

LME Warehouse Reform Update

London – 2 March 2015

LME warehouse reform

12 item reform package announced in 2013

Delivered

A

LIFO Rule

B

Commitments of Traders transparency

C

Publication of queues and stock data
by warehouse

D

Separate load-out rate for steel

E

Best-practice information barrier policy

F

Enhanced LME investigation and
action powers for artificial queues

G

Creation of Physical Market Committee
plus ongoing six-monthly reviews

Consultations
ended 9-Feb-15

H

Legal review of the LME
Warehouse Agreement

I

Logistical review

L

Premium contracts (*rule changes to
facilitate premium hedging solutions*)

Discussion
Paper

J

Assess powers to limit rents in queues
as a future policy option

K

Assess structural solutions to
high charges

A The Linked Load-In / Load-Out Rule

LILO implemented on 1-Feb-15

Delivered

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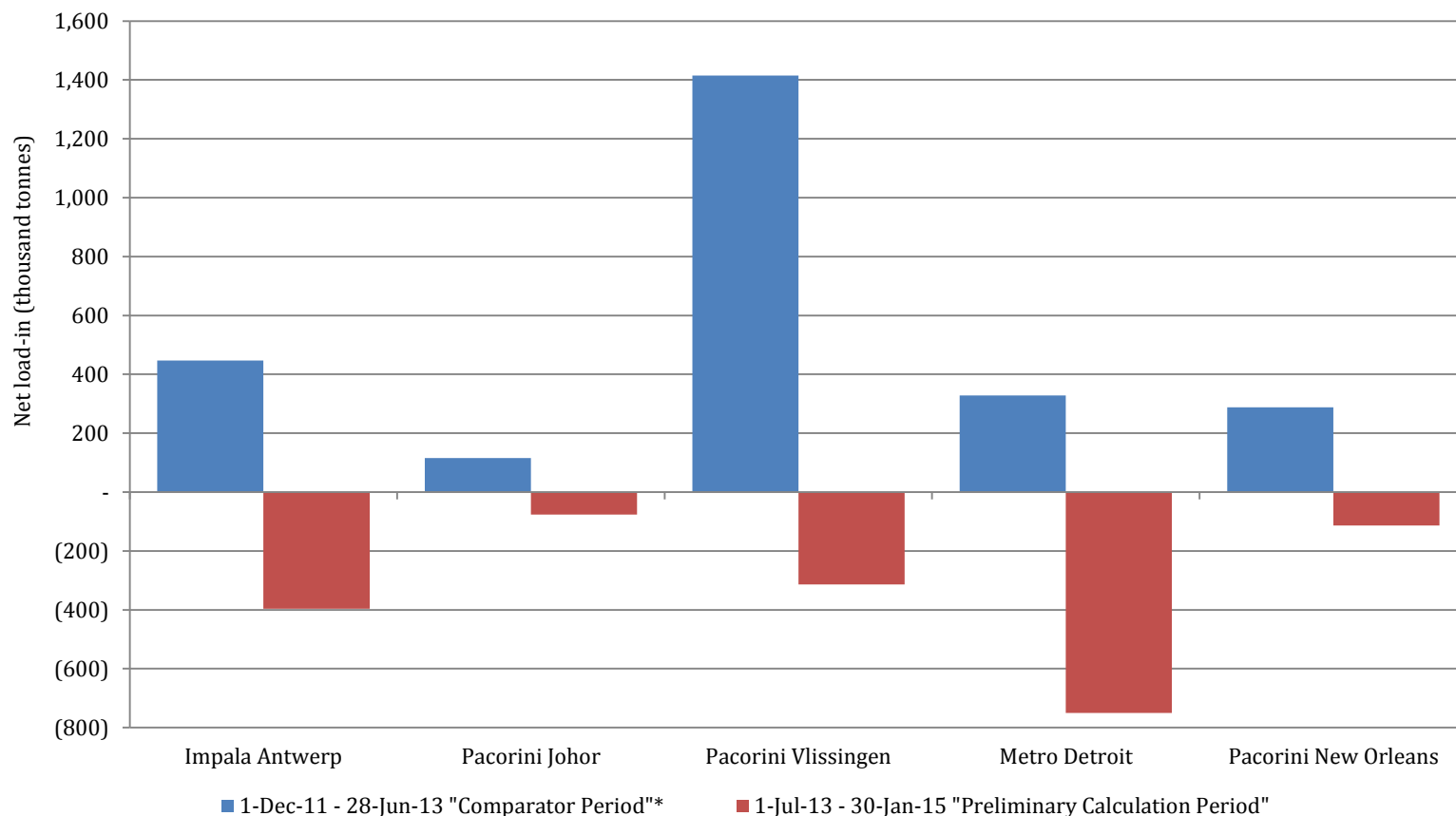
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A Load-in is falling

Pre-LILO pattern of load-out will now continue following implementation on 1-Feb-15

