

Market Summaries

People's Republic of China

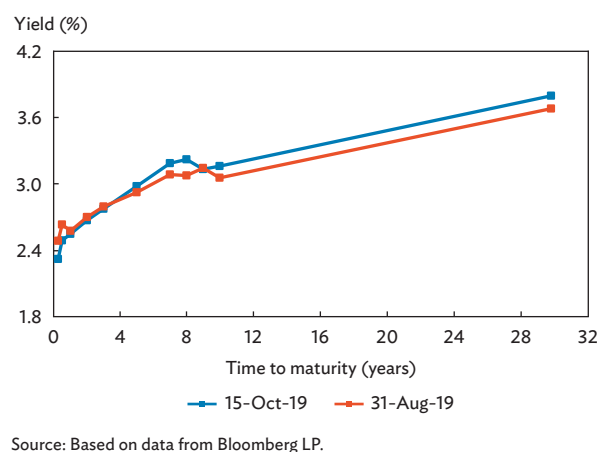
Yield Movements

The People's Republic of China's (PRC) yield curve for local currency (LCY) bonds steepened between 31 August and 15 October, driven by a rise in yields at the longer end of the curve and a decline in yields for shorter-dated tenors (**Figure 1**). Yields rose for tenors of 5 years or longer by an average of 10 basis points (bps), excluding the 9-year tenor, which fell 1 bps. For tenors of 3 years or shorter, yields fell an average of 8 bps. The steepening of the yield curve led to a rise in the 2-year versus 10-year spread to 49 bps on 15 October from 35 bps in 31 August.

Yields at the longer end of the curve rose on investor optimism that the PRC's economy would benefit from news that trade tensions between the PRC and the United States (US) were abating. On 4 September, it was announced that trade talks between the PRC and the US had resumed. Following the announcement, the prospects of a trade deal progressed. On 11 September, the PRC announced an exemption of some US products from tariffs for 1 year, while the US reciprocated with a delay of scheduled tariffs from 1 October to 15 October. On 11 October, the US announced a tentative agreement as the first phase of a potentially larger settlement. The US suspended tariffs scheduled set for 15 October, while the PRC agreed to purchase USD50 billion worth of US goods.

The news of softening trade tensions between the two economies provided a boost to longer-term yields on hopes that the PRC's economic growth would improve. Gross domestic product growth in the PRC slowed to 6.0% year-on-year (y-o-y) in the third quarter (Q3) of 2019 from 6.2% y-o-y in Q2 2019. While industrial production growth recovered somewhat in September to 5.8% y-o-y from 4.4% y-o-y in August, the overall growth trend in industrial production remains headed in a downward direction. In September, the PRC's y-o-y export growth fell to -3.2% from -1.0% y-o-y in August. For the first 9 months of the year, export growth fluctuated, but export growth was negative in 5 of those months.

Figure 1: The People's Republic of China's Benchmark Yield Curve—Local Currency Government Bonds



Outside of the trade news, yields rose amid the reluctance of the People's Bank of China (PBOC) to engage in aggressive broad-based easing. On 6 September, the PBOC announced a 50 bps reserve requirement ratio cut, with an additional 100 bps cut for smaller banks. The PBOC said that the 50 bps cut was mostly to help liquidity in anticipation of corporate tax payments during the month as opposed to a shift in monetary policy. In addition, the PBOC also reduced the 1-year loan prime rate, a new benchmark interest rate, by 5 bps to 4.20% on 20 September and left the 5-year rate unchanged.

Inflation also remains a concern in the PRC as it has been trending upward. The rise in inflation has been solely due to a supply shock as pork prices have risen due to the impact of swine flu. Consumer price inflation in the PRC rose to 3.0% y-o-y in September from 2.8% y-o-y in August, with food prices rising 8.4% y-o-y during the month.

Yields at the shorter end of the curve fell during the review period as the PBOC sought to stabilize liquidity amid investor concerns following a government takeover of a bank as well as corporate tax payments in September that raised demand for funds.

Size and Composition

LCY bonds outstanding in the PRC rose 3.6% quarter-on-quarter (q-o-q) in Q3 2019 after gaining 4.0% q-o-q in the second quarter (Q2) of 2019. On a y-o-y basis, LCY bonds grew 14.9% y-o-y (Table 1).

Government bonds. The PRC's government bond market continued to grow; however, growth moderated to 3.5% q-o-q from 4.2% q-o-q in Q2 2019. The slowing growth was due to a decline in government bond issuance during Q3 2019. The slowest government bond growth came from policy bank bonds, which grew 1.5% q-o-q in the quarter as issuance declined 17.2% q-o-q. Local government bond growth was the fastest among all government bond categories

at 5.1% q-o-q, while issuance fell 5.9% q-o-q as local governments were asked to fulfill their bond quotas by the end of September to help speed up the implementation of infrastructure projects. The government is also requiring local governments to allocate the proceeds raised from special bonds to infrastructure projects by the end of October.

