ASEAN+3 BOND MARKET GUIDE 2016

HONG KONG, CHINA

ASIAN DEVELOPMENT BANK

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ADB recognizes “China” as the People’s Republic of China; “Hong Kong” as Hong Kong, China; and “Korea” as the Republic of Korea.

Contents

Tables and Figures

Tables

Figures

Foreword

The Asian Development Bank is working closely with the Association of Southeast Asian Nations (ASEAN) and the People's Republic of China, Japan, and the Republic of Korea—collectively known as ASEAN+3—to develop local currency bond markets and facilitate regional bond market integration under the Asian Bond Markets Initiative in order to strengthen the resilience of the region's financial systems.

Thanks to the efforts of member governments, local currency bond markets in the region have grown rapidly, with the total outstanding amount of bonds reaching more than USD8 trillion in 2015. However, financial markets are still relatively less integrated than the region's trade linkages and supply chain networks. If efforts toward harmonization and integration were to succeed, financial markets in ASEAN+3 would benefit from much larger economies of scale and increased efficiencies, while vast savings could be utilized for the region's enormous investment needs. Therefore, the strengthening of bond markets should be pursued in line with a common understanding of what needs to be harmonized and integrated from the early stages of market development.

The ASEAN+3 Bond Market Forum (ABMF) was established with the endorsement of the ASEAN+3 Finance Ministers in 2010 as a common platform to foster the standardization of market practices and harmonization of regulations relating to cross-border bond transactions in the region. As an initial step, ABMF published the ASEAN+3 Bond Market Guide in 2012, which was welcomed as the first official information source offering a comprehensive explanation of the region's bond markets.

Since publication of the ASEAN+3 Bond Market Guide, bond markets in the region have continued to develop. ABMF recognizes the need for revisions to the guide to reflect these changes, though it is never an easy task to keep up with rapid changes in the markets. This report is an outcome of the strong support and kind contributions of ABMF members and experts, particularly from Hong Kong, China. The report should be recognized as a collective good to support bond market development among ASEAN+3 members. It is our hope that the revised ASEAN+3 Bond Market Guide will facilitate further development of the region's bond markets and contribute to increased intraregional bond transactions.

Ma. Carmela D. Locsin
Director General
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Acknowledgments

The Hong Kong, China Bond Market Guide was first published in 2012 as the initial output of Phase 1 of the ASEAN+3 Bond Market Forum (ABMF).[1] Across the region, domestic bond markets, including the Hong Kong bond market, have experienced tremendous development over the past 4 years. Now in Phase 3, ABMF would like to share in the public domain information on these developments by publishing an update to the Hong Kong, China Bond Market Guide.

The ABMF Sub-Forum 1 team—comprising Satoru Yamadera (Principal Financial Sector Specialist, Asian Development Bank, Sustainable Development and Climate Change Department) and Asian Development Bank consultants Shigehito Inukai and Matthias Schmidt—would like to stress the significance and magnitude of the contributions made by ABMF national members and national experts for Hong Kong, China, including Bank of China (Hong Kong) and the Hong Kong Monetary Authority. These institutions were extremely generous with their time to accommodate market visit meetings, discussions, and follow-up. They have also reviewed and provided inputs on the draft Hong Kong, China Bond Market Guide over the course of ABMF Phase 3.

The Hong Kong, China Bond Market Guide would not be complete without the support of the Hong Kong Securities and Futures Commission and the Hong Kong Exchanges and Clearing Limited, whose staff on numerous occasions patiently detailed or clarified the roles and features of their institutions in the bond market.

The ABMF team also would like to express its thanks to the ABMF international experts based in Hong Kong, China, specifically the Clearstream Banking S.A. Representative Office, Euroclear Bank Hong Kong Branch, HSBC, and JP Morgan Chase Bank N.A., who contributed significantly to the discussions and updates on developments in the Hong Kong bond market, as well as toward efforts to implement the ASEAN+3 Multi-Currency Bond Issuance Framework in Hong Kong, China. Thanks also go to the financial services partners of law firm Slaughter and May for being generous with their time and offering their firm's perspective on the Hong Kong bond market.

No part of this report represents the official views or opinions of any institution that participated in this activity as an ABMF member or expert. The ABMF Sub-Forum 1 team bears sole responsibility for the contents of this report.

November 2016

ASEAN+3 Bond Market Forum

[1] ASEAN+3 refers to the 10 members of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

Abbreviations

ABMF	ASEAN+3 Bond Market Forum (www.asean3abmf.adb.org)
ADB	Asian Development Bank (http://www.adb.org)
AMBIF	ASEAN+3 Multi-Currency Bond Issuance Framework
ASEAN	Association of Southeast Asian Nations (www.asean.org)
ASEAN+3	Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea
ATS	automated trading services
CCASS	Central Clearing and Settlement System (of HKEX)
CECF	Commodity Exchange Compensation Fund
CHATS	Clearing House Automated Transfer System
CMU	Central Moneymarkets Unit (of HKMA)
CNH	Offshore Chinese renminbi
CNY	Chinese renminbi (ISO code)
CO	Companies Ordinance (Cap. 622)
CPSS	Committee on Payment and Settlement Systems
CRA	credit rating agency
CWUMPO	Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32)
EFB	Exchange Fund Bill
EFBN	Exchange Fund Bill and Note
EFN	Exchange Fund Note
GMRA	Global Master Repurchase Agreement (available at www.icmagroup.org/)
HCMA	Hong Kong Capital Markets Association (http://www.hkcma.org)
HKD	Hong Kong dollar (ISO Code)
HKEX	Hong Kong Exchanges and Clearing Limited (http://www.hkex.com.hk)
HKFE	Hong Kong Futures Exchange Limited
HKICL	Hong Kong Interbank Clearing Limited (https://www.hkicl.com.hk)
HKMA	Hong Kong Monetary Authority (http://www.hkma.gov.hk)
HKSAR	Hong Kong Special Administrative Region
HKSCC	Hong Kong Securities Clearing Company Limited
ICF	Investor Compensation Fund
ICSD	international central securities depositories
IOSCO	International Organization of Securities Commissions
MDB	multilateral development bank
MRF	Mutual Recognition of Funds
MTN	medium-term note
OMD-C	Orion Market Data Platform for Securities Market
OTC	over-the-counter
OTC Clear	OTC Clearing Hong Kong Limited
PRC	People's Republic of China
RTGS SEHK	Real-time gross settlement The Stock Exchange of Hong Kong Limited
SF1	Sub-Forum 1 of ABMF
SFC	Securities and Futures Commission (www.sfc.hk)
SFO	Securities and Futures Ordinance
SRO	self-regulatory organization
UECF	Unified Exchange Compensation Fund
USD	United States dollar

USD1 = HKD7.755 as of 30 September 2016 (HKMA published rate).

I

Overview

A. Introduction

The bond market in Hong Kong, China has for some time been a significant market place for issuers and investors in both domestic and foreign currencies. The range of product offerings, open access for issuers and investors (both domestic and international), and the increasing significance of offshore Chinese renminbi bond issuances make the Hong Kong bond market one of the most frequented bond markets in Asia.

Public sector bonds come in the form of (i) government bonds, (ii) Exchange Fund Bills and Notes (EFBNs) issued by the Hong Kong Monetary Authority (HKMA); (iii) bonds issued by statutory bodies (e.g., Airport Authority Hong Kong and Hong Kong Housing Authority); and (iv) bonds issued by government-related corporations (e.g., Bauhinia Mortgage-Backed Securities Limited, Hong Kong Mortgage Corporation, and Hong Kong Link 2004 Limited).

The Central Moneymarkets Unit (CMU) was set up primarily to provide computerized clearing and settlement facilities for EFBNs, which provide benchmark yields that guide private debt pricing. In December 1993, the HKMA extended the service to other Hong Kong dollar debt securities. Since December 1994, the CMU has been linked to international clearing systems such as Euroclear, which has helped promote Hong Kong dollar debt securities to overseas issuers and investors. The CMU is also available for foreign-currency-denominated debt, including Australian dollars, Chinese renminbi, euros, New Zealand dollars, Singapore dollars, and US dollars.

In December 1996, an interface between the CMU and the real-time gross settlement (RTGS) interbank payment system was established. This enables the CMU system to provide its members with real-time and end-of-day delivery-versus-payment services.

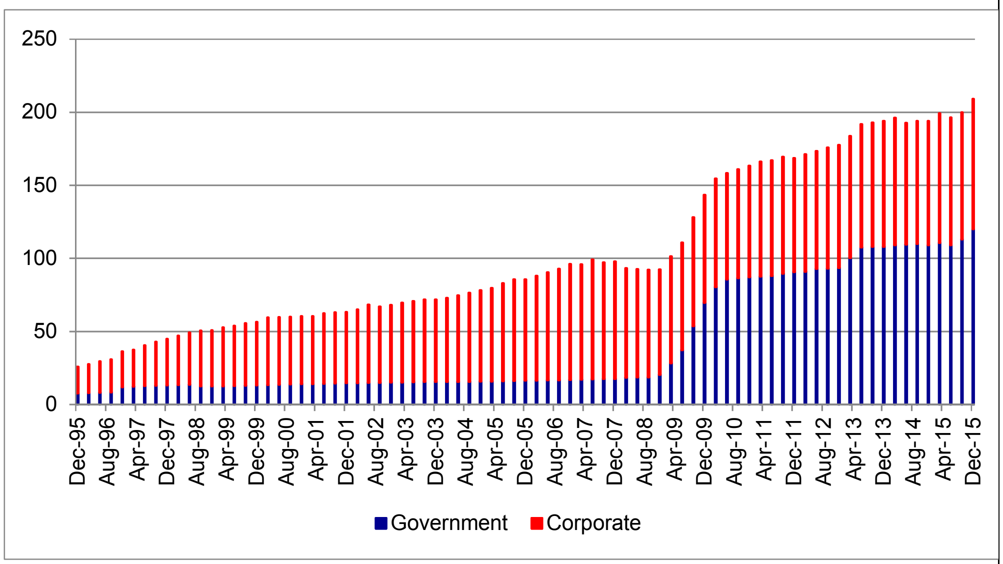
Bond trading takes place mostly through over-the-counter (OTC) markets. However, some bonds are also listed and may be traded on the securities market of Hong Kong Exchanges and Clearing Limited (HKEX), which is the holding company that owns The Stock Exchange of Hong Kong Limited (SEHK), which operates the stock exchange in Hong Kong, China.

Hong Kong, China is a preferred location within Asia for bond issues by foreign and domestic corporations—as well as supranational borrowers—because of the ease with which investors can access the market and international clearing systems. In addition, a wide range of asset classes is available for securitization. The two main securitized asset classes are (i) residential and commercial mortgages and (ii) HKMA claims on central governments and central banks. The Hong Kong Mortgage Corporation, which was established by the HKMA, and Hong Kong Link 2004 Limited were set up to facilitate securitization of residential mortgages and toll facilities, respectively.

To promote the development of the local debt market, authorities introduced a number of new products, expanded and improved market infrastructure, and provided a tax and regulatory environment conducive to market development.

In the Hong Kong dollar debt market, the total issuance volume of Hong Kong dollar debt instruments continued to grow to a record level in 2015 (Figure 1.1). Further measures were implemented by the Hong Kong Special Administrative Region (HKSAR) to support the development of the local bond market under the Government Bond Programme, including the issuance of a second *sukuk* (Islamic bond) in June and the debut of a 15-year Government Bond in July.

Figure 1.1: Local Currency Bonds Outstanding in Hong Kong, China
(USD billion)



Note: Data as of 31 December 2015 and include bonds issued by nonresidents.
Source: *AsianBondsOnline*. Hong Kong, China Bond Market.
https://asianbondsonline.adb.org/hongkong/data/bondmarket.php?code=LCY_Bond_Market_USD

Overseas issuers continued to tap the Hong Kong dollar market in 2015, with issuance volume rising by 16.5% from 2014. Overseas corporates could also expand their investor base and broaden funding sources through issuance in Hong Kong, China, thereby strengthening their funding structure.

Starting in 2015, the tenors of bonds issued under the EFBN Programme and the Government Bond Programme were streamlined. The HKMA now only issues new EFBNs for tenors of 2 years or less, and new Government Bonds for tenors of 3 years or more. After the streamlining, there is now a unitary benchmark yield curve representing the long-run credit standing of the Government of the HKSAR of the People's Republic of China (PRC), with EFBNs providing the benchmark yield for 2 years or less and Government Bonds providing the benchmark yield for 3 years or more. A unitary benchmark yield curve provides a better reference for issuers in pricing their Hong Kong dollar issues.

The government also issued a HKD10 billion inflation-linked bond, or iBond, in 2015. It was the fifth-consecutive series of iBonds since 2011. The number of valid applications was a record-high 597,895, with total subscriptions of nearly HKD36 billion. According to market sources, first-time investors have made up between 9% and 15% of the successful subscribers in the past five issuances. The iBond issuances not only provided an additional choice of investment to the public, but also sustained the growth momentum of the local bond market through enhancing public awareness of, and interest in, bond investments. The iBond issuance successfully broadened the investor base of the local bond market, encouraging more issuers to consider tapping the market through retail issuance.

Through the implementation of the Government Bond Programme, the HKMA continues to support the development of the Hong Kong dollar debt market. Ongoing communication with market participants enhances the competitiveness of the local market as a fund-raising platform. With a view to supporting the development of Islamic finance in the local market, the government will launch another *sukuk* when market conditions are favorable.[2]

The regulatory environment is also conducive to the implementation of the proposed ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF) developed by the ASEAN+3 Bond Market Forum (ABMF) under the guidance of the Asian Development Bank (ADB). The key features of the Hong Kong bond market are further enhanced by the acceptance of governing laws other than those of Hong Kong, China for professional bond and note issuances, and documentation and disclosure standards close to those of international markets. Further details on AMBIF can be found in Chapters IX and X.

For more information on recent initiatives and developments with relevance for the Hong Kong bond market, kindly also refer to Chapters IX and X.

[2] Selected statements adopted from Hong Kong Monetary Authority. *Quarterly Bulletin March 2016.* Hong Kong, China.

II

Legal and Regulatory Framework

A. Legal Tradition

The legal system in Hong Kong, China is similar to the common law system used in the United Kingdom and is defined by the Basic Law of Hong Kong, in which the common law is supplemented by local legislation.

B. English Translation

The Government of the Hong Kong Special Administrative Region of the PRC, its policy bodies, and regulatory authorities all officially publish laws, regulations, and notices in both traditional Chinese and English. As such, an English translation does not apply.

C. Legislative Structure

Hong Kong, China features a multitiered legislative structure to govern the securities markets, guided by the Basic Law of Hong Kong.

[1st tier] Basic Law of Hong Kong
- [2nd tier] Ordinances and subsidiary legislation (key legislation for the securities market)
  - [3rd tier] Guidance materials, including codes and guidelines issued under key legislation
    - [4th tier] Nonlegislative rules and guidance materials issued by market institutions, and frequently asked questions (FAQs) and circulars issued by regulators)

Table 2.1 illustrates the legislative structure mentioned above by giving significant examples of relevant securities market legislation for each of the individual tiers.

"Key legislation" is the summary term for those laws specifically aimed at a particular market, such as the securities market. These laws establish and govern the securities market, including the bond market, its institutions, and participants. These laws are enacted by the Legislative Council and take effect upon publication in the Government of the Hong Kong Special Administrative Region Gazette, unless a provision is made for them to commence on another day. The Securities and Futures Ordinance (SFO) (Cap. 571 of the Laws of Hong Kong), the Companies (Winding Up and Miscellaneous Provisions) Ordinance (CWUMPO) (Cap. 32 of the Laws of Hong Kong) and the Companies Ordinance (CO) (Cap. 622 of the Laws of Hong Kong) represent the key primary legislation for the Hong Kong bond market.

Table 2.1: Examples of Securities Market Legislation by Legislative Tier

Legislative Tier	Content or Significant Examples
Basic Law of Hong Kong	Principles, Rights, and Obligations
Ordinances and subsidiary legislation (key legislation, as amended)	• Securities and Futures Ordinance (Cap. 571) and subsidiary legislation made under it • Public Finance Ordinance (Cap. 2) • Companies Ordinance (Cap. 622) • Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) • Trustee Ordinance (Cap. 29) • Exchange Fund Ordinance (Cap. 66) • Banking Ordinance (Cap. 155) • Payment Systems and Stored Value Facilities Ordinance (Cap. 584) • Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) (Amendment) Ordinance 2013
Codes and guidelines	• Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (issued by the SFC) • Code of Conduct for Persons Providing Credit Rating Services (issued by the SFC) • Guidelines on Use of Offer Awareness and Summary Disclosure Materials in Offerings of Shares and Debentures under the Companies Ordinance (Cap. 32) (SFC) • Guideline No. 6.2.2B Recognized Credit Rating Agencies for Regulatory Purposes (issued by the HKMA)
Nonlegislative rules and guidance materials (e.g., circulars and FAQs**)**	• Circular to Licensed Corporations on Distribution of bonds listed under Chapter 37 of the Main Board Listing Rules and local unlisted private placement bonds (issued by the SFC) • Main Board Listing Rules (issued by SEHK) • Trading Rules (issued by SEHK)

HKMA = Hong Kong Monetary Authority, SEHK = The Stock Exchange of Hong Kong Limited, SFC = Securities and Futures Commission.
Source: Compiled by ADB Consultants for SF1 and based on publicly available information.

Codes and guidelines are issued by the regulatory authorities charged with the overall supervision and governance of the securities and banking system, which are the Securities and Futures Commission (SFC) and the HKMA. The SFC issues codes of conduct under section 169 of the SFO for the purpose of giving guidance relating to the practices and standards with which intermediaries and their representatives are expected to comply. The SFC also issues codes and guidelines under section 399 to provide guidance in relation to the exercise of its statutory functions and for the furtherance of its regulatory objectives.[3] The HKMA issues guidelines to govern authorized financial institutions and their activities, and on specific subjects concerning the market.

Nonlegislative rules and guidance materials are issued by the regulatory authorities (HKMA and SFC) and market institutions (e.g., SEHK) for the activities and market participants under their respective purviews. The nonlegislative rules of the market institutions provide for the operation of the market or facilities that the market

[3] Securities and Futures Commission. Codes and Guidelines. http://en-rules.sfc.hk

institutions operate. The regulatory authorities' guidance materials (e.g., circulars and FAQs) remind industry participants of the relevant requirements and help them understand specific regulatory issues.

D. Hong Kong Bond Market Regulatory Structure

The bond market in Hong Kong, China, is governed by the relevant laws, codes, guidelines, and circulars issued, administered, and enforced by the SFC, HKMA, as well as the nonlegislative rules issued by the market institutions owned by HKEX. There is no separate self-regulatory organization (SRO) governing the participants of the bond market in Hong Kong, China.

1. Securities and Futures Commission

The principal regulator of Hong Kong's securities market is the SFC, which is an independent statutory body established in 1989 by the Securities and Futures Commission Ordinance (SFCO). The SFCO and nine other securities and futures-related ordinances were consolidated into the SFO, which came into effect on 1 April 2003.

The SFC is responsible for administering the laws governing the securities and futures market in Hong Kong. Its regulatory objectives as set out in the SFO include

i. maintaining and promoting the fairness, efficiency, competitiveness, transparency, and orderliness of the securities and futures industry;

ii. promoting understanding by the public of financial services including the operation and functioning of the securities and futures industry;

iii. providing protection for members of the public investing in or holding financial products;

iv. minimizing crime and misconduct in the securities and futures industry;

v. reducing systemic risks in the securities and futures industry; and

vi. assisting the Financial Secretary in maintaining the financial stability of Hong Kong, China by taking appropriate steps in relation to the securities and futures industry.

In addition to regulating market institutions owned by the HKEX (see below for more information), listed companies,[4] and the Federation of Share Registrars,[5] the SFC oversees corporations and banks (known as Licensed Corporations and Registered Institutions), and the individuals carrying out the following regulated activities as set out in Schedule 5 to the SFO; those with direct relevance to the bond market are indicated by an asterisk:

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[4] While the SFC administers the requirements relating to the disclosure of inside information under Part XIVA of the SFO, vets listing application materials under the dual-filing regime, administers the Takeovers Code, and carries out surveillance of listed companies for limited purposes, SEHK remains the frontline regulator of listed companies for most matters.

[5] Currently, the SFC does not directly regulate (or approve) share registrars. Instead, it approves the Federation of Share Registrars whose members shall be approved share registrars and are subject to the requirements of the Code of Conduct for Share Registrars. For more details, see Part 4 of the Stock Market Listing Rules (Cap. 571V). Section 101AAO(2)(g) and (h) of the Securities and Futures and Companies Legislation (Uncertificated Securities Market Amendment) Ordinance 2015, which has yet to commence, will enable the SFC to make rules to authorize and directly regulate share registrars.

(i) dealing in securities,*
(ii) dealing in futures contracts,
(iii) leveraged foreign exchange trading,
(iv) advising on securities,*
(v) advising on futures contracts,
(vi) advising on corporate finance,*
(vii) providing automated trading services,*
(viii) securities margin financing,*
(ix) asset management,* and
(x) providing credit rating services.*

Furthermore, the SFO, the CWUMPO, and the CO empower the SFC to supervise and regulate the following:

i. the issuance of prospectuses offering shares in or debentures of a company to the public, and the publication of advertisements concerning such prospectuses (regulated under Parts II and XII of the CWUMPO);

ii. the buy-back by a corporation of its own shares and the giving of financial assistance by a corporation for the acquisition of its own shares (regulated under Part 5 of the CO);

iii. recognized exchange companies (SEHK and Hong Kong Futures Exchange Limited [HKFE]) owned by HKEX (regulated under Part III of the SFO);

iv. recognized exchange controllers (HKEX) (regulated under Part III of the SFO);

v. recognized clearinghouses (Hong Kong Securities Clearing Company Limited [HKSCC], HKFE Clearing Corporation Limited [HKCC], SEHK Options Clearing House Limited, and the OTC Clearing Hong Kong Limited [OTC Clear]) (regulated under Part III of the SFO);

vi. recognized investor compensation company (Investor Compensation Company Limited) (regulated under Part III of the SFO); and

vii. persons authorized by the SFC to provide automated trading services (ATS) (regulated under Part III of the SFO).

By law, any person carrying on a business in a regulated activity (e.g., dealing in securities or in futures contracts) in Hong Kong, China has to be licensed by or registered with the SFC.

2. Hong Kong Monetary Authority

The HKMA is Hong Kong, China's de facto central bank. The HKMA was established on 1 April 1993 by merging the Office of the Exchange Fund with the Office of the Commissioner of Banking. Its main functions and responsibilities are governed by the Exchange Fund Ordinance and the Banking Ordinance, and it reports to the Financial Secretary.

The HKMA is the government authority in Hong Kong, China responsible for maintaining monetary and banking stability. Its main functions are

- maintaining currency stability within the framework of the Linked Exchange Rate System;

- promoting the stability and integrity of the financial system, including the banking system;

- helping maintain Hong Kong, China's status as an international financial center, including the maintenance and development of Hong Kong's financial infrastructure; and

- managing the Exchange Fund.

The HKMA solely operates the CMU, which provides clearing, settlement, and depository services for both HKD-denominated and international debt securities available for trading in the Hong Kong bond market. The HKMA, through the RMB Liquidity Facility, also provides liquidity support to Authorized Institutions participating in renminbi business in Hong Kong, China.[6]

The HKMA has developed external infrastructure linkages with other regional and international central securities depositories (ICSDs) to settle securities lodged with the CMU.

The HKMA is also the front-line regulator to supervise the regulated activities (as defined under the SFO) conducted by Registered Institutions (which includes banks) and their individuals who are engaged in such activities.

Hong Kong Monetary Authority Guidelines and Circulars

To organize, direct, and govern the banking industry and the bond market, the HKMA issues guidelines and circulars, and prescribes codes of conduct for the market participants under its remit. The guidelines and circulars cover particular market segments, such as the CMU or the repo business, types of instruments (e.g., debt securities or derivatives), and other specific subjects (e.g., disclosure). Guidelines and circulars are also issued to interpret and expand on laws and regulations, including but not limited to the operational aspects of the CMU and its participants.

Hong Kong, China as an International Financial Center

In support of the policies for the further development of Hong Kong, China as an international financial center and maintenance of the stability and integrity of its financial system, the HKMA, in cooperation with other relevant authorities and organizations as appropriate, is responsible for

- promoting confidence in Hong Kong, China's monetary and financial systems through active participation in international financial and central banking forums;
- promoting market development initiatives that help strengthen the international competitiveness of Hong Kong, China's financial services, including those on the promotion of Hong Kong, China's development as the global offshore renminbi business hub ; and
- maintenance and development of Hong Kong, China's financial infrastructure.

A specific function of the HKMA under the international financial center remit is the development of the debt market in Hong Kong, China. The HKMA addresses this function through what is referred to as Important Policy Initiatives Affecting the EFBN

[6] See http://www.hkma.gov.hk/eng/key-functions/monetary-stability/liquidity-support-to-banks.shtml

Programme and other Hong Kong Dollar Debt Instruments, which include the following:[7]

- **Seven technical measures to strengthen the currency board arrangements**. The seven measures to strengthen the currency board arrangements introduced on 7 September 1998 provide that no new EFBNs are issued except when there are significant inflows of funds. This arrangement ensures that new issues of EFBNs are fully backed by foreign reserves in accordance with the discipline of the currency board system. Outstanding issues of EFBNs, which are already backed by foreign reserves, are rolled over when they mature.

- **New measures to fine tune currency board arrangements.** Since 1 April 1999, new EFBNs are issued in line with the interest payments on outstanding EFBNs. The measure is consistent with the currency board principle that interest payments on EFBNs are backed by interest income on the US dollar backing assets. This measure allows the amount of EFBNs outstanding to grow gradually and is conducive to the development of the local debt market.

- **Streamlining Issuance of Exchange Fund Bills and Notes and Government Bonds**. The issuance of EFBNs and Government Bonds has been streamlined to minimize overlap in longer tenors. Starting in January 2015, the HKMA stopped new issuance of Exchange Fund Bills (EFBs) with tenors of 3 years or more, while 2-year Exchange Fund Note (EFN) issuance continues. At the same time, new issuance of 2-year Government Bonds has ceased, while issuance of Government Bonds with tenors of 3 years or more continues.

3. Hong Kong Exchanges and Clearing Limited

HKEX is a leading global operator of exchanges and clearinghouses based in Hong Kong, China, and one of the world's largest exchange groups by market capitalization. HKEX operates the securities and derivatives markets (and their related clearinghouses) and is the frontline regulator of listed companies in Hong Kong, China.

In Hong Kong, China, HKEX regulates listed issuers and administers listing, trading, and clearing rules. It also provides services, primarily at the wholesale level, to participants and users of its exchanges and clearinghouses, including issuers and intermediaries (e.g., investment banks or sponsors, securities and derivatives brokers, custodian banks, and information vendors), which service investors directly. These services comprise trading, clearing, and settlement; deposit and nominee services and information services across multiple products and asset classes.

HKEX operates the only recognized stock market and futures market in Hong Kong, China through its wholly owned subsidiaries, SEHK and the Hong Kong Futures Exchange Limited. HKEX also operates four clearinghouses, which are the only recognized clearinghouses in Hong Kong, including HKSCC and OTC Clear. HKSCC provides integrated clearing, settlement, depository, and nominee activities to their participants, while OTC Clear provides clearing and settlement services for OTC derivative transactions. OTC Clear currently provides clearing of inter-dealer interest rate swaps, nondeliverable forwards, and cross-currency swaps. HKEX also provides market data through its data dissemination entity, HKEX Information Services Limited.

[7] For further information on HKMA policy initiatives, please see http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/debt-market-development/policy-initiatives-affecting-efbn-programme-other-hk-dollar-debt-instrument.shtml

The SEHK, a wholly owned subsidiary of HKEX, is a recognized exchange company under the SFO. It operates the stock market in Hong Kong, China and is the primary regulator of SEHK Participants with respect to trading matters (see Rules of the Exchange, which are also known as the Trading Rules) and the frontline regulator of companies listed on the Main Board and the Growth Enterprise Market of SEHK, as well as for the listing of debt securities.[8]

In addition, the Trading Rules require any person who wishes to trade on or through the SEHK's facilities to hold a Trading Right. SEHK Trading Rights are issued at a fee and in accordance with the procedures set out in their respective rules. It is also necessary for the person to be registered as a participant of the relevant exchange (Exchange Participant) in accordance with its rules, including those requiring compliance with all relevant legal and regulatory requirements.

Besides the Main Board Listing Rules and the Trading Rules, SEHK may also issue guidance materials on specific topics. For details on listing- or trading-related rules and guidance, please refer to Sections I. and J. in this chapter, respectively.

HKEX is committed to performing its public duty to promote orderly and fair markets, and ensure that risks are managed prudently, consistent with the public interest in general and the interests of the investing public in particular. HKEX is also committed to working closely with the principal regulator of Hong Kong, China's securities and derivatives markets, the SFC.

