CREDIT MATTERS

If You Don't Manage Risk, Risk Manages You.

WILL AUSTRALIA'S RECESSION BE WORSE THAN IT HAD TO BE?

By Kim Radok – December 2020
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INTRODUCTION

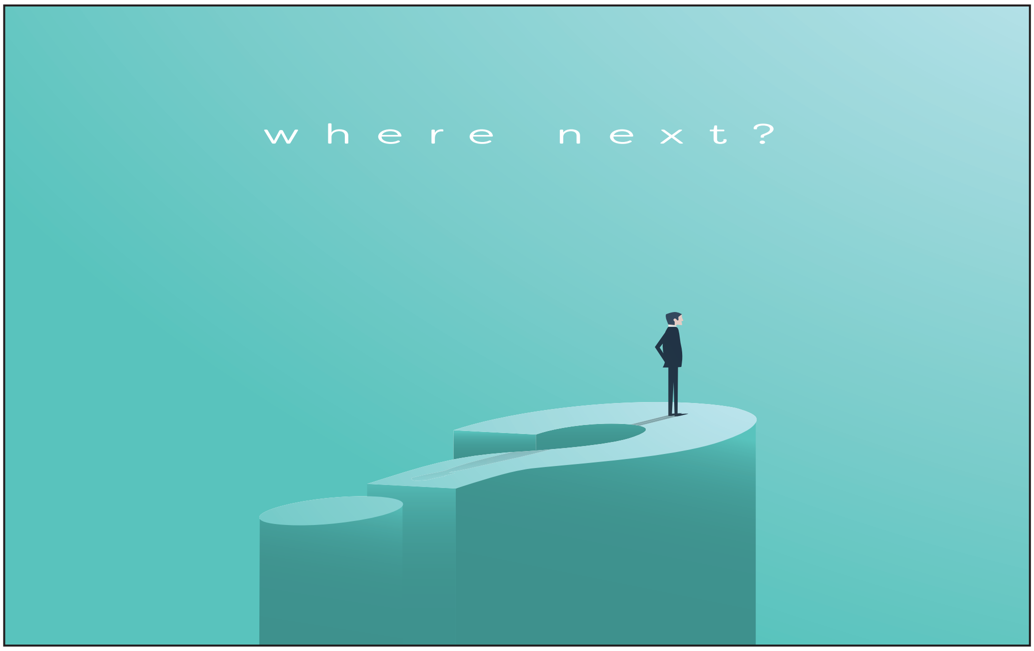
All recessions are damaging, although some are more than others. The differences between the amount of damage and ability to recover, will vary between recessions. For instance, with the current recession, Government support and interventions should minimise damage to a degree. However, it is the inappropriate actions of other parties which may negate many of the benefits provided. Consequently, this recession is likely to be more damaging than it might otherwise be, because of these other inappropriate actions.

This feature will put forward the key factors which I believe will make this recession worse than it should be. There is no doubt that the COVID19 virus is one of the main factors triggering this recession. The pandemic however, was "… only the final straw, which broke the camel's back." The pandemic, like the irresponsible lending which led to the Global Financial Crises (GFC), or the stock market crash of 1929, was only the final event which brought to light the fragility of the economic climate of that time.

In fact, we had been building up to this recession for a number of years. Unlike other recessions, we had an earlier opportunity to see and learn from the last business downturn; the GFC. Regrettably however, few people learnt the lessons of that downturn and therefore this recession will be worse than it has to be.

By reviewing and then acting on the information in this feature and related features by other commentators with a similar focus, you may be able to initiate actions to minimise the potential damage to your business and family affairs. Afterall, not all you see or read in the media may be what is actually happening around you, in your own business and family environments.

It must also never be forgotten, that in a recession, a large portion of the community will still be able to survive, although perhaps not perfectly as in the past. Furthermore, amongst all the losses that will occur as a result of this recession, there will also be opportunities to prosper and grow the wealth and security of your business and family. To take advantage of these opportunities however, you need to keep an open mind, your financial and emotional resources in check and study what is actually happening around you.



THE KEY FACTORS

The Business Community - and Their Lack of Pre-Recession Preparation

An astounding feature of this recession, was the lack of foresight by so many in business who should have known better. It is not as though there were not a number of indicators leading up to it. After all, there were the precedents from history, the warning thoughts of respected businesspeople and commentators, and a ready-made learning exercise of the GFC.

