



making business sense

LSE seminar on the London economy

The Centre for Economics and Business Research

Douglas McWilliams, chief executive

Richard Snook, senior economist



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London – is the honeymoon over?

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Objective

- To give our view on whether the credit crunch will deal a lasting blow to London's prosperity



Outline

The past — *what we said in 2005*

The present — *The credit crunch and London*

The future — *Is the honeymoon over for London?*

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The past — *what we said in 2005*

The present — *The credit crunch and London*

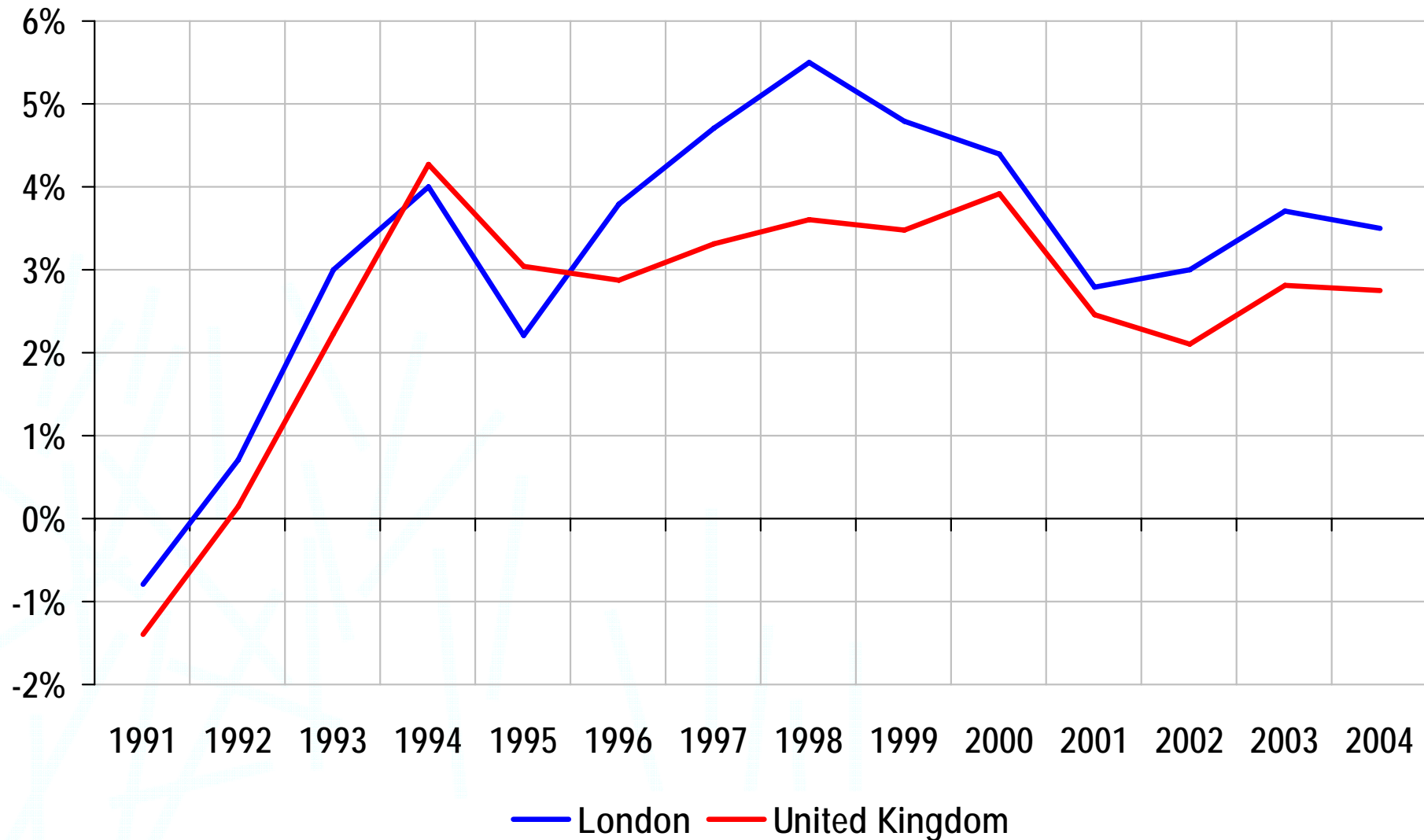
The future — *Is the honeymoon over for London?*

Factors in past success

- Supply side of the London economy is benefiting from high migration
- London has become the international financial centre
- London benefits from its role as the UK and global business services hub

