



WEEKLY REPORT 10 December 2012

*Making sense of global markets,
information and analysis for an informed investment*



This is the fifth issue in a new series of TeleTRADE Armenia weekly reports offering insightful analysis of international market trends and financial & economic developments, with a focus on Armenia but also covering global market trends and developments in the US, Europe and Asia.

Highlights

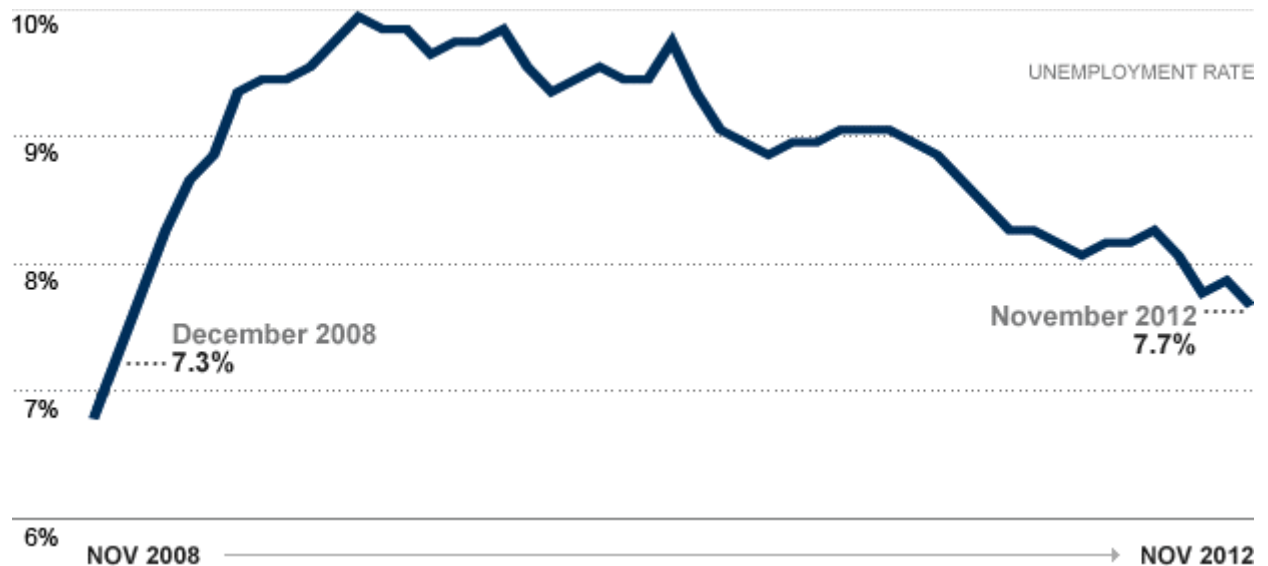
- Investor confidence in the US remained weak over the uncertainty of the politics of addressing the “fiscal cliff,” when \$600 billion in automatic spending cuts and tax increases kick in and may trigger a new recession. But positive signs, including lower unemployment, reinforced a third week of modest gains by US stocks;
- European markets were shaken by new concern over a possible recession in Germany early next year, as growth slowed, unemployment rose and industrial production declined. Elsewhere in Europe, the Portuguese economy declined by 3.5 percent for the third quarter, and manufacturing production in the UK decreased. In Ireland, the government released a new budget that included measures aimed at reducing its budget deficit, including 3.5 billion euros (\$4.58 billion) in tax increases and spending cuts;
- After an important political transition, the Chinese economy strengthened, as industrial output expanded and recent statistics suggested the start of an economic recovery, hinting at a coming increase in GDP in the fourth quarter, but matched by signs of an upward trend in inflation. In a new \$4.23 billion deal, Chinese investors acquired an 80.1 percent share in the aircraft leasing business owned by the American International Group (AIG) insurance company. If the deal is approved by US regulators, it would be the largest ever acquisition of an American business by Chinese investors. Elsewhere, the Japanese economy officially entered into recession, and continued to be plagued by weak exports and one of the highest debt-to-GDP ratios in the world.

