

Reference 2009/146
Date 6 May 2009

RESTORING CONFIDENCE IN MARKETS

ABI – speech by Business Secretary Lord Mandelson

I want to take my cue for today from the title of your conference and say something not just about financial markets regulation and about how we restore stability and confidence in markets generally, but also how we restore greater confidence in our economy as a whole.

Restoring confidence in markets

The last year has seen stability and confidence in short supply, not surprising given the shock the system has received. It is easy to forget how completely the economy, and the financial sector in particular, depends on confidence until that confidence evaporates. As a result of the crisis in the banks, confidence was removed as if the power supply to the economy had been switched off.

I don't just mean confidence in the bullish sense. But confidence in asset values, in balance sheets and disclosed liabilities, in our understanding of the risks we take.

Up to now, the Government has focused all its efforts on containing the damage of the credit crunch and the recession, getting the power supply restored as quickly as possible to all parts of the economy.

We've used the bank recapitalisation, the Credit Guarantee Scheme and the Asset Protection Scheme to address the underlying problems of toxic assets and bad debt.

The Government's successful Enterprise Finance Guarantee and the £5billion trade credit facility we launched at the Budget each counter a contraction in lender confidence in viable businesses in the economy.

And the VAT cut and investment package in last autumn's Pre-Budget Report both acted directly on the level of confidence and demand in the economy, as many independent analysts are now recording.

One of the slightly exaggerated debates in the run up to the G20 Summit in April revolved around whether it should focus on long or short term measures. Stimulus or a regulatory package for global finance. Recovery or rebalancing.

The reality is that it was required to do, and did, both. As well as advancing a global stimulus, and expanding international financing machinery, and promising to do all its takes to get back to trend growth, the G20 set out a clear agenda for global reform, including the creation of the Financial Stability Board and agreement to work on a global approach to financial service regulation.

This was and remains a huge step forward in strengthening the multilateral financial order, and Britain can take great satisfaction in driving the agenda forward.

Financial markets regulation

That work has been further advanced by the Turner and de Larosiere reports. These contain important steps on the road to rebuilding confidence in the financial services sector by showing we can address the problem of risk at the various levels of products, institutions and the financial system itself.

We can't remove risk from financial markets, or from the economy all together. Nor should we want to. All innovation involves risk. Most investment involves risk.

But excessive risk, or badly understood risk is obviously a problem. And where risk can play out across the wider economy it has to be managed.

So too does national financial regulation everywhere that has been outpaced by the increasingly global nature of global finance. It is this phenomenon, rather than who was asleep on the watch, when, which is central to the lessons to be learned from what went wrong. Which is why the G20 and European dimensions of this process are so important.

As Stephen Haddrill argued in the FT yesterday, a global approach to accounting and financial markets rules is now required. As Stephen put it, regulators need to be speaking a 'single language', because the markets now are.

The details of how we address these problems remains work in progress and is going to keep the Treasury busy for a little while yet. Harmonisation requires us to overcome all kinds of political and bureaucratic insularity – take it from someone who worked in the European Commission for four years.

But it is clear that we will need to look at capital requirements so that they are countercyclical where they need to be and reflect the kind of risk an institution is taking on.

We need new rules on what borrowing belongs on and off the balance sheet. And greater transparency for derivatives.

We also need rules that ensure that the dangerous levels of leverage that characterised the balance sheets of some institutions two years ago are not repeated.

As the Chancellor set out in his formal response to the de Larosiere report, the UK strongly agrees that there is now a need for a single set of EU rules for the financial services sector, even if we think, like others, that those rules should continue to be policed by national regulators.

As I saw all too clearly from within the Commission until my departure last year, we also need agreed rules on how we handle the liabilities of cross border banks.

All these issues are vitally important for us in Britain to see resolved because our financial services sector remains a hugely important part of the UK's industrial mix and a key advantage for Britain, internationally.

The City is one of our most successful and innovative clusters. It will remain so. But its competitiveness is ultimately inseparable from its ability to deal with risk and responsibility. And from the markets confidence in that.

The credit crunch was a professional wake up call for the banking and financial services industry.

To their approach to risk, and to the incentives that drive people to take those risks. To the culture of responsibility and professional challenge that needs to exist in these institutions.

This is not a sector that is shy about talking about the talent and incentives that make it work. Our expectations should match that, regardless of whether there is public money invested in these institutions or not.

Ultimately we all need to make sure that the financial services sector remains what it must be, which is the irreplaceable facilitator and backbone of the real economy.

That it is never again allowed, either because of flawed regulation or poor management, to become a liability for that real economy.

Restoring confidence in the future

And it is on the subject of the rest of the economy that I want to finish, by saying something about the wider confidence we must retain in Britain's economic future.

We will neither exit the recession as quickly as we can, nor build the future strength we need, if we allow pessimism to descend on us or lower our expectations of what we can achieve.