The evidence of a lack of foresight is seen with the demise of those businesses which could not survive even the first three months after the arrival of the pandemic. The common theme of these businesses was that many were built:

i. on inappropriate levels of debt; and/or

ii. without good business disciplines and risk management strategies; and/or

iii. with a lack of financial reserves and resources; and/or

iv. with overinflated asset values supporting their perceived value and borrowings; and/or

v. insufficient cashflow.

We must also not forget, that there had been substantial financial support measures from Governments, and still these businesses were too financially exposed to survive.

It is obvious, few lessons have been learnt from all previous recessions, which will only magnify the effects of this recession.

Strategies to Survive and Grow during this Recession

Despite the obvious damage to our business community and supporting reports of these damages in the media, there are still many businesspeople who are failing to accept the recession is upon us. Due to this lack of acceptance, we see that they are failing to act differently. Maybe, it's simply lacking awareness of appropriate action(s) which they could take. Alternatively, perhaps they believe the negative effects of this recession will be easily negated when people return to work and the pent-up spending demand will return profitability and cashflow to normal.

Worse still, many businesspeople who do accept the recession, are acting in panic mode. As a consequence, their actions are impacting negatively on the ability of their business to survive. Typically, you will see:

1. few businesses changing their activities to protect, and/or restore their financial and customer service reputations;
2. management placing ever increasing demands on their employees to sell and achieve pre-recession profits; and as a result,
3. incur increased costs and bad debt write-offs to customers with a history of doubtful payment integrity and fraudsters;
4. increased processing errors when raising invoices which provide customers the opportunity to slow down payments;
5. the increasing lack of quality of customer and operating information in the company's data bases and records;
6. the continued lack of respect for accounts payable and receivable employees by denying them adequate resources to do their work efficiently and correctly; because
7. management demands extra information as the focus on cashflow increases, in an attempt to protect their own reputations, even if these demands destroy productivity; etc.

As most mature aged businesspeople know, without a good reputation, cashflow and profits, few businesses survive for long. In a recession, without these factors, surviving is made even harder.

Employing People

One of the key factors in minimizing the negative effects of the recession is by ensuring you have good employees. When you look at the costs of employing people these days, you wonder why, or how, small businesses can afford to employ anybody.

When we understand the regulations under which a business employs people, it appears the entrepreneur or small business owner should be grateful to have anybody work for them at all. Furthermore, it appears that the entrepreneur or small business owner should also be beholden to the government if they are able to earn a profit. It appears, earning a profit is just immoral!

It appears the entrepreneur or small business owner in Australia is just a target to be milked at every opportunity to satisfy the needs of society. A brief review of factors which are lined up against them incudes:

Governments

1. governments like businesspeople to employ people, because it reduces the numbers of people on welfare by converting welfare recipients to income tax payers;

2. when businesses employ people, the government also benefits because of reduced future pension payments, as the business owner is also expected to pay potentially an additional 12 percent superannuation levy, on top of their employees' wages;

3. meanwhile, other governments, e.g., state and local, can charge yet another "regulatory", or "user fee" for any expansionary thoughts or needs;

4. if a business employs enough people, a state government can charge an employee tax;

5. award structures which are so complex, that they cause problems for even the largest and most sophisticated businesses with professional HR support and computer programs;

6. if a business does put their hand up for an innocent mistake, they are vilified and penalised even more.

Employees

1. Due to society's expectations, employees expect a job with ever-more benefits.
2. Employees also demand endless time off for personal needs, and any other excuse at the expense of the business.
3. Businesses are expected to provide for their employees' future superannuation and retirement needs.
4. Employees seem to have all rights to sue at no cost to themselves, irrespective of merit on any and all perceived wrong doing.

Fair Work Australia

This organisation is supposed to be a neutral body designed to help employees with awards structures, unfair dismissal claims, and dispute resolution schemes. It is a worthy objective to help the disadvantaged and those without the means to protect and maintain their rights.

