

OPINION on position limits on MILLING WHEAT No. 2 contract

I. Introduction and legal basis

1. On 2 June 2017, the European Securities and Markets Authority (“ESMA”) received a notification from the Autorité des Marchés Financiers (“AMF”) under Article 57(5) of Directive 2014/65/EU on markets in financial instruments¹ (“MiFID II”) regarding the exact position limits the AMF intends to set for the Milling Wheat No 2 commodity contract in accordance with the methodology for calculation established in Commission Delegated Regulation (EU) 2017/591 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 in commodity derivatives² (“RTS 21”) and taking into account the factors referred to in Article 57(3) of MiFID II.
2. ESMA’s competence to deliver an opinion is based on Article 57(5) of MiFID II. 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)³ (“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

MIC: XPAR

Venue product codes: EBM, OBM

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) 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).

³ 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).

III. Market description by the competent authority

3. The MATIF Milling wheat contract (also known as Euronext Wheat or European Wheat) refers to milling wheat from any EU origin.
4. The underlying EU wheat production amounted to 135 Mt in 2016/17 (vs. 153 Mt in 2015/16), out of which 27 Mt were exported. In 2016, the EU accounted for 18% of the total world production and 15% of the total world exports. The main European producers are France, Germany and the UK. European exports mostly head toward Northern Africa. The market participants are mostly European grain merchants, feed and starch industrials. Although the contract specifications correspond to wheat of milling quality (based on minimum dry matter protein content, minimum Hagberg Falling number and kilos per hectolitre specific weight among other criteria), the contract is widely used as a benchmark to set the price of commercial transactions on other cereals than wheat such as feed barley, malting barley and oat due to the liquidity of the MATIF wheat future.
5. The underlying commodity qualifies as food for human consumption.
6. Expiring months of futures are March, May, September and December. Twelve consecutive maturities are listed at any time. At expiry, the future contract is physically delivered, with four silos located in Rouen and Dunkirk. In adverse market conditions between 2014 and 2016, some of these silos happened to experience congestion of their storage capacity, resulting in episodes of delivery suspensions. Since then, new silos have been added by the trading venue and the CCP in order to increase the storage capacity and reduce the risk of delivery constraints at expiry.
7. 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.
8. Trading in the MATIF Milling wheat contract takes place in lots. One lot is equivalent to 50 tons. Delivery months are March, May, September and December so that twelve delivery months are available for trading over a three-year period.
9. The average daily volumes amounted to 35,000 lots in 2016 for futures (vs 35,400 in 2015, based on public data available on Reuters) and 4,700 lots for options (vs 7,600 in 2015, source Euronext). This decrease in option volume between 2015 and 2016 is due to lower European wheat production and a less volatile price environment.
10. The futures contract constitutes the global price benchmark for the European underlying physical market in milling wheat.



IV. Proposed limit and rationale by the competent authority

Spot month position limit

Deliverable supply

11. Deliverable supply amounts to 383,349 lots, which represents 19,167,450 tonnes.
12. Deliverable supply calculation methodology: The AMF has determined the deliverable supply according to the following process :
13. Data corresponding to the total production of wheat in Europe over the last five years have been collected from the European Commission's Directorate General for Agriculture: 139.80 Mt per year on average.
14. Then the figures have been adjusted for the specifications of the contract requiring milling quality features. This adjustment has been applied per country and per harvest year (also based on statistics of harvest quality provided by the Directorate General for Agriculture): 76.67 Mt per year on average, which accounts for 55% of the total EU production.
15. Finally, the figure has been time-prorated to take into account the duration of spot month contracts (four contracts each year i.e. three months on average): 19.17 Mt, or 383,349 lots.
16. As a reference, taking the last twelve months instead of the average of the last five years would result in 374,861 lots.
17. The four silos eligible for delivery have a cumulated storage capacity of 1.4 Mt. These silos located in ports are dedicated to export and do not keep the wheat for a long time. As a matter of fact, Senalia, the biggest silo in Rouen with a storage capacity of 0.8 Mt, had a turnover of 8.5 Mt over the latest harvest year i.e. more than ten times the storage capacity. The risk of stockpiles blocking the silos is all the more reduced with public silos which do not belong to one single participant and which turn out to account for the biggest share of the total storage capacity available for the wheat contract.
18. Under these circumstances, the AMF decided to determine the deliverable supply based on the production instead of the storage capacity. Nonetheless, the possible constraints stemming from storage capacity at delivery have been taken into account more directly through the adjustment factors for the spot month limit.

