



# The London Economy

Responding to changing economic circumstances  
**September 08**







## CONTENTS

- 04** FOREWORD
- 06** THE NEW LONDON ECONOMY: AN ECONOMIC POWERHOUSE
- 09** COPING WITH TOUGHER ECONOMIC CONDITIONS
- 12** RESPONDING TO CURRENT ECONOMIC CHALLENGES
- 19** NEXT STEPS

## FOREWORD

The global economy is facing unprecedented challenges. The twin impacts of tighter credit conditions and increases in global commodity prices, especially for oil, mean that we can expect difficult times for the UK economy in the coming months. This will affect each region in different ways reflecting the specific nature of their economy.

So far, while the tougher economic conditions have clearly affected London's property markets and financial services sector, the capital's economy has generally been resilient with employment remaining high. But it is clear that, after the strong growth of recent years, London – like the rest of the country – will need to prepare itself for a more challenging economic climate.

At this time it is critically important that the Government continues to listen carefully to the experience of businesses and local stakeholders across the UK to ensure we understand their concerns. And it is important that businesses are clear what support is offered by the public sector to help them manage these difficult times.


This paper has been drawn up by the Government as an initial framework for discussion with London's government, businesses and communities. It summarises the action the Government is now taking, both nationally and specifically in the capital, to support London's economy and help families and businesses across the city through the tougher times ahead. We are particularly keen

to hear about how the economy is affecting you, whether current policies are working, and what more needs to be done in specific sectors – to help inform the Government's work in the run up to the Pre-Budget Report and wider policy development.

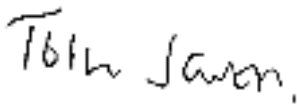
We are also keen to see a comprehensive programme of work for London being developed by local and regional partners which can take forward this framework and complement the action the Government is taking. Uniquely in England, London has a directly elected Mayor to provide strategic leadership to the capital, and we have rightly devolved to the Mayor functions which in other regions still ultimately rest with Ministers, including the London Development Agency and its economic development responsibilities.

In this context of devolved government, the Government believes that the Mayor and his functional bodies have a vital role to play ensuring businesses and families across London are effectively supported during the current economic conditions. We look forward to working with the Mayor over the coming months to ensure London gets through the difficult times ahead and in the long run consolidates its position as Europe's most dynamic world city.

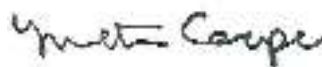
We would welcome views from the Mayor, boroughs and other London stakeholders on this framework, and in particular how the measures outlined can be built upon to address London's specific circumstances. We also want



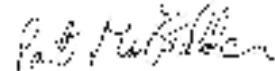
to discuss what further action is needed with London businesses and partners over the coming months and will be arranging an event later in the autumn to listen to the views of London businesses and leaders.



**Tessa Jowell**  
Minister for the Olympics  
and London



**Yvette Cooper**  
Chief Secretary to Treasury



**Pat McFadden**  
Minister for State,  
Department for Business, Enterprise  
and Regulatory Reform

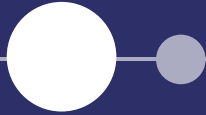
## THE NEW LONDON ECONOMY: AN ECONOMIC POWERHOUSE

**London has become, after more than a decade of strong growth, one of the most wealthy, dynamic and cosmopolitan cities in the world. So it is vital we consider and act upon the implications for London of today's more challenging global economic conditions.**

Global liberalisation has transformed London's economy. The city's historical strengths - its long history as a leading centre of international trade and commerce, transparent legal culture, strong tradition of openness and tolerance of migrants, rich cultural heritage, and use of the English language - have enabled it to benefit successfully from the opportunities the liberalisation of the world economy has brought over the last two decades.

London is one of the wealthiest major cities in Europe. With a GVA of £217 billion in 2006 - larger than the national income of many European countries including Denmark and Austria - its productivity levels are a quarter higher than the UK average, making it a major driver of the UK economy. And London's growth over the last decade has been the highest of any region in the UK, with GVA per head growing on average 3.2% per annum in real terms, making the capital an increasingly important driver of the UK economy. London now accounts for 18.8% of the UK's total GVA, significantly higher than its population share of 12.4%.

