Equity markets

GCC equities down in 3Q15 on global correction and oil price decline

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GCC markets went through a strong correction in 3Q15, led by Saudi Arabia. The correction wiped out all gains made thus far in 2015, with GCC markets down 14% during the quarter. A strong retreat in Chinese equities, alongside Fed policy uncertainty, triggered a worldwide correction. GCC markets were not spared, especially with oil prices taking another dive. Geopolitically, things have also been stirring. While markets have not had a strong reaction to any one particular event, security concerns have weighed somewhat on general sentiment. Meanwhile, speculation over whether the Fed would hike its policy rate and fears of foreign exchange wars in emerging markets have made equity markets all the more nervous and volatile. In 3Q15, GCC markets shed more than $163 billion in capitalization, which fell to $940 billion at the close of the quarter.

Chinese equities had started correcting towards the end of 2Q15 and not long after, equities around the world followed suit. Stock markets in China had started a strong rally towards the end of 2014. The Shanghai Shenzhen CSI 300 peaked at the end of May 2015, up 107% from October 2014. When economic data began to signal some softening in the Chinese economy, overpriced equities seemed due for a correction. The correction was large, with frequent daily losses above 5%. As authorities attempted to calm markets and prevent a free fall, markets interpreted the government's response as concern over fundamental weaknesses. By the close of 3Q15, the index was off 9% ytd and 38% from its peak.

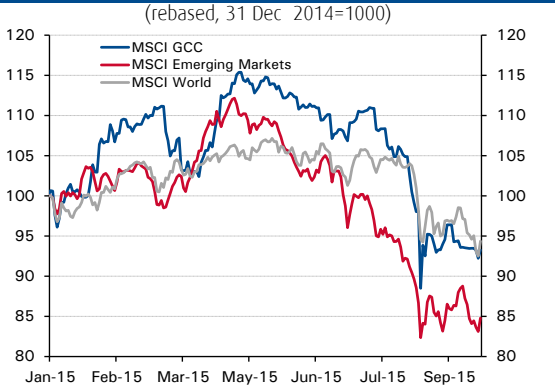
The ripples of the Chinese correction touched equity markets globally with most shedding all their 2015 gains. By the end of 3Q15, the MSCI World total return index was off 6% ytd. The S&P 500 and DJIA total return indices were off 5% and 7% ytd, respectively. European equities, which had rallied for most of 1H15, came under pressure in 3Q15; the MSCI Europe ended the quarter off 5% ytd. GCC markets had their fair share of losses too and the MSCI GCC total return index was down 7% ytd, more or less in line with other markets.

Oil was another driver of regional equity markets since mid-2014 and continued to be so in 3Q15. Oil prices and GCC equities have moved largely in tandem since oil prices started retreating in the 2H14. The relationship has been far from symmetrical with correlations increasing notably when oil prices took a dive, as they did in August. With the exception of the large petrochemical sector in the Saudi stock market, GCC equities have minimal direct exposure to oil markets to warrant such correlation. However, low oil prices do raise concerns about fiscal sustainability and growth in GCC economies. While GCC governments have expressed their commitment to support growth in the non-oil sector by sticking to their current development spending plans, a prolonged period of low oil prices could force governments to reduce capital spending or pressure finances. Indeed, the recent move by the Saudi government to issue bonds ($28 billion this year) to finance the fiscal deficit served to remind markets of these concerns.

The region's geopolitics continued to affect sentiment in GCC

Chart 1: Total return indices

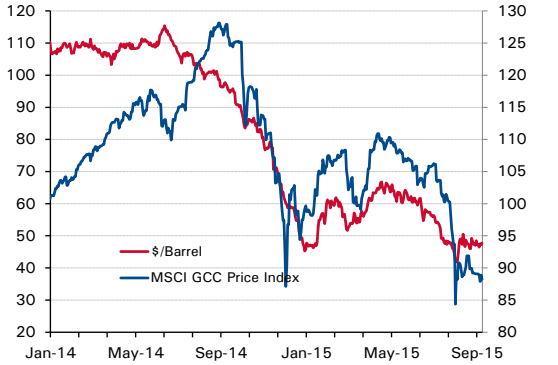
(rebased, 31 Dec 2014=1000)



