Market Summaries

People's Republic of China

Yield Movements

Between 1 June and 15 August, the People's Republic of China's (PRC) government bond yield curve shifted downward as yields fell for all tenors **(Figure 1)**. Yields dropped the most at the longer-end of the curve, with the 7-year and 10-year tenors falling 34 basis points (bps) each. The 2-year tenor fell the least, declining 16 bps, which led to the 2-year versus 10-year yield spread narrowing to 33 bps on 15 August from 52 bps on 1 June.

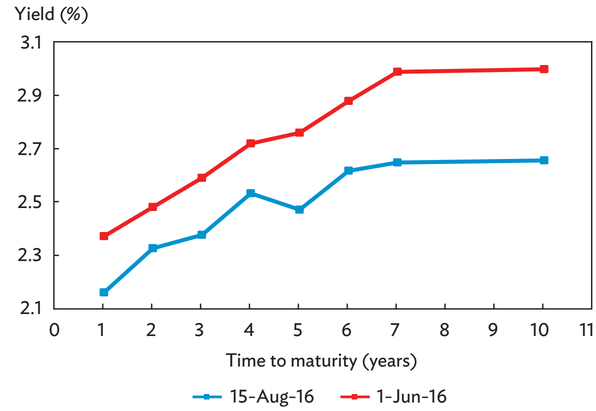
The fall in the PRC's yields was driven by recent macroeconomic data and demand factors for government bonds. The PRC's gross domestic product growth rate stood at 6.7% year-on-year (y-o-y) in the second quarter (Q2) of 2016, unchanged from the prior quarter. This growth rate is lower than that of the fourth quarter of 2015 when the PRC's economy expanded at a rate of 6.8%. Most analysts expect the PRC's economic growth to be slower moving forward compared to prior years.

Weak external demand has weighed on the economy. In United States dollar terms, exports fell 4.4% y-o-y in July, though this was a slightly better performance than June's 4.8% y-o-y drop. In addition, consumer price inflation has been on a downward trend, with consumer prices rising 1.8% y-o-y in July versus 1.9% y-o-y in June. Through the first 7 months of 2016, the inflation rate peaked at 2.3% y-o-y in February, March, and April.

Economic data also point to a softening economy in the PRC, which has pushed down yields and raised market expectations that the People's Bank of China will engage in another round of easing. The central bank last reduced reserve requirement ratios by 50 bps in February.

Yields in the PRC had risen early in the year due to increased supply risk in the LCY government bond market. While issuances of local government bonds have continued, markets have become increasingly concerned with credit risk in the corporate bond market sector. In a May 2016 news report, Deutsche Bank noted

Figure 1: The People's Republic of China's Benchmark Yield Curve—Local Currency Government Bonds



Source: Based on data from Bloomberg LP.

that there have been 40 defaults from bond issuers this year through April. As a result, there has been increased demand for safer assets such as government bonds, which has contributed to a fall in yields.

Size and Composition

LCY bonds in the PRC rose 8.0% quarter-on-quarter (q-o-q) and 30.6% y-o-y in Q2 2016, leading to CNY45.9 trillion (USD6.9 trillion) worth of bonds outstanding at the end of June **(Table 1)**.

Government Bonds. LCY government bonds outstanding rose 12.6% q-o-q in Q2 2016 versus 5.2% q-o-q in the prior quarter. The LCY government bond market grew 40.0% on a y-o-y basis. Treasury bonds were the main driver of q-o-q growth, rising 19.5% q-o-q. Within Treasury bonds, growth continues to be driven by the issuance of local government bonds. Outstanding local government bonds grew 45.5% q-o-q in Q2 2016. The rapid rise in issuance was due to an ongoing exchange of local government debt for bonds. In the first 6 months of 2016, total local government bond issuance stood at CNY3.6 trillion. In contrast,

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

	Outstanding Amount (billion)						Growth Rates (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	CNY	USD	CNY	USD	CNY	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**35,137**	**5,666**	**42,485**	**6,583**	**45,897**	**6,904**	**6.0**	**15.4**	**8.0**	**30.6**
Government	22,344	3,603	27,791	4,306	31,286	4,706	6.9	13.9	12.6	40.0
Treasury Bonds	11,284	1,820	15,856	2,457	18,955	2,851	9.9	19.3	19.5	68.0
Central Bank Bonds	428	69	428	66	428	64	0.0	(12.5)	0.0	0.0
Policy Bank Bonds	10,632	1,715	11,507	1,783	11,902	1,790	4.2	9.9	3.4	11.9
Corporate	12,793	2,063	14,694	2,277	14,611	2,198	4.4	18.1	(0.6)	14.2
Policy Bank Bonds										
China Development Bank	6,538	1,054	6,816	1,056	6,976	1,049	3.2	5.2	2.3	6.7
Export–Import Bank of China	1,797	290	1,913	296	1,988	299	6.1	21.4	3.9	10.6
Agricultural Devt. Bank of China	2,297	370	2,778	430	2,939	442	5.7	16.1	5.8	28.0

( ) = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, 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 local currency–USD rate is used.
4. Growth rates are calculated from local currency base and do not include currency effects.
Sources: *ChinaBond*, *Wind Info*, and Bloomberg LP

local governments issued CNY3.8 trillion during the whole of 2015. Out of the CNY3.5 trillion issued during the first half of 2016, CNY900 billion comprised new local government bonds issuance with the remainder coming from a debt swap. New bond issuance is already approaching the CNY1.18 trillion quota set by the PRC for total local government bond issuance for full-year 2016. The rise in issuance was also driven by maturing obligations in 2016, with an estimated CNY2.8 trillion due to mature in 2016, as well as increased funding demand driven by various local government projects.

Policy bank bonds continued to increase in Q2 2016, albeit at a slower pace than in the previous quarter, expanding 3.4% q-o-q and 11.9% y-o-y. The outstanding amount of central bank bonds remained unchanged in Q2 2016 from the prior quarter due to a lack of new issuance.

Corporate Bonds. Corporate bonds outstanding fell 0.6% q-o-q but rose 14.2% y-o-y to reach CNY14.6 trillion at the end of June **(Table 2)**. Within the major bond categories, commercial bank bonds and Tier 2 notes and local corporate bonds expanded 3.4% q-o-q and 3.6% q-o-q, respectively. Strong issuance by commercial banks and insurance companies also continued in Q2 2016. However, state-owned enterprise bonds, commercial paper, and medium-term notes outstanding all posted declines during the quarter. The largest decline was in commercial paper, which fell 6.7% q-o-q, as demand waned following several commercial paper defaults and the discovery of a trading scam involving two employees at Agricultural Bank of China.

Overall issuance levels declined in Q2 2016 versus Q1 2016 **(Figure 2)**. The overall decline in corporate bond issuance was due to increasing risk aversion among investors resulting from a rising number of corporate bond defaults. Medium-term note issuance still remains the highest among the major bond categories (excluding commercial paper) due to its relatively easy issuance process.

A relatively small number of issuers dominate the PRC's corporate bond market **(Table 3)**. At the end of June, the top 30 corporate bond issuers accounted for CNY5.6 trillion worth of corporate bonds outstanding, or about 38.6% of the total market. Out of the top 30, the 10 largest issuers accounted for CNY3.7 trillion.

The top 30 issuer list has become dominated by banks, owing to the continued issuance of commercial bank bonds as banks accelerate their fundraising. Among the top 30 corporate issuers at the end of June, 14 were in the banking industry.

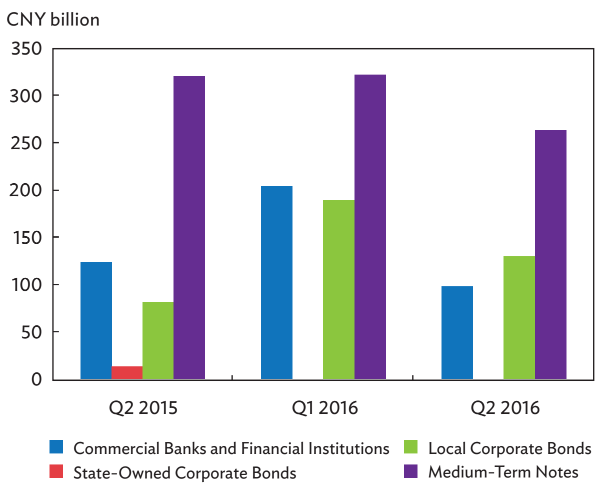
Table 4 presents the most notable corporate bond issuances in Q2 2016. The list mainly comprises financial institutions and infrastructure-related companies,

Table 2: Corporate Bonds Outstanding in Key Categories

	Amount (CNY billion)			Growth Rate (%)			
				Q2 2015		Q2 2016	
	Q2 2015	Q1 2016	Q2 2016	q-o-q	y-o-y	q-o-q	y-o-y
Commercial Bank Bonds and Tier 2 Notes	1,719	2,196	2,271	1.0	25.5	3.4	32.1
SOE Bonds	617	583	575	1.0	(0.3)	(1.4)	(6.8)
Local Corporate Bonds	2,443	2,690	2,787	1.0	17.1	3.6	14.1
Commercial Paper	2,249	2,820	2,632	1.0	22.1	(6.7)	17.1
Medium-Term Notes	4,043	4,512	4,496	1.0	8.4	(0.4)	11.2

( ) = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, SOE = state-owned enterprise, y-o-y = year-on-year.
Sources: *ChinaBond* and *Wind Info*.

Figure 2: Corporate Bond Issuance in Key Sectors



CNY = Chinese yuan, Q1 = first quarter, Q2 = second quarter.
Sources: *ChinaBond* and *Wind Info*.

reflecting the fundraising efforts of banks and the significant financing needs of the oil industry.

Investor Profile

Treasury Bonds and Policy Bank Bonds. Banks held 69.9% of all Treasury bonds, including policy bank bonds, at the end of June **(Figure 3)**. This share was down from a year earlier. The holdings of funds institutions, such as mutual funds, have steadily increased over time, comprising 12.3% of all Treasury bonds and policy bank bonds at the end of June, up from 6.4% a year earlier.

Corporate Bonds. Banks were no longer the largest holder of LCY corporate bonds at the end of June. Their share of the corporate bond market fell to 19.5% at the end of June from 25.6% a year earlier **(Figure 4)**. Fund institutions became the dominant holder of corporate bonds, driven by mutual funds seeking higher yields, with a share of the outstanding stock that rose to 41.8% at the end of June from 26.0% a year earlier.

Figure 5 presents investor profiles across corporate bond categories at the end of June. Funds institutions were the dominant holder of both local corporate bonds and medium-term notes. On the other hand, the share of banks' holdings declined from a year earlier. Banks and insurance companies were the dominant holders of commercial bank bonds at the end of June, with banks holding the majority of common bonds and insurance companies holding the most subordinated bonds.

Liquidity

Interest rate swap volumes rose 17.7% q-o-q, driven mostly by an increase in 7-day repurchase transactions. The 7-day repurchase interest rate swap is the most popular interest rate swap, accounting for nearly 91% of total transaction volume in Q2 2016 **(Table 5)**.

Figure 6 presents the turnover ratio of government bonds, broken down into Treasury bonds and policy bank bonds. There was a surge in trading activity for both types of government bonds in Q2 2016 due to increased demand for safer assets owing to credit concerns in the corporate bond market.

Table 3: Top 30 Issuers of Local Currency Corporate Bonds in the People's Republic of China

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (CNY billion)	LCY Bonds (USD billion)			
1.	China Railway	1,258.5	189.31	Yes	No	Transportation
2.	State Grid Corporation of China	472.1	71.01	Yes	No	Public Utilities
3.	China National Petroleum	410.0	61.67	Yes	No	Energy
4.	Industrial and Commercial Bank of China	283.0	42.57	Yes	Yes	Banking
5.	Agricultural Bank of China	260.0	39.11	Yes	Yes	Banking
6.	Bank of China	258.9	38.94	Yes	Yes	Banking
7.	China Construction Bank	212.0	31.89	Yes	Yes	Banking
8.	Petrochina	181.0	27.23	Yes	Yes	Energy
9.	Industrial Bank	176.0	26.47	No	Yes	Banking
10.	Shanghai Pudong Development Bank	169.6	25.51	No	Yes	Banking
11.	Bank of Communications	149.0	22.41	No	Yes	Banking
12.	State Power Investment	136.2	20.49	Yes	No	Energy
13.	China Minsheng Bank	135.1	20.32	No	Yes	Banking
14.	Bank of Beijing	122.9	18.49	Yes	Yes	Banking
15.	Central Huijin Investment	109.0	16.40	Yes	No	Diversified Financial
16.	China Citic Bank	107.5	16.17	No	Yes	Banking
17.	Senhua Group	106.0	15.94	Yes	No	Energy
18.	China Petroleum and Chemical	98.5	14.82	Yes	Yes	Energy
19.	China United Network Communications	91.0	13.69	Yes	Yes	Telecommunications
20.	China Everbright Bank	88.9	13.37	Yes	Yes	Banking
21.	China Datang	86.7	13.04	Yes	Yes	Energy
22.	China Three Gorges Project	85.5	12.86	Yes	No	Public Utilities
23.	China Guangfa Bank	84.5	12.71	No	Yes	Banking
24.	Shaanxi Coal and Chemical Industry Group	83.5	12.56	Yes	Yes	Energy
25.	Huaxia Bank	80.4	12.09	Yes	No	Banking
26.	Tianjin Infrastructure Construction & Investment Group	79.4	11.94	Yes	No	Industrial
27.	China Merchants Bank	79.0	11.88	No	Yes	Banking
28.	Haitong Securities	78.0	11.73	Yes	Yes	Brokerage
29.	China Huarong Asset Management	77.0	11.58	Yes	Yes	Asset Management
30.	China Southern Power Grid	74.0	11.13	Yes	No	Public Utilities
Total Top 30 LCY Corporate Issuers		**5,633.20**	**847.35**			
Total LCY Corporate Bonds		**14,611.50**	**2,197.88**			
Top 30 as % of Total LCY Corporate Bonds		**38.6%**	**38.6%**			

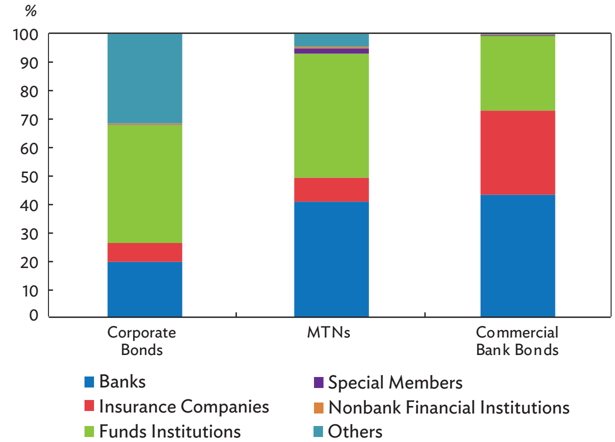
CNY = Chinese yuan, LCY = local currency, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

Table 4: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (CNY billion)
China Railway		
5-year bond	3.35	15
10-year bond	3.46	20
Industrial Bank		
10-year bond	3.74	30
Haitong Securities		
4-year bond	3.60	15
China Guangfa Bank		
5-year bond	3.52	15
China Cinda Asset Masnagement		
10-year bond	3.70	10
Ping An Life Insurance		
10-year bond	3.82	10

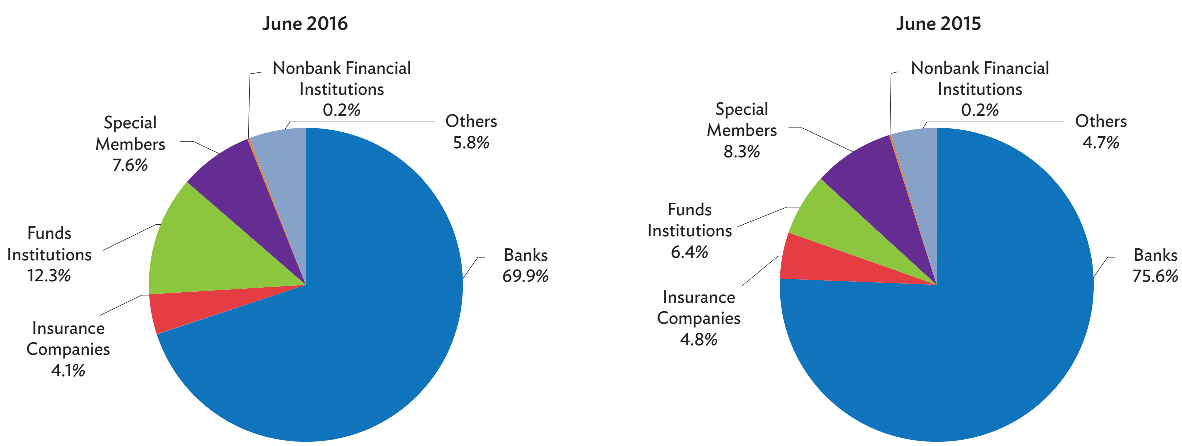
CNY = Chinese yuan, Q2 = second quarter.
Source: Based on data from Bloomberg LP.

