London's Place in the UK Economy, 2004

October 2004

THE LONDON SCHOOL OF ECONOMICS AND POLITICAL SCIENCE

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London's Place in the UK Economy 2004 is published by the Corporation of London. The authors of this report are Ian Gordon, Jan Stockdale, Tony Travers and Christine Whitehead of the London School of Economics.

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Table of Contents

Foreword

Michael Snyder
Chairman, Policy and Resources Committee
Corporation of London

London's Place in the UK Economy aims to take a long-term view of the London economy in the context of recent economic and political developments. The authors of the 2004 edition, Ian Gordon, Jan Stockdale, Tony Travers and Christine Whitehead from the London School of Economics, provide more compelling evidence of London's central role in promoting the health and wealth of the nation.

Their conclusions tie in with another recent Corporation report, - *London's Linkages with the Rest of the UK*, written by Oxford Economic Forecasting and published in May 2004, - demonstrating that the relationship between London and the regions is two-way, with both parties benefiting from the other. As this new report points out, London gives more to the Exchequer than it actually receives - London continues to make a positive economic contribution to other regions.

Central to the report is the calculation of London's contribution to the UK economy. As the balance of finances of the UK government has moved from surplus to deficit, so London's overall contribution has changed, although it remains the dominant regional contributor to the nation's finances. In the last fiscal year for which figures are available, London made an estimated net contribution of almost £11 billion.

However, if our capital city is to continue to contribute such large sums of money, it requires more investment in its infrastructure and public services to accommodate population growth and to sustain economic development. Although there are now hopes that a number of vital transport projects will go ahead, there is still no government money for Crossrail, nor an identified stream of infrastructure finance. Unless funding does become available, the city's economy will remain at risk.

This year's report also contains a special section on crime and policing in the capital. The authors point out that Londoners appear to be growing more fearful of crime despite the fact that the incidence of many types of offence is declining in the city. Perceptions of crime are important as they impinge on the quality of life. We must support both the Metropolitan and City of London police forces as they tackle problems common to those faced by other UK forces *and* the specific problems that are unique to London as a global city and economic powerhouse.

London's role as a world city makes its economy subject to pressures other than those felt by the rest of the UK, and its position as a national economic asset must not be discounted. I hope this report demonstrates to the reader the positive contribution London currently makes to the nation's economy.

Michael Snyder
London
October 2004

Ten Key Points

- London's economy has shown some recovery during the year although that recovery is not strong. Across London, demand has been sustained by population growth, increased debt and a number of major construction projects. Employment is growing more slowly than output, and investment in the commercial property sector, another indicator of the buoyancy of the London economy, has yet to pick up.

- London's relatively healthy economy is driven by the concentration of activity in growth industries, particularly services. In the majority of these activities, however, London is growing more slowly than other parts of the country.

- Earnings in London are more than 25% higher than elsewhere in the country. However, once the mix of occupations and differences in the cost of living are taken into account, standards of living in London are perhaps just 11%-12% higher than in the country as a whole.

- Employment has grown in London unlike in most of the other world cities, notably New York. Over the last year and against past trends, this growth has been concentrated more in inner rather than outer London. The east continues to perform relatively badly and there are as yet no signs of improvement following government announcements about large-scale initiatives in the Thames Gateway.

- The long boom in London house prices has undoubtedly come to an end, and prices at the time of publication are falling. However, it still seems more likely that the market will go flat for a while than that prices will fall precipitously. Over the medium term, London house prices look less over-valued compared to many other areas of the country.

- London receives an above-average share of public expenditure from central government, but this is more than offset by its very high tax bill. In 2002-2003, the best guess is that London made a net tax contribution of £11 billion to the rest of the economy - a modest decline from £15 billion over the last two years although an alternative calculation, based on the city receiving an equitable share of total UK public expenditure, produces a figure as high as £19 billion.

- Public expenditure in London - and indeed the South East - is far below the national average as a proportion of the region's economy. This is particularly significant because the sustainability of London's economy and its taxable capacity depend on adequate infrastructure and public services.

- On headline figures London appears to be disproportionately open to crime even though it has by far the largest police force in the country. But crime, on average is actually falling, and for some types of crime, quite steeply. Moreover, in addition to fighting crime and anti-social behaviour, London's police have to deal with many capital city and security activities as well as with vast inflows of commuters and tourists.

- There has been an important change in the rhetoric regarding government investment in London infrastructure, and there are hopes that a number of major transport projects are now set to go ahead in the near future. There is still no government money for Crossrail, nor an identified stream of infrastructure finance.

- London's competitiveness appears to have been at least maintained, more as a result of a flexible and relatively highly skilled workforce than of capital investment. The best guess for the future is for continuing slow growth at rates comparable to the rest of the country unless some major external economic or political shock rocks the UK.

Executive Summary

The London Economy - Recent Developments: The long boom of the late 1990s, when London's performance matched and even exceeded that of the UK economy as a whole, has been followed not by a sharp downturn but by a few years in which growth has slowed while uncertainties about the future remain unresolved.

The London Economy - A Long Term View: The three key longer-term trends remain the shift away from manufacturing to face-to-face service activities; increased decentralisation generating overspill from Greater London of both people and jobs; and regionalisation of the London economy.

Trends in the 1980s and 1990s: In the 1980s and 1990s an economic environment more favourable to London's strengths produced three positive developments: a rapid rise in earnings relative to the UK in the 1980s; the halting of long-term employment decline; and large-scale international inward migration bringing population growth to London during the 1990s.

Trends over the 1990-2002 Business Cycle: Over the current cycle, employment in London started to grow, and exceeded the national growth rate. Productivity has been growing but less dramatically than in the previous cycle.

Standards of Living in London: On average, the standard of living of the average full-time worker is perhaps 11%-12% higher in London than it is elsewhere in the country. Average figures do not reflect the great variations between occupational groups and the difficulties that new entrants have in paying for adequate housing.

Labour Market, Skills and Education: London's labour market is flexible and robust. It is also very open to commuting and benefits considerably from inward migration. On the other hand, London continues to have higher levels of unemployment and non-participation in the labour force. The labour force in London is particularly skilled by UK standards with a third of all workers in the market having degree level qualifications.

Housing in London: There is great pressure on housing supply in London, with less growth in dwellings than in household numbers since 1991. Owner-occupation has grown relatively slowly and house prices in London are particularly volatile. Low interest rates have kept first-year costs of purchasing in London below those in the last boom. Low inflation means, however, that the burden of payments lasts longer.

Sub-Regional Variations within London and the Metropolitan Region: In contrast to earlier periods, employment growth trends in inner London are now more positive than in outer areas. There are significant east-west differences in outer London and the adjoining Outer Metropolitan Area, with growth fastest in the west and south of the capital, and the east continuing to perform more weakly. To an extent, house prices reflect these trends.

London 2003-2004 - The Most Recent Evidence on Change - Levels of Economic Activity: After a modest downturn in 2002-2003, the London economy has shown some recovery in the last year. Business service employment has stabilised and is now showing signs of growth while in the rest of the London economy, demand has been sustained by a combination of major construction projects, credit-based consumption (as at the end of the 1980s) and population growth.

Property Markets: The commercial property market in London appears healthier than it did at the same time last year but the revival is not secure. Central London, especially the West End, is leading the upturn in the office market but London is lagging behind other regions, in terms of rentals and vacancy rates, in both retail and industrial property.

House prices remain a key concern. Output levels have finally started to increase perhaps exactly at the time when a downturn in demand seems likely. Social sector output remains low, and there are increasing problems of homelessness.

Summary of Recent Evidence on Change: The London economy has shown a clear bounce-back from the downturn of the previous year, with optimistic signs of further growth in the next year or two. This largely reflects national macroeconomic developments rather than factors peculiar to London.

The Competitive Position of the London Economy: London's competitiveness continues to depend on both specialisation and diversity. New evidence suggests that its strengths are heavily concentrated in financial, professional and business services, its range of markets and often in foreign owned firms.

Market Areas and Export Orientation: London's businesses serve a wide range of markets with a sizeable global sector, notably in financial services, serving markets beyond Europe and North America. London's share of export sales is above the UK average and in all its particular specialist service sectors, export performance is much stronger than elsewhere in the UK.

Ownership: Foreign-owned businesses are an important element of the London economy and are particularly strong source of international exports.

London's Competitiveness: On most indicators, London's output performance is above average. In terms of inputs, the city appears to be able to attract the skills it requires but is only average in terms of fixed capital formation.

Public Expenditure and Taxation in London and the Regions: A range of recent studies has confirmed that London continues to contribute substantial net resources to the Exchequer. This figure has been calculated as the difference between expenditure and tax. As the government's finances have gone into deficit, this has meant a fall in the "subsidy" of all contributing regions (and a similar rise in the net receipts of other regions). Because the absolute differences between contributing and receiving regions have remained reasonably steady, an alternative method of calculating London's contribution has therefore been added to this report.

London's Contribution to the UK Economy: In line with the original method of calculating London's contribution, it is estimated that between £54 billion and £66 billion of public expenditure was made in the city in 2002-2003. At its mid-point, this represents 14.5% of total UK public spending compared to 12.4% of total population. A similar estimate of the total take from households and businesses suggests that London paid taxes that year of between £65 billion and £68 billion. At its mid-point, this is 16.9% of total UK taxation, significantly above the city's share of both public expenditure receipts and population.

The alternative way of calculating London's contribution is to consider the city's public spending receipts and tax payments in terms of their shares of the UK totals, and the difference in percentage points then applied to total UK public spending. Using this method, the mid-point estimate for 2002-2003 is that the gap between London's share of taxes and its share of expenditure – its contribution, in effect - was around £11 billion. This is somewhat lower in money terms than in the past two years because of a slightly increased share of expenditure though the percentage point difference is in line with previous figures.

Public Expenditure as a Proportion of London's Economy: Public expenditure in London and the South East is far below the national average as a proportion of the region's economy. This is significant because sustainability of the city's economy and taxable capacity depends on adequate infrastructure and public services.

Crime and Policing in London: There is a growing perception that London is a city ridden by crime and anti-social behaviour. However, although crime and safety is one of the aspects of living in London that causes the greatest level of concern, the extent of this concern is declining.

Is Crime a Particular Problem in London? Recorded crime rates of nearly 150 per 1,000 residents are more than 30% above those in the rest of the country, though offence rates are below those of some other metropolitan areas. Equally, crime rates in London have stabilised over the last three years and the incidence of many types of crime is falling rapidly, though violent crime continues to increase.

Policing in London: London has 21% of the police officer strength in England and Wales higher than both its share of population and of recorded crime, and policing costs the average London household about £160 each year, a figure that is rising rapidly. However, London's police service has to cope with almost a million daily commuters and thirty million tourists each year, and also address a far wider range of activities than other forces, many related to London's role as a capital and a world city, notably state occasions and anti-terrorism activity.

Attitudes to Crime and Safety: Londoners perceive crime to be increasing both nationwide and in their own area even though incidence is actually falling. These concerns are particularly strong in the social rented sector but they do not appear to be dominant reasons for households thinking of moving out of the capital. Although controlling crime and improving safety are important issues for Londoners and the London economy, the situation is not as bad as it is painted and it is generally improving.

Key Issues for the Future: London's future looks relatively healthy but there are many uncertain factors which will help to determine what the actual outcome will be.

'Greater' Greater London and the Northern Archipelago: A recent study from Sheffield University claimed that London is a vast city embracing much of southern England, which has become richer and more successful than any other part of the UK. This is not a sudden event and it is difficult to imagine government interventions that could change the pattern without affecting international competitiveness. However, the study has revived some myths about London which this report lays to rest. These include an alleged population drift from north to south whereas the opposite is true, London's population being sustained by international inward migration; a belief that it is the banking and finance sector that has driven London's growth whereas the sector has actually performed better in other regions; and a misplaced concern that globalisation is weakening London's links to, and interdependence with, the rest of the UK.

Investing in London: Major projects such as the East London Line extension, a number of Docklands Light Railway developments and several tramway schemes are now set to go ahead. Crossrail will be given Parliamentary time, though the funding required has still not been put in place. Even so, the recent review of local government finance makes no proposals for funding this and other future projects,

Housing and Planning in the Region (The Barker Review): This review aims to free up the housing and planning system to deliver significant increases in housing output and thus reduce house price inflation, particularly in London and the South East. Its proposals support the Prescott agenda of sustainable communities, which is already concentrating on ensuring a step change in output in the South East.

Dispersal of Civil Servants (The Lyons Review): Proposals have been made to relocate 20,000 civil servants away from London and the South East of England although the policy has to some extent been overtaken by more extensive proposals to cut between 40,000 and 80,000 civil servants across the UK. No command-and-control functions will leave the capital and any relocation would be unlikely to have any long-term impact on London's powerful and private sector-driven economy.

Where is London going? Although the capital's economy remains flexible and internationally competitive, there will always be questions about its longer-term potential. The most likely scenario involves continuing economic growth but with slower expansion in employment.

1. The London Economy: Recent Developments

The long boom of the late 1990s, when London's performance matched and even exceeded that of the UK economy as a whole, has been followed not by a sharp downturn but by a few years in which growth has slowed.

This past year has seen an upturn in London's economy in terms of output, employment and take-up of premises. This reflects a strong activity base now characterised by a diverse range of services. These in turn depend on a high quality workforce and the infrastructure necessary for productivity growth. Finance and business services remain major drivers of the economy but other sectors, notably creative and media activities, are of growing importance.

Although London has clearly done a great deal better in the last few years than many commentators predicted, it is now growing at a rate comparable to the rest of the country rather than outperforming the UK as a whole. In international terms, London appears unique among world cities, which have experienced more sustained declines in activity and employment since the beginning of the twenty-first century.

On current evidence, it could be argued that London's economy is on course to achieve the growth projected in the Mayor's London Plan. However, more detailed analysis suggests that the assumed relationship between output and employment in the Plan overestimates the employment needs associated with projected growth of economic activity and income. A recent (2004) report from the Prime Minister's Strategy Unit endorsed the view that London's economy was highly productive, and that its strong relations with the rest of the economy were mutually beneficial. However, the priorities identified in the report were focused on public service delivery, quality of life and sustainable communities rather than on anything more directly related to continued economic success.

London's labour force has become more skilled and more diverse over the last few years, to the point where a third of its working population have degree-level qualifications. It remains heavily dependent upon international migration to meet both the growing range of skill requirements and the similarly expanding demands for relatively unskilled service sector workers.

Construction activity, a major predictor of a healthy local economy, has increased significantly over the last year, and will increase very much more if the major infrastructure projects which are now scheduled to go ahead actually do so. London's open economy should be able to attract the labour necessary to undertake these projects effectively, although there remains a major shortage of the senior management skills necessary to bring large infrastructure projects to fruition.

At the time of writing, the housing market in London appears to be heading for a soft landing, with evidence of falling prices and activity, but with no real sign of the often predicted complete collapse in confidence. Although some adjustment from the period of over-activity observed at the beginning of the decade is to be expected, the underlying demand pressures remain strong. Of particular importance in this context is the Buy-to-Let market which helps to provide both accommodation for the increasing flow of short-term migrants and students, and a relatively desirable investment compared to the uncertainties of the stock market. Another positive sign is that the push to increase housing output in London – encouraged by central government and the Mayor – is starting to bear fruit.

One of the most significant initiatives in London over the last 18 months was the introduction of the Congestion Charge in February 2003. It has certainly caught the world's interest and has in many ways been obviously successful: the technology has worked, much to many people's surprise; it has been easier to get around the streets within the Zone – even though journey times from outer London to the centre have not always declined; and public transport moves more quickly and more people are using the buses, although the cost per passenger has almost certainly increased. It is not surprising that large numbers of firms have asked for reductions in their business rate to offset falls in activity. There are, however, many businesses which have benefited – and whose owners are not asking for rises in their business rate.

The fundamental question that remains is whether London has the infrastructure, particularly the transport infrastructure, to support its potential economic growth. The extent to which this issue is dominating the discussion of whether London can possibly host the Olympics, let alone win the bid, reflects growing international concerns about long-term viability.

More generally, London is clearly a difficult place to live in terms of housing, education, and getting around, with concerns about safety, rising violent crime and anti-social behaviour rising across the capital. On the other hand, it also has many recognised benefits to individuals. There is little evidence that the balance between costs and benefits has changed over the last few years or that the high cost/high benefit scenario is adversely affecting investment.

The object of this report is to place the current position of London's economy in context and thus help policy-makers, decision-takers and commentators alike to make better assessments of emerging trends. In order to understand these trends, it is not enough simply to look simply at year-on-year changes in key indicators. Rather, longer-term trends and the risks of sudden changes in fundamentals must also be included in the analysis.

In particular it is important to see London in relation to the wider UK economy and that is one primary role of this report. Although the capital is clearly a global city and one of the most important facilitators of the world economy, it remains an integral part of the UK economy and this position underpins London's future strengths. The evidence from the 2001 Census of the trend towards an ever-larger Greater Metropolitan London area covering almost the whole of the south of the country from the Wash to the Severn was not a surprise and has undoubtedly contributed to the relative overall success of London and the UK (Dorling *et al.,* 2004). However, long-term stability and robust growth depends as much upon maintaining and strengthening the links with the rest of the country as it does on continuing to build links with the rest of the world.

The capital remains a major provider of tax revenues to the Treasury, although the impact of net public borrowing means that, on some measures, the extent to which London's exports its resources to the rest of the UK appears to have declined. Perhaps as importantly, London's total income includes a far smaller proportion of public expenditure within its gross value added than is the case elsewhere. London therefore clearly has to make its own way in a manner not required of other parts of the country.

This report - *London's Place in the UK Economy 2004* – addresses these issues. In section 1, we review some of the key trends in the London economy. Section 2 provides a long-term view, while section 3 examines the recent evidence. The report then looks at particular aspects of the London economy: section 4 measures some of the factors that determine London's competitive position; section 5 analyses London's public expenditure and taxation position in relation to the rest of the country; and section 6 – the year's special topic – concentrates on crime and policing, one of the areas of most concern among Londoners, and assesses whether there is indeed a crisis and how problems of crime, fear of crime and anti-social behaviour are being addressed. Finally, section 7 reviews a number of research and policy reports with implications for the London economy and looks to identify some of the most important areas of change.

Overall, London's economy has done better than expected this year. There are many factors which could push it off course but, equally, the current trend of slow but steady growth could well continue for some time.

2 The London Economy: A Long Term View

2.1 Key Long Term Trends

The three key longer-term trends remain the shift away from manufacturing to face-to-face service activities, where London has led the way within the UK; increased decentralisation generating overspill from Greater London of both people and jobs; and regionalisation of the London economy.

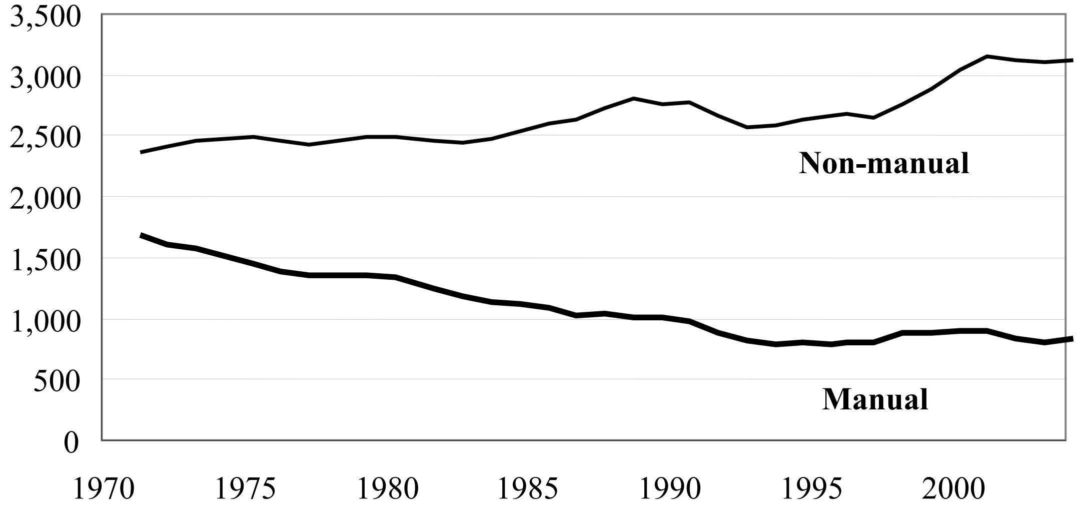
Since the early 1960s, the balance of London's particular strengths and disadvantages, particularly in relation to space and accessibility, has promoted three great trends which are still underway.

The first of these involves a sector shift in the economic base of the city, away from goods-related activities toward services of many kinds, but especially those involving high levels of face-to-face contact, notably in the office economy. The UK economy as a whole has been moving in the same direction, with extensive de-industrialisation over this period. In London, not only did these changes start earlier and proceed much faster, they also played to the city's established strengths, encouraging increased specialisation in activities in which it had always excelled and which now also enjoyed more rapidly expanding markets. Nevertheless, for a long period of time, through into the 1980s, the scale of employment decline in the goods-related sectors - manufacturing, transport and freight distribution - substantially outweighed job gains in expanding service activities.

The second great trend has been one of decentralisation, as growing incomes and productivity have driven demands for lower residential and employment densities, leading more or less inevitably to an overspill of large numbers of people and jobs (especially in space-hungry manufacturing and freight distribution) into areas well beyond the Greater London boundary. These remain integral parts of the metropolitan economy, contributing to, as well as drawing from, the city-region's economic strengths. At a Greater London level, however, decentralisation has contributed to a recorded loss of almost a million and a half manufacturing jobs in London since the early 1960s, representing a contraction of about 80%.

