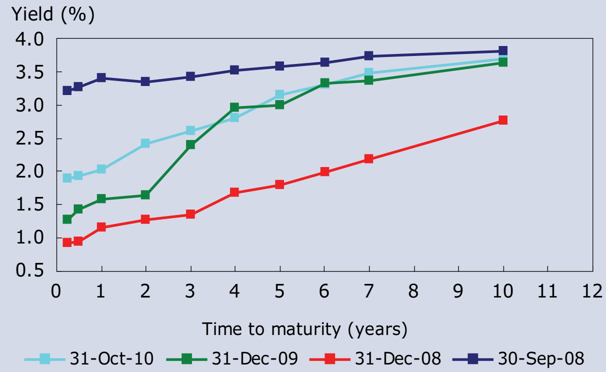
# Market Summaries

## People's Republic of China—Update

### Yield Movements

The government bond yield curve for the People's Republic of China (PRC) flattened between end-December 2009 and end-October 2010. Yields for all tenors rose except for the 4-year tenor, which fell 15 basis points, and the 6-year tenor, which was barely unchanged, fell 1 basis point. Yields rose strongly at the shorter-end of the curve with the 1-year tenor rising 44 basis points and the 2-year tenor rising 77 basis points. Yields for the 7-year tenor rose 12 basis points, while yields for the 10-year tenor rose 6 basis points **(Figure 1)**. On 20 October, the PRC surprised markets by raising policy rates by 25 basis points. The 1-year lending rate was increased to 5.56% from 5.31%, while the 1-year deposit rate rose to 2.50% from 2.25%.

**Figure 1: People's Republic of China's Benchmark Yield Curve—LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

Due to a stronger rise in short-term yields versus yields for longer-term bonds, the spread between 2- and 10-year government bonds decreased to 128 basis points from 199 basis points at end-December.

In 3Q10, the PRC's gross domestic product (GDP) growth rate moderated to 9.6% year-on-year (y-o-y) after having surged to 10.3% in 2Q10.

Recent economic data has fueled concerns over inflation. The PRC's new loans for October amounted to CNY587.7 billion, bringing total new loans for the first 10 months of the year to CNY6.89 trillion. This amount is already 91.9% of the PRC's full-year loan target of CNY7.5 trillion. The PRC's M2 money supply growth accelerated to 19.3% in October versus 19.0% in September. In addition, industrial output grew by 16.1% in the January–October period. Output growth was 11.0% in 2009. Due to high food prices, consumer price inflation hit a 25-month high of 4.4% in October, up sharply from 3.6% in September. Property prices also increased 0.2% month-on-month (m-o-m) in October, slightly down from September's 0.5% m-o-m growth. Property prices declined in June on a monthly basis and remained unchanged in July and August. In response to rising inflation, the People's Bank of China (PBOC) hiked the reserve requirement for all banks twice in the month of November by 50 basis points each time.

Other than rising inflation, the PRC has also expressed concern over potential hot money inflows. On 5 August, the State Administration of Foreign Exchange (SAFE) announced that it would continue to maintain pressure on speculative fund inflows. SAFE reiterated its stance again in a report released on 12 October, saying that it would continue to stop inflows of speculative money and crackdown on illegal foreign exchange activities. SAFE attributed the inflows of hot money to bets on

**Table 1: Size and Composition of the LCY Bond Market in the People's Republic of China**

| | **Amount** (billion) | | | | | | | | **Growth Rates** (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Jun-10** | | **Jul-10** | | **Aug-10** | | **Sep-10** | | **Jun-10** | | **Jul-10** | **Aug-10** | **Sep-10** | | |
| | **CNY** | **USD** | **CNY** | **USD** | **CNY** | **USD** | **CNY** | **USD** | **y-o-y** | **q-o-q** | **m-o-m** | **m-o-m** | **y-o-y** | **q-o-q** | **m-o-m** |
| Total | 19,316 | 2,848 | 19,498 | 2,878 | 19,958 | 2,930 | 20,013 | 2,991 | 22.5 | 6.9 | 0.9 | 2.4 | 21.4 | 3.6 | 0.3 |
| Government | 15,611 | 2,302 | 15,799 | 2,332 | 16,108 | 2,365 | 15,905 | 2,377 | 17.0 | 6.0 | 1.2 | 2.0 | 15.6 | 1.9 | (1.3) |
| Treasury Bonds | 6,069 | 895 | 6,110 | 902 | 6,336 | 930 | 6,398 | 956 | 13.5 | 6.1 | 0.7 | 3.7 | 13.1 | 5.4 | 1.0 |
| Central Bank Bonds | 4,743 | 699 | 4,795 | 708 | 4,776 | 701 | 4,442 | 664 | 14.0 | 8.3 | 1.1 | (0.4) | 10.5 | (6.3) | (7.0) |
| Policy Bank Bonds | 4,800 | 708 | 4,894 | 722 | 4,997 | 734 | 5,064 | 757 | 25.1 | 3.8 | 2.0 | 2.1 | 24.2 | 5.5 | 1.3 |
| Corporate | 3,705 | 546 | 3,700 | 546 | 3,850 | 565 | 4,108 | 614 | 52.7 | 10.4 | (0.1) | 4.1 | 50.5 | 10.9 | 6.7 |
| **Policy Bank Bonds** | | | | | | | | | | | | | | | |
| China Development Bank | 3,462 | 510 | 3,542 | 523 | 3,647 | 535 | 3,662 | 547 | 25.0 | 2.3 | 2.3 | 3.0 | 24.6 | 5.8 | 0.4 |
| Export–Import Bank of China | 481 | 71 | 477 | 70 | 480 | 70 | 509 | 76 | 42.1 | 10.9 | (0.8) | 0.6 | 36.3 | 5.9 | 6.1 |
| Agricultural Dvt. Bank of China | 857 | 126 | 876 | 129 | 870 | 128 | 892 | 133 | 17.3 | 3.3 | 2.1 | (0.6) | 16.5 | 4.1 | 2.5 |

LCY = local currency, m-o-m = month on month, q-o-q = quarter on quarter, y-o-y = year on year.
Notes:
1.Calculated using data from national sources.
2.Treasury bonds include savings bonds and local government bonds.
3.Bloomberg LP end-of-period LCY–USD rate is used.
4.Growth rates are calculated from LCY base and do not include currency effects.
Source: *ChinaBond.*

the yuan's appreciation, which hit an all-time high versus the United States (US) dollar of CNY6.6249 on 11 November.

## Size and Composition

The outstanding amount of local currency (LCY) bonds in the PRC market reached CNY20.01 trillion at the end of September, representing a y-o-y increase of 21.4% and a quarter-on-quarter (q-o-q) rise of 3.6% **(Table 1)**.

Government bonds outstanding increased 15.6% y-o-y and 1.9% q-o-q, while corporate bonds rose 50.5% y-o-y and 10.9% q-o-q. In the government sector, policy bank bonds posted the highest y-o-y increase, expanding 24.2%, followed by treasury bonds and central bank bonds, which posted growth rates of 13.1% and 10.5%, respectively. On a q-o-q basis, however, the growth rate of central bank bonds was actually negative, with central bank bonds declining 6.3%. The quarterly growth rate for policy bank bonds slightly outpaced that of treasury bonds, posting 5.5% growth versus 5.4% for treasury bonds.

## Corporate Bonds

With the exception of asset- and mortgage-backed securities and commercial bank bonds, key sectors of the corporate bond market grew by double digits in 3Q10. Medium-term notes (MTNs) grew by 73.8% y-o-y, while commercial paper and local corporate bonds posted y-o-y growth rates of 89.9% and 52.5%, respectively. State-owned corporate bonds (or SOE bonds) grew 36.1% y-o-y, and commercial bank bonds grew 3.4%. In contrast to other sectors, the amount of asset- and mortgage-backed securities has been on a steady decline, with no new issuance since 4Q08.

On a q-o-q basis, all sectors showed slower growth rates in 3Q10 compared with the prior quarter, with the exception of SOE bonds **(Table 2)**. SOE bonds grew 7.9% in 3Q10 from 1.3% in 2Q10, and MTNs increased 12.0% compared with 17.9% in 2Q10. Commercial paper showed the greatest change,

**Table 2: Corporate Bonds Outstanding in Key Sectors**

| | Amount (CNY billion) | | | | | | Growth Rates (%) | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | q-o-q | | | | | y-o-y |
| | 2Q09 | 3Q09 | 4Q09 | 1Q10 | 2Q10 | 3Q10 | 3Q09 | 4Q09 | 1Q10 | 2Q10 | 3Q10 | 3Q10 |
| Commercial Bank Bonds | 486.4 | 589.2 | 588.4 | 589.6 | 608.5 | 609.0 | 21.1 | (0.1) | 0.2 | 3.2 | 0.1 | 3.4 |
| State-Owned Corporate Bonds | 565.3 | 619.3 | 720.2 | 771.1 | 781.1 | 842.6 | 9.6 | 16.3 | 7.1 | 1.3 | 7.9 | 36.1 |
| Local Corporate Bonds | 295.7 | 328.8 | 376.9 | 420.0 | 461.7 | 501.3 | 11.2 | 14.6 | 11.4 | 9.9 | 8.6 | 52.5 |
| Commercial Papers | 384.3 | 353.1 | 456.1 | 508.8 | 615.4 | 670.6 | (8.1) | 29.2 | 11.5 | 21.0 | 9.0 | 89.9 |
| Asset/Mortgage-Backed Securities | 55.4 | 46.0 | 39.9 | 31.1 | 26.5 | 21.9 | (16.9) | (13.4) | (22.1) | (14.8) | (17.2) | (52.4) |
| Medium-Term Notes | 592.1 | 742.1 | 862.2 | 976.4 | 1,151.2 | 1,289.5 | 25.3 | 16.2 | 13.2 | 17.9 | 12.0 | 73.8 |

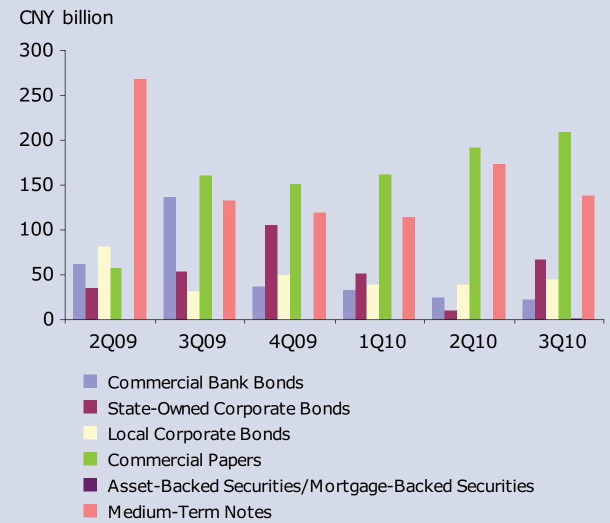
q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Source: *ChinaBond.*

growing 9.0% in 3Q10 compared with 21.0% in 2Q10, while commercial bank bonds grew at an anemic rate of 0.1% in 3Q10 from 3.2% in 2Q10.

MTNs have consistently enjoyed double-digit q-o-q growth rates for the past 6 quarters, reflecting continued strong corporate sector demand and the improved access to MTNs facilitated by relatively quick issuance approval processes.

Consistent with the lower growth rate for MTNs outstanding in 3Q10 versus 2Q10, MTN issuance declined from CNY174.1 billion in 2Q10 to CNY138.3 in 3Q10, for a q-o-q decrease of 20.6%. Issuance of MTNs has been on a downward trend since peaking at CNY268.6 billion in 2Q09 **(Figure 2)**.Commercial paper issuance reached an all-time high of CNY209.0 billion in 3Q10.

**Figure 2: Corporate Bond Issuance in Key Sectors**




Source: *ChinaBond.*

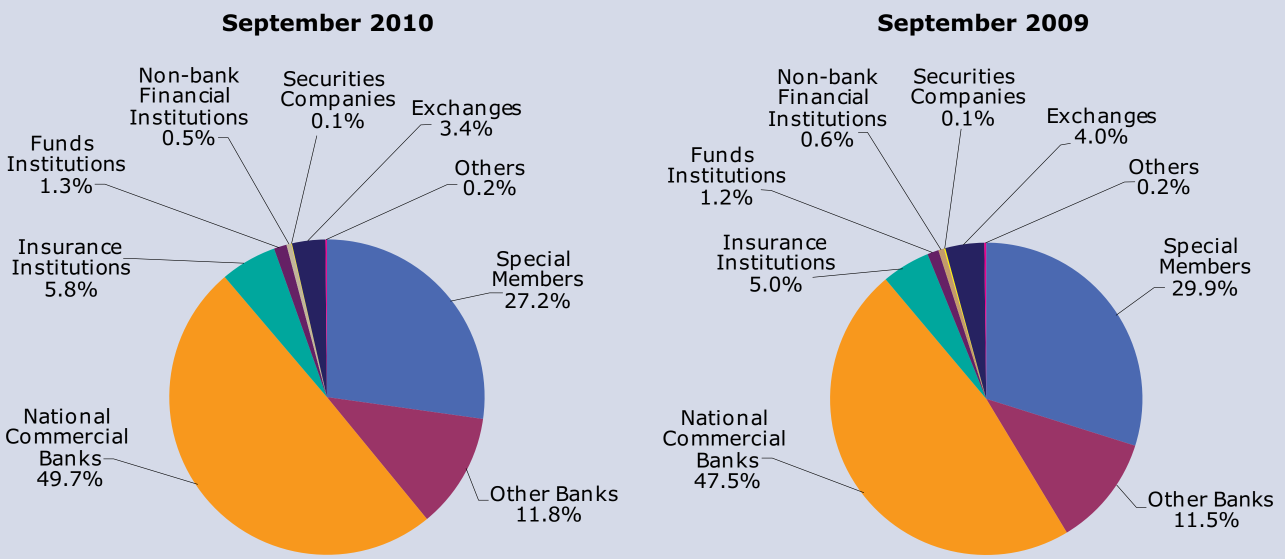
## Investor Profile

Banks remained the largest category of treasury bond investors in the PRC market, holding a larger share of these bonds at end-September 2010 (61.5%) than end-September 2009 (59.0%) **(Figure 3)**. The share held by special members dropped to 27.2% in September 2010 from 29.9% a year earlier. Special members comprise the PBOC, Ministry of Finance, policy banks, China Government Securities Depository Trust and Clearing Co., and China Securities Depository and Clearing Corporation.

## Rating Changes

On 11 November, ratings agency Moody's Investors Service upgraded its ratings on PRC government bonds to Aa3 from A1 and said it would maintain its positive outlook on the country's debt **(Table 3)**. It cited what it described as the "resilient performance" of the PRC economy since the onset of the financial crisis, as well as exceptional growth in the nation's external payment position as reasons for the upgrade. The ratings agency said it had based its view on expectations that trade and currency issues between the PRC and the US could be "constructively managed," and that it saw little risk of fallout from the PRC's efforts to prop up its

**Figure 3: LCY Government Bonds Investor Profile**




Source: *ChinaBond*.

**Table 3: Selected Sovereign Ratings and Outlook for the People's Republic of China**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | Aa3 | A+ | A+ |
| Outlook | Positive | Stable | Stable |

FCY = foreign currency, LT = long-term.
Source: Rating agencies

economy through "extraordinary credit expansion" in 2009.

# Policy, Institutional, and Regulatory Developments Ratings Upgrade

## PBOC Allows Banks to Sell Loans to Each Other

On 25 September, the PBOC launched its interbank loan transfer system to allow banks to sell loans to each other. The loan transfers will allow lenders to keep a handle on risks and promote the liberalization of interest rates, according to central bank governor Zhou Xiaochun. At the time of the launch, 21 banks had signed up for the system.

## Clearstream and Euroclear Enable Settlement of CNY-Denominated Securities

On 27 September, Clearstream and Euroclear allowed the settlement and clearance of CNY-denominated securities issued outside of the PRC, including Eurobonds and securities issued in Hong Kong, China. Prior to this move, foreign investors could only settle in Hong Kong dollars for securities listed on the Shenzhen Stock Exchange and US dollars for securities listed on the Shanghai Stock Exchange.

## Banks Barred from Providing Mortgages to Third Home Buyers

On 30 September, the State Council of China ordered banks to stop providing mortgages to buyers seeking to purchase a third (or more) home. Also, first-time home buyers must now make a down payment of 30% of the house's price compared with the previous requirement of 20%.

## PRC Revises Rules on CNY-Denominated Bonds Issued by Foreign Institutions

The PRC issued revisions to CNY-denominated bonds issued by foreign institutions in the PRC. The revised rules allow international organizations, such as the World Bank and Asian Development Bank, to convert the yuan proceeds in a different currency and transfer the funds overseas with the approval of SAFE, conditional upon the bond having a rating of AA from at least two rating agencies, one of which should be registered in the PRC to rate CNY-denominated bonds.

## PRC Allows Foreign Institutions to Open Yuan Accounts

The PBOC issued regulations on 6 October that allow foreign institutions to open cross-border settlement accounts at locally registered banks. According to the rules, foreign institutions can either open an account with a domestic bank or the local unit of a foreign bank. There are, however, restrictions imposed on the accounts. Institutions cannot convert the yuan in the accounts to a different currency or withdraw it as cash. The PBOC said that these rules do not apply to CNY-settled accounts opened by foreign central banks, interbank settlement accounts set up by foreign banks, special yuan accounts opened by qualified foreign institutional investors for trading securities in the PRC, or special accounts for investing in the PRC's interbank bond market.

