



# TRADING WITH CHINA: THE RISE OF OFFSHORE RENMINBI BUSINESS

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# INTRODUCTION

## TRADING WITH CHINA: THE RISE OF OFFSHORE RENMINBI BUSINESS

The Asia Society with the support of ANZ are delighted to launch this publication focusing on the evolution of offshore RMB trade. The aim is to provide support for dialogue among top business leaders and policymakers on the wider use of RMB, in the context of Sino-Australasian commerce and trade. Our hope is that this report will help increase awareness of the business opportunities and wide range of products and services in this new market, and promote the significance of such a market in the currency and risk management of companies engaged in trade with China.

Hong Kong has been established as the “offshore RMB” market. Since early 2010, the offshore RMB FX market in Hong Kong has grown significantly, with RMB-denominated deposits reaching RMB310bn (or US\$48bn) by the end of 2010, up from RMB62bn (US\$9bn) a year earlier. Cross-border trade settlement reached RMB101bn (US\$15bn) per month as at December 2010, compared with just RMB10bn (US\$1.5bn) in June 2010, the first month the trade settlement scheme was expanded to cover 20 Chinese provinces and cities.

We have seen the first Australian and New Zealand companies dipping their toes into this market late in 2010, and believe there will be rapid take-up and expansion in 2011 as the benefits of RMB-based transactions become clear.

ANZ’s support for this initiative falls within a broad program of corporate responsibility that expresses our deep commitment to the Asia Pacific region. ANZ has had a presence in China for more than 25 years, and has just completed a process of local incorporation to connect global business and our clients within and outside of Greater China. The continued economic and financial development of the region is critical to us and to our customers, and our corporate responsibility agenda reflects this.

The Asia Society AustralAsia Centre was launched in 1997 by Australian Prime Minister, The Hon. John Howard. The Centre is a non-profit, educational organisation and aims to broaden understanding of Asian countries and cultures amongst Australian people, and to strengthen the linkages between political, business, and cultural leaders and decision makers from the Asian region with their Australian counterparts. The AustralAsia Centre does this by running an extensive public programme of business, policy, and cultural events. Past prominent speakers include Lee Kuan Yew, then Senior Minister, Republic of Singapore; H.E. Dr Susilo Bambang Yudhoyono, President of Indonesia; and The Hon. Kevin Rudd MP, then Prime Minister of Australia.

# THE RMB

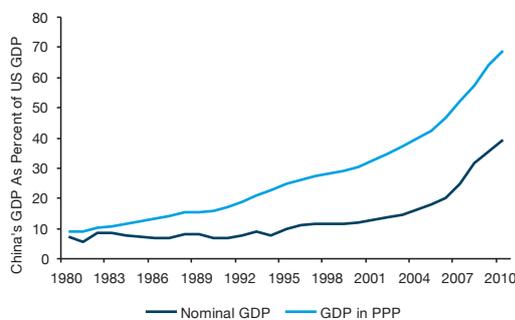
## CHINA'S EXTRAORDINARY RISE

### RAPID RECOVERY FROM THE GLOBAL FINANCIAL CRISIS MEANS CHINA IS EVER MORE IMPORTANT TO GLOBAL TRADE

China's economy achieved two important milestones in 2010: In the first quarter, it overtook Germany as the world's largest trading nation; in the third, it became the second largest economy, surpassing Japan. China also made significant gains on the US, as the size of GDP relative to the US likely rose to 68.6% in purchasing power parity (PPP) terms, up from 57.2% in 2008.

The acceleration of China's involvement in the global economy has also given rise to an important change: a new effort to internationalise the RMB. The driver for changes to RMB management results from the global financial crisis, when China undertook what turned out to have been an incredibly successful economic stimulus package. Growth accelerated, allowing China to contribute more than 30% of global growth over the last two years. The recovery was led by investment and consumption: GDP grew 10.3% year-over-year in 2010 and CPI rose, on average, 3.3%.

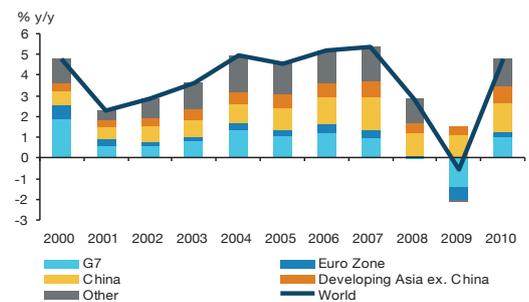
FIGURE 1. CHINA GDP VS US GDP



Source: CEIC; ANZ Economics

Amidst massive stimulus, China's exports also recovered ahead of expectations to pre-crisis levels. In 2009, in the midst of the financial crisis, net exports dragged heavily on growth. By June 2010, however, China's total export receipts, in value terms, had surpassed the pre-crisis peak. This year, net exports' contribution to GDP is expected to turn positive. The sources of China's growth have become more diversified, with external demand also now driving growth.

FIGURE 2. CONTRIBUTION TO GLOBAL GROWTH



Source: CEIC; ANZ Economics

## THE PRICE OF SUCCESS

As a result of domestic stimulus plus the net export recovery, China's growth trajectory has been far stronger than anticipated. The extraordinarily large fiscal package and accommodative monetary policies of the last two years are now of concern. With the resulting rapid increase in money supply and bank credit, inflation is accelerating. China's CPI inflation rate rose above 5% on an annual basis in late 2010, the highest in more than two years and far above the government's target of 3.0% pa. More importantly, monthly inflation has accelerated for five consecutive months, suggesting that inflation momentum has been rising, which in turn has impacted on inflation expectations.

FIGURE 3. CHINA CONSUMER PRICE INDEX

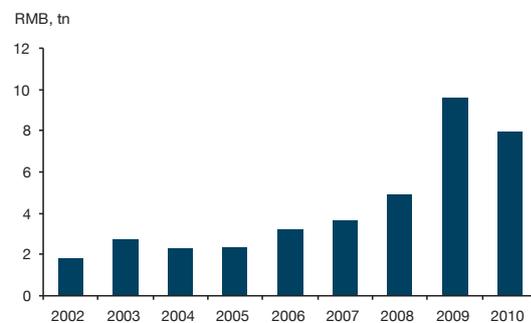


Source: CEIC; ANZ Economics

# THE RMB

Along with inflation has come concern about the risk of an overheating property market. The headline property price index rose by more than 10% per annum in 2010, from a 1.6% annual increase in 2009. The average selling price per square metre reached an historic peak, worsening the housing price to income ratio. Despite cooling measures, property prices have continued to rise and produced a return far higher than other asset classes.

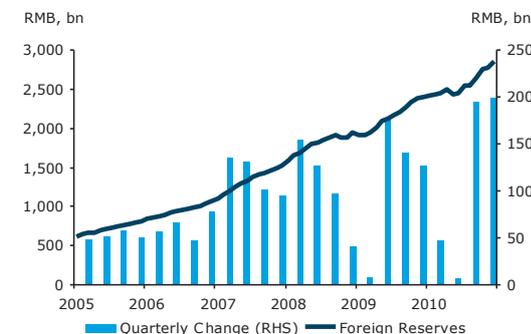
**FIGURE 4. CHINA NEW LOANS**



Source: CEIC; ANZ Economics

Strong underlying demand for housing is a fundamental driver of prices, but low funding costs due to very easy monetary conditions have also had a role to play. Easy monetary conditions can be linked to the fact that China is accumulating large foreign exchange reserves. Reserve accumulation expands the monetary base, and makes it difficult to tighten monetary conditions and reduce credit expansion.

