LONDON CHAMBER of COMMERCE AND INDUSTRY

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CAPITAL 500

LONDON QUARTERLY ECONOMIC SURVEY

Q3

2019

COMRES

July - September 2019

LCCI COMMENTARY – THE BUSINESS VIEW

"While it is somewhat gratifying to report that, for a second consecutive quarter, the Capital 500 has returned results that are better than expected, given the uncertainty of Brexit and the ongoing political turmoil, this is not a time for complacency.

Several performance indicators have had their most positive reading in 2 or 3 years. For example, export orders are now at their highest since Q2 2017, while the business investment indicator had its largest increase since Q1 2016.

The capital continues to face a skills challenge, and training has increased as businesses continue to upskill existing employees to fill recruitment gaps. London's continued skills challenge should be top of mind as ministers design a new immigration system. LCCI is clear that regional flexibility must be a central feature.

It is important to note positivity when it presents. This quarter's welcome report is testament to the resilience and tenacity of London firms to continue trading in a testing environment. However, while some figures have improved, they remain low compared to pre-referendum levels. Only clarity and certainty can create a pathway towards consistent positivity.

As we look ahead to the European Council meeting on 17 October, where Prime Minister Johnson will seek to secure a new deal with the EU, LCCI can advise that the majority of London's businesses want the avoidance of a no-deal Brexit.

The ongoing political battles in and outside Westminster are, while frustrating, largely immaterial to firms as long as the worry and threat of a cliff-edge exit recedes."

Sean McKee, Director of Policy and Public Affairs, LCCI

ABOUT '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.

Since Q2 2014 we have worked with leading polling company, ComRes, to expand the survey beyond LCCI membership to poll a panel of London businesses that are fully representative of the London economy by business size and broad industry sector. **The LCCI QES is based on responses from over 500 London businesses – the *Capital 500* – that makes it London's largest and most authoritative regular business survey.**

Since Q1 2016, the *Capital 500* has included trend graphs that track the quarterly results for the past two years.

METHODOLOGY

ComRes surveyed a total of 505 London business leaders between 31 July and 12 September 2019.

All data were weighted to be representative of all London businesses by company size and broad industry sector.

ComRes is a member of the British Polling Council and abides by its rules. Full data tables are available at www.comresglobal.com.

The balance figures represent the percentage of firms that reported an increase minus the percentage that reported a decrease. The arrow figures represent the percentage point change in the balance on the previous quarter.

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.

GUEST COMMENTARY – THE ECONOMIST'S VIEW

"The Q3 QES data shows hopeful signs of resilience among businesses in London, against a worsening global economic scenario and continued – or rather heightened - political uncertainty over Brexit. The ECB and the US have cut interest rates recently and the Bank of England has warned of stagnant conditions. Meanwhile, the prospect of a no-deal Brexit continues despite Parliamentary legislation. A small recovery in July after the small contraction in GDP in Q2 may not last much longer. Retail sales in August declined by 0.2%, particularly online, which suggests a worried consumer despite improvements in real incomes.

On the export front, much depends on whether current trade disputes are resolved and on European trends where activity has suffered, especially in Germany. But the main worry for continued competitiveness in the UK economy remains the weak investment outlook, including foreign direct investment and poor productivity figures resulting from this. The OECD recently reduced its UK growth expectations to no more than 1% for this year and 0.9% next if leaving with a deal, predicting a contraction for three years running if no deal materialises. In the short term, the question remains whether any upward trend we may see in the coming months will be a result of stockpiling in advance of the October Brexit deadline, rather than any underlying strength in the economy."

Vicky Pryce, Centre for Economics and Business Research (Cebr)

DOMESTIC DEMAND

Q3 2019 domestic sales tick up into positive territory, while domestic orders continue to linger below zero.

The domestic orders balance figure increased by a single point to -2%, while the domestic sales balance improved from -1% to 1%. This is the first positive reading since Q2 2017.

Micro businesses recorded a 3 point increase in domestic sales, from -3% in Q2 to 0% in Q3 2019, while larger businesses saw a 5 point deterioration to 13%. Turning to domestic orders, larger firms posted a significantly higher score than their micro counterparts (20% compared to -5% for micro firms).

