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A Comparative Study of Stock Exchanges in China, Hong Kong, and Taiwan

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Abstract

Equity exchanges are sprouting in developing countries due to the privatization of state-owned enterprises. China officially opened its first recognized stock exchange, the Shanghai Security Exchange in December, 1990 and a few months later the Shenzhen Stock Exchange opened. This paper compares the micro-structure of the equity markets in China, Hong Kong, and Taiwan.

For a foreign investor, the markets in Hong Kong contain the least restriction and are the most accessible. Both China and Taiwan impose restrictions on foreign investment. China restricts foreign investment by only allowing the purchase of B shares Chinese exchanges, while Taiwan limits foreign investors to only four investment funds. China also allows for higher commissions on foreign investor purchases. In addition, Non-Chinese investors in A shares may be subject to a 20% withholding tax on that portion of dividend income that exceeds the People's Bank of China's one-year rate for the same period.

These discriminatory measures can be expected to have a negative impact on foreign capital inflows and to reduce the liquidity of these markets. The impact on the prices of shares and potential rates of return cannot be positive from these restrictions since, all else constant, lower demand implies lower price. It may be, however, that the inherent potential in these growing markets from recent political and economic changes may create high rates of return, despite the restrictions on capital flows. There are also other alternatives for capital inflows to direct stock investment, such as Foreign Direct Investment (FDI). FDI, in turn, may well flow through to higher stock prices.

Keywords: emerging markets, market regulations

1. Introduction

Equity exchanges are sprouting in developing countries due to the privatization of state-owned enterprises. China officially opened its first recognized stock exchange, the Shanghai Security Exchange in December, 1990 and a few months later the Shenzhen Stock Exchange opened. This paper compares the micro-structure of the equity markets in China, Hong Kong, and Taiwan. Data and analysis are obtained through Bloomberg's financial online service. Bloomberg provides 24-hour, instant and current financial, economic and political information covering markets around the globe. It also provides analytics, historical data, up-to-minute news reports, economic statistics and political commentaries. Constant upgrades and enhancements of the system are some of the most valuable attributes of the Bloomberg service.

2. Profiles of Three Stock Markets

Emerging markets share of total world market capitalization is 13%. China and Taiwan's shares of total emerging market capitalization are 2.3% and 12.8%, respectively. Hong Kong is listed under developed markets and its share in the total developed market capitalization is 1.8%. Table 1 reports the market size, number of firms listed, turnover ratio, and P/E ratio of each market. The same statistics of the New York Stock Exchange (NYSE) in the U.S. are also reported for comparison.

Table 1 shows a combined listing of 1,471 firms for the three countries China, Hong Kong, and Taiwan, approximately half of the number listed on the New York Stock Exchange. The total market capitalization for these three countries is $638 billion, less than one tenth of the size of the NYSE market cap. While both

Taiwan's Stock Exchange and Hong Kong's Stock Exchange are of similar size, China's less than seven year old equity markets are much smaller. Even though much smaller in land mass and population, the Hong Kong Stock Exchange has more listed firms than China or Taiwan. Both the China and Taiwan Stock Exchanges have markedly higher turnover ratios (the proportion of trading volume to market capitalization) than Hong Kong or the NYSE. Taiwan's low transaction cost and high savings rate have been cited as the cause for the Taiwan Stock Exchange's lead in trading volume among Asian equity markets, second only to the Tokyo Stock Exchange. The price earnings (P/E) ratio reflects a similar phenomenon, with the Taiwan Stock Exchange higher than those in the Hong Kong and China Exchanges.

Table 1. Basic statistics of equity markets in China, Hong Kong, and Taiwan

Country	Total Market Capitalization (US # Billion)	Number of Firms Listed	Turnover Ratio (%)	P/E ratio
China	70.79	511	235.2	15.5
Hong Kong	303.70	585	77.6	17.2
Taiwan	264.10	375	323.1	28.3
U.S. (NYSE)	7,300.00	2,907	56.1	18.9

Source: Bloomberg/International Finance Corporation 2016.

