Benefits and functions of money market economics essay

Economics

Money Market is part of financial market from where the various instruments of high liquidity and short term maturity are traded for the purpose of business, trade and other reasons. Hence, money market is a market where short term obligations such as treasury bills, commercial papers and banker's acceptances are bought and sold.

Benefits and functions of Money Market:

Money markets exist to facilitate efficient transfer of short-term funds between holders and borrowers of cash assets. For the lender/investor, it provides a good return on their funds. For the borrower, it enables rapid and relatively inexpensive acquisition of cash to cover short-term liabilities.

Money Market & Capital Market:

Money Market is a place for short term lending and borrowing, typically within a year. It deals in short term debt financing and investments. On the other hand, Capital Market refers to stock market, which refers to trading in shares and bonds of companies on recognized stock exchanges. Individual players cannot invest in money market as the value of investments is large, on the other hand, in capital market, anybody can make investments through a broker. Stock Market is associated with high risk and high return as against money market which is more secure. Further, in case of money market, deals are transacted on phone or through electronic systems as against capital market where trading is through recognized stock exchanges

An introduction to Bahrain's money market:

Bahrain's democratic reform process has come to a standstill since 2009, which marked the 10th anniversary of King Hamad bin Isa Al Khalifa's accession to power. The positive developments in civil and political liberties observed with the start of the reform process in 2002 have in recent years been counteracted by repressive state tactics in which freedoms of expression and assembly have suffered most. Aside from a few small positive steps taken towards supposed democratic reform (such as the new labor law or some small changes to the rules of parliament), Bahrain remains an authoritarian state. However, promising developments have again been noted in terms of economic reform. The impact of the global economic downturn has slowed but not halted overall economic growth in Bahrain during the period under review. Thanks to prudent regulation by the authorities, the country’s economic recovery and macroeconomic stability seem to have consolidated by the end of 2010. The government has continued to implement measures to realize the country’s " Vision 2030" long-term economic development plan, designed to improve living standards by building a competitive, diversified economy.

History and Characteristics of Transformation in the money market:

When current King Sheikh Hamad bin Isa Al Khalifa came to power in 1999, Bahrain initiated an economic and political reform process. The regime has undertaken serious efforts to diversify the country’s economy. In addition to oil, financial services followed by weekend tourism from neighboring Gulf States and industrial production (e. g., aluminum, petrochemicals, ship repairing, manufacturing) have become important sources of revenues. Because these sectors proved susceptible to repeated political unrest in the 1990s, the ruling elite initiated a gradual top-down process of political liberalization. Privatization has been eagerly pursued, although the economy today remains state-dominated. The entangled problems of an unjust distribution of wealth and the predominance of the public sector have been discussed frankly in public. The government’s official long-term development plan launched in 2010, Vision 2030, will help the country move away from its dependency on finite oil reserves that are subject to market volatility. It aims to build a competitive, sustainable economy designed to improve living standards by strengthening other strategic sectors and the Bahraini skill pool

Economic Performance of Bahrain’s money market:

Bahrain’s economic performance is good, but, like everywhere else, the global economic downturn affected the national economy. Lower regional growth and a decline in foreign direct investment (FDI) and trade flows reduced economic expansion in 2009 to 3. 1%, generating a nominal GDP of $19. 319 billion, down from 6. 3% growth or $21. 902 billion in 2008, according to data released by the Central Bank of Bahrain. The fact that the economy still grew in 2009 is noteworthy given weak global demand, the sharp decline in oil and aluminum prices, and the weakness of the construction sector. Accordingly, GDP per capita remained high by world standards at $34, 955 in 2008 (the latest figure available). Due to the global recession and the downturn of the local real estate market, FDI inflows fell in 2009 to 96. 7 million dinar ($257 million, down from 674. 5 million dinar in 2008) but remained positive. The housing sector was highly affected by the financial crisis with fewer homeowners willing to take on further mortgages. Bahrain’s trade balance remained positive during the period under review, with an estimated surplus of $1. 702 billion in 2009 and $2. 182 billion forecasted for 2010. As the economic recovery was consolidating by the end of 2010, the IMF estimated a GDP growth of 4% in 2010 and predicted an acceleration to 5% in 2011 thanks to higher oil prices and careful management of the economy by the government and the central bank. These figures appear high by world standards but become less impressive when the high population growth rate is taken into account (according the official 2010 census, the Bahraini population grew by 5. 8% annually from 2008 to 2010). Actually, population growth seems to be exceeding economic growth, implying a decline in real incomes. According to Bahrain's Labor Market Regulatory Authority, total employment grew by 4. 4% in 2009, the slowest rate since 2002. As figures from the Ministry of Finance suggest, unemployment fell from 3. 8% in 2009 to 3. 7% by March 2010,

Latest developments in Bahrain:

