



Consultation Conclusions Clearing House Risk Management Reform Measures

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Why Is the Clearing House Reform Needed?



2008 global financial crisis

- Heightens need to strengthen risk management
- HKEx risk management needs to keep up

Risk management reform long overdue

	<u>Average Daily Turnover</u>	<u>Guarantee Fund Size</u>
1992	\$3bn	\$105mn
2005-2011	\$18.3bn-\$88.1bn*	\$245mn

Lehman default exposed weakness in risk management

- Lehman was then not a top 10 Clearing Participant (CP)
- HKSCC might have collapsed if a bigger CP defaulted

* The highest daily securities market turnover was \$210.5bn (3 October 2007).
 HKSCC = Hong Kong Securities Clearing Company Limited

How Will the Reform Benefit Our Market?



NOW

FUTURE

GF: Static



GF: Dynamic and scalable based on market volatility

No margin: High chance of loss sharing with defaulter



User pays

**Under-funded
GF Size: \$245mn**



**Well-funded
GF Size: Avg \$1.3bn**

GF = Guarantee Fund

Key Components of Reform

Stress Testing

- Testing methodologies significantly enhanced

Capital Adequacy

- HKSCC margin / Dynamic GF introduced
- HKCC RF adequately contributed

HKEx Capital Contribution

- Helps small and medium-sized brokerages
- HKSCC margin and Dynamic GF Credits granted
- HKCC Contingent Advance Capital granted

Consultation Process

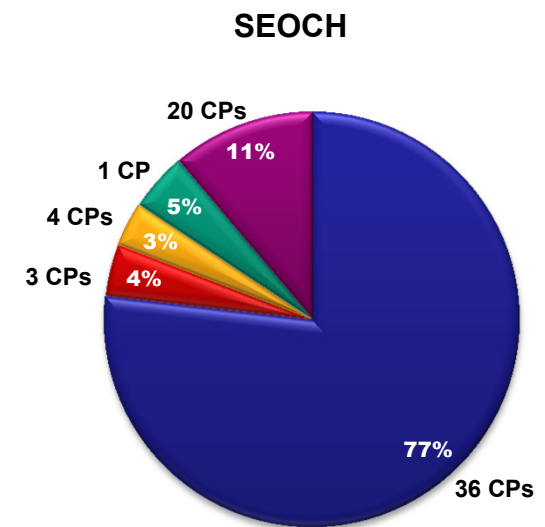
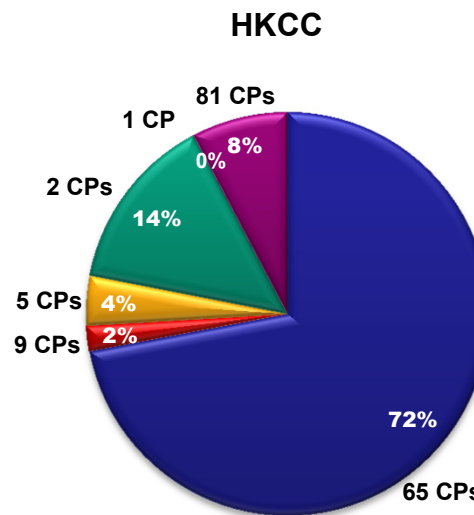
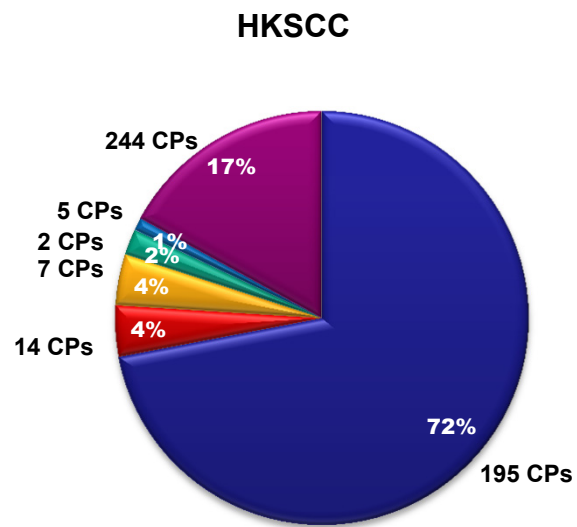
A thorough four-month consultation process to gather views from all key stakeholders



Response Overview



Response by Market Share and Number of Clearing Participants



- Agree to ALL questions
- Disagree with 1-2 question
- Disagree with 3-5 questions
- Disagree with 6-7 questions
- Disagree with all questions
- Did not respond

A total of 626 responses received, 273 were from Clearing Participants

SEOCH = SEHK Options Clearing House Limited

Market Feedback

HKEX's Response

Count GF/RF contribution as liquid capital

- Ongoing proactive discussion with SFC
- Information and proposed options presented to SFC

Increase Margin Credit

- About 80% of CPs do not need to pay on any given day
- Doubling credit yields limited incremental benefit

Allow flexibility in margin collection currency

- Allow CPs to pay margin either in the original trading currencies or in one alternative eligible currency of choice

Refinements to Proposal – Some Examples

Introduce Specific Cash Collateral

Allow offset of margin requirements with net favourable Marks*

Count RF contribution as liquid capital for purpose of calculating Capital-Based Position Limits

Provide CPs the option to pay margin in one elected eligible currency

Allow bank guarantee to satisfy up to 50% of the margin and Marks requirements

**Reduces
CPs' funding
burden**

**Enhances
funding and
operational
efficiency**

* An amount required to be provided by a CP as a result of a mark-to-market of its unsettled Market Contracts by reference to market prices.

Implementation Timetable

System development and rule amendments – ongoing

Revise SEOCH Collateral assumption – mid 2012

Communication programme – 2Q-3Q 2012

Implementation of all reform proposals – 3Q 2012

Thank You