

London's Economy Today



Issue 43 | March 2006

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Budget 2006 – London in Focus

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Last week the Chancellor presented his tenth Budget – but just how likely are his predictions? This month's *London's Economy Today* explores the Budget and looks at the three Treasury reports published at the same time. Following the Budget, we analyse some key London economic indicators including tube use. And finally, this month's supplement, *Ready for Retail*, summaries GLA Economics' work in this key London sector including our latest report: *Small Retailers in London*.

Capital focus

For Londoners, perhaps the most noticeable feature of the Budget was the focus on London issues found in three Treasury reports published alongside the Budget:

- Analysing labour market trends in London
- Financial services in London: Global opportunities and challenges
- Meeting the regional economic challenge: The importance of cities to regional growth.

GLAECONOMICS

Latest news...

Don't miss your copies of GLA Economics' latest reports:

- Retail in London: Working Paper G – Small Retailers
- Retail in London: Working Paper F – International Comparisons of Retail
- Retail in London: Working Paper E - Retail and the Labour Market
- Business and economic impacts of the congestion charge

Visit www.london.gov.uk/mayor/economic_unit, email glaeconomics@london.gov.uk or call +44 (0)20 7983 4922.

Key Points

- The Chancellor's forecasts for economic growth are identical to those presented in December's Pre-Budget Report (PBR). His forecasts for public borrowing are very similar to those set out in the PBR.
- GLA Economics projects that the Chancellor will just fail to meet his Golden Rule to borrow only to invest over the course of the current economic cycle.
- We predict that he will continue to meet his Sustainable Investment Rule, but by 2010/11 we project that public sector net debt will be just below the rule's 40 per cent ceiling. Hence the 2007 Comprehensive Spending Review should include a review of this 40 per cent ceiling in order to allow necessary investments, such as Crossrail.

The economy and public finances

The Chancellor's forecasts for economic growth for this year and next are identical to those in last December's PBR with his forecasts for public borrowing also being similar. But as Table 1 shows, his forecasts are generally more optimistic than the consensus amongst independent forecasters.

Chart 1. Projections of economic growth and public borrowing

Source: HM Treasury

	Economic Growth (%)		Public borrowing – PSNB (£ billion)	
	2006	2007	2006-07	2007-08
PBR 2005	2-2½	2¾-3¼	34	31
Consensus	2.2	2.3	38.3	36.6
Budget 2006	2-2½	2¾-3¼	36	30

Notes: Consensus = Consensus average of independent forecasts from the March 2006 HM Treasury survey; PSNB = Public Sector Net Borrowing

Will the Chancellor meet his fiscal rules?

The Chancellor has set out two key fiscal rules:

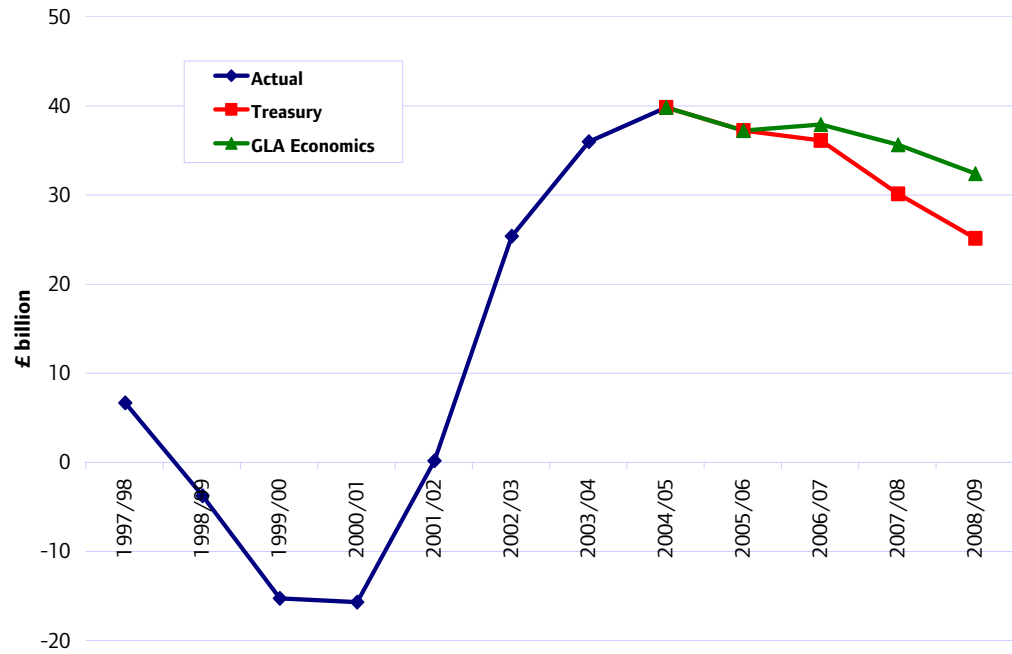
1) Golden Rule: Over the economic cycle, the Government will borrow only to invest and not to fund current spending.