London has thrived as one of the world's leading centres for international financial and business services, strengthening its position relative to other financial centres over the last decade, with only New York rivaling it. Over 300 international banks have offices in London, and it is home to some of the world's key financial markets, including the largest foreign exchange market, the leading international bond market, and specialist commodity and insurance markets. The headquarters of more than 100 of Europe's 500 largest companies are also located in London, as well as important



clusters of world class legal, accountancy and consultancy firms.

London has also consolidated its position as a leading world centre for creative industries – from architecture and advertising to the performing arts and publishing – and its tourism industry has over the last decade gone from strength to strength building on London’s rich historical legacy and modern cosmopolitan culture. The growth in these new pillars of the London economy has in turn enabled a thriving consumer service sector and strong construction and property sectors over the last decade, offsetting the continued decline in London’s traditional manufacturing base.

The dynamism of London’s economy has created on average around 70,000 new jobs a year since the early 1990s, and London now has a workforce of 4.7 million. This workforce at

the same time has become increasingly highly educated and skilled as the balance of London’s economy has moved towards higher value sectors. Nearly 40% of London’s workforce is now educated to NVQ Level 4 – significantly higher than the national average of 30%. And due to its business opportunities and vibrant cosmopolitan culture, London has been able to attract many skilled workers from around the UK and the world. Chart 1 shows the increase in London’s workforce since the early 1980s.

This economic success has made London one of the fastest growing major cities in Europe, with the city’s population since 1991 increasing by 650,000 - more than the entire population of Sheffield - to 7.55 million today. It has also strengthened the wider South East economy, with more than 700,000 workers now commuting into the capital from surrounding regions every day.



This success has ensured too that London workers continue to have the highest wages in the UK, with the average full-time worker earning £30,200 a year in April 2007 compared to the national average of £23,800. They also work longer and are more productive on average. And the dynamism of the London economy over the decade has led to London attracting a younger and more diverse workforce than the national average.

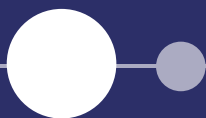
But London continues to face significant economic challenges. Its economic success has put pressure on its infrastructure, from public transport to water and waste services. And there needs to be more housing, including affordable housing, built across London to address the increased housing need generated by this economic success. Over 55,000 households are currently in temporary accommodation, and the average house price to income ratio is the highest for any region in the country.

London also has some of most deprived communities in the country living in close proximity to some of the wealthiest. And despite the success of its economy, it has still had one of the lowest employment rates for working age residents in the country over the last decade, with its rate currently 3% below the national average. Getting more Londoners into work is vital for lifting families out of poverty, increasing social cohesion, improving health and ultimately making London a more attractive place to live, work and invest.

The tougher economic conditions currently being experienced will undoubtedly make it more difficult to tackle these underlying challenges for London in the short term. But it is important that they do not divert

attention away from addressing them. Over the last decade, London has been crucial to the success of the UK economy, and as the major net contributor to the UK exchequer and significant market for the rest of the country, it is important that it continues to be.

Looking forward, it is vital for London to consolidate its position as one of the world's most open, outward-looking cities so it can rise to the challenges of globalisation and fully benefit from the opportunities which the emergence of new economic powers, such as China and India, will bring over the next few decades. And with the Olympics now less than four years away, London now has an unprecedented opportunity to showcase to the whole world how it has transformed itself over the last decade into one of most dynamic and cosmopolitan cities in the world – a city whose ambition and potential attracts businesses and individuals from across the globe.



## COPING WITH TOUGHER ECONOMIC CONDITIONS

Over the last 12 months, two world shocks have been impacting on the UK economy: the global credit crunch and rising energy and commodity prices. Businesses across Britain are finding it harder to raise capital to fund investments and are facing higher operational costs, especially for energy, which in turn are squeezing profit margins and putting pressure on prices. Consumers are also experiencing higher bills for energy and their weekly shop, and many are now paying more for their mortgages.

These tougher economic conditions are expected to hit all businesses, but their impact will vary across regions and sectors. London, like the rest of the country, is being affected by these tougher conditions, although the severity of the slowdown on the capital's economy is difficult to gauge and London's economy appears to have been relatively resilient during the first half of the year.

