

London's Economy Today



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Persistent inflation – a further brake on a slowing economy

by Richard Davies, Economist, Gordon Douglass, Economist
and Christopher Lewis, Senior Economist

Rising inflation is being driven by higher food, oil, gas and commodity prices. Inflationary pressures are currently a worldwide phenomenon and, alongside the credit crunch, are placing major strains on economies across the globe. UK CPI annual inflation rose from 3.0 per cent in April to 3.3 per cent in May (see Figure 1). Meanwhile in the Eurozone, inflation has reached 3.7 per cent and in the US, inflation is 4.2 per cent. Inflation is constraining the ability of central banks to cut interest rates to support growth at a time when economies are slowing down and it could even lead to interest rate hikes, especially by the European Central Bank.

GLAECONOMICS

Latest news...

● Credit crunch and the property market report

This report provides an assessment of the consequences of the credit crunch for the property market in London and the implications that has for policy.



● Working Paper 31: Employment in London by firm size

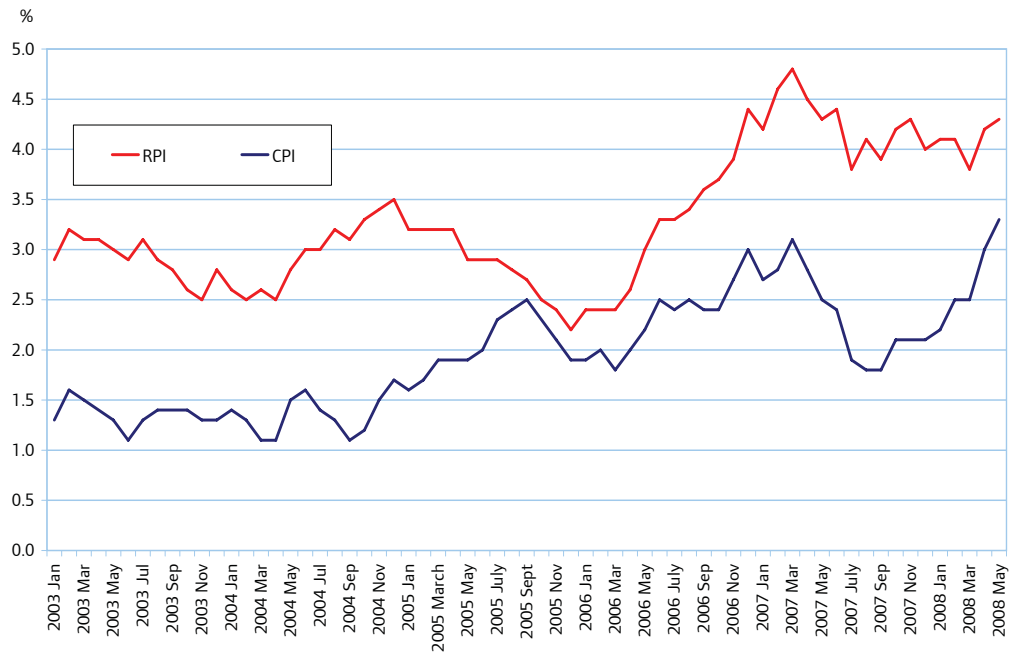
This paper provides an important advance: it is the first time that both the enterprise and local unit data from the Inter Departmental Business Register (IDBR) have been combined within one methodology in order to compile a robust dataset of London employment by firm size.



Visit www.london.gov.uk/mayor/economic_unit to download these publications.

Figure 1: UK annual inflation rates

Source: ONS



Rising inflation expectations whilst growth forecasts are revised downwards

With annual CPI inflation now more than 1 per cent above the Government's 2 per cent target the Governor of the Bank of England was required to write an open letter to the Chancellor of the Exchequer explaining why inflation had moved away from the target. The letter stated that inflation is likely to rise sharply in the second half of this year, to above 4 per cent and to remain markedly above the target well into 2009. With inflation remaining above target for so long the Bank of England is concerned that inflation expectations will continue to rise and become hard to dislodge. In June's Bank of England/GfK NOP Inflation Attitudes survey, households' perceptions of inflation over the past year and their expectations for inflation over the next year rose to their highest levels since the survey began in 1999. The perception of the current level of annual inflation was 4.9 per cent and the expectation of annual inflation in a year's time was 4.3 per cent. This suggests that any further early cut in UK interest rates seems highly unlikely making a sharper more prolonged downturn for the economy over the next couple of years a much more likely outcome.

In June the OECD forecast that UK growth will slow to 1.8 per cent in 2008 and then to 1.4 per cent in 2009 and that property prices will fall by 10 per cent by the end of 2009. Despite the majority of growth forecasts being revised downwards the risks are still that the slowdown will be even more severe than most forecasters predict.

Signs of acute weakness in the construction industry

The Construction Products Association (CPA) has forecast that house building will decline by 27 per cent in 2008 to a post Second World War low of 147,000 new dwellings. The credit crunch, lower mortgage availability and the low level of social housing schemes have been cited as factors for this collapse. Michael Ankers, the CPA's chief executive said "The impact on the new-build housing market has been more severe than any of us anticipated".

Consumer confidence is falling sharply

The British Retail Consortium's consumer confidence index has dropped dramatically. Major concerns mentioned by respondents were the state of the economy and personal debt problems. Meanwhile GfK NOP's consumer confidence index fell to an 18-year low in May. Falling consumer confidence is expected to negatively impact on consumption growth during the rest of this year and in 2009.

London rated as the world's most influential financial centre

MasterCard's second annual ranking of financial centres has again placed London as the most influential centre on the planet. The index covers 75 cities and ranks them according to their legal and political frameworks, economic stability, ease of doing business, the financial flows in the city, their reputation as a business centre, their impact on knowledge creation, and their liveability. The report noted that London benefited from "a strong and secure economy, vibrant financial markets and a legal and political framework that supports high levels of international trade". It further observed that "the City significantly outperforms its rivals in most dimensions, with liveability as the most prominent area for improvement when compared to other top cities." New York was placed second, whilst Shanghai jumped eight places to twenty fourth.