Figure 5: Investor Profile across Bond Categories



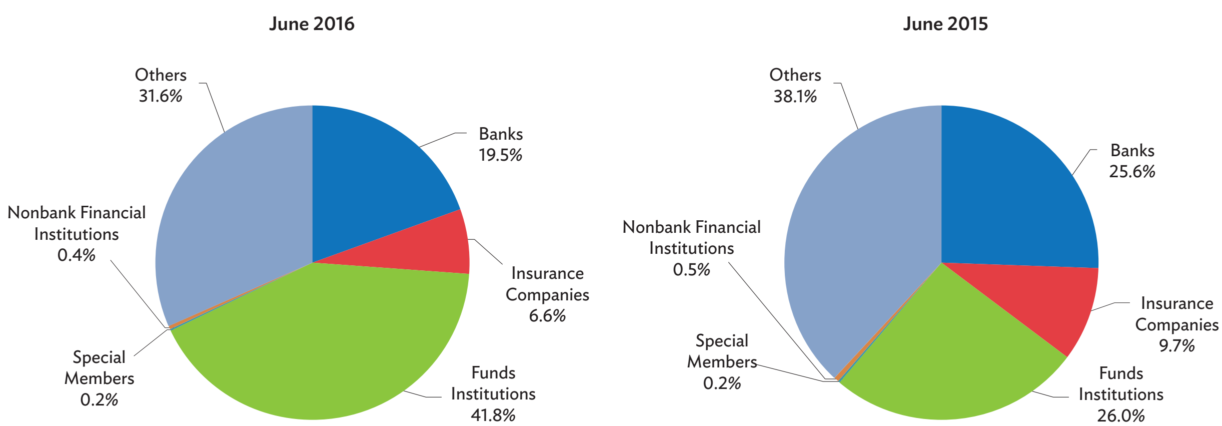
MTNs = medium-term notes.
Note: Data as of end-June 2016.
Source: *ChinaBond*.

Figure 3: Local Currency Treasury Bonds and Policy Bank Bonds Investor Profile



Source: *ChinaBond*.

Figure 4: Local Currency Corporate Bonds Investor Profile



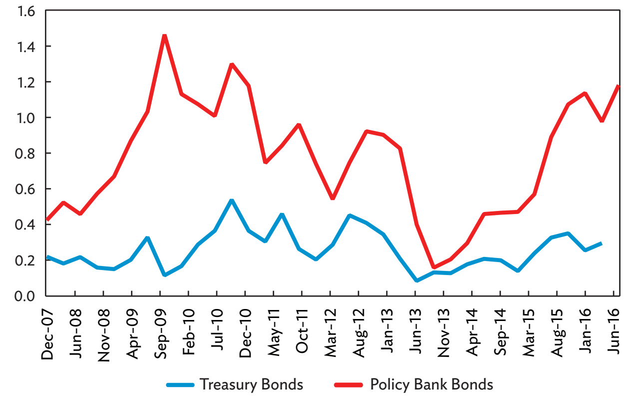
Source: *ChinaBond*.

Table 5: Notional Values of the People's Republic of China's Interest Rate Swap Market in Q2 2016

Interest Rate Swap Benchmarks	Notional Amount (CNY billion)	Percentage of Total Notional Amount (%)	Growth Rate (%)
	Q2 2016		q-o-q
7-Day Repo Rate	2,145.2	90.6	30.4
Overnight SHIBOR	53.0	2.2	(55.9)
3-Month SHIBOR	154.7	6.5	(33.9)
1-Year Term Deposit Rate	7.1	0.3	26.1
1-Year Lending Rate	8.0	0.3	23.6
3-Year Lending Rate	0.6	0.02	40.0
Total	**2,368.5**	**100.0**	**17.7**

( ) = negative, CNY = Chinese yuan, q-o-q = quarter-on-quarter, Q2 =second quarter, Repo = repurchase, SHIBOR = Shanghai Interbank Offered Rate.
Notes:
1. Growth rate computed based on notional amounts.
2. London Interbank Offered Rate, 1-Year Loan Prime Rate, and 5-Year Lending Rate had no transaction for Q2 2016.
Sources: *AsianBondsOnline* and *ChinaMoney*.

Figure 6: Turnover Ratios for Government Bonds



Source: *ChinaBond*.

Policy, Institutional, and Regulatory Developments

Green Bonds Program Expanded

On 6 April, the government launched a pilot program to allow PRC-based issuers to issue and list green bonds on the Shanghai Stock Exchange. To qualify as a green bond, the most important requirement is that only green assets and projects can be funded by the proceeds of the bond.

World Bank Group to Issue Special Drawing Rights-Denominated Bonds in the Interbank Bond Market

On 21 August, the PRC approved the International Bank for Reconstruction and Development of the World Bank Group to issue Special Drawing Rights-denominated bonds in the PRC's interbank bond market. The issue size will be SDR2 billion and the bond will be settled in renminbi.

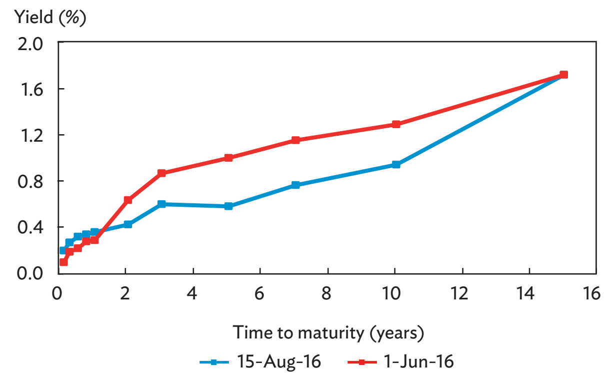
Hong Kong, China

Yield Movements

Hong Kong, China's Exchange Fund Bills and Notes yield curve, which generally tracks United States interest rate movements, shifted downward for most tenors between 1 June and 15 August. Yields for all tenors of 2 years or longer fell with the exception of the 15-year tenor, which remained unchanged. The largest decline was the yield for the 5-year tenor, which fell 42 basis points (bps). For tenors of 1 year or less, yields rose between 6 bps and 10 bps. The 2-year versus 10-year yield spread fell to 51 bps on 15 August from 65 bps on 1 June **(Figure 1)**.

Hong Kong, China's economy somewhat stabilized in the second quarter (Q2) of 2016, with gross domestic product growing 1.7% year-on-year (y-o-y) after growing only 0.8% y-o-y in the prior quarter. The increase in economic growth in Q2 2016 was largely due to improvements in external demand. Domestic demand further weakened, with personal consumption expenditures rising 0.6% y-o-y in Q2 2016 versus 1.2% in the previous quarter. Exports of goods rose 2.0% y-o-y in Q2 2016 after a decline of 3.6% y-o-y in the prior quarter. The government's forecast for full-year 2016 remains unchanged at 1.0%–2.0%. Inflationary pressures remain subdued given low external inflation. Consumer price inflation continued its downward trend, with consumer prices rising 2.3% y-o-y in July from 2.4% y-o-y in June.

Figure 1: Hong Kong, China's Benchmark Yield Curve—Exchange Fund Bills and Notes



Source: Based on data from Bloomberg LP.

Size and Composition

Hong Kong, China's local currency (LCY) bond market grew 6.6% quarter-on-quarter (q-o-q) and 15.2% y-o-y to reach HKD1,755 billion (USD226 billion) at the end of June **(Table 1)**. The q-o-q growth was mostly driven by increases in Exchange Fund Bills (EFBs) and corporate bonds.

The outstanding amount of EFBs rose 7.3% q-o-q in Q2 2016 on a relatively high level of new issuance of HKD618 billion for the quarter.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	HKD	USD	HKD	USD	HKD	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,523**	**196**	**1,646**	**212**	**1,755**	**226**	**(1.5)**	**2.0**	**6.6**	**15.2**
Government	846	109	957	123	1,013	131	(1.3)	(0.4)	5.8	19.8
Exchange Fund Bills	689	89	800	103	859	111	0.4	0.7	7.3	24.6
Exchange Fund Notes	64	8	56	7	53	7	(4.1)	(5.9)	(5.3)	(16.3)
Government Bonds	93	12	101	13	101	13	(11.3)	(4.5)	0.0	8.5
Corporate	677	87	688	89	742	96	(1.6)	5.1	7.8	9.6

( ) = negative, HKD = Hong Kong dollar, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period local currency–USD rates are used.
3. Growth rates are calculated from local currency base and do not include currency effects.
Sources: Hong Kong Monetary Authority and Bloomberg LP.

The Hong Kong Monetary Authority (HKMA) issued EFBs in Q2 2016 to help mop up liquidity due to increased inflows into Hong Kong, China's stock market ahead of its linking with the Shenzhen Stock Exchange.

Exchange Fund Notes (EFNs) further declined in Q2 2016, falling 5.3% q-o-q and 16.3% y-o-y, as HKMA preferred instead to issue Hong Kong Special Administrative Region (HKSAR) government bonds. In Q2 2016, the amount of HKSAR government bonds was unchanged on a q-o-q basis but rose 8.5% y-o-y on increased issuance, including an HKD2.5 billion 5-year HKSAR government bond and an HKD1.2 billion 10-year HKSAR government bond under the Institutional Bond Programme. In addition, an HKD10.0 billion 3-year HKSAR government bond was issued under the Retail Bond Programme.

The amount of corporate bonds outstanding rose 7.8% q-o-q and 9.6% y-o-y in Q2 2016 as issuers took advantage of lower Hong Kong dollar interest rates.

The top 30 nonbank issuers in Hong Kong, China had outstanding LCY bonds amounting to HKD140.2 billion at the end of June, representing 18.9% of total corporate bonds outstanding. The top 30 list of issuers was dominated by real estate firms and the financing vehicles of corporates **(Table 2)**. The Hong Kong Mortgage Corporation remained the top issuer with outstanding bonds of HKD29.39 billion. It was followed by the Link Finance (Cayman) 2009 with HKD8.9 billion of bonds outstanding and Sun Hung Kai Properties (Capital Market) with HKD8.85 billion. Among the top 30 nonbank issuers at the end of June, 6 were state-owned companies, and 8 were Hong Kong Exchange-listed firms.

The top 5 nonbank issuances in Q2 2016 came from Bestgain Real Estate Lyra, the Hong Kong Mortgage Corporation, Sun Hung Kai Properties (Capital Market), Hong Kong Electric Finance, and Swire Properties **(Table 3)**.

Policy, Institutional, and Regulatory Developments

Hong Kong, China Issues Silver Bonds

On 10 August, Hong Kong, China issued HKD3 billion worth of Silver Bonds under the Retail Bond Issuance Programme. The bonds, which can only be subscribed to by Hong Kong, China residents aged 65 years or older, pay interest on a semiannual basis. The coupon is based on the average rate of consumer price inflation in Hong Kong, China for the past 6 months or 2%, whichever is higher.

Table 2: Top 30 Nonbank Corporate Issuers in Hong Kong, China

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (HKD billion)	LCY Bonds (USD billion)			
1.	The Hong Kong Mortgage Corporation	29.39	3.79	Yes	No	Finance
2.	The Link Finance (Cayman) 2009	8.90	1.15	No	No	Finance
3.	Sun Hung Kai Properties (Capital Market)	8.85	1.14	No	No	Real Estate
4.	CLP Power Hong Kong Financing	8.46	1.09	No	No	Finance
5.	MTR Corporation (C.I.)	8.22	1.06	Yes	Yes	Transportation
6.	Hongkong Electric Finance	6.98	0.90	No	No	Finance
7.	HKCG (Finance)	6.94	0.89	No	No	Finance
8.	Swire Pacific	6.68	0.86	No	Yes	Diversified
9.	Wharf Finance	6.13	0.79	No	No	Finance
10.	NWD (MTN)	5.50	0.71	No	Yes	Finance
11.	Wheelock Finance	4.04	0.52	No	No	Finance
12.	Bestgain Real Estate Lyra	3.65	0.47	No	No	Real Estate
13.	Swire Properties MTN Financing	3.54	0.46	No	No	Finance
14.	Kowloon-Canton Railway	3.40	0.44	Yes	No	Transportation
15.	Urban Renewal Authority	3.30	0.43	Yes	No	Real Estate
16.	Emperor International Holdings	2.75	0.35	No	Yes	Real Estate
17.	Yue Xiu Property	2.30	0.30	No	No	Real Estate
18.	Chueng Kong Finance (MTN)	2.21	0.28	No	No	Finance
19.	Tencent Holdings	2.20	0.28	No	Yes	Comunications
20.	Airport Authority Hong Kong	2.05	0.26	Yes	No	Transportation
21.	Bohai International Capital	2.00	0.26	No	No	Iron and Steel
22.	China Energy Reserve and Chemicals Group Overseas	2.00	0.26	No	No	Oil
23.	Hong Kong Science and Technology Parks	1.71	0.22	Yes	No	Real Estate
24.	Cathay Pacific MTN Financing	1.70	0.22	No	Yes	Finance
25.	Wharf Finance (No. 1)	1.44	0.19	No	No	Finance
26.	Hysan (MTN)	1.40	0.18	No	Yes	Real Estate
27.	Nan Fung Treasury	1.31	0.17	No	No	Real Estate
28.	Henderson Land MTN	1.19	0.15	No	Yes	Finance
29.	Cheung Kong Bond Securities (02)	1.00	0.13	No	No	Finance
30.	Dragon Drays	1.00	0.13	No	No	Diversified
Total Top 30 Nonbank LCY Corporate Issuers		**140.19**	**18.07**			
Total LCY Corporate Bonds		**742.00**	**95.63**			
Top 30 as % of Total LCY Corporate Bonds		**18.9%**	**18.9%**			

LCY = local currency.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Hong Kong Monetary Authority data.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (HKD billion)
The Hong Kong Mortgage Corporation		
1-year bond	0.92	2.00
1-year bond	0.81	0.74
1-year bond	0.92	0.68
1-year bond	0.80	0.50
1-year bond	0.92	0.50
2-year bond	1.21	1.00
3-year bond	1.44	1.00
Bestgain Real Estate Lyra		
3-year bond	2.50	3.65
Sun Hung Kai Properties (Capital Market)		
10-year bond	2.50	0.50
10-year bond	2.56	0.34
Swire Properties		
7-year bond	2.25	0.20
10-year bond	2.65	0.20
Hong Kong Electric Finance		
15-year bond	2.58	0.31

HKD = Hong Kong dollar, Q2 = second quarter.
Source: Central Moneymarkets Unit, Hong Kong Monetary Authority.

Indonesia

Yield Movements

Between 1 June and 15 August, local currency (LCY) government bond yields in Indonesia declined for all tenors, which caused the entire yield curve to shift downward **(Figure 1)**. The yield for the 10-year maturity dropped the most, shedding 104 basis points (bps). Bond yields for all other tenors from the shorter-end through the longer-end of the curve declined an average of 80 bps. As a result, the yield spread between the 2-year and 10-year maturities narrowed to 32 bps on 15 August from 62 bps on 1 June.

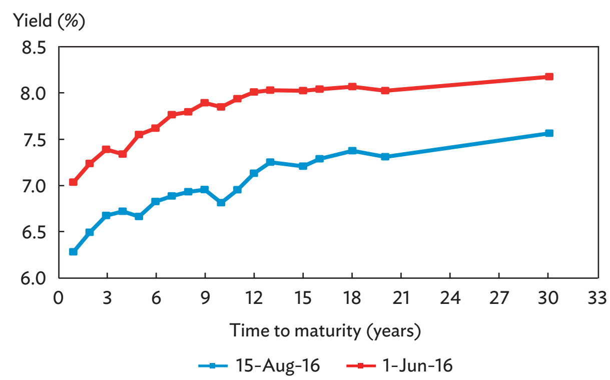
Declining yields across the length of the curve reflected, in part, strong demand from foreign investors as they continued to shore up their holdings of IDR-denominated bonds in search of yields. The delay in the United States Federal Reserve's interest rate hike has led offshore funds into emerging market assets amid a relatively low interest rate environment globally.

Also supportive of the overall drop in yields were more stable macroeconomic factors, including a generally benign inflation outlook, a stable Indonesian rupiah vis-à-vis the United States dollar, and a narrower current account deficit. In addition, policy and regulatory reforms initiated by the government, such as the Tax Amnesty Law, have helped boost sentiment in the LCY bond market (see Policy and Regulatory Developments).

The overall decline in yields across the curve was also driven by Bank Indonesia's accommodative monetary policy stance as it lowered the benchmark policy rate by 25 bps in June, reducing the previous policy rate by a cumulative 100 bps since the start of the year. Subsequently, Bank Indonesia introduced a new policy rate—the 7-day reverse repurchase rate—on 19 August to achieve a more "effective monetary policy transmission."

In its Bank of Governors meeting on 18–19 August, Bank Indonesia decided to keep the 7-day reverse repurchase rate steady at 5.25%. Bank Indonesia also kept unchanged the deposit facility rate at 4.50%, while it lowered by 100 bps the lending facility rate to 6.00%. Bank Indonesia noted that there is room for further monetary easing as long as macroeconomic stability is maintained.

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



Source: Based on data from Bloomberg LP.

Inflation is expected to remain within Bank Indonesia's target range of 3.0%–5.0% for full-year 2016. Consumer price inflation slowed to 3.6% year-on-year (y-o-y) in April and further to 3.3% y-o-y in May. A slight uptick in inflation to 3.5% y-o-y was noted in June, which coincided with increased demand for goods and services during the Muslim fasting month of Ramadan. However, inflation subsequently eased again to 3.2% y-o-y in July and 2.8% in August.

Indonesia's real gross domestic product (GDP) growth climbed to 5.2% y-o-y in the second quarter (Q2) of 2016 from 4.9% y-o-y in the first quarter (Q1) of 2016 on faster growth in consumption spending by the private sector (5.0% y-o-y) and the government (2.9% y-o-y). On the other hand, investment growth eased to 5.1% y-o-y and both exports and imports contracted during the quarter in review. On a quarter-on-quarter (q-o-q) and nonseasonally adjusted basis, real GDP growth climbed to 4.0% in Q2 2016 after contracting 0.4% in Q1 2016.

