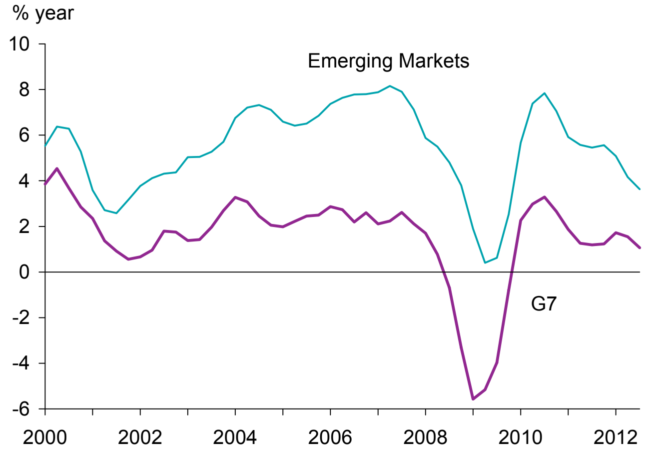
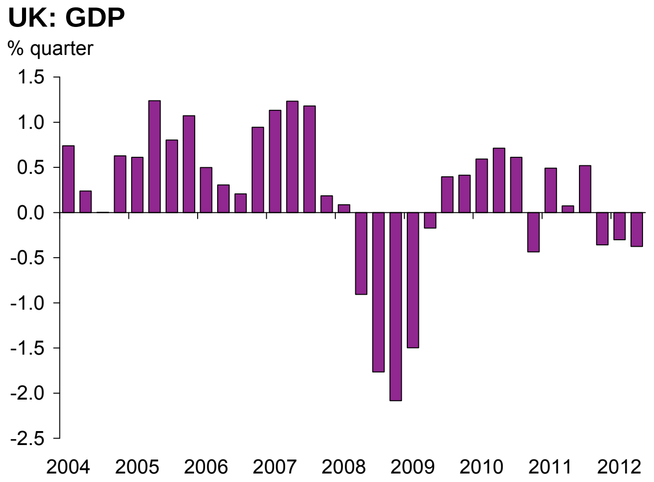
The global economy is in the midst of a slowdown…

G7 & Emerging Markets: GDP growth



Source: ITEM Club

…and the UK had been at the forefront…



Source : Haver Analytics

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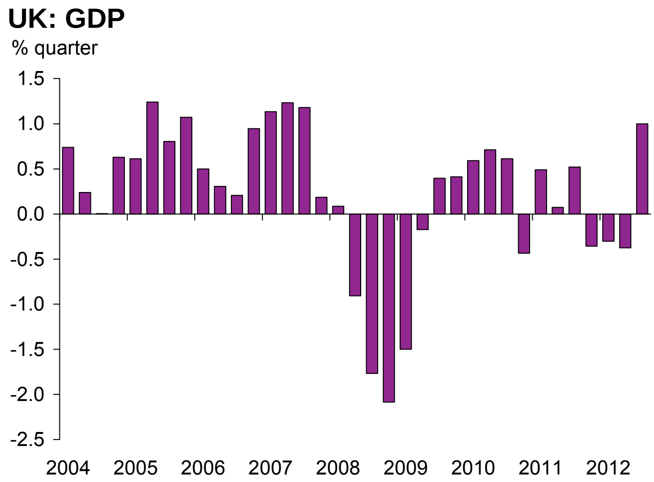
…until growth jumped in Q3

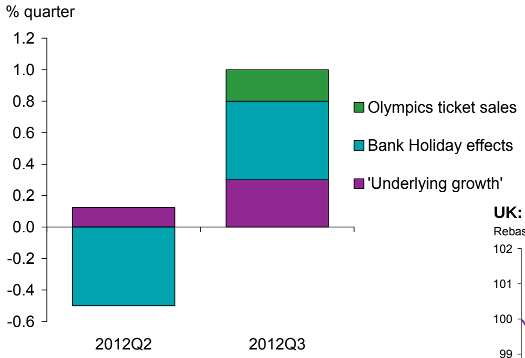


Source : Haver Analytics

Page 3

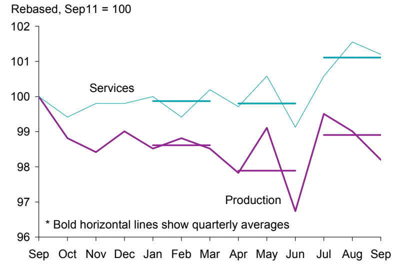
Don't get too excited…most of the growth was due to temporary factors

