



Financial Stability Directorate

Monetary and Financial Trends

Second Quarter 2010

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Monetary and Financial Trends is produced quarterly by the Financial Stability Directorate, Central Bank of Bahrain. This edition focuses on the Second Quarter of 2010 and highlights developments in the following monetary and financial indicators: i) monetary aggregates; ii) domestic credit; iii) interest rates; iv) domestic prices; v) public debt; vi) exchange rates; vii) official reserves; and viii) the stock market.

Highlights

Monetary Aggregates

- During 2010:Q2, *narrow money* (M1) increased by 8.7%. In addition, *broad money* (M2) increased by 6.1%.
- *Demand deposits* were the fastest growing component of the money stock during the quarter, growing at 9.9%. *Savings and time deposits* grew by 4.9%, followed by *Currency outside banks* which also increased by 1.7%.

Credit Developments

- Total domestic credit fell by 1.1% to reach BD 5,700.5 million.
- Private sector credit *decreased* by 1.7% while lending to general government increased by 8.0%.
- An analysis of private sector credit components shows that *personal loans* grew by 5.4% in comparison to the 6.3% drop experienced in the first quarter of 2010.
- Loans “With Salary Assignment” constituted the bulk of personal loans (52.5% of the total). This was followed by loans “Secured by Property Mortgage” which made up 19.8% of total personal loans.
- *Business loans* decreased by 4.6% during the quarter following a 0.2% drop in the previous quarter.
- *Business loans* went primarily to the “construction and real estate” segment, which accounted for 48.6% of total business loans.

Interest Rates

- Short-term interest rates witnessed some decreases during the quarter.
- The 3-month and 6-month inter-bank rates remained at 1.3% and 1.6% respectively. The 3-month and 6-month Treasury bill rates decreased to reach 0.8% and 0.9% respectively.
- The CBB key policy rate remained unchanged at 0.50% at the end of the quarter.

Domestic Prices

- Inflation numbers show that the *consumer price index* continued to increase, however at a slower rate of 0.4%.
- *Year-on-year* inflation was 2.5%.

Public Debt

- The stock of outstanding public debt (securities only) increased during the quarter to reach BD 1,981.0 million.
- Public debt increased mainly due to the growth in the outstanding balance of treasury bills to BD 560.0 million.
- Islamic leasing securities also increased to reach BD 860.0 million from its recorded BD 845.0 million.

Exchange Rates and Official Reserves

- During the second quarter, the Bahraini dinar appreciated against the Euro and the Swiss Franc while it depreciated against the Pound Sterling and Japanese Yen.
- Available data on Bahrain's *Real Effective Exchange Rate* (REER) (2005=100) shows that the Bahraini dinar appreciated against a basket of major world currencies. During 2010:Q2, the REER increased to reach an index value of 99.7 points up from the 96.2 points registered in the previous quarter.
- During 2010:Q2, official reserves decreased to reach BD 1,987.7 million, however this is still 40.4% higher than the level attained during the same period of 2009.

Stock Market

- Total market capitalisation decreased by 5.9% to reach BD 6,122.5 million, compared to BD 6,509.1 million registered last quarter. Year-on-year, market capitalisation was 5.6% lower.
- The decrease in market capitalisation was mainly due to the decrease in the *commercial banks* segment, which fell by 9.0%.
- The BSE All-Share Index decreased to 1,396.29 points during 2010:Q2, compared to 1,547.13 points in the first quarter of 2010.
- Liquidity decreased marginally during the quarter, with the turnover ratio decreasing to 0.4%.

1. Monetary Aggregates¹

In the second quarter of 2010, *narrow money* (M1) increased by 8.7%, following a 2.3% increase witnessed in the first quarter of 2010 (Table 1). *Year-on-year*, the level of M1 was 9.6% higher than its level for 2009:Q2. *Broad money* (M2) also increased by 6.1% during 2010:Q2 compared to a 1.7% increase in 2010:Q1. *Year-on-year*, the level of M2 was 13.8% higher than its level last year.

Table 1: Developments in Monetary Aggregates

(BD Million)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
M1	2,187.9	2,057.6	2,158.3	2,207.0	2,398.9
<i>M1 Growth (%)</i>	<i>5.1</i>	<i>-6.0</i>	<i>4.9</i>	<i>2.3</i>	<i>8.7</i>
M2	6,745.6	6,729.5	7,119.3	7,236.9	7,677.3
<i>M2 Growth (%)</i>	<i>-0.6</i>	<i>-0.2</i>	<i>5.8</i>	<i>1.7</i>	<i>6.1</i>

Source: Central Bank of Bahrain

Table 2 presents data on the different components of the money supply, providing further insight into the driving forces behind the movements in M1 and M2.

