



# United Kingdom Economic Update

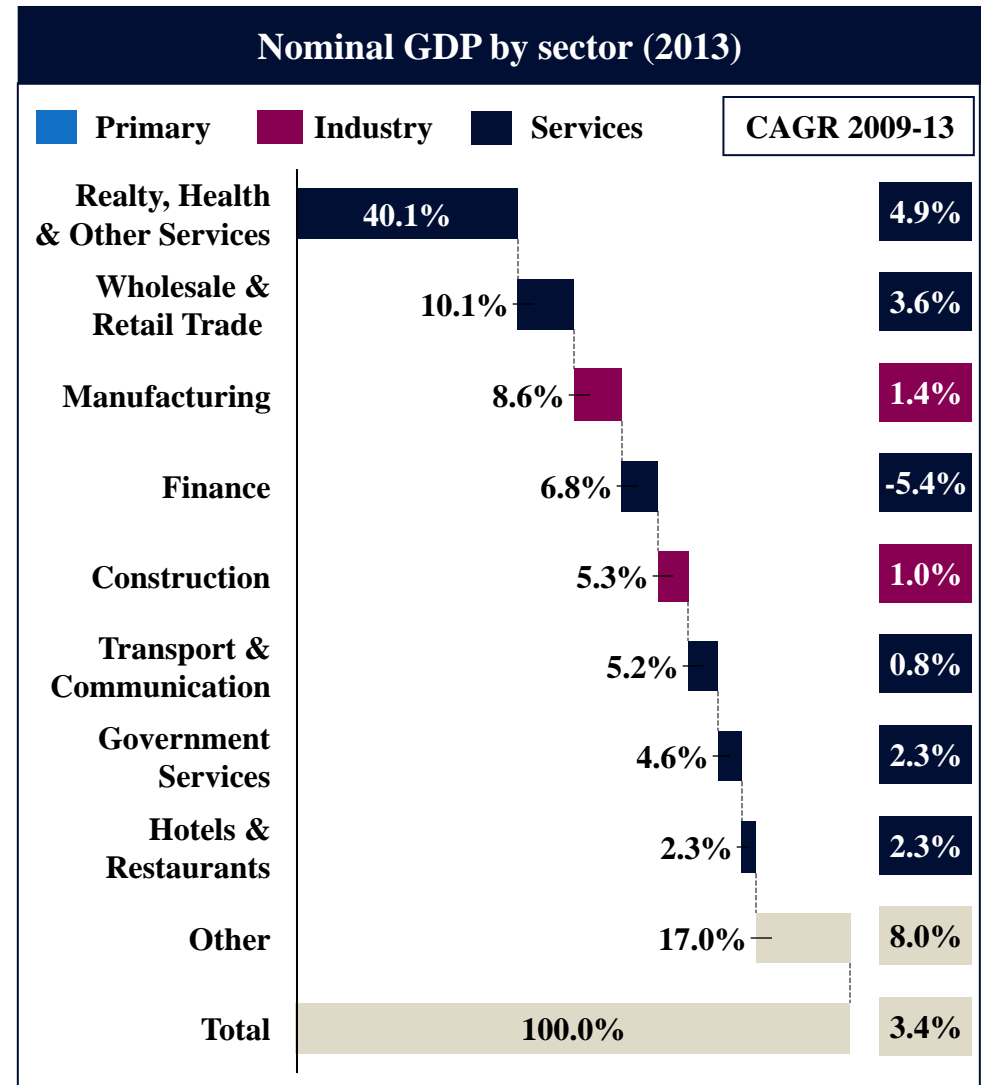
## QNB Group

September 2014

# United Kingdom – Overview

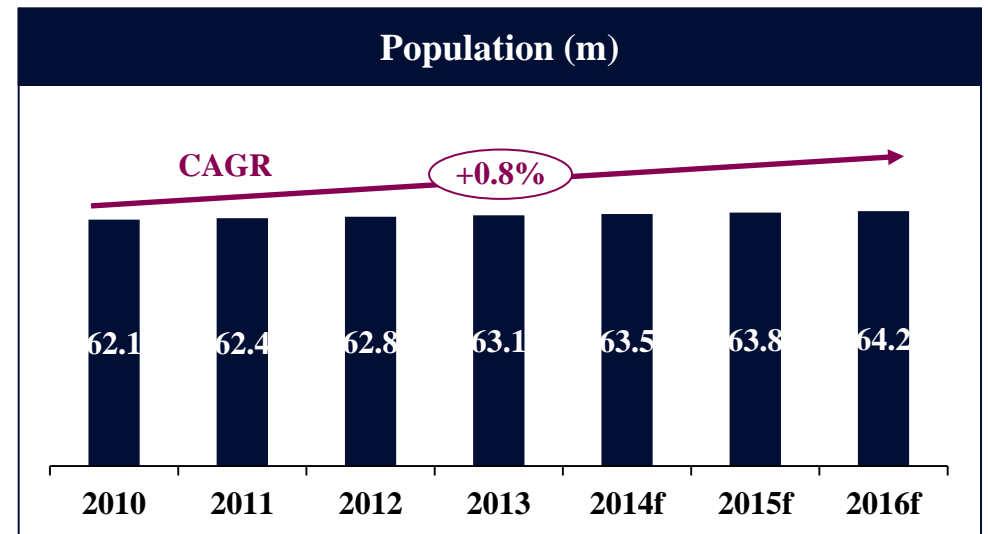
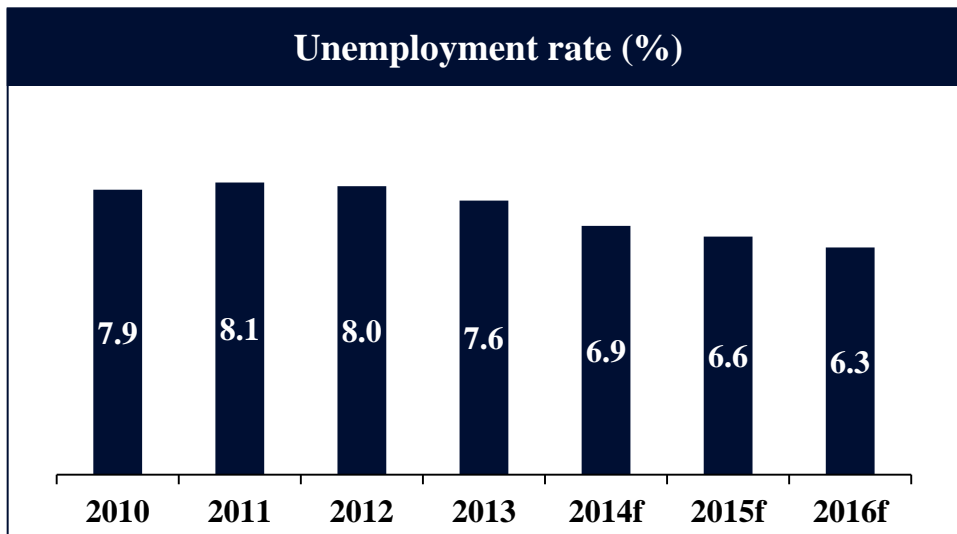
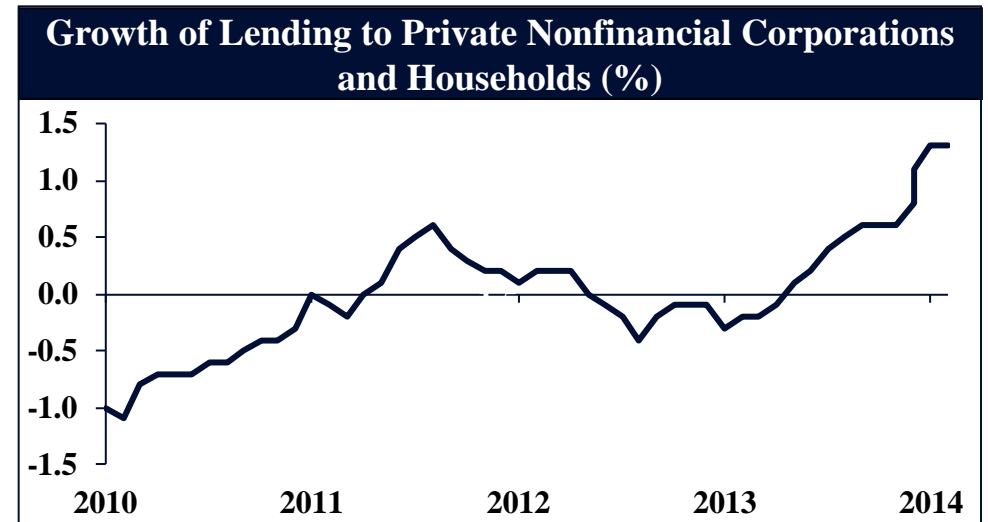
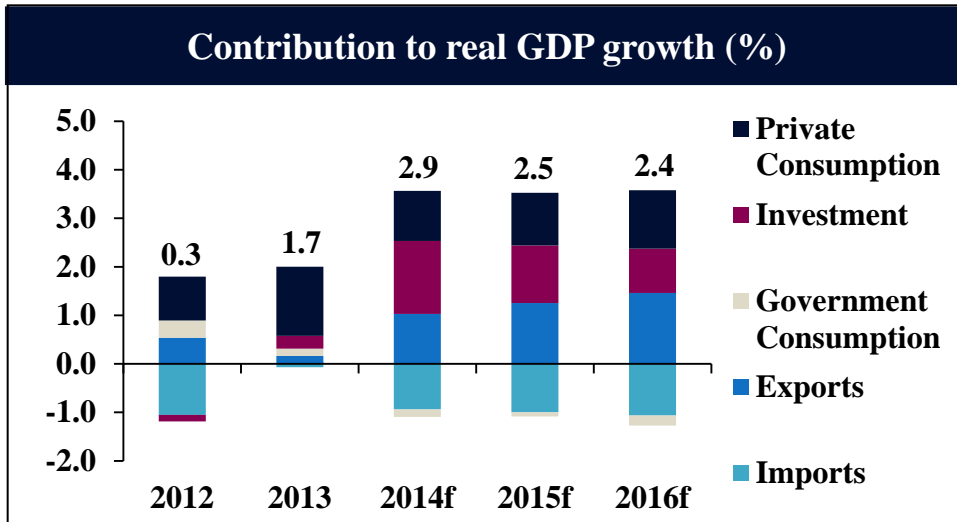
Leading services and financial center, the UK is the third largest economy in Europe after Germany and France; the UK became a net importer of energy after 2005 as coal and oil reserves are declining; sovereign ratings are high

Overview Data (2013)	
GDP (bn USD)	2,535.4
% GDP related to Services	69.1
Real GDP Growth (%)	1.7
Per Capita GDP (k USD, PPP)	37.3
CPI Inflation (%)	2.6
Current Account Balance (% of GDP)	-3.3
FX Reserves (months of import cover, end-2013)	1.4
Exchange Rate (GBP:USD, end-2013)	1.65
Fiscal Balance (% of GDP)	-5.9
Government Debt (% of GDP)	90.1
Broad Money Growth (%)	0.8
Banking Assets (% of GDP)	457.4
3-Month Interbank Rate (%)	0.5
Population (m)	63.1
Population aged 15-64 Years (% share, 2008)	41.0
Population growth (%)	0.6
Unemployment (%)	7.6
Religion (% Muslim)	4.4
Doing Business Rank out of 189 (WB)	10
Competitiveness Rank out of 148 (WEF)	10
Moody's Rating (Long-term FX debt)	Aa1



