熊猫债市场发展与国际发行人发行动因

The Panda Bond Market and Perspectives of Foreign Issuers

中国银行间市场交易商协会（NAFMII）
-国际资本市场协会（ICMA）联合工作组

第八次中英经济财金对话成果

ICMA–NAFMII Working Group
8th UK–China Economic and Financial Dialogue

2017年10月出版
Published in October 2017

The Panda Bond Market and Perspectives of Foreign Issuers

ICMA-NAFMII Working Group

8th UK-China Economic and Financial Dialogue

EDITORIAL COMMITTEE

ICMA Special Acknowledgements:

Allen &Overy, Ashurst, Bank of China (London), Deutsche Bank, Goldman Sachs, HSBC, IFC, Standard Chartered Bank

TABLE OF CONTENTS

FOREWORD

On behalf of ICMA and NAFMII, we are delighted to introduce this report on the Panda Bond Market and Perspectives of Foreign Issuers. This guide is addressed to potential issuers in the panda bond market, public authorities, legal and financial advisors, investors, and other participants in the Chinese capital markets. It is intended to provide practical guidance on raising capital in the Chinese panda bond market, and outline the range of motivations that foreign issuers currently have to pursue debt issuance in the onshore Chinese debt capital markets.

We would like to thank the members of the ICMA-NAFMII Working Group, comprising banks, investors, law firms, rating agencies and other market participants, for the time and effort they have devoted to creating this guide, as well as the many international issuers in the debt capital markets who have contributed their views and advice.

Introduction

The UK-China Economic and Financial Dialogue endorsed the continuation of a Working Group jointly chaired by ICMA and NAFMII to assist in the development of China's onshore bond market. The first report of the ICMA-NAFMII Working Group, published in 2015, was a review of practices and procedures in the Chinese onshore and international primary debt capital markets. This was followed by a report on green bond market practices and development in China and the international markets, published in 2017.

This report on the Panda Bond Market, completed pursuant to the 2016 Economic and Financial Dialogue focuses on panda bonds. In particular, the report describes the perspectives of potential foreign issuers on key considerations, attractions, and barriers with respect to issuance of RMB bonds in the onshore Chinese market. The report is based on qualitative, anonymous interviews with 27 issuers active in the international debt capital markets across various jurisdictions. Institutions that participated in the interviews include sovereigns, development institutions, international banks, asset managers, and non-financial corporations located in all regions of the globe (UK and Europe, Africa and Middle East, Americas, and Asia-Pacific). This report also reflects research conducted by NAFMII, ICMA, and member firms of the Working Group.

Executive Summary

Overall, the panda bond market is potentially attractive to foreign issuers for a variety of reasons.

1. Funding onshore operations: Many foreign corporates have significant economic ties to China, as a consumer market, operational hub, and/or manufacturing centre. Raising RMB directly onshore can simplify cash flow operations and reduce potential currency risk to match their RMB funding needs.

2. Investor diversification: The corporate finance policy of many issuers includes investor diversification as a core funding principle, and the large Chinese bond market investor base presents a significant opportunity to expand the base of creditors.

3. Liquidity: The onshore bond market as a whole is perceived to be generally more liquid than the offshore dim sum market. This is a potential advantage for issuers who seek RMB but are considering whether to issue RMB bonds offshore or onshore.

4. Marketing considerations: The greater overall accessibility of China has led to stronger economic and financial ties between domestic and foreign markets. Issuance of panda bonds by foreign institutions helps domestic market participants to develop a better understanding of how these institutions operate, builds trust between the two sides, and

EXECUTIVE SUMMARY

ultimately fosters the sustainable and efficient operations of foreign institutions in China. Furthermore, panda bond issuance by foreign government organizations also contributes to deepen bilateral financial cooperation and trade relations.

5. Global funding: The Chinese onshore bond market, like other international markets, may present an opportunity for foreign issuers to obtain funding in their primary currency (usually USD, EUR, or GBP) at attractive rates by issuing in RMB and entering into a cross-currency swap for their primary currency.

6. Market innovation: Some panda bonds to date have been motivated at least in part by a desire to be one of the first to market with an innovative transaction.

Most of the issuers surveyed expressed serious interest in the panda bond market and a willingness to manage any additional costs and risks relative to other markets. At the same time, they welcome further guidance and clarity on the issuance procedure to have more certainty over the issuance timetable and their ability to satisfy the regulator’s requirements for a successful issuance. A more regulated and institutionalized panda bond market would help stabilize the expectations of market players and increase market efficiency. Nevertheless, given that panda bond is in a nascent stage of development, there are only a limited number of issuance case studies, and it remains an open question how to align established domestic practices with international norms. Therefore, additional preparatory and exploratory studies are needed with respect to the pilot program for panda bonds before official rules would be ready for public release.

The issuance of panda bonds in China by foreign institutions is similar in many respects with the issuance of regular bonds in the Chinese interbank market. The main difference is the cross-border financing aspect. As a result, China has adopted a proactive yet gradual and prudent pace in the initial stage of the panda bond program, granting access to selected high-quality issuers. Currently, the regulatory rules governing domestic bonds serve as the basis for the regulatory framework for panda bonds, which is being adjusted in view of the special requirements of foreign issuers on the use of proceeds, preparation of registration documents, and information disclosure.

