

CEOs showing more humility

By Colin Read, Everybody's Business

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— Until recently, the North Country had at least partially escaped the widespread foreclosures and layoffs experienced elsewhere. Now we are starting to hear of layoffs and hiring freezes from our biggest North Country employers.

Ours is an export region. Exporters are experiencing a double whammy as a consequence of the meltdown of our stock markets. Such market sell-offs induce investors to sell their stocks and convert back to cash. Believe it or not, people are so disinterested in the market that they are willing to buy government bonds offering a zero interest rate. They can choose to keep their money under their mattress at a zero interest rate, or give it to the government for safekeeping.

This movement from stocks to cash or to U.S. treasury bonds has caused some currencies to rise. As Japanese investors take their money out of stocks from China or elsewhere, they must convert their savings from foreign currencies back to Japanese yen. This increased demand for yen has raised its value.

And as investors worldwide flee markets and look for safe havens to park their life savings, they often buy U.S. bonds, considered the safest of all. This means they must convert their savings to U.S. dollars, also creating more demand for the greenback and raising its value too.

These flights to safe havens that strengthen our currency have the unfortunate effect of damaging the export competitiveness of the U.S. and Japan. Unfortunately, it had been the weak U.S. dollar that had been a rare morsel of good economic news this past year for our region so dependent on the movement of trade goods.

We all remain dependent on the strength of the stock market. I am not optimistic that the market will come back soon. Rather, the indications are that we will move into a significant recession, especially given the failure of government to stay ahead of Wall Street. Still, I am optimistic that we will learn something from all this. And I am gratified that the meltdown is now receiving the focused political attention it needs.

The first indications of a positive lasting legacy has been the transformation of the archetypal financier or CEO. Once they walked with a swagger like Michael Douglas playing Gordon Gekko in the movie Wall Street. Now they appear before Congressional hearings with regret and contrition. Perhaps they still swagger in their board rooms. But they don't in hearing rooms any more.

For instance, Edward Liddy, the new CEO of AIG, appeared before Congress to explain why the company recently paid for fox- and bird-hunting junkets to England and luxury resort trips in Arizona. Rather than cover up or minimize these affronts by a company that is now partially owned by taxpayers, he sincerely apologized for these insensitivities and excesses, and promised to turn the ship around.

And we had automaking CEOs flying down to Washington in corporate jets, stylish hat in hand. By round two of their bailout campaign, they at least figured out it might look a little better if they drive down.

Even Alan Greenspan, the Maestro of Monetary Policy, has now become the Apologizer for the Financial Apocalypse. He admitted he had a lifelong love affair with free markets, but has recently come to realize that free markets are an attractive but illusory ideal.

His new found realization comes from a couple of insights. First, it is ridiculous to assume that complex financial markets peddling even more complex instruments act in the same way as the local farmers market. Competition relies on free and transparent information that can readily be digested. By this measure, financial markets are anything but competitive.

Greenspan also realized that the traditional valuation of the market, or of housing for that matter, is tragically mistaken. We came to assume that the recent past was the best predictor of the price, return and risk in financial markets. We looked at the data, focused on the good, and rejected the bad as anomalies. For instance, we focused on housing or stock-market risks and run ups following the end of the last recession. We should have included the last recessionary experience in the data. They are not anomalies, but are regular reactions to irregular growth. Of course, we also assumed a depression could never happen again, presumably because regulators and the Federal Reserve would not let things get out of hand. Or so we thought.

I was in a workshop with a former Fortune 500 CEO in New York the other day. He described how he once questioned the analysis of some of his finance people. They were showing him how much his company would make if housing prices went up by 5 percent, or 10 percent or 15 percent. He asked how much they would make if housing prices went down. They at first looked puzzled, and then told him that such a scenario is not in their model because prices never go down.

Well, we all were let down. The credit crisis began in mid 2007, and there were serious, even calamitous, shots across the economic bow in January and February of this year. In a year's time, the stock market dropped by almost half, and housing prices plunged by 25 percent or more in many areas. Financial commentators consider it good news if the stock market falls by only 300 points in a single day.

The good news is that we now have the attention of policymakers and CEOs alike. We even have some CEOs volunteering to take pay cuts, something that would have been unimaginable a year ago.

I believe all this is a good thing. Once the defensiveness is gone, we can get down to figuring out how this happened and how to prevent this, and any other such catastrophe, from happening again. We should continue to bear witness to this process. By firmly imprinting Crash II in our memory, just as we collectively did during the Watergate Trials, the Great Crash or the Great Depression, we will send the clear message that everyone is watching -- finally.

Now, if only we can ensure that our children choose to grow up to work hard and produce, rather than live high by wheeling and dealing as hedge-fund managers. If we can get back to the principle that all things good flow from invention and perspiration, we will recover our position as the bastion of creativity and innovation throughout the world.

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