



ADB

ASIA CAPITAL MARKETS MONITOR

MAY 2010

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The Asia Capital Markets Monitor 2010 was prepared by ADB's Office of Regional Economic Integration and does not necessarily reflect the views of ADB's Board of Governors or the countries they represent.

Key Questions

- Will global economy support Asia's capital markets?
- How will Asian capital markets perform?
 - Can Asian equities gain further?
 - How will Asian bonds perform?
 - Where will Asian currencies head?
- How do we effectively manage capital flows?

Key Answers for 2010

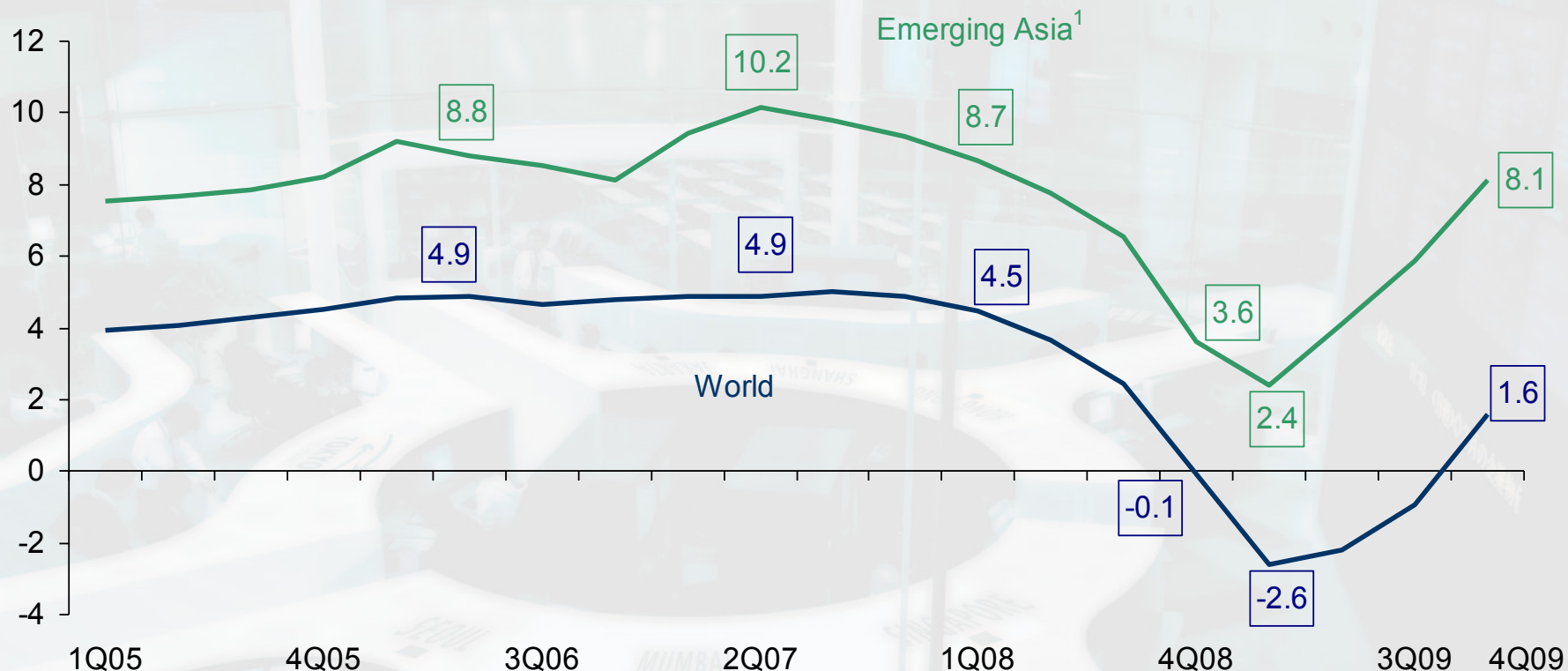
- Asia will continue to attract global investors
- Performance to vary, but generally upbeat
 - Asian equity gains may ease somewhat
 - Local currency bonds remain attractive
 - The region's currencies mostly appreciating
- Good macroeconomics, flexible FX, financial resilience key to managing capital flows

Global and Regional Environment

- Global recovery builds; emerging Asia gains traction...
- ...plus risk appetite and better yields lead to surge in capital flows
- Inflation up but manageable
- External funding fine, but Greek contagion a concern
- Timing and pace of stimulus exits key

Emerging Asia's growth gains traction...

GDP Growth—Emerging Asia and World (year-on-year, %)



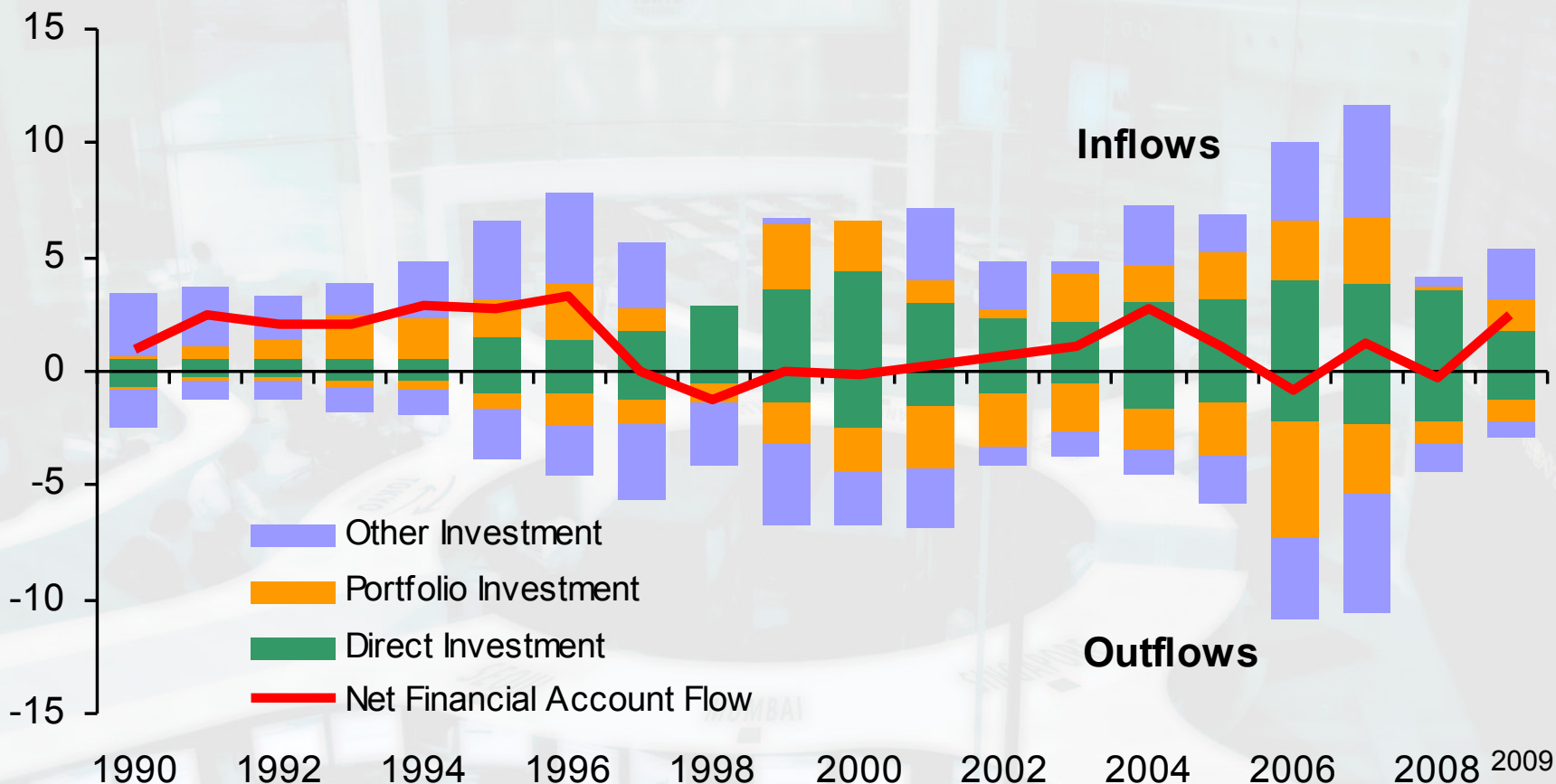
Note: Aggregates are weighted based on gross national income levels (Atlas Method in current USD prices) from World Development Indicators (World Bank).

¹ Emerging Asia includes China, People's Rep. of; Hong Kong, China; India; Indonesia; Korea, Rep. of; Malaysia; Philippines; Singapore; Taipei, China; Thailand; and Viet Nam.

Source: National sources accessed through CEIC database and *World Economic Outlook April 2010*, International Monetary Fund.

... as a result capital inflows surge

Financial Account Flows—Emerging Asia (% of GDP)



