London's Economy Today



Issue 18 | February 2004

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Interest rates go up, but economic improvement continues

by Duncan Melville

At its meeting on 5 February, the Bank of England's Monetary Policy Committee (MPC) decided to raise interest rates by a quarter of a percentage point to 4%. In explaining its decision, the MPC noted that the 'world economic recovery has become more broadly based', that UK growth had strengthened and that a further pick up was expected for early 2004.

UK growth is rising

It certainly appears that the economic environment is becoming more positive. UK GDP is provisionally estimated to have increased by 0.9% in the fourth quarter of 2003 taking growth for the whole year to 2.1% – above what many economic commentators had been expecting for much of that year. The Bank of England report that recent business survey data on new orders suggest a further strengthening in early 2004. In addition, the National Institute of Economic and Social Research (NIESR) estimate that UK GDP grew by 0.8% in the three months to January 2004.

Growth in household consumption has continued to be strong. Retail sales growth in the fourth quarter of 2003 rose to 1.9% from 1.2% in the previous quarter. This strength appears to have continued into 2004 as the British Retail Consortium reported that retail sales in January were 3.8% higher than in the same month of 2003. The prospects for investment are also upbeat. The upturn in economic activity, improved profitability, increased capacity utilisation and a sharp increase in investment intentions point to a revival in business investment.

The world economy is strengthening

As the MPC has noted this economic improvement is not confined to the UK. Chart 1 shows that growth is generally expected to increase in the world's leading economies. The second half of last year saw very strong growth in the US with output growing by 3% in that six month period. US growth has been supported by tax cuts and low interest rates. The impact from these is expected to ease, but even so strong growth is expected to continue. The dollar has declined by around 13% on average against all currencies in the last two years boosting the prospects

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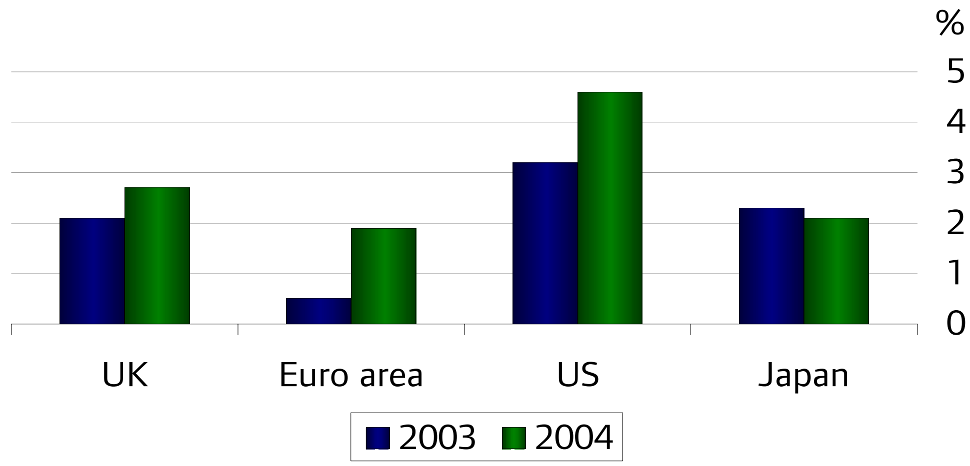
Chart 1. International economic growth

Sources: HM Treasury, The Economist



for US exports. Furthermore, the improving labour market is expected to support continued growth in personal consumption as individuals become more confident about their continued employment prospects. In January, US employment rose by 112,000 the largest monthly increase for more than three years. In addition, the unemployment rate has been falling for several months and in January reached 5.6% the lowest rate since January 2002.

While growth in the Euro area lags behind that experienced in the US and the UK it is at least on an upward path. The Euro area recorded positive growth in the third quarter of last year following three quarters of stagnation. Both the Purchasing Manager's Index (PMI) indices for manufacturing and services rose to their highest levels in around three years in the fourth quarter of 2003 suggesting that growth remained firm. Indeed, while growth figures for the fourth quarter of 2003 are not yet in for all the Euro area countries, those that are in – for Germany, France and the Netherlands – recorded positive growth.

In Japan, the prospects for growth look better than they have for some time. China's booming economy has stimulated demand for Japanese products and Japan's firms have managed to cut costs, and increase profits. Japanese corporate debts have fallen and are now back at levels last seen in the mid-1980s. Japanese prospects have been assisted by expansionary monetary policy. The Governor of the Bank of Japan, Toshihiko Fukui, stated that monetary policy will continue to be expansionary until inflation has been positive for some time. This dispels some fears about continued deflation which has been holding back economic recovery for some years.

