



Recent Developments and Future Direction

A. Recent Developments

Recent major developments are considered those that occurred or have been announced in the PRC since the first publication of the *ASEAN+3 Bond Market Guide* in April 2012, with a particular focus on the CIBM.

1. Revision of Rules and Regulations for Registration and Issuance

On 16 April 2020, NAFMII published revisions of a number of rules and regulations related to the registration and issuance of debt financing instruments by nonfinancial enterprises. The revisions included rules for both publicly offered debt financing instruments and provisions related to private placements, specifically PPN. NAFMII's stated purpose of the revisions was to streamline the registration process and to encourage further issuance of debt financing instruments.

NAFMII introduced a further differentiation of issuers through sub-categories and specific disclosure obligations or concessions for each of these sub-categories. NAFMII also included provisions for the use of a bond trustee (see also next section) in the public offering rules. The new rules took effect on 1 July 2020.

The description of the new categories and the related changes and concessions can be found in Chapter II.F.

2. Introduction of a Bond Trustee Concept

On 27 December 2019, NAFMII introduced the concept of a formal “bond trustee” to assume the role of representative of debt financing instrument holders for instruments (to be) registered with NAFMII. The new rules took effect on 1 July 2020.

The new rules, formally called Guidelines for Bond Trustee Business of Non-Financial Enterprise Debt Financing Instruments in the Inter-Bank Bond Market (for Trial Implementation) (银行间债券市场非金融企业债务融资工具受托管理人业务指引(试行)), stipulate that the bond trustee represents the debt financing instrument holders when necessary.

For more details about the designation of bond trustee and their qualifications, as well as provisions for bond trustee activities, please refer to Chapter III.S. The change of a bond trustee or of a bond trustee agreement has also been included as a reason for the calling of a meeting of debt financing instrument holders in corresponding meeting rules and procedures issued by NAFMII in December 2019 and effective in July 2020. Chapter III.R has more details on the reasons and processes around debt financing instrument holder meetings.

3. State Administration of Foreign Exchange Abolished Qualified Foreign Institutional Investor and Renminbi Qualified Foreign Institutional Investor Quotas

Effective 10 September 2019, SAFE announced the abolition of the investment quotas for the QFII and RQFII schemes for market access into the PRC capital market. With investment allocation and repatriation limitations gradually eliminated in recent years (see also section 6), only the need to apply for a QFII or RQFII license and some administrative actions remain. Please also see Chapter II.N for comprehensive descriptions of the QFII and RQFII market access schemes.

4. Inclusion of People's Republic of China Government Bonds in International Bond Indexes

In early September 2019, J.P. Morgan announced that it would begin including PRC government bonds in its GBI-EM, eventually comprising a share of 10% of the GBI-EM. The inclusion of PRC government bonds in the BGI-EM commenced on 28 February 2020 and was scheduled to occur over a 10-month period, at a rate of 1% per month, to lessen market impact.

Starting in April 2019, Bloomberg began to include PRC government bonds in its Bloomberg Barclays Global Aggregate Index; the inclusion was to be phased in over a 20-month period and would represent about 6% of the total index value upon completion. At the same time, PRC government bonds also became eligible for inclusion in the Bloomberg Barclays Global Treasury and Emerging Markets Local Currency Government Indexes.¹¹⁰

5. Unified Management of the Credit Rating Business

On 11 September 2018, the PBOC and CSRC announced the creation of unified guidelines for CRAs and their activities in both the CIBM and exchange bond markets in response to findings in a review of CRAs and their work.¹¹¹ The guidelines are intended to improve credit rating quality; increase transparency in the credit rating business in the China bond market overall; and unify the admission of CRAs, their supervision and inspection, as well as the actual credit rating process across bond market segments.

