

# Fidelity Fixed Income

## Overview of the China Bond Markets

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Investment Director



June 21

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Past performance is not a reliable indicator of future returns. Overseas investments will be affected by movements in currency exchange rates. Investments in emerging markets can be more volatile than other more developed markets. There is a risk that the issuers of bonds may not be able to repay the money they have borrowed or make interest payments. When interest rates rise, bonds may fall in value. Rising interest rates may cause the value of your investment to fall. Reference to specific securities should not be construed as a recommendation to buy or sell these securities and is included for the purposes of illustration only.

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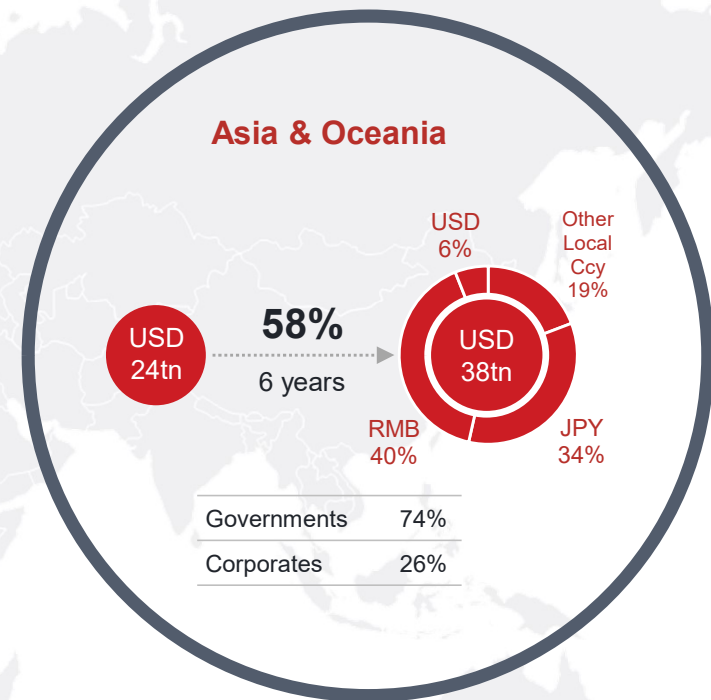
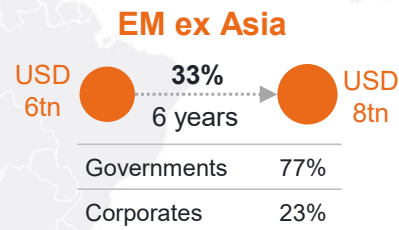
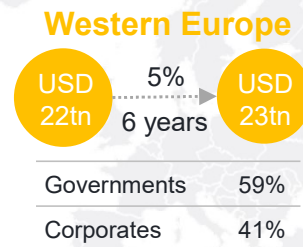
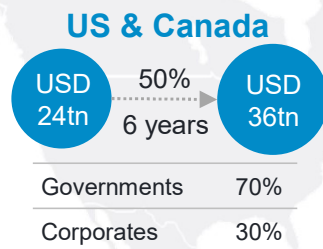
# China Bond Markets Overview

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# Global fixed income market at a glance

China still an underweight of Asia's USD 38 trillion bond opportunity

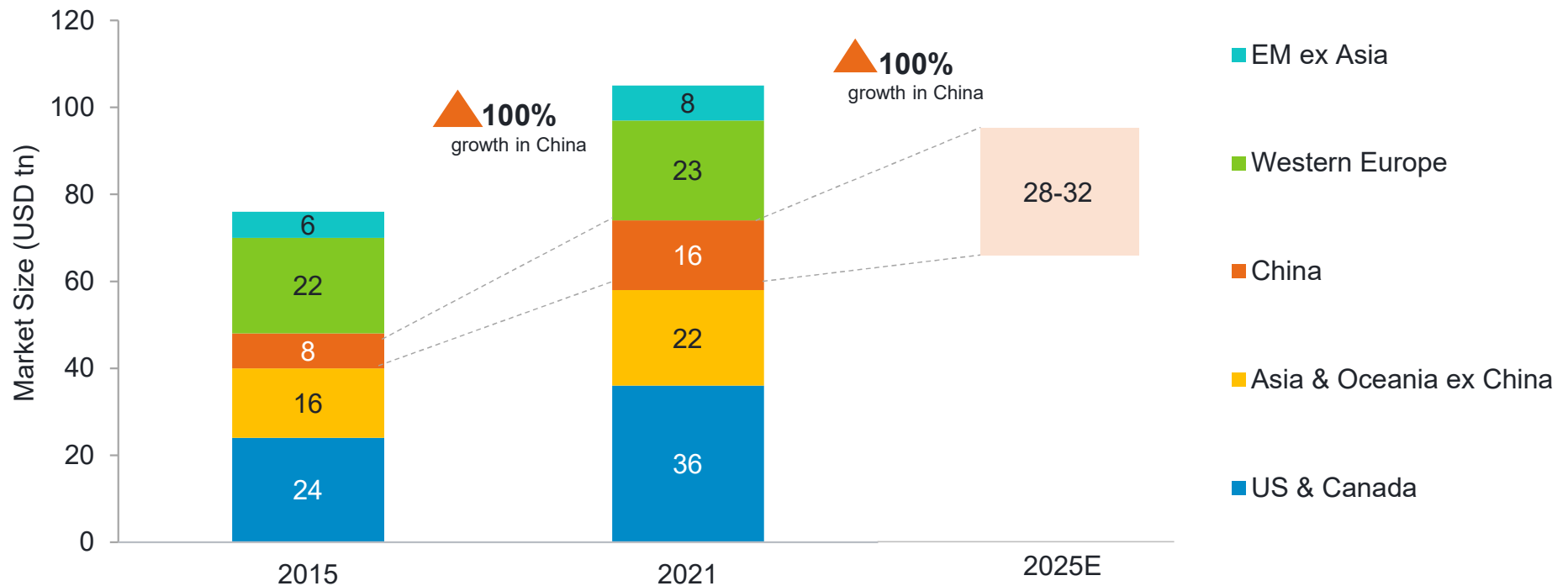
## Global bond and credit markets



Source: Fidelity estimates, Bloomberg, notional amount outstanding as of January 2021. Size of bond market is screened from Bloomberg fixed income search for Corporate and Government bonds only. US includes USD-denominated bonds. Western Europe includes EUR, GBP & USD denominated bonds while Asia and EM ex Asia includes all local currency bonds. Includes bonds with greater than USD 100mn outstanding.

# China fixed income market is the largest and fastest growing




## China bond market: 2nd largest bond market globally



Note: Global bond & credit markets at c.USD105-110tn Issuers with >100m outstanding  
 Source: Fidelity estimates, Bloomberg, notional amount outstanding as of March 2021. Size of bond market is screened from Bloomberg fixed income search for Corporate and Government bonds only. US includes USD-denominated bonds. Western Europe includes EUR,GBP & USD denominated bonds while Asia and EM ex Asia includes all local currency bonds. Includes bonds with greater than USD100m outstanding.

# Key building blocks of China fixed income exposure

Different characteristics to satisfy different market conditions

Markets	Issuers	Type	Currency	Credit Rating issued by
 <b>Onshore Bonds</b>	<b>Chinese</b>	Onshore	CNY	Onshore credit rating agencies
 <b>Offshore USD Bonds</b>	<b>Asian</b> (60-70% are issuers from Greater China)	Offshore	USD	International credit rating agencies
 <b>Dim Sum / CNH Bonds</b>	<b>Chinese or Multinational</b>		CNH	

