

Economic Views for Investors

by Roger Nightingale

4th December 2009

Lies and errors are like cucumbers: they repeat.

It's not usually possible to tell just one lie, nor to make just one policy mistake. An initial transgression almost always demands a subsequent corroboration. In the process, the first offender is transformed into the seasoned recidivist. Politicians, caring more about the now than the then, are particularly susceptible to the syndrome.

Iraq provides a classic example of the phenomenon.

Blair demonstrates it. His early exaggerations in the run-up to the invasion of Iraq later became blatant falsehoods. And the tangled web he wove proved to be, not a vindication of his actions, but a condemnation of them.

British banking may provide another.

It may be much the same for Brown. His decision to bailout hapless Scottish bankers was a mistake from which he'll probably not be able to extract himself. Each subsequent twist in the financial crisis, each requiring a further misallocation of resources, has only underlined his original misjudgement.

Are the RBS boys brave or stupid or both?

Last week, there was a new deterioration: the directors of RBS said they'd resign if they weren't allowed to pay themselves colossal bonuses. It was an obvious tactic: they knew that, doing so, they'd undermine the resale value of the bank. Taxpayers would have to bear the loss. And they'd blame, quite rightly, the politicians who'd caused the problem in the first place.

A spell on the dole would be good for their souls.

The solution, as with all blackmail, is openness. What Brown must do is call the miscreants' bluff: he shouldn't let them resign; he should sack them. Will he be brave? Of course not. That would require him to admit that his initial decision was mistaken; something he'll never do.

Brown has not thought things through.

Instead, he'll compromise. The bonuses will be paid, but they'll be slightly less generous than originally proposed: he'll settle for the outrageous in place of the unconscionable. Will that play well with the electorate? Will the unemployed factory worker or the redundant retailer feel justice has been done? Will the DC pensioner, plunged into hopeless penury, appreciatively applaud the judgment of the Prime Minister? Probably not.

Nor has Cameron.

Would the Tories have been any better? Sadly, no. From the first, they thought it right to sacrifice the rest of the economy on the altar of the bankers. One Grandee, a former Chancellor, opined at the close of 2007 that, "saving the banks would save the economy"! The view hasn't changed much since then.

The RBS board has as much talent . . .

Last week, the talk was all about banking expertise. Bonuses had to be paid, it was said, to prevent talent migrating elsewhere. Really? What talent? That which caused excessive lending to property developers? Or that which misconstrued financial derivatives? Or perhaps it was that which led to failed fund management?

. . . as the Scottish football team

The truth is that there is a lot of talent in the City, but that very little of it is to be found in banks. Indeed, the world would be safer, Britain's economy stronger, if the Scottish banks (and their loathsome directors) had been put out of their misery. Schumpeter's principles should have been applied: the "bad" had to be allowed to fail if the "good" were to be able to succeed. Woolworths and British Leyland were demonstrably not up to scratch; RBS and HBOS similarly. Is it too late to reverse policy? No, even now, something might be saved if politicians and regulators undertook an honest analysis of the situation. But don't hold your breath.

What happening to economics data?

Meanwhile, on the broader economics front, many data items have been puzzling. German unemployment, for instance, was reported to have fallen last month! Why? Was activity surging or productivity plunging? Nobody seems to know.

The numbers don't add up.

And can activity in China and India be as strong as the numbers indicate when imports are so anaemic? The latter seem to be corroborated by other countries exports; the former by commodity prices. But there's a statistical black hole somewhere.

The States and Japan are probably drifting sideways, though.

What is not to be doubted is that the world's two biggest economies are dull. Activity in both the US and Japan is lacklustre. Wages are being squeezed and spending is being cut back. There is no immediate disaster, but no imminent redemption either.

But stock valuations are climbing, albeit slowly.

Happily, company results are continuing to surprise on the upside and inflation on the downside. It's a favourable background to securities valuations. The indices will advance for a while longer.

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