Hong Kong Special Administrative Region
of the People's Republic of China

Report of the Steering Committee on Bond Market Development in Hong Kong

August 2022

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Chapter 1 – Executive Summary

The Steering Committee on Bond Market Development in Hong Kong

As a major international financial centre, with a sound legal and regulatory system, a deep and liquid capital market, robust financial infrastructure, and a wealth of financial intermediaries and talent, Hong Kong is credited with a vibrant equity market. At the same time, the bond market has seen steady development over the years, making Hong Kong top of the league in arranging Asian international issuances and first-time bond issuances by Asian issuers.

From a strategic perspective, the development of a modern bond market, along with the development of the equity market and the banking sector, will facilitate the efficient allocation of funds, thereby promoting financial stability, strengthening Hong Kong's status as an international financial centre and promoting economic development.

Against this backdrop, the Steering Committee on Bond Market Development in Hong Kong ("Steering Committee") was set up in August 2021 following the announcement in the 2021-22 Budget. The Steering Committee is chaired by the Financial Secretary and is tasked with formulating a roadmap for promoting the diversified development of Hong Kong's bond market and reinforcing its functions. Its membership and terms of reference are set out in **Annex A**.

Strategic Directions

The Steering Committee notes the Government's three-pronged approach in promoting Hong Kong's bond market development –

- **a.** Stimulating growth of the bond market through government issuances of debt instruments with varying diversity and maturity;
- **b.** Building market infrastructure to ensure a safe and efficient environment for trading and settlement and for connecting to major markets in the world; and
- **c.** Incentivising market development through an array of support measures.

Having reviewed various aspects pertaining to Hong Kong's bond market, including the local, regional and international market landscape, the strengths, opportunities and threats and existing support measures, the overall assessment of the Steering Committee is summarised as follows –

a. given the initiatives introduced over the years to develop the bond market, Hong Kong is now a major bond hub in Asia, with particular strength in primary issuance and arrangement of international bonds;

b. Hong Kong has a competitive ecosystem for the bond market, e.g. in terms of product authorisation and listing regime, government support measures, etc. Moreover, Hong Kong has successfully captured a significant share of business and talent in particular on the sell-side; and

c. looking ahead, the strategy for developing Hong Kong's bond market should focus on leveraging the opportunities presented by the Mainland market and other international trends. Enhancements should also be made to financial infrastructure and support measures to dovetail this strategy.

Based on the above comprehensive assessment, the Steering Committee makes 18 recommendations in three strategic directions of development with a suggested implementation time-frame with a view to further enhancing local bond market's competitiveness and bringing Hong Kong's bond market development to the next level. The strategic directions ("SD") and the corresponding recommendations are set out as follows –

SD1 — Leveraging the opportunities presented by the Mainland market and new global trends

- Expand government bond issuances (also SD2)
- Grow the green and sustainable and catastrophe bond market
- Attract Mainland entities for bond issuances
- Explore the provision of additional tax incentives to encourage the setting up of fixed-income funds in Hong Kong
- Develop bond-related markets as complements (also SD2)
- Participate in the setting of standards
- Attract and train up talent
- Step up promotional efforts

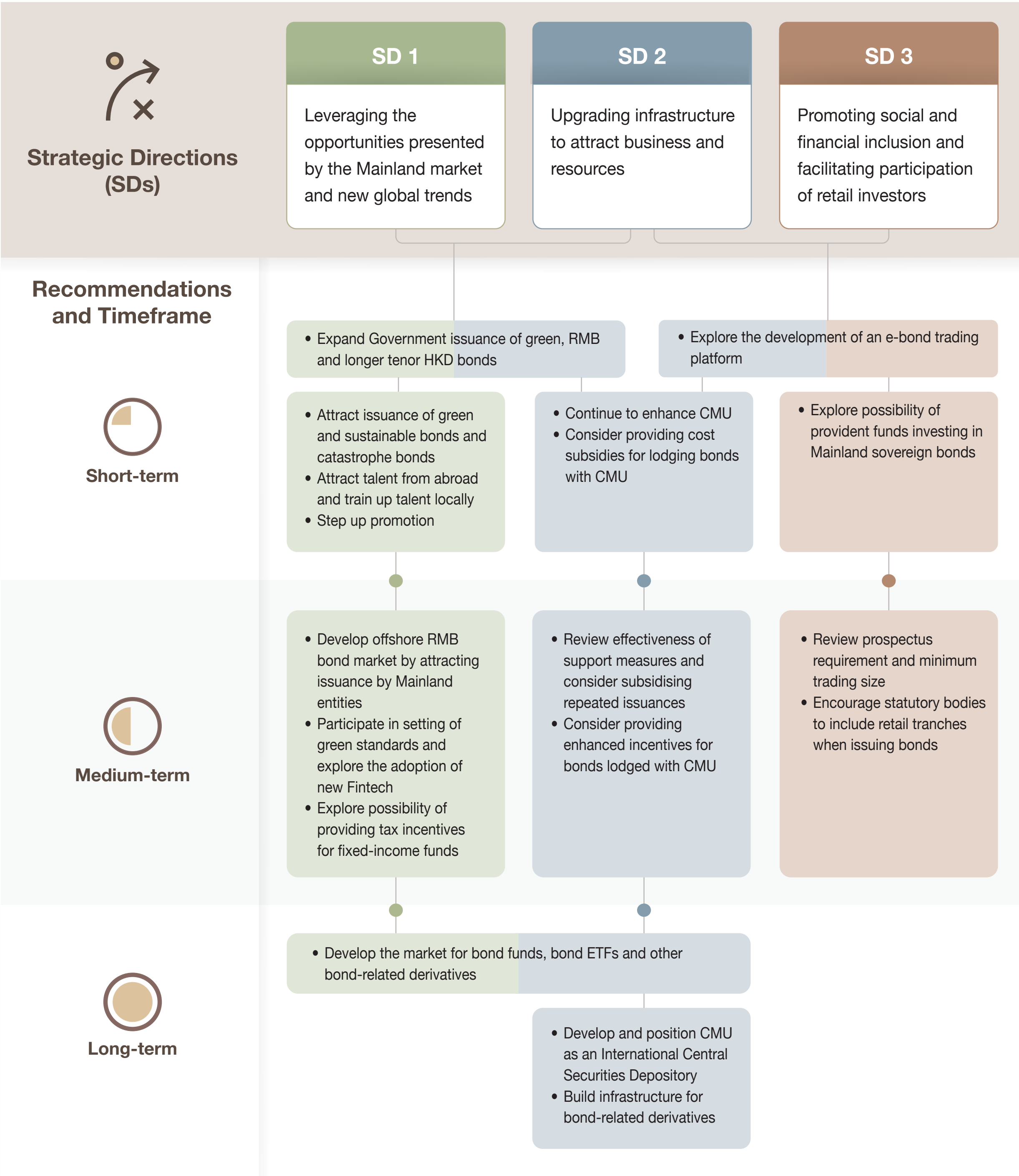
SD2 — Upgrading infrastructure to attract business and resources

- Review and enhance the support measures for issuers
- Enhance the functionalities of Central Moneymarkets Unit ("CMU")
- Subsidise lodgement at CMU
- Provide financial incentives for CMU users
- Develop CMU into a regional international central securities depository
- Explore the inception of electronic bond trading platforms (also SD3)
- Build the derivative infrastructure

SD3 — Promoting social and financial inclusion and facilitating participation of retail investors

- Enhance the Mandatory Provident Fund Scheme to allow wider scope of bond investments
- Encourage issuance of retail tranches
- Explore enhancements to the prospectus requirement

To this end, the Government and the relevant authorities will take forward the recommendations by developing specific details for implementation, and in the process continue to engage the industry, keep abreast of the dynamic in the market, and monitor any emerging opportunities and challenges on the international and local horizons.



Structure of the Report

The remainder of this report is structured as follows –

a. Chapters 2 to 4 present the Steering Committee's assessments and recommendations to the Government from three perspectives of market analysis, including market landscape of Hong Kong's bond market, bond market infrastructure and government support measures and promotion.

b. Chapter 5 concludes the report with the way forward.

c. A summary of the Steering Committee's strategic directions and recommendations is available in **Annex B**.

