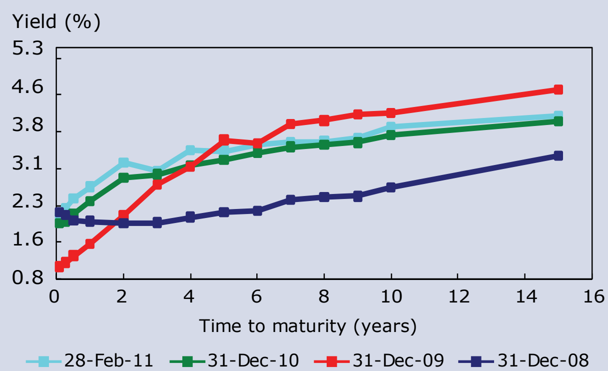
Thailand—Update

Yield Movements

Yields on Thai government bonds shifted downward in 2010 along most of the government bond curve, except at the very short-end. Between end-December and end-February 2011, however, Thai government bond yields shifted upward throughout the length of the curve **(Figure 1)**. Yields had climbed the most from the short-end to the belly of the curve, with 1-, 2- and 4-year maturities rising 30, 30, and 31 basis points, respectively. Yields along the rest of the belly of the curve rose between 10 and 20 basis points, except for the 8-year tenor, which increased 7 basis points. At the long-end of the curve, yields for the 9-, 10-, and 15-year maturities rose 10, 17, and 10 basis points, respectively. The yield spread between 2- and 10-year maturities narrowed to 73 basis points as of end-February from a spread of 86 basis points at end-December.

The Bank of Thailand (BOT) raised its 1-day repurchase rate by another 25 basis points to 2.50% on 9 March. The rate hike came on the back of increased inflationary pressures fueled by a surge in oil and commodity prices. This is the second time the BOT raised its policy rate by 25 basis points this year. On 12 January, the BOT raised its 1-day repurchase rate by 25 basis points to 2.25%. The BOT expects increases in the headline and core inflation rates to accompany sharply rising oil and commodity prices. Commercial banks responded to the policy rate hike by increasing their deposit and loan rates, while most market observers are expecting the BOT to raise its policy rate further in 2011. Thailand's consumer price inflation eased to 2.9% year-on-year (y-o-y) in February from 3.0% in January, as government subsidies helped curb food and fuel price increases. On a month-on-month (m-o-m) basis, consumer prices rose by 0.4%, partly on the back of fresh food price hikes. The Thai Ministry of Commerce sees consumer price inflation rising somewhat to between 3.2% and 3.7% in 2011 as price caps on some food staples, including eggs and sugar, will expire at the end of March.

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



LCY = local currency.
Source: Bloomberg LP.

Thailand's gross domestic product (GDP) growth continued to ease in 4Q10, slowing to a rate of 3.8% y-o-y from 6.6% in 3Q10. Thailand's economy recorded GDP growth rates of 12.0% in 1Q10 and 9.2% in 2Q10. For the whole of 2010, Thailand's GDP expanded 7.8% y-o-y, its strongest annual expansion in 15 years, on the back of solid exports and consumer spending. However, growth is expected to slow to 3.0%–5.0% in 2011 due to the strengthening baht, fluctuating oil prices, and the impact of floods on agricultural output.

Size and Composition

As of end-December, the amount of Thailand's local currency (LCY) bonds outstanding had expanded 14.4% y-o-y to THB6.8 trillion (USD225 billion), which was slightly higher than 14.2% y-o-y growth as of end-September **(Table 1)**. Total LCY bonds outstanding rose 2.7% quarter-on-quarter (q-o-q) in 4Q10, while decreasing 0.3% on a month-on-month (m-o-m) basis in December.

The outstanding stock of Thai government bonds amounted to THB5.5 trillion at end-December. Growth on a y-o-y basis was 16.7% at end-

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

	Amount (billion)								**Growth Rate** (%)						
	Sep-10		**Oct-10**		**Nov-10**		**Dec-10**		**Sep-10**		**Oct-10**	**Nov-10**	**Dec-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	6,577	217	6,680	223	6,776	224	6,753	225	14.2	2.5	1.6	1.4	14.4	2.7	(0.3)
Government	5,350	176	5,459	182	5,531	183	5,499	183	17.3	3.3	2.0	1.3	16.7	2.8	(0.6)
Treasury Bonds	2,597	86	2,583	86	2,599	86	2,595	86	9.1	1.2	(0.5)	0.6	9.9	(0.1)	(0.2)
Central Bank Bonds	2,250	74	2,378	79	2,436	81	2,412	80	36.3	7.3	5.7	2.5	32.5	7.2	(1.0)
State-Owned Enterprise & Other Bonds	503	17	499	17	496	16	493	16	(5.2)	(2.2)	(0.9)	(0.6)	(7.1)	(2.1)	(0.6)
Corporate	1,227	40	1,221	41	1,244	41	1,253	42	2.6	(1.2)	(0.4)	1.9	5.3	2.2	0.7

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. 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 (BOT) and Bloomberg LP.

