

Wiley Finance Series



# Dim Sum

# Bonds

*The Offshore Renminbi  
(RMB)-Denominated Bonds*



HUNG-GAY FUNG  
GLENN KO  
JOT YAU

WILEY



## Praise for *Dim Sum Bonds*

“A good 3-D view on the Dim Sum bond market—drilling down all the way from the macro factors that gave rise to this universe to the micro aspects of issuing details, while at the same time, providing a round-table perspective from the government, the issuers, the investors, and the investment banks.”

—Edwin Chan, Managing Director, Head of Asian Credit Research, UBS, and No. 1 ranked analyst for Asian G3 bonds by *The Asset* and *FinanceAsia*

“This book is a very useful reference for those international investors who consider investing in the offshore RMB bond market for either an appreciation or a higher carry in the RMB. It is also a convenient guide to the dim sum bond market. I highly recommend treasurers of companies who haven’t tapped this important funding source read this book.”

—Jingxin Deng, Director, Lead Portfolio Manager of Global Credit Investment, China Investment Corporation, Hong Kong

“The dim sum bond market is not just another up-and-coming EM bond market. With the internationalization of the RMB and China being the second largest economy in the world, the dim sum bond market is quickly attracting investors and issuers from around the world. The growth (and the destiny) of the dim sum bond market, I believe, will be similar to the development of the Yankee bond market over the past 20 years. This timely and well-researched reference book written by both market practitioner and academic researchers is a must-read.”

—Thomas Kwan, Head of Fixed Income, Harvest Global Investments Limited, Hong Kong

“A very useful and insightful reference to anyone who wants to comprehend the profound implication of the development of the dim sum bond market and what it means to the global capital market in the future. I believe market participants and researchers will benefit from the authors’ great insights, while investors will gain from better appreciation of the risks, opportunities, and the significance of this asset class.”

—Arthur Lau, Managing Director, Head of Fixed Income Asia ex Japan and Co-Portfolio Manager, Emerging Markets, PineBridge Investments Asia Ltd., Hong Kong, and voted the most astute bond investor in Hong Kong by *The Asset* in 2007 and 2008

“This book is essential reading for all existing and intended RMB debt market participants in Hong Kong, the biggest RMB off-shore centre.”

—Philip Li, Managing Director, China Chengxin (Asia Pacific)  
Credit Ratings Company Limited, and former chairman  
of the Hong Kong Capital Markets Association

“This book will help fill a gap in knowledge about the rapidly growing off-shore Chinese Renminbi market and specifically the ‘dim sum’ bond market in Hong Kong. This timely book will help investors, bankers, regulators, and academics better understand China’s currency as it becomes more international and as companies look to raise funds in RMB via Hong Kong and other offshore financial centers.”

—George Long, CFA, Chairman, and Chief Investment Officer, LIM  
Advisors Limited, Hong Kong, the founding president of the  
Hong Kong Society of Financial Analysts, and the founding  
chairman of the Hong Kong Chapter of the Alternative  
Investment Management Association (AIMA)

“An excellent investment handbook on dim sum bonds for practitioners. The authors have great insights on the structure and evolution of the off-shore RMB bond market.”

—Richard Mak, CFA, Head of Advisory Services—Asia, Pictet & Cie,  
and former president of the Hong Kong Society of Financial Analysts

“Kudos to the authors of this book for providing a very comprehensive source of information about the development of the dim sum bond market. As buy-side investment advisors for private banking clients in Asia, we see the trend of the growing importance of the RMB in asset allocation. The burgeoning demand for offshore RMB-denominated investments is a major driving force behind the dim sum bond market. I strongly recommend this book to anyone who wants to understand the dim sum bond market.”

—Maggie Tsui, Managing Director, Deputy Head of Investment Services,  
Asia, BNP Paribas Wealth Management, Hong Kong

“The rise of China has brought its capital markets into the global limelight. The internationalization and convertibility of its currency, the renminbi, are imminent. This book provides a very timely and comprehensive study of the dim sum bond market from both a historical and risk-reward perspectives. It also provides insights into how this asset class would continue to grow and the challenges it will face along the way. Fung, Ko, and Yau’s book



should be made a compulsory reading for any investor who has an interest in the renminbi and China's offshore bond market."

