LONDON CHAMBER of COMMERCE AND INDUSTRY

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CAPITAL 500

LONDON QUARTERLY ECONOMIC SURVEY

Q2

2018

ComRes

April - June 2018

LCCI COMMENTARY – THE BUSINESS VIEW

"For the second quarter of 2018, we saw an uptick in most of our *Capital 500* indicators of the performance, expectations and plans of London's businesses. Most notably, overall business confidence has come out of negative territory for the first time in well over a year. Although several figures remain negative, for example for domestic demand and capital investment, we welcome positive signals in areas like investment in training, exports and profitability expectations.

"Despite an improvement in many of these figures, much work needs to be done to ensure London businesses continue to prosper, now and in the future. To boost the outlook and confidence of the business community, the Government must urgently make work of securing a longer transition period after Brexit, to ensure that businesses have enough time to adapt to the new circumstances, and boost investment in export support to enable firms to benefit from the opportunities to increase trade around the world. The Mayor also has important steps to take, including by ensuring the Ultra Low Emission Zone will not disproportionally impact on London's SMEs, while we continue to call on boroughs to adopt more flexible definitions of local labour when setting their Section 106 requirements so that apprentices can move across boroughs and complete their training."

Colin Stanbridge, Chief Executive, 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 partnered 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 11 May and 8 June 2018. 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

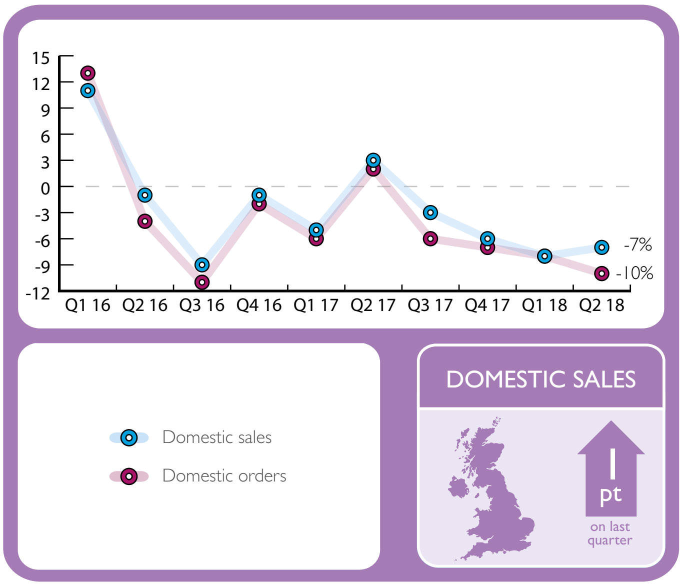
"The LCCI survey data confirm what is generally seen across the economy, namely a slow pick up from the very low activity of the first quarter. There has been some recovery in retail activity, but pressure on the sector remains and despite record employment and increasing skills shortages in many areas of the economy, the CEBR/YouGov consumer confidence indicator fell again last month.

"There is little indication so far of any meaningful pick up in business investment. There have been some prominent announcements of manufacturing cutbacks and job losses, including of Airbus of their intention to focus new investment elsewhere until the path after Brexit is clear.

"The escalation of trade wars has added to concerns about the impact on particular export sectors and industrial activity in the EU, which remains the UK's main trading partner, has slowed down in the first half of 2018. Recent forecasts for the UK have accordingly downgraded growth expectations over the next few years."

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

DOMESTIC DEMAND



More businesses continued to report a decline in domestic demand than an increase during Q2 2018, while figures have now been in negative territory for eight out of the last nine quarters.

The domestic orders balance figure fell for the third consecutive quarter to -10% – its second lowest recorded *Capital 500* level to date (which is only slightly higher than in Q3 2016, the first post-referendum poll). The domestic sales balance rose by 1 point but remained negative at -7%.

For both domestic orders and sales, larger businesses continued to report positive figures (+14% and +16% respectively), while micro businesses reported negative figures (-12% and -10%). Similarly, outer London businesses continued to report a lower balance for both orders (-13%) and sales (-11%) than inner London businesses (-5% for orders and 0% for sales).

