

## Hong Kong, China—Update

### Yield Movements

The yield curve for Hong Kong, China's Exchange Fund Bills and Notes (EFBNs) shifted markedly downward between end-December 2011 and end-July 2012 (**Figure 1**). The downward shift was greatest for the 7-year tenor, which fell 89 basis points (bps). The longer-end of the curve shifted downward more sharply than the shorter-end, with the longer-end falling between 72 bps and 89 bps. The shorter-end of the yield curve, in contrast, fell only 7 bps–9 bps.

Due to the greater downward shift at the longer-end of the yield curve, the spread between the 2- and 10-year rates fell to 50 bps at end-July from 112 bps at end-December.

Yields declined as Hong Kong, China's economy continued to weaken. Gross domestic product (GDP) growth improved slightly in 2Q12, growing 1.1% year-on-year (y-o-y) from 0.4% in 1Q12. The sluggish GDP growth in the past 2 quarters has been driven by weakness in the external environment. Real exports grew 1.1% y-o-y in 2Q12 after falling 5.7% y-o-y in 1Q12.

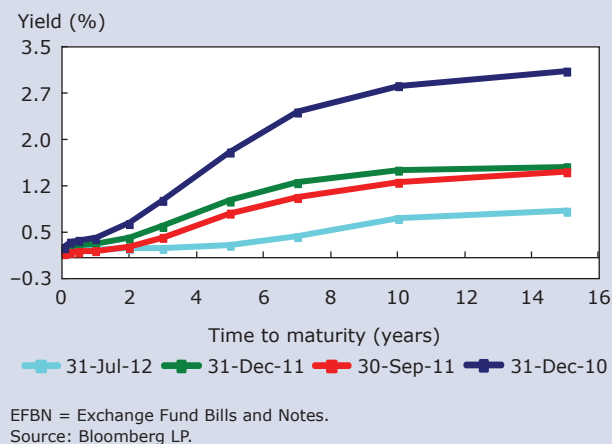
As a result of the weak economic performance, inflation tapered off in 2Q12. Consumer price inflation was at 4.3%, 3.7%, and 1.6% y-o-y for the months of May, June, and July, respectively. The decline in inflation rates was due mainly to moderating food and housing rental prices.

### Size and Composition

The size of Hong Kong, China's local currency (LCY) bond market grew 3.7% y-o-y to HKD1.3 trillion (US\$174 billion) at end-June (**Table 1**). On a quarter-on-quarter (q-o-q) basis, LCY bonds outstanding rose 1.2%.

Total LCY government bonds outstanding had risen 5.3% y-o-y and 2.1% q-o-q as of end-June. Government bonds include Exchange Fund Bills

**Figure 1: Hong Kong, China's Benchmark Yield Curve—EFBNs**



(EFBs), Exchange Fund Notes (EFNs), and bonds issued under the Institutional Bond Issuance Programme (HKSAR Bonds).

The amount of LCY government bonds outstanding at end-June reached HKD720 billion. Most of the growth in government bonds in 2Q12 can be attributed to growth in HKSAR Bonds, which expanded 113.3% y-o-y to HKD64 billion from HKD30 billion at end-June 2011. On the other hand, the stock of EFNs declined slightly by 0.9% y-o-y to HKD69 billion, while EFBs grew only 0.4% y-o-y to HKD587 billion.

In May, HKD3 billion in 3-year HKSAR Bonds were issued, while HKD1.5 billion in 5-year bonds were sold in June. Also, HKD10 billion in 3-year bonds were sold as part of the government's Retail Bond Issuance Programme in June.

The amount of LCY corporate bonds outstanding rose to HKD627 billion at end-June, reflecting growth of 1.9% y-o-y and 0.1% q-o-q. The top 25 non-bank corporate issuers in Hong Kong, China accounted for almost 15% of total corporate bonds outstanding at end-June (**Table 2**). Hong Kong, China's top corporate issuer of LCY bonds remained the state-owned Hong Kong Mortgage

Table 1: Size and Composition of the LCY Bond Market in Hong Kong, China

	Amount (billion)						Growth Rate (%)									
	Mar-12		Apr-12		May-12		Jun-12		Mar-12		Apr-12		May-12		Jun-12	
	HKD	US\$	HKD	US\$	HKD	US\$	HKD	US\$	HKD	US\$	HKD	US\$	HKD	US\$	HKD	US\$
Total	1,331	171	1,332	172	1,335	172	1,347	174	2.9	1.7	0.02	0.3	0.3	3.7	1.2	0.9
Government	705	91	705	91	709	91	720	93	3.5	0.3	0.01	0.4	0.4	5.3	2.1	1.7
Exchange Fund Bills	587	76	587	76	587	76	587	76	0.5	0.1	0.01	0.1	0.1	0.4	0.1	0.01
Exchange Fund Notes	69	9	69	9	69	9	69	9	(0.9)	0.0	0.0	(0.9)	0.0	(0.9)	(0.4)	0.4
HKSAR Bonds	50	6	50	6	53	7	64	8	80.0	3.1	0.0	6.1	0.0	113.3	29.3	21.9
Corporate	626	81	626	81	626	81	627	81	2.3	3.4	0.04	0.04	0.04	1.9	0.1	0.04

HKSAR = Hong Kong Special Administrative Region, LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.

