Corporate Communications Department
Hong Kong Exchanges and Clearing Limited
12th Floor, One International Finance Centre
1 Harbour View Street
Central, Hong Kong

Dear Sirs,

Re: Consultation Paper on the Introduction of a Price Control Mechanism during the Close Auction Session in the Securities Market

Please find our comments on the Exchange's proposed introduction of a price control mechanism during the close auction session. Should you have any questions to our comments, please do not hesitate to contact me.

1. **Do you support Approach 1, Approach 2, Approach 3 or suspending the CAS as a whole? Please state.**

   While we generally believe that markets should be able to freely trade without price limits and constraints (please refer to below #6), of the three approaches proposed by the Exchange, we favor Approach 1.

   We believe a percentage price movement, versus a spread based one, would be considerably easier to manage, especially when trading multiple markets from a centralized order management system standpoint, as well as would be easier to both script and give guidance on acceptable levels of movement

2. **If Approach 1 is adopted,**
   (i)   **Do you prefer the price limit to be set at 5%, 10% or other percentages?**

   We prefer the price limit to be set at 15%.

   (ii)   **How much lead time would your firm require for its implementation?**

   We believe only minimal lead time would be required for such implementation.

3. **If Approach 2 is adopted,**
   (i)   **Do you prefer the price limit to be set at 10 spreads, 24 spreads or other spreads?**

   We prefer a price limit at the widest spread permitted.

   (ii)   **How much lead time would your firm require for its implementation?**

   We believe only minimal lead time would be required for such implementation.

4. **If Approach 3 is adopted,**
   (i)   **Do you prefer the outstanding orders priced outside the pre-set range to be cancelled instead of carrying forward to the CAS?**

   We prefer for outstanding orders priced outside the pre-set range to be carried forward to the CAS.

   (ii)   **For securities without the day high and day low prices at 4 pm, do you prefer disallowing order input during the CAS for these securities or not imposing a price control limit at all?**

We prefer imposing a price control limit of 15% based on the previous close for such securities.

(iii) **Do you prefer the price control limit to be set at 0 spreads (i.e. simply using the day high and day low prices as limit), 10 spreads or other spreads above the day high and below the day low prices?**

We prefer the widest spread permitted.

(iv) **How much lead time would your firm require for its implementation?**

Though likely to require slightly more time than if Approach 2 were adopted, but should still only require minimal lead time for such implementation.

5. **If suspension of the CAS is adopted, how much lead time would your firm require for its implementation?**

We believe only minimal lead time would be required for such implementation.

6. **Do you have other proposed measures to reduce price volatility during the CAS or other comments or suggestions regarding the CAS? Please state.**

While there are some benefits to having a price limit, we however, do not believe this is the best approach to address the issue of price volatility during the CAS; especially when such price limits are only applied to the close while the market as a whole does not currently have any price movement limits in place.

We believe markets should be freely traded and without price caps. One of the main functions of an exchange should be to help determine price based on the order flow, and by imposing price limits above or below which a stock cannot trade, would hinder that main premise.

Instead, we believe a better alternative may be to utilize price circuit breakers whereby whenever a security's price exceeds a given pre-set percentage move, price circuit breakers would be triggered and trading would switch to a series of auctions. Such circuit breakers would be in place for the whole trading session and not just the close auction.

Such a mechanism has been widely and successfully implemented in many EU markets.

The circuit breaker can be set off in one of two ways:

1. If a stock moves *x percent* from the previous reference price, the stock would be suspended for a short period, and re-open by way of an auction.

The reference price should be either the previous close (for pre-open session) or the last auction price (including volatility suspension auctions) during continuous trading. The percentage movement necessary to trigger a break in trading can be varied i.e. in the UK they use 10% up/down initially, then movements of 5% for each successive stop. The auction to re-open can automatically roll-over to a new one if the implied movement is too great, but the premise is that it will *always* eventually re-quote, so there is no such thing as a limit up/down situation.

An example:

Assuming a stock closed at $125 the prior day. Stock opens, due to some announcement, stock trades up heavily. Once it trades up 10% ($137), the stock stops trading and flips into an auction phase. If it can re-quote within the 5% up/down level from the last trade ($144/$130), it will do so, and the new benchmark price is now the $137 level - it can now trade up/down 5% from there in the $144/$130 range before the cycle happens again. If it cannot re-quote within that spread, and is indicated greater than 5% away, the auction phase is "rolled" to another, with a further 5% price movement allowed (note, given the possibility of 'rolling' from one auction to another, the market close will not be fixed close). Thus, this should give the market ample time to react, and the exchange time to contact whoever put the order in and make sure it was valid etc.

This continues until the stock is able to re-trade. If the stock percentage movement limit is broken within either the open or closing auction, the same process is followed.

2. The second breaker is a tick-to-tick absolute price movement check. The reference price is always the last traded price (or previous close if it has yet to trade). If a stock moves greater than *x percent* from 1 tick to another, the stock suspends and heads into an auction (as above).

   For illiquid wide-spread stocks the value needs to be high, else they basically trade from one auction to another. For liquid stocks the value is generally tighter than the overall movement allowed, and is designed to pick up on fat-finger checks and also big gaps in the order book.

   Both of these options are there to give the rest of the market time to react to price movement, whether it is from news flow in the market or just plain order imbalances. With this in place along with a random end time, there is far less opportunity for "last second" orders to dramatically move a stock price, hence the volatility in the auction is reduced.

Other: to allow short selling in the CAS:
We believe to a large extent the price volatilities seen in the CAS are due to buy/sell order imbalances and that some of this price volatility could be reduced if short selling were permitted in the CAS.

Other: determination of nominal prices:

We believe the determination of nominal prices as stated in Appendix II in the consultation could, in certain cases, result in nominal prices being selected that are far away from the last traded price. Under Appendix II, where there is only a best bid or best ask, the nominal price will be the best bid or best ask. Looking at 'Case 2 (with ask only)' from Appendix II, last traded price is $122.0, no best bid, and best ask is $121.0. If this was a thinly traded stock, where there is no buy orders on the primary queue, and the best ask entered was $80 (or some other very low ask) instead of $121.0, will a best ask of $80 then be the nominal price? If so, we can foresee situations of wide price volatility in the close in that the closing price will differ greatly from the last traded price.