specifications of the BAX and CRA products and because of conventions in the CAD interest rate markets,[7] there is currently a two day gap between the start of the exposure period of the BAX and that of the equivalent CRA contract. That is because BAX expires on the 3rd Monday of the month while CRA reference periods are based on International Monetary Market ("IMM") dates (3rd Wednesday of the contract month). This particularity creates a small curve risk when trading the BAX/CRA spread strategy for a given month.

[2] Forward rate agreements (FRA's) in the OTC market and on alternative trading platforms offer smaller minimum price fluctuations than the BAX.

[3] The minimum price increment for the CRA contract is 0.0025 (¼ tick) for the first contract month and 0.005 (½ tick) for the other months).

[4] See Technical Notice 22-006 for more details

[5] See Bank of Canada Press Release for more details

[6] See Advisory Notice A22-004 for more details

[7] In the case of CDOR, as opposed to other IBOR rates (including US Libor), there is no lag period, meaning that the fixing date is also the settlement date (value date).

Example for September 2022 contract month:

- BAX provides an exposure on the (forward-looking) 3M CDOR rate as of the expiry date (September 19).
- CRA provides an exposure to the daily compounded CORRA rate, starting Wednesday, September 21, up to the next quarterly IMM date.

As there is now an end date to CDOR[8] (BAX's underlying) and because the Bourse is planning[9] to convert outstanding positions in BAX to 3M CORRA Futures for post-June 2024 expiries, we are proposing to align the start of the exposure period of the two contracts by moving the expiry date for BAX, from the 3rd Monday of the month to the 3rd Wednesday of the month, for post-June 2024 expiries. This is, in fact, requested by current users of CORRA Futures and is seen as a way to facilitate the transition from BAX to this product. The change would apply only to post-June 2024 expiries, as some participants expressed reservations if this were to be applied to more short-dated expiries. Given the actual steep shape of the short-term curve and the higher open interest level for short-dated BAX contracts, this was suggested to minimize potential impacts of such changes on the pricing of the contract. On this, it should be recognized that, based on the plan of the Bourse to convert BAX into equivalent CORRA Futures contract, any transactions on BAX contract months expiring after June 2024 should already consider the difference in exposure period, rendering this change a way to remove any ambiguity.

b. Objectives

The objective of the proposed amendments is to enhance the execution and efficiency of the BAX contract, optimizing the BAX market structure. The idea behind the tick size change is to provide a perfect price tradeoff between the incentives that a wider tick entails (ie: market making activities, incentives for investors to place orders) and the higher resulting trading costs, which are offset strategically by the need to transition flagship status from the BAX to CORRA futures

Additionally, the proposed change in aligning the BAX last Trading Day specification with the CORRA contract is expected to increase the utility and the effectiveness of its derivatives market for both hedgers and speculators involved in the short-term interest rate markets. By supporting market participants' ability to hedge their exposure on CORRA, the specification change should attract additional trading volume as we approach full cessation date. A contract that solves the curve risk mentioned previously would tailor the product to participants' needs and attract more activity to the transparent and centrally cleared futures market.

The Bourse believes this change to be beneficial to the Canadian derivatives market as a whole and that both the proposed increase in minimum price fluctuation and adjustment to expiry contracts will yield favorable results in the BAX market while the industry transitions to CORRA futures.

[8] See official press release made by Refinitiv on May 16, 2022

[9] See Advisory Notice A22-004 that provides an update on BAX and CRA contracts

c. Comparative Analysis

Increasing the minimum price fluctuation by half would be in line with the specification standards put in place by Australia's exchange, as reflected in the full tick size for the 90-day bank bill. Considering that Australia is a market that resembles Canada's in several respects (liquidity levels, types of clients, banking system), the Bourse does not consider the increase as a deviation from its respective peers. Moreover, liquidity levels in the U.S. and Europe have not experienced major disruptions under the current half tick environment.

Table 4: Minimum price fluctuation for 3M STIR futures

Futures contract	Exchange	Minimum price fluctuation
BAX (current structure)	Bourse de Montréal	0.005 = C$ 12.50 per contract for all contract months
Eurodollar	CME	0.0025 = $ 6.25 for the nearest expiring contract month 0.005 = $12.50 for all other contract months (up to 10 years)
3M Euribor	ICE	0.005 = EUR 12.50 for all contract months (up to 6 years)
3M Euroyen	TFX	0.005 = JPY 1,250 for all contract months (up to 5 years)
90-day Bank Bills	SFE (ASX)	0.01 = approx AUD 24 for all contract months (up to 5 years)

Source: Contract specifications on exchange websites

Table 4 demonstrates that other major and peripheral international STIR contracts have a minimum price fluctuation similar to what is currently offered by the Bourse. The 90-day bank bill, considered an international benchmark in the STIR future space for its comparable market structure, has a similar tick size to the Bourse's new tick size proposal.

Regarding the last Trading Day, moving it to the 3rd Wednesday of the contract month would be in line with the former 3M Sterling in futures at ICE. However (and more importantly), the exposure period would be aligned with that of comparable contracts that include a conversion mechanism to equivalent risk-free rates contracts, which is based on IMM dates.