Spot month position limit

19. The spot month definition includes 90 calendar days.
20. The spot month limit is established by decreasing on an incremental basis towards the maturity of the commodity derivative contract in accordance with Article 9(3) of RTS 21 ("gliding path limits"). At the start of the spot month, the position limits is set at 60,000 lots,



which constitutes 15.7% of the deliverable supply. Over the last twelve trading sessions before its expiry, the position limit of the spot month is reduced to 20,000 lots, which constitutes 5.2 % of the deliverable supply.

Spot month position limit rationale

21. The AMF has taken into account in particular the large open interest, the constraints on delivery and the fact that certain agricultural commodity derivatives may have an impact on consumer food prices and accordingly started from the baseline of 20% in accordance with Article 9(4) of RTS 21 before applying other adjustment factors. In order to round the limits expressed in lots, the spot month limit was set at 15.4% compared to the baseline of 20%. This value constitutes the regular limit.
22. Moreover, particular attention was paid to the sensitive period of expiry resulting in a decrease of the spot month limit in order to limit the delivery risks at silos. Although steps have been taken to increase storage capacity at delivery points, a downward adjustment of the spot month limit was considered justified to reduce any risk of delivery, as foreseen under Article 20 of RTS 21.
23. Over the last twelve trading sessions before its expiry, the position limit of the spot month is cut close to the minimum authorized rate in order to reduce any risk of delivery according to Article 20. As the cumulated delivery capacities referenced for the Euronext wheat contract correspond to 7% of the deliverable supply, setting a limit close to the level of 5% (corresponding to 19 167 lots) at the end of the spot month seems appropriate to ensure an orderly and well-functioning market. For ease of application, this temporary limit of the spot month has been rounded to 20 000 lots, or 5,2% of the deliverable supply, over the last twelve trading sessions before expiry.
24. The AMF did not consider the lifetime of the spot month contract, between two and four months depending on the expiry, to be short compared to the one month duration of most commodity contracts and therefore did not apply any downward adjustment to the baseline figure based on the maturity of the contract under Article 16 of RTS 21.
25. Similarly, the AMF deemed the risk of restriction or control of the underlying commodity to be low as the wheat produced by all EU Member State meet the Euronext specifications for milling wheat. Accordingly, no downward adjustment was made either to the baseline figure based on Article 17 of RTS 21.

Open interest

26. The open interest amounts to 290,859 lots. The open interest value was calculated as the average of the daily open interest of futures (after cumulating the open interest of all futures i.e. all maturities) from 4 January 2016 to 30 December 2016, based on public data provided by Thomson Reuters.



Other months' position limit

27. 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 100,000 lots, which constitute 34.4% of the open interest. For the rest of the other months' period, the limit is set at 60,000 lots, which accounts for 20.6 % of the open interest.

