

November 11, 2004

The Securities and Futures Commission
8th Floor, Chater House
8 Connaught Road Central
Hong Kong

Dear Sirs,

Consultation Paper on Proposed Measures to Address Risk Arising from Securities Margin Financing

We would like to extend our sincere appreciation to SFC's Working Group for working on the Consultation Paper and giving us an opportunity to respond to its contents.

As an active provider of margin financing, we fully support SFC's continuous effort to strengthen Hong Kong's position as a premier international financial center. We do appreciate the need to improve the level of investor protection by setting higher standards for regulating providers of securities margin financing ("SMF"). We feel obliged to express our views on and concerns over the Consultation Paper. Our comments are as follows:

Limit on Re-pledging of Client Collateral

We agree with the Commission that limit on re-pledging is positive toward protecting investors against excessive lending practices. We are nonetheless concerned that setting a re-pledging limit at too low a level may be detrimental to healthy market growth. In our opinion, it is important that the limit be set at an appropriate level so that the SMF providers will have the flexibility to cope with market fluctuations and guard against credit risk of their margin-financed clients. By way of illustration, even if a SMF provider limits its lending solely to loans collateralized by high-quality stocks and adheres to bank's financing ratios of between 40% and 60%, the re-pledging limit of over 200% would still be breached easily, especially in a bull market. Hence, we take the view that the re-pledging limit should not be in any case lower than 200%.

Moreover, we believe that the operational work associated with the proposed measures may not only incur significant compliance cost but also bring about practical difficulties for a SMF provider to cope with its daily funding activities.

Under the proposed re-pledging limit measure, a SMF provider is required to withdraw a particular amount of collaterals from its bank for compliance purposes. It is common knowledge that margin loans offered by a SMF provider fluctuate significantly from day to day depending on the clients' demand. Consider that a SMF provider has on a particular day determined the required re-pledging amount with its bank and on the following finds that the aggregate margin loan balance on the second day is far higher than that of the previous day. Under the existing rules, the SMF provider would simply re-pledge additional collaterals to the bank to support such additional financing. By contrast, under the proposed requirement, it appears that the SMF provider would first have to withdraw collateral from its bank and then re-deposit other collateral of a different amount to cover the new financing activities. This will incur considerable bank charges and increase daily operational work to the SMF provider. We seek your clarification in this respect.

Adjustments on FRR Haircut Rates

The proposal entails a significant increase in haircut percentages for non-HSI/HSHK LargeCap Index stocks. As the proposed re-pledging limit has already imposed restrictive limits on the financing activities of a SMF provider and the current concentrated discount factor has also addressed the concentration risk, we find the proposed rates excessively high. We believe that the haircut percentages should be increased by no more than 50% of the original rates (i.e. if the original haircut rate is 20%, we consider increasing it to over 30% inappropriate) with the concentration adjustment maintained. It is because the risks inherent to concentration or diversification when lending against those non-HSI/HSHK Large Cap Index stocks vary from one SMF provider to another. In addition, the classification by market capitalization or by inclusion in an index does not address the fact that some non-index stocks do have sound fundamentals.

We are surprised to note that over 80% of the stocks currently listed in the Main Board will be subject to a proposed haircut ratio of 80%. It is seemingly contrary to the continuous effort by the Hong Kong Government and the Exchanges to promote local listing in Hong Kong. Applying a high haircut rate to a large group of stocks might increase the ease of regulating, but it could significantly reduce market liquidity, discourage trading and cause potential disruption

to market orders. In our opinion, these are against the will of general investors and are not beneficial to the development of the financial markets as a whole.

Additional Notification requirements to the SFC

While we agree that increasing transparency of SMF activities in the market is justified for more monitoring measures, these measures should not be administratively and operationally excessive and costly to the SMF providers. The proposed measures require that notifications be made to the Commission if, for a continuous period of 2 weeks, the aggregate outstanding margin loans receivable from its top 20 margin clients that are secured against illiquid collateral has exceeded 50% of the sum of its shareholders' funds and approved subordinated loans or the SMF provider has utilized 80% or more of its available credit line. To our understanding, the existing financial resources requirements call for monthly submission of financial resources return and disclosure of credit facility. We take the view that monthly notification limited to financing on "illiquid collateral" is a more reasonable measure.

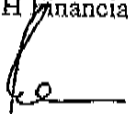
In the context of the fast-changing regulatory environment globally, it is always important to strike a balance between prudence and flexibility within the market. While we praise a regulator's effort to pursue global standards, we believe that it is equally, if not more, important to address concerns that are local and unique. In Hong Kong, it is essential that the competitiveness of the brokerage firms, particularly those locally based, is not compromised when new regulatory measures are introduced.

We thank you again for offering us this opportunity to express our views and provide our comments. We are committed to helping to make Hong Kong's financial markets fair, competitive, and well-regulated for both service providers and investors alike. If you require further clarification on any of the above, please do not hesitate to contact the undersigned.

Yours faithfully,

For and on behalf of

CASH Financial Services Group Limited


Ben Cheng

Head of Operations