



Development of Cross-border ETFs

Case Study of HK ETFs Cross-Listed to Taiwan

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Hang Seng Investment



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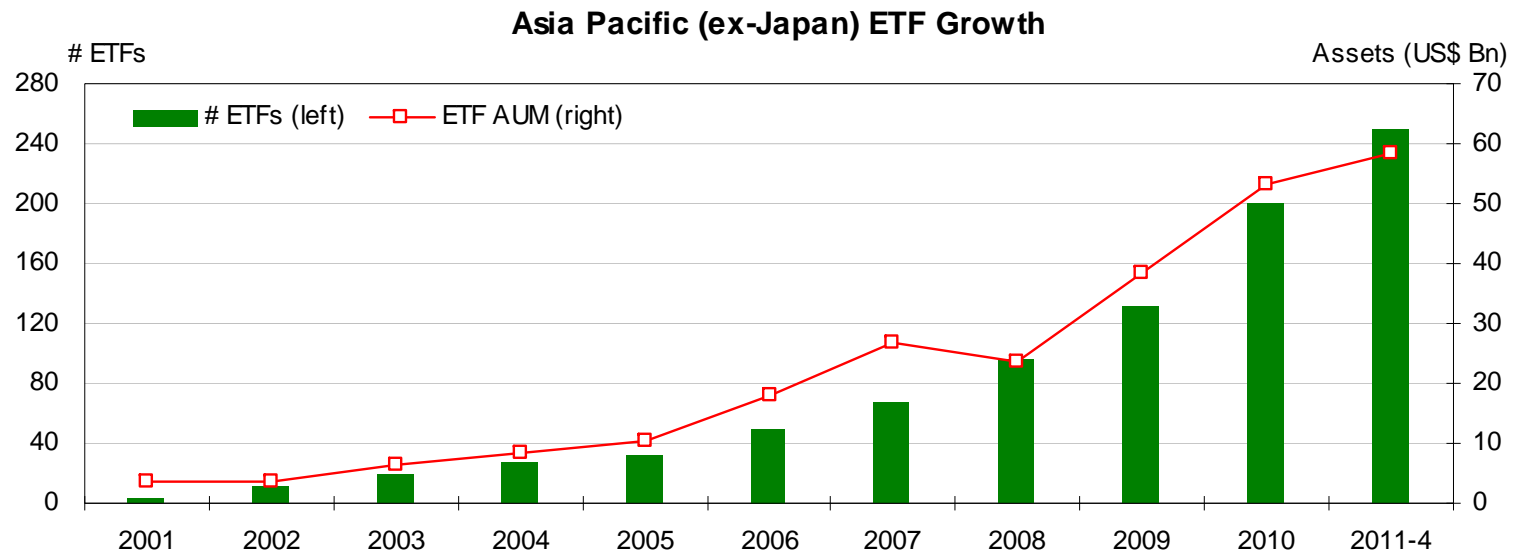
Outline

- Overview: ETFs and Cross-listing
- Regulations of ETFs Cross-listing
- Modes of Cross-listing
- Case study: Hang Seng ETFs



ETFs in Asia-Pacific

- ETFs market in Asia-Pacific region developed significantly during last 10 years, both in terms of number of ETF listed and assets under management (“AUM”).
- Total AUM of ETFs listed in HK is US\$27.9Bn (47.61% of Asia Pacific (ex-Japan)).



Source: BlackRock ETF Landscape, data as at 30 Apr 2011



ETFs and Listing Statistics

- As at 30 Apr 2011, globally there are 2,670 ETFs and 6,021 listings on different exchanges.
- In Asia ex-Japan, there are 250 ETFs and 362 listings.