## Chinese Insurers Barred from Property Speculation

The China Insurance Regulatory Commission issued regulations barring Chinese insurance companies from speculating in the property sector. According to the rules, insurers are allowed to invest up to 10% of their assets in elderly citizen communities and the medical services sector, but are not allowed to invest in commercial or residential properties, nor are they allowed to set up real estate enterprises.

## Banks Return to Exchanges

On 27 October, the China Securities Regulatory Commission allowed banks to trade bonds listed on domestic exchanges, ending a 13-year ban. Prior to this, banks were only allowed to trade on the interbank bond market. The new ruling is expected to improve liquidity on the exchange as the current participants are mostly retail investors and 95% of the PRC's bonds are traded on the interbank market.

## PRC Launches Credit Default Swaps

On 29 October, the PRC recently unveiled guidelines for the creation of its own version of Credit Default Swaps on a trial basis. Under the rules, companies who wish to trade the instrument must have a net capital of at least CNY800 million and companies who wish to originate the instrument must a have a net capital of at least CNY4 billion. By 5 November, nine financial institutions had participated: Minsheng Bank, Deutsche Bank, Bank of Communications, Everbright, Industrial and Commercial Bank, Industrial Bank, China Development Bank, China Construction Bank and China Bond Insurance. Twenty contracts were traded with a notional value of CNY1.84 billion. The swaps will be settled through the Shanghai interbank clearing system, the first time that credit default swaps will be settled through a central clearing party.

## PRC Tightens Controls over Overseas Fund Inflows

On 9 November, the SAFE announced on its website that it will introduce additional rules on currency provisioning and tighten management of banks' foreign debt-quotas. The regulator said that it will also regulate Chinese special purpose vehicles overseas and tighten controls on equity investments by foreign companies in the PRC.

## PRC Limits Hot Money Flows into Real Estate Market

On 12 November, the SAFE and the Ministry of Housing and Urban-Rural Development issued a joint notice that foreign individuals will now be only allowed to purchase one residential property. Also, overseas institutions will only be allowed to purchase non-residential property in the city where it is registered.

## PBOC Hikes Reserve Requirement Ratios

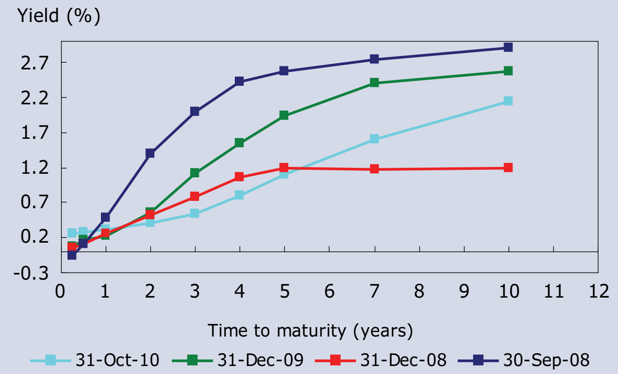
The PRC hiked its reserve requirement ratio by 50 basis points for all banks and another 50 basis points for a select few bank in response to accelerating inflation. The PBOC initially hiked by 50 basis points the reserve requirements of the four big state banks and one other bank—China Construction Bank, Bank of China, Agricultural Bank of China, and Bank of Communications on 10 November—effective 15 November. The PRC subsequently announced a 50-basis-point hike for all lenders, effective 16 November. On 19 November, the PRC again hiked the reserve requirement ratio by 50 basis points. This effectively brings the reserve requirement rate of the four big state banks to 18.5%, and to 18.0% for other large financial institutions, and 16.0% for small and medium-sized financial institutions.

# Hong Kong, China—Update

## Yield Movements

The yield curve for Hong Kong, China's Exchange Fund Bills and Notes (EFBN) between end-December 2009 and end-October 2010 rose 9–18 basis points at the short-end, but tightened by as much as 84 basis points along the rest of the curve **(Figure 1)**. The yield on the 2-year tenor fell 15 basis points, while yields on 4-, 5-, and 7- year tenors fell 75, 84, and 81 basis points, respectively. The spread between 2-year and 10-year maturities fell from 203 basis points as of end-December to 174 basis points as of end- October.

**Figure 1: Hong Kong, China's Benchmark Yield Curve—EFBNs**




EFBN = Exchange Fund Bills and Notes.
Source: Bloomberg LP.

The continued tightening along most of the EFBN yield curve reflected the large inflows of foreign capital into Hong Kong, China's financial markets. Also, these inflows into HKD-denominated instruments was paralleled by inflows into the rapidly growing yuan market in Hong Kong, China.

Consumer price inflation in Hong Kong, China eased to 2.6% year-on-year (y-o-y) in September from 3.0% in August. The drop in inflation was due to a lower base effect in August caused by the government's one-off electricity charge subsidy in August 2009. For January through September, consumer price inflation stood at 2.3% y-o-y.

Domestic demand has proven resilient, with retail sales in September rising 17.2% y-o-y—the 13th consecutive month that retail sales have expanded. Manufacturing activity in the Special Administrative Region has remained robust, with the HSBC Purchasing Managers' Index (PMI) for October standing at 53.0, compared with 52.8 in September. (A PMI reading above 50 is indicative of an expansion of manufacturing activity.) Hong Kong, China's economy grew 6.8% y-o-y in 3Q10, slightly higher than 6.5% y-o-y growth in 2Q10. Private consumption expenditure expanded 5.7% y-o-y on account of the improving employment situation as well as rising incomes.

Merchandise exports remained strong, rising 20.8% y-o-y due to strong domestic demand and further expansion in intra-regional production activity in Asian markets. On a quarter-on-quarter (q-o-q) basis, the economy expanded 0.7%.

## Size and Composition

As of end-September, Hong Kong, China's local currency (LCY) bonds outstanding reached HKD1.25 trillion, representing a y-o-y growth rate of 25.8% **(Table 1)**. On a q-o-q basis, LCY bonds outstanding rose 1.3% in 3Q10.

Total government bonds outstanding—comprising exchange fund bills (EFBs), exchange fund notes (EFNs), and Hong Kong Special Administrative Region (HKSAR) bonds—grew 61.2% y-o-y. As was the case in the previous quarter, the growth in total government bonds outstanding was largely attributable to the growth of EFBs, which expanded 69.4% y-o-y. As of end-September, the stock of EFNs remained flat at its June 2010 level of HKD70.0 billion, while HKSAR bonds outstanding rose to HKD19.5 billion, compared with HKD16.0 billion at the end of June. On a

**Table 1: Size and Composition of the LCY Bond Market in Hong Kong, China**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | HKD | USD | HKD | USD | HKD | USD | HKD | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 1,237 | 159 | 1,241 | 160 | 1,245 | 160 | 1,253 | 161 | 43.3 | 2.7 | 0.3 | 0.3 | 25.8 | 1.3 | 0.6 |
| Government | 667 | 86 | 668 | 86 | 668 | 86 | 672 | 87 | 131.4 | 6.9 | 0.0 | 0.0 | 61.2 | 0.6 | 0.6 |
| Exchange Fund Bills | 581 | 75 | 581 | 75 | 582 | 75 | 582 | 75 | 164.4 | 7.1 | 0.0 | 0.0 | 69.4 | 0.1 | 0.1 |
| Exchange Fund Notes | 70 | 9 | 70 | 9 | 70 | 9 | 70 | 9 | 2.3 | 0.1 | 0.0 | 0.0 | 0.9 | 0.0 | 0.0 |
| HKSAR Bonds | 16 | 2 | 16 | 2 | 16 | 2 | 20 | 3 | — | 39.1 | 0.0 | 0.0 | 457.1 | 21.9 | 21.9 |
| Corporate | 569 | 73 | 573 | 74 | 577 | 74 | 581 | 75 | (0.9) | (1.9) | 0.7 | 0.7 | 0.3 | 2.1 | 0.7 |

— = not applicable, HKSAR = Hong Kong Special Administrative Region, LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY—USD rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. The amount of corporate bonds outstanding for July to August were estimated based on the compounded monthly growth rate between June and September
Source: Hong Kong Monetary Authority and Bloomberg LP.

y-o-y basis, HKSAR bonds expanded 457.1%, owing to the low base of comparison in 2009 when HKSAR bonds outstanding amounted to only HKD3.5 billion.

Corporate bonds outstanding in Hong Kong, China in 3Q10 rose 0.3% y-o-y to HKD581.0 billion, while on a q-o-q basis, the outstanding amount of corporate bonds rose 2.1%. The top 20 non-bank corporate issuers in Hong Kong, China accounted for about 15% of total corporate bonds outstanding in 3Q10 **(Table 2)**. The Hong Kong Mortgage Corporation (HKMC) remained Hong Kong, China's largest single corporate issuer of local currency bonds with HKD27.6 billion of bonds outstanding as of end-September.

**Table 2: Top 20 Non-Bank Corporate Issuers**

| Top 20 Non-Bank Corporate Issuers | Outstanding Amount | |
|---|---|---|
| | LCY Bonds (HKD billion) | LCY Bonds (USD billion) |
| The Hong Kong Mortgage Corporate Ltd | 27.63 | 3.56 |
| Sun Hung Kai Properties (Capital Market) Ltd | 9.39 | 1.21 |
| CLP Power Hong Kong Financing Ltd | 8.78 | 1.13 |
| Kowloon-Canton Railway Corp | 6.60 | 0.85 |
| MTR Corporation (C.I.) Ltd | 5.20 | 0.67 |
| Swire Pacific MTN Financing Ltd | 4.10 | 0.53 |
| Hongkong Electric Finance Ltd | 3.80 | 0.49 |
| Cheung Kong Bond Finance Ltd | 2.95 | 0.38 |
| Airport Authority Hong Kong | 2.90 | 0.37 |
| HKCG (Finance) Ltd | 2.76 | 0.36 |
| Bauhinia MBS Ltd | 2.73 | 0.35 |
| The Link Finance (Cayman) 2009 Ltd | 2.23 | 0.29 |
| Hysan (MTN) Ltd | 1.77 | 0.23 |
| Urban Renewal Authority | 1.50 | 0.19 |
| Wharf Finance (No. 1) Ltd | 1.07 | 0.14 |
| Wharf Finance Ltd | 1.03 | 0.13 |
| Cheung Kong Finance (MTN) Ltd | 1.00 | 0.13 |
| Hong Kong Link 2004 Ltd | 0.80 | 0.10 |
| Wharf Finance (BVI) | 0.48 | 0.06 |
| Swire Pacific Finance Int'l Ltd | 0.20 | 0.03 |
| **Total** | 86.92 | 11.20 |

LCY = local currency.
Note: Based on Central Money Markets Unit (CMU) data on tradable non-bank debt securities issued and still outstanding as of 19 October 2010.
Source: Hong Kong Monetary Authority.

## Rating Changes

In November, Moody's Investors Service upgraded Hong Kong, China's government bond rating to Aa1 from Aa2 **(Table 3)**. Moody's also raised Hong Kong, China's foreign currency bank deposit ceiling to Aa1 and the foreign currency bond ceiling to Aaa. Moody's assigned a positive outlook to the ratings. Moody's cited the following factors as contributing to Hong Kong, China's rating upgrade: (i) prospects for continued and improving government financial strength; (ii) lessening vulnerability to external shocks; (iii) favorable prospects for the economic performance of the People's Republic of China in the coming years, which will provide support to economic growth and financial developments in Hong Kong, China.

**Table 3: Selected Sovereign Ratings and Outlook for Hong Kong, China**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | Aa1 | AA+ | AA |
| Outlook | positive | stable | stable |

FCY = foreign currency, LT = long term.
Source: Ratings agencies.

## Policy, Institutional, and Regulatory Developments

### ADB Raises CNY1.2 Billion in First Supranational Issue in Hong Kong, China

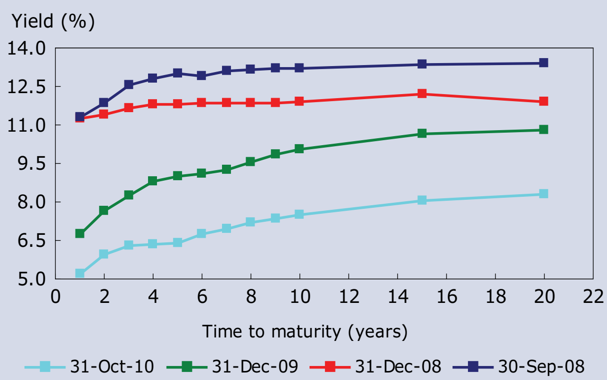
In October, the Asian Development Bank (ADB) raised CNY1.2 billion of 10-year bonds in Hong Kong, China. The bonds were sold at par and with a coupon rate of 2.85%. The offering was the first issued in Hong Kong, China by a highly-rated supranational. The bonds are expected to provide a benchmark for longer-term debt since most yuan bonds sold in Hong Kong, China have tenors of 5 years or less. Proceeds from the issuance will be used to finance ADB projects in the People's Republic of China.

# Indonesia—Update

## Yield Movements

The government bond yield curve for Indonesia shifted downward as yields fell for all maturities between end-December 2009 and end-October 2010 **(Figure 1)**. The yield curve flattened from the short-end through the long-end of the curve, as yields fell between 155 and 263 basis points. The 15-year tenor fell the most, shedding 263 basis points by end-October. The yield spread between 2-year and 10-year maturities narrowed to 156 basis points in mid-October from 241 basis points at end-December.

**Figure 1: Indonesia's Benchmark Yield Curve—LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

Yields for the shortest-dated tenor (1-year treasury bills) have remained below the Bank Indonesia (BI) rate since early July. The central bank's regulation requiring a 1-month holding period for Sertifikat Bank Indonesia (SBI), which took effect in July, led some investors to switch from SBIs to treasury bills. The subsequent increase in demand for treasury bills has resulted in a lower yield rate. A+ end-October, 1-year bills fetched a yield of only 5.219%, which was down more than 1 percentage point from end-December 2009.

On 4 November, BI's Board of Governors decided to keep its benchmark interest rate at a record-low level of 6.5%. The BI rate has been kept at this level since August 2009. According to BI, this rate was consistent with the achievement of its 2010 inflation target and remained conducive to safeguarding financial stability and promoting bank intermediation for supply-side response to accelerated demand. The central bank has repeatedly announced that it will refrain from raising interest rates as long as inflation falls within its target range. The stability of BI's monetary policy has contributed to the growth of foreign investor interest in Indonesia's local currency (LCY) bond market.

In October, consumer price inflation eased to 5.7% year-on-year (y-o-y), following 5.8% y-o-y inflation in September and 6.4% y-o-y in August. For the first 10 months of the year, inflation averaged 5.4%, which fell within the central bank's inflation target of 4.0%–6.0% for 2010.

The economy grew 5.8% y-o-y in 3Q10, down slightly from 6.2% growth in 2Q10. Household consumption expanded 5.2% y-o-y, while exports and investments grew 11.3% and 8.9%, respectively. On a quarter-on-quarter (q-o-q) basis, the economy expanded 3.5%. BI estimates that gross domestic product (GDP) growth will range between 6.0% and 6.3% for the full year.

## Size and Composition

The size of Indonesia's LCY bond market climbed 14.9% y-o-y and the total volume of LCY bonds outstanding reaching IDR995.8 trillion (USD112 billion) as of end-September **(Table 1)**. On a q-o-q basis, however, growth in LCY bonds outstanding was marginal in 3Q10 at 1.1%.

Total government bonds outstanding rose 13.3% y-o-y to reach IDR892.7 trillion (USD100 billion) at end-September, as both central government bonds (treasury bills and

**Table 1: Size and Composition of the LCY Bond Market in Indonesia**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | IDR | USD | IDR | USD | IDR | USD | IDR | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 985,359 | 109 | 965,406 | 108 | 1,016,788 | 112 | 995,822 | 112 | 13.8 | (0.03) | (2.0) | 5.3 | 14.9 | 1.1 | (2.1) |
| Government | 892,328 | 99 | 861,700 | 96 | 913,357 | 101 | 892,687 | 100 | 13.5 | (0.1) | (3.4) | 6.0 | 13.3 | 0.04 | (2.3) |
| Central Govt Bonds | 621,226 | 69 | 626,976 | 70 | 645,358 | 71 | 645,077 | 72 | 12.3 | 4.7 | 0.9 | 2.9 | 13.7 | 3.8 | (0.04) |
| Central Bank Bills | 271,103 | 30 | 234,724 | 26 | 267,999 | 30 | 247,610 | 28 | 16.5 | (9.7) | (13.4) | 14.2 | 12.2 | (8.7) | (7.6) |
| Corporate | 93,030 | 10 | 103,706 | 12 | 103,431 | 11 | 103,135 | 12 | 16.5 | 0.9 | 11.5 | (0.3) | 30.7 | 10.9 | (0.3) |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.

Notes:

1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY—USD rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.

Source: Bank Indonesia, Indonesia Stock Exchange, and Bloomberg LP.

bonds issued by the Ministry of Finance) and central bank bills (bills issued by BI in the form of SBIs) posted double-digit growth. The stock of central government bonds climbed 13.7% y-o-y, which was up slightly from 12.3% y-o-y growth in 2Q10. On a q-o-q basis, however, growth in central government bonds rose 3.8% in 3Q10.

In 3Q10, central government issuance consisted of both conventional and Islamic treasury bills and bonds. Total central government issuance for 3Q10 reached IDR32.1 trillion (USD3.6 billion), up 22.2% y-o-y. On a q-o-q basis, however, central government issuance fell 24.8%.

In August, the government issued its seventh series of retail bonds, raising IDR8.0 trillion from the sale. The government initially planned a IDR5.0 trillion offering, but raised its target to IDR8.0 trillion due to strong demand from investors. The retail bonds carried a maturity of 3 years with a coupon of 7.95%. Retail bonds constitute 7.18% of total central government bonds.

