Circular no.: MCX/TRD/184/2018 May 11, 2018

Commencement of Copper Options Contract with Copper (1 MT) Futures as underlying

In terms of the provisions of the Rules, Bye-Laws and Business Rules of the Exchange, and in continuation to circular no. MCX/TRD/176/2018 dated May 7, 2018, the Members of the Exchange are notified as under:

Exchange shall be launching Copper Options contract with Copper (1 MT) futures as underlying. Accordingly Copper Option contracts of 27 June 2018, 29 August 2018 and 28 November 2018 respectively will be available for trading with effect from Monday May 21, 2018. The Life Cycle of the Copper Option contracts is specified hereunder:

Particulars	**Dates**	**Dates**	**Dates**
Contract	Copper Option 27 June 2018	Copper Option 29 August 2018	Copper Option 28 November 2018
Underlying Futures Contract	Copper 29 June 2018	Copper 31 August 2018	Copper 30 November 2018
Contract Start Date	**May 21, 2018**	**May 21, 2018**	**May 21, 2018**
Option Contract Expiry Date	**June 27, 2018**	**August 29, 2018**	**November 28, 2018**
Sensitivity Report shall be provided on	June 21,June 22,June 25 & June 26, 2018 at End of Day	August 23, August 24, August 27 & August 28, 2018 at End of Day	November 22, November 23, November 26 & November 27, 2018 at End of Day.
Option Devolvement Intimation shall be provided from	June 25, 2018 to June 27, 2018	August 27, 2018 to August 29, 2018	November 26, 2018 to November 28, 2018
Option Devolvement Margin First Day	June 26, 2018 (from Begin of Day)	August 28, 2018 (from Begin of Day)	November 27 2018 (from Begin of Day)
Option Devolvement Margin Second Day	June 27, 2018 (from Begin of Day)	August 29, 2018 (from Begin of Day)	November 28, 2018 (from Begin of Day)
First day of Trading after Option Positions Devolving into Futures Positions	June 28, 2018	August 30, 2018	November 29, 2018

The contract specification as approved by SEBI is provided in Annexure 1. A detailed note on product design is attached as Annexure 2.

Annexure 1 and Annexure 2 shall be binding on all the Members of the Exchange and constituents trading through them.

Members are requested to take note of the same.

Sanjiv Kapur
Asst. Vice President

Encl.: As above

Kindly contact Mr. Sameer Kenia on 022- 6649 4040 or send an email at customersupport@mcxindia.com for further clarification.

Annexure 1

Contract Specification for Copper Options with Copper (1 MT) Futures as underlying

Symbol	COPPER
Underlying	Underlying shall be Copper Futures contract traded on MCX
Description	Option on Copper Futures
Option Type	European Call & Put Options
Contract Listing	Contracts will be available as per the Contract Launch Calendar
Contract Start Day	1st day of contract launch month. If 1st day is a holiday then the following business day.
Expiry Day (Last Trading Day)	Two business days prior to the Expiry day of the underlying futures contract
Trading	
Trading Period	Mondays through Fridays
Trading Session	Monday to Friday: 10.00 a.m. to 11.30 / 11.55 p.m.* * based on US daylight saving time period
Trading Unit	One MCX Copper futures contract
Underlying Quotation/ Base Value	Rs. Per Kg
Underlying Price Quote	Ex – Bhiwandi (exclusive of all taxes and levies relating to GST, import duty/customs and local taxes if any etc.).
Strikes	7 In-the-money, 7 Out-of-the-money and 1 Near-the-money. (15 CE and 15 PE). The Exchange, at its discretion, may introduce additional strikes, if required.
Strike Price Intervals	Rs. 5.00
Base price	Base price shall be theoretical price on Black 76 option pricing model on the first day of the contract. On all other days, it shall be previous day's Daily Settlement Price of the contract.
Tick Size (Minimum Price Movement)	Rs. 0.01
Daily Price Limit	The upper and lower price band shall be determined based on statistical method using Black76 option pricing model and relaxed considering the movement in the underlying futures contract. In the event of freezing of price ranges even without a corresponding price relaxation in underlying futures, if deemed necessary, considering the volatility and other factors in the option contract, the Daily Price Limit shall be relaxed by the Exchange.
Margins	The Initial Margin shall be computed using SPAN (Standard Portfolio Analysis of Risk) software, which is a portfolio based margining system. To begin with, the various risk parameters shall be as under: A. Price Scan Range – 3.5 Standard Deviation (3.5 sigma) B. Volatility Scan Range –5 % C. Short Option Minimum Margin – Minimum of 2.5% subject to Margin Period of Risk (MPOR) (i.e. 2.5% *$\sqrt{2}$ currently) D. Extreme Loss Margin – 1% (to be levied only on short option positions) E. Premium of buyer shall be blocked upfront on real time basis The Margin Period of Risk (MPOR) shall be at least two days. Parameters would be reviewed and changed, if required
Premium	Premium of buyer shall be blocked upfront on real time basis.