EXPORT DEMAND

In Q2 2018, a slight uptick was recorded in the *Capital 500* export demand figures, while four in ten respondents (40%) reported they had been exporting during the past three months.

The balance figure for export orders bounced back from negative territory (up 1 point), with as many businesses reporting an increase as a decrease. Export sales also recorded a 1 point rise, resulting in a balance of +1%.

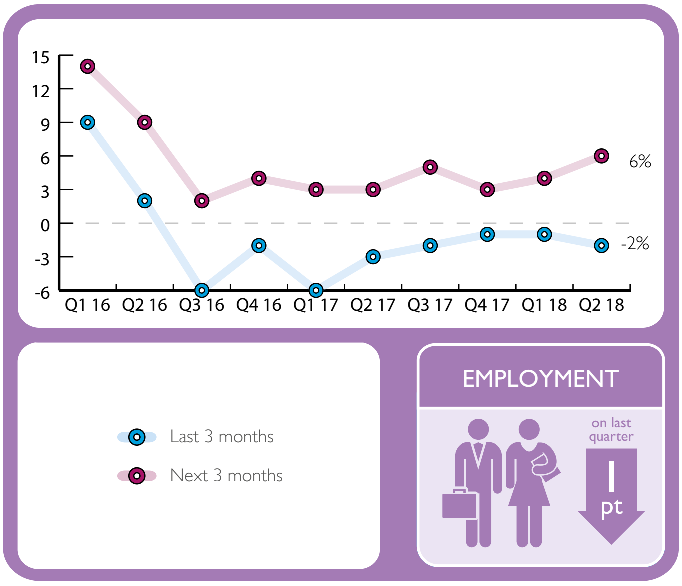
While micro businesses did not report a positive balance for either export orders or sales (-3% and 0% respectively), larger businesses continued to report a positive balance for both (+21% for orders and +15% for sales).

ComRes polling for LCCI has shown that exporting London businesses continue to face significant barriers to increasing their exports. Almost four in ten (38%) encountered difficulties finding overseas customers, agents or distributors, and two in ten exporters (20%) reported difficulties because of the cost and quality of international transport connections.[1] LCCI has been facilitating international trade since 1881 and knows from experience that many businesses, SMEs in particular, can benefit from active trade support, including through subsidised trade missions. Furthermore, given the UK's reliance, as an island economy, on frequent and direct air links with high-growth markets around the world, addressing airport capacity constraints will be vital to enabling further exports growth.

The Government should consider stepping up efforts to support exports growth through subsidised trade missions and increased funding for the Department for International Trade (DIT). Furthermore, with Brexit on the horizon, LCCI calls on the Government to boost airport capacity, including by enabling a new runway at Gatwick.

[1] ComRes survey for LCCI of 561 London business decision makers, February-March 2018.

LABOUR MARKET



During Q2 2018, the employment balance dipped slightly, and continued to be negative overall for the eighth consecutive quarter, with more businesses reporting a fall than a rise in employment levels.

However, a significant difference was recorded between micro businesses and larger businesses. While the employment balance for micro businesses dropped by 5 points to -6%, the balance for larger businesses rose by 16 points to +22% – the highest recorded *Capital 500* level to date.