In July 2017, the PBOC opened the bond credit rating market to the outside world by permitting the set-up of overseas CRAs and their conducting of credit rating operations in the CIBM, promoting the further liberalization of the CIBM and the healthy development of the credit rating industry in the PRC. In January 2019, the PBOC permitted S&P Global (China) Ratings to register for credit rating services in the CIBM. S&P Global (China) Ratings issued its first bond credit rating in July 2019.¹¹² In May 2020, Fitch (China) Bohua Credit Ratings Ltd. received PBOC approval and a license from NAFMII to carry out bond rating activities in the CIBM.

For a detailed description of the eligibility and regulation of CRAs, please see Chapter II.O. The actual credit rating requirements for the issuance of debt financing instruments in the CIBM are covered in Chapter III.O.

¹¹⁰ Information adapted from the October 2019 issue of *ChinaBond Watch* and news reports in the public domain.

¹¹¹ See Joint Notice No. 14 (2018), Enhance Unified Management of Credit Rating and Facilitate Connectivity of the Bond Market, at <http://www.pbc.gov.cn/english/130721/3628161/index.html>.

¹¹² Information adapted from news reports in the public domain.

6. Introduction of the Financial Stability and Development Commission

In November 2017, the Government of the PRC formally set up the FSDC under the State Council to oversee financial stability and development focusing on the deliberation and coordination of major issues concerning financial stability and related reform and development in the financial and capital markets.

According to a news release by the State Council, the primary purposes of the FSDC are to “strengthen financial regulatory coordination and supplement regulatory shortcomings, strengthen the regulatory role of financial regulatory departments, and ensure the safe and stable development of the Chinese financial sector.”¹¹³ Its remit includes structural optimization and improvements to financial markets, financial institutions, and the financial products system.

The FSDC is expected to uphold quality as its chief priority, guide the financial sector's development in coordination with economic and social development, expedite the convenience of financing, reduce costs in the real economy, raise resource allocation efficiency, and ensure that risk is controllable.

In addition, the National People's Congress approved the State Council Organization Reform Plan in March 2018. Under the plan, a restructuring of the financial administration was carried out, including the integration of the CBRC and the CIRC, which led to the new CBIRC with more comprehensive functions. At the same time, the functions of planning legislation and prudential policy making, originally residing with CBRC and CIRC, were transferred to the PBOC.

Traditionally, the functions of financial institution supervision and management were dispersed among the CBRC, CIRC, CSRC, and PBOC. In recent years, obstacles to the development of the domestic financial securities markets have been revealed by the expansion of shadow banking and Internet finance; in particular, the regulatory division of the separate bond markets has been noted as an obstacle. There is an urgent need for more fluid, developmentally comprehensive cooperation among market participants across the traditional industry to address market barriers and a rectification of imbalances with regard to enforcement. The financial supervisory control system under the initiative of the FSDC will use this new environment toward further integration of financial market administration.

7. One Belt, One Road Bond Issuances

The “One Belt, One Road” initiative, or the Belt and Road Initiative (BRI), is a global development strategy adopted by the Government of the PRC in 2013 that entails infrastructure development and investments in 152 countries and international organizations in Asia, Europe, and elsewhere. BRI-themed, foreign-currency-denominated bonds have been issued since 2015.

In May 2017, the first batch of a China Merchants Port Hong Kong MTN was issued in the Panda bond market, raising CNY2.5 billion and representing the first medium-term Panda bond in the CIBM for projects pursuant to the BRI.

In October 2017, a global provider of modern logistics facilities, Global Logistic Properties (via Iowa China Offshore Holdings [Hong Kong] Limited, GLP's PRC holding company) issued CNY1 billion of Panda bonds in the CIBM to finance construction of properties along BRI routes. GLP became the first international company to issue Panda bonds in both the CIBM and the exchange bond market.

¹¹³ State Council, Government of the PRC. 2017. *News Release*. 9 November. http://english.gov.cn/news/top_news/2017/11/08/content_281475936107760.htm.

In June 2016, Bank of China signed a memorandum of understanding on Panda bond issuance with Poland's Ministry of Finance. In August 2016, the Government of Poland subsequently issued CNY3 billion worth of Panda bonds with a tenor of 3 years.