E. Regulatory Framework for Debt Securities

The regulatory framework for debt securities in Hong Kong, China is very much influenced by the general regulatory approach that business may be conducted unless it contravenes the Laws of Hong Kong (or regulatory requirements made under such laws). As such, few limitations exist in the bond market, most notably only those with an emphasis for the protection of retail investors.

Hence, one key maxim for the bond market is that all relevant parties for a bond or note issuance may participate freely in the Hong Kong bond market, and transactions in such bonds and notes may be effected, subject to the relevant licensing requirements (see Section I in this chapter for more details). Licensing or registration of market intermediaries (including Licensed Corporations and Registered Institutions) under Part V of the SFO is administered by the SFC and the HKMA (as the case may be) and membership in the CMU is granted by the HKMA as a requirement to settle bond and note transactions in the market. Both market intermediaries and CMU members are subject to certain requirements including fit and proper criteria.

The SFC applies the provisions of the SFO and its related subsidiary legislations, as well as the SFC's codes and guidelines to regulate the regulated activities conducted by market intermediaries. For CMU market intermediaries that are Registered Institutions under the supervision of the HKMA as their front-line regulator, they are also required to observe the CMU Membership Rules and Guidelines issued by the HKMA. In addition, the HKMA also regulates a number of activities that are associated with its supervision of the CMU activities, including the practices for repurchase agreements (repo), short-selling, and securities lending. In turn, the SFC also has requirements relating to short selling and securities borrowing and lending (see sections 170 to 172 of the SFO and Cap. 571R).

[8] See Chapter 37 of the Main Board Listing Rules.

If debt securities are not offered to the public, issuers do not need to comply with the prospectus-related requirements in the CWUMPO or the authorization requirement in section 103 of the SFO. In addition, unless otherwise stated in the prospectus, offer document, term sheet, or similar such document, there is no restriction on the types of investors who are eligible for investing in particular debt instruments provided that the requirements in the CWUMPO and the SFO are complied with. At the same time, certain bonds that are listed on SEHK are only accessible to professional investors[9] (as defined in the SFO), constituting the professional bonds segment in the bond market. Offers of debt securities to professional investors must be clearly identified as such.

The offer of debt securities is regulated in the CWUMPO.[10] Registration of prospectus offering unlisted debt securities to the public is subject to the SFC's approval.[11] Public offers of debt securities (which do not fall within the definition of structured products[12] under the SFO) by companies are governed by Part II (in case of a company incorporated in Hong Kong) and Part XII (in case of a company incorporated outside Hong Kong) of the CWUMPO. Private placements and offers to professional investors are exempted from the public offer regimes under the CWUMPO (see Section F). The processes particularly relevant for the application for approval and reporting[13] for debt securities are explained in greater detail in the following section.

For bonds to be listed on the Main Board of SEHK, bond issuers should observe, among others, the Main Board Listing Rules which set out the qualifications for listing, application procedures and requirements, and listing documents and arrangements. For details, please refer to Chapters 22–37 of the Main Board Listing Rules (which can be accessed at http://www.HKEX.com.hk/eng/rulesreg/listrules/mbrules/vol1_4.htm).

Issuers of bonds to be listed on SEHK should observe the Trading Rules promulgated by HKEX (http://www.HKEX.com.hk/eng/rulesreg/traderules/tradingrules.htm). Issuers incorporated in Hong Kong, China and those incorporated overseas should also observe the requirements, among others, for the allotment of debentures to be listed set out in sections 44B and 342B of the CWUMPO, respectively.[14]

F. Debt Securities Issuance Regulatory Processes

Public offers for corporate bond and note issuances in Hong Kong, China require the approval of the SFC. Bond or note issuances by corporate issuers aimed at professional investors in the Hong Kong bond market do not require an approval from or notice to regulatory authorities. If a listing is sought, SEHK's approval is required. Following issuance, all debt securities to be settled in the Hong Kong bond market need to be admitted to the CMU operated by the HKMA, and listed debt securities may be admitted to the Central Clearing and Settlement System (CCASS) operated by

[9] According to paragraph 37.58 of the Main Board Listing Rules, these exclude investors prescribed by the rules made under section 397 of the SFO. However, SEHK may grant waivers to allow such investors to participate in the professional investors-only debt issues.

[10] The offer of debt securities is also regulated in section 175 of the SFO. Where an intermediary (licensed for Type 1, 4, or 6 RA) relies on the carve-out in section 103(2)(a) to issue a document (containing an offer of unlisted debentures) without SFC authorization, requirements set out in section 175 must be complied with unless any exemption in section 175(5) applies.

[11] For listed debt securities, the SFC has transferred its authorization function under section 38D(3) and (5) and section 342C(3) and (5) of the CWUMPO to SEHK by virtue of the Transfer of Functions-Stock Exchange Company Order (Cap. 571AE).

[12] The definition of "structured products" is set out in section 1A of Schedule 1 to the SFO.

[13] OTC trades of unlisted bonds do not need to be reported to SEHK. Off-market trades of listed bonds are only required to be reported to SEHK if they are executed by or between Exchange Participants (see Chapter 5 of the SEHK Trading Rules). An authorized ATS provider effecting trades (of listed or unlisted bonds) on its platform may (on a case-by-case basis) be required by the SFC to periodically report the trade statistics to the SFC.

[14] See http://www.hklii.hk/eng/hk/legis/ord/32/s44b.html, http://www.hklii.hk/eng/hk/legis/ord/32/s342b.html

HKSCC.[15] A subsequent listing of bonds and notes on SEHK would be subject to a separate listing approval.

1. Regulatory Processes by Issuer Type

Table 2.2 provides an overview of these regulatory processes by corporate issuer type and identifies which regulatory authority or market institution will be involved. In order to make the issuance processes by issuer type more comparable across ASEAN+3 markets, the table features common issuer type distinctions that are evident in regional markets. Not all markets will distinguish all such issuer types or prescribe approvals. Sovereign issuers are typically exempt from corporate issuance approvals but, at the same time, may be subject to different regulatory processes.

Table 2.2: Authorities Involved in Regulatory Processes by Issuer Type

<table>
<tr><th>Type of Issuer</th><th>SFC (public offers only)</th><th>HKEX</th></tr>
<tr><td>Resident issuer</td><td rowspan="10">Authorization by the SFC of the registration of prospectus with the Registrar of Companies required #</td><td rowspan="10">Listing eligibility follows criteria and related provisions in the SEHK Listing Rules %</td></tr>
<tr><td>Resident nonfinancial institution</td></tr>
<tr><td>Resident financial institution</td></tr>
<tr><td>Resident issuing FCY-denominated bonds and notes</td></tr>
<tr><td>Nonresident issuer</td></tr>
<tr><td>Nonresident nonfinancial institution</td></tr>
<tr><td>Nonresident financial institution</td></tr>
<tr><td>Nonresident issuing FCY-denominated bonds and notes</td></tr>
</table>

The prospectus is required to be registered with the Registrar of Companies, not with the SFC. The SFC "authorises" its registration. For reference, see the wording in section 38D of the CWUMPO.
% The Listing Rules impose different requirements in respect of certain types of issuers. For example, see Chapter 31 (States), Chapter 32 (Supranationals), Chapter 33 (State Corporations) and Chapter 34 (Banks).
FCY = foreign currency, HKEX = Hong Kong Exchanges and Clearing Limited, SEHK = The Stock Exchange of Hong Kong Limited, SFC = Securities and Futures Commission.
Source: ADB Consultants for SF1.

While the regulatory processes related to the issuance of debt securities to the public in Hong Kong, China—including the issuance approval for public offers, admission of debt instruments into the CMU or CCASS, and listing process on HKEX—are principally the same for all types of corporate issuers, mineral companies, state corporations, and banks (when pursuing a listing approval) are subject to the provisions of Chapters 30, 33, and 34 of the Listing Rules, respectively.

Nonresident issuers may issue bonds and notes in Hong Kong, China in Hong Kong dollars, offshore Chinese Renminbi, and foreign currencies. There are no differences to the regulatory process based on the denomination of the bond or note

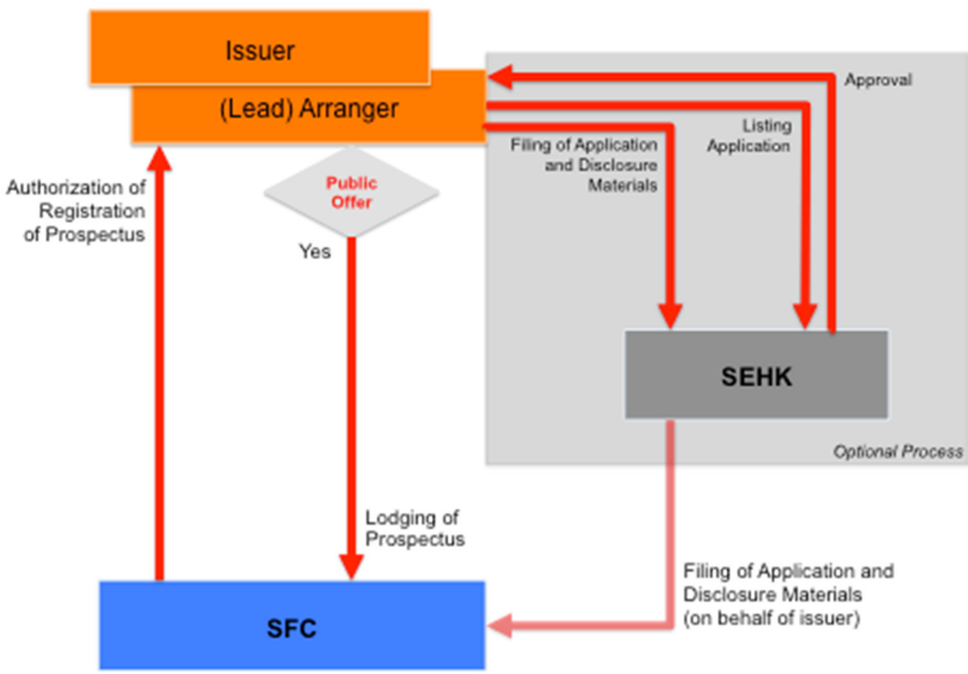
2. Regulatory Process Overview

In Hong Kong, China, issuers of proposed bonds and notes are not required to appoint an underwriter under the law; this is also the case with a public offer. At the same time, the use of one or more underwriters may be practical to reach the intended investor universe.

[15] Although it is common market practice for retail debt securities to be admitted into CCASS, there is no listing rule requirement for mandatory admission of retail debt securities into CCASS.

The technical terms used for the principal agent of an issuer in the Hong Kong bond market ranges from underwriter and arranger to listing agent or listing sponsor. For reasons of compatibility with the Bond Market Guides for other ASEAN+3 markets, the term arranger is used in illustrations in this document.

Figure 2.1: Regulatory Process Map—Bond and Note Issuance in Hong Kong, China



SEHK = The Stock Exchange of Hong Kong Limited, SFC = Securities and Futures Commission.
Notes: While the listing of debt securities is shown as an optional process, the listing approval from SEHK is not optional in the event a listing is applied for. In the event that a public bond is to be listed, SEHK will be vetting the prospectus.
Source: ADB Consultants for SF1.

An arranger (or underwriter) needs to be licensed as a Licensed Corporation or registered as a Registered Institution for such activities by the SFC. If the arranger (or underwriter) is an Authorized Institution under the Banking Ordinance, typically a bank, the arranger will be called a Registered Institution for the purposes of carrying out underwriting activities under the purview of the SFC.[16] If instead the arranger is not an Authorized Institution (e.g., broker or securities dealer), the arranger will be referred to as a Licensed Corporation.

If selected, an underwriter is appointed by the issuer. If an arranger is used, the issuer may appoint the underwriter on the advice of the arranger, or the arranger may appoint the underwriters in turn. If an arranger (or underwriter) is appointed, such an agent is expected to support the preparation and submission of all approval relevant information and necessary documents to the regulatory authorities and market institutions. A listing of the debt securities is optional. In case a listing is intended, a listing sponsor may be used, which in most cases would be the arranger or underwriter.

[16] Authorized Institution refers to a bank, restricted license bank, or deposit-taking institution as defined in section 2 of the Banking Ordinance.

The regulatory process map shown as Figure 2.1 may help with the navigation of the applicable regulatory processes to be applied to a given proposed bond or note issuance.

The issuance approval process and related requirements differ between public offers and issuances aimed at Institutional Investors or professional investors (see Chapter III.N). Sections 4 and 5 in this chapter provide detailed descriptions of Institutional Investors and professional investors, respectively.

3. Regulatory Process in Case of a Nonresident Issuer

In the Basic Law of Hong Kong, and in the regulations and rules issued by SFC and HKMA, respectively, there are no substantive distinctions between types or domicile of issuers for the purpose of issuing or trading and settling debt securities. Hence, regulatory processes for a nonresident issuer are the same as those for a resident issuer, and follow the processes described in Sections 4 and 5 below.

4. Regulatory Process for Public Offers

Public offers of debentures[17] (which are not structured products) by companies are governed by Part II (in case of a company incorporated in Hong Kong) and Part XII (in case of a company incorporated outside Hong Kong) of the CWUMPO.[18] In general, any document or advertisement offering debentures (which are not structured products) to the public in Hong Kong, China issued by companies is required to be authorized by the SFC under the CWUMPO for registration as a prospectus[19], unless an exemption set out in the 17th Schedule to the CWUMPO applies.[20] The SFC vets the prospectus against the content requirements in the 3rd Schedule to the CWUMPO. A list of unlisted bond and note offers to the public authorized by the SFC can be seen on the SFC website.[21]

The CWUMPO prospectus regime is disclosure based. The 3rd Schedule to the CWUMPO sets out matters and reports that must be disclosed in a prospectus, these include:

- general nature of the business of the company;
- authorized share capital or maximum number of shares issuable under the articles and other share details;
- names, descriptions, and addresses of the directors or proposed directors;
- dates of, parties to, and general nature of every material contract carried on or intended to be carried on by the company;
- names and addresses of the auditors; and

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[17] According to section 2 of CWUMPO, debenture, in relation to a company, includes debenture stock, bonds, and any other debt securities of the company, whether or not constituting a charge on the assets of the company.
[18] Structured products that are offered to the public in Hong Kong, China are required to obtain prior authorization from the SFC, unless an exemption under section 103 of the SFO applies. One of the exemptions is offers made only to professional investors", where the term "professional investor" is defined in section 1 of Part 1 of the SFO as extended by the Securities and Futures (Professional Investor) Rules. The definition of structured products is set out in section 1A of Schedule 1 to the SFO.
[19] According to section 2 of CWUMPO*,* prospectus refers to any prospectus, notice, circular, brochure, advertisement, or other document offering any shares or debentures in a company to the public for subscription or purchase for cash or other consideration; or calculated to invite such offers, with certain exceptions, for example, prospectus that relates to an offer specified in the 17th Schedule to the CWUMPO.
[20] Section 103 of the SFO requires any document or advertisement offering "structured products" to the public in Hong Kong, China to be authorized by the SFC, unless an exemption under section 103 of the SFO applies. One of the exemptions is offers made only to "professional investors."
[21] See http://www.sfc.hk/productlistWeb/searchProduct/USAD.do?lang=EN

- in the case of debentures, the rights conferred upon the holders including rights in respect of interest and redemption, and particulars of the security.

Apart from the specific requirements in the 3rd Schedule, the CWUMPO sets a disclosure standard requiring issuers to put in their prospectuses “sufficient particulars and information to enable a reasonable person to form as a result thereof a valid and justifiable opinion of the shares or debentures and the financial condition and profitability of the company at the time of the issue of the prospectus, taking into account the nature of the shares or debentures being offered and the nature of the company, and the nature of the persons likely to consider acquiring them.”

Each prospectus must be registered with the Registrar of Companies upon authorization of the prospectus by the SFC. The prospectus must either be in English with a Chinese translation or in Chinese with an English translation.

The CWUMPO permits a “dual prospectus” structure under which a prospectus may consist of a program prospectus and an issue prospectus that can be authorized, registered, and issued separately for facilitating the conduct of program offers (offers made on a repeat or continuous basis or through successive tranches). The features of this dual prospectus structure include

- A prospectus may consist of (i) a program prospectus; (ii) an issue prospectus; and (iii) an addendum, if necessary, updating the information in the program prospectus or issue prospectus.
- The program prospectus remains valid for not more than 12 months from the date of issue or until publication of the next annual report and accounts of the issuer, whichever comes first.
- The issue prospectus and the corresponding form of application must contain a warning statement that potential investors should read the program prospectus and addendum (if any) for further details about the issuer and program before making any application for the relevant shares or debentures.
- The program prospectus and addendum (if any) should be readily available to investors throughout the period during which the shares or debentures to which it relates are being offered.
- When an issue prospectus is registered, the information in it and in the program prospectus and addendum (if any) referred to in the issue prospectus must comply with the CWUMPO content requirements unless exempted. The program prospectus together with the addendum (if any) and issue prospectus are to be read together, and civil and criminal liabilities provisions regarding untrue statements will apply accordingly.

Pursuant to the SFC Guidelines on Use of Offer Awareness Materials and Summary Disclosure Materials in Offerings of Shares and Debentures under the Companies Ordinance, additional materials related to the offer must be issued by the issuer of the prospectus and must not contain any substantive information not contained in the prospectus nor anything that is inconsistent with the information in the prospectus.

The following steps describe the actions to be undertaken by the parties involved to obtain the authorization for registration of the prospectus from the SFC. Where the issuer uses a sponsor, the sponsor would be expected to drive and coordinate the public offer.

In cases involving a public offering of bonds or notes, or a program offering of debentures to be listed on SEHK, authorization for registration of the prospectus is administered by SEHK and becomes part of the listing approval process (see Section III.I). Also, under the Securities and Futures (Stock Market Listing) Rules (Cap. 571V), the listing applicant is regarded as having sent a copy of its application and ongoing disclosure materials to the SFC if it submits them to SEHK and authorizes SEHK to file them with the SFC on its behalf.

Step 1 – Submission of Application for Authorization to the SFC

To apply for an authorization for registration of a prospectus in respect of unlisted debentures, the issuer or its adviser will be required to submit to the SFC an application in writing, together with the draft prospectus, a completed checklist setting out compliance of all relevant provisions under the CWUMPO, the draft marketing materials (if any), and requisite application fees under the Securities and Futures (Fees) Rules (Chapter 571AF of the Laws of Hong Kong).

If the issuer intends to issue debt securities under a program, and would like to use the dual prospectus approach, the issuer or sponsor will need to seek the exemption of the SFC from the obligatory prospectus requirements. The application should be accompanied by the prospectus(es) and any relevant supporting documents.

The issuer should prepare the prospectus (and any supplemental prospectus) in physical or electronic form (in the case of an eIPO).[22] The electronic form of such documents should be prepared in a format that cannot be tampered with.

In the application, the issuer would also have to name an individual—to be approved by the SFC—and their contact details for the purpose of being served by the SFC with any notices and decisions for the issue(s) (SFO Section 105).

Step 2 – Authorization by the SFC

SFC authorization involves the review of offering documents, and in some cases the structural features of a particular product, to see if certain impartial benchmarks are met and the required information is disclosed.

The SFC reviews the issuance application and information and documents provided, and may provide feedback as necessary. The SFC may, at its discretion, ask the issuer or the arranger for additional documents or information.

Before the SFC authorizes a prospectus for registration it has to be satisfied that, based on the information provided by the issuer, all the requirements in the 3rd Schedule and in Part II or Part XII of the CWUMPO have been met or are otherwise exempted.

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As mentioned previously, the validity of a prospectus (or program prospectus in the event of an issuance program) is expected to last for no more than 12 months, unless exceptional circumstances apply and the SFC agrees to such exception.

A list of the investment products containing the offering documents that have been authorized by the SFC for issuance under the SFO or for registration under the CO (unlisted debentures) are available on the SFC website.[23] The website also contains, for unlisted debentures, the most comprehensive advertisements on the offer (such as

[22] eIPO refers to an initial public offering conducted by electronic means, such as through the internet. Details on eIPOs are contained in the SFC Guidelines for Registered Persons Using the Internet to Collect Applications for Securities in an Initial Public Offering.
[23] See http://www.sfc.hk/web/EN/regulatory-functions/products/product-authorization/list-of-investment-products.html

leaflets or factsheets) that the SFC has authorized under section 105 of the SFO and/or section 38B(2A)(b) of the CWUMPO. The documents on the website are provided by the issuers and the SFC has not independently verified those documents prior to posting.

5. Regulatory Process for Bonds and Notes Aimed at Professional Investors

Bond or note issuances by corporate issuers, regardless of domicile of issuer, aimed at professional investors in the Hong Kong bond market do not require any approval from or notice to regulatory authorities, such as an authorization from the SFC. This includes note issuance programs. If a listing is sought, SEHK's approval is required (see Chapter III.I).

Under CWUMPO, a prospectus is required only when there is a public offer. There is no definition of a public offer in the law. However, the 17th Schedule to CWUMPO sets out the types of offers that are not bound by the prospectus provisions. In practice, these offers are treated as non-public offers. These offers include:

- an offer to professional investors only,
- an offer to not more than 50 persons,
- a small offer with total consideration of not more than HKD5 million (or its equivalent in other currency),
- an offer where the minimum principal amount to be subscribed or purchased is not less than HKD500,000 (or its equivalent in other currency), and
- an offer where the exchange of debt securities does not result in an increase in the aggregate outstanding principal amount.[24]

If the issuer wishes to list such wholesale bonds on the Professional Bonds segment on HKEX, the issuer or its agent (listing sponsor) would have to complete a listing application. In such case, a listing document, such as an offering circular, will need to be provided. According to Listing Rule 37.32, such a listing document must be in English or Chinese, must contain a statement limiting its distribution to professional investors only (Listing Rule 37.31, and may be in printed or electronic form (37.33).

Details of this listing process and its requirements are outlined in Chapter III.I.

6. Obligations after Approval and after Issuance

Post-issuance reporting obligations apply to public offers only and are detailed below.

a. Public Offers

After the registration of the prospectus, the issuer or sponsor of a public offer of bonds or notes is required to report to the SFC within 10 days of an activity relating to the offer, such as the publishing of offer documents, marketing materials or advertisements.

Although there is no continuing disclosure requirement for unlisted debentures under existing law, as a matter of practice, an issuer would, in response to inquiries raised by the SFC during the document vetting process, represent in the prospectus that it will make disclosure of information to avoid the establishment of a false market or disclosure of changes which may significantly affect the ability of the issuer to make payment on the bonds or notes.

[24] See the 17th Schedule to the CWUMPO for a list of safe harbors.

b. Offer to Professional Investors Only

Since no specific approval is required for the issuance of bonds or notes aimed at professional investors only, no subsequent reporting on such issuance needs to be submitted to regulatory authorities by the issuer or its agent, except as required by the Listing Rules (see Chapter 37) in the event a listing is pursued.

If the event that specific post-issuance reporting provisions to investors or other parties have been agreed between parties involved in the issuance, such obligations would need to be observed according to agreements reached.

7. Issuance Process Specific for a Domestic Financial Institution

When issuing debt securities, a resident financial institution, termed an Authorized Institution under the supervision of the HKMA, needs to seek the approval of the HKMA if the proceeds are intended to count toward its regulatory capital.

In the event of a listing, there are specific requirements applicable to banks as issuers of debentures to the public set out in Chapter 34 of the Listing Rules.[25] No specific requirements exist for banks under the Listing Rules for Professional Debts (Chapter 37).

8. Regulatory Process for Foreign Currency Denominated Debt Instruments

There is no distinction in Hong Kong, China between the issuance process for bonds and notes denominated in Hong Kong dollars, offshore Chinese renminbi, or foreign currencies.

The CMU can also clear and settle euros, US dollars, and Chinese renminbi via the Clearing House Automated Transfer System, which is known as CHATS.

Therefore, the regulatory process for foreign-currency-denominated debt instruments follows the process described in either sections 4 or 5, as appropriate.

G. Continuous Disclosure Requirements in the Hong Kong Bond Market

1. Public Offers

Although there is no continuing disclosure requirement for unlisted debentures under existing law, as a matter of practice, an issuer would, in response to inquiries raised by the SFC during the document vetting process, represent in the prospectus that it will make disclosure of information to avoid the establishment of a false market or disclosure of changes which may significantly affect the ability of the issuer to make payment on the bonds or notes.

For issues of debt securities other than issues to professional investors only, the continuing obligations under the Listing Rules and the SFO are designed to ensure that issuers keep the holders of their debt securities (and the public) fully informed of all factors which might affect their interests and treat the holders of their debt securities

[25] See https://www.hkex.com.hk/eng/rulesreg/listrules/mbrules/documents/chapter_34.pdf

in a proper manner. A number of continuing obligations are set out in a listing agreement entered into between an issuer and SEHK and the Listing Rules. The SEHK retains the right to impose additional requirements from time to time.

The general continuing obligations under the Listing Rules include the following:[26]

- compliance with the Listing Rules;
- where there is or there is likely to be a false market in its listed debt securities, the issuer must, as soon as reasonably practicable, announce the information necessary to avoid a false market in its securities;
- announcement of inside information required to be disclosed under the Inside Information Provisions of the SFO;
- if the issuer is listed on other stock exchanges, information released to any such other exchanges is released in the Hong Kong bond market at the same time as it is released in the other markets;
- where the debt securities are guaranteed, the issuer must announce, as soon as reasonably practicable, any Guarantor actions that may have a material effect on its ability to meet the obligations under the debt securities;
- the publication of a change in either
    - the rights attached to any class of listed debt securities, or
    - the rights attached to any shares into which any listed debt securities are convertible or exchangeable;
- the publication of a decision to pass any interest payment of listed debt securities as soon as reasonably practicable after the decision has been made; and
- The publication of any purchase, redemption, or cancellation by the issuer (or any member of the group) of its listed debt securities as soon as possible after the purchase, redemption, or cancellation.

Annual reports or summary financial reports (as applicable) must be delivered to the trustee or fiscal agent (as applicable) and every holder of its listed debt securities (not being bearer debt securities) no less than 21 days before the issuer's annual general meeting. An offshore issuer must deliver its annual report no less than 21 days before the date of the issuer's annual general meeting and no more than 6 months after the end of the financial year to which they relate. Additionally, the issuer must lay its annual accounts at its annual general meeting within the period of 6 months after the end of the financial year. The Listing Rules set out additional information required to be delivered or included in the annual report and accounts.

The Listing Rules also specify certain notifications to be given to SEHK, including new issuances of debt and any decisions to change the general character or nature of business of the issuer or group.

Information such as notices, advertisements, or announcements relating to the debt securities or to a new issue of debt securities must be submitted to SEHK for review. The SEHK must confirm that they have no comments on them before they can be issued or implemented.

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[26] Practical Law. Debt Capital Markets in Hong Kong Regulatory Overview—Country Q&A. http://us.practicallaw.com/2-526-9285?source=relatedcontent#a128060

The issuer must inform SEHK if any part of the listed debt securities of the issuer or any of its subsidiaries is listed or dealt on any other stock exchange. Effective January 2013, the issuer must comply with the Inside Information Provisions as stipulated in the SFO (Part C of Appendix 7). The HKEX Listing Agreement was amended accordingly in January 2013.

Furthermore, the issuer may be required to appoint and maintain a paying agent and/or (where appropriate) a registrar in Hong Kong, China as long as the debt securities are outstanding and unless the issuer itself performs the functions of such paying agent and/or registrar.

The actual details of continuing obligations vary according to the type of issuer.

It should be noted that once a prospectus is authorized for registration by the SFC, it is available for viewing on a dedicated SFC web page, List of Investment Products, under the tab Unlisted Shares & Debentures.[27]

2. Professional Bonds (Listing for Trading or Profile Listing)

The key disclosure document for bonds or notes aimed at professional investors is the offering circular (or Information Memorandum or Offering Memorandum), which contains provisions agreed among parties involved (issuer, arranger and other agents, investors, and intermediaries) on terms and conditions, governing law and jurisdiction, and relevant supporting documentation and disclosure items.

Continuous disclosure for a wholesale bond or note, or issuance program, primarily depends on the conditions set out in the Information Memorandum or Offering Memorandum, and may be based on market expectations among investors.

In practical terms, most of the debt securities offered in Hong Kong, China represent offers to professional investors only. This includes both debt securities listed for trading as well as those listed for profiling on the HKEX Professional Bonds market.

For issues of debt securities to professional investors only that are listed, an issuer's continuing obligations under Listing Rules 37.44–53 include the following:[28]

- compliance with the Listing Rules;
- announcement of any information that is necessary to avoid a false market in its securities or that may have a material effect on its ability to meet the obligations under its debt securities;
- announcement if aggregate redemptions or cancellations exceed 10% and with every subsequent 5% interval of an issue or any public disclosure made on another stock exchange about its debt securities;
- prior notification of any proposal to replace a trustee, amend the trust deed, or amend the terms of convertible debt securities, unless the amendment occurs automatically in accordance with the terms of the debt securities;
- notification of listing of debt securities on another stock exchange;
- provision of a copy of any circular sent to bondholders or any trustee, and, if the issuer is a body corporate, provision of an annual report and interim report; and
- obligation to declare inside information or such information only privy to the issuer that could have a material impact on the debt securities of that issuer

[27] See http://www.sfc.hk/productlistWeb/searchProduct/USAD.do?lang=EN; a click on the Documents tab on the ride side of the page will launch a pop-up window listing the prospectus and marketing materials for the bond or note issue selected.
[28] Practical Law. Debt Capital Markets in Hong Kong Regulatory Overview—Country Q&A. http://us.practicallaw.com/2-526-9285?source=relatedcontent#a128060

(amended in response to the SFO Inside Information Provisions effective January 2013).