Unfortunately, all too often, we see results that do not appear to reflect the “neutrality factor” on behalf of business owners. For instance, often an employee’s antisocial, derogatory language and public statements, which are borderline defamatory, or dangerous behaviour, are ruled as “understandable”. Apparently, the employee’s behaviour is acceptable in the workplace under any given circumstances, based on many of the decisions made by Fair Work Australia.

Meanwhile, similar behaviour in the general community would not be tolerated and quickly called out for what it is by the media.

Unions

Unions unfortunately, are often all tarred with the same image, negative, unhelpful and anti-business. Many unions seem to be obstructionist, combative and still stuck in the ideology of the past, where all capitalism is bad and all workers are victims. To some degree, in certain industries unions are essential to support workers’ rights and reasonable needs.

Other unions appear to be willing to negotiate and understand the company’s position to be viable and make a profit. Furthermore, they understand there are different types of business ownership. Despite the willingness of responsible unions to work with the business community, they are also tarred with the bad label of the more militant union types.

I suggest however, there are unions at the moment, which are not doing their members, nor the image of the union movement many favours. In an effort to support their members rights, they appear to not realise that we are in a RECESSION which is going to last many years. In a recession, there is often no “additional money” to pay for unrealistic “member’s entitlements”, existing, or futuristic. Nowhere is this factor of more critical importance than in the small business community.

As we know, the world keeps changing and yesterday's employee rights, can be tomorrow's penalty for employing people.

It is a bit hard to fight for members' rights, when doing so eliminates profits and forces a business to close. Alternatively, if a business has moved to automation and different methods of production, there may be fewer jobs for union members. Whether the unions like it or not, there is a new norm. To remain relevant, unions must find ways to ditch yesterday's ideology and admit different types of businesses have different factors of operation and self-survival.

At the end of the day, if an entrepreneur or small business owner in Australia, cannot make a profit to justify their investment and the risks they take, there are three possibilities:

1. reduce the size of their business and workforce, and/or
2. demand more productivity from their existing workforce, and/or
3. close down and become employees or welfare beneficiaries themselves.

The RBA (Reserve Bank of Australia)

The actions of the RBA and its fellow central banks around the world, are in part contributing to the size of this recession and why it will be more damaging than it needs to be. It is as though they have forgotten or ignored, The Law of Unintended Consequences, in their rush to help economies recover from downturns and recessions.

One excellent example of unintended consequences is seen in the ongoing story of two banks. For instance, here in Australia, the RBA is saying debt is good. Meanwhile, the retail banks are often saying, "… no security, no borrowing!"

It's most apparent the retail banks see a very different world to that seen by the RBA.

Below are a few examples, in brief, of the issues currently confronting the RBA.

Break-even Interest Rate and Future Consequences

It appears from my limited research, there have been no discussions or studies on what is a break-even interest rate. In other words, reducing interest rates down to a certain level may be beneficial to the economy. However, when interest rates are reduced to a certain level, the economy starts to retract with negative consequences. Afterall, we are now seeing where low interest rates causes as many, yet different, problems to that caused by high interest rates.

As history shows; (i) low and negative interest rates haven't worked or achieved the desired results intended by any central bank, (ii) every interest rate announced below a certain level, sends a message that the economy is in trouble, and (iii) people responding in ways not intended by the central bankers, such as:

1. frightened people, or those who perceive the economy is in trouble, reduce spending, or save, or pay off debt;

2. those who have reduced investment income, are now unable to spend as before, because, well, they no longer have the income;

3. wise people saving their cash to buy cheaper later and/or take up wonderful opportunities not currently available;

4. other people who stop spending due to their changed perceptions of the future and income, who also stop or reduce their discretionary spending; or in turn,

5. stop spending because they realise, there is more to life than spending money on unnecessary material items:

Meanwhile, people lacking any form of foresight or understanding of the consequences, keep spending and/or borrowing. Many are without any real means of paying the debt back, and in times of desperation, they effectively commit fraud to survive. We know from studies in the field of criminology, good people, as well as a bad, will commit fraud to survive in tough times. Put another way, "desperate people will do desperate things to survive."

