LONDON of CHAMBER
COMMERCE AND INDUSTRY

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QUARTERLY ECONOMIC SURVEY – QUARTER 2 2011

London economy experiencing sluggish recovery

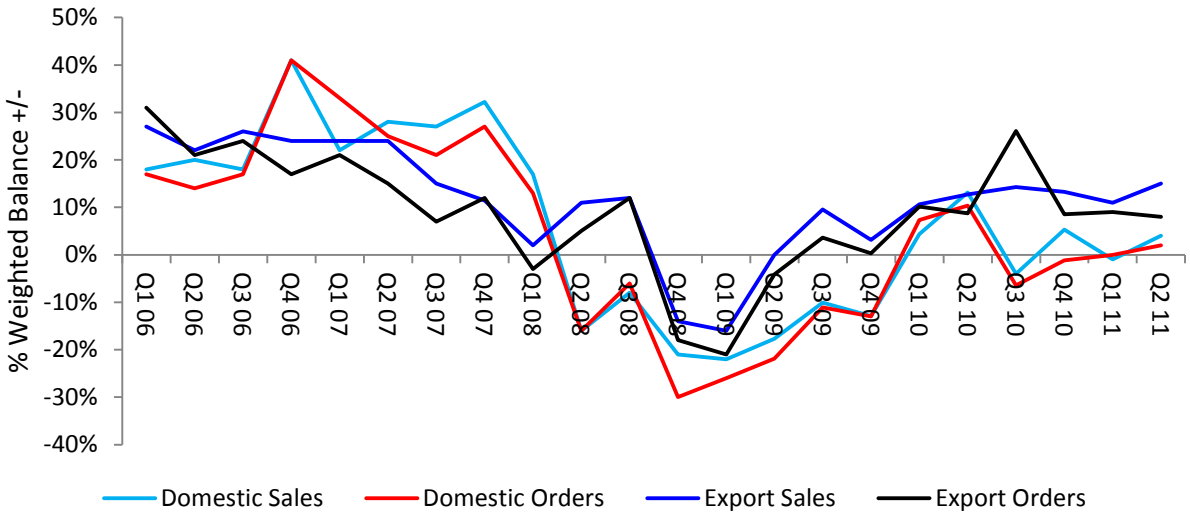
- **London's businesses only saw marginal improvement in sales and orders in Quarter 2 2011, suggesting that the recovery remains sluggish.**
- **Firms continue to perform better in export markets than in the domestic market, but hopes of an export-led recovery are still premature.**
- **Cashflow for businesses in London improved in Quarter 2 but remains a problem, with 33 per cent of companies reporting a fall compared to only 23 per cent that saw a rise.**
- **Despite these disappointing figures there has been a slight upturn in confidence, with 59 per cent of firms expecting their turnover to increase over the next 12 months (up three points on Quarter 1) and 48 per cent expecting their profitability to increase (up four points on Quarter 1).**
- **46 per cent of London businesses tried to recruit in Quarter 2 which is the highest this figure has been since Quarter 4 2007. Furthermore, there were significant increases in the number of firms that tried to recruit for full-time and permanent positions.**
- **However, of London's smallest companies (1-19 employees) only 30 per cent tried to recruit, 16 points below the average.**

Most of the key performance indicators for London's businesses have improved over the past three months, but none of them at a rate that can suggest the economic recovery is anything other than sluggish. This is according to the latest Quarterly Economic Survey (QES), conducted by **London Chamber of Commerce and Industry** (LCCI) in partnership with pollsters **ComRes**.

Sales and orders

For only the fourth time since Quarter 4 2007 the balances for both sales and orders in both domestic and export markets are positive (ie more businesses have seen a rise in sales and orders than have seen a fall). While this is a positive development, however, the improvements on the previous quarter are only marginal and should not be overstated (see Figure 1 below).

Figure 1. Excluding seasonality, how have the last three months compared to the previous three months in terms of:



Domestic market – The balance for domestic sales improved by five points in Quarter 2, from -1 per cent to +4 per cent. However, this can be explained by a five point increase in the number of businesses that reported their sales had stayed the same over the same period. That figure now stands at 50 per cent compared to only 27 per cent of businesses that saw an increase in sales, while 23 per cent saw a decrease.

