



# The Development of China's Financial Markets

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29/03/2019





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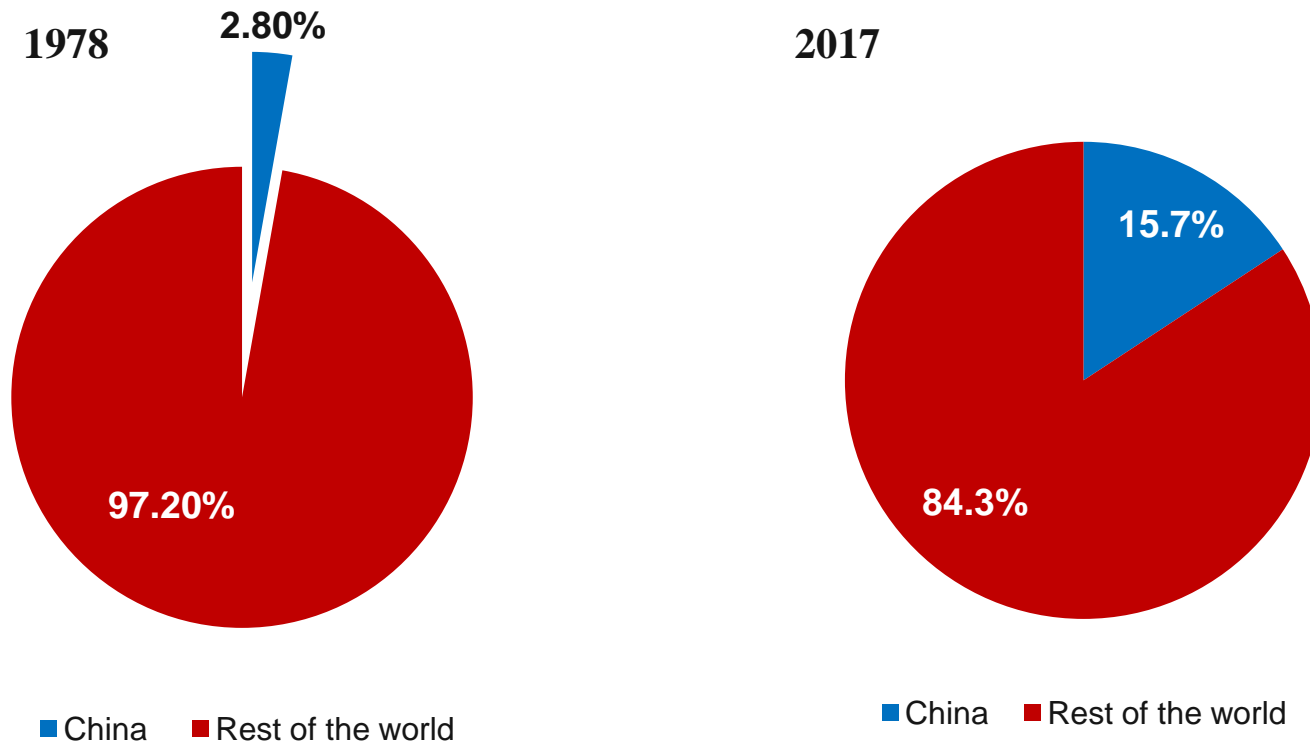
**China's Economy Overview**

02

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## □ China's GDP as a Share of the World 1978 VS 2017