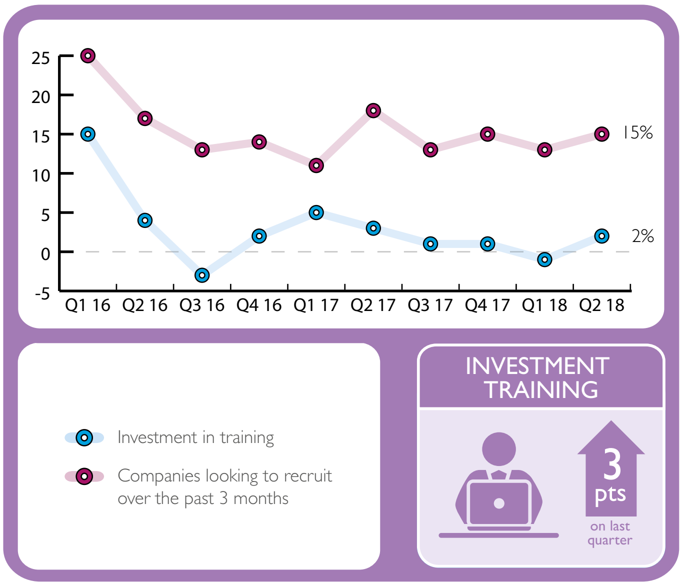
Meanwhile *Capital 500* businesses continued to be positive about their workforce size for the next three months, with on balance 6% expecting their employment levels to rise – up 2 points on last quarter. Again, the figure was higher for larger businesses (+26%) than micro businesses (+4%).

RECRUITMENT AND TRAINING

During Q2 2018, the balance figure of companies looking to invest in training turned positive again, as on balance 2% of respondents raised their planned investment (up 3 points on last quarter). While the balance for micro businesses rose to 0%, the balance for larger businesses stayed positive at +14%.

The percentage of companies recruiting over the last three months rose by 2 points to +15% (9% for micro businesses; 63% for larger businesses). Of these, 64% recruited for full-time and 42% for part-time positions.

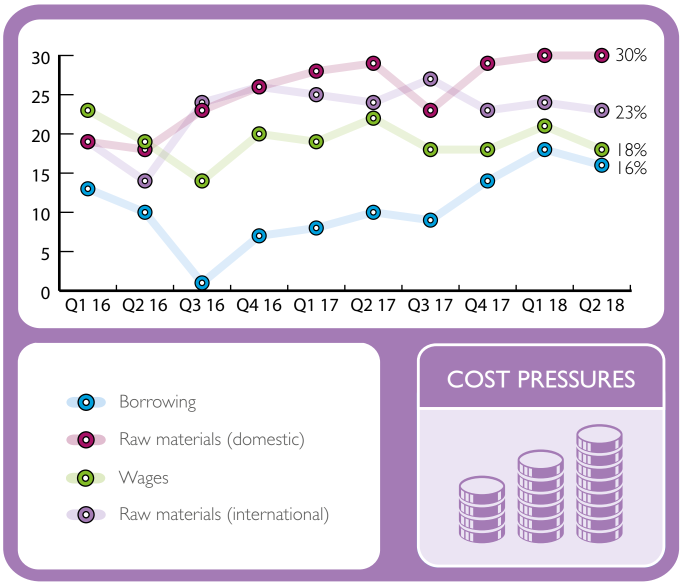
Of companies trying to recruit over the last three months, 60% encountered difficulties, the joint highest recorded *Capital 500* level to date, and up 9 points on Q1 of this year. In contrast to last quarter, professional/managerial positions where the hardest to fill for recruiting companies (45%, up 5 points), followed by skilled/manual technical roles (39%, down 24 points).



To address escalating business concerns around future access to both high and lower skilled labour, LCCI continues to call for a practical post-Brexit immigration policy that is both flexible and meets the needs of business. The current rigidity of the apprenticeship system also continues to hamper firms' ability to plug skills gaps and needs to be addressed. For example, more flexible definitions of 'local labour' when setting S106 agreements are required, in addition to allowing firms greater flexibility on how levy funds are spent. However, we are encouraged by the Mayor's focus on the skills agenda, notably through the publication of the first standalone skills strategy for capital.

London boroughs should employ more flexible definitions of local labour when setting Section 106 requirements to allow apprentices to move across boroughs and complete their training.

BUSINESS COSTS



During Q2 2018, the balance figure for the cost of raw materials sourced domestically (+30%) remained higher than for raw materials sourced internationally (+23%). Meanwhile, the figure for the cost of borrowing reached its second highest recorded level to date at +16%, following a 2 point drop on last quarter, and the pressure of employees to increase wages fell by 3 points, to +18% on balance.

