

Business / Banking & Finance

China closes another offshore investing loophole as TRS faces restrictions

Brokerages told to halt expansion of offshore-linked TRS portfolios as Beijing tightens oversight of cross-border investing channels.

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Futu Holdings was among the offshore brokerages ordered by Chinese regulators in late May to stop mainland residents from opening new accounts to trade foreign securities directly. Photo: Sam Tsang

Chinese regulators have tightened one of the remaining channels for gaining exposure to overseas assets through derivatives, the latest sign that authorities are continuing efforts to close regulatory loopholes and curb domestic investors' access to higher-risk offshore markets.

Rather than launching another high-profile crackdown like last month's action against unlicensed offshore brokers, including Futu and Tiger Brokers, regulators have instead targeted total return swaps (TRS) through so-called "window guidance" – verbal instructions conveyed to domestic brokerages on Tuesday evening, according to people familiar with the matter.

Brokerages, which often work with private funds to provide such products, were instructed to suspend any expansion of offshore-related portfolios, including new TRS contracts and increases in the size of existing mandates, one person said.

Existing portfolios linked to offshore assets are not subject to immediate liquidation.

"The move is a direct response to the massive inflow of high-net-worth capital into surging global technology stocks, including US, Japanese and South Korean equities," the person said.

A TRS is a derivative contract in which one party receives a fixed or floating payment stream, while the other receives the total return of a reference asset, such as an equity index, a basket of shares, loans or bonds.

Because the structure does not involve the direct transfer of capital across borders, TRS has become an increasingly popular route for mainland investors seeking exposure to overseas assets as other investment channels have narrowed, analysts said.



The latest restrictions on total return swaps signal Beijing's continued efforts to tighten control over cross-border investment channels. Photo: Reuters

TRS has remained one of the few channels available for mainland investors to access overseas stocks and bonds since the China Securities Regulatory Commission in late May ordered cross-border fintech brokers such as Futu Holdings and Tiger Brokers to stop mainland residents from opening new accounts to trade foreign securities directly.

Mainland investors can also access overseas markets through programmes such as Stock Connect and Wealth Management Connect with Hong Kong, but these schemes typically have higher eligibility requirements and investment thresholds.

At the same time, Hong Kong financial institutions have strengthened compliance checks on mainland clients seeking to open investment accounts in the city.

Investors can also gain exposure through exchange-traded funds tracking popular overseas sectors, including US artificial intelligence stocks, under the Qualified Domestic Institutional Investor (QDII) scheme. However, such products are often constrained by quota limits and strong demand.

"TRS is a popular derivative mechanism that allows mainland private funds to gain exposure to overseas assets through swap agreements with local brokerages," the person said.

"Alternative channels such as QDII and QDLP [Qualified Domestic Limited Partner] programmes cannot match the level of customisation and flexibility offered by TRS."

The move comes at a time of heightened volatility in overseas markets. South Korea's benchmark stock index fell sharply on Tuesday, while concerns about AI valuations and broader macroeconomic risks have triggered selling across several developed-market technology sectors.

Mofiz Chan, chairman of the Hong Kong Securities & Futures Professionals Association, said it was difficult to predict when the restrictions might be eased, but he expected regulators could eventually relax the measures once speculative activity in overseas markets subsides or more detailed regulatory guidance is introduced.