LONDON CHAMBER of COMMERCE AND INDUSTRY

CONNECT. INFLUENCE. SUPPORT.

CAPITAL 500

LONDON QUARTERLY ECONOMIC SURVEY

Q1

2017

ComRes

April 2017

LCCI COMMENTARY – THE BUSINESS VIEW

"The first *Capital 500* survey of 2017, undertaken before the triggering of Article 50 last month, shows an encouraging boost in businesses' confidence and outlook for the year ahead, especially in terms of companies' turnover and profitability expectations. Many business performance indicators also continued to improve, including for planned capital investment and investment in training. However, not all indicators are upbeat. Falling figures for domestic demand, employment and cashflow give some concern, particularly as we prepare for uncertainties during Britain's negotiations with the EU.

"Looking ahead, we need to ensure London has a secure economic foundation to meet the twin challenges of Brexit and the city's growing population – set to reach 10 million by 2030. It is encouraging that the Government has brought forward proposals for a new Industrial Strategy that seeks to address the long-term challenges facing the economy.

"We will look for this strategy to provide a framework that enables London to remain a premier global city, and gives the capital more powers to address its growing infrastructure needs. Above all, while seeking balanced growth across the UK, a new Industrial Strategy must recognise the central role that London currently has – and will continue to play – as the engine of the UK economy."

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 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 504 London business leaders between 14 February and 2 March 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

"The improved confidence in the economic outlook in the survey chimes with higher growth forecasts for 2017 as a whole by the Office for Budget Responsibility, Bank of England, OECD and IMF. But there is a question as to whether the growth momentum we saw in 2016 will be sustained through 2017.

"Growth remains unbalanced. Although exports are picking up due to the fall in the pound and slightly faster world growth, activity in the UK is being sustained mainly by household spending as consumers are borrowing at record levels, encouraged by low interest rates and high employment. But inflation is picking up and at 2.3% is running at the same rate as wage growth and for the first time in years is now higher than the Bank of England's target of 2%.

"At the same time, business input costs are rising by 20% reflecting the pound's drop – at some points these will have to be passed through. Investment is also constrained by uncertainty over Brexit, and the March budget offered little in terms of relief on business costs. Caution ahead is probably what we will see, particularly from the smaller firms which seem hardest hit and the most pessimistic in this survey."

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

DOMESTIC DEMAND

Following an increase in the previous quarter, the *Capital 500* domestic demand figures declined during Q1 2017, and remain negative overall, as more businesses reported a decline than an increase in both domestic sales and orders.

Both balance figures fell by 4 points to -5% for domestic sales and -6% for domestic orders, and have now been in negative territory for four consecutive quarters.

While the balance for domestic sales declined for micro businesses (down 5 points to -8%), a 1 point increase was recorded for larger businesses (to +18%). On the same measure, Outer London businesses reported a negative figure (-13%), whereas Inner London businesses reported a positive balance (+1%).

EXPORT DEMAND

During Q1 2017, the same proportion of businesses reported an increase in export demand as reported a decrease.

The balance figures for both export sales and orders remained unchanged from 2016's final quarter, and continue to be at their lowest recorded *Capital 500* level.

While businesses in Outer London continued to report negative balances for both export sales and orders (-2% and -1% respectively), positive figures were recorded for businesses in Inner London (both +2%). The balances for larger businesses (+14% for sales and +13% for orders) as well as micro businesses (both -1%) remained in line with the results from Q4 2016.

Domestic sales must ultimately be underpinned by a healthy and growing economy. The announcement by the Government of its intention to develop a new Industrial Strategy represents an opportunity strengthen the capital's economic foundations, not least by signalling an end of the UK's over-centralised system. Done well, the Industrial Strategy can help the capital overcome the inevitable challenges of the Brexit process, as well as capitalise on the opportunities of its pending 'megacity' status.

The Government's finalised Industrial Strategy should contain a recognition of London as a key engine of the national economy with its extensive procurement and supply chain across the UK. Efforts to generate balanced growth across the UK should not come at the expense of the capital; London's strategic infrastructure projects should not face unnecessary delay.

