

Legislative Council Panel on Financial Affairs

Proposal to Raise the Maximum Amount of Borrowings under the Government Bond Programme

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GBP with maximum amount of borrowings of HK\$100 Billion

- Proposed in the 2009-10 Budget to implement the Government Bond Programme (“GBP”) to promote the sustainable development of the bond market
- Legislative Council passed in July 2009 -
 - Resolution under the Public Finance Ordinance authorising the Administration to set up the Bond Fund
 - Resolution under the Loans Ordinance authorising the Administration to borrow a maximum amount of outstanding principal at any time of HK\$100 billion or equivalent for the purposes of the Bond Fund

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GBP-related initiatives in 2013-14 Budget

- To expand the size of the GBP from the current HK\$100 billion to HK\$200 billion so as to provide adequate room for the GBP to continue
- To launch a further issuance of inflation-linked retail bond (“iBond”) with a size of up to HK\$10 billion

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Progress made under GBP

- A total of HK\$70.5 billion of GBs outstanding at end March 2013
 - HK\$50.5 billion institutional GBs
 - HK\$20 billion retail GBs, i.e. iBond
- Taking into account HK\$16.5 billion (including HK\$10 billion iBond and HK\$6.5 billion institutional GBs) additional bonds to be issued, the total outstanding amount of GBs is expected to reach HK\$87 billion as at end August 2013

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Ensured a steady & consistent supply of bonds by public sector

- As at end August 2013, a total of HK\$71 billion institutional GBs issued is projected

Financial year	Amount issued
2009-10	HK\$11.5 billion
2010-11	HK\$16.0 billion
2011-12	HK\$19.0 billion
2012-13	HK\$18.0 billion
April – August 2013	HK\$6.5 billion (projected)
Total	HK\$71 billion (projected)

- Announce half-yearly tentative issuance schedule for institutional GBs to promote transparency and predictability

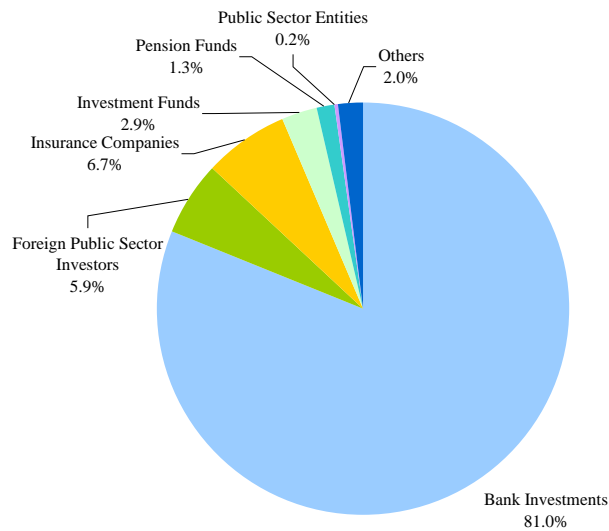
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Broadened institutional investor base

- Institutional bonds are well received by the market
 - Bid-to-cover ratio averaged to 3.32
 - A ratio of 2 and above suggests considerable demand
- Bonds of varying maturities can satisfy demand of different types of institutional investors
 - *Short-term bonds* : Commercial banks
 - *Medium-term bonds* : Investment funds
 - *Long-term bonds* : Insurance companies & pension funds

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Percentage breakdown of investors of institutional GBs at tenders



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Recognition by global bond benchmark indices

- Admitted into a number of bond benchmark indices
 - Barclays Asian Local Currency Diversified Bond Index
 - Markit iBoxx ABF Pan-Asian Index
- Helps attract benchmark tracking investors
- Only managed to get into some of these indices after implementation of GBP
- Two institutional GB issues reached a size of over US\$1 billion to efficiently meet investment and secondary market trading purposes
- HKD government bond market is still not sizeable enough to be admitted into the Citigroup World Government Bond Index

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Broadened retail investor base

- Two very successful HK\$10 billion iBond issuances
- Second issuance set new records in retail bond market in Hong Kong
- 10-15% new investors participating in the issuances
- Enhanced public awareness and interest

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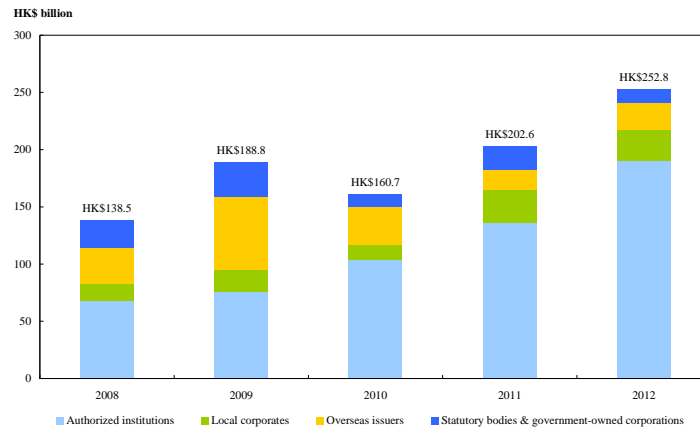
Growing demand for GBs

- Growing demand for high quality bonds issued by public sector for different purposes, such as for meeting regulatory requirements
- Banks need to hold more high quality assets (e.g. high quality bonds issued by public sector) following future introduction of Liquidity Coverage Ratio requirement under Basel III
- Some banks may increase their holding of bonds for such purposes in advance
- Hong Kong is one of the two jurisdictions with AAA credit rating in the Asian region

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Bond market offers another channel of financial intermediation

- Growing HKD bond issuances made by the private sector suggests that the bond market has become a financial intermediation channel to complement the banking sector and equity market



Proposal to expand the size of GBP

- Remaining quota of HK\$13 billion projected as at end August 2013
 - May not be sufficient for the upcoming demand from September onward
 - Not sufficient to meet the growing demand
 - Not sufficient to expand to a scale eligible for inclusion in some of the most widely tracked global bond benchmark indices
- We propose to expand the size of GBP to continue to operate GBP in a sustainable manner to demonstrate to investors the Administration's determination to develop the local bond market

Parameters of the enlarged Programme

- Flexible approach in setting issuance parameters of bond issuances to meet future demand, having regard to prevailing market conditions and GBP's capacity to support the development of different segments of the bond market
- Existing framework in managing funds will continue
 - All proceeds credited to Bond Fund
 - Bond Fund to meet expenses of GBP
 - Bond Fund is placed with the Exchange Fund for investment

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Way forward

- Plan to seek Legislative Council's approval as soon as possible of a resolution under the Loans Ordinance to raise the maximum amount of borrowings that may be outstanding by way of principal to HK\$200 billion for GBP within this legislative year
- Subject to Legislative Council's approval of the resolution by way of a positive vetting process, we will have certainty to plan the timing of the forthcoming and future GBs under both the institutional and retail parts of GBP

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End