UK: Decomposing GDP growth



Source : Haver Analytics / ITEM Club

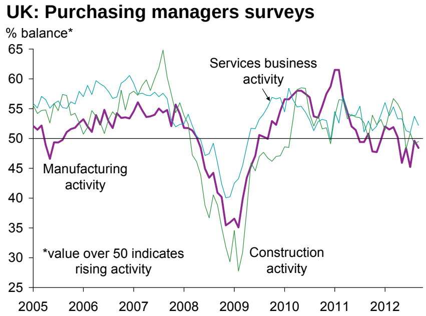
UK: Monthly output estimates



Source : Haver Analytics

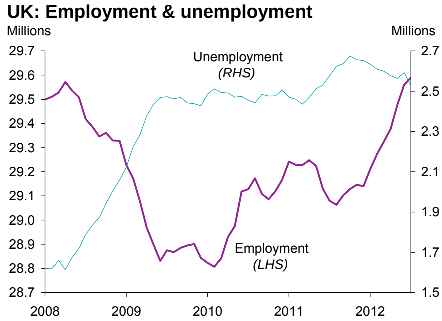
But other evidence suggests the UK economy isn't in too bad a state

UK: Purchasing managers surveys



Source : CIPS/Markit

UK: Employment & unemployment



Source : Haver Analytics

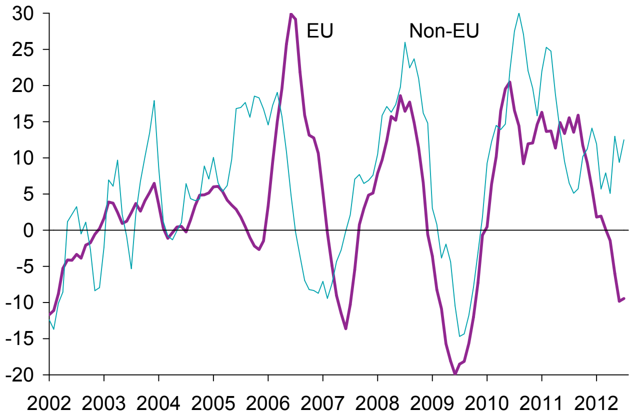
External outlook remains troubling

- UK exports to EU down almost 10% over last year
- Eurozone weakness is extending to other export markets

UK export demand has collapsed

UK: Goods exports by destination

3m-on-3m, yr ago



Source : Haver Analytics

External outlook remains troubling

- UK exports to EU down almost 10% over last year
- Eurozone weakness is extending to other export markets
- Draghi's intervention has reduced the threat of imminent Eurozone breakup and calmed financial markets…

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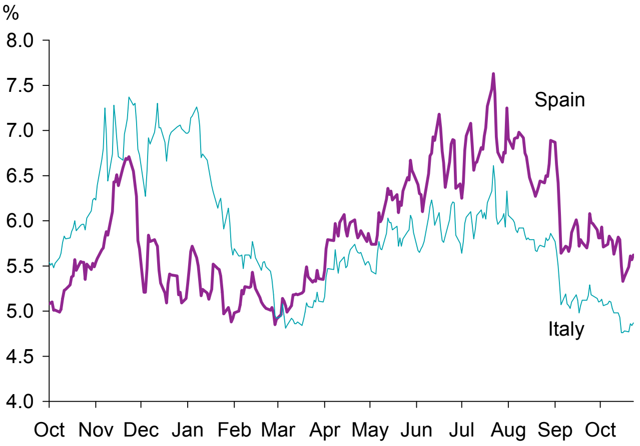
Draghi's intervention has calmed markets and bought some time