**FIGURE 5. FOREIGN EXCHANGE RESERVES**

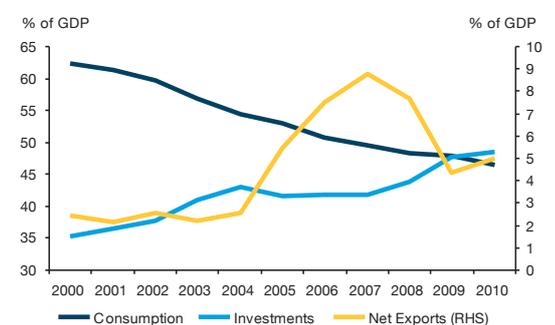


Source: CEIC; ANZ Economics

Chinese commercial banks issued, on average, loans of CNY8.5trn in 2009 and 2010, compared with an average level of CNY3trn in 2000-2008. The loan growth has led not only to higher inflation, but may also increase credit risk for banks in the coming years.

In addition to low lending rates, the investment-led stimulus package has created structural issues. The package included extension of financial facilities to numerous infrastructure projects. As a result, the weight of investment to total GDP increased further, while the share of consumption trended down. By sector, heavy industry's share in total industrial output increased to 70%, suggesting that this sector has led China's economic recovery but will also continue to place strains on global commodity prices. This pattern of growth obviously cannot be sustained.

**FIGURE 6. CHINA'S ECONOMIC STRUCTURE**



Source: CEIC; ANZ Economics

## THE INTERNATIONALISATION OF THE RMB

A shift in RMB management is one tool the government can use to address these imbalances. Allowing appreciation of the USD/RMB exchange rate, as began in June 2010, may help to reduce the trade surplus and thereby slow reserve accumulation.

However, in order to offset the impact of large capital inflows, the authorities have also started to promote the use of RMB as an invoicing currency for international trade, starting with the bilateral trade with Hong Kong. Accompanied with this move, the RMB's use in financial transaction in Hong Kong was sharply liberalised in July 2010. Given the fundamental drivers, the continued liberalisation of the RMB is likely to continue to evolve over the coming years.

# THE RMB

## BRIEF HISTORY OF THE RENMINBI (RMB)

### A STORY OF LIBERALISATION

#### PRE-REFORM PERIOD (1948-1977)

The People's Bank of China (PBoC) was established on 1 Dec 1948. Soon after, it issued the renminbi, the people's money (commonly known as the yuan), as the official currency of the People's Republic of China. In its early years, the renminbi (RMB) was linked to internal and external price indices. At the time, China's prices were extremely volatile, leading to frequent adjustments of the RMB exchange rate.

From 1953 to 1978, under China's planned economy, the exchange rate was relatively stable. The PBoC enforced a strict exchange rate policy of keeping the RMB artificially overvalued so as to discourage international trade, foreign debt and investment.

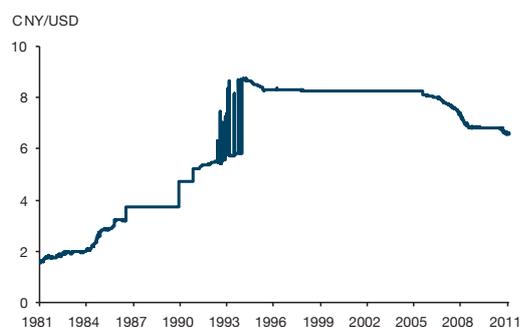
In 1973, the currency was de-linked from the US dollar and pegged to a basket of currencies.

#### REFORM PERIOD (1978-1994)

In 1978, as China started to open up its economy, the State Administration of Foreign Exchange (SAFE) was established and authorised to manage the country's foreign exchange reserves. As the overvalued RMB was hurting the development of China's external trade, from 1979 to 1984 the RMB exchange rate embarked on a dual track rate regime of an official rate and an international trade-related rate. The official exchange rate remained at around 1.5 yuan per US dollar, while the trade-related settlements enjoyed a more attractive, market-determined rate of around 2.8 yuan per US dollar. The dual track system was used until the end of 1984, when the exchange rate was again unified at 2.8 yuan per US dollar.

The RMB exchange rate was adjusted frequently until it hit 5.22 yuan per US dollar on 17 Nov 1990. In 1988 the dual track system was re-introduced with a swap rate system replacing the trade-related settlement rate. The swap rate, driven by market supply and demand for foreign exchange, depreciated slowly to 8.72 yuan per US dollar by the end of 1993.

FIGURE 1. SPOT RMB RATE

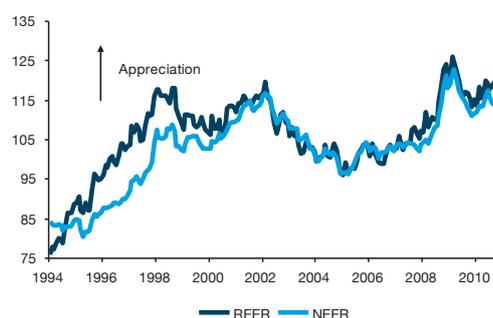


Source: Bloomberg

In 1994, the dual track system was replaced by a unified rate that was pegged to the US dollar at 8.26 yuan, resulting in a one-off sizable depreciation of the official rate. This led to China later being accused of planting the seeds for the 1997 Asian Financial Crisis.

However, empirical evidence suggests that China's foreign trade at that time—using the swap rate of 8.3 yuan per US dollar—had already accounted for nearly 80% of the total currency exchanged. Moreover, following the unification of the exchange rate—a multilateral exchange rate calculated on a trade-weighted basis and adjusted for inflation—appreciated sharply, largely owing to China's relatively high inflation when compared with its trading partners.

FIGURE 2. TRADE-WEIGHTED EXCHANGE RATE  
2005=100



Source: Bloomberg

# THE RMB

**TABLE 1: EVOLUTION OF THE RMB**

PERIOD	EXCHANGE RATE POLICY TARGET	FOREIGN TRADE REGIME	CHARACTERISTICS OF RMB EXCHANGE RATE	
Pre-reform	1949-1952	Encourages exports and remittances to China	Predominantly private companies	<ul style="list-style-type: none"> <li>- Linked to internal and external price indices</li> <li>- Changed frequently</li> </ul>
	1953-1972	Long term stability and balance the foreign exchange receipts and expenses	State-owned specialised foreign-trade corporations	<ul style="list-style-type: none"> <li>- Pegged to USD</li> <li>- Non-trade payment on agreement rate of exchange with former Soviet Union and others</li> <li>- Mostly undervalued</li> <li>- From 1968, used RMB for quoting prices and settling accounts</li> </ul>
	1973-1978	Keep the RMB strong and maintain balance of exchange income and expense	State-owned specialised foreign-trade corporations	<ul style="list-style-type: none"> <li>- RMB pegged to a basket of currencies</li> <li>- Mostly undervalued</li> <li>- Changed frequently</li> </ul>
1st reform period (1978-1994)	1979-1984	Encourage exports and limit imports	Responsibility system of operation on contracting base in foreign trade sector	<ul style="list-style-type: none"> <li>- RMB pegged to a basket of currencies</li> <li>- Dual exchange rate regime (internal settlement rate)</li> <li>- Mainly focused on the rate of earning exchange in terms of exports of products</li> </ul>
	1985-1993	Encourage exports and limit imports	Encourage Foreign Direct Investment and domestic export competition	<ul style="list-style-type: none"> <li>- Dual exchange rate regime (swap exchange rate)</li> <li>- Mainly focused to the rate of earning exchange in terms of exports of products</li> </ul>
2nd Reform Period (1995-2010)	1994-2004	Maintain stability of the exchange rate and to serve economic growth	Free competition	<ul style="list-style-type: none"> <li>- Single conventional pegged exchange rate regime</li> <li>- Stable and appreciating steadily</li> </ul>
	2005-2010	Improve the mechanism of the exchange rate based on market supply and demand	Free competition	<ul style="list-style-type: none"> <li>- Managed float exchange rate regime</li> <li>- Appreciated substantively</li> </ul>
	Beyond 2010	Increase flexibility of the exchange rate system and effectiveness of monetary policy	Free competition	<ul style="list-style-type: none"> <li>- From managed float exchange rate regime to more flexibility of exchange rate regime</li> </ul>