Testing times lie ahead for the London economy

The outlook continues to remain gloomy for the UK and London economies. The OECD has recently downgraded its growth forecasts for the UK to well below 2 per cent in 2008 and 2009. Weaker growth can also be expected for the London economy due to the ongoing credit crunch and its exposure to the financial services sector. The rise in world commodity prices such as oil has caused inflation to surge in most economies, including the UK where CPI inflation is likely to rise to above 4 per cent by the end of this year. With the Bank of England concerned that higher current inflation will embed itself into the economy via increasing inflation expectations, companies' higher price setting perceptions and the possibility of significant wage demands, further interest rate cuts in the near future seem unlikely. The next change in interest rates could even be an upward movement something that was not being considered a couple of months ago. Rising inflation will squeeze real incomes and with consumer confidence already falling, consumption growth, which has been a major driver of the economy, should ease. The housing market is expected to remain depressed over the coming year with the availability of mortgage finance remaining tight due to the credit crunch. Commercial property prices continue to fall sharply so the prospects for the private construction sector look weak. Housebuilders are already cutting back on their building programmes and laying off workers. London's economy therefore faces tough times with the overall slowdown expected to continue well into 2009.

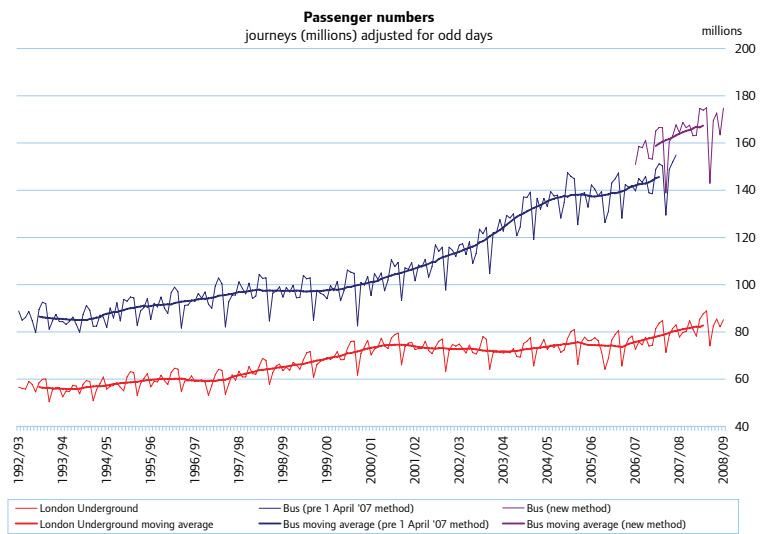
Economic indicators

Increase in moving average of passenger numbers

- The most recent 26-day period is from 1 April 2008 to 26 April 2008. Adjusted for odd days, London's Underground and buses had 259.9 million passenger journeys; 174.8 million by bus and 85.1 million by Underground.
- The moving average of passengers every period increased to 250.1 million from a downwardly revised 248.7 million passengers every period. The moving average for buses was 167.4 million. The moving average for the Underground was 82.7 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 edition 58 (June 2007).

Latest release: June 2008

Next release: July 2008



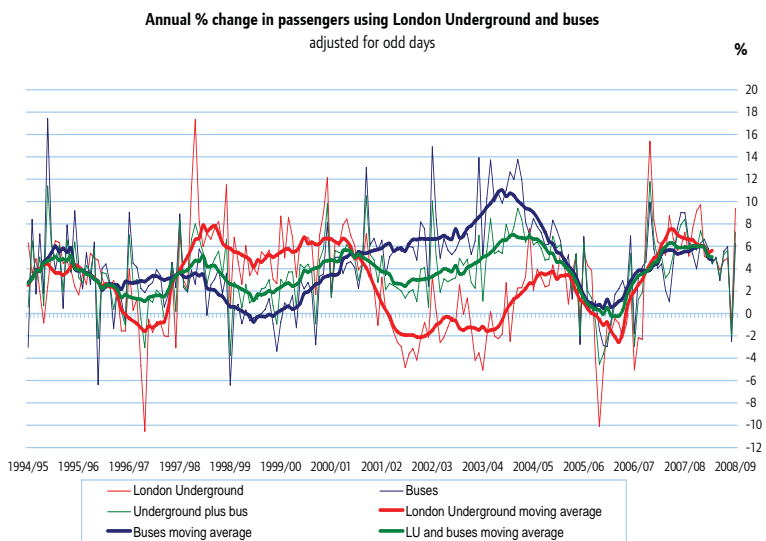
Source: Transport for London

Average annual growth rate of passengers remains constant

- The moving average annual rate of growth in passenger journeys remained at 5.1%.
- The moving average annual rate of growth in bus passenger journey numbers decreased to 4.8% from a downwardly revised 5.0% in the previous period.
- The moving average annual rate of growth in Underground passenger journey numbers increased to 5.6% from an upwardly revised 5.5% in the previous period.

Latest release: June 2008

Next release: July 2008



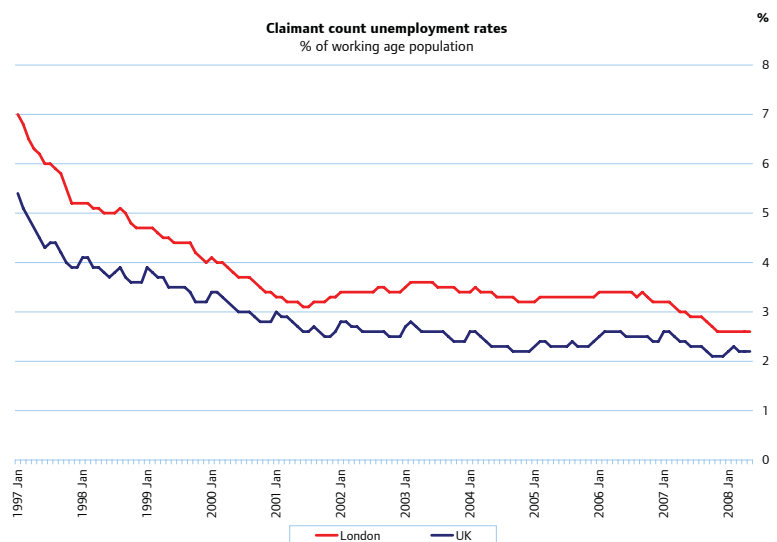
Source: Transport for London

Claimant count unemployment

- The rate of claimant count unemployment (the percentage of resident working age population who are unemployed and claiming Jobseekers' Allowance) in London was 2.6% in May 2008.
- There were 130,500 unemployment claimants in London in May 2008 compared with 150,600 in May 2007.
- The claimant count unemployment rate of the UK remains below that of London.