The growth in M1 in the second quarter of 2010 was mainly a result of a 9.9% increase in demand deposits. In addition, the 4.9% increase in saving and time deposits contributed to the growth in M2.

Table 2: Developments in Components of Money Supply

(BD Million)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
Currency Outside Banks	318.9	317.2	323.0	330.8	336.3
<i>Growth Rate (%)</i>	<i>3.7</i>	<i>-0.5</i>	<i>1.8</i>	<i>2.4</i>	<i>1.7</i>
Demand Deposits	1,869.0	1,740.4	1,835.3	1,876.2	2,062.6
<i>Growth Rate (%)</i>	<i>5.3</i>	<i>-6.9</i>	<i>5.5</i>	<i>2.2</i>	<i>9.9</i>
Savings and Time Deposits	4,557.7	4,671.9	4,961.0	5,029.9	5,278.4
<i>Growth Rate (%)</i>	<i>-3.1</i>	<i>2.5</i>	<i>6.2</i>	<i>1.4</i>	<i>4.9</i>

* Central government and the Social Insurance system

Source: Central Bank of Bahrain

¹ M1 is the sum of currency in circulation and demand deposits. M2 equals M1 plus savings and time deposits.

Table 3: Contributions to Monetary Growth

(% Change)

	2009:Q2	2009:Q3	2009:Q4	2010: Q1	2010: Q2
Net Foreign Assets (NFA)	-0.5	5.9	-5.1	20.3	0.9
Central Bank of Bahrain	-3.5	8.5	-10.4	49.6	-5.7
Retail Banks	6.1	0.8	5.9	-31.0	26.1
Domestic Assets	0.2	0.1	5.4	-1.3	10.4
Claims on Government	9.3	22.3	5.3	-4.7	10.5
Claims on Private Sector	0.3	-1.3	1.8	-2.2	6.6
Other Assets (net)	-8.4	-12.0	11.7	10.3	11.2

Source: Central Bank of Bahrain

In the second quarter of 2010, net foreign assets (NFA) increased slightly by 0.9% compared to the 20.3% increase in 2010:Q1 (Table 3). The growth in NFA during 2010:Q2 was driven mainly by a 26.1% increase in claims on retail banks.

In addition, domestic assets increased by 10.4% during the quarter compared to the 1.3% decrease in the last quarter. This was due to increases in claims on government and claims on the private sector by 10.5% and 6.6% respectively. Other assets (net) decreased for the period by 11.2%.

Assets exceeded liabilities on the “other assets (net)” category. However, the net deficit has been narrowing for the last three quarters. Other assets (net) for 2010:Q2 narrowed by 11.2%.

2. Credit Developments

During 2010:Q2, total domestic credit decreased by 1.1% to reach BD 5,700.5 million, further to a 2.1% decrease registered in the previous quarter (Table 4). This contraction is mainly a result of a 1.7% decrease in credit to the private sector, down from the 2.0% decrease experienced in 2010:Q1. On the other hand, credit to general government increased by 8.0% compared to the 3.0% decrease in the previous quarter.

Table 4: Trends in Domestic Credit

(BD Million)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
Total Domestic Credit	5,860.5	5,756.5	5,884.9	5,761.4	5,700.5
<i>Growth (%)</i>	<i>0.6</i>	<i>-1.8</i>	<i>2.2</i>	<i>-2.1</i>	<i>-1.1</i>
Credit to General Government	337.4	319.3	392.0	380.4	410.7
<i>Growth (%)</i>	<i>11.4</i>	<i>-5.4</i>	<i>22.8</i>	<i>-3.0</i>	<i>8.0</i>
Credit to Private Sector	5,523.1	5,437.2	5,492.9	5,381.0	5,289.8
<i>Growth (%)</i>	<i>0.05</i>	<i>-1.6</i>	<i>1.0</i>	<i>-2.0</i>	<i>-1.7</i>
Memo Items					
Share of Private Sector Credit	94.2	94.5	93.3	93.4	92.8
Share of Public Sector Credit	5.8	5.5	6.7	6.6	7.2

Source: Central Bank of Bahrain

On a *year-on-year* basis, total domestic credit decreased by 2.7%. Private sector credit shows a similar pattern, with year-on-year reduction of 4.2%.