Some of the continuous disclosure obligations may be more relevant for nonresident issuers since domestic issuers in Hong Kong, China are often listed and publish continuous disclosure information as a matter of course.

Where equity securities of issuers or Guarantors are also listed, an assessment should be made on whether the announcement published with regard to equity securities has any relevance to the debt securities. Information that has an impact on debt securities should be published under the debt stock codes in addition to the equity counter on the HKEXnews website to enhance transparency and facilitate information access for holders of debt securities.

Announcements related to debt securities should be submitted via the SEHK e-Submission System. SEHK also encourages issuers or guarantors to submit electronic copies of financial accounts or provide the link of a website to SEHK if the financial accounts are published on a website via e-mail.[29]

H. Self-Regulatory Organizations in the Hong Kong Bond Market

At the present time, no SRO specific to the bond market exist in Hong Kong, China. There are securities industry associations in Hong Kong, such as the Hong Kong Capital Markets Association (HKCMA). While the mission of the HKCMA is primarily to promote the Hong Kong debt capital markets and represent its members in the dialogue with regulatory authorities, the HKCMA is not an SRO.

HKEX is considered an exchange-type SRO since it is permitted under the SFO to issue and maintain rules and govern its participating institutions.

1. Hong Kong Exchanges and Clearing Limited

HKEX falls under the Limited Exchange Self-Regulatory Organization Model. The principal function of HKEX is to provide an orderly, informed and fair market for the trading of instruments on its securities and derivatives markets. HKEX is an exchange controller recognized under section 59 of the SFO, and it has statutory duties under section 63 in respect of its subsidiary exchanges and clearinghouses; HKEX is responsible for the enforcement of the trading and clearing rules of its exchanges and clearinghouses. The SFC is responsible for the prudential and conduct regulation of SEHK Participants that are Licensed Corporations under the SFO.

The SEHK, a wholly owned subsidiary of HKEX, is a recognized exchange company under the SFO. It operates and maintains a stock market in Hong Kong, China and is the primary regulator of SEHK Participants with respect to trading matters and the frontline regulator of companies listed on the Main Board and Growth Enterprise Market. SEHK is authorized by section 23 of the SFO to make Listing Rules. SEHK proposes the introduction of new Listing Rules or amendments to the existing Listing Rules, which then requires public consultation and approval from the SFC.

Given HKEX's status as the sole operator of the exchange-based securities markets in Hong Kong, China, the need to ensure that HKEX discharges its responsibilities of safeguarding the integrity of these markets, and its strategic importance to Hong Kong, China’s success as an international financial center, a comprehensive framework of checks and balances has been put in place:

[29] Reference is made to SEHK Guidance Letter. Guidance on Continuing Obligations (Chapter 37 of the Listing Rules). http://www.hkex.com.hk/eng/rulesreg/listrules/listletter/Documents/20151106.pdf

- A corporate governance structure intended to enable HKEX to balance its public functions and its commercial profitmaking objectives has been implemented.

- The fees imposed by HKEX in its capacity as a recognized exchange controller, the Stock Exchange and Futures Exchange as a recognized exchange company, and their related clearinghouses as recognized clearinghouses are required under the SFO to be set out in their respective rules and approved by the SFC. The making of, and changes to, the rules of the Stock Exchange and Futures Exchange and their related clearinghouses require the approval of the SFC. In deciding whether or not to approve a fee or changes to a fee, the SFC is required by the SFO to consider

  - the level of competition (if any) in Hong Kong, China for the matter for which the fee is to be imposed; and

  - the level of fee (if any) imposed by another recognized exchange controller, recognized exchange company, or recognized clearinghouse or any similar body outside Hong Kong, China for the same or a similar matter to which the fee relates.

- As required under the SFO, HKEX established a Risk Management Committee to formulate policies on risk management matters relating to the activities of HKEX, the Stock Exchange and Futures Exchange, and their related clearinghouses, and to submit such policies to HKEX for its consideration. The chairman of HKEX is the chairman of the Risk Management Committee.

More information on HKEX and its trading boards as it relates to the listing and trading of, and reporting on debt securities in the bond market can be found in Chapters II, III, and IV.

For details on some of the listing and trading rules underlying regulations, as well as the trading and disclosure rules of SEHK, please refer to Chapter II.J.

I. Rules Related to Licensing and Trading Conventions

In Hong Kong, China, the licensing of market participants in the securities market is first and foremost undertaken by the SFC, but HKMA Authorized Institutions (once registered with the SFC for the relevant regulated activity) may also participate in the listed bond market.

a. Trading Rights and Stock Exchange of Hong Kong Participants

Under the SFO, any person carrying on a business of regulated activities (e.g., dealing in securities, including debt securities, or dealing in futures contracts) in Hong Kong, China has to be licensed by or registered with the SFC. The SFC maintains a public register of Licensed Persons and Registered Institutions, which is publicly accessible via its website.[30]

In addition, the rules promulgated by the Stock Exchange and the Futures Exchange require any person who wishes to trade on or through their respective

[30] See http://www.sfc.hk/web/EN/regulatory-functions/intermediaries/licensing/register-of-licensees-and-registered-institutions.html

facilities to hold a Trading Right as a prerequisite to becoming an Exchange Participant.

However, the holding of a Trading Right does not of itself permit the holder to actually trade on or through the relevant exchange. In order to do this, it is also necessary for the person to be registered as a participant of the relevant exchange (Exchange Participant) in accordance with its rules, including those requiring compliance with all relevant legal and regulatory requirements. As required by the relevant exchange, prior to applying to become an Exchange Participant, the person has to be licensed by the SFC as a Licensed Corporation.

Trading Rights are conferred on both institutions and individuals.

b. Banking License (Authorized Institutions)

The HKMA licenses and supervises Authorized Institutions (licensed banks, restricted licensed banks, and deposit-taking companies) who are principally able to participate in the bond market under the provisions of the Banking Ordinance. This includes the Local Representative Offices (e.g., branches) in Hong Kong, China of Authorized Institutions established outside of Hong Kong, China.

The relevant provisions in the Banking Ordinance for the participation of Authorized Institutions in the securities market have since been integrated into the SFO. Hence, Authorized Institutions may participate in the bond market, subject to being registered with the SFC for such activities, becoming Registered Institutions in the process. The HKMA acts as the frontline regulator to supervise the regulated activities conducted by Registered Institutions.

The HKMA maintains a public register of Authorized Institutions and Local Representative Offices under its supervision, which is accessible via its website and is downloadable as an Excel file.[31]

In addition, the HKMA maintains the Register of Securities Staff of AIs, which is a database of current and former staff of Authorized Institutions engaging in securities business and/or other regulated activities, as defined under the SFO.[32]

c. Market Conventions and Best Practices

Established in 1986, the HKCMA is an industry association founded by a group of financial institutions active in Hong Kong, China to help promote the development of the local and regional debt capital markets. Since its inception, the HKCMA has performed four main functions:

i) providing various professional recommendations and feedback to regulators with respect to developmental issues of the debt markets;
ii) providing a forum for market professionals to discuss and implement best practices guidelines;
iii) organizing regular functions for market participants to network; and
iv) providing bond market education and training to the public.

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[31] See http://vpr.hkma.gov.hk/cgi-bin/vpr/index.pl
[32] See http://apps.hkma.gov.hk/eng/ereg/disclaimer.htm

Both full and associate members of the HKCMA actively participate in the affairs of the association. Being an HKCMA member is one possible prerequisite to being recognized as a CMU Member.

The HKCMA sets rules and market conventions for its members and the market at large in close cooperation with the HKMA on matters such as trading hours, the quoting and trading of debt securities, and interest calculation for the bond market and money market. At the same time, the HKCMA is advising the SFC and the HKMA on industry practices, and making recommendations for the smooth implementation of new regulations and practices.

d. Code of Conduct

The SFC issued the Code of Conduct for Persons Licensed by or Registered with the SFC, in which standards for and expectations of market participants are detailed. While not having the force of law, the SFC will be guided by this code in considering whether a licensed or registered person satisfies the requirement that it is fit and proper to remain licensed or registered, and therefore would need to be observed as a matter of course. A failure by any person to comply with the code's provisions that apply to it will also be admissible as evidence in court proceedings under the SFO.

J. The Stock Exchange of Hong Kong Limited Rules Related to Bond Listing, Disclosure, and Trading

Rules and regulations for the listing and exchange-based trading of debt instruments, as well as the applicable disclosure requirements, are contained in the Main Board Listing Rules (Listing Rules). Specific provisions with regard to the functions of SEHK in relation to the bond market are indicated below.

1. Listed and Traded Bonds

SEHK is the frontline regulator of Stock Exchange Participants with respect to trading matters and of companies listed on the Main Board and Growth Enterprise Market of the Stock Exchange.

The Listing Rules govern the listing and disclosure requirements for all instruments listed and traded on SEHK. Debt securities listed under Chapter 22 to Chapter 36 of the Listing Rules can be invested by public investors.

In addition, the rules promulgated by the Stock Exchange and Futures Exchange require any person who wishes to trade on or through their respective facilities to hold a Trading Right. The Trading Right confers on its holder the eligibility to trade on or through the relevant exchange, and is awarded by the relevant exchange.

However, the holding of a Trading Right does not, of itself, permit the holder to actually trade on or through the relevant exchange. In order to do this, it is also necessary for the person to be admitted as an Exchange Participant of the relevant exchange in accordance with its rules, including those requiring compliance with all relevant legal and regulatory requirements. The holding of a Trading Right is a prerequisite to admission as an Exchange Participant. Another prerequisite to admission as an Exchange Participant is that the person must be a corporation licensed by the SFC for Type 1 (in the case of SEHK Exchange Participants) or Type 2 (in the case of HKFE Exchange Participants) regulated activities as part of the SFC's licensing process.

The debt securities listing process is further explained in detail in Chapter III.I.

Stock Exchange Trading Rights and Futures Exchange Trading Rights are issued by the Stock Exchange and Futures Exchange, respectively, at a fee and in accordance with the procedures set out in their respective rules.

2. Professional Bonds (Profile Listing)

The provisions for Debt Issues to Professional Investors Only, typically referred to as the Professional Bonds market segment, are contained in Chapter 37 of the Main Board Listing Rules. Investors intending to trade these debt securities (in the OTC market) should ensure they meet the definition of professional investors under Part 1 of Schedule 1 to the SFO.

HKEX issued a Guidance Letter on Professional Bonds, which is available together with other pertinent information from the HKEX website at https://www.HKEX.com.hk/eng/rulesreg/listrules/listletter/Documents/20120330.pdf

The Professional Bonds listing process is further explained in detail in Chapter III.I.

3. Trading Participants

The Rules of the Exchange (Rules), including its relevant schedules, govern the participation, qualifications, trading practices and prescriptions for Trading Rights on SEHK. In addition, the Rules contain the underlying requirements of participants, their conduct, and disciplinary measures in case of noncompliance.[33]

For further details on the trading of debt securities, please refer to Chapter IV.

K. Market Entry Requirements (Nonresidents)

1. Nonresident Issuers

There are no market entry requirements for nonresident issuers in the Hong Kong bond market. There is no quota for the issuance of Hong Kong dollar, offshore Chinese renminbi, or foreign currency debt instruments by a nonresident issuer.

Nonresident issuers may issue debt securities denominated in Hong Kong dollars, offshore Chinese renminbi, or any foreign currency, subject to the approval of the relevant regulatory authorities for issuance as may apply (please see Section F). Foreign entities interested in raising funds in Hong Kong, China should however ascertain whether it is permitted under the law of their jurisdictions.

The proceeds raised from such issuance may be used either in Hong Kong, China or overseas, subject to applicable law and regulations in the relevant overseas jurisdictions. There is no limitation for nonresident issuers to open and maintain Hong Kong dollar, offshore Chinese renminbi, or foreign currency accounts with financial institutions in Hong Kong, China.

Foreign issuers can avail themselves of foreign exchange and hedging instruments to manage interest rate and currency exposure arising from the bond or note issuance with Authorized Institutions in Hong Kong, China or overseas.

[33] See http://www.HKEX.com.hk/eng/rulesreg/traderules/sehk/exrule.htm (visitors are required to accept a disclaimer).

2. Foreign Investors

There are no market entry requirements for foreign market participants to enable them to commence investing or trading in the Hong Kong bond market.

Foreign investors are free to invest in Hong Kong, China, in any form including the purchase of debt securities denominated in Hong Kong dollars, offshore Chinese renminbi, or foreign currency.

L. Market Exit Requirements (Nonresidents)

1. Nonresident Issuers

There are no market exit requirements for nonresident issuers.

2. Foreign Investors

There are no market exit requirements for foreign investors.

There are no restrictions for foreign investors to repatriate funds out of Hong Kong, China from the divestment or redemption of Hong Kong dollar, offshore Chinese renminbi, or foreign currency assets, or the interest arising from investments.

M. Regulations and Limitations Relevant for Nonresidents

Hong Kong, China, is one of the major financial centers in Asia, and a key international financial market. It has also cemented its role as the most significant offshore Chinese renminbi business center.

In consequence, there are no limitations for nonresidents on the participation in the Hong Kong bond market, or the securities or financial market at large.

N. Regulations on Credit Rating Agencies

This section covers the regulations and requirements applicable to credit rating agencies operating in Hong Kong and their business. For the actual credit rating requirements in the Hong Kong bond market, and the application of such credit ratings in the issuance process of bonds and notes, please refer to Chapter III.N.

The three largest CRAs have offices in this jurisdiction, alongside other smaller multinational and local CRAs.

The SFC issued the Code of Conduct for Persons Providing Credit Rating Services in June 2011.[34] It is based on the revised Code of Conduct Fundamentals for Credit Rating Agencies issued by the International Organization of Securities Commissions (IOSCO) in May 2008. The code applies to persons licensed by, or registered with, the SFC for Type 10 regulated activity (providing credit rating services), including representatives (as defined in section 167 of the SFO).

The code does not replace any legislative provisions, or any other codes or guidelines issued by the SFC.[35] In particular, it supplements and should be read in conjunction

[34] See http://en-rules.sfc.hk/net_file_store/new_rulebooks/h/k/HKSFC3527_1783_VER10.pdf
[35] See http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf

with the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (General Code of Conduct).[36] Like other codes and guidelines issued by the SFC, this code does not have the force of law. However, failure to comply with any provision of the code may reflect adversely on a person's fitness and properness to remain licensed or registered under the SFO.

The code stipulates the quality of the credit rating process expected by the SFC, as well as the monitoring and updating process and its underlying resources. The code emphasizes the integrity of the rating process and independence of the CRA and its representatives from external influences or conflicts of interest. It recommends the establishment of procedures and policies for all major areas of the CRA operation, and focuses on transparency and timeliness in the rating process as part of the described responsibilities of the CRA to the investing public at large and the entities it rates.

In line with the IOSCO General Code of Conduct, a CRA should establish its own code of conduct and disclose the same to the public by including the manner in which it will, through its code of conduct, discharge the obligations set by the SFC.

[36] See http://en-rules.sfc.hk/net_file_store/new_rulebooks/h/k/HKSFC3527_1868_VER50.pdf

III

Characteristics of the Hong Kong Bond Market

The SFC and, in particular, the HKMA continue to drive the development of the Hong Kong bond market, in line with global and regional trends, as well as changes in participants' expectations and behaviour. Since this Bond Market Guide was first issued in 2012, there have been and continue to be substantial changes in some of the market characteristics, not limited only to the regulatory environment.

As such, specific characteristics of the Hong Kong bond market are described in more detail in this chapter than in the previous Bond Market Guide.
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A. Definition of Securities

The principal definition of securities in Hong Kong, China can be found in the SFO. In addition, the HKMA sets out a definition of eligible securities for the CMU, while the Listing Rules of SEHK also contain a corresponding definition.

1. Definition in the Securities and Futures Ordinance

a. Section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance

Securities refer to

(i) shares, stocks, debentures, loan stocks, funds, bonds or notes of, or issued by, a body, whether incorporated or unincorporated, or a government or municipal government authority;

(ii) rights, options or interests (whether described as units or otherwise) in, or in respect of, such shares, stocks, debentures, loan stocks, funds, bonds or notes;

(iii) certificates of interest or participation in, temporary or interim certificates for, receipts for, or warrants to subscribe for or purchase, such shares, stocks, debentures, loan stocks, funds, bonds or notes;

(iv) interests in any collective investment scheme;

(v) interests, rights or property, whether in the form of an instrument or otherwise, commonly known as securities;

(vi) interests, rights or property which is interests, rights or property, or is of a class or description of interests, rights or property, prescribed by notice under section 392 of the SFO as being regarded as securities in accordance with the terms of the notice; or

(vii) a structured product that does not come within any of the paragraphs (ⅰ) to (ⅵ) but in respect of which the issue of any advertisement, invitation or document that is or contains an invitation to the public to do any act referred to in section 103(1) (a) of the SFO is authorized or required to be authorized under section 105(1) of the SFO;

but does not include

(i) shares or debentures of a company that is a private company within the meaning of section 11 of the CO (Cap 622);

(ii) any interest in any collective investment scheme that is

(a) a registered scheme as defined in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485), or its constituent fund as defined in section 2 of the Mandatory Provident Fund Schemes (General) Regulation (Cap. 485 sub. leg. A);

(b) an occupational retirement scheme as defined in section 2(1) of the Occupational Retirement Schemes Ordinance (Cap. 426); or

(c) a contract of insurance in relation to any class of insurance business specified in the 1st schedule to the Insurance Companies Ordinance (Cap. 41);

(iii) any interest arising under a general partnership agreement or proposed general partnership agreement unless the agreement or proposed agreement relates to an undertaking, scheme, enterprise or investment contract promoted by or on behalf of a person whose ordinary business is or includes the promotion of similar undertakings, schemes, enterprises or investment contracts (whether or not that person is, or is to become, a party to the agreement or proposed agreement);

(iv) Any negotiable receipt or other negotiable certificate or document evidencing the deposit of a sum of money, or any rights or interest arising under the receipt, certificate or document;

(v) any bill of exchange within the meaning of section 3 of the Bills of Exchange Ordinance (Cap. 19) and any promissory note within the meaning of section 89 of that ordinance;

(vi) any debenture that specifically provides that it is not negotiable or transferable, excluding a debenture that is a structured product in respect of which the issue of any advertisement, invitation or document that is or contains an invitation to the public to do any act referred to in section 103(1) (a) of the SFO is authorized, or required to be authorized, under section 105(1) of the SFO; or

(vii) interests, rights or property which is interests, rights or property, or is of a class or description of interests, rights or property, prescribed by notice under section 392 of the SFO as not being regarded as securities in accordance with the terms of the notice.

b. Section 7 of Part 1 of Schedule 1 to the Securities and Futures Ordinance

References to securities of a corporation

In the SFO, a reference to securities (however described) as those of a corporation shall, unless the context otherwise requires, be construed as a reference to securities (having the applicable meaning, whether under section 1 of Part 1 of Schedule 1 to the SFO or otherwise) that are

i. issued, made available, or granted by the corporation;

ii. proposed to be issued, made available, or granted by the corporation; or

iii. proposed to be issued, made available, or granted by the corporation when it is incorporated.

2. Debentures in the Central Moneymarkets Unit Reference Manual

For bonds and other debt instruments to be cleared through the CMU, they must satisfy the criteria as set out in, among others, the CMU Reference Manual.

a. Central Moneymarkets Unit Instruments

CMU Instruments are money market and capital market instruments that are specified in the CMU Service Reference Manual as capable of being held within the CMU Service.

b. List of Central Moneymarkets Unit Instruments

(i) asset-backed securities,

(ii) equity-linked instruments,

(iii) fixed-rate certificates of deposit,

(iv) government bonds,

(v) floating-rate certificates of deposit,

(vi) bonds,

(vii) fixed-rate notes,

(viii) floating-rate notes,

(ix) commercial paper,

(x) mortgage-backed securities,

(xi) fixed-rate linked securities,

(xii) floating-rate linked securities,

(xiii) zero-coupon certificates of deposit,

(xiv) zero-coupon notes,

(xv) bills of exchange other than trade bills, and

(xvi) any other money market and capital market instruments as the HKMA may specify from time to time.

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3. Definition in the Stock Exchange of Hong Kong Listing Rules

A corresponding definition of debt securities is contained in Rules 1.01 and 37.58 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (Listing Rules), for the purposes of the Professional Bonds market.

i. Debt securities refers to debenture or loan stock, debentures, bonds, notes, and other securities or instruments acknowledging, evidencing, or creating indebtedness, whether secured or unsecured, and options, warrants, or similar rights to subscribe or purchase any of the foregoing and convertible debt securities.

B. Types of Bonds and Notes

All Government bonds and most of the corporate bonds are eligible for clearing in the CMU and maintained in book-entry form.

EFBNs and Government Bonds are in scripless form, while other paper is either bearer or registered and held in physical form, represented by either definitive or global notes.

The most common currencies in which bonds are denominated are the Hong Kong dollar, offshore Chinese renminbi, euro, and US dollar.

1. Bonds and Notes Issued by Public Entities

In Hong Kong, China, bonds and notes issued by public entities include those issued by the Government of the Hong Kong Special Administrative Region of the PRC, the HKMA as the de facto central bank and representative of the government, statutory boards, and other government-related corporations.

a. Government Bonds

The Government Bond Programme, consisting of the Institutional Bond Issuance Programme and the Retail Bond Issuance Programme, was established in 2009 in order to promote the sustainable development of the local bond market.

Government Bonds are issued under the Loans Ordinance (Chapter 61 of the Laws of Hong Kong) and the principal amount of the bonds and all interest and charges thereon will be payable out of the Bond Fund set up under the Public Finance Ordinance (Chapter 2 of the Laws of Hong Kong).

i. Institutional Bond Issuance Programme

Institutional bonds of 3 years, 5 years, 10 years, and 15 years are issued regularly as announced in the half-yearly tentative issuance schedule determined by the government.

As of January 2015, new issuance of 2-year Government Bonds had ceased, with new issuance of Government Bonds only for tenors of 3 years and above. The shorter-tenor spectrum will instead be covered by EFNs (see below).

Some of the bonds issued under the government's Institutional Bond Issuance Programme are also listed on SEHK.

ii. Retail Bond Issuance Programme

Retail bonds are issued as the government may determine. Since 2011, the government, through the HKMA as its representative, has been issuing so-called iBonds on an annual basis. iBonds are 3-year inflation-linked bonds aimed only at residents of Hong Kong, China, with a maximum issue size of HKD10 billion and a minimum denomination of HKD10,000.

Some retail bonds are listed on SEHK (please see also section I in this chapter).

b. Exchange Fund Paper (Bills and Notes) Issued by the Hong Kong Monetary Authority

The EFBN Issuance Programme ensures the supply of a significant amount of high-quality Hong Kong dollar debt paper, which can be employed as trading, investment, and hedging instruments. Authorized Institutions that maintain Hong Kong dollar clearing accounts with the HKMA may use their holdings of EFBNs to borrow Hong Kong dollars overnight from the discount window.

i. Exchange Fund Bills

The EFB Programme was introduced in March 1990. Bills of 91 days (or 90 or 92 days as the calendar may fall), 182 days, and 364 days are regularly auctioned by public tender (please see Section E).

ii. Exchange Fund Notes

The EFN Programme commenced in 1993. EFNs are HKD-denominated, fixed-income debt securities issued by the government under the Exchange Fund Ordinance (Chapter 66 of the Laws of Hong Kong) and for the account of the Exchange Fund.

EFNs were originally issued with tenors of 2 years, 3 years, 5 years, 7 years, 10 years, and 15 years at such times as the HKMA determined. Notes of other maturities may be offered from time to time at the discretion of the Financial Secretary. EFNs are issued in a denomination of HKD50,000 in computerized book-entry form only.

The issuance of EFNs and Government Bonds has been streamlined to minimize overlap in longer tenors. Starting from January 2015, the HKMA has stopped new issuance of EFNs of tenors of 3 years or above, while 2-year EFN issuance continues. At the same time, new issuance of 2-year Government Bonds has ceased and new issuance of Government Bonds will only be for tenors of 3 years and above.

To enhance the liquidity of the secondary market of EFNs and facilitate access by retail investors to the EFN market, the HKMA lists EFNs on SEHK.

The HKMA publishes indicative pricings for EFBNs two times a day. The indicative pricings are calculated daily by Reuters based on indicative bid and ask quotes as of 11 a.m. and 4 p.m. (Hong Kong, China time) provided by 12 Eligible Market Markers designated by the HKMA. EFBs are quoted based on yields and EFNs are quoted based on prices. The indicative price for each of the benchmarks is calculated by taking the arithmetic mean of the middle eight quotes from the Eligible Market Makers after excluding the two highest and two lowest quotes. The indicative pricings are calculated and published via major news wire agencies at 11:30 a.m. and 4:30 p.m. (Hong Kong, China time) on every trading day for EFBNs. In addition, indicative mid-yield and mid-price quotes are posted for off-the-run EFB and EFN issues, respectively.[37]

c. Government-Related Bonds

i. Statutory Bodies

A number of statutory bodies in Hong Kong, China, including Airport Authority Hong Kong, Hong Kong Housing Authority, and Kowloon and Canton Railway Corporation regularly issue bonds in the Hong Kong bond market.[38]

ii. Government-Related Corporations

Examples of issuers considered government-related corporations who regularly issue bonds are, e.g., the Bauhinia Mortgage-backed Securities Limited, the Hong Kong Mortgage Corporation, the Hong Kong Link 2004 Limited, the Kowloon-Canton Railway Corporation, and the MTR Corporation Limited.

2. Bonds and Notes Issued by the Private Sector (Corporate Bonds)

Corporate bonds and notes are typically issued by Authorized Institutions, listed or unlisted local corporates, multilateral development banks (MDBs), or non-MDB overseas borrowers.[39] Non-MDB borrowers include foreign corporates and governments, who may issue debt securities in either Hong Kong dollar or foreign currencies.

Debt securities issued in the Hong Kong, China capital market take many forms and formats. In addition to straight bonds with longer tenors, corporate issuers may issue floating rate notes, index-linked bonds, or loan stocks.

3. Issuance Programs

Issuance programs, typically medium-term note (MTN) programs, are well established and widely accepted in the Hong Kong bond market, and are the most preferred issuance option for issuance to professional investors, both in the domestic and international segments. Issuers include domestic corporates, as well as the

[37] Please also see the HKMA website at http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/debt-market-development/exchange-fund-bills-notes.shtml
[38] The government owns 75% of MTR Corporation, the rest is owned by the public.
[39] MDBs include the African Development Bank, Asian Development Bank, Council of Europe Social Development Fund, European Bank for Reconstruction and Development, European Company for the Financing of Railroad Rolling Stock, European Investment Bank, Inter-American Development Bank, International Bank for Reconstruction and Development, International Finance Corporation, and the Nordic Investment Bank.

Government and government-related corporations. Government Bonds and EFBNs (mentioned earlier) are in fact issued under programs.

Note issuance programs are subsumed under bonds, notes, and (where the issuer is a corporation) debentures in the definition of securities in Schedule 1 to the SFO.

MTN are debt papers issued on a medium-term basis, with tenures of more than 1 year, and up to, e.g., 30 years, and are redeemable at par on maturity. MTN not only give funding flexibility to issuers but also represent the most common format of bond and note issuance in the international bond market. This means that larger and regular issuers, as well as Institutional Investors and intermediaries, are likely to be familiar with note issuance programs and related practices. At the same time, it is expected that potential issuers may benefit from reusing or adopting existing documentation or information on disclosure items.

4. Offshore Renminbi Bond Issuance

The first offshore renminbi bond was issued in Hong Kong, China in 2007. The renminbi bond market in Hong Kong, China, or the "dim-sum" bond market, has since developed steadily. Over the years, the range of issuers in the renminbi bond market in Hong Kong, China has broadened from the sovereign (e.g., Ministry of Finance) and banks in the PRC to include financial institutions and corporates from different parts of the world (as well as corporates from the PRC beginning in 2011). At the same time, the range of investors has widened from institutional and private wealth investors to include sovereigns, banks, corporates, and retail investors.

5. Securitization

A wide range of asset classes are available for securitization. The two main asset classes securitized are (i) residential and commercial mortgages, and (ii) HKMA claims on central governments and central banks.

For instance, the Hong Kong Mortgage Corporation, established by the HKMA, and the Hong Kong Link 2004 Limited were set up to facilitate the securitization of residential mortgages and toll facilities, respectively.