The figures for the cost of energy and cost of fuel (not included in the graph) continued to be highest of all analysed costs and reached respectively their joint highest (+48% for fuel) and second highest level (+40% for energy) to date.

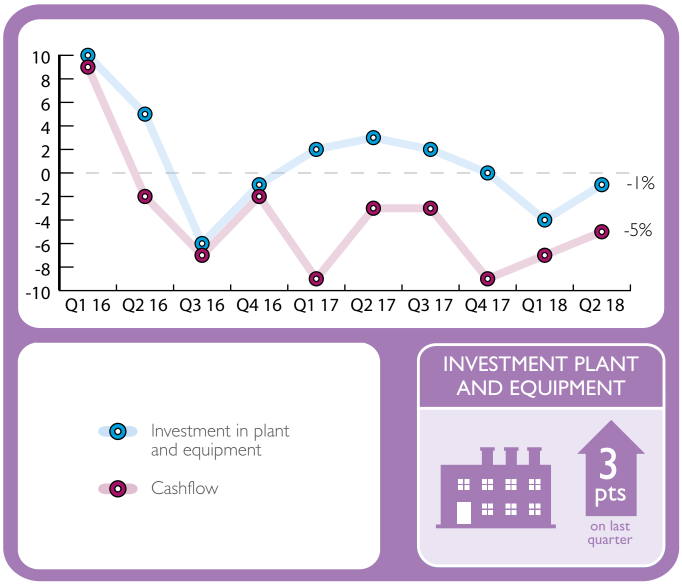
The main cost factors putting pressure on businesses to raise their prices were raw material prices (24%) and other overheads (33%). 23% of businesses, on balance, reported they expected the price of their goods or services to rise over the next three months (+21% for micro businesses; +36% for larger businesses).

CASHFLOW AND INVESTMENT

While both the cashflow figure and the capital investment figure rose on last quarter, they remained in negative territory.

With 38% of London businesses reporting they had been operating at full capacity (up 2 points on last quarter), the capital investment balance rose by 3 points to -1%, as fewer businesses increased than decreased their planned investment in plant and equipment. The cashflow balance continued to rise by 2 points but remained negative at -5%.

While the capital investment figure for larger businesses dropped by 5 points, it stayed in positive territory at +10%. In contrast, the figure for micro businesses continued to be negative at -3%, although it rose by 3 points on last quarter. Similarly, the cashflow figure remained higher for larger businesses (+4%) than for micro businesses (-6%), while the balance for larger businesses fell and for micro businesses rose.

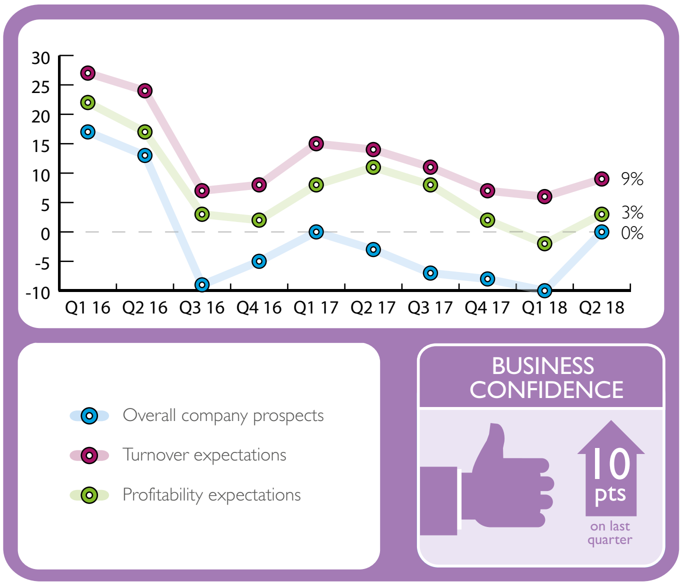


Plans to bring the introduction of the Ultra Low Emission Zone (ULEZ) forward by a year, and proposals to expand it to HGVs entering the whole of London and vans within the North and South Circulars in 2021 will impact on the costs of businesses operating throughout the capital. A TfL commissioned impact assessment[2] cited increased 'operating costs, decreased profitability and reduced levels of business' as potential impacts of a stronger low emissions zone,and suggested a tighter timetable may disadvantage SMEs who do not have the necessary resources to update their fleets as regularly as large companies. LCCI is concerned about the impact that a stronger ULEZ will put on SMEs in particular, and believes the proposals must strike the right balance between delivering improvements to air quality whilst allowing businesses to adapt to changes.

