A bigger role for the Renminbi
The new offshore Renminbi bond market (regularly called the Dim Sum market) was born in the middle of 2010 when the Chinese authorities lifted certain restrictions and made it feasible for a wider range of institutions to issue bonds. Prior to these reforms, the RMB was strictly a domestic currency with few international characteristics or opportunities for investment. Things are now changing and the currency is internationalising at a rapid pace. China’s ultimate ambition is to make the RMB a global reserve currency. The on-going internationalisation of the RMB is fortuitous because the world is keen to acquire new financial assets and the spectrum of investors from retail to central banks and sovereign wealth funds is looking to diversify away from the US dollar over time. Given the nature of this starting point and liquidity constraints, the shift away from the dollar’s global dominance will necessarily take time. But with China on track to become the world’s largest economy and exporter in the future, historical parallels imply a role for the RMB as an important reserve currency. This said, there is still much work to be done to achieve reserve currency status including opening up the capital account for international transactions.

FX policy changes picking up pace
Like most of China’s economic policy, changes in the approach to the currency have for the most part been unfolding gradually. The current foreign exchange regime now has greater flexibility and the authorities appear to be more prepared to allow the currency to appreciate than in the past, albeit gradually. Recently, on the regulatory front change seems to have gathered pace. China has set up currency swaps with many other countries including in Latin America and Asia and RMB bond issuance in Hong Kong (so-called ‘Dim Sum’ bonds) is growing as a first step towards creating a deep investable bond market for the RMB.

Projects for RMB settlement have also been in place for sometime. In 2009 RMB trade settlement schemes began in a number of mainland cities and Hong Kong participating banks were allowed to provide trade finance to foreign traders settling trades in RMB. As such changes proceed they will have the immediate advantage of reducing foreign exchange risk for Chinese companies that switch to RMB settlement. Last year there was a global roll-out of RMB trade settlement and an offshore RMB products platform was launched in Hong Kong. The RMB interbank market was also opened to selected offshore RMB holders and an RMB Overseas Direct Investment trial launched. In the coming years we expect to see a significant increase in global RMB trade settlement and increasing liquidity in the off-shore RMB bond market as Dim Sum bond issuance increases.

A rapidly growing bond market
The market cap of these bonds has been expanding rapidly from RMB29 billion in July 2010, to RMB61 billion at the end of 2010 and to more than RMB200 billion currently.
We expect the RMB bond market to continue to expand at pace in the future. The market has attracted a number of different types of issuers increasing diversification and improving liquidity. The Chinese government has issued bonds, as have the Chinese policy banks, commercial banks and corporate institutions. On top of this, the market has also attracted global issuers. Recent issues including Air Liquide in France, BP and Tesco in the UK and IDBI in India, have highlighted the market’s growing international appeal. Equally, it appears that investors also realise that if the onshore and offshore bond markets eventually merge, Chinese bonds will become an important global asset class.

In summary, Chinese policymakers are keen to internationalise the RMB and the process is already well underway. The offshore RMB bond market is central to the strategy to internationalise and there are likely to be major developments on this and other fronts in the coming years. This will open up new investment opportunities in what we believe is likely to remain one of the world’s most rapidly growing, dynamic economies. Investing in the offshore RMB bond market provides investors with exposure to the RMB and portfolio diversification, something that is hard to find in an increasingly correlated world.

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