

# Bond and Note Transactions and Trading Market Infrastructure

## A. Trading of Bonds and Notes

In Hong Kong, China, bonds and notes can be traded either OTC or on an exchange. Bonds and notes transacted in the secondary market are typically traded OTC via negotiations between buyer and seller. Most transactions take place over the telephone or via voice broker. At the same time, the trading on exchange of listed bonds and notes on the main board of SEHK is also possible, although the volume is negligible.

The dealing in unlisted debt securities is regulated by provisions in the SFO and the Companies (Winding Up and Miscellaneous Provisions) Ordinance. In turn, the SFC prescribes acceptable practices for the distribution and dealing of unlisted debt securities in the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission. Those unlisted debt securities issued via private placement may only be offered, sold to, and traded with Institutional Investors at any time.

The trading of listed debt securities is subject to the Trading Rules of SEHK. More information can be found in the individual sections of this chapter and other relevant sections in this Bond Market Guide.

## B. Trading Platforms

Trading of bonds and notes in the Hong Kong bond market can be done in the OTC market or on an exchange.

The issuance of debt securities to professional investors in the OTC market does not preclude subsequent trading on SEHK, but these securities are offered to professional investors only, typically institutions, in the expectation that they will trade the relevant securities off exchange with other professional investors. Liquidity for secondary market trading on SEHK may be limited as a result.

### 1. Over-the-Counter Market

The traditional OTC market itself is less so a trading platform but instead an organized market. Trades in bonds and notes are concluded directly between institutional counterparties via phone or using the services of a voice broker or inter-dealer broker. Individual dealers may also use Bloomberg or similar global trading system providers, and/or an in-house trading system to carry out bond and note trading activities.

### 2. Electronic Trading Platform

Launched in December 2007, the Electronic Trading Platform is one of the recommendations arising from the Review of Debt Market Development completed by

the HKMA in 2006. The platform provides the necessary infrastructure to support electronic trading of EFBNs and can be extended to cover other bonds and financial instruments available in the market. The platform increases price transparency among market players and streamlines the trading process. Market players can identify their trade counterparties and conclude deals more efficiently. Overseas as well as local market players are encouraged to use this platform to trade bonds and other financial instruments issued in Hong Kong, China.

### 3. Trading on Exchange

Debt securities issued in Hong Kong, China may be listed and traded on SEHK. Trading on SEHK, including for debt securities, happens through a number of sessions from pre-open at 9 am to the end of the afternoon session at 4 pm, Mondays to Fridays (see Table 4.1). There is no trading on Hong Kong, China public holidays. When a holiday falls on a Sunday, the following Monday will become a replacement holiday.

**Table 4.1: Hong Kong Exchanges and Clearing Limited Debt Securities Trading—Trading Hours**

Auction Session	
Pre-opening Session*	9 a.m. – 9:30 a.m.
Continuous Trading Session	
Morning Session	9:30 a.m. – 12 noon
Extended Morning Session	12 noon – 1 p.m.
Afternoon Session	1 p.m. – 4 p.m.

\*No order and trade activities are allowed during the blocking period between 9.28 a.m. and 9.30 a.m. For more details, see [http://www.hkex.com.hk/eng/market/sec\\_tradinfra/Documents/preopenfaq.pdf](http://www.hkex.com.hk/eng/market/sec_tradinfra/Documents/preopenfaq.pdf)  
 Notes: There is no Extended Morning Session or Afternoon Session on the eves of Christmas, New Year's Day, and the Lunar New Year. There will be no Extended Morning Session if there is no Morning Session.  
 Source: Hong Kong Exchanges and Clearing.

HKEX carries on its website substantial information on the securities trading infrastructure, trading information, as well as information on Exchange Participants, news and rules and circulars.<sup>66</sup>

## C. Mandatory Trade Reporting

At present, there is no mandatory reporting of OTC transactions in the Hong Kong bond market. Trades in CMU Instruments result in instructions for settlement through participant accounts maintained with CMU.

<sup>66</sup> See [http://www.hkex.com.hk/eng/market/sec\\_tradinfo/CMTradInfo.htm](http://www.hkex.com.hk/eng/market/sec_tradinfo/CMTradInfo.htm)

Trades executed on HKEX are reported on its information service as a matter of course. It is the duty of Exchange Participants to input the details of sale transactions concluded by them into the exchange's system within the time prescribed by the Trading Rules.<sup>67</sup>

## **D. Market Monitoring and Surveillance in the Secondary Market**

There is no market-wide surveillance for bond and note trading in the OTC market in Hong Kong, China.

The Market Monitoring and Surveillance Department at HKEX is responsible for monitoring the trading activities of Exchange Participants in cash and derivatives markets, as well as China Connect trading activities, and their compliance with rules and regulations, position limits, and large open position reporting requirements in derivatives contracts; and performing due diligence check on admission of market makers. It also cooperates with regulators in Hong Kong, China and the PRC on their investigation of local and cross-boundary market misconduct under China Connect. It also acts as the primary contact and representative of HKEX to deal with matters related to HKEX membership, such as exchanging information among members to perform intermarket and intra-market surveillance through the Intermarket Surveillance Group that was established to assist in the detection and prevention of fraudulent and manipulative acts and practices to protect investors and the public interest.