Through end-September, the government had issued about IDR145.3 trillion worth of bonds (gross) in 2010. The Ministry of Finance announced in July that it would reduce its issuance of debt securities as the budget deficit was estimated to be equivalent to only 1.5% of GDP, compared with an original estimate of 2.5% of GDP in the revised state budget.

Finally, the Ministry of Finance acknowledged the failure of its *sukuk* (Islamic bond) treasury auctions this year, and is now planning to negotiate rates with potential investors through a book building process instead of conducting auctions. Indonesian investors are demanding higher returns from *sukuk* because they are not actively traded.

**SBI Market Developments.** Growth in central bank bills eased to 12.2% y-o-y in 3Q10, compared with 16.5% in 2Q10. The growth rate in central bank bills, while remaining positive on a y-o-y basis, has exhibited a declining trend in recent months as new regulations governing SBIs took effect in 3Q10. On a q-o-q basis, the outstanding amount of central bank bills contracted 8.7% in 3Q10, following a decline of 9.7% q-o-q in 2Q10.

In 3Q10, three SBI auctions were held at a rate of one per month. Also, SBI issuance for the quarter comprised longer-dated tenors consisting of 3-, 6-, and 9-month tenors. BI issued its first 9-month SBI tenor in August of this year. The central bank was scheduled to issue a 12-month SBI tenor in September, but decided to delay its issuance to give investors time to switch to longer-dated tenors of SBI as well as to avoid hurting demand for 1-year treasury bills.

In November, BI cancelled the sale of its 3-month SBI in its monthly auction. The central bank chose to issue 6- and 9-month, tenors and 1- and 2-year term deposits.

**Corporate Bond Market Trends.** Corporate bonds outstanding rose to IDR103.1 trillion (USD12 billion) in 3Q10, expanding a notable 30.7% y-o-y. On a q-o-q basis, corporate bonds outstanding grew 10.9% in 3Q10, driven by a 57.4% increase in corporate bond issuance.

The top 30 corporate issuers in Indonesia accounted for nearly 80% of total corporate bonds outstanding at end-September **(Table 2)**. State-power firm PLN remained Indonesia's top corporate issuer of LCY bonds, with a total outstanding amount of IDR15.1 trillion. Taking the second spot was telecommunications firm Indosat, with IDR8.1 trillion in outstanding LCY bonds. Bank Tabungan Negara and toll operator Jasa Marga each had outstanding LCY bonds of IDR4.2 trillion. The top 30 LCY bond issuers hailed mainly from the financial sector (63%).

In 3Q10, corporate bond issuance rose to IDR11.5 trillion (USD1.3 billion) from only IDR7.3 trillion (USD0.8 billion) in 2Q10 **(Table 3)**. Corporate bond issuers in 3Q10 mainly comprised firms in the financial sector. Most of the bonds issued during the quarter carried coupons ranging from 9.0% to 10.0%. Some notable issues during 3Q10 are listed in Table 3.

**Table 2: Top 30 Corporate Issuers, September 2010**

| Top 30 Corporate Issuers | Outstanding Amount | |
|---|---|---|
| | LCY Bonds (IDR billion) | LCY Bonds (USD billion) |
| PLN | 15,100 | 1.69 |
| Indosat | 8,090 | 0.91 |
| Bank Tabungan Negara | 4,150 | 0.47 |
| Jasa Marga | 4,150 | 0.47 |
| Bank Panin | 3,900 | 0.44 |
| Indofood Sukses Makmur | 3,610 | 0.41 |
| Bank Mandiri | 3,500 | 0.39 |
| Indonesia Eximbank | 3,000 | 0.34 |
| Perum Pegadaian | 3,000 | 0.34 |
| Telkom | 3,000 | 0.34 |
| Federal International Finance | 2,845 | 0.32 |
| Astra Sedaya Finance | 2,660 | 0.30 |
| Oto Multiartha | 2,500 | 0.28 |
| Bank Ekspor Indonesia | 2,341 | 0.26 |
| Bank Tabungan Pensiunan Nasional | 2,050 | 0.23 |
| Bank Rakyat Indonesia | 2,000 | 0.22 |
| Excelcom | 1,500 | 0.17 |
| Medco Energi Internasional | 1,500 | 0.17 |
| Bank CIMB Niaga | 1,380 | 0.15 |
| Bentoel | 1,350 | 0.15 |
| Berlian Laju Tanker | 1,340 | 0.15 |
| Bank Danamon | 1,250 | 0.14 |
| Danareksa | 1,080 | 0.12 |
| Bank Negara Indonesia | 1,000 | 0.11 |
| Bank Jabar | 1,000 | 0.11 |
| Bank Mega | 1,000 | 0.11 |
| Sarana Multigriya Finansial | 978 | 0.11 |
| Bank OCBC NISP | 880 | 0.10 |
| Pupuk Kaltim | 791 | 0.09 |
| WOM Finance | 775 | 0.09 |
| **Total Top 30 Corporate Issuers** | **81,720** | **9.17** |
| **Total Corporate Bonds Outstanding** | **103,135** | **11.57** |
| **Top 30 as % of Total Corporate** | **79.24%** | **79.24%** |

LCY = local currency.
Source: Indonesia Stock Exchange.

**Table 3: Notable Corporate Issuance in 3Q10**

| Corporate Issuers | Amount Issued (IDR billion) |
|---|---|
| Indonesia Eximbank | 3,000 |
| PLN | 3,000 |
| Telkom | 3,000 |
| Bank CIMB Niaga | 1,380 |
| Sarana Multigriya Finansial | 727 |
| Others | 390 |
| **Total** | **11,497** |

Source: Indonesia Stock Exchange.

Indonesia Eximbank (formerly Bank Ekspor Indonesia) raised IDR3.0 trillion, compared with a target of IDR2.5 trillion, in a four-tranche bond deal in July. The bond issue comprised the following tranches:

- 1-year bonds worth IDR1.250 trillion with a coupon of 7.55%,
- 3-year bonds worth IDR425 billion with a coupon of 8.85%,
- 5-year bonds worth IDR250 billion with a coupon of 9.6%, and
- 7-year bonds worth IDR1.075 trillion with a coupon of 10.0%.

Eximbank also plans to issue either a *samurai* bond or a global G3-bond next year.

The state power firm, PLN, issued bonds worth IDR3.0 trillion in July after raising IDR3.0 trillion earlier in 2010. The bond issue comprised the following tranches:

- 5-year bonds worth IDR645 billion with a coupon of 9.7%,
- 5-year *sukuk* worth IDR160 billion with a coupon of 9.7%,
- 12-year bonds worth IDR1.855 trillion with a coupon of 10.4%, and
- 12-year *sukuk* worth IDR340 billion with a coupon of 10.4%.

Telecommunications provider PT Telekomunikasi issued IDR3.0 trillion worth of bonds in July. The bond issue comprised the following tranches:

- 5-year bonds worth IDR1.005 trillion with a coupon of 9.6%, and
- 10-year bonds worth IDR1.995 trillion with a coupon of 10.2%.

The state-owned mortgage financing company, Sarana Multigriya Finansial, issued IDR727 billion worth of bonds in a two-tranche deal:

- 2-year bonds worth IDR500 billion with a coupon of 9.25%, and
- 3-year bonds worth IDR227 billion with a coupon of 9.75%.

## Foreign Currency Bonds

In early November, the Indonesian government raised JPY60.0 billion in 10-year *samurai* bonds. The bonds were issued at a coupon rate of 1.6%, or 55 basis points above the yen swap rate. This was Indonesia's second issue of *samurai* bonds since selling JPY35.0 billion in 10-year *samurai* bonds in July 2009.

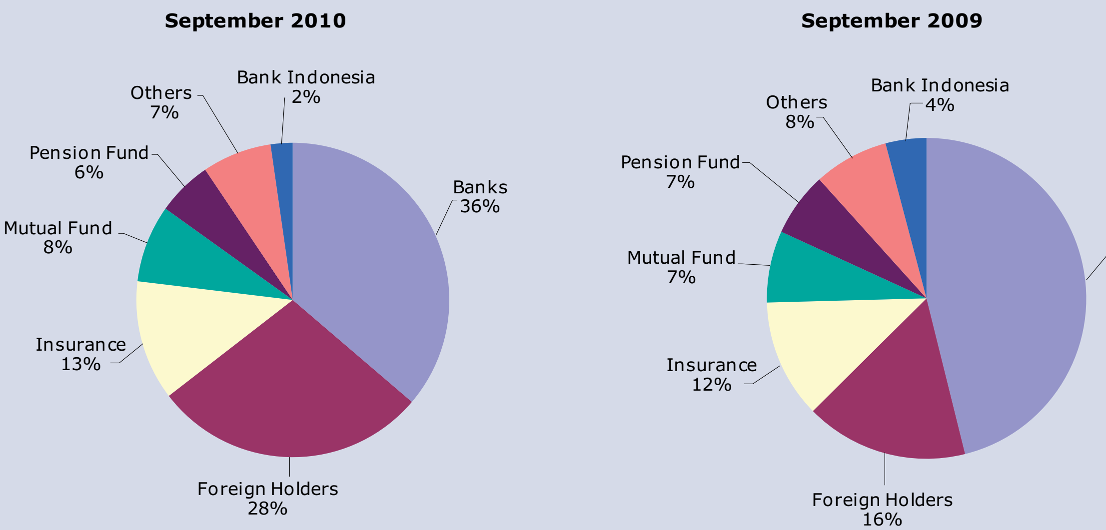
## Investor Profile

Banking institutions remained the biggest holder of Indonesian LCY central government bonds as of end-September **(Figure 2)**. However, banks' share of total LCY central government bonds, which were valued at IDR234.0 trillion at end-September, dropped to 36% from 46% a year ago. Banks' share of total central government bonds outstanding has declined significantly since 2002, when it was as high as 82%.

The second biggest holder of Indonesian LCY central government bonds as of end-September were foreign investors with a share of 28%, which was up significantly from 16% in September 2009. Foreign investors' share has exhibited an upward trend since 2002, when it stood at only 0.46% **(Figure 3)**. At end-September, nearly 70% of bonds held by foreign investors were long-dated tenors (i.e., maturities of more than 5 years). On the other hand, only 10% of bonds held by foreign investors carried maturities of less than 1 year.

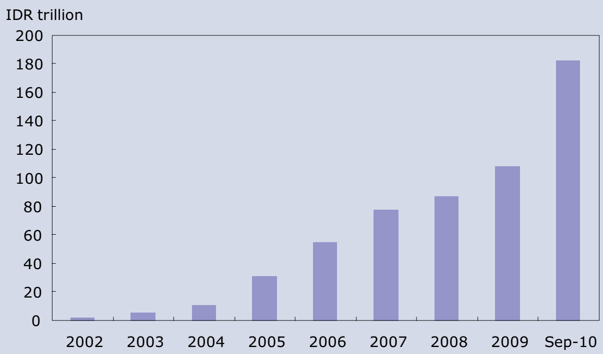
Banks were also the primary holders of SBIs, with a share of 71% at end-September **(Figure 4)**. However, banks' share in SBI holdings has fallen considerably from a high of 89% in June 2009. Foreign interest in SBIs continued to rise in 3Q10 despite the new requirement of a 1-month holding period for SBIs. The share of non-residents' holdings of SBIs rose to 26% at end-September, compared with 16% at end-June and 17% at end-September 2009. Meanwhile, the share of non-bank residents was flat, compared with both end-June and end-September 2009, at about 3%.

**Figure 2: LCY Government Bonds Investor Profile**



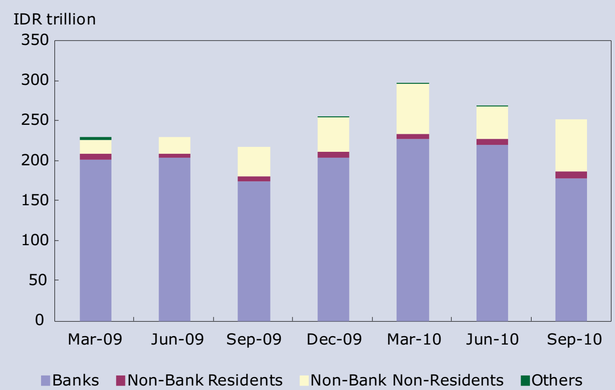

LCY = local currency.
Source: Indonesia Debt Management Office.

**Figure 3: Foreign Holdings of LCY Government Bonds**




LCY = local currency.
Source: Indonesia Debt Management Office.

**Figure 4: LCY Central Bank Bills Investor Profile**




LCY = local currency.
Source: Bank Indonesia.

## Rating Changes

On 13 July, Indonesia's sovereign rating was raised to investment grade by Japan Credit Rating Agency (JCR). Specifically, Indonesia's foreign currency long-term debt and local currency long-term debt were upgraded by JCR to BBB- (from BB+) and BBB (from BBB-), respectively, while the rating outlook for both was stable. According to JCR, the upgrade reflects the country's sustained growth, which is being accompanied by strong domestic demand; a reduced public debt burden; increased resilience to external shocks; improved political and social stability; and government efforts to deal with structural issues.

On 14 October, Rating and Investment Information (R&I) affirmed Indonesia's foreign currency issuer rating at BB+ and changed the outlook to positive from stable **(Table 4)**. R&I believes that a rating upgrade to BBB is possible once Indonesia is able to sustain balanced economic growth by boosting investment in infrastructure. The rating agency also affirmed Indonesia's foreign currency short-term debt rating at a-3.

**Table 4: Selected Sovereign Ratings and Outlook for Indonesia**

| | Moody's | S&P | Fitch | R&I |
|---|---|---|---|---|
| Sovereign FCY LT Ratings | Ba2 | BB | BB+ | BB+ |
| Outlook | positive | positive | stable | positive |

FCY = foreign currency, LT = long term.
Source: Rating agencies.

## Policy, Institutional, and Regulatory Developments

### BI Announces New Regulations on Reserve Requirements and Bank Lending

In September, BI announced new regulations on reserve requirements and bank lending to help contain inflation and boost economic growth. Beginning in November, the primary reserve requirement will be raised to 8.0% of deposits—from 5.0%—while the secondary reserve requirement will remain at 2.5%. Banks that are able to comply with the new primary reserve requirement will earn 2.5% interest on the amount covering the 3-percentage-point increase in primary reserves. On the other hand, those banks that fail to meet the new 8.0% primary reserve requirement will be fined the equivalent of 125% of the average 1-day overnight Jakarta Interbank Offered Rate (JIBOR). BI also announced a regulation designed to give banks incentives for maintaining their loan-to-deposit ratios within a range of 78%–100%, effective 1 March 2011.

### BI Plans to Offer New Term Deposits

In October, BI announced that it is planning to issue new term deposits as it seeks to reduce currency volatility following a surge in capital inflows. The central bank is looking at offering term deposits with maturities of 3, 6, and 9 months. Currently, 1- and 2-month deposits are being offered. The central bank has yet to decide when to issue the new term deposits.

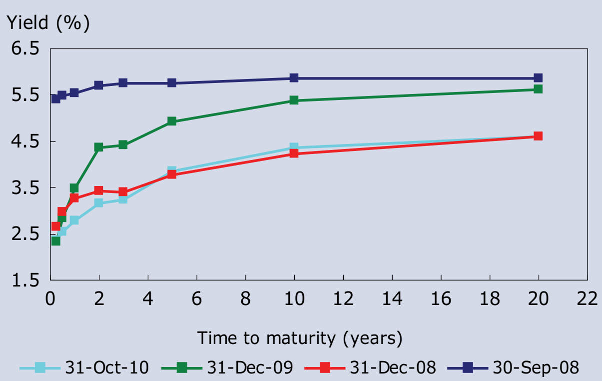
# Republic of Korea—Update

## Yield Movements

The Republic of Korea's government bond yields fell for most maturities between end-December 2009 and end-October 2010 **(Figure 1)**. Yield movements were mixed for maturities of less than 1 year, while yields for 1-, 2-, and 3-year tenors decreased 70, 121, and 116 basis points, respectively. Yields for 5-, 10-, and 20-year maturities fell 106, 103, and 102 basis points, respectively. Meanwhile, the yield spread between 2- and 10-year tenors widened by 18 basis points between end-December and end-October.

The Bank of Korea's (BOK) accommodative monetary policy stance, relatively low interest rates, and buoyant foreign investment in local currency (LCY) bonds all appear to have induced the decline in government bond yields. Based on data from the Financial Supervisory Service (FSS), foreign investor holdings of Korea Treasury Bonds (KTBs) rose sharply to KRW47.6 trillion in October from KRW27.5 trillion in December last year. The FSS also reported that the People's Republic of China's (PRC) net investments in the Republic of Korea bonds during the first 10 months of the year stood at KRW3.7 trillion, which trailed only Luxembourg's KRW5.7 trillion.

**Figure 1: The Republic of Korea's Benchmark Yield Curve—LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

The Republic of Korea's gross domestic product (GDP) growth in 3Q10 stood at 4.5% year-on-year (y-o-y), compared with 7.2% in 2Q10, and 0.7% quarter-on-quarter (q-o-q), compared with 1.4% in 2Q10. Consumer price inflation accelerated to 4.1% y-o-y in October from 3.6% in September. On 16 November, the BOK raised its 7-day repurchase rate for the second time in 2010 by 25 basis points to 2.50%.

## Size and Composition

The size of the Republic of Korea's LCY bond market grew 8.7% y-o-y and 1.8% q-o-q to reach KRW1,278.9 trillion (USD1,126 billion) as of end-September **(Table 1)**. The expansion in the size of the Republic of Korea's bond market was brought about by positive growth in both government and corporate bonds.

