

Market Summaries

People's Republic of China—Update

Yield Movements

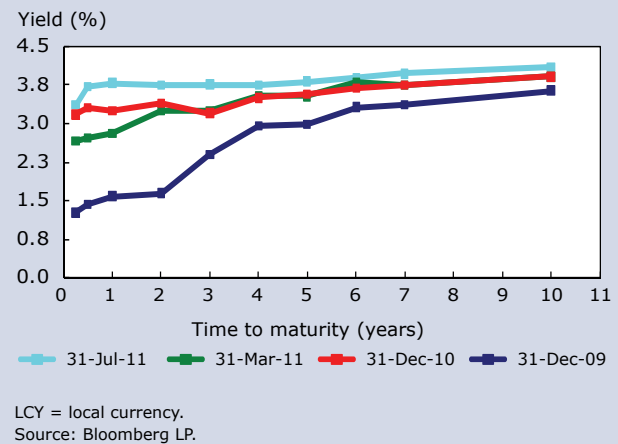
The People's Republic of China's (PRC) government bond yield curve flattened between end-March and end-July as a result of continued monetary tightening (**Figure 1**). Yields rose between 71 basis points (bps) and 99 bps on tenors of less than 1 year; yields in the belly of the curve rose between 10 bps to 49 bps; and yields on the 7- and 10-year tenors rose 22 bps and 18 bps, respectively.

Due to the much larger increase in short-term yields versus longer-term yields, the spread between 2- and 10-year government bonds narrowed to 34 bps at end-July from 51 bps at end-December 2010. The result was a yield curve at end-July that was significantly flatter than the yield curve at end-March when the spread was 65 bps.

Recent market volatility and changes in the yield curve, particularly at the short-end of the curve, are a response to efforts by the PRC to slow inflation and credit growth. The People's Bank of China (PBOC) has hiked the reserve requirement ratio six times—by 50 bps each time—since January. The PRC has also hiked its benchmark interest rates three times since January, bringing the 1-year lending rate to 6.56% and the 1-year deposit rate to 3.50%. Meanwhile, inflation reached a 37-month high in July of 6.4% year-on-year (y-o-y).

Concerns over the PRC's credit growth remain. S&P recently downgraded the outlook of Chinese property companies to negative. It was also reported that local government debt stands at CNY10.7 trillion (US\$1.66 trillion). The PRC's tightening has had some effect, with the M2 money supply growing 15.1% y-o-y in May, down from 15.3% growth in April and 17.2% in January. However, M2 money supply growth accelerated again in June to 15.9%.

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



The Purchasing Managers' Index (PMI) for manufacturing fell to 50.1 in May, the lowest level in 11 months. Gross domestic product (GDP) growth in 2Q11 was also down slightly to 9.5% y-o-y from 9.7% in 1Q11. Despite the monetary tightening, new loans in June amounted to a higher-than-forecast CNY633.9 billion.

Size and Composition

The amount of outstanding local currency (LCY) bonds in the PRC market reached CNY20.6 trillion (US\$3.19 trillion) at end-June, representing a y-o-y increase of 6.7% and a quarter-on-quarter (q-o-q) rise of 2.7% (**Table 1**).

Corporate Bonds

With the exception of asset- and mortgage-backed securities, key sectors of the corporate bond market grew by double digits in 2Q11. Medium-term notes (MTNs) grew 40.8% y-o-y, while commercial paper and local corporate bonds posted y-o-y

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

	Amount (billion)						Growth Rates (%)					
	Mar-11		Apr-11		May-11		Mar-11		Apr-11		May-11	
	CNY	US\$	CNY	US\$	CNY	US\$	Y-o-Y	Q-o-Q	M-o-M	Y-o-Y	Q-o-Q	M-o-M
Total	20,078	3,066	20,244	3,118	20,458	3,158	11.1	(0.5)	0.8	11.1	1.1	0.8
Government	15,518	2,370	15,617	2,405	15,736	2,429	5.4	(2.5)	0.6	5.4	0.8	0.2
Treasury Bonds	6,667	1,018	6,735	1,037	6,829	1,054	16.6	0.1	1.0	16.6	1.4	1.7
Central Bank Bonds	3,179	485	3,002	462	2,974	459	(27.4)	(22.2)	(5.6)	(0.9)	(0.9)	(6.4)
Policy Bank Bonds	5,672	866	5,880	906	5,933	916	22.7	9.9	3.7	25.9	6.6	1.9
Corporate	4,560	696	4,627	713	4,722	729	35.9	7.0	1.5	30.8	6.3	2.6
Policy Bank Bonds												
China Development Bank	4,075	622	4,185	645	4,225	652	21.6	10.7	2.7	23.8	5.2	1.4
Export-Import Bank of China	608	93	648	100	660	102	37.0	9.9	6.6	42.3	12.6	3.7
Agricultural Devt. Bank of China	990	151	1,048	161	1,048	162	19.3	6.8	5.8	25.6	8.7	2.7

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-US\$ rate is used.

4. Growth rates are calculated from LCY base and do not include currency effects.

Source: ChinaBond and Bloomberg LP.

growth rates of 11.7% and 54.7%, respectively. State-owned corporate bonds (SOE bonds) grew 12.3% y-o-y and commercial bank bonds grew 24.7%. In contrast, the amount of asset- and mortgage-backed securities outstanding has been on a steady decline for several years, with no new issuance since 4Q08.

On a q-o-q basis, growth slowed in all sectors in 2Q11 with the exception of asset-backed securities, which continued to decline in 2Q11, albeit at a much slower rate. Commercial bank bonds saw a noticeable uptick in growth to become the fastest growing segment of the corporate bond sector in 2Q11. SOE bonds declined 0.3% in 2Q11, after remaining unchanged in 1Q11 (**Table 2**). Local corporate bonds expanded 9.3% in 2Q11, following 14.7% growth in 1Q11. Growth of MTNs slowed to 5.8% in 2Q11 from 13.2% in 1Q11. Commercial paper outstanding declined 0.6% in 2Q11 compared with positive growth of 4.6% in 1Q11.

MTNs consistently enjoyed double-digit q-o-q growth rates for several quarters prior to 4Q10, reflecting continued strong corporate sector demand and improved investor access to MTNs due to the relatively quick issuance approval processes. The MTN market's slower growth rate in 2Q11 likely reflects the PBOC's tightening of monetary policy in recent months and the prospect of rising interest rates in the near-term.

Issuance of corporate bonds slowed in 2Q11 from 1Q11 (**Figure 2**), with the exception of commercial bank bonds, which experienced a massive surge as issuance climbed to CNY144.0 billion from CNY19.5 billion. The rise in commercial bank bond issuance was driven mostly by increases in subordinated debt issuance as the China Banking Regulatory Commission (CBRC) has issued new capital adequacy requirements that will take effect starting in 2012.

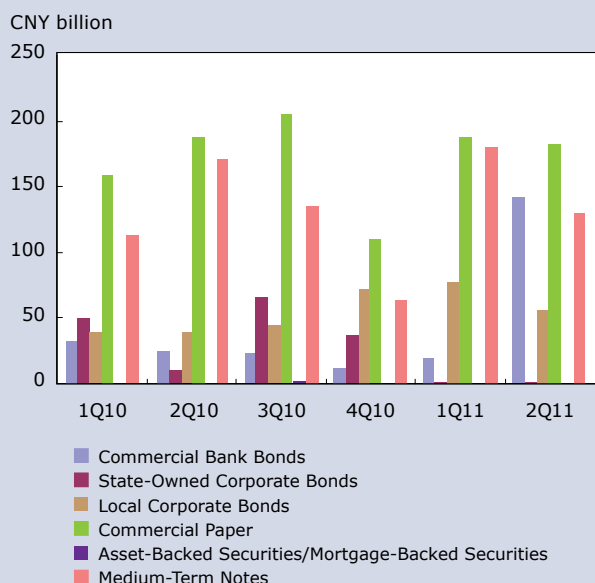
Looking at the PRC's top corporate issuers (**Table 3**), it is clear that only a handful of issuers dominate the market. The top 50 corporate bond issuers accounted for CNY3.14 trillion as of end-

Table 2: Corporate Bonds Outstanding in Key Sectors

	Amount (CNY billion)						Growth Rates (%)					
							q-o-q					y-o-y
	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	2Q10	3Q10	4Q10	1Q11	2Q11	2Q11
Commercial Bank Bonds	589.6	608.5	609.0	609.5	625.0	758.8	3.2	0.1	0.1	2.5	21.4	24.7
State-Owned Corporate Bonds	771.1	781.1	842.6	879.6	879.6	877.1	1.3	7.9	4.4	0.0	(0.3)	12.3
Local Corporate Bonds	420.0	461.7	501.3	569.4	653.1	714.1	9.9	8.6	13.6	14.7	9.3	54.7
Commercial Paper	508.8	615.4	670.6	653.0	683.3	687.1	21.0	9.0	(2.6)	4.6	0.6	11.7
Asset/Mortgage-Backed Securities	31.1	26.5	21.9	18.2	10.8	10.1	(14.8)	(17.2)	(16.8)	(41.0)	(6.1)	(61.8)
Medium-Term Notes	976.4	1,151.2	1,289.5	1,353.6	1,532.5	1,621.4	17.9	12.0	5.0	13.2	5.8	40.8

q-o-q = quarter-on-quarter, y-o-y = year-on-year.

Source: ChinaBond.

Figure 2: Corporate Bond Issuance in Key Sectors, 1Q10-2Q11

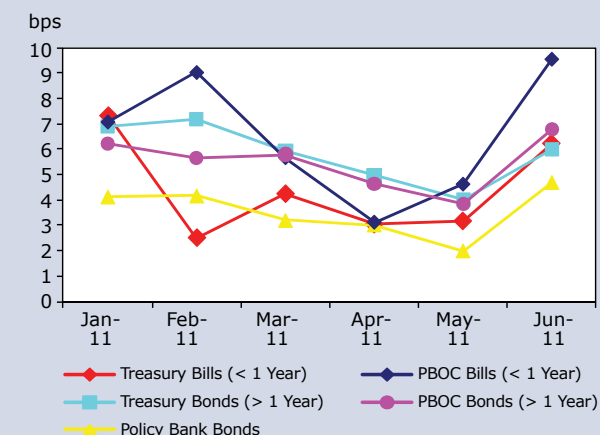
Source: ChinaBond.

June, or 65% of total corporate bonds outstanding. Furthermore, the 10 largest corporate issuers accounted for CNY1.9 trillion, or 60.5% of the total.

State-owned companies (defined as majority-owned by the government) dominate the corporate bond market in the PRC. Out of the top 50 corporate bond issuers, 42 are state-owned, with a total of CNY2.8 trillion worth of bonds outstanding.

Bid-Ask Spreads

Bid-ask spreads rose for all government bonds in May and June (**Figure 3**), reflecting volatility in the bond market resulting from expectations that the PBOC would raise interest rates in June.

Figure 3: Average Bid-Ask Spreads in the PRC, January-June 2011

bps = basis points, PBOC = People's Bank of China, PRC = People's Republic of China.

Source: Wind.

Investor Profile

Treasury bonds. Banks remain the largest category of investors in the PRC treasury bond market, holding a larger share of these bonds at end-June (63%) than at end-December 2010

Table 3: Top 50 Issuers of LCY Corporate Bonds in the People's Republic of China (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (CNY billion)	LCY Bonds (US\$ billion)				
1. Ministry of Railways	548.0	84.78	Yes	No	No	Transportation
2. State Grid Corporation of China	262.5	40.61	Yes	No	No	Public Utilities
3. China National Petroleum	206.0	31.87	Yes	No	No	Energy
4. Bank of China	196.9	30.46	Yes	No	Yes	Banking
5. Industrial and Commercial Bank of China	160.0	24.75	Yes	No	Yes	Banking
6. China Petroleum & Chemical	136.5	21.12	Yes	No	Yes	Energy
7. China Construction Bank	120.0	18.56	Yes	No	Yes	Banking
8. Central Huijin Investment	109.0	16.86	Yes	No	No	Diversified Financial
9. Agricultural Bank of China	100.0	15.47	Yes	No	Yes	Banking
10. Petrochina	99.5	15.39	Yes	No	Yes	Energy
11. Industrial Bank	73.0	11.29	No	Yes	Yes	Banking
12. China Guodian	57.4	8.88	Yes	No	No	Public Utilities
13. Bank of Communications	50.0	7.74	No	Yes	Yes	Banking
14. Shenhua Group	48.4	7.49	Yes	No	No	Energy
15. China Telecom	40.0	6.19	Yes	No	Yes	Telecom
16. China United Network Communications	39.0	6.03	No	Yes	Yes	Telecom
17. China Three Gorges Project	38.5	5.96	Yes	No	No	Public Utilities
18. China Minsheng Bank	38.3	5.93	No	Yes	Yes	Banking
19. Citic Group	37.0	5.72	Yes	No	No	Diversified Financial
20. China Southern Power Grid	36.0	5.57	Yes	No	No	Public Utilities
21. China Resources	35.0	5.41	Yes	No	No	Capital Goods
22. State-Owned Capital Operation and Management Center of Beijing	35.0	5.41	Yes	No	No	Diversified Financial
23. China Power Investment	34.6	5.35	Yes	No	No	Public Utilities
24. Shougang Group	33.0	5.11	Yes	No	No	Capital Goods
25. China Guangdong Nuclear Power Holding	32.9	5.09	Yes	No	No	Public Utilities
26. Metallurgical Corporation of China	32.6	5.04	Yes	No	Yes	Capital Goods
27. Aluminum Corporation of China	31.0	4.80	Yes	No	Yes	Raw Materials
28. China Merchants Bank	30.0	4.64	No	Yes	Yes	Banking
29. China Huaneng Group	28.7	4.44	Yes	No	No	Public Utilities
30. COFCO	28.6	4.42	Yes	No	No	Retail
31. Beijing Infrastructure Investment	27.0	4.18	Yes	No	No	Capital Goods
32. China Railway Group	26.7	4.13	Yes	No	Yes	Capital Goods
33. Aviation Industry Corporation of China	25.0	3.87	Yes	No	No	Capital Goods
34. Huaxia Bank	24.0	3.72	No	Yes	Yes	Banking
35. Wuhan Iron and Steel	24.0	3.71	Yes	No	Yes	Raw Materials
36. Bank of Beijing	23.5	3.64	No	Yes	Yes	Banking
37. China Citic Bank	22.5	3.48	Yes	No	Yes	Banking
38. China State Construction Engineering	22.2	3.43	Yes	No	Yes	Capital Goods
39. China Datang	22.2	3.43	Yes	No	No	Public Utilities
40. Shanghai Chengtou	21.2	3.28	Yes	No	No	Diversified Financial
41. Tianjin Infrastructure Construction Investment Group	20.2	3.13	Yes	No	No	Capital Goods
42. Baoshan Iron and Steel	20.0	3.09	Yes	No	Yes	Raw Materials
43. State Development and Investment	19.5	3.02	Yes	No	No	Capital Goods
44. Huaneng Power International	19.0	2.94	Yes	No	Yes	Public Utilities
45. Shanghai Pudong Development Bank	18.8	2.91	No	Yes	Yes	Banking
46. China Yangtze Power	18.5	2.86	Yes	No	Yes	Public Utilities
47. Hebei Iron and Steel	18.0	2.78	Yes	No	No	Raw Materials

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Table 3 continued

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (CNY billion)	LCY Bonds (US\$ billion)				
48. China Minmetals	17.8	2.75	Yes	No	No	Capital Goods
49. China Everbright Bank	16.0	2.48	Yes	No	Yes	Banking
50. Capital Airports Holding	15.9	2.46	Yes	No	No	Transportation
Total Top 50 LCY Corporate Issuers	3,139.4	485.69				
Total LCY Corporate Bonds	4,846.4	749.76				
Top 50 as % of Total LCY Corporate Bonds	65%	65%				

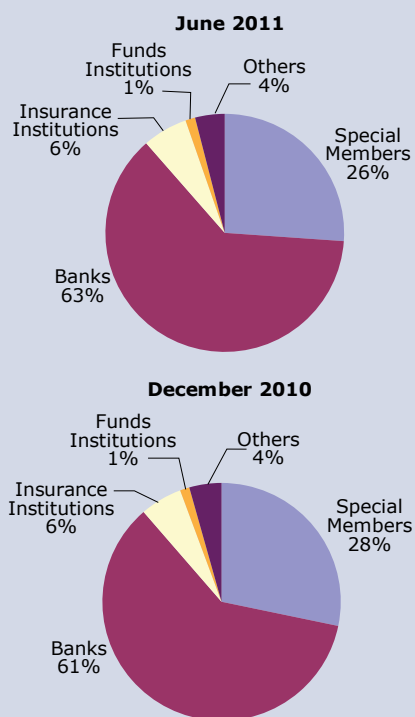
LCY = local currency.

Source: Bloomberg LP and Wind.

(61%) (**Figure 4**). The share held by the second largest group of holders, special members, dropped to 26% at end-June from 28% at end-December 2010. Special members comprise the PBOC, Ministry of Finance, policy banks, China Government Securities Depository Trust and Clearing Co., and the China Securities Depository and Clearing Corporation.

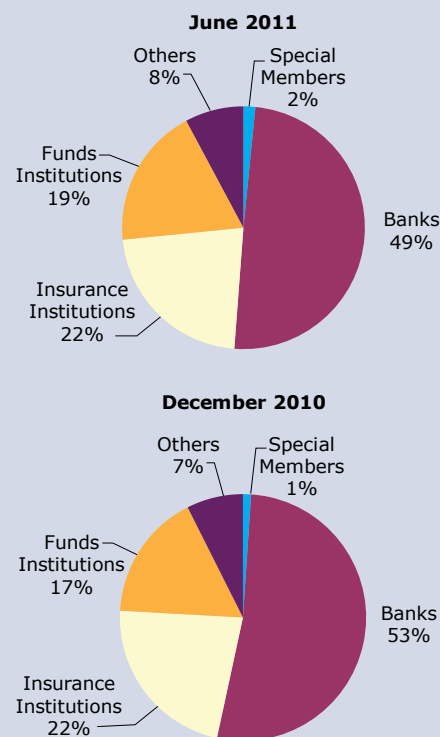
Corporate Bonds. Banks remained the largest holder of corporate bonds at end-June, however, their share declined to 49% from 53% at end-December 2010 (**Figure 5**). The share held by insurance institutions remained the same between December and June, while the share of corporate bonds held by funds increased to 19% from 17%.

Figure 4: Treasury Bonds Investor Profile



Note: Others includes security companies, non-bank institutions, individuals, and exchanges.
Source: ChinaBond.

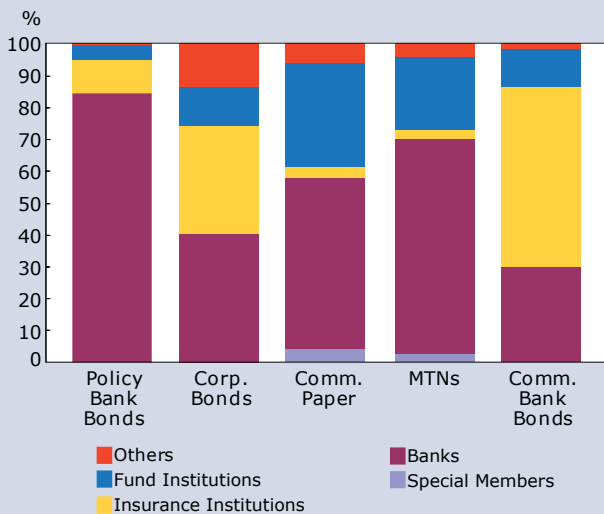
Figure 5: Corporate Bonds Investor Profile



Source: ChinaBond.

Figure 6 presents the investor profile across different bond categories, with banks as the largest group of holders of treasury bonds and policy bank bonds at end-June, including slightly more than 80% of outstanding policy bank bonds. Meanwhile, insurance institutions were the largest holders of commercial bank bonds.

Figure 6: Investor Profile across Bond Categories (as of 30 June 2011)



MTNs = medium-term notes, PRC = People's Republic of China.
 Note: Others includes security companies, non-bank financial institutions, individuals, and exchanges.
 Source: ChinaBond.

Interest Rate Swaps

Table 4 provides information on the total notional amount traded in the interest rate swap (IRS) market in 1H11 compared with the same period in 2010. Growth in the IRS market has been substantial as volumes of most benchmark instruments more than doubled from 1H2010 to 1H11. Overall, the IRS market expanded 150% y-o-y over this period.

