# The Asian USD High Yield Credit Bond Market

A complement to traditional high yield exposures?

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## A complement to traditional high yield exposures?

### Overview

Following our Asian USD credit primer published last month, we further probe the high yield segment of the Asian (ex-Japan) USD credit bond market. We explore the segment's rapid growth, sector exposures, spreads, and correlations with other asset classes. We also discuss how Chinese issuers play a significant role in this segment. In this article, we will be using relevant IHS Markit iBoxx fixed income benchmarks to represent the major high yield bond markets.

Key observations indicate that Asian USD high yield credit:

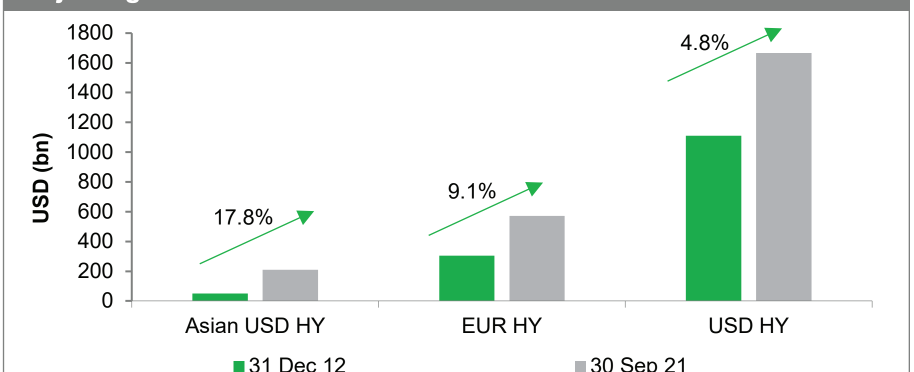
- Currently has a lower level of passive assets tracking it compared with other major high yield credit markets.
- May act as a credible diversifier to a USD and EUR high yield credit portfolio.
- Has significant exposure to China issued USD bonds by market value.
- Can offer a reasonable level of bond liquidity for calibrated portfolios.

- **Asian USD HY** is represented by *iBoxx USD Asia ex-Japan Corporates High Yield 1+* index. **EUR HY** is represented by *iBoxx EUR High Yield cum-crossover* index in USD, unhedged. **USD H**Y is represented by iBoxx *USD Developed Markets High Yield* index. Both EUR HY and USD HY are 1+ indices.
- In the following analysis, the start date of the analytical data used is 31 December 2012, as this is the earliest available data across all indices used in this article. Unless otherwise stated, all data is as of 30 September 2021.

With a total market value of $209 billion, Asian USD high yield credit bonds currently represent less than 10% of the combined EUR and USD high yield credit bond markets. Although still smaller than each of the EUR high yield and developed USD high yield markets, the Asian market has undergone considerably faster growth, measured at 17.8% compound annual growth rate (CAGR) since 31 December 2012.

Chart 1

Major High Yield Bond Markets CAGR




Source: IHS Markit Indices © 2021 IHS Markit

## Breakdown of the Asian USD high yield credit bond market

Chart 2

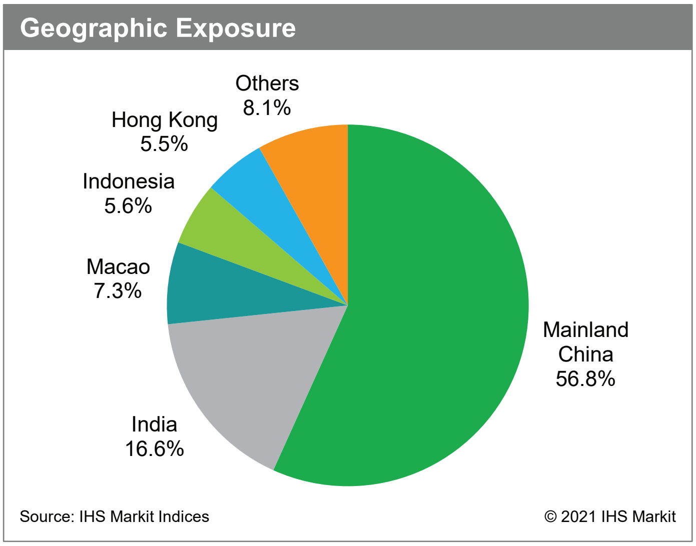
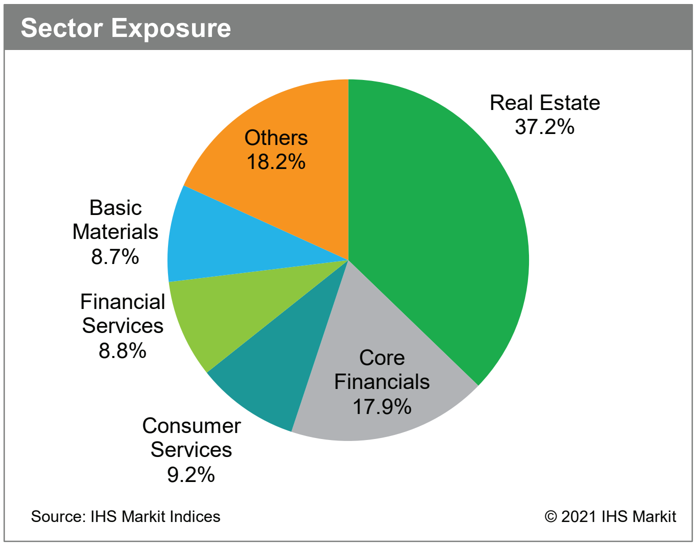
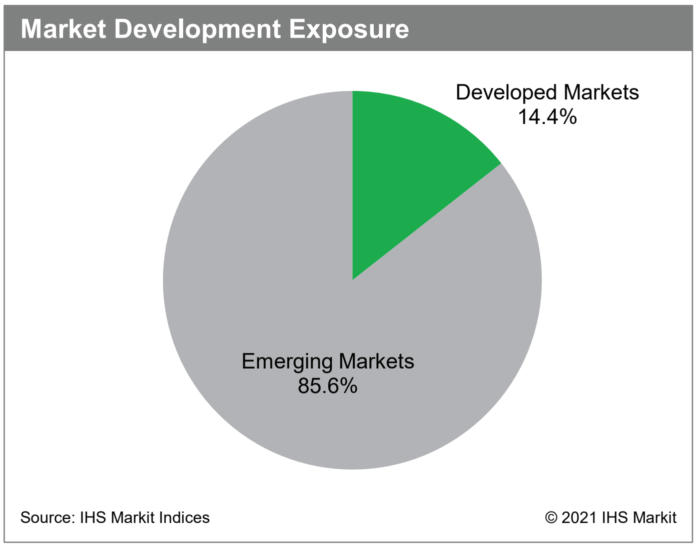



