Outlook for China dollar bonds in 2025

February 2025

Haidan Zhong
Head of Client Portfolio Management,
Invesco Fixed Income

Anthony Xiao
Associate Portfolio Manager,
Invesco Fixed Income

Key takeaways

- China dollar bonds are of higher credit quality than in 2020 given the elimination of low-quality real estate bonds from the bond universe.
- We believe China dollar bonds currently present an attractive value proposition for four main reasons, namely access to high-quality issuers, higher yields compared to onshore bonds, lower volatility, and strong technicals.
- We believe China dollar bond issuers that have higher ESG ratings than peers are better positioned to achieve excess returns.

The current universe of China dollar bonds is of higher credit quality than in 2020
Since the Chinese property sector crisis sparked by the default of Evergrande Group in 2021 and the subsequent elimination of low-quality real estate bonds from the China dollar bond universe, the bond universe is now of higher credit quality than before. The 1-year volatility of the JP Morgan JACI China & Hong Kong Total Return Index was at 2.65% in 2024, 1% lower than in 2020 (Figure 1).

In terms of sector composition of the China dollar bond universe, the real estate sector experienced the largest decrease in percentage market capitalization over the four-year period, dropping from 25% to 8%, while the financial sector saw the highest increase, rising from 26% to 40% (Figure 2).

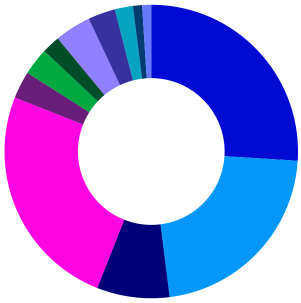
Figure 1 – Comparison of China and Hong Kong dollar bonds in 2020 and 2024 by key metrics

China and Hong Kong dollar bonds[1]	Market Cap (USDm)	Percentage of IG Bonds (%)	Average Spread	Average Duration	1-Year Volatility (%)
31 Dec 2020	704,777	74.92	357.38	3.81	3.64
31 Dec 2024	416,833	87.91	290.60	3.79	2.65

Source: J.P. Morgan Index Research, Bloomberg, as of December 31, 2024. J.P. Morgan Asia Credit Index (JACI) China and Hong Kong components are used to represent the China and Hong Kong dollar bonds. The data presented in this table serves as a representative portfolio of the China and Hong Kong dollar bond market.[1] Blended Spreads JACI China and Hong Kong components are used for Average Spread calculation. EIR Durations for JACI China and Hong Kong components are used for Average Duration Calculation. JACICNHK Index is used for 1-Year Volatility calculation.

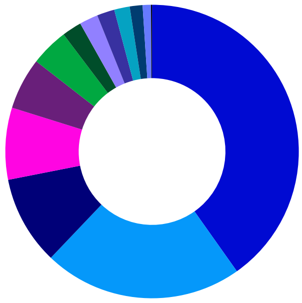
Figure 2 – Sectoral comparison of China and Hong Kong dollar bond universe from 2020 and 2024 by market cap

31 December 2020



	%
Financial	26
Quasi-Sov	22
TMT	8
Real Estate	25
Sovereign	3
Diversified	3
Utilities	2
Oil & Gas	4
Infrastructure	3
Industrial	2
Transport	1
Consumer	1
Metals & Mining	0

31 December 2024



	%
Financial	40
Quasi-Sov	22
TMT	10
Real Estate	8
Sovereign	6
Diversified	4
Utilities	2
Oil & Gas	2
Infrastructure	2
Industrial	2
Transport	1
Consumer	1
Metals & Mining	0

Data source: J.P. Morgan Index Research, Bloomberg, as of December 31, 2024. J.P. Morgan Asia Credit Index (JACI) China and Hong Kong components are used to represent the China and Hong Kong dollar bonds. The data presented in these charts serve as a representative portfolio of the China and Hong Kong dollar bond market.

