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Research Paper No. 57: Half-yearly Review of the Global and Local Securities Markets

17 July 2015



Executive summary

1. In the US, the Dow fell 1.1% during the first half of 2015 whilst the S&P 500 (S&P) and Nasdaq rose 0.2% and 5.3% respectively. After initial uncertainties about economic growth and the outlook for corporate earnings, all three indices hit record highs. Concerns of an early interest rate hike eased as economic recovery continued albeit not strongly. Subsequent concerns of the Fed on valuation trimmed gains, and the collapse of the Greek bailout deal spurred some sell-offs.
 2. In Europe, market performance was mixed. The FTSE edged lower by 0.7%, whilst the DAX and CAC rose 11.6% and 12.1% respectively. The FTSE and DAX hit record highs as improved economic prospects from a larger-than-expected stimulus package by the European Central Bank (ECB) paced gains. However, worries over a possible debt default and concerns that Greece might exit the Eurozone lingered, and major European markets retreated as Greece missed its loan repayment to the IMF and imposed capital controls. The DAX and CAC trimmed some gains.
 3. In Asia, the Nikkei rose 16.0% and hit an 18-year high amid better prospects for economic growth. The Bank of Japan maintained its accommodative monetary policy. A weaker Yen also provided support. The performance of other major regional markets was mixed, ranging from a 6.1% loss in Indonesia to an 8.7% gain in Vietnam.
 4. The Mainland market was one of the best performers amongst major markets worldwide, with the Shanghai Composite Index (SHCOMP) and Shenzhen Composite Index (SZCOMP) rising 32.2% and 74.1% respectively. Trading once hit a record high of over RMB2.3 trillion in May. Optimism prevailed despite a cut in the growth target to 7%, as monetary easing measures and prospects of the “One Belt, One Road” and the Mainland-Hong Kong Mutual Recognition of Funds initiatives helped to pace gains. However, the market was volatile on concerns about high valuations and liquidity conditions ahead of initial public offerings (IPOs). Investor sentiment was also affected by worries over the tightening of margin financing, which peaked at RMB2.2 trillion, and possible deleveraging activities.
 5. In Hong Kong, the Hang Seng Index (HSI) and the Hang Seng China Enterprises Index (HSCEI) rose 11.2% and 8.3% respectively following the rally in the Mainland market. The HSI hit a seven-year high of over 28,000. Daily market turnover also rose to a fresh high. However, the market was volatile amid worries over cooling measures in the Mainland market. Uncertainties about the timing of the US interest rate hike and the Greek debt problem also weighed on sentiment.
 6. Some of the major risks and uncertainties facing the Hong Kong market include:
 - valuation concerns, deleveraging activities and uncertainties about the economic outlook on the Mainland;
 - uncertainties about the timing and the magnitude of the interest rate hike in the US; and
 - concerns about the debt problem in Greece which may result in instability in the Eurozone.
 7. Trading in both the cash market and exchange-traded derivatives rose. Average daily trading in the cash market rose 65% from the second half of 2014. Trading in futures products rose 31%, whilst that in options products rose 28%.
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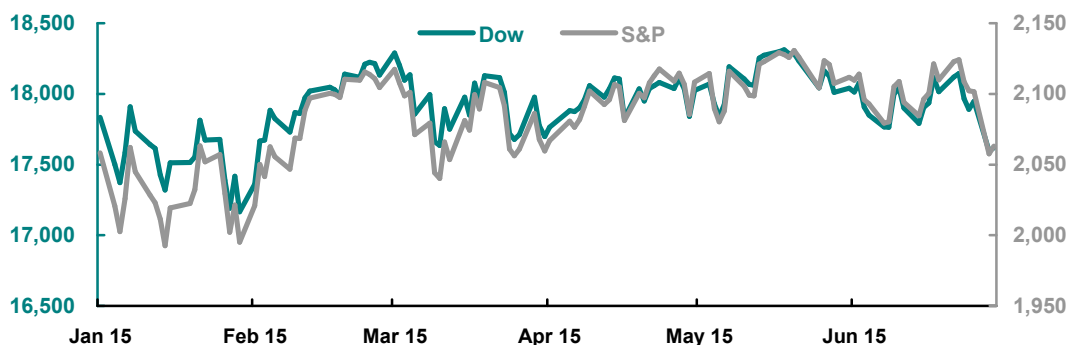


Performance of stock markets during the first half of 2015

8. During the first half of 2015, the Hong Kong market rose, boosted by the bullish performance of the Mainland market. However, valuation concerns lingered as major overseas market indices rose to record highs. Uncertainties about the timing and pace of the US interest rate hike and the Greek debt situation also weighed on sentiment.

