# ‘CAPITAL 500’

# LONDON QUARTERLY ECONOMIC SURVEY

Q4 2014

JANUARY 2015

ComRes

LONDON of CHAMBER
COMMERCE AND INDUSTRY

"The latest edition of the *Capital 500* Quarterly Economic Survey, London's biggest and most authoritative business survey, provides a timely health check of London business performance with the General Election now only five months away. While the final three months of 2014 saw marginal declines across several indicators, generally the mood of London business remains positive. There were small gains in domestic sales and recruitment during the last quarter, while firms also indicated strong improvement in their cashflow balances.

"Although businesses remain firmly positive about their own prospects, as well as the UK and London economies, underlying weaknesses may impede growth moving into 2015. Export demand continues to be sluggish and, despite Government committing additional funds towards existing export support services, more far-reaching reform will be required to boost trade.

"Considering the fragile state of the economic recovery, and with political uncertainty likely to gather pace as we near the General Election, political parties should look to provide businesses with greater assurances by laying out their economic plans as soon as possible. The confirmed review of the business rate system also provides Government with a chance to assess how greater London infrastructure investment can support growth prospects in the New Year. With the capital leading the UK's recovery, greater freedom to invest in London's infrastructure would help to drive growth across the wider UK economy and reduce exposure to potential external frailties".

**Colin Stanbridge, LCCI Chief Executive**

# 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 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.**

*Capital 500* QES results are not directly comparable to QES results published between Q1 2008 and Q1 2014, as only LCCI members were polled during this period.

# METHODOLOGY

ComRes surveyed a total of 518 London business leaders between 6 November and 26 November 2014.

All sectors of the London economy were represented including production (4%); property and construction (14%); motor trades (1%); retail and wholesale (13%); transport and storage (2%); information and communication (13%); finance and insurance (3%); professional, scientific and technical (23%); business services (8%); education (2%); health (4%); and arts, entertainment, recreation and other services (8%). All data has been weighted to be representative of all London businesses by company size and broad industry sector.

Balance figures referred to throughout this report are determined by subtracting the percentage of companies reporting decreases from the percentage of companies reporting increases.

Any data reproduced from the report should be fully referenced.

# DOMESTIC DEMAND

**DOMESTIC SALES**

**+2%**

↑ 1 POINT

21% reported increased domestic sales

**Although domestic sales figures increased marginally this quarter, overall domestic demand performance remains disappointing in Q4 2014.** The balance figure for domestic sales rose by one point on the previous quarter to +2%, as 21% of *Capital 500* businesses reported an increase and 19% reported a decrease. However, the balance figure for domestic orders declined by two points to +1% (21% of firms reported an increase and 20% a decrease).

The slight increase in domestic sales correlates with recent data published on the UK manufacturing sector, which has shown marginal improvement following growth in output and new orders (Markit/CIPS: *Purchasing Manager's Index,* December 2014). The UK service sector, however, has shown more significant improvement, supported by a rise in new business volumes (Markit/CIPS: *UK Services PMI*, December 2014).

As UK growth remains unbalanced, it is important that interest rates are kept low for as long as possible in order to minimise the risk of the recovery stalling.

# EXPORT DEMAND

**EXPORT SALES**

**+3%**

↓ 2 POINTS

8% reported increased export sales

**Following an encouraging performance in the previous quarter, the Q4 2014 balance figure for export sales fell by two points to +3%**, with only 8% of *Capital 500* businesses reporting an increase and 5% reporting a decrease. The balance figure for export orders saw a larger decrease by four points to +3%, with 8% of London firms reporting an increase and 5% a decrease.

Recent trade data highlights the difficulty firms are facing in external markets, with new export business decreasing for the third consecutive month. A combination of subdued global market conditions, the weak eurozone economy, and a relatively strong sterling-euro exchange rate is having an impact on UK exporters (Markit/CIPS: *Purchasing Manager's Index*, December 2014). Early interest rate rises risk further adding to the value of sterling at a time when export performance is already struggling in the low interest climate.

Official trade data shows that exports improved slightly between September and October 2014, helped by sales of silver to India and a small increase in exports to the EU. Yet, the lack of significant improvement in export volumes is a major concern, while the trade deficit remains large at £2 billion despite a £0.8 billion decline in September (ONS: *UK Trade October 2014, December 2014*).

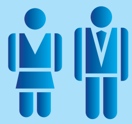
Although the Chancellor's Autumn Statement brought in a welcome package of measures to incentivise businesses to explore trade opportunities, including a £20 million funding increase for UKTI to support first-time exporters, there has been a disappointing lack of progress on export sales in 2014 as a whole. Enhanced government investment may underpin existing export support services but other cross government initiatives to facilitate and foster greater exports activity should be explored. Air Passenger Duty (APD) also remains a barrier to exporting for businesses.