## **E. Bond Information Services**

Information on bonds and notes issued in Hong Kong, China are easily available for both retail and professional investors through a number of official online resources, as well as market intermediaries and information vendors.

### **1. Government Bond Programme Website**

The Government Bond Programme website (Figure 4.1) provides comprehensive information on the government's bond issuances for both the official Institutional Bond Issuance Programme and the Retail Bond Issuance Programme. The website features an overview of the purpose and objective of the issuance programs and contains an issuance calendar, tender information, indicative prices, as well as statistics and press releases (see also Chapter VII).

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<sup>67</sup> OTC trades of unlisted bonds do not need to be reported to SEHK. Off-market trades of listed bonds are only required to be reported to SEHK if they are executed by or between Exchange Participants (see Chapter 5 of the SEHK Trading Rules). An authorized ATS provider effecting trades (of listed or unlisted bonds) on its platform may (on a case-by-case basis) be required by the SFC to periodically report the trade statistics to the SFC under the ATS authorization.

**Figure 4.1: Hong Kong Special Administrative Region Government Bond Programme Homepage**

**Government Bond Programme**  
Government of the Hong Kong Special Administrative Region  
of the People's Republic of China

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Overview Institutional Bond Issuance Programme Retail Bond Issuance Programme Statistics News & Publications

**Government Bond Programme**  
Promote the further and sustainable development of Hong Kong's bond market

**Activities Calendar**  
Apr 2016  
S M T W T F S  
3 4 5 6 7 8 9  
10 11 12 13 14 15 16  
17 18 19 20 21 22 23  
24 25 26 27 28 29 30  
**1 April 2016**  
Tender for the re-opening of 5-year Government Bonds under the Institutional Bond Issuance Programme to be held on Wednesday, 13 April 2016

**Useful Links**  
• Office of the Financial Secretary  
• Financial Services and the Treasury Bureau  
• Hong Kong Monetary Authority

**News**  
**1 April 2016**  
Tender for the re-opening of 5-year Government Bonds under the Institutional Bond Issuance Programme to be held on Wednesday, 13 April 2016  
**9 March 2016**  
Tentative issuance schedule for HKSAR Government Bonds under the Institutional Bond Issuance Programme  
**2 March 2016**  
Tender results of the re-opening of 15-year Government Bonds under the Institutional Bond Issuance Programme  
**22 February 2016**  
Tender for the re-opening of 15-year Government Bonds under the Institutional Bond Issuance Programme to be held on Wednesday, 2 March 2016  
**25 January 2016**  
Interest rate of the first interest payment for iBond Series due 2016

**Tools & Resources**  
Issuance Schedule Bond Calculator Statistics

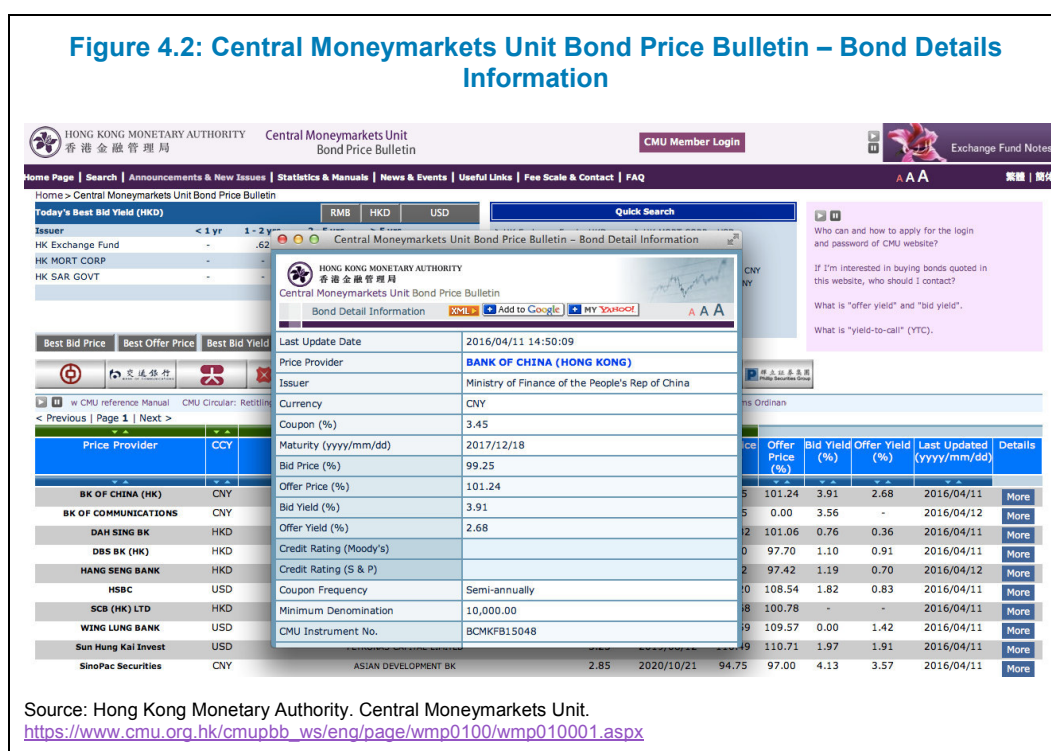
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Source: Hong Kong Special Administrative Region Government Bond Programme. <http://www.hkqb.gov.hk/en/index.html>