The US

9. During the first half of 2015, the Dow fell 1.1%, whilst the S&P and Nasdaq rose 0.2% and 5.3% respectively. In 2014, the indices gained 7.5%, 11.4% and 13.4% respectively.
10. In early 2015, the market was volatile given uncertainties about the timing of an interest rate hike. The Fed remarked that economic growth was solid and removed the pledge to be patient in raising rates from its policy statement. Worries about the economic outlook also affected investor sentiment. The World Bank cut its global growth forecast for 2015 from 3.4% to 3.0% (and subsequently to 2.8%). Energy stocks fell as oil prices hovered around six-year lows.
11. Later, rate hike concerns eased somewhat given signs of a weak economy. GDP in the first quarter shrank by 0.2%. Also, a stronger US dollar weighed on the outlook for multinationals' earnings.
12. In May, the Dow, S&P and Nasdaq all hit record highs as moderate economic data suggested that recovery was on track, but was not strong enough to justify an early rate hike. Later, gains were trimmed after Fed Chairperson Janet Yellen warned about high equity valuations.
13. The Fed, in its latest policy meeting in June, commented that the strength of the economy meant it would be able to withstand an interest rate hike later this year, and it was appropriate to raise the interest rate at a gradual pace in late 2015. However, there were some selloffs later as the disagreement between Greece and international lenders on the bailout deal spurred worries over the stability in the Eurozone.



Performance of Dow and S&P during the first half of 2015

Source: Bloomberg



Performance of major stock markets

		End of June 2015	% change			PE Ratios
		Index Level	Year-to-date	2014	2013	End-June 2015
Hong Kong and the Mainland						
Hong Kong	-HSI	26,250.03	11.2%	1.3%	2.9%	10.91
	-HSCEI	12,981.23	8.3%	10.8%	-5.4%	9.48
Mainland	-Shanghai Comp	4,277.22	32.2%	52.9%	-6.7%	21.56
	-Shenzhen Comp	2,464.23	74.1%	33.8%	20.0%	60.65
Asia						
Japan	-Nikkei 225	20,235.73	16.0%	7.1%	56.7%	22.87
Australia	-AOI	5,451.20	1.2%	0.7%	14.8%	26.85
Taiwan	-TWSE	9,323.02	0.2%	8.1%	11.8%	14.04
Korea	-KOSPI	2,074.20	8.3%	-4.8%	0.7%	17.78
Singapore	-STI	3,317.33	-1.4%	6.2%	0.0%	14.92
Thailand	-SET	1,504.55	0.5%	15.3%	-6.7%	20.01
Malaysia	-KLCI	1,706.64	-3.1%	-5.7%	10.5%	16.81
Indonesia	-JCI	4,910.66	-6.1%	22.3%	-1.0%	21.70
India	-Nifty	8,368.50	1.0%	31.4%	6.8%	21.89
Philippines	-PCOMP	7,564.50	4.6%	22.8%	1.3%	20.92
Vietnam	-VN	593.05	8.7%	8.1%	22.0%	12.64
US						
US	-Dow	17,619.51	-1.1%	7.5%	26.5%	15.20
	-Nasdaq	4,986.87	5.3%	13.4%	38.3%	30.04
	-S&P	2,063.11	0.2%	11.4%	29.6%	18.21
Europe						
UK	-FTSE	6,520.98	-0.7%	-2.7%	14.4%	20.50
Germany	-DAX	10,944.97	11.6%	2.7%	25.5%	17.67
France	-CAC	4,790.20	12.1%	-0.5%	18.0%	24.72
PIIGS and Hungary						
Portugal	-PSI20	5,551.94	15.7%	-26.8%	16.0%	n.a.
Italy	-FTSEMIB	22,460.71	18.1%	0.2%	16.6%	n.a.
Ireland	-ISEQ	6,165.04	18.0%	15.1%	33.6%	25.79
Greece	-ASE	797.52	-3.5%	-28.9%	28.1%	n.a.
Spain	-IBEX	10,769.50	4.8%	3.7%	21.4%	18.82
Hungary	-BUX	21,903.13	31.7%	-10.4%	2.2%	n.a.
Middle East and North Africa						
Egypt	-EGX30	8,371.53	-6.2%	31.6%	24.2%	17.57
Dubai	-DFMGI	4,086.83	8.3%	12.0%	107.7%	13.13
Other BRIC markets						
Brazil	-IBOV	53,080.88	6.1%	-2.9%	-15.5%	32.60
Russia	-MICEX	1,654.55	18.5%	-7.1%	2.0%	9.88

