14 March 2013

The first step to succeed or the last chance to survive – an invitation to sustainable development

Please share!

An invitation to policy makers, financial institutions, entrepreneurs and innovators, academics and other interest groups to share their observations and experience those may reveal factors required to attract investors and remove barriers for sustainable development.

Dedicated to support sustainable development trends those strengthen resilience during financial shocks and contractions of economy.

Author: Ms Asta Pravilonytė

The first step to succeed or the last chance to survive – an invitation to sustainable development

Abstract

Inflated assets' bubbles remain the key to financial risks. The other risk is ignorance of markets' inertia. It seems that financial stability encourages the economic growth, and vice versa, economic growth is required to keep financial stability. But if consumption does not generate enough incomes to cover capital expenditures, is it a sign of bad luck or unconsidered actions those fail to match customers' preferences? The main criterion of efficient markets is equal opportunities to gather information so that market participants were able to estimate and compare the value of assets. However, with markets' distortions investors take inadequate higher risks than expected returns. Thus, are there sustainable development strategies those allow companies to generate incomes during economic contractions and enable investors to withstand financial shocks in the financial markets?

A brief review of European policies

Recession in Europe undermined local businesses and consumption. According to the Eurostat data the real GDP growth rate in European Union's 27 countries was -4.6% in 2009 which followed by a positive increase of 2.1% in 2010, 1.5% in 2011 and decline of -0.3% in 2012. The rate was projected to increase by 0.1% in 2013 and 1.6% in 2014. The biggest rates of economic contraction in 2012 were registered in Greece, Portugal, Cyprus, Slovenia and Italy. The recorded real GDP growth rates amounted -6.4%, -3.2%, -2.3%, -2.3% and -2.2% respectively. According to the data recorded in January 2013, the unemployment rate in 27 European countries comprised 10.8% with the highest rates in Spain, Croatia, Portugal those amounted 26.2%, 18%, 17.6% respectively and the unemployment rate of 26.4% in Greece which was registered in December of 2012. The analysis of EU-27 household final consumption expenditure published in February 2013 at the Eurostat's Statistics in focus revealed that actual individual consumption in 2011 was close to the EU-27 average of 70% of GDP for most countries; however, the range of the actual individual consumption per capita in euros varied from €35000 in Luxembourg and €29600 in Denmark to €6400 in Hungary in 2011 (respectively €3400 in Bulgaria and €4200 in Romania based on last available data for 2010). According to the survey the Baltic economies and Greece were the most severely affected, with loss of actual

Author: Ms Asta Pravilonytė
Website: www.asta.me.uk
Email: asta@asta.me.uk

22 Hastings Street
London SE18 6SY
United Kingdom

individual consumption (in volume terms) of 12% to 15% between 2008 and 2011.

European region is also the case of multiple decisions regarding bailouts, fiscal discipline policies, strategies for economic recovery and financial stability measures. According to the European Financial Stability and Integration Report prepared in 2011, during 2008 and October 2011, the Commission approved total state aid measures of €4.5trillion (36.7% of EU GDP), the majority of which in the form of guarantees on bank liabilities. The actions taken to insure stability involved enhanced financial supervision in Europe with established new European Supervisory Authorities for the banking, securities markets and insurance and occupational pensions sectors those started operating in January 2011, the Commission's contribution to the new Basel agreement on bank regulation (Basel III) in 2010, the European Financial Stabilisation Mechanism (EFSM) and the European Financial Stability Facility (EFSF) those were created in 2010 to provide up to €500 bn to Member State governments for reduction of tensions in euro area sovereign debt markets as well as established the permanent European Stability Mechanism (ESM). The other policies include measures for increased transparency such as temporary restrictions on short sales, prohibition to use credit default swaps in emergency situations, standardised OTC derivative transactions' clearing via central counterparties as well as the maximum guarantee cover for held deposits to €100000 and investors' compensation scheme to cover investments to €50000.

Moreover, financially fragile countries required financial assistance to implement structural reforms in order the borrowing costs were kept at sustainable level in the markets. According to the European Financial Stability and Integration Report prepared in 2011, the joint European and IMF's financial assistance to Greece amounted €110 billion in 2010, financial stability support to Ireland reached up to €85 billion. Portugal received an approved €78 billion bail-out in May 2011. Additionally, the financial assistance programmes have continued in Latvia, Romania and a precautionary programme was also requested by Hungary. One of the exceptional cases could be mentioned private investors' voluntary acceptance of a 50% Greek bond haircut which enabled both a €100 billion cut in Greece's sovereign debts and allowed a new Greek programme of aid of €100 billion at the end of 2011.