3. Characteristics of Three Stock Markets

Table 2 summarizes the profiles of each market. The Table shows the stock exchanges in each country, the hours of operation, the type of trading system employed, a list of stock market indices, settlement and transfer information, types of securities traded on the exchanges, tax implications for foreign investors, reporting requirements, and investment regulations.

The two stock exchanges in the Greater China, the Shanghai Securities Exchange and the Shenzhen Stock Exchange, have relatively short trading hours (9:30 A.M. to 11:00 A.M. and 1:00 P.M. to 3:00 P.M.) as compared to the New York Stock Exchange's 62 hour trading day. The Taiwan Stock Exchange also has limited trading hours (9:00 A.M. to 12:00 Noon, Monday through Friday, and 9:00 A.M. to 11:00 A.M. on Saturday) in comparison to the NYSE. China has developed a security Trading Automated Quotation System which has equivalent trading hours to the NYSE.

Various types of securities are traded in all exchanges which include common and preferred shares, government and corporate bonds, convertibles, rights and warrants. However, in China, common shares are divided into A shares and B shares. A shares which include state, enterprise and individual shares can be traded by domestic investors. Foreign investors can only trade in B shares. B shares are traded in U.S. dollars on the Shanghai Securities Exchange and in Hong Kong dollars on the Shenzhen Stock Exchange.

Commissions are lowest in Taiwan. For shares traded on the Taiwan Stock Exchange, brokers charge 0.1425% of the amount traded. In Hong Kong, brokers collect a minimum of 0.25% on the sale of shares. The commissions are collected by brokers at Shanghai Stock Exchange is 0.5% of transacted value. On the Shenzhen Stock Exchange, the brokerage commission is 0.4% for A shares and 0.6% for B shares.

4. Conclusion

For a foreign investor, the markets in Hong Kong contain the least restriction and are the most accessible. Both China and Taiwan impose restrictions on foreign investment. China restricts foreign investment by only allowing the purchase of B shares Chinese exchanges, while Taiwan limits foreign investors to only four investment funds. China also allows for higher commissions on foreign investor purchases. In addition, Non-Chinese investors in A shares may be subject to a 20% withholding tax on that portion of dividend income that exceeds the People's Bank of China's one-year rate for the same period.

In Taiwan, dividends are subject to a 20% withholding tax if the investment is approved under the Statute for Investment by Foreign Nation and 35% if it is not. At the time of repatriation of income or capital, non-Taiwanese investors need to register with or gain permission from the Taiwanese Central Bank, which may restrict the timing of exchange release.

These discriminatory measures can be expected to have a negative impact on foreign capital inflows and to reduce the liquidity of these markets. The impact on the prices of shares and potential rates of return cannot be positive from these restrictions since, all else constant, lower demand implies lower price. It may be, however, that the inherent potential in these growing markets from recent political and economic changes may create high rates of return, despite the restrictions on capital flows. There are also other alternatives for capital inflows to direct stock investment, such as Foreign Direct Investment (FDI). FDI, in turn, may well flow through to higher stock prices.

Table 2a. Stock exchanges and their characteristics in China, Hong Kong, and Taiwan

