

DBS RMB Index for VVinning Enterprises (DRIVE) - 3Q13

DBS Group Research

12 November 2013

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Yearly report card

RMB development at the corporate level in Hong Kong throughout 4Q12-3Q13

- Corporate usage of RMB has stalled
- Business needs for RMB (customer order/invoices/trade settlement) was little changed throughout 4Q12-2Q13 and declined in 3Q13
- Large corporations have more interest in RMB customer order/invoices/trade settlement than SMEs
- Most companies are only using simple RMB spot conversion in their everyday operations. The use of RMB for investment, hedging or financing remained negligible
- There is still ample room to deepen RMB penetration locally. In Hong Kong, the popularity of using RMB for trade settlement, financing, and day-to-day business transactions is still extremely low relative to the HKD and the USD

The 3Q13 reading fell slightly - What happened to the index components?

The 3Q13 reading of DRIVE fell to 54.3 from 55.2 in 2Q13 and is the lowest recorded so far (2Q13: 55.2; 1Q13: 55.1; 4Q12: 54.9). The decrease came amid falling business demand for RMB. In 3Q13, significantly more companies indicated that they did not have RMB customer orders/ invoices and trade settlement in the past 12 months. Similarly, more companies indicated that they will not consider using RMB for these purposes in the next 12 months. In addition, fewer companies reported currently using or considered using RMB trade services than in the previous quarters. However, the decline in the use of RMB services was not across the board as more companies said they currently use or considered using RMB payment and receivables services. Companies surveyed generally had a rosier outlook for their business performance in the next 12 months and reported better business results in the previous 12 months (Charts 1a & 1b). Regarding access to RMB finance, the ease of access remained fairly constant in 3Q13 versus 2Q13 (Chart 2).

Favourable policy support remains the key driver behind corporate usage of RMB

- Despite a positive outlook on the Hong Kong economy in 3Q13, the usage of RMB in commercial transactions remained stagnant. Over the past four quarters, there was no consistent positive correlation between the state of the economy/economic outlook and the actual/intended corporate usage of RMB. Since RMB usage is still at the initial stage, a positive economic outlook alone - without policy catalysts - is insufficient to further incentivise usage
- Over the past four quarters, RMB internationalisation has expanded geographically, covering Singapore, Taiwan and even London in the UK. China has also concluded a currency swap agreement with the European Central Bank. But the lack of policy catalysts in Hong Kong,

particularly with respect to increasing the size of the RMB pool, could explain why RMB usage at the corporate level remained stagnant. HKD and USD continue to be the predominant currencies for commercial transactions and trade settlement

- Still, the potential relaxation or removal of the RMB 20,000 daily cap on personal RMB conversion could alter the picture in 2014. Personal RMB wealth management products would flourish initially, but corporate usage of RMB would gradually pick up as the size of the RMB pool in Hong Kong increases and RMB product innovation advances

Key findings and DBS insights

* Unless stated otherwise, figures in parentheses represent findings in the last survey (2Q13)

1. Business needs for RMB decreased

- Business needs for RMB decreased in 3Q13 and are expected to decrease in the next 12 months. Some 24% (42%) of companies surveyed indicated that they had RMB customer orders/invoices in the last 12 months, and 35% (49%) claimed that they would use RMB for these purposes in the next 12 months (Charts 3a & 3b)
- The usage of RMB is already quite common among large corporations (turnover >HK\$1 billion). All of the large corporations surveyed indicated that they had RMB customer orders/invoices and trade settlement in the last 12 months

DBS insights

Business needs for RMB is a key indicator of actual RMB acceptance and usage levels at the corporate level. After tracking this component for four quarters, there is no evidence that RMB corporate penetration has gained traction.

