

Innovating with Gold: How DGCX worked with FinMet to support market participants?



As market conditions continue to fuel a liquidity crunch globally, DGCX developed innovative gold repo products to support short-term liquidity requirement for its members.

Global markets are facing unprecedented challenges with rising inflation and interest rates combined with a looming recession. With the volatile economic backdrop, commodities traders are facing problems of their own. One of them is more crucial than others and something every trader in the world faces – liquidity tightening.

At DGCX, the region's largest derivatives exchange in the Middle East and working with participants to create the UAE gold pricing benchmark in the region, gold traders were facing similar challenges with liquidity. With a comprehensive market infrastructure including the Exchange, Clearinghouse, DMCC Trade Flow and approved vaults, DGCX decided to act on it.

"We understood that market participants have a low tolerance for counterparty credit risk, market risk and integrity risk of kilobars. We had to structure products that would mitigate these risks," says Sudhan Sundaram, Head of Products at DGCX. DGCX partnered with FinMet, a precious metals technology trading, training, and logistics provider, and identified the crucial role physical gold could play for traders. Global banks have lent against physical gold to support traders with working capital for decades, however, local banks were not offering options to provide such short-term hedging and economic viability for gold bullion, even though Dubai has an active physical gold kilobar market. This meant capital deployed by traders to hold physical gold inventory could not be used to access funds.

"Local Banks are willing to facilitate the transactions to support jewelry wholesalers, retailers, and manufacturers for working capital but are uncomfortable dealing in physical gold bar inventories held by refiners and traders. With approved vaults and the creation of electronic warrants in the DMCC trade flow system, the banks' concerns could be addressed," Tymoor Khan, Head of Global Sales at DGCX.

After intensive research, benchmarking, and receiving feedback from the largest banks and bullion traders in the region, DGCX created two new products – a Spot Gold contract and Physical Gold Futures, to be used together to facilitate the trade.

A bullion trader can sell the Spot Gold contract to get access to funds with its physical gold inventory stored at DGCX-approved vaults as collateral. At the same time, the trader will buy Physical Gold Future to be delivered on the 10th, 20th or 30th of every month.

A bank can do the opposite trade, i.e., buy the Spot Gold Contract and provide funds to a bullion trader and sell the Physical Gold Futures contract to ensure that it gets its funds back. As with all trades on DGCX, the DGCX Clearinghouse acts as the central counterparty to the transactions to ensure the transaction is done securely and with low risk.

The first transaction was successfully completed between DGCX member, Paloma Precious DMCC, and one of the most reputable banks in the UAE as it became the first trader to benefit from access to short term liquidity using the newly launched products. It also opens up the opportunity for other bullion traders in the region to access short term liquidity and banks to offer low risk credit facilities, facilitating the growth of market participants on both sides.

"As DGCX, we offer an ecosystem for market participants to develop and achieve their business objectives. The two products fill an extremely crucial void that was present in the local markets for decades, thanks to our culture of continuous innovation for the benefit of market participants. For us, the question is always the same – how to collaborate and innovate for the benefit of the market?" says Louis Hems, Commercial Director at DGCX.

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