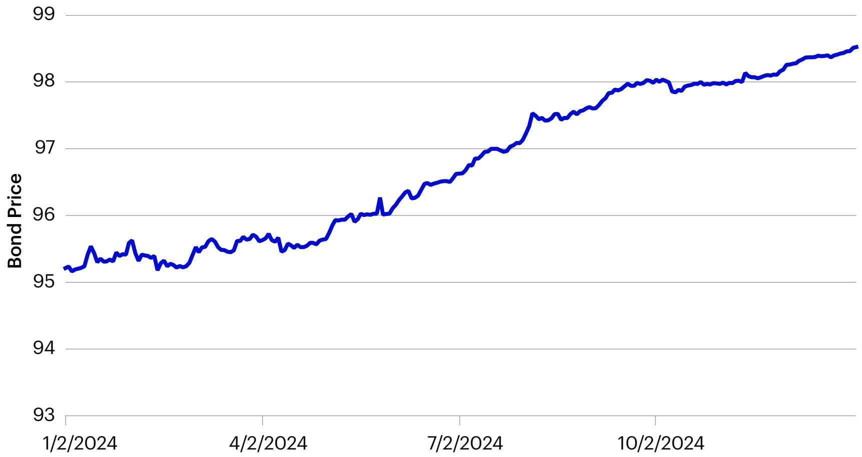
We believe China dollar bonds currently present an attractive value proposition

In our view, China dollar bonds currently present an attractive value proposition for both local and international investors for four main reasons.

1. **Investors can access high quality corporate issuers that do not issue public corporate bonds onshore**
   First, offshore USD bonds allow investors to access high quality Chinese corporate issuers that do not issue public corporate bonds onshore. Based on our observation, many high quality Chinese corporate issuers, especially private-owned entities, typically only tap the short-term commercial paper and the asset-backed securities (ABS) market for financing. As such, the offshore USD bonds create a valuable diversification option for these issuers. We outline two issuers with these characteristics in the below examples.

   - **Example: A leading Chinese dairy manufacturer**
     The first example of a bond in this universe is that of a leading Chinese manufacturing and distribution company of dairy products and ice cream, founded 30 years ago. The company is a listed on the Hong Kong stock exchange and is a component of the Hang Seng Index (HSI). While the firm does not have any outstanding corporate bonds in the domestic RMB bond market, it issued a USD bond in June 2020, with maturity date of June 17, 2025. It is rated Baa1 by Moody's. The bond offers a yield to maturity of 5.2% as of December 31st, 2024. [1] Due to the high quality and scarcity, the performance of the bond has been quite stable over time.

Figure 3 – Bond price trajectory of leading Chinese dairy manufacturer

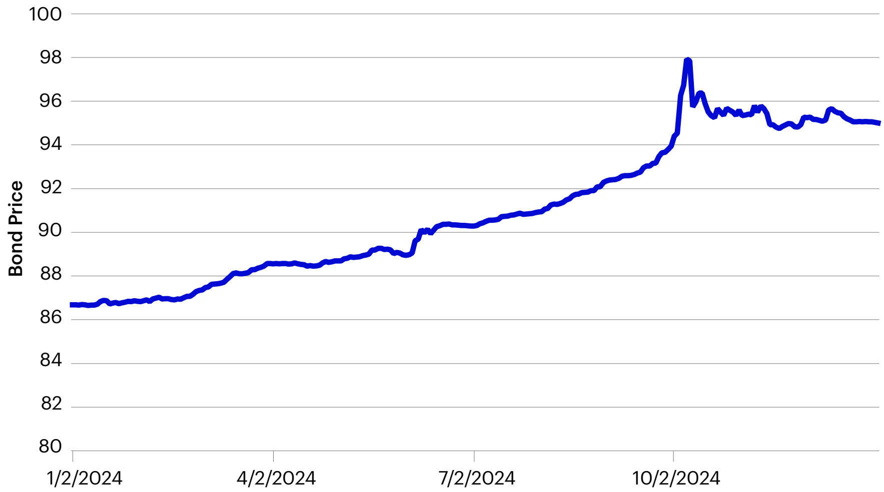


Source: Bloomberg, as of December 31, 2024.