Expansion of service jobs in London has offset about half that gross job loss but these sectors also have been growing faster in outer parts of the metropolitan region. Within the service sector in London, there were also substantial job losses in activities with large proportions of manual workers, particularly those associated with the former London Docks. These contributed, particularly in the 1980s, to the strong shift from manual to non-manual sectors of the economy, with major implications for the mix of jobs available in London (Figure 2.1). The decline of manual jobs has since slowed, as the most vulnerable activities have largely disappeared.

Figure 2.1
Manual/Non-manual Employment Greater London
1971-2004



Source: employee data from NOMIS.
Notes: for definition of the manual sector see Table 2.2 note 2.

Finally, demand for more locally-orientated consumer services was affected by the continuing out-movement of large numbers of London residents to other parts of the South East, mostly in pursuit of more living space. For some time in the 1960s and 1970s, the net outflow was around 100,000 per year, though over the last 25 years or so it has settled down to around 50,000 per year. Actual employment growth in London during this period was thus very largely the result of growth in private sector, office-based services, though the more recent upturn in overseas immigration should also have provided some boost to consumer services.

2.2 Trends in the 1980s and 1990s

In the 1980s and 1990s, an economic environment more favourable to London's strengths was reflected in three positive developments: a rapid rise in earnings relative to the UK in the 1980s; the halting of long-term employment decline; and large-scale international inward migration bringing population growth to London during the 1990s.

Most of these long-term trends continue to be important, as can be seen by looking at employment over the last couple of economic cycles for Greater London and the surrounding Outer Metropolitan Area, which represents the rest of the functional London region in economic terms. From Table 2.1, we can see in particular that

- Employment in manufacturing and the manual elements of the service sector continued to fall. With fewer jobs left to lose, the effect on overall employment has been less dramatic, however, and employment in the main sectors of manual employment stabilised from the mid-1990s

- Within the metropolitan region and beyond, the trend to decentralisation has continued, with more positive employment changes in both production activities and business services in areas outside Greater London

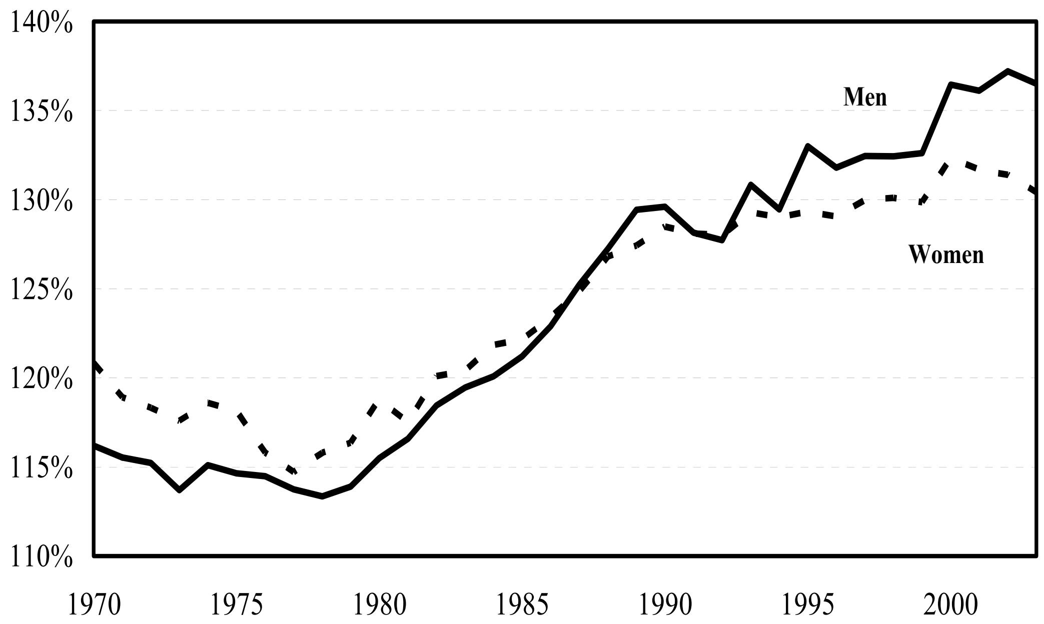
- Consumer and public service growth has also been weaker inside Greater London than in outer parts of the region, reflecting the continued heavy net outflow of migrants from London to the less densely populated parts of southern England (Figure 2.4).

Table 2.1
Employment Change in Greater London and the Metropolitan Region
(1981-2002)

	Greater London		Outer Metropolitan Area		Metropolitan Region		Great Britain
Sector	**000s**	**%**	**000s**	**%**	**000s**	**%**	**%**
Manufacturing	-383	-61%	-239	-48%	-622	-55%	-39%
Other manual sectors	-147	-20%	72	18%	-75	-7%	-5%
Business services	450	59%	335	125%	784	76%	77%
Health, education and government	-24	-3%	58	16%	34	3%	25%
Consumer services	211	38%	172	66%	383	47%	43%
Total	**108**	**3%**	**397**	**22%**	**505**	**10%**	**11%**

Source NOMIS database
Notes 1. Data relate to employees only, and are expressed as full-time equivalent jobs
2. Other manual sectors include extraction, energy, construction, transport and wholesaling; business services includes finance, IT, and other business services; consumer services includes retail, catering and other community, social and personal activities
3. The Outer Metropolitan Area, defined by central government in the 1960s, is a belt about 25 miles wide, stretching to Stevenage in the north, Reading in the west, Crawley/Gatwick in the south and Medway/Southend in the east

Figure 2.2
Average Weekly Earnings of Men and Women Full-Time Workers
Greater London relative to Great Britain (1970-2003)



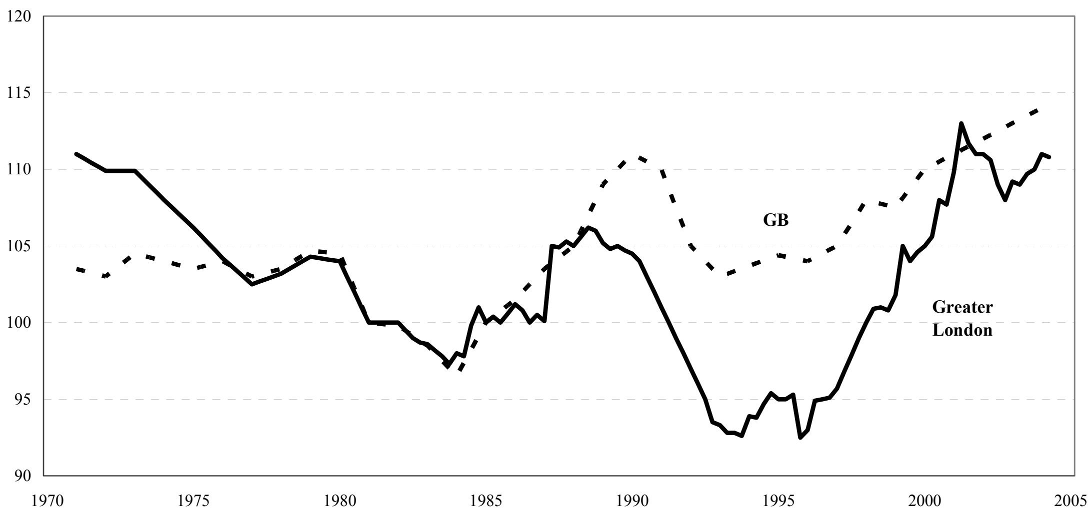
Several new factors also came into play:

- A sharp upward movement in London earnings levels relative to those in the rest of GB during the period of economic deregulation (and generally widening earnings inequalities) between 1979 and 1990. Subsequently this trend to divergence slowed, but it continues to operate for men (Figure 2.2)
- A faster rate of growth in service employment, particularly in business services, halted the strong downward trend in London employment evident during the 1960s and 1970s (Figure 2.3). In terms of employment fluctuations, London passed from being the least cyclically sensitive regional economy to being the most unstable during the 1980s and 1990s

Spring 1981=100

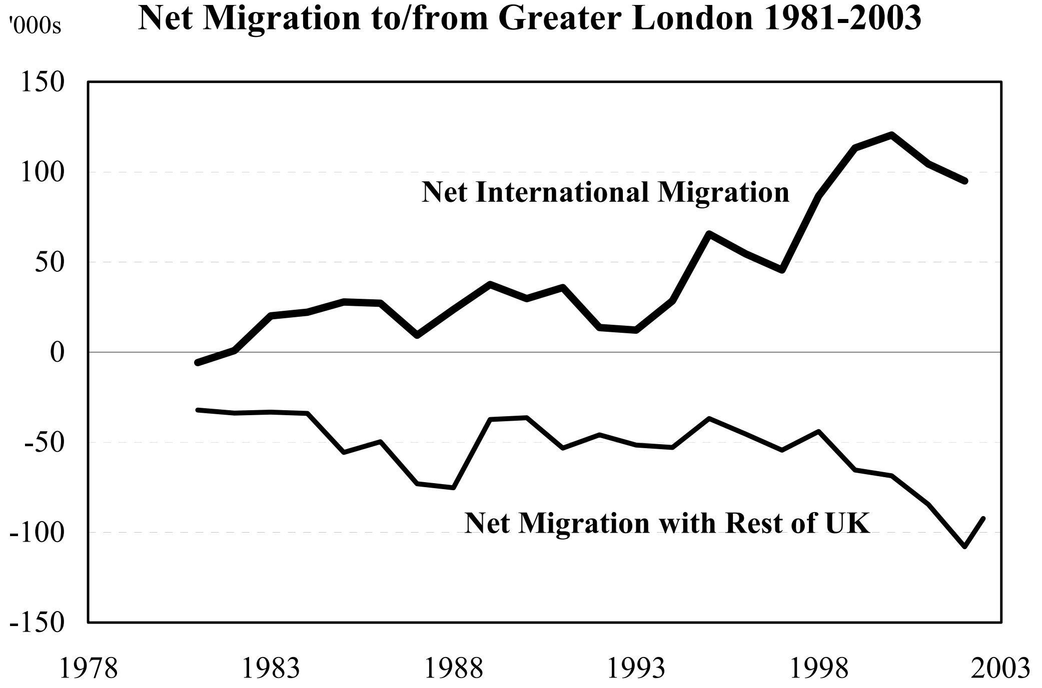
Spring 1981=100

Figure 2.3
Trends in Total employment (full-time equivalents): Greater London and GB 1971-2004



- From the late 1980s, with a second strong boost in the late 1990s, the overall balance of migration into London was reversed through substantial increases in the rate of immigration from overseas. Net gains from overseas migration came significantly to exceed the continuing net losses to the rest of the UK, although recently these too have grown substantially. One element in this new inflow is drawn from other high wage economies, notably in the EU, much of which is apparently short term, responding to cyclical developments in the London economy, but the greater part is from poorer countries, which is less obviously temporary and includes, in particular, asylum seekers for whom London is clearly the destination of choice within the UK

Figure 2.4
Net Migration to/from Greater London 1981-2003



- In the years 1991-1994, the net inflow into London from overseas averaged 29,000 per year; by the years 1998-2002 it was averaging 104,000 per year (Figure 2.4). This inflow, mostly of young adults, is the key element in the recent expansion of the city's resident workforce, though strong overall population growth, reflecting the fact that a younger London population is now generating above-average rates of natural increase, in contrast to past patterns, is also of importance.

2.3 Trends over the Latest Business Cycle 1990-2002

Over the current cycle, employment in London has grown, and exceeded the national growth rate, unlike the previous 1980-1990 cycle when there was a slight fall, following national trends. On the other hand, productivity has been growing faster in London but less dramatically than in the previous cycle.

London's positive performance reflects its specialisation in activities with above average growth rates nationally. An important new factor has been strong job growth in some consumer services.

The graph of overall employment trends (Figure 2.3 above) shows both how much more volatile the London economy has become since the early 1980s – absolutely and relative to the rest of the country – and that the timing of its up- and down-swings closely reflects those in the national economy. To some extent this may be because London is actually 'driving' the rest of the economy. Mostly, however, it reflects the fact that, despite its distinctive role, London is highly integrated with the UK economy as a whole, susceptible to national macroeconomic influences and with a very strong stake in the economic health of other regions, (as *London's Linkages with the Rest of the UK* by Oxford Economic Forecasting, May 2004, confirms).

To obtain a balanced picture of London's performance, and that of particular sectors within it, we need to look across whole macro-economic cycles. At the present time this involves some second-guessing as to where the economy may next be heading, but the indications are that 2002 (the last year for which reasonably full economic data for London are available, from the Annual Business Inquiry) was a little past the cyclical peak of employment. In terms of the margin by which employment had fallen back from the peak, the closest comparisons in the last two economic cycles would seem to be with 1981 and 1990.

During the more recent of these cycles, there were less significant shifts in relative earnings levels than in the previous decade (Figure 2.2 above), making employment changes a reasonably reliable indicator of relative growth rates, and more so than published GDP series which are not directly computed on a workplace basis. Over the course of the whole cycle, from 1990 to 2002, London's employment grew significantly, increasing its share of national employment. This was in some contrast to the previous 1980-1990 cycle (Table 2.2 below), but even more strikingly in contrast to earlier periods, when London's share had steadily reduced (Figure 2.3 above).

Judging quite how strong London's growth has been over this cycle – and hence what the underlying trend might be – is complicated, not only because of the question of an appropriate period against which to measure change, but also because of inconsistencies between different sources of employment data. As we noted last year, the published employment series (the Annual Business Inquiry (ABI) based on surveys of employers) implies both a substantially higher level of employment in London – by a margin of some 500,000 jobs in 2002 - and a higher share of national employment than does the Labour Force Survey (LFS).

In the last two economic cycles, when national employment growth was rather consistent, both sources agree that Greater London moved from a position of virtual stability during the 1980s cycle to significant employment growth in the 1990s cycle.

The recently published 2001 Census estimates of employment by area of workplace (which, like the LFS but unlike the ABI, are based on responses from workers) basically corroborate the LFS, suggesting that the ABI may have substantially over-estimated London employment levels (perhaps because some non-London workers are attributed to their company headquarters in the city). This could also have important implications for assessments of employment change since, as Urwin (2003) pointed out, the LFS implies a much less steep increase in London employment during the upswing of the late 1990s.

Rather than the addition of over 750,000 jobs as indicated by the published series, the LFS points to a more modest expansion of around 450,000 during the boom. Over a period closer to the length of the current cycle, workplace-based comparisons can only be made with data from the Population Census, which indicates a growth of about 400,000 between 1991 and 2001 (when allowance is made for the acknowledged 2001 Census undercounts in Westminster, Wandsworth and

Southwark) compared to about 500,000 from the ABI. This suggests that the longer-term trend rate of growth in London employment is closer to published employment figures than those for the boom period alone.

Table 2.2
Civilian Employment % changes 1980-1990 and 1990-2002 Cycles
Greater London and GB

	1980-1990	1990-2002
Greater London	-3%	+11%
Great Britain	+7%	+7%

Source NOMIS (based mainly on ABI/Census of Employment data)
Notes 1. Total civilian employment here is defined as the civilian workforce, including the self-employed and (small numbers of) government funded trainees as well as employees (as in Figure 2.2)
2. Changes are based on full-time equivalent numbers, with two part-timers treated as equivalent to one full-time worker
3. All figures are as at September.

Within this picture of modest growth over the cycle, there were still large differences between sectors. These are indicated in Table 2.3, although the data there cover a slightly longer period starting in 1989, and have other inconsistencies with the total employment series by, for example, excluding the self-employed, all of which lead to less positive figures for London employment change. Over the last cycle there have again been large reductions in London employment within the production sectors, totalling some 180,000 full time equivalent (FTE) jobs. These losses were, however, outweighed by gains of more than double that number in service activities. The sector pattern of gains and losses broadly reflected that in the national economy, with a high proportion of growth in non-financial business services (law, accounting, IT and 'other business services'), but with substantial increases also in hotels and catering, and other consumer services. In financial services, London showed no net growth in employment over the cycle as a whole.

Most London service industries, public or private, have grown in employment terms over this period. The notable exception has been government (that is, public administration), reflecting the continuing impact of privatisation, deregulation and restraints on public expenditure. Within manufacturing, only the paper, printing and publishing sector managed to achieve stability in employment levels, essentially because publishing activities have become dominant within this sector in London, and now operate more like a service industry than any other branch of manufacturing.

London has clearly benefited, even more than in the past, from structural changes which have tilted its employment structure strongly toward sectors where jobs are growing across the country as a whole. Paradoxically, within this structural advantage, the tendency has been for almost all sectors to have less positive employment trends within London than they do in the rest of country. This pattern was actually less clear-cut over the last cycle, when two sectors – hotels and catering, and law and accountancy – grew more strongly in London than elsewhere, and contraction was slower in the paper, printing and publishing sector. Where London clearly fell behind were in the other production industries, a couple of predominantly public sectors - government and health - and in the information and communications technology (ICT) group.

ICT was actually the third-fastest growing sector in London, but it still grew more slowly there not only than in other southern regions with established strengths in these activities, but also than in much of the north. This may reflect the maturing of these industries, with a dispersal of the more routine elements within them.

The relatively strong performance of the London hotels and catering sector which contributed substantially to the city's overall performance in the last cycle, arises in part from the faster growth of London's spending power. Increased overseas migration into the city also provides a more elastic labour supply for the sector. Taken everything together however, but for its favourable sector mix, London employment would actually have fallen by 5%, rather than expanded by 4% during this economic cycle.

Table 2.3
Employment Change by Sector: Greater London and Great Britain 1989-2002

Sector	Absolute change (000s FTE)		% change	
	GL	GB	GL	GB
Hotels and Catering	76	265	49%	28%
Other Business Services	166	735	39%	43%
IT, R&D, telecoms	40	358	32%	82%
Education	43	381	25%	29%
Other Community	17	164	24%	46%
Recreation and Culture	29	132	24%	31%
Law, accounting	17	34	15%	9%
Retail distribution	27	311	10%	18%
Health	17	478	7%	29%
Air transport	2	19	5%	20%
Wholesale distribution	-3	89	-1%	6%
Financial services	-14	-41	-4%	-4%
Other transport	-8	77	-4%	8%
Paper, printing, publishing	-8	-44	-9%	-10%
Construction	-18	19	-12%	2%
Agriculture, mining	-2	-134	-24%	-33%
Government	-75	-167	-29%	-12%
Other manufacturing	-81	-602	-50%	-28%
Engineering	-75	-559	-57%	-29%
Utilities	-21	-88	-74%	-41%
Total	**130**	**1,423**	**4%**	**7%**

Notes 1. Sector change estimates are based on splicing together series before and after 1991 based respectively on the 1980 and 1992 Standard Industrial Classifications
2. Full-time equivalent (FTE) employment estimates treat two part-time jobs as equivalent to one full-time one

Employment growth is not the only criterion of competitive success at an urban scale – productivity levels (signalled by relative earnings levels or GDP per head) and export performance, which is discussed below, are both relevant. In London's case, relatively slower growth even in advanced activities may simply reflect a natural tendency to transfer routine activities to cheaper locations when and wherever possible. This is not a matter for concern for as long as the markets for London's core activities continue to grow and these activities maintain a competitive edge in terms of their ability to anticipate and respond to new, more specialised and more exigent sources of demand.

2.4 Standards of Living in London

On average, taking costs and earnings together, the standard of living of the average full-time worker is perhaps 11%-12% higher in London than it is elsewhere in the country.

Average figures do not, however, reflect the great variations between groups and particularly the difficulties that newly forming or newly arriving households have in paying for adequate housing.

As we have seen, money earnings for those working in London clearly tend to be well above the national average by a margin that has grown in the past 25 years. In April 2003, the New Earnings Survey (NES) reported average weekly earnings of £604 for full-time workers living in London, 27% above the national average. This simple percentage figure can, however, be quite misleading for several reasons:

- the cost of living is significantly higher in London than elsewhere
- the make-up of the city's workforce in terms of skills and occupations is quite different
- not all groups reap the same earnings advantage, or face the same cost penalties, from being in London
- a substantial minority who are not in work face many of the higher costs without any earnings advantage

Within the average occupational group distinguished by the NES, average earnings in London were just 18% higher, differences in mix therefore accounting for the other 9% of the overall earnings gap. In some occupations, such as corporate managers and business professionals, the earnings differential was much wider - around 29%, more than double the typical 13% margin among groups of manual and service workers. As discussed in section 2.5, unemployment and inactivity rates among Londoners are significantly above the national average (reflecting unfavourable aspects of the population mix), and at the time of the 2001 Census, 22% of working age heads of London households were not actually in work.[1]

[1] Note that this figure includes students, the retired, family carers and the sick as well as other inactive people. The actual unemployed share was 4.4%.

The cost of living in London relative to the rest of the country depends both on how prices differ across regions and also on how households respond to those differentials by changing the quantities they purchase. Both higher prices and the consequent adjustment in quantities imply lower standards of living for a given level of earnings.

After its first partial set of estimates for 2000, which were discussed in our 2002 report, the Office of National Statistics (ONS) has recently produced a full set of regional estimates for relative consumer price levels in 2003 (Gall and Fenwick, 2004).[2] They provide both an indication of relative prices, using national weights for the mix of products purchased, and also one using regional weights, which reflect both differences in tastes and the tendency of people to consume less of commodities which are relatively expensive in their region. The figures suggest that using national weights Londoners face prices which are 7.6% above the national average (and 17.6% above the North East regional average where prices are lowest). Using regional weights appears to increase the measured differential, with a gap of 20.4% on this basis compared with the North East.[3]

There are some goods and services that are relatively cheap in London compared to the rest of the country, notably fares and other travel costs and, to a lesser extent, fuel and light. However, the vast majority of goods and services are rather more expensive in London than elsewhere.

