The Euro: Reports of its Death are Greatly Exaggerated.

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Sure, there are lots of reasons to be concerned about the Eurozone. Greece is a basket case, by any measure. And Europe is full of people who have a long and storied history of slaughtering one another on an industrial scale every couple of generations, going back to the dawn of recorded history.

But Germany isn't rattling its sabre and talking of Lebensraum, this time. France elected a socialist, sure, but he's rather a pragmatic one. And France hasn't surrendered to anyone outside its own borders in years.

Which is a nice change.

But Greece is sucking assets out of the rest of Europe like a black hole, as European financiers frantically try to save the Greek economy from collapse - or at least buy some time. But Germans are growing weary of funding Greek irresponsibility. The Greeks themselves are increasingly stashing euros in those urns their famous for making, or under their beds, or abroad - anywhere but Greek banks, where their euros become vulnerable to seizure and devaluation in a currency conversion.

Wither the Euro?

Will this be the death of the Euro? Has the Great Experiment in European unity failed?

"We're not seeing that at all," says

Rainer Vermehren, who heads up the closed-end equity fund efforts at Deutsche Bank. "The euro is too much of a reality now... Europe will not abandon the euro."

The engine driving the European economy these days is, of course, Germany. The largest single economy in Europe, Germany remains a potent manufacturing force. And the frugal Germans have historically been, culturally, a nation of savers - not spenders. "They're like Japan, in this respect," observes Vermehren, referring to the German penchant for saving over 11 percent of their after-tax income. (Greece, in contrast, has a personal savings rate of negative 12 percent.) This poses some difficulties of its own - Germans don't buy very many exports from Ireland, Greece, Spain or anywhere else - and their pro-savers' stance for a strong euro makes it tough for other countries to export outside of the Eurozone. But that healthy savings rate at the core of the European economy does give Germany and the Eurozone some breathing space for navigating the crisis: Although their population is increasingly resentful of bankrolling their prodigal neighbors to the south and west, Germany continues to provide liquidity to the more troubled nations.

Greece's Dilemma

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It's devastating to savers, and bondholders alike, but it does allow the government to pay back its obligations on paper, nominally, anyway. But unlike the United States, which is free to set its own currency level, Greece has no currency of its own. Even though the European central bank has put the liquidity pedal to the metal, providing Europe's struggling banks with nearly unlimited free liquidity, Greece cannot devalue the currency far enough to rescue itself. At this point, little choice remains but to accept fiscal ruin, or abandon the euro, and issue drachmas at a fraction of their traditional value.

The situation will be extremely difficult in Greece for a while. Inflation will destroy a generation of Greeks - and the people are already preparing, stuffing euros in mattresses and shipping money out of the country to protect it. A run on Greek banks is increasingly likely. Scenarios keeping Greece within the Eurozone are becoming increasingly untenable.

The other PIIGS - Portugal, Ireland and Spain, are deeply troubled as well. But none have comported themselves with anywhere near the irresponsibility as Greece, over the years. Vermehren expects them to remain with the euro. "Our assumption is that if anyone abandons the euro, it will only be Greece," he says. Meanwhile, other countries, such as Turkey, are clamoring to get in.

Bargains Abound

A great deal of pain is already "baked in" to European equities. The European markets, as measured by the Stoxx Europe 600 Index, have corrected over 40% since the highs in 2007. They are now trading near their cheapest levels ever - both in terms of their own history, and in comparison with U.S. markets. The price to book ratio is trading at a 40 percent discount to U.S. markets. And the dividend yield of 2.6 percent is fairly healthy, given the low interest rate environment.

"We'd have to assume that a large part of any eventual Greek "solution" is priced into stocks," Vermehren says. "But it would be naive to state that when the event actually happens, the market would not experience a negative knee-jerk reaction to the news." But Vermehren believes any such reaction will be short-lived, and prices will recover quickly.