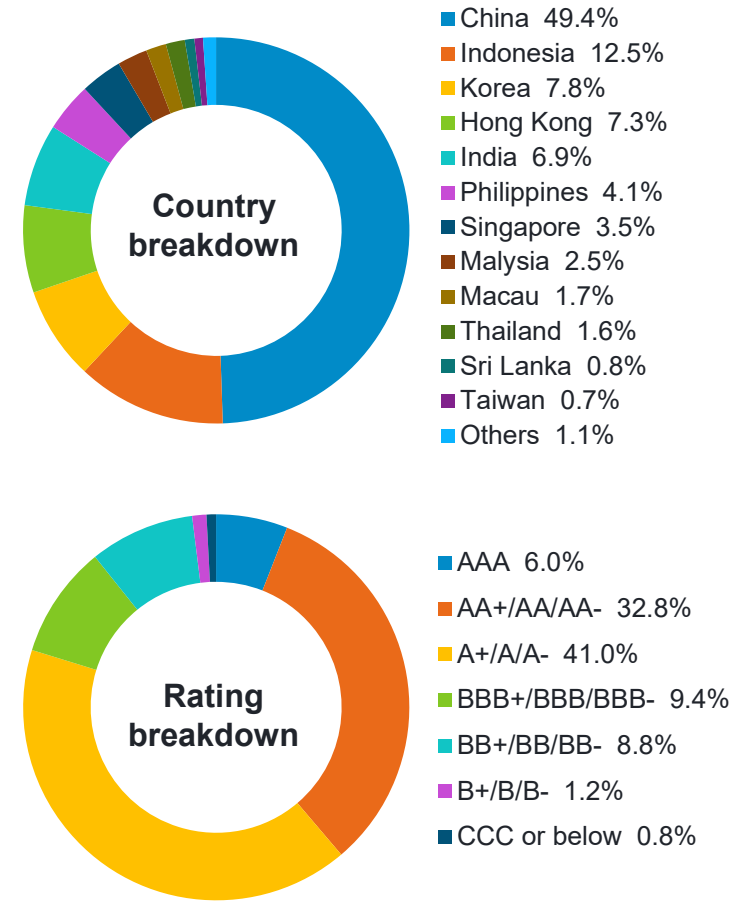
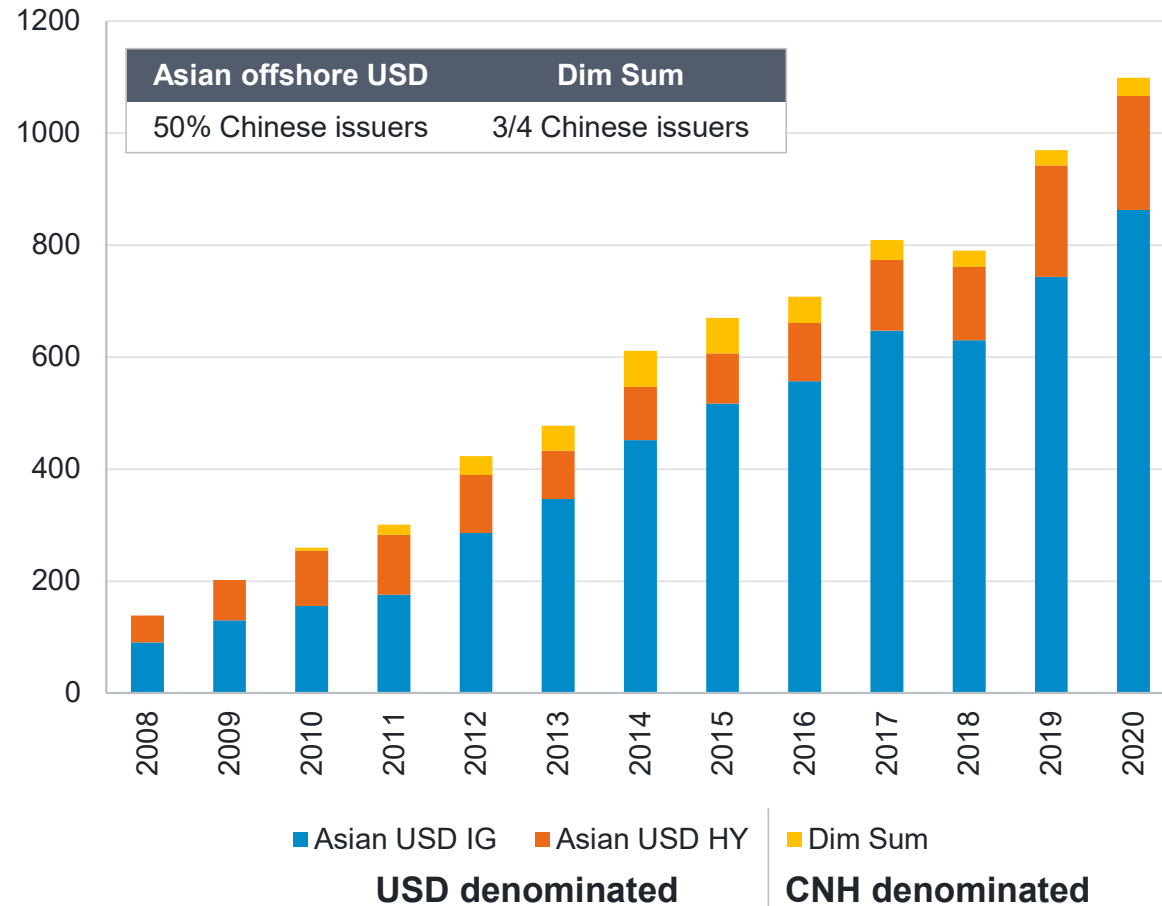


# 1. Asian offshore USD bond market

Chinese issuers account for 50% of the >USD1 trillion Asian USD Bond market

Rapid growth in USD IG and HY; shrinking Dim Sum market

Asian USD Bond



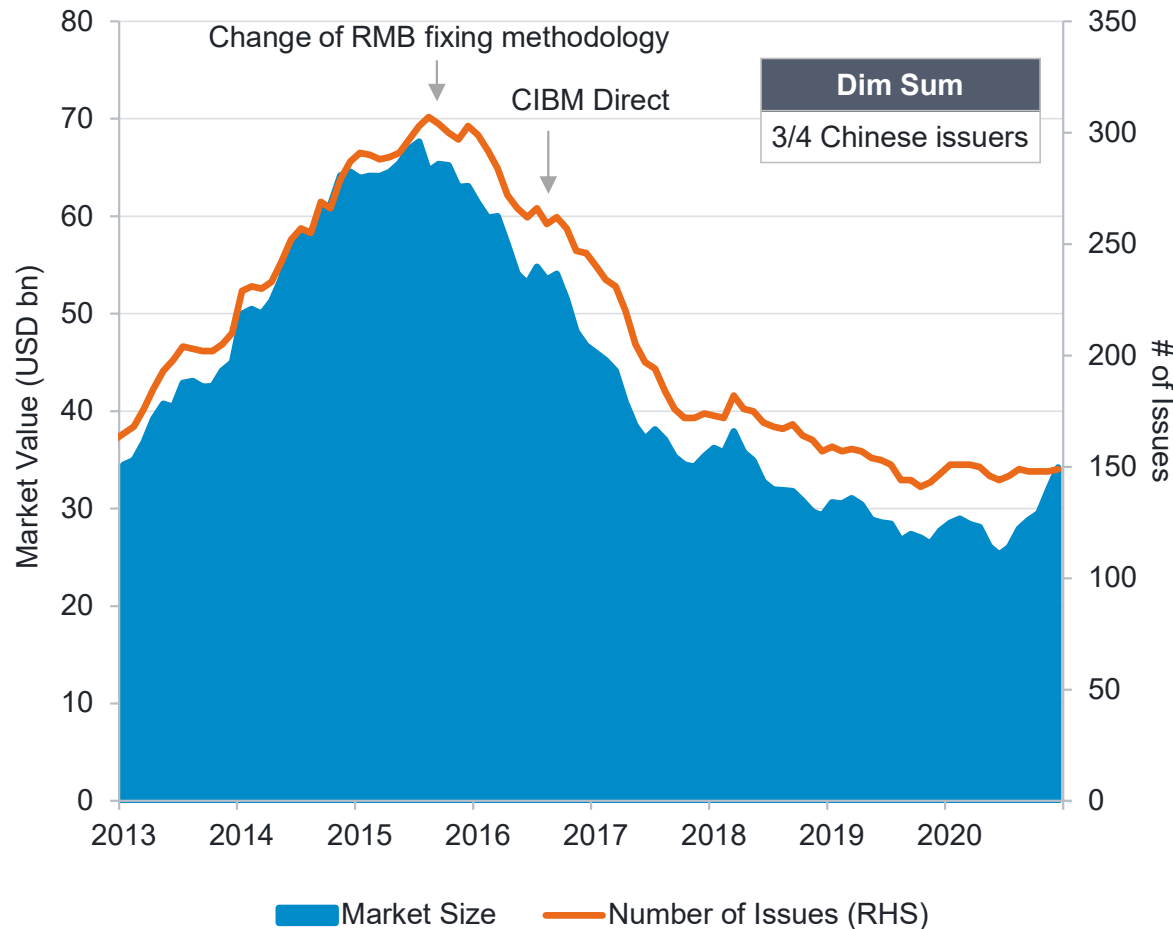
Source: Fidelity International, ICE BofAML Bond Indices, ADOL, ADIG, ADHY and CNHJ for Asia bond, Asian IG, Asian HY and Dim Sum market respectively. CHHJ index officially launched in January 2011. Data is as of December 2020.



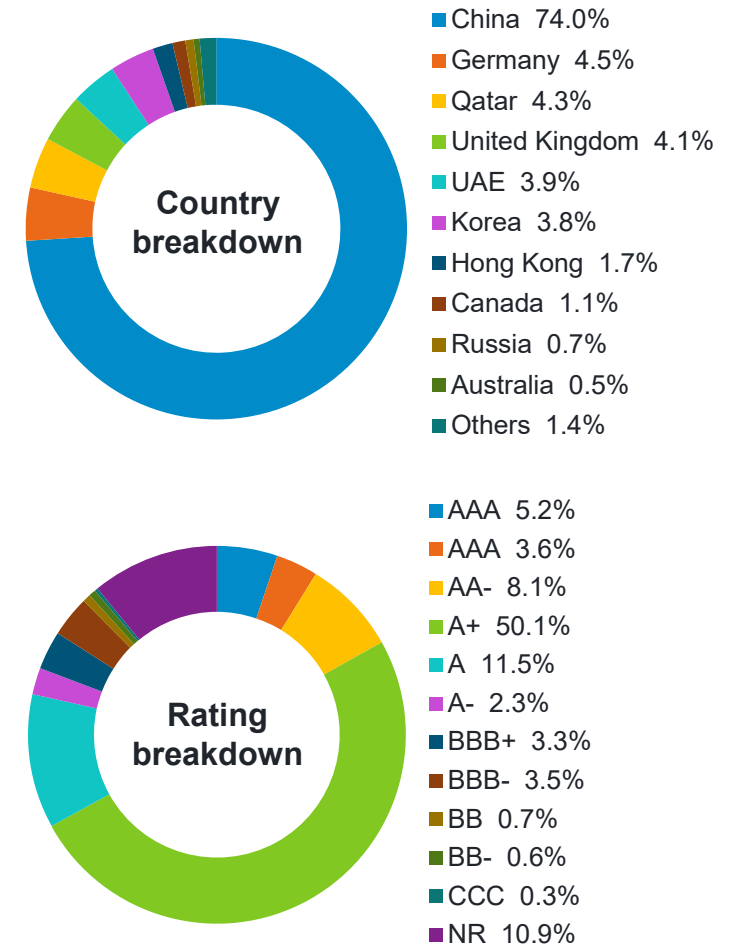
## 2. China offshore dim sum bond market

