The Asia Bond Monitor (ABM) reviews recent developments in East Asian local currency bond markets along with the outlook, risks, and policy options. The ABM covers the 10 Association of Southeast Asian Nations member countries plus the People’s Republic of China; Hong Kong, China; and the Republic of Korea.

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**Emerging East Asian Local Currency Bond Markets: A Regional Update**

**Highlights**

**Recent Bond Market Developments**

- During the first half of 2008, emerging East Asia’s local currency bond markets grew slower from end-2007; bonds outstanding-to-GDP fell marginally—trends that continued into the second half.
- Government bond issuance continues to dominate the market, driven by deficit financing and monetary sterilization, while corporate bond market activity slowed as borrowing costs increased and credit dried up.
- Government bond yield movements in emerging East Asia went through three distinct phases in 2008:
  - most yield curves shifted up during the first half as many central banks raised interest rates to fight inflation;
  - yield curves shifted downward from July to early September as the severity of the global credit crisis deepened and inflationary expectations peaked;
  - global credit markets seized-up in September and the combination of an investor “flight-to-quality” and emergency measures drove yields in government bonds lower.
- Returns on local currency bonds were lackluster in 2008 as investors reduced exposure to high-risk assets amid tightening global liquidity and increased market volatility.
- Foreign holdings of local currency government bonds rose as investors shed riskier assets, a sign of growing confidence in emerging East Asia’s bond markets.
- In the first half, market liberalization, product innovation, and diversification continued despite simmering global market turmoil; but most were placed on standby as the crisis deepened.

**Outlook, Risks, and Policy Challenges**

- Contagion from the US credit turmoil rapidly hit global financial markets, with significant spillover into the real economy.
- Concern over rising inflation, which dominated policy discussions in emerging East Asia in the first half of 2008, have given way to policies addressing deteriorating economic growth.

*Continued overleaf*
Against this backdrop and the need to stabilize troubled financial markets, monetary policy has shifted to a more accommodative stance in most countries, a trend likely to continue into 2009.  

The acceleration of capital outflows, coupled with tightened credit could choke off funds for investment and raise financing costs.  

Tight dollar liquidity, deleveraging, and weakening regional currencies may dampen foreign investor interest in local currency corporate bonds.  

Given the expected slowdown in global and regional growth, economies which have relatively comfortable fiscal balances and public debt are likely to introduce fiscal stimulus packages, boosting government bond issuance.  

Apart from immediate market stabilization measures, lessons from the current crisis can be applied to future policies to strengthen the development of local currency bond markets:  

— Strengthen international supervisory and regulatory coordination, cooperation, convergence, and surveillance;  
— Strengthen risk assessment and risk management;  
— Promote consistent standards and mutual recognition;  
— Improve transparency by better valuation and accounting of off-balance sheet instruments;  
— Prudently liberalize cross-border financial services and capital accounts;  
— Devise countercyclical policies for the financial sector;  
— Strengthen or expand existing regional initiatives such as the Asian Bond Markets Initiative and Asian Bond Fund.

Note: To conform with market practice, the Asia Bond Monitor uses two-letter official ISO Country Codes and three-letter currency codes rather than ADB’s standard symbols.

The Asia Bond Monitor November 2008 was prepared by ADB’s Office of Regional Economic Integration and does not necessarily reflect the views of ADB’s Board of Governors or the countries they represent.
Yield curves shift downward as inflation eases and fear of economic slowdown increases.

