ASX 24 Bond Futures Roll Consultation

Response to consultation feedback

26 February 2020

Contacts

For general enquiries, please contact:

Kristye van de Geer
Senior Manager, Interest Rate Products
T 02 9227 0130
E Kristye.vandegeer@asx.com.au

Luke Flory
Manager, Interest Rate Products
T +61 (0)2 9227 0577
E luke.flory@asx.com.au

Media enquiries, please contact:
David Park
Corporate Communications Adviser
T 02 9227 0010
E david.park@asx.com.au

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1. Introduction

1.1. Purpose of this paper

The purpose of this paper is to provide a summary of, and response to, the feedback received during the recent consultation on the ASX 24 Bond Futures Roll (“the Roll”) and to outline the changes that ASX intends to implement.

1.2. Background

On 3 October 2019, ASX released a consultation paper seeking feedback on proposed changes to the Bond Futures contract specification and the Roll functionality. ASX requested feedback from market participants on proposals to improve the efficient functioning of the Roll for a broad range of users.

ASX also included information on the recent rule changes governing the Pre-Trade Risk Management (PTRM) system and sought feedback on those rules and the uses of PTRM.

Although not included as a proposal, ASX also provided market users with an opportunity to comment on the potential use of block trades in the Roll.

1.3. Overview of responses received

Thirty six (36) submissions were received from a wide range of market users including trading and investment banks, proprietary trading firms, fund managers, trading participants and industry bodies who submitted on behalf of their members.

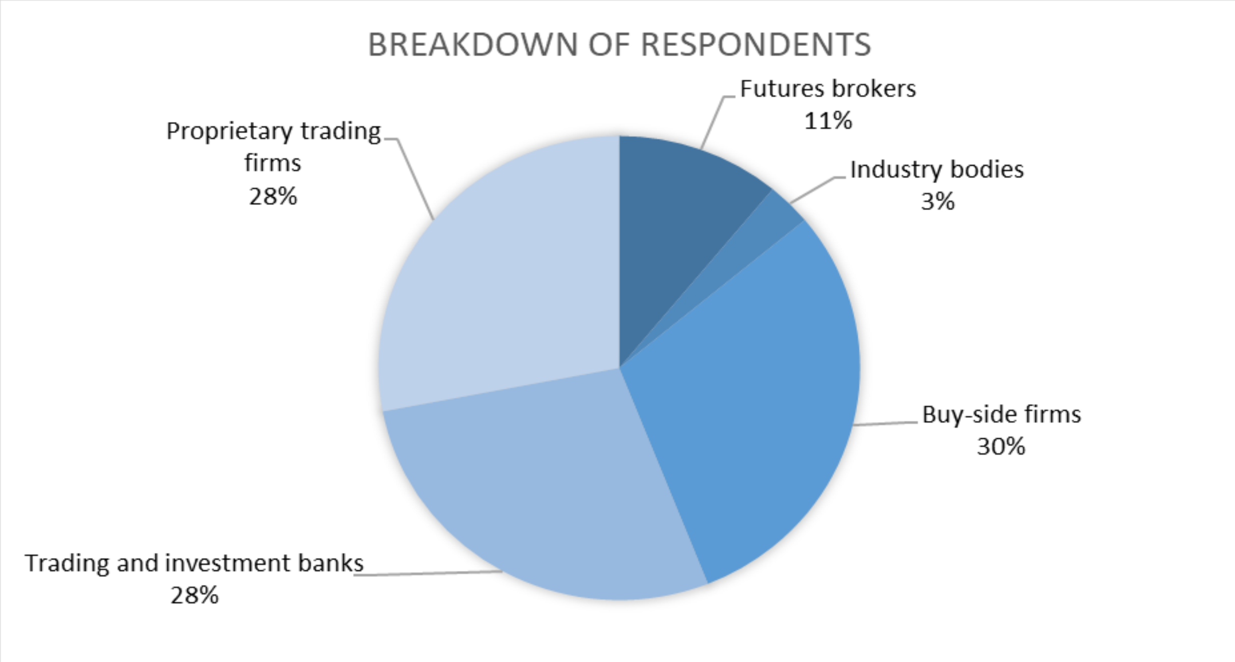
The majority of respondents expressed the view that the proposed changes would provide an opportunity to reduce costs with smaller tick increments and generate operational efficiencies and improved order management capabilities through Good Till Cancelled (GTC) functionality during the Roll period. The majority of respondents also preferred a phased approach to implementing any combination of proposed changes. Respondents believed that this would provide the market with sufficient time to adjust to the new dynamics before implementing any additional proposals.

