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Asset Management

EMERGING MARKETS

ONSHORE RMB BONDS AS STRATEGIC INVESTMENT

Chinese local currency debt: coming of age

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China's onshore renminbi-denominated bond market is an emerging asset class of global significance.

China's onshore renminbi-denominated bond market is gaining depth and opening up rapidly. These are developments investors cannot afford to ignore.

As part of a broader effort to liberalise China's capital account, authorities in Beijing have removed restrictions on overseas investors in the country's USD11 trillion onshore fixed income market, the third largest in the world.

This is sure to increase foreign investment, which currently stand at less than 2 per cent.

It should also bolster China's case for inclusion in the world's major global bond indices – which would be another important step in the market's evolution into a strategic asset class. Bloomberg has decided to add RMB onshore bonds to its Global Aggregate Index from April 2019. Should other index providers, like JPMorgan and FTSE, follow suit, some USD286 billion of foreign capital could flow into the asset class.

Adding RMB bonds to a fixed income portfolio has a number of potential benefits. Not only do such securities offer attractive yields, but their returns are also not highly correlated with those of other bonds. This means they can both boost income and diversify a portfolio's sources of risk and return. Investors should also benefit from the internationalisation of China's currency, which we believe should strengthen against the dollar over the longer term thanks to the country's healthy economic growth and trade surplus. Currency appreciation has the potential to bring an additional source of return for bond portfolios.

China's economy is on track to surpass that of the euro zone sometime this year and match the US's in the next few decades; its onshore debt market is likely to follow a similar path. This is why we believe it deserves to be featured more prominently in global fixed income portfolios.

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