

## On the Benefits and Problems of the Offshore RMB Bonds in Hong Kong and Macao Issued by Local Governments in China

**MingJing Chen**<sup>1</sup>, Faculty Of Finance, City University of Macau, Macao, China, [mingjingchen901@gmail.com](mailto:mingjingchen901@gmail.com)

**ZhongZhuoFei Tan**<sup>\*</sup>, Department of Automotive Mechanical and Electrical, Liuzhou Technical School, Liuzhou City, China, [zhongzhuofeitao@gmail.com](mailto:zhongzhuofeitao@gmail.com)

Key Words: Offshore RMB Bonds, Bond Financing, Local Government, Local Debt

Abstract:

Offshore RMB bonds, as an important component of China's financial market construction and opening-up, have received attention and research from multiple parties. At present, the governments of Guangdong Province, Shenzhen Municipality, and Hainan Province in China have issued offshore RMB bonds in Hong Kong and Macao. These bonds can broaden the government's offshore financing channels, facilitate government participation in offshore RMB transactions, and promote the development of RMB internationalization. At the same time, as the issuance of offshore RMB bonds is still in the exploratory stage and there are still certain problems, it is necessary for the central and local governments to work together to improve specific policy measures for offshore RMB bonds, optimize cross-border issuance processes, and prepare emergency plans for bond repayment, in order to make the offshore RMB bond market legal, compliant, and thriving.

### 1. Introduction

Offshore RMB bonds mainly refer to bonds issued outside Chinese Mainland that are denominated in RMB, receive interest regularly, and pay principal and interest in RMB when due. According to announcements released by local governments, in October 2021, Shenzhen Municipality recorded and issued 5 billion offshore RMB bonds in Hong Kong. In October 2022, Hainan Province issued 5 billion yuan of local bonds in Hong Kong. In addition to Hong Kong, Guangdong Province also issued 2.2 billion and 2 billion offshore RMB bonds in Macao in October 2021 and October 2022, respectively. The specific content is as follows: date, issuing region, total amount, issuing department, category, issuing period, issuing regulations.

Date	Bond Market	Total Amount	Issue Department	Bond Type	Term	Issuance Scale	Interest Rate	Subscription Multiple
2021	Hong	5 billion	Shenzhen	Blue Bond	2-year	1.1	2.60%	3.03x

Date	Bond Market	Total Amount	Issue Department	Bond Type	Term	Issuance Scale	Interest Rate	Subscription Multiple
October	Kong	yuan	Municipal Government			billion yuan		
				Green Bond	3-year	1.5 billion yuan	2.70%	
				Green Bond	5-year	2.4 billion yuan	2.90%	
2022 October		5 billion yuan	Hainan Provincial Government	Blue Bond	2-year	1.2 billion yuan	2.43%	2.20x
				Sustainable Development Bond	3-year	2.6 billion yuan	2.65%	
					5-year	1.2 billion yuan	2.85%	
2021 October	Macao	2.2 billion yuan	Guangdong Provincial Government	General Bond	3-year	2.2 billion yuan	2.68%	3.40x
2022 October		2 billion yuan		Special Bond	3-year	2 billion yuan	2.65%	2.50x

The offshore RMB bonds market, as an important component of China's financial market construction and opening-up, is playing an increasingly important role in accelerating the construction of a new development pattern with domestic circulation as the main body and domestic and international dual circulation promoting each other. According to the data in the table above, the offshore RMB bonds issued by local governments are mainly special bonds. Among them, the offshore RMB bonds issued by the Shenzhen Municipal Government include blue bonds and green bonds, mainly used for the construction of ordinary public high schools, urban rail transit, and water treatment; The offshore RMB bonds issued by the Hainan Provincial Government include blue bonds and sustainable development bonds are mainly used for green economic development, marine environmental protection, and key livelihood guarantees.

The issuance of government offshore RMB bonds by Shenzhen Municipality in Hong Kong is in response to the "Comprehensive Reform Pilot Implementation Plan for Building a Pilot Demonstration Zone of Socialism with Chinese Characteristics in

Shenzhen (2020-2025)" and the "Implementation Opinions on Supporting Shenzhen's Exploration of Innovative Financial Policy System and Management System" (Caiyu [2022] No. 139) issued by the General Office of the Communist Party of China Central Committee and the General Office of the State Council in 2020. In response to this, the Hong Kong Special Administrative Region government has introduced supporting measures to exempt the interest paid and profits obtained from Shenzhen Municipal Government debt bills from profit tax. At the same time, Hong Kong has also increased its support for the financial infrastructure construction of its fixed income market.