Latest release: June 2008

Next release: July 2008

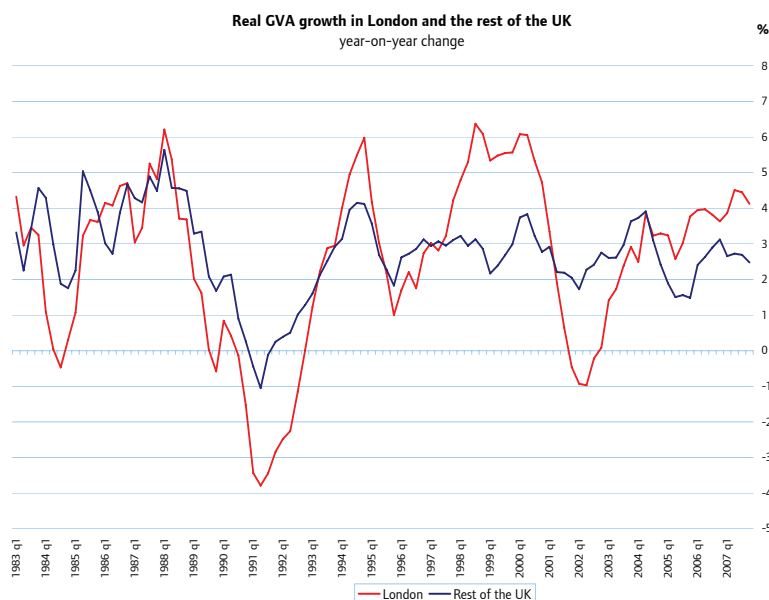


Source: Claimant Count, NOMIS

Annual growth in London quicker than the rest of the UK

- London's annual growth in output decreased to 4.1% in Q4 2007 from a downwardly revised 4.4% in Q3 2007.
- The rest of the UK's annual growth in output decreased to 2.5% in Q4 2007 from a downwardly revised 2.7% in Q3 2007. London has been growing at a faster annual rate than the rest of the UK since Q3 2004.
- There have been revisions to previous growth rates to reflect the availability of new data.

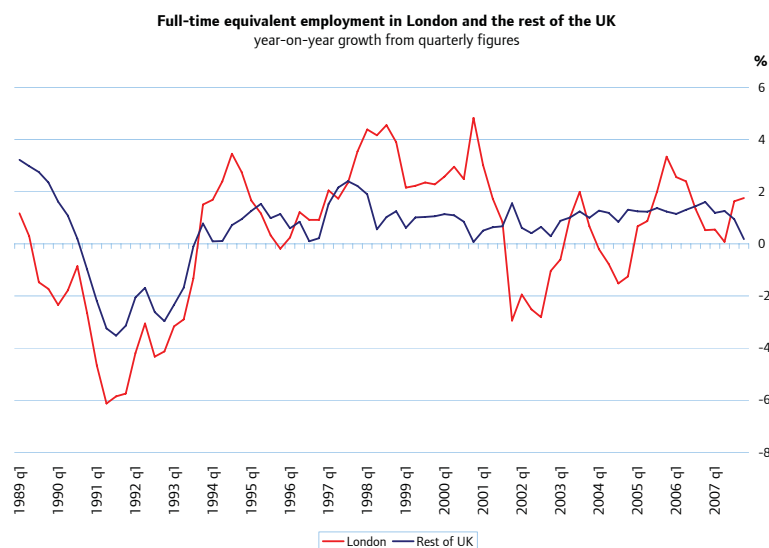
Latest release: May 2008
Next release: August 2008



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

- London's annual employment growth increased to 1.8% in Q4 2007 from 1.6% in Q3 2007.
- Annual employment growth in the rest of the UK decreased to 0.2% in Q4 2007 from an upwardly revised 0.9% in Q3 2007.
- There have been revisions to previous growth rates to reflect the availability of new data.

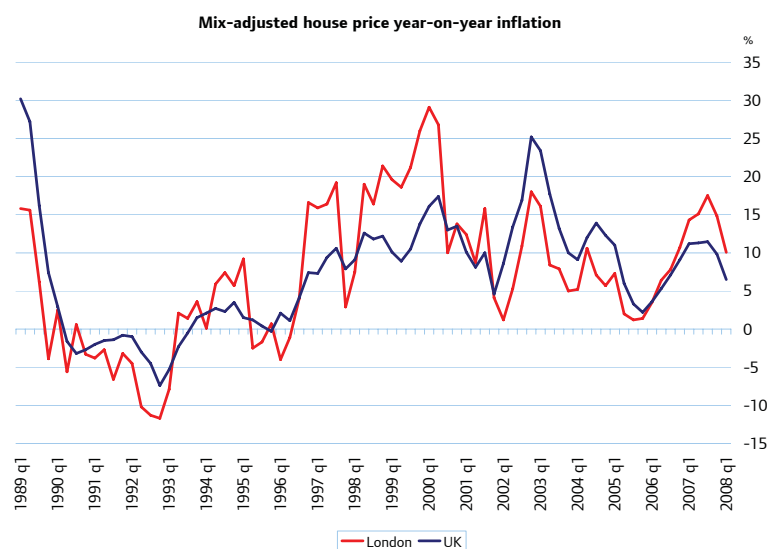
Latest release: May 2008
Next release: August 2008



Annual house price inflation slowing sharply

- The Department for Communities and Local Government (DCLG) house price index is an official measure of house prices. It is available up to Q1 2008.
- The DCLG reported a decrease in annual house price inflation in London and the UK in Q1 2008.
- Annual house price inflation in London decreased to 10.1% in Q1 2008 from a downwardly revised 14.8% in Q4 2007. Annual house price inflation in the UK decreased to 6.5% in Q1 2008 from a downwardly revised 9.8% in Q4 2007.