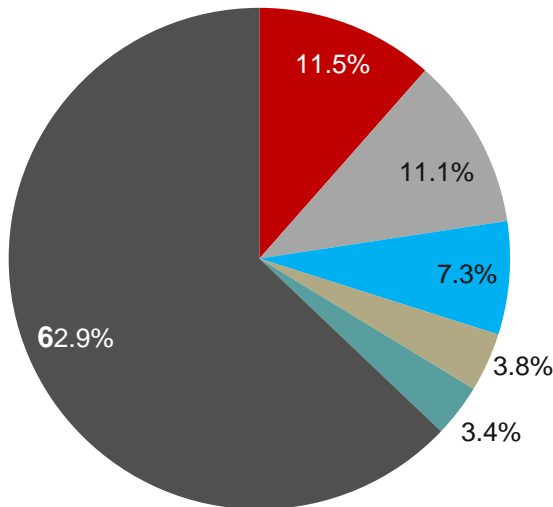
Source: World Bank, NBS



## China is the World's Leading Trading Nation

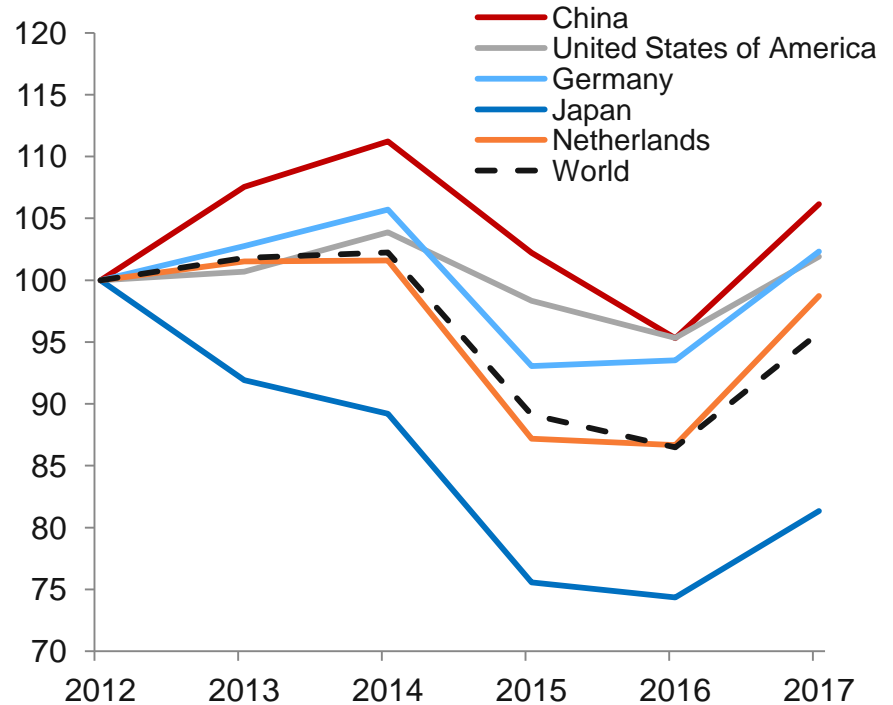
**China No.1 Trading Nation in the World**  
(export and import as a share of global total, %)

■ China    ■ United States    ■ Germany  
■ Japan    ■ Netherlands    ■ Other



Source: WTO-UNCTAD, BOC

**China is the Main Driving Force for Global Trade**  
(Annual Growth Rate Index, 2012=100)



Source: WTO-UNCTAD, BOC



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## Foreign Investment Policy Evolution: Organic and Meeting Market Demand

PBOC signing currency swap agreement with monetary authorities or foreign central banks

Three types of eligible foreign institutions allowed to trade in the interbank bond market

- RQFII allowed to invest in CIBM
- Some overseas insurance companies allowed to participate in CIBM

- Overseas clearing banks and participant banks allowed to do repo in CIBM
- PBOC released notification on CIBM investment, allowing foreign Central Banks, Sovereign Funds and Multinational Financial Organizations to invest in CIBM directly
- Foreign sovereign investors allowed to access China Interbank FX market

SAFE allowed overseas institutional investors to trade FX derivatives to hedge their FX exposure based on onshore bond positions through qualified domestic agent bank

