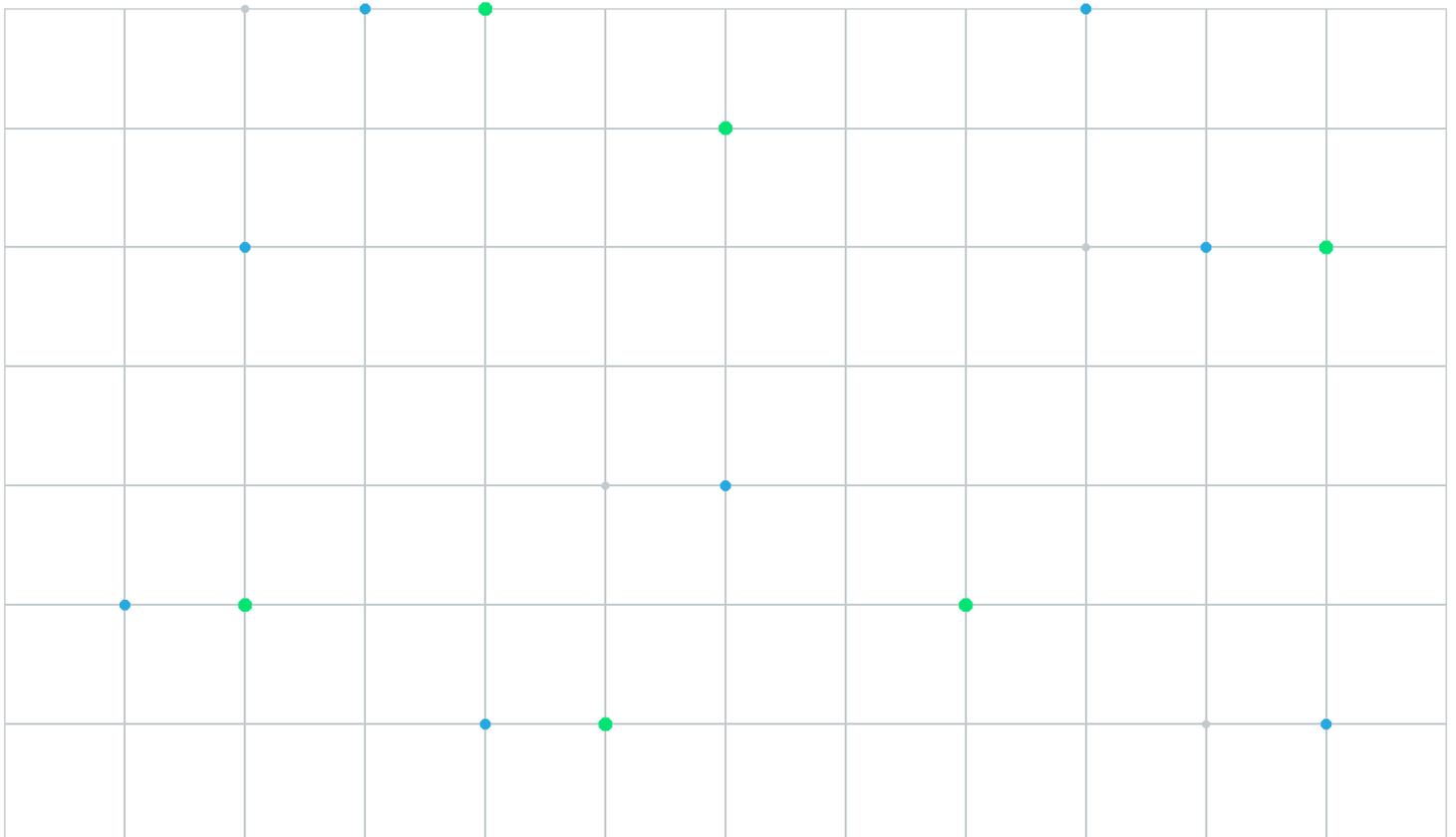


# Block Trading in CME FX Futures

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This white paper provides a detailed overview of block trading in CME foreign exchange (FX) futures contracts:

- (1) It reviews basic requirements, standards, and rules of the road for participating in block trades on the CME Group exchanges.
- (2) It summarizes the regulatory foundations on which block trading plays an essential role in an otherwise centralized and competitive futures market.
- (3) It surveys the characteristics of block trading in CME FX futures and what those characteristics tell us about when and why users of FX futures employ block trades.