Eurozone: 10-year government bond yields



Source : Haver Analytics

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External outlook remains troubling

- UK exports to EU down almost 10% over last year
- Eurozone weakness is extending to other export markets
- Draghi's intervention has reduced the threat of imminent Eurozone breakup and calmed financial markets…
- …but still much work to do and policymakers need to deliver on their promise to do what it takes to save the single currency

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What is needed to hold Eurozone together? (1)

The Eurozone has ammunition to deal with crisis but needs to act swiftly:

- **ECB even more interventionist**
  - ECB/ESM buys unlimited amounts of government bonds in peripherals to hold down yields ✓
  - More Long Term Refinancing Operations (LTRO) against poorer quality collateral if necessary
  - Outright QE – widespread purchases of bonds and other assets to boost money supply growth across the Eurozone and weaken the euro
- **More bailouts**
  - Greece allowed to not pay interest on debt to IMF, ECB etc and debt restructured
  - Full bailout for Spain
  - Further bailout for Portugal

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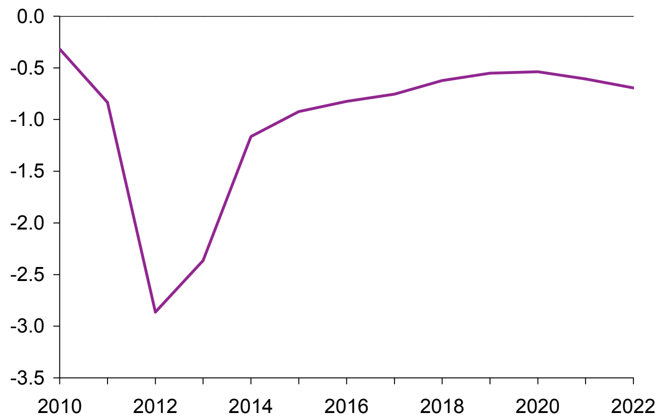
What is needed to hold Eurozone together? (2)

- **Move towards fiscal & banking union**
  - ECB to supervise all banks and set common rules
  - Eurozone-wide deposit guarantee scheme
  - ESM to grant loans to banks
  - Formalisation of transfers in fiscal union – including Eurozone bonds
- **Change in macro policy**
  - Reviving the Growth pact
  - Looser fiscal policy where there is room
  - ECB (and Bundesbank) tolerate higher inflation in Germany

Eurozone to remain intact but experience a ‘lost decade’

Eurozone: GDP growth

% point difference from historical average (2.3% pa)



Source : ITEM Club

External outlook remains troubling

- UK exports to EU down almost 10% over last year
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- In the US, QE3 should provide a boost, but it still needs to negotiate the fiscal cliff

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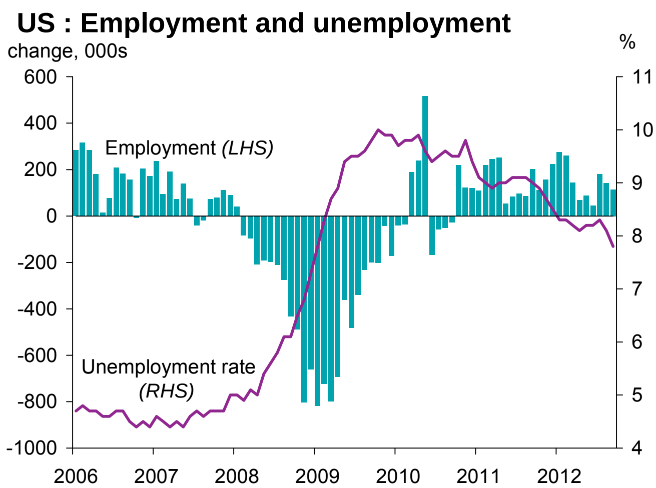
Disappointing 2012H1 in the US…