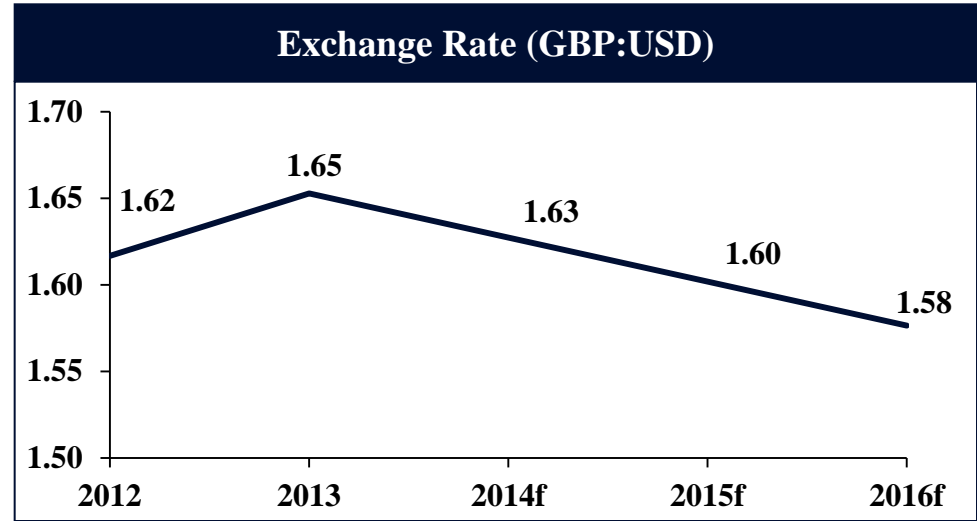
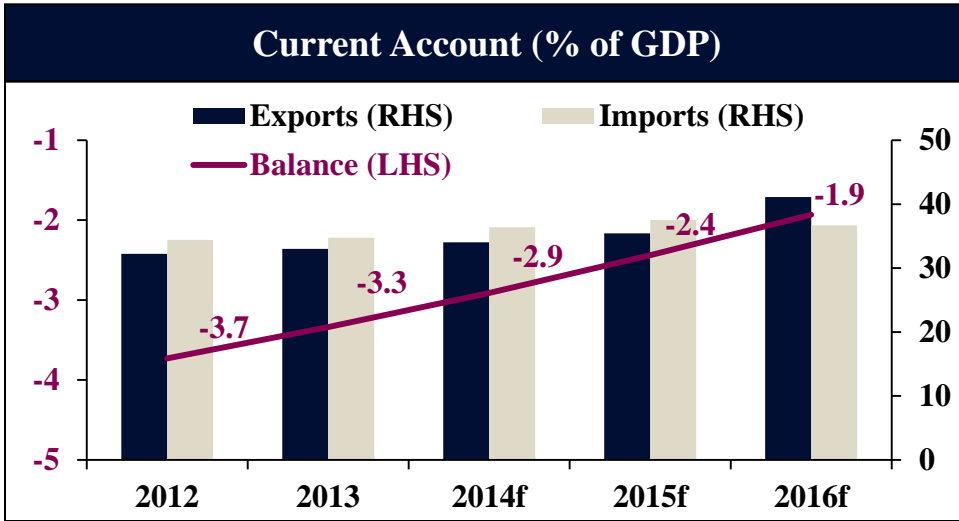
# United Kingdom – GDP Growth

Real GDP growth is recovering from the Great Recession, driven by domestic demand and improved lending to the private sector; this is projected to lead to a steady decline in unemployment, notwithstanding moderate growth in population



# United Kingdom – Balance of Payments

The current account deficit is expected to narrow as exports recover and GBP is projected to depreciate moderately; international reserves are projected to rise on lower current account deficits; trade is mostly with Europe

