☒	Trading – Interest Rate Derivatives	☒	Back-office - Options
☒	Trading – Equity and Index Derivatives	☒	Technology
☒	Back-office – Futures	☒	Regulation

CIRCULAR 128-14
September 19, 2014

SELF-CERTIFICATION

MODIFICATIONS TO THE CONTRACT SPECIFICATIONS FOR THE THREE-MONTH CANADIAN BANKERS' ACCEPTANCE FUTURES CONTRACT

AMENDMENT TO ARTICLE 6807 OF RULE SIX OF BOURSE DE MONTRÉAL INC.

MINIMUM PRICE FLUCTUATION

Due to an administrative error identified in circular 119-14, circular 119-14 is hereby repealed and replaced by this circular.

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to the minimum price fluctuation (tick size) on the contract specifications for the Three-Month Canadian Bankers' Acceptance Futures (BAX), such that the minimum price fluctuation for the second, third and fourth quarterly BAX contract months be reduced from 0.01 per $100 nominal value (a full tick), to 0.005 per $100 nominal value (a half tick). These amendments have also been made to article 6807 of Rule Six of the Bourse.

The amendments to article 6807 and to the specifications of the BAX contract, as attached, took effect on **September 8, 2014**. Please note that article 6807 and the contract specifications are also available on the Bourse's Website (www.m-x.ca).

For additional information, please contact Ms. Joanne Elkaim, Director, Fixed Income Derivatives, Financial Markets by telephone at 514 871-7891 or by email at jelkaim@m-x.ca.

M[e] Pauline Ascoli
Vice-President, Legal Affairs, Derivatives

6807 Minimum Price Fluctuations
(24.01.86, 22.04.88, 08.09.89, 16.04.92, 19.01.95, 07.09.99, 31.01.01, 29.04.02, 14.06.02, 15.10.02, 03.05.04, 17.11.04, 01.12.06, 30.05.08, 15.05.09, 18.06.10, 16.02.12, 09.06.14, 08.09.14)

Unless otherwise determined by the Bourse, minimum price fluctuations shall be as follows:

a) 30-day overnight repo rate futures	0.005 per $100 nominal value
b) Overnight Index Swap futures	0.001 per $100 nominal value
c) 1-month ~~and 3-month~~ Canadian Bankers' acceptance futures	i) For the nearest contract month(s), as determined by the Bourse, 0.005 per $100 nominal value. ii) For all contract months excluding the nearest contract month(s) as determined by sub-paragraph i), 0.01 per $100 nominal value.
d) 3-month Canadian Bankers' acceptance futures	i) For the six (6) nearest contract months, as determined by the Bourse, including serials, 0.005 per $100 nominal value. ii) For all contract months excluding the nearest contract month as determined by sub-paragraph i), 0.01 per $100 nominal value.
e) Government of Canada Bond futures Contracts	a minimum of 0.005 per $100 nominal value
f~~e~~) Futures contract on the S&P/TSX 60 Index	0.01 index point
g~~f~~) Mini Futures contract on the S&P/TSX Composite Index	1 index point
h~~g~~) Canadian share futures contract	A minimum of $0.01 CDN per Canadian share
i~~h~~) International share futures contracts	At a minimum of the corresponding unit of fluctuation used by the market on which the underlying stock is traded
j~~i~~) Futures contracts on S&P/TSX sectorial indices	0.01 index point

k~~j~~) Futures contract on carbon dioxide equivalent (CO_2e) units with physical settlement	A minimum of $0.01 CDN per metric ton of carbon dioxide equivalent (CO_2e)
l~~k~~) Futures contract on carbon dioxide equivalent (CO_2e) units with cash settlement	A minimum of $0.01 CDN per metric ton of carbon dioxide equivalent (CO_2e)
m~~l~~) Futures contracts on Canadian Crude Oil	A minimum of $0.01 U.S. per barrel
n~~m~~) Futures contracts on the FTSE Emerging Markets Index	i) 0.05 index points for outright positions ii) 0.01 index point for calendar spreads and block trades