Size and Composition

The LCY bond market in Indonesia reached a size of IDR2,003.0 trillion (USD152 billion) at the end of June, climbing 5.2% q-o-q and 20.1% y-o-y in Q2 2016 **(Table1)**. Growth was driven by increases in both government and corporate bonds. Conventional bonds accounted for the largest component of the

Table 1: Size and Composition of the Local Currency Bond Market in Indonesia

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	IDR	USD	IDR	USD	IDR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,668,177**	**125**	**1,903,610**	**144**	**2,003,006**	**152**	**2.4**	**13.8**	**5.2**	**20.1**
Government	1,429,181	107	1,649,687	125	1,732,935	131	2.0	14.5	5.0	21.3
Central Govt. Bonds	1,356,434	102	1,575,115	119	1,646,846	125	3.9	19.9	4.6	21.4
of which: *Sukuk*	156,209	12	204,222	15	218,948	17	7.6	54.2	7.2	40.2
Central Bank Bills	72,748	5	74,572	6	86,089	7	(24.3)	(37.7)	15.4	18.3
of which: *Sukuk*	8,458	0.6	7,038	0.5	7,470	0.6	(4.0)	24.5	6.1	(11.7)
Corporate	238,996	18	253,923	19	270,071	20	5.0	9.9	6.4	13.0
of which: *Sukuk*	7,944	0.6	9,216	0.7	9,561	0.7	12.2	14.2	3.7	20.4

( ) = negative, IDR = Indonesian rupiah, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period local currency–USD rates are used.
3. Growth rates are calculated from local currency base and do not include currency effects.
4. The total stock of nontradable bonds as of end-June stood at IDR260.5 trillion.
Sources: Bank Indonesia; Directorate General of Budget Financing and Risk Management, Ministry of Finance; Indonesia Stock Exchange; Otoritas Jasa Keuangan; and Bloomberg LP.

aggregate bond stock with an 88.2% share of the total at the end of June. *Sukuk* (Islamic bonds) represented an 11.8% share.

Government Bonds. The outstanding amount of government bonds expanded to IDR1,732.9 trillion at the end of June, rising 5.0% q-o-q and 21.3% y-o-y. Growth stemmed largely from central government bonds, which comprise debt securities issued by the Ministry of Finance. The stock of central bank bills, known as *Sertifikat* Bank Indonesia (SBI), while smaller in size also contributed to overall growth in Q2 2016.

Central Government Bonds. The outstanding size of central government bonds, which comprise Treasury bills and bonds, reached IDR1,646.8 trillion at the end of June, up 4.6% q-o-q and 21.4% y-o-y. The government awarded more than its targeted amount in 11 out of the 13 auctions it conducted in Q2 2016, taking advantage of lower borrowing costs and increased demand from both onshore and offshore investors.

Domestic investors began shoring up their government bond portfolios following a regulation passed by Otoritas Jasa Keuangan earlier this year requiring insurance companies and pension funds to hold 20% of their portfolio in government bonds (conventional and *sukuk*) in 2016 and 30% in 2017. Also, foreign investors remain attracted to Indonesia's government bond market amid the low interest rate environment in the global market.

In Q2 2016, central government bond issuance stood at IDR118.3 trillion, down 26.1% q-o-q but up 32.8% y-o-y. On a q-o-q basis, issuance slowed due to the base effects generated by the high level of retail *sukuk* issuance in Q1 2016. New bond issuance in Q2 2016 comprised the government's weekly auctions of conventional and Islamic Treasury instruments. All seven auctions of Islamic bills and project-based *sukuk* during the quarter were awarded either in full or above target.

Following revisions to the 2016 budget that were approved by Parliament in late June, the government needs to fund a larger deficit estimated at IDR296.7 trillion, or the equivalent of 2.35% of GDP, which is up from IDR273.2 trillion, or 2.15% of GDP. As a result, net government securities issuance increased from IDR327.2 trillion to IDR364.9 trillion. The bulk of the issuance (74%) will be issued in local currency and the remaining amount (24%) will be sourced from international bond issuance. The budget deficit is expected to be funded partly by increased revenue collections from the Tax Amnesty Law.

Central Bank Bills. The outstanding amount of central bank bills, or SBI, climbed to IDR86.1 trillion at the end of June on double-digit growth rates of 15.4% q-o-q and 18.3% y-o-y. The central bank issues SBI as part of its monetary policy tools for liquidity management. Bank Indonesia auctions both conventional and shariah-compliant SBI on a monthly basis for maturities of 9 months and 1 year. Total issuance of SBI reached

IDR28.9 trillion in Q2 2016, down 24.4% q-o-q. On a y-o-y basis, however, SBI issuance increased 13 fold in Q2 2016 due to a low base effect as Bank Indonesia temporarily ceased issuance of conventional SBI in Q2 2015 while opting to utilize other tools for managing liquidity.

Corporate Bonds. The outstanding size of LCY corporate bonds in Indonesia totaled IDR270.1 trillion at the end of June, posting growth of 6.4% q-o-q and 13.0% y-o-y in Q2 2016. The corporate bond segment constitutes a small share of the LCY bond market in Indonesia, accounting for only 13.5% at the end of June. Conventional bond issues continued to comprise a majority of the corporate bond total, representing a share of 96.5%.

At the end of June, the top 30 LCY corporate bond issuers in Indonesia had aggregate LCY bonds outstanding that reached IDR207.3 trillion **(Table 2)**. These 30 issuers together comprised 76.7% of the total LCY corporate bond stock, with 20 firms among them tapping both the bond and equity markets for their financing needs. Eleven state-owned firms were among the top 30 corporate issuers at the end of June, including the three largest. The top 30 list was dominated in Q2 2016 by firms from the banking and financial sectors, while a few names from capital-intensive industries (e.g., energy, telecommunications, building construction, and property and real estate) were also included.

The top three issuers of corporate bonds at the end of June were all state-owned firms. Leading the list was Indonesia Eximbank, which maintained its rank as the largest corporate bond issuer in Indonesia in Q2 2016. Its aggregate bond stock increased to IDR25.5 trillion at the end of June, accounting for a 9.5% share of the total corporate bond stock. Climbing to the second spot was Bank Rakyat Indonesia, which ranked ninth in Q1 2016, with an outstanding bond stock of IDR12.0 trillion. Energy firm PLN dropped to the third spot with outstanding bonds valued at IDR11.7 trillion.

The volume of new corporate debt issues more than doubled in Q2 2016 to IDR32.9 trillion, up 139.2% q-o-q. On a y-o-y basis, new corporate debt issuance rose 39.5% in Q2 2016. In Q2 2016, a total of 21 firms tapped the debt securities market for their funding requirements, taking advantage of lower borrowing costs. Most issuers of corporate bonds were from the banking and financial sectors. A total of 47 bond series were issued during the quarter, all of which were conventional bonds except for Maybank Indonesia's issuance of *sukuk mudharabah* (profit-sharing bonds).

Table 3 lists some of the largest corporate bond issuers in Q2 2016. Bank Rakyat Indonesia issued a total of IDR4,350 billion worth of bonds in three tranches in May, the largest issuance in terms of aggregate size in Q2 2016. Indonesia Eximbank also raised IDR4,000 billion from a triple-tranche bond sale in June, while Federal International Finance raised IDR3,375 billion from a dual-tranche bond sale in April.

In Q2 2016, the new corporate bonds issued were mostly short-dated in terms of maturity, with 33 out of 47 bond series carrying maturities of 3 years or less. There were nine bond series carrying a maturity of 5 years and four bond series with 7 years. Among the new corporate bond issuance in Q2 2016, the longest-dated bond series was a 10-year maturity issued by Pelindo Gerbang Nusantara.

Foreign Currency Bonds. In June, the Indonesian government raised a total of EUR3.0 billion from a dual-tranche offering. The bond sale comprised a EUR1.5 billion 7-year bond priced to yield 2.772% with a coupon rate of 2.625%, and a EUR1.5 billion 12-year bond priced to yield 3.906% with a coupon rate of 3.75%. The bonds were well received, with the order book reaching EUR8.36 billion.

Also in June, the government sold JPY100 billion worth of samurai bonds via private placement to institutional investors in Japan. The offering comprised JPY62 billion of 3-year bonds with a coupon rate of 0.83% and JPY38 billion of 5-year bonds with a coupon rate of 1.16%. The samurai bonds were issued without a guarantee from the Japan Bank for International Cooperation.

Investor Profiles

Central Government Bonds. Foreign investors continued to shore up their holdings of Indonesian LCY government bonds, increasing their share to 39.1% of total LCY central government bonds outstanding at the end of June 2016 from 38.2% a year earlier **(Figure 2)**. In absolute value terms, foreign investors held a total of IDR644.0 trillion of central government bonds at the end of June. Foreign funds continue to invest in Indonesian government bonds

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in Indonesia

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (IDR billion)	LCY Bonds (USD billion)			
1.	Indonesia Eximbank	25,539	1.93	Yes	No	Banking
2.	Bank Rakyat Indonesia	12,000	0.91	Yes	Yes	Banking
3.	PLN	11,733	0.89	Yes	No	Energy
4.	Indosat	11,033	0.84	No	Yes	Telecommunications
5.	Bank Tabungan Negara	10,950	0.83	Yes	Yes	Banking
6.	Adira Dinamika Multifinance	10,198	0.77	No	Yes	Finance
7.	Astra Sedaya Finance	9,395	0.71	No	No	Finance
8.	Telekomunikasi Indonesia	8,995	0.68	Yes	Yes	Telecommunications
9.	Bank Internasional Indonesia	8,880	0.67	No	Yes	Banking
10.	Federal International Finance	7,681	0.58	No	No	Finance
11.	Bank Pan Indonesia	7,560	0.57	No	Yes	Banking
12.	Perum Pegadaian	7,059	0.53	Yes	No	Finance
13.	Bank CIMB Niaga	6,865	0.52	No	Yes	Banking
14.	Bank Permata	6,482	0.49	No	Yes	Banking
15.	Sarana Multigriya Finansial	6,241	0.47	Yes	No	Finance
16.	Jasa Marga	5,900	0.45	Yes	Yes	Toll Roads, Airports, and Harbors
17.	Bank OCBC NISP	4,785	0.36	No	Yes	Banking
18.	Waskita Karya	4,675	0.35	Yes	Yes	Building Construction
19.	Toyota Astra Financial Services	4,591	0.35	No	No	Finance
20.	Agung Podomoro Land	4,575	0.35	No	Yes	Property and Real Estate
21.	Indofood Sukses Makmur	4,000	0.30	No	Yes	Food and Beverages
22.	Surya Artha Nusantara Finance	3,541	0.27	No	No	Finance
23.	Bank Mandiri	3,500	0.26	Yes	Yes	Banking
24.	Medco-Energi International	3,500	0.26	No	Yes	Petroleum and Natural Gas
25.	Bumi Serpong Damai	3,315	0.25	No	Yes	Property and Real Estate
26.	Indomobil Finance Indonesia	3,114	0.24	No	No	Finance
27.	Antam	3,000	0.23	Yes	Yes	Mining
28.	Wahana Ottomitra Multiartha	2,828	0.21	No	Yes	Finance
29.	Mandiri Tunas Finance	2,825	0.21	No	No	Finance
30.	Summarecon Agung	2,500	0.19	No	Yes	Property and Real Estate
Total Top 30 LCY Corporate Issuers		**207,260**	**15.69**			
Total LCY Corporate Bonds		**270,071**	**20.44**			
Top 30 as % of Total LCY Corporate Bonds		**76.7%**	**76.7%**			

IDR = Indonesian rupiah, LCY = local currency, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Indonesia Stock Exchange data.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (IDR billion)
Bank Rakyat Indonesia		
370-day bond	7.50	1,212
3-year bond	8.20	2,437
5-year bond	8.70	701
Indonesia Eximbank		
370-day bond	7.50	688
3-year bond	8.20	1,060
5-year bond	8.70	2,252
Federal International Finance		
370-day bond	8.50	868
3-year bond	9.15	2,507
Bank Pan Indonesia		
5-year bond	9.15	2,000
7-year bond	9.60	100
Waskita Karya		
3-year bond	9.25	2,000
Bank OCBC NISP		
370-day bond	7.50	837
2-year bond	8.00	380
3-year bond	8.25	783
Astra Sedaya Finance		
370-day bond	7.95	770
3-year bond	8.50	1,230

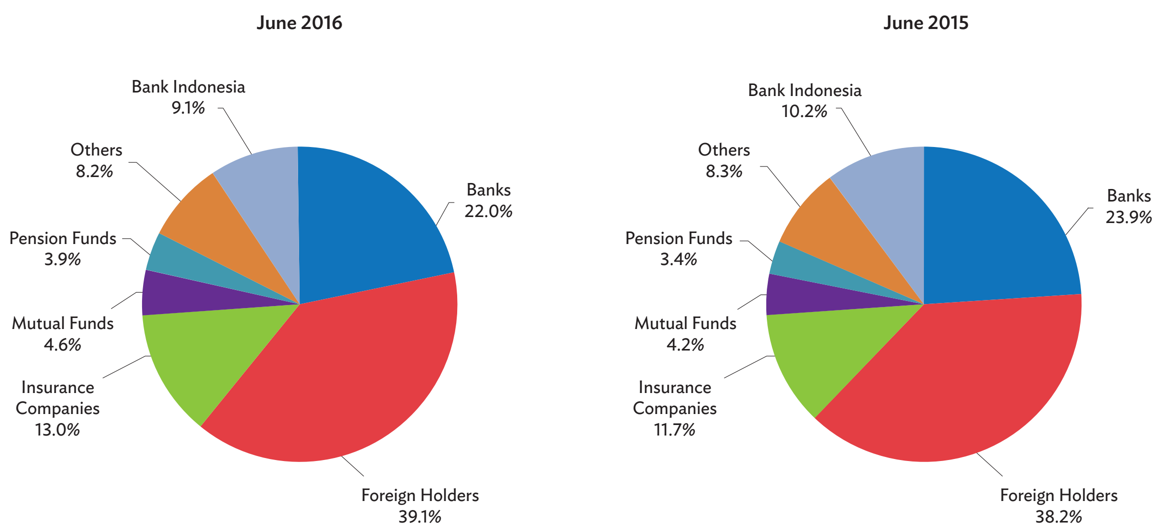
IDR = Indonesian rupiah, Q2 = second quarter.
Source: Indonesia Stock Exchange.

as the yields are among the highest in emerging East Asia. In addition, foreign governments and central banks also hold Indonesian LCY government bonds as part of their foreign reserves.

Foreign investors increased their holdings of long-term maturities, with a 47.7% share of their holdings at the end of June placed in bonds with maturities of more than 10 years, compared with 44.7% at the end of December. **(Figure 3)**. About 35.9% of their holdings were in medium-dated tenors, which are those with maturities of between more than 5 years and 10 years. Bonds with maturities of 2 years or less accounted for only 5.3% of aggregate foreign holdings.

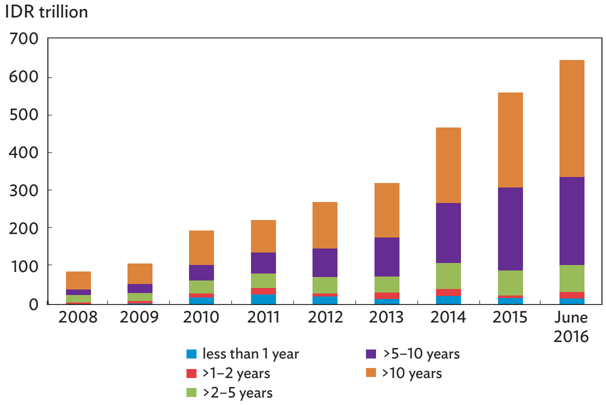
Among domestic investors, banking institutions were the largest holders of Indonesian Treasury instruments in Q2 2016. However, their share declined to 22.0% at the end of June from 23.9% a year earlier. On the other hand, insurance companies and pension funds increased their holdings of central government bonds at the end of June to 13.0% and 3.9%, respectively. Partly contributing to this increase was the regulation issued by Otoritas Jasa Keuangan earlier this year requiring insurance companies and pension funds to keep 20% of their portfolios in government bonds in 2016 and 30% in 2017.

Figure 2: Local Currency Central Government Bonds Investor Profile



Source: Directorate General of Budget Financing and Risk Management, Ministry of Finance.

Figure 3: Foreign Holdings of Local Currency Central Government Bonds by Maturity

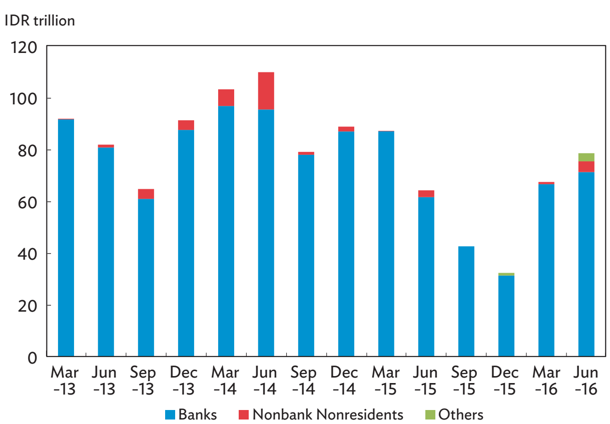


IDR = Indonesian rupiah.
Source: Directorate General of Budget Financing and Risk Management, Ministry of Finance.

