

Keynote Address: Asian Bond Monitor Launch 2011**Tuesday 29th November, ADBI Office, Tokyo****Dr. Bandid Nijathaworn****Chairman, the Thai Bond Market Association**

First, let me thank the ADB's Office of Regional Economic Integration for inviting me to give today's opening keynote address. My congratulations go to the Office for the launching of Asia Bond Monitor 2011.

In the past five years, notwithstanding the impact of the global financial crisis, the growth and the resilience of local bond markets in Asia have been impressive, with the local currency bond market expanding by about 13 percent annually. This growth has provided the region with an important source of funding, as well as being a pillar for financial stability in the wake of a severe credit crunch that occurred at the onset of the recent global financial crisis. It can be said that, since the Asian crisis in the late 1990s, the expansion of the region's bond markets has given Asia a much more balanced financial system, with the bond market becoming a source of financial intermediation no less important than the credit or the equity markets. In this context, it is welcoming to have an institution like the Office of Regional Economic Integration of the ADB providing a regular update of the bond markets in the region.

This year 2011 has been another important and eventful year for Asian bond market, especially in the context of the global economy and the implications for financial markets.

Throughout this year, policy uncertainty has been a key theme that dominates investment decision and fund flows. Most importantly, the sovereign debt problems in the highly-indebted economies of Europe and the concern about fiscal sustainability in the US have heightened uncertainty in financial markets, contributed to a weakening of private sector confidence, and pulled back the momentum of recovery in the advanced economies. At this time, policy uncertainty still remains while latest economic data are not encouraging in the way of continued recovery in the advanced economies. The challenge to policymakers, therefore, has become more difficult with the economic prospects looking to deteriorate further.

In this environment, financial markets have responded to the uncertainty in a most traditional way. The yields and bond spreads of the Euro area sovereign bonds have increased, notwithstanding the efforts to enlarge the funding capacity of the European Financial Stability Fund that has been announced. For Asia, the sovereign debt problem has affected the region in three ways: first, a lower volume of world trade that affects the region's exports; second, a more difficult international financing conditions reflected in higher funding costs and more limited availability of trade finance; and third, more volatile capital flows as investors' risk appetite is

continually shifting. Bond markets in emerging market Asia have also been affected by the volatility as the spreads on their international bonds widen and the growth of many bond markets has slowed compared to the previous years. In the case of Thailand, the bond market grew by 5.6 percent in the first nine months of this year, lower than the past five years' average growth of 12 per cent.

In the near term, as long as policy uncertainty remains, volatility in financial markets will likely persist and Asia will need to continue to rely on its prudent macroeconomic management and good fundamentals to cope with the volatility and the impact on the regional economies. The good fundamentals of Asia include the region's high rates of saving, the strong international reserve positions, and the strength and the resilience of the region's banks and the bond markets. So far, the region seems to have managed well on this front.

As I alluded to earlier, since the financial crisis of the late 1990s, development of financial markets has been an important policy issue in Asia, especially in East Asia. A robust and resilient financial sector is seen as key to sustaining the region's economic growth and to the strengthening of the region's abilities to withstand global shocks. To this end, many important initiatives have been launched by governments in the region to develop financial markets. For the bond market, the most well-known initiatives have been the ABMI or the Asian Bond Market Initiatives that aim to foster

common regional market standards and practices, the ABF I and II projects that introduce the region's US dollar and local currency denominated sovereign bonds as a distinct asset class, and more recently the setting up of the credit guarantee investment facility to promote long-term investment through the use of long-term local currency corporate bond.

Asian bond markets have responded well to those initiatives, in the form of a rapid market growth driven by local demand to diversify savings and by foreign demand to diversify investment. An important point to note is that, while these initiatives have been put up by governments, the momentum and the development in the region's bond markets have largely been market-driven. This is evidenced in a proliferation of new bond products that have emerged to serve the needs of individual economies. I am referring here to the growths of the RMB denominated international bond in Hong Kong, Islamic bond in Malaysia, and inflation-linked bond and the introduction of 50 year government bond in Thailand.

As the global economy moves into a post-crisis phase, we again are seeing a resurgence of interest on Asian financial market development and integration. The context this time is different, however. The context this time is about rebalancing of global growth and the role that Asian financial markets can play to promote domestic demand-driven growth in the region. Specifically, a more robust and well-developed financial market in Asia will help improve the capacity of Asian financial institutions to translate Asian

savings into Asian investment, while a more integrated Asian financial markets will encourage more cross-border fund flows within Asia to support intra-regional trade and investment, and hence sustaining growth of the region's domestic demand.

At this time, economic and financial developments in Asia are pointing to changes in this direction. On the trade side, closer integration of goods markets in Asia is clearly happening with intra-regional trade now accounting for a larger share of Asia's total trade. In the case of Thailand, exports to ASEAN now accounts for 23 percent of total Thai exports, a share higher than the combined share of Thai exports to the US and the EU.

On the financial side, empirical evidence in terms of price and quantity measures correlation also shows that Asian financial markets have become more integrated both globally and regionally. The degree and pace of financial integration, however, lags behind those of trade integration.

Specific to the bond market, a recent study by the ADB, co-authored by Cyn Yong Park and Jong-Wha Lee, shows that correlations across Asian local currency bond returns have increased in the past ten years, suggesting some progress on bond market integration. Sharp differences, however, do exist between groups of market in the region according to their degree of development. For example, ASEAN markets have more limited integration compared to the more developed Asian markets of Japan, Hong Kong, China, Korea, and Singapore. Also, the more developed Asian markets

tend to exhibit greater correlation amongst themselves than with the smaller Asian bond markets. All said, the degree of regional bond market correlation is improving but lags substantially behind correlation observed in the region's equity market.

These findings are very useful for understanding the current state of play in the region's bond market, and for the planning of the next steps in bond market development and integration. Low correlation does offer ASEAN bond markets an opportunity for market diversification within itself. To promote such diversification, more will have to be done by the individual bond market on market infrastructure, liquidity, product range, hedging instruments, and investor information. More importantly, these efforts at the market level will need to be supported by policy at the regional level to develop a common platform of market conduct and regulation, as well as an efficient regional clearing and payments system, to reduce transaction costs and assist a greater flow of cross border investment.

This thinking essentially reflects the approach that we are taking in Thailand in our bond market development where the Thai Bond Market Association is playing an important coordinating role. Thai bond market has grown rapidly in the last ten years with assets now totaling 70 percent of GDP. The market has large shares of sovereign and the Bank of Thailand issues, accounting for about 81 per cent of the market, while on the buy side foreign investor accounts for about 6 percent of the total outstanding. Our

current plan to develop the bond market focuses on enhancing liquidity, promoting market for corporate bond, and improving investor information and education. All this will help the Thai bond market to play a greater role in financial intermediation in Thailand while contributing to building greater resilience to the region's financial system. We are also taking active part in the region's bond market forum and policy discussion, and see today's launching of the Asia Bond Monitor as an important event for bond markets in Asia.

In closing, it has been a pleasure to share with you my views on the global economy and on the region's bond markets in this brief address. Again, I want to thank the ADB and the Office of Regional Economic Integration for the invitation, and I look forward to the presentation on the launching of Asia Bond Monitor 2011 and the discussion to come.

Thank you.