THE BOND MARKET IN HONG KONG, CHINA

AN ASEAN+3 BOND MARKET GUIDE UPDATE

SEPTEMBER 2020

ASIAN DEVELOPMENT BANK

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Notes:
ADB recognizes "China" as the People's Republic of China; "Hong Kong" as Hong Kong, China; and "Macau" as Macau, China.

In this report, international standards for naming conventions—International Organization for Standardization (ISO) 3166 for economy codes and ISO 4217 for currency codes—are used to reflect the discussions of the ASEAN+3 Bond Market Forum to promote and support implementation of international standards in financial transactions in the region. ASEAN+3 comprises the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

The economies of ASEAN+3 as defined in ISO 3166 include Brunei Darussalam (BN; BRN); Cambodia (KH; KHM); the People's Republic of China (CN; CHN); Hong Kong, China (HK; HKG); Indonesia (ID; IDN); Japan (JP; JPN); the Republic of Korea (KR; KOR); the Lao People's Democratic Republic (LA; LAO); Malaysia (MY; MYS); Myanmar (MM; MMR); the Philippines (PH; PHL); Singapore (SG; SGP); Thailand (TH; THA); and Viet Nam (VN; VNM).

The currencies of ASEAN+3 as defined in ISO 4217 include the Brunei dollar (BND), Cambodian riel (KHR), Chinese renminbi (CNY), Hong Kong dollar (HKD), Indonesian rupiah (IDR), Japanese yen (JPY), Korean won (KRW), Lao kip (LAK), Malaysian ringgit (MYR), Myanmar kyat (MMK), Philippine peso (PHP), Singapore dollar (SGD), Thai baht (THB), and Vietnamese dong (VND).

Contents

Note: the chapter and section numbering reflects that of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*, and includes only the chapters and sections being updated.

Figure

Acknowledgments

The *ASEAN+3 Bond Market Guide 2016: Hong Kong, China* was published in November 2016.[1] Being a mature market, the main features and functions in the bond market in Hong Kong, China have largely remained consistent in the years since publication, which means that a complete review is not required just yet. At the same time, an update on a number of recent market developments, particularly those that mirror or touch on developments in other jurisdictions, such as Bond Connect, is necessary.

As such, this update was compiled to coincide with the publication of the *The Inter-Bank Bond Market in the People's Republic of China: An ASEAN+3 Bond Market Guide* in August 2020.

In addition to a description of Bond Connect features in the Hong Kong bond market, this update contains information on the Government Green Bond Programme, the Green Bond Grant Scheme, the Pilot Bond Grant Scheme, a revision of the Professional Investor Rules, as well as additions to eligible collateral for the RMB Liquidity Facility offered by the Hong Kong Monetary Authority.

The ASEAN+3 Bond Market Forum (ABMF) Sub-Forum 1 team wishes to thank the Hong Kong Monetary Authority, the Securities and Futures Commission, as well as ABMF International Experts for their inputs and review of this update.

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

This update and those relating to other ASEAN+3 bond markets are available for download from *AsianBondsOnline*.[2]

September 2020

ASEAN+3 Bond Market Forum

[1] See https://asianbondsonline.adb.org/documents/abmf_hkg_bond_market_guide_2016.pdf.
[2] See https://asianbondsonline.adb.org.

Abbreviations

ABMF	ASEAN+3 Bond Market Forum
ADB	Asian Development Bank
AMBIF	ASEAN+3 Multi-Currency Bond Issuance Framework
ASEAN	Association of Southeast Asian Nations
ASEAN+3	Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea
BCCL	Bond Connect Company Limited
CCDC	China Central Depository & Clearing Co., Ltd.
CFETS	China Foreign Exchange Trade System
CMU	Central Moneymarkets Unit
CNH	offshore Chinese renminbi (ISO code)
CSD	central securities depository
EFBNs	Exchange Fund Bills and Notes
HKD	Hong Kong dollar (ISO code)
HKMA	Hong Kong Monetary Authority
HKSAR	Hong Kong Special Administrative Region
PBGS	Pilot Bond Grant Scheme
PBOC	People's Bank of China
PRC	People's Republic of China
RMB	Chinese renminbi (commonly used abbreviation in the market)
SEHK	The Stock Exchange of Hong Kong Limited
SFC	Securities and Futures Commission
SHCH	Shanghai Clearing House Co., Ltd.
USD	United States dollar (ISO code)

I

Overview

A. Introduction

The bond market in Hong Kong, China has for some time been a significant marketplace 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 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).

