

Submitted via Qualtrics

Personal view

1. Do you agree that the board lot value floor guidance should be revised? If not, please provide reasons.

Yes.

- Board lots are obsolete and should be scrapped entirely.
- Board lot rules make it harder for investors to get the exact exposure they desire.
- Let investors and brokers decide if an order is too small for them.

2. Do you agree that the board lot value floor guidance should be revised to HK\$1,000? If not, please provide reasons.

No. Just scrap the board lots altogether.

3. Do you agree with introducing board lot value ceiling guidance? If not, please provide reasons.

No. Let investors decide for themselves if an order is too small.

4. Do you agree that the board lot value ceiling guidance should be set at HK\$50,000? If not, please provide reasons.

No. The board lot should be scrapped.

5. Do you agree with applying the board lot value ceiling guidance only to issuers whose board lot units exceed 100 shares in order to facilitate potential future adoption of a single board lot unit and support alignment with Chinese Mainland markets? If not, please provide reasons.

No. Rather than do things piecemeal, just do the right thing and scrap the board lots. No new exchange in this century, and none of the crypto exchanges, have put in board lots.

6. Do you support further reduction of the board lot value ceiling guidance in the future? If not, please provide reasons.

Yes. Reducing the board lot to 1 share simplifies everything.

7. Do you support standardising board lot units as a pathway to reducing market complexity? If not, please provide reasons.

Yes. They should be standardised at one share.

8. Do you support adopting the eight board lot units specified (1, 50, 100, 500, 1,000, 2,000, 5,000, 10,000 share(s))? If not, please provide reasons.

No. It complicates the market with no real benefit.

9. If you do not support adopting eight board lot units, do you prefer a larger number of board lot units? If yes, please provide reasons.

No. I support one board lot unit: one share

10. (For issuers only) If a change is required, is six months an appropriate duration for an issuer to adjust its board lot unit or undertake other corporate action, to comply with board lot value ceiling guidance or standardisation of board lot units? If not, please provide reasons.

N/A

11. Do you support aligning implementation of standardisation of board lot units with the USM initiative? If not, please provide reasons.

No comment.

12. Are there any anticipated challenges, such as system limitations, in implementing the proposed board lot framework?

No comment.

13. Do you have any other comments regarding the board lot framework enhancements in the Hong Kong securities market?

Background

Examining board lot sizes (also known as round lots) is a current regulatory trend. This year, both Hong Kong and Singapore have opened consultations on board lots. Recently, the United States fiddled with its round lot rules. I urge HKEX to not repeat the mistake that the United States just made. Instead of fiddling around with board lot size around the edges, HKEX should just scrap the concept altogether. Board lots are obsolete and should be scrapped.

Board lot rules go back to the days when paper certificates were used in all stock transactions. In those days, it made no sense for anyone to process a very small transaction because of the

fixed costs involved. Those days are long gone. The true marginal cost of handling an all-electronic transaction is close to zero. It merely involves moving a few electrons around. (The pricing of that transaction, or course, is another matter, and minimum fixed charges can be appropriate, to be paid for by the initiator of a small transaction.)

Board lots make it harder to get precise exposures.

Often, investment strategies dictate a precise exposure to a particular instrument. Examples include:

- Merger arbitrage. For example, if one company offers to purchase another for stock, the price of the target stock may not reflect the entire promised premium. Merger arbs then buy the target stock and short the acquiring company to lock in the premium.
- Long-short and statistical arbitrage. Investors may want to bet on the differences between two stocks by going long one and short the other. The classic example in the US is Coke (KO) versus Pepsi (PEP).
- ETF market making or arbitrage. Even with a fairly large creation basket size, the large size of board lots makes it harder to precisely build a basket that exactly tracks the ETF's index.
- Derivative market making or arbitrage. Again, larger board lot sizes (or any board lot size) make it hard to hedge the underlying exposure precisely. Option market making requires hedge ratios that are constantly changing. Option market makers should be allowed to hedge in the precise quantities needed and not have the nuisance of board lots.

