Foreign Share Discount on the Chinese Stock Market: Evidence for A- and H-share markets

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Abstract

This paper examines the foreign share discount between A- and H-shares before and after the Chinese switch to a floating exchange rate regime in July 2005. Using intraday data (during the two hours of joint opening of the two exchanges) of 26 Chinese dual-listed firms on the A- and H-share markets from 2004 to 2006 for a sample, we find that large H-share discount was present before as well as after the Chinese exchange rate regime reform. The H-share discount decreased substantially and significantly during the managed floating exchange rate regime. Our cross-sectional and panel data analysis find that, in the pre-reform, the H-share discount is related to A-share intraday volatility, expected exchange rate change, index discount, which is consistent with different stock risk, expected exchange change rate change and stock market hypotheses. In the post-reform, we consider that none of the six traditional hypotheses can explain H-share discount. We suggest another explanation based on the split share reform, may as a solution to the H-share discount puzzle.

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