2008

2009

2010

2011

2012

2013

2014

2015

2016

2017

Regulation on Cross-Border RMB Trade Settlement Pilot Scheme rolled out

RQFII system introduced

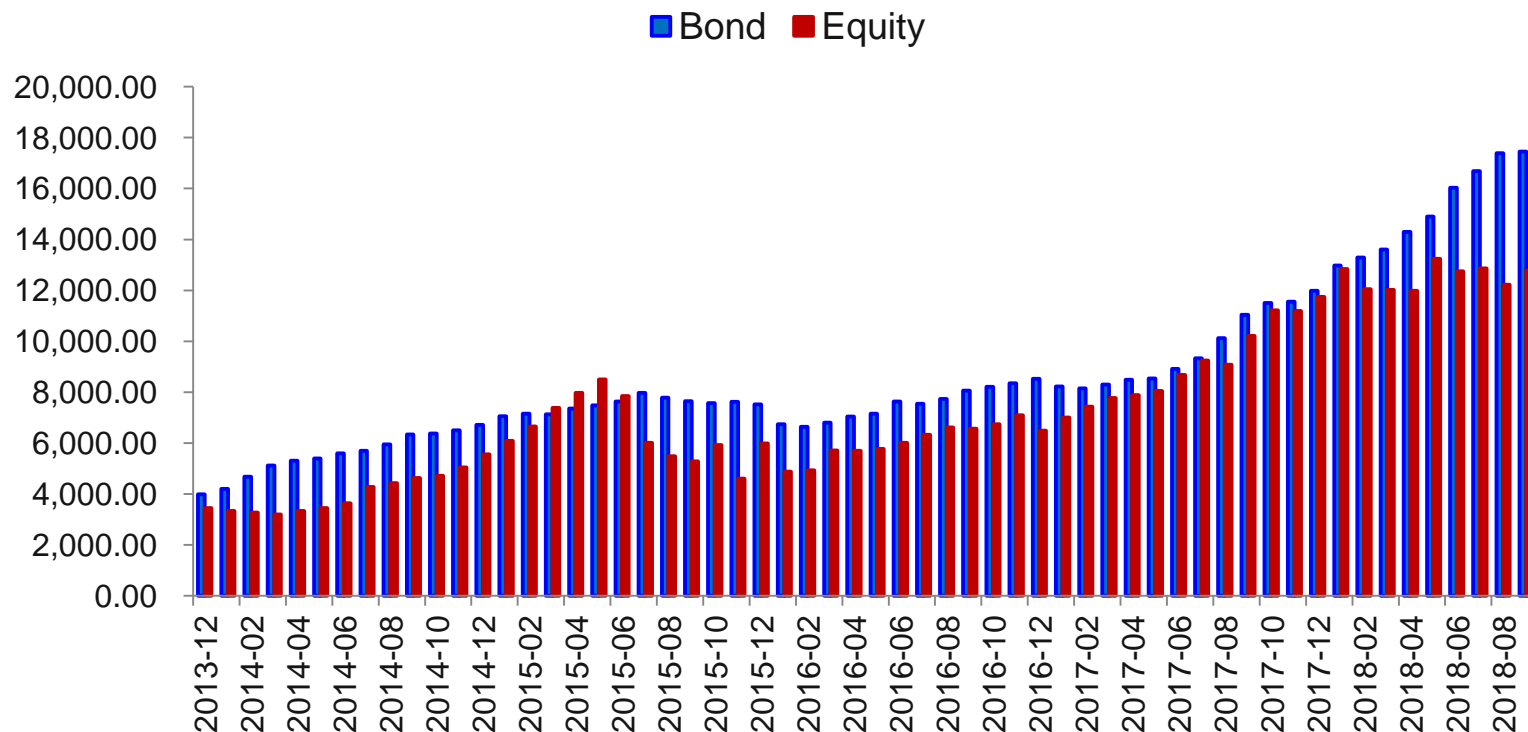
QFIIs allowed to invest in CIBM

PBOC announced to open CIBM to foreign institutional investors, removing bond investment quotas on qualified foreign institutional investors and simplifying market access

