

## Cash-Settled Forward (CSFs)

CSFs provide FX market participants with a clearable alternative to the predominant deliverable products in the G20 and several other pairs. These products serve as a viable alternative for strategies not requiring actual exchange of the physical currency (i.e. a client executing an advanced hedge of an anticipated securities purchase in Germany, will likely want to take delivery of the Euros to complete its purchase on value date).

The primary difference between a deliverable contract and a cash settled contract (same currency pair, same value date) is that the deliverable provides a continuous exposure while the cash-settled contract stops the FX exposure at the fixing.

Example: buy €100 mio Euro at 1.4000 for value 11/16/11.

- If deliverable contract, on 11/14/11 the contract becomes Spot and goes into delivery if not rolled. The 100 mio Euro is deposited in the customer's European bank account, and thus the long exposure to EUR continues until physically offset.
- If CSF, on 11/14/11 the contract is cash-settled against the London 4pm WMR Fixing. Let's assume the WMR Fix = 1.4200. This creates a net USD cash flow of +\$2,000,000, to be paid on 11/16/11, with no residual FX exposure.

From an economic perspective, the products are essentially equivalent until the Fixing of the CSF. A liquidity provider can use a deliverable contract to offset a CSF but only until the Fixing. At the Fixing time, the market maker needs to unwind the deliverable "hedge" at a rate equal or as close to the Fixing as possible. It is important that the risk systems used by participants properly identifies the terminating nature of the CSFs as opposed to regular deliverable FX in order to prevent large positional errors at maturity.

Example: buying €100 mio EUR/USD at 1.4000 for value 11/16/11 and selling a CSF in the same notional, at the same rate, for the same value, is essentially a fully hedged position until 11/14/11 4pm London. Assuming same Fixing as above, the resulting position post the Fixing time would be a combination of a negative (\$2,000,000) cash flow and a long €100 mio EUR/USD position, obviously far from a hedged combination.

The CSF is an instrument that can be used effectively by participants who utilize strategies that do not require the actual exchange of the physical currencies. In fact, using such instruments could significantly reduce settlement exposures, or expenses related to PvP systems designed to mitigate settlement exposures. Clearly, a client entering into an FX forward to hedge an anticipated purchase of a foreign security would likely need the physical currency to effectuate the eventual purchase. For such hedging requirements, a CSFs would only be appropriate if combined with the execution of a deliverable spot trade on the final date (i.e. two days before the foreign currency needs to hit the client's account). If used in this manner, the CSF would effectively hedge the exchange risk for the life of the contract with a compensation achieved through a single currency cash flow, and the spot trade is used to insure the exchange of notional at that day's appropriate rate. This strategy would effectively provide exposure protection while retaining the flexibility to decide whether physical delivery is truly needed (i.e. some other foreign currency cash flow could occur to negate the need to take delivery on this contract).

### Appendix 4

#### Chapter 300

#### CME WM/Reuters OTC Spot, Forward and Swap Contracts

##### 300.1. SCOPE OF CHAPTER

This chapter is limited in application to CME WM/Reuters OTC Spot, Forward, and Swap Contracts ("CME WMR Contracts"), based on specified currency pairs, cash-settled by reference to WM/Reuters



Closing Spot Rates (“WMR Rates”)<sup>1</sup>. Parties to transactions in CME WMR Contracts shall be limited to “eligible contract participants” as defined in Section 1a(12) of the Commodity Exchange Act.

Transactions in CME WMR Contracts shall also be subject to the general rules of the Exchange insofar as applicable. The clearing and settlement of transactions in CME WMR Contracts shall also be subject to the provisions of Chapter 8-F of the CME Rulebook (Over-the-Counter Derivative Clearing).

## **300.2. CONTRACT SPECIFICATIONS**

### **300.2.A. Contract Summary**

CME WMR Contracts shall be based upon specified currency pairings as cataloged in the Appendix to this Chapter.

The Unit of Trading and Clearing shall be specified in terms of the “clearing-unit currency.” CME WMR Contracts shall be based on a Unit of Clearing to a Precision as specified in the Appendix to this Chapter. The minimum price fluctuation shall be specified in terms of the “minimum-fluctuation currency.” CME WMR contracts shall be quoted in minimum price fluctuations as specified in the Appendix to this Chapter.

For purposes of Position Accountability and the application of Position Limits, per Rule 300.01.E, each CME WMR Contract shall be deemed to be the notional value contract equivalent as specified in the Appendix to this Chapter. The levels of Position Accountability and Position Limits, as applicable, are further specified in the Appendix to this Chapter.

### **300.2.B. Hours of Trading and Clearing Entry**

The Exchange shall determine the hours during which CME WMR Contracts may be traded and submitted to the Clearing House.

