

FURTHER WEIGHT INCREASE OF CHINA A SHARES IN MSCI INDEXES

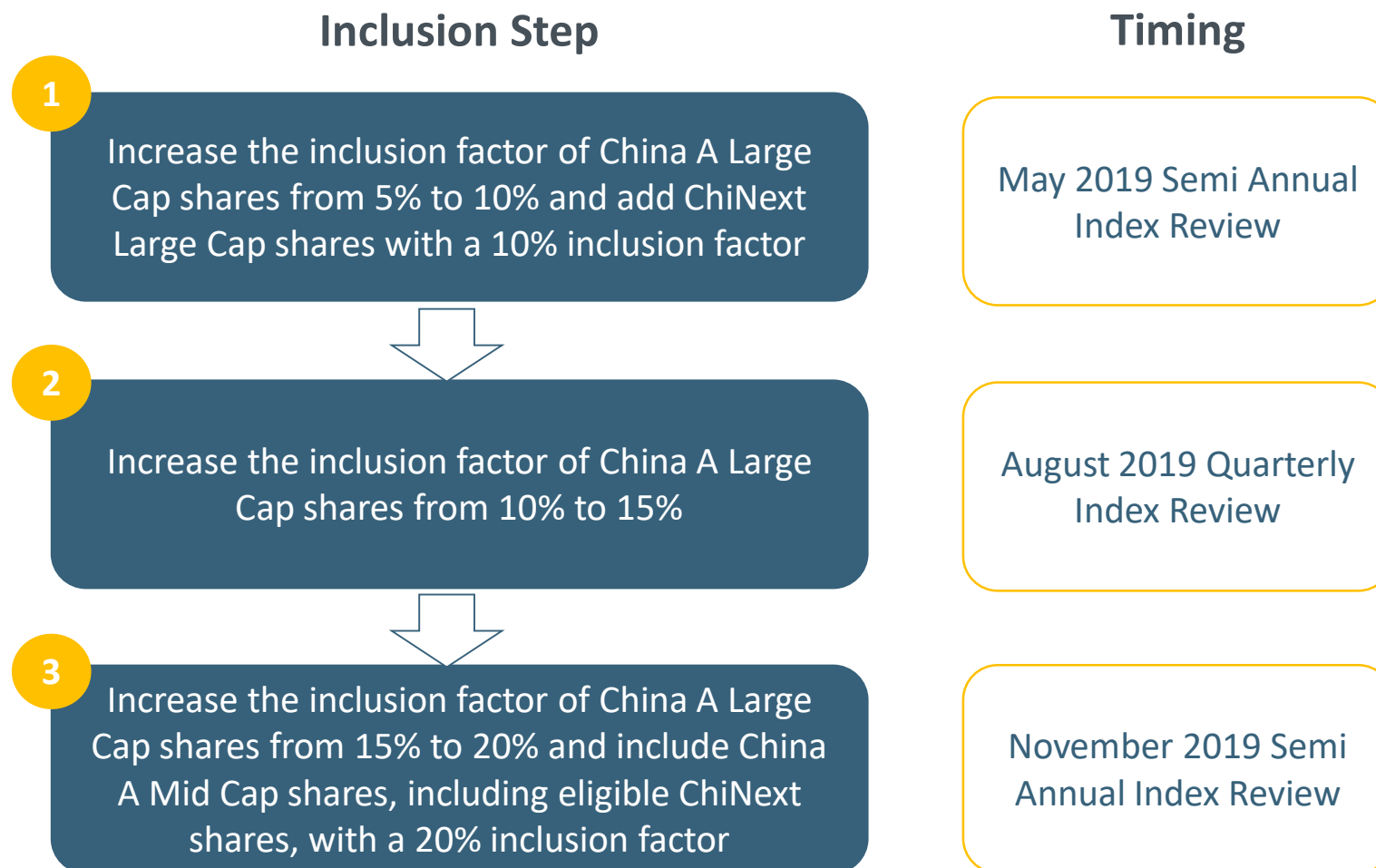
February 2019

EXECUTIVE SUMMARY

- MSCI announced on February 28, 2019 that it will **increase the weight of China A shares** in the MSCI Indexes using a **3-step inclusion process** beginning with the **May 2019 Semi-Annual Index Review**
- On completion of this three-step implementation, there will be 253 Large and 168 Mid Cap China A shares, including 27 ChiNext shares, on a pro forma basis in the MSCI Emerging Markets Index, representing a weight of **3.3% in the pro forma index**
- The decision follows overwhelming support for the weight increase from international institutional investors
 - The successful implementation of the initial 5% inclusion of China A shares provided investors with positive experience and confidence
 - Investors also welcomed the continuous commitment by the Chinese regulators to improve market accessibility including the significant reduction in trading suspensions in recent months
- MSCI performed an extensive global consultation with a large number of international institutional investors, including asset owners, asset managers, broker/dealers and other market participants worldwide

THREE STEP INCLUSION PROCESS

MSCI will increase the weight of China A in the MSCI Indexes as per the following schedule



MSCI CHINA A SHARES INCLUSION JOURNEY

CHINA'S MARKET LIBERALIZATION EFFORTS

MSCI CHINA A SHARES INCLUSION EFFORTS

2002-2012

QFII and RQFII schemes were launched in 2002 and 2011; both were relaxed and expanded in 2012