The main source of price differentials is, of course, the cost of housing. On the measures used by the ONS, the average cost of housing is recorded as 24% above the national average[4] and 65% above the level in the North East, although only 1% above prices in the South East. These differentials, although greater than for other commodities, are far lower than those for average house prices, which on a mix-

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[2] This updates and improves the earlier exercise conducted in 2000 which covered only some of the elements that make up household expenditure. The most important improvements are that the 2003 analysis now covers transport costs and, of particular relevance, owner-occupied housing costs. Even so the reassessment is not fully up-to-date, nor does it take all the differences into account. However, it certainly addresses the most important differentials. It will also, from now on, be updated on a regular basis, starting in Autumn 2004 in line with the government's commitment to publish regional indices and to take more account of regional and local conditions in determining public sector pay.

[3] Compared with the country as a whole the gap appears to narrow, but this just reflects an oddity of these calculations which lower the relative price indices for all regions!

[4] This appears to reduce to 19% when more weight is given to the types of housing expenditure that Londoners actually incur, though again the use of regional weights appears to lower relative prices everywhere.

adjusted basis were 52% above the UK average in 2003. They are also considerably lower than the estimates of imputed rents which we have used in the last two reports. There are important differences in methodology, with the ONS measure following the example of the national RPI and focusing on a mix of direct expenditure in terms of rents, mortgage costs and depreciation. In absolute terms these vary less than prices, since most home-owners have not bought their properties recently on 100% mortgages, but it is not yet clear why the ONS approach yields so much smaller a percentage differential between regions.

In terms of overall standards of living there are three important caveats:

- no allowance is made for capital gains which are higher, especially in absolute terms, in London then elsewhere
- conversely, differences in quality are not taken into account – and Londoners on average buy smaller dwellings and a higher proportion of flats than elsewhere in the country; and thus get less for their money
- these costs are averages and do not reflect the differential problems faced by new entrants nor how individual renters fare as compared to owners (or, indeed, the extent to which potential purchasers are excluded from the market)

Evidence from surveys of social tenants and the Council of Mortgage Lenders (Dataspring, 2003) in terms of rents and mortgage costs point to differentials ranging from 20% for Housing Association tenants (£72 per week in London against an English average of £60), through 30% for local authority tenants (£64 against £49) up to over 85% for new owners of the cheapest quartile of houses (£191 versus £103 for England). These variations can lead to quite substantial differences in the relative cost of living, with new entrants to owner-occupation and lower-paid groups without access to social housing facing substantially higher costs.

2.5 Labour Market, Skills and Education

London's labour market is flexible and robust. It is also very open to commuting and benefits considerably from inward migration. On the other hand, the city continues to have higher levels of unemployment and non-participation in the labour force.

The labour force in London is particularly skilled by UK standards with a third of all workers in the market having degree-level qualifications.

London's labour market is one of its key economic assets, offering uniquely large pools of specialised labour for employers and opportunities for workers, flexibility in adjusting to shifting patterns of demand and supply, and an escalator of upward occupational mobility for those with talent and ambition. The type of work found in London, coupled with easy mobility between jobs, facilitates skill development and provides much of the sophisticated human capital on which advanced activities depend. The city is not self-sufficient in terms of talent, however, and much of its skilled labour force was initially trained in other regions or abroad. In this respect, London might be seen as providing both important opportunities for advancement of young people from other regions (and countries) and also a reverse flow of able mid-career workers filling managerial and professional roles in the provinces.

The inflow of talent is sometimes seen as a brain drain, contributing, as well as responding, to an increasing concentration of higher-status jobs and functions within London and the extended London region. In this context, the effective London economy extends well beyond the boundaries of Greater London, encompassing most of South Eastern England, and perhaps some areas beyond, in what is for many purposes a single labour market. The effective integration of labour markets across this broad area rests not simply on the fact that a minority of people (mostly in higher status jobs) is prepared to commute across large parts of it – since many ordinary London workers still operate within localised travel to work areas – but more on the density of overlap between such areas across the metropolitan region. The effect is that shocks, in the form of job gains or job losses, in one locality can produce a chain of effects rippling rapidly across the wider region.

As well as economic integration, this can also promote a social differentiation of areas since workers are not tied to one locality and can choose areas of residence on the basis of a (varying) combination of purchasing power for accommodation and lifestyle preferences. One consequence is that Greater London, taken on its own, exhibits attributes (for example, levels of unemployment, or rates of GCSE success) which are not representative of the region as a whole, but which reflect distinctive characteristics of those who either choose to live further in or are constrained from moving further out.

Historically, it has been the lower-status population groups that have been concentrated in inner areas, with the more affluent, particularly families, gradually moving further out in search of (affordable) space and lower densities. As we noted last year in reporting on social change data from the 2001 Census, this pattern has changed quite radically over the past twenty years, with a larger population of young professionals being attracted to live or remain in the inner areas, which are now characterised by a mix of high-status employed residents, often childless, and poorer families, including many with the attributes least desired by employers. By late 2003, according to the Labour Force Survey, 31% of all those working in London had degree-level qualifications (compared with 18% in the rest of the country and 22% in London ten years previously) a share which rose to 44% among 25-30 year olds.

One aspect of the London labour market which seems to have changed rather little over the past couple of decades is the scale of net commuting into Greater London. The 1981 Census recorded an excess of inward over outward commuting of some 518,000; by 1991, the balance was 523,000; by 2001, it was just 487,000. This impression of relative stability may be misleading, however. First, there is indirect evidence (from labour market accounts) of large short-term swings during the 1980s' boom and bust (Gordon, 1996). Secondly, both inward and outward movements have actually shown strong growth over the past 20 years or so, increasing the openness of the London labour market. At the time of the 1981 Census, just 111,000 Londoners worked outside the capital but by the end of last year, the LFS reported that some 300,000, or 9% of all working Londoners, now did so compared to the 18% of London jobs filled by inward commuters.

Another respect in which the London labour market has become increasingly distinctive over the past decade is the high proportion of foreign-born workers, who comprised 27% of its workforce in late 2003 (LFS) compared to 5% in the rest of the country, and 18% in the city ten years earlier. Proportionately they were most important in the hotels and catering sector, where they accounted for 63% of workers, though the sector actually employs only a small proportion (8%) of all foreign-born workers, the rest being spread across the full range of occupations and industries. Foreigners are more heavily represented in lower level occupations (42% of those in elementary occupations compared to 25% of professionals, managers and associate professionals), although typically they have spent more time in education (with a median age of 19 for completion of full-time education, against 18 for home-born Londoners).

A third of the working migrants had been in the UK for 25 years or more, while another third had arrived since 1995. The size of the latter group reflects both rising immigration during the 1990s and the presence of many who only plan to stay in London (or the UK) for a few years. The most recent arrivals include many well-educated younger people from continental Europe, the Old Commonwealth, and the United States. The International Passenger Survey indicates that the majority of such immigrants expect to stay only one or two years. Despite this element of turnover, the proportion of foreign-born workers in London has increased by five percentage points over the past ten years.

A substantial factor in the overall increase in immigration to London has been the group formally identified as 'asylum seekers and visitor switchers' who accounted for 42,000 of the 95,000 net migrants into the city in 2002 (ONS, MN29, 2004) down from a peak of 75,000 out of 122,000 net migrants in 2000 (ONS, MN27, 2002) reached before the introduction of the government's dispersal policy. The impact of these immigrants on the London labour market is not at all clear, although among those adults in London who arrived from the main origin countries for asylum seekers from 1990 onwards, the LFS records that fewer than 25% were in work at the end of 2003 (against about 50% among those from other Third World countries and 75% among those from advanced economies). The speed with which this group can be integrated into the labour market appears critical to the projected substantial expansion of the city's labour supply included in the London Plan.

London's enhanced success in terms of employment and earnings growth over the last cycle has not been matched in terms of either employment or unemployment rates. In 1990 the city's unemployment rate of 6.7% of the economically active population was in line with ILO-definition national average while the employment rate of 75.4% of all 16-60 year olds was also close so the national average of 75.7%. However, by autumn 2002, and at a similar point in the economic cycle, the national unemployment rate of 5.3% was significantly lower than it had been in 1990 whereas in London the rate was actually slightly higher at 7.0%.

For employment, the contrast was even clearer, with the national rate rising to 76.7% over this period, while the London rate fell significantly, to 70.9%. In part this contrast reflects some narrowing of the employment gap between north and south, and in part the fact that labour supply as well as demand in London has been rising, with an increase of about half a million in the city's working age population over the period. It must, however, also reflect a further worsening of the competitive position of some of those particular population groups who remain concentrated within (inner) London. Generally, tighter labour markets tend to improve access to mainstream jobs, but reintegrating those who were marginalised in the recessions of the early 1980s and 1990s is an important and continuing challenge for both supply-side and equal opportunities policies in London.

2.6 Housing in London

There is great pressure on housing supply in London, with less growth in dwellings than in household numbers since 1991. Owner-occupation has grown slowly, but the size of the social housing sector has been substantially reduced, placing much more emphasis on private renting for poorer families.

House prices in London are particularly volatile, with the largest rises in the country during the recent boom following the largest falls during the preceding recession. Low interest rates have kept first-year costs of purchasing in London below those in the last boom. Low inflation, on the other hand, means that the burden of payments will last longer.

The latest post-Census evidence confirms that the regional balance between households and dwellings is at its tightest in London and that the position has worsened significantly since 1991 (Holmans, 2004). This is both because of increases in demand and need, arising from net immigration and particularly from indigenous change, and also because the total stock has increased more slowly in London – up by 7% since 1991 compared to 9% in England.

The tenure structure in London remains very different from the rest of the country notably with respect to the relative and growing importance of the private rented sector. In 2003, 16% of London's stock was officially defined as privately rented compared to 10% across England. In the city, the sector has grown by three percentage points since 1991 (indeed, probably by more as the statistics are particularly difficult to update) while in the rest of the country the proportion has held relatively stable.

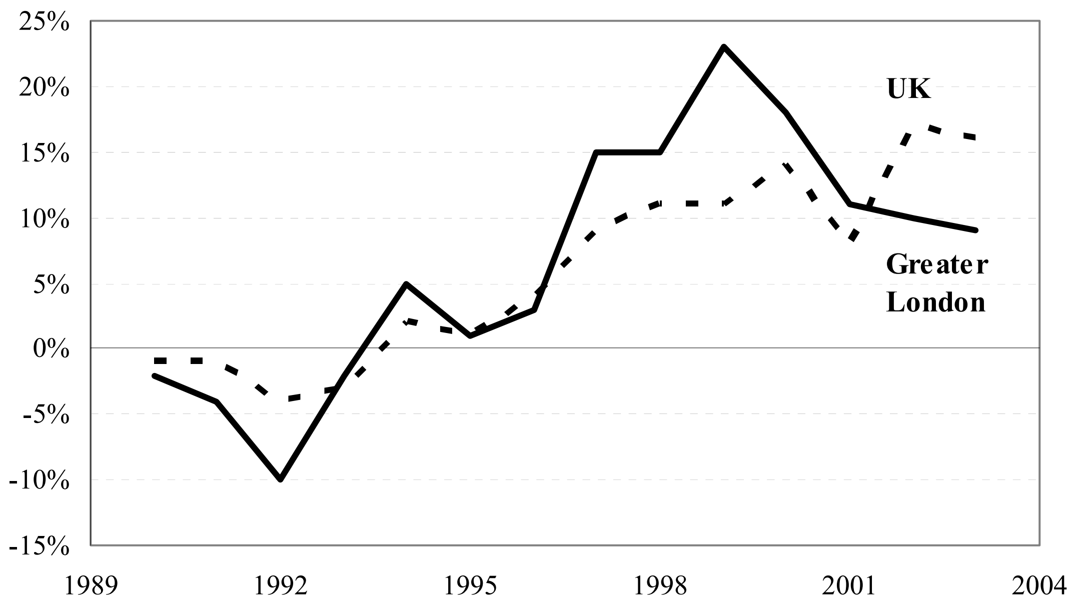
London's social rented sector is also relatively large at 24% of the stock in 2003, comparable only to the North East with 26% and well above the UK average of 19%. The proportionate decline in the social sector since 1991 has been very similar to the rest of the country but in absolute terms it is clearly more important.

As a consequence, London's owner-occupied sector share of 59% is well below the UK figure of 71%. Moreover the rate of increase has also been slower, up by just two percentage points since 1991 (with a slight dip in the early 1990s) as compared to four points overall. This mix of tenure has important implications for the efficient operation of London both because of the high proportions of Londoners outside the labour force and also because of the incentive for family households to move elsewhere.

House prices

House prices have been a central subject for discussion throughout the last decade (and longer) initially because of the relative declines experienced in London during the recession of the late 1980s which, in housing terms, hit bottom in 1993 (Figure 2.5). Since 1997, the interest has been concentrated on house price rises. In London, the annual increase in the mix-adjusted price index peaked at 23% in 1999 and has since been falling, becoming negative in the second half of 2004 on some measures.

Figure 2.5
YOY % change in mix-adjusted House Price Indices
1989-2004



Source: ODPM/Council of Mortgage Lenders
Note: These prices relate to the mortgage completion stage of transactions

Although the pattern of regional differentials in house prices is long established, the degree of variation between regions, as well as actual house price levels, itself varies cyclically, with a time lag as house price growth that starts in the London region diffuses through the whole system. Looking back over the five years since 1999, it is the regions geographically proximate to London and the South East that have faced the highest rises, in particular the South West, East Anglia and the East Midlands, all of which have seen rises of over 100% in the period. Over that time, all of the Northern regions had the lowest rises, followed by London, the West Midlands and the South East, and we have to go back to a ten-year period before London and indeed the South East can be seen to have the highest rates of increase and at that time the differentials were very much smaller (Table 2.4).

Table 2.4
Relative House Prices across Regions 1994-2004 (North = 100)

	1994	1999	2003	2004
East Anglia	119	130	167	152
East Midlands	110	113	136	129
Greater London	174	237	287	257
North	100	100	100	100
North West	114	106	112	108
South East	161	182	228	200
South West	129	136	193	175
Wales	106	102	112	113
West Midlands	118	123	145	135
Yorkshire and Humberside	108	104	114	111

Source: Council for Mortgage Lenders *Housing Finance,* table 9**.**

Because interest rates have fallen so rapidly over most of this decade, from a base rate of 14% in 1990 to 3.75% in March 2003, with only a relatively modest increase since to 4.75% in August 2004, the first-year costs of house purchase have not yet reached the levels of the late 1990s across the country, and have only just exceeded them in London. Taking account of income increases, the average burden is still less. The decline in inflation and interest rates are core factors in explaining the increased demand for housing during the 1990s. However, that burden will now last for many years because of low inflation, while in the early 1990s, the extent of the burden declined rapidly as money incomes rose.

2.7 Sub-Regional Variations within London and the Metropolitan Region

In contrast to earlier periods, employment growth trends in inner London are now more positive than in outer areas. There are significant east-west differences in outer London and the adjoining Outer Metropolitan Area, with growth fastest in the west and south of the capital, and the east continuing to perform more weakly. House prices in part reflect these trends.

Economic and social performance varies considerably within London, and there are also marked contrasts between the city and its regional hinterland. In social terms, both inner London and, to a lesser extent, the eastern side of the city have traditionally housed residents of lower status and purchasing power.

One familiar indicator of this is the heavy concentration of unemployment in a crescent of half a dozen inner boroughs on the eastern side of the centre. Among the fully employed, residence-based earnings measures for 2003 highlight this east-west divide, with weekly earnings of 25%-36% above the London average in Richmond, Wandsworth and Hammersmith, but 18%-30% below it in Newham, Barking and Waltham Forest (ONS, 2004) though at parliamentary constituency level, smaller concentrations of low-paid workers can also be unearthed in Brent South, and Hayes and Feltham.

This pattern of variation is strongly related to differences in housing demand and housing market opportunities, both in terms of tenure type and price, with the lowest prices being found in boroughs to the east (south of the river and/or beyond the Isle of Dogs), while the highest are in boroughs further west (mostly in the Inner West). Over the past five years, price gaps have changed, with faster increases in many of the boroughs with the lowest prices though the rankings, as at the regional level, have changed little (Table 2.5).

Of significance however is that the two boroughs with the highest absolute house prices – Kensington and Chelsea, and Westminster - also had well above-average increases. Equally, the prices of terraced houses in the two boroughs have risen much faster than those of flats and maisonettes, reflecting increasing differentiation at the top of the market.

Table 2.5
How the boroughs have fared: House price indices 1999-2004 vs average (1999 prices indexed to 100)

Below-average (163-195)	Average (195-200)	Above-average (201-280)
Harrow	Hackney	Newham
Lambeth	Greenwich	Waltham Forest
Sutton	Ealing	Barking & Dagenham
Hounslow	Havering	Kensington & Chelsea
Southwark	Kingston-upon-Thames	Lewisham
Camden	Barnet	Redbridge
Islington	Enfield	City of Westminster
Hammersmith & Fulham	Merton	Wandsworth
Richmond		Haringey
Tower Hamlets		Brent
City of London		Bromley
		Bexley
		Croydon
		Hillingdon

Source: Land Registry (www.landreg.gov.uk)
Note: ranked highest to lowest**,** price changes expressed as indices (1999=100)

Of the eight boroughs where prices in 1999 were lowest with average prices below £100,000, six had well above-average increases (though seven of them are still at the bottom of the league table with house prices under £200,000). At the top, the five boroughs with averages over £200,000 in 1999 are still those with the highest prices. These geographical contrasts reflect different processes of change at the two ends of the London housing market. At the bottom, the increasing pressure to enter the market is responsible for faster price rises, while at the very top, luxury end, widening income and wealth differences within London are producing a similar effect.

In economic terms, the inner-outer dimension involves a trade-off between accessibility and pressure on employment space, with higher productivity tending to be achieved in inner areas, but higher growth further out. The east-west divide, on the other hand, particularly reflects the fact that newer industries have established themselves on the western side, where more of the relevant skills are to be found and where there is better accessibility to both national markets and international airports. In terms of productivity and growth, performance has tended to be weaker in the eastern areas (which is also the case for other indicators of competitiveness such as exporting). This east-west divide is also evident in areas beyond the Greater London border in the Outer Metropolitan Area (OMA).

Recently published workplace tables from the 2001 Census, together with comparable data from the 1991 Census, provide the most reliable picture of the recent geography of employment change across the region.[6] Unfortunately the period covers less than a whole economic cycle, with a bias toward the boom years yielding growth rates above the long-term trend. Even so the strong pattern of differential change evident from these data is clear (Table 2.6).

[6] These figures do not incorporate any adjustments for the upward revisions which ONS have recently accepted to be necessary for the Westminster, Wandsworth and Southwark resident populations. Because of large commuting flows into and across these areas the impact of these revisions on borough-level employment change estimates by workplace is likely to be modest. They will also be small relative to the substantial discrepancies which have emerged between Census and ABI estimates of workplaces by borough for 2001, where we take the Census figures to be more reliable.

Table 2.6
Sub-regional Employment Changes 1991-2001

Strongest Change	% change	Weakest Change	% change
Tower Hamlets	48%	**Barking and Dagenham**	-10%
City of London	26%	**Brent**	-9%
Islington	21%	**Greenwich**	-5%
Hillingdon	18%	**Hackney**	-5%
Westminster	16%	**Haringey**	-4%
Hammersmith and Fulham	16%	**Waltham Forest**	-4%
Camden	12%	**Croydon**	-4%

Sub-Region	Employment Change by Workplace 1991-2001		Employment Change by Residence 1991-2001		Change in Commuting Balance
	000s	**%**	**000s**	**%**	**000s**
Centre	136	20%	9	11%	127
Inner West	39	6%	86	15%	-47
Inner East	78	10%	143	20%	-66
Inner London	**253**	**12%**	**239**	**17%**	**14**
Outer West	37	7%	37	7%	0
Outer South	24	5%	58	10%	-34
Outer East	5	2%	23	5%	-17
Outer London	**67**	**5%**	**117**	**7%**	**-51**
Greater London	**319**	**9%**	**356**	**12%**	**-37**
OMA West	77	15%	51	9%	26
OMA South	142	27%	115	19%	27
OMA North	62	11%	51	8%	11
OMA Essex	41	11%	33	7%	8
OMA Kent	37	11%	27	7%	11
Outer Metro Area	**359**	**15%**	**276**	**11%**	**83**

Source: 1991 and 2001 Population Census: all 2001 figures from National Tables; 1991 residence figures from SAS tables, combined with net commuting figures from SWS tables.
Note: The Centre here includes the Cities of London and Westminster, with the Inner West comprising the remainder of the standard sub-region; for coverage of the OMA see Table 2.1; OMA West includes districts from Berks, Bucks and Hants; OMA South includes all of Surrey and districts from West Sussex; OMA North includes all of Herts and districts from Beds; OMA Essex and OMA Kent include districts from the named counties.

The most striking feature is the extraordinarily rapid growth of Tower Hamlets employment over the decade, reflecting the success of the Docklands development in establishing a large offshoot of the City in Canary Wharf. Above-average growth rates were common across the whole of the extended Central Business District running from Hammersmith in the west to the Isle of Dogs in the east, and north into parts of Islington. The single outpost of rapid growth outside this area was in Hillingdon, around Heathrow, which is London’s secondary growth pole.

At the other end, Barking and Dagenham in the far east and Brent in the inner west showed significant employment declines over the decade reflecting the impact of job losses at Fords and in Park Royal, respectively. The common factor among almost all of the declining areas seems simply to be their retention into the 1990s of a significant manufacturing base, itself exposed to further decline during the decade.

