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Growth, Future Potential and Opportunities for Issuers in the United Kingdom‘s Islamic Finance Sector

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2013 outlook

2012 proved disappointing for most advanced economies as unemployment remained stubbornly high and output wavered between expansion and contraction.

The threat of a *Greek* exit from the euro dominated headlines for much of the year, but the authorities, for now, have shown signs that they are prepared to do what is needed to keep the currency zone intact. That said, the situation remains precarious and the eurozone economy is in recession again.

For now, *Europe* has adopted a *de facto* policy of muddling through. This could continue for some time. But ultimately a choice will have to be made - or the risk is one will be forced on the continent by the financial markets.

The *US* has perhaps the brightest prospects of all the major advanced economies. But this optimism could prove short-lived. In pure economic terms there is evidence the worst may be over. The housing market recovery has picked up steam, unemployment is dropping and banks are showing an increased willingness to lend.

The UK is not without its policy challenges either. Those arguing for a slowdown in the pace of deficit reduction have become increasingly vocal as growth has persistently disappointed. The weak economy is itself frustrating the deficit reduction strategy and ratings agencies have responded by threatening the UK's triple A rating. Should a downgrade be forthcoming, however, it will most probably excite the politicians but do little to alter the view of the markets.

2013 outlook

The real economy is still in the shadow of the financial crisis. Over-indebted consumers are saving rather than spending, and faced with huge uncertainty, businesses are sitting on cash rather than investing. So public sector cutbacks are reinforcing private sector retrenchment in constraining growth. At the same time, the global slowdown, in particular recession in Europe, severely limits the scope for exports to come to the rescue.

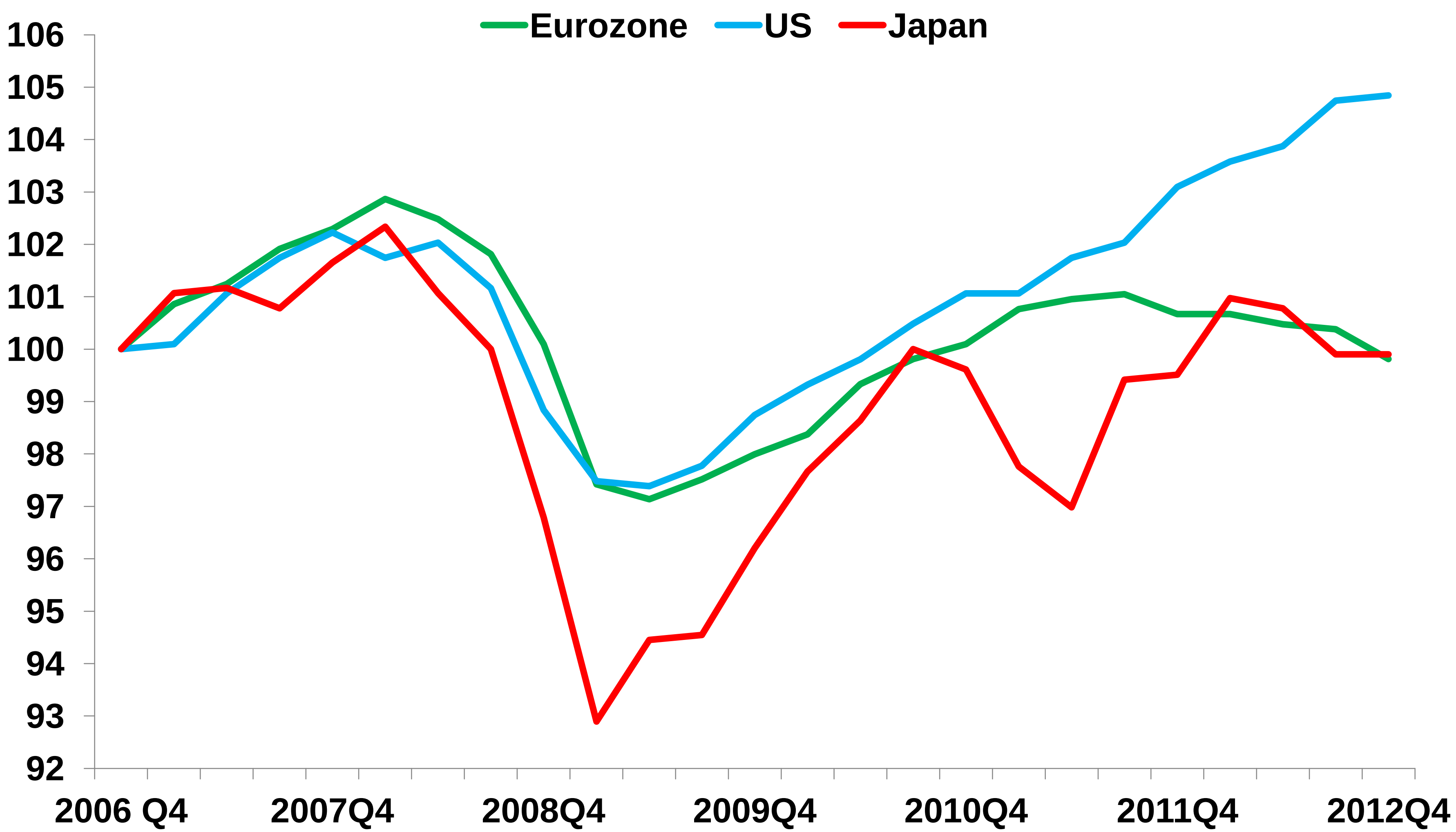
More positively, in the personal sector balance sheet repair is underway, employment is rising and the squeeze on real wages may be starting to ease. However, "austerity" means what it says on the tin, and without a change in policy, getting even weak growth for 2013 may require further stimulus from the Bank of England.