Table 5: Exposure period of international IBOR contract and equivalent RFR contracts

Futures contract	Exchange	Last trading day	**Exposure period**	Fallback provisions
BAX	Bourse de Montréal	3rd Monday of contract month	3rd Monday of contract month + 3 months (no lag period)	Conversion of outstanding positions (post June 2024) into 3M CORRA Futures

Futures contract	Exchange	Last trading day	**Exposure period**	Fallback provisions
Eurodollar	CME	3rd Monday of contract month	3rd Wednesday of contract month + 3 months (two day lag period)	Conversion of outstanding positions (post June 2023) into 3M SOFR Futures
(Former) 3M Sterling	ICE	3rd Wednesday of contract month	3rd Wednesday of contract month + 3 months (no day lag period)	Conversion of outstanding positions (post December 2022) into 3M SONIA Index Futures
(Former) 3M EuroSwiss	ICE	3rd Monday of contract month	3rd Wednesday of contract month + 3 months (two day lag period)	Conversion of outstanding positions (post December 2022) into 3M SARON Index Futures

The proposed change, in anticipation of the transition, is well accorded with the general conventions and guidelines set by other jurisdictions. Matching the start of the exposure period with that of the products into which they will be converted - that is, on the third Wednesday of the contract month - would align the BAX with its equivalent international products.

d. Analysis of Impacts

i. Impacts on Market

Raising the minimum price fluctuation range of the BAX back Whites, Reds and Greens will increase the profitability per trade for liquidity providers. The wider tick size would be considered more optimal as the benefits of increased liquidity and market maker support outweigh the cost of higher minimum bid-ask spreads. The Bourse expects a wider tick to increase dealer profitability and motivate more dealers to provide liquidity.

Feedback from market participants and volume trends suggest that the lower tick size is not favorable to optimal liquidity under existing market conditions. Considering market perception and to lessen the impact on market participants, the Bourse is planning to implement this change in different phases, starting initially with self-certification of the change for the BAX Reds and Greens contracts, followed by self-certification for the 3rd and 4th BAX Whites depending on market conditions and the results of the first phase.

The change in the last contract Trading Day for the BAX is set to increase the acceptance of the futures contract. The feedback that the Bourse has received from the industry is that a better alignment between the contracts' specifications and international standards will support market activity in both the BAX and CRA contracts. Note that there will be no impact on the Options on BAX (OBX, OBW, OBY, OBZ) resulting from this modification. The specifications of these products (including the last Trading Day) will not change.

ii. Impacts on Technology

As the proposed tick size is already supported by the Bourse, CDCC and technology providers for other Bourse products, the proposed changes should have no impact on the technological systems of the Bourse, of the Bourse's approved participants or of any other market participants.

iii. Impacts on regulatory functions

The proposed changes should have a minimal impact on the surveillance activities of the Regulatory Division of the Bourse. Procedures and parameters will be reviewed to align with changes to the contract specifications.

iv. Impacts on clearing functions

The proposed changes should have no impact on the clearing functions of CDCC, on CDCC's Rules and Operations Manual, nor on CDCC's Clearing Members, or other Industry participants dealing with CDCC.

v. Public Interest

The purpose of these amendments result from market participants' demand, including (1) the need to increase the minimum price fluctuation of the third, fourth (the back "Whites); the fifth, sixth, seventh and eighth (the "Reds"); the ninth, tenth, eleventh and twelfth quarterly BAX contract months (2) the change in contract expiry to eliminate any curve risk. As such, the Bourse considers these amendments to be in the public interest.

The Bourse is of the view that the present initiative will improve market efficiency as it will enhance the efficiency of the BAX contract by improving price precision, which will thereafter provide better liquidity and price transparency in the BAX market while allowing more participants to efficiently transact in such a market.

IV. PROCESS

The proposed amendments, including this analysis, must be approved by the Bourse's Rules and Policies Committee and submitted to the Autorité des marchés financiers, in accordance with the regulatory self-certification process, and to the Ontario Securities Commission for information purposes. Subject to public comments, the proposed amendments will take effect immediately thereafter.

V. ATTACHED DOCUMENTS

Proposed rule changes.

****** Appendix - Proposed Rules changes*****

Article 12.5 Minimum Price Fluctuation

Unless otherwise determined by the Bourse, the minimum price fluctuation is

- 0.005, representing $12.50 per contract, for the six (6) nearest contract months: the two (2) nearest non-quarterlies (serials) and the four (4) nearest quarterly ~~for all contract months~~
- 0.01 = C$25.00 per contract for all other contract months

Article 12.11 Last Trading Day

(a) For contract months expiring on or before June 28, 2024: Trading of Canadian Bankers' Acceptance Futures ceases at 10:15 a.m. (Montréal time) on the second London (Great Britain) banking day preceding the third Wednesday of the Settlement Month.

(b) For contract months expiring after June 28, 2024: Trading of Canadian Bankers' Acceptance Futures ceases at 10:15 a.m. (Montréal time) on the third Wednesday of the Settlement Month.