Bond Connect Pilot Program

## □ The Opening-up of China's Financial Market

**Domestic Financial Assets Held by Overseas Entities**  
(100 Million Yuan)



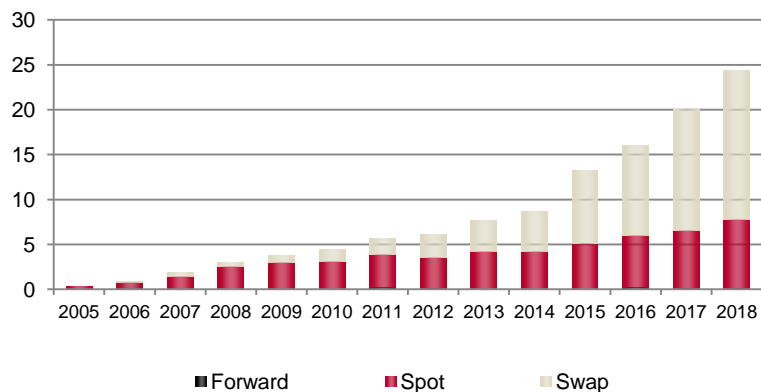
Source: Wind, BOC

## Overview of Onshore FX Market

### Growing Market Depth

- Intraday trading band: within 2% around central parity rate
- In 2018, daily trading volume averages around USD 100 Bio in the inter-bank FX market, up by 20% yoy. The average yearly growth rate in trading volume is 30% since RMB depeg from dollar in 2005.

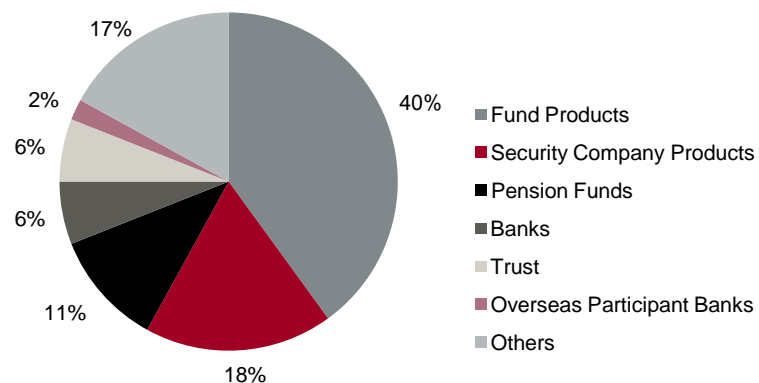
Trading Volume



Source: Bank of China, CFETS

### Increasing Market Accessibility

- More diversified market participants including: overseas institutional investors, foreign central banks, security companies and mutual funds etc., while commercial banks that deal on back of corporate & individual flows still dominate market.
- Increasing overseas participation expected with further financial sector opening-up



### Liquidity deepens & Products diversified

Trading Volume	Spot	Swap	Option
<ul style="list-style-type: none"> <li>✓ Stable growth and huge potential</li> <li>✓ 2018 Market Volume: Spot 7.7 trillion USD, Derivatives 17.3 trillion USD</li> </ul>	<ul style="list-style-type: none"> <li>✓ Daily Trading Volume: 25–35 Billion USD</li> <li>✓ Sufficient Liquidity</li> <li>✓ 23 direct trading pairs against RMB (another 4 spot-only regional pairs)</li> </ul>	<ul style="list-style-type: none"> <li>✓ Daily Trading Volume: 50–70 Billion USD</li> <li>✓ Tenors up to 10 years; great liquidity up to 2 year, decreasing into longer end</li> <li>✓ <b>Most used hedging tools for oversea investors</b></li> </ul>	<ul style="list-style-type: none"> <li>✓ European vanilla products</li> <li>✓ Liquidity fair up to 3 years</li> <li>✓ Less sophisticated than the CNH market</li> </ul>





## □ RMB FX: on the Way to Clean-floating Mechanism

- Minimal routine FX intervention and more market-determine exchange rate.
- Fixing and market price is demonstrating convergence.
- Deviation between onshore and offshore RMB FX is tightened.
- Enhanced flexibility, characterizing more bi-directional movement.

