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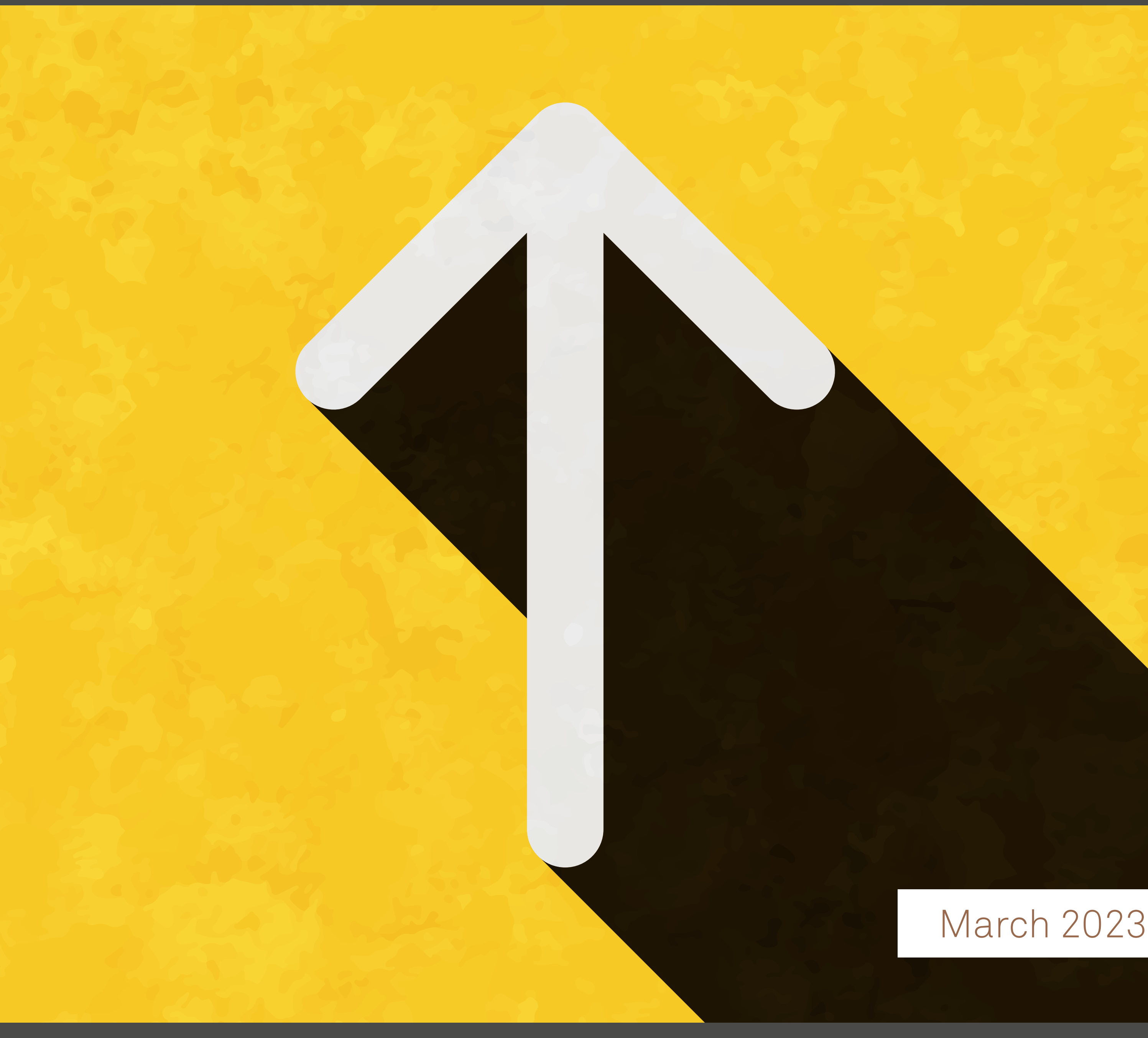
Northern Investment Index 2023



March 2023

Fresh intent

The past few years have been defined by uncertainty – from the unprecedented disruption of the pandemic to post-Brexit trade relations and now persistent inflation and the cost-of-living crisis.

