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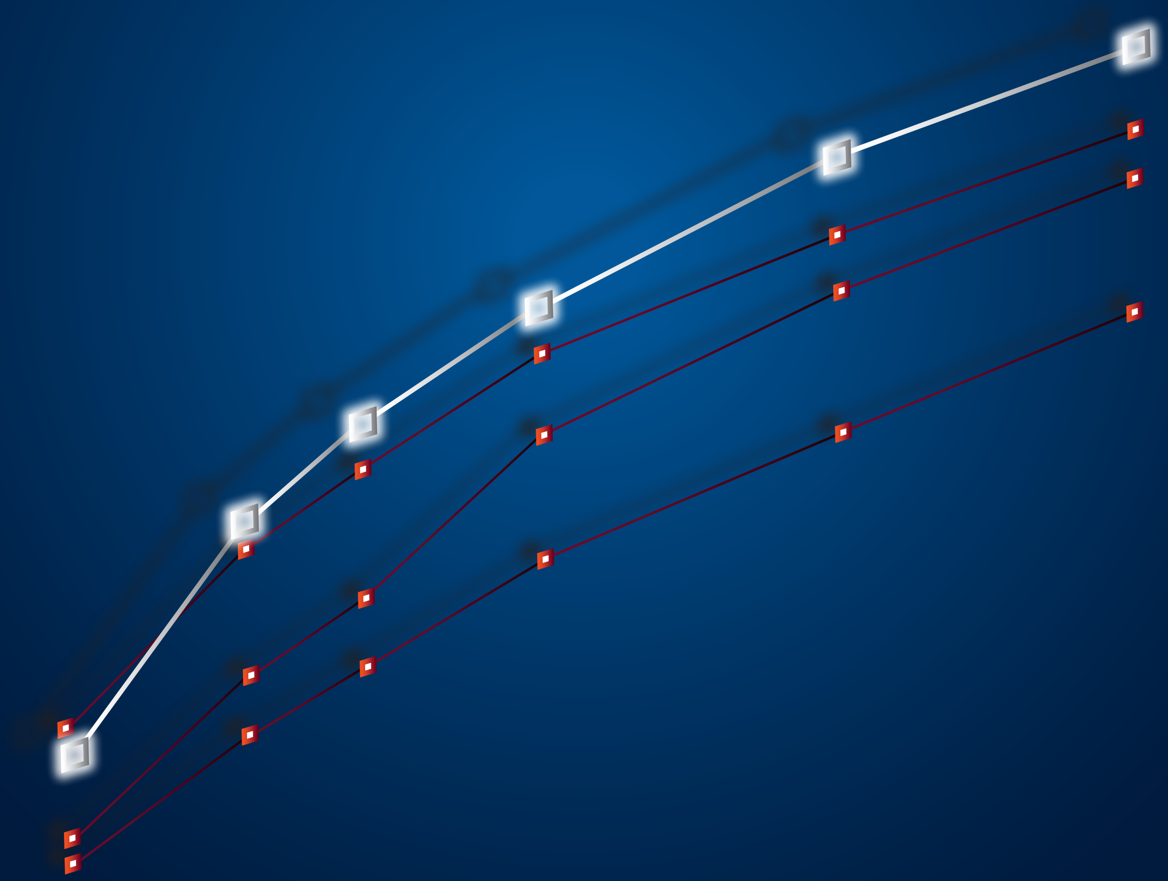
ASIA BOND MONITOR

NOVEMBER 2010



Asian Development Bank

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The *Asia Bond Monitor* (ABM) reviews recent developments in East Asian local currency bond markets along with outlook, risks, and policy challenges. It covers the 10 Association of Southeast Asian Nations (ASEAN) 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

- It's a story of two halves. The external environment facing emerging East Asia has weakened as the United States (US) economy continues to struggle and a shadow lingers over the eurozone. The debt crisis facing several peripheral economies in Europe is a reminder of the risk overhang.

- Authorities in mature economies are continuing with, and in some cases introducing more, stimulus packages to spur economic activity.

- Meanwhile, emerging East Asia's economic recovery remains buoyant. Most economies in the region have tightened monetary policy as inflationary pressures increase along with rising foreign portfolio capital inflows.

- Foreign holdings in emerging East Asia's local currency (LCY) government bonds continue to soar as investors chase higher yields, participate in the region's economic recovery, and seek to make additional gains from the anticipated appreciation of regional currencies. There is growing foreign investor interest in LCY corporate bonds.

- Some economies are now introducing capital controls and other administrative measures to dampen volatility and ease pressure on exchange rates.

- Total bonds outstanding in emerging East Asia's LCY bond market reached USD5.1 trillion in 3Q10, rising 17.2% year-on-year (y-o-y) and 3.0% quarter-on-quarter (q-o-q), driven by strong growth in corporate bonds.

- The region's LCY government bond market expanded 1.9% q-o-q in 3Q10 against 5.1% in 2Q10, reflecting a paring down of fiscal stimulus programs in 2010 and an apparent reduction in issuance by central banks and monetary authorities.

- The growth in the region's LCY corporate bond market in 3Q10 was 5.7% q-o-q, outpacing growth in government bonds. The corporate bond market now comprises 30% of total LCY bonds outstanding in emerging East Asia.

- The rapid growth of corporate bonds marks a major structural change in the evolution of regional LCY bond markets. Banks and infrastructure companies are the largest issuers of corporate bonds, which is a similar characteristic of many mature markets.

- LCY bond issuance in emerging East Asia totaled USD1.02 trillion in 3Q10, growing 6.0% q-o-q, largely driven by issuance in the corporate sector.

- Government bond yield curves in emerging East Asia have steepened lately on concerns over inflationary pressures and interest rate hikes, but still remain flat when compared to end-2009 levels.

- G3 currency bond issuance in emerging East Asia reached USD77.8 billion through mid-November, significantly above the record level of USD63.2 billion for all of 2009.

Annual Asian Bond Market Liquidity Survey

- *AsianBondsOnline*'s Annual Liquidity Survey showed an improvement in liquidity in most government and corporate LCY bond markets. This has led to a tightening of bid–ask spreads and an increase in average transaction sizes compared with last year.

- The growth in both government and corporate bonds has attracted a diverse range of investors, both local and foreign. Diversity of investors has been identified in the survey as a key factor in promoting liquidity in regional LCY bond markets.

Introduction: **Global and Regional Market Developments**

The external environment facing emerging East Asian[1] economies has weakened as the United States (US) economy continues to struggle and a shadow lingers over the eurozone. While global financial markets have largely stabilized, the debt crisis facing several peripheral economies in Europe is a reminder of the risk overhang.

Emerging East Asia's robust growth is expected to moderate due to a weaker global outlook and the normalization of stimulus packages. The region's still relatively strong growth outlook, along with rising interest rate differentials and ongoing accommodative policies in mature markets, will continue to drive foreign capital inflows into the region's asset markets **(Figure A)**. Some economies are now introducing capital controls and other administrative measures to dampen volatility and ease pressure on exchange rates.

Compared with end-2009, the government yield curves in mature markets, as well as in local currency (LCY) bond markets in the region, have witnessed a flattening trend. However, this trend has been partially reversed by the introduction of the second round of quantitative easing by the US Federal Reserve. Yields on 10-year government bonds in mature markets have risen **(Figure B)**. Market attention has also turned to high levels of public debt in the US and parts of Europe.

Financial market conditions have largely stabilized, with emerging markets posting steady gains, amid flush global liquidity. Corporate bond spreads have tightened even in mature markets experiencing a strong recovery in credit conditions this year **(Figure C)**. Since the middle of 2010, there has been a rapid recovery in global stock markets, with Latin America and emerging Asian markets leading the way **(Figure D)**.

[1] Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.

Investor preference for emerging market assets is also reflected in a renewed decline in JP Morgan's Emerging Markets Bond Index (EMBI) sovereign stripped spreads **(Figure E)** and a continued decline in credit default swap (CDS) spreads for emerging East Asian government bonds **(Figure F)**. However, CDS spreads for some European paper have widened over investor worries about fiscal conditions **(Figure G)**.

The correlation between LCY bond markets and US treasuries has decreased for some markets in recent months **(Figure H)**. LCY bond yield curves have also steepened recently on inflationary concerns and interest rate hikes in some markets. However, strong foreign demand for LCY bonds is counteracting this rise.

The growth performance of emerging East Asian economies generally tempered in 3Q10 compared with the previous quarter. The People's Republic of China (PRC) reported that its economy expanded 9.6% year-on-year (y-o-y) in 3Q10 versus 10.3% in 2Q10. The Republic of Korea's gross domestic product (GDP) grew 4.5% y-o-y in 3Q10 against 7.2% in 2Q10. However, the Republic of Korea's domestic consumption remained strong even as exports weakened. Also in 3Q10, GDP grew 6.5% y-o-y in the Philippines, 5.3% in Malaysia, 6.7% in Thailand, and 10.6% in Singapore (based on preliminary estimates).

The risks to the market outlook in the region are now tilted to the downside. These include (i) a reversal of growth in advanced economies, (ii) destabilizing capital inflows, and (iii) possible overheating of some economies if governments are too slow to withdraw their economic stimulus programs.

Emerging East Asian LCY bonds continued their strong performance in 2010, with corporate bond growth as the major driver this year compared with the generally more dominant government

Figure A: Net Foreign Portfolio Investment in Equities (USD billion)

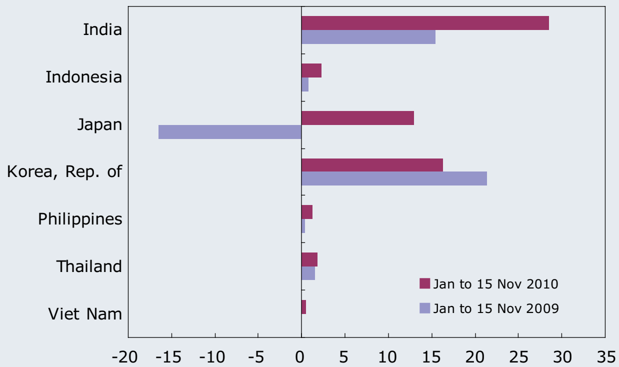


Figure D: MSCI Indexes[2] (January 2007 = 100)

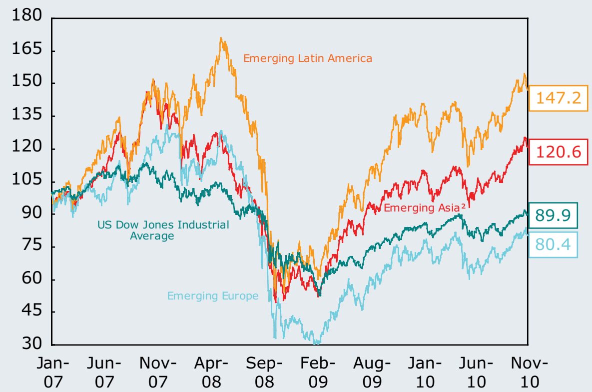


Figure B: 10-Year Government Bond Yields (% per annum)

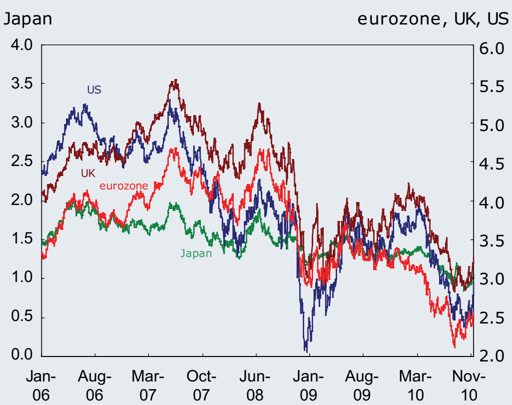


Figure E: JPMorgan EMBI Sovereign Stripped Spreads[3]

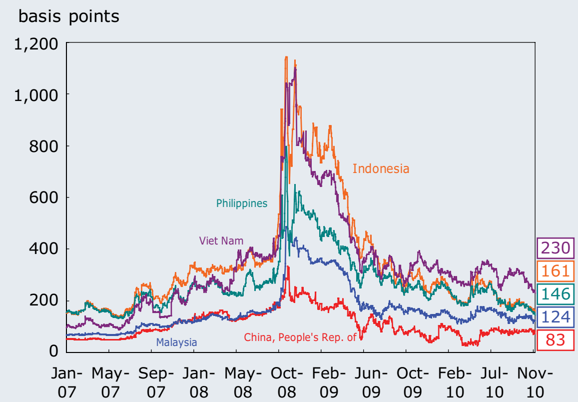


Figure C: Corporate Bond Spreads[1]

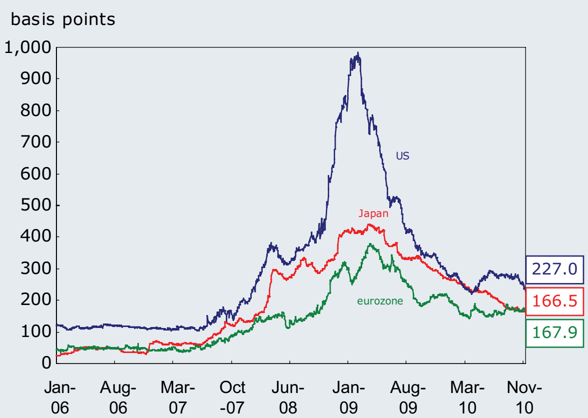
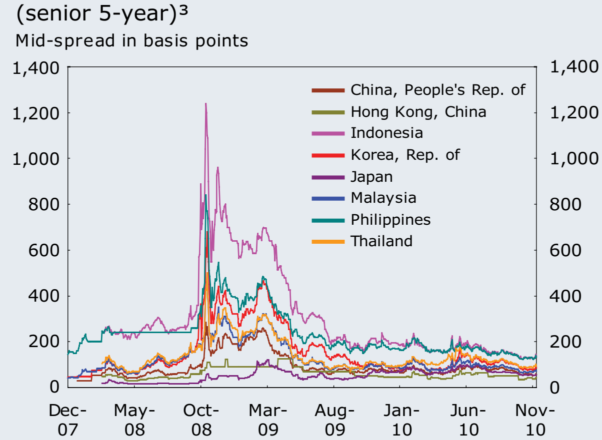
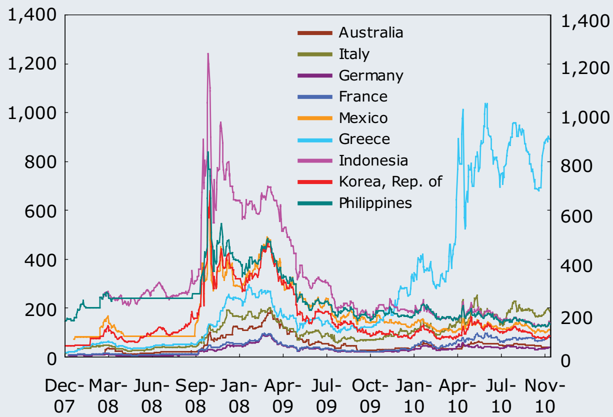


Figure F: Credit Default Swap Spreads (senior 5-year)[3]



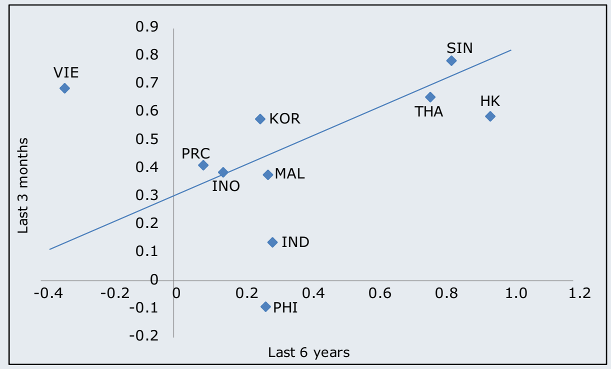
EMBI = Emerging Markets Bond Index, UK = United Kingdom, US = United States.
Notes:
[1] Bond spread refers to the difference between yields of 5-year bonds issued by BBB-rated finance companies and yields of sovereign benchmark bonds of the same tenor.
[2] Includes People's Republic of China; India; Indonesia; Republic of Korea; Malaysia; Pakistan; Philippines; Taipei, China; and Thailand.
[3] USD spread based on sovereign bonds.
Source: Thomson DataStream, Morgan Stanley Capital International (MSCI) Barra, and Bloomberg LP.

Figure G: Credit Default Swap Spreads for Select OECD and Asian Economies



OECD = Organisation for Economic Co-operation and Development
Source: Thomson DataStream.

Figure H: Correlation between Yields on 10-Year US Treasury Bonds and 10-Year LCY Government Bonds



HK = Hong Kong, China; IND = India; INO = Indonesia; KOR = Rep. of Korea; LCY = local currency; MAL = Malaysia; PHI = Philippines; PRC = People's Rep. of China; SIN = Singapore; THA = Thailand; US = United States; and VIE = Viet Nam.
Source: Bloomberg LP and Standard Chartered.

sector. The y-o-y growth rate for the region's LCY bond market in 3Q10 was 17.2% against 18.7% in 2Q10, driven by 23.8% growth in corporate bonds. The slowdown in government bonds outstanding, from 16.6% in 2Q10 to 14.6% in 3Q10, was due to a paring down of fiscal stimulus and a drop in central bank issuance.

At the end of 1Q10, emerging East Asia's share of the global bond market stood at 7.4%, compared with 2.1% before the onset of the 1997/98 Asian financial crisis **(Table A)**. The two largest markets in the region at the end of 1Q10 were the PRC (4.2% of the global bond market) and the Republic of Korea (1.7%).

Table A: Bonds Outstanding in Major Markets (USD billion)

	Mar-10		Dec-96	
	LCY Bonds Outstanding	% of World Total	LCY Bonds Outstanding	% of World Total
United States	24,978	39.8	10,926	42.9
Japan	9,754	15.5	4,456	17.5
France	3,094	4.9	1,261	4.9
Germany	2,632	4.2	1,888	7.4
United Kingdom	1,525	2.4	678	2.7
Emerging East Asia	4,633	7.4	527	2.1
of which: PRC	2,648	4.2	62	0.2
Emerging East Asia excl. PRC	1,985	3.2	465	1.8
of which: Korea, Rep. of	1,095	1.7	283	1.1
of which: ASEAN-6	735	1.2	148	0.6
Indonesia	108	0.2	7	0.0
Malaysia	199	0.3	71	0.3
Philippines	66	0.1	28	0.1
Singapore	159	0.3	25	0.1
Thailand	191	0.3	18	0.1
Viet Nam	12	0.0	—	—
Memo Items:				
Brazil	1,218	1.9	299	1.2
PRC (excl. policy bank bonds)	1,971	3.1	—	—
India	652	1.0	81	0.3
Russia	51	0.1	43	0.2

— = not applicable, ASEAN = Association of Southeast Asian Nations, LCY = local currency, PRC = People's Republic of China.
Note: Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia: Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.
Source: Bank for International Settlements and *AsianBondsOnline*.

Bond Market Developments in the Third Quarter of 2010

Size and Composition

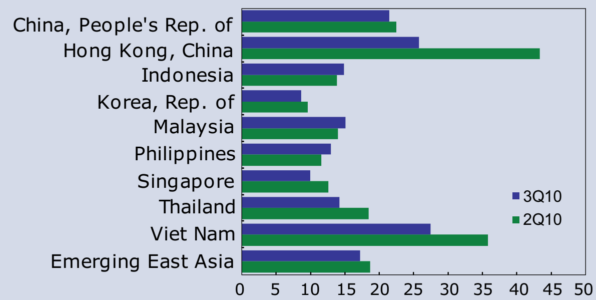
Total bonds outstanding in emerging East Asia's LCY market rose by 17.2% y-o-y and 3.0% q-o-q in 3Q10 to reach USD5.1 trillion, driven by strong growth in corporate bonds.[2]

The 3.0% quarter-on-quarter (q-o-q) growth rate in 3Q10 for emerging East Asia's local currency (LCY) bond market, which was down from 5.0% in 2Q10, reflected a sharp decline in government bond issuance—especially by central banks—in most markets across the region. While it still may be early to draw any conclusion from this data, the drop in central bank issuance in 3Q10 could be attributed to one or both of the following factors: (i) Monetary authorities in markets where inflation has risen in recent months may be allowing currencies to gradually appreciate to contain the prices of imported goods. This may have led to a decrease in sterilization activities by some central banks in the region. (ii) Alternatively, some authorities may be relying on other measures to counter the massive inflows of foreign capital instead of aggressively selling bills to mop up liquidity from local markets. Year-on-year (y-o-y) growth rates, however, remained robust **(Figure 1)** and serve as a reminder that 2010 has been an active year in emerging East Asia's LCY bond market.

Growth in the People's Republic of China's (PRC) LCY bond market fell to 3.6% q-o-q in 3Q10 from 6.9% in 2Q10 **(Table 1)**. The market contracted 1.0% q-o-q in Viet Nam. The market in the Republic of Korea expanded 1.8% q-o-q and the Indonesian market grew by 1.1% q-o-q. Malaysia reported the highest q-o-q growth rate in the region in 3Q10 at 3.7%, although this was slower than its 7.4% growth rate in 2Q10.

[2] Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.

Figure 1: Growth of Emerging East Asian LCY Bond Markets in 2Q10 and 3Q10 (y-o-y %)



LCY = local currency, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Growth rates are calculated from local currency base and do not include currency effects.
3. Emerging East Asia growth figure is based on end-September 2010 currency exchange rates and does not include currency effects.
4. For Singapore, corporate bonds outstanding quarterly figures are based on *AsianBondsOnline* estimates.
Source: People's Republic of China (*ChinaBond*); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Stock Exchange and Bank Indonesia); Republic of Korea (Bank of Korea and *KoreaBondWeb*); Malaysia (Bank Negara Malaysia); Philippines (Bureau of the Treasury and Bloomberg LP); Singapore (Singapore Government Securities, Monetary Authority of Singapore, and Bloomberg LP); Thailand (Bank of Thailand); and Viet Nam (Bloomberg LP).

The only markets to accelerate their q-o-q growth rates in 3Q10 were Indonesia, the Republic of Korea, Philippines, and Singapore. The Philippines' q-o-q growth rate rose to 3.6% in 3Q10 from 2.5% in 2Q10. Singapore's growth rate rose to 3.1% q-o-q from 1.8%, almost entirely due to growth in the corporate bond market of 7.1% q-o-q. The same was true in Indonesia, where q-o-q growth in the government bond market was flat in 3Q10, while the corporate bond market expanded 10.9%.