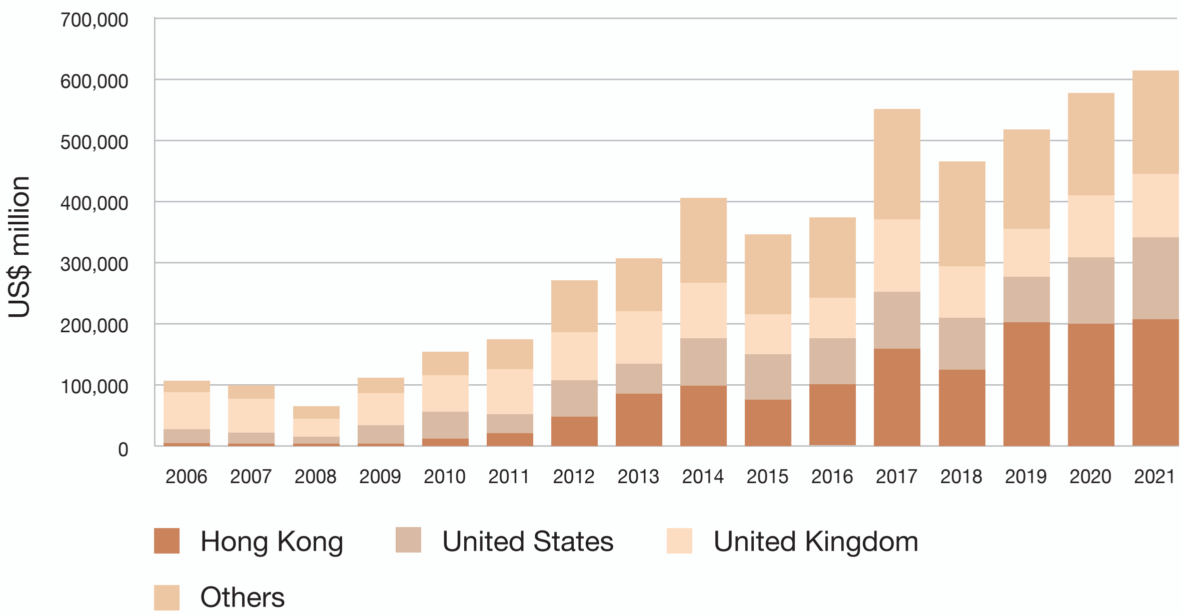
Chapter 2 – Market Landscape of Hong Kong's Bond Market

Overview of Hong Kong's Bond Market – Key Market Statistics

The Steering Committee considers that the volume of bond issuance in terms of arrangement is an important metric as it is the top of the value chain of the bond issuance process, involving much expertise and resources. On that, the Steering Committee notes that Hong Kong is particularly strong in arrangement of bonds distributed globally by Asian entities –

a. Hong Kong ranked 1st in the world both in terms of arranging Asian international bond issuances and arranging first-time bond issuances by Asian issuers[1] (See Charts 1 and 2 below); and

Chart 1: Hong Kong leads in arranging Asian international bonds

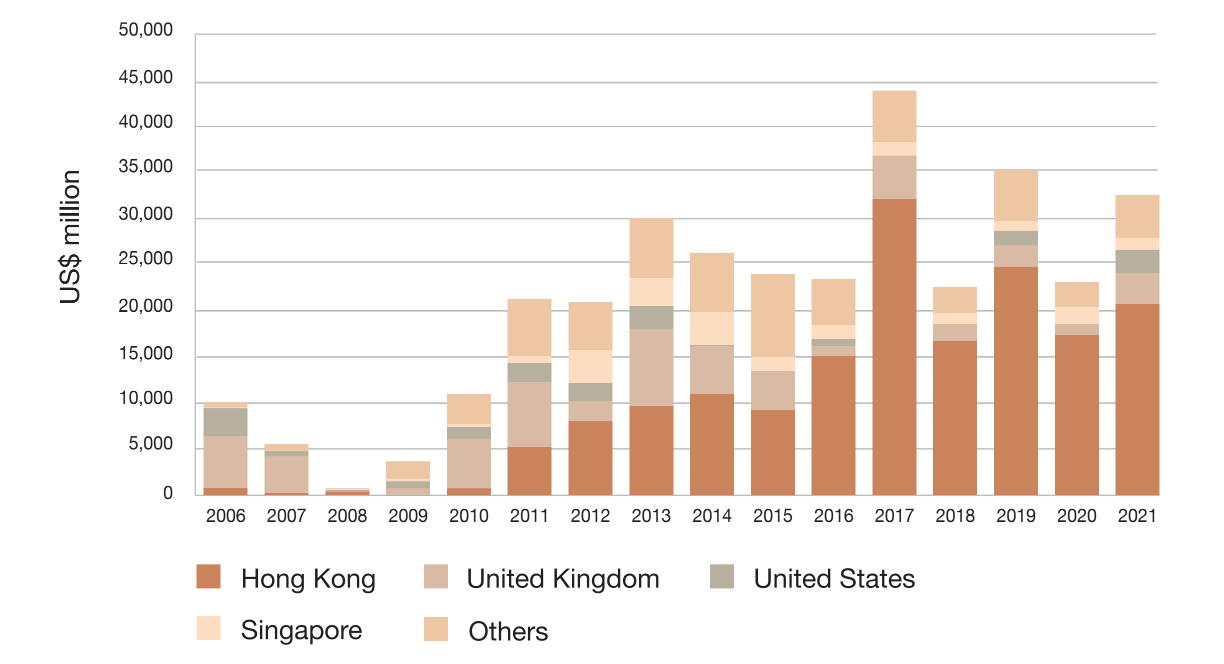


Figures of major arrangement locations in 2021

Main location of arrangement	Amount in US$ million	Market Share
Hong Kong	206,814	34%
United States	133,965	22%
United Kingdom	103,981	17%

1 Source: International Capital Market Association.

Chart 2: Hong Kong leads in arranging first-time international bonds issued by Asian issuers

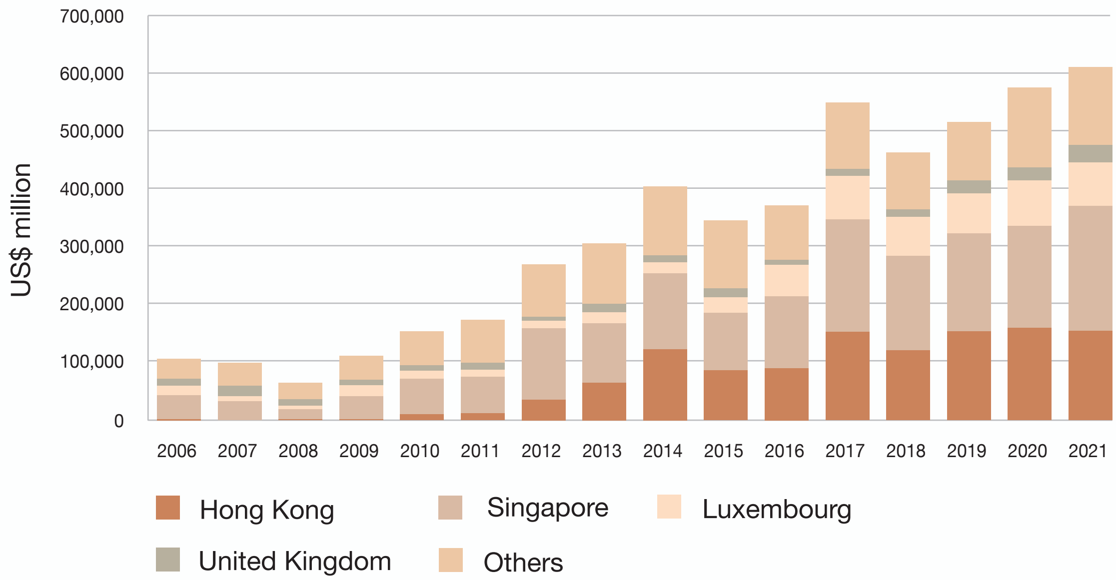


Figures of major arrangement locations in 2021

Main location of arrangement	Amount in US$ million	Market Share
Hong Kong	20,657	63%
United Kingdom	3,382	10%
United States	2,594	8%
Singapore	1,305	4%

b. Hong Kong ranked 2nd in the world in terms of listing of Asian international bonds[2] (See Chart 3 below).

Chart 3: Hong Kong ranks 2nd in listing Asian international bonds



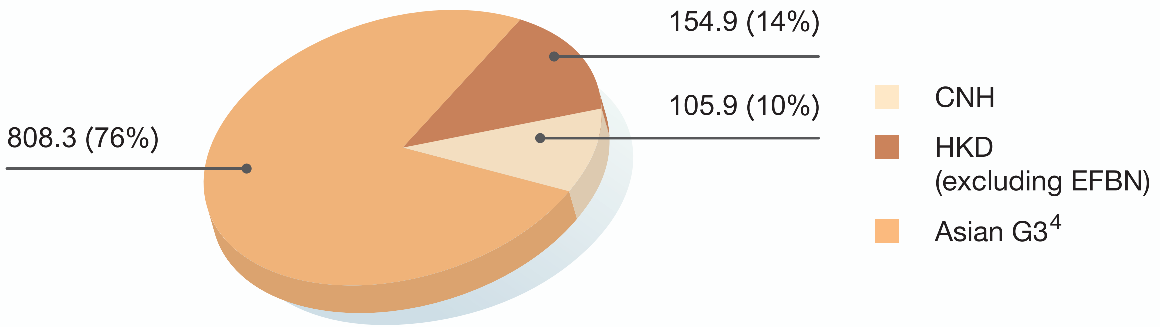
Figures of major listing locations in 2021

Listing location	Amount in US$ million	Market Share
Singapore	216,942	35%
Hong Kong	156,111	25%
Luxembourg	75,095	12%
United Kingdom	30,441	5%

With regard to the denomination of the bond issuances in Hong Kong, non-local currency bonds constitute a significant portion of Hong Kong's bond market. As at end-2021, excluding Exchange Fund Bills and Notes ("EFBN"), the outstanding size of bonds in Hong Kong amounted to US$1,069 billion, among which about 14% are denominated in Hong Kong dollar ("HKD"), 10% in Renminbi ("RMB"), and the remaining 76% in other currencies, mainly US dollar ("USD") and Euro[3] (See Chart 4 below).

2 Source: International Capital Market Association.
3 Sources: Bloomberg, CMU, Dealogic, Reuters and the Hong Kong Monetary Authority ("HKMA").

