BACK TO BUSINESS

THE VIEW
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Next stop, dark pools?

Serious work has been done to get the resurrected through train moving but the future may be global trading along with specialised exchanges

Those of us who journeyed on the through train the last time it moved through these parts proved that it is better to travel than to arrive. The excitement generated in 2007 by the thought of direct stock dealing between Hong Kong and Shanghai spread worldwide, causing highly sophisticated foreign investors to buy any stock with the word "China" in it – even Hong Kong stocks such as Hong Kong and China Gas.

Once the global financial crisis came, the air went out of that particular tank engine and nothing was heard for half a decade. The resurrected idea has recently blossomed into the Shanghai-Hong Kong Stock Connect and both stock exchanges and local governments have undertaken some serious work to get the new train moving.

The ironing out of incompatibilities such as merging stock price matching systems, settlement methods and taxation are – in public announcements – moving at full steam and we will be getting the first look at the engine when it comes out of the shed next month.

In the meantime, teenage analysts have been trying to figure out which stocks will benefit and which will not – a somewhat fruitless task if you think that we don't even know what stocks and how many will be involved in the scheme.

Could this be a big benefit to the pools of low-yielding yuan as they could invest in a much wider range of assets? Will Shanghai A shares go up, or will the H shares of dual-listed companies go down? Where will the money flow – could volumes really double on the Hong Kong market, as HSBC analysts think? Will the Shanghai market behave more rationally if the proportion of institutional investors goes up? Naturally, we believe that Shanghai will cloak itself with the characteristics of a better-run Western market.

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How crazy is it to stop trading because the clock hits 4.30?

If it is anything like the last train, we will all be disappointed at the lack of carriages. But let us not pour cold water on the scheme just yet. It is already quite ambitious. Apart from outright mergers, there are very few markets that have engaged in a true cross-listing – and one wonders why not? Stock markets should have been ravaged by technology to become one of the most global industries of all.

Stock exchanges are like airlines – every country wants one. There are 144 stock markets around the world and each of them has a regulator; Canada has 10. Exchanges are fervently regulated by jealous local authorities. On a one-seat, one-vote system, local brokers who control seats on the exchange can hold the big boys to ransom, keeping exchange development in the dark ages, typified by expensive and empty trading floors – the abandoned physical evidence of a dinosaur industry.

The rise of dark pools, or in-bank trading floors, may yet herald global trading of the largest stocks. How crazy is it for us to stop trading HSBC, Google or Deutsche Bank just because the clock hits 4.30 in a certain part of the world? Much better to have one huge market for the big stocks, to trade where we want, when we want.

Voices have been heard suggesting that the Shenzhen Stock Exchange, full of tiny illiquid local stocks, could be caught up in stock connect. If we think big, perhaps we could see a sub-sector of stock exchanges finally specialising to their strengths.

Hong Kong, with its sophistication and experience with global matters, should be a place where global titans like Caterpillar, Daimler, Exxon, Industrial and Commercial Bank of China, JP Morgan, Shell and, ironically, Alibaba, are traded in the Asian time zone. Shanghai would trade major domestic counters or foreign companies with significant activities in China while Shenzhen could act as an incubator, much like the Growth Enterprise Market in Hong Kong.

Perhaps the through train will be a game changer, showing the way to make the exchanges work for the insomniac, liquidity hungry global investor. Or maybe not. Vested interests by the markets and regulators and genuine difficulties in matching systems can instil resistance to change.

But you can't stop progress. Stock exchanges themselves are ripe for involuntary reform by developing technologies. It might be better to change yourself, rather than have change thrust upon you, as was the case with the airlines. That game changer might be the emergence of a powerful dark pool working legitimately with an insightful regulator. They will take global trading in hand for themselves and leave the rest parked in a siding.

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Illustration: Henry Wong