During 2010, the global economy underwent a recovery as world output and financial markets rebounded. World output grew by 5. 0% compared to a contraction of 0. 5% in 2009. The projections for 2011 and 2012 show that the world economy will continue to grow, but with more modestly, with growth rates of 4. 4% and 4. 5% respectively. In line with the rise in global output, consumer price inflation (CPI) increased in 2010 and is expected to increase further in 2011. Inflation in advanced economies grew by 1. 6%, up from 0. 1% in 2009. Consumer prices in emerging and developing markets increased by 6. 2% during the year, higher than the 5. 2% recorded in 2009. The IMF forecasts that in 2011 there will be a 2. 2% growth in consumer prices for advanced economies, whilst the inflation rate in developing economies is expected to be 6. 9% Interest rates remained low in 2010 due to monetary authorities' attempts to ease liquidity strains on their respective financial systems and are not expected to rise significantly in 2011. With the international economy well into recovery in 2010, global equity markets continued their path to improvement which began in the second half of 2009. The GCC was fortunate in experiencing a relatively limited impact of the US sub-prime financial crisis. With the recovery in the global economy and rising oil prices, prospects for the GCC region are estimated to have improved in 2010 and are expected to continue to improve in 2011. For the year 2010, real GDP growth for the GCC is estimated to have accelerated to 4. 5%, compared with 0. 4% in 2009. Inflation is also expected to increase to 4. 2% in 2010 from 3. 2% in 2009 and is projected to remain at that level in 2011. In line with the rise in oil prices, total revenue for the GCC is projected to increase to 42. 9% of GDP in 2010 and is expected to grow further to 43. 6% of GDP in 2011. On the other hand, the non-oil fiscal deficit is estimated to have increased to 54. 6% of non-oil GDP in 2010, as non-oil revenue declined to 20. 8% of non-oil GDP for the same year. In 2010, Bahrain's economy recovered, registering a positive 1118% nominal GDP growth rate after experiencing a negative growth rate in 2009. Real GDP also grew by 4. 5% in 2010. This economic recovery can be attributed to a rebound in the financial sector along with the rising oil prices experienced in the second half of 2010. Inflation decreased from 2. 8% in 2009 to reach 2. 0% in 2010, influenced in part by the general fall in rents in Bahrain. Total employment increased by 5. 2% in 2010, higher than the 3. 2% increase in 2009, due mainly to the increase in private sector employment. Although the Bahraini economy has diversified away from oil, oil revenues continue to play a significant role in the government's fiscal balance. Oil prices increased significantly during the year 2010, and as a result, government revenues increased by 27. 4%, though expenditures increased by 26. 6% during the year. As a result of these developments, Bahrain recorded a fiscal deficit of BD 459. 8 million (5. 6% of GDP) before rollovers of maturing debt. Money supply continued to grow in 2010, at a similar pace to 2009. M1 (currency in circulation plus demand deposits) grew by 6. 7% from BD 2, 158. 3 million in 2009 to BD 2, 303. 9 million in 2010. M2 (M1 plus time and savings deposits) rose by BD 748. 2 million (10. 5% increase) from BD 7, 119. 3 million at end 2009 to BD 7, 867. 5 million at end 2010. With global monetary policy remaining accommodative, interest rates in Bahrain remained low, in line with the operation of the currency peg. The depreciation of the US dollar, to which the Bahraini Dinar is pegged, resulted in a decrease in the real effective exchange rate against other major currencies. The financial sector continues to be the largest contributor to Bahrain's economy, accounting for 24. 6% of real GDP in 2010. The total assets of retail banks (including foreign assets) stood at BD 24, 610. 3 million at end-December 2010, an increase of BD 2, 149. 7 million or 9. 6%. Total outstanding credit facilities by retail banks amounted to BD 5, 676. 6 million at end-2010, down 3. 5% from the BD 5, 884. 9 million at end-2009 mainly due to a 4. 0% decrease in outstanding facilities to the business sector. The consolidated balance sheet for wholesale banks shrank in 2010. Aggregate data indicates that total wholesale bank assets decreased by 3. 3% to reach USD 156. 7 billion at the end of 2010, down from USD 162. 1 billion at end of 2009. The current account surplus expanded from BD 210. 6 million in 2009 (2. 9% of GDP) to

BD 289. 5 million in 2010 (3. 5% of GDP). The capital and financial account registered a net outflow of BD 329. 8 million in 2010, compared with an outflow of BD 185. 9 million in 2009. The net international investment position rose from BD 6, 028. 8 million at the end of 2009 to BD 6, 375. 0 million in 2009. Globally, major financial markets continued to recover in 2010, but at a substantially slower pace than in 2009. The US market performed well while European stock markets were held back by sovereign debt concerns in the Euro area, although Germany and the U. K were exceptions and finished at two-year highs. The performances of stock markets in the GCC region ended the year on a mixed note. The Bahrain All Share Index posted a year on year decrease of 1. 8% in 2010 closing at 1, 432. 26 points. In 2010, Bahrain's long term foreign and local currency debt ratings were unchanged by both Fitch Ratings Agency and Standard and Poor's1 Fitch reaffirmed Bahrain's rating for long term foreign currency debt at " A" (with a stable outlook) in 20101 Local currency debt ratings remained at " A+" (stable) Standard and Poor's ratings for foreign and local currency debt also remained unchanged at " A" (stable) in 2010

Conclusion:

The money market of Bahrain has performed very well and remains immune of the global activities. In the coming years, the country expects a regular growth level to be achieved without affecting the money market which is getting disturbed again at the global levels.