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 Hong Kong Special Administrative Region (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.

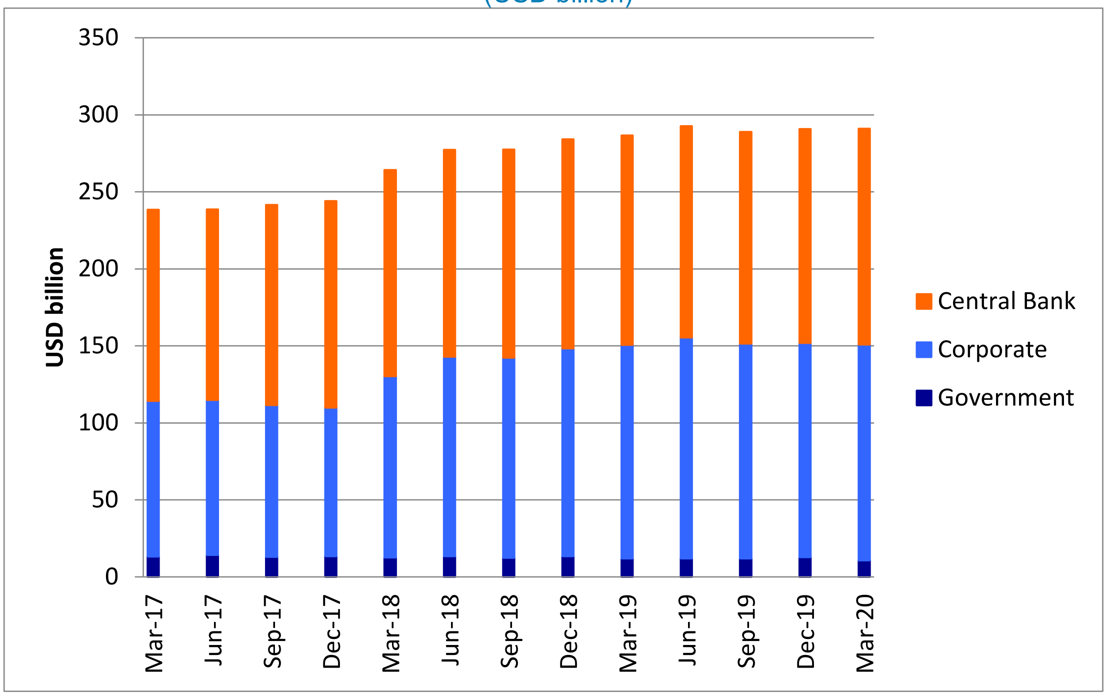
The Central Moneymarkets Unit (CMU) was set up primarily to provide computerized clearing and settlement facilities for EFBNs, which provide benchmark yields that guide private debt pricing. In December 1993, the HKMA extended this service to other Hong Kong dollar debt securities. Since December 1994, the CMU has been linked to international clearing systems such as Clearstream and 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 United States (US) dollars.

In December 1996, an interface between the CMU and the real-time gross settlement 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 markets. However, some bonds are also listed and may be traded on the securities market of Hong Kong Exchanges and Clearing Limited, which is the holding company that owns the Stock Exchange of Hong Kong Limited (SEHK), which operates the stock exchange in Hong Kong, China.

In the Hong Kong dollar debt market, the total value of outstanding Hong Kong dollar debt instruments remained stable over the 15 months prior to March 2020 after having gradually increased in the preceding 15-month period (Figure 1). Outstanding Hong Kong dollar debt has increased significantly since 2015, the last year for which data was included in the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*.

Figure 1: Local Currency Bonds Outstanding in Hong Kong, China
(USD billion)



Note: Data as of 31 March 2020 and include bonds issued by nonresidents.
Source: AsianBondsOnline. Hong Kong, China Bond Market.
https://asianbondsonline.adb.org/economy/?economy=HK.