2) Sustainable Investment Rule: Public sector net debt will be held over the economic cycle at a stable and prudent level which the Chancellor has defined as below 40 per cent of GDP.

In light of the 2006 Budget, GLA Economics has updated its economic growth and public borrowing projections starting from the consensus amongst independent forecasters as given in the March 2006 HM Treasury survey.

Our projections for public borrowing – as measured by public sector net borrowing (PSNB), the most commonly used measure of public borrowing – show it to be generally on a gradually declining path similar to the Treasury projections. However we project higher levels of borrowing than the Treasury for the financial years 2006/07 to 2008/09 – the last three years of the Treasury-defined current economic cycle.

Chart 1. Public Borrowing (PSNB)



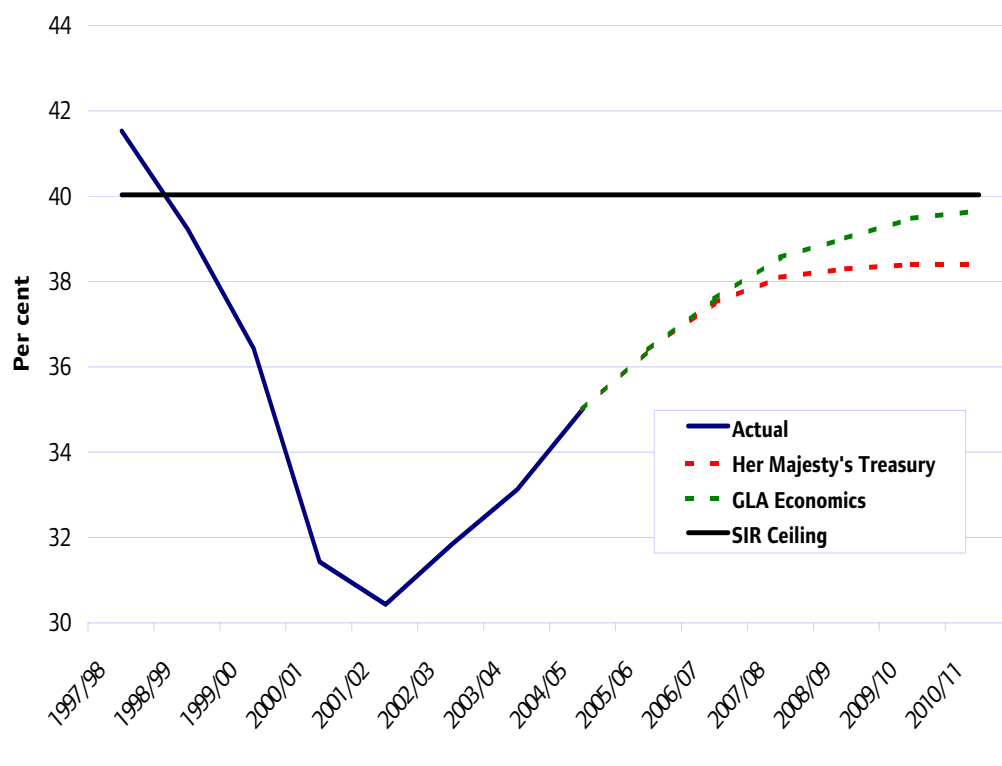
Our projections for higher levels of public borrowing will also feed through into the current budget – the relevant balance for assessing the Chancellor’s Golden Rule. *Consequently, we do not believe the Chancellor will meet his Golden Rule.* Our projections give an average annual surplus on the current budget for 1997/98 to 2008/09 of –0.02 per cent of Gross Domestic Product (GDP). In contrast, the Chancellor is projecting an average annual surplus on the current budget of around 0.1 per cent of GDP.

GLA Economics says...

GLA Economics says...

The actual economic consequence of the difference between our projected marginal failure of the Golden Rule as against the Chancellor’s projected marginal pass are insignificant and do not imply that the public accounts are out of control. PSNB reached 3.4 per cent of GDP in 2004/05 and we project that it will decline to 2.2 per cent by 2008/09 and to 1.8 per cent by 2010/11. Historically, we have seen much higher levels of borrowing.

Chart 2. Public Sector Net Debt (% of GDP)



GLA Economics says...

On our projections, the Chancellor will continue to meet his Sustainable Investment Rule to keep public sector net debt at a stable and prudent level which the Chancellor has defined as below 40 per cent of GDP. However, we do project public sector net debt reaching 39 per cent of GDP by 2008/09 and 39.7 per cent of GDP by 2010/11 – the last year of the 2007 Comprehensive Spending Review (CSR) period. Hence *the current 40 per cent ceiling in the sustainable investment rule will make it very, very difficult for the Government to invest in expensive but vital projects such as Crossrail*. A revision of the 40 per cent ceiling to a higher but still prudent level should be actively considered as part of the CSR 2007 process.

The next section of this overview looks at the three Treasury reports.

