JUNHE BULLETIN

JUNHE

August 1, 2024

Financial

More Convenience for QFI Investments – A Brief Commentary on the New QFI Capital Administrative Provisions

On July 26, 2024, the People's Bank of China (PBOC) and the State Administration of Forex (SAFE) jointly issued the amended *Administrative Provisions on Domestic Securities and Futures Investment Capital of Foreign Institutional Investors* ("New Administrative Provisions"), further facilitating investments in the domestic securities and futures markets by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors (QFIs). The New Administrative Provisions propose measures to simplify business registration, optimize account management, and facilitate QFIs' management of foreign exchange (forex) currency risks through entering into forex derivative transactions.

The existing administrative provisions ("Existing Administrative Provisions"), promulgated on June 6, 2020, implemented the registration-based management of cross-border capital remittance and exchange by QFIs, removed quota restrictions, and allowed QFIs to repatriate capital upon the submission of a written tax clearance commitment. QFIs would hope that the Existing Administrative Provisions will be further improved to offer more convenience for their investments. The New Administrative Provisions respond to the needs of QFIs by making certain improvements and enhancements in the following aspects:

I. **Simplifies business registration and optimizes account management.** The New Administrative Provisions stipulate that QFI business registrations will now be handled by the main reporting bank (i.e., the main custodian) through SAFE's digital forex management platform (ASOne), which is more convenient than at present. QFIs can combine RMB special deposit accounts for securities trading and derivative transactions, reducing the number of new accounts required to be opened, and QFIs engaged in forex derivative trading can use their existing dedicated RMB accounts, without the need to open new ones.

II. **Further relaxes the choice of currencies for remittance and repatriation.** Under the Existing Administrative Provisions, QFIs can freely choose the currency for inward remittance. According to the New Administrative Provisions, if foreign currencies are remitted for investment, the repatriation of the investment principal and proceeds can be in foreign currencies or RMB; if RMB is remitted for investment, the repatriation of the investment principal and the proceeds shall be in RMB.

III. Allows two-way transfers between QFI accounts and CIBM direct investment accounts. The New Administrative Provisions clarify that capital in QFI dedicated accounts that are in the same name, and capital in China interbank bond market (CIBM) investment dedicated capital accounts in the same name, can be transferred two-way, according to the domestic investment needs of the same foreign institutional investor.

IV. Aligns the forex hedging model of QFIs with the CIBM Direct Access. Firstly, the New Administrative Provisions allow QFIs to conduct spot forex settlement and sales as well as forex derivative transactions through qualified domestic financial institutions other than their custodian banks. Same as the policy of CIBM Direct Access, QFIs can choose to transact directly with their custodian banks or other domestic financial institutions as such financial institutions' clients, giving QFIs more market-based options and more advantageous quotes. Alternatively, QFIs can trade in the China Inter-bank Forex Market (CIFXM) by engaging prime brokerage services and becoming a member of the China Forex Trade System (CFETS). Bank-type QFIs can also trade directly in the CIFXM after becoming a member of the CFETS. If a QFI chooses to transact directly with its custodian bank or other domestic financial institution as its client, the QFI should register the names of such financial institutions with CFETS on its own or through its custodian bank.

Secondly, QFIs conducting domestic RMB/forex derivative transactions should still abide by the principle of genuine need and hedging and ensure its exposure to forex derivatives reasonably correlates with its forex risk exposure, which refers to the scale of RMB assets corresponding to its domestic securities and futures investments. When changes in securities and futures investments lead to changes in forex risk exposure, QFIs should promptly adjust the corresponding exposure of forex derivatives. The Existing Administrative Provisions require monthly adjustments of forex derivative positions, meaning that QFIs must, within five working days of the beginning of each calendar month, adjust their forex derivative positions based on the latest scale of RMB assets corresponding to their domestic securities investments at the end of the previous month, so as to comply with the principle of genuine need. The New Administrative Provisions remove these requirements, meaning that QFIs can adjust their derivative exposure at any time in response to changes in the forex risk exposure, corresponding to changes in the scale of the RMB assets and thereby locking in exchange rate risks.

Our Observations

The New Administrative Provisions will take effect on August 26, 2024. We anticipate that many QFIs will actively consider and conclude their forex derivative transactions to manage the forex currency risks. We are confident that the Chinese regulatory authorities will continue to expand the so-called rule-based opening-up of the financial sector, optimize QFIs systems and provide more convenience for QFIs to invest in China's capital market.

We will continue to monitor the situation and keep our clients apprised of any important developments.

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