Dim Sum bond market size have reached equilibrium

### Evolution of Chinese offshore dim Sum bond market



### China offshore dim sum bond

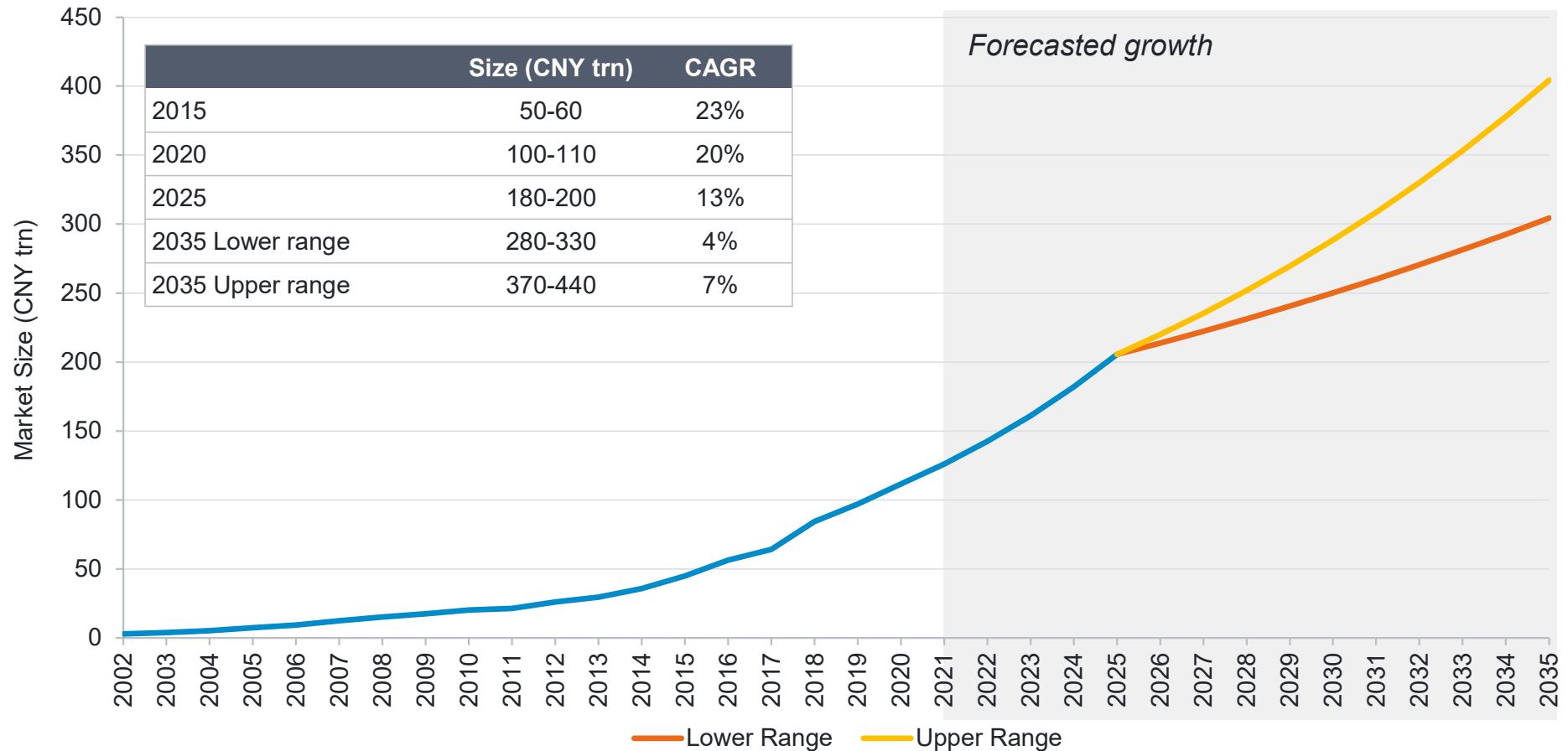


Source: Fidelity International, Bloomberg, ICE BofAML Bond Index: CNHJ, as of December 2020.

### 3. China onshore bond market

Substantial growth potential ahead

#### Size of China onshore bond market — A USD16 trillion market



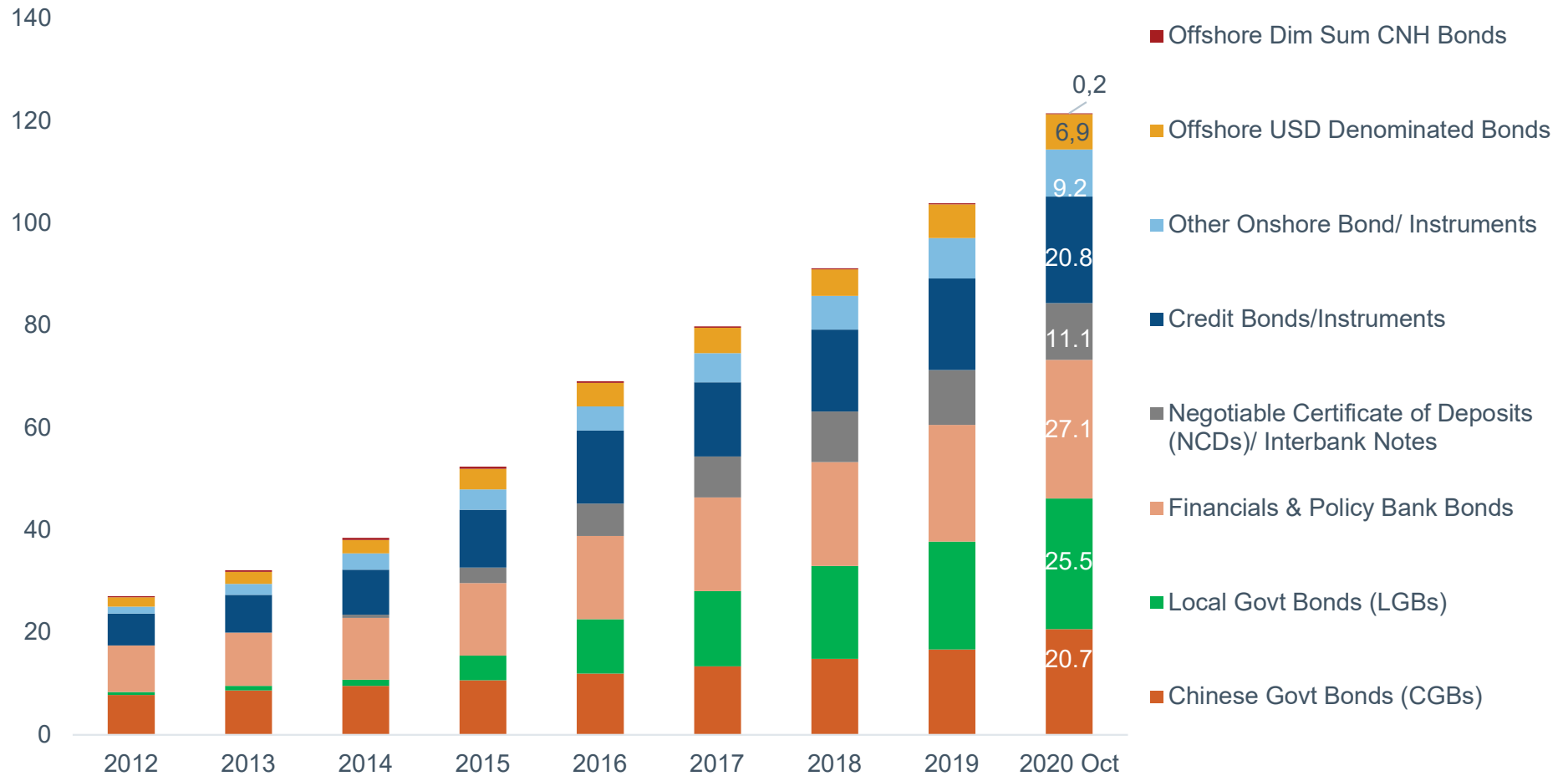
Past performance is not a reliable indicator of future results.

Source: Fidelity International, Hong Kong Exchanges and Clearing Limited, China Central Depository & Clearing Co., Ltd (CCDC), Citi, WIND, as of 2021.

# China onshore bond market: A fast-growing opportunity set

A growing variety of instruments

## Evolution of china bond market (CNY tn)



Source: Fidelity International, CCDIC, PBoC, NBS, Bloomberg, J.P. Morgan, JP Morgan Asian Credit index, ICE BofA China offshore broad market Index, as of October 2020.

