

## Hong Kong, China

### Yield Movements

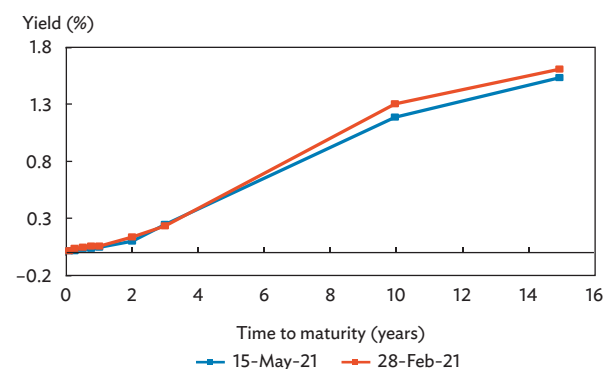
Between 28 February and 15 May, the local currency (LCY) government bond yield curve in Hong Kong, China shifted downward for all tenors except the 3-year, which gained 1 basis point (bp), and the 1-month, which was unchanged (**Figure 1**). Yields fell 3 bps on average, with the 10-year tenor showing the steepest drop at 12 bps. The spread between the 2-year and 10-year bonds narrowed from 117 bps to 109 bps from 28 February to 15 May.

The drop in yields for Hong Kong, China's LCY government bonds with maturities of 1 year or less broadly tracked the movements of short-dated United States (US) Treasury yields. Low yields also reflected strong liquidity in the domestic financial system. Due to several interventions by the Hong Kong Monetary Authority (HKMA) to maintain the Hong Kong dollar's peg to the US dollar amid seasonal and equity-related demand in 2020, the Aggregate Balance remained elevated during the review period. The Aggregate Balance, an indicator of liquidity in the financial system, totaled HKD457.5 billion on 15 May.

For bonds with maturities longer than 1 year, yield movements diverged from those of US Treasuries, whose rise reflected expectations that inflation in the US would quicken along with the pace of the domestic economic recovery. In contrast, inflation expectations in Hong Kong, China were subdued as economic activities remained below pre-recession levels. Consumer price inflation inched up to 0.7% year-on-year (y-o-y) in April from 0.5% y-o-y in March, mainly driven by a rise in local transport costs and motor fuel prices. The government's latest inflation outlook predicted headline and underlying consumer price inflation for full-year 2021 of 1.6% and 1.0%, respectively.

Hong Kong, China's GDP expanded 7.9% y-o-y in the first quarter (Q1) of 2021, ending 6 straight quarters of contraction. Nonetheless, the recovery was uneven. The growth was mainly driven by merchandise exports, which rose 30.2% y-o-y as economic recovery gained momentum in the People's Republic of China and the US. Consumption and investment remained muted as social distancing measures continued to limit tourism and other economic activities. The establishment of a travel bubble

**Figure 1: Hong Kong, China's Benchmark Yield Curve— Exchange Fund Bills and Notes**



Source: Based on data from Bloomberg LP.

with Singapore was postponed again due to a resurgence of COVID-19 cases. Private consumption inched up 1.6% y-o-y, while investment expanded moderately at 4.5% y-o-y in Q1 2021. Hong Kong, China's unemployment rate reached a 16-year high of 6.8% in January–March before easing slightly to 6.4% in February–April.

Despite the initial economic recovery, uncertainties linger stemming from several domestic and global factors. Hong Kong, China's vaccination rate trails that of other Asian financial hubs despite having an ample supply of vaccines. Geopolitical tension between the People's Republic of China and the US continues to pose downside risks to the domestic growth outlook. Finally, Hong Kong, China's path to recovery remains highly reliant on the global trajectory of the pandemic, particularly the speed and efficacy of vaccine rollouts.

### Size and Composition

Hong Kong, China's LCY bonds outstanding expanded 1.7% quarter-on-quarter (q-o-q) in Q1 2021 to reach HKD2,445.7 billion (USD314.6 billion) at the end of March (**Table 1**). The growth in the LCY bond market stemmed primarily from the corporate bond segment, which grew 3.1% q-o-q in Q1 2021. The government bond segment showed tepid growth of 0.2% q-o-q during the review period. Government bonds accounted for 48.6% of total LCY bonds outstanding at the end of March. On a y-o-y basis, the LCY bond market expanded 8.4% in Q1 2021, up from 6.1% in the fourth quarter of 2020.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2020		Q4 2020		Q1 2021		Q1 2020		Q1 2021	
	HKD	USD	HKD	USD	HKD	USD	q-o-q	y-o-y	q-o-q	y-o-y
<b>Total</b>	<b>2,255</b>	<b>291</b>	<b>2,405</b>	<b>310</b>	<b>2,446</b>	<b>315</b>	<b>(0.5)</b>	<b>0.3</b>	<b>1.7</b>	<b>8.4</b>
Government	1,170	151	1,185	153	1,187	153	(1.1)	0.7	0.2	1.5
Exchange Fund Bills	1,060	137	1,043	135	1,043	134	0.4	2.4	0.02	(1.5)
Exchange Fund Notes	27	3	25	3	25	3	0.0	(14.7)	0.0	(6.0)
HKSAR Bonds	83	11	117	15	119	15	(16.9)	(12.2)	2.3	43.2
Corporate	1,086	140	1,220	157	1,258	162	0.2	(0.2)	3.1	15.9

( ) = negative, HKD = Hong Kong dollar, HKSAR = Hong Kong Special Administrative Region, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

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

Source: Hong Kong Monetary Authority.

