

# CHATROOM

## **Chief Operating Officer Gerald Greiner Shares His Views on Some Key Market Issues**

**G**erald Greiner became HKEx's Chief Operating Officer in February of this year after serving as Deputy Chief Operating Officer (DCOO) for more than two-and-a-half years. Before joining HKEx as DCOO, he held senior executive positions at Hong Kong's Securities and Futures Commission between 1989 and 2004 and the US Securities and Exchange Commission from 1984 to 1989. Mr Greiner has degrees in economics and law from universities in the US.

### **How do your responsibilities differ from your responsibilities when you were Deputy Chief Operating Officer?**

The difference is I am now responsible for the Clearing Division, Risk Management Department and Information Services Department in addition to being responsible for the Cash Market Department, Derivatives Market Department and Participant Admission & Surveillance Department. The last three used to comprise the Exchange Division and reported to the Deputy Chief Operating Officer, who was also Head of the Exchange Division. The Exchange Division was removed from the organisation structure in February thus eliminating one senior executive position and the related cost.

I also wish to mention that we are restructuring our risk management functions. To centralise and strengthen risk management and eliminate overlapping responsibilities, we are combining Cash Clearing Risk Management, Derivatives Clearing Risk





Management, Market Surveillance, Participant Surveillance and the existing Risk Management Department into a new Risk Management Division. We are now recruiting a Head for the new division who will become the seventh member of our Senior Management Committee.

***What were the most significant developments in HKEx's secondary market activities over the last few years?***

Big increases in turnover in the cash (or securities) and derivatives markets have been a highlight of the last few years and in particular in recent months.

Average daily turnover in the cash market increased from \$18.3 billion in 2005 to \$33.9 billion in 2006 and \$59.2 billion through the end of June this year. New records are being set often with a recent day of over \$120 billion. Average daily futures and options turnover increased from over 103,000 contracts in 2005 to over 173,000 contracts in 2006 and over 276,000 contracts through the end of June. Open interest has also been setting new records frequently.

Other developments have included the rise of turnover in the warrants market to often more than 20 per cent of total cash market turnover. Amongst our Exchange Participants there has been significant growth in the bank-based Internet trading services for retail investors. All these developments coincide with Mainland enterprises becoming the dominant force in HKEx's primary and secondary markets.

***What is the status of some of your group's ongoing projects?***

A number of important market developments are due for implementation by the end of this year or early next. Third-Party Clearing in the cash market will enable existing or new Exchange Participants who wish to do so to outsource their clearing and back office functions to specialty clearing firms.

A closing auction session for the cash market, similar to the pre-opening session, will be available from 4:00 pm to 4:10 pm. The so-called "tick rule" restricting when short sales can be executed will be suspended, subject to the possibility of reinstatement in extreme circumstances as directed by the SFC (Securities and Futures Commission).

***What, in your view, would the likely prospects be for Hong Kong trading of futures and options on commodities and emissions-related products?***

As mentioned in our Strategic Plan for 2007 to 2009 we will this year work with consultants to analyse the potential for trading of commodities and or emissions-related products in Hong Kong. Emissions-related trading is interesting to me as it is at a relatively early stage of development internationally – and particularly in Asia – whilst climate change has become an accepted fact and governments and affected businesses are beginning to take more meaningful actions to address the problem. This is likely to create new business potential in the medium term.



***How would you describe HKEx's market infrastructure? Where is there the most room for further improvement?***

I would describe HKEx as having a full-service equity marketplace including primary and secondary equity markets, a good variety of equity derivatives, central counterparty clearing, stock borrowing and lending to support short selling, good retail and institutional investor participation, and readily available financing. Each part contributes liquidity to the whole and that liquidity attracts additional liquidity. We need to continuously assess and improve market operations including in relation to capacity, efficiency, cost, and transparency. HKEx is also supported by all the other necessary service infrastructure in Hong Kong including

bankers, lawyers, accountants, analysts, registrars, information vendors, company secretaries, IT providers, etc.

It is also true that we trade very little outside of our equities cash and derivatives markets. We have some modest trading in interest rate products and no trading in commodities or currencies other than a few structured products. We recently consulted the market on a renminbi/US dollar futures contract but found opposition to its launch at this time. As mentioned earlier, we will take a close look at the potential opportunities in commodities markets with the help of consultants.

***What are your views on algorithmic trading? Is HKEx seeing much now and is it ready for increased algorithmic trading in Hong Kong if the market moves in that direction?***

Algorithmic trading is here and likely here to stay. We are in the process of considering a series of initiatives to support this business. These include enhanced market data services, direct market access, remote Exchange Participants, and facilitating hosting of Participants' technology. We are upgrading overall system capacity which will increase speed – also known as reducing latency – which is very important to algorithmic traders. Medium term we must make more fundamental changes to our AMS/3 system to meet the increasing demands of our customers. (AMS/3, the Third Generation Automatic Order Matching and Execution System, is the HKEx securities market's electronic trading system.)



**What is the likely impact in Asia of the US's Regulation NMS\*, which is designed to ensure an investor's order is sent to the market where he'll get the best price, and Europe's Markets in Financial Instruments Directive, or MiFID\*, which is expected to result in new competition for Europe's established exchanges?**

We are fortunate to be able to operate a central marketplace that is fair and transparent and not currently complicated by so-called ECNs (electronic communications networks), multiple competing exchanges, payment for order flow, opaque pricing, routine bad execution, etc. When new types of competing markets do come to Hong Kong the SFC already has Guidelines for Automated Trading Systems that should require appropriate levels of fairness, transparency, best execution, investor protection and compensation arrangements, and payment of regulatory costs. As I see it the US and Europe are trying to impose appropriate standards after the fact and a by-product of Reg NMS and MiFID will be high compliance costs for their markets and market participants.

\* Regulation NMS is a series of initiatives designed to modernise and strengthen the national market system in the US for equity securities. It includes: (1) Rule 610, which addresses access to markets; (2) Rule 611, which provides intermarket price priority for displayed and accessible quotations; (3) Rule 612, which establishes minimum pricing increments; and (4) amendments to the joint-industry plans and rules governing the dissemination of market data. Additional information on Regulation NMS is available at: <http://www.sec.gov/spotlight/regnms.htm>.

MiFID and its implementing measures together establish a comprehensive legislative framework at European level relating to the establishment and conduct of investment firms, multilateral trading facilities and regulated markets. Additional information on MiFID is available at: [http://ec.europa.eu/internal\\_market/securities/isd/index\\_en.htm](http://ec.europa.eu/internal_market/securities/isd/index_en.htm).

**How has Hong Kong's financial-services sector changed since the establishment of the Hong Kong Special Administrative Region (HKSAR) in the middle of 1997?**

Unrelated to the establishment of the HKSAR, trading in our futures market in 1997 was still by open outcry on a trading floor and in the cash market about half of all trading was still done in the Stock Exchange's Trading Hall. Today, all futures and options trading is electronic and 98 per cent of stock trading is outside of the Trading Hall. Internet trading by investors is now widespread and all issuer announcements must be electronic.

Notable holdouts against this overall industry automation are the prospectuses and stock certificates which are still printed with stubbornness in vast quantities in Hong Kong. There are also pockets, some deep ones, of HKEx operations that cling to manual processes. I predict these will all be automated but that there will be resistance along the way.