London had outperformed UK average

Gross domestic product, London and the UK, annual percentage change

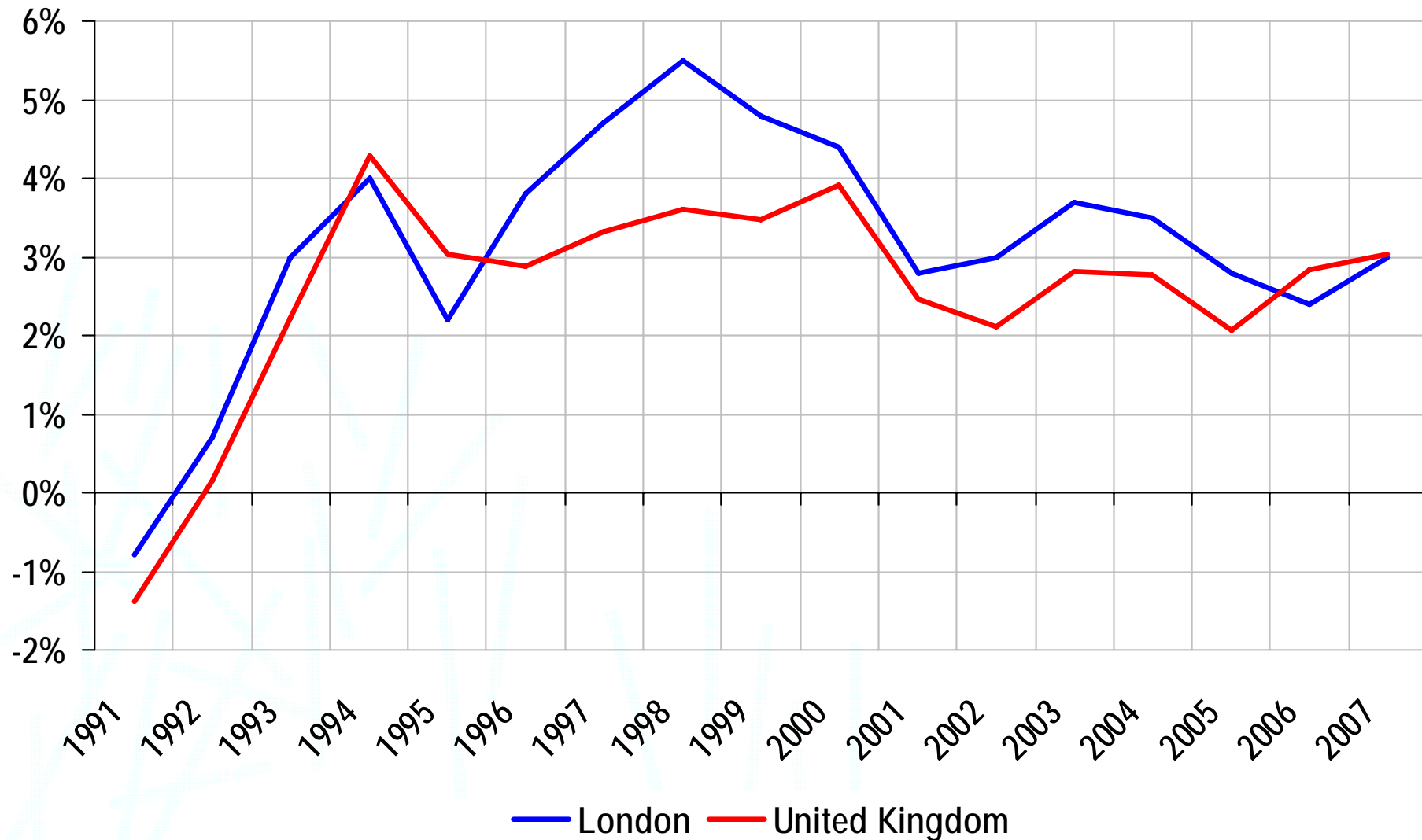


Critical success factors for the London economy looking forward from 2005

- the international economic environment
- competitiveness of the City
- London's role in supplying business services
- housing
- transport