During 1H11, the 7-day repo rate remained the most widely used benchmark among the various IRS benchmarks, accounting for 60% of the total notional amount traded. However, the overnight Shanghai Interbank Offered Rate (SHIBOR) and the SHIBOR 3-month rate have also become more widely used as benchmarks in 1H11.

Policy, Institutional, and Regulatory Developments

PBOC Hikes Reserve Requirement Ratios

In response to rising inflation and growing credit risks, the PBOC embarked on a series of reserve requirement ratio hikes, raising the ratio 50 bps in every month in 1H11. As of end-June, the reserve requirement ratio stood at 21.5% for large financial institutions and 19.5% for small and medium-sized institutions.

Table 4: Notional Values of the PRC's Interest Rate Swap Market

Interest Rate Swap Benchmarks	1H11 IRS Notional Amount (CNY billion)	% of Total Notional Amount	1H10 IRS Notional Amount (CNY billion)	% of Total Notional Amount
7-Day Repo Rate	730.9	60.0%	323.4	66.7%
Overnight SHIBOR	224.7	18.4%	69.0	14.2%
1-Week SHIBOR	0.6	0.0%	0.05	0.01%
3-Month SHIBOR	208.5	17.1%	71.0	14.6%
1-Year Term Deposit Rate	52.2	4.3%	21.1	4.4%
1-Year Lending Rate	0.1	0.01%	0.2	0.04%
5-Year and Above Lending Rate	1.4	0.1%	0.0	0%
Total	1,218.4	100.0%	484.7	100.0%

IRS = interest rate swap, PRC = People's Republic of China, repo = repurchase, SHIBOR = Shanghai Interbank Offered Rate.
 Source: ChinaMoney, Wind, and AsianBondsOnline.

CBRC Issues Stricter Bank Rules

On 4 May, the China Banking Regulatory Commission (CBRC) issued new guidelines to be adopted in 2012 that will impose stricter capital adequacy requirements and loan provisions, and liquidity provisions. There will be a number of changes to the capital adequacy rules such as differentiating between core Tier 1 and other types of Tier 1 capital. Operational risk will also be included in the guidelines and risk weights of certain assets will be increased. Banks will be required to maintain a leverage ratio of core capital to total assets of at least 4.0%. There is also a provision ratio requirement that will require banks to set aside reserves equal to 2.5% of outstanding loans.

NPL Requirements Reduced for Loans to Small Firms

On 7 June, the CBRC announced new measures to improve access to credit for smaller firms. Among the measures, loans of less than CNY5 million will not be subject to loan-to-deposit ratio requirements and a differentiated nonperforming loan (NPL) ratio requirement will be implemented for loans to small firms.

Foreign Banks Allowed to Underwrite Corporate Debt

On 17 June, the National Association of Financial Market Institutional Investors (NAFMII) gave permission to the local units of HSBC and Citibank to underwrite corporate debt, making them the first foreign banks with this underwriting authority.

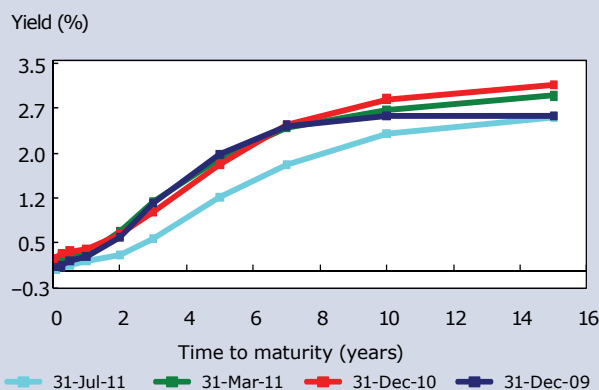
Hong Kong, China—Update

Yield Movements

The yield curve for Hong Kong, China's Exchange Fund Bills and Notes (EFBN) fell for most maturities between end-December 2010 and end-March, with the exception of the belly of the curve. The 15-year tenor declined the most, falling 19 basis points (bps). Meanwhile, the 3-year tenor rose 17 bps. Between end-March and end-July, the entire yield curve shifted downward (**Figure 1**). Yields declined the most between the 3- and 7-year tenors, falling between 61 bps and 64 bps. In contrast, yields for the 1-year tenor dropped only 12 bps. Meanwhile, the spread between 2- and 10-year maturities fell only slightly to 203 bps, compared with a spread of 204 bps at end-March.

Consumer price inflation in Hong Kong, China accelerated to 5.6% year-on-year (y-o-y) in June, up from 5.2% in May, mainly due to higher food prices and increases in utilities and private housing rental costs. Most of the major components of the composite consumer price index posted y-o-y increases in June, including food (7.2%); electricity, gas, and water (8.2%); housing (6.5%); clothing and footwear (6.7%); miscellaneous goods (4.5%); and miscellaneous services (3.3%).

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



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

Demand has proven resilient, with gross domestic product (GDP) growth accelerating to 7.5% y-o-y in 1Q11 from 6.4% in 4Q10. Growth was driven mainly by the services sector, which expanded 7.1% in 1Q11 from 6.4% in 4Q10. Growth in the construction sector remained particularly robust, expanding 22.2% in 1Q11 from 19.8% in 4Q10. On the other hand, the government is increasingly worried about rising real estate prices, which have been attributed to investments made by residents of the People's Republic of China (PRC). In June, the government enacted a number of measures to slow housing price increases including decreasing maximum loan-to-value ratios.

Size and Composition

The size of Hong Kong, China's local currency (LCY) bond market grew 5.1% y-o-y to reach HKD1.3 trillion (US\$167.0 billion) at end-June (**Table 1**). However, on a quarter-on-quarter (q-o-q) basis, LCY bonds outstanding grew at a pace of only 0.5%.

Total LCY government bonds outstanding rose 2.6% y-o-y as of end-June, while q-o-q growth was relatively flat in 2Q11 at 0.5%. Government bonds include Exchange Fund Bills (EFBs), Exchange Fund Notes (EFNs), and bonds issued under the Institutional Bond Issuance Programme (HKSAR Bonds).

The growth in total government bonds outstanding was largely attributed to the growth of EFBs, which expanded 0.6% y-o-y to HKD585 billion as of end-June. On the other hand, the stock of EFNs declined slightly by 0.9% to HKD69.6 billion. HKSAR Bonds outstanding rose 87.5% to reach HKD30.0 billion as of end-June, although they started from a low base of only HKD16.0 billion at end-June 2010.

In March, HKD3.5 billion in 2-year HKSAR Bonds were issued; HKD2.5 billion in 5-year bonds were sold in May.

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

	Amount (billion)						Growth Rate (%)					
	Mar-11		Apr-11		May-11		Mar-11		Apr-11		May-11	
	HKD	US\$	HKD	US\$	HKD	US\$	y-o-y	q-o-q	m-o-m	y-o-y	m-o-m	q-o-q
	Jun-11	US\$	HKD	US\$	HKD	US\$	y-o-y	q-o-q	m-o-m	y-o-y	m-o-m	q-o-q
Total	1,294	166	1,295	167	1,298	167	167	167	167	167	167	167
Government	681	88	682	88	684	88	88	88	88	88	88	88
Exchange Fund Bills	584	75	584	75	585	75	75	75	75	75	75	75
Exchange Fund Notes	70	9	70	9	69	9	9	9	9	9	9	9
HKSAR Bonds	28	4	28	4	30	4	4	4	4	4	4	4
Corporate	612	79	613	79	614	79	79	79	79	79	79	79

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 end-of-period LCY-US\$ 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 April, May, and June 2011 were estimated based on the compounded monthly growth rate between December 2010 and March 2011.

Source: Hong Kong Monetary Authority (HKMA) and Bloomberg LP.

The amount of LCY corporate bonds outstanding reached HKD615.3 billion at end-June, reflecting growth of 8.1% y-o-y and 0.5% q-o-q. The top 17 non-bank corporate issuers in Hong Kong, China accounted for 13.8% of total corporate bonds outstanding at end-June (**Table 2**). Hong Kong, China's top corporate issuer of LCY bonds is the state-owned Hong Kong Mortgage Corporation (HKMC), with bonds valued at HKD20.7 billion. Sun Hung Kai Properties (Capital Market) Ltd. was the next largest issuer with outstanding bonds of HKD11.8 billion, while CLP Power Hong Kong Financing Ltd. was in the third spot with HKD9.9 billion.

Financial firms dominated the list of the top 17 non-bank corporate issuers, accounting for all but four of the firms. Six state-owned companies were included on the list, while 11 were privately owned. Among the companies in Table 2, only one company is listed on the Hong Kong Exchange.

CNH Bond Market

The offshore renminbi (CNH) bond market in Hong Kong, China continued to grow in 2Q11. As of end-June, outstanding offshore renminbi deposits had grown to CNH553.6 billion from CNH314.9 billion at end-December 2010. Furthermore, year-to-date bond issuance reached CNH65.5 billion through 15 June. In comparison, total CNH bond issuance in 2010 was CNH42.7 billion. The outstanding amount of CNH bonds and certificates of deposits stood at CNH143.2 billion as of end-June.

Issuers in the renminbi bond market include high-grade issuers such as the Government of the PRC and lower-rated institutions such as Galaxy Entertainment. However, in terms of tenor, there are very few long-dated bonds available for investors as most issuers prefer to issue in the 2- to 3-year category.

Table 2: Top 17 Non-Bank Corporate Issuers (as of June 2011)

Top 17 LCY Non-Bank Corporate Bond Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (HKD billion)	LCY Bonds (US\$ billion)				
1. The Hong Kong Mortgage Corporate Ltd.	20.72	2.66	Yes	No	No	Finance
2. Sun Hung Kai Properties (Capital Market) Ltd.	11.80	1.52	No	Yes	No	Finance
3. CLP Power Hong Kong Financing Ltd.	9.90	1.27	No	Yes	No	Finance
4. Kowloon-Canton Railway Corporation	6.60	0.85	Yes	No	No	Transportation
5. MTR Corporation (C.I.) Ltd.	5.20	0.67	Yes	No	Yes	Transportation
6. Swire Pacific MTN Financing Ltd.	4.80	0.62	No	Yes	No	Finance
7. Hongkong Electric Finance Ltd.	4.21	0.54	No	Yes	No	Finance
8. Airport Authority Hong Kong	2.90	0.37	Yes	No	No	Transportation
9. HKCG (Finance) Limited	2.76	0.35	No	Yes	No	Finance
10. The Link Finance (Cayman) 2009 Ltd.	2.68	0.34	No	Yes	No	Finance
11. Cheung Kong Bond Finance Ltd.	2.45	0.31	No	Yes	No	Finance
12. Cheung Kong Finance (MTN) Ltd.	2.45	0.31	No	Yes	No	Finance
13. Wharf Finance Ltd.	2.29	0.29	No	Yes	No	Finance
14. Bauhinia MBS Ltd.	2.21	0.28	Yes	No	No	Finance
15. Hysan (MTN) Ltd.	1.80	0.23	No	Yes	No	Finance
16. Urban Renewal Authority	1.70	0.22	Yes	No	No	Property Development
17. The Hongkong Land Notes Company Ltd.	0.20	0.03	No	Yes	No	Finance
Total Top 17 Non-Bank LCY Corporate Issuers	84.66	10.88				
Total LCY Corporate Bonds	615.31	79.07				
Top 17 as a % of Total LCY Corporate Bonds	13.76%	13.76%				

LCY = local currency.
Source: HKMA Central Moneymarkets Unit (CMU).

Policy, Institutional, and Regulatory Developments

HKMA Launches CNH Fiduciary Account Service for Banks

On 31 March, the Hong Kong Monetary Authority (HKMA) launched the CNH Fiduciary Account Service to provide another investment outlet for banks' CNH deposits as an alternative to the designated clearing bank, Bank of China (BOC). The service will effectively allow banks to invest CNH deposits directly with the People's Bank of China (PBOC) via a custodial arrangement with BOC.

BOC Cuts CNH Deposit Rate

BOC cut its CNH deposit rate to 0.629% from 0.865% on 1 April due to increasing demand for the currency.

SFC to Regulate Credit Rating Agencies

On 28 April, the Securities and Futures Commission (SFC) announced that it would begin requiring credit rating agencies and their analysts to be licensed.

Hong Kong, China Introduces New Property Loan Measures

On 10 June, the Government of the Hong Kong Special Administrative Region of the PRC announced a number of additional measures designed to reign in housing prices. Most of the new measures concern lowering the maximum loan-to-value ratios for residential properties. Additionally, if the borrower is not a resident of Hong Kong, China, the loan-to-value ratio will be lowered by an additional 10%.

Indonesia—Update

Yield Movements

The government bond yield curve in Indonesia rose across all tenors, except for the 30-year maturity, between end-December 2010 and end-March (Figure 1). However, by end-July, bond yields in Indonesia had dropped across all tenors compared with end-December 2010 levels, which resulted in the shifting of the entire curve downward. Yields at the short-end of the curve shed between 53 basis points (bps) and 72 bps, while yields from the belly through the 10-year tenor fell between 7 bps and 57 bps. Yields at the long-end of the curve fell between 98 bps and 109 bps. The yield spread between the 2-year and 10-year maturities widened to 161 bps at end-July, compared with a spread of 135 bps at end-June, while narrowing slightly compared with a spread of 174 bps at end-December 2010.

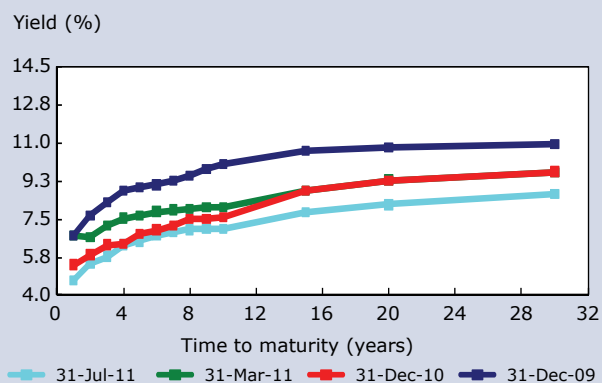
Consumer price inflation eased for a sixth consecutive month in July to 4.6% year-on-year (y-o-y) from 5.5% in June. On a month-on-month (m-o-m) basis, consumer prices were up 0.7% as food prices rose ahead of the celebration of Ramadan. Core inflation however eased slightly to 4.55% y-o-y from 4.63% in June.

Bank Indonesia's (BI) full-year 2011 inflation target stands at between 4% and 6%.

In its meeting held on 9 August, BI's Board of Governors decided to keep its reference rate steady at 6.75%. The BI rate has been kept at this level since February. According to BI, the current rate is consistent with expectations of a robust, yet stable, environment for economic growth. In addition, BI stated that it is confident that the impact on domestic financial markets of the recent turmoil in global markets due to the US credit rating downgrade by Standard and Poor's (S&P) will be limited and can be contained through monitoring and coordination with the government.

Indonesia's economy expanded 6.5% y-o-y in 2Q11, growing at the same pace it did in 1Q11 on the back of strong exports and investment. Exports grew 17.4% y-o-y in 2Q11 compared with a 12.3% expansion in 1Q11, while investment rose 9.2% y-o-y from 7.3% growth in 1Q11. Also, household and government spending posted strong growth in 2Q11, rising 4.6% and 4.5% y-o-y, respectively. On a quarter-on-quarter (q-o-q) basis, gross domestic product (GDP) growth was reported at 2.9%, up from 1.5% in 1Q11. The government's 2011 State Budget is targeting annual GDP growth of 6.4%.

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



LCY = local currency.
Source: Bloomberg LP.

Size and Composition

The size of Indonesia's local currency (LCY) bond market expanded 2.4% y-o-y in 2Q11, rising to IDR1.0 quadrillion (US\$118 billion) at end-June (Table 1). On a q-o-q basis, the size of Indonesia's bond market fell 1.7% in 2Q11.

At end-June, outstanding LCY government bonds had fallen 1.7% y-o-y to IDR877 trillion. The negative growth in LCY bonds was due mainly to the significant drop in the stock of central bank bills known as *Sertifikat Bank Indonesia* (SBI). On the other hand, the stock of central government bonds, comprising treasury bills and bonds issued by the Ministry of Finance, posted modest growth.

	Amount (billion)								Growth Rate (%)							
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11		May-11		Jun-11	
	IDR	US\$	IDR	US\$	IDR	US\$	IDR	US\$	Y-o-Y	Q-o-Q	m-o-m	Y-o-Y	Q-o-Q	m-o-m	Y-o-Y	Q-o-Q
Total	1,026,228	118	1,033,376	121	1,012,955	119	1,008,959	118	4.1	7.0	0.7	2.4	(1.7)	(0.4)		
Government	905,058	104	909,111	106	885,236	104	876,979	102	1.3	7.2	0.4	(1.7)	(3.1)	(0.9)		
Central Govt Bonds	674,910	78	679,040	79	687,365	80	691,033	81	13.8	5.3	0.6	1.2	2.4	0.5		
Central Bank Bills	230,148	26	230,071	27	197,871	23	185,946	22	(23.3)	13.3	(0.03)	(31.4)	(19.2)	(6.0)		
Corporate	121,170	14	124,265	15	127,719	15	131,980	15	31.4	5.5	2.6	2.8	8.9	3.3		

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—US\$ 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.

In May, investors swapped a total of IDR50 billion of LCY government bonds with maturities due in 2011–2014 for 15-year bonds. The government regularly conducts debt switches as a strategy to reduce refinancing risk.

As of 7 July, the government had raised IDR124.6 trillion from gross bond sales in 2011, including international bond issuance. For the full-year 2011, the State Budget estimates a deficit amounting to IDR124.7 trillion, or the equivalent of 1.8% of GDP. However, the actual budget deficit for 2011 may be higher, falling in a range of 1.9% to 2.1%, as the government is planning to raise fuel subsidy quotas. The Finance Ministry is currently holding discussion with the House of Representatives to finalize the revised 2011 State Budget.

Central Bank Bills. The stock of central bank bills declined further in 2Q11. Outstanding SBI stood at IDR185.9 trillion in 2Q11, falling 31.4% y-o-y and 19.2% q-o-q. During the quarter, BI conducted a total of only three auctions (one per month) of 9-month SBI and 9-month *sharia'h* (Islamic law)-compliant SBI.

A new regulation governing SBI, effective 13 May, extended the holding period for SBI to 6 months before they can be traded in the secondary market. The measure is part of BI's strategy to minimize the effects of sudden capital flow reversals.

Corporate Bonds. Corporate bonds outstanding grew significantly in 2Q11 to IDR132 trillion, up 41.9% from 2Q10. Although growth in the corporate sector was significant, corporate bonds still comprise a small percentage of Indonesia's total LCY bond market. At end-June, corporate bonds accounted for only about 13% of total LCY bonds outstanding in Indonesia.

The top 50 corporate bond issuers in Indonesia accounted for about 92% of total corporate bonds outstanding at end-June (**Table 2**). State-power firm PLN remained the top LCY issuer in Indonesia with outstanding bonds valued at IDR15.1 trillion. Bank Pan Indonesia took the second spot with bonds valued at IDR6.9 trillion. Telecommunications firm Indosat was the third largest issuer with bonds valued at IDR6.4 trillion.

The list of the top 50 corporate bond issuers was dominated by banking and financial institutions, which accounted for 60% of all companies on the list. Eleven issuers were state-owned firms, with four of them among the ten largest.

LCY corporate bond issuance expanded significantly in 2Q11, albeit from a relatively small base. Corporate issuance rose 104.9% y-o-y to IDR15.0 trillion in 2Q11, compared with IDR7.3 trillion in 2Q10. Corporate bond issuers in 2Q11 were mainly firms from the banking and financial sectors. Corporate bonds issued in 2Q11 included conventional bonds, *sukuk*, and subordinated bonds. Notable issues during 2Q11 are shown in **Table 3**.

Financing company Federal International Finance raised IDR3 trillion in April to fund its working capital requirements. The bonds comprised the following tranches:

- (i) 370-day bonds worth IDR621.5 billion, coupon of 7.8%;
- (ii) 2-year bonds worth IDR480 billion, coupon of 8.8%; and
- (iii) 3-year bonds worth IDR1.9 trillion, coupon of 9.6%.

Automotive financing company Adira Dinamika Multifinance issued IDR2.5 trillion worth of bonds in May. Proceeds from the bond sale will be used to fund its automotive financing business. The bonds comprised the following tranches:

- (i) 1-year bonds worth IDR612 billion, coupon of 8.0%;
- (ii) 2-year bonds worth IDR160 billion, coupon of 8.8%;
- (iii) 3-year bonds worth IDR567 billion, coupon of 9.6%; and
- (iv) 4-year bonds worth IDR1.2 trillion, coupon of 10.0%.