**Government bonds.** LCY government bonds outstanding reached HKD1,187.5 billion at the end of March on growth of 0.2% q-o-q. The growth was driven solely by a 2.3% q-o-q expansion of Hong Kong Special Administrative Region (HKSAR) bonds. The stock of Exchange Fund Bills (EFBs) and Exchange Fund Notes (EFNs) held steady during the review period. On a y-o-y basis, the stock of LCY government bonds rose 1.5% in Q1 2021. Government issuance declined 5.6% q-o-q in Q1 2021 as issuance of EFBs and HKSAR bonds contracted during the quarter.

**Exchange Fund Bills.** Due to maturities and a decline in issuance, outstanding EFBs barely grew in Q1 2021, amounting to HKD1,043.3 billion at the end of March. On a y-o-y basis, EFBs outstanding contracted 1.5% in Q1 2021. Issuance of EFBs amounted to HKD814.1 billion in Q1 2021, contracting 1.7% q-o-q.

**Exchange Fund Notes.** Since 2015, the HKMA has limited its issuance of EFNs to 2-year tenors. In February, the HKMA issued a 2-year EFN worth HKD1.2 billion. Due to maturities, outstanding EFNs remained steady at HKD25.0 billion in Q1 2021.

**HKSAR bonds.** HKSAR bonds outstanding amounted to HKD119.2 billion at the end of March on growth of 2.3% q-o-q and 43.2% y-o-y. The government issued a 10-year HKSAR bond worth HKD1.7 billion in February and a 15-year HKSAR bond worth HKD1.0 billion in March under the Institutional Bond Issuance Programme.

**Corporate bonds.** Corporate bonds outstanding reached HKD1,258.2 billion at the end of March on growth of 3.1% q-o-q and 15.9% y-o-y. The growth was driven by strong issuance as corporates tapped the bond market to meet their funding needs amid the low-interest-rate environment.

Hong Kong, China's top 30 nonbank issuers had a combined HKD283.6 billion of bonds outstanding at the end of March, accounting for 22.5% of the total LCY corporate bond market (Table 2). The government-owned Hong Kong Mortgage Corporation remained the top issuer with HKD60.7 billion of bonds outstanding at the end of Q1 2021. Sun Hung Kai & Co. maintained its position as second-largest issuer with HKD18.8 billion of bonds outstanding. The third-largest issuer was utilities provider Hong Kong and China Gas Company, with HKD17.3 billion of outstanding debt. The top 30 issuers were predominantly finance and real estate companies. A majority of the top 30 issuers were listed on the Hong Kong Stock Exchange; only four were government-owned corporations.

Corporate bond issuance totaled HKD294.8 billion in Q1 2021 on growth of 9.6% q-o-q and 38.1% y-o-y. Among the top nonbank issuers in Q1 2021, the Hong Kong Mortgage Corporation was the largest issuer with an aggregate HKD26.2 billion from 47 issuances, the largest of which was a 2-year bond with a 0.5% coupon worth HKD7.0 billion (Table 3). The next top issuer was Cathay Pacific, which raised HKD6.7 billion from a 5-year

Table 2: Top 30 Nonbank Corporate Issuers of Local Currency Corporate Bonds in Hong Kong, China

