

Chinese Bonds

Fidelity International

February 26th 2019

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Head of Asian Fixed Income

For professional investors only



Risks

The value of investments and the income from them can go down as well as up so you may get back less than you invest.

Bond investments

These funds invest in bonds whose price is influenced by movements in interest rates, changes in the credit rating of bond issuers, and other factors such as inflation and market dynamics. In general, as interest rates rise the price of a bond will fall. The risk of default is based on the issuer's ability to make interest payments and to repay the loan at maturity. Default risk may, therefore, vary between different government issuers as well as between different corporate issuers.

Corporate bonds

Due to the greater possibility of default an investment in a corporate bond is generally less secure than an investment in government bonds.

High yield bonds

Sub-investment grade bonds are considered riskier bonds. They have an increased risk of default which could affect both income and the capital value of the Fund investing in them.

Overseas Markets

These funds invest in overseas markets and so the value of investments can be affected by changes in currency exchange rates.

Currency Hedging

Currency hedging is used to substantially reduce the risk of losses from unfavourable exchange rate movements on holdings in currencies that differ from the dealing currency. Hedging also has the effect of limiting the potential for currency gains to be made.

Emerging Markets

These funds invest in emerging markets which can be more volatile than other more developed markets.

Derivatives

These funds may make increased and more complicated use of derivatives and this may result in leverage. In such situations performance may rise or fall more than it would have done otherwise. These funds may be exposed to the risk of financial loss if a counterparty used for derivative instruments subsequently defaults.

Other

The funds do not offer any guarantee or protection with respect to return, capital preservation, stable net asset value or volatility. Reference to specific securities should not be construed as a recommendation to buy or sell these securities and is included for the purposes of illustration only. Investors should note that the views expressed may no longer be current and may have already been acted upon.

Chinese Bonds

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1 Why are Chinese Bonds relevant for German investors?

2 Characteristics of Chinese Bonds

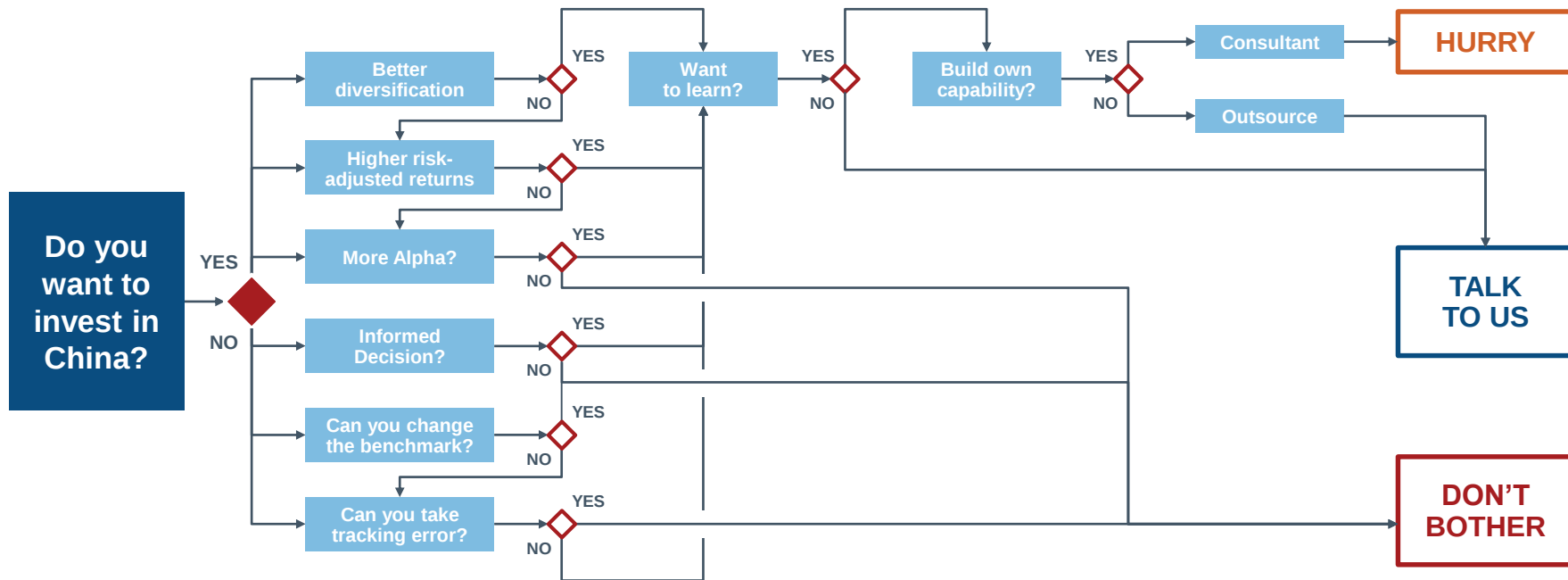
3 Risks to consider

4 Fidelity in Asia

Do you want to invest in China?

Decision tree

1



Source: Fidelity International, 2019.

Index inclusion will bring further inflows

1

2017

Reviewing

- Global Agg. + China Index
- EM Local Currency Government + China Index

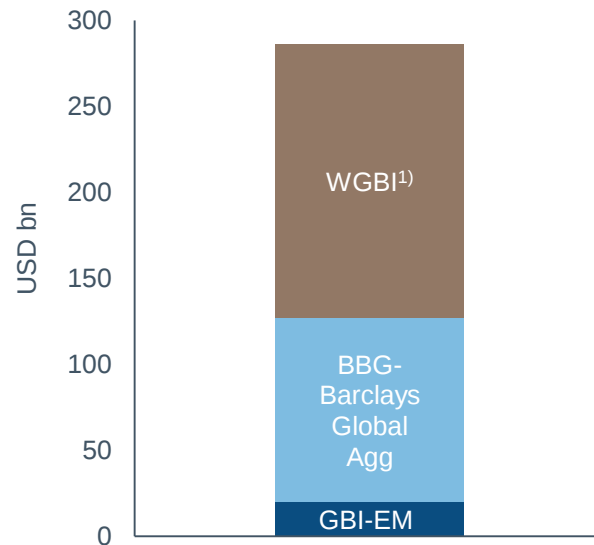
Bloomberg
 **BARCLAYS**

- FTSE World Government Bond Index
- EM Govt Bond Index
- Asian Govt Bond Index
- Asia Pacific Govt Bond Index

2018

**Bloomberg-Barclays Global
Aggregate Index**

>\$280bn potential inflows



Source: Fidelity International, Citi, Standard Chartered Research, December 2017. Third party trademark, copyright and other intellectual property rights are and remain the property of their respective owners. 1) World Government Bond Index