Growth in international economies benefits London, where many firms are more exposed to international markets than in other parts of the country

London continues to prosper

The growth in the number of passengers on London's tube and buses combined continues to be strong. In period 10, roughly December 2003, annual growth was 5.9%. This was the strongest annual growth since 1994, and suggests continuing growth in London's economic activity. This view is supported by the latest PMI regional survey for January 2004, which showed that the growth in output in London stayed above the UK average and was the second strongest of all the UK regions. London companies have now reported higher levels of economic activity for the eighth month running. Supporting this increase in output has been a marked rise in new orders, which suggests this increase in output is likely to continue into the future. Certainly this is the view taken by NIESR whose latest forecast of the London economy for the London Chamber of Commerce and Industry foresees growth in London's output rising from 2.0% in 2003 to 2.4% in 2004 and to 2.8% in 2005.

Conclusion

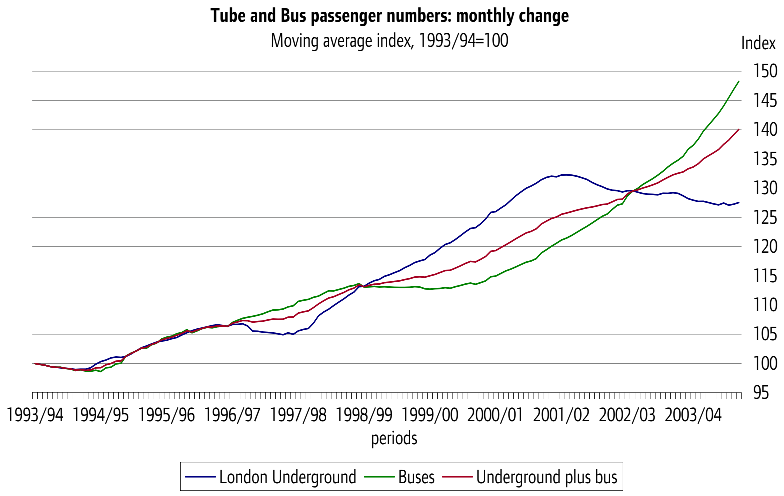
Healthy growth continues to be the most likely outcome for the London, UK and world economies. The latest indicators suggest growth is rising across all three and that the prospects are for growth to continue. The increase in UK interest rates has to be seen against this background. Interest rates at 4% are still low by historic standards and this would continue to be true even if they rise to 4 ½% by the end of this year as indicated by financial market expectations. It is better that interest rates rise now to maintain economic stability and low inflation. If no action is taken and higher inflation starts to take hold, interest rates are likely to rise to an even higher level in order to reduce inflation. This would generate higher economic costs in terms of lower output and employment.

Economic indicators

Tube numbers stable, bus numbers growing strongly

- The number of tube passengers rose for the second consecutive period between 7 December 2003 and 3 January 2004 (period 10). Passenger numbers rose 0.2%.
- Bus use continued to show strong growth from period 9, rising by 0.9%.
- The total number of passengers (tube and bus) rose by 0.7%, suggesting continued growth in London's economy.

Latest release: 02/02/04
Next release: March 2004

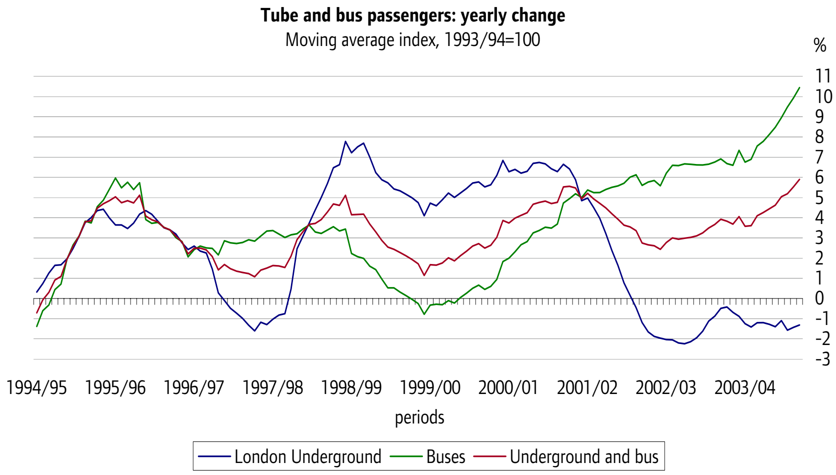


Source: Transport for London

Ten-year high in annual passenger number growth

- Annual growth in the number of people on the bus and tube combined was 5.9% in period 10. This is the strongest annual growth since 1994.
- Although the number of passengers using the tube in period 10 was still down compared to last year, tube use appears to be stabilising.
- Annual growth in bus use continued to accelerate over this period.