London's GDP outperformance forecast to end

Gross domestic product, London and the UK, annual percentage change



Outline

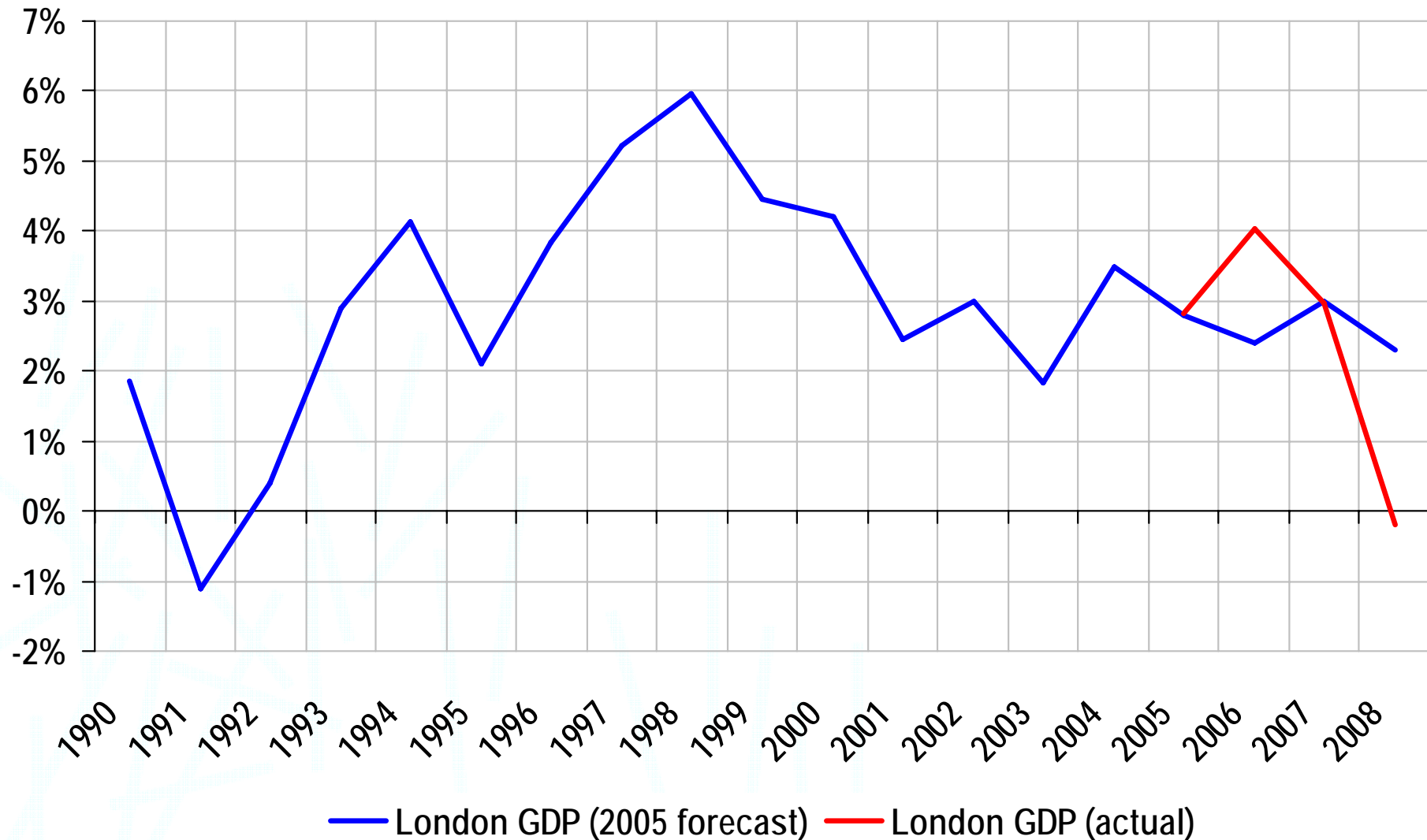
The past — *what we said in 2005*

The present — *The credit crunch*

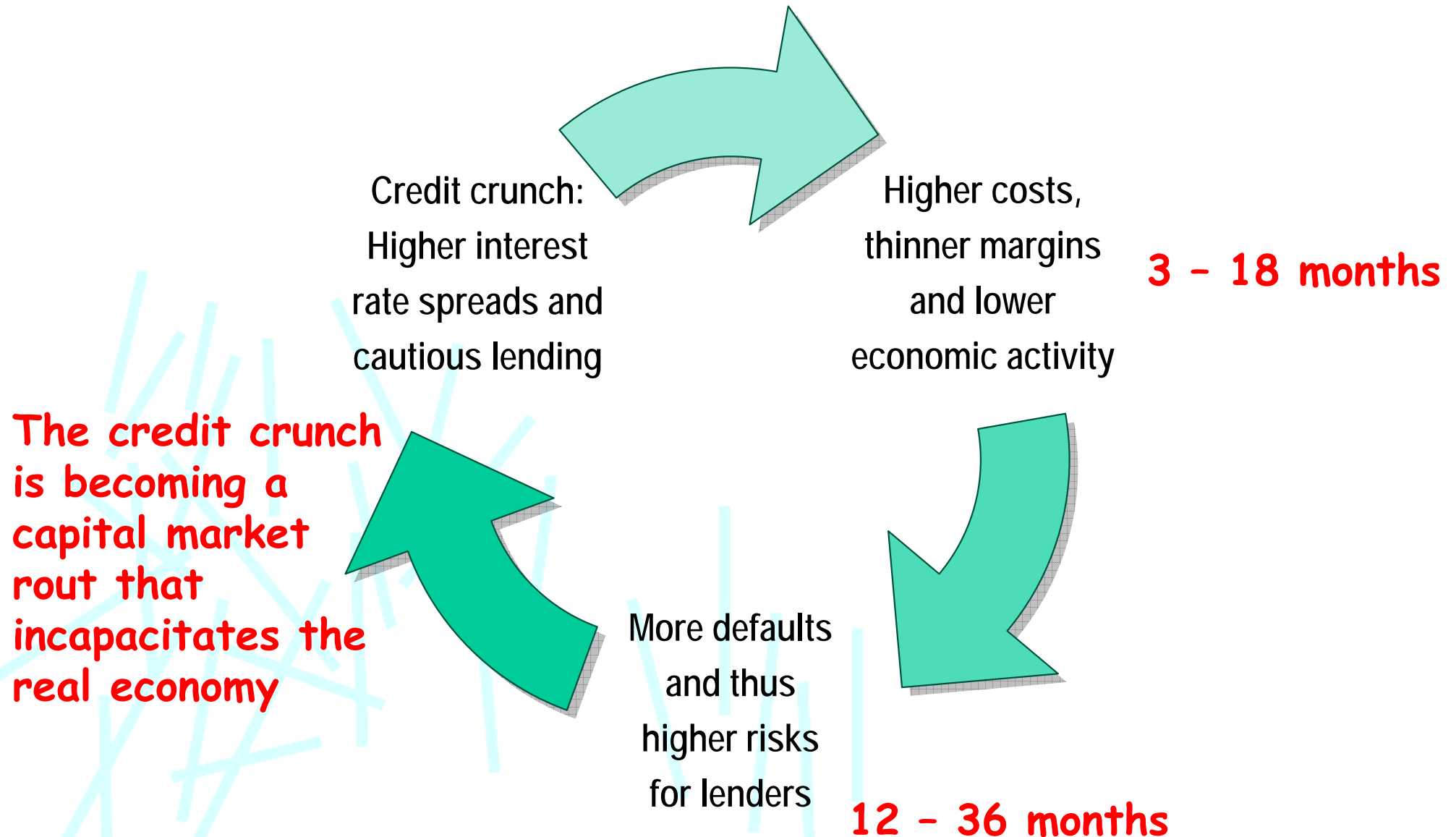
The future — *Is the honeymoon over for London?*

The cycle has been rather more volatile than we had predicted 4 years ago

London annual real GDP growth, actual compared with cebr's 2005 prediction



The vicious credit crunch circle



The hits to the finance sector from the credit crunch

Reduction in bank lending

Reduced derivatives activity

Deglobalisation of capital markets

Reduction in M&A

Less active capital markets

Private equity going into hiding

Impact of regulation

Nationalisation

Bonuses...