6% by end 2020

Pro Forma Impact on key Indices

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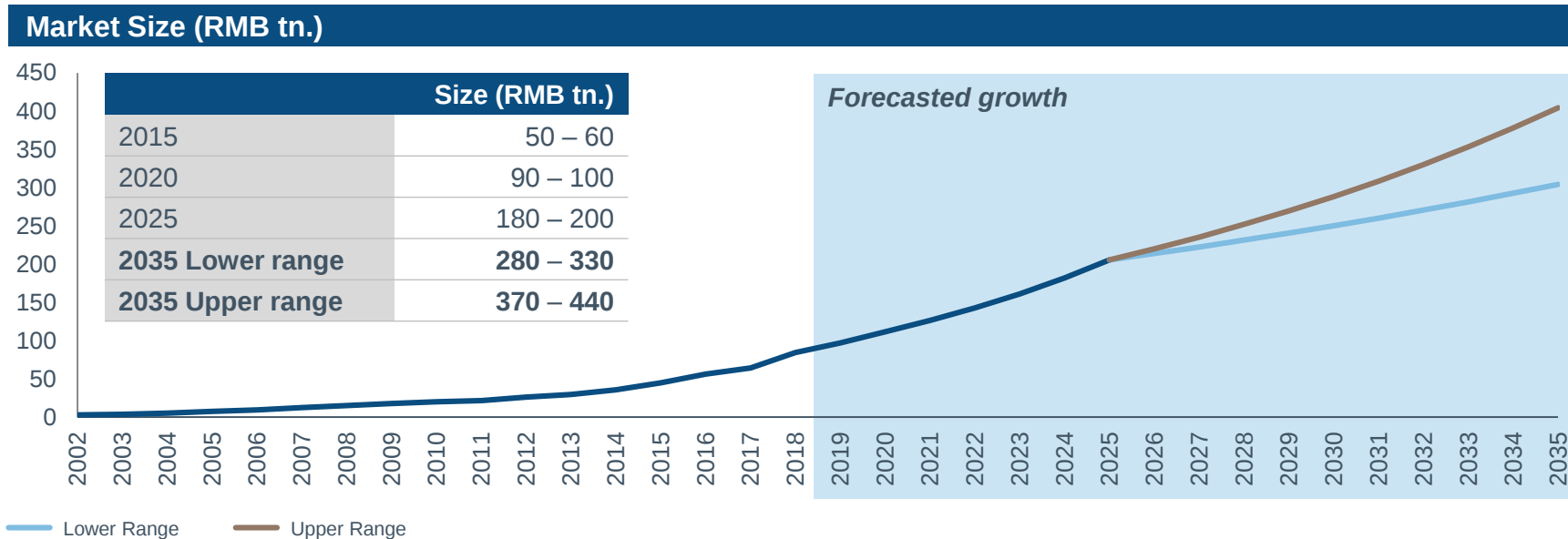
Projected	Count	MV (USD bn)	MV (%)	
Global Aggregate Index:				
+ 100% China (Full Weight in Nov 2020)	364	3,323	6.06%	4th place after USD, EUR, JPY
+ 5% China (April 2019 Scaling Factor)	364	166	0.32%	11th place
Global Treasury Index:				
+ 100% China (Full Weight in Nov 2020)	159	1,551	5.24%	5th place after USD, EUR, JPY, GBP
+ 5% China (April 2019 Scaling Factor)	159	78	0.28%	16th place
Asia-Pacific Aggregate Index:				
+100% China (Full Weight in Nov 2020)	364	362	23.83%	2nd place after JPY
+5% China (April 2019 Scaling Factor)	364	18	1.54%	5th place
EM Local Currency Government Index:				
+ 100% China	159	1,551	42.07%	1st place
+ 5% China	159	78	3.50%	9th place

Source: Bloomberg, as of 31 January 2019 projected universe.

Further growth potential

1

Size of China onshore bond market



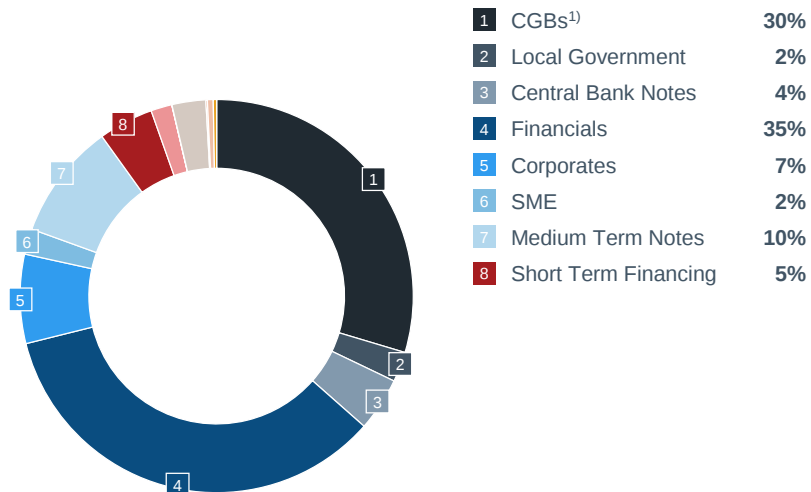
Source: Fidelity International, Hong Kong Exchanges and Clearing Limited, China Central Depository & Clearing Co., Ltd (CCDC), Citi, WIND, as of December 2018. The forecasted market sizes are estimated values and are based on assumptions made by Fidelity. Therefore, Fidelity gives no guarantee for the accuracy of the information.

Evolution of China's onshore CNY bond market

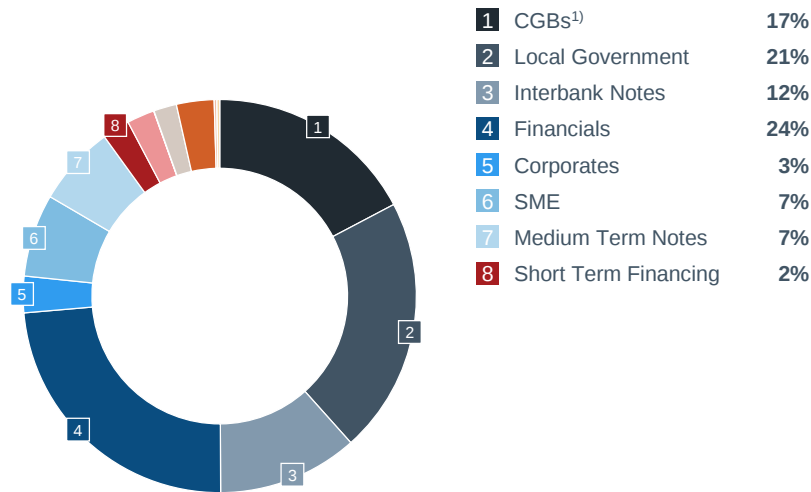
Rapidly developing, not yet developed

1

2012 Industry breakdown



2018 Industry breakdown

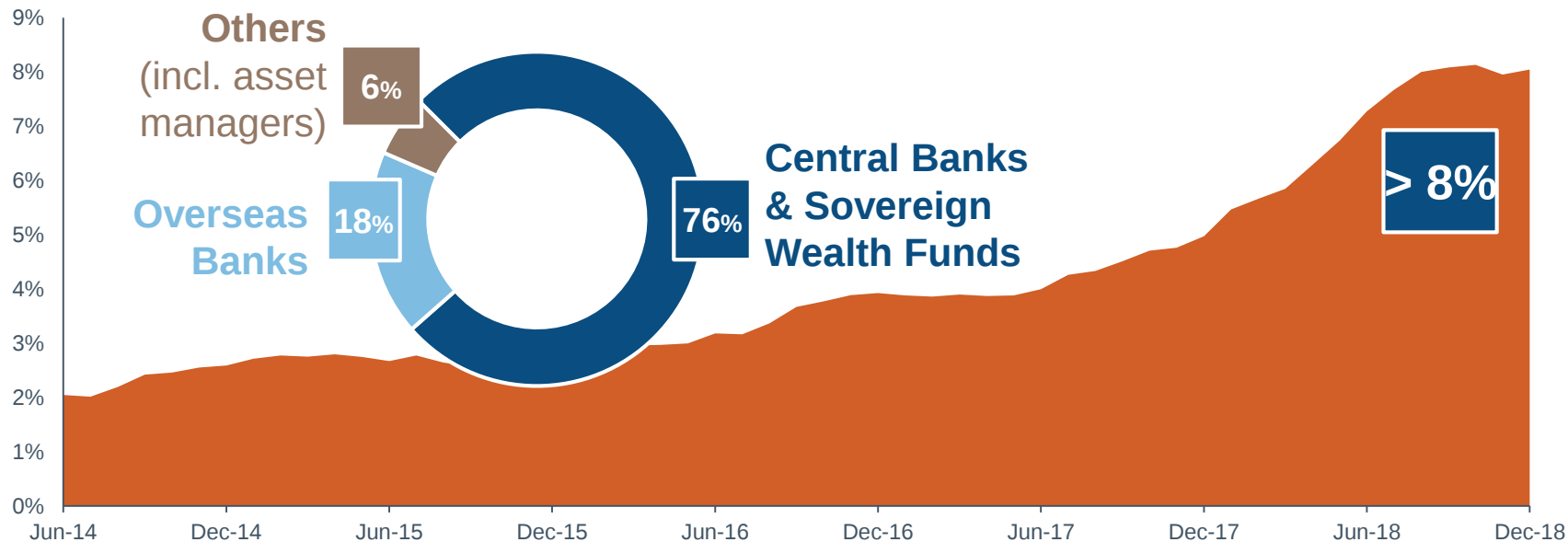


Source: Fidelity International, WIND, December 2018. 1) Chinese Government Bonds

Foreign participation increasing

Foreign ownership of China Government Bonds

1



Source: Bloomberg, Chinabond, Fidelity International, December 2018.
Pie Chart : CEIC, Morgan Stanley.

