

MexDer: Reinventing a derivatives market

The Mexican Derivatives Exchange MexDer started within a rather local framework but during the ten years of its existence has reinvented itself as the leading marketplace for trading derivatives on Mexican benchmarks.

Just like any other industry worldwide, the derivatives sector is nowadays exposed to the globalization process. The financial derivatives community demands innovation day to day, and expects a variety not only of local, but international products as well. With the excitement to try new markets, new products and a huge variety of business opportunities, this need is steadily growing. In order to satisfy today's requirements, arbitrage in different marketplaces is mandatory, as are sufficient products for trading and hedging as well as better ways to access the markets.

No different than any other participant in this industry, the exchanges face the reality of change: Reinvent or die. 'Change' is not merely necessary for life but it is life (Alvin Toffler). Especially for those exchanges that were conceived with a local vision in mind are embedded in the market structure, regulation, history and trademarks of their respective country. Those exchanges need to reinvent their structure proactively and face the challenge of providing a world class marketplace.

A clear example of such a process would be MexDer, the nearly 10 year old Mexican Derivatives Exchange which started within a rather local framework and in contrast with its beginnings, is currently one of the exchanges that has more successfully reinvented itself, showing not only its talent to adapt to worldwide standards but has also broken paradigms in the local market in order to become a global market with internationally appealing products.

"MexDer has been adding important changes to our regulatory and technological framework, towards allowing and facilitating the participation of international players in our market", says Jorge Alegria, CEO of the Mexican Derivatives Exchange.

Back in 2004, with strong support from the local authorities, MexDer took the first steps to modify the local regulation to create an Omnibus account scheme. Today these are the easiest means for foreigners to participate from overseas, replacing a rather complicated process and quite some paperwork. Through an omnibus account a foreign financial entity can trade Mexican derivatives executing through a MexDer Member. This is a highly efficient mechanism for foreign participants to start testing the market and already has driven the volume, especially in the equity products.

As expected the omnibus accounts were a very good start but not the solution required by the international participants. In addition other regulatory changes were implemented allowing for the first time the participation of remote members with a very low cost of entry. The first foreign remote member was Timber Hill, which started trading in June 2006. Currently MexDer has seven overseas members.

The last but not least regulatory change was the elimination of the withholding taxes for foreign participants in all the listed products in the Exchange again thanks to the strong support from the authorities, which are keen to develop the Mexican derivatives market. As a result of the local regulatory changes, the CFTC granted MexDer a No-Action-Letter which allows US customers to trade the Mexican stock exchange index future (IPC).

With new participants and favorable regulatory conditions volumes started to increase and soon overloaded the trading engine which required technological upgrade, too. With a substantial investment MexDer bolstered the electronic trading platform through an interface called MexFix to provide access to foreign and to local participants. Several independent software vendors have written to MexFix and are

currently providing access to international players; there are also other types of participants that have linked directly to the API with their own fix gateways.

The huge increase of foreign investments into the Mexican cash equity market and the Mexican peso bond market has improved liquidity and developed more mature markets. As a result, global participants as well as local investors are requiring hedging tools.

MexDer's flagship contract is the TIE (Mexico's short-term inter-bank rate), one of the world's most popular contracts, with more than 200 million contracts traded annually. Mexican banks use the TIE to manage their interest rate exposure and as a benchmark for corporate loans and mortgages. International players use it to hedge their Mexican bond and peso risk.

"Over the past few years, we've heard about what markets such as China and India will have to offer in the future," says Jorge Alegria, CEO of MexDer, "Mexico has a lot to offer today!"

The products offered in MexDer are financial derivatives on Mexican benchmarks.

Fixed Income Futures

- 10-year Interest Rate Swap Futures based on a 28-day TIE
- 28-day TIE (Inter-bank interest rate) – The most liquid contract at MexDer
- 10-year Bond (M-10)
- 3-year Bond (M-3)
- 91-day CETES (MXP Treasury Bill)

Equities

- IPC futures (Mexican stock exchange index)
- Options on IPC futures
- Options on individual stocks (America Movil, Cemex, Femsa and Naftrac)

FX

- MXP/USD futures.
- MXP/USD options
- MXP/EUR futures

Facilitating the participation of sophisticated global players at MexDer has helped to increase liquidity, which in turn benefits not only international investors but also – and in a major way – local investors.

MexDer's main objective is to become recognized as the reference for the pricing of both exchange-traded and OTC derivatives in Mexico, and to increase participation from arbitrageurs, hedge funds and algorithmic traders. Therefore in order to turn this vision into a reality, Mexico has implemented radical changes in its tax and regulatory environments as well as in the technology landscape. MexDer has reinvented itself as the leading marketplace for trading derivatives on Mexican benchmarks.

Berenice Corral is Vice President Sales and Marketing at MexDer.

Contact: 01152 555 342 9930 (phone); www.mexder.com