LONDONASSEMBLY

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Marina Ahmad AM
Chair of the Economy Committee

Sadiq Khan
Mayor of London
(Sent by email)

11 March 2024

Dear Sadiq,

I am writing to you as Chair of the London Assembly Economy Committee following the Committee's investigation into the impact of Brexit on London's economy.[1] The Committee held a meeting in City Hall on 11 January 2024, which was attended by the following guests:

- **Ben Brindle**, Researcher, Migration Observatory, University of Oxford
- **Laura Citron**, Chief Executive Officer, London and Partners (L&P)
- **Alex Conway**, Assistant Director for Economic Development and Programmes, Greater London Authority (GLA)
- **Professor Sarah Hall**, 1931 Professor of Geography, and Fellow of St John's College, University of Cambridge
- **Professor Dennis Novy**, Professor of Economics, University of Warwick

Our investigation set out to understand the impact that leaving the European Union (EU) has had on London's economy to date. In particular, we sought to gain a better understanding of how London's businesses have been affected by Brexit, what impact ending 'free movement' has had on London's economy, and the role of the new UK Shared Prosperity Fund (UKSPF). We also considered whether sufficient time has elapsed to make an informed judgement on any of the above.

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[1] City Hall Conservatives have dissented from the letter due to the exclusion of testimony from an additional panel member who would have been able to further articulate the benefits of Brexit.

The evidence suggests that the picture so far is nuanced. Brexit has undoubtedly created challenges for London's economy, but it also presents opportunities. We heard that London's exporting businesses have been struggling to navigate an increasingly complex web of 'red tape', and that the removal of 'passporting' harms the competitiveness of the financial sector. However, our evidence indicates London is likely to remain a uniquely attractive place to do business, provided the right regulatory frameworks are in place. Similarly, whilst the Shared Prosperity Fund (UKSPF) requires substantial modifications and does not yet live up its promise as the successor to the European Structural Investment Fund (ESIF), it already makes a vital contribution to supporting London's economy.

Ensuring London's businesses remain competitive

The Committee heard that not all parts of London's economy have been affected by Brexit in the same way. Professor Sarah Hall, 1931 Professor of Geography, and Fellow of St John's College, University of Cambridge, told the Committee that the EU-UK Trade Cooperation Agreement (TCA) makes far more provisions for trade in goods than it does for trade in services.[2] She added that London-based financial institutions were previously able to access the EU single market via 'passporting' rights, which have now been replaced by an 'equivalence regime'.[3] Within this system, financial institutions are only able to access foreign markets if the regulatory frameworks are deemed sufficiently similar. We heard that currently only one area of the financial services trade is covered by an equivalence decision. This is due to expire in 2025.[4]

However, a mass relocation of jobs within the financial services sector has not materialised, with the latest estimates suggesting that between 7,000 to 8,000 jobs have left London, far lower than what had been predicted under a 'worst case' scenario.[5] Although there is evidence to suggest that there has been 'fragmentation', as different types of financial services activities have moved to different European cities, Professor Dennis Novy from the University of Warwick told the Committee that London has held onto mergers and acquisitions and other 'high value-added' activities.[6]

This speaks to the appeal of London as an attractive hub for financial services institutions. Within the financial services sector, London offers a highly skilled pool of workers, leading to 'agglomeration benefits' which remain unrivalled by any other European city, according to Professor Dennis Novy.[7]

Despite London's strengths in financial services, the Committee heard that there is currently no coherent strategy for how this vital part of our capital's economy can remain competitive at a global level. In its new position outside the EU, the UK is now no longer able to influence global regulatory frameworks to the same extent as it was previously. However, the Committee heard that this could open up opportunities for London to craft a more agile regulatory system, tailored to the needs of London, rather than the EU as a whole.[8] Professor Sarah Hall drew the Committee's attention to the

[2] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 6)
[3] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 6)
[4] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 7)
[5] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 7)
[6] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 8)
[7] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 8)
[8] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 7)

importance of not losing sight of growth markets outside the EU, as exemplified by the recent mutual recognition agreement between the UK and Switzerland.[9]

Given the evidence heard by the Committee, we believe there is an opportunity to leverage London's unique position within the financial services field.

Recommendation 1: *The Mayor should lobby the Minister for London and the Secretary of State for Business and Trade to devise a financial services strategy to ensure the sector in London remains competitive at a global level. We recommend that such a strategy focus on creating a regulatory framework suited to London's unique strengths and make it easier for London-based firms to access market opportunities both within and outside the EU.*

Notwithstanding the importance of the financial services sector to London's economy, the Committee also heard that Brexit has had a significant negative impact on non-financial services and on those businesses exporting goods to the EU. Professor Dennis Novy highlighted the rise of 'regulatory divergence', a process whereby new regulations issued by the EU are not automatically translated into UK law. This can gradually lead to a widening chasm between regulatory regimes, making it harder for UK-based businesses to sell goods or services to EU markets.[10]

There is evidence to suggest that this is already harming London's businesses. Professor Dennis Novy told us that the current situation is characterised by uncertainty, which in turn harms investment.[11] Laura Citron from L&P shared with us that Foreign Direct Investment (FDI) flows into more heavily-regulated sectors have been affected more negatively than those into less heavily regulated sectors.[12] Recent research suggests that small businesses are affected more negatively by this than larger firms, particularly if they form part of larger cross-border supply chains spanning multiple countries.[13]

The Committee is aware that most regulatory matters fall within the remit of central Government. However, given the significant role that London plays within the UK economy, we believe this is a policy area the Mayor should take interest in and work proactively with the Government on. The review of the TCA in 2026 presents an opportunity to do this.

