Professional approach to trading

WEEKLY REPORT

7 January 2013

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

This is the first issue of the second volume in a 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

- Investors were reassured after the US Congress reached a last-minute deal resolving a fiscal crisis, although long-term investor confidence was concerned over the increasing deficit. But the outlook for the US economy was bolstered by recent reports on unemployment, job creation and positive trends in the housing market;

- Despite greater confidence from the US fiscal deal, European stocks were down, although the outlook for the European economy improved, after the German economy stabilized and improved consumer surveys suggested growth for the eurozone economies;

- In Asian markets, Japan was one of the only winners, as the Nikkei stock index posted its highest closing position in almost two years. The forecast for China improved, as the country's fourth-quarter GDP is expected to increase, ending a seven-quarter slowdown, with stronger consumer confidence reflected by a recovery in Hong Kong's luxury sales, as China overtook the US as the world's largest buyers of luxury goods;

- For commodities, gold prices decreased, although investors were encouraged by an annual increase and now hold a record amount of gold, purchasing 60 percent more gold than in 2011. Analysts expect gold prices to reach $2,000 in 2013, although demand may slow, as India, the world's largest gold buyer, may introduce a new tax on gold imports.

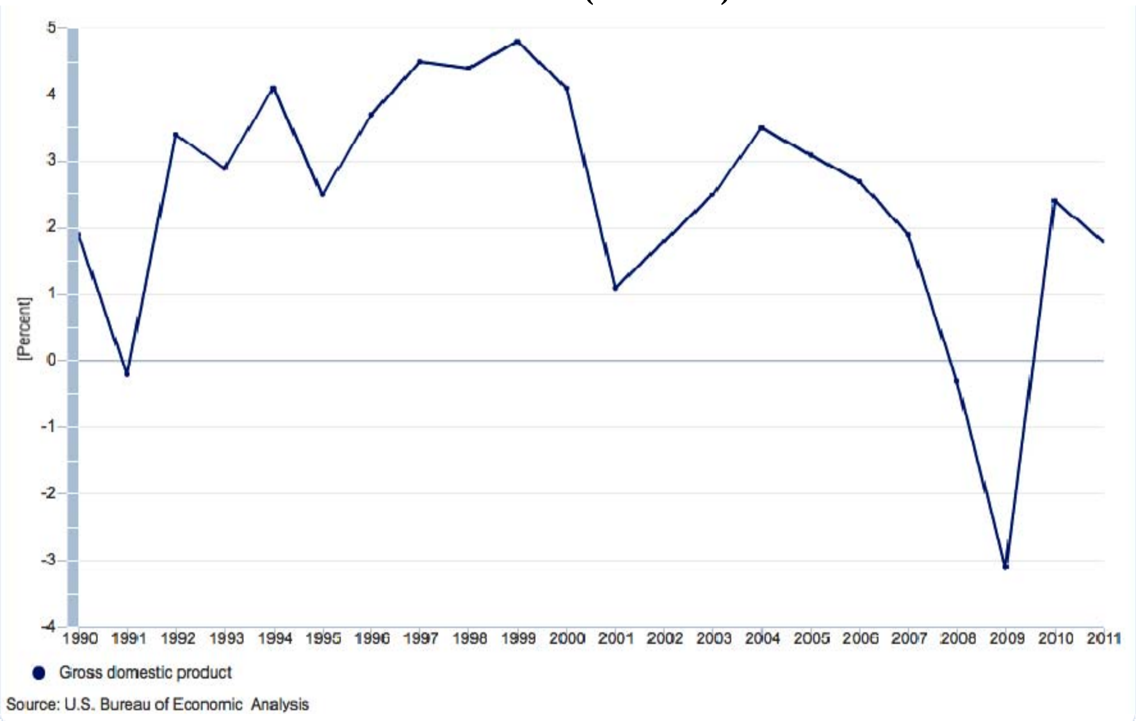
US Investors Reassured by Fiscal Deal but Concerned over Debt

Investors were reassured after the US Congress forged a last-minute deal to avert the so-called "fiscal cliff," a January 1, 2013 deadline that would have automatically triggered $600 billion in spending cuts and tax increases. The agreement was especially important, as many economists feared that those resulting automatic measures could have sparked a new US recession in the first half of 2013. But the deal did little to foster long-term investor confidence, as it failed to address the country's widening deficit and its growing level of underlying debt, which reached the official $16.4 trillion debt limit last week.

While the US Treasury moved to ease pressure last week by securing an additional $200 billion to cover about two months of government spending, the US Congress must now agree to raise the debt ceiling by late February or early March 2013. The last time the Congress attempted to raise the debt limit, it led to an intense and difficult political debate in August 2011, and which also led to the loss of the top credit rating for the US. This time, credit rating agencies have already warned that the US may face another credit downgrade if Congress fails to reach a viable long-term debt reduction plan by March 2013.

