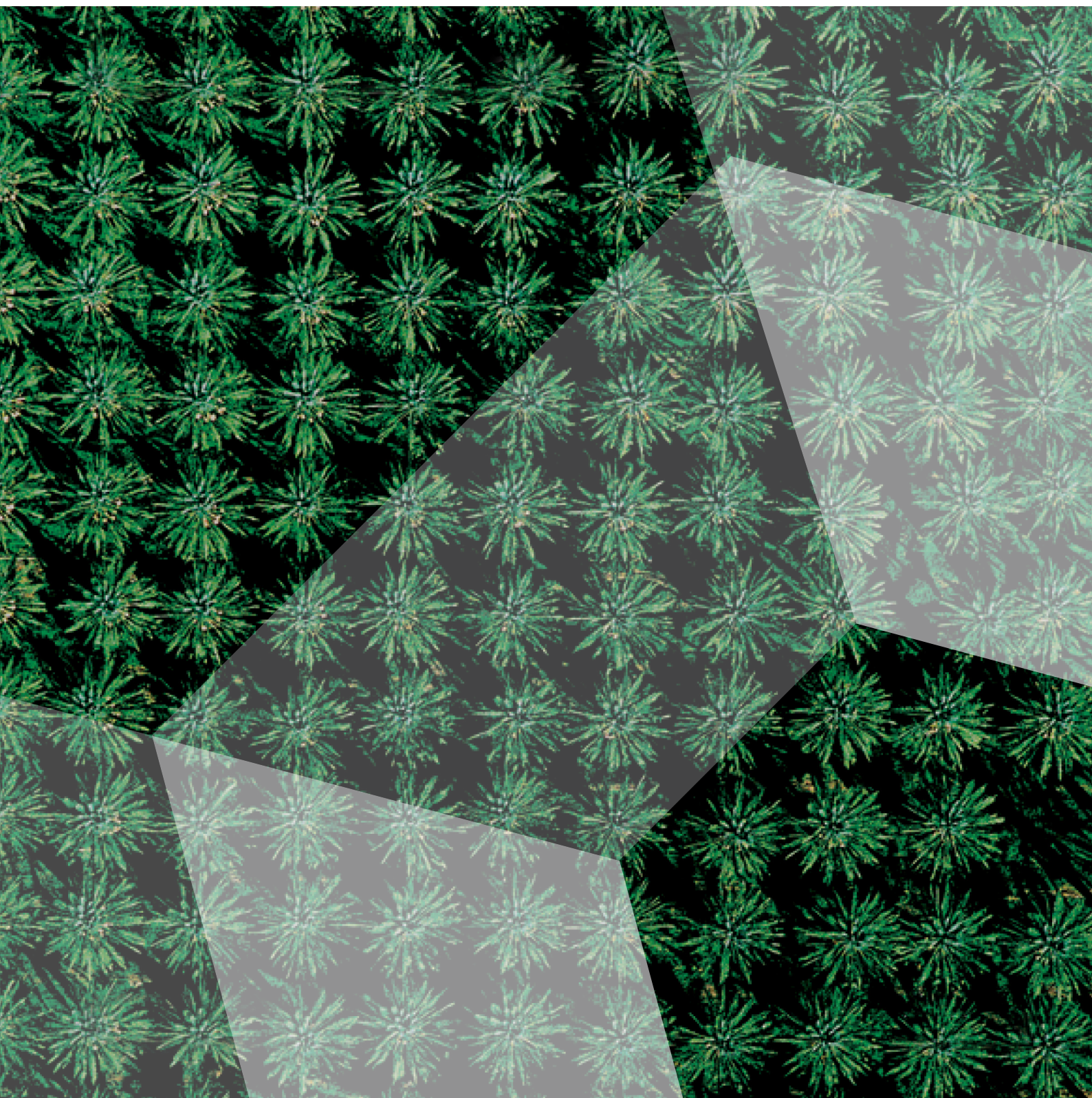


Research

FTSE Russell China Bond Research Report

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FTSE Russell China Bond Research Report

