BARCLAYS

Corporate Banking

UK Charities

Sector outlook

First quarter 2012

Summary

- Through the increased provision of service contracts, larger charities (particularly those associated with social care, housing and training) have become increasingly dependent on government funding in recent years.

- Despite the government's 'Big Society' vision, public spending cuts and pressures on households' disposable incomes are expected to weigh on sector income.

UK Charities overview

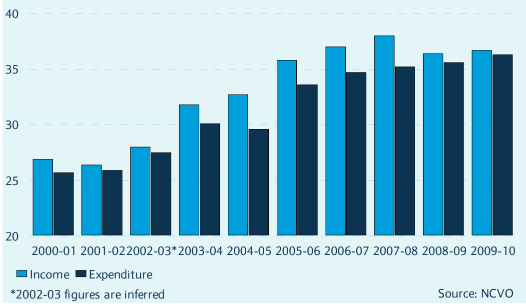
- There were 163,763 voluntary organisations in the UK in 2010, according to the National Council for Voluntary Organisations (NCVO), although most of these were very small, with over half having a turnover of under £10,000 a year and 159,205 having a turnover of under £1 million a year. A total of 4,084 had a turnover of £1 million to £10 million and 474 had a turnover of over £10 million.

- Charities are currently operating in a difficult environment, amid rising demand for their services (partly due to public expenditure cuts) and a decline, in real terms, in a number of key income streams. According to the NCVO, voluntary organisations spent 99% of their income in 2010, in order to keep pace with rising costs, which increased by £2.3 billion between 2008 and 2010 (partly as a result of high inflation) and to expand their services to cope with demand. This was the smallest gap between income and spending in 10 years, with many organisations having to dip into their reserves to stay afloat, which is clearly unsustainable in the longer term. At £42.2 billion in 2009-10, reserves were £4.1 billion lower in real terms than at the beginning of the decade.

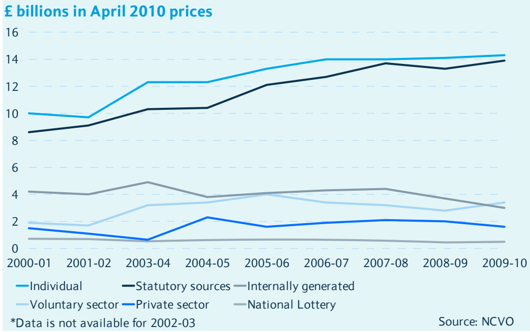
- The sector receives 38% of its £36.7 billion income from government, 79% of which is generated through contracts for the provision of services. Charities' income from statutory grants has declined from a peak of £5.3 billion in real terms in 2003-04 to £3 billion in 2009-10. Charities' income has, however, seen a significant increase from contract income over the past decade as revenue from public service delivery rose from £4.3 billion in 2000-01 to £10.9 billion in 2009-10. Overall, statutory income increased by 4.5% in the year to 2009-10.

- However, since then, austerity measures have impacted on the sector, and will continue to do so in the medium term, via cuts in funding and increases in demand for services no longer being supplied by the state. NCVO forecasts that the voluntary sector will lose £1.2 billion in government income each year until the end of the spending review period in 2015-16, a cumulative total of £3.3 billion. This is likely to affect sub-sectors that are more dependent on statutory funding more than other charities. The employment and training sub-sector receives 75% of its income from statutory sources, law and advocacy (58%), social services (56%) and community development (48%).

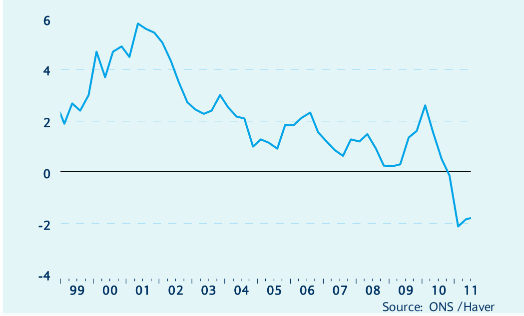
Voluntary sector income and expenditure in real terms
£ billions