2. Usage of RMB services and products have rebounded

- 3Q13 saw a rebound in the number of companies that used RMB services and products [1] to 24% after dipping to 14% in 2Q13 (1Q13: 26%) (Chart 4)
- 25% (15%) of companies surveyed are currently using or will consider using RMB payment and receivables services in the next 12 months (Chart 5)
- Fewer companies (3%) said they currently use or considered using RMB trade services than in the previous quarters (5%) (Chart 6)
- 9% (12%) of companies that used trade services (all currencies) used RMB trade services in the past 12 months while 1% (8%) that used trade services (all currencies) but are not currently using RMB trade services will consider using them in the next 12 months

DBS insights

Despite the rebound, the percentage of companies using RMB services and products only barely returned to levels seen in 1Q13. As only 1% of companies indicated an interest in using RMB trade services for the first time in the next 12 months, it is expected that the percentage of companies using RMB services and products will hover at present levels for quite some time.

3. RMB corporate product scope has narrowed

- Of those companies that used any RMB services or products, 57% (32%) used FX spot, but only 10% (22%) had RMB-denominated structured

investment deposits and only 5% (23%) had RMB savings and chequing accounts (Chart 7)

- There is still much room to grow the use of RMB hedging products. Only 2% (1%) of companies surveyed are currently using RMB hedging products, and only 1% (3%) are not currently using such products but will consider doing so in the next 12 months
- In the RMB financing space, interest is still very limited. Less than 1% of companies surveyed said they had been using RMB financing, and only 1% indicated that they are likely to use RMB financing in the next 12 months

DBS insights

The Treasury Markets Association launched CNH HIBOR fixing in June, providing a reliable benchmark to price loan facilities and helping to facilitate the development of the offshore RMB interest rate swap market. Market anticipation may have contributed to the increase in the number of companies using complex products (especially SIDs) in 2Q13. Unfortunately, surging interest in complex RMB products did not continue into 3Q13. While efforts to develop RMB products and related financial infrastructure can arouse corporate interest, a sustained take-up of RMB products ultimately depends on their business needs for RMB.

In addition, the declining popularity of RMB products may have been affected by lower RMB appreciation expectations. In 3Q13, fewer respondents reckoned that RMB will appreciate against the USD in the next 12 months (43% in 3Q13 vs. 48% in 2Q13), while more expected RMB to depreciate (6% in 3Q13 vs. 5% in 2Q13) (Chart 8)

4. HKD and USD are still the preferred currencies for payment and receivables/ trade settlement

- 3% (2%) of companies that used payment and receivables/ trade services (all currencies) preferred to use RMB for payment and receivables/ trade settlement (Chart 9)
- Of the companies that used payment and receivables/trade services, 67% (72%) preferred to use HKD while 26% (22%) preferred to use USD for payment or trade settlement (Chart 9)
- 41% of companies expected RMB trade settlement to account for 30% of their total trade settlement within five years

DBS insights

HKD remains the predominant currency used by companies for payment and commercial transactions. The use of RMB in Hong Kong is not expected to lead to the substitution or marginalisation of the HKD. The preference of local companies to use RMB may be affected by their trading partners' willingness to accept/make payments in RMB. To increase local RMB usage, it is imperative that Hong Kong's trading partners prefer to use RMB. This is because many overseas buyers determine the currency used for trade settlement, and USD is still their preferred choice. Even if certain exporting companies in Hong Kong prefer to accept RMB – an appreciating currency – the counterparty may not want to pay in RMB. In that sense, the government's strategy to promote RMB usage in nearby Asian economies is in the right direction.

5. Usage options for RMB liquid assets are limited

- 34% (43%) of respondents held RMB as part of their liquid assets in the past 12 months

- Most companies are only using simple RMB spot conversions in their everyday operations, and not utilising RMB funds in more sophisticated ways
- Most companies either use the RMB they receive to pay their suppliers, put it into deposit accounts or convert it back to HKD. The use of RMB in trade services (2%), investment (1%), hedging (2%) or financing (<1%) remain negligible over the last four quarters

DBS insights

These findings reflect that companies either did not take advantage of short-term cash management solutions or did not require such solutions. This may also indicate a lack of short-term liquid RMB instruments in the market. As RMB gradually accounts for a larger proportion of corporate liquid assets, both financial institutions and companies could begin to explore RMB liquidity management solutions.

