LONDON CHAMBER of COMMERCE AND INDUSTRY

CONNECT. CHAMPION. SUPPORT.

Q3

CAPITAL 500

London Quarterly Economic Survey

July – September **2023**

In partnership with

Savanta:

Sponsored by

haysmacintyre

JAMES WATKINS

Head of Policy and Public Impact, London Chamber of Commerce and Industry

LCCI COMMENTARY – THE BUSINESS VIEW

London businesses will be relieved to see headline inflation figures in the UK beginning to fall, particularly as it remains the number one concern for the capital's firms. Our latest Capital 500 survey showed that, whilst there has been a slight easing, cost pressures remain high for businesses.

The Bank of England's decision to maintain rates at current levels following their September meeting will also be somewhat reassuring to companies. Encouragingly, London businesses saw a slight improvement in cashflow over Q3, while demand for export orders jumped. Domestic orders and sales were largely unchanged compared to the previous quarter. Recruitment activity increased in Q3 and more businesses than not still expect their workforce to grow in the coming three months.

Businesses were more optimistic about their own firm's outlook in the next 12 months, with both turnover and profitability expectations climbing again in Q3. In light of the continued cost pressures facing London businesses, this is indeed a reassuring sight.

Nevertheless, as the latest PMI and GDP data show, the UK economy appears to be slowing again. Whilst confidence in their own company continues to recover, London businesses are not as optimistic for the wider London and UK economies.

It is for this reason that London Chamber of Commerce and Industry is not letting up in its campaign for Government to do more to boost the economy in partnership with business. This includes calling for surety over investment decisions when it comes to infrastructure, tackling high energy bills for all businesses and sustained action to deal once and for all with the capital's skills crisis.

In the meantime, the London Chamber has established a Procurement Hub, an Access to Finance hub and a Skills hub to give London firms the help they need during this cost of living crisis.

Only by genuine partnership working between Ministers, the Mayor of London, local authorities and business, can we ensure that the capital's economy remains resilient and strong.

James Watkins, Head of Policy and Public Impact, London Chamber of Commerce and Industry

ABOUT THE 'CAPITAL 500'

For over a decade London Chamber of Commerce and Industry (LCCI) has conducted a Quarterly Economic Survey (QES) of members to gauge business performance and general confidence levels across the capital. This is part of the biggest and longest running national private business survey, conducted by regional chambers of commerce across the UK every quarter.

Savanta surveyed a total of 519 London business leaders between 1 August to 1 September 2023. All data were weighted to be representative of all London businesses by company size and broad industry sector. Savanta is a member of the British Polling Council and abides by its rules. Full data tables are available at www.savanta.com.

The net balance figures represent the percentage of firms that reported an increase minus the percentage that reported a decrease. Two categories are used for business size segmentation: micro businesses with fewer than 10 employees (including sole traders), and larger (small, medium and large) businesses with 10 or more employees. Any data reproduced from the report should be fully referenced.

ABOUT HAYSMACINTYRE

haysmacintyre is an award-winning firm of chartered accountants and tax advisors, providing specialist advice to entrepreneurs, fast-growing and owner-managed businesses, and not for profit organisations across the UK and internationally.

VICKY PRYCE

Chief Economic Advisor and Board Member, Centre for Economics and Business Research (Cebr)

GUEST COMMENTARY – THE ECONOMIST'S VIEW

The latest QES survey results continue to point to a welcome improvement in activity and the general mood of London businesses, further backed by improved consumer confidence indicators in the UK and also better industrial trends surveys. Some cheer then. Additionally, if the statistics are to be believed, we did not do as badly as we thought during the pandemic. According to revisions by the Office for National Statistics (ONS), UK GDP was some 1.8% higher by the end of 2021 than previously thought. That of course simply reversed the 1.7% downgrade by the ONS in 2020, so we are none the wiser. It seems that the health sector – given the NHS and other activities, and wholesale, which we can assume refers to the logistics sector – were part of the explanation. The result is that we are now at par with other G7 countries, if not better, with GDP now above pre-pandemic levels rather than below.

Statistics are an interesting thing. They do affect the psyche and therefore possibly overall confidence and we may be seeing some of that now. However, it must be pointed out that the Head of Economic statistics at the ONS has called for help from the Statistics Regulator to check their workings. In any case, the evidence suggests that much of the improvement in confidence has come from the slowdown in inflation and a brighter outlook for prices ahead rather than the GDP revision. What's more, interest rates appear to have peaked, and pay is now rising more or less in line with inflation so real wages are being restored.