To promote the development of the local debt market, authorities have introduced a number of new products, expanded and improved market infrastructure, and provided a tax and regulatory environment conducive to market development.

C. Money Market Instruments

Money market instruments are short(er) term debt instruments issued by either HKMA or by the private sector. Money market instruments are generally limited to instruments with a maturity of less than one year.

The more common money market instruments observed in the Hong Kong, China capital market are shown by issuer type below.

1. Issued by the Government or Government Entities

a. Exchange Fund Bills

EFBs are issued by HKMA, as representative of the Hong Kong Government, for the account of the Exchange Fund under the Exchange Fund Ordinance (Chapter 66 of the Laws of Hong Kong). In the money market, EFBs may be used by Authorized Institutions to obtain discount funding or be used as collateral for repo transactions. Please also see Section B.1 for further details.

2. Issued by the Corporate Sector

a. Certificates of Deposit

A certificate of deposit is a short to medium-term instrument, which represents the deposit of a defined amount (face value) of money with an Authorized Institution. Certificates of deposit may be traded in the money markets, and are payable to the bearer or registered owner when due.

Certificates of deposit are not equivalent to a time deposit with Authorized Institutions and, hence, do not enjoy the same protection under the Deposit Protection Scheme in Hong Kong, China, as a time deposit would.

b. Commercial Paper

Commercial paper is a short-term unsecured note issued by corporations with original tenors from 1 month to 1 year. In practice, commercial paper is often rolled over upon maturity until the expiry of an issuance program.

Commercial paper is issued in bearer or registered form by corporates and Authorized Institutions.

D. Segmentation of the Market

Table 3.1: Segmentation of the Market—Outstanding Value of Hong Kong Dollar Debt Securities in Hong Kong, China by Type of Bond or Note

Type of Instrument	Type of Bond or Note	Outstanding Amount (HKD million)	% of Total
Government Debt Securities	Exchange Fund Bill	769,821	50.49
	Exchange Fund Note	58,600	3.84
	Government Bond	100,400	6.59
	Subtotal	**928,821**	**60.92**
Nonpublic Segment	Authorized Institutions	242,593	15.91
	Local Corporates	141,659	9.29
	MDBs	5,301	0.35
	Non-MDB Overseas Issuers	162,133	10.63
	Statutory Bodies and Government-owned Corporations	44,050	2.89
	Subtotal	**595,736**	**39.08**
Total		**1,524,558**	**100.00**

MDB = multilateral development bank.
Note: Data as of end-December 2015.
Sources: Hong Kong Monetary Authority. *Statistics & Manuals*. https://www.cmu.org.hk/cmupbb_ws/eng/page/wmp0160/wmp016001.aspx; Hong Kong Monetary Authority. *HKMA Quarterly Bulletin March 2016*. Hong Kong, China.

To provide a better illustration of the segmentation of the different types of debt securities issued in the Hong Kong bond market, Table 3.1 is intended to give an overview of the outstanding value by the types of instruments detailed in Section B.

Detailed information on the outstanding value of bonds and notes, new issuances per period, or specific statistics on the Hong Kong bond market can be found on the websites of the HKMA (see also Table 3.1) and the Government Bond Programme, as well as on *AsianBondsOnline*, a bond information portal operated by ADB under an initiative of ASEAN+3. Appropriate links are also provided in Chapter VII (Market Size and Statistics) and Appendix 2: Practical References.

As a result of the broad availability of comprehensive current bond market statistics for Hong Kong, China, this Bond Market Guide does not carry detailed statistics any more since the shelf life of said statistics is limited and may not be of use to the reader soon after publication. Please see the explanation and links provided in Chapter VII.

E. Methods of Issuing Bonds and Notes (Primary Market)

There are a number of different methods to issue debt securities in the Hong Kong bond market for both government and private sector instruments.

1. Government Bonds

a. Institutional Bond Issuance Programme

Government bonds are issued through competitive conventional tender or switch tender. Tenders must be submitted through Primary Dealers as announced by the government from time to time.

Both types of tenders will be on a competitive bid–price basis subject to a minimum bid of HKD50,000. Each tender bid must be for an integral multiple of the minimum denomination of the bonds.

At least four business days before each tender date, the HKMA will announce the amount of government bonds on offer. All tender applications must reach the HKMA during tendering hours on the tender date. Primary Dealers must indicate the quantity of the Government bonds applied for and the bid price. Tenders accepted will be allotted in descending order of the price bid from the highest to the lowest accepted price. Successful bidders will be allotted Government bonds at the price at which they bid. The tender results, including the amount of Government bonds allotted and the average accepted price, will be announced on the tender date on the Reuters screen (HKGBINDEX), Bloomberg (GBHK <GO>), the Government Bond Programme website (www.hkgb.gov.hk), and any other means as advised by the HKMA.

Underwriting arrangements are in place for conventional tenders by which Primary Dealers may be required to subscribe for bonds that have not otherwise been subscribed pursuant to valid tenders.

For switch tender, successful bidders will additionally be required to deliver a pre-specified issue of the bonds to the government for early redemption at a pre-specified price. The nominal value of the pre-specified issue of the bonds to be delivered by a successful bidder shall equal the nominal value of the bonds allotted to the bidder at that switch tender.

Tenders must be submitted through Primary Dealers by 10:30 a.m. on the relevant tender day. Tender results will be announced not later than 3 p.m. on the relevant tender day. Settlement will be effected on the first business day immediately following the relevant tender day.

The Government Bonds issued will subsequently be listed on SEHK (please also see Section H. in this chapter).

For further details, please refer to the most recent Information Memorandum of the Government Bond Programme.[40]

b. Retail Bond Issuance Programme

Government Bonds are offered to retail investors under the Retail Bond Issuance Programme. Retail investors can apply for the Government Bonds through a placing bank, an HKSCC or CCASS clearing participant, or custodian participants.[41]

For further details, please refer to the Retail Bond Issuance Programme—Programme Circular of the Government Bond Programme, which is published on the Hong Kong Government Bond website.[42]

2. Exchange Fund Bills and Notes issued by the Hong Kong Monetary Authority

EFBs are issued through competitive tender on a bid–yield basis, whereas EFNs are issued either through competitive tender on a bid–price basis or by noncompetitive tender. The tender and underwriting arrangements are similar to those applicable to the Government Bond Programme.

Retail investors may obtain the indicative bid and offer prices of EFBNs quoted by major banks in Hong Kong, China at the CMU Bond Price Bulletin website developed by the HKMA's CMU (www.cmu.org.hk).

For details, refer to the most recent Information Memoranda of the EFBN Programmes published on the HKMA website.[43]

3. Bonds Issued by Other Statutory Bodies and Government-Owned Corporations

The methods of issuance of bonds or notes issued by Hong Kong, China’s statutory bodies and government-owned corporations are similar to those of issuing corporate bonds and notes and are stated in the next section.

4. Corporate Bonds and Notes

Private sector entities generally adopt one of the following methods to issue corporate bonds and notes:

(a) a public offer for bonds intended to be sold to the public, or

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[40] Hong Kong Monetary Authority. Government Bond Programme—Information Memorandum of the Institutional Bond Issuance Programme (May 2016). http://www.hkgb.gov.hk/en/others/documents/Information_Memorandum.pdf

[41] Further information on CCASS can be found at https://www.HKEX.com.hk/eng/market/clr/secclr/ccass3/ccass3.htm

[42] See http://www.hkgb.gov.hk/en/retail/Programme_Circular.html

[43] See http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/debt-market-development/exchange-fund-bills-notes.shtml

(b) a private placement for bonds intended to be sold to a small group of investors.

There are some differences in the requirements for the two methods. For instance, a more comprehensive and detailed prospectus is generally required for a public offer whereas a relatively simple form of offer document or term sheet suffices for a private placement.

For details on the legal requirements, please refer to Part II and Part XII of the CWUMPO. The regulatory framework and its relevant processes for corporate bond and note issuance is also described in some detail in Chapter II.

F. Governing Law and Jurisdiction (Bond and Note Issuance)

Governing law and the jurisdiction for specific service provisions in relation to a bond or note issuance may have relevance, since potential issuers may consider issuing under the laws or jurisdiction of a market other than the place of issuance. The choice of governing law or the contractual preferences of stakeholders can affect the accessibility to a specific investor universe that may otherwise not be accessible if a bond or note were issued under the laws of the place of issuance.

Unless otherwise specified in the prospectus, offer document, or term sheet, the issuance of bonds and notes in Hong Kong, China is governed by and construed in accordance with the Laws of Hong Kong.

The Basic Law of Hong Kong, as well as the stated views of the regulatory authorities and market institutions, permit the use of governing law or jurisdictions other than that of Hong Kong, China for transactions in domestic financial markets. Parties involved in a bond or note issuance may select the governing law or jurisdiction(s) according to their contractual preferences, provided that such provisions do not contravene the Laws of Hong Kong.

Should the parties involved in a bond or note issuance choose to use the laws of Hong Kong, China, the jurisdiction of the issuance would fall to the courts by default. If, in contrast, parties involved in the issuance agree on another governing law, the parties would also have to specifically determine the jurisdiction of a court in which provisions of the bond or note issuance could be enforced and any disputes would be heard and decided.

In any case, the actual use of governing laws or jurisdictions other than those of Hong Kong, China may be subject to clarification or legal advice from a qualified law firm, as may be necessary.

G. Language of Documentation and Disclosure Items

In Hong Kong, China, contracts, bond, and note issuance documentation and disclosure items, applications to and approvals from market institutions as may be necessary, and correspondence with regulatory authorities and market institutions are expected to be in English.

Documentation and disclosure items may be drawn up in Chinese as well, and relevant documentation and offer documents to retail investors are likely to be issued in Chinese.

The prospectus for a public offer of bonds or notes must either be in English with a Chinese translation, or in Chinese with an English translation. Summary disclosure materials for a public offer must be issued both in English and Chinese but may be distributed in separate language versions. If separate language versions are used, a statement must be included in the other language in a prominent place on the front page or cover that a version is available in the other language and where copies can be obtained.[44]

H. Registration of Debt Securities

There is no concept of a formal registration of debt securities with a dedicated institution in the bond market in Hong Kong, China. Instead, the term registration is solely used in the context of effecting changes in ownership of bonds and notes in the CCASS or CMU.

The typical functions associated with a formal registration concept, such as provision of bond information, continuous disclosure and the determination of a fair market price, are carried out by specific institutions that are mandated for such functions, including the HKMA-CMU, HKEX-CCASS, the SFC, and commercial securities pricing providers. The roles of the regulatory authorities and market institutions and their corresponding functions are explained elsewhere in this document.

I. Listing of Debt Securities

A listing of debt securities is possible in Hong Kong, China for the purpose of trading or for the purpose of profile listing, e.g. to achieve visibility or to reach out to a different or larger investor universe.

The listing of a bond or note is not a regulatory requirement by the SFC or the HKMA, in the case of both domestic and foreign issuers, and including in the event of a public offer.

As an example, recent RMB bonds tend to be unlisted, but are featuring respective tranches for both retail and Institutional Investors. When considering a listing, issuers may consider the trade-off between costs and benefits, such as listing fees versus any achievable visibility for the bond or note. In contrast, fund managers may appreciate access to official pricing on SEHK, but may also be able to determine a realistic price through modelling in-house, if such capabilities exist.

For bonds to be listed on SEHK, issuers should also observe the requirements of the Listing Rules (official name Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited), as well as Parts II and XII of the CWUMPO, including section 44B.[45]

1. Listed and Traded Debt Securities

Bonds and notes can be listed and traded on SEHK, while MTN programs may be listed only. The issuer may choose to issue listed bonds by submitting a listing application to SEHK for the listing of and permission to deal in the bonds on SEHK,

[44] According to SFC Guidelines on Use of Offer Awareness Materials and Summary Disclosure Materials in Offerings of Shares and Debentures under the Companies Ordinance (February 2003). The most recent PDF is available at http://en-rules.sfc.hk/en/display/display_main.html?rbid=3527&element_id=2408
[45] See http://www.hklii.org/eng/hk/legis/ord/32/s44B.html

and satisfy certain qualifications for listing as stated in Chapters 22–37 of the Listing Rules.[46]

Issuers having debt securities listed or seeking to list debt securities on SEHK must comply with the requirements set out in the Listing Rules as promulgated by SEHK. Chapter 29 covers tap issues, debt issuance programs, and asset-backed securities. Chapter 36 covers requirements for overseas issuers.[47]

If a public offer of debt securities—pursuant to the prescriptions in the CWUMPO as detailed in chapter II.E—is to be listed on SEHK, the authorization of the prospectus(es) (required under section 105 of the SFO) accompanying the offer will be performed by SEHK, instead of by the SFC (see also Chapter II.F). As such, the prospectus (or constituent prospectuses in the event of a dual prospectus approach) and any supporting documents need to be submitted to SEHK together with the listing application. The listing applicant is regarded as having sent a copy of its application and ongoing disclosure materials to the SFC if it submits them to SEHK and authorizes SEHK to file them with the SFC on its behalf (Securities and Futures [Stock Market Listing] Rules [Cap. 571V]).

In addition, an issuer may obtain a listing of debt securities to professional investors only, pursuant to Chapter 37 of the Listing Rules.

To enhance the liquidity of the secondary market of EFNs and facilitate access by retail investors to the EFN market, the HKMA lists EFNs on SEHK. EFN trading on SEHK began on 16 August 1999. The listing and trading of EFNs has paved the way for the listing and trading of Hong Kong dollar bonds issued by other government-owned corporations.

2. Listing on the Professional Bonds Market

SEHK Listing Rules provide a listing facility for bonds and notes aimed exclusively at professional investors. This facility is officially known as Debt Issues to Professional Investors Only, and typically is referred to as Professional Bonds (please also see Section N in this chapter). In its circulars, the SFC also refers to these professional bonds as Chapter 37 Bonds.

Debt securities under the Listing Rules for Professional Debts (Chapter 37) are targeted at professional investors only who are sufficiently sophisticated to determine whether a listing document provides them the necessary information to make an informed investment decision. These debts are offered to professional investors as defined in Part 1 of Schedule 1 to the SFO, including authorized financial institutions, insurance companies and high net worth individuals or corporations having an investment portfolio of not less than certain prescribed amounts.

Professional Debts will not normally be quoted or traded on SEHK; instead, they are still traded OTC and are inaccessible to retail investors. In most cases, the purpose of listing bonds, notes, or debt issuance programs on SEHK is indeed for profiling for regulatory and price discovery purposes as mentioned above.

A profile listing is a listing without trading on an exchange. The objective of the listing is to make bonds and notes visible and more information available to investors via a recognized listing place, particularly those investors with more restrictive mandates,

[46] Issues of debt securities where only part of the maximum program's principal amount or aggregate number of securities under the issue is issued initially and a further tranche or tranches may be issued subsequently.
[47] For details, refer to Chapters 22–37 of the Listing Rules, which are available at http://www.HKEX.com.hk/eng/rulesreg/listrules/mbrules/vol1_4.htm

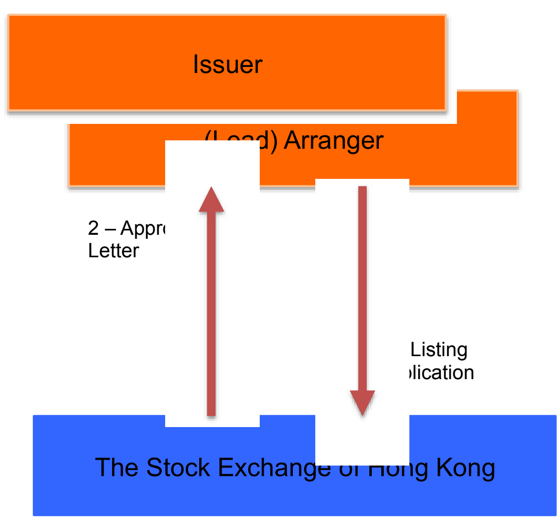
such as mutual and pension funds. A profile listing at a designated listing place can ensure the flow of continuous disclosure information and possibly even reference pricing.

At the same time, a listing for profiling of AMBIF bonds and notes on SEHK may not preclude a simultaneous listing for profiling for the benefit of (certain) professional investors in another jurisdiction.

While the listing of Professional Debts on SEHK is available for both domestic and international bonds and notes issued in Hong Kong, China, and SEHK Listing Rules do not prescribe a particular clearinghouse or place of settlement, the inclusion for settlement in CMU is required to mark a bond or note as a domestic instrument. This is signified by using the prefix “HK” in the International Securities Identification Number of the bond or note. In contrast, bonds or notes issued through ICSDs listed on the Professional Bonds market will carry the prefix “XS.”

For Professional Debts to be listed on SEHK, HKEX is generally supportive of using harmonized documents, as long as its application procedures and all listing requirements are fulfilled. Such harmonized documents are available for issuances under AMBIF. Further details are provided in Chapters IX and X.

Figure 3.1: Listing for Profiling on the Stock Exchange of Hong Kong Limited



Source: ABMF SF1.

To be listed under Debt Issues to Professional Investors Only (Professional Bonds market on SEHK) the steps outlined in Figure 3.1 need to be taken by either the issuer or the issuer’s agent.

Step 1 – Submit Application for Listing or Application for Confirmation of Eligibility to the Stock Exchange of Hong Kong Limited

Any issuer (or their agent) intending to list on SEHK will need to submit an Application for Listing to SEHK, accompanied by the required documentation and disclosure items for the type of listing selected.

At the same time, issuers may choose to first obtain confirmation on the eligibility of their bonds or notes to be listed for profiling prior to applying for a formal listing. For such determination of eligibility, an issuer needs to submit the supporting documents in draft form, as specified in Listing Rule 37.35.

For full listing approval, an issuer or their agent needs to submit the complete set of supporting documents including the final Offering Circular.

The listing criteria for issuers on the Professional Bonds market have been determined as follows:

1. An issuer needs to be a state, supranational, body corporate, or trust; if the issuer is a body corporate it must be validly incorporated or established in its place of incorporation or establishment).
2. An issuer (entity) needs to have net assets of at least HKD100 million.[48]
3. An issuer needs to be able to provide audited accounts for the 2 years before the listing application is made up to a date at most 15 months before the intended date of the listing document.[49]

In addition, the following listing criteria for debt securities have to be met:

1. The bonds and notes must have been authorized through the issuer's governing bodies.
2. The minimum denomination of bonds and notes must be HKD500,000 or the equivalent amount in foreign currency.

Chapter 37 of the Listing Rules allows issuers to tailor their documentation to professional investors who are sufficiently sophisticated to make their own judgment on whether the listing document provides them with the necessary information. In consequence, Rule 37.29 prescribes for the listing application to contain documents and simplified disclosure items that professional investors would customarily expect. It need not comply with Appendix 1 of Part C of the Listing Rules.

As part of the listing application process, the issuer will have to specify their intended listing date for the bonds and notes in the listing application.

Step 2 – Stock Exchange of Hong Kong Limited Checks Application for Listing / Issues Letter of Eligibility or Approval

SEHK will review the request for eligibility or the application, as the case may be, following the submission of the relevant and complete information in documentation and disclosure items, as required under the respective Listing Rules (Step 1). At the same time, SEHK may, at its discretion under the Listing Rules, request supplementary information from the issuer, or arranger or underwriter, if so required for the review process.

[48] This criterion does not apply for issuers already listed on SEHK or another exchange, state corporations, or supranational issuers, or for a special purpose vehicle formed for listing asset-backed securities.
[49] This criterion does not apply for issuers already listed on SEHK, state corporations, or supranational issuers, or for a special purpose vehicle formed for listing asset-backed securities.

In cases of an issuer seeking a confirmation of eligibility to list a bond or note for profiling, SEHK will advise an issuer whether the issuer and its bonds and notes are eligible for listing, typically 5 business days after receipt of the issuer's application, as per Listing Rule 37.36; SEHK will issue a Letter of Eligibility for this.

Provided that an Application for Listing is in order and the necessary information has been provided, SEHK will issue an approval letter to the issuer or underwriter.

In practice, for applications that do not involve unusual features, SEHK will, under normal circumstances, issue the listing approval letter or eligibility letter within 1 business day for issuers that are already listed in Hong Kong, China, or within 2 business days for other issuers.

The listing of professional bonds and notes on the Professional Bonds market carries a one-off listing fee of between HKD7,000 and HKD90,000, depending on issue size and tenor. There is no recurring annual listing fee.

Step 3 – Actual (Effective) Listing

The issuance process for a listing is completed with the actual listing on the Professional Bonds market. The listing of a bond or note is effective upon the listing date stipulated in the listing approval letter, based on the original request by the issuer. There is no defined cooling-off period between listing approval and actual listing.

Should an issuer not fulfill any of the conditions set in the listing approval letter by the expected (stated) listing date, the issuer or their agent would have to submit a new listing application.

3. Listing of Debt Issuance Programs

The listing of debt issuance programs follows a process similar to the one described in section 2. The one-off listing fee for an MTN debt or note program is HKD15,000.

J. Methods of Trading Bonds and Notes (Secondary Market)

Bonds and notes issued in Hong Kong, China are predominantly traded in the OTC market. At the same time, bonds and notes may also be traded on SEHK, the exchange market in Hong Kong, China. Potential investor focus, participants, and choice of instruments may define the respective trading methods.

The individual methods are briefly described in the sections below and are further detailed in the applicable sections of Chapter IV.

1. Over-the-Counter Market

In Hong Kong, China, more than 99% of bonds and notes (by volume) are traded in the OTC market, either directly between counterparties or using the services of a bank, broker, or inter-dealer broker.

OTC-traded debt securities are either cleared and settled at CMU, or through an ICSD.

2. Exchange Traded Bonds and Notes

Trading of debt securities is also available on SEHK. These debt securities are listed on the main board of the exchange and traded in smaller denominations geared towards retail investors. While there is no minimum denomination requirement for retail debts set out in the Listing Rules, SEHK Trading Rule 525 stipulates that all interest-bearing securities are to be quoted in units of HKD100 of their nominal value.

Exchange traded debt bonds and notes are quoted and reported real time on SEHK, giving investors a continuous update on the value of their securities. Trading is facilitated by SEHK Exchange Participants, being securities firms who are governed by the SEHK Trading Rules.

The volume of exchange-traded debt securities remains marginal. Issuers continue to pursue a listing as part of their strategy to attract investor universes, provide disclosure or for general profiling purposes.

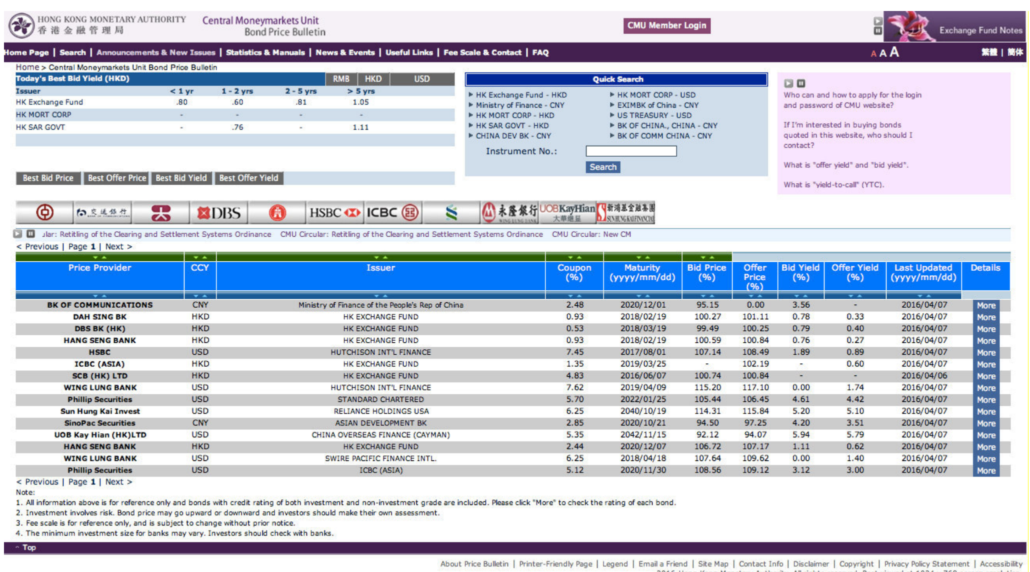
K. Bond and Note Pricing

At present, Hong Kong, China does not have a bond pricing agency, but real-time or reference bond and note prices are available from commercial securities pricing vendors. At the same time, pricing for bonds and notes is also provided by the domestic infrastructure providers for the debt securities covered under their respective remit.

1. Central Moneymarkets Unit

With the CMU Bond Price Bulletin, the HKMA provides a platform for reference pricing and information of debt securities included in CMU. The Bond Price Bulletin is freely accessible through the CMU web page (Figure 3.2).

Figure 3.2: Central Moneymarkets Unit Bond Price Bulletin



Source: Hong Kong Monetary Authority. Central Moneymarkets Unit.
https://www.cmu.org.hk/cmupbb_ws/eng/page/wmp0100/wmp010001.aspx

2. Hong Kong Exchanges and Clearing Limited

There is no requirement under the SEHK Listing Rules for the market-making of exchange-traded bonds and notes. Nevertheless, HKEX provides real-time data services for trades and prices for debt securities that are traded on SEHK through its market data system for its securities market, the HKEX Orion Market Data Platform for Securities Market (OMD-C), which was launched in September 2013. OMD-C disseminates information on debt securities in the same manner as it does for all other types of securities traded on SEHK. OMD-C is accessible to its licensed users including end-users (e.g., brokerage firms) and information vendors who can redistribute the real-time data to their subscribers.

L. Transfers of Interest in Bonds and Notes

The transfer of title or interest in bonds and notes in the Hong Kong bond market can be evidenced through registration. Relevant details and distinctions are mentioned below.

1. Transfer of Entitlement and Ownership of Securities

a. At the Central Moneymarkets Unit

Transferees and transferors should send transfer instructions to the CMU for matching and settlement. The transfer of ownership becomes effective upon matching a debit instruction with the corresponding credit instruction and registration in the book entries in the securities accounts of the CMU Members within the CMU Service.

Retail bonds are usually represented by a single global bond issued in a principal amount equal to the total principal amount of the bonds. The placing banks will hold these bonds in their securities accounts with the CMU Service for and on behalf of individual investors. The CMU account holders are treated as the bondholders. Interest and principal payments will be made to the CMU account holders (placing banks). Individual investors hold their interests only indirectly in book-entry form through the securities accounts they hold with the placing banks. Individual investors also have to rely on the CMU Participants to enforce any rights against the issuer on their behalf.

b. At the Central Clearing and Settlement System of Hong Kong Securities Clearing Company Limited

HKSCC, a wholly owned subsidiary of HKEX, owns and operates CCASS. CCASS only provides clearing and settlement services for its Clearing Participants, such as brokers and custodians. Investors have to settle their trades through their securities brokers.[50]

Investors can open Investor Accounts in CCASS and become Investor Participants. Purchases and sales of securities on SEHK by Investor Participants and the resulting settlement continues to be handled by CCASS Clearing Participants (brokers). However, buying Investor Participants can transfer shares out of the accounts of Clearing Participants or Custodian Participants into their own accounts after settlement of the relevant transactions. Securities transfers out of the accounts of selling Investor Participants initiated by Clearing Participants or Custodian Participants must be affirmed by the Investor Participants concerned. If money settlement is involved, HKSCC will deliver electronic payment instructions to the Hong Kong Interbank Clearing Limited (HKICL) after completing a securities transfer. HKICL will then debit or

[50] For further information, please visit the HKEX FAQs at https://www.HKEX.com.hk/eng/global/faq/post%20trading.htm

credit the designated bank accounts of both Participants. HKSCC acts only as a facilitator of certain securities transfers. Investors continue to manage the settlement risks involved in these transactions.[51]

2. Entitlement Perfection against a Third Party (Finality of Transactions)

a. At the Central Moneymarkets Unit

The Payment Systems and Stored Value Facilities Ordinance (Cap. 584), formerly known as The Clearing and Settlement Systems Ordinance, protects the settlement finality of transactions effected through clearing and settlement systems designated by the HKMA from insolvency laws or other legislation. The CMU is deemed to have been designated under the Payment Systems and Stored Value Facilities Ordinance since 4 November 2004 and all transactions effected through the CMU have since enjoyed statutory backing for their settlement finality.

Real-time securities transfer transactions on the CMU Members' Terminal or via SWIFT are immediately completed upon successful debiting of funds from the buyer and debiting of securities from the seller, and are deemed final (not subject to waiting time).

End-of-day securities transfer transactions are balanced during the CMU settlement run.

Notwithstanding the mode or means of transfer, all local securities transfer instructions effected through the CMU Service shall be settled by the HKMA, debiting or crediting the relevant securities accounts of the CMU Members concerned; once debited or credited to such securities accounts, such securities transfer instructions shall be deemed made, completed, irrevocable, and final.