## 2. Hong Kong Monetary Authority

In addition to information on the Hong Kong Exchange Fund and its debt issuances, the HKMA also provides the CMU Bond Price Bulletin, a dashboard-style web page with news on CMU Instruments, quoted bid and offer prices (see Chapter III.K), and yields. Detailed information on bonds is viewable in a pop-up window for each of the instruments displayed on the page (Figure 4.2). The current Exchange Fund Note Information Memorandum is available for download by clicking the tab in the top right corner.

**Figure 4.2: Central Moneymarkets Unit Bond Price Bulletin – Bond Details Information**



Source: Hong Kong Monetary Authority. Central Moneymarkets Unit.  
[https://www.cmu.org.hk/cmupbb\\_ws/eng/page/wmp0100/wmp010001.aspx](https://www.cmu.org.hk/cmupbb_ws/eng/page/wmp0100/wmp010001.aspx)

### 3. Hong Kong Exchanges and Clearing Limited

HKEX provides, on its website under the Debt Securities tab,<sup>68</sup> selected general information on debt securities, including its Debt Securities Leaflet for download by interested parties. In addition, the section also contains the list of debt securities issued to the public and to professional investors, a glossary and frequently asked questions, as well as information on debt securities aimed only at professional investors, which are further referred to as Professional Debts.

## F. Yields, Yield Curves, and Bond Indices

### 1. Government Bond Yields and Yield Curves

Indicative pricing and benchmark yields of Government Bonds issued under the Institutional Bond Issuance Programme are available for download from the Government Bond Programme website.<sup>69</sup> The data is prepared in Excel format by the HKMA as section 9 of its Monthly Statistical Bulletin (Figure 4.3).

<sup>68</sup> See <https://www.HKEX.com.hk/eng/prod/secprod/debt/debt.htm>

<sup>69</sup> See <http://www.hkqb.gov.hk/en/statistics/statistic.html>

**Figure 4.3: Prices and Yields of Government Bonds Issued under the Institutional Bond Issuance Programme (End-of-Period Figures)**

**Table 9.4 : Prices and yields of Government Bonds issued under the Institutional Bond Issuance Programme<sup>1,2</sup>**  
機構債券發行計劃下政府債券的價格及收益率<sup>1,2</sup>

Table 9.4.1 End of period figures  
期末數字

(percent per annum)  
(年率)

			Indicative Prices 指示價格					Benchmark yields 基準收益率					Closing Reference Rates 收市參考價				
			2-year 2 年	3-year 3 年	5-year 5 年	10-year 10 年	15-year 15 年	2-year 2 年	3-year 3 年	5-year 5 年	10-year 10 年	15-year 15 年	2-year 2 年	3-year 3 年	5-year 5 年	10-year 10 年	15-year 15 年
2015	Jan	1月	0.360	0.639	0.897	1.552	-	0.374	0.624	0.876	1.546	-	-	-	-	-	-
	Feb	2月	0.407	0.743	1.254	1.687	-	0.399	0.739	1.248	1.687	-	-	-	-	-	-
	Mar	3月	-	0.741	1.150	1.590	-	-	0.741	1.122	1.576	-	-	-	-	-	-
	Apr	4月	-	0.620	1.182	1.628	-	-	0.623	1.138	1.638	-	-	-	-	-	-
	May	5月	-	0.616	1.126	1.701	-	-	0.608	1.115	1.711	-	-	-	-	-	-
	Jun	6月	-	0.535	1.087	1.788	-	-	0.542	1.105	1.836	-	-	-	-	-	-
	Jul	7月	-	0.613	1.156	1.844	2.170	-	0.621	1.168	1.862	2.179	-	-	-	-	-
	Aug	8月	-	0.620	1.122	1.803	2.103	-	0.620	1.122	1.802	2.095	-	-	-	-	-
	Sep	9月	-	0.440	0.854	1.534	1.783	-	0.444	0.853	1.533	1.785	-	-	-	-	-
	Oct	10月	-	0.692	0.854	1.525	1.828	-	0.696	0.866	1.551	1.851	-	-	-	-	-
	Nov	11月	-	0.790	1.206	1.578	1.862	-	0.792	1.206	1.589	1.866	-	-	-	-	-
	Dec	12月	-	0.817	1.304	1.662	1.937	-	0.860	1.307	1.675	1.940	-	-	-	-	-
2016	Jan	1月	-	1.061	1.395	1.833	2.001	-	0.994	1.371	1.794	1.927	-	-	-	-	-
	Feb	2月	-	0.745	1.108	1.383	1.822	-	0.744	1.108	1.382	1.822	-	-	-	-	-
	Mar	3月	-	0.765	0.909	1.318	1.717	-	0.730	0.904	1.283	1.681	-	-	-	-	-

