Contracts for Difference (CFDs)

Daily margined exposure to blue-chip shares

What are CFDs?

- An agreement between a buyer and seller to exchange the difference in price of an underlying instrument over a period of time
- Leveraged exposure to shares
- No maturity or expiry date
- No automatic physical settlement
- Trade OTC (off-exchange)
- Linear price relationship to underlying shares
- Client places margin ahead of trading on a leveraged basis in shares
- Geared instrument

Features of CFDs

- Low cost market exposure
- Real-time position management
- Wholesale lending and deposit rates
- Robust, system-based trading
- Simple pricing methodology
- Daily and monthly automated statements

Buy Long - Pricing Example (BIL)

Assumptions (Stock: BHP Billiton Ltd "BIL")

- Lending rate: 7%; Deposit rate 5%; Stock borrow 0.50%
- Trading fee: Indicative all-in to Broker Client 35 bps (0.35%); Investec to take only a fraction of this
- Investec required margin: 10%

Day 1

Buy 1000 CFD at 27500; closes at 27800 that night

1. Execution fee:
   (R275.00 x 1000 x 0.35%)
   = - R962.50
2. MTM Gain:
   (R278.00 - R275.00) x1000
   = + R3000
3. Margin required to be held:
   (R278.00 x 1000) x 10%
   R27,800.00

Daily gain: + R2,037.50

Day 2

MTM gain: 285.00

1. Funding charge:
   7% x (1000 x R278.00) x 1/365
   = - R53.32
2. MTM Gain:
   (R285.00 - R278.00) x 1000
   = + R7000.00
3. Margin required to be held:
   (R285.00 x 1000) x 10%
   = R28,500.00

Daily gain: + R6,946.68

Day 3

Sell 1000 CFD at 2800

1. Funding charge:
   7% x (1000 x R285.00) x 1/365
   = - R54.66
2. Execution fee:
   (R280.00 x 1000 x 0.35%)
   = - R980.00
3. MTM loss:
   (R280.00 - R285.00) x 1000
   = - R5000.00

Daily loss: - R6,034.66

Overall: + R2,949.52

Sell Short - Pricing Example (MTN)

Assumptions (Stock: MTN Ltd "MTN")

- Lending rate: 7%; Deposit rate 5%; Stock borrow 0.50%
- Trading fee: 35 bps (0.35%)
- Investec required margin: 12%

Day 1

Sell 1000 CFD at 13000; closes at 13200 that night

1. Execution fee:
   (R130.00 x 1000 x 0.35%)
   = - R455.00
2. MTM loss:
   (R130.00 - R132.00) x1000
   = - R2000
3. Margin required to be held:
   (R132.00 x 1000) x 12%
   R15,840.00

Daily loss: - R2,455

Day 2

No trade; MTN closes 12750

1. Funding earned:
   (5% - 0.50%) x (1000 x R132.00) x 1/365
   = + R16.27
2. MTM gain:
   (R132.00 - R127.50) x 1000
   = + R4,500.00
3. Margin required to be held:
   (R127.50 x 1000) x 12%
   = R15,300.00

Daily gain: + R4,516.27

Day 3

Buy 1000 CFD at 13500

1. Funding earned:
   (5% - 0.50%) x (1000 x R127.50) x 1/365
   = + R15.72
2. Execution fee:
   (R135.00 x 1000 x 0.35%)
   = - R472.50
3. MTM loss:
   (R127.50 - R135.00) x 1000
   = - R7,500.00

Daily loss: - R7,956.78

Overall: - R5,895.51

Why trade CFDs?

- Cost-effective alternative to share trading
- Long/short strategies executed easily and reporting generated automatically
- Each underlying trade executed in price/time priority on the JSE Central Order Book
- Linear link to underlying share price
- Direct market access (DMA) platform available, with full ED desk support
- Low-cost gearing to the market (no Securities Transfer Tax under current legislation)
- Dividends flow to and from margin accounts
- Full transparency on pricing

The risks?

- High-risk trading instruments
- Interest rate is variable (linked to repo/prime/Safey)
- Direct credit risk between client and Investec Bank Ltd (no exchange involved)
- Automatic close-out on non-payment of margin
- Be aware of the dividend and corporate action effects on margin account

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