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**MARKET NOTICE**Johannesburg  
Stock ExchangeTel: +27 11 520 7000  
[www.jse.co.za](http://www.jse.co.za)

**Number:** 131/2017  
**Relates to:**  Equity Market  
 Equity Derivatives  
 Commodity Derivatives  
 Interest Rate and Currency Derivatives  
**Date:** 31 March 2017

**SUBJECT:** JSE DELIVERABLE WHEAT DERIVATIVE CONTRACT – DEC17 AND MAR18 EXPIRIES TO BE INTRODUCED ON MONDAY

**Name and Surname:** Chris Sturgess  
**Designation:** Director: Commodities & Key Client Management

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Dear Stakeholder,

Further to our recent market notice 110/2017 and the proposals the JSE have published over the past 3 months, we sincerely appreciate the collaborative intentions displayed by so many participants during our many conversations, however from the written feedback received it is evident market wide consensus will not be achieved and so to progress with specific regard to the JSE derivatives contracts, the JSE has made the final decision.

The JSE has carefully considered all the arguments going back to the consultation process that started in January this year, and has made a final decision which in our view will serve the best interests of the derivative contract we have listed.

The following will be applied to the WEAT contract for the marketing season 1 October 2017 through till 30 September 2018, participants are reminded the below is ONLY APPLICABLE to the JSE listed contract and will only be applied to physical deliveries in completion of a JSE contract.

1. The JSE **will introduce the Guaranteed Grade (GG)** wheat facility whereby storage operators, at their discretion, issue JSE silo receipts for specific grade wheat that they will honour for a period of 3 months for trading purposes and then a further 1 month to outload. Please take careful note that this enhancement to the JSE deliverable contract does not in any way deviate from the Government published wheat grades of B1, B2 or B3, but rather provide participants the assurance that when out loading the wheat, Storage Operators will not move one grade up or down, but rather supply the wheat grade as reflected on the JSE silo receipt. This enhancement will become applicable as from 1 May 2017 via the ESC system whereby the GGB1, GGB2 and GGB3 silo receipts may be issued. The JSE will then reassess the uptake of this functionality before the start of the 2018/19 marketing season before committing to continue with this functionality.

2. The JSE has decided to **remove the R100 origin discount** applicable to certain origins when delivery is made in completion of a futures contract. The JSE will not be adding additional origins as acceptable for delivery for the next season, and so to confirm the origins are: South Africa, Argentina, USA Hard Red Spring (DNS & NSW), USA Hard Red Winter, Russia, Ukraine, no 3 or better Canadian Red Western Spring wheat, Australian Hard wheat, Australian Prime Hard, Australian Prime White, Australian Standard White wheat and German Type A or B.

In reaching this decision, we considered the evidence that South Africa was already consuming large tonnages from these origins there was no need to differentiate on origin. We appreciate certain clients expressed concern around the extensive delivery of foreign product on JSE contracts could lead to an imbalance around the supply situation in the country, we of the opinion that delivery of foreign product on the JSE already has a number of additional cost components like additional handling fees, and with the increased paperwork requirements for delivery of imported wheat on JSE contracts, we will continue to only receive physical deliveries to ensure the necessary price convergence of the futures contract with the realistic dynamics of the spot market.

We again reiterate the JSE WEAT contract is a futures contract that will reflect pricing from ANY of the deliverable wheat origins approved for delivery and so clients should not view this as only reflective of South African origin wheat.

3. The JSE has decided to **continue to trade B1 wheat as the reference grade** and will continue to accept B2 and B3 wheat for delivery in completion of a futures contract, **however we will change the methodology** applied to determine the grade discounts for contracts deliverable on the JSE.

During this consultation process we have received information from participants highlighting that our current grade discounts may not be the most reflective of international reality. It must be stated categorically that for the derivatives contract to work, and in line with other global exchanges, the JSE does require a published grade discount that will be applied to all physical deliveries in completion of a futures contract. Since the main hedging reference grade is B1, we believe clients using the JSE to manage their price risk may continue to do so without the grade discounts finalized at the listing date of the new season expiries.

**The JSE aims to publish the final grade discounts only closer to the new marketing season however would like to motivate we change our current methodology to determine grade discounts as follows.**

In doing research how other wheat derivative exchanges manage delivery of different proteins, we established that Hard Red Winter (HRW) Wheat traded on Kansas under CME Group, have a 10cent/bushel discount per 0.5 % change in protein. Since this same underlying HRW wheat also forms the basis for the current wheat import tariff calculations, and is also an indicator for global wheat prices, we believe adopting the same discount except applying this to a 1% protein move, in other words instead of 10 US cents rather use 20 US cents/bushel discount for every 1% change in protein, is reflective of an international benchmark. Considering that we want to use the HRW wheat discount as applied by CME Group as the initial base for grade discounts going forward, we will convert the 20 US cents/bushel to tons using the conversion factor of 36.7440 therefore resulting in a grade discount of US\$ 7.3488 per ton. The JSE will then consider the average exchange rate for the past 7 weeks leading up to 15 September each year (as published by SAGIS for the wheat import tariff calculations - [http://www.sagis.org.za/koringtarief\(2017-03-31\).pdf](http://www.sagis.org.za/koringtarief(2017-03-31).pdf) ) in order to determine the average Dollar Rand exchange rate. The JSE has heard the request from participants to make the process as transparent and clear as possible. In this way clients should be able to get a sense of the grade discounts leading up to 15 September each year.

**The JSE therefore proposes for the marketing season 1 October 2017-30 September 2018 to apply a grade discount per 1% protein change of \$7.3488 per ton multiplied by the local exchange rate as determine and finalized by the latest 15 September 2017. The final discount will be rounded to the closest R1/ton value.**

It is difficult to predict where exchange rates would be in August and September this year, but assuming rate of 13.40 for this example, the grade discount for 2017/18 would be as follows:  $B2\ 7.3488 \times 13.40 = R99$  and for  $B3 = 99 \times 2 = R198$ .

The JSE, considering this new methodology, will publish the grade discounts for B2 and B3 wheat each year and it is expected to vary depending on the exchange rate. The JSE is considering for future years to incorporate protein values as published by the US Wheat Associates ([www.uswheat.org](http://www.uswheat.org)) but this will first require discussion with this entity and the Agricultural Advisory Committee.

Please consider this new methodology to determine grade discounts for JSE wheat contracts delivered in completion of a futures contract, if there are any improvements you would like to suggest please send this to [commodities@jse.co.za](mailto:commodities@jse.co.za) no later than 28 April 2017, the JSE will publish the final grade discount methodology shortly thereafter.

The JSE will therefore go ahead and introduce both the **Dec17 and Mar18 WEAT expiries for trading on Monday 3 April 2017.**

We appreciate and respect there will be a number of clients who would have preferred a different outcome. The JSE has considered all the facts as represented and decided the above will be in the best interest of the currently listed derivatives contract. It is unfortunate that the industry could not reach consensus on the items raised, that said we do trust the WEAT contract remains an effective contract for price risk management and that price convergence with the spot market is achieved through the necessary physical deliveries.

Please appreciate the above is only applicable to JSE derivatives contract and to JSE deliveries made in completion of a futures contract.

You are welcome to contact me directly or the rest of the Commodities Team if there are any specific questions or concerns you would like to discuss.

Should you have any queries regarding this notice, please contact [commodities@jse.co.za](mailto:commodities@jse.co.za).

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