London's Economy Today

Issue 76 | December 2008

In this issue

GLAECONOMICS

Bank of England cuts interest rates again

by **Gordon Douglass**, Economist

On 4 December the Bank of England cut interest rates by 100 basis points to 2 per cent, equalling the lowest rate ever set by the Bank (see Figure 1). It is the lowest rate since 1951. However the LIBOR rate, a key factor in banks' lending price decisions to small businesses amongst others, remains elevated compared to the Bank rate.

Also on the 4 December the European Central Bank (ECB) reduced its interest rate by 75 basis points to 2.5 per cent, whilst the Riksbank, Sweden's central bank, reduced its interest rate by 175 basis points to 2 per cent. Meanwhile on 16 December the Federal Reserve cut interest rates from 1 per cent to a target range of between 0 and 0.25 per cent. The Fed announced that it expects to keep rates at these very low levels "for some time". The central banks responded in this aggressive manner due to mounting evidence of a slowdown in their respective economies. Economic sentiment in the Eurozone has dropped to a 15-year low as measured by the European Commissions economic sentiment indicator in November, whilst Eurozone retail sales are falling. Meanwhile in the UK the Purchasing Managers Index readings by Markit Economics for the Chartered Institute of Purchasing and Supply (CIPS) for construction, manufacturing and services all hit record lows in November.

Latest news...

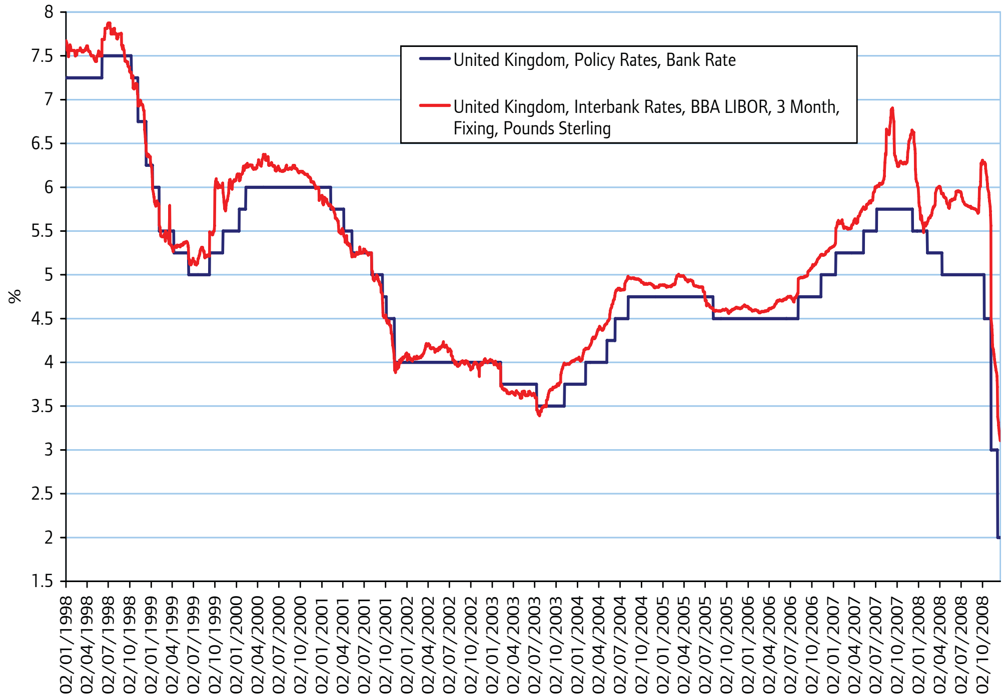
- **Current Issues Note 23: Food price increases and their impact on London's lowest income groups**

Throughout late 2007 and much of 2008 food prices were rising faster than prices as a whole in the UK. As at September 2008, CPI inflation for the lowest gross income quintile is estimated to have been substantially above the overall CPI inflation rate. However, with food prices now seeming to have peaked, the inflation spike may be short-lived. Marked falls in food commodity prices should benefit London's poor disproportionately.

Visit **www.london.gov.uk/mayor/economic_unit** to download this publication.

Figure 1: Bank of England's Repo rate and the 3 month London Inter-Bank Offered Rate (LIBOR)
Last data point is 16/12/08

