

MEMO# 34169

June 1, 2022

Regulators Announce Inclusion of ETFs in Mainland-HK Stock Connect

[34169]

June 1, 2022

TO: ICI Global Members

Global Regulated Funds Committee

Global Regulated Funds Committee - Asia SUBJECTS: Distribution

International/Global RE: Regulators Announce Inclusion of ETFs in Mainland-HK Stock Connect

On 27 May 2022, the China Securities Regulatory Commission (CSRC) and the Hong Kong Securities and Futures Commission (SFC) (the "Regulators") announced the inclusion of exchange-traded funds (ETFs) into the Mainland-Hong Kong Stock Connect ("Stock Connect").[\[1\]](#) The preparation of formal implementation will take around two months, and the official launch date is expected to be announced by the Regulators in due course.

As background, the Regulators reached a consensus to include ETFs as eligible securities under the Stock Connect in 2016. In December 2021, the Shanghai Stock Exchange (SSE), Shenzhen Stock Exchange (SZSE), the Hong Kong Exchanges and Clearing Limited (HKEX), and the China Securities Depository and Clearing Corporation reached an agreement on an overall proposal to bring ETFs onto the Stock Connect.[\[2\]](#)

Once the ETFs are officially included in the Stock Connect, eligible mainland investors may trade eligible HK-listed ETFs ("Southbound ETFs"), and eligible Hong Kong investors may trade eligible SSE-listed or SZSE-listed ETFs ("Northbound ETFs"). The HKEX, SSE, and SZSE have proposed the eligibility criteria for the inclusion of ETFs in the Stock Connect.[\[3\]](#) These eligibility criteria are not yet final and subject to regulatory approval.

This memorandum briefly summarizes key proposed eligibility criteria for Northbound and Southbound ETFs.

Investment Arrangement for ETFs under the Stock Connect

Trading under the Stock Connect is subject to a daily quota.[\[4\]](#) The investment quota for ETFs and stocks will be aggregated for calculation and administrative purposes.

Under the Stock Connect, investors may trade ETFs only on secondary markets. No subscriptions or redemptions of ETFs are allowed.

Proposed Eligibility Criteria for ETFs

The proposed eligibility criteria for Northbound and Southbound ETFs are similar. The exchanges in Hong Kong, Shanghai, and Shenzhen may adjust the scope of eligible ETFs under the Stock Connect framework in light of operational performance.

Below are the major requirements proposed by the exchanges:[\[5\]](#)

- Fund size - A Northbound ETF should have a daily average asset under management (AUM) in the last six months of no less than RMB 1.5 billion, whereas the daily average AUM of a Southbound ETF in the last six months should not be less than HKD 1.7 billion.
- Listing history - Both Northbound ETFs and Southbound ETFs should be listed for no less than six months.
- Underlying index - the underlying index for both Northbound ETFs and Southbound ETFs should be established for at least one year.
- Types of ETFs (for Southbound ETFs only) - Southbound ETFs should not be synthetic ETFs or leveraged and inverse products.
- Weighting of stocks listed in Hong Kong/mainland China in the underlying index - the total weighting of SSE-listed and SZSE-listed stocks in the underlying index of Northbound ETFs should not be less than 90%, whereas for Southbound ETFs, the total weighting of HK-listed stocks in the underlying index should not be less than 90%.
- Weighting of eligible stocks under Stock Connect in the underlying index - for Northbound ETFs, the total weighting of eligible stocks under Northbound Connect should not be less than 80%. On the other hand, for Southbound ETFs, if the underlying index is the Hang Seng Index or other selected indices,[\[6\]](#) the total weighting of eligible stocks under Southbound Stock Connect should not be less than 70%. If the Southbound ETFs track other indices, the total weighting of eligible Southbound stocks should not be less than 80%.
- Sell-only ETFs. Upon regular review,[\[7\]](#) investors will only be allowed to sell and will be restricted from buying the Northbound ETFs and Southbound ETFs, if, among others, the fund size of ETFs falls under certain thresholds or the total weighting of eligible stocks under Stock Connect in the underlying index decrease to below certain thresholds.[\[8\]](#)

ICI Global will continue to monitor and keep members informed of relevant developments.

