New How: Perspectives

UK economic and sector outlook

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Contents

01

UK economic and sector outlook

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In this report, Kitty Ussher, a UK macroeconomist and former Treasury minister, shares her thoughts on the economic outlook for the UK.

As we move into a new phase of dealing with the pandemic, business leaders are seeking to understand what trading conditions will be like in the next few months and years. To what extent has the crisis accelerated existing trends, or has it completely changed the economic landscape?

Up to the end of 2019, the main topic of conversation among economists was our historically low levels of productivity. The British economy had felt sluggish since the financial crisis, with weak levels of capital investment, an over-reliance on lower-paid sectors of the economy and concerns that smaller companies – the so-called 'long tail of British industry' – were slow to adopt the new technologies and working practices that were needed to improve their performance and efficiency.

The political backdrop certainly didn't help things: uncertainty over the nature of a trading deal with the European Union hung a dark cloud over investment decisions for a full three and a half years from the referendum result in June 2016 until the parliamentary way was cleared following the general election of December 2019.

But there were also other factors at work that could, when viewed through a different lens, be interpreted as positive. In particular the labour market put in an extraordinarily strong performance in the decade before the pandemic, with employment consistently overshooting official forecasts. Some of this was due to a surge in self employment and microbusinesses facilitated by the growth in online trading; in addition new generations of well-educated workers were finding novel ways to remain economically active when their children were young that had eluded their parents. When combined with strong growth in lower-paid sectors such as care and retail, these forces had the perverse mathematical effect of actually bringing down productivity by lowering the average output per person even when more people were employed.

Despite the headlines there were other encouraging signs of economic resilience. The fastest growing occupations between 2011 and 2019 were programmers and software developers demonstrating that many employers were seeking efficiency gains from greater use of technology (box 1). This was followed by a swathe of core business services occupations including marketing, finance and HR, suggestive of a strongly competitive economy. The fastest growing lower skill occupations were concentrated in nursery and personal care, logistics and catering, which in turn points towards rising average disposable incomes leading to the professionalistion of activities that might have previously taken place within the home.

The 20 fastest growing occupations on the eve of the pandemic (2011-2019)

Source: Office of National Statistics

Technology

- Programmers and software development professionals (top)
- IT business analysts, architects and system designers
- Information technology and telecommunications directors

Business services

- Marketing and sales directors
- Marketing associate professionals
- Human resource managers and directors
- Customer service occupations (nec)

Finance

- Financial managers and directors
- Business and financial project management professionals
- Financial accounts managers

General management

- Production managers and directors in manufacturing
- Managers and proprietors in other services

Care

- Primary and nursery education teaching professionalsCare workers and home care
- Nursing auxiliaries and assistants
- Nurses
- Nursery nurses and assistants

Low skill

- Other administrative occupations
- Van drivers
- Kitchen and catering assistants

Box 1: The 20 fastest growing occupations on the eve of the pandemic (2011-2019)

Source: Office of National Statistics

Taking a sectoral view shows a similar picture. Figure 1 shows that the fastest growing mini sector of the economy in the decade before the crisis was the category of 'employment activities', which includes HR advisory, headhunters and job agencies, suggesting a deep and flexible labour market. This mini sector grew a massive 135% over the period 2009-19, way more than the 20% growth of the economy as a whole. Not far behind, however, were IT firms (98% growth) followed by core business activities such as office administration (88%), and accounting/auditing (63%).

It follows that the parts of the country with particular specialism in the growing sectors were themselves performing well in the run-up to the crisis. This includes London (ICT, professional services, retail), the East of England (science, tech, professional), West Midlands (civil engineering, manufacturing, ICT, retail), Edinburgh (finance, professional, tech, ICT, business support) and the West of England (wholesale, construction, professional services, property). Indeed, writing just before the onset of the pandemic, in February 2020, the EY Regional Economic Forecast predicted "London, the South East and the East of England will be the three fastest growing regions in England from 2020-23".

BACK TO CONTENTS

Which are the largest markets?

Largest markets: ONS high level sectors (2019)(relative change)

Very large sectors (around 10% of economy)
- Wholesale/retail/repair (growing)
- Manufacturing (declining)

Large sectors (5-8% of economy)
- Professional and technical activities (growing fast)
- ICT (growing fast)
- Admin/support (growing)
- Financial/insurance (declined since financial crisis)
- Construction (broadly flat)
- Human health & social work (flat)
- Education (declining)
- Public administration/defence (declining)

Mid players (3-4% of economy)
- Accommodation & food (flat pre-2020)
- Real estate (flat)
- Transport & storage (slow decline)

Smaller sectors (under 3% of economy)
- Other services (flat)
- Arts & recreation (flat)
- Water & waste (flat)
- Agriculture (flat)
- Households as employers (flat)
- Electricity & gas (declining)
- Mining & & quarrying (includes oil) (declining)

Which are the fastest growing markets?

Fastest growing mini sectors (2009-2019)	10 year real growth	% of 2019 economy
Employment activities	135%	1.62%
Computer programming, consultancy and related activities	98%	2.83%
Office administrative, office support, other business support	88%	1.24%
Rental and leasing activities	85%	1.17%
Accounting, bookkeeping and auditing; tax consultancy	63%	1.24%
Trade & repair of motor vehicles	63%	1.68%
Activities of head offices; management consultancies	49%	1.26%
Architectural and engineering activities; technical testing and analysis	43%	1.24%
Wholesale trade (excl motor)	37%	3.74%
Legal activities	35%	1.47%
Civil engineering	32%	1.24%
Buildings construction	32%	2.26%
Specialised construction	32%	2.97%
Buying and selling, renting and operating of own or leased real estate (excl imputed rent)	31%	3.58%
Human health activities	29%	5.14%
Whole economy	**20%**	

Figure 1

Source: ONS. KU analysis

Post-pandemic position

The question now is to what extent this picture has been changed – or accelerated – by the pandemic. Obviously any attempt to forecast our economic path is dependent on the path of the disease, but presuming that the effect of the vaccines is substantially to reduce the risk of future lockdowns, the current prognosis does not look nearly as bad as initially thought.

