Roger Nightingale 5 March 2010

Pointon York SIPPsolutions

Economics is Noughts and Crosses, not Chess. Only highly qualified experts can misunderstand it.

Europe has lots of experts. They've emasculated their economy, but seem not to have noticed!

Does the ECB appreciate the mess it's in?

"It's absurd," said Jean-Claude Trichet last week "to suggest that Greece might leave the euro bloc." Politically, perhaps, he's right; but, economically, wrong. It's more absurd that Greece should contemplate staying.

Probably not. Hubris hides a lot.

What we are witnessing is a tussle between immovable political will and irresistible economics logic. Which will win? The latter, of course; it always does. The only uncertainty is the timing. We don't know how long the inevitable can be delayed. Nor how much damage to the country's living standards will be inflicted in the meantime.

Trichet, like Napoleon at Waterloo, seems to be prepared . . .

It looks, though, as if it'll be a long haul. Officials at the ECB and Commission regard it as a matter almost of honour that the integrity of the bloc be preserved. Last week, they did their best to raise the financial markets' perceptions of Greece's viability. Indeed, they scored a minor victory. A sizeable bond issue from the Athens authorities was well received by investors. Interest rate differentials (Greece versus Germany) declined quite significantly.

. . . to spill a lot of other people's blood to prove himself wrong.

It's one thing, though, to avert immediate crisis; quite another to resolve chronic debility. What's required for the latter is that the Greek economy be returned to vitality. There is, admittedly, an obvious correlation between fiscal deficits and GDP growth rates, but the causality goes from second to first. Take Japan as an example. Its huge borrowings are the *consequence*, not the *cause*, of the loss of its economy's momentum. If reasonably brisk rates of growth could be re-established, its deficit would disappear in a flash.

Greece is to be the sacrificial lamb.

It's much the same in Greece's case. The problem is not one of debt but of uncompetitiveness. To deal with the second is automatically to deal with the first. Sadly, Europeans don't see things this way. They reckon the causality operates in the other direction, and act accordingly. When Trichet and Barroso review Europe's performance in the last ten years, they seem to feel no shame. It hasn't occurred to them that their policies have spawned the region's scleroticism; that the institutions they represent aren't the solution, but the problem.

People get the Governments they deserve, of course.

Have they noticed what's been happening in the States, for instance? There, the focus has been on growth. The currency was devalued, labour was shed, and taxation cut rather than raised. No great surprise that activity responded. While GDP in Europe stalled in the closing months of 2009, in America it accelerated. The difference will be reflected in tax collections. There'll be a dearth in the one, lifting the deficit; a surge in the other, lowering it.

We, in Britain, must have been very remiss, therefore.

Where does Britain fit? Closer probably to European dogma than American empiricism. The currency may have been weakened, but there is no predilection for cutting taxes. None either for cutting public sector waste. Brown's team still argues it was right to take money from the good guys and give it to the bankers. And, worse still, Cameron's boys agree. Not for some considerable time, therefore, will sensible policies be implemented. It's unlikely the forthcoming election will change anything: the alternates being almost as bad as the incumbents.

On the general economics front, all is not well.

Elsewhere in the world, there is a degree of anxiety about the strength of the economics recovery. Fifteen months or more after the cyclical low point, the stimulus having been unprecedented, it would have been reasonable to expect rates of progress to be brisk. In general, they haven't been. The inevitable conclusion is that there are powerful forces of deflation still at work. If so, there is a risk, eighteen months hence, when the cycle is due to turn down, that another severe setback will occur.

Equities are set to rise, though.

The good news in the interim, though there's not much of it, is that securities' valuations will perform reasonably well. Money will be easy, interest rates low, inflation negligible and profits moderately strong. A 15% advance in the indices is justified; it might be larger.

Especially after the public sector axe starts to do its work.

Progress will certainly be rapid on each of these fronts once public sector spending employment starts to be cut. There are huge savings to be made; potentially huge benefits to be accorded to the living standards of the rest of society. All that's needed is a perceptive Government. Ah, there's the rub!

Contact us . . . For further information about Pointon York's SIPP products and services, call Natalie Oliver on 01858 419 371 or visit the corporate website at www.sippsolutions.com. Alternatively, contact Roger Nightingale, by telephone, on 01858 419 300; by e-mail at rnightingale@sippsolutions.com, or browse his web site at www.rogernightingale.com.