Chart 3




Asian USD HY is dominated by exposure to Asian emerging markets (85.6%), with mainland China (56.8%) and India (16.6%) carrying the largest weights. Hong Kong, Macao, and Singapore account for the developed markets exposure (14.4% of the index). The much-talked-about real estate sector makes up 37.2% of the index, of which over 90% are Chinese issuers by market value.

Chart 4




Various factors contributed to the growth in the Asian dollar high yield credit bond market. The opening of China to the rest of the world in recent times is one major factor, as China represents more than half of the Asian USD HY by market value. One key development was captured in a Circular[1] issued by the State Council of China in January 2017, outlining the measures to reduce market access restrictions for foreign investments. The growth in China USD bond issuance, however, was not monotonic. According to analysis by the International Capital Market Association (ICMA), China offshore bond issuance grew in 2017 before dwindling from the second quarter of 2018 until the rest of the year. This was due to stricter restrictions introduced by the National Development and Reform Commission (NDRC) for onshore companies, particularly local government financing vehicles (LGFVs), to reduce leverage via offshore financing.[2] New China USD issuances then picked up again in 2019. Since 2017, we have witnessed a 26.7% CAGR in China issued high yield USD bonds[3] that has outpaced the rate of increase in the wider Asian USD HY ex-China market (19.6% CAGR).

Increased investor sophistication and the continued chase for yield (over prolonged periods of low global risk-free rates) also supported the growth in the Asian USD bond market, including the high yield segment.

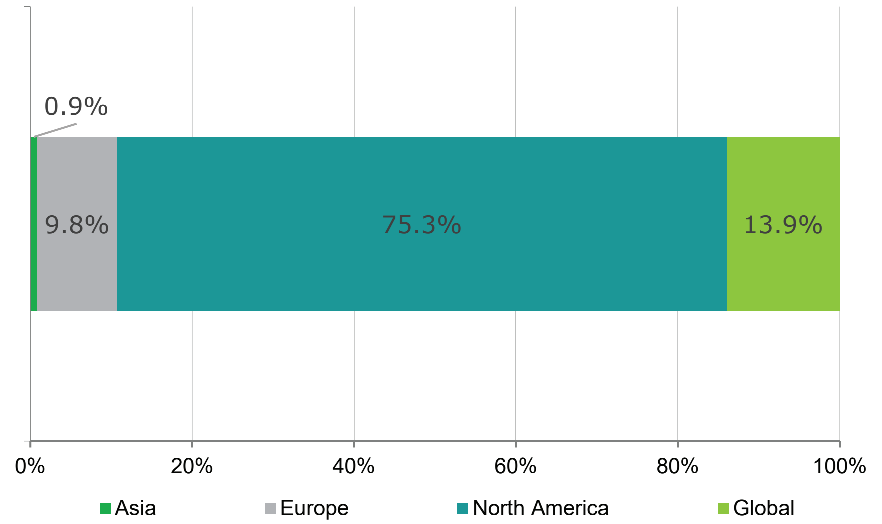
1. For further commentary on the circular, please refer to the Client Alert Commentary from Latham & Watkins published in January 2017.
2. According to the report titled 'The Internationalization of the China Corporate Bond Market' from ICMA published in January 2021.
3. Represented by *iBoxx USD Asia ex-Japan China Corporates High Yield 1+* index.

## An overlooked asset class?

In this section, we examine the assets under management (AUM) that exchange traded funds (ETFs) hold in the major high yield credit markets. Most ETFs are passively managed and track a specific market index. Therefore, liquidity in the underlying assets managed by ETFs is critical for the fund manager. Asian USD high yield credit bonds indeed exhibit generally poorer liquidity compared with their investment grade counterparts, which might be one of the reasons for the low number of ETFs tracking the Asian USD high yield credit segment today (see the 'Liquidity' section below where we discuss ways to improve the liquidity of Asian USD high yield corporate bonds portfolios from an index perspective).

Chart 5

High Yield ETF AUM by geographical expsoure of underlying assets




Source: IHS Markit EBS © 2021 IHS Markit

Despite its growth over the last few years, ETF AUM against the Asian USD high yield credit market remains small (see Chart 5). The regional disparity is clear, with HY ETF AUM highly concentrated in North America (mostly USD). Meanwhile, Europe HY (mostly EUR) and Asian USD high yield account for 9.8% and a paltry 0.9%, respectively.

Table 1 evaluates the ETF AUM in each region compared with the market value of the closest comparator high yield fixed income index.[4] The difference is quite clear to see as the Asian USD HY ratio is trivial compared with Western markets.

Table 1

| ETF AUM / Market Size* | |
|---|---|
| Asian USD HY | 0.5% |
| EUR HY | 2.2% |
| USD HY | 4.9% |

* ETF AUM is estimated based on IHS Markit Eclipse. Market value is estimated based on the underlying index market value of Asian USD HY, EUR HY and USD HY as defined in page 3.