A year ago, the discussion was whether the path of the economy was going to be U-shaped or V-shaped. In reality, the story to date, as shown in Figure 2, is something closer to the type of U-bend you see under the kitchen sink: a steep fall followed by a partial rebound and then a flattening off. However, looking into the future there is much to be positive about.

Current forecasts, correct as of August 2021 and shown by the dotted line on Figure 2, anticipate the size of the economy in a few years time to be roughly where it would have been if the previous trends were continued: if you extend the broad upward trend that has been in evidence since 2010, it joins the forecast line in early 2023.

This is in stark contrast to the 2008-09 recession which resulted in a permanent downward shift in our productive capacity, a phenomenon the economists refer to as 'scarring'. While of course for many individuals, firms and families the pandemic has been very difficult, both financially and otherwise, for the economy as a whole there is some indication it may not be as bad in the long term as was initially feared.

Real GDP Jan 2007 - June 2021 with forecast

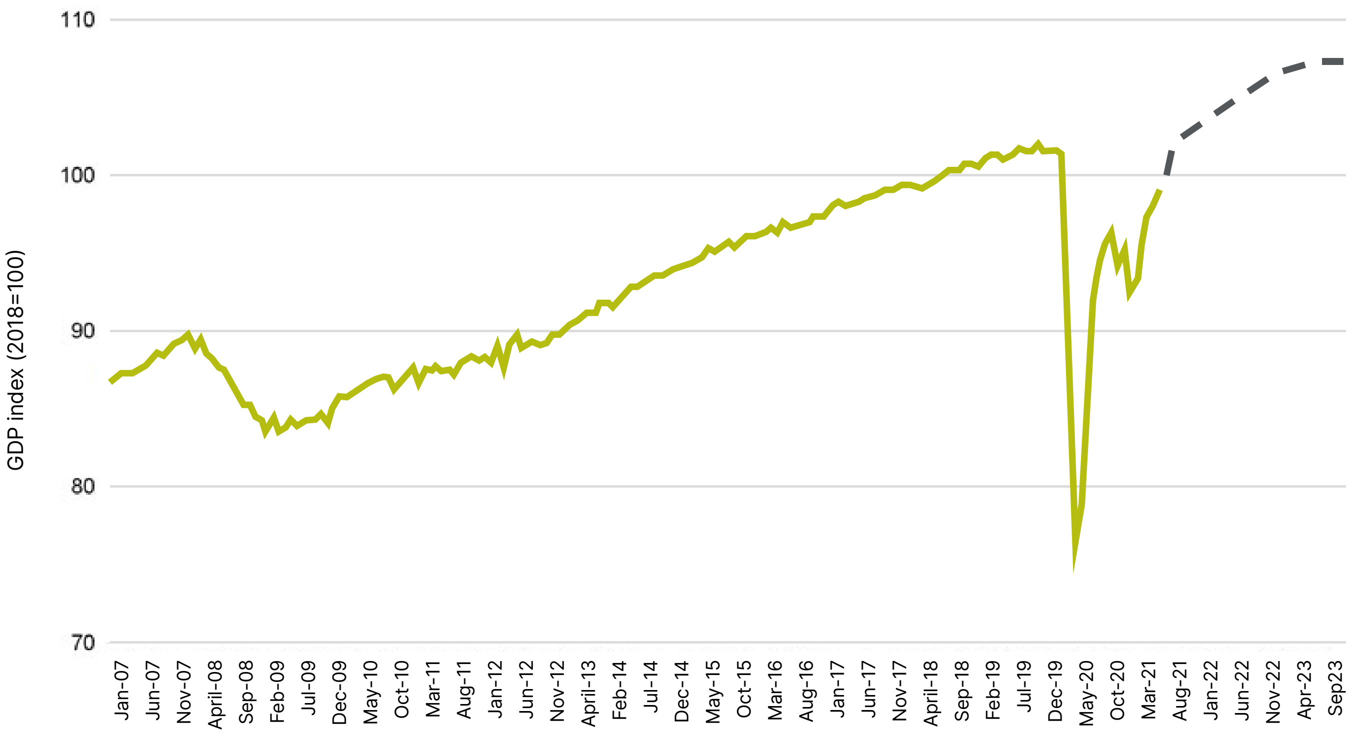

Figure 2

Source: ONS. Latest datapoint is June 2021, published 12 August 2021. Bank of England forecast (August 2021)

The reason for this is found in the amount of money people have to spend. Whereas in 2008-09 the 'credit crunch' led people to feel they were overextended and needed to spend less, we are now seeing the opposite effect with many households finding they have accumulated savings during the pandemic and see no reason why they shouldn't be run down. Household spending on home improvements, large purchases, moving house and staycations all lead to large multiplier effects in the local economy.

Combine that with the removal of Brexit uncertainty (it's now a business-as-usual reality) plus a huge increase in government spending, generous tax incentives for business investment, low interest rates and a step-change in the rate of digitisation, and we have the ideal conditions for a period of strong economic growth.

For much of this year, the fear among policymakers has been that unemployment would rise sharply when the furlough scheme comes to an end. As a result, the priority has been to run the economy fast now, even if that led to some short-term inflation, to put us in the best possible position to absorb the rise in unemployment come the autumn.

Over the summer, however, evidence has started to emerge that this fear is overstated and that, in fact, unemployment may already have peaked (Figure 3).