For two thirds of respondents, a reduction in the cost of rolling a bond futures position was a key focus. These respondents believed that the proposed changes that would reduce costs for end users and make the Roll a more efficient process. Twenty five percent (25%) wanted no change to the tick increments and the remaining respondents were neutral or provided no response.

Of the 36 respondents, 14% wanted no change to the current structure of the Roll, citing that the Roll functions efficiently for the broad range of users.

Additional market structure solutions were suggested by some respondents. These included mid-point matching, an auction, de-linking the Roll from the outright market and an auto-disconnect for limit breaches of PTRM rules. Some respondents also provided comments on how the proposals could further be applied to the SPI 200 Index Futures roll market.

ASX greatly appreciates these considered contributions. ASX will engage with market users via the ASX Interest Rate and the ASX Equity Futures working groups to discuss longer term initiatives and potential future market enhancements. These working groups will be reconvened in the first half of 2020.



1.4. Summary of topics included in the consultation paper

The consultation paper sought feedback on proposals to:

- Reduce the minimum tradeable tick increment for the 3 and 10 Year Bond Futures for the Roll
- Increase in the current maximum order size of 9,999 lots to 20,000 lots
- Implement Good Till Cancelled (GTC) functionality for combination orders in the 3 and 10 Year Bond Roll Futures.

In addition to the proposed changes listed above, ASX also sought feedback on:

- The recent rule change addressing the use of the Pre-Trade Risk Management system as an order management tool
- Block trades for the Roll. While ASX was not proposing to introduce block trades for the Roll, questions were included to enable market participants to submit their views on the topic. Feedback was sought specifically on how to ensure that robust price formation, transparency of liquidity and prices, and access to the market for both smaller and larger users, could be maintained.

2. Planned changes and implementation schedule

2.1. Overview

ASX believes there is an opportunity to reduce total costs for the Roll and to deliver enhancements to the functioning and timeliness of the Roll process. ASX feels that this would deliver a beneficial outcome for a broad range of market users. The impact of these changes will be continually measured and monitored to validate and quantify improvements, identify any adverse outcomes and signal if further changes or remediation is required.

The planned changes will be deployed in a timeline that accommodates participant feedback provided during the consultation process. However, ASX advises that future tick changes may be applied more dynamically in response to market conditions. As such, changes may be advised with a shorter notice period of 1-2 months and participants should ensure that the changes they make to support the reduced tick sizes also enable this flexible approach.

2.2. Planned changes

ASX plans to implement the following changes, subject to regulatory clearance:

I. **Reduce the minimum tradeable tick increment for the 3 Year Bond Futures outright and roll from 0.5 basis points to 0.2 basis points for the period of the Roll.**

II. **Reduce the minimum tradeable tick increment for 10 Year Bond Futures outright and roll from 0.25 basis points to 0.1 basis points for the period of the Roll.**

The target, subject to regulatory clearance, is to implement the reduced ticks from the June 2020 roll period.

For the purpose of the minimum tradeable tick increment change, the Roll period is defined as five business days (including the Last Trade Day) prior to the contract month's settlement.

ASX plans to implement GTC functionality first for the Bank Bill Futures spread market, and will then assess its applicability for the Roll. This will also enable ASX and market users to assess the impact of the reduction to the minimum tick increment on the market dynamics, cost effectiveness and efficiency of the Roll in isolation.

Key deliverables and target dates for the change to the minimum tick increment are provided in section 2.3.