| Metric | Global | | United States | | Europe | | Japan | | Asia ex-Japan | | Latin America | | Canada | | Middle East & Africa | |
|---------------|----------|----------------|---------------|----------------|---------|----------------|--------|----------------|---------------|----------------|---------------|----------------|---------|----------------|----------------------|----------------|
| | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) | Apr-11 | YTD change (%) |
| ETFs | | | | | | | | | | | | | | | | |
| AUM (US\$ Bn) | 1,469.8 | 12.1% | 997.3 | 11.9% | 328.2 | 15.5% | 29.4 | -8.8% | 58.6 | 10.0% | 10.4 | 3.1% | 43.1 | 12.3% | 2.8 | 21.1% |
| # ETFs | 2,670 | 8.5% | 972 | 8.5% | 1,128 | 5.2% | 84 | 5.0% | 250 | 25.0% | 27 | 3.8% | 180 | 14.6% | 29 | 0.0% |
| # listings | 6,021 | 8.4% | 972 | 8.5% | 3,952 | 6.8% | 88 | 6.0% | 362 | 17.9% | 407 | 11.8% | 211 | 14.1% | 29 | 0.0% |
| # providers | 140 | 2.9% | 29 | 3.6% | 39 | 0.0% | 7 | 0.0% | 63 | 6.8% | 4 | 0.0% | 4 | 0.0% | 10 | 0.0% |
| # exchanges | 48 | 4.3% | 2 | 0.0% | 23 | 4.5% | 3 | 50.0% | 13 | 0.0% | 3 | 0.0% | 1 | 0.0% | 3 | 0.0% |
| ADV (US\$ Mn) | 54,474.7 | 17.6% | 47,932.4 | 16.7% | 4,101.4 | 30.9% | 172.3 | 18.5% | 935.2 | 16.8% | 292.8 | 107.4% | 1,023.9 | -1.2% | 16.6 | 123.7% |

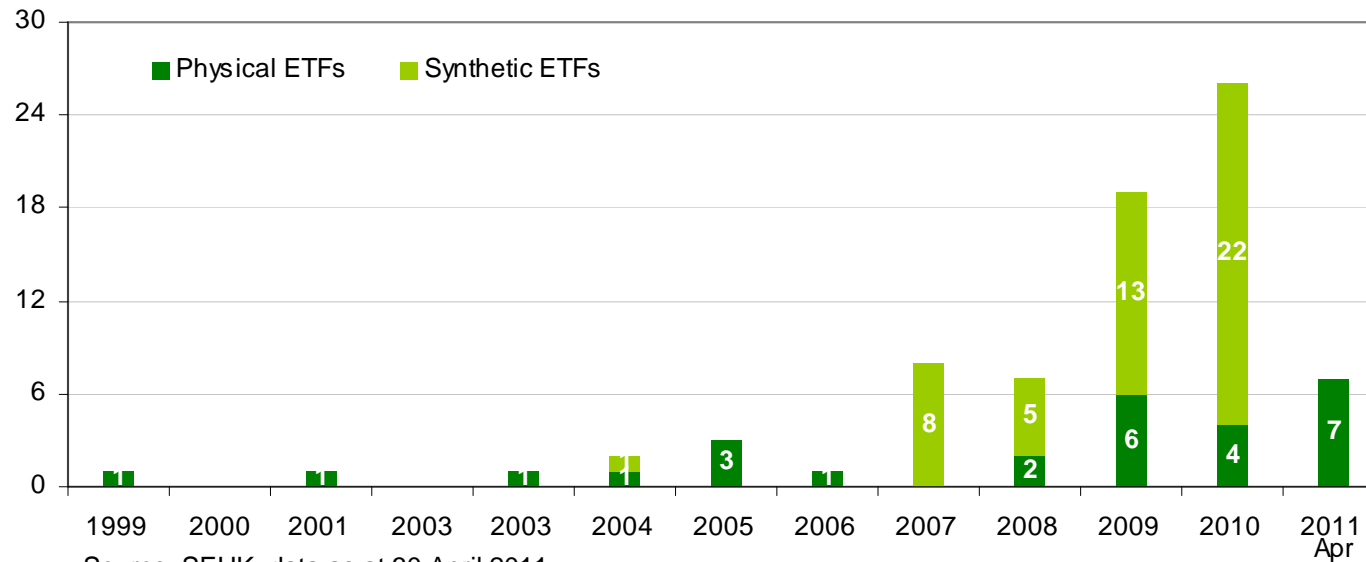
Source: BlackRock ETF Landscape, data as at 30 Apr 2011



ETFs in Hong Kong

- ETFs listed in SEHK increase steadily, especially after 2007.

