

# Asian Fixed Income Forum

*The inaugural Asian Fixed Income Forums were held in September, keynoted by Hiroto Uehara, Bank of Japan's head of international coordination division, international department. 125 fixed income specialists from private banks, family offices, and independent wealth managers gathered across Hong Kong and Singapore to discuss the outlook for regional and global debt markets — focussing on the topic of ETF implementation in fixed income discretionary strategies.*

*Special thanks to all attendees, speakers, and partners for their continued support. For full details of the event, please visit: <http://apb.events/afi2018>*



## ASIAN FIXED INCOME: A CORE FOR DRIVING THE FUTURE

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# A case for strategic allocation to Asian LC bonds

**H**igher US rates, trade tensions, and widening spreads have generated concern amongst investors about a sell-off in emerging market (EM) debt, but Asian bonds have proven to outperform overall EM debt when markets are challenging, and smart beta ETF wrappers are gaining momentum in this fixed income space.

In partnership with State Street Global Advisors (SSGA), *Asian Private Banker* recently hosted bespoke events in Hong Kong and Singapore centred on the outlook of fixed income in Asia. In addition to investment and trading professionals, more than 10 senior leaders in the discretionary mandate and fund selection domain gathered on a panel to discuss the inclusion of Asian fixed income ETF exposure in the portfolios of Asia's wealthy.

Due to the yield-driven and capital-preservation nature of fixed income, bonds have historically played a dominant role in Asian HNWI's portfolios. Additionally, with a strong home bias, Asian debts have accounted for a significant portion of fixed income allocation.

"Buoyed by favourable demographics, strengthening domestic demand, and increased global competitiveness, Asian economies are exhibiting better growth trends than developed economies," said Kheng-Siang Ng, Asia Pacific head of fixed income at SSGA.

Ng added that in contrast to EM bonds in other regions — such as Latin America and Africa — EM Asian bonds have a lower correlation with riskier assets and are a good diversifier within global asset allocation, setting the asset class apart from its EM peers.

In addition, deteriorating fiscal positions in developed markets drive investors to seek alternative exposure to more stable Asian sovereigns, making the asset class even more attractive from a technical perspective.

### Local currency vs hard currency

On positioning between Asian local currency and hard currency bonds, some private banking veterans expressed concern over foreign exchange and liquidity risks, with one DPM head from a Swiss bank saying "the biggest uncertainty in the local currency space is currency".

However, Ng pointed out that, historically, currencies have been a significant contributor to Asian local currency bond returns, as represented by the iBoxx ABF Pan Asia Index, with rolling 1-year currency returns having contributed 1.65% to the total Asian local currency bond return.

Dwyfor Evans, managing director, head of Asia-Pacific macro strategy, State Street Global Markets, said economic data indicates the global cyclical story is still strong and "real money is far less encumbered by positioning risks in EM".

### ETFs vs active funds

Although Asian trading-minded investors tend to prefer picking their own bonds, SSGA said semi-active smart beta ETFs with an open and transparent product structure provide quicker and easier access to Asian local currency bonds.



An example is the ABF Pan Asia Bond Index Fund (PAIF) managed by SSGA and dual-listed on the Hong Kong and Tokyo stock exchange. The ETF tracks the Markit iBoxx ABF Pan Asia Index, which employs an intelligent indexing approach and allocates exposure according to three factors: market capitalisation, sovereign debt ratings, and investability indicators.

Rather than allocating exposure solely based on market capitalisation (which will result in concentration in a few countries), this modified indexing approach allows for a more diversified and better-balanced portfolio, according to Ng.

In relation to fixed income ETF trading, Viktor Östebro, head of institutional trading at Flow Traders Asia, said investors should not use exchange/ADV to judge an ETF's liquidity.



“Exchange liquidity is not representative of the real liquidity of an ETF,” said Östebro, highlighting that multi-layered liquidity — which includes market liquidity, AUM/shares outstanding, and second market liquidity — enables ETFs to trade stable even in stressed markets, with each ETF at least as liquid as its underliers.

The Asian Bond Fund is a strategic initiative of the Executives' Meeting of East Asia-Pacific and Central Banks (EMEAP) to promote the development of bond markets in the region, Hiroto Uehara, head of international coordination division, international department at Bank of Japan, pointed out during the opening speech. The latest initiative was the launch of PAIF's securities lending programme, with an aim to deepen liquidity in the secondary markets of Asian local currency bonds.

“Proactive efforts [from EMEAP] are becoming increasingly important to further advance money market development [in the region] as demand for short-term transactions may increase in the possible reversal of the financial cycle,” Uehara said.