As of end-September, LCY government bonds climbed 4.6% y-o-y and 1.2% q-o-q to KRW565.4 trillion (USD498 billion). The growth stemmed from an expansion in central government bonds, which increased 10.9% y-o-y and 3.7% q-o-q to KRW370.6 trillion (USD326 billion), driven mainly by 12.3% y-o-y growth (4.3% q-o-q) in KTBs. The size of BOK bonds, or Monetary Stabilization Bonds (MSBs), also increased 5.9% y-o-y, but declined 1.9% q-o-q, to KRW164.5 trillion (USD145 billion).

The Republic of Korea's LCY corporate bond market grew 12.1% y-o-y and 2.3% q-o-q to KRW713.5 trillion (USD628 billion) as of end-September. The growth in the corporate bond market came from an expansion in both private corporate bonds and special public bonds. Private corporate bonds increased 9.6% y-o-y and 1.3% q-o-q to reach KRW255.4 trillion (USD225 billion), while special public bonds rose 34.0% y-o-y and 6.6% q-o-q to reach KRW250.6 trillion (USD221 billion). In contrast, the outstanding size of financial debentures (excluding Korea Development Bank [KDB]) fell 4.1% y-o-y and 1.4% q-o-q to KRW207.5 trillion (USD183 billion).

**Table 1: Size and Composition of the LCY Bond Market in the Republic of Korea**

| | **Amount** (billion) | | | | | | | | **Growth Rate** (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Jun-10** | | **Jul-10** | | **Aug-10** | | **Sep-10** | | **Jun-10** | | **Jul-10** | **Aug-10** | **Sep-10** | | |
| | **KRW** | **USD** | **KRW** | **USD** | **KRW** | **USD** | **KRW** | **USD** | **y-o-y** | **q-o-q** | **m-o-m** | **m-o-m** | **y-o-y** | **q-o-q** | **m-o-m** |
| Total | 1,256,605 | 1,029 | 1,258,771 | 1,064 | 1,269,076 | 1,060 | 1,278,906 | 1,126 | 10.1 | 4.6 | 0.2 | 0.8 | 8.7 | 1.8 | 0.8 |
| Total Government | 558,900 | 458 | 557,784 | 472 | 560,998 | 469 | 565,376 | 498 | 5.9 | 8.1 | (0.2) | 0.6 | 4.6 | 1.2 | 0.8 |
| Central Bank Bonds | 167,610 | 137 | 162,870 | 138 | 163,140 | 136 | 164,470 | 145 | 1.2 | 3.4 | (2.8) | 0.2 | 5.9 | (1.9) | 0.8 |
| Central Government Bonds | 357,475 | 293 | 362,550 | 307 | 366,375 | 306 | 370,643 | 326 | 14.8 | 0.2 | 1.4 | 1.1 | 10.9 | 3.7 | 1.2 |
| Industrial Finance Debentures | 33,815 | 28 | 32,364 | 27 | 31,482 | 26 | 30,263 | 27 | (33.2) | (4.4) | (4.3) | (2.7) | (40.5) | (10.5) | (3.9) |
| Corporate | 697,705 | 571 | 700,987 | 593 | 708,078 | 591 | 713,530 | 628 | 13.7 | 2.0 | 0.5 | 1.0 | 12.1 | 2.3 | 0.8 |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Central government bonds include Treasury bonds, National Housing bonds, and Seoul Metropolitan Subway bonds.
3. Bloomberg LP end-of-period LCY—USD rates are used.
4. Growth rates are calculated from LCY base and do not include currency effects.
Source: Bank of Korea and *KoreaBondWeb*.

The top 10 issuers of LCY special public bonds had a combined KRW216.4 trillion (USD191 billion) of bonds outstanding as of end-September—compared with KRW208.5 trillion (USD171 billion) at end-June—and comprised 86.3% of total LCY special public bonds outstanding **(Table 2)**. Korea Land Housing Corp., Korea Housing Finance Corp., and Korea Deposit Insurance Corp. are the three largest issuers of special public bonds.

**Table 2: Top 10 Issuers of LCY Special Public Bonds in the Republic of Korea, September 2010**

| **Issuer** | **Outstanding Amount** | |
|---|---|---|
| | **LCY Bonds** (KRW billion) | **LCY Bonds** (USD billion) |
| 1. Korea Land & Housing Corp | 54,421 | 47.9 |
| 2. Korea Housing Finance Corp | 32,229 | 28.4 |
| 3. Korea Deposit Insurance Corp | 26,381 | 23.2 |
| 4. Korea Finance Corp | 23,980 | 21.1 |
| 5. Korea Electric Power Corp | 20,730 | 18.3 |
| 6. Korea Highway | 16,760 | 14.8 |
| 7. Small & Medium Business Corp | 14,633 | 12.9 |
| 8. Korea Gas Corp | 10,430 | 9.2 |
| 9. Korea Rail Network Authority | 10,385 | 9.1 |
| 10. Korea Railroad Corp | 6,410 | 5.6 |
| **Total Top 10** | **216,359** | **190.6** |
| **Total LCY Special Public Bonds** | **250,562** | **220.7** |
| **Top 10 as % of Total LCY Special Public Bonds** | **86.3%** | **86.3%** |

LCY = local currency.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

The top 10 issuers of LCY financial debentures (excluding KDB) had an aggregate outstanding amount of KRW163.7 trillion (USD144 billion) as of end-September, which was lower than the end-June level of KRW174.7 trillion (USD143 billion), and comprised 79% of total LCY financial debentures **(Table 3)**. The largest three issuers of financial debentures were the Industrial Bank of Korea, Kookmin Bank, and Woori Bank.

The top 10 issuers of LCY private corporate bonds in the Republic of Korea had a total of KRW90.0 trillion (USD79 billion) of bonds outstanding as of end-September, up from KRW89.3 trillion (USD73 billion) at end-June, which represented about 35% of total LCY private

**Table 3: Top 10 Issuers of LCY Financial Debentures in the Republic Korea, September 2010**

| Issuer | Outstanding Amount | |
|---|---|---|
| | **LCY Bonds** (KRW billion) | **LCY Bonds** (USD billion) |
| 1. Industrial Bank of Korea | 35,681 | 31.4 |
| 2. Kookmin Bank | 31,244 | 27.5 |
| 3. Woori Bank | 20,702 | 18.2 |
| 4. Shinhan Bank | 19,737 | 17.4 |
| 5. Hana Bank | 14,631 | 12.9 |
| 6. Nonghyup | 14,442 | 12.7 |
| 7. Shinhan Card | 9,142 | 8.1 |
| 8. Hyundai Capital Services | 6,460 | 5.7 |
| 9. Export-Import Bank of Korea | 5,950 | 5.2 |
| 10. Standard Chartered First Bank Korea | 5,743 | 5.1 |
| **Total Top 10** | **163,732** | **144.2** |
| **Total LCY Financial Debentures** | **207,530** | **182.8** |
| **Top 10 as % of Total LCY Financial Debentures** | **78.9%** | **78.9%** |

LCY = local currency.
Note: Financial debentures exclude Korea Development Bank.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

**Table 4: Top 10 Issuers of LCY Private Corporate Bonds in the Republic of Korea, September 2010**

| Issuer | Outstanding Amount | |
|---|---|---|
| | **LCY Bonds** (KRW billion) | **LCY Bonds** (USD billion) |
| 1. Daewoo Securities | 19,539 | 17.2 |
| 2. Woori Investment and Securities | 14,046 | 12.4 |
| 3. Korea Investment and Securities | 11,103 | 9.8 |
| 4. Hyundai Securities | 10,985 | 9.7 |
| 5. Tong Yang Securities | 6,722 | 5.9 |
| 6. Mirae Asset Securities | 6,405 | 5.6 |
| 7. Shinhan Financial Group | 6,020 | 5.3 |
| 8. Hana Daetoo Securities | 5,136 | 4.5 |
| 9. Samsung Securities | 5,056 | 4.5 |
| 10. KT Corporation | 5,020 | 4.4 |
| **Total Top 10** | **90,032** | **79.3** |
| **Total LCY Private Corporate Bonds** | **255,438** | **225.0** |
| **Top 10 as % of Total LCY Private Corporate Bonds** | **35.2%** | **35.2%** |

LCY = local currency.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

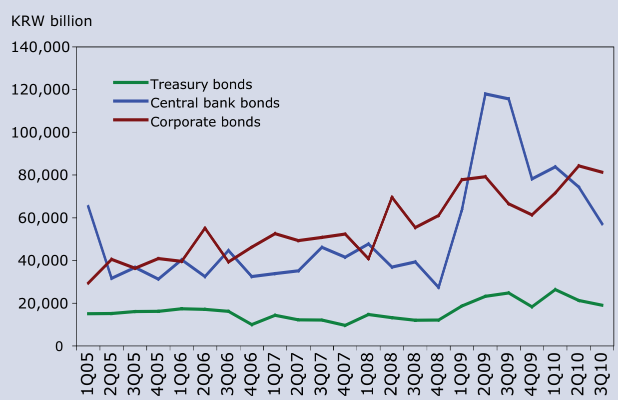
corporate bonds outstanding **(Table 4)**. The largest three issuers were Daewoo Securities, Woori Investment and Securities, and Korea Investment and Securities.

## Issuance

The issuance of major types of LCY government and corporate bonds slowed in 3Q10 **(Figure 2)**. Issuance of KTBs dropped 10.2% q-o-q and 23.0% y-o-y to KRW19.1 trillion (USD17 billion), while BOK issuance of MSBs also decreased 23.1% q-o-q and 50.5% y-o-y to KRW57.2 trillion (USD50 billion). Corporate bond issuance in 3Q10 stood at KRW81.4 trillion (USD72 billion), which was 3.5% lower than the previous quarter, but 22.3% higher on a y-o-y basis. On a q-o-q basis, the slight drop in corporate bond issuance was mainly due to declines of 19.7% and 11.0% in financial debentures and private corporate bonds, respectively, more than offsetting the 37.5% rise in the issuance of special public bonds.

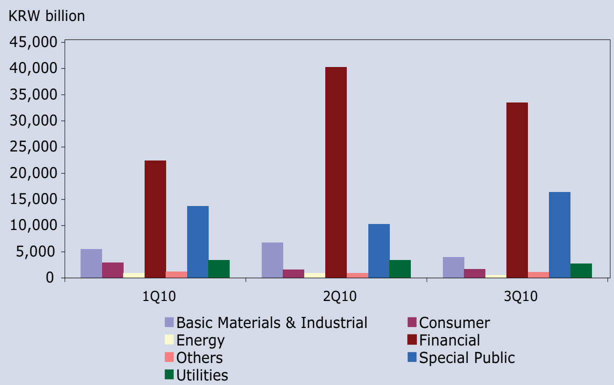
The sector with the largest corporate bond issuance in the Republic of Korea in 3Q10 was the financial sector, comprising about 56% of the total **(Figure 3)**. On a q-o-q basis, corporate bond issuance fell for most sectors in 3Q10, including the basic materials/industrial, energy, financial, and utilities sectors. On the other hand, the consumer, special public, and other sectors

**Figure 2: Local Currency Bond Issuance in the Republic of Korea, 1Q05–3Q10**




Source: *AsianBondsOnline*, The Bank of Korea, and *KoreaBondWeb*.

**Figure 3: The Republic of Korea's LCY Corporate Bond Issuance by Sector, 1Q10–3Q10**




LCY = local currency.
Source: Bloomberg LP.

recorded higher corporate bond issuance in 3Q10 that in the previous quarter. About 51% of the issuance in special public bonds during 3Q10 were made by public finance companies.

## Investor Profile

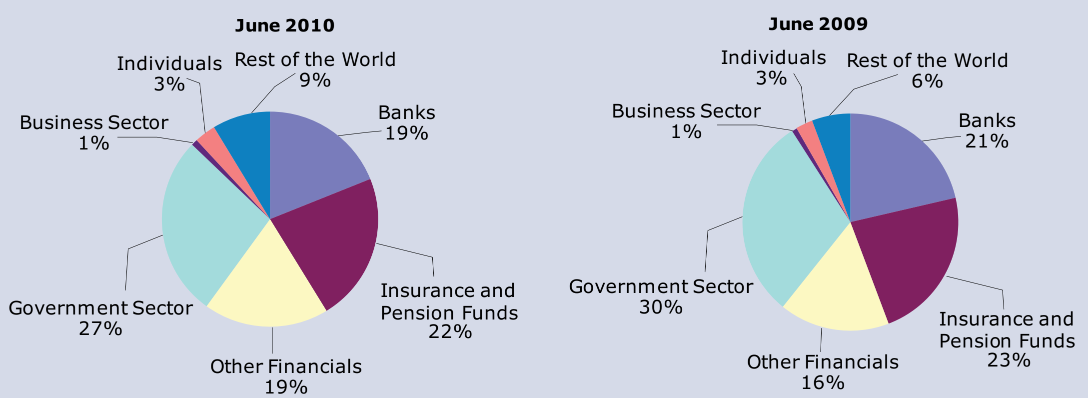
The Republic of Korea's public sector remained the largest owner of government bonds in June 2010, with a 27% share of the total **(Figure 4)**. Insurance firms/pension funds were the second-largest holder of government bonds with a 22% share, while banks and other financial institutions held 19% each. Foreign investors held 9% of government bonds. Compared with June 2009, the shares of financial institutions (other than banks and insurance firms/pension funds) and foreign investors climbed by 3 percentage points each. Conversely, the share of the government sector fell 3 percentage points, the share of banks dropped 2 percentage points, and the share of insurance firms/pension funds decreased 1 percentage point.

## Liquidity

Liquidity improved for both LCY government and corporate bonds in 3Q10 **(Figure 5)**. The trading volume for government bonds rose 39.4% q-o-q and 53.3% y-o-y, while the turnover ratio for these bonds increased to 1.19 in 3Q10 from 0.86 in 2Q10. Similarly, the trading volume for corporate bonds surged 141.1% q-o-q and 80.0% y-o-y, and the turnover ratio for corporate bonds climbed to 0.25 in 3Q10 from 0.10 in the previous quarter.

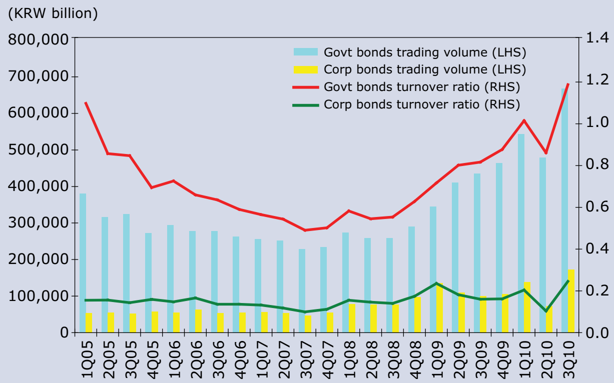
The increased liquidity of the LCY government bonds in 3Q10 may be attributed to a quarterly rise in trading volumes and turnover ratios for both central government and central bank bonds **(Figure 6)**. The trading volume for central government bonds climbed 7.2% q-o-q and 51.2% y-o-y, while the turnover ratio increased to 1.16 in 3Q10 from 1.10 in 2Q10. For central bank bonds, the trading volume soared 181.8% q-o-q

**Figure 4: Investor Profile for LCY Government Bonds in the Republic of Korea**



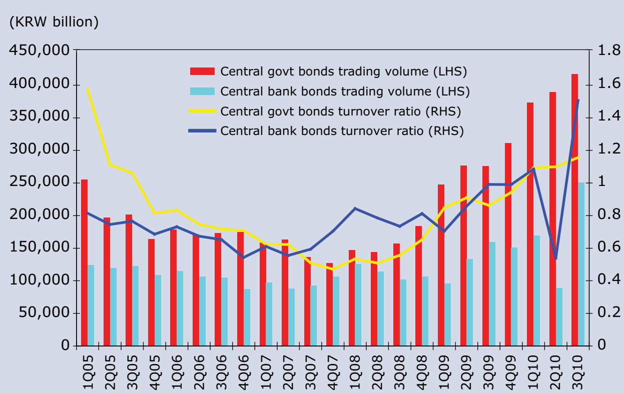

LCY = local currency.
Source: The Bank of Korea.

**Figure 5: Trading Volumes and Turnover Ratios of the LCY Government and Corporate Bonds in the Republic of Korea, 1Q05–3Q10**



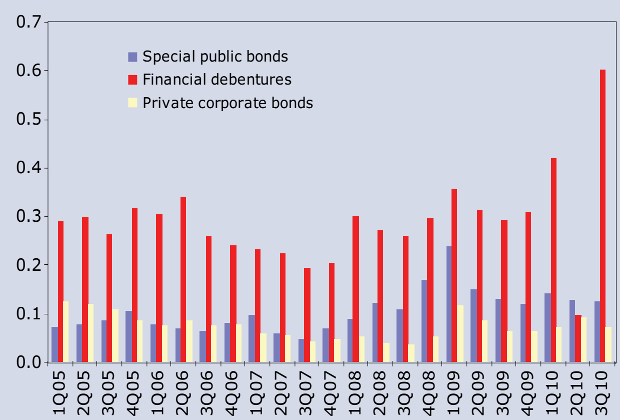

Notes:
1. LHS = left-hand side, RHS = right-hand side, LCY = local currency.
2. Trading volume is the average of sales and purchases of bonds traded.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

**Figure 6: Turnover Ratios for LCY Government Bonds in the Republic of Korea, 1Q05–3Q10**




Notes:
1. LHS = left-hand side, RHS = right-hand side, LCY = local currency.
2. Trading volume is the average of sales and purchases of bonds traded.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

**Figure 7: Turnover Ratios for Types of the Republic of Korea Local Currency Corporate Bonds, 1Q05-3Q10**




Source: *AsianBondsOnline,* The Bank of Korea, *KoreaBondWeb*.