Source: IHS Markit EBS and IHS Markit Indices © 2021 IHS Markit

## Attractive carry and risk profile

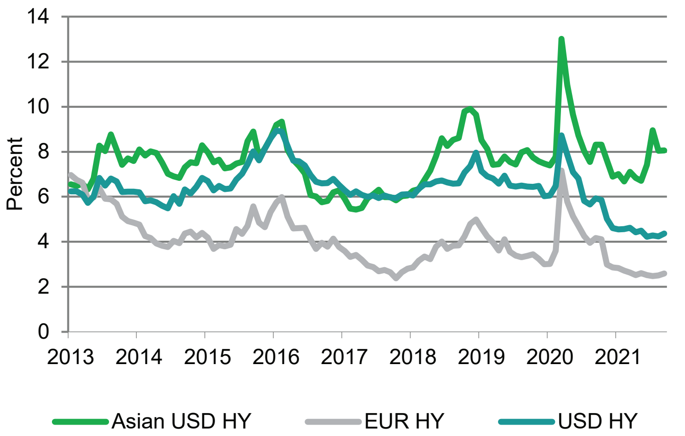
In recent years, investing in Asian USD HY has generally provided greater yield than its HY counterparts in the EUR and USD markets (Chart 6). This yield differential may be attributed to a confluence of risk factors such as liquidity and emerging market credit risk premiums. After all, the Asian market is smaller than major developed markets and is comprised mostly of emerging market issuers. Currently, the option-adjusted spread (OAS) pick-up relative to other high yield markets is at a multi-year high as shown in Chart 7.

Moreover, Asian USD HY bonds have lower durations, on average, than comparable EUR HY and USD HY bonds, making them less vulnerable to rising interest rates (Chart 8). In general, bonds in the Asian USD HY market are mostly under five years in maturity and a majority of the issuers come from the Real Estate, Core Financials, and Financial Services sectors. Chart 9 highlights the yield-over-duration ratios for Asian USD HY, EUR HY, and USD HY over the past eight years. The Asian USD HY market has consistently offered extra yield carry at lower durations since 2014.

4. 100% of Asian USD HY bonds have exposure to Asia ex-Japan. 84.3% of EUR HY bonds have exposure to Europe. 90.0% of US HY bonds have exposure to North America.

Chart 6

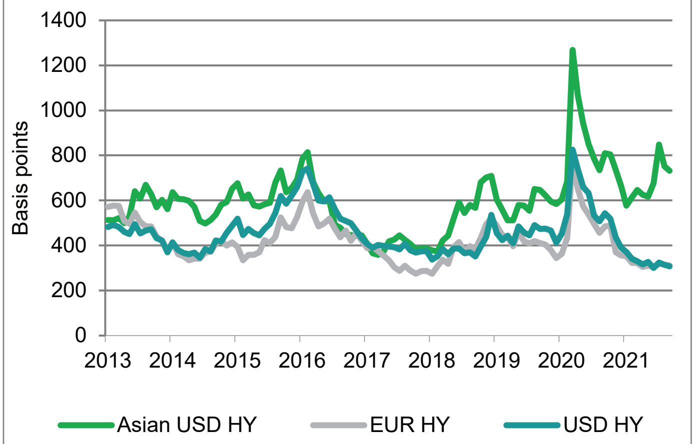
**Annual yield of HY credit**




Source: IHS Markit Indices © 2021 IHS Markit

Chart 7

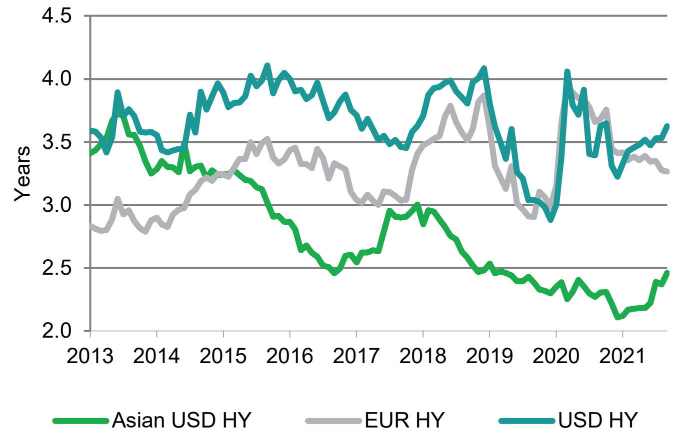
**Option-adjusted spread of HY credit**




Source: IHS Markit Indices © 2021 IHS Markit

Chart 8

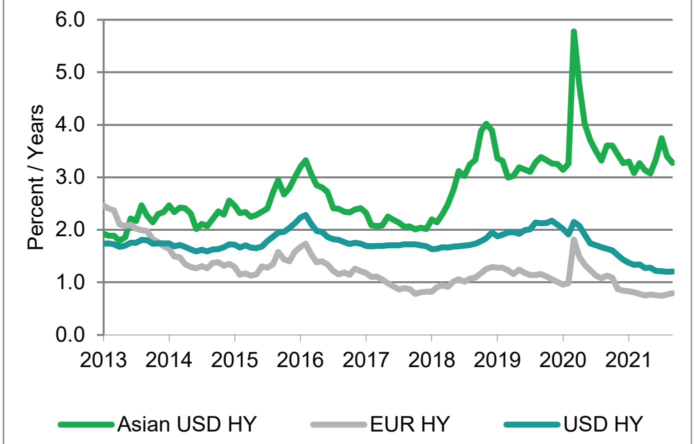
**Annual modified duration of HY credit**




Source: IHS Markit Indices © 2021 IHS Markit

Chart 9

**Yield over duration of HY credit**




Source: IHS Markit Indices © 2021 IHS Markit

Additionally, Asian USD HY typically offers larger interest income than high yield bonds in other markets. This source of income can be beneficial to investors in times of market downturns. At present, the average coupon rate offered by Asian USD HY is about 6.5%; higher than those observed in EUR HY and USD HY by about 297 bps and 75 bps, respectively.

## Historical performance

From January 2013 to September 2021, Asia's USD high yield credit bond market largely outperformed the EUR comparator market but moderately fell behind the USD HY market on a risk-adjusted basis (Table 2). With lower duration than high yield bonds in other markets, Asian USD HY displayed 1.7 times greater spread volatility than USD HY during the sample period, which may explain its underperformance against the USD HY market.

