Professional approach to trading

WEEKLY REPORT

28 January 2013

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

This is the fourth 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

- In a recent IMF assessment, the outlook for the US economy was positive, although estimated growth for 2013 was lowered to 2 percent, but projected a 3 percent increase in GDP in 2014. Other positive trends included a stronger housing market, stock market gains and an improved employment situation, as first-time claims for jobless benefits unexpectedly decreased to a five-year low;

- For the global economy, the IMF assessment projected a 3.5 percent increase in the global economy for 2013, driven by Chinese growth and a stronger US economy. The outlook for the regions of the South Caucasus and Central Asia in 2013 was also favorable, due to high oil prices and strong commodity prices and remittances;

- The IMF outlook for the eurozone focused on continued economic contraction for 2013, with sluggish growth in Germany and serious weakness in Spain and Italy, although investor confidence in Germany improved;

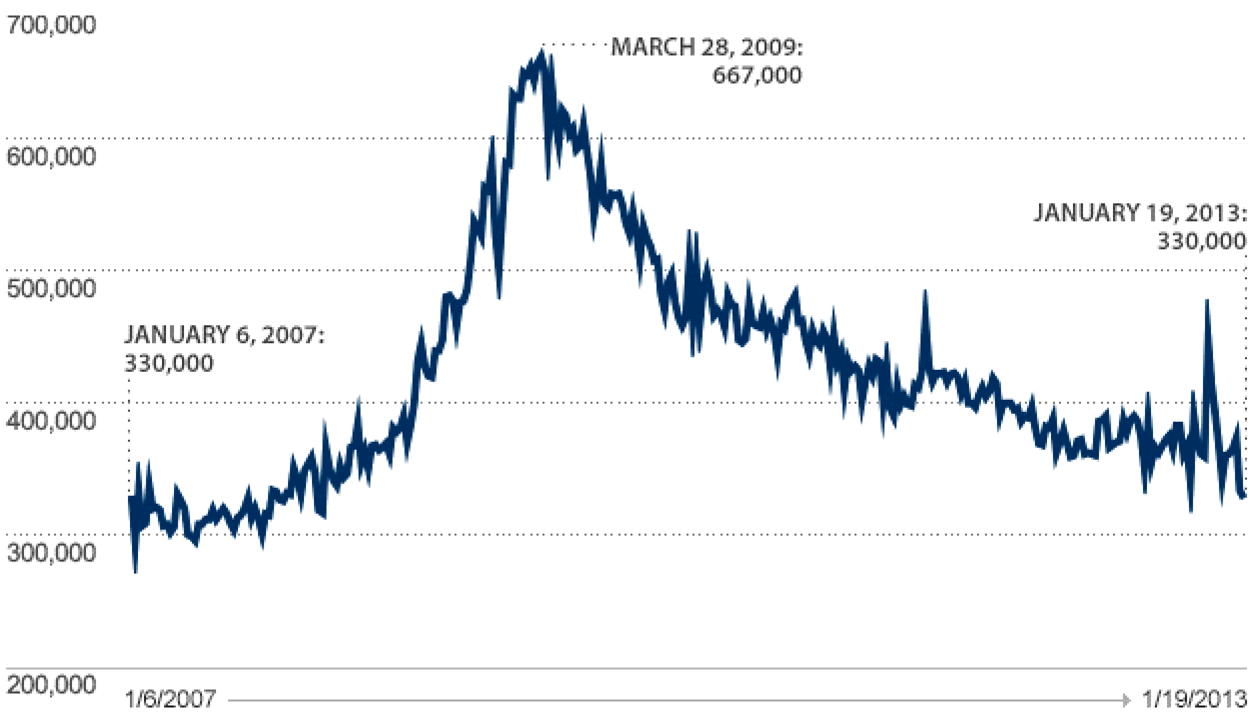
- The outlook for the Asian economies was mixed, as China continues to grow by over 8.2 percent, but Japan is plagued by slow growth, although Asian stocks rose significantly.