The situation can be more complex where the securities transfer instructions are effected through linkages with other regional central securities depositories (CSDs) including the Korea Securities Depository; AustraClear; China Central Depository and Clearing (CCDC); and a Taipei, China-based depository and clearing corporation; or with ICSDs such as Clearstream or Euroclear. For debt securities issued and cleared through CMU, the ICSDs will typically use their own Hong Kong domestic links to support the settlement and custody services.

b. At the Central Clearing and Settlement System of Hong Kong Securities Clearing Company Limited

HKSCC, the owner and operator of CCASS, acts as the central counterparty for exchange trades settled via Continuous Net Settlement. As central counterparty, HKSCC guarantees settlement to the buyer and seller participants at the time of novation of the trade.

Securities settlement will become irrevocable after the cash settlement for the underlying exchange trades has occurred in the scheduled batch settlement runs at CCASS on T+2. The actual cash is settled through the facilities of HKICL, which operates the domestic RTGS.

[51] HKSCC only guarantees the clearing and settlement of continuous net settlement transactions between its participants.

3. Prohibited Transfers

a. At the Central Moneymarkets Unit

On-exchange naked short-selling of listed securities, including debt securities, is prohibited in Hong Kong, China and all CMU Members must undertake not to incur a short position in any CMU Instruments. Securities may only be sold at or through a recognized stock market if the seller (as principal) or his principal (as agent), at the time he sells them, has, or believes he has reasonable grounds for believing that he or the principal has a presently exercisable and unconditional right to vest the securities in the purchaser (section 170 of the SFO).

The concept of "presently exercisable and unconditional right to vest the securities in the purchaser" is interpreted with some flexibility. For further illustration, see the SFC's Guidance Note on Short Selling Reporting and Stock Lending Record Keeping Requirements available at the SFC website.[52]

b. At the Central Clearing and Settlement System of Hong Kong Securities Clearing Company Limited

On-exchange covered short sales (short-selling orders) in "designated securities" (as designated by SEHK pursuant to the Short-Selling Regulations in the 11th Schedule to the Trading Rules) shall be concluded in accordance with the provisions of the regulations stipulated in the Trading Rules.[53]

HKSCC charges a default fee of 0.50% of the market value of failed transactions.

The maximum penalties for contravention of section 170 of the SFO are a fine of HKD50,000 and imprisonment for 1 year.

4. Custodian Point of View

Participants in CCASS or the CMU, typically commercial banks and brokers acting as custodians for their investor clients, recognize only the owner of the securities as reflected in their books since they are able to maintain omnibus accounts at the respective settlement system. From a custodian point of view, the transfer of securities is complete once the confirmation of settlement from the respective settlement system is received and results in a corresponding transfer in the custodian's books, which will be advised to clients by status update messages and end-of-day statements, as the case may be.

M. Market Participants

1. Issuers

The HKMA is the main issuer of Hong Kong dollar debt instruments, followed by Authorized Institutions and non-MDB overseas borrowers. In 2015, the amount of EFBs issued by the HKMA amounted to HKD2,242 billion, which accounted for about

[52] Securities and Futures Commission. SFC Regulatory Handbook. http://www.sfc.hk/sfcRegulatoryHandbook/EN/displayFileArchServlet?docno=H141
[53] See https://www.HKEX.com.hk/eng/rulesreg/traderules/sehk/Documents/sch-11_eng.pdf

90% of the aggregate amount of Hong Kong dollar debt instruments issued by any party.

In other typical years, the HKMA was still the main issuer and accounted for around 60% of total Hong Kong dollar debt instruments issued. As of the end of 2015, the outstanding amount of bonds and notes issued by public entities including the government, the HKMA, statutory bodies, and government-owned corporations accounted for about 61%; private entities including Authorized Institutions, local corporates, MDBs, and non-MDB overseas borrowers accounted for the remaining 39%.

For further details, please refer to the feature article, The Hong Kong Debt Market in 2015, in the *HKMA Quarterly Bulletin March 2016*.[54]

2. Guarantor

A guarantor may be required in case the issuer's credit rating or financial situation do not allow for an unassisted issuance of bonds or notes. The guarantor is usually the parent company of a corporate issuer.

3. Investors

Pension funds including the Mandatory Provident Fund schemes, banking institutions, and government-related institutions are the major institutional investors of bonds and notes issued in Hong Kong, China.

4. Parties Involved in Debt Securities Issuance

A number of intermediaries provide services to issuers and investors in the context of the issuance of debt securities in the Hong Kong bond market. The following text provides a brief description of the type of intermediaries and their specific functions.

a. Recognized Dealers and Market Makers

A recognized dealer is an institution which is appointed by the HKMA to hold and deal in retail bonds and institutional bonds through the CMU for the Government Bond Programme.

Recognized Dealers and Market Makers: a two-tier dealership scheme was set up when the EFBN programs were implemented. A number of Recognized Dealers and Market Makers for EFBNs were appointed by the HKMA. In return for certain privileges, the Recognized Dealers and Market Makers are obliged to support, with different degrees of commitment, the development of the EFBN market. Recognized Dealers participate in the secondary market and promote EFBNs in the retail market.

For their part, Market Makers are appointed from the pool of Recognized Dealers and participate actively in the primary market. They have the added responsibility of maintaining secondary market liquidity. Only the Recognized Dealers and Market Makers are eligible to settle EFBNs through the CMU. The Government Bond Programme, which was set up in 2009, also adopted the two-tier dealership scheme. A number of Recognized Dealers and Primary Dealers were also appointed by the HKMA. Similarly, the Government Bond Programme's Recognized Dealers participate in the secondary market while some are additionally appointed as Primary Dealers to participate in the primary market.

[54] See http://www.hkma.gov.hk/media/eng/publication-and-research/quarterly-bulletin/qb201603/fa1.pdf

b. Arranger

The term arranger (also bookrunner or lead manager) is used in the Hong Kong bond market for the lead underwriters of a bond or note issue, including and in particular for note issuance programs. Only institutions licensed by or registered with the SFC can act as arranger. The appointment of an arranger is not mandatory in Hong Kong, China, but a number of government agencies use the services of regular arrangers for the placement of their issuances in the primary market.

The arranger will structure the debt securities, together with any other arrangers or underwriters, and also submit a listing application to SEHK on behalf of the issuer, if a listing for profiling or trading is intended.

c. Underwriter(s)

Investment banks and commercial banks are the main underwriters of debt securities in the Hong Kong bond market. An underwriter is appointed by the issuer, on the advice of the arranger. The arrangers of an issue, besides inviting licensed or registered financial institutions to subscribe to or underwrite the issue, can themselves be underwriters.

Underwriters in the context of a bond or note issuance can be banks, brokers, or securities firms. They need to be either a Licensed Corporation or a Registered Institution.

The appointment of an underwriter is not mandatory in Hong Kong, China, including for a public offer of debt securities.

d. Fiscal Agent

This description of the fiscal agent role and functions is specific to provisions and practices in the Hong Kong bond market. The role and functions of a fiscal agent in other markets, while principally similar, may differ.

A fiscal agency agreement is executed between the issuer and the Fiscal Agent as the principal paying agent of the issuer. The issuer pays the interest or the principal to the fiscal agent and the fiscal agent instructs other paying agents to pay the amounts of interest or principal to the bondholders. The fiscal agent then reimburses the paying agents the amounts paid out.

The fiscal agent also has other functions, such as keeping records of payments on the bonds or notes, calling and holding bondholders' meetings when necessary, sending notices to bondholders, and issuing replacements for lost or destroyed bonds or notes (if applicable).

As a fiscal agent is the agent of the issuer, they do not represent the interests of the bondholders. The issuer would generally execute a deed of covenant, under which bond- or noteholders are given direct rights of enforcement against the issuer for default in payment or delivery of definitive bonds or notes.[55]

[55] A deed of covenant is an arrangement under which a party promises to pay a certain sum regularly to another party within a specified time frame.

e. Paying Agent

In Hong Kong, China, a paying agent is responsible, together with the trustee and/or fiscal agent, for paying the interest and principal under, and sending notices pursuant to, the notice provisions of the CMU Instruments or bonds and notes listed and traded on SEHK.

The paying agent is responsible for the cash flow involved in a bond or note transaction under the instructions of the fiscal agent (see above), specifically in receiving the proceeds from the issuance on behalf of the issuer and remitting the proceeds to the issuer or the trustee, as the case may be, as well as the payment of interest and redemption amounts to investors. The function may include the withholding of taxes and duties, as may be applicable. An underwriter may also perform the paying agent role.

The Paying Agent receives an issue position report from the CMU Service on the interest payment dates of the relevant CMU Instruments, the aggregate nominal value of the relevant CMU Instrument held by each CMU Member at the interest payment record date, the maturity date of the relevant CMU Instruments, and the aggregate nominal value of the relevant CMU Instrument held by each CMU Member at the maturity record date.

The HKMA acts as the paying agent for Hong Kong government bonds and its own EFBNs. The role of a paying agent for corporate bonds and notes is typically performed by a commercial bank.

f. Conversion Agent

In the case of convertible bonds, the issuer will engage a conversion agent, responsible for handling on behalf of the issuer the conversion notices sent by the bondholders, receiving payments from bondholders and the issuer in respect of the conversion and cancelling of the original bonds upon conversion.

The conversion agent would also be responsible for calculating the number and aggregate principal amount of new shares to which the bondholders exercising the conversion rights would be entitled.

The conversion agent is normally a bank.

g. Bond Trustee

Bonds may be constituted in a trust deed, under which the issuer covenants with the trustee to perform its duties under the terms and conditions of the bonds, including to pay any amount due under the bonds and to notify the trustee of any event of default.

The trustee is the representative of the bondholders and exercises the bondholders' rights on behalf of the bondholders and monitors the issuer's performance of its obligations under the bonds.

A paying agency agreement is executed between the issuer, the trustee, and the paying agent, under which the paying agent (as agent for the issuer) receives payments due the bondholders from the issuer and pays the relevant interest or principal to the bondholders.

Although in practice payments to bondholders are effected through paying agents, the trust deed usually provides power to the trustee, if it declares that an event of default has occurred, to require the issuer to make payments directly to it rather than to the paying agent or to require the paying agent to act as the trustee's agent, rather than the issuer's agent, when making payments. This protects the bondholders in cases where the issuer is insolvent; the money held by the paying agent would belong to the trustee rather than being vulnerable to claims by the issuer or the issuer's liquidators.

For a detailed description of the role and functions of the bond trustee, please refer to sections P.5 and Q in this chapter.

h. Authorized Institution(s) as Depository Agents

Authorized Institutions are licensed banks, restricted license banks, and deposit-taking institutions and may act as depository agents for investors or issuers. They are designated as CMU Members or CCASS Participants, respectively, and may be custodians, Recognised Dealers or Primary Dealers, or underwriters.

(i) Central Moneymarkets Unit Members and Lodging Agent

The CMU Member or CMU Lodging Agent holds the legal title of the bonds held within the CMU Service. CMU Participants are required to maintain segregated accounts in CMU for their own holdings and those belonging to clients. Client holdings are typically maintained as an omnibus account, however, clients with large holdings or holdings for specific purpose may request to open separate accounts accordingly.

If the CMU Member holds the CMU Instrument for and on behalf of its customers, it should arrange for the relevant amount of interest to be paid to the customers according to the standing arrangements between the CMU Member and the customers. The CMU Member or CMU Lodging Agent receives the Account Position Report, confirming the balances in their securities accounts with the CMU Service.

CMU membership is open to financial institutions regulated by the HKMA, SFC, Office of the Commissioner of Insurance or Mandatory Provident Fund Schemes Authority, and local and overseas financial entities at the discretion of the HKMA. All CMU Members are required to sign a CMU Membership Agreement with the CMU Service.

(ii) Central Clearing and Settlement System Participants

Many domestic intermediaries are also participants in the CCASS settlement system. The types of CCASS Participants are defined in HKSCC's Clearing House Rules under General Rules of CCASS, Chapter 3, Rule 302 lists: [56]

(i) Clearing Agency Participants,
(ii) Custodian Participants,
(iii) Direct Clearing Participants,
(iv) General Clearing Participants,

[56] See https://www.HKEX.com.hk/eng/rulesreg/clearrules/ccassgr/ccassrule.htm

(v) Investor Participants,
(vi) Stock Lender Participants, and
(vii) Stock Pledgee Participants.

For example, a Custodian Participant must be an Authorized Institution under the Banking Ordinance, a trust company, or a Licensed Corporation that can carry out Type 1 regulated activities under the SFO.

Each participant has to sign a Participant Agreement with HKSCC, which stipulates the role, functions, and obligations of the relevant type of participant.

Authorized Institutions are also typically the banks participating in the respective RTGS settlement systems for cash settlement purposes.

Custodians may also offer a range of value-added products and services in relation to the bond market, such as securities lending or repo business.

i. Legal Advisers (Legal Counsel)

Before the finalization of debt securities issues, a legal due diligence exercise is always conducted on the issuer, related projects, and project information pertaining to the debt securities issue. This is done by legal counsel appointed by the issuer, typically also referred to as a legal adviser.

Law firms involved in the bond or note issuance process in Hong Kong, China are not required to obtain a specific license or accreditation with the SFC or HKMA. There is no positive or negative list for law firms maintained or published by the SFC.

j. Auditors

Auditors are typically accounting firms involved in the bond or note issuance process in Hong Kong, China. These firms are not required to obtain a specific license or accreditation with the SFC or HKMA. There is no positive or negative list for accounting firms maintained or published by the SFC.

In addition to reviewing the financial situation of an issuing company, and the certification of the financial statements, auditors typically also perform a limited financial due diligence exercise to ascertain the credibility of the financial projections and financial data in the disclosure information for an intended bond or note issue. The primary purpose of these due diligence exercises is to ensure that no misleading and/or inaccurate information is furnished to the regulatory authorities and investors. Auditors may also issue comfort letters, if so applicable or required.

N. Definition of Professional Investors

The definition of “professional investor” is particularly significant in the issuance of (or investment in) debt securities exempt from prospectus or full disclosure requirements. Such offers for sale or subscription of bonds or notes to Institutional Investors only constitute the professional bond market in Hong Kong, China. Details and descriptions of the regulatory processes for bond and note issuance can be found in Chapter II.

Institutional entities that qualify as professional investors based in Hong Kong, China may invest in overseas markets without limitation subject to the laws and regulations in the relevant jurisdictions, unless these institutions' own mandates, investment guidelines, or specific prudential regulations prescribe particular restrictions.

1. General Definition

The SFO provides for the definition of professional investor in Hong Kong, China. This definition includes investors listed under items 1–9 below. The investors listed in items 1–5 below are typically referred to as Institutional Professional Investors and the investors listed in items 6–9, prescribed by the Securities and Futures (Professional Investors) Rules (Cap. 571D) (PI Rules), are typically referred to as Non-Institutional Professional Investors:

(i) Institutional Professional Investors include

1. regulated securities firms, any person carrying on the business of the provision of investment services regulated under the Laws of Hong Kong or the laws of any place outside Hong Kong, China;
2. regulated banks, any bank regulated under the Laws of Hong Kong or the laws of any place outside Hong Kong, China;
3. regulated insurers, any insurer regulated under the Laws of Hong Kong or the laws of any place outside Hong Kong, China;
4. authorized investment funds, any collective investment scheme authorized by the SFC or similarly constituted under the laws of any place outside Hong Kong, China, and, if regulated under the laws of such place, permitted to be operated under the laws of such place, or any person by whom any such scheme is operated; and
5. sovereign bodies, any government (other than a municipal authority) or any institution, which performs the functions of a central bank, or any multilateral agency.

(ii) Non-Institutional Professional Investors (persons who, as a result of their financial position, qualify as professional investors under the Professional Investor Rules), include:

6. High Net Worth Individuals, any individual (either alone or with any of his or her associates on a joint account) who has a portfolio of not less than HKD8 million (or its equivalent in any foreign currency);
7. corporate professional investors, any corporation or partnership with either a portfolio of not less than HKD8 million (or its equivalent in any foreign currency) or total assets of not less than HKD40 million (or its equivalent in any foreign currency); and
8. trusts, any trust corporation entrusted under the trust or trusts of which it acts as a trustee with total assets of not less than HKD40 million (or its equivalent in any foreign currency); and
9. investment holding corporations, any corporation the sole business of which is to hold investments and is wholly owned by one or more of the persons listed in items 6, 7, or 8.

The provisions of the above regulations specifically include foreign investors.

The scope of Institutional Investors corresponds closely with the typical scope of professional investors found in other markets and used in the definition of professional bond or note issuance concepts such as AMBIF (see also Chapters IX and X).

With regard to CMU practices, issuers shall ensure that their bond or note issuance meets all regulatory requirements, including compliance with the SFO and the definitions of Professional Investors contained therein, before lodging the bond or note with the CMU.

2. Use of Definition by the Stock Exchange of Hong Kong Limited

In its dealings for the Professional Bonds market, SEHK uses the term professional investors, which in Hong Kong, China includes professional investors as defined in the SFO (excluding those prescribed by rules made under Section 397 of the SFO). This includes Institutional Professional Investors but not Non-Institutional Professional Investors. However, SEHK may grant waivers to allow such Non-Institutional Professional Investors to participate in the Institutional Professional Investors-only debt issues.

Rule 37.58 of the Listing Rules contains a definition of professional investor, which is also contained in guidance letters issued by SEHK:[57]

> (a) For a person in [Hong Kong, China], a professional investor as defined in part 1 of Schedule 1 to the [SFO] (excluding those prescribed by rules made under section 397 of [the SFO]); or
>
> (b) For a person outside [Hong Kong, China], a professional investor is a person to whom securities may be sold in accordance with a relevant exemption from public offer regulations in that jurisdiction.

O. Credit Rating Requirements

This section covers the applicable credit rating requirements for bonds and notes issued in the Hong Kong bond market. For details on the underlying regulations on credit rating agencies and their business, please refer to Chapter II.N.

1. Present Requirements

As stated in Guideline 6.2.2B, the HKMA recognizes the ratings of various credit rating agencies for the purposes of the liquidity regime as well as the market risk capital adequacy framework. Under the liquidity regime, Authorized Institutions' holding of marketable debt securities may be regarded as liquefiable assets for liquidity ratio purposes if they have a qualifying credit rating recognized by the HKMA. For the purposes of the market risk capital adequacy framework, debt instruments in the trading book which satisfy certain qualifying credit ratings may be included in a "qualifying" category which carries a lower capital requirement. Guideline 6.2.2B also restates the HKMA's view of qualifying credit rating.[58]

2. Credit Rating Requirements for Debt Issues to Qualify for Profits Tax Concession

In August 2012, the HKMA announced specific credit rating requirements applicable to short-term debt instruments for the purpose of qualifying debt instruments for profits tax concession under section 14A of the Inland Revenue Ordinance.

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[57] The Stock Exchange of Hong Kong Main Board Listing Rules 37.58; see also http://en-rules.hkex.com.hk/net_file_store/new_rulebooks/c/o/consol_mb.pdf
[58] See http://www.hkma.gov.hk/eng/key-information/guidelines-and-circulars/guidelines/guide_622bb.shtml

Under the profits tax concession scheme, interest income and trading profits derived from eligible debt securities are entitled to concessionary tax rates as specified in the relevant section. To be eligible, a debt instrument should, among other criteria, possess a credit rating acceptable to the HKMA from a rating agency recognized by the HKMA. More details on the tax concessions can be found in Chapter VI.

The HKMA had already announced minimum acceptable credit ratings applicable to long-term debt instruments in June 2006. With the newly announced minimum acceptable credit ratings applicable to short-term debt instruments, the minimum credit ratings acceptable to the HKMA for the purpose of qualifying debt instruments for profits tax concession under section 14A of the Inland Revenue Ordinance are listed in Table 3.2.

Table 3.2: Credit Rating Requirements for Debt Issues to Qualify for Profit Tax Concession

Recognized CRAs	Minimum Rating Required	
	Long-Term Debt Instrument	Short-Term Debt Instrument
Fitch Ratings	BBB–	F3
Moody's Investors Service	Baa3	P-3
Rating and Investment Information, Inc.	BBB–	a-3
Standard and Poor's Ratings Services	BBB–	A-3

CRAs = credit rating agencies.
Source: Hong Kong Monetary Authority, adapted by ADB Consultants for SF1.

The HKMA reserves the right to make adjustments to the list of rating agencies and minimum credit ratings recognized by it.

3. Credit Rating for Issuance to Professional Investors

A credit rating is not mandatory for bonds and notes to be issued to professional investors in the Hong Kong bond market. Issuers may choose to use a credit rating if it would satisfy investor demand. As of 2014, the majority of bonds and notes listed on SEHK carried an investment grade rating.

A credit rating is also not a specific criterion for eligibility to list a bond or note aimed at professional investors in the Professional Bonds market on HKEX.

P. Market Features for Investor Protection

This section reviews a number of topics that have a bearing on the protection of investors in the Hong Kong bond market, particularly for retail or nonprofessional investors.

1. Investor Complaints

The SFC performs its regulatory functions with high integrity and accountability, and this commitment extends to the handling of complaints from the public. Hence, the SFC offers investors or the general public the opportunity to lodge a complaint against market participants or market activities, or against the SFC itself, via its website or direct contact.[59]

As the regulatory authority for licensed banks, restricted license banks, and other deposit-taking companies, the HKMA offers the public the ability to lodge complaints against banks. For that purpose, the HKMA provides the complaint form, frequently asked questions on complaints against banks, as well as a flowchart of the complaint handling process, on its website.[60] At the same time, the HKMA also provides a list of contact persons at the banks for the lodging of any complaint directly with these institutions should the complainant so prefer.

The HKMA does not have the legal power to order banks to pay compensation. If the complaint is about a monetary dispute, a complainant could consider using the mediation and arbitration services provided by the Financial Dispute Resolution Centre, which provides financial consumers with an independent and affordable avenue, as an alternative to litigation, for resolving some monetary disputes with financial institutions.

2. Retail Investors

Retail investors, or in fact any investors, interested in obtaining detailed knowledge about and a better understanding on debt instruments, the bond market in Hong Kong, China at large, its market infrastructure and participating institutions, licensed persons and intermediaries, and products and services in the capital market have a wide choice of available resources and websites.

The SFC details on its website a comprehensive list of laws, codes and guidelines, as well as circulars for the Hong Kong bond market, including provisions on debt instruments and bond market participants, and a register of licensed persons and institutions. In addition, the website provides access to numerous industry-related publications and research papers for the public's benefit.

Similarly, the HKMA website contains quick links to guidelines and circulars, as well as to consumer tools and reference materials. In addition, the HKMA maintains the HKMA Information Centre, which introduces the work of the HKMA and houses books, journals and other texts on central banking and related subjects. The HKMA Information Centre consists of an exhibition area and a library. It is operated as a resource for HKMA staff and as an educational and research facility for the public. The HKMA Information Centre has been open to the public since 1 December 2003 and admission is free.

The CMU itself offers free access to the CMU Bond Price Bulletin on its website, which contains reference bond prices and yields, as well as bids and offer information from a number of price providers in the market. Visitors can use quick links to go to the outstanding bonds of specified issuers.[61] The bulletin also contains news, statistics, and manuals for the easy reference of investors.

In turn, HKEX offers detailed descriptions of governing regulations and its own rules on its website, together with access to an Investment Service Centre for the public's easy reference. The available information is complemented with statistics and research materials, as well as news from, and consultations happening in the Hong Kong bond market.

[59] See http://www.sfc.hk/web/EN/lodge-a-complaint/
[60] See http://www.hkma.gov.hk/eng/key-functions/banking-stability/complaints-about-banks.shtml
[61] See https://www.cmu.org.hk/cmupbb_ws/eng/page/wmp0100/wmp010001.aspx

For retail investors, the Investor Education Centre, which is supported by the Education Bureau and financial regulators, hosts a website that offers comprehensive information about investing in bonds and other financial products. Branded as the “the Chin Family” to help viewers relate to typical, real-life situations, the website offers educational resources for teachers and students, parents and retirees, as well as the investing public at large, on bonds, their terminology, and associated investment risks.[62]

3. Foreign Investors

Foreign investors as creditors have the same rights as local creditors in Hong Kong, China.

Due to the general availability in the Hong Kong bond market of issuance documentation, disclosure items, credit ratings, and pricing information for debt securities in English through a variety of public domain websites, foreign investors enjoy the same access to relevant data as local investors. Where websites require subscription to receive information, such subscription service is also available to foreign investors.

4. Bondholder Rights

Bondholders, like other investors of securities, enjoy certain protections under the SFO and subsidiary regulations by the SFC and HKMA, respectively, including applicable codes of conduct for market participants. Under the CWUMPO, creditors, including bondholders, can file a winding-up petition for a company when debtors are unable to pay their debts (of an amount equal to or exceeding HKD10,000) after having made a statutory demand but the debtors did not pay within 3 weeks of the demand. When a winding-up order is made, the court appoints a liquidator who oversees the liquidation process.

5. Bond Trustee and Trust Deed

The Trustee Ordinance (Cap. 29 of the Laws of Hong Kong) provides for the function of a bond trustee and regulates the roles and responsibilities of the bond trustee for the benefit of the bondholders or noteholders.

While it is not mandatory in Hong Kong, China to appoint a bond trustee, the appointment of a trustee offers potential investors the added security of a party with fiduciary duties to safeguard the interests of the bondholders as set out in the trust deed and in the Trustee Ordinance.[63]

In the event a trustee is appointed, the trust deed covering the bonds or notes to be issued contains bond or note provisions and relevant covenants, and other requirements as may be agreed between issuer and trustee.

The trustee’s role, responsibilities, and eligibility criteria for bond trustees are explained further in Section M of this chapter.

For information on bankruptcy protection and event-of-default provisions, please refer to Sections R and S of this chapter, respectively.

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[62] See http://www.thechinfamily.hk/web/en/financial-products/investment/bonds/index.html

[63] Under Listing Rules 29.11(d) and 37.16, there must be a trustee or other appropriate independent party representing the interests of the holders of asset- backed securities and with the right of access to appropriate info relating to the assets. Also, Listing Rule 24.10 appears to suggest that where a trust is formed to secure or constitute the debt securities seeking listing, the trust deed needs to be submitted to SEHK.

6. Securities and Futures Ordinance

The SFO gives both the SFC and HKMA substantial powers to regulate and supervise the securities market and banking industry, respectively. The SFO provides strong protection for investor interests, and enhances corporate governance of listed companies and market transparency, with particular references and provisions in the following areas:

(i) Part VIII (Supervision and Investigations) includes details on the supervision and investigation powers of the SFC and the supervision powers of the HKMA;

(ii) Part IX (Discipline, etc.) outlines possible disciplinary actions by the SFC against infringements or violations of the SFO;

(iii) Part X (Powers of Intervention and Proceedings) sets out the powers of the SFC to intervene in the business of, or dealing with property by, a Licensed Corporation, as well as the powers of the SFC to apply to the court for injunctions and other orders;

(iv) Part XIII (Market Misconduct Tribunal) provides that the SFC may institute proceedings in the Market Misconduct Tribunal where it appears to the SFC that market misconduct has or may have taken place;

(v) Part XIV (Offences Relating to Dealings in Securities and Futures Contracts, etc.) creates criminal offenses for misconduct, such as insider dealing and disclosure of false and misleading information etc., and details provisions and mechanisms on how to address such misconduct;

(vi) Part XIVa (Disclosure of Inside Information) requires a listed corporation to disclose inside information—specific information about the corporation, its shareholders or officers, and its listed securities or derivatives that is not publicly known and is materially price sensitive—to the public as soon as reasonably practicable; and

(vii) Part XV (Disclosure of Interests) requires the disclosure to investors and the market by corporate insiders of their interests in securities of listed corporations to ensure a fair, informed, and orderly securities market.

7. The Investor Compensation Fund

Prior to the enactment of the SFO there were two separate investor compensation schemes called the Unified Exchange Compensation Fund (UECF) and the Commodity Exchange Compensation Fund (CECF) managed, respectively, by SEHK and the Hong Kong Futures Exchange Limited. The CECF was wound up in May 2006 and the residual monies were transferred to the Investor Compensation Fund (ICF). The UECF is applicable to the claims submitted before 1 April 2003 and it no longer covers the claims submitted after that.

The prevailing ICF was introduced on 1 April 2003 under the SFO. The main aim of the ICF is to pay compensation to qualifying investors (any nationality) who suffer financial losses on account of a default on the part of an intermediary licensed or registered for dealing in securities or in futures contracts, or an Authorized Institution that provides securities margin financing in relation to securities or futures contracts listed or traded on SEHK or HKFE. The maximum compensation limit for each claimant is pegged at HKD150,000 by the Investor Compensation–Compensation Limits Rules (Cap. 571AC).

The Investor Compensation Company Limited was established for the administration and determination of claims received against the ICF. The main source of income for the ICF is from the Investor Protection Levy imposed on each exchange-traded product transaction. The current levy is as follows:

Nature of Transaction	Amount Payable
Securities transactions	0.002% payable each (buyer and seller)
Futures contract	HKD0.5 per side of a contract or HKD0.1 per side of a mini-Hang Seng Index futures, mini-Hang Seng Index options contract, or mini-Hang Seng China Enterprises Index futures contract

A levy suspension and reinstatement mechanism was introduced on 28 October 2005 by amendments to the Investor Compensation–Levy Rules (Cap. 571AB). As the net asset value of the compensation fund exceeded the limit of HKD1.4billion in 2005, the payment of an Investor Compensation Levy has been suspended by the SFC, according to the levy trigger mechanism for sale or purchase of securities and futures contracts, since 19 December 2005. The other funding sources of ICF include investment income, bank interest earned on deposits maintained, and transfers from the UECF and CECF.

