

Up for the Test

-Counting down to the inclusion decision

Mark your calendar for Jun 14, 2015

MSCI will announce on June 14, 2016 (June 15, Beijing time) the results of its 2016 Annual Market Classification Review, which is just a fortnight away.

The Remaining Stock Suspension Concerns Been Addressed

Background

Early July 2015 the A-share market witnessed unusual stock market volatility, with market fell 3 weeks in a row amid draining of liquidity from the vicious cycle of deleveraging, many listed companies were out of options but to seek refuge in voluntary trading suspension. By the market close on July 7, 2015, a total of 787 stocks on the SSE and SZSE were under trading suspensions, during the evening of the same day, an additional of 200+ SH and SZ listed companies filed for voluntary trading suspension, brought the total to 1000+ , or 40% of all A-share listed names.

This unprecedented market frenzy has shocked investors, domestic and overseas alike and has brought huge challenges to passive managers whose goals are to track the underlying index, be it CSI300 or MSCI China A with minimal tracking error. After the market access and quota allocation issues have been resolved by CSRC, the focal point of MSCI inclusion stake holders have been centered on the suspension issue.

SSE and SZSE issued Stock Suspension Guidelines

On May 27 (Friday), the Shanghai Stock Exchange (SSE) and the Shenzhen Stock exchange (SZSE) have issued renewed guidelines of Trading for Listed Companies Planning for Material Events. The new guideline features the following updates and clarifications from earlier versions.

1. The coverage of suspension regulation has been expanded

Listed companies have many types of business that involve stock suspension and resumption of trading, other than major asset reorganization and non-public offerings. Those types of business include planning of change of controlling rights, purchase or sale of assets, as well as signing major contracts. The handling of stock suspension and resumption of trading for these events has certain standards in practice to abide by. However, those standards have not been publicized in the form of rules, and are thus inconvenient for listed companies to implement. The Guidelines have included these contents and clarified corresponding standards for stock suspension.

2. Suspension duration has been strictly controlled

The Guidelines have clearly stipulated the durations for various categories of suspensions.

SSE Guidelines	
Corporate actions	Max duration for suspension
Planning of consecutive plans of reorganization after suspension	5 months
Planning of major asset reorganization	3 months
Planning of non-public offering	1 month
Planning of change of controlling rights, of purchase or sale of assets, of overseas investments that necessitates the decision by the general meeting of shareholders, and of signing major contracts	10 Trading days

SZSE Guidelines	
Corporate actions	Max duration for suspension
If the duration of suspension is expected to exceed three months, a shareholders' general meeting shall be convened to review the proposal for suspension	>3months
Planning of major asset reorganization	3 months

Planning of fund raising for major asset purchase through non-public equity offer	1 month
Planning of purchases or sales of assets, external investment, transfer of controlling right by related parties, and non-public equity offering not intended to fund major asset purchases	10 Trading days

Besides, the Guidelines have specified the conditions and requirements for extension of suspension. In addition, the Guidelines have clarified that for suspension applications based on planning for material events or on non-public offering that, later on, turn into major asset reorganization, the suspension duration will be aggregated, dating from the start of suspension. Companies that change the target for reorganization during suspension should also resume trading within the specified time frame. After 3 months since the day to start suspension for major asset reorganization, they cannot change the target for reorganization to extend suspension.

3. Requirements for information disclosure during suspension and procedures for suspension extension have been specified

In the case of planning for major asset reorganization, which results to a relatively long suspension, the Guidelines have further clarified the specific contents to be disclosed along the timeline, with a monthly interval. Listed companies have to disclose in time the transaction progress at major points in time during major asset reorganization, so as to facilitate the understanding of investors about the reorganization progress and to set pressure on the listed companies and relevant parties to accelerate the reorganization. At the same time, the Guidelines have considered the internal decision-making procedures of listed companies, including board meetings and general meetings of shareholders, as mandatory if the companies intend to extend the suspension. Those considerations are based on the characteristics and planning progression of major asset reorganization, non-public offering, planning of change of controlling rights, and purchase or sale of assets. Additionally, the Guidelines have provided that interested parties including board members and shareholders should avoid voting in order to fully ensure the rights of small and medium-sized investors in the decision-making of stock suspension and resumption of trading.