Growth in the OMA ring outside Greater London over the 1990s was close to the London average, although the long-term trend has been for more rapid growth. On a residential basis, the growth in the number of people in work was actually as fast within Greater London – and clearly faster in Inner London - than in the OMA, against past experience. In part this reflects a welcome reintegration into the labour market of some of those marginalized during the recession years before 1981, but it also reflects the impact of migration on the young, economically active, population of inner London. In percentage (though not in absolute) terms, growth in the number of employed residents seems to have run ahead of numbers working in the area over these years, so that, in contrast to the experience of the1980s, large growth in inner London jobs was accomplished without much of an increase in net inward commuting. In outer London, net outward commuting did rise, with an increased outflow to the OMA where workplace growth substantially exceeded residence growth. The OMA also seems to have drawn in more commuters from the Outer South East.

London's relation with surrounding areas, both in the OMA and further afield in the Greater South East (stretching out to Cambridge, Northampton and Swindon) has become increasingly complex. In the OMA, the most obvious link is with the spending power brought in by London commuters, but both here and further out there are now concentrations of advanced activities, including company headquarters and industries with stronger records on innovation than many within Greater London, and these now form an integral part of the effective London region.

The qualitative links are difficult to show (though see OEF, 2004 for some evidence on these), whereas the income transfers associated with commuting are more easily quantified. Table 2.7 uses Labour Force Survey data on the earnings and residence of London workers to translate official estimates for GDP by industry for 2001 (the latest available) from a residence to a workplace basis. The basic assumption is that within particular sectors in London, GDP is proportionately related to employment incomes.

Thus, for example, if within construction, total earnings of those working in London are 20% higher than the total earnings of those resident in London (as is the case in the LFS sample) a conversion ratio of 1.20 is used to adjust the residence-based construction industry GDP estimate to reflect likely levels of output from London workplaces. This adjustment allows both for the scale of net commuting into London by workers in a particular sector and the extent to which inward commuters include more of the higher earners. The main results underline the contribution of the London economy to national output in financial and business services, and also in 'other services' (including entertainment and culture). The difference between residence and workplace estimates also suggests the extent to which London activities (particularly financial services) contribute to personal incomes in areas in the commuter belt.

In net terms, the gap between these estimates represents about 20% of London GDP, reasonably consistent with New Earnings Survey evidence that the wage-bill in 2002 for full-time London workers was 23% lower on a residence than a workplace basis (ONS, 2003). However, these estimates are a balance between inward and outward flows, and in terms of gross movements and the contribution which in-commuters make to the value of London's output, the share would be 25%-30%.

Table 2.7
Residence and Workplace-based estimates of London GDP by sector 2001[7]

	London			UK
Sectors	**Workplace-to-residence conversion ratio**	**Residence-based (£bn)**	**Workplace-based (£bn)**	**(£bn)**
Manufacturing	1.14	£14.6bn	£16.7bn	£151.6bn
Construction	1.49	£6.1bn	£9.1bn	£50.2bn
Wholesale and retail	1.21	£17.1bn	£20.7bn	£110.0bn
Hotels and restaurants	0.97	£6.0bn	£5.8bn	£29.5bn
Transport, storage, communications	1.27	£15.3bn	£19.4bn	£72.5bn
Financial intermediation	1.34	£15.7bn	£21.1bn	£48.5bn
Business services	1.13	£50.8bn	£57.6bn	£208.9bn
Public admin and defence	1.50	£4.9bn	£7.4bn	£44.8bn
Education	1.16	£7.4bn	£8.6bn	£51.9bn
Health and social work	1.08	£8.0bn	£8.6bn	£58.2bn
Other services	1.24	£11.6bn	£14.4bn	£45.1bn
Total	**1.21**	**£140.8bn**	**£169.9bn**	**£860.1bn**

Source: Workplace-based GDP estimates are 'headline' figures from ONS Regional Accounts (April 2004 revision); workplace-residence conversion based on data from the Quarterly Labour Force survey.
Notes: Total figures also include extractive and energy industries and the financial intermediation adjustment

Overall therefore the economic geography of London and its surrounding region is becoming more complex although underlying pressures remain much the same. Specific continuing concerns remain, including:

- The existence of some locations within London which are poorly served both in terms of space availability and physical accessibility
- The troubles faced by some particular groups within the London population who occupy a poor competitive position in the labour market, in terms of individual characteristics and past experiences

[7] 2001 is the latest year for which official disaggregated sector figures are available. In July 2004 the ONS published residence and workplace total figures for 2002 of £146.9bn and £167.3bn respectively. However, it should be noted that the latter figure is not directly comparable with the 2001 estimate shown in Table 2.6 which has been calculated on a sector basis.

3 London 2003-2004: The Most Recent Evidence on Change

3.1 Levels of Economic Activity

After a modest downturn in 2002-2003, the London economy has shown some recovery in the last year. Business service employment has stabilised and is showing signs of growth while in the rest of the London economy, demand has been sustained by a combination of major construction projects, credit-based consumption (as at the end of the 1980s) and population growth.

The London economy continues to demonstrate greater volatility than the national economy as a whole, but the fluctuations of the past couple of years have left it pretty much where it stood in 2001, facing neither the onset of a real bust nor a return to the boom path of the later 1990s. As we have already noted, there are substantial differences between employer- and employee-based sources of data, both in relation to London's share of national employment and to the scale of job growth during the boom years. However, both sources agree that London employment peaked at some point in 2001, falling significantly in the following year, but then recovering during the most recent twelve-month period for which we have data.

Average London earnings continued to increase absolutely and relative to the national average, associated with real output increases in each of the last two years, growing at below the national average in the first year, but probably above it in the second. Indications that it has been sustained by consumption, credit and house price bubbles continue to accumulate, but the simple fact is that four years of conjecture about this (since the stock market downturn of 2000) have been weathered with only a wobble in employment levels. Meanwhile, a number of forward-looking indicators suggest greater optimism than was evident a year ago.

Among the hard indicators, we attach most reliability to the Labour Force Survey (LFS) and the New Earnings Survey (NES), despite the margins of error associated with their sample bases. The most recent NES results, which relate to April 2003, showed slower growth in London earnings than in the country as a whole over the preceding year or, to take a slightly longer-term view, a continuation of the levelling off in the London differential after a significant upward step in 1998-1999 (see Figure 2.2 in chapter 2). The latest available LFS figures, which are about nine months more recent and cover the quarter from December 2003 to February 2004, point to a recovery in London employment levels over the previous year (when they had fallen), alongside continuing growth in population and labour supply (Table 3.1). This recent upturn coincided with an acceleration of national GDP growth, which moved from below to above the notional capacity growth rate of 2.5% p.a.

Table 3.1
Estimated Population and Activity changes in Greater London between Fourth Quarters of 2002 and 2003

	Change in 000s	% Change
Residents		
Total population	+ 49	+1%
Working Age Population	+ 35	+1%
Employees	-22	-1%
Self-employed	+49	+10%
ILO unemployed	-4	-2%
Economically inactive	-6	-0%
Working in London		
Total	+42	+1%
Central London	+28	+3%
Construction	+36	+17%
Financial Services	+13	+4%
Business Services	+23	+3%
Other Services	-22	-1%

Source: Quarterly Labour Force Survey; December-February quarter

Despite the reversal of employment changes, actual unemployment (on the International Labour Office definition) has hardly changed, with the slight increase of the previous year replaced by a small reduction in numbers (Table 3.1). The rate of employment growth in London was in line with the national average, and a little above that in the rest of the South East standard region. One effect has been to boost net commuting into London (reversing the previous year's downturn), though outward commuting from London has continued to grow. Employment among London residents grew rather faster than in the previous year entirely, it would seem, due to an upsurge in self-employment. The other part of the explanation is that inactivity within the working age population has continued to grow, principally among family carers and students.

Central London experienced significant employment growth after two years of decline, reflecting both a partial recovery of the business service sector and also strong growth in construction. According to the LFS these increases were offset by significant falls in other private services, preponderantly in Outer London, and not matched in other parts of the country. The short-term employment series tells a slightly different story, attributing recovery to a combination of construction and public services. Growth of construction employment on any scale is an unusual feature at this time in the economic cycle, and presumably reflects the major projects currently underway, rather than general levels of investor confidence. Inconsistent indications as to which other sectors have contributed to the apparent overall bounce-back also make it hard to infer much about the nature of change during this past year.

One new factor operating in Central London during the year was the Congestion Charge which came into force in February 2003. This might have been expected to displace some consumer service demand away from the central zone to other centres within London and the OMA (with a possible cost in lost scale economies), while potentially improving the competitive position of business services with customers who are more time- than price-sensitive. Disentangling the impact of the charge from other influences on business is not simple, even in the case of retail sales, which were affected around the same time by several other shocks (notably the Central Line closure, expectations of war in Iraq, the SARS impact on overseas visitor numbers).

A priori it seems unlikely that the negative effects on the retail sector could be large, since only 6% of all shoppers in central London use a car (Carmel, 2004). However, the one substantial piece of statistical research with real data offers convincing evidence in relation to one major Oxford Street department store that the charge has been responsible for a fall of around 5%-8% in the value of sales (Bell *et al.,* 2004). Survey evidence from the store suggested not only a general drop in shopping frequency but a proportion of customers switching purchases of large items to stores outside the city. If this response is affecting a range of other stores, however, no impact on employment levels is yet evident.

3.2 Commercial Property Markets

The commercial property market in London appears healthier than it did at the same time last year. However, increases in activity are from very low levels, and the revival is not secure. Central London, especially the West End, is leading the upturn in the office market but London is lagging behind other regions in terms of demand, new starts and occupancy rates for both retail and industrial property.

Compared to last year, the UK property market has been relatively buoyant, although recovery is slow and demand has not yet had a major impact on office construction levels (though there has been significant work elsewhere, such as Terminal 5 at Heathrow). Activity is rising most strongly in the office sector, but it should be stressed that the rise is from a very low base. After declining since 2000, rents are showing signs of increasing in some regions – notably in the North - and stabilising across the country. The IPD index shows a significant increase in total returns over the last year from 10% to 16% making it the top asset class, led by the retail sector where there is significant capital growth. More generally, there appears to be greater confidence, although this may not survive if there were to be (even more) large increases in the price of oil or continued increases in interest rates.

Central London, and London more generally, is leading the growth in take-up in the office market. It is estimated that just under 3m sq ft were taken up in central London in the second quarter of 2004 and that take-up has been increasing since the last quarter of 2003. Confidence is also at its highest in central London. There is some evidence that floor-space availability has begun to fall, although the trend is certainly not robust and overall availability in central London remains at over 27m sq ft compared to around 7m sq ft at the end of 2000. Moreover, starts and completions are still falling although at a slower pace than over the previous year. In other words, it is a picture where the optimists are starting to feel that the worst is over but one where that optimism could be easily reversed if economic conditions changed.

Looking within central London, the West End market appears the strongest with a range of new tenants from both private and public sectors. Prime rents are rising slowly and stabilising in much of the rest of the market. The City has also seen an upturn in take-up but from a quite narrow range of tenants, and availability has fallen only in the core area. The South Bank is seen as having a two-tier market with appeal across a range of tenants. The market in Docklands, on the other hand, is rather quiet and there is no evidence of rental increases.

Rents in London range from a peak £75 per sq ft in some of the most attractive West End locations to an average of around £47 in the City and down to as little as £25 per sq ft in some of the fringe areas of the City and the lower tier in the South Bank (these last are comparable to rents in Birmingham and Manchester). As always, headline rents may not take account of short-term concessions although there is evidence that slightly fewer of these are now on offer.

The office market in the South East does not yet show the same signs of picking up as in central London. Rather, demand looks firmest in the North East and North West, as do expectations of rent increases. Increases in starts are also concentrated in these regions as well as in the West Midlands and the South West.

There has been a gradual recovery in the retail market across the country over the last year. Retail demand has shown particularly strong increases in the South East, reflecting the buoyancy of sales, especially in higher income areas. Here it is undoubtedly London and, in particular, central London that is lagging. Many retailers in the Congestion Charge Zone have blamed poor sales and lack of confidence on the charge. However, there are plenty of other reasons to explain the problem, notably reductions in tourism and difficulties with the London Underground. Floorspace availability is still rising, especially in central London, bucking the increasing occupancy trend in most of the rest of the country. Retail starts and completions are both falling, although at a slower paces than last year. Confidence is also being affected by the plans for further large retail centres in the Thames Gateway. In the South East, on the other hand, starts have risen by 10% over the last year.

There is evidence of expanding manufacturing output and distribution demand, but this has not yet been reflected in the industrial property market. Activity rates are stable or falling and confidence, particularly in London, has also declined. Rents are expected to do no more than maintain their current levels. Not surprisingly both starts and completions have fallen more in London than elsewhere in the country.

Thus most of the changes in the commercial property market in London over the last year have been in the form of increased take-up with very little movement in rents and continuing declines in construction activity across all sectors.

3.3 Residential Property Markets

House prices have remained a key concern both in the region and nationally, in part because the growth in prices and the consumer borrowing that they underpin, are seen as unsustainable.

Output levels have finally started to respond to increasing demand perhaps exactly at the time when a downturn in demand seems likely. Social sector output remains low, and there are increasing problems of homelessness.

House prices

London house prices did continue to rise between the first quarters of 2003 and 2004, but by just 10.3%, making it the region with the second-lowest increase, ahead only of the South East. However, London's average house prices remain by far the highest in the UK, almost 30% above the South East average and around 160% higher than the North, which has the lowest prices (Table 3.2).

Looking at the patterns of increases over the last year, it is clear that the highest increases over the last year have been concentrated in low-priced regions, notably the North, Yorkshire and Humberside, Wales and the North West, the four regions with the lowest absolute house prices. Almost none of these relative increases has actually been large enough to change the ordering of regions, with the exception that the position in Wales has improved significantly compared to the North West. The house price gap between regions, which rose fairly consistently from the late 1990s to 2003, has been significantly reduced in 2004, however, reflecting a pattern that is generally observed over the economic cycle.

Table 3.2
Regional house price increases over one-year and five-year periods

	Average price 2004		% change 2003-2004		% change 1999-2004	
	£000s	**Rank**	%	**Rank**	**%**	**Rank**
Greater London	£262	1	10.3%	9	95	7
South East	£204	2	8.0%	10	97	5
South West	£179	3	12.3%	7	117	1
East Anglia	£155	4	12.0%	8	110	2
West Midlands	£137	5	14.3%	6	96	6
East Midlands	£132	6	17.2%	5	106	3
Wales	£115	7	23.6%	1	98	4
Yorks & Humber	£113	8	20.1%	3	91	8
North West	£111	9	20.0%	4	83	9
North	£102	10	23.5%	2	80	10

Source: CML/ODPM
Note: all figures and comparisons relate to the first quarter of the year

Within London, there are considerable differences between local markets. Prices in the most expensive areas have risen relatively slowly as have those for detached houses so the overall pattern is one of convergence but from a position of very large differentials.

New Building in London

Provisional estimates for 2003-2004 suggest that annual output rose to over 18,900 units, from a low of 12,500 in 1999-2000, an increase of 20% over the previous year and a building rate 10% higher than in 1990-1991, the peak of the last economic cycle. Only the South East, with around 25,000 units, is building more than London.

Of particular concern to policy makers, however, is the small proportion of the London output that is built for the social sector. At less than 4,000, it accounts for under 20% of the total, and is not surprisingly mainly concentrated in outer London boroughs. Once acquisitions are included, the proposed number of new social housing units rises to nearly 8,000 against which Right to Buy (running at over 10,000 units in 2001-2002 although likely to fall in the future), demolitions and other losses have to be offset. Overall, therefore, it is almost certain that London's social stock is still actually decreasing both in proportionate and absolute terms.

Of growing importance is the proportion of affordable housing provided through planning policy. S106 agreements accounted for fewer than 1,000 units in 1999-2000 but are expected to rise to nearly 4,000 units (25% of the England total) in 2003-2004, reflecting the enormous emphasis placed on this type of approach in the London Plan. There are, however, growing concerns about the mix of dwellings being produced with its increasing emphasis on small units and the difficulties of achieving family homes within the current grant and planning regime (ALG ST, 2004).

Evidence of Housing Pressure

The number of homeless households living in temporary accommodation in London at the beginning of 2004 was over 57,200, or 61% of the England total. The number of households accepted by boroughs in London as unintentionally homeless is still running at nearly 30,000 annually, around one quarter of the England total.

The annual number of social lettings is around 35,000, of which over 50% are going to homeless households. London's capacity to accommodate other households in priority need, particularly households that are severely overcrowded (a further 60,000 households) let alone those adequately housed in physical terms but unable to afford their accommodation, shows no signs of improvement. Of particular importance in this context is the extent to which both homelessness and overcrowding problems are concentrated among BME households, accounting for over 50% of all priority cases in London as a whole and up to 80% in boroughs such as Hackney (ALG ST, 2004).

3.4 Back on Track?

Recent evidence of revival in London employment growth provides only limited guidance as to what is happening to longer-term trends, largely because of inconsistencies in the available data sources.

Our interest in discussing recent developments is not so much to second-guess what might happen over the next year or two, but more to see what new evidence is offered by these developments about the longer-term situation. This may often not be a great deal, both because short-term shocks or cyclical swings tend to involve influences that are less salient in the long run, and also because the amount and quality of data on recent economic developments are rather limited.

The key issue in monitoring developments over the last three years has been to see whether they bear out the view that the late 1990s expansion of the London economy (and particularly of employment) was in large part another short-term boom, comparable with that of the late 1980s, or whether it pointed the way to a new and faster growth path for the city. Realistically, this would not be a matter of continuing or resuming the kind of growth rates enjoyed between 1995 and 2001, since those took up a lot of slack capacity in firms and the labour market that is no longer available. It is firstly a question of whether the economy can now move along a sustainable long-term growth path, retaining a stable and high level of employment of resources, and avoiding further bust and boom sequences - all of which may be a tall order, given the volatility of the last twenty years. Secondly, it is a question of whether we can expect this sustainable path to involve a faster rate of employment growth than was achieved over the 1980s cycle because London is now a fully post-industrial economy in an era in which cities generally are resurgent.

The last couple of years have not been very helpful in resolving these questions. One reason for this is the tension between quite stable aggregate behaviour, with a rapid correction to a modest downturn in jobs, and evidently unsustainable rates of growth in personal borrowing and house prices. Another reason is the continuing uncertainty about the character and significance of London's recent population growth, in terms of how many of those originally falling in the 'asylum seeker and visitor switcher' category end up in London; how far there is a direct displacement of other groups contributing to movement out of the city; and what the economic impact of new migrant groups is on consumption and the labour supply.

After the initial impact on financial services employment of stock market decline in 2000-2001, the course of change in the London economy seems largely to have paralleled national macroeconomic changes, though with apparently greater sensitivity. Expectations about the continued revival of growth in the national economy, and successful management of borrowing levels, are critical to most informed analysis and commentary on the short-medium term prospects for the London economy.

Barring a crisis in the national economy, it is reasonable to expect that the London economy should be back on track now but quite what that track is, in terms of the underlying growth rate that can be expected and what it implies for employment change, is still not clear. The average growth rate of the UK economy over the past four to five years has been close to the notional capacity growth rate of 2.5% during which time employment in London has grown by only between 1% and 4% in total, depending on which source one believes. This has included some particularly bad times for the City, however, which have undoubtedly depressed London growth.

To find an alternative benchmark period to assess London's growth track we have to go back thirteen years or so – about the span of the cycle taken as a reference in the last chapter. Over that time, annual employment growth rates seem to have averaged a bit less than 1% on the employer-based series but only about half that figure according to employee-based sources. By these standards, the last year seems to have been either at or slightly above trend rates of growth.

3.5 Recent Evidence of Change

The London economy has shown a clear bounce-back from the downturn of the previous year, with optimistic signs of further growth in the next year or two. This largely reflects national macroeconomic developments rather than factors peculiar to London.

Year-to-year developments in the London economy reflect a combination of London-specific and macroeconomic factors, often experienced in an exaggerated form (because of London's greater volatility) and in a way that is coloured by the city's post-industrial economic structure. Within the past few years, the most significant London-specific development was the downturn in the stock market in early 2000, signalling the end of the long boom (though overall London employment did not actually peak for another year). The market seems to have bottomed out early in 2003 (with the FTSE-100 index around 45% down from its peak), before moving up through the rest of that year and regaining almost a third of its lost ground. During 2004, it crabbed sideways until the beginning of October, when it finally broke out of its summer shackles. Probably the other important London-specific development over this period has been the boost to population growth provided by high rates of asylum seeker movement into London, though in this case the numbers are much less well charted – for example, in relation to how many of those dispersed from London may find their way back – and their potential impact on the city's housing and labour markets is quite unclear.

The employment downturn of the previous year and its reversal in 2003 probably owes more to the slowing and recovery of UK GDP growth than to either of these London-specific developments, just as fluctuations in overseas visitor numbers seem to owe more to exchange rates and international events and wars than to the competitive position of London as a destination. Given what has happened to London house prices, a key aspect of the macro-economic context is again the level of confidence among regional consumers that their wealth can support high levels of debt-financed consumption. Within the period considered in this report, that was still being sustained, but uncertainty is, if anything, increasing.

In general, confidence in the London economy seems to be quite high. There is evidence that service businesses are trying to economise on their cost base, not as a panic measure but in order to cope with reduced margins and/or secure their competitive position for the next upturn. This seems notably to be the case in financial services. One aspect of cost-cutting activities in the sector has been consideration of off-shoring routine activities to India or other locations offering supplies of cheap and quite highly skilled office labour.