With its inaugural CNY1.46 billion Panda bond in March 2018, the Philippines became the first ASEAN member to issue Panda bonds. Access to the issuance via Bond Connect resulted in foreign investors representing 87.7% of the allocation, the highest proportion of foreign investors for any Panda bond issuance to date.

8. Introduction of Bond Connect

On 16 May 2017, the PBOC and the Hong Kong Monetary Authority announced their approval for PRC and Hong Kong, China financial infrastructure institutions to collaborate in establishing mutual bond market access between the PRC and Hong Kong, China under a scheme known as Bond Connect.¹¹⁴

Bond Connect is an arrangement that will enable PRC-based and overseas investors to trade, settle, and hold bonds tradable in the China and Hong Kong bond markets through connections between PRC and Hong Kong, China financial infrastructure institutions. The actual connection was established between the CMU of the Hong Kong Monetary Authority with CCDC and SHCH, in the manner that CMU account holders are able to access the CIBM via the CMU by using their preferred electronic trading platforms, such as Bloomberg or TradeWeb, as a conduit to CFETS. For more information on the features of Bond Connect, please refer to Chapter IV.

Bond Connect has been implemented in phases. Trial operation of Northbound Trading commenced on 3 July 2017 as an initial phase so that, for example, overseas investors from Hong Kong, China and other economies and regions can invest in the CIBM through Bond Connect. This aims to provide overseas investors with a new and more convenient channel to invest in the CIBM in addition to existing channels such as the QFII, RQFII, and CIBM Direct schemes.

Bond Connect abides by the relevant laws and regulations of the bond markets of the two jurisdictions. Northbound Trading follows the current policy framework for overseas participation in the CIBM and, at the same time, respects international norms and practices. The scope of eligible investors and products under Northbound Trading are consistent with the scope specified in the relevant notices promulgated by the PBOC. Through cooperation and connections between the financial infrastructure of the two jurisdictions, overseas investors can more conveniently invest in the CIBM, allocate Chinese renminbi assets, and manage associated risks. There is no investment quota for Northbound Trading. A version of Bond Connect that incorporates Southbound Trading may be considered in the future.

9. Changes in the Qualified Foreign Institutional Investor and Renminbi Qualified Foreign Institutional Investor Schemes

Starting with its inception in 2002, the QFII market access concept resulted in an allocated investment quota of USD111.04 billion through the end of August 2019, before SAFE abolished the quota system in September 2019. In addition, 243 RQFII licenses had been issued through September 2019, amounting to an available quota of CNY1,990 billion, of which CNY691.6 billion had been utilized.

In the past few years, the QFII and RQFII schemes have undergone a significant liberalization in line with the broader efforts of policy bodies and regulatory authorities to liberalize the China bond and capital markets.

¹¹⁴ Information adapted from original press release referenced in NAFMII newsletter dated 19 May 2017.

In 2016, the limitations on QFII and RQFII to allocate funds to specific instruments and transaction types were removed; in June (RQFII) and September 2018 (QFII), the Government of the PRC announced that the caps and any remaining time limits for the repatriation of capital and interest had also been removed. On 10 September 2019, SAFE announced the abolition of the investment quotas for the QFII and RQFII schemes.

Please also see Chapter II.N for more detailed information on the QFII and RQFII concepts, as well as Chapter I.D for the individual development steps of the QFII and RQFII market access schemes in the context of overall bond market development.

