

Market Summaries

People's Republic of China

Yield Movements

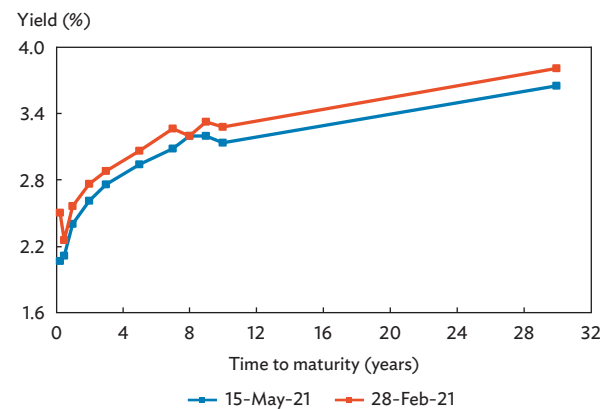
Between 28 February and 15 May, the local currency (LCY) government bond yield curve of the People's Republic of China (PRC) shifted downward for all tenors except the 8-year bond, which was unchanged (**Figure 1**). The largest decline was seen for the 3-month tenor, which fell 44 basis points (bps), followed by the 7-year tenor, which fell 18 bps. All other maturities fell between 12 bps and 16 bps. As a result, the 2-year versus 10-year yield spread moved upward only 1 bp during the review period.

While bond yields in the PRC fell, the economy continued to post strong gains as it recovered from the COVID-19 pandemic. The declines in the PRC's bond yields despite strong economic gains were largely due to expectations that the Government of the PRC would reduce the supply of government bonds outstanding given the domestic economic recovery, which has reduced the need for additional fiscal stimulus. The PRC is also focusing on mitigating credit risk in financial markets, and investors expect the government to rein in the issuance of local government bonds.

The PRC's GDP expanded rapidly in the first quarter (Q1) of 2021, growing 18.1% year-on-year (y-o-y) after gaining 6.5% y-o-y in the fourth quarter (Q4) of 2020. While all major sectors showed accelerated growth, the gains were particularly notable in the secondary and tertiary industries. The secondary industry's growth rate rose to 24.4% y-o-y in Q1 2021 from 2.6% y-o-y in the prior quarter, while the tertiary industry's growth increased to 15.6% y-o-y from 2.1% y-o-y in the same period. Primary industry grew 8.1% y-o-y in Q1 2021 versus 3.0% y-o-y in Q4 2020.

Industrial production also sustained its momentum but at a slower pace. In April, industrial production grew 9.8% y-o-y, which was lower than March's 14.1% y-o-y gain and the 35.1% y-o-y growth reported in January–February.

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



Source: Based on data from Bloomberg LP.

Despite the PRC's sustained economic recovery, inflation in the PRC remained manageable. Consumer price inflation rose to 0.9% y-o-y in April, which was higher than the rate of 0.4% y-o-y recorded in March.

Size and Composition

LCY bonds outstanding in the PRC grew 2.1% quarter-on-quarter (q-o-q) in Q1 2021 after rising 3.3% q-o-q in Q4 2020 to CNY103.5 trillion (USD15.8 trillion) (**Table 1**). Bond growth also slowed on a y-o-y basis to 17.3% from 20.5% in the same period. The slower growth rate was largely due to a decline in government bond issuance in Q1 2021.

Government bonds. Government bonds outstanding in the PRC grew 1.6% q-o-q in Q1 2021, slower than Q4 2020's growth of 3.8% q-o-q. The slowdown was due to a decline in the issuance of Treasury bonds of 37.8% q-o-q in Q1 2021 due to reduced fiscal stimulus needs amid the economy's sustained recovery. In addition, the government shifted its policies toward risk control, leading Treasury bonds and other government bonds outstanding to grow only 0.5% q-o-q in Q1 2021 versus 8.3% q-o-q in the previous quarter.

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

	Outstanding Amount (billion)						Growth Rates (%)			
	Q1 2020		Q4 2020		Q1 2021		Q1 2020		Q1 2021	
	CNY	USD	CNY	USD	CNY	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	88,270	12,464	101,413	15,537	103,528	15,799	4.9	16.1	2.1	17.3
Government	55,852	7,886	65,130	9,978	66,198	10,102	3.5	13.8	1.6	18.5
Treasury Bonds and Other Government Bonds	16,850	2,379	20,933	3,207	21,032	3,210	0.9	13.2	0.5	24.8
Central Bank Bonds	19	3	15	2	15	2	(15.9)	1,133.3	0.0	(18.9)
Policy Bank Bonds	15,985	2,257	18,040	2,764	18,382	2,805	1.8	8.2	1.9	15.0
Local Government Bonds	22,999	3,247	26,142	4,005	26,769	4,085	6.6	18.5	2.4	16.4
Corporate	32,418	4,577	36,283	5,559	37,329	5,697	7.3	20.3	2.9	15.2

CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth 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.

