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At long last we are witnessing growing confidence suggesting that the worst might be over!

The American economy still is the power plant that drives global growth, and the signs are now much more positive and point to a sustainable recovery. Consumer spending, so important for the US economy, has seen a very welcome resurgence. With personal debt back to more normal levels, the Americans this year are spending roughly twice as much as they did last year. Unemployment is down, despite the fact that Washington continues its policy of reducing job numbers in state and local government. Even the property market seems to have recovered, with foreclosures in the first quarter down some 25% when compared with last year's Q1, and house prices are rising.

Of course, there are regional variances when it comes to employment and house price figures, as is evidenced by Detroit filing for bankruptcy earlier today. For decades, it had been the hub of the American automotive industry, but the "Motor City" has seen a reversal of fortunes in recent times. General Motors, who in the 1950s was the world's largest company, filed for bankruptcy only four years ago; it has since re-emerged following a state assisted "pre-pack" reorganisation. Detroit's population has shrunk by some 60% and 80,000 properties have been abandoned. It just proves that even the biggest concerns – be they firms or municipal authorities – are not immune to calamitous downturns.

In fact, US corporations are still reluctant to invest heavily, preferring to continue bolstering their balance sheets despite the fact that many are sitting on huge cash piles, but corporate profits are quite strong. Corporate capital expenditure – companies' investment in property, plant and machinery – serves as an important gauge for where the economy is heading. Over the last decade, we have only had one year when it contracted, and that was in 2009, immediately after the Lehman Brothers bankruptcy and the ensuing banking crisis. However, the latest indications are that it might well shrink again this year, and worse is predicted for 2014. China has seen a sharp reduction in this area, and Latin America is doing even less.

The American economy registered growth of 1.8% in the first quarter of 2013, which is rather disappointing, particularly as earlier announcements had us believe that GDP growth for the period was 2.4%. However, we don't think 1.8% is too bad bearing in mind the austerity measures are now biting, coupled with the drastic cuts in public expenditure. It also follows a dismal 0.4% growth in Q4 of last year. One could argue that US GDP growth would be considerably higher if it were not for the austerity package. On the other hand, the enormous twin deficits, i.e. the deficits in the budget and the trade balance, needed to be addressed.

The current account (the international trade balance) deficit has improved quite a bit, as it has shrunk by $22 billion (2013 Q1 vs. 2012 Q1). A lot of it is down to globalisation – years of investing and setting up shop in other countries. We are witnessing a subtle shift in who America trades with: traditionally, Europe and Japan were the biggest trading partners, but they now amount to only 25% of US exports. America's NAFTA (North American Free Trade Agreement) partners Canada and Mexico now account for 32% of exports, followed by 13% to Asia (ex-Japan), 12% to the rest of Latin America and 7% to China.

President Obama has now set his sights on building two other major trade agreements, one with ten Pacific Rim countries and one with the EU. The latter is interesting, and talks have been going on since 2010. Early indications are that the UK and Germany quite like the idea, but the French are rather less enamoured with it. A potential stumbling block is the fact that the EU does not like anything that has been genetically modified – be that crops or cattle – whereas the US wholeheartedly embraced the technology.

It is not only America that displays growing business confidence. Britain also is seeing some encouraging signs that things are improving. Even the IMF, whose chief economist recently criticised George Osborne for sticking to his "A" plan, has seen fit to lift its UK growth forecast for this year from 0.7% to 0.9%. Many commentators consider that figure to be too pessimistic, suggesting the growth rate will be somewhere between 1% and 2%.

So far this year, output from the UK's industrial sector has crept up a tiny bit month after month, but the narrower measure for manufacturing output is still shrinking, albeit at a slower rate. Effectively, it is the service sector that is responsible for overall GDP growth. It would be nice to see the industrial sector assume a more dominant role, but that may prove to be wishful thinking for the time being and, quite possibly, for the longer term as well.

Surprisingly, consumer spending is up, despite the continuing fall in real wages. It suggests that we are once more reasonably relaxed about spending money, and it comes at the expense of household savings which have fallen back to near pre-financial crisis levels. Maybe people are just getting a little fed up with the ongoing austerity that is endlessly talked about by politicians and dwelt on by the media. Maybe it is the perception that the rest of the EU is doing even worse: Germany's GDP growth now is flatlining, France is on a downward trend and Italy is suffering even more. The poorer, peripheral countries of the EU, of course, are in a real mess.

Indeed, the IMF predicts a contraction of 0.6% this year for the eurozone as a whole, and even Germany, the powerhouse of the eurozone, is expected to grow by only 0.3%. That makes for an interesting background to Germany's federal elections in two months' time. It is by no means certain that Chancellor Merkel's present centre-right coalition will win a new majority. She could well be in the unenviable position of having to consider a coalition with either the Social Democrats or even the Greens. Indeed, those two parties have publicly stated that they would like to form their own coalition if the electorate wanted a change.

