

Introduction: Global and Regional Market Developments

The East Asian economy continued on its path of gradual recovery during the first several months of 2013, supported by a more optimistic investor outlook and improvements in major financial market indicators, including falling bond yields and gains in most stock markets (**Table A**). However, the region's currencies have followed divergent paths since the beginning of the year. For example, the Thai baht appreciated 4.5% against the United States (US) dollar in 1Q13, while the Korean won depreciated 3.3%.

Credit default swap (CDS) spreads in the region remained relatively stable in 1Q13 (**Figure A**), reflecting global investors' increasing confidence

as fears of a eurozone breakup receded and CDS spreads for European countries declined (**Figure B**). Emerging market sovereign bond spreads also declined on the back of growing global investor confidence amid the strong performance of the US stock market in recent weeks (**Figure C**).

Bond yields in advanced countries continued to trend downward in 1Q13, and recently bond yields in the peripheral countries of the eurozone have also been declining (**Figure D**). Meanwhile, Japanese long-term bond yields fell as the Bank of Japan stepped up efforts to meet its 2.0% inflation target with increased bond purchases.

Table A: Changes in Global Financial Conditions

	2-Year Government Bond (bps)	10-Year Government Bond (bps)	5-Year Credit Default Swap Spread (bps)	Equity Index (%)	FX Rate (%)
Major Advanced Economies					
United States	(4)	(9)	0	12.0	–
United Kingdom	(8)	(14)	6	9.0	4.6
Japan	3	(18)	(16)	35.3	(11.0)
Germany	3	(10)	(5)	4.0	0.3
Emerging East Asia					
China, People's Rep. of	(9)	(10)	6	(4.0)	1.2
Hong Kong, China	3	25	(1)	0.4	(0.1)
Indonesia	(13)	32	(1)	16.6	0.6
Korea, Rep. of	(30)	(39)	5	(1.7)	(3.3)
Malaysia	(8)	(13)	7	1.7	0.5
Philippines	(73)	(132)	(12)	21.6	(0.4)
Singapore	(8)	7	0	6.3	(0.9)
Thailand	(13)	(12)	(2)	14.8	4.5
Viet Nam	(74)	(70)	–	14.7	(0.5)
Select European Markets					
Greece	(109)	(162)	0	7.3	0.3
Ireland	(89)	(127)	(29)	13.6	0.3
Italy	(68)	(56)	(60)	3.0	0.3
Portugal	(36)	(128)	(75)	10.5	0.3
Spain	(117)	(121)	(50)	3.1	0.3

– = not available, () = negative, bps = basis points, FX = foreign exchange.

Notes:

1. Data reflect changes between 1 January and 30 April 2013.

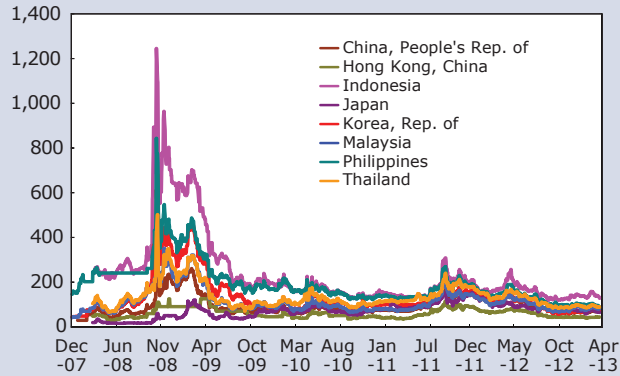
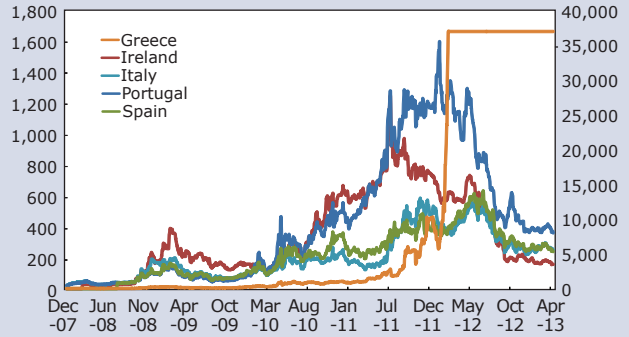
2. For emerging East Asia, a positive (negative) value for the FX rate indicates the appreciation (depreciation) of the local currency against the US dollar.

3. For European markets, a positive (negative) value for the FX rate indicates the depreciation (appreciation) of the local currency against the US dollar.

Source: Bloomberg LP, Institute of International Finance (IIF), and Thomson Reuters.

