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**Disclaimer**

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The following appendices do not constitute an offer or solicitation to anyone in any jurisdiction in which such offer or solicitation is not authorized or to any person to whom it is unlawful to make such offer or solicitation or is unlawful without compliance with any registration, filing or other requirements.

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**Appendix 1: Explanatory Notes on Delta 01 Risk Limit Set Up**

Firstly, the delta\_01 refers to the change in Net Present Value (NPV) of the IRS or CCS position when yield curve(s) is shocked by 1 basis point.

Secondly, the denominated limit currency will be **in USD**.

Thirdly, the limit can apply to the following products:

- IRS product : USD, EUR, CNH, HKD; or
- NDIRS product : CNY, KRW, INR, TWD, THB, MYR; or
- CCS product : USD/CNH, USD/HKD; or
- All Interest Rate products clearable via OTC Clear.

Finally, as delta\_01 calculated by OCASS can be a positive or a negative value the risk limit specified by Clearing Members represents the maximum and minimum delta\_01 limit. For example if a Clearing Member specifies 5 million delta\_01 limit, then actual delta\_01 for all of the Clearing Member's product cannot exceed **+5 million** or fall behind **-5 million** USD respectively. In OCASS<sup>2</sup>:

- Clearing members' receive-fixed rate position(s) will have positive delta\_01;
- Clearing members' pay-fixed rate position(s) will have negative delta\_01;

How Delta 01 risk limit works

Assume Clearing Member XYZ specifies a risk limit as follows and has no trade in the portfolio. If XYZ submits the two USD IRS trades:

- Trade 1 – 1Y maturity and receive fix with delta\_01 of 0.25 million USD
- Trade 2 – 6.5Y maturity and paying fix with delta\_01 of -0.75 million USD

Table 1

Product	Risk limit (in million USD)	Used (in million USD)
USD IRS	5	-0.5

Figure in the table is for illustration purpose only.

- Delta\_01 of trade 1 and 2 will be aggregated together and compare the amount with risk limit.

With the information in table 1, once the limit utilization (i.e. used divided by Risk limit reaches 100%) equal to or exceeds  $\pm 5$  million USD, for each subsequent trade<sup>3</sup>:

<sup>2</sup> Assume the position is a par trade. However please note that the delta\_01 will change subject to market data and/or trade terms.

<sup>3</sup> See 4.6.2 and 4.6.3, Chapter 4 –Margin and Valuation of OTC Clearing Hong Kong Limited Clearing Procedures.

<sup>3</sup> See 4.6.2 and 4.6.3, Chapter 4 –Margin and Valuation of OTC Clearing Hong Kong Limited Clearing Procedures.

- The trade will not pass limit check if it cannot reduce the limit utilization (below 100%).
- The trade will pass limit check if it can reduce limit utilization (below 100%).

Assume one year of time has passed and portfolio change as follow i.e. trade 1 has been matured and trade 2 is only one trades in member XYZ's portfolio, then OCASS will show the information below<sup>4</sup>:

Table 2

Product	Risk limit (in million USD)	Used (in million USD)
USD IRS	5	-0.75

Figure in the table is for illustration purpose only.

As trade 1 becomes matured, the delta\_01 of trade 1 will be zero, while remaining maturity of trade 2 is 5.5 years so the trade is still in the bucket. Please note that the Delta\_01 for trades may change according to various market factors such as rates movement, remaining maturity, etc.

<sup>4</sup> Assume no decay in delta\_01 for easier understanding.

**Appendix 2: Explanatory Notes on FX delta Risk Limit Set Up**

Firstly, the FX\_delta refers to the change in Net Present Value (NPV) of the Non Deliverable Forward (NDF) or Cross Currency Swap (CCS) position when the forward curve is shocked in parallel by 1 pip<sup>5</sup> (0.0001).

Secondly, the denominated limit currency will be **in USD**.

Thirdly, the limit can be specified for each NDF or CCS product or in aggregate, which means:

- By each NDF product : USD/CNY, USD/KRW, USD/INR, USD/TWD; or
- By each CCS product : USD/CNH, USD/HKD; or
- All FX products clearable via OTC Clear.