Highlights

- Foreign ownership of RMB-denominated Chinese government bonds rose to a record high in March as interest rates fell in many jurisdictions; and as the fallout from the coronavirus crisis rippled around the world. International investors owned a record 1.34 trillion RMB (US\$189 billion) of government bonds as of end-March according to FTSE Russell calculations of China Central Depository and Clearing Co (CCDC) data. This brings foreign holdings of Chinese government bonds to 8.7% by end-March.¹
- The ripple effects of the coronavirus crisis continue to make an impact on markets around the world. China's 10-year bond yields fell to record lows by end-March, falling further in April, as investors turned to sovereign debt because of the uncertainties unleashed by Covid-19.²
- The National Development and Reform Commission (NDRC) and China Securities Regulatory Commission (CSRC) announced in early March that China has launched a registration-based system for enterprise bond sales, ending the previous approval mechanism, thus encouraging the funds raised to invest in projects that conform to the macro-control policies and industrial policies. Moving forward, bond-issuing enterprises will only need to send applications to the CSRC to register.³

1 FTSE Russell; CCDC. April 2020.

2 FTSE Russell. April 2020.

3 NDRC & CSRC; Reuters. March 2020.

Chapter 1: Overview

Capital inflows rise despite a challenging time for China and other emerging markets

Foreign ownership of RMB-denominated Chinese government bonds rose to a record high in March as interest rates slipped in some markets; and as the global economy slumped due to the coronavirus crisis.

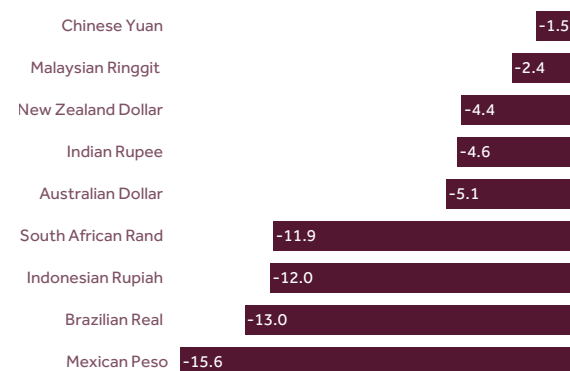
International investors owned a record 1.34 trillion RMB (US\$189 billion) of government bonds at the end of March according to FTSE Russell calculations of China Central Depository and Clearing Co (CCDC) data. This brings foreign holdings of Chinese government bonds to 8.7% by end-March. In contrast, during the same period, a number of emerging markets have experienced a larger volume of capital outflows such as Indonesia and Malaysia.⁴

For example, foreign holdings of Malaysian Government Securities (MGS) dropped by 16 billion Ringgit (US\$4.3 billion) in Q1, after reaching a 20-month high in January, when foreign investors held RM167.2 billion of MGS.⁵ Elsewhere, the outflow from Indonesia government bonds amounted to US\$8.3 billion, which reduced foreign holdings of the nation's government bonds to 32.7% in March, the lowest since January 2014.⁶

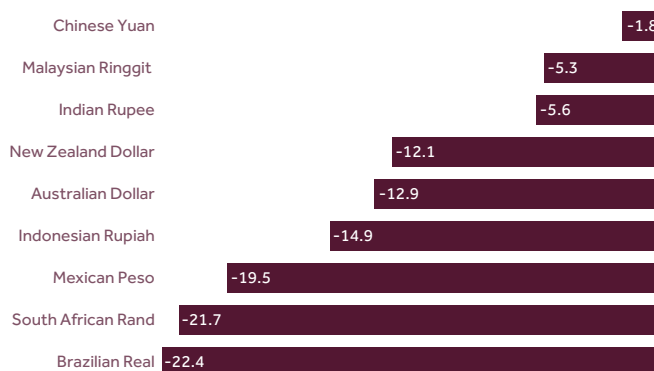
On the currency front, China's RMB depreciated by 1.8% against the US dollar in Q1. However, despite this slide, the RMB significantly outperformed a number of emerging market currencies, such as the Indonesia rupiah, Mexican peso, South African rand and Brazilian real.⁷ It also outperformed a number of developed market currencies including the New Zealand dollar and Australian dollar.⁸

Foreign Exchange Returns %

FX Moves vs USD – March



FX Moves vs USD – Q1



Source: FTSE Russell, April 2020.