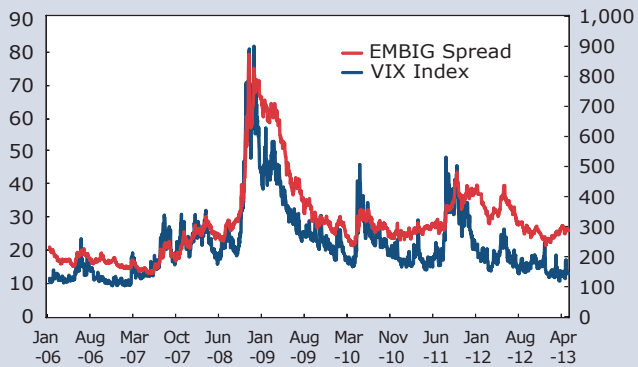
Figure A: Credit Default Swap Spreads^{a, b}
(senior 5-year)

mid-spread in basis points

**Figure B: Credit Default Swap Spreads for Select European Markets^{a, b}** (senior 5-year)Ireland, Italy, Portugal, Spain
mid-spread in basis points**Figure C: US Equity Volatility and Emerging Market Sovereign Bond Spreads^b**

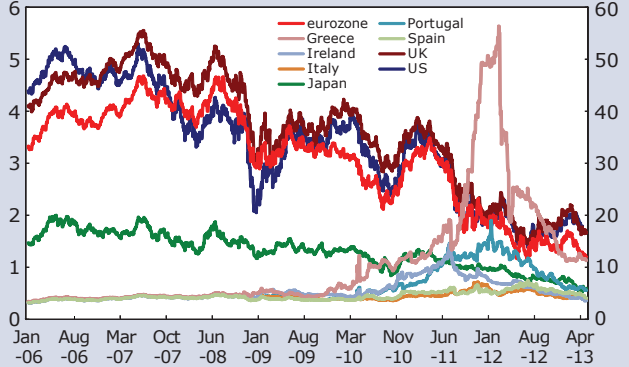
VIX index

EMBIG Spread basis points

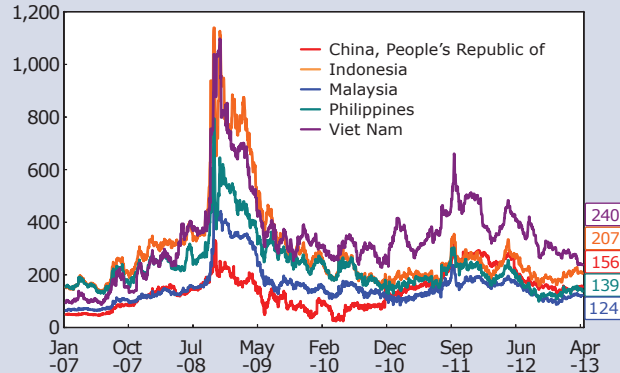
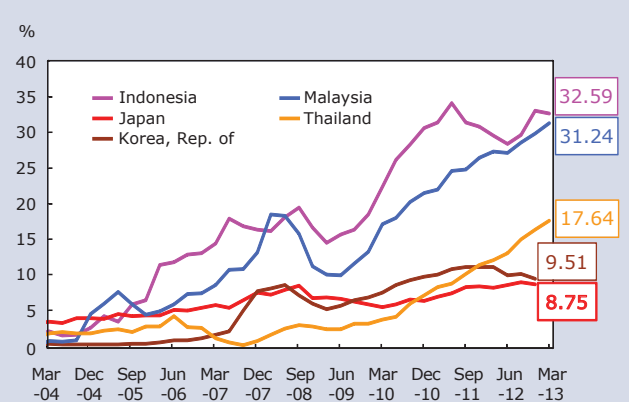
**Figure D: 10-Year Government Bond Yields^b**
(% per annum)

eurozone, Japan, UK, US

Greece, Ireland, Italy, Portugal, Spain

**Figure E: JPMorgan EMBI Sovereign Stripped Spreads^{a, b}**

basis points

**Figure F: Foreign Holdings of LCY Government Bonds in Select Asian Economies^c** (% of total)^c

EMBI = Emerging Markets Bond Index, EMBIG = Emerging Markets Bond Index Global, LCY = local currency, UK = United Kingdom, US = United States, VIX = Chicago Board Options Exchange Volatility Index.

Notes:

^a In US\$ and based on sovereign bonds.^b Data as of end-April 2013.^c Data as of end-March 2013 except for the Republic of Korea and Japan as of end-December 2012.

Source: AsianBondsOnline, Bloomberg LP, and Thomson Reuters.

Interest rates remained low in most advanced countries and held steady in emerging East Asia with a few exceptions.³ For example, sovereign spreads in Viet Nam tightened in 1Q13 and have risen slightly since the beginning of the year in the People's Republic of China (PRC) **(Figure E)**.

Finally, the shares of foreign holdings of the region's local currency (LCY) government bonds continued to rise in 1Q13, except in the Republic of Korea and Japan. The share of foreign holdings of government bonds in Indonesia remained the highest in the region at 32.6% of the total, while foreign holdings of Malaysian bonds reached 31.2% **(Figure F)**.

³ Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; the Republic of Korea; Malaysia; the Philippines; Singapore; Thailand; and Viet Nam.