

## Hong Kong, China

### Yield Movements

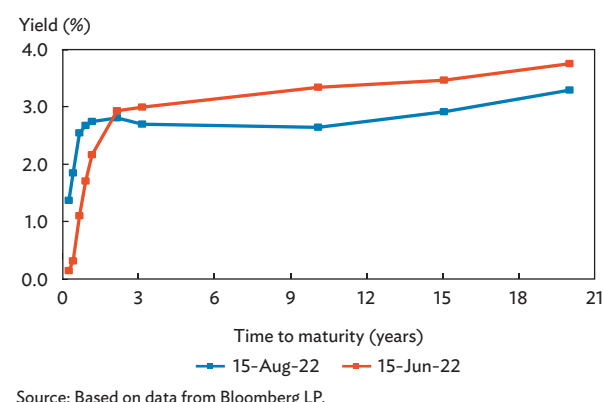
Between 15 June and 15 August, Hong Kong, China's local currency (LCY) government bond yield curve inverted, as yields rose for bonds with maturities of less than 2 years but fell for bonds with longer tenors (**Figure 1**). Yields for bonds with maturities of less than 2 years climbed an average of 115 basis points (bps). In contrast, yields for bonds with maturities of 2 years and longer dropped 43 bps on average. The 2-year yield shed 13 bps, while the 10-year yield plunged 70 bps. The yield curve's inversion started at the end of July and deepened toward the end of the review period. On 15 August, the spread between the 10-year and 2-year yields remained inverted at -16 bps.

Hong Kong, China's LCY bond yield movements during the review period tracked those of United States (US) Treasury yields as the Hong Kong dollar is pegged to the US dollar.<sup>8</sup> Yields for shorter-term US Treasuries jumped amid accelerated rate hikes by the US Federal Reserve, while yields for longer-term government debt fell, reflecting fears that the pace of monetary policy tightening could hamper economic recovery. The US Treasury yield curve was consistently inverted from 5 July through the end of the review period, with the 2-year outpacing the 10-year Treasury yield by as much as 39 bps on 15 August.

To rein in persistent inflation, the Federal Reserve raised the target range for its policy rate by 75 bps to 1.50%–1.75% in June and by an additional 75 bps to 2.25%–2.50% in July. To maintain the Hong Kong dollar's peg to the US dollar, the Hong Kong Monetary Authority (HKMA) adjusted its base rate by 75 bps to 2.00% on 16 June and by another 75 bps to 2.75% on 28 July. The rate hikes created upward pressure on yields at the shorter-end of government bond yield curves in both the US and Hong Kong, China.

The inversion in Hong Kong, China's LCY government bond yield curve also reflected lingering weakness in the domestic economy. Hong Kong, China's gross domestic product (GDP) contracted 1.3% year-on-year (y-o-y) in the second quarter (Q2) of 2022, following a decline

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



of 3.9% y-o-y in the first quarter (Q1). The contraction in merchandise exports deepened to 8.6% y-o-y in Q2 2022 from 4.5% y-o-y in Q1 2022, driven primarily by weaker exports to the People's Republic of China. Private consumption posted modest growth of 0.1% y-o-y in Q2 2022, a recovery from the 5.8% y-o-y drop in the previous quarter, as the relaxation of social distancing and government relief measures boosted demand. Government expenditure rose 13.0% y-o-y in Q2 2022, supported by spending on recovery efforts. The decline in investments narrowed to 3.0% y-o-y in Q2 2022 from 7.8% y-o-y in the prior quarter amid a slight revival of business sentiment. Given the weak performance in Q1 and Q2, and worsening global growth prospects, the government lowered its full-year 2022 GDP growth forecast in August to between -0.5% and 0.5% from a forecast of 1.0%–2.0% announced in May.

Inflation in Hong Kong, China remained moderate compared to that of other economies in the region. Consumer price inflation rose 1.9% y-o-y in July, following an increase of 1.8% y-o-y in June. The Census and Statistics Department expects inflation in the near-term to remain moderate as domestic cost pressure continues to be modest. The government's August forecast for full-year 2022 headline inflation remained at 2.1%, the same as its May projection.