Corporate bonds. In contrast to the PRC's government bonds, corporate bonds outstanding grew 3.9% q-o-q in Q3 2019, accelerating from Q2 2019's 3.6% q-o-q growth.

The growth was largely driven by an increase in financial bonds (9.2% q-o-q), medium-term notes (3.8% q-o-q), and listed corporate bonds (3.2% q-o-q) (Table 2).

Table 1: Size and Composition of the Local Currency Bond Market in the People's Republic of China

	Outstanding Amount (billion)						Growth Rates (%)			
	Q3 2018		Q2 2019		Q3 2019		Q3 2018		Q3 2019	
	CNY	USD	CNY	USD	CNY	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	71,319	10,383	79,049	11,512	81,916	11,459	5.3	15.4	3.6	14.9
Government	46,869	6,823	51,135	7,447	52,913	7,402	6.2	16.6	3.5	12.9
Treasury Bonds and Other Government Bonds	14,357	2,090	15,461	2,252	15,963	2,233	3.7	11.1	3.3	11.2
Central Bank Bonds	0	0	4	1	14	2	-	-	250.0	-
Policy Bank Bonds	14,184	2,065	15,213	2,215	15,445	2,161	1.3	8.3	1.5	8.9
Local Government Bonds	18,327	2,668	20,457	2,979	21,491	3,006	12.7	29.3	5.1	17.3
Corporate	24,450	3,560	27,914	4,065	29,003	4,057	3.6	13.1	3.9	18.6
Policy Bank Bonds										
China Development Bank	7,979	1,162	8,580	1,250	8,665	1,212	3.0	8.8	1.0	8.6
Export-Import Bank of China	2,299	335	2,533	369	2,601	364	(2.9)	0.8	2.7	13.2
Agricultural Devt. Bank of China	3,907	569	4,100	597	4,179	585	0.3	12.0	1.9	7.0

(-) = negative, -- = not applicable, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

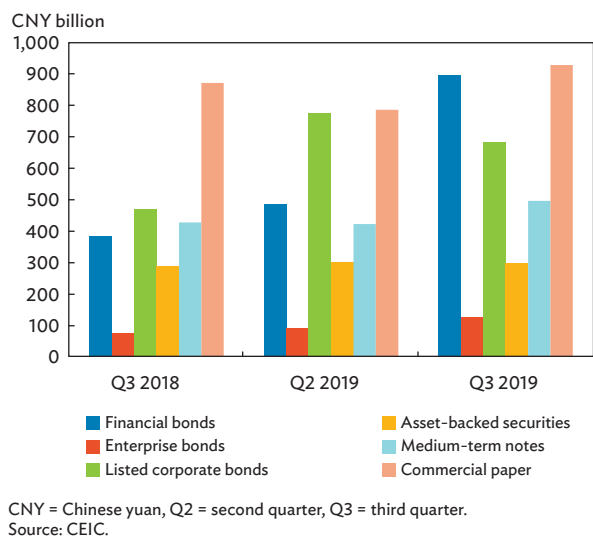
1. Calculated using data from national sources.
2. Treasury bonds include savings bonds and local government bonds.
3. Bloomberg LP end-of-period local currency-USD rates are used.
4. Growth rates are calculated from local currency base and do not include currency effects.

Sources: CEIC and Bloomberg LP.

Table 2: Corporate Bonds Outstanding in Key Categories

	Amount (CNY billion)			Growth Rate (%)			
	Q3 2018	Q2 2019	Q3 2019	Q3 2018		Q3 2019	
				q-o-q	y-o-y	q-o-q	y-o-y
Financial Bonds	4,123	5,042	5,505	1.1	20.3	9.2	33.5
Enterprise Bonds	3,968	3,834	3,840	0.9	(14.4)	0.2	(3.2)
Listed Corporate Bonds	5,963	7,024	7,250	1.0	18.1	3.2	21.6
Commercial Paper	1,896	2,197	2,152	1.1	24.1	(2.0)	13.5
Medium-Term Notes	5,270	5,919	6,141	1.0	13.4	3.8	16.5
Asset-Backed Securities	1,343	1,924	2,081	1.2	74.5	8.1	54.9

(-) = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third quarter, y-o-y = year-on-year.
Source: CEIC.