1. Bloomberg, data as of December 9, 2024.

- **Example: One of the largest Chinese shopping platform companies for locally founded consumer products and services**
  The second example is of one of China's largest shopping platform companies for locally founded consumer products and services, including entertainment, dining, delivery and travel. This company leads the Chinese market for online food delivery and had a market share of 67.3% in 2024. [2] It is also listed on the Hong Kong stock exchange and is a component of HSI. The firm, which doesn't have outstanding corporate bonds in domestic RMB bond market, issued a convertible bond in April 2021, with a coupon rate of 0% and a maturity date of April 27, 2028. The bond, which holds an international rating of Baa2 from Moody's, offers a yield to maturity of 4.9% as of December 31st, 2024. [3] The convertible feature also provides additional return upside for the security.

Figure 4 – Bond price trajectory of one of China's largest shopping platform companies



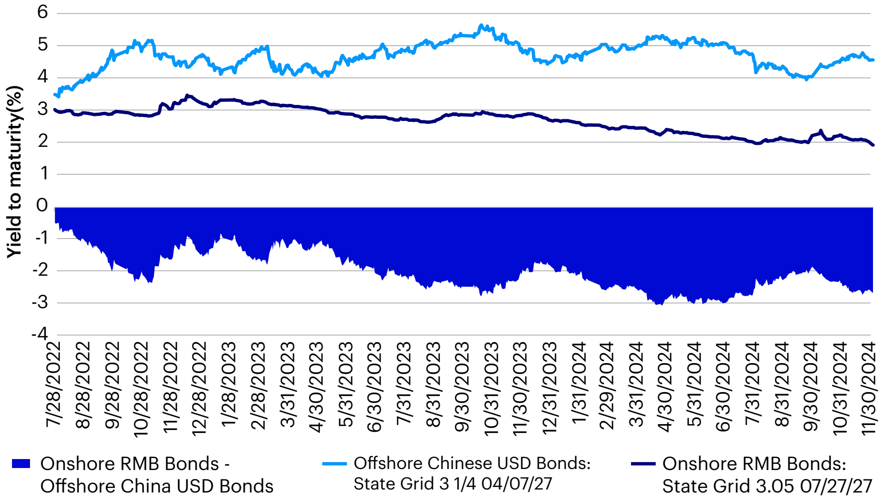
Source: Bloomberg, as of December 31, 2024.

2. Higher yield from China offshore dollar bonds than onshore bonds for the same issuers
China offshore dollar bonds could also have a higher yield than onshore bonds for the same issuer in question. In the context of relatively high global interest rates, we outline two issuer examples where the yield on offshore dollar bonds issued by Chinese issuers is higher than that of onshore RMB bonds.

- **Example: Higher yield of China's state-owned electric utility provider's onshore RMB bonds versus offshore USD bonds**
  The first issuer example we consider is of China's state-owned electric utility corporation and the largest utility provider in the world. As of March 2024, this company was the world's third largest by revenue. Major rating agencies such as S&P and Moody's have rated the company A+/A1. For this high-quality issuer, offshore dollar bonds offer a higher yield to maturity compared to onshore RMB bonds. This allows investors to access the same issuer while achieving greater yield.

2. ResearchGate, Bloomberg, data as of December 31, 2024.
3. Bloomberg, data as of December 9, 2024.

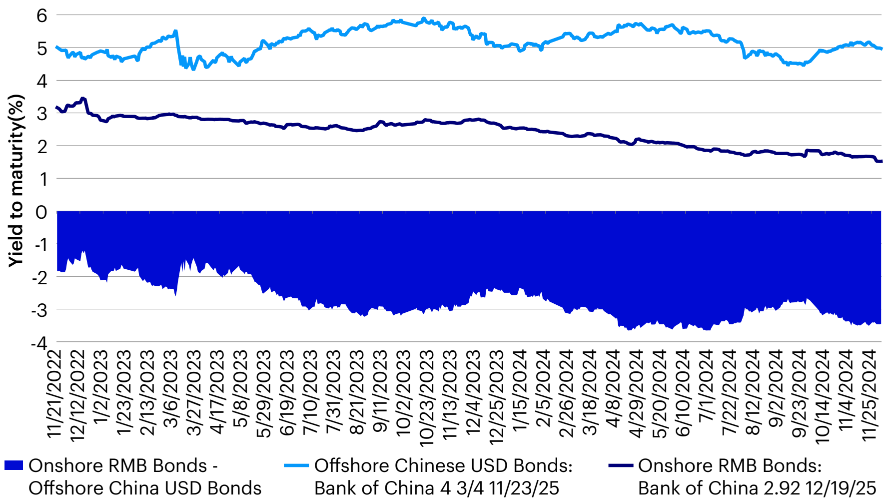
Figure 5 – Yield comparison of onshore RMB and offshore USD bonds of China's state-owned electric utility corporation