Panda Bonds and The RMB Markets

"Panda bonds" refers to bonds, issued in the Chinese bond market by foreign institutions duly registered outside the People's Republic of China, including by those registered in Hong Kong, Macau, and Taiwan. Panda bonds are usually denominated in RMB but may be issued in other currencies such as Special Drawing Rights of the International Monetary Fund (SDR).

Panda bonds are distinguished from "dim sum" bonds, which are denominated in RMB but issued in the offshore markets. Panda bonds are also not the same as Chinese domestic bonds, which are issued by onshore Chinese entities and subject to different sets of regulations specific to onshore issuers.

Panda bonds, as now generally understood, include bonds issued in both the Chinese domestic interbank bond market (which accounts for most Chinese bond issuance and trading) and the Chinese domestic exchange-traded bond market. Also, panda bonds may also technically include bonds issued by offshore affiliates of Chinese entities, such as Hong Kong subsidiaries of Chinese corporates. This report focuses on the perspectives of foreign-headquartered firms with respect to the interbank panda bond market.

Under the guidance of the People's Bank of China, NAFMII and its members actively and prudently promote the development and expansion of the panda bond market, by conducting intensive research on cross-border regulation practices in the overseas bond market, facilitating registration of pilot cases and enhancing institution building. As of the end of August, 2017, 42 panda bond issuers have entered the Chinese interbank market, 27 of which have registered panda bonds with NAFMII. Types of issuers include international development institutions, sovereign governments, financial institutions and non-financial enterprises. As of the end of August 2017, foreign issuers have issued a total of RMB 11.3 billion bonds through 57 transactions; the current outstanding volume is 96.9 billion RMB. The total registration quota has reached RMB 328.7 billion (including RMB 309.1 billion of RMB-denominated bonds and RMB 19.6 billion equivalent SDR-denominated bonds).

Bond Financing by Foreign Issuers in China's Interbank Bond Market
(At end of August, 2017)

Type of Issuers		Registration Quota (billion RMB)	Issuance Volume (billion RMB)	Outstanding Volume (billion RMB)	Number of Issuance
International Development Institution	ADB	2	2	1	2
	IFC	2	2	0	2
	New Development Bank	3	3	3	1
Government (Central/Local)	Republic of Korea	3	3	3	1
	Province of British Columbia, Canada	6	3	3	1
	Republic of Poland	6	3	3	1
	Republic of Hungary	3	1	1	1
Financial institution	HSBC(HK)	1	1	1	1
	Bank of China(HK)	10	1	1	1
	Standard Chartered(HK)	2	1	1	1
	Chong Hing Bank	3	1.5	1.5	1
	National Bank of Canada	5	3.5	3.5	1
	Agricultural Bank of China International	3	0	0	0
	China Construction Bank (Asia)	6	0	0	0
	Wing Lung Bank	10	0	0	0
	ICBC (Asia)	3	0	0	0
	China CITIC Bank International	3	3	3	1
	Malayan Banking Berhad	6	1	1	1
Non-financial Enterprise	Daimler AG	25	27	16.5	12
	China Merchants Holdings (HK)	3	0.5	0	1
	China Resources Land	20	10	10	4
	SMIC	6	2.1	1.5	2

Type of Issuers		Registration Quota (billion RMB)	Issuance Volume (billion RMB)	Outstanding Volume (billion RMB)	Number of Issuance
Non-financial Enterprise	Veolia Environment	15	1	1	1
	China Resources Cement	13.5	3.5	3.5	2
	Hengan International Group	5	2	2	1
	China Power International	5	2	2	1
	The Wharf Group	20	4	4	1
	China Traditional Chinese Medicine Co.	4.5	4.5	4.5	2
	China Merchants Port Holdings	10	4	2.5	2
	Iowa China	10	0	0	0
	Joy-City Property	10	0	0	0
	China Power New Energy Development	2.5	0.8	0.8	1
	China Jinmao	16	5	5	2
	China Gas	9.6	1.5	1.5	1
	China Huarong International Holdings	3	3	3	1
	Sino Ocean	10	4	4	2
	Bank of China Group Investment	8	1.5	1.5	1
	Kunlun Energy	10	0	0	0
	Shimao Group	8	0	0	0
	Longfor Properties	8	2	2	2
	Sun Hung Kai Properties	10	0	0	0
Total (RMB denominated bonds)		309.1	107.4	91.3	55
IBRD		18.63 (SDR 2 billion)	4.65 (SDR 0.5 billion)	4.65 (SDR 0.5 billion)	1
Standard Chartered(HK)		0.93 (SDR 0.1 billion)	0.93 (SDR 0.1 billion)	0.93 (SDR 0.1 billion)	1
Total in RMB (RMB and SDR denominated bonds)		328.7	11.3	96.9	57

The Development of The Panda Bond Market

1. Gradual expansion spearheaded by high-quality foreign issuers

In the formative stage of the interbank panda bond market, the issuers were mainly foreign institutions with strong credit profiles, stable financial positions, compliant business operations and sophisticated information disclosure practices. Among the 35 foreign issuers, 26 have been rated by Moody’s, Standard & Poor’s, or Fitch, with their ratings evenly distributed from BBB- to AAA, all classified as “investment grade.” Additionally, because foreign issuers in the interbank market are generally subject to stringent oversight in open, well-developed international markets, they have a high level of operational transparency.

