# Executive Summary

## Recent Developments in Financial Conditions in Emerging East Asia

Between 1 March and 31 May, financial conditions weakened in emerging East Asia on a delay in the expected rate cut by the United States (US) Federal Reserve.[1] A slower-than-expected disinflation path supported the likelihood of higher-for-longer interest rates and pushed up short-term and long-term bond yields in both advanced economies and regional markets. This led to bond outflows from regional markets amounting to USD20 billion in March–April.

The delay in the Federal Reserve's expected rate cut and hawkish tones from its officials contributed to weakening financial conditions in regional markets during the review period. Regional currencies depreciated by 1.8% (simple average) and 1.1% (gross-domestic-product-weighted) against the US dollar. Credit default swap spreads widened in five out of seven markets in which data are available. While most regional equity markets recorded gains during the review period on domestic factors, Association of Southeast Asian Nations (ASEAN) equity markets witnessed USD4.7 billion outflows.

With lingering uncertainty over the path of disinflation, risks to regional financial conditions are tilted to the downside. Uncertainties regarding US monetary policy could support a strong US dollar, leading to additional outflows from emerging East Asia and currency weakness. Regional domestic monetary authorities may face pressure to hold interest rates higher for a longer period to safeguard their respective currencies. Heightened geopolitical risks, trade tensions, and adverse weather events could further add inflationary pressure via rising freight costs, supply chain disruptions, and higher food prices.

## Recent Developments in Local Currency Bond Markets in Emerging East Asia

Emerging East Asia's local currency (LCY) bond market expanded 1.4% quarter-on-quarter (q-o-q) to reach a size of USD24.7 trillion at the end of the first quarter (Q1) of 2024. The region's bond market expansion slowed slightly in Q1 2024 compared to growth of 1.8% q-o-q in the previous quarter. The slower expansion was largely due to deep contractions in government bond issuance in the People's Republic of China (PRC) and Hong Kong, China, which outpaced increased issuance in other emerging East Asian markets. Meanwhile, regional corporate bonds outstanding edged up 1.2% q-o-q in Q1 2024, supported by robust corporate issuance in the PRC and Hong Kong, China that followed the PRC's introduction of easing measures to boost the domestic economy. Outstanding LCY bonds among members of the ASEAN totaled USD2.2 trillion at the end of March, accounting for 8.9% of the emerging East Asian total.

LCY bond issuance in emerging East Asia totaled USD2.2 trillion in Q1 2024, declining 9.0% q-o-q as issuance fell for both government and corporate bonds. Government bond issuance fell 18.1% q-o-q to USD853.8 billion, driven by a contraction in issuance in the PRC from a high base in the previous quarter when the government frontloaded part of its 2024 borrowing quota to boost economic growth. Regional LCY corporate bond issuance contracted 1.9% q-o-q to USD822.1 billion as high interest rates suppressed borrowing in most regional markets. ASEAN markets' LCY bond issuance amounted to USD538.6 billion in Q1 2024, comprising 24.2% of the regional issuance total.

[1] Emerging East Asia is defined to include member states of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China; Hong Kong, China; and the Republic of Korea.

Treasury bonds outstanding and issuances in emerging East Asia remained concentrated in medium- to long-term maturities. By the end of Q1 2024, the size-weighted average tenor of outstanding Treasury bonds was 8.2 years, while that for Treasury bond issuance during the quarter was 7.7 years. Over half (52.6%) of outstanding Treasury bonds at the end of March had maturities longer than 5 years; the corresponding share for Treasury bond issuance during the quarter was 54.7%.

Emerging East Asian LCY Treasury bonds remained largely held by passive investor groups such as banks and insurance and pension funds. At the end of March, banks held the largest average share of LCY Treasury bonds across all regional markets (36.6%), followed by insurance and pension funds (28.9%). Meanwhile, Treasury bond markets in Indonesia and the Republic of Korea had the most diversified investor profiles in emerging East Asia.

## Recent Developments in ASEAN+3 Sustainable Bond Markets

The ASEAN+3 sustainable bond market expanded 21.4% on an annual basis to reach a size of USD805.9 billion at the end of March.[2] Year-on-year growth in the ASEAN+3 sustainable bond market exceeded growth in both the European Union 20 (EU-20) (20.4%) and the overall global market (17.7%). ASEAN+3 continued to account for the world's second-largest regional sustainable bond market at the end of Q1 2024 with a global share of 18.9%, trailing only the EU-20's 37.6%. Despite the expansion, sustainable bonds outstanding comprised only 2.1% of ASEAN+3's total bond market at the end of March, lagging the EU-20's corresponding share of 7.3%.

Sustainable bond issuance in ASEAN+3 contracted 13.3% q-o-q to USD49.7 billion in Q1 2024 on expectations of higher-for-longer interest rates in the US and throughout the region. LCY-denominated bonds accounted for 79.3% of the quarterly issuance total, which was less than the LCY-denominated share of 96.4% for general bond market issuance. Short-term financing (maturities of 5 years or less) accounted for 77.4% of ASEAN+3 sustainable bond issuance in Q1 2024, while the size-weighted average tenor of total quarterly issuance was 5.0 years in ASEAN+3, compared with 9.7 years in the EU-20.

[2] ASEAN+3 is defined to include member states of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China; Hong Kong, China; Japan; and the Republic of Korea.