Sources of voluntary sector income
£ billions in April 2010 prices



Real personal disposable income
Four quarter moving average % change

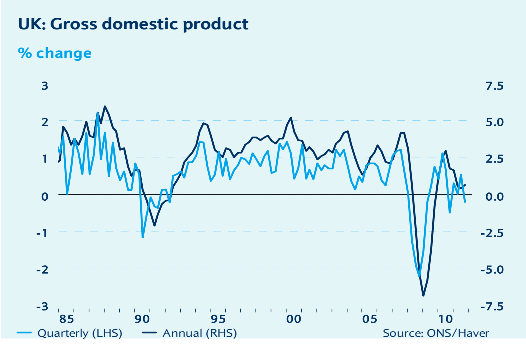


- Charities have also suffered from the decline in investment returns and low interest rates on deposits, with investment income declining from £3.1 billion in 2008-09 to £2.4 billion in 2009-10. While pressures on household budgets continue to depress donations, the charity retail sector appears to have benefited. NCVO estimates that charitable giving fell by £383 million during the recession (although it has recently stabilised in cash terms), but sales to the public from charity shops, raffle tickets, membership fees and other sources increased by £905 million.

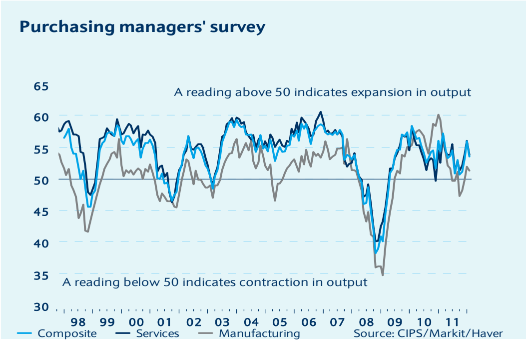
- Looking ahead, charities will continue to face a challenging environment, with strong demand for services, but persistent pressure on income from government funding cuts, low interest rates and low investment returns. Pressure on real disposable income will also dampen donations. Nevertheless, the largest charities remain relatively low risk, with the largest 474 charities controlling average net assets of £80 million each, providing a significant financial cushion.

Appendix 1 – Summary of macroeconomic overview

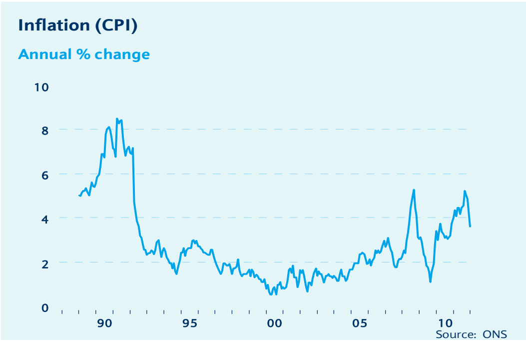
- Official data suggest that the UK economy contracted by 0.2% q/q in Q4 2011, following growth of 0.5% in Q3. The distortionary impact of events, such as the Japanese earthquake, the Royal Wedding and the associated extra bank holiday, resulted in an uneven pattern of quarterly GDP growth during 2011 (events, such as the Olympics and Diamond Jubilee holiday, will result in similar distortions in 2012). However, over the year as a whole, growth slowed to just 0.8%, compared to 2.1% in 2010, with concerns about the pace of the global economic recovery and the escalating eurozone sovereign debt crisis weighing heavily on activity and confidence in the UK (and across the advanced economies), particularly in the second half of the year.



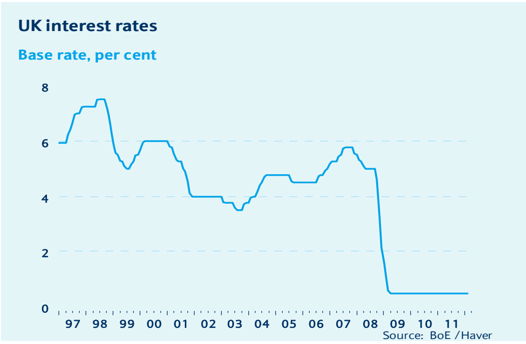
- Large-scale, long-term ECB liquidity provision and progress on a new support package for Greece appear to have eased eurozone tensions, for now, with the more positive tone of recent data from the US further bolstering confidence. Business surveys also suggest that UK economic activity has picked up once more (albeit modestly). However, whilst improving, confidence remains fragile and events in Europe continue to cast a shadow over both the UK and wider global economic outlook.