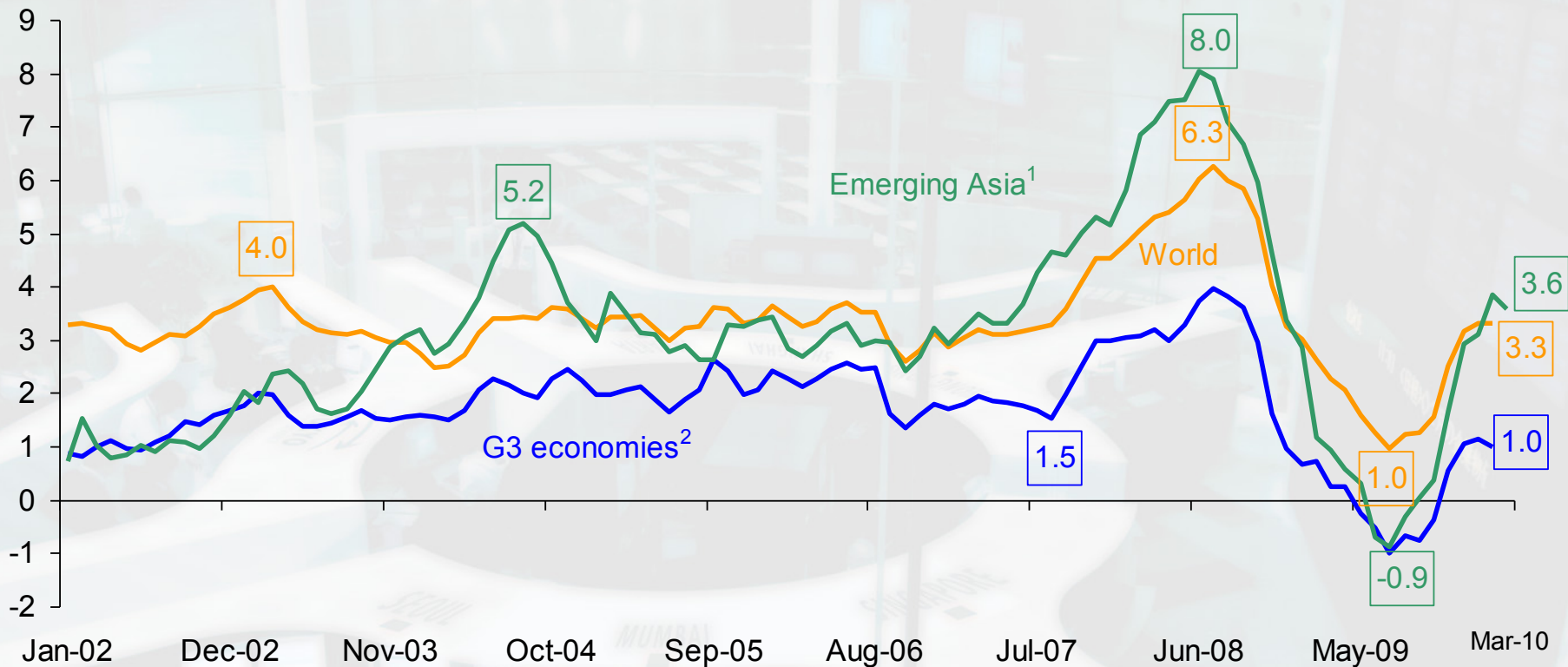
GDP = gross domestic product

Note: Emerging Asia includes People's Rep. of China; Hong Kong, China; Indonesia; India; Rep. of Korea; Malaysia; Philippines; Singapore; Taipei, China; and Thailand.

Source: *International Financial Statistics* and *World Economic Outlook Database*, International Monetary Fund; and CEIC database.

Inflation edges up but manageable

Inflation—Emerging Asia, G3 Economies, and World (year-on-year, %)



¹ Emerging Asia includes China, People's Rep. of; Hong Kong, China; India; Indonesia; Korea, Rep. of; Malaysia; Philippines; Singapore; Taipei, China; Thailand; and Viet Nam. ² G3 economies include eurozone, Japan, and United States.

Source: *World Economic Outlook April 2010*, International Monetary Fund; and national sources accessed through CEIC database.

External funding eases...

Corporate and Sovereign Eurobond¹ Issuance—Emerging Asia² (USD billion)

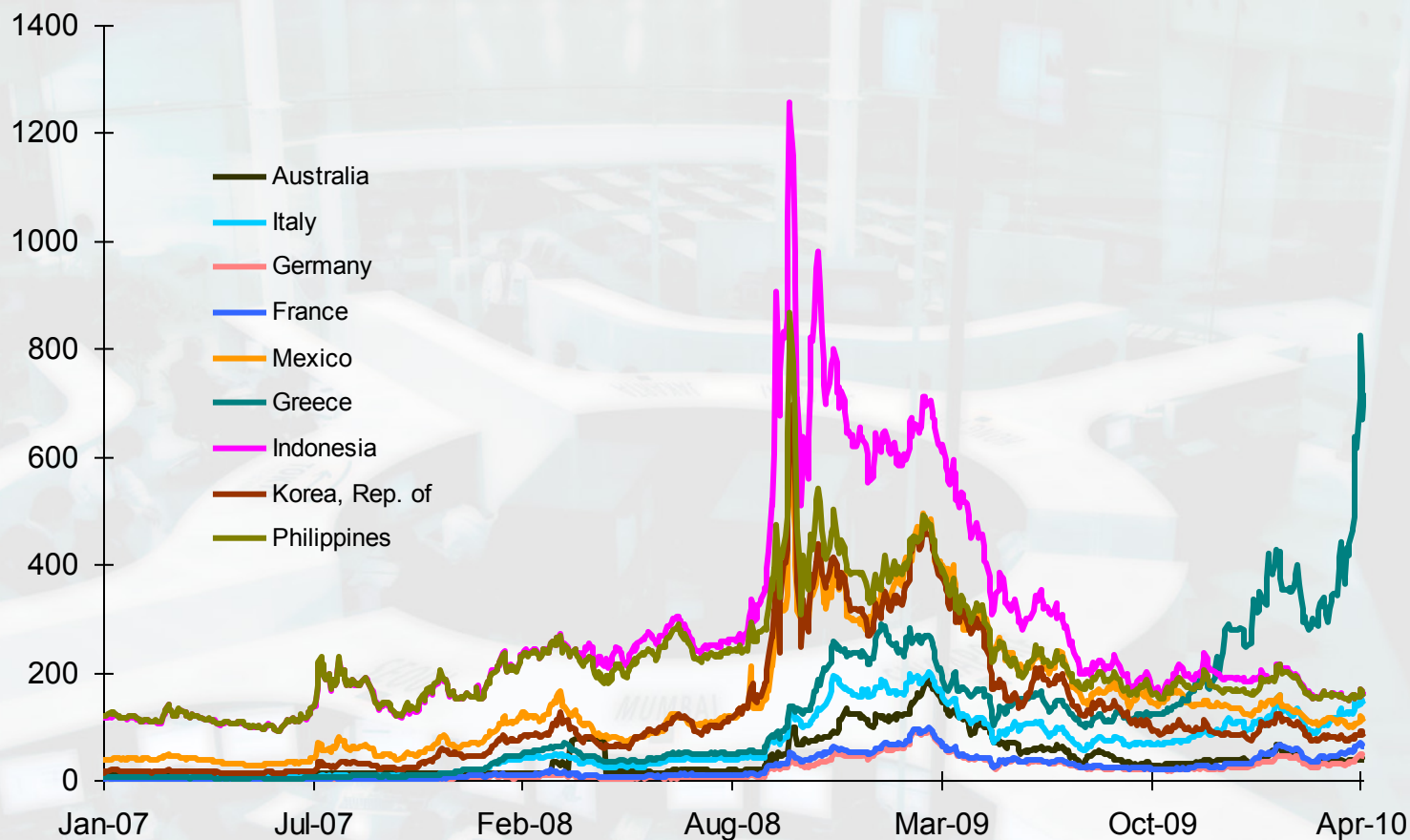


¹Includes US dollar, euro, and Japanese yen bond issuances. Sovereign bonds refer to those issued by national government and government agencies. Data excludes certificate of deposits. ²China, People's Rep. of; Hong Kong, China; Indonesia; India; Korea, Rep. of; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.

Source: OREI staff calculations using Bloomberg data.

...but Greek crisis is a strong reminder

Credit Default Swap Spreads— Selected OECD and Emerging Asian Economies (basis points)



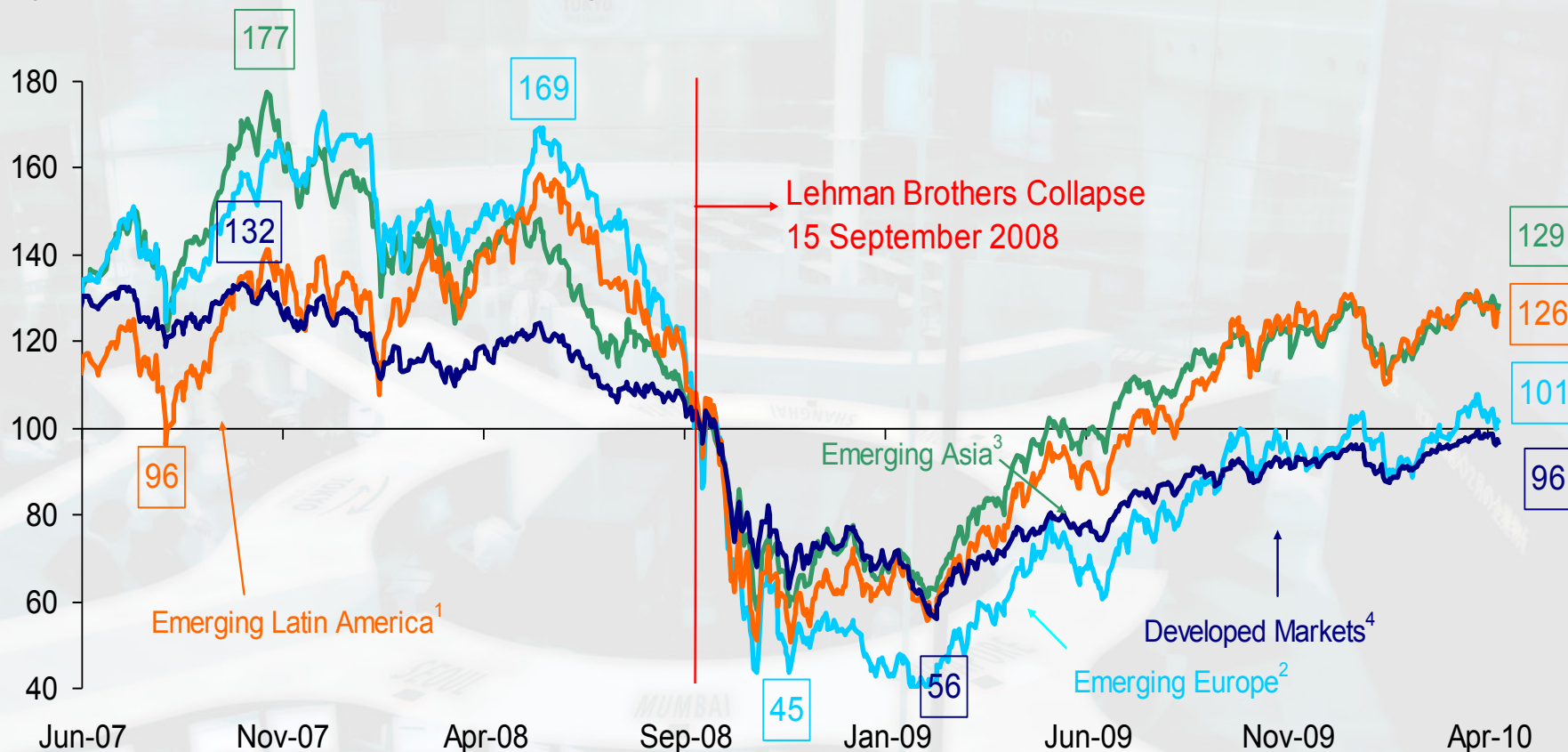
OECD = Organization for Economic Cooperation and Development.
Source: Thomson Datastream.