Local government bonds, which used to be the major driver of bond market growth in the PRC, grew only 2.4% q-o-q in Q1 2021 after rising 0.8% q-o-q in Q4 2020, largely due to base effects. In Q4 2020, local governments hardly issued bonds after having mostly completed their annual quotas for special bonds. However, in Q1 2020, despite the renewal of the quotas at the start of the year, local government bond issuance rose only 16.9% q-o-q and fell 44.5% y-o-y. The central government is slowing the issuance of local government bonds unlike in previous years when it had pushed for the utilization of the quotas early in the year. The government also reduced the local government bond quota to CNY3.65 trillion in 2021 from CNY3.75 trillion in 2020.

Policy bank bonds, however, posted a moderate growth of 1.9% q-o-q in Q1 2021 after gaining 0.9% in Q4 2020.

Corporate bonds. The PRC's corporate bond market's growth rate inched up to 2.9% q-o-q in Q1 2021 from 2.4% q-o-q in Q4 2020. Issuance of corporate bonds declined 3.0% q-o-q in Q1 2021 due to government directives on overleveraging as well as investor concerns regarding credit risks.

Commercial paper outstanding rose 8.9% q-o-q in Q1 2021 as companies used short-term borrowing in anticipation of lower interest rates (**Table 2**). State-owned enterprise bonds and medium-term notes outstanding were roughly unchanged owing to a reduction in issuance due to risk controls. Financial bonds gained 4.3% q-o-q as commercial banks beefed up their funding in anticipation of increased economic activity.

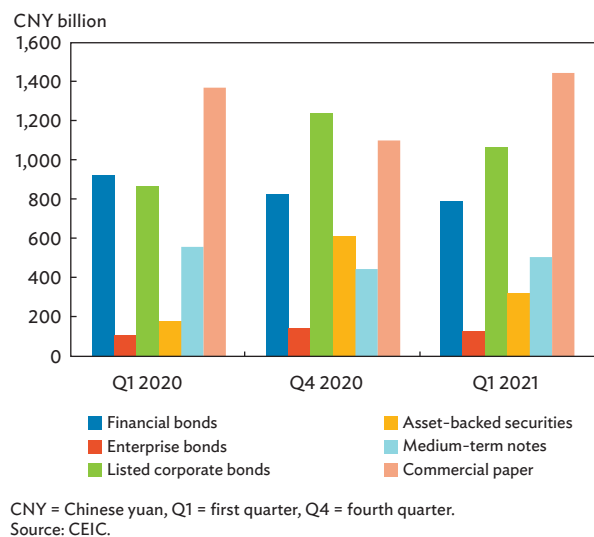
Credit risk concerns also led to a decline in nearly all major corporate bond issuance categories (**Figure 2**). The exceptions were commercial paper, with issuance

Table 2: Corporate Bonds Outstanding in Key Categories

	Amount (CNY billion)			Growth Rate (%)			
	Q1 2020	Q4 2020	Q1 2021	Q1 2020		Q1 2021	
				q-o-q	y-o-y	q-o-q	y-o-y
Financial Bonds	6,364	7,427	7,746	1.1	34.2	4.3	21.7
Enterprise Bonds	3,707	3,880	3,860	1.0	(4.3)	(0.5)	4.1
Listed Corporate Bonds	8,328	10,223	10,603	1.1	26.0	3.7	27.3
Commercial Paper	2,671	2,152	2,344	1.3	19.2	8.9	(12.2)
Medium-Term Notes	6,829	7,381	7,382	1.1	17.5	0.03	8.1
Asset-Backed Securities	2,388	2,883	2,942	1.0	38.2	2.0	23.2

() = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth quarter, y-o-y = year-on-year.

Source: CEIC.

Figure 2: Corporate Bond Issuance in Key Sectors

rising 31.3% q-o-q, and medium-term notes, which rose 13.8% q-o-q. Financial bond issuance was roughly unchanged, declining 4.3% q-o-q.