Margining at client Level	Initial Margins shall be computed at the level of portfolio of individual clients comprising of the positions in futures and options contracts on each commodity
Real time computation	The margins shall be recomputed using SPAN at Begin of Day, 10.30 am, 12.30 pm, 1.30pm, 3.00pm, 5.00pm, 7.00pm, 8.30pm, 10.30pm and End of Day.
Mark to Market	The option positions shall be marked to market by deducting / adding the current market value of options positions (positive for long options and negative for short options) times the number of long / short options in the portfolio from / to the margin requirement. Mark to Market gains and losses would not be settled in Cash for Options Positions.
Risks pertaining to option that devolve into futures on expiry	a) In the initial phase, a sensitivity report shall be provided to members of the impending increase in margins at least 2 days in advance. The mechanism shall be reviewed and if deemed necessary, pre-expiry option margins shall be levied on the buy / sell / both positions during last few days before the expiry of option contract. b) The penalty for short collection / non collection due to increase in initial margins resulting from devolvement of options into futures shall not be levied for the first day.
Additional and/ or Special Margin	At the discretion of the Exchange when deemed necessary
Position Limits	
Maximum Allowable Open Position	Position limits for options would be separate from the position limits applicable on futures contracts. For client level: 14,000 MT or 5% of the market wide open position, whichever is higher - For all Copper Options contracts combined together. For a member level: 1,40,000 MT or 20% of the market wide open position, whichever is higher - For all Copper Options contracts combined together. Upon expiry of the options contract, after devolvement of options position into corresponding futures positions, open positions may exceed their permissible position limits applicable for future contracts. Such excess positions shall have to be reduced to the permissible position limits of futures contracts within two trading days.
Settlement	
Settlement of premium/Final Settlement	T+1 day
Mode of settlement	On expiry of options contract, the open position shall devolve into underlying futures position as follows:- • long call position shall devolve into long position in the underlying futures contract • long put position shall devolve into short position in the underlying futures contract • short call position shall devolve into short position in the underlying futures contract • short put position shall devolve into long position in the underlying futures contract

	All such devolved futures positions shall be opened at the strike price of the exercised options
Exercise Mechanism at expiry	All option contracts belonging to ‘Close to the money’ (CTM)* option series shall be exercised only on ‘explicit instruction’ for exercise by the long position holders of such contracts. All In the money (ITM) option contracts, except those belonging to ‘CTM’ option series, shall be exercised automatically, unless ‘contrary instruction’ has been given by long position holders of such contracts for not doing so. The ITM option contract holders and the CTM option series holders who have exercised their options by giving explicit instruction, shall receive the difference between the Settlement Price and Strike Price in Cash as per the settlement schedule. In the event contrary instruction are given by ITM option position holders (other than those belonging to CTM option series), the positions shall expire worthless. All CTM positions which are not exercised shall also expire worthless. All Out of the money (OTM) option contracts, except those belonging to ‘CTM’ option series, shall expire worthless. In the event the OTM position holders, which are in CTM option series, exercise their option positions, shall be required to pay and settle the difference between strike price and settlement price as per the settlement schedule. All devolved futures positions shall be considered to be opened at the strike price of the exercised options. * Option series having strike price closest to the Daily Settlement Price (DSP) of Futures shall be termed as At the Money (ATM) option series. This ATM option series along with two option series each having strike prices immediately above and below ATM shall be referred as ‘Close to the money’ (CTM) option series. In case the DSP is exactly midway between two strike prices, then immediate two option series having strike prices just above DSP and immediate two option series having strike prices just below DSP shall be referred as ‘Close to the money’ (CTM) option series.
Due Date Rate (Final Settlement Price)	Daily settlement price of underlying futures contract on the expiry day of options contract.

