MacKay ON MONEY

BY FINANCIAL PLANNER CHRIS MACKAY

RECESSION? WHAT RECESSION?

Over the holiday break, I have been asking many people I have met in shops, out and about and on social occasions, how they feel about the R word, how it is affecting them and how is business in general.

Maybe we are all in denial because no-one seemed to be feeling too much pain. Although one retailer at Coastlands when I suggested he might like to give me a discount, told me "you can't be a nice guy and in business at the same time". Interesting concept!

Time will tell if we are all in for a tough old year. Business cycles come and go. After 32 years in business, I have seen it all. I wonder if our Coastlands' mate will be there in 12 months.

What is a recession anyway? The definition economists use is that it is two quarters in a row of negative growth. A recession is a period during which trade and industrial activity or prosperity in a country is reduced. How it is accurately measured, I do not know. And do they tally up all the "cashies" and underground economy transactions? What about the Trade Me deals?

I wonder if everyone gets a bit paranoid about all this stuff. I mean if the growth in the economy is negative one per cent, who cares? If The Warehouse turned over say $1 billion one year and the next year $990 million, is it the end of the world?

However, because enough people do care, and because TV and newspapers are sold on negative news, the masses get nervous and worried and stop spending money and buying stuff, and simply exacerbate the perceived problem. Companies' sales decrease and employees get laid off. They then have no money to spend and the vicious cycle continues.

Nevertheless, eventually it all comes right and some Government agency tells us we had a positive quarter and the recession is all over. The fact that because of statistical gathering issues, the announcement is a couple of months after the quarter ends means we have all been miserable for 60 days when we should have been drinking bubbly, scoffing Bluff oysters and celebrating the end of this terrible "continued reduction in industrial activity".

From a positive point of view, I was reminded recently by a commonsense economist, that "bad" recessions traditionally last for four quarters and "really bad" ones last for a maximum of six quarters.

Furthermore, if we assume the NZ and world "recessions" started around the middle of last year, then we are getting near the end; maybe June, possibly December.

I am 400 pages into a great book *The Snowball: Warren Buffett and the Business of Life*. Not surprisingly, it is about Warren Buffett, the world's richest man. He talks about the share market as "Mr Market". Well again historically and traditionally, Mr Market according to my economist mate, tends to start moving up about six months before the "end" of a recession. Again time will tell if history is going to repeat itself.

> *"Time will tell if we are all in for a tough old year. Business cycles come and go."*

This whole credit crunch business has been caused by the greedy old banks chucking vast amounts of money at all and sundry and oblivious or not caring whether the punters could pay it back or not. It has been party time for the banks and the punters and now it is hangover time.

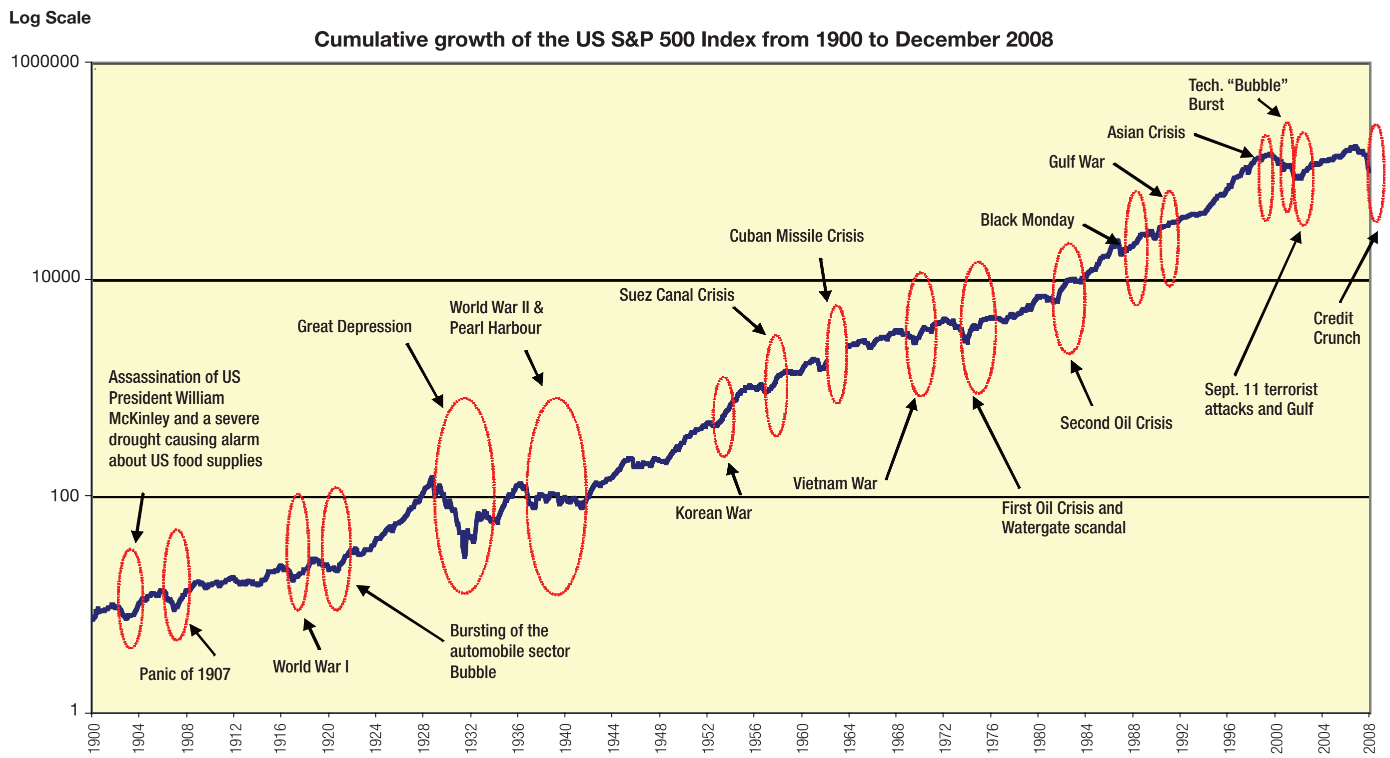
Many of the international banks look like they will have to be nationalised in order just to stay in business.