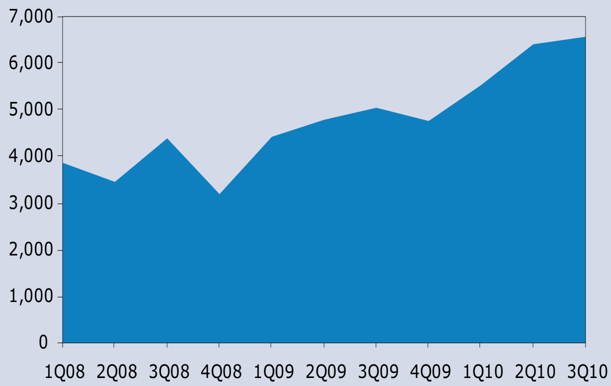
and 57.2% y-o-y in 3Q10, while the turnover ratio rose to 1.51 from 0.54.

In 3Q10, the turnover ratio for central bank bonds was higher than that for central government bonds, suggesting that central bank bonds were relatively more liquid than central government bonds. This appears to be consistent with the 2010 *AsianBondsOnline* liquidity survey results, which showed that the average on-the-run bid–ask spread for BOK bonds (excluding BOK bills) was 1.11 basis points, which was slightly lower than 1.14 basis points for KTBs.

Across the major types of LCY corporate bonds in the Republic of Korea, the turnover ratio for financial debentures increased to 0.60 in 3Q10 from 0.1 in the previous quarter, but the turnover ratios for special public bonds and private corporate bonds fell marginally in 3Q10 to 0.12 (from 0.13 in 2Q10) and 0.07 (from 0.09 in 2Q10), respectively **(Figure 7)**. This also appears to be consistent with the 2010 *AsianBondsOnline* liquidity survey results, which revealed that financial debentures were relatively more liquid than the other types of corporate bonds as evident by having the lowest average on-the-run bid–ask spread at 2.17 basis points, followed by special public bonds and private corporate bonds with average bid–ask spreads of 2.58 and 3.58 basis points, respectively.

In the KTB futures market, there was an improvement in the liquidity of 3-year KTB futures in 3Q10. In particular, the number of 3-year KTB futures contracts traded rose 2.5% q-o-q and 30.2% y-o-y to 6.6 million **(Figure 8)**.

**Figure 8: Trading Volume of 3-Year KTB Futures, 1Q08–3Q10** (number of contracts traded, thousands)




KTB = Korea Treasury Bonds.
Source: Korea Exchange (KRX).

## Rating Changes

On 11 November, Fitch Ratings affirmed the sovereign credit ratings of the Republic of Korea at A+ for its long-term foreign currency (FCY) issuer default rating, AA for its long-term LCY issuer default rating, F1 for its short-term issuer default rating, and AA for its country ceiling **(Table 5)**. It has also maintained its stable outlook for the Republic of Korea. Fitch Ratings reported that the Republic of Korea's credit strengths, including its fiscal prudence, improved external finances, and strong balance sheet, have continued to balance against the country's fiscal and geopolitical risks.

**Table 5: Selected Sovereign Ratings and Outlook for the Republic of Korea**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | A1 | A | A+ |
| Outlook | stable | stable | stable |

FCY = foreign currency, LT = long term.
Source: Rating agencies.

## Policy, Institutional, and Regulatory Developments

### Short-Term KTBs to be Introduced

In July, the Republic of Korea announced its plan to issue KTBs with maturities of less than 1 year in order to form a short-term benchmark bond rate. The issuance of short-term KTBs will take place following revisions to the National Finance Act to be made in 2011/12.

### FSC Approves Regulation to Improve Trading of Long-Term KTB Futures

In September, the Financial Services Commission approved the Korea Exchange's amended version of its Derivatives Market Business Regulation, which aims to enhance the trading of long-term KTB futures. The revised version calls for harmonizing regulations on short-term and long-term KTB futures to improve their accessibility and facilitate the trading of these derivative instruments. This provision includes a change of the final settlement method for 10-year KTB futures to cash settlement (from physical delivery) in order for primary dealers to actively trade 10-year KTB futures. The amended version aims to stabilize price movements and enhance market-making functions in the KTB futures market.

# Malaysia—Update

## Yield Movements

Between end-December 2009 and end-October 2010, Malaysian government bond yields rose at the short-end of the curve, while yields fell at the middle to the long-end of the curve **(Figure 1)**. The flattening of the yield curve reflected expectations of benign inflation, providing room for the central bank to put monetary tightening on hold. Bank Negara Malaysia (BNM) decided to keep its key policy rate steady at 2.75% during the last monetary policy committee meeting on 12 November. BNM has already raised its key rate three times in 2010 by a total of 75 basis points.

After posting robust 9.5% year-on-year (y-o-y) growth in 1H10, Malaysia's gross domestic product (GDP) is expected to expand 7.0% for all of 2010. According to the latest annual Economic Report 2010/2011 issued by the Ministry of Finance, Malaysia's economy is expected to grow 5%–6% in 2011, supported by resilient domestic demand.

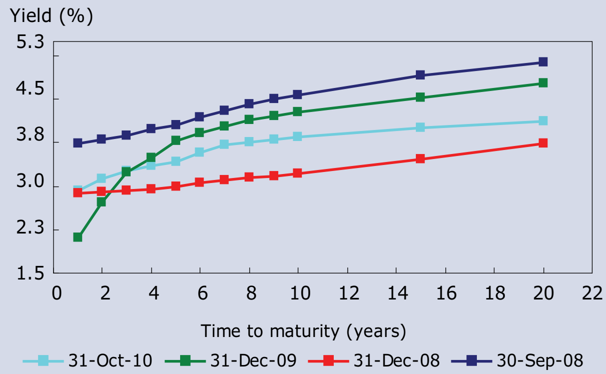
The report also says that the government is on track to meet its 2010 budget deficit target of 5.6% of GDP. Government expenditure is expected to reach MYR206.2 billion in 2010, while revenue is expected to reach MYR162.1 billion. For 2011, the government expects its budget deficit as a percentage of GDP to fall to 5.4%.

Consumer price inflation in Malaysia slid to 1.8% year-on-year (y-o-y) in September from 2.1% in August and 1.9% in July. For the January–September period, consumer price inflation was reported at 1.5% y-o-y.

## Size and Composition

As of end-September, the total amount of outstanding local currency (LCY) bonds had increased 15.1% y-o-y to MYR721.3 billion **(Table 1)**. Outstanding government LCY bonds surged 20.9% y-o-y to MYR421.6 billion, mainly due to the increase in outstanding central bank bills as BNM continued to mop up excess liquidity in the market. Excluding central bank bills, outstanding government LCY bonds rose by 9.5% y-o-y. Meanwhile, corporate LCY bonds outstanding increased by 7.8% y-o-y.

**Figure 1: Malaysia's Benchmark Yield Curve–LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding increased 3.7% in 3Q10 as outstanding central bank bills grew 17.0%. Issuance of central bank bills increased from MYR68.2 billion in 2Q10 to MYR76.0 billion in 3Q10. Corporate LCY bonds inched up slightly, posting 1.7% q-o-q growth.

Issuance of corporate LCY bonds amounted to MYR21.6 billion in 3Q10, which was down 5.8% q-o-q and 7.6% y-o-y. Among the large corporate LCY issues during July–September were the *sukuk* (Islamic bond) issuances of Celcom Transmission (MYR4.2 billion), Cagamas (MYR1.0 billion), and Malaysia Airports Capital (MYR1.0 billion). Also, two banks from the Republic of Korea issued MYR-denominated bonds: Export–Import Bank of Korea (MYR850 million) and Woori Bank (MYR320 million).

As of end-September, the top 20 corporate LCY issuers accounted for 46.2% of total corporate

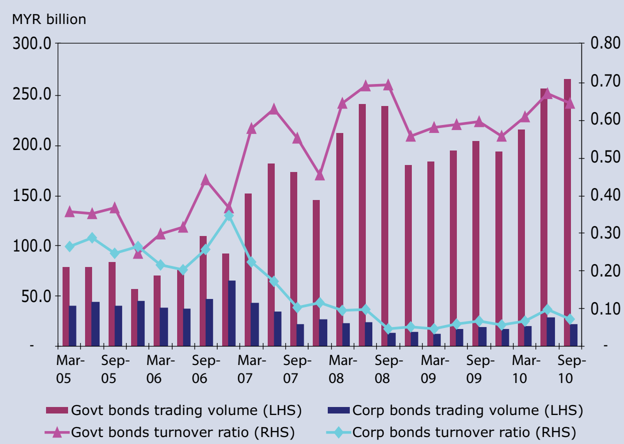
LCY bonds outstanding **(Table 2)**. National mortgage corporate Cagamas Bhd remained the biggest issuer of corporate LCY bonds, with MYR18.1 billion outstanding at the end of 3Q10, followed by Khazanah Nasional and Binariang GSM, with MYR13.2 billion and MYR11.3 billion, respectively.

## Turnover

Government LCY bond trading volume reached MYR265.8 billion in 3Q10 from MYR256.4 billion in 2Q10. However, the turnover ratio was 0.65 in 3Q10, slightly lower than the turnover ratio of 0.67 in 2Q10. Meanwhile, the trading volume of corporate LCY bonds fell to MYR21.5 billion in 3Q10 from MYR28.3 billion in 2Q10. The turnover ratio for corporate LCY bonds dropped to 0.07 in 3Q10 from 0.10 in 2Q10 **(Figure 2)**.

The trading of treasury bills and bonds remained high in 3Q10, with total trading volume reaching MYR124.1 billion, while the turnover was steady at 0.37. On the other hand, the trading of central bank bills increased in July–September, amounting to MYR141.7 billion, as the central bank issued more bills in 3Q10. However, the turnover ratio dropped for central bank bills to 1.89 in 3Q10 from 2.65 in the previous quarter **(Figure 3)**.

**Figure 2: LCY Bonds Quarterly Trading Volume and Turnover Ratio**




LCY = local currency, LHS = left-hand side, RHS = right-hand side.
Source: Bank Negara Malaysia, Fully Automated System for Issuing/Tendering (FAST).

**Table 1: Size and Composition of the LCY Bond Market in Malaysia**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | MYR | USD | MYR | USD | MYR | USD | MYR | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 695.9 | 215.7 | 702.5 | 220.2 | 710.7 | 225.6 | 721.3 | 233.8 | 14.0 | 7.4 | 1.0 | 1.2 | 15.1 | 3.7 | 1.5 |
| Government | 401.2 | 124.4 | 408.5 | 128.0 | 414.9 | 131.7 | 421.6 | 136.7 | 18.3 | 10.8 | 1.8 | 1.6 | 20.9 | 5.1 | 1.6 |
| Central Government Bonds | 331.2 | 102.7 | 337.7 | 105.8 | 336.8 | 106.9 | 339.8 | 110.2 | 15.0 | 0.9 | 2.0 | (0.3) | 10.7 | 2.6 | 0.9 |
| Central Bank Bills | 69.1 | 21.4 | 69.8 | 21.9 | 77.1 | 24.5 | 80.8 | 26.2 | 58.0 | 112.8 | 1.1 | 10.5 | 116.0 | 17.0 | 4.8 |
| Others | 1.0 | 0.3 | 1.0 | 0.3 | 1.0 | 0.3 | 1.0 | 0.3 | (87.1) | (43.7) | - | - | (77.5) | - | - |
| Corporate | 294.7 | 91.4 | 294.1 | 92.2 | 295.8 | 93.9 | 299.7 | 97.2 | 8.6 | 3.1 | (0.2) | 0.6 | 7.8 | 1.7 | 1.3 |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY—USD rate is used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. "Others" refer to Khazanah Bonds issued by Khazanah Nasional Berhad and Cagamas, Bonds and Notes, Bithaman Ajil Islamic Securities, Sanadat ABBA Cagamas, and Sanadat Mudharabah Cagamas issued by Cagamas Berhad.
Source: Bank Negara Malaysia, Fully Automated System for Issuing/Tendering (FAST), and Bloomberg LP.

**Table 2: Top 20 Corporate Issuers in Malaysia, September 2010** (MYR billion)

| Issuer | Conventional Bonds | Islamic Bonds | Conventional MTN | Islamic MTN | Total |
|---|---|---|---|---|---|
| Cagamas | - | - | 8.98 | 9.12 | 18.09 |
| Khazanah | - | 13.20 | - | - | 13.20 |
| Binariang GSM | - | 3.02 | - | 8.28 | 11.30 |
| Project Lebuhraya | - | 6.57 | - | 3.68 | 10.25 |
| Prasarana | 5.10 | 2.00 | - | 2.00 | 9.10 |
| Maybank | 6.10 | 2.50 | - | - | 8.60 |
| Malakoff Corp | - | 1.70 | - | 5.60 | 7.30 |
| Rantau Abang Capital Bhd | - | - | - | 7.00 | 7.00 |
| KL International Airport | 1.60 | 4.76 | - | - | 6.36 |
| AM Bank | 1.06 | - | 4.40 | - | 5.46 |
| Value Cap | 5.10 | - | - | - | 5.10 |
| 1 Malaysia Development Bhd | - | - | - | 5.00 | 5.00 |
| Jimah Energy Ventures | - | - | - | 4.77 | 4.77 |
| Tanjung Bin | - | - | - | 4.59 | 4.59 |
| Bank Pembangunan Malaysia | 1.00 | - | 2.60 | 0.90 | 4.50 |
| Celcom Transmission | - | - | - | 4.20 | 4.20 |
| Putrajaya Holdings | - | 0.99 | - | 3.07 | 4.06 |
| YTL Power International | 2.20 | - | 1.70 | - | 3.90 |
| Tenaga Nasional | 1.50 | 2.15 | - | - | 3.65 |
| Danga Capital | - | - | - | 3.60 | 3.60 |
| **Total** | **23.66** | **36.89** | **17.68** | **61.79** | **140.02** |
| **% of total corporate outstanding** | | | | | **46.72%** |

— = not applicable, MTN = medium-term notes.
Source: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST).

## Policy, Institutional, and Regulatory Developments

### BNM Further Liberalizes FX Rules

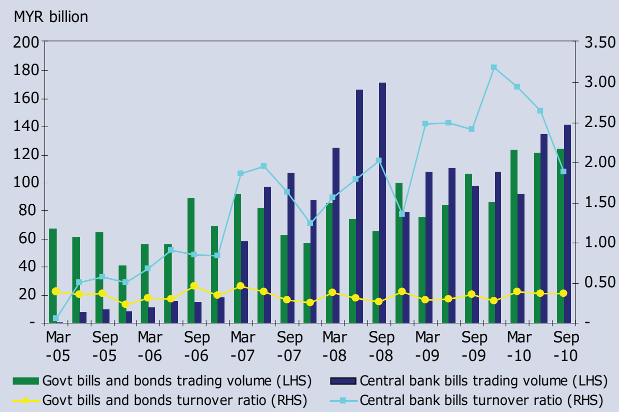
In August, BNM announced the further liberalization of foreign exchange (FX) administrative rules to promote efficiency in trade. The new rules provide for the following:

(i) the use of the ringgit as a settlement currency for the international trade of goods and services between residents and non-residents;

(ii) the borrowing of any amount of foreign currency by a resident company from its respective non-resident, non-bank related company, thus abolishing all limits on cross-border, foreign currency inter-company borrowings; and

(iii) the lifting of the limit on residents' anticipatory hedging of current account transactions with licensed onshore banks.

**Figure 3: Trading Volume and Turnover Ratios of Gov't Bills and Bonds and Central Bank Bills**




LHS = left-hand side, RHS = right-hand side.
Note: Trading volume of government bills and bonds include trading volume of treasury bills, Malaysian Government Securities (MGS), and Government Investment Issues (GII).
Source: Bank Negara Malaysia, FAST.

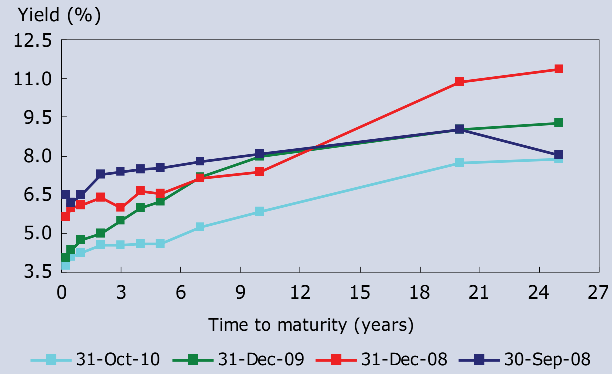
To promote bilateral trade between the People's Republic of China and Malaysia, the China Foreign Exchange Trading System (CFETS) has issued a separate statement that allows trading of the yuan against the ringgit. Aside from the ringgit, other currencies that are traded on the CFETS are the US dollar, euro, pound sterling, yen, and Hong Kong dollar.

# Philippines—Update

## Yield Movements

Philippine government bond yields fell for all maturities between end-December 2009 and end-October 2010 on expectations of sustained economic growth **(Figure 1)**. The decline at the shorter-end of the curve ranged between 25 and 95 basis points, while the drop at the belly to the longer-end of the curve was more significant, ranging from 140 to 215 basis points. Yield spreads between 2- and 10-year tenors narrowed to 133 basis points in end-October 2010, from 300 basis points at end-December 2009, as the yield curve flattened.