The offshore RMB bonds issued by Guangdong Province to Macao, including general bonds and special bonds. The general bonds issued in 2021, mainly used for external ordinary financing, and the special bonds issued in 2022 are specifically used for the construction of related infrastructure projects in Nansha District, Guangzhou City. The purpose is more clear and in line with the requirements of the "Opinions on Financial Support for the Construction of the Guangdong-Hong Kong-Macao Greater Bay Area". It also responds to the "Action Plan for Guangdong Financial Support for High Quality Economic Development in 2023" issued by the General Office of the Guangdong Provincial Government in 2023. At the same time, the Macao SAR government has also introduced certain supporting measures for local government bonds in Guangdong Province, such as exempting stamp duty and supplementary income tax on related income. The Macao SAR government is also continuously accelerating the improvement of financial market infrastructure, relevant regulatory systems, laws and regulations, and supporting guidelines, introducing tax incentives, and increasing the pace of financial talent reserves. These are of great significance for deepening the implementation of the financial markets in the Guangdong-Hong Kong-Macao Greater Bay Area and achieving interconnectivity.

## 2. The benefits of local governments about issuing offshore RMB bonds

The reason for issuing RMB local bonds through the offshore market is that offshore RMB bond financing can provide local governments with better and more convenient channels for external financing. Unlike RMB equity financing, RMB bond financing is more suitable for financing needs of different themes such as government, enterprises, and financial institutions in China. Moreover, the purchasers of bonds are mostly institutional investors, who have a relatively high ability to assess and bear risks, while there are more small and medium-sized investors among equity investors. Compared to equity financing, bond financing is relatively easier to operate. As a fixed income product, its price fluctuation is relatively small and its safety is higher. And from the experience of other economic powers, especially the United States and Japan, local currency international bonds will better promote the development of an outward oriented economy. Issuing international bonds can provide local currency financing to non residents, increase external demand, and promote domestic economic development. Moreover, compared with bank loans, RMB international bonds have longer financing terms and relatively larger financing scales, making them more

suitable for local governments to provide financing for long-term and large-scale infrastructure construction (Zhou Yu, 2017). Developing offshore RMB trading can not only broaden new channels for offshore RMB asset investment, but also facilitate the participation of government departments, commercial banks, and enterprises within China in offshore RMB trading. Among them, offshore RMB bonds are easier to scale up, and issuing offshore RMB bonds is also more convenient for domestic government departments, commercial banks, and enterprises to participate. Moreover, due to the high interest rates within China, offshore RMB assets within the country also have strong appeal to offshore investors (Wang Sunan, 2021).

The issuance of offshore RMB bonds also plays a very important role in promoting the internationalization process of the RMB. By studying the relationship between RMB internationalization and international financing of local government bonds, it can be concluded that international financing of local government bonds and RMB internationalization can mutually promote each other. RMB internationalization can export RMB outward and promote the development of offshore RMB financial products. The issuance of local government bonds in the offshore market in China can increase the breadth and depth of the offshore RMB market, and improve the internationalization level of the RMB (Wang Liping, 2019). The issuance of offshore RMB bonds not only broadens local government financing channels, reduces borrowing costs, and enriches offshore RMB asset investment varieties, but also has a significant impact on promoting the internationalization of the RMB, promoting market-oriented issuance of local bonds, further standardizing issuance standards, enhancing the international reputation of local governments, and supporting regional development (Lin Jing et al., 2023).

In terms of the issuance of offshore RMB bonds by the local government, the issuance of offshore RMB bonds has also played a leading role. From the perspective of the Ministry of Finance, the issuance of offshore RMB bonds in Hong Kong for offshore investors can be described as "one arrow and four eagles": on the one hand, it can provide international investors with sovereign bonds of high credit rating, thus meeting the international demand for RMB assets generated by the expectation of RMB appreciation in recent years; Secondly, it will help deepen economic and financial cooperation between the mainland and Hong Kong, and consolidate and strengthen Hong Kong's position as an international financial center; Thirdly, it can promote the development of the offshore RMB market in Hong Kong and advance the internationalization process of the RMB; Forth it helps to digest a portion of hot money, form an effective mechanism for the return of RMB, and eliminate some hidden risks of RMB inflation (Wang Ruzhong, 2012). Based on this, promoting the offshore issuance of local government bonds can not only attract huge amounts of funds from offshore investors, but also further promote the internationalization of the RMB, and can also promote the reform and improvement of the local government bond issuance mechanism through offshore issuance (Liu Rui, 2021). Moreover, as the offshore RMB bonds issued by local governments in China are mainly "green bonds" and "blue bonds", it is also conducive to anchoring the investment philosophy

and preferences of international investors for sustainable development (Chen Lu, 2022).