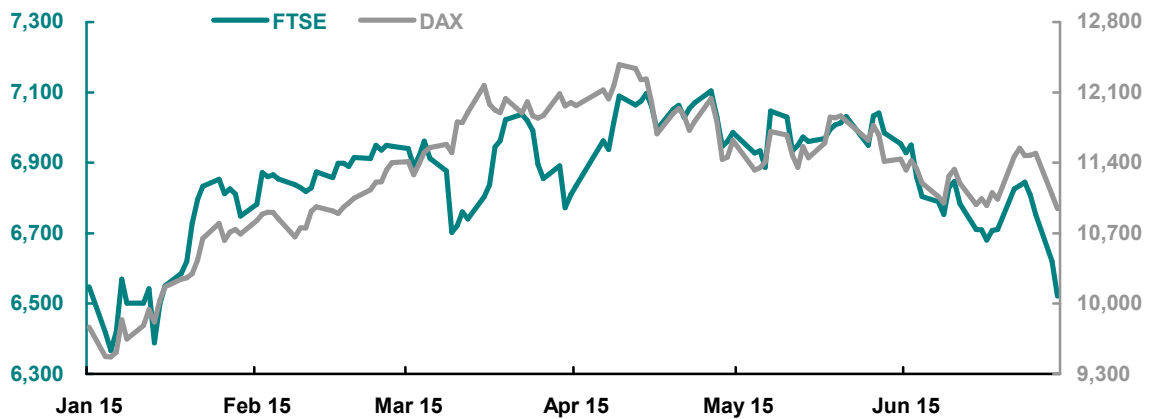
Source: Bloomberg

Europe

- In Europe, market performance was mixed. The FTSE edged lower by 0.7%, whilst the DAX and CAC rose 11.6% and 12.1% respectively. Economic prospects in Europe improved, underpinned by a larger-than-expected stimulus package by the ECB. The ECB kept benchmark rates unchanged and announced plans to purchase securities and sovereign debt of up to €60 billion per month from March 2015 to September 2016. The FTSE and DAX hit record highs.
- Market sentiment was further boosted amid optimism over the economic and earnings outlooks on the back of a weak Euro. The Euro hit a 12-year low against the US dollar. Improving economic data in the region and easing geopolitical tensions between Russia and Ukraine also lent support.



16. However, the markets became volatile later as worries heightened over a possible debt default in Greece. Investors remained cautious that Greece might exit the Eurozone. In late June, the Greek government imposed capital controls and closed banks temporarily to halt deposit withdrawals. Greece delayed a loan repayment to the International Monetary Fund (IMF). Greece's credit rating was downgraded by S&P's, Moody's and Fitch. Major European markets retreated.

