

CAPITAL 500

LONDON QUARTERLY ECONOMIC SURVEY



2017



LCCI COMMENTARY – THE BUSINESS VIEW

“The second *Capital 500* of this year, undertaken either side of the general election last month, shows the continued resilience of the capital's business community. While uncertainty remains part of the economic landscape - not least given developments in the UK's political scene following the general election result but also as Brexit negotiations begin - most business performance indicators have gone up, including for domestic sales, export sales, capital investment and recruitment. However, expectations for the future are mixed. Although businesses continue to have positive expectations for their future profitability and turnover, they are, on balance, pessimistic about their company's overall prospects as well as those for both the London and UK economy.

“Now is the time to boost confidence amongst the capital's business community. This means receiving positive signals from early Brexit negotiations that business concerns are being heard, including on the importance of 'frictionless' trade and ongoing access by UK companies to workers from overseas. Crucially, it also requires concrete steps to address the capital's pressing domestic priorities, including making sure young Londoners have the right skills to succeed in the jobs of tomorrow, that the capital's pressing 'megacity' infrastructure needs are met, and that rising business costs are addressed before they undermine competitiveness.”

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

METHODOLOGY

ComRes surveyed a total of 530 London business leaders between 23 May and 19 June 2017. All data has been 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

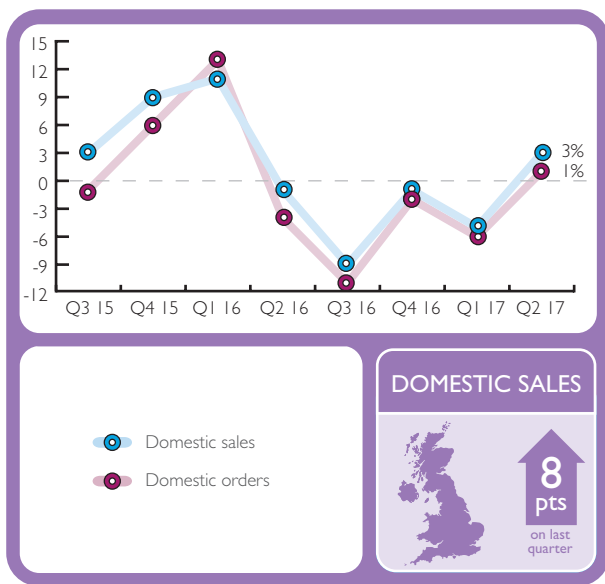
“It is encouraging that businesses in London remain resilient despite the uncertainty of Brexit. The economy as a whole has continued to benefit from a pickup in international trade, particularly from Europe which is growing at the fastest rate in 6 years - demonstrating, if anything, our dependence on Europe for prosperity and growth.

“Sterling's depreciation continues to help exports although the current account data still doesn't reflect this as the price of imports has also been rising fast. Firms still find it difficult to pass increased costs up through the supply chain, affecting profitability and cashflow. And with wage growth lagging behind inflation, which is now running at 2.9%, consumer spending is much more shaky reflecting falls in real disposable incomes.

“Since the shock snap election result which has weakened the government's Brexit negotiating stance, the final outcome is even less clear. Additionally the Bank of England is now embarking on some tightening of credit conditions. It is hardly surprising therefore that firms in this survey have suddenly turned more pessimistic again about the prospects for the economy.”

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

DOMESTIC DEMAND



Following a decrease in the previous quarter, *Capital 500* domestic demand figures rose again during Q2 2017. The figures are now back in positive territory for the first time since Q1 2016, as more businesses reported an increase than a decrease in both domestic sales and orders.

The balance for domestic orders rose by 7 points to +1% while the balance for domestic sales saw an 8 point increase to +3%.

While for larger businesses the domestic sales balance did not change much from last quarter (from +18% to +20%), an increase of 9 points was recorded for micro businesses (to +1%). On that same measure, the balance for Outer London businesses came out of negative territory (at 0%), while businesses in Inner London continued to report a positive figure (+6%).

EXPORT DEMAND

Following overall stagnation in the first quarter of 2017, the *Capital 500* export demand figures increased again during Q2 of this year.

