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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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Thailand—Update

Yield Movements

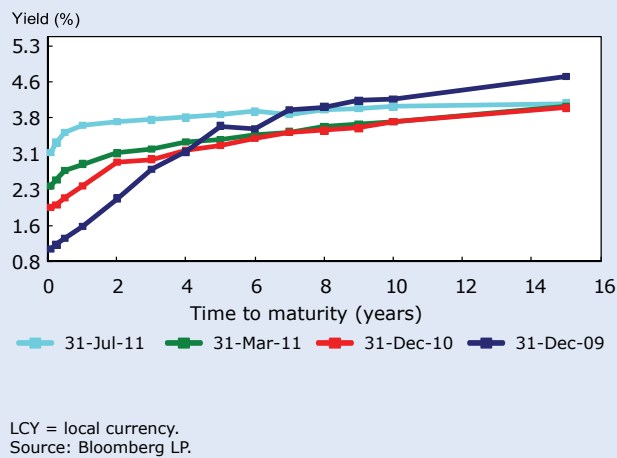
Thailand's government bond yield curve flattened between end-December 2010 and end-July (Figure 1). Yields at the short-end of the curve increased as much as 137 basis points (bps) over concerns about inflationary pressures and a policy rate hike. Government bond yields from the belly to the long-end of the curve rose as much as 55 bps, while the 15-year maturity rose only 9 bps. The yield spread between 2- and 10-year maturities narrowed to 32 bps at end-July from a spread of 65 bps at end-March.

The Bank of Thailand (BOT) raised its 1-day repurchase rate 25 bps to 3.25% at its Monetary Policy Committee (MPC) meeting on 13 July, reflecting concerns over increased inflationary pressures fueled by higher food and oil prices. BOT's stance also reflected concerns about the wage hike and fiscal spending pledges of Prime Minister Yingluck Shinawatra. The latest increase marked the fifth time that BOT has raised its policy rate by 25 bps since January.

Thailand's consumer price inflation accelerated to a 32-month high of 4.2% year-on-year (y-o-y) in May, driven mainly by higher food prices. In June, however, consumer price inflation declined slightly to 4.06% y-o-y before rising incrementally to 4.08% in July. Core inflation, which excludes energy and fresh food prices, climbed to 2.59% y-o-y in July from 2.55% in June. The Commerce Ministry still expects consumer price inflation to average between 3.2% and 3.7% for full-year 2011.

Thailand's real gross domestic product (GDP) rose 3.0% y-o-y in 1Q11 on rapid growth in exports and private investment, expansion in the tourism sector, and rising farm output. According to the National Economic and Social Development Board (NESBD), Thai exports rose 27.4% y-o-y in 1Q11, mainly driven by exports of jewelry, vehicles, parts and accessories, electrical appliances, and rubber. The tourism sector registered a total

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



of 5.4 million inbound tourists in 1Q11 for an increase of 15.0% y-o-y. Private investment grew 12.6% y-o-y in 1Q11, mainly due to an expansion in machinery and construction investment. The agricultural sector expanded 6.7% y-o-y due to increased farm output. Meanwhile the unemployment rate declined to 0.8%. The NESBD expects the Thai economy to expand between 3.5% and 4.0% in 2011.

Size and Composition

As of end-June, the size of Thailand's local currency (LCY) bond market had expanded 6.2% y-o-y to THB6.8 trillion (US\$222 billion), following 10.3% growth as of end-March (Table 1). On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding posted marginal growth of 0.1% in 2Q11, following a 0.9% increase in 1Q11. The slowdown in growth reflected lower issuance of central government bonds and zero issuance of treasury bills since the beginning of the year.

