Due Diligence in the Post-Madoff Era | Alrroya

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As the old adage goes, fool me once, shame on you, fool me twice, shame on me. The saying is as true today as ever.

In 2008 and 2009 investors were harshly reminded of the importance of rigorous due diligence. Most painful was the 2008 revelation of Bernard Madoff's multi-billion-dollar Ponzi scheme, which defrauded hundreds of individual and institutional investors and whose ramifications are still being felt. But Madoff was not the first – or the last – to victimize unwary investors.

The "Ponzi Scheme" is named after Charles Ponzi, whose misdeeds led him to notoriety in the 1920s. Other financial schemes date back even earlier. After the stock crash of 1929, concerns over fraud and poor financial governance led to the development of "due diligence" as both a legal standard and business practicality.

The Securities Act of 1933 identifies due diligence as a legal defense for financial professionals accused of making inadequate disclosures to investors, especially with regard to the purchase of securities. Other legislation soon followed that required companies to conduct due diligence, and federal agencies stepped in to investigate suspicious investment programs. But despite government oversight, the investment world still remains a perilous environment for the unwary investor. Individual investors have often lacked the resources and understanding to conduct their own due diligence on the people and institutions who are managing their money.

Although Ponzi schemes and financial malfeasance continued through the 20th century, Madoff's massive scam brought unprecedented attention to the issues of fraud and due diligence. After seeing billions of dollars vanish before their eyes, investors are determined not to be fooled twice. In an effort to mitigate the risk of fraud and poor fund management, investors are increasingly demanding more transparency, liquidity, governance, and controls. When executed carefully, these demands converge via an investment through a managed account (or managed account solution).

A managed account that is structured properly will have the investor's assets in custody with a firm that is independent of the hedge fund manager. The hedge fund manager has limited power attorney which typically only grants authority to place trades in a specific account, and usually with specific guidelines. Under this process, the hedge fund manager will still get paid based upon performance, but will not retain control of the assets, nor access the assets. In essence, the hedge fund manager cannot touch the cookie jar.

Savvy investors recognize that they should be paying the hedge fund managers for producing alpha (i.e. adding value), and there is no need for the hedge fund manager to have control over the assets in order for them to be able to achieve this. The benefits to investors using a proper managed account solution include transparency, liquidity, and a great reduction in the probability of fraud.

Hedge Fund managers which balk at granting a managed account, are not adapting to the changing landscape and may be needing a reminder of exactly whose money that they are trading. It might be rightfully asked if these hedge funds have a strategy that is so special that they can dictate the terms to the clients who pay their bills, then why don't these hedge funds just become a private proprietary trading shop (i.e. don't take any external clients, and just trade the money of the owners)?

Under a Managed Accounts solution system, Madoff's fraud would not have been a possibility (the client would immediately detect that Madoff's "trading strategy" was not making trades, and it would not have been possible for Madoff to touch the money; Madoff's power of attorney would be revoked, and no damage the client would not have suffered any damage. This highlights the importance of transparency. Indeed, the following quote astutely summarizes one of the key benefits of transparency:

“Transparency is the best antiseptic” - Aleks Kins, Founder & CEO of AlphaMetrix

The quote above refers to the fact that people do not tend to act dishonestly if they know that they are being watched. More and more investors are learning that the importance of proper governance should not be neglected.

Meanwhile, earlier this year, another high-flying lawyer Scott Rothstein was found guilty for running a $1.2 billion investment Ponzi scheme from 2005 to 2009 that had fake investments. Fool me once, …

Email the writer:

Hedge Funds are not the Bad Guys | Alrroya

http://english.alrroya.com/content/hedge-funds-are-not-bad-guys April 4, 2011

In the aftermath of the 2008 financial crisis, the term “hedge fund” hit common vocabulary like never before. From catchy pizza commercials featuring the phrase “Not you, Mr. Hedge Fund,” to a strong Congressional push for regulation, hedge funds were constantly in the media and receiving much of the blame for the economic recession.

Eighteen months after the meltdown, media attention has faded somewhat, and reports indicate that economic spirits are lifting. Hedge fund assets, however, have not yet recovered to their pre-2008 levels, and many investors remain wary. Hedge funds are easily stigmatised given their propensity for secrecy, complex strategies, and tendency to only make headlines when something goes wrong.

With recovery in the air, perhaps now is the time to take a step back and look beyond those who most offended our sensibilities: Hedge funds are not the bad guys.

Hedge funds certainly were not perfect in 2008. They were criticised for a lack of transparency, gates (restrictions which limit an investor’s withdrawals during a redemption period), and long lock-up periods. Certainly, some hedge funds warranted the criticism they received; however, the positive contributions many of them made are often overlooked. The subset of the industry which trades managed futures, for example, had outstanding performance nearly across the board. There are many hedge funds out there which have provided good returns with decade-long track records. Hedge funds such as these routinely pass the due diligence of highly sophisticated investors like pensions, to the benefit of many including state employees and senior citizens.

Furthermore, the hedge fund industry is a meritocracy in a particularly meaningful way. Hedge fund managers are the small business owners of the financial world: hedge fund managers are entrepreneurs. They invest their own capital in the funds they trade. If their funds do poorly, they lose more than just their jobs. Also, in 2008, hedge funds did not take a single dollar of the United States governments’ $700 billion TARP bailout program. While many hedge funds had disappointing results in 2008, Managed Futures (or CTAs), a category of liquid hedge funds, by and large, did extremely well during the crisis.

Since 2008, the industry has changed and the savvy hedge funds are adapting to investors’ demands. The secrecy which had been commonplace prior to the financial crisis is being deemed less acceptable, and increasingly hedge funds are doing the unthinkable: giving managed accounts. Managed accounts allow a client better transparency, better liquidity, and better custody of assets which provides protection from gates and other potentially negative conditions.