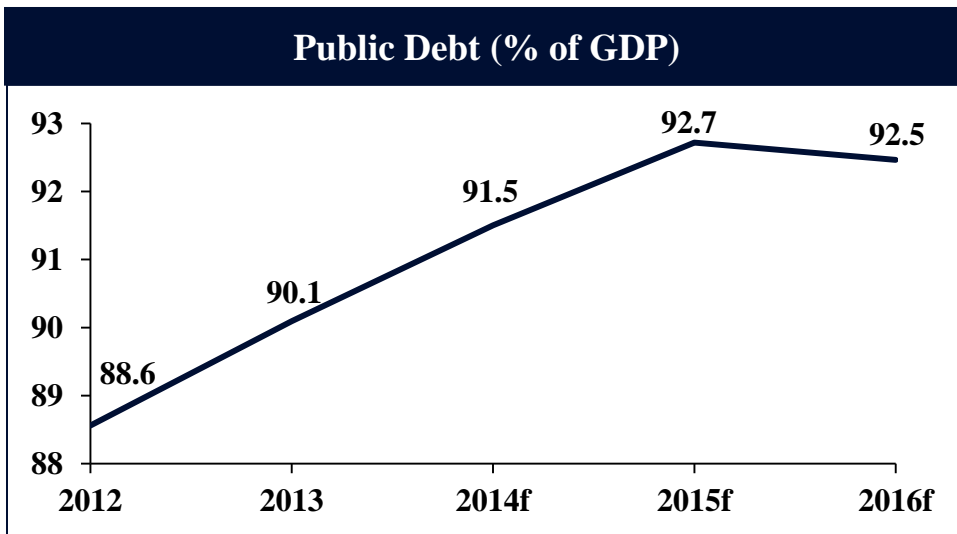
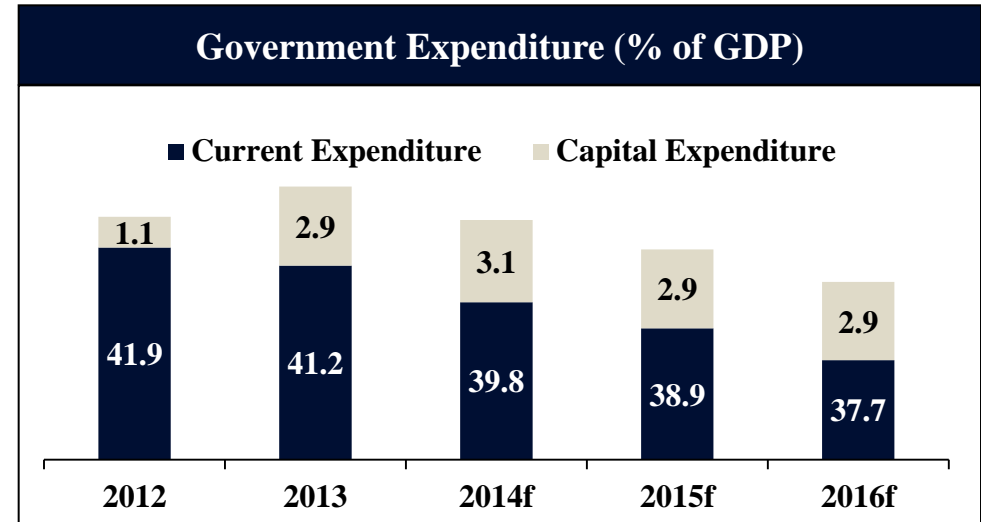
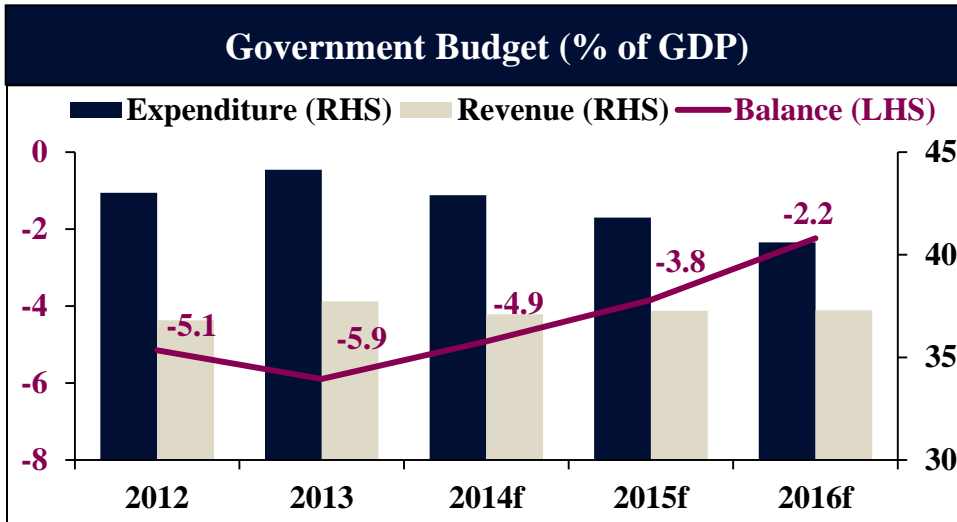


### Direction of Trade (2013)

Exports		Imports	
Destination	(bn USD)	Source	(bn USD)
Switzerland	68.7	Germany	86.6
Germany	44.5	Netherlands	53.1
United States	43.8	China	53.0
Netherlands	37.3	France	37.3
France	31.5	United States	34.6

