

Markets

To ensure orderly markets, we supervise and monitor exchanges and clearing houses in Hong Kong. We also work to improve market infrastructure and strengthen Hong Kong's role as the premier risk management centre for Mainland risk and a booking hub for Asian derivatives.

Supervision of HKEX

On-site inspection

As part of our regular on-site inspections of the non-listing-related operations of Hong Kong Exchanges and Clearing Limited (HKEX), we completed an inspection of its cash market clearing operations in 2018 and recommended improvements. We began an inspection of its futures exchange trading and clearing operations in 2019.

Recognised clearing houses

We worked with HKEX to implement risk management initiatives to improve the resilience of its clearing houses in Hong Kong and their compliance with international standards. We approved proposals to enhance the admission criteria for clearing participants, the process for managing clearing participants' defaults and recovery plans for dealing with extreme market situations.

Following our approval, HKEX introduced measures to strengthen the clearing guarantee funds, including risk-based contributions from the clearing houses.

New products

We approved five derivative products proposed by HKEX to meet the trading and hedging needs of market participants.

New derivative products approved

	Trading commencement date
MSCI Asia ex Japan Index Futures	11 June 2018
Hang Seng Index (Gross Total Return Index) Futures	5 November 2018
Hang Seng Index (Net Total Return Index) Futures	
Hang Seng China Enterprises Index (Gross Total Return Index) Futures	
Hang Seng China Enterprises Index (Net Total Return Index) Futures	

Mutual market access

Stock Connect

In April 2018, the SFC and the China Securities Regulatory Commission (CSRC) jointly announced a fourfold increase in the daily quotas for Mainland-Hong Kong Stock Connect to RMB52 billion for each of the northbound links and RMB42 billion for each of the southbound links. The new quotas took effect on 1 May 2018.

Stock Connect covered 1,321 Mainland stocks (580 companies listed in Shanghai and 741 companies listed in Shenzhen) and 479 Hong Kong stocks as of end-March 2019, representing 88% of market capitalisation in Hong Kong, 84% in Shanghai and 73% in Shenzhen.

As of end-March 2019, southbound trading reached a cumulative net inflow of RMB700.5 billion and international investors bought in RMB767.1 billion worth of A-shares through northbound trading.

During the year, Stock Connect accounted for a steady share of Hong Kong's market turnover. On average, daily southbound trading was around 6% of total trading, similar to the proportion in 2017. Northbound trading increased to 3% of the Mainland's total market turnover, compared to 1% in 2017.

We worked with the CSRC to implement an investor identification regime for northbound trading under Stock Connect on 26 September 2018. This facilitates market surveillance of northbound trades by the Mainland exchanges and regulators. We target to introduce a similar model for southbound trading in mid-2019.

Bond Connect

After a consultation with the SFC, Bond Connect Company Limited¹ introduced the Primary Market Information Platform in February 2019. As the first English-language portal disseminating information about the Mainland primary bond market, the platform provides timely and reliable information to global investors about new bond issues.

Bond Connect experienced strong growth during the year. Total funds flowing into the Mainland interbank bond market through Bond Connect reached RMB222 billion in 2018, up from RMB132 billion in 2017. Average daily trading increased to RMB3.6 billion in 2018 from RMB2.2 billion in 2017.

OTC derivatives

In line with the G20's commitment to reform the over-the-counter (OTC) derivatives market, an OTC derivatives regime is being implemented in phases in Hong Kong. In June 2018, we concluded a joint consultation with the Hong Kong Monetary Authority on mandating the use of Legal Entity Identifiers² for

the reporting obligation and expanding the clearing obligation. We also adopted the proposed process to determine for which products it may be appropriate to introduce a platform trading obligation.

We use the data reported to the Hong Kong Trade Repository to monitor OTC equity derivatives of securities listed in Hong Kong. This allows us to assess more effectively the systemic risks to the Hong Kong securities market arising from both the on-exchange and off-exchange derivatives markets. As of end-March 2019, the estimated notional value of the OTC equity derivatives of securities listed in Hong Kong was comparable to that of exchange-traded counterparts. This was in line with major overseas markets.

