

香港期貨交易所有限公司

(香港交易及結算所有限公司全資附屬公司)

HONG KONG FUTURES EXCHANGE LIMITED

(A wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited)

通告 CIRCULAR

Subject: Revision on the Capital Adjustment Method for Stock Futures in relation to Spin-offs

Enquiry: HKATS Hotline¹ Tel: 2211-6360

An internal review was conducted recently on the capital adjustment method for stock futures in relation to spin-off of the underlying stock and Hong Kong Futures Exchange Limited ("HKFE") is pleased to announce its proposal to amend its rules to make two revisions to its capital adjustment methodology in order to protect the market integrity and to maintain an orderly market when there are spin-offs.

The revised methodology will be reflected in the corresponding rules, details and the effective date of the corresponding rules will be announced in due course.

To protect the market integrity before the revised methodology is effective, HKFE may consult with the Securities and Futures Commission ("SFC") and may pursuant to Regulation 010A of Regulations for Trading Stock Futures Contracts of Rules, Regulations and Procedures of HKFE, to adopt a similar methodology in handling spin-off when the entitlement of the spin-off constitutes large portion of the underlying stock's value.

1) Adjustment ratio formula revision

The first revision is to align the valuation date on which the various components in the adjustment ratio ("AR") formula (i.e. the value of the underlying share of the stock futures and the entitlement of the spin-off) are calculated to the first trading day of the entitlement of the spin-off. For details, please refer to the table below.

¹ All calls to the HKATS hotline will be recorded. Please refer to the following link for HKEX's privacy policy statement:
http://www.hkex.com.hk/eng/global/privacy_policy.htm

Terms	Existing Formula	Revised Formula
Adjustment Ratio	$\frac{S (\text{ex date} - 1) - OD - E (1\text{st trading day})}{S (\text{ex date} - 1) - OD}$ Where: • $S (\text{ex date} - 1)$ is the closing price of the share prior to the ex-entitlement date; and • $E (1\text{st trading day})$ is the value of the entitlement of the spin-off based on the volume weighted average price ("VWAP") on its first trading day. • OD is ordinary cash dividend and OD shall be deducted from $S (\text{ex-date-1})$ only if OD and the entitlement have the same ex-date.	$\frac{S (1\text{st trading day})}{S (1\text{st trading day}) + E (1\text{st trading day})}$ Where: • $S (1\text{st trading day})$ is the value of the share based on the VWAP on its first trading day after spin-off; and • $E (1\text{st trading day})$ is the value of the entitlement of the spin-off based on the VWAP on its first trading day.

This revision can minimize the chance of having an extremely low AR² due to different market forces applying when valuing the share of the underlying stock and the entitlement of the spin-off on different days. In addition, the revision also avoids the possibility of having a negative AR.

2) Introduction of AR floor at 0.1

In order to offer additional market protection by preventing the calculated AR to be extremely low², a floor of 0.1 will be introduced to the AR for calculating the adjusted contract multiplier. Please note that an alternative AR floor value may be prescribed by HKFE from time to time, after consultation with the SFC. For details, please refer to the table below.

	When Calculated AR ≥ 0.1	When Calculated AR < 0.1
Adjusted Contract Price	Old contract price x Actual AR	
Adjusted Contract Multiplier ³	Old Contract Multiplier / Actual AR	Old Contract Multiplier / <u>0.1</u>

Inform Your Staff and Clients

² An extremely low AR will lead to a scenario where the contract size of the adjusted stock futures contract becomes abnormally high, which could jeopardize the orderliness of the underlying stock market.

³ This formula is an illustration of how the contract multiplier should be adjusted based on the AR value. For the existing arrangements for capital adjustment in relation to spin-offs, please refer to the Attachment.

Participants should notify all clients trading / holding positions in stock futures contract of the details of trading, clearing, settlement arrangements and the associated risk. Please ensure that your back office systems are ready for a smooth operation in handling the proposed revision. In addition, all your staff should be fully aware of the trading and clearing arrangements and should exercise caution with the proposed revisions when dealing with the standard and adjusted stock futures contracts when advising your clients.

Sanly Ho
Co-Head
Trading Department
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This circular has been issued in the English language with a separate Chinese language translation. If there is any conflict in the circulars between the meaning of Chinese words or terms in the Chinese language version and English words in the English language version, the meaning of the English words shall prevail.

Any information provided in this circular relating to the trading of security futures or how the law may be interpreted is provided for reference generally without considering your specific circumstances and does not constitute legal or other advice from HKFE or any member of the HKEX group. Such information should not be regarded as substitute for professional advice. You should seek independent legal or other professional advice before taking any action to trade any contracts listed on HKFE, whether for yourself or as intermediary on behalf of any other person.

Attachment

Existing Arrangements for capital adjustment in relation to spin-offs

Terms	Stock Futures (Existing Arrangements)
Adjustment Ratio	$AR = \frac{S_{(\text{ex date} - 1)} - OD - E_{(1\text{st trading day})}}{S_{(\text{ex date} - 1)} - OD}$ Where: • $S_{(\text{ex date} - 1)}$ is the closing price of the share prior to the ex-entitlement date; and • $E_{(1\text{st trading day})}$ is the value of the entitlement of the spin-off based on the volume weighted average price ("VWAP") on its first trading day. • OD is ordinary cash dividend and OD shall be deducted from $S_{(\text{ex-date-1})}$ only if OD and the entitlement have the same ex-date.
Adjusted Contract Price	Adjusted Contract Price ("ACP") = Old Contract Price ("OCP") x AR
Adjusted Contract Multiplier	Adjusted Contract Multiplier = $\frac{OCP * \text{Old Contract Multiplier}}{ACP}$