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MARKET NEWS

Bond market

Steadily open China inter-bank bonds market to foreign investors

According to the bulletin published by the People's Bank of China (PBC) on July 23, further good news about the China's bond market – The Indonesian central bank (Bank Indonesia) has started making investment in China inter-bank bond market, marking further improvement of openness of the country's inter-bank bond market to foreign investors.

The investment of Bank Indonesia in China inter-bank bond market represents a trend that the market will continuously open its arms to foreign capital. This is another move to continue opening China inter-bank bond market to the world, since this April when PBC signed the *Agency Agreement for PBC to Act as Agent of International Bank for Reconstruction and Development (IBRD) to Invest in China Inter-bank Bond Market* and *Agency Agreement for PBC to Act as Agent of the International Development Association (IDA) to Invest in China Inter-bank Bond Market with the World Bank*.

Earlier, the Austrian central bank and several other overseas entities won the green lights to enter China inter-bank bond market, and last September, PBC approved the access of BOC Macau Branch and ANZ Hong Kong Branch to the market. Through these efforts, more and more foreign institutional investors are participating in China inter-bank bond market.

Macroeconomic news

New Provisions of QFII are published to relax restrictions and market access

On July 27, China Securities Regulatory Commission (CSRC) published the Provisions Concerning the Implementation of Relevant Issues, which relaxes the restrictions on overseas institutional investors to a large extent, and expands the market access to these investors.

According to the new provisions, CSRC will lower the qualification requirements for qualified foreign institutional investors (QFIIs), and

simplify the approval procedure. These new provisions already took effect on July 27. The QFII mechanism is the major channel for overseas investors to invest in China capital market.

The new provisions ease restrictions on the scope of QFII investments and on the share of QFII equity investment in Chinese listed companies. In another statement relating to the aforesaid new provisions, CSRC says the new provisions allow QFII to invest in China inter-bank bond market and the SME private placement bond market. CSRC also notes that foreign private equity institutions can apply for QFII qualifications as asset management institutions.

Ministry of Finance: Continue implementing proactive fiscal policies

Xie Xuren, Minister of Finance, said as he deployed key areas of the fiscal work for the second half of the year on July 26 that China will continue implementing proactive fiscal policies to boost stable economic growth. The minister also pointed out that efforts will be made to strictly implement differentiated housing tax policies, enhance tax collection and administration on house trading and possession, and curb housing demands for speculative or investment purposes in the second half of the year.

At the meeting of the directors of national finance departments (bureaus) that day, Xie Xuren stressed to continue implementing proactive fiscal policies to promote stable economic growth. These policies mainly include: carrying out and improving the structural tax cut policy; accelerating and expanding the business tax-to-VAT pilot; implementing tax policies that could support the development of small and micro enterprises; improving fiscal and tax policies and measures that can drive development of the circulation industry; and stabilizing fiscal and tax policies that could support foreign trade. Xie Xuren stressed the need to give full play to regulation and control roles of the fiscal and tax policies to propel economic restructuring and transition of the development pattern.

[NAFMII NEWS](#)

NAFMII Holds “System Innovation & Interbank Market Liquidity” Seminar

On July 16, NAFMII held the “System Innovation & Interbank Market Liquidity” Seminar in Changchun, which was attended by representatives from 30 institutions, including the People’s Bank of China, China Foreign

Exchange Trading System & National Interbank Funding Center, Shanghai Clearing House and China Government Securities Depository Trust & Clearing Co., Ltd.

At the meeting, attendees fully exchanged views on, and discussed in depth, the current status of the liquidity on the interbank market, the market maker system, the repurchase system, the construction of market infrastructures and other topics. The representatives unanimously thought that from the outbreak of the American subprime crisis in 2008 to the most recent sovereignty debt crisis in Europe, all countries have attached great importance to the liquidity of financial market products, and taken various measures to enhance market liquidity. In the development of the Chinese financial market, we should pay attention to the research of the liquidity of the interbank bond market, further reinforce innovation of financial products and systems and promote continuous improvement of the pricing mechanism, so as to effectively enhance the liquidity of the interbank market.

