RMB handbook: Capitalising on Renminbi
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China: A Nation of Opportunities

China’s exponential growth has made it the world’s economic engine. Extraordinary growth in recent decades has transformed China’s economy and powered global growth. Today, China’s consumers attract global brands and its sophisticated manufacturing industry is at the heart of international supply chains. And China’s commitment to financial reforms and capital account opening mean the renminbi (“RMB”) has become a truly global trade, investment and reserve currency.

Four broad themes stand out:

- Growing Middle Class
- Digitalisation
- Belt and Road Initiative
- Green Development

Key facts:

- 2nd largest economy in the world: 2017 GDP was USD 12.8 trillion, grew by 32x in the last 27 years
- GDP growth rate: 6.9% in 2017
- Population: 1.38 billion (4x the United States population or 2x Europe population)
# China: Catalysts for Change

## Growth drivers

### Growing Middle Class
- According to HSBC Global Research, by 2025, more than 60% of the urban population will be classified as “middle class”. This drives the demand for travelling, health, education and consumer goods.
- McKinsey Global Institute foresees that 700 Chinese cities will generate USD7 trillion, or 30%, of global urban consumption growth between now and 2030.
- Over 24 million passenger cars were sold in China in 2016, equivalent to 35% of the world’s total sales or 3.5x of US’s.

### Digitalisation
- Internet penetration rate has reached over 50% with 739 million internet users as of Jun17.
- The country is now the world’s largest e-commerce market: online retail sales in mainland China totalled nearly RMB5.2 trillion in 2016, up 26.2% from a year earlier.
- China e-commerce sales are expected to grow to USD1.7 trillion by 2020, according to a recent forecast by Goldman Sachs.

### Belt and Road Initiative
- China continues to encourage Outbound Direct Investment (ODI) related to the Belt and Road Initiative (BRI) despite the overall capital outflow control by regulators.
- China is using BRI as a catalyst to raise the proportion of RMB in trade, overseas investment, financing by development banks, Chinese policy banks and commercial banks.
- The Belt and Road Initiative aims to better connect infrastructure links across Asia, Europe and Africa, which accounts for c.63% of the world’s population and c.30% of the world’s total economic output.
- China expects its trade with countries along Belt & Road routes to exceed USD2.5 trillion a year within the next decade.

### Green Development
- The People’s Bank of China (PBOC) estimates that an annual investment of at least RMB2-4 trillion (USD320-640 billion) will be required to address environmental and climate change issues.
- Green bond issuance from China increased in 2016 from almost zero to RMB238 billion (USD36.2 billion), accounting for 39% of global issuance in 2016.

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**Sources:**
1. The International Organization of Motor Vehicle Manufacturers.
2. Internet World Stats.
## Journey to RMB Internationalisation

The differences between RMB and other major global currencies are disappearing fast. Every day, all around the world, corporates and investors are using RMB for trade, investment, hedging, cash management and financing. With its inclusion in the International Monetary Fund’s (IMF) Special Drawing Rights (SDR) basket, RMB has confirmed its evolution from a trade currency to an investment currency and – ultimately – one of the world’s elite reserve currencies.

### 1 Trade Currency
- 1st offshore centre in Hong Kong for personal RMB service
- PBOC and Hong Kong Monetary Authority signed Currency Swap Agreement
- Launch of RMB trade settlement pilot scheme for Hong Kong and Macau
- Pilot trade settlement scheme went nationwide
- Launch of Shanghai Free Trade Zone (FTZ) in 2013 and the subsequent launch of 10 new FTZs in Guangdong, Fujian and Tianjin in 2015

<table>
<thead>
<tr>
<th>Quantum of Growth</th>
<th>Opportunities</th>
</tr>
</thead>
<tbody>
<tr>
<td>China’s trade in RMB¹ (% of trade settled)</td>
<td>HSBC Global Research expects that 50% of China’s overall trade will be settled in RMB by 2020</td>
</tr>
</tbody>
</table>

### 2 Investment Currency
- 1st offshore centre in Hong Kong
- 1st RMB Dim Sum Bond issued in Hong Kong
- Launch of Qualified Domestic Institutional Investor (QDII) to allow Chinese institutions to invest in offshore markets
- 1st RMB Qualified Foreign Institutional Investor (QFII) scheme launched in Hong Kong with initial quota of RMB20 billion
- Launch of Shanghai-Hong Kong and Shenzhen-Hong Kong Stock Connect and Bond Connect (Northbound)
- Policy relaxation on access to China’s Interbank Bond Market (CIBM)

### 3 Reserve Currency
- Inclusion of RMB in the basket of SDR of IMF in OCT16

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</tr>
</thead>
<tbody>
<tr>
<td>RQFII quota² RMBbn</td>
<td>2.2</td>
<td>6.6</td>
<td>8.4</td>
<td>11.7</td>
<td>22.0</td>
<td>28.7</td>
</tr>
<tr>
<td>Dim Sum Bond³ RMBbn</td>
<td>270</td>
<td>1,210</td>
<td>1,740</td>
<td>10x</td>
<td>393</td>
<td>87</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>2011</th>
<th>2015</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>RQFII quota² RMBbn</td>
<td>6.4x</td>
<td>10x</td>
</tr>
<tr>
<td>Dim Sum Bond³ RMBbn</td>
<td>39</td>
<td>87</td>
</tr>
</tbody>
</table>


- More available channels allow foreign investors to invest into China:
  - RMB Qualified Foreign Institutional Investor (QFII) scheme
  - Shanghai-Hong Kong Stock Connect
  - Shenzhen-Hong Kong Stock Connect
  - Direct access to China Interbank Bond Market (CIBM)
  - Bond Connect

- Reserve managers see the RMB’s share of global reserves rising to 9% by 2025.