Elsewhere, the pace of expansion of many emerging economies has slowed as a myriad of domestic challenges coexist against the backdrop of troubles in the West. However, whilst growth has decelerated, it has not stalled. Once again the IMF expects the emerging markets, more generally to take the lion's share of world growth.

And we mustn't forget Japan. While currently struggling, it is still the world's third largest economy and hopes are high that a new Government will sanction aggressive stimulus measures.

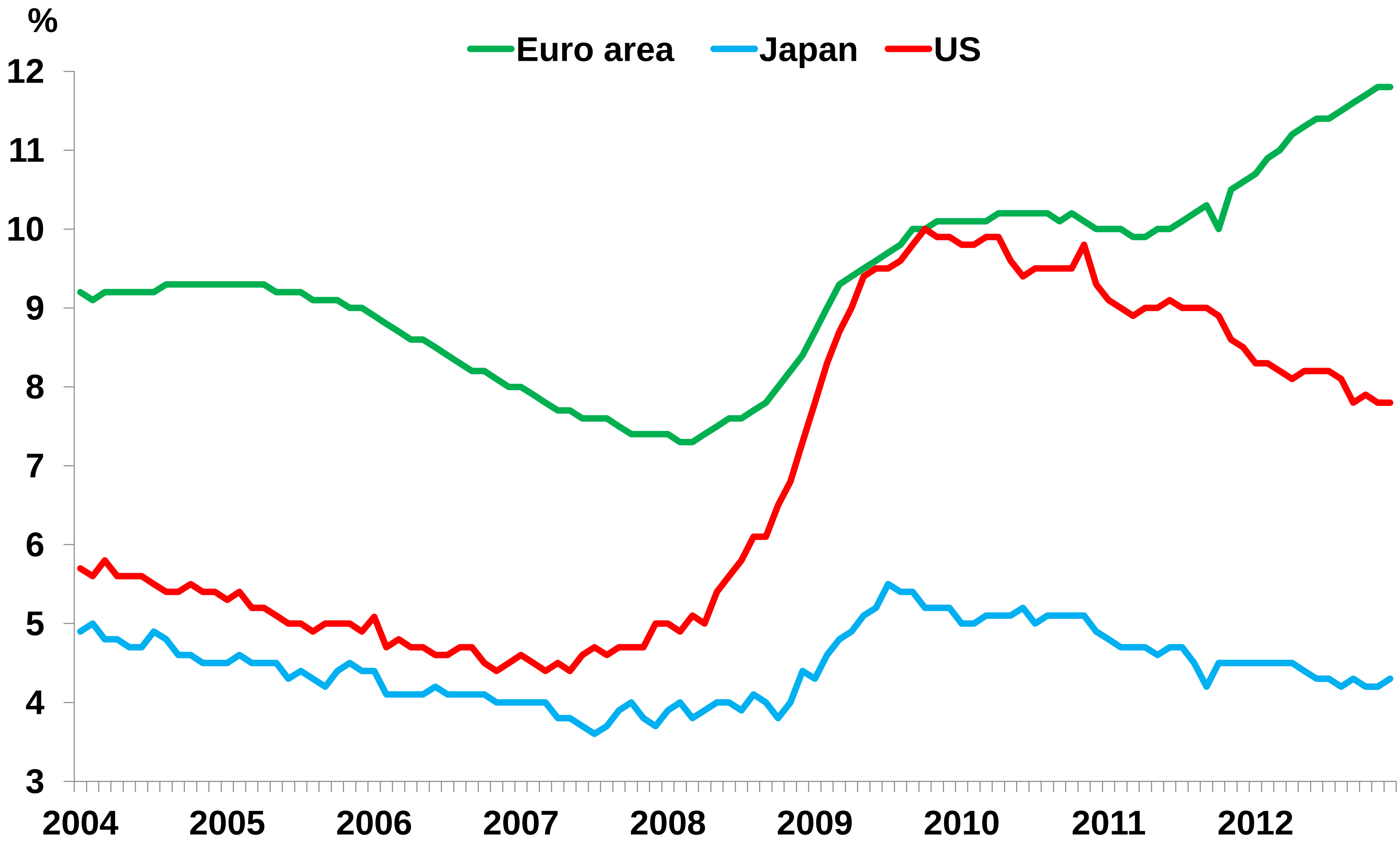
So the world stumbles on. Whether 2013 proves to be another disappointment or the start of a sustained recovery remains to be seen.

Global GDP by region (2006 = 100)