Number of ETFs Listed on SEHK



Source: SEHK, data as at 30 April 2011

| Country | # primary listings | # total listings | # providers | AUM US\$ Bn |
|--------------|--------------------|------------------|-------------|-------------|
| 29 Australia | 24 | 45 | 6 | \$4.0 |
| 30 China | 22 | 22 | 16 | \$11.7 |
| 31 Hong Kong | 47 | 76 | 10 | \$27.9 |
| 32 India | 18 | 18 | 7 | \$0.6 |
| 33 Indonesia | 1 | 1 | 1 | \$0.0 |
| 34 Japan | 84 | 88 | 7 | \$29.4 |

| Country | # primary listings | # total listings | # providers | AUM US\$ Bn |
|----------------|--------------------|------------------|-------------|-------------|
| 35 Malaysia | 4 | 5 | 3 | \$0.4 |
| 36 New Zealand | 6 | 6 | 2 | \$0.4 |
| 37 Singapore | 23 | 81 | 8 | \$3.7 |
| 38 South Korea | 87 | 87 | 13 | \$6.8 |
| 38 Taiwan | 14 | 17 | 2 | \$3.0 |
| 40 Thailand | 4 | 4 | 3 | \$0.1 |

Source: BlackRock ETF Landscape, data as at 30 Apr 2011



Benefits of Foreign ETFs

- Benefit of Foreign ETFs for difference parties:
- Local Investors
 - Broader choices of investment instruments
 - Diversification
- Local Regulators
 - Put cross-border investment under regulatory control
- Local Market Practitioners
 - Participating Dealer
 - Profit generated from arbitraging between markets
 - Master Agent
 - Service fees paid by foreign fund managers
 - Brokers
 - Revenue from trading commissions
- Foreign Fund Managers
 - Management fee from higher AUM
 - Exposure (business, brand, etc.) in listing markets



Regulations of ETFs Cross-listing in TW

- 14 Oct 2008, Financial Supervisory Commission, Executive Yuan (“FSC”)
 - Amendments to *Regulations Governing Offshore Funds*
- 27 Nov 2008, Financial Supervisory Commission, Executive Yuan
 - Amendments to *Regulations Governing Securities Investment Trust Funds*



Regulations of ETFs Cross-listing TW (cont.)

- 22 May 2009, Hong Kong SFC and the Taiwan FSC
 - *Side Letter to a bilateral Memorandum of Understanding (MOU)*
 - *ETFs listed on the Hong Kong or Taiwan stock exchange and managed by asset managers licensed respectively by the SFC or the FSC will be mutually recognised in each other's jurisdiction for the purpose of cross listings and offerings*

- 9 Jun 2009, Taiwan Stock Exchange, amendments to
 - *Taiwan Stock Exchange Corporation Rules Governing Trading of Beneficial Certificates*
 - *Taiwan Stock Exchange Corporation Rules Governing Information Reporting by Companies with Exchange-Listed Securities and Offshore Fund Institutions with Exchange-Listed Offshore Exchange-Traded Funds*
 - *Taiwan Stock Exchange Corporation Rules Governing Review of Securities Listings*
 - *Taiwan Stock Exchange Corporation Procedures for Verification and Disclosure of Material Information of Securities Investment Trust Companies with Listed Securities Investment Trust Funds and Offshore Fund Entities with Listed Offshore Exchange-Traded Funds*
 - *etc.*



