

Market Summaries

People's Republic of China

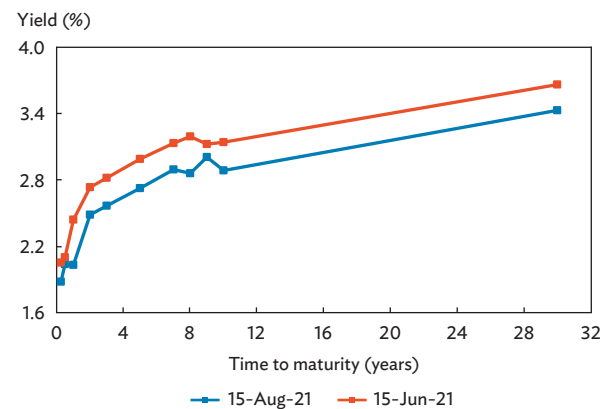
Yield Movements

The entire yield curve of the People's Republic of China's (PRC) local currency (LCY) bond market shifted downward between 15 June and 15 August (**Figure 1**). The largest decline was for the 1-year tenor, which declined 41 basis points (bps), while the smallest declines were for the 6-month tenor (6 bps) and 9-year tenor (12 bps). All other tenors fell between 17 bps and 33 bps during the review period. The 2-year versus 10-year yield spread was barely changed between 15 June and 15 August, falling marginally from 41 bps to 40 bps.

The PRC's yield curve continues to decline despite continued economic growth. The decline was largely due to concerns that the PRC's growth momentum would slow due to headwinds in the global economy, owing once again to rising COVID-19 cases. The PRC's gross domestic product (GDP) grew 7.9% year-on-year (y-o-y) in the second quarter (Q2) of 2021 after gaining 18.3% y-o-y in the first quarter (Q1). While all major sectors posted slower growth, the largest decline was in the secondary sector, where growth fell to 7.5% y-o-y in Q2 2021 from 24.4% y-o-y in Q1 2021. The next largest decline was in the tertiary sector, which grew 8.3% y-o-y after expanding 15.6% y-o-y in the previous quarter. The growth rate in the primary sector was more stable, with a growth rate of 7.6% y-o-y versus 8.1% y-o-y during the same review period.

Other more recent economic indicators also indicate a potential slowdown in momentum. The PRC's industrial production grew 6.4% y-o-y in July, falling from the 8.3% y-o-y expansion posted in June. The PRC's manufacturing Purchasing Managers Index dipped to 50.4 in July from 50.9 in June, while inflation also seems to have leveled off. The PRC reported consumer price inflation of 1.0% y-o-y in July versus 1.1% y-o-y in June and 1.3% y-o-y in May. Producer prices recorded a 9.0% y-o-y gain in July, compared with 8.8% y-o-y in June and 9.0% y-o-y in May.

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



Source: Based on data from Bloomberg LP.

Market sentiment was influenced by statements from the State Council on 7 July suggesting a shift toward policy easing via monetary tools such as reserve requirement ratio cuts to help support the economy, particularly smaller businesses. On 9 July, the People's Bank of China (PBOC) announced a 50-bps cut to its reserve requirement ratio, fueling market speculation that a cut in interest rates such as the 1-year loan prime rate would be next. However, the PBOC has so far left unchanged its benchmark interest rates.

Size and Composition

Growth in the PRC's outstanding LCY bonds accelerated to 3.0% quarter-on-quarter (q-o-q) in Q2 2021 from 2.1% q-o-q in Q1 2021, reaching a size of CNY106.6 trillion (USD16.5 trillion) (**Table 1**). On a y-o-y basis, the growth rate for Q2 2021 was slightly lower at 14.4% versus 17.3% in the previous quarter. The faster q-o-q growth for Q2 2021 was largely due to an increase in local government bonds.

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

	Outstanding Amount (billion)						Growth Rates (%)			
	Q2 2020		Q1 2021		Q2 2021		Q2 2020		Q2 2021	
	CNY	USD	CNY	USD	CNY	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	91,285	13,189	103,528	15,799	106,590	16,507	5.6	17.9	3.0	14.4
Government	58,867	8,332	66,198	10,102	68,384	10,591	5.4	15.1	3.3	16.2
Treasury Bonds and Other Government Bonds	17,775	2,516	21,032	3,210	21,548	3,337	5.5	15.0	2.5	21.2
Central Bank Bonds	15	2	15	2	15	2	(18.9)	0.0	0.0	0.0
Policy Bank Bonds	16,662	2,358	18,382	2,805	18,658	2,890	4.2	9.5	1.5	12.0
Local Government Bonds	24,415	3,456	26,769	4,085	28,163	4,362	6.2	19.3	5.2	15.4
Corporate	34,320	4,857	37,329	5,697	38,207	5,917	5.9	22.9	2.3	11.3

CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second 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.