Source: Thomson Reuters Datastream

Chart 2: Oil prices & GCC markets

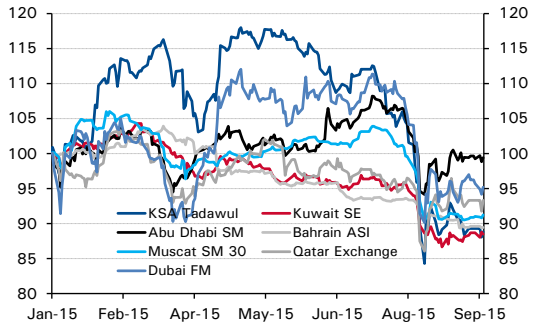
(rebased, 31 Dec 2013=1000)



Source: Thomson Reuters Datastream

Chart 3: GCC markets

(rebased, 31 Dec 2014=1000)



Source: Thomson Reuters Datastream

markets. The bomb attacks in Saudi Arabia and Kuwait, and instability in neighboring countries have elevated security concerns. While the impact on equity markets was not always obvious following any particular event, general market sentiment seemed to continue to be hampered by some security concerns.

GCC markets continued to be pressured by a number of domestic and market specific factors. In the UAE, worries about an imminent correction in the property markets continued to make headlines. In Qatar, the possible revocation of the 2022 World Cup event remains an on/off concern, though there have been no recent developments on that front. In Kuwait, with market liquidity remaining below historic averages and equities trading well below book value, several companies listed on the Kuwait Stock Exchange made requests to delist, though the companies in question were all relatively small and had little impact on market capitalization.

Meanwhile, a few positive events took place that were overshadowed by international market volatility. In Saudi Arabia, the opening up of the market to direct equity ownership by qualified investors came into effect last June. This development and related issues, such as the inclusion of KSA stocks in popular indices and changes in trading and ownership restrictions, should remain catalysts for the Saudi market. Qatar is also likely to benefit from increased foreign investor interest with the upgrading in late 3Q15 of the equity market to emerging market status by FTSE.

Although all GCC markets ended the quarter in the red, Saudi Arabia took by far the biggest hit. The Saudi Tadawul index was off 19% on the quarter, having been the only GCC market to rally earlier in the year on the decision to open up the market to foreign investors. Dubai followed with the DFM price index down 12% during the quarter. The Abu Dhabi and Qatari markets outperformed their regional peers in 3Q15 and were down 5% and 6%, respectively. Part of this was due to the more comfortable fiscal positions of the two, which along with Kuwait are perceived to be less vulnerable to corrections in oil markets. The Omani, Kuwaiti and Bahraini markets were down 10%, 8% and 7%, respectively.

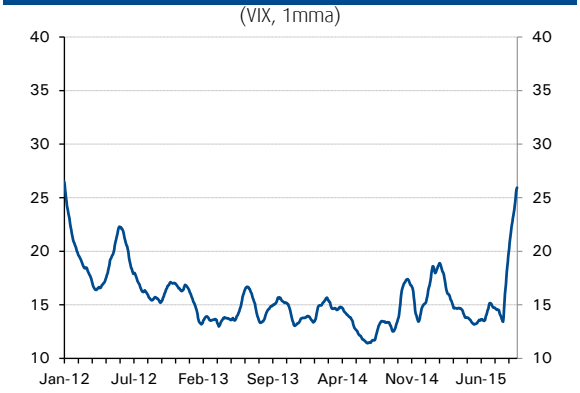
Though anticipated by most for this year, market volatility hit with a vengeance in 3Q15 (Chart 4), and some of its sources remain: China and the Fed in particular. Certainly, the Fed's decision not to hike rates in September confused markets and elevated concerns about the fragility of world markets and of the US recovery. In light of the soft US September employment report, the Fed should now be on hold for the rest of this year. The Chinese economy will also remain a focus for world markets, as investors continue to monitor the flow of data from the world's second largest economy. Regionally, geopolitical developments are fluid. Russia's renewed involvement in the region will need to be assessed. Attention will also turn to 3Q15 earnings announcements. All the while, oil prices will remain an important driver for GCC equities in the coming months, especially should China or US growth disappoint further. Otherwise, GCC economies are in good shape and should outperform, certainly in their non-oil sectors.

Table 1: GCC market capitalization

	Capitalization (as of 30 Sep 2015)	
	USD bn	% ytd
Abu Dhabi (ADSM)	116	2
Bahrain (BSE)	20	-11
Dubai (DFM)	89	4
Saudi Arabia (Tadawul)	444	-8
Kuwait (KSE)	85	-11
Muscat (MSM)	23	-5
Qatar (QE)	167	-10
GCC	**940**	**-7**

Source: Zawya

Chart 4: Volatility Index



Source: Thomson Reuters Datastream

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