Based on market capitalisation at Tuesday 20 January

RBS paid \$100bn for ABN Amro in October 2007

Today, you would get

Citibank \$15.2bn

Morgan Stanley \$13.7bn

Goldman Sachs \$23.4bn

Deutsche Bank \$11.6bn

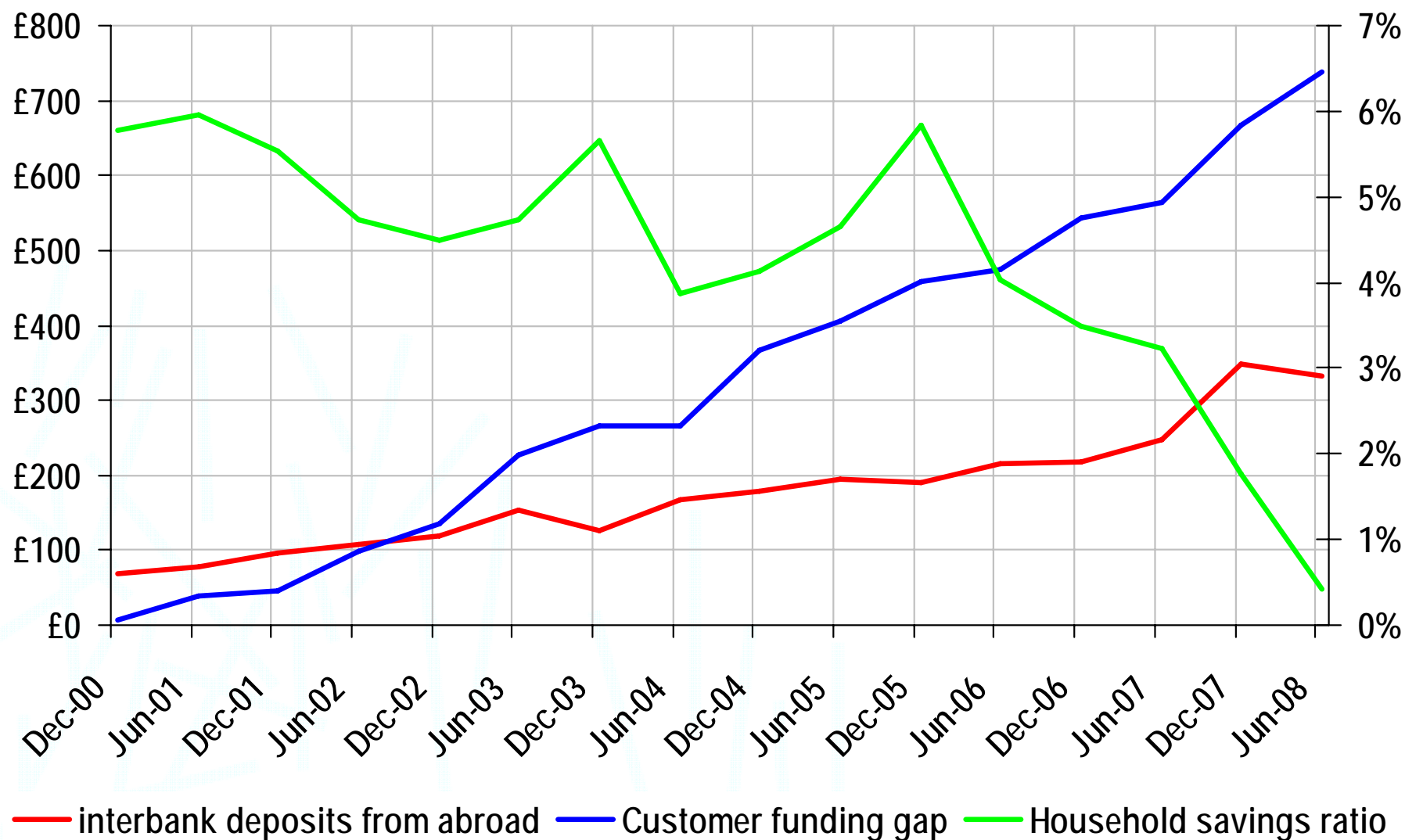
Barclays \$8.7bn

Lloyds Banking Group \$11.6bn

And still have enough change to buy GM, Ford & Chrysler

£700 billion bank funding gap

Household savings, UK banks interbank deposits and customer funding gap

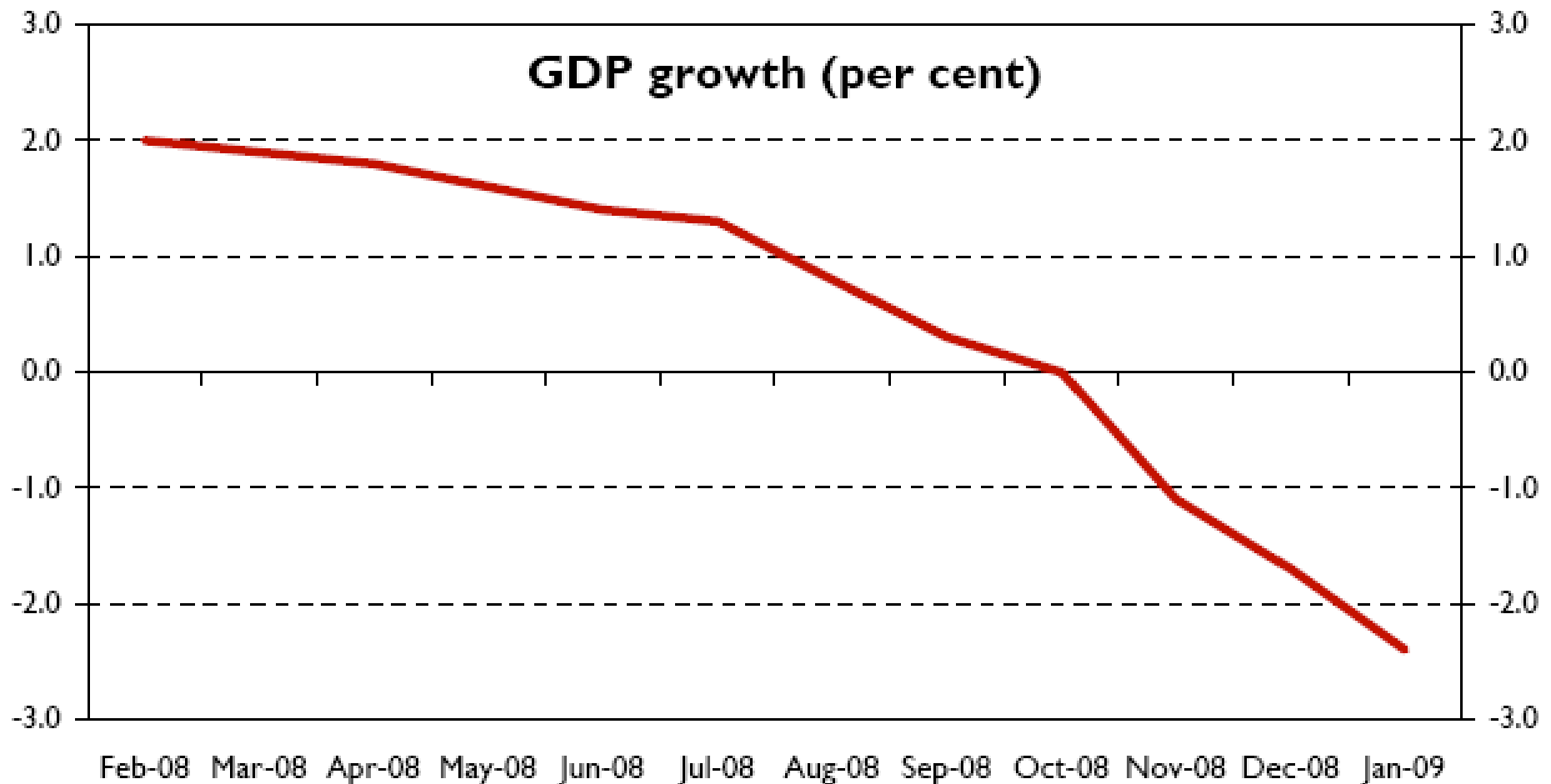


Merged, folded or focussing elsewhere

Aggregate Lending 2006 - 2008				
Rank	Lender	Deal Value (US\$) (m)	No.	%share
8	Bank of Scotland	18,103.04	158	2.93
13	Bank of Ireland	11,185.01	145	1.81
16	Dresdner Kleinwort	10,290.35	61	1.66
18	ABN AMRO	9,950.48	66	1.61
19	ING	9,812.11	101	1.59
	Accounted for almost 20% of corporate lending			1.50
21	Allied Irish Banks plc	8,535.33	118	1.38
27	Fortis	7,634.30	117	1.23
28	Bayerische Landesbank	6,946.23	82	1.12
29	UBS	5,590.39	37	0.90
30	Merrill Lynch	5,242.92	23	0.85
33	Natixis	4,856.98	73	0.78
34	WestLB	4,394.45	56	0.71
38	KBC	3,459.12	71	0.56

Forecasts drop over four per cent in a year

Median of independent forecasts for United Kingdom real gross domestic product in 2009



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Key factors driving the London economy