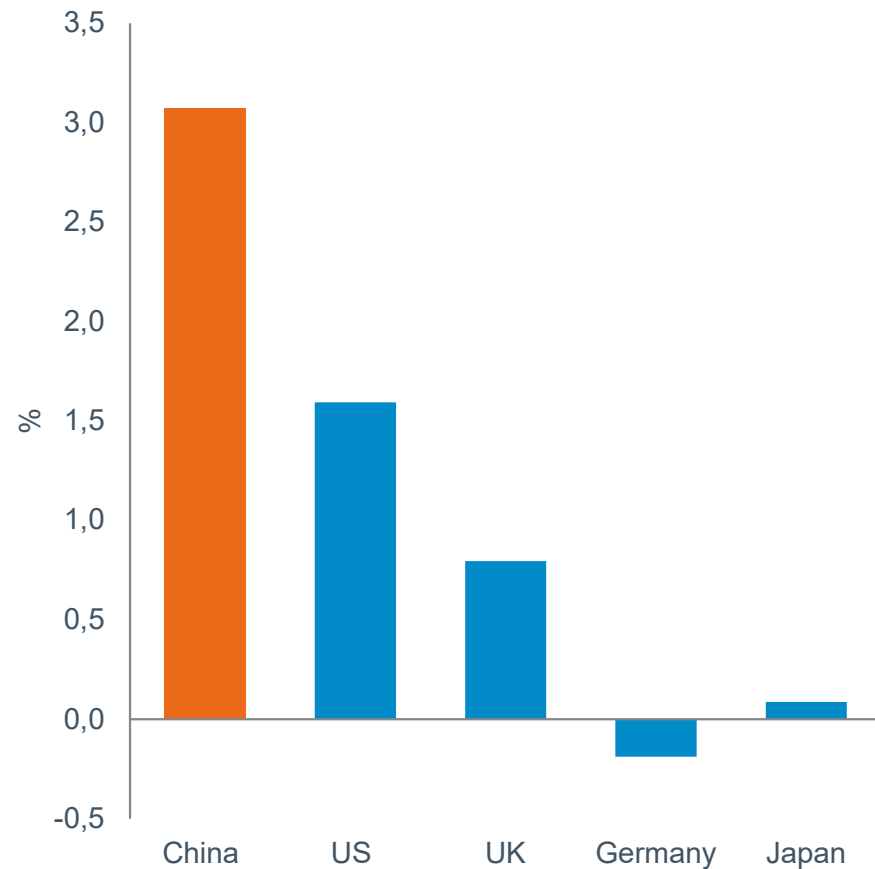
# The Case for China Bond Markets

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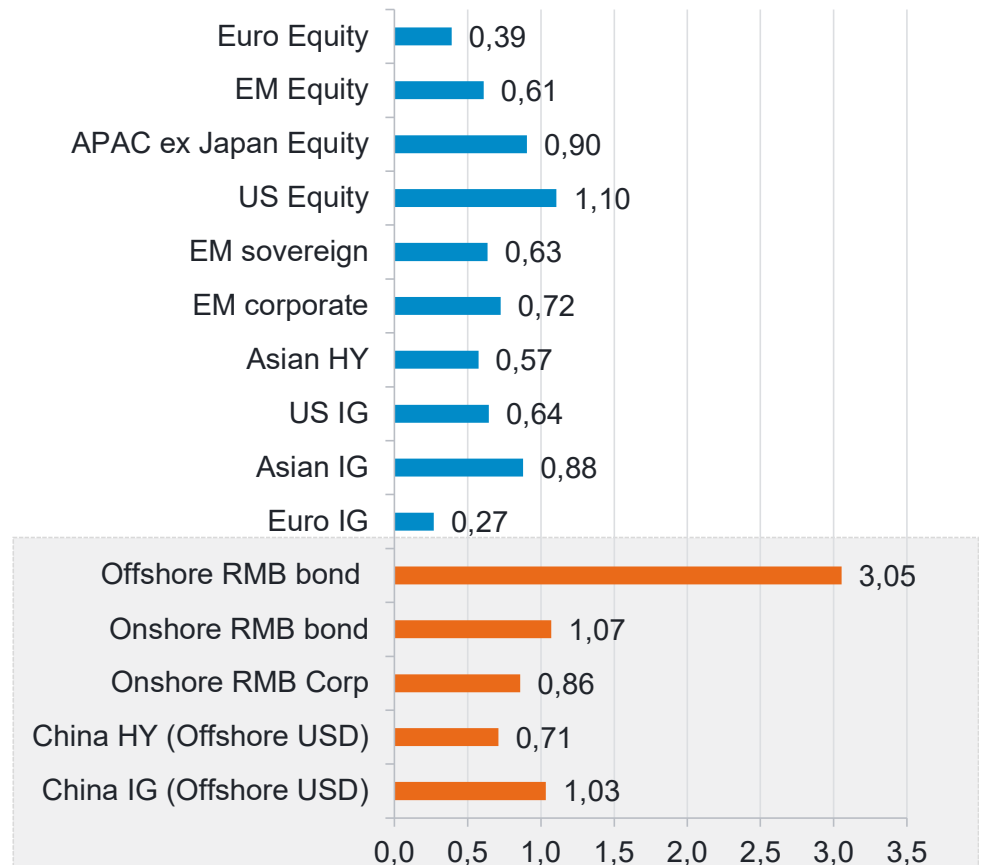
# Attractive risk-adjusted returns

Highest yielding among DM sovereign bond markets

## 10-year government bond yields



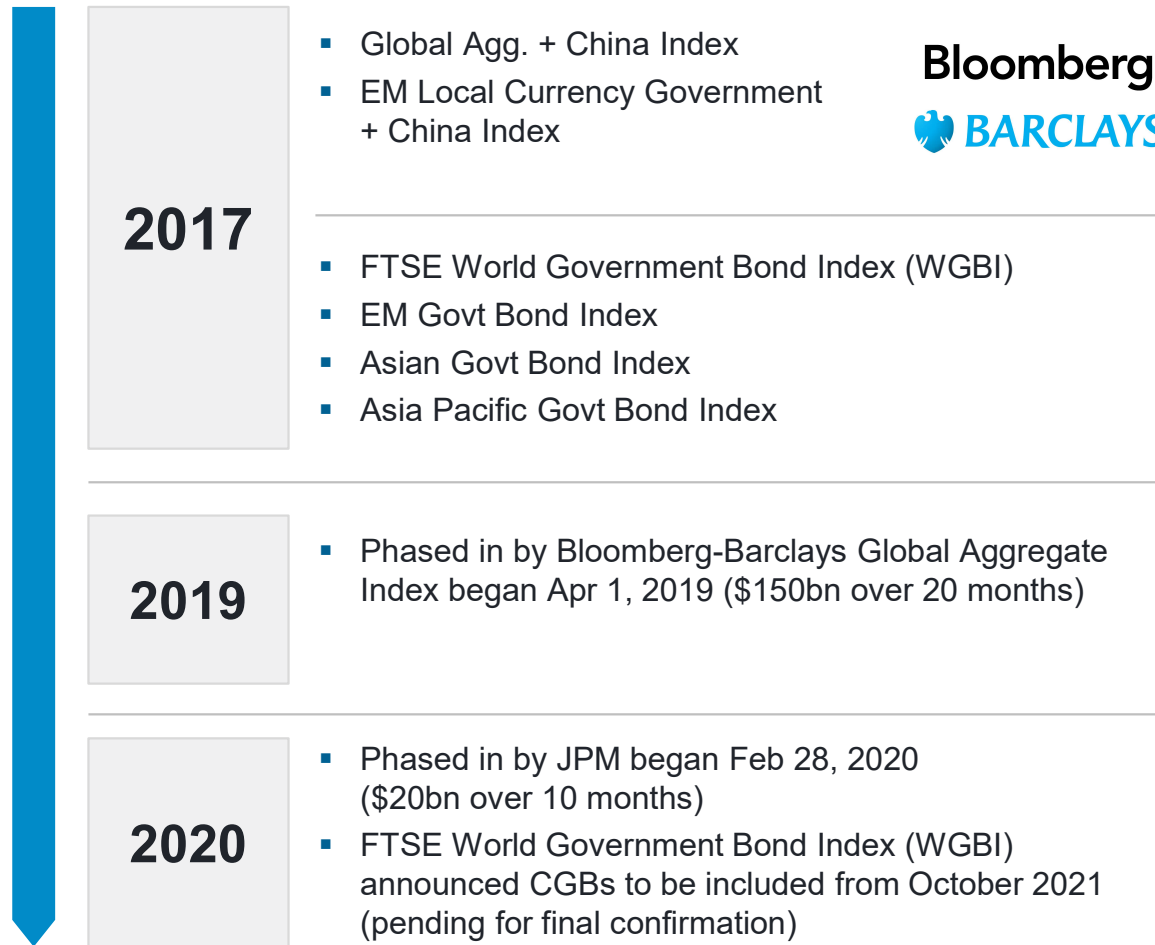
## 5-year Sharpe ratio of asset classes



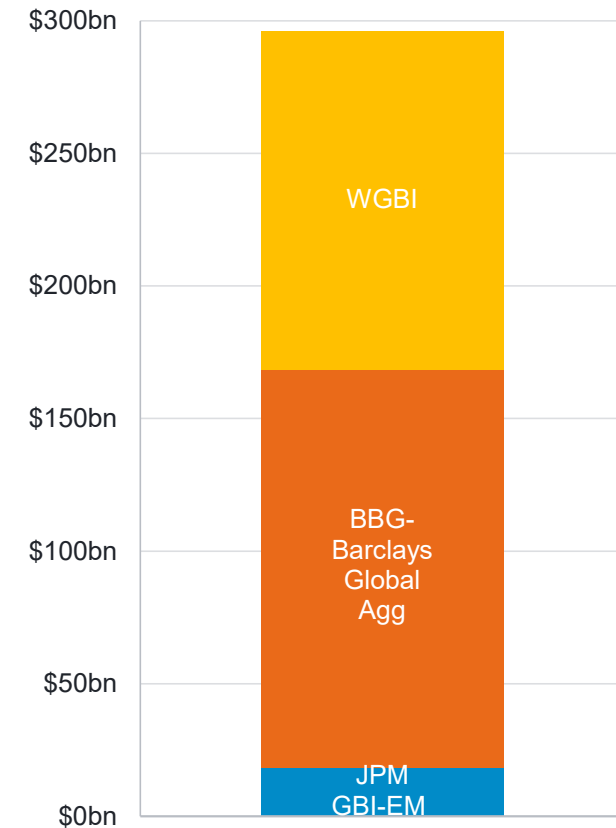
Source: Bloomberg, Fidelity International, May 2021

Source: Fidelity International, Bloomberg, ICE BofAML Bond Indices, J.P. Morgan Indices, ChinaBond, MSCI Equity Indices based on 5-years to May 2021. US 3-Month T-bill was used for Sharpe ratio calculation

