中国银行间市场交易商协会
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ICMA
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Investing in China's Interbank Bond Market: A Handbook

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This handbook will be updated and amended by NAFMII and ICMA from time to time. If any domestic or overseas market participants have any corrections, suggestions or updates, please contact the International Department of NAFMII or ICMA:

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Preface

China's financial sector has developed significantly in recent years. Reform and opening-up have improved the system's mechanism for transmitting monetary policy and its framework of macro-prudential regulation, liberalized interest and exchange rates, enhanced its capacity to allocate financial resources, and broadened its two-way connections with global markets. Against this background, the bond market, based on an OTC model with participation from institutional investors has gained both depth and breadth. By the end of 2020 it was the second largest bond market in the world, with its outstanding volume exceeding RMB 117 trillion (USD 18 trillion). The China interbank bond market (CIBM) accounts for 86% of the total size of the domestic market (exchange-traded bonds constitute the remainder). The market's progress has expanded direct financing of companies and increased the variety of sources of financing available to business sectors, reducing risk in the banking sector and enhancing the overall financial system's stability.

The regulatory authorities, including the People's Bank of China (PBC), have made efforts to open the market further to overseas issuers, investors and intermediaries, particularly investors. By the end of July 2021, in terms of entities, 487 overseas investors have registered through the CIBM Direct scheme and 686 overseas investors through the Bond Connect scheme.

Bond Connect and the CIBM Direct scheme have created new ways for overseas investors to access onshore bonds, complementing the long- established QFII and RQFII schemes. Panda bonds, asset-backed notes (ABNs) and other types of bonds have been successfully issued through Bond Connect. Tax policies have been announced to support overseas investors' participation in China's bond market. Chinese government bonds (CGBs) and policy financial bonds (PFBs) have been included in the Bloomberg Barclays Global Aggregate Index and Chinese government bonds have been included in JP Morgan's Government Bond Index-Emerging Markets and the FTSE World Government Bond Index (WGBI). Together, these steps have accelerated the acceptance of China's bond market into the mainstream of the global fixed-income market.

As a self-regulatory organization (SRO) for the China Interbank (OTC) market, the National Association of Financial Market Institutional Investors (NAFMII) actively promotes the opening-up of China's bond market. By the end of July 2021, with PBC's guidance NAFMII had assisted 56 overseas institutions in issuing bonds[1] totalling RMB 313.95 billion (USD 49 billion). Of this total, overseas investors took up no less than 88% of the panda bonds issued by the Philippines, as well as over 70% of those issued by the Province of British Columbia and 55% of those issued by Hungary.

NAFMII has also established market-based evaluation methods for credit rating agencies and underwriters so that more eligible overseas entities can expand their business in China. Moreover, NAFMII has sought to create a better 'soft environment' around the market by promoting two-way cross-border communication and carrying out joint research on domestic and international market practices.

NAFMII developed this Handbook with the International Capital Market Association and market experts to meet demand from domestic and international market participants for an objective, comprehensive and accurate source of information about China's bond market. It is divided into two parts and four chapters. The first part explores the market's key elements, current status and future outlook, as well as the benefits of investing. The second part provides detailed guidelines for international investors seeking to invest in the CIBM via three channels. The overall goal is to help overseas institutions and individuals understand the CIBM better.

1 Including RMB bonds issued in the CIBM by overseas government agencies and international development institutions.

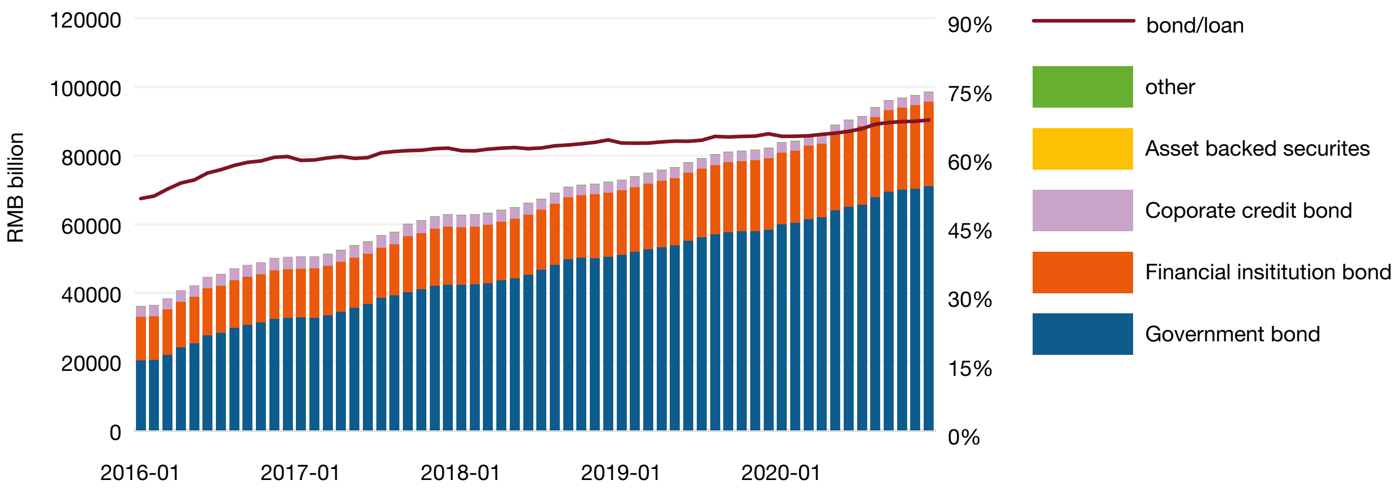
Chapter 1 - Growing international interest in CIBM

1.1 Market growth potential

Over the last 15 years, China's bond market has expanded steadily and rapidly. Traditionally, indirect financing (such as loans) has been the main form of debt financing. However, government agencies at all levels, financial institutions and enterprises in China have adopted bond financing in recent years: the ratio of the outstanding volume of bonds to loans has increased from 36% at the end of 2007 to 68% at the end of 2020. The market's product range has continued to broaden, now ranging from CGBs and local government bonds (LGBs) to PFBs and corporate credit bonds, as well as interest rate and credit derivatives. The investor base has diversified and now, according to CFETS statistics, includes 39,910 institutional investors such as sovereign institutions, banks, securities firms, insurance companies, funds and asset management products.

By the end of 2017 China had become the second largest bond market in the world and the largest in Asia[2]. The outstanding volume has increased from less than RMB 10 trillion (USD 1.6 trillion) in 2006 to over 100 trillion (USD 15.5 trillion) in 2020 with an annual growth rate of 16.5%, higher than China's GDP growth rate in the same period. The issuer universe has broadened as well. The government's share of bond financing has dropped from 56% to less than 40%, while the share of corporate issuance has increased from less than 10% to 25%.

Chart 1-1 Outstanding volume of various products and bond/loan ratio in China's bond market since 2016

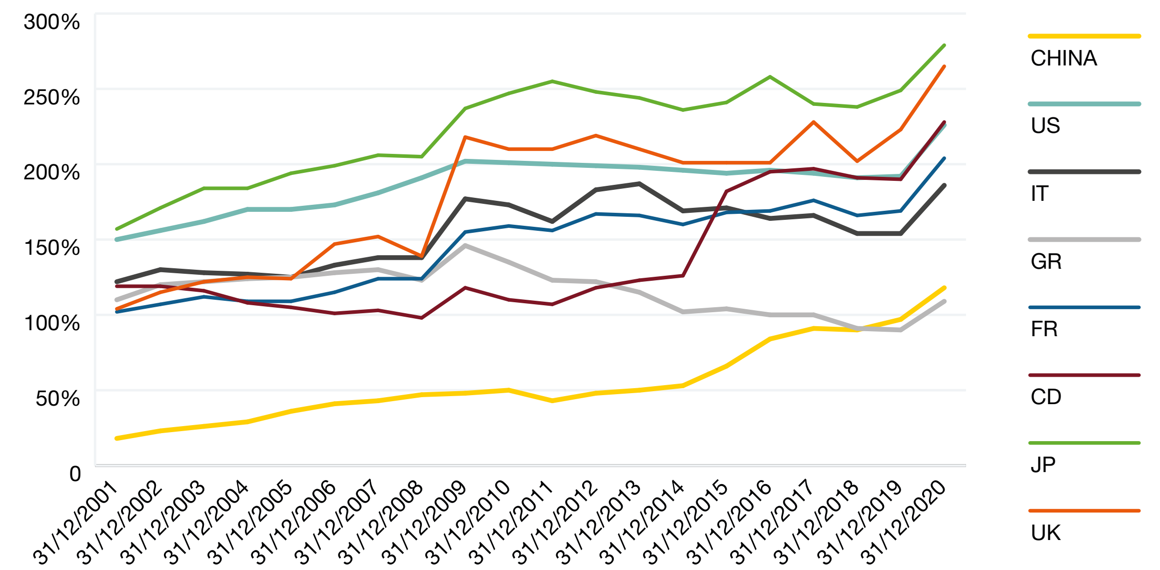


Source: Wind. Bank of China.

Although it has grown rapidly in size (and quality) in recent years, when compared with domestic GDP, China's bond market still has ample room to expand compared to other countries. After years of high growth, the market's outstanding volume still stands at about 100% of GDP, which is similar to Germany but much lower than that of other G7 countries like the United States, the United Kingdom, Japan and France. In addition, market trading is still on a growing trend. Average daily turnover has increased from RMB200 billion in early 2011 to about 1 trillion in 2020. However, this still represents less than 1% of outstanding volume. Overall China's bond market still has significant growth potential in its issuance and trading, which calls for a more active role for international issuers and investors.

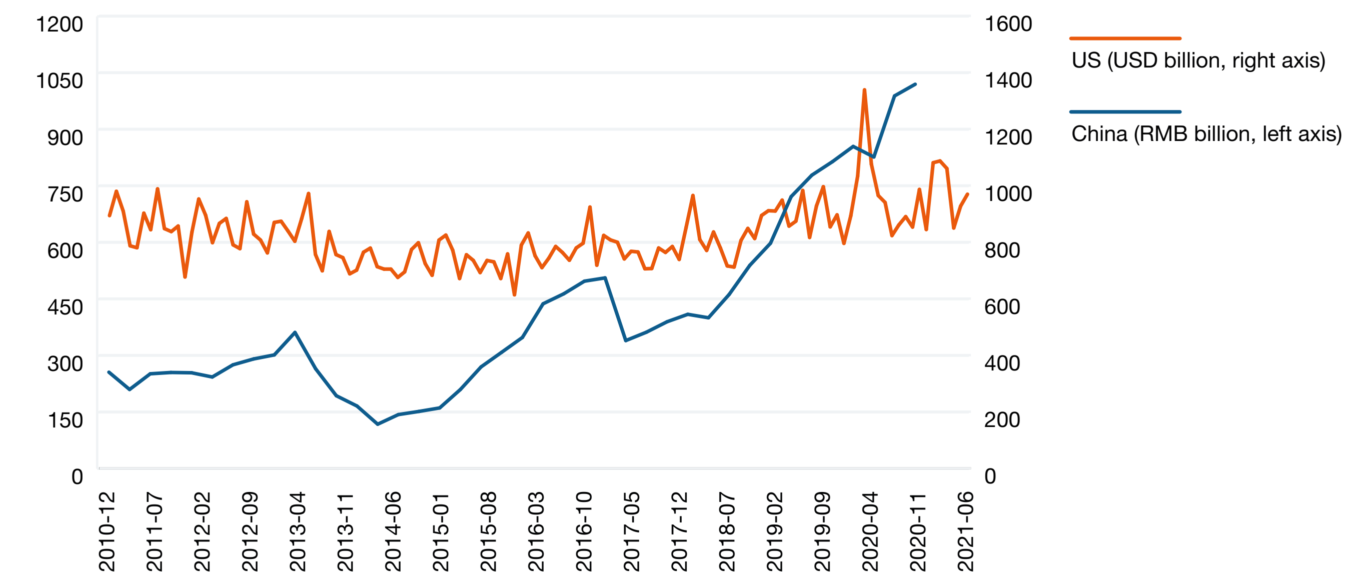
2 According to BIS, https://stats.bis.org/statx/srs/table/c1?p=20184&c=

Chart 1-2 Ratio of bond market size to GDP (current prices) - China versus G7 countries



Source: IMF, BIS. Bank of China

Chart 1-3 Comparison of monthly trend in daily average bond trading volumes - China and the US



Source: Wind, SIFMA. Bank of China.

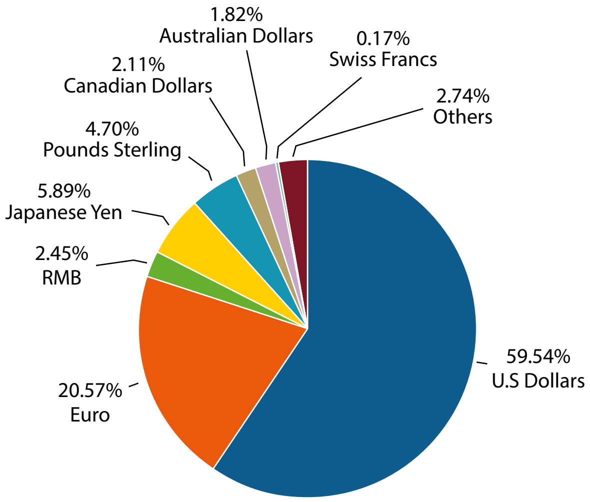
1.2 China's position in global portfolios

1.2.1 Scope for greater RMB allocation

Despite the Chinese market's significant size and growth potential, RMB bonds still account for a modest share of global portfolios. According to Boston Consulting Group's *Global Wealth Report 2018*, USD 121.6 trillion dollars of global private wealth was in investable assets and about 19% (USD 23 trillion) of this was invested in investment funds. At the end of 2017 the value of RMB bonds held by international investors was only USD 177 billion. By the end of 2020 the total value of their RMB bond holdings was about USD 503 billion.

The currency structure of global central banks' foreign exchange reserves also provides a good yardstick. Official institutions mainly invest their reserves in assets with high security and liquidity, such as CGBs. By the end of 2021Q1, RMB assets had reached an all-time high in foreign exchange reserves, but at 2.45% were still far below the proportion of Japanese yen and pound sterling and only comparable to Canadian dollars – even though RMB accounted for 10.9% of the SDR currency basket and was its third largest currency, while yen and sterling were only 8.3% and 8.1%, respectively. This suggests that global central banks have also significantly under-allocated their assets to RMB.

Chart 1-4 Currency structure of global central banks' foreign exchange reserves

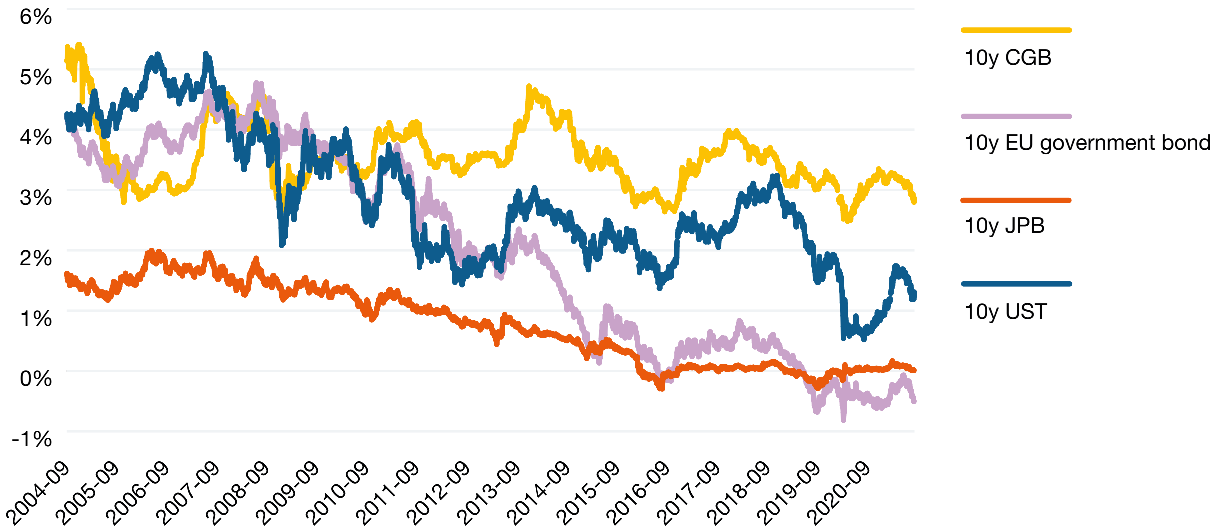


Note: as of the end of 2021 Q1.
Source: IMF, Bank of China.

1.2.2 Attractive yields

RMB bonds offer higher yields than developed economies' government bonds. The disparity has become more pronounced since the 2008 financial crisis when QE and other unconventional monetary policies were adopted widely. The 10-year CGB yield average in the past 2020 was 2.94%; the comparable figures for the US, Japan and Eurozone in the same period were 0.89%, 0.01% and –0.43%, respectively.

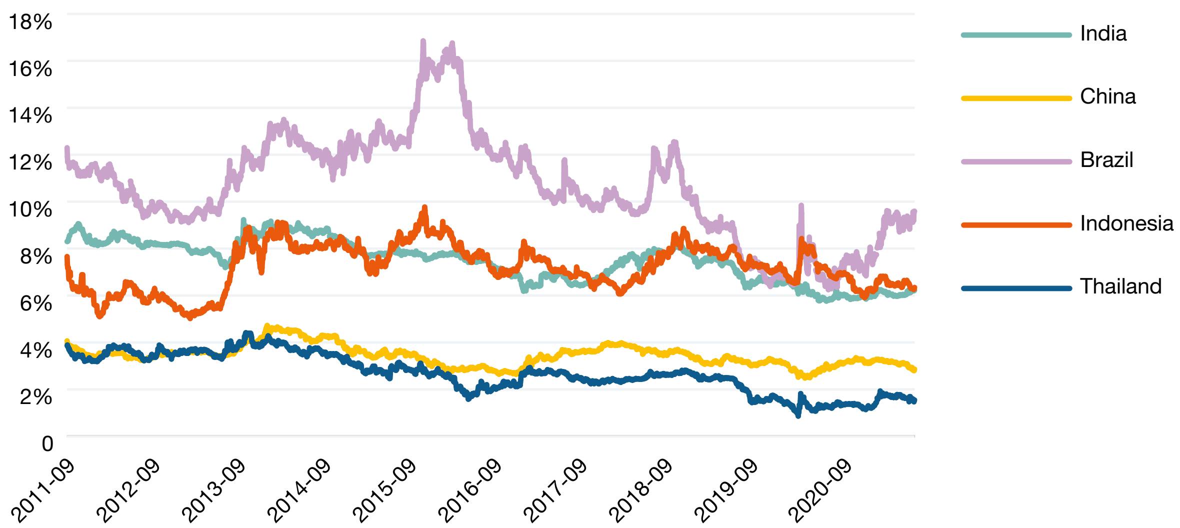
Chart 1-5 10-year government bond yields



Source: Wind, Bank of China.

Compared to emerging market government bonds, RMB yields may not always be higher, but international investors may prefer them in view of China's higher credit rating and RMB's relatively stable value. As of August 2021, China had a current sovereign rating of A1 from Moody's, whereas Thailand, Indonesia, India and Brazil are only rated Baa1, Baa2, Baa3 and Ba2, respectively.

Chart 1-6 10-year government bond yields in emerging markets



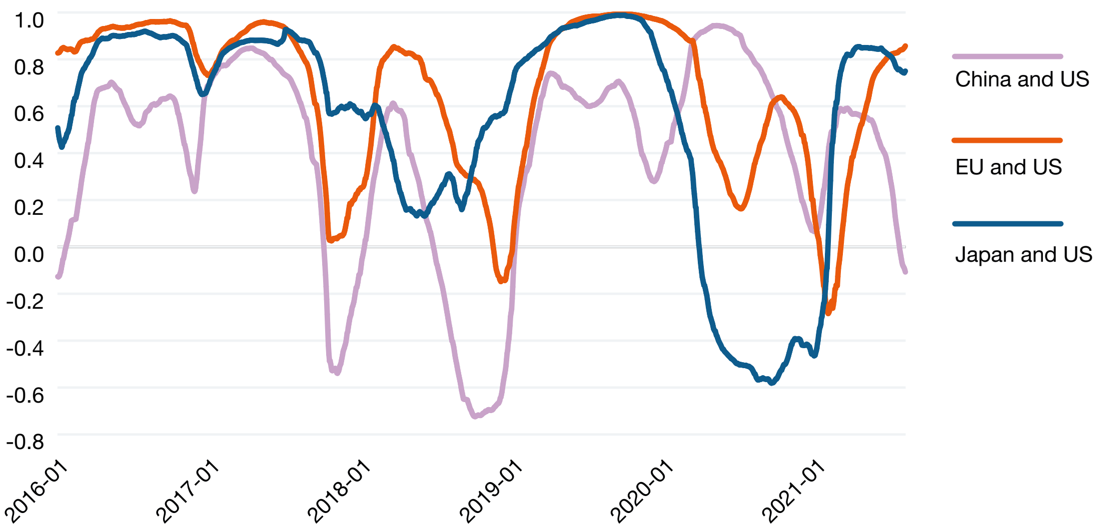
Source: Wind, Bank of China.

1.2.3 Diversification potential

From the perspective of risk diversification, the correlation between China's economic performance and that of developed economies such as the US, Japan and Europe, is relatively weak. For example, the correlation coefficient of GDP growth between China and the US is negative, whereas between the US and Japan and between the US and Europe it is above 20%.

Similarly, the rolling correlation coefficient of government bond yields between China and the US is weaker than that between Japan/ EU and the US for most periods after 2010. RMB bonds' relative 'independence' is conducive to reducing portfolio risk and increasing expected returns.

Chart 1-7 Correlation coefficient of sovereign bond yields-relative independence of RMB bond yields



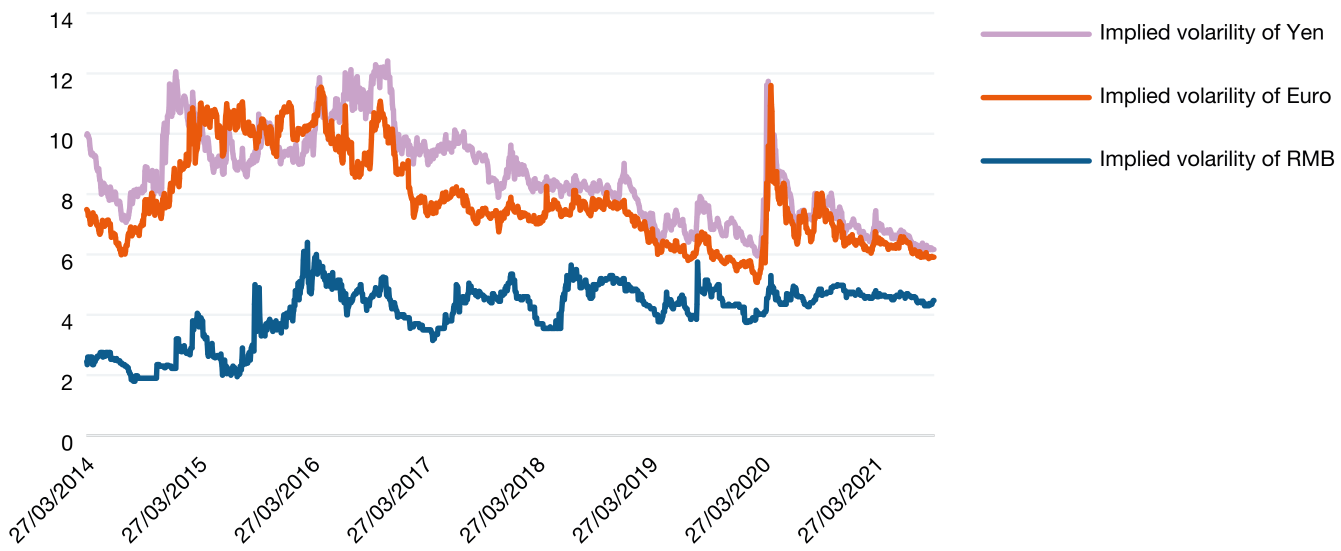
Source: Wind, Bank of China.

1.2.4 RMB stability

As in other local currency markets, investing in Chinese bonds involves foreign exchange risk for international investors. However, this is still relatively limited.

Together with absolute yields, currency volatility and outlook it plays a vital role in global bond investors' allocation decisions. Despite recent RMB moves, the currency's implied volatility has been significantly lower than those of developed countries' currencies. This implies lower foreign exchange risk for bond investors than in other local currencies.