LABOUR MARKET

Following an increase in the previous quarter, the *Capital 500* employment figures dropped again during Q1 2017.

The balance figure for businesses' employment levels over the past three months decreased by 4 points, to a *Capital 500* (joint) record low at -6%. In contrast, expectations for the quarter ahead remained positive as, on balance, 3% of businesses expect their workforce to grow.

While micro businesses continued to report a negative employment balance (-8%), larger businesses continued to report a positive figure (+8%). On balance, 22% of larger businesses expect their workforce to grow over the next three months, while micro businesses are as likely to expect an increase, as they are to expect a decrease.

RECRUITMENT AND TRAINING

The number of companies looking to invest in training continued to increase during Q1 2017. The balance for businesses planning to invest in training rose by 3 points, to +5%

11% of *Capital 500* companies were trying to recruit during Q1 2017, down 3 points on last quarter. Two thirds (65%) were recruiting for full-time positions and one third (31%) for part-time positions. Of the companies looking to recruit almost half (47%) encountered difficulties finding sufficiently skilled candidates. Skilled manual/technical roles (50%) and professional/managerial roles (43%) continued to be the hardest to fill for recruiting *Capital 500* companies.

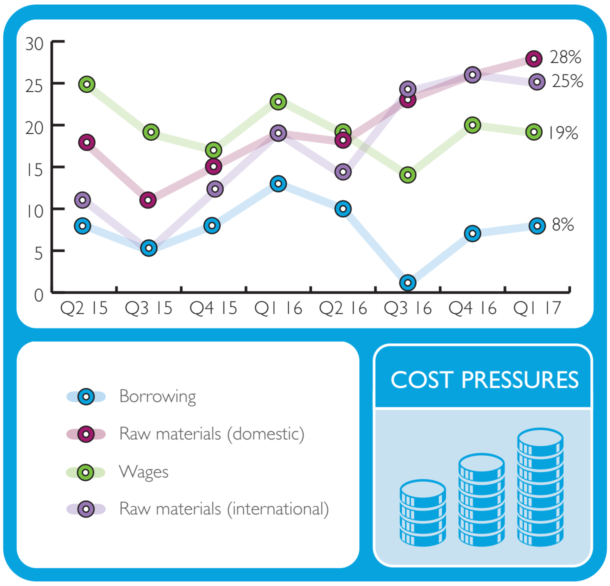
The most frequently recorded methods of acquiring new skills during the last three months were training existing staff (24%, which is the same figure as in Q4 2016) and employing new staff from the UK workforce (8%).

While London businesses continue to face significant difficulties finding suitable candidates for their vacancies, EU workers remain vital to filling urgent skills gaps. Our *Permits, Points and Visas* publication in November 2016 reported that EU nationals make up 15% of London's workforce, and that departure of EU nationals would be economically harmful, impacting upon various key industries such as construction and finance, and would put pressure on public funds.[1]

The Mayor of London should champion a single issue 'London Work Visa' granting 'indefinite leave to remain' in the UK to existing EU National employees – providing reassurance to current employees and their employers.

1 LCCI: "Permits, Points and Visas: Securing practical immigration for post-Brexit London", November 2016

BUSINESS COSTS



Compared to last quarter, cost pressures either went up or remained stable during Q1 2017. The balance figures for the cost of borrowing (+8%), pressure of employees to increase wages (+19%) and cost of raw materials sourced internationally (+25%) all saw a 1 point change on Q4 2016.

The balance figure for the cost of fuel (not included in the graph) rose by 4 points to a *Capital 500* record high of +48%. Another record high was recorded for the cost of raw materials sourced domestically which increased by 2 points to +28%.

The balance for the cost of energy (not in the graph) recorded a (joint record) 9 point rise to +35%.

CASHFLOW AND INVESTMENT

While *Capital 500* businesses' cashflow position worsened during Q1 2017, capital investment continued to rise.