Treasury report: London's labour market

The GLA has long put the issues of poverty and worklessness in the capital on the public policy agenda, mostly recently in the GLA Economics *Worklessness in London* report¹. The key purpose of the Treasury paper is to ask why 'the gap in unemployment rates between London and the rest of the UK has narrowed, while the gap in economic inactivity rates has widened,' and to consider policies to correct this.

The report notes that:

- London 'is highly productive, and excels in high value added activities'
- London 'exploits its comparative advantage in high-skilled and capital-intensive work'
- 'Relatively low gains to work for some groups and the ease with which vacancies are filled in the capital' suggest an 'excess supply of low-skilled labour'.

The report acknowledges that *compositional factors* – that is a higher percentage of ‘people with characteristics known to be associated with labour market disadvantage’ and ‘people with multiple barriers to work’ – are found in London.

However it also identifies a *London factor* – ‘significant unexplained differences ...once differences in population characteristics are taken into account’. For example, in Inner London it finds that nine percentage points of the difference between the worklessness rate there, and that for the rest of the UK outside London, are due to *composition* overall – and 2.3 percentage points are due to a *London factor*.

GLA Economics says...

The report notes that the CSR 2007 ‘provides a basis for coordinated action to tackle the challenges facing London.’ *This is a welcome opportunity for the GLA to progress issues around worklessness and poverty, especially child poverty which remains a key London concern.*

Treasury report: Financial services in London

The Treasury paper recognises that the world economy is changing rapidly. It is important that Britain adapts to these changes to remain a competitive business location.

Britain has a history of being at the centre of global trade. This leads to important opportunities for its financial services sector, and especially those located in London. London is the world’s leading international financial centre. The Government is committed to making it even more successful. It recognises the need for policies that can support London’s competitiveness.

GLA Economics says...

The GLA supports these themes as we have long argued that the financial and business services sector is an essential part of London’s (and indeed the UK’s) competitive advantage and London’s world city role.

The Government proposes a new strategy for London to be developed and implemented by a high level group representing the capital’s key interests by summer 2006. This strategy will identify priorities and actions, promoting London around the world as a centre for financial services and supporting firms in financial and business services in the capital.

In the financial services report, the Government has committed to providing supportive policies to maintain London’s competitiveness. This recognition of London’s importance provides a very helpful context for discussions relating to London’s need for additional public investment, which can be pursued by the GLA and other London stakeholders in CSR 2007.

Treasury Report: The importance of cities to regional growth

The Treasury report notes that the majority of English people live and work in cities, and that the benefits of proximity that cities provide mean that city regions, such as London, are important drivers of regional and national economic performance.

The report suggests, however, that cities can perform better and states the Government's commitment to lifting the performance of our cities' economies .

In order to bring about improved regional and national productivity and growth, the report cites a number of areas that need to address including the need to:

- Improve skills and employment in cities and towns and enhance connectivity between and within cities
- Achieve stronger collaboration between cities, towns and regions, reflecting their economic interdependence'
- Manage assets more efficiently and effectively, including the physical fabric and environment of cities
- Achieve greater economic and social inclusion.

These policy challenges are to be examined by the Government ahead of CSR 2007. This report is but one part of a new focus on cities by the Government.

(Footnotes)

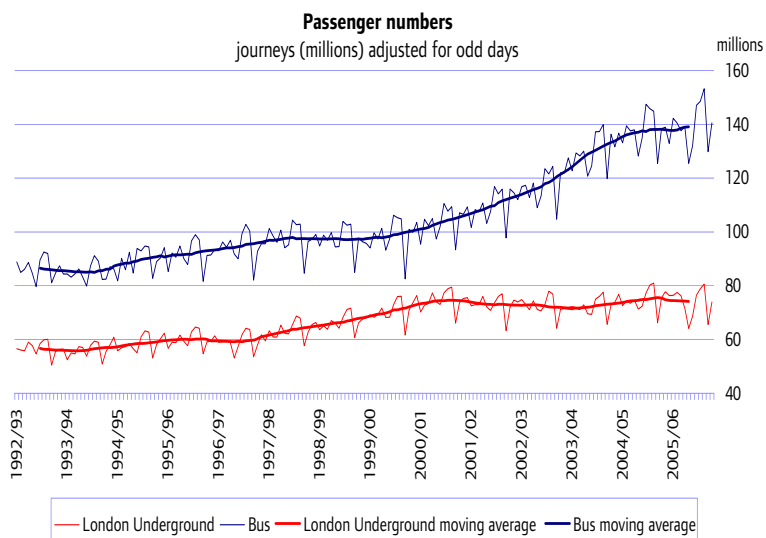
¹ GLA Economics, 2006, *Working Paper 15: Worklessness in London – Explaining the differences between worklessness in London and the UK*

Moving average of passenger numbers remain stable

- The most recent 28-day period is from 8 January to 4 February 2006. London's public transport had 214.5 million passenger journeys; 140.5 million by bus and 74 million by Underground.
- The moving average remained stable at 213.2 million passengers every period.
- The average for buses was 139.1 million passenger journeys. The average for the Underground was 74.2 million.