2. A diverse mix of foreign issuers

Foreign issuers in the interbank market now include international development agencies, governments, financial institutions, and non-financial enterprises from such countries and regions as Canada, Germany, France, Poland, Hungary, Malaysia and Hong Kong. In particular, the foreign non-financial enterprises represent a wide variety of industries, including chip manufacturing, environmental protection, automotive, ports, medicine, power, warehousing and logistics, transportation, and real estate.

3. A wide array of products

Foreign institutions can offer a wide array of products in the interbank market through either public issuance or private placement. Products in the former category include medium-term notes, commercial paper, and super & short-term commercial paper. For products in the latter category, issuers can elect to offer them to special institutional investors through what is known as the "N+X system." Panda bonds usually have a term of one to three years, but the term can be shortened to 270 days or extended to ten years by the issuer according to its needs.

4. Focus on legal and compliance matters

Foreign institutions issuing panda bonds in China's interbank market generally have already established sound disclosure practices in overseas markets. Therefore, while existing Chinese interbank market rules form the basis for the documents and information that need to be disclosed by foreign institutions as part of their offering, appropriate accommodations pertaining to the frequency and language of such disclosures have also been given in consideration of the special nature of these institutions. Even so, foreign issuers are required to make adequate disclosures in issuing panda bonds in a way that is conducive to protecting investors. Furthermore, with respect to the use and transfer of raised capital, opening of related accounts, and submission of information, activities and transactions related to panda bonds must strictly follow applicable laws and regulations in China.

Panda Bond Issuance Procedure and Case Studies

1. Registration Procedures for Public Offering of Panda Bonds (Non-financial Enterprises)

Step One **Preparation of Registration Documents**

In general, the preparation of registration documents involves three stages. First, a potential issuer selects an appropriate product; second, the issuer completes the internal approval of the registration and issuance of the debt financing instrument to be issued, and engages an eligible lead underwriter and other intermediaries; and third, the issuer and the relevant intermediaries prepare the registration documents, and have the registration documents delivered by the eligible lead underwriter to NAFMII.

Step Two **Acceptance and Pre-review of Registration Documents**

NAFMII will review the completeness of the registration documents within one working day upon receipt of the registration documents. NAFMII will accept the registration documents if all types of required documents are complete, or will recommend that the issuer or the relevant intermediary supplement or modify the registration documents if the required documents are incomplete.

NAFMII will conduct a pre-review, in form, of the completeness of the registration documents to be disclosed, and give its feedback on pre-review within 10 working days. The issuer or the relevant intermediary should submit supplementary documents within 10 working days of the receipt of NAFMII's feedback. After receipt of the supplementary documents from the issuer or the relevant intermediary, working staff from NAFMII who conducted pre-review may issue a new feedback letter for pre-review if they deem that the information to be disclosed in the supplementary documents remains incomplete, or submit the registration documents to the registration meeting if they deem that such information meets the requirements of the relevant rules and guidelines.

Step Three Registration Meeting

After the completion of pre-review, working staff from NAFMII who conducted pre-review will submit the registration documents to the registration meeting for review, and the registration meeting will decide whether to accept the registration for the issuance of the debt financing instrument. The registration meeting will employ the collective wisdom of the market participants including experts from commercial banks, accounting firms, law firms, asset management companies or other institutions to ensure the independence, objectivity and impartiality of the review results. The registration meeting is composed of five registration experts who are selected randomly by NAFMII from the list of registration experts in accordance with the relevant recusal rules.

Each registration expert will deliver an opinion on the registration documents: either “Registration accepted”, “Registration accepted with conditions,” or “Registration postponed”. If all five experts give the opinion of “Registration accepted”, NAFMII will accept the registration; if two or more experts give the opinion of “Registration postponed”, NAFMII will postpone the acceptance of registration; in any circumstance other than those above, NAFMII will conditionally accept the registration, in which case, the issuer will be required to supplement or modify the registration documents according to the opinions of the registration meeting, and be subject to review again by the experts who gave the opinion of "Conditional acceptance" or "Registration postponed" before.

Step Four Acceptance of Registration

After accepting registration, NAFMII will deliver a formal Notice on Acceptance of Registration to the issuer. If it is the first time for the issuer to complete registration, NAFMII will hold an informational meeting with the senior management of the foreign issuer or the representative from foreign issuer's domestic subsidiary, and the lead underwriter, and deliver the Notice on Acceptance of Registration in person so that NAFMII can be in a better position to understand the details of the issuer and carry out post-registration supervision of the debt financing instrument. If this is not the first time that issuer completes registration, instead of holding an informational meeting, NAFMII will deliver the Notice on Acceptance of Registration electronically via its online information service platform. After the Notice on Acceptance of Registration is delivered, NAFMII will publish the notice on its official website (www.nafmii.org.cn) to make it available to the public.