Managed accounts are a solution to many of the potential drawbacks inherent in hedge fund investment. They are not, however, without their own complications. Managed accounts require strong operational and technological infrastructure. They are not protection from a bad investment: investors must still conduct proper, thorough due diligence before making any sort of investment. Moreover, though it is no longer impossible for investors to get managed accounts with top hedge funds, it might not be easy. To even consider giving a managed account, hedge funds often require a high minimum investment of anywhere from $5 million to $100 million. This poses a problem for an investor with an interest in managed accounts who lacks the capital to create a diversified portfolio of accounts with multiple hedge funds.

One alternative is to look beyond the hedge funds themselves. As investors return to the hedge fund industry, a substantial amount of the capital they are bringing with them is going into managed account platforms. This is a solution in which a company or bank secures managed accounts with numerous hedge funds, builds funds around those managed accounts, and makes it possible for their investors to invest into the managed accounts with a much lower minimum.

Managed account platforms can provide other benefits as well, including due diligence, risk monitoring, and superior technology. They can allow an investor to build a diversified portfolio for less capital than it might take to obtain one managed account independently. From a governance perspective, there is much appeal of a managed account solution.

There are many reasons that hedge funds remain a good investment and a good portfolio diversifier, and the industry’s willingness to adapt to investor demands is heartening. Now may be the time to act for those looking to invest (or re-invest) in hedge funds, and for those who lack the capital or risk appetite to invest in hedge fund in traditional ways, managed account platforms facilitate the investment process and give an extra layer of security that is comforting in the most turbulent economic times. Like everything else, there are both good quality and poor quality hedge funds, and rigorous due diligence is always a necessity.

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Importance of Cash Preservation and the Difficulty of Coming from Behind | Alrroya

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Question: If a person makes an investment that loses twenty per cent in 2008, and gains twenty percent in 2009, then are they back to even?

Answer: The investor would NOT be back to their original amount, and would be four percent below their original investment; in order to get back to even, the investment would have had to have a twenty-five per cent gain.

This result surprises some investors (and even some traders), although it is an application of simple arithmetic. Dennis Gartman, author of The Gartman Letter, refers to this as “The Viciousness of Percentages”. The table below helps to shows how difficult it is to recoup one’s capital after a loss.

Percent Loss	Percent Gain Needed to Get Back to Even
5%	5.26%
10%	11.11%
20%	25%
25%	33.33%
30%	42.86%
35%	53.85%
40%	66.67%
45%	81.82%
50%	100%
55%	122.22%
60%	150%
65%	185.71%
70%	233.33%
75%	300%
80%	400%
85%	566.67%
90%	900%
95%	1900%
96%	2400%
97%	3233.33%
98%	4900%
99%	9900%

The above table helps to demonstrate the importance of cash preservation, and the risk involved in trying to make an investment that “swings for the fences”. The formula used to generate the above is that a loss of k, requires a gain of k/(1-k). For instance, a loss of 50 per cent (k=0.5), needs a subsequent gain of 100 per cent.

Investments that have very high returns, may also experience large losses. Living by the sword can lead to dying by the sword. It becomes increasingly difficult of recovering from a large loss. The above table does not take the time value of money into consideration (i.e. that a dollar two years from now, is worth less than a dollar today), and consequently is conservative in its assessment of the increase required in order to come back.

The table is also purely quantitative, and does not take qualitative issues into consideration which also may make it more difficult to gain back the original capital. For instance, large losses may hurt the morale of the trader, or lead to less resources being available for the company.

It is important to note, that all of this must be taken with some moderation. An investment that never experiences a negative return is of course a red flag in itself, and rebounding from modest losses is entirely possible for most investment firms. This is more applicable as the losses become higher.

The mathematics of cash preservation and the difficulty of coming from behind are simple yet very important. It is also connected in flavor to a deeper and more famous (for mathematicians) problem in mathematics aptly called “The Gambler’s Ruin”.

The Gambler’s Ruin, which has its origins to work done by French Mathematician Blaise Pascal in 1656, was influential in the early development of probability theory. The Gambler’s Ruin essentially proves that “doubling down” until a favorable outcome occurs is a losing strategy unless one has an infinite bankroll.

Conducting proper and prudent due diligence is definitely helpful in understanding the risk-reward potential of an investment, and reducing the probability of investing in a programme that falls to the point of no return.

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Angola: West Africa’s Rising Star | Alrroya

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Substantial economic growth in Africa is not just the dream of emerging market enthusiasts; it’s an inevitable force as global demand continues to increase.

With varied political landscapes, diverse inhabitants, multiple exchanges, and 53 autonomous countries, it becomes difficult to decipher which countries in Africa are poised to be the most influential to the continents economic development.

According to the African Economic Outlook 2010 report created by the African Development Bank, the United Nations Economic Commission for Africa and the Organization for Economic Co-operation and Development, Africa will grow 4.5 per cent in 2010 and 5.2% in 2011.

Aside from South Africa, there are a multitude of countries that look to become significant contributors to the economic growth of the continent. Over the past few years, Angola, located in the western portion of Sub-Saharan Africa, is gradually becoming the continent’s rising star.

The previously mentioned African Economic Outlook 2010 report also forecasts that the Angolan economy will have indicated growth of around 7 percent. The IMF maintained this estimated prediction in a new publication “Regional Outlook” for Africa, available at the end of May.

Angola’s economy is heavily dependent upon oil demand as this particular commodity makes up over 90% of the country’s exports. Angola is currently Africa’s second largest oil producer with an output of about 1.92 million barrels of oil per day in the first quarter, according to the International Energy Agency. Further, it is theorized that by 2011 Angola could possibly overtake Nigeria, which is currently generating an estimated output of 2.3 million barrels of oil per day.

