

Future Economy Scenarios

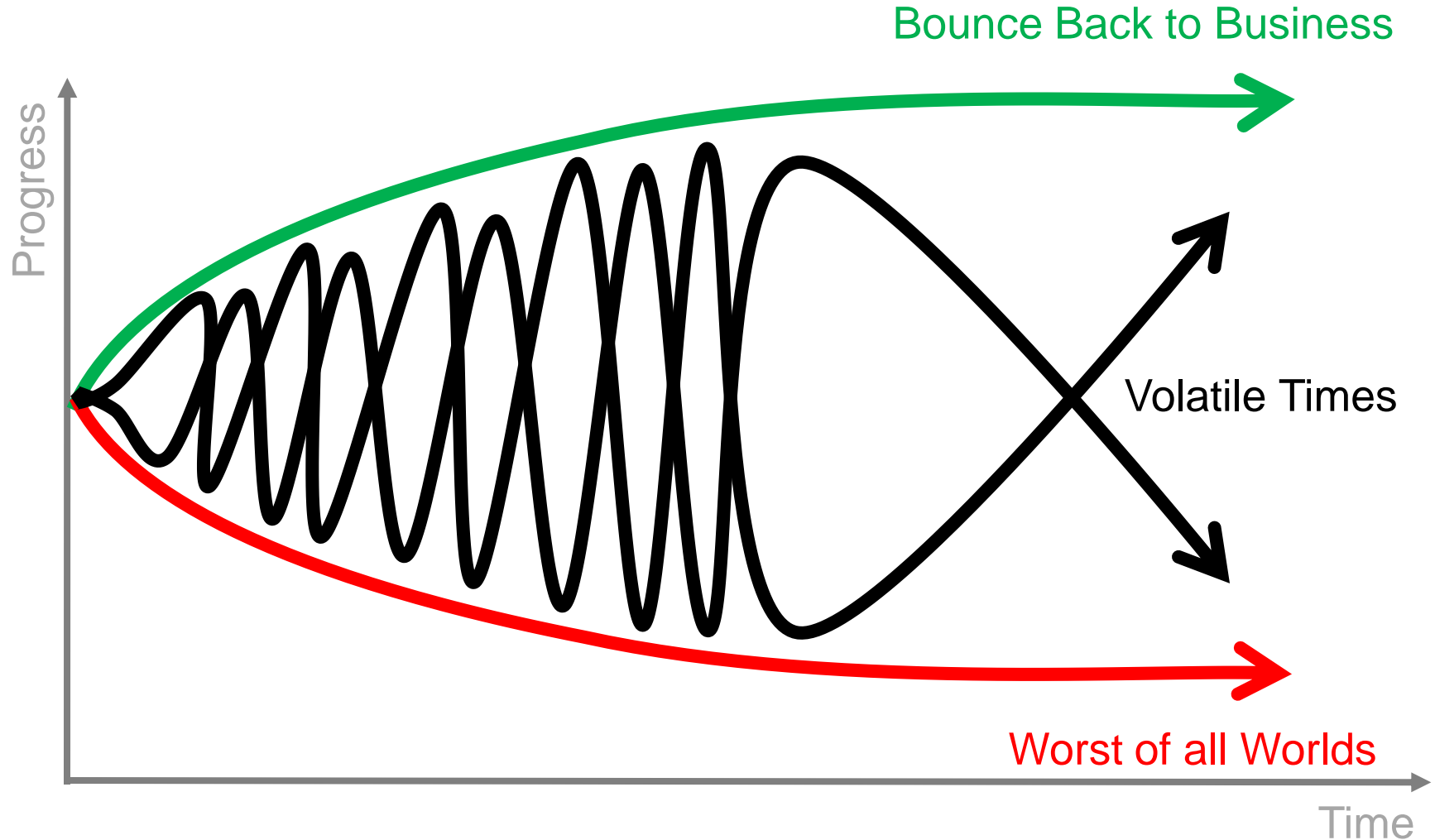
Richard O'Brien
Outsights
March 2010



outsights
insights from the outside

Framework for the Future

The Scenario framework is designed to help navigate the current uncertainty and stress test strategy.



Critical Uncertainties on Future Directions of the Global Economy

Economic Growth

After the long boom, how deep the recession, how long to recovery?

Financial Stability

How long for the financial system to right itself?

The Model

Will the free market survive the collapse of confidence?

The flows of globalisation (money, goods, services, information & people)

Bounce Back to Business

Scenario Features

Economic Growth

Fast recovery

- Fiscal and monetary stimuli work and the recession bottoms out in 2009/2010.
- Investment plans are restarted and there is a search for profit in equities.