Source: Haver Analytics

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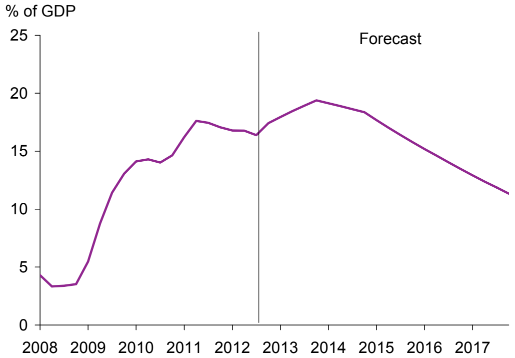
…brought about QE3 from the Fed

US: Quantitative Easing



Source : ITEM Club

- Focus on mortgage-backed securities:
  - Additional, cheaper financing for mortgages
  - To help revive the moribund housing and construction sectors
- Strong commitment from the Fed: 'highly accommodative stance'…'for a considerable period of time after the economic recovery strengthens'

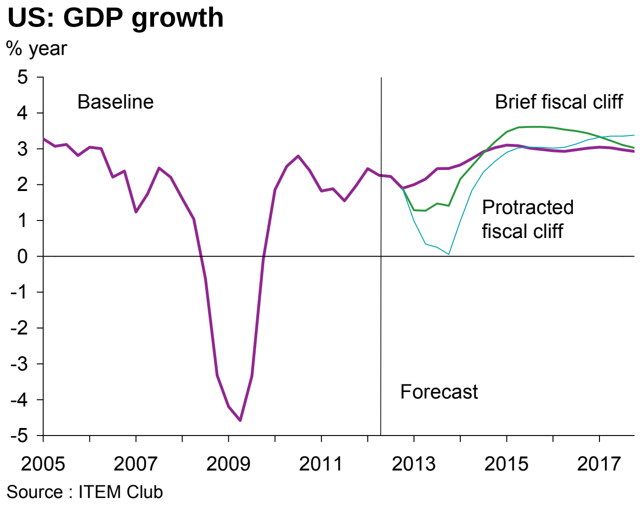
But fiscal cliff still looming on the horizon…

US fiscal cliff - 2013

Measure	Cost ($bn)
Payroll tax holiday	125
Bush tax rates, estate tax, AMT patch	295
Other tax measures	210
Medicare provider payment fix	15
Spending cuts	120
Extended unemployment benefits	35
Total	**800**
(% of GDP)	**4.9**

Source: ITEM Club

…and the fiscal cliff would push US close to recession



External outlook remains troubling

- UK exports to EU down almost 10% over last year
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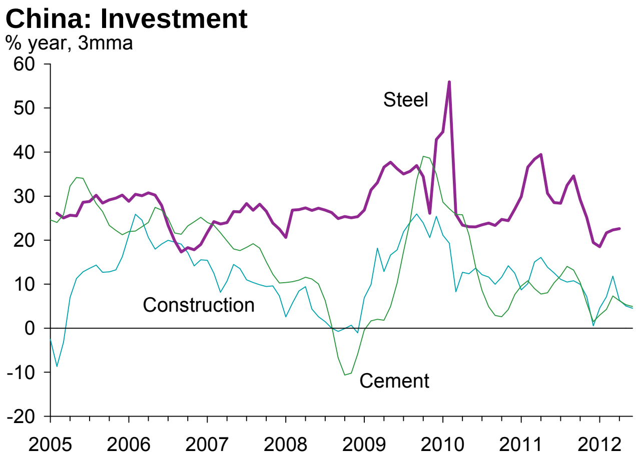
- Draghi's intervention has reduced the threat of imminent Eurozone breakup and calmed financial markets…
- …but still much work to do and policymakers need to deliver on their promise to do what it takes to save the single currency
- In the US, QE3 should provide a boost, but it still needs to negotiate the fiscal cliff
- While prospects for the rapid growth markets are less bright than they were last year

Page 19

China is trying to 'soft land' its housing and construction sectors…



Source : CEIC

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…which is spilling over to other emergers

