Exploring Determinants of Firms' Participation in the New Offshore Renminbi Debt Securities Market

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Summary

China began the process of internationalizing the RMB in successive steps initiated by making the RMB fully convertible under the current account in 1996. It has operated a managed floating exchange rate since 2005. Investors were first permitted to hold investment assets on Chinese exchanges with the opening of the Qualified Foreign Institutional Investor (QFII) scheme in 2002. The threshold for qualification was progressively reduced in 2006, 2007 and 2012, and now the People's Bank of China allows QFIIs substantial to access to investment assets including the inter-bank bond market. Use of RMB offshore has been permitted for a widening range of activities since 2009 the offshore bond market is separated from the onshore market due the central bank's intervention in the foreign exchange market Nevertheless the offshore market has also been progressively deregulated for investors. In 2011 a parallel QFII scheme in RMB was established, known as RQFII. Quotas were raised for RQFIIs from RMB20bn to RMB50bn in April 2012 and to RMB200bn in December 2012, and March and May 2013 saw further relaxation of the criteria for RQFII access.

The ‘dim sum' bond market did not exist until 2007 when the China Development Bank issued its first RMB bond; although the first issuers were Hong Kong or mainland banks, the popularity of offshore bonds developed a major market for Hong Kong but the issuance was sparse until 2010. Hong Kong now has the largest market for RMB offshore debt securities, with a substantial range of issuers and banks that facilitate the issuance and sale of these financial products to investors. Using data collected by the Market Research Division of the Research Department of the Hong Kong Monetary Authority we explore the emergence of this market at the firm level, matching the data on issuance with data from Compustat Global to provide balance sheet and profit and loss information for each firm.

Our paper focuses on a micro story that considers how firms' and investors' decisions to engage in the offshore RMB debt securities market are affected by market conditions. There are a number of papers that have explored the development of onshore and offshore bond markets in emerging economies. Mizen and Tsoukas (2012) and Mizen et al (2012) show that market depth, lower short-term interest differentials, that allow firms to issue cheaply and a supporting financial infrastructure such as sufficiently active swap markets, enhance the issuance of offshore bonds. Our paper confirms that the depth and liquidity of the market, lower costs of issuance versus onshore or foreign currency alternatives, favourable swap rates and exchange rate appreciation were also influential in the case of the RMB. These changes occurred at much the same time as a relaxation of regulations by the authorities, permitting expansion to occur as evidenced by the growth of RMB deposits and greater foreign issuance of RMB debt securities.