

Breaking recession psychology

It's July 2008. Northern Rock has long gone and the sub prime mortgage problems in the US are old news. Yet the high LIBOR rate is all but paralyzing the banking industry, Lehmanns knows that the game is up and many of the banks in the US and UK can see that their paper gains look like unsustainable liabilities. It's the perfect storm; those on the inside of the financial districts can see it and many have run for shelter. Yet at this date the public is blissfully unaware and car sales are running very well. Tata even feels good about buying Jaguar Land Rover. But within 8 weeks Lehmanns would collapse and public knowledge of the weakness of so many other sound institutions would be exposed. Crucially, credit finally dried up for most people.

The point is this; the psychological reaction to recessions is linked to perceptions and knowledge . not actual events. The public should have been tightening its belts in September 2007 when the subprime story broke but it took a year for the full effect to become understood by the people on the high street.

Robert Peston became the hero or villain of the recession and now we focus on figures and even obsess about figures. Some feel so scarred by the recession that they can no longer tolerate the figures. Yet in the main, we treat recessionary figures like the winter weather forecast . the worse they are the more that fodder and profitable banner headlines they provide for the media and the water cooler gatherings. We seem to be good news averse and in downward spirals the collective psychology serves to support the received wisdom that we are all heading downwards together. Such is the nature of collective psychology.

In this climate, even a piece of good news may scarcely get a mention and if someone dares to use the phrase 'green shoots of recovery' they will be derided as mad.

Let's look at an example of one week. On February 11th the BBC trailed the unemployment figures as being almost certain to be over 2m; they even went into some detail to explain why it would be over two million. But when the figures came out later that day they were 1.97m. Ah, but we only report the news + protests the media.

The day before this happened; the BRC figures for January showed that sales on the high street in January were UP 1.1% year on year, a figure supported by the ONS. It was barely reported because this does not conform to the broad public wisdom of sustained gloom so well fed by the media. So the country is down in the mouth and who tells us it is even worse than we think it is already and on the same day? Our number one banker, Mervyn King ('this will be a long and deep recession'). Other recent remarks by Ed Balls ('this is the worst financial crisis for 100 years') and Gordon Brown ('we live in a time of uncertainty') do nothing to reduce fear in the UK public. Should they lie? Of course not but some thoughts are better left unuttered, after all, do they really know things will get much worse? I think not. Their forecasting so far has not been very clever but our leaders cannot afford to talk down the recession.

It is an irony that many households are better off now than a year ago. Lower interest rates, cheaper mortgages, lower energy costs, lower VAT. Yet fear and apprehension are all pervading and crowd out any signs of hope. As we know, a recession becomes a self-fulfilling prophesy when consumers react to pundits' predictions of doom. They cut back spending, prompting manufacturers to produce less, freeze investment and lay off workers.

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This recession is different to all previous ones and significantly so, few people disagree with this view. Its causes, its reach and scale are all unique. But sixteen years on since the last one, the world is very very different in so many positive ways too. For example the financial interdependency in today's global economy is so great that every continent is now in it together.

Yet the mechanics of world finance and business are more complex and few people fully understand it. As it turns out few who should have understood did too. Where does this leave the consumer, the electorate, Joe the plumber and the man on the Clapham omnibus? Confused, fearful, pessimistic, cautious, isolated, depressed even. Many are angry.

The business world is arguably in a worse state economically and psychologically in the recession than the consumer world. How can this be? Many businesses depend on the now squeezed bank credit of some kind and many see signs of a slow down and perceive it to be worse than it really is. They then defer investments and even lay off staff in anticipation of the slowdown. The climate of negativity within commerce appears to be worse than on the high street.

The OECD predicts gross domestic product will fall by 0.9 per cent in the United States, 0.5 per cent in Europe and 0.1 per cent in Japan in 2009, while the unemployment rate worldwide will rise from 5.9 per cent this year to 6.9 per cent in 2009 and 7.2 per cent in 2010. These figures are not good news but neither are they disastrous and they are not 1929 all over again.

The expression used to be; ~~when~~ when the stocks go down the hems go up. The suit is now more in fashion and people are dining out in their droves, though more on pizzas than sea bass. They shop; they go to the movies even more than in 2007. What they do not do and in many cases, cannot do, is indulge in the big ticket items such as cars and houses. Plasma TVs? Yes, but these are now sub £1k and we love our TV like we love our shopping and beer. Beer sales are down in the pubs but up in the home. So the British family now gathers around a huge flat screen for the nightly update from the grim reaper. Robert Peston.