Financial Stability

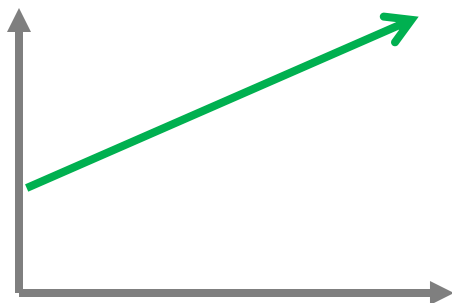
Regained

- Timely government intervention with “toxic” assets removed, improved financial regulation and a clear programme to return the banking system to the market.

The Model

Open, lightly regulated capitalism and globalisation

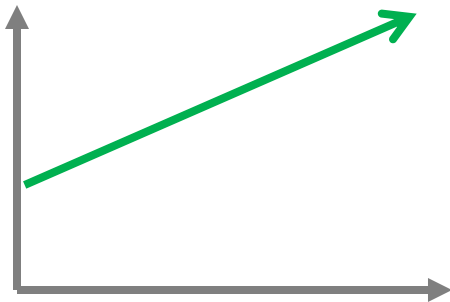
- No policy mistakes and no retreat into protectionism.
- The US leads a coordinated response with China and the EU.



Bounce Back to Business

Ingredients for Business Success

- ✓ Growth ability to keep up with **demanding consumers**
- ✓ **Access to credit**, capital, reserves
- ✓ Strong and flexible **brand**
- ✓ Strong efficient **supply chain**
- ✓ Power of **innovation** to extend boundaries of the sector

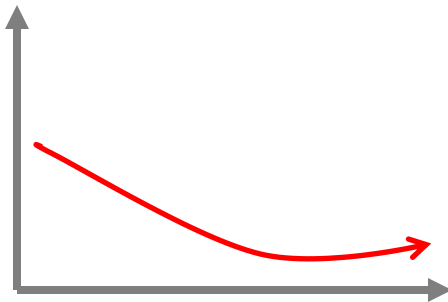


Worst of all Worlds

Scenario Features

Economic Growth Depression

- The damage spreads e.g. to Eastern Europe; there is global negative growth for up to 2 years.
- The global consumption/savings imbalance raises real tensions between deficit and surplus economies to no-one's advantage.



Financial Stability Disruption

- Policy mistakes and a lack of reform means the financial crisis worsens and toxicity remains.

The Model Closing markets, high regulation and globalisation interrupted

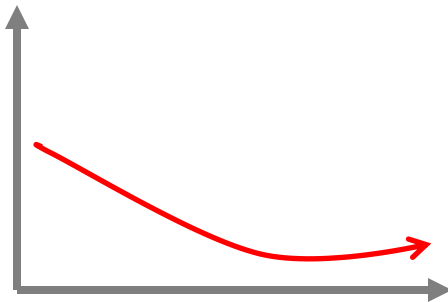
- The case for openness gets harder to sustain given so many losers. Heavy regulation and intervention intensify.



Worst of all Worlds

Ingredients for Business Success

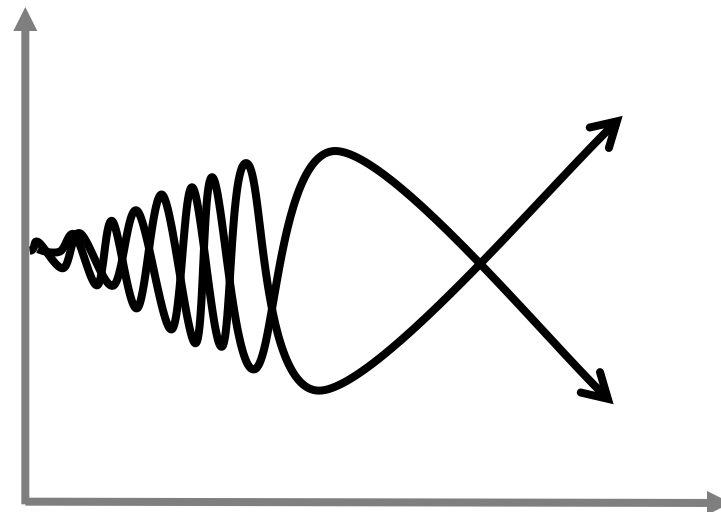
- ✓ Staying powerful: **survival of the strongest, fittest and agile**
- ✓ An underlying **long run source of consumer demand**
- ✓ Access to credit, capital, reserves and a **strong brand**
- ✓ **Flexibility** where real demand has fallen
- ✓ Ability to invest where **new demand** is emerging
- ✓ Ability to **keep supply chains open** despite disruptions
- ✓ Smart investments and **innovation**