Government bonds. The PRC's government bonds outstanding rose 3.3% q-o-q in Q2 2021 to CNY68.4 trillion after gaining 1.6% q-o-q in Q1 2021. The faster growth was largely due to an increase in local government bonds outstanding as local governments sought to utilize their bond quotas.

Issuance of Treasury bonds declined 4.5% q-o-q, but fewer maturities during the quarter led to Treasury bonds and other government bonds outstanding rising 2.5% q-o-q to CNY21.5 trillion. The larger increase was partly due to a low base effect resulting from the PRC's focus on risk control, which led to only a 0.5% q-o-q increase in Treasury and other government bonds outstanding in Q1 2021. This was visible in the decline in the y-o-y growth rate in Treasury and other government bonds from 24.8% in Q2 2020 to 21.2% in Q2 2021. Similarly, policy bank bond issuance fell 9.6% q-o-q in Q2 2021, resulting in policy bank bonds outstanding rising 1.5% q-o-q to CNY18.7 trillion after gaining 1.9% q-o-q in the previous quarter.

On the other hand, there was a rise in the issuance of local government bonds, which rose 173.5% q-o-q in Q2 2021, resulting in a 5.2% q-o-q increase in local government bonds outstanding to CNY28.2 trillion at the end of June. This was due to a low base effect as local government issuance was down in Q1 2021 due to a delay in the release of local government bond quotas. Despite this, the overall quota for local bonds outstanding in 2021 was reduced to CNY3.65 trillion from CNY3.75 trillion in 2020. Overall, local government issuance for the first half of 2021 was down 4.2% from the same period in 2020.

On a y-o-y basis, local government bonds outstanding grew 15.4%, up from 16.4% in Q1 2021.

Corporate bonds. Corporate bonds outstanding in the PRC rose 2.3% q-o-q in Q2 2021, which was down from Q1 2021's 2.9% q-o-q growth on dampened sentiment due to government efforts to rein in credit risk and rising corporate defaults this year. The PRC has also tempered issuance of debt by local government financing vehicles. While corporate bond issuance in the PRC grew 1.3% q-o-q to USD699 billion in Q2 2021 after a decline of 3.0% q-o-q in Q1 2021, corporate bond issuance was down 5.8% y-o-y.

The value of commercial paper outstanding fell 2.8% q-o-q and 19.3% y-o-y in Q2 2021 to CNY2.3 trillion at the end of June, as companies preferred to lock in lower rates with longer-dated debt (**Table 2**). Concerns regarding credit risk and rising defaults also led most major corporate bond sectors to post q-o-q declines or weak growth rates. Enterprise bonds declined 1.4% q-o-q, while medium-term notes rose 1.0% q-o-q. Listed corporate bonds and financial bonds rose 3.6% q-o-q and 3.8% q-o-q, respectively.

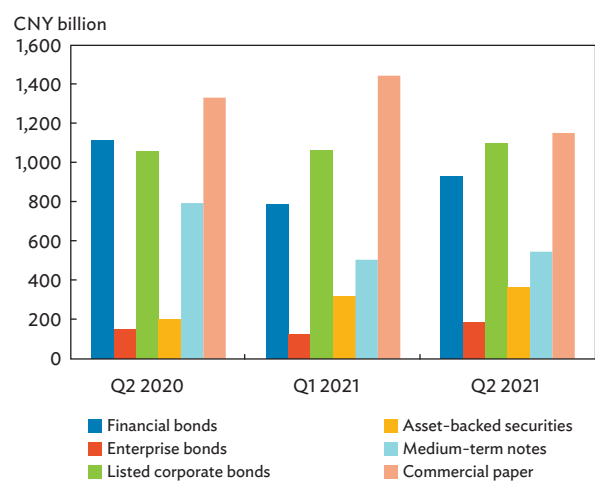
Most major corporate bond segments showed a q-o-q increase in issuance, excluding commercial paper, which declined 20.3% q-o-q (**Figure 2**). However, versus the same period a year earlier, issuance of nearly all major categories of corporate bonds exhibited a decline, excluding asset-backed securities, enterprise bonds, and listed corporate bonds.