Source: EcoWin

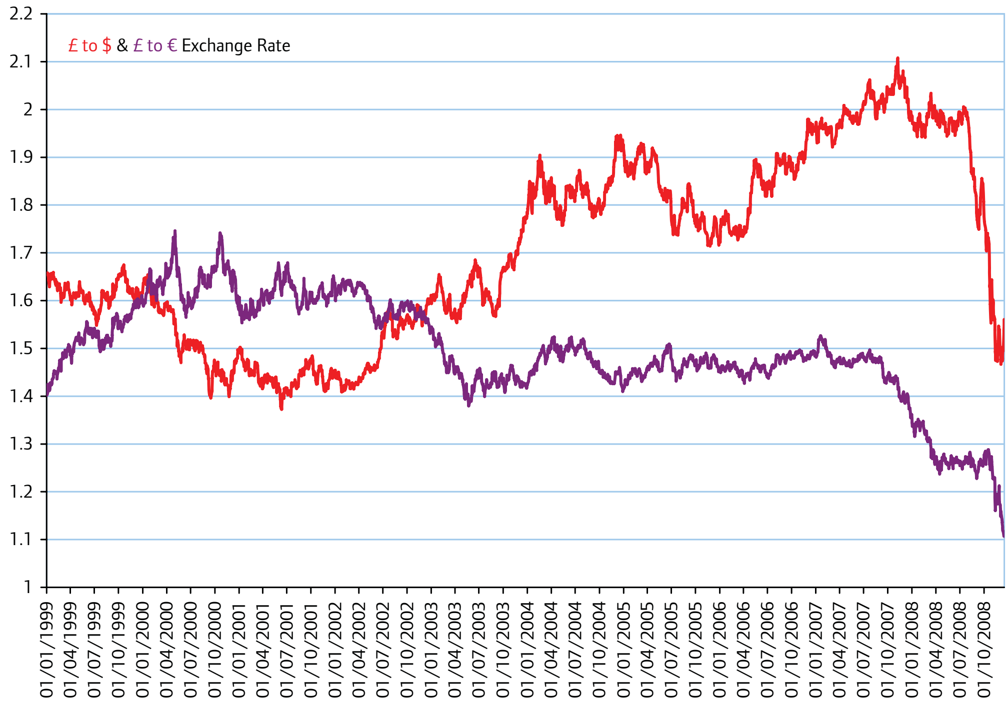


Sterling falls on the back of bad economic news

Responding to concerns about the British economy and the expectation of further interest rate cuts sterling has been depreciating. The pound fell against the dollar by the largest amount (in percentage terms) since 1992 on 1 December. The pound has also been weak against the Euro with it hitting record lows against the single currency in December (see Figure 2). Further volatility in the currency markets is expected in future months as the world economy enters 2009 in a weak state.

Figure 2: £ to $ and £ to € exchange rates
Last data point is 16/12/08

Source: EcoWin



Global car industry in big trouble

Car sales around the world continue to decline as the world economy slows sharply. UK car sales fell by 37 per cent in November 2008 compared to November 2007. Further declines in world car sales are expected in 2009 with, for example, the German Association of the Automotive Industry predicting that it will be the worst year for German car sales since reunification in 1990. The decline in sales has seriously affected car manufacturers with, amongst others, Nissan in Sunderland announcing down days in the run up to Christmas and Honda announcing that its Swindon plant will close for 50 days in February and March 2009. Meanwhile Vauxhall, which is owned by General Motors (GM), has offered its staff at Ellesmere Port the chance to take a sabbatical on 30 per cent pay, in an attempt to avoid redundancies. Elsewhere the Swedish government announced on 12 December that it would offer its car manufacturers SKr25 billion (approximately £2.1 billion) in loans and loan guarantees to protect domestic car manufacturing. Concern is also mounting in the US about the state of its big 3 car manufacturers, GM, Ford and Chrysler. A $14 billion loan deal package failed in the US Senate on 11 December. With GM and Chrysler claiming they need $15 billion to continue operations until the end of March 2009 there are now concerns about the short-term future of these two companies.

Shocks from the credit crunch still being felt

Fallout from the credit crunch continues with London Scottish Bank, a British bank that specialised in customers with poor credit histories, entering administration after the Financial Services Authority (FSA) intervened to stop it accepting deposits. The Treasury has indicated that retail depositors will get all their deposits back at the Manchester-based bank, even if their savings exceed the £50,000 limit set by the Financial Services Compensation Scheme. The Bank for International Settlements (BIS) has released new figures showing that cross border loans declined by $1.1 trillion in the first half of 2008, with foreign lending to UK banks falling by $884 billion, or 80 per cent of the entire contraction in international lending. Worldwide issuance of bonds and securities has also markedly fallen, from over a trillion dollars in Q2 2008 to just $247 billion in Q3 2008.

London business experiencing a deterioration in the availability of capital

The CBI's December 2008 London business survey report found that over a third of respondents had suffered a deterioration in the availability of capital since the onset of the credit crunch. Thirty per cent of responding businesses said their total value of business had declined over the previous six months, 38 per cent said their volume of business had decreased, and 80 per cent "expect their sales and revenues will be hit by the economic crisis." Business confidence has fallen with 35 per cent pessimistic about their prospects for the next six months, the highest level since the survey started four years ago and up from 28 per cent six months ago. Other findings of the report include that 77 per cent of respondents said that "London is a good place to do business", which is lower than the 95 per cent who responded in such a way a year ago, and that a third see London's status as a world city diminishing over the next five years up from 13 per cent two years ago. Skills constraints were seen as a problem for employers with 79 per cent of employers finding trouble in hiring people with specific technical skills and nearly half facing constraints in hiring due to a lack of generic skills. Businesses were optimistic about the impact of the 2012 Olympics with two thirds expecting them to boost London's international profile, 70 per cent expecting indirect business opportunities and nearly 60 per cent expecting direct business opportunities from the Games.

London seen as a gateway to international markets

A recent report by Think London 'The world via London: Where will your company be in 2012?' found that overall London is the preferred international city of senior executives from which to globalise their companies due to its "high-quality institutional frameworks", "highly skilled workforce" and because it "is regarded as one of the most exciting and culturally diverse places to live and work". London was found to have a brand premium over its competitors with "a 4% brand premium over New York, 20% over Singapore, and 23% respectively over Shanghai and Paris". Further London was the "clear favourite" amongst BRIC (Brazil, Russia, India and China) executives, with its top position due largely "to the quality and perceived high value for money of working with London's professionals". London is also seen to offer a business-friendly culture, is thought of as a gateway to international markets and it is felt that its diversity and vibrancy "means anyone from anywhere can feel at home". Meanwhile the Competition Commission has said it will require BAA to sell Gatwick and Stansted (as well as Edinburgh) airports, which it is hoped will increase responsiveness to the needs of London travellers. The decision is subject to a final consultation.