More Ready Than Ever

The recent Market Classification Review marks the fourth attempt by China, the world's 2nd largest equity market to be included in the MSCI index families. All stake holders, including various regulatory bodies have been pushing forward by the rolling out of more and more capital market liberalizing measures targeting each concern raised by MSCI on behalf of the global investor base.

As of now, we are delighted to see huge progress has been made and the A-shares market has been more ready than ever to embrace the inclusion decision.

Issues from 2015 Review			
	Concerns	Current Status	Comment
Quota Allocation Process (QFII/RQFII)	•Ability to access quota commensurate with the size of assets under management	✓Base quota is now linked to AUM ranging from US\$20mn to US\$5bn. ✓Quota exceeding US\$5bn subject to SAFE approval	100% resolved
	•Ability to secure additional quota with certainty should the need arise	✓No requirement for quota top-up unless it exceeds US\$5bn ✓Quota exceeding US\$5bn subject to SAFE approval	100% resolved
	•A more streamlined, transparent and predictable quota allocation process	✓Base quota automatically obtained based on AUM through filing with SAFE	100% resolved
Capital Mobility Restrictions (QFII/RQFII/Stock Connect)	•Extension of daily liquidity for all investment vehicles, including open-ended funds, ETFs and separate accounts	✓Remittance period for QFII is removed ✓Repatriation for QFII shortened to daily ✓Separated Accounts no longer treated as closed-end fund and enjoy daily repatriation	100% resolved
	•Removal of capital lock-up and repatriation restrictions on QFII/RQFII	✓Lock up period shortened from 1 year to 3 months ❖Monthly repatriation of 20% of NAV remain unchanged	Almost resolved

	• Elimination of potential trading uncertainty due to daily limit on the Stock Connect	❖ Pending clarification	Almost resolved
Additional concerns raised in April 2016			
Beneficiary Ownership	• Current QFII/RQFII framework does not provide a clear recognition on the ultimate beneficial ownership of assets under separate accounts.	✓ Client names can be now included in QFII/RQFII separated accounts ✓ CSRC has reiterated QFII beneficiary ownership in its press conference	Almost resolved
Widespread voluntary suspension	• Widespread voluntary suspension practices prevented normal market trading activities and caused liquidity and replication concern.	✓ SSE plans to limit suspensions to no longer than three months ✓ On May 27, SSE and SZSE released further regulatory measures on limiting voluntary suspension practices	100% resolved
Anti-competitive clauses	• Existence of a provision that all financial products (including Exchange Traded Funds) linked to an index containing China A Shares need to be pre-approved by the local Chinese stock exchanges even if listed internationally is unique among emerging markets.	❖ Pending resolution by the local Chinese stock exchanges	Not material and is likely to be resolved in the inclusion window

Source: MSCI, ChinaAMC

SZ-HK Connect May Just Be Around The Corner

SZ-Connect is the logical next-step of the SH-Connect program that was launched in Nov 2014. We believe given the momentum of how things are moving in the policy front, it is reasonable to foresee announcements in 1H to reinforce the case for A-share's inclusion in MSCI Index, leaving actual launching to 2H (a wide window).

Be ready to embrace changes brought by the inclusion

Initial 5% inclusion will bring approximately 21.4 Billion USD inflow to A-shares (Exhibit1). Comparing to A-share's 6 Trillion USD market capitalization, the magnitude of the inflow might not be significant, by it carries more far more symbolic meanings.

Exhibit1	A share weight (%)	Estimated inflow (USD Billion)
5% Inclusion		
MSCI ACWI	0.1	3.1
MSCI EM	1.1	15.8
MSCI Asia	1.2	2.5
Total		21.4
100% Inclusion		
MSCI ACWI	2.2	60.90
MSCI EM	17.5	263.1
MSCI Asia	20	39.9
Total		363.9

Source: MSCI, CICC

Turnover Down, Correlation Up

What to expect after the inclusion? The answer may lie within the precedents set by Korea and Taiwan. The following benefits have been observed in these two markets since their inclusion in to MSCI index family.

