

Order Execution Policy (HK)

Sep 2020

Order Execution policy

Introduction

This Order Execution Policy sets forth information relating to how BMO Capital Markets¹ institutional sales and trading team of Bank of Montreal Hong Kong Branch (BMOCM HK) seek to provide best execution as required by the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC), when executing orders in relation to financial instruments on behalf of institutional clients (Clients).

Transactions with Clients are booked in Bank of Montreal Hong Kong Branch, London Branch and Toronto Branch. The BMO Capital Markets institutional sales and trading team is based in Hong Kong to provide coverage for Clients. Our Clients include mainly institutional professional investors who are sophisticated and experienced in trading.

BMOCM HK is committed to providing our Clients with best execution of client orders in accordance with the best execution obligations under relevant BMO Capital Markets best execution policies and guidelines, FX Code of Conduct, HKMA and SFC rules. We are required to take all sufficient steps to provide best execution when we execute or transmit orders on behalf of Clients.

The purpose of this document is to provide Clients with information on how we handle order execution.

When we execute orders on behalf of Clients, we are acting to conclude agreements to buy or sell one or more financial instruments.

BMOCM HK must take all sufficient steps to obtain the best possible result for Clients when executing orders (or receiving and transmitting orders) on their behalf, taking into account factors such as price, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order. Execution of trade is on a best effort basis. Prioritization of execution factors and execution outcomes may be affected by other factors, including but not limited to market liquidity, regulatory/compliance limitations, credit/market risk limits, BMO Capital Markets' infrastructure and processes.

Execution of orders on behalf of Clients

The application of best execution will be limited to where BMOCM HK executes orders *"on behalf of clients"*.

This will always apply when we are dealing as the Client's agent or as back-to-back trading principal. This will include where our Client has placed an actionable instruction to buy or sell a financial instrument and where BMOCM HK has an element of discretion over the execution of the order.

By way of illustration, this will apply where BMOCM HK receives an instruction to, amongst other things:

- work an order for a client;
- execute an order at best; or
- execute a limit or stop loss order.

In other situations our duty of best execution will depend on whether the Client is deemed to be placing legitimate reliance upon BMOCM HK to protect its interests in relation to the execution of the order.

Products that BMOCM HK deals as back-to-back trading principal:

Back-to-back equity options

¹ BMO Capital Markets is a trade name used by BMO Financial Group for the wholesale banking business of Bank of Montreal and its subsidiaries and affiliates.

Execution of Orders in principal trading and market making: applicability to Request for Quotes (“RFQs”)

When BMOCM HK provides quotes or negotiates a price to trade on a bilateral basis with a Client on request (i.e. dealing on a RFQ basis), the application of best execution will depend on the nature and circumstances of the request and whether the Client is placing legitimate reliance on BMOCM HK at the time of the RFQ.

Whether or not the Client is placing legitimate reliance on BMOCM HK will be assessed by applying the four-fold cumulative test, which entails the consideration of the following factors:

1. which party initiates the transaction;
2. questions of market practice and the existence of a convention to ‘shop around’;
3. the relative levels of price transparency within a market; and
4. the information provided by BMOCM HK and any agreement reached.

Where the consideration of the above factors leads us to conclude that the Client is not legitimately relying on BMOCM HK, then best execution will not apply.

Products that BMOCM HK deals as trading principal and market maker:

FX forwards and options

Equity options

Interest rates derivatives

Bond & money market instruments

Structured/secured products (fixed income)

Commodity derivatives

In general, BMOCM HK does not owe Clients best execution in relation to the above products where they are generally considered transparent in price (eg. money market instruments and FX products) and/or the Clients which deal in these products are sophisticated institutional investors which shop around, and they do not rely on BMOCM HK for best execution.