Economic gloom as Christmas approaches

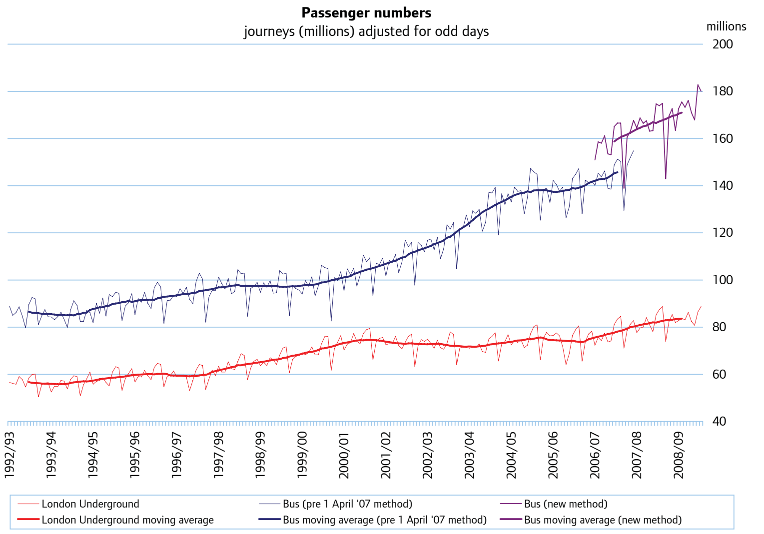
Further evidence of the depth of the slowdown affecting the UK economy has emerged with a Markit Economics survey on jobs for KPMG showing the fastest decline in permanent placements availability in the 11 years of the survey. Meanwhile the Q4 Business Confidence Monitor from the Institute of Charted Accountants in England and Wales (ICAEW) found that over the period 30 July to 24 October 2008 business confidence declined for a sixth consecutive quarter to reach a new record low. Construction, property, wholesale and retail, and hotels and catering were most pessimistic, whilst reported growth in turnover and profits also continued to decline and there was evidence of a cooling labour market. However, the Banking, Finance and Insurance sector showed "tentative" signs of confidence bottoming out. Meanwhile in the US unemployment increased by over 500,000 during November, more than was expected, to 6.7 per cent, a 15-year high. Allianz, the world's largest credit insurer, forecasts that nearly 200,000 companies will go bankrupt next year in Europe, with "an explosion" of failures in the US as well. In response to the slowdown a number of European countries have announced plans to boost their economies with Italy approving an €80 billion plan of tax breaks, public works, and mortgage relief, whilst France unveiled a €26 billion stimulus package and Germany and Spain unveiled job creation plans costing €50 billion and €11 billion respectively. With increasing job losses London also faces a challenging start to 2009. However, the recent global interest rate cuts and economic stimulus packages, along with the continuing depreciation of sterling and the recent decline of commodity prices should provide some support to London's economy.

Economic indicators

Increase in moving average of passenger numbers

- The most recent 28-day period is from 12 October 2008 to 8 November 2008. London's Underground and buses had 268.8 million passenger journeys; 180.0 million by bus and 88.8 million by Underground.
- The moving average of passengers every period increased to 254.5 million from an upwardly revised 254.0 million. The moving average for buses was 171.0 million. The moving average for the Underground was 83.6 million.
- The methodology used to calculate the number of bus passenger journeys was changed by TfL from 1 April 2007. For a detailed explanation please see LET issue 58 (June 2007).

Latest release: December 2008
Next release: January 2009

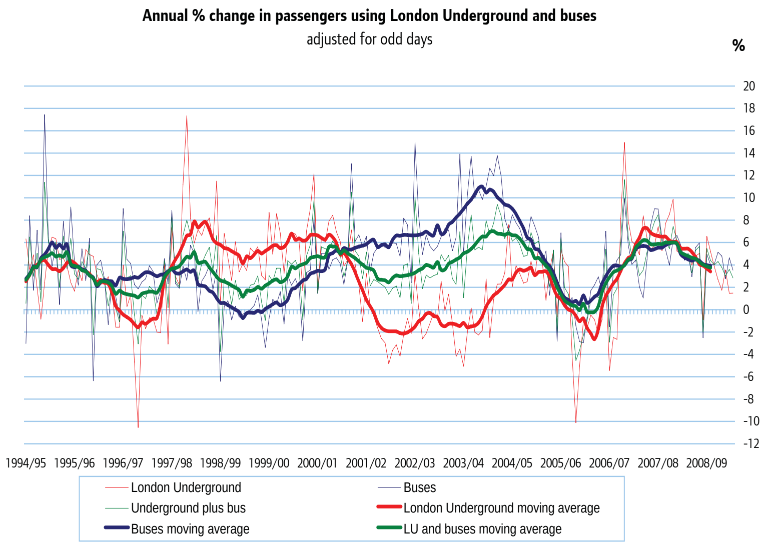


Source: Transport for London

Average annual growth rate of passengers continues to decrease

- The moving average annual rate of growth in passenger journeys decreased to 3.7% from an upwardly revised 3.9% in the previous period.
- The moving average annual rate of growth in bus passenger journey numbers decreased to 3.9% from an upwardly revised 4.0% in the previous period.
- The moving average annual rate of growth in Underground passenger journey numbers decreased to 3.4% from 3.7% in the previous period.

Latest release: December 2008
Next release: January 2009

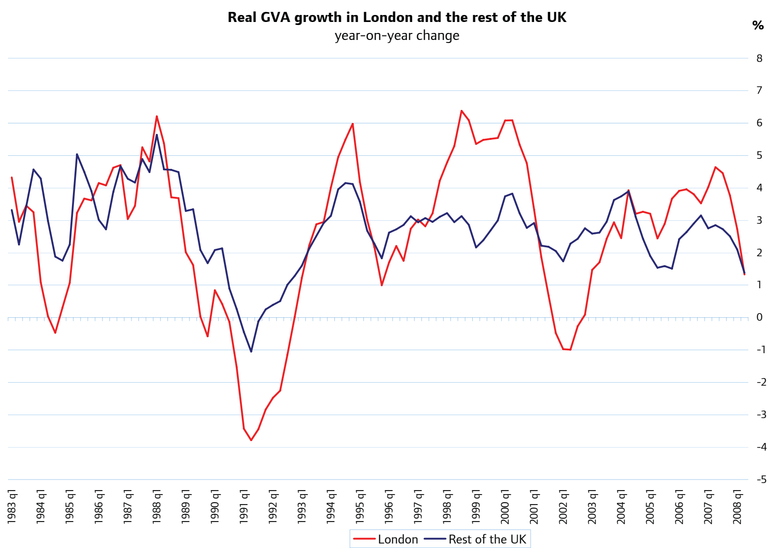


Source: Transport for London

Annual output growth slowing in London and the rest of the UK

- London's annual growth in output decreased to 1.3% in Q2 2008 from a downwardly revised 2.7% in Q1 2008.
- The rest of the UK's annual growth in output decreased to 1.4% in Q2 2008 from a downwardly revised 2.1% in Q1 2008.
- There have been revisions to previous growth rates to reflect the availability of new data.