Latest release: 02/02/04
Next release: March 2004

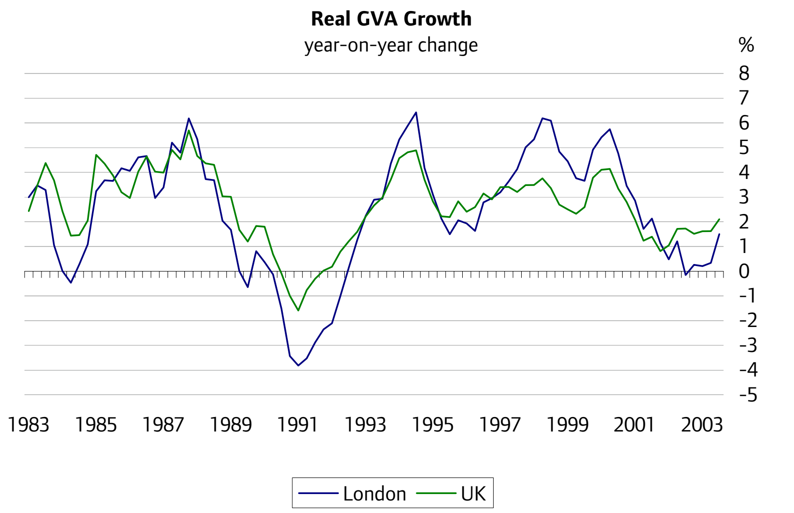


Source: Transport for London

London economy recovers, but still lags behind UK

- London's economy grew more strongly than the UK economy in Q4. London GVA rose by 1.0% from Q3 compared to UK GVA growth of 0.8%. Despite this strong rebound, London's annual GVA growth (1.5%) still lags behind the UK (2.1%).
- Provisional GDP figures are consistent with a strong recovery in the UK economy. UK GDP grew 0.9 % in Q4 compared to 0.8% in Q3. UK annual growth was 2.5% in Q4, the strongest since 2001 Q2.

Latest release: 23/01/04
Next release: 23/04/04

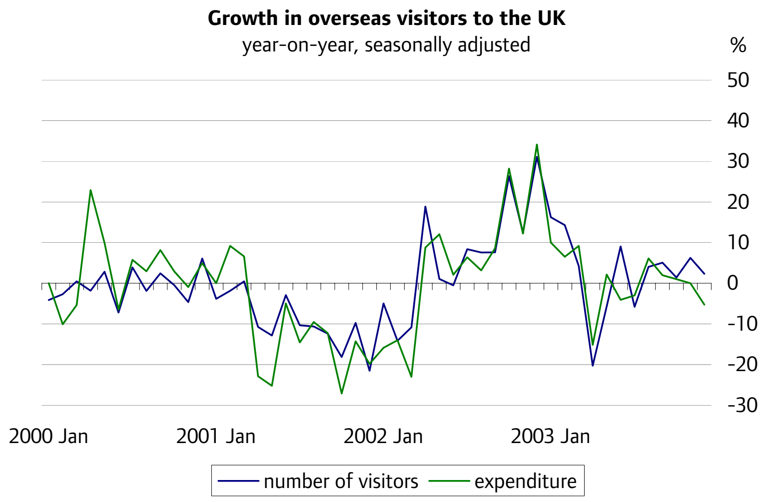


Note: Most recent EBS estimates for London GVA include changes due to the adoption of chain linking and rebasing UK figures to 2000 prices.
Source: ONS and EBS

UK tourism remains strong

- UK tourism activity slowed marginally in December, but stayed above the 2003 average. The number of overseas visitors to the UK fell by 0.5% from November.
- Overseas visitor spending recovered strongly, increasing almost 7% in December. This was probably due to a rebound in visitors from outside the US and Western Europe, and a modest increase from North America.
- Nevertheless, overseas visitor expenditure was down compared to December 2002.