- 4 years ago only 3 central banks invested in RMB and now the number is 45.

- HSBC Global Research expects that 50% of China’s overall trade will be settled in RMB by 2020.
RMB: A Truly Global Currency

The RMB is the 3rd most used currency in trade finance\(^1\).

RMB: A Truly Global Currency

6th most used global payment currency\(^1\).

23 RMB clearing banks\(^3\).

World’s 8th most actively traded currency and the most actively traded emerging market currency in 2016\(^2\).

101 countries are using the RMB for payments with mainland China and Hong Kong:
57 of those use RMB for 10%+ of their payments\(^1\).

Foreign central banks and monetary authorities holding of RMB assets: USD85bn as at the end of 2016\(^4\).

The Chinese bond market is the third largest in the world.

Estimated size of market is USD8.2tn\(^5\), and foreign holdings est. 3%.

Since October 2016 the International Monetary Fund basket is made up as follows:

Special Drawing Rights

34 currency swap agreements totalling over RMB 3trn\(^7\).

332 of foreign institutions holding RMB bonds in CIBM\(^8\).

**Doing Business in China using RMB**

**Are you operating in China?**

*Onshore corporates’ consideration*
- Save FX costs and simplify FX administrative process
- Natural hedge for payables and receivables
- Natural hedge for asset and liabilities if foreign invested companies have capital injected in RMB
- Improve client relationship and widen client base

**Are you trading with China?**

*Offshore corporates’ consideration*
- Improve supplier / buyer relationship by transacting in their home currencies
- Potentially cheaper and more transparent pricing
- Widen client / supplier base
- Overseas importers can buy RMB at a discount in the forward market, a benefit not secured by companies who still purchase goods in USD

**Have surplus RMB or need finance?**

*Corporate investment and finance*
- RMB surplus cash can be invested in a wide range of offshore products: time deposits, certificate of deposits (CDs), Dim Sum bonds, structured deposits, and Exchange-Traded Funds (ETFs)
- RMB trade loans, cross-border lending, and Dim Sum bonds are widely used financing alternatives for corporates

**RMB Opportunity for Growth**

**Trade**
- Chinese customers and suppliers want to do business in RMB, and foreign companies may be able to negotiate better pricing and reduce foreign exchange costs by settling China trade transactions in offshore RMB

**Financing**
- Financing with RMB allows international businesses to have the opportunity to participate in the growth of the Chinese economy

**FX / Risk Management**
- Companies may be able to reduce risks in invoicing and lower transaction costs of trade and investments by hedging foreign exchange in RMB

**Investments**
- RMB denominated financial instruments can provide new avenues to diversify balance sheet cash positions and investment portfolio through offshore and onshore investments
Knowing the Basics

Payments into mainland China

1. **Trade payments for GOODS**
   Mainland enterprises with import and export qualifications can export goods in RMB

2. **Trade payments for SERVICES**
   Allowed

3. **Intragroup RMB cross-border lending**
   Allowed (subject to quota control)

4. **Additional Capital Infusion**
   Allowed (subject to MOFCOM approval)

5. **Foreign Direct Investment**
   Allowed (subject to MOFCOM approval)

6. **Expatriates Salaries**
   Allowed

Payments from mainland China

1. **Trade payments for GOODS**
   Mainland enterprises with import and export qualifications can import goods in RMB

2. **Trade payments for SERVICES**
   Allowed

3. **Intragroup RMB cross-border lending**
   Allowed

4. **Capital investment overseas (ODI)**
   Allowed (subject to MOFCOM approval)

5. **Dividend Payments/Repatriation of Profit**
   Allowed

6. **Expatriates Salaries**
   Allowed

Overseas-to-overseas RMB transactions are not regulated by PBOC, but may be subject to local regulations elsewhere.

MOFCOM stands for Ministry of Commerce in China. SAFE stands for State Administration of Foreign Exchange. Both are regulators in China and manage business registration and foreign currency management respectively.