Unemployment rate Jan 2007 - June 2021

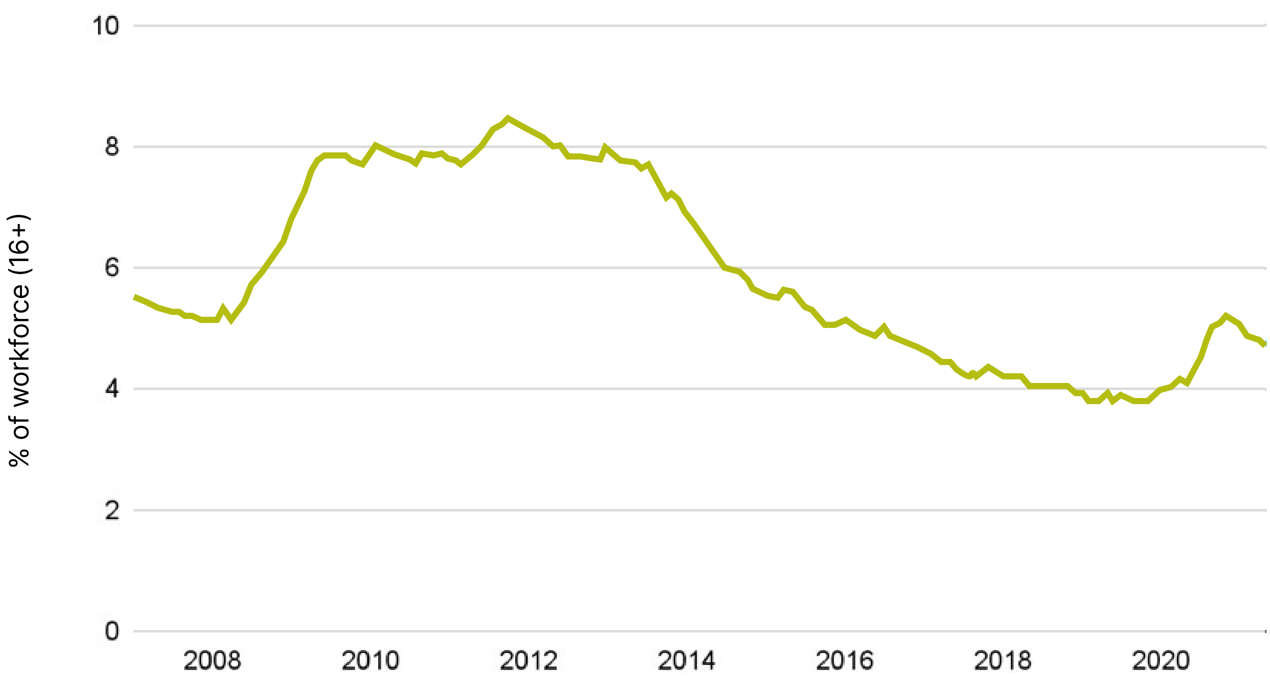

Figure 3

Source: ONS Labour Force Survey. Latest data June 2021, published 17 Aug 2021

Key to understanding what is happening is to consider the difference between the number of jobs that are furloughed, and the actual experience of the people in question. In particular, it is not necessarily the case that a person who has been furloughed is inactive. Some people working in leisure and hospitality when the pandemic hit will have left the UK, so no longer show up in the data; others may have found alternative work elsewhere in the meantime.

In fact, the latest survey evidence from the ONS Labour Force Survey suggests that the number of people temporarily away from their job, which includes those on furlough, is not far off its long-run pre-pandemic level (Figure 4). If true, this suggests that the final end of the furlough scheme will not lead to any significant rise in unemployment. In fact, even by August 2021, the number of job market vacancies was above its pre-pandemic level, suggesting no lack of opportunity.

Employees temporarily away from work ('000s)

Figure 4

Source: ONS Labour Force Survey. Latest data end-June 2021, published 17 August 2021

Add in the fact that Brexit has made the UK a less attractive destination for migrant workers and we may find that the economy hits capacity constraints sooner than previously expected. Policy-makers will not want to take any risks until the full economic effect is understood but once that is clear – likely in the autumn – then expect a strong signal from the Bank of England that it will be prepared to take action to reduce expectations of future inflation rises. This will start by phasing out bond purchases and then by starting to nudge interest rates up again. However with rates having been reduced to a record low of 0.1% when the pandemic hit, it will take a while before they are anything like the 3-5% range that felt like normal before the financial crisis took hold.

Looking to the future, there is every indication that economists in the next decade will not be as worried about low productivity as they were in the past. The step-change in digitisation will lead to greater efficiency in parts of the economy that were previously slow to adapt and a tight labour market only adds to the incentives to invest in technology and capital. For those firms that didn't make it through – difficult though it has been for the individuals concerned – the theory of creative destruction suggests that their exit will enable economy-wide resources to be deployed more efficiently and raise the performance of the average. For the rest, change brings opportunity: witness the rapid rise in share prices of small-cap firms and M&A activity.

At the same time the great working from home experiment will place a greater emphasis on output over presenteeism (like it or not) and a cultural acceptance of location-flexible work means parents of young children will find it easier to work to their full potential, contributing more to their employers and the economy alike. All of this is music to the ears of the HR advisory and employment sectors which, as we have seen, have already had a very strong decade.

A hundred years ago, as we emerged from the first world war and an earlier pandemic, the economy was described as roaring. While I wouldn't go as far as to invoke a lion metaphor this time round, there is some hope that the serene economic duck of the previous decade might make more of a splash in the years to come.

> "The final end of the furlough scheme will not lead to any significant rise in unemployment."

02

Living for the future

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Living for the future

The last eighteen months could have been cataclysmic for the living sector. With the pandemic having caused construction site closures, supply chain issues, price increases of materials, economic nervousness and, more recently, labour shortages from the 'pingdemic', the outlook at times has looked pretty bleak for the sector. But performance since mid-2020 has been nothing short of remarkable. Government interventions have certainly helped, but the market has proved itself creative and resilient in the face of significant adversity, paving the way for a resurgence in buyer confidence and corporate investment. But what now? Will the market continue to perform or are there pitfalls of which to be wary? In this article, we look at some of the trends in the market and the factors which may influence future change.