HK Regulations of overseas ETFs

- June 2010, Hong Kong SFC
 - Code on Unit Trusts and Mutual Funds
 - Appendix I Guidelines for regulating index tracking exchange traded funds
 - *Article 23 - 24: Streamlined recognition process for overseas ETFs listed in an acceptable ETF regime*
 - Annex (III): an overseas ETF is regulated in an Acceptable ETF Regime
 - Annex (IV):
 - (a) Compliance with the applicable laws and regulations of the relevant Acceptable ETF Regime;
 - (b) Compliance with the applicable listing rules and trading rules of the overseas exchange on which the ETF is primarily listed;
 - (c) There are no changes in the laws and regulations of the Acceptable ETF regime and the relevant overseas listing rules governing the offering and the listing of the ETF that would materially affect the Acceptable ETF Regime's comparability with that of Hong Kong. Where any material changes would be made to the securities regulations or the applicable listing rules of the Acceptable ETF Regimes thereby affecting their comparability with those of Hong Kong, the ETF or its management company must inform the SFC as soon as practicable; and
 - (d) The ETF complies in full with the applicable provisions in the guidelines.
- Comparing to TW
 - More flexible structure
 - No FX restrictions
 - etc.



Experiences in Other Countries

- Cross-listing of ETFs in various countries / regions
 - Difficult due to jurisdiction and regulatory differences.
 - Japan
 - Financial Instruments and Exchange Act
 - Investment Trust Act
 - Stock exchange regulation, e.g., Guidebook for Listing Foreign ETFs and Foreign Spot Commodity ETFs (8th edition, 17 Aug 2010)
 - Korea
 - Register with Financial Supervisory Commission (FSC)
 - Listing criteria (Article 42-2 of the Securities Market Listing Regulation)
- Laws and Regulations
 - one of the critical success factors for developing offshore ETF in local markets.



ETFs Categorization in TSE



Descriptions :

1. **"Domestic ETF"** is launched by domestic securities investment trust companies and listed on TWSE.
 - (1) **"ETF comprising only domestic securities"** : The constituents of ETF's underlying index are all domestic securities.
 - (2) **"ETF comprising foreign securities"** :
 - I. The underlying index of ETF consists of at least one foreign security.
 - II. **"Feeder Fund ETF"** is launched by domestic securities investment trust companies and linked to one offshore ETF.
2. **"Offshore ETF"** is launched by offshore asset management companies and cross-listed on TWSE.

Source: Taiwan Stock Exchange ("TSE")



Comparison of ETFs in TW

| | Offshore ETF | Domestic ETF | |
|---------------------------|--|--|--|
| | | ETF comprising foreign securities (Feeder ETF included) | ETF comprising only domestic securities |
| Issuer | Foreign issuer, and introduced by a master agent | Domestic issuer | Domestic issuer |
| Management fee | Charged by foreign issuer | Charged by both foreign issuer and domestic issuer | Charged by domestic issuer |
| Trading unit | Same as in primary exchange, e.g. 100 units or 200 units | 1,000 units | 1,000 units |
| Maximum price fluctuation | No limit | No limit | 7% |
| Quotation currency | Taiwan dollar | | |
| Trading venue | Any brokerage | | |
| Settlement period | T+2 days | | |
| Transaction fee | Negotiable, with the ceiling of 0.1425% | | |
| Transaction tax | 0.1%, levied on sell side only | | |
| Dividend income tax | Exempted | Exempted | Payable |
| Capital gains tax | N/A | | |
| <i>Example</i> | <i>Hang Seng H-Share Index ETF</i> | <i>W.I.S.E. Polaris CSI 300 Securities Investment Trust Fund</i> | <i>Taiwan Top50 Tracker Fund</i> |

Source: Taiwan Stock Exchange ("TSE")



Comparison of Dual-listing and Feeder Structure

| | Dual-listing Structure 直接跨境上市 (i.e. Off-shore ETF) | Feeder Structure |
|---------------|--|--|
| Pros | Higher transparency to investors | IPO allows a rapid accumulation of AUM at the initial stage |
| | Investors' rights are the same in the two markets | Issuer of the feeder fund has a higher incentive to build up the AUM |
| | One layer of management fee, cost to investors is lower | Benefit from the local presence and distribution channel of the issuer |
| | Arbitrage opportunity through PDs' creation / redemption | |
| | Tracking error is lower | |
| Cons | Time is needed to build up the AUM | Two layers of fees |
| <i>Sample</i> | <i>Hang Seng H-Share Index ETF</i> | <i>W.I.S.E. Polaris CSI 300 Securities Investment Trust Fund</i> |