<table>
<thead>
<tr>
<th>Objective</th>
<th>Cross-border transaction</th>
<th>Documentation required</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade</td>
<td>Importer pays RMB into China</td>
<td>Invoices, sales contract, bill of lading</td>
</tr>
<tr>
<td>Exporter receives RMB from</td>
<td>Exporter receives RMB from China</td>
<td></td>
</tr>
<tr>
<td>importers or intragroup</td>
<td></td>
<td></td>
</tr>
<tr>
<td>affiliates in China</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dividend</td>
<td>MNC receives RMB from China</td>
<td>Board resolution, audited financial reports, tax filing</td>
</tr>
<tr>
<td>Foreign direct investment</td>
<td>MNC pays RMB into China</td>
<td>Approval for direct investment issued by China’s Ministry</td>
</tr>
<tr>
<td>MNC injects capital into China</td>
<td></td>
<td>of Commerce and other regulators / authorities where</td>
</tr>
<tr>
<td></td>
<td></td>
<td>appropriate</td>
</tr>
</tbody>
</table>
Increasing two-way volatility of the currency...
- Policymakers have a broader economic reform agenda, and the RMB will become more market oriented and international.
- Monetary easing and wider capital flow channels should raise the RMB’s volatility.

...Raises the importance of utilising tools to manage risks
- As overseas companies continue to adopt RMB, currency risk management is becoming increasingly important.
- Foreign exchange volatility directly impact earnings.
- FX risk can manifest in a number of ways which often overlap.
- Transaction risks arise where an entity has direct exposure to currencies other than its own, typically via trade or financing. Note that a local currency functional subsidiary model typically focuses these risks at the subsidiaries.
- Translation risks arise at the consolidated level from owning foreign subsidiaries that operate in other currencies.
- Strategic risks arise in situations such as foreign M&A or project bidding. These special situations carry unique FX considerations.

Risk Management Solutions
Managing risk with a more market-driven currency and in a more dynamic environment

HSBC has acquired the China Foreign Exchange Trade System (CFETS) membership for trading of onshore CNY FX spot, forward, swap and options in China’s interbank foreign exchange market in April 2017, becoming one of the banks in Hong Kong to have direct CFETS access.

The CFETS membership allows the bank to help our offshore clients access the onshore China foreign exchange rates directly to settle their RMB transactions without going through agent banks in China or offshore RMB clearing banks. Therefore, we can provide quick time-to-market FX and hedging solutions to clients who have cross-border transaction needs in RMB, such as trade, direct investment and Bond Connect transactions with China.
## RMB Markets: Tailored to Meet Your Needs

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Client Demand</th>
<th>HSBC Global Markets RMB Capabilities</th>
</tr>
</thead>
</table>
| FX          | ✷ FX execution needs driven by transactional, hedging or investment strategy | ✷ Spot FX  
             |                                           | ✷ Deliverable / Non-deliverable FX Forward, FX Option and FX Swap  
             |                                           | ✷ FX-linked structured deposit / note  
             |                                           | ✷ Precious metal trading  
             |                                           | ✷ Global footprint, RMB / China knowledge and deep expertise to provide insights and help to manage your exposure in a manner best aligned with your objectives |
| Rates       | ✷ Debt issuance, financing, risk management and investment needs to access RMB rates market | ✷ Extensive product knowledge in the rates market  
             |                                           | ✷ To help you access liquidity and transact seamlessly  
             |                                           | ✷ A broad range of vanilla and structured interest rates products |
| Fixed Income | ✷ Invest in RMB-denominated fixed-income assets  
              |                                            | ✷ Primary and secondary offshore and onshore bonds trading  
              |                                           | ✷ Innovative ideas on synthetic funding and structured fixed income solutions |
| Equities    | ✷ Invest through Stock Connect  
              |                                            | ✷ Integrated access to A-shares combining trade execution, FX, RMB liquidity and custody services  
              |                                            | ✷ Equity linked structure deposit / note |
|             | ✷ Invest in RMB-denominated equities |                                      |                                           |
Cross-border Trade Settlement in RMB

According to HSBC’s 2017 RMB survey:

42% of businesses currently do not use RMB, but are intending to in the future, increasing from 25% in 2016.

86% of businesses currently using RMB are forecasting an increase in their RMB usage over the coming 12 months.

Top 3 factors driving the use of RMB among current RMB users:

1. Request from trading counterparts to use RMB transactions
2. To get cheaper pricing from our Chinese suppliers
3. Enabler to win more business

As a registered Chinese bank, we can also help you establish and manage operations in China. Furthermore, with RMB cross-border trade now effectively unrestricted, HSBC accounts and documentation support enables businesses to conduct almost all cross-border trade transactions with Chinese companies in RMB.

Customer benefits of RMB cross-border trade settlement:

<table>
<thead>
<tr>
<th>Onshore Importer</th>
<th>Onshore Exporter</th>
<th>Overseas Exporter</th>
<th>Overseas Importer</th>
</tr>
</thead>
<tbody>
<tr>
<td>♦ Natural hedge if the importer is selling in RMB</td>
<td>♦ Avoid losses due to FX</td>
<td>♦ Improve buyer relationship</td>
<td>♦ Improve supplier relationship by paying in their home currency</td>
</tr>
<tr>
<td>♦ Eliminate FX costs which can be significant for small importers</td>
<td>♦ Eliminate FX costs which can be significant for small exporters</td>
<td>♦ Access to an importer base which might otherwise have limited access to FX</td>
<td>♦ Overseas importers may buy RMB at a discount in the forward market, a benefit not secured by companies who still purchase goods in USD</td>
</tr>
<tr>
<td>♦ For documentary trade, Chinese importers might be able to get a longer credit period as RMB letter of credit (LC) is not governed by the short term foreign debt quota for onshore banks</td>
<td>♦ Simplified procedures for export tax rebate (no exchange rate involved)</td>
<td>♦ Overseas exporters can hedge the FX exposure in the offshore RMB market and invest surplus liquidity in a wide range of investment products offshore</td>
<td></td>
</tr>
</tbody>
</table>

Products mentioned are subject to availability.
Solutions to Manage RMB Liquidity

1. **Centralising payments and collections**
   - Client has many entities in China, and payables and receivables transactions are directly managed via an overseas treasury centre who will be paying and receiving on behalf of the entities as well as managing FX.

