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## The Impact of the Tensions in the Middle East on Global Markets

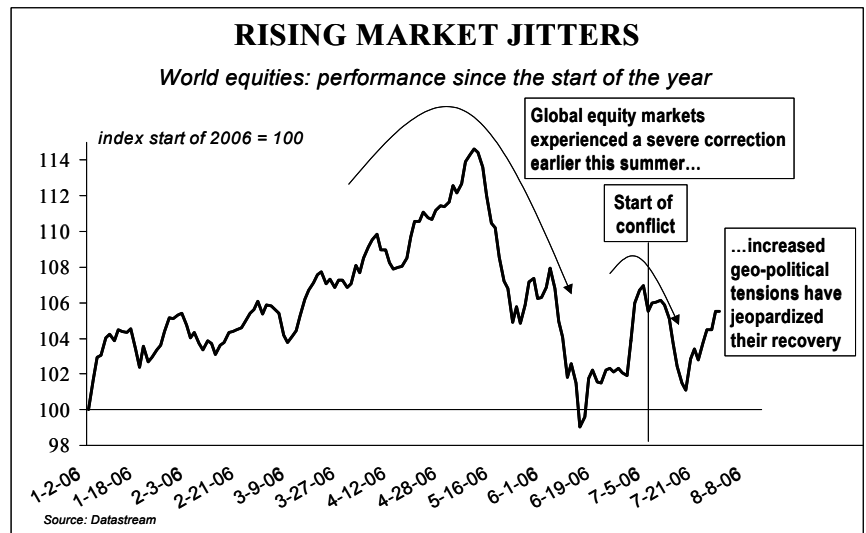
War is horrible anywhere and at any time. The human cost as a result of the current escalation of violence in the Middle East and the ongoing conflict between Israel and Hezbollah in Lebanon is incalculable.

The timing for war is never good, but the view of Vincent Lepine, vice president of research with the global asset allocation team at CIBC Asset Management is that the timing of this latest eruption could unsettle financial markets around the world.

"We have already had a severe correction in global equity markets earlier this summer and markets were just starting rebound from that," he says "This sequence of events happened to hit the markets at the exact moment when confidence was returning."

Potentially the most negative financial consequence is in the price of oil, Mr. Lepine says. When tensions between Israel and Hezbollah started escalating, the price of oil rapidly attained new highs, reaching more than US\$78 a barrel. This phenomenon is not new. Geopolitical uncertainty in the region is always accompanied by a premium in oil prices. This time oil prices were already very high and the end result is an oil shock that keeps growing.

"Given the intensity of the oil shock, an increasing number of countries have to borrow huge amounts of U.S. dollars in order to import the oil they need. This is translating into a sharp deterioration in trade balances," Mr. Lepine explains. "As the price of oil continues to increase, odds are rising significantly that the world will experience more localized financial crises, as we are already observing in Eastern Europe, especially Hungary."



Five years ago, he says, capital was essentially flowing out of the industrialized world and into Asia. While America was stuck with a ballooning trade deficit, Asian countries were always there to finance it. However, as the price of oil soared, money began massively flowing out of non-oil producing countries to oil-producing ones. "In short, global imbalances are building" he suggests.

Currently, the asset mix team at CIBC Asset Management is forecasting stabilization in the price of oil over the coming year. "If there is no stabilization, the odds are strong that you will see more geopolitical tensions and financial crisis in many countries. The end result is that markets, including equities, fixed income and currency, will be a lot more volatile," he says.

Though neither Israel nor Lebanon is an oil-producing country, Vincent Lepine says, "any moment that you get these kind of episodes, you are tipping the scale a little more towards increased market turbulence."

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