3 May 2023
ESMA70-155-13072

OPINION on position limits on MILLING WHEAT No. 2 contracts

I. Introduction and legal basis

1. On 28 March 2023, the European Securities and Markets Authority ("ESMA") considered that sufficient information was received to assess a notification received from the Autorité des Marches Financiers (AMF) under Article 57(5) of Directive 2014/65/EU on markets in financial instruments[1] ("MiFID II").

2. The notification relates to the exact position limits the AMF intends to set for the Euronext Milling wheat futures and options commodity contracts in accordance with the methodology for calculation established in Commission Delegated Regulation (EU) 2022/1310[2] ("RTS 21a") and taking into account the factors referred to in Article 57(3) of MiFID II.

3. ESMA's competence to deliver an opinion on the position limits that competent authorities intend to set is based on Article 57(5) of MiFID II.

4. On 10 August 2017, ESMA already issued an Opinion regarding the exact position limits that the AMF intended to set for the Euronext Milling wheat futures and options commodity contracts. For the spot month, the position limits considered by the AMF in June 2017 was 60,000 at the start of the sport month and 20,000 lots over the last twelve trading sessions before expiry of the contract. For the other months', the position limits considered were 60,000 lots at the start of the other months' period and 100,000 lots during the last 21 days before the spot month expiry. In the opinion, ESMA concluded that the position limits considered by the AMF complied with the methodology established in Commission Delegated Regulation (EU) No 2017/591[3] (RTS 21) and were consistent with the objectives of Article 57 of MiFID II.

5. The AMF reviewed these limits in light of the change in methodology for calculating position limits following the entry into force of RTS 21a. As a consequence, in this opinion, ESMA is assessing whether the new position limits the AMF intends to set for the Euronext Milling wheat contracts comply with the methodology established in RTS 21a and are consistent with the objectives of Article 57 of MiFID II. ESMA understands that the new position limits

[1] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).
[2] Commission Delegated Regulation (EU) 2022/1302 of 20 April 2022 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits to commodity derivatives and procedures for applying for exemption from position limits (OJ L 197, 26.07.2022, p.52)
[3] Commission Delegated Regulation (EU) 2017/591 of 1.12.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits commodity derivatives (OJ L 87, 31.3.2017, p. 479).

will apply one month after the publication of this opinion and replace the previous position limits as determined by the AMF.

6. In accordance with Article 44(1) of Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority)[4] ("ESMA Regulation"), the Board of Supervisors has adopted this opinion.

II. Contract classification

Commodity base product: Agricultural (AGRI)

Commodity sub product: Grain (GRIN)

Commodity further sub product: Milling wheat (MWHT)

Name of trading venue: EURONEXT PARIS MATIF

MIC: XMAT

Venue product codes: EBM, OBM

III. Market description by the competent authority

7. The MATIF Milling wheat contract (also known as Euronext Wheat or European Wheat) refers to milling wheat from any EU origin.

8. Over the last 5 years, milling wheat production in the European Union averaged 123 million metric tons per year, with France and Germany being the main producers (almost 50% of total EU production together). The Euronext milling wheat contract is considered as the benchmark for the European underlying physical market in milling wheat, meeting certain minimum requirements such as protein content (11%), specific weight = density (76 kg/hL) and Hadgberg fall time (220 seconds). These are the most important criteria, however seeds can be blended to meet these requirements (e.g., blend low-protein seeds with high-protein seeds, similarly for specific weight and Hagberg fall time, although this is more difficult). So can be dry seeds to meet moisture specifications.

9. Other basic characteristics are required such as moisture content (15% or less), broken kernels (4% maximum) and impurities such as other seeds, wood, wheat straw, etc. (2% maximum). On average, 75% of the production of the main EU producers meets these

[4] Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15. 12.2010, p. 84).

requirements. The underlying can be delivered in 5 licensed silos located in France (Dunkirk, La Pallice, Montoir, Nantes, Rouen).