# United Kingdom – Fiscal Policy

Fiscal policy aims to reduce the fiscal deficit through an austerity program aimed at cutting current expenditures; public debt is projected to peak in 2015 at nearly 93% of GDP, before it starts declining on lower fiscal deficits

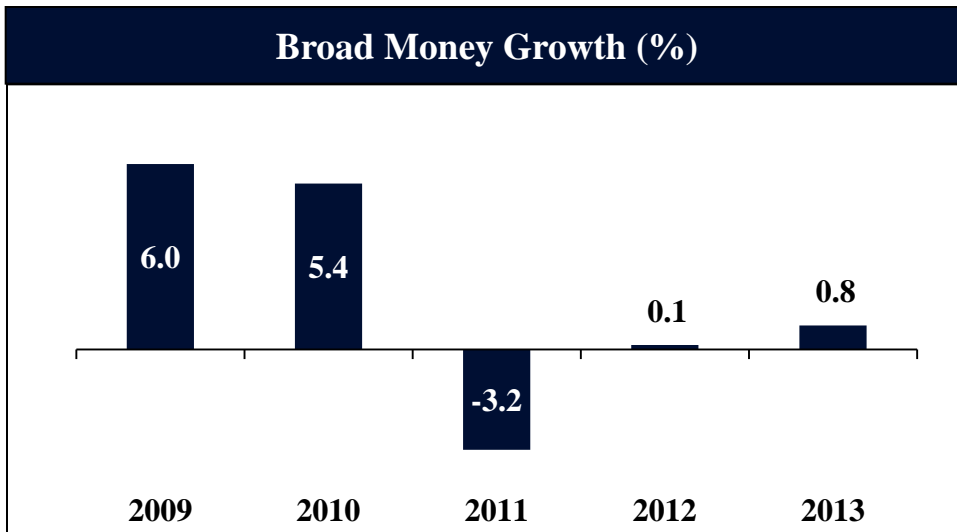
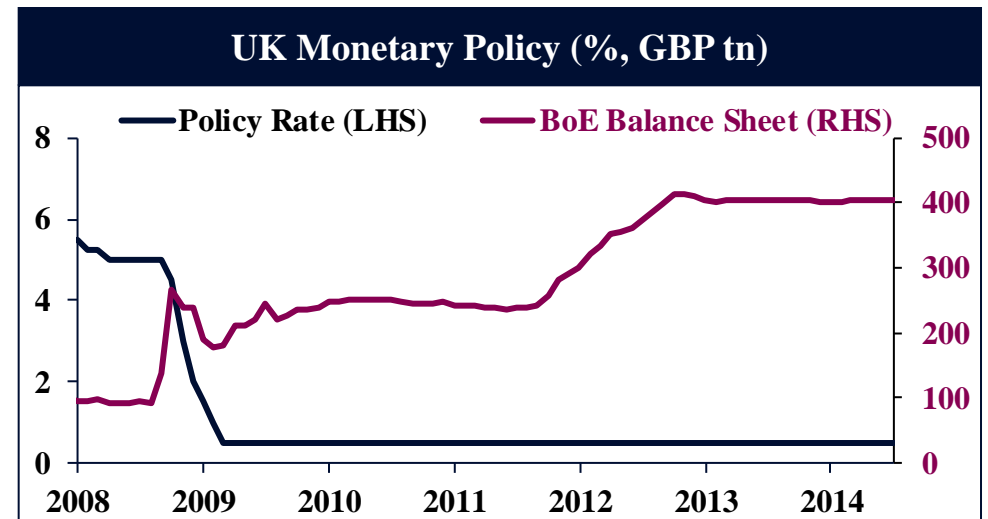
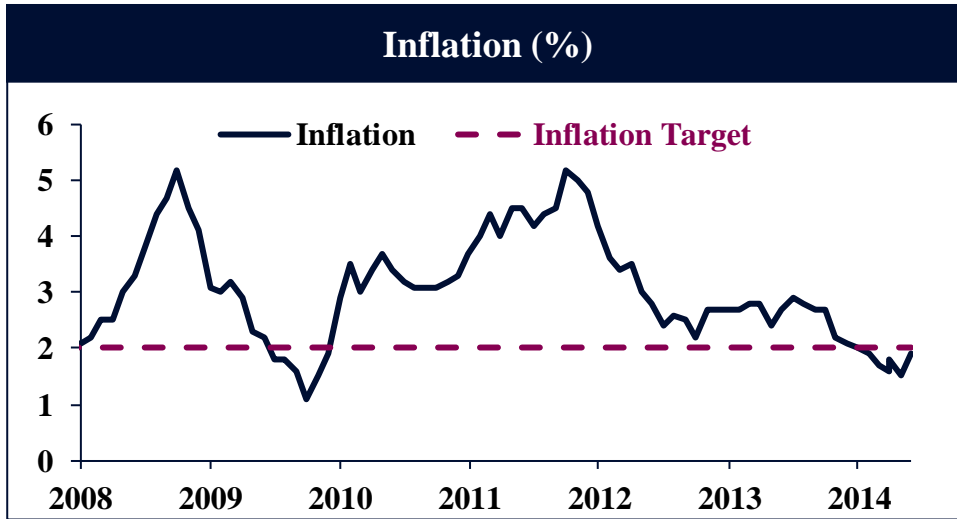