Hang Seng H-Share Index ETF

Hang Seng H-Share Index ETF tracks performance of Hang Seng China Enterprises Index (“H-Share Index”). H-Share Index is composed of 40 constituent stocks and covers 91.8% of all H Shares market value.

| Listing | Hong Kong | Taiwan |
|-----------------------|--|---|
| Exchange | The Stock Exchange of Hong Kong – Main Board | Taiwan Stock Exchange |
| Listing Date | 10 Dec 2003 | 14 Aug 2009 |
| Stock Code | 2828 | 0080 |
| Trading Lot Size | 200 Units | 200 Units |
| Currency | HKD | NTD |
| Max Price Fluctuation | N/A | |
| Asset Value | Total Asset Value 22.53 Billion HKD ; HK NAV 133.31 HKD per Unit (TW NAV 133.31 x Exchange Rate 3.74 = 498.58 NTD per Unit) | |
| Expenses | Management Fee 0.55% per annum, Trustee Fee 0.05% | |
| Dividend | Semi-annually (if any) | |
| Fund Manager | Hang Seng Investment Management Limited (“Hang Seng Investment”) | |
| Trustee | HSBC Provident Fund Trustee (Hong Kong) | |
| Participating Dealer | Hang Seng Securities Limited, Yuanta Securities (Hong Kong) Company Limited, etc. | Yuanta Securities, IBT Securities Limited, Capital Securities |

Source : Hang Seng Investment Management Limited, Hang Seng Index Limited, data as at 31 March 2011



Hang Seng Index ETF

Hang Seng Index ETF tracks performance of Hang Seng Index. Hang Seng Index is composed of 45 constituent stocks and covers 58.15% of all market value.

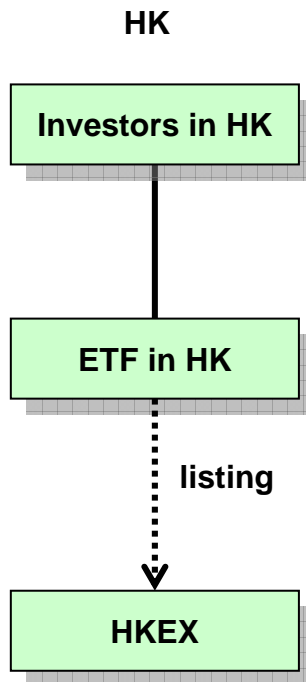
| Listing | Hong Kong | Taiwan |
|-----------------------|--|---|
| Exchange | The Stock Exchange of Hong Kong – Main Board | Taiwan Stock Exchange |
| Listing Date | 21 Sep 2004 | 14 Aug 2009 |
| Stock Code | 2833 | 0081 |
| Trading Lot Size | 100 Units | 100 Units |
| Currency | HKD | NTD |
| Max Price Fluctuation | N/A | |
| Asset Value | Total Asset Value 30.73 Billion HKD ; HK NAV 237.15 HKD per Unit (TW NAV 237.15 x Exchange Rate 3.74 = 886.94 NTD per Unit) | |
| Expenses | Management Fee 0.05% per annum, Trustee Fee 0.05% per annum | |
| Dividend | Semi-annually (if any) | |
| Fund Manager | Hang Seng Investment Management Limited (“Hang Seng Investment”) | |
| Trustee | American International Assurance Company (Trustee) Limited | |
| Participating Dealer | Hang Seng Securities Limited, Yuanta Securities (Hong Kong) Company Limited, etc. | Yuanta Securities, IBT Securities Limited, Capital Securities |

Source : Hang Seng Investment Management Limited, Hang Seng Index Limited, data as at 31 March 2011