**Figure 1: Philippines' Benchmark Yield Curve–LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

The Philippines' gross domestic product (GDP) posted 7.9% year-on-year (y-o-y) growth in 2Q10, following revised 7.8% growth in 1Q10, brought about by the improved performance of domestic investment as well as sustained moderate growth in personal consumption and government spending.

In November, the Monetary Board of the Bangko Sentral ng Pilipinas (BSP), based on its benign outlook for inflation, decided to keep its overnight borrowing (reverse repurchase) rate at 4.0% and the overnight lending (repurchase) rate at 6.0%. Consumer price inflation eased to 2.8% y-o-y in October—its lowest level in 11 months—from 3.2% in September. The inflation rate in January–October stood at 4.0%, well within the central bank's target of 3.5%–5.5% for 2010.

Meanwhile, the Philippine government posted a PHP259.8 billion fiscal deficit in the first 9 months of 2010, which was less than the budgeted amount of PHP273.7 billion due to lower-than-expected spending. Revenue collections in the first 9 months of the year for both the Bureau of Internal Revenue and the Bureau of Customs fell below their respective targets. On the other hand, total expenditure was lower at PHP1.15 trillion, compared with a PHP1.21 trillion target, as a result of savings in interest payments brought about by lower borrowing costs. The government has set its budget deficit ceiling for 2010 at PHP325 billion, or approximately 3.9% of GDP. The government also plans to cut the deficit to 3.2% of GDP in 2011 and 2.6% in 2012.

## Size and Composition

The Philippines' total local currency (LCY) bonds outstanding increased 13.0% y-o-y to PHP3.18 trillion as of end-September **(Table 1)**. On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding grew 3.6%, driven by an increase in outstanding government bonds.

Outstanding government LCY bonds rose 11.8% y-o-y to PHP2.80 trillion as of end-September, mainly due to the 15.6% y-o-y increase in outstanding government treasury bonds. Other bonds, which include government-guaranteed bonds and bonds owned by government-owned-and-controlled corporations (GOCCs), increased 47.9% y-o-y to reach PHP132 million. Meanwhile, the outstanding amount of treasury bills fell 4.8% y-o-y to PHP578 billion.

In 3Q10, the government issued a total of PHP113.3 billion in government bonds, including PHP97.5 billion worth of 5-, 7-, and 10-year retail treasury bonds. The government also issued PHP62.5 billion in treasury bills.

**Table 1. Size and Composition of the LCY Bond Market in the Philippines**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | PHP | USD | PHP | USD | PHP | USD | PHP | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 3,072 | 66.2 | 3,110 | 68.3 | 3,206 | 70.7 | 3,182 | 72.5 | 11.6 | 2.5 | 1.2 | 3.1 | 13.0 | 3.6 | (0.8) |
| Government | 2,696 | 58.1 | 2,727 | 59.9 | 2,824 | 62.3 | 2,799 | 63.7 | 9.8 | 2.1 | 1.2 | 3.5 | 11.8 | 3.8 | (0.9) |
| Treasury Bills | 567 | 12.2 | 581 | 12.8 | 613 | 13.5 | 578 | 13.2 | (16.5) | (2.0) | 2.3 | 5.5 | (4.8) | 1.9 | (5.6) |
| Treasury Bonds | 1,996 | 43.0 | 2,015 | 44.3 | 2,079 | 45.9 | 2,089 | 47.6 | 18.3 | 2.5 | 0.9 | 3.2 | 15.6 | 4.6 | 0.5 |
| Others | 132 | 2.8 | 132 | 2.9 | 132 | 2.9 | 132 | 3.0 | 47.9 | 18.1 | 0.0 | 0.0 | 47.9 | - | - |
| Corporate | 376 | 8.1 | 382 | 8.4 | 382 | 8.4 | 383 | 8.7 | 26.8 | 5.5 | 1.7 | 0.0 | 22.4 | 1.7 | 0.0 |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY–USD rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. "Others" includes government-guaranteed bonds such as Land Bank of the Philippines and National Power Corporation (Napocor).
Source: Philippine Bureau of the Treasury and Bloomberg LP.

Meanwhile, outstanding corporate LCY bonds stood at PHP383 billion as of end-September, posting growth of 22.4% y-o-y, but only 1.7% on a q-o-q basis. During July–September, three Philippine corporates issued a total of PHP5.1 billion worth of LCY bonds: (i) Philippine Long Distance Telephone Company (PHP2.5 billion), (ii) its wholly-owned subsidiary Smart Corporation (PHP2.5 billion), and (iii) Ayala Land Inc. (PHP84 million).

As of end-September, the top 20 corporate LCY issuers accounted for 80.3% of total corporate LCY bonds outstanding **(Table 2)**. San Miguel Brewery remained the top issuer with PHP38.8 billion of bonds outstanding, followed by commercial banks Banco de Oro Unibank (PHP33.1 billion) and Rizal Commercial Banking Corporation (PHP21.0 billion).

**Table 2: Top 20 Corporate Bonds Outstanding by Issuers, September 2010**

| Rank | Issuer | Amount Outstanding (PHP billion) |
|---|---|---|
| 1 | San Miguel Brewery | 38.80 |
| 2 | Banco de Oro Unibank | 33.09 |
| 3 | Rizal Commercial Banking Corporation | 21.00 |
| 4 | Manila Electric Company | 20.22 |
| 5 | Metropolitan Bank & Trust Company | 18.50 |
| 6 | Philippine National Bank | 17.75 |
| 7 | Globe Telecom | 16.80 |
| 8 | Petron Corporation | 16.30 |
| 9 | Ayala Corporation | 16.00 |
| 10 | Robinson's Land Corporation | 15.00 |
| 11 | JG Summit Holdings | 13.31 |
| 12 | Energy Development Corporation | 12.00 |
| 13 | First Philippine Holdings | 11.40 |
| 14 | Bank of the Philippine Islands | 10.00 |
| 15 | SM Investments Corporation | 9.40 |
| 16 | Allied Banking Corporation | 8.00 |
| 17 | SM Prime Holdings | 8.00 |
| 18 | Philippine Long Distance Telephone Co | 7.50 |
| 19 | Ayala Land Inc. | 7.34 |
| 20 | Aboitiz Power Corporation | 6.89 |
| **Top 20 Total** | | **307.29** |
| **Total Corporate Bonds Outstanding** | | **382.52** |
| **Top 20 as % of Total Corporate Bonds Outstanding** | | **80.30%** |

LCY = local currency.
Source: Bloomberg LP.

## Rating Changes

In August, Fitch Ratings affirmed the sovereign credit ratings of the Philippines at BB for its foreign currency (FCY) long-term issuer default rating, BB+ for its LCY long-term issuer default rating and country ceiling, and B for its short-term issuer default rating **(Table 3)**. Fitch Ratings also affirmed its stable outlook for the Philippines.

In November, Standard & Poor's (S&P) upgraded its long-term foreign currency (FCY) debt rating for the Philippines to BB from BB-, citing improvements in the country's external liquidity profile and external accounts. The rating upgrade also reflects the progress in the country's debt reduction and fiscal consolidation efforts. S&P has also affirmed its stable outlook for the country.

**Table 3: Selected Sovereign Ratings and Outlook for the Philippines**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Rating | Ba3 | BB | BB |
| Outlook | stable | stable | stable |

FCY = foreign currency, LT = long term.
Source: Rating agencies.

## Policy, Institutional, and Regulatory Developments

### Government and Petron Issue Peso Global Bonds

In September, the government sold PHP44.1 billion (USD1.0 billion) of 10-year bonds in the first offshore LCY bond issuance from an Asian country. These bonds are exempt from the Philippines' 20% tax on interest income. The Philippine government noted that the peso global bond offer will enhance its debt investor profile by attracting more offshore investors to the country's capital markets, and that it will support its external liability management, especially in mitigating exposure to foreign exchange risk. The Bureau of Treasury does not count this bond as part of the government's PHP-denominated bond stock because the bonds are mainly held by foreigners and will be settled in United States (US) dollars upon maturity.

About 1 month after the successful issue of the government's USD1.0 billion peso global bond, energy company Petron Corporation raised PHP20.0 billion from the issuance of a 7-year peso global bond. The Petron global peso bond pays a coupon of 7.0% per year and is subject to a 20% withholding tax.

### BSP Issues Moratorium on Approval of Banks' Hybrid Tier 1 and 2 Capital Instruments

BSP issued a memorandum in October to temporarily halt the approval of hybrid Tier 1, Tier 2, and other redeemable capital instruments. According to BSP, the moratorium was put in place to avoid uncertainty with the upcoming adoption of the Basel 3 reform package, as some debt instruments that are compliant with existing regulatory capital rules may be considered non-compliant under Basel 3. Banks and other financial institutions with approved but unissued hybrid Tier 1 and Tier 2 capital instruments were also advised to defer issuance to ensure conformity with the forthcoming capital guidelines. The moratorium will be in effect until 31 December 2010. The new Basel 3 capital rules, subject to approval of the leaders of the Group of 20 countries, are targeted to be implemented beginning 1 January 2013.

# Singapore—Update

## Yield Movements

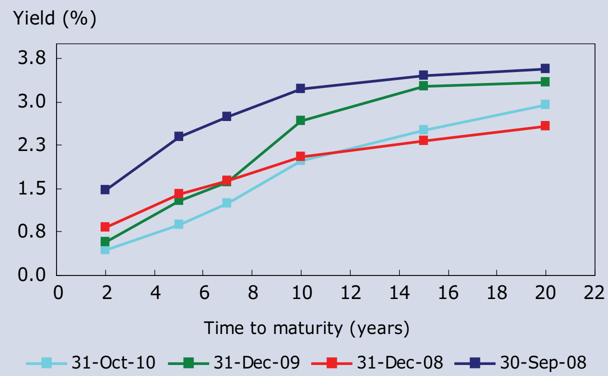
Singapore government bond yields fell throughout the length of the curve between end-December 2009 and end-October 2010 **(Figure 1)**. The yield on the 2-year tenor declined 15 basis points from its end-December level. Yields declined by larger amounts along the rest of the curve: the 5-year tenor declined 40 basis points; the 7-year tenor fell 37 basis points; and yields on the 10-, 15-, and 20-year tenors fell 68, 75, and 39 basis points respectively.

Singapore's economy expanded 10.6% year-on-year (y-o-y) in 3Q10, according to preliminary estimates from the Ministry of Trade and Industry (MTI). The 3Q10 growth rate was down from the revised growth rate 19.5% in 2Q10. Still, growth estimates for the quarter remained on track for Singapore to reach MTI's forecast of around 15.0% economic growth for the full year 2010.

On 14 October, the Monetary Authority of Singapore (MAS) announced in its second policy statement of the year that it would allow a modest and gradual appreciation of the Singapore dollar. MAS said that it would slightly steepen and widen its exchange rate policy band, but would not change the level at which the band is centered. According to MAS, this policy stance remains supportive of Singapore's economic growth and its annual inflation targets of 2.5%–3.0% for 2010 and 2.0%–3.0% for 2011. Consumer price inflation in August rose to 3.3% y-o-y due to increasing costs of transportation, housing, and food. Singapore's consumer price inflation had previously stood at 3.1% y-o-y in July, 2.7% in June, and 3.2% in May.

In April, MAS re-centered its policy band at the prevailing level of the Singapore dollar's nominal effective exchange rate (S$NEER) and shifted the policy band from zero percent appreciation to modest and gradual appreciation. Since then, the S$NEER has fluctuated in the upper half of the policy band.

**Figure 1: Singapore's Benchmark Yield Curve–LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

## Size and Composition

As of end-September, the amount of local currency (LCY) bonds outstanding in Singapore stood at SGD232.8 billion, up 9.9% y-o-y **(Table 1)**. Singapore Government Securities (SGS) bonds and bills, issued by MAS increased 4.5% y-o-y to SGD128.1 billion. MAS has created a highly tradable bond stock by limiting the number of bond issues outstanding to 19, and by frequently re-opening its benchmark issues. This has resulted in an attractive array of uniform maturities for investors, as can be seen in **Figures 2a and 2b**.

Corporate bonds outstanding increased 17.5% y-o-y to SGD104.7 billion. As of end-September, the top 30 corporate issuers accounted for 41.3% of total corporate bonds outstanding **(Table 2)**. Notable issues in 3Q10 included a SGD300 million bond from Singapore Airlines, a SGD350 million bond from property developer Capitaland, and a SGD1.0 billion bond from Temasek.

Large inflows of foreign capital have also had an impact on the corporate bond sector. Singapore corporate issuance grew by 64.8% quarter-on-quarter (q-o-q) and 104.4% y-o-y in 3Q10, resulting

**Table 1. Size and Composition of the LCY Bond Market in Singapore**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | SGD | USD | SGD | USD | SGD | USD | SGD | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 225.9 | 161.7 | 224.3 | 164.9 | 227.5 | 168.0 | 232.8 | 176.8 | 12.6 | 1.8 | (0.7) | 1.4 | 9.9 | 3.1 | 2.3 |
| Government | 128.1 | 91.7 | 125.2 | 92.1 | 125.6 | 92.7 | 128.1 | 97.3 | 10.7 | 1.2 | (2.3) | 0.3 | 4.5 | 0.0 | 2.0 |
| Bills | 53.1 | 38.0 | 53.6 | 39.4 | 54.0 | 39.9 | 54.5 | 41.4 | 15.4 | 2.7 | 0.9 | 0.7 | 10.5 | 2.6 | 0.9 |
| Bonds | 75.0 | 53.7 | 71.6 | 52.6 | 71.6 | 52.9 | 73.6 | 55.9 | 7.6 | 0.1 | (4.5) | 0.0 | 0.4 | (1.9) | 2.8 |
| Corporate | 97.8 | 70.0 | 99.1 | 72.9 | 101.9 | 75.2 | 104.7 | 79.5 | 15.2 | 2.6 | 1.3 | 2.8 | 17.5 | 7.1 | 2.8 |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Government bonds are calculated using data from national sources. Corporate bonds are based on *AsianBondOnline* estimates.
2. Bloomberg LP end-of-period LCY–USD rate is used.
3. Growth rates are calculated from LCY base and do not include currency effects.
Source: Monetary Authority of Singapore, Singapore Government Securities, and Bloomberg LP.

**Figure 2a: Singapore LCY Government Bonds by Maturity** (years)

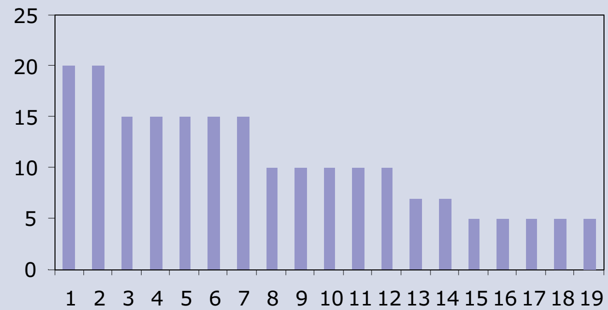
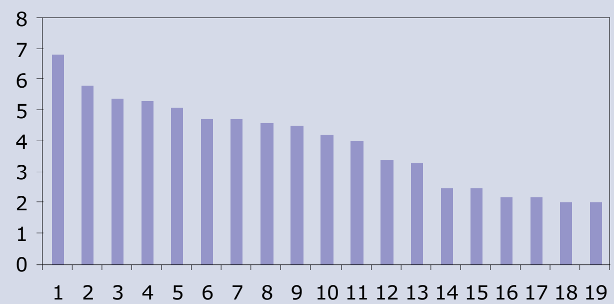



**Figure 2b: Singapore LCY Government Bonds by Size** (SGD billion)




LCY = local currency.
Source: Monetary Authority of Singapore and *AsianBondsOnline*

in increases in corporate bonds outstanding of 7.1% q-o-q and 17.5% y-o-y. While the liquidity of the Singapore corporate bond market is less than that of the SGS bond market, it is improving rapidly and fund managers are actively seeking out Singapore corporate bonds for inclusion in their portfolios.

The current structure of Singapore's corporate bond market can be seen in **Figures 3a and 3b**. In terms of maturity, the longest-dated corporate bonds were those of Temasek, with tenors of about 40 and 25 years. In terms of size, the largest single issue was that of United Overseas Bank, with an SGD1.3 billion bond. This was followed by three bond issues from property developer Capitaland, two of which amounted to SGD1.2 billion each, while the third had an issue size of SGD1.1 billion.

**Table 2: Bonds Outstanding of Top 30 Corporate Issuers, September 2010**

| Issuer | Outstanding Amount LCY Bonds (SGD billion) |
|---|---|
| Housing and Development Board (Public Housing Authority) | 5.65 |
| Capitaland (Real Estate) | 4.87 |
| United Overseas Bank (Banking) | 3.62 |
| Temasek Financial I (Investment Company) | 3.60 |
| SP Power Assets (Electricity Transmission and Distribution) | 3.01 |
| Public Utilities Board (National Water Authority) | 2.50 |
| Oversea-Chinese Banking (Banking) | 2.20 |
| Land Transport Authority (Building and Construction) | 1.88 |
| Singapore Airlines (Airlines) | 1.70 |
| DBS Bank Singapore (Banking) | 1.61 |
| F&N Treasury (Food Service, Property, Pub & Printing) | 1.32 |
| City Developments (Hotels and Motels) | 1.10 |
| Capitaland Treasury (Real Estate) | 1.05 |
| PSA Corp. (Container Transshipment Hub) | 1.00 |
| Keppel Land (Real Estate) | 0.74 |
| Sembcorp Financial Services (Engineering/R&D Services) | 0.70 |
| Capitamall Trust (REITS-Shopping Centers) | 0.65 |
| Singapore Press Holdings (Publishing-Newspapers) | 0.60 |
| Singtel Group Treasury (Telecoms) | 0.60 |
| Mapletree Treasury Services (Special Purpose Entity) | 0.53 |
| Ascott Capital (Real Estate) | 0.50 |
| CMT MTN Pte Ltd | 0.50 |
| Singapore Post (Postal Services) | 0.50 |
| ST Treasury Services (Finance) | 0.48 |
| Yanlord Land Group (Real Estate, PRC-based) | 0.42 |
| Hotel Properties (Hotels and Motels) | 0.41 |
| Capitacommercial Trust (REITS-Diversified) | 0.41 |
| HK Land Treasury Service (Property Investment Management) | 0.38 |
| Asia Pacific Breweries (Breweries) | 0.36 |
| Guocoland (Property Development and Investment) | 0.35 |
| **Total Top 30 Corporate Issuers** | **43.23** |
| **Total Corporate Bonds Outstanding** | **104.70** |
| **Top 30 as % of Total Corporate** | **41.3%** |

PRC = People's Republic of China, Pub & Printing = publishing and printing, R&D = research and development, REITS real estate investment trusts.
Note: Total corporate bonds outstanding based on *AsianBondsOnline* estimates.
Source: Bloomberg LP.

