

## EUROPEAN DEBT CRISIS

For nearly two years now the European debt crisis has captured headlines, unnerving markets and investors alike. The global economic slowdown that began in 2008 exposed the unsustainable fiscal policies of numerous nations around the globe, most notably in the peripheral euro zone countries of Portugal, Ireland, Italy, Greece and Spain, affecting those countries to varying degrees. Now, after years of reliance on easy credit combined with long-term structural issues including large public sectors and entitlement programs, and quite simply government overspending, these countries are left dealing with the negative consequences, further exacerbated by a slow growth environment.

Since last spring, the International Monetary Fund, European Union and policymakers have engineered major responses in an attempt to resolve the sovereign debt crisis. These have included bailouts, purchases of government bonds, and the establishment of emergency funds to provide liquidity when needed. The economically stronger core countries, like Germany and France, have pushed for austerity (higher taxes and lower spending) in the region. Meanwhile, the troubled peripheral economies have indeed shown notable commitment to addressing their budget deficits, but it has led to public protests, political upheaval and nervous markets. The conflicted scenario of a single currency, but largely independent fiscal policies, raises concerns about the legal ability and political willingness to make progress happen quickly. As a result, we believe that it is reasonable to expect the region to remain troubled for the foreseeable future. This is not to say that there is not opportunity for investors, but, rather we expect the “risk-on”, “risk-off” nature of the global markets to result in periods of increased volatility.

One can speculate as to how the sovereign debt crisis ultimately unfolds and whether there will be defaults. At this point, we believe the question of whether a default will occur is less important than the question of how a default might take place. A “disorderly” process would most certainly lead to greater market volatility and possible contagion. However, we believe continued progress towards greater political and fiscal unity among the euro zone members and an “orderly” process in the event of a default would result in the restoration of confidence and stability to the world’s equity and credit markets.

Given the interconnected nature of the global economy, we acknowledge how easy it is to become skittish about the developments in Europe. During difficult periods like this, it is important for investors to resist getting swept into the day-to-day frenzy of the media’s dire headlines and to make investment decisions from a disciplined perspective free of emotion. As always, we encourage investors to hold a broadly diversified portfolio across asset classes, sectors and geographic regions to hedge against risk, and to contact your trusted advisor with any questions or concerns.

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