Other nonbank investors, particularly mutual funds and other investors, recorded increases in their holdings of central government bonds, although their shares of the total remained small at less than 10.0% each. Meanwhile, Bank Indonesia's holdings of Treasury instruments declined to 9.1% at the end of June from 10.2% a year earlier.

Central Bank Bills. Central bank bills, or SBI, were still largely held by banking institutions, which had a share of 90.7% at the end of June **(Figure 4)**. Nonbank nonresident investors accounted for a 5.3% share, while the remaining 4.0% was accounted for by other investors.

Figure 4: Local Currency Central Bank Bills Investor Profile



IDR = Indonesian rupiah.
Notes:
1. For end-September and end-December 2015, nonresidents had no holdings of *Sertifikat* Bank Indonesia (SBI).
2. For end-March 2016, nonresidents held IDR0.9 trillion of SBI.
Source: Bank Indonesia.

Ratings Update

In June, S&P Global Ratings affirmed Indonesia's sovereign credit rating at BB+. The outlook on the rating was positive. S&P Global Ratings cited Indonesia's improved policy and institutional settings, credible monetary policy, and buoyant economic growth as the key factors in its decision.

Policy, Institutional, and Regulatory Developments

Finance Ministry Removes Withholding Tax on Interest Payments for Foreign Currency Government Bonds

In June, Indonesia's Ministry of Finance provided tax incentives to investors in conventional and Islamic foreign currency-denominated government bonds by removing the withholding tax on interest payments. A withholding tax of 15% had been levied for Indonesian residents while a 20% tax was levied for nonresidents. The removal of the withholding tax will help lower the government's borrowing costs on its foreign currency government bonds. This will also help corporate bonds receive better pricing as government bonds are normally used as a benchmark for pricing. The regulation is effective retroactively from 1 January 2016.

Parliament Approves Tax Amnesty Law

In June, Parliament approved the Tax Amnesty Law to lure wealthy residents to repatriate funds parked in tax havens. The new law levies tax rates of 2.0%–5.0% for assets that are declared and repatriated and 4.0%–10.0% for assets that are only declared. Investment instruments have been prepared by the government for the placement of repatriated funds, which will need to be placed in the Indonesian capital market for a period of at least 3 years.

The government estimates that the measures will attract IDR4,000 trillion in declared assets and IDR1,000 trillion in repatriated funds. The government expects to raise IDR165 trillion in revenues from this program, which will help fund the larger deficit included in the 2016 revised budget. The tax amnesty program runs from 18 July 2016 to 31 March 2017.

Parliament Approves 2016 Revised State Budget

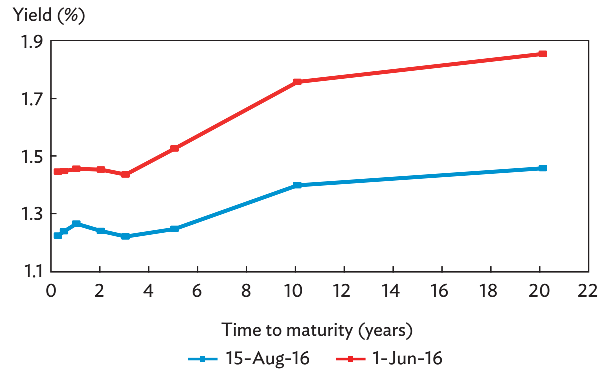
On 28 June, the Indonesian Parliament approved the revised 2016 state budget, which widened the programmed budget deficit to IDR296.7 trillion, or the equivalent of 2.35% of GDP from the equivalent of 2.15% of GDP in the original budget. The revised state budget estimates revenue of IDR1,786.2 trillion against spending of IDR2,082.9 trillion. Parliament also approved cuts in diesel subsidies and in the budgets for most ministries. The underlying macroeconomic assumptions for the revised budget were (i) annual GDP growth of 5.2%, (ii) annual inflation of 4.0%, (iii) an exchange rate of IDR13,500 per USD1, (iv) a 3-month Treasury bill rate of 5.5%, and (v) an Indonesian crude oil price of USD40 per barrel.

Republic of Korea

Yield Movements

Yields on local currency (LCY) government bonds fell for all maturities between 1 June and 15 August, resulting in a downward shift in the yield curve **(Figure 1)**. The decrease in yields ranged from 19 basis points (bps) for the 1-year tenor to 41 bps for the 30-year tenor. The fall in yields was influenced by the Bank of Korea's policy rate cut in June, the United Kingdom's decision to leave the European Union, and declines in Treasury bond yields in major economies. The yield spread between the 2-year and 10-year tenors narrowed 15 bps during the review period.

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



Source: Based on data from Bloomberg LP.

The Bank of Korea's Monetary Policy Board decided in its 14 July and 11 August meetings to maintain the base rate at 1.25%. The last policy rate cut occurred on 9 June when the board lowered the base rate by 25 bps.

Real gross domestic product (GDP) growth stood at 0.8% quarter-on-quarter (q-o-q) and 3.3% year-on-year (y-o-y) in the second quarter (Q2) of 2016, up from first quarter growth rates of 0.5% q-o-q and 2.8% y-o-y. The higher q-o-q growth in Q2 2016 was led by stronger household spending, domestic investment, and exports on the expenditure side; and more buoyant economic activity in the manufacturing and utility sectors on the production side. The stronger y-o-y growth in the second quarter also stemmed from more robust household spending, domestic investment, and exports; as well as faster growth in construction, manufacturing, and services sectors. In its economic outlook announced in July, the Bank of Korea forecast real GDP growth of 2.4% y-o-y for the second half of 2016 and 2.7% for full-year 2016.

Consumer price inflation remained relatively low, with the Consumer Price Index (CPI) inflation rate slipping to 0.4% y-o-y in August from 0.7% y-o-y in July. The Bank of Korea forecast in July that consumer price inflation would rise to 1.3% y-o-y in the second half of 2016 and settle at 1.1% for full-year 2016.

Size and Composition

LCY bonds outstanding in the Republic of Korea expanded 1.0% q-o-q and 5.4% y-o-y in Q2 2016, leveling off at KRW2,064.0 trillion (USD1,792 billion) at the end of June **(Table 1)**. The outstanding stock of LCY government bonds climbed 1.6% q-o-q and 5.9% y-o-y in Q2 2016 to reach KRW853.0 trillion at the end of June, bolstered by an expansion in LCY central government bonds.

Q2 2016 issuance of LCY government bonds tallied KRW87.0 trillion, up 0.7% q-o-q but down 1.6% y-o-y. The q-o-q uptick was driven by increases in the issuance of Korea Treasury Bonds and Monetary Stabilization Bonds. The y-o-y downturn was mainly led by lower Monetary Stabilization Bond issuance.

The outstanding size of LCY corporate bonds in the Republic of Korea expanded 0.5% q-o-q and 5.1% y-o-y in Q2 2016, buoyed by increases in stocks of financial debentures and the bonds of privately owned corporates, leveling off at KRW1,211.0 trillion at the end of June. In Q2 2016, LCY corporate bond issuance was valued at KRW90.4 trillion, down 5.5% q-o-q and 33.7% y-o-y.

The top 30 corporate issuers of LCY bonds had a cumulative outstanding bond stock worth KRW768.4 trillion (or 63.5% of total LCY corporate bonds outstanding) at the end of June, led by Korea Housing Finance Corporation **(Table 2)**. The relatively large LCY corporate bond issuances in Q2 2016 were from two domestic banks—Industrial Bank of Korea and NongHyup Bank—and from a railway operator—Korea Rail Network Authority **(Table 3)**.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	KRW	USD	KRW	USD	KRW	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,958,273**	**1,756**	**2,044,415**	**1,788**	**2,064,024**	**1,792**	**3.1**	**10.0**	**1.0**	**5.4**
Government	805,593	722	839,618	734	853,009	741	2.0	15.0	1.6	5.9
Central Bank Bonds	188,310	169	181,390	159	181,420	158	1.8	8.2	0.02	(3.7)
Central Government Bonds	527,583	473	566,919	496	583,402	507	2.7	8.6	2.9	10.6
Industrial Finance Debentures	89,700	80	91,309	80	88,188	77	(1.6)	120.5	(3.4)	(1.7)
Corporate	1,152,680	1,033	1,204,797	1,054	1,211,015	1,051	3.8	6.8	0.5	5.1

( ) = negative, KRW = Korean won, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period local currency–USD rates are used.
3. Growth rates are calculated from local currency base and do not include currency effects.
4. Central government bonds include Korea Treasury bonds, National Housing bonds, and Seoul Metro bonds.
Sources: EDAILY *BondWeb* and The Bank of Korea.

Investor Profile

Insurance companies and pension funds comprised the largest investor group in LCY government bonds in the Republic of Korea with holdings equivalent to 31.8% of the total LCY government bond stock at the end of March **(Figure 2)**. Nonfinancial corporations were the smallest investor group with less than a 1% share. In the 12 months through the end of March, households and nonprofit institutions recorded the biggest increase in their share of LCY government bond holdings with a gain of 1.2 percentage points, while banks posted the biggest decline at 1.8 percentage points.

In the LCY corporate bond market, insurance companies and pension funds are also the largest investor group with holdings constituting 37.4% of the total corporate bond market at the end of March **(Figure 3)**. In the 12 months through the end of March, this investor group and other financial institutions (except banks) posted relatively large increases in corporate bond holding shares of 2.0 and 2.1 percentage points, respectively. Over the same period, the share of LCY corporate bonds held by households and nonprofit institutions posted the sharpest y-o-y drop at –2.3 percentage points.

Foreign investors' net LCY bond outflow in the Republic of Korea declined to KRW1,229 billion in Q2 2016 from KRW4,149 billion in the previous quarter. On a monthly basis, net foreign bond investment turned negative in June at –KRW2,748 billion following positive amounts of KRW888 billion and KRW631 billion in May and April, respectively **(Figure 4)**. In July, foreign investors' net bond investment totaled KRW588 billion.

Ratings Update

S&P Global Ratings announced in August that it had raised its long-term sovereign credit rating on the Republic of Korea to AA from AA–, giving the new rating a stable outlook, and has affirmed its short-term rating at A-1+. S&P Global Ratings stated that its rating upgrade was due to the Republic of Korea's "strong record of steady growth," which has "generated a prosperous economy, greater fiscal and monetary flexibility, and continual improvements in external metrics." The rating agency also stated that despite expectations of slower GDP growth in the next 3–5 years compared with pre-global financial crisis growth levels, it believes that the economy's prospects are "superior" to that of most developed economies.

Rating and Investment Information (R&I) reported in July that it has affirmed its foreign currency issuer and domestic currency issuer ratings on the Republic of Korea at A+ and AA–, respectively, giving stable outlooks for both ratings. R&I stated that its rating affirmation was made based on the Republic of Korea's "sluggish" economic recovery, "prudent" fiscal management amid "modest" government debt levels, and "consistent" surpluses in the current account.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in the Republic of Korea

	Issuers	Outstanding Amount		State-Owned	Listed on		Type of Industry
		LCY Bonds (KRW billion)	LCY Bonds (USD billion)		KOSPI	KOSDAQ	
1.	Korea Housing Finance Corporation	92,724	80.5	Yes	No	No	Housing Finance
2.	NH Investment & Securities	59,816	51.9	Yes	Yes	No	Securities
3.	Mirae Asset Daewoo Securities	55,327	48.0	No	Yes	No	Securities
4.	Korea Land & Housing Corporation	50,705	44.0	Yes	No	No	Real Estate
5.	Korea Investment and Securities	48,329	42.0	No	No	No	Securities
6.	Mirae Asset Securities	40,282	35.0	No	Yes	No	Securities
7.	Industrial Bank of Korea	38,942	33.8	Yes	Yes	No	Banking
8.	Hana Financial Investment	34,824	30.2	No	No	No	Securities
9.	Korea Deposit Insurance Corporation	29,650	25.7	Yes	No	No	Insurance
10.	Korea Electric Power Corporation	23,970	20.8	Yes	Yes	No	Electricity, Energy, and Power
11.	Hyundai Securities	23,491	20.4	No	No	No	Securities
12.	Korea Expressway	22,000	19.1	Yes	No	No	Transport Infrastructure
13.	Korea Rail Network Authority	19,160	16.6	Yes	No	No	Transport Infrastructure
14.	Kookmin Bank	18,673	16.2	No	No	No	Banking
15.	Shinhan Bank	18,563	16.1	No	No	No	Banking
16.	Woori Bank	17,865	15.5	Yes	Yes	No	Banking
17.	Samsung Securities	17,757	15.4	No	Yes	No	Securities
18.	Daishin Securities	16,514	14.3	No	Yes	No	Securities
19.	NongHyup Bank	15,960	13.9	Yes	No	No	Banking
20.	Korea Gas	15,429	13.4	Yes	Yes	No	Gas Utility
21.	Small & Medium Business Corporation	13,510	11.7	Yes	No	No	SME Development
22.	Korea Eximbank	12,260	10.6	Yes	No	No	Banking
23.	Korea Student Aid Foundation	11,690	10.1	Yes	No	No	Student Loan
24.	Standard Chartered First Bank Korea	11,380	9.9	No	No	No	Banking
25.	Hyundai Capital Services	10,489	9.1	No	No	No	Consumer Finance
26.	Korea Water Resources Corporation	10,441	9.1	Yes	No	No	Water
27.	Shinhan Card	10,169	8.8	No	No	No	Credit Card
28.	Korea Railroad Corporation	9,680	8.4	Yes	No	No	Transport Infrastructure
29.	Shinyoung Securities	9,659	8.4	No	Yes	No	Securities
30.	NongHyup	9,190	8.0	Yes	No	No	Diversified
Total Top 30 LCY Corporate Issuers		**768,448.1**	**667.2**				
Total LCY Corporate Bonds		**1,211,015.0**	**1,051.4**				
Top 30 as % of Total LCY Corporate Bonds		**63.5%**	**63.5%**				

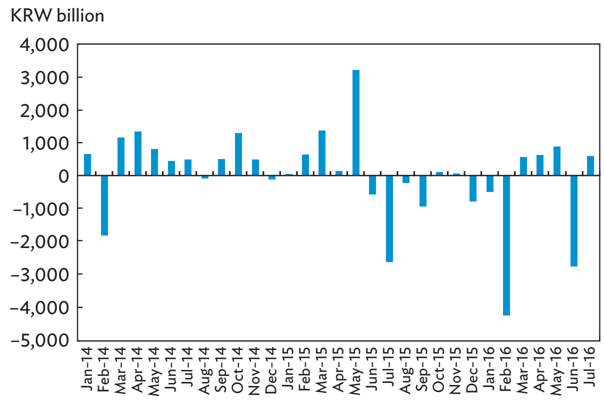
KOSDAQ = Korean Securities Dealers Automated Quotations, KOSPI = Korea Composite Stock Price Index, KRW = Korean won, LCY = local currency, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Sources: *AsianBondsOnline* calculations based on Bloomberg LP and EDAILY *BondWeb* data.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
NongHyup Bank		
0.75-year bond	1.32	470
1-year bond	1.34	770
1-year bond	1.34	500
5-year bond	1.69	400
Industrial Bank of Korea		
3-year bond	1.56	640
10-year bond	2.37	400
Korea Rail Network Authority		
30-year bond	2.13	390

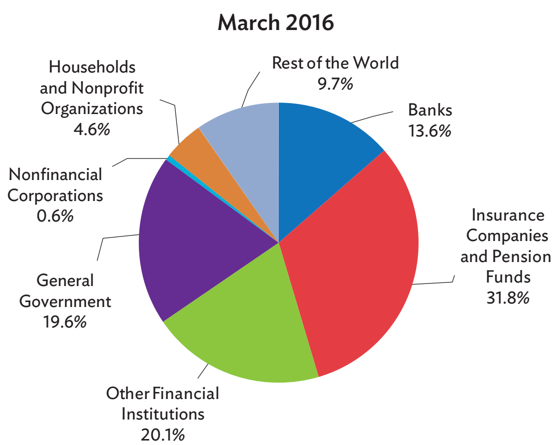
KRW = Korean won, Q2 = second quarter.
Note: Coupon rates for 0.75- and 1-year bonds of NongHyup Bank are indicative yields at end-June 2016.
Source: Based on data from Bloomberg LP.

Figure 4: Net Foreign Investment in Local Currency Bonds in the Republic of Korea



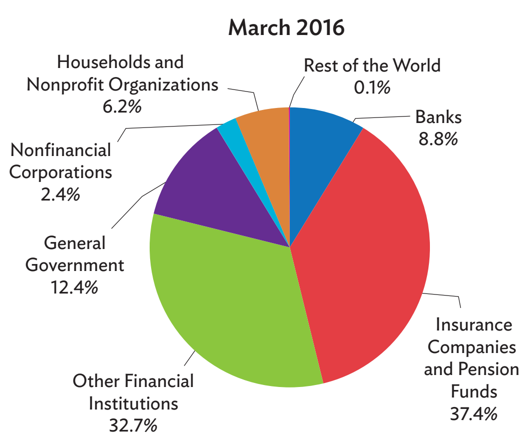
KRW = Korean won.
Source: Financial Supervisory Service.

Figure 2: Local Currency Government Bonds Investor Profile



Sources: *AsianBondsOnline* and The Bank of Korea.

Figure 3: Local Currency Corporate Bonds Investor Profile



Sources: *AsianBondsOnline* and The Bank of Korea.