Latest release: March 2006

Next release: April 2006



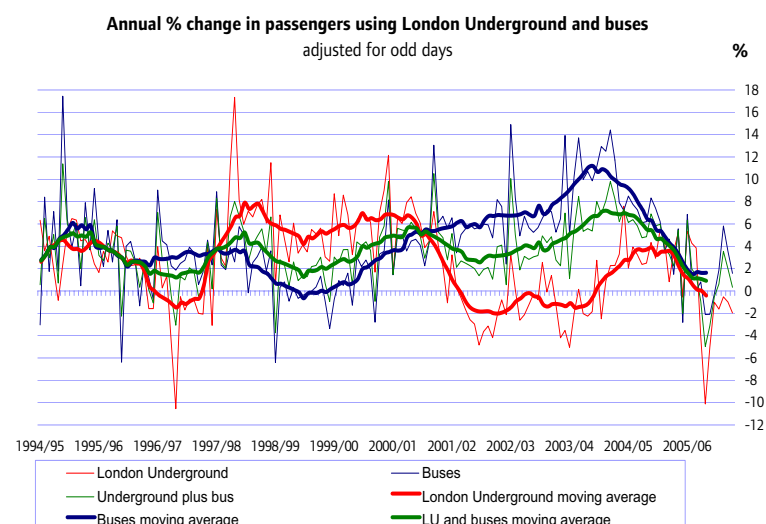
Source: Transport for London

Passenger journeys' annual growth rate continues to slow

- The moving average annual rate of growth in passenger journeys decreased slightly to 0.8% from 0.9% in the previous period.
- The moving average annual rate of growth in bus journey numbers remained stable at 1.5%.
- The moving average annual rate of growth in Underground passenger journey numbers was -0.5% down from a growth of -0.1% in the previous period.

Latest release: March 2006

Next release: April 2006



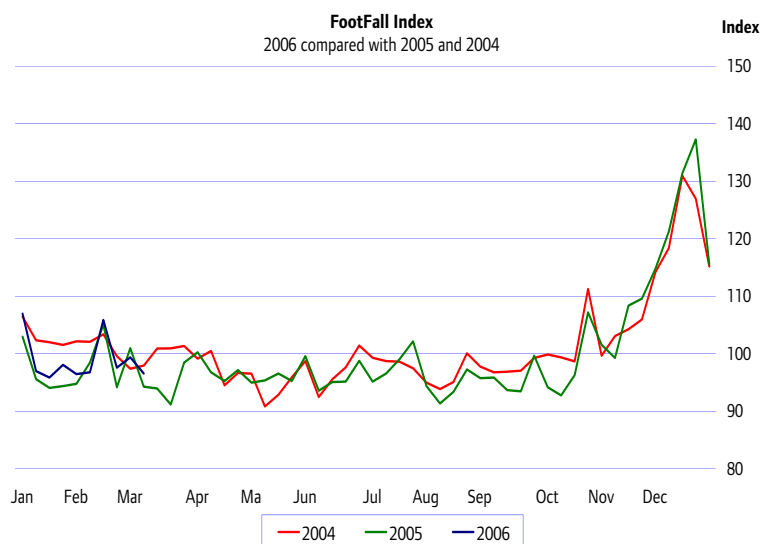
Source: Transport for London

Early 2006 FootFall remains above 2005 levels

- The FootFall Index of shoppers in London was 96.4 in the first week of March compared to 99.2 in the last week of February.
- For most weeks since the beginning of 2006, the number of shoppers has been above the level during the same period in 2005.
- The FootFall Index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: mid-March

Next release: every week



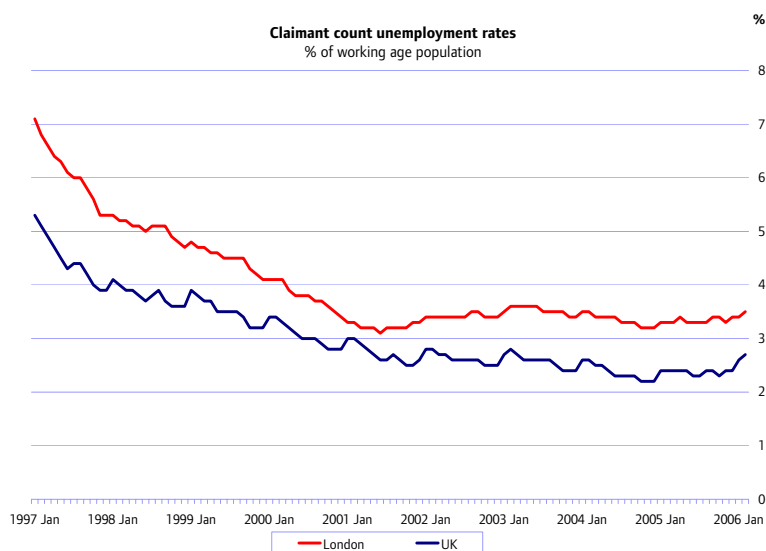
Source: FootFall Limited

Claimant count unemployment

- The rate of claimant count unemployment, people unemployed and claiming Jobseeker's Allowance, in London was 3.5% in February 2006.
- There were 171,185 unemployment claimants in London in February 2006 compared with 162,713 in February 2005.
- The claimant count unemployment rate in the UK remains below that of London's.