US Economic Recovery Tied to Employment

According to an assessment released last week by the International Monetary Fund (IMF), the outlook for the US economy remained generally positive, as the report stressed that “underlying economic conditions remain on track,” although the IMF lowered its estimate for US growth for 2013, from 2.1 to 2 percent, but raised its forecast for 2014, to a projected 3 percent increase in GDP. Other underlying trends also tended to confirm that positive assessment, including a stronger housing market, stock market gains and an improved employment situation. The stronger housing market is also expected to support a broader economic expansion, and was bolstered by data on new building permits, an indicator of future housing construction, which revealed a December 2012 highest level increase since 2008. The housing market is expected to further improve, due to a combination of lower home prices and record-low mortgage rates.

In terms of the labor market, the US Labor Department reported last week that first-time claims for jobless benefits unexpectedly decreased last week to a five-year low, falling to roughly 330,000 last week, from a high of 667,000 in late March 2009 (see chart below).

Total Unemployment Claims (thousands)



Source: US Department of Labor

Meanwhile, the unemployment situation also remained a serious priority for the US Federal Reserve Bank, reflecting its dual mandate to both manage inflation and employment. For example, in the most significant intervention to help spark a stronger economic recovery, the Federal Reserve escalated an unprecedented bond buying program, with purchases totaling a record $3.01 trillion in a bold move to reduce the country’s 7.8 percent unemployment rate. The Bank has been regularly purchasing $85 billion in securities every month, after initiating some $40 billion in monthly purchases of mortgage-backed securities in September 2012, followed by another $45 billion in purchases of Treasury securities in January 2013. The Federal Reserve is expected to continue this “quantitative easing” effort in order to overcome lingering high unemployment even after almost four years since the start of the US economic recovery.

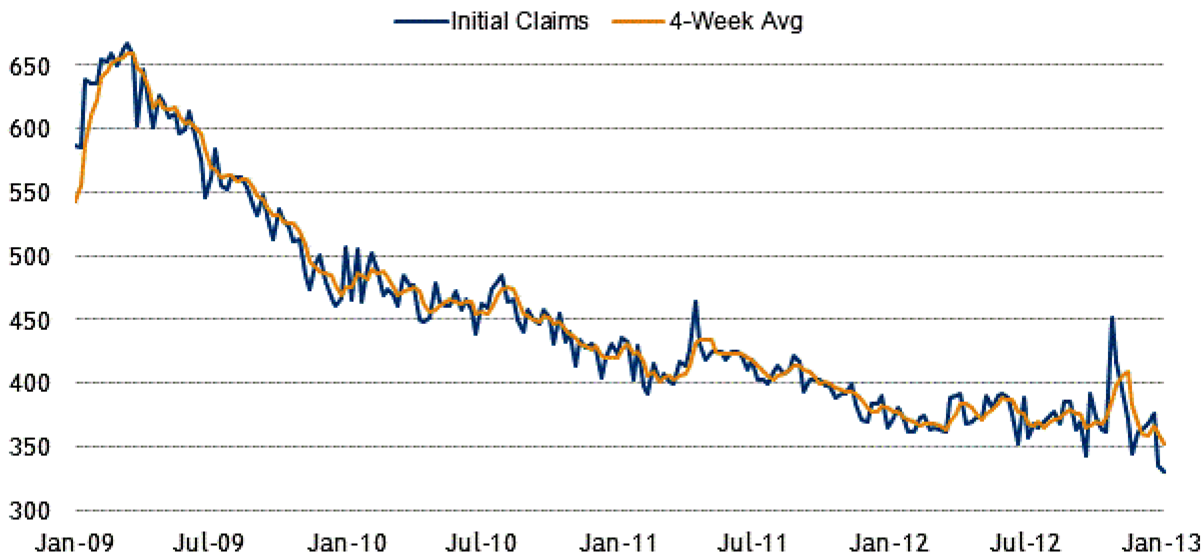
And from a longer, historical perspective assessing unemployment and labor market conditions, looking back at data starting from January 1995, initial unemployment claims sustained a temporary, but serious spike from mid-2007 to early 2009, further demonstrating the cyclical nature of the US economic recession (see chart below).

Initial Unemployment Claims (four-week average; thousands)

Source: US Bureau of Labor Statistics

Over another period, an even more impressive downward trend in initial unemployment claims was recorded from January 2009 through January 2013 (see chart below).