Latest release: November 2008
Next release: February 2009

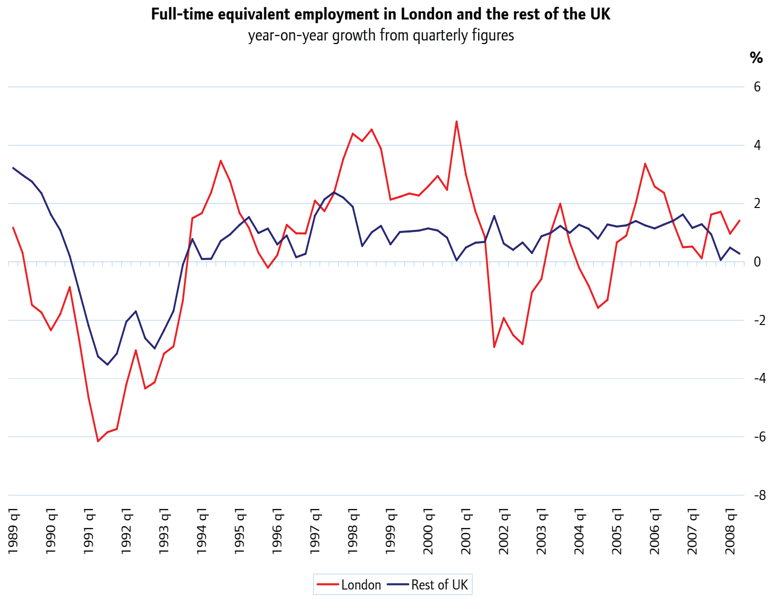


Source: Experian Business Strategies

Annual employment growth in London faster than the rest of the UK

- London's annual employment growth increased to 1.4% in Q2 2008 from an upwardly revised 1.0% in Q1 2008.
- Annual employment growth in the rest of the UK decreased to 0.3% in Q2 2008 from a downwardly revised 0.5% in Q1 2008.
- There have been revisions to previous growth rates to reflect the availability of new data.

Latest release: November 2008
Next release: February 2009

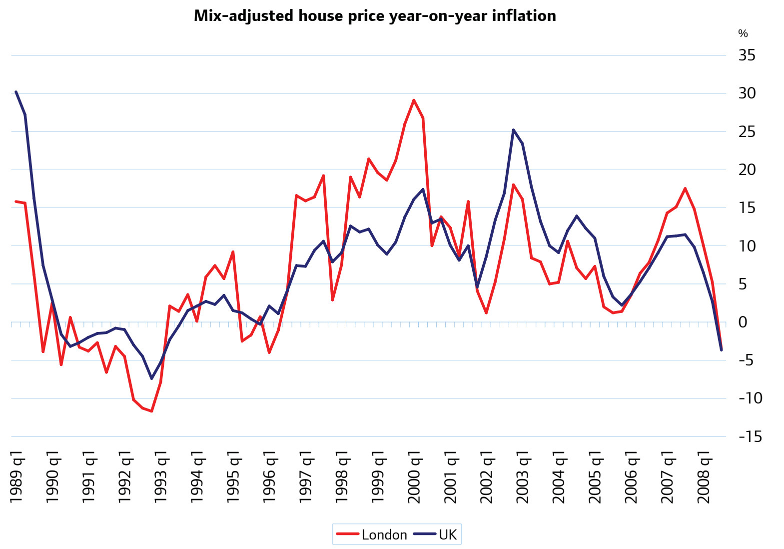


Source: Experian Business Strategies

Falling house prices

- The Department for Communities and Local Government (DCLG) house price index is an official measure of house prices. It is available up to Q3 2008.
- The DCLG reported a fall in annual house prices in both London and the UK in Q3 2008.
- Annual house price inflation in London decreased to –3.5% in Q3 2008 from 5.2% in Q2 2008. Annual house price inflation in the UK decreased to –3.7% in Q3 2008 from 2.7% in Q2 2008.

Latest release: November 2008
Next release: February 2009

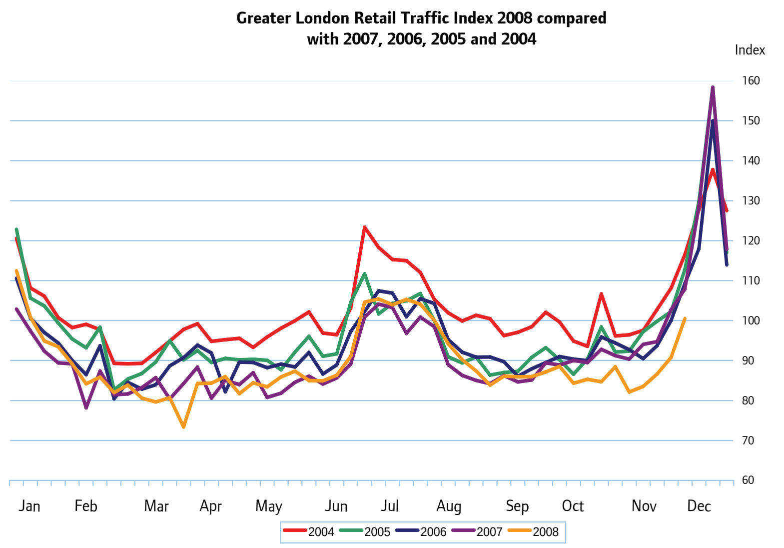


Source: Department for Communities and Local Government

SPSL Retail Traffic below 2007 levels

- The SPSL Retail Traffic Index of shoppers in London was 100.5 in the first week of December compared to 90.8 in the previous week.
- The index has been below 2007 levels since mid-September.
- SPSL's Retail Traffic Index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: Mid-December
Next release: Weekly