SDLT here to stay

Putting aside the debatable benefits of SDLT and the argument that abolition would result in a more free-flowing market, it is difficult to say that the SDLT holiday didn't mobilise buyers and sellers and provide the sector with a welcome economic boost (an additional 140,000 transactions were estimated to have been generated by the holiday alone, with the average additional expenditure on each as high as £16,000, resulting in between £1.8-£2.7 billion for the wider economy.[1]). Whilst an increase in house prices has been a partial consequence, the "experiment" has arguably strengthened the case to scrap the tax for good, with socio-economic benefits of downsizing, social mobility, wellbeing and levelling up a conspicuous side effect. That said, any change would likely need to be tackled as part of a much broader tax reform exercise and, with SDLT bringing £12 billion into the Treasury each year and Rishi Sunak so far resisting the clamour, it's fair to say that SDLT reform in the short term at least looks unlikely.

So, with SDLT to go back to normal from October once the tapering off period ends, should we expect to see a hit on transactions? And heading into winter with the threat of Covid enduring, the next six months will continue to present challenges for the housebuilding sector. However, as we've seen before, the underlying strength of the sector and the creativity of those who work within it suggests a more positive outlook for 2022.

A perfect storm for the supply chain

We have seen huge disruption to the construction industry as a result of supply shortages, as well as price increases, particularly in products sourced from Europe and the Far East. There are of course some obvious reasons for this around Brexit and Covid, bringing about a perfect storm of factors that has led to the low supply, high demand and the high costs that we are seeing. Add in increasingly congested shipping routes, a shortage of HGV/LGV drivers and the enduring effects of the pandemic on the global shipping industry, and it's fair to say that the industry is having a challenging time.

These difficult market conditions are expected to remain until at least the end of the year and, with strong demand for home improvements and new housing, the uncertainty of supply will likely result in further price increases. The larger housebuilders may well be able to accommodate these impacts into their new schemes, but smaller developers more reliant on cash flow and tied into pre-existing and inflexible contract terms may well struggle. Careful scrutiny of the volatility clauses in supply contracts and the levels of risk that are attached in terms of time and cost obligations will be more important than ever. Going forward, more flexibility may well be needed throughout the supply chain to ensure these issues doesn't escalate into an even bigger systemic problem.

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Whilst an increase in house prices has been a partial consequence, the "experiment" has arguably strengthened the case to scrap the tax for good, with socio-economic benefits of downsizing, social mobility, wellbeing and levelling up a conspicuous side effect."

[1] Lessons from the Stamp Duty Holiday – LSE & Family Building Society, July 2021 – https://www.lse.ac.uk/geography-and-environment/research/lse-london/documents/Reports/Lessons-from-stamp-duty-holiday-LSE-London-Report-2021.pdf

BTR on the up

With plenty of talk of high yield, low-risk and increasing local authority support, BTR has been attracting investor interest for a few years now. And rather than bursting BTR's balloon, the pandemic has served only to enhance its allure, with CBRE data showing £1.5bn worth of deals were transacted in H1 2021 alone, up 30% on H1 2020, itself a record-breaking year with £3.5bn of BTR investment deals completed in the full 12 months. With over 36,000 BTR units currently in the pipeline (according to Ascend Properties), the market certainly doesn't look to be slowing down. And what is more, with two-thirds of proposed schemes located outside of London, the regions are now beginning to come to the party, recognising BTR as a way to increase housing choice for their communities and boost their local economies.

Which begs the question, are we in the midst of a societal shift in mindset when it comes to home ownership? With the cost of buying a house increasingly prohibitive and the lifestyle benefits offered by BTR accommodation (resident lounges, co-working spaces, gyms, cinemas, roof gardens etc), you can understand the appeal, and not just for millennials. Certainly, the amount of capital being deployed across the sector suggests that buying a home is not necessarily the priority for a growing number of individuals that it was a generation ago. Throw in the emergence of BTR single-family housing and the question is perhaps less about a societal shift in mindset and actually more about whether we have reached a point at which home ownership is now so out of reach for twentysomethings as to be unachievable. Or it may be that demand always existed but, until the boom in BTR, was just underserved. Regardless, with all metrics pointing upwards, the future of BTR is hot.

The urbanisation of later living

"Specialist retirement properties create more local economic value and more local jobs than any other type of residential housing." As a statement endorsing the importance of the grey pound to our future town and city centres, this one from Homes for Later Living's 'Silver Saviours for the High Street' report[2] takes some beating. Yes, we have a moral obligation to look after the elderly and provide them with high quality living accommodation and a sense of community, but it is becoming increasingly clear that doing so also makes sound financial sense. With the over-65s expected to account for almost 25% of the UK population by 2039 and perennial issues around high demand and low supply, the later living sector is proving itself an attractive asset class for investors.

However, rather than locating retirement homes in leafy suburban or rural areas, as has largely been the case for decades, there is a growing argument that we need to bring our retirees more into our central town and city sites, close to shops, restaurants and amenities, as well as transport hubs. Our town and city economies would certainly benefit from this demographic's extra spending ability. With a record number of retail units having closed in the last year and with the switch to hybrid home/office working likely to reduce footfall in our centres, a blend of residential will be necessary to ensure our urban areas avoid neglect and ruin. In supporting the urbanisation of this sector, not only will we be able to address the lack of available retirement housing, we will be able to bring about a more effective use of brownfield sites, a reduction in greenfield development, the worthwhile repurposing of empty retail units and a new target market for local retail and leisure businesses. A true virtuous circle.

[2] Homes for Later Living – 'Silver Saviours for the High Street', February 2021 – https://www.housinglin.org.uk/_assets/Resources/Housing/OtherOrganisation/Report_SilverSavioursHighStreet.pdf

03

Financial Services – can we permit ourselves to be optimistic?

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Financial Services – can we permit ourselves to be optimistic?