Chart 1-8 Low implied volatility of RMB



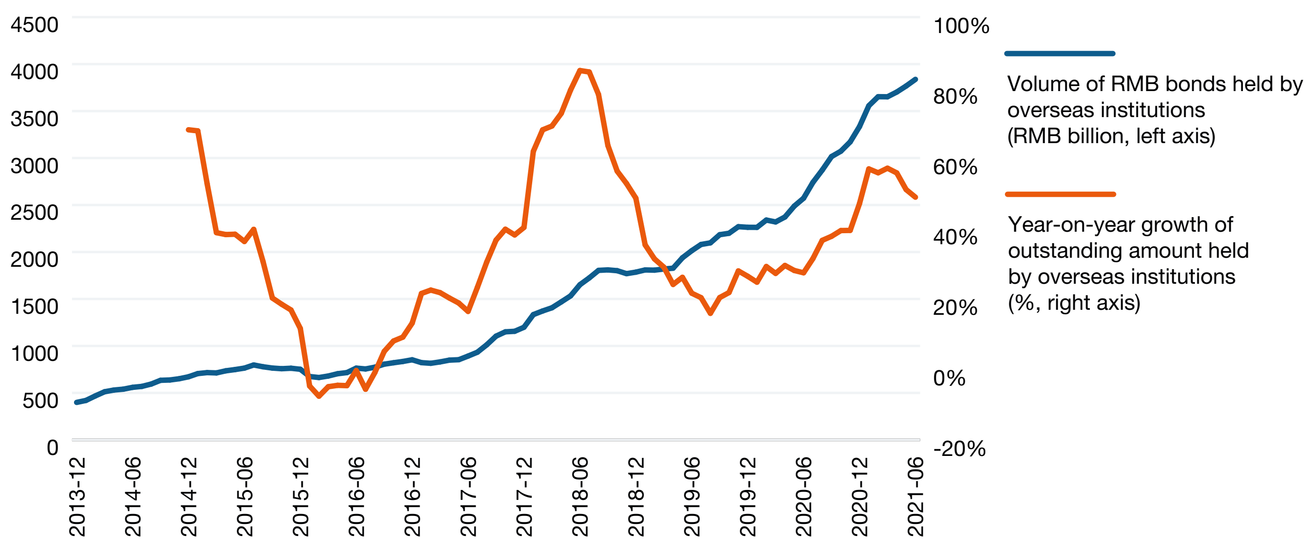
Source: Bank of China.

1.3 Continued opening-up

Driven by RMB bonds' fundamental attractiveness and the Chinese market's further opening-up in recent years, international investors have been actively purchasing RMB bonds.

The opening of China's bond market, has promoted the market's sound development and attracted additional capital inflows, which eased the pressure of bond supply. It also provides valuable opportunities for overseas investors operating in developed economies' low interest rate environment to raise their returns and diversify investment risks.

Chart 1-9 Overseas investors' holdings in the CIBM



Source: Wind, Bank of China.

International investors now enjoy broader market access, a richer variety of investible products, more liberal cross-border capital flows, and greater tax relief. In addition, Bloomberg Barclays Global-Aggregate (BBGA), JP Morgan Government Bond Index Emerging Markets and FT RUSSEL WGBI have gradually incorporated RMB bonds, which has prompted overseas investors to participate in the onshore market.

RMB bonds' growing importance in global portfolios is likely to also have a profound impact on China's bond market.

Table 1-1 Incorporation of RMB bonds into international bond indices

Index	Current Process	Tracking Asset Size	RMB Bonds Proportion
GBI-EM Global Diversified	In September 2019 JP Morgan announced that it would gradually incorporate Chinese government bonds into the index and completed the process at the end of 2020	$230 billion	10%
Bloomberg Barclays Global Aggregate	Bloomberg has been incorporating CGBs and PFBs into the index since April 2019, and has completed the process.	$2,000 billion	6-7%
FT Russell WGBI	FT-Russell has announced it will add China government bonds into its WGBI starting from 2021, September	$2,000 billion	Estimated 10%

Source: Goldman Sachs.

1.4 The case for RMB exposure

Besides the market's significant size and higher yields, the case for international investors buying Chinese bonds has further arguments. Managed properly, they provide an attractive way of diversifying portfolio risk and enhancing risk-adjusted returns.

1.4.1 Low correlations with other markets

Chinese bonds' low correlations with bonds in other markets also offers a means of allocating risks and reducing portfolio volatility.

Table 1-2 Correlations between CGB, UST, EU Government Bonds and JGB since 2009

	10y CGB	10y UST	10y EU Government Bond	10y JGB
10y CGB	1.00			
10y UST	0.57	1.00		
10y EU Government Bond	0.55	0.52	1.00	
10y JGB	0.49	0.63	0.97	1.00

Source: Wind, Bank of China.

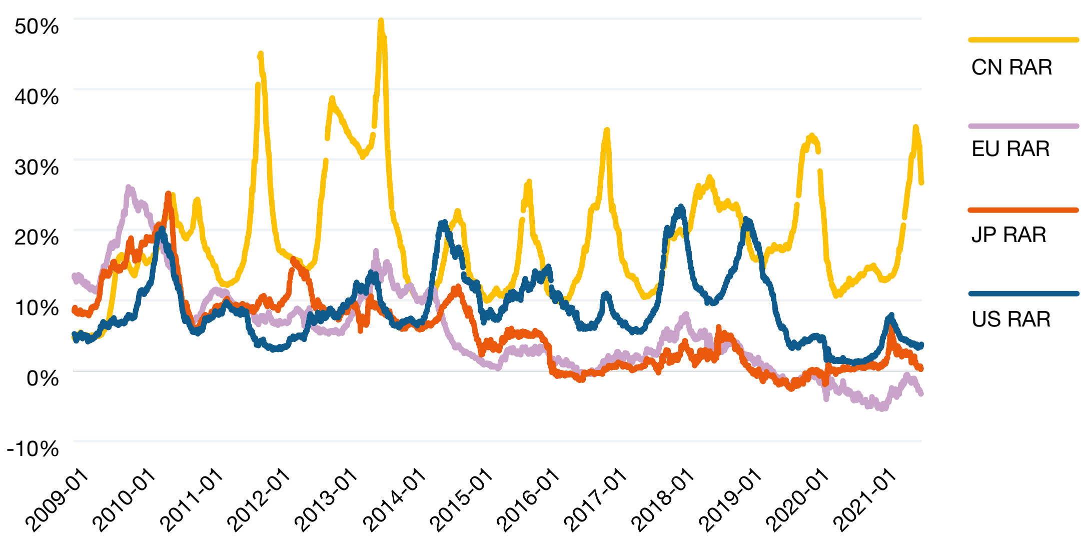
This suggests that global bond portfolios can achieve significant diversification if they include Chinese bonds. This is especially so in a market environment where global assets tend to move in tandem with general risk sentiment.

It is also true that since the 2008 financial crisis especially during the pandemic period, monetary policy and bond yields across countries have tended to move together. Accordingly, China's correlation with other countries rose a little after 2009. Nonetheless, it remains relatively low and continues to offer diversification benefits.

1.4.2 Lower volatility

In addition to low currency volatility, RMB bonds' total return has also experienced lower volatility than others in recent years. Defining the risk-adjusted return (RAR) as the bond yield divided by the 1-year rolling standard deviation, 10-year CGBs have a clear RAR advantage over comparable US Treasuries, European Area Government Bonds and JGBs.

Chart 1-10 10-year government bond RAR



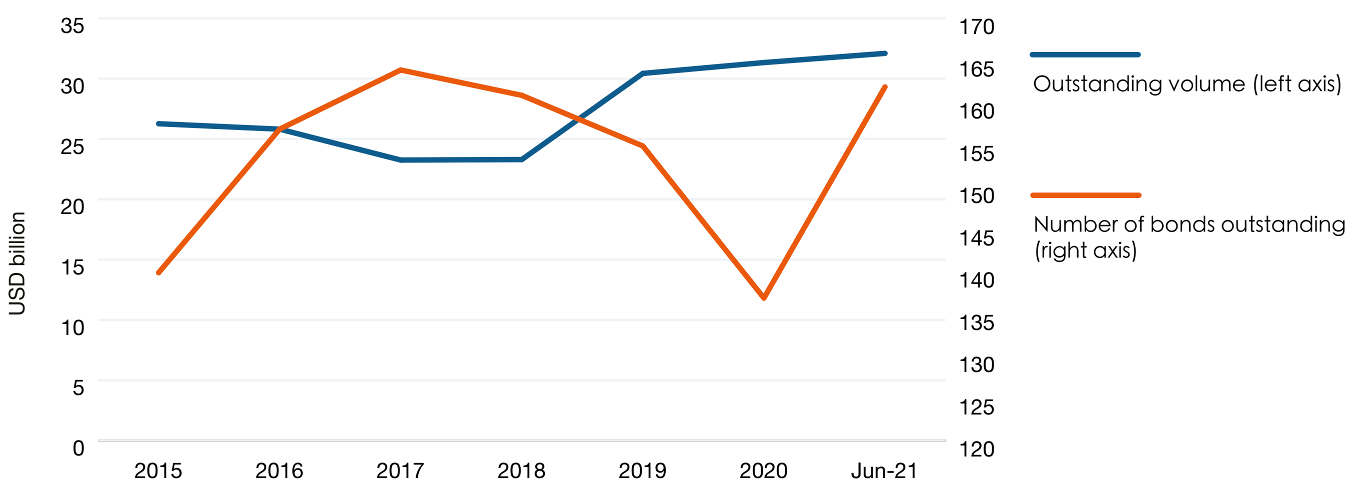
Source: Reuters, Bank of China.

Moreover, RMB bonds are still likely to be less vulnerable to external shocks than other markets.

1.4.1 Market depth

'Dim sum' bonds grew strongly before 2015, when a gap existed between the onshore and offshore markets. As the onshore market opened up, international investors gradually shifted allocations to direct investment in the onshore market, and the dim sum market stabilized in volume since then.

Chart 1-11 Contraction of dim sum bond market



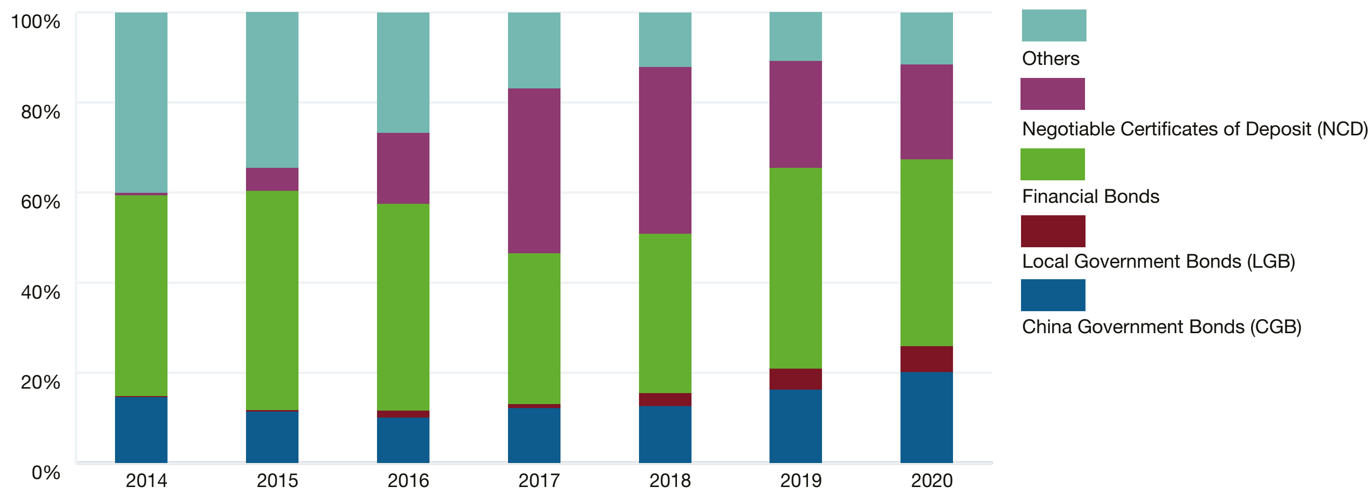
Source: Reuters, Bank of China.

1.4.2 Market liquidity

Assessing liquidity is essential for investors considering whether to enter a new market. The liquidity of China's bond market has been improving.

CGB trading volume was stable and accounts for 15-20% of the total. The proportion of financial bond trading has remained stable around 44% in recent years, while NCD has become one of the most active instruments since 2016.

Chart 1-12 Trading volume across Chinese bond types



Source: Wind, Bank of China.

Chapter 2 - CIBM overview

2.1 Oversight regime

2.1.1 Regulators & self-regulatory organizations

The regulatory authorities of China's bond market are headed by PBC, China Securities Regulatory Commission (CSRC), National Development and Reform Commission (NDRC), and the Ministry of Finance (MoF). Several SROs such as NAFMII, Securities Association of China and National Debt Association of China have also been established to protect investors and support a well-functioning market by setting market standards that promote ethical behaviour and implementing self-disciplinary actions.

As the self-regulatory organization of the Interbank market under the guidance of PBC, NAFMII undertakes the registration and post-issuance supervision of non-financial enterprises debt financing instruments (DFIs). It is also responsible for monitoring trading activities, promoting market innovation, expanding the market's opening to the outside world, and organizing and carrying out market-based evaluation of credit rating agencies and lead underwriters/ underwriters.

Generally speaking, the two lead regulators of the CIBM and the exchange bond market are PBC and CSRC respectively. Bonds that can be issued in both markets such as government bonds (CGBs and LGBs) and enterprise bonds fall within the regulatory oversight of the MoF and NDRC respectively.

In addition, the State Taxation Administration (STA) is responsible for drafting rules and proposing suggestions on tax matters related to bond investment, jointly submitting them to the State Council along with the MoF, and then implementing the measures after approval. The cross-border flow of RMB capital related to bond investment is supervised by PBC, while the cross-border flow of foreign currency capital is supervised by the State Administration of Foreign Exchange (SAFE). Accounting and auditing standards for bond issues are formulated and enforced by the MoF.

China has initiated several key moves to connect the two bond markets (interbank and exchange) in recent years.

1. An inter-ministerial coordination mechanism for corporate credit bonds led by PBC and jointly participated in by CSRC and NDRC has been established. Its role is to strengthen coordination and cooperation among regulators.
2. Approvals for foreign-invested entities to engage in credit rating business in China may permit them to provide ratings on all types of bonds in the CIBM and the exchange market, including financial bonds, corporate credit bonds, structured products and panda bonds.
3. Pilot mutual funds that can be traded on the exchanges and transferred in the CIBM will be launched to better meet investor needs for bond index products.
4. Supported by PBC and NDRC, CSRC is the authority responsible for identifying and punishing illegal activity related to corporate bonds, enterprise bonds, DFLS, and financial bonds in the interbank and exchange bond markets. The Securities Law is the applicable law for defining violations of laws and regulations and penalties for activities including information disclosure, insider trading and market manipulation.

Table 2-1 Oversight regime of China's bond market

<table>
<tr><th rowspan="2"></th><th colspan="2">CIBM</th><th colspan="2">Exchange market</th></tr>
<tr><th>Product</th><th>Supervisor</th><th>Products</th><th>Supervisor</th></tr>
<tr><td rowspan="8">Primary Market</td><td>CGB</td><td rowspan="2">MoF</td><td>CGB</td><td rowspan="2">MoF</td></tr>
<tr><td>LGB</td><td>LGB</td></tr>
<tr><td>Enterprise Bond</td><td>NDRC</td><td>Enterprise Bond</td><td>NDRC</td></tr>
<tr><td>PFB</td><td rowspan="5">PBC (NAFMII takes charge of DFI registration and issuance; CBIRC is the regulator of banking and insurance industries.)</td><td>Corporate Bond</td><td rowspan="5">CSRC</td></tr>
<tr><td>Central Bank Bill</td><td>Enterprise ABS</td></tr>
<tr><td>Financial Bond (Including Credit ABS)</td><td>Convertible Corporate Bond</td></tr>
<tr><td>NCD</td><td>Exchangeable Corporate Bond</td></tr>
<tr><td>DFI (including ABN)</td><td>Private Placement Bonds Issued by Small and Medium-sized Enterprises</td></tr>
<tr><td rowspan="2">Secondary market</td><td colspan="2">Regulated by: PBC</td><td colspan="2">Regulated by: CSRC</td></tr>
<tr><td colspan="2">Self-regulated by: NAFMII</td><td colspan="2">Self-regulated by: Stock Exchanges, Securities Association of China. etc</td></tr>
<tr><td rowspan="3">Market Participants</td><td colspan="2">Regulated by: PBC</td><td colspan="2">Regulated by: CSRC</td></tr>
<tr><td colspan="2">Self-regulated by: NAFMII</td><td colspan="2">Self-regulated by: Stock Exchanges, Securities Association of China.etc.</td></tr>
<tr><td colspan="4">• When granting approval to foreign-invested entities to engage in credit rating business in China, regulators may permit them to provide credit ratings on all types of bonds in the CIBM and the exchange market
• Law enforcement in China's bond market has been unified, with CSRC taking the lead.</td></tr>
</table>

2.1.2 CIBM rules

According to the *Law of the People's Republic of China on the People's Bank of China*, PBC regulates the CIBM and has promulgated relevant departmental rules and regulatory documents to guide the issuance and trading of bonds, including the *Measures for the Administration of Financial Bonds Issuance in the National Interbank Bond Market, the Measures for the Administration of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Bond Market and the Measures for the Administration of Bond Transactions in the National Interbank Bond Market*. In accordance with the Measures for the Administration of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Bond Market, NAFMII organizes market participants in formulating and issuing self-regulatory rules.

In addition, the MoF and NDRC release and implement relevant rules for bonds under their jurisdictions. Other regulators release rules for tax, foreign exchange, accounting and auditing matters related to bond issuance and investment.

2.2 Market infrastructure

With the bond market's growth, China has achieved robust and efficient infrastructures that play a significant role in mitigating risk by connecting issuers, investors, intermediaries and regulators in a close network.

The launch of Bond Connect enhanced the CIBM's mechanism for cross-border transactions, including post-trade arrangements. This expanded the market for Chinese bonds and brought in a new wave of investors.

2.2.1 Overview

The interbank market trading system has been developed by the China Foreign Exchange Trade System &. National Interbank Funding Center (CFETS).The two CSDs, Shanghai Clearing House (SHCH) and China Central Depository & Clearing Co., Ltd. (CCDC), provide central registration, depository, clearing and settlement services for different types of fixed-income products. The trading systems of the exchange market have been developed by Shanghai Stock Exchange and Shenzhen Stock Exchange, while China Securities Depository and Clearing Corporation Limited (CSDC) acts as the CSD. For bonds issued and traded in both markets, CCDC and CSDC have built links to facilitate the transfer of custody.

Table 2-2 China's bond market infrastructure

	Name	Main Functions	Fixed-income Products
CIBM	CFETS	Trade repository, facilitating OTC trading	All fixed-income products in the CIBM, including rate bonds, credit bonds, OTC derivatives, etc.
	CCDC	Registration, depository, clearing and settlement	CGBs, LGBs, PFBs, central bank bills, financial bonds, enterprise bonds, etc.
	SHCH		DFIs, NCDs, credit risk mitigations, etc.
Exchange Market	stock exchange	Facilitating centralized trading and market making	CGBs, LGBs, enterprise bonds, corporate bonds, etc.
	CSDC	Registration, depository, clearing and settlement	

CIBM trading and post-trade process (custody, clearing and settlement) are independent from but integrated with each other. Since the CIBM is an OTC market limited to institutional investors, most transactions are done by bilateral inquiries. FX transactions are carried out by anonymous trading, bilateral inquiries and matched trading, while local currency transactions[3] are carried out by bilateral inquiry, market- making quotation, request for quotation and bilateral matching.

Nominee account structures only apply to transactions through Bond Connect while direct custody is the mainstream in the CIBM. All transactions through Bond Connect are settled on a delivery versus payment (DVP) basis. For other transactions, SHCH operates net settlement or gross trade-by-trade settlement, while CCDC only operates settlement on a gross trade-by-trade basis. The settlement systems of SHCH and CCDC are connected with the Cross-Border Interbank Payment System (CIPS).

2.2.2 Major participants[4]

CFETS

CFETS provides trade, post-trade processing, information, benchmark and training services for the interbank FX market, money market and bond market. Its major functions include providing trading systems, transaction confirmation, transaction unwinding, straight- through processing and market data. In addition, CFETS undertakes daily monitoring of transactions and provides support and service for PBC's monetary policy transmission. It supplies reference prices by publishing market benchmarks, including RMB Central Parity Rate, Shanghai Interbank Offered Rate (SHIBOR), CFETS RMB Index, Loan Prime Rate (LPR), RMB Reference Rate, Bond Indices and yield curves.

3 The interbank local currency market, comprising the money market, bond marketand OTC derivatives market, serves as a platform for financial institutions to manage their liquidity, asset/liability, investment and trade, interest rates and credit risks, as well as a platform for monetary policy transmission.

4 Part of this section refers to the introductions published on the official websites of CFETS, CCDC and SHCH.

Table 2-3 Major participants in the interbank secondary market

<table>
<tr><th>Type of transaction</th><th>Market players</th></tr>
<tr><td>Cash Bond</td><td rowspan="4">Qualified domestic institutional investors including various financial institutions and various types of unincorporated entities, as well as asset managers and custodians of unincorporated products</td></tr>
<tr><td>Bond Repo</td></tr>
<tr><td>Bond Lending</td></tr>
<tr><td>Bond Forward</td></tr>
<tr><td>FRA</td><td rowspan="2">• Financial institutions which are eligible market makers and settlement agencies
• Other financial institutions for their own needs
• Non-financial institutions for hedging purposes</td></tr>
<tr><td>IRS</td></tr>
<tr><td>CRM</td><td>• Primary dealers (financial institutions, credit enhancement agencies, etc.)
• Dealers (unincorporated entities and non-financial institutions)</td></tr>
</table>

Adhering to the goal that market monitoring should be combined with risk management, CFETS has established a service system covering the entire life cycle of bond transactions. It operates and maintains the centralized and transparent OTC e-trading platform, which improves transaction efficiency and reduces costs; it also collects, manages and processes transaction data with the e-trading record system to provide data service for regulators and market participants.

Moreover, CFETS promotes the standardization of its business. This includes formulating three national financial standards – among them, the *Interbank Market Information Exchange (IMIX Protocol)* – as well as participating in the drafting and revision of international financial standards such as ISO 20022.

Shanghai Clearing House (SHCH)

SHCH was established to implement G20 initiatives on strengthening the regulation of the OTC derivatives market. As the world's second CCP founded after the 2008 global financial crisis (and the first in Asia), SHCH's main business includes registration, custody, clearing, settlement, delivery, margin management and collateral management for direct and indirect RMB and foreign currency transactions and derivatives transactions.

SHCH has established a CCP clearing service system of international standards covering bonds, interest rate derivatives, FX derivatives, credit derivatives and commodity derivatives. It provides CCP clearing service for bond transactions, cross-border FX transactions, RMB IRS, standardized bond forward, credit default swap and other derivatives. As a CSD, SHCH has provides depository, settlement, information disclosure, interest payment, and collateral management services for bonds.

CCDC

Under the MoF's regulation of the CGB market, CCDC is the authorized master depository for CGBs and is responsible for the establishment and operation of the CGB depository system. PBC's bond market regulation makes CCDC the CSD in the CIBM, as well as the primary depository for commercial bank book-entry government bond transactions. In addition, CCDC is acknowledged by NDRC as the master depository for enterprise bonds.

CCDC's business scope covers, depository, settlement, interest payment and information disclosure, as well as some value-added services.

2.3 Investing in Chinese bonds

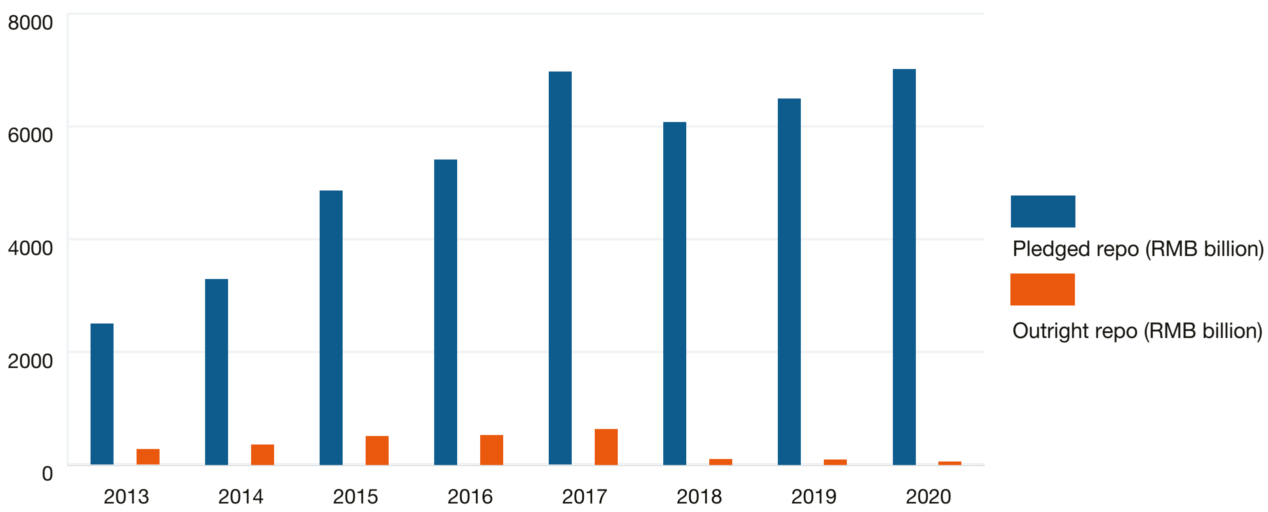
2.3.1 Wide range of bond varieties

Repo market

Bond repo is certainly an important liquidity management tool in the fixed income world. There are two types of repo transactions in the Chinese market, just like other markets, pledged repo and outright repo. In pledged repo the bondholder (the repurchase party) pledges the underlying bonds to the lender and gets them back shortly afterwards by paying interest and principal at an agreed price on a future date. In outright repo the bondholder (the repurchasing party) sells the underlying bonds to the purchaser (the reverse repurchase party) and buys them back shortly afterwards at an agreed price on a future date. The distinction between the two is that pledged repo does not shift ownership of the bond, whereas outright repo does.