⁴ FTSE Russell; CCDC. April 2020.

⁵ Bank Negara Malaysia; data calculated by FTSE. April 2020.

⁶ Bank Indonesia. April 2020.

⁷ FTSE Russell. April 2020.

⁸ FTSE Russell. April 2020.

Chapter 2: The coronavirus impact

The fallout from the coronavirus crisis continues to impact markets around the world. On that basis, China's 10-year bond yields fell by about 50bps in Q1 to a record low level by end-March, falling further in April, as investors turned to sovereign debt because of the uncertainties unleashed by Covid-19.⁹

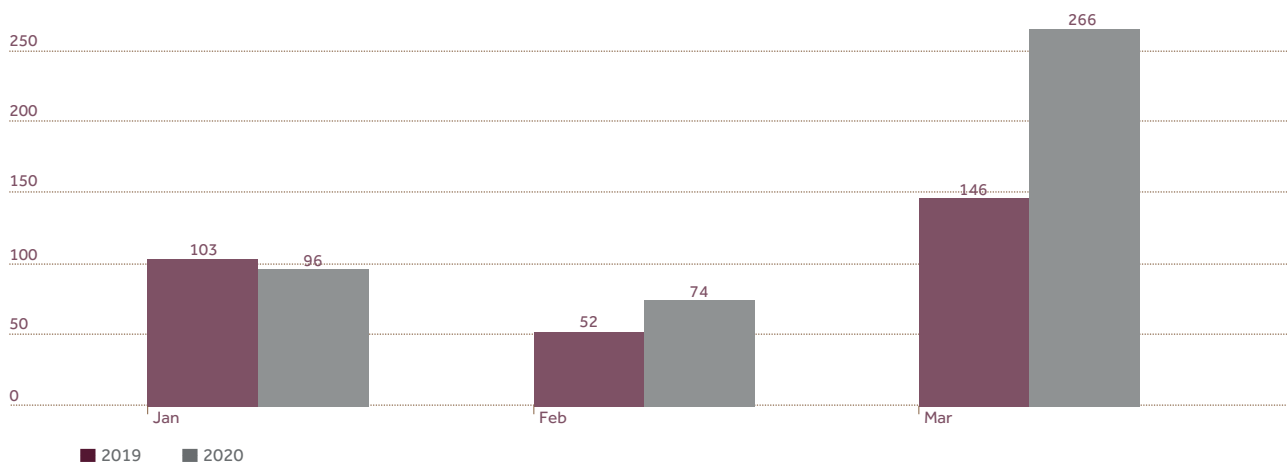
China Government Bond 10-year Yield



Source: FTSE Russell, May 2020.

Meanwhile, many Chinese companies – from drug distributors to airlines – continue to raise funds in an effort to weather the crisis. In the first half of February, more than 25 Chinese businesses raised RMB 24 billion (US\$3.4 billion)

Par Amount
CNY Billion
300



Source: Wind, May 2020.

⁹ FTSE Russell. April 2020.

¹⁰ Financial Times. February 2020.

Chapter 3: Regulatory changes and market infrastructure enhancements

Amid this uncertain environment, China's regulators are continuing efforts to further ease restrictions to encourage more capital flows into the world's second largest economy.

