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The Development of China's Stock Market under the Background of the Registration-Based System

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Abstract

Reviewing China's stock issuance system, from the approval system to the verification system, then to the pilot registration system, and finally to the full implementation of the registration system, China's stock market has also matured from its initial stages. The reform of the registration system will have multiple positive impacts on China's stock market, the most obvious manifestation being that each registration system reform will drive a wave of market index increases in the related markets. The registration system further relaxes the conditions for new stock issuance, accelerates the speed of corporate listing and financing, helps to increase the proportion of direct financing, and brings the Chinese market closer to mature markets. This article analyzes the impact of the registration system on listings, from the pilot programs in the Sci-Tech Innovation Board (STAR Market) and the Growth Enterprise Market (GEM) to the full implementation in the main board, the number of listed companies has increased, the total market value has grown, the stock market scale has expanded, and market volatility has increased. Then, it expands from three small aspects, the market style will shift to rationality and value orientation, while accelerating the transformation of the domestic stock market from a speculative market to an investment market.

Keywords

Registration System; Stock Market; Sci-Tech Innovation Board (STAR Market); Growth Enterprise Market (GEM); Main Board.

1. Introduction

In recent years, driven by the reform of the registration-based system, China's stock market has ushered in significant opportunities for transformation and development. The implementation of the registration-based system marks a profound shift in China's capital market from an approval-based system towards market-oriented and rule-of-law principles, aiming to enhance market efficiency, optimize resource allocation, and improve market transparency. Compared to the approval-based system, the registration-based system places greater emphasis on the authenticity and completeness of information disclosure, reduces administrative intervention, provides more convenient financing channels for enterprises, and creates a fairer market environment for investors.

Of course, this reform has also brought new challenges, such as increased market volatility. However, this paper primarily analyzes the positive impacts of the registration-based system on the development of China's stock market.

2. The Evolution of the Issuance System

To date, China's new stock issuance system has undergone several changes, mainly experiencing three stages: the first is the approval system stage, the second is the verification and inquiry system stage, and the third is the transition stage from the verification system to

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the full registration system. The primary condition for a company to issue stocks is to obtain indicators and quotas. The approval system was implemented starting in 1990, but at that time, the approval authority for new stock issuance and listing belonged to different government departments. It was not until April 1993 when the State Council issued the "Interim Regulations on the Administration of Stock Issuance and Trading" that the China Securities Regulatory Commission (CSRC), established in 1992, was designated to uniformly approve stock issuance[1].

The approval system includes two stages. The first is the quota management stage from 1990 to 1995, where quota indicators were assigned to provincial governments or industry authorities, who recommended enterprises within the quota limits, and then the CSRC uniformly approved the issuance of stocks by enterprises. The second is the indicator management stage from 1996 to 2000.

The verification system can also be divided into two stages, namely the "channel system stage" and the "sponsorship system stage". From 2001 to 2004 was the channel system stage under the verification system. In February 2004, the sponsorship system began to be implemented. After the implementation of the sponsorship system, the channel system was not immediately abolished. In the initial period, securities firms still needed to submit enterprises according to the channels until it was abolished on December 31, 2004. Under the sponsorship system, enterprises must have a sponsor institution to sponsor their issuance and listing, and must have practitioners with sponsor representative qualifications specifically responsible for the sponsorship work. With the continuous deepening of reforms and market development, the shortcomings of the original issuance system gradually became apparent, and it was necessary to truly hand over the choice to the market.

Therefore, in November 2018, the Chinese government announced the establishment of the Sci-Tech Innovation Board (STAR Market) at the Shanghai Stock Exchange and the pilot registration system. The prelude to China's pilot registration system was thus opened, and then it was promoted, reformed, and piloted in other sectors. The CSRC adopted a reform path of pilot first, incremental then stock, and gradual expansion, successively piloting the registration system in the STAR Market, GEM, and Beijing Stock Exchange, promoting a package of reforms, and opening a new situation for the reform and development of the capital market. In July 2019, the first batch of STAR Market companies were listed and traded. In August 2020, the reform of the GEM and the pilot registration system officially landed at the Shenzhen Stock Exchange. In November 2021, the Beijing Stock Exchange was inaugurated and opened for business, simultaneously piloting the registration system, and finally in February 2023, the full implementation of the registration system was achieved.