2013

QFII repatriation rules relaxed; First RQFII awarded and RQFII expanded to SG/London

2014

Capital gains tax clarified, RQFII expanded to more cities, Shanghai Connect launched

2015

RQFII expanded to more cities

2016

Shenzhen Connect launched; QFII/RQFII quotas linked to fund size, beneficial ownership clarified.

2017

Exchanges loosened pre-approval requirements that can restrict the creation of index-linked vehicles

2018

Connect Daily quota quadrupled; SSE introduced MOC; Suspension rules further tightened

2019

QFII quota doubled; CSRC launched consultation to harmonize and further relax QFII/RQFII schemes

June 2013

MSCI puts China A shares on the 2014 Market Classification Review list

June 2014 – 1st Consultation

No inclusion; issues on QFII/RQFII quota allocation, capital mobility, uncertainties on capital gains tax

June 2015 – 2nd Consultation

No inclusion; new concerns on beneficial ownership

June 2016 – 3rd Consultation

No inclusion; issues on QFII 20% monthly limit, stock suspension, pre-approval of investment instruments

June 2017 – 4th Consultation

MSCI announces inclusion of China A shares at 5% inclusion ratio in May and August of 2018

May 2018 and August 2018

Initial 5% inclusion of Large Cap China A shares was successfully implemented with positive feedbacks

February 2019 – 5th Consultation

MSCI announces a further increase in the weight of China A shares in MSCI Indexes

May 2019, August 2019, November 2019

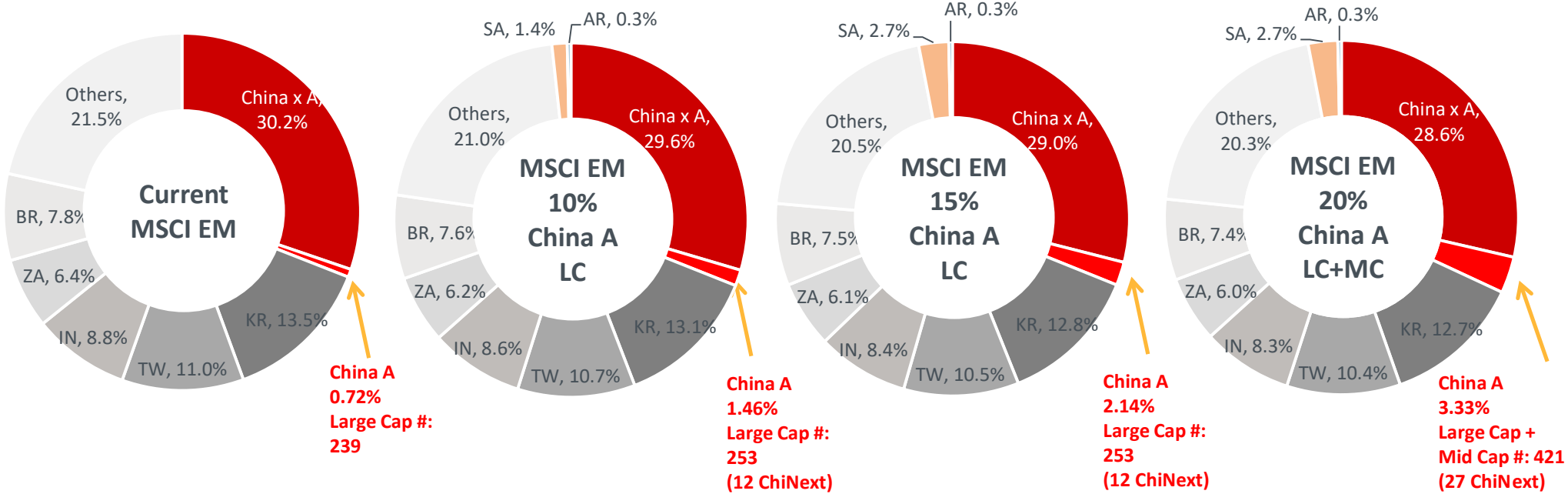
Implementing further weight increase of China A shares