About the index

The DBS RMB Index for VVinning Enterprises (DRIVE) is the first index in the industry that is specifically designed to gauge the level of RMB usage, acceptance and penetration among companies registered in Hong Kong, as well as companies' inclination to use RMB in the future. Although macroeconomic data on the circulation of offshore RMB are widely available, they are not able to offer an in-depth perspective on the developmental progress of Hong Kong as an RMB offshore centre. By focusing on the level of RMB usage and acceptance among Hong Kong-registered companies, this index aims to serve as the first benchmark to measure the pace of RMB internationalisation in Hong Kong. Policy-makers, businesses and investors alike will find this index a useful strategic tool over time.

DBS Bank (Hong Kong) Limited has commissioned an independent research house (Nielsen) to compile DRIVE and conduct the related survey on a quarterly basis, starting from the fourth quarter of 2012. Subsequent index values will be released on a quarterly basis and over time will reveal a lot more about the pace of development of Hong Kong as an offshore RMB centre. Corresponding policy recommendations can thus be drawn from analysing the future time series. In future, the index may be extended to cover other countries which are also offshore RMB centres.

Methodology

Decision-makers of companies registered in Hong Kong with annual sales turnover of HK\$200,000 and above were interviewed by telephone. A total of 209 companies were surveyed between August and October 2013. The sample comprised 197 SMEs (with annual sales turnover of HK\$200,000 to HK\$1 billion) and 12 large corporations (with annual sales turnover of over HK\$1 billion). The SMEs were selected via quota sampling based on company industry and sales turnover distribution released by the Census and Statistics Department (C&SD). The final sample was weighted to ensure it was representative of the business landscape in Hong Kong, referencing C&SD's distribution information (Tables 1 and 2).

Index computation and components

The quarterly index aims to gauge the level of RMB usage, acceptance and penetration among Hong Kong-registered companies. It is based on six questions measuring four key dimensions driving business adoption and internationalisation of RMB in Hong Kong. They are: 1) Actual business performance in the last 12 months and expectations for the next 12 months as the underlying conditions driving corporate demand for RMB; (2) Past and future demand for RMB in business operations; (3) Usage of RMB payment and receivables services and trade services; and (4) Ease of access to RMB financing. The index is the

weighted average based on the factor analysis [2] applied to these key areas. The weightings are based on the statistical variance and correlation between each of the key areas. The calculated values are then rescaled to between 0 and 100.

The index for each quarter is computed using the following formula:

Index (i,j) =

$$\frac{\sum_{i=1}^N \sum_{j=1}^K w_j Q_{ij}}{N}$$

Where,

N = Sample size for current wave

K = Number of selected questions

Q_{ij} = Response of selected questions (adjusted to 0-100)

W_j = Weighting for individual questions

Notes

[1] RMB deposit (including CNY time deposit/CNY deposit, current and saving accounts), RMB payment and receivables services (including Auto Pay, TT/Remittance). RMB investment services, RMB financing services (including loans, issuing bonds, securities etc.), RMB trade services (including trade finance, L/C, bills etc.), RMB insurance products, RMB MPF products, RMB hedging products

[2] Factor analysis is a statistical treatment to provide approximation to describe the variability of the parameters used to calculate the index

Table 1: Company industry coverage

Manufacturing	Restaurants
Construction	Hotel/ Real Estate
Wholesale	Transportation/ Communication
Retailing	Business Services
Import/ Export	Personal Services

Table 2: Company annual sales turnover (source: C&SD 2011)

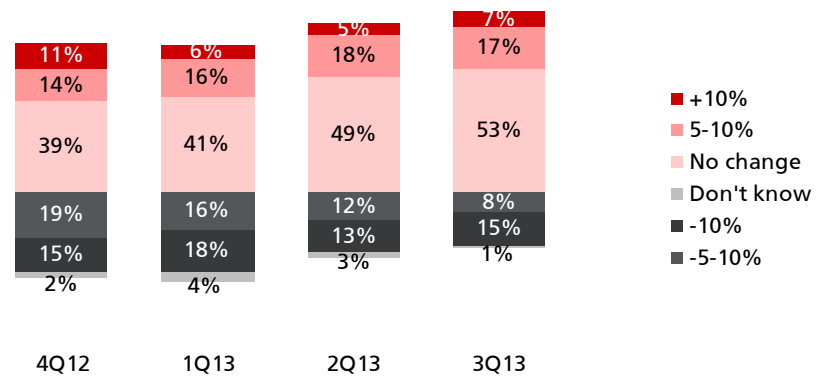
Over HK\$1 Billion	0.3%
Over HK\$50 Million to HK\$1 Billion	4.1%
Over HK\$20 Million to HK\$50 Million	5.4%
Over HK\$10 Million to HK\$20 Million	4.1%
Over HK\$1 Million to HK\$10 Million	47.0%
Over HK\$ 200,000 to HK\$1 Million	39.1%