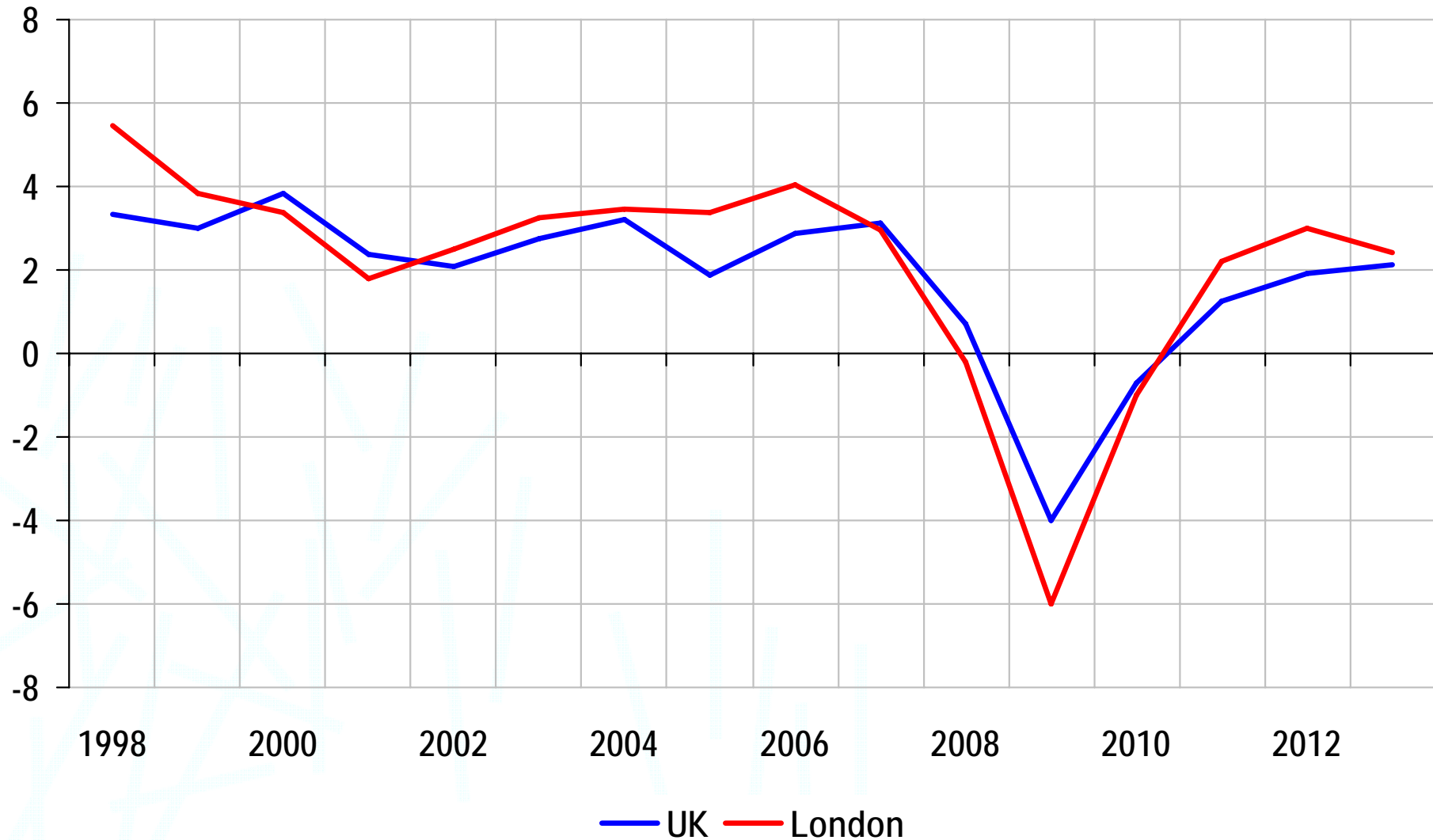
- Contraction in the financial services sector – capital market de-globalisation
- Falling house prices – reducing consumer confidence, more saving
- Rising unemployment – encourages people to save – the paradox of thrift
- Low returns on corporate spending and difficult credit conditions – collapse in business investment and spending on business services
- Weak government fiscal position – inhibiting Keynesian measures and moving UK to higher tax economy (but good for bond market!)
- The Olympics

London and South East most vulnerable

Rank	
London	1
South East	2
East	3
West Midlands	4
East Midlands	5
North West	6
South West	7
Yorkshire and the Humber	8
Scotland	9
North East	10
Wales	11

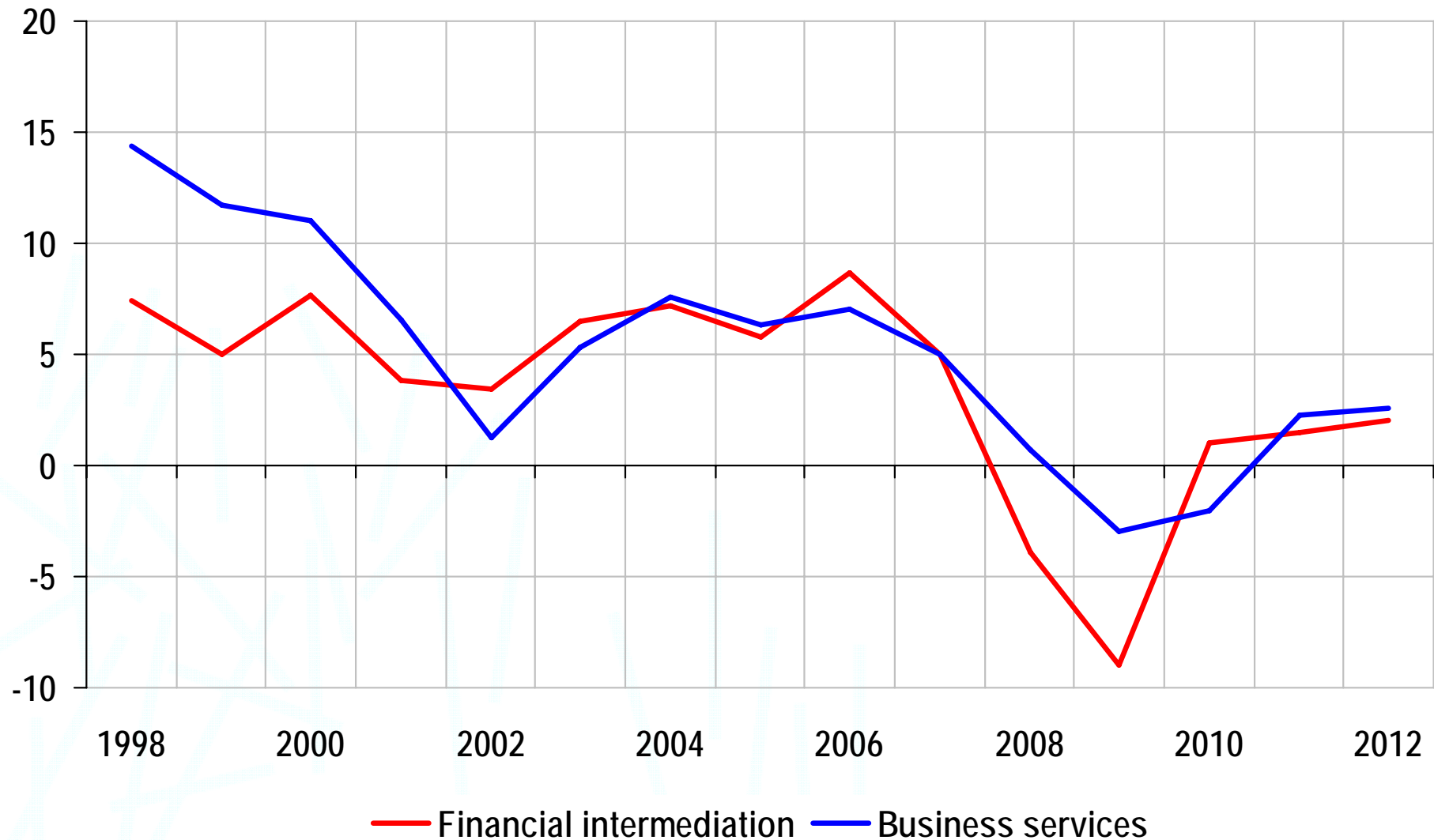
London economy to contract by 7 per cent 2007-10