EXPORT DEMAND

In Q3, both Capital 500 export demand figures increased for the second consecutive quarter, to stand at 4% (export sales) and 3% (export orders).

Export orders are now at their highest since Q2 2017.

In terms of export sales, both businesses in Inner London and those located in Outer London saw an uptick this quarter.

The rise was more pronounced in Outer London, however, where the score rose 4 points, compared to a 2 point rise in Inner London.

At this time of political turbulence, Whitehall and City Hall should look to harness the creativity and energy of the capital's businesses to progress the development of a Local Industrial Strategy (LIS) for London. *Whether or not Brexit happens,* the capital must plan to ensure satisfactory productivity in the future. London firms are best placed to identify the strengths, limitations and challenges that may arise. LISL should have an ambitious and comprehensive outlook examining potential opportunities from more devolution, as well as exploring how to positively exploit the interdependencies between London and the other English metro areas.

LABOUR MARKET

During the third quarter of 2019, the employment levels balance climbed into positive territory for the first time since the start of 2016.

Employment expectations also rose, from 6% to 9% as businesses showed confidence that the labour market will remain robust.

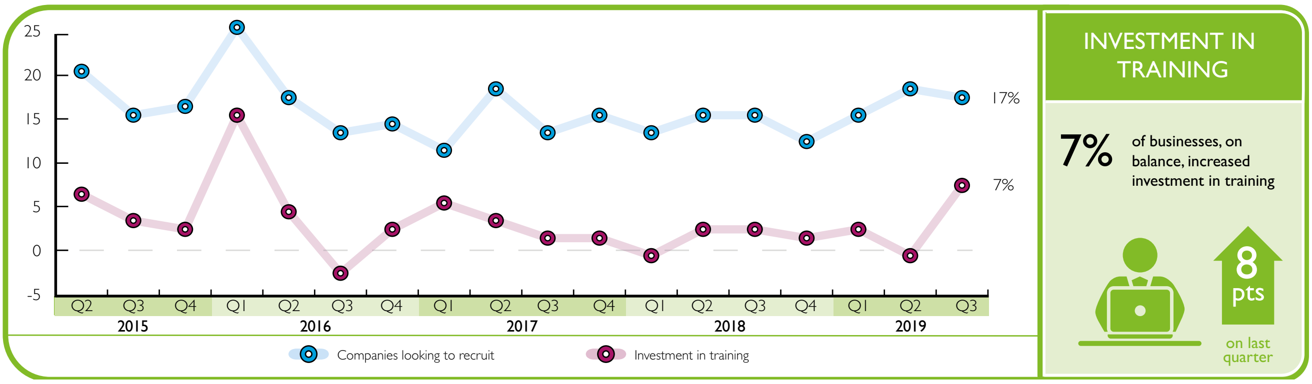
Just under one in five (17%) of London businesses expect their workforce size to increase over the next three months, a 4 point increase on last quarter.

With the UK employment and unemployment rates approaching record high and low levels respectively, the upward trend evident in both scores is little surprise. Larger firms enjoyed an especially strong three months in terms of employment with a score of 12%. This compares to a score of 0% for micro firms.

RECRUITMENT AND TRAINING

In Q3 2019, the balance figure for companies looking to invest in training rose by 8 points, boosting the measure out of negative territory. The share of companies looking to recruit was more stable, decreasing marginally from 18% to 17%.

Of London businesses that tried to recruit in the past three months, more than half (56%) faced difficulties. While this figure remains significant, it has fallen from 61% in Q2 2019.



While it is encouraging that firms have boosted investment in training, a system that equips London's workforce with the rights skills is vital to addressing recruitment challenges, particularly in light of employment levels. This will become increasingly important as technological change continues to advance and as freedom of movement ends post-Brexit.