The GLA should outline support measures for businesses affected by ULEZ. Furthermore, publication of economic assessment of impacts on London businesses, particularly SMEs, would be welcome.

[2] Jacobs (December 2017) Ultra Low Emission Zone – Further Proposals: Integrated Impact Assessment.

BUSINESS CONFIDENCE



During Q2 2018, all *Capital 500* business confidence indicators recorded a reverse of last quarter's decline.

The *Capital 500* balance figure for overall company prospects logged a record level increase on last quarter (up 10 points) and is no longer in negative territory at 0% – the joint highest recorded level since Q2 2016, the last poll before the EU referendum. The other figures also rose on last quarter, by 5 points for profitability expectations and 3 points for turnover expectations, to +3% and +9% respectively.

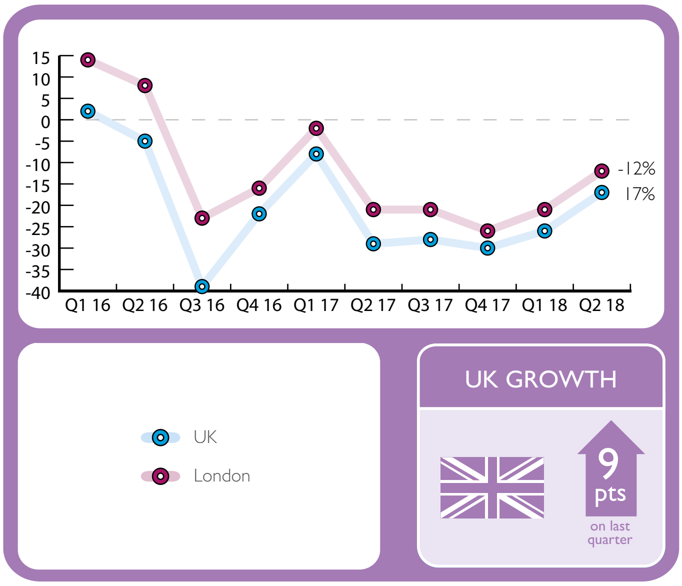
While the overall prospects for micro as well as larger businesses rose by 9 points on Q1 of this year, the figure stayed negative for micro businesses (-2%) and positive for larger businesses (+13%). On that same measure, both inner London and outer London businesses recorded a balance figure of 0% overall.

ECONOMIC OUTLOOK

Expectations for both the London and UK economy remained negative on balance, and have now been in negative territory for respectively eight and nine consecutive quarters.

The balance figure for expectations of the UK economy (-17%) as well as the London economy (-12%) rose by 9 points on last quarter, as more businesses continued to expect these prospects to worsen than improve over the next 12 months.

Inner London businesses remained more pessimistic about both the national and London economy (-21% and -14% respectively) than their outer London counterparts (-13% and -9% respectively), although compared to last quarter the gap between inner and outer London businesses shrunk by 8 points for the capital's prospects, and 12 points for the prospects of the country.



LCCI polling since the EU referendum has consistently found that avoiding a 'cliff edge' is the top priority for London business leaders. To boost confidence across the capital's economy, implementing a longer transition period of three to five years would be beneficial. The transition period the UK and EU have now agreed, of around 90 weeks is not enough to allow the bulk of UK firms to adapt to the new trading environment – whatever that will be. This will be particularly important if the final detail of the new UK-EU relationship will not be known until much later, perhaps even during the transition period.

The proposed 90-week transition period will not be enough for many London businesses. A three to five-year transition, under the current UK-EU arrangements, would be deemed reasonable by the greater number of them to adjust to the new circumstances.

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