2. **Liquidity management solutions**
   - This solution involves funds from sub-accounts being physically swept into a concentration account, and vice versa depending on the balance position in the accounts. Cross-border RMB sweeping from China can be done under the intra-group lending scheme.
   - This solution consists of notionally converting all participating balances including RMB into a base currency in order to enhance spreads on both debit and credit balances, up to the extent to which credit balances cover debit balances. Balances held in China are out of the scope due to regulation restrictions.

3. **Net settlement**
   - Client has many entities in China and each settles a high volume of cross-border payables and receivables transactions not denominated in RMB with overseas group entities by centralising all payments and collections via one cross-border payment or receipt after netting all payables and receivables.
   - This solution consists of calculating the notional total balances and rewards by way of an enhancement to the bank interest paid in the event that the total notional balances meets agreed thresholds.
Matching the Clients’ Liquidity Management Needs with the Right Solutions

**Cash rich**
- Offshore
  - Deployed
    - Funding onshore operations
    - Investing onshore/offshore
    - Funding offshore operations
    - Centralisation of liquidity

**Cash short**
- Onshore
  - Deployed
    - Funding onshore operations
    - Lower borrowing cost

**Deployment locations**
- Funding onshore operations
- Investing onshore/offshore
- Funding offshore operations
- Centralisation of liquidity

**Funding location**
- Funding onshore operations
- Lower borrowing cost

**Deployment recipient**
- Internal
- External

1. Entrusted loan to other group companies
2. Onshore money & capital market
3. Offshore financial guarantee (pledge with onshore banks)

**Funding source**
- Internal
- External

1. Dividends
2. Intra-group outbound lending
3. Offshore financial guarantee (pledge with onshore banks)

**Offshore money & capital market**
- Onshore
  - Funding onshore operations
  - Lower borrowing cost

**Offshore borrowing from offshore banks**
- Onshore
  - Funding onshore operations
  - Lower borrowing cost

**Offshore borrowing from offshore group’s entities**
- Internal

**Offshore money & capital market**
- Offshore
  - Funding offshore operations

**Offshore borrowing from offshore banks**
- Offshore
  - Funding offshore operations

**Offshore borrowing from offshore group’s entities**
- Offshore
  - Funding offshore operations

**Manual**
- Cross-border sweeping solution

**Recurring**
- Cross-border sweeping solution
Funding China Operations

HSBC offers full offshore RMB trade financing and loans as well as having the ability to raise bonds in a range of currencies. All working capital, trade and receivables finance can be used outside of China. Bonds and loans raised offshore can be remitted onshore to finance business activities in China, subject to approvals by Chinese authorities. By providing RMB financing, HSBC helps international businesses participate in the growth of the Chinese economy while also enhancing their profiles with Asian investors. In addition to market leading products, HSBC can provide expert assistance in navigating Chinese regulations and requirements.

### Funding China Operations

<table>
<thead>
<tr>
<th>Traditional bank funding</th>
<th>Traditional lending and funding options in China are available including loans and overdrafts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entrusted loan</td>
<td>Onshore entities (entrustor) can lend money to other onshore entities (borrower) by depositing the funds with an agent bank in China, which will in turn lend the fund to the onshore entities. Term of the loan is negotiated between entrustor and borrower and credit risk is not assumed by the bank</td>
</tr>
<tr>
<td>Onshore capital markets</td>
<td>Onshore entities can fund their operations in China by raising capital on the onshore capital markets</td>
</tr>
</tbody>
</table>

### Onshore financing options

As a registered bank in China, HSBC can provide tailored onshore financing. This can take the form of traditional bank funding, automated sweeps, entrusted loans or fund raising from the onshore capital market.

### Panda bond market

Issuing Panda bonds allow offshore borrowers to tap into the largest investor base in China's bond market, opening up another source of funding for their onshore subsidiaries. Although issuance volume has been hindered by the elevated onshore bond yields and capital control in 2017, with RMB71 billion bond issued in 2017 (down 44% y-o-y), further liberalisation is expected to attract more foreign investors to stimulate the growth of the Panda bond market.
Funding China Operations (cont.)

Offshore funding options

Companies funding for their operations in China can be made via offshore borrowing. These payments into China typically require case-by-case approval from or filing with Chinese authorities. This is the responsibility of the Chinese entity, which should approach the local office of the relevant Chinese agency in the first instance.