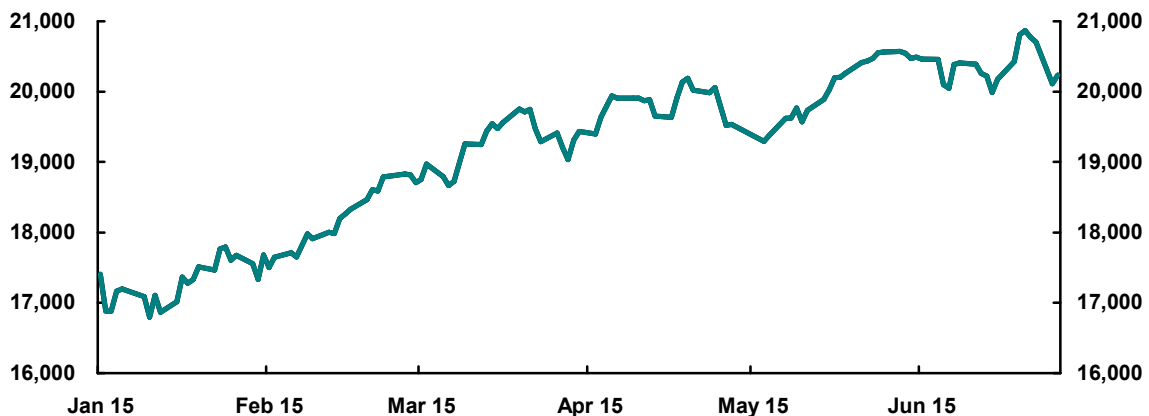


Performance of FTSE and DAX during the first half of 2015

Source: Bloomberg

Asia

17. In Japan, the Nikkei 225 Index extended gains after a 7.1% increase in 2014 and rose 16.0% during the first half of 2015. The market rose steadily amid better prospects of economic growth. The Bank of Japan maintained its accommodative monetary policy. Strong corporate earnings were supported by the depreciation of the Yen, which once slid to a 12-year low against the US dollar. Optimism over funds inflows and higher-than-expected GDP growth in the first quarter also paced gains. The Nikkei broke above the 20,000 level and rose to an 18-year high.
18. The performance of other major regional markets was mixed during the first half of 2015, ranging from a 6.1% loss in Indonesia to an 8.7% gain in Vietnam. The outbreak of Middle East Respiratory Syndrome (MERS) in South Korea seemed to have limited impact on regional markets during the period.



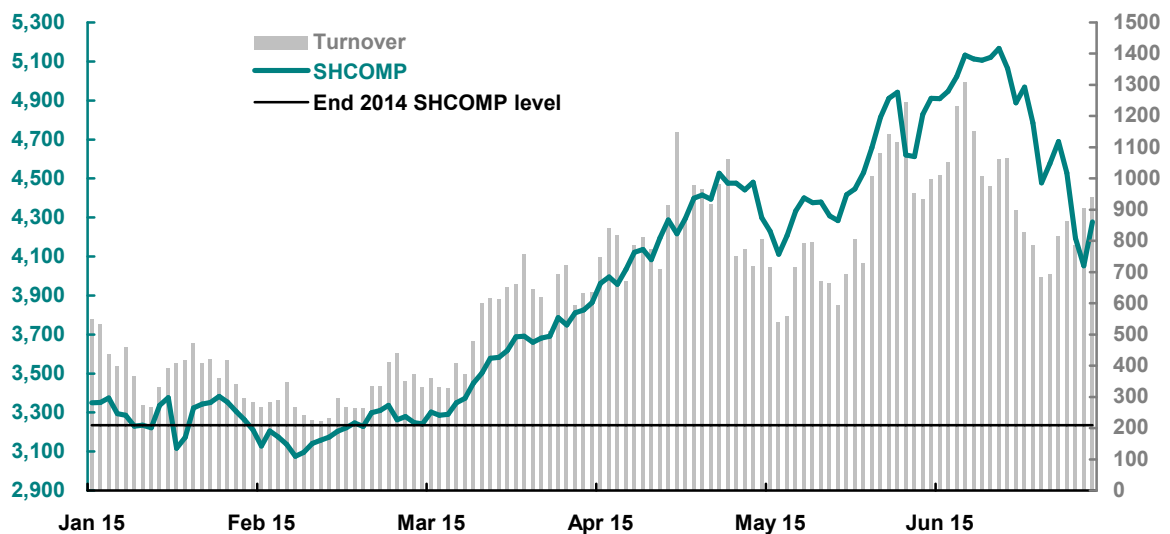
Performance of Nikkei 225 during the first half of 2015

Source: Bloomberg



The Mainland

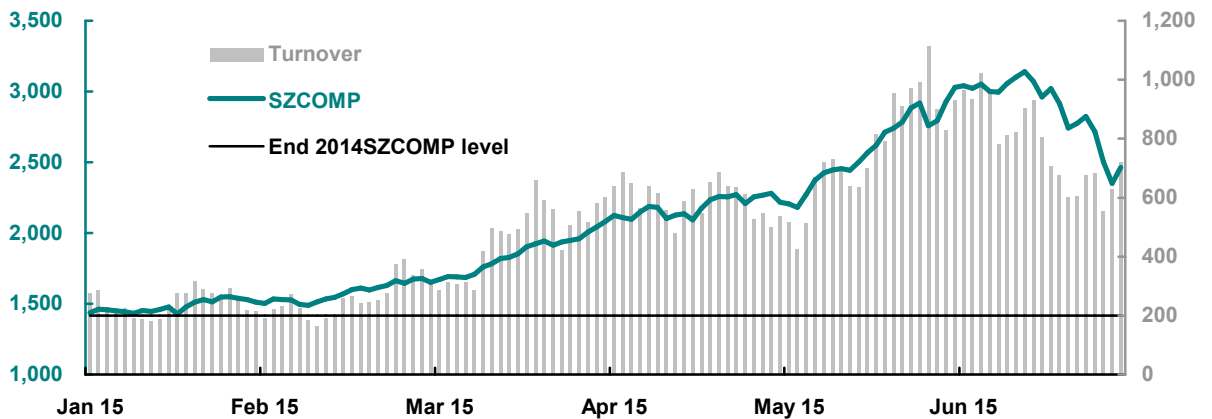
19. After rising 52.9% in 2014, the SHCOMP continued to rise by 32.2% in the first half of 2015, making it one of the best performers worldwide.
20. However, the market was very volatile and investors were sensitive to news about policy changes. Initially, the market gained amid speculation of supportive government measures. During the period, the People's Bank of China (PBoC) cut the reserve requirement ratios three times by a total of 200 basis points (bps) and lowered interest rates three times by a total of 75 bps. While the government cut its growth target to 7%, the lowest in 25 years, optimism about the "One Belt, One Road" initiatives paced gains. Investor sentiment was further boosted by the Mainland-Hong Kong Mutual Recognition of Funds initiative which would allow eligible Mainland and Hong Kong funds to be distributed in each other's market through a streamlined vetting process. Amid bullish sentiment, trading (Shanghai and Shenzhen combined) once rose to a record high of over RMB2.3 trillion on 28 May. In June, SHCOMP broke above the 5,100 level for the first time in seven years. Outstanding margin loans rose to a peak of RMB2.2 trillion.
21. However, the market corrected later amid liquidity concerns ahead of IPOs and worries over the tightening of margin financing and about deleveraging activities. Concerns over a slowdown in economic growth lingered despite market supportive measures. In light of a number of brokerage reports commenting that the valuation of the Mainland market was high and market corrections were possible, investors became concerned that the bull run might come to an end.