Contract Launch Calendar for Copper Options contracts expiring during the year 2018

Options Contract Launch Months	Options Contract Expiry Months	Corresponding Futures Contract Expiry Months
On approval from SEBI	June 2018	June 2018
March 2018	August 2018	August 2018
May 2018	November 2018	November 2018

Contract Launch Calendar for Copper Options contracts expiring during the year 2019

Options Contract Launch Months	Options Contract Expiry Months	Corresponding Futures Contract Expiry Months
July	February	February
September	April	April
December	June	June
March	August	August
May	November	November

Annexure 2

Option Contract on Commodity Futures Contract – Product Design

1. **Option on Commodity Futures**:

   Option on Commodity Futures contract shall have the corresponding Commodity Futures contract as the underlying.

2. **Strikes:**

   Each Option expiry shall have minimum fifteen strikes available; viz. seven each for In the Money (ITM), seven Out of the Money (OTM) and one At the Money (ATM).

3. **Trading Parameters and Attributes:**

   The following trading parameters and order attributes are specified for Options trading:

   a. **Order type/Order book/Order attribute**

      - Regular lot order
      - Stop loss order
      - Immediate or cancel
      - Day
      - End of session
      - Good till cancelled
      - Good till date
      - Spread IOC & 2L/3L Order

   b. **Permitted lot size**

      The permitted lot size for the commodity derivatives options contracts shall be as per the respective contract specification.

   c. **Tick size for contracts**

      The tick size in respect of commodity derivatives options contracts shall be as per the respective contract specification.

   d. **Maximum Single Order Size**

      The maximum single order size shall be 70 lots

   e. **Turnover Limits**

      By default, the Buy and Sell Turnover Limits for Options shall be set as unlimited by the Exchange. However, the Members can reset these values as per their risk management requirement.

f. Base Price & operating ranges applicable to the contracts

Base price of the Options Contracts shall be theoretical price on Black76 option pricing model on the first day of the contract. On all other days, it shall be previous day's daily settlement price of the contract.

The minimum/ maximum operating price range for options contract will be statistical daily price range computed based on Black76 option pricing model.

The formula for calculation of theoretical base price and statistical operating range as per Black76 model formula is as follows:

The options price for a Call shall be computed as per the following formula:

C = Max [e ^ -rt {(F*N(d1) - K*N(d2)},Tick size]

and the price for a Put is:

P = Max [e ^ -rt {(K*N(-d2) - F*N(-d1)},Tick size]

and

d1 = [Log Normal {U/L Price (F) / Strike (K) } + {Volatility (V)^2/2 } * Time To Expiry (T)] / [Volatility (V) * sqrt {Time to Expiry }]

d2 = d1- Volatility * sqrt (Time to Expiry)

where:

F = Underlying Price

K = Strike Price

V = Volatility

T = Time to expiry (Days to Expiry / No. of days in Year)

R = Interest rate

4. Devolvement Style:

European Style options, which can be devolved only on the day of Expiry.

5. Devolvement Mechanism:

On expiry, following mechanism shall be adopted for devolvement of the options contracts:

a. Option series having strike price closest to the Daily Settlement Price (DSP) of Futures shall be termed as At the Money (ATM) option series.

This ATM option series and two option series having strike prices immediately above this ATM strike and two option series having strike prices immediately below this ATM strike shall be referred as 'Close to the money' (CTM) option series.