Similarly for domestic orders, 50 per cent of firms did not see their level of orders change in Quarter 2, compared to only 26 per cent that saw a rise. Almost one quarter (24 per cent) saw their orders fall leaving a positive balance of +2 per cent, two points up on Quarter 1. To give a sense of perspective, the figures for domestic sales and orders in Q4 2007 (the last QES before the nationalisation of Northern Rock) stood at +32 per cent and +27 per cent respectively.

Export markets – Continuing the trend that has been seen throughout the economic downturn, firms continue to look towards export markets rather than the weak UK market. However, when compared to Quarter 1, the balance for export sales only rose by four points to +15 per cent, while the balance for export orders actually dropped by one point to +8 per cent.

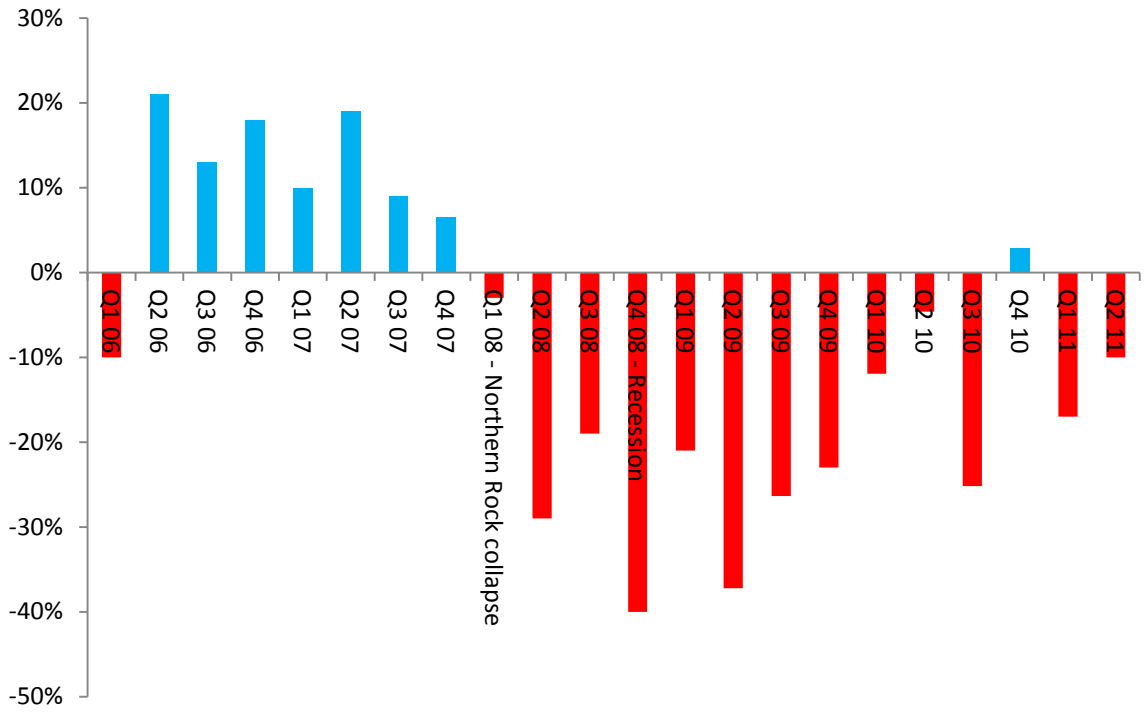
Taken together, these figures suggest that even though London's businesses did experience growth in sales and orders in Quarter 2, it was only marginal and still not near pre-recession levels. It is encouraging to see export markets outperform the UK market but it is still too premature to suggest this represents a rebalancing of the economy towards export-led growth. Ultimately, this serves to highlight the weak levels of demand in the UK economy. Unless there more is to incentivise businesses to export, it is likely that when the UK market begins to improve there will be a return back to domestic-led growth.

Cashflow concerns

The disappointing figures for sales and orders can be partly explained by the reduced number of working days in Quarter 2, due to the extra Bank Holidays given to the Royal Wedding. However, there are other pressures that businesses continue to face and cashflow is chief amongst them. Quarter 2 actually saw a seven point drop in the number of businesses reporting that their cashflow

had fallen (from 40 per cent to 33 per cent) but this can be explained by a corresponding seven point rise in the number of businesses reporting that their cashflow had stayed the same. This meant there was no change in the number of businesses reporting a rise in cashflow, remaining at 23 per cent. Therefore even though the overall balance rose by seven points it remains in negative territory at -10 per cent. The balance for cashflow has now only been in positive territory once (Quarter 4 2010) since the beginning of the economic downturn (see Figure 2 below).