Total LCY government bonds outstanding in the region grew only 1.9% q-o-q in 3Q10, compared with 5.1% in 2Q10. The driver of overall bond market growth in emerging East Asia in 3Q10 was the corporate bond market, which exceeded its 2Q10 growth rate of 5.0% q-o-q to expand 5.7% q-o-q in 3Q10. The corporate bond market has grown rapidly in recent years and now accounts for 30% of the total emerging East Asian

Table 1: Size and Composition of Emerging East Asian LCY Bond Markets

	3Q09		2Q10		3Q10		Growth Rate (LCY-base %)				Growth Rate (USD-base %)			
	Amount (USD billion)	% share	Amount (USD billion)	% share	Amount (USD billion)	% share	3Q09		3Q10		3Q09		3Q10	
							q-o-q	y-o-y	q-o-q	y-o-y	q-o-q	y-o-y	q-o-q	y-o-y
China, People's Rep. of (PRC)														
Total	2,415	100.0	2,848	100.0	2,991	100.0	4.5	13.9	3.6	21.4	4.6	14.2	5.0	23.9
Government	2,015	83.4	2,302	80.8	2,377	79.5	3.1	5.7	1.9	15.6	3.1	6.0	3.3	18.0
Corporate	400	16.6	546	19.2	614	20.5	12.5	87.7	10.9	50.5	12.6	88.2	12.4	53.6
Hong Kong, China														
Total	129	100.0	159	100.0	161	100.0	15.4	39.0	1.3	25.8	15.4	39.3	1.7	25.6
Government	54	41.8	86	54.0	87	53.6	44.4	187.3	0.6	61.2	44.4	187.8	1.0	61.0
Corporate	75	58.2	73	46.0	75	46.4	0.9	1.4	2.1	0.3	0.9	1.6	2.4	0.2
Indonesia														
Total	90	100.0	109	100.0	112	100.0	0.1	17.7	1.1	14.9	5.8	16.8	2.6	24.6
Government	82	90.9	99	90.6	100	89.6	0.3	19.6	0.04	13.3	5.9	18.7	1.6	22.8
Corporate	8	9.1	10	9.4	12	10.4	(1.2)	1.3	10.9	30.7	4.4	0.5	12.6	41.7
Korea, Rep. of														
Total	1,001	100.0	1,029	100.0	1,126	100.0	2.6	16.0	1.8	8.7	11.1	17.7	9.5	12.5
Government	460	45.9	458	44.5	498	44.2	2.4	17.1	1.2	4.6	10.8	18.9	8.8	8.3
Corporate	542	54.1	571	55.5	628	55.8	2.9	15.1	2.3	12.1	11.3	16.8	10.0	16.1
Malaysia														
Total	181	100.0	216	100.0	234	100.0	2.7	5.5	3.7	15.1	4.1	4.7	8.4	29.4
Government	101	55.6	124	57.7	137	58.4	2.8	4.7	5.1	20.9	4.2	3.9	9.9	35.9
Corporate	80	44.4	91	42.3	97	41.6	2.5	6.5	1.7	7.8	3.9	5.8	6.4	21.2
Philippines														
Total	59	100.0	66	100.0	72	100.0	2.3	7.5	3.6	13.0	3.4	6.3	9.4	22.4
Government	53	88.9	58	87.8	64	88.0	2.0	3.0	3.8	11.8	3.0	1.8	9.7	21.1
Corporate	7	11.1	8	12.2	9	12.0	5.4	65.8	1.7	22.4	6.5	63.9	7.4	32.6
Singapore														
Total	150	100.0	162	100.0	177	100.0	5.6	15.3	3.1	9.9	8.6	17.5	9.4	17.5
Government	87	57.9	92	56.7	97	55.0	6.0	20.7	0.0	4.5	9.1	23.0	6.1	11.7
Corporate	63	42.1	70	43.3	80	45.0	5.0	8.6	7.1	17.5	8.1	10.7	13.7	25.6
Thailand														
Total	172	100.0	198	100.0	217	100.0	6.2	15.8	2.5	14.2	8.3	17.0	9.5	26.0
Government	136	79.2	160	80.7	176	81.3	6.6	13.1	3.3	17.3	8.6	14.4	10.4	29.4
Corporate	36	20.8	38	19.3	40	18.7	5.0	27.2	(1.2)	2.6	7.0	28.6	5.6	13.1
Viet Nam														
Total	13	100.0	15	100.0	15	100.0	5.5	6.4	(1.0)	27.4	5.2	(1.0)	(3.1)	16.7
Government	12	92.7	14	90.8	14	91.3	2.8	3.3	(0.5)	25.5	2.6	(3.9)	(2.6)	15.0
Corporate	0.9	7.3	1	9.2	1	8.7	55.9	72.0	(6.1)	51.9	55.5	60.0	(8.1)	39.2
Emerging East Asia (EEA)														
Total	4,209	100.0	4,802	100.0	5,106	100.0	4.2	14.7	3.0	17.2	6.7	15.3	6.3	21.3
Government	2,998	71.2	3,392	70.6	3,550	69.5	3.6	9.5	1.9	14.6	5.3	10.0	4.7	18.4
Corporate	1,211	28.8	1,410	29.4	1,556	30.5	5.8	29.7	5.7	23.8	10.1	31.2	10.4	28.5
EEA Less PRC														
Total	1,795	100.0	1,954	100.0	2,115	100.0	3.9	15.7	2.1	11.8	9.6	16.9	8.2	17.8
Government	983	54.8	1,090	55.8	1,172	55.4	4.7	18.1	1.8	12.5	10.1	19.2	7.6	19.2
Corporate	811	45.2	864	44.2	942	44.6	2.9	12.9	2.5	10.9	9.0	14.1	9.1	16.1
Japan														
Total	9,831	100.0	10,466	100.0	11,228	100.0	1.3	2.3	1.1	6.3	8.8	21.2	7.3	14.2
Government	8,829	89.8	9,453	90.3	10,149	90.4	1.3	2.3	1.2	7.0	8.8	21.2	7.4	15.0
Corporate	1,001	10.2	1,013	9.7	1,079	9.6	1.2	2.4	0.3	0.2	8.6	21.2	6.5	7.7

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

Notes:

1. For Singapore, corporate bonds outstanding quarterly figures are based on *AsianBondsOnline* estimates.
2. Corporate bonds include issues by financial institutions.
3. Bloomberg LP end-of-period LCY—USD rates are used.
4. For LCY-base, emerging East Asia growth figures are based on end-September 2010 currency exchange rates and do not include currency effects.
5. Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.

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

bond market. Much attention has been given to the large inflows of foreign capital into the region's government bond markets, but there is also evidence of inflows of foreign capital into the region's corporate bond markets. Easy monetary conditions in mature markets, and more recently the quantitative easing policy of the United States (US) Federal Reserve, means that foreign investors may increase their exposure to LCY corporate bonds.

Total government bonds outstanding grew by 1.9% q-o-q in 3Q10, reflecting low growth rates for all markets except Malaysia, the Philippines, and Thailand.

The rapid growth of the government bond market was supported in 2Q10 by reform and restructuring measures in almost all emerging East Asian markets. However, in 3Q10 this strong growth trend was slowed by (i) a sharp reduction in issuance by the People's Bank of China (PBOC), (ii) an overall reduction in LCY bond issuance by the governments and central banks of both Indonesia and the Republic of Korea, and (iii) decreased issuance of treasury and other types of government bonds in Hong Kong, China; Thailand; and Viet Nam. The only markets to report significant growth in government bonds outstanding were Malaysia, the Philippines, and Thailand, which expanded 5.1%, 3.8%, and 3.3% q-o-q, respectively, and 20.9%, 11.8%, and 17.3% y-o-y, respectively.

In Malaysia, outstanding government LCY bonds surged 20.9% y-o-y to MYR421.6 billion, mainly due to the increase in outstanding central bank bills as Bank Negara Malaysia (BNM) continued to mop up excess liquidity in the market. Consumer price inflation in Malaysia rose between January and August due to an increase in domestic demand as public sector spending fueled economic growth. In September, consumer price inflation slid to 1.8% y-o-y from 2.1% in August.

Also, with the relaxation of foreign exchange rules, the Malaysian ringgit gained against the US dollar in 2Q10 and government bonds rallied on expectations of the ringgit's further appreciation, which has already gained 8.7% against the US dollar since the beginning of the year.

Meanwhile, outstanding government LCY bonds in the Philippines rose 11.8% y-o-y to PHP2.8 trillion as of end-September, mainly due to the 15.6% y-o-y increase in outstanding government treasury bonds. In 3Q10, the government issued a total of PHP113.3 billion in government bonds (including PHP97.5 billion worth of 5-, 7-, and 10-year retail treasury bonds) to finance the fiscal deficit. The Philippine government posted a PHP259.8 billion fiscal deficit in the first 9 months of 2010 and has set its budget deficit ceiling for all of 2010 at PHP325 billion, or approximately 3.9% of gross domestic product (GDP).

The growth of outstanding government bonds in Thailand was driven more by issuance from the Bank of Thailand (BOT), resulting in BOT bonds and bills growing by 7.3% q-o-q compared with a 1.2% increase for central government bonds and a 2.2% decline for bonds of state-owned companies. Issuance by the central government in 3Q10 fell by 22.6% q-o-q due to a reduction of the expected budget deficit to 3.8% of GDP in the fiscal year 2010 (ending 30 September) compared with 4.3% in fiscal 2009.

The corporate bond market in emerging East Asia expanded 5.7% q-o-q in 3Q10, compared with 4.9% in the previous quarter, led by the PRC, Indonesia, and Singapore.

The Indonesian and Singaporean corporate bond markets grew 10.9% and 7.1% q-o-q, respectively, and were followed by the Republic of Korea's corporate bond market, which grew 2.3% in 3Q10. The fast-growing PRC corporate bond market expanded by 10.9% q-o-q and 50.5% y-o-y in 3Q10 on the back of continued growth in the medium-term note (MTN) and commercial paper markets, while the state-owned enterprise (SOE) segment staged a recovery from a slowdown in 2Q10. These trends offset the decline in bond issuance by commercial banks in the PRC since the beginning of the year. Commercial bank bond issuance in the PRC is mostly in the form of subordinated notes, which can be counted as Tier II capital under the rules of the Bank for International Settlements. Banks in the PRC issued large amounts of subordinated bonds in 2008 and 2009, but have issued much less this year amid new equity issues.

The MTN market, which has helped spur massive growth in domestic corporate bonds over the past 2 years, posted substantial growth of 12.0% q-o-q in 3Q10, although this was down from 17.9% in the previous quarter. The q-o-q growth rate of the commercial paper market—the third largest sector within the PRC's corporate bond market—fell to 9.0% in 3Q10 from 21.0% in 2Q10. These declines were largely offset by the SOE sector's q-o-q growth rate of 7.9% in 3Q10, which was up from only 1.3% in 2Q10. The rise in q-o-q growth for SOE bonds may reflect a shift in corporate funding requirements to more long-term bonds, compared with the short- to medium-term funds available in the MTN and commercial paper markets.

The growth of the Indonesian and Singaporean corporate bond markets, however, was in many ways more impressive, because their growth reflects foreign investment funds' interest in these markets as being home to desirable investment securities. Furthermore, both of these corporate bond markets benefit from relatively open investment environments. As a result, they are becoming more liquid and attracting greater interest from foreign and domestic investors alike.

The 2.3% q-o-q growth rate for the Republic of Korea's corporate bond market in 3Q10 reflects major differences in growth rates for the major sectors of its large and diverse corporate bond sector. The commercial bank debenture sector, which accounts for about 29% of total corporate bonds, declined in size by 1.4% q-o-q and 4.1% y-o-y in 3Q10. However, the larger special public bond sector, which accounts for about 35% of the total corporate bond market, grew 6.6% q-o-q and 34.0% y-o-y, while the private corporate bond sector, which is about 36.0% of the total corporate bond market, grew 1.3% q-o-q and 9.6% y-o-y.

The Philippine corporate bond market grew only 1.7% q-o-q in 3Q10, compared with 5.5% in 2Q10, in part due to large amounts of corporate issuance in US dollars during the quarter. However, market observers are hopeful for a recovery in peso bond corporate issuance during the rest of 2010 and early 2011, due to investment opportunities in the infrastructure and energy sectors, as well as increasing foreign interest in the Philippines and the higher returns offered by its corporate bonds.

The most important activity being financed by this rush of new corporate bond issuance in emerging East Asia is finance itself.[3] The largest volume of bonds outstanding was issued by companies in the financial sector, ranging from banks to securities companies to government-owned housing finance companies. Typically, the second- and third-largest volumes of corporate bonds outstanding in any particular market in 3Q10 were to be found in energy and infrastructure, respectively, although consumer goods companies were also important corporate bond issuers in some markets.

The only real exception to this generalization is the PRC, where energy companies have issued the largest stock of corporate bonds outstanding. Finance—mostly in the form of subordinated debt bonds issued by commercial banks—is second, followed closely by a category of diverse conglomerates, and then infrastructure.

Given the strong revival of the Asian growth outlook at present, a new cycle of energy and infrastructure investment can be expected to follow in the coming years, with much of it possibly financed by corporate bond issuance given the trend toward privatization of energy and infrastructure in emerging East Asia. There is also the possibility of expanded use of public–private partnerships for this purpose. More detail on individual corporate bond issuers can be found in the Market Summaries for each bond market at the end of this report.

[3] This trend in the emerging East Asian corporate bond market was analyzed previously in the October issue of the *Asia Bond Monitor* (Chapter 2: Corporate Bond Market Developments).

Ratio of Bonds Outstanding to Gross Domestic Product

The ratio of LCY bonds outstanding to GDP in emerging East Asia was slightly larger in 3Q10 than in 2Q10.

The ratio of LCY bonds outstanding to GDP in 3Q10 stood at 60.2%, which was slightly higher than the 58.7% reported for 2Q10 **(Table 2)**. This reflected a slight rise in the ratio of government bonds to GDP from 41.5% in 2Q10 to 41.8% in 3Q10, and a somewhat larger increase in the ratio of corporate bonds to GDP from 17.2% in 2Q10 to 18.3% in 3Q10. The four markets that saw the greatest increase in their respective ratios of total bonds outstanding to GDP were the Republic of Korea, Malaysia, Singapore, and Thailand, while the only markets to see a decline in this ratio were Hong Kong, China; Indonesia; and Viet Nam. The PRC's ratio of total bonds to GDP was virtually unchanged.

Issuance

LCY bond issuance in emerging East Asia in 3Q10 totaled USD1.02 trillion, which represented increases of 6.0% q-o-q and 0.8% y-o-y.

Total issuance of USD1.02 trillion in 3Q10 represented a 6.0% increase from USD938 billion in 2Q10, and a 0.8% increase from USD982 billion in 3Q09 **(Table 3)**. Government bond issuance expanded 4.6% q-o-q, while corporate issuance grew 12.3%. In the government bond sector, issuance by central banks and monetary authorities rose by 4.2% q-o-q, while issuance of treasuries and other types of government bonds rose by 5.8% q-o-q, but fell by 7.2% on a y-o-y basis.

The 4.2% q-o-q growth rate for issuance by central banks and monetary authorities masked wider regional disparities. While issuance by the central banks of Thailand and Malaysia increased by 28.2% and 11.4% q-o-q, respectively, issuance by the central banks of the PRC, Indonesia, and the Republic of Korea actually declined.

Table 2: Size and Composition of Emerging East Asian LCY Bond Markets (% of GDP)

	3Q09	2Q10	3Q10
China, People's Rep. of			
Total	50.2	52.9	52.9
Government	41.9	42.7	42.1
Corporate	8.3	10.1	10.9
Hong Kong, China			
Total	61.5	72.9	72.2
Government	25.7	39.3	38.7
Corporate	35.8	33.6	33.5
Indonesia			
Total	15.9	16.5	16.1
Government	14.4	14.9	14.4
Corporate	1.4	1.6	1.7
Korea, Rep. of			
Total	113.3	112.5	123.2
Government	52.0	50.0	54.4
Corporate	61.3	62.4	68.7
Malaysia			
Total	93.3	95.3	103.3
Government	51.9	55.0	60.4
Corporate	41.4	40.4	42.9
Philippines			
Total	37.4	37.9	41.4
Government	33.2	33.2	36.4
Corporate	4.1	4.6	5.0
Singapore			
Total	80.7	79.2	86.6
Government	46.7	44.9	47.7
Corporate	34.0	34.3	39.0
Thailand			
Total	65.1	66.1	72.4
Government	51.6	53.3	58.9
Corporate	13.5	12.8	13.5
Viet Nam			
Total	14.0	16.5	15.6
Government	13.0	15.0	14.2
Corporate	1.0	1.5	1.4
Emerging East Asia			
Total	57.2	58.7	60.2
Government	40.7	41.5	41.8
Corporate	16.5	17.2	18.3
Japan			
Total	184.0	194.2	195.2
Government	165.2	175.4	176.5
Corporate	18.7	18.8	18.8

GDP = gross domestic product, LCY = local currency.
Notes:
1. Data for GDP is from CEIC. 3Q10 GDP figures for the Republic of Korea, Malaysia, Philippines, Singapore, and Thailand were carried over from 2Q10.
2. For Singapore, corporate bonds outstanding quarterly figures are based on *AsianBondsOnline* estimates.
Source: People's Republic of China (*ChinaBond*); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Stock Exchange and Bank Indonesia); Republic of Korea (Bank of Korea and *KoreaBondWeb*); Malaysia (Bank Negara Malaysia); Philippines (Bureau of the Treasury and Bloomberg LP); Singapore (Monetary Authority of Singapore, Singapore Government Securities, and Bloomberg LP); Thailand (Bank of Thailand); Viet Nam (Bloomberg LP); and Japan (Japan Securities Dealers Association).

Table 3: LCY-Denominated Bond Issuance (gross)

	LCY billion		USD billion		Growth Rate (LCY-base %)		Growth Rate (USD-base %)	
	3Q10	% share	3Q10	% share	3Q10		3Q10	
					q-o-q	y-o-y	q-o-q	y-o-y
China, People's Rep. of								
Total	2,816	100.0	421	100.0	(0.1)	(5.0)	1.2	(3.1)
Government	2,222	78.9	332	78.9	(6.5)	(9.1)	(5.3)	(7.2)
Central Bank	1,274	45.2	190	45.2	(18.2)	(13.4)	(17.1)	(11.6)
Treasury and Other Govt	949	33.7	142	33.7	15.7	(2.5)	17.3	(0.5)
Corporate	594	21.1	89	21.1	34.3	14.0	36.2	16.3
Hong Kong, China								
Total	1,889	100.0	243	100.0	39.6	44.2	40.1	44.1
Government	1,844	97.6	238	97.6	40.3	46.2	40.7	46.0
Central Bank	1,841	97.5	237	97.5	40.5	46.3	40.9	46.1
Treasury and Other Govt	4	0.2	0.5	0.2	(22.2)	0.0	(22.0)	(0.1)
Corporate	45	2.4	6	2.4	16.8	(6.7)	17.2	(6.8)
Indonesia								
Total	264,115	100.0	30	100.0	(20.2)	(41.2)	(19.0)	(36.3)
Government	252,618	95.6	28	95.6	(22.0)	(43.4)	(20.7)	(38.7)
Central Bank	220,518	83.5	25	83.5	(21.5)	(47.5)	(20.3)	(43.1)
Treasury and Other Govt	32,100	12.2	4	12.2	(24.8)	22.2	(23.6)	32.5
Corporate	11,497	4.4	1	4.4	57.4	325.8	59.9	361.7
Korea, Rep. of								
Total	161,815	100.0	143	100.0	(12.8)	(25.2)	(6.2)	(22.5)
Government	80,457	49.7	71	49.7	(20.6)	(46.2)	(14.5)	(44.3)
Central Bank	57,190	35.3	50	35.3	(23.1)	(50.5)	(17.2)	(48.8)
Treasury and Other Govt	23,267	14.4	20	14.4	(13.6)	(31.7)	(7.1)	(29.2)
Corporate	81,358	50.3	72	50.3	(3.5)	22.3	3.8	26.6
Malaysia								
Total	115	100.0	37	100.0	7.7	29.6	12.6	45.7
Government	93	81.2	30	81.2	11.3	42.9	16.4	60.7
Central Bank	76	66.2	25	66.2	11.4	87.7	16.5	111.0
Treasury and Other Govt	17	15.0	6	15.0	11.0	(30.4)	16.0	(21.7)
Corporate	22	18.8	7	18.8	(5.8)	(7.6)	(1.5)	3.9
Philippines								
Total	181	100.0	4	100.0	24.0	(25.6)	31.0	(19.3)
Government	176	97.2	4	97.2	37.5	(24.6)	45.3	(18.2)
Central Bank	0	0.0	0	0.0	—	—	—	—
Treasury and Other Govt	176	97.2	4	97.2	37.5	(24.6)	45.3	(18.2)
Corporate	5	2.8	0.1	2.8	(71.8)	(49.2)	(70.2)	(44.9)

continued on next page

Table 3 continued

	LCY billion		USD billion		Growth Rate (LCY-base %)		Growth Rate (USD-base %)	
	3Q10	% share	3Q10	% share	3Q10 q-o-q	3Q10 y-o-y	3Q10 q-o-q	3Q10 y-o-y
Singapore								
Total	62	100.0	47	100.0	7.3	23.9	13.9	32.5
Government	56	90.6	42	90.6	3.5	19.0	9.9	27.2
Central Bank	0	0.0	0	0.0	—	—	—	—
Treasury and Other Govt	56	90.6	42	90.6	3.5	19.0	9.9	27.2
Corporate	6	9.4	4	9.4	64.8	104.4	74.9	118.5
Thailand								
Total	2,991	100.0	99	100.0	16.5	9.8	24.5	21.1
Government	2,767	92.5	91	92.5	20.7	11.7	29.0	23.2
Central Bank	2,504	83.7	83	83.7	28.2	26.9	37.1	40.0
Treasury and Other Govt	263	8.8	9	8.8	(22.6)	(47.8)	(17.2)	(42.4)
Corporate	224	7.5	7	7.5	(18.5)	(8.9)	(12.9)	0.4
Viet Nam								
Total	8,650	100.0	0.4	100.0	(87.5)	(51.9)	(87.8)	(55.9)
Government	6,700	77.5	0.3	77.5	(89.4)	(43.6)	(89.6)	(48.3)
Central Bank	0	0.0	0.0	0.0	—	—	—	—
Treasury and Other Govt	6,700	77.5	0.3	77.5	(89.4)	(33.9)	(89.6)	(39.5)
Corporate	1,950	22.5	0.1	22.5	(66.7)	(68.0)	(67.4)	(70.7)
Emerging East Asia (EEA)								
Total	—	—	1,024	100.0	6.0	0.8	9.1	4.2
Government	—	—	837	81.8	4.6	(2.0)	7.4	1.4
Central Bank	—	—	610	59.6	4.2	0.1	6.8	3.3
Treasury and Other Govt	—	—	227	22.2	5.8	(7.2)	9.2	(3.5)
Corporate	—	—	187	18.2	12.3	15.6	17.5	19.5
EEA Less PRC								
Total	—	—	603	100.0	10.7	5.3	15.4	10.0
Government	—	—	505	83.8	13.5	3.3	17.8	7.9
Central Bank	—	—	420	69.6	19.1	7.7	22.8	11.9
Treasury and Other Govt	—	—	85	14.2	(7.5)	(14.0)	(2.0)	(8.2)
Corporate	—	—	98	16.2	(2.2)	17.1	4.4	22.6
Japan								
Total	50,046	100.0	600	100.0	5.3	4.2	11.8	11.9
Government	45,605	91.1	546	91.1	4.7	4.4	11.1	12.2
Central Bank	0	0.0	0	0.0	—	—	—	—
Treasury and Other Govt	45,605	91.1	546	91.1	4.7	4.4	11.1	12.2
Corporate	4,441	8.9	53	8.9	12.1	1.9	19.0	9.5

— = not applicable, LCY = local currency, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Corporate bonds include issues by financial institutions.
2. Bloomberg LP end-of-period LCY–USD rates are used.
3. For LCY-base, emerging East Asia growth figures are based on end-September 2010 currency exchange rates and do not include currency effects.
Source: People's Republic of China (*ChinaBond*); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Debt Management Office, Indonesia Stock Exchange, and Bank Indonesia); Republic of Korea (Bank of Korea); Malaysia (Bank Negara Malaysia); Philippines (Bloomberg LP); Singapore (Singapore Government Securities and Bloomberg LP); Thailand (Bank of Thailand); Viet Nam (Bloomberg LP); and Japan (Japan Securities Dealers Association).

The rise in overall central bank and monetary authority issuance in the region in 3Q10 is mostly explained by the 40.5% q-o-q increase in issuance by the Hong Kong Monetary Authority (HKMA). HKMA's issuance totaling USD237 billion (equivalent) in 3Q10 was larger than the USD190 billion (equivalent) of bonds and bills issued by the PBOC. HKMA's issuance pattern follows its currency board regime for managing Hong Kong, China's monetary policy and exchange rate.

Some monetary authorities have introduced capital controls and other administrative measures to offset the impact of rising capital inflows.

Bank Indonesia's issuance declined in 3Q10 because it began shifting most of its issuance from 1-month Sertifikat Bank Indonesia (SBIs) to 3-, 6-, and 9-month SBIs, sharply reducing roll-over financing requirements. Bank Indonesia also reduced its auction calendar from a weekly to monthly basis.

The Bank of Thailand's issuance reflected growing concerns over foreign capital inflows in 3Q10, which resulted in the imposition of a withholding tax on interest and capital gains for government securities, and the effective removal of all remaining controls on capital outflows.

In June, the Republic of Korea announced macro-prudential measures to mitigate the volatility of capital flows. On 18 November, the Republic of Korea's government announced it supported legislation being considered in the National Assembly to reimpose a 14% withholding tax on interest income and a 20% levy on capital gains from government bonds held by foreigners.

BNM increased its issuance of BNM bills in 3Q10 as the Malaysian central bank mopped up excess liquidity in the market amid concern over inflationary pressures in the economy.

In the PRC, issuance by the PBOC, which accounts for 31% of total central bank and monetary authority bond issuance in emerging East Asia, declined by 18.2% q-o-q in 3Q10 as the PBOC began to tighten its monetary policy over concerns about inflation, particularly with respect to housing and food prices. On 20 October, the PBOC raised by 25 basis points each its 1-year lending rate to 5.56% and 1-year deposit rate to 2.50%, respectively.

Issuance by government entities (excluding central banks and monetary authorities) in 3Q10 was modest as governments in the region have generally begun to reduce their fiscal stimulus programs that were initiated in response to the global financial crisis. In fact, issuance of treasuries and other types of government bonds fell on a q-o-q basis 89.4% in Viet Nam; 24.8% in Indonesia; 22.6% in Thailand; 22.2% in Hong Kong, China; and 13.6% in the Republic of Korea. Government bond issuance grew 37.5% q-o-q in the Philippines as the new government responded to an increased 2010 budget deficit. PRC government bond issuance (including issuance by policy banks) rose 15.7% q-o-q, although it shrank 2.5% on a y-o-y basis.

Corporate issuance was the major driver of growth in overall issuance in the region in 3Q10, rising 12.3% q-o-q and 15.6% y-o-y. The q-o-q rise in corporate issuance was especially large in the PRC, Indonesia, and Singapore, growing at rates of 34.3%, 57.4%, and 64.8%, respectively. Corporate bond issuance declined sharply on a q-o-q basis in the Philippines, Thailand, and Viet Nam, with more modest declines seen in the Republic of Korea and Malaysia. Some of the region's declines in LCY corporate issuance may be the result of local companies arbitraging the LCY and foreign currency (FCY) markets in order to issue in US dollars or FCY while the monetary policy of the US Federal Reserve remains accommodative. Other market observers, however, believe that the downturn in LCY corporate bond issuance in some markets in 3Q10 merely reflected a respite from very active issuance in 1Q10 and 2Q10, and a new wave of issuance will take place in these markets—including the Philippines—in 4Q10 and early next year.