When can I go back to the office? When will schools open? Can I see my family? When will I be able to travel? The outbreak of Covid-19 made us all feel that uncertainty was the only certain. The impact of so much ambiguity was felt across all parts of the world and sectors of the economy.

Now with record low interest rates; massive levels of government stimulus spending; tax incentives for business investment; an increase in consumer spending and confidence; the removal of significant Brexit uncertainty and a housing market boom, the conditions for continued, strong, economic growth appear ideal. With so many positive economic factors coming together, combined with the hope induced by the vaccine roll out, can we permit ourselves to be optimistic about the economy and our future? Will anything get in our way?

Inflation

With the economy recovering from the pandemic at such a swift pace, inflation is consequently rising along with it. Inflation is forecast to hit 4% this year, 2% above the monetary policy committee's (MPC) target of 2%. Why is this happening and what does it mean for our medium to long term outlook?

The Bank of England stated in its latest monetary policy report, "CPI inflation has risen markedly to above the monetary policy committee's target of 2% and is projected to rise temporarily to 4% in the near term. The rise largely reflects the impact of the pandemic as the economy recovers. This has led to higher energy and goods prices, which in turn reflect rising commodity prices, transportation bottlenecks, constraints on production and strong global demand for goods".

The Bank of England however believes that the forecast inflationary rise is only temporary. As the economy recovers from the pandemic, commodity prices will begin to stabilise, supply shortages will ease, and global demand will rebalance. Overall, a very good outlook in relation to growth and inflation.

Historically however, when faced with such a spike in inflation, the implementation of an interest rate rise has been the Bank's weapon of choice. Should we prepare ourselves for a rise in interest rates?

Interest rates

The Bank of England has hinted that there may be a modest increase in interest rates to help keep rising prices under control.

"If there is no other major wave of Covid19 during the winter and the economy performs in line with the Bank's forecasts, the first rate rise is likely to come in the spring or early summer of next year," said Ian Stewart, chief economist at Deloitte. However, with uncertainty linked to the Delta variant other observers note that policymakers are wary of the impact of any tightening to monetary policy and believe a rate rise will be delayed until 2023.

With interest rates having remained at a low rate for such a long period, it is hard to envisage a near future without an interest rate rise. When this will happen is uncertain, but this is something we need to be prepared for.

> "With uncertainty linked to the Delta variant other observers note that policymakers are wary of the impact of any tightening to monetary policy and believe a rate rise will be delayed until 2023."

Public Debt

Rising interest rates heighten concerns regarding public debt. Government debt has increased significantly throughout the pandemic and the cost of debt servicing is an element that will be affected if the interest rate rises faster than predicted. Two important factors are working in the favour of optimism in this regard: the recovering economy, and the Corporation Tax increase.

The Government has implemented measures to prevent a future 'spooking' of the financial markets by announcing a Corporation Tax increase effective from April 2023. The driving force behind the delay in implementation is to encourage business growth now, and the future income from the tax increase will assist in bringing public debt down to a level considered acceptable in the eyes of forecasters.

When looking at inflation, interest rates and debt collectively, these pieces of the economic puzzle appear to be working well together, balancing each other out, playing their part in what looks to be a very positive economic future.

> The driving force behind the delay in implementation is to encourage business growth now."

Environmental, Social and Governance (ESG) Strategies – increased scrutiny

Another area weighing heavily on the side of optimism – the seemingly unstoppable trend for ESG investment. Now, in more businesses than ever before, it is a driving force on the Board agenda, and they are adapting to incorporate it into their strategies.

Greater focus on the environment, emphasis on people and our society, and the importance of the corporate controls that govern these practices – these themes themselves induce an ethical optimism in us all. However, as the past has taught us, new ideas and investments, focusing on the greater good, have sometimes been driven by less than ethical motives.

In this regard, there has been a recent increase in concerns regarding potential "Greenwashing" in the ESG market. Greenwashing is when consumers are provided with overly optimistic claims in relation to an ESG investment. In some cases, investors have been led to believe that a company's products are environmentally friendly, when in fact, there may be no certain proof that they are. Cases such as these can cause distrust in the ESG market and leave investors feeling disillusioned.

In a positive move, the FCA have voiced their concern around the lack of control and have outlined a strategy to 'promote integrity' in the sustainable investing market.

The FCA's technical specialist on sustainable finance and stewardship, Mark Manning, said the regulator's focus is on 'development and the integrity' of the ESG market, including ratings and qualifications. "If the market is to grow and develop, and is to maintain integrity, consumers have to be able to trust the products they're offered and rely on them to perform as they expect. We need to ensure that our regulatory framework can help to achieve this", he said. "Through our authorisations process, we continue to exercise important challenges to firms as they bring products to us for authorisation. We have also carried out consumer behaviour research. In such a fast-moving space, it's important to strike the right balance between principles and prescription."

We can therefore look forward to greater scrutiny of the ESG market by the FCA, raising consumer confidence, encouraging investment in an ethical area that will benefit the greater good. Another reason to be optimistic about the future.

> Greenwashing is when consumers are provided with overly optimistic claims in relation to an ESG investment."

Conclusion

Prior to the pandemic, the British economy had felt sluggish. The financial crisis had caused a scar and the recent uncertainty surrounding trading deals with the EU post Brexit put the brakes on many investment decisions. Now we are seeing the economy grow at a rate we have not seen since 1941. Historically the caution raised in relation to inflation, interest rates and debt would be warranted. Now however, considering the lasting impact of the financial crisis, Brexit and the pandemic, this growth could be viewed as the economy finally catching up, regaining its position, a place it may have been in, if these three, large disruptors, had not occurred.

With the added emphasis and controls around ethical investing, the future is looking bright.

We can permit ourselves to be optimistic.