Chart 4: Outstanding size of bonds in Hong Kong at end-2021 by currency (in US$ billion)



Overview of Hong Kong's Bond Market – Market Characteristics

The Steering Committee notes the following market and structural factors behind the higher proportion of non-local currency bonds in Hong Kong's bond market –

a. The high market confidence in the Linked Exchange Rate System means currency mismatch risk (HKD versus USD) is regarded as minimal for issuers and investors to turn to the more liquid and hence more cost effective USD bond market;

b. Corporations in Hong Kong, and in Asia as well, generally rely on the very strong banking sector for funding. Compared to overseas markets, the interest in issuing bonds with meaningful size from big corporations in Hong Kong is much smaller; and

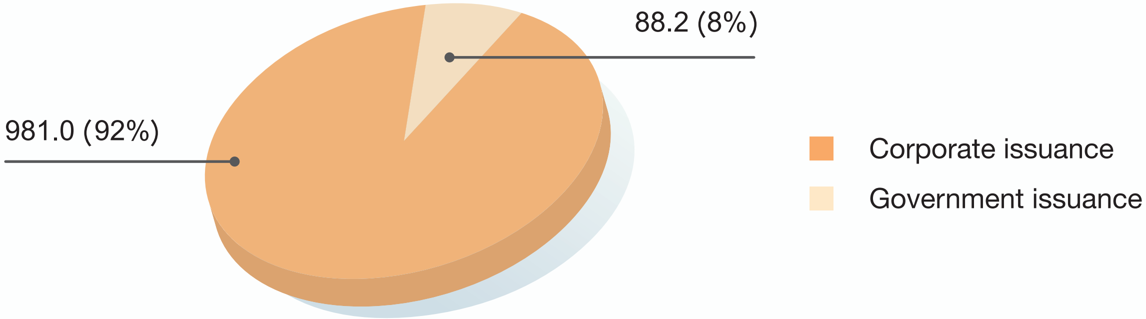
c. There is no mandatory requirement on Mandatory Provident Funds or Occupational Retirement Schemes to invest in HKD bonds so that Hong Kong lacks a captive group of investors for HKD bonds especially under a low interest rate environment.

The Steering Committee also notes the Government's efforts in encouraging participation of the private sector, especially financial institutions, in the bond market and recognises the diversity of the participation in the local bond market. Specifically, excluding EFBN, about 92% of all outstanding bonds in Hong Kong are issued by corporates and 8% by governments[5] (See Chart 5 below).

4 Refers to bonds denominated in USD, Euro or Japanese yen.

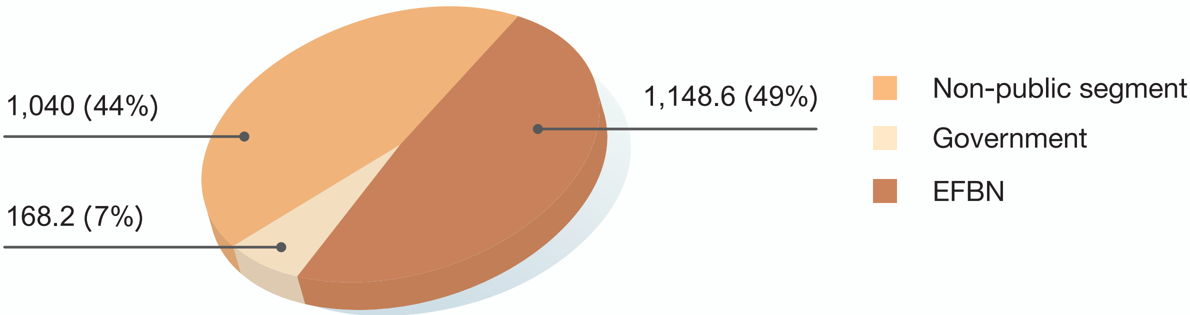
5 Government issuance refers to issuance by sovereign, provincial and local governments; corporate issuance represents the rest. Sources: Bloomberg, CMU, Dealogic, Reuters and HKMA.

Chart 5: Outstanding size of bonds (excluding EFBN) in Hong Kong at end-2021 by issuer (in US$ billion)



As at end-2021, about 44% of all outstanding HKD-denominated debt securities were issued by non-HKSAR Government authorities and the private sector and 56% by HKSAR Government authorities[6] (See Chart 6 below).

Chart 6: Outstanding HKD debt securities at end-2021 by instrument (in US$ billion)



Similar to other major markets across the globe, bond trading in Hong Kong takes place mostly through over-the-counter ("OTC") markets. It is estimated that less than one-third of all bond issuances in terms of issuance size were listed on the Stock Exchange of Hong Kong ("SEHK") and the remaining were unlisted. As at end-2021, there were 1 747 bonds listed on SEHK. In 2021, the total trading of debt securities on SEHK amounted to HK$104 billion, whilst total trading of Hong Kong bond market according to AsianBondsOnline amounted to some HK$2,770 billion, indicating that over 95% of the bond trading was conducted OTC.

Also, similar to other markets, institutional investors dominate the bond market in Hong Kong. Of the 1 747 listed bonds on SEHK as at end-2021, only 61 are open to retail investors, pre-dominantly HKMA's Exchange Fund Notes, bonds issued under the Government Bond Programme, and bonds issued by the Ministry of Finance of the People's Republic of China. As at end-2021, there has only been one listed corporate bond offered to retail investors, which is RMB-denominated and has matured in May 2020. Unlisted bonds available to retail investors are uncommon. Only four non-public segment unlisted bonds in Hong Kong have been offered to retail investors between 2010 and 2021.

6 Source: HKMA.

The Steering Committee is of the view that building a sizable retail bond market has been particularly challenging for markets across the globe, as the incentive from the issuers' point of view is very little given that retail issuances are relatively costly and subject to more stringent investor protection requirements. Issuers' appetite for retail issuances has apparently dropped significantly with the introduction of more investor protection safeguards in the aftermath of the Lehman Brothers incident since 2008.

Government Bond Programme

The Government set up the Government Bond Programme ("GBP") in July 2009 to promote the sustainable development of the bond market in Hong Kong. The borrowing ceiling of the GBP was raised progressively from the initial HK$100 billion in July 2009 to HK$200 billion in May 2013 and HK$300 billion in July 2021.

Under the institutional part of the GBP, fixed rate government bonds with tenors ranging from three to 15 years[7] are tendered regularly to ensure a consistent supply of public debt paper and help establish a representative benchmark HKD yield curve for the market. In November 2021, the inaugural issuance of one-year Hong Kong Dollar Overnight Index Average ("HONIA")-indexed Floating Rate Notes was made under the GBP to promote the adoption of HONIA as an alternative reference rate in Hong Kong. As at end-2021, 32 HKD-denominated institutional bonds totalling HK$223.3 billion have been issued under the GBP. Besides, to demonstrate the diversity and viability of Hong Kong's bond market, three tranches of USD-denominated Islamic bonds (or "sukuk") totalling US$3 billion were issued under the GBP in 2014, 2015 and 2017 respectively.

Under the retail part of the GBP, the Government issues inflation-linked bonds (including iBond for Hong Kong residents since 2011 and Silver Bond for senior Hong Kong residents since 2016) to meet the general public's demand for stable investments of high quality and to promote public understanding of bond investment. As at end-2021, eight batches of iBond and six batches of Silver Bond totalling HK$152 billion have been issued, and all were met with warm market reception and over-subscription. The introduction of retail government bonds has broadened the investor base (with 5 to 15% of subscribers in past retail bond issuances being first-time bond investors) and contributed to the development of a retail bond market in Hong Kong. The amount of debt securities holdings of Hong Kong households, although small in absolute amount when compared with deposits, equities and funds, has increased notably with the Government's effort to promote the development of the bond market since 2009.

7 Bonds of two-year tenor were also issued between 2009 and 2014.

As at end-2021, the total outstanding amount of bonds under the GBP was around HK$176 billion, comprising 13 institutional bonds totalling HK$85.5 billion, three batches of Silver Bond totalling HK$47.7 billion, two batches of iBond totalling HK$35 billion and one USD sukuk of US$1 billion. Please refer to **Annex C** for details of the bond issuances under the GBP.

Government Green Bond Programme

In addition to the GBP, the Government also launched the Government Green Bond Programme ("GGBP") in November 2018 to promote the development of the green bond market. The borrowing ceiling of the GGBP was raised from HK$100 billion to HK$200 billion in July 2021. The bond proceeds raised under the GGBP are credited to the Capital Works Reserve Fund and used to finance or re-finance eligible green projects.

The Government's issuances under the GGBP have continued to set best practice, provide good benchmarks to the market and achieve breakthroughs, highlighting the progress that has been made:

- Early 2021: the Government set up the world's first "Global Medium Term Note Programme" dedicated to green bond issuances by a government.
- February 2021: the world's then largest USD government green bond deal totalling US$2.5 billion was issued under the GGBP, with the 30-year tranche in the deal being the then longest tenor USD government green bond in Asia and the longest tenor issued by the Government.
- November 2021: inaugural offering of euro-denominated and RMB-denominated green bonds was made under the GGBP and by the Government. The issuance also marked the first time that an Asian government issued an euro-denominated green bond of as long as 20 years.
- As at end-2021, a total of over US$7 billion equivalent worth of green bonds, targeting global institutional investors and covering USD, Euro and RMB tranches in multiple tenors, have been successfully issued under the GGBP. **Annex C** provides further details on this.