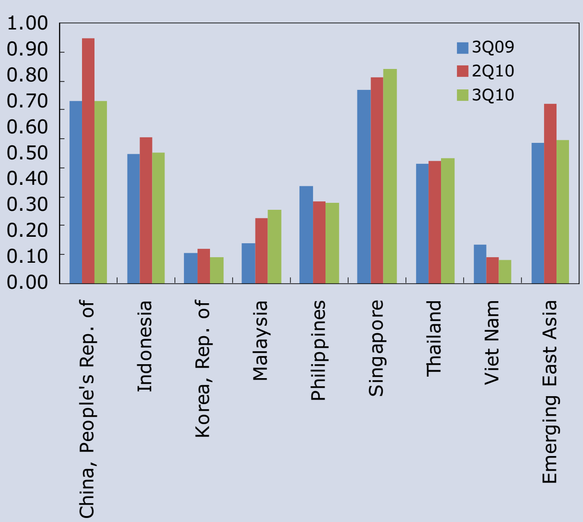
Money Market Trends and Bills-to-Bonds Ratios

The bills-to-bonds ratio fell in most emerging East Asian markets in 3Q10, mainly due to a decline in the ratio of central bank bills to bonds, rather than the ratio of treasury bills to bonds.

The total bills-to-bonds ratio for five of the eight emerging East Asian markets surveyed fell in 3Q10 on a q-o-q basis **(Figure 2)**. In addition, the bills-to-bonds ratio in Hong Kong, China also fell to 6.49 in 3Q10 from 6.74 in 2Q10. However, Hong Kong, China is not presented in Figure 2 as its ratio of bills to bonds is significantly higher than any other market in the region.

The primary reason for the drop in the total bills-to-bonds ratio in 3Q10 was the sharp decline in the region's ratio of central bank bills to bonds, which fell to 2.13 from 3.53 in 2Q10 **(Table 4)**. This, in turn, reflected a drop in the PRC's ratio of central bank bills to bonds from 9.88 in 1Q10 to 6.37 in 2Q10, and then to 2.76 in 3Q10. In 2Q10, the PRC's stock of central bank bonds rose by almost 60% q-o-q, and then again by 83.7% q-o-q in 3Q10. However, the PRC sharply cut its stock of central bank bills, which was more than six times larger than its stock of bonds at the end of 2Q10, by 20.5% q-o-q in 3Q10, resulting in an 18.2% reduction in the PBOC's total issuance.

Figure 2: Total Bills-To-Bonds Ratios



Note:
Total bills comprise central bank bills plus treasury bills. Bonds comprise long-term bonds (more than 1 year in maturity) issued by central governments and central banks.
Source: *AsianBondsOnline*.

The treasury bills-to-bond ratio for the region as a whole in 3Q10 was virtually unchanged from 2Q10 at 0.12. The ratio of treasury bills to bonds fell slightly in Viet Nam and Thailand, but these declines were more than offset by a rise in Singapore's ratio. Meanwhile, the ratio of treasury bills to bonds remained stable in Indonesia and the PRC.

The stabilization of the region's ratio of treasury bills to bonds has been a consequence of the reduction in growth rates for both treasury bonds and bills in recent quarters, as governments appear to be easing up on their various economic stimulus programs. The overall modest decline of the region's central bank bills-to-bonds ratio in 3Q10 indicates that central banks and monetary authorities have moderated their use of sterilization as a tool for dealing with the large capital inflows of the last year and, instead, may be focusing on selective capital controls and other administrative approaches to this problem.

Foreign Holdings

Foreign holdings of local domestic bonds continue to soar as investors chase yields, participate in the region's economic recovery, and seek to make additional gains from the anticipated appreciation of regional currencies.

At the end of September, foreigners held 28.3% of Indonesian government debt. High yields and better economic prospects continued to attract foreign investors to Indonesian government bonds **(Figure 3)**. Foreign holdings of Thai government bonds rose to 6.1% in 3Q10 from 4.2% in 2Q10. Meanwhile, the portion of foreign holdings at the end of June was 18.1% in Malaysia and 8.7%

Table 4: Government Bills-to-Bonds Ratios of Emerging East Asian LCY Bond Markets

	3Q09		2Q10		3Q10		Government Bills to Bonds Ratio			Growth Rate (LCY-base %) 3Q10		Growth Rate (USD-base %) 3Q10	
	Amount (USD billion)	% share	Amount (USD billion)	% share	Amount (USD billion)	% share	3Q09	2Q10	3Q10	q-o-q	y-o-y	q-o-q	y-o-y
China, People's Rep. of (PRC)													
Total	1,358.6	100.0	1,516.6	100.0	1,523.0	100.0				(0.9)	9.9	0.4	12.1
Total Bills	524.8	38.6	695.8	45.9	587.7	38.6	0.63	0.85	0.63	(16.7)	9.7	(15.5)	12.0
Treasury Bills	110.1	8.1	92.1	6.1	101.1	6.6	0.17	0.13	0.13	8.3	(10.0)	9.8	(8.2)
Central Bank Bills	414.7	30.5	603.7	39.8	486.6	31.9	2.39	6.37	2.76	(20.5)	15.0	(19.4)	17.3
Total Bonds	833.7	61.4	820.8	54.1	935.3	61.4				12.4	9.9	14.0	12.2
Treasury Bonds	660.5	48.6	726.0	47.9	758.8	49.8				3.1	12.6	4.5	14.9
Central Bank Bonds	173.2	12.8	94.8	6.3	176.5	11.6				83.7	(0.1)	86.2	1.9
Hong Kong, China													
Total	53.7	100.0	85.7	100.0	86.5	100.0				0.6	61.2	1.0	61.0
Total Bills	44.3	82.5	74.6	87.1	75.0	86.6	4.70	6.74	6.49	0.1	69.4	0.5	69.2
Treasury Bills	0.0	0.0	0.0	0.0	0.0	0.0	—	—	—	—	—	—	—
Central Bank Bills	44.3	82.5	74.6	87.1	75.0	86.6	4.93	8.28	8.29	0.1	69.4	0.5	69.2
Total Bonds	9.4	17.5	11.1	12.9	11.6	13.4				4.1	22.7	4.4	22.6
Treasury Bonds	0.5	0.8	2.1	2.4	2.5	2.9				21.9	—	22.3	—
Central Bank Bonds	9.0	16.7	9.0	10.5	9.0	10.5				0.0	0.9	0.3	0.7
Indonesia													
Total	81.7	100.0	98.6	100.0	100.2	100.0				0.0	13.0	1.6	22.5
Total Bills	25.3	30.9	33.1	33.6	31.1	31.1	0.45	0.51	0.45	(7.4)	13.7	(5.9)	23.3
Treasury Bills	2.4	3.0	3.2	3.2	3.4	3.4	0.04	0.05	0.05	4.7	27.4	6.4	38.2
Central Bank Bills	22.8	27.9	29.9	30.4	27.8	27.7	—	—	—	(8.7)	12.2	(7.2)	21.7
Total Bonds	56.5	69.1	65.5	66.4	69.0	68.9				3.8	12.7	5.4	22.2
Treasury Bonds	56.5	69.1	65.5	66.4	69.0	68.9				3.8	12.7	5.4	22.2
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—
Korea, Rep. of													
Total	361.1	100.0	393.0	100.0	426.0	100.0				0.8	13.9	8.4	18.0
Total Bills	34.8	9.6	41.6	10.6	36.3	8.5	0.11	0.12	0.09	(19.1)	0.6	(12.9)	4.1
Treasury Bills	0.0	0.0	0.0	0.0	0.0	0.0	—	—	—	—	—	—	—
Central Bank Bills	34.8	9.6	41.6	10.6	36.3	8.5	0.42	0.43	0.33	(19.1)	0.6	(12.9)	4.1
Total Bonds	326.3	90.4	351.4	89.4	389.8	91.5				3.1	15.4	10.9	19.4
Treasury Bonds	243.7	67.5	253.8	64.6	281.2	66.0				3.0	11.4	10.8	15.4
Central Bank Bonds	82.6	22.9	97.6	24.8	108.6	25.5				3.4	27.0	11.2	31.5
Malaysia													
Total	99.3	100.0	124.1	100.0	136.4	100.0				5.1	22.1	9.9	37.3
Total Bills	12.0	12.1	22.7	18.3	27.6	20.2	0.14	0.22	0.25	16.0	104.0	21.3	129.4
Treasury Bills	1.2	1.3	1.3	1.1	1.4	1.0	0.01	0.01	0.01	0.0	0.0	4.6	12.4
Central Bank Bills	10.8	10.9	21.4	17.3	26.2	19.2	—	—	—	17.0	116.0	22.4	142.9
Total Bonds	87.3	87.9	101.3	81.7	108.8	79.8				2.6	10.9	7.3	24.6
Treasury Bonds	87.3	87.9	101.3	81.7	108.8	79.8				2.6	10.9	7.3	24.6
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—
Philippines													
Total	50.8	100.0	55.3	100.0	60.7	100.0				4.0	10.5	9.9	19.7
Total Bills	12.8	25.2	12.2	22.1	13.2	21.7	0.34	0.28	0.28	1.9	(4.8)	7.7	3.2
Treasury Bills	12.8	25.2	12.2	22.1	13.2	21.7	0.34	0.28	0.28	1.9	(4.8)	7.7	3.2
Central Bank Bills	0.0	0.0	0.0	0.0	0.0	0.0	—	—	—	—	—	—	—
Total Bonds	38.0	74.8	43.0	77.9	47.6	78.3				4.6	15.6	10.5	25.2
Treasury Bonds	38.0	74.8	43.0	77.9	47.6	78.3				4.6	15.6	10.5	25.2
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—

continued on next page

Table 4 continued

	3Q09		2Q10		3Q10		Government Bills to Bonds Ratio			Growth Rate (LCY-base %)		Growth Rate (USD-base %)	
	Amount (USD billion)	% share	Amount (USD billion)	% share	Amount (USD billion)	% share	3Q09	2Q10	3Q10	3Q10 q-o-q	3Q10 y-o-y	3Q10 q-o-q	3Q10 y-o-y
Singapore													
Total	87.1	100.0	91.7	100.0	97.3	100.0				0.0	4.5	6.1	11.7
Total Bills	35.0	40.2	38.0	41.5	41.4	42.5	0.67	0.71	0.74	2.6	10.5	8.9	18.2
Treasury Bills	35.0	40.2	38.0	41.5	41.4	42.5	0.67	0.71	0.74	2.6	10.5	8.9	18.2
Central Bank Bills	0.0	0.0	0.0	0.0	0.0	0.0	—	—	—	—	—	—	—
Total Bonds	52.1	59.8	53.7	58.5	55.9	57.5				(1.9)	0.4	4.1	7.3
Treasury Bonds	52.1	59.8	53.7	58.5	55.9	57.5				(1.9)	0.4	4.1	7.3
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—
Thailand													
Total	120.5	100.0	143.8	100.0	159.8	100.0				3.9	20.2	11.1	32.6
Total Bills	35.3	29.3	42.9	29.8	47.6	29.8	0.41	0.43	0.42	3.7	22.2	10.9	34.8
Treasury Bills	8.4	7.0	5.8	4.0	5.1	3.2	0.13	0.08	0.06	(17.6)	(45.2)	(12.0)	(39.6)
Central Bank Bills	26.9	22.3	37.1	25.8	42.5	26.6	1.20	1.35	1.34	7.1	43.2	14.4	58.0
Total Bonds	85.2	70.7	100.9	70.2	112.2	70.2				4.0	19.4	11.2	31.7
Treasury Bonds	62.8	52.1	73.4	51.0	80.5	50.4				2.6	16.3	9.7	28.3
Central Bank Bonds	22.4	18.6	27.5	19.1	31.7	19.8				7.6	28.1	15.1	41.3
Viet Nam													
Total	5.8	100.0	6.3	100.0	6.1	100.0				(1.7)	14.1	(3.8)	4.5
Total Bills	0.7	11.9	0.5	8.3	0.5	7.5	0.13	0.09	0.08	(11.9)	(28.3)	(13.8)	(34.3)
Treasury Bills	0.6	10.2	0.5	8.2	0.5	7.5	0.12	0.09	0.08	(10.2)	(16.5)	(12.0)	(23.5)
Central Bank Bills	0.1	1.7	0.0	0.2	0.0	0.0	—	—	—	(100.0)	—	(100.0)	—
Total Bonds	5.1	88.1	5.8	91.7	5.6	92.5				(0.8)	19.8	(2.9)	9.7
Treasury Bonds	5.1	88.1	5.8	91.7	5.6	92.5				(0.8)	19.8	(2.9)	9.7
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—
Emerging East Asia (EEA)													
Total	2,218.7	100.0	2,515.1	100.0	2,596.1	100.0				0.2	12.8	3.2	17.0
Total Bills	725.1	32.7	961.6	38.2	860.3	33.1	0.49	0.62	0.50	(12.4)	15.1	(10.5)	18.6
Treasury Bills	170.6	7.7	153.1	6.1	166.0	6.4	0.14	0.12	0.12	5.1	(6.5)	8.4	(2.7)
Central Bank Bills	554.5	25.0	808.4	32.1	694.3	26.7	1.93	3.53	2.13	(15.7)	21.8	(14.1)	25.2
Total Bonds	1,493.6	67.3	1,553.5	61.8	1,735.8	66.9				7.8	11.8	11.7	16.2
Treasury Bonds	1,206.4	54.4	1,324.5	52.7	1,409.9	54.3				2.9	12.2	6.4	16.9
Central Bank Bonds	287.3	12.9	229.0	9.1	325.9	12.6				36.0	10.1	42.3	13.4
EEA Less PRC													
Total	860.1	100.0	998.5	100.0	1,073.0	100.0				1.8	17.4	7.5	24.8
Total Bills	200.2	23.3	265.8	26.6	272.6	25.4	0.30	0.36	0.34	(1.5)	28.5	2.6	36.1
Treasury Bills	60.5	7.0	61.0	6.1	64.9	6.0	0.11	0.10	0.10	0.5	(0.4)	6.3	7.3
Central Bank Bills	139.8	16.2	204.8	20.5	207.7	19.4	1.23	1.53	1.39	(2.1)	41.3	1.4	48.6
Total Bonds	659.9	76.7	732.7	73.4	800.5	74.6				2.9	14.0	9.2	21.3
Treasury Bonds	545.9	63.5	598.5	59.9	651.1	60.7				2.7	11.7	8.8	19.3
Central Bank Bonds	114.0	13.3	134.2	13.4	149.4	13.9				4.1	25.3	11.3	31.0
Japan													
Total	7,693.3	100.0	8,236.8	100.0	8,832.3	100.0				1.0	6.8	7.2	14.8
Total Bills	247.5	3.2	386.6	4.7	357.0	4.0	0.03	0.05	0.04	(13.0)	34.2	(7.7)	44.2
Treasury Bills	247.5	3.2	386.6	4.7	357.0	4.0	0.03	0.05	0.04	(13.0)	34.2	(7.7)	44.2
Central Bank Bills	0.0	0.0	0.0	0.0	0.0	0.0	—	—	—	—	—	—	—
Total Bonds	7,445.7	96.8	7,850.1	95.3	8,475.3	96.0				1.7	5.9	8.0	13.8
Treasury Bonds	7,445.7	96.8	7,850.1	95.3	8,475.3	96.0				1.7	5.9	8.0	13.8
Central Bank Bonds	0.0	0.0	0.0	0.0	0.0	0.0				—	—	—	—

— = not applicable, LCY = local currency, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Bloomberg LP end-of-period LCY—USD rates are used.
2. For LCY-base, emerging East Asia growth figures are based on end-September 2010 currency exchange rates and do not include currency effects.
3. Total figures for each market refer to bills and bonds issued by the central government and the central bank. They exclude bonds issued by policy banks and state-owned enterprises. Bills are defined as securities with original maturities of less than 1 year.
Source: People's Republic of China (*ChinaBond*); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Stock Exchange and Bank Indonesia); Republic of Korea (Bloomberg LP); Malaysia (Bank Negara Malaysia); Philippines (Bureau of the Treasury); Singapore (Singapore Government Securities); Thailand (Bloomberg LP); Viet Nam (Bloomberg LP); and Japan (Japan Securities Dealers Association).

in the Republic of Korea. Malaysian government securities attracted greater attention from foreign investors due to higher yields during the year and prospects for a stronger ringgit, which were in large part realized in August when Malaysia reached an agreement with the PRC on currency trading.

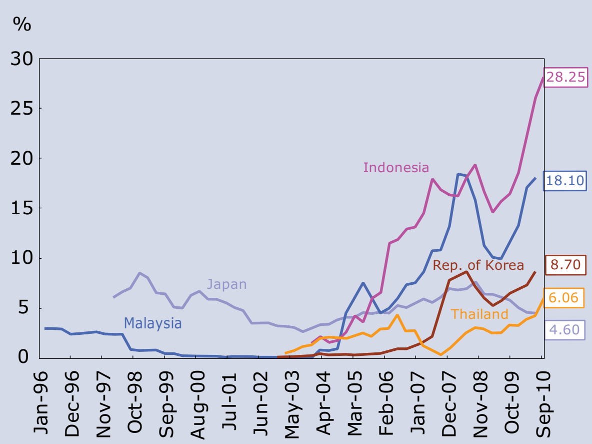
The Republic of Korea has seen a substantial rise in foreign holdings of its bonds this year, which reflects a number of factors: (i) removal of the withholding tax on government bonds in May 2009; (ii) improving performance of the Korea Treasury Bond (KTB) futures market, which makes it easier for market participants to hedge their investment positions; and (iii) entry of a new investor, the PRC, diversifying its foreign exchange holdings. The Financial Supervisory Service reported that the PRC's net bond investments in the Republic of Korea for the first 9 months of 2010 stood at KRW3.3 trillion, which was second only to Luxembourg with KRW5.5 trillion.

Maturity Profiles

The maturity profiles for emerging East Asian government and corporate bond sectors stand—in many cases—in stark contrast to one another.

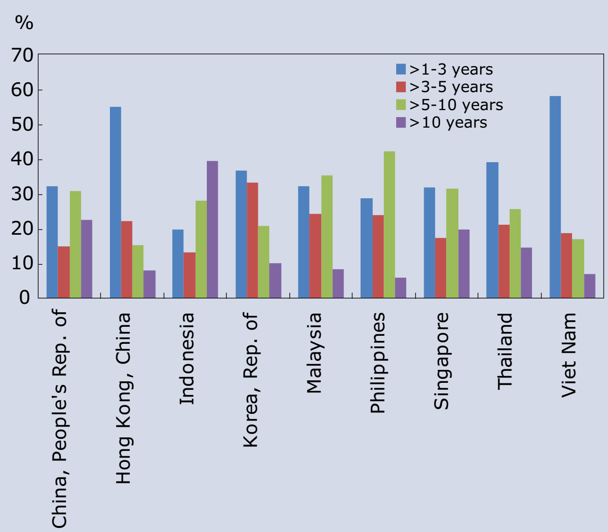
The maturity profile for most emerging East Asian government bond markets has changed little since the end of 2009. Maturities are concentrated at the shorter-end of the yield curve in Hong Kong, China; Republic of Korea; Thailand; and Viet Nam. These four markets, as well as markets in Malaysia and the Philippines, have 15% or less of their bonds outstanding in maturities of more than 10 years. The PRC and Singapore have a proportionately larger share of their bonds outstanding in maturities greater than 10 years. Indonesia, however, has structured its debt so that maturities of more than 10 years are the largest segment of its market **(Figure 4)**. It remains to be seen whether the region's governments will take advantage of lower bond yields to reduce the magnitude of their respective short-term maturities in the remaining months of 2010.

Figure 3: Foreign Holdings of LCY Government Bonds (% of total)



LCY = local currency.
Note: Data for Japan, Republic of Korea, and Malaysia as of June 2010; Indonesia and Thailand as of September 2010.
Source: *AsianBondsOnline*.

Figure 4: Government Maturity Profile
(individual maturities as % of total)



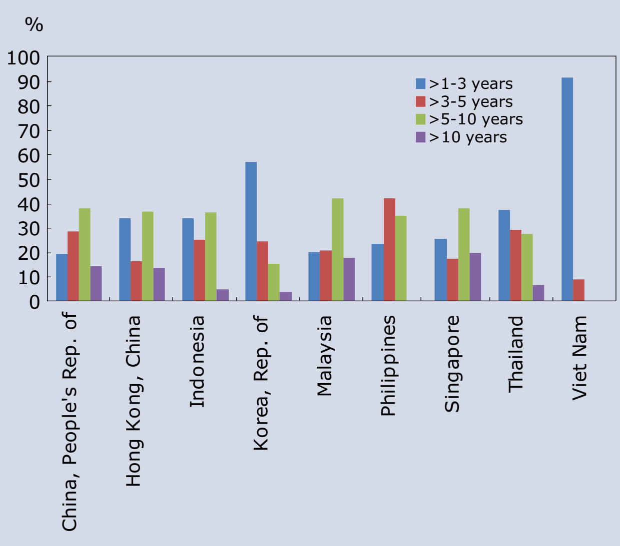
Source: *AsianBondsOnline*.

The maturity profiles of emerging East Asia's individual corporate sectors generally stand in sharp contrast to their respective government bond sectors, reflecting their different funding requirements **(Figure 5)**. The corporate bond markets of the Republic of Korea and Viet Nam have issued proportionately even more short-term debt, while the Hong Kong, China corporate sector's short-term debt is only 34% of the total. The short-term portion of Thai corporate debt was about 37% of the total.

The corporate bond markets of Malaysia, Philippines, Singapore, and Thailand carry proportionately less short-term debt than their respective government bond markets do. This may reflect the fact that many of the companies in these countries are involved in the property development, infrastructure, and energy sectors, and therefore need longer-term financing.

The maturity profiles of the corporate sector also tend to be bunched either in 3–5 or 5–10 year tenors. There is little exposure to tenors beyond 10 years in the corporate sector. Extending the tenor of corporate financing will be an objective of many firms in the emerging East Asian corporate sector in coming years. In Singapore, the recent 40-year bond from Temasek provides a useful benchmark for extending corporate bond tenors.

Figure 5: Corporate Maturity Profile
(individual maturities as % of total)



Source: *AsianBondsOnline*.

Bond Turnover Ratios

The government bond turnover ratios for Hong Kong, China; the Republic of Korea; Thailand; and the Philippines increased in 3Q10.

In keeping with the experience from most quarters over the last several years, turnover ratios for government bonds in 3Q10 were much higher than for corporate bonds in all of the region's markets, except the PRC. However, turnover among government bonds varied greatly. Quarterly government bond turnover ratios in 3Q10 rose in six of the eight markets surveyed—the PRC; Hong Kong, China; Republic of Korea; Philippines; Singapore; and Thailand—but fell in the other two markets—Indonesia and Malaysia **(Figure 6a)**. As has been the case in the past, the turnover ratio for government bonds in Hong Kong, China was higher than any other market by a factor of 10 or more. Most of Hong Kong, China's government sector debt consists of Exchange Fund Bills and Notes (EFBNs) issued by the HKMA for monetary policy purposes. One reason that the turnover ratio of EFBNs is consistently so high is that these instruments are important for bank liquidity management since they can be used as collateral when borrowing from the HKMA through repurchase agreements. Another factor contributing to the high liquidity of EFBNs is that they can be used as margin collateral for stock options and futures trading. Finally, recent changes in Hong Kong, China's market, especially the PRC's efforts to expand the role of the yuan in currency trading and bond purchases, seem to be benefiting liquidity in the Hong Kong, China market.

Past patterns also reasserted themselves once again in the region's turnover ratios for corporate bonds. The quarterly turnover ratio for the PRC's corporate bond market was larger than most other markets by a factor of four or more **(Figure 6b)**.

In addition, the PRC's corporate bond turnover ratio rose slightly in 3Q10, as did turnover ratios in most other markets. Only in Malaysia did the quarterly turnover ratio for corporate bonds decline in 3Q10.

Figure 6a: Government Bond Turnover Ratios

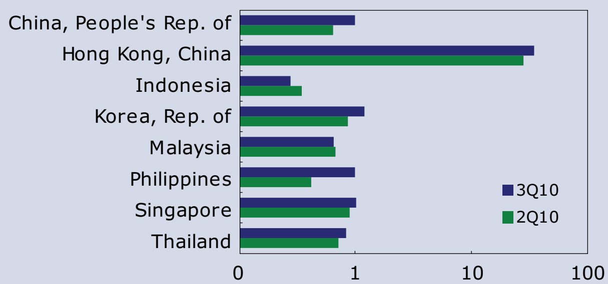
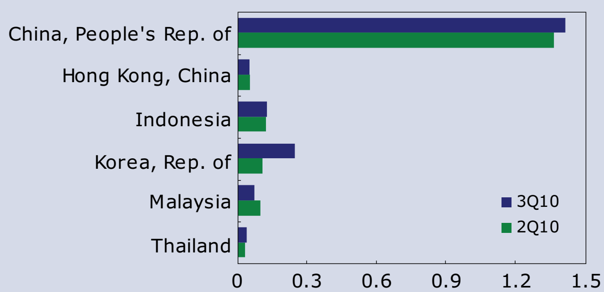


Figure 6b: Corporate Bond Turnover Ratios



Notes:
1. Government and corporate bond turnover ratios are calculated as local currency (LCY) trading volume (sales amount only) divided by average LCY value of outstanding bonds during each 3-month period.
2. Figure 6a is based on a logarithmic scale.
Source: People's Republic of China (*ChinaBond*); Hong Kong, China (Hong Kong Monetary Authority); Indonesia (Indonesia Stock Exchange); Republic of Korea (Bloomberg LP and *KoreaBondWeb*); Malaysia (Bank Negara Malaysia); Philippines (Bureau of the Treasury); Singapore (Monetary Authority of Singapore, Singapore Government Securities, and Bloomberg LP); and Thailand (Bank of Thailand and Thai Bond Market Association).