Immediately following the deal averting the fiscal crisis, Congress approved $9.7 billion in financial assistance to people whose homes were damaged or destroyed by Hurricane Sandy. That financial aid is the first element in a much larger $51 billion aid package to help homeowners and local governments recover from the storm. Those developments helped to rally US stocks last week, as the Standard & Poor's 500 Index increased by 4.6 percent, reaching its highest level since December 2007, and as other benchmark indexes posted their biggest gains in 13 months. Meanwhile, in an announcement that sparked investor concern throughout European and Asian markets, the US Federal Reserve Bank announced last week that it was reconsidering whether to continue its $85 billion monthly bond purchases sometime later in 2013.

US Real GDP (1990-2011)



The latest US employment figures, released late last week, confirmed a trend of positive but sluggish growth for the US economy. With the monthly statistics showing about 155,000 new jobs, the rather low level suggested that the economy is likely to increase by only about 2 percent for 2013, not enough to strengthen the economic recovery that first started in 2009. But there were some positive signs, as the overall unemployment rate remained at a manageable 7.8 percent and the increase in job creation was widely distributed in many areas, including in the healthcare, manufacturing and services sectors. More importantly, there were some 30,000 new jobs created in the construction sector, bolstering an already expanding housing market and encouraging a rise in consumer confidence, which rose to its highest level in eight months.

US Unemployment Rate

Source: US Bureau of Labor Statistics

Further strengthening the outlook for a more robust US economic recovery, the services sector also expanded at the fastest pace in ten months and manufacturing growth was driven by increased factory orders and improved exports. And the housing sector also improved, providing another important fundamental driver of sustained growth, as existing-home sales reached a three-year high in November, and sales of new homes increased by 4.4 percent last month, the highest level since April 2010. Homebuilding outlays also increased slightly last month, reaching a total of $295.3 billion for 2012, the highest level of spending since November 2008.

US Housing Starts ('000s)

Source: US Census Bureau

More Positive Outlook for Europe

Despite greater confidence in the US, news that the US Federal Reserve would ease its monthly bond purchases brought down European stocks last week, in a broad decline ending a 22-month high. But the overall outlook for the European economy improved last month, after the German economy stabilized and both economic indicators and improved consumer surveys suggested a return to growth for the eurozone economies in 2013. Such an improved outlook was welcome news for investors, especially as the eurozone fell into recession for the second time in four years during the third quarter of 2012 after a dramatic contraction and a deepening debt crisis and suffers from a nearly entrenched 12 percent unemployment rate.

Although the European Central Bank warned last week that past levels of economic growth were unlikely to return in 2013, German Chancellor Angela Merkel noted that her economy seems to have overcome the worst stage of crisis. Although her statement was also timed with her third term election in September 2013, her general optimism was realistic, as Europe's biggest economy recently reported strong growth in the services sector last month, an increase for the first time in five months and its strongest performance since April 2012. But the French economy continued to be challenged, as a decline in manufacturing and service sectors continued, marking a ten-month downturn, and the services sector in the UK also marked its first fall in two years, although the UK economy emerged from recession in the third quarter of 2012.

In her official New Year address, Merkel stressed that Germany was beginning to benefit from its reforms, and welcomed the positive impact from the European Central Bank (ECB) decision to launch a massive investment in weaker eurozone economies. And in line with its role as Europe's largest economy, Germany has led efforts and assumed much of the burden to bail out troubled eurozone countries like Greece, and established Europe's permanent rescue fund, the European Stability Mechanism. In return, the highly indebted eurozone states committed to adopting new austerity policies, with spending cuts and tax increases.

For the average person living in the eurozone, consumer prices increased more than expected in December, driven by higher food prices, but offset by a lower increase in energy costs. Inflation in the eurozone also remained constant at 2.2 percent, and projections by the European Central Bank (ECB) were lowered to 1.6 percent for 2013, with prices expected to increase by an estimated 1.4 percent for the year. The ECB also projects a further decline in economic activity in the eurozone, which has already weathered a contraction of two successive quarters. Overall, the outlook for the 17-nation eurozone for 2013 remained fairly bleak, as most economists predict a further contraction as deficit-cutting measures, lower tax collection and rising unemployment will challenge the Italian, Spanish, Greek and French governments to meet their budget targets, triggering new market volatility and undermining investor confidence. For France, the International Monetary Fund (IMF) recently warned that the French government was most likely to miss its 2013 target to maintain debt at 3 percent of GDP, down from 4.5 percent in 2012, as the level of economic growth for 2013 is lower than expected.

Focus on Asia

The Japanese market was one of the only winners in Asia last week, as the Japanese Nikkei stock index increased by 2.8 percent on its first trading day of the new year, representing its highest closing position in 22 months, as investors rallied over news of resolution of the US fiscal crisis. But stock markets in Hong Kong, South Korea and Taiwan each declined slightly, while the Shanghai Composite Index rose a mere 0.4 percent in the first day of trading this year.

