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Offshore Holdings Advisory March 2009 Newsletter
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Market and Currency Update – 1st March 2009
(A personal view by R.B. Skepper)
(for professional investors and business men/women only)

FTSE100: 3684 – 2nd March 2009
4231 – 1st February 2009
Change: -13%

There are only two things without limits according to Goudrief, the mystic philosopher: "Man's stupidity and the Mercy of God".

We have certainly suffered an unduly large portion of the former, and we are unlikely to earn the latter until human counsels show considerably greater wisdom.

As markets crumble again there is a tendency to remain pessimistic, but there are considerable grounds for hope as leaders everywhere, almost without exception are showing considerable skill and vigour to put humpty dumpty back together again. This is remarkable, considering the diversity of cultures that are largely acting in unison.

Whilst there are differences in the minutiae of what is the best precise package of measures for each economy, all the major economic powers are in broad harmony on the macro thrust of what to do.

Everywhere the necessity to keep credit flowing in the real economy has been recognised. To prevent any further contraction in the money supply, if necessary by quantitative easing, is now virtually agreed by all.

Different countries may be supporting their banking systems in different ways, but the aim is agreed and is unanimous - to prevent a further contraction in the money supply. That was what turned the recession of 1929/1930 into the depression of 1933.

Equally, though there is bound to be some political posturing over local jobs, every one of the major economies is agreed over the need to avoid a rise in general protectionism. Politicians will of course look to their own constituencies and there will of course be some cheating at the margin, but no general tariff obstructions as happened in the Thirties.

It is tempting and easy to criticise these efforts, and make mischief by highlighting minor divisions. It would be extraordinary if there were not many, as everybody has their own ideas of how best to navigate the uncharted waters. But they are no longer that uncharted. The scale of the problem is now becoming much clearer, and the massive measures already taken were correct as the size of the problem unfolds.

Actually we have more enemies within the capitalist tent than without these days. Politically, with the collapse of Communism and its command economy philosophy, there is no philosophical rival to "free markets" internationally.

But in the U.K. the malcontents, who have never come to terms with that collapse and continue to resent the unequal prosperity of free markets, seem to have found a kindred asylum within the BBC. These are clever people who know how to manipulate information, and slant emphasis, to maximise all of the adverse news. Some of the economic commentary has been quite vicious in its innuendos, falling into the category of shouting "FIRE" in an overcrowded assembly.

The Director General appears to be a "drip wrapped up in a politically correct wet blanket" so it goes on and on. Carol Thatcher, the symbol of free markets, is openly vilified and dumped, whilst Jonathon Ross bounces back from much nastier, not even innuendos.

There are of course socialist voices trying to reintroduce control from the top - the man in Whitehall knows best. This will hopefully be strongly resisted, as we know from experience he never does. Mandelson knows it, and his appointment looks more sensible by the day. If Harman had any economic power, what few green shoots that did appear would be immediately suffocated by interference.

Brown of course is widely blamed now for the mess to which he undoubtedly contributed - but he is respected internationally for a powerful financial mind, even if he has misused it domestically. His efforts to synchronise a world wide response to what is a not a U.K. sourced problem, but a world wide one, have been and continue to be positive.

It is sad for him that the massive transfer of resources out of the wealth producing sector in the U.K. into the public sector, has not produced the shining public services he presumably hoped for, and what many of our continental economies enjoy already. Instead we are landed with just a vastly more costly shambles. One wonders if the return of Mandelson means he sees it also. Too much to hope for, but there are only 12 months to go. One only hopes the Opposition realise what they have to do - and fast and vigorously.

Whilst attention has been focused on petty blunders like Fred the Shred's pension excesses, the general thrust of trying to get lending going and trying to support small businesses is the important part. The main impacts of his policies are now where they should be, albeit anything done by government travels slowly through an obstacle course of bureaucracy.

Much criticism has centred on the aspect that a crisis caused by excessive debt is not going to be solved by yet more debt. This misses the point. Whilst correct in the long term it is naive in the short term, as the current liquidity creation is merely replacing chunks of liquidity frozen in the banking system.

Clearly savings have got to rise, in particular in the Anglo Saxon economies. By contrast they have to fall somewhat in the over-saving Far Eastern economies and Germany for that matter.

What is encouraging is the almost unanimous decisions of the leaders of the Far Eastern nations to use their large reserves aggressively to pump up demand and counteract the inevitable extra saving tendency of ordinary citizens of these countries, where there is no social safety net.

The credit splurge of the last 5 years has landed the Western economies in their biggest potential recession since the war. The problem is large, but the coordinated actions of the world free market leaders are large too and highly positive. Keynes saw the need to emphasise the positive, since, as he said: “Without spontaneous optimism economic activity does not revive”.

STERLING:
It is easy to get carried away with one’s convictions - but nobody is right for long about the future - particularly where currencies are concerned.

Having made a strong case for why Sterling would have to fall against other currencies, the scale of the fall - about 30% - probably over-discounts the extent of the U.K.’s specific problems on the short view.
Even in a sharp world downturn, it is strongly stimulative and helpful to the U.K. economy. Effectively we are stealing the trade advantage by a competitive devaluation, and of course it is not popular with our EURO partners.

Already there are clear signs of its positive effect: Occupancy of Millennium and Copthorne Hotels in New York were off 40% in January, Beijing and Hong Kong were off 20% and London a mere 4%. London is currently the most busy retail centre of any European city.

There is a near explosion of domestic bookings for the coming holiday season. Upwards of ¾ million may take their holidays in the U.K. instead of on the (now) Costa TooMucha. That represents several billion of spending in U.K. pubs, hotels, holiday lets etc: and local shops.

Whilst U.K. manufacturers are currently claiming a 12% fall in orders, when restocking returns (and the falling off a cliff of orders in the last quarter would have been primarily due to heavy destocking), British based companies are now likely to get an above average share of orders going. It also helps the property collateral of the U.K. banks and building societies.

Property here in hard currency terms is already down 50%. It won't fall so far in Sterling terms, in which covenants and collateral are measured. By mid year the U.K. could be looking relatively more resilient than most other economies, and this could lead to quite a sharp upward recovery in Sterling - say to $1.6 and Euro 1.25.

Should this occur, one would have to clearly think again - in the absence of any serious effort to address the now hopeless imbalance between public sector costs and the private sector's ability to meet that swollen bill - a bridge too far thanks to the Labour years in power.

R.B. Skepper
3rd March 2009
Brewin Dolphin Securities

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