04

Mobility – the journey ahead

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Mobility – the journey ahead

The coronavirus pandemic sent shockwaves around the global economy, and continues to pose unprecedented challenges for international trade, supply chains and businesses of all sizes – the mobility sector impacted within each of these arenas. In such unprecedented times, global mobility is evolving – bringing with it exciting opportunity. Changing consumer habits, the continuing digital revolution, evolving climate change targets, and supply chain disruption are all paving the way for the most rapid advances seen in decades.

Customer confidence within the automotive industry

The pandemic has caused a fundamental shift in the way all sectors operate and serve consumers. The automotive sector is no exception to that. The global pandemic has turned every day commuting on its head, raising difficult questions about customer demand. A reduction in commuter travel, the anticipation of more home working, changes to the urban layout of our towns and city centres, and a shift to localism have all changed the need for cars and how they are used.

The long term consumer response to the pandemic and impact on the new and used car markets remains uncertain. On one hand, demand levels are expected to be low given the broader weak economic setting, low consumer and business confidence and anticipated rise in inflation. On the other, findings have shown that the UK adult population largely expects to choose to travel as they did before the pandemic, with the second-hand car market soaring in 2021. The rise in prices of second-hand cars was attributed as the main driver of UK inflation in July, the average used car price increasing 15.2 per cent year on year according to Auto Trader.

However, a widening deficit on new car production has slowed growth, with car manufacturing labelled as suffering from "long COVID". In August, new car registrations fell -22% in its weakest performance since 2013. The microchip shortage remains the biggest medium-term issue for the automotive industry, with some of the largest manufacturers having to slow or temporarily halt production. As such, there have been calls for the UK government to support automotive businesses to restart UK manufacturing, incentivise consumer demand and in turn aid economic recovery. Longer-term support should allow the automotive sector to maintain its pre-Covid-19 international competitiveness both within the EU and globally.

Moving on up – emerging technologies

A growing pressure remains on mobility sector companies to take bold, transformative action to remain relevant. Autonomy will make road vehicles smarter, create opportunities for new services such as last-mile delivery by drone and deliver fully autonomous urban transport. EY has explored solutions to the transportation industry's ongoing driver shortage, highlighting a need to advance the technologies within this field. Start-ups are building out prototype fleets and hauling freight for big shippers that hope autonomous trucks could help cut transportation costs and speed up deliveries. Companies with self-driving trucking technology are working to plug into existing operations, striking agreements with truck makers and large trucking fleets that they believe could eventually buy thousands of autonomous trucks. The UK government predicts that connected and autonomous vehicle technology could create around 38,000 new jobs in a UK industry that could be worth £42 billion by 2035. Over 80% of these jobs are expected to be in professional, technical and skilled trade occupations.

As for the skies above, a handful of well-funded start-ups have carried out test flights of electric vertical take-off and landing (eVTOL) aircraft. Piloted air taxi and shuttle services are expected before 2025, with Uber planning to operate aircraft without pilots by around 2030. Earlier this year, American Airlines, Virgin Atlantic and Rolls Royce made preliminary commitments to buy up to 1,000 electric air taxis from a British start-up, Vertical Aerospace, in the biggest sign of a radical shift to urban air mobility. Although the industry still faces significant challenges; including gaining public acceptance, building the necessary infrastructure and meeting regulatory demands - airborne mobility solutions will likely become a reality over the next decade, for both cargo and consumers.

[1] Retail Price Index | August 2021 - News hub - Press centre – Auto Trader Group plc
[2] SMMT VEHICLE DATA August 2021 UK new car registration data, UK car market – SMMT
[3] Why EV fleet transition is essential for transport decarbonisation Why EV fleet transition is essential for transport decarbonisation | EY UK
[4] Government paves the way for self-driving vehicles on UK roads Government paves the way for self-driving vehicles on UK roads – GOV.UK (www.gov.uk)

BACK TO CONTENTS

Greater emphasis on environmental, social and governance efforts

The pandemic has presented an opportunity for many people to reflect on what really matters to them. The same applies to businesses, with many having recently renewed their focus on environmental, social and governance (ESG) performance. Companies that realign themselves to investor agendas and prioritize long-term value creation through ESG frameworks may well have a competitive advantage in the coming years. With that in mind, mobility industry leaders are expected to be more vocal in the practices and values they expect of themselves and their future partners.

ESG concerns are becoming a standard part of deal discussions and are factored into strategy and valuations. Specific areas of focus for the automotive industry (in particular, in manufacturing) include energy use, production process innovations, EV battery and service options, supply chain resilience, health and safety, cultural issues, and diversity and inclusion.

While we are seeing rapid technological developments and a significant increase in investment in transport tech, there is also a ‘back to basics’ theme driven by ESG considerations. In April this year the Department for Transport launched its “Gear Change” initiative[5], with plans to accelerate active travel to make the UK a great walking and cycling nation. Efforts are to include creating better paths for cyclists and pedestrians, putting cycling and walking at the heart of transport decision-making, empowering and encouraging local authorities and enabling people to cycle and protecting them when they do.

Green is for go - the development of green fuels for use across all forms of transport

Climate change remains the most pressing economic and environmental challenge globally. The COVID-19 pandemic, rather than distracting from the need to drive a sustainable future, has reinforced that imperative. Alternative fuels like electricity, biofuels, and non-polluting energy sources, notably hydrogen, are all pathways towards a more sustainable mobility. PWC has predicted that by 2050, renewables will account for more than 90% of energy[6], and fossil fuels will account for less than 10%. The COP26 summit in November is only going to drive this conversation forward; countries being asked to come forward with ambitious 2030 emissions reductions targets that align with reaching net zero by the middle of the century.

It is understood that 30% of all CO2 emissions come from heavy duty vehicles[7], showing the crucial significance in the reduction of overall emissions produced by fleets. This has led to suggestions for the use of hydrogen and biofuel mixes – alongside a need for awareness, communication and education in order to accelerate fleet and truck transition across to EV and other zero emission solutions.