But the overall forecast for China improved, as the country's fourth-quarter GDP is expected to increase by between 7.8-8.0 percent compared to last year, up from a three-year low of 7.4 percent and ending a seven-quarter slowdown. The expected improvement was led by an expansion in manufacturing, although the service sector did worse than expected in December 2012. The new Chinese leadership, led by Xi Jinping, is targeting a "sustained and healthy development" of the economy, after Chinese growth last year was the weakest since 1999, prompting the Chinese government to cut taxes for smaller companies and low-income households, and increasing investment and state spending on infrastructure projects in order to bolster growth and strengthen sagging exports. Other priorities in the Chinese five-year plan include the expansion of the size of the services sector, which also includes telecommunications and transportation, from about a 43 to 47 percent share of the economy by 2015.

Stronger consumer confidence in the Chinese economy was also reflected by a strong recovery in Hong Kong's luxury sales, as the volume of sales of luxury goods, such as jewelry and watches, increased by 13.7 percent in November 2012 from a year earlier, ending a 2.9 percent decline for October 2012, and retail sales expanded by 9.5 percent compared to a year earlier. At one point last year, Chinese consumers overtook US shoppers as the world's largest buyers of luxury goods, accounting for 25 percent of global sales, with US consumers now accounting for 20 percent of the world's luxury sales, followed by Japanese shoppers at 14 percent. In addition, there was also a sudden rise in the number of mainland Chinese tourists to Hong Kong in November, to over 3 million, representing a 30 percent increase since 2011.

The Commodities Market

As the new year opened, gold prices decreased by 1.2 percent, to $1,643.85 per ounce, posting its longest weekly string of losses since 2004, despite the longest record of annual gains in gold prices for over nine decades. Encouraged by an annual increase of 7.1 percent in 2012, gold investors now hold a record amount of gold-backed assets and exchange-traded products, valued at $138.5 billion or representing about one year of global mining production. For 2012, gold investors purchased about 60 percent more in gold assets than in 2011. Most analysts expect gold prices to reach $2,000 in 2013, this year, mainly as a hedge against inflation and to offset weaker currencies. But at the same time, the future demand for gold may slow in 2013, as India, the world's largest gold buyer, is considering the introduction of a new tax on gold imports in order to reduce its current account deficit.

In other commodity markets, analysts predict a stable sugar prices for 2013, after decreasing by 16 percent last year, in a second consecutive decline. For 2012, corn prices increased by 8 percent, soybean prices surged by 17 percent and wheat prices increased by 19 percent.

Technology Stocks

In a major development in the technology sector, the US Federal Trade Commission (FTC) announced last week that it would not pursue an antitrust case against Google, closing a 19-month investigation assessing if Google engaged in business practices that "unfairly favored its own products and services in its search results against rival companies." The decision basically validates Google's defense that its products and innovations benefits all users, although the company voluntarily adopted new measures to make it easier for Google advertisers to move their campaigns to competitors, ended exclusive search deals with websites and halted its practice of re-posting reviews from other websites into its own search results.

Google also settled a separate lawsuit brought by the FTC over its patent licensing, after regulators determined that Google was "wrongfully preventing competitors from licensing certain patents." Google currently controls roughly two-third of the US internet search engine market and has integrated its own products into its search results, including its own Google+ social network, local business listings, airline schedules and weather reports, resulting in the lowering of rankings of competitors' search listings. Despite the apparent victory, Google also faces a challenge in Europe, where it controls some 90 percent of the internet search market, as European antitrust bodies are stepping up a similar investigation of Google's trade practices.

Spotlight on Armenia

The outlook for the Armenian economy was positive at the start of the new year, with GDP estimated to have increased by 7 percent for 2012, a significant improvement over the 2011 level of 4.7 percent growth. The monthly average nominal income for workers also posted a slight 0.5 percent increased in November 2012, to almost 120,000 drams (or about $294), but 5.1 percent higher than the October 2011 level. There was a regional disparity in the figures, however, with the highest average monthly salary, at 145,700 drams ($361) in the Syunik region, and the lowest, at 82,400 drams ($204), in the Aragatsotn region. In the capital Yerevan, the average nominal monthly salary was slightly more than 132,000 drams ($327) in November 2012.

In terms of the different level of wages by occupation, the highest salaries for the period were in the finance and insurance sectors, at roughly 303,700 drams ($752), in the information and communications technology sectors, at 252,900 drams ($626), in the mining sector, at about 243,000 drams ($601), followed by the energy sector, at about 154,900 drams ($383), over 154,300 drams ($382) in construction, and an average of almost 131,000 drams ($324) in monthly income for state employees and civil servants. The lowest paying jobs were in the services sector, averaging about 75,400 drams ($187) per month and for teachers, averaging about 80,000 drams ($198) in monthly income.

The country's level of international reserve funds declined by some $22 million, however, to about $1.687 billion as of November 2012. The lower level of reserves was largely due to intervention in the currency markets by the Armenian Central Bank, in support of the value of the Armenian dram. The decline was largely limited to Armenia's cash money reserves, which totaled $572 million in November, down from $592 million in October 2012. Overall, the total amount of Armenia's international reserve funds exceeded $1.8 billion at the beginning of 2012.

-Richard Giragosian