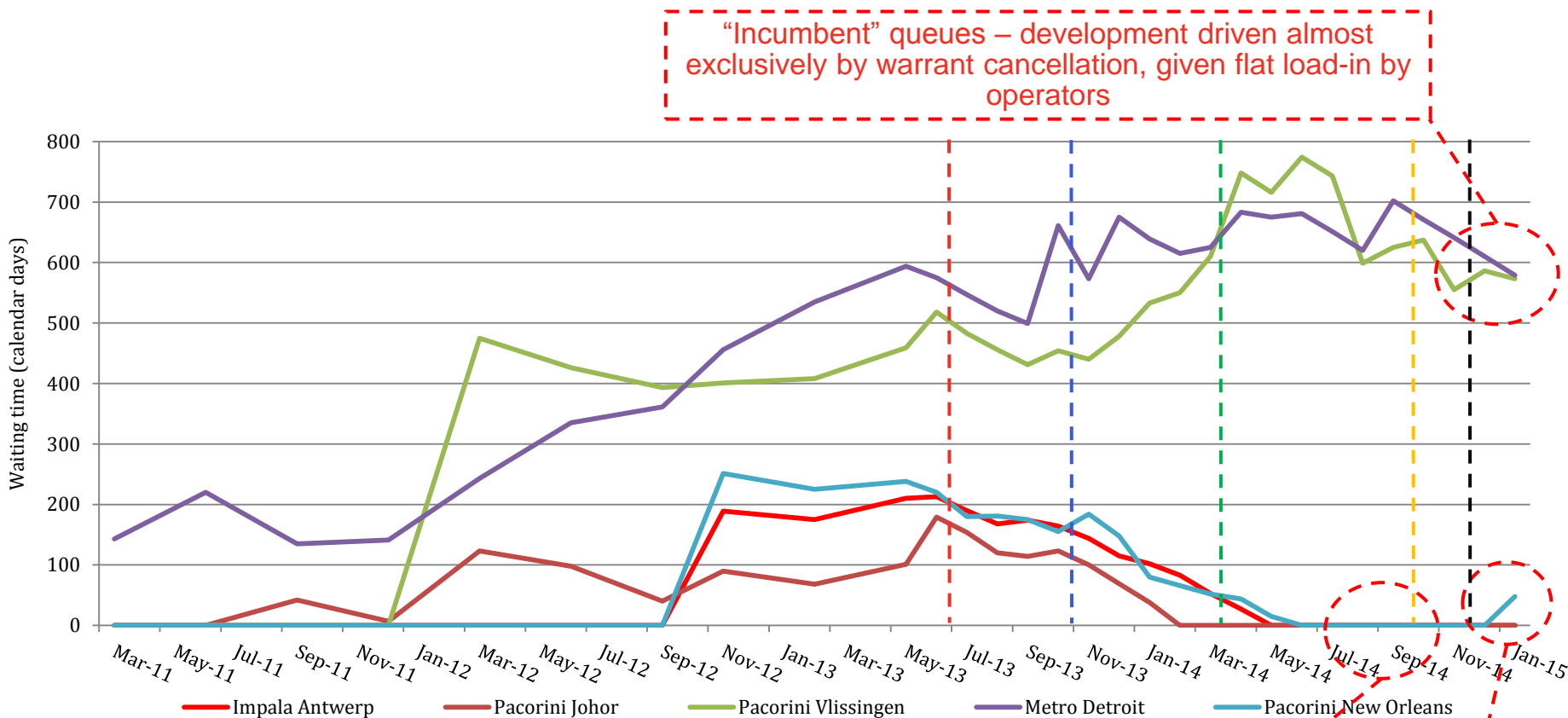
Reduced load-in during the Preliminary Calculation Period



*Comparator Period is a period of the same duration as the Preliminary Calculation Period (19 months) ending on the business day before the Preliminary Calculation Period begins

A Queue development

Cancellation represents the key driver of queues. Data as of 31-Jan-15



“Incumbent” queues – development driven almost exclusively by warrant cancellation, given flat load-in by operators

“Aspirant” queues now appear to have fallen away

“Operational queue” of 48 days has emerged at Pacorini New Orleans after a large zinc cancellation

Key:

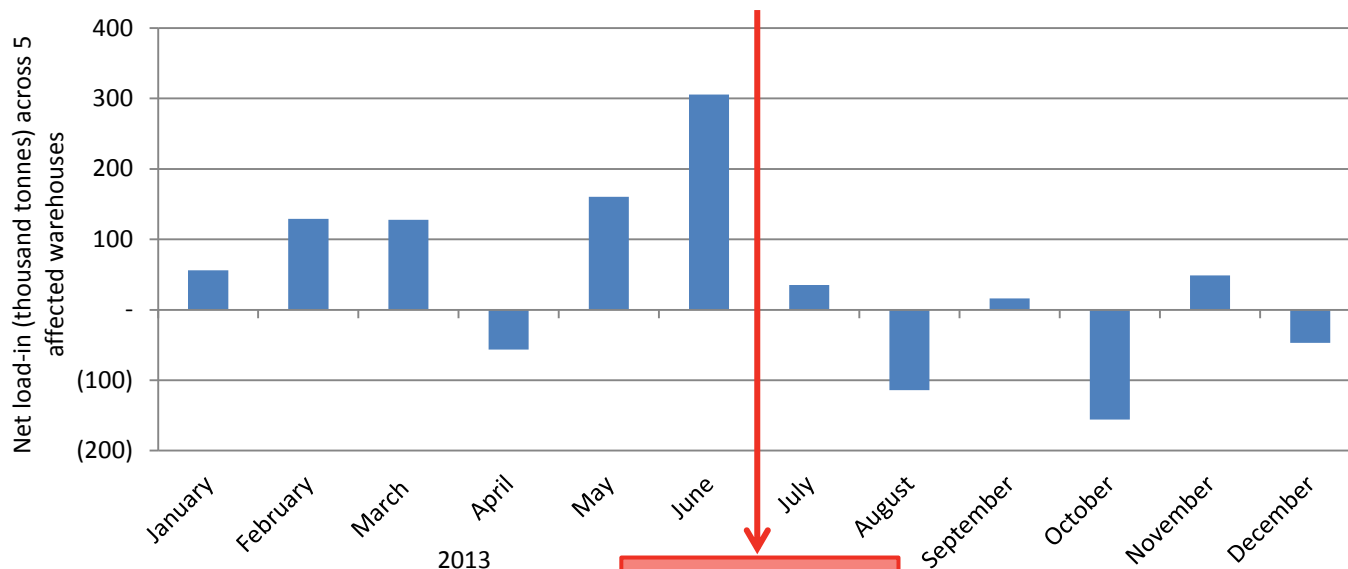
- Consultation announcement 1-Jul-13
- Decision announcement 7-Nov-13
- Initial Court Judgment 27-Mar-14
- Court of Appeal Judgment 8-Oct-14
- Supreme Court decision 17-Dec-14

A

Behavioural change driven by LILO

Clear behaviour change which has stopped stocks growing

2013 net load-in across 5 affected warehouses*



Behavioural divergence (queued vs non-queued warehouses*)

	METRO DETROIT / PACORINI VLISSINGEN	ALL OTHER LME LISTED WAREHOUSES	TOTAL
GROSS LOAD-IN 2014	541 ktonnes	1,338 ktonnes	1,879 ktonnes
GROSS LOAD-OUT 2014	1,711 ktonnes	1,729 ktonnes	3,441 ktonnes
LOAD-OUT / LOAD-IN	3.2x	1.3x	1.8x

*2013 analysis on basis of affected warehouses as at 1-Jul-13; 2014 analysis on basis of affected warehouses as at 31-Dec-14

A Decay Factor

Load-out requirement scenarios under LILO

The decay factor affects the rate at which queues are reduced under LILO (for a warehouse continuing to load in metal)

- The current decay factor (0.5x) broadly means that LILO must be in operation for two business days to eliminate one calendar day of queues¹
- The proposed increase in decay factor to 1.0x means that LILO must only be in operation for one business day to eliminate one calendar day of queues¹