The HKMA continues to implement the Government Bond Programme to promote the further and sustainable development of the local bond market. In May 2019, the Government of the HKSAR of the PRC successfully offered its inaugural green bond under the Government Green Bond Programme, with an issuance size of USD1 billion and a tenor of 5 years. At the end of 2019, the total outstanding amount of 13 issues of institutional bonds stood at HKD91.3 billion. In addition, two *Sukuk* (Islamic bonds) issued under the Government Bond Programme were outstanding, each with an issuance size of USD1 billion.[3]

The government issued the fourth batch of Silver Bonds in 2019, an inflation-linked bond with a minimum annual interest rate of 3% that targets Hong Kong, China residents aged 65 or above. The size of the issuance was HKD3 billion, with a tenor of 3 years. The number of valid applications was 56,564, with a total subscription of more than HKD7.9 billion.

[3] Selected statements and data adapted from the Hong Kong Monetary Authority. 2020. *Quarterly Bulletin March 2020*. No. 102. Hong Kong, China.

A decrease in bond issuance by overseas issuers, mainly financial institutions and corporates, was observed in 2019, while multilateral development banks also reduced their issuances. Local corporates expanded their funding scale in the Hong Kong debt market, with their issuance volume up 14% from 2018. Meanwhile, statutory bodies and government-owned corporations roughly maintained their issuance size in the Hong Kong dollar bond market in 2019, while Authorized Institutions' fund-raising activities to support their short-term funding needs decreased 6% year-on-year. The total issuance volume in the Hong Kong dollar debt market in 2019 stood at HKD4.184 trillion.

In the 2020–21 Budget, the government announced its plan to issue green bonds totaling HKD66 billion within the next 5 years, in line with the market situation. The government also announced that it would resume the issuance of iBonds (inflation-linked bonds) and continue to issue Silver Bonds to promote the development of the retail bond market and the silver market.

The HKMA will continue to support the development of the local bond market through implementation of the Government Bond Programme, Government Green Bond Programme, and various other initiatives.

The regulatory environment is also conducive to the implementation of the 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 the ABMF Report on the implementation of AMBIF, published by ADB.[4]

Information on recent initiatives and developments with relevance for the Hong Kong bond market can be found in the update to Chapter X in this note.

[4] See ADB. 2015. *Implementation of the ASEAN+3 Multi-Currency Bond Issuance Framework: ASEAN+3 Bond Market Forum Sub-Forum 1 Phase 3 Report*. Manila. https://www.adb.org/publications/implementation-ambif-asean3-bond-market-forum-sf1-p3.

III

Characteristics of the Hong Kong Bond Market

The Securities and Futures Commission (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 behavior. Since the *ASEAN+3 Bond Market Guide* was first introduced in 2012, there have been and continue to be substantial changes in some market characteristics that are not limited to the regulatory environment.

As such, some of the more recent additions or changes to the characteristics of the Hong Kong bond market are described in this chapter in the context of the existing structure of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*, which was published in 2016.

B. Types of Bonds and Notes

All Government Bonds and most 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 HKSAR 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 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).

iii. Government Green Bond Programme (From 2018) [NEW]

The Chief Executive of the Government of the HKSAR of the PRC announced in the 2017 Policy Address that the government would take the lead in arranging the issuance of a green bond to demonstrate the government's support for sustainable development and determination to combat climate change, and to promote the development of green finance. The Financial Secretary further announced in the 2018–19 Budget that a Government Green Bond Programme would be launched. The Government Green Bond Programme represents a separate initiative, independent of the Government Bond Programme, which has been in place for some time.

On 15 November 2018, the Legislative Council passed a resolution under the Loans Ordinance (Cap. 61), authorizing the government to borrow up to a maximum principal amount outstanding of HKD100 billion (or equivalent in other currencies) at any one time under the Government Green Bond Programme. The proceeds of the issued green bonds will provide funding for green public works projects of the government.

The HKSAR of the PRC's Green Bond Framework, which is aligned with the Green Bond Principles, sets out how the government intends to issue green bonds to fund projects that will improve the environment and facilitate the transition to a low-carbon economy.[5]

The HKMA assists in implementing green bond issuance under the Government Green Bond Programme. The first green bond under the program was issued in May 2019, with an issuance size of USD1 billion and a 5-year tenor, setting an important new benchmark for potential issuers in Hong Kong, China and the region. The green bond was nearly four times oversubscribed and placed with a wide range of global institutional investors. The bond also won a number of green bond awards. Riding on the success of the inaugural issue and heeding market demand for continued issuances, the Financial Secretary announced in the 2020–21 Budget the continuation of green bond issuances totaling HKD66 billion (USD8.5 billion) over the next 5 years in line with market conditions.