6807 Minimum Price Fluctuations

(24.01.86, 22.04.88, 08.09.89, 16.04.92, 19.01.95, 07.09.99, 31.01.01, 29.04.02, 14.06.02, 15.10.02, 03.05.04, 17.11.04, 01.12.06, 30.05.08, 15.05.09, 18.06.10, 16.02.12, 09.06.14, 08.09.14)

Unless otherwise determined by the Bourse, minimum price fluctuations shall be as follows:

a) 30-day overnight repo rate futures	0.005 per $100 nominal value
b) Overnight Index Swap futures	0.001 per $100 nominal value
c) 1-month Canadian Bankers' acceptance futures	i) For the nearest contract month(s), as determined by the Bourse, 0.005 per $100 nominal value. ii) For all contract months excluding the nearest contract month(s) as determined by sub-paragraph i), 0.01 per $100 nominal value.
d) 3-month Canadian Bankers' acceptance futures	i) For the six (6) nearest contract months, as determined by the Bourse, including serials, 0.005 per $100 nominal value. ii) For all contract months excluding the nearest contract month as determined by sub-paragraph i), 0.01 per $100 nominal value.
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TMX Montréal Exchange

THREE-MONTH CANADIAN BANKERS' ACCEPTANCE FUTURES

Specifications

Underlying	C$1,000,000 of Canadian bankers' acceptances with a three-month maturity.
Expiry cycle	Quarterlies: March, June, September and December. Serials: two (2) nearest non-quarterly months.
Price quotation	Index: 100 minus the yield in percentage point on an annual basis for a 365-day year on Canadian bankers' acceptances with a three-month maturity.
Minimum price fluctuation	0.005 = C$12.50 per contract for the six ~~three~~ (6~~3~~) nearest listed contract months, including serials. 0.01 = C$25 per contract for all other contract months.
Contract type	Cash-settled.
Last trading day	Trading ceases at 10:00 a.m. (Montréal time) on the second London (Great Britain) banking day preceding the third Wednesday of the contract month, provided it is a business day. If it is not a business day, trading will cease on the first preceding business day.
Expiration day	Expiration occurs on the last trading day.
Final settlement price	Based on the average bid-rate of Canadian bankers' acceptance with a three-month maturity, as quoted on CDOR on the last trading day at 10:15 a.m., excluding the highest and the lowest values.
Position reporting threshold	300 contracts.
Position limit	Information on position limits can be obtained from the Bourse as they are subject to periodic changes.
Price limit	None.
Minimum margin requirements	Information on minimum margin requirements can be obtained from the Bourse as they are subject to periodic changes.
Trading hours	Regular session: 6:00 a.m. to 4:00 p.m. Note: During early closing days, the regular session closes at 1:30 p.m.
Clearing corporation	The Canadian Derivatives Clearing Corporation (CDCC).
Ticker symbol	BAX

THREE-MONTH CANADIAN BANKERS' ACCEPTANCE FUTURES

Specifications

Underlying	C$1,000,000 of Canadian bankers' acceptances with a three-month maturity.
Expiry cycle	Quarterlies: March, June, September and December. Serials: two (2) nearest non-quarterly months.
Price quotation	Index: 100 minus the yield in percentage point on an annual basis for a 365-day year on Canadian bankers' acceptances with a three-month maturity.
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Clearing corporation	The Canadian Derivatives Clearing Corporation (CDCC).
Ticker symbol	BAX

Circulars 037-14 and 104-14: Summarised comments and responses

Note: Of the 33 comment letters received, 25 favoured the proposal… a support rate of more than 75%.