Fixing /USDCNY Spot /USDCNH Spot since 2014





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## ❑ **RMB, Icon of Bigger China**

- Further opening up under Capital account
- Comparatively independent FX rate movement
- Lower correlation with current account balance
- More asset-like characters: sentiment vs fundamentals
- Yield spread accounts more as RMB FX demand factor
- Increased weight of the reserve asset allocation by global central banks

## ❑ **RMB Outlook**

- Reform trend in future FX Market Scheme
  - Further easy access to RMB FX trading
  - Multiple layers of onshore FX markets are forming
  - Diversified types of participants to be introduced
  - More financial facilities are being built to match international markets

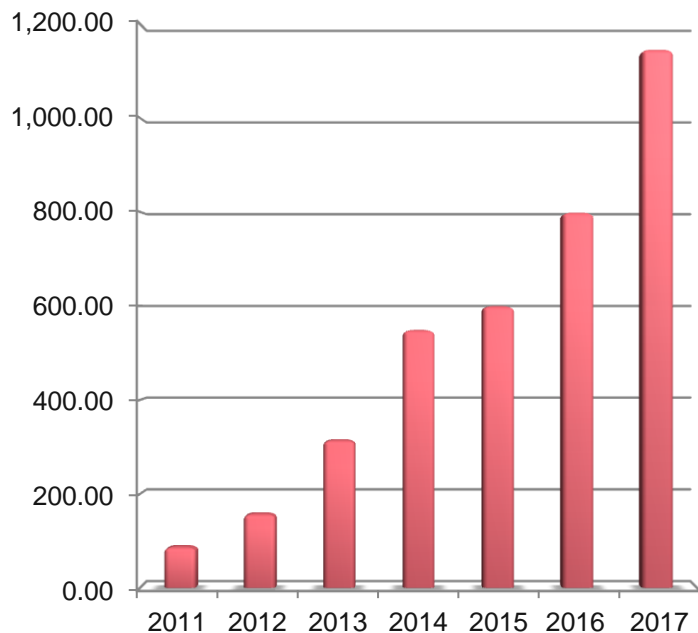


## □ Glance on China Interbank Bond Market

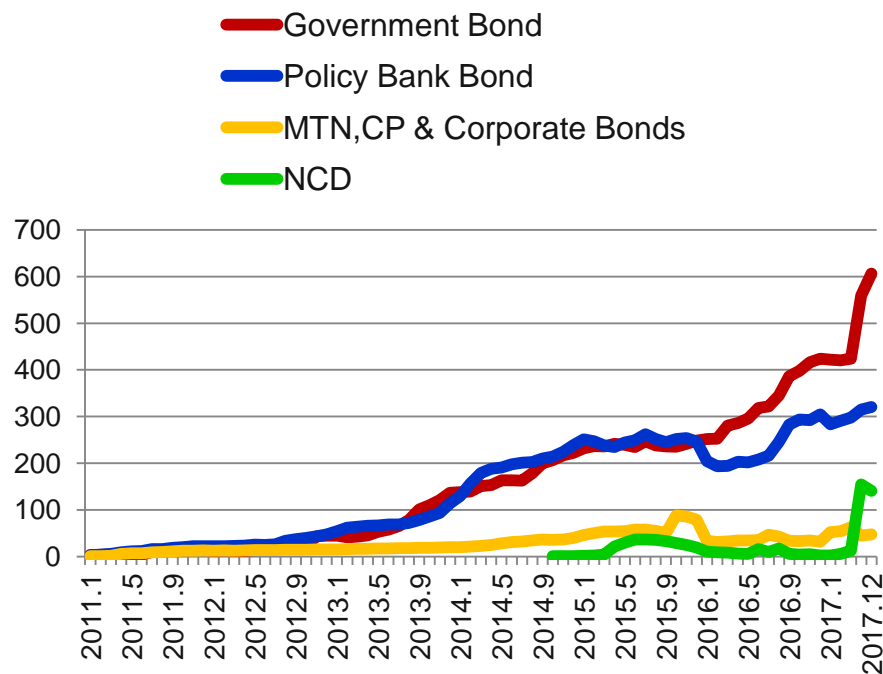
- CIBM is the world's 3<sup>rd</sup> largest OTC fixed income market, with a significantly large issuer base, strong liquidity and instrument diversification.
- CIBM has an established segment of Fixed-income-based derivatives.
- CIBM Investors vs. QFIIs/RQFIIs
  - CIBM is the primary entrance point for overseas investors who have interest purely in fixed income instruments, while QFIIs/RQFIIs have extra access to exchange market, thus can trade equities, along with warrants, ETSs, mutual funds, stock index futures and other instruments approved by CSRC.
- Number of Overseas Investors
  - Until end of 2018, more than **1,200** overseas investors entered the CIBM market either with agency model or Bond Connect.