Source: Bloomberg, Wind, as of December 3, 2024.

- **Example: Higher yield of one of China's "Big Four" banks' onshore RMB bonds versus offshore USD bonds**
  Another issuer example is that of a Chinese state-owned multinational bank headquartered in Beijing (one of the "Big Four") that is also the fourth largest bank globally by total assets. The company is listed on both the A-share and H-share markets and is a constituent of the SSE 50 Index (A-shares) and the Hang Seng Index (H-shares). This issuer is rated A1 from the Moody's and A from S&P and Fitch. Like the earlier example, their offshore dollar bonds offer a higher yield compared to onshore RMB bonds.

Figure 6 – Yield comparison of onshore RMB and offshore USD bonds of one of China's "Big Four" banks



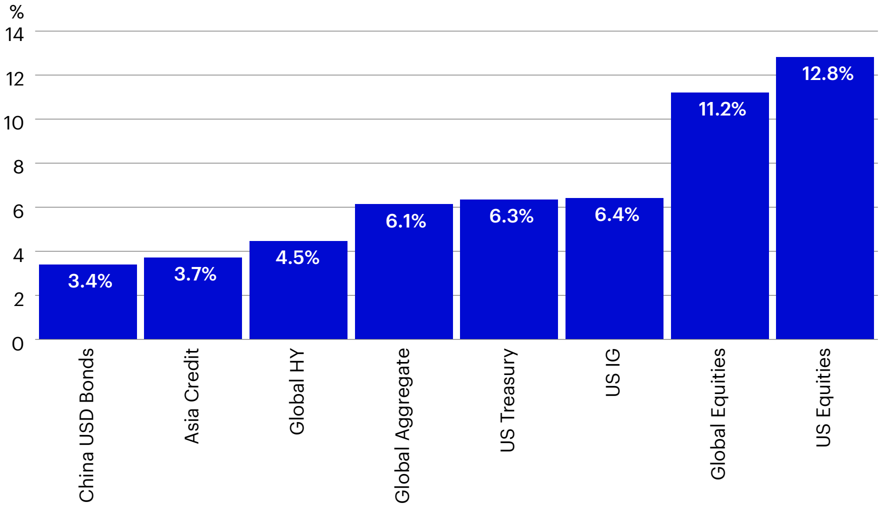
Source: Bloomberg, Wind, as of December 3, 2024.

4. PBoC, Invesco calculation, data as of 30 November 2024.
5. J.P.Morgan, data as of 30 November 2024.

3. China dollar bonds have lower volatility as compared to other fixed income asset classes

Over the past two years, the volatility of China dollar bonds has been the lowest among various major fixed income asset classes, including global aggregate, US treasuries, and US investment grade (IG) bonds (Figure 7). From the end of 2022 to the end of 2024, China dollar bonds had a volatility of 3.4%, which is even lower than that of the commonly used risk-free benchmark, US treasury bonds (6.3%). Both duration and strong technical support positively contributed to the relative performance.