Item No.	Arguments for the proposal	Number of market participants
1	Will greatly benefit traders thanks to the ease of entry and exit.	7 participants
2	Will greatly reduce the implied cost of trading.	16 participants
3	Will reduce slippage.	3 participants
4	Will increase liquidity.	12 participants
5	Will increase volume. *The CGB offers the equivalent to a tenth of a basis point, 10 times tighter than the BAX. CGB volume is up 40%. CGB open interest is up 25%. The CGB regularly trades more, in duration terms, than the BAX.*	10 participants
6	Will encourage existing participants to increase activity.	8 participants
7	Will bring the BAX in line with competing OTC products.	5 participants
8	Will align the frequency of reversals in trade prices more closely with that of other international rates products.	4 participants
9	Will effect a necessary change that is long overdue.	5 participants
10	Will enhance transparency.	4 participants

11	Will encourage new market participants to start trading the BAX.	4 participants
12	Will align the BAX more closely with competing products in the US market.	3 participants
13	Will make the BAX a competitive product and return it to its rightful place as the mechanism for transferring short term interest rate risk in Canadian dollars.	3 participants
14	Will appeal to end-user participants, who will always choose the most cost effective hedge, which is currently OTC.	2 participants
15	Should implement on the BAX Reds as well.	3 participants
16	Will reap significant benefits for the Canadian derivatives markets as a whole.	2 participants
17	Will allow for more precise settlements.	1 participant
18	Will increase the number of market orders.	1 participant
19	Will bring more capital into the market.	1 participant
20	Will allow clients to actively trade strategies in international markets and in Canada at the same time.	1 participant
21	Will facilitate living up to a fiduciary responsibility to obtain the best price for customers.	1 participant
22	Will be massively beneficial to market participants such as them.	1 participant
23	Will add value for clients.	1 participant
24	Will put the bid ask more in line as a percentage of daily standard deviation.	1 participant

25	Firms have been forced to look for other sources of liquidity that are less expensive to use and the proposed changes will make the BAX a more attractive instrument.	1 participant
26	The bid-ask spread is substantially wider on the BAX than it is on other fixed income instruments at the Bourse, and the proposed changes will benefit the market by tightening that bid-ask spread.	1 participant
27	Will modernise the BAX by making it compatible with OTC products such as bonds and FRAs.	1 participant

Item No.	**Arguments against the proposal**	**Number of market participants**	**Response**
1	The Bourse's proposal is being considered due to the low volatility and interest rate environment.	6 participants	The low interest rate environment and low volatility is only one aspect of why the Bourse has decided to move forward with this initiative. Other key determining factors are, firstly, that major buy-side clients have expressed the need for this change, secondly, that the change will lead to increased cost-efficiency for participants as execution costs ("slippage") will decrease, thirdly, that the BAX will be in greater alignment with the OTC market which prices similar products in half-ticks, and fourthly, that the BAX contract will be better positioned to mitigate competitive forces in the STIR space and will more closely emulate international markets. The Bourse believes that even if volatility returns to "normal" levels, half-ticks will ultimately create a cheaper, more equitable and more efficient market.
2(a)	Will end up like the LIFFE, hurting the market and having to revert	5 participants	As to LIFFE and EUREX's decisions, they were based on exceptional circumstances.

	to full ticks.		
2(b)	Eurex also reversed a decision to change the Bobl to half ticks introduced in 2007 for similar reasons.	1 participant	LIFFE and EUREX reversed their implementation of the half-tick minimum price fluctuation in order to support their markets through arguably the worst financial crisis in the history of capital markets. Therefore, it is not considered a realistic comparison to the situation in which the Bourse finds itself. Furthermore, the full tick minimum price fluctuation on LIFFE's Short Sterling contract works out to £12.50, whereas that for the BAX works out to $25. A full tick minimum price fluctuation on the LIFFE's Short Sterling Futures contract actually equates more closely, to a half tick minimum price fluctuation on the BAX.
3	Will hurt the BAX market, which is now performing well, and result in a reduction in market depth and trading volume.	4 participants	It is indeed true that the BAX has a very deep and liquid market; the ratio of resting orders to executed volume is far lower for the BAX than for any of its counterparts. The Bourse believes that, while there may be a drop in trading volumes over the short term, the increase in end-user participation in the BAX market will increase trading volumes over the mid to long-term. Furthermore, while, from a short-term perspective, market depth may decrease somewhat with the change in minimum price fluctuation, the excess of resting orders to executed trading volume will lessen the impact. Recent business development initiatives and marketing strategies have contributed in large part to the awareness and the growth of the BAX market. Still, the ratio of BAX market participation between end users and liquidity providers has become an increasing source for concern. While overall trading volumes have grown steadily for a number of years, that growth has been disproportionately biased towards those who provide liquidity, rather than to the buy side. To be healthy over the long-term, the BAX market needs to have a sustainable balance of participation between end-user participants and liquidity providers.