To reinforce Hong Kong's position as a premier green finance hub regionally and internationally, the Government plans to issue green bonds totalling HK$175.5 billion equivalent under the GGBP in the five financial years from 2021-22 having regard to market condition. The issuances will involve different types of currencies, green projects and issuance channels.

The Government also issued the inaugural retail green bond of HK$20 billion in May 2022 so that the general public can directly contribute to greening Hong Kong and share the fruit of the sustainable development of Hong Kong. The retail green bond was well received by the public. The introduction of the retail green bond has broadened the variety of green and sustainable financial products in Hong Kong and further promoted the development of the local retail bond market.

Bond Connect

The HKMA and the People's Bank of China have also taken forward a new initiative named "Bond Connect" in July 2017. The scheme seeks to promote two-way connectivity between bond markets in Hong Kong and the Mainland. It started with Northbound Trading, which allows offshore overseas investors to invest in the China Interbank Bond Market through a linkage between the financial infrastructure institutions in Hong Kong and the Mainland in respect of trading, custody, settlement, etc. A number of enhancements have been made to the Northbound Trading since its launch. They include launching Delivery versus Payment settlement, block trade functionality, addition of new electronic trading platforms, extension of the settlement cut-off time, increased options for the settlement cycle, and flexibility for investors to engage more than one bank to conduct currency conversion and foreign exchange hedging. Tax exemption for interest income arising from overseas institutional investors' onshore bond investments was also extended. In four years' time, the average daily turnover of Northbound Trading under Bond Connect has expanded more than 11 times from RMB2.2 billion in 2017 to RMB25.8 billion in 2021. Riding on the success of Northbound Trading, Southbound Trading under Bond Connect was launched in September 2021, completing the two-way connection under Bond Connect and providing an effective channel for qualified onshore investors to make diversified asset allocation to offshore bonds. Under Southbound Trading, all cash bonds that are issued offshore and traded OTC in Hong Kong are included. Southbound Trading has been well received and operations have been smooth, with transactions covering major bond products tradeable in the Hong Kong market and denominated in multiple currencies.

Having considered the above, the Steering Committee has the following views:

- the Government's initiatives introduced over the years, coupled with the opportunities arising from the fast-growing economies in the region and more importantly the gradual opening-up of the Mainland market, have developed Hong Kong into a major bond hub in Asia;
- the Government bond issuances under the GBP and GGBP have significantly enriched the market, in particular the market for primary issuance and arrangement of international bonds, and set benchmarks for market reference. Also, the landmark

issuances of the GGBP have raised Hong Kong's profile and help promote the fast-growing green and sustainable bond market;

- the Bond Connect with the Mainland provides a good window for Hong Kong to further enrich its bond market. In particular, the launch of Southbound Trading has expanded the product suite of the Connect family and further underlines the unique function of Hong Kong in connecting Mainland capital and the wide range of products in the international market. It also enhances the attractiveness of Hong Kong as a bond issuing platform and the liquidity of the bond market in Hong Kong; and
- thanks to these developments, the local bond market has been growing substantially and continuously in terms of its breadth and depth with greater variety of bonds in different currencies and wider participation from the market.

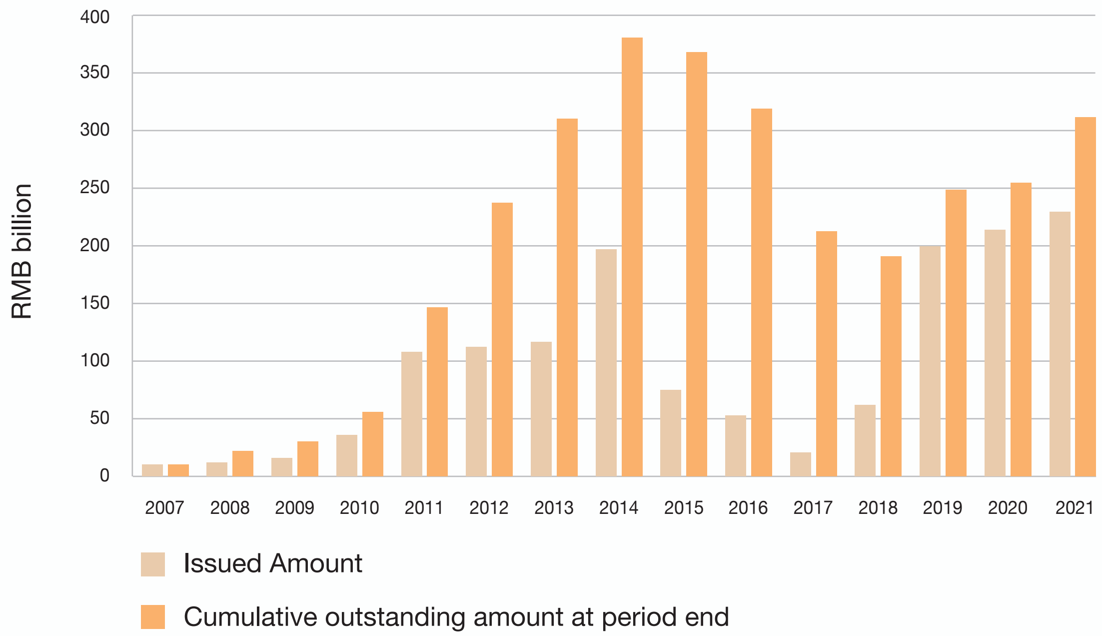
Unique Advantages and Green Opportunities

The Steering Committee notes that Hong Kong's bond market possesses a number of unique advantages given Hong Kong's economic ties in the region and past development trajectory. These advantages provide a myriad of opportunities for further developing the bond market, as set out in the ensuing paragraphs.

Against the backdrop of continuous opening-up of Mainland market translating into increasing demand for RMB bond issuances, Hong Kong has been well-positioned as a gateway to the Mainland's capital market. Particularly, leveraging its unique value propositions of being a major international financial centre with sound and robust regulatory and supervisory financial framework, Hong Kong has been a premier platform for offshore RMB bond issuances. To illustrate, the first offshore RMB bond in the market was issued by the China Development Bank in Hong Kong in 2007. Subsequently, RMB bond issuances in Hong Kong has continued to grow strongly with issuances by foreign multinational corporations, Mainland companies and the regular issuance by the Ministry of Finance since 2009. The amount of RMB bond issuances in Hong Kong peaked in 2014. Since 2018, the People's Bank of China has been issuing RMB bills in Hong Kong regularly and continued to drive the market. The outstanding amount of RMB debt instruments in Hong Kong reached RMB 311.4 billion as at end-2021[8] (See Chart 7 below).

8 Sources: Newswire and HKMA.

Chart 7: Issuance volume of RMB debt instruments in Hong Kong



In October 2021, the Shenzhen Municipal People's Government issued offshore RMB municipal government bonds totalling RMB5 billion in Hong Kong, including RMB3.9 billion of green bonds, which are listed on SEHK. That was the first time a Mainland municipal government issued bonds outside the Mainland, enriching Hong Kong's spectrum of RMB financial products. In respect of interest paid or profit received arising from the debt instruments issued in Hong Kong by the Shenzhen Government, the Government exempts the payment of profits tax for any year of assessment commencing on or after 1 April 2021. Riding on this successful issuance, the Government will encourage more Mainland issuers to make use of Hong Kong's platform to issue RMB bonds, including green bonds, to enrich the market.

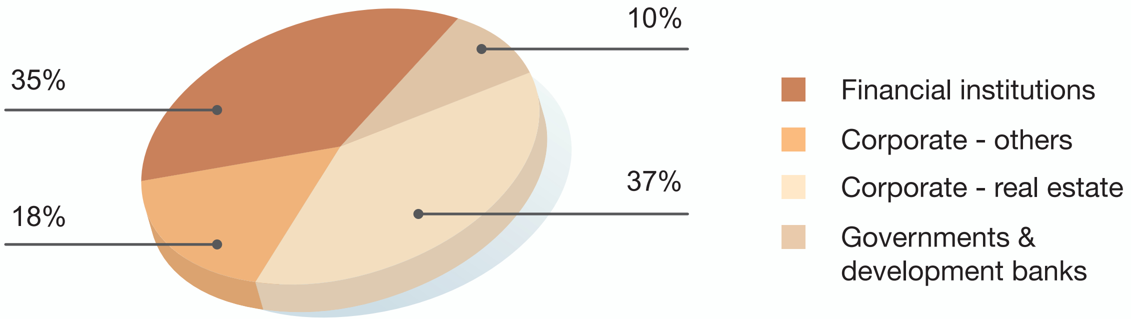
From market experience, the growing number of bond issuances by Mainland entities in Hong Kong was conducive to attracting greater presence of bond issuers and traders in Hong Kong, thanks to its proximity to the Mainland market.

Besides, to contribute to the target of carbon neutrality in the Mainland before 2060 and to achieve carbon neutrality in Hong Kong before 2050, Hong Kong has already adopted proactive strategies and measures on reducing carbon emissions. On the financial services front, the Government has been actively promoting the development of the local green and sustainable bond market, such as adopting internationally accepted standards and promoting eligible green and sustainable financing, with a view to maximising its first mover advantages. Specifically, in 2021, US$31 billion of green and sustainable bonds were arranged in Hong Kong, accounting for one-third of the Asian green and sustainable bond market[9]. Around 90% of the

9 Source: International Capital Market Association.

issuances in Hong Kong were made by private sector issuers, with real-estate developers and financial institutions each taking up more than one third of the market (see Chart 8 below). Over 80% of the bonds by issuance size were issued by Mainland entities. According to the Climate Bonds Initiative[10], green debt market has been soaring at a growth rate of over 50% in the five preceding years before 2022, and it is estimated that the annual issuance could exceed the US$1 trillion mark by 2022[11].