**SHCOMP and Shanghai Market Turnover (RMB billion)
during the first half of 2015**

Source: Bloomberg

22. The SZCOMP rose 74.1% in the first half of 2015, after a gain of 33.8% in 2014. The market in Shenzhen outperformed in anticipation of the launch of Shenzhen-Hong Kong Stock Connect. Both the SZCOMP and the ChiNext Price Index rose to record highs. Later, concerns about high valuations and deleveraging erased some gains. In June, market sentiment was affected by news reports of a possible launch of the Strategic Emerging Industries Board in Shanghai to compete with the ChiNext Board.

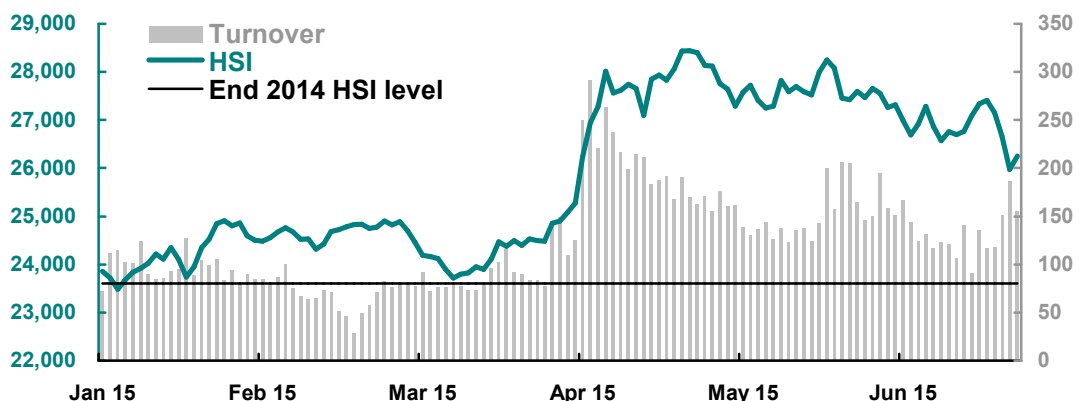


SZCOMP and Shenzhen Market Turnover (RMB billion) during the first half of 2015

Source: Bloomberg

Hong Kong

23. During the first half of 2015, the Hong Kong market rose in tandem with the rally in the Mainland market. The HSI and the HSCEI rose 11.2% and 8.3% respectively after recording gains of 1.3% and 10.8% respectively in 2014. Trading was very active and the market was volatile.
24. In early 2015, uncertainties over an interest rate hike in the US and worries over an economic slowdown in the Mainland weighed on the market. Later, the market rose amid optimism generated by the stimulus measures in the Mainland. Hopes for more capital inflows also paced gains on the news that Mainland mutual funds would be allowed to invest in Hong Kong stocks via Shanghai-Hong Kong Stock Connect. Easing worries of an early rate hike in the US also paced gains.
25. In April, the HSI rose to a seven-year high of over 28,000 points. Market turnover also rose to a fresh high of \$291.5 billion¹ on 9 April.
26. However, the market became more volatile later as worries mounted on the cooling measures in the Mainland market. Uncertainties about the timing of the US interest rate hike and the Greek debt problem paced losses.