Further comments on minimum tick increments:

Given the current tick increments of 0.5bps for the 3 Year Bond Future and 0.25bps for the 10 Year Bond Future, the logical next step might appear to be to halve the current tick increments to 0.25bp for the 3 Year Bond Future, and 0.125bps for the 10 Year Bond Future. ASX would ideally prefer to be able to use these increments and may revisit these for use in the future. However, these preferred tick sizes are challenging or unavailable in the short to medium term for the following reasons:

- A move to a 0.25bp tick in the 3 Year Bond Future would require a longer implementation time of approximately 12 months (6 months' ASX work, followed by a further 6 months for development and coordinated testing with our Clearing Participants and trading platform vendors).
- A move to a 0.125bp tick in the 10 Year Bond Future is not currently supported by ASX systems and many vendor platforms due to a restriction on the total number of characters.

ASX therefore believes that the planned changes to 0.2bps and 0.1bps respectively are the best available solution to ensure the effectiveness of the Roll for a broad range of users within a reasonable time period.

Market users should note that when the tick increments change for the Roll period:

- In the 3 Year Bond Future, some orders (spread and outright) will be purged during the transition into the Roll, and some orders will be purged during the transition out of the Roll. That is, orders at a 0.005 price will be purged during the transition from the non-Roll period into the Roll as these increments will not be supported, therefore non-tradeable, during the Roll (at a 0.002 price increment). Similarly, any orders that have a non-tradable price (i.e. a price ending in 0.002, 0.004, 0.006 or 0.008) will be purged during the transition from the Roll period to the non-Roll period.
- In the 10 Year Bond Future, some orders (spread and outright) will be purged during the transition out of the Roll. That is, orders at increments other than 0.005 and 0.010 will be purged during the transition from the Roll period to the non-Roll period, as these increments will not be supported, therefore non-tradeable, during the non-Roll period (i.e. a price ending in 0.001 – 0.004, 0.006 – 0.009).

2.3. Key activities and target dates

Subject to market readiness and regulatory clearance, ASX is targeting the following dates for the key activities:

Activity	Responsibility	Target Dates
Publication of Bond Roll Consultation response paper	ASX	26 February 2020
Publication of impact assessment for tick change: - Roll and outright price examples - One Session Option VWAP rounding rules - Daily and expiry settlement price calculation and rounding rules - Order management (order purging on tick change)	ASX	March 2020
ASX 24 Operating Rules - Procedure amendments	ASX	March 2020
Testing – Availability on ASX 24 external customer development environment	Participants	April 2020–June 2020
Implementation	ASX and Participants	8 June 2020

3. Summary of consultation feedback on proposals and ASX response

3.1. Reduction in minimum tradeable tick increment for the Roll

ASX believes there is an opportunity to improve the efficiency of the Roll via narrowing the minimum tradeable tick increments. This would have the effect of reducing total costs for the Roll and improving the functioning and timeliness of the Roll process. ASX feels that this would deliver a beneficial outcome to the market for a broad range of users.

ASX asked respondents to indicate preferences and potential impacts for reducing the minimum tick increments or maintaining them at current levels. ASX was also interested in the lead time businesses would require to make tick increment changes.

Support to reduce the tick increment

There was strong support from respondents wanting to see a reduction in the minimum tick increment for both the 3 and 10 Year Bond Roll, with 66% of respondents favouring finer tradeable increments. This feedback suggested that a reduction in the minimum tick increments was the most supported change and may result in a more efficient and timely outcome for market users, encouraging them to cross the bid/offer spread rather than be passively filled.

The main views cited in support of a reduction in the minimum tick increments were that it would:

- Result in a material cost reduction for those needing to roll their exposure
- Provide market users with the flexibility to choose the timing of their roll activity based on fair value dynamics rather than queue position
- Improve price discovery as a result of more granular pricing points, particularly important in a low interest rate volatility environment
- Align the Roll tick value with comparable international exchange contracts in dollar value terms
- Align the futures bid/offer spread with the finer spread available in the underlying physical market
- Increase volatility, enabled by finer tick increments, and potentially attract new participants to the Roll

- Encourage new liquidity providers who employ alternative trading strategies that provide liquidity at narrower tick sizes

For a number of market users, the Roll is a mechanism to maintain existing exposure and hedges rather than an opportunity to add value for their end clients. Within that group, some market users believe a tick reduction could more appropriately balance the interests of those wishing to roll their positions with those providing liquidity in both the Roll and the outright contracts.