UK and London GDP, real annual percentage change



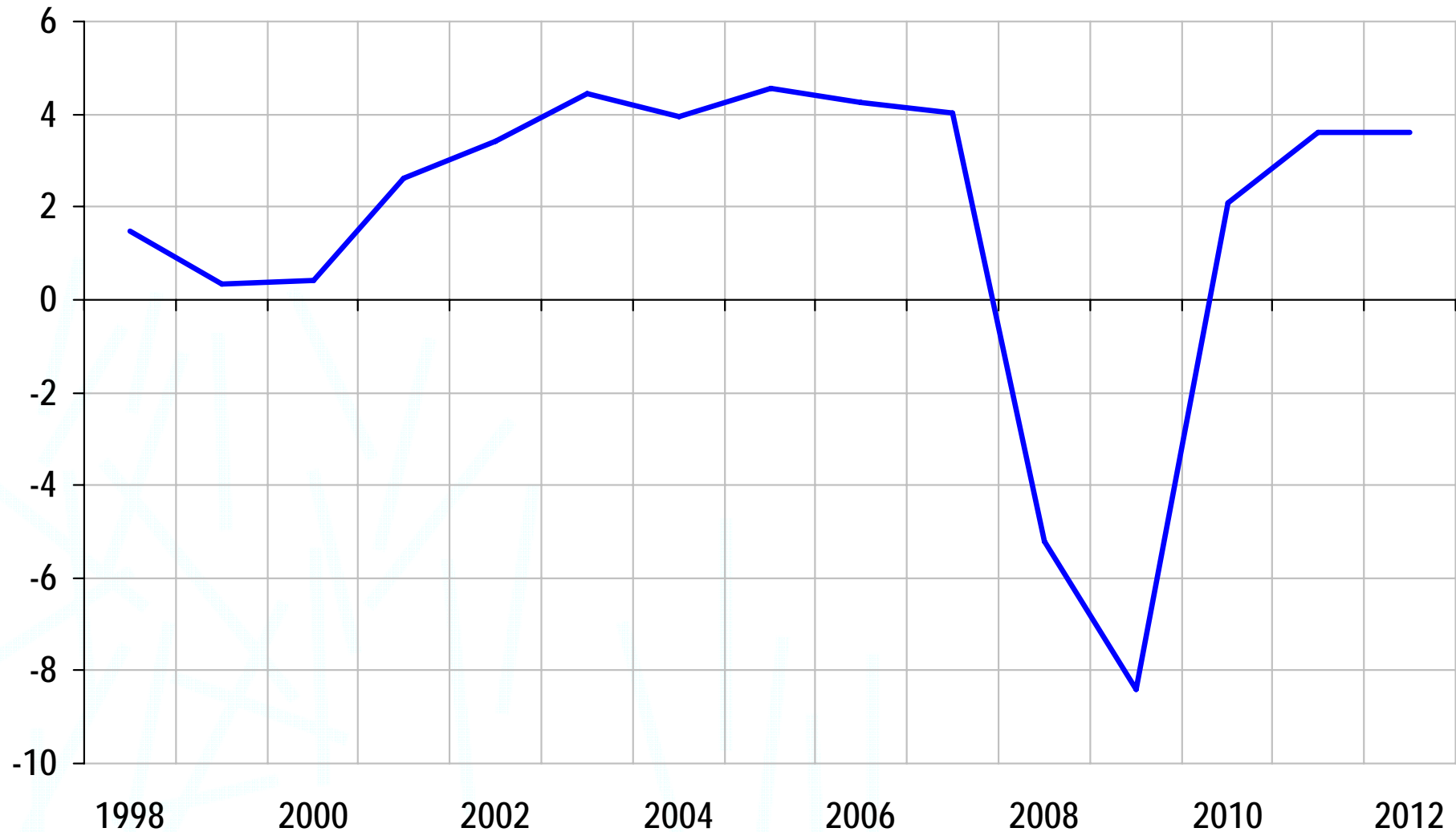
Financial services contract, dragging business service growth down