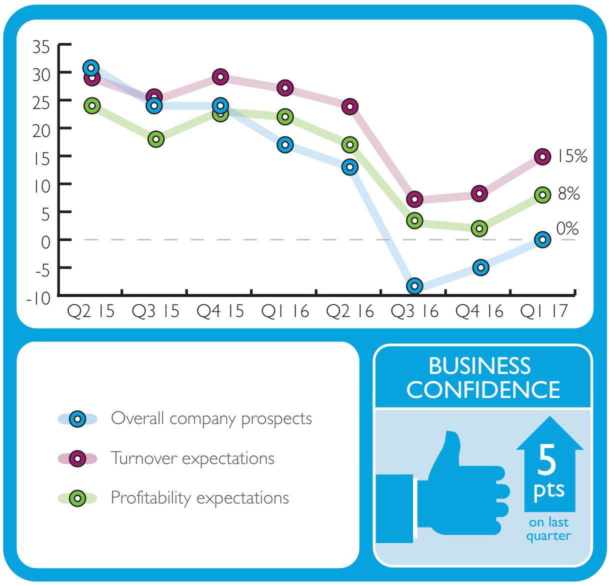
The cashflow balance dropped by 7 points to a *Capital 500* record low of -9%, and has now been in negative territory for four consecutive quarters. In contrast, the balance for investment in plant and equipment rose by 3 points (to +2%), as a positive balance was recorded for the first time since the referendum vote in June 2016.

Whereas for micro businesses the cashflow balance decreased during Q1 2017 (by 8 points) to -11%, the balance for larger businesses continued to rise (by 4 points) to +11%. Although the balance figure for capital investment rose for both micro businesses and larger businesses (up 2 points and 8 points respectively), the former recorded a neutral balance (0%) whereas the latter recorded a positive figure (+15%).

London businesses are being hit disproportionally by the 2017 revaluation of business rates which puts a strain on many businesses' growth and investment plans. The budget announcement on the revaluation was of some relief to London, but was in reality just enough to show that the Government recognises that in many cases the rises are undesirable and unfair. A fundamental review of business rates is long overdue in today's digital age. An innovative change could see a 'de-coupling' of London from the national valuation system - whereby an increase in London's rateable values would not inevitably lead to significant increases in business rates.

While welcome, the discretionary relief announced at the Budget will only be beneficial if it reaches the businesses most affected by the Business Rates revaluation. Government should look to ensure transparency on where, when and how much relief has been allocated in local authority areas across the capital.

BUSINESS CONFIDENCE



All business confidence indicators went up during Q1 2017. The balance figure for overall company prospects rose by 5 points, and came out of negative territory for the first time since Q2 2016 (when a balance of +13% was reported).

The balance figures also increased for turnover expectations (up 7 points) and profitability expectations (up 6 points) to +15% and +8% respectively.

While larger businesses, on balance, continued to be positive about their company's prospects (+8%), micro businesses recorded a negative figure (-1%). In contrast to previous quarters, businesses based in Inner London were more positive about their prospects (+2%) than businesses based in Outer London (-1%).

ECONOMIC OUTLOOK

Expectations of both London and the UK economy continued to improve during Q1 2017, but remain negative overall.

The balance figures for expectations of the UK and London economy both increased by 14 points, to -8% and -2% respectively. This is a substantial improvement on Q3 2016 in particular (the first poll following the referendum), when balances of -39% and -23% were recorded.

Micro businesses, on balance, reported negative a perception of the prospects of both London (-3%) and the UK (-9%); in contrast, larger businesses recorded positive expectations for both (+1% for the UK, +6% for London). Inner London businesses continued to be more pessimistic about both London (-6%) and the UK (-10%), than businesses based in Outer London (+2% and -5% respectively).

Now is the time to boost confidence in the economy and signal to the world that the UK is open for business. The Government should pledge investments in Crossrail 2 and other key infrastructure projects, to increase productivity and unlock new opportunities. In doing so, the Government should avoid pitting regions against one another, as we have seen with High Speed 3 and Crossrail 2, and instead devolve powers to the regions so that they can prioritise their own infrastructure projects.

A revised business case for the Crossrail 2 project is currently before the Department for Transport for consideration. The Government should move to ensure that accommodation is made within Parliamentary timetabling for a hybrid bill by 2019.

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 Wagemaakers
Senior Policy Researcher
E: twagemaakers@londonchamber.co.uk
T: +44 (0)20 7203 1925