About The Nielsen Company

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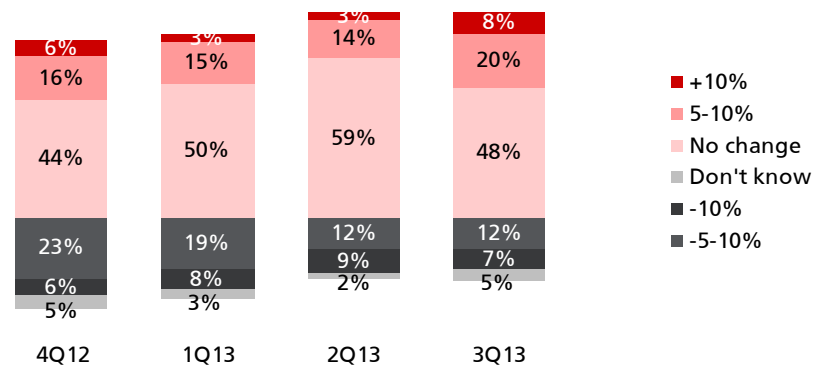
Key charts and graphs

Chart 1a: Business results in the past 12 months (sales turnover)



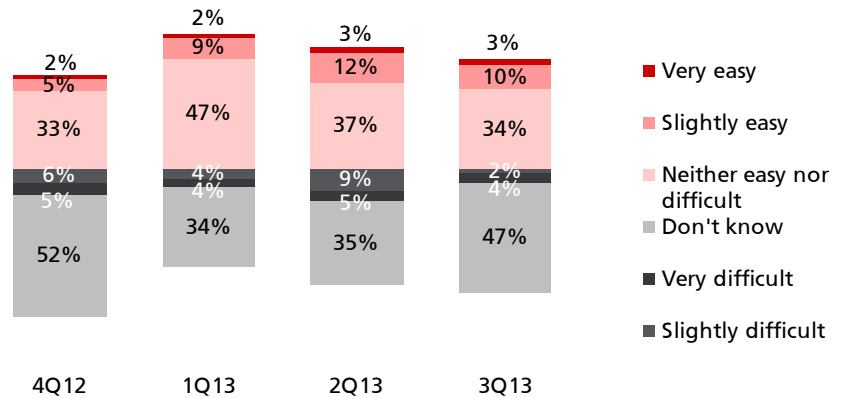
Base: All respondents

Chart 1b: Business performance outlook in the next 12 months (sales turnover)