Investor Confidence in US Markets Shaken

Larger investment decisions in the US market have been delayed due to ***investor concern over political negotiations over the so-called “fiscal cliff,”*** with an automatic \$600 billion in spending cuts and tax increases set for the start of next year, and raising ***fears that the US economy could slip back into recession.*** The fiscal cliff deadline of January 1, 2013 was set by Congress as a way to force a negotiated resolution of fiscal disagreements over taxes and spending, and the market has generally only increased when investors were more confident of an agreement. If Congress fails to reach an agreement by that deadline, the result would trigger a fall into recession in the first half of 2013, with a projected rise in unemployment to 9.1 percent in the fourth quarter of 2013, up from 7.7 percent in November 2012.

But there were still ***some positive signs,*** as ***demand has risen*** and ***business investment is set to recover*** in 2013, with orders for non-defense capital goods, excluding aircraft, rose by 2.9 percent in October, in the largest increase in eight months and following a 0.5 percent decline in September. This trend will be tested in the coming week, as a set of US economic indicators are set to be released in the coming days, including retail sales, figures for wholesale manufacturing inventories, industrial production, business inventories and the producer price index (PPI), as well as international trade reports for import and export prices and the trade balance. US market activity also reflected this, as the S&P 500 and Dow Jones Industrial Average posted a ***third week in a row of modest gains.***

Another positive report last week was an additional 146,000 new jobs in the US economy in November and a ***decline in the unemployment rate,*** which fell to 7.7 percent in November, the lowest level since December 2008, although the decline was also due to the fact that workers dropped out of the labor force.



Source: US Bureau of Labor Statistics

Developments in Europe

In a statement released last week, the ***German central bank warned that the country faces the threat of recession*** early next year, adding that the German economy is now set to grow by a meager 0.4 percent in 2013, a serious reduction from a June estimate of 1.6 percent growth. Other statistics confirm the danger of recession, as German unemployment is expected to rise to 7.2 percent this year, up from 6.8 percent for 2012, and German industrial production decreased by 2.6 percent in October, on top of a decline of 1.3 percent in September.

Over the longer term, however, the Bundesbank added that a *possible German recession would be temporary*, with a projected 1.9 percent rate of growth in 2014, but only if reforms in the eurozone continue and the overall global economy recovers. The Bundesbank warning follows a related forecast by the European Central Bank predicting a further contraction of the broader 17 eurozone economies, following the onset of its second recession since 2009 in the third quarter of this year.

Elsewhere in Europe, the *Portuguese economy declined* by 3.5 percent for the third quarter of 2012, after falling by 3.1 percent in the second quarter, and manufacturing production in the UK decreased by an unexpected 1.3 percent. In *Ireland, the government released a new 2013 budget* that included strict measures aimed at reducing its budget deficit, including 3.5 billion euros (\$4.58 billion) in tax increases and spending cuts, and reflecting Ireland's commitments under earlier bailout packages and necessary to return to the bond markets by the end of 2014.

Focus on Asia

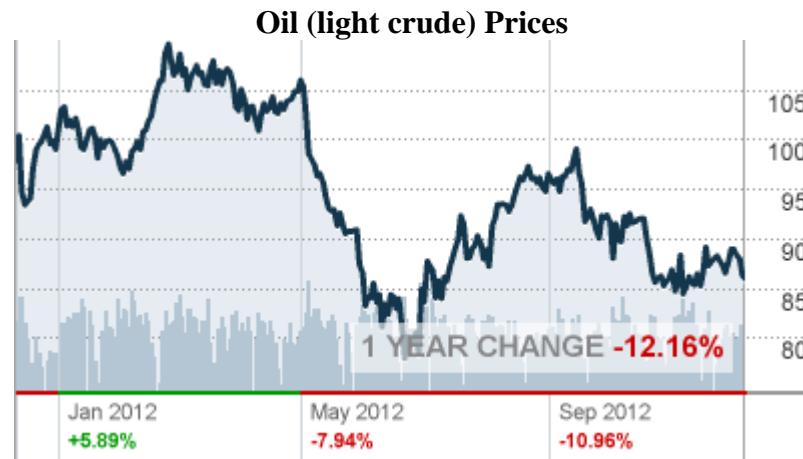
In one of the first public events since the ascension of the new Chinese leadership, China's new Community Party leader, Xi Jinping, chose a clear symbolic demonstration of his commitment to reform, by visiting Shenzhen, the southern Chinese city famous as an "incubator" for market reforms. The political transition was also aided by a *strengthening of the Chinese economy* in November, as industrial output expanded by 10.1 percent in November, on a year-to-year basis, an increase from the October level of 9.6 percent and representing the strongest rise since March. Other trends also pointed to an economic upturn, including a rise in electricity production, from 6.4 to 7.9 percent, but also with a slight 2 percent increase in consumer prices, as food prices rose 3 percent year-over-year, and revealing an *upward trend in inflation*. Overall, the recent statistics suggest that the *Chinese economy has now started to recover* from its midyear slump, and hinting at a coming increase in GDP in the fourth quarter of 2012, after China posted a disappointing three-year low of 7.4 percent in the third quarter.