However, in contrast to international market practice, pledged repo is the most popular form in China. In 2020, the trading volume of pledged repo increased 18% YoY to 953 trillion yuan, leaving a minimal market share for outright repo. The outstanding amount of pledged repo in the end of 2020 was around 7 trillion yuan while the amount of outright repo was only 55 billion yuan. The most actively traded tenors are overnight (O/N) and 7-day, which together account for more than 96% of total repo trading.

Chart 2-1 Repo outstanding amount in the CIBM (unit: billions of RMB)



Source: Wind, Bank of China.

Rate bonds and credit bonds

Chinese bonds can be broadly divided into rate bonds and credit bonds.

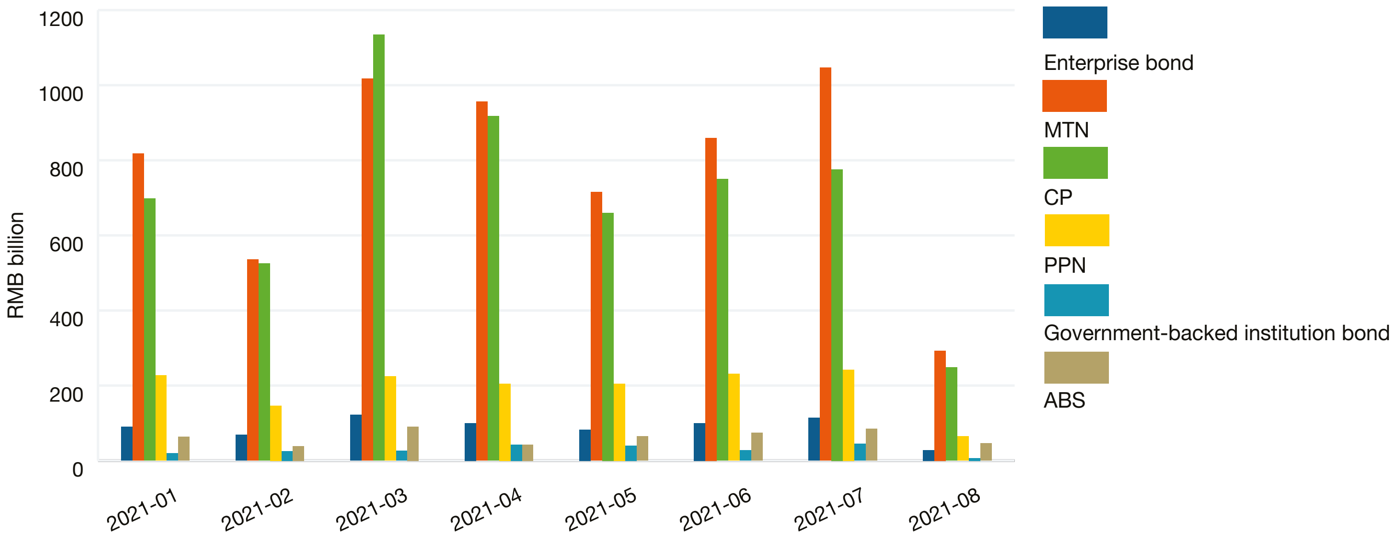
Rate bonds are issued by entities with almost no credit risks for onshore investors, including CGBs, LGBs and PFBs[5].

In contrast, credit bonds are issued by entities that carry credit risks, including financial bonds, non-financial enterprise debt financing instruments (DFI), enterprise bonds, corporate bonds and so on. DFIs includes CP, SCP and MTN and they differ in tenors. The longest term for CP is about 365 days, while for SCP the maximum is about 270 days. MTNs usually mature in 1-5 years, but do not have any limits on maximum tenor.

5 Financial policy banks (China Development Bank, China Export and Import Bank and China Agricultural Development Bank) are assigned credit ratings almost equal to China's sovereign rating (rating of the central government), so PFBs are defined as rate bonds.

Private placement notes (PPNs) are targeted at limited groups of investors. PPN investors are divided into Specialized Institutional Investors and Designated Institutional Investors; enterprises can opt to issue PPNs to both categories or Designated Institutional Investors only.

Chart 2-2 Monthly trading volume of various credit bonds



Source: Wind, Bank of China.

Table 2-4 Bond comparison

Products	Tax	Liquidity	Market Share (%)	Average Ticket Size (millions of RMB)	Tenor
CGB	Exempt	Excellent	17.37	50-100	3m-50y
LGB	Exempt	Acceptable	22.78	100	1-30y
PFB	Income Tax & VAT	Excellent	16.03	50-100	6m-30y
NCD	Income Tax & VAT	Excellent	10.20	50-100	3,6,9,12m
Commercial Bank Note	Income Tax & VAT		5.18	—	2-15y
ABS	Income Tax & VAT		3.94	—	—
CP&SCP	Income Tax & VAT		1.83	100	<1y
MTN	Income Tax & VAT		6.33	50	1-30y
Corporate Bond	Income Tax & VAT		7.79	30-50	3-30y
Enterprise Bond	Income Tax & VAT		1.84	30-50	5-10y

2.3.2 Liquidity & turnover

Liquidity varies among different types of bonds. Rate bonds are generally more liquid than credit bonds. CDB's are the most liquid rate bonds, especially in the 10-year tenor maturity where issues are frequent and in substantial size with a more diversified investor base. Its liquidity premium over other PFBs is some negative 6bp.

As the most liquid credit bonds, NCDs are mostly issued at discount. Single issues normally amount to RMB 50 million or even more. DFIs such as CP, SCP and MTNs are also deemed to be liquid assets as their tenors are usually shorter than 3 years.

Enterprise bonds and corporate bonds are traded in a less dynamic way, and their liquidity depends heavily on the issuers' credit.

Table 2-5 CIBM turnover ratio

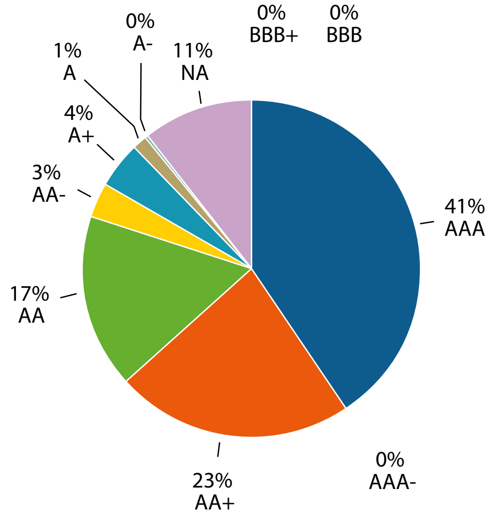
Turnover Ratio	2020	2019	2018	2017	2016	2015
CGB	2.79	1.67	1.26	0.89	1.04	0.90
LGB	0.64	0.38	0.24	0.06	0.19	0.06
NCD	4.53	4.49	5.55	4.48	3.13	1.39
PFB	4.18	3.48	2.58	1.78	3.48	2.88
Enterprise	0.56	0.61	0.61	0.87	2.22	2.15
MTN	1.72	1.23	1.31	1.30	2.38	2.22
CP&SCP	5.02	3.98	3.64	4.26	6.64	4.85
PPN	1.12	0.71	0.48	0.24	0.00	0.00

Source: Wind, Bank of China.

Credit rating distribution[6]

At the end of 2020, 41% of Chinese credit issuers were rated AAA and 17% were rated AA. As this distribution is different from the overseas market, where investors recognize BBB-(international rating) as the threshold for investment grade, some domestic investors define AA+ as their standard for investment grade instead.

Chart 2-3 Credit rating of issuer distribution in China's bond market by number of bonds



Source: Wind, Bank of China.

6 Credit ratings mentioned in this book are Chinese domestic ratings, unless other wise specified.

Liquidity screening

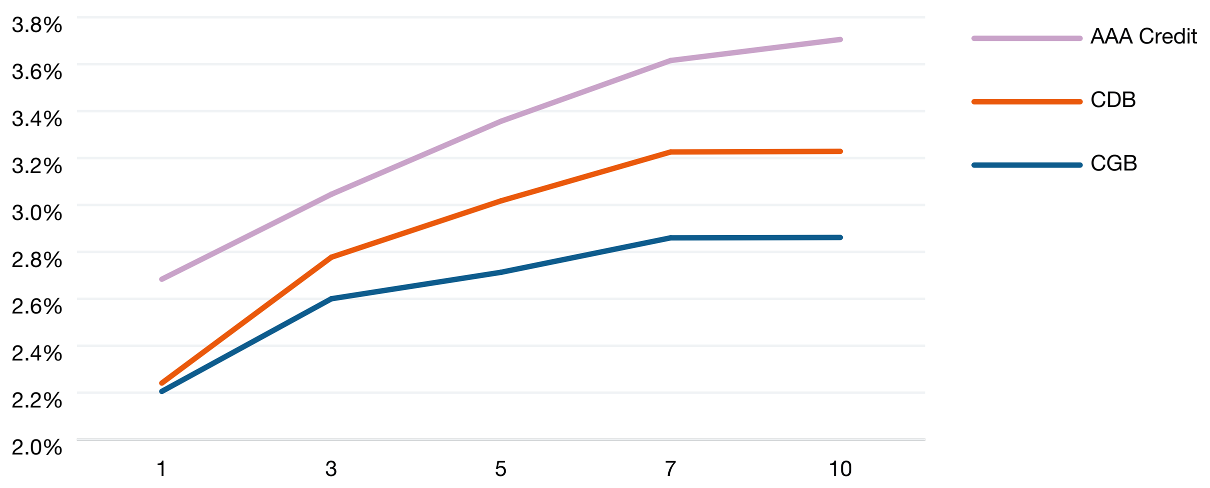
1. Trading volume

In 2020, Chinese bond trading volume increased 10.4% YoY to RMB 234.867 trillion. with an average daily turnover of RMB 939.0 billion.

2. Curve shape

Short-dated CIBM bonds normally yield less than bonds of the same credit quality at the long end, giving the curve an upward slope. Investors usually expect more compensation for greater long-end risk from changes in interest rates and increased exposure to potential defaults. However, sometimes the yield of 10-year CDB drops below the 7-year tenor because of liquidity premium (10-year bonds are much more liquid than 7-year bonds in a bullish environment resulting in lower yields).

Chart 2-4 Yield curve of CGBs, CDBs and AAA-rated credit bonds (Aug 31, 2021)



Source: Wind, Bank of China.

1. Main drivers

The short end of the CIBM yield curve tends to be influenced by money market liquidity and monetary policies. Short-term rates usually rise when PBC tightens money market liquidity and fall when liquidity is loosened.

Meanwhile, the long end of the curve is usually affected by market expectations for inflation, economic growth, supply and demand and investors' risk appetite. Generally speaking, higher inflation, faster growth, and elevated risk appetites cause the yields in the long end to rise. Conversely, mild inflation, slower growth, and depressed risk appetites cause yields in the long end to fall.

2. Index inclusion

Chinese RMB-denominated rate bonds have been included in the Bloomberg Barclays Global Aggregate Index, Global Treasury and EM Local Currency Government Indices since April 2019 and the J.P. Morgan Government Bond Index - Emerging Markets since February 2020, while Chinese Government Bonds will be included in the FTSE World Government Bond Index starting from October 2021.

Index inclusion is strategically important for the opening of China's bond market. Analysts estimate that it will lead to significant inflows to the CIBM. It may also promote the development of risk management instruments as overseas investors have substantial demand for hedges against FX, interest rate and credit risks. Inclusion is also likely to drive innovations such as passive investment among domestic investors.

2.4 Risk management

2.4.1 Interest rate risk

Interest rate risk is the risk of unexpected interest rate changes. Besides diversifying portfolios, investors in the CIBM also employ bond lending, interest rate swaps (IRS) and CGB futures to hedge interest rate risk.

In a bond lending transaction, the borrower receives a loan of bonds by using its own portfolio of bonds as collateral and paying a bond lending fee quoted at an annual interest rate. Later, on an agreed date, the borrower returns the bonds and receives its collateral back. The term of bond lending is determined by negotiation, with a minimum of one day and a maximum of 365 days.

Bond lending is a tool that enables borrowers to sell bonds short by covering their temporary demand for bonds. It also helps bond lenders to revitalize bonds in their possession and gain profits, thus improving trading efficiency. According to Wind data, 2020 saw RMB 7.46 trillion of bond lending, with CGBs, LGBs and PFBs the main bond types used.

As the most popular interest rate derivative in the CIBM, interest rate swaps (IRS) are contracts in which two parties agree to exchange cash flows based on a specified principal amount to manage interest rate risk. IRS usually involve the exchange of a floating interest rate for a fixed rate, or vice versa, to reduce or increase exposure to fluctuations in rates. The reference rates for onshore IRS include FR007 (7-day Fixing Repo Rate), Shibor_3M (3-month Shanghai Interbank Offered Rate), SHIBOR O/N (Overnight Shanghai Interbank Offered Rate), Depo_1Y (1-year bank deposit rate), LPR (Loan Prime Rate) and FDR007 (7-day Fixing Depository-Institutions Repo Rate), of which FR007 is the most actively traded. 1 and 5-year swaps are the most actively traded.

Table 2-6 Trading share of IRS with different tenors/underlyings

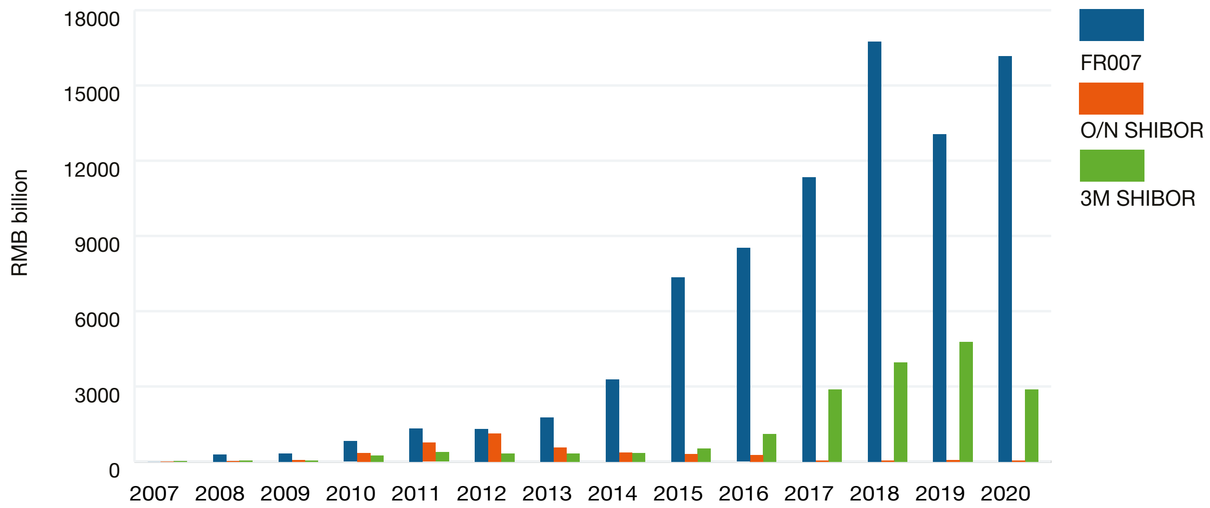
Tenors	Trading share (%)	Reference rates	Trading share (%)
≤1y	63.8	FR007	84.7
1y-5y	6.9	SHIBOR	14.9
≥5y	29.3	Others	0.4

Source: Wind, Bank of China.

Since China officially launched RMB IRS in February 2006, the market has flourished with increasing efficiency and a broader set of market participants. All standard RMB IRS in the CIBM are subject to centralized clearing in SHCH, and CFETS provides trade offsetting services while SHCH offers trade compression services.

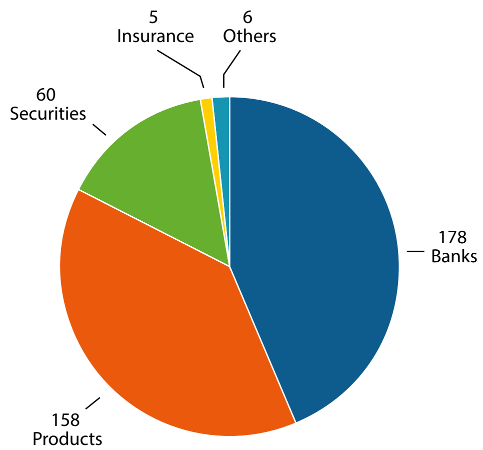
In 2020, according to PBC's statistics, IRS trading volume has reached 19.6 trillion yuan, a rise of 7.8% on YoY. IRS with 1Y or tenor below are the most active, accounting for 63.8% market share. The main reference rate is FR007 and SHIBOR 3M is the second most active reference rate.

Chart 2-5 IRS Trading Volume



Source: Wind, Bank of China.

Chart 2-6 IRS market participants (Jun 2019)



Source: Wind, Bank of China.

The main purpose of IRS is to reduce the cost of funds (i.e. interest rates) for both parties and enable them to obtain the interest payment method they need (fixed or floating). The economic value of the IRS for both trading parties should be zero at the initial stage of the contract. Over time, if interest rates fall and stay lower than expected, the receiver of the fixed leg will earn profits. If interest rates rise and stay higher than expected, the fixed receiver will suffer losses.

Similar to cash bonds, the short end of IRS yields are greatly affected by changes in money market liquidity, while inflation and macroeconomic conditions are the main drivers for the long end. However, IRS demonstrates some differences compared with cash bonds. For one thing, changes in IRS yields are closely related to money market liquidity as the reference rates of IRS are all money market base rates. For another, IRS is more efficient and sensitive with its standardized structure and non-principal settlement.

Key IRS trading strategies include directional trading, carry and roll-down, curve spread and basis spread strategies.

Interest rate options have been launched in the CIBM, including interest rate swap options and interest rate cap options, both linked to LPR. Although interest rate options are in the early stage of development, it is expected that relevant products will be enriched and the market will be further opened up, and interest rate options may help market players including overseas investors to better hedge risks, diversify arbitrage strategies and refine hedging tools.

2.4.2 Credit risk

Credit default swap (CDS) is one of the most widely used tools in managing credit risk and capital in advanced markets. In 2010, NAFMII introduced two similar products called Credit Risk Mitigation Agreement (CRMA) and Credit Risk Mitigation Warrant (CRMW) in CIBM. As their names imply, CRMW is a warrant that allows the investor to transfer a specific credit risk to the seller, while CRMA is a derivative contract in which the seller promises to compensate the buyer in the event of a default or other credit events. Both CRMW and CRMA can only insure against a specific reference asset.

In 2016 NAFMII released the Rules for the Pilot Program of *Interbank Market Credit Risk Mitigation Instruments, Guidelines on the Issuance of Credit-Linked Note, Guidelines on the Issuance of Credit Default Swap and Basic Terminologies and Applicable Rules for Credit Derivatives Trading in China's OTC Market*, introducing CDS and CLN that may insure against an array of reference assets. Although the trading activity and outstanding volume of Chinese credit derivatives is not yet substantial, the increasing involvement of financial institutions in the market makes a more dynamic market likely in the future.

2.4.3 Currency risk

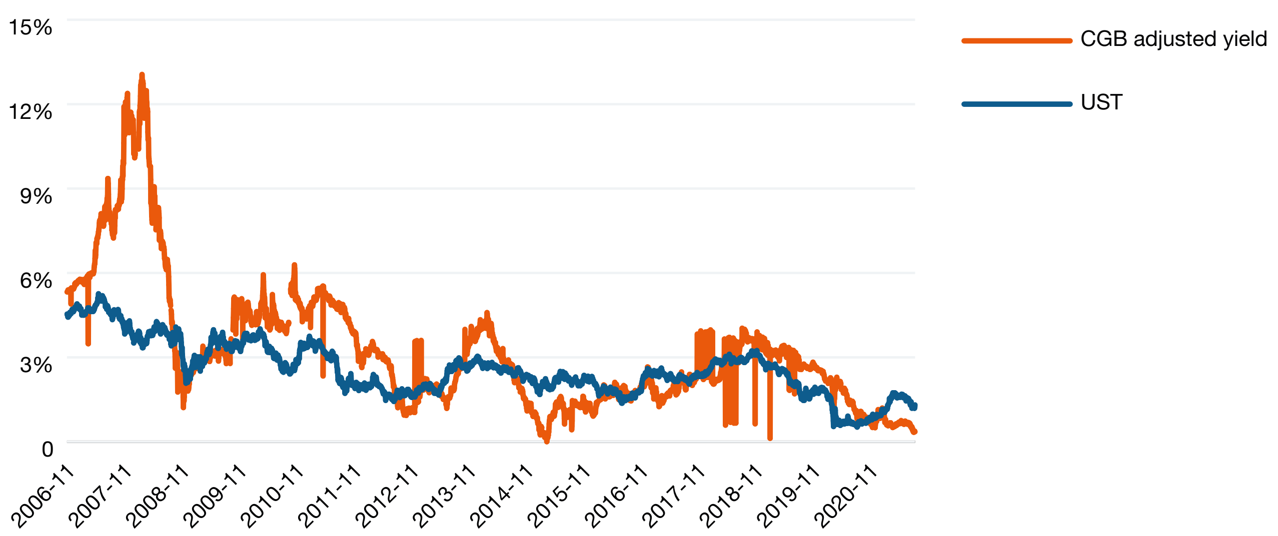
FX trading requirements for overseas institutional investors

Table 2-7

Higher yields than global peers

As RMB has been relatively stable against G7 currencies, many overseas investors in onshore bonds have chosen not to hedge their FX risks. Even with FX risk fully hedged (using a 12-month onshore swap, for example), CGBs can still provide a pick-up over alternatives.

Chart 2-7 Yield comparison between 10-year CGB and UST



Source: Bloomberg, Bank of China.

Chapter 3 - CIBM's opening-up

3.1 Rapid development

CIBM has experienced rapid growth since its establishment in 1997, becoming the main board of China's bond market. The market is open to international issuers and international investors.

Foreign government agencies, international development institutions, overseas financial institutions and non-financial enterprises are all allowed to issue panda bonds in the CIBM. As panda bond rules continue to improve and align with international rules, the market has grown in size dramatically. Panda bond issuance reached RMB 53billion in 2020, a year-on-year increase of 12.2%.

The first batch of overseas investors entered the CIBM in 2005. In August 2010 PBC issued the *Notice on Issues concerning the Pilot Program on Investment in the Interbank Bond Market with RMB Funds by Three Types of Institutions Including Overseas RMB Clearing Banks*; the RMB Qualified Foreign Institutional Investors (RQFII) regime was introduced in November 2011; in March 2013 Qualified Foreign Institutional Investors (QFII) were allowed to invest in the CIBM under a quota system.

