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Why it's just the beginning for China's RMB bond market

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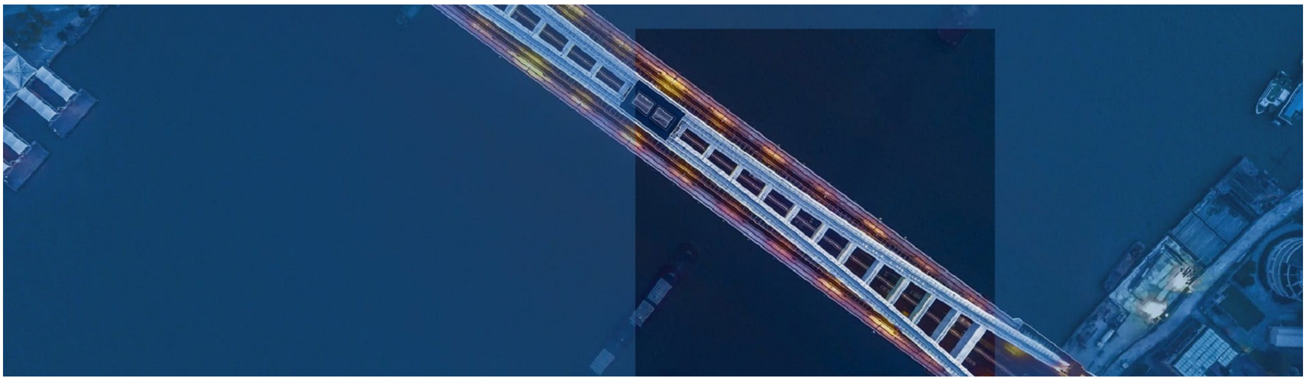

Summary

China's efforts to provide greater access to the renminbi bonds market – work that began more than a decade ago – is giving international investors the confidence to increase their holdings.

Key takeaways

- As China's onshore bond market has opened up, China government bonds and policy bank bonds have been included in a number of major international bond indices, prompting many investors to rapidly build up their holdings
- Foreign investors are attracted to the added yield potential of China's RMB bonds, plus the monetary policy flexibility of China's central bank, but the steady stream of reforms is what has made these bonds more accessible
- Some foreign investors have become worried about rising credit defaults and poor liquidity in onshore corporate credit bonds in particular, but China's regulators are alert and taking action

The following article is a summary of insights from our 2021 Asia Conference.

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In the world of fixed income, China is quickly drawing international interest and investment. Its bond market has been steadily opening up, which has led to the inclusion of China "rates" bonds – a category consisting of government bonds (CGBs) and policy bank bonds – in a number of major international bond indices.

As a result, many investors are rapidly building their China exposure, albeit from a low base. Foreign ownership in China's "onshore" bond market – bonds denominated in renminbi (RMB) – has doubled in less than three years, according to Yin Liu, who spoke at the Allianz Global Investors 2021 Asia Conference in June. Mr Liu is a senior director of international cooperation at China's National Association of Financial Market Institutional Investors (NAFMII)[1]. At the end of 2020, according to Mr Liu, foreigners owned RMB 3.25 trillion of the bonds traded on the China Interbank Bond Market (CIBM). That is equivalent to 3.23%,[2] up from the June 2018 figure of 1.5%.

What is attracting so much international investment? Some of the top factors are the attractive yield pick-up of Chinese bonds versus other markets, alongside ample monetary policy flexibility from China's central bank. But the international investors recently drawn to Chinese bonds would not even be considering this asset classes without the steady stream of reforms that recently opened up the market.

“This influx of foreign flows has been happening for two or three years,” explained Mr Liu. “It’s very profitable to invest in China. Further, the economy is stable, monetary policy is normal and we have ample tools to take care of any market turmoil. That’s the main backdrop for the foreign inflow of money. But we do a lot of work to support the foreign investors coming into the market.”.

Opening up of the onshore bond market

The work to make China’s onshore markets more accessible started over a decade ago (see accompanying timeline).