10. In terms of market evolution, since 2021 the price of milling wheat has started to follow an upward trend. Before that, the price was evolving between €100/mt and €290/mt with an average price of €180/mt. Russia's invasion of Ukraine caused the price to reach a peak around €450/mt on 7 March 2022 (+130% since mid-2021). The price of the Euronext milling wheat No. 2 contract has declined nearly by 40% since mid-May 2022 due to the Black Sea grain deal and good production in Europe. Today, the market price is back to August 2021 levels and daily volatility has returned to its usual level.

11. Non-financial counterparties hold the majority share of open interest in the milling wheat contract. The share of open interest held by financial participants never exceeded 52% at its utmost, reached in June 2022 and decreased since then to be now close to 40%.

12. The wheat market is highly correlated with the corn market, as both products can be used for animal feed. When one is cheaper than the other, feed producers rearrange the composition of their feeds (to some extent) in order to obtain cheaper suitable feeds, by, for example, replacing a few percent of corn with wheat or the other way around.

13. The underlying commodity qualifies as food for human consumption.

14. Expiring months of futures are March, May, September and December. Twelve consecutive maturities are listed at any time. At expiry (the 10th of the month or the following business day), the future contract is physically delivered within the five silos located in France. Options expire the 15th of the month preceding each maturity of future (or the following business day). The delivery of options being physical, their exercise results in the assignment of future contracts at the exercise price, i.e. at the strike price.

15. Trading in the Euronext Milling wheat No. 2 contract takes place in lots. One lot is equivalent to 50 tons.

IV. Proposed limit and rationale by the competent authority

Spot month position limit

<u>Deliverable supply</u>

16. Deliverable supply amounts to 479,375 lots.

17. The AMF has determined the deliverable supply in a 3-step process, described in the following paragraphs.

18. First, the AMF estimated the yearly average of the total wheat production in Europe and the yearly average of the quantity of wheat imported by Europe (based on statistics from the French Ministry of Agriculture) over a five-year period based on the latest data available, i.e. 01/07/2017-31/06/2022) in accordance with Article 12(2)(b) of RTS 21a. This corresponds respectively to 124,842 Mt and 2,991 Mt for a total of 127,833 Mt.

19. Then this figure has been adjusted to the contract specifications requiring milling quality characteristics (statistics provided by the French Ministry of Agriculture): 95,875 Mt, which represents 75% of the total available quantity.

20. Finally, the figure has been time-prorated to take into account the duration of spot month contracts (3 months), multiplied by the equivalent number of unit (50 mt/lot): 479,375 lots.

21. Deliverable supply should be based on production, imports and storage capacity. However, the AMF does not consider storage capacity as a deliverable quantity since, under market practice, the amount of wheat in the storage at the end of the year should be equal to the initial quantity at the beginning of the same year, in order to compensate for a possible deterioration of production in the following season. The AMF therefore deems that the amount of wheat held in storages should not be considered as a usable quantity and included in the calculation of deliverable supply.

Spot month position limit

22. The spot month definition includes 90 calendar days.

23. The spot month limit is split into two periods, established by decreasing on an incremental basis towards the maturity of the commodity derivative contract in accordance with Article 11(2) of RTS 21a ("gliding path limits"):

   a. At the start of the spot month, the position limit is set at 70,000 lots, which constitutes 14.6% of the deliverable supply; and

   b. Over the last twelve trading sessions before its expiry, the position limit of the spot month is reduced to 20,000 lots, which constitutes 4.2 % of the deliverable supply.

Spot month position limit rationale

24. In accordance with Article 11(3) of RTS 21a, the baseline for the spot month limit for commodity derivatives with an underlying that qualifies as food for human consumption, with a total combined open interest in spot month and other months' contracts exceeding 50,000 lots over a consecutive 3-month period, amounts to 20% of the deliverable supply.

For those commodity derivatives, a range between 2.5% and 35% of the deliverable supply can be used for setting the spot month limit for commodity derivatives.