Table 3-1 Incremental opening-up to overseas investors

Stage	Time	Event	Relevant Rules
Early stage of opening-up	2005	PBC approved the Pan- Asian Fund and ABF China to enter the CIBM.	
	August 2010	Pilot of three types of overseas institutions to invest in the CIBM was launched.	Notice of People's Bank of China on Issues concerning the Pilot Program on Investment in the Interbank Bond Market with RMB Funds by Three Types of Institutions Including Overseas RMB Clearing Banks
	November 2011	RQFII was brought in and allowed to invest in the CIBM.	
	March 2013	QFIIs allowed to invest in the CIBM within quotas.	Announcement of the People's Bank of China and the State Administration of Foreign Exchange in Domestic Securities Investment of Qualified Foreign Institutional Investors
Accelerating stage of opening-up	June 2015	Overseas RMB business clearing banks and overseas participating banks were allowed to conduct bond repurchase transactions in the CIBM.	Notice concerning the Bond Purchase Transactions in the Interbank Bond Market by the Overseas RMB Clearing Banks and Overseas Participation Banks
	July 2015	For overseas central bank institutions to simplify the process of entering the market, the review system was changed to the filing system and the quota limit was abolished. They were allowed to independently choose PBC or interbank market settlement agent to settle their agent transactions The range of products that they are allowed to invest was also broadened.	Notice on the Relevant Issues concerning the Investment in the CIBM with RMB Funds by Foreign Central banks, International Financial Institutions and Sovereign Wealth Funds
	February 2016	The medium and long- term overseas institutional investors recognized by PBC were allowed to invest in the CIBM without quota limits.	People's Bank of China Announcement [2016] No. 3
	June 2016	Overseas financial institutions were allowed to invest in interbank NCDs	Interbank Market Trading Rules of Negotiable Certificates of Deposit

Stage	Time	Event	Relevant Rules
Accelerating stage of opening-up	July 2017	Bond Connect was opened ('Northbound') for investment into CIBM.	Interim Measures for the Administration of Mutual Market Access between Mainland China and Hong Kong Bond Markets
	November 2017	All kinds of overseas institutional investors were allowed to conduct cash bond trading in the CIBM and can conduct bond lending, bond forwards, forward rate agreements and interest rate swaps based on their hedging needs. Overseas RMB business clearing banks and participating banks can also conduct bond repurchase transactions in the CIBM.	Procedures of Entering the Interbank Bond Market for Overseas Commercial Institutional Investors
	June 2018	20% ratio limit on the remittance of QFII/RQFII funds and the requirement of the principal lock-up period were canceled and foreign exchange risk hedging of domestic investment of QFII/ RQFII funds was allowed.	Administration Rules on the Domestic Securities Investment in Foreign Exchange by Qualified Foreign Institutional Investors Circular of People's Bank of China and the State Administration of Foreign Exchange on the Domestic Securities Investment of RMB Qualified Foreign Institutional Investors
	August 2018	The executive meeting of the State Council decided to temporarily exempt corporate income tax and value-added tax on bond interest income from overseas institutions investing in the domestic bond market within three years.	MoF and STA Notice on the Policy of Enterprise Income Tax and Value- added Tax Relating to Overseas Institutional Investors' Investment in the interbank Bond Market
	September 2019	With the approval of the State Council, SAFE decided to cancel the limit of QFII and RQFII investments.	SAFE: Cancel QFII/RQFII Investment Limit and Expand the Opening of Financial Market
	October 2019	The transfer of CIBM bonds and cash of a single foreign institutional investor between its accounts opened under the regime of QFII/ RQFII and the CIBM Direct regime is allowed to be executed. Also a single foreign institutional investor may do the filling once for QFII/RQFII or CIBM direct regime to enjoy access under both regimes.	the Circular of the People's Bank of China and the State Administration of Foreign Exchange of Matters Relating to Further Facilitating Investment of Foreign Institutional Investors in the Interbank Bond Market
	November 2019	To facilitate the foreign exchange risk management of the foreign institutions' bond investments, they may participate in the onshore FX market.	Circular on Improving the Foreign Exchange Risk Management of Foreign Institutional Investors in the Interbank Bond Market (Consultation Papers)
	July 2020	PBC and CSRC gave their approval to undertaking interlinked and interconnected cooperation between the relevant infrastructure institutions of the interbank bond market and exchange bond market	People's Bank of China, China Securities Regulatory Commission Announcement ([2020] No. 7)
	September 2020	SAFE cancelled investment quota limit of qualified overseas institutional investors (QFII) and RMB qualified overseas institutional investors (RQFII)	
	September 2020	The investment scope of QFIs was expanded. The eligibility requirements for QFIs were relaxed. The corresponding compliance obligations applicable to QFIs were also reinforced	Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors (QFII) and RMB Qualified Foreign Institutional Investors (RQFII)

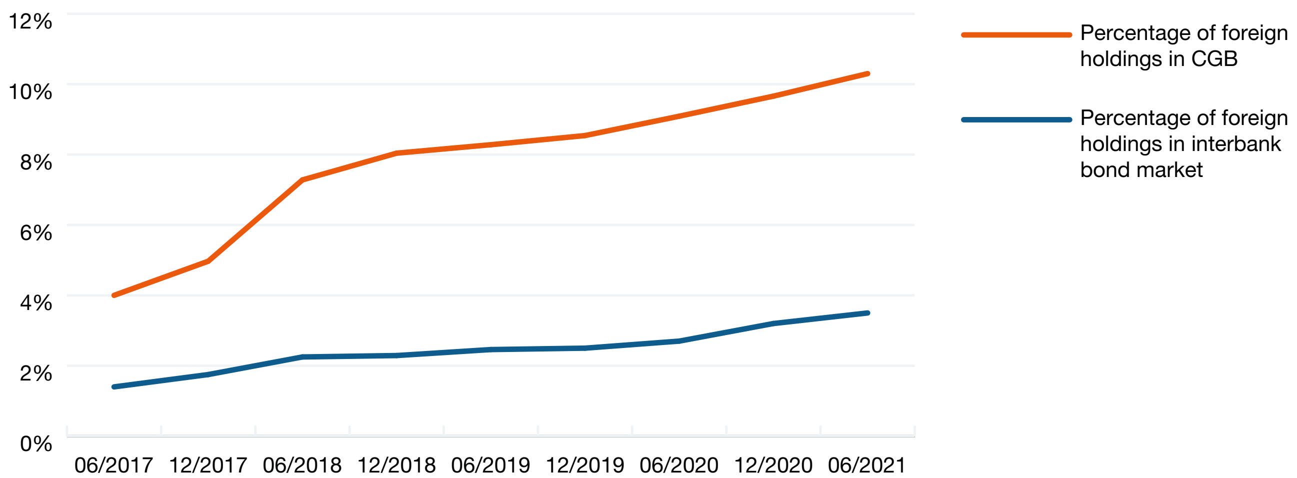
Source: according to public information

Since 2015 China has adopted policies to accelerate the CIBM's opening. In 2015 restrictions on overseas investors' involvement in repo transactions were partially relaxed allowing two types of overseas investors, introducing new RMB liquidity management tools. In July 2015 market entry procedures for overseas central banks, international financial organizations and sovereign wealth funds were simplified and the quota limit removed. In February 2016 CIBM Direct was broadened further for medium and long-term overseas institutional investors.

The launch of Bond Connect in 2017 provided greater convenience for overseas investors and the scope of investable products was expanded. In 2018 major improvements in cross-border capital flow and taxation included the cancellation of the QFII/RQFII remittance limit and the principal lock-up period, as well as the temporary tax exemption of the interest income earned by overseas investors till November 2021. In September 2019 PBC and SAFE issued the Circular of the People's Bank of China and the State Administration of Foreign Exchange of Matters Relating to Further Facilitating Investment of Foreign Institutional Investors in the Interbank Bond Market, allowing foreign institutional investors to transfer CIBM bonds and cash between their own QFII/ RQFII and CIBM Direct accounts. In September 2020, SAFE cancelled investment quota limit of qualified overseas institutional investors (QFII) and RMB qualified overseas institutional investors (RQFII) as it announced a year previously.

These efforts have expanded international institutions' role in China's bond market significantly. The proportion of bonds held by overseas investors has increased from 1.4% at the end of June 2017 to 3.5% at the end of June 2021. Moreover, foreign ownership of CGBs has increased from 4.0% to 10.3%.

Chart 3-1 Overseas investors have been playing an active role in China's bond market



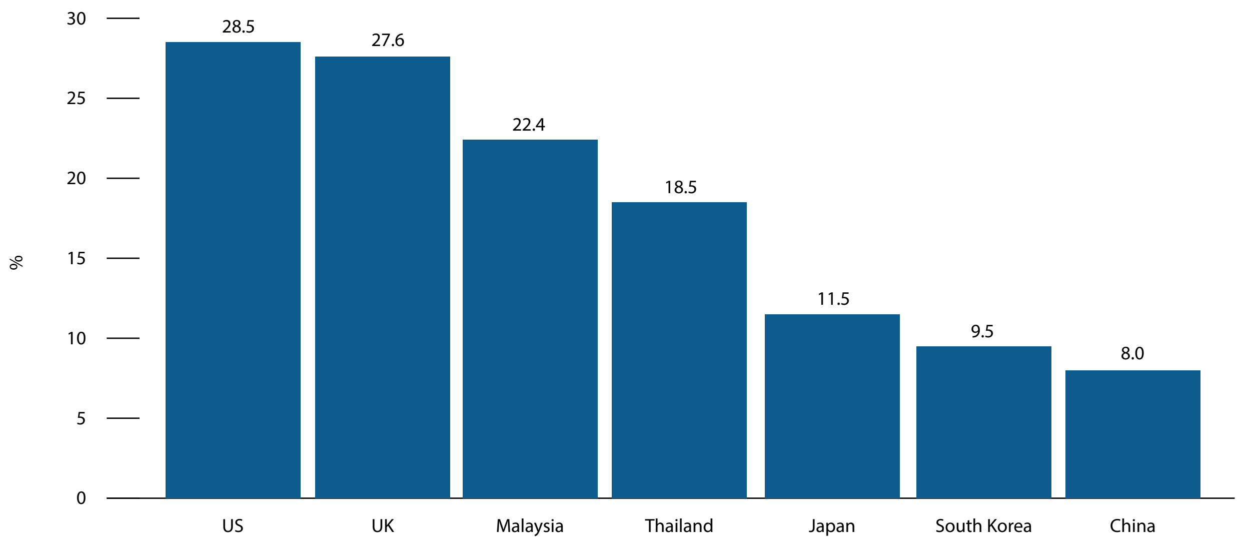
Source: CEIC, PBC.

In addition, some foreign-funded financial institutions have been involved in secondary market trading activities. JP Morgan (China), Citibank (China), Standard Chartered (China) and others have acted as market makers in the CIBM. HSBC (China), Citibank (China), Deutsche Bank (China), Bank of Tokyo-Mitsubishi UFJ (China), Mizuho (China), Standard Chartered (China), BNP Paribas (China), DBS (China), JP Morgan (China) and Bank of America (China) have become quotation banks under Bond Connect.

In February 2019 the Chinese subsidiary of Standard & Poor's became the first foreign-funded credit rating agency allowed to conduct business in the CIBM. This represented substantial progress for China's credit rating industry in opening up to the outside world. In May 2020, Fitch (China) Bohua Credit Ratings entered the Chinese interbank bond market as the second wholly foreign-owned credit rating agency.

The CIBM's continuing opening – part of the long-term opening-up trend in China's financial sector – will have far-reaching effects on bond market infrastructure, trading rules and trading activity. While the internationalization of China's bond market is still far below that of developed countries and even some emerging economies, there is significant potential for more international participation. At the end of 2018 overseas investors only accounted for 8% of holdings in China's treasury bond market, compared to around 10%, 20% and 30% in Japan/Korea, Malaysia/ Thailand and the US/UK, respectively.

Chart 3-2 Percentage of overseas holdings in their government bond markets across countries, as of end of 2018



Source: Wind, China Merchants Securities.

3.2 Panda bonds

RMB bonds issued by overseas issuers in China's bond market are called panda bonds. This instrument is an important component of China's opening-up of its financial markets. Its emergence broadens the opportunities for international borrowers, who benefit from an efficient and transparent issuance mechanism, to finance operations and optimize their debt structure. It also provides new options for overseas investors to allocate capital and diversify RMB asset portfolios.

3.2.1 Overview

In 2005 international development institutions were allowed to start issuing RMB bonds in the CIBM for the first time. The International Finance Corporation (IFC) and Asian Development Bank (ADB) issued panda bonds of RMB 1.1 billion and RMB 1 billion, respectively.

Since restarting in 2014, the market has expanded its issuers to non-financial enterprises, financial institutions and government agencies. In 2014 Daimler issued panda bonds in the CIBM, becoming the first overseas non-financial enterprise issuer.

In September 2015 HSBC and Bank of China (Hong Kong) issued financial panda bonds, followed by Korea issuing sovereign panda bonds in December of the same year.

Subsequently, the market has expanded steadily. A host of positive factors have supported this, including the implementation of the 'Belt and Road Initiative', the RMB's inclusion in the International Monetary Fund (IMF)'s Special Drawing Rights (SDR) currency basket, and the Chinese currency's further internationalization.

Since 2018 panda bond rules have been clarified, making the market more attractive. In September 2018 PBC and MoF jointly issued the *Interim Measures for the Administration of Bonds Issued by Overseas Issuers on the National Interbank Bond Market* (Measures). NAFMII issued the *Guidelines on Debt Financing Instruments of Overseas Non-Financial Enterprises* in early 2019 and amended it in 2020. Guidelines on Bond Issuance by Foreign Governmental Agency and International Development Institution Issuers (for Trial Implementation) is also issued in 2020.

Table 3-2 Milestones in the development of panda bond market

Date	Events
2005	• The Interim Measures for the Issuance Administration of RMB Bond by International Development Institutions was issued • International development institutions issued RMB bonds for the first time in China
2014	• The first panda bond of a non-financial enterprise was issued
2015	• The first panda bond of a financial institution was issued • The first panda bond of a foreign government agency was issued
2016	• The first SDR-denominated bond was issued • RMB was included in IMF SDR basket
2018	• PBC and MoF released the *Interim Measures for the Administration of Bonds Issued by Overseas Issuers on the National Interbank Bond Market, and officially abolished the Interim Measures for the Issuance Administration of the RMB Bonds by International Development Institutions*.
2019	• NAFMII issued the *Guidelines on Debt Financing Instruments of Overseas Non-Financial Enterprises*
2020	• NAFMII Issues Detailed Rules for the Administration of Tiered Management of Debt Financing Instruments of Overseas Non-Financial Enterprises and Form Requirements for Registration Documents for Debt Financing Instruments of Overseas Non-Financial Enterprises. • NAFMII Issues Guidelines on Bond Issuance by Foreign Governmental Agency and International Development Institution Issuers (for Trial Implementation). • NAFMII Issues Guidelines on Debt Financing Instruments of Overseas Non-Financial Enterprises (2020).

3.2.2 Current status

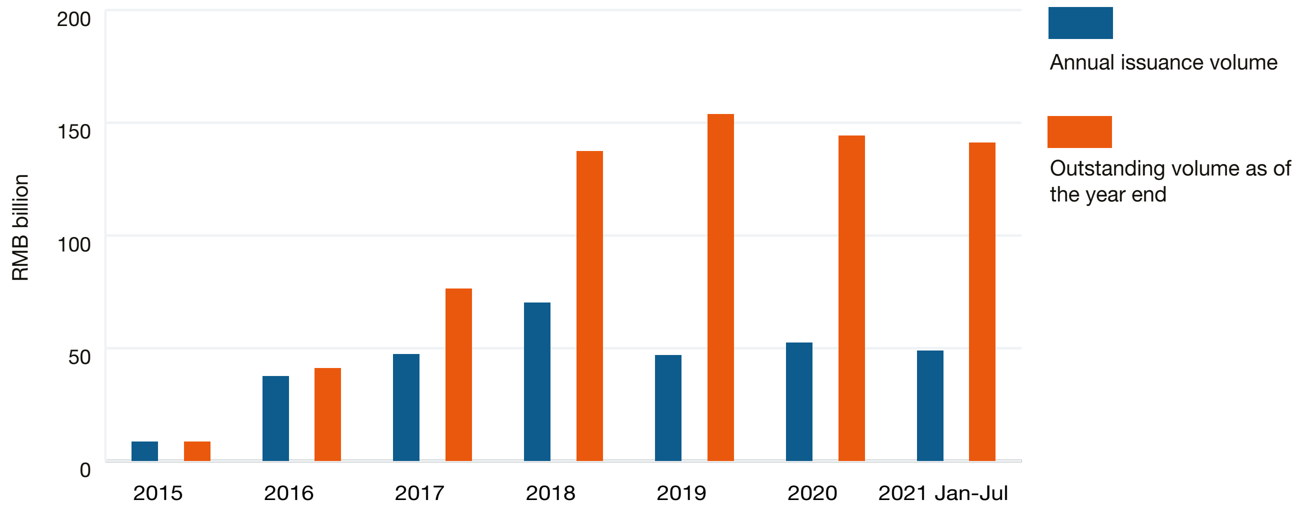
The panda bond market has established comprehensive rules and regulations. PBC and MoF's Measures clarify the requirements and procedures for panda bond issuance, and provide rules for information disclosure, issuance registration, custody, settlement, account opening, and investor protection, etc. The Measures classify panda bond issuers into foreign government agencies, international development institutions, financial institutions and non-financial enterprises. Among them, overseas financial institutions issuing bonds in the CIBM are subject to PBC's approval. Foreign governmental agencies, international development institutions and non-financial enterprises must register with NAFMII for bond issuance.

The Guidelines issued by NAFMII set out rules for information disclosure, use of proceeds, and intermediaries related to panda bond registration and issuance.

These rules and regulations have clarified several important issues, including accounting standards, eligibility of overseas auditing firms, required disclosures, use of proceeds and code of conducts of relevant intermediaries. Non-Chinese accounting standards are allowed but may be subject to more disclosure requirements. Overseas accounting firms are allowed to practice after filing with the MoF. The proceeds can be used within or outside PRC in accordance with applicable laws, regulations and regulatory requirements. Account opening, cross-border settlements, and information reporting related to the proceeds must be incompliance with PBC and SAFE rules.

The panda bond market has expanded steadily in recent years, with issuers and maturities diversifying. By July 2021, a total of 56 overseas issuers (43 overseas non-financial enterprises 4 international development institutions and 9 overseas government agencies) had completed panda bond registration with NAFMII and successfully issued 184 bonds amounting to RMB 313.95 billion, with the outstanding volume reaching RMB 141.24billion.

Chart 3-3 Registration and issuance of panda bonds registered with NAFMII (2015-2021.7)



Source: NAFMII

Non-financial enterprise panda bond issuers include members of the world's top 500 companies such as Air Liquide, Daimler, Trafigura and Veolia, as well as 'red-chip' companies such as China Merchants Group, CLP New Energy and SMIC. Panda bonds support the development of many industries such as chip manufacturing, environmental protection, automotive, ports, pharmaceuticals, power, warehousing and logistics, and transportation. Foreign government issuers include the Province of British Columbia, South Korea, Poland, Hungary, Emirate of Sharjah, the Philippines and Portugal. International development institutions include the World Bank and New Development Bank. Financial institutions include major international banks such as HSBC, Standard Chartered and National Bank of Canada.

Table 3-3 Registration and issuance of panda bonds in the CIBM

Type of issuers	Issuing volume (RMB billion)	Outstanding volume (RMB billion)	Number of issuances
International Development Organization	22	18	11
Government Agency	21	18	10
Financial Institution	36	13	20
Non-financial Enterprise	278	108	168
Total (RMB-denominated bonds)	357	156	209
World Bank	5 (500 million SDR)	0 (500 million SDR)	1
Standard Chartered Bank (HK)	1 (100 million SDR)	0 (100 million SDR)	1
Total in RMB (RMB and SDR dominated bonds)	363	156	211

Note: as of the end of July 2021.

Foreign non-financial enterprises may choose the tenor and type of bond according to their own financing needs, in accordance with NAFMII's requirements for information disclosure. Panda bonds issued by non-financial enterprises include CP, MTNs, SCP, green bonds and PPNs, with maturities ranging from 270 days to 10years.

The market has met diverse financing needs. To support the 'Belt and Road' initiative, a number of foreign government agencies, international development institutions, overseas enterprises and financial institutions that facilitate infrastructure connectivity have issued panda bonds. To support the development of environmentally-friendly industries, overseas enterprises have issued green panda bonds to fund energy conservation and clean energy projects; some have adopted the 'SPV (financing vehicle) with parent company guarantee' structure commonly seen in the international market.
New Development Bank raised a Sustainable Development Goals (SDG) panda bond which is supported by NDB's Environmental and Social Framework and issued with reference to the UNDP Sustainable Development Goals Impact Standards for bonds and the SDG Finance Taxonomy (China). BMW Group became the first European panda bond issuer to issue medium-term notes and commercial paper which features higher information disclosure requirements for issuers and larger potential buyer pools.

The market is increasingly attracting overseas investors. Overseas investors can invest in panda bonds in the CIBM through Bond Connect and other channels. When Hungary issued panda bonds through Bond Connect in July 2017, this marked the first time in China that overseas investors subscribed for more than half (55%) of a single tranche of a bond. In March 2018 the Philippines' RMB bonds through Bond Connect were 6.3 times over-subscribed and 88% was allocated to overseas investors. The Asian Infrastructure Investment Bank (AIIB)'s inaugural panda bond in 2020 was 2.78 times oversubscribed by more than 20 investors with 65% allocated to international investors.

3.2.3 Attractions for international investors

RMB asset allocation. Panda bonds provide a new choice for overseas investors to allocate RMB assets. Denominated in RMB, the instrument adds to their options for diversifying portfolios.

Higher returns. With yields in most major global markets very low, China's bond market offers attractive yields.

Familiar issuers. Overseas investors are more likely to invest in familiar international names active as panda bond issuers.

3.3 Credit ratings

Prior to 2017 the 'credit appraisal and investigation' industry was regarded as a restricted one under the *Catalogue of Foreign-funded Industry Guidance.* Overseas credit rating agencies were permitted to operate in China only in the form of joint ventures with shareholdings less than 50%.

Since 2017 China's credit rating industry has further opened up to foreign participation. On June 28, 2017, the Catalogue of *Foreign-funded Industry Guidance* (revised in 2017) issued by the NDRC and the Ministry of Commerce removed access restrictions on foreign investment in 'credit appraisal and investigation' in the service sector. In July 2017 *the No.7 Announcement of People's Bank of China* loosened restrictions on the independent operation of overseas credit rating agencies in China.

The *Rules for the Registration and Evaluation of Credit Rating Agencies of Non-financial Enterprise Instruments in the Interbank Bond Market* released by NAFMII in March 2018 further specified the procedures of registration and evaluation, requirements for and structured management of credit rating agencies. Domestic and international credit rating agencies operating in the CIBM were expected to comply with these rules.

On July 20, 2019 the Financial Stability and Development Committee under the State Council announced policies and measures to allow foreign agencies to rate all types of bonds in the interbank and the exchange market when carrying out credit rating businesses in China.

In 2018 three leading international institutions set up wholly-owned subsidiaries in China - Moody's Credit Ratings (China) Limited, S&P Ratings (China) Co., Ltd. and Fitch (China) Bohua Credit Ratings Ltd.

In January 2019 PBC approved S&P Ratings (China) Co., Ltd., a wholly-owned subsidiary of S&P Global Inc. established in Beijing, for registration. Its registration to NAFMII was accepted on the same day. In July 2019 S&P Ratings (China) Co.,Ltd. released its first credit rating report, with rating symbols identical to those of domestic credit rating agencies. Fitch (China) Bohua Credit Ratings Ltd. received its approval to provide credit rating services to China's bond market in May 2020.

Chapter 4 - CIBM access channels

4.1 Bond Connect

Since 2017 Bond Connect has become the ‘go-to’ China access scheme. It allows international investors access to the CIBM with enhanced convenience in onboarding, trading, settlement and custody.

4.1.1 Market snapshot

Development of Bond Connect

Since CIBM’s launch, PBC has progressively allowed increased access of international investors to the onshore bond market. In the early days, investors generally participated in the CIBM through agency models such as QFII, RQFII, and CIBM Direct, where they sign agency agreements, complete registration with multiple regulators, open onshore cash accounts, and trade and clear through their agents.

As China heightened the speed of RMB internationalization, it led to the birth of Bond Connect in 2017. Bond Connect was an important milestone in China mutual market access, allowing investors from Mainland China and overseas to trade in each other’s bond markets through a market infrastructure linkage in Hong Kong (China). Northbound trading commenced on July 3, 2017, offering international investors the capacity to invest in the CIBM through mutual access arrangements in respect of trading, custody and settlement.

Southbound Trading under Bond Connect was also launched from September 24, 2021. Southbound Trading under Bond Connect provides Mainland institutional investors with a convenient and secure channel to invest in the Hong Kong bond market via the connection between the Mainland and Hong Kong (China) financial infrastructure services institutions.

For the purpose of this guide, Bond Connect here below refers to Northbound trading only.

Established in Hong Kong (China) in 2017, Bond Connect Company Limited (BCCL) supports the admission and registration of Northbound investors, liaises closely with the Recognised Access Platforms through which international investors are able to trade CIBM instruments, provides datafeed services, and conducts investor education activities in relation to the Chinese bond market and Bond Connect. On the primary market front, BCCL facilitates dissemination of Chinese primary bond market information, supports NCD primary subscription, and offers a one-stop electronic solution for bond issuance through its ePrime system.

Consistent enhancements to the access scheme and general onshore market infrastructure have been made to cater for evolving investor demand. During the first Bond Connect Anniversary Summit in 2018, Pan Gongsheng, PBC Deputy Governor, announced seven measures including full implementation of DVP, co-operation with mainstream international e-trading platforms (such as Bloomberg), tax policy clarification, launch of trade allocation, reduction of transaction fees, addition of 10 Bond Connect dealers, and permission for repo and derivatives trading. The first six were all implemented in 2018, while repo and derivatives trading are still being discussed.