More detailed information on the Government Green Bond Programme and the underlying Green Bond Framework may be accessed via the website of the Government Green Bond Programme.[6]

N. Definition of Professional Investors

The professional investor concept in Hong Kong, China, its definition, and eligibility criteria and related rules are explained in Chapter III.N of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*.

The following changes occurred to the Professional Investor Rules in 2018 and are hereby added to this update.

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[5] The Green Bond Principles are compiled and maintained by the International Capital Markets Association on behalf of international bond market participants. Information on the Green Bond Principles is available from the ICMA website at https://www.icmagroup.org/green-social-and-sustainability-bonds/green-bond-principles-gbp/.

[6] See https://www.hkgb.gov.hk/en/greenbond/greenbondintroduction.html.

2. Changes to the Professional Investor Rules (2018) [NEW]

Effective 13 July 2018, the SFC amended the Securities and Futures (Professional Investor) Rules (Cap. 571D) to include additional entities to be eligible as professional investors, following a public consultation on the proposed amendments; the consultation conclusions had been published on 18 May 2018.

Key among the amendments was the ability for parties to be able to obtain and submit alternative forms of evidence of qualification as a professional investor. Such evidence includes certificates issued by custodians, auditors, or certified public accountants, or the use of public filings made under legal or regulatory requirements to demonstrate professional investor qualifications.

The new eligibility criteria included companies that have investment holding as their principal business purpose and are owned by one or more professional investors, as well as companies that wholly own a company that is qualified as a professional investor.

In addition, portfolios—defined as comprising securities, certificates of deposit issued by banks, or money held by custodians for a person—in joint accounts with persons other than the spouse or any child of the individual, and in investment corporations wholly owned by an individual, were admitted to count against the individual professional investor eligibility criterion of an HKD8 million portfolio.[7]

The revision to the Professional Investor Rules made permanent some previous modifications granted by the SFC under Section 134 of the Securities and Futures Ordinance (Cap. 571), which allows the SFC to grant a modification or waiver of requirements in relation to certain persons, including intermediaries, in the capital market.

[7] The official announcement by the SFC, together with links to the public consultation and its conclusions, is available from the SFC website at https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=18PR54.

IV

Bond and Note Transactions and Trading Market Infrastructure

Bond Connect and changes to the RMB Liquidity Facility offered by the HKMA represent recent additions to transaction infrastructure and facilities in the Hong Kong bond market and are described here in the established structure of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*.

Bond Connect was mentioned in the bond market guide as a future development; it was subsequently introduced in 2017. The RMB Liquidity Facility of the HKMA was mentioned in Chapter IV.G of the bond market guide in the context of the repo market.

G. Repo Market

5. Additions to Eligible Collateral for the RMB Liquidity Facility (2018) [NEW]

From 21 September 2018, the HKMA allowed the use of bills issued in Hong Kong, China by the People's Bank of China (PBOC) as eligible collateral for its RMB Liquidity Facility. On 20 September 2018, the HKMA and the PBOC signed a memorandum of understanding on the PBOC's ability to tender and issue PBOC bills denominated in offshore Chinese renminbi (ISO code: CNH) in the Hong Kong bond market, using the bond tendering platform of the CMU, which is called CMU BID. The memorandum of understanding made CNH-denominated PBOC bills eligible as CMU instruments.

For more information about CMU instruments, the issuance platform of the HKMA, and issuance-related processes, please refer to Chapters II and III in the *ASEAN+3 Bond Market Guide: Hong Kong, China*.

Effective 18 October 2018, the HKMA also admitted debt securities issued in Hong Kong, China by the Ministry of Finance of the PRC and denominated in US dollars as eligible collateral for the RMB Liquidity Facility.