Chart 8: Green and sustainable bonds arranged in Hong Kong in 2021 (by industry)



In view of the growing demand for green financing in the Mainland and globally, the Steering Committee is of the view that given its continuously expanding bond market and the status as a unique gateway to the Mainland market, Hong Kong is well-positioned to capture the enormous opportunities ahead.

Recommendations

In light of the above analysis and other observations, the Steering Committee recommends that the Government can work further in the following areas to develop the market landscape.

Recommendation 1 — Expand government bond issuances

Consider expanding the issuance of green, RMB and longer tenor HKD bonds under the Government's bond programmes to stimulate the growth of Hong Kong's RMB and green bond markets, as well as enhance the formation of local yield curve (SD1 & SD2)

10 Climate Bonds Initiative is an investor-focused and not-for-profit international organisation working to mobilise global capital for climate action.

11 https://www.climatebonds.net/2022/01/500bn-green-issuance-2021-social-and-sustainable-acceleration-annual-green-1tn-sight-market

The Steering Committee acknowledges the effectiveness of the GBP and GGBP and considers that the Government should issue longer tenor HKD bonds. It observes that some jurisdictions have been proactive in boosting their local bond market by building a yield curve with longer tenor bond issuances. In the case of Hong Kong, the HKD bonds issued by the Government currently are with tenors up to 15 years only. Against this backdrop, there is scope for the Government to consider further expanding the issuance of longer tenor HKD bonds, with a view to furthering the diversified development of the local bond market.

The Steering Committee observes that, owing to the depth of the USD bond market or due to the smaller supply of longer tenor HKD bonds in the past, some investors or long term insurers may hold USD bonds in their fixed-income portfolio, and use derivatives to hedge against the associated currency risks when required. The Government's efforts in furthering the development of the local yield curve and bond market would help encourage further participation from investors and insurers, thereby promoting the sustainable development of the local bond market in the long run.

The Steering Committee considers that the Government should issue more green bonds and RMB bonds. This will help provide further market benchmarks for issuers to price their products with different tenors and calculate the borrowing cost, and also enrich the market. On this, the Steering Committee sees the great opportunities presented by the unique position of Hong Kong in developing a premier offshore RMB bond market for both green and conventional bond products.

Recommendation 2 — Grow the green and sustainable and catastrophe bond market

Promote the issuance of green and sustainable bonds and catastrophe bonds in Hong Kong to grow the market size (SD1)

The Steering Committee considers that the Government should grasp the opportunities presented by the global economy's transition towards a low carbon and sustainable economy, in particular the Mainland's goal of achieving carbon neutrality before 2060, and promote the issuance of green and sustainable bonds and catastrophe bonds by other issuers.

With the inaugural issuance of insurance-linked securities ("ILS") taken place on 1 October 2021, the Steering Committee sees the potential for Hong Kong to strive towards becoming a catastrophe risk management centre for the Mainland and Asia Pacific.

Recommendation 3 — Attract Mainland entities for bond issuances

Encourage Mainland entities, in particular municipal governments and corporates, to issue offshore RMB bonds in Hong Kong to increase the breadth and depth of the bond market (SD1)

The Steering Committee considers that the Mainland will remain the key engine of growth in the next decade and Hong Kong should also assume key roles on the further opening up of the Mainland market. With increasing number of Mainland corporates developing the habit of raising funds through bond issuances, the growth of the local bond market will be very substantial if Hong Kong can attract a fraction of these corporates to issue bonds in Hong Kong. Hong Kong should therefore encourage Mainland entities, in particular municipal governments and credible corporates to issue offshore RMB bonds via the Hong Kong platform. The Government may seek support from the Mainland authorities on certain dedicated policies for offshore bond issuances in Hong Kong. On that, pilot arrangements confining to certain product types, entities or geographical areas and quota systems can be explored.

The Steering Committee considers that providing more diverse investment products denominated in offshore RMB, providing more distribution channels for the products and growing the investor base are also possible ways to attract more Mainland entities to issue offshore RMB bonds in Hong Kong.

Recommendation 4 — Encourage issuance of retail tranches

Encourage statutory bodies to include retail tranches when they issue bonds in Hong Kong to develop the retail market (SD3)

The Steering Committee agrees that the development of a sizable retail bond market has been challenging across the globe. Yet, from the perspective of social and financial inclusion, Hong Kong should strive to expand the retail bond market. Apart from continuing the issuance of retail tranches under the GBP and GGBP, the Government should encourage statutory bodies to include retail tranches.

Recommendation 5 — Develop bond-related markets as complements

Develop the bond-related markets with a greater variety of products, such as bond funds, bond exchange-traded funds, derivatives and repo, which would complement the development of the bond market (SD1 & SD2)

The Steering Committee considers that at present, retail investors participate in bond investment mainly through bond funds and bond exchange-traded funds ("ETFs"). Therefore, a well-developed bond fund or ETF ecosystem will help engage the mass and promote financial inclusion. The Steering Committee also notes that in some highly vibrant and liquid ETF market, investors can use ETFs to gain liquidity. Growing the bond ETF market will thus add impetus to the bond market and attract a wider spectrum of investors.

The Steering Committee considers that the Government should foster the development of bond-related markets such as derivatives and repo, which in turn provide liquidity and risk management tools to investors and fund managers and help deepen the development of the bond market. In particular, there are limited tools to hedge against exchange rate risks of bond products at present.

Chapter 3 – Bond Market Infrastructure

Overview of Market Infrastructure

In order to capture the opportunities identified in Chapter 2, including the growing demand for green finance and Mainland-related financing, it is of paramount importance for Hong Kong to further improve its bond issuance framework and bond listing and trading infrastructure.

Central Securities Depositories — Central Moneymarkets Unit

The Steering Committee has reviewed the development, strengths and limitations of the central securities depository ("CSD") in Hong Kong – Central Moneymarkets Unit ("CMU")[12] and noted that the usage of CMU has been gradually expanded over the years. As at end-2021, the total outstanding amount of debt securities lodged with CMU was HK$2,211 billion, representing an increase of 11.9% over that in 2016. In 2021, the average daily turnover of local secondary market transactions processed by CMU was HK$15.6 billion, an increase of 2.6% over that in 2016. The introduction of the Bond Connect has boosted the usage of CMU. The holding of China Interbank Bond Market bonds through CMU under the Bond Connect as at end-2017 was RMB88.8 billion. It increased by 11 times to over RMB1.04 trillion as at end-2021.

In recent years, CMU has expanded its services to provide a full range of debt securities depository services to local, regional and international market participants and is also involved in overseas tendering and issuance of RMB sovereign bonds by the Ministry of Finance and RMB bills by the People's Bank of China. CMU has linkages with international central securities depositories ("ICSD") to facilitate the reach of local investors to international bonds, and the participation of overseas investors in the Hong Kong market. It also provides important financial infrastructure support for the implementation of a number of cross-border financial initiatives, especially the Northbound Trading under Bond Connect and Southbound Trading under Bond Connect launched in July 2017 and September 2021 respectively.

To cope with the evolving market demand, a wider participation of the international investment community and support the Bond Connect, CMU conducted a strategic review of its position in 2019 and engaged a consultant in 2020 to help map out the path for enhancing its system and service. Based on the recommendations of the consultancy study, which were formulated based on extensive industry engagements, the HKMA has

12 The CMU established in 1990 and operated by the HKMA, offers issuance, clearing and settlement services for EFBN and provides liquidity management for banks through its delivery-versus-payment linkage with the real time gross settlement system, which forms an integral part of the monetary management arrangement under the Linked Exchange Rate System. Apart from the role in monetary management, CMU's functions have been extended to providing depository services for debt securities issued by non-government institutions.

embarked on a project to enhance the CMU system, with near-term priorities being put on further smoothening Northbound Trading under Bond Connect operation and supporting the launch of Southbound Trading under Bond Connect, such as automation and digitalisation of operation flow, developing new user interfaces and reporting tools and strengthening the automatic interface with the CSDs in the Mainland. The system enhancement project is also targeted at supporting the development of CMU into an ICSD in Asia over the long term, by enhancing the flexibility of the system and aligning the service offerings of CMU with those of the ICSDs.

After the system enhancement, CMU is prepared to extend its operating window from currently 10 hours to 22 hours per day and introduce new services to better support international bond investment, including: (i) tax services to support comprehensive tax handling such as processing of withholding taxes; (ii) cash accounts for members to efficiently settle bonds in currencies other than HKD, RMB, USD and Euro; and (iii) a full spectrum of corporate action services. The enhanced system would also enable CMU to directly provide collateralised lending services to non-bank participants subject to market demand for the services.