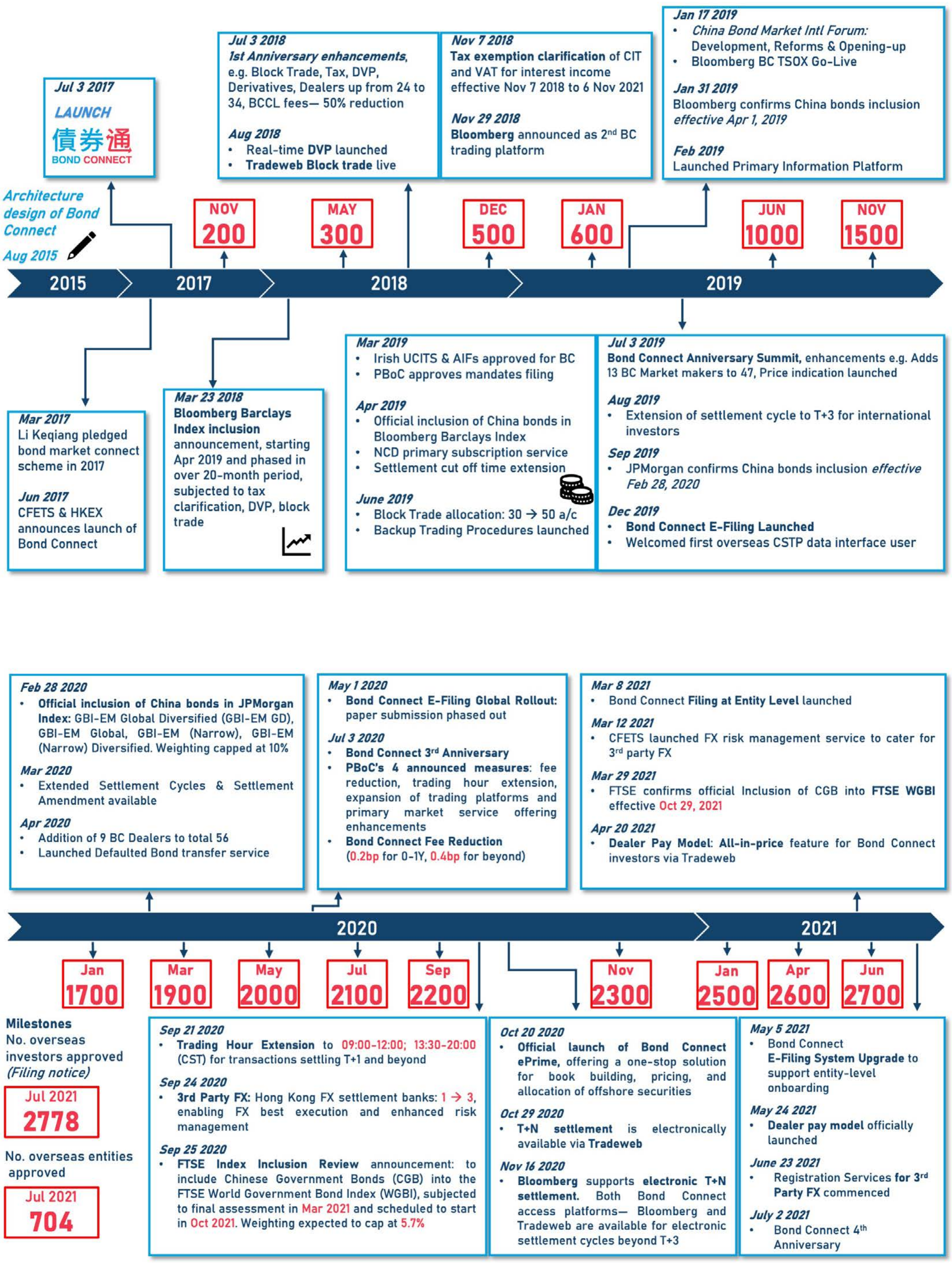
These measures enabled China’s bond market to meet all the conditions for inclusion in the Bloomberg Barclays Global Aggregate Indices, which took effect in April 2019.

During the 2019 Bond Connect Anniversary Summit PBC announced six further measures to enhance the scheme. These included broadening eligibility for Bond Connect market-makers, as well as prospective developments such as enriching transaction mechanisms, fungibility between Bond Connect, CIBM Direct and QFII/ QFII, mechanism for trading defaulted bonds, increased FX hedging options, and a solution to problems with close-out netting.

In 2020, PBC announced another 4 measures to facilitate the opening-up of the China bond market, including fee reduction, trading hour extension, expansion of trading platforms and primary market service offering enhancements.

In the past year, Bond Connect has witnessed further scheme enhancements, including launch of new entity filing, enablement of 3rd party FX hedging, validation of all-in price (dealer pay) model, extension of trading hour and launch of ePrime, an international electronic bond issuance system.

Chart 4-1 Timeline of Key Milestones and Market Development



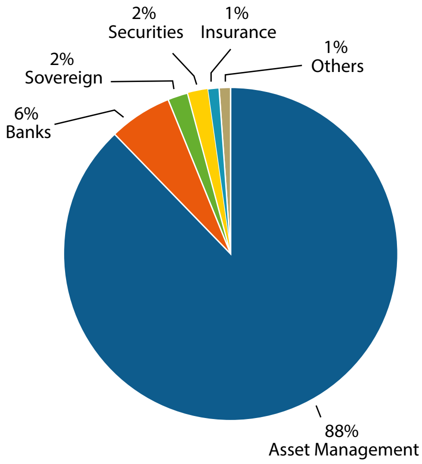
Source: Bond Connect Company Limited.

Market snapshot

Starting from only 139 investors in 2017, Bond Connect has grown to include (as of August 2021) more than 2770 overseas investors from 713 entities, representing twenty-fold growth over 4 years. Bond Connect's global footprint has expanded to 37 jurisdictions, mostly from the US, Hong Kong (China) and the UK.

Majority of registered accounts (about 88% of the investor base) are financial products, SMAs (separately managed accounts) or mandates of asset managers. Banks represent the second largest category of Bond Connect investors with 6% of market share, followed by sovereign accounts, security firms and insurance companies.

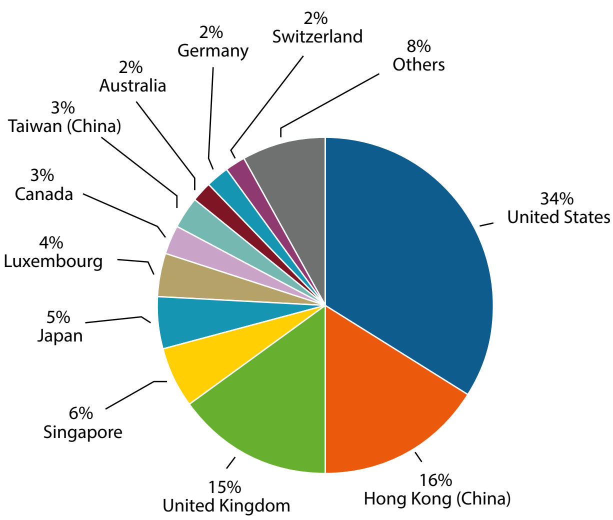
Chart 4-2 Bond Connect investor base by type



Note: end-July 2021.
Source: Bond Connect Company Limited.

In terms of jurisdiction, 34% of Bond Connect investors come from the US, followed by HK, UK and Singapore with 16%, 15% and 6% of the market shares respectively.

Chart 4-3 Bond Connect investor base by registration region

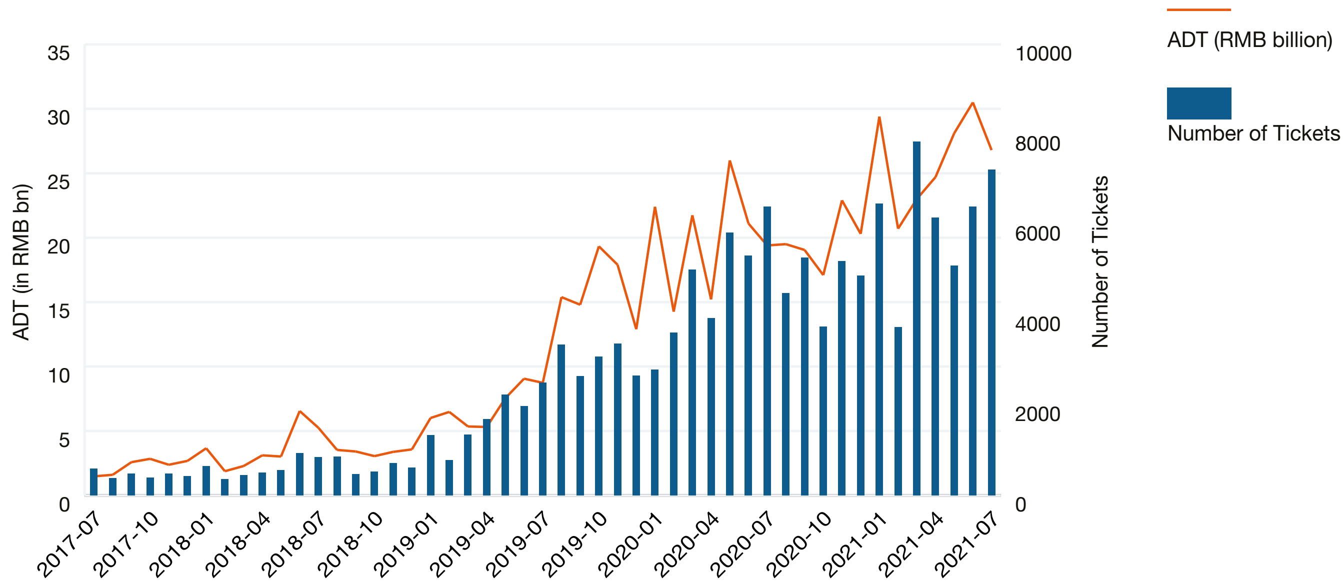


Note: end July 2021.
Source: Bond Connect Company Limited.

The average daily turnover (ADT) of Bond Connect has risen significantly from RMB 2.2 billion in 2017 to RMB 26.6 billion by end of July 2021, increasing by 13 times in 4 years. Moreover, the number of trade tickets saw a remarkable increase, recording a total of 137,000+ since launch and a single-day high of 750 on July 30, 2021.

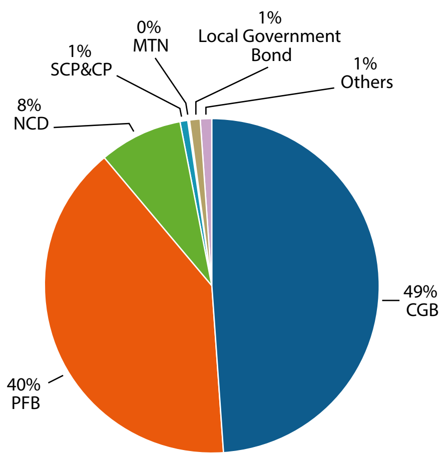
The majority of trading activities centre around China government bonds (CGBs), Policy Financial Bonds (PFBs) and Negotiable Certificate Deposits (NCDs) in 2021, representing 47%, 37% and 13% respectively. Bonds of 7 to 10-year maturities were most attractive to overseas investors, accounting for as much as 45% of trading in 2021 by end July. In recent years, global investors have been increasingly interested in credit products such as MTNs, ABSs, and green bonds.

Chart 4-4 Average daily Bond Connect turnover/ number of tickets



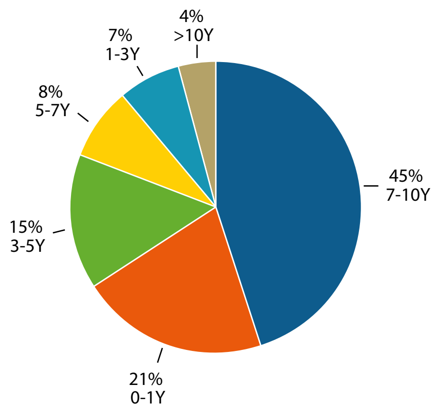
Source: Bond Connect Company Limited.

Chart 4-5 Bond Connect trading activity by bond type – July 2021



Source: Bond Connect Company Limited.

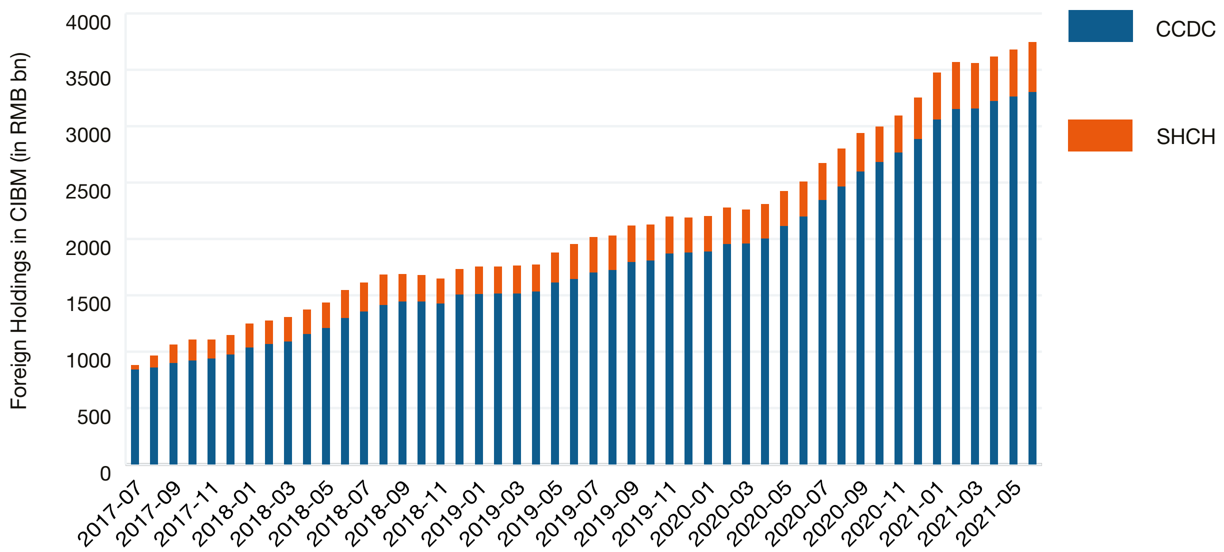
Chart 4-6 Bond Connect trading activity by tenor – July 2021



Source: Bond Connect Company Limited.

Overseas investment in the CIBM has continued to grow since Bond Connect's launch. By the end of June 2021, international investors' holdings exceeded RMB 3.74 trillion - more than four times the amount before the launch. The increase of foreign holdings can be explained not only by the global low yield environment and low correlation between China and other major bond markets, but also by the continued market infrastructure enhancements adding convenience to investment, global index inclusion, an RMB appreciation trend, and increasing asset diversification needs.

Chart 4-7 Total amount of overseas holdings in the CIBM



Source: Bond Connect Company Limited.

4.1.2 Investor eligibility

PBC published the *Notice No. 3 in 2016*[7] to specify the CIBM admission criteria. Types of investors that are allowed for Bond Connect are as follows:

- Overseas Central Banking Institutions, including:

— Foreign central banks, international financial institutions, sovereign wealth management funds.

- Overseas Financial Institutions including:

— Commercial banks, insurance companies, securities companies, pension funds, fund management companies, other asset management institutions lawfully registered and incorporated outside the territory of the People's Republic of China[8];

— Other medium and long-term institutional investors approved by PBC, such as charity fund and endowment funds.

4.1.3 Filing process

Application forms

In order to simplify the access workflow for overseas investors, PBC implemented New Entity Filing in June 2021. Under this enhancement, eligible financial institutions need only apply for PBC's approval once via Bond Connect's E-Filing. Upon PBC approval, the financial institution can proceed with trading account and CFETS ID set-up with BCCL and CFETS.

For a Foreign Central Bank/ Sovereign Wealth Fund, the required documents are different. See below table for more details.

Table 4-1 Application documents by filing types

Application Documents		Financial Institutions			Foreign Central Bank/ Sovereign Wealth Fund
		New Entity-based Filing	Trading Account Opening		
			Funds/ Products	Mandates/ SMA	
Forms to be filled in:					
[New] Entity Filing Form	Registration Form for Overseas Institutional Investors in China's Inter-Bank Bond Market	√			
Annex 2-1	CIBM Registration Application Form	√			
Annex 3	Bond Connect Investors Business Application Form/ Compliance Commitment Statement for Investing in China CIBM		√	√	√
The following form will be generated automatically:					
Annex 2-4	Letter of Authorization to Registration Agent	√			
Annex 6	Undertaking to Bond Connect Company Limited	√	√	√	
Annex 7	Compliance Statement for Mandates			√	
Form for Foreign Central Bank/Sovereign Wealth Fund to be filled in:					
Annex *	Chinese Intern- Bank Market Investment Registration Form				√

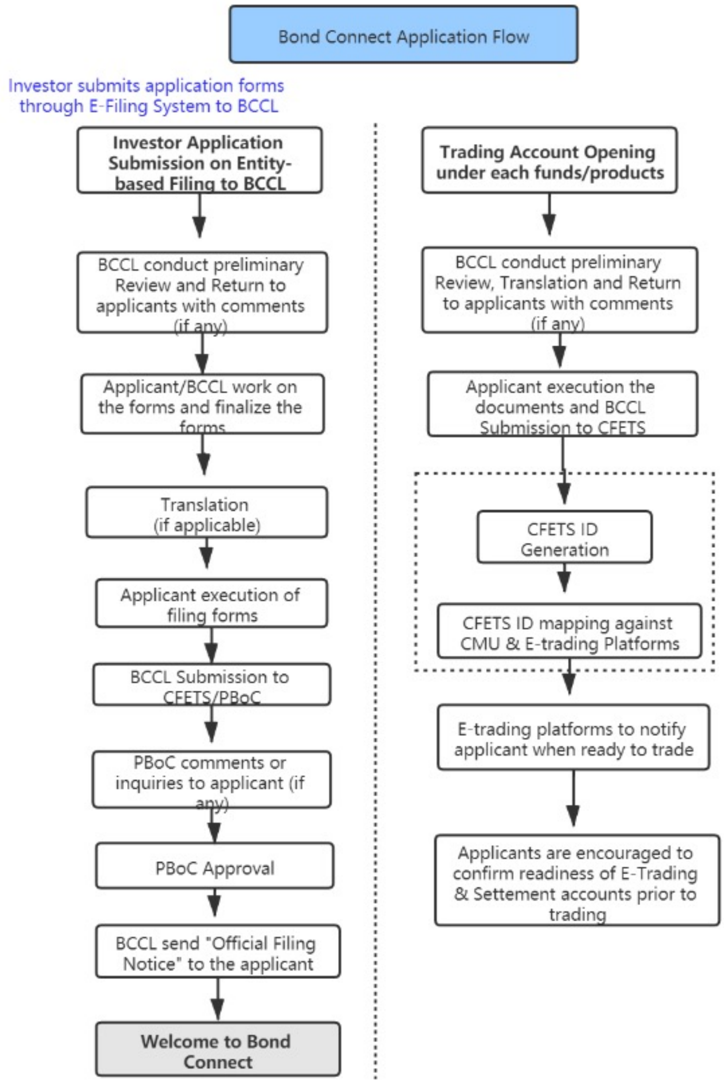
7 Public Notice No. 3 [2016]can be found at http://www.pbc.gov.cn/english/130721/3037272/index.html
8 Applicable to institutional investors from the Hong Kong Special Administrative Region (SAR) (China), Macao SAR (China) and Taiwan (China).

Application process

The Bond Connect application process is outlined below:

1. Investors submits application forms to BCCL through E-Filing system (https://efiling.chinabondconnect.com/index.html)
2. BCCL conducts review and revert to investors with comments (if any) through E-Filing system
3. Once the contents are finalized, investors can elect to use their own or BCCL's service to assist with Simplified Chinese translation. Once confirmed, investors execute the forms and BCCL submits the application to the CFETS/PBC.
4. PBC reviews or makes inquiries (if any).
5. After approval from PBC, BCCL sends filing notice to investors.
6. CFETS allocates CFETS ID to investors and then conducts mapping against CMU & e-trading platforms.
7. E-trading platform notifies applicant when ready to trade.

Chart 4-8 Bond Connect Application Flow Chart



Source: Bond Connect Company Limited.

Admission guidance

To provide comprehensive guidance to international investors, BCCL has published [The Handbook to Admission-Guidance & Forms] on its website. A dedicated account manager from BCCL will be appointed for individual investors and provide further tailored guidance and prompt responses to clients and custodians.

In conjunction with the application process, investors are advised to complete other operational set-ups such as completing KYC process with at least one onshore dealer, setting up trading platforms (currently Bloomberg and Tradeweb, availability varies across jurisdictions) and opening a custody account (including cash account and CMU ID) with their custodians. This will enable them to be ready to trade upon obtaining PBC's approval.

4.1.4 Market structure & trading mechanism

Market structure

The Bond Connect market structure comprises three key segments: 1) regulatory authorities, 2) trading link, and 3) settlement and custody link.

1. Regulatory authorities

Regulatory authorities of the Bond Connect scheme include PBC and HKMA.

2. Trading link

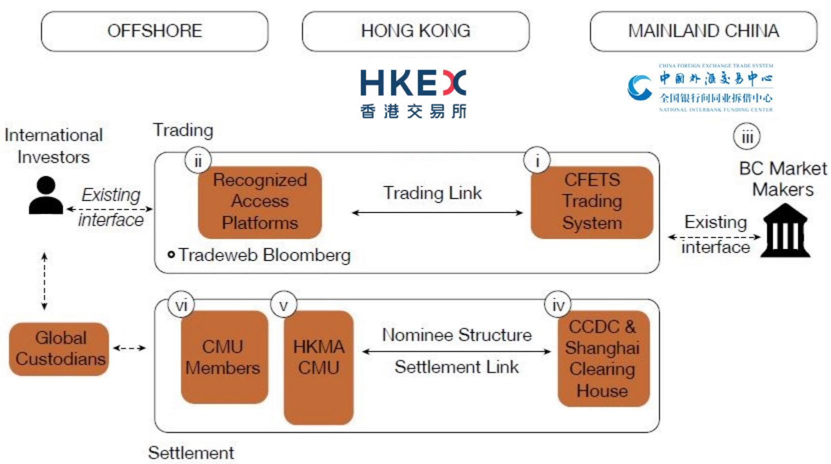
(1) Trading arrangements

Qualified Bond Connect investors approved by PBC can trade directly with eligible onshore dealers through electronic request-for-quote (RFQ) functions via established global trading platforms. Onshore dealers will provide quotes and market-making services to overseas investors through CFETS terminals.

Upon conclusion of the transactions, trade tickets will be registered and generated onshore in the CFETS system, where overseas investors can check details (in English) of each transaction in real time through recognized access platforms (Tradeweb and Bloomberg). BCCL also offers a complimentary data interface service that provides transaction details.

It is worth noting that Bond Connect's block trade allocation function (including pre-trade/post-trade allocation) can adequately support global asset managers' allocation of a single block trade to a number of funds and satisfy the 'best execution' requirement sought by international regulators and self-regulatory bodies.

Chart 4-9 Overview of Bond Connect infrastructure



Source: Bond Connect Company Limited.

(2) Key trading providers

i. CFETS

CFETS is the only bond trading platform approved by PBC in the CIBM.

ii. Global trading platforms

Under Northbound Bond Connect, trading links are established between global access platforms and the CFETS system, allowing international investors to trade CIBM instruments using an established international interface.

Currently recognized electronic trading platforms include Tradeweb and Bloomberg.

iii. Onshore market-makers

There are 56 authorised onshore Bond Connect Dealers in total as of end-July 2021 including onshore incorporated commercial banks and securities houses of both domestic and foreign background.

3. Settlement and custody link

(1) Custody arrangement

Bond Connect adopts the nominee system widely used among overseas investors to support a multi-level custodian framework involving global custodians (if any), sub-custodian banks (members of the CMU of HKMA), sub-custodian institutions (CMU) and CSDs (CCDC and SHCH). CMU has nominee accounts in both CCDC and SHCH, under which bonds purchased by international investors under Bond Connect are registered and through which they enjoy legal rights and interests to their securities holdings.

Under Bond Connect, a purchase of CIBM bonds is recorded in book entry form after the transaction is cleared and settled. Assets are distinctly segregated at three levels across the mainland and offshore CSDs[9]:

i. At the mainland/onshore CSD level

CIBM bonds purchased will be held in the omnibus securities account maintained with relevant mainland CSDs in the name of HKMA CMU, which holds the CIBM bonds as a nominee holder for CMU members and their underlying clients.

ii. At the offshore CSD level

The account of each CMU member in the CMU system is separate from those of other CMU members. Therefore, CIBM bonds held in the account of a CMU member are segregated from those held in other CMU members' accounts.

Each investor is required to open a segregated debt securities account (at investor, fund or sub-fund and mandate/segregated managed account level) with its local custodian (a CMU member) which in turn opens and maintains segregated sub- accounts within its account in the CMU system to hold its own or its clients' CIBM bonds at individual eligible investor level. The sub-account of each investor is separate from those of other investors with the same CMU member and the CIBM bonds held in an investor's sub-account are therefore segregated from those held in other investors' sub-accounts.

System processes and operational procedures have been established to ensure timely daily reconciliation of CMU members' holdings of CIBM bonds in the CMU system with those of CMU's omnibus accounts maintained with the mainland CSDs.

iii. At the CMU member level

CMU requires each CMU member to keep proper records for each of its client's holdings under Bond Connect.

9 Source: Bond Connect Settlement Link FAQ on this website.
https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/financial-market-infrastructure/debt-securities-settlement-system/

(2) Settlement arrangements

Bond Connect provides real-time delivery versus payment (DVP) settlement of each bond transaction in full for overseas investors. Bond transfers are effected through the bond registration systems of the CSD. Fund transfers are effected under the CIPS. Overseas investors can opt to settle transactions on a T+N basis.