[5]Cycling and walking plan for England Cycling and walking plan for England – GOV.UK (www.gov.uk)
[6]Inventing tomorrow’s energy system: The road ahead for molecules and electrons Inventing tomorrows energy system: PwC
[7]CO2 emission performance standards for new heavy-duty vehicles CO2 emission performance standards for new heavy-duty vehicles – GOV.UK (www.gov.uk)

05

Totally wired – technology sector zooms forward

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Totally wired – technology sector zooms forward

While the COVID-19 pandemic has been catastrophic for some markets, the technology sector has largely remained resilient. The pandemic may even be regarded as a catalyst for change, with many organisations forced to accelerate their digital transformation efforts and remote operations creating an opportunity for new solutions to be developed. Combined with the strong underlying ecosystem that has established over the last decade, the outlook for the technology sector remains extremely positive.

Resilience of the technology sector

The technology sector showed remarkable resilience in light of the global pandemic, lockdown restrictions creating a real dependency from businesses and society on technology. Significant numbers of consumers moved to conducting their business online, with industries responding in turn. Key sectors reporting technology increases included pharmaceutical, financial and professional services. By way of example, 'Baby Boomers' who had previously shunned on-line banking tried it for the first time during the pandemic. Digital transformation that would typically take years was accelerated to a period of weeks according to findings from McKinsey[1]. Research highlighted that the pandemic speeded the adoption of digital technologies forward by an average of three to four years.

A shift in dependency on technology allowed consumers to be more connected than ever, tech firms praised as a force for good. From ordering groceries to "contact free" medical supplies, virtual visiting solutions for families with loved ones in intensive cares to iPads in care homes to tackle loneliness -technology firms have stepped up to help in the last 18 months.

> "Technology allowed consumers to be more connected than ever, tech firms praised as a force for good."

Which companies are most attractive to investors?

The last 12 months has seen a significant increase in "megadeals" (where £50 million or more has been invested into UK companies), as highlighted in recent research from Shoosmiths in partnership with intuitive data platform Beauhurst (you can access the report here). Where megadeals are concerned, it is technology companies who are the primary beneficiaries, particularly financial technology (fintech) companies that are both consumer and business -to-business oriented. Some of the largest deals in the last 18 months have involved fintechs including Revolut, KI Insurance, Checkout.com and Go Cardless. This, together with the recent London Stock Exchange listing of Wise, reflects the strength of the UK fintech market and investor confidence in London as a global financial centre and gateway to the European market post-Brexit. Buy now pay later (BNPL) models continue to receive interest, with Amazon and Apple both revealing plans for customers to split purchases – leading to calls for banks seeking long term growth to explore BNPL market entry.

Unsurprisingly, health tech is also attracting investment, COVID-19 triggering a reliance on virtual care delivery, an increased focus on mental health and well-being and a push for quicker drug and vaccine discoveries. Health tech innovators were critical to this response, specifically with products and solutions that address well-being and care delivery – all likely to continue receiving investor interest for the rest of 2021 and beyond.

With the government's ambitious Net Zero commitments and Glasgow hosting COP26 in November, transport tech and energy tech are key focus areas too. The good news for the preponderance of tech start up and scale ups looking to expand nationally or globally is that alongside government-backed schemes such as the Future Fund, there is a previously unprecedented amount of money being invested in private UK companies.

We are also seeing increasing interest in online retailers. In recent years there has been a wave of entrepreneurs establishing an online business when they have spotted a gap in the market for a product. These online businesses are now ripe for acquisition with investors scouring the market place for the upcoming consumer brands. As part of this new trend, acquisitions are made, the companies' new owners inject working capital to grow sales and run them alongside other acquisitions, thereby negotiating savings with suppliers and cutting administration and marketing costs.

[1]McKinsey How COVID-19 has pushed companies over the technology tipping point—and transformed business forever COVID-19 digital transformation & technology | McKinsey

BACK TO CONTENTS

Overseas investment in the UK

With the UK technology sector continuing to beat both the US and China on global growth, overseas confidence in investment in the UK tech is soaring. Boasting a long-standing reputation for innovation, the UK provides an attractive opportunity for overseas funds looking to grow their investments within the tech market. UK unicorns have stampeded, hitting a milestone of 105 $1 billion tech companies in September 2021, more than the rest of Europe combined.[2]

Collectively, the UK's 100 tech unicorns have raised almost £23 billion in venture capital (VC) investment[3], across multiple tech sub-sectors, including e-commerce, insurtech, and cyber security and energy. Household names achiving unicorn status include car marketplace Cazoo, online events platform Hopin, sports clothing company Gymshark, meal-kit manufacturer Gousto, zero emission electric public transportation vehicle creator Arrival and utility supplier Octopus Energy.

Levelling up agenda

The vast majority of the UK's tech unicorns are based in London, and as our recent report highlights the majority of companies that have raised money by way of megadeals are located in London and the South East. While the capital will always be regarded as an epicentre for access to finance, talent and customers, it is important that VC investment in the UK is accessible across all regions.

University spin outs are pushing against the capital's dominance - with a combined 20 potential "futurecorns" identified in Cambridgeshire and Oxfordshire. A further five potential futurecorns have been identified in the North West[4], along with five high scaling companies in Scotland. These are all positive signs that investment is reaching the right companies no matter where geographically located, but to maintain the UK's leading position in the European market, perhaps more action needs to be taken to raise awareness of investment opportunities across all regions. It is crucial that all scaling businesses have the necessary tools and support they need to achieve growth potential. This includes access to the appropriate skills, market opportunities and growth capital. This in turn will provide job opportunities and drive innovation across the entire nation.