Source : PMI/Markit/China NBS/Haver Analytics

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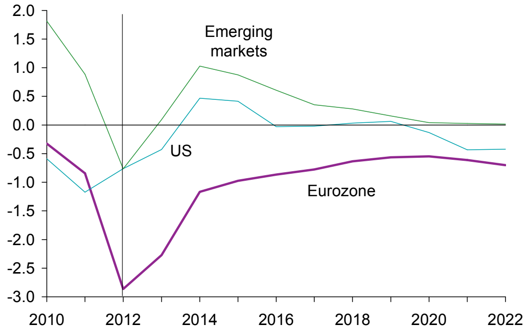
Eurozone crisis remains key to UK prospects

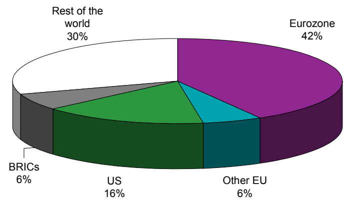
World: GDP growth

% point difference from historical average



Source : ITEM Club

UK: Goods & services exports by destination (2011)



Source : ONS 'Pink Book'

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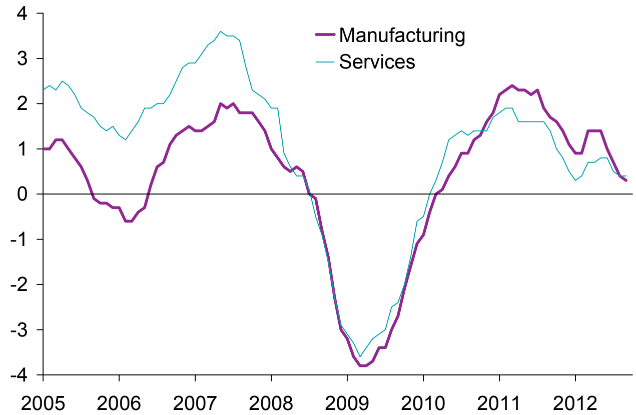
Uncertain global outlook continues to harm corporate confidence

UK:BoE agents' survey: Investment intentions

% balance



Source : Haver Analytics

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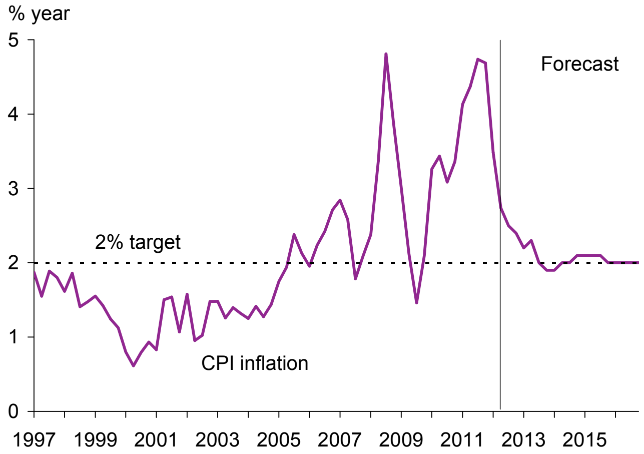
But domestic storm forces are easing

- Falling inflation and rising employment are set to spark a consumer recovery

Falling inflation will support household finances

UK: Inflation relative to target



Source: ITEM Club

But domestic storm forces are easing

- Falling inflation and rising employment are set to spark a consumer recovery
- While the mortgage and housing markets are now primed for recovery next year, reversing another strong headwind…

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The stage is now set for lending to resume

- Strong inflows of savings deposits and lending restraint allowed the official support to be finally repaid last year
- The funding gap is now just £200bn, making the banks more resilient

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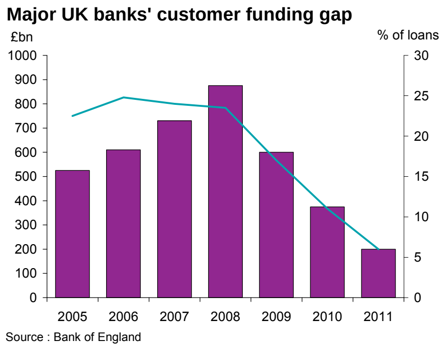
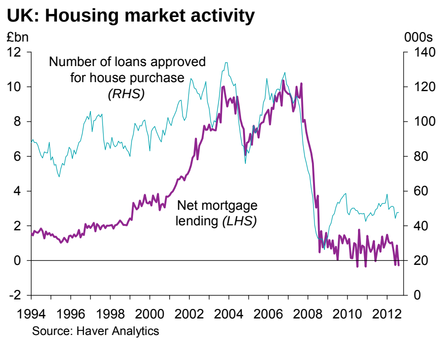
Closing the funding gap has hammered the housing market