Eligible collateral for the RMB Liquidity Facility also includes EFBNs issued by the HKMA and bonds issued by the Government of the HKSAR of the PRC, as well as CNH-denominated debt securities issued in Hong Kong, China by the Ministry of Finance of the PRC and policy banks of the PRC.[8] Also eligible as collateral are USD-denominated debt securities issued in the Hong Kong bond market by the Ministry of Finance of the PRC.[9]

The RMB Liquidity Facility was established by the HKMA in June 2012 to address potential short-term liquidity tightness in the offshore Chinese renminbi market and has

[8] The policy banks are Agricultural Development Bank of China, China Development Bank, and Export and Import Bank of China.
[9] See https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2018/20181018e1.pdf.

since supported banks managing their renminbi liquidity in relation to the Shanghai–Hong Kong Stock Connect, Shenzhen–Hong Kong Stock Connect, and Bond Connect (also see next section) via intraday (introduced in November 2014), overnight, 1 day, and 1 week repurchase transactions. The announcement of the changes and the complete list of eligible collateral for the RMB Liquidity Facility are available from the HKMA website.[10]

Additional information about the practices for the RMB Liquidity Facility is contained in Chapter IV.G of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China.*

J. Bond Connect (From 2017) [NEW]

The pending implementation of Bond Connect had been mentioned as a subject for the future direction of the Hong Kong bond market in Chapter X.B of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*.

Bond Connect represents a mutual access scheme between the bond markets of Hong Kong, China and the PRC. It was announced on 16 May 2017 by the HKMA and the PBOC, with trial operations commencing on 3 July 2017.

In Bond Connect, the term "Northbound Trading" represents the access of eligible institutional investors from Hong Kong, China and other domiciles specifically to the Inter-Bank Bond Market in the PRC, while the term "Southbound Trading" is used to describe access for PRC investors to the Hong Kong bond market.[11] The information contained in this update focuses on the Northbound Trading route. In May 2020, the PBOC, the China Banking and Insurance Regulatory Commission, the China Securities Regulatory Commission, and the State Administration of Foreign Exchange jointly released the Opinions on Providing Financial Support for the Development of the Guangdong–Hong Kong–Macau Greater Bay Area, which mentioned the exploring of Southbound Trading under Bond Connect at the appropriate time.[12]

This update focuses on the features and functions of Bond Connect related to the bond market in Hong Kong, China. For a description of the Bond Connect functionality in the Inter-Bank Bond Market, as the target market of the Northbound Trading leg, please refer to the *The Inter-Bank Bond Market in the People's Republic of China: An ASEAN+3 Bond Market Guide*, also published by ADB.[13]

1. Eligibility and Participation

Northbound Trading access to the Inter-Bank Bond Market int the PRC is available to overseas institutional investors who meet the admission criteria prescribed by the PBOC in the relevant notices. Investors need to contract with a recognized trading access platform and maintain or have access to account(s) at CMU, the central depository for debt instruments operated by the HKMA. CMU accounts may be in the name of the investors or held by their appointed intermediaries (i.e., local or global custodian). Bond Connect adopts a see-through principle, which allows regulatory authorities to identify the underlying account holders accessing the Inter-Bank Bond Market via CMU accounts.

[10] See https://www.hkma.gov.hk/eng/key-functions/money/liquidity-facility-framework/rmb-liquidity-facility-and-primary-liquidity-providers/.
[11] Bond Connect is open to all local and overseas investors who have met the admission criteria, maintain or have access to a CMU account, and have completed the necessary steps for the commencement of Northbound Trading.
[12] The announcement of the publication can be found at http://www.pbc.gov.cn/en/3688110/3688172/4024534/index.html.
[13] See https://www.adb.org/publications/asean3-inter-bank-bond-market-prc.

Under Bond Connect, there is no limitation on the size or origin of the investors wishing to engage in Northbound Trading. However, overseas investors will need to register with the PBOC and carry out onboarding steps before they may commence trading in the Inter-Bank Bond Market. There is no need to open a separate onshore account for trading through Bond Connect.

As of the end of May 2020, Bond Connect accounted for 1,951 Northbound investors.

2. Legal Basis and Regulatory Framework

Bond Connect builds on the existing regulations issued or administered by the HKMA and the SFC, including the Automated Trading Services authorization regime that Bond Connect Company Limited (BCCL) and the recognized trading access platforms (if incorporated in Hong Kong, China) are subject to. Bond Connect makes use of the typical function of the CMU as the clearing house, settlement agency, and central depository for debt instruments in the Hong Kong bond market. As Bond Connect adopts a multi-tier custody structure, CMU will act as the single nominee of all Bond Connect investors and holds one omnibus bond account with each of the onshore central securities depositories (CSDs) for the Inter-Bank Bond Market.