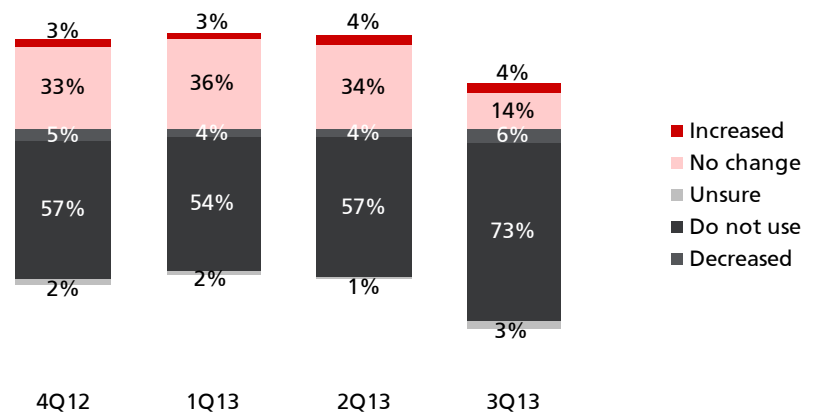
Base: All respondents

Chart 2: Ease of access to RMB loan or credit facilities



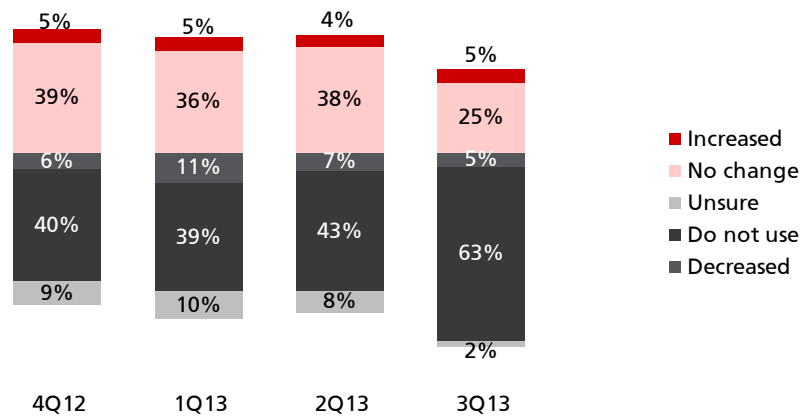
Base: All respondents

Chart 3a: Change in RMB customer order/ invoices and trade settlement in P12M



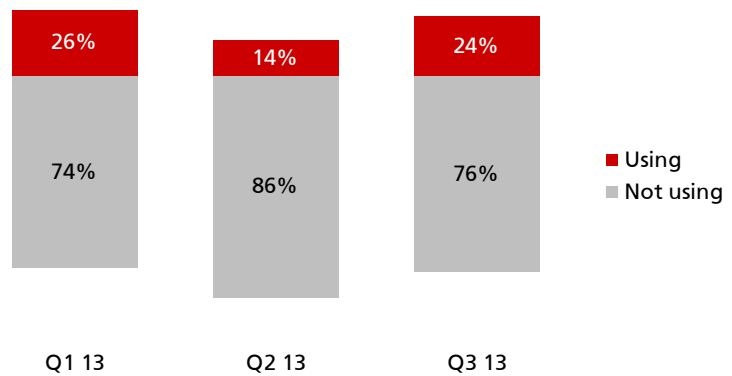
Base: All respondents

Chart 3b: Change in RMB customer order/ invoices and trade settlement in N12M



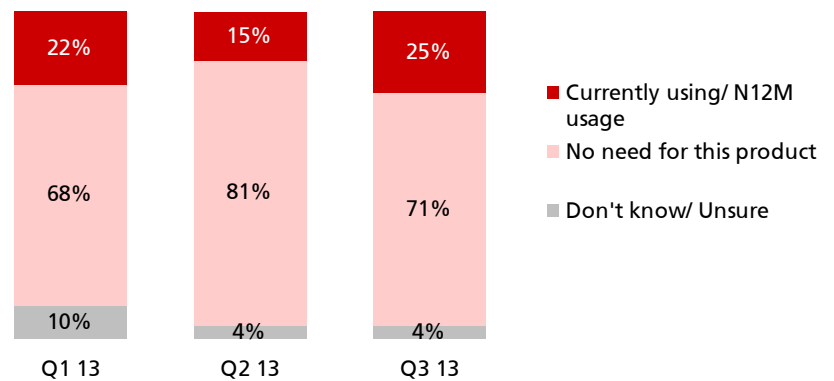
Base: All respondents

Chart 4: Overall RMB products or services usage



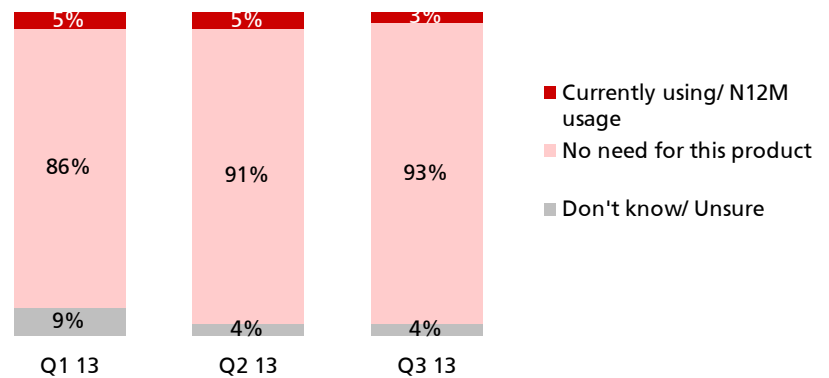
Base: All respondents