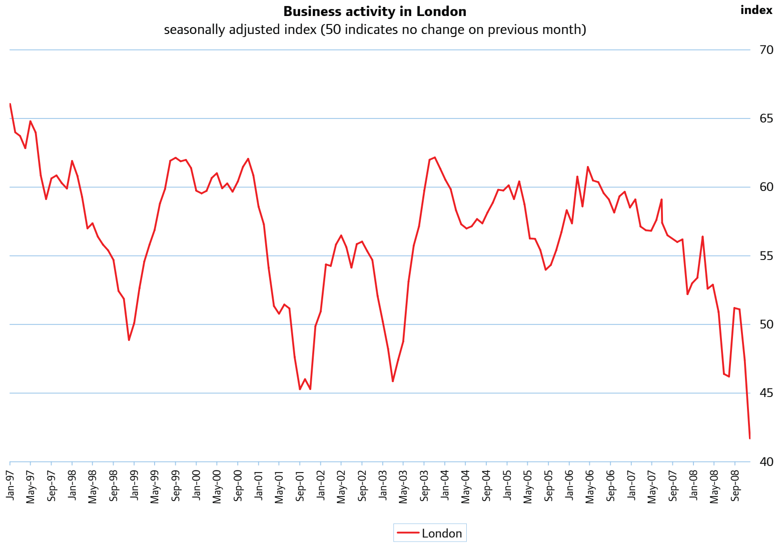


Source: SPSL

London's business activity decreases

- London firms decreased their output of goods and services in November 2008.
- The Purchasing Managers' Index (PMI) of business activity recorded 41.7 in November compared to 47.4 in October.
- A rate of below 50 on the index indicates a decrease in business activity from the previous month.

Latest release: December 2008
Next release: January 2009

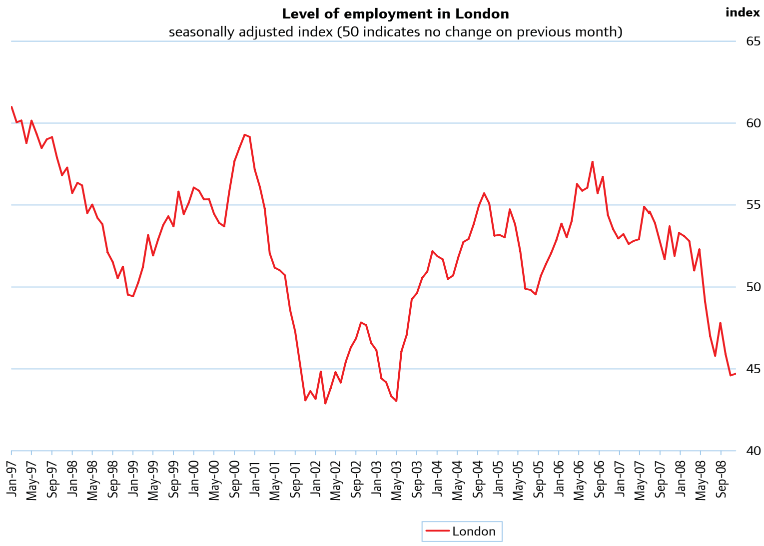


Source: RBS/Markit Economics

London employment weak

- The PMI shows that the level of employment in London firms decreased in November 2008.
- The PMI for the level of employment was 44.7 in November compared to 44.6 in October.
- A rate of below 50 on the index indicates a decrease in the level of employment from the previous month.

Latest release: December 2008
Next release: January 2009

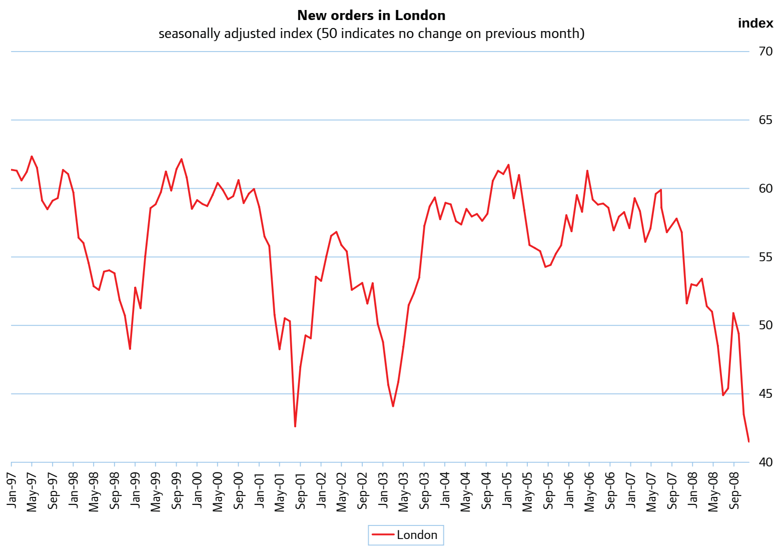


Source: RBS/Markit Economics

New orders in London falling

- November 2008 saw a fall in new orders for London firms.
- The PMI for new orders recorded 41.5 in November compared to 43.5 in October.
- A rate of below 50 on the index indicates a decrease in new orders from the previous month.

Latest release: December 2008
Next release: January 2009

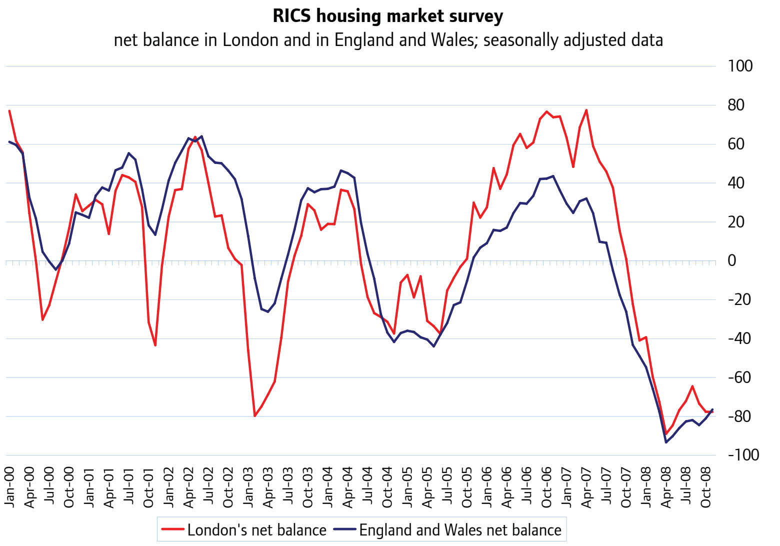


Source: RBS/Markit Economics

Surveyors report that house prices are falling in London and in England and Wales

- The RICS survey shows a negative net balance of -78 for London house prices over the past three months to November 2008. This net balance remained the same as October's revised balance.
- Surveyors reported a negative net house price balance for England and Wales of -76 in November 2008, up from an upwardly revised -81 in October 2008.
- London's net house price balance is now very similar to that of England and Wales.