Government Bond Yield Curves

Yield curves for LCY government bonds have steepened recently on concerns of rising inflationary pressure and the impact of the US Federal Reserve's new round of quantitative easing.

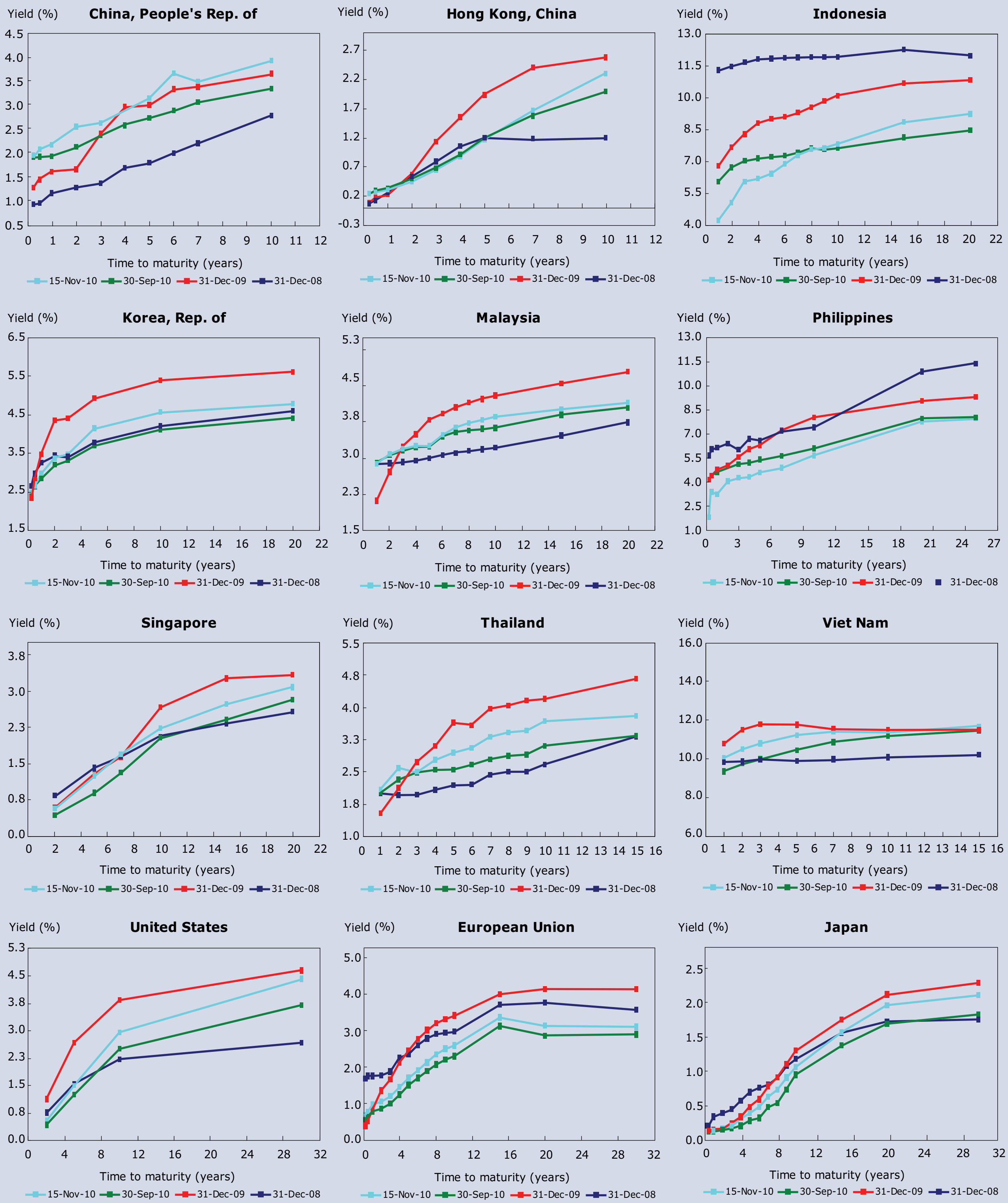
Between end-December 2009 and the end of 3Q10, yield curves for LCY government bonds flattened and in some cases shifted downward. Strengthened demand in 2Q10 for Asian government bonds remained in 3Q10. The bullish flattening of the LCY government yield curves could be attributed to the following factors: (i) attractive yields and strong growth amid an uncertain global economic outlook, (ii) central banks' reserve diversification, (iii) anticipation of potential currency appreciations, and (iv) better hedging and risk management products.

Yield compression differed somewhat from market to market. Government bond yield curves for the PRC, Malaysia, Philippines, Singapore, and Thailand flattened from the belly to the long-end of the curve: (i) in the Philippines, yields beyond 5 years fell more than shorter-term tenors as the May presidential election reduced political uncertainty; (ii) the Indonesian yield curve flattened from the short-end through the very long-end of the curve; (iii) yield curves for Hong Kong, China and the Republic of Korea shifted downward except at very short-end; and (iv) the Vietnamese yield curve steepened, most dramatically for maturities under 5 years.

Since the end of 3Q10, these trends have reversed somewhat **(Figure 7)**, as investors balanced their overall positive outlook against concerns over rising inflationary pressure in some markets; recent policy hikes in the PRC, the Republic of Korea, and Viet Nam; and concerns over the market impact of capital inflows and US quantitative easing:

(i) Government bond yield curves for the PRC; Hong Kong, China; Indonesia; and Thailand have steepened relative to end-3Q10 positions. However, this happened with a modest drop in yields since the end of 3Q10 at the short-end of the Hong Kong, China curve, and a sharp decline in yields at the short end of the Indonesian curve. (ii) Government bond yield curves for the Republic of Korea and Malaysia have also steepened through 10-year maturities and—in Singapore—through 15 years. (iii) Viet Nam's curve flattened relative to its end—3Q10 position, shifting sharply upward at its short-end. (iv) The Philippine yield curve was the exception—it has shifted sharply downward at its short-end since the end of 3Q10, resulting in a steepening of the overall curve, below 3Q10

Figure 7: Benchmark Yield Curves—LCY Bonds



LCY = local currency.
Source: Based on data from Bloomberg LP.

levels. As of 15 November, several of the region's curves had risen less for maturities over 10 years, suggesting that longer-term investors have retained their appetite for duration.

The underlying trend of declining long-term yields between the end of 2009 and the end of 3Q10—at a time when short-term yields were largely unchanged—resulted in a decline of the yield spread between 2- and 10-year government bond yields in all emerging East Asian bond markets except for Viet Nam **(Figure 8)**. However, the sudden rise in 10-year yields between the end of September and 15 November reversed this trend, with yield spreads rising in all markets except Viet Nam.

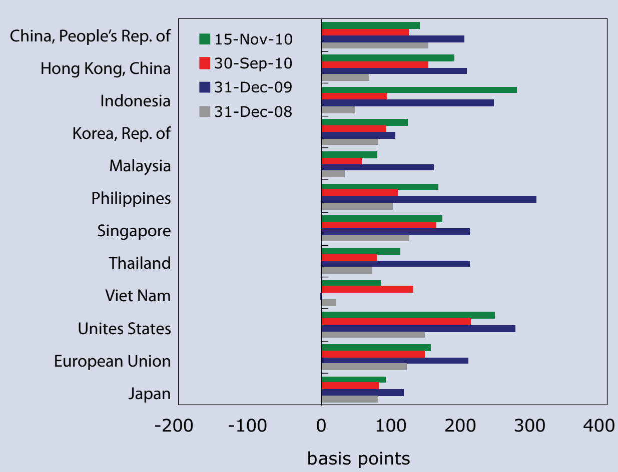
The near-term outlook for government bond yields is mixed. Bond yield curves might steepen further if inflationary expectations gain and East Asian central banks tighten further. On the other hand, ample global liquidity and sustained foreign capital inflows into LCY bond markets will continue to exert downward pressure on yield curves.

Some central banks are already normalizing rates **(Figure 9)** with others joining lately to keep a lid on rising inflationary pressures.

BNM raised its policy rate by 25 basis points in February, May, and July for a total increase of 75 basis points in 2010. Central banks in the Republic of Korea and Thailand raised their respective policy rates by 25 basis points in July, followed by the BOT in August and Bank of Korea in late November. In mid-October, the PBOC increased both its 1-year lending rate and 1-year deposit rate by 25 basis points each to 5.56% and 2.50%, respectively. The PBOC also raised its bank reserve ratio requirements twice in November. Finally, the State Bank of Vietnam raised its policy rate by 100 basis points to 9.0% in early November.

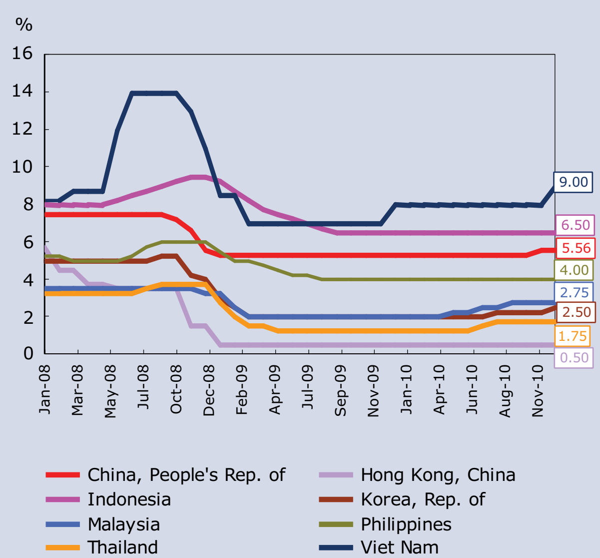
Current inflation trends in the region vary. **(Figure 10)**. Inflation has risen recently in the PRC, the Republic of Korea, and Viet Nam, but fallen for several months in the Philippines, Thailand, and Indonesia.

Figure 8: Yield Spread between 2- and 10-Year Government Bonds



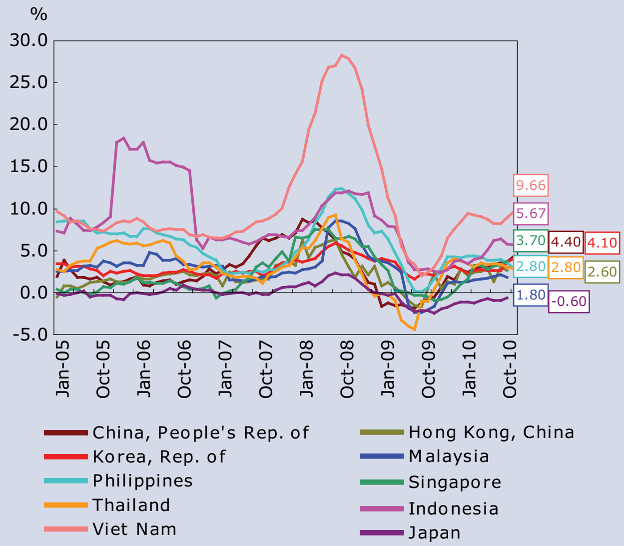
Source: Based on data from Bloomberg LP.

Figure 9: Policy Rates (November 2010)



Source: Bloomberg LP except for Viet Nam (State Bank of Viet Nam).

Figure 10: Headline Inflation Rates (October 2010)



Note: Inflation for Hong Kong; China; Malaysia; Singapore and Japan are September figures.
Source: Bloomberg LP.

Corporate Bond Credit Spreads

High-grade corporate bond credit spreads have fallen in most markets since the end of December 2009, while credit spreads for lower-rated corporates have generally fallen only at the short-end of their respective curves and, in some cases, have risen.

Credit spreads on high-grade corporate bonds—rated AAA—fell between end-December 2009 and mid-November 2010 along the entire length of the corporate bond credit curves of the PRC and the Republic of Korea **(Figure 11a)**. The Malaysian curve steepened, with credit spreads rising above end-December 2009 levels for all maturities, except at the very short-end of the curve.

The behavior of the Thai yield curve was more complex. Thai credit spreads fell along the entire length of the curve compared with end-December 2009 levels, but Thai credit spreads fell much more for maturities of 1–3 years than for maturities of less than 1 year or more than 3.5 years.

Trends for lower-rated corporate bonds **(Figure 11b)** were unique for each of the four markets in which data were available:

(i) In the PRC, credit spreads with tenors of 15 years or more fell slightly, while credit spreads under 15 years fell significantly, especially for maturities under 5 years.

(ii) In the Republic of Korea, credit spreads fell modestly between end-December 2009 and mid-November 2010. But instead of signaling a steepening of the curve, credit spreads simply fell below end-December 2009 levels along the entire length of the curve.

(iii) In Malaysia, the credit curve steepened along its entire length relative to its position at end-December 2009.

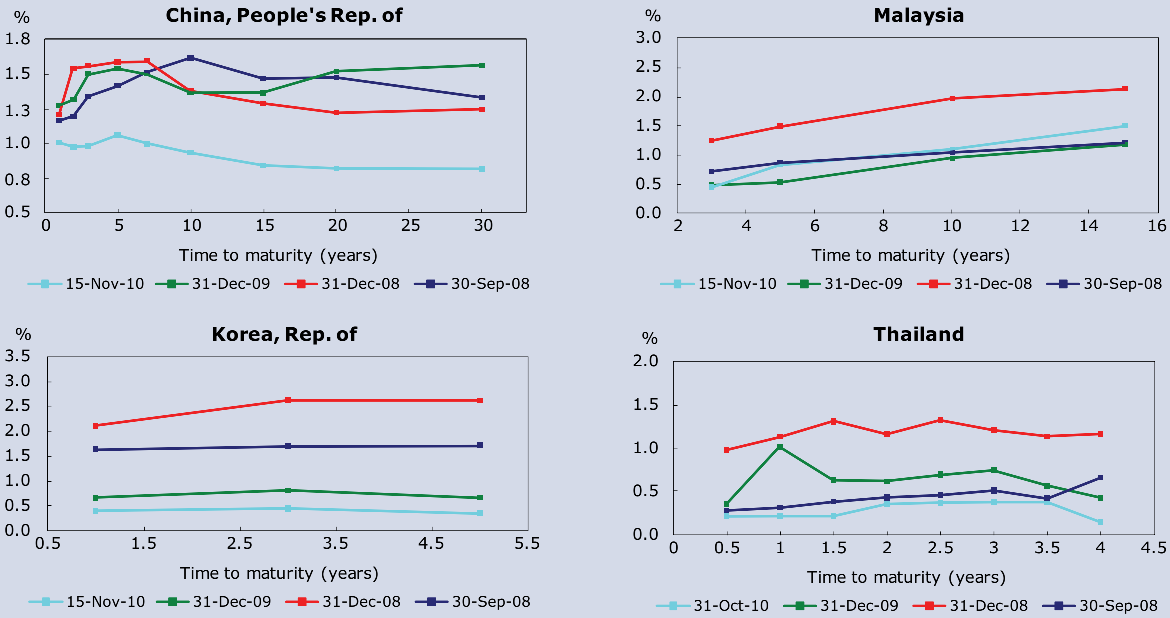
(iv) The trend for the lower-rated Thai credit curve was similar to that of the higher-rated curve, except that spreads on the lower-rated curve were roughly zero and therefore even lower than the 0.2%–0.3% spreads on the higher-rated curve. The short- and long-end of the lower-rated Thai credit curve also approached levels similar to those of end-September 2008, except for the very end of the curve, where the credit spreads rose above their end-December 2008 levels.

G3 Currency Issuance

G3 currency issuance in emerging East Asia reached USD77.8 billion in mid-November, which was significantly above the full-year 2009 level of USD63.2 billion.

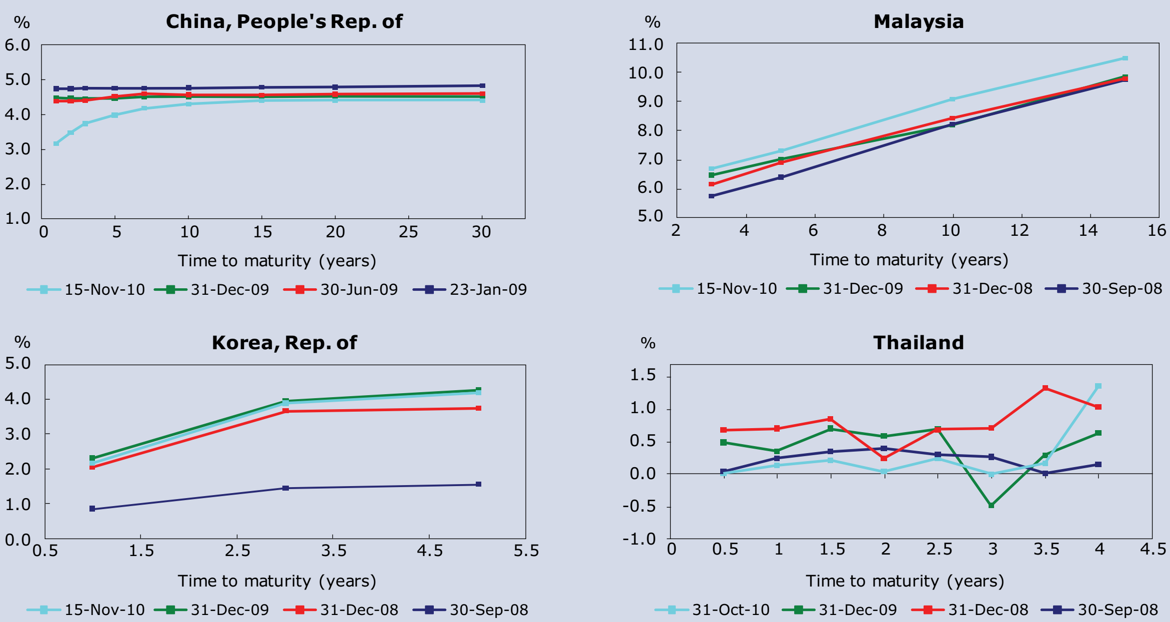
The new issuance of bonds denominated in G3 currencies in 2010 reached USD77.8 billion in mid-November. New issuance in G3 currencies was USD31.8 billion in the first half of 2010, with an additional USD45.9 billion issued between 1 July and 15 November **(Table 5)**. This upsurge in G3 currency issuance reflected the return of investor appetite for the bonds of major Asian governments, corporations, and financial

Figure 11a: Credit Spreads—LCY Corporates Rated AAA vs. Government Bonds



Note:
1. Credit spreads obtained by subtracting government yields from corporate indicative yields.
Source: People's Republic of China (*ChinaBond*); Republic of Korea (*KoreaBondWeb*); Malaysia (Bank Negara Malaysia); and Thailand (ThaiBMA).

Figure 11b: Credit Spreads—Lower Rated LCY Corporates vs. AAA



LCY = local currency.
Notes:
1. For the People's Republic of China, credit spreads are obtained by subtracting corporate indicative yields rated as AAA from corporate indicative yields rated as BBB.
2. For Malaysia, credit spreads are obtained by subtracting corporate indicative yields rated as AAA from corporate indicative yields rated as BBB.
3. For the Republic of Korea, credit spreads are obtained by subtracting corporate indicative yields rated as AAA from corporate indicative yields rated as BBB+.
4. For Thailand, credit spreads are obtained by subtracting corporate indicative yields rated as AAA from corporate indicative yields rated as A.
Source: People's Republic of China (*ChinaBond*); Republic of Korea (*KoreaBondWeb*); Malaysia (Bank Negara Malaysia); and Thailand (ThaiBMA).

Table 5: G3 Currency Bond Issuance (1H10 and 1 July—15 November 2010)

1H10		
Issuer	**USD million**	**Issue Date**
China, People's Rep. of	**4,770**	
Evergrande 13% 2015	1,350	27-Jan-10
Agile Property 8.875% 2017	650	28-Apr-10
MCE Finance 10.25% 2017	600	17-May-10
Country Garden 11.25% 2017	550	22-Apr-10
Citic Bank 6.875% 2020	500	24-Jun-10
Kaisa Group 13.5% 2015	350	28-Apr-10
Others	770	
Hong Kong, China	**5,405**	
Bank of China (Hong Kong) 5.55% 2020	1,600	11-Feb-10
Bank of China (Hong Kong) 5.55% 2020	900	19-Apr-10
Li & Fung 5.25% 2020	750	13-May-10
Fita International 7.0% 2020	750	10-Feb-10
CLP Power 4.75% 2020	500	19-Mar-10
Noble Group 6.75% 2020	400	9-Feb-10
Others	505	
Indonesia	**4,004**	
Indonesia Sovereign 5.875% 2020	2,000	19-Jan-10
Star Energy 11.5% 2015	350	12-Feb-10
Listrindo Capital 9.25% 2015	300	29-Jan-10
Others	1,354	
Korea, Rep. of	**10,833**	
Export-Import Bank of Korea 5.125% 2020	1,250	29-Jun-10
Export-Import Bank of Korea 4.125% 2015	1,000	9-Mar-10
Korea Development Bank 4.375% 2015	750	10-Feb-10
Shinhan Bank 4.375% 2015	700	15-Mar-10
Hana Bank 4.5% 2015	500	30-Apr-10
Woori Bank 4.5% 2015	500	7-Apr-10
Hynix Semiconductor 2.65% 2015	500	14-May-10
Hyundai Motors 4.5% 2015	500	15-Apr-10
Others	5,133	
Malaysia	**1,950**	
1Malaysia Sukuk 3.928% 2015	1,250	4-Jun-10
Others	700	
Philippines	**2,829**	
Philippines Sovereign (Samurai) 2.32% 2020	1,070	2-Mar-10
Philippines Sovereign 6.5% 2020	650	13-Jan-10
International Container Terminal 7.375% 2020	450	17-Mar-10
Others	658	
Singapore	**845**	
CMT MTN 4.321% 2015	500	8-Apr-10
Others	345	
Thailand	**200**	
Export-Import Bank 0.9% 2015	200	14-Jan-10
Viet Nam	**1,000**	
Viet Nam Sovereign 6.75% 2020	1,000	29-Jan-10
Emerging East Asia Grand Total	**31,835**	
Memo Items:		
India	**3,579**	
Vedanta Resources 4.0% 2017	883	30-Mar-10
Bank of India (London) 4.75% 2015	500	31-Mar-10
IndianOil 4.75% 2015	500	22-Jan-10
Others	1,696	
Sri Lanka	**378**	

1 July–15 November 2010		
Issuer	**USD million**	**Issue Date**
China, People's Rep. of	**5,900**	
China Overseas Finance 5.5% 2020	1,000	10-Nov-10
Sino-Ocean Land Capital 8.0% Perpetual	900	27-Jul-10
Franshion Capital 6.8% Perpetual	600	12-Oct-10
China Resources Power 3.75% 2015	500	3-Aug-10
Shimao Property 9.65% 2017	500	3-Aug-10
Country Garden 10.5% 2015	400	11-Aug-10
Others	2,000	
Hong Kong, China	**11,327**	
Hutch Whampoa 6.0% Perpetual	2,000	28-Oct-10
Sinochem 4.5% 2020	1,500	12-Nov-10
PHBS 6.625% Perpetual	1,000	29-Sep-10
Sino-Forest 6.25% 2017	600	21-Oct-10
Bank of East Asia 6.125% 2020	600	16-Jul-10
Hong Kong Land Finance 4.5% 2025	600	7-Oct-10
Others	5,027	
Indonesia	**1,825**	
Indonesia Sovereign (Samurai) 1.6% 2020	725	12-Nov-10
Indosat 7.375% 2020	650	29-Jul-10
Berau Capital Resources 12.5% 2015	450	8-Jul-10
Korea, Rep. of	**15,630**	
Export-Import Bank of Korea 4.0% 2021	1,000	20-Oct-10
Polyvision 0.0% 2013	990	1-Oct-10
Korea Development Bank 3.25% 2016	900	9-Sep-10
Korea Finance Corp. 3.25% 2016	750	20-Sep-10
Posco 4.25% 2020	700	28-Oct-10
Korea Electric Power 3.0% 2015	700	5-Oct-10
Korea National Oil Corp. 2.875% 2015	700	9-Nov-10
Woori Bank 4.75% 2016	600	20-Jul-10
Export-Import Bank of Korea 1.343% 2012	500	13-Sep-10
Others	8,790	
Malaysia	**0**	
Philippines	**5,251**	
Philippines Sovereign 4.0% 2021	2,242	6-Oct-10
Philippines Sovereign 6.375% 2034	950	6-Oct-10
Alliance Global 6.5% 2017	500	18-Aug-10
Others	1,559	
Singapore	**3,936**	
DBS Bank 2.375% 2015	1,000	14-Sep-10
Bumi Investment 10.75% 2017	700	6-Oct-10
STATS ChipPAC 7.5% 2015	600	12-Aug-10
Others	1,636	
Thailand	**2,050**	
Bangkok Bank 4.8% 2020	800	18-Oct-10
Others	1,250	
Viet Nam	**0**	
Emerging East Asia Grand Total	**45,919**	
Memo Items:		
India	**4,610**	
State Bank of India (London) 4.5% 2015	1,000	27-Jul-10
Reliance Holdings (US) 4.5% 2020	500	19-Oct-10
ICICI Bank 5.0% 2016	500	15-Jul-10
Others	2,610	
Sri Lanka	**1,195**	

Sources: Compilation from newspaper and wire reports.

institutions; a renewed search for yield; and low US interest rates.