Chart 5: Usage of RMB payment and receivables services



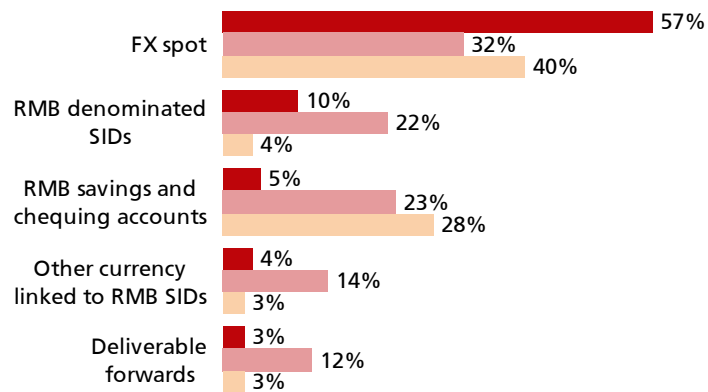
Base: All respondents

Chart 6: Usage of RMB trade services



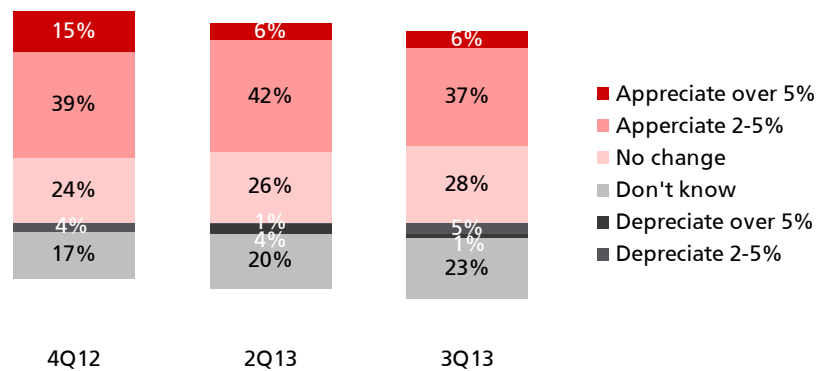
Base: All respondents

Chart 7: RMB products used in the past 12 months



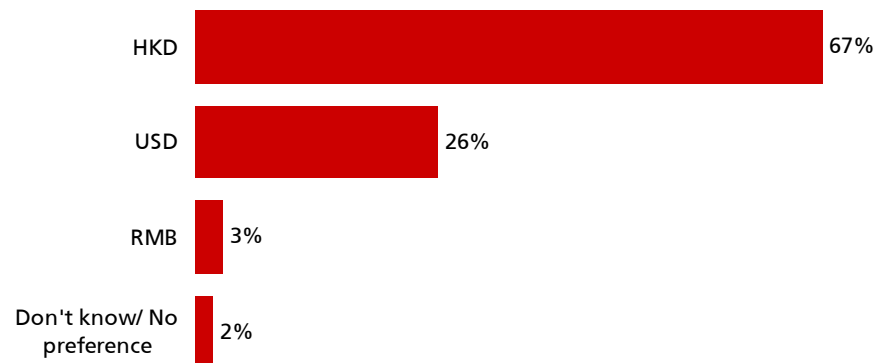
Base: Companies using any RMB services or products

Chart 8: Expectations on RMB vs. USD



Base: All respondents

Chart 9: Preferred currency for payment/ receivable or trade settlement (3Q13)



Base: Companies using payment and receivable services/ trade services

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