Asian equities

- Recovery, attractive values, and rising confidence spur gains
- Foreign investment back in black
- IPOs and private deals escalate
- Current values, however, suggest limited gains down the road

Asian equity markets rebound strongly...

MSCI Equity Market Indexes (15 September 2008 = 100)

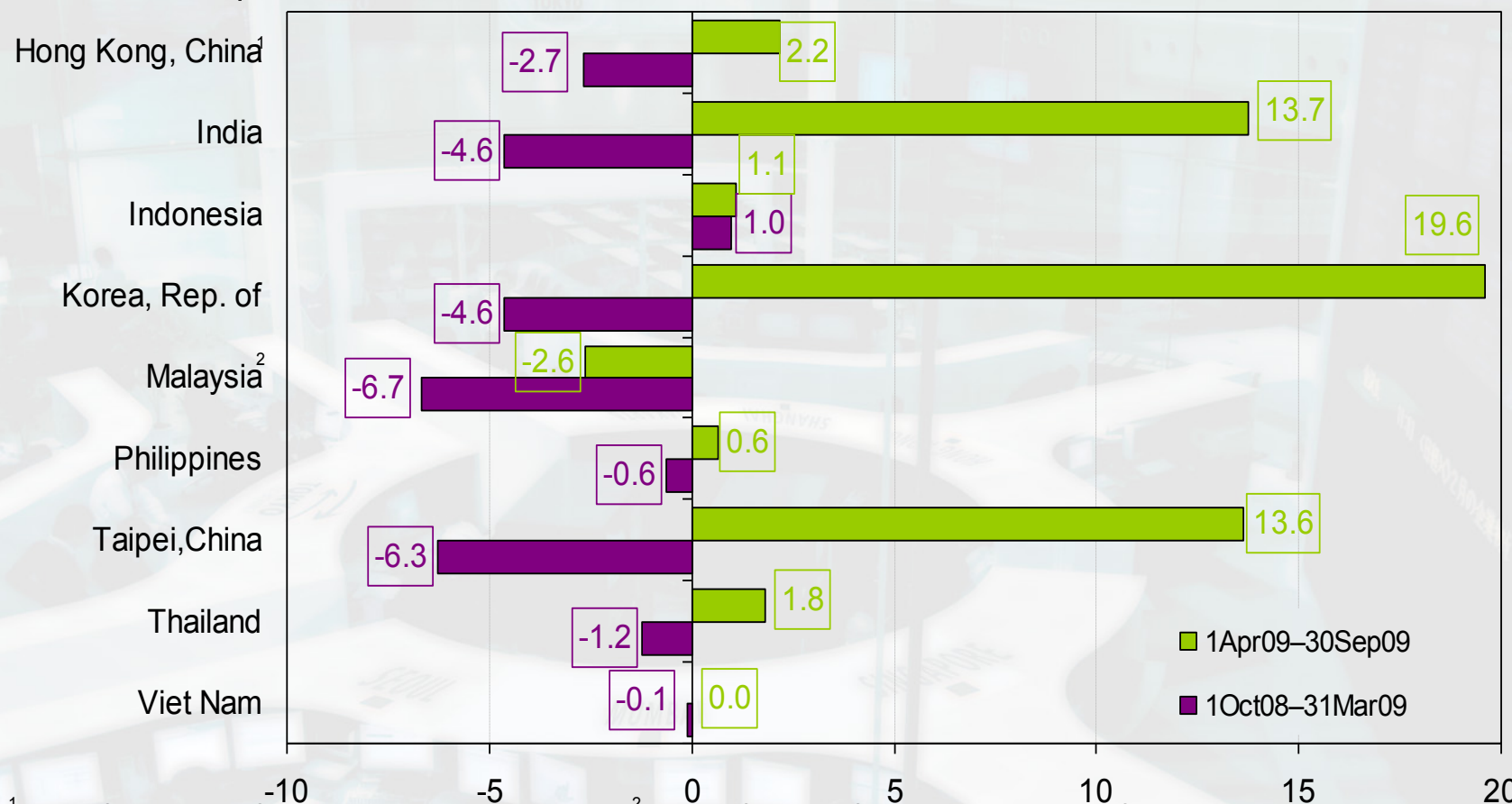


¹Brazil, Chile, Colombia, Mexico, and Peru. ²Czech Republic, Hungary, Poland, Russia, and Turkey. ³China, People's Rep. of; India; Indonesia; Korea, Rep. of; Malaysia; Philippines; Taipei, China; and Thailand. ⁴Canada, France, Germany, Italy, Japan, United Kingdom, and United States.

Sources: Morgan Stanley Capital International (MSCI) Barra.

...with foreign investment surging

Net Foreign Portfolio Investment in Equities—Emerging Asia (USD billion)

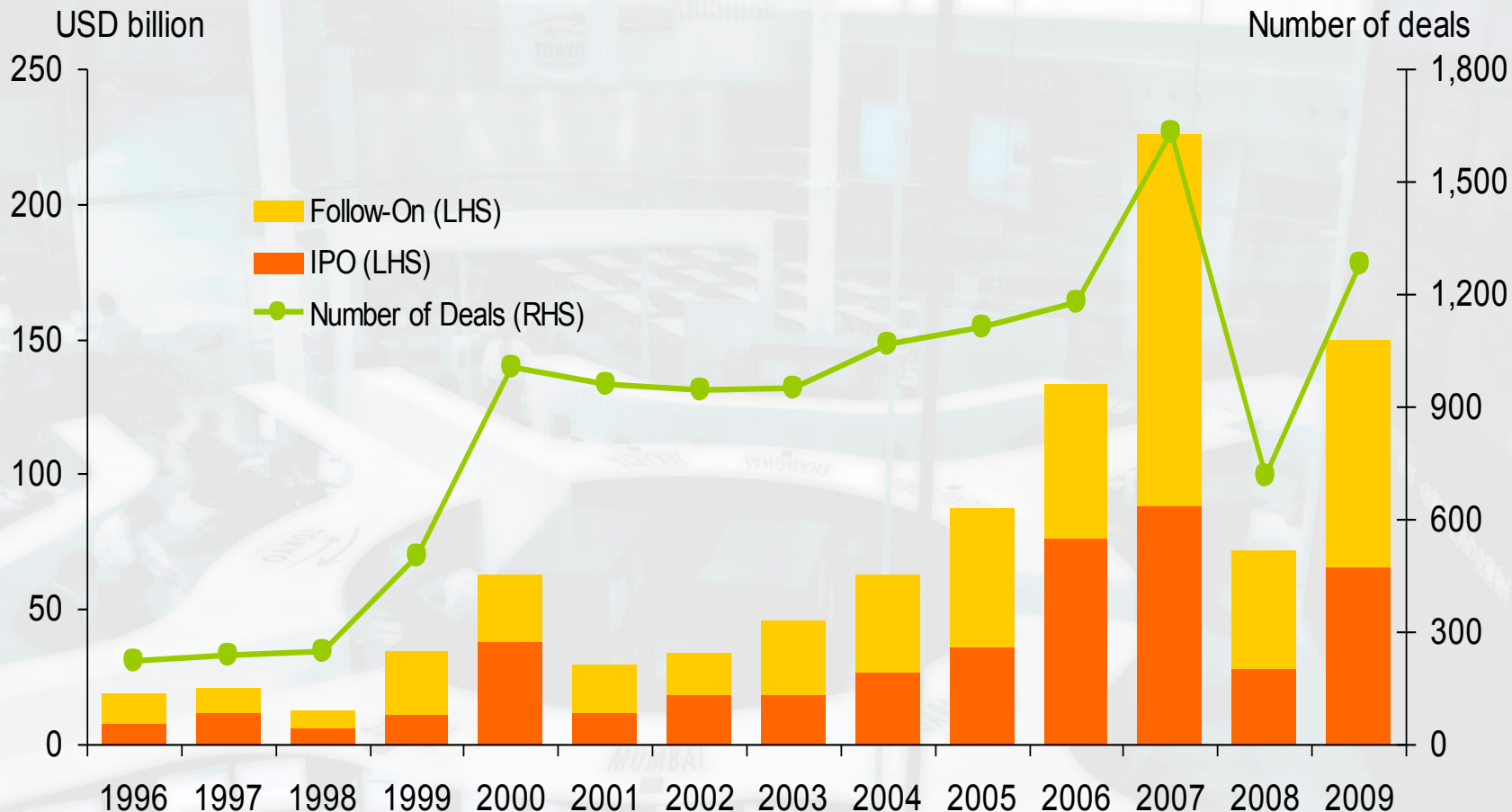


¹ Data refers to net portfolio investment in equity securities. ² Values refers to net foreign and domestic portfolio investment in shares and corporate securities.

Source: Bloomberg, CEIC, and Bank Negara Malaysia.

IPOs and private deals buoyant...