Q. Bond Trustee or Fiscal Agent Structure

In Hong Kong, China, bond and note issues are generally structured in one of two possible manners, i.e. using a trustee structure or a fiscal agent structure. The rights and obligations of the bondholders and the issuer are different depending on the structure.

While the trustee has fiduciary responsibility towards the bondholders, the fiscal agent does not; hence, from the perspective of foreign institutional investors, and those investors subject to a prudential mandate, the appointment of a trustee may appear safer than the use of a fiscal agent.

The appointment of a trustee is possible but not mandatory under the law. Approximately 90% of all bonds and notes issued feature a fiscal agent structure instead of the use of a trustee. According to market participants, the choice may typically be determined by the question of cost, and the availability of a limited number of trustees in the market; at the same time, however, some issuers may appreciate the use of a central party to handle all relevant functions with regards to bondholders and other matters.

1. Bond Trustee Structure

Issuers or their agents in the issuance of a bond or note to professional investors may appoint a bond trustee. Having a bond trustee is not mandatory under the law and optional for bonds and notes listed on the SEHK Professional Bonds market. However, Listing Rule 24.10(6) stipulates the requirement for a trustee in retail debt offerings. Issuers or their agents in the issuance of a bond or note aimed at Institutional Investors may appoint a bond trustee, if investors or the applicable Listing Rules so require. For example, under Listing Rules 29.11(d) and 37.16, there must be a trustee or other appropriate independent party representing the interests of the holders of asset-backed securities and with the right of access to all appropriate information relating to the assets. Also, Listing Rule 24.10 requires submission of a trust deed or other document securing or constituting the debt securities to SEHK if available.

The bonds or notes may be constituted in a trust deed, under which the issuer covenants with the trustee to perform its duties under the terms and conditions of the bonds or notes, including to pay any amounts due under the bonds or notes and to notify the trustee of any event of default.

The trustee is the representative of the bondholders and exercises the bondholders' rights on behalf of the bondholders and monitors the performance by the issuer of its obligations under the bonds or notes.

A paying agency agreement is executed between the issuer, the trustee and the paying agent under which the paying agent (as agent for the issuer) receives payments due to the bondholders from the issuer and pays the relevant interest or principal to the bondholders.

Although, in practice, payments to the bondholders are effected through the paying agents, the trust deed usually provides power to the trustee, if it declares that an event of default has occurred, to require the issuer to make payments directly to it rather than to the paying agent, or to require the paying agent to act as the trustee's agent, rather than the issuer's agent, when making payments.

This protects the bondholders where the issuer is insolvent; the money held by the paying agent would belong to the trustee, rather than being vulnerable to claims by the issuer or the issuer's liquidators.

2. Fiscal Agent Structure

A fiscal agency agreement is executed between the issuer and the fiscal agent (as the principal paying agent of the issuer). The issuer pays the interest or the principal to the fiscal agent and the fiscal agent instructs the other paying agents to pay the amounts of interest or principal to the bondholders. The fiscal agent then reimburses the paying agents the amounts paid out.

The fiscal agent typically also has other functions, such as the keeping of records of payments on the bonds or notes, the calling and holding of bondholders' meetings when necessary, the sending of notices to bondholders and the issuing of replacements for lost or destroyed bond or note certificates (if not a scripless bond or note).

As the fiscal agent is the agent of the issuer, it does not represent the interests of the bondholders. The issuer would generally execute a deed of covenant under which bondholders are given direct rights of enforcement against the issuer (for default in payment or delivery of definitive bonds).[64]

R. Meeting of Bondholders

The terms as to the rights to convene meetings of bondholders or noteholders and quorum requirements may be stated in the trust deed or the fiscal agency agreement and depend on the agreement of the parties involved.

[64] An arrangement under which a party promises to pay a certain sum regularly to another party within a specified time frame.

1. Fiscal Agent Structure

The issuer or noteholders holding not less than 10% of the nominal amount of the bonds or notes for the time being outstanding may convene a meeting of bondholders or noteholders.

The quorum is one or more persons holding or representing not less than 50% in nominal amount of the notes for the time being outstanding.

2. Trustee Structure

Bondholders or noteholders holding not less than 10% of the principal amount of the bonds and notes for the time being outstanding may convene a meeting of bondholders or noteholders, as may be applicable.

The quorum is two or more persons holding a clear majority of the principal amount of the bonds or notes for the time being outstanding (except where the business of the meeting covers certain reserved matters, a higher threshold is required).

Resolutions passed in a meeting of bond- or note-holders, or simply written resolutions of holders holding a specified per cent of the aggregate principal amount of outstanding bonds would be binding on all holders of the bonds.

Usually any changes to the terms would have to be agreed to by the issuer. Practically speaking, bondholders' meetings, other than in the case of default, are generally only convened by the Issuer.

S. Bankruptcy Procedures

Any bond issuers declaring bankruptcy are subject to the relevant rules set out in the CWUMPO. In the case of Hong Kong, China, the Bankruptcy Ordinance (Chapter 6 of the Laws of Hong Kong) generally only applies to individuals.

The ranking of a bond among an issuer's overall debt is determined by taking into account the terms and conditions set out in the prospectus, offer documents, term sheets or similar documents, as well as section 38 (Priority of Debts) of the Bankruptcy Ordinance and section 265 of the CWUMPO.

The insolvency law in Hong Kong is contained in the Companies (Winding Up and Miscellaneous Provisions) Ordinance, the Bankruptcy Ordinance and the Companies (Winding-up) Rules. It is based on the law of the United Kingdom, prior to the introduction of the Cork Report. Like the regimes in Australia and New Zealand, which are also based on the laws of the United Kingdom, it is generally creditor friendly.

Out-of-court restructuring, schemes of arrangement, compulsory liquidations, creditors' voluntary liquidations, and receiverships are available under the insolvency law. No corporate rescue procedure is currently available.

Further details on the restructuring and insolvency frameworks of Hong Kong, China and other Asia-Pacific economies can be found in *The Asia-Pacific Restructuring and Insolvency Guide 2006* and *A Guide to Asia-Pacific Recovery and Insolvency Procedures*.[65]

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[65] Clifford Chance. 2013. *A Guide to Asia-Pacific Recovery and Insolvency Procedures*. http://financialmarketstoolkit.cliffordchance.com/en/financial-markets-resources/resources-by-type/guides/restructuring-and-insolvency-guide-asia-pacific.html

T. Event of Default and Cross-Default

1. Terms of Event of Default

Events of default are a matter of negotiation, but generally cover nonpayment of principal or interest by the issuer; noncompliance with obligations under the bond instruments; nonpayment of other indebtedness of the issuer or guarantor when due; and the occurrence of certain specified events, for example, change of control; commencement of proceedings against the issuer; or the passing of an effective resolution for the winding up, administration, or dissolution of the issuer or guarantor.

Events of default are usually described in the Terms and Conditions of the Bonds.

2. Declaration of Default

a. Fiscal Agent Structure

Bondholders or noteholders may give written notice to the issuer to declare that the bonds or notes would become forthwith due and payable. This direct right is contained in a deed of covenant.

b. Trustee Structure

The trustee may, at its discretion, give notice of default by

(i) declaring the bonds or notes immediately due and repayable (with a certified opinion that the event is materially prejudicial to the interests of the holders of the bonds or notes); or

(ii) if so directed in writing by the holders of at least 25% in principal amount of the bonds or notes, or by an extraordinary resolution of the holders of the bonds or notes, declaring all the bonds or notes immediately due and repayable.

The trustee may institute proceedings against the issuer to enforce repayment of the principal of the bonds or notes with accrued interest and to enforce the provisions of the trust deed. However, the noteholders are not entitled to proceed directly against the issuer unless the trustee fails to do so within a reasonable period and such failure is continuing. The noteholders’ interests are represented by the trustee.

c. Time of Event of Default

The default may happen at any time during the day.

3. Cross-Default

Debt securities issued in Hong Kong, China, including those issued by government-related corporations and large corporates may carry in their issuance documentation and terms and conditions a cross-default clause that allocates the right for bondholders or noteholders to seek immediate repayment of all debt securities by the same issuer held by them in case an event of default would be declared on a single bond or note of such issuer.

In practice, a bondholder or a group of bondholders holding a certain percentage of bonds or notes of an issuer have the right to call an event of default if the issuer fails to make a payment of principal or interest in respect of ‘borrowed money’ in an amount above a certain threshold. The threshold may be determined in the issuance documentation.

IV

Bond and Note Transactions and Trading Market Infrastructure

A. Trading of Bonds and Notes

In Hong Kong, China, bonds and notes can be traded either OTC or on an exchange. Bonds and notes transacted in the secondary market are typically traded OTC via negotiations between buyer and seller. Most transactions take place over the telephone or via voice broker. At the same time, the trading on exchange of listed bonds and notes on the main board of SEHK is also possible, although the volume is negligible.

The dealing in unlisted debt securities is regulated by provisions in the SFO and the Companies (Winding Up and Miscellaneous Provisions) Ordinance. In turn, the SFC prescribes acceptable practices for the distribution and dealing of unlisted debt securities in the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission. Those unlisted debt securities issued via private placement may only be offered, sold to, and traded with Institutional Investors at any time.

The trading of listed debt securities is subject to the Trading Rules of SEHK. More information can be found in the individual sections of this chapter and other relevant sections in this Bond Market Guide.

B. Trading Platforms

Trading of bonds and notes in the Hong Kong bond market can be done in the OTC market or on an exchange.

The issuance of debt securities to professional investors in the OTC market does not preclude subsequent trading on SEHK, but these securities are offered to professional investors only, typically institutions, in the expectation that they will trade the relevant securities off exchange with other professional investors. Liquidity for secondary market trading on SEHK may be limited as a result.

1. Over-the-Counter Market

The traditional OTC market itself is less so a trading platform but instead an organized market. Trades in bonds and notes are concluded directly between institutional counterparties via phone or using the services of a voice broker or inter-dealer broker. Individual dealers may also use Bloomberg or similar global trading system providers, and/or an in-house trading system to carry out bond and note trading activities.

2. Electronic Trading Platform

Launched in December 2007, the Electronic Trading Platform is one of the recommendations arising from the Review of Debt Market Development completed by the HKMA in 2006. The platform provides the necessary infrastructure to support electronic trading of EFBNs and can be extended to cover other bonds and financial instruments available in the market. The platform increases price transparency among market players and streamlines the trading process. Market players can identify their trade counterparties and conclude deals more efficiently. Overseas as well as local market players are encouraged to use this platform to trade bonds and other financial instruments issued in Hong Kong, China.

3. Trading on Exchange

Debt securities issued in Hong Kong, China may be listed and traded on SEHK. Trading on SEHK, including for debt securities, happens through a number of sessions from pre-open at 9 am to the end of the afternoon session at 4 pm, Mondays to Fridays (see Table 4.1). There is no trading on Hong Kong, China public holidays. When a holiday falls on a Sunday, the following Monday will become a replacement holiday.

Table 4.1: Hong Kong Exchanges and Clearing Limited Debt Securities Trading—Trading Hours

Auction Session	
Pre-opening Session*	9 a.m. – 9:30 a.m.
Continuous Trading Session	
Morning Session	9:30 a.m. – 12 noon
Extended Morning Session	12 noon – 1 p.m.
Afternoon Session	1 p.m. – 4 p.m.

* No order and trade activities are allowed during the blocking period between 9.28 a.m. and 9.30 a.m. For more details, see http://www.hkex.com.hk/eng/market/sec_tradinfra/Documents/preopenfaq.pdf
Notes: There is no Extended Morning Session or Afternoon Session on the eves of Christmas, New Year's Day, and the Lunar New Year. There will be no Extended Morning Session if there is no Morning Session.
Source: Hong Kong Exchanges and Clearing.

HKEX carries on its website substantial information on the securities trading infrastructure, trading information, as well as information on Exchange Participants, news and rules and circulars.[66]

C. Mandatory Trade Reporting

At present, there is no mandatory reporting of OTC transactions in the Hong Kong bond market. Trades in CMU Instruments result in instructions for settlement through participant accounts maintained with CMU.

[66] See http://www.hkex.com.hk/eng/market/sec_tradinfo/CMTradInfo.htm

Trades executed on HKEX are reported on its information service as a matter of course. It is the duty of Exchange Participants to input the details of sale transactions concluded by them into the exchange's system within the time prescribed by the Trading Rules.[67]

D. Market Monitoring and Surveillance in the Secondary Market

There is no market-wide surveillance for bond and note trading in the OTC market in Hong Kong, China.

The Market Monitoring and Surveillance Department at HKEX is responsible for monitoring the trading activities of Exchange Participants in cash and derivatives markets, as well as China Connect trading activities, and their compliance with rules and regulations, position limits, and large open position reporting requirements in derivatives contracts; and performing due diligence check on admission of market makers. It also cooperates with regulators in Hong Kong, China and the PRC on their investigation of local and cross-boundary market misconduct under China Connect. It also acts as the primary contact and representative of HKEX to deal with matters related to HKEX membership, such as exchanging information among members to perform intermarket and intra-market surveillance through the Intermarket Surveillance Group that was established to assist in the detection and prevention of fraudulent and manipulative acts and practices to protect investors and the public interest.

E. Bond Information Services

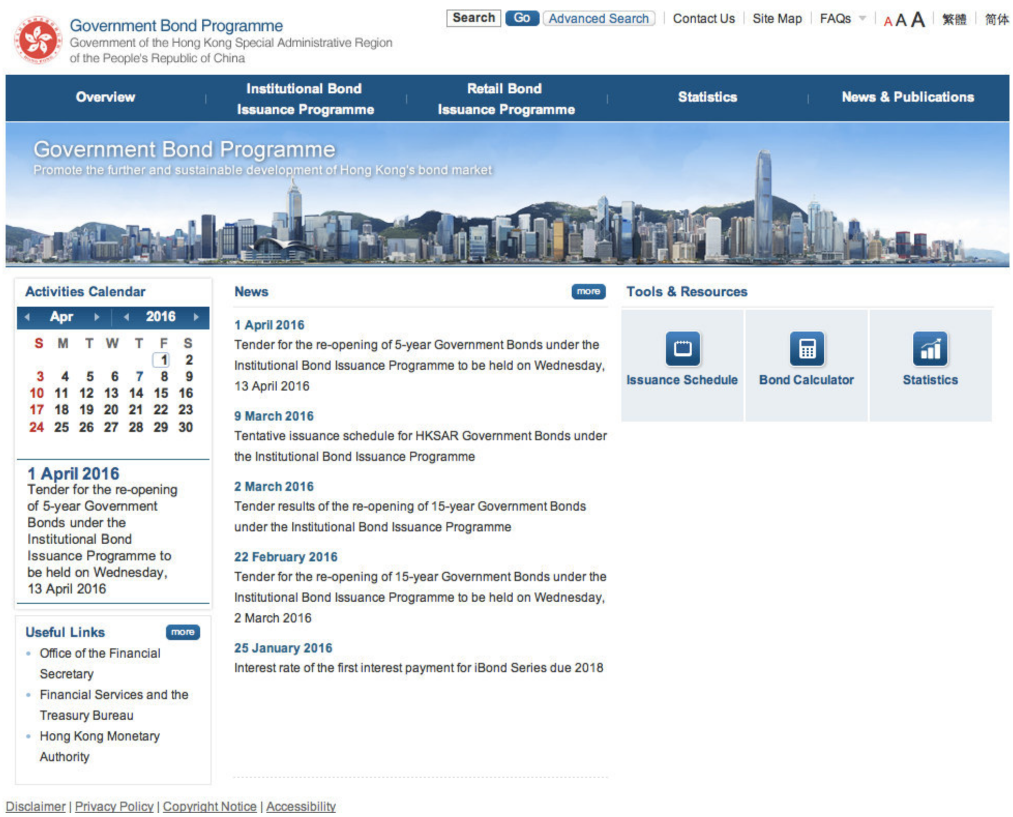
Information on bonds and notes issued in Hong Kong, China are easily available for both retail and professional investors through a number of official online resources, as well as market intermediaries and information vendors.

1. Government Bond Programme Website

The Government Bond Programme website (Figure 4.1) provides comprehensive information on the government's bond issuances for both the official Institutional Bond Issuance Programme and the Retail Bond Issuance Programme. The website features an overview of the purpose and objective of the issuance programs and contains an issuance calendar, tender information, indicative prices, as well as statistics and press releases (see also Chapter VII).

[67] OTC trades of unlisted bonds do not need to be reported to SEHK. Off-market trades of listed bonds are only required to be reported to SEHK if they are executed by or between Exchange Participants (see Chapter 5 of the SEHK Trading Rules). An authorized ATS provider effecting trades (of listed or unlisted bonds) on its platform may (on a case-by-case basis) be required by the SFC to periodically report the trade statistics to the SFC under the ATS authorization.

Figure 4.1: Hong Kong Special Administrative Region Government Bond Programme Homepage

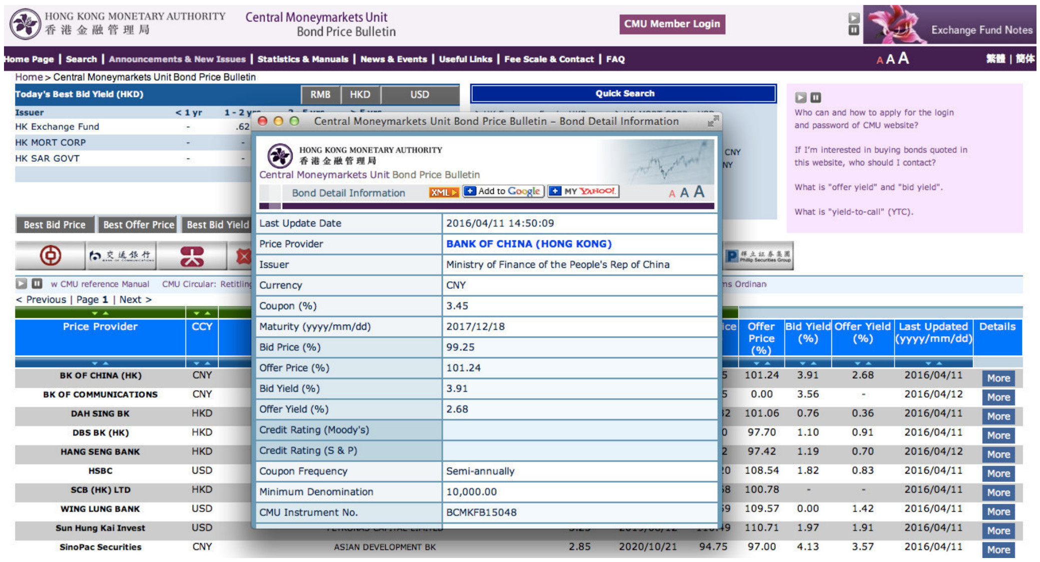


Source: Hong Kong Special Administrative Region Government Bond Programme. http://www.hkgb.gov.hk/en/index.html

2. Hong Kong Monetary Authority

In addition to information on the Hong Kong Exchange Fund and its debt issuances, the HKMA also provides the CMU Bond Price Bulletin, a dashboard-style web page with news on CMU Instruments, quoted bid and offer prices (see Chapter III.K), and yields. Detailed information on bonds is viewable in a pop-up window for each of the instruments displayed on the page (Figure 4.2). The current Exchange Fund Note Information Memorandum is available for download by clicking the tab in the top right corner.

Figure 4.2: Central Moneymarkets Unit Bond Price Bulletin – Bond Details Information



Source: Hong Kong Monetary Authority. Central Moneymarkets Unit. https://www.cmu.org.hk/cmupbb_ws/eng/page/wmp0100/wmp010001.aspx

3. Hong Kong Exchanges and Clearing Limited

HKEX provides, on its website under the Debt Securities tab,[68]selected general information on debt securities, including its Debt Securities Leaflet for download by interested parties. In addition, the section also contains the list of debt securities issued to the public and to professional investors, a glossary and frequently asked questions, as well as information on debt securities aimed only at professional investors, which are further referred to as Professional Debts.

F. Yields, Yield Curves, and Bond Indices

1. Government Bond Yields and Yield Curves

Indicative pricing and benchmark yields of Government Bonds issued under the Institutional Bond Issuance Programme are available for download from the Government Bond Programme website.[69] The data is prepared in Excel format by the HKMA as section 9 of its Monthly Statistical Bulletin (Figure 4.3).

[68] See https://www.HKEX.com.hk/eng/prod/secprod/debt/debt.htm
[69] See http://www.hkgb.gov.hk/en/statistics/statistic.html

Figure 4.3: Prices and Yields of Government Bonds Issued under the Institutional Bond Issuance Programme (End-of-Period Figures)

Table 9.4 : Prices and yields of Government Bonds issued under the Institutional Bond Issuance Programme[1, 2]

機構債券發行計劃下政府債券的價格及收益率[1, 2]

Table 9.4.1 End of period figures 期末數字 (percent per annum) (年率)

			Benchmark yields 基準收益率									
			Indicative Pricings 指示價格					Closing Reference Rates 收市參考價				
			2-year 2 年	3-year 3 年	5-year 5 年	10-year 10 年	15-year 15 年	2-year 2 年	3-year 3 年	5-year 5 年	10-year 10 年	15-year 15 年
2015	Jan	1月	0.360	0.639	0.897	1.552	-	0.374	0.624	0.876	1.546	-
	Feb	2□	0.407	0.743	1.254	1.687	-	0.399	0.739	1.248	1.687	-
	Mar	3□	-	0.741	1.150	1.590	-	-	0.741	1.122	1.576	-
	Apr	4□	-	0.620	1.182	1.628	-	-	0.623	1.138	1.638	-
	May	5□	-	0.616	1.126	1.701	-	-	0.605	1.115	1.711	-
	Jun	6□	-	0.535	1.087	1.788	-	-	0.542	1.105	1.836	-
	Jul	7□	-	0.613	1.156	1.844	2.170	-	0.621	1.168	1.862	2.179
	Aug	8□	-	0.620	1.122	1.803	2.103	-	0.620	1.122	1.802	2.095
	Sep	9□	-	0.440	0.854	1.534	1.783	-	0.444	0.853	1.533	1.785
	Oct	10□	-	0.692	0.854	1.525	1.828	-	0.696	0.866	1.551	1.851
	Nov	11□	-	0.790	1.206	1.578	1.862	-	0.792	1.206	1.589	1.866
	Dec	12□	-	0.817	1.304	1.662	1.937	-	0.860	1.307	1.675	1.940
2016	Jan	1月	-	1.061	1.395	1.833	2.001	-	0.994	1.371	1.794	1.927
	Feb	2月	-	0.745	1.108	1.383	1.822	-	0.744	1.108	1.382	1.822
	Mar	3月	-	0.765	0.909	1.318	1.717	-	0.730	0.904	1.283	1.681

1. Figures powered by Thomson Reuters.
數據由湯森路透提供。

2. Calculation method and further information are set out in the Reference Manual for Government Bond Indicative Pricings (http://www.hkgb.gov.hk/en/others/documents/IndicativePricings_Manual.pdf).
計算方法及相關資料請參閱政府債券指示價格參考手冊(英文版本)(http://www.hkgb.gov.hk/en/others/documents/IndicativePricings_Manual.pdf)。

Source: Hong Kong Government Bond Programme, http://www.hkgb.gov.hk/en/statistics/statistic.html

Figure 4.4: Government Bond Yields and Yield Movements on *AsianBondsOnline*

ADB AsianBondsOnline
An ASEAN+3 Initiative

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Hong Kong, China

Market-at-a-Glance | Data | Market Structure | ABMF | Guide To Buying Bonds | Market Summary | News

Currency: Hong Kong Dollar (HKD)

Market Watch

Close of April 6, 2016		CHANGE FROM		
Govt. Bond Yields	Latest Yield	Previous Day	Previous Week	YTD
2 Year	0.614	▲ 2.3	▼ 3.2	▲ 9.8
5 Year	0.941	▲ 0.9	▼ 9.8	▼ 15.2
10 Year	1.267	▲ 4.3	▼ 6.7	▼ 31.2

* Government bond yield changes are expressed in basis points.
>> More details

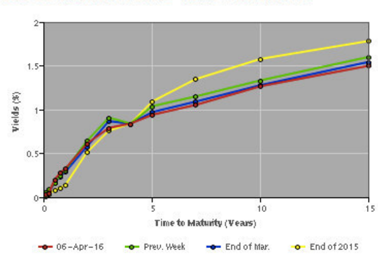
Currencies	Latest Rate	Previous Day	Previous Week	YTD
HKD per USD	7.757	▲ 0.0	▼ 0.0	▼ 0.1
HKD per JPY	0.071	▼ 0.5	▼ 2.4	▼ 9.6

* Exchange rate changes are expressed as a percentage change.
>> More details

Interest Rates	Latest Rate	Previous Day	Previous Week	YTD
1D HIBOR	0.061	▼ 0.4	▼ 0.3	▲ 1.4
3M HIBOR	0.556	▼ 0.1	▼ 0.6	▲ 16.2

* Interest rate changes are expressed in basis point change.
>> More details

LCY GOVERNMENT BOND YIELD MOVEMENTS



NEWS HIGHLIGHTS

- External merchandise trade statistics for February 2016
- Provisional statistics of retail sales for February 2016
- February CPI up 3.1%
- Has the Global Scare Over China Eased? Hong Kong Dollar Says Yes
- Exchange Fund foreign assets up

CPI = consumer price index, LCY = local currency, YTD = year to date.
Source: *AsianBondsOnline*. Selected Government Bond Yields and Yield Movements.

In addition to yields for specific benchmark issues, an aggregate Government Bond yield curve for selected periods, as well as many more data points can also be accessed using the *AsianBondsOnline* website.[70] An example of the yield data and composite curve style of display is shown in Figure 4.4.

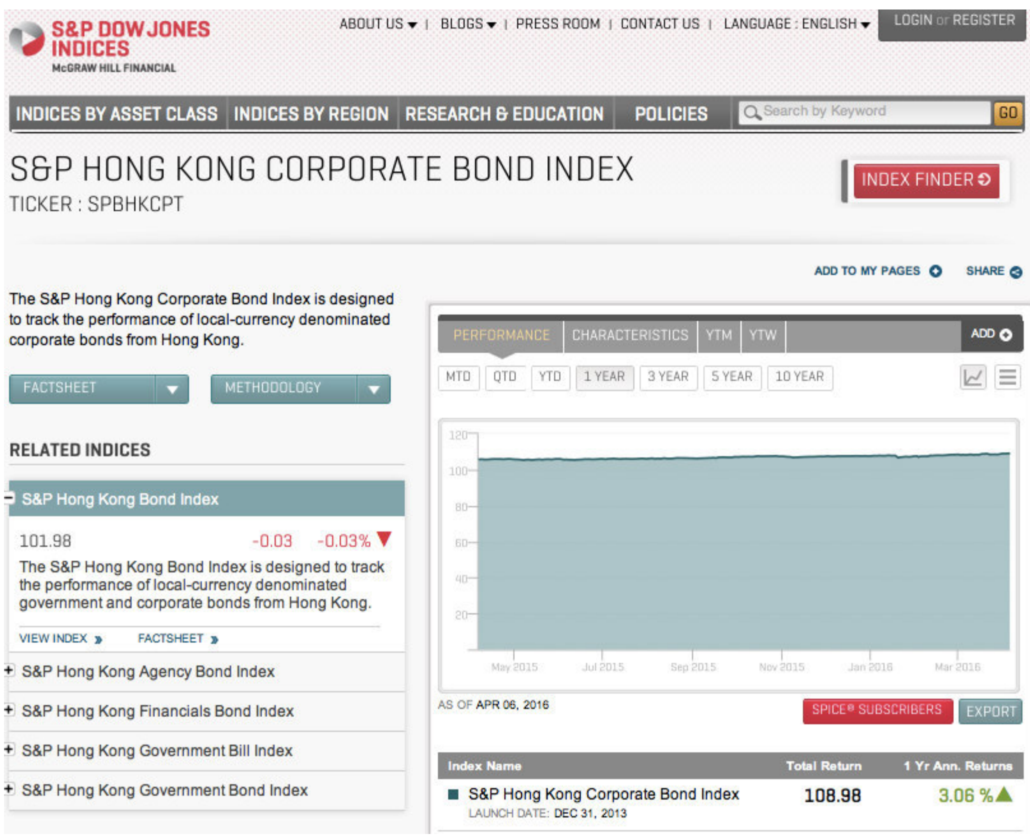
2. Other Bond Yields—Exchange Fund Bonds and Notes

HKMA also makes EFBN yields available for download from its website.[71] HKMA also publishes the yield data, as well as much other information for EFBNs, on its CMU Bond Price Bulletin web page. For details, please also refer to E.2 in this chapter.