StepFive Issuance

After receiving the Notice on Acceptance of Registration, the issuer may proceed with its first issuance of its panda bond. The issuer should issue its panda bond in accordance with the following classified self-regulation principles: (i) in the case of super & short-term commercial papers (SCPs), it may issue them at its discretion within a period of two years; (ii) in the case of commercial papers

(CPs)and medium term notes (MTNs), it may issue them at its discretion within 12 months after acceptance of registration, and should make a prior filing with NAFMII if it intends to issue them after the 12-month period; and (iii) in the case of asset-backed notes (ABNs), project revenue notes (PRNs), and perpetual notes,the time of issuance and prior filing shall comply with corresponding self-regulatory rules of NAFMII.

Panda bonds can be issued through public offering or private placement. The book building procedure for both is consistent with the generally adopted process for onshore bond issuance. Currently, technical support and service for the book building system of debt financing instruments are provided by Beijing Financial Assets Exchange. Prior to issuance, the issuer and the lead underwriter should prepare and disclose the Issuance Program, and submit it to NAFMII for filing.

Registration Documents for Public Offering of Panda Bonds (Non-financial Enterprises)

Consistent with previous panda bond issuances, registration documents for a public offering of panda bonds include:

- Registration report (accompanied by a legal registration certificate and the Articles of Association, Resolution of Board of Directors or other certification documents) :
- Recommendation letter from the lead underwriter
- Prospectus
- Audited financial reports for the recent three (3) accounting years and the accounting report for the most recent period(if any);
- Credit rating reports and statement on follow-up credit rating;
- Legal opinion letters issued by law firms in China and the country (or region) where the issuer is registered respectively;
- Underwriting agreement;
- Letter of consent from an overseas accountant (if applicable).

Case study China Merchants Holdings (HK) Company

Bond Profile

China Merchants Holdings (HK) Company Commercial Paper

Issuer Profile

Established by China Merchants Group and China Steam Navigation Company in 1987, China Merchants Holdings (HK) Company is a leading state-owned conglomerate which has three main business sectors of Transport (ports, roads, energy shipping, logistics, ship-repairing, marine engineering), Finance (banks, securities, funds, insurances), and Property (zones development, real estate).

Registration Location: Hong Kong

Accounting Standards: CASS

Registration Quota: RMB 3 billion

First Issuance Volume: RMB 500 million

First Issuance Maturity: 1 years

First Issuance Date: 2015-11-02

First Issuance Coupon Rate: 3.03%

Case Innovation

This commercial paper is the first non-financial enterprise panda bond issued by public placement.

China Merchants Holdings (HK) Company is the first red-chip company based in Hong Kong that issued panda bond in the interbank bond market.

Case study The Wharf (Holdings) Limited

Bond Profile

The Wharf (Holdings) Limited Mid-term Note

Issuer Profile

The Group is active in Hong Kong and Mainland China with prime real estate as primary strategic focus. Site acquisition, development and marketing are its core competencies while mall development and retail management remain its strategic differentiation. The Group also owns an emerging hotel business under Wharf Hotels, valuable port assets under Modern Terminals, and Communications, Media & Entertainment assets in Hong Kong.

Registration Location: Hong Kong

Accounting Standards: HKFRS

Registration Quota: RMB 20 billion

First Issuance Volume: RMB 4 billion

First Issuance Maturity: 3 years

First Issuance Date: 2016-09-22

First Issuance Coupon Rate: 3.10%

Case Innovation

The Wharf (Holdings) Limited is the first HK-based blue-chip company that issued panda bond in the interbank bond market.

Case study China Merchant Port Holdings

Bond Profile

China Merchant Port Holdings Super & Short-term Commercial Paper

Issuer Profile

China Merchants Port is the largest public port operator in China with investments in Mainland China, Hong Kong and overseas. Its parent company is China Merchants Group, a conglomerate established in 1872. It became a Hong Kong Hang Seng Index constituent stock in September 2004.

Registration Location: HongKong

Accounting Standards: HKFRS

Registration Quota: RMB 4 billion

First Issuance Volume: RMB 1.5 million

First Issuance Maturity: 270 days

First Issuance Date: 2016-11-18

First Issuance Coupon Rate: 3.19%

Case Innovation

This is the first Super & Short-term Commercial Paper panda bond.

2. Registration Procedures for Private Placement of Panda Bonds (Non-financial Enterprises)

The registration procedures for private placement are simpler than those for a public offering. An issuer only needs to submit the relevant registration documents, and NAFMII will initiate the acceptance procedures for such private placement registration documents that meet the relevant requirements, and verify, in form, the completeness of the registration documents. If the private placement registration documents submitted by the issuer are complete in form, NAFMII will accept its registration, and issue to the issuer the Notice on Acceptance of Registration. The registration quota will be valid for a period of two years.

Step One Preparation of Registration Documents

The issuer should complete the internal approval of the registration and issuance matters of the private placement note, engage an eligible lead underwriter and other intermediaries, and have written documents submitted by the eligible underwriter to NAFMII. The preparation of such written documents should meet NAFMII's requirements for the content and format of information disclosure in relation to private placement of debt financing instruments.

Step Two Acceptance and Pre-Review of Registration Documents

NAFMII will review the completeness of the registration documents within one working day upon receipt of the registration documents. NAFMII will accept the registration documents if all types of required documents are complete, or will recommend the issuer or the relevant intermediary to supplement or modify the registration documents if required documents are incomplete.