London's pre-eminent **financial service sector** has inevitably been affected by the turmoil in global credit markets over the last year. During the first half of the year, there has been a sharp decline in merger and acquisition activity and private equity investments, while market trading activity has generally been subdued, although trading at London's various commodity exchanges has continued to expand. Job losses and lower bonuses are widely expected in the City over the next few months, although the extent of these losses remains uncertain.

London's **residential and commercial property sectors** have also been hit hard by the credit crunch. Although the number of completions has remained high over the past year as pipeline developments come on stream, house prices in London have fallen by 4% between January and June (according to CLG's latest figures) and the number of housing transactions has halved. This is having a major impact on future developments across London, with significantly fewer new developments being started. Speculative commercial office developments, including several high profile developments in the City, are also increasingly being postponed, as office vacancy rates in central London increase and credit becomes more difficult to obtain.

**Tourism** in London, after a period of strong growth since 2005, also appears to be slowing in recent weeks, with softer future booking levels. Higher visitor numbers from Europe in response to the appreciation in the Euro against Sterling also appear to have been offset by lower North American visitor numbers. Visit London has lowered its visitor forecasts, with the number of visitors expected to be down by 2.7% to 24.8 million visits this year. Passenger numbers at London's airports are also slightly down on last year's levels.

General business surveys (such as the RBS Purchasing Managers' Index) also suggest declining business activity across London, although some sectors appear to have been less significantly affected by the tougher economic conditions to date.

The **retail sector**, especially in central London

where tourists and wealthy international residents account for a significant proportion of expenditure, appears to be holding up. New retail developments are continuing, with for instance Westfield London at White City – which will be the third largest major shopping centre in the country – on track to open in late October, creating 7,000 jobs. And Westfield Stratford City – an even larger centre at the gateway to the Olympic Park due to open in 2011 – is now under construction, creating a further 18,000 jobs when open and over 25,000 construction jobs over the project's lifetime.

**Public sector construction** also remains strong due to sustained high levels of public investment in London, particularly in relation to transport, education and health services. General consumer confidence in London is difficult to assess due to the absence of readily available data. Londoners have clearly been





affected by higher food and energy prices and mortgage costs in a similar way to families across the country. Given the high levels of mortgage debt in London, the increase in mortgage costs would have particularly impacted on household budgets, especially for those Londoners who have bought homes over the last few years and whose fixed term mortgages have come to the end this year. But Londoners should have generally been less affected by the recent petrol price increases than other parts of the country due to the capital's lower level of car ownership.

Crucially, London's employment trends remain positive to date. Official data indicates that London's workforce was still growing strongly in the year to March, with around 50,000 new jobs mainly in the construction, transport and business service sectors. The employment rate of working age Londoners during the second quarter of this year has sharply increased too by 140,000 to 71.6% compared with a year ago – a significantly greater increase than any other region. The unemployment level at 6.9% also remains slightly down compared to a year ago, and the claimant count for July shows no significant monthly change.

Chart 2 shows the unemployment rate trend since the early 1990s.

It is unclear, however, how far this positive employment trend over recent months will continue given the current economic conditions. Deteriorating economic conditions from a sharper slowdown would suggest upward pressure on unemployment levels in London, which in turn would have an adverse impact on consumer demand and confidence. The London labour market is, however, becoming increasingly complicated, with

considerable migration in and out of the capital every year and high levels of commuting from neighbouring regions.

It is crucial therefore that policy makers, both nationally and regionally, carefully monitor developments across the London economy over the next few months by continuing to listen to businesses and other stakeholders and remain responsive to their needs.

## RESPONDING TO CURRENT ECONOMIC CHALLENGES

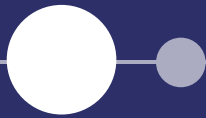
**Despite the success of the London economy over the last decade and its long term prospects, the challenges of the current economic conditions will require an immediate, coherent and comprehensive response. It is the Government's intention to use all means possible so that the impact on individuals and businesses is mitigated and they are well equipped to respond to the situation.**

That is why the Government is determined to ensure London – along with the rest of the country – is as well-placed as possible to respond to any economic downturn. Considerable action is already being taken at both international and national levels, including a further package of measures announced last week to support the housing market nationally. There are also a number of actions that the Government is specifically taking which will support the London economy. This includes action to:

- support international and national economic stability;
- enhance the City's competitiveness;
- support London's businesses;
- invest in London's public services and infrastructure;
- address London's housing problems; and
- help Londoners with their finances.