Latest release: May 2008
Next release: August 2008

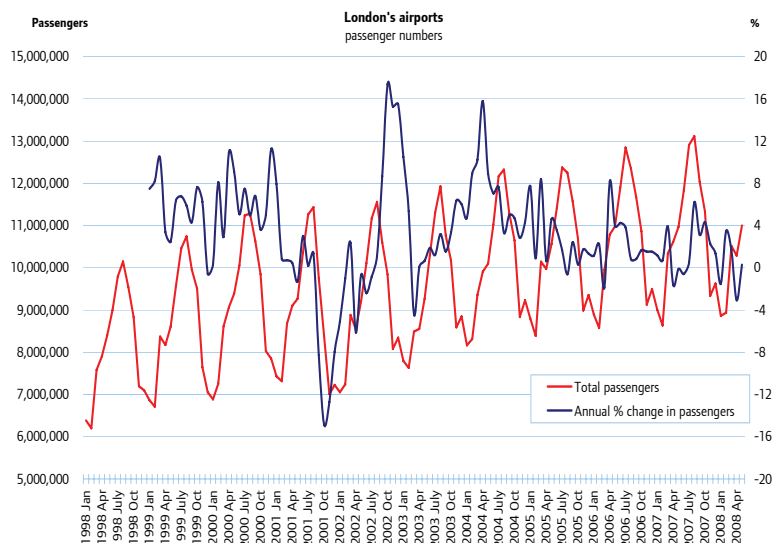


Positive annual growth in airport passenger numbers

- 11.0 million passengers travelled through London's airports in May 2008.
- The number of passengers using London's airports increased by 0.3 per cent from May 2007 to May 2008.
- The number of passengers using London's airports year-on-year has increased again from a fall in April.

Latest release: June 2008

Next release: July 2008



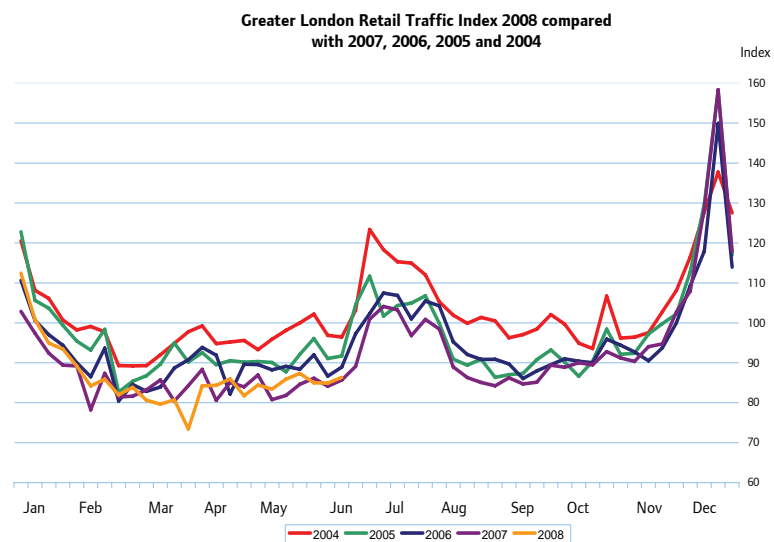
Source: Civil Aviation Authority

SPSL Retail Traffic similar to 2007 levels

- The SPSL Retail Traffic Index of shoppers in London was 86.3 in the second full week of June compared to 84.9 in the previous week.
- The index has been quite similar to 2007 levels this year.
- SPSL's Retail Traffic Index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: Mid-June

Next release: Weekly



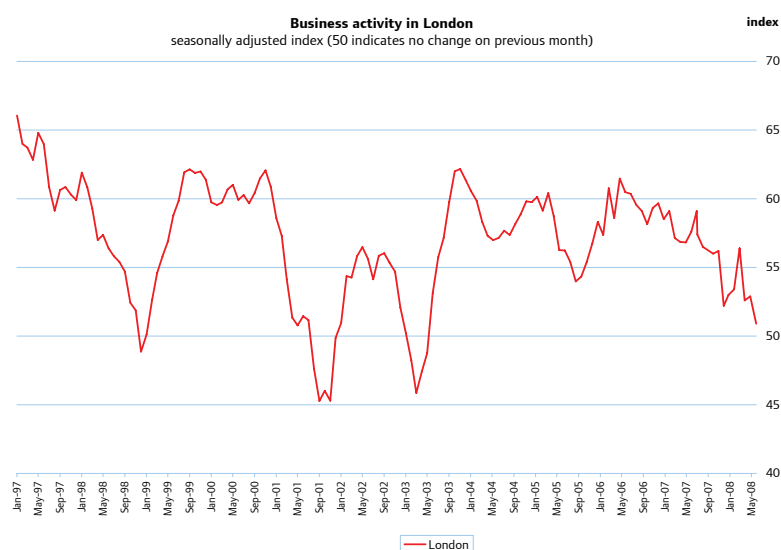
Source: SPSL

London's business activity slows down

- London firms continued to expand their output of goods and services in May 2008, but at a slower rate than in April.
- The Purchasing Managers' Index (PMI) of business activity recorded 50.9 in May compared to 52.9 in April.
- A rate of above 50 on the index indicates an increase in business activity from the previous month. The PMI for business activity has been above 50 since June 2003.

Latest release: June 2008

Next release: July 2008



Source: The Royal Bank of Scotland /NTC Economics

London employment weakens

- The PMI shows that the level of employment in London firms was below the 50 mark in May 2008 for the first time since August 2005.
- The PMI for the level of employment was 49.1 in May compared to 52.3 in April.
- A rate of below 50 on the index indicates a decrease in the level of employment from the previous month.