DAILY GROSS LOAD-OUT REQUIREMENT¹

DAILY GROSS LOAD OUT REQUIREMENT (tonnes)												
		DAILY LOAD-IN (tonnes)										
		0	500	1,000	1,500	2,000	2,500	3,000	3,500	4,000	4,500	5,000
DECAY FACTOR	0.0	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,500	4,000	4,500	5,000
	0.1	3,000	3,050	3,100	3,150	3,200	3,250	3,300	3,800	4,300	4,800	5,300
	0.2	3,000	3,100	3,200	3,300	3,400	3,500	3,600	4,100	4,600	5,100	5,600
	0.3	3,000	3,150	3,300	3,450	3,600	3,750	3,900	4,400	4,900	5,400	5,900
	0.4	3,000	3,200	3,400	3,600	3,800	4,000	4,200	4,700	5,200	5,700	6,200
	0.5	3,000	3,250	3,500	3,750	4,000	4,250	4,500	5,000	5,500	6,000	6,500
	0.6	3,000	3,300	3,600	3,900	4,200	4,500	4,800	5,300	5,800	6,300	6,800
	0.7	3,000	3,350	3,700	4,050	4,400	4,750	5,100	5,600	6,100	6,600	7,100
	0.8	3,000	3,400	3,800	4,200	4,600	5,000	5,400	5,900	6,400	6,900	7,400
	0.9	3,000	3,450	3,900	4,350	4,800	5,250	5,700	6,200	6,700	7,200	7,700
	1.0	3,000	3,500	4,000	4,500	5,000	5,500	6,000	6,500	7,000	7,500	8,000
	1.1	3,000	3,550	4,100	4,650	5,200	5,750	6,300	6,800	7,300	7,800	8,300
	1.2	3,000	3,600	4,200	4,800	5,400	6,000	6,600	7,100	7,600	8,100	8,600
	1.3	3,000	3,650	4,300	4,950	5,600	6,250	6,900	7,400	7,900	8,400	8,900
	1.4	3,000	3,700	4,400	5,100	5,800	6,500	7,200	7,700	8,200	8,700	9,200
	1.5	3,000	3,750	4,500	5,250	6,000	6,750	7,500	8,000	8,500	9,000	9,500
	1.6	3,000	3,800	4,600	5,400	6,200	7,000	7,800	8,300	8,800	9,300	9,800
	1.7	3,000	3,850	4,700	5,550	6,400	7,250	8,100	8,600	9,100	9,600	10,100
	1.8	3,000	3,900	4,800	5,700	6,600	7,500	8,400	8,900	9,400	9,900	10,400
	1.9	3,000	3,950	4,900	5,850	6,800	7,750	8,700	9,200	9,700	10,200	10,700
2.0	3,000	4,000	5,000	6,000	7,000	8,000	9,000	9,500	10,000	10,500	11,000	

DAILY NET LOAD-OUT REQUIREMENT¹

DAILY NET LOAD OUT REQUIREMENT (tonnes)												
		DAILY LOAD-IN (tonnes)										
		0	500	1,000	1,500	2,000	2,500	3,000	3,500	4,000	4,500	5,000
DECAY FACTOR	0.0	3,000	2,500	2,000	1,500	1,000	500	0	0	0	0	0
	0.1	3,000	2,550	2,100	1,650	1,200	750	300	300	300	300	300
	0.2	3,000	2,600	2,200	1,800	1,400	1,000	600	600	600	600	600
	0.3	3,000	2,650	2,300	1,950	1,600	1,250	900	900	900	900	900
	0.4	3,000	2,700	2,400	2,100	1,800	1,500	1,200	1,200	1,200	1,200	1,200
	0.5	3,000	2,750	2,500	2,250	2,000	1,750	1,500	1,500	1,500	1,500	1,500
	0.6	3,000	2,800	2,600	2,400	2,200	2,000	1,800	1,800	1,800	1,800	1,800
	0.7	3,000	2,850	2,700	2,550	2,400	2,250	2,100	2,100	2,100	2,100	2,100
	0.8	3,000	2,900	2,800	2,700	2,600	2,500	2,400	2,400	2,400	2,400	2,400
	0.9	3,000	2,950	2,900	2,850	2,800	2,750	2,700	2,700	2,700	2,700	2,700
	1.0	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000
	1.1	3,000	3,050	3,100	3,150	3,200	3,250	3,300	3,300	3,300	3,300	3,300
	1.2	3,000	3,100	3,200	3,300	3,400	3,500	3,600	3,600	3,600	3,600	3,600
	1.3	3,000	3,150	3,300	3,450	3,600	3,750	3,900	3,900	3,900	3,900	3,900
	1.4	3,000	3,200	3,400	3,600	3,800	4,000	4,200	4,200	4,200	4,200	4,200
	1.5	3,000	3,250	3,500	3,750	4,000	4,250	4,500	4,500	4,500	4,500	4,500
	1.6	3,000	3,300	3,600	3,900	4,200	4,500	4,800	4,800	4,800	4,800	4,800
	1.7	3,000	3,350	3,700	4,050	4,400	4,750	5,100	5,100	5,100	5,100	5,100
	1.8	3,000	3,400	3,800	4,200	4,600	5,000	5,400	5,400	5,400	5,400	5,400
	1.9	3,000	3,450	3,900	4,350	4,800	5,250	5,700	5,700	5,700	5,700	5,700
	2.0	3,000	3,500	4,000	4,500	5,000	5,500	6,000	6,000	6,000	6,000	6,000

¹For simplicity, this analysis assumes that the warehouse is subject to a 3,000 tonne per day load-out requirement (top tier of the current LME load-out rules), and that other rules (such as non-dominant requirements) do not apply in this case.

A Decay Factor

Indicative queue decay profile

ESTIMATED DECAY TIME¹

<i>Time to reach 50 day queue threshold (in years)</i>	<u>Pacorini Vlissingen</u>			<u>Metro Detroit</u>		
	Upside	Mid	Downside	Upside	Mid	Downside
A. 0.5x decay factor	1.5	2.6	4.1	1.7	2.4	2.6
B. 1.0x decay factor	1.5	1.7	2.3	1.7	1.5	1.6

2-Mar-15
4 week
consultation

30-Mar-15
4 week
consideration
period following
consultation

Not later than
1-May-15²
90 days' notice of
implementation

1-Aug-15²
Implementation

¹NOTE: for important information as to modelling approach and assumptions, please see Notice 15/071 : A070 : W024