European financial sector also required governments' interventions and bailouts of banks due to mismanaged aggressive business strategies. According to the European Financial Stability and Integration Report 2011, the total amount of state aid actually used by the financial sector in EU 27 during October 2008 and December 2010 comprised €1.6 trillion (13.1% of EU27 GDP) of which: €1.2 trillion and other liquidity measures; €288 billion for recapitalisations; €121 billion for asset relief interventions. Restructuring of banks in Ireland, Denmark, Germany, Spain, United Kingdom involved mergers, recapitalization, deleveraging and operational optimizations.

Author: Ms Asta Pravilonytė
Website: www.asta.me.uk
Email: asta@asta.me.uk

22 Hastings Street
London SE18 6SY
United Kingdom

In addition, the European Central Bank's (ECB) role was also significant. According to the European Central Bank's Annual Report 2009, following the consequences of financial crisis the Governing Council of the ECB lowered interest rate on the main refinancing operations at 1.00%, the rate on the deposit facility at 0.25% and the rate on the marginal lending facility at 1.75% in 2009. The rates were slightly increased in 2011 as a result of the improved economic outlook; however, due to new demand of liquidity and intentions to support economic recovery with facilitated lending to businesses, the interest rates were lowered even more in 2012. The effective rates from 11 July 2012 are the following: rate on the main refinancing operations is 0.75%, the rate on the deposit facility is 0.00% and the rate on the marginal lending facility is 1.55%. According to the ECB's annual report prepared in 2009, the enhanced credit support to economy comprised the following five measures:

– the provision to euro area banks of unlimited liquidity at a fixed rate in all refinancing operations against adequate collateral;

– the lengthening of the maximum maturity of refinancing operations from three months prior to the crisis to one year;

– the extension of the list of assets accepted as collateral;

– the provision of liquidity in foreign currencies (notably US dollars); and

– outright purchases in the covered bond market.

The first 12-month LTRO, conducted on 24 June 2009, resulted in a record €442 billion being allotted to the euro area banking system at a fixed rate of 1%, bringing the total volume of outstanding refinancing operations to nearly €900 billion, and thereby contributed to lower money market rates also at longer maturities. The stabilisation in euro area and the recovery in asset prices from the record lows after the collapse of Lehman Brothers were indicated first time at the end of the first quarter of 2009. However, due to dysfunctional markets the ECB continued interventions in 2010, 2011 and 2012. According to the European Financial Stability and Integration Report 2011, between May 2010 and the end of December 2011 the ECB bought securities those amounted €218 billion, and at the end of 2011 its holdings contained about €211 billion. Furthermore, due to the ECB's launched two 3-year long-term refinancing operations (LTROs), the ECB allotted €489 billion in December of 2011 and during the second round of LTROs in February 2012 the ECB lent a total of €529 billion.

Moreover, investigations of supervisory authorities disclosed other systemic weaknesses of the European financial sector such as mis-sales of insurance, illegally fixed Libor rates and money laundering cases. Taxes on transactions and caps on bonuses are the further policies beside increased capital and liquidity requirements those are intended to shift banks' business models towards stability and credibility.

The basis of stronger European Union was set in the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union on 2 March 2012. One of the main elements of the Treaty was the so-

Author: Ms Asta Pravilonytė
Website: www.asta.me.uk
Email: asta@asta.me.uk

22 Hastings Street
London SE18 6SY
United Kingdom

called fiscal compact which proposes steps forward towards greater budgetary discipline and better coordinated fiscal policies in the EU. The other major agreement was reached regarding the European banking union in December 2012. Member States agreed to give to the ECB a supervisory responsibility. The Single Supervisory Mechanism will enable the ECB to detect risks in banking sector, request necessary actions, ensure compliance with capital requirements, grant and revoke licences for credit institutions.

Observations about recent events

Considering the economic contraction, raised unemployment and diminished consumption due to austerity measures the European countries went through in order to balance their sovereign budgets, stabilise financial sector and reduce borrowing costs, similar economic consequences may affect the US as it also attempts to reduce sovereign deficit. According to the Congressional Budget Act of 1974, an agreement for the budget for the United States Government for fiscal year 2014 and appropriate budgetary levels for fiscal years 2015 through 2023 should be achieved by April 15. The findings of the House of Representatives reported by the Committee on the Budget at the legislative text stated that measures those were used to boost economic activities during the recession and early stages of recovery added over $1 trillion to the debt though economy continues to perform at a subpar trend. Moreover, a view that large debt levels impose higher tax burden, creates uncertainties for businesses, stagnates the US economic growth and job creation was expressed. Consequently, the Budget Committee proposed to spend $4.6 trillion less in the next decade compared to the current path of spending. Private sector which is highly dependent on the government stimulus policies may suffer the most due to the government's budget discipline policies.