After accepting the registration documents, two reviewers from NAFMII will review the registration documents. Where the reviewers deem the information disclosed in the registration documents incomplete, NAFMII will send a Letter of Recommendation on Supplementing Information.Ifit is the first time the issuer completed the registration, the Letter of Recommendation from NAFMII shouldbe sent within 10 working days after accepting the registration documents; otherwise the Letter of Recommendation should be sent within five working days.The issuer or the relevant intermediary should submit any required supplementary documents within 10 working days of the receipt of NAFMII's feedback.

Step Three Acceptance of Registration

NAFMII will deliver a Notice on Acceptance of Registration to the issuer after the review of registration documents is completed. The delivery methods and the scope of application of conversational meetings in private placement are the same as those for a public offering.

Step Four Issuance

After receipt of the Notice on Acceptance of Registration, the issuer may proceed with the initial issuance of its panda bonds, which should meet the same requirements as for a public offering.

Registration Documents for Private Placement of Panda Bonds (Non-financial Enterprises)

Consistent with previous panda bond issuance, the registration documents for a private placement of panda bonds include:

- Registration report (accompanied by a legal registration certificate and the Articles of Association, Resolution of Board of Directors or other certification documents) :
- Recommendation letter from the lead underwriter
- Private Placement Agreement
- Audited financial reports for the most recent accounting year;
- Credit rating reports and statement on follow-up credit rating;
- Legal opinion letters issued by law firms in China and the country (or region) where the issuer is registered respectively;
- Underwriting agreement; and
- Letter of consent from an overseas accountant (if any).

Case study Daimler AG

Bond Profile

In December, 2013, Daimler AG’s RMB 5 billion private placement notes were officially registered. By the end of 2015, five times of issuance have been completed.
In February 2016, Daimler AG registered RMB 20 billion private placement notes.

Issuer Profile

With its divisions Mercedes-Benz Cars, Daimler Trucks, Mercedes-Benz Vans, Daimler Buses and Daimler Financial Services, the Daimler Group is one of the biggest producers of premium cars and the world’s biggest manufacturer of commercial vehicles with a global reach.

Registration Location: Germany

Accounting Standards: EUIFRS

Registration Quota: RMB 5 billion (2013); 20 billion (2016)

Latest Issuance Volume: RMB 1 billion

Latest Issuance Maturity: 3 years

Latest Issuance Date: 2016-11-07

Case Innovation

Daimler AG is the first non-financial enterprise panda bond issuer in China's bond market.

Case study Veolia Environment Group

Bond Profile

Veolia Environment Group private placement note

Issuer Profile

Veolia helps cities and industries to manage, optimize and make the most of their resources. The company provides an array of solutions related to water, energy and materials – with a focus on waste recovery – to promote the transition toward a circular economy.

Registration Location: France

Accounting Standards: EUIFRS

Registration Quota: RMB 15 billion

First Issuance Volume: RMB 1 billion

First Issuance Maturity: 3 years

First Issuance Date: 2016-09-01

Case Innovation

This private placement note is the first panda bond issued by a French issuer.

3. Panda Bonds Issued by Government Organizations

Registration Procedures for Government Organizations' Issuance of Panda Bonds

(1) The issuer communicates its intent of issuance with and makes application to PBOC. PBOC conducts a comprehensive assessment on whether to accept the application.

(2) NAFMII will accept the registration documents after receiving a consent letter from PBOC.

(3) During the registration process, review timing and standards, for non-financial enterprises should apply to the review of the issuance program of government organizations.

Registration Documents for Offering of Panda Bonds by Government Organizations

Consistent with previous panda bond issuance, the registration documents for an offering of panda bonds by government organizations include:

- Registration report
- Recommendation letter from the lead underwriter
- Authorization for bond issuance: an act, letter of approval or letter of consent of the legislature or the government with respect to the bond issuance, or an official confirmation letter with respect to the bond

issuance from the competent fiscal or economic authority of the issuing country Prospectus

- Legal opinion letter issued by a law firm in China
- Legal opinion letter issued by a law firm in the issuer country (or region)
- Financial report or economic data report for the most recent three years (and the most recent period, if any)
- Credit rating report and statement on follow-up credit rating (if any)
- Underwriting agreement

Case study Republic of Poland

Issuer Profile

Republic of Poland is a unitary state divided into 16 administrative subdivisions in Central Europe, a country along the Belt and Road.

Registration Location: RMB 6 billion

First Issuance Volume: RMB 3 billion

First Issuance Maturity: 3 years

First Issuance Date: 2016-8-15

First Issuance Coupon Rate: 3.40%

Case Innovation

This is the first panda bond issued by an European government.

Case study British of Columbia of Canada

Bond Profile

British Columbia of Canada is a province with the third largest population and an area of 95million hectares accounting for 9.5% of total land area of Canada.

Issuer Profile

British Columbia of Canada's economy is witnessing integrated development in areas of economic structure, employment, productivity and trade.

Registration Quota: RMB 6 billion

First Issuance Volume: RMB 3 billion

First Issuance Maturity: 3 years

First Issuance Date: 2016-01-21

First Issuance Coupon Rate: 2.95%

Case Innovation

This is the first panda bond issued by a government.