### **300.2.C. Valid Value Dates for Cash Settlement**

CME WMR Contracts shall be cash settled for any valid value date mutually agreed to by buyer and seller, and accepted by the Exchange for the applicable currency pair as a valid value date(s) for cash settlement and clearing. In general, for any currency pair, a valid value date shall be any business day that is a banking business day in the countries of issue for both currencies.

### **300.2.D. Delivery Price and Delivery Value**

Delivery for CME WMR Contracts assigned pursuant to Chapter 300 shall be by cash settlement according to Rule 300.02.

### **300.2.E. Position Limits and Position Accountability**

1. Authority - Position Limits and Position Accountability may be applicable, as defined by Rule 560, and as per the following.
2. Aggregation - For purposes of this Rule, where applicable:
  - futures,
  - options on futures,
  - E-mini futures,
  - E-micro futures,

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<sup>1</sup> The WM/Reuters Closing Spot Rates are provided by The World Markets Company PLC (WM) in conjunction with Reuters and are used for certain currencies (the “Rates”) displayed herein. WM and Reuters shall not be liable for any errors in or delays in providing or making available the WM/Reuters Closing Spot Rates, nor for any actions taken in reliance on the same. The Rates can not be used, reproduced, distributed, redistributed, licensed or disclosed in any way without a written agreement with WM.

- spot, forward and swaps (combinations of spot and forwards or two maturity forwards), including but not limited to CME WMR Contracts,
  - options on spot and forwards, including but not limited to CME WMR Contracts; and
  - in addition, where applicable, the analogous reciprocal versions of the aforementioned contracts for the respective foreign exchange pairs, shall be aggregated with all products utilizing that foreign exchange (FX) pair regardless of quoting conventions. The baseline for this aggregation shall be the denomination of the underlying full-size CME futures contract. Contract equivalents shall be determined through the conversion of the notional value (or contract size times the number of contracts in standardized products) to the CME base currency using the prior day's Regular Trading Hours (RTH) settlement, and dividing the result by the contract size or notional of the full-size CME futures contract.
3. Contract Equivalent - For purposes of this Rule, each CME WMR Contract shall be deemed to be the notional value contract equivalent as specified in the Appendix to this Chapter.
  4. Position Accountability - A participant owning or controlling more than the aggregated equivalent of the number of contracts specified in the Appendix to this Chapter, net long or net short, shall provide, in a timely fashion, upon request by the Exchange, information regarding the nature of the position, trading strategy, and hedging information if applicable.
  5. Spot Position Limit – A participant shall not own or control more than the equivalent of the number of contracts specified in the Appendix to this Chapter which are settled in the spot period between the second and third Wednesdays (inclusive) during the months of March, June, September and December.
  6. Single Expiration Position Limit – A participant shall not own or control more than the equivalent of the number of contracts specified in the Appendix to this Chapter that expire on the same date.
  7. Aggregate Position Limit– A participant shall not own or control more than the equivalent of the number of contracts specified in the Appendix to this Chapter, net long or net short, in all expiration dates combined.
  8. Exemptions - The foregoing position limits shall not apply to bona fide hedge positions meeting the requirements of Regulation 1.3(z)(1) of the CFTC and the rules of the Exchange, and shall not apply to other positions exempted pursuant to [Rule 559](#).

### **300.2.F. Last Day of Trading**

The last day on which a transaction in a CME WMR Contract may be traded, in respect of a specified cash settlement date, shall be one (1) valid business day prior to the cash settlement date.

### **300.2.G. Liquidation and Delivery Standards**

1. At Maturity. After clearing of CME WMR Contracts in respect of a specified cash settlement date has ceased, in accordance with Rule 300.01.G. of this chapter, outstanding contracts for such cash settlement date shall be liquidated by cash settlement through procedures as prescribed in Rule 300.02 and in a manner prescribed by the Clearing House.
2. Prior to Maturity. Standard offsets of futures and options on futures shall not apply to positions in CME WMR Contracts. Prior to the Cash Settlement Date, positions may be closed out upon the request of the clearing firm to the Clearing House, and in the manner prescribed by the Clearing House.

### **300.2.H. Contract Modifications**

Specifications shall be fixed as of the first day of trading of a contract, except that all deliveries must conform to government regulations in force at the time of delivery. If any national or international government agency or body issues an order, ruling, directive or law that conflicts with the requirements of these rules, such order, ruling, directive or law shall be construed to take precedence and become part of these rules and all open and new contracts shall be subject to such government orders.

### 300.3. CASH SETTLEMENT

#### 300.3.A. Day of Cash Settlement

Each CME WMR Contract, for a valid value date for cash settlement in one business day, shall be liquidated by cash settlement at a price equal to the daily Final Settlement Price for that day. The daily Final Settlement Price shall be equal to the WM/Reuters Closing Spot Rate for that day for the specific currency pair in question, rounded to the nearest integral multiple of the minimum price increment as identified per the Appendix to this Chapter.