In case the DSP is exactly midway between two strike prices, then immediate two option series having strike prices just above DSP and immediate two option series having strike prices just below DSP shall be referred as 'Close to the money' (CTM) option series.

b. All option contracts belonging to 'CTM' option series shall be devolved only on 'explicit instruction' for devolvement by the long position holders of such contracts failing which they will expire worthless.

c. All In the money (ITM) option contracts, except those belonging to 'CTM' option series, shall be devolved automatically, unless 'contrary instruction' has been given by long position holders of such contracts for not doing so.

d. All Out of the money (OTM) option contracts, except those belonging to 'CTM' option series and devolved by the long position holders, shall expire worthless.

e. All devolved contracts within an option series shall be assigned to short positions in that series on a random basis.

f. On the option contract devolving in the underlying futures contract, the trading and settlement regulations of the underlying futures contract shall apply.

Examples are given below for identification of ITM, CTM, ATM and OTM strikes as per the underlying settlement price:

Strike Interval	5
U/L Settlement Price	452

Strike Interval	5
U/L Settlement Price	452.5

Strike Interval	5
U/L Settlement Price	453

For Call	
Strike Available	**Strike Type**
435	ITM
440	CTM
445	CTM
450	ATM
455	CTM
460	CTM
465	OTM
470	OTM

For Call	
Strike Available	**Strike Type**
435	ITM
440	ITM
445	CTM
450	CTM
455	CTM
460	CTM
465	OTM
470	OTM

For Call	
Strike Available	**Strike Type**
440	ITM
445	CTM
450	CTM
455	ATM
460	CTM
465	CTM
470	OTM
475	OTM

For Put	
Strike Available	**Strike Type**
435	OTM
440	CTM
445	CTM
450	ATM
455	CTM
460	CTM
465	ITM
470	ITM

For Put	
Strike Available	**Strike Type**
435	OTM
440	OTM
445	CTM
450	CTM
455	CTM
460	CTM
465	ITM
470	ITM

For Put	
Strike Available	**Strike Type**
440	OTM
445	CTM
450	CTM
455	ATM
460	CTM
465	CTM
470	ITM
475	ITM

Strike	Devolvement Procedure	Effect
ITM (Other than CTM)	Positions shall devolve automatically	• Difference between settlement price and strike price shall be cash settled • Positions would get devolved into Futures contract
	ITM long position holder can give contrary instruction	• Expire worthless i.e. There will be no cash settlement • No positions will get devolved into Futures contract
CTM – ITM / CTM – OTM	No position shall devolve automatically. An ‘explicit instruction’ shall be placed for exercise of Options.	If the option holder gives the ‘explicit instruction’ Then • Difference between settlement price and strike price shall be cash settled. In case of CTM- OTM position member have to pay the Difference between settlement price and strike price to the Exchange • Positions would get devolved into Futures contract Else • Expire worthless i.e. There will be no cash settlement • No positions will get devolved into Futures contract
OTM (Other than CTM)	Positions shall not devolve into Futures	All position will expire worthless i.e. There will be no cash settlement

Submission of request for Devolvement of Positions –

The Members shall submit request for devolvement of positions request through manual entry or Bulk File Upload feature provided under MAT/ TWS→ Ex/Dex/DI menu. Members may place multiple requests for devolvement of positions. The Exchange shall consider only the latest request placed by the member.

Members are requested to refer

1. Circular no. MCX/C&S/139/2018 dated 6th April 2018 - regarding timing for submission of request.

2. Circular no. MCX/TECH/092/2018 dated 15th March 2018 – relevant file format under sr.no. 5.61 to 5.63 for submission of request.

6. **Settlement Method**:

Daily Settlement:

The Options Premium settlement will be done on T+1 day basis.

Final Settlement:

On exercise, Options positions shall devolve into underlying Futures position as follows:-

- Long Call position shall devolve into long position in the underlying Futures contract
- Long Put position shall devolve into short position in the underlying Futures contract
- Short Call position shall devolve into short position in the underlying Futures contract
- Short Put position shall devolve into long position in the underlying Futures contract

On Expiry of options contract, all such devolved Futures positions shall be opened at the strike price of the exercised Options.

Cash settlement for difference between settlement price and strike price will be done on option devolvement day (contract expiry) + 1 day basis.