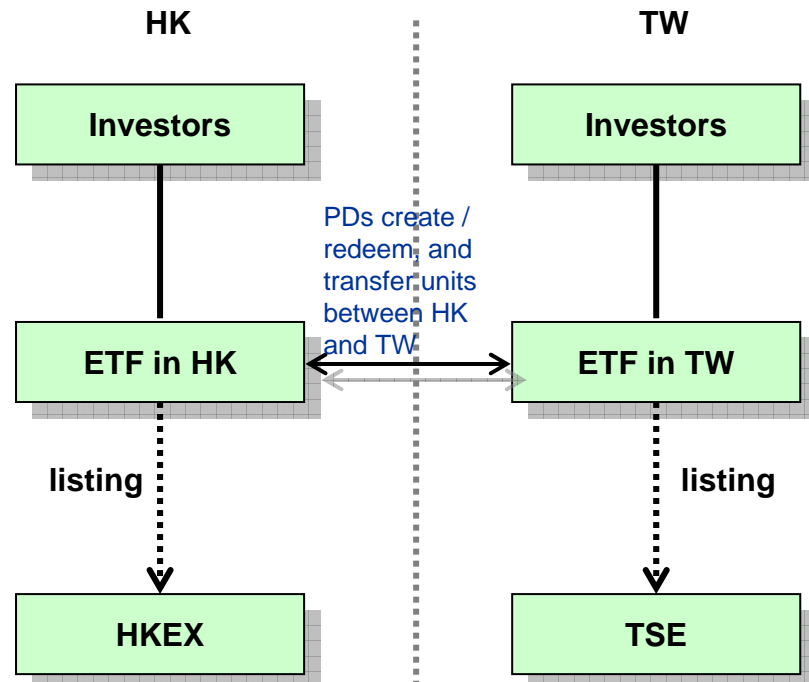


Key Attributes of Dual-listing Structure

Before Dual-listing



After Dual-listing




No change of structure in HK

ETF units in TW is the same class as units in HK



Key Attributes of Dual-listing Structure

Dual-listing



- Overseas fund manager remains the product issuer
- Same class of listed units in HK (HKD) & Taiwan (NTD)
- Units are “fungible” between the two markets
- Rights of investors identical in the two markets
- No delivery of constituent stocks in Taiwan
- Subject to the regulations governing offshore Fund