Over the past 8.8 years, Asian USD HY delivered the second-highest annualised return and had the lowest maximum drawdown. This asset class posted positive monthly returns more than two-thirds of the time despite the occurrence of several regional geopolitical, as well as global risk events[5] over the same period.

Table 2

**Performance in HY credit bond markets**
On monthly USD unhedged returns

| Index | Annualised Return (%) | Annualised Volatility (%) | Return / Volatility | Maximum Drawdown (%) | OAS Volatility (%) |
|---|---|---|---|---|---|
| **From Jan 2013 to Sep 2021** | | | | | |
| Asian USD HY | 4.7 | 7.3 | 0.6 | 12.1 | 280.3 |
| EUR HY | 3.3 | 10.6 | 0.3 | 22.0 | 178.8 |
| USD HY | 5.6 | 6.7 | 0.8 | 13.1 | 165.2 |
| **From Jan 2021 to Sep 2021** | | | | | |
| Asian USD HY | -8.6 | 8.8 | -1.0 | 8.4 | 280.4 |
| EUR HY | -2.2 | 6.7 | -0.3 | 3.8 | 42.8 |
| USD HY | 6.3 | 1.5 | 4.1 | 0.1 | 57.8 |

Source: IHS Markit Indices © 2021 IHS Markit

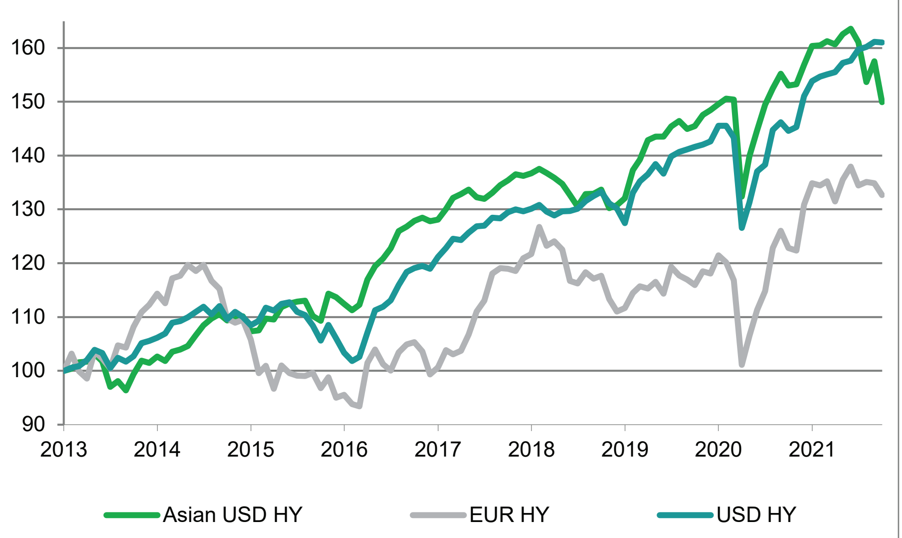
However, 2021 has been a challenging year so far for Asian high yield bonds. Several high-profile events in the China real estate sector that caused spreads to spike have heightened investor concern (see 'The role of China' section below where we discuss the Chinese real estate sector further). Meanwhile, growth prospects[6] outside of Asia have been improving since the end of 2020, particularly in the US market. With strong economic data, backed by co-ordinated fiscal and monetary effort from central banks and continued progress on vaccine distribution and inoculations, global economic recovery has been gaining momentum. Against this backdrop, Asian USD HY has underperformed USD HY (and EUR HY) year-to-date.

Looking back at the most recent global crisis in history, however, Asia's economic and market resilience over developed markets placed it in a unique position when financial markets experienced widespread systemic volatility.

As illustrated in the first quarter of 2020, when global credit spreads widened sharply due to the outbreak of the COVID-19 pandemic, the performance of Asian USD HY bonds (-11.5%) fared better than those of EUR HY (-16.8%) and USD HY (-13.1%). Subsequently, the rebound in April 2020 saw greater strength in Asian USD HY (+5.7%) than in the EUR HY (+5.4%) and USD HY (+3.8%) markets.

Chart 10

**Performance of HY credit**




Source: IHS Markit Indices © 2021 IHS Markit

5. These events included the US taper tantrum in 2013; market pessimism of China's economy heading for a hard landing in 2015; uncertainty around several major regional elections in Asia; the deterioration of US-China trade relationship in 2018 and the outbreak of COVID-19 pandemic in 2020.

6. See article "Global Economic Recovery: Overview of World's Top Economies" by IHS Markit.

## Diversification benefit

Asia has become an integral part of the world's growth engine over the past several decades. Home to over 20 developing countries, Asia and its trade-dependent economies differ considerably from those of the West—from demographics to consumer behaviour and from economic development to capital market financing needs. This diversity in market fundamentals highlights the potential diversification benefits of introducing Asian USD HY bonds to a global high yield portfolio.

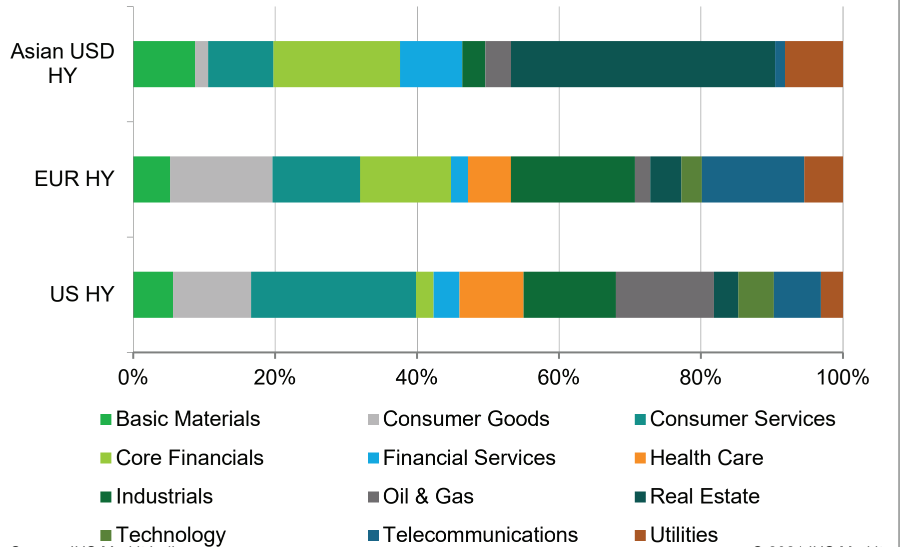
### Variation in sector exposure

Chart 11 shows the differences in sector breakdown across the major high yield credit bond markets. The Asian USD HY has the highest weight by market value in the Real Estate sector (37.2%), while the US HY and EUR HY have highest exposures to Consumer Services (23.2%) and Industrials (17.5%), respectively.