From the development process, it can be seen that China's issuance system is divided into the approval system, verification system, and registration system. Simply put, the approval system was used in the early stages of China's stock market development to maintain the stability of listed companies and balance complex socio-economic relations, using administrative and planned methods to allocate stock issuance indicators and quotas, with local governments or industry authorities recommending enterprises to issue stocks according to the indicators, which is a non-market-oriented issuance system. The verification system is an intermediate form of semi-market-oriented issuance system between the registration system and the approval system. On the one hand, it cancels the government's indicator and quota management and introduces the responsibility of securities intermediaries to judge whether enterprises meet the conditions for stock issuance; on the other hand, securities regulatory agencies simultaneously conduct substantive reviews of the compliance and marketability conditions of stock issuance and have the right to reject stock issuance applications. The verification system is currently the longest-implemented issuance system in China, but due to the CSRC's review of enterprises for issuance and listing, it objectively forms a government

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endorsement of the asset quality and investment value of new stock issuers, which is not conducive to investors forming a risk-bearing investment awareness, and will also weaken the performance responsibilities of issuers and intermediaries, which is not conducive to the cultivation and formation of market self-discipline mechanisms, and is not conducive to fully exerting the decisive role of the market in resource allocation.

Finally, due to the development of China's stock market and the defects of the previous system, the registration system has been piloted and implemented. It refers to the requirement that when an issuer applies to issue stocks, it must legally and accurately report various public materials to the securities regulatory agency. The responsibility of the securities regulatory agency is to conduct a formal review of the completeness, accuracy, truthfulness, and timeliness of the reported documents, and not to conduct a substantive review and value judgment of the issuer's qualifications, leaving the quality of the issuing company's stocks to be decided by the market[2].

3. The Impact of the Registration System on the Three Major Sectors of China's Stock Market

Since 2018, the registration system has been smoothly implemented in the STAR Market and GEM, significantly optimizing the conditions for issuance and listing. The registration system only retains the necessary qualification and compliance conditions for enterprises to publicly issue stocks, and converts the substantive thresholds under the verification system into information disclosure requirements as much as possible. Regulatory authorities no longer make judgments on the investment value of enterprises. After the full implementation of the registration system in 2023, the number of listed companies will show explosive growth, analyzed from three aspects: the STAR Market, GEM, and the main board.

In terms of the STAR Market, on December 28, 2022, with the listing of Yingshi Network and Qingyue Technology, the number of STAR Market listed companies will reach 500. Starting from the first batch of 25 listed companies in 2019, the STAR Market has walked a development path from nothing to something, from small to large, and from weak to strong in more than three years: IPO financing scale is nearly 760 billion yuan, refinancing scale exceeds 100 billion yuan, total market value is about 6 trillion yuan, and 7 companies have a total market value of over 100 billion yuan; six major strategic industrial clusters are developing, with national-level "specialized and sophisticated" small giants accounting for nearly half, and the three-year compound growth rate of operating income and net profit attributable to the parent company of listed companies reaching 25% and 63%. Standing at the new starting point of "500", the STAR Market will adhere to the positioning of "hard technology" and continue to play the spirit of the system reform "experimental field". In the future, more technology innovation enterprises are expected to obtain sustainable development momentum through the STAR Market. Currently, 7 STAR Market companies have a market value of over 100 billion yuan, 15 companies have a market value of over 50 billion yuan, and 47 companies have a market value of over 30 billion yuan, with industry benchmark enterprises emerging one after another. In terms of industry, the leading industrial cluster development trend of the STAR Market is becoming more and more obvious. In the field of integrated circuits, the total number of STAR Market companies has grown from 5 at the beginning of the market to 84. In the field of biomedicine, 107 enterprises have been listed, covering major categories such as innovative drugs, generic drugs, medical devices, and CRO. In the field of new energy, "wind, light, electricity, and storage" are gathered, covering 24 listed companies, developing synergistically. In the field of software, 50 companies have been listed, extending from basic software to CDA, EDA, network security, and artificial intelligence, the main links of the digital industry[3].