Low correlation offers diversification benefits

1

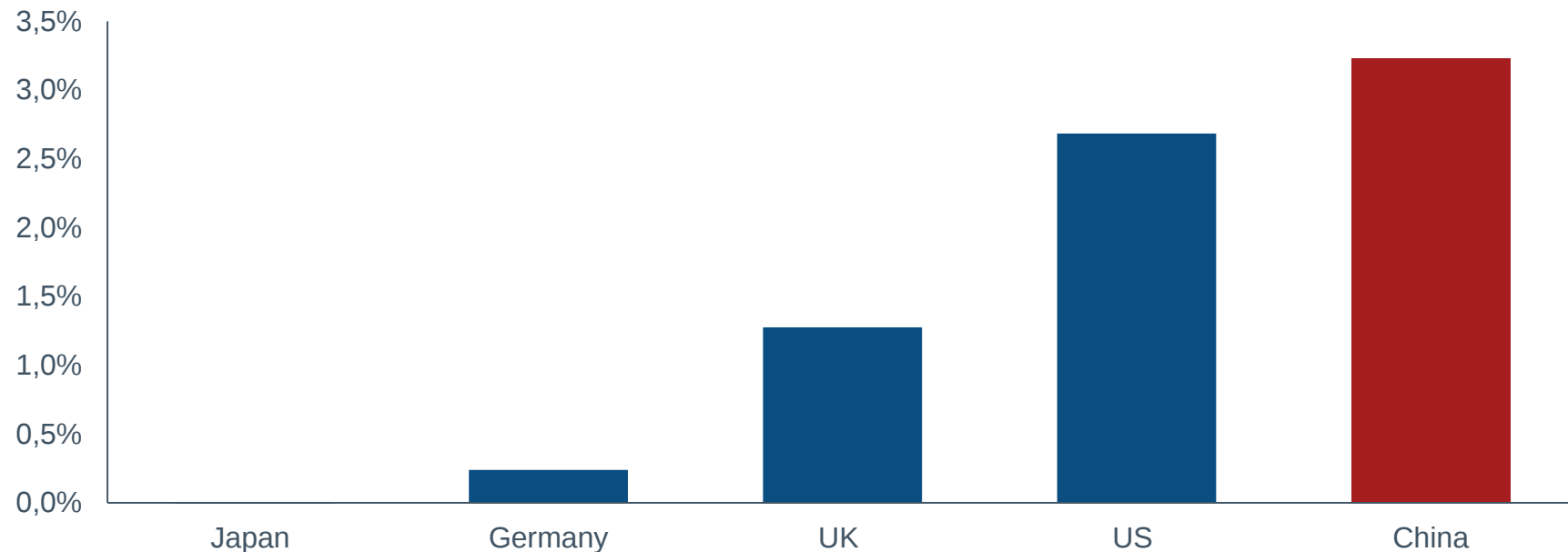
	Onshore RMB Bond	Asian IG	Asian HY	US IG	Euro IG	EM Corp USD	Asian Equity	US Equity	Euro Equity	US Treasury
Onshore RMB Bond	1.00									
Asian IG	-0.11	1.00								
Asian HY	-0.16	0.86	1.00							
US IG	-0.12	0.88	0.74	1.00						
Euro IG	-0.08	0.66	0.59	0.80	1.00					
EM Corp USD	-0.20	0.92	0.92	0.83	0.67	1.00				
Asian Equity	-0.17	0.61	0.79	0.58	0.52	0.75	1.00			
US Equity	-0.14	0.44	0.63	0.38	0.40	0.61	0.82	1.00		
Euro Equity	-0.17	0.41	0.57	0.41	0.53	0.58	0.71	0.82	1.00	
US Treasury	0.23	0.40	0.06	0.44	0.20	0.13	-0.13	-0.26	-0.30	1.00

Source: Bloomberg, ICE BofAML Bond Indices, J.P. Morgan Indices, MSCI Equity Indices based on 10-years to 31st July 2018. The table uses a linear color scale from 0 = green to 1 = red. For offshore RMB Bond, data since January 2011. For Onshore RMB Bond, data since January 2013.

Chinese government bonds offer higher yields

1

10-year government bond yields



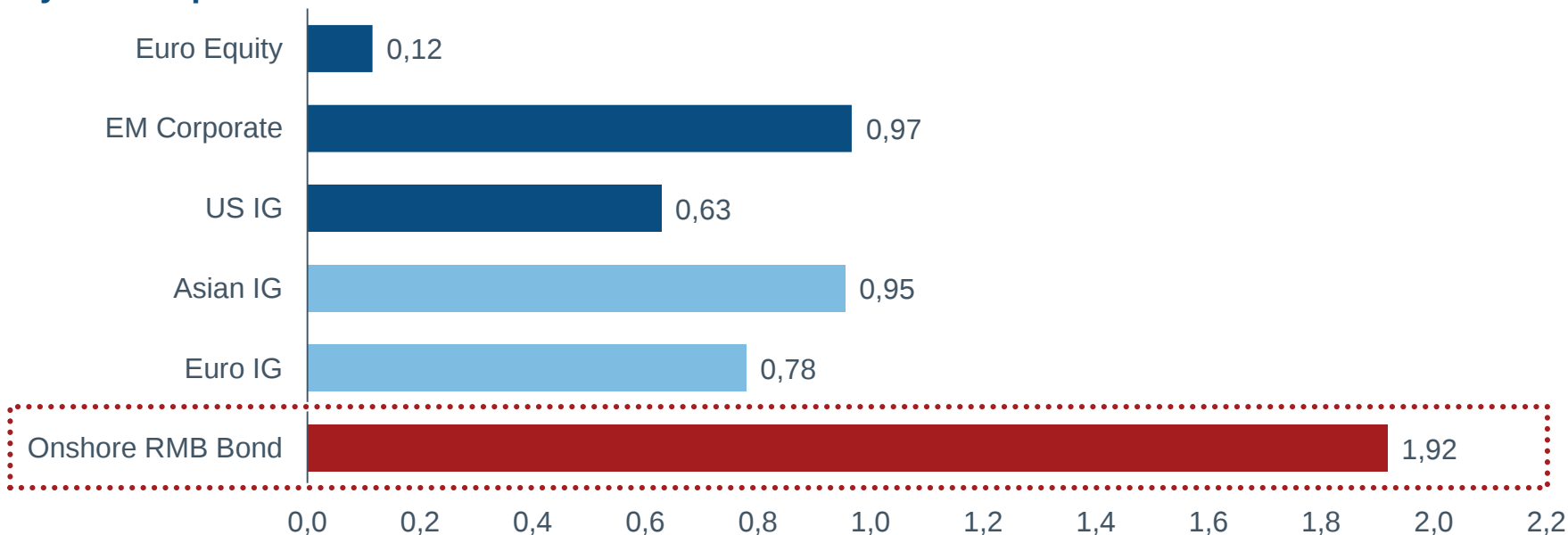
Past Performance is not a reliable indicator of future results. The value of shares may fluctuate and can not be guaranteed.

Source: Bloomberg, Fidelity International, February 2019.

Attractive risk-adjusted returns

1

5-year Sharpe ratio of asset classes



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Source: Fidelity International, Bloomberg, ICE BofAML Bond Indices, J.P. Morgan Indices, ChinaBond, MSCI Equity Indices based on 5-years to September 2018.
US 3-Month T-bill was used for Sharpe ratio calculation.

Performance

Backtesting including China

1

	Ann. Std. Dev.	Cumulative Return
Global Agg	4.47%	7.13%
Global Agg + 5% CGB	4.36%	7.76%
Global Agg + 10% CGB	4.27%	8.39%
Global Agg + 20% CGB	4.12%	9.66%
WGBI	2.86%	16.62%
WGBI ¹⁾ + 5% CGB	2.78%	16.82%
WGBI ¹⁾ + 10% CGB	2.72%	17.01%
WGBI ¹⁾ + 20% CGB	2.69%	17.38%

Past Performance is not a reliable indicator of future results. The value of shares may fluctuate and can not be guaranteed.

Source: Barclays, Bloomberg, Factset, FTSE Russell, ICE, Fidelity International as of January 2019.