Equity Issuance—Emerging Asia¹



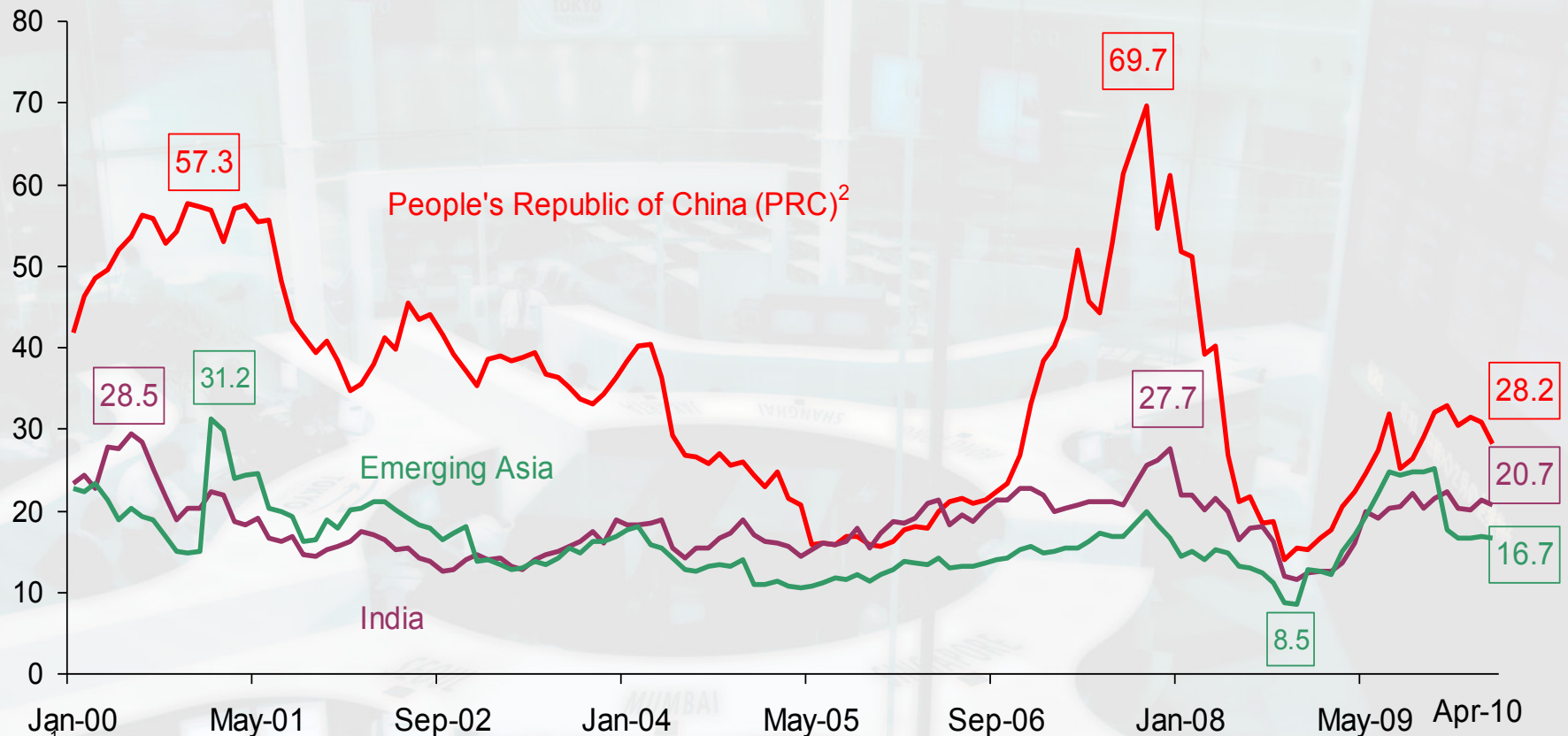
IPO = initial public offering, LHS = left-hand side, RHS = right-hand side

¹ Includes China, People's Rep. of; Hong Kong, China; India; Indonesia; Korea, Rep. of; Malaysia; Philippines; Singapore; Taipei, China; Thailand; and Viet Nam.

Source: Dealogic.

...but values suggest limited room for more gains

Price–Earnings Ratio—Emerging Asia,¹ PRC, and India



¹ Data refers to MSCI AC Asia (excluding Japan) which includes PRC; Hong Kong, China; India; Indonesia; Korea, Rep. of; Malaysia;

Philippines; Singapore; Taipei, China; and Thailand. ² Price-Earnings Ratio of combined Shanghai and Shenzhen Composite, weighted by their respective market capitalization.

Source: CEIC database and Bloomberg.

Asian Bonds

Low interest rates and better risk appetite help robust growth

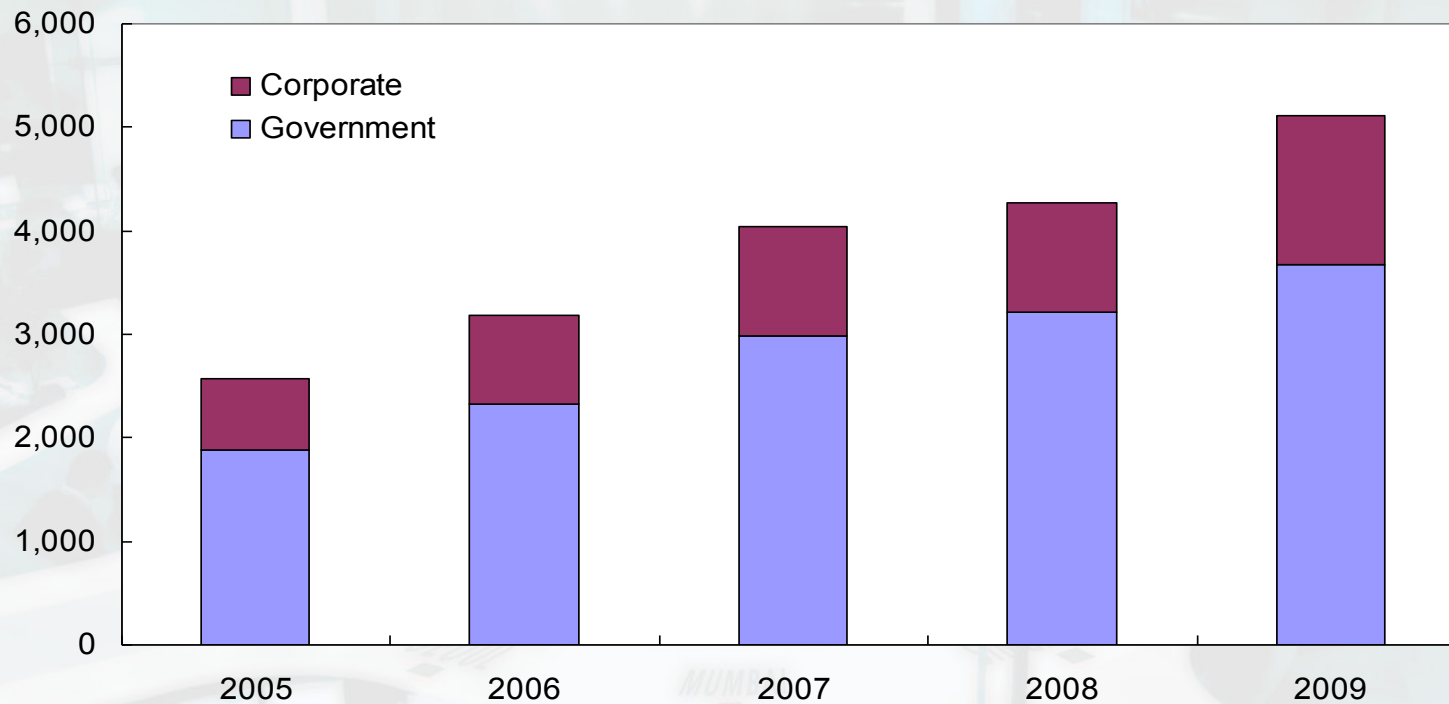
Foreign interest in LCY sovereigns much higher

LCY issuance surges with stimulus

Yield curves steepen

LCY bonds grow quickly...

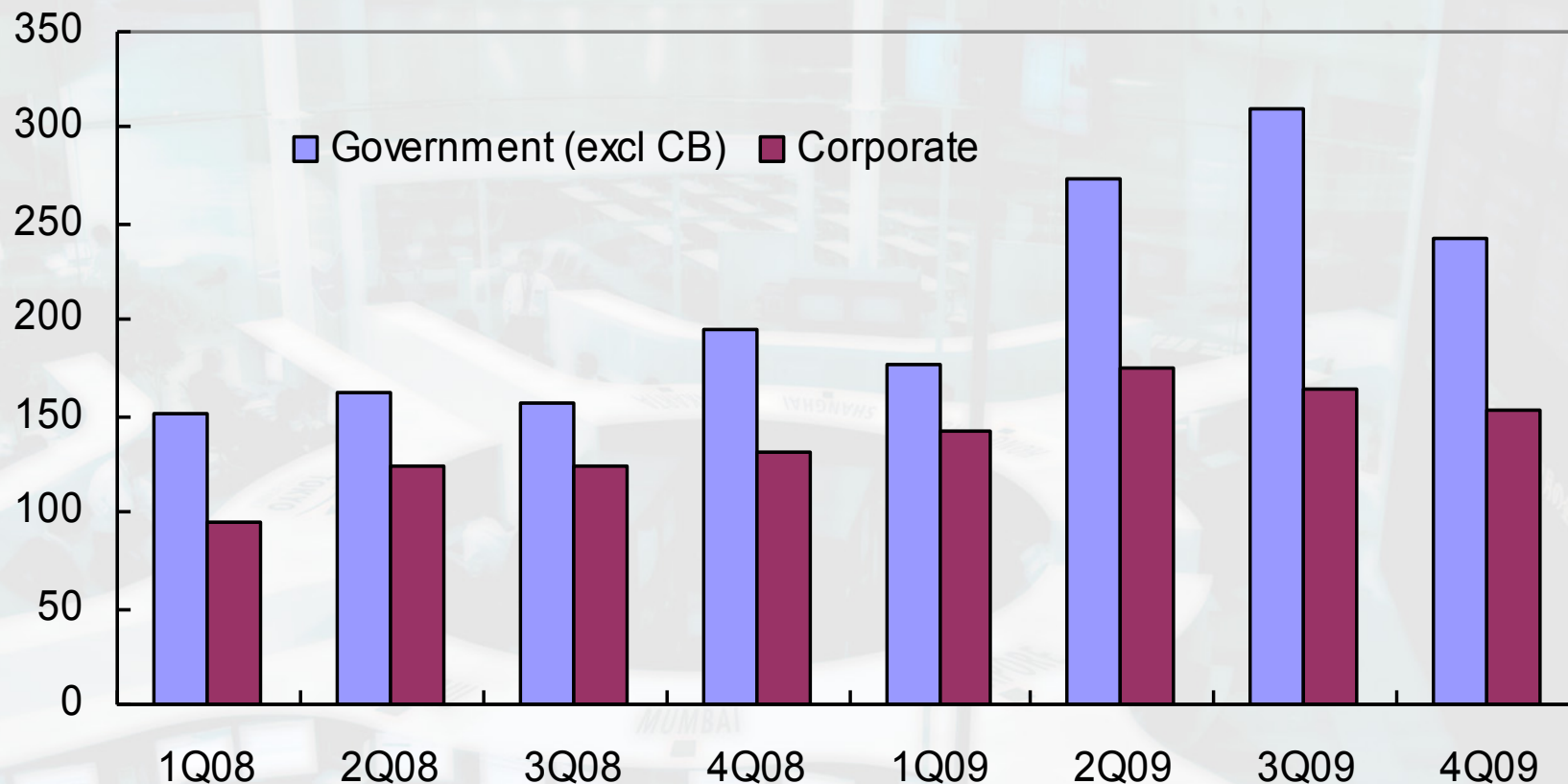
Total Bonds Outstanding—Emerging Asia (USD billion)



Source: AsianBondsOnline and Bloomberg LP.