<table>
<thead>
<tr>
<th>Offshore RMB borrowing</th>
<th>Onshore entities can borrow directly from offshore banks and remit the necessary capital funds to China. Alternatively, onshore entities can also borrow from its overseas affiliates via inter-company lending, enabling better liquidity management by fund sweeping between onshore and offshore entities manually or automatically</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMB synthetic loan</td>
<td>US-denominated loan, the principal of which is swapped into RMB and then transferred to the onshore subsidiary via an inter-company loan</td>
</tr>
<tr>
<td>RMB capital injection</td>
<td>Injection of capital into a new entity setup or existing entity in China</td>
</tr>
<tr>
<td>Dim Sum bond issuance</td>
<td>A RMB-denominated bond sold in offshore markets</td>
</tr>
<tr>
<td>RMB IPO / Hong Kong follow-on offering</td>
<td>A RMB-denominated equity sold in offshore markets</td>
</tr>
</tbody>
</table>

Dim Sum Bond Market

In 2017, Dim Sum bond issuance volume was RMB87 billion, down 51% y-o-y, as issuers moved to the onshore market to leverage potentially lower financing rates. As an active underwriter and lead manager in the offshore Dim Sum market, HSBC was ranked first in the league table of lead managers by Bloomberg as of December 2017.
Managing Surplus Liquidity

Investing Onshore

HSBC can help companies make the most of surplus cash generated from operations in China with an onshore RMB fund which can potentially offer attractive returns. This is combined with the ability to tailor allocations to meet different liquidity and operating requirements.

With the dynamic regulatory landscape in China, HSBC can act as a guide to help companies navigate the constantly changing environment.

<table>
<thead>
<tr>
<th>Dividend payments</th>
<th>Designed for companies with Chinese ownership that want to repatriate surplus funds overseas to shareholders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Offshore financial guarantee</td>
<td>The Chinese entity deposits its surplus of liquidity with HSBC China as a pledge in order to provide a loan to the overseas entity</td>
</tr>
<tr>
<td>Intra-group outbound lending</td>
<td>The Chinese locally-incorporated enterprises remit RMB funds offshore as an inter-company loan to their entities overseas</td>
</tr>
<tr>
<td>Money Market funds in China</td>
<td>Designed for companies with operations in mainland China. The investing entity must have an onshore legal entity incorporated in China</td>
</tr>
</tbody>
</table>

Deploying RMB Offshore

**Offshore RMB investment products at a glance**

<table>
<thead>
<tr>
<th>Certificates of deposit</th>
<th>Issuers tend to be offshore branches of mainland banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonds</td>
<td>The range of issuers has expanded from sovereigns (Ministry of Finance of China) and banks in mainland China to financial and non-financial companies from different parts of the world</td>
</tr>
<tr>
<td>Structured notes</td>
<td>Typically linked to an underlying index that ranges from currency, interest rate, equity, or gold</td>
</tr>
<tr>
<td>Insurance products</td>
<td>Allowing overseas insurance companies to invest in China’s Interbank Bond Market (CIBM) increases insurance companies’ ability to pay higher interest rates</td>
</tr>
<tr>
<td>Investment funds</td>
<td>Offshore funds can offer access to onshore markets through QFII, RQFII and the various “connect” programmes. Offshore investors can also access onshore funds through the mainland-Hong Kong Mutual Recognition of Funds</td>
</tr>
<tr>
<td>Equity products</td>
<td>RMB-denominated equity products have been listed in Hong Kong</td>
</tr>
<tr>
<td>Exchange-traded funds</td>
<td>Unlike synthetic ETFs that invest in derivative instruments, RQFII A-share ETFs give offshore investors direct exposure to A-shares</td>
</tr>
</tbody>
</table>
Accessing China’s Capital Markets

For institutional investors, HSBC can help them access the world’s second largest stock market and third largest bond market\(^1\), which are gradually opening up to foreign investors. Development of China’s capital markets has made significant progress with recent examples including the launch of various Stock / Bond Connect programmes and opening of the Chinese Interbank Bond Market (CIBM) to a wider range of international investors. Inclusion of China A-shares into MSCI indices and potential inclusion of the CIBM into Global Bond indices also signify the gradual international recognition of China’s capital markets. With more developments in the pipeline, China’s financial markets will continue to transform and adapt to the requirements of its growing economy.

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1 Shenzhen Stock Exchange, Shanghai Stock Exchange as of 31 August 2017 and Asian Development Bank as of 30 September 2017
Key Differences of the Various Platforms