Extrapolating from US experience in finance as well as IT (where much work to counter the Y2K bug was off-shored), as well as the prospect of 80%-90% labour cost reductions, radical projections have been made of both the number of financial service jobs liable to be off-shored and the higher level functions to which the process might be extended. So far, however, the actual number of British financial service jobs moved is limited, there is little evidence of plans to move higher grade non-IT work offshore, and the indications are that the jobs most at risk are those in back-office functions that were moved out of London some time ago in previous waves of post-boom cost-cutting.

More generally, it is clear that the London economy is now operating in an environment which may be post-boom but which is clearly not in a bust phase yet. Ironically the avoidance thus far of any substantial downturn in the London economy is itself the cause of substantial uncertainty about what comes next. These are essentially doubts about the short-medium term, however, and quite disconnected from longer term issues about the city's competitive position, vis-à-vis other British or international cities, and its own hinterland across southern England.

4 The Competitive Position of the London Economy

London's competitiveness continues to depend on both specialisation and diversity. New evidence confirms that its strengths are heavily concentrated in services, its range of markets and often in foreign-owned firms.

Cities compete in a number of different markets: for inward investment, prestige projects (as in London's current Olympic bid), rich or talented residents and, most fundamentally, through their firms for a larger share of profitable product markets. In each of these they may compete in different ways, reflecting their particular strengths, as well as simply greater or less success. Overall assessment of performance must involve a combination of indicators, including at least growth, productivity and market penetration. The distinctive role of London within the UK economy can be seen particularly in terms of its pattern of sector strengths, the markets within which London businesses operate, and patterns of ownership.

4.1 Sector Strengths and Specialisations

London's strengths are concentrated in financial, professional and business services; in communications of many types; in cultural activities; in travel; and in a small number of specialist, quality-orientated manufacturing industries.

At a broad sector level, the basic fact is that over the past 40 years, Greater London has become more and more obviously a post-industrial economy. Traditional competitive strengths in many service activities have been reinforced while, in employment terms at least, manufacturing activity has increasingly been squeezed out. In many ways this has represented an exaggerated version of trends evident elsewhere in the UK economy, but its effect has been to make the structure of the London economy increasingly distinctive. One indicator of this is the contrast in the age distribution of its commercial and industrial buildings. Whereas 10% of the surviving UK inter-war factory floor-space is in London, the city has just 3% of the stock built since 1965: for offices, the corresponding proportions are 44% and 28% in space terms, or 66% and 47% in value terms. The process is continuing, with a reduction of 11% in London factory floor-space recorded between 2000 and 2003 (ODPM, n.d.). Where employment in manufacturing or other goods-handling activities does survive in London, it is often in parts of the process with lower demands for space or road transport, and more for face-to-face contact. The last London Employer Survey indicated that just 2% of London jobs were in establishments mainly involved in manufacturing production, while three-quarters of London jobs identified with 'manufacturing' in the Standard Industrial Classification were in establishments citing some other main function (typically sales, administration or service provision).

More detailed comparisons of the shares of employment in particular sectors (using 2003 LFS data) show that almost all manufacturing industries are under-represented in Greater London, while its sector strengths seem to be spread across a range of business and private consumer services (Table 4.1). Within manufacturing, the one really significant exception now is printing-related activities, which account for a third of employment in the sector (though actual printing is now a minor element). The remaining specialisation is publishing in most of its forms, notably books, periodicals, and sound and video-recordings (though less so newspapers), where the core activities are information-handling services, closely integrated with the city's other media, knowledge and cultural service activities. The fashion clothing trade provides a smaller example of specialisation within manufacturing, but here too the majority of jobs are in establishments not directly involved in production. Conversely, most of London's surviving production jobs are in activities where the city does not have a particular specialisation or evident competitive advantage.

Almost all service activities are over-represented in the city, showing the breadth of its competitive advantage as a service centre. However, many locally-orientated activities have a slightly below-average share of employment within London, since commuters purchase many of these in their home areas.

Three other significant instances are worth noting. Both the accommodation element of the tourist industry and higher education (HE) are less heavily represented than might be expected from the visible presence of so many tourists and foreign students. In both cases, London has only an average share of employment, and it is likely that space costs are a significant consideration. In tourism, London has a very strong international sector, but only a modest amount of domestic tourism involving stays in the capital's expensive hotels. In the case of HE, it is not simply market demand and responses to high living costs, but also public policy, which locates the activity outside the capital. The effect is that, despite some institutions of global status, there is a net outflow of students away from London to universities elsewhere (though this is more than matched by inflow after graduation).

The third case is government, where a combination of decentralisation, privatisation, and the creation of arms length agencies has substantially reduced the concentration of central government employment over the last 25 years. Since 1997, numbers in London have grown significantly, but its share of civil service employment has continued to fall (C.O., 2004b). Space costs have again been among the motives, although the Lyons (2004) review of the scope for relocation of public sector jobs out of the South East emphasises a combination of regional balance and staff cost concerns.

Areas of particular strength within the service sector emerge from the listing in Table 4.1 which covers those groups of industries where London accounts for more than 25% of national activity. Activity levels are represented by jobs, though this may understate the value of London's share. In some cases, where London has specialist strengths within a broad group (such as banks, law, or accountancy) which cannot be disaggregated, the shares of national employment do not do them justice. However, their combined significance is seen in the final column, which represents the extent to which London employment in a sector exceeds what would be expected in relation to its population (that is, the excess over what is required simply to serve local demands).

Five broad groupings of specialist sectors show up: finance; other business services; representation/governance; media/culture; and transportation. This division is arbitrary, since there are various strong links between sectors in different groups. For example, advertising and fashion might be seen as being linked to the cultural industries, while the travel industries could be grouped with hotels in a tourism category (were hotels to appear in this list). It does, however, convey something of the range of activities within which London has an array of specialist strengths reflecting real competitive advantage.

Table 4.1
Specialist Strengths of the London Economy 2003:
Activity Groups in which London accounted for greater than 25% of National Employment

	London employment		Excess of employment over population share
	'000s	**% of GB**	**'000s**
Financial Services			
Banks and central banking	151	30%	89
Financial markets, security broking/dealing and fund management	33	56%	26
Trusts, and financial leasing	43	67%	35
Property, Professions, IT and Other Business Services			
Real estate, management and development	54	25%	28
Law	85	29%	43
Market research, data bases, consultancy and social research	73	32%	45
Advertising	38	46%	27
Representation and Governance			
Employers, professional and political organisations	9	27	5
Foreign Affairs and extra-territorial organisations	13	62	10
Media, Creative and Cultural Services			
Radio and TV	48	52%	37
Artistic and literary: creation and facilities	43	33%	27
Publishing: books, journals and pictures	50	40%	35
News agencies	20	50%	9
Sound publishing/reproduction and recording media	3	29%	1
Film/video production, distribution	19	52%	14
Fashion: women's outerwear, hats and leather	9	35%	6
Jewellery, clocks and watches	3	34%	2
Travel and Distribution			
Air transport and cargo handling	45	40%	31
Rail transport, bus and transport rental	64	27%	43

Source: Labour Force Survey (average of March-May and December-February quarters); original comparisons are based on 4 digit SIC categories, which have been grouped for presentation here, with labels reflecting the particular activities in which London had a more than 25% share, while keeping separate activities with distinctively high proportions in London.

4.2 Market Areas and Export Orientation

London's businesses serve a wide range of markets with a sizeable global sector, notably in financial services, supplying markets beyond Europe and North America.

London's overall share of export sales is around the national UK average though in all of its particular specialist service sectors, export performance is much stronger than elsewhere in the UK.

The London economy is diverse in terms of its geographical markets. In the last two reports, this has been documented with evidence from the 2002 London Employer Survey (LES) on the main markets served by London business and service establishments, and from the 2003 London Business Survey on the share of exports in their sales. These surveys showed that the largest part of the purchasing power brought into the region from outside came from the UK national market. However, there are no reliable data series on regional exports of goods and services[8] which can provide direct evidence on the comparative success of London businesses in export markets as compared with those in other parts of the UK.

Microdata on trade questions which are very close in form to those asked in the London surveys used in the last two *London's Place* reports and which have only recently been released from the 2001 Employer Skills Survey for England, provide a basis for reasonable comparison. These new data allow separate analyses for each of the English regions of the main markets and export shares reported by firms. With some assumptions and complementary evidence from national input-output tables and regional accounts, these data can also provide the basis for regional comparisons of estimated export shares within the manufacturing and service sectors.

[8] Customs and Excise do now publish regionally disaggregated tables of *goods* exports and imports derived from their records, but there is evidence that London trade is much exaggerated through a misattribution of flows to traders' headquarters.

The survey data confirm the significance of London's specialisation in globally-orientated services, with a 46% share of national employment in service activities with main markets beyond the EU. In our estimates (Table 4.2) this is reflected in a well above-average share of exports in service sector sales (11% compared with 6%-7% in the other two Greater South East (GSE) regions and 3%-5% in other parts of England). Even so, London seems to have the lowest proportion of exports in sales of goods, well behind the South East which ranks first for exports of goods (and second for exports of services). Indeed, London's export rate is below average in all goods-producing sectors other than paper/printing/publishing. On the other hand, it is clearly above average in all service activities, except for computing/R&D, where it falls well behind not only the South East but also the West Midlands and the North East. Combining exports of goods and of services, differences in the export intensity of the English regions seem rather small, with London being average and the highest export rate apparently being found in the North East.

Table 4.2
Estimates of Exports as a Proportion of Sales by England Region 2000-2001

Government Office Region	Goods	Services	Goods and Services
London	15%	11%	12%
South East	26%	7%	13%
Eastern	22%	6%	12%
East Midlands	18%	3%	11%
West Midlands	19%	5%	12%
North West	19%	4%	11%
Yorkshire & Humberside	21%	3%	13%
North East	23%	5%	15%
England	21%	7%	12%

Sources: estimated from establishment level responses to a question about exports as a proportion of sales in the Employers' Skill Survey (Hogarth *et al.,* 2001) combined with sectoral data on exports, sales and net output from the UK Input-Output Tables, 2001, and regional/sectoral data on net output per head from UK regional accounts.

4.3 Ownership

Foreign-owned businesses are an important element of the London economy and are a particularly strong source of international exports.

London businesses are less likely to be branches of UK companies headquartered elsewhere but more likely to be overseas-owned. Results from the 2001 Employers Skills Survey (Hogarth *et al.,* 2001) indicate that 16% of London employment was in businesses which were partly or wholly foreign-owned, above the 13% average for England as a whole, and higher than in any other region. Even more than in the rest of the country these firms tend to be export-orientated, and they account for 36% of London jobs in firms with main markets outside the UK. To a far greater extent than UK-owned businesses, foreign-owned firms are in London because of the advantages which it offers as a location from which to carry out international transactions, monitor intelligence about the global economy, and serve international markets.

4.4 London's Competitiveness

On most indicators, London's output performance is at least above average. In terms of inputs, the city appears to be able to attract the skills it requires but is only average in terms of fixed capital formation.

The two most straightforward indicators that London's competitive position is quite healthy are that, over the past ten to twenty years, it has managed to achieve a level of employment growth around the national average, alongside above-average productivity and earnings growth, and above-average export growth rates in those sectors in which it specialises. It is not unique in these respects, and other parts of the Greater South East also show strong performance on these criteria.

On the more subjective indicators provided by firms in the Employer Skills Survey (Hogarth *et al.,* 2001) London firms appear only average in their rating of the relative quality of their product and/or service and the degree to which they lead the way in developing new products, materials or techniques, even though they were least inclined to see their sales as price-dependent, and more than others (except those in the South East) to regard their market as high quality.

On the input side, in relation to attraction of talent, the position seems clear cut – London is the destination of choice for well qualified and ambitious young people from both the rest of the UK and abroad. In terms of investment, the position is less obvious. The city's record on inward investment looks weak in manufacturing (just 4% of 'project successes' recorded by Invest-UK 1998-2003) but strong in other sectors (31% of completed projects over this period, though employment levels in these are low[9]). More generally, on fixed capital formation, London's overall share of the UK total (18.5% in 2000) is very close to its share of GDP, with sector variations also paralleling the city's output share, though greater than expected in hotels and catering but lower in finance and dwellings (Cope and Flanagan, 2003).

[9] With 150-200 projects in 2003-2004 expected to produce just 2,572 jobs.

5. Public Expenditure and Taxation in London

5.1 Expenditure, Taxation and the Regions

A range of recent studies has all confirmed that London continues to contribute substantial net resources to the Exchequer. This figure is calculated as tax less expenditure.

London's capacity to use its own tax resources to provide the public services it requires is heavily circumscribed by the centralised nature of the United Kingdom's public finance system. In common with other parts of the UK, London's local and regional governments can raise a single locally-determined revenue – the council tax - plus a number of small charges for services. In 2002-2003, council tax was just 4.2% of all government receipts (HM Treasury, 2003, Table C8) meaning that the other 95.8% of taxation and other revenues was determined by central government.

The implication of this centralisation of tax-raising power is straightforward: central government is responsible for the overwhelming proportion of resource allocations to all levels of government. Such allocations can either be direct, for example, in the decision to spend public money on defence equipment or on farming subsidies. Other allocations are made using distribution formulae, and income from the national non-domestic rate is distributed on the basis of population, for example. The implication of this top-down allocation process is clear: even a city as large and important as London must bid for the resources it needs to Whitehall departments.

The total paid by London taxpayers is the amount that the national tax system extracts from the residents and businesses within the capital. This total is to some extent incidental since different taxes will tend to raise more or less from London. Stamp Duty (paid on property transfers) will raise disproportionately large amounts in London because of the high property values in the city. On the other hand, vehicle excise duty payments will be lower than the national average because car ownership and use are relatively low in London.

The exercise this publication has undertaken in each recent year has involved estimating the total paid in taxes within London and then comparing this sum with the government's own calculations of public expenditure for the same year. Calculations made for earlier years have been reinforced by research undertaken by GLA Economics, the economic research division of the Greater London Authority (Greater London Authority, 2004a) which has produced results very similar to those published in the *London's Place in the UK Economy* series. The Prime Minister's Strategy Unit's 2004 *London Project Report* cited the scale of the tax export as lying in the range £10-£20 bn per annum (Cabinet Office, 2004).

The Mayor of London published a submission to the government's Spending Review 2004 which stated: "Quite properly, London pays more in taxation than it receives in public expenditure (often called the capital's tax export to the rest of the UK)... Increasing spending and investment in London will not necessarily reduce this contribution. Rather it will provide the support the capital needs to continue to generate the output and activity that provides this tax export to the rest of the UK" (Greater London Authority, 2004b, p.6). This emollient approach by the Mayor stands in contrast to demands made by other commentators for the "repatriation" of London's net contribution to the rest of the country. Nevertheless, the proposition is that investment is required in London if it is to continue to generate its tax export.

As earlier *London's Place* volumes (and, more recently, GLA Economics) have argued, there is no simple way of allocating either public spending or the payment of taxation between UK regions. Public expenditure flows from the Exchequer to particular services through a number of allocation mechanisms, including the so-called Barnett formula (which maintains a balance in public spending between England, Wales, Scotland and Northern Ireland) and many one-off payments. The allocation of a flow of resources to a public service within a particular region does not necessarily mean that the benefit will be enjoyed by the inhabitants of that region. Central government may allocate money, by formula, to a London university for example, while the benefit of the service thus provided is derived by a student normally resident in another part of the country.

There are significant difficulties in allocating certain forms of tax – notably company taxation – between individual regions. The question of where profits, for example, are earned has proved particularly difficult to answer, even at the national level. Indeed, while the Treasury has made efforts in recent years to provide a region-by-region analysis of public expenditure (in its *Public Expenditure Statistical Analyses* series), there had not, until recently, been a similar analysis to estimate regional tax payments or, indeed, of the balance between public spending and taxation at the regional level. The quality and proposed reform of regional statistics is further considered below.

Last year's edition of *London's Place in the UK Economy* was able to compare the results of LSE calculations with data generated by an exercise undertaken by the Office of National Statistics (ONS). In January 2003, an article appeared in the ONS publication *Economic Trends* exploring the question of "which regions have funded government and which regions have received government expenditure" – a question that has featured in a number of research projects sponsored by the Corporation of London over several years. This study (ONS, 2003), described as "experimental" and undertaken as part of a Eurostat pilot exercise, considered the allocation of virtually all taxation and most – though not all – public expenditure.

The results confirmed earlier studies that had suggested that London contributes substantial net resources to the Exchequer. The capital was shown as making a per capita contribution towards overall public expenditure greater than every other region apart from the East and the South East. In line with earlier studies, Northern Ireland, Wales, the North East, the North West, Scotland and Yorkshire & Humberside were shown as most likely to be net beneficiaries of the overall tax/spend distribution.

The ONS has not subsequently published any further work on the subject of regional taxation payments and public expenditure receipts. As a result, the overall balance between the public spending within a particular region and the tax paid by all the individuals and companies within that same region will continue to be derived from estimates.

The results of such estimation should be viewed with care for at least two reasons. Firstly, significant approximation is required. Secondly, it is very likely that there will be differences between regions in the balance between taxation paid and public expenditure in the same way as there are differences between the tax payments and the public spending benefits of individuals and households.

Such qualifications should not, however, inhibit efforts to understand the underlying dynamics of regional public finance in the United Kingdom. Work undertaken in the *London's Place in the UK Economy* series and the recent GLA Economics study to estimate tax and public expenditure flows have not been challenged. Indeed, as is explained below, the Treasury and ONS are currently engaged upon a much wider effort to improve regional statistics.

A positive or a negative balance of tax or expenditure for a particular region does not mean there is anything inherently "unfair" or wrong with the existing pattern of tax or public expenditure. However, knowledge of which regions are providing the tax resources to support other areas will throw light on the interdependence of different parts of the UK, and evidence about which regions are supporting others will also have implications for the distribution of investment resources from area to area.

5.2 Public Finances in the UK

As the government's finances have clearly gone into deficit, this has had major implications for the distribution of regional contributions.

The overall total of public expenditure and tax income in 2002-2003 is shown in Table 5.1 below.

Table 5.1
Public expenditure and income, 2002-2003, United Kingdom

	£bn
Total Managed Expenditure	£419.1bn
Public sector receipts	£396.2bn
- of which, council tax	£16.7bn

Sources: 1. HM Treasury (2004) *Budget 2004*, HC 301, Session 2003-04, London:TSO, Table C11
2. ***op cit.*** Table C8

The Government's public finances crossed the point between surplus and deficit in 2002-2003. Tax and other receipts were broadly in balance with public expenditure up to 2001-2002, but from 2002-2003 onwards there will be a significant excess of spending over taxation, requiring a return to public sector borrowing. Table 5.1 highlights the low proportion (4.2%) of public sector receipts that is derived from council tax.

5.3 Regional Allocations of Public Expenditure

Any calculation of the regional allocation of expenditure involves assumptions, but a mid-point estimate suggests that London received about £60 billion in 2002-2003 – 14.5% of total UK public spending compared with 12.4% of total UK population.

Because such a large proportion of taxation is determined centrally, the allocation of United Kingdom public expenditure is heavily driven from the centre. All expenditure on social security, the National Health Service and on many other aspects of government is wholly determined by Whitehall. Even locally-raised income – the council tax – is subject to significant prescription because Whitehall departments determine expenditure norms (Formula Spending Shares) and because of the possibility of expenditure capping. During 2004, the government decided to use selective capping against a number of local authorities.

Resources allocated to the devolved administrations in Scotland, Wales and Northern Ireland are based on the so-called Barnett formula which, from the late-1970s onwards, has determined the share of public expenditure (making allowances for population changes) given to each country within the UK. Within England, the regional share of public expenditure is determined by a number of resource allocation mechanisms for local government, health authorities, Learning and Skills Councils, the Higher Education Funding Council, and via the social security system. There is also an array of one-off and special purpose grants. Furthermore, the government announced its intention during the summer of 2004 to move to funding the whole of schools' education by means of a Whitehall-determined specific grant.

The only reasonably comprehensive source about region-by-region public expenditure is HM Treasury's annual *Public Expenditure Statistical Analyses* volume which, for 2004, has been significantly improved and refined. There are now better regional spending data than previously, covering a series of years, separately for central and local government, and for current and capital expenditure.

The Treasury is making a number of efforts to improve the quality of regional statistics. Following an Oxford University report on the measurement of public expenditure flows to the regions (ODPM, 2003) and the Allsopp Report on statistics for economic policymaking (HM Treasury, 2004b), improvements are being undertaken to the quality and timeliness of regional economic and public finance statistics. The Treasury and the ONS have published a memorandum entitled *Measuring Government Expenditure by Region* (HM Treasury 2004c), which has been followed by a further paper about proposed changes to regional public expenditure statistics from 2004 and beyond (HM Treasury, 2004c).

The question of how precisely to measure regional public expenditure has in recent years become a greater priority for government statisticians. Devolution and other regional public policy concerns have evidently driven a search for greater accuracy, timeliness and consistency in the production of official data. The outcome of these efforts to create better regional statistics will have profound implications for our understanding of the operation of regional economies. Publications such as *London's Place in the UK Economy* have long had to rely – at least in part – on data sets that are either out of date, or imprecise, or both.

Until any revision work is completed, the Treasury is likely to continue to believe there are limitations to the precision of its analysis, particularly because of the difficulty of allocating spending to reflect the benefits accruing to those living in a particular area. Nevertheless, the annual exercise has been carried out for the years up to 2002-2003 to estimate public expenditure on services. Further qualifications must also be noted, because some parts of public expenditure, for example, overseas representation, are not identifiable with a particular location within the UK. As the Treasury's data are currently the only ones available – and because they are official – there is nevertheless a strong argument for using them as the sole reliable source.

Table 5.2 shows identifiable public expenditure per head in 2002-2003 for England, Wales, Scotland and Northern Ireland, while Table 5.3 gives comparable figures for each English region.

