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Hong Kong Law

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## SHANGHAI-HONG KONG STOCK CONNECT TO COMMENCE MONDAY, 17 NOVEMBER 2014

### Introduction

The Securities and Futures Commission (**SFC**) and the China Securities Regulatory Commission (**CSRC**) announced on 10 November 2014 that Shanghai-Hong Kong Stock Connect, the pilot programme to allow mutual trading access between the Shanghai and Hong Kong stock markets, will start operating on 17 November 2014. For the first time, global investors will be able to trade Shanghai-listed shares through Hong Kong, while Mainland Chinese investors will be able to trade Hong Kong-listed shares directly. Announced in April, the programme had been expected to launch in late October, although a formal commencement date was never announced. Rumours circulated that operations would commence on 7 November, but turned out to be unfounded. Giving only seven days' notice, the Stock Exchange of Hong Kong Limited (the **Exchange**), announced the 17 November launch date on 10 November, following the SFC/CSRC joint announcement of approval of the launch date. Trading through Shanghai-Hong Kong Stock Connect will begin on 17 November 2014.

The programme allowing a net 23.5 billion yuan of daily cross-border share purchases is seen as a major step towards China opening up its capital account and increasing use of the yuan. Access to the Chinese markets is currently restricted to a limited number of qualified institutional investors under the Qualified Foreign Institutional Investor (**QFII**) scheme established in 2002 and the Renminbi Qualified Foreign Institutional Investor (**RQFII**) scheme established in 2011. The

Shanghai-Hong Kong Stock Connect will broaden access to the Shanghai market to anyone with a Hong Kong brokerage account. It will also allow Chinese professional investors (i.e. Chinese institutional investors and individual investors with RMB 500,000 in cash and securities) direct access to Hong Kong-listed companies. Currently, Chinese investors are only able to invest in foreign securities markets through certain fund management institutions, securities companies and asset management institutions under the Qualified Domestic Institutional Investor (**QDII**) scheme.

The development of Shanghai-Hong Kong Stock Connect was jointly announced by the SFC and CSRC on 10 April 2014. Since then, the two regulators have agreed on the principles and arrangements for cross-boundary cooperation. On 17 October 2014, a Memorandum of Understanding between the CSRC and SFC on Strengthening Regulatory and Enforcement Cooperation under Shanghai-Hong Kong Stock Connect was signed. The SFC and CSRC stated their joint commitment to take action against cross-boundary illegal activities and market misconduct, to maintain an orderly market, handle investor complaints and protect investors trading through the Shanghai-Hong Kong Stock Connect.

### Stocks Eligible for Trading

The so-called Northbound trading link allows trading in Shanghai-listed companies on the SSE 180 Index and SSE 380, while the Southbound link permits trading in the constituent stocks of the Hong Kong Exchange's Hang Seng

Composite LargeCap Index and Hang Seng Composite MixCap Index. Trading in companies with dual listings on the Shanghai and Hong Kong Stock Exchanges is also allowed through the link. Only secondary market trading is allowed under the programme so investors will not be able to subscribe in IPOs on either market.

The website of the Hong Kong Stock Exchange has the following lists of eligible stocks under the programme<sup>1</sup>:

#### Northbound Trading

- Shanghai-listed stocks that are eligible for selling and buying;
- the Shanghai-listed special stocks that are eligible for selling only (no stocks are currently specified and will be included on the programme's launch date); and
- Shanghai-listed stocks that are eligible for margin trading;

#### Southbound Trading

- Hong Kong-listed stocks that are eligible for selling and buying; and
- the Hong Kong-listed special stocks that are eligible for selling only.

### Trading Calendar

The northbound trading calendar for trading of Shanghai-listed stocks is available on the Hong Kong Stock Exchange Website<sup>2</sup>.

### Trading Quotas and Currency

Trading through Shanghai-Hong Kong Stock Connect will be subject to initial aggregate and daily quotas, which are expected to be increased over time. The initial quotas are:

- For northbound trade:
  - a daily quota of RMB 13 billion; and
  - an aggregate quota of RMB 300 billion;

1 [http://www.hkex.com.hk/eng/market/sec\\_tradinfra/chinaconnect/Documents/SSE\\_Securities.xls](http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/Documents/SSE_Securities.xls)

2 [http://www.hkex.com.hk/eng/market/sec\\_tradinfra/chinaconnect/Documents/2014\\_calendar.pdf](http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/Documents/2014_calendar.pdf)

- For southbound trade:
  - a daily quota of RMB 10.5 billion; and
  - an aggregate quota of RMB 250 billion.

