Part B Consultation Questions

Please reply to the questions below that are raised in the Consultation Paper downloadable from the HKEX website at:
http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201604.pdf
Please indicate your preference by checking the appropriate boxes.

Where there is insufficient space provided for your comments, please attach additional pages.

1. Do you support the revision of the current model with the introduction of a three-tier system with a review mechanism for HKEX's stock option position limit to address the issues with the existing regime?

   ☒ Yes

   ☐ No

   Please give reasons for your view.

   Yes - the introduction of tiered limits based on market capitalisation and liquidity will allow increased limits for those underlying names where demand is most required. This will address the current issue of one-size limit regardless of such factors which manifests as a restriction on volume of business during active market periods.

2. Do you agree the implementation of the proposed model (three-tier system with review mechanism) would be an important step in enhancing Hong Kong's stock options market and increasing its competitiveness?

   ☒ Yes

   ☐ No

   Please give reasons for your view.

   Yes - Increase in limits for SSO options is a welcome trend as hedging with such contracts increases liquidity, price transparency, order visibilty and market depth of listed SSO, increasing effective market operations and competitiveness.

3. Do you have any comments on the proposed model? Please give reasons for your view.

The change in tiering of limits is a good first step forward in order to allow increased client business by non-MM firms. However, the position limit for SSO is still calculated based on a contracts basis, without taking in to account the delta/in-the-moneyness or out-of-money status of the options. This places increased pressure on the usage of limits when there is significant open interest and market directional movement. In such cases, many strikes of options may fall out-of-the-money but continue to count towards the limt with same weighting as an at-the-money strike. Therefore we would like to see further progress in methodology to the use of the delta-based approach, as used by Hang Seng and HSCEI Index Futures and options in order to standardise monitoring across both Index and Single Stock contracts.
In general, the use of position limits in developed markets continues to encourage the use of OTC contracts (much higher listed volumes are seen in US markets which have higher or no associated limit), which with the advent of OTC reporting in Hong Kong we would hope eventually that a methodology removing position limts, but with full listed and OTC reporting transparency could be adopted.

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