PRO-FORMA WEIGHT IN MSCI EM INDEX

Step 1

Step 2

Step 3



May 2019

August 2019

Nov 2019

The pro forma MSCI Emerging Market Index is estimated to have an aggregate turnover of **5.8%*** from its current composition upon completion of the 3-step inclusion process

FEEDBACK FROM THE CONSULTATION

- **Overwhelmingly positive support** on further weight increase of China A Shares
 - Over 90% of investors MSCI consulted with* supported the proposal on increasing China A Large Cap inclusion factor to 20%, including China A Mid Cap stocks at 20% inclusion factor, and including ChiNext stocks respectively
- Investors prefer to see China A Large Cap stocks' weight increase in 3 steps
 - Three step implementation could help alleviate potential execution pressure on the implementation dates vs. originally proposed two-step plan
- A significant proportion of investors suggested a more timely implementation of China A Mid Cap stocks together with the Large Cap stocks' weight increase

ACCESSIBILITY ISSUES TO BE ADDRESSED BEYOND 20%

International institutional investors also stressed that a future weight increase of China A shares in the MSCI Indexes beyond 20% would require Chinese authorities to address the following accessibility concerns

- **Access to hedging and derivatives**
 - The lack of listed futures and other derivatives products hamper investors' ability to implement and risk manage a large scale inclusion
- **Short settlement cycle of China A shares**
 - The short settlement cycle of China A presents operational risk and tracking challenges. It becomes a larger risk as the A shares weight and number of securities grows
- **Trading holidays of Stock Connect**
 - The misalignment between onshore China and Stock Connect holidays continues to create investment frictions
- **Availability of Omnibus trading mechanism in Stock Connect**
 - A functioning omnibus mechanism is critical to facilitate best execution and lower operational risk

