

State Street Response to HKEX T+1 Consultation Paper -- “Accelerated Settlement for the Hong Kong Cash Market”

Q1 - Do you support the proposed arrangements under the T+1 settlement cycle across the Cash Market trade lifecycle? In particular, please comment on: (i) Trade amendment; (ii) Post Trade; (iii) Risk management; (iv) Other processes, including reporting, corporate actions, stock conversion arrangement and stamp duty arrangement. Please give reasons for your views.

State Street supports a carefully managed transition to T+1 in Hong Kong, minimizing as much as possible settlement gaps with other major financial jurisdictions. The move to T+1 should be effective as soon as practically possible and should be coordinated with all relevant stakeholders moving simultaneously to a harmonised settlement cycle.

Based on the experience in the US, we would like to stress that the implementation of T+1 settlement is a significant undertaking that requires careful planning and coordination by market participants in conjunction with financial market infrastructures. Due to the need for resource planning and allocation, the timing decision should be carefully considered in consultation with industry while also keeping in mind other concurrent T+1 migrations efforts in the European Union, Switzerland and the UK. (Please also refer to our response in Question 5 on the proposed timeframe).

Regarding the proposed T+1 operating model in Chapter 5 of the consultation paper, at a high level, we wish to highlight the following:

- T+1 settlement cycle in Hong Kong under the proposed compressed timeline will effectively mean a T+0 operational environment for European and US investors. This will require the industry’s commitment to apply technology across the settlement value chain and the post trade settlement infrastructure, and the implementation of technology solutions and automation (e.g. the proposed workflow tool solution in Exhibit 2) to alleviate some of the compressed timing related concerns.
- Matching and settlement mechanisms will need to be improved to cater for the settlement compression. Potential solutions include real time settlement and real time matching. Alternative solutions may include additional batches in both matching and settlement. This will significantly increase the efficiency of post-trade systems and allows more time for foreign investors in other time-zones to react.
- In addition, cutoff times will need to be mutually agreed across regulatory authorities and market infrastructure to ensure Hong Kong continues to remain

attractive for foreign investors. Ultimately, a complete settlement requires both the movement of cash and securities. It is important to ensure the market intermediaries handling the cash portion are also part of the working group discussions.

Q2 - Do you have any comments on the assessment of the implications for Exchange Traded Products (ETPs) and Stock Options under the proposed T+1 settlement cycle? In particular, please comment on: (i) Guiding principles for the ETP primary market; (ii) Buy-in considerations for ETPs; and (iii) Stock options (including exercise and assignment). Please give reasons for your views.

State Street welcomes HKEX's consideration of the implications of T+1 settlement for Exchange Traded Products (ETPs), and is supportive of the proposed guiding principle that ETP primary market settlement timelines should, where feasible, align with or move as close as practicable to the T+1 settlement cycle used in the secondary market. We agree that a resilient, efficient and well-coordinated primary market operating model is important to support the broader transition of Hong Kong's ETP ecosystem to T+1, particularly given the role of ETF creation and redemption activity in supporting orderly market functioning and for secondary market liquidity.

At the same time, we would highlight that the ETP primary market involves a broader and more complex set of operational dependencies than secondary market trading. Creation and redemption orders typically require coordination among multiple stakeholders, including the issuer, participating dealers, custodians, trustees, transfer agency / registrar functions and, where relevant, other service providers. This is consistent with HKEX's observation that creation and redemption processes often involve multiple parties and that close coordination and alignment across all parties will be important in a T+1 environment.

In practice, many creation and redemption workflows continue to involve manual, sequential or partially manual processing steps, including order validation, basket confirmation, settlement instruction processing, cash and securities movement, reconciliation, and exception handling. Accordingly, while we support the direction of travel toward accelerated primary market settlement, the ability of ETF issuers to design and implement an accelerated primary market workflow will depend not only on issuer readiness, but also on corresponding process improvements across the wider ETF servicing ecosystem.

