

15 October 2018

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& BY MAIL

Securities and Futures Commission
35/F., Cheung Kong Center,
2 Queen's Road Central,
Hong Kong.

To whom it may concern:

Re: Consultation Paper on the Proposed Guidelines for Securities Margin Financing Activities

We refer to the captioned consultation paper issued by Securities and Futures Commission on 17 August 2018 ("Consultation Paper") and enclose herewith our comments. Unless otherwise defined, all capitalized terms used herewith shall have the same meanings as those defined in the Consultation Paper.

1. Total margin loans controls (paragraph 1.2 of page 24 of the Consultation Paper)

We agree that SMF broker should control its margin loans with reference to its SMF's shareholders' fund and subordinated loans. However, depending on SMF broker's financial background, business models, market situation and clients' trading history, the setting of appropriate loans-to-capital ratios may vary from small to medium SMF brokers. We recommend setting the benchmark for total margin loans-to-capital ratio at 4 times or above.

2. Highly correlated securities (paragraph 3.1 of page 25 of the Consultation Paper)

Note (2) of the definition refers to two or more securities which exhibit a high correlation in historical price movements and their issuers either have group affiliations, material cross-shareholdings, significant business affiliations or are engaged in the same industry.

Different SMF brokers may have different understanding regarding “high” correlation in historical price movements, “significant” business affiliations and “material” cross shareholdings. SMF brokers may also experience practical difficulties in identifying these with undue cost and effort. The inclusion of these highly correlated securities as per Note (2) of the definition in setting securities collateral concentration limit may not be effective and practical for the purpose of monitoring concentration risk on a regular basis.

3. Proposed quantitative benchmark of securities collateral concentration (paragraph 3.9 of page 26 of the Consultation Paper)

Apart from “index stocks”, the classification of securities collateral under “other stock” can be further sub-divided into liquid and illiquid stocks following the same definition of illiquid collateral as acceptable by the FRR for liquid capital calculation purpose. The suggested quantitative benchmark is as follows:

<u>Index stocks</u>	:	40%
<u>Non-index stocks</u>		
-Liquid stocks	:	30%
-Illiquid stocks	:	20%

4. Proposed quantitative benchmark of haircut for securities collateral (paragraph 5.5 of page 28 of the Consultation Paper)

It is very difficult to keep track of the average haircut changes of the top three lending banks as different lending banks may have different methodology and frequency in updating the haircut percentage. Therefore, setting quantitative benchmark on the haircut for securities collateral is not feasible. Instead, the haircut of the lending banks should only form a reference in addition to the qualitative factors as mentioned in paragraph 5.2 of the Consultation Paper in setting the haircut prudently.

5. Proposed quantitative benchmark of unsettled and long outstanding margin calls
(paragraph 6.4 of page 29 of the Consultation Paper)

Setting quantitative benchmark is not feasible as SMF broker will normally consider other qualitative factors, including market value and quality of client's stock holdings (such as price trends, liquidity, publicly available information) together with client's trading history, settlement history, financial background and creditworthiness. Also, different SMF broker has different margin call policy and clients mix. With an aim to maintain competitiveness in the brokerage industry, such proposed quantitative benchmark may discourage SMF to adopt a more tightening margin call policy that may result in a higher amount of unsettled and long outstanding margin calls.

Thank you for your kind attention.

Yours faithfully,