# Index Inclusion will bring further inflows



## >\$290bn estimated inflows

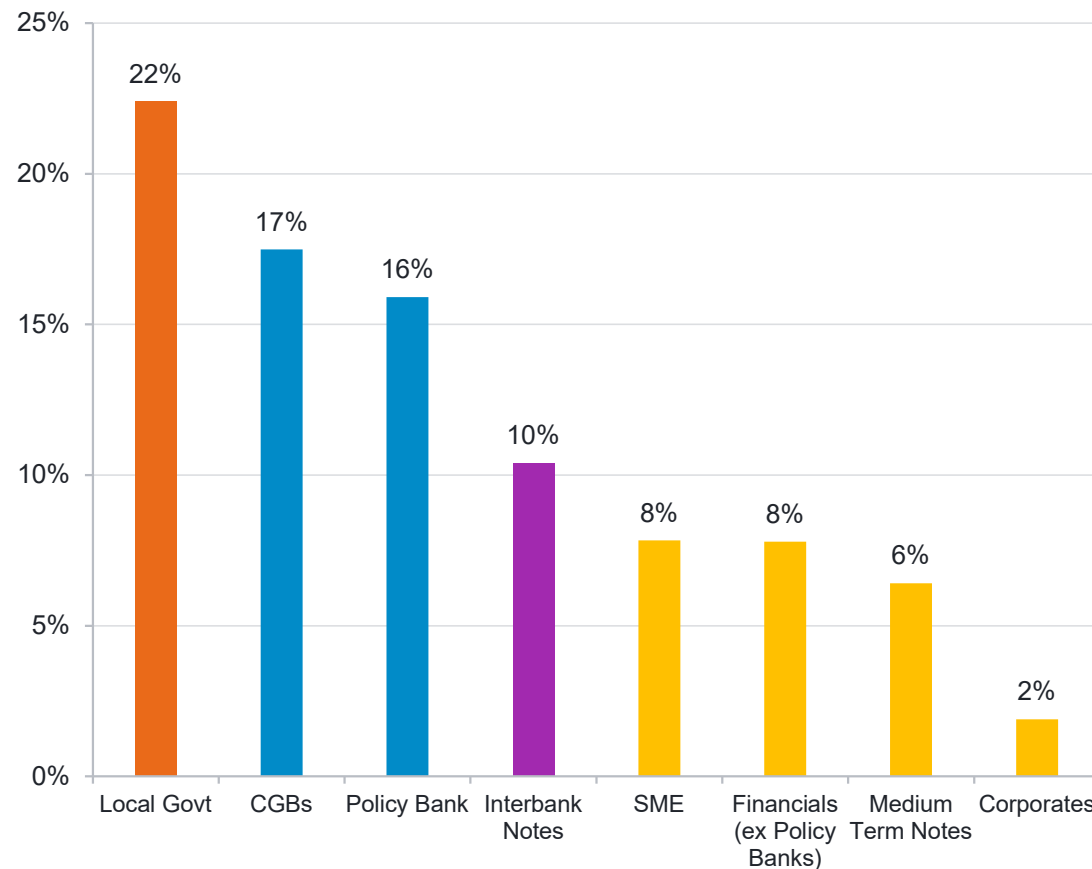


Source: Fidelity International, Citi, Standard Chartered Research. Third party trademark, copyright and other intellectual property rights are and remain, the property of their respective owners. as of 2020

# China onshore bond market

Rapidly developing both in size and sophistication

## China onshore bond market breakdown by segment



Segment	Characteristics	Foreign ownership
<b>Chinese Govt bonds (CGBs) (17%)</b>	<ul style="list-style-type: none"> <li>Index Inclusion</li> <li>Rates futures available</li> <li>Technicals</li> </ul>	~10-15 %
<b>Policy Bank bonds (16%)</b>	<ul style="list-style-type: none"> <li>Exposure to Currency, Curve (rates)</li> <li>Lower volatilities</li> </ul>	~3-5%
<b>Local Govt bonds (LGBs) (22%)</b>	<ul style="list-style-type: none"> <li>Fastest growing</li> <li>Intricacy between Local Gov and issuers</li> <li>Exposure to Currency, Credit</li> </ul>	~0.01%
<b>Onshore Corporate Bonds</b>	<ul style="list-style-type: none"> <li>Mostly onshore rated</li> <li>Liquidity diminish down the credit scale</li> <li>Exposure to Currency, Credit</li> <li>Lower liquidity and yield vs offshore USD bonds</li> </ul>	~1%

Source: Fidelity International, WIND, May 2021. Fidelity estimates on foreign ownership.

# Low correlation offers diversification benefits

	Offshore RMB Bond	Onshore RMB Bond	Onshore RMB Gov	Onshore RMB Corp	Asian IG	Asian HY	US IG	Euro IG	EM Sov USD	EM Sov Local	EM Corp USD	Asian Equity	China Equity	US Equity	Euro Equity	EM Equity	US Treasury
Offshore RMB Bond	1.00																
Onshore RMB Bond	0.08	1.00															
Onshore RMB Gov	0.25	0.97	1.00														
Onshore RMB Corp	0.08	0.96	0.91	1.00													
Asian IG	-0.15	-0.13	0.13	-0.16	1.00												
Asian HY	0.37	-0.02	-0.04	0.03	-0.09	1.00											
US IG	0.29	0.03	0.05	0.05	-0.01	0.73	1.00										
Euro IG	0.35	-0.02	0.01	0.00	0.13	0.69	0.67	1.00									
EM Sov USD	0.36	-0.04	-0.03	0.01	0.00	0.88	0.79	0.74	1.00								
EM Sov Local	0.40	-0.03	0.23	0.00	-0.16	0.52	0.45	0.61	0.54	1.00							
EM Corp USD	0.37	-0.07	-0.05	-0.02	-0.19	0.79	0.56	0.64	0.75	0.72	1.00						
Asian Equity	0.44	-0.05	-0.04	-0.02	-0.17	0.71	0.47	0.46	0.61	0.47	0.65	1.00					
China Equity	0.40	-0.08	-0.05	-0.07	-0.10	0.33	0.15	0.16	0.26	0.26	0.25	0.53	1.00				
US Equity	0.40	-0.08	-0.07	-0.05	-0.13	0.70	0.44	0.61	0.62	0.69	0.69	0.71	0.46	1.00			
Euro Equity	0.11	-0.04	-0.09	-0.03	0.06	0.54	0.36	0.36	0.48	0.04	0.28	0.47	0.29	0.55	1.00		
EM Equity	0.40	-0.06	-0.04	-0.05	0.44	0.73	0.51	0.51	0.68	0.51	0.71	0.97	0.50	0.73	0.58	1.00	
US Treasury	0.03	0.22	0.26	0.19	0.52	-0.20	0.40	0.04	0.03	0.36	-0.10	-0.20	-0.22	-0.36	-0.34	-0.24	1.00

Source: Bloomberg, ICE BofAML Bond Indices, J.P. Morgan Indices, MSCI Equity Indices based on 10-years to 31 March 2021. The table uses a linear colour scale from 0 = green to 1 = red. For offshore RMB Bond, data since January 2011. For Onshore RMB Bond, data since January 2013. Return calculation in local currency.



# Low correlation offers diversification benefits

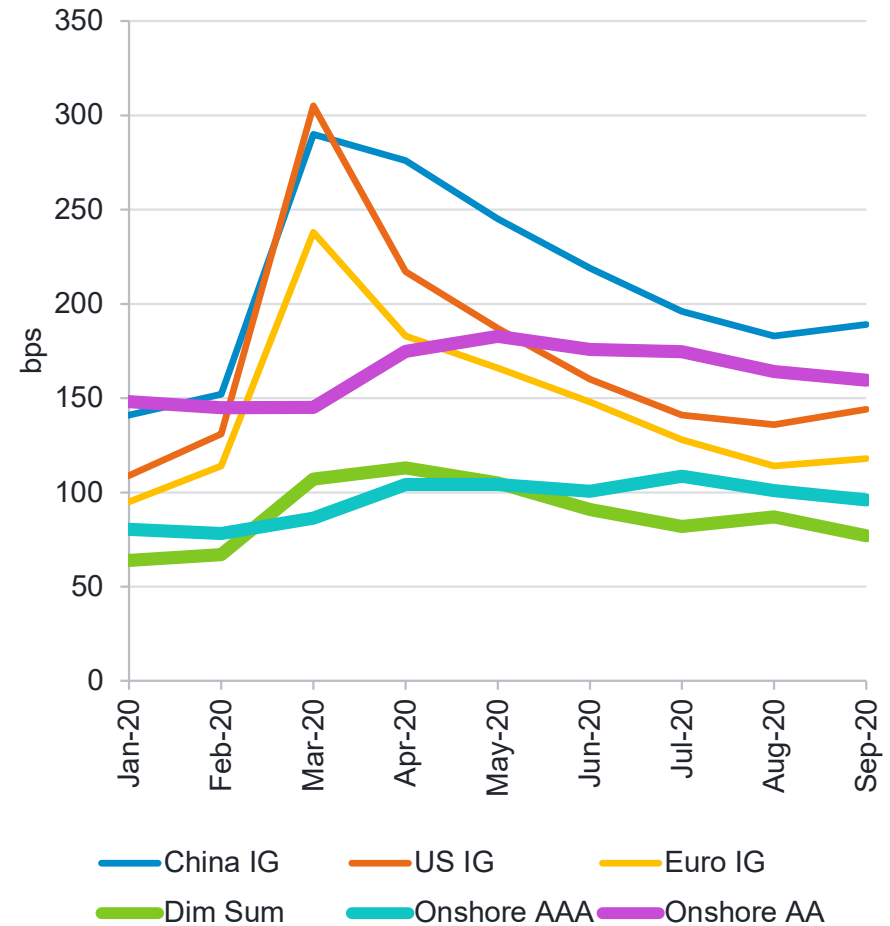
March 2020: Clear divergence

## Government bond yields (%)



Source: Bloomberg; Fidelity International, as of 31 March 2021.

## Onshore and offshore credit spreads across regions

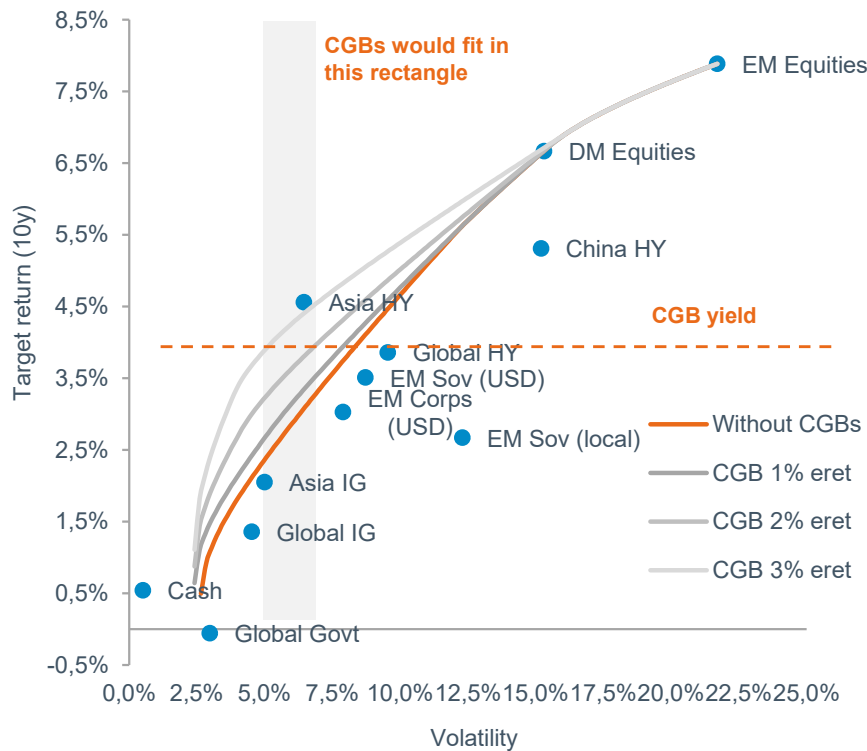


Source: Bloomberg; Fidelity International, as of 30 September 2020.