# THE RMB

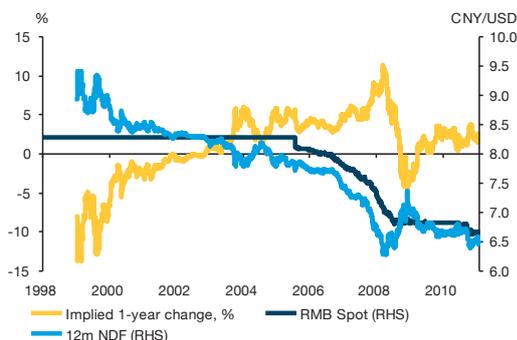
The USD/RMB 8.26 rate was maintained until 2005. In July 2005, the authorities announced a one-step revaluation of the USD/RMB exchange rate of just over 2%, and also announced the RMB would once again be managed against a basket of currencies. From mid-2005 until the start of the global financial crisis in September 2008, the USD/RMB exchange rate appreciated by nearly 20% in nominal terms. The exchange rate then held steady against a falling USD from late 2008 through mid-2010, at which point a gradual pace of appreciation resumed.

## RMB EXCHANGE RATE CONTROVERSY

China's exchange rate policy has been a point of significant international discussion. Some argue that an undervalued RMB combined with government subsidies delivers an unfair advantage to Chinese enterprises. With the rapid rise of its export sector, China's trade surplus has jumped sharply from around 1.7% of GDP in 2004 to a peak of almost 8% of GDP in 2007.

However, readers should note that while China is a net exporter to the EU and the US, it also runs a large trade deficit with Asia's larger economies such as Japan, Taiwan and South Korea. In addition, China's large trade surplus can be sourced to its processing trade sector, which imports and assembles intermediary products, using Chinese labour, for re-export. Meanwhile, China's ordinary trade is mostly balanced or run at a small surplus.

**FIGURE 3. MARKET VALUATION OF RMB EXCHANGE RATE**



Source: Bloomberg; ANZ Economics

Regardless of the underlying causes of China's trade surplus, trade tensions with the rest of the world have been rising. Between 1995 and 2009, China was the greatest recipient of anti-dumping complaints to the World Trade Organisation. Among emerging economies, India led the charge, while the EU and the US led the advanced economies.

## RMB DOMESTIC TENSIONS

The RMB exchange rate regime has also created tensions on the home front. As the Chinese economy rebounds from the global financial crisis of 2008, it runs the risk of overheating. The extraordinarily loose monetary and fiscal policies of the last two years – during the time the RMB has held steady against a weak USD and thereby depreciated versus the EUR – have resulted in rising inflation and the increasing risk of a property bubble.

At the same time, the slow recovery of the US has led the Federal Reserve to undertake quantitative easing (QE), creating more relaxed monetary conditions and generating inflation expectations. The second round of QE, announced in Nov 2010, is expected to keep US dollar yields low and extend the weakness of the US dollar in the coming months.

Historically, a weak US dollar is associated with high commodity prices. The US dollar has had three periods of marked depreciation (1973 to 1979, 1985 to 1995, and 2002 to present day) which coincided with rising global commodity prices. As a weaker US dollar pushes global commodity prices higher, China will continue to import inflation, as Japan did in 1974 and 1975 when its inflation soared to 25% despite the yen appreciating by 50% from 1972 to 1978.

Supporters of a stronger RMB point out that a stronger currency would be conducive to China's structural change in the medium term by encouraging growth in consumption at the expense of exports and investment. As China has fully recovered from the crisis, policy makers may be willing to address structural imbalances. Not only would a stronger currency help boost domestic consumption, it would also help contain imported inflation. With rising political pressures and domestic imperatives to prevent imported inflation, we believe the RMB will appreciate at a faster pace in the coming months.

## RECENT RMB REFORM: REFERENCING A BASKET?

On 19 June 2010, the PBoC announced that it would relinquish the RMB's 23-month peg to the US dollar, while maintaining the existing trading band at +/-0.5%. Since then, the RMB has been allowed to appreciate gradually.

# THE RMB

Notably, the correlation between the RMB spot rate and a basket of major traded currencies (EUR, JPY, AUD and GBP) has been rising significantly. Our analysis shows that the correlation coefficient between the RMB and the currency basket was limited during the first two months following the de-pegging, suggesting that the RMB spot rate has little correlation with the currency basket. However, the correlation coefficient between the RMB spot rate and currency basket has grown stronger since September, indicating that the PBoC is allowing the RMB to be traded on market conditions. This provides a good reference for forecasting the RMB exchange rate going forward.

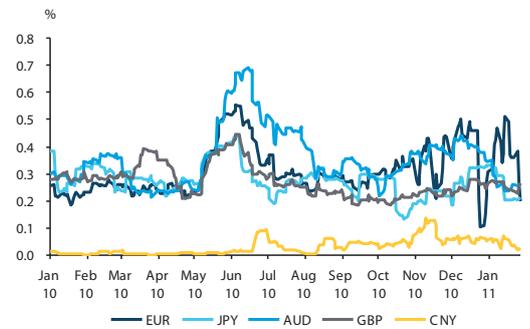
**FIGURE 4. RMB VS BASKET**



Source: Bloomberg; ANZ Economics

The current state of financial sector sophistication and capital account liberalization suggest that pegging to a currency basket is still the second best choice as it provides a reliable reference for both the market and the monetary authorities. This mechanism also brings higher transparency and removes the suspicion of currency manipulation. At the same time, the RMB trading band will need to be progressively enlarged to allow more daily volatility, in order to break the one way bet on RMB appreciation.

**FIGURE 5. RMB VOLATILITY VS BASKET**



Source: Bloomberg; ANZ Economics

# OFFSHORE RMB MARKET – HONG KONG

## OFFSHORE USE OF THE RMB

### RMB TRADE OPENS IN HONG KONG

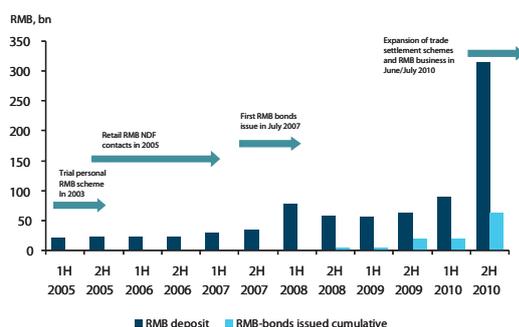
In July 2010, the “people’s money” was allowed much greater flexibility to travel outside China on deliverable basis, and Hong Kong, with its sophisticated financial infrastructure, was its clearly endorsed destination.

Hong Kong’s banks have conducted personal RMB business since 2004, including deposit-taking and remittances. Now, with the relevant monetary authority agreements in place, the offshore RMB business (also known as CNH business) has made a quantum leap.

