

## Moussaka in Drachmas?

Will the Greeks opt out of the Euro and go back to the Drachma? Well probably not after the agreement of support from the European Union and the International Monetary Fund in late March. What is / was this crisis about, and does it matter for the UK investor?

It certainly is important for all those countries within the Euro zone as it affects the value of the Euro and more importantly its very existence. The crisis arose because the Greek Government borrowed too much money and then spent it, and now later this year has to arrange further loans to replace it. It looked like nobody was prepared to lend them the money unless they had some type of guarantor and this is something that the agreement hatched out in Brussels has attempted to do. The package however includes more direct monitoring of the Budgets of all EU countries. At this stage it is not certain that this will be enough to work, and with the Greeks facing stringent cuts in their standard of living, the problems are far from over.

The crisis does bring to the fore the basic dichotomy of this single currency amongst different nations, because inherent in this is a common interest rate which may at any one time be entirely appropriate for one of the countries but may be counter productive for another, perhaps controlling inflation in one whilst exacerbating unemployment in another at the same time. In addition a falling currency value can help a country in financial difficulties as it makes its prices lower when selling goods or services abroad. Those in the Euro don't have that available to them. The advantages of the simplicity and economic efficiency of one common currency may however more than make up for these disadvantages. The jury is still out on that, but there is so much political will for the Euro to survive that it probably shall do, but not with the same certainty that there was a few years ago.

The health of the Euro is important for the UK, and it is not just the cost of a foreign holiday because Europe is our biggest trading partner and the health of their economies is important to us, and of course investors in European funds are directly affected by the value of the Euro.

This brings me on to the problems of debt throughout Europe and especially the UK. The debt is substantial and will mean lower growth in European countries because of the need to reduce it. The dream way to bring it down is to achieve massive growth in the economy so higher receipts from taxes are achieved which then can pay off that debt. However the present Chancellor's expectations of growth of 3.5% in 2011 seem hopelessly optimistic to most commentators. "The Economist" (27.03.10) projects 2.1% which is nearer the average long term rate. Thus the only other two methods of reducing debt are higher taxes and/or reductions in public spending. For the UK this is probably not quite what the poor Greeks will have to go through, but not far off it over a longer time period.

Before my next Newsletter there will have been at least one new Government. Will the election result affect the markets? Whoever wins faces the same problems and will have to act and this is what the markets expect. Probably even a hung Parliament won't have much effect.

## Now for the good news

Many parts of the world are unaffected by this overhang of debt and are continuing to grow healthily providing sales opportunities for UK and international companies. Many companies have slashed their costs over the last two years and now look well on the way to achieving increased profits. Dividends which have been reduced or in some cases missed out are likely to be increased or reinstated. This applies to many UK domestic companies as well as overseas traders. The current yield on many of these is well above the yield on UK Treasuries, never mind the poor deposit rates.

There are a few international equity funds specialising in this area and one is the Newton Global Higher Income Fund. It has a current dividend income of 4.57% compared to UK Government Bonds' 10 year yield of 3.94%. This fund has also increased its income every year since inception. Whilst not being specifically targeted at capital growth, any investment which increases its income every year will over time also achieve capital growth. This seems a good opportunity at this time, but as always should only ever form part of a diversified portfolio.

## Ravings

The present tax system could be described as bonkers. At some stages of income, the marginal rate of tax goes from 40% to 60%, back down to 40%, and then to 50%. If National Insurance were included, and employer's as well, there is a point where the marginal rate is just under 74%, and then goes down again. Taxation should be understandable and just and certainly should not dampen incentive at any level of income. What is just, is a subjective decision; the other two are not.

Yours sincerely

**Andrew Roberts**

*Notes:*

*Prices at 01.04.10.*