In addition, we know people who should not borrow are encouraged to borrow and many will have negative consequences which will include:

1. people who are buying their homes now because of a cheap interest rate, may later lose their homes and credit rating when they lose their jobs;

2. becoming addicted and/or over committed to debt and when they cannot borrow at the cheapest rate, will go to more expensive borrowing sources, which means

3. their spending is reduced as any extra money goes on paying the higher rate, or on slow payment penalties; and in time

4. some of these borrowers, when they cannot borrow via regulated financial sources, will resort to criminals for their needs, and as we know

5. the penalties for not repaying loans from criminals, typically ARE NOT just the normal financial penalties, and can often necessitate the use of your Medicare card...

In addition, there is very little information from the RBA and their other central bank associates on the future consequences of their actions today. For example, what happens if people no longer save because bank charges and negative interest rates start to reduce their savings? Where will the cash and asset reserves come from to bail out the economy next time there is a downturn?

What we do see from central bankers is a great disconnect from their citizens and the economies which they claim to protect. A perfect example are the numbers of bank notes circling in each country's economy that nobody can account for! It is said in Australia alone, there are many millions of notes which seem to have been withdrawn from the economy. Is it, as one former Prime Minister said famously, "hidden under mattresses" because few people trust the authorities? Alternatively, is it also one of the reasons for the rise and rise of cryptocurrencies?

Currently, all we seem to read and hear from central bankers are more theories for the future based on their book learning and actions proposed by fellow associates. Meanwhile, the majority of citizens, such as pensioners, savers, unsophisticated investors, parents trying to teach their children positive life skills, etc., are ignored.

What we are not hearing from the central bankers, is how their current thoughts and actions will impact in the future based on research in the aftermath of previous recessions and business downturns. For instance, do central bankers even reflect or understand how their policies and actions will affect themselves and their families in the future?

Probably the most dangerous message currently espoused from central bankers is that; "... debt is good and savings are bad!" I cannot think of a more dangerous message which could be promoted by a responsible body.

Low or Negative Interest Rates – Further Negative Consequences

The evidence is that low and negative interest rate strategies have not worked for over 20 years. In fact, the latest results as reported in the media, show that bank deposits are increasing at an exponential rate and borrowings are being repaid where possible. This is despite central bankers' theory; saving is bad for the economy and going into debt is good.

Now let us assume that the strategies of low or negative interest rates work in the short-term. What are the likely repercussions in the medium and long term?

1. A world awash with debt; and as a result

2. little savings to help people and businesses survive in bad times, or to take advantage of profitable opportunities without going further into debt;

3. risky investment strategies by desperate people trying to survive on their savings and losing their funds to scam artists and fraudsters; which means

4. essential funds which might have been used to buy genuine products and services is lost to the general economy;

5. the vain attempt by grandparents, parents, trusted elders and professionals to convince younger generations to save; because after all,

6. how do you convince young people that savings are essential in life when they see the majority of any monies saved, disappearing due to negative interest rates and bank charges; and as result,

7. banks lose access to free or low-cost funds, which in turn

8. means the cheapest and safest forms of borrowings from the banks, will become even more expensive;

9. the creation of asset bubbles which will inevitably burst at some time in the future; and

10. the potential damage to the younger generations who are being encouraged to go into debt, in a time when job, cashflow, business volatility and uncertainty are the norm; etc

We are now living in a time of unbridled debt advancement where uncertainty is the dominate factor. In addition, the attack on savings means there will be less savings available in the future to cover forthcoming requirements.

We have also seen the disconnect between central bankers and the general public in response to central bankers' actions, with many people not responding as desired.

Flawed Spending and Investment Recovery Strategies

At the moment, as lock-downs are being lifted and some freedoms returned, the call has gone out to spend ever more money. It does not matter even if that means going further into debt. A portion of this money will be spent and will be of benefit to the Australian economy and community immediately. However, a great deal of that money spent, will be wasted on flawed strategies.

The reason for these flawed strategies is based on yesterday's thinking and believing it will bring yesterday's results. Our world has changed with life experiences, thinking and situations changing dramatically. The effects of these changes will therefore remain with many people for some time, years in fact, not just months.

After all, this recession is far worse than the

GFC. It took many years for people who lost out in that period to recover. There are many people talking about the fact we are in for a decade-long recovery period, with the economy changed in so many ways.