Table 5.2
Identifiable public expenditure by country, 2002-2003

	£ per head	**£ million**
England	£5,453	£270,273m
Wales	£6,479	£18,911m
Scotland	£6,579	£33,254m
Northern Ireland	£7,267	£12,329m
United Kingdom	£5,652	£334,766m

Source: HM Treasury (2004*) Public Expenditure Statistical Analyses 2004*, Cm 6201 Table 8.1 (populations from paragraph A11 p128)

Tables 5.2 and 5.3 show that, on a broadly comparable basis, London's public expenditure per capita is about 1% below the Scottish figure, though some 15% above the England average. These figures exaggerate London's advantage over the other regions/countries because, while all of the other areas are an urban/rural mix which together forms a region, London is really the urban area at the centre of the South East (or Greater South East) region. If London were aggregated with the South East and the Eastern region, its identifiable expenditure per head in 2002-2003 would be £5,343 compared with the England average of £5,453.

Table 5.3
Identifiable public expenditure by English region 2002-2003

	£ per head	**£ million**
North East	£6,463	£16,243m
North West	£6,043	£40,914m
Yorkshire & Humberside	£5,538	£27,594m
East Midlands	£5,011	£21,124m
West Midlands	£5,374	£28,505m
South West	£4,976	£24,688m
Eastern	£4,697	£25,459m
London	**£6,522**	**£47,970m**
South East	£4,699	£37,775m
England	£5,453	£270,273m
Memo: London, East, S East	***£5,343***	***£111,204m***

Source: HM Treasury (2004) *Public Expenditure Statistical Analyses 2004*, Cm 6201, Table 8.1

The data in Tables 5.2 and 5.3 are for identifiable expenditure on services. A number of elements within overall public expenditure are excluded because they cannot be attributed to regions. In total, these non-identifiable items add up to £58 billion (14%) of the overall total expenditure (on this definition) of just over £400 billion. In addition, a further £19 billion of accounting adjustments must be added to bring the overall total of expenditure up to the Total Managed Expenditure figure in Table 5.1.

There is logic to allocating non-identifiable items and accounting adjustments to regions pro rata to identifiable expenditure (largely because it is impossible to imagine another way of making this allocation). In the overall scale of this analysis, this pro rata allocation of 14% of the total is unlikely to have a radical effect on the results but an alternative would be to assume a tolerance of between 50% above or below this allocation to reflect the possibility that some elements of public expenditure might be concentrated in particular regions (see Table 5.4).

One significant change that has been made to *Public Expenditure Statistical Analyses 2004 (PESA 2004)* is the effort to make a region-by-region attribution of a proportion of this "unallocated margin". Table 8.17 of the 2004 volume attributes a proportion of the pay costs within the "unallocated margin" between regions. Of the full margin of £58 billion, £8.3 billion (14% of the unallocated total) has been attributed in this way. London's share of these pay costs is just under a quarter of the overall total, a rather higher proportion than its share of the "allocated" total of public expenditure. In previous years, *London's Place in the UK Economy* has attributed the whole of the unallocated margin pro rata to the capital's share of the larger, allocated total. The new Treasury figures suggest that this method may have under-estimated an element within London's public expenditure figure.

In line with the practice adopted in earlier years, our calculations for 2002-2003 will continue to make the assumption that any unallocated margin that the Treasury cannot attribute in other ways will simply be attributed pro rata to all other, allocated spending. The new information provided by the Treasury about pay costs within the unallocated margin will, however, be used as the basis for the regional attribution of the relevant part of the "pay" share of the unallocated margin shown in Table 8.17 of *PESA 2004*.

Table 5.4
Public expenditure in London, 2002-2003

	£ bn
Identifiable expenditure	**£48.0bn**
- plus all unallocated items	**£11.8bn** range: £5.9-£17.7bn
Total	**£59.8bn** range: £53.9-£65.7bn

Source: see text above

Table 5.4 shows London's share of identifiable public expenditure, plus a pro rata allocation of debt interest and other government expenditure allocated in proportion to the identifiable total. For the remaining non-identifiable amount, a range is shown, from 50% below the pro rata share to 50% above.

The overall total of public expenditure in Greater London is thus likely to be in the range £53.9 billion-£65.7 billion, with a mid-point of £59.8 billion. This would represent 14.5% of all UK public spending (compared with a population share of 12.4%). Even at the lower range of the expenditure share, London would appear to receive a slightly larger share of spending than its population share alone might justify. However, given the higher costs associated with private and public sector operations in the capital, such a spending difference is unlikely to buy a disproportionate level of public services.

5.4 The Regional Tax Take

Broad estimates of the tax take from households and businesses suggest that London pays between £65 billion and £68 billion depending on the assumptions made.

Unlike the expenditure figures in Table 5.4, there are no regular or comparable (or official) region-by-region figures for tax payments including those from both residents and businesses. However, in May 2002, for the first time, the ONS did publish a regional breakdown of income tax, council tax and certain other taxes, based on 1999 figures. The results of this exercise, which has not yet been repeated for any later years, are shown in Table 5.5.

It is important to stress that the taxes paid figure in the table above applies only to income tax, council tax and taxes on vehicles. It does not include customs and excise duties or VAT. Social contributions figures include contributions made by employees, employers and the self-employed.

Table 5.5

Taxes and social contributions paid, by region, 1999

	Total taxes paid (£bn)	Total social contributions (£bn)	Total taxes paid (% of UK)	Total social contributions (% of UK)
North East	£3.36bn	£5.15bn	3.0%	3.6%
North West	£10.79bn	£14.81bn	9.5%	10.5%
Yorks & Humber	£7.65bn	£10.75bn	6.7%	7.6%
East Midlands	£7.13bn	£9.55bn	6.3%	6.7%
West Midlands	£8.58bn	£12.28bn	7.6%	8.7%
East	£11.90bn	£14.05bn	10.5%	9.9%
London	**£19.77bn**	**£22.25bn**	**17.4%**	**15.7%**
South East	£20.81bn	£21.23bn	18.3%	15.0%
South West	£8.87bn	£10.70bn	7.8%	7.6%
Wales	£3.74bn	£5.55bn	3.3%	3.9%
Scotland	£8.55bn	£12.64bn	7.5%	8.5%
Northern Ireland	£1.97bn	£3.08bn	1.7%	2.2%

Source: *Economic Trends May 2002*, Office for National Statistics, Table 5e

As Table 5.5 makes clear, London paid 17.4% of total UK income tax, council tax and vehicle tax in 1999. This total is significantly greater than either the capital's population share of 12.4% or its 14.5% share of public expenditure. The 15.7% share of social security contributions made by London is also above these figures.

Overall, these totals given in Table 5.5 represent some 70% of all tax income. The remaining 30% is accounted for by VAT, corporation tax, various customs and excise duties, Stamp Duty and a number of smaller levies. There has been no official regional breakdown for these other taxes, so it is again necessary to make assumptions about their region-by-region attribution. Allocating corporation tax and VAT between regions is not easy. However, as far as the latter is concerned, there is probably merit in assuming the amount of the tax paid in London is consistent with consumption expenditure, and ONS data for 1999 (the latest available) suggest that London took a 15.2% share of total UK consumption expenditure.

Thus, by applying the percentage figures for taxes, social contributions and VAT shown in the table and paragraphs above (still, unfortunately, for 1999) to the UK taxation totals for 2002-2003, it is possible to make a broad estimate of the overall taxes likely to have been paid in London in that year. Table 5.6 shows the results of this calculation, and a fuller explanation of the method is given in Annex 1 to the 2003 edition of *London's Place*.

Table 5.6
Taxation paid in London, 2002-2003

	£ bn	**% of UK**
Residence-based	£65.1bn	16.4%
Workplace-based	£68.7bn	17.3%

Source: see text above and LPUK 03, Annex 1

Two figures are shown. The first residence-based total is for taxation paid by Londoners resident in London. The second figure is slightly higher because it takes account of the fact that a significant number of people work in London while living outside the city. Their income tax and social security contributions can be argued to be generated in London, though other taxes such as council tax, VAT and many customs and excise duties will be attributable to home districts outside the capital. There is inevitably some heroic estimation involved in assessing the extent of workplace-based taxation paid. This study assumes that the difference between official residence- and workplace-based GDP for London is a fair and reasonable proxy for the likely extent of the difference affecting some taxes.

5.5 London's Contribution to the UK Economy

The estimates of taxation and expenditure can lead to a wide range of possible contributions, and the move into deficit of the government's finances has further implications. The best estimate of London's contribution in 2002-2003, based on the percentage point gap between its public expenditure receipts and its tax payments, and then applying this figure to total UK public expenditure, is that it was around £11 billion, though it may have been as high as £19 billion.

The range of London's net tax contribution to the rest of the UK in 2002-2003 appears to be lower than those given for earlier years. Indeed, at the extreme end of the range, it is possible that the capital received more public expenditure than it paid in taxation during that year. However, this outcome is highly unlikely as it involves using the opposite extremes of both the taxation and public expenditure estimates.

The apparent decline in London's contribution – essentially, its tax export - has occurred purely because total UK public expenditure increased significantly in 2001-2002 and 2002-2003 while taxation hardly rose. At the national level, a surplus of taxation over public spending in 2000-2001 and earlier years has now been eliminated and, indeed, a significant public sector deficit has developed in the UK. Consequently, in each UK region and constituent country, there is likely to have been an increase in expenditure with little change in the tax burden. To put it another way, all regions that have historically been net contributors to other regions have seen the level of their contributions fall while recipient regions have enjoyed an increase in the level of their net receipts. For London, the contribution, measured as the gap between public spending and taxation will have reduced in 2001-2002 and 2002-2003, and it is likely to do so again in 2003-2004.

An alternative way of measuring regional contributions, which has the benefit of giving a truer picture over time irrespective of the state of the economic cycle – at least, inasmuch as it affects government finances - is explored below. Using the estimated public expenditure and taxation figures for London from Tables 5.4 and 5.6, it is however possible to calculate the city's contribution on the basis – the method used in earlier *London's Place* reports – of the difference between taxes paid and public expenditure. Because ranges have been given for both expenditure and taxation within London, this contribution, or resource export, to the rest of the UK must also be across a range. The results are shown in Table 5.7.

Table 5.7
Difference between total public expenditure and taxes paid in London 2002-2003

	£ bn
Expenditure	£53.9bn to £65.7bn
Taxation	£65.1bn to £68.7bn
Difference	**£0.6 bn to £14.8 bn**

Source: calculated from figures in Tables 5.4 and 5.6

The alternative method of calculating London's contribution referred to above involves the construction of a measure of the net fiscal contribution that will remain robust over time, independent of shifts in the national budget between surplus and deficit. To do this, we first compare London's estimated shares of the national tax and expenditure totals. We then convert the difference between these two figures into monetary terms by calculating the extent to which expenditure in London would be higher if it received the same share of spending as it paid in taxes.

This calculation is carried through in Table 5.8 which brings together our estimates of expenditure and tax – both the mid-points and the full range of estimates. It then expresses these estimates as shares of the UK totals, and presents the differences between these shares, first in percentage and then in monetary terms. This shows, on the different assumptions already discussed, that the net fiscal transfer from London to the rest of the UK in 2002-2003 was somewhere between £3.0 billion and £18.6 billion, with a mid-point estimate of £10.8 billion. This mid-point estimate of the transfer represented about 7% of gross value added in London.

Applying the same method to estimates for the previous two years yields mid-point estimates of £14.8 billion (2000-2001) and £13.2 billion (2001-2002). The reason for this steady slide in the value of London's contribution on this basis is the net effect of a more or less constant share of tax payments on the one hand, alongside a modestly increasing share of public expenditure in London (up from 13.2% to 14.3% over the two years on the mid-point estimates).

Table 5.8
Net fiscal transfers from London to the rest of the UK
(percentage allocation approach)

[A]	**£bn**	
	Range	**Mid-point**
Taxation	£65.1bn to £68.7bn	£66.9bn
Public expenditure	£53.9bn to £65.7bn	£59.8bn
[B]	**As % share of UK total**	
	Range	**Mid-point**
Taxation	16.4% to 17.3%	16.9%
Public expenditure	12.9 % to 15.7%	14.3%
	Range	**Mid-point**
Difference between share of taxation and expenditure [derived from B above]	0.7% to 4.4%	2.6%
Difference expressed as £bn of expenditure	**£3.0bn to £18.6bn**	**£10.8bn**

Given London's higher income earners and productivity, it is not surprising there is a relatively higher tax take than the allocation of public expenditure. However, the use of resources generated in the capital to fund services in other parts of the country underlines the importance of ensuring the London economy can continue to flourish. If this capacity of the capital's economy to continue to generate a surplus were undermined, transfers of resources to other regions would be reduced and general taxation would have to increase.

5.6 Public Expenditure as a Proportion of London's Economy

What is absolutely clear is that public expenditure in London and the South East is far below the national average as a proportion of the region's economy. London has to stand on its own feet to a greater extent than the rest of the country – and even as compared to New York.

Because of the highly-centralised nature of public expenditure control in Britain, local authorities have to spend a great deal of time convincing Whitehall of the merit of their particular case for public funding. There is no "fair" level of public spending for a particular city, town or county. Current levels of area-by-area expenditure are, as argued above, the result of many decisions, formulae and interventions. There is therefore constant lobbying for additional public spending in all parts of the country. The services and infrastructure bought with public resources should, in theory at least, improve the quality of welfare services such as the NHS, education and social housing. Public expenditure is certainly needed to finance most new rail, bus and other transport services. Regeneration almost always requires public intervention to start it off. But this does not mean that all public expenditure, at every level, would be appropriate. Excessive levels of public intervention might crowd out or discourage entrepreneurial activity. On the other hand, inadequate public service funding might undermine competitiveness. There is clearly an appropriate balance for the scale of public intervention within a national, regional or local economy. Different levels of public spending might be needed at different times.

This section considers public spending in London and other UK regions within the context of the scale of the regional economy. While the population share of a region may be a plausible comparator for its share of public spending, there is also a case for considering public spending as a proportion of the economy within which it takes place. Table 5.9 shows estimated public expenditure as a share of gross value added for each UK region in 2001. It is important to note that this exercise simply compares official estimates of public spending with GVA figures: it is a relatively crude attempt to look at the scale of the public sector intervention within each regional economy.

Table 5.9
Public expenditure as a proportion of workforce GVA, 2001

	GVA £ bn	Public Expenditure £ bn	PE as % of GVA
North East	£27.7bn	£19.0bn	68%
North West	£87.6bn	£47.3bn	54%
Yorks & Humber	£61.9bn	£32.0bn	52%
East Midlands	£55.4bn	£24.6bn	44%
West Midlands	£68.8bn	£33.3bn	48%
East	£75.1bn	£28.9bn	38%
London	**£162.5bn**	**£53.7bn**	**33%**
South East	£127.4bn	£43.8bn	34%
South West	£63.6bn	£29.5bn	46%
Wales	£33.1bn	£21.4bn	64%
Scotland	£69.2bn	£39.2bn	57%
Northern Ireland	£19.1bn	£14.1bn	74%
United Kingdom	£851.4bn	£386.7bn	45%

Sources: GVA - *Regional Trends 2004 Edition*, London: TSO, Table 12.6
Public Expenditure - *Public Expenditure Statistical Analyses 2004*, London: TSO, Table 8.1 ("unallocated margin" allocated to each region pro rata to identifiable expenditure)

Public expenditure represents just 33% of London's and 34% of the South East's workplace-based GVA – well below the average equivalent figure for the United Kingdom or even the United States. In three other regions or countries, the average share of public spending within the economy is over 60%, with Northern Ireland now easily exceeding 70%. The impact of such different scales of intervention on the economy, productivity and entrepreneurship of each region to region remains un-researched.

However, the First Minister of Scotland, Jack McConnell, has conceded that the public sector in his country needs to be reduced. Speaking in June 2004, he said: "The size of Scotland's public sector, compared to the size of the private sector, is too big". He then qualified this remark by stating that there was a need to "rebalance Scotland's economy – not by shrinking the public sector, but by growing the private sector". In fact, public spending represents a smaller share of Scotland's public expenditure (56%) than in Wales (64%), the North East (68%) or Northern Ireland (74%), but the issue of whether an over-large public sector can be a problem is evidently on the political agenda.

The figures in Table 5.9 for public spending as a proportion of each regional economy are higher – for each region – than the corresponding ones for 1999 published in *London's Place in the UK Economy 2003*. Public expenditure in the UK has increased somewhat in recent years, though the analysis shown in Table 5.9 suggests that relatively faster GVA growth in London and the South East between 1999 and 2001 has ensured a smaller relative increase in the scale of the public sector in these areas than in the rest of the UK.

6. Special Topic: Crime and Policing in London

There is a growing perception that London is a city ridden by crime and anti-social behaviour, and that this is beginning to have negative impacts on the economy and well-being of the capital. However, although crime and safety is one of the aspects of living in London that causes the greatest level of concern, the extent of this concern is declining.

Crime, anti-social behaviour and fear of crime certainly rank high among the concerns of both individual Londoners and government. The perception is that London has become less desirable and less safe to live in, while fears about terrorism, especially since 9/11, are at their greatest in the city. Anti-social behaviour is felt to be blighting many London neighbourhoods, and newspaper headlines scream of steamers and violent crime on public transport.

Overall, crime rates are significantly higher in London than elsewhere in the country and Londoners are more likely to be victims, especially of violent crime. Moreover, while London certainly has a disproportionate share of policing in the country, detection rates are much lower than elsewhere.

The government has finally started to put fighting crime at the top of its list of priorities, and is taking action to increase police presence on the street, as well as introducing Anti-Social Behaviour Orders (ASBOs) to control those who make their neighbours' lives impossible. As the Prime Minister stated in the summer it is now seen to be time to mark the end of the "1960s liberal, social consensus on law and order" (19 July 2004).

However the reality is far more complex than these facts would suggest and raises many questions, such as:

- Is the situation really as bad as is perceived, – and particularly is it worse in London than elsewhere and getting even worse?
- Are the problems being addressed and how much is this costing Londoners?
- Do crime, anti-social behaviour and fear of crime truly affect decisions on whether to live, work, and invest in London and thus are there adverse impacts on the city's economy?
- Are there any pointers to what the future might hold?

This chapter attempts to answer these questions, by reviewing the current position on crime and policing and looking at implications for the future economic health of London.

6.1 The Significance of Crime for Londoners

The annual MORI poll of Londoners provides an overview of how those who live and work in the capital think about their city. The poll shows that 38% of respondents claim that crime and perceived threats to personal safety are one of the two or three worst things about living in London. However, this figure has fallen from over 50% in 2001 when the survey was first carried out and both the cost of living (47%) and traffic congestion (46%) are now seen as more problematic while affordable housing is of comparable concern (also 38%).

Even so, nearly 60% of respondents say that fear of crime is adversely affecting their quality of life, and over 50% say the same about unease over safety. These concerns are particularly strong among older people and women. Again, the figures show a decline of seven percentage points over the last year with commensurate falls in concerns about specific types of crime, such as physical attack. Addressing safety and crime is the second most important priority for improving London as a place to live, after affordable housing. It is the highest priority in many parts of London, especially those with lower house prices. On the other hand, crime and safety appear much further down the list of what has to be done to improve London as a place in which to work. So crime and safety are clear priorities for Londoners – but not to the exclusion of other issues, and levels of concern are falling quite rapidly.

6.2 Is Crime a Particular Problem in London?

Recorded crime rates of nearly 150 per 1,000 residents are more than 30% above those in the rest of the country. However offence rates are below some other metropolitan areas, and crime rates in London have stabilised over the last three years, with the incidence of many types of crime falling rapidly, though violent crime continues to increase.

London still has less than half the murder rate of New York, though London has not yet observed the very rapid falls in crime – over two-thirds in ten years - experienced in New York.

Recorded crime in London 2003-2004

Home Office crime statistics for 2003-2004 show that almost 1.1 million offences were recorded as taking place in London, of which slightly fewer than 10,000 occurred in the City (Dodd *et al.,* 2004). The overall level of recorded offences has been fairly stable over the last three years but there are wide differences between categories of crime (see Table 6.1) with robbery and burglary in particular falling significantly. Crimes aimed mainly at businesses, such as fraud and forgery, have also shown a tendency to fall, in some cases quite substantially.

What has risen is the number of violent and drug-related crimes. There has been an increase of over 15% in the last two years in total violent crimes against the person, although the major increases are concentrated among lesser offences. Grievous Bodily Harm (GBH) has fallen while murder, crimes involving an offensive weapon, and Actual Bodily Harm (ABH) have risen at well below average rates. The figures for drug-related crimes, which show an increase of 23%, are particularly difficult to interpret, as offences and arrests are more closely related than for crimes where there is more third-party reporting. The numbers therefore tend to reflect police activity as much as actual incidence.

Table 6.1
Reported Offences in London Metropolitan Police District

	2001-2002 (000s)	2002-2003 (000s)	2003-2004 (000s)	% change 2001-2004
Violence against persons	161	179	186	+15%
Robberies				
Persons	49	39	38	-24%
Business	4.1	3.5	3.2	-22%
Burglary				
Dwellings	74	72	68	-8%
Other Buildings	42	41	37	-11%
Theft and Handling	444	464	449	+1%
Fraud and Forgery	88	83	78	-11%
Criminal Damage	148	144	148	-0%
Drugs	26	33	32	+23%
Total	**1,057**	**1,081**	**1,061**	**+0%**

Source: MPS
Note: these data exclude the City of London.