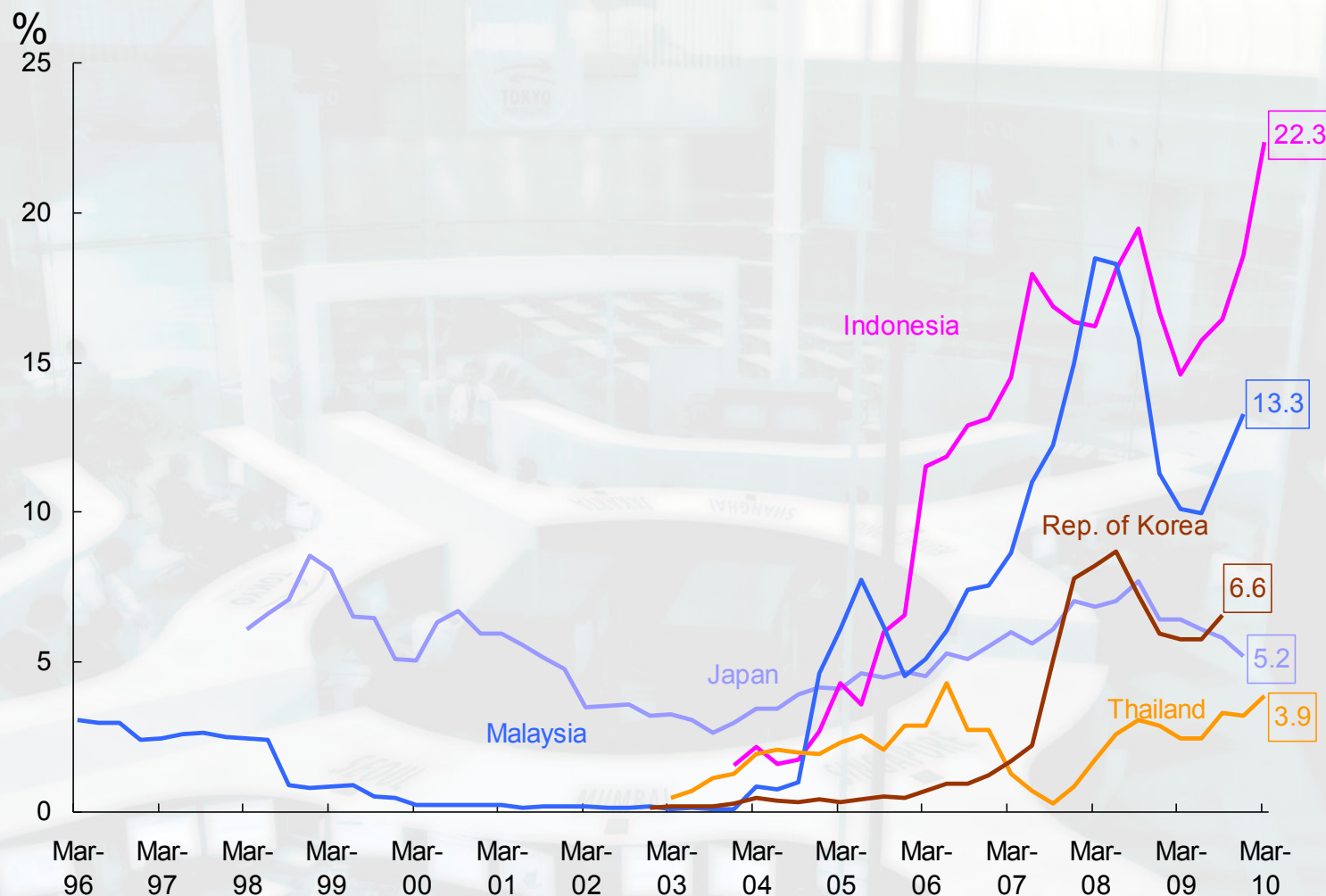
...as LCY issuance jumps

Government (excluding Central Bank) and Corporate Bond Issuance—Emerging Asia (USD billion)



Source: People's Republic of China (ChinaBond); Hong Kong, China (Hong Kong Monetary Authority); India (Bloomberg); Indonesia (Bloomberg); Republic of Korea (Bank of Korea); Malaysia (Bank Negara Malaysia); Philippines (Bloomberg); Singapore (Singapore Government Securities and Bloomberg); Thailand (Bank of Thailand); and Viet Nam (Bloomberg).

Foreigners like LCY government bonds

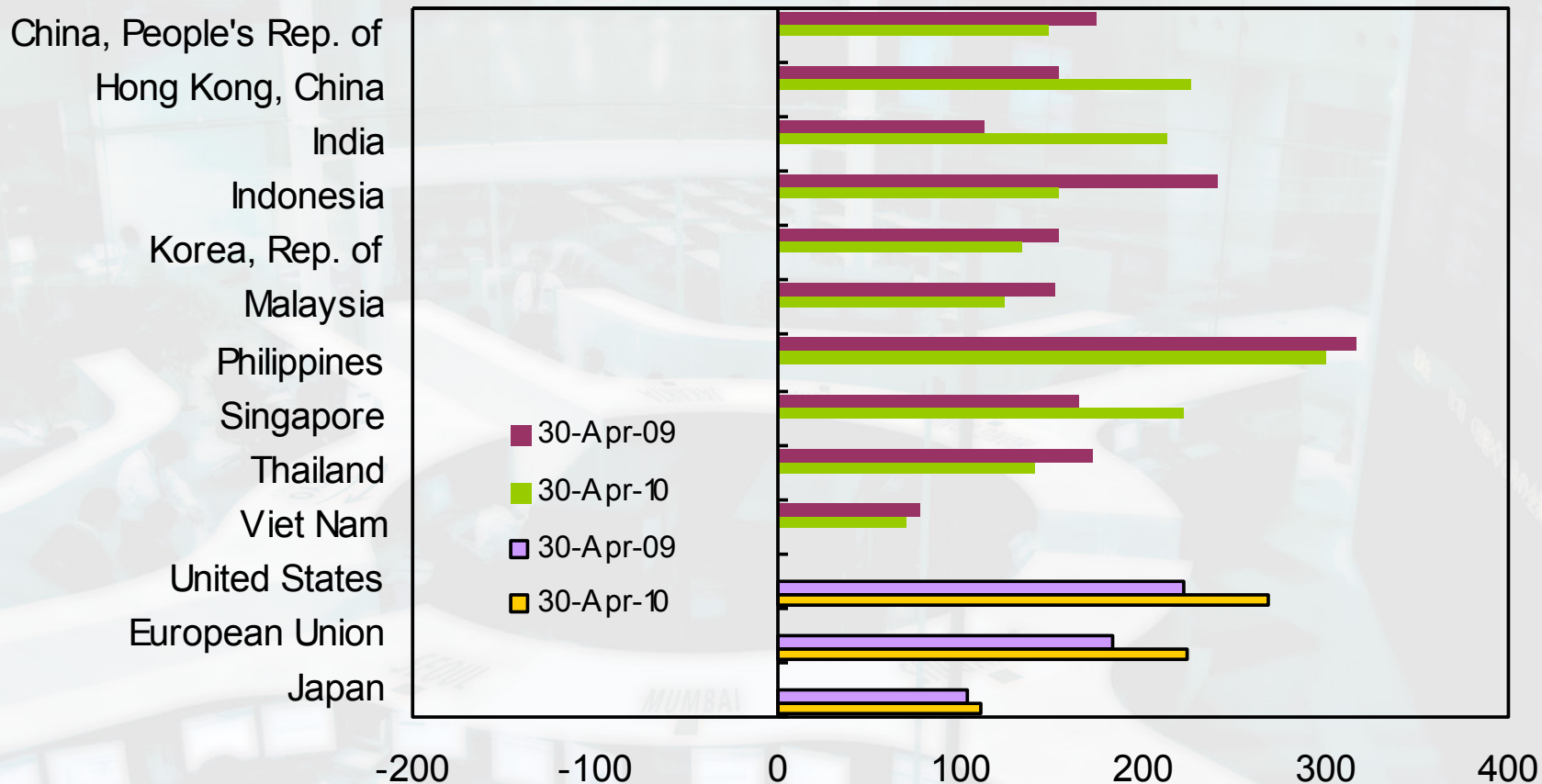


Note: Data as of March 2010. Values for the Republic of Korea as of September 2009, and Malaysia and Japan as of December 2009.

Source: AsianBondsOnline.