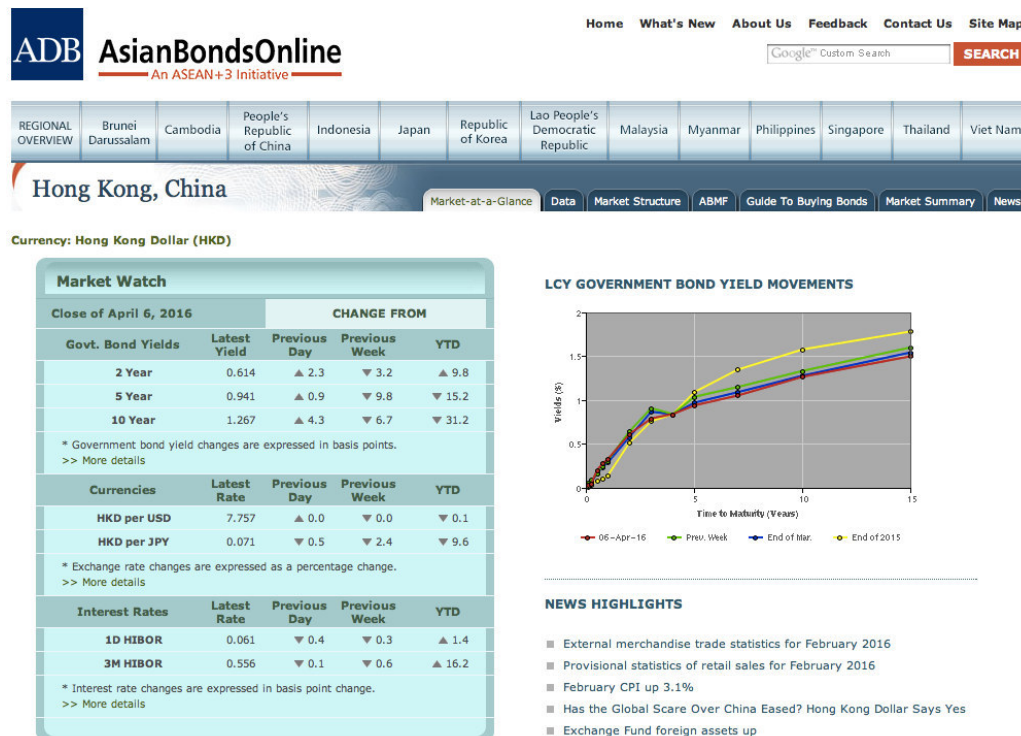
1. Figures powered by Thomson Reuters.

數據由湯森路透提供。

2. Calculation method and further information are set out in the Reference Manual for Government Bond Indicative Prices ([http://www.hkqb.gov.hk/en/other/documents/indicativeprices\\_manual.pdf](http://www.hkqb.gov.hk/en/other/documents/indicativeprices_manual.pdf)).  
計算方法及有關資料請參閱政府債券指示價格參考手冊(英文版本)([http://www.hkqb.gov.hk/en/other/documents/indicativeprices\\_manual.pdf](http://www.hkqb.gov.hk/en/other/documents/indicativeprices_manual.pdf)).

Source: Hong Kong Government Bond Programme, <http://www.hkqb.gov.hk/en/statistics/statistic.html>

**Figure 4.4: Government Bond Yields and Yield Movements on AsianBondsOnline**



CPI = consumer price index, LCY = local currency, YTD = year to date.

Source: AsianBondsOnline. Selected Government Bond Yields and Yield Movements.



In addition to yields for specific benchmark issues, an aggregate Government Bond yield curve for selected periods, as well as many more data points can also be accessed using the *AsianBondsOnline* website.<sup>70</sup> An example of the yield data and composite curve style of display is shown in Figure 4.4.

