

香港聯合交易所有限公司

(香港交易及結算所有限公司全資附屬公司)

THE STOCK EXCHANGE OF HONG KONG LIMITED

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

通告 CIRCULAR

Subject: Enhancements to Stock Option Market Maker Obligations

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The Stock Exchange of Hong Kong Limited (the “Exchange”) is pleased to announce enhancements to the obligations of Market Makers in its stock option market. The enhancements aim to support market liquidity, with obligations refined for the characteristics of the underlying securities and relevant market conditions. The enhancements have been approved by the Securities and Futures Commission.

The enhancements will be introduced in two phases. The effective date of the first phase, including the introduction of a new liquidity level and normalisation of obligations for option classes whose underlying is an Exchange Traded Fund (“ETF options”), is 31 October 2022. The effective date of the second phase, handling obligation adjustments in exceptional conditions, will be in the 1st half of 2023, subject to market readiness. Please refer to the circular ([ref: LSD/065/2022](#)) for the relevant rule amendments for each phase. The effective date of the second phase will be issued through a separate circular.

Unless otherwise defined in this Circular, terms used in this Circular shall have the same meanings ascribed to them in the Options Trading Rules of the Exchange.

Phase 1 – to be introduced on 31 October 2022

1. Introduction of Liquidity Level 3

Liquidity levels define the obligations of an option Market Maker. Currently, all option classes are classified as Liquidity Level 1 (“LL1”) or Liquidity Level 2 (“LL2”). A new liquidity level of Liquidity Level 3 (“LL3”) will be introduced. LL3 obligations will apply to consistently volatile option classes, which are defined as those with an average implied volatility above 50%. For the remaining option classes, they will be classified as LL1 or LL2, based on the liquidity of the underlying security, as is the current practice. The liquidity level of option classes are updated on a monthly basis¹.

Obligation table for option classes, effective 31 October 2022

Option Series	Option Class		
	Liquidity Level 1	Liquidity Level 2	Liquidity Level 3
Spot month with 3 Business Days or less to expiry	20% of option bid, or 3 x BUS, whichever is the lower.	20% of option bid, or 4 x BUS, whichever is the lower.	30% of option bid, or 7 x BUS, whichever is the lower.
Spot month with 4 Business Days or more to expiry and the next 3 calendar expiry months	10% of option bid, or 3 x BUS, whichever is the lower.	10% of option bid, or 4 x BUS, whichever is the lower.	20% of option bid, or 7 x BUS, whichever is the lower.
The next 2 calendar quarter expiry months	20% of option bid, or 4 x BUS, whichever is the lower.	20% of option bid, or 6 x BUS, whichever is the lower.	30% of option bid, or 10 x BUS, whichever is the lower.
The 3rd calendar quarter expiry month	20% of option bid, or 8 x BUS, whichever is the lower.	20% of option bid, or 12 x BUS, whichever is the lower.	30% of option bid, or 20 x BUS, whichever is the lower.

Note: BUS = Best Underlying Spread

2. Normalization of Market Maker obligations for ETF Options

With the recent introduction of an ETF spread table, the minimum price increment for ETF securities is smaller than the minimum price increment for stock securities of the same price. The ETF option obligations of a Market Maker which are measured by the Best Underlying Spread (“BUS”), will be multiplied by a factor of 2.5 in order to normalize obligations. The component of ETF option obligations which is measured as a percentage of the Market Maker’s quote bid will not be adjusted.

¹ Current liquidity level classifications can be found at https://www.hkex.com.hk/Products/Listed-Derivatives/Market-Maker-Program/Market-Maker-Obligations-and-Incentives?sc_lang=en

Obligation table for ETF Options, effective 31 October 2022

Option Series	Option Class		
	Liquidity Level 1	Liquidity Level 2	Liquidity Level 3
	<i>Obligation is the tighter obligation of the two metrics</i>		
Spot month with 3 Business Days or less to expiry	20% of option bid, or 7.5 x BUS , whichever is the lower.	20% of option bid, or 10 x BUS , whichever is the lower.	30% of option bid, or 17.5 x BUS , whichever is the lower.
Spot month with 4 Business Days or more to expiry and the next 3 calendar expiry months	10% of option bid, or 7.5 x BUS , whichever is the lower.	10% of option bid, or 10 x BUS , whichever is the lower.	20% of option bid, or 17.5 x BUS , whichever is the lower.
The next 2 calendar quarter expiry months	20% of option bid, or 10 x BUS , whichever is the lower.	20% of option bid, or 15 x BUS , whichever is the lower.	30% of option bid, or 25 x BUS , whichever is the lower.
The 3rd calendar Quarter expiry month	20% of option bid, or 20 x BUS , whichever is the lower.	20% of option bid, or 30 x BUS , whichever is the lower.	30% of option bid, or 50 x BUS , whichever is the lower.

Phase 2 – to be introduced in 1st Half 2023

3. Obligation adjustments in exceptional conditions for stock options

To support liquidity during all market conditions, the Exchange is introducing two mechanisms to adjust obligations of Market Makers during exceptional market conditions: (1) Agile–LL3, and (2) Fast Market. These enhancements will be introduced in the 1st half of 2023 and will be announced through a separate circular.

3.1 Agile-LL3

When a specific option class² in LL1 or LL2 becomes exceptionally volatile, the option class will be reclassified as “Agile-LL3” for 5 Business Days, inclusive of the date of reclassification. During this period, the obligations of Market Makers for the option class will match those of LL3. Reclassification will be triggered by the implied volatility from the bid price of a second month at-the-money option exceeding 75%. Option classes categorized as LL3 are not eligible for reclassification as Agile-LL3.

² A stock option class refers to all possible option series on the same underlying security

To have an option class reclassified as Agile-LL3, a reverse inquiry must be raised with the Exchange from a Market Maker. When the implied volatility is validated to have met the reclassification criteria, the option class will be reclassified and Options Exchange Participants will be informed by the Exchange. Please see Attachment I for the detailed workflow.

3.2 Fast Market

For scenarios where the entire market becomes exceptionally volatile, a “Fast Market” will be declared, after a reverse enquiry has been raised by a Market Maker and validated by the Exchange. The criteria for a Fast Market is either the Volatility Hang Seng Index (“VHSI”) exceeding a value of 40, or an intraday move in the Hang Seng Index (“HSI”) that is greater than +/-4% during the trading hours of the stock options market. Please see Attachment I for the detailed workflow.

When a Fast Market is declared, all Market Maker obligations will be reclassified as Agile-LL3 for one day. The scope of Fast Market may be revised in the future as necessary.

The Exchange retains discretion on what criteria is established for classifications of LL1, LL2, LL3, Agile-LL3 and Fast Market, and may review and revise the criteria as appropriate.

Brian Roberts
Managing Director
Head of Equities Product Development
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This circular has been prepared in English with a Chinese translation. If there is any inconsistencies between the two versions, the English version shall prevail.

Attachment I

Reclassification Workflow

- In the reverse inquiry for Agile-LL3, the Market Maker must report the option series, the option bid price, and the timestamp of the observation
- In the reverse inquiry for Fast Market, the Market Maker must report the specific triggering condition and timestamp of the observation for the Exchange to validate.

