

**For discussion
on 9 April 2021**

Legislative Council Panel on Financial Affairs

**Resolution to Raise the Maximum Amount of Borrowings
under the Government Bond Programme**

PURPOSE

This paper briefs Members on an initiative to raise the maximum amount of borrowings under the Government Bond Programme (“GBP”) from HK\$200 billion to HK\$300 billion by way of a resolution to be moved by the Government under the Loans Ordinance (Cap. 61), as announced by the Financial Secretary in the 2021-22 Budget Speech.

BACKGROUND

2. The GBP was set up in 2009 with the policy objective of promoting the further and sustainable development of the bond market in Hong Kong. It was established pursuant to the passage of a resolution by the Legislative Council (“LegCo”) in July 2009 under section 29 of the Public Finance Ordinance (Cap. 2) authorising the Government to set up a fund known as the Bond Fund for managing sums raised under the GBP, and a separate resolution under section 3 of the Loans Ordinance authorising the Government to borrow up to a maximum principal amount outstanding at any time of HK\$100 billion or equivalent for the purposes of the Bond Fund. The limit of the size of the GBP was raised from HK\$100 billion to HK\$200 billion following the passage of a resolution by LegCo on 22 May 2013 under section 3 of the Loans Ordinance to raise the borrowing limit of the Bond Fund.

3. On 24 February 2021, the Financial Secretary announced in the 2021-22 Budget Speech the plan to expand the size of the GBP from HK\$200 billion to HK\$300 billion with a view to promoting the sustainable development of the bond market in Hong Kong. It is proposed that a resolution be moved under the Loans Ordinance to raise the borrowing limit of the GBP accordingly.

JUSTIFICATIONS

GBP's Contribution to Bond Market Development

4. Since its establishment, the GBP has been promoting the development of the local bond market through systematic issuances of institutional and retail bonds. Under the institutional part of the GBP, Government Bonds (“GBs”) with tenors ranging from three to 15 years are tendered regularly to ensure a steady supply of public debt paper to satisfy the demand of institutional investors, such as pension funds, banks and insurance companies. Institutional GBs are issued in a systematic and consistent manner with issuance schedule determined and published in advance on a half-yearly basis in order to promote transparency and predictability in the market. While most GBs are denominated in Hong Kong dollar, three tranches of US dollar denominated Islamic bonds (or “sukuk”) were also issued in the past, demonstrating the diversity and viability of Hong Kong’s bond market as a fund-raising platform for the Islamic world.

5. Driven in part by regular government issuances, the Hong Kong dollar debt market has continued to grow since the GBP’s expansion in 2013. The outstanding amount of GBs has increased from HK\$47 billion at the beginning of 2013 to HK\$80.6 billion as at end-2020. Excluding the issuances of GBs and Exchange Fund Bills and Notes, total issuances of Hong Kong dollar debt instruments by the non-public segment increased from HK\$203 billion in 2013 to HK\$875 billion in 2020. Meanwhile, Hong Kong’s public debt market continues to attract attention and recognition by global indices such as the Markit iBoxx ABF Hong Kong Index and the Standard and Poor Hong Kong Government Bond Index.

6. Under the retail part of the GBP, retail government bonds are issued to meet the general public’s demand for stable investments of a high quality and to promote public interest in bond investment. So far, seven batches of iBond, an inflation-linked retail bond, and five batches of Silver Bond have been issued, all met with warm market reception and over-subscription (see [Annex](#) for the subscription results). As indicative in the fact that 6-13% of iBond subscribers in each issuance were first-time bond investors who specifically opened an investment account for iBond subscription, the introduction of iBond has broadened the investor base and contributed to the development of a retail bond market in Hong Kong. Silver Bond targets senior residents aged 65 or above who look for stable investment with steady return to support retirement planning. The success of the Silver Bond has not only enhanced the senior population’s interest in bond investment (6-15% subscribers being first-time bond investors), but also encouraged the financial industry to tap into the

immense potential of the silver market by providing more investment options for senior citizens.