Figure 2. Excluding seasonality, how have the last three months compared to the previous three months in terms of: Cashflow



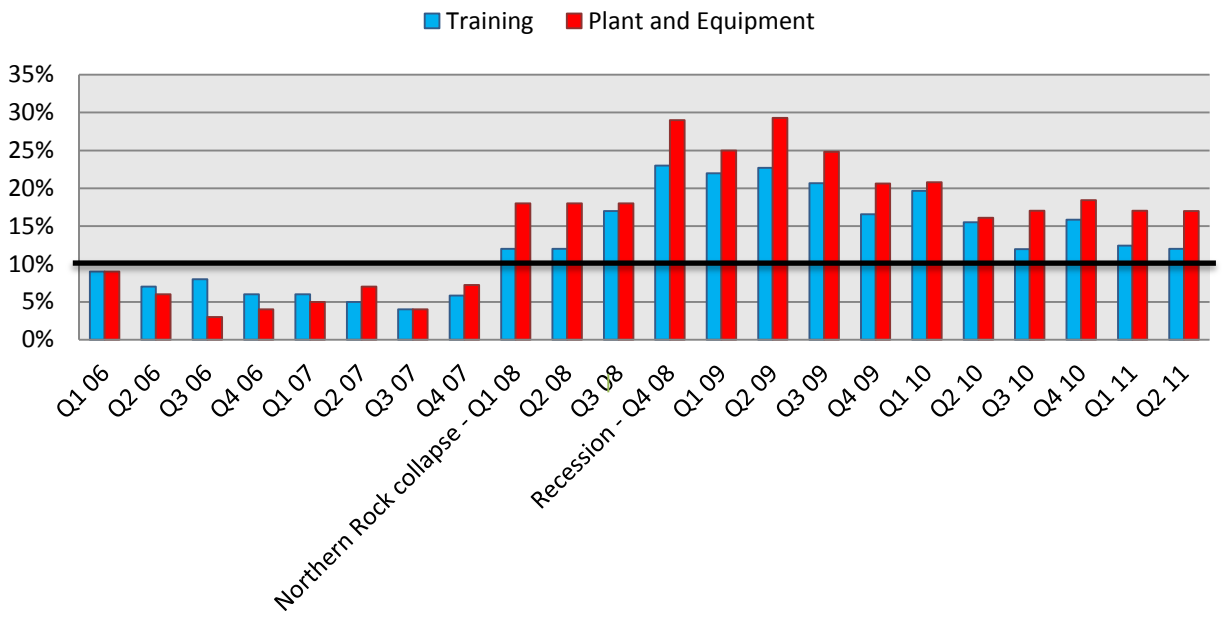
Lack of investment

Perhaps as a result of these consistently poor figures for cashflow, the vast majority of businesses in London are still unable to ramp up their investment plans. Some 85 per cent of firms saw their investment plans for training either stay the same or fall in Quarter 2 (73 per cent stayed the same and 12 per cent fell) compared with only 15 per cent that reported an increase. This final figure is actually three points down on the previous quarter. Similarly, investment plans in plant and equipment also remain below pre-recession levels with 81 per cent of firms reporting that their investment plans in this area either stayed the same or fell in Quarter 1 (64 per cent stayed the same and 17 per cent fell), compared with only 19 per cent that reported an increase.

Prior to the economic downturn the number of businesses reporting a decrease in their investment plans, in both training and plant and equipment, remained consistently in single digits. However, these figures now remain stubbornly in double digits (see Figure 3 below). When a business is underperforming the budget for investing in training or equipment is often seen as a discretionary cost and therefore more likely to be cut back. This suggests there are a minority of businesses that

are continuing to struggle, and are focussed more on survival than they are on growth and investment.