Prior to the crisis only 50% of mortgage lending came from retail deposits – the rest was financed through securitisation and overseas borrowing. This had to be repaid in a hurry when the crisis struck – through Bank of England support and lower lending

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The stage is now set for lending to resume

- Strong inflows of savings deposits and lending restraint allowed the official support to be finally repaid last year
- The funding gap is now just £200bn, making the banks more resilient
- Now regulators are more relaxed, encouraging lending
- The cost of money market funding has fallen by nearly 1½% in 6 months
- Funding for Lending Scheme provides a big incentive
- Now, deposit inflows can be used to support lending again

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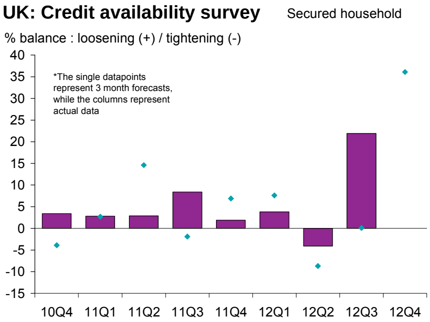
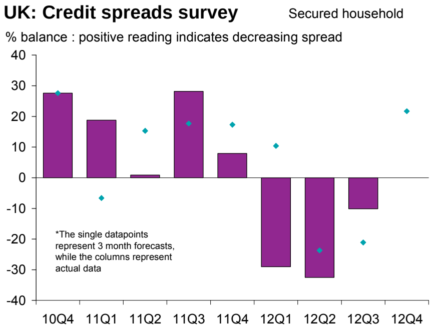
Banks are signalling a dramatic loosening of credit conditions…



Source : Bank of England



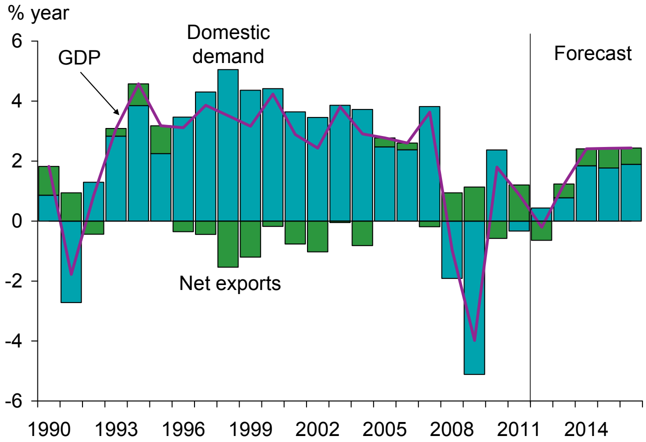
Source : Bank of England

But domestic storm forces are easing

- Falling inflation and rising employment are set to spark a consumer recovery
- While the mortgage and housing markets are now primed for recovery next year, reversing another strong headwind…
- …though the scale of this revival depends upon the demand for mortgages, which remains uncertain given the household sectors' efforts to deleverage
- However about half of the necessary adjustment has already been made, leaving many families in a position to consider taking on new financial commitments.

Slow & 'unbalanced' recovery in the short-term

UK: Contributions to GDP growth



Source: Oxford Economics

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ITEM Club forecast – Autumn 2012

The ITEM Club forecast for the UK Economy, Autumn 2012
% changes on previous year except borrowing, current account and interest & exchange rates

	GDP	Domestic Demand	Consumer spending	Fixed investment	Exports	Imports
2009	-4.0	-4.0	-3.1	-13.7	-8.2	-11.0
2010	1.8	1.5	1.3	3.5	6.4	8.0
2011	0.9	-0.7	-0.9	-2.4	4.5	0.5
2012	-0.2	1.0	0.6	1.4	0.6	2.6
2013	1.2	0.4	0.8	2.0	6.2	4.5
2014	2.4	1.8	2.0	6.8	6.9	5.0
2015	2.4	1.8	2.2	6.5	6.8	4.9