Cross-borough variation in crime levels

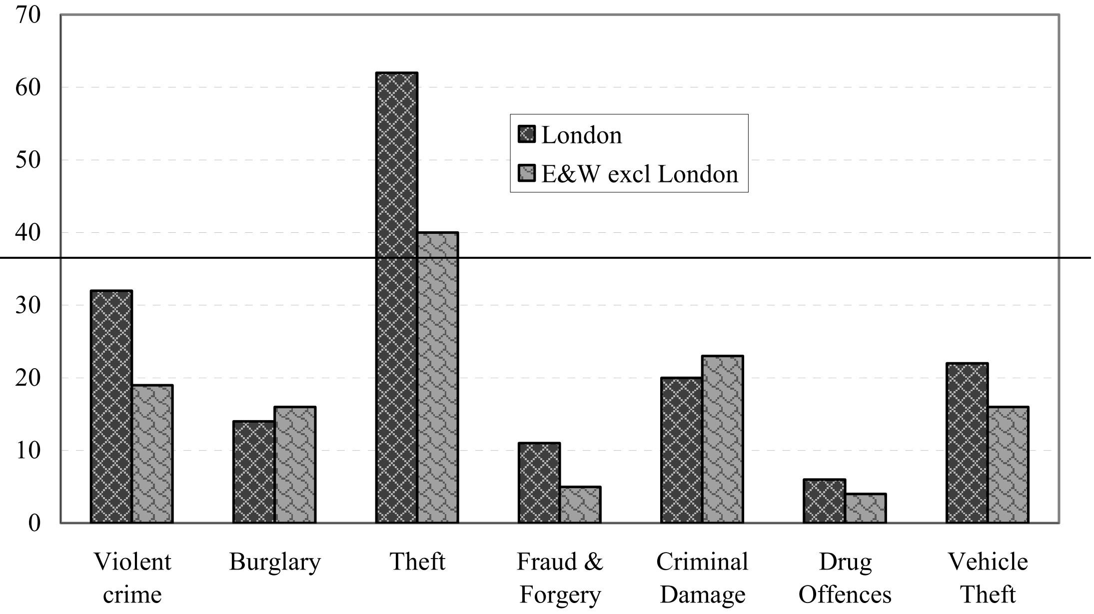
The average level of recorded offences across the Metropolitan Police District (MPD) masks great variation across boroughs. Crime rates are generally significantly higher in the inner London boroughs compared to those in outer London, especially for violent burglary and car crime, where the incidence is over one-third higher in the inner area.

Annual variations also differ greatly across boroughs. For example, although the annual decline in total recorded crime (using year-on-year averages to August 2004) was 2%, some boroughs have seen increases of more than 10% while others have had decreases of well over 5%. These variations show no clear spatial pattern.

Comparison with the rest of England and Wales

London has the highest rate of recorded crime per capita in England and Wales (Moore and Yeo, 2004). In 2003-2004, there were 145 offences per 1,000 residents in London compared with 108 in the rest of England and Wales (Figure 6.1). The offence rate in London was thus 34% higher than for the rest of the country - and almost 60% above that in the South East.

Figure 6.1
Recorded Offences per 1000 population 2003-2004



Within these totals, robbery, theft, violent and vehicle crime in London are all well above the overall average. On the other hand, London has lower levels of recorded burglary and criminal damage than England and Wales as a whole. In many ways, a more relevant comparator is with other metropolitan areas. The total number of recorded crimes in 2003-2004 per 1,000 residents in London (145) was lower than in either West Yorkshire or Greater Manchester (156 and 146 respectively) although higher than in the West Midlands and Merseyside (132 and 124 respectively). Using this index, London has a higher incidence of both violence against the person and total violent crime, but a lower incidence of burglary and criminal damage. (More details on the comparative performance of these areas can be found in HO, 2004.)

Violent crime

Looking in more detail at violent crime, which is what the press and public tend to concentrate on, we find that violence against the person was highest in London with 25 offences per 1,000 residents compared with 18 per 1,000 in England and Wales (Upso *et al,* 2004). In part, however, this reflects the large number of people coming into London for work and leisure, and does not therefore necessarily provide an accurate representation of risk for people who live in London.

Importantly, recorded violent crime is concentrated in relatively few localities across the country, one of which is London. Two-thirds of all recorded robberies took place in just five police force areas: the MPD, West Midlands, Greater Manchester, West Yorkshire, and Avon and Somerset. Furthermore, for both violence against the person and robbery, almost two-thirds of all firearms offences (excluding air weapons) occurred in just three police force areas - the MPD, Greater Manchester and West Midlands. Research conducted by the Audit Commission on behalf of the Home Office (reported April 2004) examined four types of violent behaviour in more detail: violence by a stranger; violence in a public place; violence associated with licensed premises; and violence by an individual under the influence. The data, which covered the period 2002-2003, were collected from more than 200 local authorities in England.

Table 6.2
Violence by a stranger 2002-2003: top ten England boroughs

Council	**Number of incidents per 1,000 residents**
City of London*	**67.2**
Westminster*	**53.0**
Nottingham	37.3
Tower Hamlets	**33.4**
Haringey	**25.1**
Leicester	21.8
Wandsworth	**15.8**
Weymouth	15.5
Bristol	14.1
South Kesteven	14.0

* Low resident population makes index misleading

On the face of it, the City of London has the highest number of incidents of both violence committed by individuals under the influence (21.6) and violence by a stranger (67.2) per 1,000 residents. However, these figures are misleading because of the extremely small number of residents in the City in comparison to the daily workforce and visitors. Similarly, the relatively high number of non-residents working and passing through the area distorts the figures for Westminster which has the second highest number of incidents of violence by a stranger (53.0). However, three other London – Tower Hamlets, Haringey and Wandsworth - are in the top ten for violence by a stranger (Table 6.2).

Anti-social behaviour and disorder

For most people, anti-social behaviour (ASB) is likely to have a more immediate impact on their lives than major crimes. In a recent single day count, 66,107 reports of ASB were recorded in England and Wales – one every 1.3 seconds (Home Office, 2003) - and the significance of ASB is now being increasingly recognised in government policy. Figures for London are not easy to obtain and there is little hard evidence as to whether ASB is becoming more or less of a problem. In the case of criminal damage, however, it is known that recorded levels have not increased in London over the last couple of years and are actually lower than in the rest of the country (Table 6.1).

Generally, London suffers more from ASB than elsewhere. To take one example, London is the car-dumping capital of Britain, accounting for almost two in five of all abandoned vehicles, with more than 250 cars abandoned on London's streets every day. In addition, London has the highest levels of perceived disorder with a rate that is some 50% above the rest of the country.

A rather different way of looking at the same question is that reflected in the British Crime Survey (BCS) statistics (see Dodd *et al,* 2004). This measures victimisation as reported by respondents rather than recorded offences, which depend on the extent to which the police are informed. It also locates the crime by where the victim lives rather than where the incident takes place. The results from the BCS indicate that although the prevalence of victimisation (the proportion of the population who have been victimised at least once) for household crime at 21% is in line with that for England and Wales, for personal crime, the rate for London, at 11%, is almost 60% above the England and Wales average of 7%. Incidents of property crime (burglary and vehicle crime) and violent crime as measured by the BCS in London are also above the E&W average. The difference is particularly concerning for violent crime (772 incidents per 10,000 adults in London versus 640 in England & Wales, or 618 excluding London). Within this category, the differential is especially dramatic for mugging (243 incidents per 10,000 adults in London versus 94 in England & Wales, or 70 excluding London).

Comparisons with New York City

Adverse comparisons have been made between the continuing rise in crime in London and the massive falls recorded in New York over the last decade. New York's experience is undoubtedly impressive, with total offences recorded by the police falling from not far short of half a million in the early 1990s to under 150,000 in 2003, at a time when the population was rising rapidly. Indeed, over a ten-year period, total crime was cut by almost two-thirds (Table 6.4). This decline was fairly consistent across types of crime and across the conurbation, with crime in Manhattan falling at a very similar pace to New York as a whole.

London's headline crime figures are now very much higher than those for New York. Direct comparisons in absolute terms need to be treated with care as definitions and reporting procedures differ greatly between the two cities, and London's murder rate is still less than half of that in New York, even though the latter's rate has fallen by almost 70% over the decade, while London's has continued to rise. On the other hand, violence against the person, on London definitions (which have been widened considerably over the years) is running at 25 per 1,000 residents compared to under six per 1,000 in New York (on that city's much narrower definition).

Table 6.3
New York: Crimes per 1000 population

	1993	2003	% change
Murders	0.26	0.07	-69%
Robbery	11.45	3.16	-70%
All crimes against persons	17.62	5.74	-64%
Burglary	13.46	3.56	-71%
Total	**57.39**	**17.82**	-66%
Memo: Population	*c.7.5m (1990 7.3m)*	*c.8.2m (2000 8.0m)*	+9.5%

A more valid comparison is between changes over time, and here New York clearly comes out on top. The decline over the last decade is both very large and very consistent across all categories (Table 6.3). In London, some types of crime are now falling in much the same way as in New York but for other types, notably violence against people, the picture is one of continuing increase. There is thus much less consistency in the pattern of change compared to New York. One reason given for this difference is that the impact of cocaine and crack cocaine on overall crime figures emerged much earlier in New York where measures to control the impact were put in place some years ago, while London is just catching up both in terms of the problem and the response.

6.3 Policing in London

London has 21% of the police officer strength in England and Wales compared to slightly over 14% of the population and 18% of recorded crime. Policing costs the average London household about £160 per annum, a figure that is rising rapidly.

The effectiveness of the police measured by detection rates is relatively low at around 16% compared to 25% in the rest of the country although the last three years have seen some reversal of the downward trend.

Home Office statistics (Christopherson and Lal, 2004) show that at the end of September 2003, there were 29,250 police officers in London (four per 1,000 residents) compared to a total England and Wales police strength of around 140,000 (three per 1,000 residents). London thus appears to be better policed in numbers than the rest of the country especially as the Metropolitan Police Service (MPS) also has nearly 1,500 Police Community Support Officers (PCSOs), 12,500 civilian staff, 750 voluntary constables and 500 traffic wardens.

The current total workforce of almost 45,000 is planned to rise rapidly to 60,000. However, this is not comparing like with like, since London's police service also has to cope with almost a million daily commuters as well as 30 million tourists each year. The MPS also has to address a far wider range of activities, including those related to London's role as a capital and a world city, notably state occasions and anti-terrorism activity.

In particular, London must police all state activities which can take large proportions of the total force away from their regular tasks in a predictable pattern, leaving Londoners in general more vulnerable to crime. Other events, such as the Rugby World Cup victory parade in December 2003, can have a similar impact.

The MPS takes the lead on anti-terror activity which, when the capital is on high alert as it is frequently at present, can dominate all other issues. London also leads many of the more innovative special initiatives aimed at reducing gun and drug-related crime as well as being the location of new agencies addressing serious crime, notably against serious fraud, led by the City police. The environment in which the MPS works is unique in this country when the numbers of tourists and commuters, a diverse population and an increasingly diverse police force are taken into account. (MPS/MPA, 2004).

London is policed mainly by the MPS. In addition, the City of London Police cover the area within the boundaries of the Corporation of London; the British Transport Police (BTP) are responsible for policing on rail and Underground systems; and the Royal Parks Constabulary patrol some of London's major parks. MI5, the internal security service, also contributes to the protection of national security with the deployment of intelligence officers and surveillance experts in London and across the country working with the police to tackle terrorist threats. The scale of the MPS, now at around 30,000 officers, is worth comparing to New York which has 39,100 police officers - 30% more than London - for a population that is just 11% greater.

The organisation of policing in London

Most of the day-to-day policing of London is undertaken by the 32 borough operational command units. The MPS also includes specialist groups which tackle serious and organised crime in the capital, and expert units which deal with security, protection and the investigation of certain categories of crime, including terrorism.

Governance of the MPS involves a tripartite relationship between the Home Secretary, the Metropolitan Police Authority (MPA) and the Commissioner of the Police of the Metropolis. The Home Secretary has national responsibility for policing funding, legislation and guidance. Since the implementation of the Greater London

Authority Act 1999 in July 2000, the Mayor of London and the MPA are responsible for overseeing the policing strategy. The Mayor is also responsible for setting the budget of the MPA.

The City of London Police is responsible for the Square Mile which has just over 7,000 residents but which has to manage a daily workforce, including the self-employed, of up to 350,000 as well as people travelling through the area and tourists. The City of London force has 800 officers and 400 civilian support staff.

One of the most important policing initiatives over the last few years has been the introduction of staff auxiliary to the core service, most notably PCSOs who are intended to undertake routine duties, assist officers, gather intelligence and provide public reassurance. In addition, there have also been initiatives such as neighbourhood wardens, encouraged by the ODPM and employed by local authorities in part to address issues of anti-social behaviour.

The growth of specialist units within the police force has a focus on financial crime, where the City Police are the lead force on serious fraud. This means that they are involved helping to spread good practice in cases not just within the City but also across the South East. The City Police is also training most of the 2,000 private security officers employed by City institutions on how to manage terrorism incidents. These types of initiative reflect a more diverse and sophisticated approach to policing, both supporting the reassurance agenda and providing a response to concerns about the changing nature of criminality.

The cost of policing London

The MPA, which has responsibility for financial control, recommends a budget for the MPS to the Mayor who then seeks endorsement from the GLA. Responsibility for the operation of the budget is delegated to the Commissioner of Police of the Metropolis.

The main sources of funding are a police grant, allocated by the Home Office using the police funding formula; a special payment in recognition of the MPA's role in international, national and capital city functions; income raised by non-domestic rates;

and council tax. The MPA cannot set its own council tax rate – this is decided by the GLA. There are also grants allocated for specific purposes, such as counter-terrorism.

The MPA/MPS has a gross revenue budget of £2.7bn, nearly half of which is devoted to police pay and overtime, and there is a capital budget of £163,000 mainly used for IT and data initiatives. Over 50% of funding comes from central government grants based on the national allocation formula, and London also receives £200,000 to cover national and capital functions, and a further £200,000 for special initiatives. These figures are regarded by many as quite inadequate to address the special needs of the capital.

Although the level of central funding rose by 11.4% between 2002-2003 and 2003-2004, the impact of higher costs on local tax payers was much greater than this – twice as much, in fact, with the local contribution rising by 22.8% over the period. A Band D council tax payer (the average household) now contributes £160 per annum.

The budget from the Home Office is set to rise from £17.3bn in 2004-2005 to £20.1bn in 2007-2008, but this increase will have to fund initiatives on neighbourhood policing and the Serious Organised Crime Agency as well as providing an extra £50m for counter-terrorism. To meet the agreed increases, notably in staffing, Londoners will certainly have to pay considerably more over the next few years.

Effectiveness of policing in London

Detection Rates

The overall detection rate in London is far below that of any other part of the country - 16% compared to 25% (Thomas and Feist, 2004). It is particularly poor for violence against the person where rates in London are less than half those in the rest of England and Wales. However, there has been a marginal improvement over the previous year compared to a slight decline elsewhere in the country. Even so, as can be seen from Table 6.4, it remains far below the levels of the late 1990s.

Table 6.4

Recorded crime: annual detection rates for the Metropolitan Police, City of London Police, London (including the City of London Police) and England and Wales (including and excluding London)

Police force area and region	1997-1998	1998-1999	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004
Metropolitan Police	25%	22%	16%	15%	14%	14%	15%
City of London	28%	33%	32%	27%	34%	36%	33%
London Region	25%	22%	16%	15%	14%	15%	16%
England & Wales	28%	29%	25%	24%	23%	24%	23%
England & Wales (excl London)	29%	31%	28%	27%	26%	26%	25%

Detection rates vary widely between types of crime, in part reflecting the extent to which crimes are actually recorded. Thus the detection rate for drug offences in London is 87% while that for violence against people is 26% and for criminal damage it is around 9%. Rates also vary enormously over time and between areas.

Police presence on the streets

As has already been noted, the special nature of London means that the manner in which its resources are used has to be very different from other parts of the country. As a result, the share of overall police resources used for territorial policing is considerably lower than elsewhere. The need to provide increased anti-terrorism patrols or police high-profile events likely to lead to disturbances, such as state visits by US or Chinese Presidents, regularly diverts officers from core activities.

The most important initiative taken to provide a greater "police" presence on the streets has been the introduction of PCSOs. The Chancellor has indicated that the numbers of PCSOs will be increased from 4,000 to 20,000 across England and Wales over the next three years.

A rather different initiative aimed at addressing local concerns is the Safer Neighbourhoods programme. This provides teams of officers initially operating in a small number of wards in each borough to provide local, community-based policing. The intention is eventually to extend the scheme to all wards in all boroughs. In theory, these officers will be ring-fenced to protect them from other duties enabling them to provide a permanent presence in the community.

6.4 Attitudes to Crime and Safety

Londoners perceive crime to be increasing both nationwide and in their own area - even though incidence is actually falling. Concerns about crime and safety are particularly strong in the social rented sector.

Generally, concerns about crime and safety do not appear to be dominant reasons for households thinking of moving out of the capital. Most businesses are concerned about crime in their area but again it is not generally a dominant concern. Londoners are relatively sanguine compared to much of the rest of the country and are generally rather more supportive of the police.

Perceptions of changing crime levels

Concern about crime is often as significant, if not more so, as the amount of crime actually experienced. Despite a considerable decrease in both actual personal and household crime over recent years, 65% of respondents in England and Wales thought that crime had increased in the country as a whole over the previous two years 48% of respondents perceived that crime in their local area had increased over the same period, with about a third believing it to have risen a lot. London is traditionally at the higher end of the range regarding perceptions of both national and local crime, with a significant majority believing that crime had risen both nationwide and locally.

Table 6.5
Fear of Crime 2003-2004

% very worried about…	Burglary	Car crime	Violent crime	Disorder
London	16%	19%	22%	25%
South East	11%	13%	13%	17%
England & Wales excl London	12%	14%	15%	16%

Source: Home Office 2004

The 2003-2004 BCS provides figures on fear of crime for four categories of crime (Table 6.5). These show that, compared to the rest of the country, Londoners are particularly worried about violent crime and disorder, where the incidence in the capital is undoubtedly higher than elsewhere.

In London-specific social surveys, concern appears to be much greater than reflected in national crime surveys. The MORI survey found that 33% felt unsafe outside their area in 2003, with particularly high levels of insecurity in the City and east London and among women. Fear of mugging, burglary, and teenagers hanging around were the main reasons for feeling unsafe, with the lack of a police presence coming fourth. Over 60% said that more police on foot would help improve safety levels.

The levels of concern about crime in London reflected in the 2002 London Household Survey are very high indeed, with almost two-thirds of households seeing the general level of crime in their neighbourhood as a problem (Table 6.6). Concern is particularly high among social tenants, although almost two-thirds of owner-occupiers also view crime as a problem. Owner-occupiers are more concerned about being burgled than are tenants, while concerns about vandalism and drug dealing are particularly concentrated in the social sector. Troublesome teenagers are seen as important by nearly a quarter of social tenants, but by only 13% of private sector households.

Feeling unsafe is particularly concentrated among older people, lone parents and single-person households but there are surprisingly few differences between ethnic groups. In terms of locality, attitudes are very similar between those living in the inner and the outer boroughs. Furthermore, although those living in the most deprived areas do feel slightly more unsafe and concerned about crime than those living in the least deprived areas, the differences are again quite small. The most significant differences are undoubtedly between tenures, with those living in the social sector feeling consistently more dissatisfied about their neighbourhood and more concerned about safety and crime than either owner-occupiers or private tenants.

The sample can be broken down (Table 6.7) into those who expect to move within the next five year (group 1), those who want to move but do not expect to be able to do so (group 2), and those who do not want or expect to move within that period (non-movers). Perception of general levels of crime are clearly strongly related to the wish to move and with the expectation of moving. Concerns about safety and dissatisfaction with the neighbourhood, however, are more closely correlated with wanting to move but not being able to do so.

Table 6.6
Londoners' views on their neighbourhoods

	LA Tenants	HA Tenants	Private Tenants	Owner-Occupier	Total
Ever feel unsafe at night	57%	57%	40%	44%	48%
General level of crime a problem	70%	67%	56%	65%	65%
Fear of being burgled	57%	55%	52%	63%	59%
Presence of arms dealers	48%	45%	28%	30%	35%
Vandalism/hooliganism	63%	61%	49%	57%	57%
Troublesome teenagers	24%	25%	13%	13%	16%
Litter/rubbish in streets	64%	60%	58%	65%	64%
Total in sample	**1,812**	**677**	**1,149**	**4,520**	**8,158**
% shares	**22%**	**8%**	**14%**	**55%**	**100%**

Source: London Household Survey, 2002

Table 6.7
Attitudes to the neighbourhood by expectations of moving

	Non-movers			Potential movers					
				Group 1			Group2		
	Social	**Private**	**O/Os**	**Soc**	**Priv**	**O/Os**	**Soc**	**Priv**	**O/Os**
Unsafe at night	56%	44%	46%	58%	38%	43%	66%	29%	61%
General level of crime	65%	54%	62%	77%	57%	72%	79%	64%	67%
Area has got worse	26%	17%	28%	33%	10%	34%	45%	14%	44%
General dissatisfaction with neighbourhood	22%	18%	14%	41%	17%	27%	54%	29%	29%

Source: London Household Survey, 2002

The evidence suggests that safety and crime are indeed high on people's list of concerns but that these concerns are neither necessarily related to neighbourhood attributes, but more to tenure and the capacity to choose where one lives.

Crime against business

Because so much of the available data are derived from surveys of individuals and because Home Office statistics do not distinguish crime against business as a separate category, there is little detailed evidence on the effect of crime and policing on business. Within recorded crime, only non-residential burglary and theft can be distinguished, together with certain crimes which are more likely to be against businesses, such as forgery and fraud. These data suggest that such crimes are a relatively small proportion of the total in incident terms and that their number has generally been declining quite rapidly (Table 6.1).