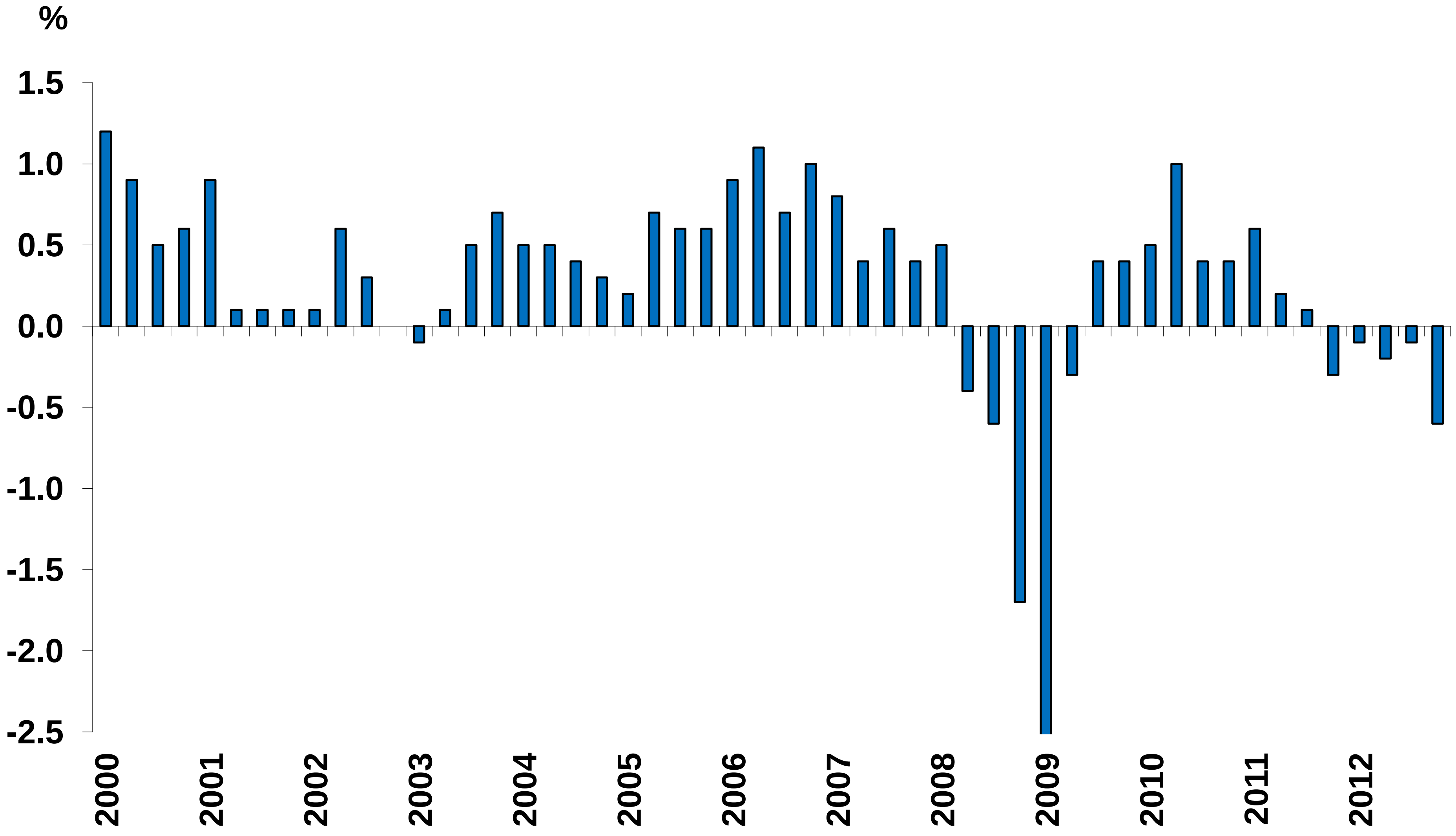
Source: Eurostat/ IMF

Unemployment



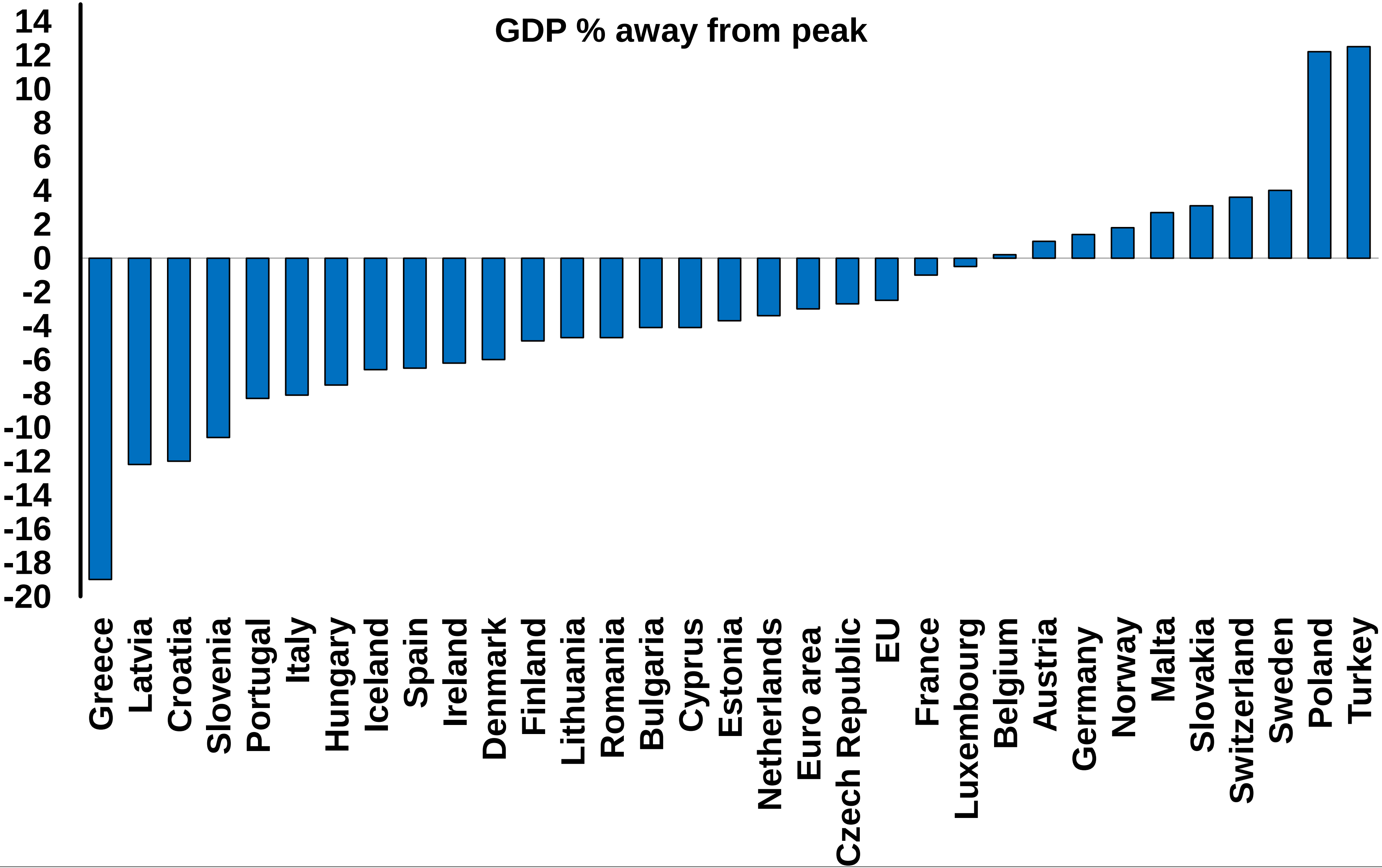
Source: BEA/ Japan Stat/ Eurostat

Eurozone: GDP (quarter-on-quarter)



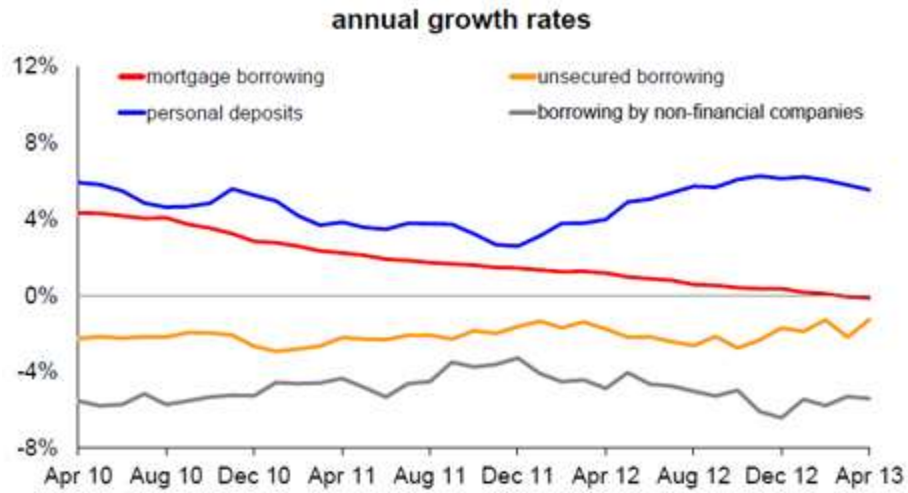
Source: Eurostat

“Recoveries” to date



Source: Eurostat

Banks seem to have a lot of money, so why aren't they making more loans?



Banks seem to have a lot of money, so why aren't they making more loans?

The Bank of England announced that overall net lending fell by £2.4bn in the final quarter of 2012 compared with the previous three months.

The British Bankers Association (BBA) said lending to 4 million small and medium-sized businesses fell by £382m in the last quarter of 2012.

Banks have cut the amount they lent to retailers by 5.7% in the year to the end of December 2012. Over the last three years, loans to High Street shops have fallen by more than 18%. Recent casualties in the High Street have included Comet, Jessops, Blockbuster and Republic.

Are any banks lending more?

Barclays:	**+ £1.8bn**
Nationwide:	**+£1.7bn**
Lloyds Group:	**- £3bn**
Santander:	**-£2.8bn**
RBS:	**-£1.6bn**

Banks seem to have a lot of money, so why aren't they making more loans?

Some of the banks are still trying to increase their reserves, rather than lend more money out.

Banks' lending standards and conditions mostly remain stricter than they were prior to the crisis

The top UK banks recorded loan impairment charges of c. £60 billion p.a. for past few years.