	Net Govt Borrowing(*)	Current account (% of GDP)	Average earnings	CPI	3-month interest rate	Effective exchange rate
2009	10.9	-1.3	1.8	2.2	1.2	80.6
2010	9.4	-2.5	2.4	3.3	0.7	80.5
2011	8.1	-1.9	2.6	4.5	0.9	79.9
2012	6.4	-3.4	2.0	2.8	0.9	83.2
2013	6.3	-0.9	2.8	2.1	0.8	84.2
2014	4.6	0.0	3.2	2.0	1.6	83.6
2015	3.2	0.9	3.9	2.0	2.5	81.8

(*) Fiscal years, as % of GDP
Source: ITEM Club

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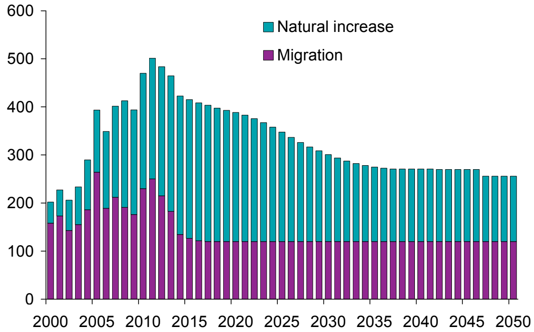
Demographics are likely to be less supportive going forwards…

UK: Population forecasts

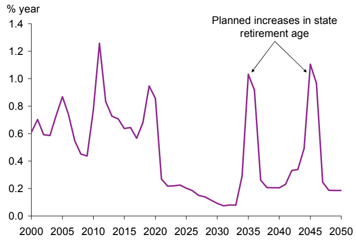
Annual change (000s)



Source : ITEM Club

UK: Working age population

% year



Source : ITEM Club

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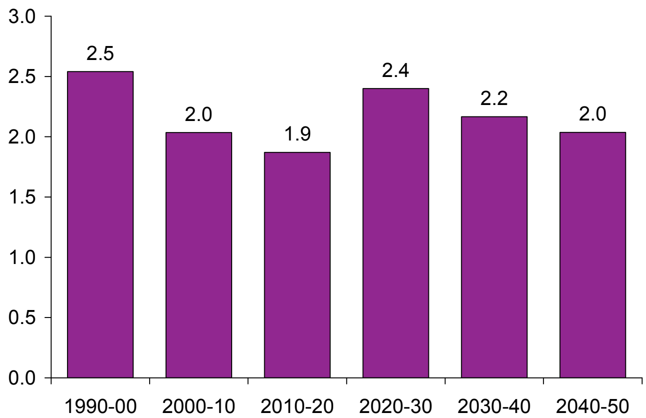
…pointing to slower growth over the longer term

UK: GDP

Average anunal growth, %



Source : ITEM Club

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Implications for business

- The UK looks to have passed the bottom and is on the road to recovery. But that road will be long and bumpy
- For the first time in five years there is light at the end of the tunnel for UK households and consumer-facing businesses
- But the problems in the Eurozone will take a long time to resolve and the area faces a lost decade. Given the importance of the Eurozone to UK exports, this will have a major influence on UK growth prospects
- Deleveraging by consumers and the Government will weigh on the medium term outlook – this will not be a ‘normal’ recovery
- The challenges of an ageing population mean that over the longer term, growth may never get back to the rates achieved prior to the crisis

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Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

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About ITEM Club
The ITEM Club is the only non-governmental economic forecasting group to use the HM Treasury's model of the UK economy. ITEM stands for Independent Treasury Economic Model. HM Treasury uses the UK Treasury model for its UK policy analysis and Industry Act forecasts for the Budget. ITEM's use of the model enables it to explore the implications and unpublished assumptions behind Government forecasts and policy measures.

Uniquely, ITEM can test whether Government claims are consistent and can assess which forecasts are credible and which are not. Its forecasts are independent of any political, economic or business bias.