In terms of composition, the private sector continues to receive the bulk of domestic credit, accounting for 92.8% of total private sector credit during the second quarter. Compared to the same period last year, this share has decreased significantly, where it accounted for 94.2% of total private sector credit in 2009:Q2.

A breakdown of private sector credit indicates that lending to business contracted during the second quarter, decreasing by 4.6% following the 0.2% decrease recorded during 2010:Q1 (Table 5). Personal loans experienced an expansion by 5.4% in 2010:Q2 compared to a 6.3% decrease during the previous quarter. Year-on-year, Business and personal loans reduced by 5.8% and 0.5% respectively for the same period.

Table 5: Trends in Retail Private Domestic Credit

(BD Millions)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2	2010:Q2 Growth (%)
BUSINESS	3,860.0	3,740.7	3,816.6	3,809.7	3,634.3	-4.6
--Manufacturing	401.8	367.0	389.5	379.5	448.2	18.1
--Mining and Quarrying	13.1	6.9	7.7	7.8	7.2	-7.7
--Agriculture, Fishing and Dairy	5.5	5.2	5.4	6.7	5.7	-14.9
--Construction and Real Estate	1,576.7	1,604.9	1,659.5	1,654.9	1,767.4	6.8
--Trade	1,057.1	1,017.8	998.7	968.6	726.9	-25.0
--Non-bank Financial	268.5	231.7	211.3	233.6	224.3	-4.0
--Transport and Communication	132.4	137.4	178.3	171.9	113.1	-34.2
--Hotels and Restaurants	72.1	72.8	65.2	67.4	64.7	-4.0
--Other Sectors	332.8	297.0	301.0	319.3	276.8	-13.3
PERSONAL	1,663.1	1,696.5	1,676.3	1,571.3	1,655.5	5.4
--Secured by Property Mortgage	342.9	349.0	360.3	337.4	327.6	-2.9
--Secured by Vehicle Title	129.8	149.5	138.3	135.4	120.3	-11.2
--Secured by Deposits	25.1	26.7	26.9	25.5	26.6	4.3
--With Salary Assignment	868.9	901.5	890.6	843.9	869.5	3.0
--Credit Card Receivables	76.6	79.7	52.0	51.5	51.7	0.4
Other	219.8	190.1	208.2	177.6	259.8	46.3
TOTAL	5,523.1	5,437.2	5,492.9	5,381.0	5,289.8	-1.7

Source: Central Bank of Bahrain

Table 5 also presents a breakdown of lending to the private sector by activity. Outstanding personal loans stood at BD 1,655.5 million at the end of 2010:Q2, accounting for 31.3% of total outstanding private sector credit. Personal loans “with salary assignment” represented the largest proportion of total personal loans (52.5%) during the quarter. Personal loans “secured by property mortgage” were the next largest component of total personal loans, accounting for 19.8%.

The growth in total personal loans outstanding in 2010:Q2 was mainly due to the 46.3% increase in “other” personal loans.

Business loans outstanding stood at BD 3,634.3 million in 2010:Q2, representing 68.7% of outstanding private sector credit. Loans to the “construction and real estate” segment accounted for the largest share of business loans (48.6%), followed by “trade” at 20.0%.

Although overall business loans contracted in 2010:Q2 some of its segments experienced increases such as “manufacturing” and “construction and real estate” (18.1% and 6.8% respectively). However, the largest drop was in “transport and communication” which contracted by 34.2% followed by “trade” which decreased by 25.0%.

3. Interest Rates

Most of the short-term interest rates witnessed a decrease for the quarter. The 3-month and 6-month inter-bank rates staid nearly the same at 1.3% and 1.6% respectively in 2010:Q2. Moreover, the 3-month and 6-month Treasury bill yield decreased to reach 0.8% and 0.9% respectively in the second quarter of 2010. The CBB key policy rate remained unchanged for the quarter at 0.50%.