While the balance figure for export sales saw a 1 point rise, the export orders balance increased by 3 points. This is the first time the figures have gone up since Q1 2016, and the balances are now back in positive territory for the first time since Q3 2016.

In terms of both export sales and orders, Outer London businesses (+3% for sales and +5% for orders) outperformed their Inner London counterparts (0% for sales and +2% for sales), which is a reversal from the previous quarter. The balances for larger businesses declined from Q1 but remain positive overall (+9% for sales, +6% for orders), while in contrast to last quarter, the balances for small businesses were no longer negative (0% for sales, +2% for orders).



The EU is the UK's biggest export market, and UK businesses are part of value chains stretching across the continent. Any increases in trade and investment barriers post-Brexit will harm UK business, be it through increased import costs or lower export demand. Whilst minimising actual tariffs will be imperative, preventing new non-tariff barriers will be no less important – including in relation to customs procedures, quotas and product standards.

Avoiding additional barriers to trade post-Brexit must be a top priority for negotiations with the EU. If customs procedures between the UK and EU are reintroduced, an enhanced system for clearing customs that allows pre-clearance away from the ports of entry must be designed and adequately resourced.

LABOUR MARKET



Although the *Capital 500* employment figures went up compared to Q1 2017, they remained in negative territory for the fourth consecutive quarter.

Coming from a *Capital 500* record low at -6%, the balance figure for business' employment levels over the past three months rose by 3 points during Q2 2017, but stayed negative overall. Expectations for the next three months remained unchanged, as on balance, 3% of businesses expect their workforce to grow.

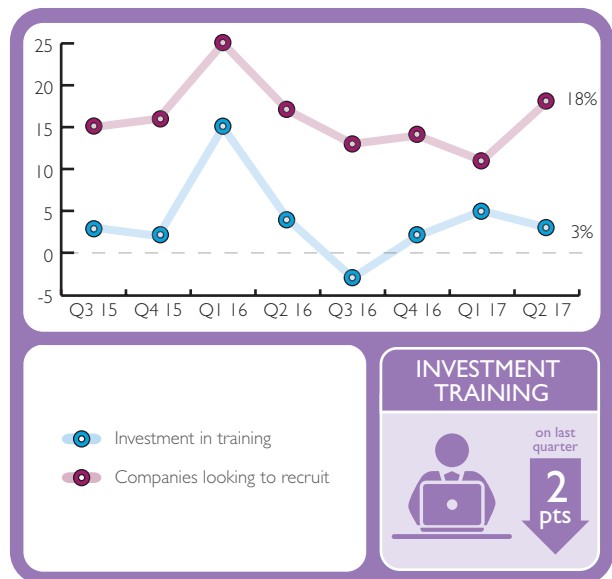
While the employment balance for larger businesses declined from 8% to 0%, the balance figure for micro businesses went up to -3% (from -8%) - resulting in a narrowing of the gap by 15 points. In terms of employment expectations, the balance figures for both micro businesses and larger businesses changed by just one point (to +1% and +21% respectively).

RECRUITMENT AND TRAINING

The balance of companies looking to invest in training declined during Q2 2017, but remains positive. On balance, 3% of *Capital 500* companies were looking to invest in training, down 2 points on Q1's figure.

18% of *Capital 500* companies were trying to recruit during Q2 2017, up 7 points on last quarter – the biggest rise since Q1 2016. 62% recruited for full time positions (down 3 points) and 38% for part time positions (up 5 points).

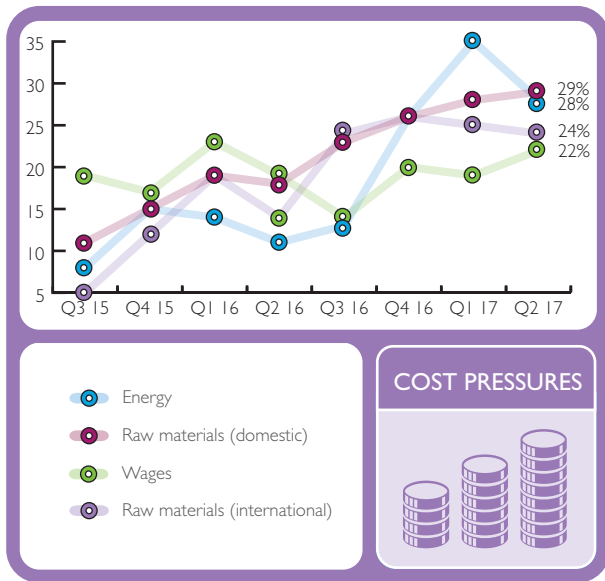
Of the companies looking to recruit, half (52%) encountered difficulties finding sufficiently skilled candidates – up from 47% in Q1. Professional/managerial roles (54%, up from 43%) and skilled manual/technical roles (42%, down from 50%) were the hardest to fill for recruiting *Capital 500* companies.