3. Bond Indices in Hong Kong, China

HKMA does not issue official indices for the Hong Kong bond market. Instead, bond indices that include bonds and notes issued in Hong Kong, China are available from securities market participants and data vendors, respectively.

Figure 4.5: Screenshot of S&P Hong Kong Corporate Bond Index



Source: Standard and Poor's. Hong Kong Corporate Bond Index. http://us.spindices.com/indices/fixed-income/sp-hong-kong-corporate-bond-index.

The Citi Asian Government Bond Index (AGBI) comprises local currency Asian government bonds, providing a broad benchmark for the Asian sovereign market. The AGBI rules and methodologies are consistent with those of the World Government

[70] See http://asianbondsonline.adb.org/singapore/data/marketwatch.php?code=government_bond_yields
[71] HKMA. Market Data and Statistics. http://www.hkma.gov.hk/eng/index.shtml

Bond Index in order to enable performance comparisons across sovereign debt markets. The index provides exposure to a broad array of countries and subindexes are available in any combination of currency, maturity, and rating. Coupon-bearing government bond issues with a minimum issue size of HKD800 million are included in AGBI and its subindexes.[72]

In turn, the S&P Hong Kong Corporate Bond Index (Figure 4.5) is an example of the bond indices tracked by securities market information providers, and available in the public domain.

G. Repo Market

1. Repo Market Overview

The repo market in Hong Kong, China is relatively small when compared to lending conducted through the unsecured interbank and foreign exchange swap markets despite having the necessary infrastructure for, and no legal or tax impediments to, conducting repo. This is largely because the relevant institutions are more used to obtaining Hong Kong dollar funding through the two abovementioned channels. Nonbank financial institutions do not generally conduct repo in Hong Kong, China.[73]

There are generally no restrictions on participation in the Hong Kong, China repo market. Nevertheless, participation has been largely confined to financial institutions (particularly the banks) and money brokers and dealers. This notwithstanding, financial institutions are more used to obtaining funding via the unsecured interbank market or via foreign exchange swaps for two reasons. First, there has not been a large stock of government securities or central bank paper for banks to conduct repo in Hong Kong dollars. Secondly, since the Hong Kong dollar is pegged to the US dollar, which has much deeper and more liquid markets, banks can obtain Hong Kong dollar funding through the US dollar and foreign exchange swap markets with relative ease.

Repo transactions between financial institutions are sometimes conducted via inter-dealer brokers for reasons of convenience and anonymity, although banks also rely on other bilateral and tripartite repo services from time to time. Abundant Hong Kong dollar liquidity in the system in recent years has reduced banks' funding needs in general, whether in the form of unsecured lending or repos.

Banks are allowed to obtain temporary liquidity through the discount window provided by HKMA using repurchase agreements with EFBNs as collateral.

2. Acceptance of Standards

The Global Master Repo Agreement (GMRA) is the standard legal documentation used in the local repo market. Banks in Hong Kong, China are reportedly more used to executing GMRA bilaterally under their own entity names due to established practice. In other words, instead of using a Hong Kong, China annex, they typically execute a standalone GMRA for conducting Hong Kong dollar repo trades.[74]

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[72] Citi Fixed Income Indices. 2016. *Index Guide*. https://www.yieldbook.com/f/m/pdf/citi_indices/Citi_Indx_Guide_20160304_WEB.pdf

[73] Adapted from Executives Meeting of East Asia–Pacific Central Banks. 2014. *EMEAP Repo Markets: State of Play—A Report by the EMEAP Working Group on Financial Markets*. http://www.emeap.org/emeapdb/upload%5CWGMeeting%5CEMEAP_Working_Group_on_FinancialMarkets_-_Report_on_EMEAP_Repo_Markets_....pdf

[74] See Footnote 57.

3. Specific Repo Practices

This section summarises a number of relevant practices in the repo market in Hong Kong, China. Most repo transactions occur in the interbank (OTC) market. A certain number of repo transactions are conducted on SEHK.[75]

a. Type of Repo

Repo transactions in Hong Kong, China represent the classic repo type, which is the outright sale and simultaneous (re)purchase of securities.

At the same time, the underlying legal and taxation infrastructure in Hong Kong, China does not prohibit the pledged type of repo transaction.

b. Size and Tenure

Repo transaction may be conducted for any tenure or size, in line with market acceptance of such conditions. Owing to the fact that there is no specific Hong Kong, China annex to the GMRA, conditions are typically agreed bilaterally between counterparties.

c. Eligible Debt Securities as Collateral

There are no restrictions or limitation on the eligible securities in Hong Kong, China.

Most of the repo transactions among financial institutions are conducted using either government bonds or EFBNs. For the purposes of funding, use of other securities (e.g., corporate bonds, asset-backed securities, or equities) are not as common as these securities are either less liquid or subject to more volatile price movements.

The Hong Kong, China repo market infrastructure allows substitution of collateral during the term of the repo but it is not standard practice among participants.

For eligible securities in repo transactions between Authorized Institutions and HKMA, please see Section 4.

d. Closeout Netting

There are no specific prescriptions in Hong Kong, China for the closeout netting of repo transactions. However, provisions for closeout netting are commonly included in Master Agreements (e.g., ISDA Master Agreement) that bind the market participants to established practices.

e. Accounting and Tax Treatment

Under the tax laws of Hong Kong, China, stock borrowing and lending transactions (including repo transactions) where specific criteria are satisfied, require no stamp duty to be payable. This means the tax treatment is that of a loan rather than an outright purchase and sale of securities.

[75] Adapted by ADB Consultants for SF1 from a 2016 ASEAN+3 SRO Working Group case study on repo markets, with the kind permission of the author.

The difference between the sale and (re)purchase amount is considered as interest income in substance, which may be subject to profits tax.

Most funding-driven repo transactions are conducted using EFBNs and government bonds, which do not attract any taxation even for outright purchases and sales.

f. Market Participants

Financial institutions in Hong Kong, China conduct repo transactions with both local and international market players. For the local market, clearing and settlement of repo transactions can be conducted through, amongst other channels, the bank repo platform administered by the CMU as delivery-versus-payment transactions.

The cash lenders tend to be money market funds, mutual funds, or treasury desks from banks, corporates, insurance companies, or the HKMA repo desk. The bond lenders include dealers and bond traders, hedge funds, proprietary trading desks, or repo desks.

The CMU also provides cross-border collateral management service with the global tripartite platforms, Euroclear, J.P. Morgan, and Clearstream. To further enhance the cross-border collateral management service, delivery-versus-payment links between Hong Kong's RTGS systems and the tripartite repo systems have been established to enable liquidity movements to be done in Hong Kong's RTGS systems while the collateral movements are done concurrently through the repo platform.

There are no restrictions on the entrance of foreign investors into the Hong Kong bond market for repo transactions.

4. Introduction of Intraday Repo under the Renminbi Liquidity Facility

In November 2014, the HKMA announced the provision of renminbi intraday liquidity to Authorized Institutions participating in renminbi transactions in Hong Kong, China via repo.[76]

Under an existing RMB Liquidity Facility, the HKMA had already provided overnight funds on a T+0 basis as well as 1-day and 1-week funds settled on a T+1 basis. In light of the increased volume of payments alongside the growth of the offshore renminbi market, the HKMA started to provide intraday renminbi funds of up to CNY10 billion to assist Participating Authorized Institutions in managing their renminbi liquidity and to promote efficient payment flows in Hong Kong, China. This also provided banks with greater flexibility in managing their payment flows upon the launch of the Shanghai–Hong Kong Stock Connect.

Participating Authorized Institutions may initiate a sale and repo transaction with the HKMA to obtain intraday renminbi funds. The HKMA will charge a fee, based on the actual time of usage, with reference to the prevailing overnight interest rate. The list of securities eligible for the previously existing renminbi liquidity facility was expanded to include renminbi bonds issued by the PRC's policy banks in Hong Kong, China.

In light of its experience operating the facility and given developments in the offshore renminbi market, the HKMA has made enhancements to the facility. Please refer to the HKMA website for more details.[77]

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[76] Reference is made to the announcement of the new facility by HKMA at www.hkma.gov.hk/eng/key-information/press-releases/2014/20141103-4.shtml

H. Securities Borrowing and Lending

Since the introduction of the exemption from stamp duty for properly executed securities borrowing and lending (SBL) transactions, Hong Kong, China has emerged as a regional SBL center.

Legally, SBL falls under the covered short selling provisions in sections 171 and 172 of the SFO. According to the SFC Guidance Note on Short Selling Reporting and Stock Lending Record Keeping Requirements, a securities borrowing and lending agreement is defined in Schedule 1 of the SFO as an agreement whereby a person borrows or lends securities pursuant to an arrangement where the borrower undertakes to return securities of the same description to the lender or pay the equivalent value of the securities. The definition expressly includes a securities borrowing within the meaning of section 19(16) of the Stamp Duty Ordinance. Relief from payment of the Hong Kong, China stamp duty is available under section 19 of the Stamp Duty Ordinance, in which securities are borrowed pursuant to a stock borrowing and lending agreement.

SBL transactions in Hong Kong, China, may be executed on SEHK or using the CMU Lending Programme.

1. Securities Lending on Hong Kong Exchanges and Clearing Limited

The 6th Schedule to the SEHK Trading Rules contains the Securities Borrowing and Lending Regulations of HKEX.[78] An Exchange Participant shall be permitted to borrow or lend securities only in accordance with these regulations or the CCASS Rules (as the case may be) and, where the securities borrowing relates to Hong Kong stock, with applicable law and in particular the Stamp Duty Ordinance and the relevant Stamp Duty Interpretation and Practice Notes of the Internal Revenue Department of Hong Kong.

Compulsory stock borrowing to close out overdue positions in CCASS was introduced by HKSCC in May 1999. The underlying Compulsory Stock Borrowing and Lending Regulations are contained in Appendix 6 to the CCASS Rules. Participants require a stock lending account in CCASS (one per Participant). The opening of a stock lending account needs to be advised to the Collector of Stamp Revenue of the Internal Revenue Department in order for the lender to avail themselves of a stamp duty exemption (see also Section 4).

Collateral is required for all SBL transactions executed through SEHK. Normal SBL transactions will need to be collateralized at 100% at all times; transactions in support of short sales (which are defined in the 11th Schedule to the Trading Rules) are required to be collateralized at 105%. Uncovered securities borrowing positions are required to be marked to market at least daily, and an increase of the amount of collateral to 100% or 105% is required where the value of the collateral falls under the 100%, or 105%, respective levels. Collateral of higher value than the 100% or 105%, respectively, may be released by the lender to the borrower.

In contrast, Compulsory Stock Borrowing transactions in CCASS do not require HKSCC to deliver any form of collateral to the Lender.

[77] See http://www.hkma.gov.hk/eng/key-functions/monetary-stability/liquidity-support-to-banks.shtml
[78] See http://www.hkex.com.hk/eng/rulesreg/traderules/sehk/documents/sch-6_eng.pdf

2. Central Moneymarkets Unit Securities Lending Programme

CMU operates a Securities Lending Programme for debt securities issued by the private sector.[79] This program provides a mechanism for CMU Participants to lend or borrow CMU Instruments and Government Bonds issued under the Government Bond Issuance Programme (Eligible Instruments) through the CMU. All CMU Participants may participate in the program as a Lender. However, only Market Makers for Eligible Instruments under this program can borrow Eligible Instruments. Any Recognized Dealer for Government Bonds who is also a CMU Member may participate in the program as a lender and/or Borrower.

The maximum aggregate amount of each Loan of Eligible Instruments is 20% of the total issue size of those Eligible Instruments.

Borrowers shall be required to provide collateral but may substitute collateral pursuant to the rules of the Programme. Only EFBNs and those CMU Instruments eligible for repo under the discount window are eligible Collateral. If the Eligible Instruments are issued by the borrower itself, its subsidiaries, its holding company, or any subsidiary of that holding company, such Eligible Instruments are not allowed to be used by the Borrower as Collateral. All Borrowed Instruments and Collateral will be marked to market on a daily basis. A Borrower is required to top up any shortfall to ensure continuous compliance with the haircut requirements.

Lenders transfer Eligible Instruments they are willing to lend into their Lending Account, while Borrowers send Borrowing Requests on the required securities into the CMU system, which then matches and concludes the transaction.

For a detailed description of the Securities Lending Programme, interested parties are advised to download the CMU Reference Manual or check the descriptions on the HKMA website.

3. Eligible Debt Securities

For SBL transactions on SEHK, or via the compulsory stock borrowing in CAASS, only securities deposited and settled at CCAAS are eligible.

In the CMU Programme, Eligible Instruments are those CMU Instruments and Government Bonds issued under the institutional and retail tranches of the Government Bond Issuance Programme arranged by HKMA. The issue size of each of those eligible CMU Instruments must be of or over HKD500 million equivalent and have at least one CMU Participant who has agreed to act as the Market Maker of the issue.

4. Tax Treatment

Similarly to repurchase transactions, SBL transactions are considered loans rather than outright sales of securities. As such, no stamp duty is payable, provided that the lender has registered their lending agreement with the Internal Revenue Department.

The fee income for the lender from the SBL transactions may be subject to profits tax, unless the underlying securities qualify for a tax exemption.

[79] Adapted from CMU. 2016. *Reference Manual*. http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/infrastructure/cmu.shtml

5. Pan-Asian Securities Lending Association

The Pan-Asian Securities Lending Association (PASLA)[80] is an association of firms that are active in the business of borrowing and/or lending securities of Asian markets. PASLA was founded in Hong Kong in 1995, as Hong Kong is the regional headquarters for many financial firms, and it was and remains easy for borrowers and lenders to meet and resolve any issues; moreover, the credibility of counterparties in Hong Kong has always been high. Its meetings are held in Hong Kong.

At the time of the compilation of this bond market guide, PASLA had 63 member firms made up of 18 lenders, 35 borrowers, and 10 others who are domiciled across multiple continents. PASLA membership is open to both international firms, which are active in several markets, and local firms, which are active primarily in their home market.

PASLA, as a collective group of major firms in the industry, provides an important benefit to Asian securities regulators, stock exchanges, and monetary authorities by providing an industry consensus on issues that affect the development of the securities lending business. PASLA also provides country profiles and market information to its members.

I. Interest Rate and Fixed-Income Futures

Exchange traded interest rate futures are available in the Hong Kong bond market, while futures on fixed income products were discontinued.

1. Interest Rate Futures

HKFE's introduction of 1-Month HIBOR futures contracts on 20 October 1998 and 3-Month HIBOR futures contracts on 26 September 1997 provides a set of interest rate products that allow market participants to manage their interest rate exposures more effectively.

The 1-Month HIBOR and 3-Month HIBOR futures contracts are based on the 1-Month and 3-Month HIBORs (Hong Kong Interbank Offered Rate), which are the benchmarks for short-term interest rates in the Hong Kong dollar money market.

HIBOR futures are traded on the Hong Kong Futures Exchange Limited, a wholly owned subsidiary of HKEX. Details on the trading practices, contract specifications, trading hours, and other relevant information is available from the HKEX website.[81] Trading fees and commissions for HIBOR futures are also available on the HKEX website.[82]

2. Fixed-Income Futures

In December 2014, HKEX announced it would discontinue trading in its 3-year EFN Futures because the HKMA would stop issuing 3-Year EFNs in January 2015.

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[80] See http://www.paslaonline.com
[81] See https://www.HKEX.com.hk/eng/prod/drprod/DMProducts.htm
[82] See https://www.HKEX.com.hk/eng/prod/drprod/hkifo/fees.htm

V

Description of the Securities Settlement System

This chapter, as included in the original ASEAN+3 Bond Market Guide published in 2012 has been discontinued in favor of a more comprehensive and updated description in the Phase 2 Report of the ABMF Sub-Forum 2 (SF2), Information on Transaction Flows and Settlement Infrastructures, dated 13 June 2014. The SF2 Phase 2 Report contains information on the post-trade features of the Hong Kong bond market, its market infrastructure and settlement systems, interest payment and redemption practices, as well as market and message standards (pp. 108–120). In addition, the SF2 Phase 2 Report contains detailed infrastructure and transaction flow diagrams for the bond market in Hong Kong, China (pp. 375–397).

The SF2 report is available on a dedicated ADB website, as well as through a number of mirror sites.[83]

[83] See http://www.adb.org/publications/asean3-information-transaction-flows-and-settlement-infrastructures

VI

Bond Market Costs and Taxation

This chapter details the typical costs incurred by issuers and investors in the Hong Kong bond market, with a particular emphasis for costs associated with bond or note issuance and settlement.

For ease of reference, the descriptions of the types of costs are given in the context of the actions to be taken by issuers or investors (as explained in this document) and follow the lifecycle of a bond or note or in the Hong Kong bond market.

A. Costs Associated with Bond and Note Issuance

1. Submission of Application for Authorization to the Securities and Futures Commission (Public Offers)

All documents containing offers of bonds and notes to the public in Hong Kong, China require the authorization of the SFC. For details and conditions of the application process, please refer to Chapter II.F.

The SFC applies a fee for the application process, payable at the time of submission of the application and in case of any re-submission of amendments to the application or supporting documents. The fee is not refundable in the case of an unsuccessful application.

2. Arranger and Listing Sponsor Fee (Optional)

The appointment of an arranger or listing sponsor in the Hong Kong bond market is not mandatory. The sponsor or listing agent is, among other roles, responsible for the submission of listing applications and supporting information to the relevant regulatory authorities.

The arranger will charge a fee, which should be expected to follow established market practice and may be subject to negotiations between issuer and arranger.

3. Underwriter Fee (Optional)

Issuers are not required by law to appoint an underwriter in Hong Kong, China; often, the arranger performs the role of an underwriter as well. However, some offers of bonds and notes may require the services of one or more underwriters to place the debt securities with Institutional Investors or distribute the issuance to the public.

Underwriters charge a fee, typically commensurate with the effort and risk of taking over parts or all of a bond or note issue from the issuer. This fee or service charge should be expected to follow established market practice and may be subject to negotiations between issuer and underwriter(s).

4. Agent Fees (Mandatory and Optional)

In the Hong Kong bond market, the appointment of a number of agents in the context of a bond or note issuance is mandated to ensure effective and professional administration of the issue, a division of duties, and the observance of international best practice. The facility agent will administer the issuance process of debt instruments into the market, while a paying agent is responsible for handling the cash flow at issuance, for benefits arising from the issue, and upon redemption. The trustee holds the fiduciary responsibility towards the bond- or noteholders, and acts in the case of default or distress.

Facility and paying agents, as well as the trustee, are remunerated for their services based on market practice.

5. Central Moneymarkets Unit and Central Clearing and Settlement System Fees

Certain costs and fees are incurred by the issuer or issuing agent for the creation or admission of new debt securities in the CMU and CCASS, respectively. The fee schedules for both the CMU and CCASS are available from the websites of the HKMA and HKEX, respectively.[84]

a. Fees Relating to New Issues of a Central Moneymarkets Unit Instrument

The CMU levies a fee of HKD1,500 for every new issue of a CMU Instrument, which is to be borne by the issuer or issuing agent. The same fee applies for every instrument created through a CMU tender offer.

b. Fees Relating to Debt Securities in the Central Clearing and Settlement System

In principle, a registration and transfer fee applies for the re-registration of securities in the name of HKSCC Nominees Limited. However, this fee is not applicable for EFNs, government bonds, specified instruments, CMU Instruments, and foreign securities.

B. Ongoing Costs for Issuers of Corporate Bonds and Notes

Resident and nonresident (foreign) issuers in the Hong Kong bond market tend to appoint a commercial bank as the paying agent for their corporate bonds or notes. This service provision is likely to result in the following charges:

Interest Payment and Redemption Fees

a. Central Moneymarkets Unit Instrument

The CMU charges an income distribution service fee relating to CMU Instruments at a cost of HKD1,000 per issue and per income event. The cost is to be borne by the paying agent.

[84] See http://www.hkma.gov.hk/media/eng/doc/key-functions/finanical-infrastructure/infrastructure/CMU_Tariff.pdf

b. Debt Securities in the Central Clearing and Settlement System

HKSCC charges 0.12% of the aggregate of the cash amount of debt securities' interest paid to participants in one currency on the same day, subject to a maximum of HKD10,000 (or its equivalent in foreign currencies). The fee and other applicable bank charges will be deducted at source at the time of distribution to participants. The fee is also applicable to EFNs, government bonds, specified instruments, CMU instruments, and foreign debt securities.

A handling fee is charged for the conversion, redemption, and corporate actions of registered and bearer debt securities. The handling fee is also applicable to EFNs, government bonds, specified instruments, CMU instruments, and foreign debt securities.

HKSCC may also charge disbursements and other out-of-pocket expenses, as incurred, to participants.

C. Costs for Deposit and Withdrawal of Bonds and Notes

Deposit and withdrawal fees may only be applicable to eligible securities deposited and settled in CCASS.[85] CMU Instruments are in scripless form only.

1. Deposit Fee

The deposit of eligible securities into CCASS presently does not incur a fee.

2. Withdrawal Fee

The withdrawal of eligible bearer debt securities incurs a fee of HKD100 per certificate. A withdrawal of foreign debt securities incurs a fee of HKD600 per instruction plus reimbursement for out-of-pocket expenses incurred by HKSCC.

D. Costs for Account Maintenance at the Central Moneymarkets Unit and Central Clearing and Settlement System

1. Account Maintenance Fee at the Central Moneymarkets Unit

There is no account maintenance fee for CMU accounts. At the same time, a custodian fee applies to account holders that are institutions. (The CMU does not charge a custodian fee to accounts that are held by individuals.) The custodian fee is charged in basis points on a sliding scale on the basis of the monthly average nominal value of securities held in the CMU account. The fee is charged to CMU participants.

The custodian fee sliding scale is as follows:

Up to HKD15,000 million	0.32 basis points
HKD15,000–HKD20,000 million	0.30 basis points
Over HKD20,000 million	0.25 basis points

The CMU tariff also applies to holdings relating to the CMU's linkages with AustraClear in Australia, and Korea Securities Depository in the Republic of Korea.

[85] The current CCASS fee schedule for Depository and Nominee Services is available at https://www.HKEX.com.hk/eng/market/clr/secclr/feeschedule_hkscc/dns_fees/t3.htm

2. Account Maintenance Fee at the Central Clearing and Settlement System

HKSCC does not charge an account maintenance fee as such. Nonetheless, HKSCC charges a statement service fee of HKD10 per account per month for participants maintaining stock segregated accounts with statement service in CCASS.

The custody fee of bearer debt securities, EFNs, and specified instruments held in the CCASS Depository is charged at 0.012% (1.2 basis points) per annum on the nominal value calculated on a daily basis, subject to a maximum of HKD300,000 per month per participant (fee calculated on aggregate daily balance of nominal values of bearer debt securities, EFNs, and/or specified instruments in the account of each participant).

In the HKSCC fee schedule, the term Portfolio Fee is used only for China Connect securities, which does not include debt securities as of May 2016.

E. Costs Associated with Bonds and Notes Trading

1. Brokerage Fee (applicable to trades on the Stock Exchange of Hong Kong Limited)

Effective 1 April 2003, the brokerage of security transactions became freely negotiable between brokers and their clients.

2. Trading Fee (applicable to trades on the Stock Exchange of Hong Kong Limited only)

A trading fee of 0.005% per side of the consideration of a transaction (rounded to the nearest cent) is payable to SEHK. There is no trading fee on Securities Market Maker transactions.

3. Trading Tariff (applicable to trades on the Stock Exchange of Hong Kong Limited only)

A trading tariff of HKD0.50 is payable to SEHK on each and every purchase or sale transaction. The decision on whether or not to pass the trading tariff on to investors is at the discretion of brokers.

4. Transaction Levy (applicable to trades on the Stock Exchange of Hong Kong Limited only)

Effective 1 November 2014, a transaction levy of 0.0027% (rounded to the nearest cent) is charged per side of the consideration of a transaction, and the amount is collected for the SFC. There is no transaction levy on Securities Market Maker transactions.

5. Brokerage Fee (Unlisted Debt Securities)

Market participants trading unlisted debt securities for their investor clients in the OTC market may also charge brokerage fee or levy other such charges for each trade, subject to their own conditions and considerations.

F. Costs for Settlement and Transfer of Bonds and Notes

Settlement and transfer fees for CMU and CCASS transactions are described below.

1. Transaction Fee (Settlement and Transfer Fee)

a. Central Moneymarkets Unit Instrument

The CMU charges a transaction fee of HKD20 for all settlements of CMU Instruments, regardless of whether the settlement is done delivery-versus-payment or free-of-payment. In-house transfers, the movement of CMU Instruments between CMU accounts, attract a transfer fee of HKD10 per transfer.

Repo transactions other than a bank repo do not attract a transfer fee.

The CMU tariff also applies to transactions relating to CMU's linkages with AustraClear in Australia, and Korea Securities Depository in the Republic of Korea.

b. Debt Securities in the Central Clearing and Settlement System

The settlement fee applied by HKSCC depends on the nature of the trade as shown in Table 6.1.

Table 6.1: Settlement Fee for Hong Kong Exchanges and Clearing Limited Trades in the Central Clearing and Settlement System

Nature of Transaction		Fee Amount
Exchange Trade	Broker–broker trade	0.002% of gross value of an SEHK trade, subject to a minimum fee of HKD2 and maximum of HKD100 per side per trade
	Crossed trade (where the same Exchange Participant handles buy and sell side of a trade)	0.001% of gross value of a crossed trade, subject to a minimum fee of HKD1 and maximum of HKD50 per side per trade
SI Transaction	Broker–custodian or clearing agency participant transaction	0.002% of gross value of an SI transaction, subject to a minimum fee of HKD2 and maximum of HKD100 per side per SI transaction
	Other SI transactions (e.g., stock borrowing or lending, stock pledging, and portfolio movement)	0.002% of gross value of a SI transaction, subject to a minimum fee of HKD2 and maximum of HKD100 per side per SI transaction
ISI Transaction	Investor–broker or custodian participant transaction	Nil

ISI = Investors Settlement Instruction, SI = Settlement Instruction, SEHK = The Stock Exchange of Hong Kong Limited.
Source: Compiled by ADB Consultants for SF1 from Hong Kong Exchanges and Clearing Limited Fee Schedule and Clearing and Settlement Services.
https://www.hkex.com.hk/eng/market/clr/secclr/feeschedule_hkscc/cco_fees/t1.htm

The transfer of EFNs and/or specified instruments between a participant and a recognized CMU dealer is charged the same tariff as a Transfer Instruction.[86]

[86] Please see the full fee schedule for Transfer Instructions in the CCASS Tariff (Section 21.3A) at http://www.hkex.com.hk/eng/rulesreg/clearrules/ccassop/documents/sec21.pdf

HKSCC may charge disbursements and out-of-pocket expenses in connection with clearing and settlement services to participants as incurred.

G. Taxation Framework and Requirements

Residents and nonresidents investing in the Hong Kong bond market are charged no withholding tax on fixed income from debt securities. Table 6.2 provides and overview of the applicability of and practices for the relevant taxes, with details explained in the subsequent sections.

Table 6.2: Duties and Taxes on Fixed-Income Securities in Hong Kong, China

Duties and Tax	Type of Bond	Tax Rate
Withholding Tax	Government	Not applicable
	Corporate	Generally, no withholding tax
Capital Gains Tax	Government	Not applicable
	Corporate	Not applicable
Stamp Duty	Government	Stamp duty on SEHK transactions: 0.1% of the value of the transaction on both the buyer and the seller Stamp duty on contract notes: HKD1 for every HKD1,000 and part thereof on the transaction value [a]
	Corporate	
GST and VAT	Universal	Not applicable

GST = goods and services tax, SEHK = The Stock Exchange of Hong Kong Limited, VAT = value-added tax.
[a] See stamp duty conditions under Section 4.
Source: Compiled by ADB Consultants for SF1 from public domain sources.

1. Profits Tax

Full exemption from profits tax for interest income and trading profits with respect to certain debt instruments is granted under section 26A of the Inland Revenue Ordinance.[87] These debt instruments include, among others, long-term debt instruments with an original maturity of not less than 7 years.

In addition, pursuant to section 14A of the Inland Revenue Ordinance, a tax concession at 50% of the normal profits tax rate is applied to interest income and trading profits derived from a debt instrument that satisfies the following criteria:

a. it is lodged with and cleared by the CMU operated by the HKMA;
b. it has an original maturity of not less than 3 years but less than 7 years;
c. it has a minimum denomination of HKD50,000 or its equivalent in a foreign currency;
d. it is issued to the public in Hong Kong; and
e. it is issued by a person and has at all relevant times a credit rating acceptable to the HKMA from a credit rating agency recognized by the HKMA.

2. Withholding Tax

[87] See http://www.hklii.org/eng/hk/legis/ord/112/s26A.html

Residents and nonresidents investing in the Hong Kong bond market are charged no withholding tax on dividends and fixed income. Interest income derived from bond holdings is not taxable for individuals.