HSI and Hong Kong Market Turnover (\$ billion) during the first half of 2015

Source: Bloomberg

¹ Unless otherwise stated, the \$ in this paper denotes the Hong Kong dollar.



Risks and uncertainties facing the Hong Kong market

27. The Hong Kong market's performance will continue to be affected by a combination of risks related to the Mainland and uncertainties in overseas markets. With growing linkage with the Mainland market, the performance of the local market is more susceptible to Mainland risks. Also, changes in overseas market conditions could affect the direction and size of fund flows, potentially adding volatility to the Hong Kong market.
- In the Mainland, in the face of a very volatile market, sentiment has become increasingly fragile. As the market has accumulated substantial gains, valuation concerns began to weigh on the market. The outstanding margin level is high, triggering worries over margin curbs. Deleveraging activities have grown, with investors taking early gains to cut their equities positions. Investors have also become cautious given the uncertain outlook for the economy and concerns that any disappointing data or news about policy changes could trigger sell-offs and market corrections.
 - In the US, the timing and magnitude of the interest rate hike remained uncertain. The expectation is that the rate hike will start in late 2015, depending on the Fed's assessment of the economic situation. The concern is that when this happens, it could trigger capital outflows from regional and emerging markets, adding downward pressure on regional asset markets. Moreover, investor worries over valuations have heightened as equity indices rose to fresh record highs.
 - In Europe, despite the region's improving economic outlook and some progress in Greek debt talks with its creditors, the debt problem in Greece continued to hang over the market. In addition to the lack of clear arrangements and procedures for handling a potential default of Greek bonds or a potential exit of Greece from the Eurozone, political instability in the region and fluctuations in commodity prices also pose risks of much greater volatility ahead for markets.



Major statistics of Hong Kong securities market during the first half of 2015

Trading activity in the local stock market

28. Trading in the local stock market increased. During the first half of 2015, average daily turnover amounted to \$125.3 billion, 65% higher than the \$75.9 billion in the second half of 2014.
29. Mainland stocks remained the most actively traded. Their share of total market turnover was 36% in the first half of 2015 (38% in the second half of 2014), while HSI stocks (excluding H-shares and red chips) accounted for about 12% (16% in the second half of 2014).

Average Daily Turnover (\$ billion)

	1H 2015		2H 2014		1H 2014		% change over	
							2H 2014	1H 2014
HSI (ex H shares & red chips)	15.5	(12%)	12.0	(16%)	12.2	(19%)	29%	27%
Mainland Stocks	45.7	(36%)	28.5	(38%)	22.4	(36%)	60%	104%
<i>H-shares</i>	34.1	(27%)	20.2	(27%)	15.3	(24%)	69%	123%
<i>Red chips</i>	11.6	(9%)	8.3	(11%)	7.1	(11%)	40%	63%
Derivative Warrants	21.6	(17%)	9.8	(13%)	6.7	(11%)	120%	222%
CBBCs	6.7	(5%)	5.4	(7%)	4.6	(7%)	24%	46%
ETFs	10.9	(9%)	6.9	(9%)	2.5	(4%)	58%	336%
Others	24.9	(20%)	13.3	(18%)	14.5	(23%)	87%	72%
Market Total	125.3	(100%)	75.9	(100%)	62.9	(100%)	65%	99%

Remark: Percentages in parenthesis denote market share.

