

# **Chinese Local Bond Spreads, Monetary Policy and “Misallocation”**

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## **Summary**

We examine the impact of Chinese monetary policies on excess local bond yields (the spreads over Chinese government bonds), on local bonds issued by Chinese local government entities. We find that an expansion in M2 generally raises the excess yields on bonds issued by local government entities, and the impact is amplified for bonds issued by the local governments. This last category is considered as having a high degree of existing resource misallocation. Our estimation results confirm that excess yield on local bonds can be an indicator of market risk of local government debts and the financial efficiency of local governments.