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## Basics

On any US-regulated futures market, including any of the CME Group exchanges,<sup>1</sup> a block trade is a privately negotiated transaction that:

- (a) is executed in accordance with exchange rules certified with and accepted by the Commodity Futures Trading Commission ("CFTC") and
- (b) equals or exceeds an exchange-prescribed minimum size, permitting it to be executed apart from the centralized, competitive contract market.

## Who, what, when

Not everyone can participate in block transactions. Each party to a block trade must be an Eligible Contract Participant, as defined in Section 1a(18) of the US Commodity Exchange Act.<sup>2</sup>

Not all products listed on the CME Group exchanges are permissible for block trading. Products, product spreads, and product combinations<sup>3</sup> eligible for block transactions, and the corresponding minimum size requirements, are determined solely by the exchange. Minimum size requirements in effect at any given time are published at: <http://www.cmegroup.com/clearing/trading-practices/block-trades.html#generalInfo>.

A block trade may be executed in an eligible product at any hour of the day, irrespective of whether the centralized, competitive market in that product is open or closed. A block trade may not, however, be executed in a futures contract or option contract after the contract has expired.

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<sup>1</sup> CME Group owns and operates four designated contract markets: Chicago Mercantile Exchange Inc. ("CME"), the Board of Trade of the City of Chicago, Inc. ("CBOT"), the New York Mercantile Exchange, Inc. ("NYMEX"), and the Commodity Exchange, Inc. ("COMEX") (collectively, the "CME Group exchanges" or "the exchange").

Rules for block trading on the CME Group exchanges are codified in Rule 526 ("Block Trades") in Chapter 5 of the CME Rulebook, the CBOT Rulebook, and the NYMEX Rulebook. The magisterial interpretative reference is the CME Group Market Regulation Advisory Notice ("MRAN") entitled Block Trades, available at: <http://www.cmegroup.com/rulebook/files/cme-group-Rule-526.pdf>.

<sup>2</sup> 7 USC 1a(18).

<sup>3</sup> Here and in what follows, we refer to "products, product spreads, and product combinations" as "products."

## Price standards

Any outright purchase or sale of a contract made via a block trade must be executed at a single price. Similarly, for a block trade in any eligible spread or combination, each leg of the spread or combination must be executed at a single price. In all instances, the block trade price must be consistent with the permitted minimum price increment for the contract, spread, or combination.

Crucially, for any block trade involving a given futures or option contract, the price must be fair and reasonable in light of (i) the transaction's size, (ii) prices and sizes of other transactions in the same contract at the relevant time, (iii) prices and sizes of transactions in other relevant markets at the relevant time, including, without limitation, the cash market corresponding to the contract or related contract markets, and (iv) market conditions and the circumstances of the parties to the block trade at the relevant time.

## Entering the trade

Upon agreeing to the terms of a block transaction, the parties must report it to the exchange via CME Direct or CME ClearPort<sup>4</sup>. In any block-eligible CME FX futures or options product, a block trade must be submitted to the exchange within 15 minutes of trade execution during all trading hours including Regular Trading Hours (RTH), European Trading Hours (ETH) or Asian Trading Hours (ATH).<sup>5</sup>

Provided that (a) both parties to the block trade pass the required credit checks and (b) the relevant terms of both sides of the transaction – purchase and sale – have been confirmed to match, the block trade is accepted for clearing and is routed automatically to CME Clearing, and a price report of the trade is published to the marketplace by the exchange.

Frequently, a block trade involves, on one side, a dealer who quotes bids and offers for block transactions and, on the other side, a customer of the dealer. Although the exchange does not post dealers' indicative quotes for block trades, it does publish contact information for market makers who actively provide liquidity for both block trades and exchange-for-related-position ("EFRP") transactions in CME FX products.<sup>6</sup>

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4 For information on how to register for access to CME Direct, visit: <http://www.cmegroup.com/trading/cme-direct/registration.html#newFirmUserRegistration>. For general information about CME Direct, please visit: <http://www.cmegroup.com/trading/cme-direct.html>. Information on registering for access to CME ClearPort is available at: <http://www.cmegroup.com/clearport/registration.html>. For general information about CME ClearPort, please visit: <http://www.cmegroup.com/clearport.html>.