Bank Permata issued IDR1.75 trillion of subordinated bonds in June. The subdebt issue carried a coupon of 11.0% and a maturity of 7 years. The deal was an upsize from an original plan of IDR1 trillion. Proceeds from the issue will be used to fund the bank's Lower Tier 2 capital requirements.

In May, Bank Internasional Indonesia issued IDR1.5 trillion of subordinated bonds. The subdebt bonds carried a coupon of 10.75% and a maturity of 7 years. The proceeds from this issue will be used to help meet the bank's 20% loan expansion target for 2011.

Home mortgage provider Bank Tabungan Negara sold IDR1.3 trillion of 10-year bonds in June. The bonds carried a coupon of 9.5%. Proceeds from the bond sale will be used to support the expansion of the bank's housing loan program.

Also in June, BCA Finance raised a total of IDR1.1 trillion from a five-tranche bond sale. The bonds comprised the following tranches:

- (i) 1-year bonds worth IDR392 billion, coupon of 7.9%;
- (ii) 1-year bonds worth IDR178 billion, coupon of 8.1%;
- (iii) 2-year bonds worth IDR230 billion, coupon of 8.7%;
- (iv) 3-year bonds worth IDR200 billion, coupon of 8.9%; and
- (v) 4-year bonds worth IDR100 billion, coupon of 9.0%.

Table 2: Top 50 Issuers of LCY Corporate Bonds in Indonesia (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (IDR billion)	LCY Bonds (US\$ billion)				
1. PLN (Persero)	15,100	1.76	Yes	No	No	Energy
2. Bank Pan Indonesia Tbk	6,900	0.80	No	Yes	Yes	Bank
3. Indosat Tbk	6,350	0.74	No	Yes	Yes	Telecommunication
4. Bank Tabungan Negara (Persero)	5,450	0.64	Yes	No	Yes	Bank
5. Indonesia Eximbank	5,341	0.62	Yes	No	No	Bank
6. Jasa Marga (Persero) Tbk	5,000	0.58	Yes	No	Yes	Toll Road, Airport, Harbor, and Allied Products
7. Adira Dinamika Multifinance Tbk	4,903	0.57	No	Yes	Yes	Financial Institution
8. Federal International Finance	4,742	0.55	No	Yes	No	Financial Institution
9. Bank Danamon Indonesia Tbk	4,050	0.47	No	Yes	Yes	Bank
10. Astra Sedaya Finance	3,660	0.43	No	Yes	No	Financial Institution
11. Bank Tabungan Pensiunan Nasional Tbk	3,650	0.43	No	Yes	Yes	Bank
12. Indofood Sukses Makmur Tbk	3,574	0.42	No	Yes	Yes	Food and Beverages
13. Bank Mandiri (Persero) Tbk	3,500	0.41	Yes	No	Yes	Bank
14. Perum Pegadaian	3,000	0.35	Yes	No	No	Financial Institution
15. Telekomunikasi Indonesia Tbk	3,000	0.35	Yes	No	Yes	Telecommunication
16. Bank CIMB Niaga	2,980	0.35	No	Yes	Yes	Bank
17. Bank Jabar Banten	2,750	0.32	No	Yes	Yes	Bank
18. Bank Permata Tbk	2,250	0.26	No	Yes	Yes	Bank
19. Bank Rakyat Indonesia (Persero) Tbk	2,000	0.23	Yes	No	Yes	Bank
20. Oto Multiartha	2,000	0.23	No	Yes	No	Financial Institution
21. Wahana Ottomitra Multiartha Tbk	1,990	0.23	No	Yes	Yes	Financial Institution
22. Summit Oto Finance	1,865	0.22	No	Yes	No	Financial Institution
23. Bank Internasional Indonesia Tbk	1,500	0.17	No	Yes	Yes	Bank
24. Bank DKI	1,500	0.17	No	Yes	No	Bank
25. Excelcomindo Pratama Tbk	1,500	0.17	No	Yes	Yes	Telecommunication
26. Medco Energi Internasional Tbk	1,500	0.17	No	Yes	Yes	Crude Petroleum and Natural Gas Production
27. BCA Finance	1,489	0.17	No	Yes	No	Financial Institution
28. Bank OCBC NISP Tbk	1,480	0.17	No	Yes	Yes	Bank
29. Bentoel International Investama Tbk	1,350	0.16	No	Yes	Yes	Tobacco Manufacturers
30. Berlian Laju Tanker Tbk	1,340	0.16	No	Yes	Yes	Transportation
31. Danareksa (Persero)	1,250	0.15	Yes	No	No	Others Finance
32. Indomobil Finance Indonesia Tbk	1,204	0.14	No	Yes	No	Financial Institution
33. Sarana Multigriya Finansial (Persero)	1,190	0.14	Yes	No	No	Financial Institution
34. Bank Jabar Banten	1,000	0.12	No	Yes	Yes	Bank
35. Bank Mega Tbk	1,000	0.12	No	Yes	Yes	Bank
36. Bank Negara Indonesia (Persero) Tbk	1,000	0.12	Yes	No	Yes	Bank
37. Pupuk Kalimantan Timur	791	0.09	No	Yes	No	Chemicals
38. Salim Ivomas Pratama	730	0.09	No	Yes	No	Plantation
39. BW Plantation	700	0.08	No	Yes	Yes	Plantation
40. Bank Pembangunan Daerah Sumatera Barat	681	0.08	No	Yes	No	Bank
41. Lontar Papyrus Pulp & Paper Industry	675	0.08	No	Yes	No	Pulp and Paper
42. Bakrie Telecom Tbk	650	0.08	No	Yes	Yes	Telecommunication
43. Mobile-8 Telecom Tbk	604	0.07	No	Yes	Yes	Telecommunication
44. Surya Arya Nusantara Finance Tbk	600	0.07	No	Yes	No	Financial Institution
45. Mandiri Tunas Finance Tbk	600	0.07	No	Yes	No	Financial Institution
46. Bumi Serpong Damai Tbk	600	0.07	No	Yes	Yes	Property and Real Estate
47. Arpeni Pratama Ocean Line Tbk	600	0.07	No	Yes	Yes	Transportation

continued on next page

Table 2 continued

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (IDR billion)	LCY Bonds (US\$ billion)				
48. Apexindo Pratama Duta Tbk	600	0.07	No	Yes	No	Crude Petroleum and Natural Gas Production
49. Surya Citra Televisi	575	0.07	No	Yes	No	Advertising, Printing, and Media
50. Matahari Putra Prima Tbk	528	0.06	No	Yes	Yes	Retail Trade
Total Top 50 Corporate Issuers	121,292	14.14				
Total Corporate Bonds Outstanding	131,980	15.38				
Total Top 50 LCY Corporate Issuers	91.9%	91.9%				
Total LCY Corporate Bonds	114,817	12.76				
Top 50 as a % of Total LCY Corporate Bonds	94.1%	94.1%				

LCY = local currency.
Source: Indonesia Stock Exchange.

Table 3: Notable Corporate Issuance in 2Q11

Corporate Issuers	Amount Issued (IDR billion)
Federal International Finance	3,000
Adira Dinamika Multifinance Tbk	2,500
Bank Permata Tbk	1,750
Bank Internasional Indonesia Tbk	1,500
Bank Tabungan Negara (Persero)	1,300
BCA Finance	1,100
Indomobil Finance Indonesia Tbk	1,000
Others	2,813
Total	14,963

Source: Indonesia Stock Exchange.

Automotive financing firm Indomobil Finance Indonesia issued a total of IDR1.0 trillion of bonds in June. The bonds comprised the following tranches:

- (i) 1-year bonds worth IDR75 billion, coupon of 8.0%;
- (ii) 3-year bonds worth IDR400 billion, coupon of 10.15%; and
- (iii) 4-year bonds worth IDR525 billion, coupon of 10.65%.

Foreign Currency Bonds

In May, the government issued US\$2.5 billion worth of 10-year bonds. The US\$-denominated bonds were issued with a coupon of 4.875% to yield 5.1%. The bond sale was oversubscribed by 2.76 times. The bonds were allocated to asset managers (70%), banks (24%), insurance and

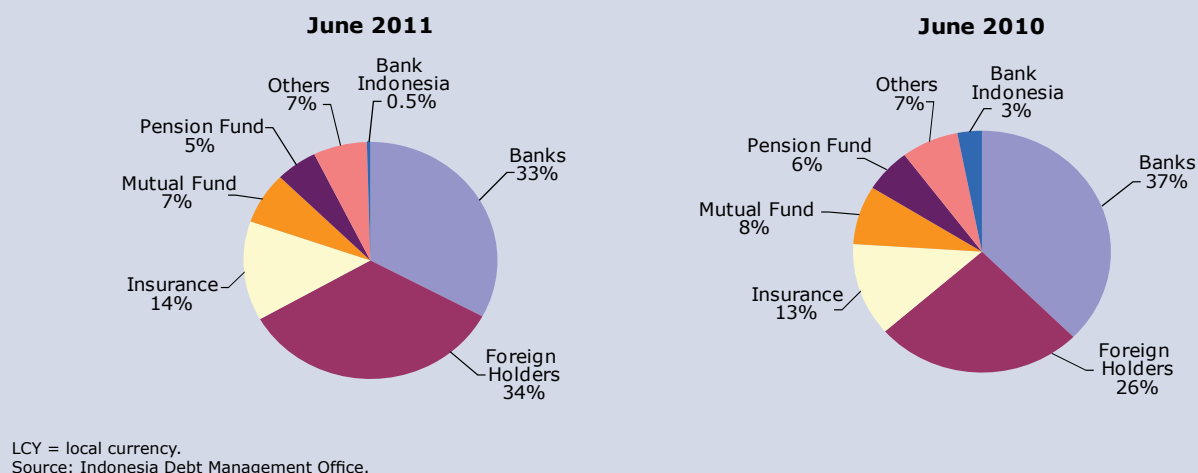
pension funds (3%), and private banks (3%). In terms of distribution, 29% were sold to investors in Asia, 22% in Europe, and 49% in the United States (US).

Investor Profile

Central Government Bonds. Banking institutions, which were the largest holder of LCY government bonds in Indonesia at end-June 2010, ranked second after foreign holders at end-June 2011. Banks' share of central government bonds fell to 33% from 37% over this period (**Figure 2**). In 2002, banks held as much as 82% of total LCY government bonds.

Foreign investors as a group became the largest holder of Indonesian LCY bonds in 2Q11, with their share rising to 34% at end-June compared with 26% in June 2010. Foreign holders include non-resident private banks, fund and asset management firms, securities firms, insurance companies, and pension funds. The holdings of foreign investors have steadily grown from only IDR2 trillion (0.5%) in 2002 to IDR235 trillion (34%) in 2011 (**Figure 3**).

Of the bonds held by foreigners at end-June, 63% carried maturities of more than 5 years (**Figure 4**). However, this reflected a drop from 67% in 2010 and 71% in 2009. Meanwhile, the share of bonds held by foreign investors in short-dated tenors (bonds with maturities of less than 1 year) jumped

Figure 2: LCY Government Bonds Investor Profile

to 12% in June 2011, compared with only 10% in 2010 and 5% in 2009. Some investors may have shifted their investments to short-dated treasury instruments as the central bank issued regulations concerning SBI (see **Policy, Institutional, and Regulatory Developments** for more details).

The share of insurance companies grew marginally to 14% at end-June from 13% at end-June 2010. The share of mutual funds and pension funds fell slightly to 7% and 5%, respectively, compared with their June 2010 levels of 8% and 6%.

Central Bank Bills. SBI remain an attractive investment instrument among domestic lenders as well as foreign investors because of their high yields and short duration. As of end-June, banks remained the largest investor in SBI with a 62% share of the total (**Figure 5**). This, however, was a steep decline from the banks' share of 82% in June 2010. The share of bank holdings of SBI reached a high of 89% in June 2009.

Foreign investors' SBI holdings continued to grow in 2011 as the share of non-residents more

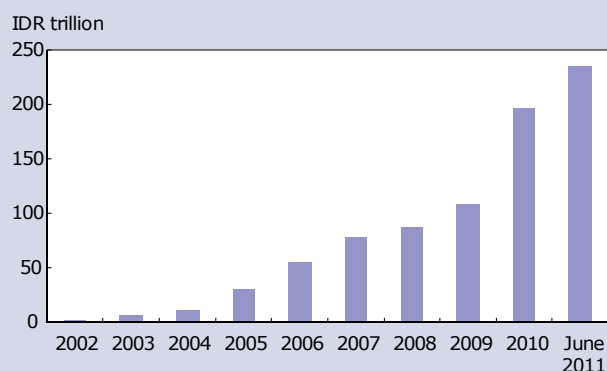
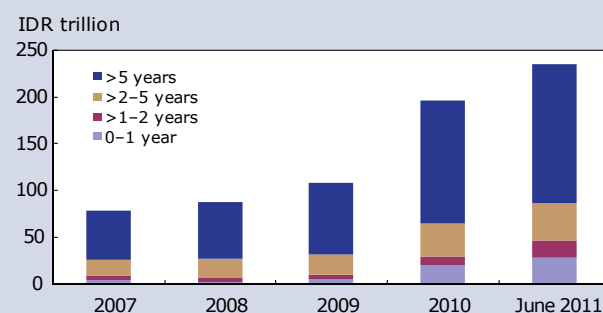
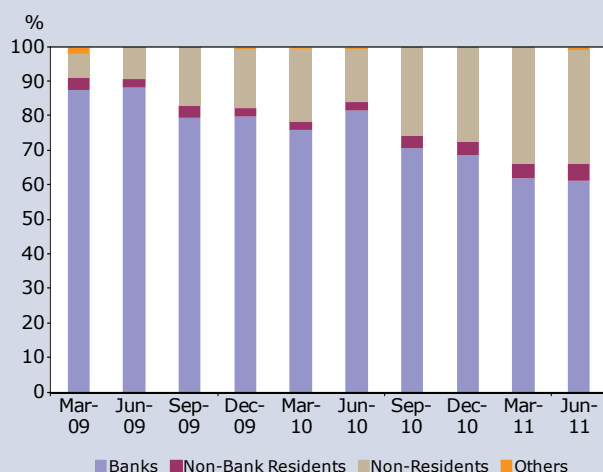
Figure 3: Foreign Holdings of LCY Government Bonds**Figure 4: Foreign Holdings of LCY Government Bonds by Maturity**

Figure 5: LCY Central Bank Bills Investor Profile

LCY = local currency.
Source: Bank Indonesia.

than doubled to 33% at end-June from 16% in June 2010. Also, non-bank residents' share increased to 5% at end-June compared with 3% in June 2010.

Rating Changes

On 8 April, S&P raised Indonesia's long-term foreign currency sovereign ratings to BB+ from BB, and affirmed its long-term LCY rating at BB+ (**Table 4**). The outlook for both ratings is positive, indicating a potential upgrade in the near future. S&P cited improvements in the government's balance sheet and external liquidity as the main factors for the upgrade.

Policy, Institutional, and Regulatory Developments

Finance Ministry Issues 3-Month Treasury Bills

On 22 March, the Finance Ministry issued treasury bills with a 3-month tenor for the first time ever. The issuance of 3-month bills was initiated as part of efforts to deepen the market for short-term financial instruments following a BI announcement

Table 4: Selected Sovereign Ratings and Outlook for Indonesia

	Moody's	S&P	Fitch	R&I
Sovereign FCY LT Ratings	Ba1	BB+	BB+	BB+
Outlook	stable	positive	positive	positive

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

in February that it would no longer issue SBI with maturities of less than 9 months.

IBPA Sets Daily Fair Market Price for *Mudharaba Sukuk*

In April, the Indonesia Bond Pricing Agency (IBPA) commenced setting daily fair market prices for *mudharaba* (risk and profit sharing) *sukuk* to serve as a benchmark for investors in determining price valuation for any *sukuk* issued by private companies and listed on the Indonesia Stock Exchange. Prior to this, IBPA provided fair market price for government bonds, *sharia'h*-compliant government bonds, conventional corporate bonds, and *ijarah* (lease and buy back) corporate *sukuk*.

Holding Period for SBI of 6 Months

Effective 13 May, the holding period for SBI—the amount of time before they can be sold by investors in the secondary market—was extended to 6 months. This policy aims to reduce the potential for sudden reversals of foreign short-term funds.

Indonesia's Parliament Approves IDR30.2 Trillion of Underlying Assets for *Sukuk*

In June, the House of Representatives approved the government's proposal to use state properties valued at IDR30.2 trillion as underlying assets for government-issued *sukuk*. The state properties that will be used to back the *sukuk* consist of buildings and land owned by ministries and other government institutions. Two scheduled auctions of IDR-denominated *sukuk*—on 31 May and 14 June—were postponed as the government waited for approval of the underlying assets.

Fitch Changes Bond Rating Process

Fitch Ratings announced that it has changed the process for rating proposed bond issuances in Indonesia's domestic bond market, effective 7 July. According to Fitch, it will no longer assign initial expected ratings and subsequent final national ratings. It will now provide only one rating for a proposed bond issue. For bond issuers involved in both domestic and international markets, any international rating already assigned will not be affected by this new practice.

Finance Ministry Issues Islamic Treasury Bills

On 2 August, the Finance Ministry issued its maiden Islamic treasury bills, as part of efforts to diversify and increase the liquidity of Islamic bond instruments. The first issue of Islamic treasury bills carried a maturity of 6 months.

Republic of Korea—Update

Yield Movements

The Republic of Korea's government bond yield curve flattened between end-March and end-July (**Figure 1**). Yields for 1-, 2-, and 3-year tenors rose during this period, with the 1-year tenor increasing the most at 26 basis points (bps). Yields for 5-, 10-, and 20-year tenors fell 9 bps, 28 bps, and 34 bps, respectively. The yield spread between 2- and 10-year tenors narrowed by 46 bps between end-March and end-July. The flattening of the yield curve appeared to reflect market expectations of further policy rate hikes amid inflationary pressures.

The Bank of Korea raised its base rate—the 7-day repurchase rate—25 bps in January, March, and June for a total increase of 75 bps in the first half of the year. The policy rate hikes were made to counter inflationary pressures and ensure overall price stability. On 11 August, the Bank of Korea decided to hold steady the base rate at 3.25%, noting both the domestic economy's upward growth trend and heightened inflation risk, as well as global downside risks—such as slowing economic growth in the United States (US) and Europe's sovereign debt problems.

In the first 3 months of the year, consumer price inflation climbed steadily from 4.1% year-on-year (y-o-y) in January to 4.5% in February and 4.7% in March. At the start of 2Q11, however, the inflation rate dipped to 4.2% y-o-y in April and declined further to 4.1% in May, after which it rose to 4.4% in June. In July, consumer price inflation increased further to 4.7% y-o-y mainly due to a 10.0% spike in the price index for food and non-alcoholic beverages.

Advance estimates for the country's real gross domestic product (GDP) released in July showed that economic growth eased to 0.8% quarter-on-quarter (q-o-q) in 2Q11 from 1.3% in 1Q11, as export growth slowed to 1.8% from 3.3% in the previous quarter. On a y-o-y basis, the real GDP growth rate fell to 3.4% in 2Q11 from 4.2% in 1Q11.

Size and Composition

The local currency (LCY) bond market in the Republic of Korea had grown 8.1% y-o-y and 2.3% q-o-q as of end-June, with total bonds outstanding amounting to KRW1,358.9 trillion (US\$1.3 trillion) (**Table 1**). The outstanding amount of LCY government bonds reached KRW582.4 trillion at end-June, up 4.2% from June 2010 and 1.3% from the previous quarter. Central government bonds—largely consisting of Korea Treasury Bonds (KTBs)—increased 8.2% y-o-y and 2.2% q-o-q to KRW386.9 trillion. In contrast, Monetary Stabilization Bonds (MSBs)—bonds issued by the Bank of Korea—decreased 1.0% y-o-y and 1.5% q-o-q to KRW166.0 trillion. Meanwhile, the outstanding size of industrial finance debentures—bonds issued by the Korea Development Bank (KDB)—fell 12.7% y-o-y, but rose 5.2% q-o-q.