10. China Banking and Insurance Regulatory Commission Issued Guidelines for Commercial Banks to Manage Collateral

In May 2017, CBRC (now CBIRC) issued the Guidelines for Commercial Banks to Manage Collateral (银监会发布《商业银行押品管理指引》). The guidelines, composed of seven chapters with 48 articles, emphasize that commercial banks shall abide by the principles of legitimacy, validity, prudence, and subordination; improve the organizational structure of collateral management; enhance risk management of key aspects such as classification and valuation of collateral, and the rate setting of mortgages or pledges, among others; and regulate such processes as collateral investigation and assessment, pledge or mortgage establishment and duration management, as well as return and disposal of collateral.¹¹⁵

The guidelines direct commercial banks to improve their collateral-related systems and rules, as well as the information systems in use, to define job responsibilities, and to regulate the collateral management processes. The guidelines raise clear requirements for the classification and valuation of collateral, concentration management, and stress tests, helping commercial banks strengthen their risk management in relation to raising, valuing, and managing collateral.

11. Launch of CIBM Direct

PBOC Public Notice No. 3, issued on 17 February 2016, paved the way for foreign central banks, foreign currency authorities, sovereign wealth funds, RMB clearing banks in Hong Kong, China and Macau, China, and any foreign institutional investor who was qualified as a QOII to access the CIBM directly to trade cash bonds and other transactions approved by the PBOC, without a ceiling investment amount or restrictions of fund transfer, under the so-called CIBM Direct concept. Please see Chapter I.D.4 for a more detailed description of the CIBM Direct concept.

In the CIBM, QFIIs and RQFIIs (see also Chapter III.N) have been considered and regulated as QOIIIs since then.

12. Broadening and Deepening of Panda Bond Issuances

In recent years, the China bond market has seen a significant broadening and deepening of the Panda bond issuance avenue, from initial issuances being made only by multilateral development organizations to present-day corporate and foreign sovereign bond issuances.

In March 2014, German carmaker Daimler AG became the first issuer of a corporate Panda bond in the CIBM. In September 2015, the PBOC eased restrictions on the use of proceeds from Panda bonds to be used within and outside the PRC, and on

¹¹⁵ Information adapted from NAFMII newsletter dated 12 May 2017.

8 September 2018, the PBOC and MOF jointly issued the Interim Measures for Administration of Bond Issuance by Overseas Institutions in the National Inter-Bank Bond Market, which introduced the ability to issue Panda bonds in the CIBM via a public offering or a private placement to DIIs or SIIIs, and further defined information disclosure, issuance registration, custody, settlement, as well as CNY-denominated account opening, fund exchange, and investor protection. In 2016, Poland became the first European country to issue Panda bonds in the CIBM, while Hungary issued the first sovereign Panda bond in 2017 for which the subscription and allocation was accessible through Bond Connect.

In January 2019, NAFMII issued the Guidelines on Debt Financing Instruments of Overseas Non-Financial Enterprises (for Trial Implementation), which further clarified details for Panda bond issuance registration and information disclosure by nonresident corporate issuers. Both the interim measures and the NAFMII Guidelines contain concessions for nonresident issuers on the use of English in issuance documentation and disclosure information.

For further information on Panda bonds as the issuance method for nonresident issuers, please see Chapter III.E. In addition, Chapter I.D.5 outlines some of the steps mentioned above in the context of the increased opening of the China bond market overall.

13. First Special-Drawing-Rights-Denominated Bonds in the Inter-Bank Bond Market

In September 2016, the World Bank successfully issued its first tranche of SDR-denominated bonds in the CIBM. The first issuance amounted to SDR500 million with a term of 3 years. The bonds will be payable in Chinese renminbi. Over 50 domestic institutional investors—including banks, securities firms, and insurance companies—as well as foreign monetary authorities and international institutions submitted bids for the bonds, with a bid-to-cover ratio of 2.47. In October 2016, Standard Chartered Bank (Hong Kong) Limited issued SDR100 million worth of 1-year bonds, the first commercial bank to sell SDR-denominated bonds.

The SDR-denominated bond added a new product category to the China bond market, which may be used to diversify the portfolios of domestic and international investors. The issuance also helped broaden the use and acceptance of SDR.