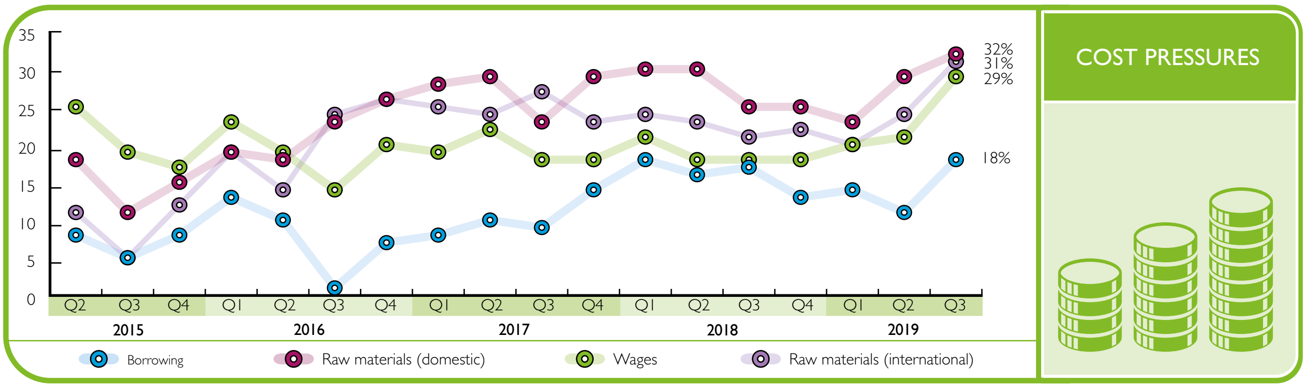
LCCI commends the 'Call for Action' by Mayor Sadiq Khan and London Councils for a new devolved funding deal from Government. The capital needs additional competencies to address the skills needs and employment requirements of London's employers. A new deal delivering a holistic skills and employment system with dedicated apprenticeships, ongoing careers advice, enhanced further education investment as well as control over adult education to embed lifelong learning, would provide a strong foundation for the future economic growth of London.

BUSINESS COSTS AND PRICES

All business cost indicators displayed increased sharply in the third quarter of 2019. Out of the four categories, raw materials sourced domestically have the highest score at 32%.

The balance figure for the cost of fuel – not included in the graph – stood at 39% in Q3 2019 down from 44% in Q2. This cost element is likely to exert even greater pressure on businesses in the coming months, given that the recent attacks on Saudi oil facilities have substantially disrupted supply.

The balance figure for the pressure to increase wages jumped 8 points. This is reflective of a tight labour market pushing up wages.

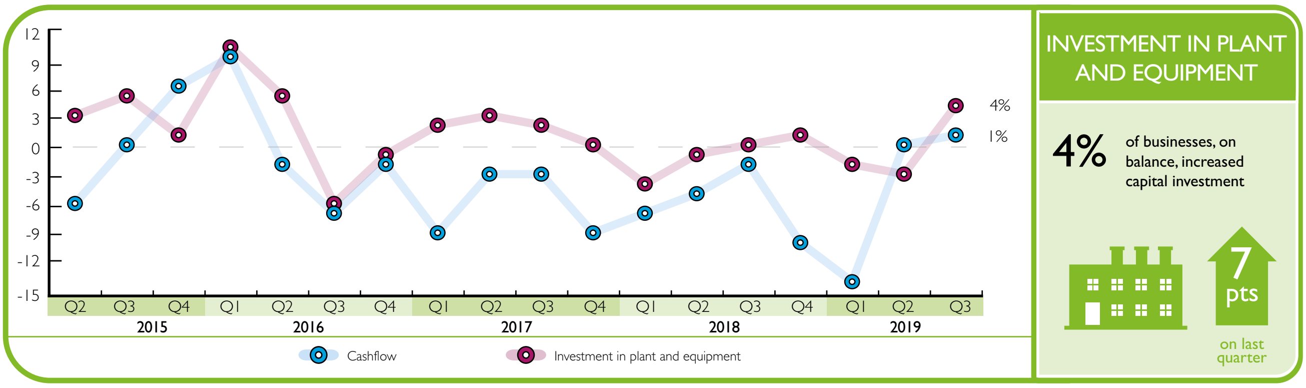


CASHFLOW AND INVESTMENT

In Q3 2019, the cashflow balance figure improved further and rose to 1%, building on the strong gains made in the previous quarter. This means that the cashflow balance figure is now above 0% for the first time since Q1 2016.