			While the BAX has enjoyed great success over the past years, there is significant opportunity for further growth, which can be achieved by ensuring the contract is more closely attuned to the needs of major buy-side participants. The Bourse has lost some trading volume to various competitive forces. Many hedge funds use alternatives to the BAX and this poses a major risk to the BAX market over the long term. The over-the-counter market does offer a half-tick price fluctuation, which appeals greatly to the buy-side participants who have told the Bourse time and time again that the BAX needs a half-tick minimum price fluctuation on at least the front four quarterly contracts for them to trade it. The Bourse is fully committed to this change and does not anticipate reversing its decision. The Bourse is confident that the lower minimum price fluctuation will attract hedge funds of their prolonged and consistent demands for a reduction in the minimum price fluctuation, because of the additional granularity being provided, and because of the increased capital efficiency and the reduced cost of trading. It should be noted, all the same, that the Bourse will always act in the best interests of its markets and will monitor the BAX very closely once the modifications have gone into effect to monitor exactly how the market is evolving and if that evolution is moving in the right direction.
4(a)	Will reduce profit per trade for independent traders.	4 participants	While the lower minimum price fluctuation may reduce the profit per transaction for liquidity providers, that reduction in profit per trade will be offset by the additional inflow of buy-side activity that those same liquidity providers can trade against.
4(b)	The reduction in profit per trade will force them to trade twice as much.	1 participant	

			It is only to be expected that there will be a transition period from when half-ticks are introduced on the second, third and fourth quarterly BAX contracts to when buy-side activity increases sufficiently to return the BAX liquidity providers overall profits to current levels. In order to ease the transition for the liquidity providers, the Bourse is pleased inform you that an incentive program has been approved by the TMX Executive Committee and Board of Directors, to compensate liquidity providers for any potential reduced profit per trade until such time as there is sufficient buy-side activity to do so organically. Rather than half-ticks doubling the resting orders between any two given prices, the Bourse is of the opinion that, by offering more price points, the reduced minimum price fluctuation will add greater efficiency to the order matching process, fostering additional trading activity and thereby facilitating a reduction in the rate of resting orders to executed orders.
4(c)	This will make it harder to attract new liquidity providers. As a result, liquidity will be reduced.	2 participants	
5	The equivalent contract in Australia currently trades at a full tick and fluctuates with the level of interest rates. The Bourse should consider doing the same.	2 participants	There are simply fundamental differences between the Australian and Canadian economies that can not be put aside, namely, that Australia enjoys the highest volatility of all of its peers. That is far from the situation in which Canada has found itself for some time now. While the ASX has an interesting strategy, that of varying the minimum price fluctuation with the level of interest rates, regretfully the implementation of such a protocol would be problematic as the process of defining the parameters by which the rate must move for the minimum price fluctuation to change touches on too broad a spectrum of variables.
6	Will hurt the Montreal-(or Province of Quebec) based	3 participants	The liquidity providers in Montreal have been a great support for the BAX contract for many years; however the ratio of BAX