Policy, Institutional, and Regulatory Developments

Financial Services Commission Introduces Plan to Develop "Mega-Investment Banks"

The Financial Services Commission (FSC) announced in August its plan to develop "mega-investment banks" by enabling investment banks to acquire more than KRW10 trillion of equity capital and to broaden their scope of new business. The FSC stated that it plans for securities firms with more than KRW4 trillion of equity capital to be allowed to sell promissory notes and conduct foreign exchange transactions; for securities firms with equity capital of nearly KRW10 trillion to create investment management accounts and conduct property trust business; and for securities firms with equity capital of less than KRW4 trillion to be subjected to certain reforms to enable them to secure enough capital for corporate financing purposes. The plan is envisioned to take effect starting in 2017.

Financial Services Commission to Apply Foreign Currency Liquidity Coverage Ratio to Banks

The FSC reported in June its plan to apply a foreign currency liquidity coverage ratio rule in 2017. The rule will require commercial banks to hold 60% of their foreign exchange debt in the form of high-quality liquid assets starting in 2017, with the ratio increasing to 70% in 2018 and 80% in 2019.

Malaysia

Yield Movements

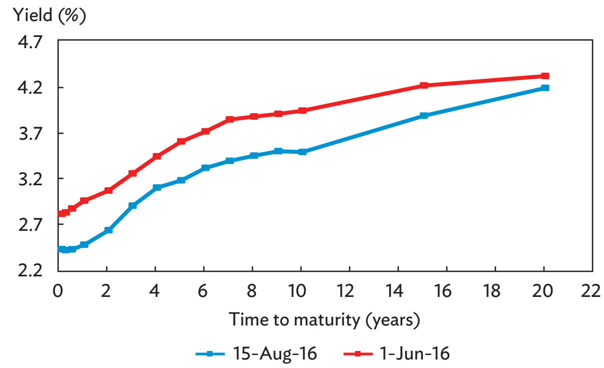
Between 1 June and 15 August, Malaysian local currency (LCY) government bond yields fell for all tenors on lowered expectations of a United States Federal Reserve interest rate hike this year and the unexpected policy rate cut by Bank Negara Malaysia (BNM) in July **(Figure 1)**. Except for the 20-year tenor, which fell only 13 basis points (bps), yields for all tenors fell 41 bps on average. The 2-year versus 10-year spread was barely changed during the review period at 85 bps from 87 bps.

In its monetary policy meeting on 13 July, BNM decided to lower its overnight policy rate by 25 bps to 3.0%. The ceiling and floor rates for the overnight policy rate corridor were also reduced to 3.25% and 2.75%, respectively. BNM's decision to cut rates was seen by the market as a preemptive move due to heightened risks to global and domestic growth prospects, following the United Kingdom's referendum on leaving the European Union, commonly known as "Brexit." Brexit has also further dampened market expectations of a Federal Reserve rate hike this year, providing more support to domestic bonds.

Foreign holdings of LCY bonds remained high in the second quarter (Q2) of 2016 as demand for higher-yielding emerging East Asian LCY bonds persists amid low global interest rates. Data from BNM showed an increase in foreign holdings of central government debt securities from MYR191 billion in March to MYR207 billion in June and to MYR213 billion in July. As a result, the Malaysian ringgit remained supported during the review period despite a temporary depreciation due to Brexit and oil price volatilities.

Inflation continued to decelerate from 2.6% year-on-year (y-o-y) in March to 1.6% y-o-y in June and further to 1.1% y-o-y in July, as communications and transportation prices continued to post y-o-y decreases. In its monetary policy meeting on 13 July, BNM lowered its forecast for full-year 2016 inflation to 2.0%–3.0% from 2.5%–3.5%, citing as reasons the lapse in the impact of the Goods and Services Tax implemented last year and low global energy prices.

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



Source: Based on data from Bloomberg LP.

Malaysia's economic growth slowed to 4.0% y-o-y in Q2 2016 from 4.2% y-o-y in Q1 2016, primarily due to an accelerated contraction in the agriculture sector of 7.9% y-o-y following a decline of 3.8% y-o-y in Q1 2016. All other industries posted annual increases in Q2 2016. The slower growth was driven by continued weakness in exports, which increased 1.0% y-o-y in Q2 2016. On the other hand, economic growth was supported by the accelerated increase in gross fixed capital formation of 6.1% y-o-y in Q2 2016, up from only 0.1% y-o-y in the previous quarter. Private final consumption expenditure and government spending also posted larger annual increases in Q2 2016.

Size and Composition

The Malaysian LCY bond market grew 2.0% quarter-on-quarter (q-o-q) to MYR1,163 billion (USD289 billion) at the end of June **(Table 1)**. The rise was most notable in the government bond sector as the amount of outstanding corporate bonds barely changed from the previous quarter. On a y-o-y basis, the LCY bond market expanded at a faster pace of 8.2%. Total government bonds outstanding amounted to MYR644 billion, while corporate bonds totaled MYR519 billion. The share of *sukuk* (Islamic bonds) in Malaysia's LCY bond market continued to exceed that of conventional bonds, with a majority share of 55% at the end of June.

Table 1: Size and Composition of the Local Currency Bond Market in Malaysia

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	MYR	USD	MYR	USD	MYR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,076**	**285**	**1,141**	**293**	**1,163**	**289**	**0.2**	**2.1**	**2.0**	**8.2**
Government	608	161	628	161	644	160	(0.7)	(0.6)	2.5	5.9
Central Government Bonds	557	148	579	148	600	149	4.9	9.6	3.8	7.9
of which: *Sukuk*	209	55	223	57	232	57	7.1	9.9	3.9	10.8
Central Bank Bills	23	6	22	6	15	4	(59.1)	(73.6)	(29.1)	(34.5)
of which: *Sukuk*	4	1	0	0	0	0	(78.4)	(88.1)	–	(100.0)
Sukuk Perumahan Kerajaan	28	7	28	7	28	7	14.3	80.0	0.0	1.8
Corporate	468	124	512	131	519	129	1.4	6.0	1.4	11.0
of which: *Sukuk*	337	89	366	94	375	93	2.7	11.8	2.5	11.3

( ) = negative, – = not applicable, MYR = Malaysian ringgit, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period local currency–USD rate is used.
3. Growth rates are calculated from local currency base and do not include currency effects.
4. Sukuk Perumahan Kerajaan are Islamic bonds issued by the Government of Malaysia to refinance funding for housing loans to government employees and to extend new housing loans.
Sources: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST) and Bloomberg LP.

Government Bonds. LCY government bonds outstanding increased 2.5% q-o-q to MYR644 billion at the end of June, led by increases in the outstanding stock of Malaysian Government Securities and Government Investment Issues. Meanwhile, the outstanding stock of central bank bills continued to decline. On a y-o-y basis, government bonds outstanding rose 5.9% in Q2 2016.

Government bond issuance in Q2 2016 was almost on par with the previous quarter as the higher issuance of Malaysian Government Securities was offset by lower issuance of Government Investment Issues and Treasury bills.

Corporate Bonds. LCY corporate bonds slightly increased 1.4% q-o-q to MYR519 billion at the end of June from MYR512 billion at the end of March. *Sukuk* continued to dominate the Malaysian LCY corporate bond market with their share of the total rising to 72.2% in Q2 2016 from 71.4% in Q1 2016.

At the end of June, the aggregate bonds outstanding of the top 32 LCY corporate bond issuers in Malaysia amounted to MYR295.3 billion, or 56.8% of the total LCY corporate bond market **(Table 2)**. Financial firms, including banks, comprised the majority of the 32 largest corporate bond issuers with total bonds outstanding worth MYR163.6 billion. Highway operator Project Lebuhraya Usahasama remained the largest issuer with outstanding bonds valued at MYR30.6 billion, followed by state-owned mortgage firm Cagamas with MYR26.3 billion.

Issuance of corporate bonds increased slightly to MYR34.1 billion in Q2 2016 from MYR33.5 billion in Q1 2016. *Sukuk* issuance continued to exceed that of conventional bonds, with their share of total issuance rising to 58.9% at the end of June from 55.4% at the end of March. By type of instrument, Islamic medium-term notes had the highest share of total issuance at 43.2%, followed by conventional commercial paper with a share of 25.7%. **Table 3** lists the notable corporate bond issuances in Q2 2016.

The largest corporate bond issuers in Q2 2016 were from government-owned entities, mostly in the utilities sector. Sarawak Energy, an electricity generator and transmitter company, issued Islamic medium-term notes comprising an MYR800 million 15-year tranche and a MYR700 million 20-year tranche with coupon rates of 5.04% and 5.18%, respectively. Pengurusan Air SPV, a water services company, also issued Islamic medium-term notes comprising a MYR400 million 5-year tranche, an MYR800 million 7-year tranche, and a MYR250 million 10-year tranche with coupon rates of 4.04%, 4.23%, and 4.40%, respectively.

Table 2: Top 32 Issuers of Local Currency Corporate Bonds in Malaysia

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (MYR billion)	LCY Bonds (USD billion)			
1.	Project Lebuhraya Usahasama	30.6	7.6	No	No	Transport, Storage, and Communications
2.	Cagamas	26.3	6.5	Yes	No	Finance
3.	Danainfra Nasional	25.2	6.3	Yes	No	Finance
4.	Prasarana	20.6	5.1	Yes	No	Transport, Storage, and Communications
5.	Khazanah	20.0	5.0	Yes	No	Finance
6.	Maybank	14.9	3.7	No	Yes	Banking
7.	Pengurusan Air	13.8	3.4	Yes	No	Energy, Gas, and Water
8.	Perbadanan Tabung Pendidikan Tinggi Nasional	11.0	2.7	Yes	No	Finance
9.	CIMB Bank	10.1	2.5	No	No	Banking
10.	Sarawak Energy	9.5	2.4	Yes	No	Energy, Gas, and Water
11.	Jimah East Power	9.0	2.2	Yes	No	Energy, Gas, and Water
12.	Public Bank	8.6	2.1	No	No	Banking
13.	Aman Sukuk	6.3	1.6	Yes	No	Construction
14.	Rantau Abang Capital	6.0	1.5	Yes	No	Finance
15.	RHB Bank	5.4	1.3	No	No	Banking
16.	Turus Pesawat	5.3	1.3	Yes	No	Transport, Storage, and Communications
17.	CIMB Group Holdings	5.2	1.3	Yes	No	Finance
18.	BGSM Management	5.1	1.3	No	No	Transport, Storage, and Communications
19.	1Malaysia Development	5.0	1.2	Yes	No	Finance
20.	Danga Capital	5.0	1.2	Yes	No	Finance
21.	Putrajaya Holdings	4.9	1.2	Yes	No	Property and Real Estate
22.	Manjung Island Energy	4.9	1.2	No	No	Energy, Gas, and Water
23.	YTL Power International	4.8	1.2	No	Yes	Energy, Gas, and Water
24.	Celcom Networks	4.5	1.1	No	No	Transport, Storage, and Communications
25.	Malakoff Power	4.4	1.1	No	No	Energy, Gas, and Water
26.	Bank Pembangunan Malaysia	4.4	1.1	Yes	No	Banking
27.	GOVCO Holdings	4.3	1.1	Yes	No	Finance
28.	AM Bank	4.2	1.0	No	Yes	Banking
29.	Cagamas MBS	4.2	1.0	Yes	No	Finance
30.	Tanjung Bin Power	4.0	1.0	No	No	Energy, Gas, and Water
31.	Telekom Malaysia	4.0	1.0	Yes	Yes	Transport, Storage, and Communications
32.	Valuecap	4.0	1.0	Yes	No	Finance
Total Top 32 LCY Corporate Issuers		**295.3**	**73.3**			
Total LCY Corporate Bonds		**519.4**	**128.9**			
Top 32 as % of Total LCY Corporate Bonds		**56.8%**	**56.8%**			

LCY = local currency, MYR = Malaysian ringgit, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST) data.

Table 3 : Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR million)
Sarawak Energy		
15-year Islamic MTN	5.04	800
20-year Islamic MTN	5.18	700
Pengurusan Air		
5-year Islamic MTN	4.04	400
7-year Islamic MTN	4.23	800
10-year Islamic MTN	4.40	250
GOVCO Holdings Berhad		
7-year Islamic MTN	4.27	300
10-year Islamic MTN	4.40	400
15-year Islamic MTN	4.73	550
CIMB Bank		
Perpetual Capital Securities - Tier 1	5.80	1,000

MTN = medium-term note, MYR = Malaysian ringgit, Q2 = second quarter.
Source: Bank Negara Malaysia Bond Info Hub.

Investor Profile

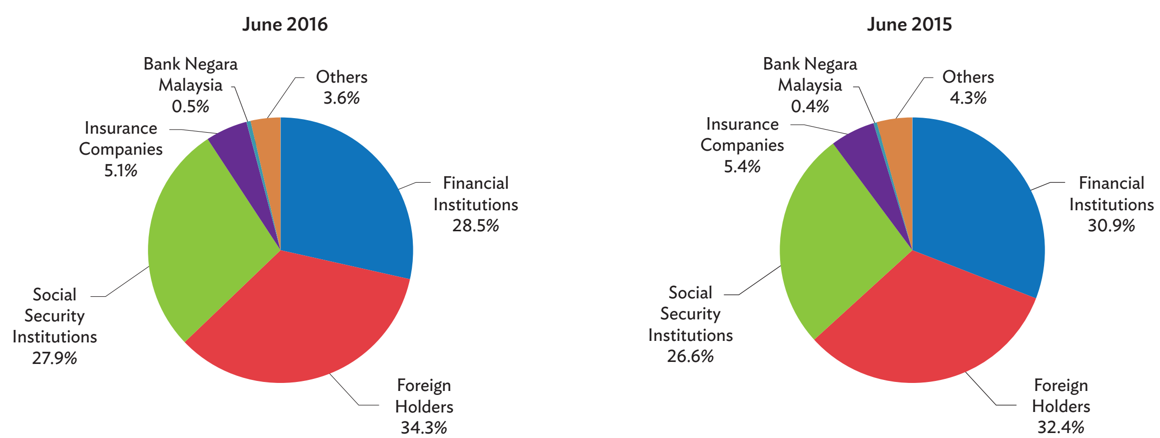
Foreign investors' holdings of LCY government bonds were up in June from a year earlier, both in nominal terms and as a share of the total. In a change from a year earlier, foreign holdings accounted for the largest investor share at the end of June at 34.3%, surpassing financial institutions' share of 28.5%. Social security institutions remained the third largest holders of government bonds at the end of June with a share of 27.9%, down from 26.6% a year earlier.

Malaysia's corporate bond market investor profile was barely changed in June compared with a year earlier **(Figure 3)**. Domestic banks, both commercial and Islamic, continued to account for the largest share of LCY corporate bonds at 46.5%, followed by life insurance companies with a share of 31.5%.

Ratings Update

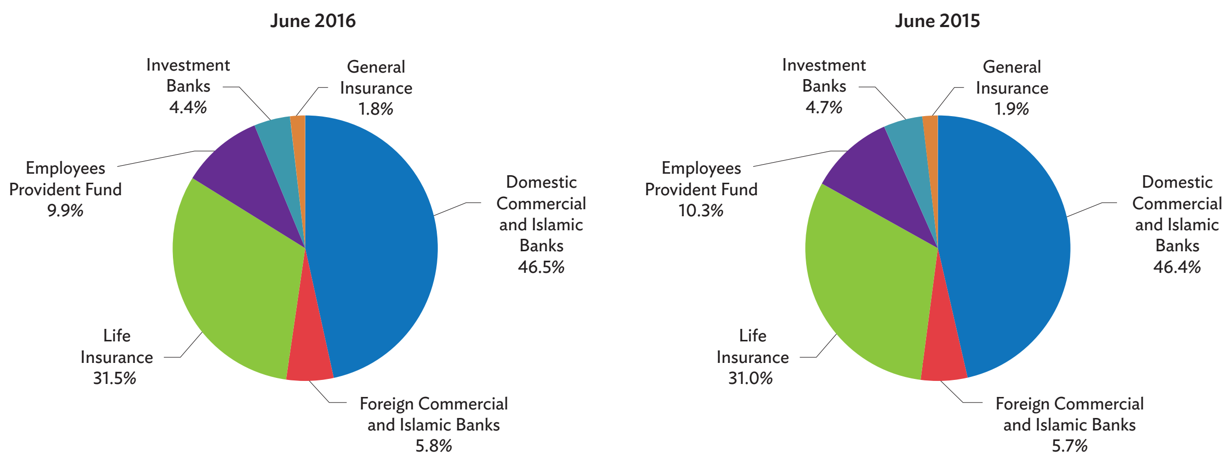
In August, Fitch Ratings (Fitch) affirmed its long-term foreign currency and local currency issuer default ratings of A– for Malaysia, with a stable outlook. Fitch cited as reasons for its decision Malaysia's strong net external creditor position and current account surplus, and strong (despite slower) economic growth relative to its A– rated peers. However, Fitch also noted weakness in Malaysia's governance standards, citing ongoing issues with state-owned 1Malaysia Development Berhad as well as concerns over its federal government debt and deficit levels.

Figure 2: Local Currency Government Bonds Investor Profile



Notes:
1. "Others" include statutory bodies, nominees and trustee companies, and cooperatives and unclassified items.
2. Data are based on the Bank Negara Malaysia Monthly Statistical Bulletin Table 3.1.5: Federal Government Debt Issued Domestically, Classification by Holder.
Source: Bank Negara Malaysia.

Figure 3: Local Currency Corporate Bonds Investor Profile



Note: The Employees Provident Fund's bond holdings data are as of end-December 2015 since data are based on EPF's annual report.
Source: Bank Negara Malaysia and the EPF.