²Subject to consultation

B Commitments of Traders Report

First published on 5-Aug-14 for each day of the previous week

Delivered

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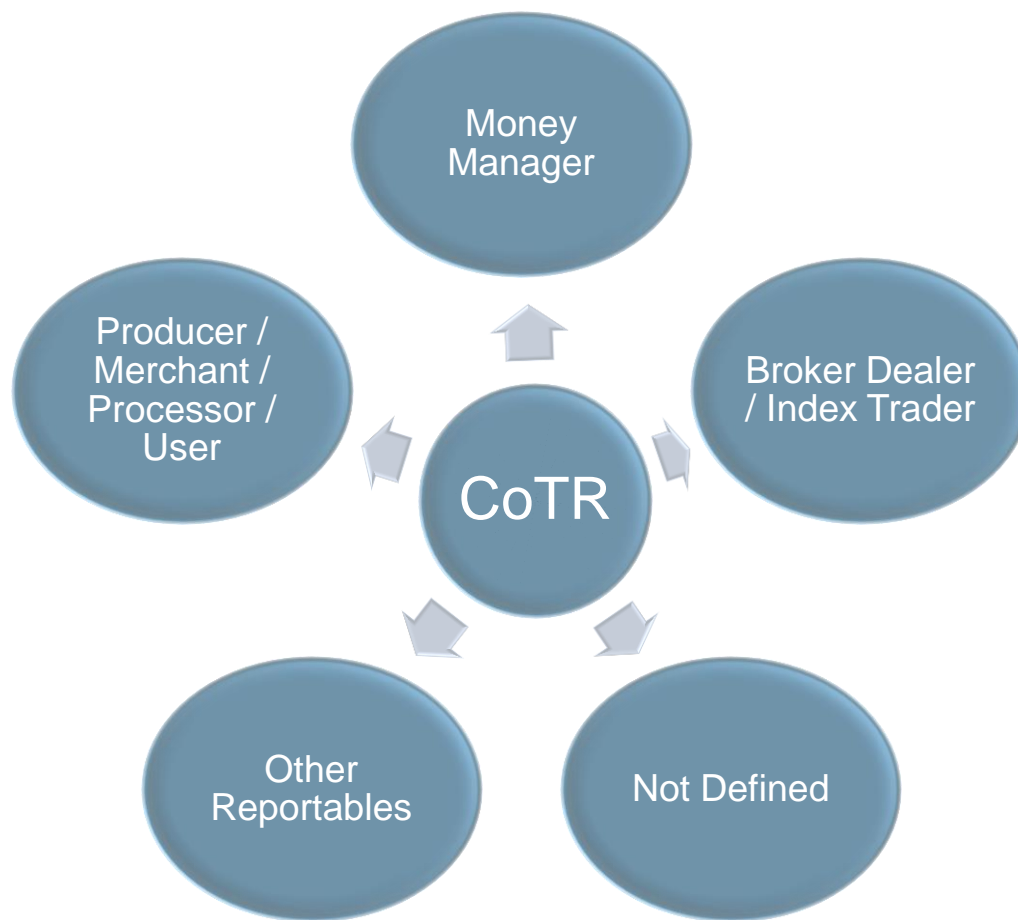
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Assess structural solutions to
high charges

Commitments of Traders Report (CoTR)

Reports designed to increase transparency as per the industry standard

COT reporting	
Frequency	Weekly
Delay	<ul style="list-style-type: none"> Each Tuesday, for the previous week's data First reports published on 5-Aug-14, for week Mon 28-Jul-14 – Fri 1-Aug-14
Information	<ul style="list-style-type: none"> 5 reports, one for each day of the previous week Breakdown of open interest in LME traded contracts Summarised following pre-defined classifications
Dissemination approach	<ul style="list-style-type: none"> Free to all users Via the LME website Via data vendors



C Publication of queues and stock data by warehouse

First published in May-14, for April-14 queue and stock data

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D Separate load-out rate for steel

Implemented on 1-Apr-14

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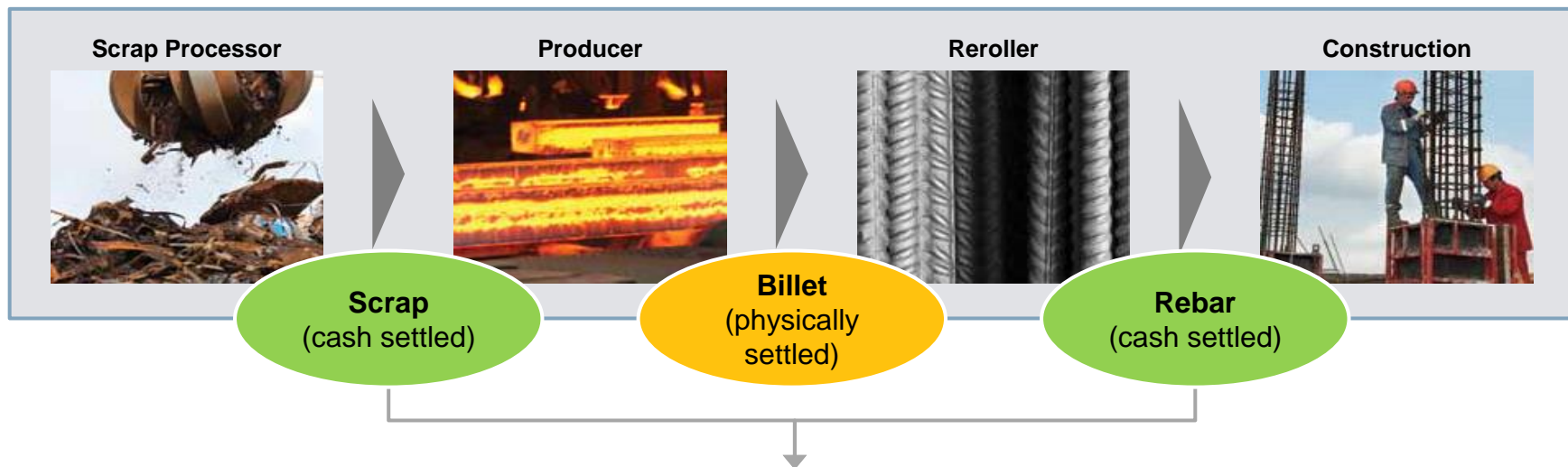
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D LME's proposed new ferrous suite

New scrap and rebar futures complete the value chain for long steel products



Underlying index base	European index prices for Scrap and Rebar – based on industry preference
Lot size	100 metric tonnes
Contract months	Monthly futures contracts going out to 15 months
Price quotation	US Dollar per metric tonne
Trading venues	Electronic and telephone
LAUNCH DATE	26 OCTOBER 2015 ¹