For business investment in the UK, it has contributed to a sense of near permanent volatility. The latest quarterly data from the Office for National Statistics shows business investment to be down 8% on pre-coronavirus levels[1]. If we take the UK tech sector as an example of one of the most attractive industries for investment, 2021 saw a record $36bn deployed as investors unleashed pent up funds. However, that investment then fell by 23% to $27.9bn in 2022[2] as economic headwinds strengthened during the second half of the year.

But amid these challenging conditions, is there a silver lining?

The relative weakness of the pound is certainly an opportunity for overseas investors. There are well-founded expectations that central banks will begin to ease up on interest rates and investors will be active over the next 12 months with company valuations dropping and the possibility that insolvencies may increase.

We wanted to take a closer look at the topic, with a particular focus on the regional economy in the North of England.

To that end, we commissioned a survey of 400 institutional investors, including 250 based in the UK and 150 who are US-based with interests in the UK, and enquired about their investment intentions for the next 12 months, as well as exploring how competitive the North is in a global inward investment market. With regional authorities continuing to lobby for a stronger, more affluent North, the results bring significant room for optimism. We hope you find them useful!

1. https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/businessinvestment/julytoseptember2022revisedresults

2. https://www.uktech.news/news/investment-news/uk-tech-investment-atomico-2022-report-20221207

Mark Rathbone
Head of Corporate (Liverpool)

Sam Mabon
Head of Corporate (Manchester)

Nicola Whittle
Head of Corporate (Lancashire)

Marcus Armstrong
Head of Corporate (Leeds)

More investment inbound

To help set the scene for 2023, first let's look back on 2022.

While the UK was still living with Covid, the majority of legal coronavirus restrictions ended by March and the economy could reopen in earnest. As such, when we asked investors how their UK investment activity had changed during 2022, responses from both the UK and the US showed a marginal increase.

Perhaps unsurprisingly, given the impact of the pandemic in 2021, over half (55%) of homegrown institutional investors said they had increased their UK investment activity in 2022. The story was similar for US-based investors, with 53% increasing their UK investment – both seeing a median average increase of between 20% and 30%.

However, as 2022 unfolded, the global economy experienced a wave of shocks, which are now well understood – though many remain largely unresolved. Accordingly, investment intentions looking ahead into 2023 are more subdued, especially among UK-based investors.

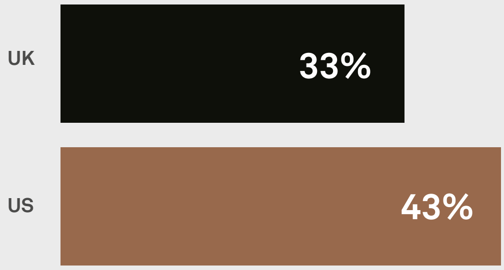
Given the level of uncertainty that still exists, including that resulting from the political upheaval in 2022, many UK-based investors are adjusting their plans. Just a third (33%) of domestic fund managers say they will increase their UK investment activity in the coming year, compared to 43% of transatlantic investors.

However, while it is perhaps understandable to see a drop off in those planning to increase their investment, the largest cohort (44%) still plan to maintain it at 2022 levels, and only a relatively small proportion (19%) plan to reduce it.

That's reassuring, and many will be targeting opportunities to invest in those sectors that traditionally prove more resilient, like healthcare and utilities – especially while company valuations are lowered by weakened demand and favourable exchange rates. »

Investors increasing their activity in the UK in 2022:

Investors planning to increase their activity in the UK in 2023:



Mark Rathbone

Head of Corporate (Liverpool)