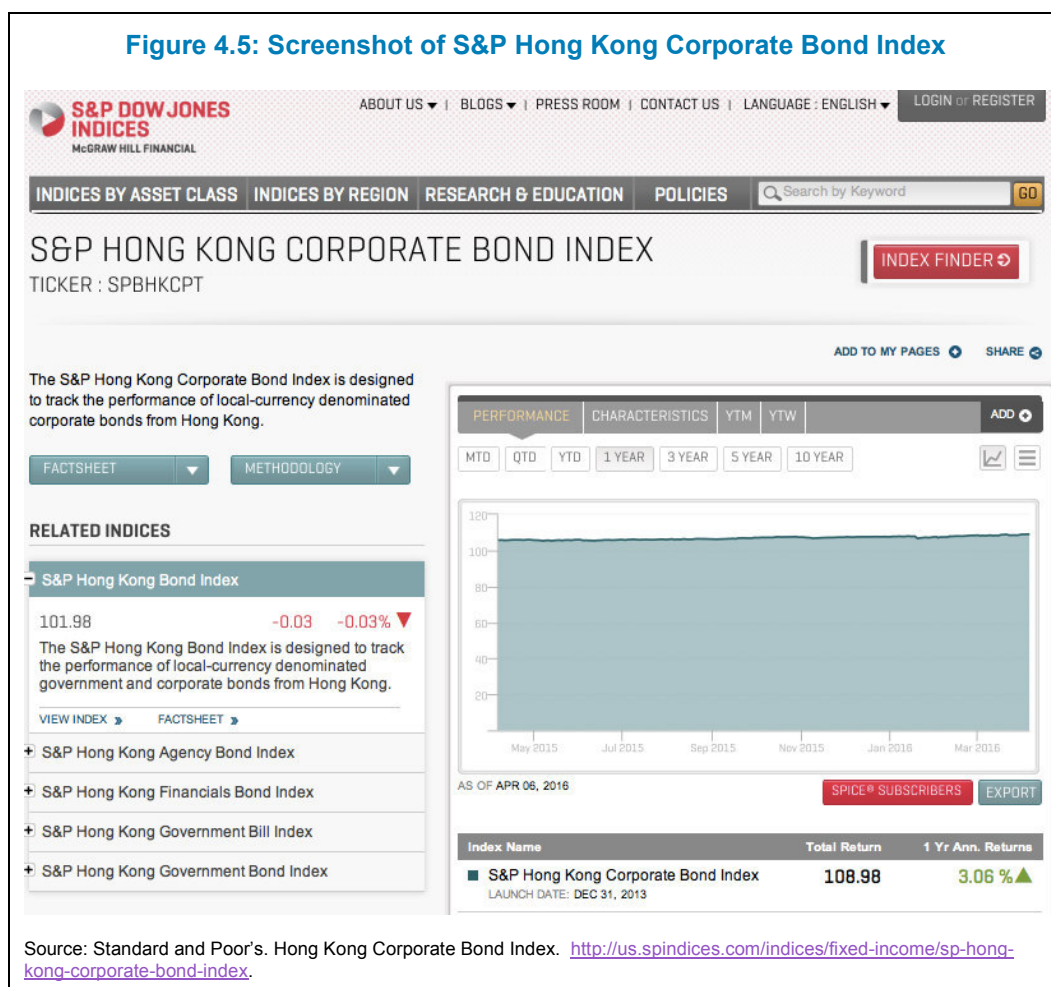
## 2. Other Bond Yields—Exchange Fund Bonds and Notes

HKMA also makes EFBN yields available for download from its website.<sup>71</sup> HKMA also publishes the yield data, as well as much other information for EFBNs, on its CMU Bond Price Bulletin web page. For details, please also refer to E.2 in this chapter.

## 3. Bond Indices in Hong Kong, China

HKMA does not issue official indices for the Hong Kong bond market. Instead, bond indices that include bonds and notes issued in Hong Kong, China are available from securities market participants and data vendors, respectively.

Figure 4.5: Screenshot of S&P Hong Kong Corporate Bond Index



The Citi Asian Government Bond Index (AGBI) comprises local currency Asian government bonds, providing a broad benchmark for the Asian sovereign market. The AGBI rules and methodologies are consistent with those of the World Government

<sup>70</sup> See [http://asianbondsonline.adb.org/singapore/data/marketwatch.php?code=government\\_bond\\_yields](http://asianbondsonline.adb.org/singapore/data/marketwatch.php?code=government_bond_yields)

<sup>71</sup> HKMA. Market Data and Statistics. <http://www.hkma.gov.hk/eng/index.shtml>

Bond Index in order to enable performance comparisons across sovereign debt markets. The index provides exposure to a broad array of countries and subindexes are available in any combination of currency, maturity, and rating. Coupon-bearing government bond issues with a minimum issue size of HKD800 million are included in AGBI and its subindexes.<sup>72</sup>

In turn, the S&P Hong Kong Corporate Bond Index (Figure 4.5) is an example of the bond indices tracked by securities market information providers, and available in the public domain.

## G. Repo Market

### 1. Repo Market Overview

The repo market in Hong Kong, China is relatively small when compared to lending conducted through the unsecured interbank and foreign exchange swap markets despite having the necessary infrastructure for, and no legal or tax impediments to, conducting repo. This is largely because the relevant institutions are more used to obtaining Hong Kong dollar funding through the two abovementioned channels. Nonbank financial institutions do not generally conduct repo in Hong Kong, China.<sup>73</sup>

There are generally no restrictions on participation in the Hong Kong, China repo market. Nevertheless, participation has been largely confined to financial institutions (particularly the banks) and money brokers and dealers. This notwithstanding, financial institutions are more used to obtaining funding via the unsecured interbank market or via foreign exchange swaps for two reasons. First, there has not been a large stock of government securities or central bank paper for banks to conduct repo in Hong Kong dollars. Secondly, since the Hong Kong dollar is pegged to the US dollar, which has much deeper and more liquid markets, banks can obtain Hong Kong dollar funding through the US dollar and foreign exchange swap markets with relative ease.