Both quotas apply on a "net buy" basis so that investors can always sell stocks cross-border.

All trades under the programme will be settled in yuan. Chinese investors will use yuan to invest in Hong Kong stocks and the exchange to Hong Kong dollars will take place in Hong Kong through ChinaClear. Hong Kong and overseas investors must use yuan to purchase Shanghai-listed stocks.

Trading in Shanghai-listed stocks is subject to a general price limit of  $\pm 10\%$  (and  $\pm 5\%$  for stocks in the risk alert board) based on the previous closing price. For the trade of Hong Kong listed stocks, trading will follow the existing quotation rules.

The SFC and the CSRC advise participants of the Shanghai-Hong Kong Stock Connect to familiarise themselves with the differences between the laws, regulations, rules and market practices in Hong Kong and Mainland China. Hong Kong's Investor Education Centre and Mainland China's Investor Protection Bureau have agreed to cooperate on investor education in relation to Shanghai-Hong Kong Stock Connect. The Investor Education Centre now has a dedicated page of information for the pilot programme<sup>3</sup>.

### Exchange Circular on the Launch of the Shanghai-Hong Kong Stock Connect

The Exchange's circular of 10 November<sup>4</sup> announced that, in preparation for the launch of Shanghai-Hong Kong Stock Connect, a Pre-launch System Readiness Test will be conducted from 9:00 a.m. to 12:00 p.m. on 15 November 2014 (Saturday). Participants are reminded that northbound buy orders at a price that is 3% lower than the best bid price during the opening call auction and continuous auction sessions will be blocked. The Exchange has created a dedicated page to provide information on Shanghai-Hong Kong Stock Connect<sup>5</sup>.

3 <http://www.hkiec.hk/web/en/investment/understanding-products/stock/stockconnect/index.html>

4 Stock Exchange of Hong Kong Limited Circular "Launch of Shanghai-Hong Kong Stock Connect on 17 November 2014" available at: <http://www.hkex.com.hk/eng/market/partcir/sehk/2014/Documents/CT05914E.pdf>

5 <http://www.hkex.com.hk/eng/csm/chinaConnect.asp?LangCode=en>

## Information Book and FAQs

An Information Book on the operations of Shanghai-Hong Kong Stock Connect is available on the Hong Kong Exchange's website<sup>6</sup>. Also available are FAQs on Shanghai-Hong Kong Stock Connect<sup>7</sup> which set out details relating to trading, clearing and settlement, fees and other transaction costs. Particular points to note include:

- Day trading

Day trading is not allowed on the Shanghai Stock Exchange since A shares purchased by investors cannot be sold before settlement. The Hong Kong Stock Exchange will perform pre-trade checking at the Exchange Participant (**EP**) level on all northbound orders to ensure that EPs do not conduct day trading. EPs must also ensure that their clients do not conduct day trading in Shanghai-listed stocks.

- Pre-trade checking

Chinese investors are only allowed to sell Shanghai-listed stocks which are available in their ChinaClear accounts at the end of the previous day (**T-1**). This shareholding information is forwarded to the Shanghai Stock Exchange at the end of each day and based on the T-1 shareholdings, the Exchange will reject a sell order if the investor does not have sufficient shares in his account. The Shanghai Exchange will carry out the same pre-trade shareholding checking for the Hong Kong Stock Exchange subsidiary's sell orders. Shanghai-listed securities acquired by Hong Kong and overseas investors under the programme will be held in HKSCC's omnibus stock account maintained with ChinaClear. On each trading day, the Shanghai Exchange will validate the Hong Kong Stock Exchange subsidiary's sell orders in respect of Shanghai-listed stocks against HKSCC's account balance as of T-1 day-end.

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6 Information Book for Market Participants<sup>8</sup> available at:  
[http://www.hkex.com.hk/eng/market/sec\\_tradinfra/chinaconnect/Documents/EP\\_CP\\_Book\\_En.pdf](http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/Documents/EP_CP_Book_En.pdf)

7 [http://www.hkex.com.hk/eng/market/sec\\_tradinfra/chinaconnect/Documents/EP\\_CP\\_FAQ\\_En.pdf](http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/Documents/EP_CP_FAQ_En.pdf)

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