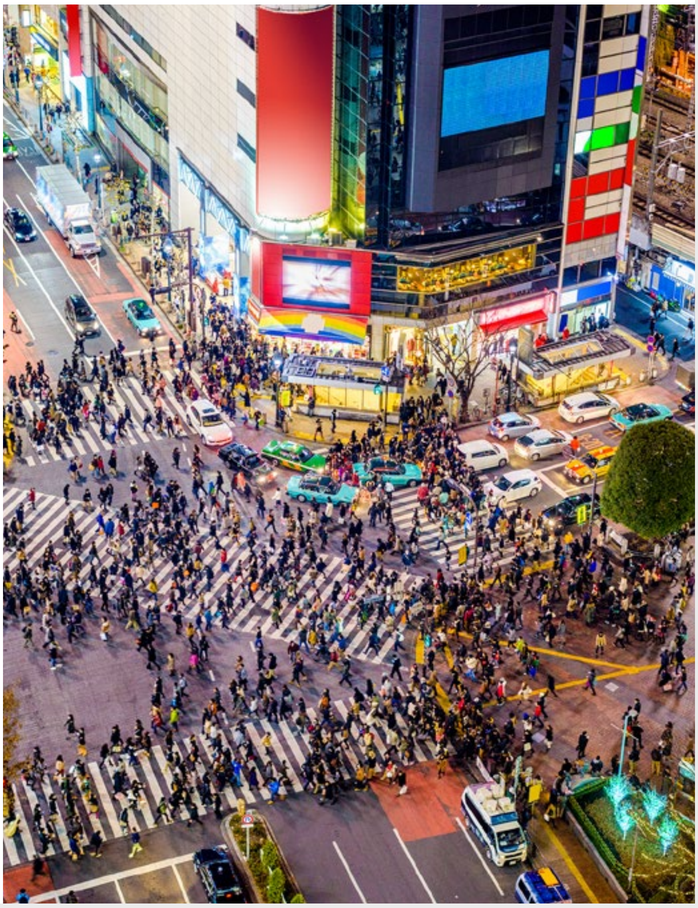
“We are expecting activity levels to remain strong in 2023. Our discussions with acquisitive clients suggest they have a long list of opportunities to explore and the amount of capital available, and access to it, remains encouraging. Particularly for larger corporates, the private equity market, and those that have access to international funds.

“The transaction sizes we are observing – up to £130 million – remain robust nationwide, with a sizeable proportion either occurring or originating in the North.

“In addition, perhaps understandably in the post-COVID era, geography appears to have become less of a factor, outweighed by it playing a lesser part in securing access to talent.

“It also appears that moves towards regional mayors, devolved governance and the resulting ecosystems that are being put in place are starting to play their part in the North. Although there is still much to do.”

> **“Investors are eyeing opportunities everywhere from Germany to Japan and India to Australia.”**



Competing in a global market

A key focus for this report was to understand investors’ priorities for the year ahead as they seek to deploy their capital in an environment of a diverse set of global challenges. So, it was particularly encouraging to see that the UK is viewed as the most attractive market for investment for both UK (45%) and US (34%) respondents.

China was the second most attractive investment proposition for UK investors, cited by 24% of investors - though only 18% of US firms had a similar perspective, likely reflecting ongoing political tensions between the US and China, which includes trade tariffs.

However, it is the geographical diversity of likely investment markets that is truly striking, with investors eyeing opportunities from Germany to Japan, and India to Australia.

So, in a competitive global market, what factors are driving decision making?

UK investors told us that their primary concerns when investing in foreign markets were government leadership (31%), infrastructure (25%), taxes and talent (both 24%). Whereas US investors prioritise talent (32%), tax and infrastructure (both 30%) and regulation (29%). >>

Considering institutional investors in particular, we asked respondents how they intend to invest in the UK over the next 12 months. UK investors favoured direct investment (48%), while the biggest proportion of US investors (52%) preferred to invest indirectly, through hedge funds, mutual funds and Real Estate Investment Trusts.

When it comes to considering which UK-based asset classes are the most attractive, there is a broad spread of views, although risk mitigation appears to be the principle influence on decision making, with fixed-income securities most popular with UK investors (35%) and US firms favouring cash (41%).

For both UK and US-based investors, stocks and equities were the least popular investment target, though they were still favoured by 30% of respondents.