### 3. Problems that local governments should pay attention to when issuing offshore RMB bonds

The main purpose of local governments issuing offshore RMB bonds in Hong Kong and Macao is to finance large-scale public services and infrastructure projects. For example, the bonds issued by the Guangdong Provincial Government and the Shenzhen Municipal Government are aimed at supporting high-quality development in areas such as transportation, energy, basic education, and housing projects, as well as urban sewage treatment and marine ecological protection, in the context of the integration plan of the Guangdong-Hong Kong-Macao Greater Bay Area. The issuance of offshore RMB bonds by the Hainan Provincial Government is mainly to support the construction of the free trade port. Its fundraising will help promote sustainable water resources and wastewater management, shantytown renovation, and medical infrastructure construction projects, and promote green economic transformation.

Previously, there were four issuance markets for local bonds in China, namely the interbank market, including the commercial bank counter market. In addition, there were also Shanghai Stock Exchange, Shenzhen Stock Exchange, Beijing Stock Exchange, etc. However, these markets are onshore rather than offshore. The issuance of offshore RMB bonds by local governments in Hong Kong and Macao is not only an important breakthrough but also a huge challenge for China's bond market and relevant departments. Therefore, attention should be paid to the following aspects:

#### 3.1 Improving relevant specific policy measures

To support local governments in issuing offshore RMB bonds in Hong Kong and Macao, the Guangdong Provincial Government, Hainan Provincial Government, and Shenzhen Municipal Government have all introduced certain policy measures to promote the issuance of offshore RMB bonds. However, these measures are basically incentive policies rather than restrictive policies. For example, the Opinion on Financial Support for the Construction of the Guangdong-Hong Kong-Macao Greater Bay Area includes relevant clauses such as "Supporting non bank financial institutions in mainland China to carry out cross-border business with Hong Kong and Macao regions", "Orderly promoting the interconnection of financial markets and infrastructure between Guangdong, Hong Kong and Macao", "Promoting the development of offshore RMB markets and supporting the development of offshore RMB businesses in Hong Kong and Macao", and "Supporting financial regulatory cooperation between Guangdong, Hong Kong and Macao". The Implementation Opinions on Supporting Shenzhen Municipality's Exploration and Innovation of Fiscal Policy System and Management System only include "Improving the local government debt management system" and "Supporting Shenzhen Municipality to continue issuing offshore RMB bonds offshore". The 2023 Guangdong Province

Financial Support for High Quality Economic Development Action Plan only mentions "Continuing to apply to the Ministry of Finance for the issuance of offshore RMB bonds in Hong Kong and Macao", "Expanding multi-channel financing such as equity and bonds", and "Maintaining stable development loan and bond financing". Other files even have a global plan without specific content, so it's just a matter of going into detail.

Offshore RMB bonds are a new financing method and means. Since 2021, the local governments of Shenzhen Municipality, Guangdong and Hainan provinces have issued offshore RMB bonds in Hong Kong and Macao, which has also received encouragement, annotation, and support from the local government. However, the issuance time of offshore RMB bonds is relatively short, and there are currently relatively few policies related to offshore RMB bonds issuance in local government bond policies. Local governments mainly issue offshore RMB bonds in accordance with the financial market policies of Hong Kong and Macao, while there are still many gaps in the cross-border issuance issues that arise from the mainland to offshore.

Therefore, it is recommended that the Chinese government accelerate reforms, collaborate with the governments of Hong Kong and Macao Special Administrative Region, and improve supporting policies and measures for cross-border financial markets, such as issuance pricing mechanisms, credit ratings, and information disclosure. At present, China's domestic local bonds are in the process of "Anchor Changing" from the treasury bond yield as the benchmark to the local bond yield as the benchmark. In the case that local governments actively go to Hong Kong and Macao to issue offshore RMB bonds, they can consider promoting the market pricing of offshore RMB bonds. Currently, there are relatively few offshore RMB bonds participating in debt rating, less than 50%. The lack of corresponding credit ratings for bonds will reduce their recognition. Therefore, it is recommended to introduce professional rating agencies and standards to conduct credit ratings on each bond and improve the credit rating mechanism. Information disclosure on offshore RMB bonds is even rarer. Therefore, it is recommended that relevant departments establish a sound information disclosure mechanism for offshore RMB bonds issued by local governments, and reasonably disclose the use of raised funds and project implementation progress. This is also beneficial for investors to understand. If the project makes good progress, it will also give potential investors a positive investment signal.