The trading activities of investors accessing the Inter-Bank Bond Market via Bond Connect are regulated by the PBOC and governed by the trading rules of the China Foreign Exchange Trade System (CFETS) as the central trading platform for the Inter-Bank Bond Market, as well as the terms and conditions of the recognized trading access platforms that investors use to connect to CFETS (see also Section 6).

3. Connectivity

Most of the market activity under Bond Connect occurs in the Inter-Bank Bond Market. However, two touch points exist with institutions in the Hong Kong bond market: BCCL and CMU.

a. Bond Connect Company Limited

BCCL is a joint venture of Hong Kong Exchanges & Clearing Limited and CFETS that was established to facilitate the access for eligible overseas institutional investors, including those domiciled in Hong Kong, China, to the Inter-Bank Bond Market. BCCL is incorporated in Hong Kong, China and is an authorized Automated Trading Services provider supervised by the SFC.

BCCL does not trade or facilitate trading in the Inter-Bank Bond Market but acts as a service provider to those eligible overseas institutional investors wishing to utilize Bond Connect to access the Inter-Bank Bond Market. Its key functions are onboarding of Northbound investors, marketing and providing information for Bond Connect as an access route into the Inter-Bank Bond Market, and liaising with the international bond trading systems that are connected to CFETS, which here are termed “Recognised Access Platforms.” BCCL also provides data feeds on Inter-Bank Bond Market trading activities as well as information on primary market activities.

b. Central Moneymarkets Unit

CMU represents the market infrastructure link between the Hong Kong bond market and the Inter-Bank Bond Market.

For the purpose of Bond Connect, CMU acts as account holder in both the China Central Depository & Clearing Co., Ltd. (CCDC) and the Shanghai Clearing House Ltd. (SHCH), the two CSDs in the Inter-Bank Bond Market. These accounts are maintained on an omnibus basis, but CMU adheres to the see-through principle, which requires access to information on underlying CMU participants if the need arises.

4. Subscription of Primary Issuance of Debt Instruments in the Inter-Bank Bond Market via Bond Connect

The primary issuance of PRC debt instruments may be subscribed to via Bond Connect (Northbound) and follows the issuance and offer processes in the Inter-Bank Bond Market; in this context, Bond Connect represents a sales channel for debt instruments issued in the PRC. For more information on these processes, please refer to the *The Inter-Bank Bond Market in the People's Republic of China: An ASEAN+3 Bond Market Guide*.

5. Eligible Debt Instruments

Eligible debt instruments accessible via Bond Connect for eligible overseas institutional investors with accounts at CMU include all types of rates and credit bonds issued in the Inter-Bank Bond Market, including central and local government-issued bonds, policy bank bonds, enterprise bonds, Panda bonds (those issued by nonresident issuers), commercial paper, asset-backed securities and notes, medium-term notes, and negotiable certificates of deposit. The eligibility for offer, distribution, and trading via Bond Connect is determined by the regulatory authorities for the Inter-Bank Bond Market.

6. Trading

Before commencing trading, eligible overseas institutional investors need to designate a bond trading platform (presently, Bloomberg and TradeWeb are recognized) through which they intend to access CFETS. Overseas institutional investors also need to establish a mutual counterparty relationship through the trading links with onshore market makers—so-called Onshore Participating Dealers—that are participating in Bond Connect to provide market liquidity.

Trading in debt financing instruments in the Inter-Bank Bond Market is subject to the trading rules issued by CFETS and the supervision of the PBOC.

Please see Chapter IV in *The Inter-Bank Bond Market in the People's Republic of China: An ASEAN+3 Bond Market Guide* for more information on CFETS, its trading platform, and the general trading practices in the Inter-Bank Bond Market, including as a result of Bond Connect market access.

7. Clearing, Settlement, and Depository Activities

All depository activities, settlements, interest and redemption payments, and corporate actions under Bond Connect are facilitated by CCDC and SHCH as the dedicated onshore CSDs for Bond Connect and with CMU as the designated offshore CSD. Cross-border cash settlement is completed through the Cross-Border Interbank Payment System.

CMU acts as the single nominee of all overseas investors under Bond Connect and holds one omnibus bond account each with CCDC and SHCH. Overseas investors may open subaccounts with CMU through a custodian in Hong Kong, China who carries CMU membership, or through their global custodian, which then appoints a custodian based in Hong Kong, China for subaccounts handling.