¹Subject to regulatory approval

E Best practice information barrier policy

Updated on 1-Jan-15 following independent review and consultation

Delivered

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F Enhanced LME investigation and action powers

For artificial queues – implemented on 1-Apr-14

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G Creation of Physical Market Committee

First meeting was in Apr-14

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H Legal review of the Warehouse Agreement

Market-wide consultation ran from 7-Nov-14 to 9-Feb-15

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Legal Review of the Warehouse Agreement

Responses were broadly supportive, two key areas of debate

- Incentive reporting
 - Anonymous reporting
 - Guidance issued on acceptable incentives
 - ✓ “Ordinary course of business”
 - x Funded by queues
 - x Funded by trading houses (but can introduce parties)
- Off-warrant stock reporting
 - No intention to publish “eligible stocks”

I Logistical Review

Market-wide consultation ran from 7-Nov-14 to 9-Feb-15

Delivered

- A LIFO Rule
- B Commitments of Traders transparency
- C Publication of queues and stock data by warehouse
- D Separate load-out rate for steel

- E Best-practice information barrier policy
- F Enhanced LME investigation and action powers for artificial queues
- G Creation of Physical Market Committee plus ongoing six-monthly reviews

Consultations ended 9-Feb-15

- H Legal review of the LME Warehouse Agreement
- I Logistical review

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I **Logistical Review**

Covered all amendments to the Policies and Procedures which govern the LME physical network

- Load-out definition
 - Generally welcomed to prevent “merry-go-round” trades
 - Physical Market Committee to consider “staging areas”
- Separate load-out rule for aluminium alloys
- Premium contract rules

J

K

Discussion Paper items

Published on 2-Mar-15 for market discussion

Delivered

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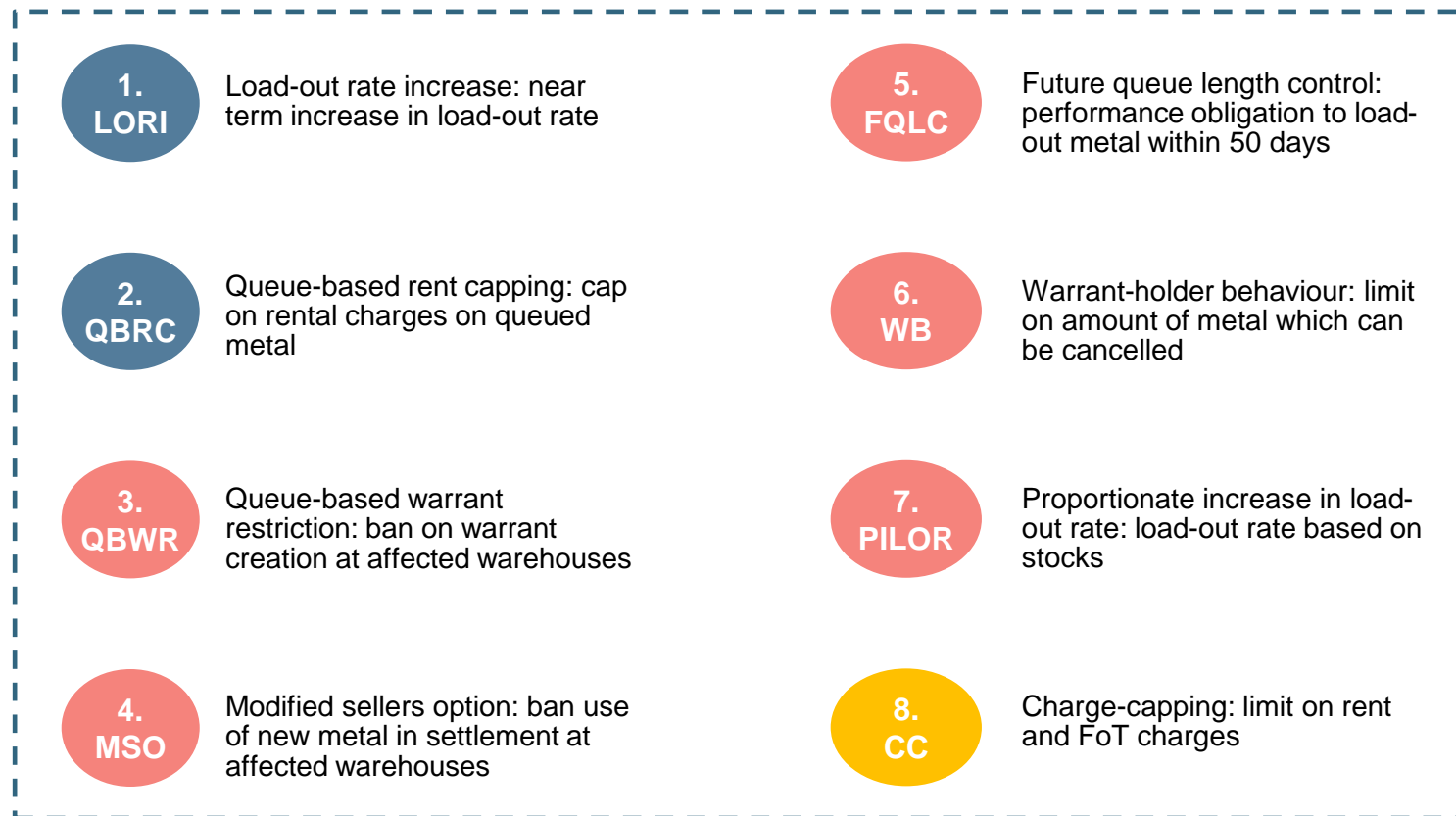
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LONDON METAL EXCHANGE

Discussion Paper

Broad set of options for market discussion



Measures to address existing queues and/or the impact of existing queues



Measures to prevent accumulation of future queues



Measures to address levels of rent and FoTs



LONDON METAL EXCHANGE

1

Load-Out Rate Increase (“LORI”)

A near term increase in the load-out rate for late-2015 or early-2016

CURRENT RULES

0 – 150,000 tonnes of metal in storage

Authorised space in sq. metres (ex steel)	Min. daily tonnage (ex cobalt, RMC & steel)
2,500	800 tonnes
5,000	1,200 tonnes
7,500	1,500 tonnes

150,000 tonnes and above of metal in storage

Tonnage stored (ex steel)	Min. daily tonnage (ex cobalt, RMC & steel)
150,000 – 299,999 tonnes	1,500 tonnes
300,000 – 599,999 tonnes	2,000 tonnes
600,000 – 899,000 tonnes	2,500 tonnes
900,00 tonnes and over	3,000 tonnes