The low level of US interest rates has allowed many banks and corporations in the Republic of Korea to issue bonds at lower coupons. As a result, the Republic of Korea accounted for the largest amount of new G3 currency issuance between the beginning of the year and mid-November at USD26.5 billion. The largest group of issuers in the Republic of Korea was the banks. In the first half of the year, the Export–Import Bank of Korea issued two bonds for a total of USD2.25 billion, while the Korea Development Bank (KDB) and Shinhan Bank issued bonds of USD750 million and USD700 million, respectively, with a further USD900 million issued by KDB in September. In September, Korea Finance Corp. issued USD750 million in bonds. The Export–Import Bank of Korea issued an additional USD500 million of bonds in September, and USD1.0 billion in October.

The next largest issuers of G3 currency bonds through mid-November were the PRC and Hong Kong, China. The PRC's total issuance amounted to USD10.7 billion and included a number of prominent real estate developers. Issuance out of Hong Kong, China amounted to USD16.7 billion, including two issues from Bank of China (Hong Kong) totaling USD2.5 billion. And finally, the Philippine government issued two sovereign bonds in October (USD950 million and USD2.2 billion) under its dollar bond exchange program.

Bond Market Returns

Returns on LCY bonds for most markets have been buoyant in 2010, with Indonesia, the Philippines, Thailand, and Malaysia posting the largest gains.

The Asian Bond Fund (ABF) Pan-Asian Bond Index has gained 11.2% to date in 2010, compared with 5.0% for all of 2009 **(Table 6)**. The Indonesian bond market was the best performer, gaining 26.7%, followed by the Philippines (20.4%), Thailand (18.1%), and Malaysia (14.4%). The worst performing bond market in the ABF index was that of Hong Kong, China (3.7%), followed by the PRC (4.9%).

Table 6: iBoxx Asia Bond Fund Index Family Returns

Market	Modified Duration (years)	2009 Returns (%)		3Q10 Returns (%)		2010 YTD Returns (%)	
		LCY Total Return Index	USD Unhedged Total Return Index	LCY Total Return Index	USD Unhedged Total Return Index	LCY Total Return Index	USD Unhedged Total Return Index
China, People's Republic of	5.83	(0.64)	(0.69)	4.03	6.06	2.66	4.92
Hong Kong, China	3.89	(0.76)	(0.82)	3.74	3.67	3.71	3.69
Indonesia	5.77	20.22	35.61	19.36	24.62	21.46	26.66
Korea, Rep. of	3.74	1.94	9.73	8.04	10.20	7.88	11.37
Malaysia	4.82	0.48	1.64	5.11	15.49	4.84	14.41
Philippines	4.38	9.00	11.88	10.92	16.04	13.33	20.43
Singapore	5.80	0.48	3.06	5.18	11.30	5.15	12.66
Thailand	4.96	(3.47)	0.73	7.73	16.91	7.45	18.07
Pan-Asian Index	4.88	—	5.00	—	10.66	—	11.15
HSBC ALBI	8.20	—	6.13	—	11.22	—	12.07
US Govt 1-10 years	3.93	—	(1.38)	—	7.02	—	7.35

— = not applicable, ALBI = Asian Local Bond Index, LCY = local currency, US = United States, YTD = year to date.
Notes:
1. The Asian Bond Fund (ABF) indices contain only government debt and government-guaranteed debt obligations.
2. Market bond indices are from iBoxx Index Family. 2010 returns are year-to-date as of 31 October 2010.
3. Annual return is computed for each year using natural logarithm of end-of-year index value/beginning of year index value.
4. Duration is as of 31 October 2010.
Source: *AsianBondsOnline* and Bloomberg LP.

These overall high returns, however, have been matched—broadly speaking—by the returns in Asia's equity markets. The Morgan Stanley Capital International (MSCI) Far East ex-Japan Index has generated a return of 11.9% to date **(Table 7)**. The largest returns in the MSCI index have come from Thailand, the Philippines, Indonesia, and Malaysia. These four markets were also the strongest performers in the ABF Index. Year-to-date returns in the equity markets of Hong Kong, China; Singapore; and the Republic of Korea have also been substantial, but still below the top four markets listed above. While the PRC's returns in the MSCI index are positive, growth in 2010 has been in the single digits.

The appreciation of the region's currencies in 2010 has helped to push up returns on LCY bonds **(Table 8)**. As of mid-November, the Thai baht had gained 10.7% y-o-y against the US dollar, the Philippine peso 6.4%, the Malaysian ringgit 7.2%, and the Singaporean dollar 6.3%. The only currencies to decline against the US dollar have been the Vietnamese dong and the Hong Kong dollar, while the PRC yuan has only risen by 2.7% y-o-y.

Table 8: Appreciation (Depreciation) of Emerging East Asian Currencies (%)

Currency	2008	2009	3Q10		As of 15-Nov 2010	
	y-o-y	y-o-y	y-o-y	q-o-q	y-o-y	q-o-q
CNY	6.7	(0.02)	2.0	1.4	2.7	0.7
HKD	0.6	(0.04)	(0.1)	0.3	(0.03)	0.1
IDR	(18.7)	17.8	8.1	1.6	4.2	(0.8)
KRW	(29.7)	8.4	3.5	7.3	1.8	0.2
MYR	(4.5)	0.6	11.7	4.5	7.2	(1.8)
PHP	(13.9)	2.7	8.0	5.5	6.4	0.3
SGD	0.1	2.2	6.7	5.9	6.3	1.2
THB	(3.1)	3.9	9.8	6.7	10.7	1.4
VND	(8.8)	(5.5)	(8.8)	(2.1)	(8.7)	(0.1)
JPY	20.8	(2.6)	7.2	6.0	7.9	0.8

q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Appreciation (depreciation) is equal to -LN (end-of-period rate/start-of-period rate).
2. For 15 November 2010 q-o-q figures, appreciation (depreciation) is equal to -LN (15 November 2010 rate/end-3Q10 rate).
Source: Bloomberg LP.

Table 7: MSCI Index Returns

Market	2008 Returns (%)		2009 Returns (%)		2010 YTD Returns (%)	
	LCY terms	USD terms	LCY terms	USD terms	LCY terms	USD terms
China, People's Rep. of	(52.23)	(51.94)	58.89	58.80	5.57	5.59
Hong Kong, China	(53.16)	(52.88)	55.28	55.20	17.10	17.12
Indonesia	(50.76)	(57.57)	90.27	120.75	29.56	36.19
Korea, Republic of	(40.62)	(55.87)	56.63	69.42	8.96	12.76
Malaysia	(40.77)	(43.39)	46.25	47.78	18.35	30.23
Philippines	(46.77)	(53.79)	55.79	60.24	28.10	37.66
Singapore	(49.50)	(49.55)	63.02	67.29	6.13	15.12
Thailand	(48.72)	(50.34)	63.00	70.04	30.53	45.16
Far East ex-Japan Index	(48.14)	(51.96)	60.32	65.01	8.58	11.91
MSCI USA Index	—	(38.58)	—	24.20	—	6.38

— = not applicable, LCY= local currency, MSCI = Morgan Stanley Capital International, YTD = year to date.
Notes:
1. Market indices are from MSCI country indexes. 2010 returns are year-to-date as of 31 October 2010.
2. Far East ex-Japan includes People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Taipei, China; and Thailand.
Source: *AsianBondsOnline* and Bloomberg LP.

Policy and Regulatory Developments

People's Republic of China (PRC)

Clearstream and Euroclear Enable Settlement of CNY-Denominated Securities

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

PRC Revises Rules on Panda Bonds

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

Banks Barred from Providing Mortgages to Third Home Buyers

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

PRC Allows Foreign Institutions to Open Yuan Accounts

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

Chinese Insurers Barred from Property Speculation

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

PBOC Hikes Reserve Requirement Ratios

The PRC hiked its reserve requirement ratio by 50 basis points for all banks and another 50 basis points for a select few bank in response to accelerating inflation. The PBOC initially hiked by 50 basis points the reserve requirements of the four big state banks and one other bank—China Construction Bank, Bank of China, Agricultural Bank of China, and Bank of Communications—

effective 15 November. The PRC subsequently announced a 50 basis points hike for all lenders, effective 16 November. On 19 November, the PRC again hiked the reserve requirement ratio by 50 basis points. This effectively brings the reserve requirement rate of the four big state banks to 18.5%, and to 18.0% for other large financial institutions, and 16.0% for small and medium-sized financial institutions.

Hong Kong, China

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

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

Indonesia

BI Announces New Regulations on Reserve Requirements and Bank Lending

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

BI Plans to Offer New Term Deposits

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

Republic of Korea

The Republic of Korea to Introduce Short-Term KTBs

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

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

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

Malaysia

BNM Further Liberalizes FX Rules

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

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

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

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

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

Philippines

Government and Petron Issue Peso Global Bonds

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

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

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

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

Singapore

Singapore Exchange Launches Initiatives to Boost Bond Listing and Trading

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

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

SGX Launches ADRs

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

Thailand

Finance Ministry Relaxes Capital Outflow Controls

In September, the Finance Ministry of Thailand announced regulatory changes to promote foreign investment and capital outflows in an effort to slow the appreciation of the baht, which has gained about 8% against the US dollar year-to-date due to capital inflows and a steady trade surplus. The five new regulatory measures include

(i) allowing Thai firms to invest and lend without limit to affiliate companies abroad;

(ii) allowing Thai firms to lend up to USD50 million per year to non-affiliated companies abroad;

(iii) increasing the foreign property investment cap from USD5 million to USD10 million;

(iv) increasing the maximum foreign currency deposits held by Thai individuals and companies from USD100,000 and USD300,000, respectively, to USD500,000 for both; and

(v) increasing mandatory repatriation of export earnings from USD20,000 to USD50,000.

Thai Cabinet Approves a 15% Tax on Bonds

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

BOT Relaxes Regulations on Foreign Exchange Transactions

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

Viet Nam

Fees on Corporate Bonds to Be Cut by 50%

In August, the prime minister's working group proposed that the Ministry of Finance reduce corporate bond issuance acceptance fees by 50% in an effort to harmonize them with fees on other licenses such as investment registration and construction. The proposed changes would adjust fees to the following levels:

(i) VND5.0 million for bond issues of less than VND50 billion,

(ii) VND10.0 million for issues of less than VND150 billion,

(iii) VND17.5 million for issues of less than VND250 billion, and

(iv) VND25.0 million for issues larger than VND250 billion.

Viet Nam's Central Bank to Revise Bank Legal Capital Roadmap

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

AsianBondsOnline Annual Bond Market Liquidity Survey

Recent Trends in Quarterly Turnover Ratios of LCY Government Bonds in Emerging East Asia

The liquidity of local currency (LCY) government bonds—as measured by quarterly turnover ratios[4]—improved in most emerging East Asian markets during 3Q10 **(Figure 12)**.

- In the People's Republic of China (PRC), quarterly turnover ratios for government, central bank, and policy bank bonds all rose in 3Q10. Central bank bonds had the highest turnover ratio at 1.53, followed by policy bank bonds at 1.31 and treasury bonds at 0.37.

- In the Republic of Korea, central government and central bank bonds both registered higher turnover ratios in 3Q10 compared with the previous quarter. The turnover ratio for central government bonds rose to 1.16 in 3Q10 from 1.10 in 2Q10, while the turnover ratio for central bank bonds increased to 1.51 from 0.54.

- The liquidity of Philippine government bonds increased in 3Q10, with the turnover ratio reaching 0.99 from 0.41 in the previous quarter.

- In Singapore, the turnover ratio for government bonds rose to 1.01 in 3Q10 from 0.89 in the previous quarter, on the back of quarterly rises for both treasury bills and treasury bonds.

In the region's other government bond markets, quarterly movements in turnover ratios have been mixed for various types of bonds.

- In Malaysia, the turnover ratio for central government bonds remained unchanged in 3Q10 from the previous quarter at 0.37, but fell for central bank bills to 1.89 from 2.65.

[4] The quarterly turnover ratio is defined as the quarterly trading volume for a particular type of bond divided by the average stock of bonds outstanding at the end of the previous and current quarters.

- In Thailand, the turnover ratio for Bank of Thailand (BOT) bonds climbed to 1.68 in 3Q10, and the turnover ratio for treasury bonds rose slightly to 0.23. On the other hand, the ratios for treasury bills and state-owned enterprises bonds remained at the very low levels of 1.05 and 0.02, respectively.

- In Indonesia, the turnover ratio for government bonds dropped to 0.27 in 3Q10 from 0.34 in 2Q10, partly reflecting a 24.8% quarter-on-quarter (q-o-q) decline in new issuance in 3Q10.

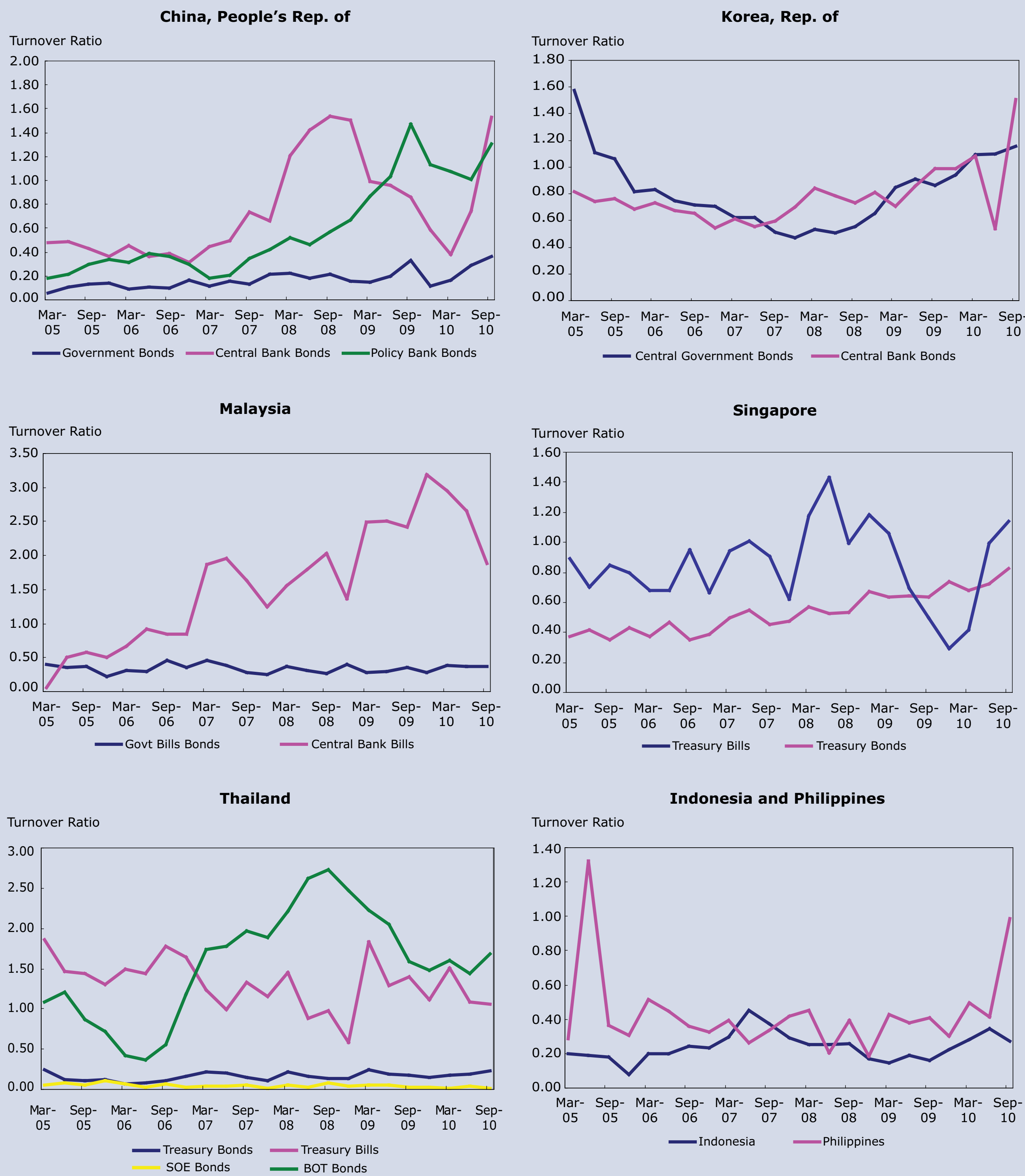
Figure 12 puts these developments in a multi-year perspective, demonstrating that liquidity ratios in most markets have been on an upward trend since at least the latter part of 2008. This reflects the combined impact of accommodative monetary policies and expansionary fiscal policies, as well as continued inflows of foreign capital—and liquidity—into Asia over the last several years. Additionally, it reflects the specific efforts of governments in Singapore, the Republic of Korea, and the Philippines to consolidate their respective bond issuances through exchange offers and by re-opening existing bond issues to further increase the size of these issues and improve their liquidity.

Amid this environment of rising liquidity in LCY bond markets, *AsianBondsOnline* conducted its annual Bond Market Liquidity Survey.

AsianBondsOnline Annual Bond Market Liquidity Survey

The 2010 survey polled 112 respondents, which was up slightly from 106 participants in 2009 and considerably higher than the 40–50 participants polled in previous years, and included trading desk staff and managers, portfolio managers, and bond market analysts and strategists, as well as pricing agencies. The number of domestic and foreign firms and institutions surveyed was exactly equal:

Figure 12: Trends in Quarterly Government Bond Turnover Ratios



Source: *AsianBondsOnline*.

56 employees of foreign firms and institutions, and 56 employees of domestic firms and institutions. Respondents were asked to give quantitative and qualitative responses on measures of liquidity in emerging East Asian LCY bond markets, as well as their views on the appropriate policies needed to improve liquidity and efficiency.

Market participants were asked to provide representative bid–ask spreads and accepted bond transaction sizes for both "on-the-run" and "off-the-run" government bonds. In the case of corporate bonds, survey participants were asked to provide (i) bid–ask spreads at the time when a new bond is issued, and (ii) typical market-accepted transaction sizes.

The survey analysis includes a table for benchmark government bonds for each market—usually the most representative treasury bond—which allows for comparisons among the individual markets of emerging East Asia. For the larger markets that issue a variety of both government and corporate bonds, the analysis compares the different types of bonds in each market in terms of the bid–ask spread and average transaction size. Data for turnover ratios show that the ratios for various types of government bonds within a single market can sometimes vary more than ratios between markets. Thus, intra-market variations in liquidity between different bond types are sometimes as important as variations between different markets.

Table 9 summarizes the indicators for the benchmark bond in each market, which, as mentioned above, is usually a treasury or equivalent type of bond. Market participants were asked to provide data representative of bid–ask spreads and market-accepted transaction sizes for both on-the-run and off-the-run government benchmark bonds for the end-August to mid-October period in which the survey was conducted.

Bid–Ask Spreads. The bid–ask spread is perhaps the most commonly used measure of market liquidity as it directly measures the cost of executing a trade. However, bid–ask spreads are only valid for market-accepted transaction sizes and for a limited period of time.

The average on-the-run bid–ask spread for the government benchmark bond in each of the nine markets surveyed, as reported by a total of 102 market participants, was 7.2 basis points, which was tighter than 8.6 in 2009. The standard

Table 9: Government Bond Market Quantitative Indicators

		PRC	HK	ID	KR	MY	PH	SG	TH	VN	Regional
Typical Bid-Ask Spread "On-the-Run" (bps)	Average	2.2	5.1	31.7	1.1	2.6	3.1	3.0	3.1	13.2	7.2
	Count	12	5	15	20	11	11	10	14	4	102
	SD	0.7	1.5	16.5	0.5	1.1	2.3	0.7	1.4	9.3	9.8
Typical Bid-Ask Spread "Off-the-Run" (bps)	Average	5.1	5.8	38.2	1.7	6.2	12.4	3.5	7.7	25.7	11.8
	Count	5	3	15	20	8	10	9	12	4	86
	SD	1.7	1.4	22.1	1.4	2.8	8.3	0.5	4.4	20.5	12.2
Accepted LCY bond Transaction Size "On-the-Run" (USD million)	Average	16.9	15.7	1.9	8.6	2.0	4.5	8.6	1.9	2.3	6.9
	Count	12	5	15	20	10	12	9	14	5	102
	SD	15.8	10.1	1.4	1.0	0.5	5.1	5.4	1.6	0.7	6.0
Accepted LCY Bond Transaction Size "Off-the-Run" (USD million)	Average	11.0	11.6	1.4	8.5	1.5	1.3	8.9	1.2	2.2	5.3
	Count	3	4	15	20	7	7	8	11	4	79
	SD	4.9	9.7	0.6	1.4	0.2	0.3	5.7	0.9	0.8	4.6

bps = basis points; HK = Hong Kong, China; ID = Indonesia; KR = Republic of Korea; LCY = local currency; MY = Malaysia; PH = Philippines; PRC = People's Republic of China; SD = standard deviation; SG = Singapore; TH = Thailand; VN = Viet Nam.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

deviation was 9.8 in 2010 compared with 10.0 in 2009. The average bid–ask spread tightened for the PRC, Philippine, Vietnamese, and Thai markets. It was largely unchanged in the Republic of Korea and Singapore, and widened somewhat in Hong Kong, China; Indonesia; and Malaysia. The tightening of the Philippine market accelerated after the presidential election in May. The lowest bid–ask spread was 1.1 basis points in the Republic of Korea, followed by 2.2 basis points in the PRC and 2.6 basis points in Malaysia. The tightening of bid–ask spreads in the region as a whole reflected the combined effects on overall market liquidity of economic stimulus programs, accommodative monetary policies and large capital inflows.

Liquidity can also be measured by the difference between bid–ask spreads for on-the-run and off-the-run bonds, given that the more liquid on-the-run benchmark bonds have tighter spreads. The largest differences between on-the-run and off-the-run bid–ask spreads were in the Philippines and Viet Nam. In some markets, such as the PRC, the Republic of Korea, and Singapore, the off-the-run market is very small. In fact, the majority of respondents from the PRC viewed the off-the-run market as the less meaningful of the two.

Average Transaction Size. Transaction size is a useful measure of market depth. It is an ex-post measure of the quantity of bonds that can be traded at the bid or ask price. In this survey, the average transaction size for on-the-run government bonds ranged from a low of USD1.9 million–USD2.0 million (equivalent) in Indonesia, Thailand, and Malaysia, to a high of USD16.9 million in the PRC. In Hong Kong, China, the average transaction size for on-the-run bonds was USD15.7 million, followed by USD8.6 million for both the Republic of Korea and Singapore. Average trading sizes for the Philippines and Viet Nam were lower, with average trading sizes of USD4.5 million and USD2.3 million, respectively.

These figures represent a significant increase from 2009 when the average trading sizes in the lower-bound markets were USD1.1 million in the Philippines, USD1.5 million in Indonesia, and USD1.6 million in Thailand, while the largest average trading size was USD14.3 million in the PRC. Some of these increases reflect capital inflows and a strengthening of local currencies against the United States (US) dollar. But in markets where bid–ask spreads have declined, trading desks have sought to trade in larger volumes to maintain the profitability of their trading activity.

Finally, the average trading size for off-the-run bonds was lower than for on-the-run bonds in most government bond markets in 2010, although not much lower in the more liquid markets.

Characteristics of Individual Government Bond Markets

As mentioned above, the survey also collected data on bid–ask spreads and average transaction sizes for the different types of bonds in the larger markets, as well as information on market structure developments.

People's Republic of China. Market liquidity greatly increased in the PRC over the last year, resulting in a drop in bid–ask spreads to 2–3 basis points, not only for treasury bonds but also for bonds issued by policy banks **(Table 10)**. Policy bank bonds trade on a basis roughly equivalent to treasury bonds, except that the tradable universe of treasury bonds tends to comprise those with maturities of 7–10 years, while the most tradable policy bank bonds tend to have tenors of 5–7 years.

Survey participants reported that bonds and bills issued by the People's Bank of China (PBOC) trade with bid–ask spreads of 0.5–2.0 basis points, depending on maturity. (PRC market participants view the benchmark PBOC bond as a "bill" and therefore see no practical difference between PBOC bonds and bills.) The shortest maturity for a PBOC bill is 3 months and the longest maturity for a PBOC bond is 3 years. PBOC bills and bonds are generally more liquid than policy bank bonds and treasury bills and bonds, with an average bid–ask spread of around 1.5 basis points and an average trading size of CNY285.9 million for PBOC bills and

Table 10: PRC Government Bond Survey Results

	Government Bonds	Policy Bank Bonds	PBOC Bonds	Government Bills	PBOC Bills
Bid–Ask Spread (bps)	2.2	2.8	1.5	2.3	1.5
Average Trading Size (CNY million)	113.3	109.2	290.6	141.7	285.9

bps = basis points, PBOC = People's Bank of China, PRC = People's Republic of China.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

CNY290.6 million for PBOC bonds. This compares with average trading sizes of CNY113.3 million for government bonds, CNY109.2 million for policy bank bonds, and CNY141.7 million for treasury bills. The bid–ask spread for treasury bills is roughly the same as for government bonds.

Since the survey was conducted, bid–ask spreads for government benchmark bonds have risen to levels as high as 3–6 basis points in response to recent policy rate hikes by the PBOC. Market observers, however, expect bid–ask spreads to settle down to about 3 basis points as the market adjusts to recent policy developments.

Trading in off-the-run bonds is very limited in the PRC at the present time. This reflects the issuance of most treasury and policy banks bonds in almost identical sizes of roughly CNY30 billion, as well as the ample liquidity generated by the PBOC's accommodative monetary policy of the last several years.