Total LCY government bond issuance in 2Q11 stood at KRW88.1 trillion, which was 16.3% higher than in the previous quarter. The increase was bolstered by a 26.9% q-o-q rise in MSB issuance in 2Q11, which totaled KRW60.8 trillion. On the other hand, issuance of central government bonds declined

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

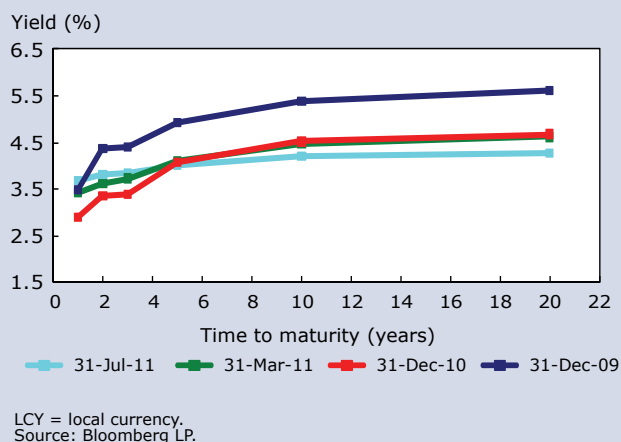


Table 1: Size and Composition of the LCY Bond Market in the Republic of Korea

	Amount (billion)												Growth Rate (%)					
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11		May-11		Jun-11			
	KRW	US\$	KRW	US\$	KRW	US\$	KRW	US\$	y-o-y	q-o-q	m-o-m	m-o-m	y-o-y	q-o-q	m-o-m			
Total	1,328,907	1,211	1,339,038	1,250	1,352,823	1,254	1,358,854	1,273	7.3	2.7	0.8	1.0	8.1	2.3	0.4			
Government	575,093	524	577,252	539	585,980	543	582,414	546	3.7	3.8	0.4	1.5	4.2	1.3	(0.6)			
Central Bank Bonds	168,470	154	165,550	154	169,620	157	165,960	155	3.9	3.0	(1.7)	2.5	(1.0)	(1.5)	(2.2)			
Central Government Bonds	378,557	345	382,579	357	386,481	358	386,942	362	6.1	4.4	1.1	1.0	8.2	2.2	0.1			
Industrial Finance Debentures	28,066	26	29,123	27	29,879	28	29,512	28	(20.7)	0.2	3.8	2.6	(12.7)	5.2	(1.2)			
Corporate	753,814	687	761,786	711	766,843	711	776,440	727	10.2	1.9	1.1	0.7	11.3	3.0	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. Central government bonds include Korea Treasury Bonds, National Housing Bonds, and Seoul Metropolitan Subway Bonds.
3. Bloomberg LP end-of-period LCY-US\$ rates are used.
4. Growth rates are calculated from LCY base and do not include currency effects.

Source: The Bank of Korea, EDAILY BondWeb, and Bloomberg LP.

3.6% from the previous quarter to KRW23.8 trillion in 2Q11.

Two of the largest government bond issues in 1H11 were a KRW12.7 trillion 2-year MSB issued in April at a 3.83% coupon and a KRW10.7 trillion 5-year KTB issued in March with a coupon rate of 4.0%.

The government started auctioning 28-day treasury bills in March and had sold a total of KRW9.7 trillion worth by end-June. In addition, the government sold a 10-year inflation-linked bond in June worth KRW244 billion with a coupon rate of 1.5%. At end-June, the outstanding size of inflation-linked bonds was KRW3.6 trillion.

The LCY corporate bond market at end-June amounted to KRW776.4 trillion, having expanded 11.3% y-o-y and 3.0% q-o-q (Table 1). The growth was spearheaded by private corporate bonds that grew 25.9% y-o-y and 5.2% q-o-q to reach KRW317.5 trillion. In 2Q11, the amount of outstanding special public bonds climbed 7.7% y-o-y and 2.8% q-o-q, totaling KRW253.2 trillion. Meanwhile, financial debentures (excluding KDB bonds) slipped 2.2% y-o-y and 0.1% q-o-q to KRW205.8 trillion.

The top 50 issuers of LCY corporate bonds had a cumulative outstanding balance at end-June of KRW577.8 trillion, or 74% of total corporate bonds outstanding (Table 2). Of the top 50 issuers of LCY bonds in the Republic of Korea at end-June, 70% were financial institutions and 56% were privately owned entities. Meanwhile, 44% were listed on the Korea Exchange. Korea Land & Housing Corp. remained the largest issuer of corporate bonds with total outstanding bonds of KRW55.3 trillion at end-June.

In 2Q11, total LCY corporate bond issuance was KRW84.1 trillion, of which 54% were private corporate bonds, 27% were financial debentures, and the remaining 19% were special public bonds. Corporate bond issuance in 2Q11 was up 14.8% q-o-q, but down 0.3% y-o-y. On a q-o-q basis, issuance increased for all three types of corporate bonds—financial debentures, private

Table 2: Top 50 Issuers of LCY Corporate Bonds in the Republic of Korea (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed In		Type of Industry
	LCY Bonds (KRW billion)	LCY Bonds (US\$ billion)			KOSPI	KOSDAQ	
1. Korea Land & Housing Corp.	55,277	51.8	Yes	No	No	No	Real Estate
2. Korea Housing Finance Corp.	36,190	33.9	Yes	No	No	No	Financial
3. Industrial Bank of Korea	30,715	28.8	Yes	No	Yes	No	Bank
4. Korea Finance Corp.	29,430	27.6	Yes	No	No	No	Financial
5. Korea Highway	24,580	23.0	Yes	No	No	No	Infrastructure
6. Korea Deposit Insurance Corp.	24,520	23.0	Yes	No	No	No	Insurance
7. Kookmin Bank	22,508	21.1	No	Yes	No	No	Bank
8. Korea Electric Power Corp.	22,200	20.8	Yes	No	Yes	No	Utility
9. Daewoo Securities	20,515	19.2	Yes	No	Yes	No	Securities
10. Shinhan Bank	19,677	18.4	No	Yes	No	No	Bank
11. Woori Bank	17,732	16.6	Yes	No	No	No	Bank
12. Woori Investment and Securities	16,666	15.6	Yes	No	Yes	No	Securities
13. Hana Bank	14,819	13.9	No	Yes	No	No	Bank
14. Small & Medium Business Corp.	14,603	13.7	Yes	No	No	No	Financial
15. Korea Investment and Securities	13,732	12.9	No	Yes	No	No	Securities
16. Nonghyup (National Agricultural Cooperative Federation)	12,850	12.0	Yes	No	No	No	Bank
17. Korea Rail Network Authority	12,325	11.5	Yes	No	No	No	Infrastructure
18. Tong Yang Securities	10,861	10.2	No	Yes	Yes	No	Securities
19. Korea Gas Corp.	10,580	9.9	Yes	No	Yes	No	Utility
20. Mirae Asset Securities	9,842	9.2	No	Yes	Yes	No	Securities
21. Hyundai Securities	9,470	8.9	No	Yes	Yes	No	Securities
22. Shinhan Card	9,329	8.7	No	Yes	No	No	Financial
23. Hyundai Capital Services	7,400	6.9	No	Yes	No	No	Securities
24. Standard Chartered First Bank Korea	7,060	6.6	No	Yes	No	No	Bank
25. Shinhan Financial Group	7,050	6.6	No	Yes	Yes	No	Financial
26. Hana Daetoo Securities	6,849	6.4	No	Yes	No	No	Securities
27. Korea Railroad Corp.	6,840	6.4	Yes	No	No	No	Infrastructure
28. Korea Water Resources	6,814	6.4	Yes	No	Yes	No	Utility
29. Korea Eximbank	6,430	6.0	Yes	No	No	No	Bank
30. KB Kookmin Card	6,190	5.8	No	Yes	No	No	Financial
31. SH Corp.	6,058	5.7	No	Yes	No	No	Manufacturing
32. Hyundai Card	5,640	5.3	No	Yes	No	No	Financial
33. Samsung Securities	5,421	5.1	No	Yes	Yes	No	Securities
34. Kiwoom Securities	5,316	5.0	No	Yes	Yes	No	Securities
35. Shinhan Investment Corp.	5,227	4.9	No	Yes	No	No	Securities
36. Korea Student Aid Foundation	4,870	4.6	Yes	No	No	No	Education
37. KT Corp.	4,740	4.4	No	Yes	Yes	No	Telecoms
38. Dongbu Securities	4,532	4.2	No	Yes	Yes	No	Securities
39. Samsung Card	4,280	4.0	No	Yes	Yes	No	Financial
40. Incheon Urban Development Corp.	4,258	4.0	Yes	No	No	No	Infrastructure
41. Korea Exchange Bank	3,950	3.7	No	Yes	Yes	No	Bank
42. Korea Hydro & Nuclear Power	3,730	3.5	Yes	No	No	No	Utility
43. Woori Financial Group	3,660	3.4	Yes	No	Yes	No	Financial
44. Hana Financial Group	3,640	3.4	No	Yes	Yes	No	Financial
45. GS Caltex Corp.	3,460	3.2	No	Yes	No	No	Utility
46. Posco	3,300	3.1	No	Yes	Yes	No	Manufacturing
47. Korean Air Lines	3,270	3.1	No	Yes	Yes	No	Air transport

continued on next page

Table 2 continued

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed In		Type of Industry
	LCY Bonds (KRW billion)	LCY Bonds (US\$ billion)			KOSPI	KOSDAQ	
48. National Federation of Fisheries Cooperatives	3,195	3.0	Yes	No	No	No	Financial
49. Kyobo Securities	3,181	3.0	No	Yes	Yes	No	Securities
50. Shinyoung Securities	3,049	2.9	No	Yes	Yes	No	Securities
Total Top 50 LCY Corporate Issuers	577,831	541.2					
Total LCY Corporate Bonds	776,440	727.2					
Top 50 as % of Total LCY Corporate Bonds	74.4%	74.4%					

KOSPI = Korea Composite Stock Price Index, KOSDAQ = Korean Securities Dealers Automated Quotations, LCY = local currency.
Source: AsianBondsOnline, EDAILY BondWeb, and Bloomberg LP.

corporate bonds, and special public bonds—by 10.8%, 22.9%, and 1.5%, respectively. On a y-o-y basis, private corporate bond issuance surged 33.8%, whereas issuance of financial debentures and special public bonds fell 28.2% and 14.3%, respectively.

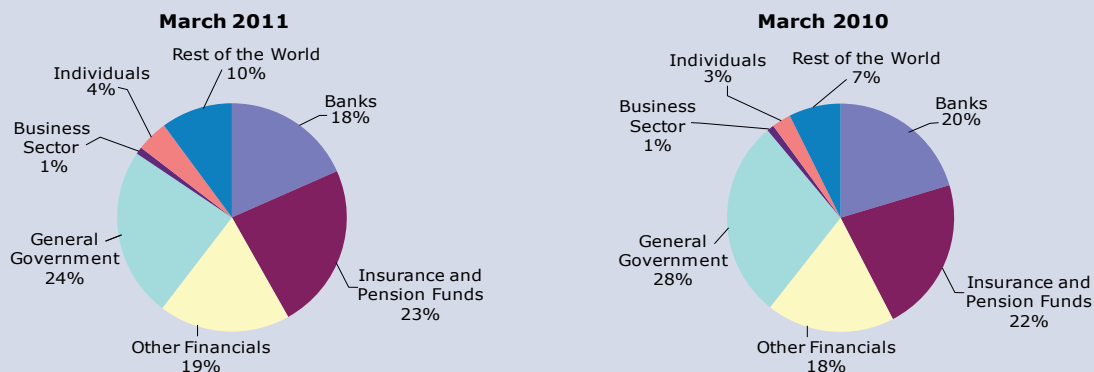
Two of the largest individual LCY corporate bond issues in 1H11 were the Industrial Bank of Korea's KRW550 billion 6-month zero-coupon bond issued in May and Hana Financial Group's KRW520 billion 5-year bond issued in January. The latter bond has a coupon rate of 4.78%.

Investor Profile

As of end-March, the Republic of Korea's general government—which comprises the central government, local government, and social security

funds—remained the largest investor in LCY government bonds with a 24% share (**Figure 2**). The general government was closely followed by insurance companies and pension funds, which held 23% of the total. Between March 2010 and March 2011, the share of the general government's holdings declined 4 percentage points, while the share of insurance companies and pension funds increased 1 percentage point. The largest share increase during this period came from foreign investors, which held 10% of total government bonds at end-March, a y-o-y increase of 3 percentage points. Between March 2010 and March 2011, the shares of local individual investors and other financial institutions (financial institutions other than banks, insurance firms, and pension funds) rose 1 percentage point each, whereas the share of banks dropped 2 percentage points.

Figure 2: LCY Government Bonds Investor Profile



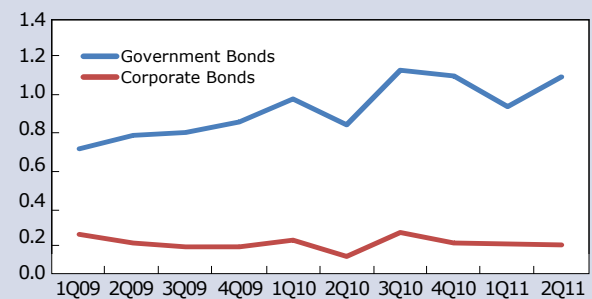
LCY = local currency.
Source: The Bank of Korea.

Insurance firms and pension funds surpassed other financial institutions as the largest holder of LCY corporate bonds at the end of March (**Figure 3**). Between March 2010 and March 2011, the share of corporate bonds held by insurance firms and pension funds climbed from 29% to 32%, while that of other financial institutions remained steady at 30%. Also, the respective shares of the general government and local individual investors increased 1 percentage point each, whereas the share of banks fell 5 percentage points over the same period.

Liquidity

Liquidity in the LCY government bond market improved in recent quarters, but it has remained stagnant in the LCY corporate bond market (**Figure 4**). The turnover ratio for government bonds rose sharply to 1.15 in 2Q11 from 0.97 in 1Q11 as the trading of MSBs and central government bonds—particularly KTBs—increased during this period. For example, the turnover ratio for central government bonds climbed from 0.98 in the previous quarter to 1.21 in 2Q11, reflecting a rebound in central government bond market liquidity following a downward trend in 4Q10 and 1Q11. Similarly, the bid-ask spreads for both KTBs and MSBs narrowed in January–June (**Figure 5**), highlighting improved liquidity for both of these government bond instruments.

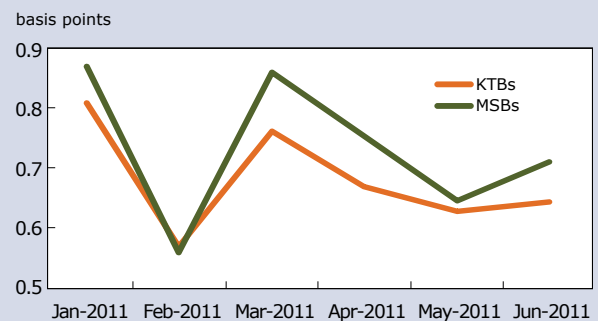
Figure 4: Turnover Ratio for Government and Corporate Bonds, 1Q09–2Q11



LCY = local currency.

Source: The Bank of Korea and EDAILY BondWeb.

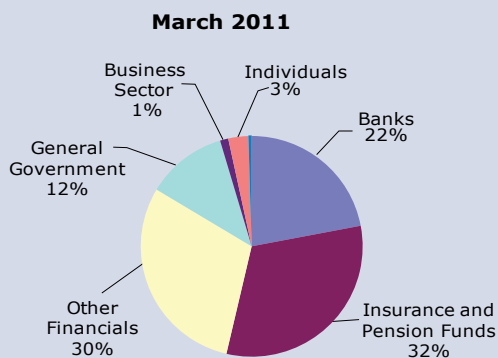
Figure 5: Bid-Ask Spreads for Government Bonds, January–June 2011



LCY = local currency, KTBs = Korea Treasury Bonds, MSBs = Monetary Stabilization Bonds.

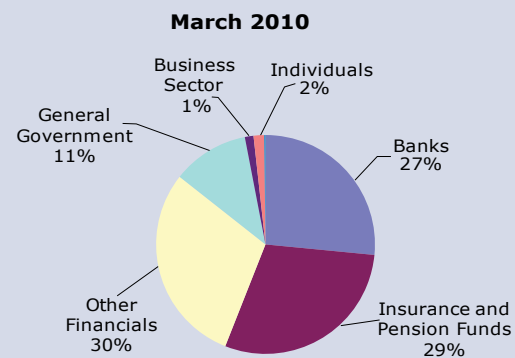
Source: EDAILY BondWeb.

Figure 3: LCY Corporate Bonds Investor Profile



LCY = local currency.

Source: AsianBondsOnline, The Bank of Korea.



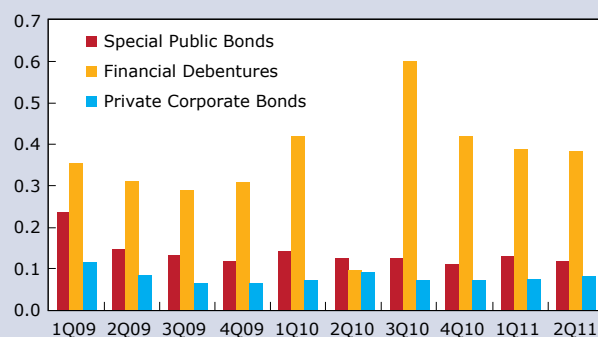
On the other hand, the turnover ratio for corporate bonds remained flat at 0.18 between 4Q10 and the end of 2Q11. Financial debentures were still the most liquid of all types of corporate bonds with a turnover ratio of 0.38 in 2Q11, followed by special public bonds (0.12) and private corporate bonds (0.08) (**Figure 6**). In 2Q11, the turnover trends for corporate bonds were marginal and mixed—rising 0.01 point for private corporate bonds and falling 0.01 point for both financial debentures and special public bonds.

The trading activity of 3-year KTB futures was relatively buoyant in 1Q11, as the number of traded contracts for this type of derivative totaled 8.1 million, which is slightly lower than the record-high of 8.4 million in 1Q11 (**Figure 7**). In the first 5 months of the year, the number of 3-year KTB futures contracts traded reached 12.8 million, up 24.0% y-o-y. The largest investor group in 3-year KTB futures was securities and futures companies, which sold 55.3% of all contracts during the first 5 months of the year, while the second largest was banks, which sold 24.3% of the total in the same period.

Rating Changes

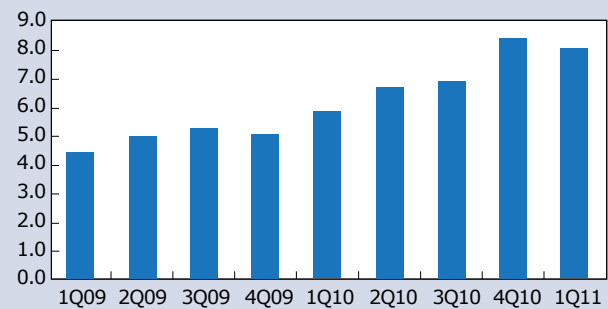
In May, Rating and Investment Information (R&I) affirmed its foreign currency issuer rating and LCY issuer rating for the Republic of Korea

Figure 6: Turnover Ratio for Major Types of LCY Corporate Bonds, 1Q09–2Q11



LCY = local currency.
Note: Financial debentures exclude Korea Development Bank.
Source: EDAILY BondWeb.

Figure 7: Trading Volume of 3-Year KTB Futures, 1Q09–1Q11 (millions of contracts traded)



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

at A+ and AA-, respectively, and maintained its stable outlook for the country (**Table 3**). In affirming its ratings, R&I noted the country's "economic strength" on the back of more than 6% growth in 2010 and expected growth of more than 4% in 2011. It also attributed its ratings to the country's "prudent fiscal management" and current account surplus.

Table 3: Selected Sovereign Ratings and Outlook for the Republic of Korea

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

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

Policy, Institutional, and Regulatory Developments

Investment of Foreign Exchange Agencies in Domestic Foreign Currency-Denominated Bonds Restricted

The Bank of Korea restricted foreign exchange agencies' investments in foreign currency-denominated bonds issued domestically for Korean won financing, effective 25 July. This change was made in light of the Bank of Korea's

new measures to enhance regulations on foreign currency-denominated loans implemented in July 2010, requiring these loans to be used for overseas purposes only. The Bank of Korea has noted that domestic foreign currency-denominated bond issuance by local enterprises has increased recently, with issuers converting 70% of their proceeds into the Korean won.