Table 6: Structure of Interest Rates

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
3 Month Inter-bank Rate (BHIBOR)*	1.6	1.4	1.3	1.3	1.3
6 Month Inter-bank Rate (BHIBOR)*	2.0	1.6	1.5	1.5	1.6
CBB Key Policy Rate (end-of-quarter)	0.75	0.50	0.50	0.50	0.50
3 Month Treasury Bill Yield	1.1	0.8	0.9	0.9	0.8
6 Month Treasury Bill Yield	1.3	0.8	1.0	1.1	0.9
Commercial Bank Lending Rate— Personal**	8.1	7.7	7.7	7.7	7.1
Commercial Bank Lending Rate— Business**	6.9	6.8	6.8	6.8	5.6
Commercial Bank Deposit Rate (3-12 mths)**	1.5	1.7	1.4	1.4	1.1

*BHIBOR was introduced in December 2006

** Weighted averages of rates during the last month of each quarter

Source: Central Bank of Bahrain

The weighted average lending rate for business loans and personal loans decreased for the quarter to reach 5.6% and 7.1% respectively. Average deposit rates (3-12 months) also decreased and registered a 1.1% for the same period.

Because of the above decreases, the spread between personal loan and deposit rates narrowed from 6.3% in 2010:Q1 to 6.0% in 2010:Q2, an indication that loan rates decreased faster than deposit rates. Similarly, the spread between business loan and deposit rates also narrowed from 5.4% in 2010:Q1 to 4.5% in 2010:Q2.

4. Domestic Prices

Inflation numbers for 2010:Q2 show that the consumer price index continued to increase during the quarter, although this was at a slower pace by 0.4% following a 0.9% growth in 2010:Q1. *Year-on-year*, inflation stands at 2.5%, up from 1.8% in 2010:Q1 (Table 7).

Table 7: Consumer Price Index

(2006=100)

Major Group of Commodities	2009:Q2*	2009:Q3*	2009:Q4*	2010:Q1*	2010:Q2*
Food and non-alcoholic Beverages	125.0	126.0	127.1	130.8	134.1
Alcoholic beverages & Tobacco	107.3	114.6	116.2	117.3	117.3
Clothing & Footwear	104.5	105.3	104.3	105.1	106.3
Housing, Water, Electricity & Fuels	109.5	109.5	109.5	109.0	107.9
Household Goods & Services	111.5	112.5	112.7	112.5	112.2
Healthcare Services	101.6	102.3	103.6	104.3	105.8
Transport	101.6	101.4	102.9	104.4	105.8
Communication	98.3	94.9	94.9	94.9	94.9
Recreation & Culture	105.3	105.4	105.4	105.4	105.5
Education	103.6	106.3	111.7	111.7	111.7
Restaurants	106	106	108.2	112.7	112.9
Miscellaneous	114.5	114.7	116.5	117.5	117.0
General Index	109.4	109.7	110.7	111.7	112.1
Growth rate (%)	-0.3	0.3	0.9	0.9	0.4
Inflation (Year on Year)	3.1	2.1	1.4	1.8	2.5

*Quarterly averages

Source: Central Informatics Organisation

On a year-on-year basis² prices for “alcoholic beverages & tobacco” increased by 9.3%, the largest increase among the segments. “education” and “food and non-alcoholic beverages” followed increasing by 7.8% and 7.3% to reach an average of 111.7 and 134.1 index points respectively. For the same period, “communication” decreased by 3.5% to reach 94.9 index points.

During the latest quarter, the highest price rise was in the “food and non-alcoholic beverages” segment, which grew on average by 2.5%, this was followed by the “healthcare services” segment, which experienced a price increase of 1.4%.

5. Public Debt

The size of Bahrain’s outstanding public debt (securities only) increased to BD 1,981.0 million during the second quarter of 2010, compared to BD 1,871.0 in the previous quarter. Public debt as a percentage of 2009 nominal GDP also rose to 25.6% higher than the 24.2% registered at the end of 2010:Q1 (Table 8).

Table 8: Public Debt Outstanding

(BD Millions)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
Total Outstanding	1,038.0	1,203.0	1,348.0	1,871.0	1,981.0
--% of GDP	12.6	14.6	16.4	24.2	25.6
Development Bonds	0.0	0.0	55.0	525.0	525.0
Treasury Bills	325.0	325.0	415.0	465.0	560.0
Islamic Leasing Securities	695.0	860.0	860.0	845.0	860.0
Al Salam Islamic Securities	18.0	18.0	18.0	36.0	36.0

Source: Central Bank of Bahrain

The outstanding balance of treasury bills increased to reach BD 560.0 million, with BD 360.0 million in new treasury bills issued. Islamic leasing securities also increased to reach BD 860.0 million. However, the outstanding balance of the development bonds and Al Salam Islamic securities outstanding remained unchanged at BD 525.0 million and 36.0 million respectively for the quarter.