Last year, Hong Kong’s total RMB deposits recorded over a three-folded increase and the number of mainland enterprises eligible for the cross-border RMB trade settlement scheme rose to 67,000.

This chapter reviews the development of RMB business in Hong Kong and its prospects.

FIGURE 1. RMB IN HONG KONG



Source: Bloomberg; ANZ Economics

### JOURNEY TO OFFSHORE

For its first 62 years, circulation of the “people’s money” was limited to within mainland China because of tight capital controls. Even after China’s economy started to open in 1978, the currency was not widely used outside China as the authorities maintained strong control of capital flow (see Table 1 in previous chapter).

While China liberalised foreign direct investment in the early 1980s and all trade related transactions in 1996, capital controls on financial flows were prohibited. In recent years, financial flows have been liberalised with the introduction of the Qualified Foreign Institutional Investor scheme (QFII) and the Qualified Domestic Institutional Investor scheme (QDII). As Chinese citizens started to travel abroad in greater numbers, the RMB has increasingly become used in the retail settings, especially in Hong Kong.

### 2004 - 2009

In late 2003, the PBoC agreed to provide clearing arrangements for banks in Hong Kong to conduct personal RMB business on a trial basis. This trial was limited to four areas:

1. Deposit-taking
2. Exchange between the Hong Kong dollar and the RMB
3. One way remittances to corresponding accounts on the Mainland, and
4. Renminbi debit and credit card issuance

Under the trial, Hong Kong banks placed RMB funds absorbed from their depositors with a designated RMB clearing bank in Hong Kong (the Bank of China(Hong Kong Limited)). The clearing bank in turn deposited all RMB funds absorbed from its own depositors and other participating banks with the PBoC Shenzhen Sub-Branch. A clearing agreement signed between the PBoC and the clearing bank, and in turn by the clearing bank with banks participating in the scheme, set out the scope of the business.

In November 2005, the trial RMB deposit scheme was extended to business. Merchants engaging in personal tourism or consumer services were allowed to open RMB deposit accounts and conduct a one-way exchange of their RMB deposits into HKD. At the same time, Hong Kong residents could open a RMB current account and make payment, by cheque, for consumer spending in Guangdong Province, subject to a daily limit of RMB80,000 per account. RMB remittances by Hong Kong personal depositors to savings accounts on the mainland increased to RMB80,000. Credit limits of RMB credit cards were also lifted.

November 2005 marked another significant development with the launch of RMB non-deliverable forward contracts (NDF) in five tenors: 1, 2, 3, 6, and 12 months with a minimum contract size of US\$10,000. As a result, small and medium enterprises, or individuals, were allowed to lock in an RMB/USD exchange rate prior to their actual date of transaction. Since NDFs were transacted on a market basis, its rate has been regarded as a market expectation of future RMB movement. Physical deliveries of RMB in the forward market were still prohibited.

Finally, in 2007, the first RMB-denominated bonds were issued in the Hong Kong market.

# OFFSHORE RMB MARKET – HONG KONG

## 2009 ONWARD

The introduction of the RMB trade settlement scheme in 2009 was a significant milestone that expanded the scope of business conducted by banks to include a much wider range of RMB services to corporates.

In 2010, following the expansion of the RMB trade settlement scheme, the Hong Kong Monetary Authority (HKMA) and the PBoC agreed to strengthen their co-operation and further promote Hong Kong's status and role as a RMB market platform.

In June 2010, the cross-border RMB trade settlement scheme was expanded from trade transactions between five mainland cities and ASEAN economies to 20 mainland cities and provinces and the rest of the world. In July, another significant step was taken with the amendment of the clearing agreement to extend the ability of Hong Kong's banks to lend RMB loans and raise RMB bonds.

Financial institutions are now eager to develop and distribute RMB-denominated financial and derivative products in addition to their usual RMB banking business. A slew of RMB-denominated financial products, including time deposit schemes, savings insurance, foreign exchange-linked deposits and interest rate-linked deposits, have been quickly developed.

The trade settlement scheme has increased the circulation of the RMB in Hong Kong, reflected by the increase in Hong Kong-held RMB deposits. In December 2010, RMB deposits reached RMB310bn (US\$48bn), compared with just RMB60bn from the year before (See Figure 1). Cross-border trade settlement witnessed a 10-fold increase to RMB101bn (US\$15bn) per month in December 2010, compared with RMB10bn the previous June. The increase in RMB liquidity in Hong Kong has strengthened the city's role as a world leading offshore RMB financial centre.

## KEY POINTS OF THE RMB AGREEMENT

Restrictions on RMB business transactions in Hong Kong were relaxed with the July 2010 amendment to the 2009 RMB clearing agreement between the PBoC and participating banks. The amendment allowed Hong Kong-based banks, securities companies and asset management firms to sell RMB-denominated financial products. Key points of the agreement include:

**Deposit taking** - Participating authorised institutions (AI's) are now able to open RMB deposit accounts for any enterprise (instead of the previously designated seven industrial sectors). Also, there are no restrictions on the offer of RMB-denominated financial products.

**Currency conversion** - There is no upper limit on conversion services provided to enterprises if neither AIs have to square the corresponding open position with the clearing bank, nor do they need to square such open position with other participating AIs, suggesting that banks can use their own RMB deposits to satisfy enterprises' RMB conversion needs.

**Remittance to and from the mainland** - It is no longer necessary for Hong Kong AIs to undertake background checks with respect to whether the remitter or recipient on the mainland is in compliance with mainland rules and requirements.

**Interbank transfers, use of cheques and cash withdrawals** - There is no restriction on the transfer of RMB funds between different customers, whether within the same AI or not. The same goes for cash deposits and withdrawals from RMB-deposit accounts of corporate customers. However, participating AIs must exercise caution when handling cash transactions.

**RMB loans** - There is no restriction on the type of corporations that can be granted an RMB loan or on the type of RMB loans that can be extended to a corporate customer. Separately, conversion of RMB for the repayment of trade finance can be conducted, and the associated open position can be squared with the clearing bank.

**RMB bonds** - Any customer with an RMB deposit account maintained with a participating AI can invest in RMB bonds issued in Hong Kong. AIs can issue a RMB certificate of deposit (CDs) in Hong Kong. Meanwhile, there is no restriction on remittance of proceeds raised from a RMB bond issuance of proceeds raised from a RMB bond issuance in Hong Kong to the mainland. These proceeds can be converted into another currency without any restrictions.

# OFFSHORE RMB MARKET – HONG KONG

## WHY HONG KONG?

There is a strong business case for China to develop an offshore RMB centre in Hong Kong.

Offshore RMB circulation meets the interests of China's monetary policy. By December 2010, China's foreign exchange reserves reached US\$2.8trn, suggesting that the internationalisation of the RMB may provide a buffer and reduce pressures on China's monetary conditions from continuous capital inflows. Opening up the RMB market may reduce the need for PBoC to "sterilise" capital inflows, a commonly used term describing the need for central bank to absorb excess liquidity.

The offshore centre in Hong Kong will also facilitate trade flows in the Greater China region. Hong Kong's position as the designated offshore RMB centre reflects its role in cross-strait RMB clearing. At present, the RMB and the Taiwan dollar (TWD) carry no official status in their counterpart jurisdiction. For several decades, Hong Kong was the gateway for cross Strait trade and visitor exchanges and is now taking one step forward in terms of fund flows.<sup>1</sup>

The risk of developing an offshore RMB centre within the national border, HKSAR inclusive, is rather low. Firstly, there is a close, cooperative relationship between the PBoC and the HKMA. Secondly, the large size of China's economy should allow a buffer as expanded market forces are slowly introduced.