Figure 3. Percentage of businesses that have seen investment plans decrease



Recruitment and employment

More encouraging figures can be found when looking at recruitment and employment. In Quarter 2, 46 per cent of London's business tried to recruit, which represents an eight point increase on the previous quarter and is at its highest level since Quarter 4 2007 (when it was 55 per cent). Furthermore, there were promising increases in the number of firms recruiting for full-time and permanent positions, reversing a recent trend that had seen an increasing number of firms hiring for part-time and temporary positions. In Quarter 2 the number of firms recruiting for full-time positions rose by ten points to 85 per cent, while the number recruiting for part-time positions fell by nine points to 30 per cent. Similarly, the number of businesses recruiting for permanent positions rose by six points to 28 per cent, while the number recruiting for temporary positions fell by five points to 22 per cent.

Increased recruitment efforts represent good news for the coalition government as public sector job cuts begin to take effect. However, despite there being an eight point increase in the number of businesses that tried to recruit in Quarter 1 there was only a four point rise in the number of firms that saw their workforce actually increase over the last three months (from 18 to 22 per cent). This can be explained by the fact that Quarter 1 saw a ten point rise in the number of firms reporting that they met difficulties when recruiting (from 35 to 45 per cent). With unemployment relatively high it is a concern that businesses feel they cannot find suitable workers for the jobs they have available. With skills shortages now further exacerbated by the coalition government's decision to impose a cap on non-EU migrants this is a figure that must be monitored closely in the future.

Micro-businesses – The generally positive employment figures mask a more worrying trend within the smallest firms (1 to 19 employees). While 46 per cent of companies overall tried to recruit in Quarter 2, only 30 per cent of micro-businesses did. Of those that did try to recruit 48 per cent experienced difficulties, which is three points higher than the overall average. Furthermore, only 13

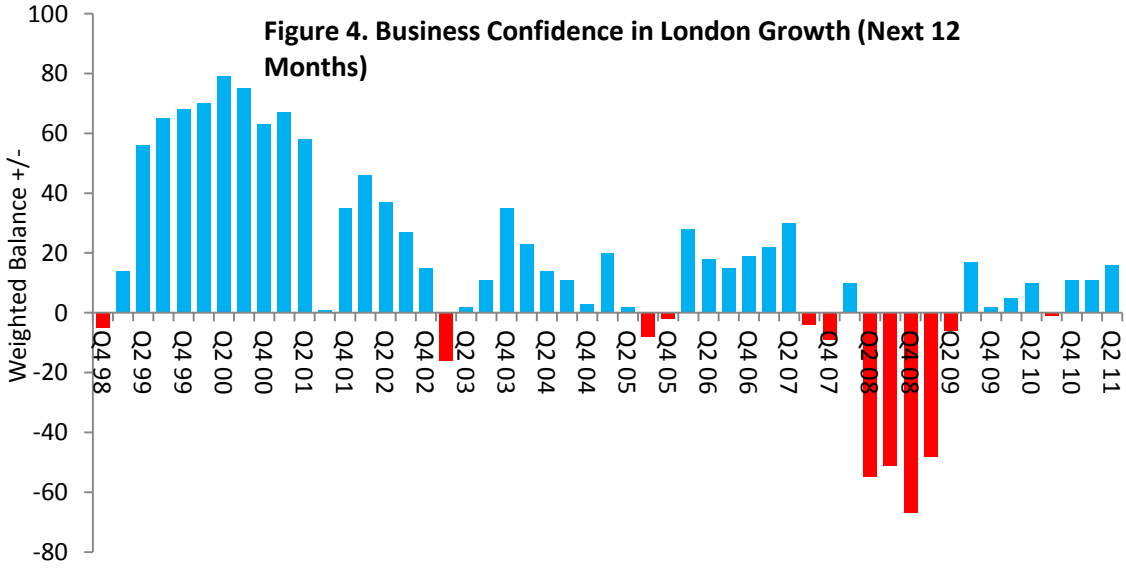
per cent of these companies saw their workforce increase over the last three months, nine points below the average.

Given the important role these small businesses play in the UK economy it is a real concern that they are not recruiting at the same level as other firms, and experiencing more difficulties when they do try to recruit. If the economy is to return to more positive levels of growth then it is these kinds of firms that need to grow into tomorrow's medium sized companies.

Confidence in the capital

On a positive note, Quarter 2 saw an upturn in all confidence indicators amongst London's firms. Looking ahead over the next 12 months, 59 per cent of London's firms now expect their turnover to increase, up three points on the previous quarter. Similarly, 48 per cent of companies expect their profitability to increase, which is a four point rise on Quarter 1. When asked to think about their company's prospects overall for the next 12 months, 47 per cent said they expected an improvement, up two points on the previous quarter.

