

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 in 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.