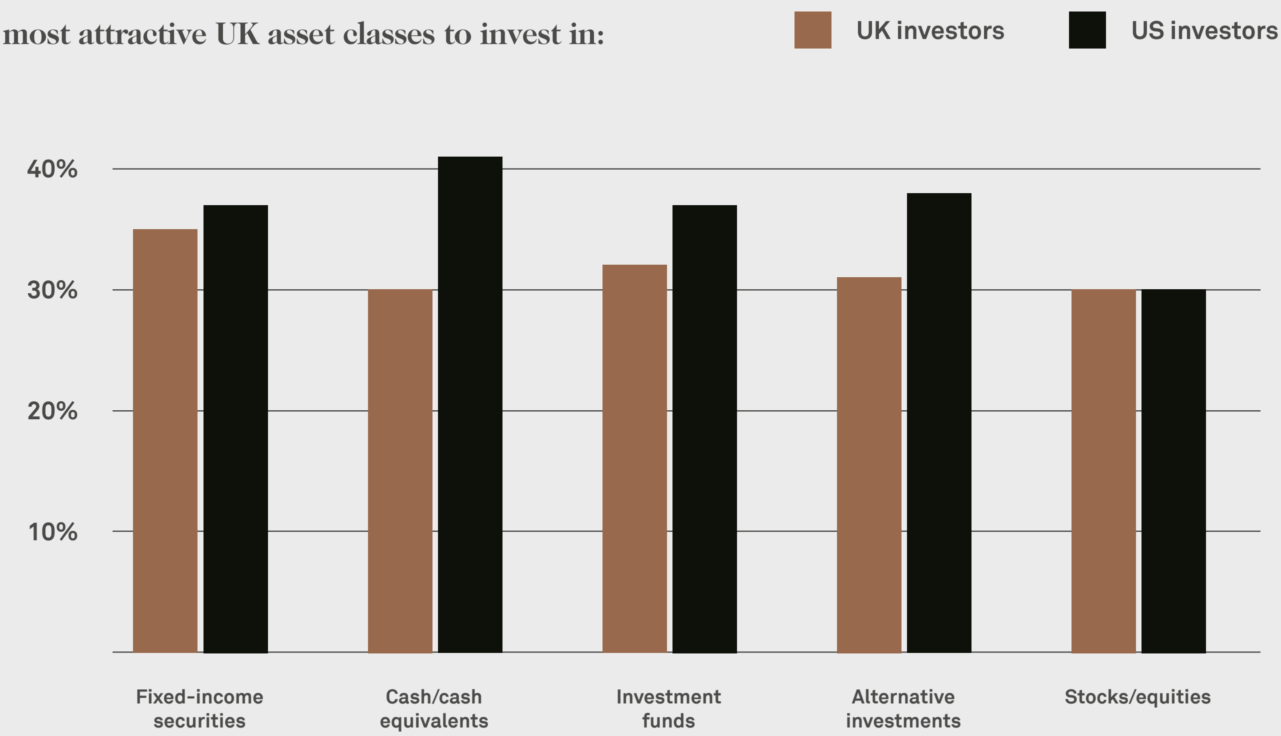
Alternative investments were flagged as an attractive option by 31% of British investors and 38% of American investors, with this asset class covering a diverse range of investment opportunities, from real estate to precious metals, fine art and foreign currency. Perhaps most surprising was to see cryptocurrency top the list of the most attractive alternative investments, given the challenging time the sector has had since peaking in November 2021.

Marcus Armstrong
Head of Corporate (Leeds)