Who is most of this oil going to? China. The economic bond between Angola and China has grown much stronger within the past years. This strengthening connection is largely due to China’s increase in overseas oil production. According to a recent article in Bloomberg, as Chinese state-owned companies purchased and swapped loans for supply, overseas oil output increased to roughly 1.5 million barrels a day from 1.1 million barrels a day.

“Chinese oil companies are now operating in the upstream sector of 31 countries and have equity production in 20,” the IEA said. “Their equity shares are overwhelmingly concentrated in only four: Kazakhstan, Sudan, Venezuela and Angola. Last year, the country imported 47 percent of its oil from the Middle East with Saudi Arabia, Angola and Iran the largest suppliers”

Aside from oil, Angola’s diamond industry is another staple of the country’s economy. Companies like De Beers, the world’s largest diamond producer, and Alrosa have invested millions of dollars to transform Angola into one of the world’s biggest diamond exporters. According to an article from Reuters, Angola is now the world’s fifth largest diamond producer. Northeastern Angola, mostly in the provinces of Lunda Norte and Lunda Sul, is known for its bountiful diamond reserves and is an abundant source of the finest quality stones. Roughly 70% of the diamonds discovered in this region are of great quality.

In the wake of this relatively newfound influx of foreign investment, the Angolan government has slowly begun to implement laws to bring revenue to the community. The most recent of which is a law that will require diamond companies to use 50 percent of their revenues to pay for operational costs and the remaining 50 percent to pay taxes, investors and help the local community.

"The goal is to make the mining sector more attractive for investors and also contribute to the development of local communities," says Sebastiao Panzo, an official for Endiama, a state-run diamond company.

Angola’s promising future is a far cry from its troubling past. From 1975 until 2002 Angola endured a civil war between its Government, with support from the Cuban military, and Angolan rebels. This conflict has left at least 500,000 Angolans dead and over 4 million displaced. Poor infrastructure and corrupt governments have been liabilities previously, and Angola must stay clear of these problems if she wishes to prosper and improve.

Since the civil war there have been significant strides towards improving the quality of life for Angolan citizens. The Angolan Government has been able to gain capital due to taxes on oil and diamond extraction profits. This has allowed them to increase the governmental budget and improve the Angolan infrastructure and educational system. This economic optimism should ultimately improve the conditions of Angola and the returns of its investors.

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China’s Corn: From Surplus to Scarcity | Alrroya

http://english.alrroya.com/content/china%25E2%2580%2599s-corn-surplus-scarcity April 4, 2011

, By Ranjan Bhaduri & Oisze Lam Altonaga, AlphaMetrix Alternative Investment Advisors

Unfavorable weather conditions in China have observers concerned that China’s corn production could not sustain the nation’s demand. The cost of Chinese corn is currently more than double the price in Chicago. As a result, China purchased 115,000 metric tons of corn from U.S. exporters this year, the largest reported transaction since 2001.

A drought in China’s Northeast regions reduced the national corn output by 13 percent, creating a 7-8 million ton shortage. Moreover, current heavy rainfall in southwestern China may further reduce corn harvest by as much as 2,700 tons. Similar shortfalls have become increasingly common in China’s grain markets spurring an additional purchase of 600,000 tons of U.S. corn for delivery before September 2010, according to the U.S. Grains Council.

In addition to decreased output last year, a Chinese government-issued policy last November to subsidize southern buyers to purchase northeast corn also pushed up market prices beginning earlier this year. The policy was aimed at increasing corn farmers' revenues by attracting more southern buyers to purchase corn domestically rather than importing from the United States. China’s corn prices are generally 20-40 percent higher than U.S. prices due to ocean freight costs and taxes preventing imported corn from being price-competitive.

Provisional corn reserves went on the market in June 2010, the nation’s most recent effort to curb skyrocketing prices. As much as 30 percent of the grain in some stockpiles have showed “significant signs of degradation” caused by mold due to high temperatures. Chinese Corn output is expected to reach 170 million tons this year, 6 million tons more than last year if there is no drought in major growing regions, said Sun Yu, a corn analyst with Galaxy Futures. The profitability of the pig farming industry, however, the largest consumer of corn, may offset the effect. China’s corn consumption this year may be 150 million tons, the grain administration’s Zeng said.

But China has been working hard to keep up with the demand within its own borders. Ever since it was introduced to China, corn production has expanded steadily, at some points creating a surplus. Less than a year ago, the U.S. Department of Agriculture reported that China’s corn supply exceeded demand. The government has encouraged the intelligent development of the corn industry to overcome the problems that the country and its farmers face today.

Chinese Corn Production

Corn was first introduced to China in the 16th century by early European missionaries. Originally stemming from the east coast, corn is now grown in every province in China. About two thirds of Chinese corn is grown in temperate conditions in the northern and eastern coastal provinces. The rest is grown in subtropical and tropical regions.

Cold temperatures and short growing seasons limit farmers to one crop a year in northeast China. In the rest of China, corn is commonly grown as the second crop in tight annual rotations. Corn production now ranks second to rice production. While all grain prices have risen since the early 1990s, corn prices have risen faster and remained relatively higher than wheat and rice. Chinese policymakers have set minimum purchase prices for corn which have encouraged farmers to plant the crop.

Since the early 1980’s, China’s consumption of pork, beef, and poultry has more than tripled. Corn is primarily used as animal feed and increasingly in large scale commercial hog and poultry operations.

Xu Xiaoqing, deputy director of the Development Research Center of the State Council, says

China’s farmland area will decline to 119 million hectares this year and to 109 million hectares by 2020 (compared with 128 million hectares in 2001). The drop is caused by urbanization, industrialization and a lack of water, Xu said.

Chinese Premier Wen Jiabao recently visited Poliwang village in Central China, a major wheat-producing area, urging local governments to harvest crops as soon as possible and to strengthen field management. According to Wen, a good summer harvest and stable farm produce prices are crucial for managing inflation expectations and for realizing the nation's macroeconomic targets this year. Agriculture is a cornerstone for the national economy and the nation must always attach great importance to agricultural production, Wen advises.