Latest release: December 2008
Next release: January 2009

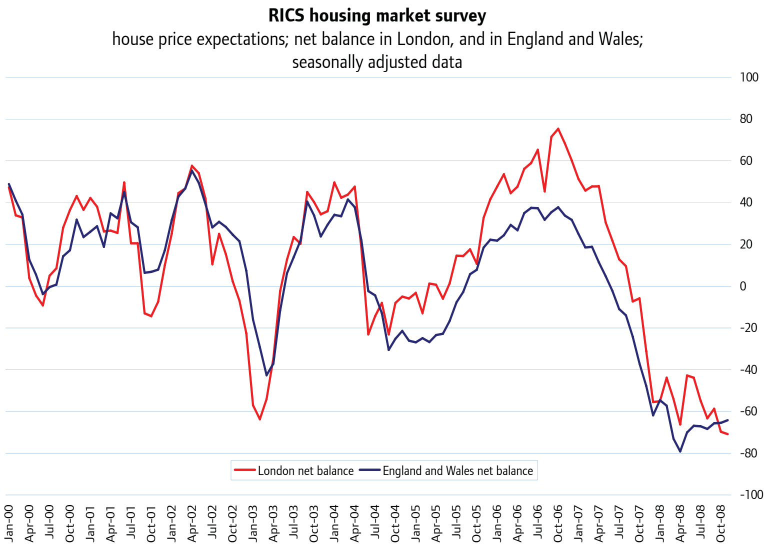


Source: Royal Institution of Chartered Surveyors

Surveyors expect house prices to continue falling

- The RICS survey shows that surveyors expect house prices to continue to decrease over the next three months in London and in England and Wales.
- The net house price expectations balance in London was -71 in November 2008, down from -70 in October.
- For England and Wales, the net house price expectations balance was –64 in November 2008, up from –65 in October.

Latest release: December 2008
Next release: January 2009

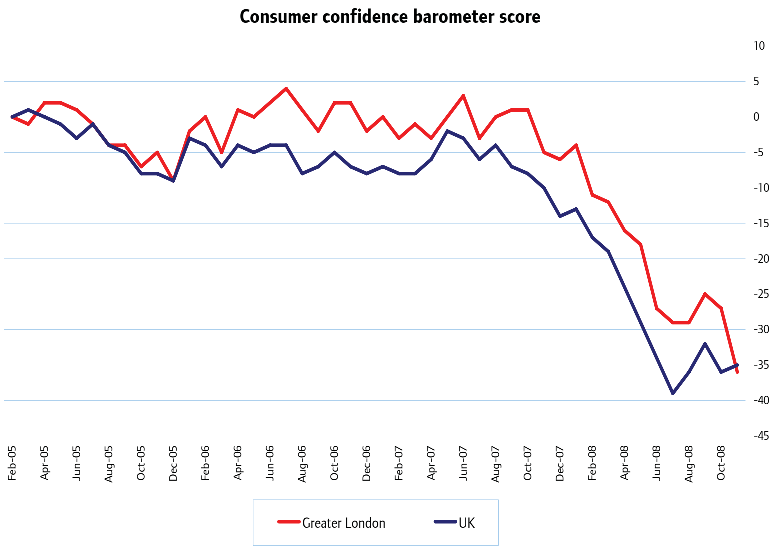


Source: Royal Institution of Chartered Surveyors

Consumer confidence still negative

- The GfK index of consumer confidence reflects people's views on their financial position and the general economic situation over the past year and their expectations for the next 12 months (including whether now is a good time to make major purchases). A score below zero signifies a negative change in views.
- For Greater London the consumer confidence score decreased to –36 in November from -27 in October.
- For the UK the consumer confidence score increased to –35 in November from –36 in October.

Latest release: November 2008
Next release: December 2008



Source: GfK NOP on behalf of the European Commission

Capacity takes centre stage in Transport for London's latest business plan

Nick Ennis,
Economist

As a centre of global trade, London's economy relies on the movement of people and goods. The city's transport network is one of the best in the world, but suffers from historic under investment. London's transport network has operated above capacity for some time and, despite the ongoing economic downtown, Transport for London's (TfL's) latest traffic report shows London Underground passenger numbers keep growing. In the long term, demand will only continue to grow as London is forecast to grow by one million more residents and 900,000 more jobs by 2026. Fortunately, the future of London transport looks much rosier than its past, with significant upgrades to the Tube already underway and other large works funded and ready to start.

Transport for London recently published its newest Business Plan, which lays out how it will invest over the next 10 years. It is the first devised under the new Mayor. The Business Plan includes only budgeted items and eliminates preparatory plans for projects where funding was uncertain. As a result, it focuses on completing planned works to renew and increase capacity on the existing public transport network. On the roads, more funding is committed to cycling initiatives, including a cycle hire scheme for central London, and special attention will be paid to improving traffic flow across Greater London.

There are many capital projects on the way; the two largest of which are the ongoing Tube upgrades and Crossrail, both of which will deliver significant new capacity and reduce overcrowding. Londoners will have noticed the frequent weekend station and line closures on the Underground in the last few years. These are part of work to gradually increase Tube capacity 25 per cent by 2022. Since trains can not be extended on most lines, work must be done to upgrade track and signalling equipment to allow trains to run more frequently. Nearly all lines will be improved, with the Circle, Metropolitan, District and Hammersmith & City lines seeing capacity grow by nearly 50 per cent. These lines will also see new air-conditioned carriages phased in from 2010.