<table>
<thead>
<tr>
<th>QFII</th>
<th>RQFII</th>
<th>Stock Connects</th>
<th>CIBM direct access</th>
<th>Bond Connect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Who’s eligible?</td>
<td>Asset managers</td>
<td>Qualified financial institutions registered and having its principal place of business in the approved RQFII sites with asset management license issued by the competent local securities regulator and have already conducted relevant asset management business</td>
<td>All Hong Kong and overseas institutional and individual investors</td>
<td>Non-sovereign entities:</td>
</tr>
<tr>
<td></td>
<td>Insurance companies</td>
<td></td>
<td>Shares listed on the ChiNext Board of the Shenzhen Stock Exchange will be available only to institutional professional investors</td>
<td>-- Fls including commercial banks, insurance, securities companies, asset managers</td>
</tr>
<tr>
<td></td>
<td>Securities companies</td>
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<td>-- Products launched by the aforesaid institutions</td>
</tr>
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<td></td>
<td>Commercial banks</td>
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<td></td>
<td>-- Others mid/long term investors</td>
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<td>Others types</td>
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<tr>
<td>What can be invested?</td>
<td>Exchange-traded or transferred A-shares, bonds and warrants</td>
<td>Shanghai Stock Exchange (SSE) Equities (SSE180 and SSE380 constituent stocks, dual listed A&amp;BH-shares)</td>
<td>Cash bond³</td>
<td>Cash bond³</td>
</tr>
<tr>
<td></td>
<td>Fixed income products traded in the CIBM</td>
<td>Shenzhen Stock Exchange (SZSE) Equities (Constituents of SZSE Component &amp; SZSE Small/Mid Cap Innovation indexes with a market capitalisation of at least RMB6 billion, and SZSE-SEHK A+H shares)</td>
<td>Repo⁴</td>
<td>Repo</td>
</tr>
<tr>
<td></td>
<td>Securities investment funds</td>
<td></td>
<td>Bond IPO</td>
<td>Bond IPO</td>
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<td></td>
<td>Equity index futures</td>
<td></td>
<td>Bond lending &amp; borrowing (solely for hedging purpose)</td>
<td>Bond lending &amp; borrowing</td>
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<tr>
<td></td>
<td>Subscription to IPO, additional issuance, rights issues and convertible bond issuance</td>
<td></td>
<td>Bond forward, Forward Rate Agreement (FRA), Interest Rate Swap (IRS) (for hedging purpose only)</td>
<td>Bond forward, IRS, FRA, etc.</td>
</tr>
<tr>
<td></td>
<td>Other instrument approved by CSRC</td>
<td></td>
<td>Interbank Deposits</td>
<td>Interbank Deposits</td>
</tr>
</tbody>
</table>

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1 Fulfilling CSRC track record, operational and AUM requirements, including but not limited to pension funds, charity funds, endowment funds, trusts, government investment institutions

2 Fulfilling the requirements set out by the PBOC

3 PBOC verbally clarified that cash bond includes ABS, Panda Bond and other eligible cash bond products traded in CIBM on 9-10APR16

4 For overseas RMB clearing banks and participating banks repo is allowed to be traded
# Key Differences of the Various Platforms (cont.)

<table>
<thead>
<tr>
<th></th>
<th>QFII</th>
<th>RQFII</th>
<th>Stock Connects</th>
<th>CIBM direct access</th>
<th>Bond Connect</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Key features</strong></td>
<td>– Broader range of products are available</td>
<td>– Primary market participation is possible</td>
<td>– No lock up period</td>
<td>– No lock up period</td>
<td>– No lock up period</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>– Wider range of hedging tools are available</td>
<td>– Hedging are conducted offshore</td>
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<td></td>
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<td></td>
<td>– Trades are conducted through offshore</td>
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<td></td>
<td></td>
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<td>electronic trading platform linking</td>
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<td></td>
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<td>to the onshore system</td>
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<tr>
<td></td>
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<td></td>
<td>– Bonds are kept in custodian accounts in</td>
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<td></td>
<td>Hong Kong</td>
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</tbody>
</table>
Allocating to China

A sizeable market, underappreciated by global investors
China’s USD8.3 trillion¹ onshore equity market and USD8.2 trillion² bond market are the second and third largest of their kind in the world. However, they are both acutely underrepresented in major international indices, partly explaining the negligible foreign participation in these markets. This looks set to change as China continues to open up its capital markets, most recently with the launch of the Stock Connect and the Bond Connect schemes. These developments in turn will enable a greater degree of inclusion in widely-tracked global indices, and drive significant fund flows into Chinese asset markets.

Why invest in onshore assets for exposure to China?

RMB bonds
China: The third largest bond market globally

Market size: USD8.2 trillion

- Higher yields when compared with bonds from markets of a similar size or credit rating
- Deeper and broader market when compared with offshore bonds
- Pricing differentiation (which is currently very limited) to become more pronounced between low and high quality bonds as the market continues to evolve.

China A-shares
China has a disproportionally small representation in MSCI ACWI

Foreign participation: 3%
Potential capital inflow upon full index inclusion: USD155 billion

- Strong upside potential on the back of strengthening economy and improving corporate profitability
- A-share market offers access to investment opportunities in new economy sectors, such as technology, healthcare and e-commerce, that are powering the next phase of China’s growth story
- Major beneficiary of China’s reform agenda and global growth recovery
- Moreover, both China A-shares and onshore RMB bonds are great candidates for portfolio diversification given their relatively low correlation with peers in other markets.