**Figure 3a: Top 30 LCY Corporate Bonds by Maturity** (years)

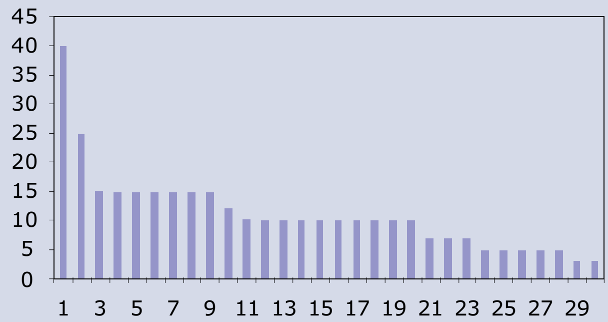
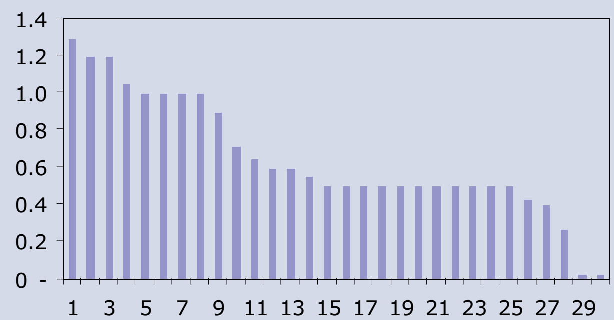



**Figure 3b: Top 30 LCY Corporate Bonds by Size** (SGD billion)



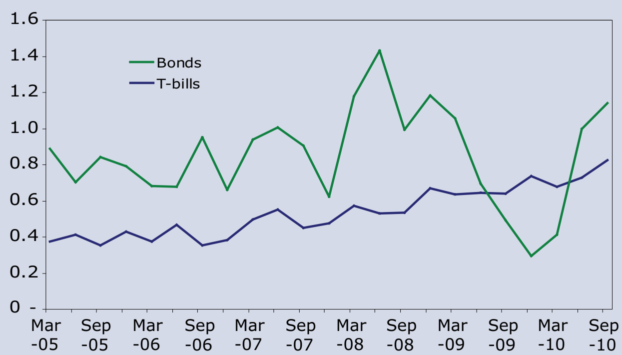

LCY = local currency.
Source: Bloomberg LP and *AsianBondsOnline*

Other large bond issues included those of Temasek (two SGD1.0 billion bonds), Singapore Airlines (SGD0.9 billion), and Oversea-Chinese Banking (SGD0.7 billion).

## Turnover Ratios

The third quarter of the year saw increased liquidity for both SGS bonds and bills, as indicated by rising turnover ratios. In 3Q10, the turnover ratio for bonds was 1.14, compared with 1.00 in the previous quarter, while the turnover ratio for treasury bills stood at 0.83, compared with 0.73 in the previous quarter. The turnover ratio for treasury bills has been on a broad, upward trend since 2005, while the turnover ratio for bonds has been on an uptick since March 2010 after falling off from peaks reached in 2008 **(Figure 4)**. This trend reflects a combination of large inflows of foreign capital and the consolidation of issue size for SGS bonds over the last several years, which has made them more attractive to investors.

**Figure 4: Quarterly Turnover Ratio Trends for Singapore Treasury Bonds and Bills**




T-bills = treasury bills.
Source: Monetary Authority of Singapore.

## Rating Changes

In August, Standard & Poor's (S&P) affirmed Singapore's long-term and short-term sovereign credit ratings at AAA and A-1+, respectively, with a stable outlook **(Table 3)**. S&P said that the ratings were supported by Singapore's "extensive fiscal and external strengths" and "solid record of prudent macroeconomic management." In particular, S&P cited Singapore's significant foreign exchange reserves and sound fiscal position, which allowed the government to introduce a SGD20.5 billion stimulus package in 2009 in response to the global financial crisis. According to S&P, the package helped the economy weather the crisis as the economy contracted at a slower rate than it would have absent a stimulus package.

**Table 3: Selected Sovereign Ratings and Outlook for Singapore**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | Aaa | AAA | AAA |
| Outlook | stable | stable | stable |

FCY = foreign currency, LT = long-term.
Source: Ratings agencies.

## Policy, Institutional, and Regulatory Developments

### PBOC and MAS Agree to a Bilateral Currency Swap

On 23 July, the People's Bank of China (PBOC) and MAS agreed to a bilateral currency swap arrangement to promote bilateral trade and direct investment. The swap arrangement will provide yuan liquidity of up to CNY150 billion and Singapore dollar liquidity of up to SGD30 billion. The initial term of the arrangement is 3 years with the possibility for extension.

### Singapore Exchange Launches Initiatives to Boost Bond Listing and Trading

In August, the Singapore Exchange (SGX) launched initiatives to promote the listing, trading, and distribution of fixed-income instruments in Singapore. Among the initiatives are measures to attract companies listed in Singapore to issue bonds that can be listed and traded on the SGX, which, in turn, plans to streamline the approval process for bond listings and cut the time required for approval in half.

In addition to attracting bond listings, SGX plans to encourage the listing and trading of preference shares and convertible bonds. By 1Q11, SGX expects to put in place an on-exchange secondary market allowing for the trading of SGS both by individual and institutional investors.

## SGX to launch ADRs

In October, SGX launched American Depository Receipts (ADRs) on its GlobalQuote platform (SGX's quotation board for international securities). SGX-quoted ADRs will enable investors to trade shares of 19 major Asian companies, including Baidu and Suntech Power Holdings, which do not have Asian home exchanges. The availability of Asian ADRs will enable investors to trade the shares of all of these companies during Asian trading hours. The launch also marks cooperation between SGX and NASDAQ OMX to bring ADR quotations on GlobalQuote, thereby linking up market participants on both trading pools. The Bank of New York acts as the depository bank for this new ADR program.

# Thailand—Update

## Yield Movements

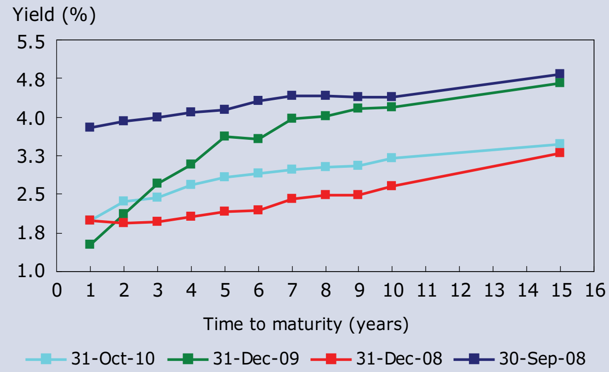
Thai government bond yields fell for most maturities between end-December 2009 and end-October 2010 **(Figure 1)**. Yields for 1- and 2-year maturities rose 46 and 25 basis points, respectively, while yields fell for all other maturities, resulting in a flattening of the curve. Specifically, yields for 3- and 4-year bonds declined 28 and 39 basis points, respectively. Yields fell by more than 100 basis points along the rest of the curve, with the 15-year tenor declining the most (120 basis points). The yield spread between 2- and 10-year maturities narrowed to 84 basis points in end-October from a spread of 207 basis points at end-December.

The flattening of the yield curve reflected increased foreign investor demand in Thai bonds, which prompted the Thai government to take stronger measures to tame appreciation of the baht. The Thai government's recent moves include imposing a 15% withholding tax on foreign investors and relaxing regulations on foreign exchange transactions. Meanwhile, the Bank of Thailand (BOT) held its 1-day repurchase rate at 1.75% on 20 October, while raising concerns over a faltering global recovery. The BOT declined to increase rates further in October after two consecutive monthly rate hikes in July and August.

Thailand's consumer price inflation slowed for the third straight month in October to 2.8% year-on-year (y-o-y), from 3.0% and 3.3% in September and August, respectively. Government subsidies helped contain price pressures, but floods in October seem to have caused a modest increase in food prices. The BOT projects inflation to fall within 2.5%–3.8% in 2010 and 2.5%–4.5% in 2011.

Thailand's gross domestic product (GDP) slowed to 6.7% y-o-y in 3Q10, after expanding 9.1% y-o-y in 2Q10. Growth in the Thai economy is expected to drop further in 4Q10 due to the strengthening baht, fluctuating oil prices, and the impact of flooding on agricultural output. Thailand's GDP is expected to grow 7.3%–8.0% in 2010, according to BOT, and 3.0%–5.0% in 2011.

**Figure 1: Thailand's Benchmark Yield Curve—LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

## Size and Composition

The size of Thailand's total local currency (LCY) bond market expanded 14.2% y-o-y to reach THB6.6 trillion (USD217 billion) in 3Q10, lower than the 18.4% y-o-y growth recorded in 2Q10 **(Table 1)**. Total LCY bonds outstanding rose 2.5% quarter-on-quarter (q-o-q) and 1.1% month-on-month (m-o-m).

The outstanding stock of government bonds was up 17.3% y-o-y at end-September for a total of THB5.3 trillion (USD176 billion). BOT bonds had the highest growth rate among all categories of government bonds at 36.3% y-o-y for a total of THB2.3 trillion, followed by treasury bonds, which posted growth of 9.1% y-o-y to reach a total of THB2.6 trillion. State-owned enterprise and other bonds, however, declined 5.2% y-o-y to THB503.0 billion.

Central government bonds retained a dominant share of total bonds outstanding (49% as of end-September) as the central government continued to issue 28-, 91-, and 182-day treasury bills. The government also issued 3-, 4-, 5-, 7-, and

**Table 1: Size and Composition of the LCY Bond Market in Thailand**

| | **Amount** (billion) | | | | | | | | **Growth Rate** (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Jun-10** | | **Jul-10** | | **Aug-10** | | **Sep-10** | | **Jun-10** | | **Jul-10** | **Aug-10** | **Sep-10** | | |
| | **THB** | **USD** | **THB** | **USD** | **THB** | **USD** | **THB** | **USD** | **y-o-y** | **q-o-q** | **m-o-m** | **m-o-m** | **y-o-y** | **q-o-q** | **m-o-m** |
| Total | 6,419.0 | 198.0 | 6,499.7 | 201.5 | 6,506.0 | 208.1 | 6,576.6 | 216.8 | 18.4 | 3.9 | 1.3 | 0.1 | 14.2 | 2.5 | 1.1 |
| Government | 5,177.5 | 159.7 | 5,256.2 | 162.9 | 5,274.5 | 168.7 | 5,349.8 | 176.4 | 21.0 | 4.3 | 1.5 | 0.3 | 17.3 | 3.3 | 1.4 |
| Treasury Bonds | 2,566.7 | 79.2 | 2,593.9 | 80.4 | 2,567.7 | 82.1 | 2,596.7 | 85.6 | 14.5 | 3.9 | 1.1 | (1.0) | 9.1 | 1.2 | 1.1 |
| Central Bank Bonds | 2,096.8 | 64.7 | 2,151.2 | 66.7 | 2,196.8 | 70.3 | 2,250.2 | 74.2 | 37.8 | 6.3 | 2.6 | 2.1 | 36.3 | 7.3 | 2.4 |
| State-Owned Enterprise & Other Bonds | 514.0 | 15.9 | 511.2 | 15.8 | 510.0 | 16.3 | 502.9 | 16.6 | (0.4) | (1.3) | (0.6) | (0.2) | (5.2) | (2.2) | (1.4) |
| Corporate | 1,241.4 | 38.3 | 1,243.5 | 38.5 | 1,231.5 | 39.4 | 1,226.8 | 40.4 | 9.0 | 2.3 | 0.2 | (1.0) | 2.6 | (1.2) | (0.4) |

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY—USD rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.
Source: Bank of Thailand and Bloomberg LP.

12-year loan and savings bonds in 3Q10. In July, THB3.5 million in 3-year savings bonds were issued for sale to retail investors.

Since July, the Thai government has issued THB57.0 billion of loan bonds to finance the budget deficit. The expected budget deficit for fiscal year 2010 (ending 30 September) narrowed to 3.8% of GDP, compared with 4.3% in fiscal year 2009.

New issuance of government bonds in 3Q10 reached THB2.8 trillion, with BOT accounting for 90% of the total. State-owned enterprises such as Government Housing Bank, Bangkok Mass Transit Authority, State Railway of Thailand, and Provincial Waterworks Authority issued THB14.2 billion in bonds, with maturities ranging between 5 and 15 years.

Meanwhile, the Thai government is planning to issue the longest-dated security ever in Thailand—a 50-year government bond. The bond issue will likely take place in 1Q11 and will be targeted to institutional investors. Proceeds will help cover the budget deficit and a portion will be used to refinance existing government debt. Currently, the longest-dated bond issued in Thailand is the 30-year government bond.

Corporate bonds outstanding stood at THB1.2 trillion (USD40.4 billion) as of end-September, up 2.6% y-o-y. Total corporate bonds outstanding declined on both a q-o-q and m-o-m basis by 1.2% and 0.4%, respectively. New issuance in 3Q10 reached THB224.0 billion, which represented declines of 8.9% y-o-y and 18.5% q-o-q. Notable THB-denominated corporate bond issues for the quarter included Toyota Leasing's THB4.0 billion of 3-year bonds and Mahboonkrong's THB3.0 billion of 3-year bonds.

In August, the Thai Finance Ministry granted approval to three firms from the Republic of Korea to issue a total of THB14.0 billion of bonds in the Thai market before the end of 2010. Industrial Bank of Korea and Korea Development Bank have each been granted permission to issue

THB5.0 billion, while Korea Water Resources Corp. has been approved to issue THB4.0 billion.

In October, the Finance Ministry approved three more foreign entities to issue THB-denominated bonds before 31 March 2011. Central American Bank for Economic Integration (CABEI), ING Bank, and the Export–Import Bank of Korea (KEXIM) have been approved to issue bonds of THB4.0 million, THB10.0 million, and THB8.0 million, respectively. Also in October, Thailand's second-largest property developer Pruksa Real Estate sold a total of THB5.0 billion of 3- and 5-year bonds.

The following corporations have bond issues in the pipeline for 4Q10:

(i) Thailand's largest energy firm PTT will sell THB20.0 billion worth of bonds.

(ii) Leading coal miner Banpu PCL plans to raise up to THB20.0 billion to purchase Australia's Centennial Coal.

(iii) PTT Chemical plans to raise THB3.0 billion to repay project investments.

The top 30 corporate issuers in Thailand at end-September were mainly from the industrial and financial sectors, and together represented 75% of total LCY corporate bonds outstanding **(Table 2)**. PTT PCL ranked first as the top LCY and foreign currency (FCY) corporate issuer, with total bonds outstanding of THB179.2 billion and USD1.2 billion, respectively.

In July, PTT Exploration and Production became the first Thai issuer to sell bonds in the international market in 3 years. The firm issued USD500 million worth of 5-year bonds with a coupon of 4.152%. Asian investors bought 69% of the bonds, Europeans took 11%, and offshore investors from the United States (US) purchased 20%. Prior to July, the last Thai corporate bond issuance in the international market—USD350 million worth of 7-year bonds—was conducted by True Move in July 2007.

