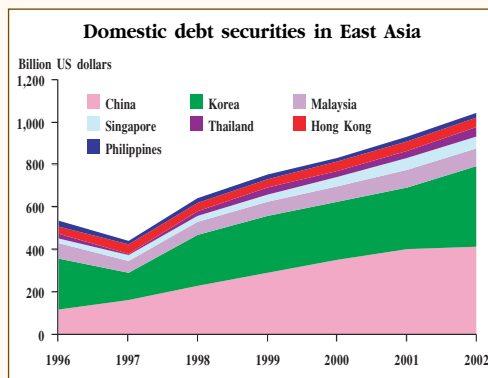


## Asian Bond Fund for Development in Asia

The launch of the Asian Bond Fund (ABF) on 2 June 2003 marked another important step towards closer cooperation among East Asia and Pacific economies. The Fund was established under the Executives Meeting of East Asia and Pacific Central Banks<sup>1/</sup>(EMEAP), comprising 11 central banks and monetary authorities in the East Asia and Pacific region. With an initial size of 1 billion US dollars<sup>2/</sup>, it will invest in Asian sovereign and quasi-sovereign bonds of EMEAP economies denominated in US dollars<sup>3/</sup>. The Fund will be managed by the Bank for International Settlements in a passive style<sup>4/</sup> according to a specific benchmark.

Since the 1997 crisis, the outstanding value of bonds in Asian markets rose continuously. The value of domestic bonds increased from 535.0 billion US dollars to 1,047.4 billion US dollars, equivalent to an increase of approximately 95.8 per cent during 1996-2002. While the value of bonds denominated in US dollars remained close to the level issued prior to the crisis. This reflected



Source: BIS Quarterly Review, Table 16 A

### Reserves between 1997-2002

Billion US dollars	1997	1998	1999	2000	2001	2002
Australia	17.1	14.3	21.1	19.0	19.5	20.8
China	144.5	144.7	156.8	176.2	234.0	292.0
Hong Kong	93.5	86.6	95.3	112.2	120.2	111.9
Indonesia	16.9	22.1	26.3	29.9	29.6	30.6
Japan	222.5	209.2	285.4	371.5	428.6	462.4
Korea	20.5	50.2	73.3	100.3	111.2	121.4
Malaysia	21.1	24.8	30.4	30.9	33.0	34.3
New Zealand	4.5	4.1	4.4	3.5	3.3	3.7
Philippines	7.6	9.2	13.4	14.0	14.9	13.6
Singapore	71.8	72.3	76.1	83.6	81.5	82.0
Thailand	26.5	27.9	33.9	33.5	35.1	38.2
EMEAP Economies	646.4	665.3	816.4	974.6	1,111.1	1,210.9
IMF Members	1,761.3	1,741.4	1,909.2	2,153.5	2,360.1	2,555.8
EMEAP/IMF	36.7	38.2	42.8	45.3	47.1	47.4

Source: International Financial Statistics, International Monetary Fund, May 2003

the change in public and private sectors' preferences for alternative sources of funds, apart from the traditional bank loans, which helped mitigate the risks of maturity mismatch as term of financing matched term of investment.

Even though the ABF aims to invest in US dollar-denominated bonds, this initiative will also benefit local Asian bond markets. More new

<sup>1/</sup> Comprises central banks and monetary authorities of Australia, People's Republic of China, Hong Kong SAR, Indonesia, Japan, Republic of Korea, Malaysia, New Zealand, the Philippines, Singapore and Thailand.

<sup>2/</sup> Thailand contributed 120 million US dollars.

<sup>3/</sup> Excluding bonds issued by Japan, Australia and New Zealand.

<sup>4/</sup> Passive style refers to the investment style which the fund manager adjusts and rebalances portfolios according to a certain benchmark.

active investors introduced by the ABF will prompt developments, competition and remove impediments in regional domestic bond markets. A developed bond market will act as a new source of funds as well as investment alternatives, with the ABF initiative being a first step of bond market development on a regional basis. As international reserves of the EMEAP economies are high and continue to increase steadily, through the ABF, a fraction of these reserves would help promote bond market developments in the region. As of end-2002, the total amount of international reserves among EMEAP members stood at 1,211 billion US dollars, or approximately half of the world's international reserves.

Owing to the nascent development of bond markets in Asia, regional investors preferred to invest their funds in bond markets outside the region. Some of this capital was re-invested in short-term securities markets in Asia, causing volatile and unstable capital flows as investors could withdraw their funds at any time. The ABF, therefore, is expected to increase the efficiency of the disintermediation process in the region through bond markets. Moreover, the high saving rates of EMEAP economies reflected the potential of the ABF initiative in redistributing these international reserves to invest in Asian bond markets.

**Saving Rates** (Per cent of GDP)

Country/Regional Group	1997	1998	1999	2000	2001	2002
World	22.9	22.5	23.2	23.8	22.4	22.3
Japan	30.8	29.7	28.4	28.7	27.7	26.4
Newly-Industrialized Asian*	32.5	32.7	31.9	30.9	29.0	28.5
Developing Asia**	28.3	29.0	31.9	30.6	29.0	29.7

Source : World Economic Outlook, International Monetary Fund, February 2003

\* Comprised Hong Kong, Korea, Singapore and Taiwan

\*\* Comprises Afghanistan, Bangladesh, Bhutan, Cambodia, China, Fiji, India, Indonesia, Kiribati, Lao PDR, Malaysia, Maldives, Nepal, Pakistan, Papua New Guinea, the Philippines, Samoa, Solomon Islands, Sri Lanka, Thailand, Tonga, Vanuatu and Vietnam

The ABF will help facilitate intra-regional investment, creating a closer link among regional financial markets. At the same time, utilization of financial centres in Asia, such as Tokyo, Hong Kong, Singapore, Seoul and Shanghai, as alternatives for both investors and savers worldwide will be observed.

With the successful launch of the ABF in US dollar terms, EMEAP economies will explore the possibility of introducing bonds denominated in local currencies, based on the ABF concept, which could lead to broader and deeper bond markets in the region.

The MPC assessed that the ABF will broaden and deepen the US dollar-denominated sovereign and quasi-sovereign bond markets, becoming an alternative source of funds, reducing the reliance on traditional bank lending. In addition, the ABF initiative is expected to promote developments in domestic bond markets as well as to provide additional tools for conducting more effective monetary policy.