The most important hedging product in the PRC market is the interest rate swap (IRS) and the most important benchmark for the IRS market is the 7-day repo rate, which comprises about 50%–60% of the IRS market, followed by the 3-month Shanghai Interbank Offered Rate (SHIBOR), which comprises about 30%–40% of the IRS market.

Two interesting developments that may have a significant effect on the PRC's LCY bond market in 2011 are (i) the emergence of the offshore yuan market in Hong Kong, China; and (ii) a recent decision by the National Association of Financial Market Institutional Investors (NAFMII), which is a trade body set up by the PBOC, to launch its much-anticipated credit default swap (CDS) market. Regarding the first development, the Asian Development Bank (ADB) issued a CNY1.2 billion bond at a coupon of 2.8% in October to raise funds for its projects in the PRC and to establish a 10-year benchmark for yuan bond issuers in Hong Kong, China. Meanwhile, NAFMII has structured its CDS market to avoid the pitfalls of CDS markets in Europe and the US, which contributed heavily to the recent financial crisis, and to trade through the Shanghai interbank clearing system.

Republic of Korea. Bid–ask spreads for on-the-run Korean Treasury Bonds (KTBs) were little changed between 2009 and 2010 at 1.1 basis points, although the average trading size rose slightly to USD8.6 million from USD8.0 million last year (Table 9). Typical bid–ask spreads of 1.1 basis points for Bank of Korea (BOK) Monetary Stabilization Bonds (MSBs) were roughly the same as for KTBs, although the average trading size of KRW9.3 billion for MSBs was slightly less than KRW9.8 billion for on-the-run KTBs **(Table 11)**. In the off-the-run segment of the market, however, the typical bid–ask spread of 1.7 basis points for KTBs was modestly larger than 1.3 basis points for MSBs. As in the on-the-run market, the average trading size for off-the-run MSBs of KRW9.2 billion was less than the off-the-run trading size of

Table 11: Republic of Korea Government Bond Survey Results

	Treasury Bonds	MSB	BOK Bills
On-the-Run			
Bid–Ask Spread (bps)	1.1	1.1	1.5
Average Trading Size (KRW billion)	9.8	9.3	9.1
Off-the-Run			
Bid–Ask Spread (bps)	1.7	1.3	1.7
Average Trading Size (KRW billion)	9.7	9.2	9.1

bps = basis points, BOK = Bank of Korea, MSB = Monetary Stabilization Bonds.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

KRW9.7 billion for KTBs. Typical bid–ask spreads for BOK bills, however, were slightly higher: 1.5 basis points for on-the-run bills and 1.7 basis points for off-the-run bills. The average trading sizes for both on-the-run and off-the-run BOK bills were roughly the same at KRW9.1 billion.

As mentioned previously, liquidity for KTBs dramatically improved in 2010 in large part due to the high level of capital inflows into the Republic of Korea. KTBs are especially attractive to foreign investors because the government of the Republic of Korea has successfully consolidated issues by offering new bonds in larger sizes and frequently re-opens benchmark issues to improve their liquidity.

One of the more interesting structural changes under consideration in the KTB market includes a government plan to introduce the Republic of Korea treasury bills. The current short-term benchmark in the market is a 3-month certificate of deposit, which the government believes is not a sufficiently flexible monetary instrument since it fails to quickly respond to financial market changes.

The market is watching another government plan to effect structural change in the KTB market by introducing a 10-year KTB futures contract, although the current 3-year KTB futures contract is liquid and popular. In 3Q10, the number of 3-year KTB futures contracts traded rose 2.5% q-o-q and 30.2% year-on-year (y-o-y) to 6.6 million. Still, the government is seeking to establish a 10-year futures market for the purpose of supporting its efforts to extend the tenor on future KTB issues and has already taken supporting steps, such as making cash settlement available as a means for settling trades of 10-year futures contracts.

Thailand. The 2010 liquidity survey results for Thai government bonds showed an average on-the-run bid–ask spread of 3.1 basis points for benchmark treasury bonds **(Table 12)**. Bid–ask spreads for BOT bonds and bills were slightly wider than for treasury bonds, while the bid–ask spreads for treasury bills were slightly tighter than for treasury bonds. Average off-the-run bid–ask spreads were highest for treasury bonds at 7.7 basis points, while off-the-run BOT bonds were slightly less at 6.3 basis points. Treasury bills and BOT bills had a typical off-the-run bid–ask spread of 4.9 and 5.2 basis points, respectively. The average on-the-run transaction size for treasury bonds stood at THB56.4 million, with BOT bonds at a larger average size of THB68.6 million. Treasury bills and BOT bills had the largest average transaction sizes at around THB130 million.

Table 12: Thailand Government Bond Survey Results

	Treasury Bonds	BOT Bonds	Treasury Bills	BOT Bills
On-the-Run				
Bid–Ask Spread (bps)	3.1	3.6	3.0	3.2
Average Trading Size (THB million)	56.4	68.6	129.5	129.5
Off-the-Run				
Bid–Ask Spread (bps)	7.7	6.3	4.9	5.2
Average Trading Size (THB million)	35.5	46.6	76.6	76.6

bps = basis points, BOT = Bank of Thailand.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Malaysia. The Malaysian government LCY bond market is subdivided into four major components **(Table 13)**. According to data from the Fully Automated System for Issuing/Tendering (FAST) of Bank Negara Malaysia (BNM), liquidity in recent months has been limited to only a few Malaysian Government Securities (MGS) and Government Investment Issues (GII) bonds. The most liquid segment of the bond market in 3Q10 consisted of central bank bills, with a turnover ratio of 1.89. Bid–ask spreads for MGS and GII bonds averaged 2.6 and 2.8 basis points, respectively. Average bid–ask spreads for both BNM bills and treasury bills were 4.9 basis points. Average trading sizes for these securities were around MYR6.2 million for MGS and around MYR13.0 million for BNM bills and treasury bills. Bid–ask spreads for off-the-run MGS and GII were significantly wider and average trading sizes somewhat lower than their on-the-run counterparts. Bid–ask spreads for off-the run BNM bills and treasury bills were also somewhat wider than for on-the-run bills, but average trading sizes were significantly lower.

Table 13: Malaysia Government Bond Survey Results

	MGS	GII	BNM Bills	Treasury Bills
On-the-Run				
Bid–Ask Spread (bps)	2.6	2.8	4.9	4.9
Average Trading Size (MYR million)	6.2	6.7	13.3	13.3
Off-the-Run				
Bid–Ask Spread (bps)	6.2	6.8	5.3	5.3
Average Trading Size (MYR million)	4.5	5.0	5.0	5.0

BNM = Bank Negara Malaysia, bps = basis points, GII = Government Investment Issues, MGS = Malaysian Government Securities.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Qualitative Indicators for Government Bond Markets

Participants in the region's government and corporate bond markets were asked questions about market structure and ways to improve liquidity. The following spider charts capture market participants' perceived importance of the following bond market structure and policy issues:

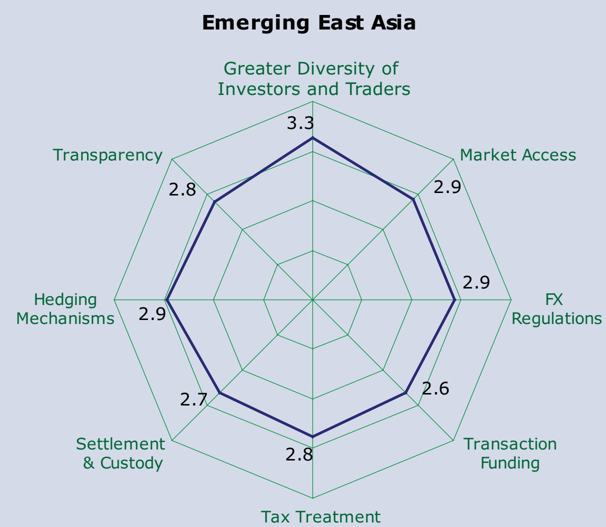
(i) greater diversity of investors and traders,
(ii) easing other restrictions on market access,
(iii) easing of foreign exchange regulations and restrictions,
(iv) funding availability for market participants,
(v) tax treatment,
(vi) settlement and custody,
(vii) more efficient hedging instruments, and
(viii) transparency.

Market participants were asked to assign a value between 1 and 4 to reflect the perceived importance of each issue in strengthening market structure and improving liquidity:

4 = Very important
3 = Important
2 = Somewhat important
1 = Not important

Figure 13 summarizes the results of the government bond market structure section of the 2010 *AsianBondsOnline* liquidity survey. It reveals that the most important structural issue for participants in the region's government bond markets was investor diversity, which had the highest score of 3.3, followed by hedging mechanisms, market access, and foreign exchange regulations, all with scores of 2.9. Comparing the 2010 survey results with 2009, market participants appeared to put more importance on structural issues this year.

Figure 13: Regional Averages—Government Bond Market Structural Issues



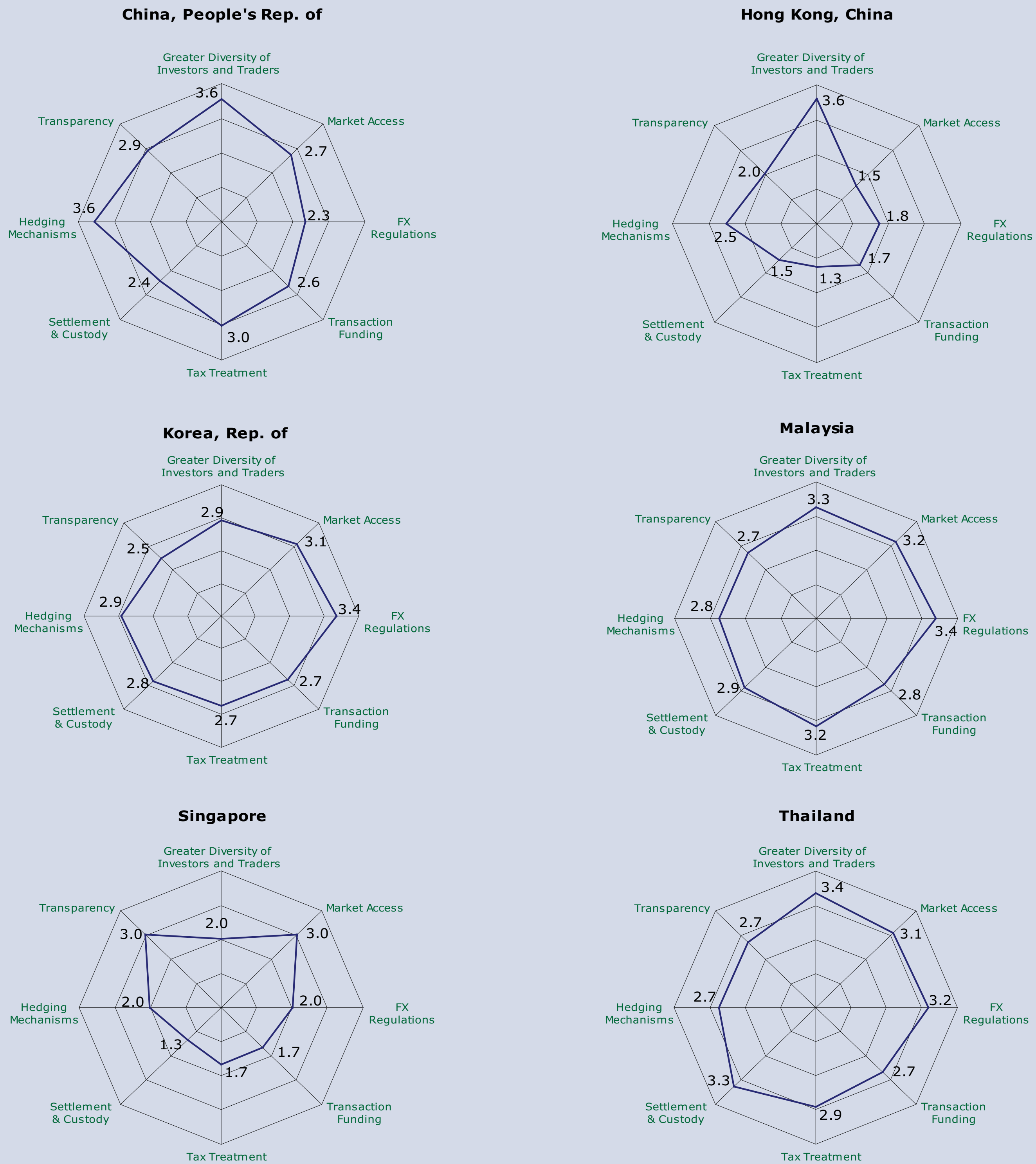
FX = foreign exchange.
Notes: Emerging East Asia comprises People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Figure 14 provides spider charts for each individual government bond market in emerging East Asia.

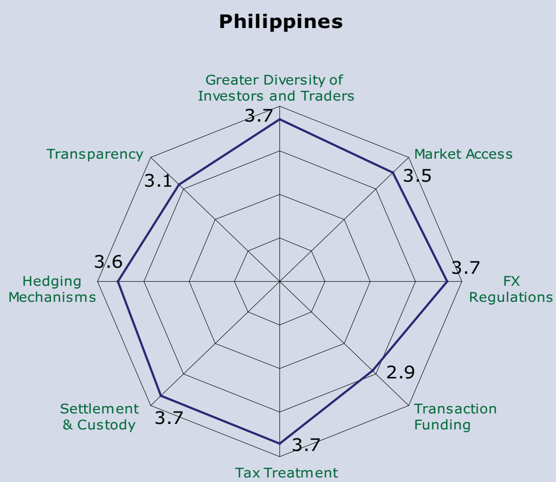
Greater Diversity of Investors and Traders

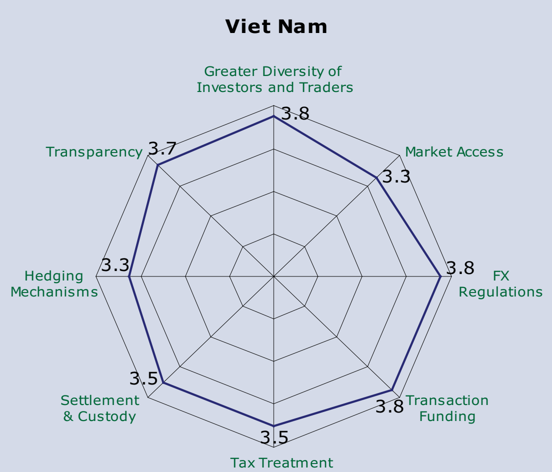
Greater investor diversity was viewed in most government bond markets in emerging East Asia as being important for promoting liquidity. This was especially true in Viet Nam, which registered the highest score for this indicator at 3.8, followed by the Philippines (3.7); the PRC (3.6) and

Figure 14: Structural Issues for Individual Government Bond Markets



FX = foreign exchange.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.





Hong Kong, China (3.6); Thailand (3.4); Malaysia (3.3); Indonesia (3.2); and the Republic of Korea (2.9). On the other hand, Singapore had the lowest score for this category at 2.0, indicating that greater investor diversity was only somewhat important for participants in this market.

Banks and other financial institutions continue to dominate most LCY government bond markets in emerging East Asia. As of June, banks' holdings of LCY treasury bonds in the PRC stood at about 60% of the total. Meanwhile, in the Republic of Korea, financial institutions—banks, insurance firms, pension funds, and other financial institutions—also held about 60% of all KRW-denominated government bonds.

Foreign investor holdings of LCY government bonds in some of the region's markets have risen rapidly over the last year, but these foreign holdings continue to be much smaller than the bond holdings of domestic investors.[5]

Hedging Mechanisms

The availability of hedging or derivative instruments (e.g., forwards, futures, options, swaps) had an average score of 2.9 across the region, suggesting that the increased availability of such mechanisms is an important requirement for promoting greater bond market liquidity. This criterion had the highest scores in the PRC and the Philippines at 3.6 each, followed by Indonesia and Viet Nam at 3.3 each. In Hong Kong, China and Singapore, however, the ratings were only 2.5 and 2.0, respectively.

Certain hedging instruments are currently available in emerging East Asian markets. For example, in Hong Kong, China, interest rate and cross-currency swaps are available and relatively liquid, as are 3-year Exchange Fund Note (EFN) futures. Interest rate and cross-currency swaps are also offered in the PRC. In the Republic of Korea, 3-, 5-, and 10-year KTB and MSB futures are offered, but only the 3-year KTB futures are currently liquid. Furthermore, the short-selling of government

[5] See Figure 3 in "Bond Market Developments in the Third Quarter of 2010."

securities is allowed under certain conditions in most emerging East Asian markets.

Foreign Exchange Regulations

Government bond market participants generally rated foreign exchange regulations as being important, with a regional average score of 2.9. Participants in several markets in particular highlighted the importance of the relationship between foreign exchange regulations and bond market liquidity, including Viet Nam (3.8), the Philippines (3.7), the Republic of Korea (3.4), Malaysia (3.4), and Thailand (3.2). However, for the PRC; Hong Kong, China; Indonesia; and Singapore, foreign exchange restrictions were considered to be only somewhat important.

Market Access

On average, market access was deemed an important issue by government bond market participants in the region, garnering a score of 2.9. Specifically, participants rated market access as important in the Philippines (3.5), Viet Nam (3.3), Malaysia (3.2), the Republic of Korea (3.1), Thailand (3.1), and Singapore (3.0). Market participants in the PRC (2.7) and Indonesia (2.5) felt less strongly about the importance of increasing market access. Finally, Hong Kong, China recorded the lowest score for this criterion at 1.5.

Other Indicators

The other indicators included in the survey on bond market liquidity—settlement and custody, tax treatment, transaction funding, and transparency—averaged between 2.6 and 2.8 across the region, suggesting that these issues were less important for market participants when compared with the four indicators detailed above.

Corporate Bond Market Trends

Corporate bond market participants were asked to respond to questions similar to the ones put to government bond market participants, with some slight variation. **Table 14** compiles the responses from corporate bond market participants with regard to average bid–ask spreads and trading sizes.

Bid–Ask Spreads. Bid–ask spreads for corporate bonds are typically much higher than those for government bonds, reflecting much lower levels of liquidity, which in many cases is limited to the months immediately following issuance. Emerging East Asia corporate bonds tend to be quickly absorbed by buy-and-hold investors. In Table 14, Indonesia had the highest average bid–ask spreads for corporate bonds at 99.7 basis points. The second highest bid–ask spread was 30.5 basis points for the Philippines. Other markets ranged between 5.7 basis points (PRC) and 25.0 basis points (Viet Nam).

Typical Transaction Size. Participants in the liquidity survey identified the largest average transaction sizes for corporate bond trades in Hong Kong, China (USD9.7 million) and the Republic of Korea (USD8.8 million). The PRC had the next largest average transaction size for corporate bond trades at USD6.4 million. Average transaction sizes in the region's other markets ranged from USD2.9 million in Malaysia to a low of USD0.3 million in the Philippines.

Inter-Market Comparisons

People's Republic of China. The most liquid elements of the PRC's corporate bond market in recent years have been its medium-term note (MTN) and commercial paper segments. In 3Q10, the stock of MTNs outstanding rose by 12.0% q-o-q and 73.8% y-o-y, while commercial papers outstanding increased by 9.0% q-o-q and 89.9% y-o-y. Robust growth in both of these segments has contributed to the relatively high turnover ratios for these types of securities **(Figure 15)**. By comparison, the turnover ratios for bonds issued by state-owned enterprises (SOEs) were much lower in 3Q10.

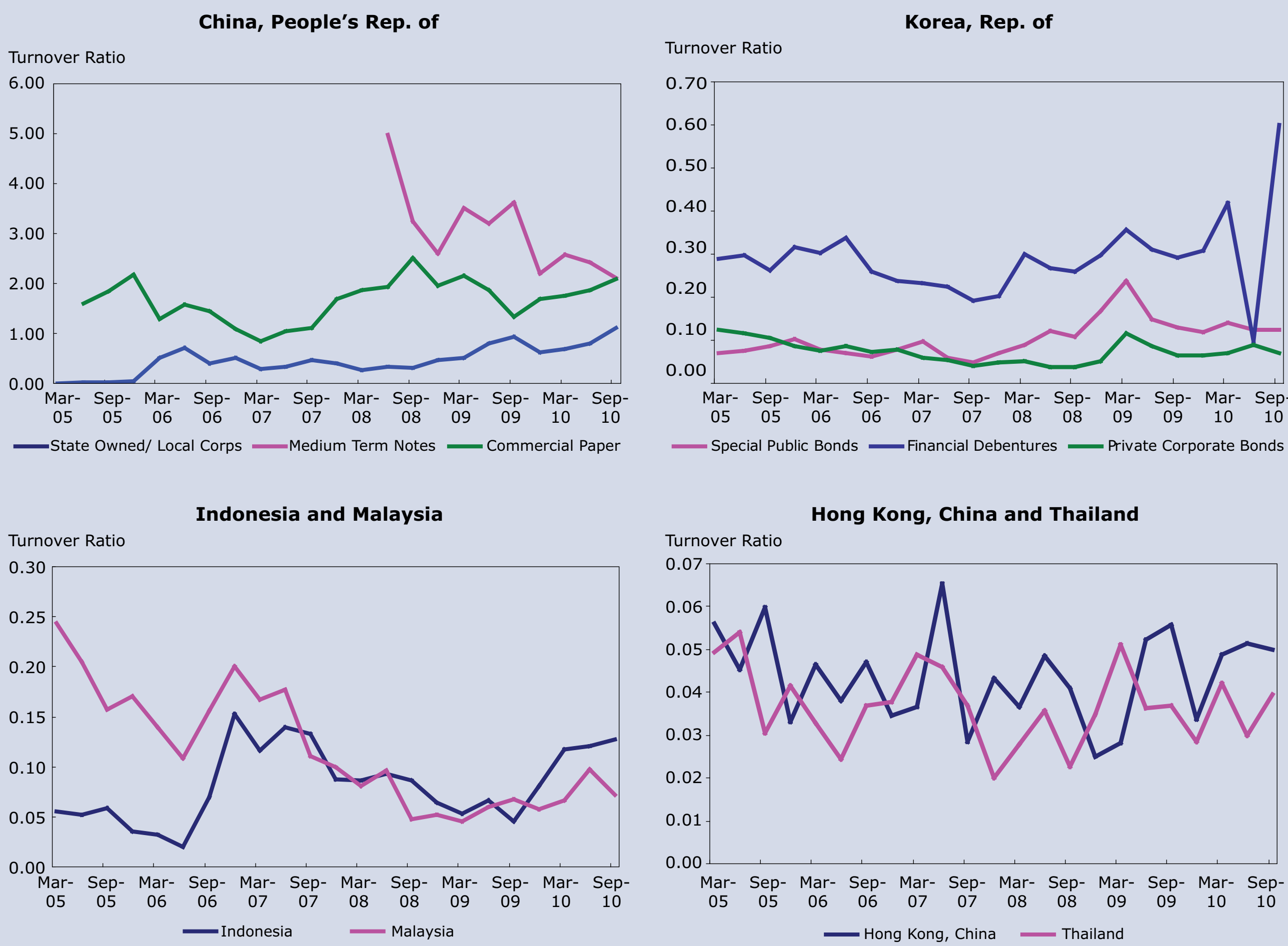
Overall, bid–ask spreads for MTNs and commercial papers were tighter than the bid–ask spreads for SOE and commercial bank bonds **(Table 15)**.

Table 14: Corporate Bond Market Quantitative Indicators

		PRC	HK	ID	KR	MY	PH	SG	TH	VN	Regional
Typical Issue Size of Corporate Bonds (USD million)	Average	458.8	48.3	123.4	50.4	131.8	127.9	193.0	115.4	84.7	148.2
Typical Bid–Ask Spread for New Corporate Issues (bps)	Average	5.7	12.5	99.7	2.6	16.0	30.5	10.4	11.1	25.0	23.7
	Count	6	2	8	6	5	5	6	10	3	51
	SD	1.5	10.6	46.6	1.0	2.2	5.7	4.6	6.3	5.0	29.8
Typical Transaction Size of LCY Corporate Bonds (USD million)	Average	6.4	9.7	0.8	8.8	2.9	0.3	2.8	0.7	2.6	3.9
	Count	6	2	8	6	5	5	6	10	3	51
	SD	2.6	4.6	0.2	-	1.4	0.2	0.8	0.4	-	3.5

— = not applicable; bps = basis points; HK = Hong Kong, China; ID = Indonesia; KR = Republic of Korea; LCY = local currency; MY = Malaysia; PH = Philippines; PRC = People's Republic of China; SD = standard deviation; SG = Singapore;TH = Thailand; VN = Viet Nam.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Figure 15: Trends in Quarterly Corporate Turnover Ratios



Source: *AsianBondsOnline*.

MTNs and commercial papers also traded in larger sizes than SOE bonds do, according to the survey results. Trading sizes for commercial bank bonds were the largest within the PRC corporate bond market, but these issues consisted almost entirely of subordinated debt bonds, which are not particularly liquid.