Other months' position limit rationale

28. Taking into account in particular the large size of open interest and, as for the spot month limit, the fact that certain agricultural commodity derivatives may have an impact on consumer food prices the limit has been set 5% lower than the baseline before rounding. In order to round the limits expressed in lots, the other months' is set at 20.6% (compared to the standard baseline of 25%). This value constitutes the regular limit.
29. The AMF also noted that the open interest (291,000 lots) is significantly lower than the deliverable supply (383,000 lots) and considered that this requires the limit to be adjusted upward momentarily so that participants holding positions in the spot month contract coming close to expiry but not interested in going to delivery can roll back their positions into the first other months contract that will soon become a spot month contract. When the positions on the spot month future which roll into the contract that will become the next spot month add to those of all other months futures, a temporary increase of the all other months limit is considered necessary to accommodate the transfer of positions until the expiry of the current spot month contract. After this the rolled position becomes the new spot month and the other months' limit can go back to its normal value.
30. The roll of positions on the milling wheat is spread over a longer period, typically over the three to four weeks preceding the expiry (significant positions start to roll after the expiry of options on the corresponding spot month future, which takes place three to four weeks before the expiry of the spot month future).
31. To accommodate this sensitive period of expiry and facilitate the rolling of contracts, the other months' limit is increased close to the maximum authorised value of 35% of the open interest (before rounding the limit expressed in lots at 100 000 i.e. 34.4% of the deliverable supply) during the roll period corresponding to the three weeks preceding the expiry of the spot month.
32. The other months' includes eleven separate expiries. By comparison with the more than 100 separate expiries listed in some gas derivative contracts, the AMF did not consider the number of separate expiries to be large and therefore did not apply any adjustment to the baseline figure based on the maturity of the contract under Article 16 of RTS 21.

V. ESMA's Assessment

33. This Opinion concerns positions held in MATIF Milling wheat No 2 futures and options.

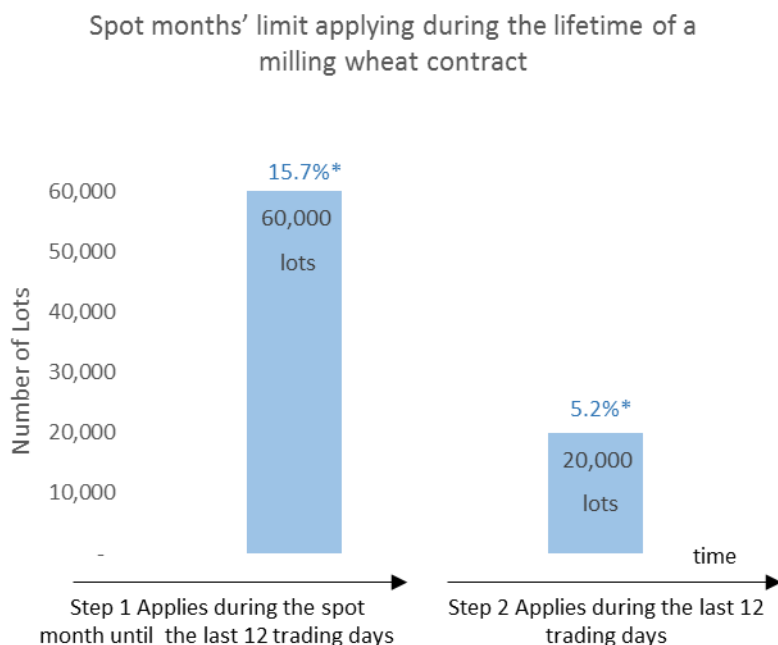
34. ESMA has performed the assessment based on the information provided by the AMF.

35. For the purposes of this Opinion, ESMA has assessed the compatibility of the intended position limits with the objectives of Article 57(1) of MiFID II and with the methodology for calculation of position limits established in RTS 21, in accordance with Article 57(3) of MiFID II.

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

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

Spot month position limit



*Position limit as % of Delivery Supply

37. 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 10(2) of RTS 21 which sets out that “the deliverable supply must be determined by reference to the average monthly

amount of the underlying average commodity available for delivery over the one year period immediately preceding the determination”.