Why active management for RMB assets?
While gaining access to Chinese asset markets has become a relatively painless process, picking the right investments still remains somewhat challenging for international investors because of the unique features that characterise Chinese equities and bonds. For example – the A-share market is largely retail driven, which makes it more prone to valuation dispersions and mispricing of stocks. As for RMB bonds, 99% of onshore bonds are rated AA and/or above by local credit rating agencies, suggesting that there is little differentiation between different quality issuers in that market at present.

The opening up of onshore markets has certainly presented investors with interesting opportunities, however, current investor exposure is low and knowledge of Chinese asset classes is still limited. Asset managers with experience in Chinese equity and fixed income investing, who can combine a robust investment framework with a rigorous credit selection process, are the necessary bridge for international investors who wish to enter this exciting and complex market.

Why HSBC Global Asset Management for investing in China?

<table>
<thead>
<tr>
<th>Why HSBC Global Asset Management for investing in China?</th>
<th>Why active management for RMB assets?</th>
</tr>
</thead>
<tbody>
<tr>
<td>A leading international asset manager with USD461.5 billion in assets under management and 2,200 employees³ – including around 80 investment professionals³ based in Hong Kong and China who focus on Chinese asset markets</td>
<td>While gaining access to Chinese asset markets has become a relatively painless process, picking the right investments still remains somewhat challenging for international investors because of the unique features that characterise Chinese equities and bonds. For example – the A-share market is largely retail driven, which makes it more prone to valuation dispersions and mispricing of stocks. As for RMB bonds, 99% of onshore bonds are rated AA and/or above by local credit rating agencies, suggesting that there is little differentiation between different quality issuers in that market at present.</td>
</tr>
<tr>
<td>Best use of global resources and local insights, by leveraging on-the-ground expertise from HSBC Jintrust, our Shanghai-based joint venture</td>
<td>The opening up of onshore markets has certainly presented investors with interesting opportunities, however, current investor exposure is low and knowledge of Chinese asset classes is still limited. Asset managers with experience in Chinese equity and fixed income investing, who can combine a robust investment framework with a rigorous credit selection process, are the necessary bridge for international investors who wish to enter this exciting and complex market.</td>
</tr>
<tr>
<td>Comprehensive suite of China investment capabilities including onshore and offshore equities, fixed income, multi-asset and liquidity solutions</td>
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<tr>
<td>Employing a clear investment philosophy and a disciplined, repeatable process built on solid proprietary research</td>
<td></td>
</tr>
<tr>
<td>Over 25 years of experience in managing Chinese assets for clients; Manager of HGIF Chinese Equity, one of the oldest and largest offshore Chinese equity funds</td>
<td></td>
</tr>
<tr>
<td>Robust risk management process that optimises returns in volatile markets while maintaining a diversified portfolio</td>
<td></td>
</tr>
</tbody>
</table>

3 HSBC Global Asset Management as of 30 September 2017
Awards

HSBC has won Best Overall International Bank for Belt and Road Initiative (BRI) in the inaugural Asiamoney New Silk Road Finance Awards, as well as:

- Best Bank for BRI-Related Infrastructure Finance in Southeast Asia
- Best Bank for BRI-Related Infrastructure Finance in South Asia
- Best Bank for BRI-Related Finance in Central & Eastern Europe
- Best International Bank for BRI in the Middle East & Africa

One of the largest global RMB networks with established RMB capabilities (in terms of trade settlement and payments) across 50 markets
- Ranked 1st in the offshore RMB bond underwriting league table since 2011
- Leading RQFII custodian bank, with over 53% market share; ranked 1st in all active RQFII markets (December 2017)
- At the forefront of developments in China’s FTZs – 1st batch of banks to complete an RMB cross-border settlement transaction for individuals in the Shanghai FTZ

“HSBC has a wide margin on the competition across product lines, as shown once again in this year’s Asiamoney offshore renminbi survey”
Asiamoney 2017.

Finance Asia 2017
“Best Bank in Hong Kong”
“Best Foreign Bank in China”

EuroMoney 2017
“World’s Best Bank”
“Asia’s Best Bank”

Risk Awards 2017
“Currency Derivatives House of the Year”
“Inflation Derivatives House of the Year”

Trading and Forfaiting Review Awards for Excellence 2017
“Best Trade Bank in the World”
“Best Trade Bank in Asia”
“Best Trade Bank for Innovation”
“Best Trade Bank for SMEs”

Global Capital Bond Awards 2017
“Best Corporate Bond Bank for Creative and Useful Funding Ideas”
“FIG Bond House of the Year”
“Best SSA Bond Bank for Sales Expertise”

Global Capital Bond Awards 2017
“Best Corporate Bond Bank for Creative and Useful Funding Ideas”
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N. Aronsen, F. Perse, “At the forefront of developments in China’s FTZs – 1st batch of banks to complete an RMB cross-border settlement transaction for individuals in the Shanghai FTZ”

N. Aronsen, F. Perse, “At the forefront of developments in China’s FTZs – 1st batch of banks to complete an RMB cross-border settlement transaction for individuals in the Shanghai FTZ”
HSBC is one of the world’s largest financial services organisations with a vast global network

- c3,900 offices in 67 countries and territories worldwide
- RMB capabilities across 50 markets
- 1st bank with capability to settle RMB in six continents
- HSBC has 25 China Desks with dedicated China specialists across the Group