We seem to be seeing a deliberate political or media ploy to move us from recognising how severe and painful the present recession is, to believing that we can never recover or be as strong again. That, indeed, the country is being run into the ground.

This attempt to make us feel worse about ourselves may have an understandable electoral motivation. But its effect, if we are not careful, will be felt beyond politics.

If insecurity breeds economic hopelessness, we risk cutting ourselves off from the economic opportunities and growth markets the world economy offers us.

Sapping our nation's will to succeed won't help us win in global markets.

This matters because Britain trades with a global economy that is going to double in size in the next decades, driven by the growing, prosperous middle classes of the emerging world.

Many of the big commercial opportunities in this century will be in new multifunctional technologies in which we can excel.

Low carbon vehicles, lightweight building materials, biotechnology, renewable energy, next generation broadband, advanced technologies like plastic electronics.

Twenty years from now these things will have redefined everything we make.

The question is: what will be Britain's share in this reshaping of the technological and economic landscape? Where will our firms and our workers fit into these global supply chains? What will the role of government be in helping us get there where our potential is constrained or blocked? These seem to me to be the real questions we face.

What we know for sure is that these opportunities are not going to fall into our lap. We have to work for them. Our capacity to commercialise new technologies, to produce workers with the skills we need, and to ensure that viable and innovative firms don't fail to grow for lack of finance, will all be decisive.

It's not ideology but common sense to say that there is a role for government in closing these gaps where the market will not.

In the 'New Industry New Jobs' policy framework the Government published two weeks ago, we set out how a smarter and more strategic approach from government can help us identify and unlock this potential.

As a country we're always a bit uncomfortable with the language of national endeavour. But that is what this has to be. There is no greater social or political priority for the years ahead than doing what we can to unlock the power of business and enterprise to drive our return to growth.

That's why, to get through the present recession, the only way back to sustainable growth is by continued investment in the competitive foundations of our economy: our skills, our infrastructure, our science and our ability to innovate.

This does not mean being oblivious to the implications for the national finances. We know that we must deliver more from every pound in public services and be ready through further reform, to work with the best in the private sector to extract more value for money from the public sector.

We know that the sort of growth in public expenditure and employment we have seen in the last decade will not be possible in the next.

But we are rightly setting our face against the sort of retreat that marked recessions under previous administrations - Conservative and Labour – and which cut to ribbons much prized growth in schools and hospitals, as well as economic infrastructure, only having to spend more to catch up later on.

So we need to avoid talk of austerity becoming a licence to talk down the country and to cut back on our capabilities and confidence as a nation.

These will be sorely needed by businesses investing and taking risks again on the back of new market opportunities, technology drivers and innovation.

And we cannot afford the Government sitting on the sidelines of economic change rather than actively helping to pull away the barriers holding businesses back.

If we do not have confidence in ourselves, why should others? If we do not believe in our capabilities, how are we going to persuade investors to do so? This is a route to inexorable economic decline.

The decision in the Budget to raise the top tax rate has produced criticism of this country's supposed lack of commitment to enterprise and success.

Frankly, nobody likes taxes having to go up.

But the UK under this government has one of the most open business environments in the world. It has a labour market as flexible as any in Europe, and a competition regime that positively encourages new market entrants. It has a capital gains tax regime that makes the UK one of the best places in the world to make money from starting a business.

That's why, when it comes to regulatory reform, we are clear that the goal is to make financial markets work better and restore confidence in them. Not to replace them, or regulate the vitality out of them.

Conclusions: raising our expectations

My final point is a simple one. A lot of research has been done over the years about how a recession affects the basic expectations of a society.

Sometimes recession creates a sense of shared purpose. Sometimes it does the opposite, replacing the greater tolerance and optimism that often comes with economic growth with a starker and more fatalistic mindset.

A recession, in other words, is a psychological event as well as an economic one. It is an expression of our confidence to invest and spend, of our confidence in ourselves and in the future.

We have to believe in our capacity for renewal because if we give in to the sort of fatalism we are starting to hear in some quarters now, there will be no renewal.

We must not allow temporary setback to produce a poverty of vision, a lowering of our expectations of Britain's future potential in a global economy. This can only become a self-fulfilling prophecy which is why we need to reject it, and to reject it now.

So, I do not offer false optimism. I'm not naive about the challenges we face in our economy and public finances but I do reject the politics of doing nothing and peddling despondency. That is no way to lift ourselves out of recession. It is no way to embrace the future. And it is no way to put in place the conditions we need to assure our continuing economic success.

Department for Business, Enterprise & Regulatory Reform
7th Floor, 1 Victoria Street, London SW1H 0ET

Press enquiries +44 (0)20 7215 5972 | (Out of hours) +44 (0)20 7215 3234/3505 | Public enquiries +44 (0)20 7215 5000
Textphone +44 (0)20 7215 6740 (for those with hearing impairment) | Press Office fax +44 (0)20 7222 4382
www.berr.gov.uk