Latest release: June 2008

Next release: July 2008



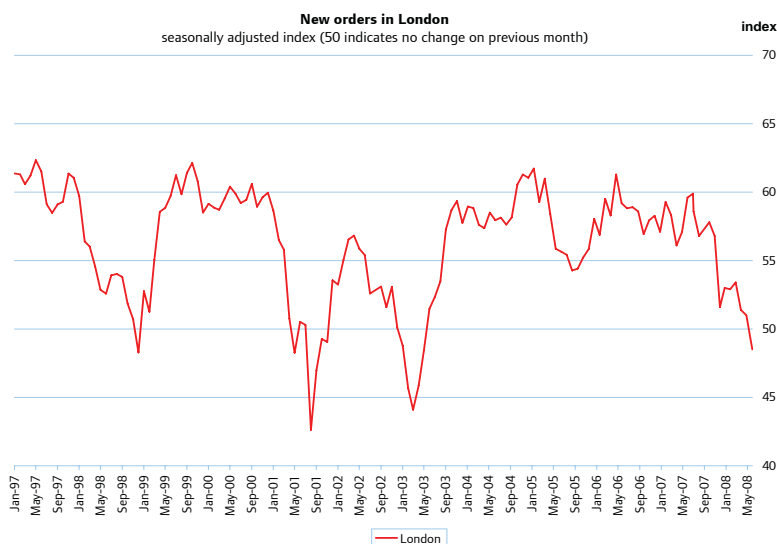
Source: The Royal Bank of Scotland /NTC Economics

New orders in London decreasing

- May 2008 saw a fall in new orders for London firms for the first time since May 2003.
- The PMI for new orders recorded 48.5 in May 2008 compared to 51.0 in April 2008.
- A rate of below 50 on the index indicates a decrease in new orders from the previous month.

Latest release: June 2008

Next release: July 2008



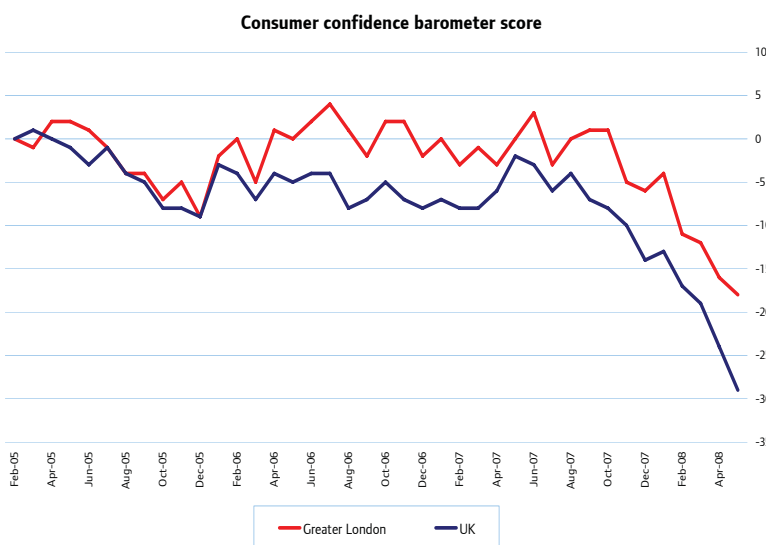
Source: The Royal Bank of Scotland /NTC Economics

Consumer confidence continues to fall

- 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 above zero signifies a positive change in views.
- For Greater London the consumer confidence score decreased to -18 in May from -16 in April.
- For the UK the consumer confidence score fell to -29 in May from -24 in April.

Latest release: May 2008

Next release: June 2008



Source: GfK NOP on behalf of the European Commission

The evolution of UK and London employment rates

Lubomira Chirmiciu,
Economist

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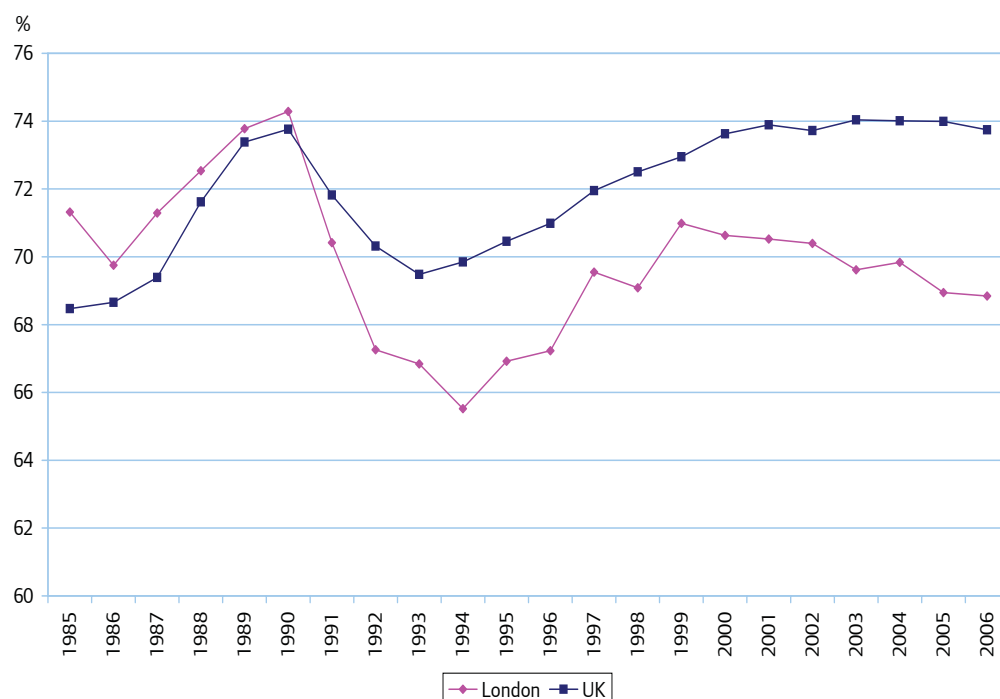
The evolution of London and UK employment rates presents an interesting puzzle: why did the employment rate in London fall below that of the UK in the early 1990s and why has it not matched the UK rate ever since? A forthcoming GLA Economics report looks at this issue using data from the Labour Force Surveys (LFS) which, despite existing discontinuity issues, change of definitions and variables over time, is broadly consistent over time¹.

