



WEEKLY REPORT 19 November 2012

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



This is the second 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

- US markets strengthened by new optimism after steady increases in consumer spending, improved housing market and falling interest rates, with more credit for business expansion, likely increasing employment; US technology stocks face new volatility;
- Euro zone crisis deepened after onset of second recession, marked by sluggish growth; imports and exports broadly decline and pressure builds for further budget cuts; greater instability after coordinated strikes in several countries, disrupting trade and transport, and triggering expectations for new round of fresh increases in food and fuel prices;
- Asian markets focused on new more conservative Chinese leadership; US president on regional tour pursuing trade and investment opportunities; Japan faces market volatility from coming election and as Japanese farmers resist cuts in state agricultural subsidies;
- Global commodities market dominated by decline in gold and increase in oil prices; new unrest in Jordan over rising fuel prices renews concern in Middle Eastern markets, as Jordan faces unprecedented protests and struggles to manage \$5 billion budget deficit.
- Armenia can benefit from Georgian proposal to restore railway link to Russia through Abkhazia; Armenian presidential visit to Paris promises greater trade and French investment; mass slaughter of livestock in Armenia due to spike in prices for animal feed may trigger coming wave of corresponding price rises for meat and dairy products.

US Markets: New Optimism & Falling Interest Rates

For much of the past week, ***Wall Street remained concerned*** over the implications from the need for the US Congress to address an approaching showdown, known as a “fiscal cliff.” The fiscal showdown is driven by a 1 January 2013 deadline when automatic measures will be activated, unless the US Congress takes action. The automatic measures include the introduction of \$607 billion in tax increases and \$1.5 trillion in reductions in federal spending. But after his first news conference since his re-election, President ***Obama now seems in a stronger position as leading US institutional investors have expressed new optimism*** that the White House will be able to pressure Congress to reach an agreement to avert the crisis. That optimism is also matched by steady increases in consumer spending, the US economy’s main driver of growth, a rebound in employment, reductions in household consumer debt, and an improved housing market.

Meanwhile, US Federal Reserve Bank Chairman Bernanke also ***reassured the market*** by promising to “use all the tools at his disposal to accelerate economic growth and recovery in the housing market.” Most importantly, he also signaled that the Federal Reserve Bank is most likely to continue and even expand its monthly bond purchases through next year, a move that will ***drive down interest rates***. More specifically, the impact of a further reduction in the interest rate on US Treasury 10-year bonds will then ***trigger a broader rate decrease***, as home mortgages and other lending rates, such as corporate borrowing are tied directly to the value of Treasury bonds. In turn, this will ***free up even more “easy-access,” low-interest credit for business expansion and capital investment***, thereby helping to increase employment.

US technology stocks are likely to face a new degree of volatility as senior figures from Microsoft and Apple have recently resigned or been fired. The moves raise ***new concerns over the future strategy of market leaders Microsoft and Apple***. For Microsoft, the departure of Steven Sinofsky, the head of the company’s Windows unit since 2006, comes only two weeks after the launch of the new Windows 8 and Surface, a new series of tablet computers, and is ***likely to raise consumer concern over Microsoft products***, which he helped to develop. The launch of both products represent an attempt by Microsoft to regain software market share and leadership after coming under threat from greater competition from the iOS and Android mobile tablet devices. For Apple, Scott Forstall, the head of Apple’s iOS for several years, and Apple’s head of retail sales, were both fired, ***shaking investor confidence over internal problems within Apple***. Forstall led the development of Apple’s new, but troubled Maps program, and was widely seen as a successor to Steve Jobs as the company’s “visionary” and strategic planner.

On November 16, a major ***US corporation, Hostess Brands, entered into bankruptcy***, thereby ending the production of several American brand icons. Although the closure of Hostess Brands means the loss of six famous American products, like “Wonder Bread,” and its line of processed pastries, “Twinkies” and “Devil Dogs,” the ***larger impact*** is the loss of roughly 20,000 jobs and, the ***company’s roughly \$2 billion in unfunded pension liabilities*** to its workers’ three unions.

Developments in Europe

The crisis in the Euro zone only deepened for this period, as a statistical report released on 16 November confirmed that for July-September, the ***Euro bloc officially entered a second recession***, the second one since the onset of the global financial crisis in 2009. The report further noted a slight 1.1 percent decline in euro area exports and a 2.7 percent fall in imports for September, boosting a ***widening trade surplus***, from 8.0 million to 11.3 billion euros (\$14.4 billion) since last month. Overall, both ***imports and exports posted across the board declines***, while German exports were down and the euro traded last week at its lowest level since August.