Therefore, amongst the many flawed strategies, well intentioned as they are, means perhaps the following spending initiatives need to be reconsidered. For instance, spending on road infrastructure around capital cities, trying to rebuild vibrant cities too quickly, encouraging people to spend again on endless and unnecessary consumer goods and experiences, may not offer the returns the new economy needs to grow quickly.

Major Cities

The fact is people are leaving the cities because they don't have to work there anymore. Employers will be reluctant to force their employees back into the city on a daily basis for work and we know already, employees no longer want to commute to work on a daily basis. This is in the face of the desperate city-based business owners saying workers must return to the city, if their businesses are to survive.

Overseas tourists and students will not return for some time and local visitors will be busy living different lives. These people will only visit the cities when absolutely necessary, or for special occasions.

What about major events, (sporting, artistic etc.) and conferences which are not proceeding? We also know that even if these events do take place, they have vastly reduced attendances. Many established annual events are still being cancelled, or conducted via on-line and digital methodologies. How many of these events will take place in 2021 even if a vaccine is produced and delivered?

When you quantify the workforce and lack of people that will not return to commuting to the cities on a regular basis, it is obvious that foot-traffic will be reduced. This reduction will subsequently have a negative impact on business opportunities within the cities. Therefore, throwing money at projects within the major cities where foot-traffic and dollars spent will be reduced, doesn't make much sense at this time.

Where is the Money Coming From?

Once the pent-up demand, plus the first flush of money is spent in the lead up to Christmas, there will be limited funds available for discretionary spending. The sad truth is that many people are going to lose their jobs, businesses close down and mental health issues increase, as government assistance payments are reduced and debts must be repaid.

Consequently, city councils will have less income to maintain their city. Once cities lose their vibrancy, the lack of workers, overseas students, coupled with the sad look of empty shops, maintenance will be reduced and “the grand look” of the city will diminish.

Infrastructure Projects

Building better road infrastructure into and around major cities sounds good. The problem is; fewer people will be employed and want to live in cities, especially once they have tasted a new lifestyle without commuting. These projects are also not ready for immediate action and any benefit is some years away. Furthermore, a lot of the money will be dedicated to fixing problems already exposed, and therefore, will be of little value in creating new jobs outside the road construction industry in major city areas.

Meanwhile, if spending on increased resources of already known and ready to go projects such as fast rail between regions and interstate cities, and smaller infrastructure projects in regional areas, might be more beneficial. After all, this is where many people, families and businesses are relocating to live and work.

These projects in turn, would employ more people and with the increased flow on of beneficial effects, create even more business opportunities throughout the state. Before the pandemic, one of the biggest impediments for people moving to regional areas was the lack of infrastructure like hospitals, nursing homes, medical professionals, etc.

The right type of strategic thinking and understanding how technology can be used effectively, is essential. After all, when technology does not currently add value, and therefore inhibits growth, its inappropriate use will prevent moving forward as quickly as desired. As an example, what type of hospital, or aged-care services are really required in regional Australia?

In summary, if the governments of all persuasions and sizes really want to get a decent and quick return on their investments, and for their citizens, they will need different spending objectives than those previously considered of worth. Based on recent announcements from some Governments, this thinking has not got through to the decision makers.

SOCIATAL SANCTIONED FRAUD

In recent years, debt collectors, consumer finance providers and even B2B credit providers, have noticed an acceptance, (by people who should know better) to sanction fraud by debtors.

Today, although well intentioned, processes exist via legislation, the courts, mediation and the introduction of consumer support services, to protect "innocent debtors". Now, unfortunately, we often see the credit provider is no longer the enemy of "innocent debtors". They are now the victim of society sanctioned fraud because of new debtor protection strategies introduced by supposedly well-intentioned people.

We all know that there are innocent debtors who have become the victim of scandalous and unprincipled sales people and activities from normal business enterprises. In these situations, there is no problem, there should be protection for the innocent and penalties for the guilty. Furthermore, there are times, where unfortunately legislation is required to force creditors to make some allowances for short-term problems of debtors, or for catastrophic events which are out of the normal. In such cases, creditors were recognised as being unable to see common sense, or that being lenient as actually a good commercial decision.