High board lot sizes deter investors from investing.

Some investors may not have the money or the risk appetite to buy an entire board lot. I myself have been deterred from investing in some SGX stocks because of the high board lot size.

Even worse, the high board lot size may induce some investors to take on more risk than they would prefer and end up in an under diversified portfolio.

High board lot sizes deter young investors from learning about investing.

Young investors typically have little money, but they have a desire to learn. One of the best ways to learn about trading is to actually trade. In the US, our low trading commissions and the ability to trade in odd lots and even fractional shares has brought in a new generation of investors.

When high board lot sizes keep new investors out of the equity market, they are likely to turn to unregulated offshore crypto exchanges.

High board lot sizes inhibit investor diversification.

One of the basic principles of investing is portfolio diversification. Investors should not be placing all of their eggs in one basket. Most studies show that it takes at least a dozen different securities to get reasonable diversification, and many more if the securities are concentrated in a particular industry or factor. If we assume a minimum of 12 stocks are needed and that a board lot costs \$1,000, that implies a prudent investor must start out with \$12,000. This can be far beyond the reach of many novice investors.

New exchanges don't create board lot systems. That says a lot.

As a finance professor, my market specialty is studying the market structure of exchanges. I have been to over 100 licensed stock, bond, commodity, and derivative exchanges in my career.

Many new exchanges in numerous asset classes have been set up in the last 40 years as stock exchanges emerged in many post-communist and developing countries. Almost none of them have the equivalent of a board lot. There is good reason for this, as the board lot is obsolete. If SGX did not exist and was being founded today, it would not come up with board lots.

Similarly, crypto exchanges, both centralized and decentralized, don't bother with board lots. Indeed, most of them empower fractional trading.

Let investors decide if a trade is too small for them.

There is nothing wrong with brokers or exchanges or clearing houses imposing a minimum ticket charge on a transaction. In many cases such pricing policies make good economic sense. However, it should be left up to the investor to decide whether a particular trade size is too small to make economic sense to them relative to the fixed trading costs. They may well have valid reasons to them for wanting to buy less than a thousand dollars' worth.

Questions remain about the definition of the best bid and offer and the measurement of execution quality.

Eliminating board lots does create some questions regarding the measurement of liquidity and execution quality. Again, SGX can use this opportunity to modernize and leapfrog technology laggards like the United States.

An Indicative BBO should be based on trading a constant dollar amount.

In the US, investors pay a lot of attention to the consolidated National Best Bid and Offer (NBBO). Our rules require brokers to display this in order to give investors a sense of the current state of liquidity for a stock. However, the current NBBO is for a tiny dollar amount for low-priced stocks and an absurdly high dollar amount for high-priced stocks.

The US Securities and Exchange Commission has implemented a kludge by changing the round lot size for some high-priced stocks, but this just adds still more costly complexity to the market and does not fix the problem. The NBBO is not a consistent indicator of liquidity or the cost of trading to investors, even with the recent changes.

It makes sense to construct a general benchmark that shows the price at which one could buy or sell a constant dollar amount such as \$5,000. The Indicative Best Bid and Offer (IBBO) would be disseminated through standard data feeds.

Investors should be shown the Effective Best Bid or Offer (EBBO) for the exact size of their order.

It is now trivial for a computer to examine the displayed depth of book and calculate what the price would be to trade a given dollar amount against the displayed orders. Brokers should display an Effective Best Bid and Offer (EBBO) to investors when they place an order for a given size. This would give investor much more precision about the price they are likely to receive.

Execution quality should be measured against the EBBO.

There has been much discussion over the years around “price improvement.” However, how much of the current “price improvement” is really an improvement over the displayed interest in the market and how much of it is just an artifact of bad quotes that ignore odd lots? Using the EBBO provides a much more precise benchmark for measuring execution quality.

Just scrap the board lot.

The board lot is obsolete. Rather than tinker with it around the edges, the rational thing to do is to just eliminate the board lot altogether. This creates a simpler market structure that benefits all participants.

Respectfully submitted,

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