Finally, as FX\_delta calculated by OCASS can be a positive or a negative value the risk limit specified by Clearing Members represents the upper and lower bound of FX\_delta limit. For example if a Clearing Member sets FX\_delta limit to 2 million for all products, then actual FX\_delta for all of the Clearing Member's product cannot exceed **+2 million** or fall behind **-2 million** USD respectively. In OCASS:

- Clearing members' long primary currency i.e. USD position(s) will have positive FX\_delta;
- Clearing members' short primary currency i.e. USD position(s) will have negative FX\_delta;

How FX\_delta risk limit works

Assume Clearing Member XYZ specifies a risk limit as follows and has no trade in the portfolio. If XYZ submits the two USD/CNY NDF trades:

- Trade 1 – 3M maturity long USD position with FX\_delta of 0.1 million USD
- Trade 2 – 1Y maturity short USD position with FX\_delta of -0.3 million USD

Table 3

Product	Risk limit (in million USD)	Used (in million USD)
USD/CNY NDF	5	-0.2

Figure in the table is for illustration purpose only.

- FX\_delta of trade 1 and 2 will be aggregated and compare the amount with risk limit.

With the information in table 3, once the limit utilization (i.e. used divided by Risk limit reaches 100%) equals to or exceeds  $\pm 5$  million USD, for each subsequent trade<sup>6</sup>:

<sup>5</sup> It is an acronym for Percentage in Point.

<sup>6</sup> See 4.6.2 and 4.6.3, Chapter 4 –Margin and Valuation of OTC Clearing Hong Kong Limited Clearing Procedures.

- The trade won't pass limit check if it cannot reduce the limit utilization (below 100%).
- The trade will pass limit check if it can reduce limit utilization (below 100%).

Assume three months of time has passed and portfolio change as follow i.e. trade 1 has been matured and trade 2 are only one trades in member XYZ's portfolio, then OCASS will show the information below<sup>7</sup>:

Table 4

Product	Risk limit (in million USD)	Used(in million USD)
USD/CNY NDF	5	-0.3

Figure in the table is for illustration purpose only.

As trade 1 becomes matured, the FX\_delta of trade 1 will be zero, while remaining maturity of trade 2 is 9 months so the trade is still in the bucket. Please note that the FX\_delta for trades will change according to various market factors such as spot/forward rates movement, remaining maturity, etc.

<sup>7</sup> Assume no decay in FX\_delta for easier understanding.

**Appendix 3: Risk Limit Level Assessment**

The following steps show how OTC Clearing Hong Kong Limited assesses Clearing Member's risk limit level with its Tier 1 Capital.

Consider the following situation:

Clearing Member: CM A

Clearing Member Tier 1 Capital: 50 billion HKD

Tolerated Exposure by OTC Clearing (Tier 1 Capital \* 20%)<sup>8</sup>: 10 billion HKD (1.2747 billion USD)

Tolerated Delta\_01 risk limit level<sup>9</sup>:

$$\begin{aligned} \text{Delta}_01 \text{ limit} &= \text{CM's Tier 1 Capital} * 20\% \times \text{Delta}_01 \text{ factor}^{10} \\ &= 1.2747 \text{ billion USD} \times 0.41\% \\ &= 5.26 \text{ million USD} \end{aligned}$$

Tolerated FX\_Delta risk limit level<sup>11</sup>:

$$\begin{aligned} \text{FX}_\text{Delta} \text{ limit} &= \text{CM's Tier 1 Capital} * 10\% \times \text{FX}_\text{Delta} \text{ factor}^{12} \\ &= 1.27 \text{ billion USD} \times 0.005\% \\ &= 0.06 \text{ million USD} \end{aligned}$$

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<sup>8</sup> Initial Tolerance is a soft limit, higher level subject to further review by OTC Clearing Hong Kong Limited

<sup>9</sup> The assumption of calculations for Delta\_01 risk limit base on USD IRS and USDCNH CCS products.

<sup>10</sup> Delta\_01 factor is an internal factor used by OTC Clearing Hong Kong Limited and subject to change.

<sup>11</sup> The assumption of calculations for FX-Delta risk limit base on USDCNH CCS products.

<sup>12</sup> FX\_Delta factor is an internal factor used by OTC Clearing Hong Kong Limited and subject to change.