There is individual and collective psychology at play in the way the recession is treated by the public. Let us not blame the public for some negligent herd instinct and lack of individuality. After all it was the smaller herd instinct of the financial elite that got us into this mess. They thrived on the good news and the misplaced confidence that this bolstered just as the media feeds on the bad news.

What do they do when they hear news that does not fit their frothy mood? They fire the messenger. Welcome to the cast Mr. Moore - late of HBOS who warned that HBOS was growing dangerously.

The individual psychology in these situations can be summarized as in the herd, the response to the crisis is: Fright, Fight or Flight. With relatively few in a position to take flight (where's the refuge?), most hunker down with their fright. Some are in a fighting mood. We have seen unrest in France and Russia, even the mild mannered Icelandics and Irish protesting on the streets. These fights are so often manifestations of anger and frustration. Few believe that they will effect any change.

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Once the financial system is stabilised then Governments all over the world and economists are hoping for an increase in consumer confidence to take hold. The US should take the lead in this. Americans are by nature more optimistic and their economy is mature, sophisticated and of course large. The arrival of a dynamic new president with a spectacular recovery package of \$800b with rapid monetary and fiscal benefits should see a shift in confidence in the US . quite quickly. At least by spring.

Developed countries, and some emerging ones such as China, are pumping cash into their financial systems to restore confidence in the banks and other deposit-taking institutions and to encourage more lending. Central banks all over the world have been slashing interest rates to make borrowing less costly.

The OECD has urged governments that have the wherewithal to provide tax rebates or payments to households and to invest in public infrastructure projects. This is happening.

The oil is now very low and moderate oil prices may be a defining feature of the global economy for some time. The International Energy Agency sees oil demand in the developed world falling by 1.8 million barrels a day from 46.5 million last year to 43.9 million over the next 15 years.

The price of other commodities is falling as well. Share values are often so far below asset values that they make no more sense than the absurdly high multiples of the dot.com bubble of 2000.

So we're counting on our political leaders to give us reasons to be hopeful. In addition to sounding bullish about their decisions they should also look at the value of blame. Most of the public do not understand the principles of what has gone wrong and what is happening now. But they will understand the sight of the CEO of Lehmanns in the dock and they do understand the RBS directors being paraded and saying we are sorry. This brings positive closure to matters that concern people and are not understood. More of this will be helpful.

The U.S., the OECD says, will lead the way out of recession, possibly beginning as early as the second half of 2009. The economies of developed countries are largely driven by consumer spending -- which accounts for up to 70 per cent of GDP in the U.S. So in breaking the psychology of recession it is vital that the consumer takes a central role in all economies, not least the UK.

Consumer confidence will come from credible initiatives that are understood and believed in. Confidence will also come from highly visible, strong, confident, clear and consistent leadership. This is a time for a special type of leadership. This is a Churchillian moment in time if you like. Between 1939 and 1942 Winston thought there to be a good chance that Britain would lose the war. The public never sensed that. Gordon Brown needs to walk, talk and look like a man who believes he can win this war on the economic front.

I rather doubt that the jobless total will reach 3m, much less hurtle towards it as some predict. Inflation will stay low, money will stay cheap, and we will start to see benefits from the low value of sterling and people will holiday in the UK more. Much else besides will be good news such as order and stability in the financial world. When enough good news filters through . assuming that the ghoulish media permit it . then we will see a change in mood in the economy.

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Leaders of the world's 20 richest countries will meet in London in April. You would think that in the current circumstances they would bring the meeting forward by a month? What else are they doing that is more important?

The G20 leaders may not be able to wave a wand over the recession but they can lessen its grip and shorten its duration with a number of monetary and fiscal interventions. Many of these are already in play though they have not yet taken effect.

Above all the governments need to be taking decisive action communicating it exceptionally well and look like they believe it. If they don't believe it then why are they doing? In truth, these uncharted waters demand of a level of decisiveness and even risk taking that is alien to the risk averse leaders of governments. The public is looking to them to provide the leadership of strength and confidence. The leaders must engage vigorously with the public. Obama has done it but Brown is languishing in the polls as punishment for being seen to be too remote.

Then genuine green shoots will appear and the tide will be turned by the positive side of our psychology. We will all believe that there is a future where our investments in human creativity and ingenuity will have a positive pay back to society and generate wealth for all.

This belief and its benefits are available to everyone far sooner than is realised and this belief will be the final making of the recovery. Bring it on.

Stephen Archer

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