Total LCY government bonds outstanding rose 5.6% y-o-y to THB5.5 trillion as of end-June, or only about one-half of the 10.3% increase recorded at the end of 1Q11. BOT bonds expanded

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

	Amount (billion)						Growth Rate (%)										
	Mar-11		Apr-11		May-11		Jun-11		Mar-11		Apr-11		May-11		Jun-11		
	THB	US\$	THB	US\$	THB	US\$	THB	US\$	THB	US\$	THB	US\$	THB	US\$	THB	US\$	
Total	6,813.9	225.0	6,839.0	228.9	6,827.9	225.2	6,819.8	221.9	10.3	10.3	0.9	0.9	0.4	(0.2)	6.2	0.1	(0.1)
Government	5,476.8	180.9	5,481.2	183.4	5,452.7	179.8	5,466.2	177.9	10.3	10.3	(0.4)	(0.4)	0.1	(0.5)	5.6	(0.2)	0.2
Treasury Bonds	2,546.6	84.1	2,576.2	86.2	2,602.3	85.8	2,557.3	83.2	3.1	3.1	(1.9)	(1.9)	1.2	1.0	(0.4)	0.4	(1.7)
Central Bank Bonds	2,447.9	80.8	2,424.6	81.1	2,369.1	78.1	2,426.5	79.0	24.1	24.1	1.5	1.5	(1.0)	(2.3)	15.7	(0.9)	2.4
State-Owned Enterprise and Other Bonds	482.3	15.9	480.4	16.1	481.4	15.9	482.4	15.7	(7.4)	(7.4)	(2.1)	(2.1)	(0.4)	0.2	(6.1)	0.03	0.2
Corporate	1,337.1	44.2	1,357.9	45.4	1,375.2	45.4	1,353.6	44.1	10.2	10.2	6.7	6.7	1.6	1.3	9.0	1.2	(1.6)

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 end-of-period LCY-US\$ rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.

Sources: Bank of Thailand (BOT) and Bloomberg LP.

the most, posting an annual growth rate of 15.7%. Treasury bonds, however, dropped 0.4% y-o-y, following 3.1% growth in 1Q11. The decline in state-owned enterprise bonds slightly improved to -6.1% y-o-y as of end-June from -7.4% as of end-March.

New issuance of government bonds rose 26.3% y-o-y to THB2.9 trillion in 2Q11, while declining 9.7% on a q-o-q basis. BOT bonds once again dominated new issuance, representing 95.7% of total government issuance in 2Q11. BOT bonds grew 42.0% y-o-y while declining 11.0% q-o-q. Bond issuance from state-owned enterprises rose 23.7% y-o-y and 35.5% q-o-q, the majority coming from the Government Housing Bank (THB3.0 billion), Provincial Waterworks Authority (THB2.6 billion), and Provincial Electricity Authority (THB2.3 billion). New issuance from the central government, however, declined 65.7% y-o-y to THB113.8 billion, primarily due to zero issuance of treasury bills in 2Q11.

In February, the Thai Finance Ministry issued its longest-dated security ever—a 50-year government bond amounting to THB3.5 billion. Thailand is the fourth country to issue 50-year bonds, joining the United Kingdom, France, and the People's Republic of China. The Thai government plans to issue a series of 50-year bonds in 3Q11 and 4Q11 worth a total of THB3 billion–THB4 billion. Proceeds will help cover the budget deficit and a portion will be used to refinance existing government debt. Thailand's international reserves stood at US\$180 billion as of end-May and have remained above US\$100 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 2012). This target represents an improvement from a THB420 billion deficit in fiscal year 2011. The Public Debt Management Office (PDMO) announced that it plans to focus on medium- and long-term bonds with maturities of 5, 7, 10, 15, and 30 years, in addition to the 50-year bond and inflation-linked bonds, as part of the government's target to achieve a balanced budget within 5 years.

In July, Thailand's debut sale of its 10-year inflation-linked bonds swelled to THB40 billion (US\$1.3 billion), the top-end of the indicated size range of THB20 billion–THB40 billion. The successful deal came at a coupon of 1.2%, which was also at the higher-end of the unofficial price guidance of 1.00%–1.25%. Foreign investors—asset managers, sovereign wealth funds, insurance companies, and private banks—were the single largest group of buyers. However, the offered amount of THB13 billion for retail investors only drew THB6 billion worth of bids. PDMO attributed the low pick-up to a lack of knowledge about inflation-linked bonds among retail investors. The remaining THB7 billion was allocated to domestic institutional investors. PDMO revealed that it will re-open the bond and has plans to issue in different tenors as well, although it may no longer market the bonds to retail investors. The structure of Thai inflation-linked bonds are similar to the United States (US) Treasury's inflation-protected securities wherein the bond coupon is constant but the principal is indexed to the country's consumer price index and compounded.