Applicability to orders

When executing orders on a principal basis, subject to any specific Client instruction, we will take all sufficient steps to obtain the best possible result for the Client taking into account the prioritisation of factors below:

1. price;
2. size and nature of the order;
3. likelihood of execution;
4. speed of execution;
5. costs;
6. likelihood of settlement; and
7. any other consideration relevant to the execution of the order.

Certain factors are more important than others. When we execute a Client order, by default, we will consider the key factors listed above to be the most important. The relative importance of these factors will change in response to the instructions provided or circumstances prevalent in the general market or specific execution venues during the execution of the order. For example, with illiquid instruments “*size and likelihood of execution*” will likely take priority over price.

Delivering on our commitment to obtain the best possible result

Subject to any specific instructions that may be given by a Client, when executing or transmitting orders on a Client’s behalf or when dealing as back-to-back trading principal, we will take all sufficient steps to obtain the best possible result taking into account the execution factors and criteria considered below.

The execution factors that will be taken into account are:

- price;
- likelihood of execution and settlement (liquidity);
- size and nature of the order;
- speed of execution;
- execution costs; and

- any other consideration relevant to the efficient execution of the order.

We will determine the relative importance of each factor taking into account the following criteria:

- the characteristics and nature of the order such as benchmark, strategy, aggressivity/passivity;
- the characteristics of the Client (e.g. they are institutional investors);
- the characteristics of the financial instruments that are the subject of the order; and
- the characteristics of the execution venues to which that order can be directed.

Ordinarily, price will merit a high relative importance in obtaining the best possible result for Clients with the next most important factor being the liquidity of the underlying market.

The choice of execution venue will be determined in relation to the prioritisation of the execution factors above.

When conducting business in a principal capacity on a RFQ basis, ordinarily price – subject to size – will be the primary factors of consideration. However, during highly volatile markets or in very illiquid instruments it will be more likely that size and likelihood of execution will take priority over price. For instance, equity option of North America underlyings will have very thin market liquidity in Asia time zone. Likelihood of execution and size becomes the prevailing factors. There may also be circumstances in large trades where minimisation of market impact takes priority.

Notwithstanding this, the relative importance of these factors will change in response to the circumstances of the general market or during the execution of the order or instructions provided.

Appendix A describes how best execution is applied in the context of each product, and Appendix B describes the key and other execution factors.

Aggregation and allocation

Our procedures and arrangements:

- provide for the prompt, fair and expeditious execution of Client orders, relative to other Client orders or the trading interests of BMO Capital Markets; and
- allow for the execution of otherwise comparable Client orders in accordance with the time of their reception by BMOCM HK.

We will process Client orders in the sequence in which we receive them unless the nature of the order or prevailing market conditions makes this impracticable or the Client requires otherwise.

We will generally place orders onto the appropriate execution venue as soon as we have agreed to work the order, unless potential market impacts dictate that we do not.

Should we receive multiple orders at, or around, the same time, we may aggregate the orders and allocate the resulting fills as the aggregate order is executed. This may mean that we will provide you with partial fills at different prices or a single fill at an average price. Orders may only be aggregated if it is unlikely that this will work overall to the disadvantage of any Client whose order is to be aggregated.

Should our book position dictate that we wish to execute an order from our book in the same direction as a Client order, we will execute the Client order in full ahead of our own order unless by aggregating the order we can demonstrate that the Client will receive the same or better execution outcome; for the avoidance of doubt, if we are already working an order for our own book when a Client order comes in then our order will take priority.

If we aggregate a Client order with our own order and the aggregated order is partially executed, the resulting fills must be allocated to the Client's in priority to us. However, if we are able to demonstrate on reasonable grounds that without the combination we would not have been able to carry out the Client's order on such advantageous terms or at all, we may allocate the transaction for our own account proportionally.

Where aggregated own account and Client orders have been allocated, care and consideration will be taken that reallocation of trades is not detrimental to the Client.