Table 15: PRC Corporate Bond Survey Results

	SOE Bonds	MTNs	Commercial Bank Bonds	Commercial Paper
Bid–Ask Spread (bps)	5.7	3.9	7.1	3.8
Average Trading Size (CNY million)	42.5	54.2	58.3	57.5

bps = basis points, MTNs = medium-term notes, PRC = People's Republic of China, SOE = state-owned enterprise.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Republic of Korea. Liquidity trends in the Republic of Korea corporate bond market have been relatively volatile over the past several years. Figure 15 shows that the turnover ratio for special public bonds, which are bonds issued by state agencies and government-owned corporations, rose between 4Q07 and 1Q09 before falling off. The turnover ratio for commercial bank debentures, which has historically been much higher than the ratio for special public bonds, rose sharply throughout 2009 and early 2010 before falling dramatically in 2Q10. This ratio subsequently made a quick recovery to rise to new highs at the end of 3Q10. Meanwhile, the turnover ratio for private sector bonds has historically been extremely low, averaging around 0.1.

The data collected on average bid–ask spreads and transaction sizes across the major types of LCY corporate bonds in the Republic of Korea are broadly consistent with the trends in turnover ratios described above. Financial debentures had the lowest average bid–ask spread at 2.2 basis points, followed by special public bonds at 2.6 basis points. Private corporate bonds had the highest average bid–ask spread at 3.6 basis points. Average transaction sizes, however, are the same across the three types of corporate bonds at KRW10.0 billion **(Table 16)**.

Table 16: Republic of Korea Corporate Bond Survey Results

	Special Public Funds	Financial Debentures	Private Corporate Bonds
Bid–Ask Spread (bps)	2.6	2.2	3.6
Average Trading Size (KRW billion)	10.0	10.0	10.0

bps = basis points.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Philippines. Trading volume data was not available for the Philippine corporate bond market as a whole. Therefore, turnover ratios for Philippine corporate bonds cannot be calculated as a measure of liquidity.

The Philippines had been one of the most rapidly growing LCY corporate bond markets in Asia until 3Q10 when its growth rate fell to 1.7% q-o-q. Yet, the y-o-y growth rate in 3Q10 was still a robust 22.4%.

The Philippine Dealing and Exchange Corporation (PDEx) maintains a data base on the trading volume of large bonds and bond issuers. The bonds of the Power Sector Assets and Liabilities Management Corporation (PSALM) have become the most actively traded bonds on the PDEx this year. The trading volume of PSALM bonds stood at PHP15.0 billion in 3Q10, comprising 80% of the total trading volume of all PDEx-listed bonds **(Table 17)**. PSALM bonds are classified as government bonds since PSALM is a government company and all of its bonds carry a government guarantee. Thus, PSALM bonds are included in our data base for Philippine government issuance and bonds outstanding, but not in the turnover ratio for Philippine government bonds, which is limited to treasury bonds.

PDEx also provides data on the trading volumes of private sector bonds, such as San Miguel Brewery (PHP1.4 billion), Ayala Corporation (PHP721.8 million), Energy Development Corporation (PHP586.5 million), JG Summit (PHP283.7 million), Globe Telecom (PHP235.1 million), and Tanduay Distillers (PHP165.8 million).

Finally, the average bid–ask spread for Philippine corporate bonds was 30.5 basis points in 2010, down from 43.8 basis points in 2009. The average trading size roughly doubled over the same period from PHP6.3 million to PHP14.1 million (USD0.3 million), following the trend toward much larger trading sizes in the government bond sector, which more than quadrupled between 2009 and 2010.

Table 17: Trading Volume of Top Philippine LCY Corporate Bonds, 1Q10–3Q10

Corporate Bond Issues	1Q10	2Q10	3Q10
	(PHP million)		
Ayala Corp bonds due 2012 and 2017	229.2	238.5	721.8
Globe Telecom bonds due 2012 and 2014	46.3	49.6	235.1
San Miguel Brewery bonds due 2012	958.4	266.4	1,413.6
Energy Development Corp bonds due 2015 and 2016	469.4	707.3	586.5
PSALM bonds due 2015	—	17,567.4	14,982.7
JG Summit bonds due 2014	—	4.7	283.7
Tanduay Distillers bonds due 2015	—	0.0	165.8

— =not applicable, LCY= local currency, PSALM = Power Sector Assets and Liabilities Management Corp. (PSALM).
Source: Philippine Dealing and Exchange Corporation (PDEx)

Malaysia: Malaysian corporate bond liquidity was broadly in the average range for quarterly bond market turnover ratios (0.1 to 0.3) in emerging East Asia in 3Q10, as shown in Figure 15. However, the overall corporate bond market liquidity ratio masks a large difference between liquidity for financial companies and non-financial companies. According to data of the Fully Automated System for Issuing/Tendering (FAST) of BNM, the monthly number of trades for bonds of financial companies is typically two to three times higher than for non-financial companies.[6] The survey results show that the average bid–ask spread for a typical new corporate bond in Malaysia is around 16 basis points, somewhat higher than in the neighboring markets of Singapore and Thailand. The average transaction size was USD2.9 million, somewhat larger than in Singapore, and significantly larger than in Thailand or the Philippines.

[6] This situation is consistent with *AsiaBondOnline*'s analysis of the Malaysian corporate bond sector, which was published in the second chapter of the October edition of the Asia Bond Monitor (Corporate Bond Market Developments). **Figure 13** of the October edition (page 37) showed that a very large majority of corporate bonds issued in emerging East Asia are issued by financial companies, and this is especially true in Malaysia.

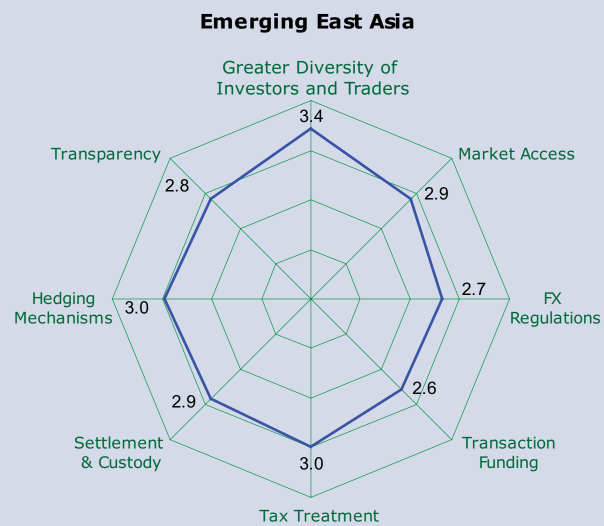
Indonesia. Indonesia was the region's most rapidly growing bond market in 3Q10 outside of the PRC. The Indonesian corporate bond market's y-o-y growth rate was 30.7% compared with 50.5% for the PRC, and the Indonesian corporate bond market's q-o-q growth rate of 10.9% was identical to that of the PRC in 3Q10. The Indonesian corporate bond market's y-o-y issuance growth rates in 3Q10 was 325.8%—higher than any other corporate bond market in emerging East Asia on a y-o-y basis. The Indonesian corporate bond market's q-o-q issuance growth rate of 57.4% was exceeded only by that of Singapore (64.8%).

The three most notable issuers in 3Q10 were Indonesia Eximbank (formerly Bank Ekspor Indonesia), the state-owned electricity company PLN, and telecommunications company Telkom (52% state-owned). These three companies issued a series of bonds in 3Q10 for a total of IDR3.0 trillion (USD340 million) each. Most of these bonds carried coupons of 9%–10%. In addition, Bank CIMB Niaga issued IDR1.7 trillion of bonds. The typical bid–ask spread for Indonesian corporate bonds in 2010 was 99.7 compared with 112.5 in 2009, while the average transaction size of USD0.75 million in 2010 was approximately the same level as in 2009.

Singapore: Singapore's corporate bond market grew 7.1% q-o-q in 3Q10, making it the third most rapidly growing corporate bond market in the region on a q-o-q basis. Furthermore, Singapore's corporate bond issuance rose 64.8% q-o-q in 3Q10, the highest q-o-q issuance growth rate recorded for any corporate bond market in emerging East Asia. This impressive performance was driven by a series of issues notable for both their size and duration. The largest of these issues was the impressive SGD1.0 billion (USD159 million) 40-year issue of Temasek Financial. When this issue was announced in August of this year, it created a new long-dated benchmark for corporate bond issues in Singapore, effectively giving Singapore the longest duration of any corporate bond market in emerging East Asia. Other large issues in 3Q10 included SGD500 million each from City Developments, Ltd., Singapore Airlines (issued with a maturity of 10 years), and the Housing Development Board. Other notable bonds issued with maturities ranging from 10 to 15 years came from the Public Utilities Board, Capitaland, Neptune Orient Lines, SP Powerassets, and Sembcorp Financial Services.

Singapore's corporate bid–ask spreads averaged 10.4 basis points in 2010, down from 12.5 basis points in 2009, while the average transaction size more than doubled in 2010 to USD2.8 million.

Figure 16: Regional Averages—Corporate Bond Market Structural Issues



FX = foreign exchange.
Notes: Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

Qualitative Indicators for Corporate Bond Markets

Figure 16 summarizes the results of the corporate bond market structure section of the 2010 *AsianBondsOnline* Bond Market Liquidity Survey. The results are similar in many respects to the spider charts for the government bond market. For example, the most important structural issue for participants in the region's corporate bond market was investor diversity. The score of 3.4 for investor diversity in the corporate bond market survey was slightly higher than the 3.3 score in the government bond market survey. The responses of corporate bond market participants were also very similar to those of government bond market participants with respect to market access, transaction funding, hedging mechanisms, and transparency.

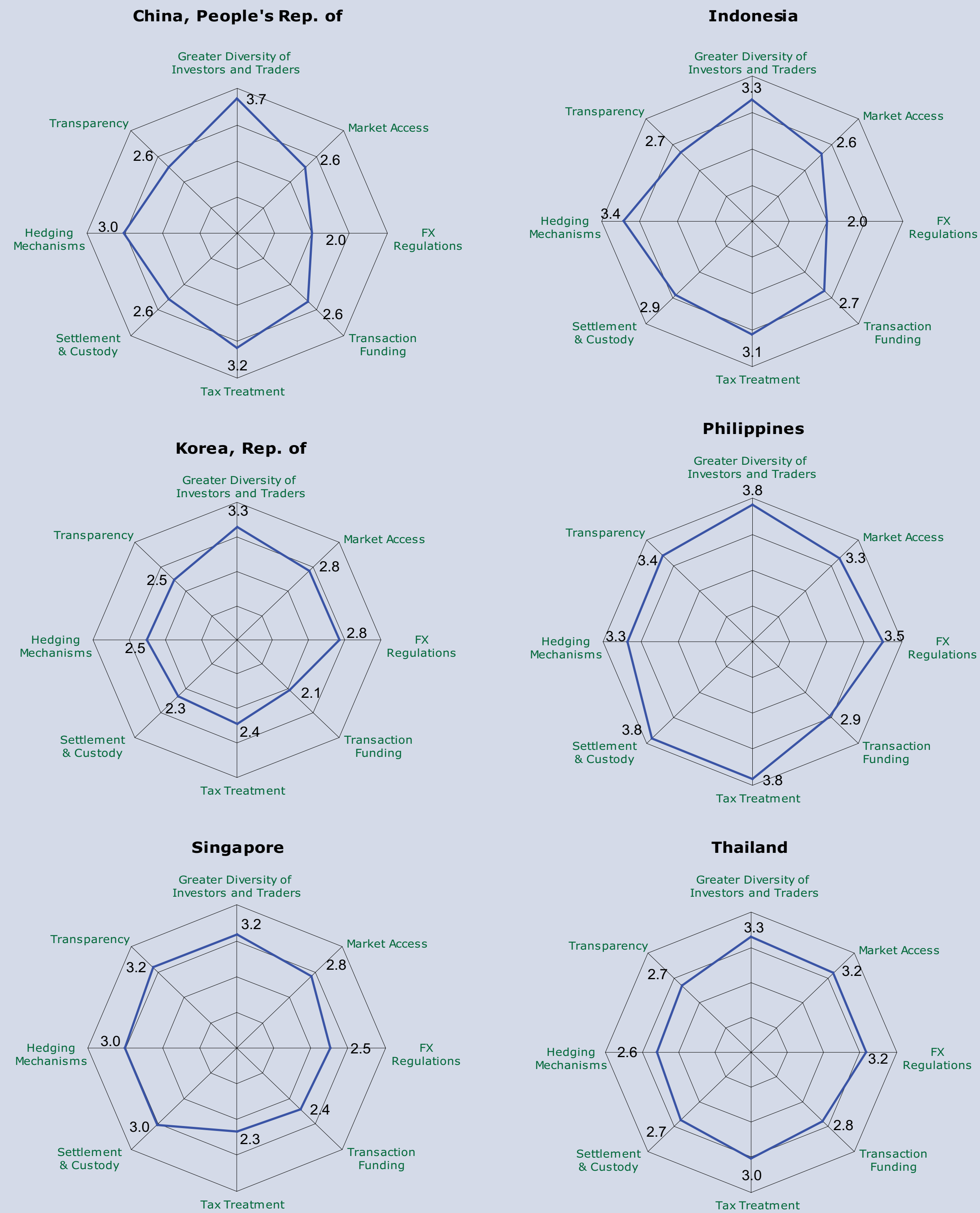
However, corporate bond market responses were higher than the government bond market responses for tax treatment (3.0 vs. 2.8), settlement and custody (2.9 vs. 2.7), and hedging mechanism (3.0 vs. 2.9).

The corporate bond market responses differ significantly across individual markets **(Figure 17)**. The two corporate bond markets where survey participants were seeking the most structural changes were in the Philippines and Thailand. Still, survey participants from Thailand gave scores ranging between 2.6–2.7 for transparency, availability of hedging mechanisms, and settlement custody. Respondents from the Philippines placed more weight on reforming market structure as evident by scores of 3.0–4.0 for all market structure categories, with the exception of transaction funding (2.9).

Average market structure scores for the corporate bond market in the Republic of Korea were the lowest among all markets surveyed, ranging between 2.0 and 3.0, with the exception of investor diversity, which had an average score of 3.3.

Scores for Indonesia, Singapore, and the PRC, which were the three most rapidly growing corporate bond markets in 3Q10, lay in a range of 2.0–3.0 for the majority of market structure categories. Market access, foreign exchange regulations, and transaction funding were criteria that generated scores of 2.8 or less in Indonesia, Singapore, and the PRC, which is to suggest that these issues were deemed as less than important by most participants in these markets. Other issues—such as tax treatment, settlement and custody, and transparency—generated scores that varied considerably across the three markets, reflecting differences in market structures and operating environments.

Figure 17: Structural Issues for Individual Corporate Bond Markets



FX = foreign exchange.
Source: *AsianBondsOnline* 2010 Local Currency Bond Market Survey.

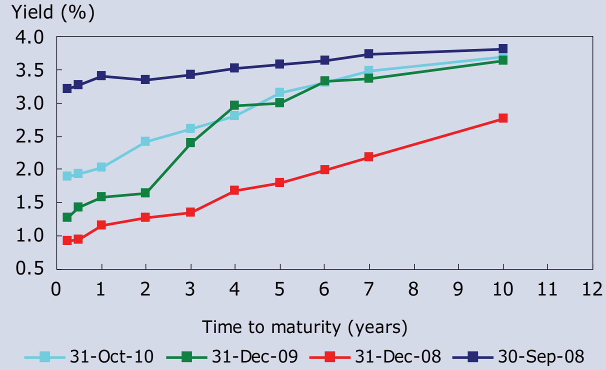
Market Summaries

People's Republic of China—Update

Yield Movements

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

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



LCY = local currency.
Source: Bloomberg LP.

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

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

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

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

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

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

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

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

Size and Composition

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

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

Corporate Bonds

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

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

Table 2: Corporate Bonds Outstanding in Key Sectors

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

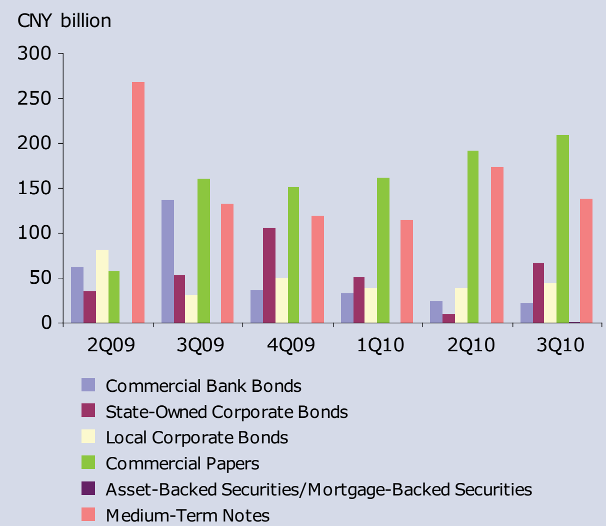
q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Source: *ChinaBond.*

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

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

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

Figure 2: Corporate Bond Issuance in Key Sectors



Source: *ChinaBond.*

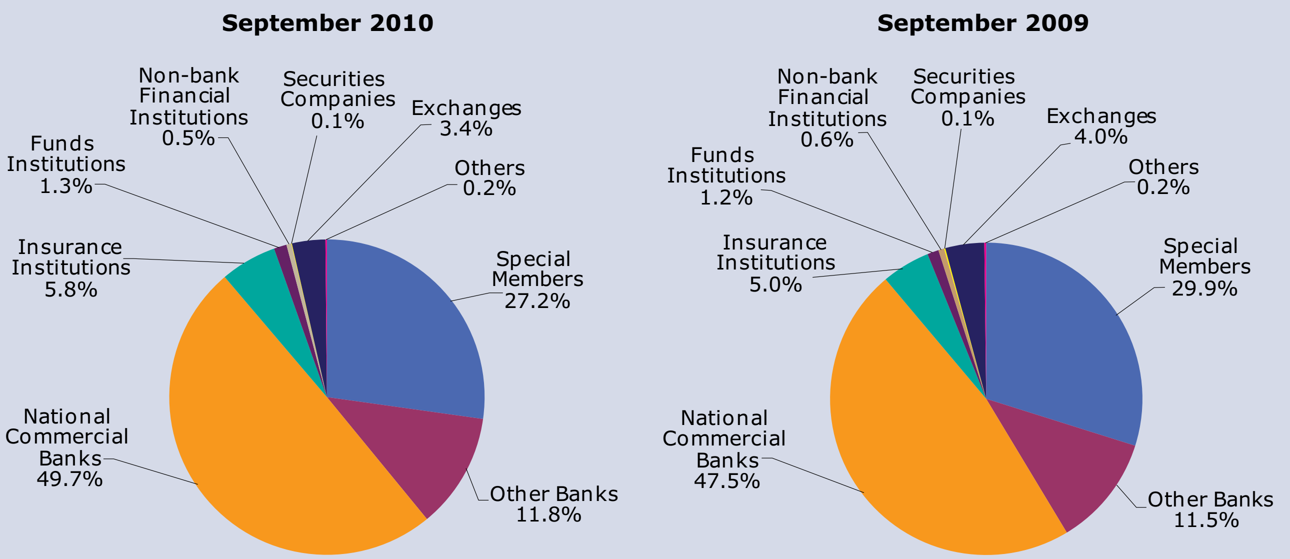
Investor Profile

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

Rating Changes

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

Figure 3: LCY Government Bonds Investor Profile



Source: *ChinaBond*.

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

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

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

economy through "extraordinary credit expansion" in 2009.

Policy, Institutional, and Regulatory Developments Ratings Upgrade

PBOC Allows Banks to Sell Loans to Each Other

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

Clearstream and Euroclear Enable Settlement of CNY-Denominated Securities

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

Banks Barred from Providing Mortgages to Third Home Buyers

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

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

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

PRC Allows Foreign Institutions to Open Yuan Accounts

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

Chinese Insurers Barred from Property Speculation

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

Banks Return to Exchanges

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

PRC Launches Credit Default Swaps

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

PRC Tightens Controls over Overseas Fund Inflows

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

PRC Limits Hot Money Flows into Real Estate Market

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

PBOC Hikes Reserve Requirement Ratios

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

Hong Kong, China—Update

Yield Movements

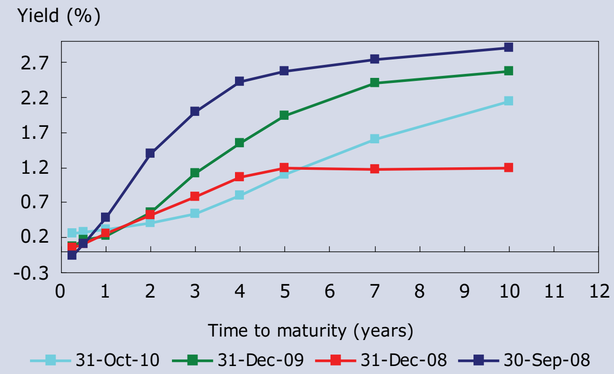
The yield curve for Hong Kong, China's Exchange Fund Bills and Notes (EFBN) between end-December 2009 and end-October 2010 rose 9–18 basis points at the short-end, but tightened by as much as 84 basis points along the rest of the curve **(Figure 1)**. The yield on the 2-year tenor fell 15 basis points,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

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

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

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

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



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

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

Size and Composition

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

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

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

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

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

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

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

Table 2: Top 20 Non-Bank Corporate Issuers

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

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

Rating Changes

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

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

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

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

Policy, Institutional, and Regulatory Developments

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

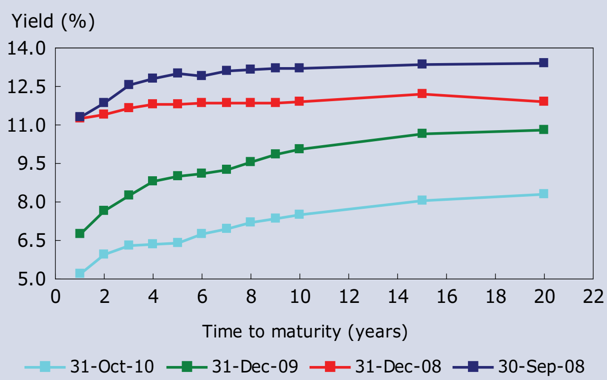
In October, the Asian Development Bank (ADB) raised CNY1.2 billion of 10-year bonds in Hong Kong, China. The bonds were sold at par and with a coupon rate of 2.85%. The offering was the first issued in Hong Kong, China by a highly-rated supranational. The bonds are expected to provide a benchmark for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

Indonesia—Update

Yield Movements

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

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



LCY = local currency.
Source: Bloomberg LP.

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

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

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

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

Size and Composition

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

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

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

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

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

Notes:

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

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

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

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

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

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

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

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

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

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

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

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

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

Table 2: Top 30 Corporate Issuers, September 2010

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

LCY = local currency.
Source: Indonesia Stock Exchange.

Table 3: Notable Corporate Issuance in 3Q10

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

Source: Indonesia Stock Exchange.

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

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

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

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

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

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

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

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

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

Foreign Currency Bonds

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

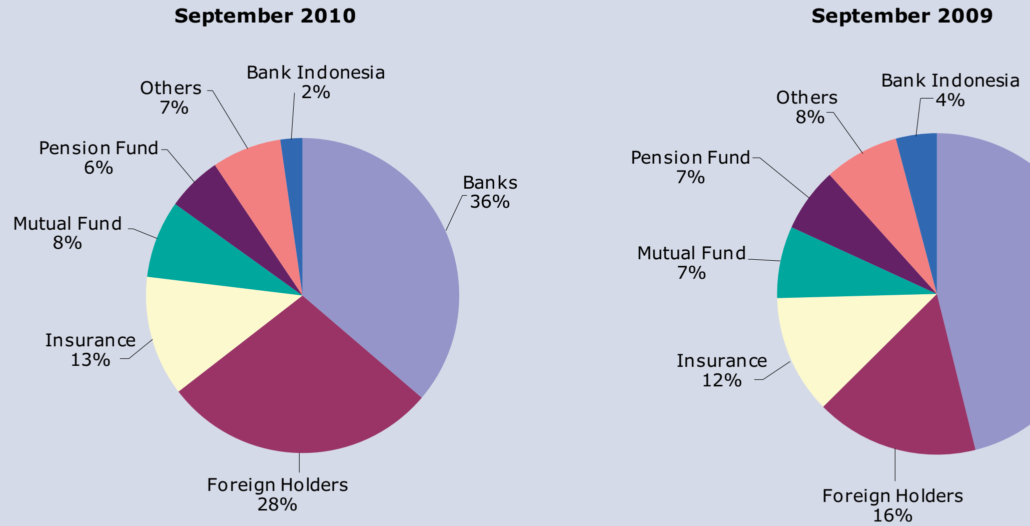
Investor Profile

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

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

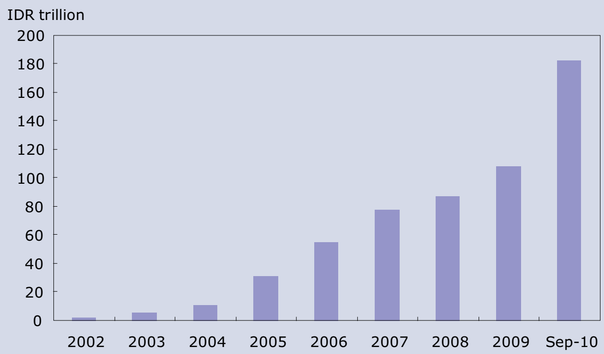
Banks were also the primary holders of SBIs, with a share of 71% at end-September **(Figure 4)**. However, banks' share in SBI holdings has fallen considerably from a high of 89% in June 2009. Foreign interest in SBIs continued to rise in 3Q10 despite the new requirement of a 1-month holding period for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

Figure 2: LCY Government Bonds Investor Profile



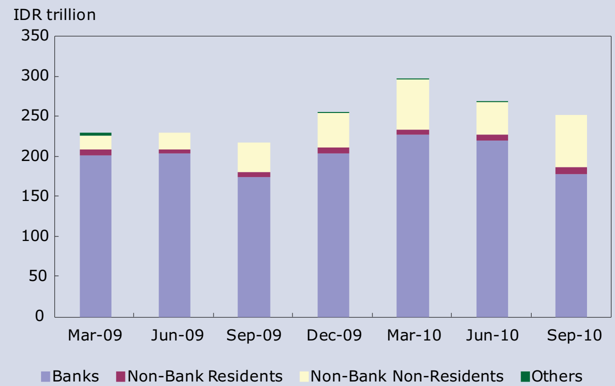
LCY = local currency.
Source: Indonesia Debt Management Office.