RULES UNDER LORI

Authorised space in sq. metres (ex steel)	Min. daily tonnage (ex cobalt, RMC & steel)
2,500	800 tonnes
5,000	1,200 tonnes
7,500	1,500 tonnes

Tonnage stored (ex steel)	Min. daily tonnage (ex cobalt, RMC & steel)
150,000 – 299,999 tonnes	2,000 tonnes
300,000 – 599,999 tonnes	2,500 tonnes
600,000 – 899,000 tonnes	3,500 tonnes
900,00 tonnes and over	4,000 tonnes

Possible implementation
in late 2015, early 2016



LONDON METAL EXCHANGE

2

Queue-Based Rent Capping (“QBRC”)

Details of potential structure – potential regulatory and litigation risks

CANCELLATION



TIME IN QUEUE

0-30 days

Rent per
published
schedule

31-50 days

50% of rent as
per published
schedule

50+ days

No daily rent
charge

Possible implementation dates for i)
existing metal – early 2016 ii) future
metal – 1-Apr-18

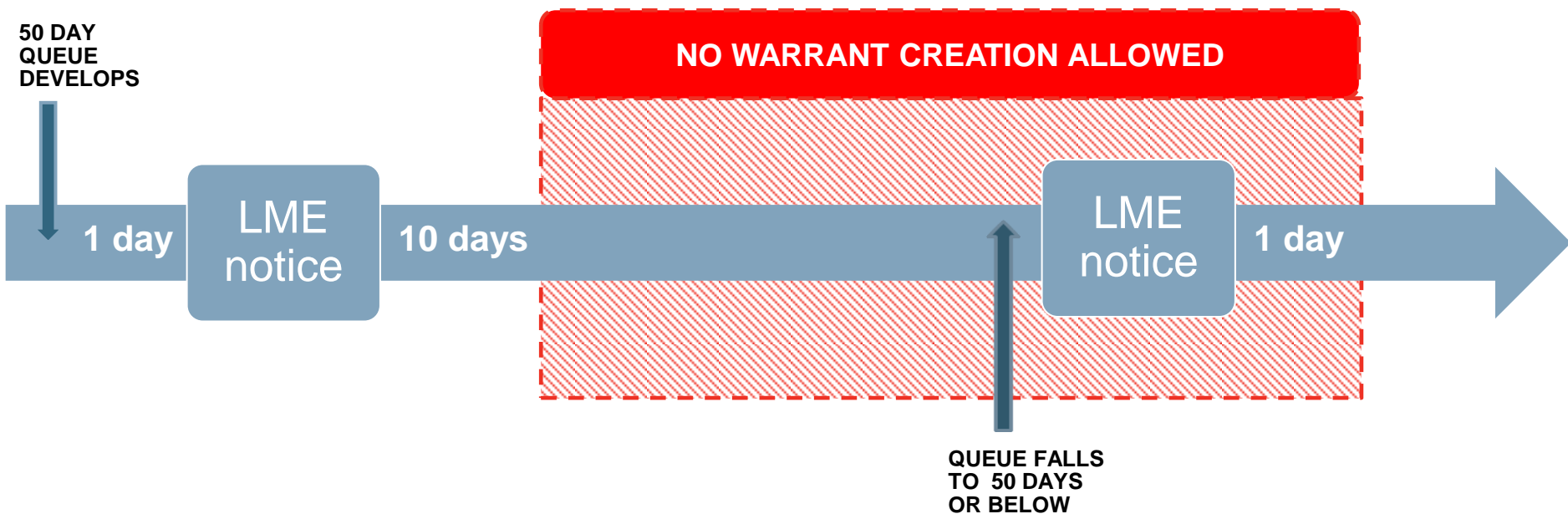


LONDON METAL EXCHANGE

3

Queue-Based Warrant Restriction (“QBWR”)

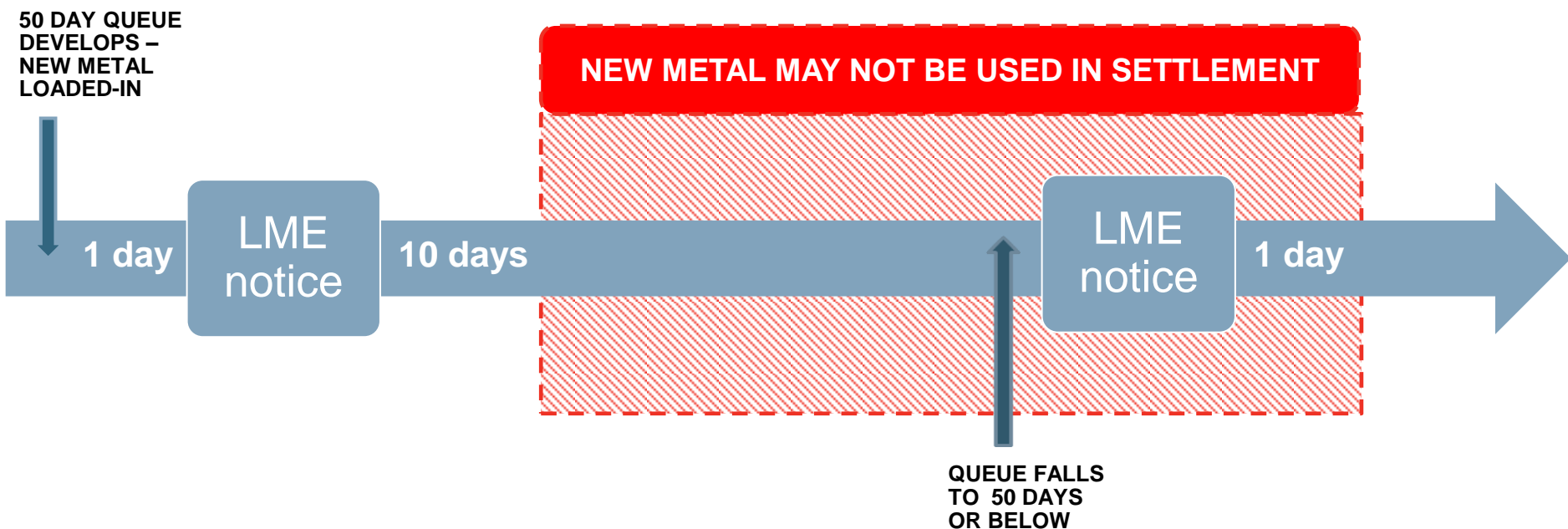
Ban warrant creation at affected warehouses with queues over 50 days



