

Northbound Swap Connect: Launching Soon

At initial stage, Swap Connect will be open for "Northbound Trading" only, allowing international investors to access the onshore interbank derivatives market. "Northbound Swap Connect" will firstly enable investments in the interbank RMB interest rate swap (IRS) products which will be quoted, traded and settled in RMB. At the same time, "Northbound Swap Connect" implements quota management, and the quota will be adjusted in due course according to market conditions.

"Northbound Swap Connect" will be co-operated by China Foreign Exchange Trade System (CFETS), Shanghai Clearing House (SHCH) and OTC Clear Hong Kong Limited (OTC Clear), the three institutions will connect each other's infrastructures to support the development of the Swap Connect. One of the most important features of the "Northbound Swap Connect" is the interconnectivity among clearing houses, which taps into the solid foundation between financial markets of Chinese Mainland and Hong Kong SAR, meanwhile it adapts the mechanism similar to the "Bond Connect" to bridge financial market infrastructures.

At the same time, "Northbound Swap Connect" marks a new milestone in China's opening-up of its capital markets, facilitating global investors to manage interest rate risks in accordance with their own trading habits and is of great significance to further open China's domestic bond and derivatives markets to the world.

CNY IRS vs CNY NDIRS

CNY NDIRS, also called RMB Non-Deliverable Interest Rate Swap (NDIRS), reflects the expectation and judgment of foreign institutions on the trend of domestic interest rates. Although foreign investors can also use NDIRS to manage interest rate risk, the liquidity of onshore RMB (CNY) IRS and the correlation with benchmark rate trends are relatively better than CNY NDIRS. Moreover, the bid-ask spread of onshore RMB IRS is also tighter than that

of CNY NDIRS, which means that investors may have lower transaction costs and higher hedging efficiency when using onshore RMB IRS.

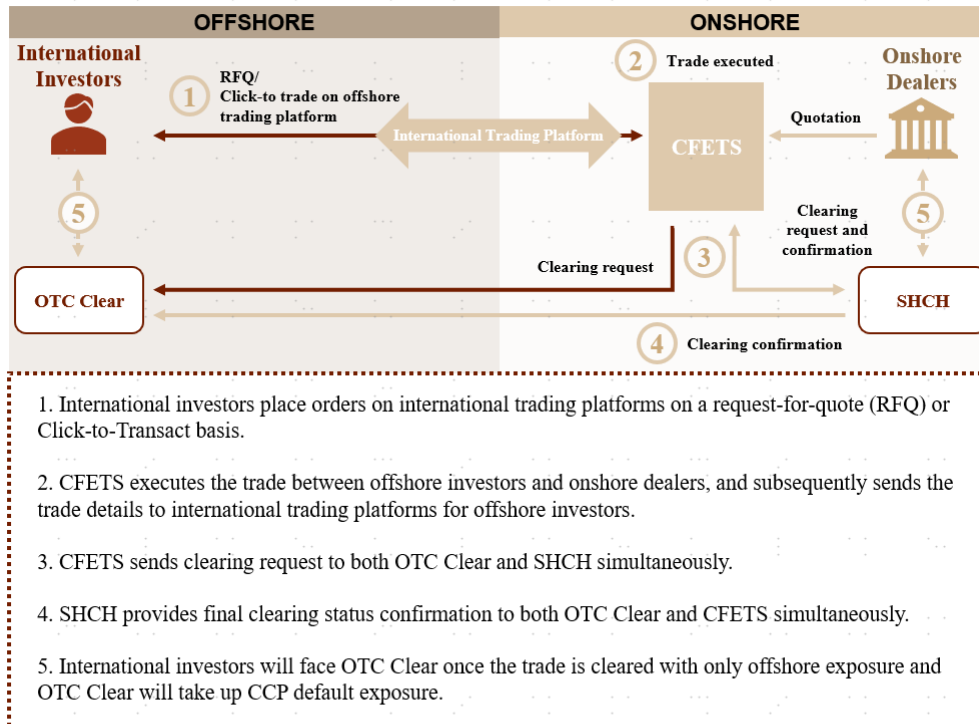
	Settlement currency	Trading volume	Clearing	Participants	Trading platform	Bid-ask spread
CNY IRS	CNY	CNY IRS in the onshore interbank market reached 21.1 trillion yuan in 2021	Shanghai Clearing House + OTC Clear	All qualified domestic and foreign investors	CFETS + offshore electronic trading platforms	The onshore market bid-ask spread of FR007_5Y (one of the most active varieties) usually remains at 0.25bp.
CNY NDIRS	USD	Less liquid compared with CNY IRS	London Clearing House or OTC bilateral clearing	Foreign investors	Offshore electronic trading platforms such as Bloomberg and Tradeweb	Bid-ask spread of FR007_5Y usually remains at 1-1.5bps.

【IRS vs NDIRS】

"Northbound Swap Connect" trading and clearing procedures

CFETS provides service in transaction for investors, then after the transaction is made on the approved trading platform, it will send the transaction to OTC Clear and SHCH in a timely manner for central clearing.

As for clearing, SHCH and OTC Clear will offer central counterparty (CCP) clearing services and jointly realize the central clearing. Specifically, SHCH will provide central clearing services for onshore investors, while OTC Clear will provide central clearing services for offshore investors. Offshore investors can directly use the clearing services provided by OTC Clear to participate in the domestic interbank IRS market.



Source: HKEX, CICC FICC

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