### 3.2 Optimizing the cross-border issuance process

The issuance of offshore RMB bonds, in addition to the general processes of document provision, rating, bookkeeping, pricing, distribution, settlement and delivery, also requires the establishment of a special working group for offshore debt, including the lead underwriter and underwriter, as the issuance is located offshore. It is responsible for conducting due diligence in legal, financial, and business aspects, and drafting issuance letters, bond terms and conditions, subscription agreements, and

legal opinions by international lawyers. In the process of preparing for issuance, as the lead person, the issuer, in addition to the parts that can be completed through the working group, needs to participate in many processes, including but not limited to project coordination, regulatory approval, and transaction document preparation. Due to the issuance location being offshore, government personnel are subject to certain restrictions on leaving the country, and the issuance of offshore RMB bonds requires strong professionalism and entry barriers. Local governments located far away from Hong Kong and Macao may not have a good understanding of the business of issuing offshore RMB bonds. Therefore, due to a series of issues such as distance and domestic and offshore restrictions, they may abandon their plans to issue offshore RMB bonds in Hong Kong and Macao. It can be seen that the local governments currently issuing offshore RMB bonds in Hong Kong and Macao mainly include Guangdong Province, Shenzhen Municipality, and Hainan Province, all of which are located in areas closer to Hong Kong and Macao.

The development of offshore RMB bonds can further improve the offshore RMB financial market and promote the two-way development of China's bond market. At present, offshore RMB bonds are still in the exploratory period, with a relatively small scale and a relatively low proportion held by offshore institutions, and the bond recognition is not high enough. If further support can be provided to local governments to issue offshore RMB bonds in Hong Kong and Macao, it will have a positive effect on expanding financing channels, improving local bond management mechanisms, and enhancing the marketization level of local bonds, promoting the internationalization of local bonds, and accelerating the exchange between local bonds and the international market.

Therefore, it is recommended to increase the promotion of offshore RMB bonds by local governments, enhance their awareness and recognition of offshore bond issuance, optimize the cross-border issuance process of local bonds, and provide issuers (government personnel) with certain convenience for cross-border issuance under legal and compliant conditions, facilitating their cross-border travel and work. Alternatively, corresponding cross-border issuance departments and platforms can be established to directly connect with local governments, Hong Kong and Macao Special Administrative Region governments, and offshore financial institutions, facilitating the cross-border issuance of offshore RMB bonds by local governments.

### 3.3 Preparing a plan for bond maturity repayment.

The main reason for issuing local bonds is when the local government's fiscal revenue and expenditure are unbalanced, issuing local bonds to obtain development funds for the region. According to information on offshore RMB bonds issued by local governments, the repayment terms of these bonds are generally 2 years, 3 years, and 5 years. Guangdong Province will face bond repayment issues in October 2023 and October 2024, while Hainan Province will face bond repayment issues in October 2024, October 2025, and October 2027. Date Issuing Department Issuing Period Issuing Scale Pricing Interest Rate Subscription Multiple Return.

It is worth mentioning that the total scale of offshore RMB bond issuance in Guangdong Province and Hainan Province is 4.2 billion yuan and 5 billion yuan respectively, while Shenzhen, a single city, has issued offshore RMB bonds with a total scale of 5 billion yuan. It will face the repayment problem of the first bond in October 2023, the second bond in October 2024, and the third bond in October 2026. Although Shenzhen Municipality's economic development level has always been among the top in the country, according to information released by the Shenzhen Municipal Finance Bureau, the general public budget revenue in Shenzhen Municipality's jurisdiction in 2021 was 1111 billion yuan, while in 2022 it was 1107.48 billion yuan, a decrease of 0.3% from the previous year. In addition, the balance of local bonds in Shenzhen in 2021 was 142 billion yuan, which has risen to 208.3 billion yuan by 2022. This raises concerns about whether there is enough funds to repay the local bonds issued and matured in 2023. According to relevant research data, the debt scale of Guangdong Province in 2022 is 2508.23 billion yuan, with a debt ratio of 19.49%, a government debt ratio of 220.56%, and a GDP coverage rate of 316.95%. The debt scale of Hainan Province in 2022 is 348.66 billion yuan, with a debt ratio of 51.1%, a government debt ratio of 312.53%, and a GDP coverage rate of 167.65%. Although the debt scale of Hainan Province is not as large as that of Guangdong Province, its debt ratio has reached 51.1%, approaching the debt anomaly warning line of 60%. The issuance of offshore RMB bonds, while filling the funding gap for local government public service projects and infrastructure construction, will also increase the debt repayment pressure on local governments, leading to new financial problems that need to be jointly solved by central institutions and local governments.