Once a transaction is completed in the trading system, the transaction information is passed to CCDC's or SHCH's system as appropriate and confirmed by the CMU for settlement purposes. The respective Mainland CSDs will lock up the relevant CIBM bonds in their respective systems and at the same time initiate payment instructions to the CMU via the CIPS system. The payment instructions will be settled if CMU's account has sufficient funds and settlement will be performed on a DVP basis. In the event that the CMU account has insufficient funds, the payment instructions will be placed in a queue in the system pending for payment until sufficient funds are available.

Any trade that cannot be settled on the intended settlement date must be reported by a settlement report to BCCL and CMU respectively. BCCL with then submit the failed settlement to CCDC/SHCH.

(3) Key settlement providers

i. Onshore CSD

CCDC and SHCH are bond depository and settlement institutions approved by PBC. They mainly provide bond registration, depository and settlement services.

ii. Offshore CSD

The CMU acts as a Central Securities Depository (CSD) and the offshore depository for Bond Connect. CMU is a debt securities clearing and settlement system which provides clearing, settlement and custodian services for debt securities issued by both public and private sector entities.

iii. CMU members

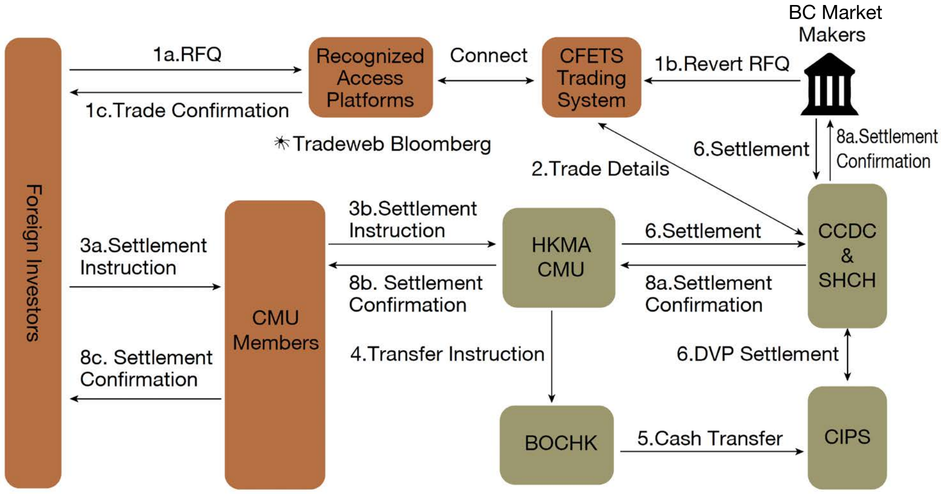
The members of CMU are local custodians appointed by investors' global custodians. To become a member of the CMU, a financial institution must be regulated by any one of the following authorities: (i) Hong Kong Monetary Authority; (ii) Securities and Futures Commission;

(iii) Insurance Authority or (iv) Mandatory Provident Fund Schemes Authority.

Bond Connect trading mechanism

1. To initiate a CIBM trade, overseas investors send onshore market-makers RFQs through recognized e-trading platforms connected to CFETS. Onshore market- makers revert with corresponding price quotes. Once transactions are made, investors receive trade confirmation on the e-trading platform
2. Transaction details are sent from CFETS to mainland CSDs (CCDC/SHCH)
3. Investors send settlement instructions to CMU members
4. CMU sends cash transfer instructions to BOCHK
5. BOCHK prepares for cash settlement via CIPS system
6. CMU sends settlement instruction to mainland CSDs, who prepare relevant bonds for settlement
7. Once confirmed that both bonds and cash positions are ready, real-time delivery versus payment (DVP) is performed
8. Mainland CSDs send settlement confirmation, which is passed to investors through CMU and CMU members

Chart 4-10 Trading and settlement workflow under Bond Connect



Source: Bond Connect Company.

4.1.5 Investment products

Currently Bond Connect investors can trade all cash bonds in the CIBM, including CGBs, PFBs, ABS, NCDs, SCPs, CPs, MTNs, enterprise bonds etc. Under the scheme, overseas investors can hedge their currency risk by trading FX spot, forwards and swaps, using CNY or CNH funding. In terms of currency conversion, the arrangement for Bond Connect's foreign exchange transactions has been further enhanced in September 2020. Investors can now elect up to 3 FX Settlement Banks to conduct currency conversion and hedging services. Registration for 3rd party FX in designating FX Settlement Banks can now be carried out via BCCL.

In the future Bond Connect will gradually expand to other financial products, as well as offering further enhancements to existing investment products. The pipeline includes but is not limited to:

- Facilitating investor participation in the primary market under ePrime;
- Launching an FX system to address the need for regulatory reporting and FX trade data monitoring;
- Enabling offshore access to derivatives products including IRS, futures, credit derivatives and repo.

4.1.6 Legal considerations

PBC, in *the PBC FAQ*[10], and *HKMA*, in the *Bond Connect Settlement Link FAQ*[11], have addressed the question of beneficial ownership in a Bond Connect context. Below are a few points for reference:

Bond Connect adopts the internationally accepted nominee holding arrangement and recognises offshore investors' beneficial ownership of the CIBM bonds that are held by the CMU through the nominee holding arrangement. PBC expressly indicated that the meanings of the terms 'nominee holder' and 'beneficial owner' of CIBM bonds under Bond Connect follow international rules and are the same as those under Stock Connect. An eligible offshore investor, as the beneficial owner of the CIBM bonds, should be able to exercise its rights with the bond issuer through the nominal holder CMU.

10 PBC FAQ dated 22nd June 2017 is available at http://www.pbc.gov.cn/goutongjiaol iu/113456/113469/3331208/index.html. Only Chinese is available.
11 Bond Connect Settlement Link FAQ is available on this website. https://www.hkma.gov.hk/media/eng/doc/key-functions/finanical-infrastructure/infrastructure/Bond_Connect_Settle_Link_FAQ.zip

On this basis, it is recognized that beneficial ownership in CIBM bonds held through Bond Connect would be similarly respected by mainland regulators and Chinese courts. Subject to an eligible offshore investor providing evidence that it is the beneficial owner of the relevant CIBM bonds (namely, certificate or proof provided by CMU and CMU members showing that the investor is the legitimate beneficial owner under Hong Kong law), the offshore investor should be entitled to bring legal proceedings in its own name in the mainland courts.

Based on the certification of bond holding issued by the CMU, plus similar bond holding documentation provided by the relevant CMU member, which serves as a local custodian, as well as the relevant global custodian (if applicable), the eligible investor will have documentary evidence of beneficial bond ownership under Bond Connect.

4.1.7 Outlook

Bond Connect's success stems from its facilitation of international participation in the onshore China bond market. Not only has it continued to expand its product range in an increasingly investor-friendly manner, but it has introduced and will continue to introduce enhancements in onboarding, trading and settlement, opening-up to further e-trading platforms and market makers, and facilitation of investor participation in primary market under ePrime.

Future enhancements of Bond Connect may include: refining of FX trading processes and allowing trading with multiple FX settlement banks; expansion of product range by permitting repo and derivatives trading such as IRS and futures as appropriate; development of Bond Connect primary market access; enhanced data and information dissemination; potential integration of Bond Connect with other access schemes; strengthening market promotion; and providing better trade- related services.

With the continued opening-up efforts of the CIBM and the inclusion of Chinese securities into global bond indices by providers such as FTSE Russell, Bloomberg Barclays and JP Morgan, demand for Bond Connect is likely to grow.

4.2 CIBM Direct[12]

4.2.1 Introduction

Efforts have been made to open up the CIBM to overseas investors since 2005. As part of the RMB's internationalization, PBC allowed foreign central banks and monetary authorities, overseas RMB clearing banks and overseas RMB participating banks to enter the CIBM; bonds traded on the CIBM became eligible investments for QFII and RQFII in 2013.

The most significant and recent milestones are:

- In July 2015 PBC promulgated the *Notice on the Relevant Issues concerning the Investment in the CIBM with RMB Funds by Foreign Central Banks, International Financial Institutions and Sovereign Wealth Funds* (PBC Notice 2015 No. 220), permitting three types of entities (foreign central banks, international financial institutions and sovereign funds) to engage in bond trading, bond repurchases, bond lending, bond forwards, interest rate swaps and other trades permitted by PBC, without any PBC approval or quota restrictions.
- In February 2016 PBC promulgated the *Announcement on Issues concerning the Further Improvements to the Investment in the Interbank Bond Market by Foreign Institutional Investors* (PBC Announcement 2016 No. 3), which further relaxed the rules applicable to other overseas institutional investors (OII) accessing the CIBM. Section 4.2.2 below elaborates on the types of OIIs. Accordingly, the term 'CIBM Direct' is often used to refer to this route for OIIs to directly access onshore bonds.
- Two ground-breaking features of PBC Announcement 2016 No. 3 are the removal of prior approval and quota requirements for all OIIs accessing the CIBM. This has resulted in more OIIs (particularly medium and long-term

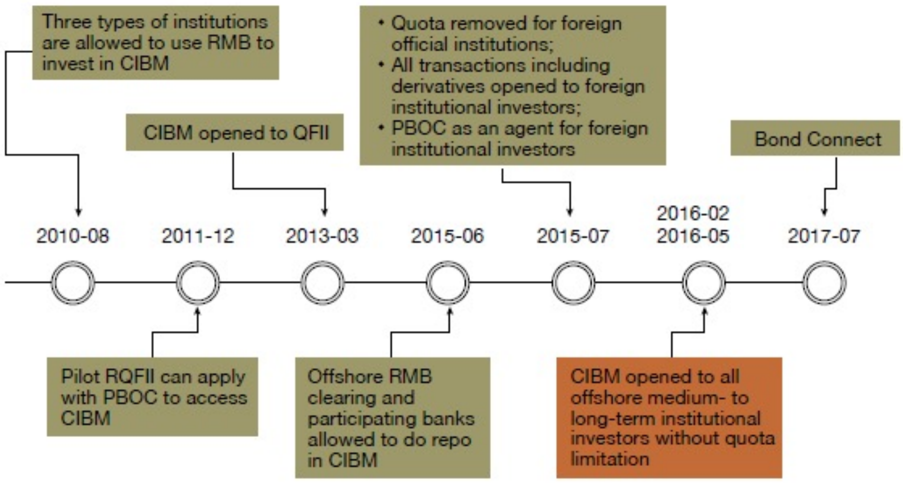
12 Section 4.2 is written by Richard Mazzochi, David Mu and Stella Wang (King and Wood Mallesons).

investors) investing in the CIBM.

- In May 2016 PBC Shanghai Head Office issued the *Implementing rules on Filing Requirements for the Investment in the Interbank Bond Market by Overseas Institutional Investors* (PBC SH Rules 2016 No. 2) which provided a streamlined filing process for OIIs, through their appointed onshore settlement agents.
- In May 2016 SAFE issued the *Notice on the Relevant Foreign Exchange Issues concerning the Investment in the Interbank Bond Market by Overseas Institutional Investors* (SAFE Notice 2016 No. 12) which revised requirements on FX registration, fund remittance and repatriation in relation to OIIs.
- In February 2017 SAFE issued the *Notice on the Relevant Issues concerning the Foreign Exchange Risk Management for Overseas Institutional Investors in the Interbank Bond Market* (SAFE Notice 2017 No. 5) which allowed certain onshore settlement agents to enter into FX derivative transactions with OIIs for the purpose of hedging OIIs' FX risk. Further relaxation is expected in the future to bring more flexibility to OIIs' hedging in the interbank FX market.
- In July 2021 PBC issued the *Administrative Measures on bond lending business in the China Interbank Bond Market (Consultation Paper)*, supplemented the 2006 rules on bond lending with more detail, including the collateral used in CIBM bond lending, master agreement documentation, centralized bond lending and risk controls. The consultation paper does not specifically address foreign participation in CIBM bond lending but it should apply, once finalized, to foreign participants' onshore bond lending / borrowing business (for hedging purposes) which have been granted since 2016. Parties are required to document their CIBM bond lending / borrowing trades under the master bond lending agreement recognized by PBC.

CIBM opening-up

Chart 4-11 CIBM opening-up timeline



Source: HKEX: Research Report: The inclusion of China into global bond indices: current status and future development, June 2018.

4.2.2 Accessing the CIBM

Type of OIIs

Based on PBC Notice 2015 No. 220, PBC Announcement 2016 No. 3 and other rules and regulations, OIIs include:

(i) foreign central banks, international financial institutions and sovereign wealth funds;

(i) foreign commercial banks, insurance companies, securities companies, fund management companies and other asset management companies (including QFIIs and RQFIIs);

(ii) foreign investment products (having no legal personality) issued by any foreign financial institution in paragraph (ii) above;

(iii) foreign pension funds, charity funds, donation funds and other foreign medium-and long-term institutional investors; and

(iv) other institutional investors incorporated in Hong Kong (China), Macau (China) and Taiwan (China).

Each OII is required to meet the following criteria:

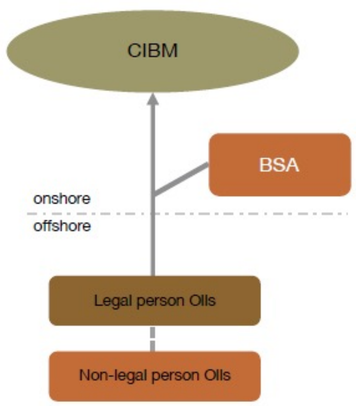
- it is duly established under the laws of the place of incorporation;
- it has a sound corporate governance and complete internal control policies. It has received no material punishment from the applicable regulators for any illegal conduct or misconduct in bond investments in the past 3 years;
- the sources of funds are legal;
- it is able to identify and assume the risks, and it understands and agrees to assume the investment risks; and
- it meets other requirements of PBC.

As of the end of June 2021, the number of foreign participants accessing CIBM through CIBM Direct model reached 483.

Filing with PBC and SAFE

Before an eligible OII can access the CIBM, it must appoint an onshore bond settlement agent (BSA) and file an application through that BSA with PBC.

Chart 4-12 structure of CIBM Direct



In particular, foreign central banks, international financial institutions and sovereign wealth funds must file with PBC:

these types of OII prepare and submit the registration form to PBC either themselves or via their BSA (the Bond Settlement Agency Agreement can be submitted to PBC at a later stage). PBC provides feedback to the applicant via email within 7-10 working days[13] upon receipt of the registration form.

Other types of OIIs must file with PBC Shanghai Head Office following these procedures:

The BSA is required to apply general principles such as “Know Your Client”, “Know Your Business” and due diligence for onboarding an OII. It files the application and settlement agency agreement with PBC SH Head Office through the PBC filing system.

Two sets of registration forms were published by PBC SH Head Office for OIIs and their BSA to use:

- Registration form for OIIs in CIBM (for incorporated entities): to be used by OIIs which are legal persons;[14] and
- Registration form for OIIs in CIBM (for unincorporated entities): to be used by OIIs which are non-legal persons.[15]

In March 2021, PBC issued a circular requesting PBC SH Head Office, CFETS, CCDC and SHCH to further streamline the account opening process for OIIs that wish to enter into the CIBM.

When the OII is a foreign legal person (meaning has title to the investment), the name filed with PBC SH Head Office is normally the name of that OII. However, if the OII is not a legal person, a two-layer naming convention is usual. For example, a foreign fund manager may choose to file an investment fund under its management as a non-legal person OII. The naming convention is then “*[Fund Manager] – [Investment Fund]*”. The name chosen might be influenced by tax considerations.[16]

PBC SH Head Office may complete a filing within 20 working days. Each OII is required, after its successful filing, to register through its BSA with SAFE[17] before the settlement agent can proceed to open the FX account for that OII.

Opening onshore accounts

After the completion of the OII filing, the BSA must assist investors with the opening of the Basic RMB account (if applicable) and relevant RMB account(s) with PBC SH Head Office upon receipt of account opening documents and account opening instructions.

The BSA must assist the OIIs with the opening of the bond accounts and DVP cash clearing accounts with the CCDC, the SHCH and applying for trading codes with the CFETS, including completing all required documents and application forms, and submitting the application documents to the CCDC, the SHCH and the CFETS.

4.2.3 Settlement & custody

Appointment of BSA

Each OII must enter into an agency agreement with the BSA it chooses from a list published by PBC.[18] The basic services of a BSA include:

- filing and submitting registration applications

13 The actual time limit is subject to the official release of the regulatory body.
14 For example, types (ii) and (v) listed above.
15 For example, types (iii) and (iv) listed above.
16 Three-layer naming convention is sometimes used too. For instance, one non-legal person OII (being a sub-fund) filed its name in the form of “[Fund Manager] – [Mother Fund] – [Sub-fund]” so as to (a) reflect the full picture of the offshore fund structure and (b) highlight the sub-fund as the ultimate beneficiary. In some other rare cases, three-layer naming convention in the form of “[Fund Manager] – [Sub-manager] – [Fund]” is also accepted for non-legal person OIIs. In either case, the name must not exceed 30 Chinese characters.
17 Pursuant to SAFE Notice 2016 No. 12.
18 The list of onshore BSA can be found at the official website of PBC SH Head Office.

- opening, maintaining and cancelling the relevant accounts such as the RMB special saving account, bond accounts, special cash accounts for settlement and bond trading accounts
- processing the orders from the OII to trade and settle the CIBM bonds
- collecting, and repatriating out of China, the investment principal and interest to the OII.

The BSA can also provide custodian services including asset custody, accounting, auditing, valuation and financial report/statement preparation.

The BSA is required[19] to:

- ensure and verify the eligibility of the OII;
- fully disclose the CIBM regime and the risks associated with CIBM investments;
- report to PBC SH Head Office the OII's information and its investment positions, and assist PBC, NAFMII, CFETS and the bond register and clearing institutions with relevant market analysis and oversight; and
- monitor the OII's RMB special saving account on a real-time basis, and submit to PBC timely, accurate and complete reports on RMB cross-border remittance data through the RMB Cross-border Payment Information System.

An OII may change its BSA upon filing an application for change with PBC SH Head Office and SAFE.

Inbound remittance of funds

An OII may remit RMB or FX into China for CIBM investment.

Permitted investment scope

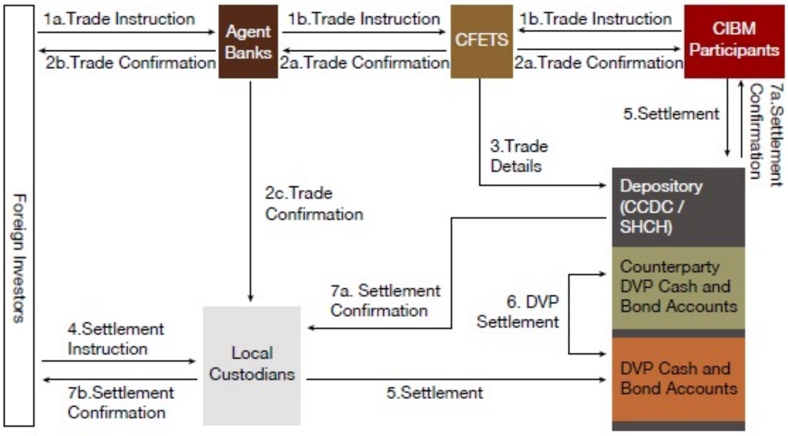
The table below summarises the permitted investment scope of different types of OIIs.

Table 4-2

Types of OIIs	Permitted trades
All OIIs	• Spot bond trades; • Bond lending, bond forwards, interest rate forwards and interest rate swaps for hedging purposes; • FX derivatives, including FX forwards, FX swaps, cross-currency swaps and options with BSA for hedging purposes; • NCD
Offshore RMB clearing banks, offshore RMB participating banks and foreign central banks and monetary authorities, international financial institutions and sovereign wealth funds	• Bond repos

19 pursuant to PBC Notice 2016 No. 3.

Trading and settlement[20]
Chart 4-13 Trading and settlement flow of CIBM Direct scheme



Source: CFETS: China CIBM Overview, January 2019.

1. Trading arrangements

Under CIBM Direct, OIIs can contact the Agent Trading System (ATS) or other communication platforms to provide transaction orders to the BSAs. The BSAs will then send the inquiries and execute trades in the CFETS trading system. In the CIBM Direct mode, OIIs can trade with all CIBM participants.

OIIs can also send CIBM trading instructions to the BSAs via a Bloomberg terminal, by the following two methods: either using Bloomberg VCON to send instruction to their BSAs, which will then use CFETS ATS to affirm the OIIs' instruction; or the BSAs using the CFETS ATS to send the pre-filled authorized trade instruction to OIIs, which use the Bloomberg VCON to affirm the instruction.

A third option for OIIs filed with PBC SH Head Office is to trade directly with onshore market makers through electronic request-for-quote (RFQ) functions via established global trading platforms that have been connected to the CFETS system. Onshore market makers will then provide quotes and market-making services to OIIs through CFETS terminals.

2. Settlement arrangements

After the trade is executed in the CFETS system, the OIIs will receive the trading ticket generated in CFETS from the BSA. OIIs using the CFETS ATS can search the trading ticket via real-time inquiries in the CFETS system. Upon receipt of the trading ticket, the OII can send the settlement instruction to the BSA directly or via their global custodian to complete the settlement. If the bonds are settled on receipt of the settlement instructions, the BSA shall (a) verify and activate the settlement instruction on the settlement day, (b) transfer the funds from the RMB special cash account (NRA account) opened by the OII with the BSA to the bond settlement cash account opened by the OII with the onshore bond depositories (i.e., the CCDC or the SHCH) and (c) complete the settlement confirmation in the CCDC or SHCH's settlement system on behalf of the OII. The DVP settlement is then completed between the OII's bond account and bond settlement cash account and the counterparty's bond account and bond settlement cash account opened with the CCDC or SHCH or the clearing account opened in the China National Advanced Payment System (CNAPS).

In respect of bond settlements that can go automatically without a settlement instruction, the BSA can complete the bond and cash settlement directly on behalf of the OII. On the settlement day, the BSA must send the settlement confirmation to the OII or its global custodian to confirm completion.

20 Subject to the RMB/FX ratio limit on repatriation (see the paragraph headed 'Repatriation'), FX derivatives must be entered into by OIIs with BSAs based on their genuine business needs.

Repatriation

There are generally no quota limits or repatriation restrictions for an OII to remit investment principal and income out of China. It can elect to repatriate proceeds in RMB and/or FX after it converts the RMB proceeds into FX through the BSA, provided that the RMB/FX currency ratio for repatriation[21] is consistent (within 10 per cent.) with the rate that applied on the original inbound remittance.

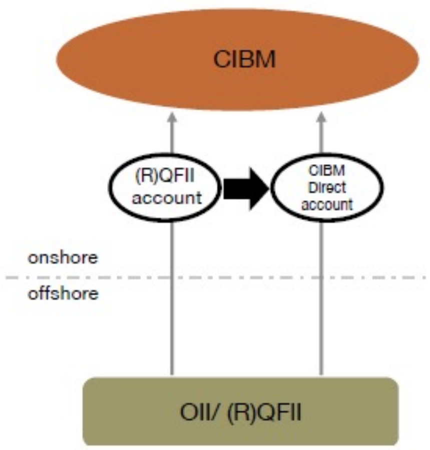
In March 2019 SAFE published a Q&A[22] regarding control of the CIBM repatriation currency ratio. According to the Q&A, OIIs can also follow a second method where the accumulated RMB outflow shall not exceed 110% of the original RMB inflow or the accumulated FX outflow shall not exceed 110% of the original FX inflow for any specific repatriation arrangement. However, this restriction does not apply if the OII opts to repatriate all investment proceeds out of China.

In November 2018, the MoF and the STA jointly issued the *Notice on the Policy of Enterprise Income Tax (EIT) and Value-added Tax (VAT) relating to Overseas Institutional Investors' Investment in the Interbank Bond Market* (MOF and STA Notice 2018 No. 108), exempting OIIs from enterprise income tax and value-added tax for three years. That period expires on November 6, 2021, unless a further exemption is granted.

Position switch

PBC and SAFE jointly published the *Circular of the People's Bank of China and the State Administration of Foreign Exchange of Matters Relating to Further Facilitating Investment of Foreign Institutional Investors in the Interbank Bond Market* (PBC Notice [2019] No. 240) which allows international investors to switch CIBM investments between different channels.

Chart 4-14



Bonds and cash of a single overseas institutional investor are permitted to be transferred between its accounts opened under QFII/RQFII and CIBM Direct.

PBC Notice [2019] No. 240 was driven by the fact that a large number of OIIs are also QFIIs or RQFIIs. Investors were previously obliged to choose either the CIBM Direct or QFII/RQFII channel, which were segregated and subject to different regulatory and operational regimes.

This liberalization will provide greater flexibility to international participants in structuring and managing their portfolios.

21 For the first repatriation, the RMB/FX currency ratio requirement does not apply but the funds must not exceed 110% of the aggregated capital remitted into China for CIBM investments.
22 See: http://www.safe.gov.cn/safe/2019/0329/12845.html.

4.2.4 International concerns

Market expectations

The CIBM Direct channel has been operating for over three years, and features a wide range of hedging tools, access to market information, no investment quota limits and few repatriation restrictions.

