

## The Bulletin, Feb 09

Just occasionally, the truth hurts

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### Spending dam-burst ahead

The economic crisis is in large part caused by people uncertain of the future holding spending back. In the UK, low interest rates mean we get a tiny return on savings, mortgage costs have not fallen as far, so the gap between borrowing and savings rates has increased sharply. While this should incentivise spending, many are paying off some of their mortgages instead, as the effective return is higher. The trouble is, even those in work are nervous about spending - fearing tough times ahead. The business response is to cut spending and headcounts. With low confidence in government, economic decline is inevitable. So although most are still in work, on the same salary as before, sales are down and companies are going under.

However, this spend reduction means people are building backlogs of things they need. Many will have saved cash, or reduced debts, so will soon be in a better position to go out and spend again. Emotionally, we have also got used to having money and spending and Generation Y (born 198-1999) has limited experience of living in a recession. At some point, the dam of pent up desire will burst and this postponed spending will flood onto the market. Sadly, many companies who so desperately need help now will not survive long enough to benefit.



It is hard to say when confidence will return. Maybe later this year, maybe not till next year. In the short term, savings rate reductions greatly favour debt repayment over buying stuff. The real power lies with those who have no mortgage and accessible savings. Further economic decline means things will probably

cost less in the next few months, as companies are forced to offer large discounts. Large purchases are more likely to be postponed if people think they can get them for less later. So for everyone, there is less incentive to spend right now and little prospect of change in the next few months – except for those businesses forced to close before the recovery starts.

But this dam-burst is inevitable. When some of the debt has been paid off, when money is burning a hole in the pocket, and as new technology brings exciting products to market, people will spend heavily again. When they do, the pick up will be rapid. Companies that survive should be more efficient, less wasteful, more innovative, leaner and meaner. The banking system will hopefully have been reformed and better regulated. The economy should be far healthier when it recovers than when we entered the recession and better prepared for the world we are moving into. Well, almost...

#### **Coming Next - Video Visors**

This could be the year when video visors make it into the mainstream, probably as one of this year's must have Christmas presents. Video visors contain displays that allow the wearer to watch video, play games, or browse the web. The first generation will be opaque, so will only be suitable for when the wearer is seated, but soon, semi-transparent ones will be available, that allow imagery from computers to be superimposed onto the everyday field of view. This will enable merging of the web and the real world, so that characters from games, or friends' avatars from social networking sites could populate the high street along with 'real' people, or even replace real people. This 'dual architecture' could give a different appearance to every pedestrian.

#### **Ian's Rant 1 -**

##### **Backlash against the civil service**

One big fly in the economic ointment is the rapid growth of the civil service over recent years. In many areas, the civil service employs most of the working population - voters who could in turn favour a government that looks after civil servants. So there is a strong political

momentum associated with improving civil service working conditions. These have gradually become much more favourable than in the private sector, especially as the private sector has been forced to close many final salary pension schemes, and taken the full impact of the recession. Recent attempts to level the playing field between public and private employment conditions have been very feeble and fizzled out quickly.

Nevertheless, this is the year it must be addressed. Public anger at what is seen as a two stream society, one part living in protected comfort at the expense of the other, is growing rapidly. When the civil service was associated with low pay, it was assumed a reasonable trade off for better job security, low stress, and a nice pension. Now the average civil servant is paid significantly better than their private industry equivalent, gets more leave, takes more sick days, works less hard for fewer hours, and retires earlier on a far better pension. The now all-round superiority of public service terms and conditions is simply not sustainable, paid for as it must be by those working in the private sector. So if the government fails to address the disparity voluntarily, they will be forced to by a fierce private sector backlash. This so far amounts to no more than a number of irate press articles and letters, but it could erupt soon into demonstrations and unrest if left to fester.

#### **Rohit's Rant 1 –**

##### **Banking - Bail Out or Black Hole**

As over eight trillion dollars in the US and hundreds of billions in the UK are channelled to the financial services sector through a variety of mechanisms, governments try to convince us the taxpayer could profit handsomely from the bail outs. However history is not on our side. Recent research from the IMF studied 124 banking and financial services failures since 1970. They found that, on average, it takes 3-7 years for a full recovery, the cost is around 13% of GDP and taxpayers get back just 18% of the bailout investment. With – for example - the total assets of the big three UK banks being roughly three times the size of UK GDP, the

question is really whether these banks are just too big to bail out in their current form.

The money poured in to prop up bank balance sheets isn't being recycled into new lending at anywhere near the rate government expected. One wonders why these deals went through without clear agreement on such basic issues. We're told – mainly by the banks – that if they aren't propped up in their current form, the economy will suffer. That horse has already bolted – just ask those losing jobs and closing businesses on a daily basis.

Maybe we need to look at a much more radical restructuring and simplification of the banking system – splitting out consumer banking and day to day business banking from the riskier investment banking, leveraged debt and proprietary trading operations. Ring fencing the toxic wastelands and putting the other sectors under new management might take some time because of the complex structure of these patently unmanageable behemoths. However, it would allow new investment funds to flow into the safer banking sectors, start to rebuild trust, and get the real economy going. It would also allow full valuation of the possible scale of bad debt on banks' books and enable tough decisions to be made about how to share out the losses between all involved.

## **Ian's Rant 2** **End of the greens**

Now that everyone is environmentally aware, even if they don't always act that way, 'greens' are rapidly losing control of environmental issues. This has to be a good thing, since green politics was often thinly disguised socialism. The subscription to environmental protection by almost all parties now allows the issue to be given over to scientists to deal with it.

As the greens lose their mandate, so meta-religious environmentalists will also lose their haloes. In fact, it is now apparent that many of the earlier policies forced through by environmental groups have actually significantly damaged the environment. Policies such as favouring bio-fuels and carbon trading have

done great harm by incentivising destruction of rain-forests and drainage of peat bogs, both of which have increased the amount of CO<sub>2</sub> in the atmosphere. With science at last starting to take control, we should look forward to seeing new ideas that will actually help fix the problem.

## **Rohit's Rant 2** **How Modern are we?**

The two most frequently aired management themes of the last decade have been (1) the need to transform customer service and (2) the imperative to innovate. The most commonly cited enablers have been unleashing our people and embracing the internet and social networks. However, in the current crisis, it seems that while we are still committed to service and innovation, we're paying scant attention to people and the potential of the internet - if the results of our current survey on Winning in a Downturn are anything to go by.

The survey's still running, but as we stand, the most popular actions are cost cutting (60%), improving customer service (48%) and innovation (40%). Only 17% prioritise either staff motivation or increased use of the online channel and only 8% are spending more on training. When asked for the top three priorities for surviving the downturn, clear direction and strategy (59%), customer relationships (57%) and cost control (48%) came out top. Just 24% see staff motivation as a priority and only 3% opted for greater use of the internet.

We don't need data to tell us that unmotivated employees hold back performance – but it's strange how easily we've ignored the people factor when things get tough. I'm also amazed at how many businesses are ignoring the power of the web as a virtually free sales, service and recruitment tool, as a magnet to source new ideas, as a research tool, as an engagement vehicle and a means of driving word of mouth communication. Given that both motivation and exploiting the web can be done a virtually no cost – this feels like a massive missed opportunity.

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***If you'd like to meet up, in March Ian is in London, Edinburgh and Abu Dhabi and Rohit is in London, Edinburgh, Liverpool, Turin, Berlin, Mauritius and Abu Dhabi.***

***Please let us know about developments and topics you'd like covered in future issues.***

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