Latest release: March 2006

Next release: April 2006

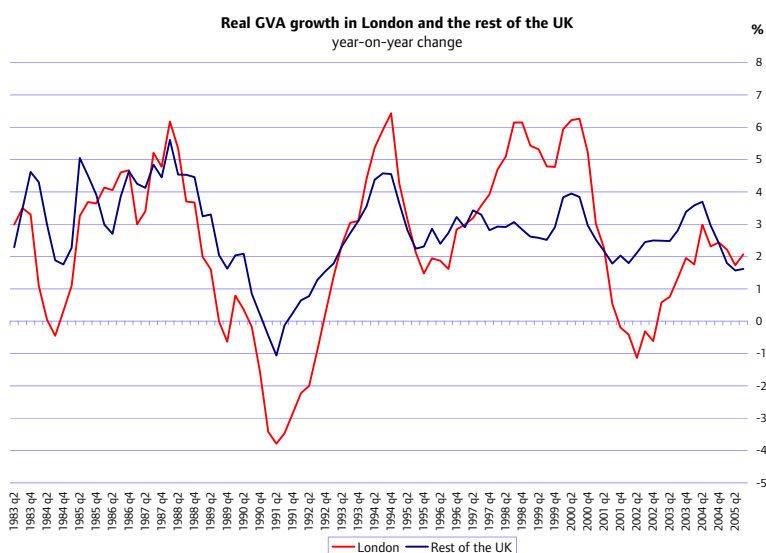


London's economy growing faster than the rest of the UK's

- London's annual growth in output was 2.1% in Q3 2005, up from 1.7% in the previous quarter.
- The annual growth in output for the rest of the UK was 1.6% in Q3 2005, unchanged from Q2 2005.
- London's output growth was higher than the growth experienced in the rest of the UK in Q3 2005.

Latest release: February 2006

Next release: May 2006

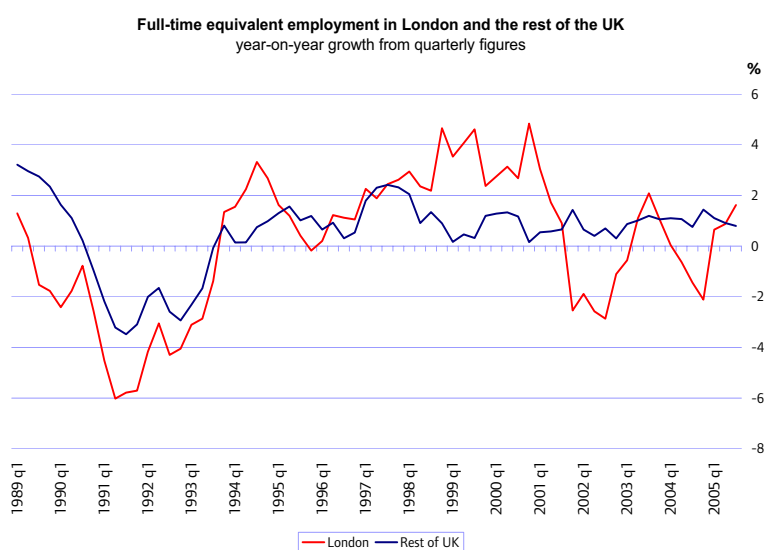


London employment continues to grow

- London's year-on-year employment growth increased further to 1.6% in Q3 2005 compared to 0.9% in Q2 2005.
- Annual employment growth in the rest of the UK decreased slightly to 0.8% in Q3 2005 from 0.9% in Q2 2005.
- London's annual employment growth was twice as high as that for the rest of UK in Q3 2005.

Latest release: February 2006

Next release: May 2006

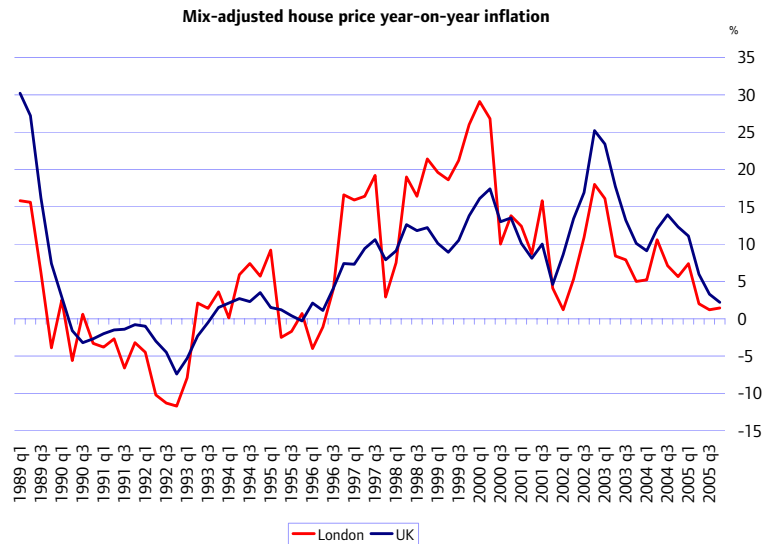


Small increase in London's house price growth in Q4

- The ODPM house price index is an official measure of house prices. It is available up to Q4 2005.
- Annual house price growth in London increased slightly to 1.4% in Q4 2005 from 1.2% in Q3 2005.
- Annual house price growth for the UK slowed to 2.2% in Q4 2005 from 3.3% in Q3 2005.