Those supportive of a reduction to the minimum tick increment stated that it would not have a negative impact on the functioning of the Roll. Many respondents felt that there was sufficient liquidity to facilitate risk transfer with a narrower tick. Some highlighted that the top of book depth relative to open interest is very large when compared to other global exchanges, and saw this as an indication that the current bid/offer spread is too wide. A few respondents commented that while a tick reduction may reduce the liquidity pool provided from a subset of participants, it may improve the timeliness of the Roll process. This feedback was consistent with many respondents who suggested market users would be more inclined to cross the bid/offer spread if the tick increment was narrowed from current levels. Respondents also noted that by reducing the overall cost of participating in the futures market it may add liquidity to the broader market. It may also result in additional opportunities to deploy new trading strategies during the Roll.

Some respondents suggested that a reduction in the minimum tick increment for the Roll would not have a significant impact on liquidity of the outright markets in the non-Roll period.

In the absence of change, some respondents stated there would be a continued reluctance to cross the bid/offer spread. Without addressing this, the Roll will remain a costly and time intensive way to maintain their exposure.

Support to maintain the current tick increment

Twenty-five percent (25%) of respondents believe the minimum tick increments should remain at the current levels. The main concern from respondents against a reduction was the impact on available liquidity in both the Roll and outright markets. Some respondents would like ASX to consider de-linking the outright 3 and 10 Year Bond Futures and the Roll, citing concerns that there would be diminished liquidity in the outright 3 and 10 Year Bond Futures should the outright tick increments be reduced in the Roll period.

A few respondents indicated that a reduction in the tick increment may lead to an overall reduction in the liquidity of the outright futures, in the event that Roll liquidity providers leave the market altogether. Further comments from respondents against the minimum tick reduction included that:

- The current tick increment supports a timely, efficient and stable Roll that is resilient to moderate levels of outright volatility. It may be detrimental to the liquidity of the Roll period by reducing top of book volumes
- It would heighten risks of increased volatility and price movement in the Roll and outright markets, which may result in an unwillingness to leave resting orders in the order book, reducing overall liquidity
- It could reduce liquidity at each tradeable level which could neutralise the value added by the minimum tick reduction and result in price slippage on larger orders. As a result, market users may cross the same minimum tick spread in aggregate
- It will reduce the profitability for some liquidity providers in the Roll and dis-incentivise those liquidity providers from participating during the non-Roll period, resulting in lower liquidity, increased volatility and price slippage on large orders

Implementation timeframe

ASX requested feedback on the implementation timeframe for a change in the minimum tick increment for the Roll. Responses varied regarding the lead time that market users would require from zero lead time to 9 months with the majority stating they could make changes on short notice. Those that indicated a longer implementation time were contacted individually and subsequently all have confirmed they could support changes in a shorter window of time.

ASX response: *ASX believes there is an opportunity to reduce total costs for the Roll and to deliver improvements to the functioning and timeliness of the Roll process, distributing value to a broad range of market users. This view is derived from detailed analysis of current market top of book liquidity, market depth and roll market behaviour.*

The majority of respondents were supportive of ASX prioritising a reduction in the minimum tick increment over, but not in isolation of, the other proposals set out in the consultation.

ASX will reduce the 3 Year Bond Futures roll from 0.5 basis points to 0.2 basis points for the five days prior to the expiry of the lead futures contract.

For the 10 Year Bond Futures roll, ASX will reduce the minimum tick increment from 0.5 basis points to 0.1 basis points for the five days prior to the expiry of the lead futures contract.

ASX anticipates that we may see lower top of book liquidity in the Roll. Current liquidity is excessive of demand which is indicative that there is ample liquidity and depth to meet demand at a finer tick increment.

The impact of these changes on both the Roll and outright markets will be continually measured and monitored to validate and quantify improvements, identify any adverse outcomes and signal if further changes or remediation is required. This ongoing review of market quality and dynamics will help identify the optimal point at which the market continues to be a cost effective, liquid and efficient market for the broader set of market users.

ASX is aware that some market users may require a longer lead time to implement the tick reduction changes in their systems. ASX has already been in discussion with those market users to ensure a delivery timeframe that accommodates all. However, ASX advises future tick changes may be applied more dynamically in response to market conditions. As such, changes may be advised with a shorter notice period of 1-2 months.