## WHAT CONSTITUTES THE HONG KONG OFFSHORE RMB MARKET?

The upshot of these changes is that new offshore RMB market, sometimes referred to as the CNH, has been developing rapidly. Apart from the trading of RMB for trade-related purposes, there has been an increasing volume of transactions done in the interbank market for non-trade settlement purposes. Currently the interbank CNH rate is generally quoted stronger than the clearing bank's rate. Banks may also quote the "offshore rate" for trade settlement purposes.

Although there is no official data as yet on market turnover, it is believed that transaction volumes in both markets have expanded rapidly.

<sup>1</sup> According to the Cross-strait Financial Cooperation Agreement signed in 2009, the exchange, supply and repatriation of RMB and TWD will be conducted through suitable means with commercial banks as intermediaries. In July 2010, it was announced that these operations of RMB cashnotes with Taiwan is to be conducted in Hong Kong. Under the arrangement, the renminbi clearing bank in Hong Kong will provide RMB cashnote exchange and related services to the Hong Kong branches of eligible Taiwan commercial banks. In turn, the Taiwan head offices of such commercial banks will provide RMB cashnote exchange services to other authorised financial institutions in Taiwan, for the purpose of serving personal customers locally.

FIGURE 2. ONSHORE V OFFSHORE EXCHANGE RATES



Source: Bloomberg; ANZ Economics

When we compare the movement of USDCNY and USDCNH, the onshore versus the offshore market, the CNH exhibits a greater volatility than the onshore CNY rate (See Figure 2 and Figure 3). In the derivative market, the CNH one-year forward rate is quite similar to the onshore deliverable forward rate.

FIGURE 3. ONSHORE V OFFSHORE FORWARDS



Source: Bloomberg; ANZ Economics

At first glance, China's capital controls would appear to present a considerable obstacle to a flourishing RMB offshore market in Hong Kong. However, the current Hong Kong CNH market shares some similarities to the Eurodollar market of the late 1960s and early 1970s. Though US authorities had imposed capital controls, US banks were still able to settle offshore trade and investment transactions. Therefore, non-resident convertibility of the US dollar occurred, encouraging both long and short positions of the US dollar to be built up offshore.<sup>2</sup>

<sup>2</sup> See He and McCauley (2010), "Offshore Markets for the Domestic Currency: Monetary and Financial Stability Issues," BIS Working Papers, No 320.

# OFFSHORE RMB MARKET – HONG KONG

## RMB-DENOMINATED BONDS IN HONG KONG

From the list of new RMB products developed, RMB-denominated bonds, commonly known as “Dim Sum Bonds”, is perhaps one of the most significant.

By the end of 2010, 50 offshore RMB-denominated bonds had been issued in Hong Kong. A total of RMB35.7bn (US\$5.5bn) was raised. The average coupon in the offshore market is 1.53% (without any adjustment for credit rating), compared with about 4% for onshore state-owned enterprises. Issuance is expected to more than double in 2011. Entities who have raised bonds include:

- > Financial institutions such as commercial banks (e.g. ANZ, Bank of China)
- > Multinational corporations who demand for RMB currencies (e.g. MacDonald)
- > Policy-oriented banks or international organisations (e.g. World Bank, China Development Bank)
- > Hong Kong corporations with operations in China

Of particular interest are foreign corporations issuing RMB bonds. Given that onshore RMB yields are relatively high, there is greater incentive for financial institutions to repatriate the RMB to the onshore market. As RMB yields in the offshore market remain low, many financial institutions and companies are interested in issuing RMB-denominated bonds in Hong Kong as demonstrated by McDonald’s with its CNY200mn RMB-bond issuance in Sep 2010 and ANZ’s CNY200mn RMB-bond issuance in Dec 2010 (case study below). Note that the transaction costs remain high as each transaction under the capital account has to be approved by the Mainland on a case-by-case basis. A truly active offshore RMB bond market requires further efforts to facilitate the smooth repatriation of funds raised.

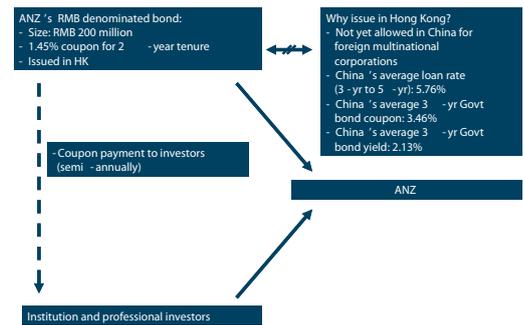
## OTHER POTENTIAL MARKETS

RMB-denominated equity listings

Hong Kong has one of the largest stock markets in the world. Naturally, the offshore RMB business will extend its reach to the equity market. The Hong Kong Exchanges and Clearing (HKEx) is studying the possibility of setting up a

RMB liquidity pool for investors interested in RMB-denominated IPO but do not have the currency. It is expected that there will be RMB-denominated IPO in Hong Kong this year.

FIGURE 4. CASE STUDY ANZ’S RMB BOND



Source: ANZSee Appendix A for a list of RMB bonds issued as of Jan 2010.

## PRIVATE AND COMMERCIAL BANKING

China is expected to gradually open its capital accounts, allowing Chinese citizens and enterprises to invest overseas. It is expected that this will further activate the offshore RMB banking business, including private banking. In January 2011, the PBoC announced a trial scheme that will allow enterprises operating in China to invest offshore using their RMB holdings. Yuan denominated IPO activities in the equity market are also expected in 2011.

Hong Kong has long been the prominent platform for the mainland’s outward direct investments. The mainland’s outward direct investments amounted to US\$55.9bn in 2008 and US\$56.5bn in 2009, of which 69% and 63%, respectively, was invested in Hong Kong or through Hong Kong to other parts of the world. On implementation of the Pilot Scheme, mainland enterprises were able to conduct such investments through Hong Kong’s offshore RMB centre, and at the same time make use of the multi-currency and multi-functional financial platform in Hong Kong for the related financing and fund management activities.

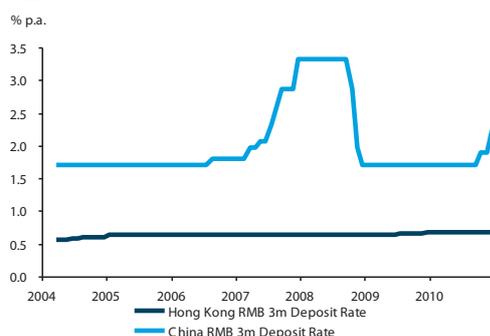
# THE FUTURE OF THE MARKET

## OUTLOOK: EXPECTATIONS OF THE FUTURE OFFSHORE RMB MARKET

### ECONOMIC DRIVERS

The CNH market is not bound by reserve requirements or a tax on the interest income on RMB deposits, which for banks makes the cost of holding and using the RMB cheap. The differentials in RMB deposit yield will also attract more RMB bond issuances and product development in Hong Kong in the near term, thus stimulating the development of the CNH market. We expect interest rate differentials to gradually diminish as Hong Kong's RMB market becomes more liquid and China's capital controls are progressively relaxed.