Latest release: 06/02/04
Next release: 07/03/04

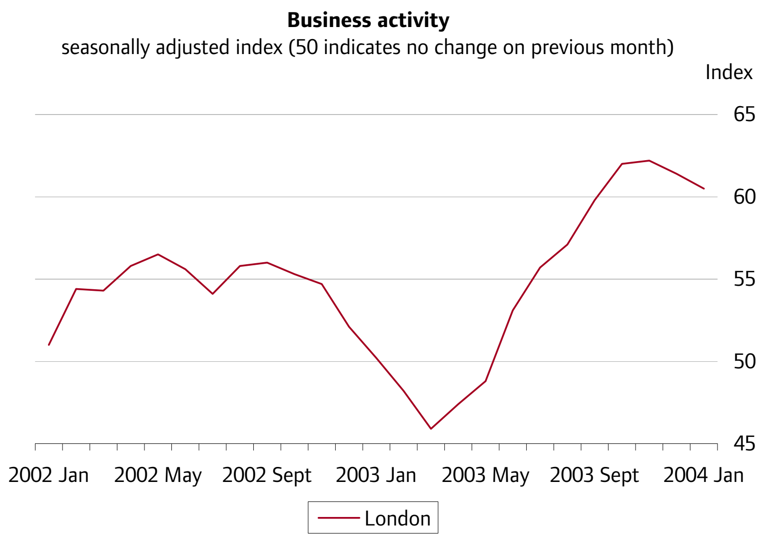


Source: ONS

Business activity in London expands rapidly

- The Purchasing Managers' Index (PMI) indicates that activity in London firms expanded strongly in January (50 indicates no change).
- The London index has fallen for two months in a row, but remains strong at 60.5 in January.
- Activity continues to expand at a faster rate in London than in the UK.

Latest release: 19/01/04
Next release: February 2004



Source: Royal Bank of Scotland /London PMI

Profit expectations improve

- London firms were more optimistic regarding the outlook for profitability in Q4, compared to the previous quarter.
- In Q4, service sector firms felt more optimistic about their future profitability than manufacturers did.
- However, business confidence among manufacturers is still the highest it has been since 1997 Q1.

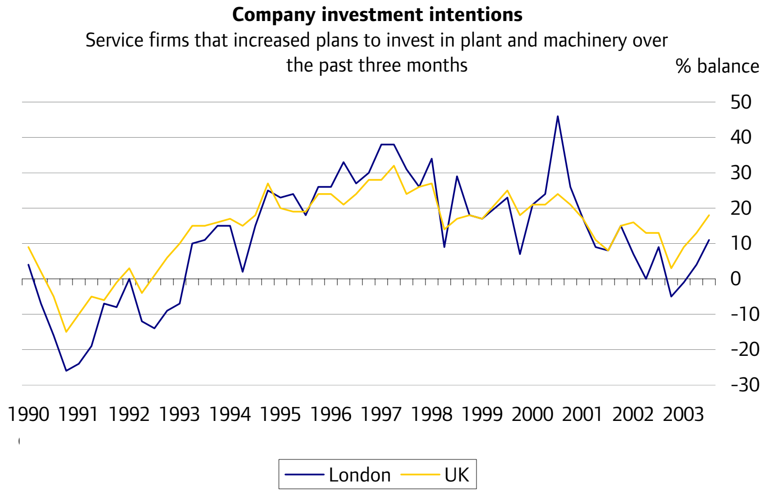
Latest release: 23/01/04
Next release: April 2004

Source: BCC and LCCI

Positive outlook for service sector investment

- London's service sector firms were planning to increase their future investment levels in Q4 2003. This is the second consecutive quarter that more service sector firms were planning to increase rather than decrease future investment.
- However, more UK service sector firms are planning to increase investment than London firms in Q4.

