

YIELD-HUNGRY INVESTORS DEVOUR DIM SUM BONDS

BY MICHELLE CHEN

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Yield-hungry investors are moving to the offshore yuan bond market in search of higher returns, flocking to three high-yield bonds issued in the past week which were all priced lower than initial guidance due to strong demand. Investors put in a total of more than 14 billion yuan (\$2.25 billion) worth of orders for the bonds sold by Chinese firms Gemdale (Asia), 21Vianet and Russian Standard Finance, which raised a combined 3.75 billion yuan after a quiet high-yield dim sum bond pipeline so far this year.

Lack of supplies from sub-investment-grade issuers in the primary market partly explains that enthusiasm, especially from fund and asset managers who took the bulk of these transactions.

"The yield level for high-yield dim sum bonds still has room to fall further in the coming months, thanks to ample liquidity and restoration of confidence in China's economy and currency," said a portfolio manager in Hong Kong.

The average yield of high-yield and non-rated dim sum bonds tracked by HSBC has been declining since last June and is now at an 18-month low. It stood at 4.91 percent on Thursday for a collection of bonds with an average duration of 1.9 years.

HSBC analysts said they remain constructive on the high-yield space as investors continue to chase yield. In their view, the existing dim sum bonds in the property space are fairly valued and they thus favor potential new issues from China and Hong Kong developers.

The current favorable environment has greatly compressed the pricing levels of recent bond issuance, even for those whose names are unfamiliar to the market and which do not have an international rating.

Take 21Vianet Group as an example. Neither the company nor the issue is rated, but the Chinese internet data centre services provider managed to sell its debut three-year bond at 7.95 percent, much tighter than the initial guidance of 8.25 percent.

"We think this was priced too tight for a company with a business model subject to regulatory headwinds, significant structural subordination risk and weak covenant protection," said OCBC bank in a note.

The appetite for dim sum bonds comes at a time when the red-hot dollar bond market has begun to cool down. Asian junk-rated dollar bonds rallied significantly and demand for bonds sold by Chinese real estate companies well exceeded supply at the beginning of the year.

"The dollar bond market is digesting previous heavy issuance and there's some evidence that funds are also flowing from bond markets to stock markets, putting upward pressure on yield levels," said a bond trader at a brokerage house in Hong Kong.

Dim sum bonds have attracted more attention, though, as funding costs have been steadily declining. Chinese property firm Gemdale (Asia) sold a five-year dim sum bond at 5.625 percent, and that could be translated to Libor+360 to Libor+400 basis points, calculated by traders.

It was quite a low level even in the dollar bond market and was much cheaper than the three-year offshore yuan bond the company sold last July which carried a coupon of 9.15 percent.

That said, the chance of an adjustment in the dim sum bond market will increase in the second half the year as inflation concerns in China may gradually surface and force the central bank to take measures to mop up excess liquidity, the portfolio manager in Hong Kong said.

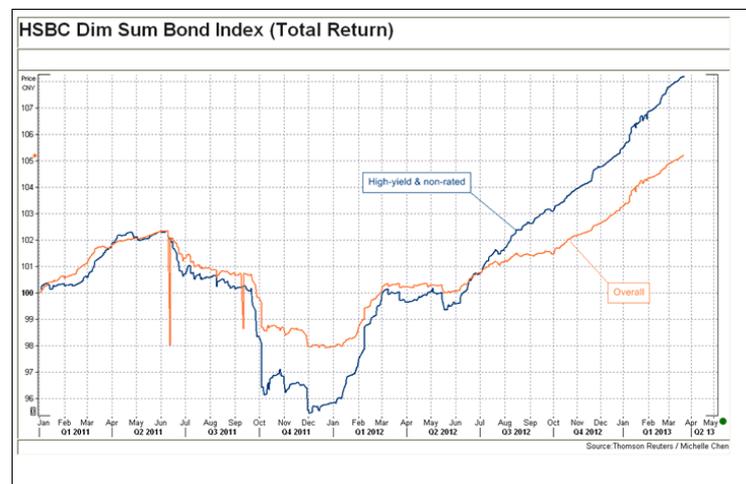
China's central bank chief Zhou Xiaochuan recently emphasized the importance of stabilising inflation expectations and pledged to manage the risks of rising prices as the economy recovers. The country's consumer inflation quickened to 3.2 percent in February.

Asian Development Bank said in a report on Monday that emerging East Asia's local currency bond markets continued to expand in 2012, signaling continued investor interest in the region's fast-growing economies but also raising the risk of asset price bubbles.

The region is much more resilient than it used to be, but governments still need to be careful that they are prepared for a possible reversal in the flows when the U.S. and European economies pick up again, the bank said.

CHART OF THE WEEK

HSBC dim sum bond index: <http://link.reuters.com/fuv76t>



LEAGUE TABLES

YTD Dim sum bond issuance

Bookrunner	Amount Rmb (m)	Number of issue
HSBC Holdings PLC	15,559.2	43
Standard Chartered PLC	7,512.5	21
BNP Paribas SA	7,388.3	24
National Australia Bank	2,000.0	3
Bank of China Ltd	1,876.7	2

Based on Thomson Reuters data as of March 21, 2013

WEEK IN REVIEW

- China can complete the reform on yuan convertibility under the capital account and the use of yuan in cross-border trade over the next 10 years if there is no big changes in the international market, Liu Shiyu, deputy central bank governor of China, said.
- Taiwan's financial regulator said on Thursday it is planning to ease rules for local companies to sell yuan-denominated bonds in the island by waiving credit ratings on the issuers, a move aimed at catching up with Hong Kong's dim sum bond market.
- Taiwan's central bank governor Perng Fai-nan said on Monday the bank is actively working on a currency swap agreement with China, and he hopes the quota will be no less than 300 billion yuan.
- China will speed up reforms to open up its capital account now that People's Bank of China Governor Zhou Xiaochuan has been reappointed, the PBOC Deputy Governor Yi Gang said on Sunday. Yi said China was also close to finalizing new or renewed currency swap agreements with Brazil, Argentina and Britain.
- A bipartisan group of U.S. lawmakers began a new attempt on Wednesday to pass legislation that puts pressure on China to change its currency practices. It came as U.S. Treasury Secretary Jack Lew was wrapping up a two-day visit to China, where he pressed Beijing to allow the yuan to rise further against the dollar.
- A \$200 million-equivalent, five-year loan has been launched for Fujian Fuxin Special Steel, reported by Basis Point, a Thomson Reuters publication. The loan comprises a \$140 million tranche that offers a margin of 120bp over Libor, and a 400 million yuan tranche that offers a margin of 130bp over the average of the CNH Hibors of Bank of China Hong Kong and HSBC.

(Editing by Kim Coghill)

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(\$1 = 6.2118 Chinese yuan)



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