Figure 3: Foreign Holdings of LCY Government Bonds



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

Figure 4: LCY Central Bank Bills Investor Profile



LCY = local currency.
Source: Bank Indonesia.

Rating Changes

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

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

Table 4: Selected Sovereign Ratings and Outlook for Indonesia

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

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

Policy, Institutional, and Regulatory Developments

BI Announces New Regulations on Reserve Requirements and Bank Lending

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

BI Plans to Offer New Term Deposits

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

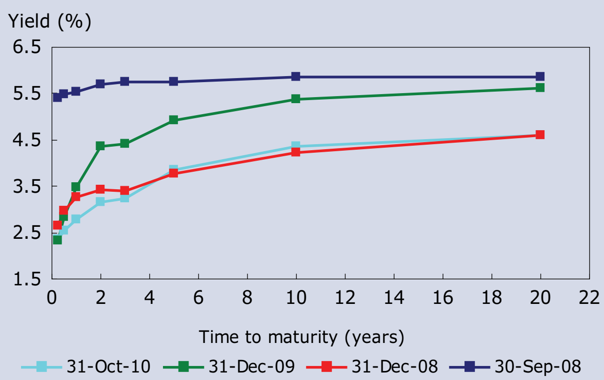
Republic of Korea—Update

Yield Movements

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

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

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



LCY = local currency.
Source: Bloomberg LP.

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

Size and Composition

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

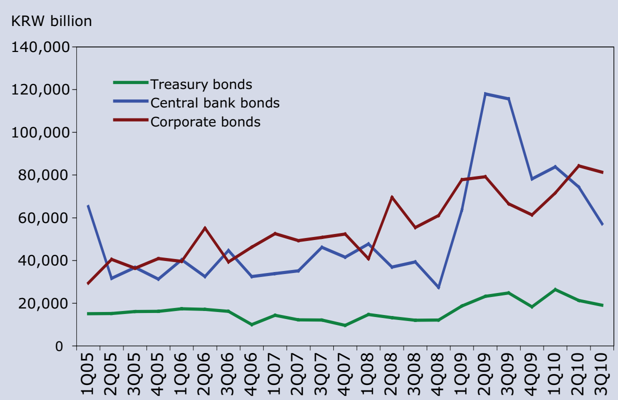
corporate bonds outstanding **(Table 4)**. The largest three issuers were Daewoo Securities, Woori Investment and Securities, and Korea Investment and Securities.

Issuance

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

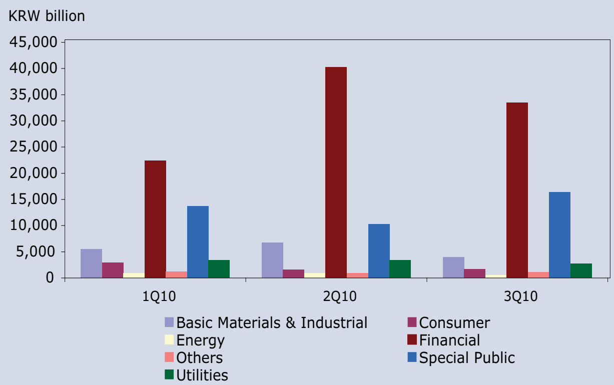
The sector with the largest corporate bond issuance in the Republic of Korea in 3Q10 was the financial sector, comprising about 56% of the total **(Figure 3)**. On a q-o-q basis, corporate bond issuance fell for most sectors in 3Q10, including the basic materials/industrial, energy, financial, and utilities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

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



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

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



LCY = local currency.
Source: Bloomberg LP.

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

Investor Profile

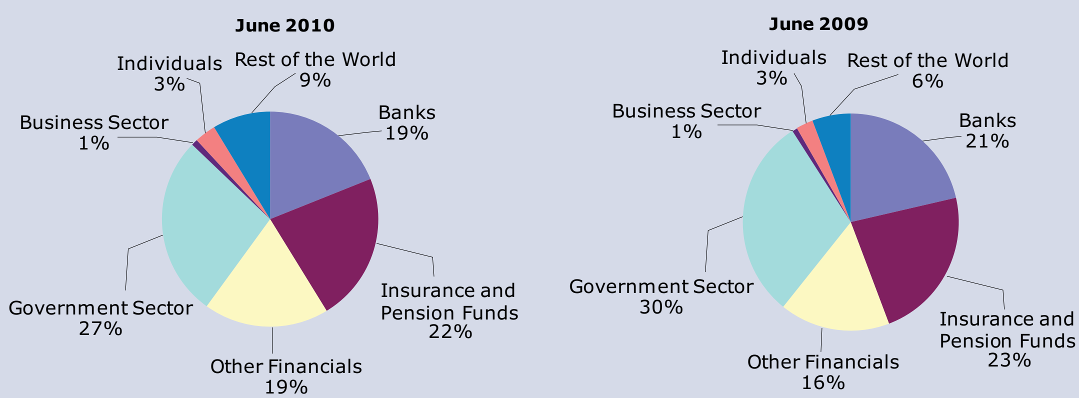
The Republic of Korea's public sector remained the largest owner of government bonds in June 2010, with a 27% share of the total **(Figure 4)**. Insurance firms/pension funds were the second-largest holder of government bonds with a 22% share, while banks and other financial institutions held 19% each.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

Liquidity

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

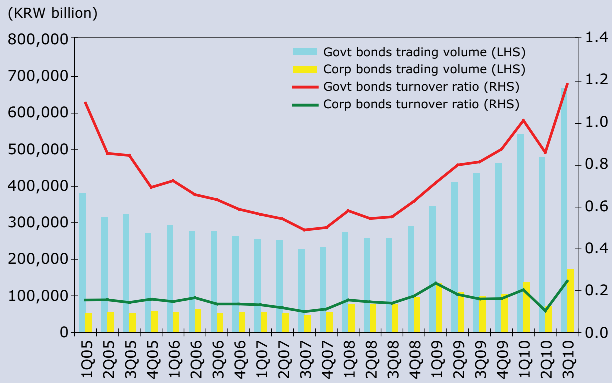
The increased liquidity of the LCY government bonds in 3Q10 may be attributed to a quarterly rise in trading volumes and turnover ratios for both central government and central bank bonds **(Figure 6)**. The trading volume for central government bonds climbed 7.2% q-o-q and 51.2% y-o-y, while the turnover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

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



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

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

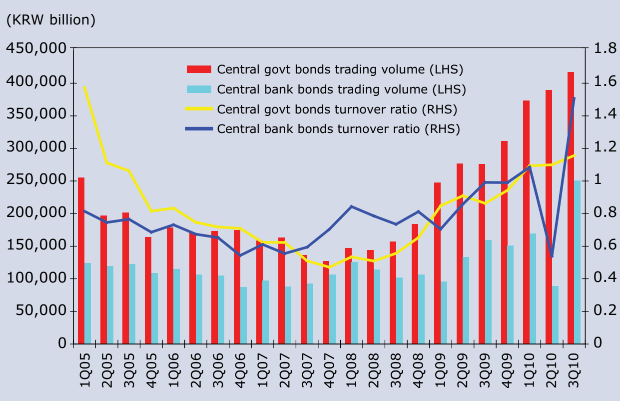


Notes:
1. LHS = left-hand side, RHS = right-hand side, LCY = local currency.
2. Trading volume is the average of sales and purchases of bonds traded.
Source: *AsianBondsOnline*, Bloomberg LP, and *KoreaBondWeb*.

spread for BOK bonds (excluding BOK bills) was 1.11 basis points, which was slightly lower than 1.14 basis points for KTBs.

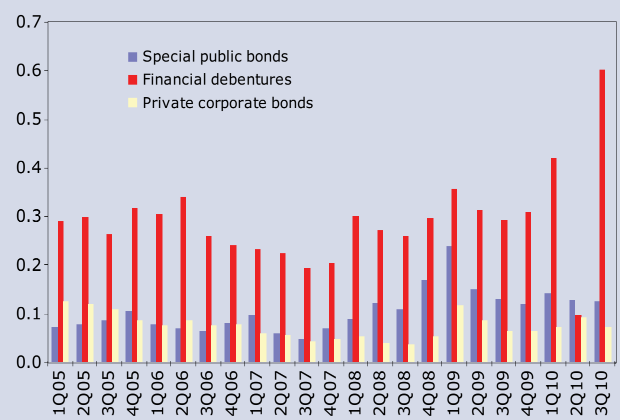
Across the major types of LCY corporate bonds in the Republic of Korea, the turnover ratio for financial debentures increased to 0.60 in 3Q10 from 0.1 in the previous quarter, but the turnover ratios for special public bonds and private corporate bonds fell marginally in 3Q10 to 0.12 (from 0.13 in 2Q10)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

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



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

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



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

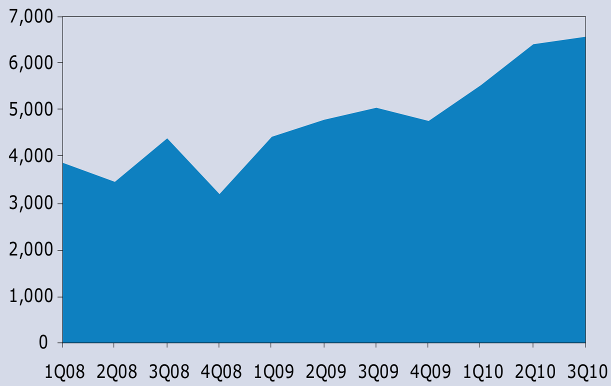
and 57.2% y-o-y in 3Q10, while the turnover ratio rose to 1.51 from 0.54.

In 3Q10, the turnover ratio for central bank bonds was higher than that for central government bonds, suggesting that central bank bonds were relatively more liquid than central government bonds. This appears to be consistent with the 2010 *AsianBondsOnline* liquidity survey results, which showed that the average on-the-run bid–ask

points, followed by special public bonds and private corporate bonds with average bid–ask spreads of 2.58 and 3.58 basis points, respectively.

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

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



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

Rating Changes

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

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

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

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

Policy, Institutional, and Regulatory Developments

Short-Term KTBs to be Introduced

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

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

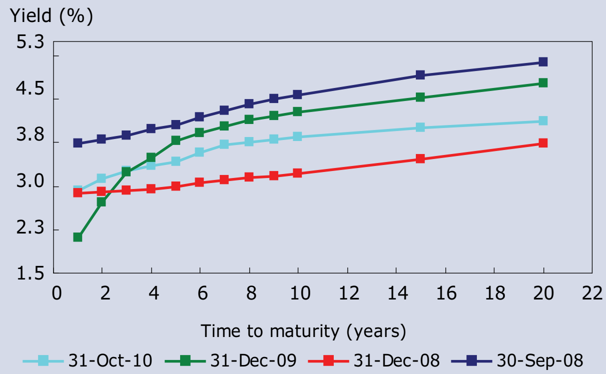
In September, the Financial Services Commission approved the Korea Exchange's amended version of its Derivatives Market Business Regulation, which aims to enhance the trading of long-term KTB futures. The revised version calls for harmonizing regulations on short-term and long-term KTB futures to improve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

Malaysia—Update

Yield Movements

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

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



LCY = local currency.
Source: Bloomberg LP.

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

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

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

Size and Composition

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

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

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

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

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

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

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

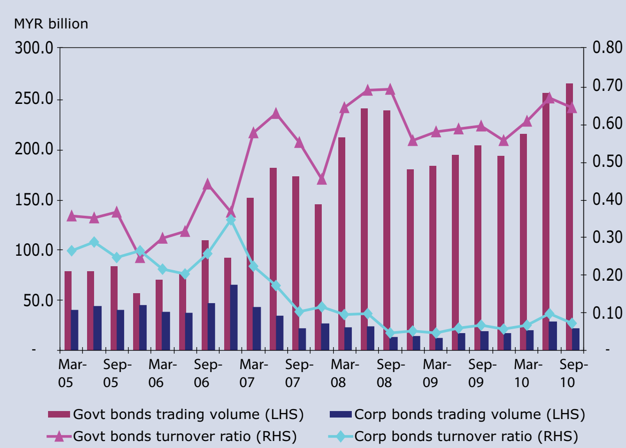
LCY bonds outstanding **(Table 2)**. National mortgage corporate Cagamas Bhd remained the biggest issuer of corporate LCY bonds, with MYR18.1 billion outstanding at the end of 3Q10, followed by Khazanah Nasional and Binariang GSM, with MYR13.2 billion and MYR11.3 billion, respectively.

Turnover

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

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

Figure 2: LCY Bonds Quarterly Trading Volume and Turnover Ratio



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

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

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

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

Policy, Institutional, and Regulatory Developments

BNM Further Liberalizes FX Rules

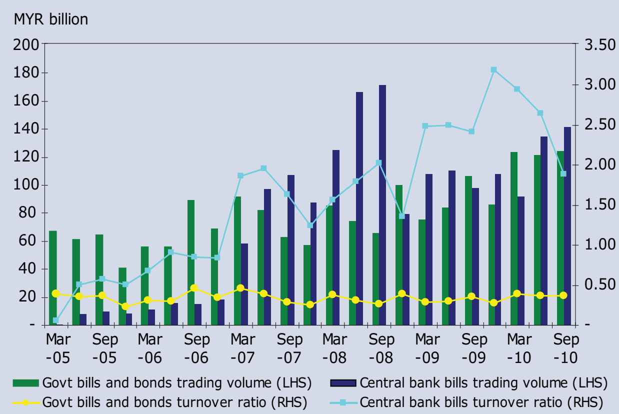
In August, BNM announced the further liberalization of foreign exchange (FX) administrative rules to promote efficiency in trade. The new rules provide for the following:

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

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

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

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



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

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

Philippines—Update

Yield Movements

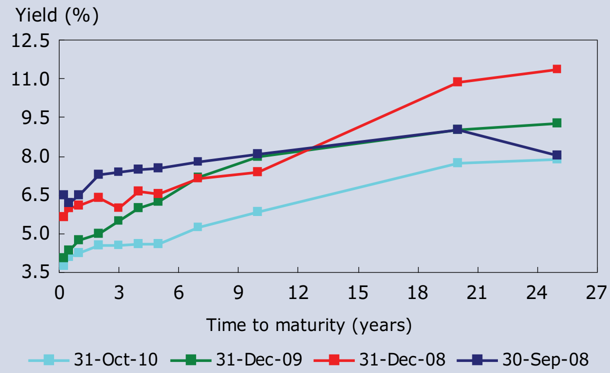
Philippine government bond yields fell for all maturities between end-December 2009 and end-October 2010 on expectations of sustained economic growth **(Figure 1)**. The decline at the shorter-end of the curve ranged between 25 and 95 basis points, while the drop at the belly to the longer-end of the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

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

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

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

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



LCY = local currency.
Source: Bloomberg LP.

Size and Composition

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

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

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

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

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

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

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

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

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

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

LCY = local currency.
Source: Bloomberg LP.

Rating Changes

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

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

Table 3: Selected Sovereign Ratings and Outlook for the Philippines

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

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

Policy, Institutional, and Regulatory Developments

Government and Petron Issue Peso Global Bonds

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

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

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

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

Singapore—Update

Yield Movements

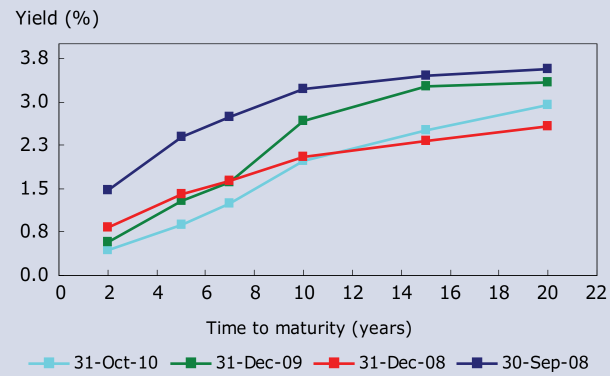
Singapore government bond yields fell throughout the length of the curve between end-December 2009 and end-October 2010 **(Figure 1)**. The yield on the 2-year tenor declined 15 basis points from its end-December level. Yields declined by larger amounts along the rest of the curve: the 5-year tenor declined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

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

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

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

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



LCY = local currency.
Source: Bloomberg LP.

Size and Composition

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

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

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

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

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

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

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

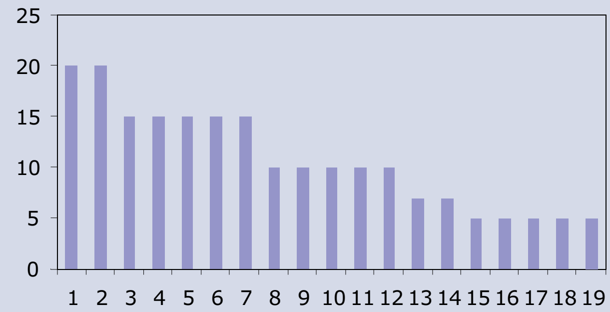
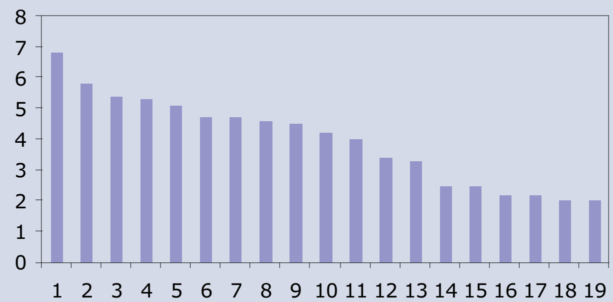


Figure 2b: Singapore LCY Government Bonds by Size (SGD billion)



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

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

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

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

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

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

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

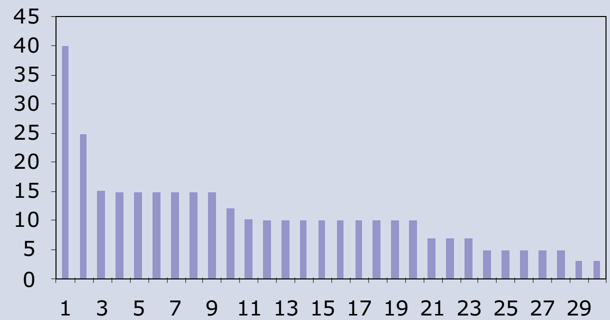
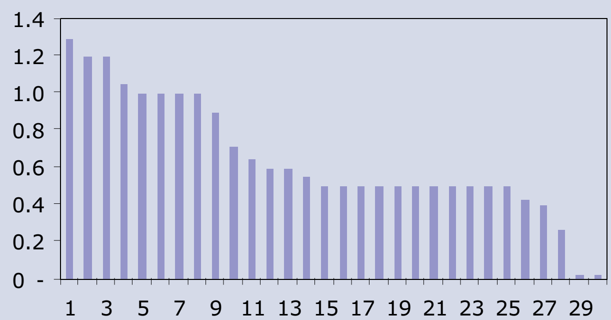


Figure 3b: Top 30 LCY Corporate Bonds by Size (SGD billion)



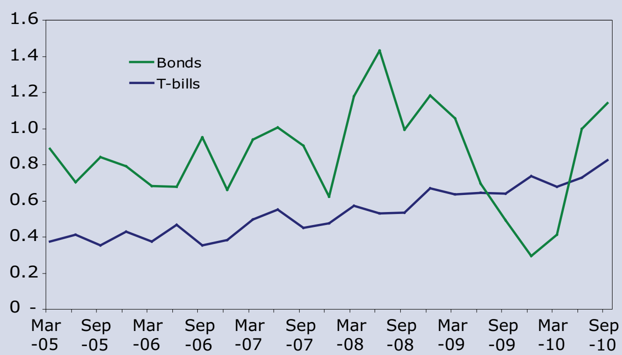
LCY = local currency.
Source: Bloomberg LP and *AsianBondsOnline*

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

Turnover Ratios

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

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



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

Rating Changes

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

Table 3: Selected Sovereign Ratings and Outlook for Singapore

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

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

Policy, Institutional, and Regulatory Developments

PBOC and MAS Agree to a Bilateral Currency Swap

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

Singapore Exchange Launches Initiatives to Boost Bond Listing and Trading

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

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

SGX to launch ADRs

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

Thailand—Update

Yield Movements

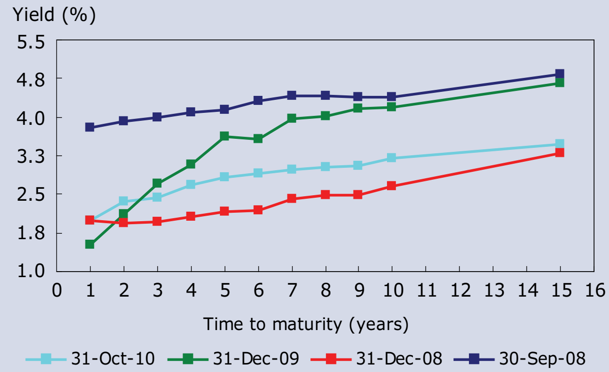
Thai government bond yields fell for most maturities between end-December 2009 and end-October 2010 **(Figure 1)**. Yields for 1- and 2-year maturities rose 46 and 25 basis points, respectively, while yields fell for all other maturities, resulting in a flattening of the curve. Specifically, yields for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

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

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

Thailand's gross domestic product (GDP) slowed to 6.7% y-o-y in 3Q10, after expanding 9.1% y-o-y in 2Q10. Growth in the Thai economy is expected to drop further in 4Q10 due to the strengthening

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



LCY = local currency.
Source: Bloomberg LP.

baht, fluctuating oil prices, and the impact of flooding on agricultural output. Thailand's GDP is expected to grow 7.3%–8.0% in 2010, according to BOT, and 3.0%–5.0% in 2011.

Size and Composition

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Table 2: Top 30 Corporate Issuer, September 2010

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

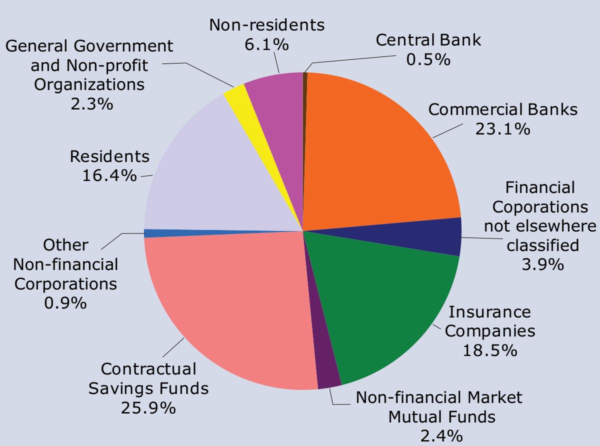
— = not applicable, FCY = foreign currency, LCY = local currency.
Source: Bloomberg LP.

Investor Profile

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

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

Figure 2: LCY Government Bonds Investor Profile, September 2010



LCY = local currency.
Source: Bank of Thailand.

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

Rating Changes

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

Table 3: Selected Sovereign Ratings and Outlook for Thailand

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

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

Policy, Institutional, and Regulatory Developments

Finance Ministry Relaxes Capital Outflow Controls

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

Thai Cabinet Approves a 15% Tax on Bonds

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

BOT Relaxes Regulations on Foreign Exchange Transactions

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

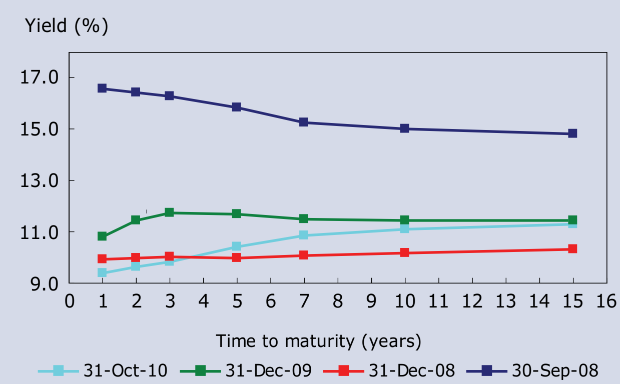
Viet Nam—Update

Yield Movements

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

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

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



LCY = local currency.
Source: Bloomberg LP.

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

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

Size and Composition

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

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

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

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

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

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

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

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

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

Table 2: Top 10 Corporate Issuers, September 2010

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

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

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

Rating Changes

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

Table 3: Selected Sovereign Ratings and Outlook for Viet Nam

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

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

Policy, Institutional, and Regulatory Developments

Limited Liability Companies To Issue Bonds

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

Fees on Corporate Bonds To Be Cut by 50%

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

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

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

Asia Bond Monitor November 2010

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.

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: 1.8 billion people who live on less than $2 a day, with 903 million struggling on less than $1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

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