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In terms of the GEM, compared with the main board market, the listing requirements are often more relaxed, mainly reflected in the requirements for establishment time, capital scale, and medium- and long-term performance. Focus on two types of enterprises, one is biomedicine, new energy, electronic information, environmental protection and energy-saving enterprises, and the other is enterprises with innovative capabilities and high market share in technical business forms. The biggest feature of the GEM market is low threshold entry and strict operation requirements, which helps potential small and medium-sized enterprises obtain financing opportunities. In October 2009, the GEM was officially launched, and the first batch of 28 GEM companies were listed on the Shenzhen Stock Exchange. By May 12, 2023, there were 1258 companies, nearly 14 years of effort, from ten digits to thousands. The figure below captures some data from 2015 to 2023, and it can be clearly seen that from 2015 to May 12, 2023, the number of GEM listed companies increased from 492 to 1258, an increase of nearly 155.7%. In 2020, the GEM ushered in reform and pilot, and the GEM in the era of the registration system, with a more inclusive and open attitude, accepted growth-oriented innovation and entrepreneurship enterprises. As of August 23, 2022, if two years are converted into "increment", since the implementation of the registration system reform, the GEM has cumulatively added 355 listed companies, with nearly 330 billion yuan of IPO funds nourishing the "new seedlings" of the capital market; if converted into "stock", in the past two years, the Shenzhen Stock Exchange has accepted 525 refinancing applications from GEM companies, 319 have been implemented and completed, and 339.4 billion yuan of refinancing funds have helped enterprises to upgrade again. The combination of increment and stock outlines the full picture of the effectiveness of the GEM registration system reform. As of now, the number of GEM listed companies has reached 1175, with a total market value of over 12 trillion yuan, gathering nine strategic emerging industries, with a combined market value accounting for as high as 73%, cultivating 13 companies with a market value of over 100 billion yuan, and emerging a number of influential and innovative leading enterprises such as CATL, Mindray Medical, Zhifei Biological, and Inovance Technology. In addition, the GEM actively serves the three major fields of advanced manufacturing, digital economy, and green low-carbon, and related new energy, biomedicine, new materials, high-end equipment manufacturing industries, and new generation information technology companies have formed cluster development advantages.

In terms of the main board, as the core market of China's stock market, after the implementation of the registration system, the requirements highlight the characteristics of "large blue chips". Main board enterprises are generally large-scale, stable, and mature enterprises with stable profitability. On April 10, 2023, the situation of 10 enterprises listed on the Shanghai and Shenzhen main boards, according to data, the issuance prices of 10 main board registration system new stock enterprises are concentrated between 10 yuan/share and 20 yuan/share, with the highest value being Haisun Pharmaceutical (44.48 yuan/share) and the lowest value being CITIC Metal (6.58 yuan/share). The issuance price-to-earnings ratio of 10 IPO enterprises is mostly between 20 times and 40 times, with a median of 34.75 times; the median ratio to the industry price-to-earnings ratio is 1.95 times. The actual raised funds of 8 enterprises exceeded the expected raised funds, and conversely, the actual raised funds of two enterprises were less than expected, among which CITIC Metal raised 805 million yuan less than expected, and Nanfang Mining Group raised 440 million yuan less than expected. In addition, the first batch of 10 new stocks of the main board registration system were collectively opened high on the first day of listing, and most of them have triggered a temporary suspension. Under the verification system model, the market information asymmetry is relatively serious, and the weight of market pricing is relatively low, resulting in the issuance price being underestimated, and there may be a large difference between the issuance price and the market trading price on the first day of issuance, which will achieve a higher increase. However, after the implementation of the registration system, although the short-term stock market cannot be

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estimated, in the long run, because the listing process becomes more transparent and the results are more predictable, the degree of information asymmetry will decrease, which will help the IPO (new stock issuance) price better reflect the fundamentals of the enterprise. If the valuation is reasonable, it may reduce the enthusiasm for "new stock speculation"[4]. For IPO enterprises, this is undoubtedly good news. Since the valuation of the primary market and the secondary market will be more reasonable in the future, it is beneficial to improve the efficiency of the capital market, guide resource allocation, and play the price discovery function. From the perspective of the domestic market, this reform will improve the listing efficiency of main board large blue chip enterprises, increase the supply of large blue chip enterprises, improve the quality of listed companies, and thus introduce more medium- and long-term funds. In addition, the multi-level capital market system will be clearer and more in line with international financial markets.