If you believe in capitalism though and the will of Governments around the world to make sure the whole system does not collapse, then it will all come right eventually. We have been through lots of bad times and the sun keeps shining, the world keeps spinning and over time the share markets keep going up, just like property inevitably will. Look at the attached graph.

History tells us major events will have a significant impact on the markets but the markets will recover and continue to track upwards as we go forward. As touched on earlier, last year we witnessed the deterioration of financial markets across the globe which gave rise to many banking failures and plummeting share markets. While the volatility of the markets is continuing and may do so for some time yet, it is important to remember the fundamentals and not be swayed by emotions or "noise" from the media.

In the graph the major events which have affected us over the years dating back to 1900 are shown. You will note even with some significant market corrections, the

Markets have always recovered from economic and geopolitical shocks



The chart shows that while markets have always reacted to economic and political events in the short- term, over the longer-term, not only have they always recovered, but they have gone on to make new highs. Overall the US S&P 500 total return index has delivered a 9.2% p.a. gross return between 1900 to 2008.

The chart Illustrates the growth of the US S&P 500 index in US dollars for the calendar years to December between 1900 and 2008. Source: Standard and Poors and Grosvenor Financial Services Group.

graph continues to trend upwards over the medium to longer term.

The table below provides a more focused analysis of the major market corrections enjoyed during the past 40 years. The data shows the date the market was at the peak before the correction, followed by the date at which time the market fell to the lowest point, including the number of days and percentage decline in moving from peak to trough. A snap shot of the market performance at six and 12 months from the date of the bottom point (trough) to illustrate the extent of the rebound is shown.

While we cannot guarantee history will repeat itself, we can all learn from these lessons. Times like this when history does have a habit of repeating itself, it is time to take heed of the advice from great people like Warren Buffett who says "Be very cautious when other people are being greedy and be greedy when other people are being cautious". He is now a "buyer of good quality assets currently at bargain prices".

Bob Jones wrote a good article in *the Dom Post* in January. Basically he said he had seen it all before (over about 50 years in business in his case) and everything would come right. *I agree.*

PRIOR PEAK	DAYS	DECLINE	TROUGH	6 MONTH PERFORMANCE	12 MONTH PERFORMANCE
26 October 1973	343	-41.5%	4 October 1974	35.5%	37.3%
13 February 1980	43	-14.3%	27 March 1980	31.6%	39.0%
12 August 1981	365	-17.6%	12 August 1992	38.0%	54.4%
2 May 1984	83	-13.1%	24 July 1984	20.7%	39.3%
27 August 1987	60	-21.4%	26 October 1987	22.8%	24.7%
4 January 1990	267	-26.3%	28 September 1990	21.6%	25.6%
17 April 1991	124	-10.1%	19 August 1991	10.7%	2.5%
6 January 1992	93	-13.8%	8 April 1992	5.0%	21.9%
31 October 1994	84	-8.2%	23 January 1995	16.2%	21.9%
7 October 1997	97	-10.2%	12 January 1998	23.3%	29.2%
20 July 1998	77	-20.7%	5 October 1998	34.2%	44.1%
28 September 2000	358	-35.2%	21 September 2001	19.9%	-5.7%
19 March 2002	204	-28.3%	9 October 2002	10.7%	42.7%
31 October 2007	385	-49.8%	20 November 2008	??	??

Source: Grosvenor Financial Services Group / MSCI World Index in Local Currency Terms