B. Future Direction

1. Further Opening of the People's Republic of China Capital Market (Bond Market)

On 11 April 2018, at the Boao (博鳌) Forum for Asia Annual Conference, President Xi Jinping announced that the PRC would significantly broaden market access, and PBOC Governor Yi Gang announced specific measures and a time frame for the further opening of the financial industry.

The PRC is expected to continue with capital account convertibility reform and deepen the reform of the Chinese renminbi exchange rate formation mechanism. Market participants are expected to be more involved and active in the Chinese renminbi exchange market and the CNY-denominated bond market.

Financial institutions, especially commercial banks, will need to provide better services in Chinese renminbi clearing and settlement, investment and financing, trading, and asset management to facilitate the use of Chinese renminbi in payment, settlement,

investment, and as a reserve currency so that the breadth and depth of the Chinese renminbi's internationalization will be enhanced.

The release of the associated PBOC notice improved the institutional arrangements for overseas institutions to issue bonds in the CIBM, aligned the domestic institutional rules with international standards, and helped further the internationalization of the China bond market.

Furthermore, on 30 August 2018, the State Committee of the State Council proposed a 3-year exemption from CIT and VAT on interest income derived by foreign investors from their investment in the China bond market. The MOF and the SAT are expected to issue detailed regulations in due course.

In recognition of the importance of eliminating potential anxiety factors over the medium to long term, it is expected that more permanent tax exemption measures will be put in place to support the development of a stable and sustainable domestic bond market.

2. Consideration of a China Inter-Bank Bond Market-Wide Trustee Concept

To further strengthen the mechanisms for investor protection in the CIBM, both the PBOC and NAFMII had been considering the implementation of a trustee-like concept for the CIBM, similar to the exchange bond market, which would allow for the consolidation of a number of roles presently performed by different entities in the CIBM. While NAFMII introduced a formal bond trustee concept in December 2019 (effective July 2020) for debt financing instruments (to be) registered with NAFMII, the PBOC may consider implementing a similar concept for all issuances in the CIBM, potentially making allowances for certain types of issuances (e.g., private placements), as is common in other regional markets.

Please see Chapter III.S for more information on the bond trustee concept introduced by NAFMII.

3. ASEAN+3 Multi-Currency Bond Issuance Framework

The introduction of AMBIF in regional markets in 2015 signaled another potential opportunity for bond issuance activities in markets other than those of the framework's original adopters, which were Hong Kong, China; Japan; Malaysia; the Philippines; Singapore; and Thailand.

Potential issuers have identified the PRC as one of the markets of particular interest, largely due to the size and attractiveness of such a large market but also to support the decentralized funding of domestic business operations in the PRC.

Aimed particularly at the issuance of debt financing instruments and corporate bonds to professional investors in participating markets, AMBIF encourages domestic and regional issuers to take advantage of streamlined issuance approval processes across the region. For additional information on AMBIF, kindly refer to the ADB website.¹¹⁶

The key advantage of AMBIF for the PRC lies in the ability of regional issuers (including those from the PRC) to tap multiple markets in addition to their domestic bond market while using the same or similar key disclosure documentation and comparable approval processes. This offers an alternative for corporate issuers to

¹¹⁶ See ADB. 2015. *Implementation of the ASEAN+3 Multi-Currency Bond Issuance Framework: ASEAN+3 Bond Market Forum Sub-Forum 1 Phase 3 Report*. <https://www.adb.org/publications/implementation-ambif-asean3-bond-market-forum-sf1-p3>.

issue bonds across markets instead of (or in addition to) relying on other forms of funding.

AMBIF prescribes, among other elements, the presence of a professional investors only market segment and the use of documentation in English. The CIBM private placement scheme already contains many of the features necessary for the issuance of AMBIF bonds in the near future.

Notably, the use of issuance documentation and disclosure information in English, possibly in addition to documentation in Chinese, is permitted in principle in the most recent Panda bond regulations (see also Chapter III.G). It has become a subject for adoption in market practice and is under further consideration by the policy bodies and regulatory authorities in the PRC.