Nevertheless, the underlying economy continues to be a worry. UK GDP fell by 0.5% in July, and although retail sales picked up by 0.6% in August as the weather improved, this did not fully offset the 1.1% drop in July. Strikes are still with us disrupting movement and output. Workplace absences seem to be at their highest for a decade and staff shortages, though easing, remain in many sectors. The latest PMIs for the UK suggest a continued contraction in manufacturing and services in September.

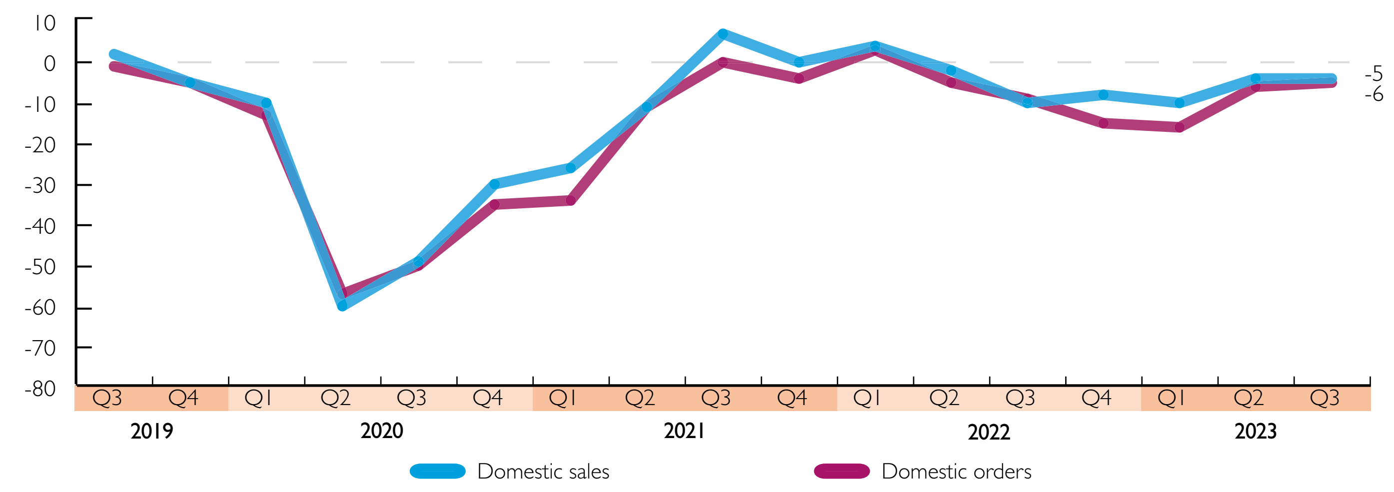
Yes, interest rates are likely to be lower ahead and the economy mortgage markets have been repricing their rates down. However, they are still at over 6%, some four to five times what they were a year and a half ago. That is already affecting the housing market and many firms, particularly SMEs, are struggling from the burden of high borrowing costs. While electricity and food price inflation are slowing down, the OPEC production cuts and the just-announced Russian ban on diesel and gasoline exports are already having an impact on prices at the pump. For businesses, the super deduction tax incentive has now come to an end and the uncertainty on net-zero policies and HS2 could act as a dampener to investment ahead. With Europe also slowing down, there is no guarantee that the UK will escape a technical recession sometime over the next 12 months.

Vicky Pryce, Chief Economic Advisor and Board Member, Centre for Economics and Business Research (Cebr)

DOMESTIC DEMAND

24% of London businesses reported an **increase** in domestic sales last quarter

19% of London businesses reported an **increase** in domestic orders last quarter



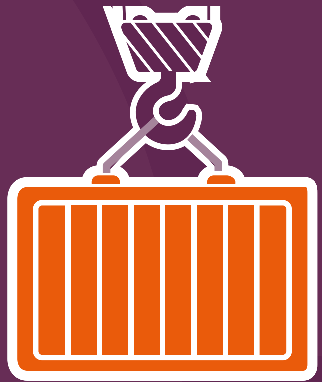
London businesses saw little change in domestic demand during the third quarter of 2023. A quarter (24%) of companies said their domestic sales had risen in Q3, unchanged from Q2. The proportion who said sales had fallen also remained stable last quarter (29%). As a result, the net balance (the percentage of firms noting an increase minus the percentage noting a decrease) was -5 in Q3, consistent with the previous quarter.