- Significant inflow in foreign fund inflow
- More balanced investor structure
- Improving investment styles(Exhibit2)
- Increased correlation with global markets(Exhibit3)

Exhibit2: Turnover coming down since the inclusion, Korea (LHS) and Taiwan (RHS)

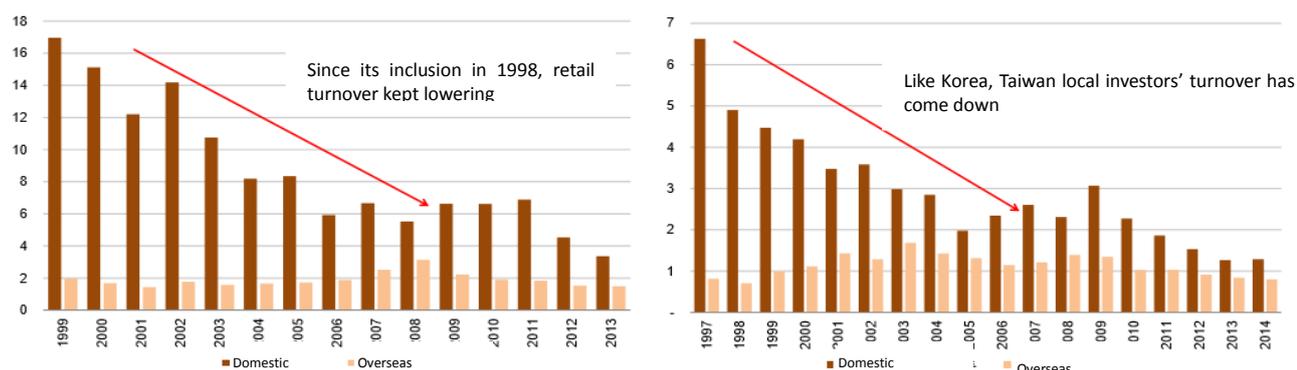
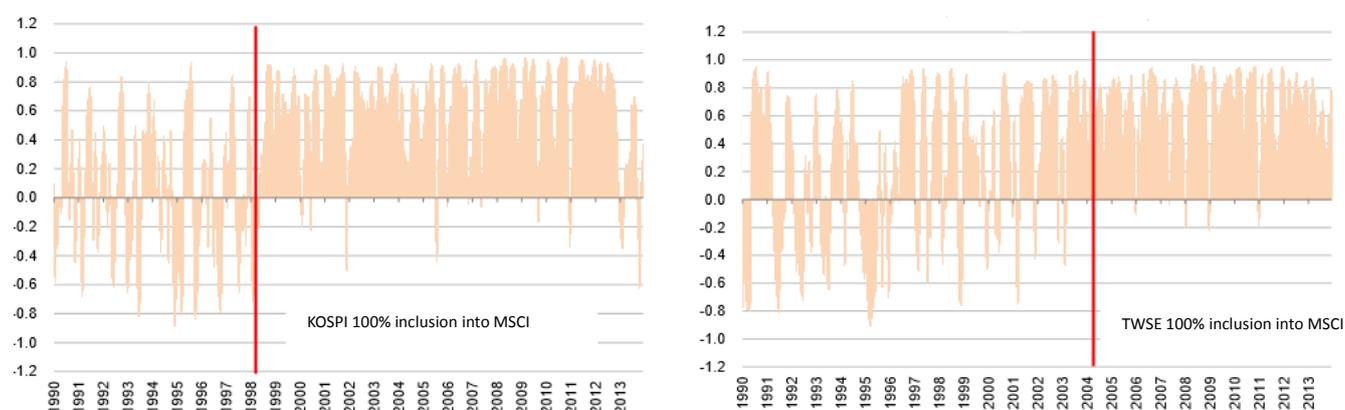


Exhibit3: correlation with US equity market up since inclusion Korea (LHS) and Taiwan (RHS)



Source: CEIC, CICC

ChinaAMC's Answer to the MSCI Inclusion Opportunity

- **ChinaAMC MSCI China A ETF (the first and only in China) and other A-share indexed products.**