**FIGURE 1. ONSHORE AND OFFSHORE DEPOSIT RATE**



Source: Bloomberg

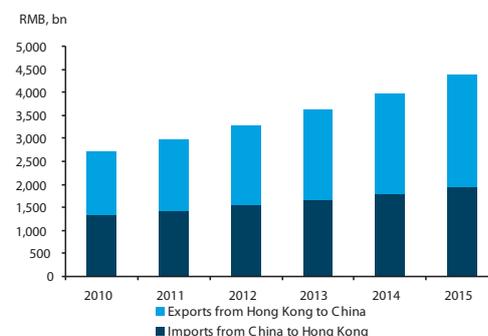
Looking ahead, the supply of RMB in Hong Kong will increase, and Hong Kong will become an international RMB business centre. There are five economic forces that will inject greater momentum for growth:

1. RMB carried by mainland visitors
2. Foreign / Hong Kong's residents' demand for RMB notes
3. International, intra-regional and cross-border trade financing
4. Inter-bank (including inter-HK-mainland banks) transactions
5. RMB-denominated bond and other security issuance.

### HOW BIG WILL IT BE?

By the end of 2010, total RMB deposit reached RMB315bn (US\$48 bn). Parallel to this development was a three-fold rise in trade settlement volume, in the first five months since expansion of trade settlement, to RMB340bn (US\$52bn). Trade settlement will still be the primary factor determining the size of supply of offshore RMB in Hong Kong. We do not expect one-off liberalisation of capital accounts in the near future.

**FIGURE 2. PROJECTED TRADE BETWEEN MAINLAND CHINA AND HONG KONG**



Source: ANZ Economics

As RMB is still an infant market in Hong Kong, the incredible growth rate of 2010 is unlikely to be repeated. However, it is not unreasonable to project that 50% of trade flow will be settled in RMB in coming years. By 2015, cross-border trade is forecast to reach RMB4.4trn (or US\$675bn using CNY/USD equal to 6.5). At that point, the volume of total RMB trade settlement business would hit RMB2.2trn.

The RMB-denominated bond market in Hong Kong is a different case, and has been driven by demand and regulation. We expect this market to continue its rapid growth.

China is expected to undergo a more aggressive form of liquidity tightening as part of its overall plan of macroeconomic management. It is likely to induce more corporations to look for bond issuance as an alternative funding source. In Jan 2011, about RMB20bn of the so-called synthetic RMB bonds had been issued. Assuming a constant rate, the total of this bond class could reach RMB240bn. A conservative projection could be a 3-fold increase to RMB750 by 2015 even with its popularity. By then, it is expected that half of this bond issuance will be generic

# THE FUTURE OF THE MARKET

RMB-bonds and the real RMB bond market will reach RMB375bn in five years.

Once the RMB reaches critical mass, we project that a large and liquid CNH market, possibly emulating the current eurodollar market, could be operating within five years. The RMB market has the potential to transform Hong Kong's economy in much the same way as China's trade opening and Foreign Direct Investment did in the early 1980s.

Hong Kong will be the leading offshore RMB market in the world. Hong Kong is ranked number three globally as an international financial centre, behind New York and London. The first-mover advantage with its sophisticated financial market and legal system will be conducive to financial innovation, providing a solid testing ground for RMB derivative products. Its geographic proximity and deep commercial ties to mainland China point to its pre-eminence in this market. Products popular in the offshore market could eventually be adopted in mainland China.

## OPPORTUNITIES?

The liberalization of RMB business in Hong Kong opens the door for individuals, Chinese and foreign business to access to a new range of cash management and investment opportunities.

In the short term, corporates are more able to identify opportunities in this new market. Since the offshore RMB interest rate is lower than that in onshore markets, a simple opportunity is to place RMB-denominated assets in mainland China, while holding the RMB-denominated liabilities in Hong Kong. Think about a multi-national corporate: its Hong Kong subsidiary is able to draw down RMB loans from the Hong Kong financial institutions, but the affiliate in mainland China repays its RMB loans to onshore banks. As a result, the MNC as a whole is better off.

For the individual investor, very strict capital account controls make transacting difficult. Investors will find it is almost impossible to take advantage of the interest spread, as they are not allowed transfer the offshore RMB onshore to enjoy the higher yields. That is also the reason why interest differentials persist between onshore and offshore RMB. Currently, with the PBoC's special approval, some offshore financial institutions can invest their RMB positions into the onshore inter-bank bond market.

Definitely, there are some technical problems involving, for example, the offshore banks which might not be able to provide large amounts of RMB loans. However, this should be one of the best ways to take advantage of cheaper funding costs in Hong Kong.

# RECENT DIM SUM BOND ISSUANCE

## APPENDIX A – RECENT OFFSHORE RMB BOND ISSUANCE

### RECENT DIM SUM BOND ISSUES

Issuer	Issue Date	Maturity	Coupon	Amount Issued (RMB mn)	Bid	Yield	S&P Rating	Moody's Rating
ROYAL BK SCOTLND	20/01/2011	20/01/2014	1.8000	100	-	-	A+e	Aa3e
INT BK RECON&DEV	14/01/2011	14/01/2013	0.9500	500	-	-	-	Aaa
BK OF COMM - HK	10/01/2011	10/01/2013	1.4000	500	-	-	-	-
ANZ BANKING HK	24/12/2010	24/12/2012	1.4500	200	-	-	-	-
AGR BK CHINA(HK)	23/12/2010	23/12/2011	1.2000	500	-	-	-	-
AGR BK CHINA(HK)	23/12/2010	24/12/2012	1.4000	500	-	-	-	-
CHINA POWER INT	23/12/2010	23/12/2015	3.2000	800	-	-	-	-
VTB CAPITAL SA	23/12/2010	23/12/2013	2.9500	1000	-	-	BBB	Baa 1e
CHINA GOVT BOND	20/12/2010	20/12/2012	1.6000	3000	100.27	1.4589	-	Aa3
GALAXY ENTERT GP	16/12/2010	16/12/2013	4.6250	1380	-	-	-	-
EXP-IMP BK CHINA	2/12/2010	2/12/2012	1.9500	1000	101.62	1.0740	-	-
EXP-IMP BK CHINA	2/12/2010	2/12/2013	2.6500	4000	101.35	2.1629	AA-	-
CATERPILLAR FINL	1/12/2010	1/12/2012	2.0000	1000	101.50	1.1902	A	A2
CHINA GOVT BOND	1/12/2010	1/12/2013	1.0000	2000	100.23	0.9205	AA-	Aa3
CHINA GOVT BOND	1/12/2010	1/12/2015	1.8000	2000	100.27	1.7407	AA-	Aa3
CHINA GOVT BOND	1/12/2010	1/12/2020	2.4800	1000	93.10	3.3044	AA-	Aa3
UBS AG HK	22/11/2010	22/11/2012	2.5000	200	-	-	-	-
CHINA MERCHANTS	19/11/2010	19/11/2013	2.9000	700	-	-	-	-
HONG & SHAN BANK	19/11/2010	19/05/2011	1.8000	90	-	-	-	-
CHINA RESOURCES	12/11/2010	12/11/2013	2.9000	1000	102.85	1.8581	BBB-	NR
CHINA RESOURCES	12/11/2010	12/11/2015	3.7500	1000	104.35	2.7791	BBB-	NR
CHINA DEV BANK	11/11/2010	11/11/2013	2.7000	3000	103.88	1.2954	AA-	-
SINOTRUK HK LTD	29/10/2010	29/10/2012	2.9500	2700	100.92	2.4157	-	-
ICBC ASIA	22/10/2010	22/10/2012	2.3000	117.12	-	-	-	-
ICBC ASIA	22/10/2010	22/10/2013	2.6500	47.1	-	-	-	-
ASIAN DEV BANK	21/10/2010	21/10/2020	2.8500	1200	-	-	AAA	Aaa
CHINA DEV BANK	14/10/2010	14/10/2013	4.4367	2000	-	-	-	-
BANK OF CHINA	30/09/2010	30/09/2012	2.6500	2200	102.05	1.4235	A-	-
BANK OF CHINA	30/09/2010	30/09/2013	2.9000	2800	104.25	1.2951	A-	-
DEUTSCHE BANK AG	28/09/2010	28/09/2012	2.0000	200	-	-	-	-
BK TOKYO-MIT UFJ	24/09/2010	26/09/2011	1.9800	20	-	-	-	-
ICBC ASIA	24/09/2010	24/09/2012	2.2500	1000	-	-	-	-
ICBC ASIA	24/09/2010	24/09/2012	2.2500	1000	-	-	-	-
MCDONALD'S CORP	16/09/2010	16/09/2013	3.0000	200	-	-	A	A2
CHINA DEVELOP BK	13/09/2010	13/09/2012	2.1000	1000	-	-	-	-
CHINA DEVELOP BK	13/09/2010	13/09/2012	2.1000	500	101.75	1.0347	-	-
CHINA DEVELOP BK	10/09/2010	12/09/2011	1.9500	100	-	-	-	-
HONG & SHAN BANK	17/08/2010	17/02/2011	2.0000	114.45	-	-	-	-
CITIC BANK INTL	20/07/2010	20/07/2011	2.6800	500	-	-	-	-
HOPEWELL HIGHWAY	13/07/2010	13/07/2012	2.9800	1380	-	-	-	-
CHINA GOVT BOND	27/10/2009	27/10/2011	2.2500	3000	100.78	1.2308	-	Aa3
CHINA GOVT BOND	27/10/2009	27/10/2012	2.7000	2500	102.91	1.0478	-	Aa3
CHINA GOVT BOND	27/10/2009	27/10/2014	3.3000	500	106.95	1.4038	-	Aa3
HSBC BANK CHINA	14/09/2009	14/09/2011	2.6000	2000	100.75	1.4478	-	-
CHINA DEV BANK	20/08/2009	20/08/2011	3.1996	1000	-	-	-	-
CHINA DEV BANK	20/08/2009	22/08/2011	2.4500	2000	100.54	1.5244	AA-	-
BEA CHINA LTD	23/07/2009	23/07/2011	2.8000	4000	100.72	1.3971	A-	-
HSBC BANK CHINA	13/07/2009	13/07/2011	4.5751	1000	-	-	-	-
BANK OF CHINA	22/09/2008	22/09/2011	3.4000	1000	-	-	A-	-
EXP-IMP BK CHINA	4/09/2008	4/09/2011	3.4000	3000	100.75	2.1973	-	-