## ❑ Overseas Investors via CIBM

Face Value of Bonds Held by Overseas Institutions (Billion Yuan)



Major Bond Holdings of Overseas Institutions (Billion Yuan)

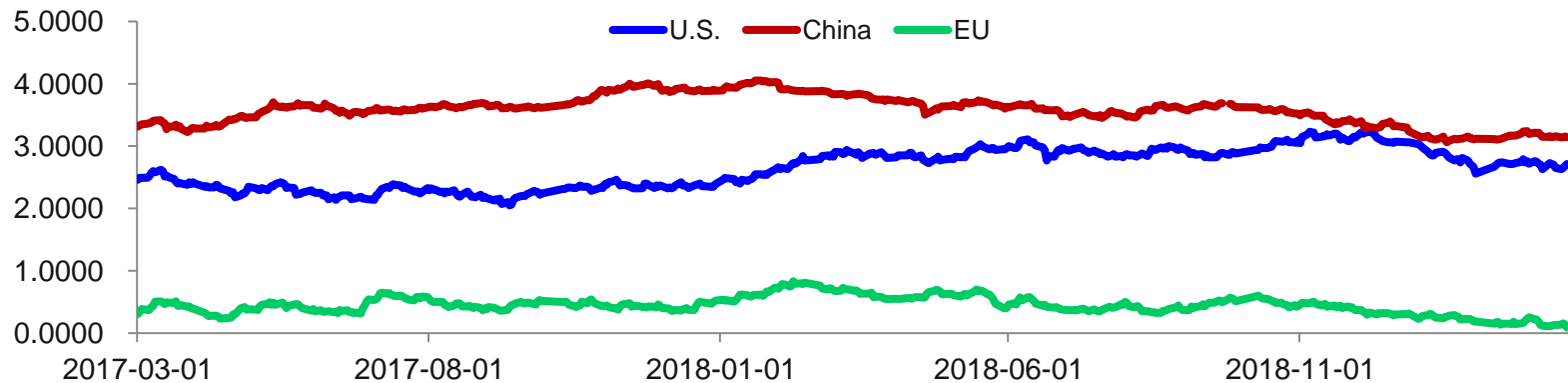


Source: Wind, BOC



## □ China's Outperformance

10Y Government Bond Yield



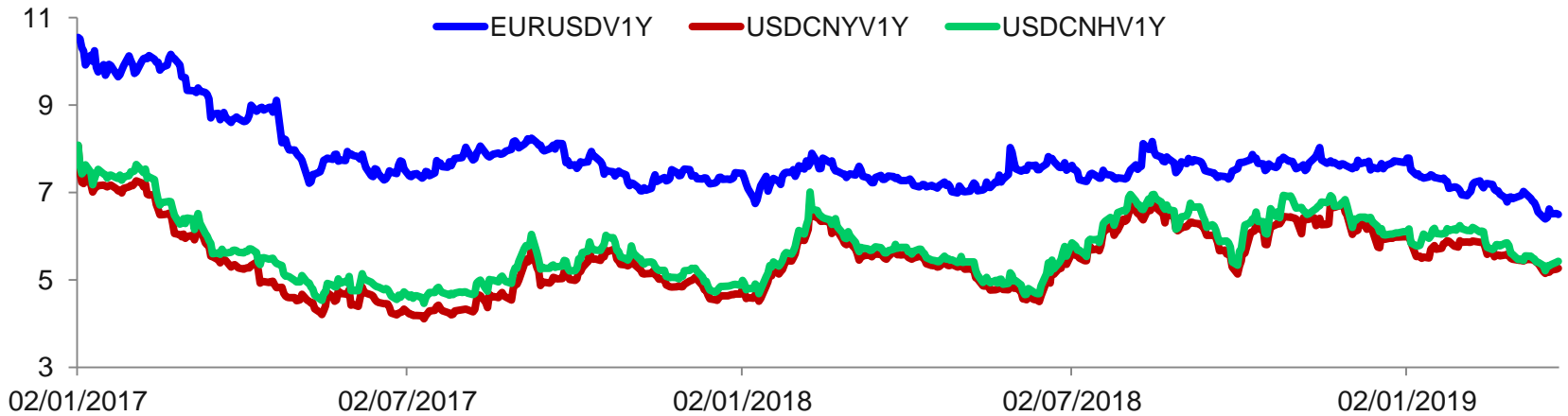
Source: BOC, WIND

## □ Future Growth of China's Bond Market

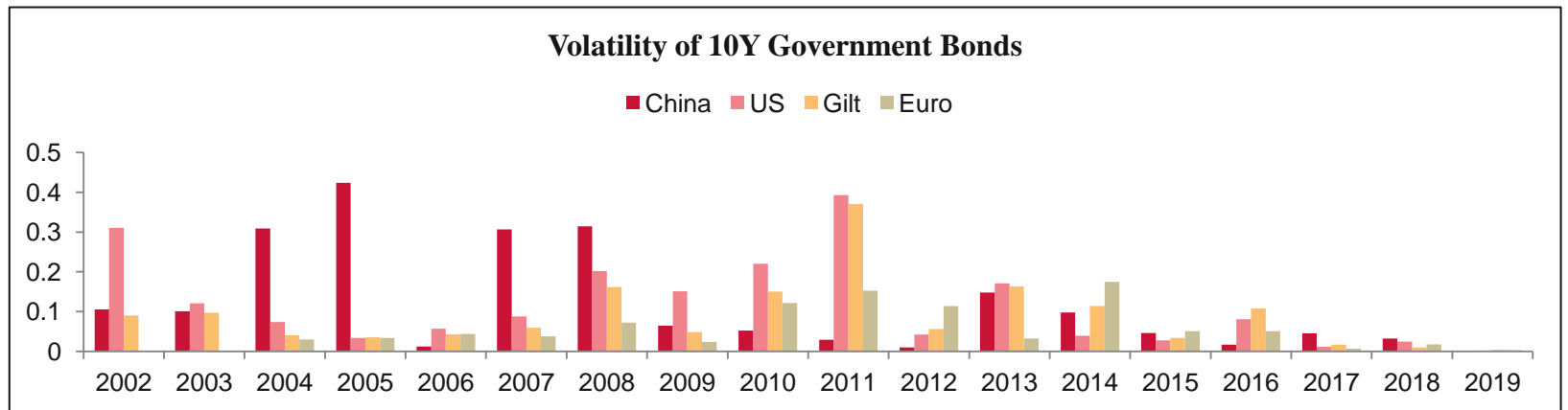
- The upcoming inclusion of China bonds into **Bloomberg Barclays Global Aggregate Index** in April and **JPM EM Bond Index** expected
- Yuan-dominated bonds will be the fourth largest currency component following the US dollar, euro and Japanese yen



## □ Less Volatility of China's Financial Market



Source: BOC, Bloomberg



Source: BOC, Wind; Volatility calculated as the annual variance of yield.



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## □ Key Messages from the PBOC

- Maintaining financial stability
  - Further create a fair and impartial market environment
  - Improve the transparency of market supervision
  - Keep the RMB exchange rate basically stable at reasonable and balanced level.
- Maintaining opening-up
  - Further relax controls over market access
  - Shortened the negative list for foreign investment
  - Strengthen efforts to protect foreign investors' lawful rights and interests.
- China Economy Outlook
  - Keep 2019 growth within reasonable range: 6-6.5%.

Thank you



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