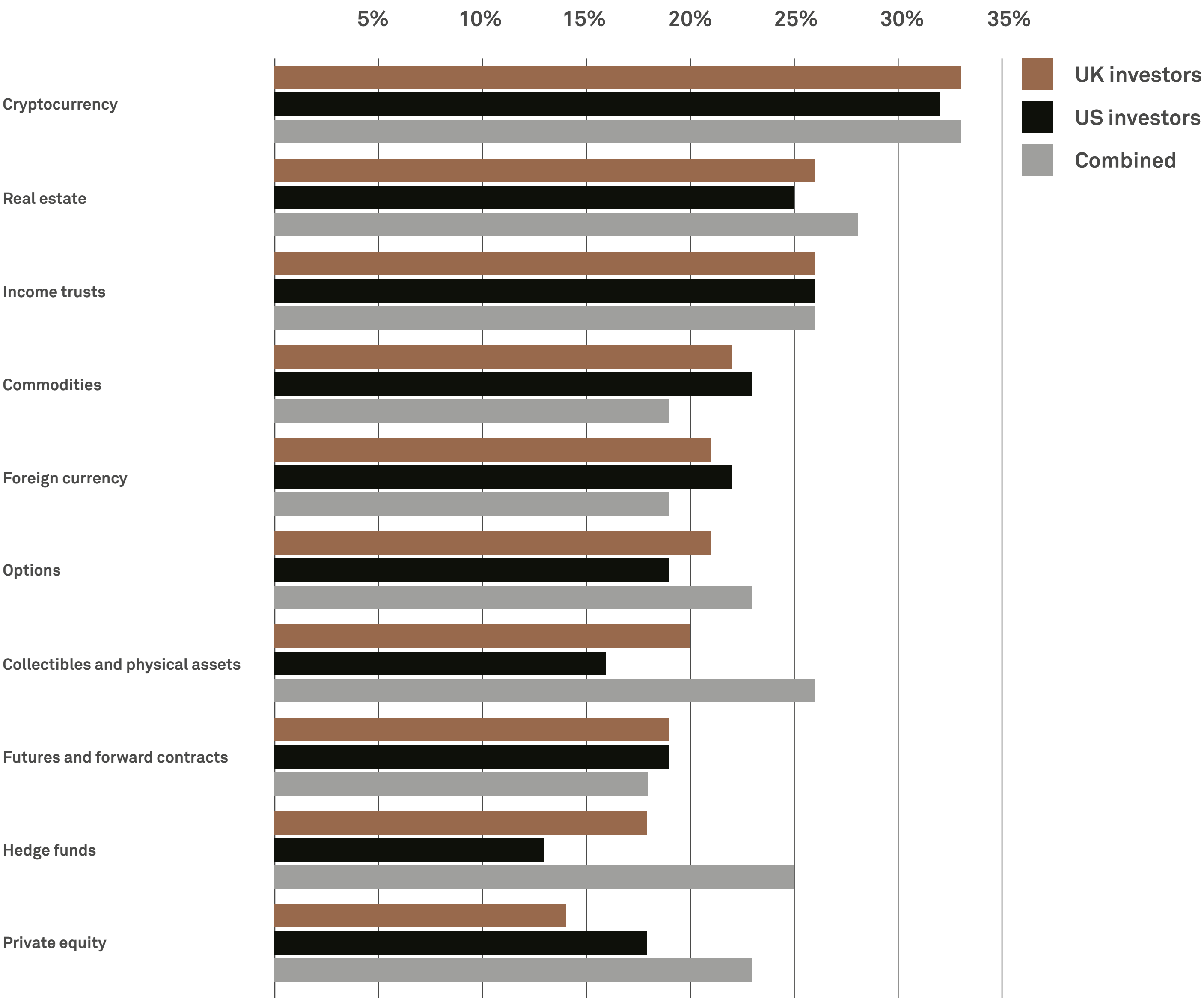
"There remains a significant amount of international interest in the UK, as the market represents increasingly good value for overseas investors. For example, US investors are clearly targeting reduced-value assets and we continue to see increasing interest from investors in the Arab Emirates, the Far East and Europe.

"Where that investment has traditionally largely focused on London, we can now also see a shift towards the regions, as UK-wide assets represent good value, supporting a more balanced spread of interest across the country."

The most attractive UK asset classes to invest in:



The most attractive UK alternative asset classes to invest in:



Power to the regions

The UK is still widely considered as an important investment opportunity, and investors are increasingly looking to deploy their capital across the country to generate positive returns.

When we asked respondents to name the most attractive cities to invest in, it was striking to see the relatively small gap for US investors between table-topping London (33%) and Manchester (29%), Liverpool, Edinburgh and Cardiff (all 26%).

Most notably UK-based investors considered Manchester (27%), Birmingham (26%), Glasgow (23%), Bristol (22%) and Cardiff (22%) to be more attractive to invest in than the capital.

We also asked investors which UK business sectors they thought were the most attractive. In the US, utilities were the top target, cited by a third (32%), followed by hospitality (25%), manufacturing (24%) and agriculture (24%).

Nicola Whittle
Head of Corporate (Lancashire)

"External investment is on the increase among Lancashire companies.

"Business owners are becoming more aware of the opportunities presented by external investment and how it can help them to de-risk their operations, which is having a snowball effect as investors increasingly begin to understand the county's economy.

"In addition, consolidation is happening across a range of sectors and we may get to a point where traditional exit options, such as trade sales, are less available to business owners. That will mean private equity and other forms of external investment will continue to become more appealing."

However, UK investors favour hospitality (24%), professional and financial services (22%) and real estate (21%).