LCY corporate bonds outstanding grew 9.0% y-o-y to THB1.4 trillion in 2Q11, a growth rate that was down from 10.2% in 1Q11. On a q-o-q basis, corporate bond growth slowed to 1.2% in 2Q11 from 6.7% in 1Q11. New issuance in 2Q11 increased 9.8% y-o-y to THB302 billion but declined 21.0% on a q-o-q basis.

Notable THB-denominated corporate bond issues in 2Q11 included a THB15.0 billion bond from Siam Cement, THB10.0 billion each from Thanachart Bank and BTS Group, and THB5.5 billion from energy firm Banpu. The maturities of these bonds ranged between 4 and 8 years. Meanwhile, Thailand's largest agribusiness firm Charoen Pokphand Foods issued Thailand's first ever 30-year corporate bond in August worth THB4 billion, following PTT's THB4 billion December 2110 century bond.

In July, Thailand's PDMO permitted five foreign banks to issue THB-denominated bonds up until 31 December. First Gulf Joint Stock Company

plans to issue its debut bond worth THB6 billion, while Credit Agricole Corporate and Investment Bank, ING Bank, and Export–Import Bank of Korea were granted permission to issue THB10 billion each. Meanwhile, Lloyds TSB Bank was given approval to issue bonds worth up to THB6 billion. In addition, the Finance Ministry allowed Australia and New Zealand Banking Group, Hana Bank, and Shinhan Bank to issue THB-denominated bonds between 1 April and 30 September, with an issue size of THB8 billion each.

An increase in the issuance of corporate bonds is likely in the coming months ahead of expected rate hikes. Corporates rated from BBB to A by Tris Rating have recently issued smaller bond sizes with tenors between 3 and 5 years. Phatra Leasing and BSL Leasing have each issued THB500 million, with credit ratings of A- and BBB, respectively. Motor cycle leasing company Thitikorn also issued THB500 million of senior bonds with a rating of A-. In the property sector, Noble Development issued THB1.5 billion of BBB-rated 3-year bonds, while Asian Property Development sold THB1.5 billion bonds with an A- rating.

The top 30 corporate issuers in Thailand accounted for 70% of total LCY corporate bonds outstanding at end-June (**Table 2**). PTT topped the list, with total LCY bonds outstanding of THB180.9 billion. Siam Cement followed with THB110.0 billion. As a group, financial institutions dominated the list of top 30 corporate issuers, followed by consumer and energy firms. About one-third of the list consisted of state-owned enterprises, while the majority of firms were listed on the Stock Exchange of Thailand (SET).

Foreign Currency Bonds

In April, state-owned PTT Exploration and Production, acting through its subsidiary PTT Canada International Finance, sold US\$700 million of 10-year bonds at a coupon of 5.692%. The foreign currency (FCY) deal was one of the rare sole mandates outside of Asia. US-based investors bought 56% of the bonds, while Asian and European investors purchased 30% and

Table 2: Top 30 Issuers of LCY Corporate Bonds in Thailand (as of June 2011)