All open positions for that valid value date for cash settlement will be cash settled in the minimum fluctuation currency based upon the difference between the Final Settlement Price for the valid value date for cash settlement and the original trade price as submitted for clearing, times the notional value of the transaction in the clearing unit currency.

#### 300.3.B. Procedures if No Cash Settlement Price is Available

In the event that the Final Settlement Price for a valid value date for cash settlement cannot be published on a given day by WM/Reuters, and in order to minimize basis risk, the Final Settlement Price shall be determined as the next available WM/Reuters Closing Spot Rate for the specific currency pair in question.

#### 300.3.C. Amendments to Timings

The Exchange may amend the timings of notifications, deliveries, and transfers under this Rule 300.02 to reflect as appropriate the adoption of daylight savings time in the relevant countries of delivery.

### 300.4. DISPUTES

All disputes between interested parties may be settled by arbitration as provided in the Rules.

(End Chapter 300)

#### Appendix to Chapter 300: Contract Specifications

Currency Pairing	Unit of Trading and Clearing	Precision	Minimum Price Fluctuation	Contract Equivalent	Position Accountability	Spot Month Position Limit	Single Month Position Limit	All Months Combined Position Limit
GBP/USD	1 GBP	0.01 GBP	0.000001 USD/GBP	62,500 GBP	10,000	Na	Na	Na
USD/CAD	1 USD	0.01 USD	0.000001 CAD/USD	100,000 USD	6,000	Na	Na	Na
USD/JPY	1 USD	0.01 USD	0.0001 JPY/USD	100,000 USD	10,000	Na	Na	Na
USD/CHF	1 USD	0.01 USD	0.000001 CHF/USD	100,000 USD	10,000	Na	Na	Na
AUD/USD	1 AUD	0.01 AUD	0.000001 USD/AUD	100,000 AUD	6,000	Na	Na	Na
USD/MXN	1 USD	0.01 USD	0.000001 MXN/USD	100,000 USD	6,000	20,000	Na	Na
NZD/USD	1 NZD	0.01 NZD	0.000001 USD/NZD	100,000 NZD	6,000	Na	Na	Na
USD/ZAR	1 USD	0.01 USD	0.000001 ZAR/USD	100,000 USD	6,000	5,000	Na	Na
EUR/USD	1 EUR	0.01 EUR	0.000001 USD/EUR	125,000 EUR	10,000	Na	Na	Na
USD/NOK	1 USD	0.01 USD	0.000001 NOK/USD	100,000 USD	6,000	Na	Na	Na
USD/SEK	1 USD	0.01 USD	0.000001	100,000	6,000	Na	Na	Na

			SEK/USD	USD				
USD/CZK	1 USD	0.01 USD	0.00001 CZK/USD	100,000 USD	6,000	2,000	Na	Na
USD/HUF	1 USD	0.01 USD	0.0001 HUF/USD	100,000 USD	6,000	2,000	Na	Na
USD/PLN	1 USD	0.01 USD	0.000001 PLN/USD	100,000 USD	6,000	2,000	Na	Na
USD/ILS	1 USD	0.01 USD	0.000001 ILS/USD	100,000 USD	6,000	2,000	Na	Na
USD/TRY	1 USD	0.01 USD	0.000001 TRY/USD	100,000 USD	6,000	2,000	Na	Na
USD/DKK	1 USD	0.01 USD	0.000001 DKK/USD	100,000 USD	6,000	Na	Na	Na
EUR/GBP	1 EUR	0.01 EUR	0.0000001 GBP/EUR	125,000 EUR	6,000	Na	Na	Na
EUR/JPY	1 EUR	0.01 EUR	0.0001 JPY/EUR	125,000 EUR	6,000	Na	Na	Na
EUR/CHF	1 EUR	0.01 EUR	0.0000001 CHF/EUR	125,000 EUR	6,000	Na	Na	Na
AUD/JPY	1 AUD	0.01 AUD	0.000001 JPY/AUD	100,000 AUD	6,000	Na	Na	Na
CAD/JPY	1 CAD	0.01 CAD	0.00001 JPY/CAD	100,000 CAD	6,000	Na	Na	Na
EUR/AUD	1 EUR	0.01 EUR	0.000001 AUD/EUR	125,000 EUR	6,000	Na	Na	Na
USD/HKD	1 USD	0.01 USD	0.000001 HKD/USD	100,000 USD	6,000	Na	Na	Na
USD/SGD	1 USD	0.01 USD	0.000001 SGD/USD	100,000 USD	6,000	5,000	Na	Na
USD/THB	1 USD	0.01 USD	0.0001 THB/USD	100,000 USD	6,000	2,000	Na	Na