	trading community.		market participation between end-users and liquidity providers has become an increasing source for concern. While overall trading volumes have grown steadily for a number of years, that growth has been disproportionately biased towards those who provide liquidity, rather than to the buy side participants. To be healthy over the long-term, the BAX market needs to have a sustainable balance of participation between end-user participants and liquidity providers.
7(a)	Will facilitate a transfer of wealth from independent liquidity providers to large institutions and hedge funds.	2 participants	The Bourse is confident that this decision is in the best interests of all participants in the BAX market and that any negative impacts felt by BAX liquidity providers over the short-term will be compensated for by the additional buy-side activity that will support those liquidity providers over the long-term, and softened by the incentive program that the Bourse will be offering.
7(b)	This transfer of wealth will also increase the proportion of risk born by the independent traders.	1 participant	
8	Will not result in any increase in end-use participation as those asking for this change are the same that said they would trade the CGZ, the CGF, the ONX and the OIS. *ONX and OIS were mentioned by one participant, whereas CGF, CGZ and OIS were mentioned by the second participant.	2 participants	In fact, participation in the CGZ and CGF contracts has grown steadily. The CGF contract in particular achieved three trading records in 2013 alone, one for open interest of 9,305 contracts on April 25th, one for trading volume of 42,606 contracts for the month of May, and one for trading volume of 276,610 contracts for the year. As for the ONX and OIS contracts, it was made clear that the contracts were not expected to trade right away, but that they were being put in place for when the timing is right.
9	Will attract HFTs to the BAX market which may result in aberrancies and flash crashes, risking having an empty book in times of crisis and a game rigged	3 participants	There is very little to no HFT activity in the BAX market, and the Bourse does not expect the move to a half tick minimum price fluctuation in the second, third and fourth quarterly contracts to attract significant HFT trading activity. The current BAX market is not conducive for high-frequency traders. They seek highly

	market with instances of front running.		volatile markets with a high proportion of client business and only start participating if the market becomes very volatile and there is a sharp increase in client activity. The minimum price fluctuation is irrelevant to the high-frequency traders. In any case, the Bourse will closely monitor the BAX market to measure to level of HFT activity, and if necessary, will implement measures to limit the appeal of the BAX market to HFTs. The Bourse can do so by limiting the interest of high-frequency traders in the BAX market by raising their fees, by limiting the number of messages they can send per second, or by excluding them from the LPRP program or even by requiring a certain percentage of liquidity making to liquidity taking for participants to maintain their eligibility for the LPRP program.
10	Will reduce trading activity just like with the front contract, which went half-ticks in 2002 and trades the least.	1 participant	There is even more justification for the reduction in minimum price fluctuation for the second through fourth quarterly BAX contracts in 2014 than there was in 2002. Firstly, the prolonged low volatility environment with no indications of movement for the foreseeable future at the time of the drafting of this Detailed Analysis. Secondly, the increasingly insistent demands that the Bourse is fielding from buy-side clients. Thirdly, the exceptionally high ratio of resting orders to executed trades on the BAX. Finally, the first quarterly contract has always been the least traded because it is the least volatile of all of the quarterly BAX contracts and buy side participants tend to gravitate to more volatile contracts, traditionally the second and third quarterly contracts, but now more so the third and fourth quarterly contracts.
11	Will increase risk to the short-term interest rate system in an exponential way.	1 participant	The Bourse does not believe that the move to half ticks on the second, third and fourth quarterly contracts will increase risk to the short term interest rate system in an exponential way, for

			several reasons. The full tick price movement is too expensive for contract entry and exit given normal market volatility, existing execution protocols, and exchange fees. This discourages new participants from entering and existing participants from remaining in the BAX market. Major market participants will always choose to execute investment and hedging strategies in the most cost effective manner while utilizing the same interest rate risk exposures. At this moment that alternative would be over the counter products (bonds, FRAs) which provide users the same interest rate risk exposures at a lower cost. In our Detailed Analysis, we note that, with a half-tick minimum price fluctuation on the BAX Whites, the implicit cost of trading will be reduced and that trading activity will be enhanced. We strongly believe more activity will migrate to BAX if the investing and hedging cost decreases. This measure would allow the cost structure of the BAX to fall into line with the OTC market and thereby eliminate one of the major negatives to BAX and help offset the negative implications of existing execution protocols. Further, migration to lowering the tick increment does come with the advantage of “fairer” and more accurate pricing, transparency, liquidity and price discovery which are the features and benefits of what should be available on an exchange.