

Responses to Follow-up Questions from the FA Panel

Question (a): -

In 2011, Category A and Category B brokers accounted for 67% and 27% of the total short selling turnover respectively. Category A brokers are the top 14 Exchange Participants of the Stock Exchange of Hong Kong (SEHK) and Category B brokers are the top 15 to 65 Exchange Participants. The remaining Exchange Participants (i.e. Category C brokers) accounted for about 6% of the total short selling turnover in 2011.

Question (b): -

Short selling plays an important role in today's financial market. The International Organisation of Securities Commissions (IOSCO) published two reports on short selling, namely "Report on Transparency of Short Selling" in June 2003 and "Regulation of Short Selling" in June 2009. In the IOSCO reports, it is recognised that short selling can contribute to market efficiency and the benefits of short selling include:

- helping to maintain efficient pricing by correcting the price of an over-valued security;
- facilitating liquidity provision (e.g. by going short, a market maker can meet a customer buy order when it does not hold the relevant securities in inventory, thus facilitating liquidity and continuous trading);
- providing a risk management tool for those needing to manage market risk;
- keeping prices of related securities properly aligned (e.g. through arbitrage); and
- adding to overall liquidity and trading capacity.

Question (c): -

Securities borrowing and lending is a bi-lateral transaction between lenders and borrowers. Securities lenders are mostly long-term institutional investors. These investors usually employ an agent (such as a custodian bank) to arrange and manage lending of securities. We understand that some brokerage firms also provide securities lending services for their customers. Securities can be borrowed through custodian banks and brokerage firms offering securities lending services.