Amid the nation’s efforts in improving sustainability, the current shortage cannot be resolved immediately. Rising imports by China is expected to prolong as reserves are being rebuilt. There is evidence that there will be an increasing global demand for corn, and it would appear to be an excellent opportunity for the U.S. to increase its supply.

The U.S. Department of Agriculture forecasts that China, consuming 19 percent of global output this year, may boost overseas purchases. The nation will probably more than double targeted imports in the year starting October 1st to 3.5 million tons from 1.5 million tons, according to Li Qiang, managing director of Shanghai JC Intelligence Co.

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Growth in Africa Extends Beyond World Cup | Alrroya

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, By Dr Ranjan Bhaduri & Lucas Monroe, AlphaMetrix Alternative Investment Advisors

Today more eyes from around the world are focused on Africa than ever before, as South Africa hosts the World Cup.

Although the excitement and attention Africa has received may not extend beyond July 11, Africa has been and still is a land of opportunity with a bright future that will remain long after the glory of the Cup fades. Second to Asia, Africa is the world's largest and most populous continent and leaders from all over the world have been examining Africa long before the Cup.

The United States, China, India, Brazil and many countries from the European Union are investing in, trading and researching the continent's most promising of markets. Even though many of these countries have been involved in trading with Africa for some time, the prospect for growth is staggering.

During a recent Diplomacy Briefing Series on Sub-Saharan Africa given June 14th, 2010, Secretary of State Hillary Clinton stated that the U.S. wants to build a relationship with Africa not based on patronage, but on partnership. This mindset would benefit all trading partners and investors who are recognizing the rise of African governments increasing presence on the world stage.

Africa is located close to the two Asian powers, India and China, neither of which have shied away from investing with Africa. For example, since India set up trade with South Africa in 1993, their trade volume has grown from 93 million dollars per year to 4.5 billion dollars in 2009. Taking advantage of this progress, South African President Jacob Zuma visited India with a goal of increasing interaction to 10 billion dollars of bilateral trade by the year 2012.

This may be a difficult goal to achieve, but Zuma looks ahead to a large increase in value-added trade between the two countries. Indian car companies Tata Motors and Mahindra & Mahindra have both recently launched new vehicles in South Africa's motor industry. Other goods, such as information and communications technology, energy and pharmaceuticals are expected to help continue the increasing trade.

In another effort to grow this relationship, India launched a "Focus: Africa" program in 2002 to promote relations with African countries. During the Focus Africa program, 500 Indian farmers were sent to East Africa to cultivate land in the East African nations, mainly in Kenya and Uganda. It was seen as a way for Indian farmers to utilize their knowledge on valuable farm land, which was hard to come by in India. Now the gates are open for Indian farmers and corporations alike to lease land in Africa. Countries with the most significant opportunities include Ethiopia, Congo, Ghana, Liberia, Malwai, Uganda, Kenya and Rwanda. African countries have been fairly receptive to Indian businesses because they create jobs that allow the community to grow.

In addition to India, China sees Africa as a land that can help facilitate the ever changing Chinese economy. In 2007, China pledged $20 billion dollars towards trade and infrastructure over the next three years. Together, Angola and Sudan supply China with a third of its oil and a significant amount of other natural resources. China is experiencing a large growth in its middle class, which is expected to grow from 80 million people in 2007 to 700 million people by the year 2020.

This burgeoning middle class will experience increases in purchasing power, and require businesses in China to meet their needs. China may need to rely on Africa more than they have in the past. Growth in China is occurring outside the largest cities where more building needs to occur, which will likely cause China to look to Africa to fulfill their natural resource needs.

“There’s no reason why African countries with all of these resources cannot be so much richer,” Clinton said at the diplomacy series.

Africa has a diverse range of countries that want their goods. The increase of capital that India and China have invested into Africa in the past decade has decreased Africa’s reliance on North America and The European Union, thus making Africa’s success less correlated to any single country.

It certainly seems as if African countries have the resources and ability to become richer. The task of realizing this potential, however, seems daunting when considering some of the obstacles that Africa faces: trade between countries within Africa, corruption, and poverty.

Yet these obstacles are much more manageable when global forces from all over the world rely on Africa to progress in years to come. The people of Africa will play a crucial role in deciding how far their continent will progress, and by then the rest of the world may be watching.

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Housing, Inflation and the Chinese Middle Class | Alrroya

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, By: Ranjan Bhaduri and Bart Scagnelli, AlphaMetrix Alternative Investment Advisors

The past decade has seen substantial growth in the Chinese middle class. Growing from 65.5 to 80 million between 2005 and 2007, the Chinese middle class is expected to expand to a massive 700 million by 2020. While the percentage of the population that fits into this category is still far below the 60 per cent in many developed countries, there seems to be tremendous desire among Chinese families to join the ranks of the middle class.

A December 2009 survey of Chinese workers showed that the average period within which they expected to become middle class was 5.85 years. Almost 70 per cent said they wanted to become middle class within 5 years.

Several reasons have been cited for this growth. Steady improvements in the quality and availability of education have led to an increase in the percentage of the population with college degrees. At the same time, foreign companies that have come in to take advantage of China’s booming economy have created jobs for educated, middle-class workers. The overall effect is that disposable income and home sales have jumped among the middle class. But while these results have created new opportunities for foreign investment and local entrepreneurship, they have also created challenges for foreign investors as well as the Chinese government.

Businesses have not hesitated to take advantage of this growing market. Many consumer goods and retail companies such as Procter & Gamble, Inditex, and Tesco are making major investments in China. But China’s landmass is enormous, and one challenge for foreign investments has been identifying the best areas to cater to the growing middle class.