4. Improving the Efficiency of Economic Resource Allocation

Although the substantive review of the previous verification system will filter out some inferior enterprises, for high-tech start-ups and unicorn enterprises with high growth and high investment value, it is difficult to generate profits during the R&D period, and most of them adopt a light asset operation mode, making it difficult to pass the listing review; for small and medium-sized enterprises and start-ups in emerging industries, it is very difficult to directly finance through the stock market; in addition, there are some "zombie enterprises", that is, enterprises that rely on subsidized loans to survive, or have poor performance and face continuous losses, technical bankruptcy, or potential risks such as delisting, can still obtain financing by issuing stocks. The pilot and implementation of the registration system are conducive to clarifying the boundary between the invisible hand and the visible hand, and at the same time simplifying the listing process, leaving the substantive review of listed companies to the market, reducing the government's direct allocation of resources[5]. Promote the allocation of resources according to market rules, market prices, and market competition to achieve maximum benefits and optimal efficiency. Most directly, those "zombie enterprises" and "shell companies" will lose the value of the "listing channel" under the comprehensive registration system, and lose the ability to compete for resources with high-quality companies. Small and medium-sized enterprises will also find it easier to obtain financing through the stock market than before. However, this move will intensify the concentration of resources to the industry head, and the registration system will leave the substantive review to the market, which may intensify the Matthew effect. Leading securities firms have greater advantages in inquiry and pricing capabilities, customer resources, etc., and the issuance duration, fundraising scale, and industry reputation form a positive cycle, which is expected to further promote the concentration of high-quality projects to the industry head, and enhance the stability and certainty of the performance growth of industry leaders.

5. Purifying the Capital Market

The regulatory characteristics of the US market are the emphasis on information disclosure and the implementation of a strict delisting system. In terms of issuance and listing regulations, the US separates issuance regulation and listing regulation. In terms of issuance, the Securities and Exchange Commission conducts a formal review of the issuance application documents and makes a decision on whether to approve the issuance. In terms of listing, the exchange makes a judgment on the market value of the issuer, including substantive elements such as profitability and development prospects. In terms of delisting, the US implements a strict delisting system, and capital market companies present a "big in and big out" operation mode. Although the delisting standards of various exchanges in the US are different, they basically have fixed

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standards for various data such as shareholder equity, market value, total assets, net profit, stock price, and the number of publicly held shares of listed companies. Once the company data does not meet the standards, it will face the risk of forced delisting.

Hong Kong, China implements a "dual filing system", which has strong colors of both the verification system and the registration system. The issuance review must be completed by the Hong Kong Securities and Futures Commission and the Hong Kong Stock Exchange, and two sets of repeated reviews are required. The Stock Exchange conducts a substantive review of the issuer, while the Securities and Futures Commission is responsible for the formal review. The Securities and Futures Commission has the power to veto the listing, while the Stock Exchange has the power to approve. This review method ensures both the transparency and marketization of the listing process and the quality of listed companies. In terms of delisting, the Hong Kong Stock Exchange adopts non-quantitative delisting standards and does not judge whether a company should be delisted through quantitative performance, which also leads to the phenomenon of "penny stocks" in the Hong Kong stock market.

In 2020, the most stringent delisting new regulations in the history of the A-share market were implemented, and the situations that trigger delisting of listed companies are more diversified. For example, the new regulations add that the annual report of a company under delisting risk warning is issued with a reserved opinion, an unqualified opinion, or a negative opinion, and the audit opinion is also cross-applied with financial indicators. "Difficulty in delisting" has long been a chronic disease of the A-share market. Since the pilot of the registration system, the A-share market has significantly increased the delisting efforts by establishing a normalized delisting mechanism, simplifying delisting procedures, and improving delisting standards. 2022 is considered a critical year for the implementation of the new delisting regulations. Taking the Shenzhen Stock Exchange as an example, a total of 24 companies were delisted in the Shenzhen market throughout the year, close to the sum of the past three years. Among the 24 companies, 2 were voluntarily delisted, and 22 were forced to delist.

By 2023, the diversified delisting system has demonstrated its power, and the survival of the fittest mechanism has become more stable; at the same time, the A-share market has fully implemented the registration system. In this context, the normalized delisting mechanism continues to exert its power and is accelerating the purification of the market ecology. Under the background of the comprehensive registration system, the future market reshuffle will be accelerated, and the capital market will pay more attention to liquidity performance. The possible result is that the future market liquidity will further gather to leading enterprises or scarce assets, but for ordinary enterprises, they may face risks such as insufficient liquidity. That is to say, the future market liquidity differentiation will be more obvious, the number of low-priced stocks may increase, and more and more stocks will fall below the face value of 1 yuan, and face value delisting will become more common.