Sensitization Report / Devolvement Margin:

Sensitivity report shall be provided to members for sensitizing the impending increase in margins at least 2 days prior to the Options Expiry. Further, the Exchange shall levy devolvement margin beginning from at least one day prior to options expiry date. The Exchange shall review the mechanism and if deemed necessary shall increase/ decrease the number of days for which sensitivity report is being provided and the number of days for which devolvement margin is being levied. The exchange reserves the right to increase/ decrease the quantum of devolvement margin.

A. **Sensitivity Report**

- Sensitivity Report to be provided to the members would be an *End of Day* report.
- The report would be made available to members four days prior to the devolvement date of the options contract.
- The Report would be based on "*What if Scenario*", wherein all In the Money (ITM), including CTM option contracts (which are ITM) in the near month option contract, would be identified based on the respective day's settlement price, and converted into futures positions.
- The "what-if scenario" margins shall be calculated at client portfolio level, and grossed up at member level.
- The "what-if scenario" margins shall be computed using SPAN software.
- Spread charge, as currently applicable would be considered for expected margin computation i.e. benefit on spread positons shall be considered.

- If the member has given “Contrary Instruction” the same will not be considered for computation of expected margin in Sensitivity Report.
- A file shall be provided to members giving the information on existing margins, ‘what if’ scenario margins and incremental margins requirement.
- Profit element on expected Devolved Call and Put option positions shall be considered and will be reduced in the calculation of margin requirement. If the profit element exceeds the additional margin requirement due to devolvement of positions into futures, then the margin requirement shall be considered as zero for the purposes of Sensitivity Report.

B. Devolvement Margin

- Based on the outcome of the Sensitivity Report, the Exchange shall levy Devolvement margin.
- As stated, Devolvement Margin shall be computed at the end of the day, starting from the end of the second day prior to option devolvement date. Of the total Devolvement Margins arrived at based on the methodology specified for computation of margins in Sensitivity Report, Exchange shall levy one-fourth of the total Devolvement Margin computed on the day prior to the Option Devolvement Date. The said margin shall be made applicable for the entire next day (i.e. from the beginning of the day till the end of the day).
- At the end of the day on the day prior to option Devolvement Date, Devolvement Margin shall be re-computed considering the revised and updated Sensitivity Report and the Settlement price. On this day, one-half of the computed Devolvement Margin shall be made applicable on the next day.
- Devolvement Margin shall be in addition to all other applicable margins. In case of a situation where there is a margin reduction due to devolved position, no benefit would be passed on.
- In case of multiple contracts having different expiry dates but a common devolvement margin period, an average rate of the applicable margins numbers shall be applied, subject to a maximum margin rate of 50%.
- Exchange shall not consider devolvement margins for the purpose of client margin reporting.

7. **Position Limits:**

Position limits of options would be separate from position limits of futures contracts and numerical value for client level/member level limits shall be twice of corresponding numbers applicable for futures contracts.

Upon expiry of the options contract, after devolvement of options position into corresponding futures positions, open positions may exceed their permissible position limits applicable for future contracts. Such excess positions shall have to be reduced to the permissible position limits of futures contracts within two trading days.

The excess position limits would be permitted for only those clients, who had exceeded position limits at the time of devolvement.

8. Margins:

Risk management shall be managed with Standard Portfolio Analysis of Risk (SPAN*). The initial margin shall be imposed at the level of portfolio of individual client comprising of his positions in futures and options contracts on each commodity. Margins shall be adequate to cover 99% VaR (Value at Risk) and Margin Period of Risk (MPOR) shall be two days.

For buyer of the option, buy premium shall be charged as margins and blocked from the collaterals. On completion of settlement, the premium blocked shall be released.

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Calendar Spread Charge:

The margin on calendar spread shall be calculated on the basis of delta of the portfolio consisting of futures and options contracts in each month. The Calendar Spread charge shall be 25% on both the legs of the position.

Net Option Value

Net Option Value is computed as the difference between the long option positions and the short option positions, valued at the last available closing price and shall be updated intraday at the current market value of the relevant option contracts at the time of generation of risk parameters. Thus, mark to market gains and losses shall not be settled in cash for options positions.