Note: Analysis period is from 31/12/2013 to 31/01/2019. Chinese Government Bond (CGB) returns represented by ICE China Government Index (GOCN). Returns shown are USD unhedged. 1) World Government Bond Index

Chinese Bonds

Fidelity International

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2 Characteristics of Chinese Bonds

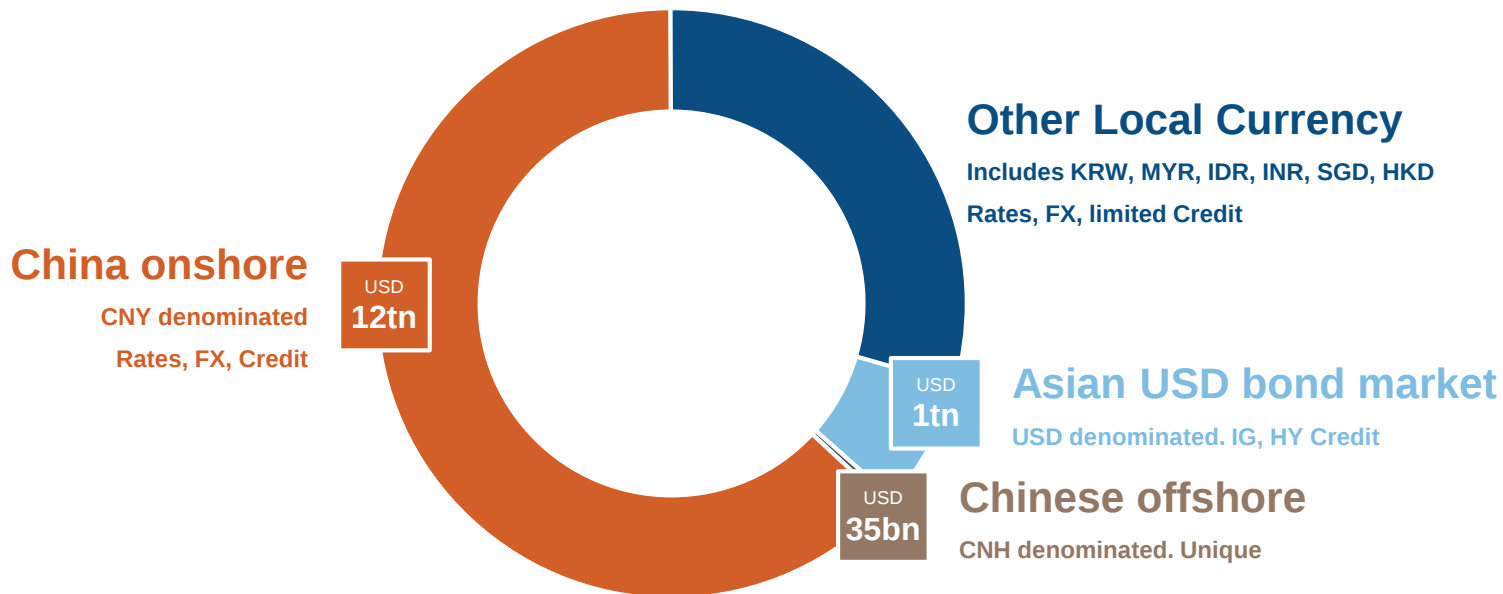
3 Risks to consider

4 Fidelity in Asia

Asia's bond market

Three quite different ways to buy China

2



Source: Fidelity International, ICE BofAML ADOL and CNHJ Indices, 2019.

Accessing China onshore

Various options

2

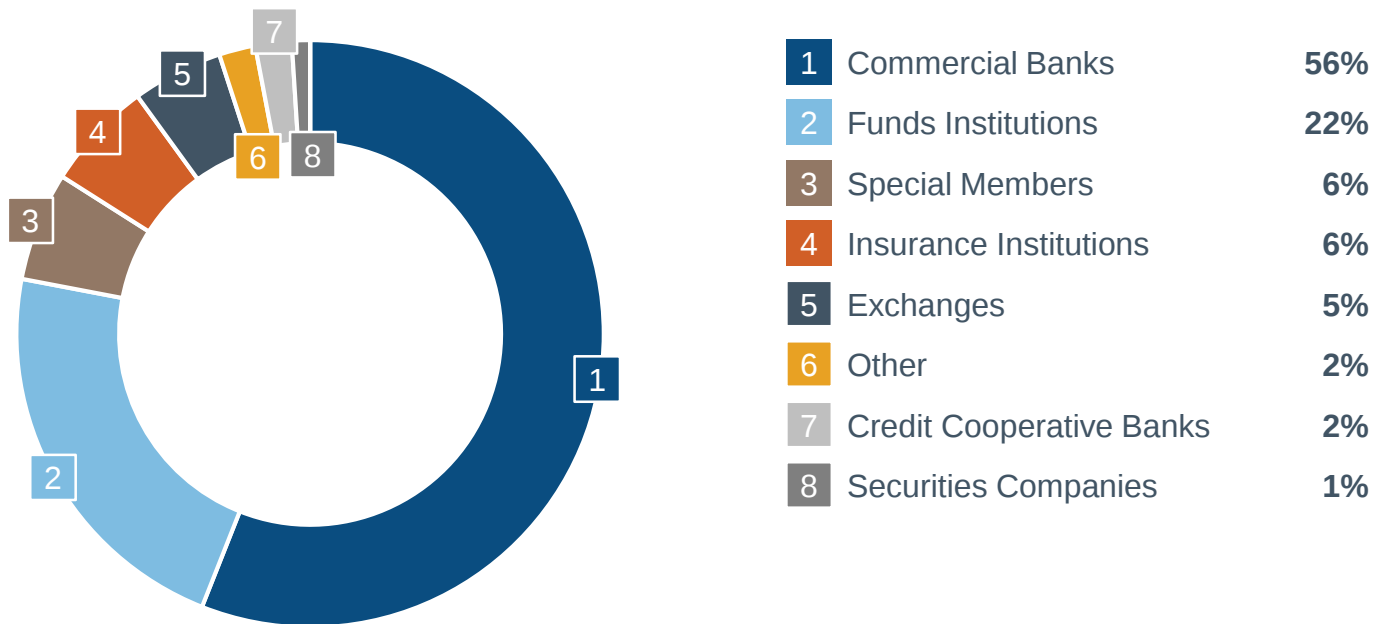


Source: Fidelity International, 2019. 1) Chinese Interbank Bond Market; 2) QFII = Qualified Foreign Institutional Investors; RQFII = Renminbi QFII

Onshore China bond market investor base

Growing in depth and breadth

2



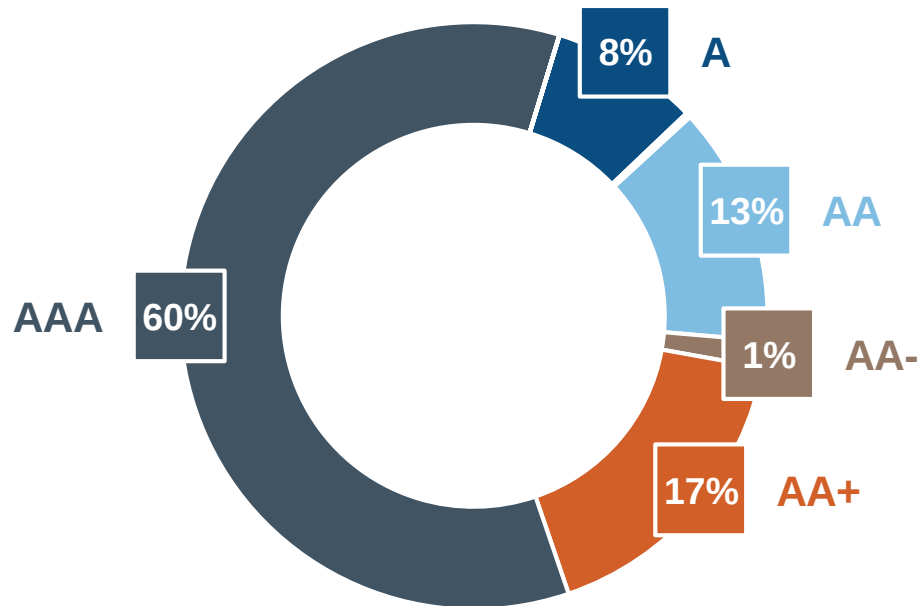
Source: Chinabond, Goldman Sachs Global Investment Research, 2018.