The real problem is that there seems to be a lack of understanding of personal and commercial responsibilities by the "do-gooders" of society, the courts and financial counsellors. As a result, we see the pendulum has swung the other way, and now genuine and honest credit providers, or debt collectors, are supposed to accept all claims and penalties for "harassment and unconscionable lending."

We also see the rather deplorable situation where a number of parties are seeking, (and encouraging) victims of "harassment and unconscionable lending" to take action against credit providers, irrespective of whether their cases are genuine or not.

We are also seeing calls from respected bodies which are now wanting to make it easier for bankrupts to borrow again. It is all well-meaning, especially as it is government behaviour, which caused so many insolvencies and bankruptcies in the first place. But how do you tell the difference between:

1. those people who are genuine cases; verses
2. the incompetents who operated zombie businesses, or ripped off their suppliers and employees; verses
3. the criminals and fraudsters?

Irrespective of why businesses became insolvent, or people bankrupt, credit providers will still be reluctant to grant these parties credit, let alone at the cheapest market rates. Again, this is another impediment to a faster recovery of the economy.

WHO CAN WE TRUST ANYMORE?

One of the saddest aspects we are currently seeing, is the loss of trust in what were formerly trusted people and institutions. It appears that, particularly during difficult times, the true nature of people comes to the fore. In the good times, the worst of actions by the unscrupulous can be hidden and/or considered to have a negligible impact. Now, in the tough times, we see people under pressure unveiling their true selves, for what and who they really are, along with those businesses and institutions in which they work.

In 2020, we have seen several "trusted" organisations and business people which were previously held in high regard, that have betrayed the trust of the general public. Here are a few examples.

Central bankers

1. making unpopular decisions which are opposed by other bankers, pensioners, savers, self-funded retirees; and
2. despite there not being any evidence that their strategies are working, but in actual fact are causing more damage; and most dangerously
3. actively promoting debt as good and savings as bad.

Banks

1. not lending without security;
2. slow to lend to small business;
3. paying very low interest rates for savings:

Politicians

1. playing with people lives, careers and businesses because of politics and lacking any true compassion for those in most need of it;

2. having given themselves and /or the senior bureaucrats pay rises, then announcing their employees and frontline carers who risked the most and worked diligently during extreme uncertainty throughout the pandemic, a wage freeze.

Government bureaucrats

Unelected bureaucrats playing politics, giving themselves pay rises and seemingly lacking any semblance of responsibility, or common sense.

Business people and their businesses

There are a number of businesses which are accepting government handouts whilst retrenching their employees, and/or withholding payments to their creditors and suppliers, and/or, proudly announcing senior management bonuses.

With growing distrust between the above groups and the general public, the civil and commercial environments become ever more volatile and unpredictable. The word of authorities and former respected parties is rightfully less respected than ever before.

IN SUMMARY

All recessions are damaging, although some worse than others. The differences between the scale of damage and ability to recover will vary between the recessions. For instance with the current recession, Government support and interventions will minimise damage to a degree. However, it is the actions of other parties which may negate many of the relief/benefits provided by Government support - and make this recession more damaging than it otherwise should have been.

This feature has put forward the key factors which will make this recession worse than it should have been. There is no doubt that the COVID19 virus is one of the main factors of this recession. The pandemic however, was "… only the final straw, which broke the camel's back." The pandemic, like the irresponsible lending which lead to the GFC, or the stock market crash of 1929, was merely the final event which brought to light, the already failing economic climate at the time.

In fact, we had been building toward a recession for a number of years. Unlike other recessions, we had an earlier opportunity to see and learn from the last business downturn; the GFC. Regrettably however, few people learnt lessons from that downturn. You can also add the factors presented in this feature, which suggest unfortunately, that this recession will be far worse than it had to be.

It is by reviewing and then acting on the information in this feature and other similar features, that you may still be able to initiate actions to minimise the potential damage to your business and family affairs. Afterall, not all you see or read in the media may be what is actually happening around you, in your own business and family environments.

It must also never be forgotten, that in a recession, a large portion of the community will still be able to survive, albeit at a reduced rate. Furthermore, amongst all the losses that will occur as a result of this recession, there will also be opportunities to prosper and grow the wealth and security of your business and family. To take advantage of these opportunities however, you need to keep an open mind, your financial and emotional resources in check and study what is actually happening around you.

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