Spread contracts Q&A

1. **What is a spread contract?**
A spread contract is a financially settled futures contract with an underlying price that is differential, positive or negative, between two different securities, and in particular two different futures. Buying a spread contract is fundamentally equivalent to buying one futures and selling the other futures contract.

2. **What spread contracts will be launched on Euronext?**

- European Milling Wheat vs Chicago Wheat Spread Futures Contract
- European Milling Wheat vs KC HRW Wheat Spread Futures Contract
- European Milling Wheat vs European Corn Spread Futures Contract

3. **How does it work?**

- **Specifications**: The contract size is 50 metric tons and quoted in Euros and centimes per metric tonne; the contract tick size is €0.25 per tonne and tick value is €12.50.
- **Trading**: The Spread Contract will trade on a separate order book from the underlying futures contracts. It will have a daily opening and closing price until the expiry of the maturity.
Like an independent contract, the daily settlement price (DSP) will be calculated using trades, bids and offers made in relation to the spread futures contract. The daily settlement price should be similar but may sightly differ from the difference in price between the prices of the two underlying futures.
- **Settlement**: The exchange delivery settlement price (EDSP), or final price, is set on the Last Trading Date (LTD) of the spread futures. It will consist of the difference in prices of the two underlying futures contracts at that date, at the same time. The convergence between the spread futures and the underlying contracts is therefore ensured.
For instance, the EDSP of the Euronext Milling Wheat No. 2 vs CME Chicago Wheat Spread will be the difference between (i) the DSP of Euronext Milling Wheat No. 2 futures on the last trading date of the spread and (ii) the Chicago Wheat Marker at 18:30 CET on the same date, converted to Euros using the mid-rate of the WM/Refinitiv 18:30 CET Intraday Spot Rate for EUR/USD. The EDSP is rounded to the nearest €0.25 per ton.

4. **What is the Chicago Wheat Marker and the Kansas Wheat Marker?**

- The Chicago Wheat Marker is the value of the CME Chicago Wheat Futures Contract used to settle the spread contracts at the close of the Euronext market. It is the price of the Chicago Wheat Futures as determined and calculated by CME during a period ending at 18:30 CET.
- The Kansas City Wheat Marker is similar to the Chicago Wheat Marker, except that it takes as reference the CME Kansas City Wheat Futures Contract.

5. **Will wholesale trading be available?**

- Wholesale trading will be available, Large-Scale facilities may be used, subject to compliance with minimum volume threshold of five lots.

6. **What are the trading months ?**

- Four contract months will be available for trading: March, May, September and December starting with December 2024.

7. **Why do market participants use spreads?**

- Trading spreads between asset classes, products or periods have been developed as a relatively less risky and capital-intensive strategy, compared to trading outright contracts:
    - **Lower market risk**: the price relationship between two correlated contracts is less volatile than the price of each outright contract. In the case of an unfavourable market trend, there would be smaller losses compared to trading outright futures contracts.

    - **Better margin efficiency**: traders can expect lower margins for a spread contract compared to trading each leg individually.
- **Arbitrage opportunities** arising from the differentiated dynamics of each side of the spread strategy: there are differentiated drivers of (i) wheat production in the European Union and in the US, (ii) currency value in the US and Europe and (iii) wheat and corn production in Europe. As market demand between European wheat and US wheat, or between wheat and corn, is however somewhat correlated, market participants, both hedgers and investors, to trade for example spreads between Euronext wheat (in Euros) and CME Group (in USD) Wheat Contracts by taking inverse positions on each exchange.

8. What are the advantages of trading Euronext-listed spreads?

- The listed spread contracts launched by Euronext allow to execute a spread strategy in one trade, instead of planning for two parallel, inverse trades on each outright. Euronext-listed spreads thus allow market participants to benefit from the following advantages:
    - **Reduced transaction costs**: Trading two different products. In particular, when they belong to different exchanges, it is more expensive than trading a single contract.
    - **Mitigate execution risk**: There is an execution risk when trading a spread strategy, particularly when the legs of the spread are listed on different exchanges. However, the Euronext-listed spread contract is a single contract and is structured as a price difference between both legs.
    - **Optimise clearing efficiencies**: Trading two contracts on different exchanges and clearing them with different clearing houses requires higher collateral to be deposited with the two clearing houses as margining efficiencies are forfeited.
    - **Mitigate FX exposure and risk**: Trading two contracts listed in different currencies, such as Euronext Milling Wheat No. 2 in EUR and CME Chicago Wheat in USD, involves associated FX risks.

9. What are the benefits for Euronext to launch Euronext vs CME spread contracts?

- Euronext and CME Group list the three global wheat benchmarks: Euronext Milling Wheat, Chicago Soft Red Winter Wheat and Kansas City Hard Red Winter Wheat. These three contracts are interlinked, market participants already trade inter-commodity spreads by doing each leg on each respective exchange.
- However, there are some limitations, as described above. In particular, trading each contract individually is only possible for 3 hours in a day, when both markets are open (CME Wheat Market opens at 15:30 CET). Trading spreads is then possible until 18:30 CET, when Euronext's Market closes. As a result, spread trading opportunities are not possible in the morning sessions.
- Partnering with CME to cross-list spread contracts will address the above limitations following the feedback from several market participants and thereby facilitate trading spreads between the two markets.
- An easier, more cost-efficient and less risky way of trading spreads between the two markets is expected to attract more market players from different regions, USA in particular, to the European Wheat Market.

10. Will the introduction of new spreads reduce the number of existing tools to manage price risk or adversely affect volumes?

- The introduction of listed spread contracts will expand the set of hedging tools for investors. The attractiveness of listed spread contracts is expected to bring additional volume from both new and existing clients.

11. Who can I contact for more questions?

- Please contact the Euronext commodities team at commodities@euronext.com.