Crossrail received Royal Assent in July. The railway will stretch from Maidenhead and Heathrow in the west to Shenfield and Abbey Wood in the east and will run 24 trains per hour through central London in the morning peak period. It will increase capacity on London's rail-based transport network by 10 per cent when it enters service in 2017. Journey times will be improved greatly, mostly because trains will run directly into central London and passengers will not need to change at Paddington or Liverpool Street stations.

Table 1: Sample journey times after Crossrail

Source: Crossrail

	Journey time	Savings
Abbey Wood to Isle of Dogs	9 mins from 30	70%
Ealing Broadway to Farringdon	17 mins from 25	32%
Paddington to Liverpool Street	11 mins from 17	35%

Crossrail will do more than reduce journey times. The range of destinations within easy reach of central London will grow significantly, giving businesses access to a wider labour pool and customer market. People will find parts of outer London more appealing as places to live. Current residents will similarly benefit from improved access to job opportunities.

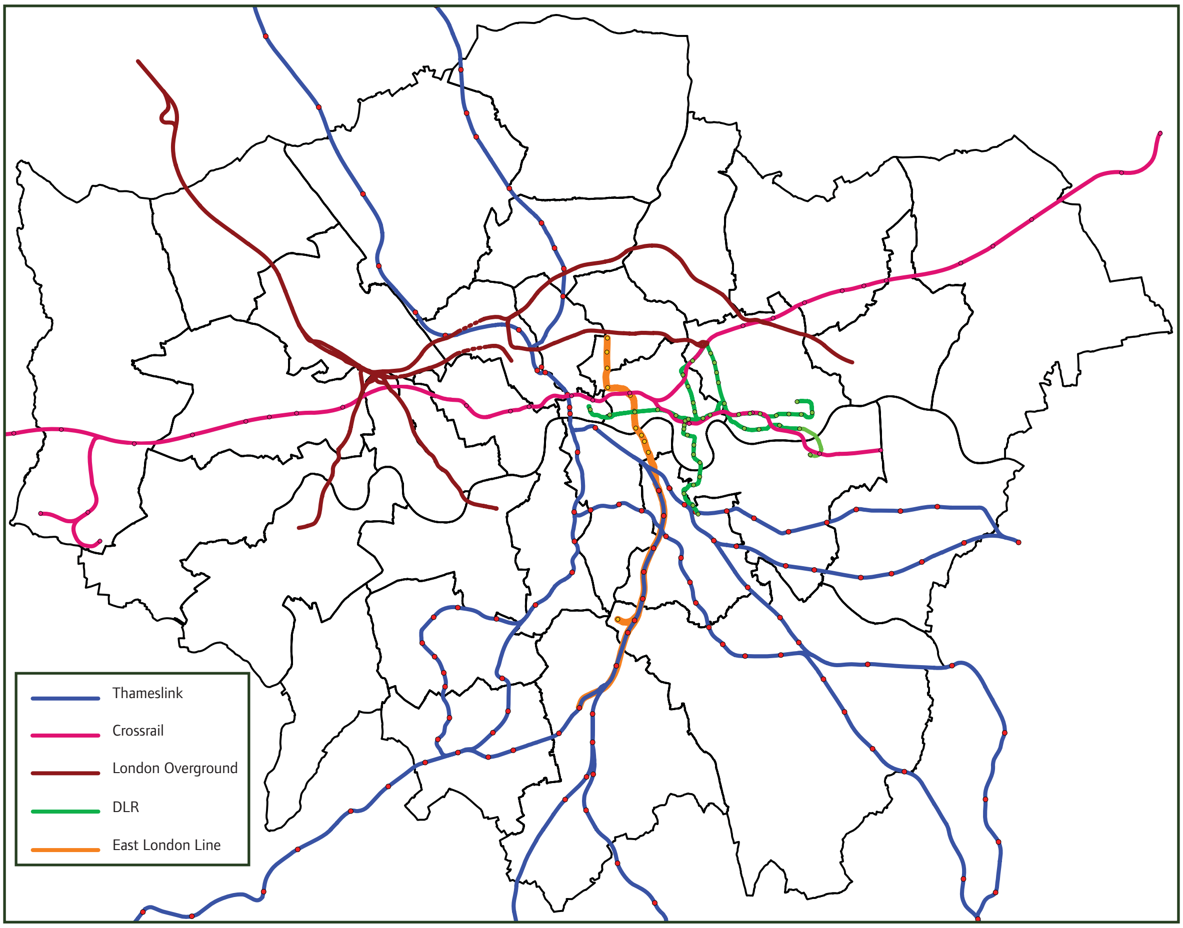
The Business Plan also confirms plans to add a third carriage to trains on the whole of the Docklands Light Railway (DLR). This is effectively a 50 per cent increase in capacity to the fast-growing DLR, which carried 66 million passengers last year. Work is already underway on the crowded Bank/Tower Gateway to Lewisham branch. Two extensions to the DLR are in progress now, to Woolwich Arsenal (opening early 2009) and Stratford International (2010). The extension to Woolwich will drastically reduce journey times from Woolwich Arsenal: from 45 to 20 minutes to Stratford and from 40 to 20 minutes to Canary Wharf. This will give residents access to a greater range of employment opportunities and make Woolwich a more desirable place to live. The service to Stratford International will link up with the existing network at Canning Town, replacing the former North London Line service. Higher frequency and new intermediate stops will facilitate residential development here.

Transport for London will also continue to invest in London Overground, a national rail franchise it took responsibility for last year that includes the North London Line. TfL has invested in station renovations and improved lighting and security. It has also introduced Oyster cards to the network and is awaiting new rolling stock for the line. London Overground is planned to become a high frequency service improving on today's four trains per hour. The East London Line, formerly part of the Underground, is being extended north from Shoreditch to Dalston in Hackney and south to Crystal Palace and Croydon in 2010 and will become an integral piece of the expanding orbital railway when it is linked to the North London Line in 2011. The East London Line extension will improve access to much of inner London, giving current residents better access to employment opportunities while also making these areas more appealing as residential areas. The North and East London lines are each forecast to carry more than 30 million passengers annually. Plans to extend the London Overground service from Surrey Quays to Clapham Junction are not fully funded.