—Michael Yong-Haron, CFA, Managing Director, Credit Suisse Private Banking Division, Greater China

"In *Dim Sum Bonds*, Fung, Ko, and Yau provide a fascinating account of the dim sum bond market from relative obscurity a few years ago to a leading position in the growing offshore RMB bond market. The book presents cases of the landmark dim sum bond issues, which illustrates clearly the issuers' perspectives. This book is a must-read for anybody who wants to know this market in Hong Kong."

—Jimin Guo, Ph.D., CFA, Executive Director, China Galaxy Securities, Beijing

"Fung, Ko, and Yau have done a superb job in sizing up the development of the offshore RMB bond market to date and laying out the opportunities and risks ahead. The book is an indispensable reference tool for anyone investing or contemplating investing in this budding market."

—David Lai, CFA, Investment Director, Fixed Income, Eastspring Investments (Singapore) Limited

"This book provides an easy-to-follow road map and delivers crystal clear details on every aspect of the dim sum bond market. It is a must-read for both seasoned professionals and novices alike."

—Lee Kerk Phua, CFA, Chief Strategist, Phillip Mutual Malaysia

"*Dim Sum Bonds* offers insight into one of the more complex aspects of China's efforts to become a major player in global financial markets. It explains in detail the internationalization of the RMB and China's efforts to create an alternative global reserve currency. This book is a must-read for academics and practitioners interested in understanding the remarkable developments now taking place in China's capital markets."

—Keith Ferguson, Chief Investment Officer, University of Washington, Seattle

"This book is an outstanding achievement that brings the reader into the world of dim sum bonds—the offshore renminbi bond market. The combined practitioner and academic experience of the authors is well translated into this book that gives not only a detailed overview of the dim sum bond

market, but also a thorough quantitative analysis of the bond characteristics in this fledgling market. A must-read!”

—Wai Lee, Ph.D., Chief Investment Officer and Director of Research, Neuberger Berman, New York, and author of *Theory and Methodology of Tactical Asset Allocation*

“Fung, Ko, and Yau have authored a timely reference that sheds light on a nascent yet soon to be vital financial instrument in the global marketplace. The authors address the development of the dim sum bond market and its role in supporting the Renminbi as a global reserve currency in a way that is both entertaining and informative, both in breadth and depth. Readers, whether fixed income and equity professionals or investors, will find this book a useful desk resource today and even more so as the market begins to mature.”

—Derrick Tzau, CFA, International Research Analyst, Rainier Investment Management, Seattle/New York

# **Dim Sum Bonds**

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# Dim Sum Bonds

*The Offshore Renminbi (RMB)-  
Denominated Bonds*

HUNG-GAY FUNG  
GLENN KO  
JOT YAU

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*To my wife, Linda; my daughter, Anna;  
and my brothers and sister*

—Hung-Gay Fung

*To my family*

—Glenn Ko

*To Marie*

—Jot Yau





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# Preface

**A**s you are reading this preface, we know that the title of this book, *Dim Sum Bonds*, has done its job piquing your curiosity. We hope you will find this book interesting and “dim sum” meals satisfying.

Whenever we mentioned to our friends and colleagues that we were working on a book on “dim sum bonds,” all of them<sup>1</sup> were in awe with no exception. Many of our friends, colleagues, and professional acquaintances thought that we had reinvented ourselves, switching our lifelong careers in finance/investment research and management to culinary art. A friend actually said to one of us,<sup>2</sup> “I didn’t know that you were a chef!” We are, of course, more than happy to explain, elucidate, and explicate what dim sum bonds are and will be. We wouldn’t mind having this type of 3 “E’s” conversations over “dim sum” luncheons for years to come.

“Dim sum,” in Cantonese<sup>3</sup> refers to a variety of tiny, bite-sized, steamed food that is usually served for breakfast or lunch. It is supposed to be a small, hot meal that goes with Chinese tea. A traditional dim sum meal would have “Ha Gau” (shrimp dumpling) and “Siu Mai” (pork and mushroom dumpling), whereas fusion dim sum would have food crossing over from different Chinese regions as well as Western cuisines.

The term *dim sum bonds* is used to refer to the offshore renminbi (RMB)-denominated bonds issued in Hong Kong, where “dim sum” is served in most restaurants.<sup>4</sup> Since the dim sum bond market made its debut in 2007, China has been contemplating establishing offshore RMB bond markets at other locations such as Taiwan, Singapore, London, and Paris. In this book, we focus on the dim sum bond market, the offshore RMB market in

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<sup>1</sup> More specifically, those living outside Asia.

