

## **A question of timing**

There is a well-known cliché that Napoleon demanded not good generals, but lucky ones. Well, he would have liked the style of the euro so far. It was conceived in a world that was buttressed on all sides by a triumphant American dollar and a booming world economy, and even though Europe was relatively depressed, there was no major international turmoil to upset the gestation.

But as we move toward the birth of the new currency, things are getting a little unhinged.

That nice Mr Brown hasn't quite managed to abolish the economic cycle, and the City of London is starting to resemble some kind of financial Stalingrad with the toll of casualties rising daily.

This may not, now, be quite the best time for a new currency! Especially one with foundations which are not perhaps of quite the quality that the architect had ordered...

The next weeks and months may well ensure that the preparations which have been made in the financial markets are tested to the limit. Let us consider what is happening:

The euro is the currency of what will be the largest single currency economic grouping on Earth. It will be managed by a central bank which deliberately has no democratic mandate and thus can, single-mindedly, devote itself to its only job, the maintenance of value of the euro.

On the other hand, the US dollar is currently looking like the repository of an increasingly unpleasant set of financial booby traps which may yet take out some very major market participants. It may end up making getting into the US market or its currency something which the cautious investor may wish to avoid.

So we just may see the euro becoming a very desirable haven from the unravelling of the hedge funds and their underlying securities. But this will mean that the financial markets which sell and process euro denominated securities will be hit with quite a wave of activity and buying – after all, once you have disinvested from one set of securities, the 'under the bed in a suitcase option' is not usually the best.

This world is a bit of a funny place. Japan, for example, is a rich and successful financial disaster. Mrs Watanabe, the typical Japanese investor, has become wary of investing locally, and even seems to fear local banks will fail. However, she, like millions of her fellows has plenty of wealth seeking safety. She was never a real 'punter', but rather seeks a safe investment with a reasonable real return. Just now, as she sees Lenin's dream of the debauchment of the capitalist's currencies become reality, will she think that the suitcase – or the safety deposit box – looks less bad than LTCM's clients?

So what will Mrs Watanabe, our rational, sensible, high-risk averse investor go? The USA? Home of LTCM, inventor of the triple-X junk bond? Or Europe, where the central bank has just one job, the preservation of value of the currency?

Already we have seen reported in the press the fact that a large ECU denominated issue for the Kingdom of Denmark was snapped up in Japan. Does this mean that we shall see a wave of investment in European bonds and equities? Quite probably.

But on the other side, there is the matter of supply. If there is a severe limit on the supply of euro denominated bonds, this will force the price to a level where the lack of risk no longer justifies the premium paid. However, the other side of this equation is the vast amount of European corporate funding which is currently provided by banks. But these are some of the very banks which have lent most heavily to Russia and the dodgier bits of the Far East, so the opportunity for corporate bonds of less than AAA quality suddenly looks very interesting.

Perhaps we are about to enter a second virtuous circle for the euro – one in which there is a sudden appearance of lower quality bonds, at just the time when there is a desperate market for them ...

Maybe Napoleon had something in the idea of luck being a virtue after all.