But signs of a ***deep and lingering crisis*** only continued last week, as the overall sovereign debt crisis exerted greater pressure on euro zone member states to enact even tighter budget cuts. This also fueled an additional ***downturn in the wider euro area***, as GDP declined by another 0.1 percent for the third quarter, following an earlier 0.2 percent decline over the prior three months. The most sustained declines were in Greece, where the economy has declined for 17 consecutive quarters, and Portugal, where the economy suffered through a second year of recession. This deeper trend suggests that ***any rebound in economic growth will not be possible until September 2013***.

A ***leading European company, Ikea***, the Swedish furniture company, also faces a new threat to its stock value, with its ***stock prices likely to take a hit*** in the coming weeks. After media reports accused Ikea of using East German prison labor to make some of its products years ago, Ikea formally apologized and brought in an independent Ernst & Young auditing team to carry out an investigation. But the ***most troubling sign of European instability*** was the eruption of demonstrations and ***organized strikes by millions of workers*** protesting budget cuts and rising unemployment. The strikes were significant as they were ***coordinated in several EU countries***, with the largest strikes in Spain and Portugal, and with smaller actions in Italy and Greece, but also matched by protests in Belgium, Germany, and France. These strikes not only demonstrate a new degree of coordination, but have the power to ***disrupt trade, transport and air travel throughout Europe***, thereby ***triggering at least temporary increases in food and fuel prices***, to be felt in the coming weeks as inventories run out and replacement shipments are delayed.

Other lesser developments in Europe last week include the start of ***loan talks between the International Monetary Fund (IMF) and Serbia***, aimed at supporting the Serbian economy through the coming year and to help Belgrade manage its public debt, now at almost 50 percent of its GDP, and to address a budget deficit of over 7 percent of GDP. Earlier this year, the IMF suspended a \$1.3 billion credit for Serbia as punishment for the Serbian government's "overspending" prior to the election last May. The ***IMF loan is expected to be finalized*** within the coming month and is ***likely to stabilize Serbia's volatile currency market and may open up new sectors of the economy*** for greater foreign investment, in return for the adoption of liberalization reform measures and some targeted budget cuts by the Serbian government.

Another development was the decision by EU finance ministers and international lenders to provide ***Greece with a two-year extension to the deadline to reduce its budget deficit***. The decision follows a Greek parliamentary vote to adopt fresh budget cuts and tighter 2013 budget, although ministers also ***postponed a decision to release a new installment of 31.5 billion euros*** (\$40 billion) until November 20. Now in its sixth straight year of recession, Greece has received 150 billion euros (\$193.5 billion) of a 240 billion-euro (\$310 billion) rescue package.

Focus on Asia

Recent ***developments in Asia center on China, as a new generation of leaders assumed power***, in an organized process that occurs once every decade. On November 15, Xi Jinping was approved as the new leader of the Chinese Communist Party, replacing Hu Jintao, and becoming chairman of the powerful Central Military Commission, in preparation for his expected promotion to the post of Chinese state president in March 2013. Widely seen as ***more politically conservative and cautious over economic reform***, the new Chinese leadership will ***struggle to manage declining economic performance, widening disparities in wealth and income, mounting social tension and sporadic labor unrest***.

On his first foreign visit since his reelection, US President Obama is in Asia for a series of state visits to three South Asian countries. The visit is part of a **broader US “Asian Pivot,” or shift in focus toward the Asia-Pacific region** and is a response to “balance” rising Chinese power and influence and a **renewed US emphasis on trade and investment opportunities** in Asia. Starting his regional tour in Thailand, the US president will also be the first president to visit Burma (officially known as Myanmar), marking that country’s difficult transition from a military dictatorship, before ending his regional tour in Cambodia, where he will also attend an East Asian trade meeting. For trade and investment, the visit confirms a **new strategy of broadening US engagement in the markets of Vietnam, Thailand, Malaysia and the Philippines.**

A broader, developing trend in Asia centers on **Japanese interest in joining** the Trans-Pacific Partnership (TPP), an **extensive US-led free trade agreement** that seeks to integrate the Asian and North American economies, while Tokyo also seeks to forge a Japanese-South Korean-Chinese free trade agreement. But **Japan faces only greater market volatility** prior to an **important election next month**, as Prime Minister Noda is struggling to remain in power in the face of serious political and economic challenges made worse by rising Japanese nationalist politics driven by lingering conflict with China over disputed islands. **Japanese market instability will also continue** as the country’s powerful farmers oppose the free trade policies and will fight any government attempt to reduce state agricultural subsidies.

