Asia Bond Monitor Executive Summary

Global investment sentiment recovered and financial conditions in emerging East Asia improved amid monetary easing and fiscal stimulus that softened the impact of the coronavirus disease (COVID-19) pandemic.

From 15 June to 11 September, 2-year and 10-year local currency (LCY) government bond yields in most emerging East Asian markets declined on the back of accommodative monetary policies and weakening economic growth across the region.[1]

The improved sentiment led to gains in equity markets and narrowed credit spreads in most emerging East Asian economies during the review period. Most regional currencies also strengthened against the United States (US) dollar. However, trends in foreign investor holdings were mixed.

Despite improved sentiment, risk appetite has not fully recovered to pre-pandemic levels. Regional equity indexes were 11.0% lower on 11 September compared with 2 January, on average, while credit spreads were up an average of 16 basis points. Risks remain tilted to the downside. The economic impact of the pandemic may be deeper and more persistent than initially expected. The worsening of the COVID-19 outbreak and/or it lasting longer than expected is the biggest risk factor to the projections. Other risks include heightened social unrest due to the economic impact of the pandemic, as well as ongoing trade tensions between the People's Republic of China (PRC) and the US.

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LCY bonds in emerging East Asia reached USD17.2 trillion at the end of June. The market expanded by 5.0% quarter-on-quarter (q-o-q) and 15.5% year-on-year (y-o-y) in the second quarter (Q2) of 2020, accelerating from growth of 4.2% q-o-q and 14.0% y-o-y in the first quarter of 2020.

Government bonds stood at USD10.5 trillion and accounted for 60.8% of the region's aggregate bond stock at the end of June, while corporate bonds reached USD6.7 trillion, or 39.2% of the total.

The PRC remained home to the region's largest bond market at the end of June, accounting for 76.6% of emerging East Asia's total bond stock. The PRC was followed by the Republic of Korea with 12.3%. Members of the Association of Southeast Asian Nations (ASEAN) had a collective share of 9.3%.[2]

The size of emerging East Asia's LCY bonds as a share of regional gross domestic product climbed to 91.6% at the end of June from 87.8% at the end of March and 81.5% at the end of June 2019. The uptick was due to the large amount of funding needed to fight the pandemic and mitigate its impact.

LCY bond issuance in the region climbed to USD2.0 trillion in Q2 2020, growing by 21.3% q-o-q and 32.0% y-o-y. Issuance of government bonds grew 29.1% q-o-q and 27.8% y-o-y in Q2 2020, and issuance of corporate bonds rose 11.7% q-o-q and 38.5% y-o-y.

The September issue of the *Asia Bond Monitor* includes four special discussion boxes. One box reviews recent trends and changes in the investor profile in LCY bond markets in Asia. Another box discusses the increased use of digital payment amid the COVID-19 pandemic. Two boxes examine environmental, social, and governance (ESG) investments and their resilience during the COVID-19 era.

Box 1: Asian Bond Markets—Recent Trends and Developments

This box analyzes trends and changes in the investor profile in emerging East Asian bond markets since January 2020. The bond spreads of select emerging East Asian markets widened amid March market turmoil,

[1] Emerging East Asia comprises the People's Republic of China; Hong Kong, China; Indonesia; the Republic of Korea; Malaysia; the Philippines; Singapore; Thailand; and Viet Nam.
[2] LCY bond statistics for the Association of Southeast Asian Nations include the markets of Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam.

which saw large outflows of portfolio investments and rapid declines in foreign holdings in LCY bond markets. Domestic institutions such as banks increased their holdings of LCY bonds as foreign investors retreated in the first quarter of 2020. To maintain financial stability and mitigate the impact of COVID-19, the region's central banks cut interest rates, which contributed to the improved financial conditions beginning in April. Regional bond markets recovered in Q2 2020. Portfolio investment flows stabilized, bond spreads narrowed, equity markets rose, and currencies appreciated. The box also notes that bond markets in emerging East Asia continue to expand to help meet the funding needs of both the public and private sectors as they try to contain the epidemic and mitigate its impact.

Box 2: Contactless Payment in Post-COVID Asia

This box discusses the increasing use and development of contactless payment technology in Asia as a result of the COVID-19 pandemic. While Asia still lags behind the global average, the use of digital payment is growing rapidly across the region. The box highlights the role of economic and health shocks in triggering the development of digital payment. The region's economies must build the necessary infrastructure to further advance contactless payment technologies, including robust identification systems, reliable internet networks, secure financial services, and strong regulatory frameworks.

Box 3: Environmental, Social, and Governance Investment Growth amid the COVID-19 Crisis

This box examines the growth of ESG investment in Asia since the onset of COVID-19. Data show that cumulative ESG investment in mutual funds expanded between December 2019 and May 2020. Using stock market data from Q1 2020 for the top 100 Japanese-listed companies, the study found that firms with the highest ESG ratings had the smallest average decline and the most stable stock prices. This finding points to the resilience of ESG investment amid COVID-19. The box concludes with a discussion of the remaining challenges in promoting ESG investment in Asia.

Box 4: Is Green the New Gold? ESG Resilience during the COVID-19 Crisis

This box discusses the resilience of ESG funds during the COVID-19 crisis, which have thus far outperformed equity markets and exchange-traded funds globally. The superior performance of ESG funds can be partly attributed to their exposure to sectors that are less impacted by containment and social distancing measures. Amid the crisis, investment has continued to flow to ESG funds, possibly due to (i) investors perceiving that ESG funds are "pandemic-proof"; (ii) investors tending to hold their ESG investments even during a crisis, as they potentially derive utility from the act of investing responsibly; and (iii) ESG funds benefiting from investor preference for a safe-haven investment.