Latest release: March 2006

Next release: June 2006



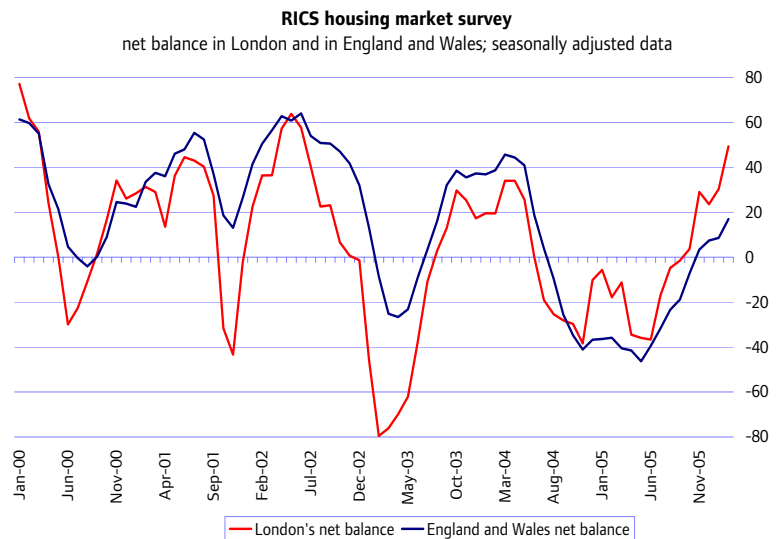
Source: ODPM

Surveyors reporting higher house prices in London in February

- The RICS survey showed a positive net balance of 49 for London house prices in February 2006.
- This was much stronger than the net balance of 30 in January. Since October 2005 the house price net balance has been positive.
- Surveyors are also reporting a continued recovery in house prices in England and Wales. The net balance was 17 in February, up from 9 in January.

Latest release: March 2006

Next release: April 2006



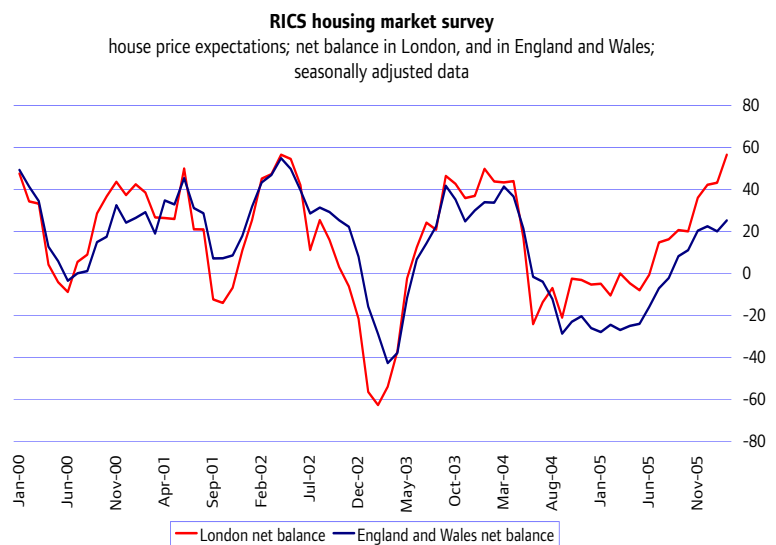
Source: Royal Institute of Chartered Surveyors

Surveyors expect house price growth

- The RICS survey shows a clear majority of surveyors expect house prices to increase over the next 3 months in London.
- The net expectations balance in London was 56 in March 2005, rising from a balance of 43 in February.
- For England and Wales, the net expectations balance was also positive. It was 25 in November 2005 up from 20 in October.