London's employment rate is lower than that for the UK

Figure 2 shows that while the employment rate in London exceeded that for the UK until 1990, London's employment rate declined much faster in the 1990-1994 period. After a short period of convergence (1994-1999), the gap between the employment rate for London and that for the UK continued to increase, reaching a 5 percentage point gap in favour of the UK in 2006.

**Figure 2: Employment rates
1985-2006**

Source: LFS, UK data archive



The female employment rate is largely responsible for the continuing divergence

An analysis of male and female employment rates provides a useful insight into the dynamics of labour market trends in London and the UK. While for males the gap between UK and London employment rates has been relatively small and stable since the mid 1990s (Figure 3), for females this gap has been steadily increasing over time (Figure 4).

Figure 3: Employment rates of males, 1985-2006

Source: LFS, UK data archive

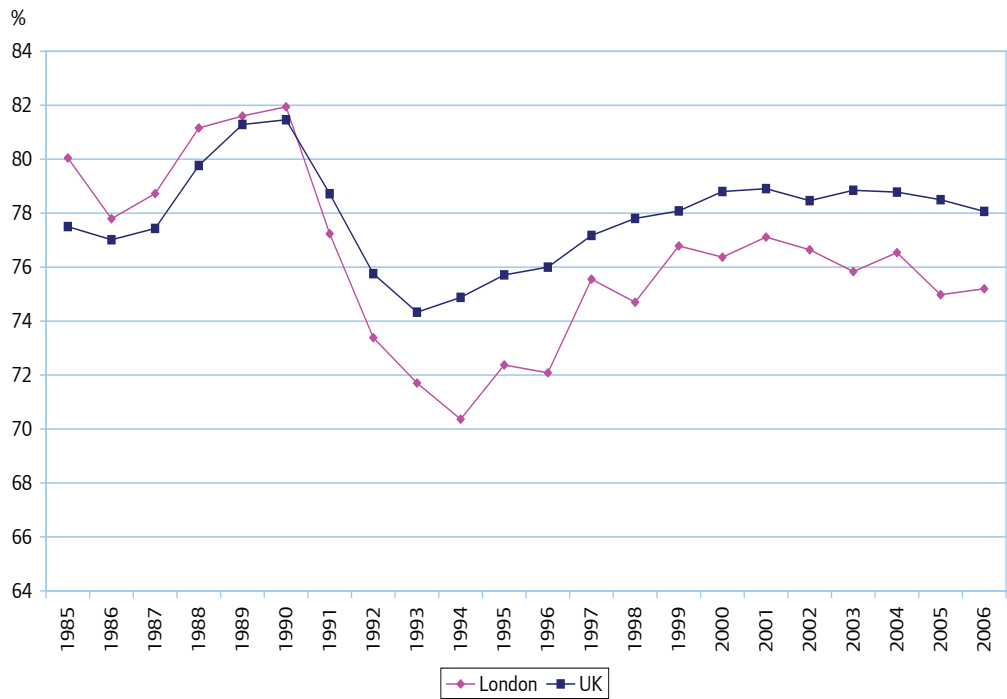
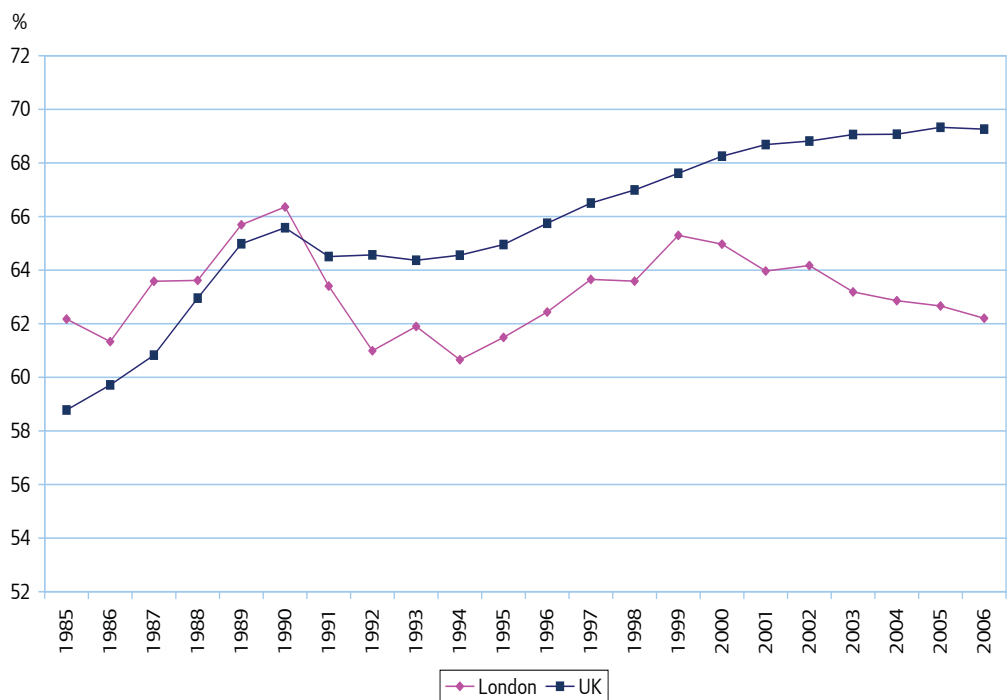


Figure 4: Employment rates of females, 1985-2006

Source: LFS, UK data archive



Whilst the decrease in London’s employment rate started with a substantial fall in both male and female employment rates between 1990 and 1994, in the main, female employment rates are responsible for the continuing divergence of UK and London employment rates. This is illustrated by Figure 5, which shows that until the turn of the millennium, the employment rate for males and females in London had moved in a similar fashion when compared to the employment rate for males and females in the UK as a whole. However, since the turn of the millennium the gap between the female employment rate for London and the female employment rate for the UK has grown to a much greater extent than for men.

