BCS
Canada Bank
Credit Futures

MONTRÉAL EXCHANGE

FTSE Canada Bank Credit Index Futures (BCS) trading: Long vs. Short Credit

Let's illustrate a hypothetical trade involving a trade in BCS.

The price of the Futures contract is calculated as **100 - FTSE Canada Bank Credit Spread Index**.

Per the above quotation,the futures price reflects an inverse price/spread relationship: A higher price means a tighter credit spread index and a lower perceived credit risk (stronger credit). Conversely, a lower price means a wider credit spread index and higher perceived credit risk (weaker credit).

Scenario

A FTSE Canada Bank Credit Index Futures has a current price of $99.13. Each tick movement is 0.005, representing $25 per contract. This implies that 1 point (or $1) of price movement is worth $5,000 per contract. The dollar value of a 1 basis point movement in the underlying credit spread (CS01) is considered constant at $50.

1. Trader A Goes Long (Buys) the Futures

Position: Trader A believes that credit quality will improve (i.e., perceived credit risk will decrease) in the Canadian corporate bond market. This means they are long credit. They expect the FTSE Credit Spread Index to decrease and the futures price to rise.

Action: Trader A buys one futures contract at $99.13.

2. Trader B Goes Short (Sells) the Futures

Position: Trader B believes that credit quality will deteriorate (i.e., perceived credit risk will increase) in the Canadian corporate bond market. This means they are short credit. They expect the FTSE Credit Spread Index to increase and the futures price to fall.

Action: Trader B sells one futures contract at $99.13.

How Price Moves and its Impact

Let's consider two possible outcomes after a week:

Outcome 1: Credit Quality Improves (Price Rises)

Due to positive economic news and strong corporate earnings, the perceived credit risk in the manager’s basket of Canada corporate bonds decreases. The FTSE Credit Futures price rises to $99.1450.

Trader A (Long):

Bought at $99.13, value is now $99.1450.

Profit: 0.015 points. If 1 point is $5,000 (0.005 is $25), then profit is 0.015 * ($5,000/point) = $75.

Trader A's long position has gained value as they were "long credit" and credit improved.

Trader B (Short):

Sold at $99.13 value is now $99.1450.

Loss: 0.015 points. Loss is 0.015 * ($5,000/point) = $75.

Trader B's short position has lost value as they were "short credit" and credit improved.

Outcome 2: Credit Quality Deteriorates (Price Falls)

Due to concerns about a potential recession and corporate defaults, the perceived credit risk in the manager’s basket of Canada corporate bonds increases. The FTSE Credit Futures price falls to $99.06.

Trader A (Long):

Bought at $99.13, value is now $99.06.

Loss: 0.07 points. Loss is 0.07 * ($5,000/point) = $350.

Trader A's long position has lost value as they were "long credit" and credit deteriorated.

Trader B (Short):

Sold at $99.13, value is now $99.06.

Profit: 0.07 points. Profit is 0.07 * ($5,000/point) = $350.

Trader B's short position has gained value as they were "short credit" and credit deteriorated.

The following table summarizes potential P&L variations following Index spread moves:

	SCENARIOS	Futures price: 100 - credit Index (expressed in % - so it's the Index / 100) Multiplier: $5,000 Tick size: 0.005 = 25$		
	FTSE CREDIT SPREAD INDEX	**BCS CONTRACT PRICE**	**BCS MARKET VALUE**	**P&L OF LONG POSITION**
Day 1	87.00	$99.1300	$495,650	
Day 2	88.50	$99.1150	$495,575	-$75
Day 3	94.00	$99.0600	$495,300	-$275
Day 4	87.50	$99.1250	$495,625	$325
Day 5	85.50	$99.1450	$495,725	$100
Day 6	92.00	$99.0800	$495,400	-$325

What "Long Credit" and "Short Credit" Mean

Long Credit: You are "long credit" when you benefit from improving credit quality or decreasing credit risk. In the context of these futures, this means you expect the price of the futures to rise. This is analogous to selling protection in the CDX market.

Short Credit: You are "short credit" when you benefit from deteriorating credit quality or increasing credit risk. In the context of these futures, this means you expect the price of the futures to fall. This is analogous to buying protection in the CDX market.

Considering the significance of the Canadian bank bond basket underlying the Index and its correlation with the Canadian corporate bond Sector, the Index serves as a strong proxy for Canada's corporate bond and financial bond sectors, with comparable levels of volatility.

Overall, FTSE Canada Bank Credit Index Futures provide a transparent and efficient way to take a directional view on the credit health of a basket of Canadian corporations, allowing market participants to manage or express opinions on credit risk without directly interacting with the less Canadian-specific CDX market.

More information about FTSE Canada Bank Credit Spread Index can be found here.

Additional details regarding the Futures contract are accessible on MX landing page.

For more information

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