<sup>8</sup> The Hong Kong dollar is pegged to a narrow band of between 7.75 and 7.85 versus the US dollar. The base rate is set at either 50 bps above the lower end of the prevailing target range of the US Federal Reserve rate or the average of the 5-day moving averages of the overnight and 1-month Hong Kong Interbank Offered Rate, whichever is higher.

## Size and Composition

Hong Kong, China's LCY bond market expanded 2.1% quarter-on-quarter (q-o-q) and 7.1% y-o-y in Q2 2022 to reach a size of HKD2,599.3 billion (USD331.3 billion) at the end of June (**Table 1**). Growth accelerated from 0.8% q-o-q and 4.1% y-o-y in Q1 2022, driven by a rebound in the corporate bond segment. Growth in the government bond segment dropped to near-zero in Q2 2022 from 3.3% q-o-q in the previous quarter. Meanwhile, the corporate bond segment registered a 4.4% q-o-q expansion in Q2 2022, reversing the 1.9% q-o-q decline in the preceding quarter. Robust issuance underpinned the expansion in corporate bonds. In terms of composition, Hong Kong, China's LCY bond market had a slightly higher share of government bonds (52.4%) than corporate bonds (47.6%) at the end of June.

**Government bonds.** Outstanding LCY government bonds totaled HKD1,361.1 billion at the end of June. Quarterly growth in Q2 2022 was marginal, as outstanding Exchange Fund Bills (EFBs) inched up 0.2% q-o-q, while outstanding Exchange Fund Notes (EFNs) and Hong Kong Special Administrative Region (HKSAR) bonds dropped 3.4% q-o-q and 0.4% q-o-q, respectively. On an annual basis, the government bond segment expanded 12.0% y-o-y in Q2 2022, down from 14.6% y-o-y in Q1 2022.

Total issuance of new government bonds reached HKD957.0 billion in Q2 2022 after rising 1.7% q-o-q and 11.9% y-o-y. Growth stemmed primarily from increased

issuance of HKSAR bonds, which rose 157.6% q-o-q during the review period.

**Exchange Fund Bills.** EFBs outstanding totaled HKD1,167.8 billion at the end of June on growth of 0.2% q-o-q and 11.8% y-o-y. EFBs continued to be the most dominant type of government bond, comprising 85.8% of total government bonds at the end of June. EFB issuance growth eased to 1.1% q-o-q in Q2 2022 from 3.0% q-o-q in the previous quarter.

**Exchange Fund Notes.** Outstanding EFNs amounted to HKD22.6 billion at the end of June after contracting 3.4% q-o-q and 6.6% y-o-y in Q2 2022. Since 2015, issuance of EFNs has been limited to the 2-year tenor. The HKMA issued HKD2.0 billion of such EFNs in May with a record-high coupon of 2.35%. EFNs continued to be the least dominant type of government bond, accounting for 1.7% of the total at the end of June.

**HKSAR bonds.** The outstanding stock of HKSAR bonds reached HKD170.7 billion at the end of June after a decline of 0.4% q-o-q. Bonds issued under the Institutional Bond Issuance Programme totaled HKD8.5 billion in Q2 2022. This included the inaugural issuance of 20-year bonds amounting to HKD0.5 billion in May. In addition, the government issued HKD4.0 billion of 3-year bonds in April, HKD1.5 billion of 1-year floating-rate notes indexed to the Hong Kong Overnight Index Average in May, and HKD2.5 billion of 5-year bonds in June. HKSAR bonds accounted for 12.5% of total LCY government bonds outstanding at the end of June.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2021		Q1 2022		Q2 2022		Q2 2021		Q2 2022	
	HKD	USD	HKD	USD	HKD	USD	q-o-q	y-o-y	q-o-q	y-o-y
<b>Total</b>	2,427	313	2,546	325	2,599	331	(0.8)	7.0	2.1	7.1
<b>Government</b>	1,216	157	1,361	174	1,361	173	2.4	5.1	0.04	12.0
Exchange Fund Bills	1,044	134	1,166	149	1,168	149	0.08	0.2	0.2	11.8
Exchange Fund Notes	24	3	23	3	23	3	(3.2)	(6.2)	(3.4)	(6.6)
HKSAR Bonds	147	19	171	22	171	22	23.6	66.4	(0.4)	15.9
<b>Corporate</b>	1,211	156	1,186	151	1,238	158	(3.7)	8.9	4.4	2.2