Sources: Hong Kong Exchanges and Clearing Limited (HKEx) and SFC Research

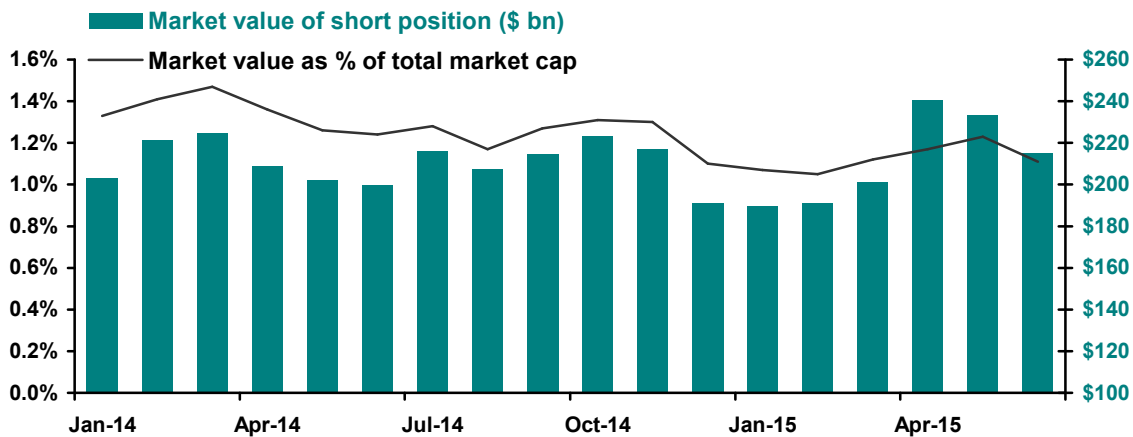
Stock Connect

30. Stock Connect was launched on 17 November 2014 to provide mutual trading access between the Shanghai and Hong Kong stock markets. The Shanghai Stock Exchange and HKEx enable investors to trade eligible shares listed on the other market subject to daily and aggregate quotas.
31. The northbound daily quota is set at RMB13 billion, and the southbound daily quota at RMB10.5 billion. During the first half of 2015, daily quote usage ranged between
- RMB0.04 billion (0.3%) and RMB7.8 billion (60.0%) for northbound; and
 - RMB0.02 billion (0.1%) and RMB10.5 billion (100.0%) for southbound.
32. The northbound aggregate quota is set at RMB300 billion, and the southbound aggregate quota at RMB250 billion. As of 30 June 2015, cumulatively:
- the northbound aggregate quota usage was RMB163.6 billion (54.5%); and
 - the southbound aggregate quota usage was RMB103.6 billion (41.4%).
33. As of 30 June 2015, there were 569 eligible stocks for northbound trading and 286 eligible stocks for southbound trading. During the first half of 2015,
- Northbound average daily trading (counting both buy and sell) was RMB7.4 billion, or 0.6% of the Shanghai market trading; and
 - Southbound average daily trading (counting both buy and sell) was RMB3.5 billion, or 1.8% of the Hong Kong market trading.



Short-selling activity

34. Compared to the second half of 2014, short selling was higher in absolute terms but lower as a percentage of total market turnover. Average daily short selling was \$10.9 billion, or 8.8% of total market turnover in the first half of 2015. In the second half of 2014, average daily short selling was \$7.9 billion, or 10.5% of total market turnover.
35. Based on the data submitted, as at 26 June 2015, aggregated short positions amounted to \$215 billion (or 1.1% of the market cap of the reported stocks).



Sources: HKEx and SFC Research

Initial public offerings

36. There were 45 IPOs in Hong Kong during the first half of 2015. IPO funds raised totaled \$129.4 billion. This compared to 115 IPOs (\$232.5 billion) in 2014. IPO funds raised by Mainland companies accounted for 92% of the market total during the first half of 2015. According to market estimates, Hong Kong ranked first in IPO activities during the first half of 2015.