In early March, the NDRC – the regulator for enterprise bonds – and CSRC jointly announced that China has launched a registration-based system for enterprise bond sales, making it easier for enterprise to raise funds to invest in projects that conform to the macro-control policies and industrial policies. Moving forward, the previous 'approval system' will be abandoned, and bond-issuing enterprises will only need to send applications to the CSRC to register.¹¹

At the same time, China Central Depository & Clearing Co., Ltd. (CCDC) and Shanghai Clearing House launched two new initiatives, namely recycling settlement services to handle failed trades and longer settlement cycles beyond T+3 to accommodate the special settlement needs of foreign investors.¹²

The Recycling Settlement Service – which allows overseas investors to rearrange the settlement of cash bond trades that failed on the original settlement date within the required 3-days buffer period – offers overseas investors an effective tool for operational risk management; and the T+N (N≥4) Settlement Service allows investors to settle cash bond trades with non-standard settlement cycles (i.e. T+N, N≥4), aligning domestic settlement rules with international practices to meet special requirements from certain overseas investors, particularly during extended public holiday periods.¹³

Finally, in February, regulators announced further opening up of the treasury futures market to allow banks and insurance companies to participate with the first batch of top five commercial banks serving as pilot banks. This move marks the reopening of a market that was shut in the 1990s after a panicked sell-off that saw the collapse of the country's largest brokerage. The availability of treasury futures is important for market makers as an additional hedging tools to manage interest rate risks.

Chapter 4: Performance of the FTSE Russell China Bond Indexes

Onshore Report

Yield

Five major sectors are covered in FTSE Chinese (Onshore CNY) Broad Bond Index (CNYBBI). The yield of the CNYBBI as of end-March was 2.60%. Among the five major sectors, the Government Bond (CGB) sector was at 2.41%; the Policy Bank sector (issued by Agricultural Development Bank of China, China Development Bank and The Export-Import Bank of China) was at 2.67%; the Regional Government sector was at 2.58%; the Corporate sector was at 2.89%; the Government Sponsored (issued by China Central Huijin Ltd. and China Railway Co.) was at 2.92% as shown in the chart below.

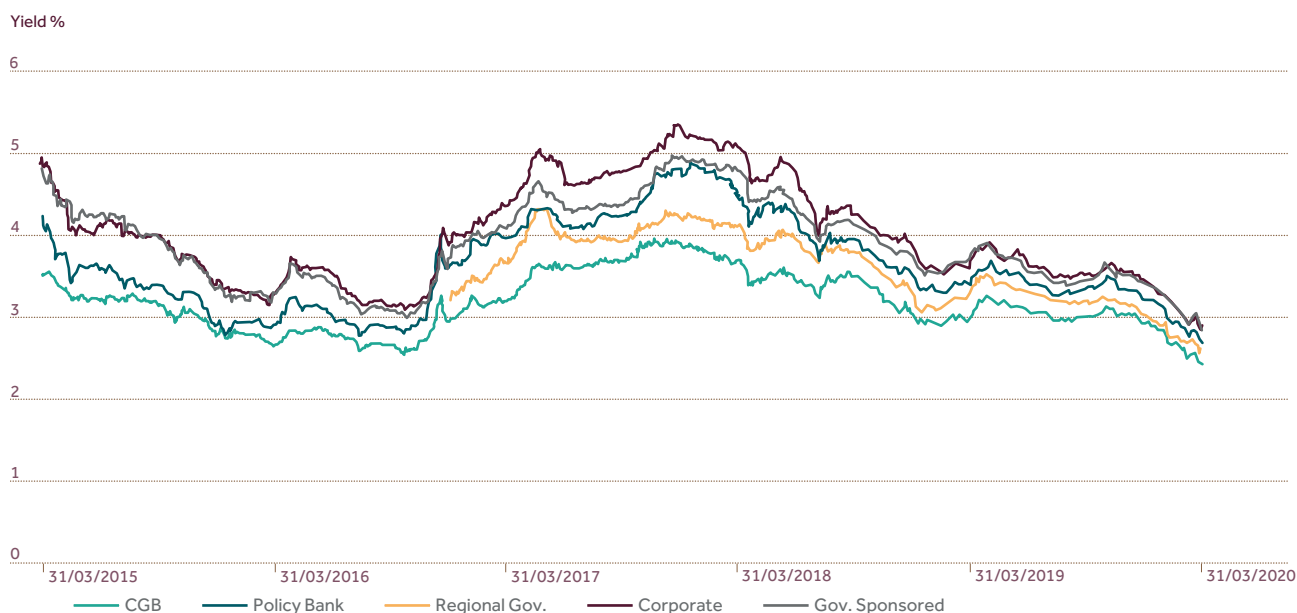
¹¹ NDRC & CDRC; Reuters. March 2020.

