

Changes to ASX Clear (Futures) Initial Margin Parameters for ASX 24 Energy Derivative Products - Information Sheet

| 19 December 2017 | Version 2

Introduction

ASX Clear (Futures) issued a market notice on the 30th October 2017, advising that ASX Clear (Futures) is increasing initial margin parameters for ASX 24 energy derivative products to a 3 day margin period of risk. The previous market notice is available for download [here](#).

On the 19th December, ASX Clear (Futures) issued a market notice advising of the new initial margin parameters for ASX 24 energy derivatives to be effective as at close of business Friday, 12th January 2018 for initial margins called on Monday, 15th January, 2018.

1. Why are we making margin changes?

Margin is an important risk management tool to protect market stability and the interests of all users in the event of a default by a Participant.

ASX Clear (Futures) has recently reviewed its approach to setting initial margin parameters for ASX 24 energy derivative products. ASX's review identified that these products are characterised by relatively low average daily trading volumes versus overall open interest, and large price movements. This has heightened exposure to risk.

To ensure that margin requirements for ASX 24 energy derivative products continue to provide the right level of risk management protections, ASX is making a change to the margin period of risk and methodology used to determine initial margin parameters.

2. What is changing?

The margin period of risk used to determine initial margins will be increased from the greater of 1 or 2 days, to the greater of 1,2 or 3 days.

In addition, ASX will change the margin methodology calculation to use a time series of observed price returns instead of an assumed normal distribution of returns.

This change allows for a better reflection of extreme price movements¹ in initial margin levels. The result of the change is an increase in initial margins levels across the expiry curve. This impact is most apparent for the near quarter Base Quarterly Futures and Cap products.

ASX is making these changes to ensure that initial margin levels adequately protect ASX Clear (Futures) and the energy derivative market in the event of a participant default.

Example: Comparison of Price Return Assumptions - Base New South Wales, Front Quarter Futures

Chart 1 below shows the frequency distribution of price returns for the front Base New South Wales Futures contract, across the period December-16 to Demember-17.

¹ For example, across the margin review period extreme moves of 34.2% (3rd Feb-17) and 44.5% (6th Feb-17) were observed for the front Base New South Wales Futures contract.

Black and Red vertical lines denote the level of coverage provided by initial margin² settings for the contract, under normally distributed and actual return assumptions respectively.

The chart highlights that, initial margins, set under a normally distributed approach, will not accurately reflect extreme price moves observed for the contract.

In the example below, we see that initial margins set under a normally distributed approach will understate the level of price risk associated with the contract.

Chart 1: Base New South Wales, Front Quarter Futures – Distribution of Price Returns (Dec16- Dec17)

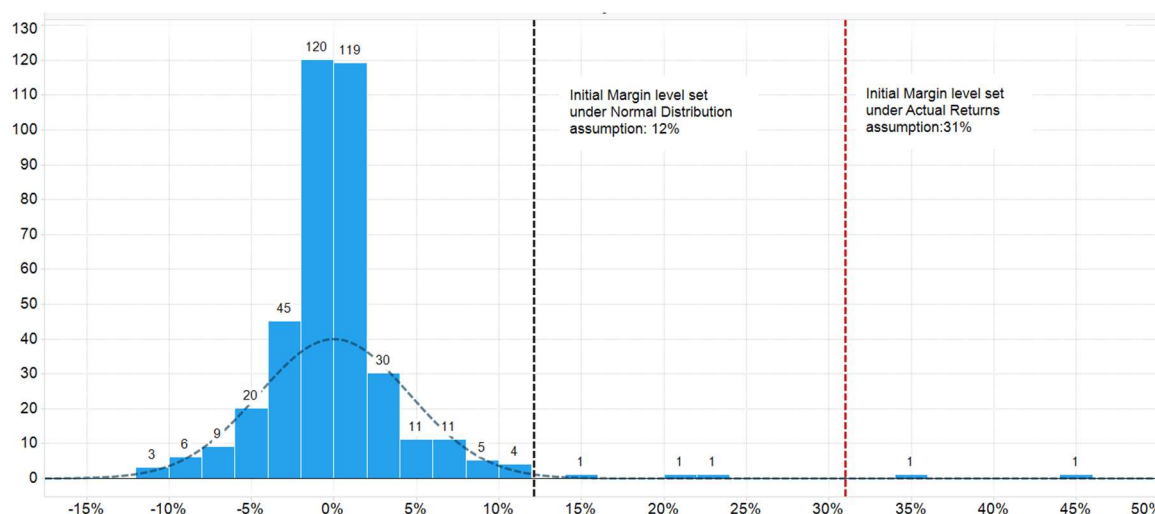


Table 1: Base New South Wales, Front Quarter Futures – Extreme Price Returns (Dec16- Dec17)

Name	Contract	Date	Price Return (%)
Base New South Wales Front Quarter Futures	BNH2017F	2017-02-06	44.50%
Base New South Wales Front Quarter Futures	BNH2017F	2017-02-03	34.20%

3. When are the changes effective from?

ASX is mindful of the impact that the margin change may have on Participants, and has sought to be as least disruptive as possible by providing advance notice of the changes while putting in place a risk framework that reflects the current state of market liquidity. The new margin parameters based on a 3 day margin period of risk are available [here](#).

The revised initial margin parameters will be effective for open ASX 24 energy derivative contracts as at close of business on Friday, 12th January 2018 for initial margins called on Monday, 15th January 2018.

4. How will Participants be impacted?

The margin changes are directly applicable to Clearing Participants of ASX Clear (Futures) and will apply to any open position in ASX 24 energy derivative products. The impact of the changes will vary depending on the portfolio of contract positions in the Clearing Participant Accounts.

ASX24 Trading Participants trading in ASX 24 energy derivative products that are not self-clearers should contact their Clearing Participant to discuss the changes.

² Initial margin levels in Chart 1 are calibrated under a 99.5% Confidence Interval.

5. How will end users (“Clients”) be impacted?

The impact to end users (“Clients”) will vary depending on their margining arrangements with their Clearing Participant.

It’s recommended that Clients contact their Clearing Participant to discuss impacts to their portfolio.

6. Where can I go for further information?

ASX Clear (Futures) issued a market notice on the 19th December 2017, advising of new initial margin parameters for ASX 24 energy derivative products.

All ASX 24 energy derivative product margin parameters are available on the ASX website at:

http://www.asx.com.au/data/clearing/ASX_Energy_Margin_Parameters.pdf