December, which was down from 17.3% y-o-y growth at end-September. BOT bonds had the highest annual growth rate in 2010 among all categories of government bonds at 32.5%, followed by treasury bonds with an annual growth rate of 9.9%. State-owned enterprise and other bonds, however, declined 7.1% in 2010.

New issuance of government bonds climbed 57.9% y-o-y to THB3.0 trillion in 4Q10, compared with 11.7% y-o-y growth in 3Q10. The BOT accounted for 96% of total government issuance in 4Q10, amounting to THB2.9 trillion, which was up 74.5% y-o-y. BOT bills accounted for a 67% share of total BOT issuance in 4Q10. New issuance from the central government and state-owned enterprises, however, declined 47.8% (THB126 billion) and 76.1% (THB3.6 billion), respectively, on a y-o-y basis in 4Q10.

In February, the Thai Ministry of Finance announced the postponement of its planned issuance of THB100 billion of savings bonds. The reason given was that Thailand's considerable fiscal reserves obviated the need to issue more debt. According to the Public Debt Management Office (PDMO), the bonds would have had maturities of 7–12 years, with the proceeds being used to restructure the national debt.

The Thai Finance Ministry issued its longest-dated security ever in February—a 50-year government bond amounting to THB3.5 billion. Thailand is the fourth country to issue 50-year bonds after the United Kingdom, France, and the People's Republic of China. The Thai government also plans to issue a series of 50-year bonds in 3Q11 and 4Q11 in a range of between THB3 billion and THB4 billion. Proceeds will help cover the budget deficit and a portion will be used to refinance existing government debt. As of end-January, Thailand's international reserves stood at USD170 billion and had remained above USD100 billion since September 2008. Thailand expects to run a budget deficit of THB350 billion, or not more than 4.0% of GDP, for fiscal year 2012 (ending on 30 September), an improvement from a THB420 billion deficit in fiscal year 2011. The PDMO announced that it plans to focus on long-term bonds with maturities of 5, 7, 10, 15, and 30 years, together with the issuance of 50-year bonds and inflation-linked bonds, as part of the government's target to achieve a balanced budget in 5 years.

Corporate bonds outstanding stood at THB1.3 trillion (USD42 billion) as of end-December, up 5.3% y-o-y. Total corporate bonds outstanding rose 2.2% q-o-q and 0.7% m-o-m, respectively. New issuance in 4Q10 reached THB259 billion, an increase of 0.7% y-o-y and 15.4% quarter-on-quarter (q-o-q). Notable THB-denominated corporate bond issues for 4Q10 included THB14 billion from PTT PCL, THB8 billion from Charoen Pokphand Foods, and THB7 billion from Don Muang Tollway. Maturities for these bonds ranged between 3 and 10 years.

In October, the Ministry of Finance approved three foreign entities to issue THB-denominated bonds prior to 31 March. Central American Bank for Economic Integration (CABEI), ING Bank, and the Export–Import Bank of Korea (KEXIM) have received approval to issue bonds of THB4.0 million, THB10.0 million, and THB8.0 million, respectively. In February, CABEI offered a total of THB3.1 billion in three tranches. CABEI priced its 3-year bonds at 3.85%, 5-year bonds at 4.51%, and 10-year bonds at 4.88%. In early February, the Export–Import Bank of Korea raised THB2.2 billion by issuing bonds in the Thai market. In January, the Thai Ministry of Finance approved another 10 foreign entities to issue THB-denominated bonds during the period 1 January–30 June 2011. These entities are as follows:

(i) BNP Paribas (THB10 billion)
(ii) Commonwealth Bank of Australia (THB8 billion)
(iii) Citigroup Inc. (THB10 billion)
(iv) Deutsche Bank Aktiengesellschaft (THB6 billion)
(v) Industrial Bank of Korea (THB5 billion)
(vi) International Bank for Reconstruction and Development (THB5 billion)
(vii) Kommunalbanken AS (THB4 billion)
(viii) Korea Development Bank (THB8 billion)
(ix) Swedish Export Credit Corporation (THB5 billion)
(x) Westpac Banking Corporation (THB6 billion)

In November, Thailand's largest oil and gas company, PTT, raised THB4 billion of 100-year bonds, the first-ever long-tenor paper in Thai bond market history. The bonds will mature in 2110 and were priced at 5.9%. The issuance attracted five insurance companies, which took 90% of the deal, while the remainder of the bonds were purchased by a private fund and a few high net-worth individuals. The century bonds have a put option on their 50th and 75th years.