Repo transactions between financial institutions are sometimes conducted via inter-dealer brokers for reasons of convenience and anonymity, although banks also rely on other bilateral and tripartite repo services from time to time. Abundant Hong Kong dollar liquidity in the system in recent years has reduced banks' funding needs in general, whether in the form of unsecured lending or repos.

Banks are allowed to obtain temporary liquidity through the discount window provided by HKMA using repurchase agreements with EFBNs as collateral.

### 2. Acceptance of Standards

The Global Master Repo Agreement (GMRA) is the standard legal documentation used in the local repo market. Banks in Hong Kong, China are reportedly more used to executing GMRA bilaterally under their own entity names due to established practice. In other words, instead of using a Hong Kong, China annex, they typically execute a standalone GMRA for conducting Hong Kong dollar repo trades.<sup>74</sup>

<sup>72</sup> Citi Fixed Income Indices. 2016. *Index Guide*.

[https://www.yieldbook.com/f/m/pdf/citi\\_indices/Citi\\_Indx\\_Guide\\_20160304\\_WEB.pdf](https://www.yieldbook.com/f/m/pdf/citi_indices/Citi_Indx_Guide_20160304_WEB.pdf)

<sup>73</sup> Adapted from Executives Meeting of East Asia–Pacific Central Banks. 2014. *EMEAP Repo Markets: State of Play—A Report by the EMEAP Working Group on Financial Markets*.

[http://www.emeap.org/emeapdb/upload%5CWGMeeting%5CEMEAP\\_Working\\_Group\\_on\\_FinancialMarkets\\_Report\\_on\\_EMEAP\\_Repo\\_Markets\\_....pdf](http://www.emeap.org/emeapdb/upload%5CWGMeeting%5CEMEAP_Working_Group_on_FinancialMarkets_Report_on_EMEAP_Repo_Markets_....pdf)

<sup>74</sup> See Footnote 57.



### 3. Specific Repo Practices

This section summarises a number of relevant practices in the repo market in Hong Kong, China. Most repo transactions occur in the interbank (OTC) market. A certain number of repo transactions are conducted on SEHK.<sup>75</sup>

#### a. Type of Repo

Repo transactions in Hong Kong, China represent the classic repo type, which is the outright sale and simultaneous (re)purchase of securities.

At the same time, the underlying legal and taxation infrastructure in Hong Kong, China does not prohibit the pledged type of repo transaction.

#### b. Size and Tenure

Repo transaction may be conducted for any tenure or size, in line with market acceptance of such conditions. Owing to the fact that there is no specific Hong Kong, China annex to the GMRA, conditions are typically agreed bilaterally between counterparties.

#### c. Eligible Debt Securities as Collateral

There are no restrictions or limitation on the eligible securities in Hong Kong, China.

Most of the repo transactions among financial institutions are conducted using either government bonds or EFBNs. For the purposes of funding, use of other securities (e.g., corporate bonds, asset-backed securities, or equities) are not as common as these securities are either less liquid or subject to more volatile price movements.

The Hong Kong, China repo market infrastructure allows substitution of collateral during the term of the repo but it is not standard practice among participants.

For eligible securities in repo transactions between Authorized Institutions and HKMA, please see Section 4.

#### d. Closeout Netting

There are no specific prescriptions in Hong Kong, China for the closeout netting of repo transactions. However, provisions for closeout netting are commonly included in Master Agreements (e.g., ISDA Master Agreement) that bind the market participants to established practices.

#### e. Accounting and Tax Treatment

Under the tax laws of Hong Kong, China, stock borrowing and lending transactions (including repo transactions) where specific criteria are satisfied, require no stamp duty to be payable. This means the tax treatment is that of a loan rather than an outright purchase and sale of securities.

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<sup>75</sup> Adapted by ADB Consultants for SF1 from a 2016 ASEAN+3 SRO Working Group case study on repo markets, with the kind permission of the author.

The difference between the sale and (re)purchase amount is considered as interest income in substance, which may be subject to profits tax.

Most funding-driven repo transactions are conducted using EFBNs and government bonds, which do not attract any taxation even for outright purchases and sales.

#### f. Market Participants

Financial institutions in Hong Kong, China conduct repo transactions with both local and international market players. For the local market, clearing and settlement of repo transactions can be conducted through, amongst other channels, the bank repo platform administered by the CMU as delivery-versus-payment transactions.

The cash lenders tend to be money market funds, mutual funds, or treasury desks from banks, corporates, insurance companies, or the HKMA repo desk. The bond lenders include dealers and bond traders, hedge funds, proprietary trading desks, or repo desks.

