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SHANGHAI - HONG KONG CROSS-BORDER SHARE TRADING PLAN

Background

On 10 April, 2014 the China Securities Regulatory Commission ("CSRC") and the Hong Kong Securities and Futures Commission ("SFC") announced that they have approved, in principle, the development of a pilot programme ("Shanghai-Hong Kong Stock Connect") for establishing mutual stock market access between Mainland China and Hong Kong.

Shanghai-Hong Kong Stock Connect will operate between the Shanghai Stock Exchange ("SSE"), the Stock Exchange of Hong Kong Limited ("SEHK"), China Securities Depository and Clearing Corporation Limited ("ChinaClear") and Hong Kong Securities Clearing Company Limited ("HKSCC").

Currently, the only option for mainland investors who wish to invest in stocks listed on non-Mainland stock exchanges is to utilise the Qualified Domestic Institutional Investor ("QDII") program. Foreign investors' access to mainland listed stocks is similarly controlled through various quota programs. Such investors may invest in B-shares (shares of companies based in China that are traded on the Shanghai Stock Exchange in U.S. dollars or on the Shenzhen Stock exchange in Hong Kong dollars) and in A-shares (shares that are traded on the two Mainland stock exchanges in Renminbi) through the Qualified Foreign Institutional Investor ("QFII") program and the Renminbi Qualified Foreign Institutional Investor ("RQFII") program. For further information on both of those programs please see the Dillon Eustace publication Irish Funds and QFII RQFII

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The CSRC and the SFC are also working on the creation of a mutual recognition platform for locally domiciled funds in Hong Kong and Mainland China, which, if adopted, will enable funds established in either market to be distributed in the other market where they satisfy the criteria established by both regulators.

▣ Five Principal Elements of the Shanghai-Hong Kong Stock Connect

Quotas

Trading under Shanghai-Hong Kong Stock Connect will initially be subject to a maximum cross-boundary investment quota, together with a daily quota that will be monitored on a real time basis. A Northbound Trading Link will be established which will permit Hong Kong investors to place orders to trade eligible shares quoted on the SSE subject to an aggregate quota of RMB300 billion and a daily quota of RMB13 billion. A Southbound Trading Link will also be established which will permit Mainland investors to place orders to trade eligible shares listed on the SEHK subject to an aggregate quota of RMB250 billion and a daily quota of RMB10.5 billion.

While the quotas under the Shanghai-Hong Kong Stock Connect Project are not as large as the quota granted under the QDII, QFII and RQFII programs, the announcement does provide that the initial quotas may be adjusted in the future.

Eligible investors

Initially, the SFC will require Mainland investors participating in the Southbound Trading Link to be limited to institutional investors, and those individual investors who hold an aggregate balance of not less than RMB 500,000 in their securities and cash accounts. There is no mention of requirements being imposed by CSRC on investors in Hong Kong.

Eligible shares

Under the pilot programme, all the constituents of the SSE 180 Index and SSE 380 Index, and shares of all SSE-listed companies which have issued both A shares and H shares will be eligible to be traded through the Northbound Trading Link. All the constituents of the Hang Seng Composite LargeCap Index and Hang Seng Composite MidCap Index, and shares of all companies listed on both SSE and SEHK Shares are eligible to be traded through the Southbound Trading Link. The announcement specifically provides that the scope of Shanghai-Hong Kong Stock Connect is subject to further adjustment following its launch.

Applicable Trading, Clearing and Listing Rules

Trading and clearing arrangements will be subject to the regulations and operational rules of the market where trading and clearing take place. Listed companies will continue to be subject only to the listing and other rules and regulations of the markets where they are listed.

Clearing

Clearing will occur through a direct link to be established through ChinaClear and HKSCC.

Conclusion

The Shanghai-Hong Kong Stock Connect project is another important development in the opening up of China's capital markets and shows the continuing determination of the Chinese authorities to attract foreign investors into the Chinese capital markets and indeed to allow Chinese investors access to international capital markets. It is a part of a series of developments consisting of improvements to existing schemes (QFII and RQFII) and development of new schemes (mutual recognition) which will be watched closely by investors seeking to access the Mainland capital markets.

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