The top 30 issuers' share of total LCY corporate bonds outstanding remained roughly unchanged at 28.7% in Q1 2021 (Table 3). By the end of March, the bonds outstanding of the top 30 issuers reached CNY10.7 trillion. Of the top 30, the 10 largest issuers accounted for an aggregate CNY7.0 trillion. China Railway remained the largest issuer, accounting for 24.8% of the total bonds outstanding of the top 30 issuers. The top 30 issuers included 14 banks.

Table 4 lists the largest corporate bond issuances in Q1 2021. Of the five top issuers, four are financial institutions that sought to increase their liquidity and funding during the quarter. The largest issuer in the PRC has consistently been China Railway, which again issued bonds for infrastructure development in Q1 2021. The firm raised a total of CNY70 billion during the quarter through bonds with various maturities.

Investor Profile

Government bonds. Banks remained the majority investor group in the government bond market in Q1 2021 (Figure 3). However, with strong inflows from other types of investors, banks' holding share fell somewhat from a year earlier. At the end of March, banks

held 65.5% of outstanding Treasury bonds (down from 67.5% at the end of March 2020), 55.9% of outstanding policy bank bonds (down from 57.4%), and 87.6% of outstanding local government bonds.

In contrast, the Treasury bond holdings share of foreign investors increased during the review period, rising to 10.9% at the end of March from 9.0% a year earlier, while their share of policy bank bonds rose to 5.4% from 3.4%.

Liquidity

The volume of interest rate swaps rose 6.4% q-o-q in Q1 2021 (Table 5). Demand for interest rate swaps was lower given the decline in interest rates. The 7-day repo rate remained the most used interest rate swap with an 85.7% share of all transactions.

Policy, Institutional, and Regulatory Developments

The People's Bank of China and the State Administration of Foreign Exchange Implement Cross-Border Pilot Program for Multinational Corporations

In March, the People's Bank of China and the State Administration of Foreign Exchange launched a pilot program to allow multinational corporations with good credit standing to enjoy a more streamlined process for cross-border fund transfers. The pilot program is meant to integrate multinational corporations' transfers of both Chinese yuan and foreign currencies. The benefits of the pilot program for the companies include a unified policy on Chinese yuan and other foreign currencies, the relaxation of quotas on external debt and overseas loans, and the easier cross-border transfer of currencies and purchases of foreign currencies subject to quota.

The People's Bank of China Adjusts Foreign Exchange Reserve Requirement Ratio

Effective 15 June, the foreign exchange reserve requirement ratio of financial institutions was raised to 7.0% from 5.0%, as previously announced by the People's Bank of China in May.

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	2,648.5	404.2	Yes	No	Transportation
2.	Agricultural Bank of China	680.3	103.8	Yes	Yes	Banking
3.	Bank of China	641.4	97.9	Yes	Yes	Banking
4.	Industrial and Commercial Bank of China	640.1	97.7	Yes	Yes	Banking
5.	Shanghai Pudong Development Bank	485.9	74.2	No	Yes	Banking
6.	Bank of Communications	462.1	70.5	No	Yes	Banking
7.	Central Huijin Investment	456.0	69.6	Yes	No	Asset Management
8.	China Construction Bank	388.1	59.2	Yes	Yes	Banking
9.	Industrial Bank	326.3	49.8	No	Yes	Banking
10.	State Grid Corporation of China	291.0	44.4	Yes	No	Public Utilities
11.	China National Petroleum	274.9	42.0	Yes	No	Energy
12.	China Securities Finance	264.0	40.3	Yes	No	Financial Services
13.	China Minsheng Banking	260.0	39.7	No	Yes	Banking
14.	China CITIC Bank	255.0	38.9	No	Yes	Banking
15.	State Power Investment	253.8	38.7	Yes	No	Energy
16.	China Everbright Bank	215.9	32.9	Yes	Yes	Banking
17.	China Merchants Bank	209.2	31.9	Yes	Yes	Banking
18.	Ping An Bank	198.7	30.3	No	Yes	Banking
19.	Huaxia Bank	198.0	30.2	Yes	No	Banking
20.	China Southern Power Grid	182.5	27.9	Yes	No	Energy
21.	CITIC Securities	168.8	25.8	Yes	Yes	Brokerage
22.	Tianjin Infrastructure Construction and Investment Group	160.6	24.5	Yes	No	Industrial
23.	Postal Savings Bank of China	160.0	24.4	Yes	Yes	Banking
24.	Shaanxi Coal and Chemical Industry Group	144.0	22.0	Yes	No	Energy
25.	China Merchants Securities	136.0	20.8	Yes	No	Brokerage
26.	Huatai Securities	131.8	20.1	Yes	Yes	Brokerage
27.	PetroChina	119.0	18.2	Yes	Yes	Energy
28.	Jinneng Holding Coal Group	118.2	18.0	Yes	Yes	Coal
29.	Datong Coal Mine Group	114.2	17.4	Yes	No	Coal
30.	China Three Gorges Corporation	114.0	17.4	Yes	No	Power
Total Top 30 LCY Corporate Issuers		10,698.1	1,632.6			
Total LCY Corporate Bonds		37,329.5	5,696.7			
Top 30 as % of Total LCY Corporate Bonds		28.7%	28.7%			