² Year-on-year comparisons for the CPI use average quarterly data.

6. Exchange Rates and Official Reserves

During 2010:Q2, the Bahraini dinar appreciated against the Euro and the Swiss Franc while it depreciated against the Pound Sterling and the Japanese Yen (Table 9).

Table 9: BD Exchange Rates Against Selected Currencies*

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
US Dollar	0.376	0.376	0.376	0.376	0.376
Pound Sterling	0.625	0.603	0.604	0.566	0.567
Euro	0.530	0.550	0.540	0.503	0.459
Japanese Yen**	3.940	4.200	4.070	4.020	4.240
Swiss Franc	0.348	0.364	0.363	0.352	0.348

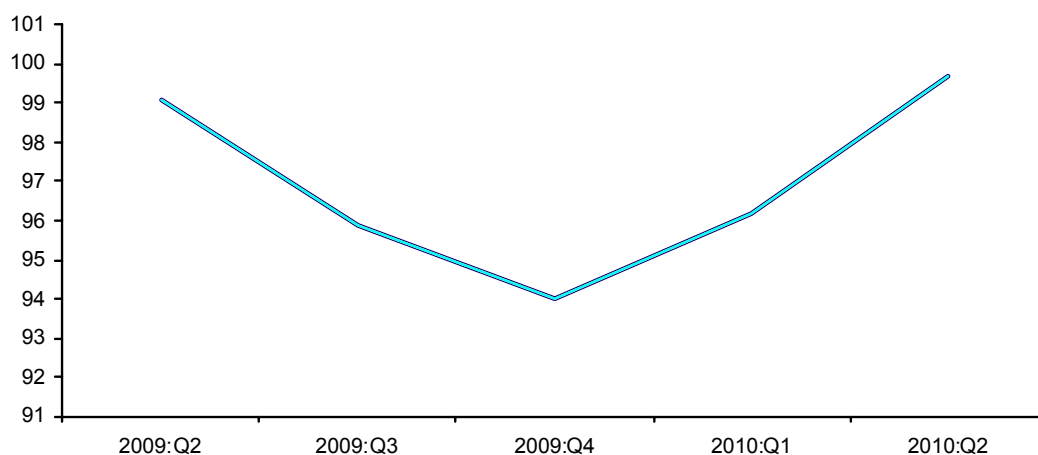
*Last working day of each period

** Per 1000 units

Source: Central Bank of Bahrain

Available data on Bahrain's Real Effective Exchange Rate (REER) (2005=100) shows that after a period of steady decline since 2009:Q1, the REER began to increase to reach an index value of 99.7 points in 2010:Q2, up from the 96.2 points recorded in the first quarter of 2010 (Chart 2).

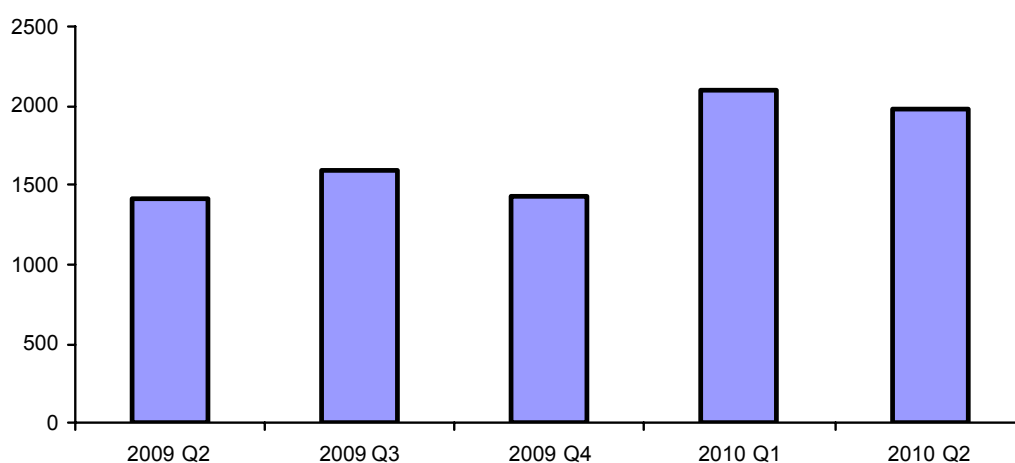
**Chart 1: Trends in Real Effective Exchange Rates
(2005=100; period averages)**



Source: IMF, International Financial Statistics

During the second quarter of 2010, official reserves decreased with the total level of reserves (gold, foreign exchange, SDR and IMF reserve position) standing at BD 1,987.7 million at the end of the quarter (Chart 3). This was 5.5% lower than the level attained at the end of the first quarter of 2010 and 40.4% higher than the level registered in Q2: 2009.