Table 2: Corporate Bonds Outstanding in Key Categories

	Amount (CNY billion)			Growth Rate (%)			
	Q2 2020	Q1 2021	Q2 2021	Q2 2020		Q2 2021	
				q-o-q	y-o-y	q-o-q	y-o-y
Financial Bonds	6,803	7,746	8,038	1.4	34.9	3.8	18.2
Enterprise Bonds	3,771	3,860	3,808	1.0	(1.4)	(1.4)	1.0
Listed Corporate Bonds	8,996	10,603	10,986	1.4	3.6	3.6	22.1
Commercial Paper	2,825	2,344	2,279	1.3	(2.8)	(2.8)	(19.3)
Medium-Term Notes	7,300	7,382	7,457	1.3	1.0	1.0	2.1
Asset-Backed Securities	2,406	2,942	3,075	1.4	4.5	4.5	27.8

(-) = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, y-o-y = year-on-year.
Source: CEIC.

Figure 2: Corporate Bond Issuance in Key Sectors



CNY = Chinese yuan, Q1 = first quarter, Q2 = second quarter.
Source: ChinaBond.

The top 30 issuers' share of total LCY corporate bonds outstanding fell to 28.5% in Q2 2021 from 28.7% in Q1 2021 (Table 3). By the end of June, the bonds outstanding of the top 30 issuers reached CNY10.9 trillion. Of the top 30, the 10 largest issuers accounted for an aggregate CNY7.1 trillion. China Railway remained the largest issuer, accounting for 24.3% of the total bonds outstanding of the top 30 issuers.

Table 4 lists the largest corporate bond issuances in Q2 2021. Of the five top issuances, four were from financial institutions that sought to increase their liquidity and funding during the quarter. To help raise funds, the Bank of Communications and the Industrial and Commercial Bank issued perpetual bonds.

Investor Profile

Government bonds. Commercial banks remained the dominant investor in the PRC's government bond market in Q2 2021, albeit with a declining share of the total (Figure 3). Banks are the most significant holders of local government bonds by far, holding a share of 87.0% in Q2 2021, down slightly from 87.9% in Q2 2020.

Banks are also significant holders of Treasury bonds, holding 65.0% of the total stock at the end of Q2 2021, down somewhat from 66.5% at the end of Q2 2020. Banks also held 55.5% of policy bank bonds at the end of June 2021, down from 57.3% in June 2020.

Foreign investors saw their share of government bond holdings increase the most. Their share of Treasury bonds increased to 11.1% in Q2 2021, up from 9.5% in Q2 2020, while the foreign holdings' share of policy bank bonds also rose to 5.5% from 3.8% in the same review period.

Liquidity

The volume of interest rate swaps rose 6.1% q-o-q in Q2 2021 after a 0.4% q-o-q gain in the previous quarter, reflecting increased demand (Table 5).

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	410.17	Yes	No	Transportation
2.	Industrial and Commercial Bank of China	711.4	110.17	Yes	Yes	Banking
3.	Bank of China	658.1	101.92	Yes	Yes	Banking
4.	Agricultural Bank of China	650.3	100.71	Yes	Yes	Banking
5.	Bank of Communications	544.5	84.33	No	Yes	Banking
6.	Shanghai Pudong Development Bank	485.9	75.25	Yes	Yes	Banking
7.	Shanghai Pudong Development Bank	433.5	67.14	No	Yes	Banking
8.	China Construction Bank	388.1	60.10	Yes	Yes	Banking
9.	China Citic Bank	315.0	48.78	No	Yes	Banking
10.	China Securities Finance	302.5	46.85	Yes	No	Finance
11.	State Grid Corporation of China	296.5	45.92	Yes	No	Public Utilities
12.	China Minsheng Bank	290.0	44.91	No	Yes	Banking
13.	Industrial Bank	286.3	44.33	No	Yes	Banking
14.	China National Petroleum	274.9	42.58	Yes	No	Energy
15.	State Power Investment	253.3	39.22	Yes	No	Power
16.	China Merchants Bank	229.2	35.50	No	Yes	Banking
17.	China Everbright Bank	215.9	33.44	No	Yes	Banking
18.	Ping An Bank	185.0	28.65	No	Yes	Banking
19.	Huaxia Bank	180.0	27.88	No	Yes	Banking
20.	China Southern Power Grid	177.5	27.49	Yes	No	Public Utilities
21.	CITIC Securities	164.3	25.45	Yes	Yes	Brokerage
22.	Postal Savings Bank of China	160.0	24.78	Yes	Yes	Banking
23.	Shaanxi Coal and Chemical Industry Group	156.0	24.16	Yes	Yes	Coal
24.	China Merchants Securities	150.9	23.37	No	No	Brokerage
25.	Tianjin Infrastructure Investment Group	147.4	22.83	Yes	No	Capital Goods
26.	Huatai Securities	141.7	21.94	No	Yes	Brokerage
27.	China Datang	115.7	17.91	Yes	No	Power
28.	China Three Gorges	115.0	17.81	Yes	No	Power
29.	GF Securities	113.9	17.64	No	Yes	Brokerage
30.	China Bohai Bank	113.0	17.49	No	No	Banking
Total Top 30 LCY Corporate Issuers		10,904.2	1,688.7			
Total LCY Corporate Bonds		38,206.6	5,917.0			
Top 30 as % of Total LCY Corporate Bonds		28.5%	28.5%			