### Fiscal Policy

- Fiscal policy aims to reduce the fiscal deficit by cutting current expenditures
- The fiscal deficit is expected to narrow to 2.2% by 2016 as the government continues to implement its austerity program
- Public debt is projected to peak at nearly 93% of GDP in 2015 before it starts declining on lower fiscal deficits

# United Kingdom – Monetary Policy

Monetary policy aims to achieve a 2% inflation target over the medium term; inflation has recently slowed to below 2%; with the policy rate at 0.5%, the BOE has expanded its balance sheet to revive broad money growth

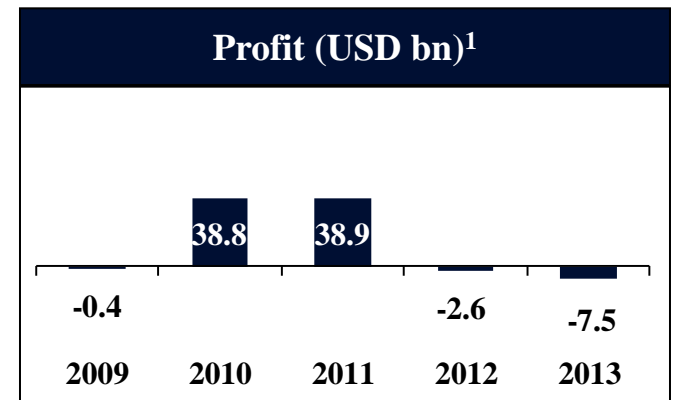
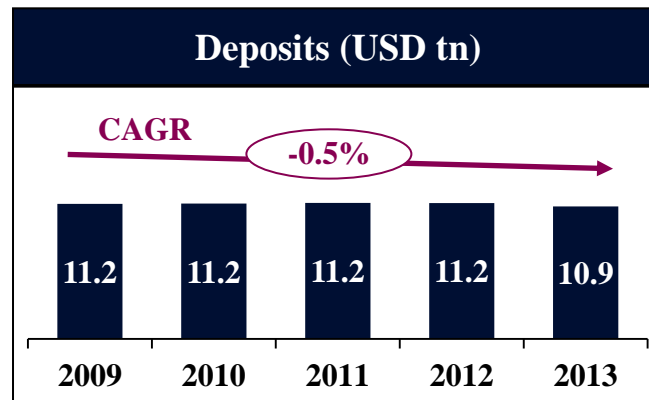
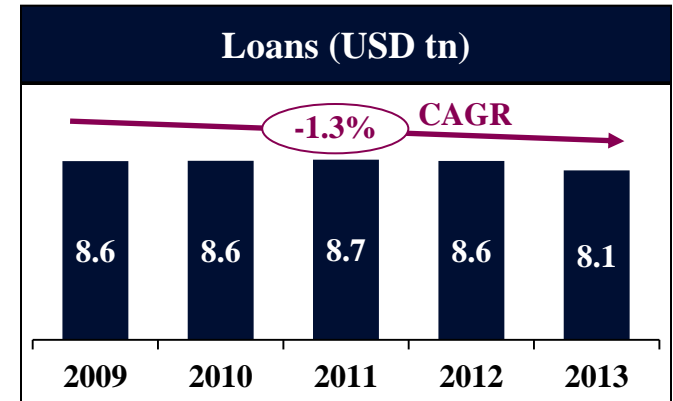
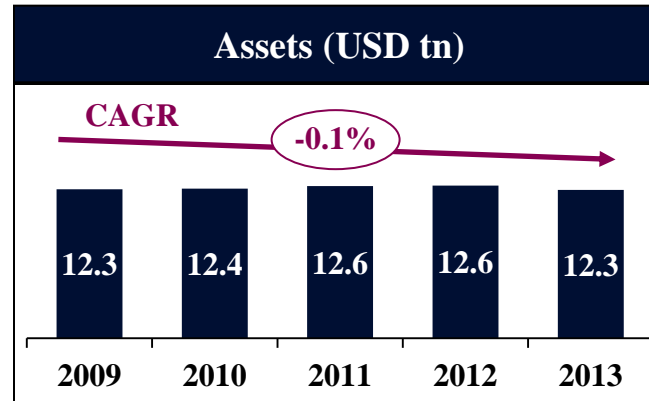
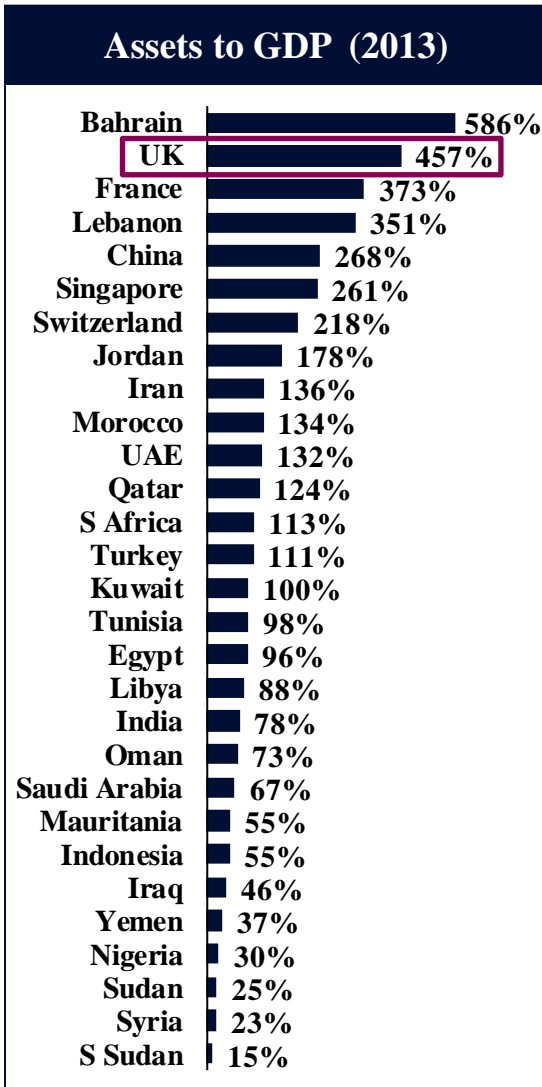