[2]2021 mid-year update of UK tech | Dealroom.co
[3]The UK hits milestone of 100 UK tech companies valued at $1bn or more - Tech Nation
[4]2021 mid-year update of UK tech | Dealroom.co

06

Infrastructure and energy – reflections and prospects

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BACK TO CONTENTS

Infrastructure and energy – reflections and prospects

Energy source and consumption

The Covid-19 pandemic created an unprecedented drop in energy demand due to the restrictions on transport and the closure of shops, offices and restaurants, which outweighed the increase in domestic demand as more people stayed and worked from home. It has been reported that demand for energy across the UK in 2020 dipped so dramatically that it resembled levels not seen since the 1950s.

Commentators have remarked it may be this significant dip in demand that led to the much- proclaimed news that, in 2020, for the first time more of the UK's annual electricity demand was met by renewable energy sources than fossil fuels. According to the Digest of UK Energy Statistics (DUKES), published by the Department for Business, Energy and Industrial Strategy (BEIS), renewables accounted for circa 43% of electricity generation last year compared to the circa 38% generated by fossil fuels. This is positive news given the UK Government's intention to phase out fossil fuels by 2035 and its decision to bring forward the ban on coal-fired electricity to 1 October 2024 (although it should be noted that of the vast majority of fossil fuel generation is by gas, with less than 2% attributable to coal).

The big success story was wind generation which accounted for 24% of the UK's electricity last year – an 18% increase on 2019.

While consumption has begun to pick up according to 2021 Q1 figures published at the end of June, the (then on-going) restrictions on transport, most obviously air travel, was still impacting demand. Renewable generation is heavily dependent on factors which cannot be controlled, such as favourable weather conditions, but even when demand does resume to pre-pandemic levels, the thinktank Ember predicts that renewables will most likely outweigh fossil fuels again in 2021, and if fossil fuels do emerge as the victor, it will be a short-lived reign.

> "The big success story was wind generation which accounted for 24% of the UK's electricity."

Consolidation in the domestic energy supplier market

At its peak in 2018, there were 62 suppliers of domestic energy in the UK market. Since then, challenging market conditions has led to a sharp rise in the number of exits - some strategic and planned, others down to unsustainable business models or a lack of differentiation in market offering. Consequently, at 30 April 2021, the number of suppliers had dropped to 47 – down by a quarter in just 3 years.

At the start of September we published a report with Cornwall Insight (link here) predicting there would be further market exits and that these could include suppliers exiting with larger numbers of customers than to date. This has proved true. The current surge in gas prices means these exits are coming thick and fast with thirteen suppliers collapsing since we issued that report, including Avro Energy – with a 2% share of the overall market, the biggest supplier to exit the market so far.

While we are not likely to return to the days of the 'Big 6' suppliers, it seems inevitable there will be further casualties and the domestic energy supplier marker will look significantly different in 2022 compared with how it looked four years ago. Whilst the recent collapses have clearly stemmed from the surge in gas prices and the impact of the retail price cap, even if prices settle, to survive in this new market, suppliers will need to diversify and embrace technology to provide a different offering to attract and retain customers. As our report highlights, those that fail to go beyond selling energy will not be sustainable in the long-term.

Hydrogen

Driving the growth of low carbon hydrogen is high on the government's agenda and forms point 2 in the 'Ten Point Plan for a Green Industrial Revolution'. Wind and solar are ideal technologies to produce renewable hydrogen and, with a greenhouse gas emission of virtually zero during green hydrogen production, it will have a significant role to play as a clean source of fuel and heat for our homes, transport and industry.

In August, BEIS published the UK hydrogen strategy – setting out its approach to developing a thriving low carbon hydrogen sector in the UK to meet the government's ambition for 5GW of low carbon hydrogen production capacity by 2030.

With the right roadmap and policy, the UK has a real opportunity to be at the forefront of low carbon hydrogen development and adoption, and Scotland and Northern Ireland look set to lead the way.

Provisional figures from the Scottish government indicate that in 2020 the equivalent of 97.4% of Scotland's gross electricity consumption was from renewable sources, so there is an abundant existing clean energy source for the production of green hydrogen with a significant opportunity for inward investment, environmental and employment benefits. As I have commented previously, North Sea oil has left a legacy of the skills needed to build and operate such hydrogen and carbon capture facilities which, together with the geographic advantage of being close to transport and storage infrastructure, makes Scotland an attractive location.

Northern Ireland is in a similar position, with 49.2% of total electricity consumption generated by renewable sources in 2020, an ideal geographical location and a skilled workforce required to accelerate hydrogen innovation and deployment. Due to these high levels of intermittent renewable energy generation and the nature of the electricity network on the island of Ireland, hydrogen could also play a very significant part in helping developers and funders manage curtailment risk through storage and/or injection into the gas grid.

Infrastructure and net zero cities

Sustainability is at the top of most business agendas. It is incumbent on businesses of all sizes to make the transition to net zero – whether that be large organisations who are required to report on the measures they are taking or SMEs who need to be carbon competitive to ensure they remain in the supply chain. But what is required to deliver net zero cities? The thing that stands out is collaboration.

Rather than looking at sustainability initiatives on a piecemeal basis, greater results can be achieved more quickly and effectively by taking a whole system approach. For example, from a real estate perspective, rather than just looking at how a building is powered and heated, considerations should extend to: how people travel to and from the building, the efficiency of the building's location as part of the logistic network and its impact generally on the greater supply chain.

Many councils have made great advances in decarbonised public transport plans through hydrogen-powered buses, but a decarbonised public transport system will fall short if the city itself is unable to progress to become a truly sustainable economic hub.

To this end, there is a need for a more joined up approach between developers and other key stakeholders (local authorities, transport authorities, regulators, utility companies etc) in delivering net zero cities. While there is an opportunity for developers to lead the charge here, it will require local and national government support to drive this collaboration and find innovative solutions, whether that be by way of policy, legislative change and/or financial intervention (subsidy or penalty). With the world's eyes on the UK in the run up to COP26 in November, it would be great to see the government implementing a strategy to engage the public in transitioning to net zero and setting down the foundations for an environment which promotes interested stakeholders to come together to collaborate and innovate and make carbon neutral eco-systems a reality.

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