# Channels: How to gain exposure?

## Building block vs One strategy for China fixed income

### Building block approach: Adding pure onshore CGBs



### An all China fixed income strategy

#### Market index returns



Source: (LHS) Bloomberg, Bank of America Merrill Lynch, Fidelity International, February 2021. Figures represent assumptions based on Fidelity International proprietary models. Data based on monthly total returns for the period December 2004 – June 2020. Indices used: Global Govt: ICE BofA G7 Government Index, Global Investment Grade: BofA ML Global Broad Corp, Asia Investment Grade: ICE BofA Asian Dollar Investment Grade Index, Global High Yield: Barclays Global High Yield Total Return Index Value Hedged USD, Asia High Yield: J.P. Morgan JACI composite Total Return, China High Yield: ICE BofA Asian Dollar High Yield Corporate China Issuers Index, EM Sov (USD): J.P. Morgan EMBI Global Diversified Composite, EM Corps (USD): J.P. Morgan Corporate EMBI Broad Diversified Composite Index, EM Sov (local): J.P. Morgan GBI-EM Global Diversified Composite Unhedged USD, DM Equities: MSCI World total return index, EM Equities: MSCI EM total return index, China gov: ICE BofA China Government Index, Cash: BBA Libor USD 1 month. Past performance is not indicative of future performance. For illustrative purposes only. (RHS) Fidelity International, Bloomberg, Ice BofA Merrill Lynch, April 2021. Index return in based currency. \*Representative strategy comprising onshore China bonds, offshore USD bonds and offshore CNH dim sum bonds.

# Accessing China onshore

Various options



Source: Fidelity International. As of 2021

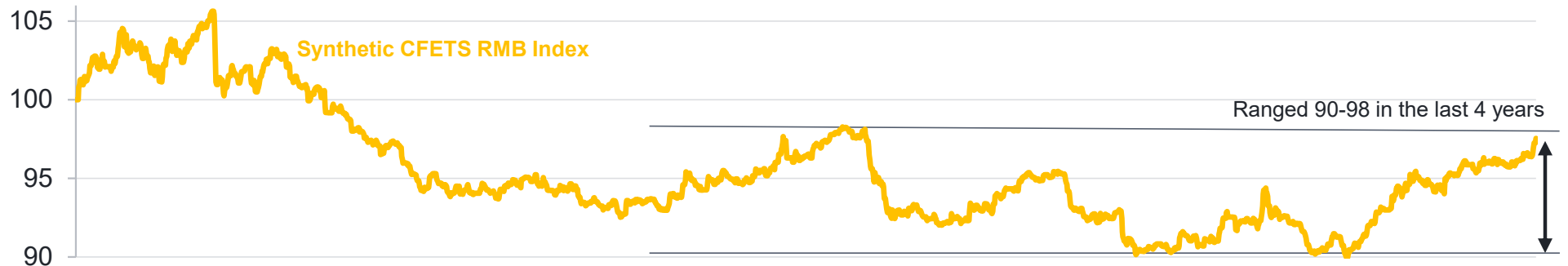
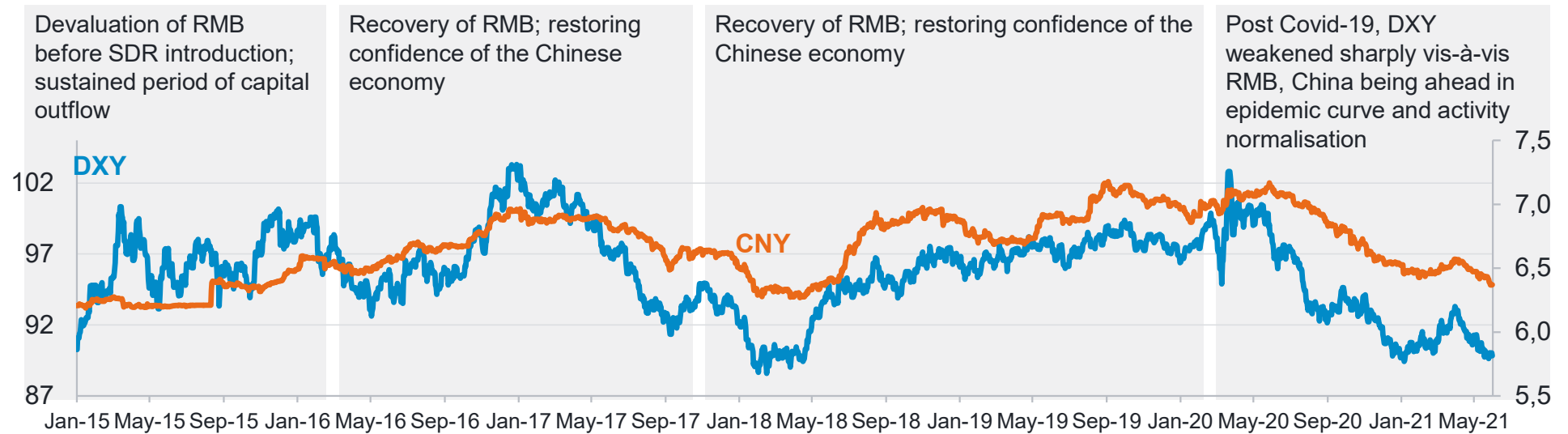
# Frequently Asked Questions

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# RMB

Exhibited stability for the last 4 years on trade-weighted basis

## Most volatility of USDRMB could be explained with USD strength

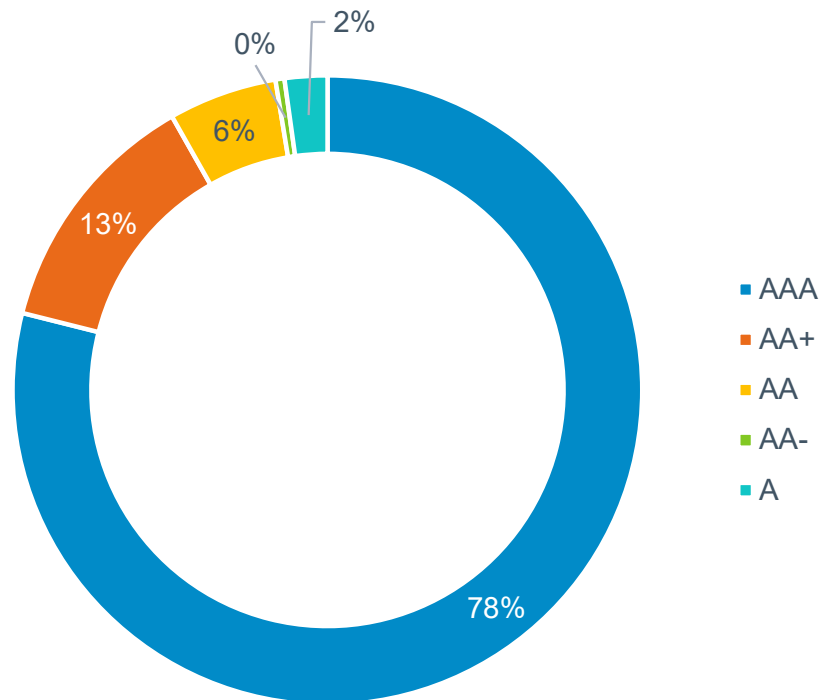


Source: Bloomberg, as of 31 May 2021.

# China onshore bond market: Domestic ratings

Different scales and standards between onshore and international ratings

## Onshore China bond universe by ratings



Onshore Credit Rating	International Equivalent *
AAA	~A/BBB
AA	~BBB/BB
A	~B

Source: Wind, Fidelity International. as of April 2021. \*Credit rating comparison is indicative.

# Credit rating agencies cross border expansions

## International Rating Agencies

S&P

- S&P Global (China) Ratings is the first wholly foreign owned credit agency in the onshore market
- Gained approval from Chinese regulators in Jan 2019

Fitch

- Was JV partner with Lianhe
- Announced plan to launch Chinese rating units in May 2018
- Set up Beijing office in 1997

Moody's

- Owns 30% of China Chengxin International Credit Rating Co (CCXI)