The Asian USD HY has limited exposure to Consumer Services and Oil & Gas sectors which were hit hard by the COVID-19 shockwave. Adding Asian USD HY to a traditional US and EUR HY portfolio may help soften the volatility impact if further challenges appear as global economies seek to recover to pre-pandemic levels.

Chart 11

**Sector exposure of major HY credit bond markets**




Source: IHS Markit Indices © 2021 IHS Markit

### Exposure to factors other than USD risk-free rate

In view of yield change correlation, both Asian USD HY and USD HY have low negative correlation with US 10-year treasuries over the sample period (as seen in Table 3). When looking at high yield spread changes versus USD rates, the negative sample correlations become more significant, but with Asian USD HY less negatively correlated to USD rates than USD HY is. These observations indicate that there might be other non-common risk factors driving the yield and spread changes of the Asian USD high yield bonds besides USD risk-free rate.

Table 3

**Correlations of HY credit bonds with US treasuries**
On monthly index yield and OAS changes since Jan 2013

| Index | US 10-yr constant maturity treasury |
|---|---|
| **Yield change correlations** | |
| Asian USD HY | -10.6% |
| USD HY | -7.4% |
| **OAS change correlations** | |
| Asian USD HY | -29.1% |
| USD HY | -46.5% |

Source: IHS Markit Indices and US 10-year treasury constant maturity yield data from Federal Reserve Economic Data (FRED) database. © 2021 IHS Markit

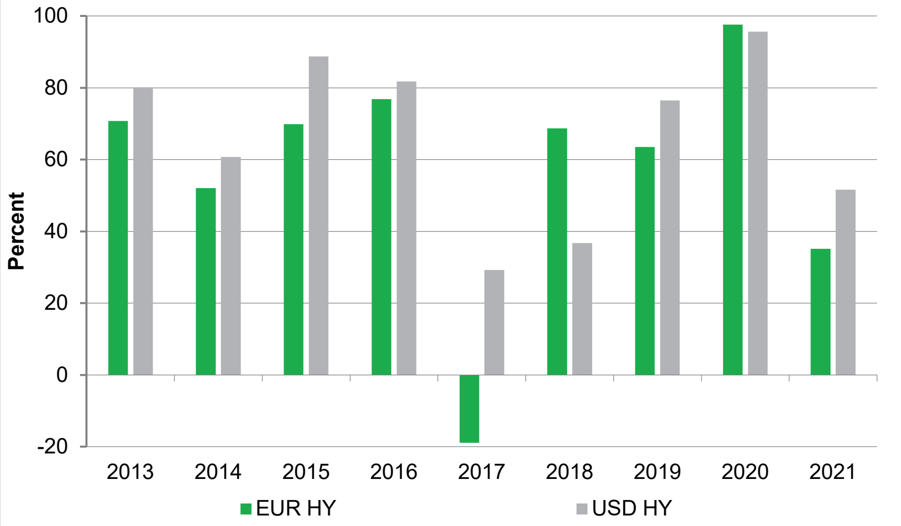
## Imperfect OAS correlations with other HY markets

Chart 12 shows how the yearly correlations of Asian USD HY OAS with OAS of other high yield asset classes have varied over time since 2013.

The average OAS correlation between Asian USD HY and USD HY is moderately high at 66.8%, while with the European market, the correlation is moderate at 57.3%. Of course, the pandemic was an ex-ante undiversifiable systemic risk event that severely battered the global economy. This impact was reflected in the unequivocal increase of the yearly spread correlations to above 95% in 2020.

Chart 12

**Asian USD HY OAS correlations against other HY**




Source: IHS Markit Indices © 2021 IHS Markit

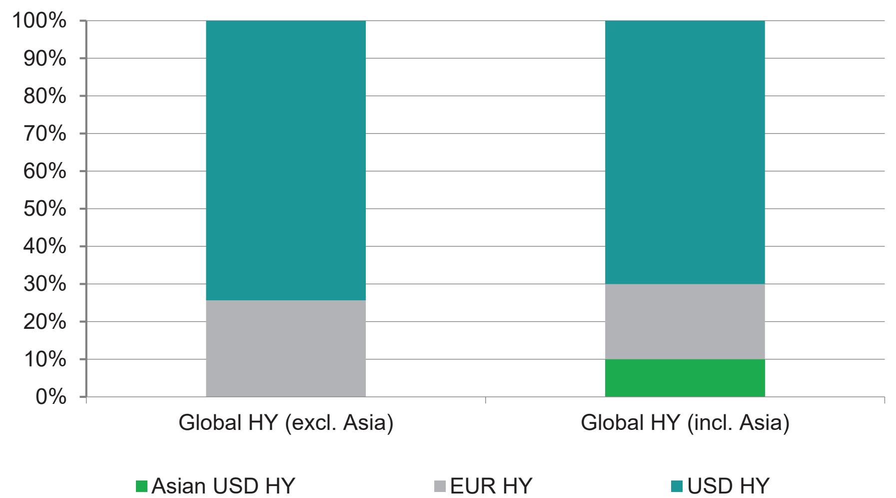
## Inclusion of Asian USD HY to a traditional high yield credit portfolio

To examine the impact of combining Asian USD HY bonds to a traditional high yield portfolio, we compare the performance of two sample portfolios[7]—Global high yield (excl. Asia) and Global high yield (incl. Asia)—from January 2013 to September 2021. These sample portfolios are constructed in USD, unhedged.

