

Eddie Yue: Developing local-currency bond markets in Asia

Statement by Mr Eddie Yue, Deputy Chief Executive of the Hong Kong Monetary Authority and Head of the Delegation of Hong Kong, at the 45th Asian Development Bank Annual Meeting, Manila, 4 May 2012.

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I would like to thank the Government of the Philippines for hosting the 45th Annual Meeting of the Asian Development Bank (ADB). I would also like to congratulate ADB on the successful conclusion of the Tenth Replenishment of the Asian Development Fund (ADF XI), which would provide critical resources to ADB to further its work in poverty reduction in Asia.

The global economy has shown signs of improvement in 2012 following a marked slowdown amid the intensification of the euro zone debt crisis in the latter part of last year. Nevertheless, significant downside risks remain, with the euro zone debt crisis yet to be fully resolved and rising oil prices adding further uncertainty to the recovery outlook.

Asia has remained resilient so far, in large part attributable to the reforms taken by regional economies over the years to strengthen economic fundamentals, improve fiscal discipline and enhance the resilience of their financial systems since the Asia financial crisis. Nevertheless, the region is not immune from the lingering fragility in the global environment. To date, the deleveraging by European banks has not caused significant short-term credit tightening in Asia, with banks in the region and elsewhere having stepped in to fill the gap left by European banks. However, the ability of Asian banks to continue to take up the slack could be constrained by the already high loan-to-deposit ratio and limited access to US dollar funding. More importantly, it is doubtful whether these non-European banks would have the appetite to take up long-term project and infrastructure financing, which is a specialised business traditionally dominated by the European banks.

Any cutback in infrastructure financing could have serious repercussions for developing Asia, which has a strong need to build and upgrade infrastructure networks to promote sustainable growth, create employment opportunities and boost competitiveness. ADB estimates that Asia requires as much as US\$8.3 trillion in overall infrastructure investment between 2010 and 2020, with an average of US\$750 billion in annual infrastructure spending. It is therefore vital to further develop the capital markets in Asia, in particular the local-currency bond markets, to effectively channel the region's vast savings to meet its huge demand for infrastructure financing.

Asian governments have been making efforts to develop the bond markets. At the national level, initiatives such as consolidation of issuance in a few benchmark maturities and development of interdealer markets have helped increase liquidity and improve reliability of yield curves in a number of jurisdictions. Meanwhile, collaborative efforts are being made in regional forums. A notable example is ASEAN+3's Asian Bond Markets Initiative with the strong support from ADB. The Initiative has been looking into both demand and supply side issues pertinent to the development of the bond markets. Under the Initiative, a Credit Guarantee and Investment Facility has been set up as a Trust Fund of ADB to provide credit guarantee to allow investment-rated issuers to issue local currency bonds in ASEAN+3 markets. Another good example is the Asian Bond Fund project of the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP). The launch of the ABF funds introduced to the region's bond markets a new low-cost and efficient product in the form of passively-managed index bond funds and helped catalyse infrastructure, tax and regulatory reforms at both the regional and domestic levels. The Hong Kong Monetary Authority took an active part in the design and implementation of the project.

These efforts, along with the rapid economic growth and improved investment climate, have contributed to considerable growth in the local currency bond markets. According to ADB, the

amount of local currency bonds outstanding in emerging East Asia increased by more than ten folds from US\$528 billion prior to the Asian financial crisis in 1996 to US\$5,479 billion in 2011. We have also seen the interesting development of offshore bond markets. In Hong Kong, the RMB bond market has grown substantially since the first issuance in 2007, with total issuance increased to over RMB 100 billion in 2011 from RMB 10 billion in 2007. The range of issuers has also diversified, from predominantly the sovereign and banks in China to multinational companies and international financial institutions. Among the latter, ADB was the first to issue RMB bond in Hong Kong in October 2010. A number of multilateral agencies also issued RMB bonds in Hong Kong after ADB's debut issue. With the rapid growth of China's cross-border trade and investment flows, the offshore RMB bond market would provide a useful financing platform and facilitate the greater use of RMB in these transactions, thereby minimising the currency risk associated with the use of a third currency.

Notwithstanding the encouraging developments over the past years, the capacity of the regional bond markets is still limited compared with the huge infrastructure and other financing needs of the region, resulting in heavy reliance on bank financing. Much work still needs to be done, including but not limited to expanding the issuer and investor types, gradual liberalisation of barriers to entry of non-resident investors, promoting financial infrastructure linkages, improving corporate disclosure and transparency, more standardisation in legal and governance terms, to name a few. Policymakers will have a key role to play in facilitating market developments and removing market impediments in the process. And we hope to see ADB, the region's long-standing partner in promoting bond market development, to further its efforts and cooperation with governments in the region on this front.

Thank you.