One area of particular concern for the City is serious fraud. The City Police obtained 23 convictions in 2003-2004, recovering and saving nearly £190m, compared to the previous year when 32 convictions were obtained but only £57m recovered or saved (City of London Police statistics). Current government concerns about serious and organised crime are more societal - trafficking in sex, drugs and illegal immigrants, and money laundering related to these crimes - than business-related. Moreover, performance measures concentrate on numbers of incidents and convictions which will always act against giving high priority to such a person-intensive crime as fraud.

The most recent survey of business by the British Chamber of Commerce (BCC, 2004) shows that the business community regards crime as a major problem, with nearly two-thirds of firms reporting having been victims during the year mainly through damage to vehicles and burglary. Crime is concentrated in retailing and the hotel and catering industry, and its incidence is highest among larger organisations. In almost all contexts, it is not businesses in London but those in the North of England that experience the highest levels of crime.

Most businesses perceive the problem in terms of levels of crime in their area rather than crime specific to their business, with 17% regarding this as very serious and a further 39% seeing it as a hazard. Not surprisingly, concern is concentrated in urban areas, but again the highest proportions are found in the North rather than in London. Evidence from small-scale research conducted by the authors suggests that it is street and drug-related crime in the area that particularly affects the attitudes of the business community.

Perceptions of the police

Although crime is higher and detection is lower than elsewhere in the country, Londoners' trust in their police force appears rather higher than the national average. According to the BCS, the proportion of Londoners who believe that local police do a very or fairly good job rose from 78% in 2001-2002 to 80% in 2002-2003, compared to a figure of 74% in both years elsewhere in England and Wales (Ringham, 2004).

London BCS respondents were also more satisfied than respondents from elsewhere with the way that the police dealt with incidents where they had been a victim. In 67% of incidents in London, victims were satisfied with the police action, compared with a 58% satisfaction rating elsewhere (Ringham, 2004). Moreover, a comparison of recorded crime and BCS victimisation figures suggests that violent crimes and burglary are more likely to be reported in London.

Even so, the 2002 MORI survey of Londoners showed far lower satisfaction with the way that their area was being policed than reported in the BCS, with only 42% very or fairly satisfied against 30% fairly or very dissatisfied. Satisfaction rates vary enormously between areas, from 58% in West Central to 23% in Merton and Wandsworth. Again, however, there appears to be no obvious spatial pattern in these responses. Where Londoners were clear was in their support for PCSOs, with around 80% in favour of the initiative and only 9% against. Support is particularly strong among those living in outer London and does not vary much by age or ethnicity.

6.5 Conclusions and Implications for the Future

Controlling crime and improving safety – and especially reducing fear of crime - are important issues for Londoners and for the London economy, but the situation is not as bad as it is painted and is generally improving.

Looking again at the questions set at the beginning of the chapter, it would appear that the situation is not as bad as it is painted. The incidence of many types of offence is declining in London although crime in general remains more prevalent in London than elsewhere in the country. Most importantly, violent crime is still increasing and there is concern that the impact of drug-related crime has yet to reach its peak. Moreover, detection rates, although beginning to increase, remain far lower than elsewhere in the country.

Fear of crime is, as everywhere else in England and Wales, more prevalent than actual victimisation. However, Londoners appear to be relatively more sanguine than those living in areas with lower levels of crime. The problems are being addressed through an increasing range of initiatives. These involve considerable extra expenditure, paid for partly by central government but proportionately more by Londoners themselves.

London is relatively well policed in terms of the number of officers of every type and the scale of policing is on the increase. The introduction of PCSOs, aimed at reassuring the public and meeting demands for a street presence, appears to have been welcomed by all groups of Londoners. Peoples' perceptions of the risks they face regarding crime and anti-social behaviour clearly affect their satisfaction with living in London, but there is very little evidence that this perception is the deciding factor when making decisions about where to live, work or invest.

Finally, and looking to the future, there are hints that some of the crime and safety problems facing London are beginning to come a little more under control, although there is still a long way to go before Londoners will be convinced that there has been a major improvement. The challenge remains one of meeting the demands for crime reduction and greater detection rates, at the same time as providing general reassurance to the public and an effective control of the terrorist threat.

7. Key Issues for the Future

London's future looks relatively healthy on current trends but there are many uncertain factors which will help to determine what the actual outcome will be.

London's future is determined by a range of factors including economic fundamentals: the quality of its labour force; appropriate investment in infrastructure; a high quality living and working environment, including affordable housing and safety and security; a healthy relationship with the rest of the UK; and a diverse and forward-looking economic structure which ensures international competitiveness. This chapter reviews some important evidence and policy initiatives which may impact on London's future.

7.1 'Greater' Greater London and the Northern Archipelago

According to a new study written by a group from Sheffield University, London is a vast city embracing much of southern England, which has become richer and more successful than any other part of the UK.

This spreading out of London into its surrounding regions is not a sudden occurrence. Moreover, it is difficult to imagine government interventions that could change this pattern of development without adversely affecting international competitiveness.

The North/South divide and the concentration of economic drivers especially in London are well-established if stylised facts about how the UK economy works. It is seen by many commentators as a necessary evil in order to maintain international competitiveness, although others see it as generating an unequal and unsustainable society. The 2001 Census provided a chance for a new look at what is actually going on and to see whether the underlying trends are shifting. A particularly important contribution has been made by academics from Sheffield University who published a graphic study of the nature and extent of the divide and the 'drift to the South East' which included a careful, but attention-grabbing, mapping of evidence from the 2001 and earlier Censuses (Dorling *et al.,* 2004).

Two things set this study apart from otherwise similar discussions from the 1960s and 1980s:

- the emphasis on the urban dimension with the entire southern half of the country presented as effectively an extension of London and its economic dynamism, while the northern half is seen as an 'archipelago' of urban decline
- the detailed analysis of the evidence base which shows that the 1990s represented the continuation of a century-long process of restructuring the country around London, rather than displaying a recent, and therefore perhaps readily reversible, development

In some qualitative respects, the picture does show an acceleration of past trends. In particular, the proportion of all UK graduates living in London has grown from 16% to 20% between 1991 and 2001, a trend with powerful implications for the ability of northern cities to compete for or retain advanced service functions.

The immediate response to the study in the media has revived some myths:

- that there is a general drift of population to the south
- that growth of opportunity in the extended London region is substantially attributable to banking and finance
- that, in a globalised economy, London does not need the markets of northern Britain

There is a danger that such myths will be taken as reality when, in fact, it is relatively straightforward to refute or put into context all of them. Population growth in the south of the UK actually has more to do with patterns of international migration since net emigration continues from London and the South East to the rest of the UK. In 2002, as Table 3.16 in *Regional Trends* shows, there was net migration from London to the rest of the UK of 262,000 with just 155,000 immigrants arriving in London from all other regions.

For the three south east regions in total, 612,000 left for the rest of the country, while 534,000 arrived from other parts of the country. Insofar as there is mobility within the UK, it is now from the southern regions to the northern ones. However, there is substantial migration from overseas to London (a net inflow of 519,000 between 1998 and 2002) and the surrounding regions, and it is this which has led to the net increase in population in and around the capital.

The growth of opportunity in the Greater South East attributed to banking and finance, has actually taken place across a far wider group of business services. According to the ONS, between 1994 and 2000, the financial intermediation share of the London economy fell from 14.6% to 11.2%, while the share of real estate, renting and business activities (essentially, business services) increased from 27.0% to 35.5%.

Finally, as Chapters 2 and 3 of this report made clear (and the OEF report *London's Linkages with the Rest of the UK*, May 2004, spelled out in much detail), the London economy is still closely integrated with the overall UK economy. The Sheffield research does nevertheless help to inform some key policy issues at a time when the government is both reviving aspects of regional policy (if with quite modest ambitions) and also keenly interested in boosting productivity, which other current research is showing to be ever more clearly linked to agglomeration (Rice and Venables, 2004). There are increasingly obvious challenges also in the relation between the government's regional devolution agenda and the availability of potential regional leadership outside London.

7.2 Investing in London

Major projects such as the East London Line extension, a number of Docklands Light Railway developments and several tramway schemes are now set to go ahead.

Crossrail will be given Parliamentary time, though the funding required has still not been put in place. The recent review of local government finance makes no concrete proposals for funding this and other future projects, however.

As Chapter 5 of this volume suggests, public expenditure in London is low in relation both to the level of economic activity and to the taxes it generates. Virtually all tax and spending decisions concerning the capital are made by central government. Two major public policy statements during 2004 could therefore have significant impacts for London services and investment. First, the government's *2004 Spending Review* (SR 2004) set out overall public expenditure totals for three years up to 2007-2008. Second, the Balance of Funding review considered the future of local government finance.

Both the Mayor of London and the Association of London Government made strong submissions to the Spending Review, pointing out the capital's public service expenditure requirements. The Mayor's document, *The Case for London,* which focused particularly on Crossrail, the East London Line extension, Thameslink, extensions to the Docklands Light Railway, and proposed new trams was able to cite Number Ten Strategy Unit's conclusion that the city's transport infrastructure "has not kept step with the city's developing needs over the last 50 years" (GLA, 2004b)

The detailed outcomes of the Balance of Funding review (HM Treasury, 2004f) will not be known for some months. However, Transport for London (TfL) interprets the related consultative document on the future of transport (Department for Transport, 2004a) as offering London a package enabling £3bn of additional investment over the next five years. Prospects for the achievement of the East London line and DLR projects have also been enhanced by the government's announced reform of the local government capital expenditure control system for 2004-2005 and beyond, under which the GLA group had been given freedom to invest some £400 million per annum under new ‘prudential borrowing’ rules. TfL also appears surprisingly confident of government funding to meet a widening budgetary gap associated with the growing subsidy for London buses.

Prospects for Crossrail remain uncertain. The government has announced its intention to introduce legislation providing the necessary planning powers, but not finance. The latest Crossrail review (the Montague Report, DoT, 2004b) raises concerns about number of aspects of the business case including links with the mainline, understated costs, the governance structure and financial market capacity. The earliest completion date now envisaged is 2013 or 2014, too late to benefit from London’s 2012 Olympic bid, which has helped advance other regeneration and transport schemes.

Overall, SR 2004 implies a slowing in the growth of public expenditure after 2005-2006 compared with the last three years, with continuing priority given to health and education. There is no reason to imagine that London will be treated differently from other parts of the UK. Both this and the need to find a new funding stream to finance borrowing for Crossrail, give particular importance to the Balance of Funding review, which is looking for additional independent revenue sources for local government. The initial review (the Raynsford Report, ODPM, 2004) examined a series of ideas, though none as radical as the forms of betterment levy suggested in relation to Crossrail (or, indeed, in the Barker Review). The search for possible local taxation reforms continues with a further review to be chaired by Sir Michael Lyons (see below). Thus, there has been little apparent progress on the financing issue which is key to securing infrastructure for London.

7.3 Housing and Planning in the Region (The Barker Review)

The Barker Review made recommendations about how to free up the housing market and planning system to deliver significant increases in housing output and thus reduce house price inflation, particularly in London and the South East. The Review's proposals, if accepted, are expected to support the Prescott agenda of sustainable communities which is already concentrating on ensuring a step change in output in the South East.

Last year, the Chancellor, concerned by the lack of responsiveness of housing supply to increasing demand and its impact on UK competitiveness, commissioned Kate Barker, a member of the Monetary Policy Committee, to examine what could be done to improve the situation.

The Barker Review (HM Treasury, 2003 and 2004g) concluded that the planning system, the structure of the construction industry, uncertainties faced by the industry and lack of incentives to local authorities, as well as a simple lack of land, all helped to make supply unresponsive. As a result, the Review estimated that British housing prices have risen in real terms by 2.4% per annum over the last 30 years, compared with an EU average of 1.1%. Modelling suggested that between 70,000 and 120,000 additional private sector homes per annum plus around 20,000 more social sector homes would be needed in England to reduce price rises to more acceptable levels and to meet housing need.

To achieve such an increase, Barker recommends requiring the land use planning system to make more land available in response to evidence of increasing affordability problems; providing incentives to local authorities to ensure provision; introducing an independent Regional Planning Executive to advise on requirements and to co-ordinate key players such as infrastructure providers and developers; taxing planning gain and hypothecate some of these gains to fund larger scale infrastructure; and restricting the use of planning obligations, known as S106, to the provision of affordable housing and the direct costs to the community associated development.

The overall tone of the Barker review is concerned with removing impediments to economic activity and easing labour mobility by making housing supply more responsive to economic signals; reducing uncertainty about development; paying for some of the social costs of that development; and redistributing the benefits away from landowners to the community. Barker's proposals have been met with Treasury support, although the latter has yet to make clear its views on the taxation proposals. Concern has been expressed, however about how the shift from one regime to another can be effected without the process itself generating increased uncertainty and cutting output.

In the context of London, the Barker Review, while providing a long term approach to increasing responsiveness, does little more than support the Prescott agenda for growth areas. The areas included in the policy have been expanded, particularly in East Anglia, and the policy now calls for more than 200,000 extra dwellings to be built in these areas over the next fifteen years with the intention of freeing up homes for commuters for London as well as building sustainable communities in the wider South East.

Whether together these initiatives can succeed is unclear. Increasing emphasis on growth areas, some of which are very difficult to develop, together with changes in the S106 approach could undermine the impetus behind expanding output and ensuring higher proportions of affordable housing within London's boundaries.

7.4 Dispersal of Civil Servants (The Lyons Review)

Proposals have been made to relocate 20,000 civil servants away from London and the South East of England although the policy has to some extent been overtaken by more extensive proposals to cut between 40,000 and 80,000 civil servants across the UK.

It is clear that no command-and-control functions will leave the capital. Consultants working for the Lyons Review concluded that any relocation would be unlikely to have any long-term impact on London's powerful and private sector-driven economy.

Another recent government review focused on the issue of London's relations with the rest of the UK was Sir Michael Lyons' review of the case for moving civil servants out of London and the South East - the most memorable element in the government's new, revitalised regional policy. The review confirmed that it would be feasible to move some 20,000 jobs to elsewhere in the UK (as the Chancellor had proposed) and suggested that it would be desirable to move more. A major motive for the Treasury was cost saving, with prospective gains of £2bn over 15 years to add to those of the planned reduction of 40,000-80,000 civil service jobs across the UK as a whole, included in a broader review by Sir Peter Gershon.

The real substance of the Lyons Review seems pretty limited in the London context. Quantitatively, 20,000 jobs are substantially less than one recent year's reduction in City employment, which left Londoners' general prosperity almost untouched. It is also quite modest in relation to the long-term trend of decentralisation which contributed substantially to a shrinkage of 63,000 in the number of non-industrial civil servants in London over a 25-year period (Buck *et al.,* 2002) and 130,000 across London and the South East as a whole since 1969. Indeed, this region no longer has a disproportionate share of the civil service as a whole, though London itself does still retain a very high proportion of senior civil servants in the policy-making positions.

More radical unofficial proposals (Amin *et al.,* 2003) have envisaged the break-up of this policy cluster as a means of engendering a growth of higher-status jobs in selected provincial centres to help to stem a brain drain sapping these of what should be their key economic asset in a knowledge economy. This is probably unrealistic both because of the likely strength of resistance to dispersal and the impact on links between departments and with parliament. Rather, the Lyons report envisages another round of dispersal of lower-middle level jobs associated with less strategic functions.

Thus the real gains for more peripheral regions are likely to be limited, and the economic losses for London will certainly be small. The expectation of both of Lyons' consultants (Experian, 2004) and of the London Development Agency which backs dispersal is that it will help the reduce overheating in the capital's labour and property markets without weakening any significant agglomeration economies, hence reinforcing London's comparative and competitive advantages. More jobs, and more senior jobs, might in principle be at stake were the Chancellor's more general promise to cut civil service employment to be carried out. As the Institute of Fiscal Studies (2004) has pointed out, however, annually repeated plans since 1999 to reduce jobs and administrative costs have had no impact on actual growth.

7.5 Where is London Going?

Although the capital's economy remains flexible and internationally competitive, there will always be questions about its longer-term potential. Other British cities are making claims to revival and there are as many factors that imply continuing risk as there are suggesting sustainable growth.

The most likely scenario appears to involve continuing economic growth but with slower expansion in employment even though additional City-type jobs are now being generated in the capital.

Since last year, some longer-term economic prospects appear more encouraging, especially the moves towards building an improved public transport infrastructure.

For the last three years, the strong employment growth trend that characterised London in the second half of the 1990s has been on hold. However, there has been no sign of the sharp downturn which followed the last boom at the start of the 1990s. Indeed, forecasters such as the centre for economics and business research are now predicting substantial growth in City-type employment in the years ahead. This is encouraging, in the light of the terrorist threats and other difficulties (such as infrastructure weaknesses) facing the capital. London's economy appears to have prospered while those of its key competitor cities, notably New York and Tokyo, have been depressed (for an analysis of the New York situation, see Bureau of Labour Statistics, 2004). New York City's economy is still 170,000 jobs below its mid-2000 peak, with no off-setting growth in the rest of the metropolitan area, while London's employment total, on a broadly similar base, is more or less unchanged.

As in previous years, we are faced with the need to make a judgement about the likely future facing the London economy over the long as well as the short run. This task can now be informed by the work of GLA Economics, who publish an annual economic outlook as well as quarterly reviews. The 2004 edition suggests a strong return to GVA growth in 2004 with a consensus forecast of 3.3%. Growth in London exceeded that in the UK as a whole from the final quarter of 2003 and London seems likely to expand at or above the UK rate for the full year. Consensus forecasts for 2005 and 2006 are for GVA growth of 2.9% and 3.0%, respectively. Although such figures are respectable, they are well below the growth rates of up to five per cent which supported the employment expansion of the late 1990s, though they are expected to yield an additional 150,000 jobs between the end of 2003 and 2006 (GLA Economics, 2004).

Though encouraging, it is not possible, as GLA Economics, 2004 makes clear, to use these medium-term forecasts to assess the credibility of the London Plan's long-term trend projections which involve net growth of 636,000 jobs between 2001 and 2016. One reason is that the GLA Economics forecasts are actually "calibrated to the GLA's employment projections for 2010" (*op cit.,* p.16), while another is that is almost impossible to judge underlying trends except in relation to performance across a whole economic cycle. Evidence discussed in Chapter 2 about the apparent overstatement of London job growth in the official ABI employment series in the period running up to the Plan's preparation does, however, suggest that its trend projections are likely to be over-optimistic. Relying as far as possible on the survey-based sources (Labour Force Survey and/or Census) which we believe to be more reliable, we get estimates of growth across the last cycle of 140,000 (peak-peak 1989-2001) or 180,000 (1990-2003)[10] – around a third of the trend growth rate projected by the Mayor's Plan, which still therefore needs to be viewed sceptically. As discussed in Chapter 3, there are also big questions as to whether the potential labour supply from among asylum seekers will be mobilised as effectively as the projections imply.

In relation to the medium term, there are two main areas of uncertainty: how robust is this prediction to macro-economic and external shocks, and how closely will employment growth follow economic expansion? At the moment, the most likely scenario is that London will witness sustained economic growth more or less in line with the UK average. Such an outcome might of itself be beneficial in that with comparable rates of growth, there is less chance the government will feel inhibited to sanction new investment.

[10] Although another version actually gives a loss of 40,000 for this period.

An obvious current concern is what is going to happen to house prices. London prices have grown less rapidly than the national average for some months. Clearly, a major fall in London house prices could have a significant impact on the wider economy, although not on the same as in the early 1990s unless either interest rates and/or unemployment rise rapidly. The more likely scenario is a continued slowdown with decreasing differentials to the rest of the country. This is what the Monetary Policy Committee is aiming at, in part because of its concerns about overall private sector borrowing with total UK indebtedness exceeding £1 trillion for the first time in the summer of 2004.

The conclusion of this report, as with previous editions, is that London's economy is inherently more volatile and more open to external shocks than the rest of the country. The report continues to believe that the fundamentals of London's longer-term economic position remain very positive. The main concern remains delayed and inadequate investment in the city's infrastructure. In this context, it is still too early to be certain about many of the new transport and infrastructure proposals but there are some grounds for optimism about the East London Line extension, the Docklands Light Railway extensions, tramways and conceivably Crossrail.

The big uncertainties remain the same – global pressures from a possible oil crisis; significant changes in interest rates; terrorism attacks; and the impact of greater uncertainties on confidence and particularly investment. As last year, on current longer-term trends, London appears relatively well placed both nationally and internationally but it equally remains more exposed to external change than the rest of the country.

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The Corporation of London

The City of London is exceptional in many ways, not least in that it has a dedicated local authority committed to enhancing its status on the world stage. The smooth running of the City's business relies on the web of high quality services that the Corporation of London provides.

Older than Parliament itself, the Corporation has centuries of proven success in protecting the City's interests, whether it be policing and cleaning its streets or in identifying international opportunities for economic growth. It is also able to promote the City in a unique and powerful way through the Lord Mayor of London, a respected ambassador for financial services who takes the City's credentials to a remarkably wide and influential audience.

Alongside its promotion of the business community, the Corporation has a host of responsibilities which extend far beyond the City boundaries. It runs the internationally renowned Barbican Arts Centre; it is the port health authority for the whole of the Thames estuary; it manages a portfolio of property throughout the capital, and it owns and protects 10,000 acres of open space in and around it.

The Corporation, however, never loses sight of its primary role – the sustained and expert promotion of the 'City', a byword for strength and stability, innovation and flexibility – and it seeks to perpetuate the City's position as a global business leader into the new century.

CORPORATION OF LONDON