PTT also sold THB10 billion of 4- and 7-year debentures in November. The 4-year tranche was priced with a coupon of 3.2%, while the 7-year tranche was priced at 3.7%. Both were sold to retail investors. In November, PTT became the first Thai group to tap the Islamic capital market with its issuance of a MYR600 million serial *sukuk.* The Islamic bonds were sold by PTT's subsidiary, Trans Thai–Malaysia (TTM), through a special purpose vehicle called TTM *Sukuk* and with 5–15 year tenors.

The top 30 corporate issuers in Thailand at end-December were mainly from the financial and consumer sectors, which together accounted for 73% of total corporate bonds outstanding **(Table 2)**. The majority of the issuers included privately-owned corporations and listed companies. PTT ranked first as the top LCY corporate issuer, with total LCY bonds outstanding of THB191.5 billion as of end-December.

Foreign Currency Bonds

As of end-December, the amount of total foreign currency (FCY) bonds outstanding in Thailand stood at USD7.7 billion, of which private corporations had issued 43%, while financial institutions and the government had issued 39% and 19%, respectively. The majority of FCY bonds outstanding were issued in US dollars (85%), with Japanese yen accounting for the rest. In 4Q10, total FCY bond issuance amounted to

Table 2: Top 30 Issuers of LCY Corporate Bonds in Thailand (as of 31 December 2010)

Issuer	Bonds Outstanding		State-Owned	Privately-Owned	Listed Company	Sector
	LCY Bonds (THB billion)	LCY Bonds (USD billion)				
1. PTT PCL	191.5	6.4	Yes	No	Yes	Energy
2. Siam Cement PCL	110.0	3.7	Yes	No	Yes	Diversified
3. Bank of Ayudhya	56.3	1.9	No	Yes	Yes	Financial
4. Krung Thai Bank	55.4	1.8	Yes	No	Yes	Financial
5. PTT Exploration and Production Company	49.0	1.6	Yes	No	Yes	Energy
6. Charoen Pokphand Foods	30.7	1.0	No	Yes	Yes	Consumer
7. Thai Airways International	29.3	1.0	Yes	No	Yes	Consumer
8. Toyota Leasing Thailand	26.7	0.9	No	Yes	No	Consumer
9. Kasikorn Bank	25.1	0.8	No	Yes	Yes	Financial
10. Krungthai Card	24.2	0.8	Yes	No	Yes	Financial
11. DAD SPV Company LTD	24.0	0.8	Yes	No	No	Financial
12. Thai Oil	20.8	0.7	Yes	No	Yes	Energy
13. PTT Chemical	20.4	0.7	Yes	No	Yes	Basic Materials
14. Siam Commercial Bank	20.0	0.7	No	Yes	Yes	Financial
15. Advanced Info Service	19.5	0.6	No	Yes	Yes	Communications
16. Thanachart Bank	18.0	0.6	No	Yes	No	Financial
17. TMB Bank	17.3	0.6	No	Yes	Yes	Financial
18. Bangkok Expressway	15.1	0.5	No	Yes	Yes	Consumer
19. Glow Energy	15.0	0.5	No	Yes	Yes	Utilities
20. PTT Aromatics and Refining	15.0	0.5	Yes	No	Yes	Energy
21. True Corporation	14.9	0.5	No	Yes	Yes	Communications
22. Ayudhya Capital Auto Lease	14.7	0.5	No	Yes	No	Financial
23. Kiatnakin Bank	14.3	0.5	No	Yes	Yes	Financial
24. Quality Houses	14.0	0.5	No	Yes	Yes	Consumer
25. Thanachart Capital	13.5	0.4	No	Yes	Yes	Financial
26. Bangkok Mass Transit System	12.0	0.4	Yes	Yes	No	Industrial
27. CH Karnchang Public Company	12.0	0.4	No	Yes	Yes	Industrial
28. Land and Houses	11.0	0.4	No	Yes	Yes	Consumer
29. Minor International	10.9	0.4	No	Yes	Yes	Consumer
30. Central Pattana	10.7	0.4	No	Yes	Yes	Financial
Total Top 30 LCY Corporate Issuers	**911.3**	**30.3**				
Total LCY Corporate Bonds	**1,253.4**	**41.7**				
Top 30 as % of Total LCY Corporate Bonds	**72.7%**	**72.7%**				

LCY = local currency.
Source: Bloomberg LP.

USD1.5 billion, including Bangkok Bank's issuance of USD1.2 billion of 5- and 10-year bonds in the offshore bond market. Meanwhile, the Export–Import Bank of Thailand issued a total of USD250 million of 4- and 6-year bonds in 4Q10.