5 For CME FX products, the following definitions apply:  
RTH: 7 a.m. – 4 p.m. Chicago time ("CT"), Monday through Friday on regular business days.  
ATH: 4 p.m. – 12 a.m. CT, Monday through Friday on regular business days and at any time on weekends.  
ETH: 12 a.m. – 7 a.m. CT, Monday through Friday on regular business days.

6 Market-making firms who have agreed to accept customer enquiries in respect of either block trades or EFRP trades in CME FX futures are listed at: <http://www.cmegroup.com/trading/fx/fx-futures-blocks-and-efps-market-makers.html>. To register to receive market-maker contact information, please visit: <https://go.cmegroup.com/market-maker-contact-info>.

## What do block trades do?

The signal feature of any futures contract is the centralized, competitive, all-to-all market in which it trades and in which price discovery occurs. US law requires any organized futures exchange to "provide a competitive, open, and efficient market and mechanism for executing transactions that protects the price discovery process of trading in the centralized market."<sup>7</sup> The corresponding regulatory requirement is that "all purchases and sales of any commodity for future delivery, and of any commodity option, on or subject to the rules of a contract market shall be executed openly and competitively" through the market's central limit order book.<sup>8</sup>

Exceptions are permitted for trades to be executed privately and non-competitively, provided that such trades are:

- (a) authorized by exchange rules that have been submitted to and approved by the CFTC, and
- (b) "made in accordance with written rules of the contract market," and
- (c) made for "bona fide business purposes."

Block trading counts among these exceptions, as an accommodation to the business purposes of market participants for whom private negotiation of transactions may be occasionally necessary, or at least strongly preferred, as an alternative to centralized and competitive trade execution.<sup>9</sup> Historically, a block transaction meets these needs in two ways:

### Trade facilitation –

In a futures market that is historically illiquid, or for a transaction that takes place at an hour of day when an otherwise liquid futures market is relatively inactive, the buyer and seller of the futures contract might resort to a block trade to ensure they can execute the trade at all.

### Price uniformity –

The buyer and seller of the futures contract may use a block trade to ensure they can execute a large transaction at a single price.

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7 See US Commodity Exchange Act Core Principle 9 for Designated Contract Markets (17 USC 38.500):

*The board of trade shall provide a competitive, open, and efficient market and mechanism for executing transactions that protects the price discovery process of trading in the centralized market of the board of trade. The rules of the board of trade may authorize, for bona fide business purposes:*

- (a) *Transfer trades or office trades;*
- (b) *An exchange of:*
  - (1) *Futures in connection with a cash commodity transaction;*
  - (2) *Futures for cash commodities; or*
  - (3) *Futures for swaps; or*
- (c) *A futures commission merchant, acting as principal or agent, to enter into or confirm the execution of a contract for the purchase or sale of a commodity for future delivery if the contract is reported, recorded, or cleared in accordance with the rules of the contract market or a derivatives clearing organization.*

8 See 17 CFR 1.38 ("Execution of transactions").

9 It was not always thus. Only in the 1990s did US-regulated futures markets gradually recognize privately negotiated block transactions as allowable trade practice.

*US-regulated securities exchanges, by contrast, made allowance for blocks in their trading rules several decades earlier. For example, on the New York Stock Exchange ("NYSE") bilaterally negotiated block transactions were permissible by at least the early 1960s. In terms of share of NYSE trading volume, blocks represented around 10 percent in the late 1960s. By the late 1990s, they routinely accounted for more than 50 percent.*

## Block trading in CME FX products

Exhibit 1 indicates minimum allowable block trade sizes for each of these FX products as of January 2021.