Measures on Household Debt Announced

The Financial Services Commission (FSC) and the Financial Supervisory Service (FSS) announced a set of comprehensive measures in June to improve the growth and soundness of household debt, provide better credit access to low-income households, and enhance consumer protection. The household debt measures, which are intended for implementation in the second half of the year, include (i) applying higher Bank for International Settlements (BIS) risk weights on banks' high-risk mortgage loans, (ii) introducing leverage regulations covering credit companies, (iii) widening the accessibility of microcredit programs, and (iv) promoting banks' issuance of covered bonds and mortgage-backed securities (MBSs).

Guidelines on Covered Bond Issuance Released

In June, the FSC and the FSS jointly released guidelines on covered bond issuance, including the definition of covered bonds as well as the requirements for their issuance and cover assets. The guidelines specify that the eligible issuers of covered bonds are banks with more than a 10% BIS ratio, or securitization entities established by such banks. Furthermore, the issuance amount must not be greater than 4% of the issuer's total liabilities and the maturity profile must be between 1 and 30 years. Finally, the cover assets must comprise certain mortgage loans and MBSs issued by the Korea Housing Finance Corporation.

Revision on Loan-Loss Requirements for Credit Card Assets

The FSC revised its regulations on loan-loss requirements for credit card assets in June with the aim of strengthening the ability of credit card companies to absorb losses and mitigate excessive competition in the credit card debt market. Specifically, the FSC raised the loan-loss provisioning ratio for sales on credit and credit card debt for most loan classification types—particularly precautionary, substandard, and doubtful loans.

Preliminary Primary Dealer System Launched

The government launched its preliminary primary dealer (PPD) system in March in order to enhance the market-making primary dealer system and help further the development of the KTB market. In April, the government appointed two foreign banks—ING CB Seoul and Credit Agricole CIB Seoul—as PPDs in the domestic bond market. PPDs can participate in KTB auctions and conduct market-making obligations, but receive fewer incentives than primary dealers.

Malaysia—Update

Yield Movements

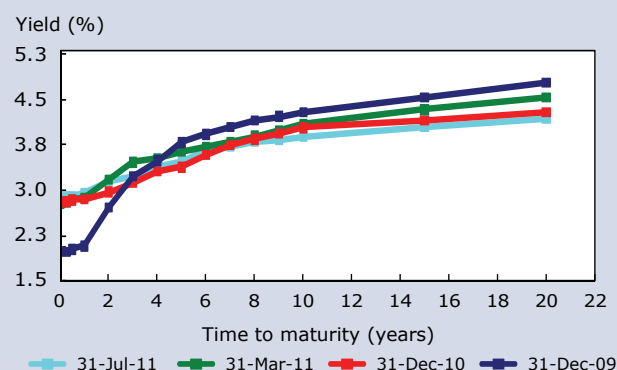
The yield curve for Malaysian government bonds flattened between end-March and end-July, with rates rising on the very short-end of the curve and falling from the belly to the long-end (**Figure 1**). Movement at the very short-end of the yield curve, which rose between 7 basis points (bps) and 14 bps, reflected rising inflation. Yields at the belly to the long-end of the curve fell between 2 bps and 36 bps. As a result, the yield spread between 2- and 10-year maturities narrowed to 72 bps at end-July from 92 bps at end-March and 106 bps at end-December 2010.

Bank Negara Malaysia (BNM) decided to keep its key policy rate steady at 3.0%, but increased the statutory reserve requirement ratio 100 bps during its last Monetary Policy Committee meeting on 7 July. BNM has increased the statutory reserve requirement ratio a total of 300 bps to 4.0% since the start of the year.

In June, consumer price inflation in Malaysia rose to 3.5% year-on-year (y-o-y) from 3.3% in May and 3.2% in April. During the first 6 months of 2011, the consumer price index increased 3.0%, driven mainly by the rise in the cost of food and transportation.

Malaysia's economic growth eased slightly to 4.6% y-o-y during 1Q11 from 4.8% in the previous quarter. Robust growth in domestic demand cushioned a decline in net export growth. Domestic demand increased 6.6% y-o-y in 1Q11, driven by strong private sector consumer spending and public consumption, which rose 6.7% and 6.1% y-o-y, respectively. Meanwhile, gross fixed capital formation expanded 6.5% y-o-y in 1Q11. Exports posted 3.7% growth in 1Q11, up from 1.7% in the previous quarter but significantly lower than the 9.9% growth for full-year 2010. Imports increased 8.4% y-o-y, driven by stronger demand for intermediate, capital, and consumer goods. Amid lingering uncertainty over the condition of the global economy, the Malaysian government

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



LCY = local currency.
Source: Bloomberg LP.

expects the domestic economy to grow 5.0%–6.0% in 2011 on the back of a sustained increase in domestic consumption.

Size and Composition

As of end-June, the total amount of outstanding local currency (LCY) bonds had increased 16.7% y-o-y to MYR812.2 billion (US\$269 billion), driven by double-digit growth in both LCY government and corporate bonds (**Table 1**). Outstanding LCY government bonds expanded 20.9% y-o-y to MYR484.9 billion, with outstanding central bank bills surging 57.0%. Excluding central bank bills, outstanding LCY government bonds rose a more modest 13.4% y-o-y. Meanwhile, outstanding LCY corporate bonds increased 11.1% y-o-y.

On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding increased 3.7% in 1Q11, as LCY government and corporate bonds grew 2.9% and 4.9% q-o-q, respectively.

During the first half of 2011, issuance of government bonds—Malaysian Government Securities (MGS) and Government Investment Issues (GII)—surged 60.6% to MYR53.0 billion from MYR33.0 billion in the same period last year. The increase in issuance

	Amount (billion)										Growth Rate (%)					
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11		May-11		Jun-11	
	MYR	US\$	MYR	US\$	MYR	US\$	MYR	US\$	y-o-y	q-o-q	m-o-m	y-o-y	m-o-m	y-o-y	q-o-q	m-o-m
Total		783	259	794	268	797	265	812	269	20.9	3.7	1.4	0.3	16.7	3.7	1.9
Government		471	156	481	162	481	160	485	161	30.1	5.8	2.0	0.0	20.9	2.9	0.9
Central Government Bonds		371	123	365	123	372	124	376	125	13.2	7.0	(1.8)	2.1	13.5	1.3	1.1
Central Bank Bills		100	33	116	39	108	36	108	36	206.9	2.0	16.1	(6.4)	57.0	8.8	0.1
Others		0	0	0	0	0	0	0	0	(73.0)	(52.1)	0.0	0.0	(52.1)	0.0	0.0
Corporate		312	103	314	106	316	105	327	108	9.2	0.7	0.6	0.7	11.1	4.9	3.5

Notes:

2. Bloomberg LP end-of-period LCY—US\$ rate is used.

4. "Others" refers to Khazars

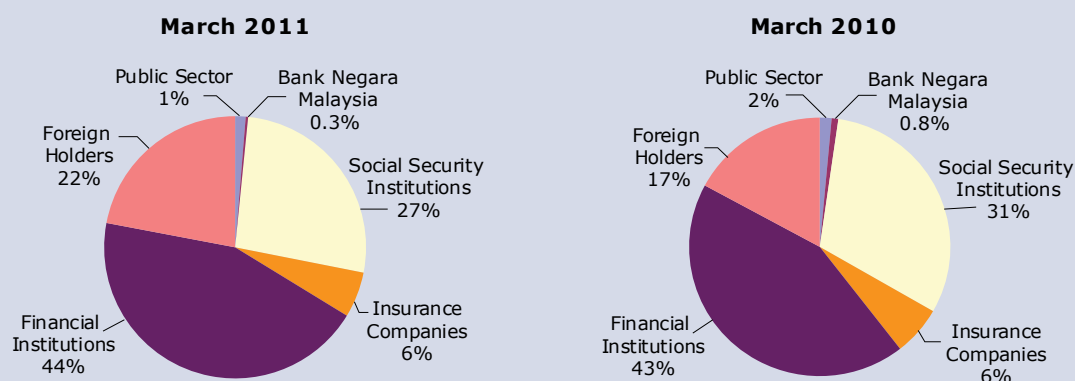
Source: Bank Negara Malaysia, Fully Automated System for Issuing/Tendering (FAST), and Bloomberg LP. Issued by Cagamas Berhad.

As of end-March, financial institutions were still the largest holders of MGS and GII, with 44.2% of total outstanding government bonds, followed by social security institutions, which held 26.5%. Insurance companies comprised 5.6% of the total **(Figure 2)**. Meanwhile, foreign investors held 22.0%, up slightly from a 21.5% share at the end of 2010, partly due to expectations of further appreciation of the Malaysian ringgit. Partly as a result of the appreciation of the ringgit since mid-2009, foreign holdings of Malaysian government bonds have risen from a low of 10.0% at end-June 2009 to 22.0% at end-March 2011 **(Figure 3)**.

Table 2: Top 20 Corporate Issuers in Malaysia (as of June 2011)

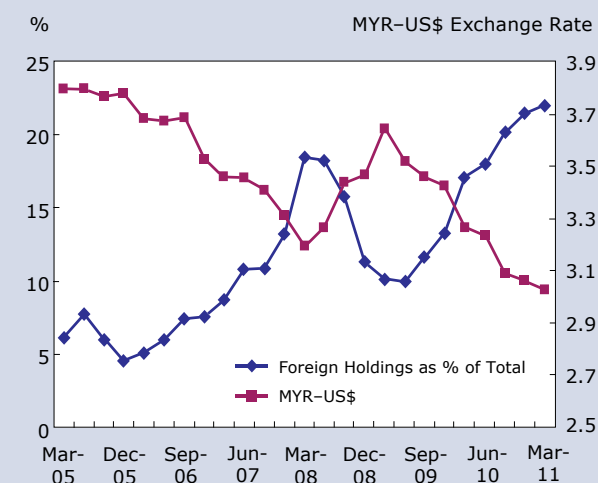
Issuers	Outstanding Amount (MYR billion)					State-Owned	Privately-Owned	Listed Company	Type of Industry
	BONDS	IBONDS	MTN	IMTN	TOTAL				
1. Cagamas			9.42	9.70	19.12	Yes	No	No	Finance
2. Khazanah		13.20			13.20	Yes	No	No	Quasi-Govt. and Other
3. Binariang GSM		3.02		8.28	11.30	No	Yes	No	Transport, Storage, and Comm.
4. Pengurusan Air SPV				10.65	10.65	Yes	No	No	Utilities
5. Project Lebuhraya		5.82		3.68	9.50	No	Yes	Yes	Transport, Storage, and Comm.
6. Prasarana	5.10	2.00		2.00	9.10	Yes	No	No	Finance
7. Maybank	6.10	1.50			7.60	No	Yes	Yes	Finance
8. Malakoff Corp		1.70		5.60	7.30	No	Yes	No	Finance
9. KL International Airport	1.60	4.26			5.86	Yes	No	No	Transport, Storage, and Comm.
10. Rantau Abang Capital Bhd				5.80	5.80	No	Yes	No	Quasi-Govt. and Other
11. Senai Desaru Expressway Bhd				5.58	5.58	No	Yes	No	Construction
12. CIMB Bank	5.50				5.50	No	Yes	No	Finance
13. Valuecap	5.10				5.10	Yes	No	No	Finance
14. 1Malaysia Development				5.00	5.00	Yes	No	No	Finance
15. AMBank	0.49		4.48		4.96	No	Yes	Yes	Finance
16. Jimah Energy Ventures				4.54	4.54	No	Yes	No	Utilities
17. Putrajaya Holdings		0.67		3.78	4.45	Yes	No	No	Finance
18. Bank Pembangunan Malaysia	1.00		2.40	0.90	4.30	Yes	No	No	Finance
19. Celcom Transmission				4.20	4.20	No	Yes	No	Transport, Storage, and Comm.
20. Tanjung Bin Power				4.07	4.07	No	Yes	No	Utilities
Total Top 20 LCY Corporate Issuers					147.12				
Total LCY Corporate Bonds					327.30				
Top 20 as % of Total LCY Corporate Bond Outstanding					45.0%				

IBONDS = Islamic bonds, IMTN = Islamic medium-term notes, LCY = local currency, MTN = medium-term notes.
Source: Bank Negara Malaysia, Fully Automated System for Issuing/Tendering (FAST).

Figure 2: LCY Government Bond Market Investor Profile

LCY = local currency.
Source: Bank Negara Malaysia.

Figure 3: Foreign Holdings of LCY Government Bonds vs. the MYR-US\$ Exchange Rate, 2005–2011



LCY = local currency.
Source: Bank Negara Malaysia and Bloomberg LP.

Rating Changes

In July, Standard & Poor's (S&P) lowered Malaysia's LCY long-term sovereign credit rating from A+ to A with a stable outlook following the implementation of a revised methodology and assumptions for sovereign ratings. According to S&P, the gap between LCY and foreign currency (FCY) ratings narrowed on most sovereigns under the revised methodology. Meanwhile, S&P affirmed Malaysia's LCY short-term rating at A-1 as well as the FCY short- and long-term ratings at A-2 and A-, respectively. S&P also noted that despite the forecast of 5.2% economic growth in 2011, the country is experiencing slow fiscal consolidation as a result of rising government subsidies (**Table 3**).

Table 3: Selected Sovereign Ratings and Outlook for Malaysia

	Moody's	S&P	Fitch
Sovereign LCY LT Rating	A3	A	A
Outlook	stable	stable	stable
Sovereign FCY LT Rating	A3	A-	A-
Outlook	stable	stable	stable

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

Policy, Institutional, and Regulatory Developments

SC Issues Guidelines on the Registration of Credit Rating Agencies

In March, the Securities Commission (SC) in Malaysia issued guidelines on the registration of credit rating agencies. The guidelines are meant to enhance the agencies' standards in key areas such as the transparency of rating criteria, objectivity of the rating process, and management of conflicts of interest. The new guidelines set out the regulatory and supervisory requirements for rating agencies and supersede the Practice Note on Recognition of Credit Rating Agencies for the Purpose of Rating Bond Issue that was issued by the SC in January 2006.

Among the provisions in the new guidelines is the requirement that the rating agencies maintain a minimum of MYR1 million of shareholders' funds unimpaired by losses. The agencies are required to develop rating criteria and methodologies appropriate for each type of bond and industry, and to publish these before any rating is assigned to a bond issue. The credit rating agencies are also required to conduct timely and regular rating reviews of outstanding bonds, and regularly publish these rating reviews and reports.

SC Launches New Capital Market Masterplan

In April, the SC launched the Capital Market Masterplan 2 (CMP2), a continuation of the previous Capital Market Masterplan, in an effort to expand the role of domestic capital markets in financing economic growth. The CMP2 aims to provide market participants a clear understanding of the government's long-term strategies for the development of Malaysia's capital markets, including

- (i) promoting capital formation,
- (ii) expanding intermediation efficiency and scope,
- (iii) deepening liquidity and risk intermediation,

- (iv) facilitating internationalization, and
- (v) building capacity and strengthening information infrastructure.

The CMP2 cites the need to increase the capacity of the bond market to finance a wider base of industries and projects, as well as more sophisticated ventures. To this end, the CMP2 has articulated strategies that include

- (i) strengthening disclosure and documentation standards and practices,
- (ii) enhancing the credit rating agency regulatory framework,
- (iii) reviewing the bond default process and promoting an active market for pricing distressed issues,
- (iv) expanding participation of the investment management industry in the bond market,
- (v) strengthening bond trading and post-trade infrastructure,
- (vi) facilitating greater retail participation in the bond market, and
- (vii) expanding the range of fixed-income products.

The CMP2 also outlines governance strategies to ensure investor protection and stability.

BNM Liberalizes Rules on Direct Investment Abroad

BNM announced new measures in May to liberalize regulations on residents directly investing abroad and on inter-company loans and trade financing. Effective 1 June, the measures allow resident companies that meet prudential requirements to undertake any amount of direct investments abroad, effectively exempting them from the prevailing MYR50 million limit on investment in FCY assets. Resident companies will also be allowed to borrow any amount, in either ringgit or FCY, from non-bank related companies.

BNM also lifted the MYR5 million limit on offshore FCY trade financing. Residents may now borrow offshore, including for FCY trade financing, up to an existing aggregate limit of MYR10 million for individuals and MYR100 million for companies.

BNM Issues New Islamic Monetary Instrument

BNM began issuing a new Islamic monetary instrument in June called BNM Monetary Notes–*Istithmar*. The notes are based on the *istithmar* (investment) concept, which refers to a portfolio structure combining the principles of *ijarah* (sale and lease-back of assets) and *murabahah* (commodity mark-up sale transaction).

SC Issues Revised Guidelines for Corporate Bonds and Sukuk

In July, the SC issued revised guidelines for private debt securities and *sukuk* in line with the broader objectives of the CMP2. The revised guidelines will replace the earlier Guidelines on Offering Private Debt Securities and Guidelines on the Offering of Islamic Securities, both of which were issued in July 2004. The revised guidelines streamline the approval process and time-to-market for the issuance of corporate bonds and *sukuk*. The revised guidelines also remove the mandatory rating requirement for selected issues or offers, and provide greater disclosure of relevant information for debenture holders. The revised Islamic Security Guidelines provide greater clarity to ensure compliance with *sharia'h* (Islamic law) rulings and principles endorsed by the *Sharia'h* Advisory Council of the SC.

Philippines—Update

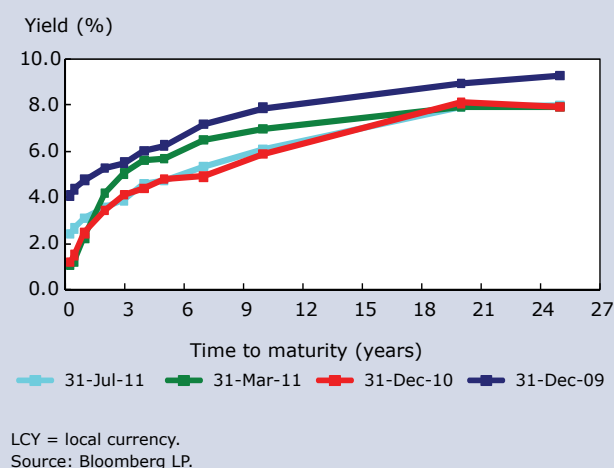
Yield Movements

Yields in the belly of the Philippine government bond yield curve rose between end-December 2010 and end-March on the back of inflationary concerns and monetary tightening (**Figure 1**). The curve then flattened between end-March and end-July as yields at the short-end rose and yields in the belly of the curve fell. During this period, yields for 3- and 6-month tenors rose 139 basis points (bps) and 143 bps, respectively, while yields for 1-, 20-, and 25-year tenors rose 83 bps, 3 bps, and 7 bps, respectively. Yields in the belly of the curve fell between 61 bps and 117 bps from end-March to end-July. Yield spreads between 2- and 10-year tenors narrowed to 250 bps in July from 280 bps in March after a 90 bps drop in the 10-year yield. Overall, the Philippine yield curve flattened between end-December 2010 and end-July.

Consumer price inflation accelerated in 2Q11, rising to 4.6% year-on-year (y-o-y) in June from 4.5% in May, based on National Statistics Office (NSO) inflation series data from 2000. The NSO's more recent 2006-based data reflected higher inflation rates in both June (5.2%) and May (5.0%). Year-to-date inflation levels through June were 4.3% using the 2000-based data and 4.7% using the 2006-based data. Both rates fall within the government's target range of 3%–5% for full-year 2011.

Rising commodity prices have emerged as a threat to the price stability objective of the Bangko Sentral ng Pilipinas (BSP), which has tried to contain the secondary effects of inflation by maintaining a relatively hawkish policy stance. BSP raised both of its policy rates 25 bps following Monetary Board meetings in March and again in May. BSP's overnight borrowing facility stands at 4.5%, while the overnight lending facility is 6.5%. In its June and July meetings, BSP kept its policy rates steady but followed steps taken by its Asian counterparts in hiking the reserve requirement by 100 bps each. Given the possibility that the current inflation trend might exceed BSP's annual target, the central bank

Figure 1: Philippines' Benchmark Yield Curve—LCY Government Bonds



has said it will remain vigilant for any potential build up of inflationary expectations and is ready to tighten monetary policy as needed.

Gross domestic product (GDP) growth in the Philippines fell to 4.9% y-o-y in 1Q11 from 6.1% in 4Q10, based on 2000 price levels. (Until 2011, the National Statistical Coordination Board [NCSB] had used 1986 as its base year.) Reduced government spending, slowing exports, and consumption weakened by escalating consumer prices contributed to lower GDP growth in 1Q11.