Investor Profile

Commercial banks remained the largest holder of Thai government bonds with a total of THB598.5 billion as of end-December **(Figure 2)**. However, commercial banks' total share decreased to 23.1% in December 2010 from 25.7% in December 2009. Contractual savings funds were the second largest holder of government bonds with a 22.6% share in December 2010, down from 25.3% from a year earlier. Insurance companies were in the third spot, increasing their share to 20.4% in December 2010 from 17.5% a year earlier. Thai residents had a share of 16.3%, followed by nonresidents (7.2%), financial corporations "not elsewhere classified" (3.1%), general government and non-profit organizations (2.3%), and the central bank (2.0%). Finally, non-financial market mutual funds had a 1.9% share, while other non-financial corporations held a 1.0% share.

Foreign holdings of Thai government bonds stood at THB187.5 billion as of end-December, an increase of 145.7% y-o-y and 19.1% q-o-q.

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."

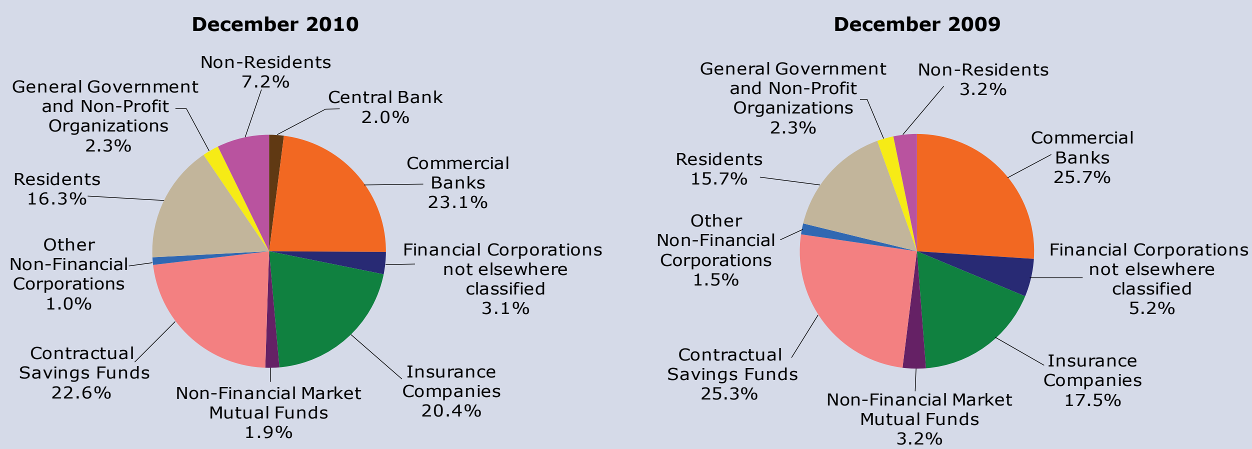
On 9 December, Standard & Poor's (S&P) raised its credit rating outlook for Thailand to stable from negative. According to S&P, the decision for the upgrade was based on Thailand's low level of

Table 3: Selected Sovereign Ratings and Outlook for Thailand

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

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

Figure 2: LCY Government Bonds Investor Profile



LCY = local currency.
Source: Bank of Thailand.

government debt and prudent fiscal policies. S&P affirmed Thailand's BBB+/A-2 foreign currency rating and A-/A-2 local currency sovereign credit ratings.

Policy, Institutional, and Regulatory Developments

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 FCY 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 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 the Export–Import Bank of Thailand—are also 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 FX Transactions

The BOT relaxed foreign exchange (FX) regulations to increase the flexibility of Thai businesses in managing FX risk. 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 FX 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.

Thai Financial Regulators to Strengthen Bond Information

In December, the BOT signed an agreement with the Securities and Exchange Commission (SEC), Stock Exchange of Thailand (SET), Thai Bond Market Association, and PDMO to create the Thailand Financial Instruments Information Center (TFIIC). TFIIC is part of the Thai government's 5-year capital market master plan, which aims to collect information on financial instruments by related sources, share the information, and provide linkages among related agencies.

Revenue Department of Thailand to Slash Corporate Income Tax

In January, the Revenue Department of Thailand considered slashing the corporate income tax rate to 18% from the current 30%. The tax department is preparing to restructure taxes in order to boost Thailand's competitiveness in advance of Thailand's membership in the Association of Southeast Asian Nations (ASEAN) Economic Community (AEC) in 2015. The AEC will permit the free movement of goods, investment, and labor between member countries without the imposition of taxes or other barriers.

Thailand to Allow New Securities Exchanges

In February, the SEC announced that a law is being drafted to allow new securities exchanges to compete with the SET, with the aim of lowering the cost of raising capital for domestic companies. SET, a wholly state-owned bourse, currently has a monopoly on equity and financial derivatives trading.