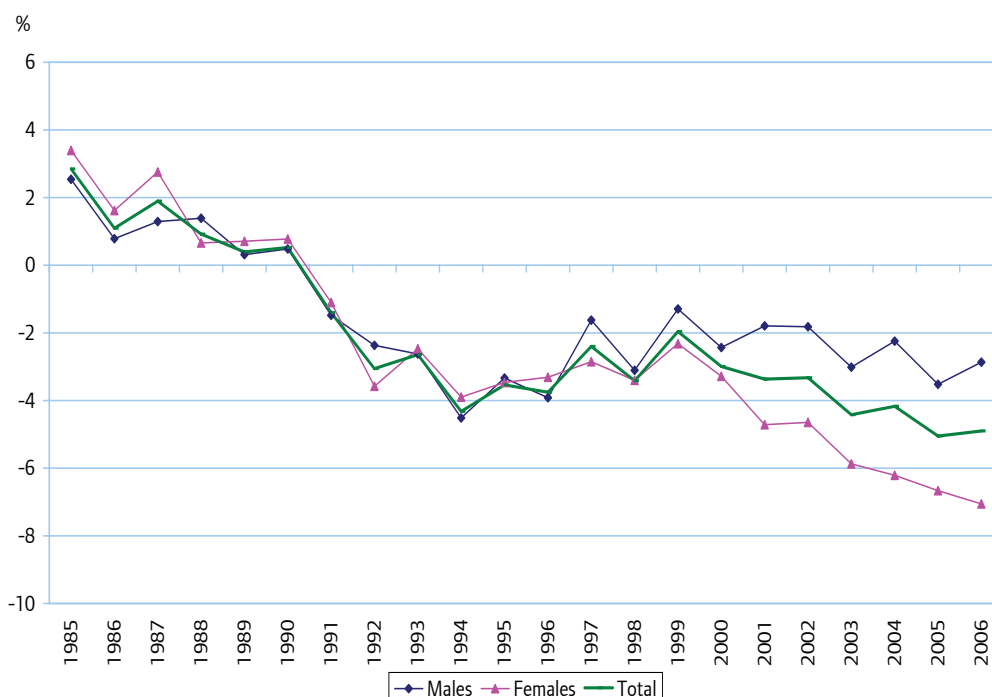
Figure 5: Employment rate gaps (London-UK) percentage points

Source: LFS, UK data archive

Note: The 'Males' line shows London's male employment rate minus the UK's male employment rate.

The 'Females' line shows London's female employment rate minus the UK's female employment rate.

The 'Total' line shows London's total employment rate minus the UK's total employment rate.



Sector analysis

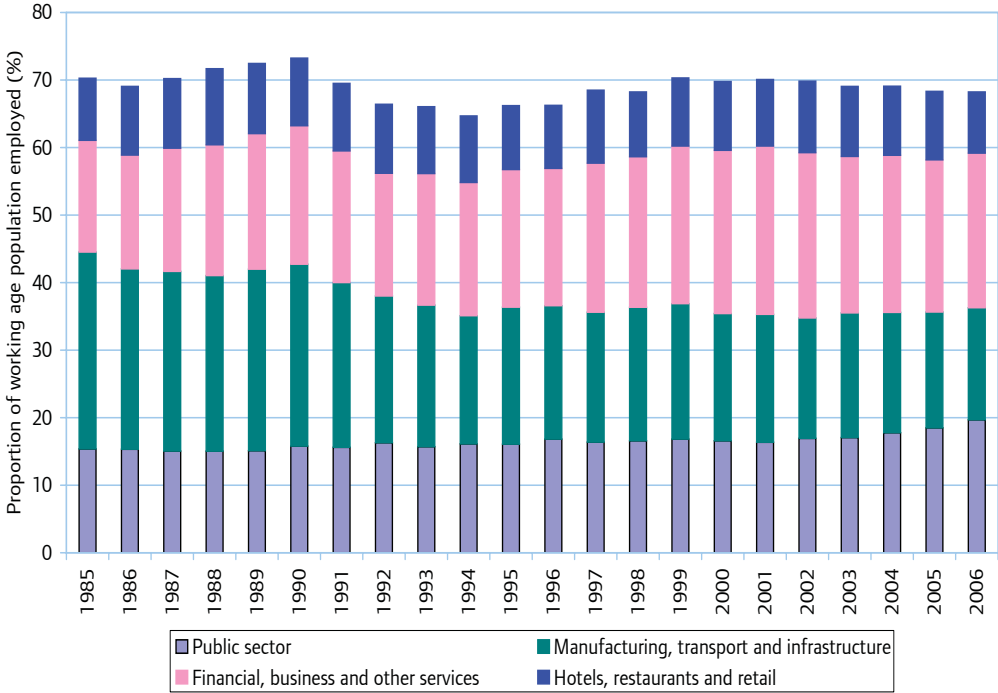
As well as male and female employment rates, the forthcoming report focuses on employment rates and growth in employment levels across four broad groupings of sectors: 'manufacturing, transport and infrastructure'; 'financial, business and other services'; 'hotels, restaurants and retail' and the 'public sector'. Figure 6 shows the relative contribution of each sector to London's overall employment rate; it shows the proportion of London's working-age population employed in each of the four major sectors.

In the 1985-1991 period the 'manufacturing, transport and infrastructure' sector contributed most to London's employment rate but experienced a sharp decline between 1990 and 1994.

The subsequent period of 1995-2006 is characterised by a further decline in 'manufacturing, transport and infrastructure', an increase in 'financial, business and other services', mainly between 1996 and 2001 and some public sector growth. The proportion of London's working age population employed in the 'hotels, restaurants and retail' sector has remained stable at around 10 per cent throughout the whole period.

