



Stock market volatility and investment opportunities

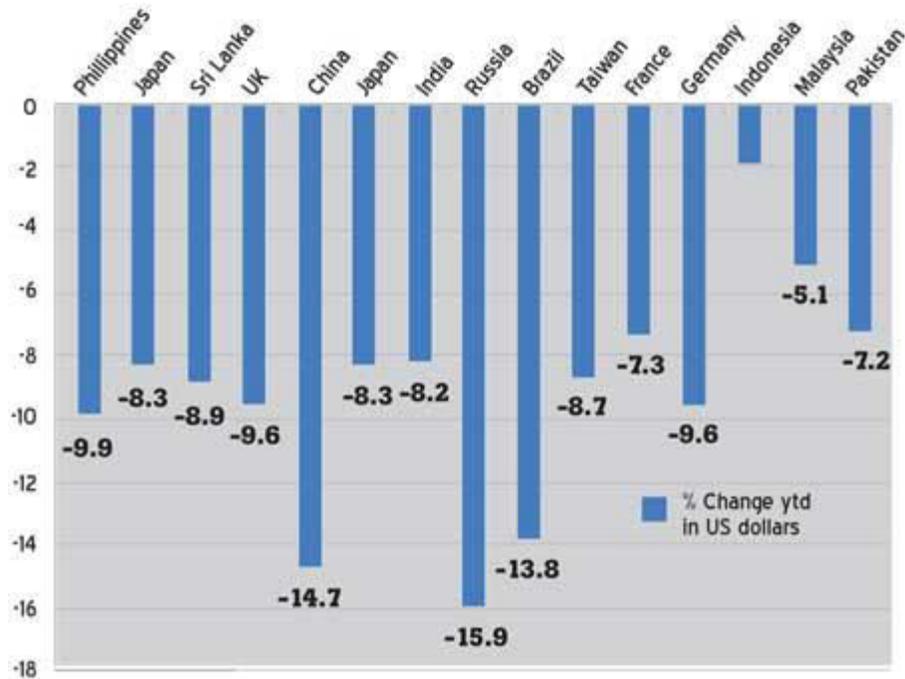
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Equity is an ideal financial instrument for a portfolio that is geared at long-term returns. It is undoubted that the rate of return on equity has been impressive when compared to other instruments. If the market generates lucrative returns in the long run it is natural to question why investors are indifferent towards market volatility. At a juncture the Colombo Stock Exchange (CSE) is experiencing a certain level of volatility, it is timely to answer the aforesaid question by elaborating on market volatility and long-term investment opportunities.

Market volatility: Fear not

A sharp increase in volatility was witnessed in the local equity market during the last few weeks. The market that went down by almost 100 points on certain days observed a reverse in the trend the next day. This phenomenon is not restricted to Sri Lanka. Readers who are well acquainted with global affairs are aware that this has become a common phenomenon in markets across borders. The rapid decline in stock prices in China is a classic example.

MSCI Share Price Indexes



After years of unabated growth and double-digit annual gains, investors are recovering from the recent stock market crash. Further on, the S&P 500 is down almost eight percent since the beginning of the year; the Dow Jones Industrial Average is down more than eight percent and the Russell 2000 Small Cap Index is off an eye-watering 11.0 percent and at a two-plus-year low. It is also interesting to note that oil prices have shot down to considerably low levels. Even the Indian stock market (the giant of South Asia) has decreased by nearly 8.2 percent for the current year.

China, the world's second-largest economy, is on the skids, the global economy remains bleak, the U.S. dollar is strong and the Federal Reserve raised rates for the first time in a decade, signalling four additional quarter-point increases throughout 2016 (negative relationship between interest rates and stock prices). Geopolitical tensions in the Middle East aren't helping matters either.

Answers to the market trend of the CSE could be partially perceived in the light of this glum global economic condition. Within such an environment it is a futile effort to expect the market to record a positive trend. Nevertheless, it is interesting to note that the CSE dipped down only by 5.5 percent last year when other Asian markets went down drastically. Even in the current year, the performance of the CSE is satisfactory when compared to other countries (refer the tables given).

When the world economy went into recession in 2008, Sri Lanka was able to maintain satisfactory growth. Similarly, we would once again be able to overcome the negative impact of the global economic slowdown. This is feasible as Sri Lanka is not a 100 percent open economy (capital restrictions). This was restated at the Economic Forum that was held a few days ago.

Brighter times are ahead

As we mark the end of a 30-year war, the country is well poised for economic growth. The perception amongst the international community on the current political regime will definitely fuel the development story of the country. Already many countries have given their consent to partner with us. Many constructive trade agreements were signed during the past year.

For the first time the Government of Sri Lanka was invited for the World Economic Summit that was held in Switzerland. The support extended by the international community will increase the inflow of foreign investments as well as exports. These are vital factors that are required to achieve satisfactory growth levels.

It is also said that there will be a boost in tourism and infrastructure. This will send positive vibes to the economy by increasing the gross domestic product (GDP). Independent research (e.g. Fox News) predicts that Sri Lanka would be an ultimate destination for tourist this year.

The government sector is undoubtedly a live wire of the Sri Lankan economy. Last year's budget revealed that some of these companies would be listed in the coming year. This would definitely influence the market. It would also increase the transparency and credibility of the government sector.

Further on, plans are underway to introduce a trading board for small and medium-scale industries. This would enable the market to play a more effective role in diverting funds to vital investments in the country.

Throughout the years the economy was pushed up by increasing aggregate demand. However, if we are looking at sustainable growth, we need to increase investments, preferably foreign investments.

Equity is a key source of attracting foreign investments. Foreign funds can be diverted only if we create an efficient market that can compete with other emerging markets. Thus, the Securities and Exchange Commission of Sri Lanka (SEC) has taken various measures to maintain an efficient market. The SEC Act is amended to encompass relevant regulatory measures required to foster efficient markets. This initiative will enable us to keep in line with international regulatory standards.

Another hindrance towards attracting foreign funds was the lack of a Central Counter Party System (CCP). Foreign investors are concern about the risk involvement in investing. The CCP is expected to curtail settlement risk and asset commitment risk in the market.

- See more at: <http://www.dailymirror.lk/104003/stock-market-volatility-and-investment-opportunities#sthash.9Dw9L5en.dpuf>