X

Recent Developments and Future Direction

A. Recent Developments

Recent major developments are considered those that occurred in the Hong Kong bond market since publication of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China* in November 2016.

1. Initiatives to Develop Hong Kong's Green Bond Market (2018) [NEW]

As a market facilitator, the Government of the HKSAR of the PRC has taken several concrete steps to encourage green bond uptake and nurture growth of the market.

Apart from the launch of the Government Green Bond Programme (see also Chapter III.B in this update) to both promote bond market development and encourage green bond issuers to make use of Hong Kong, China's competitive capital markets and sophisticated financial and professional services, the government also launched a Green Bond Grant Scheme in June 2018 to subsidize the cost of obtaining certification under the Hong Kong Quality Assurance Agency's Green Finance Certification Scheme.

To ensure access to reputable market information, the HKMA worked in collaboration with the Climate Bonds Initiative to launch the *Hong Kong Green Bond Market Briefing 2019* in February 2019, with a second edition being published in May 2020. The latest report indicated that green bonds arranged and issued in Hong Kong, China totaled USD10 billion in 2019, with cumulative green bond issuance amounting to USD26 billion at the end of 2019. There has also been increased diversification of issuer types and project categories funded by green bonds. For more information on the latest edition of the *Hong Kong Green Bond Market Briefing* please refer to the website of the Climate Bonds Initiative.[14]

2. Pilot Bond Grant Scheme (2018) [NEW]

The Pilot Bond Grant Scheme (PBGS) was announced as a new measure by the Financial Secretary during the delivery of the 2018–19 Budget. The PBGS became effective on 10 May 2018 and is valid for 3 years from the commencement date. The scheme supports the first-time issuance of bonds in the Hong Kong bond market and is aimed at attracting additional domestic, PRC-based, and international enterprises to issue debt securities in the Hong Kong bond market. The HKMA announced the scheme's details on 10 May 2018.

[14] See https://www.climatebonds.net/resources/reports/hong-kong-green-bond-market-briefing-2019.

a. Eligibility Criteria

A bond issue is eligible if issued in Hong Kong, China, defined as when a substantial amount of the issuance arrangements takes place in Hong Kong, China. In this context, the HKMA will look at the lead arrangers' debt capital market operations and plans in Hong Kong, China to determine whether the above criterion is fulfilled.

The bond will need to be issued to more than 10 investors, or it may be issued to less than 10 investors, if these investors are not associates of the issuer.[15]

The bond will have to be deposited in (the formal term is "lodged") and cleared by CMU or be listed on SEHK. The issuance size will have to amount to at least HKD1.5 billion or its equivalent in a foreign currency.

b. Scheme Benefits

The Government of the HKSAR of the PRC supports first-time issues with a grant of up to 50% of the eligible issuance expenses, with a cap of HKD2.5 million for issues (or issuer or guarantor) with a credit rating from a credit rating agency recognized by the HKMA, or a cap of HKD1.25 million for issues that do not have a credit rating and where neither the issuer nor the issue's guarantor have a credit rating.[16]

Eligible issuance expenses include the following fee categories:

1. fees to Hong Kong, China-based arrangers;
2. fees to Hong Kong, China-based legal advisors;
3. fees to Hong Kong, China-based auditors and accountants;
4. fees to Hong Kong, China-based credit rating agencies;
5. fees to Hong Kong, China-based external green reviewers (in the case of green bonds);
6. SEHK listing fees; and
7. CMU lodging and clearing fees.

c. Application Process

Issuers or lead arrangers may apply for a grant to the HKMA within 3 months from the date of issuance of an eligible bond and must provide supporting documents. Application forms for the PBGS are available from the HKMA.[17]

The HKMA encourages issuers and lead arrangers to contact the HKMA early in the issuance process to confirm eligibility of the issue and related expenses. Registered Institutions (i.e., licensed intermediaries in the capital market that service the issuer and the issuance) are expected to support the issuer in completing and submitting the grant application.

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[15] In the PBGS conditions, the term "associate" refers to (i) a person or corporation over which the issuer has control, (ii) a person or corporation which has control over the issuer, or (iii) a person or corporation that is under the control of the same person or corporation as the issuer.
[16] First-time issuance is defined as an issuer not having issued bonds in Hong Kong, China between 10 May 2013 and 9 May 2018 (the day preceding the HKMA announcement), both days inclusive. The credit rating agencies recognized by the HKMA are Fitch Ratings, Moody's Investors Service, Rating and Investment Information, Inc., and S&P Global Ratings.
[17] Issuers and lead arrangers may request a PBGS application from the HKMA via pbgs@hkma.gov.hk.