The CMU also provides cross-border collateral management service with the global tripartite platforms, Euroclear, J.P. Morgan, and Clearstream. To further enhance the cross-border collateral management service, delivery-versus-payment links between Hong Kong's RTGS systems and the tripartite repo systems have been established to enable liquidity movements to be done in Hong Kong's RTGS systems while the collateral movements are done concurrently through the repo platform.

There are no restrictions on the entrance of foreign investors into the Hong Kong bond market for repo transactions.

### 4. Introduction of Intraday Repo under the Renminbi Liquidity Facility

In November 2014, the HKMA announced the provision of renminbi intraday liquidity to Authorized Institutions participating in renminbi transactions in Hong Kong, China via repo.<sup>76</sup>

Under an existing RMB Liquidity Facility, the HKMA had already provided overnight funds on a T+0 basis as well as 1-day and 1-week funds settled on a T+1 basis. In light of the increased volume of payments alongside the growth of the offshore renminbi market, the HKMA started to provide intraday renminbi funds of up to CNY10 billion to assist Participating Authorized Institutions in managing their renminbi liquidity and to promote efficient payment flows in Hong Kong, China. This also provided banks with greater flexibility in managing their payment flows upon the launch of the Shanghai–Hong Kong Stock Connect.

Participating Authorized Institutions may initiate a sale and repo transaction with the HKMA to obtain intraday renminbi funds. The HKMA will charge a fee, based on the actual time of usage, with reference to the prevailing overnight interest rate. The list of securities eligible for the previously existing renminbi liquidity facility was expanded to include renminbi bonds issued by the PRC's policy banks in Hong Kong, China.

In light of its experience operating the facility and given developments in the offshore renminbi market, the HKMA has made enhancements to the facility. Please refer to the HKMA website for more details.<sup>77</sup>

<sup>76</sup> Reference is made to the announcement of the new facility by HKMA at [www.hkma.gov.hk/eng/key-information/press-releases/2014/20141103-4.shtml](http://www.hkma.gov.hk/eng/key-information/press-releases/2014/20141103-4.shtml)

## H. Securities Borrowing and Lending

Since the introduction of the exemption from stamp duty for properly executed securities borrowing and lending (SBL) transactions, Hong Kong, China has emerged as a regional SBL center.

Legally, SBL falls under the covered short selling provisions in sections 171 and 172 of the SFO. According to the SFC Guidance Note on Short Selling Reporting and Stock Lending Record Keeping Requirements, a securities borrowing and lending agreement is defined in Schedule 1 of the SFO as an agreement whereby a person borrows or lends securities pursuant to an arrangement where the borrower undertakes to return securities of the same description to the lender or pay the equivalent value of the securities. The definition expressly includes a securities borrowing within the meaning of section 19(16) of the Stamp Duty Ordinance. Relief from payment of the Hong Kong, China stamp duty is available under section 19 of the Stamp Duty Ordinance, in which securities are borrowed pursuant to a stock borrowing and lending agreement.

SBL transactions in Hong Kong, China, may be executed on SEHK or using the CMU Lending Programme.

### 1. Securities Lending on Hong Kong Exchanges and Clearing Limited

The 6th Schedule to the SEHK Trading Rules contains the Securities Borrowing and Lending Regulations of HKEX.<sup>77</sup> An Exchange Participant shall be permitted to borrow or lend securities only in accordance with these regulations or the CCASS Rules (as the case may be) and, where the securities borrowing relates to Hong Kong stock, with applicable law and in particular the Stamp Duty Ordinance and the relevant Stamp Duty Interpretation and Practice Notes of the Internal Revenue Department of Hong Kong.

Compulsory stock borrowing to close out overdue positions in CCASS was introduced by HKSCC in May 1999. The underlying Compulsory Stock Borrowing and Lending Regulations are contained in Appendix 6 to the CCASS Rules. Participants require a stock lending account in CCASS (one per Participant). The opening of a stock lending account needs to be advised to the Collector of Stamp Revenue of the Internal Revenue Department in order for the lender to avail themselves of a stamp duty exemption (see also Section 4).

Collateral is required for all SBL transactions executed through SEHK. Normal SBL transactions will need to be collateralized at 100% at all times; transactions in support of short sales (which are defined in the 11th Schedule to the Trading Rules) are required to be collateralized at 105%. Uncovered securities borrowing positions are required to be marked to market at least daily, and an increase of the amount of collateral to 100% or 105% is required where the value of the collateral falls under the 100%, or 105%, respective levels. Collateral of higher value than the 100% or 105%, respectively, may be released by the lender to the borrower.

In contrast, Compulsory Stock Borrowing transactions in CCASS do not require HKSCC to deliver any form of collateral to the Lender.