<sup>2</sup> More specifically, Jot Yau.

<sup>3</sup> Cantonese refers to the language that originated in the vicinity of Canton (i.e., Guangzhou), the capital city of the province of Guangdong in southern China. It also refers to the people or things that come from that area.

<sup>4</sup> For the credit of the use of the term *dim sum bonds* to refer to the offshore RMB-denominated bonds issued in Hong Kong, see Robert Minikin and Kelvin Lau, *The Offshore Renminbi: The Rise of the Chinese Currency and Its Global Future*. John Wiley & Sons Singapore Pte. Ltd., 2013, p. xv.

Hong Kong, emphasizing the experience and perspective of major market participants, although we also discuss how other offshore RMB bond markets are in the making in light of the development and growth in the dim sum bond market. This approach is like introducing readers to the traditional dim sum such as “Ha Gau” and “Siu Mai,” while ordering some fusion dim sum for different flavors and tastes.

The purpose of this book is to provide a panoramic view of the Hong Kong offshore RMB-denominated bond market that has played a pivotal role in China’s grand scheme of making the RMB a global reserve currency by providing an investment option to holders of offshore RMB as part of the strategy for internationalizing the RMB. As China does not allow free flow of funds in and out of the mainland, its domestic financial market is basically closed to foreign investors. Since many companies issuing offshore RMB (dim sum) bonds have operations in mainland China, investing in these dim sum bonds offers investors an opportunity to participate in the upside of the Chinese economy.

We discuss and analyze the dim sum bond market from the vantage points of issuers, investors, investment banks, and the Chinese government. We hope our readers appreciate the dynamics among all market participants affecting the growth, opportunities, and challenges in this nascent market. The dim sum bond market in Hong Kong has grown rapidly over the past few years. Given limited investment options for the offshore RMB deposits and expectations of RMB appreciation, the dim sum bond market was more of a seller’s or issuer’s market until more recently. Issuers would thus be able to obtain lower-cost funding through dim sum bond issues, whereas investors were willing to buy dim sum bonds for lower yields.

Now, the dim sum bond market is maturing. We outline changes that have taken place thus far in the dim sum bond market. For example, the more active involvement of institutional investors, such as the long-only funds and hedge funds, has made the dim sum bond market become more investor friendly. Also, the yields of dim sum bonds are now more reflective of issuers’ credit quality, while terms and conditions such as covenants and the requirement of credit ratings are converging toward those of the Asian U.S. dollar bonds.

Moreover, we explain the intricacies in the primary dim sum bond issue origination process and contrast the main difference between them with those of the Asian U.S. dollar bond issues, which lies in the premarketing efforts due to differing issuer and investor profiles.

Overall, we believe the prospects of the dim sum bond market are promising despite challenges ahead. We expect the RMB will become an increasingly accepted currency worldwide, albeit the path it takes in the course of RMB internationalization will have obstacles. Worldwide circulation of the

RMB will support a sustainable growth of the global offshore RMB bond markets, including those to be developed over the long term, although the immediate future of the Hong Kong's nascent dim sum bond market depends very much on the Chinese and world economy. Changes in China's policy could present significant challenges to Hong Kong's dim sum bond market. The recently announced policy of the Chinese government authorizing RMB clearing banks in Taiwan and Singapore and thereby giving birth to offshore RMB bond markets in both countries is an example. Likewise, expansion of the Renminbi Qualified Foreign Institutional Investor (RQFII) program beyond Hong Kong will pose a threat to the dim sum bond market, although the program itself encourages international investors to hold more RMB, a positive toward the RMB internationalization efforts. Nevertheless, we believe the growth of the dim sum bond market in Hong Kong will benefit from the burgeoning offshore RMB pools around the world (e.g., Taiwan, Singapore, London, Paris, and New York), although dim sum bonds will account for a lower share of the overall offshore RMB pool.

All told, the dim sum bond market deserves attention from retail and institutional investors, issuers from different countries and industries, and investment bankers, as well as government regulators and policymakers. Practitioners, such as financial advisers, wealth and asset managers, and bond and currency traders, may find the dim sum bond market offers global investors a potentially viable asset class for portfolio diversification.