Despite the hospitality sector being amongst those hardest hit by the pandemic and subsequent cost-of-living crisis, and with pub closures hitting 50 a month during 2022[3], investors appear to remain confident in the long-term prospects of subsectors like hotels and accommodation. The UK saw more hotel investment than anywhere in Europe in the first half of 2022, up 40% on the same period a year earlier[4].

The results of our survey also suggested a willingness among investors to invest at all stages of the business lifecycle. However, US investors appear to have more appetite to invest in micro businesses with fewer than ten employees, with 25% of US investors identifying this category of business as the most attractive (compared to 15% of UK investors).

3. https://www.bighospitality.co.uk/Article/2022/10/10/50-pubs-closing-every-month-as-numbers-hit-record-low

4. https://www.cushmanwakefield.com/en/united-kingdom/insights/hospitality-market-trends-and-data

The most attractive UK cities to invest in:

UK investors

1	Manchester
2	Birmingham
3	Glasgow
4	Cardiff
=	Bristol
5	London
6	Leeds
=	Edinburgh
7	Liverpool

US investors

1	London
2	Manchester
3	Cardiff
=	Edinburgh
=	Liverpool
4	Glasgow
=	Leeds
5	Birmingham
=	Bristol

The most attractive UK sectors to invest in:

UK investors

1	Hospitality
2	Professional/financial services
3	Real estate
4	Utilities
=	Sport
=	Retail
5	Tech
6	Manufacturing
=	Health & social care
7	Agriculture

US investors

1	Utilities
2	Hospitality
3	Health & social care
=	Manufacturing
=	Agriculture
4	Sport
5	Retail
6	Real estate
=	Tech
7	Professional/financial services

Looking North

Investors are clearly looking beyond London for growth opportunities, but what is it about the market in the North that is proving appealing?

A small majority, of 51%, think investment prospects in the North have improved in the past year and a similar proportion (52%) have increased their investment in northern businesses in the same period, by an average of 23%.

Around one sixth (17%) of investors have invested less in the North over the last year, with their investment falling by an average 26% when they do.

However, 88% of UK-based investors said they would maintain or grow their level of investment in businesses headquartered in the North over the next 12 months, as did 82% US-based investors.

Over half (54%) of all respondents say the environment for investment and business growth in the region is good, with 59% of US-based investors reporting a positive perspective on the region.

Investors singled out the funding ecosystem (33%), real estate (31%), sector clustering (30%) and wage costs (28%) as key positive factors, and of particular interest, a third (33%) of US-based investors highlighted devolved local government as a principal benefit.

This view appears to support the long held argument that devolution is an effective stimulus for Foreign Direct Investment (FDI), as it gives local leaders the powers and resources to enhance the attractiveness of their locality. »

Sam Mabon
Head of Corporate (Manchester)

"Investors appear to remain positive about investing in Northern businesses, buoyed by continuing liquidity in the market and an attractive business environment.

"Although investors with portfolios that are heavily backed by debt will need to be mindful of higher borrowing costs, which appear to be here for the foreseeable future.

"While there are undoubtedly some sectors that will continue to struggle in the face of high energy costs, international supply chain issues and the cost-of-living crisis, there remains plenty of opportunities to invest.

"These opportunities will be supported by the combined impact of the thriving business clusters developed in recent years; a greater appetite to invest from further afield; and local investors keen to invest in Northern businesses."

The Northern Powerhouse Partnership brings together business and civic leaders to collaborate on shared goals like improving connectivity and devolving economic decision-making.

Following a concerted effort to market the North to international investors, the region has recorded a 72% uplift in FDI in the past five years, while FDI into Greater London fell by 23% in the same period[5].