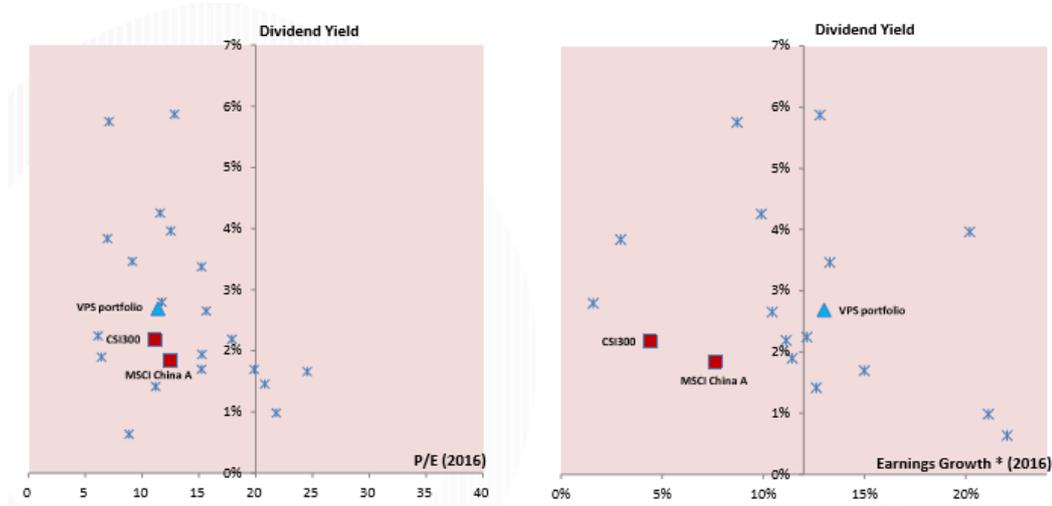
Exhibit4: ChinaAMC A-share Indexed Equity Product Offerings

Ticker	Fund Name	Inception Date	NAV RMB (Bn)	2015		2014		2013		2012		2011		2010		Morningstar 1Yr Rating	Morningstar 3Yr Rating	Morningstar 5Yr Rating
				Excess Return	TE													
510330	CSI 300 ETF	25-Dec-12	17.95	1.80%	1.34%	-2.11%	0.69%	0.04%	0.36%	-	-	-	-	-	-			
000051	CSI 300 ETF Feeder Fund	10-Jul-09	11.39	2.02%	1.52%	-2.42%	1.15%	0.06%	0.93%	0.16%	0.93%	-0.59%	0.84%	-0.52%	0.95%	★★★	★★★	--
510050	China 50 ETF	30-Dec-14	30.15	-0.69%	0.89%	-3.57%	0.97%	0.15%	0.62%	-0.93%	0.55%	-0.39%	0.57%	-0.21%	0.86%	★★	★★★	★
159902	China SME ETF	8-Jun-06	2.94	0.22%	1.10%	-1.26%	0.41%	-0.58%	0.41%	-0.88%	0.60%	-0.16%	0.78%	-1.42%	0.76%	★★★	★★	--
001051	China 50 ETF Feeder Fund	17-Mar-15	0.49	-5.14%	5.79%	-	-	-	-	-	-	-	-	-	-			
512990	MSCI China A Index ETF	12-Feb-15	0.53	1.06%	1.87%	-	-	-	-	-	-	-	-	-	-			
000975	MSCI CHINA A ETF Feeder Fund	12-Feb-15	0.12	-0.03%	2.22%	-	-	-	-	-	-	-	-	-	-			
512500	CSI 500 ETF	5-May-15	1.15	2.61%	1.98%	-	-	-	-	-	-	-	-	-	-			
001052	CSI 500 ETF Feeder Fund	5-May-15	0.89	-0.44%	3.35%	-	-	-	-	-	-	-	-	-	-			

Source: ChinaAMC

- **ChinaAMC Active Equity VPS (Value-Payout-Sustainability) Strategy.**
 - ✓ Value and Large to Mid Cap Strategy Poised to benefit from MSCI Inclusion Decisions
 - ✓ Quantitative screening + Fundamental Stock Selection

Exhibit5: ChinaAMC VPS Portfolio has better dividend and valuation profile than the CSI 300 and MSCI China A index



Source: ChinaAMC

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