### Exhibit 1 – Minimum Block Trade Sizes for March Quarterly (“Quarterly”) Delivery Months and Non-March-Quarterly (“Monthly”) Delivery Months in Various CME FX Futures, February 2021

| FX PAIR | MINIMUM BLOCK TRADE SIZE (CONTRACTS) |         | MINIMUM BLOCK TRADE SIZE (BASE CURRENCY AMOUNT, MLNS) |            | BLOCK MINIMUM PRICE INCREMENT* |
|---------|--------------------------------------|---------|---|------------|--------------------------------|
|         | QUARTERLY                            | MONTHLY | QUARTERLY   | MONTHLY    |                                |
| EUR/USD | 150                                  | 20      | EUR 18.75   | EUR 2.50   | \$0.00001 per EUR              |
| JPY/USD | 150                                  | 20      | JPY 1,875.00  | JPY 250.00 | \$0.0000001 per JPY            |
| GBP/USD | 100                                  | 20      | GBP 6.25  | GBP 1.25   | \$0.00001 per GBP              |
| AUD/USD | 100                                  | 20      | AUD 10.00   | AUD 2.00   | \$0.00001 per AUD              |
| CAD/USD | 100                                  | 20      | CAD 10.00   | CAD 2.00   | \$0.00001 per CAD              |
| MXN/USD | 100                                  |         | MXN 50  |            | \$0.00001 per MXN              |
| BRL/USD | 50                                   |         | BRL 5   |            | \$0.00005 per BRL              |
| RUB/USD | 50                                   |         | RUB 125   |            | \$0.00005 per RUB              |
| ZAR/USD | 50                                   |         | ZAR 25  |            | \$0.000025 per ZAR             |

\*Effective February 22, 2021  
Source: CME Group.

Against this backdrop, consider a bank treasury FX dealer and a bank customer wanting to sell FX futures. If the intended sale is large enough to qualify, the dealer and the customer could agree to a bilaterally negotiated block trade. Or they could go their separate ways, respectively, buying and selling futures in the centralized and competitive market on the CME Globex electronic trading platform (“CME Globex”). Why would they opt to use a block trade? They might opt to use a block trade, because they have similar characteristics to OTC market trades which can be done on a disclosed basis with a chosen provider at a single price. Trade facilitation and price uniformity discussed below are two other reasons they might opt to use a block trade.

## Trade facilitation

If the bank dealer and the customer are contemplating their transaction at an hour of day when futures liquidity is relatively sparse in the centralized, competitive CME Globex market, then the primary concern for both may be that a privately negotiated block is the only practical way to do the trade.

To the extent that this consideration is significant for market participants, it suggests that, all other things being equal, the observed share of product trading volume attributable to blocks should be larger during times of day when trade flows are thinner and, conversely, smaller during intervals when traffic is heavier. However, the relative incidence of block transactions throughout the typical CME Globex trading day varies from product to product.

### **Price uniformity**

Alternatively, the priority for the bank dealer and the bank customer might be to execute the FX futures transaction at a single price. A block trade would ensure this outcome, whereas buying or selling a futures position through the centralized, competitive CME Globex market provides no such guarantee. Indeed, a single price is an unlikely outcome in a competitive market purchase or sale, unless the intended trade size is less than the resting volume quoted at, respectively, the best offered price or the best bid price in the central limit order book.

Block trading offers buyers and sellers the convenience of privately negotiating a trade with a selected eligible counterparty, the ability to execute a large transaction at a fair and reasonable single price, and the security of a trade cleared by CME Clearing. They are designed to meet institutional trading needs. CME expects the majority of FX trading to be conducted in the centralized and competitive market on CME Globex, but block trades are a useful and convenient outlet for some traders who find this a convenient and expeditious way of conducting business.



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Neither futures trading nor swaps trading are suitable for all investors, and each involves the risk of loss. Swaps trading should only be undertaken by investors who are Eligible Contract Participants (ECPs) within the meaning of Section 1a(18) of the Commodity Exchange Act. Futures and swaps each are leveraged investments and, because only a percentage of a contract's value is required to trade, it is possible to lose more than the amount of money deposited for either a futures or swaps position. Therefore, traders should only use funds that they can afford to lose without affecting their lifestyles and only a portion of those funds should be devoted to any one trade because traders cannot expect to profit on every trade. All references to options refer to options on futures.

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PM21FX005/0421