Table 4 shows Global HY (incl. Asia) marginally outperformed the Global HY (excl. Asia) on a risk-adjusted basis over the past 8.8 years. Between the two sets of global high yield credit portfolios, the one that included Asian USD HY posted slightly lower annualised volatility and maximum drawdown.

Chart 13

**Sample allocations in global HY credit portfolios**




Source: IHS Markit Indices © 2021 IHS Markit

7. **Global high yield (excl. Asia)** combines **USD HY and EUR HY** using market value weights, which is the conventional universe investors look at when seeking for high yield opportunities. **Global high yield (incl. Asia)** as represented in Chart 13 and Table 4 combines **USD HY, EUR HY and Asian USD HY** with an allocation of 70%, 20% and 10% respectively.

Table 4

**Performance of global HY credit and equity portfolios (USD unhedged returns)**

| Index/sample portfolios | Annualised Return (%) | Annualised Volatility (%) | Return / Volatility | Maximum Drawdown (%) | Correlation vs EMIX World (%) |
|---|---|---|---|---|---|
| **From Jan 2013 to Sep 2021** | | | | | |
| Global HY (incl. Asia) | 5.09 | 7.03 | 0.72 | 13.66 | 83.75 |
| Global HY (excl. Asia) | 5.06 | 7.17 | 0.71 | 13.93 | 83.28 |
| World Equities | 11.39 | 13.23 | 0.86 | 20.94 | 100.00 |

Source: IHS Markit Indices © 2021 IHS Markit

Focusing on the period Jan 2013 to Dec 2020 (thus excluding the unfolding real estate crisis in China) we observe Global HY (incl. Asia) outperformed Global HY (excl. Asia) by 14 bps in annualised returns (5.29% vs 5.15%), and by 3 bps on a risk-adjusted basis (0.72 vs 0.69).

For the full period analysis, we also include the performance of World Equities[8] in Table 4, as some investors may view holding high yield bonds as equity-like exposure.

Both global high yield sample portfolios underperformed against global equity on a risk-adjusted basis, but their returns were highly correlated at above 80%. While high yield bonds displayed less upside in annualised return compared to global stocks, they were markedly less volatile (at 7.0 or 7.2%, annualised) compared with global equity (at 13.2%). Moreover, both global high yield portfolios exhibited lower maximum drawdowns, suggesting high yield bonds may have better downside protection than stocks during market turmoil.

## The role of China

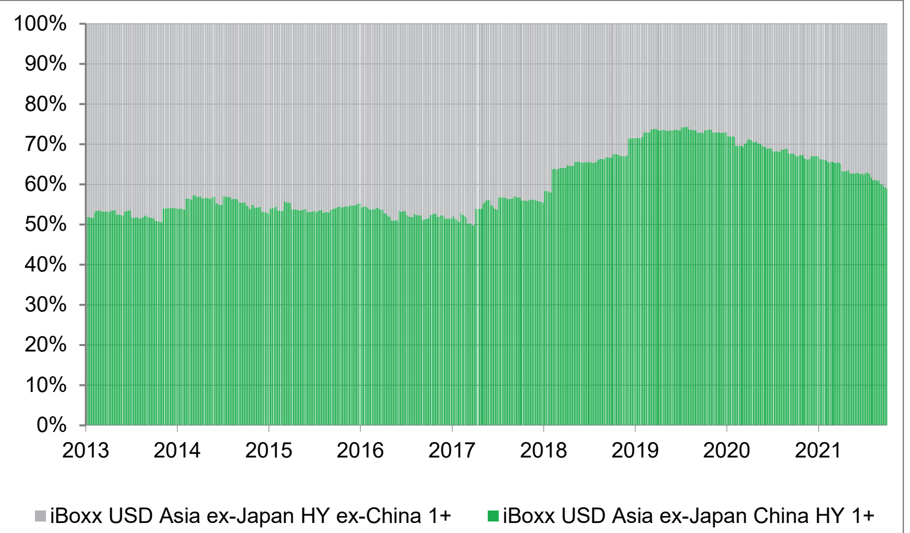
Along with the emergence of China, the China USD high yield bond market has grown rapidly over the past decade.

The representation of China-issued USD bonds in Asian USD HY has a market value of more than USD 120 billion and makes up 59.0% of the index, having peaked in July 2019 when they accounted for 74.4%.[9]

While more than half of the issuance are BB-rated (62.9%)[10], the China dollar high yield market is skewed towards shorter maturities, with over 95% of the bond outstanding amount below five years in maturity. The market is also heavily concentrated in the Real Estate sector, with approximately 60.2% of the total issuance from China real estate issuers.

Chart 14

**China HY Market Value representation in Asian USD HY**




Source: IHS Markit Indices © 2021 IHS Markit

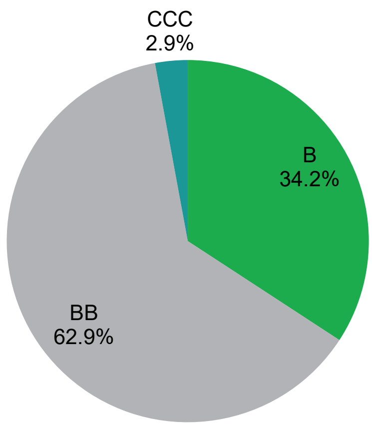
8. **World Equities** is represented by EMIX World index

9. Please note that on 31 January 2018, the jump in market value, as depicted in Chart 14, was largely due to a change in the index methodology which allowed unrated bonds to enter the index.