Country	Exchange	Hours of Operation	Trading System	Indices	Commissions
China	Shanghai Securities Exchange 15 Huangpu Road Shanghai 200080 People's Republic of China Telephone: (21) 306 8888 Shenzhen Stock Exchange 15/F International Trust and Investment Building Hong Ling Zhong Road Shenzhen 518001 People's Republic of China Telephone: (755) 557 4637 Securities Trading Automated Quotation System Asia Hotel Xinzhong Xijie Gongti Bei Lu Beijing 100027 People's Republic of China Telephone: (1) 500 7788 Ext. 41	9:30am to 11:00am and 1:00pm to 3:00pm Monday to Friday. 9:30am to 11:00am and 1:00pm to 3:00pm Monday to Friday. 9:30am to 4:00pm Monday to Friday.	Trading is accomplished using a computerized system.	The Shanghai Securities Exchange Index, Shenzhen Stock Exchange Index and Jingan Index are the most commonly watched indices for the People's Republic of China exchanges.	Commissions collected by brokers as the result of the sale of shares is 0.5% of transacted value on the Shanghai Exchange with a minimum fee of $20.00. On the Shenzhen Exchange, the brokerage commission is 0.4% for AA≅ shares and 0.6% for AB≅ shares.
Hong Kong	The Stock Exchange of Hong Kong, Ltd. P. O. Box 8888 First Floor One & Two-Exchange Square Central Hong Kong Telephone: (852) 522 1122 Internet Web-Site: n/a	10:00 am to 12:30 pm and 2:30 pm to 3:55 pm, Monday to Friday.	Trades are accomplished using a computerized system.	Heng Seng Stock Index (**HIS**); AMEX Hong Kong 30 Index (**HKX**); AMEX Hong Kong Option Index (**HKO**)	Brokers collect a minimum of 0.25% on the sale of shares.
Taiwan	Taiwan Stock Exchange Corporation 7-10th Floors City Building 85 Yen-Ping South Road, Taipei, Taiwan Telephone: (2) 311 4020 Internet Web-Site: http://www.tse.com.tw	9:00am to 12:00 noon Monday to Friday and 9:00am to 11:00am on Saturday	Buy and sell orders are entered and displayed on the Exchange's computer, where they are matched.	Taiwan Weighted Index (**TWSE)**	Brokers collect a commission on the sale of shares of .1425% of the amount of the sale.

Source: Bloomberg/International Finance Corporation 2016.

Table 2b. Stock exchanges and their characteristics in China, Hong Kong, and Taiwan

Country	Settlement and Transfer	Types of Securities	Tax Implications for Foreign Investors	Reporting Requirements
China	Settlement takes place three trading days following the transaction date.	Treasury bonds, financial instruments, investment bonds, corporate bonds, AA≅ shares, which comprise state, enterprise and individual shares, and AB≅ shares, which are reserved for non-Chinese owners, are traded on the Exchanges.	Non-Chinese investors in AB≅ shares may be subject to a 20% withholding tax on that portion of dividend income above the People's Bank of China=s one-year Renminbi CD rate for the same period.	Listed companies are required to report any price sensitive events to regulatory authorities who then decide whether the news should be disclosed to the public.
Hong Kong	Share certificates and payment are exchanged two days following the transaction date.	Common, preference, preferred common and convertible stocks, bonds, unit trusts, rights and warrants are traded on the exchange.	Neither dividends nor capital gains are taxed that result from shares owned in Hong Kong companies.	Listed companies are required to disclose to their shareholders and the Exchange dividend information, announcements concerning profits and losses and anything that may affect their financial position. Directors=reports must disclose information on the company=s and each director=s bank loans and other borrowings and each director=s beneficial interest in the share capital of the company.
Taiwan	Settlement takes place the next trading day following the transaction.	Common and preference shares and government, corporate and convertible bonds are traded on the Exchange.	Non-Taiwanese investors are permitted to invest in only four investment funds. Dividends paid to non-Taiwanese investors are subject to a 20% withholding tax if the investment is approved under the Statute for Investment by Foreign Nationals and 35% if it isn't. Capital gains are not taxed.	Listed companies are required to report to the Securities and Exchange Commission within two days anything that may affect the business or affairs of the company. Companies must submit annual, semi-annual and quarterly financial statements and monthly operating reports.

Source: Bloomberg/International Finance Corporation 2016.

Table 2c. Stock exchanges and their characteristics in China, Hong Kong, and Taiwan

Country	Foreign Shareholder Limits
Taiwan	1. Overseas investor can purchase a total of 25 percent of a company=s shares. 2. Single foreign investor may buy up to 10 percent of an individual company=s shares.

Source: Bloomberg/International Finance Corporation 2016.

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