25. The AMF has considered the following factors relevant for adjusting downwards the baseline in accordance with:

- Article 19(1) of RTS 21a, as there is a large volume of open interest;
- Article 20(1) of RTS 21a, as there is a high number of market participants holding a position in the commodity derivative;
- Article 21(1) and more specifically 21(2)(e) of RTS 21a, to reflect macroeconomic or other related factors that influence the operation of the underlying commodity market including the delivery, storage, and settlement of the commodity.

26. With respect to macroeconomic and other related factors, it should be noted that the conflict in Ukraine and the closure of ports in the Black Sea (responsible for 38% of wheat imports in Europe and 30% of world exports) led to a limitation of logistical capacities for nearly five months, putting the market under pressure. While the agreement on export corridors in the Black Sea has improved the situation, the scenario remains fragile.

27. On top of the general position limit for most of the spot month described in the previous paragraphs, the AMF has set a second lower position limit which applies only to the last twelve trading sessions before expiry to reduce delivery risk and ensure an orderly settlement of the contract. During this period, the limit is set at 20,000 lots, which constitutes 4.2% of deliverable supply.

28. All the other potential adjustment factors set out in RTS 21a have been considered by the AMF and were not regarded as material or relevant to require additional adjustments from the baseline.

29. Based on the above, the AMF considered that it was appropriate to set the spot month' limit at the start of the spot month at 14.6% of the deliverable supply representing 70,000 lots, and to set the limit at 4.2% of the deliverable supply representing 20,000 lots for the last twelve trading sessions before the expiry of the spot month.

<u>Open interest</u>

30. The open interest amounts to 503,521 lots.

31. The AMF has calculated the open interest based on the daily position reports received from Euronext in accordance with Article 58 of MiFID II from January 2022 to December 2022. The AMF first aggregates positions by day, ISIN and position holder in order to have

net (either long or short) positions per ISIN, day and position holder. Then, the AMF computes (1) the total long positions (per day and underlying contract) by adding up all the long positions calculated at the previous step; and (2) the total short positions (per day and underlying contract) by adding up all the short positions calculated at the previous step.

32. The AMF finally calculates the daily open interest (per underlying contract) by taking the greatest (in absolute terms) between the total long positions and the total short positions[5] and then calculates an average of this value over a period of one year.

Other months' position limit

33. Two different limits are set for the other months. During the last 21 days before the spot month expiry, the position limit is set at 120,000 lots, which constitute 23.8% of the open interest. For the rest of the other months' period, the limit is set at 100,000 lots, which accounts for 19.9 % of the open interest.

Other months' position limit rationale

34. In accordance with Article 13(1) of RTS 21a, the baseline figure for the other months' limit amounts to 25% of the open interest. A range between 2.5% and 35% of the open interest can be used for setting the other months' for contracts with an underlying that qualifies as food intended for human consumption with a total combined open interest in spot month and other months' contracts exceeding 50,000 lots over a consecutive 3-month period.

35. The AMF has considered relevant to adjust the baseline downwards in accordance with:

- Article 19(1) of RTS 21a, as there is a large volume of open interest;
- Article 20(1) of RTS 21a, as there is a high number of market participants holding a position in the commodity derivative;
- Article 21(1) and more specifically 21(2)(e) of RTS 21a, to reflect macroeconomic or other related factors that influence the operation of the underlying commodity market including the delivery, storage, and settlement of the commodity, as described in paragraph 26 above.

36. For most of the other months, the AMF has set out the limit at 100,000 lots, which corresponds to 19.9% of the open interest. The AMF decreased the position limit from the

[5] Although the sum of all long positions should be equal to the sum of all short positions on a given day and a given underlying contract, small differences may exist in the data.

initial baseline of 25% to 19.9% in light of the aforementioned adjustment factors and to round-up the limit at 100,000 lots.