Policy, Institutional, and Regulatory Developments

Bank Negara Malaysia and Financial Markets Association of Malaysia Announce Kuala Lumpur USD–MYR Reference Rate

In June, BNM and the Financial Markets Association of Malaysia announced the adoption of a new methodology for the computation of the Malaysian ringgit's exchange rate. The new rate shall be known as the Kuala Lumpur USD–MYR Reference Rate. Effective 18 July, the new reference rate will be based on the daily weighted average volume of the interbank USD–MYR foreign exchange spot rate transactions of domestic financial institutions between 8 a.m. and 3 p.m. BNM stated that the new methodology promotes transparency and is based on underlying trades, while the previous methodology was based on the submission of quotations by selected banks.

In addition, the official closing time for the onshore ringgit foreign exchange market will be extended from 5 p.m. to 6 p.m.

Bank Negara Malaysia and Otoritas Jasa Keuangan Sign Bilateral Agreement

In August, BNM and Otoritas Jasa Keuangan signed a bilateral agreement under the Association of Southeast Asian Nations Banking Integration Framework to further promote banking and financial integration between Malaysia and Indonesia. The implementation of the agreement will involve BNM allowing Qualified Association of Southeast Asian Nations Banks from Indonesia to operate in Malaysia. The agreement envisions a greater role for Malaysian and Indonesian banks in facilitating cross-border trade and investment between the two markets.

Philippines

Yield Movements

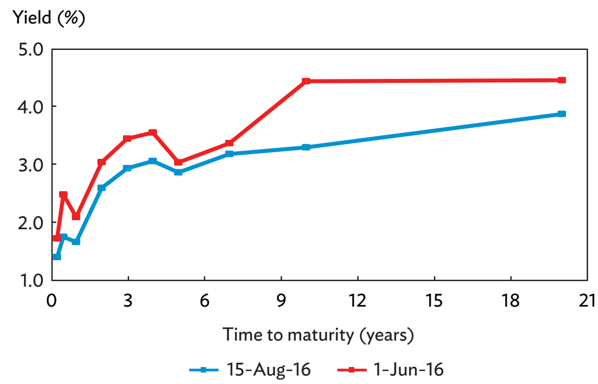
Local currency (LCY) government bond yields fell for all maturities between 1 June and 15 August. The yield drop ranged from 17 basis points (bps) for the 5-year tenor to 114 bps for the 10-year tenor **(Figure 1)**. The drop in yields during this period was driven by strong demand for LCY government securities—especially the Treasury bills that were auctioned in July—as well as the United States Federal Reserves' delay in raising interest rates and the United Kingdom's vote to exit from the European Union. Meanwhile, the yield spread between the 2-year and 10-year tenors narrowed 69 bps during the review period.

The Monetary Board of the Bangko Sentral ng Pilipinas (BSP) decided during its meetings on 23 June and 11 August to keep the interest rate on the overnight reverse repurchase facility at 3.0%. Interest rates on the overnight lending and deposit facilities were also left unchanged. The BSP noted that inflation in the Philippines continued to be "manageable."

The headline inflation rate, based on the Consumer Price Index, stood at 1.9% year-on-year (y-o-y) in July, unchanged from the previous month. In the second quarter (Q2) of 2016, consumer price inflation averaged 1.5% y-o-y, up from 1.1% y-o-y in the previous quarter. In the first half of 2016, the headline inflation rate averaged 1.3% y-o-y. Consumer price inflation has continued to remain below the Government of the Philippines' 2016–2018 inflation target range of 3.0%±1.0 percentage point.

Real gross domestic product growth was robust at 6.9% y-o-y in the first half of 2016, buoyed by relatively strong growth in household expenditure, government spending, and domestic investment on the demand side; and in the industrial and services sectors on the supply side. On a quarterly basis, real gross domestic product growth accelerated to 7.0% y-o-y in Q2 2016 from 6.8% y-o-y in the previous quarter on the back of faster growth in household spending, government expenditure, and domestic investment; as well as an expansion in the services sector.

Figure 1: Philippines' Benchmark Yield Curve—Local Currency Government Bonds



Source: Based on data from Bloomberg LP.

Size and Composition

The LCY bond market exhibited mixed trends in Q2 2016, falling 0.4% q-o-q but rising 0.9% y-o-y to reach PHP4,688 billion (USD99 billion) at the end of June **(Table 1)**. The q-o-q decline was induced by a quarterly contraction in Treasury bonds and corporate bonds, while the y-o-y growth stemmed from annual increases in Treasury bills and corporate bonds. At the end of June, government bonds accounted for more than 80% of total bonds outstanding.

Banks remained the largest issuer group in the LCY corporate bond market, with the value of their issued bonds comprising 28.3% of the total LCY corporate bond market at the end of June, followed by property firms with a 24.4% share **(Figure 2)**. Compared to June of the previous year, the share of banks registered the biggest drop among all issuer groups, while property firms posted the largest increase.

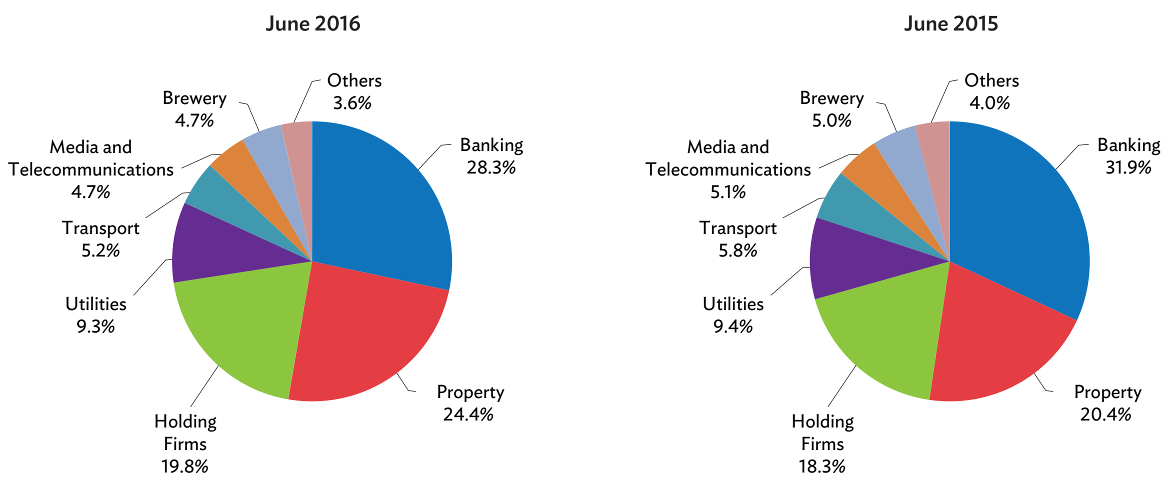
The top 30 corporate bond issuers accounted for a combined PHP722.9 billion worth of outstanding LCY bonds at the end of June, representing 89.5% of the LCY corporate bond market **(Table 2)**.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	PHP	USD	PHP	USD	PHP	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**4,645**	**103**	**4,706**	**102**	**4,688**	**99**	**(0.8)**	**3.3**	**(0.4)**	**0.9**
Government	3,896	86	3,893	85	3,880	82	(0.5)	2.0	(0.3)	(0.4)
Treasury Bills	275	6	279	6	288	6	(1.1)	(4.6)	3.2	4.6
Treasury Bonds	3,541	79	3,539	77	3,517	75	(0.2)	3.7	(0.6)	(0.7)
Others	80	2	76	2	76	2	(12.4)	(30.9)	0.0	(5.6)
Corporate	749	17	813	18	808	17	(2.0)	10.5	(0.6)	7.9

( ) = negative, PHP = Philippine peso, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg end-of-period local currency–USD rates are used.
3. Growth rates are calculated from a local currency base and do not include currency effects.
4. "Others" comprise bonds issued by government agencies, entities, and corporations for which repayment is guaranteed by the Government of the Philippines. These include bonds issued by Power Sector Assets and Liabilities Management (PSALM) and the National Food Authority, among others.
5. Peso Global Bonds (PHP-denominated bonds payable in US dollars) are not included.
Sources: Bloomberg LP and Bureau of the Treasury.

Figure 2: Local Currency Corporate Bonds Outstanding by Sector



Source: Based on data from Bloomberg LP.

LCY bond issuance in Q2 2016 stood at PHP182.2 billion, down 4.0% q-o-q but up 62.3% y-o-y. Government bond issues, comprising mainly Treasury bills and bonds, were valued at PHP175.2 billion, were down 1.1% q-o-q but up 93.8% y-o-y. Only one corporate bond was sold in Q2 2016—Ayala Land's 9.5-year bond worth PHP7 billion and carrying a 4.75% fixed interest rate—resulting in total corporate bond issuance declining 44.0% q-o-q and 67.9% y-o-y.

Investor Profile

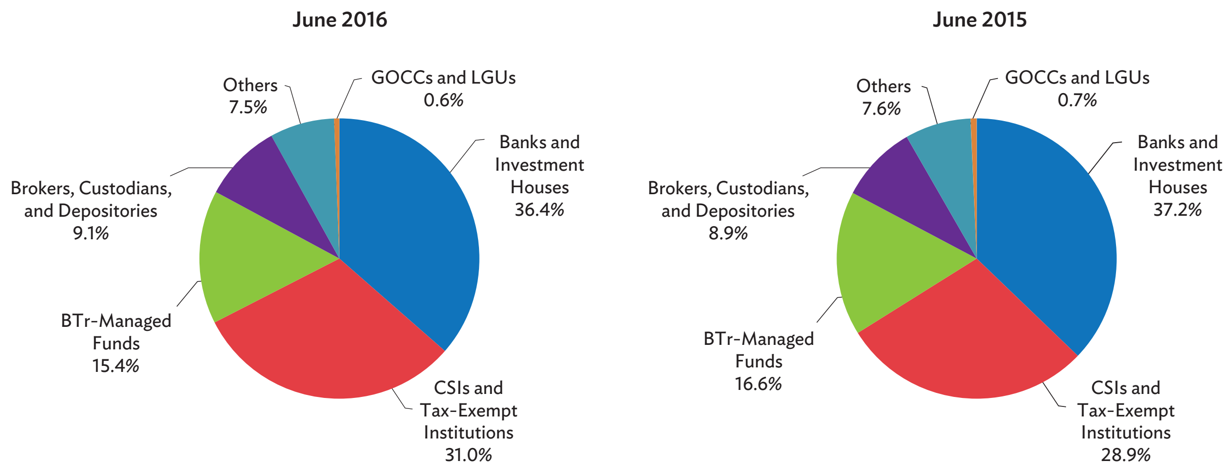
The largest investor group in the LCY government bond market comprises banks and investment houses, which had holdings equivalent to 36.4% of the total LCY government bond market at the end of June **(Figure 3)**. This share of the market was down from a year earlier. The shares of all other investor groups declined as well on a y-o-y basis except for contractual savings and tax exempt institutions, as well as brokers, custodians, and depositories.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in the Philippines

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (PHP billion)	LCY Bonds (USD billion)			
1.	Ayala Land	71.2	1.5	No	Yes	Property
2.	Metrobank	46.8	1.0	No	Yes	Banking
3.	SM Prime	45.0	1.0	No	Yes	Property
4.	Ayala Corporation	40.0	0.8	No	Yes	Holding Firms
5.	San Miguel Brewery	37.8	0.8	No	No	Brewing
6.	BDO Unibank	37.5	0.8	No	Yes	Banking
7.	Philippine National Bank	34.6	0.7	No	Yes	Banking
8.	Aboitiz Equity Ventures	32.0	0.7	No	Yes	Holding Firms
9.	Filinvest Land	32.0	0.7	No	Yes	Property
10.	JG Summit	30.0	0.6	No	Yes	Holding Firms
11.	SM Investments	27.3	0.6	No	Yes	Holding Firms
12.	Meralco	23.5	0.5	No	Yes	Electricity, Energy, and Power
13.	Security Bank	23.0	0.5	No	Yes	Banking
14.	Rizal Commercial Banking Corporation	22.1	0.5	No	Yes	Banking
15.	GT Capital	22.0	0.5	No	Yes	Holding Firms
16.	South Luzon Tollway	18.3	0.4	No	No	Transport
17.	Globe Telecom	17.0	0.4	No	Yes	Telecommunications
18.	East West Bank	16.8	0.4	No	Yes	Banking
19.	Maynilad Water Services	16.3	0.3	No	No	Water and Wastewater Services
20.	MCE Leisure (Philippines)	15.0	0.3	No	No	Casinos and Gaming
21.	Philippine Long Distance Telephone Company	15.0	0.3	No	Yes	Telecommunications
22.	Union Bank of the Philippines	14.0	0.3	No	Yes	Banking
23.	First Metro Investment Corporation	12.0	0.3	No	No	Banking
24.	Robinsons Land	12.0	0.3	No	Yes	Property
25.	Manila North Tollways	11.9	0.3	No	No	Transport
26.	MTD Manila Expressway	11.5	0.2	No	No	Transport
27.	Energy Development Corporation	10.5	0.2	No	Yes	Electricity, Energy, and Power
28.	Aboitiz Power	10.0	0.2	No	Yes	Electricity, Energy, and Power
29.	8990 Holdings	9.0	0.2	No	Yes	Property
30	Filinvest Development	8.8	0.2	No	Yes	Holding Firms
Total Top 30 LCY Corporate Issuers		**722.9**	**15.3**			
Total LCY Corporate Bonds		**807.9**	**17.1**			
Top 30 as % of Total LCY Corporate Bonds		**89.5%**	**89.5%**			

LCY = local currency, PHP = Philippine peso, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

Figure 3: Local Currency Government Bonds Investor Profile



BTr = Bureau of the Treasury, CSIs = contractual savings institutions, GOCCs = government-owned or -controlled corporations, LGUs = local government units.
Source: Bureau of the Treasury.

Policy, Institutional, and Regulatory Developments

Bangko Sentral ng Pilipinas Further Liberalizes Foreign Exchange Rules

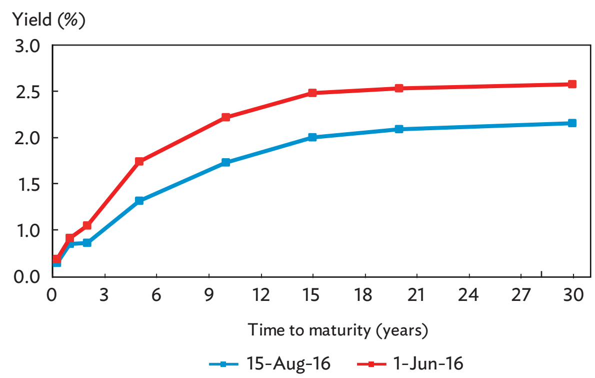
The BSP announced in August that its Monetary Board approved further liberalization of its foreign exchange rules and regulations in line with the Philippine economy's increasing integration with the global economy. The new measures include, among others, increasing the amount of foreign exchange that local residents, both individuals and corporations, can purchase from the banking system, as well as allowing the sale of foreign exchange by banks and their foreign exchange entities for resident-to-resident transactions.

Singapore

Yield Movements

Local currency (LCY) government bond yields in Singapore fell for all tenors between 1 June and 15 August **(Figure 1)**. The yield curve for Singapore Government Securities (SGS) flattened as yields continued to decline, with yields falling more sharply at the longer-end than the shorter-end of the curve. During the review period, yields for bonds with 1-year maturities and below declined an average of 5 basis points (bps). Yields for bonds with 2-year maturities dropped 19 bps, while yields fell an average of 45 bps for the 5-year through 30-year maturities. The spread between the 2-year and 10-year tenors narrowed to 87 bps on 15 August from 117 bps on 1 June.

Figure 1: Singapore's Benchmark Yield Curve–Local Currency Government Bonds



Source: Based on data from Bloomberg LP.

The yields for SGS bonds declined on increased demand, especially as the United States (US) Federal Reserve has continued to delay its much-anticipated interest rate hike, while the fallout from the United Kingdom's vote to exit the European Union has sent jitters through financial markets, causing investors to seek safe havens. The yield spread between 10-year Singapore bonds and 10-year US Treasuries declined from 38 bps on 1 June to 18 bps on 15 August. Continued weakness in global demand, which negatively affects export-oriented economies such as Singapore, and the persistence of deflation also contributed to the drop in bond yields.

Singapore's gross domestic product (GDP) grew 2.1% year-on-year (y-o-y) during the second quarter (Q2) of 2016, a rate of expansion that was unchanged from the first quarter (Q1). The manufacturing sector recorded positive growth of 1.1% y-o-y in Q2 2016, a reversal from the 0.5% y-o-y decline in Q1 2016, while construction sector growth moderated to 3.3% y-o-y in Q2 2016 from 4.0% y-o-y in Q1 2016. The services sector registered growth of 1.4% y-o-y in Q2 2016, down from 1.7% y-o-y in the previous quarter. On a quarter-on-quarter (q-o-q) and seasonally adjusted annualized basis, GDP expanded 0.3% in Q2 2016, a slight improvement from 0.1% growth in Q1 2016.

The Ministry of Trade and Industry has narrowed Singapore's 2016 GDP growth forecast range to 1%–2% from 1%–3%, mainly due to external factors such as a weaker global outlook following the British referendum to leave the European Union, weaker growth momentum in the US, and a continued slowdown in investments and economic restructuring in the People's Republic of China.