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

Notes:

1. Data as of 30 June 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 Second Quarter of 2021

Corporate Issuers	Coupon Rate (%)	Issued Amount (CNY billion)
China Securities Finance^a		
1-year bond	3.90	20.0
1-year bond	3.88	20.0
1-year bond	3.85	20.0
1-year bond	3.93	20.0
1-year bond	3.87	20.0
Bank of Communications		
1-year bond	3.40	40.0
Perpetual bond	4.06	41.5
Industrial and Commercial Bank		
Perpetual Bond	4.04	70.0
China Everbright Bank^a		
1-year bond	2.82	3.0
1-year bond	2.82	8.0
1-year bond	2.86	4.0
1-year bond	2.84	3.0
1-year bond	2.80	2.5
1-year bond	2.98	6.0
2-year bond	2.88	3.0
2-year bond	2.93	5.0
2-year bond	3.09	3.0
2-year bond	3.13	6.0
2-year bond	3.23	4.5
2-year bond	3.20	4.5
China State Railway Group^a		
10-year bond	3.54	5.0
10-year bond	3.54	5.0
10-year bond	3.54	5.0
20-year bond	3.80	5.0
20-year bond	3.84	5.0
20-year bond	3.80	5.0
20-year bond	3.80	5.0

CNY = Chinese yuan.

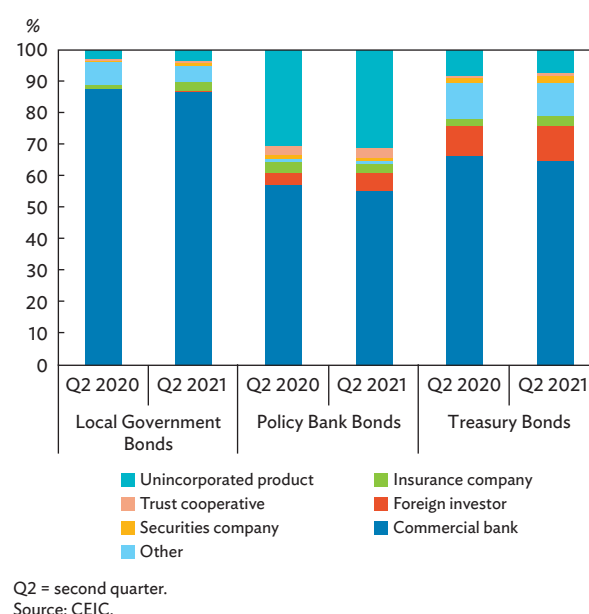
^a Multiple issuance of the same tenor indicates issuance on different dates.

Source: Based on data from Bloomberg LP.

Policy, Institutional, and Regulatory Developments

People's Bank of China Reduces Reserve Requirement Ratios

Effective 15 July, the PBOC reduced the reserve requirement ratio of financial institutions by 50 bps (excluding institutions with an existing 5% reserve requirement ratio). The PBOC estimated that the move would reduce the weighted average reserve requirement ratios of financial institutions to 8.9%. The PBOC's stated goal was to reduce borrowing costs and support the economy.

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 Second Quarter of 2021**

Interest Rate Swap Benchmarks	Notional Amount (CNY billion)	Share of Total Notional Amount (%)	Growth Rate (%)
		Q2 2021	q-o-q
7-Day Repo Rate	4,847.3	85.2	1.1
7-Day Repo Rate (Deposit Institutions)	2.2	0.04	8.9
Overnight SHIBOR	10.3	0.2	0.5
3-Month SHIBOR	800.1	14.1	1.2
1-Year Lending Rate	12.0	0.2	0.5
5-Year Lending Rate	1.9	0.0	0.3
10-Year Treasury Yield	5.3	0.1	0.5
China Development Bank 10-Year Bond Yield	4.8	0.1	0.4
10-Year Bond Yield/10-Year Government Bond Yield	4.5	0.1	0.4
3-Year AAA Short-Term Notes/ Government Debt	0.1	0.001	0.3
Total	5,688.4	100.0	6.1

CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q2 = second quarter,

Repo = repurchase, SHIBOR = Shanghai Interbank Offered Rate.

Note: Growth rate computed based on notional amounts.

Sources: AsianBondsOnline and ChinaMoney.