3.2. To increase the maximum allowable order size for the 3 and 10 Year Bond Futures to 20,000 contracts

The current maximum allowable order size is 9,999 contracts for the 3 and 10 Year Bond Futures. ASX sought feedback on whether an increase to 20,000 contracts or another number was supported. Reasons for not supporting an increase in the order size were also requested.

Against increasing the allowable maximum order size

A majority of the respondents (61%) preferred that the current maximum order size of 9,999 lots remain unchanged. This was supported by a range of market users who believe the current size is appropriate.

Respondents cited the following reasons against an increase to the maximum order size:

- If delivered in isolation (without a reduction to the minimum tick size) it may be used by participants that employ Roll trading strategies to crowd out queue position in greater volume
- Conversely, others believed that if delivered with a minimum tick reduction, it may result in increased price slippage and have a larger market impact on price movements than fundamentals may imply
- Increased risk around order entry and order management with the possibility of larger execution errors
- Little demand from clients to execute transactions greater than 10,000 contracts
- It may further disadvantage firms with higher latency market access technology
- It may result in the order book being further locked up by larger orders, particularly in periods of low volatility
- Larger orders being executed in the market may increase the potential for more a disorderly market
- Liquidity providers may reduce the liquidity shown in the order book, which may result in increased price slippage for large orders

Support for increasing the maximum allowable order size

Nineteen percent (19%) of respondents supported an increase in the maximum order size, with most respondents supportive of an increase to 20,000 contracts. A few respondents suggested that an increased maximum order size should be determined by the open interest of each participant. Respondents in favour of an increase in the maximum allowable order size stated that it would:

- Assist their workflow by consolidating orders into larger, more manageable parcels
- Simplify the Roll management process by reducing the number of orders required to roll open positions
- Aggregate more client orders into one order allowing agency firms the potential to share good queue position across multiple clients
- Be reflective of the level of open interest and top-of-book depth, indicating that larger order sizes would be sustainable in the market
- Allow more efficient order management for those with larger dollar value of a basis point (DV01) to hedge in futures
- Potentially discourage order proliferation and entering of orders without genuine intent to trade
- Not have a negative impact on order book liquidity during non-Roll periods, and may benefit traders of the Roll

Some respondents suggested that any change to the maximum allowable order size should be constrained by each participant's open interest level, restricting Roll activity and volume by the relative amount required to roll. Respondents noted any change to the maximum allowable order size should be monitored and have appropriate oversight and checks against credit limits by Clearing Participants. Any increase in the maximum allowable order size should not expose the broader market to greater systemic risk.

***ASX response**: ASX will retain the current maximum order size at 9,999 lots. ASX will continue to assess market conditions and the dynamics of the Roll to determine whether there is sufficient demand and available liquidity to support an increase to the maximum allowable order size in the future.*

3.3. To support Good Till Cancelled (GTC) functionality for combination orders

On the ASX 24 platform, combination contract orders – calendar and inter-commodity spreads – are only valid for the current trading session. Customers wishing to maintain a Bond Roll order over multiple trading sessions are required to re-enter their orders at the start of each trading session.

ASX asked if there was support for the introduction of GTC spread order types for the 3 and 10 Year Bond Futures. Benefits and drawbacks were requested along with consideration as to when the GTC functionality should be available: ie at all times, or for a more limited window of time prior to expiry. Finally, comments were sought on a proposed GTC order reinstatement approach.

Support for the introduction of GTC functionality

A moderate majority of respondents supported this proposal with 58% in favour of introducing GTC functionality for the Roll**.** Respondents in a favour of GTC spread functionality represented a wide range of market users with many highlighting similar perceived benefits. These suggested benefits included:

- Consolidated user workflow and risk reduction by not having to re-enter orders at the opening of every session
- Reduced operational overhead of re-instructing and re-confirming existing orders with trading participants
- A longer time period for Roll orders to persist in the order book and potentially be passively filled
- Rewarding participants who show liquidity and may promote a longer Roll period
- Increased price discovery for the Roll over multiple trading sessions
- Bring ASX 24 Bond Futures Roll into line with equivalent global exchange functionality

While the majority suggested the functionality be made available at all times, some thought it was only beneficial for a shorter time period - for example, five or 14 business days prior to expiry. Some respondents opted for a 24-hour or Trade Date GTC order type. The main rationale cited was that it may reduce order proliferation during the most liquid rolling period.