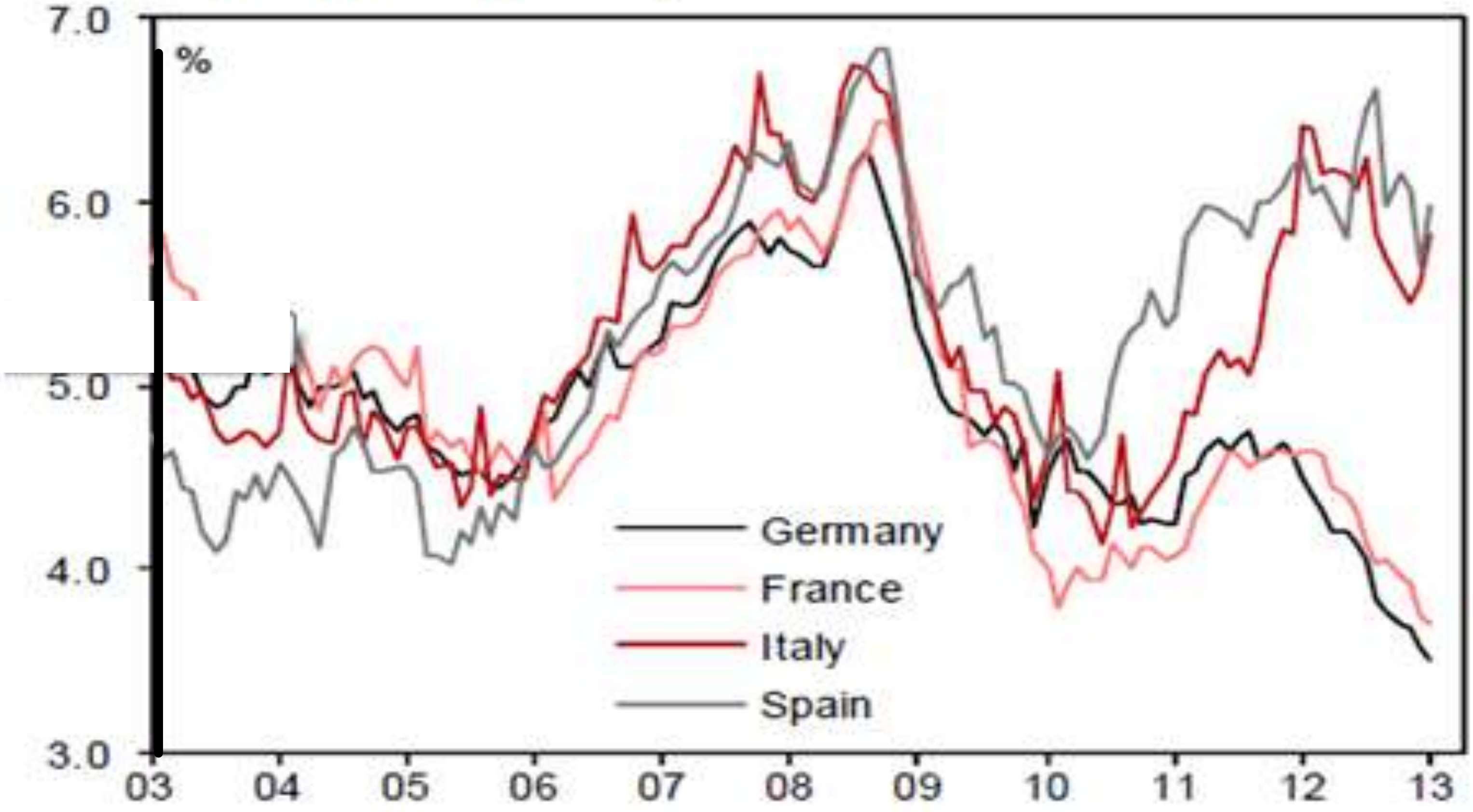
Some believe that enhanced supervision and regulation has made it more difficult for banks to expand their lending.

The BBA said small and medium-sized businesses were sitting on large cash reserves and choosing to pay down their debts, rather than borrow more. Some large, high-quality firms have been issuing long-term corporate bonds, which generate funds they can use to pay down their bank debt.

Bank of England considering "extraordinary" policies to encourage more business lending, including the idea of charging High Street banks a negative interest rate. This would encourage banks to lend cash to small firms, rather than pay to deposit it with the Bank of England.