Figure 7 - 2-year volatility comparisons across various fixed income asset classes



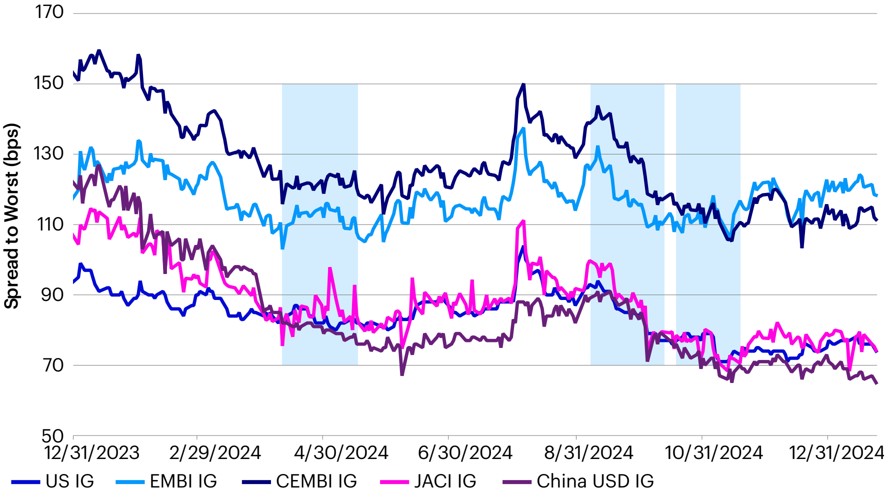
Source: Bloomberg, JP Morgan, data as of 31 December 2024, daily frequency. China USD Bonds is represented by J.P. Morgan JACI China & Hong Kong Total Return Index. Asia credit is represented by J. P. Morgan Asia Credit Index. Global HY is represented by Bloomberg Global High Yield Total Return Index. Global Aggregate is represented by Bloomberg Global Aggregate Total Return Index. US Treasury is represented by ICE BofA US Treasury Index. US IG is represented by S&P 500 Investment Grade Corporate Bond Total Return Index. Global Equities is represented by MSCI World Index. US Equities is represented by S&P 500 Index.

4. China dollar bonds are supported by strong technicals

Strong technical factors have recently supported Asian credit and China dollar credit market performance, which we expect to continue in the year ahead. Local demand, especially from Asian banks, has been a key driver behind the strong performance of Asian investment grade bonds. Chinese banks increased their foreign currency bond investment on a net basis by USD 33 billion in the first 11 months of 2024. [4] On the other hand, net redemption (as bonds mature and are repaid by issuers) in Asia has averaged around USD 40 to 80 billion annually. [5] With global investors' allocation to Asian bonds currently at low levels, we expect the Asian credit market to remain well supported by favorable supply-demand dynamics.

Specifically, China dollar IG bonds benefit from strong technical factors, as evidenced by their spread performance when compared to peers. During periods of selloffs and spread hikes, China dollar IG bonds demonstrate relative stability and exhibit less volatility relative to peers.

Figure 8 – Spread performance of China dollar bonds relative to other investment grade bonds



Source: Bloomberg, as of 23 January 2025. China USD IG is represented by ICE BofA Asian Dollar Investment Grade Corporate China Issuers Index. US IG is represented by Bloomberg US Aggregate Credit Average OAS. EMBI IG is represented by J.P. Morgan - EMBIG Diversified IG Spread to Worst. CEMBI IG is represented by J.P. Morgan CEMBI Broad Div High Grade Spread to Worst. JACI IG is represented by J.P. Morgan JACI Investment Grade Strip Spread to Worst (%).

Growing importance of sustainable investing when evaluating China dollar bonds

As outlined in the earlier section, China dollar bonds present an attractive value proposition given the relative stability of these instruments and strong technical support. As global sustainability trends drive a shift in investment strategies towards more sustainable approaches, ESG has become an important topic within China bond investing. Evidence shows that despite some investors' concerns about potentially lower returns, sustainable investing can enhance risk-adjusted returns in China fixed income strategies. China dollar bond investors can therefore consider incorporating sustainable investing concepts into their portfolios.

Conclusion

China dollar bonds have shown resilience despite the market turmoil in the property sector in 2020. The bond universe has evolved since then and is currently of higher credit quality than before. We believe this asset class currently presents an attractive investment opportunity for investors. We are positive on China dollar bonds as they could provide investors with access to high-quality issuers and could offer higher yields compared to onshore bonds, alongside lower volatility and strong technicals.