Figure 2: Corporate Bond Issuance in Key Sectors

The rise in financial bonds has been largely driven by perpetual bonds issued by commercial banks as part of its efforts to replenish capital after write-downs of bad assets. Asset-backed securities grew strongly at 8.1% q-o-q, but the contribution to growth was smaller given this category's overall size (**Figure 2**).

The PRC's LCY corporate bond market continued to be dominated by a few big issuers (**Table 3**). At the end of Q3 2019, the top 30 corporate bond issuers accounted for a combined CNY7.7 trillion worth of corporate bonds outstanding, or about 26.5% of the total market. Of the top 30, the 10 largest issuers accounted for an aggregate CNY4.9 trillion. China Railway, the top issuer, had more than three times the outstanding amount of bonds as Agricultural Bank of China, the second-largest issuer. The top 30 issuers included 14 banks, which continued to generate funding to strengthen their capital bases, improve liquidity, and lengthen their maturity profiles.

Table 4 lists the largest corporate bond issuances in Q3 2019. The top issuers consisted largely of banks and state-owned enterprises as banks sought to improve their funding and capital bases.

Investor Profile

Among the major government bond categories, banks were the single-largest holder at the end of September (**Figure 3**), with banks owning at least 73.4% of all

outstanding government bonds. The concentration of bank ownership was the highest for local government bonds (87.9%), as banks are being asked by the government to help support the funding efforts of local governments. Policy banks were the next largest holder of local government bonds. Unincorporated products were the second-largest holder of policy bank bonds after banks.¹²

The volume of interest rate swaps rose 11.7% q-o-q in Q3 2019. The 7-day repurchase remained the most used interest rate swap, comprising a 70.7% share of the total interest rate swap volume during the quarter (**Table 5**).

Policy, Institutional, and Regulatory Developments

People's Bank of China Reduces Reserve Requirement Ratio for Banks

On 6 September, the PBOC announced that it would reduce by 50 bps the reserve requirement ratio of financial institutions, effective 16 September. In addition, rural commercial banks operating solely within provincial administrative regions would be entitled to an additional 100 bps cut, with the reduction to be phased in on 15 October and 15 November.

The People's Republic of China Removes Quota on Some Foreign Investor Programs

On 10 September, the State Administration of Foreign Exchange announced that it would remove quota limits on its Qualified Foreign Institutional Investor and Renminbi Qualified Foreign Institutional Investor programs. The government said that this would make it easier for foreign investors to participate in the domestic market of the PRC.

China Securities Regulatory Commission Places Limit on Private Corporate Bond Issuance

On 15 October, the China Securities Regulatory Commission announced that the total amount of outstanding corporate bonds sold privately would be limited to 40% of a company's net assets. Additional bonds issued exceeding this ratio may only be used to repay existing debt.

¹² Unincorporated products include banks' wealth management products, securities investment funds, trust funds, and insurance products.

Table 3: Top 30 Issuers of Local Currency Corporate Bonds in the People's Republic of China

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (CNY billion)	LCY Bonds (USD billion)			
1.	China Railway	1,715.5	240.0	Yes	No	Transportation
2.	Agricultural Bank of China	453.1	63.4	Yes	Yes	Banking
3.	Industrial and Commercial Bank of China	450.7	63.0	Yes	Yes	Banking
4.	Bank of China	423.1	59.2	Yes	Yes	Banking
5.	Central Huijin Investment	371.0	51.9	Yes	No	Asset Management
6.	China Construction Bank	333.3	46.6	Yes	Yes	Banking
7.	China Minsheng Banking	305.3	42.7	No	Yes	Banking
8.	State Grid Corporation of China	292.7	40.9	Yes	No	Public Utilities
9.	China CITIC Bank	267.5	37.4	No	Yes	Banking
10.	Shanghai Pudong Development Bank	260.5	36.4	No	Yes	Banking
11.	Bank of Communications	254.3	35.6	No	Yes	Banking
12.	China National Petroleum	225.0	31.5	Yes	No	Energy
13.	Industrial Bank	183.0	25.6	No	Yes	Banking
14.	Huaxia Bank	173.4	24.3	Yes	No	Banking
15.	China Everbright Bank	173.3	24.2	Yes	Yes	Banking
16.	Tianjin Infrastructure Construction and Investment Group	170.7	23.9	Yes	No	Industrial
17.	State Power Investment	161.6	22.6	Yes	No	Energy
18.	Ping An Bank	158.7	22.2	No	Yes	Banking
19.	China Merchants Bank	143.5	20.1	Yes	Yes	Banking
20.	PetroChina	135.0	18.9	Yes	Yes	Energy
21.	CITIC Securities	135.0	18.9	Yes	Yes	Brokerage
22.	Datong Coal Mine Group	117.6	16.5	Yes	No	Coal
23.	China Datang	113.5	15.9	Yes	Yes	Energy
24.	China Life Insurance	103.0	14.4	Yes	Yes	Insurance
25.	China Three Gorges Corporation	99.0	13.8	Yes	No	Power
26.	China Merchants Securities	93.2	13.0	No	Yes	Brokerage
27.	Bank of Beijing	93.0	13.0	No	Yes	Banking
28.	Guotai Junan Securities	90.2	12.6	No	Yes	Financial
29.	Guangzhou R&F Properties	90.1	12.6	No	Yes	Real Estate
30.	China Cinda Asset Management	90.0	12.6	Yes	Yes	Asset Management
Total Top 30 LCY Corporate Issuers		7,675.8	1,073.8			
Total LCY Corporate Bonds		29,003.0	4,057.3			
Top 30 as % of Total LCY Corporate Bonds		26.5%	26.5%			