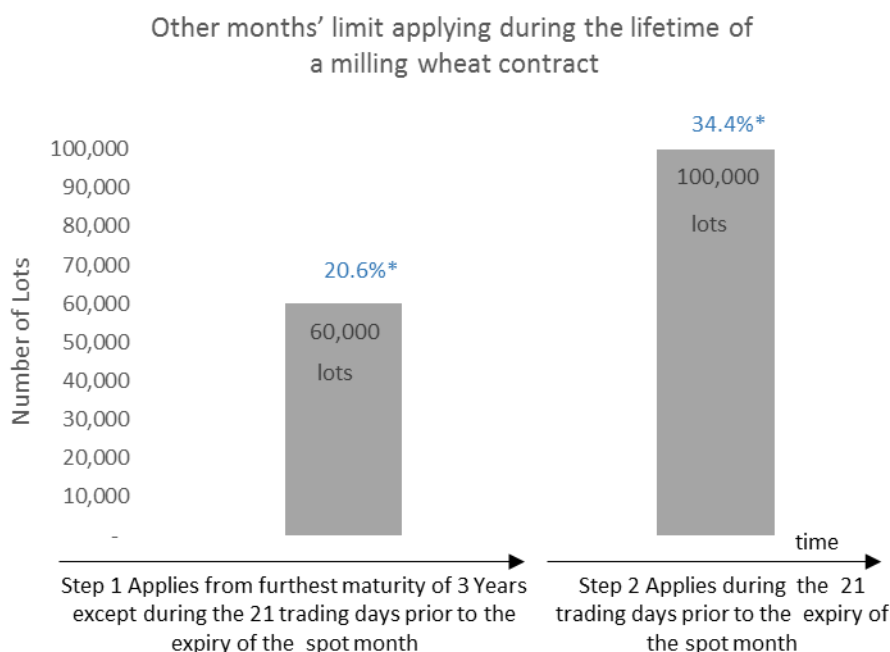
38. The gliding path limits are within the boundaries established in Article 14 of RTS 21.

39. 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 to 60,000 lots, i.e. to 15.7% of deliverable supply, due to the large volume of overall open interest. This downward adjustment is consistent with Article 17 of RTS 21.

40. 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 5.2 % of the deliverable supply. This significant downward adjustment takes into account the capacity constraints at delivery points and aims at reducing any risk of delivery. This downward adjustment is consistent with Article 20(2)(b)(iii) of RTS 21.

41. The decreasing spot month limits towards the maturity of the derivative contract are consistent with Article 9(3) of RTS 21.

Other months’ position limit



*Position limit as % of Open interest

42. The open interest was calculated as the average value of open interests reported by a data vendor over 2016. ESMA considers such an approach sensible in this case as an average for



a period of time gives a more stable measure of open interest and considers such approach consistent with Article 12 of RTS 21.

43. Two position limits are established for the other months': one for the 21 trading days preceding the start of the spot month and one for all the other months. Since there are no market makers in the Euronext Milling wheat No. 2 future and option contracts, setting two different position limits is consistent with Article 19(2) of RTS 21 which foresees the possibility to have different limits for the other months' where the number of investment firms acting as market makers at the time the position limit is set is lower than three.
44. For most of the other months', the baseline figure of 25% has been adjusted downwards to 60,000 lots, i.e. 20.6% of the open interest, to take into account the large volume of open interest. This is consistent with Article 18(1) of RTS 21.
45. Taking into account the fact that the open interest is significantly lower than the deliverable supply, the position limit is adjusted upward to 100,000 lots during the 21 trading days preceding the start of the spot month. This is consistent with Article 18(3) of RTS 21 and with the related Recital (20) of RTS 21 which clarifies that significant discrepancies between open interest and deliverable supply justify adjustments from the baseline applicable to the other months' limit in order to avoid disorderly market.
46. Consequently, these position limits have been set following the methodology established by RTS 21.

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

47. These position limits have been set following the methodology established by RTS 21.
48. ESMA has found no evidence indicating that the proposed position limits are not consistent with the objectives 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.
49. 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

50. Based on all the considerations and analysis presented above, it is ESMA's opinion that the spot month position limits do comply with the methodology established in RTS 21 and are consistent with the objectives of Article 57 of MiFID II. The other months' position limits do comply with the methodology established in RTS 21 and are consistent with the objectives of Article 57 of MiFID II.

Done at Paris, 10 August 2017

Steven Maijoor

ESMA Chair