Possible implementation
1-Jan-16

4 Modified Sellers Option (“MSO”)

Ban use of new metal in settlement at warehouses with queues over 50 days



Possible implementation
1-Jan-16

Future Queue Length Control (“FQLC”)

A performance obligation on warehouses to load-out metal

The Rule

- Performance obligation for new metal only – as of 1 April 2018, all metal loaded-in since 1 April 2016 would be subject to the FQLC Rule
- Warrants must be loaded-out within 50 days of cancellation
- Warehouses failing to meet these obligations would face potential sanctions

Key points

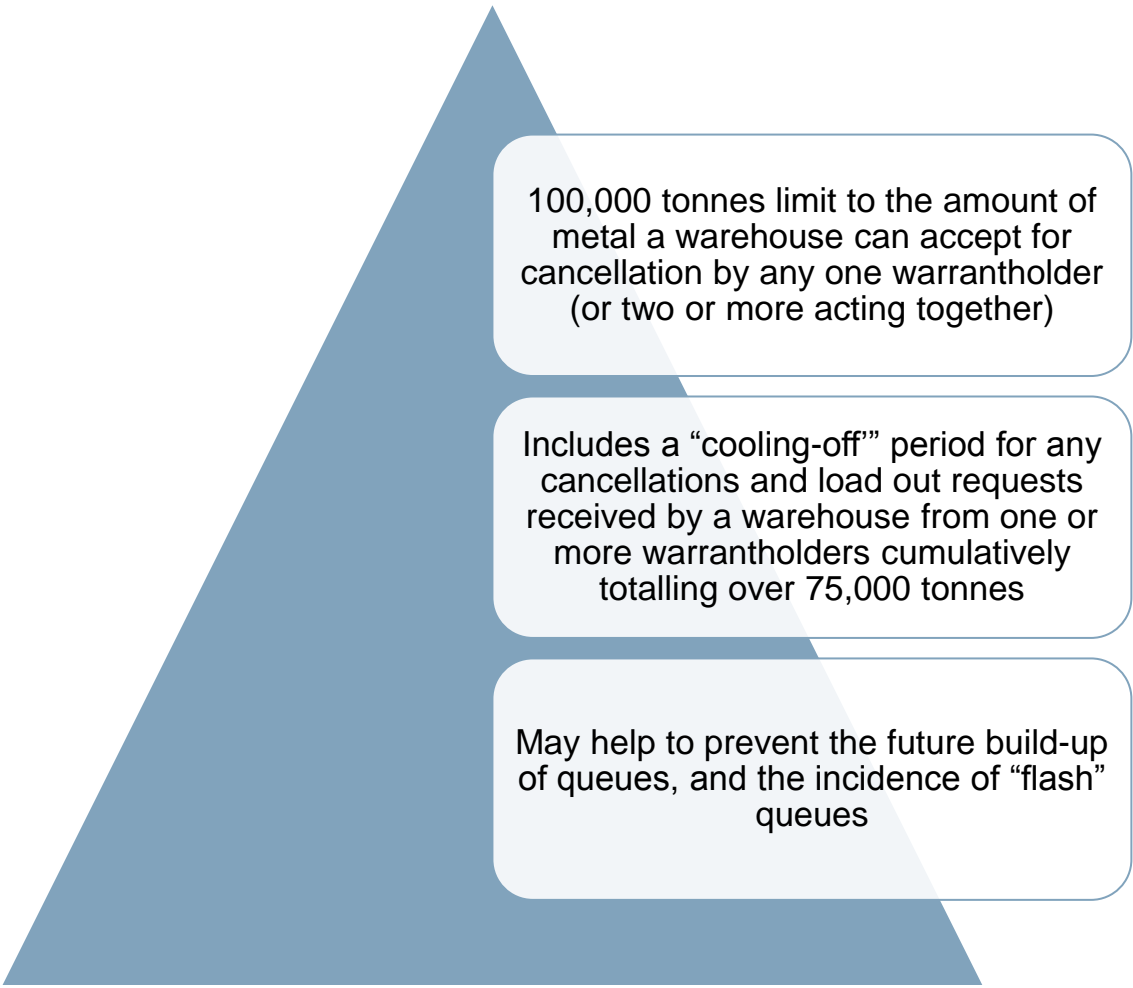
- All warrantholders would be protected by the FQLC Rule and would receive their metal within 50 days, failing which the relevant warehouse might be subject to disciplinary proceedings
- In the case of a pre-existing warehouse the FQLC Rule would be more incremental – as new metal is loaded-in and older metal is loaded-out, then the balance of metal in the warehouse would shift towards new metal, and hence eligible for the protections afforded by the FQLC Performance Obligation

Possible implementation
1-Apr-18

6

Warrant-holder behaviour (“WB”)

Designed to limit the impact of warrant-holders on the creation and / or elongation of queues



100,000 tonnes limit to the amount of metal a warehouse can accept for cancellation by any one warrant-holder (or two or more acting together)

Includes a “cooling-off” period for any cancellations and load out requests received by a warehouse from one or more warrant-holders cumulatively totalling over 75,000 tonnes

May help to prevent the future build-up of queues, and the incidence of “flash” queues