## **ORGANIZATION OF THIS BOOK**

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As mentioned, we present the dim sum bond market from the perspective of four major players in the market: the Chinese government, issuers, investors, and investment banks/bookrunners. From the Chinese central government's perspective, the development of the dim sum bond market is part of a grand scheme aiming at making the RMB a global reserve currency. It is part of the national multipronged strategy in internationalizing the RMB, controlling capital flows into China so as to provide price stability and harness inflation in mainland China, as well as developing a funding channel for tapping foreign capital. The Chinese government will thus continue to support the growth of the dim sum bond market.

From the issuers' perspective, Chinese corporations consider the dim sum bond market as an alternative to the Asian U.S. dollar (USD) bond market for lower-cost and shorter-tenor funding. The dim sum bonds are typically shorter in maturity (three years vs. five years-plus for Asian USD bonds). Many of the earlier dim sum bonds are unrated and without USD bond covenants. As such, issuers turned to the dim sum bond market for

lower-cost funding with less demanding requirements on credits and covenants. Nonetheless, we note that terms and conditions of dim sum bonds are converging with those of the Asian USD bonds given the increasing participation of institutional investors. The rapidly growing of the dim sum bond market was also under the backdrop that the onshore credit environment was tightening as the Chinese government tried to rein in credit growth, issuers had resorted to the offshore bond markets for funding needs. In addition, for private corporations, the dim sum bond market provides funding, which they cannot easily obtain onshore in the CNY market. Corporations can also obtain goodwill with the Chinese government by supporting the activities in this offshore market that help China to achieve its goal of internationalizing the RMB. Finally, corporations raising capital in the capital markets may gain publicity.

From the investors' perspective, dim sum bonds provide risk-averse investors investment options, as well as exposure to take advantage of the RMB appreciation, if any. Investors can obtain yield pickup over CNH deposits through investing in dim sum bonds. Investors now ask for benchmark RegS deal size, greater variety in terms of credits and tenor, ratings, and stricter covenants, closer to those of Asian USD bonds.

From the investment banks/bookrunners' perspective, the dim sum bond market represents new business opportunities from issuers in China for bond origination as well as for sales and trading. More business opportunities in dim sum bonds will probably come from potential issuers who are not yet ready for Asian USD bond issues with regard to their smaller operating scales, credit profile, and credit ratings. While the size of the dim sum bond issue, on average, is generally smaller, the fee income from bond origination and trading could be less attractive as compared with those of Asian USD bonds since fee income is tied to bond issue size. The smaller issue size also implies thin trading liquidity. Nevertheless, the size and potential growth of the dim sum bond market could be tremendous. Furthermore, investment banks can establish a relationship with potential dim sum bond issuers as they may eventually become repeat customers for future investment banking business.

To present the perspectives of the players in the dim sum bond market, we have separate chapters focusing on the characteristics of dim sum bonds and the dim sum bond market (Chapter 2), investors' investment objectives and the performance of dim sum bonds (Chapter 3), motivations of issuers (Chapter 4), and the investment banks/bookrunners' role in the dim sum bond issuing process (Chapter 5). We present cases of landmark issues by type of issuer (Chapter 6): mainland Chinese financial institutions (e.g., Chinese Development Bank), the Chinese central government (e.g., Ministry of Finance), supranational agencies (e.g., Asian Development

Bank), China-incorporated foreign banks (the Bank of East Asia [China] Limited), and Chinese corporations incorporated outside the mainland China and listed in Hong Kong (e.g., Sinotruk [Hong Kong] Limited), and foreign corporations (e.g., McDonald's Corporation). We also present two cases of special credit enhancement structures (Beijing Capital Land Ltd. and Gemdale Corporation). We discuss the salient features of each landmark issue to highlight the evolving market development. We also present the benchmark issues for 10-, 15-, and 20-year bonds. We conclude with Chapter 7, in which we also provide an outlook of the future development of the dim sum bond market.

The source of data used in the analysis is Bloomberg unless stated otherwise. The time period for the analysis we use throughout the book is July 1, 2007, to December 31, 2012, referred to as 2007–2012 for brevity. We sincerely hope that this book becomes a valuable resource for the investment community, corporations, sovereign and sub-sovereign entities, supra-national agencies, regulators, policymakers, and academics. Any errors or omissions are ours.

We hope you enjoy reading this book as much as we enjoyed writing it.  
Bon appétit!

Hung-Gay Fung  
Glenn Ko  
Jot Yau