



HONG KONG MONETARY AUTHORITY
香港金融管理局

Our Ref: B1/15C

16 December 2011

To: The Chief Executive
All Market Makers and Eligible Market Makers in the Exchange Fund Bills
and Notes market
All Primary Dealers in the Institutional Government Bonds market

Dear Sir/Madam,

**Trading in the Exchange Fund Bills and Notes /
Institutional Government Bonds Markets**

As you know, the Exchange Fund Bills and Notes (EFBN) Programme and the Institutional Government Bonds (GB) Programme both have a market making system to help maintain liquidity in the secondary markets. For the EFBN market, 23 market makers (MM) have been appointed by the Hong Kong Monetary Authority (HKMA) and they are obliged to quote bid and offer prices to investors during normal trading hours. Likewise for the Institutional GB market, 12 primary dealers (PD) have been appointed with similar functions by the HKMA on behalf of the Government.

As MMs and PDs are expected to be active in trading EFBNs and GBs in the secondary market, they are expected to meet a number of quantitative and qualitative criteria (including minimum turnover requirements) in the respective market. During previous market consultations on refinements to the market making system, there was some concern as to the use of “round-tripping” trades. These are trades which appear to have no economic substance and appear to serve no purpose other than to boost the turnover figures of the institution involved. All along the HKMA has considered this practice unacceptable and the HKMA has made it clear in the past that trades involving this kind of practice will be excluded for the purpose of evaluating the institution’s turnover performance. In this connection, the HKMA has taken measures to enhance the MM system by including a broader range of assessment criteria other than turnover and removed some institutions engaging in such trades from the list of eligible MMs.

The purpose of this circular is to remind Authorized Institutions, once again, that they must conduct their business with a high degree of professionalism and integrity. In order to ensure that this is indeed the case, your institution should now review your trading practices in the EFBN and GB markets

and take steps to ensure your internal controls are effective in preventing and detecting any round-tripping trades. The HKMA will continue to monitor these markets and to ensure that all institutions appointed as MMs or PDs continue to contribute to market liquidity in accordance with the terms and conditions of their appointments.

Yours faithfully,

Meena Datwani
Executive Director (Banking Conduct)

c.c. The Treasurer