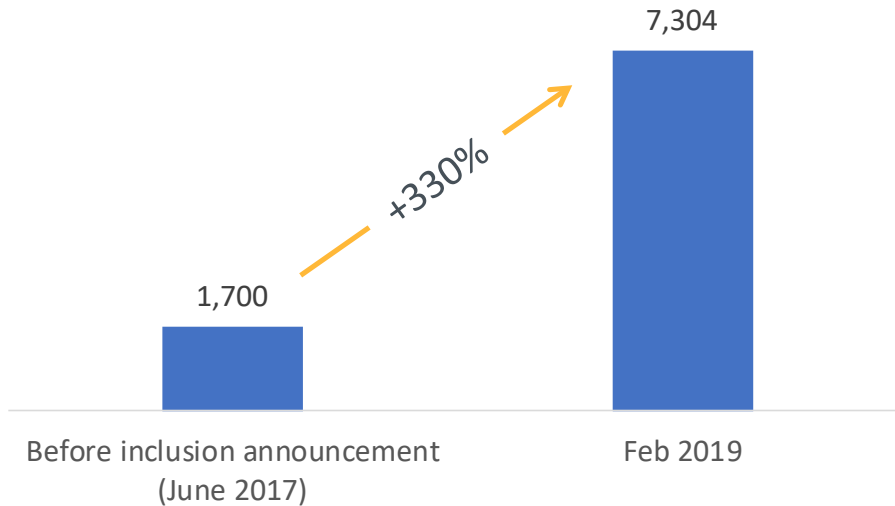
APPENDIX

Update on market liberalization developments in China

BROAD PARTICIPATION SINCE THE INITIAL INCLUSION

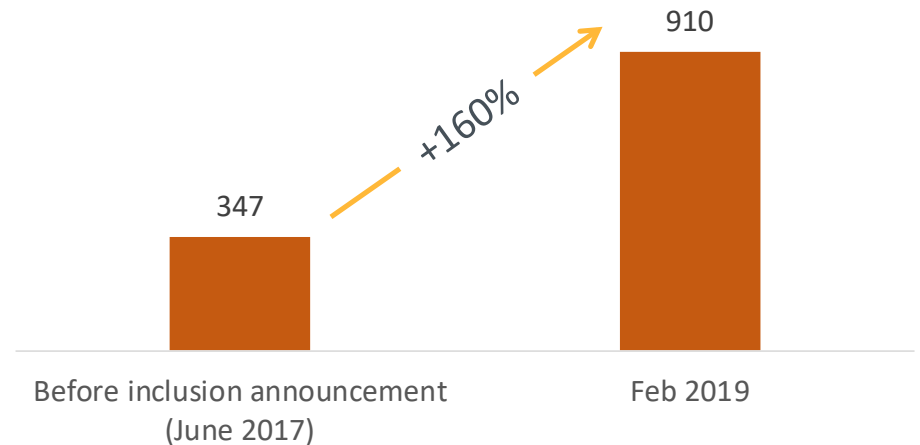
Since the announcement of the MSCI China A shares inclusion, more than **5,600** new Stock Connect accounts have been opened to trade China A shares and the total Northbound Connect portfolio value grew by **US\$84** billion

Number of SPSA accounts



Source: HKEx

Northbound Connect AUM Rmb billions



Source: HKEx

SIGNIFICANT ADVANCEMENTS IN ACCESSIBILITY ISSUES HIGHLIGHTED IN PREVIOUS CONSULTATIONS

Market Accessibility Issue Highlighted in Previous Consultation	Status of Resolution
<ul style="list-style-type: none"> • QFII and RQFII Quota Allocation (2015) 	<ul style="list-style-type: none"> • Harmonization of QFII and RQFII into a single scheme with simplified qualification requirement and Expanded investment scope
<ul style="list-style-type: none"> • Capital Mobility Restrictions in QFII/RQFII (2015) 	<ul style="list-style-type: none"> • The 20% monthly repatriation restriction was removed in 2018
<ul style="list-style-type: none"> • Beneficial Ownership in Stock Connect (2015) 	<ul style="list-style-type: none"> • Resolved after CSRC clarification
<ul style="list-style-type: none"> • Widespread Trading Suspensions (2016) 	<ul style="list-style-type: none"> • Suspensions dropped to historic low levels; SSE/SZSE implemented new suspension rules
<ul style="list-style-type: none"> • Anti-competitive clauses/pre-approval requirement on investment instruments (2016) 	<ul style="list-style-type: none"> • Pre-approval condition was abolished on non-derivatives financial products
<ul style="list-style-type: none"> • Absence of Market Closing Auction (2017) 	<ul style="list-style-type: none"> • Closing auction mechanism was implemented by Shanghai Stock Exchange in 2018
<ul style="list-style-type: none"> • Daily limit of Stock Connect (2017) 	<ul style="list-style-type: none"> • Daily net buy quota quadrupled in 2018