For micro companies (0-9 employees), the domestic sales balance remained at -8 in Q3, with no change in the proportions noting an increase (22%) or decrease (30%) in sales compared to the previous quarter. However, for larger firms (10 or more employees), domestic sales bounced in Q3: the net balance climbed 8 points to +34. Just under half (47%) of larger businesses said their sales had risen in Q3, up from 42% in Q2.

Turning to domestic orders, the net balance nudged up from -7 to -6 in Q3. The proportion of companies who saw an increase in orders shrunk slightly from 22% to 19%, although the share who noted a decrease in orders was also smaller in Q3 (25%) compared to Q2 (29%).

Larger companies saw a second consecutive improvement in domestic orders, with the net balance climbing 10 points to +30 in Q3. Only 7% of larger firms reported a fall in orders last quarter, while 37% saw a rise. For micro companies, the domestic orders balance was unchanged at -10 in Q3.

Manufacturers saw a marked improvement in the net balance for domestic orders, which jumped from -21 to +8 last quarter. This was due to a much smaller share of manufacturing firms who said that orders had fallen in Q3. For service sector businesses, the domestic orders net balance nudged down from -6 to -7.



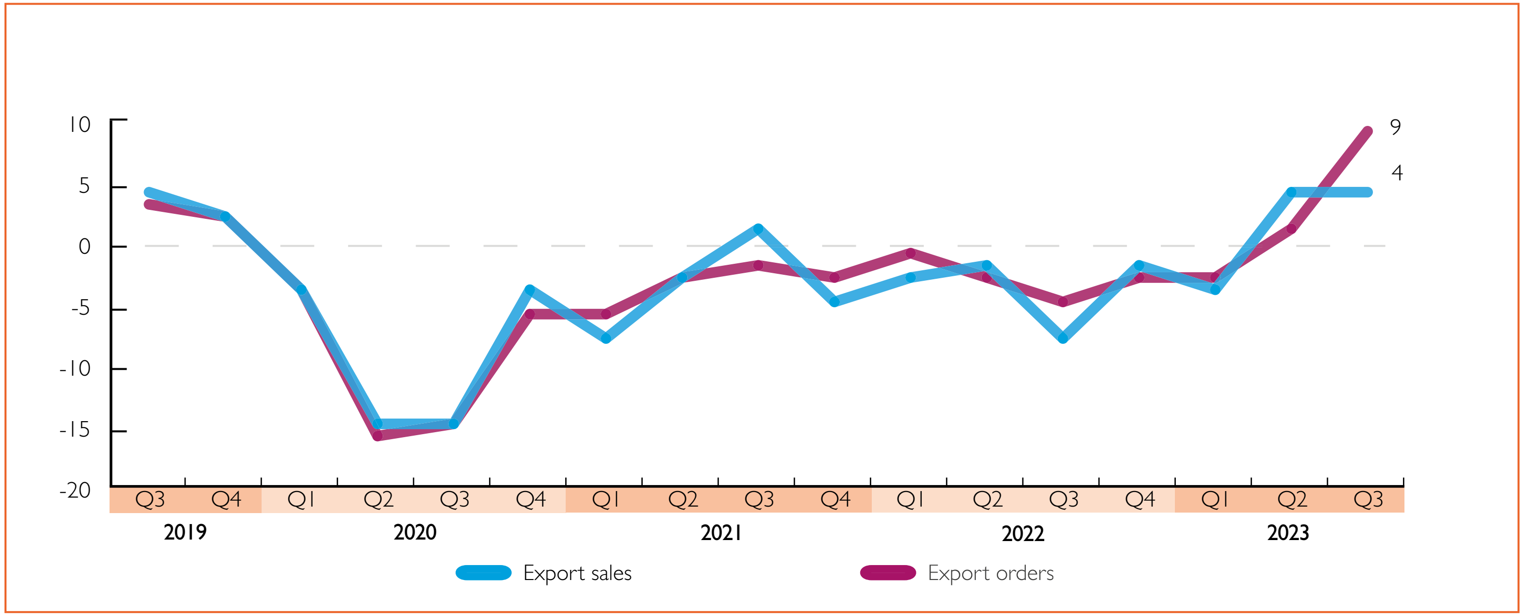
11%

of London businesses reported an **increase** in export sales last quarter

15%

of London of London businesses reported an **increase** in export orders last quarter

EXPORT DEMAND



There was a sharp increase in export orders reported by London's businesses last quarter, with the net balance jumping from +1 to +9: this is the joint-highest reading since the Capital 500 survey began. More than one in six (15%) London firms said their export orders grew in Q3, up from 11% in Q2. There was also a smaller proportion of companies who reported a fall in orders (6% in Q3, 10% in Q2).

