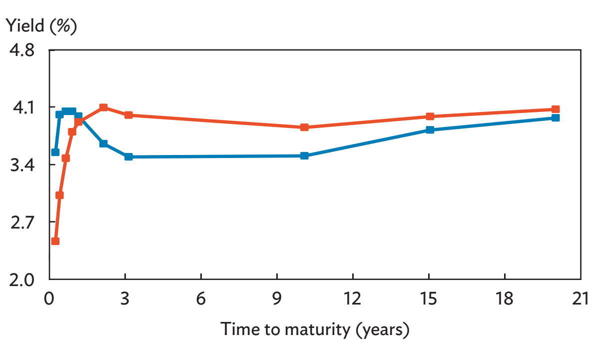
Hong Kong, China

Yield Movements

Hong Kong, China's local currency (LCY) government bond yields showed mixed movements between 1 March and 2 June. Yields jumped at the short-end but rose for all tenors longer than 1 year (**Figure 1**). The rise at the short end of the yield curve reflected tightened liquidity conditions. Several interventions by the Hong Kong Monetary Authority (HKMA) to defend the Hong Kong dollar's peg to the United States (US) dollar drained liquidity from the banking system. The aggregate balance—a measure of interbank liquidity—was down to HKD44.8 billion on 2 June from HKD77.0 billion on 1 March. The uptick in short-term bond yields was also influenced by the rise in the HKMA's policy rate. The HKMA adjusts its base rate in line with the US Federal Reserve's policy rate decisions to maintain the Hong Kong dollar's peg to the US dollar. On 4 May, the HKMA increased its base rate by 25 basis points to 5.50% after the Federal Reserve raised the target range for its policy rate by a quarter percentage point to a range of 5.00% to 5.25%. Meanwhile, the decline in yields for tenors longer than 1 year largely tracked yield movements of US Treasuries, which fell amid expectations that the Federal Reserve would pause its monetary policy tightening during its June meeting.

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

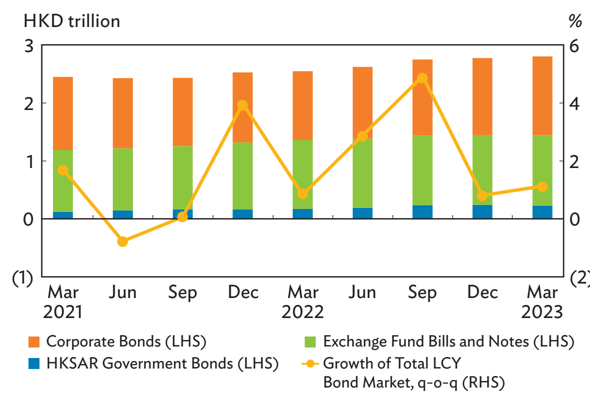


Source: Based on data from Bloomberg LP.

Local Currency Bond Market Size and Issuance

Hong Kong, China's LCY bond market reached a size of HKD2.8 trillion (USD356.9 billion) at the end of March. Total LCY bonds outstanding rose 1.1% quarter-on-quarter (q-o-q) in the first quarter (Q1) of 2023, up from 0.8% q-o-q in the preceding quarter (**Figure 2**). Growth was largely driven by the corporate bond segment, which expanded faster in Q1 2023 amid the recovery of the domestic economy. Hong Kong, China's gross domestic product rebounded, rising 2.7% year-on-year in Q1 2023 after recording 4 quarters of contraction in 2022. Corporate bonds dominated the LCY bond market, with the outstanding corporate bond stock of HKD1.4 trillion comprising 48.5% of total LCY bonds at the end of March. Exchange Fund Bills and Exchange Fund Notes together accounted for 43.4% of total LCY bonds, while Hong Kong Special Administrative Region (HKSAR) bonds had a smaller share of 8.1%. Exchange Fund Bills and Exchange Fund Notes are utilized as liquidity management instruments, hence their relatively larger share in Hong Kong, China's bond market.

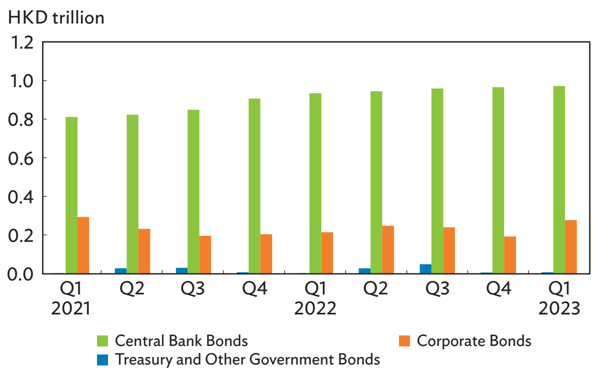
Figure 2: Composition of Local Currency Bonds Outstanding in Hong Kong, China



( ) = negative, HKD = Hong Kong dollar, LCY = local currency, LHS = left-hand side, q-o-q = quarter-on-quarter, RHS = right-hand side.
Source: Hong Kong Monetary Authority.

New issuance of LCY bonds jumped 7.8% q-o-q to HKD1.3 trillion in Q1 2023. Growth in HKSAR bond issuance rebounded, rising 30.0% q-o-q in Q1 2023 after posting an 87.8% q-o-q contraction in the prior quarter (**Figure 3**). HKSAR government bonds issued in Q1 2023 tallied HKD7.8 billion, including HKD0.8 billion of institutional green bonds and HKD1.5 billion of floating-rate notes indexed to the Hong Kong Dollar Overnight Index Average.

Figure 3: Composition of Local Currency Bond Issuance in Hong Kong, China



HKD = Hong Kong dollar, Q1 = first quarter, Q2 = second quarter, Q3 = third quarter, Q4 = fourth quarter.
Source: Hong Kong Monetary Authority.

The world's first tokenized government green bonds were issued in Hong Kong, China in February. A total of HKD0.8 billion worth of 365-day government green bonds were issued using distributed ledger technology, which shortened the settlement cycle. The same technology will be applied for the bond's coupon payment, settlement of secondary trading, and maturity redemption. The landmark issuance was part of Hong Kong, China's initiatives to promote innovation in financial technology and green and sustainable finance.

Issuance of corporate debt totaled HKD278.1 billion in Q1 2022, rising 43.3% q-o-q in Q1 2023 after contracting 19.7% q-o-q in the preceding quarter. The reopening of borders with the People's Republic of China and the return of business activities revived investor confidence and boosted demand for corporate bonds in Q1 2023. The largest nonbank corporate bond issuer was Hong Kong Mortgage Corporation with total issuances amounting to HKD28.2 billion in Q1 2023.