### Monetary Policy

- UK monetary policy aims to achieve a 2% inflation target over the medium term
- Inflation was above target for almost four years due to high commodity prices and a series of administrative price shocks; however it has recently fallen to below 2% on lower global food prices
- With the policy rate at the lower bound (0.5%), the BOE has expanded its balance sheet to revive broad money growth through a series of quantitative easing programs

# United Kingdom – Banking Sector Overview

Assets, loans and deposits fell during the financial crisis and have not yet recovered with the improved economy; following the Funding for Lending Scheme (FLS), credit to the SME sector has recovered while overall loans are declining

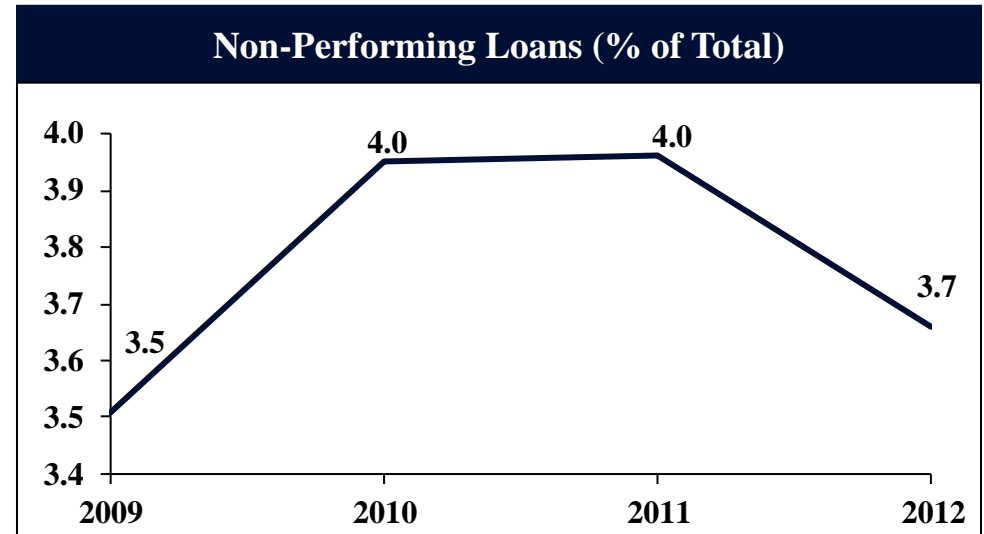
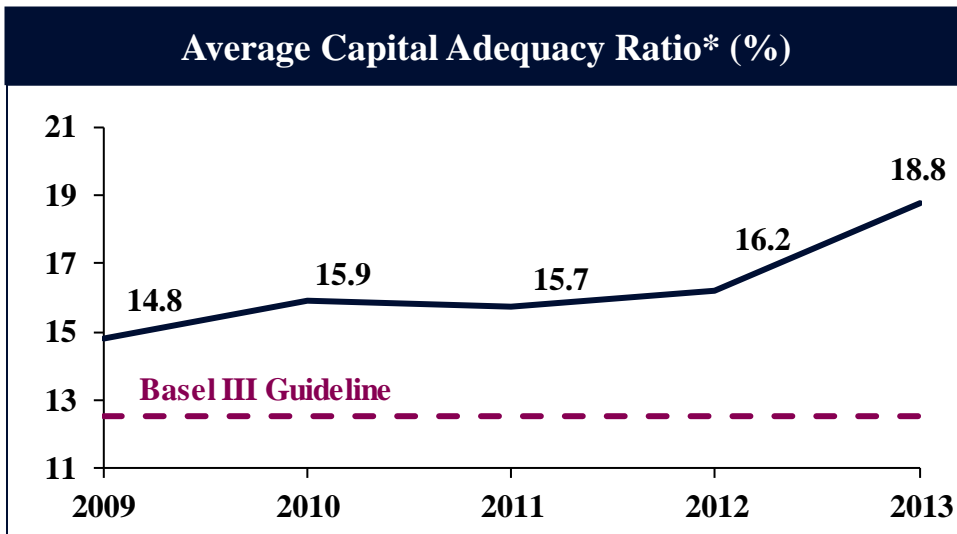
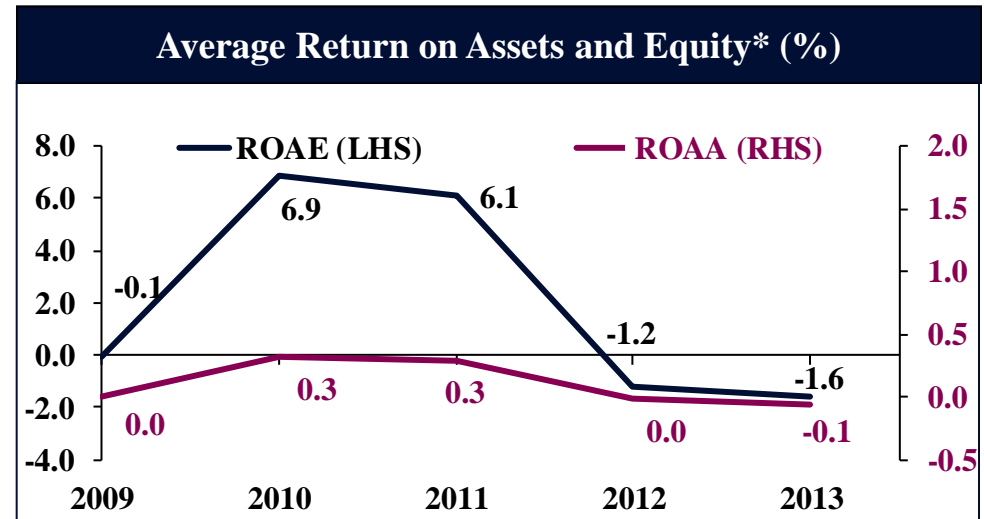
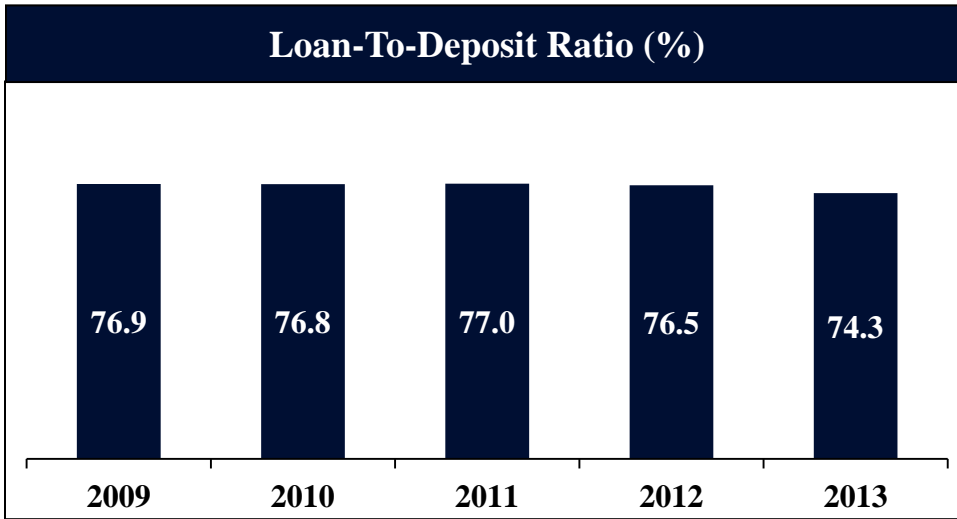


### Funding for Lending Scheme (FLS)

- FLS provides incentives for banks to lend to the real economy by linking the quantity and the price of funding to banks to their lending performance. It was introduced in July 2012 and extended in April 2013 to provide additional incentives to lend to SMEs

# United Kingdom – Banking Sector Ratios

The declining loan-to-deposit ratio reflects a reluctance of banks to lend; average returns on assets and equity have turned negative in 2012-13; banks are adequately capitalized while the share of non-performing loans is stabilizing





# United Kingdom – Banking Sector Competitor Analysis

Banking sector health has improved somewhat since the depth of the crisis, but a few banks are still under public control; profitability at the top 5 banks has been low in recent years on rising non-performing loans