For corporations, interest on bonds issued by the government and government related entities are not taxable; other interest is taxable if it has a Hong Kong, China source. Thus, interest on a corporate bond listed on SEHK is taxable.

3. Capital Gains Tax

There is no capital gains tax in Hong Kong, China.

4. Stamp Duty

In principle, a stamp duty is applicable on securities, including debt securities traded in Hong Kong, China. However, a stamp duty is only applicable to shares and those registered debt securities that are not considered loan capital. In turn, most debt securities are structured so that no stamp duty is payable.

Under the Stamp Duty Ordinance, the stock of the transfer which is *required to be registered in Hong Kong, China* is subject to stamp duty. There are various exclusions to the definition of stock, including any Exchange Fund debt instrument, certain non-HKD-denominated debt securities, etc. Part VA of the Stamp Duty Ordinance also provides relief for certain types of *sukuk*.

If a stamp duty is payable, the following applies:

a. Stamp duties and transaction levies are payable on transactions by both buyer and seller. Both the buyer and seller are charged at 0.1% of the consideration by the Inland Revenue Department of Hong Kong, China. Any fraction in the ad valorem stamp duty will be rounded up to the nearest HKD1.

b. A transfer stamp duty must be paid by the seller on transactions for securities, which are physically settled and not cleared in CCASS. This transfer stamp duty is charged at the rate of HKD5 per transfer deed by the Inland Revenue Department of Hong Kong, China.

For trades executed on SEHK, the stamp duty is included in the contract note issued by the broker. The broker pays ad valorem stamp duty on behalf of their clients on T+2. It is the responsibility of the investor to ensure that stamp duty is paid at the correct rate or else severe penalties can be imposed for nonpayment under the Stamp Duty Ordinance.

5. Value-Added Tax or Goods and Services Tax

There is no value-added tax or goods and services tax in Hong Kong, China.

6. Double Taxation Agreements

There is principally no withholding tax on interest from debt securities in Hong Kong, China. Hence, there are no double taxation agreements with respect to interest received on debt securities issued in Hong Kong, China and no tax reclamation procedures are applicable.

7. Tax Exemption for Nonresident Investors

A tax exemption for nonresident investors is not applicable since Hong Kong, China does not have capital gains and withholding taxes on the income or considerations from debt securities.

VII

Market Size and Statistics

The original ASEAN+3 Bond Market Guide was published in April 2012 and included 11 pages of Hong Kong bond market statistics, including historical data such as bond holdings, bondholder distribution, outstanding amounts, and trading volumes. Not surprisingly, this data became stale soon after publication.

Since the ASEAN+3 Bond Market Guide is most likely to be updated only on a bi-annual basis, it is not the best channel for the dissemination of market statistics. Hence, a chapter comprising bond market statistics has been discontinued and replaced with a list of recommended sources for detailed, accurate, and current information sources on the Hong Kong bond market. These sources are listed below in alphabetical order.

- *AsianBondsOnline (an ASEAN+3 initiative lead by ADB)*
  http://www.asianbondsonline.adb.org/hongkong.php
  - Market-at-a-Glance
  - Data (market size, yields, indicators, ratings, including historical data)
  - Market structure
  - Market summary
  - News (latest statistics)

- Hong Kong Special Administrative Region Government Bond Programme website
  http://www.hkgb.gov.hk/en/statistics/statistic.html
  - Market turnover
  - New issuance
  - Outstanding amount
  - Prices and yields
  - Tender results

- Hong Kong Exchanges and Clearing Limited
  http://www.HKEX.com.hk/eng/stat/statistics.htm
  - Monthly market highlights
  - Securities and derivatives markets quarterly report
  - Fact book
  - Monthly bulletin
  - Daily quotations

- Hong Kong Monetary Authority—Central Moneymarkets Unit Bond Pricing Bulletin
  https://www.cmu.org.hk/cmupbb%5Fws/eng/page/wmp0100/wmp010001.aspx
  - Announcements
  - Bid–offer yields, bid–offer prices

- Turnover
- Outstanding amounts
- New issues
- List of instruments
- By Hong Kong dollar, Chinese renminbi, and US dollar

- Hong Kong Monetary Authority—Central Moneymarkets Unit Statistics
  http://www.hkma.gov.hk/eng/market-data-and-statistics/monthly-statistical-bulletin/table.shtml#CMU
  - Securities turnover (monthly)
  - Outstanding amounts
  - By Hong Kong dollar, Chinese renminbi, and US dollar and other foreign currencies

VIII

Presence of an Islamic Bond Market

A. Current Status of the Islamic Bond Market in Hong Kong, China

The tax laws in Hong Kong, China were amended in 2013 to provide a taxation framework for *sukuk* (Islamic bonds) comparable to conventional bonds. The government also issued two *sukuk* in 2014 and 2015 to play a lead role to the market. These measures have helped create a conducive environment for the *sukuk* market to grow in Hong Kong, China.

B. The Nature of *Sukuk*

In its simplest form, *sukuk* are certificates of equal value that represent an undivided interest (proportional to the investor's interest) in the ownership of an underlying asset (both tangible and intangible), usufruct, services, or investments in particular projects or special investment activities. Unlike conventional debt securities that mirror debts or loans on which interest is paid, *sukuk* can be structured based on innovative applications of Islamic principles and concepts. Nonetheless, *sukuk* share some similarities with conventional debt securities in that they are similarly structured based on the ability of the issuer to pay the periodic distribution and principal repayment.

A prerequisite for *sukuk* is the compliance with Islamic, or Shariah, principles that prohibit the charging of interest. A *sukuk* is structured so that it involves an exchange of Shariah-compliant assets for financial consideration that allows investors to earn profits and rentals from transactions in the future.

There are various types of *sukuk* since different Shariah principles are used for the creation of Islamic securities. The more prominent ones are the sale and purchase of an asset based on deferred payment, the leasing of specific assets, and a profit- and loss-sharing scheme.

C. Legal Implications for Investors

Sukuk represent ownership claims on a pool of assets or rights to receivables or participation. *Sukuk* may be issued as public offers or via private placements.

The various transaction contracts that form the genesis for a *sukuk* issue have different legal implications for investors. *Sukuk* investors should, therefore, be fully apprised of and knowledgeable about their rights and obligations under the various underlying Islamic concepts and principles, which are explained hereafter.

1. Rights to Underlying Asset and Its Cash Flow

For *sukuk* that represent ownership of assets, their usufruct or services (the underlying asset), the claim embodied in the *sukuk* is not just a claim on the underlying asset used in the *sukuk* transaction, but also the right to the cash flow and proceeds from the sale of the asset.

2. Rights to Cash Flow from the Contract of Exchange but Not the Asset

For *sukuk* issued as evidence of indebtedness arising from the sale of the asset based on contracts of exchange, the claim is on the obligations stemming from the applied contract of exchange, and not ownership of the physical asset as ownership has been transferred to the obligor.

3. Rights to Undivided Interest in Specific Investments

For special investment activities funded through a loss-sharing scheme, the *sukuk* represent the holders' undivided interests in the specific investments. This structure is used to raise funds for projects on the basis of partnership contracts. *Sukuk* holders or investors then become the owners of the project in proportion to their respective shares. Profits are distributed according to a pre-agreed proportion while losses are prorated according to their equity share.

D. *Sukuk* Issuance in Hong Kong, China

The government successfully issued two *sukuk* under its Government Bond Programme in September 2014 and June 2015. The two *sukuk* were well-received by global investors, achieving multiple times oversubscriptions and setting a benchmark for the market. The first *sukuk* used an *ijarah* (leasing) structure and the second *sukuk* used an asset-light *wakalah* (agency) structure in which only 34% of the underlying assets were fixed assets, compared to 100% for the *ijarah* structure. The two *sukuk* issuances have demonstrated the viability and flexibility of Hong Kong, China's platform.

E. Regulations for *Sukuk*

The current regime of the SFO and CWUMPO—in terms of public offering of securities and the prospectus registration and disclosure requirements for debt securities, conduct regulations of intermediaries, and other investor protection provisions—apply to mainstream *sukuk* as they apply to conventional debt instruments. The product structure of the *sukuk* and the way it is marketed needs to be examined to exactly determine the application of the relevant legislation in any particular case.

F. Basic Market Infrastructure Required to Facilitate Islamic Finance

Enhancements have been made to the US dollar and euro RTGS systems as well as the CMU to facilitate participating members to identify transactions related to Islamic finance and to segregate Islamic-related funds from others.

G. Tax-Related Issues for Islamic Finance in Hong Kong, China

The more complicated structure of *sukuk*, which involves the setting up of a special purpose vehicle and multiple transfers of underlying assets, has led to additional tax liability for *sukuk* issuers in the past.

The enactment of the Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) (Amendment) Ordinance 2013 in July 2013 has overcome this obstacle by removing the additional profits tax and stamp duty charges incurred when issuing *sukuk*, thus leveling the playing field and providing a comparable taxation framework between *sukuk* and other conventional bonds.

The legislation adopts a prescriptive and religion-neutral approach, introducing the Alternative Bond Scheme to denote the *sukuk* arrangements. It covers five common types of *sukuk* in the global market: *ijarah* (lease arrangement), *musharakah* and *mudarabah* (profits sharing arrangement), *murabahah* (purchase and sale arrangement), and *wakalah* (agency arrangement).

IX

Hong Kong Bond Market Challenges and Opportunities

This chapter discusses some of the real and perceived challenges facing the Hong Kong bond market and its participants, and also describes the possible mitigating factors or market developments that could address these challenges in an appropriate manner.

A. Challenges in the Hong Kong Bond Market

1. Issuance of Renminbi Bonds by Companies in the People's Republic of China

In its *Half-Yearly Monetary and Financial Stability Report, March 2016*, the HKMA commented that regulatory changes in the PRC might make it easier for PRC-based companies to tap the onshore bond market instead of continuing to issue offshore renminbi bonds in the Hong Kong bond market. The HKMA is, hence, expecting the issuance volume of renminbi bonds by PRC-based companies to possibly remain subdued for the near future.

As reported by the HKMA, after a period of rapid growth, the offshore renminbi debt market in Hong Kong, China is showing signs of moderation. In 2015, offshore renminbi debt issuance amounted to RMB350.6 billion, down 19.3% from the previous year, marking the first annual decline since 2007.[88]

2. Competition for Offshore Renminbi Issuances

According to market feedback and media reports, the increasing competition among established and emerging renminbi offshore centers may lead to a reduction in the issuance of offshore renminbi debt securities in the Hong Kong bond market. In recent years, Singapore, Luxembourg, and (most recently) London have seen an increase in offshore renminbi bond and note issuance activities that have found strong investor interest in their markets and time zones. The concern of Hong Kong bond market participants is that this may affect the issuance volume and liquidity of the offshore renminbi bond market in Hong Kong, China.

At the same time, the International Monetary Fund's decision to include renminbi in its Special Drawing Rights basket may boost demand for renminbi-denominated assets in the long-run across all markets in general and in Hong Kong, China in particular as the most established of these markets.

[88] Selected statements adopted from Hong Kong Monetary Authority. 2016. *Half-Yearly Monetary and Financial Stability Report March 2016.* http://www.hkma.gov.hk/media/eng/publication-and-research/quarterly-bulletin/qb201603/E_Half-yearly_201603.pdf

3. Limited Size of Repo Market

The relatively small size of the repo market in Hong Kong, China is partly due to the established practice of banks funding in the unsecured interbank and foreign exchange swap markets rather than repo. Since the global financial crisis, there are signs that banks are less willing to engage in unsecured lending. However, given the abundant liquidity in the local banking sector at present, the need for funding activities is rather limited, suggesting that banks may not have strong motivation to increase their use of repo.

Notwithstanding the above, the HKMA is aware that recent developments in international financial regulations may result in a reallocation of assets for use as collateral. An efficient repo market would be conducive to such reallocations. To support the further development of the repo market in Hong Kong, China, the HKMA will continue to refine and provide the necessary financial infrastructure to facilitate the conduct of repo both locally as well as on a cross-border basis. The HKMA will also closely monitor the developments in international financial regulations and their implications for the development of the repo market in Hong Kong, China.[89]

B. Opportunities in the Hong Kong Bond Market

1. General Regulatory Environment

Since the global financial crisis, regulators around the world have been strengthening laws and regulations across many areas of the capital and financial markets. Of particular interest have been banking regulations and the focus on risk-weighted capital. The outcome for the financial markets include a limitation of what banks can or are willing to lend, to whom, and under what circumstances. A number of these regulatory initiatives may, in consequence, lead to a rebalancing of funding options for the corporate sector from bank loans to the capital markets.

While not unique to Hong Kong, China, this development might just positively influence the interest of potential domestic issuers to consider raising funds via bond, note, or *sukuk* issuance, and to diversify their debt portfolio. Such increased interest, coupled with a broader and deeper investor base (see below), might also have a beneficial impact on funding costs.

3. Association of Southeast Asian Nations Plus Three Multi-Currency Bond Issuance Framework

The implementation of AMBIF is expected to benefit not only AMBIF issuances, but the Hong Kong bond market at large (see also Chapter X). ABMI and policy bodies and regulatory authorities in Hong Kong, China focus on a suitable balance between bank loan and capital market funding opportunities for corporates. AMBIF has been created to provide an additional bond, note, or *sukuk* issuance avenue for these corporates. AMBIF in Hong Kong, China focuses on the issuance of bonds and notes in the form of private placements to Institutional Investors, which is further supported by the Professional Bonds profile listing option on SEHK (please also refer to Chapter III.I).

At the same time, the Hong Kong bond market generates strong interest from potential AMBIF bond or note issuers who may already have substantial commercial operations

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[89] Statements contained in Executives Meeting of East Asia–Pacific Central Banks. 2014. *EMEAP Repo Markets: State of Play—A Report by the EMEAP Working Group on Financial Markets*. http://www.emeap.org/emeapdb/upload%5CWGMeeting%5CEMEAP_Working_Group_on_FinancialMarkets_-_Report_on_EMEAP_Repo_Markets_....pdf

in the region and would like to issue bonds and notes and use local currency proceeds in these markets in order to, for example, eliminate foreign exchange risk or more effectively manage their debt portfolio. The value proposition for Hong Kong, China is the significant presence of professional investors, and the role of a listing hub. AMBIF is likely to attract the attention of these investors in local currency bonds and notes.

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Recent Developments and Future Direction

A. Recent Major Developments

Recent major developments are considered those that occurred or have been announced in the Hong Kong market since the first publication of the Bond Market Guide in April 2012.

1. Shanghai–Hong Kong Stock Connect

Shanghai–Hong Kong Stock Connect, a pilot scheme enabling mutual stock market access between the Shanghai Stock Exchange and SEHK, was launched on 17 November 2014.

Under Shanghai–Hong Kong Stock Connect, SEHK and the Shanghai Stock Exchange have established mutual order-routing connectivity and related technical infrastructure to enable investors of their respective market to trade designated equity securities listed in the other's market. HKSCC and ChinaClear are responsible for clearing and settlement, and the provision of depository, nominee, and other related services of the trades executed by their respective market participants and/or investors.[90]

According to Charles Li, Chief Executive of HKEX, the greatest significance of Shanghai–Hong Kong Stock Connect is that it provides the PRC with an interim model for opening up before it is completely ready for the large-scale arrival of international investors and departure of Chinese domestic investors. The interim model works like a "mutual market" in which investors on each side of the boundary are able to trade products of the other market within their home time zone, relying on their home market infrastructures. With the joint oversight of the two regulators, capital flows from the PRC and international markets are able to congregate and interact with each other in this mutual market, facilitating the gradual convergence of the PRC with international markets.

This model has the potential to be extended to other products, including equity derivatives, commodities, fixed income, and currencies. Capital market products in the PRC that are of interest to international investors can be placed in this mutual market, while those international products that have demand among Chinese investors can be added, thereby enabling Chinese investors to diversify their investments and hedge against international price risks.[91]

Under its Strategic Plan, 2016–2018 (see also Section B), HKEX is looking at initiatives to extend and enhance mutual connectivity by first seeking to enhance the

[90] For further information, please see the Information Booklet and FAQ available from the HKEX website at http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/Documents/EP_CP_Book_En.pdf
[91] For comments on this and other HKEX initiatives, please see the Charles Li Direct blog on the HKEX website at http://www.HKEX.com.hk/eng/newsconsul/blog/150120blog.htm

functionality of Shanghai–Hong Kong Stock Connect, launch Shenzhen–Hong Kong Stock Connect, and add exchange-traded funds, listed bonds, and convertible bonds to the two Stock Connect schemes. Second, HKEX will work with regulators in Hong Kong, China and the PRC to relax trading restrictions including quotas, eligible securities, eligible investors, holiday trading, and stock borrowing and lending.

For details on the envisaged enhanced connectivity for debt securities, please see item B.3.

The SFC has been in discussion with the China Securities Regulatory Commission, Shenzhen Stock Exchange, and HKEX on a proposed extension of the Stock Connect to the Shenzhen Stock Exchange.

B. Future Direction

A number of significant developments will come into effect beginning in the second half of 2015 and are expected to have a beneficial impact on the Hong Kong bond market and, possibly, the region's bond markets at large.

1. Enhancements to Post-Trade Processing in Asian Bond Markets

The HKMA will continue to collaborate with central banks and central securities depositories in the region to improve the post-trade environment in Asia, taking into account the specific needs for Asia in terms of cross-border access, stimulation in local issuance, automation of post-trade process, the possibility of cross-border collateralization, and reductions in post-trade costs.

2. Consultations on Changes to the Professional Investor Regime

In May 2013, the SFC issued a consultation paper to invite public comments on proposed amendments to the Professional Investor Regime that aimed to strengthen the manner in which market participants treat Professional Investors and Non-Professional Investors.

In September 2014, the SFC published the conclusions paper on the proposed amendments to the Professional Investor Regime. The proposals will not affect the definition of the professional investor under the SFO as mentioned in the General Definition section in Part N. The amendments only relate to regulatory exemptions that intermediaries can rely on when serving certain types of professional investors. Please refer to the Consultation Conclusions on the Proposed Amendments to the Professional Investor Regime and Further Consultation on the Client Agreement Requirements published on 25 September 2014 for details.

In summary, as set out in the Consultation Conclusions, the SFC decided to proceed with the proposal not to allow intermediaries, when serving Individual Professional Investors and certain Corporate Professional Investors,[92] to be exempt from (i) the suitability requirement,[93] (ii) the requirement to enter into a written client agreement and provide relevant risk disclosure statements,[94] and (iii) other fundamental requirements that have a significant bearing on investor protection under the General Code of Conduct. Except for the requirement to enter into a written client agreement and provide relevant disclosure statements, which will come into effect on 9 June 2017, all other amendments relating to the Professional Investor Regime became effective on 25 March 2016.

[92] Paragraph 15.2 of the General Code of Conduct.
[93] Paragraph 5.2 of the General Code of Conduct.
[94] Paragraph 6.1 of the General Code of Conduct.

In this context, the SFC has started public consultations on the need to strengthen the manner in which market participants treat professional and nonprofessional investors. Changes to the present SFO provisions were expected to take effect by March 2016.

3. Potential Shanghai–Hong Kong Bond Connect

As mentioned under A.1, the connection between SEHK and the PRC's exchange-traded bond market is a potential next step in the fulfilment of a mutual market concept between the two jurisdictions.

In its Strategic Plan, 2016–2018, HKEX is exploring mutual market access with the PRC in the institutional cash bond market through a proposed Bond Connect scheme.[95] HKEX believes that stimulating cross-border capital flows in the underlying CNY bond market is an important prerequisite for the long-term success of fixed-income derivatives traded on HKFE. To facilitate these flows, HKEX will explore the creation of a Bond Connect scheme to provide cross-border cash bond trading and settlement connectivity with the PRC's major onshore bond market infrastructures, with a focus on the institutional bond market.

4. Upcoming Hong Kong Exchanges and Clearing Limited Initiatives

Also mentioned in the HKEX Strategic Plan, 2016–2018 are a number of initiatives aimed at building new capabilities in pre-trade risk management, stock borrowing, and lending (which includes fixed-income securities traded on SEHK and settled in CCASS), remote participant-ship, a new hedge exemption regime for derivatives position limits, and new after-hour and holiday trading arrangements.

In addition, HKEX plans to launch exchange-traded derivatives in Hong Kong, China based on renminbi and onshore interest rates on HKFE.

5. Association of Southeast Asian Nations Plus Three Multi-Currency Bond Issuance Framework

The introduction of AMBIF in regional markets over the course of 2015 signalled another opportunity for additional bond or note issuance activities in the Hong Kong bond market. Potential issuers have identified Hong Kong, China as one of the markets of particular interest, largely due to the presence of Institutional Investors and its role as a listing hub for CNY-denominated bonds and notes and an issuance hub for bonds and notes denominated in offshore Chinese renminbi.

Aimed particularly at the issuance of bond and note to Institutional Investors (professional investors), AMBIF encourages domestic and regional issuers to take advantage of streamlined issuance approval processes in Hong Kong, China and other regional markets. For additional information on AMBIF, kindly refer to Chapter IX.5.

The key advantage of AMBIF lies in the ability of regional issuers to tap multiple markets, including Hong Kong, China, by using the same or similar approval processes. This additional issuance avenue is seen as offering an alternative to other forms of funding for corporate issuers.

[95] Available for download from the HKEX website at http://www.HKEX.com.hk/eng/exchange/corpinfo/mission/mission.htm

6. People's Republic of China–Hong Kong, China Mutual Recognition of Funds

On 18 December 2015, the SFC granted authorization for the first batch of four PRC-based funds under the PRC–Hong Kong, China Mutual Recognition of Funds (MRF) initiative for public offering in Hong Kong, China. The SFC also welcomed the approval by the China Securities Regulatory Commission of the first batch of three funds from Hong Kong, China for offering in the PRC market.

The MRF initiative is a major breakthrough in the opening up of the PRC's funds market to offshore funds. It will open up a new frontier for the PRC and Hong Kong, China's asset management industries and make available a wider selection of fund products to investors in both markets. The SFC and the China Securities Regulatory Commission have been accepting MRF applications since 1 July 2015. The approval of the first batch of funds under the MRF initiative is a milestone in the implementation of this important cross-border cooperation initiative.

The initiative, while aimed at funds, is also expected to draw fixed-income products, which in turn are expected to provide further stimulus for the Hong Kong bond market.

7. Enhancements to Post-Trade Processing in Asian Bond Markets

The HKMA will continue to collaborate with central banks and central securities depositories in the region to improve the post-trade environment in Asia, taking into account the specific needs of Asian investors in terms of cross-border access, stimulation of local issuance, automation of the post-trade process, the possibility of cross-border collateralization, and reductions in post-trade costs.

Appendix 1
Group of Thirty Compliance

The Group of Thirty recommendations were originally conceived as the group's Standards on Securities Settlement Systems in 1989, detailing in a first-of-its-kind report nine recommendations for efficient and effective securities markets covering legal, structural and settlement process areas. The recommendations were subsequently reviewed and updated in 2001, under the leadership of the Bank for International Settlements, and through the efforts of a joint task force of the Committee on Payment and Settlement Systems and the Technical Committee of the International Organization of Securities Commissions. Compliance with the Group of Thirty recommendations in individual markets is often an integral part in securities industry participants' and intermediaries' due diligence process.

Table A1: Group of Thirty Recommendations—Compliance for Hong Kong, China

Recommendation		Implemented
1	Eliminate paper and automate communication, data capture, and enrichment.	Yes
2	Harmonize messaging standards and communication protocols.	Yes
3	Develop and implement reference data standards.	Yes
4	Synchronize timing between different clearing and settlement systems and associated payment and foreign exchange systems.	Yes
5	Automate and standardize institutional trade matching.	Yes
6	Expand the use of central counterparties.	Yes
7	Permit securities lending and borrowing to expedite settlement.	Yes
8	Automate and standardize asset servicing processes, including corporate actions, tax relief arrangements, and restrictions on foreign ownership.	Yes
9	Ensure the financial integrity of providers of clearing and settlement services.	Yes
10	Reinforce the risk management practices of users of clearing and settlement service providers.	Yes
11	Ensure finals, simultaneous transfer and availability of assets.	Yes

Recommendation		Implemented
12	Ensure effective business continuity and disaster recovery planning.	Yes
13	Address the possibility of failure of a systematically important institution.	Yes
14	Strengthen assessment of the enforceability of contracts.	Yes
15	Advance legal certainty over rights to securities, cash, or collateral.	Yes
16	Recognize and support improved valuation methodologies and closeout netting arrangements.	Yes
17	Ensure appointment of appropriately experienced and senior board members (of the boards of securities clearing and settlement infrastructure providers).	Yes
18	Promote fair access to securities clearing and settlement networks.	Yes
19	Ensure equitable and effective attention to stakeholder interests.	Yes
20	Encourage consistent regulation and oversight of securities clearing and settlement service providers.	Yes

Source: Group of Thirty. 2003. *Global Clearing and Settlement–A Plan of Action*.
http://newsite.group30.org/publications/detail/123

Appendix 2
Practical References

For easy access to further information about the market features described in the Hong Kong, China Bond Market Guide—including information on the policy bodies, regulatory authorities, and securities market-related institutions—interested parties are encouraged to utilize the following links (all websites available in English, as well as in simplified and traditional Chinese):

AMBIF Implementation Guideline for Hong Kong, China
http://tinyurl.com/AMBIF-Impl-GL-for-HKG

AMBIF—Single Submission Form (as supported by regulatory authorities and market institutions in Hong Kong, China)
http://tinyurl.com/AMBIF-Single-Submission-Form

AsianBondsOnline (ADB)
http://www.asianbondsonline.adb.org/hongkong.php

Bank of China (Hong Kong)—RMB Clearing Bank
http://www.bochk.com/web/common/multi_section.xml?section=rmb&level_2=rmb_clearing&fldr_id=31806

Hong Kong Exchanges and Clearing Limited
http://www.HKEX.com.hk/eng/index.htm

Hong Kong Exchanges and Clearing Limited—Central Clearing and Settlement System
https://www.HKEX.com.hk/eng/market/clr/secclr/ccass3/ccass3.htm

Hong Kong Exchanges and Clearing Limited—Professional Bonds
http://www.HKEX.com.hk/eng/prod/secprod/debt/professional_debt/professional_debt.htm

Hong Kong Monetary Authority
http://www.hkma.gov.hk/eng/index.shtml

Hong Kong Monetary Authority—Central Moneymarkets Unit
http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/infrastructure/cmu.shtml

Hong Kong Monetary Authority—Exchange Fund Bills and Notes
http://www.hkma.gov.hk/eng/key-functions/international-financial-centre/debt-market-development/exchange-fund-bills-notes.shtml

Securities and Futures Commission
http://www.sfc.hk/web/EN/index.html

Appendix 3
Glossary of Technical Terms

Alternative Bond Scheme	Denotes *sukuk* arrangements as an alternative to conventional bonds and notes (in most recent legislation)
Authorized Institutions	Licensed banks, restricted license banks, and deposit-taking companies as defined in the Banking Ordinance
filing	Action of submitting documentation
iBond	Inflation-linked bond issued by the Government of the Hong Special Administrative Region of the People's Republic of China
Information Memorandum	Synonymous with Offering Memorandum; term typically used for key documentation for a private placement mainly to professional investors
Licensed Corporations	Corporations licensed under sections 116 or 117 of the SFO
listing	Typically, action of submitting a bond issue or other securities to an exchange for the purpose of trading, price finding, disclosure, or profiling
Offering Memorandum	Synonymous with Information Memorandum; term typically used for key documentation for a private placement mainly to professional investors
PI Rules	Securities and Futures (Professional Investors) Rules (Cap. 571D)
Professional Bonds	Short form for wholesale bonds listing facility on HKEX
Professional Debts	Term used in HKEX documentation (including Chapter 37 of SEHK Listing Rules) for debt securities aimed at professional investors
Prospectus	Term generally used to refer to a disclosure document offering shares in or debentures of a company to the public for subscription or purchase.; in the case of Hong Kong, China only, prospectus is used as a term in regulations to describe all offers to any parties to subscribe to or purchase securities
Recognised Dealers	An institution appointed by the HKMA to hold and deal in retail bonds and institutional bonds through the CMU for the Government Bond Programme
Registered Institutions	Authorized Institutions registered under section 119 of the SFO to conduct activities regulated by the SFC
registration	Action of registering a bond issue, for reference pricing or disclosure purposes

sukuk	Islamic bond or note
sponsor	Party who helps list a bond or note on SEHK
uncertified securities (regime)	describes the movement toward a dematerialized market

Source: ABMF SF1.

ASEAN+3 Bond Market Guide 2016 Hong Kong, China

ASEAN+3 Bond Market Guide is a comprehensive explanation of the region's bond markets. It provides various information such as the history, legal and regulatory framework, specific characteristics of the market, trading and transaction, and other relevant information. The Hong Kong, China Bond Market Guide is an outcome of the strong support and kind contributions of ASEAN+3 Bond Market Forum members and experts, particularly from Hong Kong, China. The report should be recognized as a collective good to support bond market development among ASEAN+3 members.

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