Participants look forward to further improvements in the ability to take security over an OII's interest in CIBM bonds.

However, it is likely that rules to address these concerns will be gradually introduced.

An absence of rules on how to enforce a pledge, particularly in the context of CIBM bonds, has now been addressed effectively with the recent introduction of the following default rules:[23]

- *Operational Guidance on Enforcement of Collateral* (Trial) (CCDC Enforcement Rules) and *Operational Procedures of Enforcement of Collateral by Auction* (CCDC Auction Rules), and the press release of Questions and Answers published by the CCDC
- *Implementing Rules on Enforcement of Bonds underlying Repurchase Agreements (Trial)* (SHCH Enforcement Rules) and *Implementing Rules on Auction of Bonds underlying Repurchase Agreements (Trial)* (SHCH Auction Rules), published by the SHCH
- *Implementing Rules on Enforcement of Bonds underlying Repurchase Agreements (Trial)* (CFETS Auction Rules), published by the CFETS, (CCDC, SHCH and CFETS are collectively called 'Enforcement Organizations').

The table below provides a comparison of the Default Rules published by the three Enforcement Organisations:

23 Please refer to https://www.kwm.com/en/hk/knowledge/insights/self-remedy-enforcement-rules-in-china-bond-market-20190726

Table 4-3 Comparison of the default rules published by three enforcement organizations

Self-remedy enforcement organized by		Registration institutions		Trading facility
		CCDC	SHCH	CFETS
Security agreement to be enforced		All security agreements in respect of CIBM bonds registered with the CCDC as collateral, provided that the parties have entered into the *Collateral Management Service Agreement (CMSA)* with the CCDC in advance (except for repos where a CMSA is not required)	Repurchase agreements in respect of CIBM bonds registered with the SHCH as repurchased securities	Repurchase agreements in the CIBM including pledges and outright transfers
Self-remedy enforcement	Conversion into value[24]	To be agreed by the pledgor and the pledgee, and to submit a joint application to the CCDC	To be agreed by the pledgor and the pledgee,[25] and to submit a joint application to the SHCH	Not applicable
Self-remedy enforcement	Auction	√ to be applied for by the pledgee alone √ bid floor price to be determined by the CCDC by reference to the average trading price for the latest 30 consecutive trading days and the dirty price published by ChinaBond Pricing Center Co., Limited ("ChinaBond Valuation") on the trading day immediately preceding the auction date √ to be conducted by way of tender – inviting by price, bidding in full-price (or dirty-price) and accepting in multiple prices[26] √ proceeds realised from auction to be transferred from the successful bidders' cash account to the CCDC's enforcement special cash account, and then to the pledgee's cash account	√ to be applied for by the pledgee alone √ bid floor price at 80% of the average trading price for the latest 30 consecutive trading days, or 80% of the valuation price on the trading day immediately preceding the enforcement date √ to be conducted by way of tender-inviting by price, bidding in full-price (or dirty- price) and accepting in multiple prices √ the SHCH to register the title transfer after the auction, and remit the proceeds from the successful bidders' cash account to the pledgee's cash account	√ to be applied for by the pledgee alone √ bid floor price at 80% of the average trading price for the latest 30 consecutive trading days, or 80% of the valuation price on the trading day immediately preceding the auction date √ one single auction price to be determined based on the principle of price priority and time priority[27] √ upon the completion of the auction, the relevant registration institution to effect the transfer of the proceeds and the title of the bonds

24 PRC law prohibits a "fluidity" clause under which the parties agree at the time of entry into the pledge agreement that the title to the collateral will transfer to the pledgee upon the pledger's default (in effect, a self-executing title transfer).
25 In the context of a repurchase agreement, the pledgor is also known as 'repurchaser' or 'seller' and the pledgee is known as 'reverse-repurchaser' or 'buyer'.
26 "Inviting by price, bidding in full-price (or dirty-price) and accepting in multiple prices" means that:
(a) the Enforcement Organisation invites bids from eligible bidders. The bids will be sorted by price (from highest to lowest);
(b) the price on each bid is a dirty-price if it includes accrued interest; and
(c) the bidder with the highest bid price is successful for the amount of bonds it bid at its bid price; the bidder with the second highest bid price is also a successful bidder for the amount of bonds it bid at its bid price, and so on, until the aggregate amount of all successful bids reaches the amount auctioned.
27 Unlike the mechanism used by CCDC and SHCH ("inviting by price, bidding in full-price (or dirty-price) and accepting in multiple prices"), CFETS calculates a single auction price at which all successful bidders will buy the respective amounts of the auctioned bonds

4.3 QFI regime

4.3.1 Overview

The QFII and RQFII regimes were introduced in 2002 and 2011, respectively, to allow certain qualified non-PRC institutional investors to invest directly in the Chinese domestic securities market.

Since its introduction, the QFII regime has served as a key component of China's financial market liberalisation initiative and has grown rapidly to attract a wide range of overseas investors. The RQFII regime was launched later to encourage the use of RMB by overseas market participants. The RQFII regime can be used by eligible foreign institutional investors who raise RMB funds outside China for investment in the Chinese securities market.

(1) Latest developments

In September 2019, SAFE announced that, as recognised by the State Council, the restrictions on investment quota for QFIIs and RQFIIs would be removed. In May 2020, SAFE formally repealed the filing and approval requirements in respect of QFII/RQFII investment quotas. Restrictions on the scope of RQFII pilot jurisdictions were removed as well.

Following the landmark removal of the investment quota for both regimes, PRC regulators have consolidated the two parallel regimes of QFII and RQFII by a unified set of rules applicable to all QFIIs and RQFIIs (collectively "**QFIs**") which came into effect from 1 November 2020.[28]

The primary PRC regulators of the QFI regimes are:

(a) CSRC, which is responsible for approving license applications made by prospective overseas investors (each an "**Applicant**") and supervises and regulates the securities investments;

(b) SAFE, which administers and monitors account opening, currency conversion, cross-border remittance of funds, and statistics collection for balance of payments; and

(c) PBC, which is involved in policy-making, regulating the interbank market as well as monitoring RMB cross-border remittance.

Under the new QFI regime, a QFI shall appoint at least one onshore commercial bank to act as its custodian to, among others, handle licence application, trade settlement, asset custody and routine reporting. In addition, a QFI must also engage onshore broker(s) for securities and futures trading.

A timeline of the milestone developments of the QFII and RQFII regimes since their launch is set out below.

28 PBC, CSRC and SAFE jointly released the QFI Measures on 25 September 2020, together with the QFI Implementing Rules.

Chart 4-15 Milestone Developments of the QFII Regime

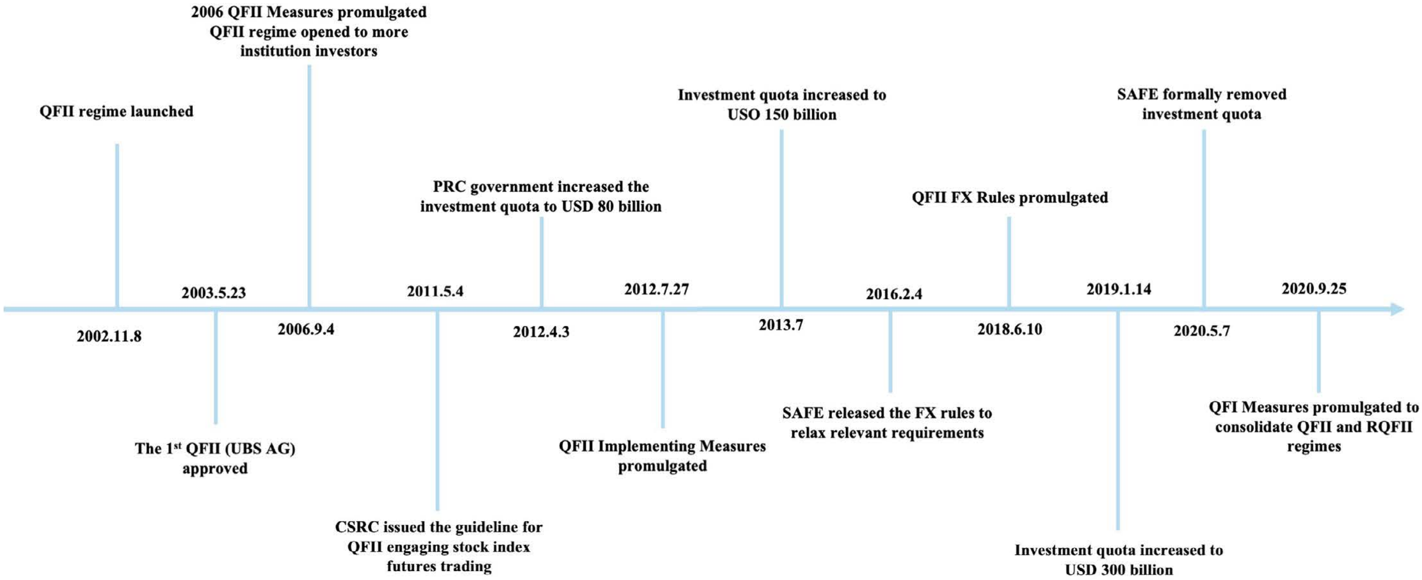
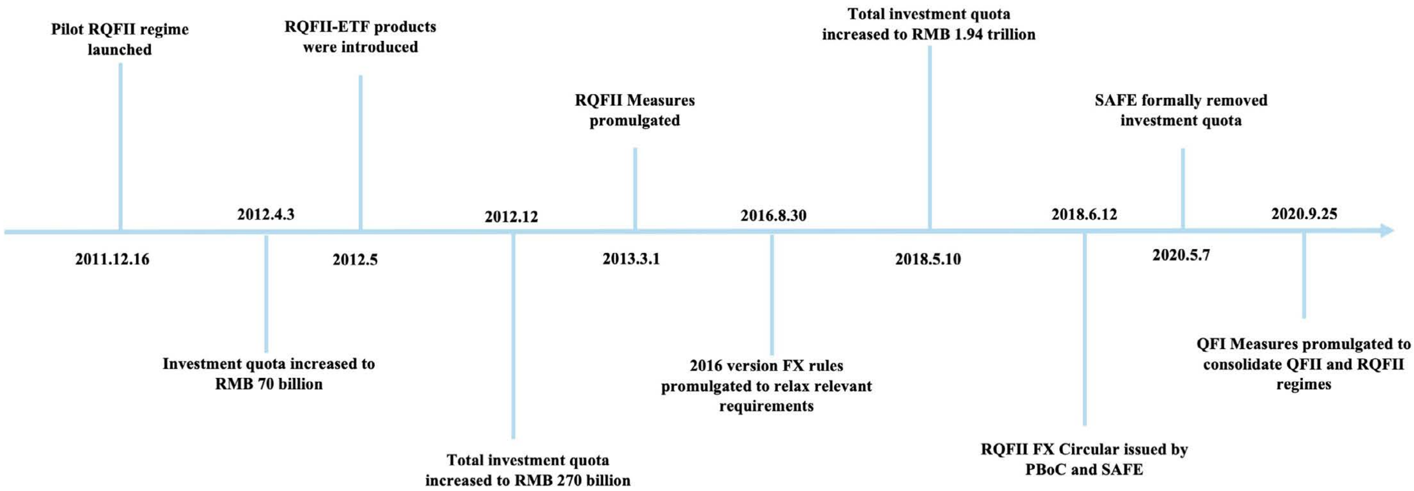


Chart 4-16 Milestone Developments of the RQFII Regime



(2) Investment in CIBM through QFI Regime

The investment scope of QFIs has been expanded under the QFI regime, and more investment products on the stock exchange market ("**SEM**"), CIBM and exchange-traded derivatives market ("**EDM**") are now available to QFIs. The table below sets out the amendments to the current regimes:

Segment	Previous QFII/RQFII regime	New under QFI regime
SEM	Shares, bonds and warrants	• Depositary receipts and asset-back securitisation products (the Measures and Implementing Rules clarify that asset-backed securities are permitted investments for QFIs) • Securities borrowing and margin trading • Securities lending to securities finance company • Bond repo • Shares and other types of securities admitted on the National Equities Exchange and Quotations
CIBM	Cash bonds	Derivatives linked to bonds, interest rate and FX
EDM	Stock index futures	Other futures and listed options
Funds/Asset Management Products	Public securities investment funds	Private investment funds

QFIs are subject to the same regulations as other qualified institutions using CIBM Direct to invest in the CIBM. However, QFIs have more flexibility as they can move their investments from the CIBM to the A-share market (or other eligible investments) directly and do not need to go through a repatriation process.

It should be noted that a QFI may also engage in FX derivatives transactions. This is permitted only on a "real demand" basis and solely for hedging FX risk exposure arising from the QFI's domestic investment according to the QFI FX Rules.

4.3.2 Eligibility requirements

To qualify as a QFI, an applicant must satisfy the following (non-exhaustive) eligibility requirements:

(a) the applicant should have sound financial status, good creditworthiness and experience in securities and futures investment;

(b) the principal person-in-charge of PRC onshore investment should satisfy the relevant qualification requirements prescribed by the laws of the applicant's home country or jurisdiction;

(c) the applicant should have a sound governance structure, internal control and compliance management system, and the applicant should designate supervisor(s) responsible for supervising compliance with applicable laws and regulations;

(d) the applicant should have not been subject to any material penalty by regulatory authorities in the most recent three years or since establishment (if it has been established for less than three years); and

(e) there is no circumstance that may exert a significant impact on the operation of the PRC domestic capital markets.

Existing QFII and RQFII license holders should be converted into QFI license holders automatically, but such existing license holders should check with their PRC Custodian (as defined below) on the relevant formalities and logistics.

4.3.3 Application & account opening process

Under the consolidated QFI regime, the Applicants will only need to apply to CSRC for a QFI Licence (as defined below). After obtaining the QFI Licence, the QFIs shall make a registration with SAFE. These processes need to be done through the PRC commercial bank appointed as custodian (the "**PRC Custodian**").

(1) Application for a QFI License with CSRC

An eligible QFI Applicant should submit (via the PRC Custodian)[29] a set of application documents (by both electronic means and hard copy) including, but not limited to:

(a) application letter;

(b) business license or registration certificate and evidentiary materials of business operation qualification;

(c) statement on whether any material penalties have been imposed on it by any regulatory body in the immediately preceding three years or since its establishment (if it has been established for less than three years), which should be issued by the competent regulator of the Applicant or an independent counsel;

(d) power of attorney granted to the PRC Custodian; and

(e) other documents required by CSRC based on the principle of prudential regulation.

The timeframe for CSRC reviewing the application is tremendously shortened under the consolidated QFI regime. After the relevant application materials have been officially lodged with CSRC, it will take up to 10 working days for CSRC to review and (if the application is approved) issue the License for Operation of Securities and Futures Business (the "**QFI Licence**").

(2) Registration with SAFE

After obtaining the QFI Licence from CSRC, the Applicant should, through the PRC Custodian, make a registration with SAFE. A QFI needs to submit the following materials to its PRC Custodian for such registration:

(a) the standard registration form published by SAFE; and

(b) a photocopy of the QFI Licence issued by CSRC.

(3) Account opening

As a prerequisite for carrying out investment in the PRC market, a QFI must arrange to open accounts with its PRC Custodian after obtaining the QFI Licence from CSRC and registering with SAFE, respectively. The PRC Custodian may, upon the request of the QFI, open and maintain a basic RMB deposit account, designated RMB special account(s) and/or corresponding foreign exchange account(s), where necessary. A QFI should also apply (through the PRC Custodian) to the CSDCC (the equities depository institution) to open securities account(s) and CCDC/SHCH/CFETS for bond accounts and CIBM trading accounts. Once all of these are in place, a QFI may start making investments.

4.3.4 Appointment of intermediaries

(1) PRC Custodian

A QFII/RQFII is required to appoint a PRC Custodian to hold its cash and RMB denominated securities. In practice, the PRC Custodian will help the QFI process the relevant CSRC and SAFE applications or registrations[30] as well. Under the prevailing rules, a QFI may appoint more than one PRC Custodian.[31]

29 See Section 4.3.4 below for further information on the role of the PRC Custodian.
30 See Sections 4.3.3(1) and 4.3.3(2) above.
31 In such case, the QFI needs to select one of the PRC Custodians as the main custodian to perform the relevant formalities.

PRC Custodians are major Chinese commercial banks. They are responsible for the segregation and safekeeping of the securities and cash of each QFI.

In addition to normal custody services, a PRC Custodian is also required by PRC regulators to monitor QFIs' compliance status and report/file information about their investments in China (including derivatives or structured products traded outside China but which reference PRC securities).

(2) Settlement agent

QFIs that intend to access the CIBM are required to engage a settlement agent and complete a filing with PBC.

It is common, though not mandatory, that the PRC Custodian is appointed to serve concurrently as the Settlement Agent to provide the QFIs with trading and settlement agency services for its CIBM investments.

The Settlement Agent is responsible for assisting the QFIs in applying to PBC for the qualification to trade CIBM bonds, opening the bond custody accounts and trading accounts and filing with PBC in relation to the opening of accounts.

The Settlement Agent also executes transactions on the CFETS system on behalf of QFIs and settles transactions through CCDC/ SHCH.

The Settlement Agent is also required by PRC regulators to undertake an active monitoring role similar to the PRC Custodian. As the Settlement Agent role is a combination of custodian and broker, it is often intertwined with that of the PRC Custodian. Accordingly, co-ordination is required if two different entities are appointed to the respective roles.

(3) Broker

Furthermore, a QFI is required to appoint one or more onshore securities/futures companies as its broker(s) for onshore securities/futures trading. In addition to providing brokerage services, such brokers are also responsible for monitoring the QFI's securities/futures trading activities on behalf of PRC regulators.

4.3.5 Investing in CIBM

If a qualified investor chooses to access the CIBM in its capacity as a QFI, it will need to comply with the PBC Announcement 2016 No.3, PBC SH Rules 2016 No.2 and SAFE Notice 2016 No.12. At the same time, it remains subject to the QFI regime's specific restrictions and compliance requirements.

Upon the QFI's request, the Settlement Agent should submit the filing application to PBC Shanghai Head Office for access (the "**Access Filing**"). The Settlement Agent will have to apply the general principles of "Know Your Client", "Know Your Business" and due diligence to conduct the eligibility assessment at its own discretion. After receipt of the filing notification certificate (the "**PBC Filing Certificate**") issued by PBC upon completion of the Access Filing (which usually takes up to 20 working days after the Access Filing has been officially lodged with PBC), the Settlement Agent should then upon the QFI's request register with SAFE through the Capital Account Information System, according to the SAFE Notice 2016 No.12.

The Settlement Agent should open a bond account and cash settlement account with CCDC and SHCH respectively. These will be used to hold bonds and cash for settlement. The operation of the bond account and the settlement account will be handled by the Settlement Agent on behalf of the QFIs. The Settlement Agent should also apply to CFETS to open a bond trading account.

Once the Access Filing is completed and all the accounts opened, the QFI may invest in the CIBM in accordance with relevant laws and regulations. PBC Shanghai Head Office together with CFETS and the clearing houses will monitor the Settlement Agents and QFI to ensure continuing compliance by means of conversation/meeting, on-site inspection and so on.

4.3.6 Key legal & regulatory issues

(1) Remittance and repatriation

As the restriction on foreign exchange quotas has been formally repealed, there is no specific time limit for remitting funds into China under the current consolidated QFI regime.

In the past, certain repatriation restrictions were imposed on QFII/ RQFIIs (such as a monthly repatriation limit of 20%). However, these have been removed and the three-month lock-up period for investment principal repatriation is also no longer in force.

Currently, a QFI is permitted to repatriate the investment principal and profits subject to tax clearance or filing. The required documents in terms of the repatriation of investment profits are simplified by replacing the special audit report on investment return issued by a Chinese certified public accountant and the tax clearance or tax filing certificate with a self-commitment letter on paying taxes in full signed by the QFI (except in the case where the QFI winds up the entire portfolio).

(2) Non-trade transfer

PBC and SAFE issued the *Circular of the People's Bank of China and the State Administration of Foreign Exchange on Matters Relating to Further Facilitating Investment of Foreign Institutional Investors in the Interbank Bond Market* in September 2019, allowing the transfer of CIBM bonds and cash of a single foreign institutional investor between its QFII/ RQFII (now QFI) and CIBM Direct accounts. This circular also indicates that where a foreign institutional investor invests in the CIBM through both the QFII/RQFII (now QFI) regime as well as the CIBM Direct regime, it only needs to make a single filing with PBC SH Head Office. As a related matter, CCDC and SHCH have issued implementing rules on non-trade transfer of CIBM bonds in October 2019.

(3) Beneficial ownership

In this regard, this issue was first clarified following a FAQ issued by CSRC in May 2016 (the "**FAQ**"). The FAQ confirms that the legal relationship between the beneficial owner of securities (the overseas investor) and the nominee holder (the manager of the QFI), including the arrangements to segregate client assets from those of the manager, will be defined by and construed from the governing law of the agreements entered into by the parties. CSRC fully respects the contracts' provisions, including those concerning investors' rights and interests over the relevant assets.

In addition, the QFI Implementing Rules explicitly provide that a QFI may choose to open accounts in the form of "QFI–Client Name" or "QFI–fund". This rule further helps demonstrate that assets in these accounts belong to the relevant beneficial owner, and that they are separate from and independent of those of the manager.

According to the QFI Measures and QFI Implementing Rules, for the securities investment made in China by Qualified Foreign Institutional Investors, a nominee holder (i.e., a QFI managing clients' assets) must periodically report the actual investor/fund's name, place of domicile, asset allocation and securities investment situation to CSRC and SSE/SZSE.

4.3.7 Conclusion

The QFI regime is an important regime under which international investors can access the CIBM. Recent milestone reforms establishing the combined and consolidated QFI regime have removed many of the obstacles that have restricted QFIIs/RQFIIs from expanding their China business and/or applying more diversified and flexible investment strategies. Specifically, with the streamlined regulatory framework and the availability of bond futures/options and other financial derivatives under the new QFI regime, we expect the combined and consolidated QFI regime to become more advantageous for international institutions looking to execute fixed-income investment strategies in China.