Volatile Times

Scenario Features

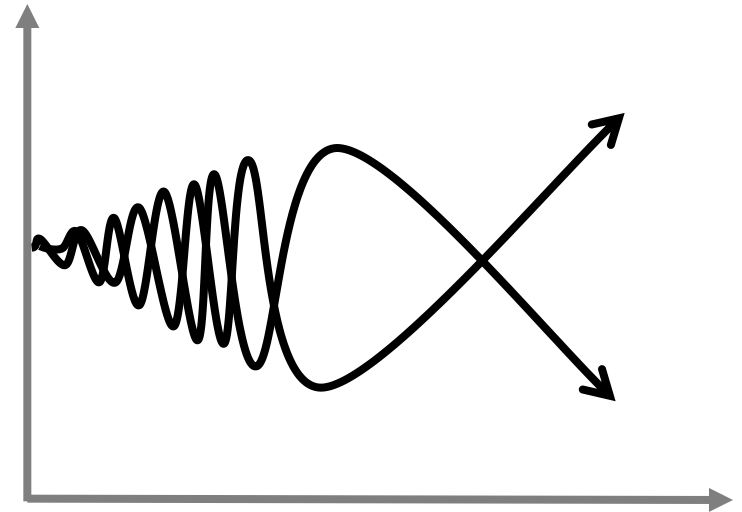
- ✓ We live in **Volatile Times**.
- ✓ There is uncertainty over:
 - Future growth rates
 - Exchange rates
 - Interest rates
 - Government intervention and regulation
 - In the short term: deflation
 - In the longer-term: whether there will be high levels of inflation
- ✓ This uncertainty contrasts with the Long Boom which occurred during relative stability.
 - When making strategic decisions people developed consistent expectations – an anticipated future of steady growth and low inflation.
 - As uncertainty has increased the confidence to make decisions has evaporated.
- ✓ Volatile Times is *either* a period of reform that allows recovery and eventually for people to emerge with confidence (*Bounce Back to Business*) *or* a period of wasted opportunity followed by further decline (the *Worst of all Worlds*).



Volatile Times

The Management Challenge

- **No clarity** on offer
- Expect **continued uncertainty** and confusion
- Market **volatility may persist**
- **Mixed signals** by sector and country
- The longer it goes on, the harder (yet more important) it is for **policy makers to hold their nerve**
- Solutions will have **unexpected consequences**



The Big Questions Right Now

Four Pressure Points

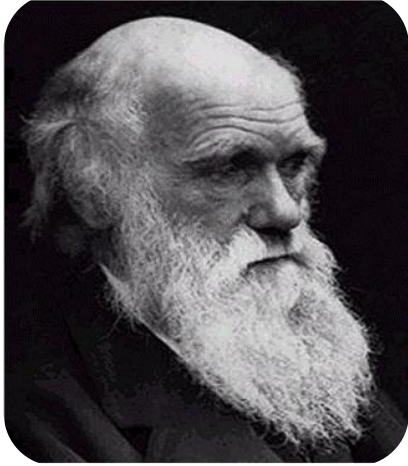
1. Imbalances remain a problem
2. Some highly indebted Governments will have to start cutting spending or raising taxes or both
3. The fear of higher interest rates and of inflation
4. The risk/reward deal in finance is still imbalanced

Five Critical Challenges

1. Resources
2. Security
3. Health
4. Climate
5. Migration

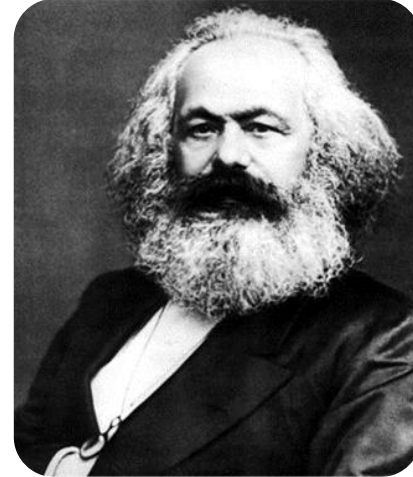
There will be winners and losers: who will they be?

The Bottom Line



Darwin: adapt to prosper

- **Be ready for two extremes** – the uncertainty is for real
- **Be prepared to manage volatility**, complexity and uncertainty
- **Look long-term as well as short-term**: decisions now have a long-term impact



The alternative...

Marx's forecast that **capitalism will self-destruct** remains uppermost in people's minds, restraining a return of confidence

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