The Home Office should examine how to simplify the visa application process for foreign business people wanting to trade with the UK. While it should ultimately be abolished, in the short term the Treasury should explore the merits of devolving London airport Air Passenger Duty (APD) to the Mayor of London.

# LABOUR MARKET

**EMPLOYMENT**

0%



↑ 2 POINTS

9% increased employment in the last three months

**The vast majority of *Capital 500* businesses (82%) reported no change in employment levels over Q4 2014.** There was a slight improvement in the overall balance figure for employment over the last three months, with 9% of firms reporting an increase in employment levels and 9% reporting a decrease, **leaving a neutral balance figure of 0%. This represents a two point improvement on the previous quarter.**

The capital's businesses have similar expectations about employment levels over the next three months. Over four-fifths (83%) of *Capital 500* firms anticipate no change to their workforce size in the next quarter. 13% of London companies predict their workforce size will increase, four points lower than the previous quarter (17%), while a smaller proportion of companies believe their workforce size will contract (4% against 7% in Q3 2014).

*Capital 500* employment figures compare well with recent UK jobs data, which shows employment levels continuing to rise while unemployment falls (ONS: *Labour Market Statistics*, November 2014).

# RECRUITMENT AND TRAINING

**INVESTMENT**
**TRAINING**

+3%

↓ 6 POINTS

11% increased investment in training

The number of London businesses looking to recruit declined during Q4 2014. Over the last three months **16% of London's companies sought to recruit, a seven point decline on the previous quarter.** The majority of jobs being advertised were for full-time positions (61%). 55% of *Capital 500* firms recruited for part-time workers, a 19 point increase on the previous quarter.

**However, difficulties in recruiting became more pronounced for *Capital 500* businesses, with over half (52%) of companies experiencing problems hiring sufficiently skilled workers over the last quarter, a seven point increase from Q3 2014.** Skilled manual or technical staff positions remained the area where most difficulties were experienced, with 49% of recruiting London companies struggling to fill those roles, while professional or managerial job vacancies also remained a challenge for hiring firms (42% of recruiting companies reported difficulties compared to 48% the previous quarter).

Despite growing difficulties in recruiting workers, firms are not investing in training staff to the same level as they were in the previous quarter. **The balance figure for investment in training saw a six point decline to +3% in Q4 2014**, with only 11% of *Capital 500* businesses planning to increase their training budgets and 8% planning a reduction.

Encouraging businesses to employ apprentices would go some way to training young people with the skills that companies need to grow. LCCI welcomed the Chancellor's announcement in the Autumn Statement of abolishing National Insurance for apprentices up to 25 years of age, which would encourage more businesses to recruit and train apprentices. However, apprentices are only fully-funded between 16 to 18 years of age, while those aged 19-23 are only half-funded and those over 24 are no longer eligible for Government funding. This adds significantly to the cost of employing apprentices. The Government should consider reforms to the way that apprenticeships are funded for those over 19.

The Government must look to increase the level of funding given to apprentices between 19 and 23 years of age in order to encourage the take up of higher-level qualifications.

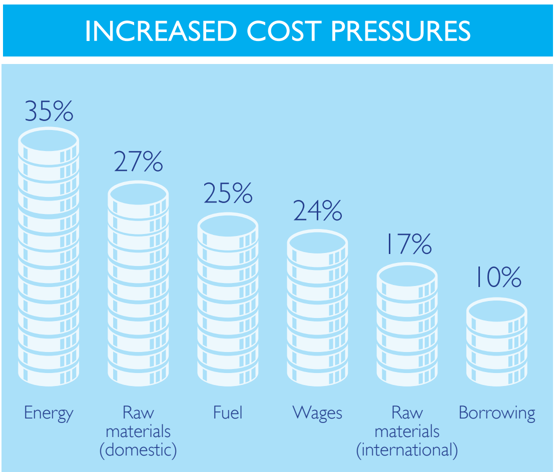
# CASHFLOW AND INVESTMENT


The final quarter of 2014 saw *Capital 500* businesses record strong gains in cashflow balances. While over half (55%) of *Capital 500* firms saw no change in their cashflow position in the last three months, **the overall cashflow balance figure increased by seven points from the previous quarter to +5%** (25% reported an increase and 20% a decrease). The changing level of cashflow balances over the last three quarters reinforces the case for maintaining low interest rates in order to provide businesses with a period of stable growth and build up cash reserves.

Despite the improving cashflow picture, business investment plans have deteriorated in the last quarter. **The Q4 2014 balance figure for investment in plant and equipment decreased by seven points to +3%**, with only 11% of *Capital 500* businesses reporting an increase, compared to 8% reporting a decrease.