LCY government bond yield curves steepen

Yield Spread Between 2- and 10-Year Government Bonds (basis points)



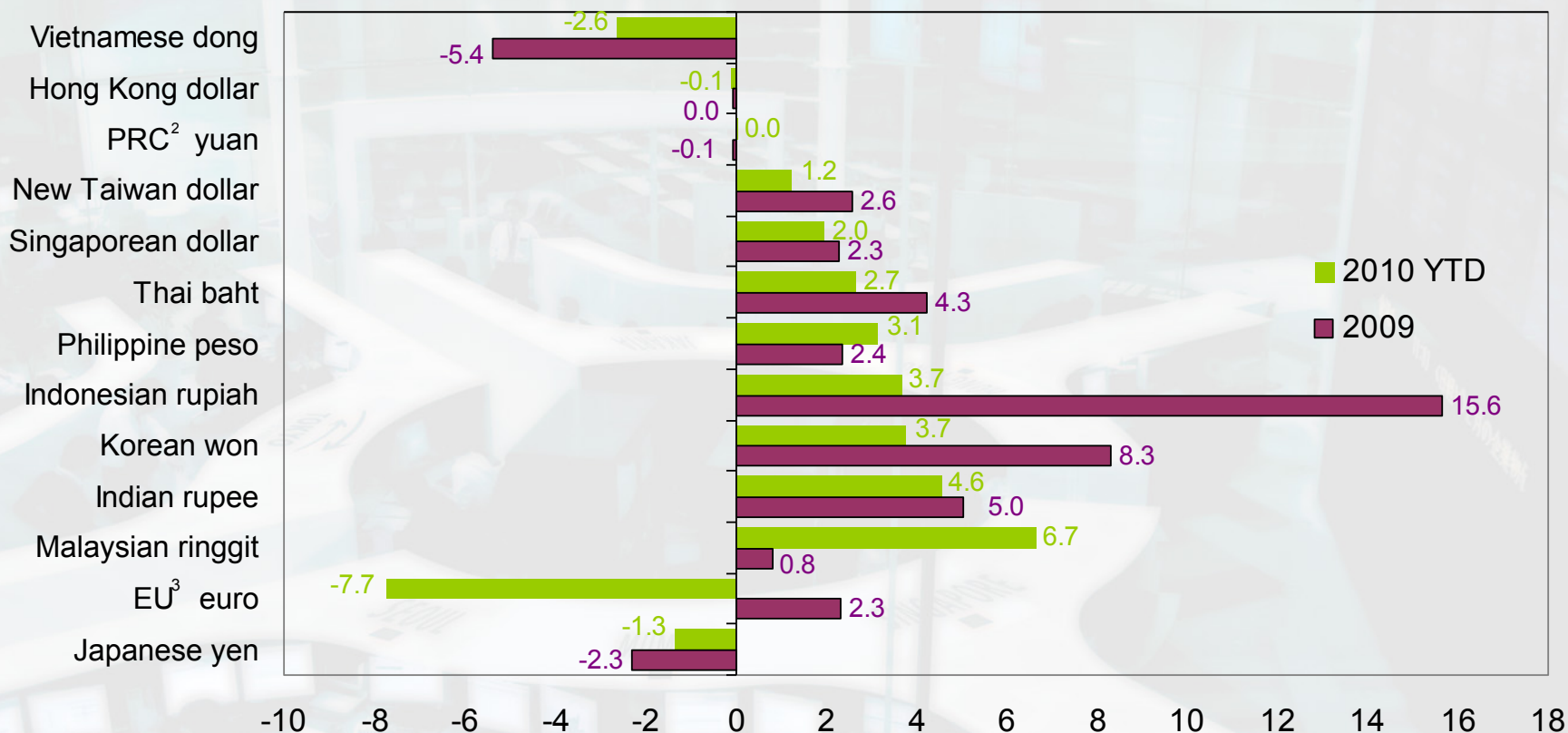
Source: Based on data from Bloomberg LP.

Asian Currencies

- Mostly appreciate with recovery
- Attract interest as an asset class
- Volatility steadily subsides
- Real effective exchange rates edge upward

Strong appreciation pressures continue...

Change in Exchange Rate versus the US dollar¹ (%)

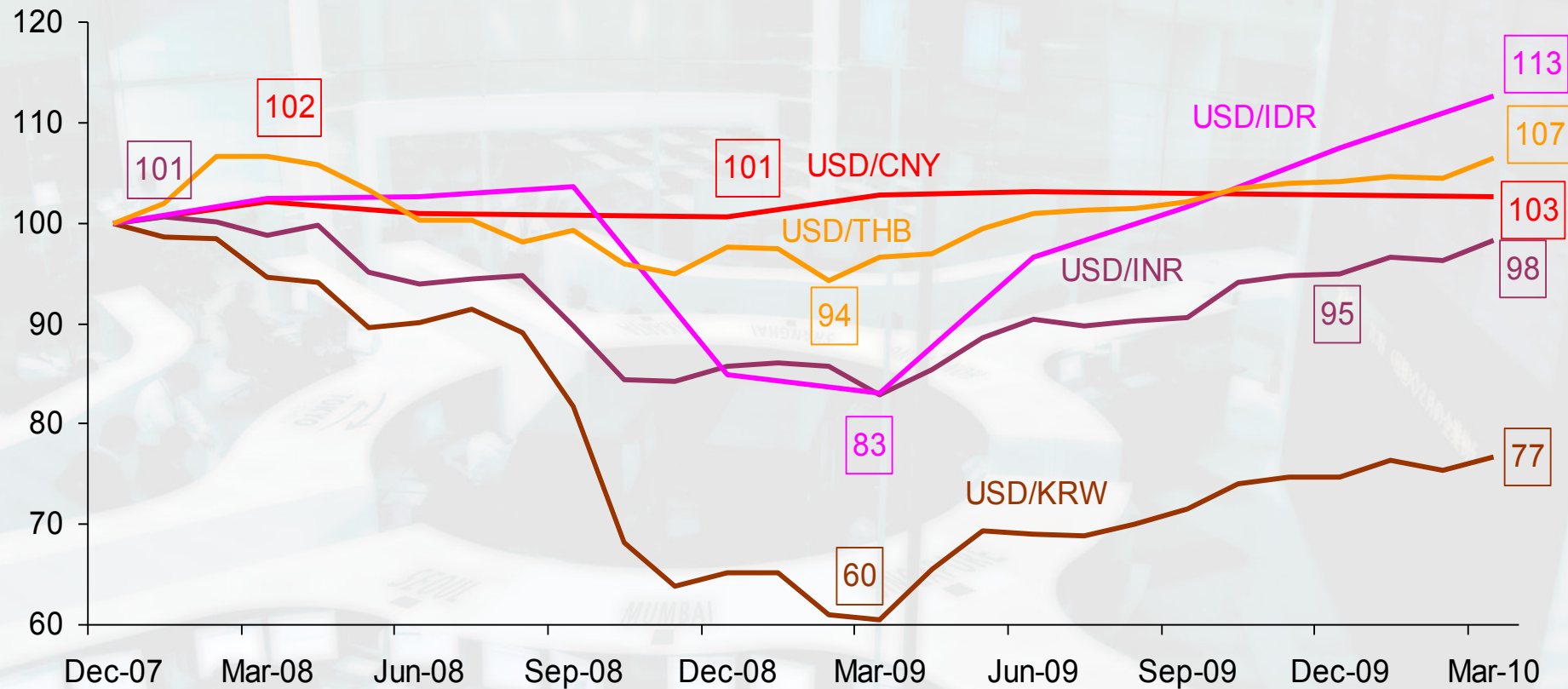


¹Year-to-date (YTD) figures for 2010 from 4 January to 30 April. Negative figures indicate depreciation of local currency; positive values indicate appreciation of the local currency. ²PRC = People's Republic of China. ³EU = European Union.

Source: OREI staff calculations based on Reuters data.

...and regain favor as an asset class

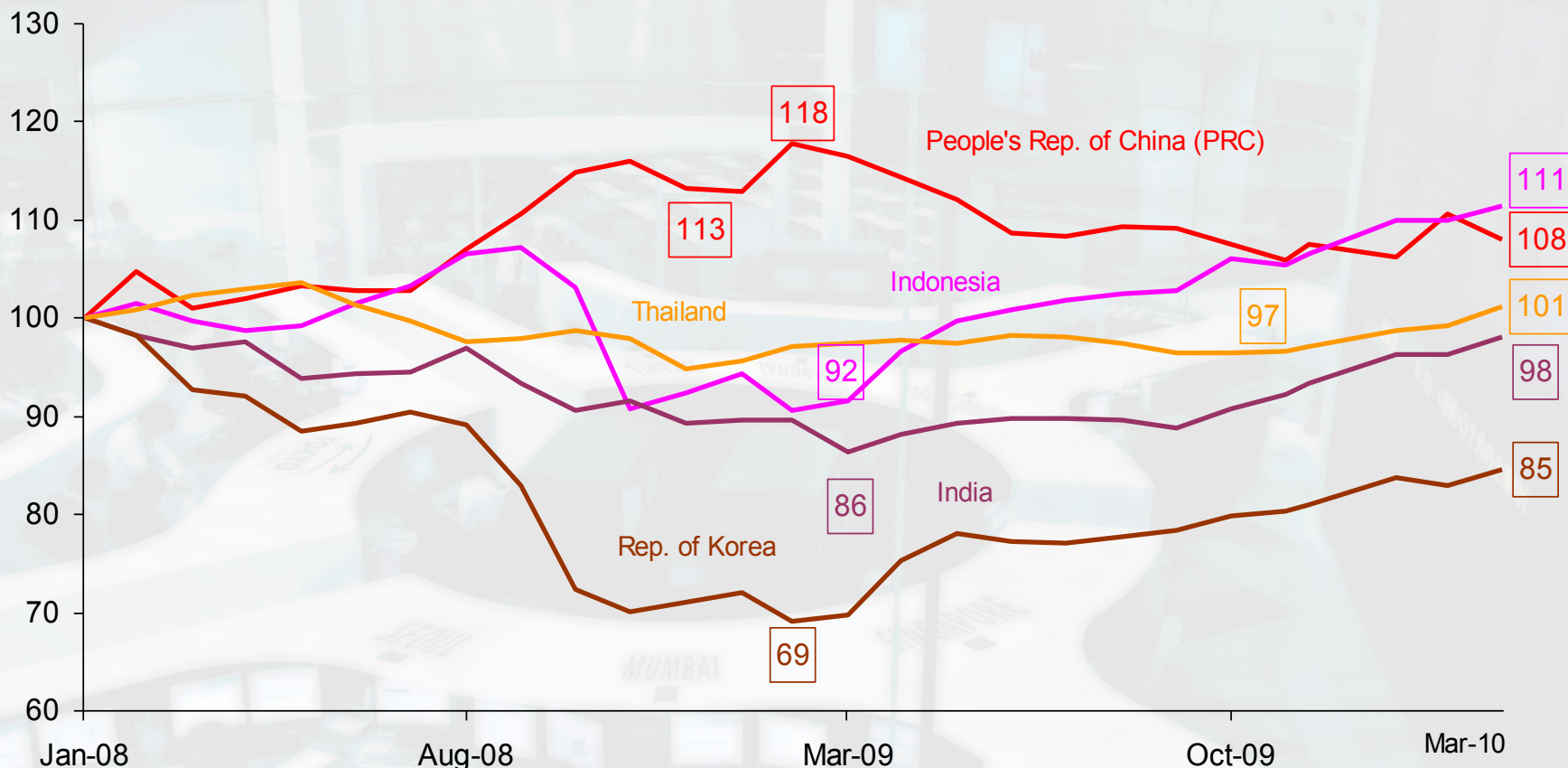
Currency Returns: Selected Asian Economies (December 2007 = 100)



Source: OREI staff computations using data from Thomson Reuters accessed through Datastream.