37. The AMF has decided to set a different limit for the other month's during the last twenty-one trading sessions before the expiry of the spot month to take into account the roll of spot month position to other months. Rolling is the transfer of positions from one expiring contract to the next one. This strategy is followed by many participants who want to maintain exposure on the most liquid contract, usually the first contract to expire. As maturity approaches, spot month positions will decrease, while other month's positions will temporarily increase. Once the maturity date has passed, the second maturity becomes the new first maturity (spot month), and all other month's positions decrease.

38. Since the roll of positions is typically spread over the three to four weeks preceding the expiry of the spot month, the other months' limit is temporarily increased during the last twenty one trading days before the expiry of the spot month by 20,000 lots, a quantity equivalent to the maximum position limit allowed on the spot month during the last 12 days (so that this quantity on the expiring contract can be transferred to the other month's contract before it becomes the new spot month).

39. All the other potential adjustment factors set out in RTS 21a have been considered by the AMF and were not regarded as material or relevant to require additional adjustments from the baseline.

40. Based on the above, the AMF considered that it was appropriate to set the other month' limit at 19.9% of the open interest corresponding to 100,000 lots, except for the last twenty-one days before the spot month expiry where the limit is set a 23.8% of the open interest, representing 120,000 lots.

V. ESMA's assessment

41. This Opinion concerns positions held in Euronext Milling wheat No. 2 futures and options.

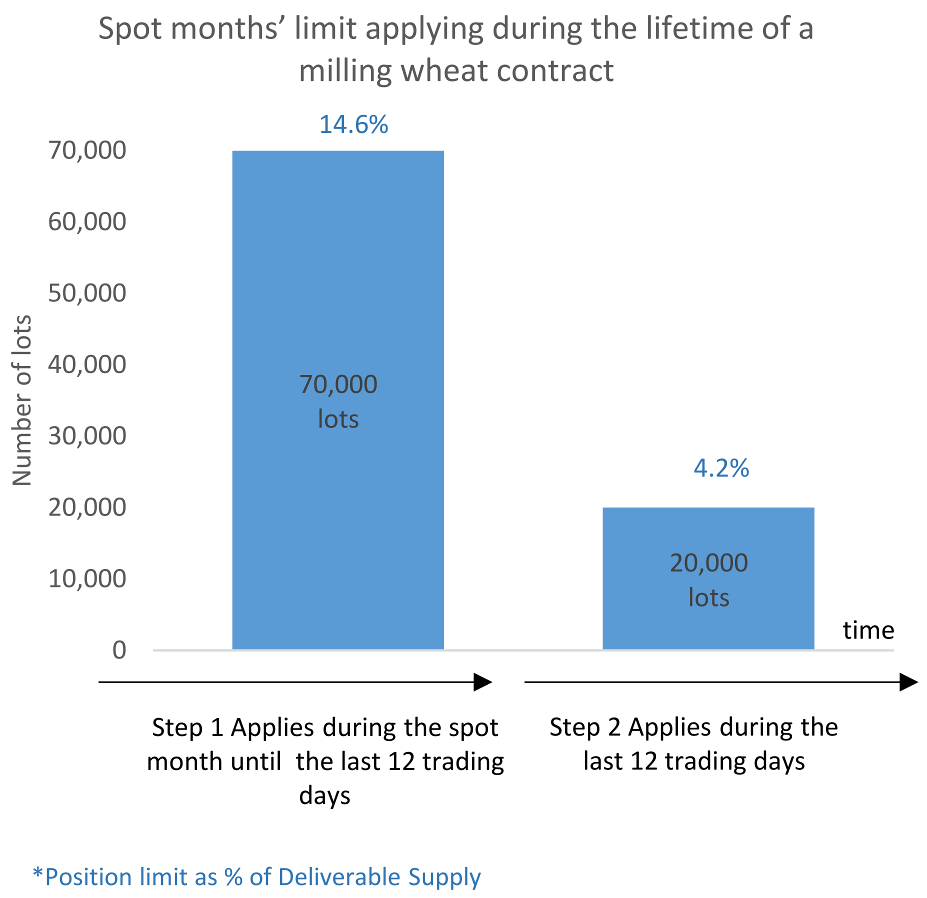
42. ESMA has performed the assessment based on the information provided by the AMF.

