

Cable vision



AT THE ACT ANNUAL DINNER, ACT PRESIDENT GERRY BACON AND TOP POLITICIAN VINCE CABLE, ONE OF WESTMINSTER'S MOST MEDIA-FRIENDLY INDIVIDUALS, GAVE THE TREASURER COMMUNITY PLENTY TO THINK ABOUT, AS **GRAHAM BUCK** REPORTS.

The choice of guest speaker at the ACT's annual dinner in November, again held at London's Grosvenor House Hotel, could be seen as representing political balance. In 2008 the after-dinner speech was delivered by the Conservative party's shadow foreign secretary, William Hague. This year it was the turn of the Liberal Democrats' deputy leader and shadow chancellor, Vince Cable, who has been something of a media star since his memorable description of Gordon Brown's "remarkable transformation... from Stalin to Mr Bean". Perhaps the current prime minister will have more time on his hands come next November and be able to do the honours for the 2010 annual dinner.

Cable was introduced by ACT president Gerry Bacon, whose own speech focused on three areas arising from the financial situation that he regards as particularly noteworthy.

ROLES Bacon began by considering the underlying purpose of the treasurer and the banker, whose respective roles he characterised as supporting their operational business and oiling the wheels of those businesses by allocating capital effectively. But do we always focus on these matters as financiers, he asked?

Bacon's own experience in the financial markets over a period of 25 years – including a 15-year stint as group treasurer of Vodafone – has led him to believe that a significant amount of time is occupied in zero-sum games. A prime example he gave was the trading of credit derivatives, where for everyone who makes money there must also be a loser. He asked whether such trading really contributed anything to the world's GDP.

He observed that the volume of credit derivatives traded in

Executive summary

- The finance industry must give up playing zero-sum trading games and concentrate on adding value to the business as well as commerce and society in general. And while the government's economic medicine has succeeded in pulling the patient back from the brink, the prognosis is sombre.

Vodafone exceeded its amount of debt outstanding – which with over £20bn of public debt outstanding was not an insignificant figure and highlighted more than just hedging activity. It caused daily volatility, but in a medium-term measure – namely, the risk of default over a five-year period – which is not helpful for issuers.

While the ACT president said he was not opposed to liquid markets or transparent pricing, he pointed out that as "temporary custodians of our roles in organisations", treasurers could usefully reflect on what they were able to add, not only to the organisation's bottom line but also to society at large and even to world GDP.

TEAMWORK Bacon's second point considered the teamwork needed between providers of capital – ranging from bank to bond investor to other financial investor – and borrowers. "At Vodafone, I owed a duty of care to those who lent us money to ensure they got it back," he said. "And if we don't think we can repay it then we shouldn't take it. I wanted to ensure that, as an organisation, when we made statements about our credit ratings we stuck to them. Equally, I





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expected those with capital to be able to lend it to us when needed.”

This understanding is a two-way street, Bacon suggested, in which the respective businesses will be strengthened if capital is provided, serviced and returned. These are the basics that appear to have been glossed over by recent events.

AWARENESS Finally, he observed that the lessons of the past two years have been how important it is for everyone in the financial services industry to understand that they should be aware of what their organisation is doing, what is happening and could happen in the market, and how each connects.

“This is applicable to everyone, whether they are running the boards of banks, sitting on corporates’ audit committees, acting as CFOs, treasurers, regulators or politicians,” Bacon said. Education, principles and communication are all of paramount importance in achieving this understanding, he added.

He suggested that all those fortunate enough to work in the financial services industry should direct much of their energy into three main areas: ensuring that real economic value is created; respecting the two-way street between borrower and lender; and checking that their peers, bosses and staff are properly educated and trained for their roles.

LOW ESTEEM Cable, the Liberal Democrat deputy leader, began his speech by admitting that the profession of the politician, which doesn’t stand very high in public esteem at the best of times, is particularly low at the moment. However, the disillusion that has been deepened by the financial crisis could be starting to lift, with signs that the worst of the downturn may be over. As he observed, the headline on that day’s Evening Standard had proclaimed: Britain On The Way Back.

But was this true?, he asked. There are evidently signs of a revival in confidence on the part of both companies and consumers. Yet the unemployment figures are still rising and too many young people are unable to get work. Cable suggested that the rise in graduate unemployment was particularly noticeable.

Added to this, the chancellor has recently agreed a further massive bailout for the banks. Yet the sums already spent in propping them up are already so massive that “no-one batted an eyelid”. Cable added: “The image I have of the UK economy is that of a patient who suffered a massive heart attack a year ago. While the patient is fortunately still alive, he hasn’t yet moved out of intensive care.”

The good news is that modern economic medicine, in managing to save the patient, has also prevented a reoccurrence of the Great

Depression of the 1930s. Intervention by the government was the right thing to do at the right time and was further helped by governments around the world working together for a co-ordinated response to the crisis. China’s response in stimulating its economy in order to resist the downturn was also correct.

But Britain has been hit particularly hard by the crisis because of its reliance on the banking system. Its collapse has had a disproportionate effect on our economic performance, while the property bubble has also served to make us particularly vulnerable.

The question is what happens next. Cable offered two possible scenarios, both of them very plausible.

The first is that the UK motors firmly back on the road to recovery. Unemployment figures improve, confidence returns and by 2011 the rally will be well in train.

It’s not an unlikely scenario, but we should keep in mind the possibility of the rather bleaker alternative: there are still serious impediments to the anticipated recovery becoming reality. British consumers are still heavily in debt, unemployment remains high and this, in turn, undermines consumer confidence and spending. Quantitative easing is also creating another artificial bubble in the property market, while interest rates have been cut to practically zero. This policy will have to be reversed in due course, which will jeopardise any revival. Bank lending is still very subdued and the government’s budget is a mess. Borrowing has reached 13% of GDP in the extremity of the crisis, because of the collapse in government revenues. While these steadily wilt, public spending has ballooned to 48-49% of GDP and the difference has to be borrowed.

“The government is fortunate in still being able to borrow cheaply, but there is an awareness that this can’t continue indefinitely,” warned Cable.

The necessary adjustment – something in the order of 6-7% of GDP – needs to be made. This inevitably means that some difficult decisions will have to be taken on issues such as public sector pensions.

The government’s challenge lies in meeting these problems. Having pumped so much money into the economy, it can’t stop doing so too quickly or the economy will plunge straight back into recession; but if it acts too slowly, we will lapse back into inflation.

Still, there continues to be potential in this country for serious entrepreneurs, Cable concluded. “There are a lot of companies that will help the economy to recover, provided that we – as politicians – let it happen!”

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