- The unemployment rate rose to 8.4%, with some 2.67 million people unemployed in the UK, in the three months to December 2011. Weak growth in private sector employment has failed to offset public sector job cuts over the past year and a continued rise in 'involuntary' part-time and temporary employment (by those seeking full-time, permanent posts) suggests that the degree of slack in the labour market is greater than the headline unemployment figures indicate.



- At 3.6%, inflation remains well above the 2% target rate, but has slowed markedly from its recent peak of 5.2%. With domestic inflationary pressures relatively subdued, and the temporary factors that contributed to high inflation last year (such as the increase in VAT and earlier rise in fuel and energy costs) set to fall out of the annual comparison, it is expected to continue to decline, although the recent rise in oil prices highlights the potential risks to this scenario.



- Allied to the weak prospects for the economy, the benign inflationary outlook has seen the MPC maintain interest rates at their historic low of 0.5%. In February, the MPC also sanctioned a further £50 billion of quantitative easing (QE), raising the limit on the Bank's asset purchase facility to £325 billion. Whilst financial markets now expect the MPC to pause QE, Bank Rate is expected to remain on hold during 2012-13.

- Despite a brief pick-up in the quarterly data in Q4, official figures show that consumers' expenditure declined by 0.8% during 2011. Falling inflation should gradually begin to ease some of the downward pressure on real disposable income (RDI). However, consumer spending is likely to remain weak over the next 12 months, as households remain heavily indebted, confidence remains weak and, with wage growth likely to remain below the rate of inflation, RDI is likely to continue to decline (albeit more slowly) in the near term.

- Fiscal tightening will also continue to bear down on the economy. Although official data suggest that the 2011-12 fiscal deficit will be lower than originally forecast, the Chancellor's Autumn Statement revealed significant downward revisions to the Office for Budget Responsibility's (OBR) medium-term economic forecasts. As a result, the Chancellor has stated that there will be no loosening of fiscal policy in the forthcoming Budget, which will be fiscally neutral. Indeed, the OBR's revised forecasts suggest that the austerity programme will likely have to be extended to 2016-17 to meet the government's medium-term fiscal targets.

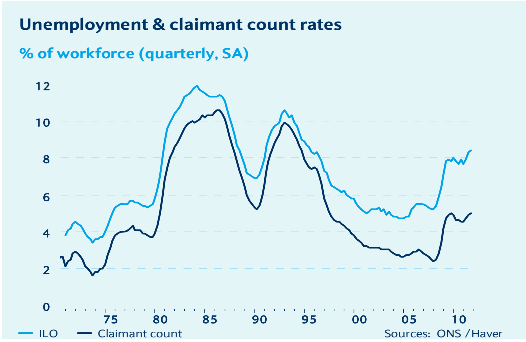
- Business investment was volatile last year, but declined once more in Q4 (by 5.6% q/q and by 2% y/y), resulting in growth of just 0.2% over the year as a whole. The corporate sector has been running a sizeable aggregate financial surplus, raising hopes that investment would provide a catalyst for both the recovery and the rebalancing of the UK economy. However, firms have adopted a more cautious approach as a result of spare capacity and/or the increasingly uncertain outlook.

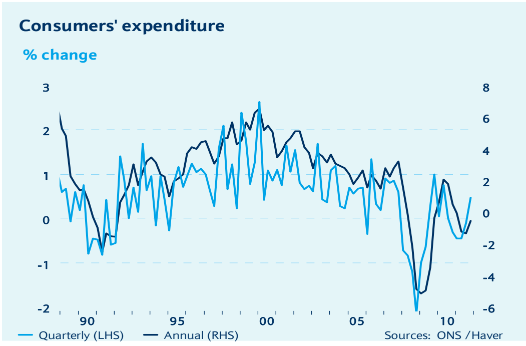
- Bolstered by the earlier sharp depreciation of sterling, the weak domestic UK performance was offset by a relatively strong contribution (1.2% points) to GDP growth from net trade last year. However, growth prospects for the UK's key European export partners have deteriorated markedly as a result of the eurozone sovereign debt crisis.