### 1. International action

No single government can stop the global economic downturn, or solve the challenges of high prices immediately, but the Government is working closely with other countries to face up to the international causes of the problems. It has recently discussed with Saudi Arabia and other oil producers how the world



might be able to increase oil production in the short term, and is simultaneously working with European and other countries to cut the world's dependency on oil in the medium term. We have also worked closely with the IMF to support financial stability and take steps to get global credit markets moving again.

## 2. National action to support economic stability

Nationally, it is essential that we avoid a temporary international inflation shock being transferred into domestic inflation, leading to a return to the price/wage spirals of the 1970s and 1980s. The Government has made clear the need for responsible wage-setting in both the public and private sector, from the boardroom to the shop floor.

The independent Bank of England has a responsibility to set interest rates so that inflation is kept under control. The Bank has an agent in all regions, including London, to ensure that the Bank's decisions on rates are informed by conditions on the ground.

To address the blockages in mortgage markets, the Treasury is also facilitating the Bank of England's Special Liquidity Scheme. By providing increased liquidity to the banking system, this will help take pressure off the banks and building societies during the present period of uncertainty, maintaining the stability of financial markets. It will create the right conditions to ensure banks will be able to lend to each other, and to others, which will in turn support the provision of new mortgage lending to households.

## 3. Supporting the City's competitiveness

The Government is committed to ensuring London remains one of the leading financial centres in the world. In 2006, we established a High Level Group on City Competitiveness comprising senior representatives from across the financial sector to develop and support a new strategy to promote London as the leading international financial centre. It has been focusing on the City's competitiveness and overseas promotion.

The High Level Group has recently agreed to establish a new Financial Services Global Competitiveness Group, jointly chaired by the Chancellor and Citi Chairman, Sir Win Bischoff, to advise it. The group will meet monthly to analyse global trends affecting the competitiveness of the international financial services industry, such as the impact of the sub-prime crisis and the rapid growth of new financial centres in emerging markets. The resulting analysis should enable the High Level Group to prioritise the commercial challenges facing the financial services sector in London and the rest of the country, and will help to inform the Government's policy response to these global challenges. It will report back to the High Level Group in Spring 2009.

The Government also reformed the tax regime in Budget 2007 to support the City's competitiveness. Measures included a reduction in the main rate of corporation tax to 28% - the lowest rate of corporation tax in the G7; tax changes to facilitate market development and innovation in areas such as Islamic finance and carbon trading; and the simplification of aspects of insurance tax rules.

## 4. Supporting London's businesses

It is important that businesses in London – whatever their size or sector – are prepared to respond not just to the tougher economic conditions ahead, but also to look ahead to the longer term challenges that may affect their business. The public sector can play an important role supporting businesses in a variety of ways, and the Government's primary role is to develop a clear national policy framework to encourage enterprise, innovation, and productivity, as well as support the inward investment and international trade opportunities for British companies. In particular, we are nationally:

- making support to business simpler through the Government's Business Support Simplification programme. This will make it easier for business to access the £2.5 billion worth of tools and techniques available through Business Link and other routes;
- putting employers at the centre of the delivery of skills provision through employer-led Sector Skills Councils and free, employer-specific skills brokerage services in Train to Gain;
- enhancing business competitiveness through the Government's Enterprise Strategy published in April, which includes measures to help businesses to access finance; and
- working across government to promote prompt payment in the public sector, as well as exploring non-legislative approaches to tackling late payment issues, to reduce the

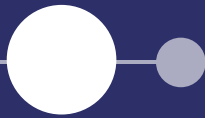
difficulties in cash-flow and financing costs for all businesses.