Size and Composition

The local currency (LCY) bond market continued to grow modestly in the first half of 2011. Growth in the issuance of treasury and corporate bonds overshadowed the contraction in treasury bills and other government debt issuances, resulting in the continued overall expansion of the Philippine LCY bond market.

Total LCY bonds outstanding rose to PHP3.26 trillion (US\$75.1 billion) at end-June, up 6.0% y-o-y (**Table 1**). On a quarter-on-quarter (q-o-q) basis, LCY bonds increased 3.1% on the back of 4.6%

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

	Amount (billion)						Growth Rate (%)					
	Mar-11		Apr-11		May-11		Mar-11		Apr-11		May-11	
	PHP	US\$	PHP	US\$	PHP	US\$	y-o-y	q-o-q	m-o-m	y-o-y	q-o-q	m-o-m
Total	3,160	73	3,161	74	3,222	75	5.7	(0.7)	(0.2)	1.9	6.0	3.1
Government	2,758	64	2,774	65	2,825	65	4.5	(2.1)	0.6	1.8	5.4	3.0
Treasury Bills	400	9	385	9	385	9	(31.0)	(24.2)	(3.6)	0.1	(32.8)	0.0
Treasury Bonds	2,236	52	2,269	53	2,320	54	14.8	3.5	1.5	2.2	17.2	4.6
Others	122	3	119	3	119	3	9.5	(6.7)	(2.7)	0.0	(9.7)	0.0
Corporate	402	9	387	9	397	9	14.4	10.7	(5.1)	2.6	10.9	5.0

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 end-of-period LCY-US\$ 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 National Power Corporation and Power Sector Assets and Liabilities Management.

Source: Philippine Bureau of the Treasury and Bloomberg LP.

and 3.6% growth in treasury bonds and corporate bonds, respectively. Treasury bonds surged to PHP2.34 trillion at end-June, a 17.2% y-o-y increase. Corporate debt expanded 10.9% y-o-y to close out the first half of the year at PHP417 billion.

Government securities still dominated the Philippine LCY bond market in 2Q11, but the share of treasury bills notably decreased while treasury bonds gained as a result of the government's policies of fiscal consolidation and debt maturity restructuring. Treasury bills outstanding shrank to PHP400 billion in March, a decline of 31.0% y-o-y, and fell further to PHP381 billion in June, a 32.8% y-o-y decline.

Corporate and government issuance in 1H11 supported growth in the LCY bond market. Retail treasury bonds (5- and 10-year tenors) totaled almost PHP104 billion in March, representing the most significant government borrowing in 1H11. Meanwhile, corporate issuance was led by Ayala Land Inc. (January) and Ayala Corporation (May), which each sold PHP10 billion worth of bonds. Two companies owned by retail industry leader Henry Sy, Banco de Oro Unibank, and SM Investments, sold bonds worth PHP8.5 billion in June and PHP7.0 billion in February, respectively.

Corporate Bond Market Development

Total outstanding LCY corporate bonds stood at PHP417 billion at end-June. In total, there were less than 50 firms with corporate bonds outstanding, while the top 30 issuers accounted for more than 93% of the total. Among the top issuers, 28 were listed companies on the Philippine Stock Exchange, suggesting that it is easier for listed companies to borrow publicly due to greater financial and operating transparency. San Miguel Brewery led the roster of borrowers with PHP38.8 billion of issued debt. Banco de Oro Unibank was the second-largest with PHP36.5 billion and Ayala Corporation was next with PHP26.0 billion (**Table 2**).

A plurality of the top 30 bond issuers were banks (34%), followed by real estate developers and operators (14%), holding companies (13%),

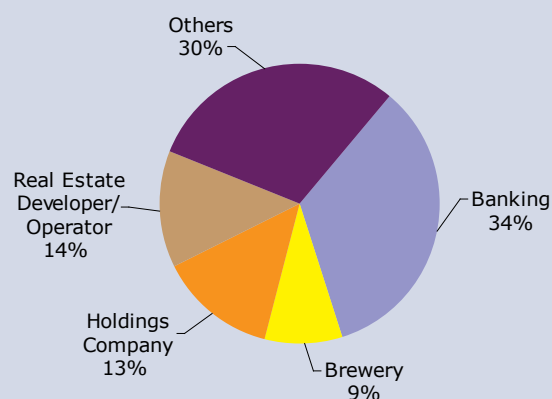
Table 2: Top 30 Issuers of LCY Corporate Bonds in the Philippines (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (PHP billion)	LCY Bonds (US\$ billion)				
1. San Miguel Brewery, Inc.	38.80	0.89	No	Yes	Yes	Brewery
2. Banco De Oro Unibank, Inc.	36.50	0.84	No	Yes	Yes	Banking
3. Ayala Corporation	26.00	0.60	No	Yes	Yes	Diversified Operations
4. Philippine National Bank	21.25	0.49	No	Yes	Yes	Banking
5. Rizal Commercial Banking Corporation	21.00	0.48	No	Yes	Yes	Banking
6. Manila Electric Company	18.84	0.43	No	Yes	Yes	Electric-Distribution
7. Metropolitan Bank & Trust Company	18.50	0.43	No	Yes	Yes	Banking
8. Ayala Land, Inc.	17.34	0.40	No	Yes	Yes	Real Estate Developer/Operator
9. SM Investments Corporation	16.40	0.38	No	Yes	Yes	Diversified Operations
10. Petron Corporation	16.30	0.38	No	Yes	Yes	Oil Refining & Marketing
11. Robinsons Land Corporation	15.00	0.35	No	Yes	Yes	Real Estate Developer/Operator
12. JG Summit Holdings, Inc.	13.31	0.31	No	Yes	Yes	Diversified Operations
13. Globe Telecom, Inc.	12.72	0.29	No	Yes	Yes	Telecom Services
14. Philippine Long Distance Telephone Co.	12.50	0.29	No	Yes	Yes	Telephone-Integrated
15. Energy Development Corporation	12.00	0.28	No	Yes	Yes	Electric-Generation
16. Bank of the Philippine Islands	10.00	0.23	No	Yes	Yes	Banking
17. SM Development Corporation	10.00	0.23	No	Yes	Yes	Real Estate Developer/Operator
18. First Philippine Holdings Corporation	8.49	0.20	No	Yes	Yes	Electric-Integrated
19. Allied Banking Corporation	8.00	0.18	No	Yes	Yes	Banking
20. Aboitiz Power Corporation	6.88	0.16	No	Yes	Yes	Electric-Generation
21. Megaworld Corporation	6.38	0.15	No	Yes	Yes	Real Estate Developer/Operator
22. Metrobank Card Corporation	6.30	0.15	No	Yes	Yes	Diversified Financial Services
23. Manila North Tollways Corporation	5.28	0.12	No	Yes	No	Public Thoroughfares
24. China Banking Corporation	5.00	0.12	No	Yes	Yes	Banking
25. Filinvest Land, Inc.	5.00	0.12	No	Yes	Yes	Real Estate Developer/Operator
26. Tanduay Distillers, Inc.	5.00	0.12	No	Yes	No	Beverages-Wines/Spirits
27. United Coconut Planters Bank	4.52	0.10	No	Yes	Yes	Banking
28. Manila Water Company, Inc.	4.00	0.09	No	Yes	Yes	Water Distribution
29. SM Prime Holdings, Inc.	3.99	0.09	No	Yes	Yes	Real Estate Management Services
30. Union Bank of the Philippines, Inc.	3.75	0.09	No	Yes	Yes	Banking
Total Top 30 LCY Corporate Issuers	389.06	8.97				
Total LCY Corporate Bonds Outstanding	417.04	9.61				
Top 30 as % of Total LCY Corporate Bonds Outstanding	93.3%	93.3%				

LCY = local currency.
Source: Bloomberg LP.

and a brewery (9%) (**Figure 2**). Bond sellers from various other industries accounted for the remaining 30%.

Figure 2: LCY Corporate Bond Issuers by Industry
(as of June 2011)



LCY = local currency.
Source: Bloomberg LP.

Foreign Currency Bonds

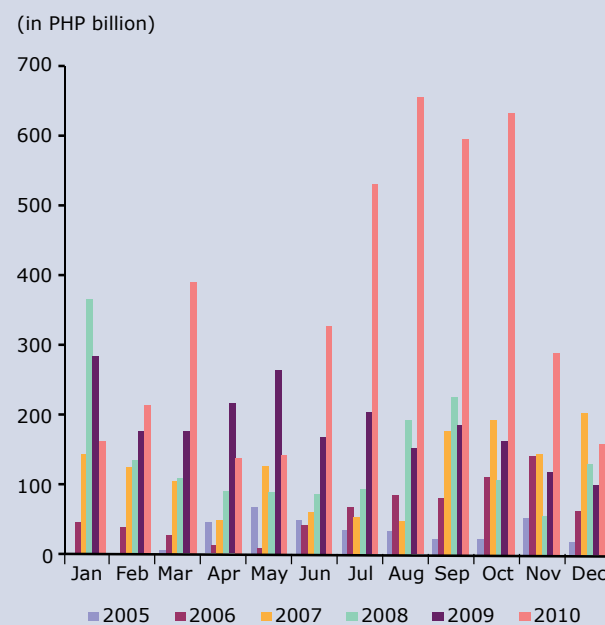
In March, the government sold US\$1.5 billion of 15-year US\$-denominated global bonds with a coupon rate of 5.5%. The sovereign raised US\$2.8 billion from international markets in 1H11, led by a US\$1.3 billion 25-year global peso bond issued in January. The Development Bank of the Philippines (DBP) also sold US\$300 million worth of 10-year bonds at a coupon rate of 5.5%. DBP has a program of foreign borrowing that will reach US\$1.2 billion in 2011.

In May, San Miguel Corporation—a diversified conglomerate with businesses in a number of sectors including food and beverage, power, mining, infrastructure, and telecommunications—sold 3-year US\$600 million exchangeable bonds with a coupon rate of 2.0%. The bonds can be converted into common shares to be sourced from the treasury stock of the company with a 25% premium on the offer price. The bonds are listed on the Singapore Exchange.

Trading Volume Trends

According to the sole fixed-income exchange and reporting platform in the country, PDEX, the liquidity of government securities, particularly Fixed-Rate Treasury Notes (FXTNs), improved dramatically between 2005 and 2010. The trading volume of FXTNs increased by a factor of 12 over this period, from PHP357 billion in 2005 to PHP4.25 trillion in 2010. Monthly trading volume averages rose from PHP 35.7 billion in 2005 to PHP354 billion in 2010. Assuming an average of 20 trading days per month, daily trading volume soared from PHP1.8 billion in 2005 to PHP21.3 billion in 2010. The highest recorded trading volume in a single day was PHP122 billion in October 2010. A number of factors have contributed to the increased trading of government securities including improved transparency in market activities, growing capitalization of the banking system, and improving regional and domestic economic indicators (**Figure 3**).

Figure 3: Fixed-Income Treasury Notes Trading Volume, 2005–2010



Note: PDEX reports one side of trades only.
Source: Philippine Dealing & Exchange Corporation (PDEX).

Bid-Ask Spreads

In 1H11, the bid-ask spreads of the five benchmark bonds were recorded using the data from the four voice brokers operating in the Philippines. The benchmark bonds are FXTN 5-67 (2.6 years remaining until maturity), FXTN 7-48 (4.6 years), FXTN 10-42 (5.2 years), FXTN 10-52 (9.5 years), and FXTN 25-08 (24.5 years). The lowest bid and the highest offer in terms of yield among the brokers at the close of a trading session (as reflected on their Bloomberg pages) are used to construct the market bid-offer spread. The weekly average market bid-offer spreads of the five benchmark bonds are presented in **Figure 4**.

The most that the market bid-offer spread widened in a single week was 37 bps during 17–21 January, when financial institutions began selling government securities as loss-limit stops were hit and inflationary fears signaled the onset of rising interest rates. Spreads narrowed at times in 1H11 on the back of better-than-expected data releases (e.g., a lower government budget deficit), higher liquidity (as reflected in auction tenders that were more than two times oversubscribed), more long-term maturities, and increased foreign and local corporate buying. The tightest weekly average was 8 bps recorded during 21–24 June after Moody's and Fitch upgraded their respective credit ratings for the Philippines, which was

followed by the announcement of the government's debt swap scheduled for early July.

Among the five benchmark bonds, FXTN 25-08 posted the tightest market bid-offer spread with an average of 7.8 bps in 1H11. This was followed by FXTN 5-67 (10.0 bps), FXTN 7-48 (15.3 bps), FXTN 10-42 (16.6 bps), and FXTN 10-52 (33.3 bps).

Rating Changes

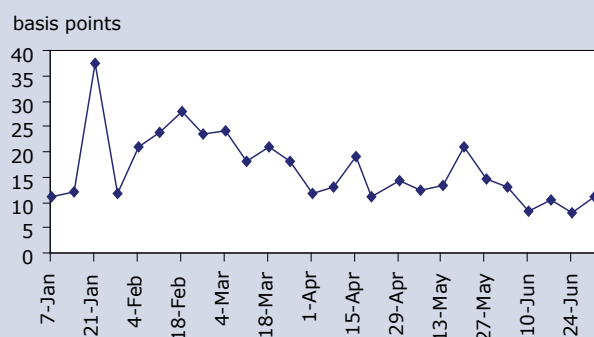
On 14 June, Rating and Investment Information Inc (R&I) affirmed the foreign currency (FCY) long-term bond rating of the government at BBB- with a stable outlook. The country's FCY short-term debt rating of a-2 was also affirmed. R&I highlighted the need to expand the revenue base and upgrade infrastructure conditions. Low public and private investment-to-GDP ratios and high (albeit declining) levels of debt were also factored into the ratings.

On 15 June, Moody's upgraded the FCY and LCY long-term bond ratings on debt issued by the government to Ba2, or two notches below investment grade, with a stable outlook for both. The upgrade was the result of the (i) progress made in fiscal consolidation by the current administration and (ii) sustained nature of macroeconomic stability on the back of a strong external payments position and economic growth.

On 23 June, Fitch Ratings upgraded the Philippines' long-term FCY issuer default rating to BB+ from BB. The long-term LCY issuer default rating and the country ceiling were also upgraded to BBB- from BB+. The outlook for all of these ratings is stable. The short-term FCY rating has been affirmed at B. The rating agency took note of the government's progress on fiscal consolidation, sustained macroeconomic stability and favorable prospects, and improving external finances.

On 29 July, Standard & Poor's (S&P) affirmed its BB/B (FCY) and BB+/B (LCY) sovereign credit ratings for the Philippines. The outlook for both is stable. The ratings reflect strong external liquidity and signs of improving growth prospects balanced

Figure 4: Benchmark Government Securities Bid-Ask Spreads, January–July 2011



Note: 1 basis point = 0.01 percent.
Source: AsianBondsOnline.

against enduring fiscal weakness with high, albeit improving, debt ratios. The stable outlooks reflect S&P's expectation that remittances will continue to drive current account surpluses, while the weak fiscal profile will require more effort to address.

Table 3: Selected Sovereign Ratings and Outlook for the Philippines

	Moody's	S&P	Fitch	R&I
FCY Long-Term Rating	Ba2	BB	BB+	BBB-
Outlook	stable	stable	stable	stable

FCY = foreign currency.
Source: Rating agencies.

Policy, Institutional, and Regulatory Developments

Government Mulls New Global Peso Notes

The Philippine government is planning to issue Global Peso Notes (GPNs) and dollar bonds, possibly in September. The BSP has approved in principle the sale of up to US\$1.5 billion of 15-year GPNs and as much as US\$1.5 billion of new 25-year dollar bonds or the reopening of a US\$1.0 billion bond due in October 2034. GPNs are PHP-denominated bonds that are sold offshore and payable in US dollars to investors. GPNs are tax-exempt. Principal and interest are converted into US dollars for payment. The US\$ equivalent is calculated based on the prevailing PHP-US\$ exchange rate on interest and principal payment dates. Under this scenario, investors bear the currency risk. The Philippines has sold a total of US\$2.25 billion of GPNs in January 2011 and September 2010 (**Table 4**).

Table 4: Philippine Global Peso Notes

Issues	Outstanding Amount (PHP billion)	Coupon (%)	Issue Date	Maturity Date
PHILIP 4.95 21	44.109	4.95	17-Sep-10	15-Jan-21
PHILIP 6.25 36	54.77	6.25	14-Jan-11	14-Jan-36

Source: Bloomberg.

BSP Raises Reserve Requirement Ratio to 21%

On 28 July, BSP raised the statutory reserve requirement for peso deposit liabilities and deposit substitutes of all banks and non-bank financial institutions with quasi-banking functions. The statutory reserves of universal and commercial banks increased from 9% to 10%. Including a liquidity reserve requirement of 11%, the latest adjustment raised the total level of required reserves to 21% from 20%. The reserve requirement hike was a preemptive move to counter inflationary pressures arising from excess liquidity driven by strong capital inflows given the favorable outlook for the Philippine economy. BSP, however, stated that inflation risks were still present and it remains ready to implement measures to ensure price stability.

BTR Conducts Another Domestic Debt Swap

On 13 July, the Bureau of the Treasury (BTR) completed its sixth domestic bond exchange program since 2006. The latest exchange received the highest level of participation to date, with PHP299.4 billion worth of bonds being offered in exchange for new 10.5- and 20-year bonds. On 19 July, BTR issued PHP67.6 billion of 10.5-year and PHP255.8 billion of 20-year bonds—a total of PHP323.4 billion of new benchmark bonds—in exchange for eligible bonds. It was also the first time that bonds were exchanged for 20-year bonds. The 10.5-year bond carries a coupon of 6.375%, while the 20-year coupon is 8.0%. The last debt swap lengthened the average maturity of government bonds outstanding by 2 years. The series of debt exchanges have resulted in fiscal consolidation and a lengthening of the country's debt maturity profile, allowing the government more flexibility in spending on infrastructure, social services, and public works.

BSP Amends Meaning of Qualifying Capital Instruments

BSP adopted the Basel III criteria for inclusion of non-common equity components in banks' capital base when determining capital instruments that can be counted as regulatory capital by Philippine banks, effective 1 January 2011. Basel III states that the majority of the capital base must be in the form of common equity elements and sets out minimum criteria for instruments to qualify in each of the sub-categories of capital. Instruments to be included as capital should not contain conditions that give the issuing bank an incentive to redeem the instrument. These conditions include step-ups of coupon rates on a call or maturity date, rights to accelerate the repayment of future scheduled payments except in liquidation, and a credit-sensitive dividend feature. Repayment of the principal of capital instruments requires prior supervisory approval and banks should not assume or create market expectations that supervisory approval will be given. BSP aims to implement other Basel III guidelines prior to earlier 2015—the year set by the international committee for compliance.

Singapore—Update

Yield Movements

The government bond yield curve for Singapore shifted downward across all maturities between end-December 2010 and end-July (**Figure 1**). Between end-March and end-July, bond yields for longer maturities fell the most, following the Monetary Authority of Singapore's (MAS) announcement of an upward re-centering of its exchange rate policy band in a bid to ease inflationary pressures. Yields fell for the 3- and 12-month tenors by only 2 basis points (bps) and 6 bps, respectively, while yields for the 5-through the 20-year tenor fell between 35 bps and 56 bps. The yield spread between 2- and 10-year maturities narrowed to 184 bps at end-July from a spread of 203 bps at end-March.

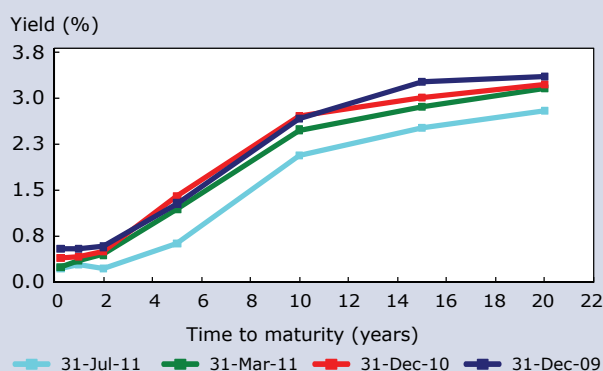
In its semi-annual policy statement on 14 April, MAS announced an upward re-centering of its exchange rate policy band to a level below that of the prevailing Singapore dollar nominal effective exchange rate (S\$NEER). The slope and width of the policy band will remain unchanged. The policy decision, which allows for the further appreciation

of the Singapore dollar, aims to moderate surging prices while protecting the economy's expansion. The move is also in line with MAS' tighter policy stance announced first in October 2010 and again in April.