Reasons For Issuing Panda Bonds

An issuer's decision whether or not to issue panda bonds is not made in a vacuum. Any foreign issuer wishing to fund in RMB would consider carefully other alternatives, chiefly the dim sum bond market. Even within the scope of panda bonds, there may be alternate markets and methods of issuance such as private placement, the exchange-traded market and the nascent Shanghai Pilot Free Trade Zone. Potential options may exist outside the capital markets, such as direct loans from local banks or fully funded swaps in RMB.

Among corporates, there is a wide variation in the funding vehicle structure. Some have only one global funding vehicle and centralize treasury operations completely. Some have set up funding vehicles by region, for the Americas, Europe/Middle East/Africa, and Asia-Pacific. Still others have set up funding vehicles in one or more jurisdictions that allow the most tax-efficient capital raising. Ultimately this means that the regulatory constraints, costs of issuance, and attractiveness of the panda bond market will vary widely even for corporate issuers in the same jurisdiction or the same industry.

Issuers wishing to fund in home currencies other than RMB will consider panda bond pricing in comparison to other international opportunities to swap into home currencies. Several of the issuers interviewed have considered issuing, or already issued, in other Asia-Pacific currencies such as Japanese yen, Australian dollar, Singapore dollar, Malaysian ringgit, and Thai bhat, and will be familiar with the domestic markets in the region outside of China. Many international corporates, financials, and multilateral institutions already have Asian currencies embedded in their issuance programs.

In this context, the panda bond market is potentially attractive to foreign issuers for several different reasons. Among the aggregate of issuers interviewed for this study, the main reasons cited for issuing panda bonds are: (1) directly funding onshore operations, (2) investor diversification, (3) secondary liquidity, (4) political considerations, (5) global funding and (6) market innovation.

Funding onshore operations

Many foreign issuers have significant economic ties to China. For corporates, China may be a major consumer market, operational hub, or manufacturing centre. They may also conduct trade finance with China or have Chinese partners on joint ventures. Multilateral financial institutions also are involved in funding onshore development in China. However, economic ties alone may not be reason enough to need actual onshore funding in RMB through panda bonds. For example, some corporates have limited operations or investment in China, but significant revenues from Chinese consumers and businesses, and may have a greater need to match these with RMB assets rather than liabilities. Issuers with the most interest in panda bonds are those with significant production facilities in the onshore market and a genuine need for onshore RMB funding. [A foreign issuer may have other reasons to raise RMB, whether onshore or offshore. The panda bond market may also be used to raise funds to pay other RMB liabilities generated from trade, loans or offshore RMB bonds. At least one issuer noted that it seeks to hold RMB assets in treasury as a matter of internal policy. Some issuers, particularly financial institutions, simply wish to diversify the currency mix of their term debt.] Raising RMB directly onshore can simply cash flow operations and reduce potential currency risk.

A number of foreign corporates and financial institutions have significant revenue in China and some have onshore legal affiliates. In theory, these entities might wish to raise money directly in the domestic RMB bond markets through the domestic entities. However, at least among those corporates surveyed, these affiliates are generally operating entities that have no long-term assets and would not be used for financing. Most corporates with onshore Chinese subsidiaries would not want to borrow directly through onshore entities in the Chinese markets, either because the onshore subsidiaries are set up as operational entities or because of balance sheet and regulatory constraints. Therefore, even if these issuers require RMB funding onshore, they would still expect to remit panda bond proceeds back to a central or regional treasury, and then fund the China operations through cross-border transactions as they would for other international operations. An international corporate would issue in the Chinese market from its international funding vehicle, then use the money onshore in China.

Investor diversification

The corporate finance policy of many issuers includes investor diversification as a core funding principle. The large Chinese bond market fixed income investor base is impossible to ignore for any issuer with a global perspective, and presents a significant opportunity to expand the base of creditors. However, investor diversification is, in general, a secondary rather than primary reason for considering panda bonds. While a small minority of issuers would be willing to pay a premium to diversify the investor base into China, none of the issuers surveyed would decide to issue panda bonds solely for this reason.

For issuers in emerging markets outside of China and Europe, the panda bond market could be attractive. Chinese investors may in some cases take a different view toward political risk of certain countries. They may also have a more favorable allocation policy toward emerging market assets. Institutional investors in China may also, from the perspective of foreign issuers, have appetite for longer-duration bonds in significant size. China's private wealth investor base also presents a major opportunity as they are perceived to be under-allocated in bonds as opposed to other asset classes, and may already have familiarity and exposure to foreign names.

