

**Stimulation Plan for Long-term KTB Futures Trade: Revision of Derivatives Market Business Regulation was approved by FSC**

To promote trading of long-term KTB futures, the KRX amended its Derivatives Market Business Regulation and the Financial Services Commission (FSC) approved the amended Regulation on September 1, 2010.

As the follow-up of the plan for promoting long-term KTB futures that was devised jointly by the Financial Services Commission, Ministry of Strategy and Finance and KRX, the latest amendment streamlined the regulations related to KTB futures.

The key amendments are 1) the harmonization of regulations governing KTB futures to ensure the balanced growth of short-term and long-term KTB futures, 2) stabilization of market operation and 3) reinforcement of market making function in the Derivatives Market.

**1. Harmonization of regulations governing individual KTB futures**

By minimizing the differences in the regulations applied to short-term and long-term KTB futures, it has been attempted to make easy the trade linking the short-term and long-term KTB futures contracts and enhance the accessibility of KTB futures.

(1) To ensure the settlement expediency of 10-year KTB Futures, the plan is made to change the final settlement method from physical delivery to cash settlement. Accordingly, like the case of 3-year KTB Futures, the final settlement price of 10-year KTB Futures will be calculated on the basis of yield of basket bonds for final settlement and present value model for underlying bond and the final settlement day will be changed to T+1 day, i.e., the day after the last trading day, from the existing T+2 day.

(2) By considering the recent market interest rate, the coupon rate of underlying bonds of 3-year and 5-year KTB Futures would be lowered to 5% per year from 8% per year in order to enhance the hedge effectiveness.

(3) The plan is made to increase the trading unit of 10-year KTB Futures to KRW 100 million at par value from KRW 50 million at par value and lower the quotation unit to 0.01 from current 0.02. However, the tick value of KRW 10,000 will be kept unchanged.

(4) To facilitate efficient trading of spread between short-term and long-term KTB futures, the number of delivery month contracts of 10-year KTB Futures will be reduced from 3 quarterly month contracts to 2 quarterly month contracts and the longest trading period will be reduced to 6 months from 9 months.

#### <Trading and Settlement Regulations of KTB Futures>

|                        | Existing regulation |                    |   | Amended regulation |
|------------------------|---------------------|--------------------|---|--------------------|
|                        | 3-yr & 5-yr         | 10-yr KTB          |   | All KTB futures    |
| Settlement method      | Cash settlement     | Physical delivery  | ➡ | Cash settlement    |
| Trading unit           | KRW 100 million     | KRW 50 million     |   | KRW 100 million    |
| Coupon rate            | 8% per year         | 5% per year        |   | 5% per year        |
| Delivery month         | 2 quarterly months  | 3 quarterly months |   | 2 quarterly months |
| Longest trading period | 6 months            | 9 months           |   | 6 months           |
| Quotation unit         | 0.01                | 0.02               |   | 0.01               |
| Final settlement date  | T+1                 | T+2                |   | T+1                |

## 2. Stabilization of KTB futures market

To overcome the problem of sudden price drop or increase caused by the difference between the most recent matching price and closing price during the single price

auction at market closing time, the indicative price will be made public during the quotation receiving time for single price auction at market closing time. However, to prevent the input of deceitful quotations, correction or cancellation of quotations will be restricted during the last 1 minute before the market closing.

### 3. Reinforcement of market making function in the Derivatives Market

Presently, the incentive given to the market makers is a fixed percentage of transaction fees of product for which the market maker provided the market making service. Financial resource available for paying incentives for low liquidity products such as 10-year KTB Futures is rather insufficient because of their low trading volume. To solve this problem, the plan is made to use the service fees collected in the Derivatives Market as the financial source for paying incentives to the market makers, thus making the market making function more substantial.

This amended Derivatives Market Business Regulation will be put into effect in October 2010.

#### <Contract specifications of KTB Futures>

|                            | 3-yr KTB<br>Futures          | 5-yr KTB<br>Futures          | 10-yr KTB<br>Futures                       | Amendment                        |
|----------------------------|------------------------------|------------------------------|--|----------------------------------|
| <b>1. Underlying asset</b> | Hypothetical Benchmark KTB   |                              |  |                                  |
| 1) Par value               | KRW 100                      |                              |  |                                  |
| 2) Maturity                | 3 year                       | 5 year                       | 10 year                                    |                                  |
| 3) Interest payment        | Every 6 months               |                              |  |                                  |
| <b>4) Coupon rate</b>      | <b><u>5% per year</u></b>    | <b><u>5% per year</u></b>    | 5% per year                                | 8% → 5%                          |
| <b>2. Trading unit</b>     | KRW 100 million at par value | KRW 100 million at par value | <b><u>KRW 100 million at par value</u></b> | KRW 50 million → KRW 100 million |

|   |   |  |  |   |
|---|---|--|--|---|
| <b>3. Multiplier</b>  | 1,000,000   | 1,000,000  | <b><u>1,000,000</u></b>  | 500,000 → 1,000,000   |
| <b>4. Delivery month</b>  | 2 quarterly months  | 2 quarterly months   | <b><u>2 quarterly months</u></b>   | 3 → 2   |
| <b>5. Longest trading period</b>  | 6 months  | 6 months   | <b><u>6 months</u></b>   | 9 months → 6 months   |
| <b>6. Quotation unit</b>  | 0.01  | 0.01   | <b><u>0.01</u></b>   | 0.02 → 0.01   |
| 7. Price quoting method   | P/KRW 100   |  |  |   |
| 8. Last trading day   | 3 <sup>rd</sup> Tuesday of delivery month (to move forward if it is a market holiday) |  |  |   |
| <b>9. Final settlement day</b>  | T+1   | T+1  | <b><u>T+1</u></b>  | T+2 → T+1   |
| <b>10. Final settlement method</b>  | Cash settlement   | Cash settlement  | <b><u>Cash settlement</u></b>  | Physical delivery → Cash settlement   |
| <b>11. <u>Final settlement price</u></b><br>( <i>r</i> : Yield of basket bond for final settlement) | $\sum_{i=1}^6 \frac{(5/2)}{[1 + (r/2)]^i} + \frac{100}{[1 + (r/2)]^6}$                | $\sum_{i=1}^{10} \frac{(5/2)}{[1 + (r/2)]^i} + \frac{100}{[1 + (r/2)]^{10}}$ | $\sum_{i=1}^{20} \frac{(5/2)}{[1 + (r/2)]^i} + \frac{100}{[1 + (r/2)]^{20}}$ | ① Lowering of coupon rate<br>② Taking into consideration the cash settlement method |
| <b>12. Basket bonds for final settlement (KTBs)</b>   | Of 6-month coupon bonds, those designated by the KRX                                  | Of 6-month coupon bonds, those designated by the KRX                         | <b><u>Of 6-month coupon bonds, those designated by the KRX</u></b>           |   |

\* Bold letter indicates the parts amended.

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**About KRX**

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