

What Future for the Hong Kong Dollar Corporate Bond Market?

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Summary

There have been persistent calls for development of bond markets in Asia. But most of the urging has come from officials or academics. The distinctive approach of this study, which focuses mainly on prospects for the corporate bond market in Hong Kong, has been to elicit, mostly through a series of interviews, the opinions of the actual or prospective end-users of the market, or those representing their interests, since, without the corporate issuers and the ultimate investors, the market could not be expected to mature further.

The study finds that the market lacks sufficient mass to generate the liquidity, fine pricing and narrow spreads observable in, say, the US market. However, it is in all other respects efficient. There is little evidence of unsatisfied demand to issue corporate bonds or to invest in them. This reflects the limited population of companies which could, given size, credit standing, costs, etc, realistically aspire to issue; the limited investor appetite for such paper; and the competing attractions of the US dollar market for both sides.

A comparison of the characteristics of bank finance and the bond market suggests that the purported advantages of the latter in providing a 'spare tyre' for times of crisis may be exaggerated. In particular, many of those who have argued, notably since the 1997 Asian financial crisis, for action to develop the corporate bond market, have seemingly failed to appreciate that only a minority of firms can realistically expect to access the market, and that the market itself, especially at sub-investment grade, can, if existing at all, be extremely capricious.

In view of these findings, it seems that there need be no great concern over the oft-remarked underdevelopment of the Hong Kong dollar corporate bond market. Meanwhile, regardless of how that market segment fares, Hong Kong institutions should continue to contribute value added to the economy through the arrangement, distribution, etc of bond issues more generally, and should, in particular, be well placed for involvement in renminbi bond business, once that is permitted to develop further.

¹ This paper was finalised in May.