BMOCM HK shall not carry out a Client order or a transaction for own account in aggregation with another Client order unless the following conditions are met:

1. it is unlikely that the aggregation of orders and transactions will work overall to the disadvantage of any client whose order is to be aggregated;
2. it is disclosed to each client whose order is to be aggregated that the effect of aggregation may work to its disadvantage in relation to a particular order; and
3. an order allocation policy is established and effectively implemented, providing for the fair allocation of aggregated orders and transactions, including how the volume and price of orders determines allocations and the treatment of partial executions.

Where BMOCM HK aggregates an order with one or more other Client orders and the aggregated order is partially executed, it shall allocate the related trades in accordance with its order allocation policy.

Fees, commissions and mark-ups

We will charge commission or mark-ups for the execution services we provide for Clients.

In RFQ driven markets, like fixed income, FX/IR/metal/commodity products and equity options transactions, BMOCM HK, like other market participants, will charge a spread between where BMOCM HK may buy a financial instrument and where we may sell the same instrument (if applicable). In most cases, BMOCM HK may just manage the risk as a principal so charging a spread is not applicable.

BMOCM HK will ensure that mark-ups and spreads charged on transactions where best execution is owed are: (1) reasonable, (2) not excessive and (3) within a range that we consider reasonable for the product type, tenor and size of the trade. This does not mean that commissions and mark-ups will be exactly the same for all Clients.

BMOCM HK will not seek to benefit from a Client through asymmetric price movements, for example, where we may pass on any adverse price movements to the Client while retaining for BMO Capital Markets any movement in the Client's favour.

Please note that pricing offered to Clients may be reflective of an array of factors, including, but not limited to:

- Client's relationship with BMO Capital Markets;
- Client type;
- product being sold;
- size of transaction;
- current market conditions;
- Client's credit worthiness;
- competitive landscape; and
- potential risk to BMO Capital Markets.

Monitoring and review

BMOCM HK will monitor the effectiveness of our execution arrangements and execution policy in order to identify and where appropriate correct any deficiencies. This obligation has been incorporated into our Trading Floor Supervision monitoring and testing process.

BMOCM HK will review this Order Execution Policy at least annually and the latest version is available at <https://www.bmocm.com/about-us/regulatory/>.

Appendix A: Best execution by product

How best execution is applied in the context of each product.

Asset class	Prioritisation of factors ²	Best execution applicable?
FX forwards	<ol style="list-style-type: none"> 1. size and nature of the order;³ 2. price;³ 3. speed of execution; 4. likelihood of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	Normally best execution would not apply, unless BMOCM HK is executing client orders with discretion.
FX options	<ol style="list-style-type: none"> 1. size and nature of the order; 2. price; 3. likelihood of execution; 4. speed of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	Normally best execution would not apply, unless BMOCM HK is executing client orders with discretion, including the execution of delta hedges.
Bonds and money market instruments	<ol style="list-style-type: none"> 1. size and nature of the order;³ 2. price;³ 3. speed of execution; 4. likelihood of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	Normally best execution would not apply, unless BMOCM HK is executing client orders with discretion.
Commodity derivatives	<ol style="list-style-type: none"> 1. size and nature of the order; 2. price; 3. speed of execution; 4. likelihood of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	Normally best execution would not apply, unless executing client orders with discretion or unwinding a BMO Capital Markets issued structure where client legitimately relies on BMOCM HK.

² Price, costs, speed, likelihood of execution and settlement, together with any other consideration relevant to the execution of the order. In determining the relative importance of these factors, we will take into account our clients' status as Professional Investors, together with the nature of the order, the characteristics of the financial instruments to which the order related and the characteristics of the execution venues to which the order can be directed. We will generally give the highest priority to total consideration, representing the price of the instrument and the costs related to execution. However, we may at our discretion prioritise other factors, including the impact on market prices of displaying and executing clients' order, the speed and likelihood of execution and the availability of price improvement. We may prioritise such other factors where there is insufficient immediately available liquidity on the relevant execution venue(s) to execute clients' order over a period of time or by reference to a benchmark calculated over a period of time or where we determine that there are other circumstances such that obtaining the best immediately available price may not be the best possible result for clients.

