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Financial Services

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A brief overview

The financial services sector in the United Kingdom is, very rightly, seen to be one of the most important and most advanced financial markets anywhere in the world. Not only is it one of the world's oldest financial services markets but it also has a worldwide reputation for impartiality and integrity. Given its size and global importance it is not surprising that it is also of great significance to the UK economy as a whole. Indeed, the financial services sector in the City of London contributes around £17 billion to the United Kingdom's balance of payments, which is a respectable part of the total GDP each year.

Not only does the United Kingdom as a whole have an enviable reputation for the size and quality of the financial services companies that operate here, but the very words 'City' or 'City of London' are synonymous with the world's leading location for the financial services sector.

The statistics are impressive and the reach and depth of the markets can start to be understood when it is appreciated that there are more US banks in the City than there are in New York, or that each of the world's top 20 insurance companies operate in London or, indeed, that 375 of the top 500 global companies have offices in London. All these firms understand the importance of the UK market as a whole and the pre-eminence of the financial markets in the City of London.

In this age of sophisticated communication it is often argued that a local presence is not required, but the banks, traders, investment funds, insurers, shipping brokers, accountants, lawyers and all the other parts of the financial services sector that congregate in the United Kingdom and primarily in the City of London, create a critical mass that is not seen anywhere else in the world.

It is a dynamic place, ever-changing and evolving in order to ensure its place at the forefront of new developments, but at the same time its

solidity and permanence is one of the many attractions for companies establishing a presence or investing in the United Kingdom.

The United Kingdom in general, but London more specifically, also has extremely good international flight connections. With over 170 flights each day going to countries that generate more than 80 per cent of the world's GDP and over 230 international destinations in total, more than 90 million people use London's airports each year. Yet another reason for investing in the United Kingdom.

Banks

The exact number of banks in the City varies, declining as banks merge and rationalize operations and increasing as other banks grow and expand their international presence, but at the last count there were some 450 banks operating in London, of which more than 300 were foreign owned. Indeed, almost 100 of the banks with offices in London are from other EU countries.

Foreign banks in the City manage more than US\$3,000 billion on behalf of foreign clients and the volume of international lending is more than twice as high as in the United States or Germany. Consequently, more syndicated loans are completed in London than anywhere else in the world. As such, companies from around the world looking to raise large debt facilities approach the markets in London rather than the less developed markets in their home country.

The fact that the United Kingdom is not part of the Eurozone has had no impact on the markets despite predictions from some that the United Kingdom needed to convert to the euro in order to ensure the continued success of the City. Indeed, statistics show that if anything the City has prospered even more since the Eurozone was established. Eurobonds now account for the majority of bond issues, about 60 per cent of them originate in London and about 70 per cent of the secondary market in bonds is in London. Despite the euro's rise, most foreign exchange deals worldwide are still in US dollars but London still dominates the foreign exchange markets. Daily transactions total some US\$637 billion and represent about one in three of all foreign exchange transactions worldwide, making the London market nearly twice the size of the nearest rival, the United States.

Mergers and acquisitions and other investment bank activities are centred on London, with many European and US banks having large operations reflecting the level of business. Often, regional head offices are based in London and cover areas as wide as Europe (Western, Central and Eastern), Africa and the Middle East. Investment bankers providing advice on matters such as privatization in the emerging markets of Central Europe, and other countries worldwide are often

based in London even if they are working for large US investment banks.

It is a similar story with trade and project finance, with many foreign banks centring their trade and project finance departments in London rather than in their home countries. Not only is there more expertise and activity in London than any other centre but also the high level of deal origination leads to more opportunities for all. The secondary markets (where banks buy and sell existing debt and trade finance paper among themselves) are also centred on London. The ever-growing presence around the world of public private partnership structures to utilize private sector capital to finance public sector services is another area that is driven by the concentration of experience in the United Kingdom and the financial services expertise in the City of London.

Capital markets

The London Stock Exchange is also pre-eminent among the world's stock exchanges, with more foreign equities listed in London than on any other of the world's exchanges, with turnover in these companies accounting for 58 per cent of the world's trading in foreign companies, which is almost twice as much as the nearest rival.