According to a recent article in Forbes, In 2005, a consumer company doing business in 70 locations (cities and counties) in China could reach 70 per cent of consumers in the middle and affluent classes. To achieve the same coverage today, a company must be in nearly 240 locations. By 2020, that number will exceed 400. A dramatic shift in the geographic distribution of consumer spending power is under way in China. The middle classes are expanding out beyond the largest cities more rapidly and in greater numbers than any market has ever witnessed.

Just as the location of the burgeoning middle class is creating challenges for foreign investments, their impact on the housing market as a whole is also raising concerns. Skyrocketing home prices may actually stifle the growth of the middle class, as more and more workers find themselves priced out of home ownership. According to Gu Yunchang, Deputy Director of China Real Estate Research Association, Chinese people will pay half of their income to buy an apartment this year. Experts predict the government will react by strengthening regulation and control on the real estate industry in 2010. The effectiveness of the government’s regulation will be an important issue in the years to come.

Projections about the growth of the middle class are susceptible to a multitude of variables, and poor governance could undermine this growing market. Furthermore, with the impact of the U.S. housing meltdown still fresh in mind, some foreign businesses may be hesitant to invest too heavily in a middle class that could be undercut by a similarly disastrous housing bubble.

Increases in property prices followed record levels of lending by domestic banks and a 4 trillion yuan (about $585 billion) stimulus package. These facts also call attention to another issue of concern to foreign investors and the Chinese government: inflation.

With the growth in the middle class, increased disposable income, and the economy as a whole indicative of China’s formidable presence on the world stage, many in China’s government recognise that uncontrolled economic growth can lead to runaway inflation rates later on.

As workers pour a large portion of their income into their homes, inflation could severely undermine the buying power of the middle class’s disposable income. Goldman Sachs' chief economist, John O'Neill, has recently hinted that China may move to strengthen its currency as much as 5 per cent in a bid to slow the pace of its economic growth. O’Neill’s prediction followed an announcement by China's central bank of a 50 basis-point rise in commercial bank reserve requirements in a bid to soak up excess liquidity.

Chinese authorities are also moving to curb credit growth in response to 2009’s fourth quarter numbers, in which the economy registered its fastest growth since 2007. So far the 2010 numbers suggest that the situation is not yet under control. Data indicates that banks in China had already extended about $1.1 trillion, or 19 per cent of the 2010 lending target of 7.5 trillion yuan, in January alone.

Indonesia’s Growth Led by its Private Sector | Alrroya

http://english.alrroya.com/content/indonesia%25E2%2580%2599s-grow th-led-its-private-sector April 4, 2011

, By Dr Ranjan Bhaduri and Lucas Monroe, AlphaMetrix Alternative Investment Advisors

While some economies around the world stalled or even shrank in the wake of the recent global financial crisis, Indonesia has seen steady economic growth. Between 2007 and 2009, Indonesia’s GDP grew approximately 6.3 per cent, 6.1 per cent, and 4.5 per cent respectively. The region’s growth has not showed signs of easing soon, as it is expected to grow about 6 per cent in 2010. Amidst growing interest in Indonesia’s labor force and consumer base, the nation is part of a new wave of emerging markets fast on the heels of the BRICs.

Indonesia is the fourth most populous country in the world with 230 million people, and has the largest Muslim population of any country in the world. The largest economy in Southeast Asia, Indonesia is comprised of 17,500 islands in the Pacific. Credit rating agencies throughout the world have taken note of the positive trends emerging from Indonesia.

Fitch Ratings, Standard & Poor’s and Moody’s Investors Service have all upgraded their ratings on Indonesia’s outlook and debt. According to Bloomberg Businessweek, some investors expect to see Indonesia become an investment grade country within the next year to year and a half.

Indonesia’s steady growth can be partially attributed to its robust domestic consumption. About two thirds of the nation’s economy is based on domestic consumption. While other nations’ economies rely heavily on exports and foreign consumption, Indonesia’s strong consumer base helped insulate its economy from the global financial crisis. According to a recent BBC report, some of Indonesia’s largest department stores, which serve its growing middles class consumers, receive 80 per cent of their goods from domestic factories. As consumer purchasing power grows, so do domestic sales of locally produced goods. The higher demand for goods fuels increased production, creating new jobs, higher salaries, and an increased standard of living. This trickle-down effect channels the growth in Indonesia’s economy, protecting it to some extent from the global recession.

In the past five years Indonesia’s large population, room for growth, and low labor costs has also attracted the attention of foreign companies. Indonesia has the lowest unit labor costs in the Asia-Pacific, attracting foreign companies looking to expand their manufacturing activities. According to the Jakarta Globe, during the first half of 2010 foreign investment in Indonesia was up almost fifty percent compared to 2009. The levels of foreign investment have noticeably surpassed pre-financial crisis levels, reaching a total of $7.8 Bilion during the first half this year, compared to $6.5 Billion during the same period in 2008. Indonesia also expects continued growth in the size and earning power of its middle class, which currently makes up 35 million Indonesians. In June, Nissan announced plans to double production capacity and quadruple sales in Indonesia by 2013.

Indonesia has been an attractive region to sell goods, as well as manufacture them. Indonesia’s consumption habits are forecasted to continue to increase. In the past four years, Indonesia has seen a large number of shopping malls open up, conveniently located near business centers such as the Jakarta Stock Exchange. International franchises such as Starbucks and McDonald’s have also opened stores that are geared towards the Indonesian middle class. Transportation, housing and telecommunications sectors combined to attract 40 per cent of foreign investment in the 2nd quarter—a clear sign of a growing economy. As foreign companies expand their operations in Indonesia more jobs will be created and consumption will likely increase, thus continuing the cycle that has helped Indonesia grow in the 2000s.