¹² ChinaBond. April 2020.

¹³ ChinaBond. April 2020.

For 2020 Q1, the yield of CNYBBI decreased by 50.85bps with corporate spread tightened by 7.66bps.

Chart 1. The Historical Yield of 5 Sectors in CNYBBI Sectors



Source: FTSE Russell, data as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

Total Return

The CNYBBI in USD unhedged terms finished up 1.23% while its return in CNY finished up 3.09% during the last quarter. The returns of some sectors are shown in Table 1.

Table 1. Performance and Volatility – Total Return (USD)

	Cumulative Return (USD, unhedged)					Annualized Volatility		
	3M	6M	1YR	3YR	5YR	1YR	3YR	5YR
CNYBBI	1.23	5.11	0.94	14.06	11.67	4.32	4.29	3.98
CGB	1.66	5.41	0.72	12.36	9.75	4.63	4.51	4.19
Policy Bank	1.30	5.30	1.29	15.37	12.52	4.31	4.34	4.09
Corporate	0.32	3.85	-0.01	14.12	13.15	4.27	4.16	3.84

Source: FTSE Russell – total return data in USD, as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

FTSE Chinese (Onshore CNY) Green Bond Index

Yield

There are three different versions of FTSE Chinese (Onshore CNY) Green Bond Index (CNYGRBI): CNYGRBI, FTSE Chinese (Onshore CNY) Internationally-Aligned Green Bond Index, and FTSE Chinese (Onshore CNY) Internationally-Aligned Green Bond Index – Interbank. The yield of the CNYGBRI as of end-March was 2.94%. Among the sub-indexes, FTSE Chinese (Onshore CNY) Internationally-Aligned Green Bond Index, was at 2.71%; FTSE Chinese (Onshore CNY) Internationally-Aligned Green Bond Index – Interbank was at 2.66%, as shown in the chart below.

For 2020 Q1, the yield of CNYGRBI decreased by 53.75bps.

Chart 2. The Historical Yield of China Green Bond Index

Yield %



Source: FTSE Russell, data as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

Total Return

The FTSE Chinese (Onshore CNY) Green Bond Index finished up 0.28% during the last quarter, with its Internationally-Aligned sub-index up 0.10% and its Internationally-Aligned – Interbank sub-index up 0.08%.

Table 2. Performance and Volatility – Total Return (USD)

	Cumulative Return (USD, unhedged)				Annualized Volatility	
	3M	6M	1YR	3YR	1YR	3YR
Chinese Bond Index	0.28	3.99	0.01	13.74	4.26	4.15
Chinese Bond Index – International Align	0.10	3.73	-0.36	13.27	4.29	4.17
Chinese Bond Index – IA – Interbank	0.08	3.71	-0.41	13.26	4.29	4.17

Source: FTSE Russell – total return data in USD, as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