10. According to the *iBoxx USD Asia ex-Japan China Corporate High Yield 1+* index.

Chart 15

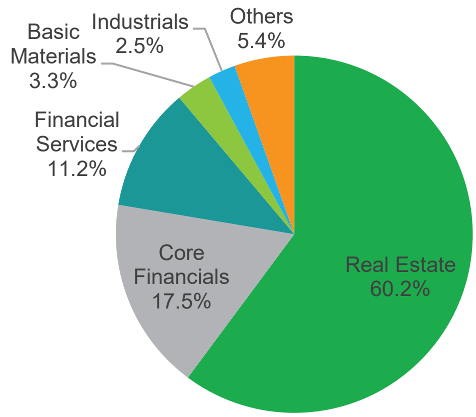
**China USD HY Ratings Breakdown**




Source: IHS Markit Indices © 2021 IHS Markit

Chart 16

**China USD HY Sector Breakdown**




Source: IHS Markit Indices © 2021 IHS Markit

At the time of writing, the China dollar high yield market has underperformed of late as one of the largest property developers, Evergrande Group, has fallen into a liquidity crisis. Furthermore, worries over possible contagion effects emanating from the Evergrande Group have spilled over to other real estate developers.[11] Fantasia Holdings—another property developer based in Shenzhen—followed suit as they missed their debt obligation in early October. Modern Land (China) based in Beijing has also asked for an extension to repay its debt due late October. Questions have surfaced as to whether the Chinese government will intervene to prevent a ripple effect on the economy. There would likely be repercussions regardless of the decision they make and only time will tell. Some would argue that it is only natural for defaults to arise as the market liberalises, and that this process may weed out poorly managed companies from the system, thus strengthening the market in the long run.

Having said this, the China USD Real Estate high yield sector is not dominated by one or two major issuers. In fact, it is quite diversified with over 50 issuers. As shown in Table 5, the top 5 issuers account for approximately one-third of the sector by market value, and the largest issuer has a weight of approximately 10.3%.[12]

Table 5

**Top 5 issuers in the China USD HY Real Estate sector**

| Issuer | % Weight |
|---|---|
| Kaisa Group Holdings Ltd | 10.3% |
| Sunac China Holdings Ltd | 7.9% |
| CIFI Holdings Group Co Ltd | 5.1% |
| Yuzhou Properties Co Ltd | 4.9% |
| Agile Group Holdings Ltd | 4.7% |

Source: IHS Markit Indices © 2021 IHS Markit

11. Recent issuers in the China real estate sector who have missed their offshore USD bond payments include China Fortunate Land Development Co., Sichuan Languang Development Co, Oceanwide Holdings Co, Tus-Holdings Co, China Evergrande Group, and most recently, Fantasia Holdings and Modern Land (China).

12. Bonds from China Evergrande Group were removed in the 30 September 2021 index rebalance as they were trading flat of accrued interest.

The following section examines the performance of China USD Real Estate high yield over time and compares it against the broader China USD and Asian USD high yield markets.

The recent events surrounding Evergrande might have a knock-on effect in the China real estate industry. Market participants are monitoring the distress situation closely as it continues to develop. However, it is worth noting that the historical annualised returns of the real estate index have been higher compared with the wider China USD high yield and Asian USD high yield indices over a long investment horizon.

Based on the historical performance in Table 6, broader indices have shown higher risk-adjusted returns. Investors who are more risk-sensitive might want to look at the Asian USD HY portfolio as the risk-return profile may be more palatable.

Table 6

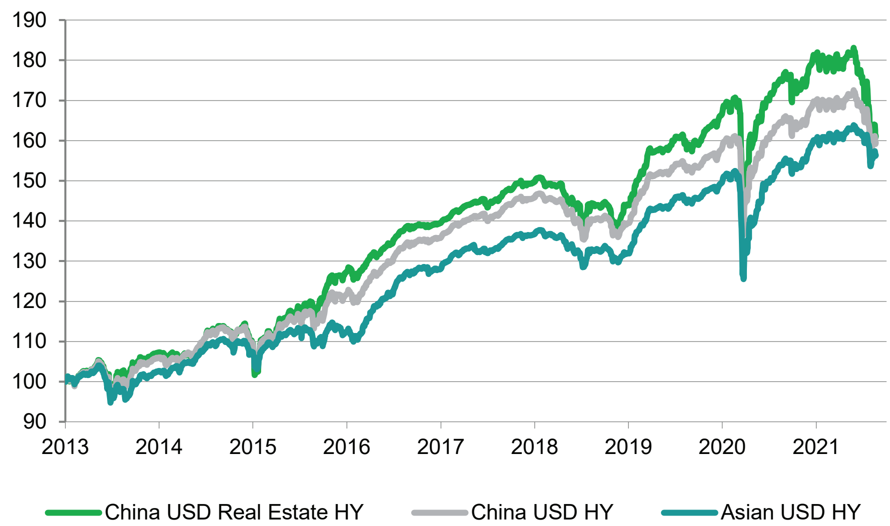
**Performance**
31 Dec 2012 to 30 Sep 2021

| | Annualised Return (%) | Annualised Volatility (%) | Return / Volatility |
|---|---|---|---|
| China USD Real Estate HY* | 5.6 | 6.2 | 0.9 |
| China USD HY | 5.5 | 4.9 | 1.1 |
| Asian USD HY | 5.2 | 4.4 | 1.2 |

*China USD Real Estate HY refers to *iBoxx USD Asia ex-Japan China Real Estate High Yield 1+* index, and China USD HY refers to *iBoxx USD Asia ex-Japan China Corporates High Yield 1+* index
Source: IHS Markit Indices © 2021 IHS Markit

Chart 17

**China USD Real Estate HY Returns**




Source: IHS Markit Indices © 2021 IHS Markit

## Risks remain, but more so than other high yield markets?

There are certainly more risks associated with sub-investment grade assets compared with ones with higher credit quality. However, as discussed above, we have seen more flows into ETFs tracking EUR and USD high yield fixed income assets. Does this mean that ETF investors have shunned Asian USD high yield bonds thus far because of higher perceived risk?

To put things in perspective, we compare defaults across global high yield in recent years (see Table 7).

Year-to-date, there have been increasing defaults in the Asian USD high yield space, largely contributed to by Chinese real estate issuers. However, if we take a step back and look at the picture across the major markets, the average yearly notional defaulted since 2015 as a proportion of index notional of Asian USD HY is not distinctly higher than that of EUR HY and USD HY.