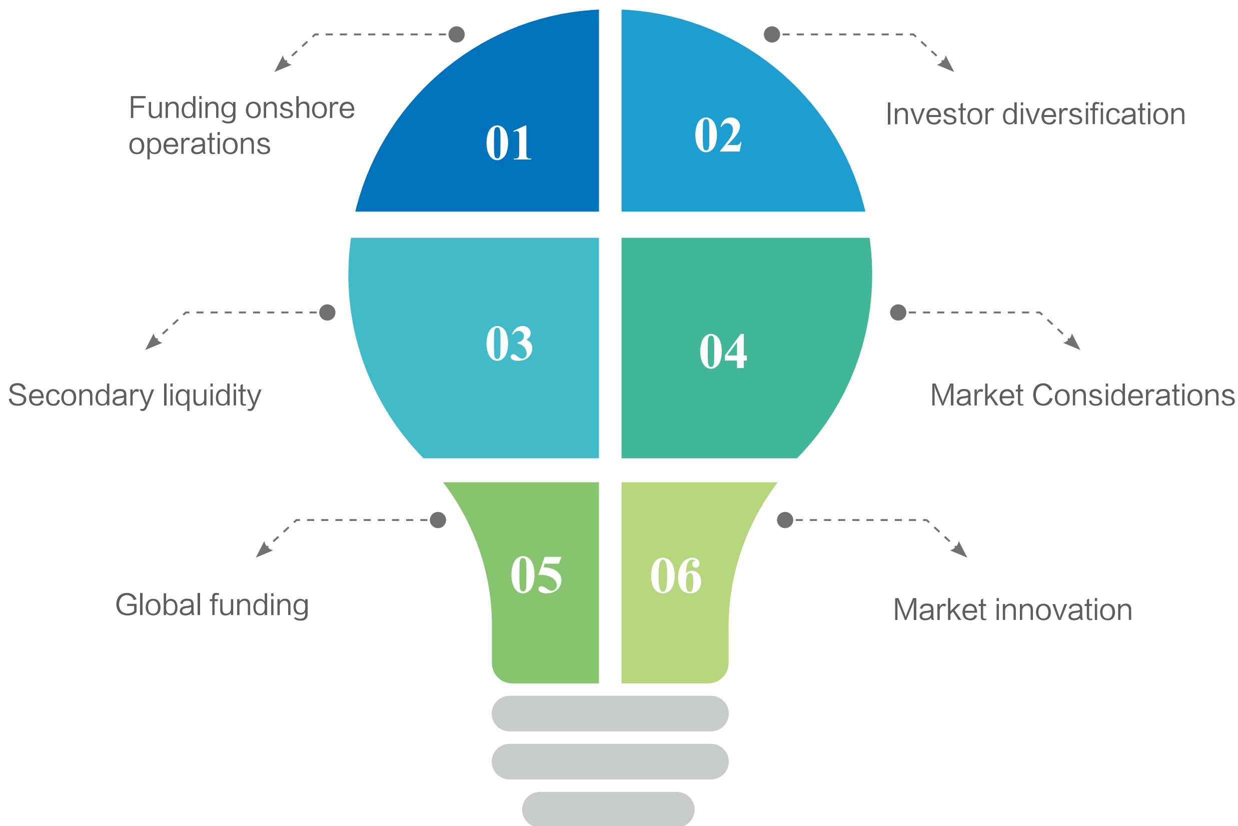
Some of the foreign issuers noted that they already have Chinese investors (particularly the government and banks) who have purchased the issuers' non-RMB bonds in the international markets. However, local investors in general may be unfamiliar with foreign names and there are challenges for local investors to diversify into international names. Investing in a panda bond will require additional credit analysis work for local investors, given that they have had only limited experience with international names.

A private placement of panda bonds, under current practice, may allow for less stringent reporting requirements and a simpler issuance procedure. Issuers vary in their views on private placement versus public issuance. Some, especially corporates motivated to fund in RMB, would be eager to pursue the private placement route as it would potentially reduce issuance cost and legal risk. However, other potential issuers, particularly multilateral institutions, would prefer to make a public issuance for internal policy or reputational reasons.

It is worth noting that panda bond investors already include non-Chinese investors as well. Since 2015, the PBOC has opened up opportunities for foreign investors and central banks to access the onshore bond market. Demand for panda bonds could be increased by foreign financial institutions (particularly foreign central banks, supranational organizations and sovereign wealth funds) which may be prepared to invest in a non-local name on the onshore market. PBOC has allowed most types of foreign financial institutions and asset managers to invest in the onshore fixed income market without a quota or any specific restrictions from a Chinese regulatory perspective.

Even with foreign investment now allowed into the onshore Chinese bond market, foreign issuers expect demand for panda bonds to come mainly from local Chinese investors. The launch of "Bond Connect" has further facilitated overseas investors' investment in China's interbank bond market.

REASONS FOR ISSUING PANDA BONDS



Foreign investors are more likely to prefer investing in normal yuan bonds issued by Chinese entities as opposed to panda bonds issued by foreign entities. Clearly, if a European corporate decides to issue a panda bond, foreign investors could already invest in the company's bonds in the European market, so there would be no advantage to purchasing the company's panda bonds unless the pricing was favorable from the investor's perspective. However, for the most part, the issuers themselves are unlikely to issue panda bonds if they are more expensive when converted to their home currency.

Secondary Market Liquidity

The onshore bond market is far larger and more liquid than the dim sum market. As the panda bond market is simply a subset of the onshore bond market, this could eventually be a potential advantage for issuers who are comfortable issuing RMB but considering whether to issue RMB bonds offshore or onshore. However, the panda bond market in isolation is still small compared to the overall domestic market, and most investors in panda bonds to date intend to hold them until maturity.

From the foreign issuer's perspective, more secondary liquidity is generally better. Secondary liquidity may be generally useful to benchmark prices in the primary market. But for almost all issuers surveyed, secondary liquidity in the panda market is not a major concern. Secondary liquidity is important to issuers mainly to the extent it is important to the investor's decision to purchase the bonds in the primary market. If issuers in the panda bond market expect that most investors will remain buy-and-hold, they will not be deterred by a lack of secondary liquidity in panda bonds.