³ Generally, size of a transaction is considered for relatively large order. For more liquid products such as FX forwards, price would normally be given a higher priority under normal market situation, subject to the size of the order.

Asset class	Prioritisation of factors ²	Best execution applicable?
Interest Rate derivatives	<ol style="list-style-type: none"> 1. size of the order; 2. price; 3. likelihood of execution; 4. speed of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	Normally Best Execution would not apply, unless BMO Capital Markets London are executing client (for clients who are entitled to best execution based on their categorisation) orders with discretion.
Structured / securitized products (fixed income)	<ol style="list-style-type: none"> 1. likelihood of execution 2. size and nature of the order; 3. speed of execution 4. price; 5. costs; 6. likelihood of settlement 7. any other consideration relevant to the execution of the order. 	Best execution would apply in the context of secondary market trading in BMO Capital Markets issued instruments.
Securities borrowing and lending	<ol style="list-style-type: none"> 1. size of the order; 2. price; 3. speed of execution; 4. likelihood of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	BMOCM HK does not undertake agency lending and best execution would not otherwise apply other than if the Client is legitimately relying on BMOCM HK.
Equity options	<ol style="list-style-type: none"> 1. size and nature of the order; 2. price; 3. speed of execution; 4. likelihood of execution; 5. costs; 6. likelihood of settlement; and 7. any other consideration relevant to the execution of the order. 	<p>Normally best execution would not apply, unless BMOCM HK is executing client orders with discretion or where BMOCM HK is executing orders as back-to-back trading principal.</p> <p>Where acting as back-to-back trading principal, BMOCM HK shall solicit quotes from eligible counterparties for execution of equity options. BMOCM HK takes into account "Prioritization of factors" and endeavors to provide the best quote to the Client. Under certain special circumstances, such as counterparty limit or regulatory restrictions, BMOCM HK may not be able to offer quotes from all eligible counterparties. If Client explicitly requires speed/ timeliness as priority of execution and Client duly notifies BMOCM HK, BMOCM HK shall provide the best quotes available within the time limit as requested by the Client.</p>

Appendix B: Execution factors

Key Execution Factors

Price: this refers to the resulting price of the transaction excluding BMOCM HK execution charges. Price will usually be our most important consideration. After price, size of the order, likelihood of execution and speed are usually our most important considerations.

Likelihood of execution and size: we interpret this as the likelihood that we are able to fill your order, in its entirety or a substantial part of it. Size and likelihood of execution are negatively correlated and are related to the concept of liquidity of the instrument. The more liquid an instrument is considered, the easier it will be to execute an order and all other things being equal, size.

Size and likelihood of execution increase in importance in situations where access to liquidity in the relevant instrument is constrained in some way. For example, if the security itself is illiquid or if the order has a limit price which is not marketable.

Speed of execution: BMOCM HK defines this as the rate at which it is able to progress an order. Where order instructions do not refer to speed (or participation rate), we will progress your order at a rate which we believe represents a balance between creating market impact and executing your order in a timely fashion so as to reduce execution risk.

Other Execution Factors

Likelihood of settlement: we expect transactions that we execute for you to settle in a timely fashion. Generally, in equity security markets, likelihood of settlement is not a significant factor when executing on regulated markets, organized trading facilities and multilateral trading facilities due to the involvement of a central counterparty.

However, if we become aware that a particular execution strategy may compromise likelihood of settlement, we may not pursue that strategy even if it would result in a better price. Likelihood of settlement will also become more significant when executing through systematic internalisers or other OTC channels.

Costs: if you have a commercial arrangement with us in which those costs influence our own charges to you, we will agree an appropriate way with you to incorporate costs into our execution strategy. We will not structure or charge commissions in a way as to discriminate unfairly between execution venues.