Consumer price inflation accelerated in January to its highest level since 2008, led by higher prices for transportation, housing, and food. Consumer price inflation climbed to 5.5% year-on-year (y-o-y) in January before leveling off at 5.0% y-o-y in February and March. Consumer price inflation then eased slightly to 4.5% y-o-y in April and held steady at the same level in May before surging to 5.2% y-o-y in June. Inflation stemming from higher oil, labor, and transportation costs remains a potential threat to the economy. MAS expects consumer price inflation to range between 4% and 5% for full-year 2011.

Singapore's gross domestic product (GDP) growth slowed to 0.9% y-o-y in 2Q11, based on the data released by the Ministry of Trade and Industry (MTI), from a rapid expansion of 9.3% in 1Q11. According to MTI, the easing revealed a slowdown in many sectors, particularly manufacturing, which posted a contraction of 5.9% y-o-y following growth of 16.5% in 1Q11. The decline in the manufacturing sector reflected a slump in the production of electronics and pharmaceuticals. Meanwhile, growth in the construction and services sectors in 2Q11 moderated to 1.5% and 3.9% y-o-y, respectively, from 2.4% and 7.6% in 1Q11. The MTI expects Singapore's economy to grow between 5% and 6% in 2011.

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



LCY = local currency.
Source: Bloomberg LP.

Size and Composition

Total local currency (LCY) bonds outstanding in Singapore expanded 18.0% y-o-y in 2Q11 to reach SGD250.5 billion (US\$204 billion) (**Table 1**). This y-o-y growth was driven mainly by Singapore Government Securities (SGS) bonds, which grew 7.5%, and corporate bonds, which grew 33.0%.

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

	Amount (billion)										Growth Rate (%)					
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11		May-11		Jun-11	
	SGD	US\$	SGD	US\$	SGD	US\$	SGD	US\$	SGD	US\$	y-o-y	q-o-q	m-o-m	y-o-y	q-o-q	m-o-m
Total	240	191	245	200	247	200	251	204	204	15.4	4.8	2.1	0.4	18.0	4.3	1.6
Government	133	106	136	111	136	110	139	113	113	5.3	0.8	1.9	-	8.1	3.9	2.0
Bills	58	46	58	47	58	47	58	47	47	12.0	1.4	-	-	9.0	-	-
Bonds	75	60	78	64	78	63	81	66	66	0.7	0.3	3.3	-	7.5	6.9	3.5
Corporate	107	85	110	90	111	90	112	91	91	31.1	10.3	2.4	1.0	33.0	4.7	1.2

- = data not available, 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 *AsianBondsOnline* estimates.

2. Bloomberg LP end-of-period LCY-US\$ rate is used.

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.

3. Growth rates are calculated from ECI base and do not include currency effects.
Source: Monetary Authority of Singapore, Singapore Government Securities, and Bloomberg LP.

On a quarter-on-quarter (q-o-q) basis, growth in total LCY bonds outstanding eased slightly to 4.3% in 2Q11 from 4.8% in 1Q11 due to slower growth in corporate bonds.

The outstanding stock of SGS rose 8.1% y-o-y as of end-June to reach SGD138.5 billion, compared with 5.3% y-o-y growth as of end-March. SGS bills outstanding have remained flat at SGD57.9 billion since January, with y-o-y growth slowing to 9.0% in 2Q11 from 12.0% in 1Q11. Meanwhile, SGS bonds outstanding rose 7.5% y-o-y to SGD80.6 billion in 2Q11, following marginal growth of only 0.7% in 1Q11.

SGS bills comprised 91% of total SGS outstanding at the end of 2Q11. On a q-o-q basis, issuance of SGS bills climbed 7.1% in 2Q11 after declining 5.2% in 1Q11. On a y-o-y basis, however, growth in the issuance of SGS bills slowed to 9.0% in 2Q11 from 21.9% in 1Q11. Meanwhile, the issuance of SGS bonds rose 30.0% y-o-y to SGD5.2 billion in 2Q11 due to two new issuances: a SGD2.5 billion 5-year bond and a SGD2.7 billion 10-year bond in April and June, respectively.

The Singapore government does not need to finance its expenditures through the issuance of government bonds as it has operated on budget surpluses in recent decades. However, there are three primary objectives with the issuance of SGS bonds: (i) build a liquid SGS market to facilitate pricing of corporate issuance, (ii) foster the growth of an active secondary market, and (iii) encourage issuers and investors to participate in the Singapore bond market.

In July 2010, MAS announced that it would begin issuing MAS bills in 2Q11 for the purpose of liquidity management in the banking system. On 25 April, the first SGD1.0 billion of MAS bills were issued. These bills are one of four instruments available to MAS for use in money market operations. The other three instruments are foreign exchange (FX) swaps or reverse swaps, SGS repos or reverse repos, and clean lending or borrowing. MAS bills are available in tenors of 4, 6, and 8 weeks, as well as 3 months. The issuance size will be announced

1 business day ahead of the scheduled auction, with MAS committing to announce the issuance calendar in May and November of each year. MAS bills are not listed on the Singapore Exchange (SGX).

The SGS issuance calendar for the second half of 2011 includes more than 26 issues of 3-month treasury bills and re-openings of benchmark bonds. (The 7-year bond has not been used as a benchmark bond since February, given that the bond yield curve now extends meaningfully beyond 10 years.) Future bond issuance will concentrate liquidity on existing securities across the curve, including 2-, 5-, 10-, 15-, and 20-year bonds.

LCY corporate bonds outstanding in Singapore were up 33.0% y-o-y as of end-June, following 31.1% growth in 1Q11, to reach SGD112 billion.

The rapid expansion was the result of a 2.3% y-o-y increase in new bond issuances in 2Q11. However, the 4.7% q-o-q growth of LCY corporate bonds outstanding in 2Q11 was less than half of the 10.3% growth rate in 1Q11.

Notable issues in 2Q11 included SGD1 billion of subordinated bonds from United Overseas Bank, as well as SGD462 million from real estate developer Street Square. Water treatment systems provider Hyflux issued SGD400 million worth of bonds, while Housing and Development Board and CapitaMall Trust issued SGD350 million each.

The top 40 corporate issuers in Singapore at end-June were mainly from the financial and consumer sectors, and accounted for 49% of total corporate bonds outstanding (**Table 2**). The majority of the issuers included privately

Table 2: Top 40 Issuers of LCY Corporate Bonds in Singapore (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (SGD billion)	LCY Bonds (US\$ billion)				
1. Housing and Development Board	6.9	5.6	Yes	No	No	Financial
2. Capitaland	4.9	4.0	No	Yes	Yes	Financial
3. United Overseas Bank	4.6	3.8	No	Yes	Yes	Financial
4. DBS Bank Singapore	4.1	3.3	No	Yes	Yes	Financial
5. Temasek Financial I	3.6	2.9	No	Yes	No	Financial
6. Public Utilities Board	2.5	2.0	Yes	No	No	Utilities
7. SP Power Assets	2.5	2.0	No	Yes	No	Utilities
8. Land Transport Authority	2.4	1.9	Yes	No	No	Industrial
9. Oversea-Chinese Banking	2.2	1.8	No	Yes	Yes	Financial
10. CapitaMall Trust	1.7	1.4	No	Yes	Yes	Financial
11. Singapore Airlines	1.7	1.4	No	Yes	Yes	Consumer
12. F&N Treasury	1.3	1.0	No	Yes	No	Financial
13. Keppel Land	1.2	1.0	No	Yes	Yes	Financial
14. City Developments	1.1	0.9	No	Yes	Yes	Consumer
15. PSA Corporation	1.0	0.8	No	Yes	No	Consumer
16. GLL IHT PTE	0.8	0.7	No	Yes	No	Financial
17. Mapletree Treasury Services	0.7	0.6	No	Yes	No	Financial
18. Capitaland Treasury	0.7	0.6	No	Yes	No	Financial
19. Sembcorp Financial Services	0.7	0.6	No	Yes	No	Industrial
20. Hyflux	0.7	0.6	No	Yes	Yes	Industrial
21. Overseas Union Enterprise	0.6	0.5	No	Yes	Yes	Consumer
22. Singapore Press Holdings	0.6	0.5	No	Yes	Yes	Communications
23. Singtel Group Treasury	0.6	0.5	No	Yes	No	Communications
24. Neptune Orient Lines	0.6	0.5	No	Yes	Yes	Industrial
25. CapitaMalls Asia Treasury	0.6	0.4	No	Yes	No	Financial

continued on next page

Table 2 continued

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (SGD billion)	LCY Bonds (US\$ billion)				
26. Olam International	0.6	0.4	No	Yes	Yes	Consumer
27. Capitacommercial Trust	0.5	0.4	No	Yes	Yes	Financial
28. Ascott Capital	0.5	0.4	No	Yes	No	Financial
29. Keppel Corporation	0.5	0.4	No	Yes	Yes	Diversified
30. Singapore Post	0.5	0.4	No	Yes	Yes	Industrial
31. Street Square	0.5	0.4	No	Yes	Yes	Financial
32. Hotel Properties	0.5	0.4	No	Yes	Yes	Consumer
33. ST Treasury Services	0.5	0.4	No	Yes	No	Financial
34. Joynote Limited	0.4	0.3	No	Yes	No	Financial
35. Yanlord Land Group	0.4	0.3	No	Yes	Yes	Financial
36. Savu Investments	0.4	0.3	No	Yes	No	Financial
37. Great Eastern Life Assurance	0.4	0.3	No	Yes	Yes	Financial
38. HK Land Treasury Service	0.4	0.3	No	Yes	Yes	Financial
39. Asia Pacific Breweries	0.4	0.3	No	Yes	Yes	Consumer
40. Guocoland	0.4	0.3	No	Yes	Yes	Financial
Total Top 40 LCY Corporate Issuers	54.9	44.7				
Total LCY Corporate Bonds	112.0	91.2				
Top 40 as % of Total LCY Corporate Bonds	49.0%	49.0%				

LCY = local currency.
Source: Bloomberg LP.

owned corporations and three of Singapore's statutory boards: (i) Housing and Development Board (HDB), (ii) Public Utilities Board, and (iii) Land Transport Authority. HDB has ranked as the top LCY corporate issuer in the first half of the year, with total LCY bonds outstanding of SGD6.9 billion at end-June.

Policy, Institutional, and Regulatory Developments

SGX to Trade SGS

SGX commenced trading SGS on 8 July in an effort to improve price transparency and liquidity in SGS bonds. It will also provide retail investors with a safe but higher yielding alternative to bank deposits. Prior to this development, investors could only trade SGS bonds through dealer banks. A total of 19 SGS bonds amounting to SGD74 billion are currently traded on the SGX, with maturities of 5, 7, 10, 15, and 20 years. SGX's Central Depository acts as the custodian of SGS bonds.

SGX to Begin Clearing Non-Deliverable Forwards in September

SGX announced that in September it will begin clearing non-deliverable forwards (NDFs) of emerging Asian currencies, including the People's Republic of China (PRC) renminbi, Indonesian rupiah, Indian rupee, Korean won, Malaysian ringgit, Philippine peso, and NT dollar. The move was the result of new regulations in most G-20 economies requiring that trades involving a number of previously over-the-counter (OTC) derivatives be made through a central clearinghouse in order to provide a guarantee to the counterparty if the other party defaults. Though Singapore has not announced any mandatory requirements for central clearing, the finalization of rules on derivatives clearing in the United States, European Union, and several Asian countries will likely drive the success of this service. NDFs represent a large share of the trade in emerging market currencies as a majority of them are not fully convertible outside their country of origin. In November, SGX successfully launched its first financial OTC derivatives clearing service for Singapore dollar interest rates.

MAS Announces New Capital Requirements for Singapore Banks

MAS has released new capital rules for banks in Singapore that exceed the levels established under the Basel III agreement. MAS will require Singapore-incorporated banks to have a minimum common equity Tier 1 capital adequacy ratio (CAR) of 6.5%, a Tier 1 CAR of 8.0%, and a total CAR of 10.0%, effective 1 January 2015. MAS will require Singapore-incorporated banks to meet the minimum capital adequacy requirements of Basel III by 1 January 2013, which is 2 years ahead of the Basel Committee's 2015 timeline. MAS also plans to adopt Basel III's capital standards to improve the consistency, transparency, and quality of the capital base, and to strengthen the risk coverage of bank capital rules.

Thailand—Update

Yield Movements

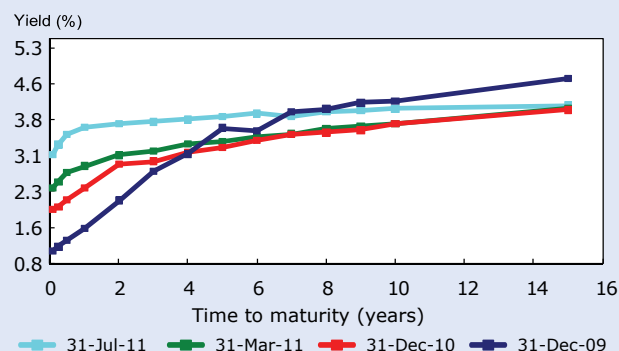
Thailand's government bond yield curve flattened between end-December 2010 and end-July (Figure 1). Yields at the short-end of the curve increased as much as 137 basis points (bps) over concerns about inflationary pressures and a policy rate hike. Government bond yields from the belly to the long-end of the curve rose as much as 55 bps, while the 15-year maturity rose only 9 bps. The yield spread between 2- and 10-year maturities narrowed to 32 bps at end-July from a spread of 65 bps at end-March.

The Bank of Thailand (BOT) raised its 1-day repurchase rate 25 bps to 3.25% at its Monetary Policy Committee (MPC) meeting on 13 July, reflecting concerns over increased inflationary pressures fueled by higher food and oil prices. BOT's stance also reflected concerns about the wage hike and fiscal spending pledges of Prime Minister Yingluck Shinawatra. The latest increase marked the fifth time that BOT has raised its policy rate by 25 bps since January.

Thailand's consumer price inflation accelerated to a 32-month high of 4.2% year-on-year (y-o-y) in May, driven mainly by higher food prices. In June, however, consumer price inflation declined slightly to 4.06% y-o-y before rising incrementally to 4.08% in July. Core inflation, which excludes energy and fresh food prices, climbed to 2.59% y-o-y in July from 2.55% in June. The Commerce Ministry still expects consumer price inflation to average between 3.2% and 3.7% for full-year 2011.

Thailand's real gross domestic product (GDP) rose 3.0% y-o-y in 1Q11 on rapid growth in exports and private investment, expansion in the tourism sector, and rising farm output. According to the National Economic and Social Development Board (NESBD), Thai exports rose 27.4% y-o-y in 1Q11, mainly driven by exports of jewelry, vehicles, parts and accessories, electrical appliances, and rubber. The tourism sector registered a total

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



LCY = local currency.
Source: Bloomberg LP.

of 5.4 million inbound tourists in 1Q11 for an increase of 15.0% y-o-y. Private investment grew 12.6% y-o-y in 1Q11, mainly due to an expansion in machinery and construction investment. The agricultural sector expanded 6.7% y-o-y due to increased farm output. Meanwhile the unemployment rate declined to 0.8%. The NESBD expects the Thai economy to expand between 3.5% and 4.0% in 2011.

Size and Composition

As of end-June, the size of Thailand's local currency (LCY) bond market had expanded 6.2% y-o-y to THB6.8 trillion (US\$222 billion), following 10.3% growth as of end-March (Table 1). On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding posted marginal growth of 0.1% in 2Q11, following a 0.9% increase in 1Q11. The slowdown in growth reflected lower issuance of central government bonds and zero issuance of treasury bills since the beginning of the year.

Total LCY government bonds outstanding rose 5.6% y-o-y to THB5.5 trillion as of end-June, or only about one-half of the 10.3% increase recorded at the end of 1Q11. BOT bonds expanded

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

	Amount (billion)						Growth Rate (%)					
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11	
	THB	US\$	THB	US\$	THB	US\$	THB	US\$	y-o-y	q-o-q	m-o-m	m-o-m
Total	6,813.9	225.0	6,839.0	228.9	6,827.9	225.2	6,819.8	221.9	10.3	0.9	0.4	0.1
Government	5,476.8	180.9	5,481.2	183.4	5,452.7	179.8	5,466.2	177.9	10.3	(0.4)	0.1	0.2
Treasury Bonds	2,546.6	84.1	2,576.2	86.2	2,602.3	85.8	2,557.3	83.2	3.1	(1.9)	1.2	(1.7)
Central Bank Bonds	2,447.9	80.8	2,424.6	81.1	2,369.1	78.1	2,426.5	79.0	24.1	1.5	(1.0)	2.4
State-Owned Enterprise and Other Bonds	482.3	15.9	480.4	16.1	481.4	15.9	482.4	15.7	(7.4)	(2.1)	(0.4)	0.2
Corporate	1,337.1	44.2	1,357.9	45.4	1,375.2	45.4	1,353.6	44.1	10.2	6.7	1.6	(1.6)

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 end-of-period LCY-US\$ rates are used.

3. Growth rates are calculated from LCY base and do not include currency effects.

Sources: Bank of Thailand (BOT) and Bloomberg LP.

the most, posting an annual growth rate of 15.7%. Treasury bonds, however, dropped 0.4% y-o-y, following 3.1% growth in 1Q11. The decline in state-owned enterprise bonds slightly improved to -6.1% y-o-y as of end-June from -7.4% as of end-March.

New issuance of government bonds rose 26.3% y-o-y to THB2.9 trillion in 2Q11, while declining 9.7% on a q-o-q basis. BOT bonds once again dominated new issuance, representing 95.7% of total government issuance in 2Q11. BOT bonds grew 42.0% y-o-y while declining 11.0% q-o-q. Bond issuance from state-owned enterprises rose 23.7% y-o-y and 35.5% q-o-q, the majority coming from the Government Housing Bank (THB3.0 billion), Provincial Waterworks Authority (THB2.6 billion), and Provincial Electricity Authority (THB2.3 billion). New issuance from the central government, however, declined 65.7% y-o-y to THB113.8 billion, primarily due to zero issuance of treasury bills in 2Q11.

In February, the Thai Finance Ministry issued its longest-dated security ever—a 50-year government bond amounting to THB3.5 billion. Thailand is the fourth country to issue 50-year bonds, joining the United Kingdom, France, and the People's Republic of China. The Thai government plans to issue a series of 50-year bonds in 3Q11 and 4Q11 worth a total of THB3 billion–THB4 billion. Proceeds will help cover the budget deficit and a portion will be used to refinance existing government debt. Thailand's international reserves stood at US\$180 billion as of end-May and have remained above US\$100 billion since September 2008. Thailand expects to run a budget deficit of THB350 billion, or not more than 4.0% of GDP, for fiscal year 2012 (ending on 30 September 2012). This target represents an improvement from a THB420 billion deficit in fiscal year 2011. The Public Debt Management Office (PDMO) announced that it plans to focus on medium- and long-term bonds with maturities of 5, 7, 10, 15, and 30 years, in addition to the 50-year bond and inflation-linked bonds, as part of the government's target to achieve a balanced budget within 5 years.

In July, Thailand's debut sale of its 10-year inflation-linked bonds swelled to THB40 billion (US\$1.3 billion), the top-end of the indicated size range of THB20 billion–THB40 billion. The successful deal came at a coupon of 1.2%, which was also at the higher-end of the unofficial price guidance of 1.00%–1.25%. Foreign investors—asset managers, sovereign wealth funds, insurance companies, and private banks—were the single largest group of buyers. However, the offered amount of THB13 billion for retail investors only drew THB6 billion worth of bids. PDMO attributed the low pick-up to a lack of knowledge about inflation-linked bonds among retail investors. The remaining THB7 billion was allocated to domestic institutional investors. PDMO revealed that it will re-open the bond and has plans to issue in different tenors as well, although it may no longer market the bonds to retail investors. The structure of Thai inflation-linked bonds are similar to the United States (US) Treasury's inflation-protected securities wherein the bond coupon is constant but the principal is indexed to the country's consumer price index and compounded.

LCY corporate bonds outstanding grew 9.0% y-o-y to THB1.4 trillion in 2Q11, a growth rate that was down from 10.2% in 1Q11. On a q-o-q basis, corporate bond growth slowed to 1.2% in 2Q11 from 6.7% in 1Q11. New issuance in 2Q11 increased 9.8% y-o-y to THB302 billion but declined 21.0% on a q-o-q basis.

