NOTICE FOR SOLICITATION OF PUBLIC COMMENTS
WIDENING OF SCRIP LEVEL CIRCUIT BREAKERS, AND
INTRODUCTION OF INDEX BASED MARKET HALTS

Pakistan Stock Exchange Limited (PSX) is contemplating to introduce Index Based Market Halts, in a phased manner by widening the existing scrip level Circuit Breakers from 5% to 10% within a span of six months.

CIRCUIT BREAKERS—PSX PRESENT POSITION

A Circuit Breaker refers to a measure used by stock exchanges to avert panic selling or over-exuberant buying. After the stock’s price has risen or fallen by a certain percentage, many exchanges across the globe activate restrictions or trading halts. PSX management has imposed a circuit breaker of 5% or Rs. 1/= whichever is higher, for the purpose of upward/downward price fluctuations in the stock price from the closing price of the previous day. It may be noted that this present system operates only on individual scrip level and not at the index level.

INDEX BASED MARKET HALTS

Index based Market Halt is an index-based circuit breaker system, which brings to halt trading in all equity and equity derivative markets in case of an excessive volatility, large price movements or steep swing in share movements of the designated index.

PROPOSAL UNDER CONSIDERATION—SOLICITATION OF PUBLIC COMMENTS

A phased manner approach for widening of existing Circuit Breaker, followed by induction of Index Based Market Halts is under consideration at PSX Board. Given below are key aspects / salient features of the subject mechanism based on KSE30 Index:

**Phase-1 (Months 1-3)**

- The daily scrip level circuit breaker will be enhanced from 5% to 7.5%, and
- Index Based Trading Halt will be made operational on the basis of 5% index movement.
- In case KSE-30 Index continues to trade 5% up or down for consecutive 5 minutes from its opening index value, there will be a trading halt for 30 minutes. Such trading halt will not be applicable in case the movement takes place in the last 1 hour of the market. In case of a market halt, following procedures are proposed to be adopted:
  - All equity and equity derivative markets will be suspended
  - All orders will be cancelled
  - All margins and Mark-to-Market losses will be collected

Page 1 of 2
The market will have a 5 minutes pre-open before its Opening
- Only those UINs, which have met the payment obligations, shall be eligible for trading after resumption of trading for that day

- For the rest of the day, the following restrictions will be observed:
  - Individual scrips will be allowed to be traded up to 7.5% up or down from its previous day closing price
  - The KSE30 Index can fluctuate 7.5% (circa) up or down from its previous day closing price

**Phase-2 (Months 4-6):** The Exchange will operate in similar manner as that of Phase-1 with following parameters:

- The daily scrip level circuit breaker to operate on 10%, enhanced from 7.5%, and;
- Index based trading halt will be made operational on the basis of 7.5% index movement, in the similar manner described in Phase-1.

  For the rest of the day, the following restrictions will be observed:
  - Individual scrip will be allowed to be traded up to 10% up or down from its previous day closing price
  - The KSE30 Index can fluctuate 10% (circa) up or down from its previous day closing price

The Market Participants are requested to kindly send their input, assessment, suggestions and feedback to undersigned in writing or e-mail their comments at sani.khan@psx.com.pk latest by 1:30 p.m. April 15, 2016.

Sani-e-Mehmood Khan
General Manager,
Market Development & New Products

PS: In order to further facilitate the understanding of the subject matter, a detailed presentation along with consultation papers of the said process has already been made available in the sub-section: "Presentation and Product Papers" of the main section: "Product & Services" of PSX website.

Copy to:
PSX Website
Commissioner, Securities Market Division
Mutual Funds Association of Pakistan
Members, Divestment Committee of the Exchange
Chairman, Market Development and New Product Committee of Exchange
April 15, 2016

Sani-e-Mahmood Khan
General Manager
Market Developments & New Products
Pakistan Stock Exchange

Sub: Comments on Widening of Circuit Breakers & Index Based Trading Halts

Dear Sir

With reference to your notice no PSX/N-2025 dated April 1st, 2016 please find comments from CFA Society Pakistan on the subject matter. We have solicited advice from our parent organization CFA Institute\(^1\). Our views in this letter reflect and are aligned with the global positions of CFA Institute. CFA Institute represents the views of investment professionals before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues that affect the efficiency, integrity and accountability of global financial markets.

CFA Society Pakistan Positions referred to as CFASP
We broadly agree with the principles for trading venues to constrain trading and manage excessive volatility. However, we also note that while trading halts are an important safeguard for trading venues to incorporate, they can be disruptive to trading activity and can slow down the price discovery process. For example, mechanisms to inhibit extreme price movements can impede price discovery at times of breaking fundamental news; as limits are hit, the natural price adjustment process can be constrained. Therefore, trading halts and circuit-breaker systems should be seen as a mechanism of last resort to stabilise markets.

Trading halts and circuit-breaker mechanisms should be implemented in a harmonised fashion across trading venues to provide investors with similar expectations and safeguards on whichever venue they trade.

Trading venues should publicise the operating mode of trading halts. Such disclosure provides needed transparency to investors over the trading environment and the safeguards present. Trading venues should also establish guidelines for breaking trades and disclose such policies to investors.

\(^1\) CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The not-for-profit organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. CFA Institute has over 136,200 members in 145 countries and territories, including 129,800 CFA charterholders, and 147 member societies. CFA Society Pakistan is a member society of CFA Institute. For more information, visit www.cfainstitute.org.
CFA Society Pakistan further recommends that circuit breakers should be widened gradually and should not stay for the whole trading period. Both trading halts and circuit breakers should be removed after cooling off period and let the market continue with its price discovery function. We believe freezing the stock price at the lock price is tantamount to closing the market in that particular script and such interventions could also accentuate financial imbalances.

Finally, we suggest that as the calibration of circuit breakers for the Pakistan stock market evolves, the authorities should consider fine-tuning the framework to take into account liquidity factors at the individual stock level. For instance, the price bands should be wider for relatively illiquid stocks (which typically have higher volatility and lower market capitalisation) than the most liquid stocks (typically the most heavily traded, large capitalisation stocks and that also have lower information-based volatility).

Additional References
We wish to provide additional references for your due consideration. Our colleague Alan Lok, CFA, Director of Capital Markets Policy at CFA Institute, recently conducted research on China’s introduction of a draft regulation on circuit breakers in September 2015. We would like to point your attention to his blog post on that development, which provides good basic background on circuit breakers in general (concerns, positives, negatives etc.) and a summary of our position. His post can be accessed at: https://blogs.cfainstitute.org/marketintegrity/2016/01/14/chinas-circuit-breaker-boon-or-bane/

As further background reference we have also attached three documents drawn from international regulators and research houses:
1. “Market Interventions During the Financial Crisis: How Effective and How to Disengage?”
   – Chapter Three extracted from the Global Financial Stability Report - Navigating the Financial Challenges Ahead, published in October 2009 by the International Monetary Fund
2. “China’s Share Market Intervention – Cause and Effect”
   – An article by the Supervision of Markets Division of the Securities and Futures Commission (SFC) of Hong Kong, published in the SFC Quarterly Bulletin Autumn 2001 edition

If you need any further clarification please feel free to contact us.

Best Regards

Ashraf Bava, CFA
President & Advocacy Chair
CFA Society Pakistan