Future Development of GBP

7. As at end-2020, the total outstanding amount of bonds under the GBP was HK\$124.3 billion, comprising 11 institutional issues totalling HK\$80.6 billion, three batches of Silver Bond totalling HK\$20.9 billion, one batch of iBond of HK\$15.0 billion, and one batch of US dollar sukuk with an issuance size of US\$1.0 billion. In the 2021-22 Budget Speech, the Financial Secretary has announced the plan to issue at least HK\$15 billion of iBond and HK\$24 billion of Silver Bond in the coming year. It is expected that when the interest rates normalise from the current ultra-low levels and the yield curve steepens, there will be a need to increase GB issuances further to meet growing demand from institutional investors. There is also scope for the Government to explore further expansion of the inflation-hedging retail bond issuances which offer stable and attractive returns to investors when the global investment environment is expected to remain challenging. The Bond Fund's position is projected to reach HK\$191.5 billion, near its borrowing capacity, by end-2022 if the current issuance pattern of institutional and retail bonds continues. It is therefore necessary to raise the borrowing limit for the GBP to operate in a sustainable manner and meet its mandate of further developing the Hong Kong bond market.

PARAMETERS OF THE ENLARGED PROGRAMME

8. The proposed increase of HK\$100 billion (for the maximum amount of outstanding principal) will provide room for further issuances under the GBP for the next few years and allow flexibility for the Government to adjust the issuance size and tenor of individual tranches in response to prevailing market conditions. When considering the types and other parameters of future issuances under the GBP, our overriding objective will continue to be promoting the further and sustainable development of the local bond market.

Issuance Framework

9. A flexible approach will be taken to ensure that issuance parameters (e.g. choice of issuance size and tenor) of individual bond issuances are conducive to the long-term development of the local bond market. We will not set limits for the proportion of institutional and retail bonds under the GBP. Due consideration will continue to be given to prevailing market conditions such as market demand, interest rates and potential impacts on other prospective

bond issuers in Hong Kong, as well as the GBP's capacity to support the development of different segments of the bond market. The Government will also continue to monitor market conditions with a view to issuing more institutional GBs with longer tenors at the far-end of the yield curve. Furthermore, we will look for opportunity to further diversify the types of GBs that will act as a benchmark for other issuers.

Management of Proceeds

10. The management of funds under the GBP will continue to follow the existing framework. All proceeds raised under the GBP will be credited to the Bond Fund. Expenses including interest payments and principal repayment for bonds issued under the GBP as well as other relevant expenses (e.g. expenses for external services) will be met by the Bond Fund. The Bond Fund does not form part of fiscal reserves and is managed separately from the Government accounts. The Bond Fund is placed with the Exchange Fund for investment and attracts investment income on the basis of the "fixed rate" sharing arrangement applicable to fiscal reserves.

THE RESOLUTION

11. The purpose of the proposed Resolution under section 3 of the Loans Ordinance is to authorise the Government to borrow for the purposes of the Bond Fund such sums not exceeding in total HK\$300 billion or equivalent, being the maximum amount of all borrowings made under the authorisation that may be outstanding by way of principal at any time. The Resolution requires that sums borrowed be credited to the Bond Fund, and is to replace the previous resolution passed by LegCo under the Loans Ordinance on 22 May 2013 prescribing the current ceiling of borrowings of HK\$200 billion or equivalent.

NEXT STEPS

12. We plan to move the proposed Resolution for positive vetting by LegCo within this legislative year.

13. Members are invited to note the legislative proposal in this paper.

Financial Services and the Treasury Bureau
April 2021

Subscription Results of iBond and Silver Bond

iBond

Year	Number of valid applications	Total valid application amount (HK\$ billion)	Allotment of bonds to valid applications	Percentage of first-time bond investors
2011	155,835	13.2	1 to 45 units	15%
2012	332,467	49.8	1 to 4 units	10%
2013	520,823	39.6	1 to 2 units	13%
2014	488,170	28.8	1 to 3 units	10%
2015	597,895	35.7	1 to 2 units	9%
2016	507,978	22.5	1 to 3 units	8%
2020	456,380	38.4	1 to 4 units	6%

Silver Bond

Year	Number of valid applications	Total valid application amount (HK\$ billion)	Allotment of bonds to valid applications	Percentage of first-time bond investors
2016	76,009	8.9	1 to 5 units	15%
2017	44,842	4.2	1 to 10 units	10%
2018	45,488	6.2	1 to 8 units	6%
2019	56,564	7.9	1 to 6 units	8%
2020	135,243	43.2	1 to 14 units	11%