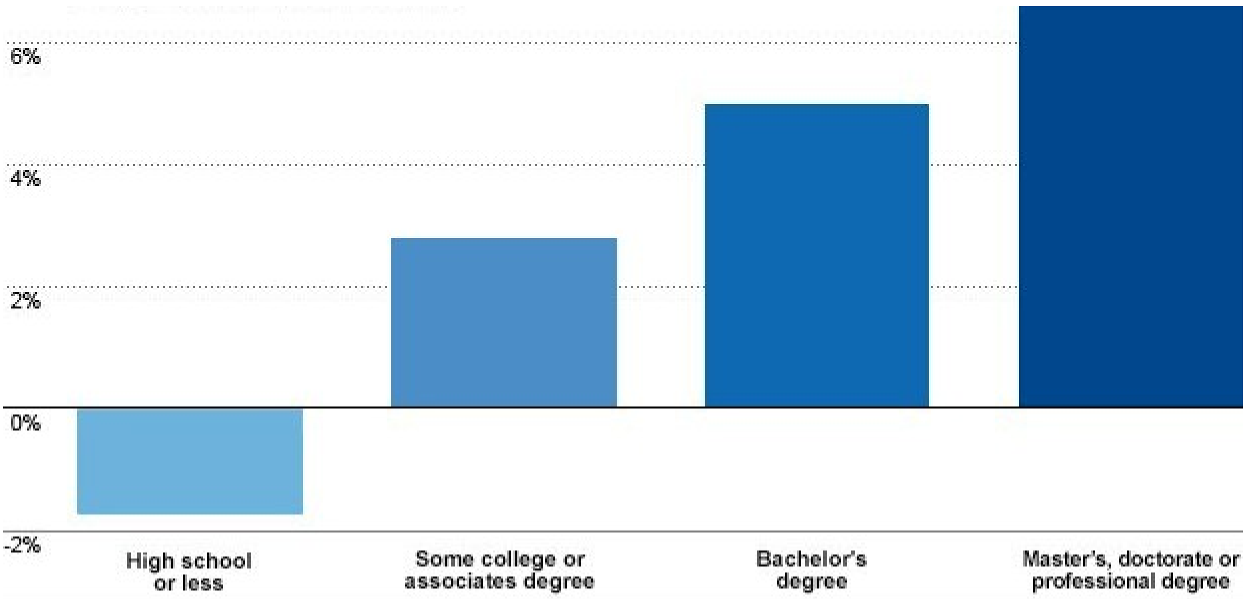
Initial Unemployment Claims (thousands)



Source: US Bureau of Labor Statistics

But much of the improvement in the labor market was limited to job seekers with higher education. According to data for 2010-2012, the largest gains in finding work were for job seekers with graduate degrees, as 1.1 million individuals with higher degrees secured new jobs in 2012, representing a roughly 6.7 percent increase, while those with only a high school degree or less suffered from a negative 1.75 percent decrease in terms of finding work. For those with only a high school education or less, which accounts for a larger group of about 36 percent of all workers in the US over the age of 25, the data was especially negative (see chart below).

Employment by Education
(in percent change; 2010-2012)



Source: US Bureau of Labor Statistics

For example, job losses for this group began a steady and continuing decline in 2007, with almost 770,000 fewer workers among this group holding jobs in 2012 compared to 2010, and almost 2 million now unemployed. While this demonstrates a deeper trend in the US economy toward higher skilled jobs, such as those in the health care and engineering professions, it also reveals a decline in the older, more traditional manufacturing and construction sectors, and a need for greater job training programs for these less-educated workers.