**1: Size of Emerging East Asian Local Currency Bond Markets**

<table>
<thead>
<tr>
<th>Country</th>
<th>Amount (USD billion)</th>
<th>Y-o-Y 1H08</th>
<th>YTD 1H08</th>
</tr>
</thead>
<tbody>
<tr>
<td>China, People’s Rep. of</td>
<td>2,004.22</td>
<td>31.86</td>
<td>11.41</td>
</tr>
<tr>
<td>Hong Kong, China</td>
<td>92.64</td>
<td>(6.85)</td>
<td>(5.47)</td>
</tr>
<tr>
<td>Indonesia</td>
<td>82.88</td>
<td>(2.65)</td>
<td>(4.48)</td>
</tr>
<tr>
<td>Korea, Rep. of</td>
<td>985.91</td>
<td>7.91</td>
<td>3.88</td>
</tr>
<tr>
<td>Malaysia</td>
<td>187.49</td>
<td>27.19</td>
<td>12.76</td>
</tr>
<tr>
<td>Philippines</td>
<td>56.67</td>
<td>10.59</td>
<td>6.22</td>
</tr>
<tr>
<td>Singapore</td>
<td>138.58</td>
<td>15.36</td>
<td>7.66</td>
</tr>
<tr>
<td>Thailand</td>
<td>150.23</td>
<td>16.16</td>
<td>7.13</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>11.90</td>
<td>75.49</td>
<td>27.76</td>
</tr>
<tr>
<td>Total Emerging East Asia</td>
<td>3,710.53</td>
<td>20.74</td>
<td>8.15</td>
</tr>
<tr>
<td>Government</td>
<td>2,690.20</td>
<td>22.16</td>
<td>9.13</td>
</tr>
<tr>
<td>Corporate</td>
<td>1,020.33</td>
<td>17.17</td>
<td>5.67</td>
</tr>
</tbody>
</table>

**Source:** People’s Republic of China (ChinaBond); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Stock Exchange and Bank Indonesia); Republic of Korea (KoreaBondWeb); Malaysia (Bank Negara Malaysia); Philippines (Bureau of the Treasury); Singapore (Monetary Authority of Singapore); Thailand (Bank of Thailand); and Viet Nam (Bloomberg).

**2: 10-Year Selected LCY Government Bond Yields**

<table>
<thead>
<tr>
<th>Markets</th>
<th>basis points change 1 Jan 08–31 Oct 08</th>
<th>1-Jan-08 Closing</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>-7.01</td>
<td>4.023</td>
</tr>
<tr>
<td>EU</td>
<td>-43.00</td>
<td>4.330</td>
</tr>
<tr>
<td>Japan</td>
<td>-3.40</td>
<td>1.510</td>
</tr>
<tr>
<td>PRC</td>
<td>-135.00</td>
<td>4.460</td>
</tr>
<tr>
<td>Hong Kong, China</td>
<td>-105.90</td>
<td>3.441</td>
</tr>
<tr>
<td>Indonesia</td>
<td></td>
<td>728.30</td>
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<tr>
<td>Malaysia</td>
<td></td>
<td>15.50</td>
</tr>
<tr>
<td>Korea, Rep. of</td>
<td>-21.00</td>
<td>5.700</td>
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<tr>
<td>Philippines</td>
<td></td>
<td>289.42</td>
</tr>
<tr>
<td>Singapore</td>
<td></td>
<td>27.00</td>
</tr>
<tr>
<td>Thailand</td>
<td>-118.40</td>
<td>4.955</td>
</tr>
<tr>
<td>Viet Nam</td>
<td></td>
<td>592.50</td>
</tr>
</tbody>
</table>

**Source:** Based on data from Bloomberg.

**3: Writedowns and capital raised by major banks since the third quarter of 2007 (USD billions)**

**Source:** Bloomberg, October 2008.
Bias shifting toward looser monetary policies as inflation eases and oil prices slide.

Risk premium remains elevated, more so for lower-rated sovereigns and high-risk corporates.

Tighter dollar liquidity has weakened Asian currencies and may dampen foreign investor interest in local currency corporate bonds.
About the Asian Development Bank

ADB’s vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries substantially reduce poverty and improve the quality of life of their people. Despite the region’s many successes, it remains home to two thirds of the world’s poor. Nearly 1.7 billion people in the region live on $2 or less a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance. In 2007, it approved $10.1 billion of loans, $673 million of grant projects, and technical assistance amounting to $243 million.