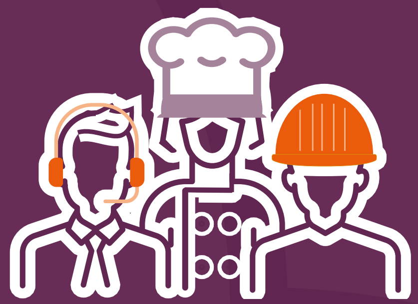
For micro firms, the net balance for export orders rose 6 points to +7, with 14% of micro companies reporting an increase in orders last quarter. Larger businesses also saw an improvement in orders, as the net balance jumped 17 points to +25.

Manufacturers saw a big rise in export orders (balance climbed 19 points to +19 in Q3). The export orders balance for service sector businesses increased from +1 to +7.

Turning to export sales, the net balance was unchanged at +4 in Q3. The proportion of companies who said export sales had risen shrank slightly from 13% in Q2 to 11% in Q3, but the share who saw a fall in sales also declined (from 9% to 7%).

Micro companies saw no change in their export sales last quarter, with the net balance remaining at +3. There was a small rise in the sales balance for larger businesses, from +14 to +18, on the back of a bigger proportion who reported an increase in sales.

LABOUR MARKET

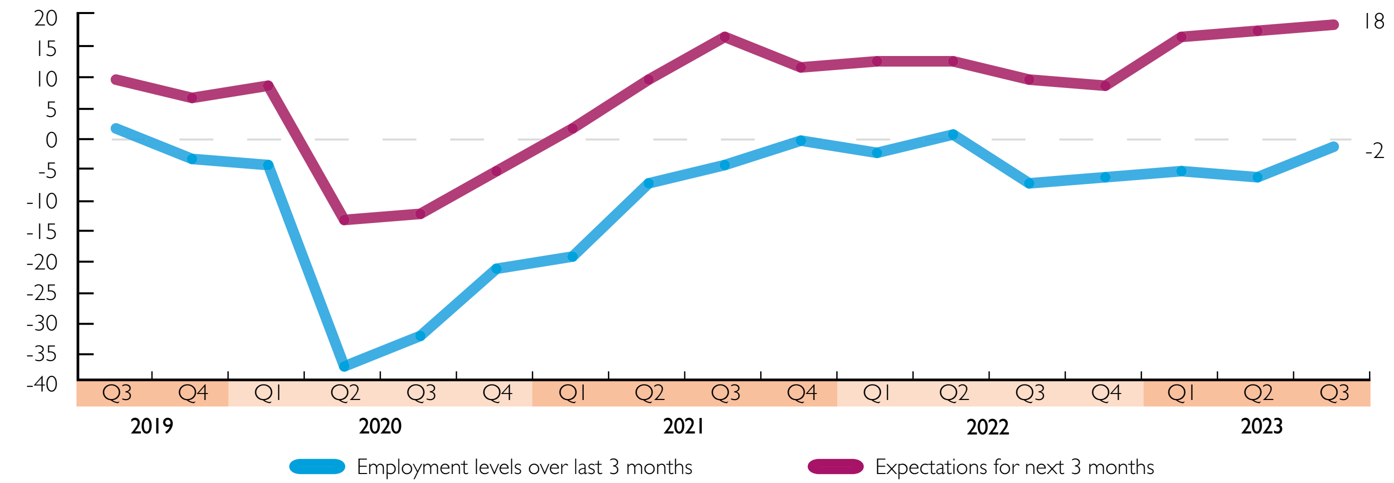


9%

London businesses reported an **increase** in their workforce size last quarter

22%

of London businesses expect their workforce size to **increase** over the coming three months



