

Do you have any comments or concerns on the proposed risk management arrangements?

The HKEX rejected the Derivatives Market Consultative Panel's proposal to skip the proposed mandatory market open variation adjustment (VA) and margin call. Hence, under the current proposed arrangement, clearing participants will be subjected to VA and margin calls twice in the morning, once at 9.15 am and the latter at 11.00 am. The rationale behind the additional mandatory call is to collect the margins for the new positions established during the T+1 session and to conform to risk management practices adopted by overseas clearinghouses. But it is worth pointing out that clearinghouses have different methodologies of calculating margin requirements and risk management frameworks. Those that do not operate mandatory intra-day margin calls may have higher initial margin requirements and other more stringent risk control measures than those international clearinghouses that do. A comprehensive review is recommended lest we end up with a prudent but inefficient framework requiring excessive level of margin.

Suggestion: The HKEX can still manage its risk prudently and achieve its objective by combining the two separate VA and margin calls into one and based the calculation on the latest positions of its clearing participants and the closing prices at the end of the T+1 session. HKEX can still trigger ad-hoc market open or intra-day call when necessary. Exchange and clearing participants would welcome the streamlined process and some of the cost savings thereof. Moreover, the above suggestion is an improvement over the existing risk management arrangement that had withstood the test of time.

Are there any other issues regarding the Proposal that HKEx should consider?

According to the consultation paper, the volume of after hours trading in the major overseas stock index futures amounted to 15% to 37% of the volume in their respective day sessions. The median is about 20% and using the market share as a proxy for the number of investors, only 20% of the daytime investors will be participating in the T+1 session. This number would be lower initially. Firstly the volume would take time to build up, secondly, there are fewer EPs participating and some investors will not be able to participate in the night session and finally, even for those who can, it is envisaged some, especially the individual investors, may not want to participate when the cash market is not open and the underlying Hang Seng indices are not available.

HKEX expect the after-hours futures trading to attract more European and US investors, most of which are likely to be institutional investors, to participate in its futures market both during and after their working hours. These institutional investors would likely have access to the live prices of some of the constituent stocks traded in overseas markets and the ability to calculate the underlying indices of the traded futures. This may put our local investors at a competitive disadvantage.

Suggestion: HKEX may want to consider providing some reference indices to the traded futures, similar to the Hang Seng London reference index, and if possible but I doubt it, the live prices of the constituent stocks traded in overseas markets. This initiative should level the playing field for individual investors and provide them with more information to trade in the T+1 session more confidently.

What are the concerns of the majority of those investors who would not or could not participate in the T+1 session? It is recognized and even mentioned in the consultation paper that in the build up of trading liquidity, there may be periods of low liquidity where volatility may increase. While steps and system enhancements have been taken not to exacerbate volatility such as fill-or-kill orders and fill-and-kill orders will not be applicable during the T+1 session and a new dynamic price banding mechanism will be introduced to reduce the potential impact of a sequence of error trades, there are concerns among investors, especially 80% of those investors who would not be participating in the T+1 session, how flash crashes that happen in overseas markets affect the HK market during the T+1 session and whether their positions will be forcibly closed out.

Suggestion: To allay such fear and prevent market whipsaw, it may be worth considering, in addition to the measures taken, for the HKEX to have limit up/down trading restrictions, similar to what we have years ago, until liquidity builds up.