



CIR/DNPD/ 5 /2010

July 30, 2010

Recognized Stock Exchanges
and their Clearing Corporations / Clearing Houses

Dear Sir/Madam,

Sub: Options on USD-INR Spot Rate

1. This is in continuation of SEBI Circular No. SEBI/DNPD/Cir- 38 /2008 dated August 06, 2008 regarding Exchange Traded Currency Derivatives.
2. It has now been decided to permit introduction of options on USD-INR spot rate on currency derivatives segment of Stock Exchanges. Eligible Stock Exchanges may do so after obtaining prior approval from SEBI.
3. The details in terms of product design and risk management framework for options on USD-INR spot rate are as given under Annexure I.
4. The position limits specified vide SEBI Circular No. SEBI/DNPD/Cir-38/2008 dated August 6, 2008 and SEBI circular No. SEBI/DNPD/Cir-45/2009 dated March 24, 2009 now stand modified and the revised position limits are as given under Annexure II.
5. This circular is issued in exercise of the powers conferred under Section 11 (1) of the Securities and Exchange Board of India Act 1992, read with Section 10 of the Securities Contracts (Regulation) Act, 1956 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.
6. The circular shall come into force from the date of the circular.
7. This circular is available on SEBI website at www.sebi.gov.in., under the category "Derivatives- Circulars".

Yours faithfully,

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Encl: as above



ANNEXURE I

PRODUCT DESIGN AND RISK MANAGEMENT FRAMEWORK FOR OPTIONS ON USD-INR SPOT RATE

1. **Underlying**
US Dollar – Indian Rupee (US\$-INR) spot rate
2. **Type of option**
Premium styled European Call and Put Options
3. **Trading Hours**
9 a.m. to 5 p.m.
4. **Size of the contract**
US\$ 1000
5. **Quotation**
The premium would be quoted in rupee terms. However, the outstanding positions would be in USD terms.
6. **Available contracts**
Three serial monthly contracts followed by three quarterly contracts of the cycle March/June/September/December.
7. **Strike price**
Minimum of three in-the-money, three out-of the-money and one near-the-money strikes would be provided for all available contracts.
8. **Settlement mechanism**
The contract would be settled in cash in Indian Rupee.
9. **Expiry / last trading day**
The expiry / last trading day for the options contract would be two working days prior to the last working day of the expiry month.
10. **Settlement price**
The final settlement price would be the Reserve Bank Reference Rate on the date of expiry of the contracts.
11. **Final settlement day**
The options contract would settle on the last working day (excluding Saturdays) of the contract month. The last working day would be taken to be the same as that for Interbank Settlements in Mumbai. The rules for Interbank Settlements, including those for 'known holidays' and 'subsequently declared holiday' would be those as laid down by FEDAI.



12. Exercise at Expiry

On expiry date, all open long in-the-money contracts, on a particular strike of a series, at the close of trading hours would be automatically exercised at the final settlement price and assigned on a random basis to the open short positions of the same strike and series.

13. Initial Margin

The Initial Margin requirement would be based on a worst scenario loss of a portfolio of an individual client comprising his positions in options and futures contracts on the same underlying across different maturities and across various scenarios (as detailed under Annexure III) of price and volatility changes. In order to achieve this, the price range for generating the scenarios would be 3.5 standard deviation and volatility range for generating the scenarios would be 3%.

The sigma would be calculated using the methodology specified for currency futures in SEBI circular no. SEBI/DNPD/Cir-38/2008 dated August 06, 2008 and would be the standard deviation of daily logarithmic returns of USD-INR futures price.

For the purpose of calculation of option values, the following standard option pricing models - Black-Scholes, Binomial, Merton - would be used.

The initial margin would be deducted from the liquid networth of the clearing member on an online, real time basis.

14. Extreme Loss margin

Extreme loss margin equal to 1.5% of the Notional Value of the open short option position would be deducted from the liquid assets of the clearing member on an on line, real time basis. Notional Value would be calculated on the basis of the latest available Reserve Bank Reference Rate for USD-INR.

15. Net Option Value

The Net Option Value is the current market value of the option times the number of options (positive for long options and negative for short options) in the portfolio. The Net Option Value would be added to the Liquid Net Worth of the clearing member. Thus, mark to market gains and losses would not be settled in cash for options positions.

16. Calendar Spread Margin

A long currency option position at one maturity and a short option position at a different maturity in the same series, both having the same strike price would be treated as a calendar spread. The margin for options calendar spread would be the same as specified for USD-INR currency futures calendar spread.

The margin would be calculated on the basis of delta of the portfolio in each month. A portfolio consisting of a near month option with a delta of 100 and a far month option with a delta of -100 would bear a spread charge equal to the spread charge for a portfolio which is long 100 near month currency futures and short 100 far month currency futures.



17. Settlement of Premium

Premium would be paid in by the buyer in cash and paid out to the seller in cash on T+1 day.

Until the buyer pays in the premium, the premium due shall be deducted from the available Liquid Net Worth on a real time basis.



ANNEXURE II

POSITION LIMITS FOR PARTICIPANTS IN OPTIONS CONTRACT ON USD-INR SPOT RATE

- 1. Client Level:** The gross open positions of the client across all contracts (both futures and options contracts) shall not exceed 6% of the total open interest or USD 10 million whichever is higher. The Exchange will disseminate alerts whenever the gross open position of the client exceeds 3% of the total open interest at the end of the previous day's trade.
- 2. Trading Member Level:** The gross open positions of the trading member across all contracts (both futures and options contracts) shall not exceed 15% of the total open interest or USD 50 million whichever is higher.
- 3. Bank:** The gross open positions of the bank across all contracts (both futures and options contracts) shall not exceed 15% of the total open interest or USD 100 million whichever is higher
- 4. Clearing Member Level:** No separate position limit is prescribed at the level of clearing member. However, the clearing member shall ensure that his own trading position and the positions of each trading member clearing through him is within the limits specified above.



ANNEXURE III

SCENARIOS USED IN COMPUTATION OF WORST SCENARIO LOSS OF A PORTFOLIO OF AN INDIVIDUAL CLIENT COMPRISING HIS POSITIONS IN OPTIONS AND FUTURES CONTRACTS ON THE UNDERLYING ACROSS DIFFERENT MATURITIES

Risk Scenario Number:	Price Move in Multiples of Price Range	Volatility Move in Multiples of Volatility Range	Fraction of Loss to be Considered
1	0	1	100%
2	0	-1	100%
3	+1/3	1	100%
4	+1/3	-1	100%
5	-1/3	1	100%
6	-1/3	-1	100%
7	+2/3	1	100%
8	+2/3	-1	100%
9	-2/3	1	100%
10	-2/3	-1	100%
11	1	1	100%
12	1	-1	100%
13	-1	1	100%
14	-1	-1	100%
15	2	0	35%
16	-2	0	35%

The price range for generating the scenarios would be 3.5 standard deviation and volatility range for generating the scenarios would be 3%.

While computing the worst scenario loss, it shall be assumed that the prices of futures of all maturities on the underlying move up or down by the same amount.

The maximum loss under any of the scenario (considering only 35% of the loss in case of scenarios 15 and 16) is referred to in this circular as the Worst Scenario Loss.