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## Professionals' View August 2011

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### IT WON'T GO AWAY?

If there's one thing that is becoming abundantly clear it is this ; policy makers and politicians in Europe, the UK and the US may talk, meet, discuss, wrangle, agree, disagree, agree to disagree, convene, consult and posture all they like, but the underlying problem – the mountainous debt crisis - WON'T GO AWAY. Tommy Tiernan, the Irish comedian, described the size of the problem perhaps the most accurately. We all know that Greece, Portugal, Ireland, Spain and Italy all owe amounts ranging from billions to gazillions. The UK owes a bit more, probably somewhere in the squidillions range. But the US? The US debt isn't even a number. It's an aaaaaagh type of noise. And IT WON'T GO AWAY.

The recent death of Amy Winehouse sadly reminded everyone of the dangers of addiction and the failure to deal with such. Help can be offered, but ultimately it is down to the individual to accept initially that there is a problem, and then accept that help in order to try to treat the problem. And the help is not always pleasant. In fact, it is usually deeply unpleasant and requires an enormous amount of self discipline and will power to stick with it otherwise the old problems keep resurfacing. And, in the end, if they're not permanently dealt with, something very nasty indeed happens.

The "Developed Economies" have an addiction – to debt. It is what our lives are based around. If you think of most of the things that we take for granted – healthcare, roads, rubbish collections, schools, the armed forces, the emergency services, state pensions (the list goes on) – most of it is not provided through tax revenue but by ever-increasing borrowing. Or at least, it has been. Greece is a classic case of a society

not getting to grips with the reality that money isn't magically plucked from thin air. And reality is painful when you are forced to face it. The Greek junky has just had its dealer taken away and it appears that the dealer's client list was a lot longer than anticipated.

The cure, though, is a long, long process and the patient will have many opportunities to fall off the wagon. If we look at the recent fixes that have been proposed, we see a recurring problem. Democracy.

### Is Democracy Helpful?

We take it for granted that democracy is a right worth fighting for. And of course it is. But.....wouldn't it be a lot easier to solve the debt crisis if the victims were not the largest democracies on the planet? The Europeans got together towards the end of July and astonishingly reached agreement under the leadership of Angela Merkel (German Chancellor amusingly referred to by Artemis Asset Managers as the Dominatrix of Debt) so that all 17 member states spoke as one. However, a recent description of Europe resembling a centipede hurdling is an accurate one. In fact, let's change the analogy to a slug pole vaulting, because the highest obstacle is yet to be encountered – namely the European electorate.

It's all very well for the European leaders to come up with a deal that allows Greece to effectively default on its debt (OK, let's not call it a default but a lowering of repayment interest rate and an extended period in which to make those repayments; it sounds better) which realistically has to be offered to Portugal and Ireland too, plus the core factor of the creation of the European Financial Stability Facility (EFSF), effectively a sovereign cash point facility that banks and

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other strugglers such as Spain and Italy can turn to in times of need, but who funds it all? Germany have just about finished absorbing the costs of reunification, and very successfully too. Their economy is flourishing. Will the German people have the stomach to now see their taxes supporting the profligate European states that don't display the same discipline and ethic as they do?

### The Mad Hatter's Tea Party:

Then there's the small matter of the US, which is the very epitome of democracy. The very fact that some of their politicians are calling for a default on their debt shows just how insular they can be. The Tea Party there is not a very welcoming one to outsiders and the world plays Dormouse as the Republican and Democrat adversaries play chicken with the global economy. Tom Stevenson of Fidelity quotes Winston Churchill; "America will always do the right thing, but only after exhausting all the other options." Let's hope he's right.

But the stand-off is driven by the need to be elected, or re-elected, every so often. The same applies in Europe and the UK. Solving the debt crisis is necessarily a long term problem. Our children will be feeling the effects. But democracies don't allow for long term decisions to be made, particularly those that are deeply unpopular.

### Stepping Outside The Echo Chamber:

Liam Halligan makes the point in the Sunday Telegraph that "if you really want to see clearly, to understand what is going on in the US, UK and the Eurozone, then you need to escape the echo chamber of Western self-justification and give credence to – or at the very least, not to instantly discredit – the reasoned analysis of those looking on from

afar." The Western economies are like an addict that won't acknowledge its problem. They don't seem to realise that the economic see-saw has tipped. China is the biggest debtor to the States. If they asked for their money back, or refused to lend any more in the event that the US became an unreliable borrower, the "developed" world would soon realise who is pulling the strings. The "emerging" world has emerged, if not fully then at least significantly. For the European Trade Commissioner Karel De Gucht to arrogantly recognise that "if China wants to engage in our sovereign debt market, they're more than welcome" is akin to shruggingly offering the fire brigade the chance to raise their ladders to the top floor of a burning building to allow us to escape down them.

"It's no use throwing dollars out of a helicopter," says the Brazilian finance minister. "Quantitative Easing amounts to economic hooliganism," says Russian Prime Minister Vladimir Putin. "People are investing in assets with no idea of the risks that they're taking", said Zhu Min in 2007, now an IMF special adviser. But what do these chaps know? They can't really be expected to understand how we "developed" economies work so successfully can they? And besides, they probably haven't even been voted in by their people like "civilised" societies would do. Now, where's the "on" switch for the printing press? We seem to be running low on cash again.

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