Issuers	Outstanding Amount		State-Owned	Privately-Owned	Listed Company	Type of Industry
	LCY Bonds (THB billion)	LCY Bonds (US\$ billion)				
1. PTT PCL	180.9	5.9	Yes	No	Yes	Energy
2. Siam Cement PCL	110.0	3.6	Yes	No	Yes	Diversified
3. Krung Thai Bank	75.8	2.5	Yes	No	Yes	Financial
4. PTT Exploration and Production Company	50.0	1.6	Yes	No	Yes	Energy
5. Bank of Ayudhya	47.2	1.5	No	Yes	Yes	Financial
6. Thai Airways International	31.3	1.0	Yes	No	Yes	Consumer
7. Charoen Pokphand Foods	30.7	1.0	No	Yes	Yes	Consumer
8. Kasikorn Bank	28.4	0.9	No	Yes	Yes	Financial
9. Thanachart Bank	28.0	0.9	No	Yes	no	Financial
10. TMB Bank	27.8	0.9	No	Yes	Yes	Financial
11. DAD SPV Company LTD	24.0	0.8	Yes	No	No	Financial
12. Banpu	23.8	0.8	No	Yes	Yes	Energy
13. Toyota Leasing Thailand	21.9	0.7	No	Yes	No	Consumer
14. Krung Thai Card	21.0	0.7	Yes	No	Yes	Financial
15. Thai Oil	20.8	0.7	Yes	No	Yes	Energy
16. PTT Chemical	20.4	0.7	Yes	No	Yes	Basic Materials
17. Siam Commercial Bank	20.0	0.7	No	Yes	Yes	Financial
18. True Corporation	19.6	0.6	No	Yes	Yes	Communications
19. Advanced Info Service	19.5	0.6	No	Yes	Yes	Communications
20. Ayudhya Capital Auto Lease	18.2	0.6	No	Yes	No	Financial
21. Bangkok Expressway	17.1	0.6	No	Yes	Yes	Consumer
22. Kiatnakin Bank	16.3	0.5	No	Yes	Yes	Financial
23. Quality Houses	15.3	0.5	No	Yes	Yes	Consumer
24. PTT Aromatics and Refining	15.0	0.5	Yes	No	Yes	Energy
25. Glow Energy	15.0	0.5	No	Yes	Yes	Utilities
26. CH Karnchang Public Company	14.0	0.5	No	Yes	Yes	Industrial
27. Land and Houses	13.6	0.4	No	Yes	Yes	Consumer
28. Thanachart Capital	13.5	0.4	No	Yes	Yes	Financial
29. Ratchaburi Electricity Generating	13.3	0.4	No	Yes	Yes	Utilities
30. Bangkok Mass Transit System	13.0	0.4	Yes	Yes	No	Industrial
Total Top 30 LCY Corporate Issuers	965.4	31.4				
Total LCY Corporate Bonds	1,375.2	44.8				
Top 30 as % of Total LCY Corporate Bonds	70.2%	70.2%				

LCY = local currency.
Source: Bloomberg LP.

14%, respectively. Proceeds will be used to fund exploration, development, and production activities. Other US\$-denominated bond issuers in 2Q11 include Export-Import Bank Thailand and Siam Commercial Bank, with issue sizes of US\$120 million and US\$400 million, respectively.

The foreign holdings of Thai government bonds stood at THB227.8 billion at end-June, an increase of 110.0% y-o-y and 6.8% q-o-q. Foreign holdings represented 8.9% of total government bonds outstanding as of end-June.

Investor Profile

Contractual savings funds are the largest holder of Thai government bonds, with a total of THB572 billion at end-June (Figure 2). Contractual savings funds' total share decreased to 22.4% in June 2011 from 25.4% in June 2010. Insurance companies were the next largest holder with a 21.8% share in June 2011, up from 18.1% a year earlier. Residents landed in the third spot, decreasing their share to 16.3% in June 2011 from 16.9% a year earlier. Commercial banks had a share of 15.9%, followed by nonresidents (8.9%), the central bank (7.5%),

financial corporations "not elsewhere classified" (3.9%), and general government and non-profit organizations (2%). Finally, other non-financial corporations held a 0.8% share, while non-financial market mutual funds had a marginal 0.6% share.