Outlook for China dollar bonds in 2025

February 2025

Investment risks
The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

When investing in less developed countries, you should be prepared to accept significantly large fluctuations in value.

Investment in certain securities listed in China can involve significant regulatory constraints that may affect liquidity and/or investment performance.

Important information
This document is for Professional Clients only in Dubai, Jersey, Guernsey, the Isle of Man, Continental Europe (as defined below) and the UK; for Institutional Investors only in the United States; for Professional/Qualified/Sophisticated Investors in Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates; for Qualified Clients/Sophisticated Investors in Israel; for Sophisticated or Professional Investors in Australia; in New Zealand for wholesale investors (as defined in the Financial Markets Conduct Act); for Professional Investors in Hong Kong; for Qualified Institutional Investors in Japan; in Taiwan for Qualified Institutions/Sophisticated Investors; in Singapore for Institutional/Accredited Investors; for Qualified Institutional Investors and/or certain specific institutional investors in Thailand; for certain specific sovereign wealth funds and/or Qualified Domestic Institutional Investors approved by local regulators only in the People's Republic of China; for certain specific institutional investors in Malaysia upon request; for certain specific institutional investors in Brunei; for Qualified Professional Investors in Korea; for certain specific institutional investors in Indonesia; for qualified buyers in Philippines for informational purposes only; in Canada, this document is restricted to i) accredited investors and ii) permitted clients as defined under National Instrument 45-106 and 31-103 respectively. It is not intended for and should not be distributed to or relied upon by the public or retail investors. Please do not redistribute this document.

Forward-looking statements are not a guarantee of future results. They involve risks, uncertainties, and assumptions. There can be no assurance that actual results will not differ materially from expectations.

This is marketing material and not financial advice. It is not intended as a recommendation to buy or sell any particular asset class, security, or strategy. Regulatory requirements that require impartiality of investment/investment strategy recommendations are therefore not applicable nor are any prohibitions to trade before publication.

By accepting this document, you consent to communicate with us in English, unless you inform us otherwise. Data as at February, 2025, unless otherwise stated.

For the distribution of this document, Continental Europe is defined as Austria, Belgium, Denmark, Finland, France, Germany, Greece, Italy, Ireland, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, and Switzerland.

All articles in this publication are written, unless otherwise stated, by Invesco professionals. Views and opinions are based on current market conditions and are subject to change. This publication does not form part of any prospectus. This publication contains general information only and does not take into account individual objectives, taxation position or financial needs. Nor does this constitute a recommendation of the suitability of any investment strategy for a particular investor.

This publication is not an invitation to subscribe for shares in a fund nor is it to be construed as an offer to buy or sell any financial instruments. As with all investments, there are associated inherent risks. This publication is by way of information only. This document has been prepared only for those persons to whom Invesco has provided it. It should not be relied upon by anyone else and you may only reproduce, circulate and use this document (or any part of it) with the consent of Invesco. Asset management services are provided by Invesco in accordance with appropriate local legislation and regulations.

This publication is issued:

- in **Hong Kong** by Invesco Hong Kong Limited景順投資管理有限公司, 45/F, Jardine House, 1 Connaught Place, Central, Hong Kong. This document has not been reviewed by the Securities and Futures Commission.

- in **Singapore** by Invesco Asset Management Singapore Ltd, 9 Raffles Place, #18-01 Republic Plaza, Singapore 048619.

- in **Taiwan** by Invesco Taiwan Limited, 22F, No.1, Songzhi Road, Taipei 11047, Taiwan (0800-045-066). **Invesco Taiwan Limited is operated and managed independently.**

- in **Japan** by Invesco Asset Management (Japan) Limited, Roppongi Hills Mori Tower 14F, 6-10-1 Roppongi, Minato-ku, Tokyo 106-6114; Registration Number: The Director- General of Kanto Local Finance Bureau (Kin-sho) 306; Member of the Investment Trusts Association, Japan and the Japan Investment Advisers Association.