( ) = negative, HKD = Hong Kong dollar, HKSAR = Hong Kong Special Administrative Region, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

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

Source: Hong Kong Monetary Authority.

**Corporate bonds.** Hong Kong, China's LCY corporate bond market growth rebounded in Q2 2022 to reach a size of HKD1,238.2 billion at the end of June. The LCY corporate bond market expanded 4.4% q-o-q and 2.2% y-o-y in Q2 2022, reversing the 1.9% q-o-q and 5.8% y-o-y contractions in the previous quarter. Strong issuance supported the growth, as investor confidence improved during the review period amid the easing of movement restrictions.

The outstanding LCY bonds of the top 30 nonbank issuers in Hong Kong, China amounted to HKD317.8 billion at the end of June, accounting for 25.7% of the total LCY corporate bond market (**Table 2**). The Hong Kong Mortgage Corporation remained the largest issuer; its outstanding corporate debt of HKD87.4 billion at end of June comprised 7.1% of the total LCY corporate bond market. A distant second was Sung Hung Kai & Co. with outstanding corporate debt of HKD20.6 billion. The Hong Kong and China Gas Company, New World Development, and Henderson Land Development were the next largest issuers with outstanding bonds of HKD17.5 billion, HKD15.3 billion, and HKD14.1 billion, respectively, at the end of June. The top issuers were predominantly finance and real estate firms. Most corporate issuers were listed on the Hong Kong Stock Exchange, and only three were state-owned companies.

Corporate bond issuance during the review period amounted to HKD249.9 billion. Issuance growth almost tripled to 15.6% q-o-q in Q2 2022 from 5.5% q-o-q in the previous quarter, boosted by improved business sentiment amid the relaxation of social distancing measures.

**Table 3** shows notable issuances of the top corporate issuers in Q2 2022. The Hong Kong Mortgage Corporation was the largest issuer with a total of HKD17.3 billion from 38 issuances, the longest of which was a 3-year bond with a 3.66% coupon. The state-owned Airport Authority was the next largest issuer in Q2 2022, with six issuances totaling HKD5.0 billion. Haitong International raised a

total of HKD1.8 billion from short-term bonds, including the largest single issuance in Q2 2022: a 215-day bond worth HKD1.7 billion. Issuances during the review period had notably shorter maturities compared with the previous quarter. The longest tenor issued in Q2 2022 were 3-year bonds issued by The Hong Kong Mortgage Corporation, The Hong Kong and China Gas Company, and The Wharf (Holdings).

## Policy, Institutional, and Regulatory Developments

### Hong Kong Monetary Authority Participates in the Bank for International Settlements Renminbi Liquidity Arrangement

On 25 June, the Bank for International Settlements (BIS) announced a Renminbi Liquidity Arrangement developed with the People's Bank of China to provide liquidity to central banks through a new reserve pooling system. The HKMA is among the initial group of central bank participants, which includes the People's Bank of China, Bank Indonesia, the Bank Negara Malaysia, the Monetary Authority of Singapore, and the Banco Central de Chile. To set up the reserve pool placed with the BIS, each participating central bank contributed a minimum of CNY15.0 billion. The arrangement complements existing BIS liquidity facilities in providing liquidity access to contributing central banks in times of market volatility.

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

On 2 August, the HKMA decided to hold the countercyclical capital buffer (CCyB) ratio unchanged at 1.0%. The HKMA noted that although the latest data indicated a stabilization of economic activities, uncertainties from global and domestic factors remained elevated. Maintaining the CCyB at its current level and monitoring the economic situation was deemed appropriate. The CCyB is an integral part of the Basel III regulatory capital framework intended to strengthen the resilience of the banking sector globally.