HSBC in China

HSBC China has over 170 outlets covering 57 cities and 23 provinces/municipalities, the largest network among all foreign banks in mainland China
### Glossary

<table>
<thead>
<tr>
<th>Term</th>
<th>Description</th>
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<tbody>
<tr>
<td>Bond Connect</td>
<td>Bond Connect is a mutual market access scheme that allows investors from Mainland China and overseas to trade in each other’s bond markets. Northbound trading has been commenced in July 2017, allowing overseas investors to invest in the China Interbank Bond Market through mutual access arrangements in relation to trading, custody and settlement. Southbound Trading will be explored at a later stage.</td>
</tr>
<tr>
<td>CBRC – China Banking Regulatory Commission</td>
<td>Formulates supervisory rules and regulations governing the banking institutions; authorises market entry, business scope, changes and termination of banking institutions.</td>
</tr>
<tr>
<td>CIBM – China Interbank Bond Market</td>
<td>The third largest bond market in the world after the US and Japan with government and quasi-government bonds heavily dominating issuances.</td>
</tr>
<tr>
<td>CIPS – Cross-border interbank payment system</td>
<td>A RMB payment infrastructure similar to SWIFT that facilitates cross-border clearing of RMB.</td>
</tr>
<tr>
<td>CNH</td>
<td>RMB traded outside of mainland China.</td>
</tr>
<tr>
<td>CNY</td>
<td>Onshore RMB market. Also the International Organization for Standardisation currency code for RMB regardless of whether traded in the onshore and offshore markets.</td>
</tr>
<tr>
<td>Dim Sum bond</td>
<td>RMB-denominated bonds sold in Hong Kong.</td>
</tr>
<tr>
<td>FDI – Foreign Direct Investment</td>
<td>An investment made by a company or individual in one country in business interests in another country, in the form of either establishing business operations or acquiring business assets in the other country, such as ownership or controlling interest in a foreign company.</td>
</tr>
<tr>
<td>FTZ – Free Trade Zone</td>
<td>An area designated by the government for institutional reform, liberalisation, and innovation in investment, foreign trade, finance, and post-filing supervision. The first FTZ was established in Shanghai in September 2013 as a pilot project, it introduced free market reforms to ease financial, currency restriction, and administrative control burdens. There is a total of 11 FTZs now.</td>
</tr>
<tr>
<td>ODI – Outward Direct Investment</td>
<td>Opposite to FDI, a domestic firm expands its operations to a foreign country.</td>
</tr>
</tbody>
</table>
### Glossary continued

| **PBOC – People’s Bank of China** | The central bank in China, formulates and implements monetary policies; regulate interbank markets and mitigate systematic financial risks; maintains financial services infrastructures like payment, FX, bond etc.; prevents financial crimes. |
| **Panda bond** | RMB-denominated bonds issued by non-Chinese issuers in mainland China. |
| **QDII – Qualified Domestic Institutional Investor** | An institutional investor in mainland China that has met certain qualifications to invest in securities outside of the country. |
| **QFII – Qualified Foreign Institutional Investor** | A programme that permits licensed foreign investors to invest directly in mainland China’s bond and equity markets. |
| **RMB – Renminbi** | “The people’s currency” in Chinese. The official name of the currency. It is also referred to as “Yuan”. |
| **RQFII – RMB Qualified Foreign Institutional Investor** | A programme that permits licensed foreign investors to invest directly in mainland China’s bond and equity markets in RMB. |
| **SAFE – State Administration of Foreign Exchange** | Supervises foreign exchange market and implement regulations related to foreign exchanges and cross-border capital flow. |
| **SDR – Special Drawing Right** | The RMB joined the Intentional Monetary Fund’s Special Drawing Right basket on Oct 1, 2016. The SDR is an international reserve asset created by the IMF in 1969 to supplement its member countries’ official reserves. |
| **SHIBOR – Shanghai Interbank Offered Rate** | The Shibor is the benchmark interest rate of China’s money market, which has been calculated and announced by the China Foreign Exchange Trade System under the authorisation of the PBOC since January 4, 2007. |
| **Shanghai-Hong Kong or Shenzhen-Hong Kong Stock Connect** | Programmes that establish access between the two markets. It allows international investors to trade in a number of shares listed in Shanghai or Shenzhen without having to apply for individual licenses and quotas, and for domestic Chinese investors to trade in some Hong Kong stocks. |
Renminbi (RMB) is currently not freely convertible and conversion of RMB through banks in Hong Kong is subject to certain restrictions. Clients should be reminded of conversion risk in RMB products. In addition, there is a liquidity risk associated with RMB products, especially if such investments do not have an active secondary market and their prices have large bid/offer spreads. RMB products in Hong Kong are denominated and settled in RMB deliverable in Hong Kong, which represents a market which is different from that from that of RMB deliverable in mainland China. For individual clients, conversion of RMB is subject to daily limit in Hong Kong, the clients may have to allow time for conversion of RMB from/to another currency of an amount exceeding the daily limit. Please refer to the offering documents of the respective RMB products for details, including risk factors.

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