On the development of CMU, the Steering Committee notes that the following market practices and regulatory requirements prevent existing issuers or investors from switching to CMU from other well-established ICSDs -

a. ICSDs, including Euroclear and Clearstream, have been long established and dominated the custodian business of international bonds. Unless justifiable by sizeable holding and turnover in the local bond market, international issuers and investors generally have strong inertia against switching to local clearing, settlement and custody solutions, due to system, operation, compliance and cost considerations, etc.;

b. Certain jurisdictions have imposed rules to specify the types of financial products to be sold to qualified investors and to be cleared and lodged with overseas institutions. For example, bonds issued under the Rule 144A of the US Securities Act enjoy exemption from registration requirements under the Act by being sold or offered to the US investors and usually cleared through the Depository Trust and Clearing Corporation ("DTCC"), a US-domiciled central securities depository; and

c. CMU has linkages with ICSDs in the Asian and European markets including Euroclear and Clearstream but not DTCC, which affects its adoption by the US market participants, a significant share of the global market.

Noting the strong inertia of existing issuers or investors to switch to CMU from other well-established ICSDs, the Steering Committee observes that even first-time issuers in Hong Kong subsidised by the Government's grant schemes hesitate to use CMU. The Steering Committee considers that there is an imminent need to upgrade CMU and promote it to market players.

Despite the challenges identified above, the Steering Committee sees an enormous opportunity presented by the Bond Connect and the gradual opening up of the Mainland market. In particular, the successful launch of Northbound Trading under Bond Connect has attracted a large number of overseas investors to invest in the China Interbank Bond Market through Hong Kong, and the launch of the Southbound Trading under Bond Connect has made Hong Kong a window for Mainland investors to reach out. Both developments will accelerate the formation of a critical mass of bond market participants in Hong Kong. Together with the new CMU system which supports a wide spectrum of effective and efficient services, the developments will promote Hong Kong as a CSD hub for Asian bonds with a cluster of Mainland and international bond investors and issuers as well as intermediaries operating through Hong Kong's bond market platform.

Electronic Bond Trading Platforms

Bond trading is traditionally conducted by voice. The migration to electronic trading ("e-trading") on third-party platforms has accelerated in recent years in pursuit of better efficiency and liquidity. Uptake in Asia, however, appears to be generally lagging behind than other markets.

Having examined the design of common trading modes adopted in e-trading platforms, the Steering Committee believes that e-trading can increase transparency and liquidity of the market and widen the participant base. In addition, if "all-to-all" e-trading[13] becomes more prevalent in the future, electronic platforms may take on the role of a central marketplace akin to that of a stock exchange.

The Steering Committee has reviewed the secondary bond market landscape in Hong Kong. In view of the market characteristics in Hong Kong and the increasing prevalence of electronic mode of trading, the Steering Committee considers that Hong Kong should explore the opportunities ahead and build up the new infrastructure needed. For instance, in addition to the current infrastructure of CMU as a clearance limb, Hong Kong may explore the possibility of setting up a bond trading platform to promote bond trading.

Product Authorisation and Listing Regime

The Steering Committee has also reviewed the product authorisation and listing regime of debt securities in Hong Kong and agreed that the listing regime of Hong Kong is competitive. While the Steering Committee notes that the global competition in the bond listing market is keen, it considers that the economic benefits of having a vibrant bond listing environment in Hong Kong cannot be underestimated.

13 This is where investors and dealers trade anonymously with one another, as opposed to the traditional request-for-quote setting where the client solicits quotes from specific dealers and strikes a bilateral deal with the chosen dealer.

The product authorisation and listing regime of debt securities depend on three main factors - whether the debt securities are listed or unlisted, whether they are offered to the public or only to professional investors and whether the issuer is a “company” under the Companies (Winding-up and Miscellaneous Provisions) Ordinance (“CWUMPO”). Based on these factors, the typical debt securities issuance in Hong Kong are listed and unlisted retail bonds and listed and unlisted debt securities offered to professional investors only. Please refer to **Annex C** for a summary of key product authorisation and listing regime for debt securities in Hong Kong.

Generally speaking, the prospectus requirement in CWUMPO applies to the issuance of bonds to Hong Kong public (i.e. retail bonds), unless an exemption (e.g. an offer to professional investors only) applies. The Steering Committee notes that a prospectus contains information designed to enable retail investors to assess the issuer and its debt securities in order to make an informed investment decision. It ensures access to information regarding an issuer of debt securities which such investors would otherwise not have. Nevertheless, there are comments that the stringent prospectus requirement under CWUMPO deters issuers from issuing retail bonds, and that it has been difficult even for some high-net-worth individuals to gain access to bonds. The number of publicly offered bonds listed under Chapters 22 to 36 of the Main Board Listing Rules (“Listing Rules”) of the Hong Kong Stock Exchange (“HKSE”) is very small and there are currently no unlisted retail corporate bonds in issuance in Hong Kong.

As for bonds targeting professional investors, the Steering Committee notes that the Chapter 37 regime under the Listing Rules was streamlined in 2011 so that it could be more closely aligned with the listed debt regime for professional investors in other markets with a view to maintaining Hong Kong’s competitiveness. It offers an expedient and streamlined listing process for issuers needing a quick and technical listing, such as offerings aimed at professional investors like certain funds which may only invest in listed debt products.

The HKSE requires all Chapter 37 Bonds’ listing documents to carry the statement that the listing status of Chapter 37 Bonds “should not be taken as an indication of the commercial merits or quality” of the bond. In line with their pursuit of a technical listing, Chapter 37 Bonds are predominantly traded off-exchange and with the majority of issuances cleared through overseas clearing systems. The Steering Committee considers having a streamlined and expedient listing channel for professional investor bonds a right strategy, considering how the choice of the listing venue for the type of product listed on these platforms is generally driven more by convenience and speed of listing than market access.

Recommendations

In light of the above analysis and other observations, the Steering Committee recommends that the Government can work further in the following areas to develop the market infrastructure.

Recommendation 6 — Explore the inception of electronic bond trading platforms

> Anchor the operation of electronic bond trading platforms in Hong Kong and explore the development of an electronic bond trading platform to facilitate secondary trading and broaden the investor base (including retail investors) (SD2 & SD3)

On e-trading, the Steering Committee considers that Hong Kong may look into two directions: (a) to anchor the operation of some existing e-trading platforms; and/or (b) to explore the necessity and plausibility of developing a new platform of its own, taking into account key issues around liquidity aggregation, information transparency and connectivity with local, Mainland and international financial market infrastructure.

Recommendation 7 — Enhance the functionalities of CMU

> Enhance the functionalities of CMU to promote its adoption by market players (SD2)

The operations and functions of CMU should be enhanced to better meet user requirements and support international transactions. With the successful launch of Bond Connect, CMU is expected to continue enhancing its system with more automation features to facilitate high volume transactions and exchanges with other CSDs. Under its enhancement project, CMU could provide additional tools such as support features for corporate actions, provision of liquidity analyses, data products, financing options, etc. to meet clients' needs and capture the growing Asian market.

Recommendation 8 — Enhance the MPF Scheme to allow wider scope of bond investments

> Explore the possibility of allowing provident funds to invest in Mainland sovereign bonds without credit ratings (SD3)

The Steering Committee considers that the investment choice of Mandatory Provident Funds ("MPF") should be relaxed to allow sovereign bonds of the Mainland which do not bear a credit rating from an international credit rating agency given the positive economic outlook of the Mainland and the importance of RMB in the long run. The Steering Committee considers that the relaxation will widen the investor base of offshore RMB bonds and sustain the sovereign issuances in Hong Kong, hereby consolidating Hong Kong's position as an offshore RMB bond centre.

Recommendation 9 — Explore enhancements to the prospectus requirement

> Explore enhancements to the prospectus requirement and minimum trading size of bonds to allow easier access by retail investors, taking into account the investor protection impact (SD3)

The Steering Committee considers that the prospectus requirement under the CWUMPO is one of the underlying reasons leading to the scarce number of retail bonds in the market. While the requirement is waived under the safe harbour provisions under the Seventeenth Schedule of CWUMPO if the offer meets certain conditions, such as being offered to professional investors only, being offered to not more than 50 persons, with a minimum denomination of HK$500,000, etc., the Steering Committee suggests that the Government may look into relaxing the safe harbour provisions. The relaxations may be confined to certain products, products of certain issuers, certain group of investors based on their asset level or experience, etc. Bearing in mind the potential implications from the investor protection angle, the Government may target high quality products as the first step.

Recommendation 10 — Participate in the setting of standards

> Facilitate Hong Kong to participate in the setting of international green standards, and explore the feasibility of adopting new financial technologies (SD1)

The Steering Committee considers that green bond market is growing fast and propelled by the Mainland's goal of achieving carbon neutrality before 2060. There are different green standards across the globe and the Steering Committee sees enormous opportunities for Hong Kong to assume thought leadership in developing standards on classification and disclosure for adoption in the local market while aligning with international best practice, thereby ensuring that the green ecosystem will base and expand in Hong Kong with an Asian perspective.

The Steering Committee considers that one of the worldwide focus in the next couple of years would be financial technology ("Fintech"). Hong Kong should strive to position itself at the frontier of the Fintech side of the bond market. The Government may encourage development of new and convenient mobile tools for bond investment to engage the mass and look into the tokenisation technology for Government issuances. It is also believed that the adoption of Fintech to facilitate retail bond investment in Hong Kong may in turn attract more issuers to launch their products here.

Recommendation 11 — Develop CMU into a regional ICSD

Subject to the progress of and taking the opportunities arising from the further opening up of the Mainland financial market, develop CMU into a regional ICSD (SD2)

The Steering Committee considers it a strategic issue for Hong Kong and the Mainland to have their own ICSD for custody, clearing and settlement of debt securities. Under its vision to grow into a regional ICSD which provides a premier platform for the Asian market, CMU is expected to continue enhancing its system and introducing new services to help capitalise on opportunities arising from the open up of the Mainland financial markets and global development.