6. Changing Investment Philosophy

First, under the registration system, investors will pay more attention to the research of fundamentals rather than speculation on companies, and investors' investment behavior will also be more rational than before. The service function of the capital market to the real economy, especially technological innovation, has been greatly improved, the market structure and market ecology have undergone profound changes, the market vitality and market resilience have been significantly enhanced, and all parties in the market have brought a real sense of gain. Investors should pay attention to the comparison with the STAR Market and GEM. The issuance and listing review mechanism of the comprehensive registration system is similar to the existing STAR Market and GEM, maintaining the review and registration architecture of the exchange review and the CSRC registration; at the same time, further improving the main board

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trading system: (1) No price limit for the first 5 trading days of new stock listing; (2) Optimizing the intraday temporary suspension system; (3) New stocks can be included in the margin trading and securities lending targets on the first day of listing, optimizing the securities lending mechanism, and expanding the scope of securities lending sources. However, this reform did not liberalize the 10% price limit of the main board, maintaining the existing investor suitability requirements.

Second, the structure of listed companies, the structure of investors, and the valuation system have undergone positive changes. The proportion of technology companies and the proportion of professional institutional transactions have increased significantly. The pricing of new stock issuance and the valuation of the secondary market have shown a trend of high quality and high price. From the perspective of investor structure, the comprehensive registration system will amplify the disadvantages of individual investors in investment research capabilities and risk-bearing capabilities. On the one hand, the comprehensive registration system will further improve the requirements for individual investors' ability to identify individual stocks, and value investment will become the mainstream. Institutional investors are expected to give full play to their professional risk control capabilities and profound investment research capabilities, and achieve continuous profitability in the investment process. On the other hand, individual investors have limited capital strength, and under the trend of normalized delisting mechanisms and the polarization of individual stock trends, they are more likely to suffer losses beyond their risk-bearing capacity. Referring to international experience, the US experienced a three-year bear market before the implementation of the registration system. After the implementation of the registration system in 1933, it gradually changed, experienced the "crazy bull" market from 1933 to 1937, and although it experienced a "slow bear" trend from 1937 to 1942, in the end, the US stock market experienced a "slow bull" market with a hundred-fold increase.

Finally, due to the increase in the number of stocks, the cost of individual stock research and the difficulty of selection for individual investors have increased, and more time and energy are needed to judge the investment value of listed companies, that is, the difficulty of retail investment may increase, and the institutionalization process of secondary market investment will accelerate. Therefore, the value of professionalism is more prominent, and fund investment that practices long-term value investment philosophy is more suitable for individual investors, and choosing to hold the funds they are optimistic about is sufficient. However, after the full implementation of the registration system, there is still a lack of perfect supporting systems, and it is urgent to pay attention to the protection of investors.

7. Epilogue and Outlook

The full implementation of the registration system is a well-established reform. After the pilot in the STAR Market, GEM, and Beijing Stock Exchange, the registration system has been steadily promoted to the entire market. This reform, which affects the whole body, is expected to bring about a comprehensive and profound change in the capital market: the issuance and listing conditions are more inclusive, and the review is more efficient; the market mechanism of survival of the fittest is more perfect; the role of intermediaries as "gatekeepers" is further strengthened; investors are more professional and institutionalized; market order continues to improve, the ecology is continuously optimized, and the stable development of the market will usher in a new pattern.

At present, all parties in the market have not fully adapted to the comprehensive registration system from concept to ability, and are still in the running-in period. In terms of information disclosure, it is not enough to just fully disclose information in form. We always emphasize the truthfulness, accuracy, and completeness of information disclosure, and strictly control the

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quality of information disclosure in the review. At the same time, we also need to consider the positioning of the sector, whether it complies with industrial policies, etc. At present, the investor structure of China's stock market has shown marginal improvement, but the proportion of institutional investors still lags behind that of developed countries. In short, the comprehensive registration system is of milestone significance to the development of China's capital market, and it is a reform that touches the soul of the capital market system. Of course, the full implementation of the registration system is not the end of the development of China's stock market, and the comprehensive development of the stock market is always on the road.

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