Some respondents were supportive of GTC only on the condition that it is implemented after a reduction to the minimum tick size. There was common feedback that delivering GTC in isolation, while maintaining the current tick size could potentially exacerbate the risk of an increase in resting orders resulting in the order book building up. Respondents believed that this build-up of orders, combined with a reluctance to cross the bid/offer spread, could result in the Roll locking up much earlier.

All respondents agreed with the proposed GTC order reinstatement approach outlined in the paper.

Against the introduction of GTC functionality

Almost one third (31%) of respondents were against the implementation of GTC functionality. These respondents raised varying concerns about the impact GTC functionality would have on the structure of the market. Some respondents stated that it may result in an increase in excess orders in the Roll. Alternatively, one respondent suggested that GTC functionality would result in diminished top of book volumes (citing equivalent offshore treasury futures that have GTC functionality), which may lead to less orderly Roll flows and wider traded price ranges during the Roll.

Further suggested concerns included:

- It may result in the order book locking up when the new contract month is first listed
- It would disadvantage funds whose mandates restrict activity to liquid contracts, limiting their ability to place GTC spread orders earlier
- It may not result in a reduction in transaction costs if market users were still having to cross the bid/offer spread without receiving passive fills
- It may create a new set of risks and resourcing requirements for trading participants who will be managing the GTC orders through the day and evening sessions
- It may increase quotation risk for market makers or liquidity providers
- It may result in "predatory strategies" being employed if the order book becomes relatively thin

- GTC spread orders entered at three months out from the Roll may not be a true indication of real interest to trade

Many respondents acknowledged that this is a large technical build and there will be a longer delivery time frame compared to the other proposals.

> ***ASX response:*** *ASX will revisit the applicability of GTC functionality to the Roll once the system enhancements have been delivered. ASX plans to implement GTC functionality for the Bank Bill Futures spread market first. This will enable ASX and market users to assess the impact of the reduction to the minimum tick increment on the market dynamics, cost effectiveness and efficiency of the Roll.*

3.4. Use of Pre-Trade Risk Management tools

This section sought feedback on recent changes made to the rules governing the use of ASX's Pre-Trade Risk Management (PTRM) system. This is a risk management tool accessible to all direct members of the exchange and as such, may not be relevant to all respondents of the consultation paper.

The intention of the rule change and subsequent published guidance was to address behaviour where PTRM was being used as an order management tool, with excess messages rejected by PTRM functionality, rather than for risk management.

As a part of the consultation, ASX sought feedback on the effectiveness of the PTRM procedure and general support for the change. The requirement to undertake development for real-time monitoring was raised as a concern following the implementation of the rule. Respondents were asked to comment if this requirement was addressed with the additional wording and guidance provided in the PTRM procedure, or whether a reliance on the Class Waiver for No Action remains.

Use of PTRM for order management rule change

All respondents that addressed this proposal were supportive of ASX clarifying the appropriate use of PTRM. Respondents agreed that a reject message limit was prudent to discourage the use of PTRM as an order management tool. However, many believe that due to the limited individual waivers that were granted over the September 2019 Roll, the positive impacts of the PTRM changes were not fully realised at the time of submitting their response to the consultation paper. Some respondents, although supportive of the intention of the PTRM changes, believe these changes may not be the most effective way of addressing the underlying issue, with the new rule inadvertently impacting on genuine uses of PTRM. Some respondents cited concerns that the risk of breaching the rules may decrease the utility of the PTRM system for reducing risk.

Continued need for real-time monitoring

Many respondents stated that despite the additional guidance and wording, that there was still a need for real-time monitoring. This requirement has added further technological development and compliance overhead. Some participants suggested that the recent rule change be re-addressed so that those operating under the Class Waiver for No Action would no longer require the waiver to continue their business.