London services sub-sector output, real annual percentage change



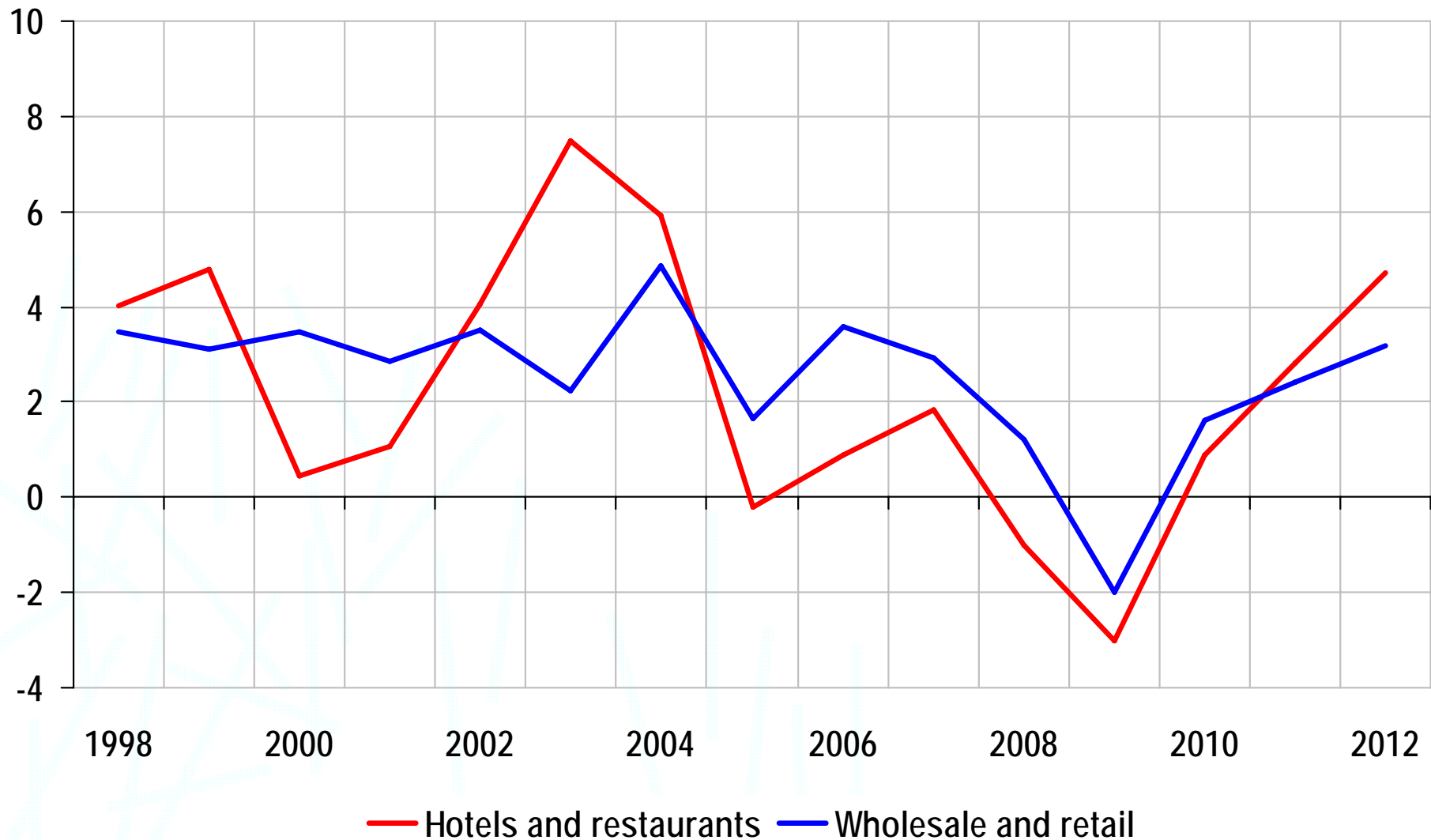
Construction sector in recession

London construction output, real annual percentage change



Under pressure consumer to hit growth in retail and hospitality

London services sub-sector output, real annual percentage change



London earnings to show more pronounced cycle than UK

London and UK average earnings, nominal annual percentage change



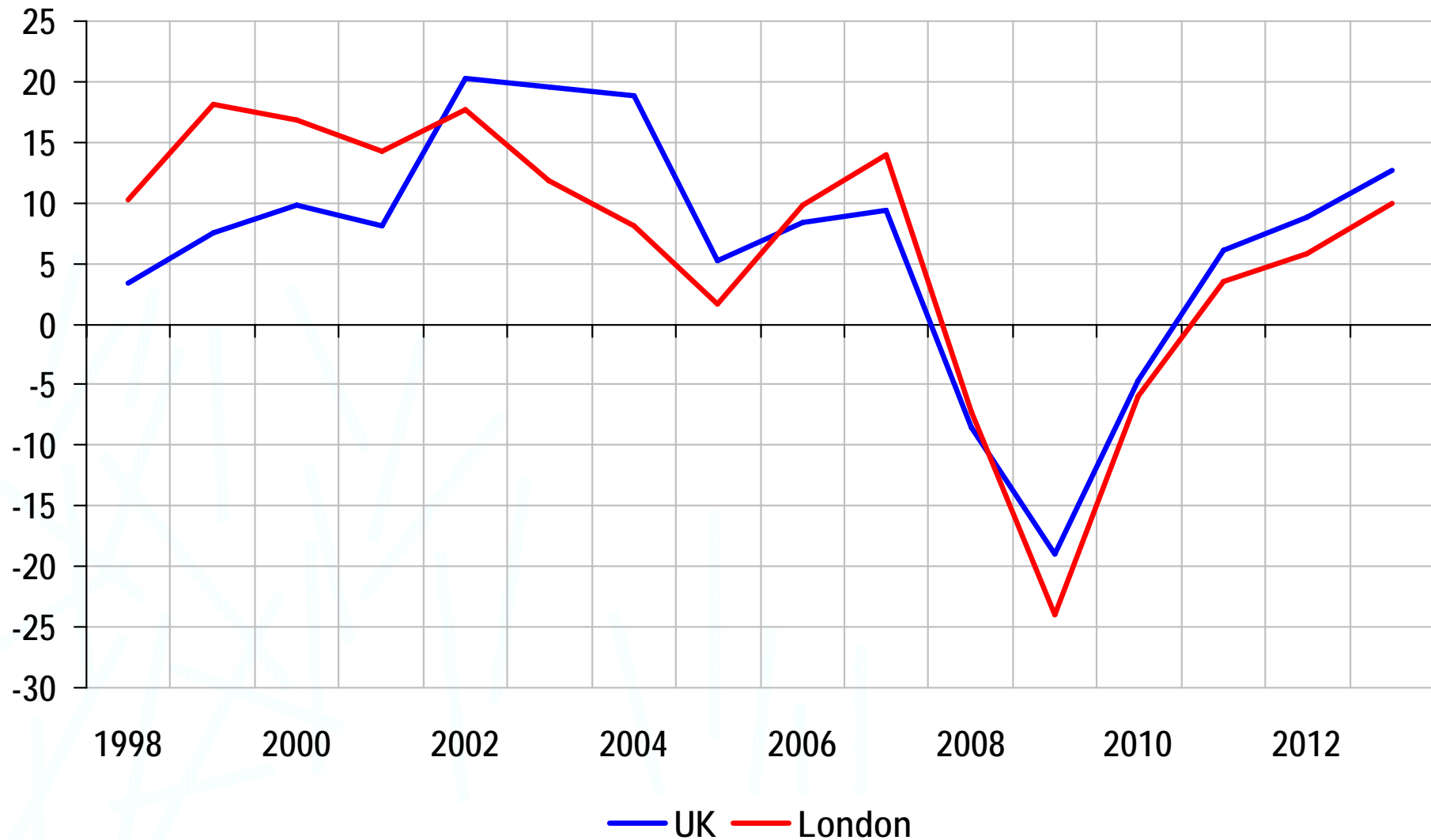
Unemployment is set to soar

London and UK unemployment, percentage of working age population, claimant count



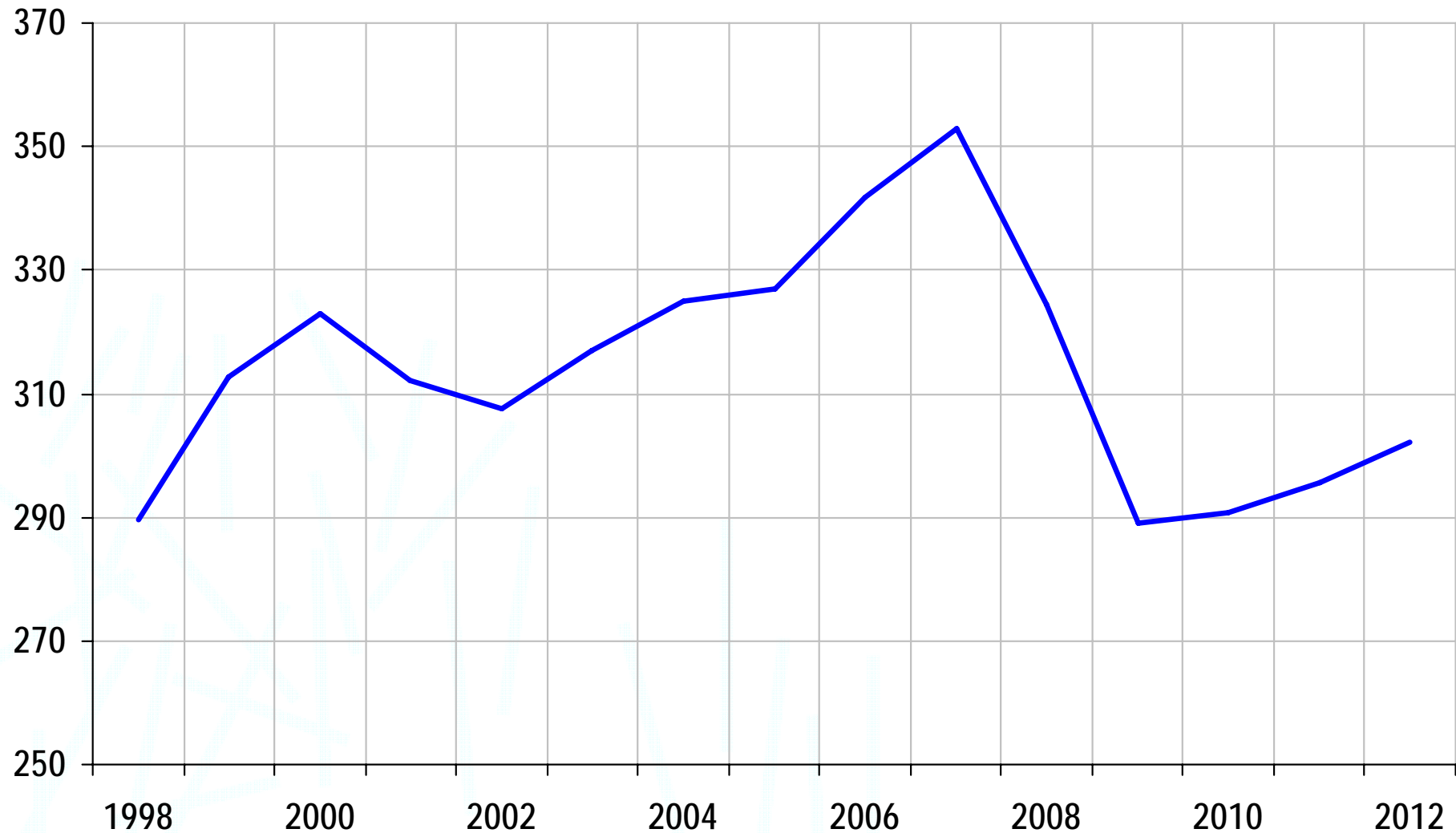
London house prices to underperform the UK

London house price inflation, annual percentage change