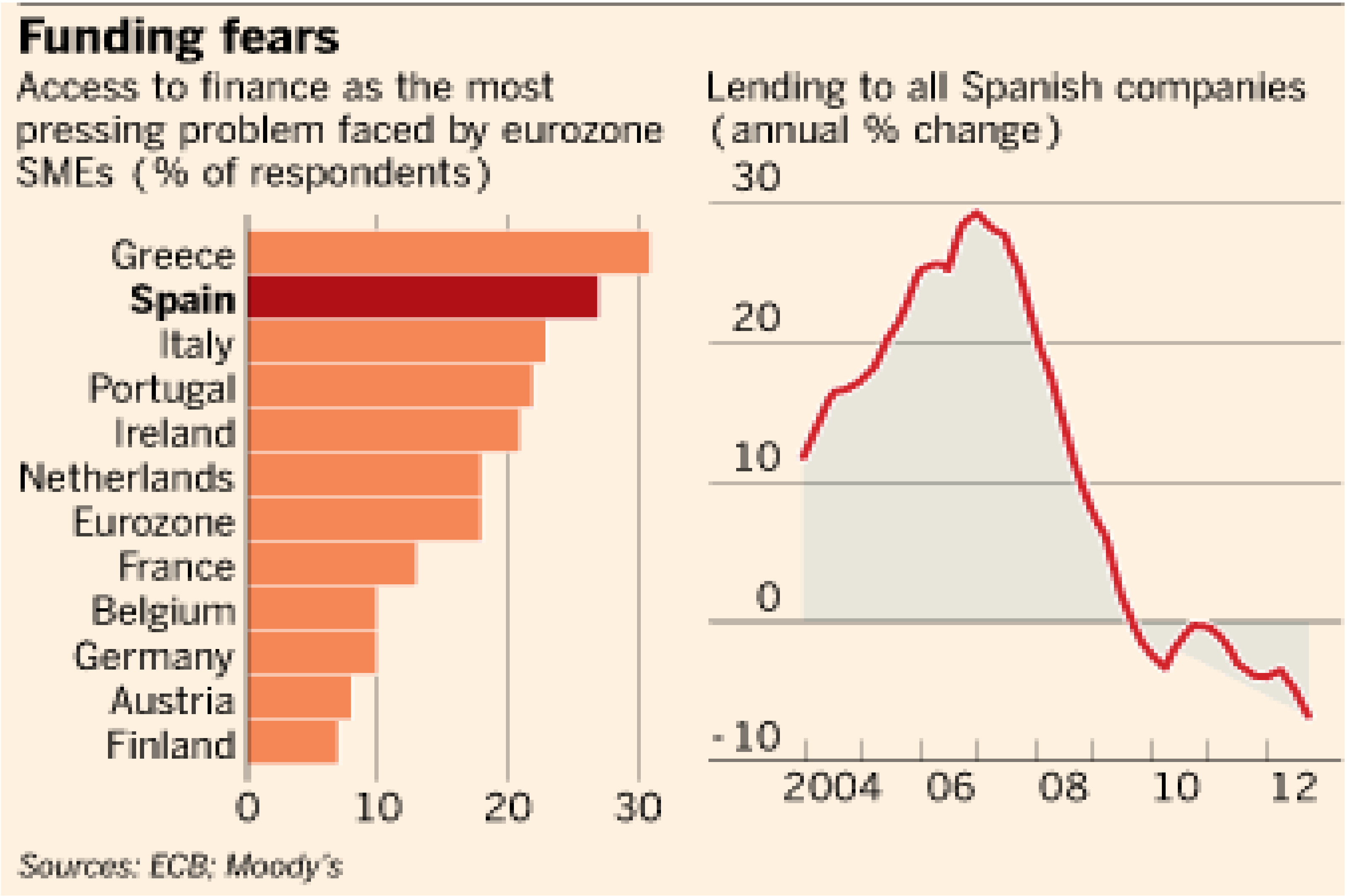
Bank lending rates - Europe

Bank lending rates to companies remain divergent
% pa, interest rates on business loans up to EUR1mn with maturity between 1 and 5 years

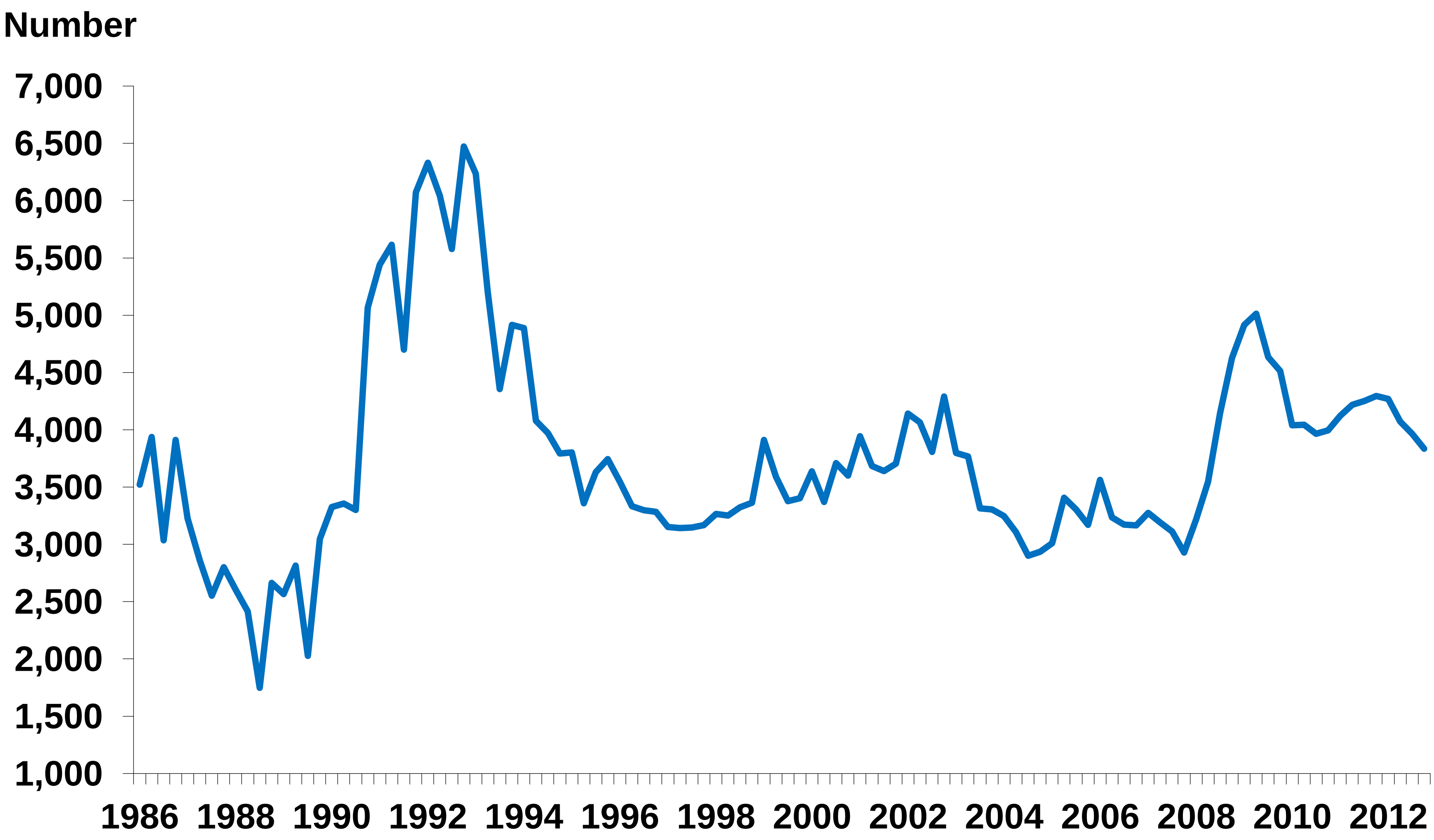


Source: GS Global ECS Research.

