

# JUSTIN'S COMMENTARY

Justin Urquhart Stewart is one of the most recognisable and trusted market commentators on television, radio and in the press. Originally trained as a lawyer he has observed the retail market industry for 30 years whilst in corporate banking and stockbroking, and has developed a unique understanding of the market's roles and benefits for the private investor.



## RISING ECONOMY, RATES & STERLING

So when should rates rise? Some would say that they already have if you look at some of the charges and fees you have to pay on certain facilities. However, the question remains when the Monetary Policy Committee should raise the Base Rate from this record low level.

Last week's encouraging growth figures would imply that action should likely be taken sooner rather than later. In fact such a move could be regarded as a badge of success and not necessarily the precursor of the next downturn.

Given the proximity of a general election (2015 is not too far ahead) it is obviously going to be a very sensitive subject. Now of course that decision is made by the independent MPC at the Bank of England, but you do have to wonder sometimes just how really independent they are. After all who selected the external members, approved the internal ones and, come to that, recruited the Governor? The paw prints of HM Treasury will be clearly seen by even the most amateur of Poirots.

Nonetheless as the economy improves, action will have to be taken. Firstly we are in a position of abnormally low rates and thus as the economy heals so we should be looking to try and return to a more normal level (although exactly what the 'new normal' is by no means very certain). Additionally, as many have warned, these incredibly low rates could be creating asset bubbles and distortions which if left too long could create far worse difficulties in the future.

Actually I think we should see rising rates as a good sign - it's a sign of recovery and although the popular papers will scream about the mortgage payments pain, we should also remember that there are far more oppressed depositors than borrowers. Perhaps we should recall that it was these savers who were the financially responsible ones. Sadly also these were often the older members of the population who now found themselves dependent upon a declining income off measly deposit returns. Those least likely to be taking more risks were being asked to do so at the worst times of their lives. They paid down their debts and saved for the future, and yet when the financial explosion came it was they who have borne the real brunt and pain of the fiasco. So even if it is a tiny 0.25% change then at least there might be some small respite.

Of course there will be pain for those who have big mortgages and have geared themselves up to the hilt. However, they have had plenty of warning to try and prepare for a period of higher interest payments. The recent media furore over the checks being given for mortgage applications is all part of this process, and if it prevents some people from overstretching themselves now, it will save them from a period of far greater pain later.

The other key concern that will be also on the minds of the decision makers both at the Treasury and the Bank of England will be the timing. Too soon and they could choke off the recovery, just as the USA suffered when they raised rates too early after the Depression in 1936. Too late and they run the risk of asset prices rising too fast in key areas, and even inflation starting to take hold.

This decision will be the Judgment of Solomon, and no-one can know with any certainty the outcome of such a change. However, despite the fear of the politicians, I wouldn't be at all surprised if the decision comes earlier than many had been previously considering.

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### **The Pound has been getting bigger**

Related to my points on interest rates is of course the value of the Pound. Sterling has been rising of late against both the Euro and the US\$, and while we have not come near the madness of \$2 to the £ of a few years ago, the current strength is having an impact.

Often there is a fear that we make ourselves uncompetitive, but we shouldn't be quite as fearful of this as we have been in the past. We are not generally a low cost mass manufacturer. That type of production has long gone overseas and will never in any likelihood return. No, the UK is a quality provider of products and services and thus can and should command a sensible if not premium price. I don't imagine that the Germans have ever felt the need to ensure that BMWs have to compete on price for the quality of what they build.

However, the stronger Pound does affect our overseas income. Although not as much as in previous decades, the UK's overseas investments have been a vital part of our economy and balance of payments. These have declined more recently but are not to be ignored.

In 2010 such dividend income for the UK from our overseas companies was around £56bn which is certainly not to be sneezed at. An estimate for this year has it at over £80bn which is obviously an encouraging increase. Then you must take into effect the cost of translating these income streams into the Pound and of course with being stronger, Johnny Foreigner's currency can't buy as many Pounds as before, which must have affected us. Well some figures have suggested that we could have lost as much as £3.5bn on the currency conversion.

Such an impact will affect investment houses, as they will have been factoring in these income streams, and quite a few companies who are denominated in US\$ will be finding it harder to keep their institutional investors satisfied if they are still expecting such sustainable returns.

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**And finally...**you may remember a week or so ago the news that there was a hijack scare on a Virgin Australia flight from Brisbane to the Indonesian holiday island of Bali.

It is now apparent that the passenger, Australian Matt Lockley, banged on what he thought was the toilet door for a last-minute bathroom break before the Boeing 737-800 aircraft landed.

The door was actually the cockpit door and the pilot, Neil Thomas Cooper, responded by alerting Indonesian traffic controllers of a possible hijacking. Crew members then seized Lockley and handcuffed him.

Virgin Australia said the 137 passengers and seven crew on board were never in any danger during the flight.

After taking blood samples from Lockley, police said the Australian had taken several painkillers, including four Panadol and two Voltaren pills. Lockley, who was travelling to visit his Indonesian wife, was shown on local television shortly after the flight landed, surrounded by armed security and a mob of reporters at the airport.

He has not made any public comments about the incident and remains in police custody.

Police said Lockley "was still depressed, so he needs to rest."

Yes and to try and remember that the pointy end of the plane is normally where the pilots are.

Have a good week.

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