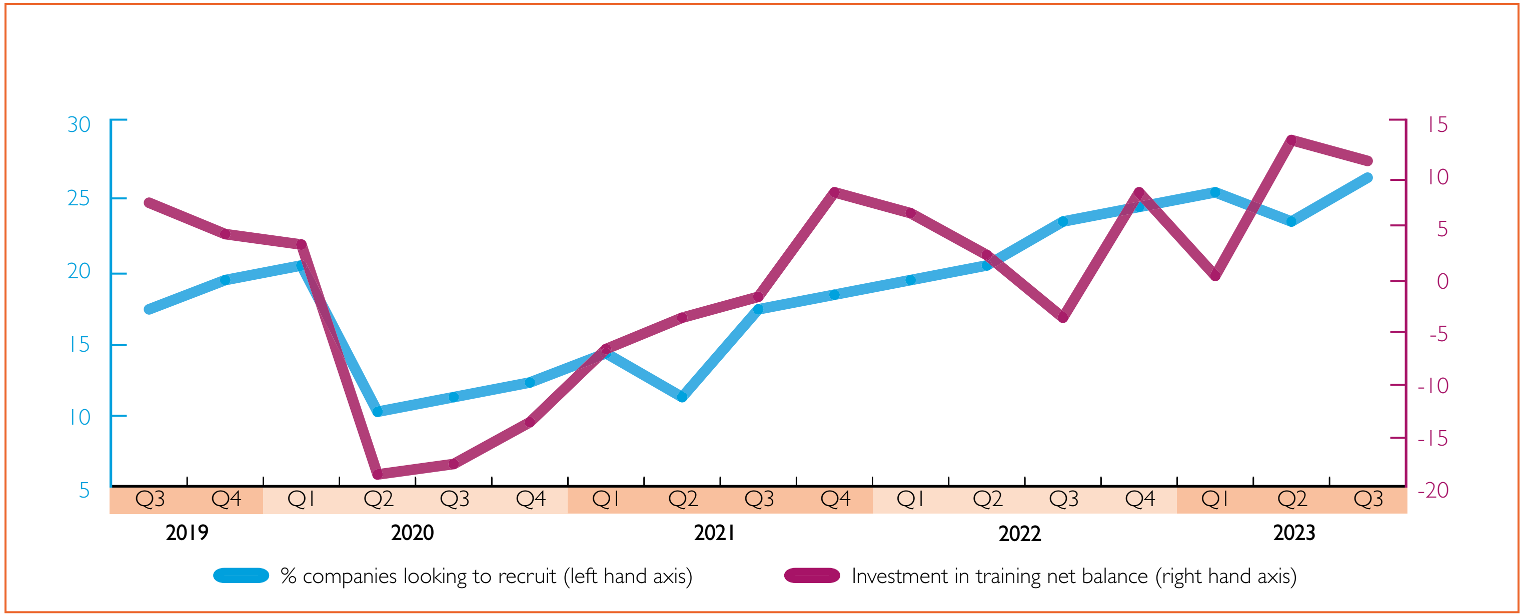
The latest Capital 500 suggested there were no significant changes in London's labour market over the summer. The employment balance rose from -7 to -2 in Q3, although the proportion of companies who said their workforce had increased shrunk slightly from 13% to 9%. The share of firms who said their workforce had declined in size also halved (from 20% in Q2 to 11% in Q3).

Micro companies saw an improvement in the employment balance in Q3, rising from -10 to -6. Whilst there was a smaller proportion of micro firms who reported an increase in their workforce levels (from 11% to 6% in Q3), fewer micro businesses also said their workforce had shrunk (21% in Q2, 12% in Q3). The picture was even more positive for larger companies (10 or more employees): 37% said their employment levels increased in Q3, up from 30% in Q2. Only 8% of larger firms said their workforce had decreased in size last quarter. The net balance climbed 11 points to +29.

Employment expectations for the coming three months were slightly stronger in Q3 as well. For all London firms, the net balance nudged up from +17 to +18, with 22% of companies expecting their workforce to grow over the coming three months. Just 4% of London businesses thought their workforce would decline in size in Q4.

Expectations were stable for micro firms, with the net balance up 1 point to +15 in Q3. However, for larger businesses the balance slipped from +46 to +40. The share of larger companies who thought their workforce would increase shrunk slightly, but remains high at 47%.

RECRUITMENT AND TRAINING



26% of London businesses reported that they had looked to recruit in the last quarter

21% of London businesses reported an **increase** in investment in training last quarter

Recruitment activity picked up last quarter after stalling in Q2. Just over a quarter (26%) of London companies tried to hire in Q3, a new high for the Capital 500. The proportion of companies who had difficulties whilst trying to recruit also eased from 67% to 58% in Q3.

This increase in hiring activity was driven by manufacturers, who saw a sharp increase in recruitment efforts, rising from 27% in Q2 to 47% in Q3. The share of service sector companies who tried to recruit also nudged up from 23% to 24%, with companies in professional and business services, information and communication, and finance all more active in hiring.