Continued reliance of Class Waiver for No Action

A few participants thought that the lack of consultation in setting out the new conditions may have had unintended consequences and resulted in a review of workflows. Some respondents noted that they will continue to rely on the Class Waiver for No Action until they have completed enhancements to order management systems to prevent any potential breach of the new PTRM rules.

Some noted that removal of the Class Waiver for No Action may result in some participants having to cease certain business for clients or invest in significant infrastructure to monitor rejects on a real-time basis.

Additional technical developments

A few respondents have highlighted that they will require additional technical build to ensure they remain compliant with the new rules and avoid any inadvertent breaches. There was some feedback that respondents would like ASX to provide monthly reporting of activity to assist compliance with the PTRM message reject rule. Some respondents have requested ASX review the rule and consider further enhancements to the PTRM system to introduce centralised alerts for the participant and ASX, as well as an auto-disconnect functionality, in lieu of a rule breach.

> ***ASX response:*** *The purpose of the recent rule change is to ensure that the functionality provided by PTRM is used for its intended purpose. PTRM is an important tool provided as part of the ASX 24 Trading Platform, delivering an additional layer of pre-trade risk management. ASX's intent was to address the use of PTRM as an order management tool where excess messages are rejected by PTRM functionality. The rule change was not intended to penalise breaches that occur when the system is being used for its intended purpose.*
>
> *ASX will maintain the current PTRM rules and will continue to monitor effectiveness of the message reject levels and amend if required.*
>
> *Participants should ensure that their risk management systems have appropriate risk limits in place such that the PTRM functionality provided by ASX is used as the second layer of risk management. ASX actively monitors the use of PTRM and investigates any breaches of the reject message limit should a breach occur.*

3.5. General questions

Of the four proposals presented in the consultation paper and notwithstanding the fact that PTRM changes have already been made, ASX sought feedback on a single priority proposal for implementation. If there was a view that more than one of the options should be implemented or if any combination of options was potentially detrimental, additional commentary was sought.

Priority of proposal implementation

The majority of respondents prioritised a reduction to the minimum tick increment above the other proposed changes. Many felt that delivering this change was the most readily achievable and equitable change to the functioning of the Roll. Some noted that further changes should be contingent on how the Roll dynamics change following a minimum tick increment reduction.

A subset of respondents believed that the correct use, guidance and enforcement of the Pre Trade Risk Management tools could have a successful impact on the functioning of the Roll.

Some recommended that the most impactful change ASX could make to the functioning of the Roll would be to limit the total number of trading sessions that participants could use simultaneously. This would reduce the competitiveness of those with certain trading strategies and would make it more equitable for others in competing for queue position.

Preferred combination of proposals

The most popular combination for the proposed changes was delivering a reduction to the minimum tick increment followed by implementing GTC functionality. Many respondents were aware that the implementation of the GTC functionality requires a significant technical build and has a longer delivery to market than the other proposals. A few respondents felt that implementing a reduction to the tick size and GTC functionality may have a destabilising effect on the Roll order book and remove any incentive to provide liquidity.

Some feedback stated that increasing the maximum order size and implementing GTC functionality without first reducing the minimum tick increment may be detrimental to the quality of the market. Another combination that was flagged as potentially adverse to the quality of the Roll market was the reduction in the minimum tick increment and an increase in the maximum allowable order size. Some respondents believed that in this scenario, clients would be more willing to cross the bid/offer spread in larger sized orders. It was suggested that, this could heighten the risks around manual errors and potentially result in slippage.

ASX response: *ASX plans to deliver (subject to regulatory clearance) a reduction to the minimum tick increments of the 3 and 10 Year Roll as a priority. Following this implementation and an appropriate review period to assess the impact, ASX will consider the application of GTC functionality for the Roll.*

3.6. ASX block trades

ASX's objective is to encourage as much activity as possible to transact through the central limit order book. This has the benefit of supporting robust price formation; maximising liquidity and therefore efficient trade execution for the whole market; and delivering transparency to all market users.

ASX does not allow block trades during the 3 and 10 Year Bond Futures Roll and is not proposing to change this. ASX believes that block trades are not necessary or appropriate in the Roll because there is already sufficient on-screen liquidity.