## China Onshore Rating Agencies

China Chengxin International

- SFC Type 10 license in July 2012

Pengyuan International

- SFC Type 10 license in August 2012

Dagong International

- SFC Type 10 license in Jul 2014
- China Operations were suspended in 2018

Lianhe Global

- SFC Type 10 license in Jul 2014

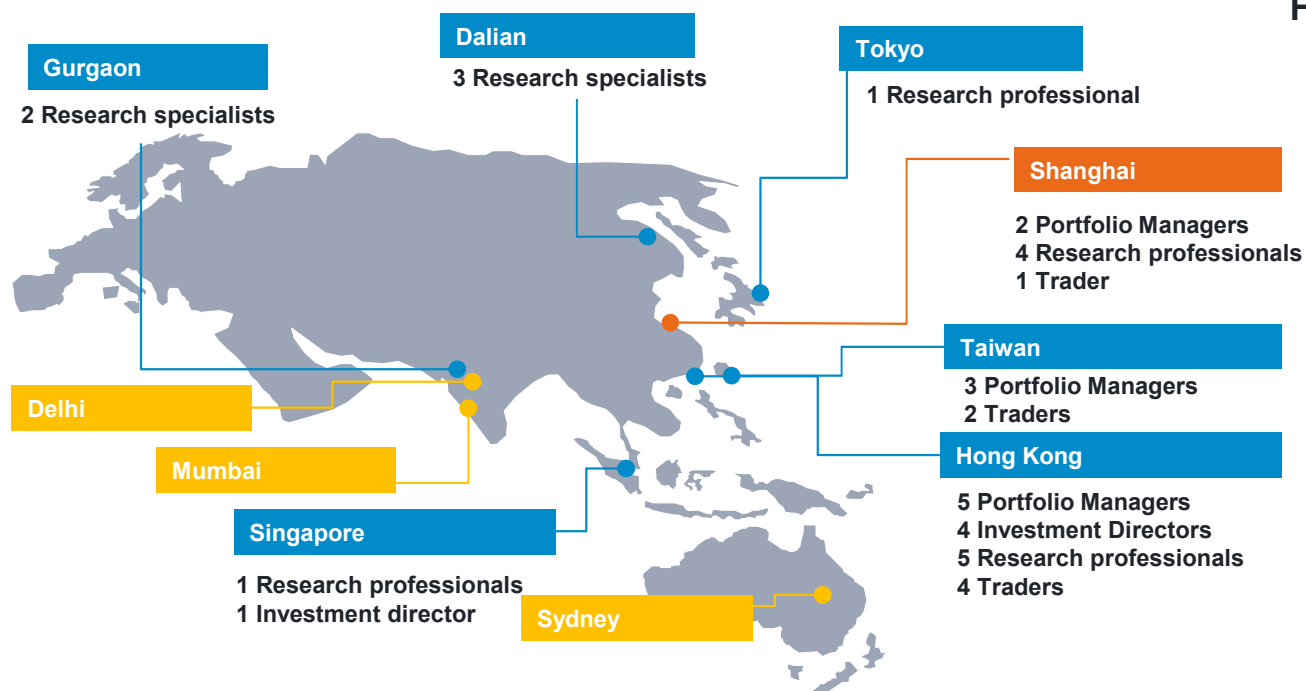
Dongfang Jincheng International

- Focus in onshore operation
- Yet to expand overseas

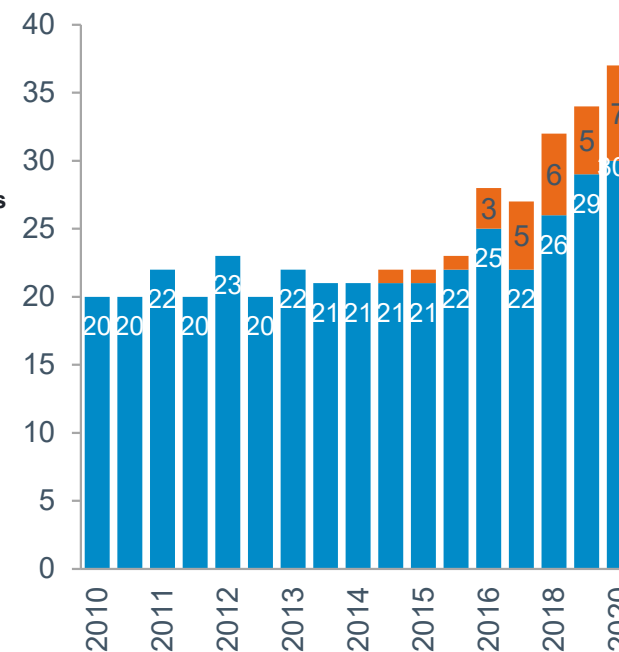
Source: Fidelity International, 2021

# Fidelity fixed income in Asia

## Overview



Headcount \*



■ Mainland China-based (Shanghai WFOE)

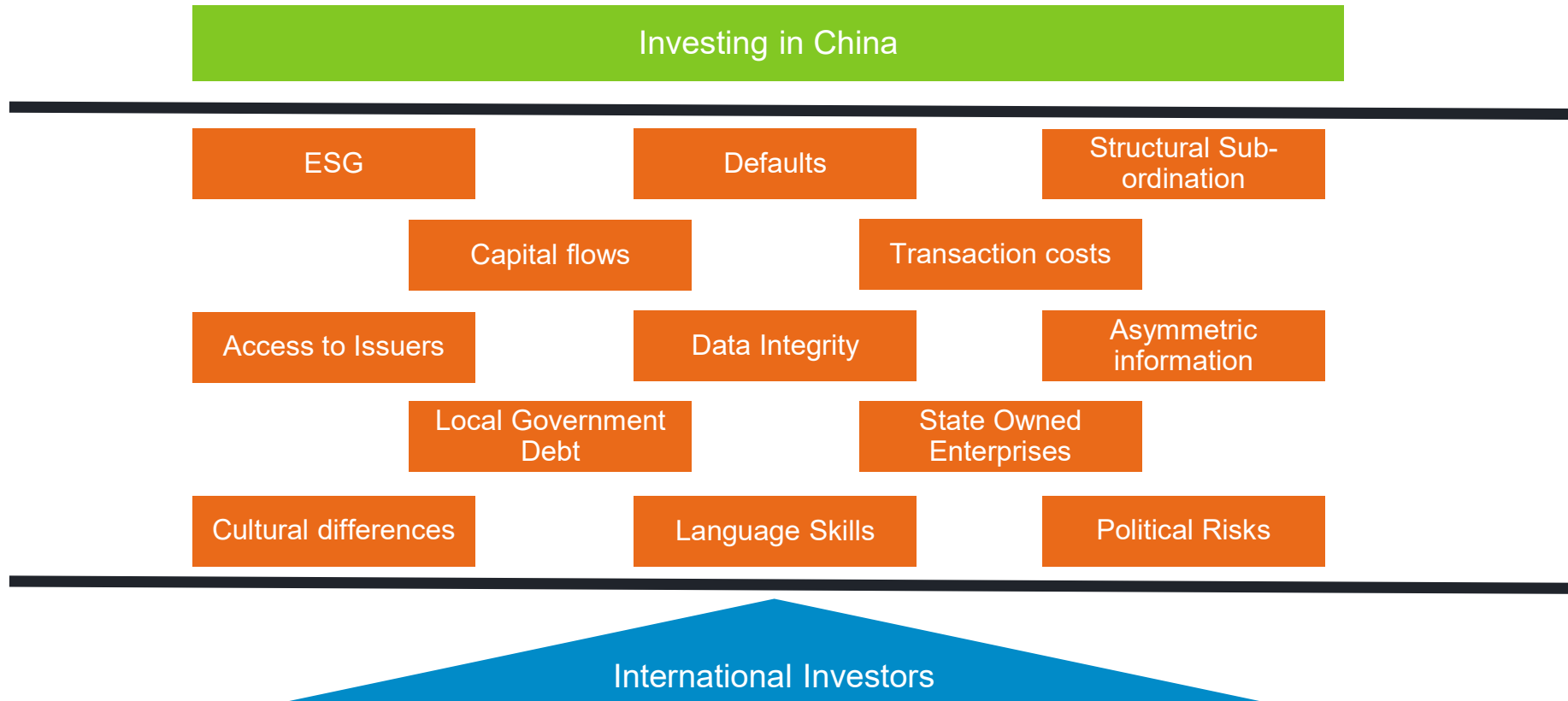
■ Asia xChina based

Source: Fidelity International, March 2021. The chart shows Fidelity's presence in multiple locations including business and investment functions.

Source: Fidelity International, December 2020.  
\* excludes Dalian/Gurgaon Specialists, Operations and Graduates