Table 7

**Issuer defaults / traded flat**

| No. of issuer defaults | Asian USD HY | EUR HY | USD HY | Notional defaulted as a proportion of index notional | Asian USD HY | EUR HY | USD HY |
|---|---|---|---|---|---|---|---|
| 2015 | 2 | 3 | 28 | 2015 | 3.2% | 2.4% | 2.6% |
| 2016 | 3 | 6 | 40 | 2016 | 1.9% | 2.3% | 2.7% |
| 2017 | 2 | 7 | 31 | 2017 | 1.0% | 1.1% | 1.2% |
| 2018 | 3 | 3 | 21 | 2018 | 1.0% | 0.6% | 1.9% |
| 2019 | 3 | 6 | 25 | 2019 | 0.7% | 1.0% | 2.1% |
| 2020 | 3 | 7 | 46 | 2020 | 0.9% | 1.2% | 5.0% |
| 2021 YTD | 5 | 6 | 7 | 2021 YTD | 8.4% | 0.6% | 0.1% |
| **Average** | **3** | **6** | **29** | **Average** | **2.4%** | **1.4%** | **2.3%** |

Source: IHS Markit Indices

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# Liquidity

Liquidity in the Asian USD credit market has long been a concern amongst investors, especially in relation to the high yield segment. It is indeed true that Asian USD high yield bonds are less liquid than their investment grade counterparts, as you can see from liquidity scores computed by the IHS Markit Pricing and Reference Data service (displayed in Table 8). The liquidity score ranges from 1 to 5, with 1 being the most liquid and 5 being the least liquid.[13]

Table 8

**Liquidity Score (Based on bond count)**

| Index / Universe | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| Asia USD Investment Grade Universe[1] | 77.9% | 9.6% | 3.3% | 2.7% | 6.6% |
| iBoxx USD Asia ex-Japan Corporates IG[2] | 85.6% | 11.9% | 2.0% | 0.4% | 0.2% |
| Asia USD High Yield Universe | 43.3% | 11.7% | 9.9% | 10.4% | 24.7% |
| iBoxx USD Asia ex-Japan Corporates HY | 82.8% | 11.1% | 2.9% | 1.9% | 1.2% |

[1] The Asia USD IG and HY Universe represents the entire set of Asian IG and HY bonds that are covered by IHS Markit's Evaluated Bond Pricing service.

[2] The *iBoxx USD Asia ex-Japan Corporates IG and HY* indices have a minimum notional outstanding of USD$250 million for bonds to be eligible for the index. This threshold significantly improves the liquidity scores of the underlying bonds.

Source: IHS Markit Evaluated Bond Pricing

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One way to improve the liquidity of an underlying portfolio is to set a minimum issuer notional amount outstanding for bonds to qualify for a liquid portfolio. Typically, issuers with larger bonds or multiple smaller bonds tend to be more frequently traded by market participants as compared with small one-off issuances. In Table 9 below, the second Asian USD HY index includes an issuer floor of USD 400m notional outstanding.

Table 9

**Liquidity Score (Based on bond count)**

| Index / Universe | Market Value | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|---|
| iBoxx USD Asia ex-Japan Corporates High Yield | 100.0% | 82.8% | 11.1% | 2.9% | 1.9% | 1.2% |
| iBoxx USD Asia ex-Japan Corporates High Yield ($400m min issuer notional) | 89.6% | 89.6% | 8.4% | 1.7% | 0.3% | 0.0% |
| iBoxx MSCI ESG USD Asia ex-Japan High Yield Capped[1] | 48.4% | 94.6% | 5.0% | 0.4% | 0.0% | 0.0% |

[1] The *iBoxx MSCI ESG USD Asia ex-Japan High Yield Capped* index is jointly developed with Tabula Investment Management and Haitong International Asset Management. The index has a minimum issuer notional of USD400 million and applies ESG screens based on MSCI ESG Research data. The index weight is also tilted according to MSCI ESG ratings and rating momentum. Lastly, an issuer and sector cap are applied on the index to limit exposure concentration.

Source: IHS Markit Evaluated Bond Pricing and IHS Markit Indices

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13. Liquidity score data is provided by IHS Markit's Evaluated Bond Pricing which falls under the Pricing and Reference Data service. The score considers a variety of factors, including market depth, bid/ask spread, maturity, and shadow liquidity.

The data shows the percentage of the most liquid bonds (Liquidity score of 1) improved from 82.8% to 89.6% after applying the issuer floor. In terms of market value, the constrained index still captures almost 90% of the parent Asian USD HY index.

Taking an additional step by overlaying ESG strategies further improves the liquidity of the underlying portfolio as 94.6% of the *iBoxx MSCI ESG USD Asia ex-Japan Capped* index constituents have a liquidity score of 1. It is perhaps of no surprise as bonds and issuers who score high on ESG criteria are generally more sought after these days with the focus on sustainable investing.

## Conclusion

We have discussed multiple angles of the Asian USD high yield credit market in this article. Higher yields (and spreads) and shorter durations are clearly attractive points, but recent defaults, especially in the real estate segment, have certainly caused jitters amongst investors. High exposure to Chinese issuers might also be a concern to some.

However, investors who are looking to diversify their high yield credit portfolio, and at the same time potentially achieve higher risk-adjusted return (based on back test result discussed in this article), can consider re-calibrating their asset allocation to include Asian USD HY bonds. Year-to-date, even though the Asian USD HY market has also been one of the hardest hit (-6.5% return), value investors might perceive price levels at this juncture attractive enough to participate in this market.

Looking at the bigger picture, the Chinese bond market is the second largest globally, having overtaken Japan in 2019. Despite recent woes, the Chinese economy is still projected to grow 8.0% this year and 5.6% in 2022 according to latest forecasts by the International Monetary Fund (IMF) in mid-October 2021. Investing in the Asian USD HY credit bond market can yet be a long-term play on emerging Asia and, in particular, China's continued rise in the world economy.

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