The election in Germany is important because it is Germany that is in the driving seat when it comes to the eurozone and its single currency. Mrs. Merkel has been pursuing a policy of doing just enough to avoid the eurozone disintegrating, but that course of action, bizarrely, makes the overall situation worse. Essentially, the eurozone now consists of creditors and debtors, and a diktat from the core creditors to the periphery debtors insisting that further austerity measures be introduced and maintained condemn these poorer countries to prolonged and deepening recessions whilst further increasing their debt burdens. This will lead to more social unrest in the negatively affected countries where the situation already is at near-breaking point.

Sadly, politicians are the worst people to be in charge of this situation, given their short-term outlook and their need to pander to the electorate. Euro bureaucrats are little different in that respect. Both rarely are proactive, instead only responding to a crisis and doing just enough to calm the financial markets. Remember ECB President Mario Draghi saying he would do "whatever it takes" to protect the euro? The moment that crisis was overcome, Germany started to conveniently forget some of the promises made.

The problems won't go away - they will resurface time and time again. Indeed, right now we have another crisis flash point in the case of Portugal where the 10-year bond yield has soared to around 8% following the government's request to defer the review of the EU-IMF Troika bailout which in turn sparked a constitutional crisis, raising the prospect of an early general election.

Elsewhere, Greece still remains a problem. A leaked European Commission report states that Greece will miss its austerity targets by a wide margin and goes on to say that the country was unwilling and incapable of collecting taxes! Standard & Poor's have downgraded Italy to near-junk BBB status and Spain's ruling party and Prime Minister Rajoy are embroiled in a massive slush-fund scandal which led to *El Mundo* writing about the country being in "pre-revolutionary" mood.

It is no good to simply point the finger at the financial crisis of 2008 and blame the bankers for this malaise. As we have often stated in our Newsletters, the Maastricht Treaty's convergence criteria were over-ambitious – they since have become a Utopian dream. The process of trying to achieve this convergence, however, has led to the "great divide" in the European Union. Just look at the unemployment figures: in Greece and Spain they stand at a scary 28%, whilst Germany's look pretty healthy at 5%. In terms of employment – or lack of it! – it is the young people in the periphery nations who are facing real hardship: youth jobless figures (16 to 24 year old) now stand at 60% in Greece, 56% in Spain, 42% in Portugal and 39% in Italy.

The eurozone situation is untenable and it is only a matter of time before it will unravel. The worst outcome would be a disorderly exit from the euro by one or more member states, which would have a serious and, dependent on which countries were to leave, possibly catastrophic effect on financial markets everywhere.

Could the eurozone in its present form be saved? There has been talk about replacing the individual sovereign bonds with new "Super Eurobonds", which is an interesting theory as it would not only remove the yield differences that plague the poorer countries, but it would also help their economic recovery. The so called Fiscal Pact, signed in March last year by all European Union member states with the exception of the Czech Republic and the UK, would have to be strictly adhered to, and other monetary stimuli would be necessary, but it would greatly help periphery nations regain some of their lost competitiveness. Of course, such a move would effectively have to be underwritten by Germany. Mrs. Merkel so far has been adamantly opposed to it, and she certainly is not going to change her mind with an election looming. After the election, however, we might see a change in German attitude. Yes, Germany would have to pay more for its own borrowing, but over the longer term a recovery in the depressed eurozone economies may pay handsome dividends.

Stock markets since January 1 have been "interesting" to observe and have registered very different results. Japan has been the star performer, with the Nikkei 225 up over 40%, no doubt due to Prime Minister Abe's new policy by making the Bank of Japan open the Quantitative Easing floodgates. At the other extreme, BRIC countries (Brazil, Russia, India and China) are down by a collective 8.3%, and Hong Kong's Hang Seng shows a negative 5.7%. The DJ Eurostoxx 50 has gone nowhere, but elsewhere things are looking better: the Dow Jones and S&P 500 are up around 18%, and the FTSE managed 11.5%. Bonds and gilts are slightly negative, following an outflow when Federal Reserve chairman Bernanke stated that he may scale down QE earlier than previously thought. Bernanke's statement also did no favours to the gold price, having already fallen from $1,664 per ounce on January 1. It crashed to nearly $1,200 before recovering a little to around $1,300. The second quarter alone saw a fall of nearly 25%! As $1,200 per ounce is widely considered to be the product cost price floor, we may well have seen the worst of the correction, particularly as Russia, Kazakhstan and Turkey recently have added some 28 tons to their gold reserves, according to IMF data.

As far as the outlook for financial markets is concerned, much will depend on whether America's economic recovery really is sustainable.

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Lacomp plc
77 High Street, Bagshot, Surrey, GU19 5AH, England.
Tel: (Intl. +44) (0)1276 475123 Fax: (0)1276 475273 e-mail: info@lacomp.co.uk website: www.lacomp.co.uk & www.lacompeisfunds.co.uk
Registered in England No. 1851201
Authorised and Regulated by The Financial Services Authority (FSA)