A number of firms have asked for inclusion of block trades for the Roll. Questions were included in the consultation process to enable market participants to submit their views on the topic. Feedback was sought, in light of ASX's concerns, on how to ensure that robust price formation, transparency of liquidity and prices, and access to the market for both smaller and larger users, could be maintained.

Sixty-seven percent (67%) of all respondents addressed the questions on block trading functionality for the purpose of the Roll. Of those who provided feedback, 54% were against the introduction of block trading.

Against block trade functionality

A common concern raised by respondents was that it would take liquidity off-screen and result in a fragmented and less transparent market. These respondents also expressed the view that this functionality would be to the benefit of a small subset of participants only.

Those respondents commented that the lack of real-time information flow from the block trading mechanism would fragment liquidity and reduce transparency of the Roll. Others questioned what benefit is achieved by "siphoning" liquidity into an off-market facility when there is ample available liquidity on screen. It was also noted that the inclusion of block trades would increase the complexity of the Roll process, reduce transparency and fragment liquidity. For some market users this would require the implementation of additional comprehensive compliance frameworks.

Supportive of block trade functionality

Those who were supportive of the introduction of block trades (33% of respondents who addressed the questions on the block trade functionality, or 22% of all respondents) believed it would provide greater certainty of execution and deliver the most efficient way for clients and liquidity providers to transfer risk. Many respondents supportive of block trades for the Roll referenced other global futures exchanges that offer block trade functionality for liquid contracts during the Roll period.

Market users supportive of permitting block trading wished to be transacting at prices within the on-screen bid/offer, thereby reducing the cost of maintaining futures exposure. Some respondents stated that during the Roll, a large proportion of executions take place over the last few minutes leading into the day session close. This can create last second price volatility at the end of the day and often forces market participants to cross the spread, trading at levels that differ from the day's average price range. By allowing block trades during the Roll, it was proposed that market users may choose to trade using block trades or on-screen depending on the stability of the Roll, their market view and where liquidity exists. A couple of respondents suggested that this would reduce price volatility and manage market impact during the Roll. One respondent stated it could also provide for best execution to clients without needing to cross the spread to ensure execution certainty. Another respondent stated that with block trades liquidity will move to where it is actually trading.

It was also proposed that by allowing block trading to cover both the day session and the Roll period, increased liquidity and improved market quality would result. A couple of respondents were supportive of permitting block trading for both the Bond and SPI Rolls.

Addressing price formation, transparency and equal access concerns

To address transparency concerns, some respondents suggested ASX provide an opening auction or matching phase (as an alternative to block trades) for roll orders where all larger parcels are matched on an aggregate basis at a reduced tick size. Other responses focused on improving the timely reporting of off-market transactions while enforcing block trades to occur only within the current bid/offer spread. More specifically, some respondents highlighted that robust requirements in the ASX 24 Operating Rules relating to the block trade agreement price, combined with updated block trade registration and market reporting requirements, would increase awareness and timeliness of block trades delivering transparency for all market users.

On the question of equal access, a few respondents suggested ASX should set the minimum block trade threshold low enough to include as many participants as possible to alleviate the concept of the block mechanism being exclusive to a subset of market users.

While some respondents did not directly address some of the concerns ASX voiced in the consultation regarding the potential impact of introducing block trades for the Roll, some welcomed the chance to explore the concept further in a separate consultation or working group.

Appropriate minimum block trade threshold

In reference to the minimum block trade threshold, some respondents indicated that the threshold should be orders that exceed the current maximum allowable on-screen order size of 9,999 lots. Some suggested that by making the minimum block trade thresholds DV01 neutral for each tenor, it may keep the bulk of liquidity on-screen. Other respondents suggested the thresholds be set at 25,000 contracts. A few respondents suggested a smaller minimum block size threshold would make it more accessible for those with smaller positions to roll.

ASX response: *ASX would like to thank respondents for their views on how we may alleviate concerns around transparency, price formation and equal access if the block trade mechanism was to be introduced for the ASX 24 Bond Futures Roll.*

A few respondents voiced an interest in being part of further discussions in order to address the concerns ASX has raised in the consultation paper. ASX will engage with market users via the ASX Interest Rate Working Group to discuss block trades and alternative longer term initiatives, taking into account the impacts on the market which will result from the changes outlined in this paper.