In recent years, the government has made it increasingly difficult to hire workers from overseas, and further restrictions are anticipated with the end of the current system of free movement of people between the UK and EU. To plug the capital's ongoing skills gaps, it is essential that any Industrial Strategy prioritises upskilling the capital's domestic workforce and making sure young people have the skills needed to succeed in tomorrow's economy. This means adequate schools funding and an ongoing focus by government on technical education both for young Londoners and those looking to retrain, in addition to a flexible, demand-led migration system post-Brexit.

The new government should guarantee high-quality work placements for students pursuing a technical route and prioritise new 'T-Levels' in Construction and Digital areas to help meet the demands of the UK industry and support young people into long-term sector careers.

BUSINESS COSTS



In terms of business costs, *Capital 500* businesses reported a mixed picture for Q2 2017. The balance figure for the cost of raw materials sourced domestically reached its highest recorded level at +29%, following a 1 point rise on last quarter. At +24%, the balance for the cost of raw materials sourced internationally continued to be lower than for domestic materials, down 1 one point on last quarter.

The balance figure for the cost of employees to increase wages rose by 3 points to +22%, while the balance for the cost of borrowing (not included in the graph) went up by 2 points to +10%.

Balances for the cost of energy and cost of fuel (not included in the graph) both declined during Q2, by 7 points for energy (to +28%) and by 18 points for fuel (to +30%). Despite these decreases, balances continue to be relatively high (higher than in any of the quarters in the period from Q3 2014 until Q3 2016).

CASHFLOW AND INVESTMENT

While *Capital 500* businesses' capital investment continued to rise, cashflow balances remained negative.

The cashflow balance increased by 6 points on last quarter, but remained negative overall, as on balance, 3% of businesses reported a decline in cashflow. In contrast, a positive balance was reported for investment in plant and equipment, as 3% of businesses, on balance, planned to increase their capital investment (up 1 point on Q1).

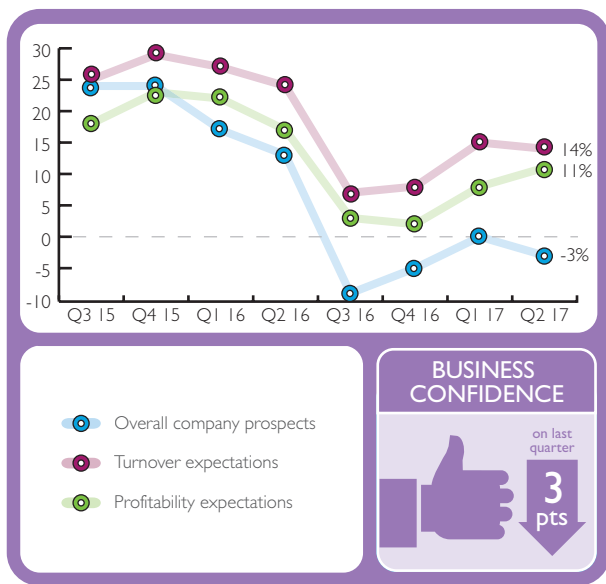
During Q2 2017, for larger businesses the cashflow balance remained positive at +12% (up 1 point), while for micro businesses it remained negative at -4% - an improvement of 7 points on last quarter. For investment in plant and equipment, a positive figure was reported for both micro businesses (+1%, up 1 point) and larger businesses (+17%, up 2 points).