Notes:

1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY-US\$ rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.

Source: Hong Kong Monetary Authority and Bloomberg LP.

Corporation (HKMC) with outstanding bonds valued at HKD17.7 billion at end-June. Sun Hung Kai Properties (Capital Market) Ltd. was the next largest issuer with outstanding bonds of HKD10.9 billion, while CLP Power Hong Kong Financing Ltd. was in the third spot with HKD10.5 billion.

Financial firms dominated the list of the top 25 non-bank corporate issuers, accounting for 9 out of the 25 issuers. Six state-owned companies were included on the list, while 14 were privately owned. Among the companies in Table 2, five are listed on the Hong Kong Exchange.

## Policy, Institutional, and Regulatory Developments

### HKMA Removes 20% Renminbi Net-Open Position Limits

On 22 May, the Hong Kong Monetary Authority (HKMA) removed the 20% renminbi net-open position limit for authorized institutions. The affected institutions may now set their own position limit so long as the HKMA is informed and endorses the proposed limit.

### Renminbi Liquidity Facility Opened

On 15 June, the HKMA established a facility through which authorized institutions can obtain renminbi funding, provided sufficient eligible collateral is available. The renminbi funding has a tenor of 1 week; eligible collateral includes EFBNs, HKSAR Bonds, and CNH-denominated bonds issued by the People's Republic of China (PRC).

### HKMA Launches Microfinance Scheme

On 29 June, the Hong Kong Mortgage Corporation, in cooperation with six banks and five non-governmental organizations (NGOs), launched the Microfinance Scheme to provide microfinance loans of up to HKD300,000 with a maximum tenor of 5 years. The target borrowers for the program are business starters; self-employed persons; and those wishing to undergo training, upgrade their skills, or take certification programs.

**Table 2: Top 25 Non-Bank Corporate Issuers in Hong Kong, China** (as of end-June 2012)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (HKD billion)	LCY Bonds (US\$ billion)				
1. The Hong Kong Mortgage Corporate Ltd.	17.66	2.28	Yes	No	No	Finance
2. Sun Hung Kai Properties (Capital Market) Ltd.	10.86	1.40	No	Yes	No	Real Estate
3. CLP Power Hong Kong Financing Ltd.	10.48	1.35	No	Yes	No	Energy
4. Kowloon-Canton Railway Corporation	6.30	0.81	Yes	No	No	Transportation
5. MTR Corporation (C.I.) Ltd.	6.20	0.80	Yes	No	Yes	Transportation
6. The Link Finance (Cayman) 2009 Ltd.	5.29	0.68	No	Yes	No	Finance
7. HKCG (Finance) Limited	5.29	0.68	No	Yes	No	Gas
8. Swire Pacific MTN Financing Ltd.	4.98	0.64	No	Yes	No	Diversified
9. Hongkong Electric Finance Ltd.	4.01	0.52	No	Yes	No	Energy
10. Urban Renewal Authority	3.00	0.39	Yes	No	No	Property Development
11. Airport Authority Hong Kong	2.60	0.34	Yes	No	No	Transportation
12. Wharf Finance Ltd.	2.50	0.32	No	Yes	No	Diversified
13. Cheung Kong Bond Finance Ltd.	2.45	0.32	No	Yes	Yes	Finance
14. Hysan (MTN) Ltd.	2.43	0.31	No	Yes	No	Finance
15. Cheung Kong Finance (MTN) Ltd.	2.21	0.28	No	Yes	No	Finance
16. Yue Xiu Enterprises (Holdings) Ltd.	2.00	0.26	No	Yes	No	Diversified
17. Henderson Land MTN Ltd.	1.83	0.24	No	Yes	Yes	Finance
18. Wheelock Finance Ltd.	1.59	0.20	No	Yes	No	Diversified
19. Cathay Pacific MTN Financing Ltd.	1.18	0.15	No	No	Yes	Airlines
20. Wharf Finance (No.1) Ltd.	1.14	0.15	No	Yes	No	Diversified
21. Dragon Drays Ltd.	1.00	0.13	No	Yes	No	Diversified
22. Bauhinia MBS Ltd.	0.86	0.11	Yes	No	No	Finance
23. Cheung Kong Infrastructure Finance (BVI) Ltd.	0.26	0.03	No	Yes	Yes	Finance
24. Wharf Finance (BVI) Ltd.	0.25	0.03	No	Yes	No	Diversified
25. The Hongkong Land Notes Company Ltd.	0.20	0.03	No	Yes	No	Finance
<b>Total Top 25 Non-Bank LCY Corporate Issuers</b>	<b>93.99</b>	<b>12.12</b>				
<b>Total LCY Corporate Bonds</b>	<b>626.73</b>	<b>80.79</b>				
<b>Top 25 as % of Total LCY Corporate Bonds</b>	<b>15.0%</b>	<b>15.0%</b>				

LCY = local currency.

Note: Based on Central Money Markets Unit data on tradeable non-bank debt securities issued and outstanding as of 1 July 2011.

Source: Hong Kong Monetary Authority.