New Rules to Enhance Self-regulation in the Interbank Market

Assisted by investors, issuers, underwriters, law firms, accounting firms and other members, NAFMII has formulated the Protocol of the Self-regulatory Disciplinary Meeting of Debt Financing Instrument Market of Non-financial Enterprises (“Protocol”) and the Expert Management Procedure of the Self-regulatory Disciplinary Meeting of Debt Financing Instrument Market of Non-financial Enterprises (“Expert Management Procedure”) in accordance with the Self-regulatory Action Disciplinary for the Debt Financing Instrument Market of Non-financial Enterprises (“Self-regulatory Disciplinary Rules”) and relevant self-regulatory provisions of NAFMII. Upon the urgent appeal of market members following the publishing of the Self-regulatory Disciplinary Rules, the Protocol and Expert Management Procedure were made to secure the effective implementation of the market operation rules jointly studied and devised by market members, safeguard the legitimate rights and interests of the members, and maintain a good market order. Besides, based on the recommendation of the members, NAFMII has also built a pool of expert for the self-regulatory disciplinary meeting of debt financing instrument market of non-financial enterprises (the “Expert Pool”) to ensure the holding of the self-regulatory disciplinary meeting in a compliant, planned and efficient manner, elaborate the requirements for due performance of the experts of the self-regulatory disciplinary meeting, and smoothly carry out the self-regulatory disciplinary actions. The two systems and the pool of the expert were approved and adopted at the Second Meeting of the Third Executive Council of NAFMII on July 6, 2012, and officially published on July 16, 2012, which will be implemented as of October 1, 2012.

NAFMII Holds a Special Event on Interbank Market Investor Education and Service in Changchun amid to Enhance Risk Education and Establish Correct Investment Philosophy

On July 17, 2012, NAFMII hosted a special event on interbank market investor education and service in Changchun, which was attended by more than 40 banking institutions from the interbank market. The event aims to proactively deliver on the service philosophy of NAFMII, advocate and communicate correct investment concepts, reinforce risk awareness of investors, enhance investor capacity to prevent and manage risks, and continuously conduct investor education. NAFMII deputy secretary general Yang Nong and leaders of PBC Changchun Central Sub-branch attended the event and delivered speeches.

At the invitation of NAFMII, renowned experts and senior professionals in the domestic market presented at the event and delivered detailed elaboration and lecturing on such topics as the current macroeconomic trend and policy outlook, new financial cycle and risk management, trading strategy for the interbank market, trading and pricing of interest rate derivatives, credit risk mitigation instruments and risk management. The experts and representatives presented at the event made thorough discussions and in-depth exchanges on current market hotspots, including China's macroeconomic climate, the development of bond market and current investor structure, economic cycle and credit risk, new trend of the financial cycle and market risk, credit risk decentralization & sharing mechanism, investor protection and building of the investor team.

NAFMII Holds 2012 Mid-year Financial Market Operation Analysis Seminar

On July 27, NAFMII held the 2012 Mid-year Financial Market Operation Analysis Seminar, which was attended by 25 financial institutions and enterprises, including the Financial Market Department of the People's Bank of China (PBC), Beijing Financial Assets Exchange, China Development Bank and Industrial and Commercial Bank of China (ICBC), and also present at the meeting was Secretary-General Mr. Shi Wenchao. At the seminar, experts had in-depth discussions and exchanges on such issues as the world's economic and financial climate in the middle of 2012, the trend and future prospects of China economy, the macro control policy mix, and the operation of the financial markets, particularly the bond market.

NAFMII Publishes the Form System of Registration Document for Debt Financing Instruments of Non-financial Enterprises

To regulate information disclosure by the non-financial enterprises issuing debt financing instruments on the interbank bond market, urge intermediaries to perform duties with diligence and loyalty, and protect the lawful rights and interests of investors, NAFMII formulated the Form System of Registration Document for Debt Financing Instruments of Non-financial Enterprises (the Form System) in accordance with the Administrative Measures for Debt Financing Instruments of Non-financial Enterprises in the Interbank Market (PBC Decree [2008] No.1) and relevant rules and guidelines of NAFMII. The Form System was examined and adopted by the Third Executive Council at its first meeting on March 1, 2012, and has been registered with and approved by the People's Bank of China.

The content of the Form System mainly includes: First is the list of registration documents, which clearly indicates in a form that all the written documents should be provided by issuers and relevant intermediaries when applying for the registration of debt financing instruments. Second is the information disclosure form, which lists in detail the minimum disclosure requirements for information disclosure documents of issuers when they issue debt financing instruments. Third is the supplementary form of Form M, which is particularly designed to satisfy investors' requirements for information disclosure on special items such as health and safety, qualified audit report, related-party transactions, major asset restructuring and credit enhancement.

A Delegation Headed by Deputy Governor Hu Youtao Visited NAFMII

On August 2, 2012, a delegation led by Hu Youtao, Deputy Governor of Jiangxi Provincial Government visited NAFMII. They took a tour of the registration information system for debt financing instruments of non-financial enterprises and the information management system of the Post-registration Supervision Center, and discussed with NAFMII leaders on leveraging the interbank bond market to boost economic and financial development in Jiangxi Province.