Real effective exchange rates edge upward

Real Effective Exchange Rate: Selected Asian Economies (January 2008 = 100)

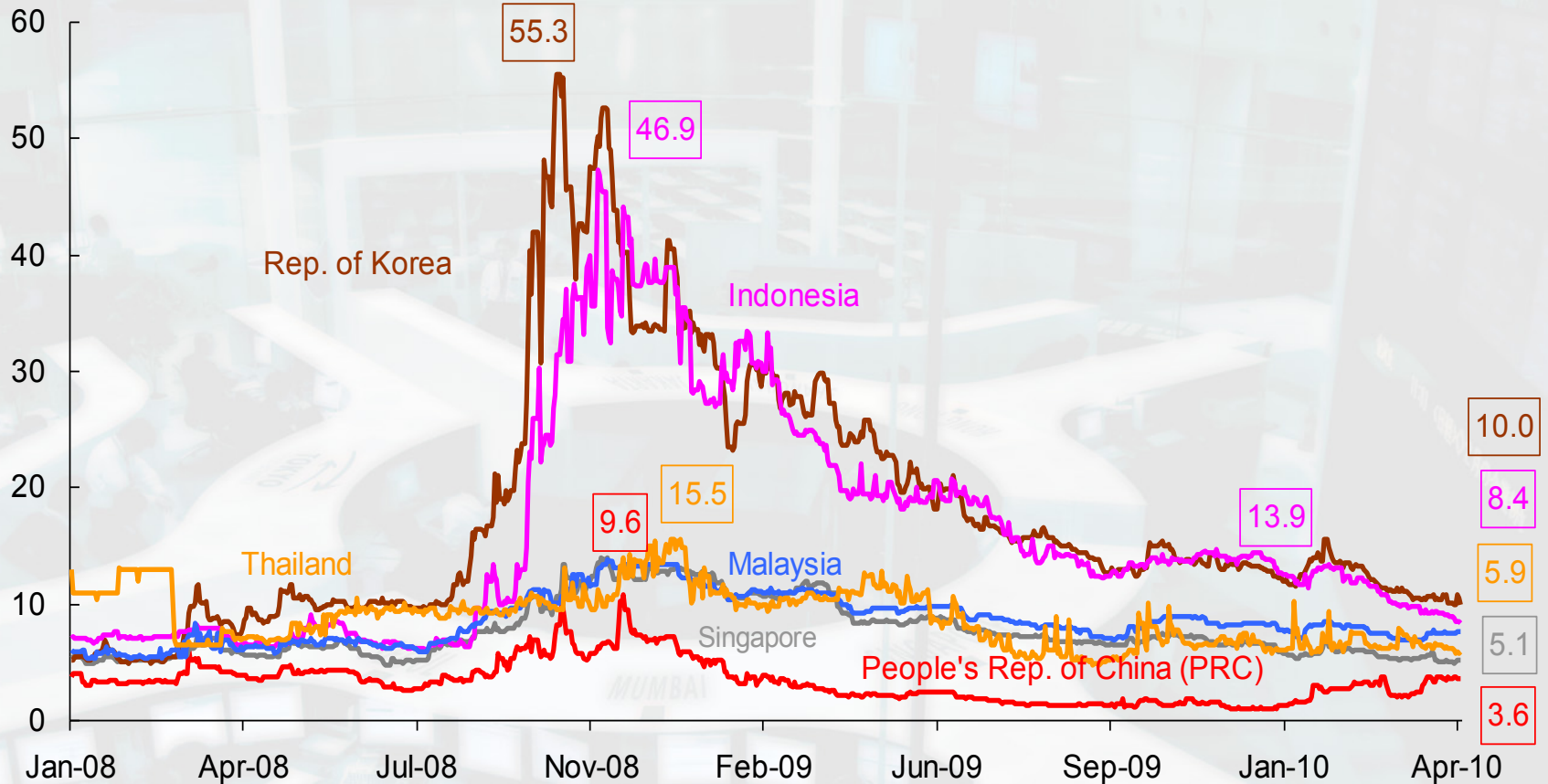


¹ Adjusted by relative consumer prices.

Source: OREI staff calculations using data from Bank for International Settlements.

FX volatility subsidies

Implied Volatility of Exchange Rates¹—Selected Emerging Asian Economies (%)



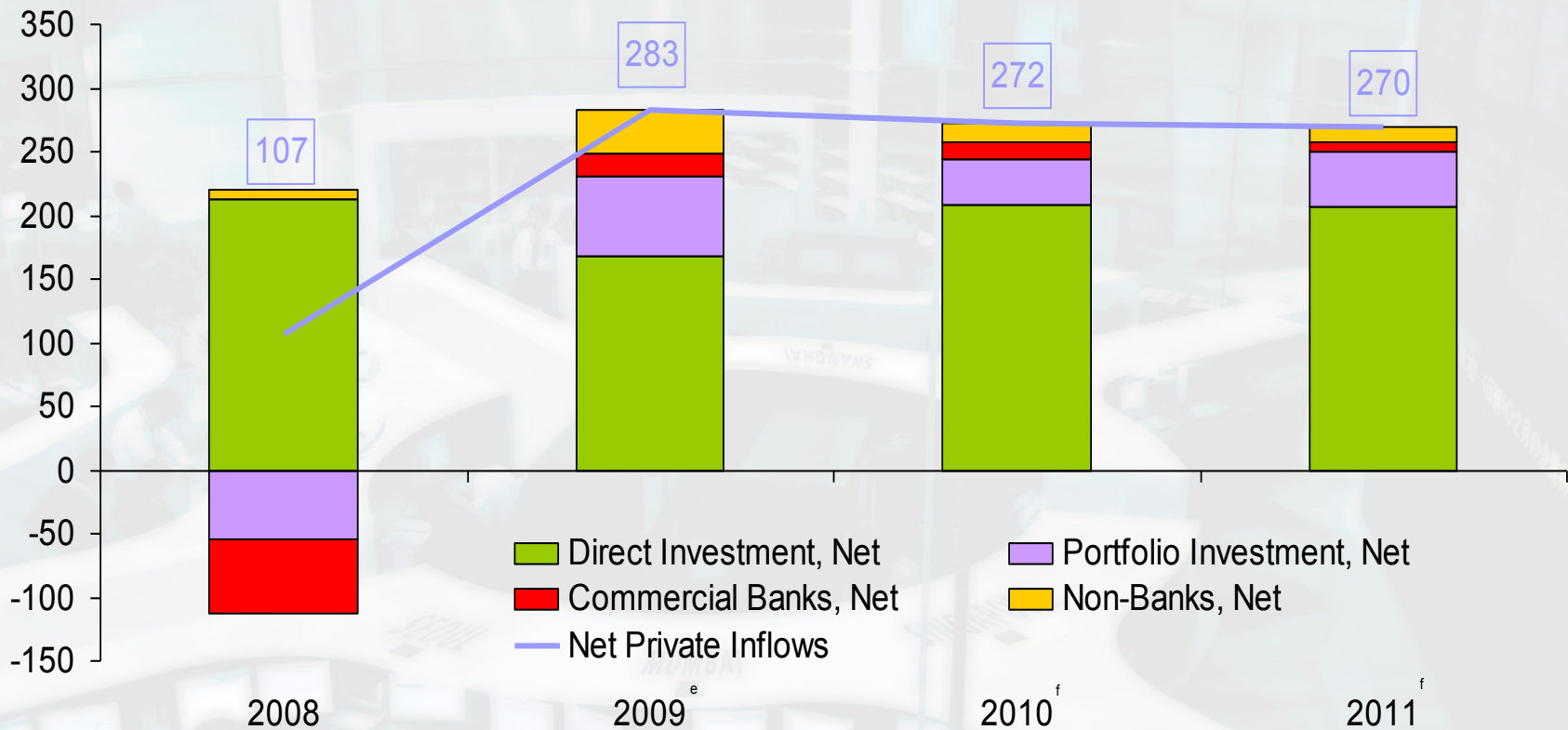
¹Data refers to 3 months implied volatility at-the-money strike (ATM).
Source: Bloomberg.

Managing Capital Flows: Issues and Challenges for Emerging Asia



Net private capital flows into emerging Asia up

Net Private Capital Flows (USD billion)



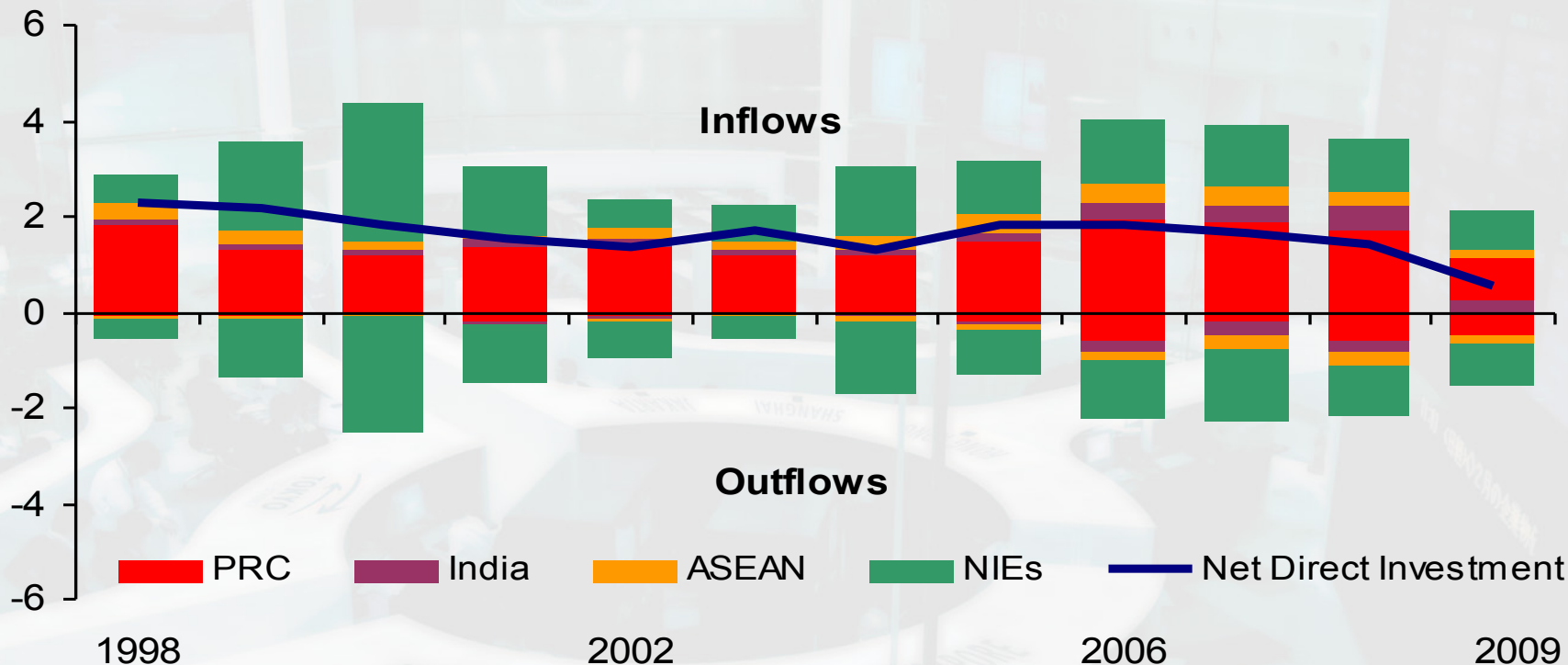
e = estimate; f = forecast.