In particular, support from key stakeholders such as custodians, trustees and transfer agency / registrar service providers will be critical. These parties will need to review their

own operating models, cut-off times, service levels, system capabilities and exception-management processes to ensure that ETF creation and redemption activity can be processed within a compressed settlement timeline. State Street therefore encourages HKEX to recognise that implementation of accelerated ETP primary market settlement should be approached as an end-to-end ecosystem change, rather than as an issuer-only operational change.

State Street also agrees with HKEX's emphasis on greater digitalisation and a reduction in manual or paper-based procedures across the ecosystem. Enhancements that promote automated and streamlined workflows will be important to reduce operational risk, improve processing certainty, and support smoother settlement under shortened timelines. Where technology development or system enhancement is required by custodians, trustees, transfer agents / registrars, participating dealers or other stakeholders, it will be important to provide sufficient implementation lead time and appropriate transition buffers. This will help stakeholders assess requirements, secure resources and budget, complete technology changes, conduct testing, update operating procedures, and coordinate documentation or contractual changes where necessary.

For these reasons, State Street supports a principles-based approach under which ETP primary market settlement timelines are encouraged to align with T+1 where operationally feasible, while allowing flexibility for cases where full alignment is not immediately achievable. In such circumstances, settlement timelines should move as close to T+1 as practicable, supported by clear and predictable cut-off times, appropriate industry guidance, coordinated stakeholder readiness, and sufficient implementation lead time.

Overall, State Street is supportive of the transition toward accelerated ETP primary market settlement as part of Hong Kong's broader move to T+1. We believe the successful implementation of this model will require coordinated action across all parties in the ETF primary market lifecycle, with particular focus on process redesign, automation, stakeholder readiness and sufficient time buffers for any required technology development.

Q3 - Do you have any comments that consequential amendments should be made to the Listing Rules to reflect the arrangements proposed under the T+1 operating model?

[No comments]

Q4 - In assessing your circumstances for a T+1 transition, are there any other key topics, perspectives or types of market participants which you believe are relevant to highlight, that have not been covered in Exhibit 1 and paragraphs 110-113? Please share your views.

While we welcome HKEX's efforts to develop an industry-wide guidance to support the T+1 transition in Hong Kong, we note that currently there is no communication platform/mechanism set up for relevant stakeholders to come together to work through the wide range of topics that is needed to effectively plan for T+1.

Draw from our experiences from the US processes, we would recommend HKEX consider the following:

- **Develop a multiyear industry planning schedule** that involves numerous working groups with focus on different topics (settlements, securities lending, FX, ETFs, asset servicing);
- **Clear mandates from the regulator(s)** to push for firms to adopt same-day affirmation, improve cut-off discipline, invest in automation and straight-through processing etc;
- **Establish an industry command centre** to ensure a smooth conversion by providing support prior to, during and post implementation, sharing conversion status information and increase transparency into participant activity. The command centre can also serve as a central check point for issue identification and socialization and included various progress reports.
- **Establish industry best practices** in using automation to accelerate trade affirmation, real time allocation and confirmation workflows, and earlier funding and securities borrowing decisions to reduce manual exceptions and improve overall processing quality.

As we shared in our previous submission, one of the key factors that made the transition to T+1 a success in the US was close industry coordination through joint trade association/ industry forums. We encourage HKEX to establish similar industry-wide collaboration, topical working groups and deep-dive sessions, and change management mechanism to ensure timely identification of issues and the development of potential solutions. State Street looks forward to actively participate in these industry forums to collectively identify issues, craft solution, define measures of success and shape timeframes as part of a high-level roadmap.

In addition, we would like to highlight specific comments on two topics below that may best be handled through industry deep-dive discussions among relevant parties to effectively explore and resolve areas of concerns:

1) Securities Lending

The proposed transition to T+1 in the Hong Kong market presents notable challenges for securities lending. The current auto buy-in construct under CCASS introduces systemic constraints that may be exacerbated by the compressed timeline.