- in **Australia** by Invesco Australia Limited (ABN 48 001 693 232), Level 26, 333 Collins Street, Melbourne, Victoria, 3000, Australia which holds an Australian Financial Services Licence number 239916.

This document has been prepared only for those persons to whom Invesco has provided it. It should not be relied upon by anyone else. Information contained in this document may not have been prepared or tailored for an Australian audience and does not constitute an offer of a financial product in Australia. You may only reproduce, circulate and use this document (or any part of it) with the consent of Invesco.

The information in this document has been prepared without taking into account any investor's investment objectives, financial situation or particular needs. Before acting on the information the investor should consider its appropriateness having regard to their investment objectives, financial situation and needs.

You should note that this information:
- may contain references to dollar amounts which are not Australian dollars;
- may contain financial information which is not prepared in accordance with Australian law or practices;
- may not address risks associated with investment in foreign currency denominated investments; and
- does not address Australian tax issues.

- in **New Zealand** by Invesco Australia Limited (ABN 48 001 693 232), Level 26, 333 Collins Street, Melbourne, Victoria, 3000, Australia which holds an Australian Financial Services Licence number 239916.

This document is issued only to wholesale investors (as defined in the Financial Markets Conduct Act) in New Zealand to whom disclosure is not required under Part 3 of the Financial Markets Conduct Act. This document has been prepared only for those persons to whom it has been provided by Invesco.

It should not be relied upon by anyone else and must not be distributed to members of the public in New Zealand. Information contained in this document may not have been prepared or tailored for a New Zealand audience. You may only reproduce, circulate and use this document (or any part of it) with the consent of Invesco. This document does not constitute and should not be construed as an offer of, invitation or proposal to make an offer for, recommendation to apply for, an opinion or guidance on Interests to members of the public in New Zealand. Applications or any requests for information from persons who are members of the public in New Zealand will not be accepted.

- in the **United States** by Invesco Advisers, Inc., 1331 Spring Street NW, Suite 2500, Atlanta, GA 30309, USA.

- in **Canada** by Invesco Canada Ltd., 16 York Street, Suite 1200, Toronto, Ontario M5J 0E6.

- in **Austria** and **Germany** by Invesco Asset Management Deutschland GmbH, An der Welle 5, 60322 Frankfurt am Main, Germany.

- in **Belgium, Denmark, Finland, France, Greece, Italy, Ireland, Luxembourg, Netherlands, Norway, Portugal, Spain** and **Sweden** by Invesco Management S.A., President Building, 37A Avenue JF Kennedy, L-1855 Luxembourg, regulated by the Commission de Surveillance du Secteur Financier, Luxembourg.

- in **Dubai, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia** and the **United Arab Emirates** by Invesco Asset Management Limited, Index Tower Level 6 - Unit 616, P.O. Box 506599, Al Mustaqbal Street, DIFC, Dubai, United Arab Emirates. Regulated by the Dubai Financial Services Authority.

- in the **Isle of Man, Jersey, Guernsey** and the **UK** by Invesco Asset Management Limited, Perpetual Park, Perpetual Park Drive, Henley-on-Thames, Oxfordshire, RG9 1HH, United Kingdom. Authorised and regulated by the Financial Conduct Authority.

- in **Switzerland** by Invesco Asset Management (Schweiz) AG, Talacker 34, 8001 Zurich, Switzerland.

- in **Israel** by Invesco Asset Management Limited, Perpetual Park, Perpetual Park Drive, Henley-on-Thames, Oxfordshire RG9 1HH, UK. Authorised and regulated by the Financial Conduct Authority. This document may not be reproduced or used for any other purpose, nor be furnished to any other person other than those to whom copies have been sent. Nothing in this document should be considered investment advice or investment marketing as defined in the Regulation of Investment Advice, Investment Marketing and Portfolio Management Law, 1995 ("the Investment Advice Law"). Investors are encouraged to seek competent investment advice from a locally licensed investment advisor prior to making any investment. Neither Invesco Ltd. nor its subsidiaries are licensed under the Investment Advice Law, nor does it carry the insurance as required of a licensee thereunder.