However, despite the success that Indonesia has recently seen, the nation still faces some significant challenges. First challenge, and perhaps its greatest challenge, is its high level of poverty. It is estimated that almost half of all Indonesians live on less than two dollars a day. These people are largely unemployed and poorly educated. Although the average income has doubled to

$2,350 in the past 5 years, there is still room for improvement. An increase in factory jobs could benefit those in the lower income class and increase their income levels. A better opportunity of education for these folks is important. There is also a rising concern about high levels of inflation, reaching a yearly high in July.

With rising food prices and electricity tariffs, the state-run Bank Indonesia is keeping a tight watch on inflation, which is not unusual for a growing economy. In the first week of August Bank Indonesia maintained the benchmark rate of 6.5 per cent. On August 16th Susilo Bambang Yudhoyono, President of Indonesia, gave a Speech to Parliament that highlighted Indonesia's growth. Yudhoyono stated that Indonesia should reach 7.7 per cent annual economic growth in 2014 and hoped to slash poverty by ten percent within that time. These are lofty and difficult goals, and it remains to be seen what will actually be attained.

Overall, though Indonesia's growing economy shows has not shown many signs of slowing down. Perhaps one of the most encouraging signs of Indonesia's economic stability is the fact that its growth has not been fueled by government intervention. Instead, about 90 per cent of the nation's GDP comes from the private sector. With a growing labor force, consumer base, and lack of government intervention, the nation's outlook seems to remains favorable for its population and foreign investors alike.

Email the writer:

Saudi Arabia, China and the Energy Shift | Alrroya

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Since forming diplomatic relations in the summer of 1990, the economic and diplomatic bond between Saudi Arabia and China has greatly tightened during the past decade.

Since China began importing oil in 1993, it has become the second largest consumer of petroleum in the world, and is now Saudi Arabia's top oil customer. Both countries have substantially benefited from the relationship.

China takes advantage of Saudi Arabia's liberally regulated business practices and increased privatization. Saudi Arabia has continually benefitted from China's "no questions asked" attitude, and has reduced its total reliance on the US for exporting oil.

China, recognizing the potential of this relationship, began an effort to develop it further. In the early 2000s, China worked to gain a stable and solid relationship with the Kingdom. The effort was met with great success.

In a two year time period Saudi Arabia and China engaged in regular political meetings and formal talks with Opec, ultimately signing a deal allowing China's government run oil company to explore for gas in the Kingdom's vast Empty Quarter (Rub al Khali). The Kingdom did not hesitate to reach out to China either.

In January 2006, the Saudi King Abdullah bin Abdul-Aziz al Saud was the first Saudi King to visit China, and his first visit outside the Middle East after taking the throne. Many called this move "a strategic shift" in Saudi foreign policy. During the visit, the two countries signed a pact on energy cooperation and joint investments, and also discussed other issues including trade, taxation, and deals with the Saudi Arabian Development Bank.

Saudi-China relationship reached a landmark in the past decade with total trade volume reaching more that US $10 billion. According to an Arab News article by John Sfakianakis, Saudi Arabia exports saw a 10 year increase of 3,463 per cent, with Chinese exports experiencing a strong 167 per cent growth. Saudi Arabia's exports were valued at US $7 billion and consisted of refined oil and plastic material.

Chinese exports were between $2 and $3 billion, consisting mainly of clothes, appliances, mechanical/construction equipment, and a small percentage of Chinese automobiles. Both powerhouses have found a huge trading partner and their growing relationship has no end in sight, as the estimated goal of $40 billion in bilateral trade by 2010 was reached in 2008.

Following King Abdullah's January 2006 visit to China, Chinese President Hu recently visited the Saudi city of Riyadh in April 2010. The meeting further solidified their relationship as the Kingdom recognized China's rising economic influence and presence on the world stage as well as its appetite for hydrocarbon resources. Both sides continued their discussions over trade, businesses, oil, natural gas and minerals.

Now, there are more than 90 Chinese companies doing business in Saudi Arabia, most of which are construction companies. Besides the topic of trade, Saudi Arabia and China have also initiated talks about reforming global financial institutions. Both countries want to work closely in mutual investments and ensuring that they are protected from high financial risks.

China has surpassed the United States as the leading consumer of Saudi oil. Many have termed this shift of the energy trade from West to East as a shift in the geopolitics of oil. Riyadh based Jadwa Investment's research director Brad Bourland states that, "Saudi Arabia used to be very much an American story, but those days are gone forever.

That’s just a reflection of a globalized world and the rise of Asia. They now see their relationship with China as very strategic and very long term.” On the other hand, a US-Saudi Arabia relationship is far from over, as it is just not a business relationship like how it is in China, it is much deeper with political implications that will not die down any time soon.

A relationship between China and Saudi Arabia is mutually beneficial. Saudi Arabia was the largest donor for China’s May 2008 earthquake relief.

The Kingdom can take advantage of having the second largest economy on their side, and make use of the China’s increasing need for energy. Over the next two years China’s demand for oil will grow by one million barrels per day.

China, on the other hand, benefits by having a reliable resource to meet its energy needs, allying itself with another Asian force, and also increasing its global influence overall.

* With contribution from Sabah Rehman

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Strengthening Africa’s Grain Trade through Market-based Solutions | Alrroya

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, By Dr Ranjan Bhaduri and Bart Scagnelli, AlphaMetrix Alternative Investment Advisors

When it comes to grains, Africa’s diversity and resources make it a key region today and in the years to come. Africa is home to more native cereals than any continent, and many see this genetic wealth as the future of crop development.

While the grain industry spends billions of dollars to develop genetically advantageous strains of corn, wheat, and other traditional commodity-yielding crops, Africa is sitting on a cornucopia of natural genetic diversity. As Africa’s less-mainstream grains such as Sorghum, Pearl Millet, and Tef gain a foothold in global markets, the continent is also seeing improvements in the production and marketing of mainstream grains due to progress in storage, trade, and finance arrangements.