Commodities

For this period, the global commodities market was dominated by a significant **decline in gold prices** and an **increase in oil prices**. The fall in gold prices, a decline of close to \$15 per ounce and reaching a level of \$1710, was driven by a third-quarter fall in demand. The rise in crude oil prices, which capped at \$87.05 per barrel, was sparked by renewed violence in the Middle East and expectations of an Israeli military invasion of Gaza. And as clashes between Israelis and Palestinians escalate, **investor concern will only continue to drive the price of oil higher.**

Middle East

Despite the appearance of a general calm in the Middle East as the new Arab Spring government’s have each settled down to governing their countries, a new degree of **unrest in Jordan is renewing instability in Middle Eastern markets**. Although both the kingdoms of Jordan and Morocco have tended to overcome initial waves of discontent during the Arab Spring revolutions, fresh unrest in Jordan continue to escalate, posing a serious threat to Jordanian King Abdullah’s government. The new unrest in Jordan is driven by **large protests over rising fuel prices** imposed by the government attempting to address the country’s \$5 billion budget deficit.

Most importantly, the protests have expanded to several cities since a large opposition demonstration demanding political reform last month and, unusually for Jordan, are openly expressing discontent with the Jordanian king. In turn, King Abdullah has attempted to meet demonstrators’ demands by calling early elections in January 2013, although such concessions may not be enough to satisfy rising social discontent. Jordan is also vulnerable to broader changes in the Middle East, as its traditional **imports of Egyptian natural gas have been disrupted by attacks targeting the gas pipeline supplying both Jordan and Israel** and as mounting nationalism threatens the moderate Jordan king as violence between Israelis and Palestinian escalate, especially as Palestinians now account for approximately 60 percent of Jordan’s overall 6.5 million population.

Spotlight on Armenia

One of the most significant ***longer term trends impacting the Armenian economy*** is a recent proposal by the new Georgian government to ***restore the railway link to Russia through Abkhazia***. Heralded in Tbilisi as an important “confidence building” measure, the Georgian government has also offered to restore the highway through Abkhazia as a supplement to the railway line. The Abkhaz railway is an important link connecting Russia to the South Caucasus and its reopening would help to restore, improve and expand regional trade routes, especially following the development of rail links between Georgia and Turkey. ***For Armenia, the restoration of the railway line through Abkhazia would help to end Armenia’s isolation*** by weakening the effects of the closed Armenian borders with Turkey and Azerbaijan.

Armenia received a boost last week when the ***Forbes business magazine ranked Armenia as having the 77th best economy for doing business***, although both Azerbaijan and Georgia ranked higher than Armenia, with scores of 73rd and 50th respectively. The survey ranked Russia 105th, with the Baltic states were rated as the best performers among former Soviet economies.

During a ***state visit to France*** last week, Armenian President Sarkisian discussed bilateral economic cooperation in his first meeting with French President Hollande and both sides identified agriculture, infrastructure, transportation and telecommunications as ***priority sectors for greater French investment***. French officials are also ***seeking the establishment of free trade zones to help attract new investments*** by French companies in Armenia. As France is now the second largest investor in Armenia, French-Armenian economic and trade ties have been expanding in recent years and are projected to increase in the fields of innovative technology and IT, water supply, entrepreneurship and the development of the private sector. ***France is also interested in the energy sector*** and is planning to bid for the construction of a new nuclear power plant to replace the aging Medzamor facility, the only nuclear power plant in the region.

Recent reports of a ***sudden decrease in the price for meat*** and some meat products in Armenia may actually be a ***result of a spike in killings of farm animals and livestock*** in the country after farmers were faced by an unprecedented jump in the price for animal feed. Although the price for beef, which usually sells for roughly \$6 per kilogram, fell by almost \$0.75 on the Armenian market in recent days, farmers have been forced to kill much of their cattle stocks as the more expensive animal feed makes it hard for farmers to afford necessary winter forage. Armenian officials downplayed the concern over the animal husbandry crisis, arguing that the cattle slaughter was “common for this time of year,” but failing to address the ***price rise for animal fodder***, despite the fact that prices for livestock feed rose to 1,500-1,600 drams (about \$3.7-\$4.00). There are also ***wider implications*** from the mass slaughter, including a related price rise in dairy products and a possible shortage of meat, triggering a later spike in meat prices.



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