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<sup>77</sup> See <http://www.hkma.gov.hk/eng/key-functions/monetary-stability/liquidity-support-to-banks.shtml>

<sup>78</sup> See [http://www.hkex.com.hk/eng/rulesreg/traderules/sehk/documents/sch-6\\_eng.pdf](http://www.hkex.com.hk/eng/rulesreg/traderules/sehk/documents/sch-6_eng.pdf)

## 2. Central Moneymarkets Unit Securities Lending Programme

CMU operates a Securities Lending Programme for debt securities issued by the private sector.<sup>79</sup> This program provides a mechanism for CMU Participants to lend or borrow CMU Instruments and Government Bonds issued under the Government Bond Issuance Programme (Eligible Instruments) through the CMU. All CMU Participants may participate in the program as a Lender. However, only Market Makers for Eligible Instruments under this program can borrow Eligible Instruments. Any Recognized Dealer for Government Bonds who is also a CMU Member may participate in the program as a lender and/or Borrower.

The maximum aggregate amount of each Loan of Eligible Instruments is 20% of the total issue size of those Eligible Instruments.

Borrowers shall be required to provide collateral but may substitute collateral pursuant to the rules of the Programme. Only EFBNs and those CMU Instruments eligible for repo under the discount window are eligible Collateral. If the Eligible Instruments are issued by the borrower itself, its subsidiaries, its holding company, or any subsidiary of that holding company, such Eligible Instruments are not allowed to be used by the Borrower as Collateral. All Borrowed Instruments and Collateral will be marked to market on a daily basis. A Borrower is required to top up any shortfall to ensure continuous compliance with the haircut requirements.

Lenders transfer Eligible Instruments they are willing to lend into their Lending Account, while Borrowers send Borrowing Requests on the required securities into the CMU system, which then matches and concludes the transaction.

For a detailed description of the Securities Lending Programme, interested parties are advised to download the CMU Reference Manual or check the descriptions on the HKMA website.

## 3. Eligible Debt Securities

For SBL transactions on SEHK, or via the compulsory stock borrowing in CAASS, only securities deposited and settled at CCAAS are eligible.

In the CMU Programme, Eligible Instruments are those CMU Instruments and Government Bonds issued under the institutional and retail tranches of the Government Bond Issuance Programme arranged by HKMA. The issue size of each of those eligible CMU Instruments must be of or over HKD500 million equivalent and have at least one CMU Participant who has agreed to act as the Market Maker of the issue.

## 4. Tax Treatment

Similarly to repurchase transactions, SBL transactions are considered loans rather than outright sales of securities. As such, no stamp duty is payable, provided that the lender has registered their lending agreement with the Internal Revenue Department.

The fee income for the lender from the SBL transactions may be subject to profits tax, unless the underlying securities qualify for a tax exemption.

<sup>79</sup> Adapted from CMU. 2016. *Reference Manual*. <http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/infrastructure/cmu.shtml>

## 5. Pan-Asian Securities Lending Association

The Pan-Asian Securities Lending Association (PASLA)<sup>80</sup> is an association of firms that are active in the business of borrowing and/or lending securities of Asian markets. PASLA was founded in Hong Kong in 1995, as Hong Kong is the regional headquarters for many financial firms, and it was and remains easy for borrowers and lenders to meet and resolve any issues; moreover, the credibility of counterparties in Hong Kong has always been high. Its meetings are held in Hong Kong.

At the time of the compilation of this bond market guide, PASLA had 63 member firms made up of 18 lenders, 35 borrowers, and 10 others who are domiciled across multiple continents. PASLA membership is open to both international firms, which are active in several markets, and local firms, which are active primarily in their home market.

PASLA, as a collective group of major firms in the industry, provides an important benefit to Asian securities regulators, stock exchanges, and monetary authorities by providing an industry consensus on issues that affect the development of the securities lending business. PASLA also provides country profiles and market information to its members.

## I. Interest Rate and Fixed-Income Futures

Exchange traded interest rate futures are available in the Hong Kong bond market, while futures on fixed income products were discontinued.

### 1. Interest Rate Futures

HKFE's introduction of 1-Month HIBOR futures contracts on 20 October 1998 and 3-Month HIBOR futures contracts on 26 September 1997 provides a set of interest rate products that allow market participants to manage their interest rate exposures more effectively.

The 1-Month HIBOR and 3-Month HIBOR futures contracts are based on the 1-Month and 3-Month HIBORs (Hong Kong Interbank Offered Rate), which are the benchmarks for short-term interest rates in the Hong Kong dollar money market.

HIBOR futures are traded on the Hong Kong Futures Exchange Limited, a wholly owned subsidiary of HKEX. Details on the trading practices, contract specifications, trading hours, and other relevant information is available from the HKEX website.<sup>81</sup> Trading fees and commissions for HIBOR futures are also available on the HKEX website.<sup>82</sup>

### 2. Fixed-Income Futures

In December 2014, HKEX announced it would discontinue trading in its 3-year EFN Futures because the HKMA would stop issuing 3-Year EFNs in January 2015.

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<sup>80</sup> See <http://www.paslaonline.com>

<sup>81</sup> See <https://www.HKEX.com.hk/eng/prod/drprod/DMPProducts.htm>

<sup>82</sup> See <https://www.HKEX.com.hk/eng/prod/drprod/hkifo/fees.htm>