The business investment indicator saw a strong 7 point increase over the quarter to 4%. This was the largest increase in the indicator since Q1 2016. This is good news for the UK economy, as weak investment has been one of the most persistent problems weighing on growth over recent years.

The investment score has risen both for micro and for larger companies. However, there remains a significant gap between the two with larger businesses achieving a score of 17% while the score for micro businesses stands at just 3%, following three quarters of negative balances.



With cost pressures rising, the price many London businesses are paying for the continued delay to the opening of Crossrail, coupled with the spiralling cost of HS2, is doing little for general business confidence.

With an ever-increasing population the capital needs transport upgrades. In any post-Brexit scenario London will need adequate infrastructure to compete against other major cities and remain an attractive location to live, work and invest. The delays with Crossrail have been disappointing but the project is nearing completion. However, there will be learnings from Crossrail for both government and City Hall, when considering other London-linked strategic infrastructure projects. The Oakervee review of HS2 provides a platform for a robust analysis of cost benefits and an opportunity to build a clear understanding of the project's business case.

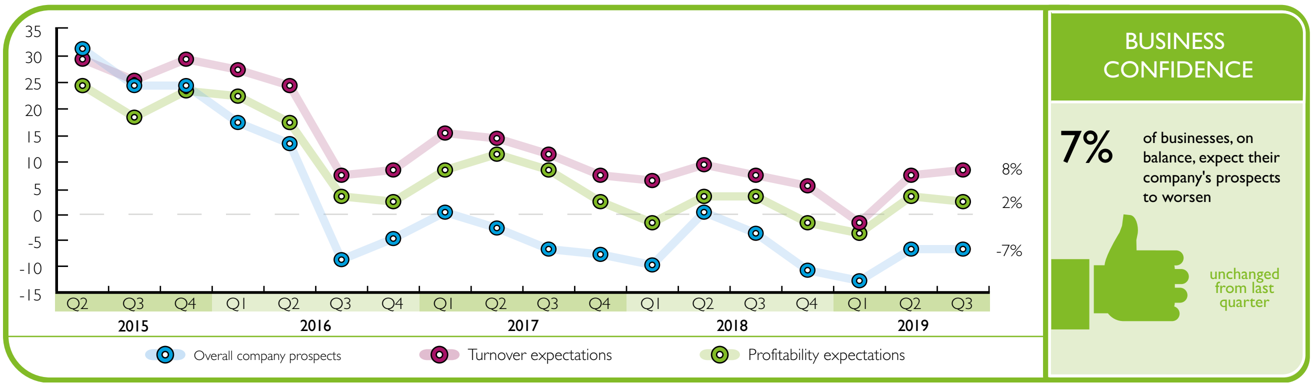
BUSINESS CONFIDENCE

In Q3 2019, the business confidence indictors showed a mixed picture with profitability expectations falling by 1 point to 2%.

Meanwhile, businesses were more confident that their turnover would increase, leading to a 1 point increase to 8% for the indicator, the highest level since Q2 2018.

The diverging performance between the two indicators suggests that even as demand remains resilient, businesses are facing higher cost pressures weighing on profitability.

As a result, the net score for overall company prospects remained unchanged at -7% in the third quarter.



ECONOMIC OUTLOOK

Expectations for the London economy worsened in Q3 2019 as the net balance figure for the capital dropped to -23%, down 6 points from last quarter.

Meanwhile, the UK-wide economic outlook also deteriorated with the net balance falling to -33%, down from -28% in the second quarter.

The decline in the economic outlook comes on the back of reports of an output contraction in the UK economy in the second quarter. While growth seems to have returned in July, the data showed that London as well as the wider UK economy remain vulnerable as growth in exports and business investment remains muted. Looking ahead, businesses clearly see a challenging picture emerging as the risk of a no-deal Brexit continues.

The majority of London firms are of the view that a 'no-deal' Brexit scenario would be harmful to their business. The reassurance that firms need to plan ahead is nowhere in sight with political battles ongoing in Parliament. Ministers must recognise that firms have faced uncertainty for too long and now move to provide some indications on the future UK business environment.

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