Onshore China bond universe

Investment grade by international standards

2

Onshore Credit Rating	International Equivalent
AAA	~AA/A
AA	~BBB/BB
A	~B



Source: Wind, Fidelity International. Credit rating comparison is indicative.

Chinese Bonds

Fidelity International

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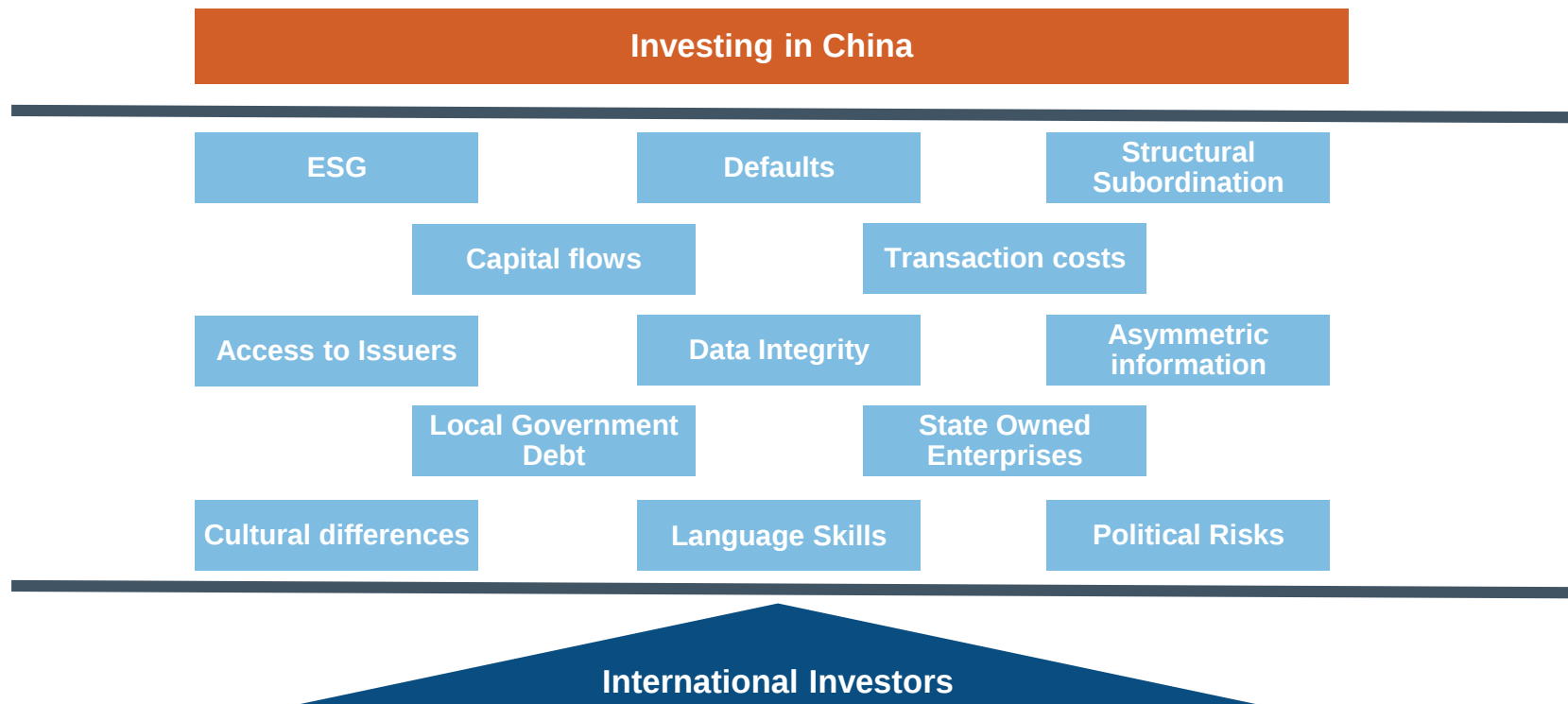
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Is China any different?

3



Source: Fidelity International, 2019.

Key developments in China

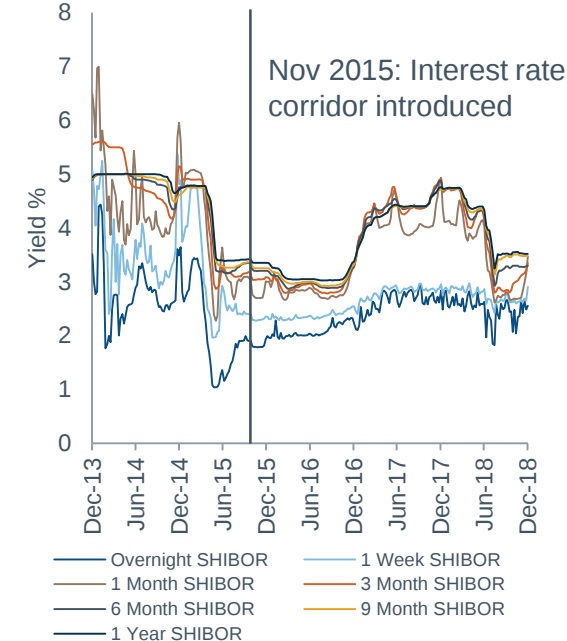
3

Structural improvements

Onshore credit differentiation



Monetary policy mechanism



Controlled currency



Past Performance is not a reliable indicator of future results. The value of shares may fluctuate and can not be guaranteed.

Source: Bloomberg; Fidelity International, December 2018.

Source: PBOC; Bloomberg; Fidelity International, December 2018.

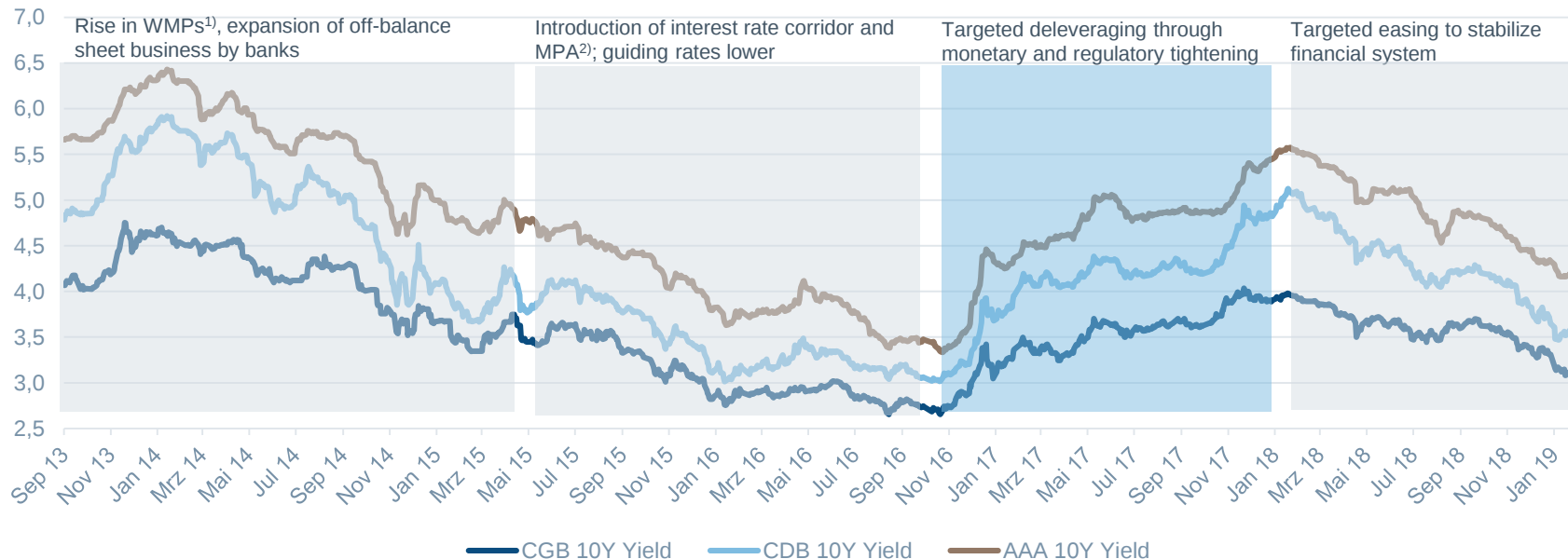
Source: Bloomberg; Fidelity International, December 2018.