Lisa Cheng
Research Analyst
ICI Global

endnotes

[\[1\]](#) The Stock Connect is a cross-boundary stock trading arrangement between China and Hong Kong. It consists of (i) Shanghai-Hong Kong Stock Connect ("Shanghai Connect"), which was launched in 2014, and (ii) Shenzhen-Hong Kong Stock Connect ("Shenzhen Connect"), which was launched in December 2016. Under the Stock Connect, eligible Hong

Kong and overseas investors could trade eligible stocks listed on the Shanghai Stock Exchange or Shenzhen Stock Exchange through brokers and securities firms in Hong Kong (Northbound trading), whereas eligible mainland investors could trade eligible Hong Kong-listed stocks through brokers and securities firms in mainland China (Southbound trading). See HKEX - Connect Scheme: Stock Connect at https://www.hkex.com.hk/Mutual-Market/Stock-Connect?sc_lang=en for further details.

[2] See HKEX Reaches Agreement with Mainland Partners on Adding ETFs to Stock Connect, 24 December 2021, available at https://www.hkex.com.hk/News/News-Release/2021/211224news?sc_lang=en.

[3] The HKEx, SZE, and SZSE have separately released the proposed set of eligibility criteria for the inclusion of ETFs in Stock Connect. The SZE and the SZSE welcome public comments until 10 June 2022. See HKEx Circular on Further Update on the Inclusion of ETFs in Stock Connect, available at <https://www.hkex.com.hk/-/media/HKEX-Market/Services/Circulars-and-Notices/Participant-and-Members-Circulars/SEHK/2022/CT05922E.pdf> ("HKEX Circular"). Also see Implementing Measures of the Shanghai Stock Exchange for Shanghai-Hong Kong Stock Connect (2022 First Revision) (Draft for Comments), available (in Chinese only) at http://www.sse.com.cn/lawandrules/publicadvice/c/c_20220527_5702702.shtml ("Revised Draft Shanghai Connect Measures"). And see Implementing Measures of the Shenzhen Stock Exchange for Shenzhen-Hong Kong Stock Connect (2022 Revision Draft for Comments), available (in Chinese only) at <http://docs.static.szse.cn/www/disclosure/notice/W020220527727207464701.pdf> ("Revised Draft Shenzhen Connect Measures").

[4] Under both Shanghai Connect and Shenzhen Connect, Northbound trading and Southbound trading are respectively subject to a separate set of daily quotas, which will be monitored by HKEX and SSE/SZSE respectively. The daily quota limits the maximum net buy value of cross-boundary trades under Shanghai Connect and Shenzhen Connect each day.

The Northbound daily quota is set at RMB 52 billion for each of Shanghai Connect and Shenzhen Connect, and the Southbound daily quota is set at RMB 42 billion for each of Shanghai Connect and Shenzhen Connect.

[5] See HKEX Circular, *supra* note 3, at Appendix for a full list of proposed eligibility criteria for Northbound ETFs and Southbound ETFs.

[6] Other selected indices include Hang Seng China Enterprises Index (HSCEI), Hang Seng TECH Index (HSTECH) and Hang Seng Hong Kong-Listed Biotech Index (HSKBBIO).

[7] Regular review refers to the half-yearly reviews of constituents of the Hang Seng Index (for Southbound trading), or the half-yearly reviews of the Shanghai Stock Exchange 180 A-Share Index / Shenzhen Component Index. See Revised Draft Shanghai Connect Measures, *supra* note 3, at Chapter 6, Article 126(23). Also See Revised Draft Shenzhen Connect Measures, *supra* note 3, at Chapter 6, Article 126(19).

[8] See HKEX Circular, *supra* note 3, at Appendix for the conditions for sell-only Northbound ETFs and Southbound ETFs.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.