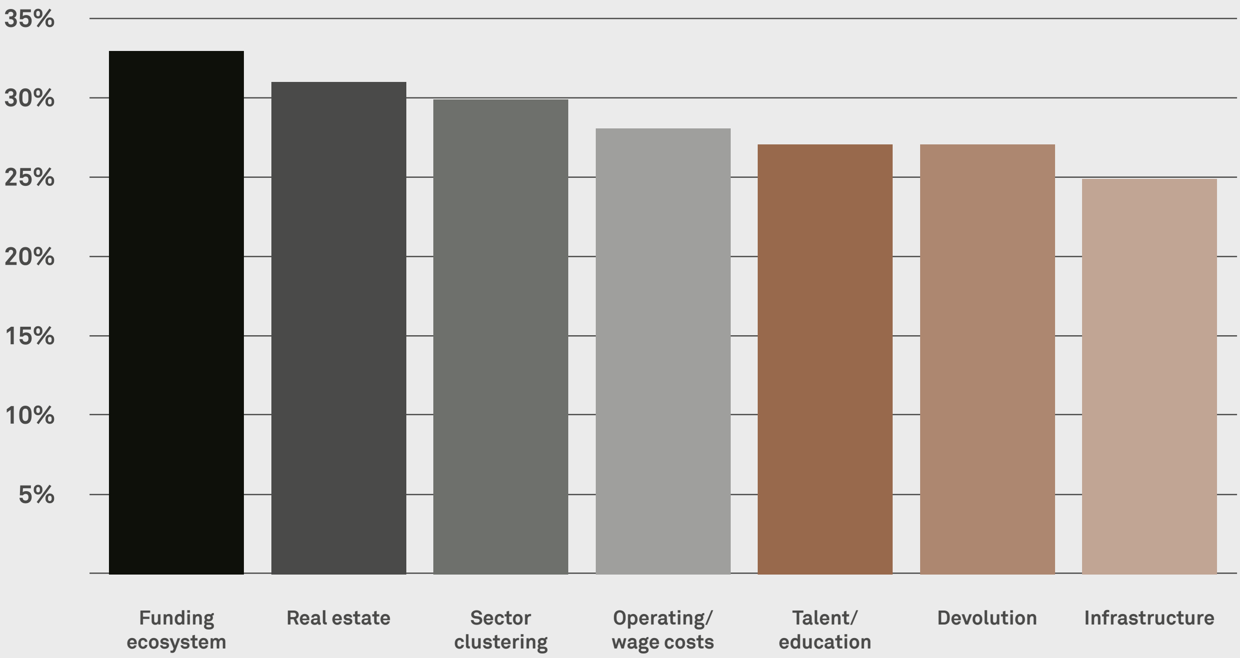
That said, our survey found that one in ten investors still perceive the region's prospects to be poor. We asked those with a negative impression what would help to change their opinion.

For US-based investors, top of the wish list was improved transport infrastructure and a deeper pool of skilled talent (both 43%), while UK-based investors highlighted greater sector clustering (32%) and a stronger funding ecosystem (33%).

These observations appear to support the region's focus on building business clusters in recent years in sectors such as renewables, digital, media, life sciences, nuclear, aerospace and more; as well as its focus on attracting a strong, diverse pipeline of talent; and on improving infrastructure. While there remain deep rooted challenges around connectivity, it does look like this is not yet deterring investment – pointing to a promising year ahead.

5. https://www.northernpowerhousepartnership.co.uk/news/foreign-direct-investment-into-the-north-soars%ef%bf%bc/

Why investors are looking to the North:



Investment that makes the difference

Reflecting on the insight collated in this report, you would be forgiven for thinking that we are on the cusp of a golden age for the North – with inward investment on the up and institutional investors increasingly recognising the potential to invest in the region.

However, while the North is primed to kick-start wider economic growth through its well-documented strengths, not only in emerging sustainable and R&D-led industries, it would be remiss not to acknowledge the wider picture.

The data developed for our Northern Investment Index is private sector-oriented and, though it points to increased funding for businesses in the North, it does not focus on the support the region needs to 'level up' in other ways.

Indeed, data published by the IPPR North points to the low base from which the region is starting. The think tank ranks the North as one of the world's least supported advanced economies when compared with its international peers.

This year's Convention of the North and the subsequent distribution of Levelling Up funding was a reminder of the challenges that the North faces, but also the exciting opportunities that lie ahead.

Devolution and cross-city collaboration are powerful tools and ones that we, as a firm that is anchored across the North, welcome and continue to support.

While we, as businesses, may not be able to directly address challenges such as transport infrastructure, we can play our part in contributing to other long-standing issues, like professional education and social mobility, which have the potential to significantly enhance productivity, while also building a more innovative, diverse and sustainable future.

Speaking on behalf of a business that believes in bringing about positive change, it is clear that the investment highlighted in this report provides a major opportunity to do so. Our responsibility as business leaders is to harness that investment and to make sure that it does.

Robert White
CEO