Annex I - Comparison of the three access schemes into China's Interbank Bond Market

	CIBM Direct	Bond Connect	QFI
Key regulators	PBC SH Head Office (record filing made by a Settlement Agent) and SAFE	PBC SH Head Office (filing facilitated by BCCL and CFETS)	CSRC (approves application), PBC and SAFE (regulate FX-related matters)
Eligible overseas investors	OIIs, including: • foreign central banks, international financial institutions and sovereign wealth funds; • foreign commercial banks, insurance companies, securities companies, fund management companies, other asset management companies and other overseas medium and long term institutional investors (including QFIIs and RQFIIs).		QFI holders, including • foreign fund management companies, commercial banks, insurance companies, securities companies, futures companies, trust companies • foreign government-funded investment institutions, sovereign wealth funds • foreign pension funds, charitable foundations, donation funds • international organizations, and other institutions recognized by the CSRC
Investment scope	• Any product that is traded on the CIBM (including ABS)		
	• Bond forwards, bond lending, interest rate forwards, interest rate swaps and FX derivatives for hedging purposes • CIBM bond repos (only permitted for certain OIIs such as offshore Renminbi clearing banks (人民币清算行), offshore Renminbi participating banks (人民币参加行), foreign central banks and monetary authorities, international financial institutions and sovereign wealth funds (外国央行及主权类机构))		• Shares, bonds, warrants, depository receipts, bond repo, ABS traded on stock exchanges; • Shares and other types of securities admitted on the National Equities Exchange and Quotations; • Bond forwards, bond lending, interest rate forwards, interest rate swaps and FX derivatives for hedging purposes traded on the CIBM; • Public securities investment funds and private investment funds; • Financial futures and commodity futures traded on futures exchanges as approved by CSRC; • Listed options; • Permitted FX derivative for hedging purposes; • Securities borrowing and margin trading on stock exchange market; • Securities lending to securities finance company on stock exchange market; • Other financial instruments approved by the CSRC.
CIBM investment currency	CNY (converted from foreign currency) and CNH		CNY (converted from foreign currency) and CNH
Investment quotas	None		
CIBM clearing & settlement	Direct clearing & settlement	Through CMU as the nominee holder	Direct clearing & settlement

	CIBM Direct	Bond Connect	QFI
Legal / Beneficiary ownership	• Assets are held in segregated and dedicated accounts, which are opened with the name of the institutional investor or the fund/client account	• Arrangement between nominee holder (i.e. CMU) and beneficial owner is recognised • Legal relationship between CMU participants and CMU shall be governed by Hong Kong law	• Assets are held in segregated and dedicated accounts, which are opened with the name of the QFI - fund/client account • Arrangement between nominee holder and beneficial owner is recognised • Legal relationship between beneficial owner and QFI nominee holder governed by the asset management agreement (parties can select governing law for this agreement)
Scope of counterparties	No specific restriction	Onshore Bond Connect Dealers only	No specific restriction
Inter-connectivity with other onshore markets	Non-trade bond/cash transfer between accounts under the QFII/RQFII and CIBM Direct regimes is permitted to facilitate future consolidation of CIBM Direct and QFII/RQFII regimes	None for the time being	• Sale proceeds/coupon income can be invested into other permissible investments (such as A-shares and other products of securities market) without cross-border remittance • Non-trade bond/cash transfer between accounts under the QFI and CIBM Direct regimes is permitted to facilitate future consolidation of CIBM Direct and QFI regimes
Hedging possibility	Permitted (trading RMB/FX derivatives with the settlement agent and other qualified onshore financial institutions on a “real demand” basis for the purpose of hedging the FX risk exposure)	Permitted (hedging the FX risks exposures with the Hong Kong settlement banks only; Hong Kong settlement banks may then square the positions generated from such trades in PRC onshore market on a “real demand” basis under the northbound trading)	Permitted (trading FX derivatives with onshore custodians/other financial institutions on a “real demand” basis for the purpose of hedging the FX risk exposure)

Annex II - Glossary

Abbreviation	Refer to
CCDC	China Central Depository & Clearing Limited
CFETS	China Foreign Exchange Trade System
CIBM	China Interbank Bond Market
Consultation Papers	*Administrative Measures of Domestic Securities and Futures Investment by QFII and RQFII (Consultation Paper)* and the draft implementing rules promulgated by the CSRC
CSDCC	China Securities Depository and Clearing Company Limited
CSRC	China Securities Regulatory Commission
CIBM Direct	the route for OIIs to access onshore bonds via the CIBM directly
CST	China Standard Time
CIFM	China Interbank Forex Market
CDS	Credit Default Swap
CLN	Credit Linked Notes
CRM	Credit Risk Mitigation
CRMW	Credit Risk Mitigation Warrant
CRMA	Credit Risk Mitigation Agreement
CP	Short-term Commercial Paper
CGB	China Government Bond
CDB	China Development Bank Bond
DEPO	Deposit Rate
DVP	Delivery versus Payment
EIT	Enterprise Income Tax
FX	Foreign Exchange
LGB	Local Government Bond
LPR	Loan Prime Rate
MOF	Ministry of Finance
MOF and STA Notice 2018 No. 108	MOF and STA Notice on the Policy of Enterprise Income Tax (EIT) and Value-added Tax (VAT) relating to Overseas Institutional Investors' Investment in the Interbank Bond Market (Caishui [2018] No. 108)
MTN	Medium Term Notes
NAFMII	National Association of Financial Market Institutional Investors
NEEQ	National Equities Exchange and Quotations
OII	Overseas Institutional Investor
PBC	People's Bank of China

Abbreviation	Refer to
PBC Announcement 2016 No. 3	PBC Announcement on the Relevant Issues concerning the Further Improvements to the Investment in the CIBM by Foreign Institutional Investors (PBC Announcement [2016] No. 3)
PBC Notice 2015 No. 220	PBC Notice on Relevant Issues concerning the Investment in the Interbank Bond Market with RMB Funds by Foreign Central Banks, International Financial Institutions and Sovereign Wealth Funds (PBC YinFa [2015] No. 220)
PBC Q&A	People's Bank of China's Questions and Answers regarding the Investment in the CIBM by Overseas Institutional Investors
PBC SH Head Office	Shanghai Head Office of PBC
PFB	Policy Financial Bond
PPN	Private Placement Notes
PRC	People's Republic of China
QFI	Qualified Foreign Investor
QFI FX Rules	Administrative Rules on Foreign Institutional Investors' Domestic Securities and Futures Investment Funds
QFI Implementing Rules	Announcement No. 63 [2020] of the China Securities Regulatory Commission—Provisions on Issues concerning the Implementation of Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors (QFII) and RMB Qualified Foreign Institutional Investors (RQFII)
QFI Measures	Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors (QFII) and RMB Qualified Foreign Institutional Investors (RQFII)
QFII	Qualified Foreign Institutional Investor
QFII FX Rules	Foreign Exchange Administrative Provisions on the Domestic Securities Investment by Qualified Foreign Institutional Investors
RCPMIS	Renminbi Cross-border Payment & Receipt Management Information System
Repo	repurchase transaction
RMB or CNY	Renminbi, the lawful currency of China
RQFII	Renminbi Qualified Foreign Institutional Investor
RQFII FX Circular	Circular of the People's Bank of China and the State Administration of Foreign Exchange on the Domestic Securities Investment by RMB Qualified Foreign Institutional Investors
SAFE	State Administration of Foreign Exchange
SAFE Notice 2017 No. 5	SAFE Notice on the Relevant Issues concerning the Foreign Exchange Risk Management for Overseas Institutional Investors in the Interbank Bond Market (SAFE Huifa [2017] No. 5)
SAFE Notice 2016 No. 12	SAFE Notice on the Relevant Foreign Exchange Issues concerning the Investment in the Interbank Bond Market by Overseas Institutional Investors (SAFE Huifa [2016] No.12)
SCP	Super short-term Commercial Paper
SHCH	Shanghai Clearing House
SSE	Shanghai Stock Exchange
STA	State Taxation Administration
SZSE	Shenzhen Stock Exchange
VAT	Value-added Tax

Annex III - Definition of terms

Term	Definition
Asset-backed Securities	A form of financing for the issuance of tradable securities, backed by a specific portfolio of assets or a specific cash flow.
Asset-backed Notes	Refers to a securitized financing instrument issued by a non-financial business through a special purpose vehicle in a structured manner, the cash flows derived from underlying assets are payment source, principal and interest are paid as agreed.
Asset-backed Plan	Refers to the business activity in which a professional asset management institution such as an insurance asset management company establishes an asset-backed plan as the trustee, with cash flows derived from underlying assets as the repayment source, and issues beneficiary certificates to qualified investors such as insurance institutions.
Asset-Backed Special Plan	A business takes assets such as rights to proceeds or creditor's rights as its underlying assets, and the cash flows derived as the basis for repayment, and transforms them into securities that can be sold and circulated in financial markets through structured transaction and credit enhancement measures.
Auto ABS	Refers to a securitized financing instrument that a financial institution such as a commercial bank and an auto finance company in China, acting as the originator, entrusts personal auto loans (including credit card instalment auto loans and auto mortgages) to the trustee, and the latter issues beneficiary securities to institutional investors in form of asset-backed securities, and pays proceeds of asset-backed securities with cash derived from the personal auto loans.
Business Loans Asset-backed Securities	Refers to a securitized financing instrument that a banking financial institution and other financial institution recognized by the regulatory authorities in China, acting as the originator, entrusts non-revolving small- and micro-business loans to the trustee, and the latter issues asset-backed securities to investors, and pays principal and interests of asset-backed securities with cash derived from the small- and micro-business loans asset pool.
Consumer Loans ABS	Refers to a securitized financing instrument that a banking financial institution in China, acting as the originator, entrusts consumer loans to the trustee, and the latter issues beneficiary securities to institutional investors in form of asset-backed securities, and pays proceeds of asset-backed securities with cash derived from the consumer loans.
Credit Asset-Backed Securities	A banking financial institution takes credit assets and mortgages and subordinated security interests as underlying assets, and the cash flows derived as the basis for repayment, and transforms them into securities that can be sold and circulated in financial markets through structured transaction and credit enhancement measures.
Fund Depositary Institution	An institution that is entrusted by a trustee and responsible for managing the fund of entrusted assets accounts.
Lead Underwriter	An institution that exclusively underwrites or organizes the underwriting syndicate in distributing securities.
Loan Servicer	An organization that is entrusted by a trustee and responsible for managing the loan. The loan servicer may be the originator of credit asset-backed securities.
Non-performing ABS	Refers to a securitized financing instrument that a banking financial institution and other financial institution recognized by the regulatory authorities in China, acting as the originator, entrusts NPLs to the trustee, and the latter issues beneficiary securities to institutional investors in form of asset-backed securities, and pays proceeds of asset-backed securities with cash derived from the NPLs.
Originator	An institution that issues asset-backed securities by setting up a special purpose trust.
Rating Institution	A qualified rating institution that is hired by a principal or a trustee to rate asset-backed securities.
Revolving Assets	The borrower can borrow or repay the loan multiple times, at any time within the limit, and the credit line can be recycled.

Term	Definition
Revolving Purchase Structure	A trustee may repurchase qualified underlying assets several times with the principal recovered or principal and interest recovered (which may include excess proceeds) according to the standards stipulated in the transaction contract and incorporate them into the asset pool within the duration of the trust.
RMBS	Refers to a securitized financing instrument that a banking financial institution in China, acting as the originator, entrusts personal housing mortgages to the trustee, and the latter issues beneficiary securities to institutional investors in form of asset-backed securities, and pays proceeds of asset-backed securities with cash derived from the personal housing mortgages.
Target Balance	One or two of certain senior tranches sets (set) a target balance on the amortization date, which enables the allocatable amounts to firstly pay the principal of the senior tranche to the target balance, and the remaining amounts will be used to pay the principal of other senior tranches. If allocatable amounts are insufficient to pay the target balance, they will be replenished to the current target balance in the next period. Strictly speaking, the target balance is a fixed amortization, but it differs from fixed amortization in that the cash flow can generally reach the target balance under certain early repayment assumptions.
Trustee	An organization entrusted for managing specific purpose trust assets and issuing asset-backed securities.

Annex IV - Relevant laws and regulations

Laws and Regulations	Published by	Description
Rules for Registration and issuance		
Measures for the Administration of Financial Bond Issuance in the National Interbank Bond Market	PBC	General requirements for issuing financial bonds in the CIBM
Measures for the Administration of Debt Financing Instruments of Non-financial Enterprises in the Interbank Bond Market	PBC	General provisions on the issuance, transaction, custody and settlement of debt financing instruments of non- financial enterprises in the CIBM
Interim Measures for the Administration of Bond Issuance by Overseas Issuers on the National Interbank Bond Market	PBC MoF	General requirements for issuing panda bonds in the CIBM
Announcement on Matters concerning the Issuance of Green Financial Bonds in the Interbank Bond Market	PBC	General requirements for issuing green bonds in the CIBM
Rules for the Registration and Issuance of Debt Financing Instruments of Non-financial Enterprises in Interbank Bond Market	NAFMII	Provisions on matters relating to registration for public issuance and private placement of various DFI
Rules and Procedures for the Registration of Debt Financing Instruments of Non-financial Enterprises for Public Issuance in Interbank Bond Market		
Non-financial Enterprises in the Interbank Bond Market		
Provisions for the Selection of Specialized Institutional Investors of Private Placement Debt Financing Instrument (2018)		
Guidelines on Debt Financing Instruments of Overseas Non-Financial Enterprises (for Trial Implementation)		
Guidelines on Green Note of Non- financial Enterprises		
Guidelines on the Issuance Standards of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Market		
Guidelines on Book-Building Issuance of Debt Financing Instruments by Non-Financial Enterprises		
Model Investor Protection Covenants (2019)	NAFMII	Recommended terms to be included by the issuer in the prospectus to enhance investor protection
Rules for Post-issuance Supervision		
Notice of the People's Bank of China on the post-issuance management of Green Financial Bonds	PBC	Post-issuance management, evaluation and certification related rules of green bonds
Guidelines for the Assessment and Certification of Green Bonds (for interim implementation)	PBC CSRC	

Laws and Regulations	Published by	Description
Rules for Information Disclosure of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Bond Market	NAFMII	Relevant rules for DFI post- issuance management
Procedures for Holders' Meeting of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Bond Market		
Self-Regulatory Guidelines for Credit Rating Services relating to Debt Financing Instruments of Non- Financial Enterprises		
Rules for the Registration and Evaluation of Credit Rating Agencies of Non-financial Enterprise Debt Financing Instruments in the Interbank Bond Market		
Rules for the Credit Rating Information Disclosure of Debt Financing Instruments of Non- Financial Enterprises in the Interbank Bond Market		
Self-Regulatory Convention for Credit Rating Agencies of Debt Financing Instruments of Non-Financial Enterprises		
Rules for the Conflict of Interests for Credit Rating Agencies of Debt Financing Instruments of Non-Financial Enterprises in the Interbank Bond Market		
Self-Disciplinary Rules for Debt Financing Instruments of Non- Financial Enterprises in the Interbank Bond Market		
Rules for the Administration of Experts for Self-Disciplinary Meeting in Non-Financial Enterprises Debt Financing Instruments Market	NAFMII	Relevant rules for DFI post- issuance management
Rules for Secondary Market Trading		
Measures for the Administration of Bond Transactions in the National Interbank Bond Market	PBC	Regulating pledged repo behavior in the CIBM
Regulations on the Outright Bond Repo in the Chinese Interbank Bond Market		Regulating pledged repo behavior in the CIBM
Announcement on the Pledged Bond Repo Transactions in the Chinese Interbank Market		Regulating pledged repo behavior in the CIBM
Rules on the Bond Transactions in the Chinese Interbank Market	CFETS	Detailed rules for engaging in bond transactions within the CFETS system
Self-Regulatory Rules for Bond Trading in the Interbank Bond Market	NAFMII	Self-regulatory management rules for bond trading and market making in the CIBM
Guidelines on Market Making Business in the Interbank Bond Market		
Master Agreement for Financial Derivatives Trading in China's Interbank Market		Texts of the master agreements to be signed for derivatives trading and repo transactions in the CIBM
Master Agreement for Financial Derivatives Trading in China's Interbank Market (For Warrants)		
Master Agreement for Bond Repurchase in China's Interbank Market (2013)		

<table>
<tr><th>Laws and Regulations</th><th>Published by</th><th>Description</th></tr>
<tr><td>Guidelines for the Pilot Program of Interbank Market Credit Risk Mitigation Instruments</td><td rowspan="6">NAFMII</td><td rowspan="6">Operational rules related to interbank market credit risk mitigation instruments</td></tr>
<tr><td>Guidelines for the Issuance of Credit Risk Mitigation Agreement</td></tr>
<tr><td>Guidelines for the Issuance of Credit Risk Mitigation Warrant</td></tr>
<tr><td>Guidelines on the Issuance of Credit Default Swap</td></tr>
<tr><td>Guidelines on the Issuance of Credit-Linked Note</td></tr>
<tr><td>Basic Terminologies and Applicable Rules for Credit Derivatives Trading in China's OTC Market (2016)</td></tr>
<tr><td>Operational Guidance on Enforcement of Collateral (Trial)

Operational Procedures of Enforcement of Collateral by Auction</td><td>CCDC</td><td>Default Rules concerning collateral enforcement in the CIBM</td></tr>
<tr><td>Implementing Rules on Enforcement of Bonds underlying Repurchase Agreements (Trial)

Implementing Rules on Auction of Bonds underlying Repurchase Agreements (Trial)</td><td>SHCH</td><td>Default Rules concerning collateral enforcement in the CIBM</td></tr>
<tr><td>Implementing Rules on Enforcement of Bonds underlying Repurchase Agreements (Trial)</td><td>CFETS</td><td>Default Rules concerning collateral enforcement in the CIBM</td></tr>
<tr><td>Joint Announcement of the People's Bank of China and Hong Kong Monetary Authority-On Approving China Foreign Exchange Trade System & National Interbank Funding Centre, China Central Depository & Clearing Co.,
Ltd, Shanghai Clearing House (together the "Mainland Financial Infrastructure Institutions"), together with Hong Kong Exchanges and Clearing Limited and Hong Kong Central Money markets Unit (together the "Hong Kong Financial Infrastructure Institutions"), to collaborate in establishing mutual bond market access between Hong Kong and Mainland China (Bond Connect).</td><td>PBC
HKMA</td><td>Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect</td></tr>
<tr><td>Interim Measures for the Administration of Mutual Market Access between Mainland China and Hong Kong Bond Markets</td><td rowspan="4">PBC</td><td rowspan="4">Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect</td></tr>
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<tr><td>"Bond Connect" Market Access Handbook - Guidelines and Forms</td><td rowspan="2">CFETS</td><td rowspan="2">Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect</td></tr>
<tr><td>National Interbank Funding Center "Bond Connect" Trading Rules (for Trial Implementation)</td></tr>
</table>

Laws and Regulations	Published by	Description
Rules on Registration, Custody and Settlement Operations of "Bond Connect" (Northbound Connect)	CCDC	Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect
Notice on Implementing the Interim Procedures for the "Bond Connect" Settlement Operation of the People's Bank of China		
Implementation Rules for the Registration, Custody, Clearing and Settlement Operations for Mutual Bond Market Access between the Mainland China and Hong Kong Bond Markets (for Trial Implementation)	SHCH	Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect
Operational Guidelines for "Bond Connect" (Northbound Connect) of Shanghai Clearing House Co., Ltd.		
Circular of the People's Bank of China and the State Administration of Foreign Exchange of Matters Relating to Further Facilitating Investment of Foreign Institutional Investors in the Interbank Bond Market	PBC SAFE	Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect
Notice of the People's Bank of China on Issues Concerning the Pilot Program on Investment in the Interbank Bond Market with RMB Funds by Three Types of Institutions Including Overseas RMB Clearing Banks	PBC	Relevant arrangements for overseas investors to invest in the CIBM through Bond Connect
Notice of the People's Bank of China concerning the Bond Repurchase Transactions in the Interbank Bond Market by the Overseas RMB Clearing Banks and Overseas Participating Banks	PBC	Relevant arrangements for overseas investors to invest in the CIBM through CIBM Direct scheme
Notice of the People's Bank of China concerning the Investment in the Interbank Bond Market with RMB Funds by Foreign Central Banks, International Financial Institutions and Sovereign Wealth Funds		
Announcement of the People's Bank of China on Issues concerning the Further Improvements to the Investment in the Interbank Bond Market by Foreign Institutional Investors		
People's Bank of China's Questions and Answers regarding the Investment in the Interbank Bond Market by Overseas Institutional Investors		
People's Bank of China Shanghai Headquarters Announcement [2015] No. 1 (Interbank Access Filing System)		
Implementing Rules on Filing Requirements for the Investment in the Interbank Bond Market by Overseas Institutional Investors		
Relevant Requirements for Simplifying the Filing of Overseas investors Accessing China's Interbank Bond Market		

Laws and Regulations	Published by	Description
Announcement on Matters concerning the Management of the Filing of Overseas investors Accessing China's Interbank Bond Market	PBC	Relevant arrangements for overseas investors to invest in the CIBM through CIBM Direct scheme
Procedures of Entering the Interbank Bond Market for Overseas Commercial Institutional Investors		
Operational Guidelines for Networking and Account Opening of Foreign Institutional Investors in the Interbank Market	CCDC SHCH CFETS	Relevant arrangements for overseas investors to invest in the CIBM through CIBM Direct scheme
SAFE Notice on the Relevant Foreign Exchange Issues concerning the Investment in the Interbank Bond Market by Overseas Institutional Investors	SAFE	Relevant arrangements for overseas investors to invest in the CIBM through CIBM Direct scheme
SAFE Notice on the Relevant Issues concerning the Foreign Exchange Risk Management for Overseas Institutional Investors in the Interbank Bond Market		
Circular on Improving the Foreign Exchange Risk Management of Foreign Institutional Investors in the Interbank Bond Market (Consultation Papers)		
Measures for the Administration of Securities Investment Made in China by Qualified Foreign Institutional Investors	CSRC	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
Provisions on Issues concerning the Implementation of the Administrative Measures for Securities Investment Made in China by Qualified Foreign Institutional Investors		
Notice on the Relevant Issues concerning the Registration and Settlement of Domestic Securities Transactions Made in China by Qualified Foreign Institutional Investors		
Administrative Rules on the Domestic Securities Investment in Foreign Exchange by Qualified Foreign Institutional Investors	SAFE	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
China Securities Depository and Clearing Corporation Limited's Implementation Rules for Registration and Settlement of Domestic Securities Investments of Qualified Foreign Institutional Investors	CSDCC	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
Measures for the Pilot Program of Securities Investment Made in China by RMB Qualified Foreign Institutional Investors	CSRC	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
Regulations on the Implementation of Measures for the Pilot Program of Securities Investment Made in China by RMB Qualified Foreign Institutional Investors		
Circular of the People's Bank of China and the State Administration of Foreign Exchange on the Domestic Securities Investment of RMB Qualified Foreign Institutional Investors	PBC SAFE	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime

Laws and Regulations	Published by	Description
Shanghai Stock Exchange Implementation Rules of Securities Transactions by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors	SSE	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
Shenzhen Stock Exchange Implementation Rules of Securities Transactions by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors	SZSE	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
Administrative Measures of Domestic Securities and Futures Investment by QFII and RQFII (Consultation Paper and the Implementing Rules)	CSRC	Relevant arrangements for overseas investors to invest in the CIBM through the QFII/ RQFII regime
MOF and STA Notice on the Policy of Enterprise Income Tax (EIT) and Value-added Tax (VAT) Relating to Overseas Institutional Investors' Investment in the Interbank Bond Market	MoF STA	Tax exemption policy for overseas investors
Selected Regulatory and Self-disciplinary Documents on Asset-backed Securities		
Notice on the Relevant Issues concerning the Pilot Program of the Asset-backed Securities by Securities Companies	CSRC	Clarifying the definition, basic requirements, underlying assets and transfer, product structure, and related subject responsibilities of corporate asset-backed securities.
Administrative Measures for the Pilot Program of Credit Asset- backed Securities	PBC CBIRC	Stipulating the operational process, and the participants, rights and obligations, issuance and transactions, and information disclosure of credit asset-backed securities. It marks the official launch of the pilot program of credit asset-backed securities in China.
Information Disclosure Rules for Assets-backed Securities	PBC	Clarifying the information disclosure content, method, time and other considerations of asset-backed securities issued and traded in the interbank bond trading market.
Notice on Relevant Matters concerning Further Expanding the Pilot Program of Credit Assets-backed Securities	PBC CBIRC MoF	It marks the launch of the second round of the pilot program of credit asset- backed securities.
Guidelines on Asset-Backed Notes of Non-Financial Enterprises in the Interbank Bond Market	NAFMII	Proposing corresponding provisions for asset-backed securities operation by non- financial enterprises in the interbank market, marking the official launch of the asset- backed notes.
Notice on Investment in Financial Products with Insurance Funds	CBIRC	Allowing investments in securitized financial products such as insurance asset management products and project asset-backed plans with insurance funds, and promoting the initial issuance of project asset-backed plans.
Notice on the Working Procedures of the Filing and Registration of Credit Asset-backed Securities	CBIRC	Clarifying that the credit asset-backed securities will be filed instead of being approved case by case.
Administrative Measures for the Filing of Asset-backed Special Plans, and its supporting documents: the Guidelines for Asset-backed Securities Operation Risk Control and the Guidelines for Negative List of Underlying Assets in Asset- backed Securities	AMAC	Implementing the filing system for corporate asset- backed securities, and carrying out negative list management.

Laws and Regulations	Published by	Description
Announcement on the Trial Implementation of Registration System of Credit Asset-backed Securities	PBC	Simplifying the issuance management process of credit asset-backed securities, marking the implementation of the registration system for issuance of credit asset- backed securities.
Information Disclosure Guidelines for Auto Loans Asset- Backed Securities (for Trial Implementation), Information Disclosure Guidelines for MBS (for Trial Implementation)	NAFMII	Stipulating that the trustee, the originator and the institution providing the securitization services should fully disclose relevant information regarding auto loans asset-backed securities and MBS in the registration, issuance and post-issuance periods in accordance with the requirements of the Guidelines and related tablet systems.
Information Disclosure Guidelines for Urban Renovation Projects Asset-Backed Securities (for Trial Implementation)	NAFMII	Stipulating key contents that need to be disclosed for urban renovation projects asset-backed securities from issuance to post-issuance periods.
Information Disclosure Guidelines for Consumer Loans Asset- Backed Securities (for Trial Implementation) and supporting tablet systems	NAFMII	Stipulating key contents that need to be disclosed for consumer loans asset-backed securities from issuance to post-issuance periods.
Information Disclosure Guidelines for Non-Performing Loans Asset- Backed Securities (for Trial Implementation) and supporting tablet systems	NAFMII	Providing specific operational guidelines for the pilot program of NPL asset-backed securities, and proposing detailed information disclosure standards for NPL asset-backed securities.
Information Disclosure Guidelines for Small- and Micro-Business Loans Asset-Backed Securities (for Trial Implementation) and supporting tablet systems	NAFMII	Under the framework of the previous credit asset-backed securities information disclosure rules, targeted institutional arrangements were made. Firstly, defining the underlying assets and the criteria for entering the pool; secondly, adding information on the historical static pool sampling loans of the originator; thirdly, adding the disclosure requirements for targeted loan policies and regulatory indicators of the originator.
Rules and Procedures for Evaluation of Information Disclosure of Credit Asset-Backed Securities (for Trial Implementation)	NAFMII	Applicable to evaluation on the information disclosure behaviors of relevant participants of credit asset- backed securities by the market members organized by NAFMII.
Guidelines on Asset-Backed Notes of Non-Financial Enterprises in the Interbank Bond Market (Revised) and supporting tablet systems	NAFMII	Mainly stipulating asset type, transaction structure, risk isolation, information disclosure of asset-backed notes, rights and obligations of all parties involved, and investor protection mechanisms.
Information Disclosure Guidelines for Consumer Loans Asset-Backed Securities (2019)	NAFMII	For the first time, the revolving assets were included in the ABS underlying assets category, further clarifying the information disclosure arrangements for consumer loans asset-backed securities with revolving assets.