Recommendation 2: *Ahead of the 2026 review of the EU-UK Trade Cooperation Agreement, the Mayor should work with London & Partners to build the evidence base for the effects of regulatory divergence on London-based businesses. He should use this evidence to lobby the Government to ensure that London-based businesses are not negatively impacted by regulatory divergence from the EU.*

Supporting London's economy through the UK Shared Prosperity Fund

In April 2022, the UK Government launched the UK Shared Prosperity Fund (UKSPF) to replace the EU's European Structural and Investment Funds (ESIF). London's allocation of £144 million is

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[9] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (pp. 4-5)

[10] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 5)

[11] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 2)

[12] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 16)

[13] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (pp. 1-2)

directly managed by the GLA and is invested in a variety of programmes, which make an important contribution to London's economy. This includes investments into infrastructure, skills and employment programmes, as well as £62 million for targeted support for local businesses. Laura Citron from L&P told us that her organisation was awarded around £19 million of this money. Much of this is directed at supporting smaller firms, which have traditionally struggled to navigate the fragmented business support landscape.[14]

We heard that the GLA and L&P are both drawing on this funding to create a support 'ecosystem', where businesses can access the right support programme, depending on their needs.[15] This is in line with the Mayor's 2021 manifesto pledge to create a 'single front door' for small business support, having stated that small businesses form the 'backbone of London's economy'.[16]

The Committee welcomes this ambition. However, we heard that the current total funding available under this programme is lower than the total amount that had been available under the EU's equivalent programmes. Alex Conway from the GLA told us that, under the UKSPF, London currently receives £144 million over three years, which amounts to approximately half of the funding available under the ESIF.[17] In addition to this, we learned that £38 million of the above-mentioned £144 million, intended to be allocated to skills and employment programmes, can only be spent over the course of the next (2024/25) financial year by the GLA. We heard that in other UK nations, this funding can be spread over three years.[18]

The Committee also learned that there is currently no plan in place for when the UKSPF comes to an end in March 2025. As a result of this, the current funding situation is characterised by a high degree of uncertainty, particularly with regards to timescales. Alex Conway warned the Committee about "hitting a cliff edge" in March of next year, with funding stopping abruptly unless arrangements are made for an extension to the programme.[19] There is therefore a risk of vital support programmes being put on hold or discontinued altogether.

Recommendation 3: *The Mayor should ask the Government to put plans in place for an extension to the UK Shared Prosperity Fund to avoid jeopardising the continued delivery of programmes after the current round of funding expires in March 2025. The Mayor should further lobby the Government to revise the funding available under the UK Shared Prosperity Fund to bring funding levels closer to those available under the European Structural and Investment Funds (ESIF).*

Improving pay and conditions to address vacancies

The Committee heard that migration patterns have changed significantly since the end of 'free movement' between the UK and the EU. In broad terms, migration has become more restrictive for EU citizens, whilst at the same time becoming more liberal for those outside of the EU. Ben Brindle from Oxford University's Migration Observatory told us that London's hospitality, wholesale, retail

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[14] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 22)

[15] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (pp. 22-23)

[16] Mayor of London, Press Release, "Mayor delivers boost to capital's small businesses as he launches new service to support 'backbone of London's economy'"

[17] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 19)

[18] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 20)

[19] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 24)

and manufacturing sectors were strongly affected by this, due to the high number of EU citizens they traditionally employed.[20]

Whilst vacancy rates across all of these sectors are high, there is evidence to suggest that this has not been solely caused by changes to the UK's immigration rules. Ben Brindle said that whilst the number of EU citizens working in these sectors has gone down, the number of non-EU citizens working in these sectors has increased. In the case of hospitality, the fall in workers from the EU has been offset by an influx of migrants from outside of the EU. In the wholesale, retail and manufacturing sectors, this fall has been more than offset, meaning more workers from outside the EU have joined these sectors than workers from the EU have left.[21]

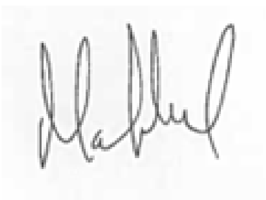
The Committee learned that, despite this, vacancies in these sectors remain high, suggesting that migration patterns after Brexit cannot alone explain high vacancy rates. Ben Brindle suggested improving pay and conditions in these sectors to make them more appealing to those already in the UK.[22]

The Committee is aware that the Mayor launched the Good Work Standard (GWS) in 2019, allowing businesses to become accredited and recognised as 'leading employers'.[23] However, the GWS is currently not targeted specifically at those industries experiencing high vacancy rates. Based on the evidence heard, we believe there is an opportunity for the Mayor to leverage the GWS to attract employees to London's hospitality, wholesale, retail and manufacturing sectors and reduce vacancy rates.

Recommendation 4: *The Mayor should actively encourage businesses in sectors experiencing high vacancy rates to adopt the Good Work Standard as a means to attract new employees and reduce vacancies.*

The Committee would welcome a response to this letter by Friday 10 May 2024. Please send you response to by email to the Committee's clerk, Jack Booth (jack.booth@london.gov.uk).

Yours sincerely,



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[20] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 9)

[21] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 9)

[22] London Assembly Committee – Thursday 11 January 2023: The Impact of Brexit on London's Economy (p. 10)

[23] Mayor of London, The Good Work Standard (GWS)