43. For the purposes of this Opinion, ESMA has assessed the compatibility of the new position limits the AMF intends to set according to Article 57(4) of MiFID II with the objectives of Article 57(1) of MiFID II and with the methodology for calculation of position limits established in RTS 21a, in accordance with Article 57(3) of MiFID II.

Compatibility with the methodology for calculation of position limits established in RTS 21a in accordance with Article 57(3) of MiFID II

44. The AMF has set two position limits for the spot month and two position limits for the other months.

45. <u>Spot month position limit</u>



46. The calculation of the deliverable supply is based on average data over the last five years. As four expiries are traded each year, the yearly available deliverable supply has been divided by four. The calculation of deliverable supply is consistent with Article 12(2)(b) of RTS 21a that sets out that "Competent authorities shall determine the deliverable supply (…) by reference to (…); (b) a one to five-year period immediately preceding the determination for an agricultural commodity derivative".

47. Setting different position limits for different times within the spot month period which decrease on an incremental basis towards the maturity of the contract is consistent with Articles 11(2) of RTS 21a.

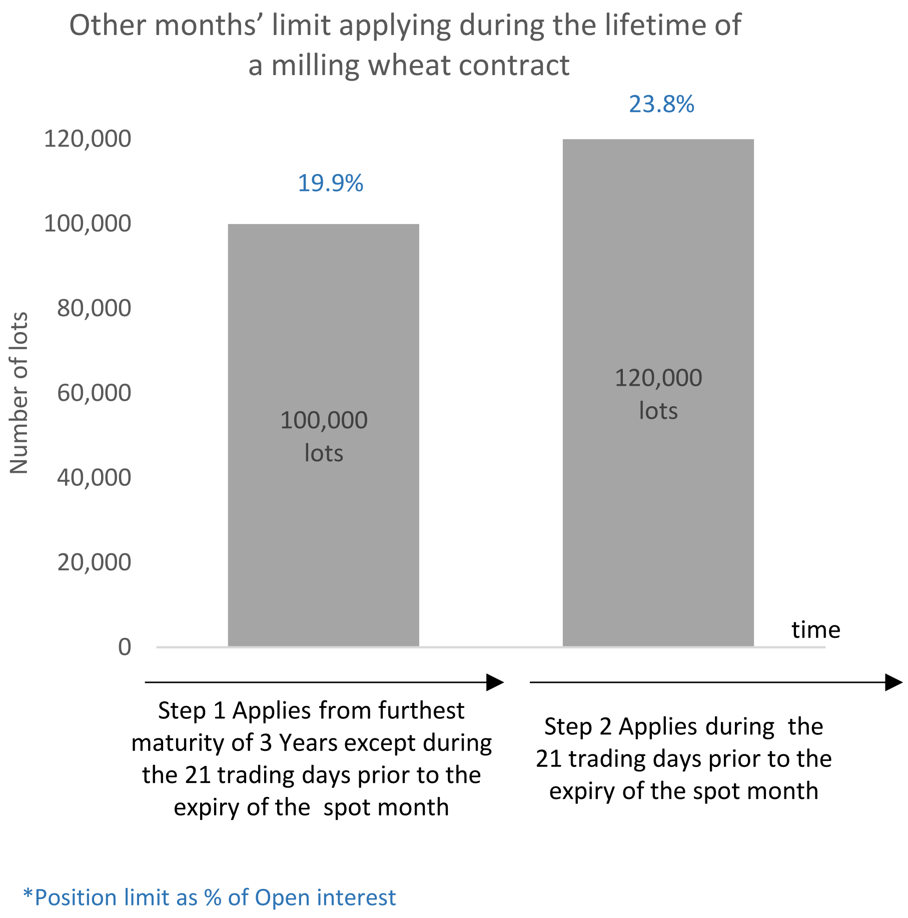
48. The gliding path limits are within the boundaries established in Article 16 of RTS 21a.