Rice was the first traditional grain to make its way to the African continent centuries ago. In the 16th century, maize was brought over, followed by modern strains of wheat. With the introduction of these seeds, African grain production has shifted from ancestral strains to the mainstream foreign strains. Modern trading of these grains has been stifled to some degree by inefficiencies inherent in African trade systems. But promising improvements in the system advocated by groups like the East African Grain Council have lessened and, in some cases, eliminated these inefficiencies.

According to a recent EAGC newsletter, the organization promotes agricultural market institutions and best practices, including “adequate storage capacity, organized small scale farmers who have capacity to aggregate volume, institutionalized and harmonized grades and standards, and adherence to contracts and rules of trade.” With this in mind, the Council has advocated the implementation of structured trading systems, which are large-scale organizational structures that bring market participants together in an orderly way.

One important building block of a structured trading system is a Warehouse Receipt System. WRS allows farmers to aggregate their harvest yields and efficiently deliver them to warehouses efficiently. With reliable warehouse receipts, banks can advance loans that allow farmers to sustain and expand their operations. Surplus output can be stored for later sale when prices are higher.

These efforts have helped to protect the industry from loss. Other elements of a structured trading system address inefficiency through better communication between trading partners. These systems, which are standard in other grain producing markets, promise to greatly improve the liquidity, efficiency, and ease of grain trading in Africa.

But overproduction of mainstream grains exposes African grain markets to a potential vulnerability, which is why the wealth of indigenous grains may prove especially valuable in the future.

Kenya was recently reminded of the dangers of relying too heavily on individual strains of grain. A fungus growing on maize crops in Kenya has contaminated 2.3 million bags of the commodity, making it too toxic for human or even animal consumption. The toxin, known as aflatoxin, is a poisonous cancer-causing chemical. Millions of small-scale Kenyan farmers rely on maize, which is the country’s main staple. Although scientists have since found solutions to deal with the aflatoxin problem, other diseases, fungus, and parasitic insects could have similarly disastrous effects on African and other regional grain markets.

Local farmers and industry could protect themselves through diversification much like a hedge fund manager protects a portfolio from individual sector risk, by incorporating more varieties of grain into African markets. There is also opportunity for African companies to export some of the continent’s genetic diversity to other countries, where particular strains might be especially robust.

Meanwhile, improvements in trading and marketing systems are reinforcing the stability and productivity of African grain producers. All these factors contribute to a bright outlook for African grain opportunities in the future, and likewise for grain traders who pay close attention to African markets.

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Sustainable Wealth: The Future of African Economies? | Alrroya

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For hundreds of years, Africa's substantial natural resources have captured the attention of foreign businesses and nations. Outside interests have traditionally sought to tap the continent's reserves of ivory, precious metals, and of course, oil. But until recently, foreign investment in sustainable economic development has largely eluded African economies. Now, renewed interest in Africa promises more sustainable economic growth, an encouraging prospect for African nations as well as global businesses that hope to serve the continent's population of over one billion people.

Three important developments have changed the way the world looks at Africa: Hedge funds have been watching Africa's emerging markets as an attractive source of alternative investment opportunities. Energy companies are also eyeing the continent's untapped oil and gas reserves which are more accessible in the wake of increasing political stability. Finally, microloan banks and non-profit groups such as MBAs Without Borders are developing sustainable economies at the grassroots level, raising the standard of life and purchasing power of the African population. Although challenges still lie ahead for Africa, these recent developments have the potential to transform Africa into a sustained source of wealth and consumer demand.

Hedge Funds

Hedge funds have long looked to the emerging markets in Asian and South American countries for alternative investment opportunities. But some alternative investment vehicles are beginning to look at emerging markets in Africa. With significant advances in the availability of technology and access to the benefits of globalization, Africa could become the new frontier for emerging market alternative investment managers.

Africa's 53 countries make up nearly 20% of the world's land mass, and are home to over a billion people. Grassroots economic development is strengthening the buying power of many Africans, presenting opportunities for corporations seeking an underserved consumer base with limited competition.

Historically, internal conflicts and overwhelming external debt have discouraged foreign investment managers. But as these factors are beginning to subside, hedge funds and institutional investors are taking a second look. For example, Renaissance Capital has established its Africa Fund and Oryx SA Fund (the largest South African Hedge Fund) to focus solely on securities and commodities associated with Africa.

Most of Africa's hedge funds are located in South Africa, which is home to the Johannesburg Stock Exchange (JSE), the 17th largest stock exchange in the world. But other African countries have progressed towards political and financial stabilization, allowing hedge funds to branch out beyond South Africa.

For example Zephyr Management's Pan-African Investment Partner Fund and ZM Africa Investment Fund demonstrate the growing interest in African infrastructure, insurance companies, and consumer credit institutions.

Energy

Much of Africa's sustainable growth is also fueled by a renewed interest in its untapped oil and natural gas reserves. While energy exportation has thrived for years in OPEC member nations such as Nigeria and Angola, the changing energy trade is driving interest in other African countries as well. The United States and China are hoping that these reserves will provide a solution to their energy problems, leading companies such as Canadian Natural Resources to pour money into energy exploration projects in Africa.

According to Shawn McCarthy, a global energy reporter, CNRL will spend $260 million to develop offshore oil production in Africa. In 2009, Exxon Mobil spent $6.2 billion in exploration and development in Africa, putting Africa just behind Asia and the Middle East in terms of capital allocation. McCarthy has posited that countries like Ivory Coast and Sierra Leone might use their oil revenues to finance reconstruction in the wake of recent civil wars.

