

China-Hong Kong Connect - Part 6: Approval of Shenzhen-Hong Kong Train

In November 2014, the Shanghai-Hong Kong Stock Connect (the “**Shanghai-Hong Kong Train**”), a pilot program for establishing mutual stock market access between Mainland China¹ and Hong Kong, was officially launched. The new cross-border investment channel established mutual stock market access between Hong Kong and Mainland China, allowing Hong Kong and international investors to invest directly in designated securities listed on the Shanghai Stock Exchange (the “**SSE**”), and investors from Mainland China to invest directly in designated securities listed on the Hong Kong Exchanges and Clearing Limited (the “**HKEx**”).²

Related Capabilities

- Capital Markets
- Hong Kong
- China

Following the launch of the Shanghai-Hong Kong Train, a second connect, the Shenzhen-Hong Kong Stock Connect (the “**Shenzhen-Hong Kong Train**”) was introduced. Collectively, both trains are referred to as the “**China-Hong Kong Connect**”. Although initially expected to commence operations in summer 2015, stock market turbulence during the period resulted in the Shenzhen-Hong Kong Train being delayed, due to the Mainland’s stock market turbulence and the Hong Kong government refusing to compromise on investor protection and financial market stability.³

On August 16, 2016, the HKEx announced that the China Securities Regulatory Commission and the Securities and Futures Commission had now approved in principle the establishment of the highly anticipated mutual stock market access between Shenzhen and Hong Kong. The HKEx expects that it will take roughly four months to complete the technical and operational preparations for the new link, meaning it should be operating by December 2016.⁴

[Part 1](#) and [Part 2](#) of this e-Update series discuss key features of the Shanghai-Hong Kong Train and the Shenzhen-Hong Kong Train, respectively. [Part 3](#) explains the unique nature and foreseeable advantages regarding the proposed commodities connect. [Part 4](#) highlights the concerns and reasons behind the delay in launching the Shenzhen-Hong

Kong Train. Part 5 focuses on Hong Kong's challenges and opportunities in further fostering connections with Mainland China. Part 6 will examine the details of the Shenzhen-Hong Kong Train and the benefits that it should bring.

The announcement

In their announcement confirming the approval of the Shenzhen-Hong Kong Train launch, the HKEx highlighted that there is no reason it will not be implemented, since it follows the existing legal, regulatory and operational framework of the Shanghai-Hong Kong Train.⁵ The HKEx also announced in their statement that the existing total quota of a combined 550 billion yuan for the Shanghai-Hong Kong Train will be abolished as of the date of announcement, August 16, 2016, which will help further open up Mainland China's market to international investors.⁶

The benefits

The new Shenzhen-Hong Kong Train will be welcome news to investors who will benefit from greater investment choices. It will further strengthen the interconnectivity between the Mainland China and Hong Kong capital markets, promote the internationalisation of the Renminbi, and bolster Hong Kong as an international finance centre.

Chief Executive of the HKEx Mr Charles Li claims it will create another reliable and secure investment channel for investors in the Hong Kong and Mainland China in an environment that they are familiar with.⁷ The Shenzhen market, the world's seventh-largest at US \$3.2 trillion, could attract foreign investors since it is where fast-growing Mainland Chinese companies in sectors such as technology and pharmaceuticals list.⁸

According to Mr Li, the link will increase chances for A shares to be added to the MSCI index when the index compiler conducts its next review.⁹ A commentator added: "It improves the odds for the MSCI to reconsider the A shares inclusion in the longer term. Shenzhen's stock market accounts for nearly half of A shares' market cap".¹⁰ If the MSCI is finally persuaded to add Mainland China to its key emerging-market indexes, billions of dollars could be poured through Hong Kong into Mainland Chinese shares.¹¹

The details so far

Mr Li announced there will be no aggregate quota under the Shenzhen-Hong Kong Train, which was confirmed by China Securities Regulatory Commission.¹² The daily quota will be the same as that currently under the Shanghai-Hong Kong Train, amounting to a daily quota of RMB13 billion for the Northbound Shenzhen Trading Link and RMB10.5 billion for the Southbound Hong Kong Trading Link.¹³ There will be 417 Hong Kong stocks traded in Shenzhen, which exceeds the 318 Hong Kong stocks currently traded on the Shanghai-Hong Kong Train.¹⁴

The joint announcement also disclosed that, after the launch of the Shenzhen-Hong Kong Train, mutual stock market access between the Mainland and Hong Kong will

comprise:

- under the Shanghai-Hong Kong Train, the Northbound Shanghai Trading Link and the Southbound Hong Kong Trading Link; and
- under the Shenzhen-Hong Kong Train, the Northbound Shenzhen Trading Link and the Southbound Hong Kong Trading Link.¹⁵

For the Northbound Shenzhen Trading Link, eligible shares refer to:

- any constituent stock of the Shenzhen Stock Exchange (“**SZSE**”) Component Index and SZSE Small/Mid Cap Innovation Index which as a market capitalization of RMB 6 billion or above; and
- all SZSE-listed shares of companies which have issued both A shares and H shares.¹⁶

For the Southbound Hong Kong Trading Link, the scope of eligible shares will be:

- the constituent stocks of the Hang Seng Composite LargeCap Index, and Hang Seng Composite MidCap Index;
- any constituent stock of the Hang Seng Composite SmallCap Index which has a market capitalization of HK\$5 billion or above; and
- all HKEx-listed shares of companies which have issued both A shares and H shares.¹⁷

Moreover, exchange trade funds will now be included as eligible securities under the scheme to increase the variety of traded products and provide more investment opportunities for investors. A launch date will be announced separately after Shenzhen-Hong Kong Train has been in operation for a period of time and upon the satisfaction of relevant conditions.¹⁸

¹ “Mainland China” or the “Mainland” in this article refers to the geopolitical area under the jurisdiction of the People’s Republic of China, excluding Hong Kong, Macau and Taiwan.

² “HKEx celebrates the launch of Shanghai-Hong Kong Stock Connect”, HKEx New Release, Hong Kong Stock Exchange, November 17, 2014.

³ “Hong Kong-Shenzhen stock connect may be delayed by market turmoil” by Enoch Yiu, South China Morning Post, September 7, 2015.

⁴ “Shenzhen-Hong Kong Stock Connect and Shanghai-Hong Kong Stock Connect”, HKEx Announcement, Hong Kong Stock Exchange, August, 16, 2016.

⁵ See footnote 4.

⁶ “Joint Announcement of the China Securities Regulatory Commission and the Securities and Futures Commission”, Securities and Futures Commission, August, 16,

2016.

⁷ “HKEx Set for Another Step Forward in Mutual Market Access”, HKEx News Release, Hong Kong Stock Exchange, August, 16, 2016.

⁸ “China Approves Shenzhen-Hong Kong Stock Link”, Wall Street Journal, August, 16, 2016.

⁹ “Shenzhen-Hong Kong Stock Connect may help push A shares closer to MSCI”, South China Morning Post, August, 17, 2016.

¹⁰ See footnote 9.

¹¹ See footnote 8.

¹² See footnote 6.

¹³ See footnote 6.

¹⁴ “Shenzhen-Hong Kong stock trading link operational by Christmas, says HKEx chief”, South China Morning Post, August, 16, 2016.

¹⁵ See footnote 6.

¹⁶ See footnote 6.

¹⁷ See footnote 6.

¹⁸ See footnote 6.