Latest release: March 2006

Next release: April 2006



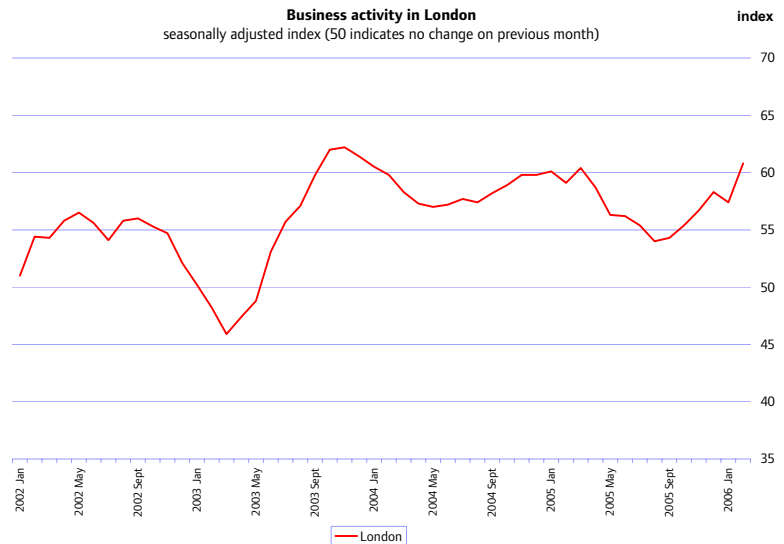
Source: Royal Institute of Chartered Surveyors

Business activity in London expands more rapidly

- London firms continued to expand their output of goods and services in February 2006.
- The Purchasing Managers' Index (PMI) of business activity recorded 60.8 in February 2006, its highest level for over two years.
- A rate above 50 on the index indicates an increase in business activity from the previous month.

Latest release: March 2006

Next release: April 2006



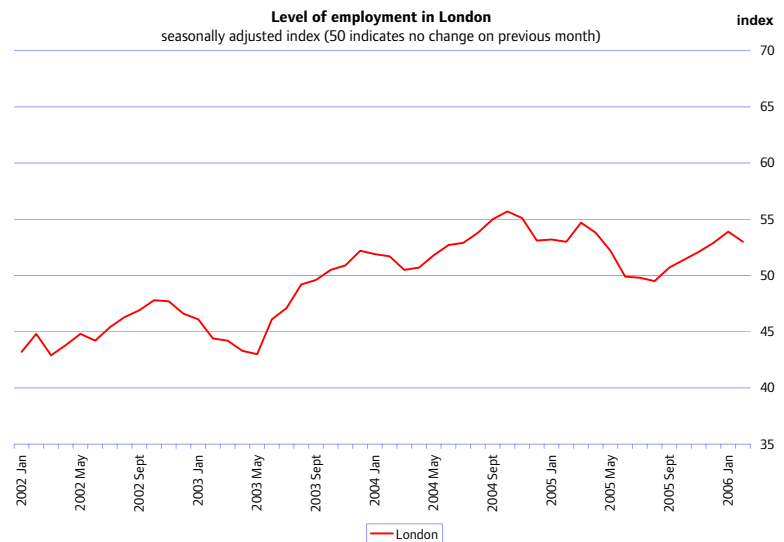
Source: PMI/The Royal Bank of Scotland

Steady increase in London employment

- London firms continue to increase their level of employment. The PMI for the level of employment was 53 in February 2006, slightly below the 53.9 recorded in January 2006.
- The PMI shows that the employment level in London firms has increased continuously since September 2005.
- A rate above 50 on the index indicates an increase in the level of employment from the previous month.

Latest release: March 2006

Next release: April 2006



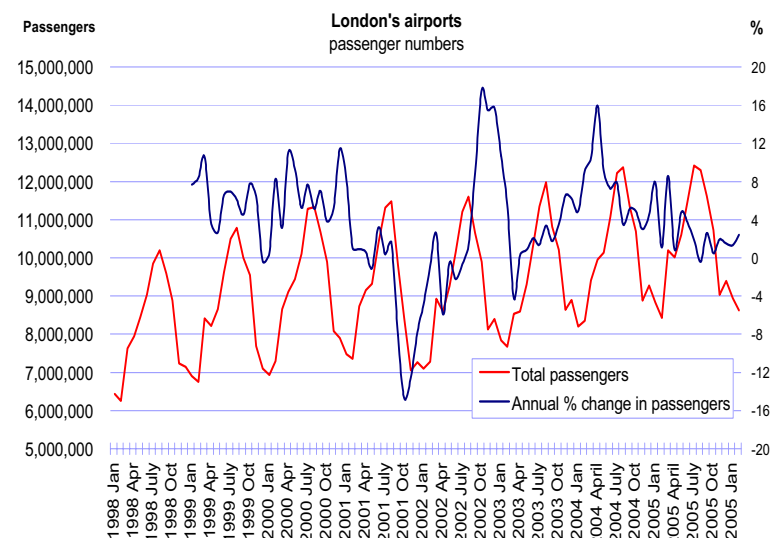
Source: PMI/The Royal Bank of Scotland

Annual growth in airport passenger numbers

- 8.58 million passengers travelled through London's airports in February 2006.
- The number of passengers using London's airports increased by 2.2% from February 2005 to February 2006.
- International travel through London's airports has continued to grow year-on-year since September 2005.

Latest release: March 2006

Next release: April 2006



Source: Civil Aviation Authority

Ready for Retail

GLA Economics' work in the retail sector

Matthew Waite
Senior Economist,
GLA Economics

As part of our research into London's retail sector, we've published four new working papers that discuss some of the key issues confronting this key sector.