Just under a quarter (23%) of micro companies tried to recruit in Q3, up from 19% in Q2. By contrast, the share of larger firms who sought to hire last quarter fell from 66% to 59%.

Investment in training was relatively stable in Q3, with the net balance slipping 2 points to +11. A fifth (21%) of London businesses said they had raised spending on training in Q3, consistent with the previous quarter (22%). One in ten (10%) firms said they had reduced investment in training, up slightly from Q2 (9%).

For micro companies, the training investment balance edged down 1 point to +10 in Q3, while for larger companies the balance fell from +33 to +29.

53%

53% of London businesses reported an **increase** in their fuel costs last quarter

64%

64% of London businesses reported an **increase** in their energy costs last quarter

BUSINESS COSTS

Cost pressures continue to show tentative signs of stabilising in Q3 according to the latest Capital 500. Just under two-thirds (64%) of London businesses said their energy costs had increased last quarter, down from 69% in Q2. The proportion who said their fuel costs had risen shrunk from 59% in Q2 to 53% in Q3. However, for both fuel and energy only 5% of companies said they had seen a decrease in costs from Q2 to Q3.

Just under half (49%) of London businesses said their costs for domestic raw materials rose in Q3, compared to 2% who saw a decline: the net balance fell 5 points to +47. Considering raw materials sourced internationally, the net balance declined from +46 to +37 in Q3.

Pressure to increase wages slightly eased in Q3, with the net balance sliding 3 points to +40: this was the third consecutive decline in the balance, although it remains at an elevated level.

London firms reported lower borrowing costs in Q3 as well – the net balance fell from +43 to +37. Two in five (41%) businesses said borrowing costs had increased in Q3 compared to the three months prior.

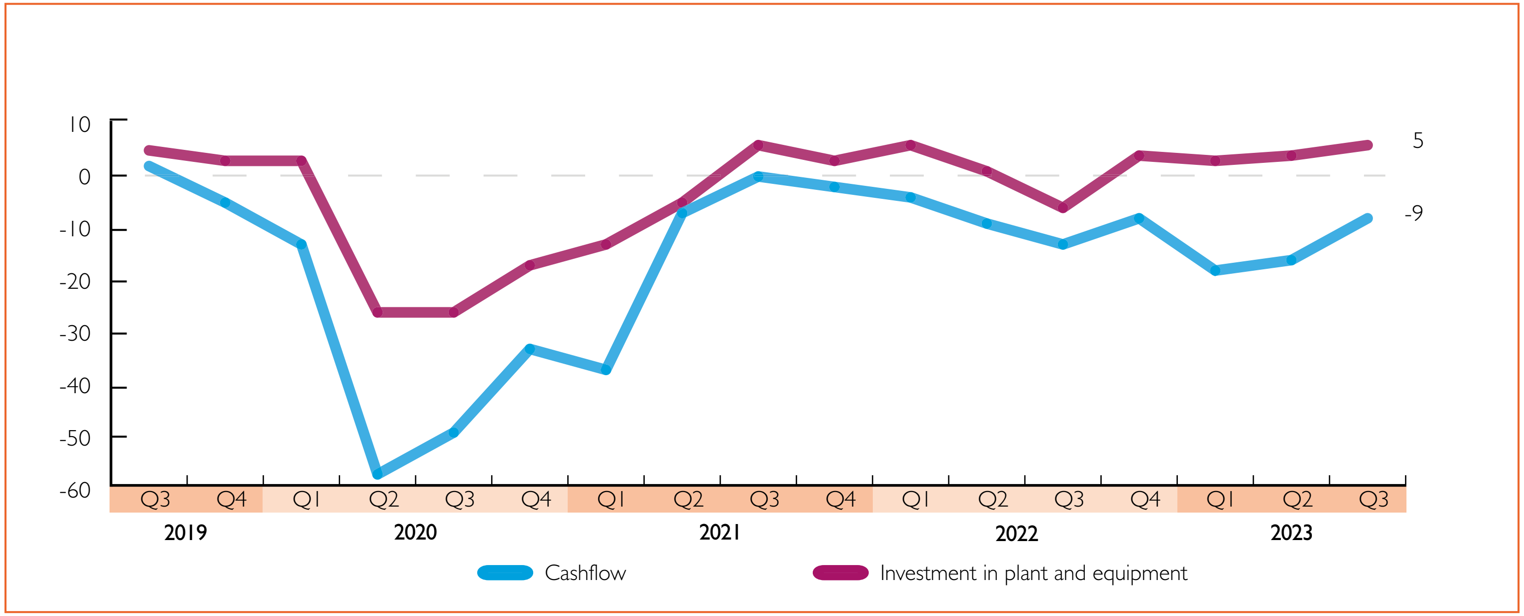
Firms were most likely to say that the cost of utilities were putting pressure on them to raise prices in Q3, followed by labour costs and finance costs. Just under half (45%) of companies expect the prices of their goods and / or services to increase in the next three months, compared to 2% who thought prices would decline.