Market Considerations

The greater overall accessibility of China has led to stronger economic and financial ties between domestic and foreign markets. Issuance of panda bonds by foreign institutions helps domestic market participants to develop a better understanding of how these institutions operate, builds trust between the two sides, and ultimately fosters the sustainable and efficient operations of foreign institutions in China. Furthermore, panda bond issuance by foreign government organizations also contributes to deepen the bilateral financial cooperation and trade relations.

For those corporate issuers whose strategy involves increased engagement or major transactions with China, panda bonds may be seen as a way to build trust with the regulators and financial markets. Also, sovereign and multilateral issuers may wish to enter the panda bond market to strengthen diplomatic ties with China and encourage further cross-border investment.

Some issuers, especially multilateral financial institutions, seek to play leading roles in RMB internationalization. International banks also seek to expand in mainland China and understand that their own issuance could help support their capital markets business as arrangers and underwriters.

Global funding

Many of the issuers surveyed perceive the panda bond market as an opportunity to obtain relatively inexpensive funding in their primary currency (commonly either USD, EUR, GBP, or CHF) by issuing in RMB and swapping the funds back. A number of issuers, particularly emerging market financial institutions, effectively fund only in USD from the international capital market. They may consider borrowing in the capital market in a number of currencies, often swapping into USD floating or fixed.

As such, for many issuers the decision whether to issue panda bonds will take into consideration market conditions, swap markets, and issuance cost. Many issuers already have RMB built into their bond documentation as an issuance currency, along with a number of other global and emerging market currencies, and monitor the markets to determine the effective funding cost in their home currency.

Market innovation

Some previously issued panda bonds were motivated at least in part by an objective to be one of the first to market with an innovative and groundbreaking financing. Multilaterals and corporates early to the market could benefit from prestige and favorable publicity. However, as of 2017 market innovation is not a major motivating factor for potential panda bond issuers anymore, as several panda bonds have now been issued, with many more in the pipeline, and the dim sum market has continued to mature.

Conclusion

The outstanding volume of China's bond market has surpassed RMB 70.4 trillion (approximately USD 10.6 trillion) as of the end of August, 2017, making it the third largest in the world. On the other hand, efforts to make the domestic bond market more accessible to foreign issuers and investors are still in their early stages. With the inclusion of RMB into the SDR basket and ongoing market-based reform of the RMB exchange rate regime, China's bond market will continue to attract stronger interest from foreign institutions. Boosted by continuous progress on the pilot program of panda bonds, an expanding pool of practical knowledge, the increasing familiarity of foreign institutions with the Chinese market, and more sophisticated systems and rules, the panda bond market is expected to achieve more concrete progress in the future.

中国银行间市场交易商协会

中国银行间市场交易商协会经国务院同意、民政部批准于2007年9月3日成立，为全国性的非营利性社会团体法人，其业务主管部门为中国人民银行，会址设在北京。中国银行间市场交易商协会是由市场参与者自愿组成的，包括银行间债券市场、同业拆借市场、外汇市场、票据市场和黄金市场在内的银行间市场的自律组织。协会单位会员涵盖政策性银行、商业银行、信用社、保险公司、证券公司、信托公司、投资基金、财务公司、信用评级公司、大中型工商企业等各类金融机构和非金融机构等。

About NAFMII

National Association of Financial Market Institutional Investors was founded on September 3, 2007, under the approval of the State Council of China. NAFMII aims to propel the development of China OTC financial market, which is composed of interbank bond market, inter-bank lending market, foreign exchange market, commercial paper market and gold market. As a self-regulation organization (SRO) in China, the membership of NAFMII includes policy banks, commercial banks, credit cooperative banks, insurance companies, securities houses, fund management companies, trust and investment companies, finance companies affiliated with corporations, credit rating agencies, accounting firms and companies in non-financial sectors.

国际资本市场协会（ICMA）

国际资本市场协会是一家代表国际资本市场的国际性组织，现有超过500家机构会员，分布于全球60个国家，其会员包括银行，发行人、资产管理公司，金融基础设施，律师事务所等等。ICMA通过提供行业准则及指引，包括涵盖了国际固定收益及相关产品的发行、交易及交割等，发挥了市场中重要且中心的作用。ICMA还与国家或多边的监管机构及政府部门紧密合作，确保相应的金融法规可以促进资本市场的效率同时又兼顾成本效益。

About ICMA

ICMA is the trade association for the international capital market, with over 500 member firms from 60 countries, including banks, issuers, asset managers, infrastructure providers and law firms. It performs a crucial central role in the market by providing industry-driven standards and recommendations for issuance, trading and settlement in international fixed income and related instruments. ICMA liaises closely with regulatory and governmental authorities, both at the national and supranational level, to ensure that financial regulation promotes the efficiency and cost effectiveness of the capital market.

DISCLAIMER

中国银行间市场交易商协会
地　址：北京市西城区金融大街甲9号 金融街中心南楼16层
联系电话：010-66539000　传　真：010-66539100
网　址：http://www.nafmii.org.cn/

ICMA

International Capital Market Association (ICMA)
Address: Dreikönigstrasse 8, CH-8002 Zurich, Switzerland
Tel: +41 44 363 4222　Fax: +41 44 363 7772
URL: http://www.icmagroup.org