Recommendation 12 — Build the derivative infrastructure

Build the necessary infrastructure to support bond-related derivatives (SD2)

The Steering Committee considers that developing the derivative infrastructure around the bond market can add vibrancy to the market itself. Apart from helping investors to manage risk, derivative products will add diversity, create liquidity and attract a lot of interest from investors around the world. The Government should build the necessary infrastructure to support bond-related derivatives.

Chapter 4 – Government Support Measures and Promotion

Overview of Government Support Measures and Promotion

The Steering Committee notes that the Government has all along been attaching great importance to the development of the local bond market and has introduced a wide range of financial support measures, including tax incentives and grant schemes, to incentivise bond issuances in Hong Kong.

Qualifying Debt Instrument Scheme

Since 1996, the Government has put in place the Qualifying Debt Instrument ("QDI") scheme to provide concessionary tax treatment on interest income and trading profits derived from eligible debt instruments with a view to attracting overseas bond issuers to Hong Kong and enlarging the local debt market. Over the years, the Government has made continuous enhancements to the QDI scheme, including relaxing the minimum denomination of debt instruments, broadening the scope of QDIs and enhancing the tax concessions provided, in response to changing market landscape. Caveats and definitions were added to the relevant provisions in the Inland Revenue Ordinance to improve clarity and certainty in application.

Since the implementation of the enhancement measures with effect from April 2018[14], the number of QDIs in Hong Kong has grown substantially. As at end-2021, there were over 1 000 QDIs and over 80% of them were issued after April 2018.

Profits Tax Exemption for Sovereign Debt Instruments

Following the introduction of profits tax exemption for RMB sovereign bonds with effect from the year of assessment 2009/10, the Government extended the exemption to cover non-RMB sovereign bonds issued by the Central People's Government as well as debt instruments issued by the People's Bank of China in Hong Kong with effect from the years of assessment 2017/18 and 2018/19 respectively, with a view to consolidating Hong Kong's position as the Mainland's premier platform for issuing sovereign bonds. Recently, the Government has

14 The Government made significant enhancements to the QDI scheme in 2018. From 1 April 2018 onwards, a debt instrument issued meeting the following criteria is a QDI eligible for 100% tax exemption –
(a) being entirely lodged with and cleared by CMU or listed on the SEHK;
(b) being issued by a person with a credit rating acceptable to the HKMA from a credit rating agency recognised by the HKMA;
(c) having a minimum denomination of HK$50,000 or its equivalent in a foreign currency; and
(d) being issued in Hong Kong to: (i) 10 or more persons; or (ii) less than 10 persons none of whom is an associate of the issuer.

extended the profits tax exemption to the bonds offered by the Shenzhen Municipal People's Government, which launched the debut issuance in Hong Kong in October 2021. Going forward, the Government will consider extending the profits tax exemption to bonds issued in Hong Kong by other Mainland authorities as appropriate.

Subsidy Schemes for Issuers

To further encourage bond issuances in Hong Kong, in particular green bond issuances, in 2018, the Government introduced a three-year Pilot Bond Grant Scheme ("PBGS") and Green Bond Grant Scheme ("GBGS") to cover bond issuance costs and green certification costs incurred by eligible issuers respectively. In view of market feedback, the Government consolidated the PBGS and GBGS into a new Green and Sustainable Finance Grant Scheme ("GSF Grant Scheme") in May 2021 with enhanced features[15].

In the first year since the launch of the GSF Grant Scheme, close to 100 green and sustainable debt instruments including green bonds, sustainability bonds, green loans and sustainability-link loans, issued in Hong Kong have been granted subsidies on the bond issuance costs or external review. The total underlying issuances amount to around US$30 billion.

In May 2021, the Government launched a two-year Pilot Insurance-linked Securities Grant Scheme to cover the upfront costs incurred by issuers of catastrophe bonds or other types of ILS[16] in Hong Kong, subject to a cap of HK$12 million or HK$6 million per eligible issuance depending on the maturity period involved.

Analysis

Having reviewed the financial support measures introduced by the Government over the years, the Steering Committee has affirmed the positive feedback from the market on a wide range of support measures introduced by the Government in view of market needs. The measures are largely practical suiting market needs.

In view of the golden opportunities, including the growing demand for green finance and Mainland-related financing, for Hong Kong's bond market and with the enhanced bond listing regime and infrastructure discussed in Chapters 2 and 3 above, the Steering Committee

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15 The GSF Grant Scheme subsidises –
   (a) bond issuance costs of eligible issues by first-time issuers of green and sustainable bonds, subject to a minimum issuance size of HK$1.5 billion and a maximum subsidy of HK$2.5 million per issuance; and
   (b) external review costs from the use of recognised external reviewers, by green and sustainable bond issuers and loan borrowers, subject to a minimum issuance size of HK$200 million (which was relaxed to HK$100 million with effect from 1 March 2022) and a maximum subsidy of HK$800,000 per issuance.

16 ILS is a risk management tool that enables insurers or reinsurers to offload risks that they have underwritten to the capital market by way of securitisation, and are often treated as an alternative form of reinsurance. Catastrophe bonds is a common type of ILS.

views that the Government could implement targeted support measures to further speed up the development of local bond market, in particular during the key stage of reaching a critical mass of buy-side and sell-side parties in the fixed-income ecosystem in Hong Kong.

While the financial support measures in place have been effective in attracting bond issuers to Hong Kong, the Steering Committee suggests that in addition to attracting issuers from the sell-side, the Government may consider rolling out supplementary measures to attract stakeholders from the buy-side community, including bond investors, traders and fund managers, with a view to further enhancing the fixed-income ecosystem in Hong Kong.

Moreover, the Steering Committee notes that the grant schemes launched by the Government so far focus largely on attracting first time issuances in Hong Kong. To better evaluate the effectiveness of the grant schemes, the Steering Committee suggests the Government may consider conducting an analysis on the utilisation and the effectiveness of extending and enhancing the existing schemes to promote repeated issuances and to localise the related professional services.

Apart from the financial support measures introduced by the Government, the Steering Committee has reviewed the HKMA's strategies and approach in promoting Hong Kong as Asia's premier bond hub through general marketing, targeted pitching and individual engagement. The Steering Committee views that the Government and the relevant regulators should step up their efforts in promoting Hong Kong's premier position as an Asian international bond issuance centre.

Besides, the Steering Committee notes that, in addition to enhancing the bond listing regime and infrastructure, securing sufficient talent is key to further developing the local bond market. It also viewed that this is particularly important when it comes to grasping the opportunities from green financing and Mainland-related financing as discussed in Chapter 2 above. At present, competition for talent is undoubtedly keen. Governments around the globe have launched various policy measures in a bid to attract talent to supplement their local labour force. In this connection, the Steering Committee notes that the Government should also step up the efforts to secure talent, in particular on green, environmental, social and governance ("ESG") and Fintech, with a view to consolidating Hong Kong's position as a regional bond hub.

Recommendations

In light of the above analysis and observations, the Steering Committee recommends that the Government can work further in the following areas to enhance the government support measures and promotion.

Recommendation 13 — Explore the provision of additional tax incentives to encourage the setting up of fixed-income funds in Hong Kong

Explore the possibility of providing additional tax incentives to, for example, encourage the setting up of fixed-income funds in Hong Kong (SD1)

The Steering Committee notes that for bond investment in Hong Kong, interest income eligible for tax exemption is subject to the 5% incidental income rule, i.e. receipt of interest is treated as an incidental transaction and is exempted from tax provided that it does not exceed 5% of the total trading receipts from qualifying and incidental transactions for that year. Given that fixed-income funds derive a majority of their income from interest income and would almost certainly breach the 5% limit, this renders it tax-inefficient to manage fixed-income funds in Hong Kong and results in discriminatory treatment of such funds as compared to equity funds. The Steering Committee suggests the Government consider bringing Hong Kong's tax regime on par with that of other jurisdictions with a view to attracting fund managers to set up or relocate their business activities to Hong Kong.

Recommendation 14 — Review and enhance the support measures for issuers

Review the effectiveness of the support measures and consider making enhancements that would attract issuers to make repeated issuances in Hong Kong (SD2)

The Steering Committee notes that governments around the globe are launching similar grant schemes to attract issuers. To ensure issuers are not taking advantage of the grant schemes to conduct one-off issuance only, the Government should analyse the utilisation and the effectiveness of the schemes in promoting repeated issuances and on retaining the related professional services locally. Enhancements can then be made to the schemes to maximise their effects.

Recommendation 15 — Subsidise lodgement at CMU

Consider providing cost subsidies for those who lodge their bonds with CMU (SD2)

The Steering Committee notes that with the launch of Southbound Trading under Bond Connect that requires the products for cross-boundary trade to be lodged on CMU, more entities are moving their bonds to CMU from other ICSDs. The Steering Committee suggests that CMU may consider waiving CMU lodgement fee and providing other cost subsidies, which may also help signal the aspiration of CMU.

Recommendation 16 — Provide financial incentives for CMU users

With necessary enhancements made to CMU, consider providing enhanced financial incentives for those lodging their bonds with CMU (SD2)

The Steering Committee considers that synergy can be achieved if the grant schemes or financial incentives provided by the Government can also promote the use of infrastructure or services in Hong Kong. With the necessary enhancements made to CMU on both capacity and functions, the Government can provide enhanced financial incentives for bonds lodged with CMU, growing the number of users and raising its recognition strategically.