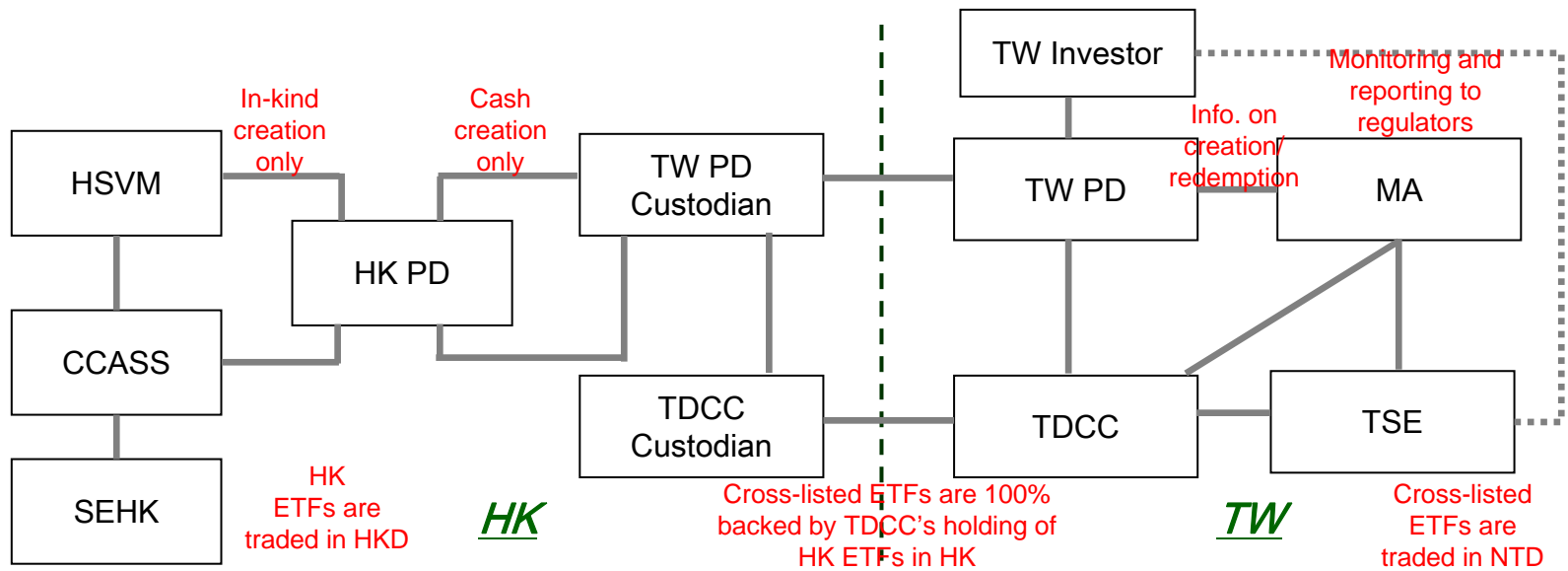


Key Parties

| Party | Functions |
|--------------|--|
| ETF Manager | <p>Hang Seng Investment Management Limited (“HSVM”)</p> <ul style="list-style-type: none"> • A wholly-owned subsidiary of Hang Seng Bank Limited • Fund manager of the HK-listed ETF |
| Master Agent | <p>HSBC Global Asset Management (Taiwan) Limited</p> <ul style="list-style-type: none"> • Representative of the ETF in Taiwan • Seeking approval from Securities Investment Trust & Consulting Association (“SITCA”), Securities & Futures Bureau (“SFB”) & TSE • Sales and marketing • On-going reporting to regulators/TW investor communication • Monitoring of PD activities (including FX quota) • Handling dividend payment and corporate action of the ETF |
| Taiwan PD | <p>Taiwan domestic companies - Yuanta, IBT, Capital, etc.</p> <ul style="list-style-type: none"> • Responsible for cash creation/redemption of ETF • Arbitrage within Taiwan and between HK/Taiwan market |
| Clearings | <p>Taiwan Depository & Clearing Corporation (“TDCC”)</p> <ul style="list-style-type: none"> • Counterpart of CCASS in Taiwan • Safe-keeping of ETF units issued to Taiwan investors |



Overview of Dual-listing Setup



Notes:

| | |
|-------|---|
| MA | Master Agent (<i>HSBC Global Asset Management (Taiwan) Limited</i>) |
| TW PD | Taiwan Participating Dealer |
| HK PD | Hong Kong Participating Dealer |
| SEHK | Stock Exchange of Hong Kong |
| CCASS | Central Clearing And Settlement System |
| TSE | Taiwan Stock Exchange |
| TDCC | Taiwan Depository and Clearing Corporation |



Challenges in Cross-listing

Value Creation

- ❑ Business opportunities and incentives for MA / PD and value added to local investors

Technical Issues

- ❑ Selection of the listing structure and the identification of appropriate partners
 - Preference gap existing between MA, PD and Fund Manager on Feeder and Dual-listing
- ❑ Different trading hours (Risk for PDs in market making for ETFs)
- ❑ FX quota limit control in Taiwan

Governing Law

- ❑ HK / TW listed ETFs are governed by laws and regulation of HK / TW, respectively
 - Side Letter to MOU between HK SFC and TW FSC

Marketing and Investor Education

- ❑ Communication and coordination with MA in marketing and investor education
- ❑ Adhere to local laws and regulations



Key Success Factors

- Laws and regulations
- Contribution of regulators
- Capability of participants (e.g. issuer, PD, etc.)
- Operational efficiency
- Investor education



Thanks



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