Inflation remains the number one concern for businesses, with 66% saying they were more concerned about inflation in Q3 than they were in the previous three months. Despite the slight easing in the borrowing costs net balance, there was a greater share of companies who said that they were more concerned about interest rates in Q3 than in Q2 (41%, up from 36%).

CASHFLOW AND INVESTMENT

23% of firms reported an **increase** in cashflow last quarter

17% of firms reported an **increase** in investment in plant and equipment



Perhaps reflecting the improved domestic and export demand figures from recent quarters, companies reported another uptick in cashflow. The net balance for cashflow climbed 8 points to -9 in Q3, with 23% of firms saying cashflow had increased over the previous three months (up slightly from 22% in Q2). The share of firms who said cashflow had worsened shrunk to 32% in Q3 too.

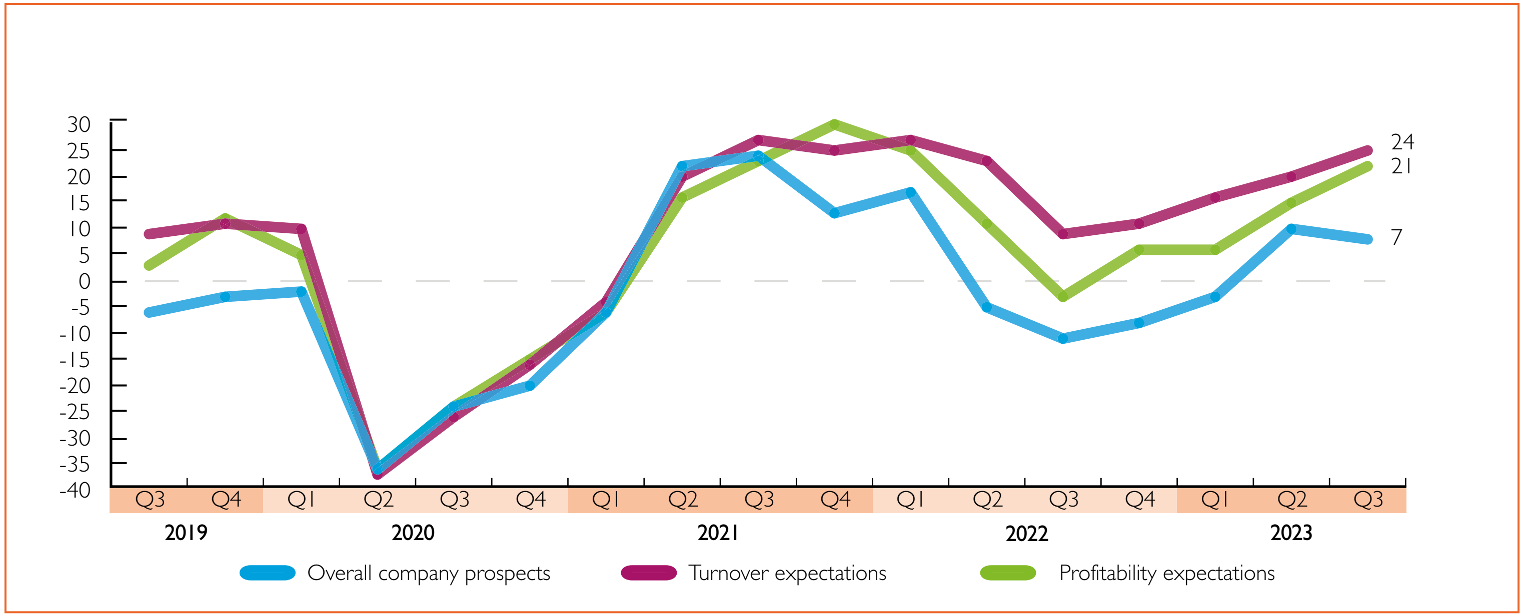
Just over two in ten (22%) micro companies said cashflow had risen in Q3, while the proportion who saw a decline in cashflow shrunk from 41% to 34%. The cashflow balance for micro firms improved from -21 to -12 as a result. By contrast, the cashflow net balance for larger firms fell from +22 to +18 in Q3.