Chinese government bonds

Reflecting the evolution of the financial system

3

Historical 10-year Chinese Government, Chinese Development Bank, and AAA Bond Yield



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Source: Bloomberg, Fidelity International, 2019. 1) Wealth Management Products; 2) Macro Prudential Assessment

China policy responses

Monetary easing bias to continue

3

INCREASING EASING BIAS

1. Jan 2018: 1st targeted 50-100bps RRR cut
2. Apr: 2nd 100bps RRR cut
3. **Early June: Medium-term Lending Framework (MLF) expanded to include lower grade AA+ and AA onshore corporate bonds**
4. Late June: 3rd RRR cut of 50bps across 5 SOE banks and 12 joint stock banks which would release around RMB500-700bn liquidity into the market to support debt-to-equity program
5. **Mid July: Providing banks with additional funding through MLF to support additional loan supply and buying of lower rated onshore bonds**
6. Mid July: Fine tuning Asset Management Product (AMP) rules
7. Early Oct: 4th 100 bps RRR cut
8. **Late Oct: Launched public consultation for personal income tax deduction**
9. **Mid Nov: PBoC's Shanghai unit will introduce more debt financing tools to support fundraising of POEs**
10. Early Jan 2019: The PBOC delivered a blanket 100bps RRR cut
11. **End Jan 2019: CBS (Central Bank Bills Swap) to improve liquidity of Bank's perpetual bonds**

Source: Fidelity International, January 2019.

Chinese Bonds

Fidelity International

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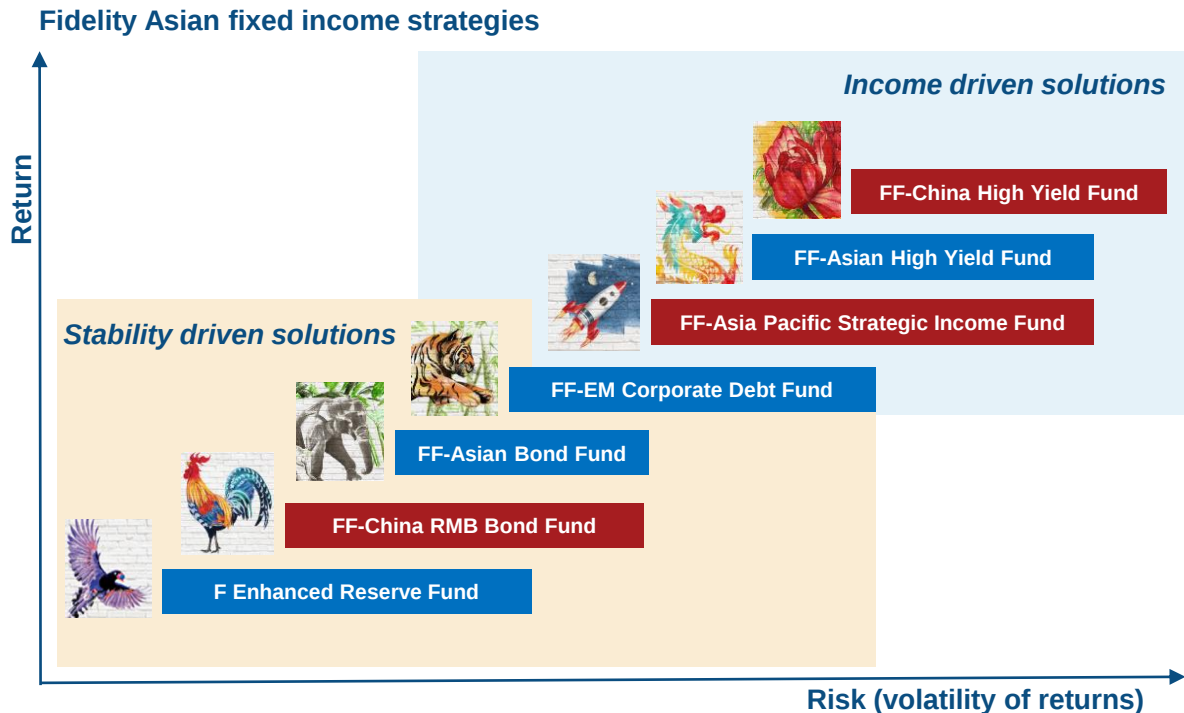
3 Risks to consider

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Our product range continues to expand

4

Offering China focused strategies across the risk and return spectrum



- Managing bond assets since 1982, with fixed income team structure in place since 1995
- Established Asia FI since 2002
- \$84.7bn fixed income AUM for institutional, wholesale and retail clients globally*

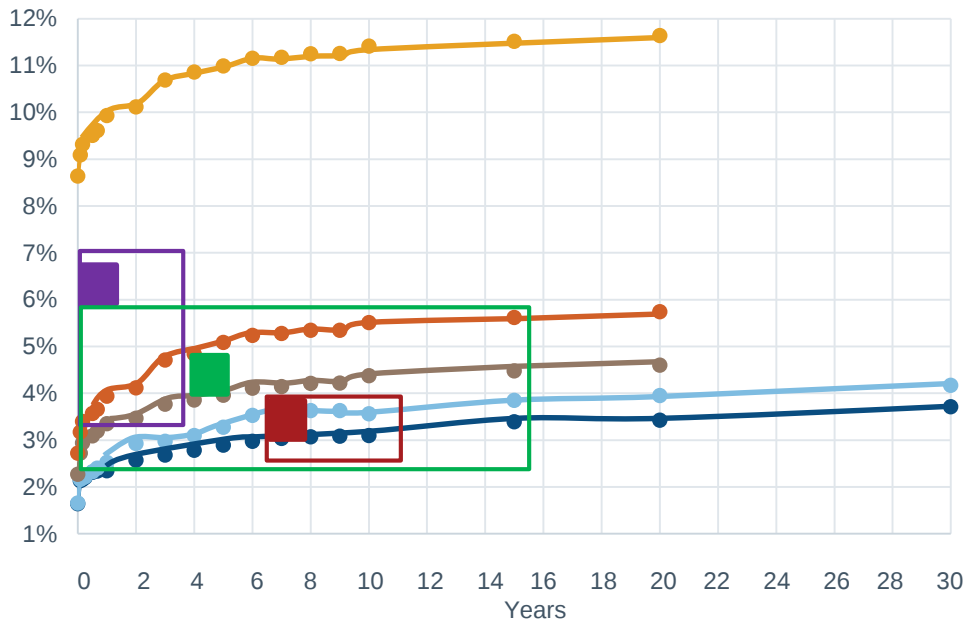
Date	Fund Launches
2007	Asian High Yield Fund (USD)
2011	China RMB Bond Fund (RMB)
2015	China High Yield Fund (USD)
2017	1 st Onshore WOFI FI Private Fund
2018	Onshore CGBs ¹⁾ & SDBC ²⁾ Pool Fund
2018	3 rd Onshore WOFI FI Private Fund

Source: Fidelity International, 2018. *Fidelity International, 3Q18. * Includes Boston managed assets of \$11.6bn of assets.
 1) Chinese Government Bonds, 2) State Development Bank of China

New onshore bond strategies

Fully integrated on-the-ground investment team

4



Fidelity Asian Fixed Income Funds in Onshore China

- Fidelity Multi-Asset onshore CGB-SDBC Pool
- Fidelity China Bond No.1 Private Fund*
- Fidelity China Bond Opportunity No.1 Private Fund*