Source: Bloomberg

## FREQUENTLY ASKED QUESTIONS

### THE BASICS OF RMB IN MAINLAND CHINA

- Q. What is the international currency symbol for RMB?*
- A. CNY is a generic term referencing the unit of currency. Historically it was used to describe the currency irrespective of jurisdiction and market. Note: CNY is still the only ISO code for RMB.
- Q. How are onshore RMB exchange rates determined?*
- A. The par rates are fixed daily at 9:15am in the inter-bank foreign exchange market in Shanghai. Daily trading band is +/- 0.5 percent from the par value.
- Q. Is there an inter-bank money market for RMB?*
- A. Yes. Participating banks must be licensed first by the regulators. Some non-bank financial institutions have been licensed to participate in the market.
- Q. Who can trade RMB?*
- A. Only licensed institutions; one party must be a designated foreign-currency bank.
- Q. Who can trade RMB currency forwards and swaps?*
- A. Only licensed institutions. Supporting documents are required for corporate hedging needs.
- Q. Are Forward Rate Agreements available?*
- A. Yes, in the inter-bank market.
- Q. Are Interest Rate Swaps available?*
- A. Yes. The market is liquid with tenor going out to 10 years.
- Q. Are Interest Rate Options available?*
- A. No. Neither is it available offshore.
- Q. Are cross-currency swaps available?*
- A. Yes, in the inter-bank market.
- Q. What is a NDF?*
- A: Non-Deliverable Forwards. It is only available offshore. Daily fixing is at 9:15am Hong Kong time.
- Q. What is a NDO?*
- A: Non-Deliverable Options. It is only available offshore. Daily fixing is at 9:15 Hong Kong time.

### CROSS-BORDER TRADE SETTLEMENT IN RMB

- Q. What is cross-border trade settlement in RMB?*
- A. Since July 2009, the Chinese government started to promote use of RMB for settlement of cross-border trade.
- Q. What is the scope of trade that is eligible for RMB settlement?*
- A. All current account transactions.
- Q. Is there any limitation on trade destinations that are eligible for RMB settlement?*
- A. No, as long as one leg of the trade touches mainland China.
- Q. Who are the eligible parties for cross-border trade settlement in RMB?*
- A. Any importers in the 20 pilot provinces and cities (e.g. Beijing's not a province). These importers can issue RMB letter of credit (LC), remit RMB to any overseas exporter. A list of eligible exporters is maintained by the government, aka Mainland Designated Enterprises (MDEs). These exporters can receive RMB LC and RMB remittances from any overseas importer.
- Q. Where are the 20 pilot provinces and cities?*
- A. Shanghai, Beijing, Tianjin, Inner-Mongolia, Liaoning, Jilin, Heilongjiang, Jiangsu, Zhejiang, Fujian, Shandong, Hubei, Guangxi, Hainan, Chongqing, Sichuan, Yunnan, Tibet, Xinjiang and Guangdong.
- Q. What is a RMB Non-resident Account (NRA)?*
- A. Any offshore company that has trading needs with China can open non-resident account(s) with an onshore bank approved by the PBoC.
- Q. What is an onshore RMB cross-border settlement bank?*
- A. Any onshore bank approved by the PBoC. On the import side, it can issue RMB LC, and remit RMB for import clients. On the export side, it can handle RMB export LC including settlement and discounting, and receive RMB remittance for export clients.
- Q. What is a RMB cross-border agent bank?*
- A. Onshore, it is any bank approved by the PBoC. Offshore: Bank of China (Hong Kong) (BOC HK) and Bank of China Macau Branch.

# FAQS

Q. *What is an overseas RMB participating bank?*

A. Any overseas bank which has a settlement arrangement with a RMB agent bank. Through their agent bank, these banks can issue RMB LC, remit RMB cross-border for their overseas import clients, as well as discount/settle RMB LC, receive RMB remittance for their overseas export clients.

Q. *Can RMB funding be obtained from the HKMA?*

A. It is possible. Participating Authorised Institutions (PAIs) that do not have long RMB trade positions and cannot obtain RMB from the RMB Clearing Bank to meet customers' demand can approach the HKMA for RMB funding.

Q. *What is the HKMA's source of RMB funding?*

A. It is through the activation of the RMB Currency Swap Arrangement with the PBoC.

Q. *What is the size of the HKMA-PBoC Currency Swap Arrangement?*

A. CNY200bn.

Q. *How many accounts have been opened for cross-border trade settlement in HK?*

A. There were around 110,000 accounts (as at January, 2011) from about 15,000 in June 2010.

Q. *What is the value of cross-border trade settlements?*

A. Cross-border trade settlements amounted to around RMB500bn in 2010.

Q. *What are Participating Authorized Institutions?*

A. Authorised Institutions (AIs) authorised by the HKMA to conduct in deposit-taking business that are participating in the business of cross-border trade settlement in RMB.

