money matters

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by Charles Purdy

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So where to for the Euro and Sterling?

This is a question I am often asked and has been very simple to answer ever since the collapse of Northern Rock twenty plus months ago.

Sterling has enjoyed brief periods of respite, but the overall direction has been one way - and that is downwards against the Euro.

Mid year, Sterling gained against the Euro as the market decided the future for the UK economy was on the up and we got close to €1.19/£1. However, the Bank of England meeting in early August resulted in an increase in the Bank's programme of quantitative easing. In my simple way, I understand this to be the Bank of England printing money which they pump into the economy with the hope that it will get us all spending again. The market took this very badly, viewing it as a major negative on the UK economy.

At the same time, the European Central Bank has been much more effective and efficient in supplying liquidity and the necessary boost to the Euro zone economy. There are major problems which are clear to see when looking at Spain or Ireland. The housing booms have gone into fast reverse and as such, their respective construction industries are suffering. Actually, they are in intensive care with a very long recovery period ahead.

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But one major advantage that the Euro zone has is the might of German industry, still the world's exporter. But Germany has suffered as the world's economy has contracted, which means that its goods are not as needed as they once were.

They are also suffering as the Euro is so strong against many other currencies including the US Dollar. At one stage last month, we even saw a rate of US$1.50/£1. This means that the Euro zone's exports are becoming more expensive. Not a great situation when fewer goods are needed and there is so much surplus capacity.

There is one batch of people who have benefited from the current strength of the Euro and that is the people returning to the UK. If you bought your property at say €1.50/£1 or better and you are now able to sell at a price in excess of the original cost, you will make a profit in Sterling terms of over 25 per cent. And house prices have pulled back in the UK as well.

But Sterling seems to be slowly gaining credibility and a few fans. Early November, we had the latest Bank of England meeting and they increased their programme of quantitative easing to 200 billion pounds sterling. But Sterling held its own against the Euro. Two reasons: firstly the market was worried that they could increase it to 225 billion pounds sterling so anything less was a relief and secondly, the Bank of England made it clear that they would only feed the increase into the market at a slower rate than the previous tranches.

At the start of this year, when Sterling was close to parity against the Euro, the market was talking about a year end price higher than €1.20/£1. I never knew what drove this, apart from some wishful thinking. I still believe it is probably wishful thinking anytime soon.

Also the European Central Bank has handled matters more effectively than the Bank of England in the past year, which has benefited the Euro. But the strong Euro is really beginning to hurt the Euro zone and as such, it is difficult to see a huge amount of downside for Sterling against the Euro. Clearly, any major shock in the UK economy would reverse this thought process, but we could well be closer to €1.20/£1 rather than €1.10/£1 by the end of 2010. But please note I have been wrong in the past!

- *Charles Purdy is a Director at Smart Currency Exchange Limited – the International Payment Specialists. To move money between Spain and the UK go to www.SmartCurrencyExchange.com for more information - or if you prefer to speak to us in person, we're only a local call away on (00 34) 966 260 709.*