Consumer prices fell 0.7% y-o-y in July, which was unchanged from June and also the 21st consecutive month of deflation. The continued contraction in transportation costs and housing and utilities costs accounted for most of the decline. The Monetary Authority of Singapore (MAS) noted the slowdown in housing rentals stemming from the large supply of new residential units available this year, the likelihood that low global oil prices will persist given ample supply and low global demand, and expectations of a lower wage-growth trajectory as the domestic labor market eases. These factors will continue to contribute to deflation in Singapore, which MAS is forecasting at between −1.0% and 0.0% for full-year 2016.

Size and Composition

Singapore's LCY bonds outstanding were SGD314 billion (USD233 billion) at the end of June **(Table 1)**. Growth remained sluggish in Q2 2016, inching up a mere 0.2% q-o-q. On a y-o-y basis, the LCY bond market contracted 4.9%.

Table 1: Size and Composition of the Local Currency Bond Market in Singapore

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	SGD	USD	SGD	USD	SGD	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**330**	**245**	**314**	**233**	**314**	**233**	**3.0**	**5.5**	**0.2**	**(4.9)**
Government	197	147	184	136	182	135	2.8	4.2	(1.1)	(8.0)
SGS Bills and Bonds	105	78	110	81	109	81	5.3	5.1	(0.5)	3.7
MAS Bills	92	68	74	55	73	54	0.0	3.3	(1.9)	(21.3)
Corporate	133	99	130	96	133	98	3.4	7.4	2.0	(0.3)

( ) = negative, MAS = Monetary Authority of Singapore, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, SGD = Singapore dollar, SGS = Singapore Government Securities, USD = United States dollar, 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. SGS bills and bonds do not include the special issue of Singapore Government Securities held by the Singapore Central Provident Fund.
3. Bloomberg LP end-of-period local currency–USD rates are used.
4. Growth rates are calculated from local currency base and do not include currency effects.
Sources: Bloomberg LP, Monetary Authority of Singapore, and Singapore Government Securities.

Government Bonds. LCY government bonds outstanding decreased 1.1% q-o-q to SGD182 billion at the end of June as the outstanding stocks of SGS bills and bonds and MAS bills posted q-o-q decreases. In Q2 2016, SGS bond issuance amounted to SGD6.4 billion, mainly due to a reopening of a 7-year SGS bond and new issuances of 10-year SGS bonds. SGD4.2 billion of SGS bills were redeemed in Q2 2016, which nearly balanced out the SGD4.5 billion worth of SGS bills that were issued during the quarter.

The outstanding stock of MAS bills declined 1.9% q-o-q in Q2 2016 to SGD73 billion. In y-o-y terms, the stock of MAS bills declined 21.3% from SGD92 billion in Q2 2015. New issuance of MAS bills amounted to SGD69.7 billion, reflecting a drop of 2.5% q-o-q and 21.3% y-o-y.

Corporate Bonds. Based on *AsianBondsOnline* estimates, the outstanding stock of LCY corporate bonds reached SGD133 billion at the end of June, up 2.0% q-o-q but down 0.3% y-o-y.

At the end of June, the top 30 largest LCY corporate bond issuers accounted for a combined SGD68 billion worth of notes, or a 51.3% share of the total corporate bond stock **(Table 2)**. Singapore's Housing and Development Board topped the list with outstanding bonds worth SGD20.4 billion. United Overseas Bank was a distant second with total bonds valued at SGD4.7 billion. Temasek Financial I, a wholly owned financing subsidiary of state-owned investment company Temasek Holdings, had total bonds outstanding of SGD3.6 billion.

Among the 30 largest corporate bond issuers, 4 were state-owned agencies, while the rest comprised a diverse set of issuers from the banking, consumer goods, education, finance, real estate, transportation, and utilities sectors.

A downside development in the LCY bond market in Q2 2016 concerns Swiber Holdings, a large Singapore oil services company, which in August defaulted on its coupon payments for SGD150 million worth of notes maturing in August 2018 and with a coupon rate of 6.5%. Despite being able to redeem bonds worth SGD130 million due in June and SGD75 million worth of bonds due in July, Swiber Holdings applied to be placed under judicial management review. Four SGD-denominated notes worth SGD460 million and one renminbi-denominated note worth CNY450 million remain to be paid. The global downturn in the oil and gas industry since 2014 has led to a shortage of projects for energy services firms, which in turn puts strain on their coupon and loan payments. With more notes from Swiber Holdings and other oil and gas industry firms due to mature in 2016–2017, it remains to be seen how the bond market and banking industry will accommodate this stress.

In Q2 2016, a total of 22 companies issued new LCY corporate debt amounting to SGD4.6 billion, reflecting a 41.3% q-o-q rise but a decline of 18.4% y-o-y. The largest issuance in Q2 2016 was United Overseas Bank's perpetual bond worth SGD750 million. It was followed by the Housing and Development Board's 5-year bond sale worth SGD675 million. **Table 3** presents the notable corporate bond issues in Q2 2016.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in Singapore

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (SGD billion)	LCY Bonds (USD billion)			
1.	Housing and Development Board	20.4	15.2	Yes	No	Real Estate
2.	United Overseas Bank	4.7	3.5	No	Yes	Banking
3.	Temasek Financial I	3.6	2.7	Yes	No	Finance
4.	Land Transport Authority	3.5	2.6	Yes	No	Transportation
5.	Capitaland	3.0	2.2	No	Yes	Real Estate
6.	DBS Bank	2.7	2.0	No	Yes	Banking
7.	FCL Treasury	2.4	1.8	No	No	Finance
8.	SP Powerassets	1.9	1.4	No	No	Utilities
9.	Hyflux	1.7	1.3	No	Yes	Utilities
10.	Olam International	1.7	1.3	No	Yes	Consumer Goods
11.	Keppel Corporation	1.7	1.3	No	Yes	Diversified
12.	Public Utilities Board	1.7	1.2	Yes	No	Utilities
13.	City Developments Limited	1.6	1.2	No	Yes	Real Estate
14.	DBS Group Holdings	1.5	1.1	No	Yes	Banking
15.	Oversea-Chinese Banking Corporation	1.5	1.1	No	Yes	Banking
16.	Neptune Orient Lines	1.3	1.0	No	Yes	Transportation
17.	Capitaland Treasury	1.2	0.9	No	No	Finance
18.	Singtel Group Treasury	1.2	0.9	No	No	Finance
19.	Mapletree Treasury Services	1.1	0.8	No	No	Finance
20.	Capitamalls Asia Treasury	1.0	0.7	No	No	Finance
21.	Singapore Airlines	1.0	0.7	No	Yes	Transportation
22.	Ascendas REIT	1.0	0.7	No	Yes	Finance
23.	Sembcorp Financial Services	1.0	0.7	No	No	Engineering
24.	GLL IHT	0.9	0.7	No	No	Real Estate
25.	CMT MTN	0.9	0.7	No	No	Finance
26.	National University of Singapore	0.9	0.7	No	No	Education
27.	Overseas Union Enterprise	0.8	0.6	No	Yes	Real Estate
28.	Sembcorp Industries	0.8	0.6	No	Yes	Shipbuilding
29.	Global Logistic Properties	0.8	0.6	No	Yes	Real Estate
30.	SMRT Capital	0.8	0.6	No	No	Transportation
Total Top 30 LCY Corporate Issuers		**68.0**	**50.5**			
Total LCY Corporate Bonds		**132.6**	**98.4**			
Top 30 as % of Total LCY Corporate Bonds		**51.3%**	**51.3%**			

LCY = local currency, SGD = Singapore dollar, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (SGD million)
United Overseas Bank		
Perpetual bond	4.00	750
Housing and Development Board		
5-year bond	1.75	675
Hyflux		
Perpetual bond	6.00	500
Starhub		
10-year bond	3.55	300
Perennial Real Estate Holdings		
4-year bond	4.55	280
Mapletree Logistics Trust		
Perpetual bond	4.18	250
FCL Treasury		
10-year bond	4.25	250

Q2 = second quarter, SGD = Singapore dollar.
Source: Bloomberg LP.

Ratings Update

On 29 August, RAM Ratings affirmed Singapore's global- and Association of Southeast Asian Nations-scale sovereign ratings of $_{g}AAA_{(pi)}$ and $_{sea}AAA_{(pi)}$, respectively. Both ratings were given a stable outlook. RAM Ratings cited Singapore's strong external position, robust financial profile, sound institutional framework, and stable political governance as the main reasons for the affirmation. The rating comes amid a backdrop of slower economic growth due to a weak external environment and domestic structural challenges posed by labor shortages and an aging population.

Policy, Institutional, and Regulatory Developments

Monetary Authority of Singapore's Renminbi Investments Included in Official Foreign Reserves

MAS announced that it would include renminbi financial investments as part of its Official Foreign Reserves beginning in June. MAS cited the following reasons for this move: (i) the People's Republic of China having taken significant steps to liberalize foreign institutional investors' access to its foreign exchange and securities markets, and (ii) the International Monetary Fund's announcement that it will include the renminbi in the Special Drawing Rights basket of currencies beginning in October.

Singapore Launches First Listed Private Equity Bonds

Astrea III, which is ultimately backed by Singapore's state-owned Temasek Holdings, successfully launched a series of private equity bonds in June. The bonds are backed by 34 private equity funds with interests in more than 590 companies, the first-of-its-kind bond series to be listed in Singapore. The issued bonds are designed to make private equity more accessible to a wider range of institutional and individual investors. The issuance amounted to USD510 million and comprised four classes of 10-year bonds—A-1 (SGD228 million), A-2 (USD170 million), B (USD100 million), and C (USD70 million)—ordered according to seniority and maturity, and with interest rates of 3.90%, 4.65%, 6.50%, and 9.25%, respectively. Class A-1 bonds are redeemable starting in year 3, while Class A-2 bonds can be redeemed starting in year 5.

Singapore Exchange in SGD153 Million Deal to Buy Baltic Exchange

Singapore Exchange (SGX) and the Baltic Exchange Limited (Baltic Exchange) announced on 22 August a SGD153 million deal for SGX to acquire Baltic Exchange. The deal is expected to be completed by November. The acquisition will enable SGX to diversify into the commodities and shipping finance markets; allow SGX to develop new products, benchmarks, and services; and strengthen Singapore's role as a preferred location for the trading and settlement of shipping contracts.

Thailand

Yield Movements

Thailand's local currency (LCY) government bond yields fell for most tenors between 1 June and 15 August **(Figure 1)**. Yields for bonds with maturities of 1 month to 1 year declined 2–10 basis points (bps). Yields for tenors of between 3 years and 7 years fell between 8–24 bps. Yields for tenors of between 8 years and 30 years fell between 13–40 bps, except for the 9-year bond which fell marginally by 2 bps. Only yields for bonds with 2-year, 14-year, and 16-year maturities rose during the review period. The 2-year versus 10-year yield spread narrowed from 79 bps to 50 bps between 1 June and 15 August, leading to a flattening of the yield curve.

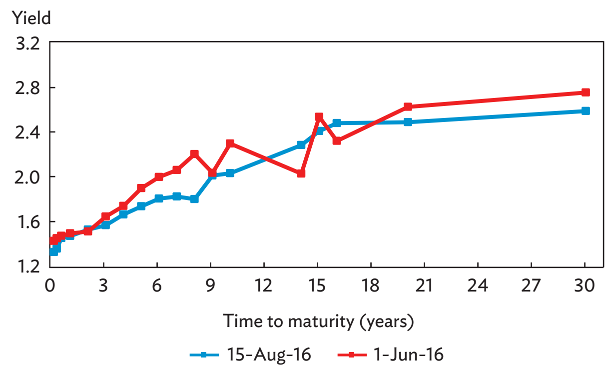
The decline in government LCY bond yields was due to the sudden increase in capital flows induced by increased investor appetite for emerging market assets resulting from the United Kingdom's referendum to leave the European Union on 23 June as well as the United States (US) Federal Reserve refraining from a policy rate increase at its mid-June and end-July meetings.

Bond yields temporarily rose in the days leading up to Thailand's referendum on 7 August in which more than 60% of Thai voters approved the military-backed constitution. The result boosted investor confidence that Thailand's economy, which had suffered due to political uncertainty, is poised to improve. As an example of increased confidence, the Thai baht appreciated to a year-to-date high of THB34.6 to the US dollar on 15 August.

The Bank of Thailand's (BOT) Monetary Policy Committee voted unanimously to maintain the policy rate at 1.50% in its 3 August meeting. The central bank maintained its accommodative monetary policy stance as it assessed that the economy would continue recovering at a gradual pace despite a perceived increase in downside risks generated by the results of the British referendum, weakness in the European financial sector, and financial stability risks in the People's Republic of China.

Consumer price inflation was positive for the fifth consecutive month in August, albeit at a pace of only 0.3% year-on-year (y-o-y), since Thailand exited from deflation in April. The slight uptick in the Consumer Price Index in August came mainly from rising prices for food and nonalcoholic beverages, which account for 33.5% of the index. Prices of nonfood items and beverages, which account for 66.5% of the index, continued to fall, led by housing and furnishings, and transportation and communications. Inflation is expected to gradually rise but the timing will depend on global oil price movements.

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



Source: Based on data from Bloomberg LP.

Thailand's gross domestic product growth rose to 3.5% y-o-y in the second quarter (Q2) of 2016 from 3.2% y-o-y in the first quarter (Q1) of 2016, buoyed by a rise in private consumption and continued growth in government spending, gross fixed capital formation, tourism, and the manufacturing sector. Exports of services remained strong on growth of 12.1% y-o-y, though this was down from 18.2% y-o-y growth in Q1 2016. Exports of goods remained weak, contracting 2.5% y-o-y in Q2 2016 after tepid growth of 1.0% in Q1 2016. According to the Office of the National Economic and Social Development Board, Thailand's economy is projected to surpass the 2.8% annual growth it achieved in 2015 by expanding 3.0%–3.5% in 2016.

Size and Composition

Thailand's LCY bond market expanded 1.6% quarter-on-quarter (q-o-q) to THB10,372 billion (USD295 billion)

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	THB	USD	THB	USD	THB	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**9,606**	**284**	**10,206**	**291**	**10,372**	**295**	**3.1**	**4.6**	**1.6**	**8.0**
Government	7,299	216	7,607	217	7,720	220	3.1	4.2	1.5	5.8
Government Bonds and Treasury Bills	3,602	107	3,964	113	3,884	111	0.7	5.2	(2.0)	7.8
Central Bank Bonds	2,910	86	2,869	82	3,030	86	8.5	3.0	5.6	4.1
State-Owned Enterprise and Other Bonds	787	23	774	22	807	23	(3.8)	3.7	4.3	2.5
Corporate	2,307	68	2,599	74	2,652	75	3.2	6.2	2.0	14.9

( ) = negative, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, THB = Thai baht, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg end-of-period LCY–USD rates are used.
3. Growth rates are calculated from an LCY base and do not include currency effects.
Sources: Bank of Thailand and Bloomberg LP.

at the end of June **(Table 1)**. On a y-o-y basis, the LCY bond market grew 8.0% in Q2 2016. Of the total amount, government bonds account for THB7,720 billion and corporate bonds for the remaining THB2,652 billion.

Government Bonds. LCY government bonds outstanding rose 1.5% q-o-q to THB7,720 billion at the end of June. The increase came mainly from the 5.6% q-o-q increase in central bank bonds outstanding and the 4.3% q-o-q increase in outstanding state-owned enterprise and other bonds. At the end of June, the outstanding stock of central government bonds stood at THB3,884 billion, a slight decrease of 2.0% q-o-q. Central bank bonds rose to THB3,030 billion, leading the overall rise in bonds outstanding.

In Q2 2016, newly issued government bonds totaled THB2,216 billion, up from THB2,103 billion in Q1 2016. Most of the new issuance comprised central bank bonds worth THB1,908 billion, which was roughly on par with the previous quarter's issuance and up 36.9% on an annual basis. New issuance of central government bonds rose 42.0% q-o-q to THB251 billion in Q2 2016 but declined 37.8% y-o-y.

Corporate Bonds. Total LCY corporate bonds outstanding rose to THB2,652 billion at the end of June on growth of 2.0% q-o-q and 14.9% y-o-y. LCY corporate bond issuance amounted to THB380 billion in Q2 2016.

At the end of June, the top 30 LCY corporate bond issuers in Thailand had combined outstanding LCY bonds amounting to THB1,465 billion. The top 30 issuers accounted for 55.3% of total LCY corporate bonds outstanding **(Table 2)**. CP All remained the largest corporate issuer in Thailand with THB180 billion of LCY bonds outstanding. Siam Cement, on the back of recent issuances, overtook PTT to become the second largest borrower with THB166.5 billion in outstanding bonds. PTT was in third spot with THB145.4 billion of LCY bonds outstanding.

In Q2 2016, the largest corporate issuance was Siam Cement's 4-year bond sale worth THB25 billion and with a coupon rate of 3.0%. This was followed by Advanced Wireless with a dual-tranche bond sale comprising 7-year and 10-year maturities totaling THB15 billion, and Bangkok Expressway and Metro's issuance of a multitranche bond with maturities ranging from 3 years to 12 years totaling THB15 billion. **Table 3** lists notable corporate bond issuances in Q2 2016.

Investor Profile

Contractual savings funds remained the largest holder of LCY government bonds in Thailand with a share of 28.8% of the total at the end of June, up slightly from 27.9% in Q2 2015 **(Figure 2)**. Insurance companies accounted for the second largest share at 26.3%, which was little changed from 25.8% in Q2 2015. Meanwhile, the share of foreign investors fell to 14.5% at the end of June from 16.5% a year earlier.