Other potential threats for the financial stability were reported in February and March. While money laundering investigations and €17 billion bailout which was negotiating for Cyprus seemed to be insignificant in terms of the scope of influence on financial markets, the downgraded UK's AAA credit rating to AA1 by rating agency Moody's and the Bank of England's estimates on the capital shortfall of £35 billion for Britain's banks if risk-weighted assets were standardised are important risk factors considering investment. Moreover, it seems that the US Federal Reserve's report on the stress test of banks was also ignored. According to the Federal Reserve's released results on 7 March 2013, the nation's largest banks have continued to improve their ability to withstand severe economic conditions with stronger capital positions. However, due to the stress scenario which includes a peak unemployment rate of 12.1%, a drop in equity prices of more than 50%, a decline in housing prices of more than 20%, and a sharp market shock for the largest trading firms, projected losses at the 18 bank holding companies would total $462 billion during the nine quarters of the hypothetical stress scenario. Additionally, the aggregate tier 1 common capital ratio, which compares high-quality capital to risk-weighted assets, would fall from an actual 11.1% in the third quarter of 2012 to 7.7% in the fourth quarter of 2014 in the hypothetical stress scenario.

Despite the on-going fiscal discipline measures, economic contraction threats and estimated potential losses due to financial shocks the S&P 500 Index exceeded pre financial crisis level and reached 1556 on the 11th of March 2013. The FTSE 100 Index similarly reached a new high of 6510 on the 12th of March 2013.

Even though the international standards and supervision on financial institutions were enhanced, deterioration of assets' value remains a major pressure on stability. Consequently, investors may face waves of gradual downtrends if performance of companies misses estimated earnings due to diminished consumption and weak economic growth. The other possible scenario is higher volatility - if resilience of declined equities' value is stimulated with continuing monetary easing policies.

And if it is not true, then how much such development cost and how long such recovery last?

Author: Ms Asta Pravilonytė
Website: www.asta.me.uk
Email: asta@asta.me.uk

22 Hastings Street
London SE18 6SY
United Kingdom

An invitation

Certainly, various regions are exposed to different economic development and financial stability challenges; however, is it possible to balance economy and financial stability by successful expansion of sustainable businesses and reduced financial risks?

Taking into account threats of current economic growth and financial stability issues, we would like to invite policy makers, financial institutions, entrepreneurs and innovators, academics and other interest groups to share their observations and experience those may help to identify factors required to attract investors and remove barriers for sustainable development. So, that launched financial facility programmes supported development necessary to strengthen resilience during financial shocks and contractions of economy.

Proposed topics are the following.

1. The concept and benefits of sustainable development. Threats and barriers attracting investors. Consumer's preferences. Estimation of the long term value instead of initial costs of the investment projects. Business resilience during financial shocks and contraction of economy.

2. Challenges introducing specific sustainable development projects/investment opportunities in different regions. The attractiveness of business environment, issues related to the market uptakes of innovations, transfer of knowledge and skills. Preparation of investment projects and managing risks of project implementation.

3. Business development, competitive advantage of investment in environmentally friendly innovations those let to achieve greater resource efficiency. International investment opportunities, benefits and challenges of business development, international cooperation, cross continental partnerships, required legal reforms, preparation of business development plans and risk management.

4. Market uptake of innovations, issues related to standardisation and investment in innovations. Protection of intellectual property rights, practices and strategies for launched innovations.

5. Attractive investment opportunities, expectations of investors, assessment of investment opportunities, risk management practices. What makes proposed investment project attractive?

6. Fund raising practices. Available alternative funds and financial facilities for implementation of sustainable development projects. Preparation of investment proposal, feasibility of investment opportunity, assessment of alternative strategies and project risk management.

7. Balanced interests in public and private partnerships. Balanced rights and obligations of public and private partnerships, challenges managing conflicts of interests.

Author: Ms Asta Pravilonytė
Website: www.asta.me.uk
Email: asta@asta.me.uk

22 Hastings Street
London SE18 6SY
United Kingdom

8. Financial stability issues. Management of counterparty, credit and market risks. Practices and challenges in estimation of risks, returns and costs of capital, assessment of leverage in financial decisions.

9. Sovereign wealth funds interest in sustainable development solutions. Investment priorities of sovereign wealth funds, assessment of attractive investment opportunities.

10. Managing conflicts of interests, international disputes. Demand of legal advice, services and reforms.

If you are interested in topics mentioned above and investment in sustainable development please let us know.

Thank you for your time in considering cooperation.

We look forward to hearing from you.

Yours sincerely,

Ms Asta Pravilonytė

Website: www.asta.me.uk
Email: asta@asta.me.uk

Tel: +44 (0) 2083166205
Mob: +44 (0) 7531222596

22 Hastings Street
London SE18 6SY
United Kingdom