Funding fears - Europe

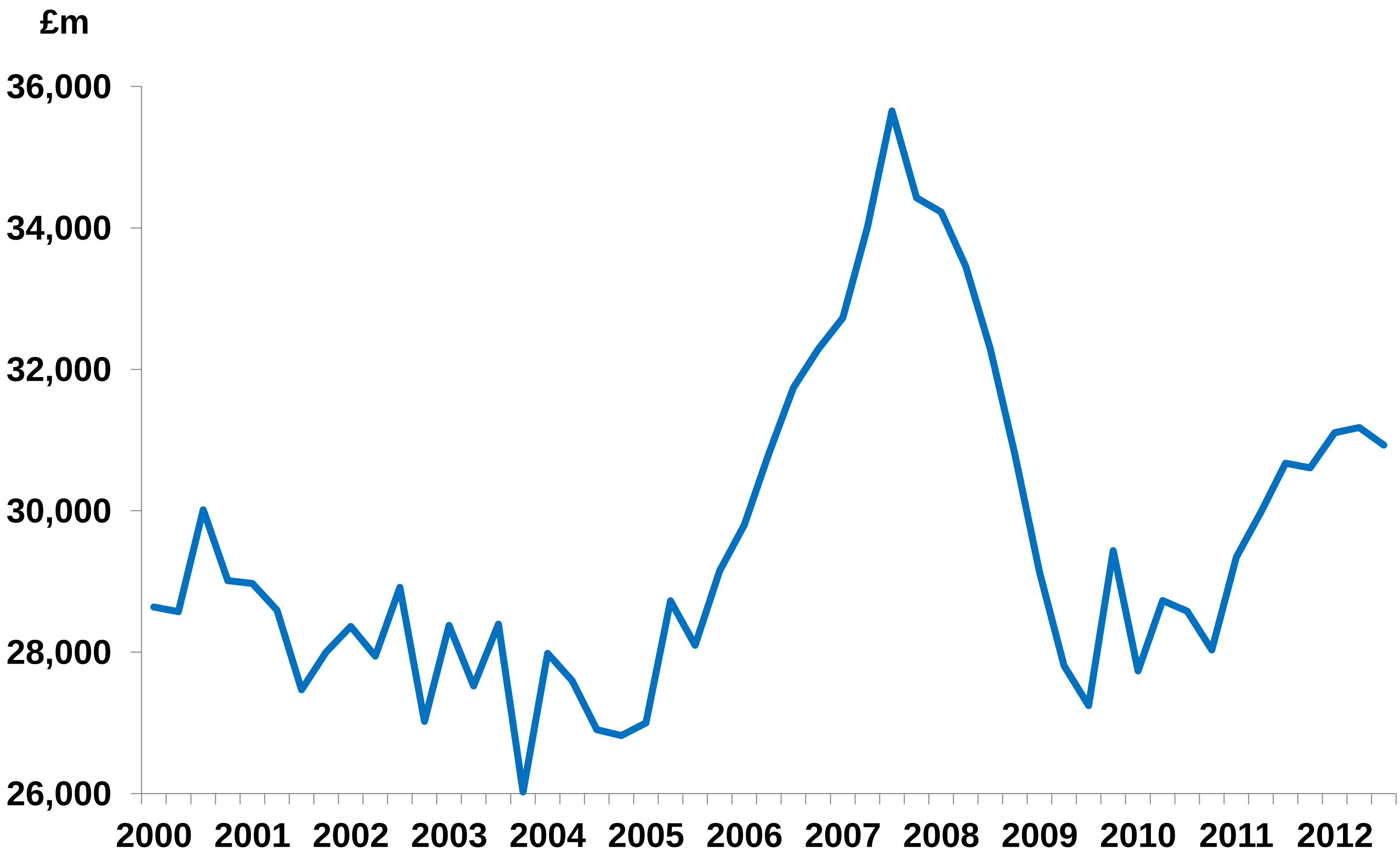


Company insolvency puzzle – England and Wales



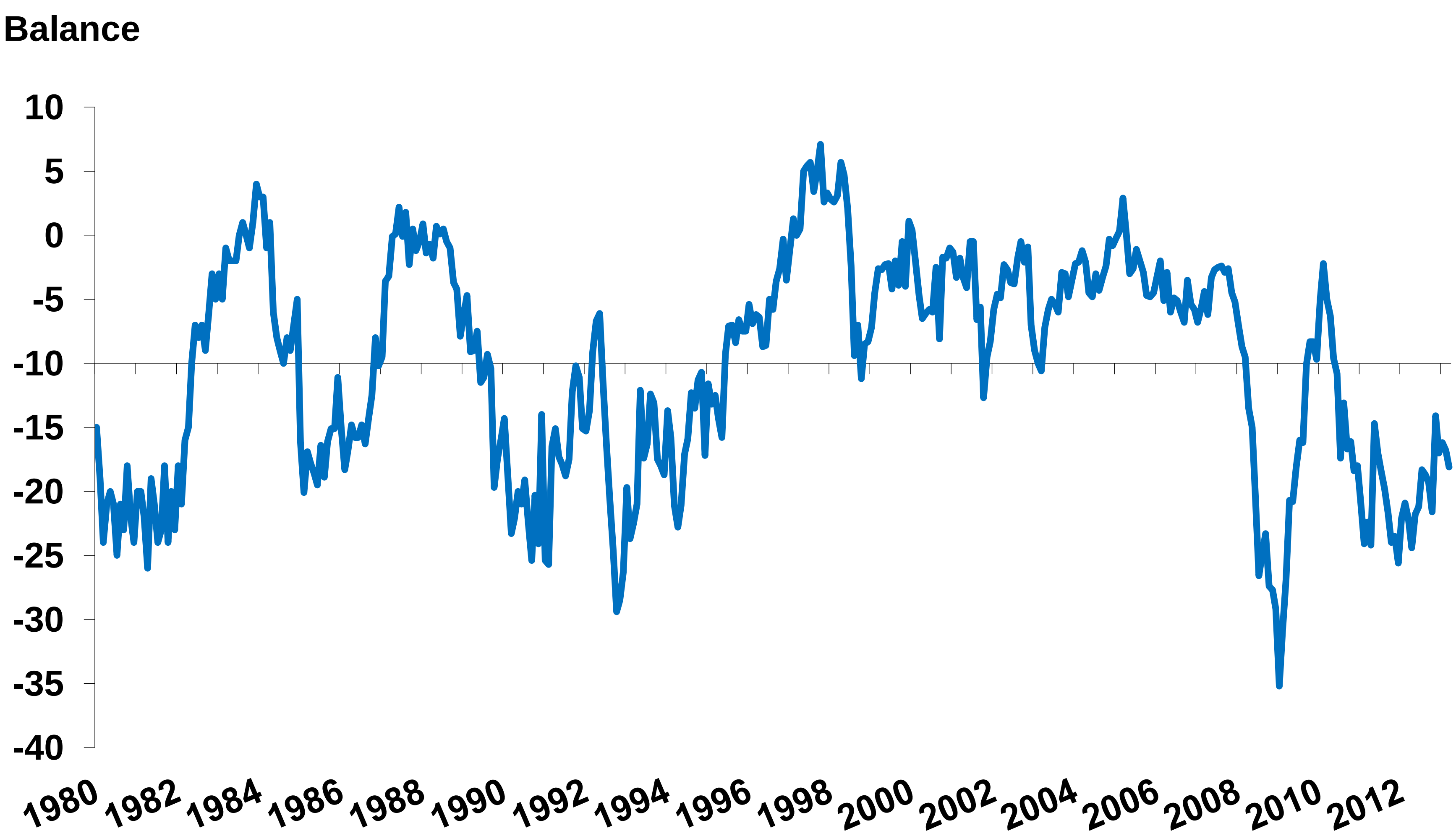
Source: Insolvency Service

UK – business investment (quarterly)



Source: ONS

UK: consumer confidence



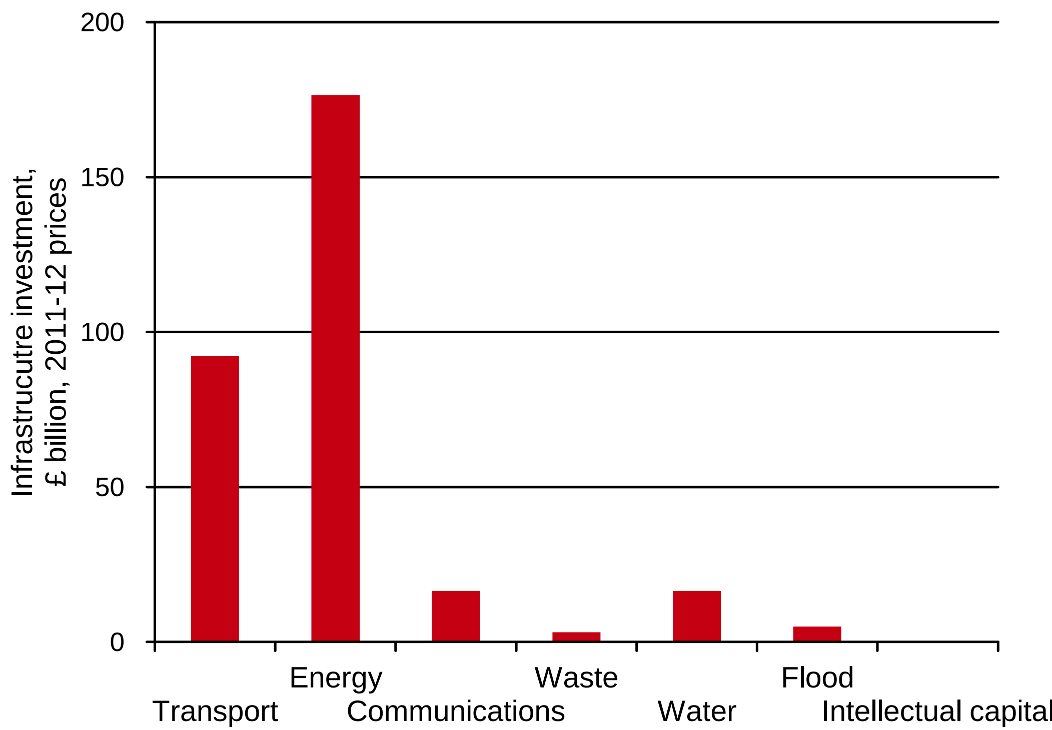
Source: DataStream

The UK Infrastructure investment pipeline

The 2012 infrastructure pipeline update includes over ***550 projects*** and programmes and is worth over ***£310 billion***.

Most of the investment is contained within major programmes – for example ***highways, rail, energy, offshore wind and broadband***.

Over 85 per cent of the expected investment to 2015 and beyond will be privately funded in full or in part. The remainder will be publicly funded.



Looking forward...

- Depends on your expectations – consensus has got so gloomy most people would be grateful for anything!
- Stronger equity markets help to generate confidence and spending
- Progress in corporate balance sheet repair
- Upturn in business investment in UK and US
- Ambitious infrastructure plans of UK Government
- But what hope for Europe?
- Many attractive/Sharia'a compliant corporate and public assets which could be used for sukuk issuances
- UK corporate sukuk precedent already taken place – why no others?
- Now is the time for alternative forms of finance & capital!

Thank You

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