Key Risk Dimensions - These risks run counter to the initiative's stated goal of enhancing market efficiency and vibrancy and include:

- **Settlement Risk:** The shortened cycle increases the likelihood of settlement fails for securities on loan.
- **Liquidity Risk:** Lenders may reduce participation or retain greater inventory to manage settlement exposure, shrinking lending pools.
- **Operational Risk:** Operational complexity may deter market participants, undermining market liquidity.

Strategic Recommendations - To mitigate these concerns, the following options are proposed, grouped by feasibility and stakeholder involvement:

Short-Term Operational Adjustments

- **Partial Settlement Flexibility** - Allowing the partial settlement of available inventory can reduce fail rates and associated costs, improving overall settlement probability.
- **Easing Buy-In Penalties and Expanding Exemptions** - Aligning with practices in regional markets such as Australia and Japan, where fails may roll without immediate action, could reduce punitive costs and enhance resilience.

Medium-Term Infrastructure Enhancements

- **Transition to Continuous Net Settlement (CNS)** - Upgrading CCASS from batch processing to CNS could improve operational flexibility and reduce risk in stock lending and OTC movements.
- **DLT-Based Trade flow Processing (e.g., SYNAPSE)** - Leveraging distributed ledger technology for sale processing, recall issuance, and SBL review could streamline workflows. However, this would require significant investment by market participants.

Long-Term Policy Considerations

- **Lender of Last Resort Mechanism** - While unlikely given current HKEX priorities, a backstop facility could address systemic shortfalls.

To ensure a successful transition, we recommend initiating a multi-stakeholder dialogue involving HKEX, custodians, and lending participants. A phased implementation approach, coupled with targeted infrastructure and policy enhancements, will be critical to balancing market stability with operational resilience.

2) Exception Handling

The topic of exception management and settlement failing was discussed in the consultation paper at a high level where details are still lacking on how buy-in or other fail management processes will be managed under T+1. We recommend HKEX to organize separate deep-dive sessions on various relevant topics included but not limited to: timing provisions for handling exceptional cases, automated exception process, change in buy-in exemption etc.

Q5 - Do you consider the timeframe to be sufficient for you to prepare for T+1 to become effective in Q4 2027, given the advance visibility and lead time provided? Do you have any comments on the discussion and implementation approach? Please share your views on the proposed approach and timeline.

Regarding the timing of T+1 implementation for Hong Kong, we would caution that the proposed Q4 2027 timeline coincides with the T+1 implementation in UK, Switzerland and Europe. Furthermore, this also coincides with various large scale initiatives in the US: Treasury Clearing Q2 2027 and DTCC Modernization (partial settlements) Q3 2027 and 2028. This will create a significant resource challenge for the industry and we encourage HKEX to soon establish an industry mechanism where the timing decision can be discussed among market participants. Our experience with the US and Canada's T+1 implementation is that it required a multi-year effort with numerous working groups addressing different financial products and asset administration processes (settlements, securities lending, FX, ETFs, asset servicing).

Supplemental Qs

QA - Do you agree that the proposed workflow tool solution (as set out in Exhibit 2) would facilitate the implementation of a shortened settlement cycle under T+1? Please give reasons for your views.

We welcome HKEX's initiative to develop additional tools to facilitate industry implementation of T+1. However, we would stress that for any proposed tools or solutions,

they should be made optional rather than mandatory, and should be made interoperable with other commercially available solutions.

QB - Would you consider adopting the following components described in the proposed streamlined workflow under Exhibit 2 to better prepare for the T+1 implementation? (i) Matching; (ii) Centralised SSI Repository; (iii) SI Automation; (iv) Dashboard for MIS. Please give reasons for your views and share your considerations relevant to your decision.

[No comments]