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

Notes:

1. Data as of 31 March 2021.

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.

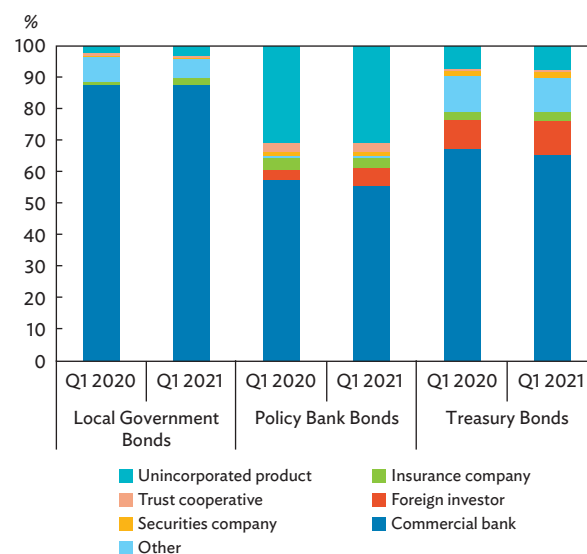
Table 4: Notable Local Currency Corporate Bond Issuances in the First Quarter of 2021

Corporate Issuers	Coupon Rate (%)	Issued Amount (CNY billion)
China Railway ^a		
5-year bond	3.40	20.0
5-year bond	3.53	20.0
10-year bond	3.65	15.0
10-year bond	3.56	7.0
20-year bond	3.82	8.0
Shanghai Pudong Development Bank		
3-year bond	2.48	60.0
China Merchants Securities ^a		
3-month bond	2.49	4.0
3-month bond	3.03	3.0
3-month bond	3.25	4.2
1-year bond	3.55	6.0
2-year bond	3.85	6.0
2-year bond	3.24	1.5
3-year bond	3.95	6.0
3-year bond	3.95	4.8
3-year bond	3.53	4.5
3-year bond	3.58	1.4
China Everbright Bank		
3-year bond	3.45	40.0
Bank of China		
3-year bond	3.36	10.0
10-year bond	4.15	15.0
15-year bond	4.38	10.0

CNY = Chinese yuan.

^a Multiple issuance of the same tenor indicates issuance on different dates.

Source: Based on data from Bloomberg LP.

Figure 3: Local Currency Treasury Bonds and Policy Bank Bonds Investor Profile**Table 5: Notional Values of the People's Republic of China's Interest Rate Swap Market in the First Quarter of 2021**

Interest Rate Swap Benchmarks	Notional Amount (CNY billion)	Share of Total Notional Amount (%)	Growth Rate (%)
	Q1 2021		q-o-q
1-Day Repo Rate (Deposit Institutions)	0.2	0.004	0.0
7-Day Repo Rate	4,594.3	85.7	1.0
7-day Repo Rate (Deposit Institutions)	0.3	0.005	0.4
Overnight SHIBOR	21.3	0.4	2.1
3-Month SHIBOR	685.1	12.8	1.2
1-Year Lending Rate	23.0	0.4	2.1
5-Year Lending Rate	5.8	0.1	9.7
10-Year Treasury Yield	10.5	0.2	0.5
3-Year AAA Short-Term Notes/ Government Debt	0.1	0.001	0.3
China Development Bank 10-Year Bond Yield	11.0	0.2	0.5
10-Year Bond Yield/10-Year Government Bond Yield	10.5	0.2	0.5
Total	5,362.1	100.0	6.4

CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter,

Repo = repurchase, SHIBOR = Shanghai Interbank Offered Rate.

Note: Growth rate computed based on notional amounts.

Sources: AsianBondsOnline and ChinaMoney.