Chart 3. CNYBBI Performance in USD vs in CNY for the past 5 years

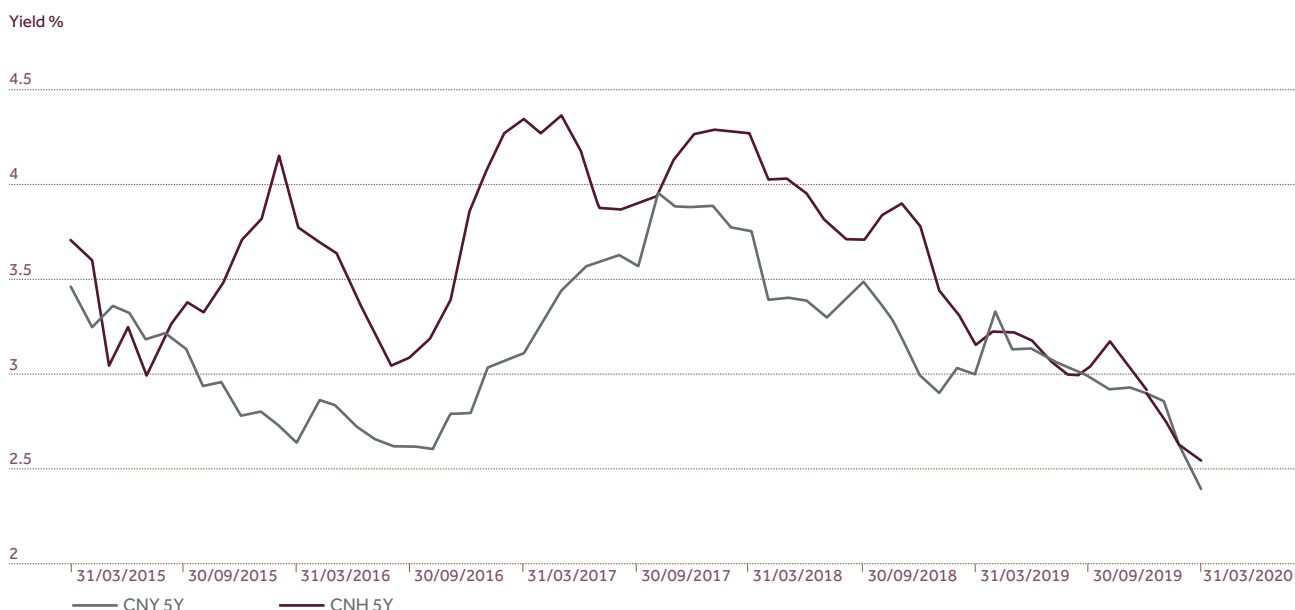
Source: FTSE Russell – total return data in USD and CNY, as of March 31, 2020. Past performance is no guarantee of future results. Please see the end for important legal disclosures.

Comparison of Offshore Sovereign Bonds and Onshore Sovereign Bonds

Yield

The yield of onshore 5-year Sovereign bonds was at 2.40% and the yield of offshore 5-year Sovereign bonds was at 2.54% as of end of Q1. The spread widened by 15bps for Q1 of 2020 as shown in Chart 4.

Chart 4. Onshore 5 Year Yield vs Offshore 5 Year Yield



Source: FTSE Russell as of March 31, 2020. Past performance is no guarantee of future results. Please see the end for important legal disclosures.

As of end of Q1 2020, the Offshore Chinese Treasury Yields were higher than the Onshore Chinese Treasury Yields over the entire curve. The short end curve 1-year spread was 53bps and the long end curve 10 year spread was 15bps.

Total Return

The FTSE Chinese Government Bond Index outperformed the FTSE Offshore counterpart during Q1 2020 as shown in Table 3.

Table 3. Performance and Volatility – Total Return (USD)