Recommendation 17 — Step up promotional efforts

Step up promotional efforts to enhance the image of Hong Kong as a bond centre, and in particular focus on the buy-side, as well as professional advisors to issuers (SD1)

The Steering Committee considers that the current scale of marketing and promotion of Hong Kong as a bond centre can be further amplified. Despite the premier position and outstanding performance of Hong Kong as an Asian international bond issuance centre, the general conception is that Hong Kong's financial market is praised primarily for its vibrant equity market as opposed to its bond market. Apart from the strengths of Hong Kong in arranging bond issuances, more promotion is needed on the merits of listing in Hong Kong, lodgement of bonds in CMU, etc. to raise Hong Kong's profile as a whole. The promotion should reach all audience including issuers, investors, traders, fund managers, service providers, professionals, industry associations, etc.

Recommendation 18 — Attract and train up talent

Step up measures to attract green and ESG talent from abroad and train up talent locally on core financial service areas including green, ESG and financial technology (SD1)

The Steering Committee notes that governments around the globe are in search of talent. The Government should step up the efforts to secure talent in particular on green, ESG and Fintech. The possible ways to attract talent from abroad are subsidy schemes and talent admission programmes. On the other hand, Hong Kong may train up local talent through internship programmes and bridging programmes for local universities and financial institutions. Considering local universities are offering top-rated business programmes or finance programmes to students, training up local talent should not be difficult.

Chapter 5 – Way Forward

The Steering Committee aims to set the strategic directions and identify the measures to be implemented in phases to develop the local bond market in an incremental approach. The strategic directions and measures form a roadmap for promoting the diversified development of Hong Kong's bond market and reinforcing its functions. It believes that the Government and relevant authorities will, having regard to resources and other relevant considerations, take forward the recommendations by developing the specific details for implementation.

Given the recommendations are based on the prevailing situation and the market is ever-changing, the Steering Committee further encourages the Government to continue engaging the industry, keep abreast of the dynamic in the market, and monitor any emerging opportunities and challenges on the international and local horizons. The Steering Committee believes that a more developed bond market for Hong Kong, along with the well-developed equity market and banking sector will promote financial stability, strengthen Hong Kong's status as an international financial centre and promote economic development.

Annex A

Membership and Terms of Reference of the Steering Committee on Bond Market Development in Hong Kong

Membership

Chairman:	Financial Secretary
Members:	Secretary for Financial Services and the Treasury
	Permanent Secretary for Financial Services and the Treasury (Financial Services)
	Under Secretary for Financial Services and the Treasury
	Chief Executive, Hong Kong Monetary Authority
	Chief Executive Officer, Securities and Futures Commission
	Chief Executive Officer, Insurance Authority
	Chief Executive, Hong Kong Exchanges and Clearing Limited
	Mr Stephen Chang Koon-bong
	Mr Francesco Forte
	Mr JIA Hongrui
	Mr Freddy Wong Ka-shing
	Ms Annie Zhu Jing
Secretary:	Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) 5

Terms of Reference

a. To review the strategic direction of bond market development in Hong Kong and formulate a roadmap for promoting its long-term and sustainable development.

b. To provide steer on enhancement of market infrastructure, including trading, clearing, settlement and depository facilities, product authorisation and listing regime and cross-boundary connectivity platforms, to support the development and strengthen the competitiveness of the local bond market.

c. To provide steer on ways and means to promote bond issuances in Hong Kong by public and private sector entities.

d. To provide steer on promotion of Hong Kong's bond market to potential issuers and investing public in the region and beyond.

Annex B

Summary of Steering Committee's Recommendations

	SD1 – Leveraging opportunities	SD2 – Upgrading infrastructure	SD 3 – Promoting financial inclusion
Short-term	• Consider expanding the issuance of green, RMB and longer tenor HKD bonds under the Government's bond programmes to stimulate the growth of Hong Kong's RMB and green bond markets, as well as enhance the formation of local yield curve[17] • Promote the issuance of green and sustainable bonds and catastrophe bonds in Hong Kong to grow the market size • Step up measures to attract green and ESG talent from abroad and train up talent locally on core financial service areas including green, ESG and financial technology • Step up promotional efforts to enhance the image of Hong Kong as a bond centre, and in particular focus on the buy-side, as well as professional advisors to issuers	• Anchor the operation of electronic bond trading platforms in Hong Kong and explore the development of an electronic bond trading platform to facilitate secondary trading and broaden the investor base (including retail investors)[18] • Enhance the functionalities of CMU to promote its adoption by market players • Consider providing cost subsidies for those who lodge their bonds with CMU	• Explore the possibility of allowing provident funds to invest in Mainland sovereign bonds without credit ratings

17 This recommendation will also benefit Strategic Direction 2.
18 This recommendation will also benefit Strategic Direction 3.

	SD1 – Leveraging opportunities	SD2 – Upgrading infrastructure	SD 3 – Promoting financial inclusion
Medium-term	• Encourage Mainland entities, in particular municipal governments and corporates, to issue offshore RMB bonds in Hong Kong to increase the breadth and depth of the bond market • Facilitate Hong Kong to participate in the setting of international green standards, and explore the feasibility of adopting new financial technologies • Explore the possibility of providing tax incentives to, for example, encourage the setting up of fixed-income funds in Hong Kong	• Review the effectiveness of the support measures and consider making enhancements that would attract issuers to make repeated issuances in Hong Kong • With necessary enhancements made to CMU, consider providing enhanced financial incentives for those lodging their bonds with CMU	• Explore enhancements to the prospectus requirement and minimum trading size of bonds to allow easier access by retail investors, taking into account the investor protection impact • Encourage statutory bodies to include retail tranches when they issue bonds in Hong Kong to develop the retail market
Long-term	• Develop the bond-related markets with a greater variety of products, such as bond funds, bond exchange-traded funds, derivatives and repo, which would complement the development of the bond market[19]	• Subject to the progress of and taking the opportunities arising from the further opening up of the Mainland financial market, develop CMU into a regional ICSD • Build the necessary infrastructure to support bond-related derivatives	

19 This recommendation will also benefit Strategic Direction 2.

Annex C

Other Figures and Information

Table 1: HKD-denominated Bond Issuances under the Government Bond Programme

Year	Issuance Size (HK$ billion)		
	Institutional	Retail	Total
2009	5.5	-	5.5
2010	18.5	-	18.5
2011	17.5	10.0	27.5
2012	16.0	10.0	26.0
2013	20.0	10.0	30.0
2014	20.8	10.0	30.8
2015	20.4	10.0	30.4
2016	16.4	13.0	29.4
2017	16.6	3.0	19.6
2018	16.6	3.0	19.6
2019	17.4	3.0	20.4
2020	18.2	30.0	48.2
2021	19.4	50.0	69.4
Total	**223.3**	**152.0**	**375.3**

Table 2: USD-denominated Sukuk Issuances under the Government Bond Programme

Issuance	September 2014	June 2015	February 2017
Structure	Ijarah (leasing)	Wakalah (agency)	Wakalah (agency)
Issuance Size	US$1 billion	US$1 billion	US$1 billion
Tenor	5 years (matured)	5 years (matured)	10 years
Listings	Hong Kong Stock Exchange, Bursa Malaysia and NASDAQ Dubai	Hong Kong Stock Exchange, Bursa Malaysia and NASDAQ Dubai	Hong Kong Stock Exchange, Bursa Malaysia and NASDAQ Dubai

Table 3: Issuances under the Government Green Bond Programme (as at end-2021)

Government Green Bond Issuances (Institutional)								
Issuance	May 2019	February 2021			November 2021			
Tenor	5 years	5 years	10 years	30 years	3 years	5 years	10 years	20 years
Issuance Size	US$1 billion	US$1 billion	US$1 billion	US$500 million	CNH2.5 billion	EUR1.25 billion CNH2.5 billion	US$1 billion	EUR500 million

Table 4: Summary of Key Product Authorisation and Listing Regime for Debt Securities in Hong Kong

	Offered to Professional Investors only	**Offered to the Public (including Retail Investors)**
Unlisted Debt Securities	• They are exempted from prospectus requirement in the CWUMPO and do not require authorisation from the Securities and Futures Commission ("SFC").	• The prospectus regime under the CWUMPO must be complied with for issuances to the Hong Kong public (that are not considered to be structured products), unless an exemption applies[20] and will require authorisation from the SFC.
Listed Debt Securities	• They are governed by Chapter 37 of the Listing Rules. • The HKSE takes a "light-touch" approach to vetting and in practice the HKSE will typically process applications within one to two business days.	• For debt securities that are to be listed, pursuant to the Memorandum of Understanding Governing Listing Matters dated 28 January 2003 and its First Addendum dated 9 March 2018, the HKSE is the primary front-line regulator and remains the contact point for all listing applications. Hence, approval must be obtained from the HKSE and the listed retail bonds must comply with the requirements set out in the Listing Rules. The listing of retail bonds is governed by Chapters 22 to 36 of the Listing Rules.

20 The exemptions are set out in the Seventeenth Schedule of the CWUMPO, commonly known as the "safe harbours" from having to comply with the prospectus regime. Where an exemption applies, the offering document needs not be a "prospectus" and the provisions governing prospectuses under the CWUMPO would not apply.

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