London is the leading fund management centre in the world with more than £2,550 billion of assets under management. Not only is London way ahead of New York in this respect but also more funds are invested in the City than in the next 10 European centres combined. Another leading centre of fund management expertise (and life insurance companies) in the United Kingdom is Edinburgh.

There are private equity investors and venture capital funds based around the United Kingdom. Many of these are specialist funds catering for specific sectors and are based near the centres of expertise in the respective sectors, for example, a number of locations such as Oxford and Cambridge boast a cluster of funds and these tend to specialize in sectors such as high technology, biotechnology and the like, but the majority of investment funds are based in London. Tax breaks exist in the United Kingdom to encourage private investors to put money into equity funds and other capital market instruments but even more generous tax breaks exist to encourage private investors to invest in Venture Capital Trusts, which are funds that specialize in investing private equity into start-up and early stage opportunities (see Chapter 2.7).

Insurance

The world's first insurance market was Lloyd's of London and it is still the best-known name in the industry, especially for any unusual or bespoke insurance requirements. For example, space rockets and satellites are often insured here and many famous musicians and film stars use Lloyd's to insure their fingers, face, legs and many other parts of the body. Lloyd's specializes in aviation and marine insurance and it is the global market leader in these sectors. Again, the sheer number and diversity of insurance companies and brokers, both UK and foreign, clustered together in the area adjacent to Lloyd's makes the insurance market in the United Kingdom unique.

The United Kingdom insurance industry is not only the largest in Europe but it is the third largest in the world. In 1998 the value of insurance sold in London was £123 billion and this generated gross premiums of £14 billion and by 2003 Lloyd's of London alone accepted insurance premiums of £14.4 billion, demonstrating the continued rise of these markets.

The UK life and pensions market is twice the size of that of the nearest European rivals and each day pays out over £140 million of benefits, which is more than the UK government.

Other markets

The United Kingdom is also home to a range of other leading financial service markets such as metal trading, derivatives, ship chartering and the professional services such as accountants, consultants and lawyers that are an integral part of a fully functioning market.

The London Metal Exchange transacts over 90 per cent of the world's traditional metal trading and, separately, some 36 per cent of the world turnover of derivative products is handled in London. The 2,000 members of the Baltic Exchange in London transact about 50 per cent of the worldwide tanker chartering business, about 40 per cent of worldwide dry-bulk business and more than 50 per cent of new and second-hand tonnage is sold through brokers in London.

All the large accountancy firms have offices in London, employing thousands of people and, as with the banking sector, many regional head offices or sector specialist teams are based in the United Kingdom, drawing on the high degree of local expertise and attracting other experts from markets worldwide. The accountancy firms based in the United Kingdom are leaders in providing not just accounting and auditing services but also consultancy and advisory services around the world.

Five of the 15 largest law firms worldwide are City firms and more

than 60 US law firms have London offices. Given the importance of the UK market and the international expertise in London, law firms from around the world have offices here. In more recent years London has become a centre for arbitration (reducing the time and costs involved in settling international contractual disputes), drawing on the expertise of the large number of law firms with operations in the United Kingdom and the worldwide reputation of English law and the impartiality of the whole of the judicial system. Indeed English law is normally the law of choice in transactions between international parties operating under different jurisdictions.

The Financial Services Authority (FSA) is the regulator of all the financial services in the United Kingdom (see Chapter 5.5) and has a worldwide reputation for striking a good balance between being sufficiently strong to ensure the integrity of the markets while being sufficiently flexible so as to ensure that competition and growth in the markets is not hindered. There is a constant demand from other regulators around the world to visit the FSA in order to learn from their expertise.

Summary

One of the strengths of the financial services sector in the United Kingdom is that it draws on expertise from around the world and its size and reputation acts as a magnet for individuals and companies wanting to take part in and benefit from its dynamism. In London alone there are resident communities (of more than 10,000 people) from 33 different countries and over 300 different languages are spoken.

The level of expertise, together with the strength and depth of the market, are a compelling reason for many companies to invest in the United Kingdom but even if this is not the primary reason for the investment decision, the quality of the financial services sector can only increase opportunities for inward investors and enhance a decision to invest based on other reasons.