# Is China any different?

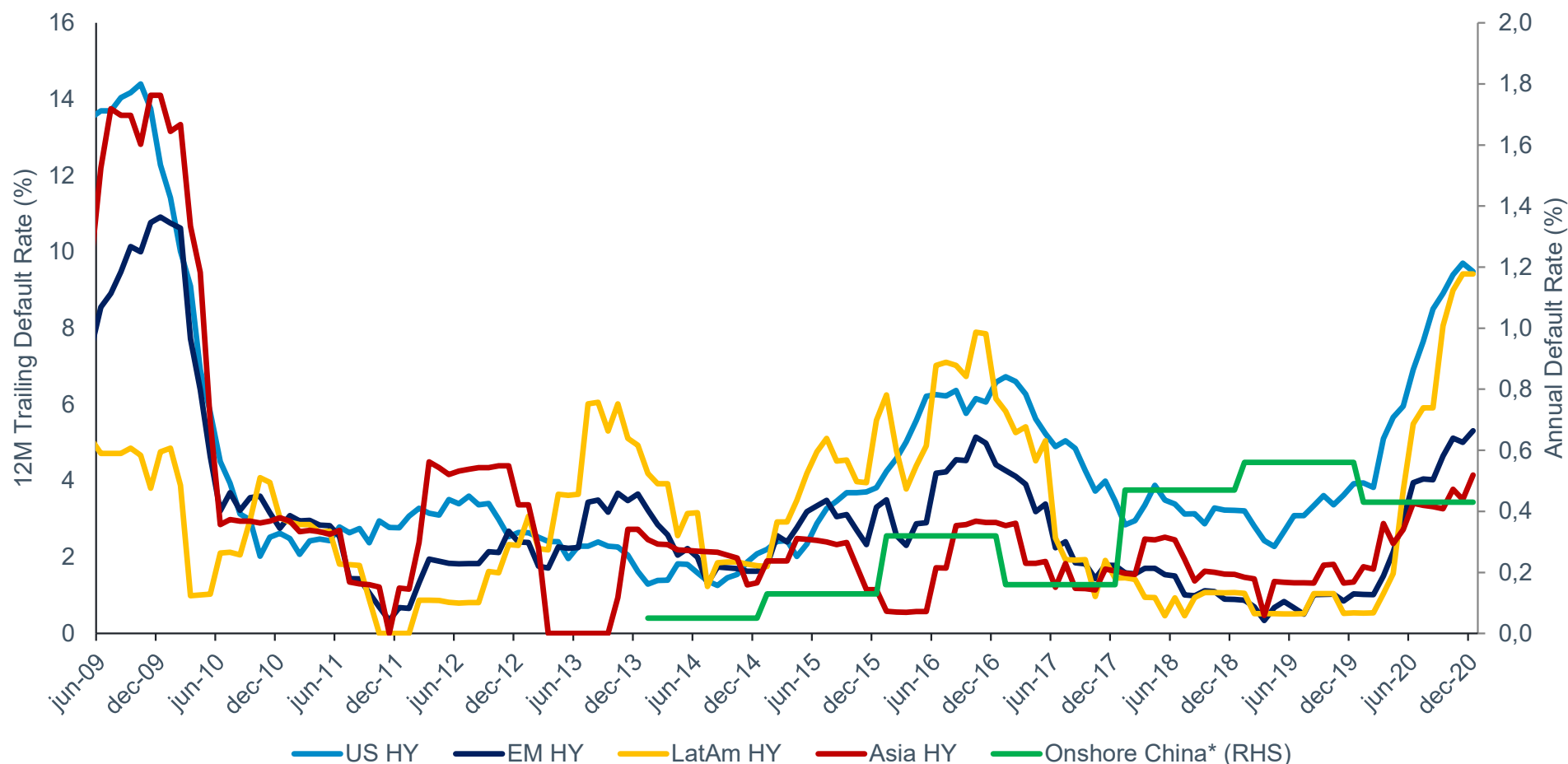


Source: Fidelity International. As of 2021

# Default rate

Asia HY/onshore China show lower default rate than other HY markets

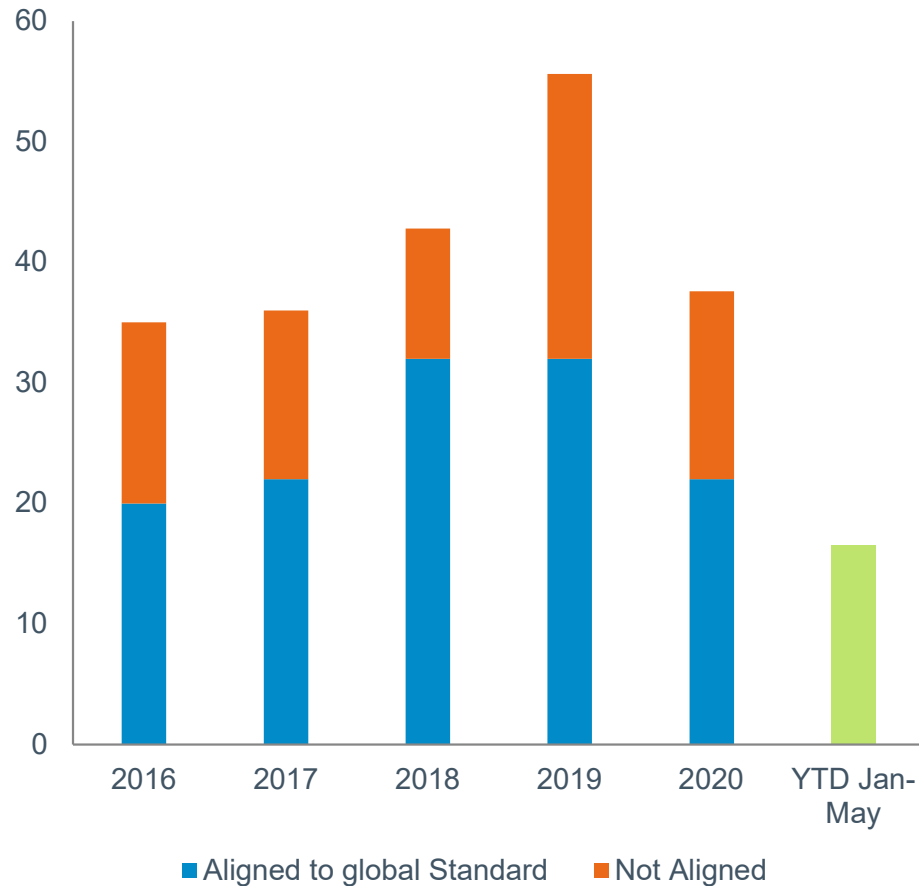
Default rates of US, EM, Latam, Asian High Yield and Onshore China Bonds (Since 2008)



Source: BofA Global Research, WIND, as of December 2020. Onshore China default data is shown annually while 2020 data refers to YTD defaults as of December 2020. Past default rate is not a reliable indicator of future default rates. BofA revised the methodology for calculating default rates for US in July 2020.

# Green bonds in China onshore

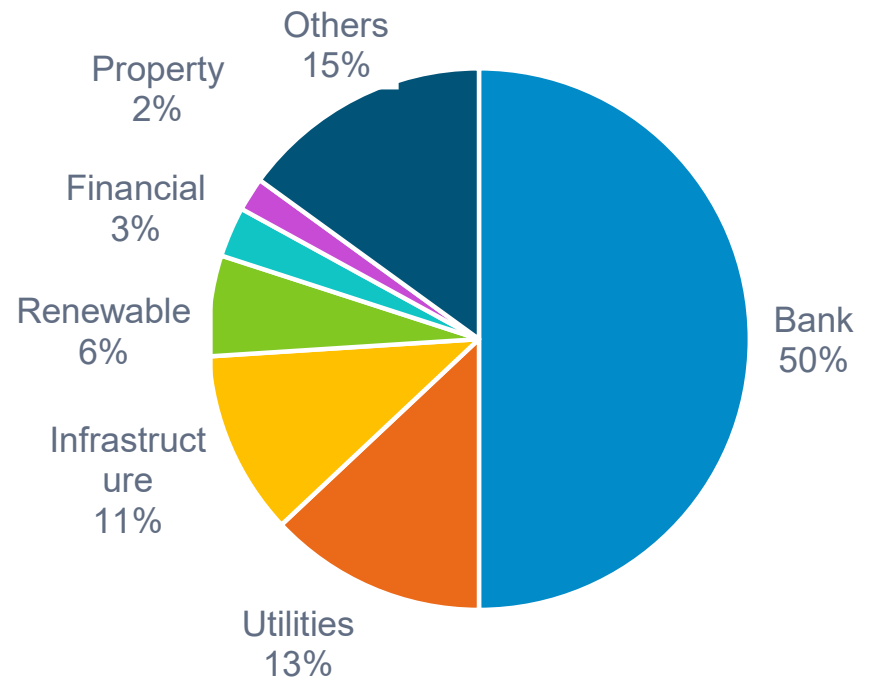
Not all Chinese green bonds are aligned to global standards (Issuance USD bn)



Source: Climate Bonds Initiative, Bloomberg, Brokers estimates, as of May 2021

Note: Alignment is based on use of proceeds

Banks are the largest group of domestic green bond issuers in China

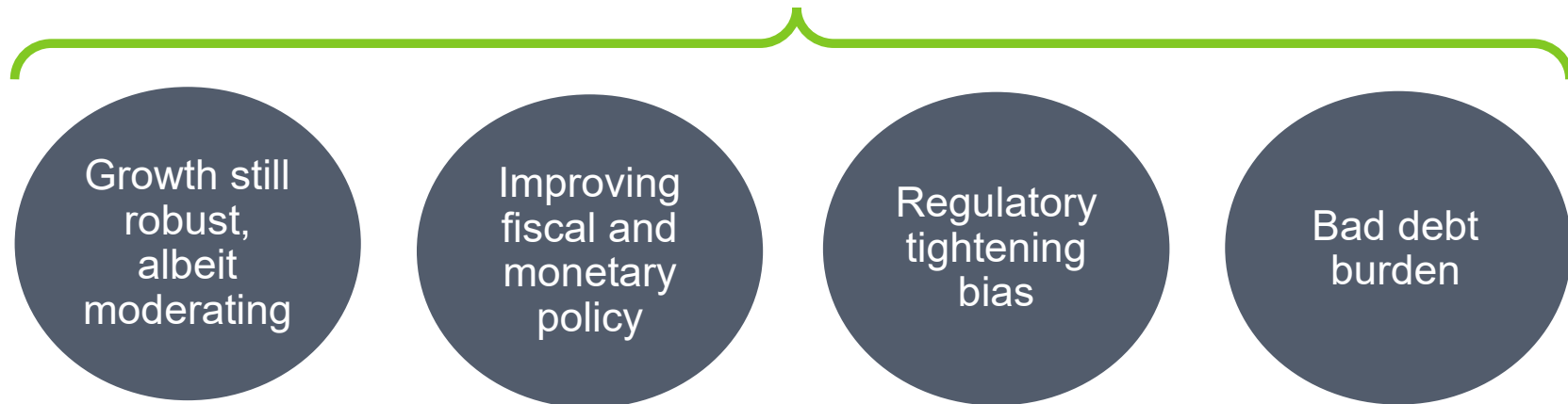


Source: Bloomberg, brokers estimates, as of May 2021

# China Overview

Generally supportive backdrop and manageable near-term risks

## Current Environment



## What to watch?



Source: Fidelity International. As of 2021

# Vanessa Chan

## Investment Director, Asian Fixed Income



### Vanessa Chan

Investment Director, Asian Fixed Income

**Based in:** Hong Kong

**Industry Experience:**  
20 years

**Investment Experience:**  
3 years

**Education:**  
The London School of Economics  
and Political Science,  
Bsc. Accounting and Finance

**Vanessa Chan** is an Investment Director, Asian Fixed Income where she has a strong focus in Asian and China High Yield as well as China. She has spent over 17 years in Asian Fixed Income market covering both sell side, buy side and rating agencies roles.

She joined Fidelity in August 2017 from Fitch Ratings Hong Kong where she was a Director in the Corporates team. Prior to Fitch, she had over 10 years of Investment Banking experience in Hong Kong and UK.

At Fitch, Vanessa was responsible for rating Chinese and Hong Kong issuers, with a focus on property companies, retailers and conglomerates. Besides her credit analysis background, Vanessa has gained a long experience in investment banking, at Credit Suisse as Head of Ratings Advisory as well as at other tier-one banks such as HSBC and UBS.

Vanessa holds a BSc degree in Accounting and Finance from the London School of Economics and Political Science in the United Kingdom. She is fluent in English, Mandarin and Cantonese.

Source: Fidelity International, 2020.

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