Appendix 2
Resource Information

For easy reference and access to further information about the topics discussed in this update, interested parties are encouraged to utilize the following links (all websites available in English):

ASEAN+3 Bond Market Guide 2016: Hong Kong, China
https://asianbondsonline.adb.org/documents/abmf_hkg_bond_market_guide_2016.pdf

AsianBondsOnline (Asian Development Bank)
https://asianbondsonline.adb.org/economy/?economy=HK

Bond Connect Company Limited **[NEW]**
https://www.chinabondconnect.com

Climate Bonds Initiative **[NEW]**
https://www.climatebonds.net

Green Bond Principles (International Capital Market Association) **[NEW]**
https://www.icmagroup.org/green-social-and-sustainability-bonds/green-bond-principles-gbp/

Hong Kong Exchanges and Clearing Limited
https://www.hkex.com.hk/?sc_lang=en

Hong Kong Monetary Authority
https://www.hkma.gov.hk/eng

Hong Kong Special Administrative Region Government—Green Bond Programme **[NEW]**
https://www.hkgb.gov.hk/en/greenbond/greenbondintroduction.html

Securities and Futures Commission
https://www.sfc.hk/web/EN/index.html

Appendix 3
Glossary of Technical Terms

Authorized Institutions	Licensed banks, restricted license banks, and deposit-taking companies as defined in the Banking Ordinance
Automated Trading Services provider	Provider that operates or provides access to a trading platform, which represents an activity regulated by the SFC [NEW]
Bond Connect	Access channel to the Inter-Bank Bond Market for eligible investors with a CMU account [NEW]
Climate Bonds Initiative	International investor-focused, not-for-profit organization promoting and supporting the issuance of green and sustainable bonds and credit instruments [NEW]
Government Green Bond Programme	Bond issuance program of the Government of the HKSAR of the PRC to support green public works [NEW]
Green Bond Framework	Policy and process framework underlying the Government Green Bond Programme to ensure that identified processes are in line with Green Bond Principles [NEW]
Green Bond Grant Scheme	Grant scheme of the Government of the HKSAR of the PRC to attract green bond issuance in Hong Kong, China [NEW]
Green Bond Principles	Voluntary process guidelines that recommend transparency and disclosure, and promote integrity in the development of the green bond market [NEW]
iBonds	Inflation-linked bonds
Inter-Bank Bond Market	Bond market segment in the PRC regulated by the PBOC
Northbound Trading	Refers to access to the Inter-Bank Bond Market in the PRC via Bond Connect by eligible investors with an account at the CMU in Hong Kong, China [NEW]
Pilot Bond Grant Scheme	Grant scheme of the Government of the HKSAR of the PRC to attract new issuers to issue bonds in Hong Kong, China [NEW]
Professional Investor Rules	Securities and Futures (Professional Investors) Rules (Cap. 571D)
RMB Liquidity Facility	Facility offered by the HKMA to address potential short-term liquidity tightness in the offshore renminbi market
Silver Bonds	Inflation-linked bonds aimed at residents 65 years and over
Southbound Trading	Refers to access for investors in the China bond or capital market to the capital market in Hong Kong, China [NEW]

Source: ASEAN+3 Bond Market Forum Sub-Forum 1 team.

The Bond Market in Hong Kong, China

An ASEAN+3 Bond Market Guide Update

This report provides updates on the bond market in Hong Kong, China since the publication of the *ASEAN+3 Bond Market Guide 2016: Hong Kong, China*. It also highlights those changes and developments that have a connection to the bond market of the People's Republic of China. The *ASEAN+3 Bond Market Guide* series provides member-specific information on the investment climate, rules, laws, opportunities, and characteristics of local bond markets in Asia and the Pacific. It aims to help bond market issuers, investors, and financial intermediaries understand the local context and to encourage greater participation in the region's rapidly developing bond markets.

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ADB is committed to achieving a prosperous, inclusive, resilient, and sustainable Asia and the Pacific, while sustaining its efforts to eradicate extreme poverty. Established in 1966, it is owned by 68 members —49 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

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