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Asian Dollar Bonds Favored by UOB, Mizuho on Currency Risk (1)
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(Adds fund manager comment at the last paragraph.)

By LilianKarunungan and YumiTeso

Dec. 23 (Bloomberg) -- **Asian dollar bonds may beat domestic notes for a second year in 2012 as central banks cut interest rates to spur economic growth, curbing currency gains, UOB Asset Management Ltd. and Mizuho Securities Co. said.**

The region's global debt has returned 5.3 percent this year, compared with 5.1 percent for local-currency securities in U.S. dollar terms, HSBC Holdings Plc indexes show. The Bloomberg-JPMorgan Asia Dollar Index, which tracks the region's 10-most traded currencies excluding the yen, weakened 1.1 percent in 2011 as Europe's debt crisis sapped demand for emerging-market assets.

"With global growth likely to slow and several Asian central banks expected to ease monetary policy in reaction to slower inflation and economic growth, Asian currencies are unlikely to gain," said Chia Tse Chern, co-head for Asian fixed-income at UOB Asset Management in Singapore, which manages the equivalent of $13.6 billion of assets. "This could depress the performance of Asian local-currency bonds in 2012."

Indonesia is preparing to tap the international market after it was raised to investment grade by Fitch Ratings on Dec. 15. The Philippines is also planning to sell dollar bonds after its outlook was changed to positive by Standard & Poor's the following day. Dollar notes from the Philippines and Indonesia are the best-performing in Asia in 2011, advancing 11 percent and 8.8 percent, respectively, HSBC indexes show.

India's rupee led declines in Asian currencies this year, falling 15 percent against, followed by a drop of 4.2 percent in Thailand's baht and 3.8 percent in Taiwan's dollar.

First Rate Cut

Bank Indonesia was the first major Asian emerging central bank to cut its benchmark interest rate this year, lowering it by 25 basis points in October and 50 basis points to 6 percent the following month. The Bank of Thailand followed in November, reducing its one-day bond repurchase rate by 25 basis points to 3.25 percent.

UOB's Chia said he favors dollar debt from Indonesia and Malaysia. His United Asian Bond Fund returned 6.1 percent in 2011, exceeding the 1.8 percent average among peers.

Implied volatility, a measure of expected foreign-exchange swings used to price options, is climbing. The one-month gauge for South Korea's won averaged 14 percent in the second half from 10.7 percent in the first, while for Indonesia's rupiah it was 11 percent, compared with 6.2 percent in the first half.

Foreign ownership of Indonesian rupiah debt fell 12 percent as of Dec. 20 from a record high of 251.23 trillion rupiah ($28 billion) on Sept. 9, according to finance ministry data. The amount of South Korean fixed-income securities owned by overseas investors fell by 336.9 billion won ($292 million) to 86.7 trillion won in November, the biggest drop since January, the Financial Supervisory Service said on Dec. 4.

Dollar Liquidity Better

Global funds lowered holdings of ringgit bonds by 8 percent to 171.6 billion ringgit ($54 billion) at the end of October from a record high of 186.5 billion ringgit in July, according to Bank Negara Malaysia. Foreign ownership of Thai bonds fell to 6.5 percent of the total in the week ended Dec. 16 from 10.5 percent in the last week of 2010, according to data from the Thai Bond Market Association.

"There's less chance of gains from potential currency appreciation under the current uncertain conditions," said Tadashi Tsukaguchi, senior fund manager at the asset-management office in Tokyo at Mizuho Securities, part of Japan's third- largest bank. "The liquidity of the dollar as a major currency remains better," he said, adding that he thought Asian global debt will beat local-currency bonds in 2012.

HSBC Holdings, Europe's largest lender, recommended in a report on Dec. 14 that clients hold emerging-market hard- currency notes versus local-currency securities as policy makers seek weaker currencies to support growth. Developing economies in Asia will grow 8 percent in 2012, compared with 1.9 percent for advanced nations, according to forecasts from the International Monetary Fund in September.

Widening Spread

The yield on Asia's dollar debt over comparable U.S. Treasuries widened to 238 basis points as of Dec. 21, compared with 165 basis points at the start of 2011, according to JPMorgan Chase & Co.'s EMBI Plus Asia Sovereign Spread index.

"The spread for the dollar bonds has expanded, increasing interest income," said Tatsuya Higuchi, a Tokyo-based senior portfolio manager at Kokusai Asset Management Co., which oversees about $51 billion of assets. He said he favors local-currency debt from India because of its high yield, as well as such securities from Indonesia and the Philippines. Kokusai Global Sovereign Open is Asia's biggest debt fund.

Thomas Kemmsies, the Frankfurt-based head of fixed-income at Nomura Asset Management Co., which managed $288 billion as of October, predicts Asia's dollar debt will do better in the first half before local bonds end "marginally ahead" in 2012.

'Policy Headroom'

"We still believe Asia, in general, has quite a lot of policy headroom to address any cyclical deceleration," said Kemmsies, who manages the Nomura Asian Bonds Fund, which has advanced 4.6 percent in 2011 compared with an 0.08 percent gain among its peers. He said he favors local-currency bonds from Thailand, the Philippines and Taiwan because the relatively low foreign ownership of those notes makes them less vulnerable to sell-offs.

JPMorgan Asset Management predicts domestic Asian debt will outperform in 2012 as near-zero interest rates in the developed world push funds to seek higher yields in Asia.

"We do anticipate the gradual slowing of U.S. growth will lead to more quantitative easing by the Federal Reserve and the situation in Europe will lead to further liquidity injections," said Stephen Chang, Hong Kong-based head of Asian fixed-income at JPMorgan Asset, which oversees $1.3 trillion worldwide. "When those measures are in place, we believe Asian currencies should be outperformers."

Chang, whose JF SAR Asian Bond Fund gained 2.7 percent in 2011 compared with an average of 1.7 percent among its peers, prefers local securities from the Philippines, Indonesia and India, he said.

Hitoshi Ueda, senior fund manager of the fixed income investment group at Sumitomo Mitsui Asset Management Co., which managed about $130 billion at the end of August, also expects local debt to perform better due to their higher yields.

“Among Asian nations, Indonesia looks to be most attractive due to its superior position on economic fundamentals,” Ueda said in an interview last week. Together with its higher yields in the region, “we expect continued fund inflows into Indonesia,” he said.

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--Editors: Andrew Janes, Sandy Hendry

To contact the reporters on this story:
LilianKarunungan in Singapore at +65-6212-1115
orlkarunungan@bloomberg.net;
YumiTeso in Bangkok at +662-654-7315 or
yteso1@bloomberg.net.

To contact the editor responsible for this story:
Sandy Hendry at +852-2977-6608
orshendry@bloomberg.net.