In London, we will continue to work with regional and local partners, to ensure these national priorities are being delivered effectively for the benefit of London businesses. The London Development Agency has an important role ensuring business support is simplified in London, and is responsible for managing Business Link in the capital on behalf of Government. From April 2009, as part of the simplification agenda, the Train to Gain brokerage service will be included within Business Link, so that businesses can access the whole skills offer from basic to technical and graduate level skills through Business Link.

## 5. Investing in London

The Government is committed to investing in London's public services and infrastructure to support the city's long term growth and economic success. Public expenditure per head in London has increased by 39% since 2002/3, and this expenditure has played in a pivotal role in ensuring London has been an increasingly attractive place to live, work and invest in – after decades of under-investment.

We have invested heavily in London's key public services. Educational attainment is significantly higher, hospital waiting lists markedly lower, and bus services considerably better than a decade ago. London has already benefited from major new hospital and school building



programmes, and we will continue to invest in new buildings and facilities, including academies and health centres, to ensure the city has world class public services.

We also remain committed, not only to the continued modernisation of London Underground, but to the delivery of Crossrail, the biggest transport project in the capital for fifty years and one of the key priorities for London businesses over the last decade. This £16bn project, which will significantly enhance public transport capacity through almost all of London's key employment centres from 2017, will have a major impact on the London economy, boosting construction jobs in the short term and stimulating further development and business investment across the city in the long term.

In addition, we have provided Transport for London with a long term funding settlement which will enable the delivery of its investment programmes, which will see the East London Line extension opening in 2010 and further DLR extensions to Woolwich and Stratford. And Network Rail has begun work on the £5.5 billion Thameslink modernisation programme, considerably enhancing north/south rail capacity across London when it is fully completed in 2015.

Similarly, we are investing significantly in the 2012 Olympic and Paralympic Games. The 2012 Games will generate over £6 billion worth of direct contractual opportunities with £2.9 billion worth of contracts already let, providing significant opportunities for London businesses

and Londoners. As of early September:

- 31,000 companies were registered on CompeteFor, the London 2012 business brokerage system, of which 9,100 are London firms;
- 92 contracts have been awarded to businesses in the five Olympic host boroughs and an additional 331 London companies have won work supplying the Olympic Delivery Authority; and
- Over 3,400 people are employed on the development of the Olympic Park, many from East London.

This investment for the Olympics will also enable the longer term regeneration of one of the most deprived areas of London. And crucially, it will ensure the world's attention is firmly focused on London over the next four years, helping to consolidate London's global image as a dynamic and cosmopolitan world city and stimulate more inward investment and tourism.

## 6. Addressing London's housing problems

In London, and nationally, the housing market has been hit hard since the credit crunch: first-time buyers and others are finding it harder to get mortgages despite falling prices, there are an increasing number of homeowners at risk of repossession, and house building is slowing.

In order to respond to this, the Government announced a comprehensive £1 billion support package on 2 September to help households in difficulty, to support the housebuilding industry and to help first-time buyers get onto the housing ladder. These measures include:

#### **Help for homeowners in difficulty:**

- Supporting thousands of vulnerable homeowners facing repossession to remain in their home through a new mortgage rescue scheme.
- Reforming the Support for Mortgage Interest scheme to increase help for some of the most vulnerable homeowners on very low, or no, incomes.

#### **Support for social rented homes:**

- Bringing forward £400 million of Government spending to deliver up to 5,500 new social rented homes, at a good price over the next eighteen months while the private sector market remains weak.

#### **Help for first-time buyers:**

- Offering 10,000 more first-time buyers currently frozen out of the mortgage market the chance to get onto the property ladder through HomeBuy Direct, a new shared equity scheme in a new partnership with housing developers.
- A one-year Stamp Duty holiday (from 3 September 2008) for all houses costing up to £175,000, increased from £125,000.

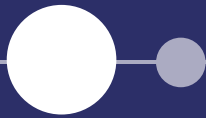
This new package of national measures forms

only part of the considerable investment the Government has already committed for affordable housing nationally. Over £10.4 billion is being provided from the Regional Housing Fund in England over the 2008-2011 period, of which £8.4 billion is being invested in affordable housing, and London's indicative share of this funding is £3.3 billion.