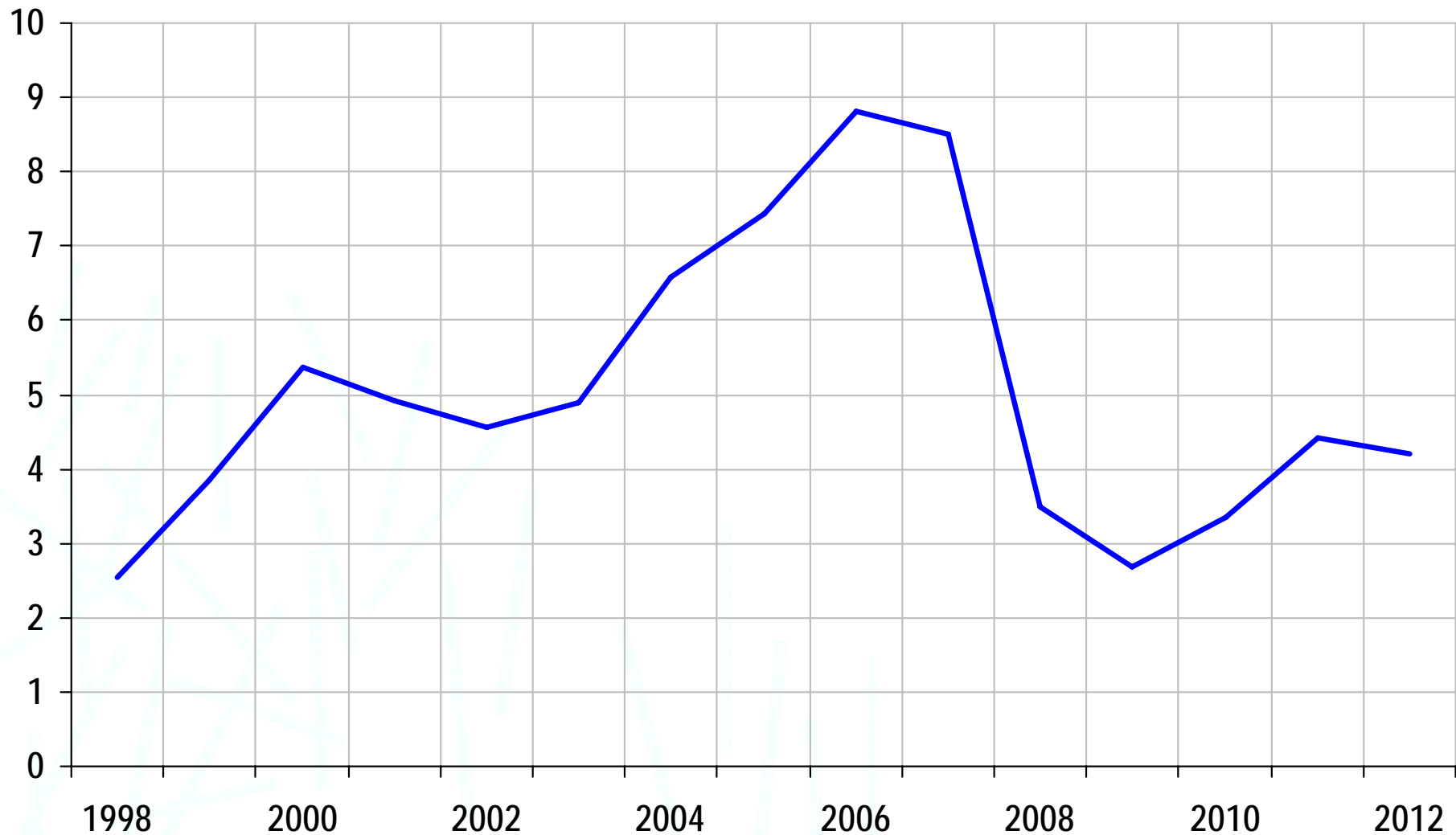
Current crisis will set the City back a decade, with 62,000 jobs lost

City-type jobs in London, annual average, thousands



City bonuses down 70 per cent from peak

City bonuses, annual payments, £ billion



Five critical success factors for the London economy

~~the international economic environment~~

~~competitiveness of the City~~

~~London's role in supplying business services~~

- housing
- transport

Critical success factors for 2009 and beyond

- Stabilisation in asset values (equities and house prices)
- Recovery in the US then Asia and Europe
- Efficient regulatory changes in finance and banking
- Taxation in the UK
- Banking recovery
- A non protectionist world



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