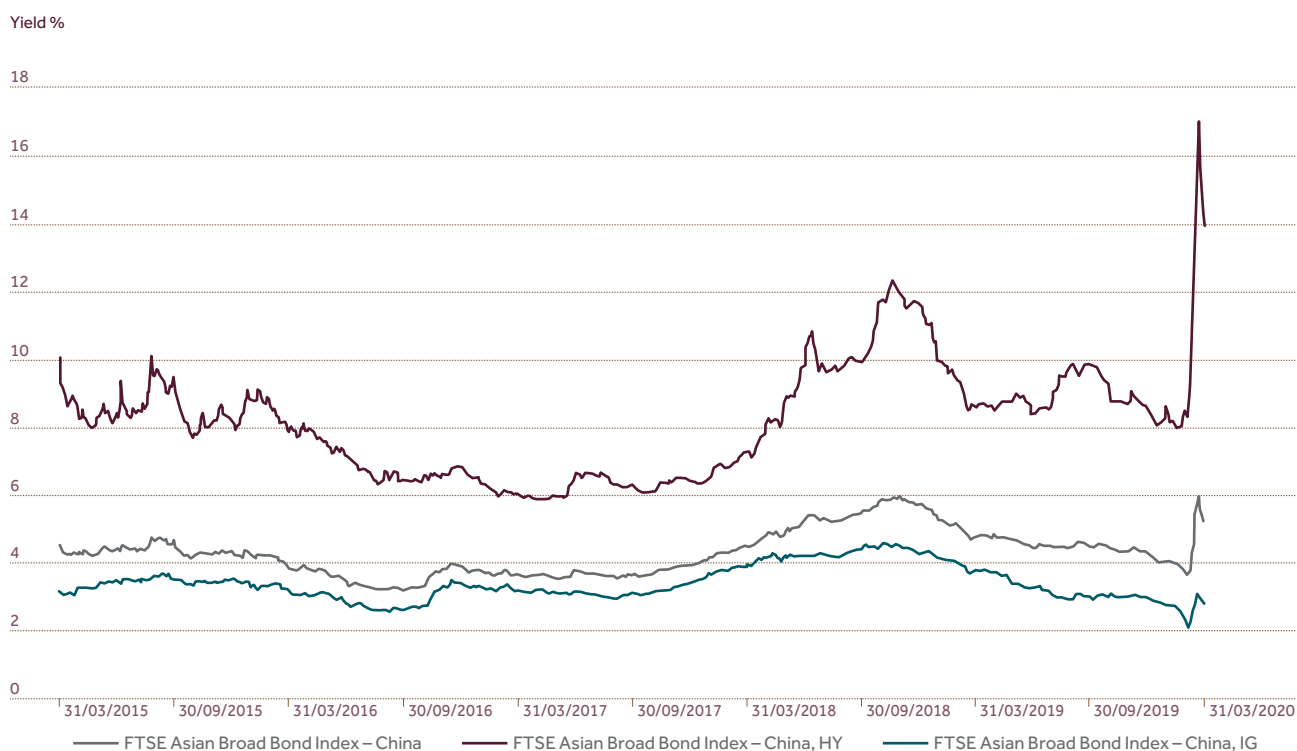
	Cumulative Return (USD, unhedged)					Annualized Volatility		
	3M	6M	1YR	3YR	5YR	1YR	3YR	5YR
FTSE Chinese Government Bond Index (Onshore CNY)	1.66	5.41	0.72	12.36	9.75	4.63	4.51	4.19
FTSE Chinese Government Bond Index (Offshore CNY)	0.12	3.57	-0.41	14.19	8.02	5.01	4.72	4.69

Source: FTSE Russell, total return data in USD, as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures. FTSE Chinese Government Bond Index (Offshore CNY) is a sub-index in the FTSE Dim Sum (Offshore CNY) Bond Index.

USD Bonds Issued by Chinese Issuers

Yield

The yield of the FTSE Asian Broad Bond Index - China was at 5.21%. Among the two sub-indexes the FTSE Asian Broad Bond Index – China, Investment-Grade Index was at 2.82%; the FTSE Asian Broad Bond Index – China, High-Yield Index was at 13.98% as shown in the below chart.

Chart 5. The Yield of FTSE Asian Broad Bond Index – China and Sub-Indexes

Source: FTSE Russell - total return data in CNY, as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

Total Return

The FTSE Asian Broad Bond Index-China finished down 1.03% during the last quarter, with its Investment-Grade sub-index up 1.63% and its High-Yield sub-index down 9.66%.

Table 4. Performance and Volatility – Total Return

	Cumulative Return (USD, unhedged)					Annualized Volatility		
	3M	6M	1YR	3YR	5YR	1YR	3YR	5YR
FTSE Asian Broad Bond Index – China	-1.03	0.43	4.79	12.83	24.29	3.72	2.47	2.43
FTSE Asian Broad Bond Index – China, IG	1.63	2.25	7.84	15.83	23.89	3.38	2.37	2.46
FTSE Asian Broad Bond Index – China, HY	-9.66	-5.66	-5.02	2.90	30.50	7.68	4.97	4.59

Source: FTSE Russell - total return data in USD, as of March 31, 2020. Past performance is no guarantee of future results. Returns shown prior to index launch reflect hypothetical historical performance. Please see the end for important legal disclosures.

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