49. Compared to the baseline figure of 20% for derivative contracts with an underlying that qualifies as food intended for human consumption with a total interest in spot and other months' contract exceeding 50,000 lots, the position limit at the start of the spot month has been adjusted downwards. This downward adjustment is consistent with Article 18 of RTS 21a.

50. The position limit at the start of the spot month has been further adjusted downwards as there is a high number of market participants holding a position in the commodity derivative and to reflect macroeconomic or other related factors that influence the operation of the underlying commodity market including the delivery, storage, and settlement of the commodity. These two downward adjustments are consistent with Article 20(1) and 21(1) of RTS 21a, respectively.

51. The position limit applicable to the last twelve trading days before the expiry of the spot month has been adjusted downwards to 20,000 lots, i.e. to 4.2 % of the deliverable supply. This significant downward adjustment aims at reducing delivery risk and ensuring an orderly settlement of the contract. This downward adjustment is consistent with Article 21(2)(b)(iii) of RTS 21a.

<u>Other months' position limit</u>



52. The open interest has been calculated by the AMF based on the position reports daily received in accordance with Article 58 of MiFID II. The daily average open interest has been calculated adding the open interest from each identified related contract that can be aggregated. ESMA considers such aggregation sensible, as the contracts will be covered by the same limits. The daily average open interest has been calculated over one year, from January 2022 until December 2022. ESMA considers that such calculation of open interest by the competent authority provides an accurate and reliable figure and promotes convergence in the setting of position limits by competent authorities. ESMA also considers such approach consistent with Article 14 of RTS 21a.

53. For most of the other months', the baseline figure of 25% has been adjusted downwards to 100,000 lots, i.e. 19.9% of the open interest, to take into account the large volume of open interest. This downward adjustment is consistent with Article 19(1) of RTS 21a.

54. The position limit for most of the other months' has been further adjusted downwards as there is a high number of market participants holding a position in the commodity derivative and to reflect macroeconomic or other related factors that influence the operation of the underlying commodity market including the delivery, storage, and settlement of the commodity. These two downward adjustments are consistent with Article 20(1) and 21(1) of RTS 21a, respectively.

55. ESMA considers that temporarily adjusting the other months' limit upwards during the 21 trading days preceding the expiry of the spot month is a reasonable approach to allow for the rolling of positions from the spot month contract to the other months' contract and takes into account the objective characteristics of the market, as clarified in Recital 18 of RTS 21a.

56. Consequently, these position limits have been set following the methodology established by RTS 21a.

Compatibility with the objectives of Article 57(1) of MiFID II

57. These position limits have been set following the methodology established by RTS 21a.

58. ESMA has found no evidence indicating that the proposed position limits are not consistent with the objectives of preventing market abuse and supporting orderly pricing and settlement conditions established in Article 57(1) MiFID II. The AMF has given due consideration to the orderly delivery and settlement of the Milling wheat contract by reducing the authorised position limit during the last twelve trading days before the expiry of the spot month. The limits set on the quantity of milling wheat each person may make or take delivery of should prevent any person from accumulating a dominant position such that persons are enabled to squeeze the market through restricting access to milling wheat and will support orderly pricing and settlement conditions.

59. Overall, the position limits set for the spot month and the other months achieve a reasonable balance between the need to prevent market abuse and to ensure an orderly market and orderly settlement while ensuring that the development of commercial activities in the underlying milling wheat market and the liquidity of Euronext milling wheat futures and options are not hampered.

VI. Conclusion

60. Based on all the considerations and analysis presented above, it is ESMA’s opinion that the spot month position limit complies with the methodology established in RTS 21a and is consistent with the objectives of Article 57 of MiFID II. The other months’ position limit also complies with the methodology established in RTS 21a and is consistent with the objectives of Article 57 of MiFID II.

Done at Paris, 20 April 2023

Verena Ross

Chair

For the Board of Supervisors