In parallel, the Government wants to see the continued regeneration of London, particularly in the London part of the Thames Gateway, to address the long term need for more housing. We have established the Homes and Communities Agency – from the merger of English Partnerships and the Housing Corporation – to bring together the Government's housing and regeneration programmes, and the Agency will work closely with regional partners, local authorities and developers to ensure key schemes in London continue to be taken forward in the more difficult market conditions.

## **7. Helping Londoners with their finances**

It is important for the success of local businesses that consumer demand holds up. The Government is committed to achieving this through reforms to the tax system. Most families across London with children should be getting extra cash this year already as Tax Credits have gone up, and basic rate taxpayers can expect an extra £120 from this autumn due to the changes in tax allowances too.



Action is also being taken to help alleviate the impact of high fuel bills which are causing stress to many families. The Government's Winter Fuel Payments will give at least £200 to pensioners, and more to over 80s, including extra money for this winter, and the energy companies have pledged an extra £225 million over three years to help support vulnerable consumers. Certain groups can also get a Government grant to pay for insulation and heating improvements, and pensioners on low incomes can receive free central heating or fuel discounts.

## The Mayor of London

Government action collectively aims to ensure that businesses and families in London, and the rest of the country, are as well-placed as possible to respond to the tougher economic conditions. We will continue to listen to businesses and other stakeholders about the developing economic situation and the effectiveness of current policies – to inform the Government's work in the run up to the Pre-Budget Report and wider policy development.

Local government and regional institutions have an important role to play too, and in London where we have restored democratic strategic leadership to the city, this means the Mayor of London through his functional bodies playing a crucial role.

The Government created the office of Mayor of London eight years ago to provide strong

democratic leadership and strategic direction to London. We have rightly devolved key powers and responsibilities down to the Mayor, especially in relation to economic development where the Mayor is often better placed to decide what interventions best contribute to London's sustainable economic growth.

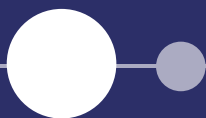
While Ministers remain accountable for Regional Development Agencies in other English regions, the Mayor is responsible for the London Development Agency and we have devolved to the Agency key functions which support London's economy, including:

- regeneration projects and programmes for London;
- business support advice through Business Link London and specific funding for London's businesses;
- inward investment promotion through Think London; and
- tourism promotion through Visit London.

The Government has increasingly delegated responsibilities and freedoms to Regional Development Agencies over recent years, and this has given the London Development Agency the flexibility to prioritise investments and to shape its expenditure programmes in light of London's changing economic circumstances. This has enabled the Agency to fund innovative programmes specifically to address London's economic issues, for instance its affordable childcare programme jointly developed with Sure Start.

In addition, the Mayor has several other

important responsibilities which impact on London's economy, including preparation of the London Plan and Transport for London. And following the Government's review of the Mayor's powers in 2006, we have given the Mayor more strategic influence over housing and skills funding in London through his Housing Strategy and chairmanship of the London Skills and Employment Board.



## NEXT STEPS

This paper sets out an initial framework for discussion with stakeholders about how London should respond to the tough economic conditions the capital is likely to face over the coming months. It is not intended to be a final statement on the matter.

Given the complex nature of the London economy, the Government is keen to work closely with a whole range of local and regional partners, including business, to address the challenges described in this document and to build on the support and initiatives described above. And we want to see a comprehensive programme of work being developed for London which can take forward this framework and inform the Government's work in the run up to the Pre-Budget Report later this autumn.

Given London's unique governance arrangements, we particularly want to see the Mayor of London playing a strong leadership role to ensure that London can effectively respond to the current economic challenges. We have rightly devolved to him key economic development responsibilities. It is now up to the Mayor to use his powers and responsibilities effectively, working where necessary with London's councils and businesses, to develop further practical measures which complement the Government's own plans.

We would welcome views from the Mayor, boroughs, businesses and other London stakeholders on this framework, and in particular how the measures outlined can be built upon to address London's specific circumstances. We also want to discuss what further action is needed with London's businesses and partners over the coming months and will be arranging an event later in the autumn to listen to views of London's businesses and leaders.

Comments on the framework should be sent to:

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