## Financials for Top 5 Banks (2013)\*

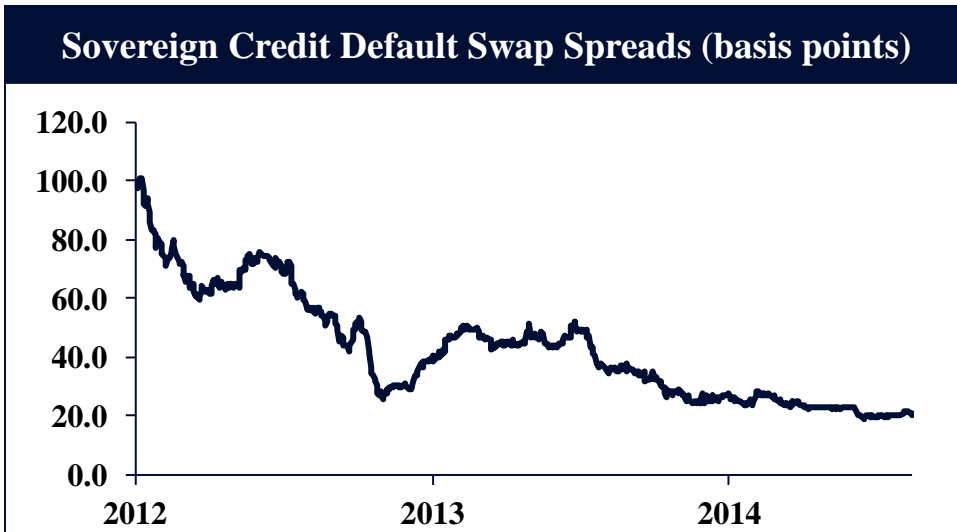
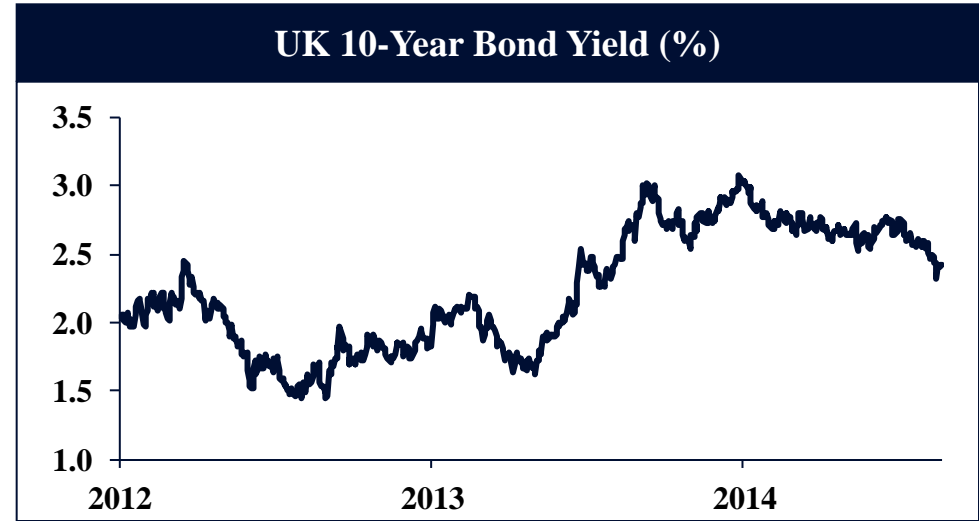
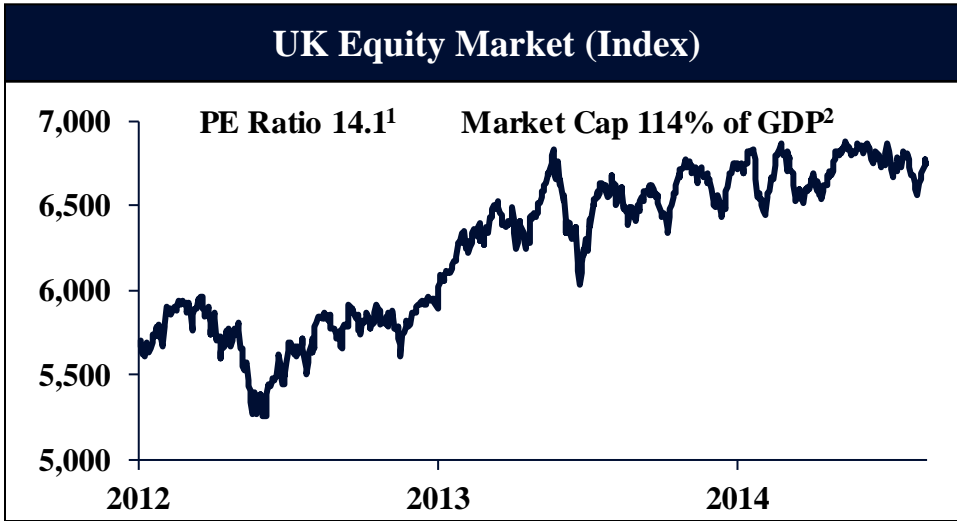
	Market Share by Assets (%)	Net Income (bn USD)	Equity (bn USD)	Return on Equity (%)	Assets (tn USD)	Return on Assets (%)	Loan to Deposit Ratio (%)	Non-Performing Loans (%)
HSBC Holdings	20.4	17.8	190	9.5	2.7	0.7	74	3.6
Barclays	16.5	2.1	105	2.1	2.2	0.1	102	5.7
Royal Bank of Scotland Group	12.9	-14.0	98	-13.1	1.7	-0.7	100	8.9
Lloyds Banking Group	10.6	-1.3	65	-2.0	1.4	-0.1	117	6.3
HBOS	7.0	2.6	36	6.9	0.9	0.3	144	8.4

## Analysis

- There are 239 banks operating in the UK, most of them conventional privately-owned, although a significant proportion are foreign
- Following the financial crisis of 2008, the government has acquired shares in a number of failing banks, including Lloyds and Royal Bank of Scotland
- The top five banks have a 67% market share in terms of assets, with an even larger control of the total loan book
- Most banks reduced their lending after the crisis as they tried to deleverage their balance sheets and to protect themselves against unrealized losses
- Funding costs for a number of the large UK banks have fallen significantly, reflecting quantitative easing by the BOE and the FLS

# United Kingdom – Financial Markets

The FTSE 100 index is virtually unchanged since end-2013 on expectations of higher interest rates and a weak global recovery; bond yields rose in line with US yields since mid-2013; CDS spreads are low and ratings remain strong



### Sovereign Ratings (July 2014)

	Rating	Outlook
Moody's	Aa1	Stable
Standard & Poor's	AAAu	Stable
Capital Intelligence	AA-	Stable
Fitch	AA+	Stable

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