



FSC INTRODUCES DEREGULATORY MEASURES TO BOOST KOREA'S DERIVATIVES MARKET

The FSC introduced deregulatory measures to make Korea's derivatives markets more vibrant and competitive. The reforms are intended to strengthen the derivative market's role for risk hedging and price discovery, as part of the government's broader efforts to vitalize capital markets and support the real economy.

Background

Korea's derivatives trading volume fell sharply from its peak in 2011 but recovered to an extent after 2015 with increased trading of index products.¹ Since the introduction of tighter regulations to curb speculative trading in 2011, the derivatives market's soundness improved with an increase in the number of longer-term open contracts for risk hedging.²

By investors, foreigners accounted for 50.4% of derivatives trading in 2018, up from 25.7% in 2011. Over the same period, the share of institutional investors decreased from 48.7% to 36.1%; and retail investors from 25.6% to 13.5%. Excessive entry barriers act as obstacles to retail investors, while strict margin requirements hinder institutional investors' participation.

The derivatives market is disproportionately concentrated in KOSPI200-related products, making it difficult to serve investors' demand for a variety of derivatives products.

Reform Measures

- ▶ **Lower entry barriers for retail investors** (Q4 2019/FSC, KRX)
 - Minimum deposit requirement will be abolished for professional investors and eased for non-professional investors: (i) KRW 10million or more for futures and options trading; and (ii) KRW 20million or more for all derivatives trading.
 - One hour of education and three hours of mock trading
- ▶ **Ease margin requirements for institutional investors** (Q3 2019/FSC, KRX)
 - Currently, institutional investors are required to deposit an extra margin, 10 % of credit risk limit, in addition to 100% of the volume exceeding the credit limit. The

¹ Average daily turnover (unit: trillion won): 66.3(2011), 47.9(2013), 37.2(2014), 41.2(2015), 45.0(2018)

² KOSPI 200 Futures Open Interest (unit: 10,000 contracts): 11.0(2011), 12.0(2013), 12.4(2015), 17.6(2018)

extra margin requirement will be abolished.

► **Enhance convenience for foreign investors**

- The omnibus account system will be improved to address complaints filed by foreign investors so far since it was introduced in June 2017. The number of algorithm accounts allowed to register with an omnibus account, currently limited to three, will be increased. A 'kill switch', currently activated by each omnibus account, will be allowed to be activated by end investors. (3Q 2019/KRX)
- Compression services, which enable aggregation or netting of multiple OTC derivatives trading, will be introduced. (After 2022/FSC, KRX)

► **Strengthen market-making activities** (4Q 2019/KRX)

- Market-making obligations will be expanded from the nearby futures contract, the future or option with the shortest maturity or settlement date, to the next closest futures contract
- More incentives will be granted to market makers for low-liquidity products.

► **List new derivatives products** (3Q 2019/FSC, KRX)

- e.g. KOSPO 200 Weekly Options, Spread Trading between 3-year and 10-year KTB futures.

► **Facilitate developing and listing of new derivatives products** (4Q 2019/KRX)

- The current regulatory regime which stipulates details about derivative products will be replaced with a 'negative-list' approach, which sets minimum standards to allow more autonomy for securities firms in developing new derivative products.

► **Expand centrally-cleared OTC derivatives** (After 2021/FSC, KRX)

- Currently, Korean won-denominated interest rate swaps (IRS) and U.S. dollar-denominated IRS are cleared through the KRX. The FSC and KRX will gradually expand the scope of centrally-cleared OTC derivatives – e.g. non-deliverable forward (NDF), currency rate swap (CRS), and credit default swap (CDS).

► **Introducing a Trade Repository for OTC derivatives** (4Q 2020/FSC, KRX)

- A trade repository(TR) will be introduced in October 2020 as scheduled.