**Table 2: Top 30 Corporate Issuer, September 2010**

| Top 30 Corporate Issuers | Outstanding Amount | | |
|---|---|---|---|
| | LCY Bonds (THB billion) | LCY Bonds (USD billion) | FCY Bonds (USD billion) |
| PTT PCL | 179.2 | 5.9 | 1.2 |
| Siam Cement PCL | 110.0 | 3.6 | — |
| Bank Ayudhya Public Ltd | 63.2 | 2.1 | — |
| Krung Thai Bank PCL | 53.4 | 1.8 | 0.2 |
| PTT Exporation and Product PCL | 49.0 | 1.6 | 0.5 |
| Thai Airways International PCL | 36.8 | 1.2 | — |
| Toyota Leasing Thailand | 29.5 | 1.0 | — |
| Charoen Pokphand Foods | 26.2 | 0.9 | — |
| Kasikorn Bank PCL | 25.1 | 0.8 | 0.2 |
| Dad SPV Company Ltd | 24.0 | 0.8 | — |
| Thai Oil PCL | 20.8 | 0.7 | 0.4 |
| PTT Chemical PCL | 40.2 | 1.3 | 0.3 |
| Siam Commercial Bank Co | 20.0 | 0.7 | |
| Krung Thai Card PCL | 19.5 | 0.6 | — |
| Advanced Info Service | 19.5 | 0.6 | — |
| Thanachart Bank PCL | 18.0 | 0.6 | — |
| TMB Bank PCL | 17.3 | 0.6 | 0.02 |
| Bangkok Expressway PCL | 15.1 | 0.5 | — |
| Glow Energy PCL | 15.0 | 0.5 | — |
| PTT Aromatics and Refining | 15.0 | 0.5 | — |
| Quality Houses Public Co | 15.0 | 0.5 | — |
| Ayudhya Capital Auto Lease | 14.7 | 0.5 | — |
| True Corporation PCL | 13.8 | 0.5 | — |
| Thanachart Capital PCL | 13.5 | 0.4 | — |
| Bangkok Mass Transit System | 12.0 | 0.4 | — |
| Kiatnakin Bank PCL | 11.9 | 0.4 | — |
| Central Pattana Public | 11.7 | 0.4 | — |
| Land & Houses Public Co | 11.0 | 0.4 | — |
| Minor International PCL | 10.4 | 0.3 | — |
| Siam City Bank PCL | 10.0 | 0.3 | — |
| **Total Top 30 Corporate Issuers** | **920.8** | **30.4** | **2.7** |
| **Total Corporate Bonds Outstanding** | **1,231.5** | **40.6** | |
| **Top 30 as % of Total Corporate** | **75%** | **75%** | |

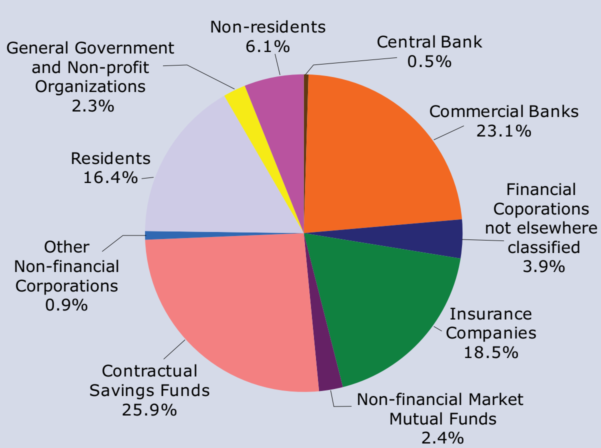
— = not applicable, FCY = foreign currency, LCY = local currency.
Source: Bloomberg LP.

## Investor Profile

At the end of September, contractual savings funds were the largest holder of Thai government bonds with a total amount of THB671.8 billion and a share of 26.0% **(Figure 2)**. Commercial banks were the second largest holder of government bonds with a 23.1% share, followed by insurance companies (18.5%), residents (16.4%), and non-residents (6.1%). Financial corporations "not elsewhere classified" held 3.9% of all Thai government bonds, non-financial market mutual funds had 2.4%, and general government and non-profit organizations had a 2.3% share. Finally, other non-financial corporations held a 0.9% share while the central bank had a 0.5% share.

Foreign holdings of Thai government bonds stood at THB157.5 billion at the end of September, an increase of about 45% since the end of June. Foreign investors increasingly sought safe haven in Thai bonds as low returns in the developed world are pushing many Asian currencies higher. As a result of foreign fund inflows, the Thai baht strengthened to a 13-year high of 30.33 against the US dollar at the end of September.

**Figure 2: LCY Government Bonds Investor Profile, September 2010**




LCY = local currency.
Source: Bank of Thailand.

In response, the BOT relaxed foreign exchange regulations on 5 October and has imposed a 15% tax on interest and capital gains earned by foreign investors from Thai bonds.

## Rating Changes

On 28 October, Moody's upgraded the outlook for Thailand's long-term FCY and LCY government bond ratings to stable from negative **(Table 3)**. According to Moody's, the decision for the outlook change was based on Thailand's "robust economic recovery" and the "stabilization of government finances despite continuing domestic political turmoil."

**Table 3: Selected Sovereign Ratings and Outlook for Thailand**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | Baa1 | BBB+ | BBB |
| Outlook | stable | negative | stable |

FCY = foreign currency, LT = long term.
Source: Rating Agencies.

## Policy, Institutional, and Regulatory Developments

### Finance Ministry Relaxes Capital Outflow Controls

In September, the Finance Ministry of Thailand announced regulatory changes to promote foreign investment and capital outflows in an effort to slow the appreciation of the baht, which has gained about 8% against the US dollar year-to-date due to capital inflows and a steady trade surplus. The five new regulatory measures include (i) allowing Thai firms to invest and lend without limit to affiliate companies abroad; (ii) allowing Thai firms to lend up to USD50 million per year to non-affiliated companies abroad; (iii) increasing the foreign property investment cap from USD5 million to USD10 million; (iv) increasing the maximum FCY deposits held by Thai individuals and companies from USD100,000 and USD300,000, respectively, to USD500,000 for both; and (v) increasing mandatory repatriation of export earnings from USD20,000 to USD50,000.

### Thai Cabinet Approves a 15% Tax on Bonds

The Thai government has approved the imposition of a 15% tax on interest and capital gains earned by foreign investors from Thai bonds in an effort to slow foreign currency inflows and ease the baht's appreciation. Effective 13 October, foreign investors trading government, central bank, or state enterprise bonds were required to pay a withholding tax of 15%. Meanwhile, the Customs Department is considering waiving import tariffs on machinery that cannot be produced in Thailand as the government wants to help exporters and small and medium-sized enterprises (SMEs) improve their productivity. State banks—Krung Thai Bank, Small and Medium Enterprise Development Bank of Thailand, Islamic Bank of Thailand, and Export–Import Bank of Thailand—are offering forward contracts to protect SMEs against volatility in the exchange rate. The Government Savings Bank provides SMEs a credit line of up to THB5.0 billion. Also, the Revenue Department is planning to offer local companies additional tax breaks for asset depreciation. According to the Ministry of Finance, about 10,000 SMEs need assistance as a result of the baht's recent appreciation.

### BOT Relaxes Regulations on Foreign Exchange Transactions

The BOT issued measures relaxing foreign exchange regulations to increase the flexibility of Thai businesses in managing foreign exchange risks. Effective 12 October, Thai exporters were permitted to transfer FCY deposits to counterparties in Thailand for payment of goods and services, with the limit on foreign exchange transactions being increased to USD50,000 from USD20,000. Also, Thai businesses undertaking direct investment or lending abroad of USD10 million or more per year are now required to notify the BOT.

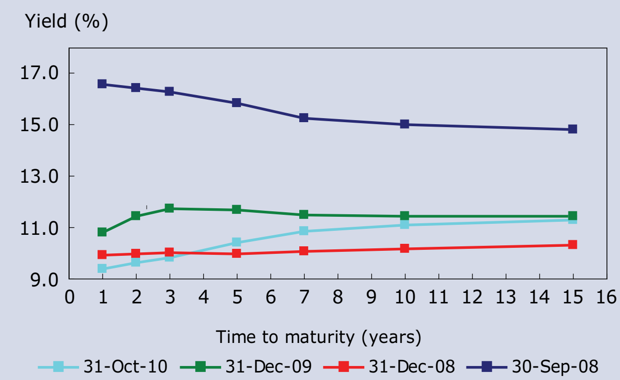
# Viet Nam—Update

## Yield Movements

Vietnamese government bond yields fell for all maturities between end-December 2009 and end-October 2010 **(Figure 1)**. Yields at the short-end of the curve fell by over 100 basis points more than yields along the rest of the curve, resulting in a modest steepening. Yields fell the most for the 3-year tenor, dropping 187 basis points, while yields for 7-, 10-, and 15-year bonds declined by 66, 37, and 13 basis points, respectively. The yield spread between 2- and 10-year maturities widened to 144 basis points at end-October from a spread of –2 basis points at end-December.

The decline in government bond yields at the short-end of the curve reflected the fact that the State Bank of Viet Nam (SBV) has kept its base interest rate unchanged at 8.0% since December 2009 as it strives to boost bank lending. However, on 5 November, SBV decided to increase the base interest rate by 100 basis points to 9.0%. This followed its recent decision on 27 October to maintain the policy rate at 8.0% for the twelfth consecutive month. The SBV also raised other interest rates such as the discount rate and the refinancing rate by 100 basis points each to 7.0% and 9.0%, respectively. The much smaller decline in yields at the longer-end of the curve reflects concerns over rising inflation.

**Figure 1: Viet Nam's Benchmark Yield Curve–LCY Government Bonds**




LCY = local currency.
Source: Bloomberg LP.

Consumer price inflation rose to 9.7% year-on-year (y-o-y) in October, compared with 8.9% y-o-y in September, as a result of continued hikes in food prices and education services. The General Statistics Office of Viet Nam has taken the view that inflation will continue to fluctuate in the remaining months of 2010 due to increases in essential commodity prices, a continuous depreciation of the Vietnamese dong against the United States (US) dollar, and price hikes for industrial inputs and imported products.

Viet Nam's gross domestic product (GDP) grew 6.5% y-o-y in 3Q10 as the industry/construction sector and the services sector grew 7.3% and 7.2%, respectively. Viet Nam's economy expanded 6.4% y-o-y in 2Q10. GDP is expected to expand 6.7% for all of 2010, compared with 5.3% annual growth in 2009.

## Size and Composition

Viet Nam's total local currency (LCY) bonds outstanding grew 27.4% y-o-y to reach VND290 trillion (USD14.9 billion) as of end-September 2010 **(Table 1)**. Total LCY bonds outstanding declined on both a quarter-on-quarter (q-o-q) and month-on-month (m-o-m) basis by 1.0% and 1.8%, respectively. The LCY bond market q-o-q growth rate soared to 29% in 2Q10, following growth of only 2.3% in 1Q10 and similarly-low, single-digit growth for most of 2009. Meanwhile, the corporate bond market grew very rapidly in 2009 and 1H10 before contracting by 6.1% on a q-o-q basis in 3Q10.

Total VND-denominated government bonds outstanding stood at VND265 trillion as of end-September, rising 25.5% y-o-y, while falling 0.5% q-o-q. The quarterly decline in government bonds was due to a 1.6% drop in outstanding

**Table 1: Size and Composition of the LCY Bond Market in Viet Nam**

| | Amount (billion) | | | | | | | | Growth Rate (%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Jun-10 | | Jul-10 | | Aug-10 | | Sep-10 | | Jun-10 | | Jul-10 | Aug-10 | Sep-10 | | |
| | VND | USD | VND | USD | VND | USD | VND | USD | y-o-y | q-o-q | m-o-m | m-o-m | y-o-y | q-o-q | m-o-m |
| Total | 293,569.2 | 15.4 | 297,789.2 | 15.6 | 295,751.6 | 15.2 | 290,489.6 | 14.9 | 35.8 | 29.0 | 1.4 | (0.7) | 27.4 | (1.0) | (1.8) |
| Government | 266,629.3 | 14.0 | 269,799.3 | 14.1 | 266,901.3 | 13.7 | 265,199.3 | 13.6 | 29.8 | 30.1 | 1.2 | (1.1) | 25.5 | (0.5) | (0.6) |
| Treasury Bonds | 120,390.2 | 6.3 | 123,890.2 | 6.5 | 120,045.2 | 6.2 | 118,490.2 | 6.1 | 15.9 | 30.2 | 2.9 | (3.1) | 16.0 | (1.6) | (1.3) |
| Central Bank Bonds | 200.0 | 0.0 | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Viet Nam Development Bank Bonds, State-Owned Enterprise Bonds and Other Bonds | 146,039.1 | 7.7 | 145,909.1 | 7.6 | 146,856.1 | 7.5 | 146,709.1 | 7.5 | 43.7 | 30.0 | (0.1) | 0.6 | 36.6 | 0.5 | (0.1) |
| Corporate | 26,939.9 | 1.4 | 27,989.9 | 1.5 | 28,850.3 | 1.5 | 25,290.3 | 1.3 | 152.2 | 19.3 | 3.9 | 3.1 | 51.9 | (6.1) | (12.3) |

— = not applicable, LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.

Notes:

1. Bloomberg LP end-of-period LCY—USD rates are used.
2. Growth rates are calculated from LCY base and do not include currency effects.

Source: Bloomberg LP.

treasury bonds in 3Q10. Viet Nam Development Bank bonds and state-owned enterprise bonds increased 0.5% q-o-q, while all outstanding central bank bonds matured in 3Q10.

Government bond issuance in 3Q10 included a total of VND5.7 trillion of long-term treasury bonds, and VND1.0 trillion of 3-year senior unsecured bonds issued by state-owned Viet Nam National Shipping Lines. Total government bond issuance in 3Q10 was only 10% of total 2Q10 issuance. The Vietnamese government has been issuing to repay maturing bonds and to cover the budget deficit, which is expected to reach 6.0% of GDP this year. State-owned Viet Nam Electricity submitted a proposal to the government to issue USD1.0 billion of government-guaranteed bonds in the international market by early 2011. Proceeds of the bonds would be used to upgrade Viet Nam's power generation capacity.

Total corporate bonds outstanding in 3Q10 increased 51.9% y-o-y to VND25.3 trillion. On a q-o-q basis, however, VND-denominated corporate bonds outstanding declined by 6.1%. Total corporate bond issuance only totaled VND2.0 trillion in 3Q10, after reaching VND5.9 trillion in 2Q10. Top issuers for the quarter included Refrigeration Electrical Engineering (VND810 billion) and Hoa Phat Group JSC (VND 800 billion).

As of end-September, the top 10 corporate issuers in Viet Nam comprised 91% of total corporate bonds outstanding, or VND23.1 trillion **(Table 2)**. The majority of LCY corporate issuers were from the financial sector. Vietnamese property developer Vincom JSC (formerly the Viet Nam General Commercial Joint Stock Company) ranked first with total bonds outstanding of VND5.0 trillion, followed by Techcombank (VND3.9 trillion) and Asia Commercial Joint Stock Bank (VND3.6 trillion). Vincom JSC (USD80 million) is the only major Vietnamese corporation that has issued a foreign currency (FCY) bond to date. Vincom JSC successfully issued its first offshore convertible bonds worth USD100 million in December 2009. The 5-year bonds, which are listed on the Singapore Exchange, are convertible to equity at

**Table 2: Top 10 Corporate Issuers, September 2010**

| Corporate Issuers | Outstanding Amount | | |
|---|---|---|---|
| | LCY Bonds (VND billion) | LCY Bonds (USD billion) | FCY Bonds (USD billion) |
| Vincom JSC | 5,000 | 0.26 | 0.08 |
| Techcombank | 3,850 | 0.20 | — |
| Asia Commercial Joint Stock Bank | 3,600 | 0.18 | — |
| Vietnam JSC Commercial Bank | 3,000 | 0.15 | — |
| Saigon Securities Inc | 2,000 | 0.10 | — |
| Saigon Thuong Tin Commercial | 2,000 | 0.10 | — |
| Military Commercial Bank | 1,000 | 0.05 | — |
| Vinpearlland Tourism JSC | 1,000 | 0.05 | — |
| Refrigeration Electrical Engineering | 810 | 0.04 | — |
| Hoa Phat Group JSC | 800 | 0.04 | — |
| **Total Top 10 Corporate Issuers** | **23,060** | **1.18** | |
| **Total Corporate Bonds Outstanding** | **25,290** | **1.30** | |
| **Top 10 as % of Total Corporate** | **91%** | **91%** | |

— = not applicable, FCY = foreign currency, JSC = joint-stock company, LCY = local currency.
Source: Bloomberg LP

a 5.0% premium. Proceeds of the issuance will be used for development projects in Hanoi.

## Rating Changes

In July, Fitch Ratings announced that it had downgraded both its long-term FCY and LCY issuer default ratings for Viet Nam to B+ from BB- **(Table 3)**. Fitch placed Viet Nam on a stable outlook, replacing the negative outlook announced in March 2010. Fitch also downgraded Viet Nam's country ceiling from BB- to B+, and affirmed its short-term FCY issuer default rating of B.

**Table 3: Selected Sovereign Ratings and Outlook for Viet Nam**

| | Moody's | S&P | Fitch |
|---|---|---|---|
| Sovereign FCY LT Ratings | Ba3 | BB | B+ |
| Outlook | negative | negative | stable |

FCY = foreign currency and LT = long term.
Source: Rating agencies.

## Policy, Institutional, and Regulatory Developments

### Limited Liability Companies To Issue Bonds

In July, the Ministry of Finance issued a draft decree that allows limited liability companies to issue corporate bonds in domestic and international capital markets. The draft decree identifies which limited liability companies are allowed to issue bonds and provides a legal framework to enterprises on international bond issuance.

### Fees on Corporate Bonds To Be Cut by 50%

In August, the prime minister's working group proposed that the Ministry of Finance reduce corporate bond issuance acceptance fees by 50% in an effort to harmonize them with fees on other licenses such as investment registration and construction. The proposed changes would adjust fees to the following levels: (i) VND5.0 million for bond issues of less than VND50 billion, (ii) VND10.0 million for issues of less than VND150 billion, (iii) VND17.5 million for issues of less than VND250 billion, and (iv) VND25.0 million for issues larger than VND250 billion.

### Viet Nam's Central Bank to Revise Bank Legal Capital Road map

In August, the SBV's governor signed Decision No. 2020/QD-NHNN forming a draft commission to prepare, revise, and edit Decree No. 141/2006/ND-CP, which promulgates minimum chartered capital and the accompanying timelines for local banks. The proposal seeks to set minimum legal capital for commercial banks at VND3 trillion by the end of 2010, VND5 trillion by the end of 2012, and VND10 trillion by the end of 2015. Currently, Viet Nam has nine commercial banks with over VND3 trillion in chartered capital, while 30 banks have less than VND3 trillion.