Uncertificated securities market

In January 2019, we launched a consultation jointly with HKEX and the Federation of Share Registrars Limited proposing a revised operational model for implementing an uncertificated, or paperless, securities market in Hong Kong (see sidebar below).

Going paperless

The SFC is working to introduce a paperless securities market in Hong Kong.

In January 2019, we issued a consultation paper jointly with HKEX and the Federation of Share Registrars Limited to seek the public's views on a proposed operational model which would enable investors to hold and transfer securities in their own names without share certificates or other paper documents.

Investors would enjoy a direct relationship with the listed company and better legal protection. Listed companies would have more transparency when it comes to the genuine owners of their shares.

^a Securities held through the HKEX system will be registered in the name of HKSCC Nominees Limited.

The existing nominee structure within the clearing and settlement infrastructure would be preserved^a, which means that investors who want to hold a beneficial interest in securities through brokers and banks may continue to do so.

The digitisation of securities holdings and removal of paper and manual processes will help make post-trade settlement and servicing more efficient. This makes our markets more dynamic and globally competitive.

After the enactment of legislation, implementation is expected to be conducted in phases from 2022.

¹ Bond Connect Company Limited is an authorised automated trading services provider facilitating the operation of Bond Connect.

² A unique 20-digit, alpha-numeric code which identifies entities in a financial transaction.

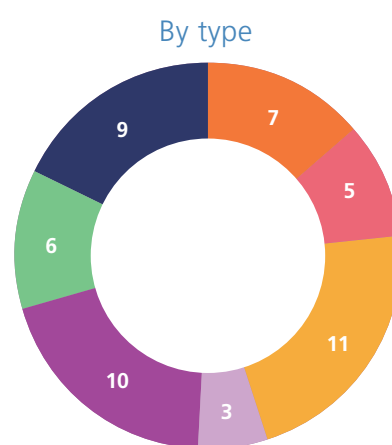
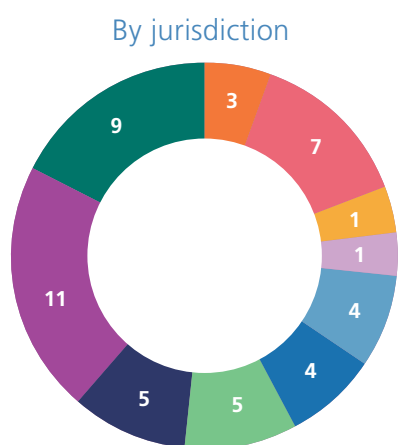
Markets

Automated trading services

Under the Securities and Futures Ordinance (SFO), two regimes regulate automated trading services (ATS) providers. Typically, those that offer facilities similar to those of a traditional exchange or a clearing house are authorised under Part III of the SFO. Intermediaries which provide traditional dealer functions along with ATS as an added facility (eg, operating a dark pool or a pre-IPO trading platform) are expected to be licensed under Part V of the SFO.

Over the past year, we approved eight applications from overseas regulated exchanges and bond trading platforms. Trades conducted on authorised trading venues were mainly in benchmark index futures and options, commodity futures, bonds, equities and exchange-traded funds offered by overseas exchanges. The average daily trading volume of futures contracts originating from Hong Kong was about 348,000 contracts for the 12 months ended 31 March 2019.

ATS providers under Part III



Note: One ATS provider is both a financial futures exchange and a central counterparty.

ATS providers

	As at 31.3.2019	As at 31.3.2018	As at 31.3.2017
Under Part III	50	57	49
Under Part V	24	24	24

Short position reporting

	As at 31.3.2019	As at 31.3.2018	As at 31.3.2017
Market value of short positions as a percentage of market capitalisation of reported securities	1.5%	1.5%	1.4%