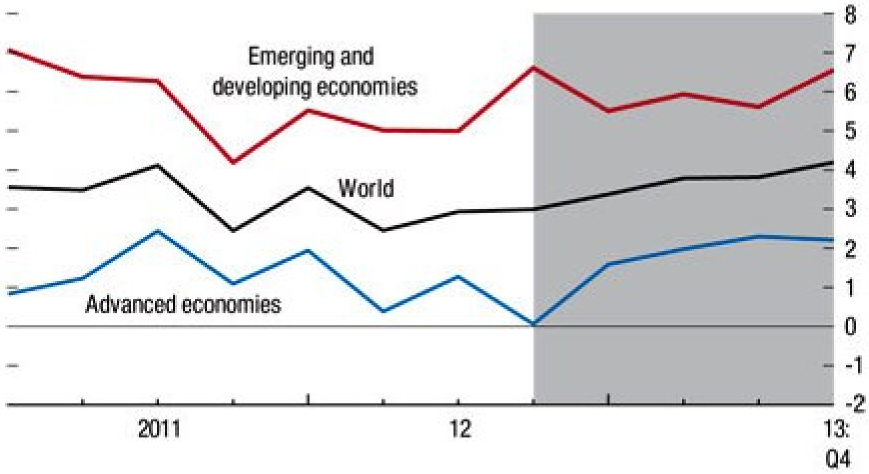
For the same period, most US stocks also rose, as investors were encouraged by stronger economic data and better than expected corporate earnings. The wide increase in the Standard & Poor's 500 Index of stocks, showing a five percent rise, also helped to soften the impact from a serious 12 percent fall in value for Apple stock, which suffered its largest decrease in four years.

Overall, the now strengthening US economy is expected to help restore global growth, as the economic recovery in the world's largest economy, with GDP expected to have grown by a 1.2 percent rate for the last three months of 2012, and matched by a return to growth in China, the number two economy, will underpin a more global recovery.

The Global Economy

The International Monetary Fund (IMF) released an update of its *World Economic Outlook* (www.imf.org) last week forecasting a 3.5 percent increase in the global economy for 2013. Although the forecast represents a downward correction to the previous prediction of a 3.6 percent rate of growth, it is still better than the 2012 level of 3.2 percent growth (see chart below). But two trends contribute an improved global economy included a pronounced recovery in the Chinese manufacturing sector, which expanded by fastest pace in two years, and a less than expected decrease in eurozone services and factory output for this month.

Global GDP Growth Forecast (quarterly percent)



Source: IMF *World Economic Outlook*, January 2013

In an accompanying set of policy recommendations, the IMF also highlighted the priority for the US government to "avoid excessive fiscal consolidation" over the short-term, to raise the "debt ceiling" limited on US debt, and to agree on "a credible medium-term fiscal consolidation plan, focused on entitlement and tax reform." For the eurozone, the IMF also noted the continued risk of "prolonged stagnation" and stressed that European leaders must continue reform, sustain "adjustment efforts in periphery countries" and adopt "further steps toward full banking union and greater fiscal integration." And turning to Asia, the IMF identified the priority for Japan as the need to renew an "emphasis on raising growth and inflation with more ambitious monetary policy easing," and recommended that the Japanese government "raise potential growth through structural reforms." For China, the IMF noted that "ensuring sustained rapid growth requires continued progress with market-oriented structural reforms" and a "rebalancing of the economy more toward private consumption." For the regions of the South Caucasus and Central Asia, the IMF outlook for 2013 remains favorable, in large part based on the impact from high oil prices, which benefit energy producers in those regions, and as commodity prices and the influx of remittances both contribute to economic improvement.

In other international developments, former Ukrainian Economy Minister Volodymyr Lanovyi warned last week that the Ukrainian government is in "real danger" of defaulting on its foreign loans in 2013. Lanovyi expressed concern over a serious decline in the level of Ukrainian central bank's hard-currency reserves, which now totals an estimated $25 billion, after some $10 billion in reserves were reportedly spent to meet mounting domestic demand for US dollars last year. He also added that the Ukrainian government is now challenged by meeting roughly $9.3 billion in approaching loan repayments to Russia and a mix of private investors and international lenders in 2013.

The Outlook for Europe

According to the International Monetary Fund's (IMF) recent World Economic Outlook, the 17-economy eurozone is expected to post a 0.2 percent economic contraction for 2013, replacing the IMF's earlier October 2012 forecast of a slight, 0.2 percent increase in the wider Eurozone economy. Elsewhere in Europe, the IMF also forecast German growth of 0.6 percent in 2013, but expected to increase by 1.4 percent next year, while the Spanish economy is expected to contract by 1.5 percent this year, before growing 0.8 percent in 2014. Italy is set to suffer an economic contraction of 1 percent in 2013 and then set to expand by 0.5 percent in 2014.