Chart 2: Trends in Official Reserves—2009:Q2-2010:Q2 (BD Million)*



*Includes holdings of gold, foreign currencies, SDR and reserve position at the IMF
Source: Central Bank of Bahrain

7. The Stock Market

During 2010:Q2, total market capitalisation of the Bahrain Stock Exchange (BSE) decreased by 5.9% to reach BD 6,122.5 million, compared to BD 6,509.1 million registered in the last quarter (Table 10). Year-on-year, market capitalisation was 5.6% lower. The decrease in market size during 2010:Q2 was mainly due to the decrease in the “commercial banks” segment, which fell by 9.0%.

Table 10: Market Capitalisation on the Bahrain Stock Exchange*

(BD Million)

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2	2010:Q2 Growth (%)
Commercial Banks	2,206.6	2,267.8	2,038.5	2,504.1	2,279.3	-9.0
Investment	2,789.7	2,624.1	2,546.6	2,439.4	2,357.0	-3.4
Insurance	166.1	168.3	173.3	182.0	169.7	-6.8
Services	1,148.4	1,166.4	1,178.8	1,188.3	1,125.2	-5.3
Industrial	13.6	17.5	17.7	16.6	16.6	0.0
Hotel and Tourism	158.3	156.6	176.2	178.7	174.6	-2.3
TOTAL	6,482.8	6,400.7	6,131.0	6,509.1	6,122.5	-5.9

*end of quarter numbers

Source: Bahrain Stock Exchange

The BSE All-Share Index dropped to 1,396.29 points in 2010:Q2 (compared to 1,547.13 in 2010:Q1) (Table 11). Measured year-on-year, the index level during 2010:Q2 was 11.7% lower than the corresponding figure for 2009:Q2.

Table 11: Sectoral Indices of Bahrain All-Share Index*

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
Commercial banks	1,839.84	1,867.97	1,679.17	2,063.43	1,878.19
Investment	1,359.10	1,278.12	1,173.53	1,121.20	969.37
Insurance	1,867.73	1,859.76	1,915.92	2,014.72	1,875.97
Services	1,513.66	1,537.38	1,553.69	1,566.31	1,483.15
Industrial	1,179.04	1,514.37	1,529.80	1,435.75	1,435.75
Hotel and Tourism	2,954.42	2,922.18	3,287.74	3,333.42	3,257.41
OVERALL INDEX	1,581.67	1,554.51	1,458.24	1,547.13	1,396.29

*end of quarter numbers

Source: Bahrain Stock Exchange

Liquidity on the BSE decreased marginally during 2010:Q2, with the turnover ratio (value of trading as a share of market capitalisation) standing at 0.4% (Table 12). For the same period, the “commercial banks” and “services” segments represented 44.9% and 23.8% of the total value of shares traded respectively.

Table 12: Liquidity on the BSE

	2009:Q2	2009:Q3	2009:Q4	2010:Q1	2010:Q2
A. Overall Market Liquidity (BD Million)					
Value of Shares Traded	64.7	37.6	49.9	44.3	25.9
Market Capitalisation	6,482.8	6,400.7	6,131.0	6,509.1	6,122.5
Turnover Ratio*	1.0	1.0	0.8	0.7	0.4
B. Value of Shares Traded by Sector (% Shares)					
Commercial Banks	55.9	61.4	60.1	26.3	44.9
Investment	27.7	12.5	19.9	50.9	16.7
Insurance	0.9	0.6	0.5	7.0	14.3
Services	14.8	17.4	18.5	15.5	23.8
Industrial	0.0	0.1	0.0	0.0	0.0
Hotel and Tourism	0.6	1.3	0.8	0.4	0.3

*Turnover ratio is calculated as value of shares traded as a percentage of total market capitalisations

**Figures may not add to a hundred due to rounding

Source: Bahrain Stock Exchange