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (HKD billion)	LCY Bonds (USD billion)			
1.	Hong Kong Mortgage Corporation	60.7	7.8	Yes	No	Finance
2.	Sun Hung Kai & Co.	18.8	2.4	No	Yes	Finance
3.	The Hong Kong and China Gas Company	17.3	2.2	No	Yes	Utilities
4.	New World Development	14.2	1.8	No	Yes	Diversified
5.	Link Holdings	12.9	1.7	No	Yes	Finance
6.	Hong Kong Land	12.5	1.6	No	No	Real Estate
7.	Hang Lung Properties	12.4	1.6	No	Yes	Real Estate
8.	Henderson Land Development	12.3	1.6	No	Yes	Real Estate
9.	MTR	12.2	1.6	Yes	Yes	Transportation
10.	Swire Pacific	11.6	1.5	No	Yes	Diversified
11.	Cathay Pacific	9.3	1.2	No	Yes	Transportation
12.	Airport Authority Hong Kong	8.9	1.1	Yes	No	Transportation
13.	Hongkong Electric	8.5	1.1	No	No	Utilities
14.	Wharf Real Estate Investment	8.2	1.1	No	Yes	Real Estate
15.	CLP Power Hong Kong Financing	7.7	1.0	No	No	Finance
16.	Guotai Junan International Holdings	7.6	1.0	No	Yes	Finance
17.	Swire Properties	7.6	1.0	No	Yes	Diversified
18.	Smart Edge	6.5	0.8	No	No	Finance
19.	ALA Group	6.3	0.8	No	Yes	Insurance
20.	Hysan Development Corporation	5.7	0.7	No	Yes	Real Estate
21.	Future Days	4.2	0.5	No	No	Transportation
22.	Lerthai Group	3.0	0.4	No	Yes	Real Estate
23.	China Dynamics Holdings	2.4	0.3	No	Yes	Automotive
24.	Champion REIT	2.3	0.3	No	Yes	Real Estate
25.	South Shore Holdings	2.2	0.3	No	Yes	Industrial
26.	IFC Development	2.0	0.3	No	No	Finance
27.	Nan Fung	1.8	0.2	No	No	Real Estate
28.	Kowloon-Canton Railway	1.7	0.2	Yes	No	Transportation
29.	Haitong International	1.4	0.2	No	Yes	Finance
30.	Emperor Capital	1.4	0.2	No	Yes	Finance
<b>Total Top 30 Nonbank LCY Corporate Issuers</b>		<b>283.6</b>	<b>36.5</b>			
<b>Total LCY Corporate Bonds</b>		<b>1,258.2</b>	<b>161.8</b>			
<b>Top 30 as % of Total LCY Corporate Bonds</b>		<b>22.5%</b>	<b>22.5%</b>			

HKD = Hong Kong dollar, LCY = local currency, REIT = real estate investment trust, USD = United States dollar.

Notes:

1. Data as of 31 March 2021.

2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.

Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

**Table 3: Notable Local Currency Corporate Bond Issuances in the First Quarter of 2021**

Corporate Issuers	Coupon Rate (%)	Issued Amount (HKD billion)
Hong Kong Mortgage Corporation		
2-year bond	0.50	7.00
Cathay Pacific		
5-year bond	2.75	6.74
New World Development		
10-year bond	3.50	1.50
Guotai Junan International Holdings		
1-year bond	1.00	0.56
Hang Lung Properties		
7-year bond	2.35	0.56
Swire Pacific		
10-year bond	2.35	0.30

HKD = Hong Kong dollar.  
Source: Bloomberg LP.

bond with a 2.75% coupon. Other notable issuers during the quarter include New World Development, Guotai Junan International Holdings, Hang Lung Properties, and Swire Pacific. The longest tenor issued during the quarter were 10-year bonds from two issuers. New World Development raised HKD1.5 with its 10-year bond carrying a 3.50% coupon, while Swire Pacific raised a relatively smaller amount of HKD0.3 billion with its 10-year bond carrying a 2.35% coupon. Finance company Guotai Junan was another large issuer during the quarter. It raised a total of HKD2.7 billion from 10 issuances, the largest of which was a 1-year bond worth HKD0.6 billion and with a 1.0% coupon. Hang Lung Properties, another finance company, also raised a total of HKD2.7 billion. Its largest issue was a 7-year bond with a 2.35% coupon worth HKD0.56 billion.

## Policy, Institutional, and Regulatory Developments

### Hong Kong Monetary Authority and Bank of Japan Launch a Cross-Border Delivery-Versus-Payment Link

On 1 April, the HKMA and the Bank of Japan (BOJ) launched a delivery-versus-payment link for cross-currency securities transactions between the Hong Kong Dollar Clearing House Automated Transfer System and BOJ Financial Network System for Japanese Government Bond (JGB) Services. The delivery-versus-payment link provides settlement infrastructure for Hong Kong dollar sale and repurchase transactions using

JGBs as collateral. It helps reduce settlement risk by guaranteeing simultaneous delivery of Hong Kong dollars in Hong Kong, China and JGBs in Japan. The link is operated by BOJ in Japan and the Hong Kong Interbank Clearing Limited in Hong Kong, China.

### Hong Kong Monetary Authority Launches Green and Sustainable Finance Grant Scheme

On 10 May, the HKMA launched the Green and Sustainable Finance Grant Scheme, which will provide subsidies for eligible bond issuers and loan borrowers to cover expenses related to bond issuance and external review services. The scheme, which will last for 3 years, aims to strengthen Hong Kong, China's position as a regional green and sustainable finance hub, and help enrich its green and sustainable finance ecosystem. Eligible green and sustainable loans are those issued in Hong Kong, China with a size of at least HKD200 million, or the equivalent in a foreign currency, and have procured pre-issuance external review services by a recognized provider.

### Hong Kong Monetary Authority Holds Countercyclical Capital Buffer at 1.0%

On 17 May, the HKMA announced that the countercyclical buffer (CCyB) would remain unchanged at 1.0%. The HKMA noted that while there have been initial signs of recovery, the economy continued to face uncertainties driven by the global pandemic. Thus, holding the CCyB steady and monitoring the economic situation for a few more quarters was deemed more appropriate. The CCyB is an integral part of the Basel III regulatory capital framework designed to increase the resilience of the banking sector during periods of excess credit growth.