Possible implementation
1-Jan-16



LONDON METAL EXCHANGE

7 Proportionate Increase in Load-Out Rate (“PIJOR”)

A proportionate load-out rate increase based on stock levels

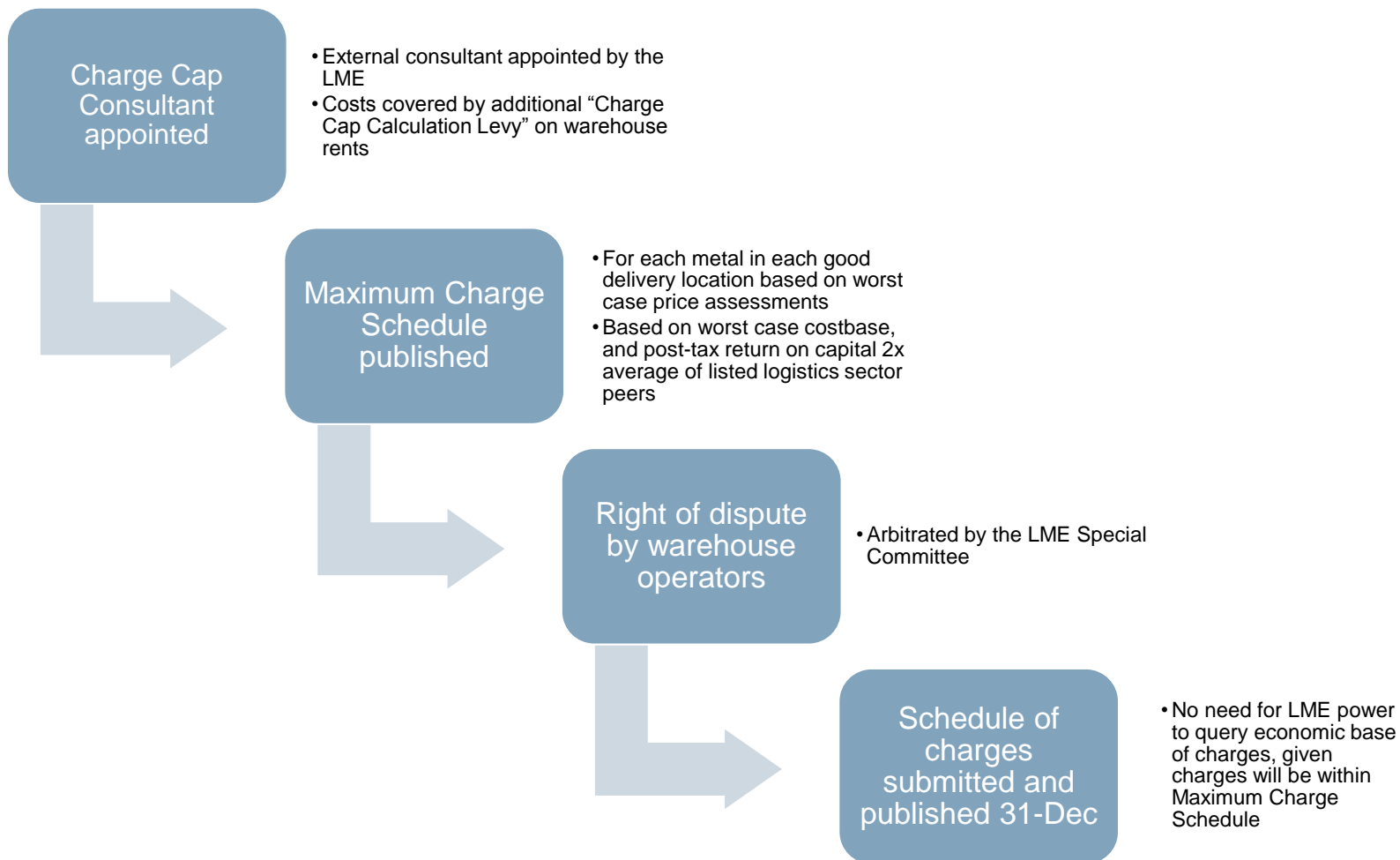
TOTAL STOCK (tonnes)	DAILY MINIMUM LOAD-OUT RATE (tonnes)
100,000 – 199,999	2,000
200,000 – 299,999	3,000
300,000 – 399,999	4,000
400,000 – 499,999	5,000
500,000 – 599,999	6,000
600,000 – 699,999	7,000
700,000 – 799,999	8,000
800,000 – 899,999	9,000
900,000 +	10,000

Possible implementation
1-Apr-18

8

Charge-Capping (“CC”)

Details of potential structure – potential regulatory and litigation risks



Possible implementation
1-Oct-16

L Premium contracts

Ready to launch once discussion paper has been considered by the market

Delivered

A

LILO Rule

B

Commitments of Traders transparency

C

Publication of queues and stock data
by warehouse

D

Separate load-out rate for steel

E

Best-practice information barrier policy

F

Enhanced LME investigation and
action powers for artificial queues

G

Creation of Physical Market Committee
plus ongoing six-monthly reviews

Consultations
ended 9-Feb-15

H

Legal review of the LME
Warehouse Agreement

I

Logistical review

L

Premium contracts (rule changes to
facilitate premium hedging solutions)

Discussion
Paper

J

Assess powers to limit rents in queues
as a future policy option

K

Assess structural solutions to
high charges

Proposed new aluminium contract suite

LME's leading global aluminium contract will be supplemented with four proposed regional premium contracts

LME's new aluminium contract suite



**GLOBAL
LME ALUMINIUM**

Warehouse reform programme

Premium contracts

- 1 Four regional contracts covering the key centres of aluminium demand
- 2 Hedging of regional all-in price of aluminium
- 3 Physical delivery of readily available metal in Premium Warehouses
- 4 Monthly contract to concentrate liquidity

Physical premium contract specifications

Specifications for the LME Premium Futures Contracts

Contract specification	Description			
Contract names	LME US Aluminium Premium	LME Western Europe Aluminium Premium	LME Eastern Asia Aluminium Premium	LME South-Eastern Asia Aluminium Premium
Regions	Midwest, Northeast and South US regions (as per US Census Bureau)	Western Europe (as per UN Geoscheme M49 classification)	Eastern Asia (as per UN Geoscheme M49 classification)	South-Eastern Asia (as per UN Geoscheme M49 classification)
Underlying metal	High grade primary aluminium premium warrant in the designated region			
Lot size	25 tonnes			
Prompt dates	Third Wednesday of each maturity month, subject to trading regulations			
Maturity months	Monthly out to 15 months			
Price quotation	US dollars per tonne			
Clearable currencies	US dollar			
Position limits	An appropriate position management regime will be implemented			
Minimum price fluctuation (tick size) per tonne	<div><div>Tick sizes to follow the main LME Aluminium contract:</div><div><div><div>Outrights</div><div>Ring: \$0.50</div><div>LMeselect: \$0.25</div><div>Inter-office: \$0.01</div></div><div><div>Carries</div><div>Ring: \$0.01</div><div>LMeselect: \$0.01</div><div>Inter-office: \$0.01</div></div></div></div>			
Last trading day and time	By 12.30 (London local time) two business days before the third Wednesday of the contract month trading in the expiring contract			
Settlement type	Physically delivered <i>Seller provides:</i> LME aluminium premium warrant in the designated region <i>Buyer provides:</i> Any LME aluminium warrant, PLUS the Premium cash as agreed at contract formation, LESS the premium aluminium FOT charge at the warehouse where the LME aluminium premium warrant is delivered			
Trading venues	Ring, LMeselect, inter-office telephone			
Trading hours	Ring: 5 minutes for all regions at end of Ring 2 for Official Prices and Afternoon Kerb for Closing Prices LMeselect: 01:00 – 19:00 London local time Inter-office: 24 hours a day			
Margining	Initial and contingent variation margins applied per LME Clear risk management parameters			

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*Subject to regulatory approval

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<http://www.lme.com/trading/warehousing-and-brands/warehousing/warehouse-consultation/>

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