NAFMII Publishes Guidelines on Asset-backed Notes

To propel the development of the financial market, improve utilization efficiency of outstanding assets of enterprises, broaden financing channels for enterprises, and regulate the conduct of non-financial enterprises to issue asset-backed notes on the interbank bond market, the National Association of Financial Market Institutional Investors (NAFMII) organized market players to draft the Guidelines on Asset-backed Notes of

Non-financial Enterprises on the Interbank Bond Market (the Guidelines). The Guidelines was launched for implementation on August 3, 2012 after being examined and adopted by the second meeting of the NAFMII Third Executive Council on July 6, 2012, and being filed with and approved by the People's Bank of China (PBC).

As an emerging debt financing product, the asset-backed note product has special arrangement in risk isolation, information disclosure, investor protection and other dimensions. When drafting the Guidelines, NAFMII fully borrowed the general practice of asset-backed securities in the mature markets and the practical experience of credit asset securitization in China, and, in consideration of the actual demand and development environment of the Chinese financial market, mainly regulated the asset type, risk isolation, trading structure, information disclosure, rights and obligations of participants and other aspects relating to asset-backed notes, with emphasis, in particular, on the reasonable protection mechanism for asset-backed note investors. In addition, during the drafting of the Guidelines, NAFMII fully considered the actual legal environment and supervisory environment faced by the implementation of asset securitization, and extensively solicited and absorbed the opinions of the market institutions like issuers, investors, lead underwriters, law firms, accounting firms and rating agencies. On this basis, NAFMII set the inclusive regulations on such aspects as the type of underlying assets and design of trading structure to reserve a space for future innovation.

NAFMII signs Four Trilateral MOUs with Local governments and Central Sub-branches of PBC

NAFMII signed four trilateral MOUs with Local governments and Central Sub-branches of PBC last month.

On July 11, NAFMII signed a trilateral MOU with the People's Government of Qinghai Province and PBC Xining Sub-branch in Xining. On July 12, NAFMII and PBC Urumchi Central Sub-branch signed the MOU with the People's Government of Xinjiang Uygur Autonomous Region and Xinjiang Production and Construction Corps (the Corps) respectively in Urumchi. On July 24, NAFMII signed a trilateral MOU with the People's Government of Jiangxi Province and PBC Nanchang Sub-branch in Nanchang.

[NAFMII RESEARCH](#)

Renminbi Exchange Rate Regime under Gradual Liberalization of Capital Accounts in China—From the Perspective of Financial Market

This report reviews the Renminbi exchange rate formation mechanism and the gradual reform of China's capital accounts, analyzes the history and current status of the international monetary system and the international status of Renminbi, and assesses the financial risks in the liberalization of the Renminbi capital accounts. On this basis, this report analyzes the capital account management and the Renminbi exchange rate formation mechanism in depth, suggests the onshore financial markets, especially the onshore bond market, should play a greater role during the opening of the capital accounts and the liberalization reform of the Renminbi exchange rate formation mechanism, provides suggestions for the capital account management and the reform of the Renminbi exchange rate formation mechanism, and analyzes scenarios Renminbi exchange rate will lead to.

Research on Relevant Issues of Accounting & Taxation System for Credit Risk Mitigation (CRM) Instruments

On October 29, 2010, the National Association of Financial Market Institutional Investors (NAFMII) organized market members to research and launch the Chinese version of credit derivatives – Credit Risk Mitigation (CRM).

To serve the market, and further promote the compliant, healthy and sustained development of CRM business, NAFMII organized market members to make research on the CRM accounting and taxation system. Based on the market significance of the launch of CRM, the report studies the accounting treatment and taxation treatment of the CRM in three parts. Part 1 mainly discusses the classification and operating mechanism of CRM products as well as the current status and problems of the CRM business. Part 2 compares and analyzes accounting treatment and information disclosure in detail. Part 3 mainly addresses tax collection on the CRM business, gives relevant policy suggestions on turnover tax, income tax and stamp tax based on the foreign practices, and provides references for tax authorities to determine the tax payment method of the CRM.

Research on Valuation & Pricing Technologies for Credit Risk Mitigation (CRM)

Due to a short history, China's debenture and credit derivatives market has neither accumulated enough underlying data relating to the credit risk, nor achieved broad information coverage. For this reason, serious restrictions exist when the Merton model, the simplified model, the Monte Carlo simulation and other modeling method widely used internationally are applied to China debenture and credit derivative

market. Besides, the current CRM follows the principle of “penetrability” relating to single subject entity and single subject debt, so it is different from the traditional CDS. Thus, the reasonable pricing method of the CRM has become one of the market concerns.

To address the problem, this report reviews the pricing principles and models for traditional credit derivatives, sums up the basic pricing model suitable for the CRM, and suggests the direction for future improving, based on the actual conditions of the domestic CRM market, theoretical derivation and empirical test.

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