Rating Changes

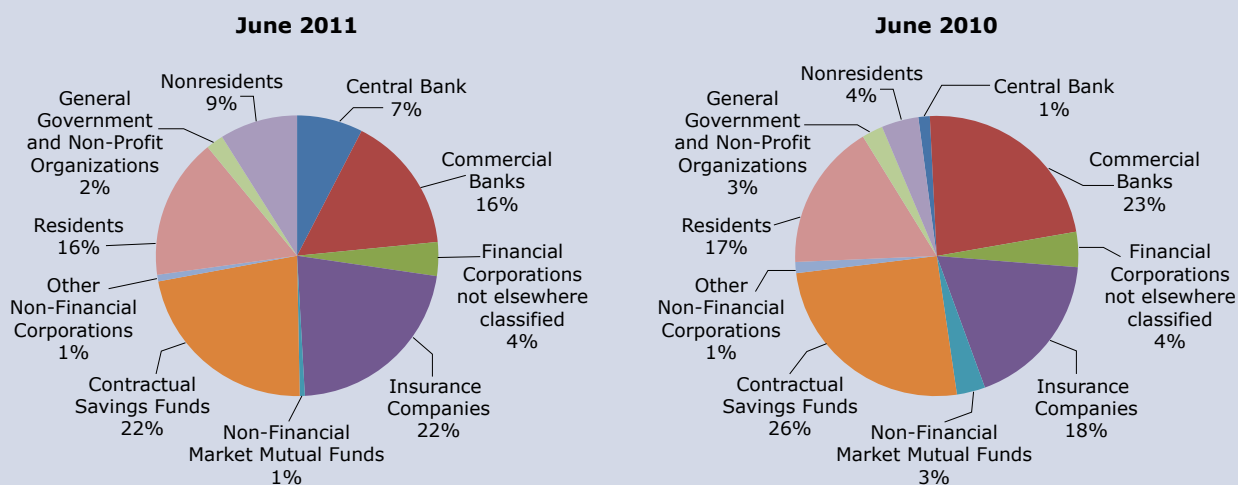
In April, Ratings and Investment Information (R&I) upgraded the outlook for Thailand's long-term FCY and LCY government bond ratings to stable from negative (Table 3). According to R&I, a rating upgrade is possible if Thailand "demonstrates the strength of its economic base even if political conflict continues."

Table 3: Selected Sovereign Ratings and Outlook for Thailand

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

Policy, Institutional, and Regulatory Developments

PDMO Plans Bond Trading via ATMs

In April, PDMO announced that it plans to allow retail investors to trade bonds via automated teller machines (ATMs). According to PDMO, the Thai Finance Ministry plans to assign commercial banks as distributors of government savings bonds to retail investors through ATMs across Thailand.

BOT Announces New List of Primary Dealers

BOT announced a new list of primary dealers for bilateral repurchase transactions, effective 3 May. The list includes Bangkok Bank, Krung Thai Bank, Bank of Ayudhya, Kasikorn Bank, Siam Commercial Bank, TMB Bank, Bank for Agriculture and Agricultural Cooperatives, Standard Chartered Bank, The Bank of Tokyo-Mitsubishi UFJ, United Overseas Bank, Government Savings Bank, and HSBC. BOT periodically reviews its list of primary dealers to encourage competition and enhance efficiency in conducting monetary operations.

SEC Tightens Rules on Bills of Exchange

Thailand's Securities and Exchange Commission (SEC) released tighter rules on bills of exchange in May, addressing potential risks as local banks have recently been aggressive in issuing bills of exchange to manage short-term liquidity. The SEC announced that bills of exchange should be treated similar to other debt instruments and therefore subject to SEC regulations. Exemptions previously offered to financial institutions will be reversed, although a grace period will be provided before any new measures take effect.

Thai Local Governments to Issue Bonds

PDMO announced in May that the cities of Bangkok and Pattaya, as well as several other local governments, will be allowed to raise funds through bond issues. However, the central government will not guarantee these issues. The SEC will supervise the bond issues and a credit rating will be required. Currently, local governments source funds from banks to finance investment projects. The Finance Ministry and the Interior Ministry are working together on this regulation as part of the public finance bill that is currently under review by the State Council.

Thai Treasury Department Plans to Issue Securitized Bonds

The Treasury Department of Thailand announced in July it plans to issue THB3 billion worth of securitized bonds to finance property development projects. A major component of the construction efforts will be new government office buildings in Soi Ratchakru, Phaholyothin Road. The estimated construction cost of this project is THB2 billion–THB3 billion. If approved by the government, it would be the second time that Thailand has issued securitized bonds since it issued a THB21 billion securitized bond in 2005.