Over this past weekend, *Chinese investors acquired* an 80.1 percent share in the *aircraft leasing business owned by the American International Group (AIG)* insurance company. The Chinese investors, comprising the China Aviation Industrial Fund, New China Trust, and the P3 Investments group, agreed to pay \$4.23 billion in the deal, which also includes an option for the purchase of an additional 9.9 percent stake. If that option is exercised, additional Chinese investors may also acquire shares, including New China Life Insurance and the Hong Kong-based ICBC International, a subsidiary of the Chinese state-owned Industrial and Commercial Bank of China, one of the largest banks in the world. If the deal is approved by US regulators, it would be the *largest ever acquisition of an American business by Chinese investors*. The Chinese investment is related to their longer term strategy of improving and expanding its air travel infrastructure and aircraft fleet. For AIG, the sale is tied to efforts to sell off "non-core assets," in an attempt to help rebuild after requiring a massive US government bailout.

According to new reports released this morning, the *Japanese economy officially entered into recession*, as GDP decreased by an annual rate of 3.5 percent from July to September, a fall of two straight quarters, meeting the technical definition of an economic recession. Although Japan remains the third-largest economy in the world, it has been plagued by weak exports and one of the highest debt-to-GDP ratios in the world, with GDP expected to further decline for the remainder of 2012. Other developments in Asia included a fall in Malaysian exports, for the third time in four months, while Taiwanese exports rose by 0.9 percent in November.

Commodities

In the commodities market, the main driver was a **rise in oil prices**, up from the lowest level in three weeks, mainly due to a significant increase in the level of Chinese crude oil processing, reaching a record 9.1 percent in November from a year ago, to 10.2 million barrels a day and bolstered by a 10.1 percent gain in Chinese industrial production. But with the Organization of Petroleum Exporting Countries (OPEC) set to meet this week, **global oil markets will likely stabilize**, as **OPEC is determined to keep its production quota steady** at 30 million barrels a day.



Spotlight on Armenia

The **Armenian parliament adopted a new 2013 state budget** last week, which includes an almost ten percent **increase in state spending**, set at 1.15 trillion drams (\$2.84 billion), and projects a fiscal deficit of almost 120 billion drams, roughly equivalent to some 2.6 percent of Armenian GDP, with a deficit-to-GDP ratio of 2.8 percent for 2012. According to the new state budget, the government has also pledged to reduce the deficit by **increasing the level of overall tax collection** by a planned 13 percent, targeted at a total of 993 billion drams in new tax revenue. The 2013 budget is also based on a **projected 6.2 percent rate of growth** in the Armenian economy, following the government's previous forecast of a 7 percent level of economic growth for 2012. According to the latest figures, Armenian GDP **increased by 9.3 percent in the third quarter** of 2012, a rate matching the level of economic growth for the third quarter of last year.

At the same time, the Armenian **parliament also rejected a proposal** from the opposition to introduce **new sweeping anti-trust measures** to curtail business monopolies and improve competition. The proposed legislation would have required a new government strategy to implement "urgent measures aimed at the elimination of illegal monopolies" by imposing a new ban limiting companies from owning more than one-third of shares "in all areas of economic activity other than public utilities." A second element would have further imposed fines on any company determined to hold a "dominant position" in any specific sector of the economy.

But in a sign of **deeper economic weakness** in Armenia, for the third quarter of 2012, the level of **foreign investment declined** by 35.2 percent over the same period last year, falling to a level of only \$391 million. For the first time, Canada emerged as the leading foreign investor in Armenia, with an increase of 4.4 percent to \$102 million, largely due to an increase in Canadian investment in the mining sector. Russian investment fell to second place in the third quarter, while Switzerland posted the largest increase in investment, to \$38.8 million. Almost half of all foreign investment in Armenia, or about 45.6 percent, is limited to the mining sector.



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