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.	The Hong Kong Mortgage Corporation	87.4	11.1	Yes	No	Finance
2.	Sun Hung Kai & Co.	20.6	2.6	No	Yes	Finance
3.	The Hong Kong and China Gas Company	17.5	2.2	No	Yes	Utilities
4.	New World Development	15.3	1.9	No	Yes	Diversified
5.	Henderson Land Development	14.1	1.8	No	Yes	Real Estate
6.	Airport Authority	13.8	1.8	Yes	No	Transportation
7.	Hang Lung Properties	13.1	1.7	No	Yes	Real Estate
8.	Hongkong Land	12.0	1.5	No	No	Real Estate
9.	The Wharf (Holdings)	10.9	1.4	No	Yes	Finance
10.	CK Asset Holdings	10.0	1.3	No	Yes	Real Estate
11.	Link Holdings	9.8	1.3	No	Yes	Finance
12.	MTR	9.8	1.2	Yes	Yes	Transportation
13.	Swire Pacific	9.3	1.2	No	Yes	Diversified
14.	AIA Group	8.9	1.1	No	Yes	Insurance
15.	Cathay Pacific	8.7	1.1	No	Yes	Transportation
16.	Hongkong Electric	8.5	1.1	No	No	Utilities
17.	CLP Power Hong Kong Financing	7.4	0.9	No	No	Finance
18.	Swire Properties	7.3	0.9	No	Yes	Diversified
19.	Hysan Development Corporation	5.9	0.8	No	Yes	Real Estate
20.	Guotai Junan International Holdings	3.6	0.5	No	Yes	Finance
21.	Wheelock and Company	3.3	0.4	No	Yes	Real Estate
22.	Haitong International	3.1	0.4	No	Yes	Finance
23.	Lerthai Group	3.0	0.4	No	Yes	Real Estate
24.	Farsail Goldman International	2.4	0.3	No	No	Finance
25.	Ev Dynamics Holdings	2.4	0.3	No	Yes	Diversified
26.	South Shore Holdings	2.2	0.3	No	Yes	Industrial
27.	Future Days	2.2	0.3	No	No	Transportation
28.	IFC Development	2.0	0.3	No	No	Finance
29.	Nan Fung	1.8	0.2	No	No	Real Estate
30.	Champion REIT	1.7	0.2	No	Yes	Real Estate
<b>Total Top 30 Nonbank LCY Corporate Issuers</b>		<b>317.8</b>	<b>40.5</b>			
<b>Total LCY Corporate Bonds</b>		<b>1,238.2</b>	<b>157.8</b>			
<b>Top 30 as % of Total LCY Corporate Bonds</b>		<b>25.7%</b>	<b>25.7%</b>			

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

Notes:

1. Data as of 30 June 2022.

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 Second Quarter of 2022**

Corporate Issuers	Coupon Rate (%)	Issued Amount (HKD million)
The Hong Kong Mortgage Corporation <sup>a</sup>		
90-day bond	0.00	515
0.5-year bond	0.00	1,000
0.9-year bond	2.50	1,000
0.9-year bond	2.50	1,000
1-year bond	1.70	1,000
2-year bond	2.63	460
3-year bond	3.66	250
Airport Authority <sup>a</sup>		
2-year bond	2.80	1,500
2-year bond	2.80	1,000
2-year bond	2.80	1,000
Haitong International <sup>a</sup>		
0.6-year bond	2.10	1,700
0.6-year bond	2.00	100
Henderson Land <sup>a</sup>		
2-year bond	3.80	1,000
2-year bond	2.40	300
2-year bond	3.45	150
The Wharf (Holdings)		
2-year bond	2.85	400
3-year bond	3.40	300
The Hong Kong and China Gas Company <sup>a</sup>		
3-year bond	3.20	300
3-year bond	2.35	250

HKD = Hong Kong dollar.

<sup>a</sup> Multiple issuance of the same tenor indicates issuance on different dates.

Source: Bloomberg LP.