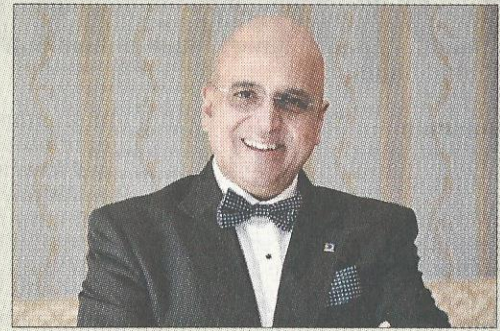
BANKING ON KNOWLEDGE

Banker's Take

Challenging times for capital and bond markets

By Dr R Seetharaman



The concerns of American economy came down after the economy generated 280,000 new jobs in May 2015. It suggests the economy is regaining momentum following a winter slowdown. The unemployment rate edged up to 5.5%, but mainly because more Americans entered the labour market in search of work.

US markets closed lower by the end of last week after the strong jobs data which indicated that the Federal Reserve is likely to raise interest rates in September. In month to date, the Dow Jones Industrial Average dropped by 0.90%, to close at 17,849; the Standard & Poor's 500 dipped 0.69%, to end at 2,093 and the Nasdaq composite dropped by 0.03%, to finish at 5,068. The yield on the US 10-year Treasury soared to as high as 2.43% following the release of the jobs data, about seven basis points higher from where it was ahead of the release. It closed at 2.4076% by end of last week. Brazil's IBOV Index surged by 0.40% in the month to date.

European stock markets came lower by the end of last week as Greece notified the International Monetary Fund that it plans to bundle its loan repayments falling due this month into one payment of $1.7bn. The UK's FTSE 100 index had fallen by 2.6% in the month to date on concerns of Greece and uncertainty over outcome of Opec meeting last week contributed to the fall in the FTSE 100 index last week.

In Frankfurt, the DAX declined 1.90% in the month to date to hit a new 3-month low. In Paris, the CAC40 fell 1.74% in the month to date to hit a new 1-month low. The yield on the benchmark German 10-year bond touched 0.99% last Thursday, its highest level since September after the head of the European Central Bank said markets should get used to volatility. However it later erased the day's rise and fell back to 0.84%. Apart from ECB comments, improving euro zone data, and the possibility of a deal between Greece and its creditors had prompted bond investors to head for the exit, with a lack of market liquidity exacerbating changes in yield and prices. Japan's Nikkei had fallen only by 0.5% in the month to date; it fell on Friday as investors grew cautious before US job data. Japanese government bond prices fell last Thursday, sending the benchmark 10-year yield to 0.50%, its highest level since November, on the back of a rally in global bond yields after the ECB's comments on volatility.

India's Nifty index had fallen by 3.78% in the month to date despite the Reserve Bank of India cutting key repo rate by 25 basis points to 7.25% on account of the hawkish stance by the RBI on further rate cuts and concerns of monsoon. RBI governor Raghuram Rajan said that monetary policy would continue to be data-contingent, warning that a below normal monsoon, global crude prices and external sector risks pose a threat to inflation. The central bank projects inflation at around 6% by January 2016.

MSCI Russia had fallen by more than 5% in the month to date. The volatility in oil prices and a slowdown in the economy created volatility in stocks. The Shanghai index had surged by close to 9% during last week and had climbed above 5000 points, since 2008.

As for the Gulf Cooperation Council markets, on month to date basis, the Qatar Index was up by 0.37%; Dubai up by 2.78%; Abu Dhabi by 1.32%; Saudi Tadawul index down by 0.21%; Kuwait index up by 0.5%, Muscat index up by 1.16% and the Bahrain index up by 0.25%.

The Dubai index surged last week mainly from Amlak shares. The opening of Saudi Arabia's bourse to direct foreign investment may create billions of dollars of business. However regulatory obstacles and uncertainty about the size of fund inflows will result in a cautious approach. The GCC's 5-year CDS rates: Qatar 59.582 basis points; Dubai 193.109 basis points, Abu Dhabi 56.5 basis points, Saudi Arabia 61.695 Basis points and Bahrain 272.85 basis points. The capital and bond markets are impacted by uncertainty in the timing of rate hike by the Fed and Greece debt progress, thereby contributing to drop in indices and swings in bond yields.

The recent comments from the ECB on volatility made the markets more vulnerable and resulted in surge in bond yields. The GCC capital markets are impacted by swings in oil prices, concerns of slowdown in economy and impact on earnings and continue to witness volatility.

On the whole we are witnessing challenging times for capital and bond markets.

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