- Since 2011, a series of reforms allowed foreign investors increasing access to a wider range of fixed-income instruments in China’s onshore bond market.
- A milestone event was the introduction of China Interbank Bond Market (CIBM)[3] Direct in 2016, which allowed foreign investors quota-free access to CIBM. All that was required was registration with the People’s Bank of China (PBoC) and the appointment of an onshore custodian bank.
- Separately, in 2017, the introduction of the Bond Connect programme enabled trades to be settled via custodian banks in Hong Kong, further liberalising foreign investors’ market access to the mainland bond market through Hong Kong.

As the market opened up, major global bond indices began to include CGBs and policy bank bonds, which further encouraged international investors. Most recently, FTSE Russell completed the inclusion of CGBs in its flagship FTSE World Government Bond Index (WGBI). The initial inclusion came in March 2021, at a 5.25% weighting.

Market access regulations have relaxed in recent years

Source: IPECapital, Data as of 30 September 2019. The above is for illustrative purposes only and is not a recommendation or advice to buy or sell any security. Past performance, or any prediction, projection or forecast, is not indicative of future performance.

Looking forward

Even as foreign investment has ramped up, some foreign investors have become worried about rising credit defaults and poor liquidity in corporate credit bonds in particular. On both topics, Mr Liu stressed that the regulators are alert and taking action. In the case of credit ratings, he cited the enforcement actions taken against local rating agencies, as well as the issuance of licences to international agencies S&P Global and Fitch Ratings. He also said that NAFMII was examining ways to improve liquidity in areas such as government bonds and repurchase agreements (repos).

What Mr Liu made clear was that the regulators, led by the PBoC, were committed to continuing improving the market, listening to investors as they go.

Giving an international investor’s view, David Tan, CIO Fixed Income Asia Pacific at Allianz Global Investors, said: “Recently, we've seen Asia grow tremendously and become a big part of most global equity portfolios. As a bond market investor myself, I see this trend also happening for the RMB bond market. I think it's just the beginning.”

[1] NAFMII was founded under the approval of the State Council of China to aid the development of China’s over-the-counter (OTC) financial markets. These OTC markets include China’s inter-bank bond market and foreign exchange market, among others.
[2] Sources: China Central Depositary & Clearing Co. Ltd.; Shanghai Clearing House.
[3] CIBM is the main trading venue for Treasury, policy bank and commercial bank bonds accounting, accounting for 85% of the entire onshore bond market. Originally, foreign investors were allowed to invest in the CIBM under the QFII/RQFII market access schemes, following certain quotas.

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DISC

Unwrapping the potential of sustainable packaging

by | 04/01/2022

Summary

Plastics – and especially plastic packaging – play an essential role in the global economy, as they prevent products from being spoiled, and significantly extend the shelf-life of food. Additionally, the comparatively low weight of plastic packaging contributes to energy and fuel savings, and to reducing greenhouse gas emissions from freight transport. However, the advantages of plastics have to be set against a number of drawbacks, particularly for the environment. The absence of a circular plastic economy, and the leakage of millions of tonnes of plastic material, not only contribute in large part to marine pollution, but also trigger immense economic costs, and billions of USD in negative externalities. Fostering the further development of sustainable packaging therefore not only helps to limit the volume of plastic waste, but also offers attractive opportunities to participate in a market that is predicted to show a double-digit percentage growth rate within the next five years.

Key takeaways

- According to analysis, 95% of plastic packaging material value, equivalent to between USD 80–120 billion per year, leaves the economy (in the form of waste).[1]
- The recycling rate of plastics is only around 14%. Due to additional value losses during sorting and reprocessing, only about 5% of plastic packaging is reused for packaging, while most of the remaining 9% is used for lower-value applications.[2]
- Nearly a third of all plastic packaging is not available for recycling.[3]
- Plastic packaging contributes almost USD 40 billion-worth of greenhouse gas emissions and other environmental damage every year.[4]
- Expenditures arising from these post-use effects, as well as from greenhouse gas emissions caused by plastic production, amount to at least USD 40 billion annually.[5]
- The sustainable-packaging market is expected to grow from an estimated USD 305 billion in 2020 to almost USD 470 billion in 2027.[6]