Onshore China Bond Market Yield Curves

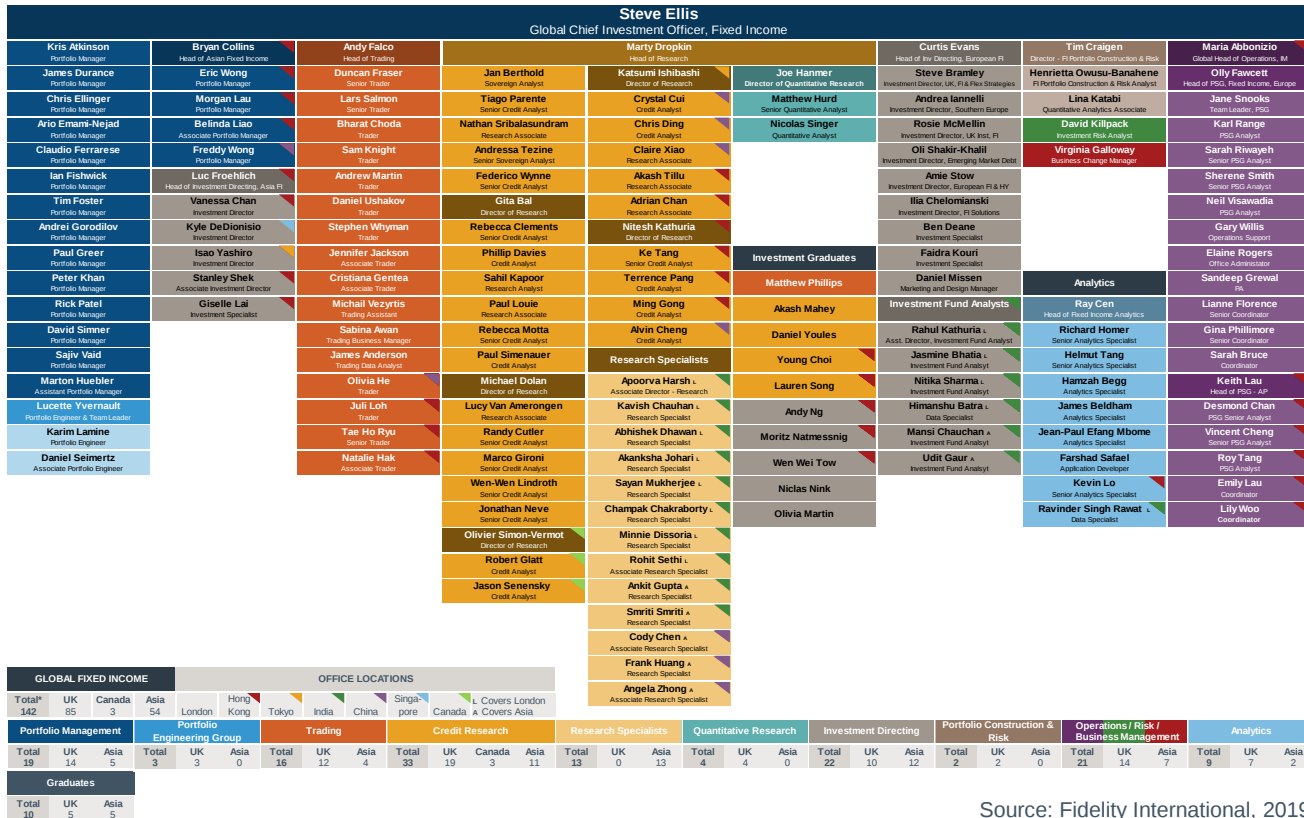
- Onshore China Government Bond (CGB)
- Onshore China Development Bank Bond (SDBC)
- Onshore AAA Rated Corporate (~ AA/A Int'l Rating)
- Onshore AA Rated Corporate (~ BBB/BB Int'l Rating)
- Onshore A Rated Corporate (~ B Int'l Rating)

Past Performance is not a reliable indicator of future results. The value of shares may fluctuate and can not be guaranteed.

Source: Fidelity International, WIND, as of 3 February 2019. * Only available for onshore institutional or private clients

Fixed Income Organisation Structure

4



Source: Fidelity International, 2019.

Chinese Bonds

Summary

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Why?

- Higher risk-adjusted returns
- Alpha opportunities increasing
- Diversification benefits
- Index inclusion

2

Characteristics: Different but similar

3

Risk: Consider China like any other market

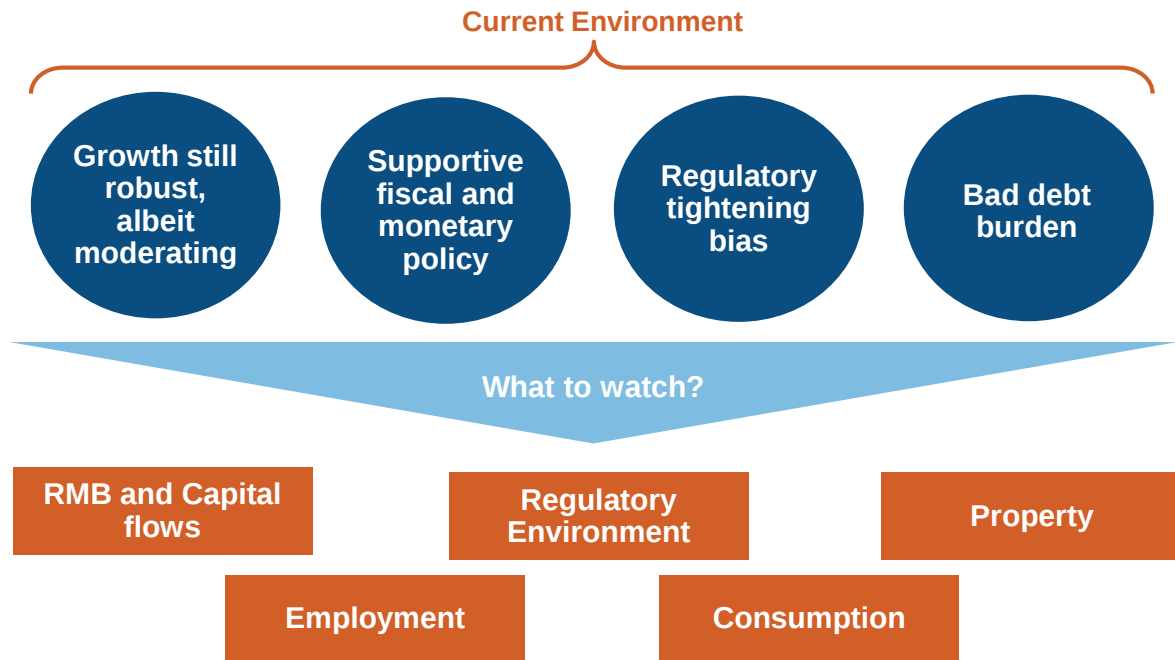
4

Fully integrated on-the-ground investment team

Appendix

China

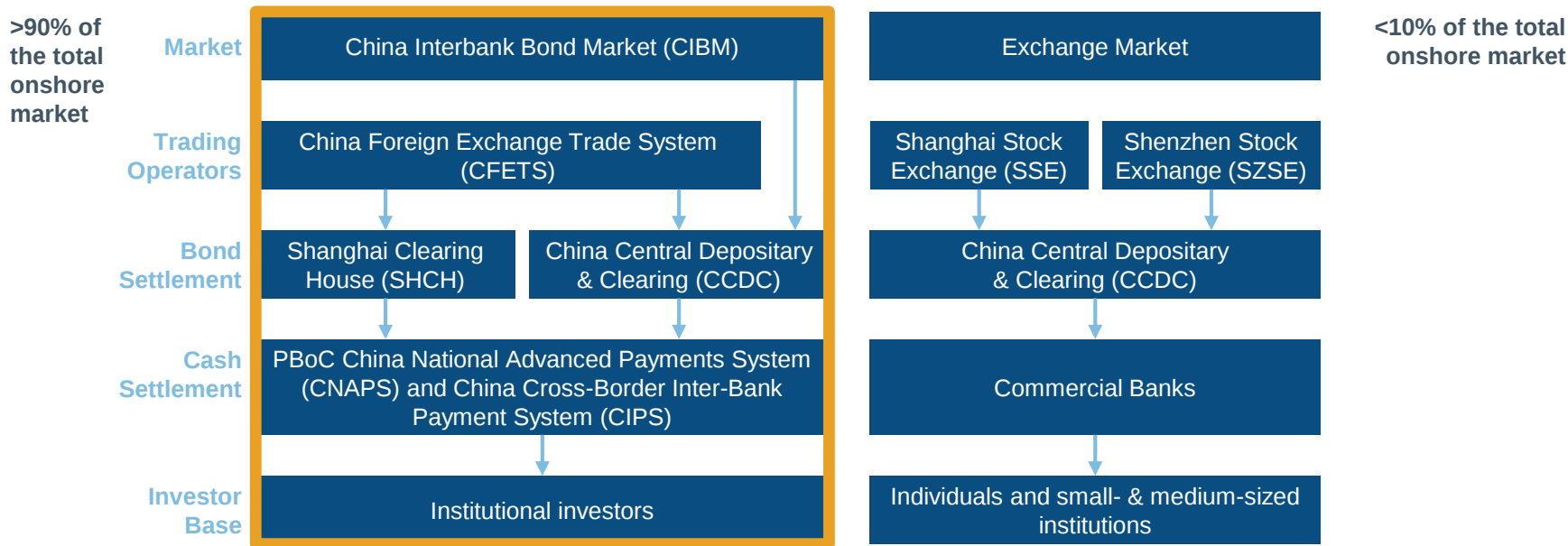
Generally supportive backdrop and manageable near-term risks