Q. *What is a RMB clearing bank?*

A. A RMB clearing bank is an offshore bank that can obtain RMB funding from the PBoC to square the net RMB positions of other participating banks arising from cross-border trade settlement. Currently, only Bank of China (HK) and Bank of China (Macao) are the RMB clearing banks.

## RMB BUSINESS IN HONG KONG

### TRADING OF RMB

Q. *Is RMB traded in HK?*

A. Yes.

### DEPOSIT-TAKING, INTER-BANK TRANSFER AND WITHDRAWAL

Q. *What is the size of RMB deposit in HK?*

A. Total RMB deposits stood at RMB315bn as of December 2010. This is about 5 percent of HK's total bank deposit or 0.4 percent of total RMB deposits on the mainland China.

Q. *Can PAIs open RMB deposit accounts for any corporate customers?*

A. Yes.

Q. *Can RMB-denominated investment products be offered to customers?*

A. Yes.

Q. *Can non-AI financial institutions open RMB accounts with PAIs to facilitate their offering of RMB-denominated investment products to customers?*

A. Yes.

Q. *Can PAIs issue RMB certificate of deposits in Hong Kong?*

A. Yes. However, the HKMA expects PAIs not to place an over-reliance on a single source of wholesale RMB funding if the PAI does not have a retail deposit base.

Q. *Can RMB funds be transferred from the account of one corporate customer to another corporate or personal customer, and vice versa?*

A. There is no restriction on the transfer of RMB funds (including cheque payment in Hong Kong) between types of customers, whether within the same AI or not.

Q. *Are RMB cash deposits and withdrawals allowed for RMB deposit accounts of corporate customers?*

A. There is no particular restriction on cash deposits and withdrawals for RMB deposit accounts of corporate customers, but Participating AIs should exercise caution when handling cash transactions. It should be satisfied that such cash deposits or withdrawals are reasonable in the context of the customer's ordinary course of business in Hong Kong. There should also be monitoring procedures to guard against potential money-laundering activities.

Q. *What is the limit on RMB cash withdrawal?*

A. Up to RMB20,000 per transaction per person in banknotes for walk-in personal customers.

## CURRENCY CONVERSION AND REMITTANCE

Q. *What are the requirements for conducting RMB conversion for corporate customers?*

A. There is no restriction on conversion services provided to corporate customers if PAIs do not square the corresponding open position with the Clearing Bank, or if they seek to square such open position with other Participating AIs. The open position resulting from the conversion services provided for corporate customers for the following purposes can be squared with the RMB Clearing Bank:

- > cross-border trade settlement up to the amount of the relevant trade transactions settled or to be settled in RMB;
- > RMB trade finance in relation to cross-border trade transactions where customers do not have sufficient RMB for loan repayments;
- > settling expenses relating to RMB bond issuance in Hong Kong by mainland financial institutions as approved by relevant mainland authorities; or
- > transactions allowed by mainland authorities to be ultimately squared by the RMB Clearing Bank in the China Foreign Exchange Trading Centre.

Q. *What is the limit of RMB conversion for personal customers and Designated Business Customers (DBC)?*

A. The existing permitted conversions in relation to personal (and DBC) business are (i) up to RMB20,000 for personal customers per person per day; (ii) one-way conversion from RMB to other currencies for DBCs.

Q. *If a corporate customer receives RMB funds from the mainland that are not related to cross-border trade transactions, can such RMB funds be converted into another currency?*

A. For RMB funds not related to cross-border trade and are remitted from the mainland, there is no restriction with respect to the provision of conversion services by PAIs if they do not square the corresponding open position with the Clearing Bank, or if they seek to square such open position with other PAIs.

Q. *Is there a limitation on the timing difference between the RMB conversion and the trade settlement?*

A. No. However, if the resulting position from RMB conversion is to be squared with the RMB Clearing Bank, PAIs should only provide trade-related RMB conversion services in relation to transactions due for settlement not more than three months from the date of conversion.

Q. *Can RMB funds unrelated to cross-border trade settlement be remitted to and from the mainland?*

A. Yes, but subject to rules and regulations in the mainland China. This type of transaction has been part of usual banking practices in Hong Kong and properly regulated by established policies and procedures including those to guard against potential money laundering activities.

Q. *Is there any limitation on RMB remittances?*

A. Yes, a daily limit of CNY80,000 for personal customers.

## RMB LOANS

Q. *Can AIs extend RMB loans to corporate customers?*

A. Yes. However, RMB lending to DBCs is not permissible for the time being.

# FAQS

Q. *Is there any restriction on the type of RMB loans that can be extended?*

A. There is no restriction on the type of RMB loans that can be extended to a corporate customer.

Q. *Can Als extend RMB loans to personal customers?*

A. No.

Q. *Can the conversion of the RMB be conducted for the repayment of RMB trade finance or other loans extended to corporate customers?*

A. Conversion of the RMB for the repayment of trade finance can be conducted and the associated open position can be squared with the Clearing Bank. For other types of loans extended to corporate customers, there is no restriction on conversion services if the PAIs do not square the corresponding open position with the Clearing Bank, or if they seek to square the position with other PAIs.

Q. *Can RMB deposits be used as collateral for loans extended in RMB or other currencies?*

A. Yes. However, RMB lending to personal customers and DBCs is not permissible for the time being.

## **RMB BONDS**

Q. *What is a offshore RMB bond?*

A. It is a bond denominated in RMB and issued in HK.

Q. *How many RMB Bonds have been issued in Hong Kong?*

A. As of January 20, 2011, a total of CNY66.3bn for 53 offshore RMB bond have been issued since April 2008, according to data from Bloomberg. In 2010, CNY41.4bn was raised at an average coupon rate of 2.59%, compared to the 4% mainland onshore average coupon rate.

Q. *Who can invest in offshore RMB Bonds?*

A. Any customer with an RMB deposit account maintained with a HK PAI.

Q. *Can proceeds raised from a offshore RMB Bond issuance by a corporate customer be converted into another currency?*

A. There is no restriction on conversion if the PAIs do not square the corresponding open position with the Clearing Bank, or if they seek to square the open position with other PAIs.

Q. *Can proceeds raised from a Offshore RMB Bond issuance by a corporate customer be remitted to the mainland?*

A. There is no restriction on remittance of proceeds raised from a RMB bond issuance in Hong Kong to the mainland, although the issuer will need to obtain any necessary approval from the relevant mainland authorities.

Q. *What is a Panda bond?*

A. It is a bond denominated in RMB and issued in mainland China by an offshore issuer. Thus far, this market has been restricted to supra-national issuers.

Q. *Can locally incorporated foreign companies issue RMB bonds in mainland China?*

A. Yes, to date access has been granted to selected locally incorporated banks.

Q. *How many Panda bonds have been issued?*

A. To date, only Bank of Tokyo-Mitsubishi UFJ, International Finance Corp (IFC) and the Asian Development Bank (ADB) have issued Panda bonds.

Q. *Can foreign companies invest in the bond market in mainland China?*

A. On August 10, 2010, the PBoC announced that RMB clearing banks, foreign central banks, and other eligible foreign institutions are able to apply for a quota to use their RMB funds to invest in the mainland's inter-bank bond market.

## **RMB EQUITIES**

Q. *Are RMB-denominated stocks available?*

A. Not yet, although a plan by the Hong Kong Exchange and Clearing is in the works.

## **RMB BUSINESS OUTSIDE CHINA**

Q. *Is RMB trading available outside China?*

A. Bank of China offers spot and NDF trading of RMB in New York and Los Angeles subject limits: for individuals, the daily limit is USD4,000 worth of RMB, and the annual limit is USD20,000 worth of RMB; international trading business customers can also trade the RMB.

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