¹ Emerging Asia includes China, People's Rep. of; India; Indonesia; Korea, Rep. of; Malaysia; Philippines; and Thailand.

Source: *Capital Flows to Emerging Market Economies (April 2010)*, Institute for International Finance.

FDI net inflows; but PRC dominates

Foreign Direct Investment Flows—Emerging Asia (% of GDP)



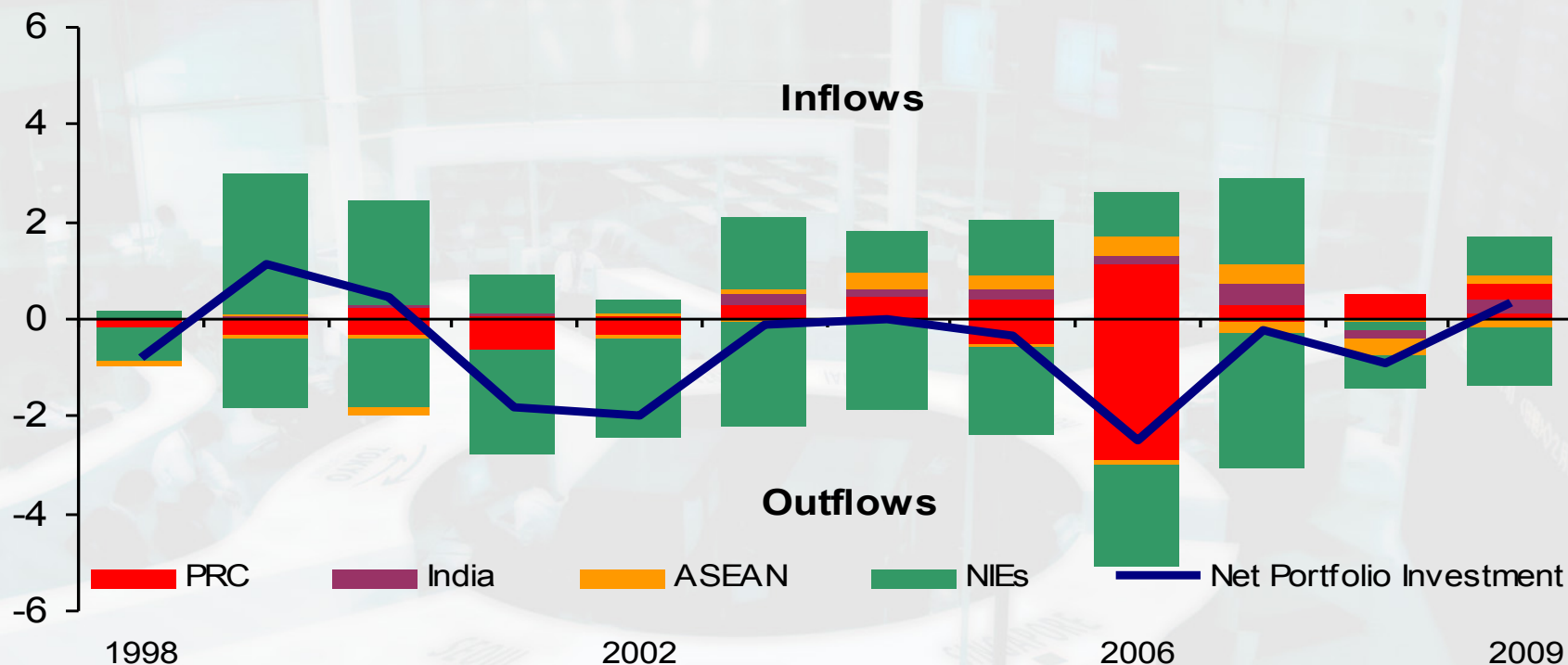
ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, NIEs = newly industrialized economies, PRC = People's Rep. of China

Note: Emerging Asia includes People's Rep. of China; Hong Kong, China; Indonesia; India; Rep. of Korea; Malaysia; Philippines; Singapore; Taipei, China; and Thailand.

Source: *International Financial Statistics* and *World Economic Outlook Database*, International Monetary Fund; and CEIC database.

Foreign portfolio investment flows increase both ways

Foreign Portfolio Investment Flows—Emerging Asia (% of GDP)



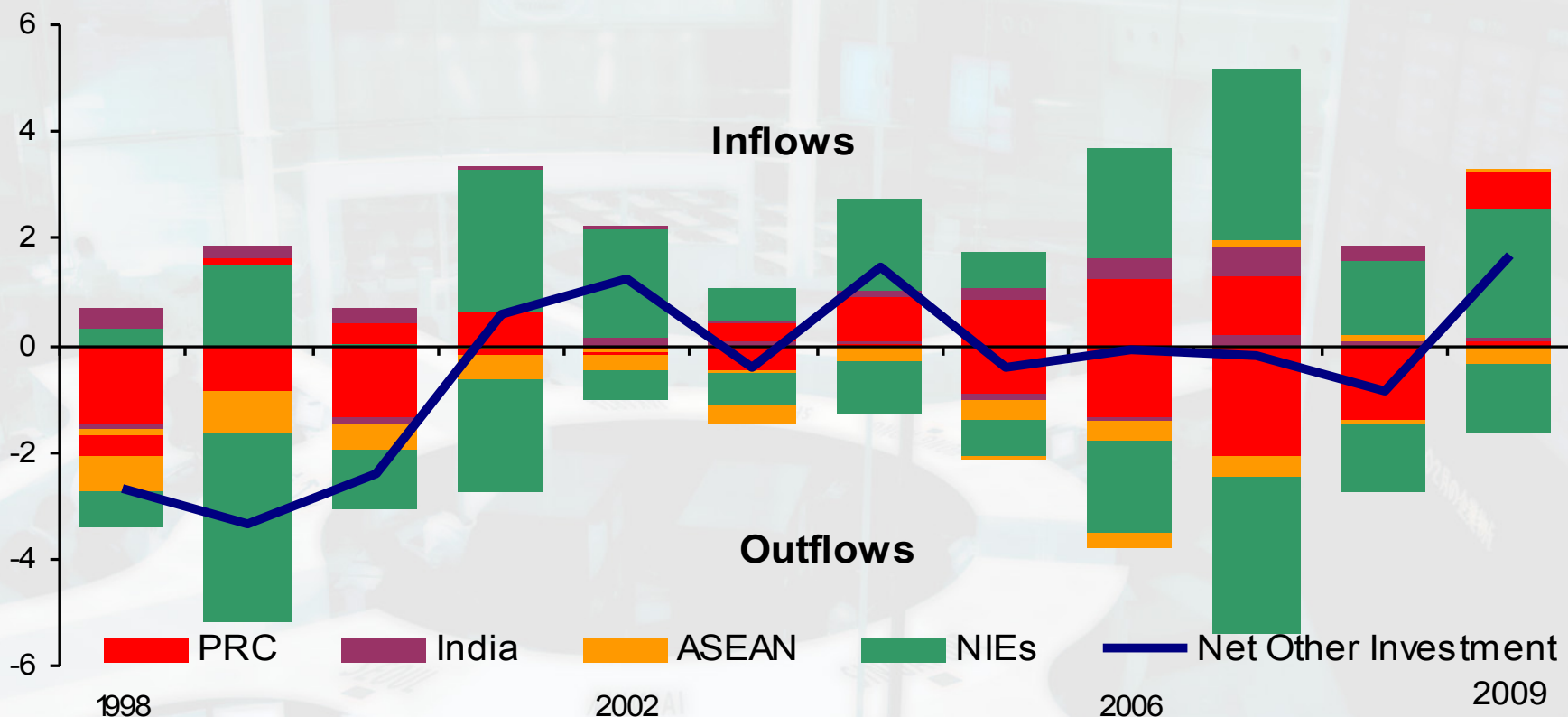
ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, NIEs = newly industrialized economies; PRC = People's Rep. of China

Note: Emerging Asia includes People's Rep. of China; Hong Kong, China; Indonesia; India; Rep. of Korea; Malaysia; Philippines; Singapore; Taipei, China; and Thailand. Inflows refer to foreign portfolio liabilities; outflows refer to foreign portfolio assets.

Source: *International Financial Statistics* and *World Economic Outlook Database*, International Monetary Fund; and CEIC data

Volatile banking flows a concern

Other Investment Flows—Emerging Asia (% of GDP)



ASEAN=Association of Southeast Asian Nations; GDP=gross domestic product; NIEs=newly industrialized economies; PRC=People's Rep. of China
 Note: Emerging Asia includes People's Rep. of China; Hong Kong, China; Indonesia; India; Rep. of Korea; Malaysia; Philippines; Singapore; Taipei, China; and Thailand. Inflows refer to foreign portfolio liabilities; outflows refer to foreign portfolio assets. Values include financial derivatives
 Source: *International Financial Statistics* and *World Economic Outlook Database*, International Monetary Fund; and CEIC database.

Effective management of capital flows crucial

Broad-based policy approach includes

- sound macroeconomic management
- flexible exchange rates
- resilient financial systems
- temporary and targeted capital controls

Capital controls may be warranted when...

- inflows are transitory,
- add undue pressure on exchange rates,
- pose risks to financial stability, and
- where the effectiveness of macroeconomic policies is uncertain

Thank you

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