TAM INTERNATIONAL INVESTMENT NOTE

Stick to your principles

"We have to fight for principles. We could maybe set them aside in the short term. But in the medium and long term, we will suffer damage that way." Angela Merkel, 29th June 2015

"Those are my principles, and if you don't like them…well, I have others." Attributed to Groucho Marks in 1983

Chucking the rule book out with any or all principles in the short term is not unfamiliar behaviour in the EU and maybe that's why we all expected a deal by now. Perhaps this was a tad too optimistic because it's been a busy start to the week in the wake of the breakdown of talks between Greece and its creditors at the weekend when an eleventh hour deal was expected.

It now seems that Greek Prime Minister, Alexis Tsipras, may have jumped the gun by walking out when he did due to his objection that the package on offer from the Troika did not include any debt relief, without which Greece cannot meet its payments. This is something that Mr. Tsipras believes would be impossible to get through his fragmented and agitated parliament. Unfortunately, he seems to have walked out before playing to the rules of the game the EU had in mind.

Jean Claude Juncker, President of the European Commission, said that he felt "betrayed" by Mr. Tsipras and that, if only he had accepted the austerity measures in principle, the final offer from the EU, including debt relief and growth measures, was about to be sprung. That offer has now been withdrawn. Instead, Mr. Tsipras opted for a snap referendum on Sunday 5th July. The exact wording has yet to be seen but, from a Greek perspective, the question is essentially "Do you want to accept the EU offer?". The EU were rather it was "Do you want to stay in the eurozone?". Incidentally, there is some speculation as to how Greece will print 16 million ballot papers and 8 million envelopes by that time, let alone ship in all the necessary election officials.

It's all a bit shabby and nobody comes out of this looking particularly good. We note this morning Mr. Junker's comment "If they vote No, it would be disastrous for the future. No would mean they are saying no to Europe". Bad for whose future, he doesn't say. And when he says "Europe" we think he means "eurozone". Still, when you're trying to convince a confused electorate to vote a certain way on a non-existent deal which has already been withdrawn, maybe anything goes.

Meanwhile, global stock markets have fallen a few percent and there has been the familiar rush to perceived safe haven of government bonds. The calling of a Greek referendum this coming Sunday is fraught with uncertainty, which investors hate, and so we expect the market to remain pretty jumpy for the rest of the week. However, the stock market falls that we have seen are far from the panic of previous chapters in the never ending Greek saga.

There are a number of reasons for this. Firstly, the private sector is far less exposed to Greek debt than it was in Q3 2011, which was a very difficult time for everyone worried about economic contagion from an exploding situation which had no precedent. The risks are now far better understood and quantifiable.

Secondly, the state of the global economy, and Europe in particular, is in much better shape today than it was then. The US economy, the first out of the mire of the post Lehman crisis in 2008, has recovered so well that, until last week, everyone was more concerned about the Federal Reserve raising interest rates in order to not get caught behind a curve of rising inflation. The UK economy is ticking along nicely, and we were sufficiently confident in Europe to invest TAM client portfolios late last year; an investment that has worked very well for those eurozone investments that were either currency hedged or even un-hedged given the euro posted its best quarterly gain against the dollar for almost four years underling the single currency's reliance in the face of the Greek crisis.

Thirdly, it is true that Greece, in the grand scheme of things is very small. It is just 1.8% of EU GDP, and 0.4% globally. The bailout sums themselves are not particularly large in absolute terms. The real risk here is political and it is longer term. If Greece left the Euro, it would set an uncomfortable precedent that the single currency is reversible. If you are of the opinion, as Nigel Lawson (ex-chancellor of the UK Exchequer) was, that adopting the Euro was allowing Federalism by the back door, then it is logical that if one can abandon the currency, then one can abandon the EU stated mission of "Ever closer union".

This well illustrated by the way that the USA expresses its incredulity that the EU won't just sort Greece out and be done with it. From the White House perspective, Greece is a geographical linchpin between Europe and the mounting problems around it; Russia, Balkans, Middle East and North Africa. For the sake of a few billion, why not just do it?

The EU has some justification, however, in their view that if you allow one member of the union to break all the rules and principles, then Greece leaves the Euro anyway and the door is open to everyone else who doesn't fancy a decade of austerity and 50% youth unemployment.

In our opinion, on balance, a Yes vote looks the most likely outcome but anything can happen. Even with a No vote, Greece does not necessarily leave the Euro. Furthermore, compared to the gains made in the TAM stock, bond and property investments, very little has changed even with these market falls. To our mind, we would be inclined to see any market turmoil this week as an opportunity to increase our exposure to equities. We see no reason why investors will not come out looking for higher yields in both stocks and bonds when the fundamental global economic backdrop remains positive. These are the principles we are sticking with.

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