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At the end of the beginning, still a long way to go

By John Wright

A huge amount of debate is raging in the West at the moment, largely driven by our political 'friends', as to what phase we are in this current recession. My own view is that we are probably at the 'end of the beginning' but we have a long way to go! I suspect we will be bumping along the bottom for the next couple of years with almost negligible levels of GDP growth. The level of indebtedness at the government and personal levels will be a huge millstone round our necks until this is put back into balance.

As for the business environment in the West and in many Gulf countries, companies who successfully addressed their cost bases during 2008 and created structures that reflected the current realities, have in all probability avoided what I call the 'death spiral' and are now continuing to trade, but with significantly lower or even marginal profitability. There are of course notable exceptions, but generally I believe this is the norm.

As we experienced in the early 1980s, I suspect we will find that well into the so called 'recovery phase' and we will continue to see a series of company failures. These will be firms that did not really address their costs aggressively in 2008 and have been cutting gradually through the balance of the downturn. In many cases this strategy will be found wanting. Therefore, even though you have reached what is probably a sustainable level, finance directors need to be extremely vigilant about the quality of receivables over the coming couple of years, especially where credit insurance has been all but withdrawn.

This is a time when companies require more than ever the support and empathy of their bankers. This, I'm afraid, appears to be in very short supply! Risk managers in the banks are on the ascendancy as the banks run like mad to rebuild their balance sheets and try to regain at least a modicum of market confidence. As a result, decision making is extremely slow for existing customers, who have viable business models; a snails' pace for any new proposals and the rush to exit from businesses that appear to be on the cusp. Not much sympathy here!

Breaches of terms and conditions are punished brutally and re-pricing is the order of the day. Substantial 'facility fees' of various types have been imposed for no apparent reason on a 'take it or leave it' basis. The customers have no practical option but to accept this treatment. In many countries the personal banking segments are much the same with consumers paying the price for the bankers sins of the past. The simmering resentment that this is causing is hard to overstate. There is no doubt that when things eventually do return to normal the banks will have a heavy price to pay in terms of their customer relationships and the willingness of customers to continue to do business with them. Clearly anything that impacts negatively on the long-term customer relationship has a direct impact on the banks' profitability going forward and the bank managements and market analysts should think carefully about this.

The staff in the banks are just afraid of making poor decisions, there is a huge bureaucracy around any form of a lending decision and there are certainly no prizes for 'enterprise'. However, strong risk management will be recognised!

The worry is that this 'risk-averse' culture will be embedded in these institutions and any move back to the middle ground will be slow. No bad thing, one might argue, but a massive change for customers from only two years back: the customers are paying through the nose.

Looking out through the 'front of the bus' one has to feel that the process of unwinding, recognising and then providing for 'business as usual' bad and doubtful debts is ongoing in the banks. With the levels of unemployment in many countries likely to continue to rise through 2010, the banks' problems with credit quality are likely to persist. Unemployment statistics do not consider the hundreds of thousands of individuals, who have accepted salary cuts or have been placed on short time working.

What are the answers for the customers? No matter how uncomfortable and distasteful they might feel about it, they must get as close as they can to their lenders whether or not in the business or the personal sectors and make sure that even if the lender is not at all interested in a 'relationship', we are. The banks on the downside are as disinterested in relationship banking as they are on the upside!

So, the 'end of the beginning'? Yes. We have reached a level but the road back will be, I'm afraid, long and bumpy.

Qatar has been fortunate as the country's revenue streams have been robust. It has allowed the authorities to deal effectively with difficulties experienced by the banks in their property and investment portfolios. While this has been helpful, it will, I suspect, take the banks and companies some considerable time to return to 'business as usual'. In addition, the sharply lower levels of inflation may very well force banks to consider carefully their costs bases and the underlying profitability.