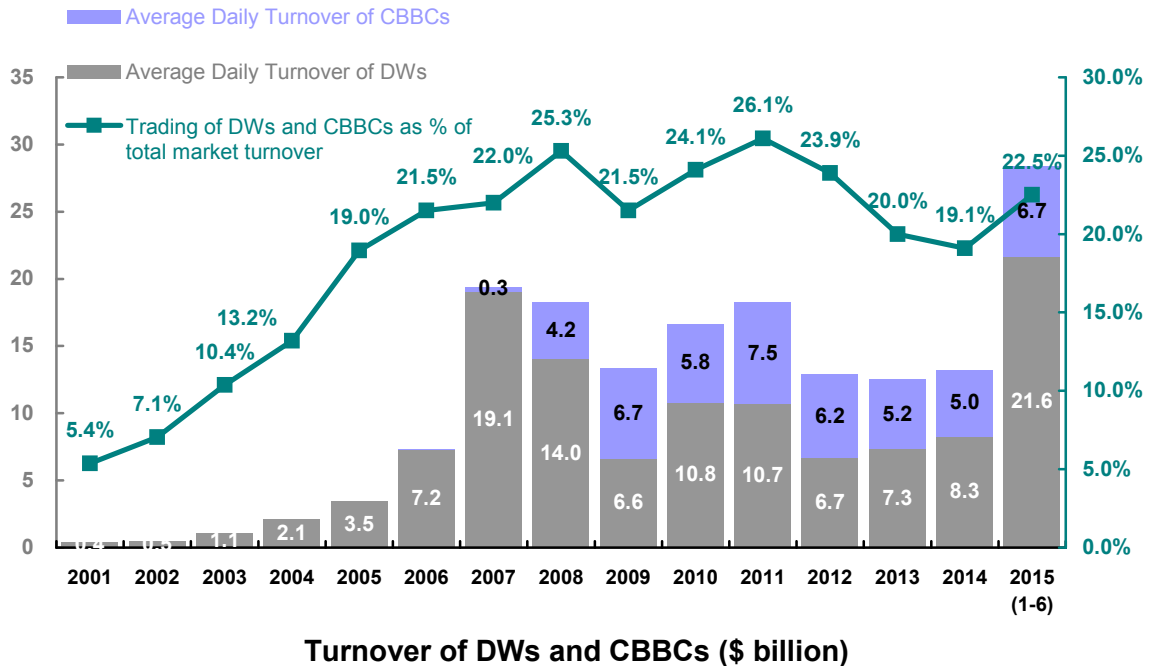
Exchange-traded funds

37. The number of exchange-traded-funds (ETFs) rose to 128 as at end-June 2015 from 122 as at end-2014. Their average daily turnover was \$10.9 billion in the first half of 2015, which was 58% higher than the \$6.9 billion turnover in the second half of 2014. ETFs accounted for 9% of total market turnover in the first half of 2015 (compared to 9% in the second half of 2014). The average daily turnover of A-share ETFs was \$9.1 billion, contributing 83% of total ETF turnover (compared to \$5.5 billion and 80% in the second half of 2014).



Derivatives warrants and callable bull/bear contracts

38. In the first half of 2015, trading of derivatives warrants (DWs) increased in absolute terms and as a percentage of total market turnover. The average daily turnover of DWs rose to \$21.6 billion (17.2% of total market turnover), compared to \$9.8 billion (13.0% of total market turnover) in the second half of 2014.
39. In the first half of 2015, trading in callable bull/bear contracts (CBCBs) increased in absolute terms but decreased as a percentage of total market turnover. The average daily turnover of CBCBs increased to \$6.7 billion (5.3% of total market turnover), compared to \$5.4 billion (7.1% of total market turnover) in the second half of 2014.



Source: SFC Research

Exchange-traded derivatives

40. In the first half of 2015, average daily trading in exchange-traded derivatives increased by 29%, compared to the second half of 2014. Average daily trading in futures products rose 31%. Among futures products, HSI futures and HSCEI futures were the most actively traded contracts, representing about 26% and 47% of all futures trading respectively. The average daily trading volume of HSI futures rose by 4% compared to the second half of 2014, whilst that of HSCEI futures rose by 42%.
41. Average daily trading in options rose by 28% in the first half of 2015. Stock options remained the most actively traded options products and their trading volume rose by 31%, compared to the second half of 2014.



Average daily trading volume of derivatives traded on HKEx by product type (contracts)

		1H 2015	2H 2014	1H 2014
Futures	HSI Futures	72,875	69,884	68,280
	Mini-HSI Futures	36,118	29,964	26,317
	HSCEI Futures	131,474	92,701	85,156
	Mini-HSCEI Futures	32,488	16,443	11,219
	Stock Futures	3,656	1,949	1,505
	3-Month HIBOR Futures	1	0	0
	RMB Currency Futures	766	763	900
	Gold Futures	0	0	0
	Other futures products	1,350	1,040	1,444
	Total Futures	278,728	212,745	194,822
Options	HSI Options	31,398	31,990	28,825
	Mini-HSI Options	4,508	4,192	3,579
	HSCEI Options	50,559	37,538	35,282
	Stock Options	442,928	338,898	263,163
	Other options products	256	155	144
	Total Options	529,649	412,774	330,994
Total Futures and Options		808,377	625,519	525,816

Remark: The average daily trading volume was based on the number of trading days after the product was launched.
Sources: HKEx and SFC Research

After-hours futures trading

42. Trading of HSI and HSCEI futures during the after-hours futures trading (AHFT) session relative to the daytime session remained active during the first half of 2015.
- The average daily trading volume of HSI and HSCEI futures was 11,941 contracts, about 6.2% of the volume during the daytime session (9,344 contracts and 6.1% in the second half of 2014).
 - The average daily volume of mini-HSI futures and mini-HSCEI futures was 6,288 contracts, about 10.0% of the volume during the daytime session (3,886 contracts and 9.1% in the second half of 2014).
 - The average daily volume of RMB currency futures was 79 contracts, about 11.3% of the volume during the daytime session (62 contracts and 8.8% in the second half of 2014).