But European investors were reassured last week by European Central Bank (ECB) President Mario Draghi's statement that the worst of the European debt crisis may be over, matched by a significantly improved investor confidence in Germany, the largest economy in Europe, which rose to its highest level in nearly three years. And data to be released at the end of the month is expected to show a 0.4 percent contraction of the eurozone economy for the final quarter of 2012, with a record-high 11.8 percent eurozone unemployment rate and continued government-imposed austerity and serious budget cuts, suggesting a looming downturn in consumer spending and confidence. With new data released last week, Spain continues to be one of the most vulnerable economies in Europe, as unemployment rose to a record level of more than 26 percent for the closing quarter of 2012, account for more than 6 million out of work.

Focus on Asia

The outlook for the Asian economies remained mixed, as the Chinese economy is set to continue to grow by 8.2 percent this year, and 8.5 percent for 2014, reflecting a longer upward trend, while Japan continued to be plagued by slow economic growth, estimated to reach 1.2 percent this year, mainly due to new fiscal and monetary measures to stimulate its economy, and is expected to post a small 0.7 percent growth rate for 2014. And Asian stocks also rose significantly last week, driven by an improvement in the US economy and after declining Japanese consumer prices added pressure on the Japanese government to impose greater monetary stimulus, which in turn sparked a continued weekly gain for Japanese stocks for almost three months, in the longest consecutive gain in almost fifty years.

Global Commodities

Global oil prices rose for a seven-week consecutive advance last week, in the longest sustained increase in nearly four years, driven by signs of global economic recovery and declining crude oil stockpiles and inventories. Elsewhere in the global oil market, the roughly $10 billion Venezuelan oil industry suffered its first decrease in drop in funding and investment in five years, after from some of its closest partners, including China, India and Russia, each expressed concern over political uncertainty stemming from the poor health of Venezuela's President Hugo Chavez. The downturn in foreign investment and funding now undermines the country's capacity to stem its already serious decline in oil output and production, which declined by 13 percent, to 2.7 million barrels per day in 2011, since Chavez first came to power in 1999.

In a potentially major development for the global natural gas market, Ukraine signed a new agreement with Royal Dutch Shell last week, worth at least $10 billion, for the development of the Yuzivska shale-gas field in eastern Ukraine utilizing controversial new "fracking" technology, or hydraulic fracturing. Ukrainian shale-gas reserves are estimated to total 1.2 trillion cubic meters, roughly the third-largest in such deposits in Europe. Ukrainian officials explained that the level of investment from Shell would likely total roughly $10 billion, but could reach as much as $50 billion, depending on the conditions of the field.

In other developments in the global commodity market, the world largest producer of uranium, Kazakhstan, reported a new record for uranium output, to 20,900 tons in 2012, an increase from up the 2011 level of 19,400 tons. The new production figures raised Kazakhstan's global share of uranium production to an impressive 37 percent of total production for 2012. Kazakhstan sells most of its uranium output to Asia, with the Chinese, South Korean, Japanese and Indians being the largest customers.

Spotlight on Armenia

According to recent data released by the Armenian National Statistical Service (NSS), the Armenian economy increased by 7.2 percent in 2012, with increases in both agricultural and industrial output, and a slight 0.2 percent rise in the construction sector. In other data released last week, the Commonwealth of Independent Sates (CIS) Statistical Service reported that for the first nine months of 2012, the level of remittances and financial transfers from Russia to Armenia reached $877 million. Among CIS member states, Armenia was ranked sixth in terms of the total level of remittances from Russia, behind Uzbekistan, Tajikistan, Ukraine, Moldova and Kyrgyzstan.

Last week, Mihran Poghosyan, the head of the Armenian State Service for the Mandatory Execution of Judicial Acts (SMEJA), a law enforcement body agency empowered to carry out court-approved seizures of property and assets, reported a significant 20 percent increase in the level of asset seizures and confiscations for 2012. According to the official figures, the state agency seized more than $37 million (over 15 billion drams) in assets and property, with an overwhelming majority of cases involving the seizure and foreclosure of homes, residences and other personal property of Armenians for failing to relay loans from commercial banks.

The majority of these homeowners were low-income farmers defaulting on their credit payments who leveraged their rural property as collateral for the loans. Although the level and availability of agricultural loans and lending programs have expanded over the past decade, many of the private borrowers are unable to meet their payment schedules due to unexpected weather conditions, and sudden fluctuations in prices for seeds and fertilizer, as well as by poor crop harvests.

-Richard Giragosian