CNY = Chinese yuan, LCY = local currency, USD = United States dollar.

Notes:

1. Data as of 30 September 2019.

2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.

Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

Table 4: Notable Local Currency Corporate Bond Issuance in the Third Quarter of 2019

Corporate Issuers	Coupon Rate (%)	Issued Amount (CNY billion)	Corporate Issuers	Coupon Rate (%)	Issued Amount (CNY billion)
China State Railway Group			Industrial Bank		
5-year bond	3.50	10	3-year bond	3.55	20
5-year bond	3.45	10	10-year bond	4.15	30
5-year bond	3.34	10	10-year bond	4.12	20
5-year bond	3.35	13	Bank of Communications		
5-year bond	3.37	12	10-year bond	4.10	30
5-year bond	3.41	12	15-year bond	4.49	10
20-year bond	4.07	5	Industrial Bank		
20-year bond	4.10	5	10-year bond	3.98	30
20-year bond	4.02	5	15-year bond	4.34	10
20-year bond	3.99	13	China Merchants Bank		
20-year bond	4.03	8	3-year bond	3.45	30
			3-year bond	3.33	20

CNY = Chinese yuan.

Source: Based on data from Bloomberg LP.

Figure 3: Government Bonds Investor Profile

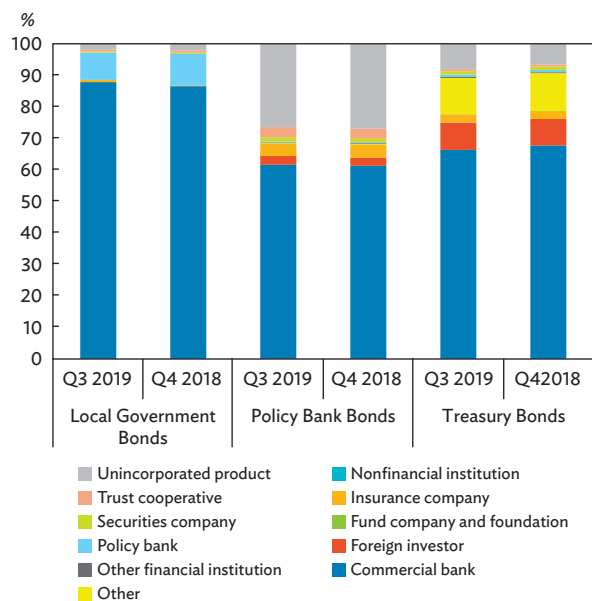


Table 5: Notional Values of the People's Republic of China's Interest Rate Swap Market in the Third Quarter of 2019

Interest Rate Swap Benchmarks	Notional Amount (CNY billion)	Share of Total Notional Amount (%)	Growth Rate (%)
7-Day Repo Rate	3,557.9	70.7	5.0
Overnight SHIBOR	16.3	0.3	(51.9)
3-Month SHIBOR	1,397.4	27.8	33.2
1-Year Lending Rate	34.2	0.7	(100.0)
Loan Interest Rate, 1 Year	0.1	0.001	(100.0)
5-Year Lending Rate	1.7	0.03	(100.0)
10-Year Bond Yield	10.6	0.2	(20.0)
10-Year Treasury Yield	11.4	0.2	(27.9)
3-Year AAA Short-Term Notes/ Government Debt	0.7	0.01	(100.0)
10-Year Bond Yield/ 10-Year Government Bond Yield	0.2	0.004	(93.1)
Total	5,030.5	100.0	11.7

() = negative, - = not applicable, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q3 = third quarter, Repo = repurchase, SHIBOR = Shanghai Interbank Offered Rate.
Note: Growth rate computed based on notional amounts.

Sources: AsianBondsOnline and ChinaMoney.