Figure 6: Sector composition of London's employment rate (%)

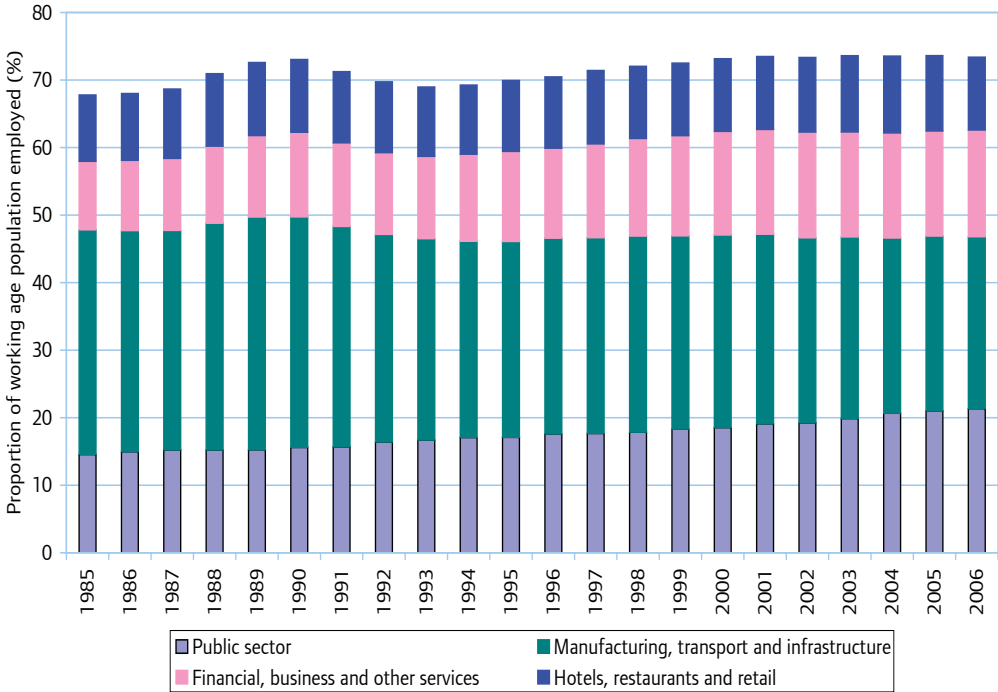
Source: LFS, UK data archive



In contrast to London, ‘manufacturing, transport and infrastructure’ remains the most significant contributor to the UK employment rate (Figure 7). The decline of the ‘manufacturing, transport and infrastructure’ sector in the UK has been much less pronounced than for London. The contribution of the ‘financial, business and other services’ sector to the UK employment rate is lower than for London. In contrast to London, the contribution of the public sector to the UK employment rate is higher. The contribution of the ‘hotels, restaurants and retail’ sector to the UK employment rate is similar to that for London.

Figure 7: Sector composition of the UK employment rate (%)

Source: LFS, UK data archive



London-UK employment rate gaps

Figure 8 presents an overall picture of the difference between the employment rates for London and the UK over time across the four broad sector groups. The gap in total employment rates between London and the UK has a general downward trend starting at 2.8 percentage points in 1985 in favour of London, and deteriorating to -4.9 percentage points in favour of the UK in 2006.

The employment rate gap in 'manufacturing, transport and infrastructure' deteriorated mainly between 1985 and 1994. Since 1994, the gap between the proportion of London's working-age population employed in the 'manufacturing, transport and infrastructure' sector and that for the UK as a whole, has remained about the same (at around 9 percentage points).

Figure 8: Employment rate gaps (London-UK) (percentage points)

Source: LFS, UK data archive

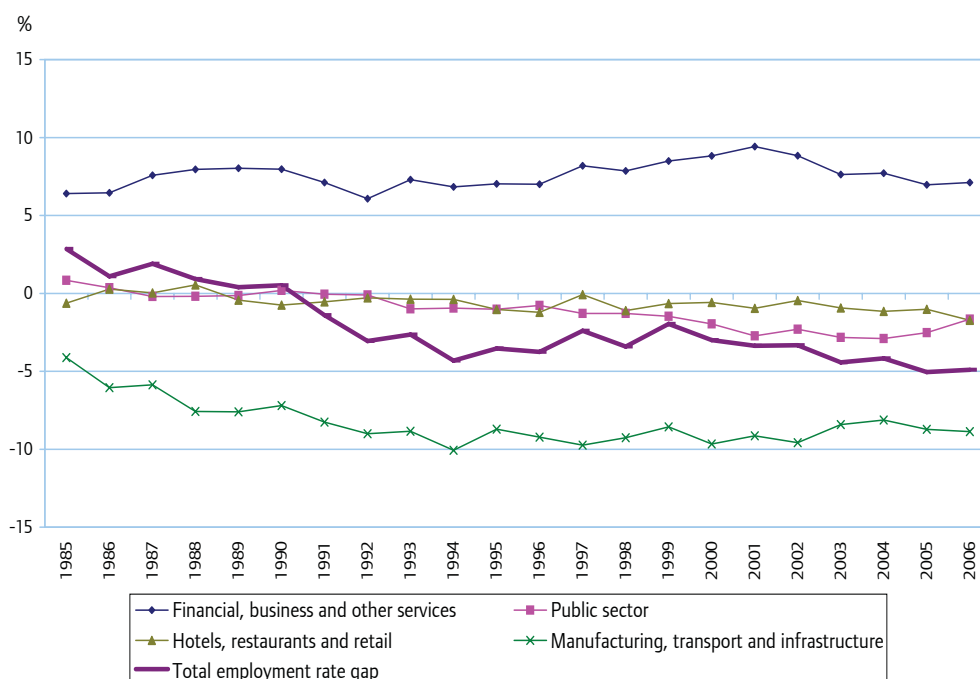


Figure 8 shows that the proportion of the working-age population employed in the 'financial, business and other services' in London was higher than that in the UK throughout the whole 1985-2006 period.

The proportion of the working-age population employed in the 'hotels, restaurants and retail' sector in London has been similar to that for the UK for most of the period.

Whilst the proportion of the working-age population employed in the public sector in both London and the UK was similar between 1985 and 1991, the data for the period of 1992-2006 show that a higher proportion of the UK working-age population was employed in the public sector than was the case for London.

Footnotes

1 For more detailed information see the forthcoming GLA Economics Working Paper 'The Evolution of UK and London employment rates'.

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
House prices	www.nationwide.co.uk/hpi/
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 will be 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 will be eleven 28-day periods, one 26-day period and one 31-day period. Period 1 started on 1 April.

Acronyms

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

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GLA Economics provides expert advice and analysis on London's economy and the economic issues facing the capital. Data and analysis from GLA Economics provide a sound basis for the policy and investment decisions facing the Mayor of London and the GLA group. The unit was set up in May 2002.

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