Amid growing inflation, the current uncertainty, both domestic and regarding the UK's future relationship with the EU, is putting a strain on London business. Meanwhile, the capital's businesses have had to absorb several additional business costs, including disproportionate business rates rises, the introduction of the Apprenticeship Levy and Immigration Skills Charge and increases in the national living wage. Consideration should be given to the impact of any further increases in taxes or costs on businesses, and a fundamental review of business rates remains long overdue.

The government should expedite a fundamental review of business rates to ensure the tax remains fit for purpose in today's digital age, and so businesses in London are not taxed disproportionately.

BUSINESS CONFIDENCE



While turnover and profitability expectations remained positive during Q2 2017, overall company prospects declined. On balance, 11% of *Capital 500* businesses expected a rise in their profitability over the next 12 months (up 3 points on Q1) and 14%, on balance, expected the same of their turnover (down 1 point on last quarter).

In contrast, a negative balance was reported for overall company prospects, as, on balance, 3% of businesses expected their economic prospects to worsen – down from 0% in Q1 of this year.

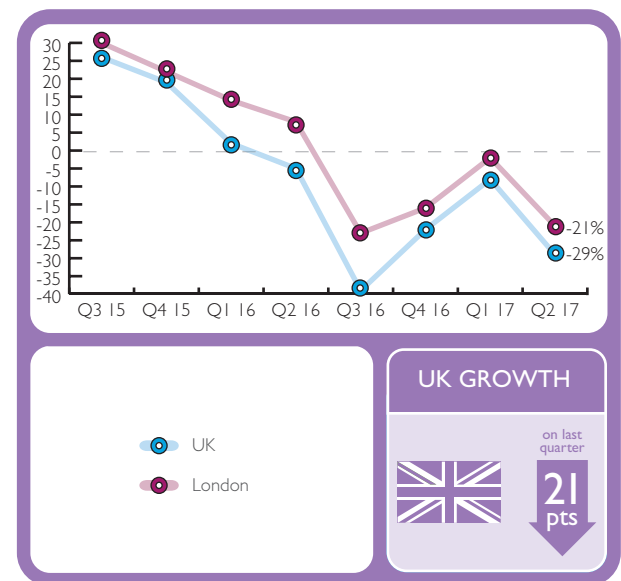
While micro businesses continued to be negative about their company's prospects (-5%), and larger businesses continued to be positive (+6%), both balance figures declined (by 4 points and 6 points respectively). Businesses from both Inner London (-1%) and Outer London (-5%) were, on balance, found to be negative about their company's prospects for the year ahead.

ECONOMIC OUTLOOK

Expectations of both London and the UK economy declined during Q2 2017, and remain negative overall.

Following an uptick in the previous quarter, the balance figure for expectations of London's economy dropped by 19 points to -21%, and the balance figure for the UK economy dropped by 21 points to -29%. Both figures have now been in negative territory for four consecutive quarters, and have reached their second lowest recorded *Capital 500* level (although still markedly higher than in Q3 2016 – the first poll after the EU referendum).

While micro businesses continued to be particularly pessimistic about the prospects of both London (-22%) and the UK economy (-31%), larger businesses, in contrast to last quarter, also recorded negative figures (-1% and -11% respectively).



Now is the time to boost confidence amongst the capital's business community. Although negotiations with the EU27 will be vital for the country's future prosperity, they should not distract from the capital's pressing domestic economic priorities which, if not addressed, risk leaving the capital overcrowded and uncompetitive. These include upgrading London's transport and housing infrastructure, most urgently by designating Crossrail 2 as a major infrastructure project of national importance, as well as boosting London's airport capacity and delivering additional East London river crossings.

The government should commit to progressing London Strategic Infrastructure Projects (LSIPs) including Crossrail 2, fixed river crossings in East London and a new runway at Gatwick, after Heathrow.

For further information on this report, please contact

London Chamber of Commerce and Industry
 E: research@londonchamber.co.uk
 T: +44 (0)20 7248 4444
 W: londonchamber.co.uk/research

Sean McKee
 Director of Policy and Public Affairs
 E: smckee@londonchamber.co.uk
 T: +44 (0)20 7203 1882

Thomas Wagemakers
 Policy Research Manager
 E: twagemakers@londonchamber.co.uk
 T: +44 (0)20 7203 1925