Net foreign flows into Thailand's LCY bond market were positive in January–July. In Q1 2016, foreign investors showed renewed interest in the region after

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in Thailand

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (THB billion)	LCY Bonds (USD billion)			
1.	CP All	180.0	5.1	No	Yes	Commerce
2.	Siam cement	166.5	4.7	Yes	Yes	Construction Materials
3.	PTT	145.4	4.1	Yes	Yes	Energy and Utilities
4.	Charoen Pokphand Foods	80.0	2.3	No	Yes	Food and Beverage
5.	Bank of Ayudhya	67.3	1.9	No	Yes	Banking
6.	Thai Airways International	54.3	1.5	Yes	Yes	Transportation and Logistics
7.	Indorama Ventures	45.3	1.3	No	Yes	Petrochemicals and Chemicals
8.	Kasikorn Bank	42.5	1.2	No	Yes	Banking
9.	Tisco Bank	40.8	1.2	No	No	Banking
10.	The Siam Commercial Bank	40.0	1.1	No	Yes	Banking
11.	Toyota Leasing Thailand	39.1	1.1	No	No	Finance and Securities
12.	Mitr Phol Sugar	37.8	1.1	No	No	Food and Beverage
13.	Banpu	37.3	1.1	No	Yes	Energy and Utilities
14.	True Corp	37.1	1.1	No	Yes	Communications
15.	True Move H Universal Communication	34.0	1.0	No	No	Communications
16.	Krungthai Card	32.8	0.9	Yes	Yes	Banking
17.	Thanachart Bank	32.5	0.9	No	No	Banking
18.	Land & Houses	32.5	0.9	No	Yes	Property and Construction
19.	PTT Exploration and Production Company	32.1	0.9	Yes	Yes	Energy and Utilities
20.	TPI Polene	32.0	0.9	No	Yes	Property and Construction
21.	Advanced Wireless	31.6	0.9	No	Yes	Communications
22.	Thai Oil	28.0	0.8	Yes	Yes	Energy and Utilities
23.	Minor International	25.8	0.7	No	Yes	Food and Beverage
24.	Quality Houses	25.4	0.7	No	Yes	Property and Construction
25.	TMB Bank	25.4	0.7	No	Yes	Banking
26.	ICBC Thai Leasing	24.9	0.7	No	No	Finance and Securities
27.	Glow Energy	24.6	0.7	No	Yes	Energy and Utilities
28.	CH. Karnchang	24.5	0.7	No	Yes	Property and Construction
29.	IRPC	23.0	0.7	Yes	Yes	Energy and Utilities
30.	Bangkok Dusit Medical Services	22.6	0.6	No	Yes	Medical
Total Top 30 LCY Corporate Issuers		**1,465.1**	**41.7**			
Total LCY Corporate Bonds		**2,651.5**	**75.5**			
Top 30 as % of Total LCY Corporate Bonds		**55.3%**	**55.3%**			

LCY = local currency, THB = Thai baht, USD = United States dollar.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

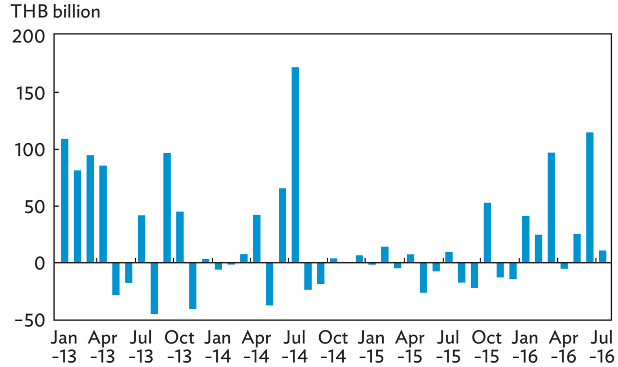
the US Federal Reserve announced it would delay further increases in its policy rate. Toward the end of Q2 2016, the United Kingdom's referendum on leaving the European Union caused uncertainty in global financial markets and directed funds toward the region. In addition, there was a further delay in the next rate hike by the US Federal Reserve. Aggregate net fund inflows in Q2 2016 amounted to THB133 billion. On a monthly basis, the decline in net inflows from THB113 billion in June to THB11 billion in July was the result of political uncertainty ahead of Thailand's referendum on 7 August **(Figure 3)**.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (THB million)
Siam Cement		
4-year bond	3.00	25,000
Advanced Wireless		
7-year bond	2.51	7,820
10-year bond	2.78	7,180
Bangkok Expressway and Metro		
3-year bond	2.22	5,000
5-year bond	2.52	1,915
7-year bond	3.00	2,000
10-year bond	3.30	3,335
12-year bond	3.61	2,750
Bank of Ayudhya		
2-year bond	1.89	5,000
3-year bond	1.96	7,000
Charoen Pokphand Foods		
4-year bond	2.28	3,060
8-year bond	3.11	3,500
15-year bond	3.73	2,500

Q2 = second quarter, THB = Thai baht.
Source: Bloomberg LP.

Figure 3: Foreign Investor Net Trading of Local Currency Bonds in Thailand

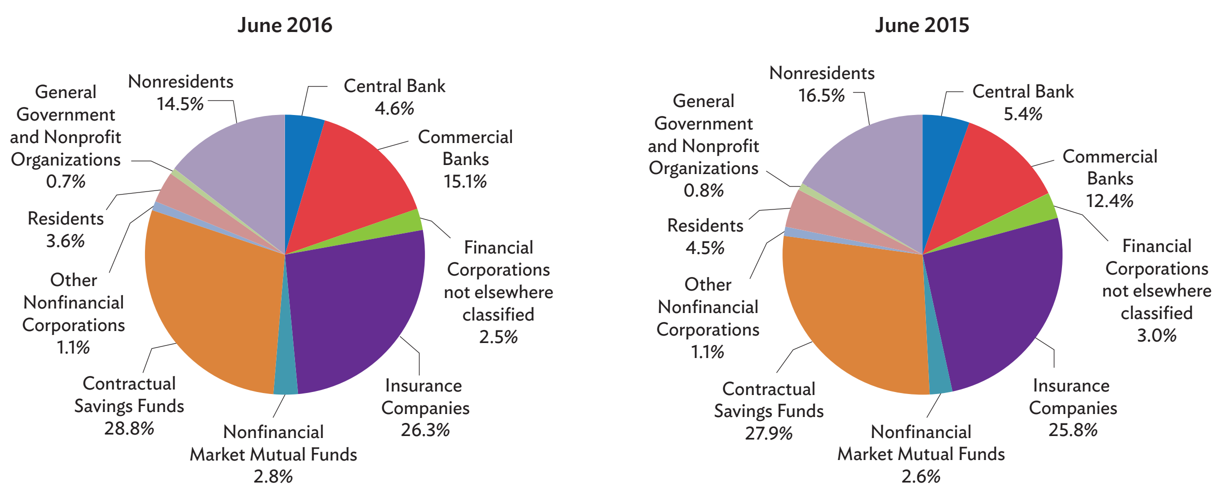


THB = Thai baht.
Source: ThaiBMA.

Ratings Update

On 22 July, Fitch Ratings (Fitch) downgraded Thailand's long-term local currency issuer default rating (IDR) to BBB+ from A–, while it affirmed the long-term foreign currency IDR at BBB+. Both ratings were given a stable outlook. Thailand's country ceiling was affirmed at A–, while its short-term local and foreign currency IDRs were assigned a rating of F2. The downgrade was in accordance with the revised sovereign rating criteria set forth on 18 July. Among other factors, Fitch stated that Thailand's key rating drivers are its strong and robust external and public finances amid multiple domestic and external economic shocks. However, these positives are tempered by weak growth prospects and the uncertain political environment.

Figure 2: Local Currency Government Bonds Investor Profile



Note: Government bonds exclude central bank bonds and state-owned enterprise bonds.
Sources: *AsianBondsOnline* and Bank of Thailand.

On 25 July, RAM Ratings reaffirmed Thailand's global scale rating of $_{g}BBB1_{(pi)}$ with a stable outlook. It cited Thailand's robust external finances, strong fiscal position, and well-diversified economy as the primary basis for the reaffirmation. It notes, however, political instability, weak private demand, and structural challenges as key concerns for the economy.

Policy, Institutional, and Regulatory Developments

Bank of Thailand Releases Plan for Bond Issuance Program for the Second Half of 2016

In June, the BOT announced its plan to increase the maximum issuance sizes of all bills and fixed-coupon bonds, except for the 3-year floating-rate bond, as a response to potentially rapid changes in market liquidity conditions and large swings in the appetite for bonds amid heightened volatility in the global financial markets. Auction days and issuance frequencies for all types of BOT bonds will remain the same. Depending on liquidity conditions and the issuance calendar for Treasury bills, the central bank will also consider issuing 1-month BOT bills on an occasional basis.

Bank of Thailand Eases Rules for Ownership of Foreign Securities

On 5 July, the BOT issued a memorandum allowing Thailand's citizens direct investment access to foreign securities, effective 20 July. Individuals and corporations with deposits or securities of at least THB100 million can directly invest a maximum amount each year of USD5 million in foreign securities. Corporate treasuries will also be allowed to both issue and invest in onshore and offshore foreign-currency-denominated debt beginning 28 July. Previously, stricter rules only allowed for firms to borrow foreign currency from financial institutions and invest in foreign-currency-denominated securities that were issued offshore. This comes as part of the central bank's effort to dampen the strengthening of the Thai baht vis-à-vis the US dollar.

Viet Nam

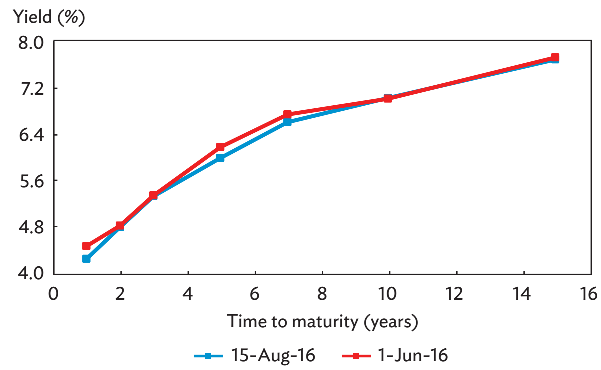
Yield Movements

Local currency (LCY) government bond yields in Viet Nam fell for all tenors between 1 June and 15 August except for the 10-year maturity **(Figure 1)**. Yields fell the most at the very short-end of the curve, with the 1-year maturity shedding 22 basis points (bps), while yields declined 19 bps for the 5-year maturity and 13 bps for the 7-year tenor. All other maturities across the curve fell by an average of 2 bps during the review period except for the 10-year maturity, which gained 1 bp. The spread between the 2-year and the 10-year maturities widened to 221 bps on 15 August from 217 bps on 1 June.

The decline in yields can be partly attributed to new regulations passed by the State Bank of Vietnam easing investment restrictions on government bonds by banking institutions and foreign banks (see Policy and Regulatory Developments). Efforts by the State Bank of Vietnam to lower interest rates and maintain a more stable Vietnamese dong vis-à-vis the United States dollar also led to increased demand for government bonds. Further contributing to the decline in yields was the delay in the anticipated United States Federal Reserve rate hike, which has resulted in increased demand for higher-yielding assets.

Real gross domestic product (GDP) growth stood at 5.5% y-o-y in the first half of the year, roughly unchanged from the first 3 months of the year. Growth was buoyed by a 7.1% y-o-y expansion in the industrial and construction sector and a 6.4% y-o-y increase in the services sector.

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



Source: Based on data from Bloomberg LP.

Size and Composition

The size of Viet Nam's LCY bond market stood at VND969.9 trillion (USD43 billion) at the end of June on growth of 10.8% quarter-on-quarter (q-o-q) and 0.7% y-o-y **(Table 1)**. Growth was led by an increase in the stock of government bonds, particularly Treasury bonds and central bank bills. The corporate bond segment also contributed to growth, though this segment is still small relative to the aggregate bond stock.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2015		Q1 2016		Q2 2016		Q2 2015		Q2 2016	
	VND	USD	VND	USD	VND	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**963,522**	**44**	**875,076**	**39**	**969,903**	**43**	**(0.8)**	**7.1**	**10.8**	**0.7**
Government	939,049	43	838,284	38	931,111	42	(1.7)	6.3	11.1	(0.8)
Treasury Bonds	546,192	25	627,691	28	717,149	32	(6.3)	7.0	14.3	31.3
Central Bank Bonds	200,308	9	4,905	0.2	9,999	0.4	26.5	23.5	103.9	(95.0)
State-Owned Enterprise Bonds	192,549	9	205,688	9	203,963	9	(9.8)	(8.7)	(0.8)	5.9
Corporate	24,473	1	36,792	2	38,792	2	52.7	48.9	5.4	58.5

( ) = negative, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second quarter, USD = United States dollar, VND = Vietnamese dong, y-o-y = year-on-year.
Notes:
1. Bloomberg LP end-of-period local currency–USD rates are used.
2. Growth rates are calculated from local currency base and do not include currency effects.
Source: Bloomberg LP and Vietnam Bond Market Association.

Government Bonds. At the end of June, LCY government bonds in Viet Nam reached VND931.1 trillion, up 11.1% q-o-q but marginally lower by 0.8% y-o-y. Much of the growth came from increases in the stock of Treasury bonds, which rose 14.3% q-o-q and 31.3% y-o-y. Central bank bills also contributed to the growth, albeit from a low base. The stock of state-owned enterprise bonds marginally declined 0.8% q-o-q during the review period.

Corporate Bonds. At the end of June, the outstanding stock of corporate bonds reached VND38.8 trillion on growth of 5.4% q-o-q and 58.5% y-o-y. The entire corporate bond market of Viet Nam comprised 19 corporate firms at the end of June **(Table 2)**. The largest corporate bond issuer was Masan Consumer Holdings with bonds outstanding amounting to VND11.1 trillion, representing 28.6% of the aggregate corporate bond stock. In the second spot was real estate firm Vingroup with VND8.0 trillion of outstanding bonds. Asia Commercial Joint Stock moved up to the third spot with bonds valued at VND4.6 trillion.

In Q2 2016, three corporate firms in Viet Nam raised capital from the bond market. The largest new corporate debt issuance was Asia Commercial Joint Stock, which raised a total of VND1,600 billion from an issuance of 5-year bonds **(Table 3)**. Saigon–Hanoi Securities issued VND300 billion in 2-year bonds, while Dongnai Plastic issued VND100 billion in 3-year bonds.

Table 3: Notable Local Currency Corporate Bond Issuance in Q2 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (VND billion)
Asia Commercial Joint Stock		
5-year bond	8.50	800
5-year bond	8.20	800
Saigon-Hanoi Securities		
2-year bond	9.50	300
Dongnai Plastic		
3-year bond	9.75	100

Q2 = second quarter, VND = Vietnamese dong.
Source: Bloomberg LP.

Table 2: Corporate Issuers of Local Currency Corporate Bonds in Viet Nam

Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
	LCY Bonds (VND billion)	LCY Bonds (USD billion)			
1. Masan Consumer Holdings	11,100	0.50	No	No	Diversified Operations
2. Vingroup JSC	8,000	0.36	No	Yes	Real Estate
3. Asia Commercial Joint Stock	4,600	0.21	No	Yes	Finance
4. Hoang Anh Gia Lai	4,000	0.18	No	Yes	Real Estate
5. Techcom Bank	3,000	0.13	No	No	Banking
6. Ho Chi Minh City Infrastructure	2,102	0.09	No	Yes	Infrastructure
7. DIC	1,000	0.04	Yes	No	Chemicals
8. Ocean Group	980	0.04	No	Yes	Consulting Services
9. Saigon-Hanoi Securities	950	0.04	No	Yes	Finance
10. Tasco	500	0.02	No	Yes	Engineering and Construction
11. Vietinbank Securities	500	0.02	Yes	Yes	Finance
12. Sotrans	400	0.02	No	No	Logistics
13. Vietnam Investment Construction and Trading	350	0.02	No	Yes	Building and Construction
14. Anphat Plastic & Green Environment	300	0.01	No	Yes	Industrial
15. Hung Vuong	300	0.01	No	Yes	Food
16. Saigon Securities	300	0.01	No	Yes	Finance
17. Ha Do	200	0.01	No	Yes	Construction
18. Ho Chi Minh City Securities	110	0.005	No	No	Finance
19. Dongnai Plastic	100	0.004	No	Yes	Industrial
Total LCY Corporate Issuers	**38,792**	**1.73**			

LCY = local currency, USD = United States dollar, VND = Vietnamese dong.
Notes:
1. Data as of end-June 2016.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP and Vietnam Bond Market Association data.

Policy, Institutional, and Regulatory Developments

State Bank of Vietnam Raises Prudential Ratios for Credit Institutions and Foreign Banks

In May, the State Bank of Viet Nam revised its regulation on prudential ratios for credit institutions and foreign banks. The revision included increasing the ceiling limits on the purchase or investment of government bonds by banking institutions from 15% to 25% of their short-term funding source. The investment cap for foreign banks was also raised to 35% of their short-term funding source.

State Bank of Vietnam Allows Foreign Currency Loans for Exporters

Effective 1 June, the State Bank of Vietnam began allowing commercial banks to provide short-term foreign currency loans for the short-term capital requirements of exporters. Under the new regulation, exporters are required to exchange borrowed foreign currency into Vietnamese dong, unless the loan will be used for a foreign currency payment. This new regulation will be in effect through 31 December. The State Bank of Vietnam had previously tightened regulations on foreign currency lending in March.