Fund Flows

Global investors have been pulling capital out of Europe as an asset class for some time - focusing on more global approaches to portfolio allocation, rather than more focused allocations to Europe. A good deal of the "hot money," in our view, has already been pulled out of the European markets - hence the substantial discounts on European stocks compared with U.S. markets. European stocks also seem to be reflecting the eventuality of a recession that may already be upon

us. But dividend yields are still strong. Vermehren's funds are closed-end funds, which shelters investors somewhat from the buffeting of the ebbs and flows of capital: Sudden redemptions are not a concern for the closed-end fund manager.

Vermehren's funds tend to trade at discounts to NAV as well - both the European Equity Fund (EEA) and the New Germany Fund (GF) consistently trade at discounts of 8 to 12 percent - which effectively magnifies any dividend yield on a cash-on-cash basis. When fund flows are negative, and the environment volatile, closed-end funds are the way to go.

Portfolio Moves

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And although Deutsche bank has traditionally been a growth-at-a-reasonable-price outfit, by training and temperament, the company's fund management teams have pulled in their horns. They've abandoned their growth-stock focused approach for the time being, concentrating instead on an equity capital-preservation strategy. They're focusing on strong earners, and strong dividend payers. What's more, the focus is on the stronger economies at the European core: The Netherlands, Germany and Switzerland, rather than the PIIGS.

Specifically, the European Equity Fund - one of the funds under Vermehren's supervision - has beefed up holdings in Austria, Denmark, Norway, Germany and the UK. At the sector level, Vermehren's team has souped up their exposure to consumer discretionaries, financials (but not banks), information technology and health care. The fund now trades at a discount of 9.45 percent to NAV, while sporting a dividend yield of 2.27 percent based on the share price. The fund has an average P/E of 12.21 as of 29 May, 2012, and trades at 1.39 times book value.

The New Germany Fund, of course, can't go anywhere besides Germany, by definition. But Vermehren is finding bargains in industrials, construction, food and beverages, software and insurance companies. The New Germany fund currently trades at just under 10 times earnings, and at just 1.05 percent of book value. Theoretically, investors are buying the assets of great German companies - and getting future growth for free. This is a compelling value argument to make, and a 1.05 percent of book value is a nice floor underneath these stocks - especially in the industrial sector, where book values have meaning. (They're a little more tricky in the banking world, which has to treat bad debt as an asset long after most people have given up hope.)

Uncertainty Remains

Vermehren, of course, is an equity guy. They tend to be bullish, by definition. If they weren't optimistic, they wouldn't be equity guys! The three funds under Vermehren's control are not hedging currency exposure vis. the dollar - and never have. And a general abandonment of the euro is not even among the scenarios they are seriously wargaming, so confident are they in the strength of the euro experiment.

Insurance underwriters, on the other hand, are paid to be paranoid. They are naturally pessimistic by training and temperament. Lloyd's of London announced this week that they are positioning themselves to be prepared for a general Eurozone collapse. We've been there before, with Italy, though, and managed to step away from the precipice.

Which is a good thing: When insurers are ready, it makes the negative market event much less likely to occur.

And as of this writing, there were some more rumblings that Spain's financial system was coming under increasing strain - with yields on Spanish sovereign debt approaching 7 percent.

Perspective

It's useful to put the Greek bailout effort in perspective: The Greek problem is not the only large intervention in the European economy in the last generation. Remember: Germany absorbed a financially devastated East Germany in the 1990s and 2000's. The cost: About $1.9 trillion over 20 years. The entire Greek bailout effort amounts to $320 billion, though over a shorter period of time. Germany was able to absorb reunification, with little assistance, other than the American security umbrella.

Europe can absorb Greece, and the euro will survive, even if (or when) Greece abandons the currency.

Meanwhile, global investors will do well to keep their eyes on the prize: Despite the headlines, the Northern European countries- Germany, especially - are still strong. With their strong manufacturing tradition, German wages are still extremely competitive on a global basis, at least at the top end of the manufacturing food chain. German wages have room to rise - which can boost domestic consumption or the savings rate or both.

Meanwhile, closed-end funds provide investors with some shelter from volatile cash flows, while giving owners a chance to sidestep basket cases like Greece that broad ETFs have to hold on to. ■