Retail and the Labour Market

This report shows that in London in 2003, there were more than 400,000 people working in retail, making it one of the biggest sectors of London's economy.

The paper highlights that the retail sector provides a route into work for people with few recognised skills, or who for other reasons find it difficult to compete in the labour market. As such the retail sector acts as a gateway to the wider labour market for many people by providing skills and training to workers that are in demand in the rest of the economy. In addition, the retail sector provides flexible employment opportunities for those who cannot, or who do not want to work, full-time. Women in particular combine working part time with taking care of children. However, the paper shows that part-time work in retail (as in other sectors) is less viable in London than in the rest of the country.

'Retail spend in London's West End is more than the combined retail spend in Manchester and Glasgow.'

GLA Economics
Retail and the West End

Small Retailers

This working paper looks at the main issues facing small retailers in London and how these might differ to those faced by large retailers, and retailers in the rest of the UK.

The paper highlights that the increased market share of large retailers,

'93 per cent of London's population lives within one mile of a store of one of the top five grocery retailers.'

GLA Economics
Grocery Retailing

especially grocery retailers, over at least the past 20 years has resulted in greater buyer power for large retailers. This has resulted in large retailers being able to sell goods at lower prices than small retailers in many instances.

In addition, the recent move by retailers, predominately large grocery retailers, into small format stores in high street locations together with extended opening hours has seen small retailers lose much of their previous comparative advantage of convenience (in terms of location and opening hours).

Whilst these factors, together with issues such as succession, have resulted in a number of small retailers closing down, the paper highlights some ways in which small retailers can compete more effectively with large retailers; these include increased specialisation and competing on quality of service for instance.

Retail and Leisure

The Retail and Leisure report shows that, over time, shopping has become more of a leisure activity. As disposable incomes have risen, people's demand for leisure has increased. Indeed data shows that over recent decades, spending on leisure has grown in London and the UK at a faster rate than total spending (and retail spending).

The paper highlights three different types of leisure associated with retail;

'The value of retail spending on shopping by overseas visitors to London is estimated to be £1,000-1,700 million.'

GLA Economics
International Comparisons of Retail

these are ambient, magnet and heritage-destination. Ambient leisure refers to the factors that make a shop or shopping centre pleasant to be in, such as the provision of toilets, seating and food courts. Magnet leisure refers to standalone leisure

attractions, such as cinemas or bowling alleys. Heritage-destination leisure refers to instances where retail is located close to a heritage tourist destination and, as a result, has the spin-off advantage that customers visiting the heritage site spend money on the nearby retail outlets.

The trend towards more leisure has resulted in more ambient leisure facilities being incorporated into shops and shopping areas. This is likely to be an important issue for some of London's older shopping centres, which are, relative to more recent developments, lacking in ambient leisure facilities. Indeed, a report by London First found that one of the main criticisms shoppers have about the West End relates to the environment, for example noise, congestion and lack of toilets – highlighting the importance of retail surroundings and environment to consumers.

International Comparisons of Retailing

This working paper looks at retail in London in the international context. This paper shows that, in terms of rents, Bond Street and Oxford Street are the sixth and seventh most expensive shopping streets in the world; that London has more international visitors than any other world city; that 115 million passengers travel through London's airports annually; and, that overseas visitors spent an estimated £5,905 million in London in 2003.

The paper finds that London's retail offer is characterized by its range of shops, department stores, and the quality of goods offered. However, London is perceived to be an expensive city with cost and value for money the biggest deterrents to potential overseas visitors coming to London.

'Women make up around 57% of retail employees in London.'

GLA Economics
Retail and the Labour Market

Overseas visitors represent around a quarter of all shoppers in central London, slightly more than the proportion of shoppers coming from the rest of the UK outside London. Most overseas visitors and overseas shoppers in London come from the US and the EU15 countries. The value of spending on retail by overseas visitors to London is estimated to be £1,000 – 1,700 million.

'Small retailers account for 87 per cent of all retailers in London.'

**GLA Economics
Small Retailers**

Although only one per cent of overseas visitors come to London specifically *for* shopping, overseas visitors who come to London for other reasons often shop while they are here. In this sense international retail spending is a spill-over benefit from tourism.

In total ten working papers will be published as part of GLA Economics' study into retail in London. Other topics covered include the West End, retail and regeneration, grocery retailing, and servicing and delivery amongst others.

For copies of all the retail working papers currently printed, view: www.london.gov.uk/mayor/economic_unit.

If you'd like to subscribe to receive hard copies of future retail working papers, please contact GLA Economics:
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Data sources

Tube and bus ridership	Transport for London on 020 7941 4500
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
Employment	www.rbs.co.uk/pmireports
London FootFall	www.footfall.com
Office space demand	www.cbhillierparker.com
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.

FootFall Index

Measures the average number of people passing through London shopping centres on a weekly basis. This index is positively correlated with UK retail spending so it can provide an indication of consumer spending in London.

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 – twelve 28-day periods and one 29-day period. Period 1 starts at the beginning of the financial year rather than the calendar year.

Acronyms

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

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About GLA Economics

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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