Monthly Newsletter – June/July 2024

In the last newsletter I mentioned some political events and the first US presidential debate on 27th June which might impact the investment world. Politics has become even more relevant now.

In the UK there was the General Election which saw the Labour party win far more Members Of Parliament than the Tories and they can now proceed with their program for the next five years. They have promised not to increase income tax, national insurance or VAT but there are many other financial areas where changes might come. For example, I expect them soon to remove the non domicle status which was mooted by the Tories. This status allow the very wealthy to live in the UK and not pay tax on their worldwide income. It made the UK a tax oasis for the mega wealthy and few other countries offer such benefits. The ending of this will highlight the question of domicile.

Domicile in the UK is often confused with UK residence. The latter is easy to lose but UK domicile is very difficult. It matters because UK inheritance tax (IHT) is based on domicile and not on residence. The UK has many tax treaties regarding income tax but there are very few that include IHT. It is therefore possible to face IHT both in the UK and another country where ones lives. I can see the concept of domicile being replaced by residence for IHT tax purposes but perhaps the scope of IHT expanded to include pensions.

A paper by the Tony Blair Institute from May 2023 highlighted the case for more investment in UK companies and mentioned the UK pension funds as being ideal investors. This is rather ironic as it was the Labour government's finance minister Gordon Brown who took away tax benefits for UK pension funds on dividends paid by UK companies. This together with ever increasing risk and liability controls resulted in pension trustees investing less and less in UK companies. In times past perhaps 50% of the assets of a UK pension fund would be allocated to the UK stock market but that has now dropped down to less than 5% with the allocation to bonds now dominating. This caused huge problems when the Liz Truss government upset the UK government bond market (Gilts) to the point where some were about to collapse. Calm was restored, but Liz Truss was replaced.

That crisis affected defined benefit pensions set up by UK companies for their retiring employees. However those schemes have been largely closed to new members for some years as companies found them a drain on resources and balance sheets. The public were then encouraged to have their own personal pension, called Self Invested Personal Pensions (Sipps). These have over the last years built up significantly with tax benefits for investors and currently they invest with a great deal of flexibility. Might the new Labour government look at these funds and wish to direct them into UK companies and even support their policies, such as their energy policy? The latter is the quest for "Net Zero" emissions for CO2 and will cost billions. Do employees wish to see their pension funds switched into UK wind and solar farm companies, across the country? Also Sipps are at the moment IHT free. But for how long?

One interesting point is that the new Labour government has not had a negative impact on the Pound, indeed it has strengthed in the last weeks and is today almost touching 1.20 to the Euro and 1.30 to the US dollar. UK investors will therefore see overseas investments worth less in sterling terms, but with less imported inflation, the opportunity for the Bank of England to lower interest rates on 1 August might arise.

In the USA big events are unfolding. The presidential election is on the 5th November and Biden has just stepped down as a candidate. Who ever replaces him, voters will have a choice between two very different people and policies. If Trump wins, as the polls suggest, then he will increase oil production in the USA, raise tariffs and have a very much America first foreign policy. How all this impacts the investment world is an open question but it makes the investment world much more unpredictable.

The political landscape of Europe has also seen changes. In France the recent elections have changed some things but Mr Macron will remain president until 2027. In the EU commission, Mrs Von der Leyen has won a second five year term as director. "Plus ca change, plus c'est la meme chose " (the more things change, the more they stay the same) but they are getting worse. The European economy has recession problems and the problem of Greek's massive debts have not gone away. My Feb 2015 newsletter pointed out the Greek debt at Euros 321 billion for a population of 11 million people which is Euros 29,000 per person.

The IMF loan repayments are due to end in 2024 and then it will be about Euros 5 billion per year to repay Euro members for the bailout. The last loan payment is due in 2057 effectively to be paid by Greeks not even born today! But in 2022 the debt was at $400 billion or Euros 430 billion. It is getting worse. And all those bonds issued by Germany at negative yields, are still held by someone (European Central Bank) and will have massive unrealised losses. How this develops and the impact on the Euro is unpredictable. (Newsletter Feb 2015 on request)

We avoided investing in the Far East because of questions about China and Japan and how unpredictable they had become. The latter has recently seen its stock market rising to top the high of 1989 (a 35 year wait for some investors) but the currency has collapsed from 110 to the dollar in summer 2021 to 160 by summer 2024. That is a fall of nearly 50% in just three years, so much of the stock market rise in Japan has been more than lost for overseas investors. As for China the Hong Kong market is 30% lower over the last 3 years and the Chinese property market continues to crash. Where this will end for investors in the Far East is difficult to predict.

Had Japanese investors 3 years ago decided things were too unpredictable and bought gold they would have seen a rise of over 80% in Yen terms (Gold 2022 +13.4%, 2023 +21.6%, 2024 +30%)

Gold is an asset to hold in a portfolio when a currency gets into trouble or the world become more unpredictable.

People forget that there is still a major war in eastern europe, with massive loss of life and it has continued for over two years. Wars are unpredictable!

Best wishes and have a wonderful summer

Tim 22 July 2024

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