Date	Issue Department	Term	Issuance Scale	Interest Rate	Subscription Multiple	Repayment Time
2021 October	Shenzhen Municipal Government	2-year	1.1 billion yuan	2.60%	3.03x	October 2023
		3-year	1.5 billion yuan	2.70%		October 2024
		5-year	2.4 billion yuan	2.90%		October 2026
2022 October	Hainan Provincial Government	2-year	1.2 billion yuan	2.43%	2.20x	October 2024
		3-year	2.6 billion yuan	2.65%		October 2025
		5-year	1.2 billion yuan	2.85%		October 2027
2021 October	Guangdong Provincial Government	3-year	2.2 billion yuan	2.68%	3.40x	October 2023



2022 October		3-year	2 billion yuan	2.65%	2.50x	October 2024
-----------------	--	--------	-------------------	-------	-------	--------------

In this regard, the central government of China, such as the Ministry of Finance, should calculate indicators such as debt ratio, new debt ratio, debt repayment ratio, and overdue debt ratio based on the general debt, special debt, and contingent debt situation of each region, evaluate the debt risk situation of each region, and provide risk warnings for high-risk debt areas. Chinese Local Governments should also effectively control the scale of debt and strictly implement limit management. Establish an emergency response mechanism for debt risk. Chinese Local Governments also should strengthen budget constraints, prevent moral hazards, and clarify debt repayment responsibilities. Governments at all levels should develop emergency response plans and establish accountability mechanisms. If Chinese Local Governments encounter difficulties in debt repayment, they can consider using methods such as controlling project scale, compressing public funds, and disposing of existing assets to raise funds through multiple channels to repay debts. When it is difficult to repay debts on their own, they should be reported in a timely manner. The Chinese local and higher-level governments should activate emergency response plans and accountability mechanisms for debt risks, effectively resolve debt risks, and hold relevant personnel accountable.

#### 4. Conclusion

The issuance of offshore RMB bonds is a key link in promoting RMB internationalization, as well as an important way to broaden local government financing channels and alleviate funding gaps in China. However, the development of offshore RMB bonds in China is still in the initial exploration stage, with a relatively small issuance scale and few participating issuers (local governments). Externally, offshore institutional investors hold a small number of bonds and have low recognition. Therefore, it is recommended that China accelerate the improvement of specific policy measures for offshore RMB bonds, optimize the offshore issuance process of offshore RMB bonds, and prepare a bond maturity repayment plan to achieve the vigorous and sound development of the offshore RMB bond market as soon as possible.

## References:

- [1]Lin Jing, Ma Jingchao, Sun Bo, Xiao Zhipeng&Feng Yuchi (2023). Research and Discussion on Offshore RMB Local Government Bonds Bonds (03), 20-24
- [2]Liu Rui (2021) Actively promote the overseas issuance of local government bonds China Foreign Exchange (17), 40-41
- [3]Wang Liping&Shen Jianwen (2019). Research on the International Financing Mechanism of Local Government Bonds in China Journal of Central University of Finance and Economics (10), 14-29
- [4]Wang Ruzhong and Dou Jiao (2012). Research on the Development Reasons, Problems, and Countermeasures of Hong Kong's Offshore RMB Bond Market Shanghai Finance (07), 79-83+118
- [5]Wang Sunan (2021). Reform suggestions for developing the offshore RMB market within China Tsinghua Financial Review (11), 60-62
- [6]Zhou Yu (2017). Supporting infrastructure investment of the "the Belt and Road" with RMB international bonds: a comparative analysis based on the international bonds of the US dollar and the Japanese yen World Economic Research (10), 15-24+135