On the roads, Transport for London will be widening its focus on traffic congestion to the whole of Greater London. Peak-hour traffic congestion is a problem on much of London's core road network, particularly around town centres, and causes significant delays for residents and businesses. The timing and phasing of thousands of traffic signals is being tested in an effort to improve traffic flow and make more of the road network.

Figure 3: The geography of transport investment

Source: TfL



Beyond TfL's investments, London also stands to gain from Government investment in the National Rail network as the Thameslink Programme gets underway, a new high-speed rail service to Kent launches and more train carriages are put on commuter services.

The much-anticipated Thameslink Programme will improve north/south transport in the Capital along its route from Bedford to Brighton. The large scheme is set to dramatically increase capacity on the route, especially in central London. But it will also bring commuter services further into the centre of the City. From March, some trains operated by Southeastern from Kent and South London will continue beyond Blackfriars station to the north of London or beyond.

On the core 'Thameslink' route from Bedford, trains will be extended to 12 carriages by 2012, increasing capacity by 50 per cent. Extending trains will require upgrades at Blackfriars and Farringdon stations, which will cause significant disruption in the short term. The last of the Programme work finishes in 2015 when a new viaduct near London Bridge will allow for more frequent trains. Upon completion, 24 trains per hour will operate in the core section, with commuter services from the south and east running through central London rather than terminating at London Bridge as they do now. A new franchise for the line will be awarded in 2015 so there may be more changes to destinations served.

All of London's commuter rail services will benefit from hundreds of new train carriages. The Government announced in 2007 that 1,300 new carriages would be put in service with around 70 per cent going to services terminating in London. This will bring welcome relief to overcrowding on London's commuter rail services.

Finally, one of the more immediate changes will occur in 2009 when a high-speed rail service will commence from St Pancras to serve the eastern half of Kent. This will cut travel time significantly to some distant towns and expand London's traditional commuting belt east.

Table 2: Sample journey times on the Southeastern high-speed service to London

Source: Southeastern Railway

	Journey time	Savings
Ramsgate to London	84 mins from 130	35%
Dover Priory to London	74 mins from 112	34%
Ashford to London	37 mins from 83	55%

Together, these investments will do much to improve transport in London. Significant new capacity will be delivered to central London, which will reduce overcrowding and allow more employment growth in the most productive region in the country. Some limited expansion of the network will improve access to parts of inner and East London, giving residents better access to employment and social opportunities. However, the benefits will take time and will not fully materialise until 2022 when the last of the Tube upgrades are complete.

Transport for London's new Business Plan leaves little extra funds to plan future investment beyond 2017/18, apart from new capacity upgrades to the Northern Line. The Mayor's focus on delivery of current funded projects should ensure successful completion. TfL will need to monitor London's longer-term transport requirements as transport projects are slow in planning and take a long time to implement. So even in the midst of an economic downturn, it is important that transport investment in London continues so that long-term economic, population and employment growth can be accommodated.

Table 3: Project timeline

Source: TfL

Project	Scheduled End
Kent high-speed rail	2009
DLR Woolwich extension	2009
DLR three-car upgrade	2010
DLR Stratford International extension	2010
East London Line Phase 1	2010
East London Line Phase 2	2011
Traffic signal rephasing	2012
New National Rail carriages	2014
Thameslink	2015
Crossrail	2017
Tube upgrades	2022

Additional information

Data sources

Tube and bus ridership	Transport for London on 020 7222 5600 or email: enquire@tfl.gov.uk
GDP/GVA growth	Experian Business Strategies on 020 7630 5959
Tourism – overseas visitors	www.statistics.gov.uk
Tourism – domestic visitors	www.visitlondon.com
London airports	www.caa.co.uk
Business activity	www.rbs.co.uk/pmireports
Unemployment rates	www.statistics.gov.uk

Glossary

Civilian workforce jobs

Measures jobs at the workplace rather than where workers live. This indicator captures total employment in the London economy, including commuters.

Claimant count rate

Unemployment rate based on the number of people claiming unemployment benefits.

Employee jobs

Civilian jobs, including employees paid by employers running a PAYE scheme. Government employees and people on training schemes are included if they have a contract of employment. Armed forces are excluded.

Gross domestic product (GDP)

A measure of the total economic activity in the economy.

Gross value added (GVA)

Used in the estimation of GDP. The link between GVA and GDP is that GVA plus taxes on products minus subsidies on products is equal to GDP.

ILO unemployment rate

The International Labour Organisation's calculation of the number of people out of work.

Tube ridership

Transport for London's measure of the number of passengers using London Underground in a given period. There are 13 periods in a year. In 2008/09 there are eleven 28-day periods, one 26-day period and one 31-day period. Period 1 started on 1 April.

Bus ridership

Transport for London's measure of the number of passengers using buses in London in a given period. There are 13 periods in a year. In 2008/09 there are eleven 28-day periods, one 26-day period and one 31-day period. Period 1 started on 1 April.

Acronyms

ABI	Annual Business Inquiry
BAA	British Airports Authority
BCC	British Chamber of Commerce
BITOA	British Incoming Tour Operators Association
CAA	Civil Aviation Authority
CBI	Confederation of British Industry
DCLG	Department for Communities and Local Government
EBS	Experian Business Strategies
GDP	Gross domestic product
GVA	Gross value added
ILO	International Labour Organisation
IMF	International Monetary Fund
LCCI	London Chamber of Commerce and Industry
LET	London's Economy Today
MPC	Monetary Policy Committee
ONS	Office for National Statistics
PMI	Purchasing Managers' Index
PWC	PricewaterhouseCoopers
RICS	Royal Institution of Chartered Surveyors

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75	Pre-Budget report 2008

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