The decline in capital investment figures correlates with recent Government data, which shows that business investment in the UK decreased by an estimated £0.3 billion in Q3 2014 compared to the previous quarter. However, the contribution of business investment to the economy is now £2.6 billion higher than its pre-downturn peak in Q2 2008 (ONS: *Business Investment, Q3 2014 Provisional Results*, November 2014).

# BUSINESS COSTS




**The cost of energy remains the biggest cost pressure on *Capital 500* businesses.** 35% of London companies reported an increase in energy costs over the last three months, a one point increase on the previous quarter. Oil price falls may provide some welcome relief.

The cost of materials sourced domestically was the second biggest cost pressure on businesses, with over a quarter (27%) of firms seeing a rise in domestic material prices over the last three months. The number of companies reporting fuel as their biggest cost pressure fell by six points to 25% in Q4 2014. This may be a result of recent price reductions on the cost of petrol and diesel.

**In terms of business concerns, competition remains London companies' major worry, with 40% of *Capital 500* businesses more concerned about competition than they were three months ago. Interest rates and inflation were businesses' joint second highest concern, with 22% more worried about them in Q4 2014.** In comparison to the previous quarter, the percentage of London firms concerned about interest rates has declined by 10 points, which may be a result of recent indications from the Bank of England that rates are unlikely to rise until the latter half of 2015 following a downgrade of inflation forecasts for the next year.

18% of *Capital 500* businesses were more concerned about business rates than they were three months ago in Q4 2014, a five point rise on the previous quarter. LCCI welcomed the extension of business rate relief announced in the Autumn Statement and the commitment to review the entire business rate system, an issue that we have long campaigned for. However, this review should not be postponed and its recommendations must be implemented at the end of the process.

**The commitment to overhaul the business rate system is welcome, but meaningful reform must follow that allows greater flexibility for rates to shift in line with changing economic conditions. The Government should also use the opportunity of reforming the business rate system to give London greater power over its finances.**

# BUSINESS CONFIDENCE

**BUSINESS CONFIDENCE**

**+25%**

↓ 2 POINTS

37% expect their company's prospects to improve over the next 12 months

Confidence figures for the next 12 months saw a slight drop in Q4 2014, but remain in firmly positive territory. **The balance figure for *Capital 500* businesses' expectation for their overall performance over the next 12 months decreased by two points to +25%, with 37% expecting an improvement and only 12% a deterioration.** Half (51%) expect their company's prospects to stay the same for 2015.

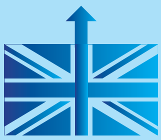
**Company performance indicators also remain positive for the next 12 months.** The balance figure for turnover expectations remained the same as the previous quarter at +25%, with 41% of *Capital 500* businesses anticipating increased turnover and 16% a decrease. The balance figure for profitability expectations fell marginally by four points to +19% in Q4 (36% predicted an increase and 17% a decrease).

These confidence figures support findings from other business surveys, with slight dips in confidence levels tempered by the fact that figures remain high by historical standards (ICAEW & Grant Thornton: *UK Business Confidence Monitor Q4 2014*).

# ECONOMIC OUTLOOK

**UK GROWTH**

**+29%**



↓ 7 POINTS

42% expect UK growth to improve over the next 12 months

The final three months of 2014 saw *Capital 500* businesses less confident about the UK's economic outlook than they were in the previous quarter. While 45% of London businesses expect the UK's economic growth rate to stay at the same level for the next 12 months, 42% anticipate the economy to grow faster and only 13% expect it to worsen, **leaving a balance figure of +29%. This is 7 points lower than the balance figure from the last quarter**.

This still though points to businesses having a positive overall view for the UK's economic prospects, as indicated by the high balance figure. It is mirrored in the latest forecasts for UK GDP in 2015, with the Office for Budget Responsibility (OBR) revising up its previous estimates for GDP growth by 0.1% to 2.4% in the Autumn Statement. However, the OBR has downgraded expectations for the later years underlining the fragile nature of the economic recovery. External market factors such as the weak eurozone economy and slowing global market conditions should alert the authorities to introducing any interest rate rises in a slow and gradual manner to prevent derailing continued growth for the year ahead. Targeted infrastructure investments would also help stimulate growth and reduce reliance on the household sector's spending to keep the economy growing.

On the other hand, London firms are more confident about the capital's economic prospects for 2015. **The balance figure for London's prospects for growth over the next 12 months is +39%, a two point increase on the previous quarter** (47% expected growth and only 8% a decline). With London expected to grow at a faster rate than the UK as a whole, greater freedom for the capital to invest in its own infrastructure would help stimulate growth across the economy.

> London should be given greater freedom to invest in its own infrastructure to cater for population and economic growth. The Government should look to lift restrictions on London's borrowing for capital investment and devolve property taxes to give London more scope to invest in infrastructure and drive further growth, which will benefit the UK as a whole.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