Grassroots

Africa is also seeing investment at the grassroots level. Banks and nonprofits are investing directly in Africa’s population. Grassroots investment, which strengthens the earning and spending power of the continent’s one billion inhabitants, will be important to creating a sustainable economy in Africa. By empowering Africa’s population to create their own wealth independent from natural resources, grassroots investment helps Africans to start their own businesses and take advantage of the benefits of globalization.

Microloans have been helping African entrepreneurs build new sources of wealth for over thirty years. ACCION, an organization that offers financial services to Africa’s poorest residents, has lent more than $145 million over the past 10 years. Kiva, another microloan lender, has lent over $137 million. The loans, which are typically for amounts between $20 and $200, are used to purchase assets for new businesses. Microlending received great attention in 2006 after Muhammed Yunus won the Nobel Prize for his work with Grameen Bank (another microlender).

MBAs Without Borders (MWB) is another source of grassroots investment in Africa. MWN partners MBAs with local businesses, multinational corporations, and NGOs with the goal of fostering trade and social development. Members of the organization train underdeveloped populations to better conceptualize, market, and implement their own local businesses. Rather than donating raw goods, MWB provides Africans with the knowledge and tools to succeed in a globalized marketplace, which in turn raises income and living standards.

Conclusion

The African Union, an intergovernmental organization established in 2002 that includes all African states except Morocco, plans to create a single currency for the countries within the organization by 2023. Developments such as that would increase the stability of many African nations. Increased stability, along with foreign investment in the form of hedge funds, energy exploration, and microcredit, can help Africa build a sustainable economy that will outlast its natural resources.

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U.S. and Saudi Business Interests Come Together in Chicago | Alrroya

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The 2010 US-Saudi Business Opportunities Forum brought together almost 1,100 senior executives and high-level government officials from Saudi Arabia and the United States. The forum, which was held in Chicago on April 27-29, sought to enhance economic cooperation between the two countries. This cooperation bore fruit, with several companies entering into agreements with Saudi officials.

For example, General Electric Co. and the Saudi Ministry of Commerce signed an agreement to explore manufacturing opportunities in the Middle East. Morgan Stanley also signed an agreement with the National Commercial Bank of Saudi Arabia for advisory services relating to the privatisation of its main division. The coming together of U.S businesses and Saudi government officials, and the forum itself, were possible due to the efforts of the U.S.-Saudi Arabian Business Council.

The U.S.- Saudi Arabian Business Council, which hosted the event, was formed in December 1993 to bring about a greater understanding of the U.S. and Saudi cultures and business issues. The council began an important dialogue between business representative of both countries, with the goal of developing trade and investment. Both the U.S. and Saudi governments have supported the council, which is reflected in the participation of the Minister and Secretary of Commerce from both countries.

The two day conference offered informative panels and discussions from numerous high level speakers. William Daley, former US Secretary of Commerce and current Chairman of the U.S.-Saudi Business Opportunities Forum, opened the first session. The first day included a panel with the Saudi Minister of Finance, the President of J.P. Morgan Chase, and the Saudi Chairman of the Capital Market Authority discussing the nations' role in the new economic order. This was followed by a discussion between the President of The Boeing Company and the current US Secretary of Commerce regarding ways to expand US-Saudi trade during an increasingly competitive world. The delegations concluded the day with a grand dinner at Chicago's Navy Pier, and had speeches from Chicago's Mayor Richard Daley, the US Ambassador to Saudi Arabia, and the Saudi Arabian Ambassador to the United States.

The U.S. and Saudi delegations spent the second day of the forum discussing new opportunities in the energy, water, and electricity sectors. Although Saudi Arabia's economy is doing well despite the global economic crisis, participants in the forum spoke with one voice when identifying the need for cooperation in order to promote global economic recovery. During the day's Saudi Arabia Infrastructure Development and Agricultural Development panels, Saudi ministers discussed their work on forming a knowledge-based society with increased infrastructure development. They also expressed the growing sentiment that the nation no longer wants to be known as, "the gas station of the world."

The last session included many workshops and panels regarding commercial investment opportunities in the Kingdom, as well as incentives promoting Saudi trade and investments. Overall, the Kingdom presented the United States with numerous investments worth almost 1 trillion riyals (266 billion USD).

For attendees needing a break from the discussions, the forum offered shows for the 3D IMAX film "Arabia," as well as an exhibition of artwork and fashion by Saudi female artists. The conference had its fair share of female representation, as Dr. Lama Al- Sulaiman, Vice Chairman of the Jeddah Chamber of Commerce and Industry, expressed her satisfaction with the number of women involved in the conference. She also emphasised that the Kingdom has taken substantial steps toward involving women in the workplace and economic development as a whole.

Rita Athas, President of World Business Chicago, thanked Saudi Arabia for hosting the first US-Saudi Business Forum in one of America’s most important financial centres, Chicago. Athas stressed that Chicago is home to two of the world’s top Universities (University of Chicago and Northwestern University), the geographic centre of global derivatives trading, and a city full of financial and economic talent with over 50,000 traders in the city. Additionally, Chicago was named the Best Trading City by Trader Monthly magazine in 2007 and 2008. Chicago’s most vital resource is its educated population, with over 4 million employees and a gross regional product of almost $500 bln. Chicago is home to more than 400 corporate headquarters, and is home to the Chicago Mercantile Exchange and the Chicago Board of Trade.

Furthermore, Chicago is connected to the world with thousands of daily flights to over 200 cities. The city is also home to several major sports teams, including the Blackhawks, the city’s professional hockey team whose youth and talent has captivated North America as they compete in the National Hockey League playoffs.

The highly successful conference concluded with the Forum’s Chairman and the attendees calling the meeting a great accomplishment. Dr. John Sfakianakis, Chief Economist for Banque Saudi Fransi, commented that such a large attendance in the “heartland of America, is a very positive sign” regarding the future ties and relationship between Saudi Arabia and the United States. The relationships forged at the forum will help chart the future of the council and of U.S.-Saudi business development in the future.

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