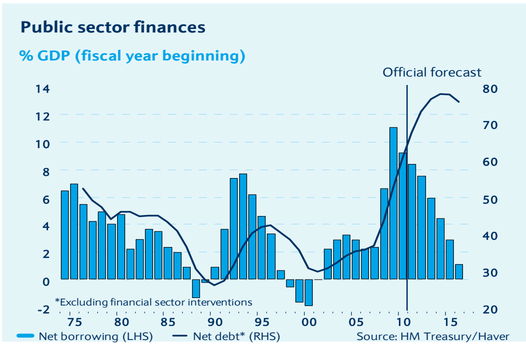
- Industrial production declined once more in 2011, with the pace of decline deepening as the year progressed. Following a period of robust annual growth at the beginning of the year, manufacturing activity stalled in Q4. Mining and oil extraction output also fell sharply (by 15.5%) in 2011, partly due to extra maintenance work in the North Sea, where production is now in long-term decline. Utilities output also declined last year, with relatively mild winter weather resulting in a particularly steep fall (10.9% y/y) in Q4. Annual growth in construction output also slowed markedly in the second half of 2011.

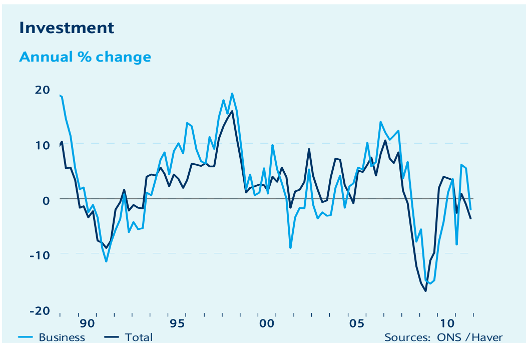
- Annual growth in services activity, which accounts for around 75% of UK GDP, proved more stable in 2011, although the quarterly pattern of growth was somewhat uneven. Growth in activity in this sector accelerated to 1.8% y/y in Q4, resulting in 1.6% growth during the year as a whole. However, performance was highly variable across the service industry's various sub-sectors, with business-oriented sub-sectors generally out-performing consumer-facing sub-sectors.

- UK economic forecasts have been revised downwards, with growth of just 0.5% expected this year and 1.8% next. As a result, recovery is likely to be protracted and weak, with risks weighted on the







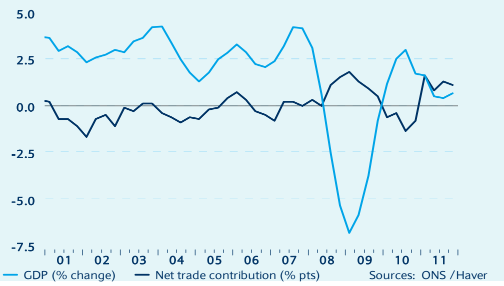


downside, given continued concerns over events in the eurozone, tensions in the Middle East(and the actual and potential impact of these tensions on oil prices) and signs of slowing growth in key Asian economies.

- Although expected to gradually pick up, as pressures on RDI gradually ease, consumer spending is forecast to remain subdued, from a longer-term perspective, during 2012-13, while fiscal tightening will see public sector activity and demand fall. Net trade is expected to continue to make a positive contribution to growth, but weak prospects for the eurozone are likely to see this diminish. However, investment should gradually pick up as economic growth accelerates.

- Unemployment is likely to continue to rise, as a result of further public sector job losses and cautious private sector job creation, but slowing inflation should, in the absence of unforeseen price shocks, enable the Bank of England to keep interest rates low.

Annual GDP growth and net trade contribution



UK consensus economic forecasts: February 2012

Annual % change (unless otherwise stated)	2009	2010	2011	2012f	2013f
Real GDP	-4.4	2.1	0.8	0.5	1.8
Consumer spending	-3.5	1.2	-0.8	0.2	1.6
Government consumption	-0.1	1.5	0.3	-0.4	-1.0
Investment (total GFCF)	-13.4	3.1	-1.7	0.9	4.0
Stockbuilding (contribution to GDP growth)	-1.0	1.3	-0.1	0.0	0.1
Net trade (contribution to GDP growth)	1.1	-0.8	1.2	0.3	0.3
Unemployment rate %	7.6	7.9	8.1	8.8	9.2
Consumer prices (CPI)	2.2	3.3	4.5	2.0	2.1
Base rate (end period)	0.50	0.50	0.50	0.50	0.50

Sources: HM Treasury; Bank of England; ONS; Barclays Corporate Economics

Prepared by Economics Team, Client Capital Management, Corporate Banking, Barclays Bank PLC.

All data and factual information referred to in this report were correct as of March 2012.