MARKET LIBERALIZATION CONTINUES TO DATE

The pace of market opening continued to accelerate during the past few months

Latest opening up measures in the China financial sector



APPENDIX

Update on trading suspension

SSE/SZSE TRADING SUSPENSION/RESUMPTION GUIDANCE

- **Narrowing down the list of approved reasons for trading suspension:** Suspensions arising from restructuring not involving share offering, non-public share offering, outward foreign investment and conclusion of material contracts are forbidden
- **Shortening the trading suspension term**
 - Limit the general trading suspension period to a maximum of 2-5 trading days.
 - Limit suspensions due to restructuring to 5-10 trading days
- **Enhancing disclosure requirements**
 - Companies need to disclose, among other information, the specific reasons for a trading suspension, the progress of the reorganization, and the anticipated trading resumption date
- **Improving the supporting regulatory mechanism.**
 - Clarification of trading suspension/resumption principles and mandatory resumption provisions, enhancements to due diligence of relevant parties and establishment of a trading suspension notification system

SIGNIFICANT REDUCTION IN TRADING SUSPENSIONS

Trading Suspension in Since June 2017

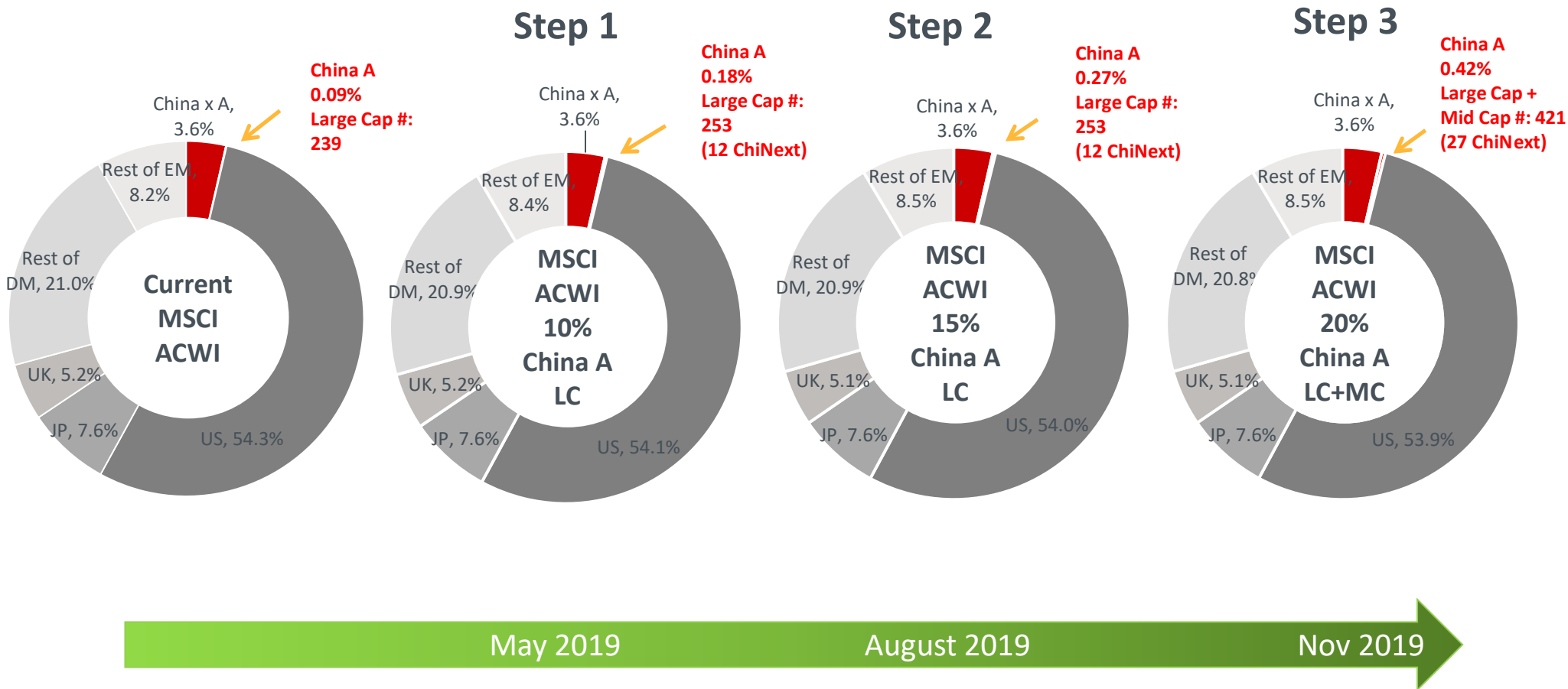


Based on the full China A shares universe of over 3,000 securities

APPENDIX

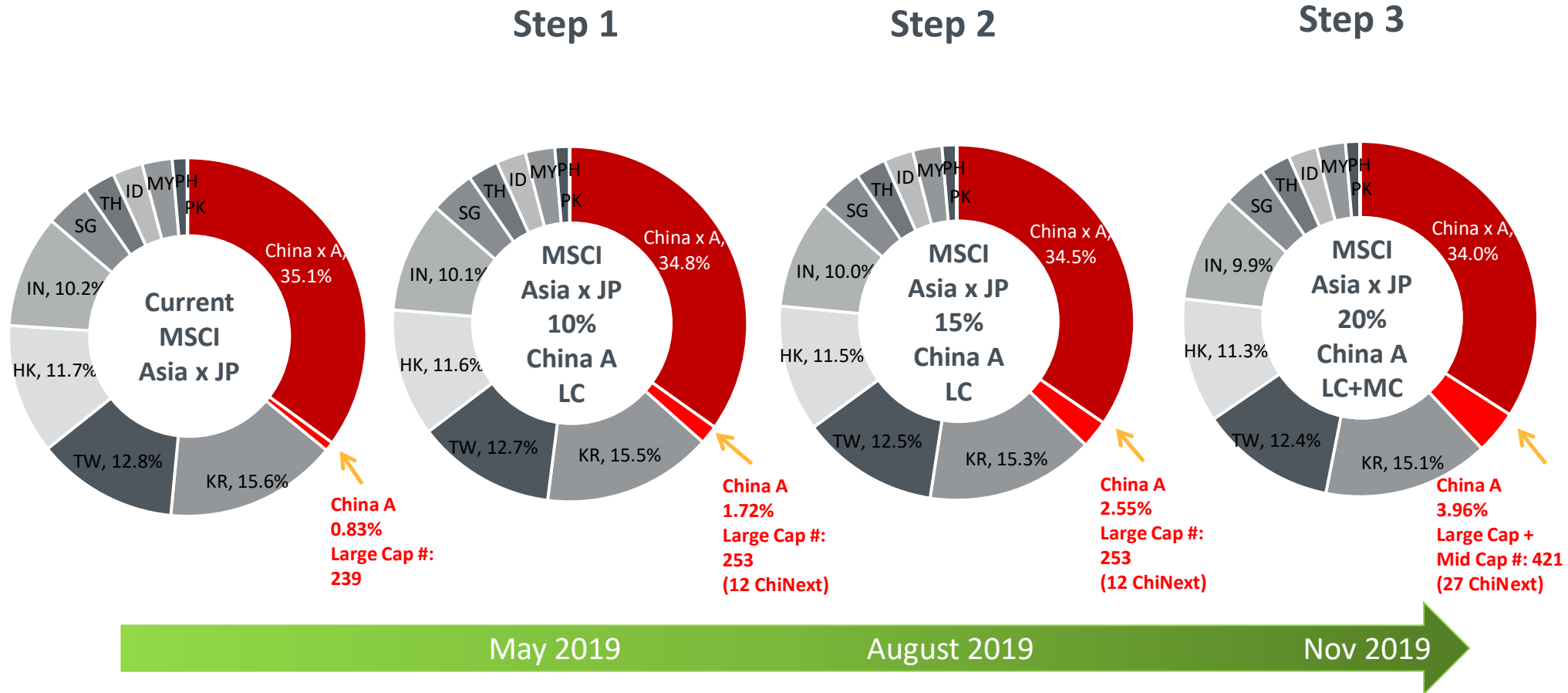
Further weight increase in MSCI ACWI, Asia ex Japan and China Indexes