Confidence in the capital's economy also grew in Quarter 2. One third of London's firms now expect the London economy to improve over the next 12 months, a one point improvement on Quarter 1. Those expecting the London economy to worsen fell by four points in Quarter 2 to 17 per cent, meaning the overall balance increased by five points to +16 per cent (see Figure 4 below).



Radical plans for growth

Overall, these figures are a disappointment. This time last year it would have been hoped that by now businesses would be experiencing much better trading conditions, and that growth levels would be moving more quickly towards pre-recession levels. This, however, is not the case.

Perhaps the most telling figures are those showing the difficulties London's smallest businesses are facing when trying to hire new staff. This should act as a reminder to the coalition government

that further efforts are needed to simplify and reduce the amount of regulations that employers face. It is exactly these types of micro-businesses that are affected disproportionately by regulation which, as the figures serve to highlight, acts as a disincentive for businesses to expand.

Commenting on these results, Peter Bishop, Deputy Chief Executive of LCCI, said:

“London’s businesses saw conditions improve during Quarter 2 but at a frankly disappointing and sluggish rate, with growth still way below pre-recession levels. There was admittedly a reduction in working days but that should not mask the difficulties many firms in the capital continue to face. The coalition government needs to be more radical in its plans for growth, by ensuring red tape is dramatically reduced and introducing more incentives to encourage firms to invest and expand their business.”

Quarterly Economic Survey – Q2 2011 Results Table

Quarterly Economic Survey Questions	Weighted Responses			Weighted Balances
	Increase	***No Change***	***Decrease***	***Balance***
Over the next twelve months, what do you think will happen to your profitability?	48 %	26 %	26 %	+ 22 %
	Increase	***No Change***	***Decrease***	***Balance***
Over the next twelve months, what do you think will happen to your turnover?	59 %	22 %	20 %	+ 39 %
	Improve	***Stay Same***	***Worsen***	***Balance***
What do you expect to happen to the following UK economic indicators over the next 12 months?				
Economic Growth	24 %	51 %	25 %	- 1 %
Inflation	6 %	24 %	70 %	- 64 %
Interest Rates	3 %	37 %	60 %	- 57 %
Unemployment	12 %	26 %	62 %	- 50 %
	Improve	***Stay Same***	***Worsen***	***Balance***
Over the next 12 months, what do you expect to happen to the economic prospects of…				
London	33 %	50 %	17 %	+ 16 %
Company	47 %	38 %	15 %	+ 32 %
	Improve	Stay Same	Worsen	Balance
How have your investment plans changed over the past three months?				
Plant and Equipment	19 %	64 %	17 %	+ 2 %
Training	15 %	73 %	12 %	+ 3 %

Quarterly Economic Survey Questions	Weighted Responses			Weighted Balances
	Up	***Same***	***Down***	***Balance***
Excluding seasonality, how have the last three months compared to the previous three months in terms of the following…				
Domestic Sales	27 %	50 %	23 %	+ 4 %
Domestic Orders	26 %	50 %	24 %	+ 2 %
Export Sales	33 %	48 %	18 %	+ 15 %
Export Orders	31 %	46 %	23 %	+ 8 %
Employment	22 %	63 %	15 %	+ 7 %
Cashflow	23 %	44 %	33 %	- 10 %

	Yes	***No***	***Balance***
Have you tried to recruit in the past three months	46 %	54 %	- 8%
	Part-time	***Full-time***	***Temporary***	***Permanent***
If yes, were the jobs	30 %	85 %	22 %	28 %
	Yes	***No***	***Balance***
Have you tried to recruit in the past three months	45 %	55 %	- 10 %

Notes

1. A total of 162 companies responded to the Quarterly Economic Survey – Quarter 2 2011.
2. All sectors of the London economy were represented including financial and business services (23 per cent); professions (20 per cent); manufacturing/transport/logistics (15 per cent); retail/wholesale (9 per cent); and other services (33 per cent).
3. Balances figures, referred to throughout this report, are determined by subtracting the percentage of companies reporting decreases in a factor from the percentage of companies reporting increases.
4. In terms of inflation, interest rates and unemployment, 'improve' = fall/ 'worsen' = rise
5. For a full set of the questions and results, please contact Iain Smith, Policy & Public Affairs Executive at ismith@londonchamber.co.uk.

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