Notable THB-denominated corporate bond issues in 2Q11 included a THB15.0 billion bond from Siam Cement, THB10.0 billion each from Thanachart Bank and BTS Group, and THB5.5 billion from energy firm Banpu. The maturities of these bonds ranged between 4 and 8 years. Meanwhile, Thailand's largest agribusiness firm Charoen Pokphand Foods issued Thailand's first ever 30-year corporate bond in August worth THB4 billion, following PTT's THB4 billion December 2110 century bond.

In July, Thailand's PDMO permitted five foreign banks to issue THB-denominated bonds up until 31 December. First Gulf Joint Stock Company

plans to issue its debut bond worth THB6 billion, while Credit Agricole Corporate and Investment Bank, ING Bank, and Export-Import Bank of Korea were granted permission to issue THB10 billion each. Meanwhile, Lloyds TSB Bank was given approval to issue bonds worth up to THB6 billion. In addition, the Finance Ministry allowed Australia and New Zealand Banking Group, Hana Bank, and Shinhan Bank to issue THB-denominated bonds between 1 April and 30 September, with an issue size of THB8 billion each.

An increase in the issuance of corporate bonds is likely in the coming months ahead of expected rate hikes. Corporates rated from BBB to A by Tris Rating have recently issued smaller bond sizes with tenors between 3 and 5 years. Phatra Leasing and BSL Leasing have each issued THB500 million, with credit ratings of A- and BBB, respectively. Motor cycle leasing company Thitikorn also issued THB500 million of senior bonds with a rating of A-. In the property sector, Noble Development issued THB1.5 billion of BBB-rated 3-year bonds, while Asian Property Development sold THB1.5 billion bonds with an A- rating.

The top 30 corporate issuers in Thailand accounted for 70% of total LCY corporate bonds outstanding at end-June (**Table 2**). PTT topped the list, with total LCY bonds outstanding of THB180.9 billion. Siam Cement followed with THB110.0 billion. As a group, financial institutions dominated the list of top 30 corporate issuers, followed by consumer and energy firms. About one-third of the list consisted of state-owned enterprises, while the majority of firms were listed on the Stock Exchange of Thailand (SET).

Foreign Currency Bonds

In April, state-owned PTT Exploration and Production, acting through its subsidiary PTT Canada International Finance, sold US\$700 million of 10-year bonds at a coupon of 5.692%. The foreign currency (FCY) deal was one of the rare sole mandates outside of Asia. US-based investors bought 56% of the bonds, while Asian and European investors purchased 30% and

Table 2: Top 30 Issuers of LCY Corporate Bonds in Thailand (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (THB billion)	LCY Bonds (US\$ billion)				
1. PTT PCL	180.9	5.9	Yes	No	Yes	Energy
2. Siam Cement PCL	110.0	3.6	Yes	No	Yes	Diversified
3. Krung Thai Bank	75.8	2.5	Yes	No	Yes	Financial
4. PTT Exploration and Production Company	50.0	1.6	Yes	No	Yes	Energy
5. Bank of Ayudhya	47.2	1.5	No	Yes	Yes	Financial
6. Thai Airways International	31.3	1.0	Yes	No	Yes	Consumer
7. Charoen Pokphand Foods	30.7	1.0	No	Yes	Yes	Consumer
8. Kasikorn Bank	28.4	0.9	No	Yes	Yes	Financial
9. Thanachart Bank	28.0	0.9	No	Yes	no	Financial
10. TMB Bank	27.8	0.9	No	Yes	Yes	Financial
11. DAD SPV Company LTD	24.0	0.8	Yes	No	No	Financial
12. Banpu	23.8	0.8	No	Yes	Yes	Energy
13. Toyota Leasing Thailand	21.9	0.7	No	Yes	No	Consumer
14. Krung Thai Card	21.0	0.7	Yes	No	Yes	Financial
15. Thai Oil	20.8	0.7	Yes	No	Yes	Energy
16. PTT Chemical	20.4	0.7	Yes	No	Yes	Basic Materials
17. Siam Commercial Bank	20.0	0.7	No	Yes	Yes	Financial
18. True Corporation	19.6	0.6	No	Yes	Yes	Communications
19. Advanced Info Service	19.5	0.6	No	Yes	Yes	Communications
20. Ayudhya Capital Auto Lease	18.2	0.6	No	Yes	No	Financial
21. Bangkok Expressway	17.1	0.6	No	Yes	Yes	Consumer
22. Kiatnakin Bank	16.3	0.5	No	Yes	Yes	Financial
23. Quality Houses	15.3	0.5	No	Yes	Yes	Consumer
24. PTT Aromatics and Refining	15.0	0.5	Yes	No	Yes	Energy
25. Glow Energy	15.0	0.5	No	Yes	Yes	Utilities
26. CH Karnchang Public Company	14.0	0.5	No	Yes	Yes	Industrial
27. Land and Houses	13.6	0.4	No	Yes	Yes	Consumer
28. Thanachart Capital	13.5	0.4	No	Yes	Yes	Financial
29. Ratchaburi Electricity Generating	13.3	0.4	No	Yes	Yes	Utilities
30. Bangkok Mass Transit System	13.0	0.4	Yes	Yes	No	Industrial
Total Top 30 LCY Corporate Issuers	965.4	31.4				
Total LCY Corporate Bonds	1,375.2	44.8				
Top 30 as % of Total LCY Corporate Bonds	70.2%	70.2%				

LCY = local currency.
Source: Bloomberg LP.

14%, respectively. Proceeds will be used to fund exploration, development, and production activities. Other US\$-denominated bond issuers in 2Q11 include Export-Import Bank Thailand and Siam Commercial Bank, with issue sizes of US\$120 million and US\$400 million, respectively.

The foreign holdings of Thai government bonds stood at THB227.8 billion at end-June, an increase of 110.0% y-o-y and 6.8% q-o-q. Foreign holdings represented 8.9% of total government bonds outstanding as of end-June.

Investor Profile

Contractual savings funds are the largest holder of Thai government bonds, with a total of THB572 billion at end-June (**Figure 2**). Contractual savings funds' total share decreased to 22.4% in June 2011 from 25.4% in June 2010. Insurance companies were the next largest holder with a 21.8% share in June 2011, up from 18.1% a year earlier. Residents landed in the third spot, decreasing their share to 16.3% in June 2011 from 16.9% a year earlier. Commercial banks had a share of 15.9%, followed by nonresidents (8.9%), the central bank (7.5%),

financial corporations "not elsewhere classified" (3.9%), and general government and non-profit organizations (2%). Finally, other non-financial corporations held a 0.8% share, while non-financial market mutual funds had a marginal 0.6% share.

Rating Changes

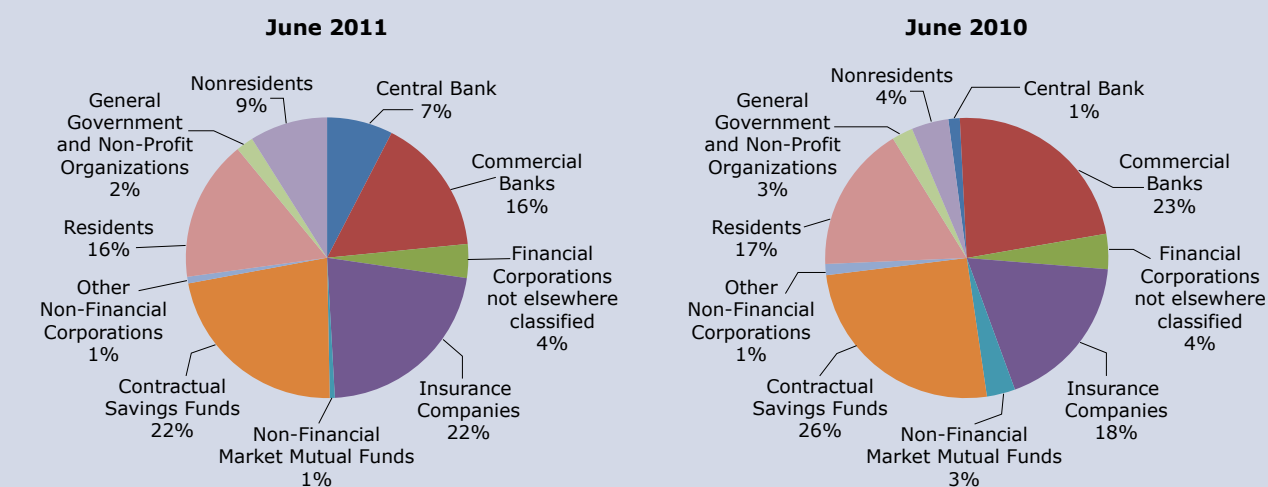
In April, Ratings and Investment Information (R&I) upgraded the outlook for Thailand's long-term FCY and LCY government bond ratings to stable from negative (**Table 3**). According to R&I, a rating upgrade is possible if Thailand "demonstrates the strength of its economic base even if political conflict continues."

Table 3: Selected Sovereign Ratings and Outlook for Thailand

	Moody's	S&P	Fitch	R&I
Sovereign FCY LT Ratings	Baa1	BBB+	BBB	BBB
Outlook	stable	stable	stable	stable

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

Figure 2: LCY Government Bonds Investor Profile



LCY = local currency.
Source: Bank of Thailand.

Policy, Institutional, and Regulatory Developments

PDMO Plans Bond Trading via ATMs

In April, PDMO announced that it plans to allow retail investors to trade bonds via automated teller machines (ATMs). According to PDMO, the Thai Finance Ministry plans to assign commercial banks as distributors of government savings bonds to retail investors through ATMs across Thailand.

BOT Announces New List of Primary Dealers

BOT announced a new list of primary dealers for bilateral repurchase transactions, effective 3 May. The list includes Bangkok Bank, Krung Thai Bank, Bank of Ayudhya, Kasikorn Bank, Siam Commercial Bank, TMB Bank, Bank for Agriculture and Agricultural Cooperatives, Standard Chartered Bank, The Bank of Tokyo-Mitsubishi UFJ, United Overseas Bank, Government Savings Bank, and HSBC. BOT periodically reviews its list of primary dealers to encourage competition and enhance efficiency in conducting monetary operations.

SEC Tightens Rules on Bills of Exchange

Thailand's Securities and Exchange Commission (SEC) released tighter rules on bills of exchange in May, addressing potential risks as local banks have recently been aggressive in issuing bills of exchange to manage short-term liquidity. The SEC announced that bills of exchange should be treated similar to other debt instruments and therefore subject to SEC regulations. Exemptions previously offered to financial institutions will be reversed, although a grace period will be provided before any new measures take effect.

Thai Local Governments to Issue Bonds

PDMO announced in May that the cities of Bangkok and Pattaya, as well as several other local governments, will be allowed to raise funds through bond issues. However, the central government will not guarantee these issues. The SEC will supervise the bond issues and a credit rating will be required. Currently, local governments source funds from banks to finance investment projects. The Finance Ministry and the Interior Ministry are working together on this regulation as part of the public finance bill that is currently under review by the State Council.

Thai Treasury Department Plans to Issue Securitized Bonds

The Treasury Department of Thailand announced in July it plans to issue THB3 billion worth of securitized bonds to finance property development projects. A major component of the construction efforts will be new government office buildings in Soi Ratchakru, Phaholyothin Road. The estimated construction cost of this project is THB2 billion–THB3 billion. If approved by the government, it would be the second time that Thailand has issued securitized bonds since it issued a THB21 billion securitized bond in 2005.

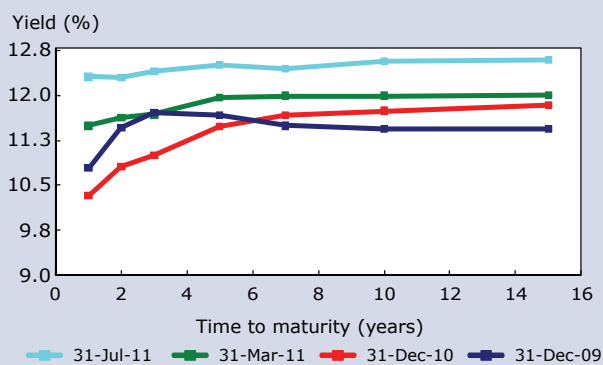
Viet Nam—Update

Yield Movements

Between end-December 2010 and end-March, government bond yields in Viet Nam rose for all maturities, particularly at the short-end of the curve. Viet Nam's government benchmark yields continued to rise for all maturities between end-March and end-July. Due to accelerating inflation, the government bond benchmark yield for the 1-year tenor rose to 12.32% at end-July, up 82 basis points (bps) from its end-March level (**Figure 1**). Yields for the 2- and 3-year maturities rose 68 bps and 73 bps, respectively. Meanwhile, the increase in yields from the belly to the long-end of the curve was less pronounced, ranging between 46 bps and 59 bps. By end-June, the curve had flattened and the yield spread between 2- and 10-year maturities narrowed to 28 bps from 37 bps at end-March.

The large increase in the yield for the 1-year benchmark reflects the rise in consumer price inflation in Viet Nam, which accelerated to 22.2% year-on-year (y-o-y) in July from 20.8% in June and 19.8% in May. Price increases in recent months have mainly been driven by higher costs for food and transportation.

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



LCY = local currency.
Source: Bloomberg LP.

Early this year, the State Bank of Viet Nam (SBV) adjusted its key policy rates upward to counter rising inflation. The SBV has raised its refinancing rate by a total of 500 bps since the beginning of the year, hiking its refinancing rate from 9.0% in January to 14.0% in May. The SBV raised the discount rate from 7.0% to 12.0% in March, and by an additional 100 bps to 13.0% in May. The SBV has also increased its reverse repurchase rate by a total of 500 bps from 10.0% at the beginning of the year to 15.0% in May. More recently, the SBV decided in early July to cut its reverse repurchase rate for open market operations from 15.0% to 14.0%.

On 11 February, the SBV adjusted the inter-bank average exchange rate to VND20,693 = US\$1 from VND18,932 = US\$1, while narrowing the trading band for the exchange rate to $\pm 1.0\%$ from $\pm 3.0\%$. The devaluation of the Vietnamese dong was part of government efforts to improve liquidity in the foreign exchange market. In June, the SBV hiked foreign currency reserve requirement ratios for state-owned commercial banks, joint stock commercial banks, joint venture banks, foreign bank branches, and wholly owned foreign banks (see **Policy, Institutional, and Regulatory Developments** for more detail).

Viet Nam's economy grew 5.6% y-o-y in 1H11, down from 6.2% growth in the same period last year. In 2Q11, Viet Nam's gross domestic product (GDP) expanded 5.7% y-o-y after growing 5.4% in the previous quarter. In 1H11, the country's agriculture, forestry, and fisheries sector grew 2.1% y-o-y, while the industry and construction sector and the services sector registered 6.5% and 6.1% growth rates, respectively.

Size and Composition

Viet Nam's local currency (LCY) bond market grew 18.8% y-o-y and 5.0% quarter-on-quarter (q-o-q) to VND347 trillion (US\$16.9 billion) as of end-June,

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

	Amount (billion)						Growth Rate (%)					
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11	
	VND	US\$	VND	US\$	VND	US\$	VND	US\$	y-o-y	q-o-q	m-o-m	y-o-y
Total	330,858	16	334,249	16	337,914	16	347,278	17	46.2	8.7	1.0	18.8
Government	296,008	14	299,259	14	303,724	15	314,479	15	44.7	10.1	1.1	18.8
Treasury Bonds	116,467	6	119,053	6	122,838	6	130,413	6	25.9	(1.3)	2.2	8.3
Central Bank Bonds	-	0	-	0	-	0	-	0	-	-	-	-
Viet Nam Development Bank Bonds, State-Owned Enterprise Bonds, and Other Bonds	179,542	9	180,207	9	180,887	9	184,067	9	60.6	18.9	0.4	27.8
Corporate	34,850	2	34,990	2	34,190	2	32,799	2	60.3	(1.7)	0.4	18.9
												(2.3)
												(5.9)
												(4.1)

– = 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–US\$ rates are used.

2. Growth rates are calculated from LCY base and do not include currency effects.

Source: Bloomberg LP.

due to growth in both government and corporate bonds outstanding (**Table 1**).

Total LCY government bonds outstanding stood at VND314 trillion at end-June, representing growth of 18.8% y-o-y and 6.2% q-o-q. Treasury bonds rose 8.3% y-o-y and 12.0% q-o-q to VND130 trillion in 2Q11. Meanwhile, Viet Nam Development Bank bonds and state-owned enterprise bonds surged 27.8% y-o-y to VND184 trillion.

Total LCY corporate bonds outstanding rose 18.9% y-o-y to VND33 trillion in 2Q11 but fell 5.9% q-o-q. The top 15 corporate issuers in Viet Nam, most of which were financial institutions, comprised 93.5% of total corporate bonds outstanding at end-June (**Table 2**).

Policy, Institutional, and Regulatory Developments

SBV Issues New Regulations on Foreign Currency Loans

In March, the SBV issued a circular on foreign currency lending as part of its effort to curb inflation and stabilize the economy. Under the circular, credit institutions are allowed to extend foreign currency loans to resident borrowers under the following circumstances: (i) short-, medium-, and long-term loans to pay for imported commodities and services; (ii) short-term loans for the production and trade of goods through border points; and (iii) loans for other demands approved in writing by the SBV.

SBV Requires Credit Institutions to Comply with Set Lending and Deposit Rates

On 17 June, the SBV issued Document No. 4605/NHNN-CSTT requiring credit institutions to strictly comply with the maximum Vietnamese dong mobilizing interest rate—the rates for deposits and valuable papers—which was set at 14.0% per year under Circular No. 02/2011/TT-NHNN dated 3 March. The SBV is encouraging credit institutions to minimize operational costs to

Table 2: Top 15 LCY Corporate Issuers in Viet Nam (as of June 2011)

Issuer	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (VND billion)	LCY Bonds (US\$ billion)				
1. Vietin Bank	7,095.00	0.34	No	Yes	Yes	Finance
2. Asia Commercial Joint Stock Bank	5,090.00	0.25	No	Yes	Yes	Finance
3. Vincom	5,000.00	0.24	No	Yes	Yes	Real Estate
4. Vietnam Techcombank	3,880.00	0.19	No	Yes	No	Finance
5. Sacombank	2,000.00	0.10	No	Yes	Yes	Finance
6. Agribank Securities	2,000.00	0.10	No	Yes	Yes	Finance
7. Vietnam Maritime Commercial Bank	1,000.00	0.05	No	Yes	No	Finance
8. Refrigeration Electrical	810.42	0.04	No	Yes	Yes	Industrial
9. Hoa Phat Group	800.00	0.04	No	Yes	Yes	Industrial
10. An Binh Bank	600.00	0.03	No	Yes	No	Finance
11. HAGL	530.00	0.03	No	Yes	Yes	Real Estate
12. Kinh Bac City Devt Corp	500.00	0.02	No	Yes	Yes	Real Estate
13. Vinpearl	500.00	0.02	No	Yes	Yes	Resorts/Theme Parks
14. HCMC Gen Import Export & Investment	450.00	0.02	No	Yes	Yes	Trade
15. Vietnam Steel	400.00	0.02	No	Yes	No	Industrial
Total Top 15 LCY Corporate Bond Issuers	30,655.42	1.49				
Total LCY Corporate Bonds	32,799.76	1.59				
Top 15 as % of Total LCY Corporate Bond Outstanding	93.5%	93.5%				

LCY = local currency.
Source: Bloomberg LP.

lower lending rates, especially those extended to agricultural and rural areas, exporters, small and medium-sized enterprises, and supporting industries. The document also instructed the SBV Financial Supervision Agency as well as SBV provincial and municipal branches to enhance the supervision of credit institutions and deal severely with violators.

Viet Nam Hikes Foreign Currency Reserve Requirement Ratios

The SBV hiked foreign currency reserve requirement ratios for state-owned commercial banks, joint stock commercial banks, joint venture banks, foreign bank branches, and wholly owned foreign banks in June. The reserve requirement ratio for foreign currency demand deposits and time deposits with terms of up to 12 months was raised to 7.0% from 6.0%. For foreign currency deposits with terms longer than 12 months, the reserve requirement ratio was increased to 5.0% from

4.0%. For the Viet Nam Bank for Agriculture and Rural Development, Central People's Credit Fund, and cooperative banks, the reserve requirement ratio for foreign currency demand deposits and time deposits with terms of up to 12 months was set at 6.0% while that for deposits with terms of more than 12 months was set at 4.0%.