PRO-FORMA WEIGHT IN MSCI ACWI INDEX



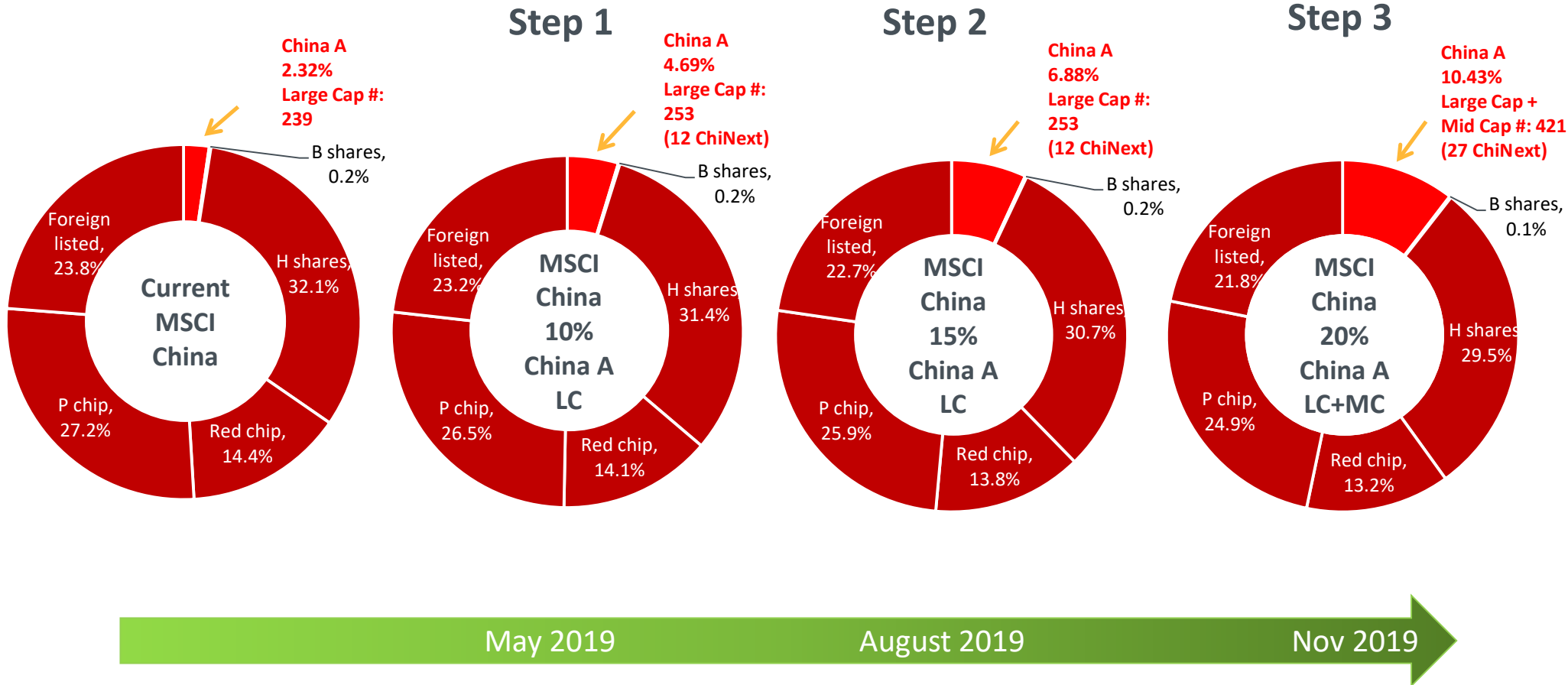
The pro forma MSCI ACWI Index is estimated to have an aggregate turnover of **0.7%*** from its current composition upon completion of the 3-step inclusion process

PRO-FORMA WEIGHT IN MSCI ASIA EX JAPAN INDEX



The pro forma MSCI Asia ex Japan Index is estimated to have an aggregate turnover of **3.3%** from its current composition upon completion of the 3-step inclusion process

PRO-FORMA WEIGHT IN MSCI CHINA INDEX



The pro forma MSCI China Index is estimated to have an aggregate turnover of **8.5%** from its current composition upon completion of the 3-step inclusion process

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