Investment in plant and equipment was steady last quarter, with the net balance edging up 2 points to +5: 17% of businesses said they had increased capital expenditure, slightly up on Q2. Around one in ten (12%) firms said they had lowered spending on plant and equipment.

For micro companies, the net balance for investment in plant and equipment nudged up 2 points to +2 in Q3, while for larger firms the balance slipped from +29 to +21.

There was a significant increase in the plant and equipment investment balance for manufacturing companies in Q3 (up 19 points to +27), although this metric can be quite volatile. For service sector companies spending on plant and equipment was unchanged from Q2 to Q3.

BUSINESS CONFIDENCE



43% of London businesses expect their profitability to **improve** over the coming 12 months

42% of London businesses expect their turnover to **improve** over the coming 12 months

London businesses were more upbeat about their underlying financials in Q3. Turnover expectations for all companies improved for a fourth consecutive quarter, with the net balance climbing 5 points to +24: this was the highest reading in one-and-a-half years. In Q3, more than two-fifths (43%) of London businesses thought that their turnover would increase over the coming 12 months, while the share of firms who think turnover will decline shrunk slightly from 20% to 19%.

Both micro and larger firms were more upbeat on their turnover expectations. For micro companies, the turnover expectations balance climbed 5 points to +23 in Q3, with 42% anticipating an increase over the coming year. The improvement for larger firms was more pronounced: the net balance for turnover expectations jumped 9 points to +42 in Q3. More than half (54%) of larger businesses think their turnover will increase in the next 12 months.

Profitability expectations strengthened in Q3 as well, as the net balance rose 7 points to +21. As with turnover, more than two-fifths (42%) of London companies think their profitability will increase over the year ahead. Two in ten (21%) think their profitability will worsen, down from 25% in Q2.

There was a divergence based on business size. For micro firms, the profitability expectations balance rose 7 points to +18 in Q3, on the back of a bigger share of micro businesses anticipating an increase over the next 12 months. By contrast, profitability expectations from larger companies were slightly down in Q3, with the net balance slipping 6 points to +42: this is still a high reading by historical standards.

Despite this improved outlook for turnover and profitability, businesses were slightly less optimistic about their overall company prospects in Q3. The net balance fell 2 points to +7, as the share of firms who felt their prospects would improve in the next 12 months shrunk from 33% to 30%.

ECONOMIC OUTLOOK

25% of London businesses expect London's economy to **improve** in the next 12 months

25% of London businesses expect the UK's economy to **improve** in the next 12 months

Business confidence for London's economic outlook has stalled somewhat in the most recent Capital 500 survey. The net balance for businesses' expectations for the London economy edged up 1 point to -13 in Q3, with 25% of firms anticipating the capital's economy will improve in the next 12 months. Four in ten (38%) firms expect London's economy will worsen in the coming year, unchanged from the previous Capital 500 survey.

This was due to a sharp pullback in confidence among larger businesses: the proportion of larger firms who think London's economy will grow shrunk from 37% in Q2 to 22% in Q3, while there was also an increase in the share who expect the capital's economy to worsen (from 26% to 36%). The net balance slumped from +11 to -14 as a result. It is worth noting however that in recent quarters, this metric has been volatile.

By contrast, micro firms were less pessimistic about London's economy in Q3. The net balance for micro companies' expectations for the capital's economy rose from -16 to -13.

There was a bigger shift in firms' views on the wider UK economy in Q3. A quarter (25%) of companies thought that the UK economy would improve in the coming year, up slightly from 23% in Q2. The proportion of businesses expecting the UK to worsen also shrunk, from 44% to 38%. This pushed the net balance up 8 points to -13 in Q3, an 18-month high. This was also the fourth consecutive improvement in the UK economic outlook.

As with their views on London, there was a divergence in business opinion based on the size of the firm. For micro companies, the UK economic outlook improved in Q3 (net balance rose 10 points to -13). However, for larger businesses the balance fell sharply from +7 to -17, with far fewer larger firms expecting the UK economy to grow in the next 12 months.

Q3

James Watkins
Head of Policy and Public Impact
jwatkins@londonchamber.co.uk

Stephen Jones
Policy and Research Manager
sjones@londonchamber.co.uk