Reference in this document to specific securities should not be construed as a recommendation to buy or sell these securities, but is included for the purposes of illustration only. Investors should also note that the views expressed may no longer be current and may have already been acted upon by Fidelity International.
Source: Fidelity International, 2018.

Onshore bond market structure overview

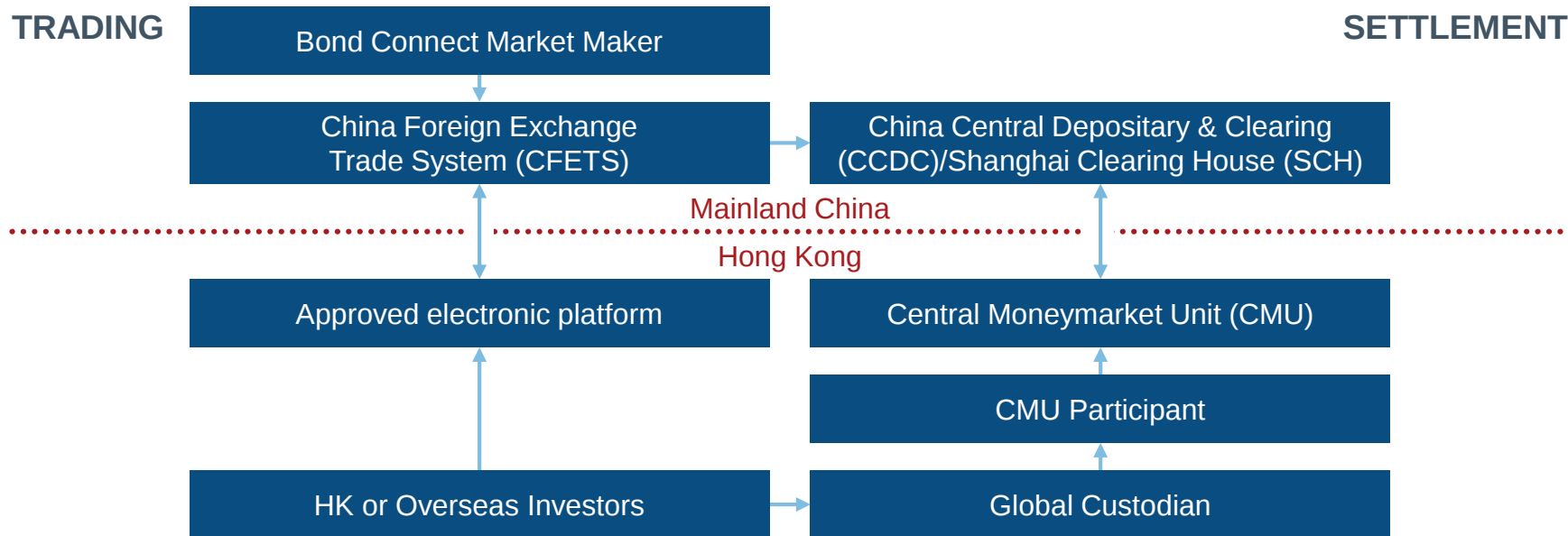
Focus on CIBM (China Interbank Bond Market)



Source: Fidelity International, NAFMII, ADB, 2018.

China “Bond Connect” mechanism

Operational



Source: PBoC, HKMA, Citi Research, 2018.

Scope of local Chinese bonds that will be added

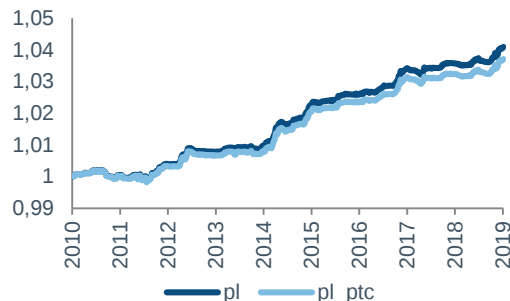
Chinese Treasury and Policy Bank Debt Being Included in the Global Aggregate Index

Issuer	Ticker	Count	MV (CNY tn.)	Amt Out (CNY tn.)	MV (USD tn.)	Amt Out (USD tn.)	Duration (Years)	YTW (%)
China Government Bond	CGB	159	10,400.5	9,992.7	1,551.0	1,490.2	6.69	3.00
China Development Bank	SDBC	102	6,558.2	6,272.4	978.0	935.4	4.78	3.37
Agricultural Development Bank	ADBCH	58	3,321.5	3,192.5	495.3	476.1	4.08	3.33
Export-Import Bank of China	EXIMCH	45	2,002.0	1,926.4	298.6	287.3	3.86	3.31
Total		364	22,282.1	21384.0	3323.0	3189.0	5.49	3.19

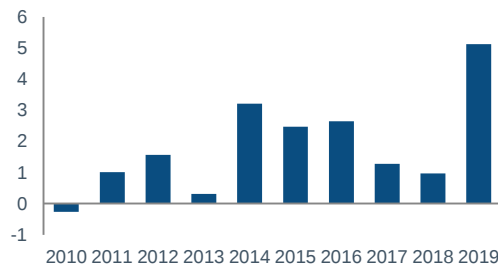
Source: Bloomberg, 31 January 2019.

China Duration Model

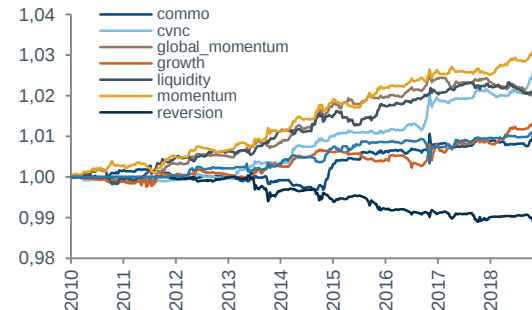
Cumulative Performance



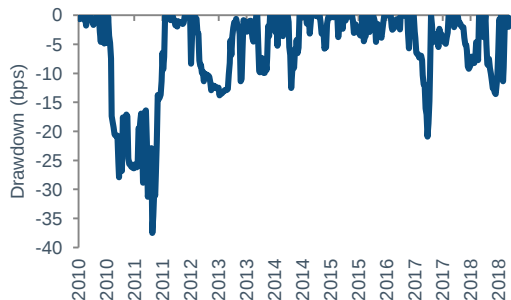
Information Ratio per year post transaction cost (ptc)



Performance by Signal



Underwater Plot @ 25.05 bp



Signal Correlation (W)

	Commo	Cvnc	Global momentum	Growth	Liquidity	Momentum	Reversion
Cvnc	0.51						
Global momentum	0.50	0.61					
Growth	0.36	0.69	0.43				
Liquidity	0.17	0.16	0.24	0.25			
Momentum	0.35	0.55	0.53	0.55	0.28		
Reversion	-0.32	-0.47	-0.47	-0.49	-0.22	-0.82	
Slope	-0.24	-0.31	-0.06	-0.27	-0.06	-0.03	-0.08

Past Performance is not a reliable indicator of future results. The value of shares may fluctuate and can not be guaranteed.

Source: Fidelity International, 31 January 2019. pl = profit and loss; ptc = post transaction cost

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