Latest release: 23/01/04
Next release: April 2004

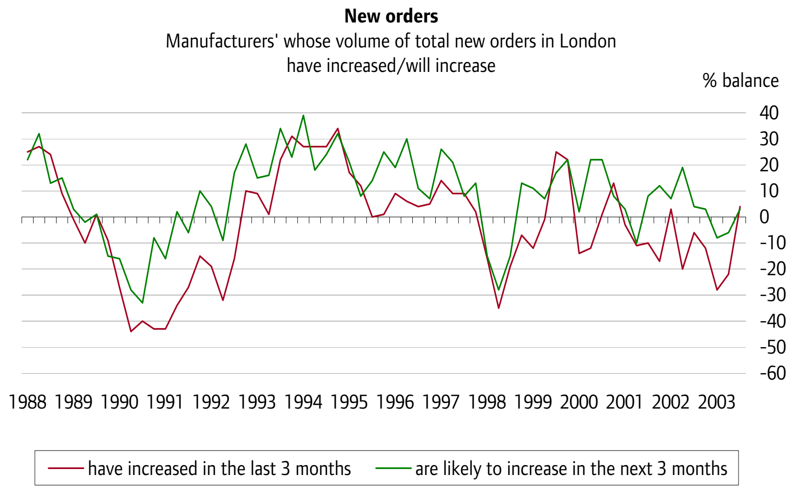


Source: BCC and LCCI

London manufacturers new orders

- For the first time in over a year, more London manufacturers reported increases rather than decreases in new orders during October–December.
- London manufacturers were also more optimistic about their future orders for the next three months.
- However, figures for UK manufacturers were higher than figures for London.

Latest release: February 2004
Next release: May 2004

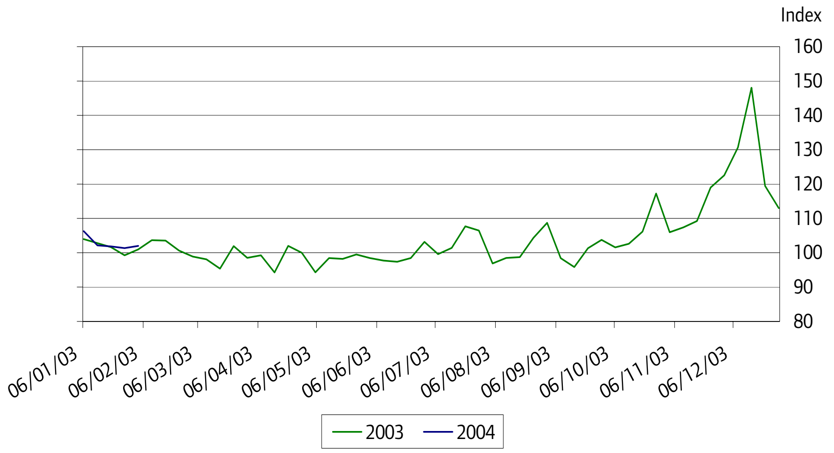


Source: CBI and Regional Trends Survey

Number of shoppers in London slightly up in 2004

- The number of visitors to shopping centres in London during the first week in January was marginally up compared to last year.
- This is consistent with the rebound in consumer confidence during January.

Latest release: 2/02/2004
Next release: next week

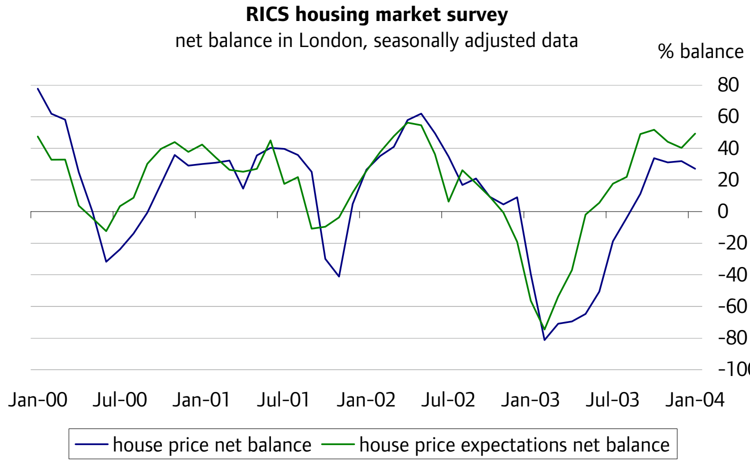


Source: FootFall Limited

London house price inflation slowed in January

- House price inflation slowed slightly in the capital in January, but remains positive. Fewer surveyors reported price increases than declines in the three months to January (27%) than in the three months to December (34%).
- New sellers instructions increased in January for the first time since September 2003. New buyer enquires also showed steady growth.
- With this positive outlook, the net balance of surveyors expecting price rises rose to 49% in January from 40% in December.

Latest release: 17/02/04
Next release: 16/03/04

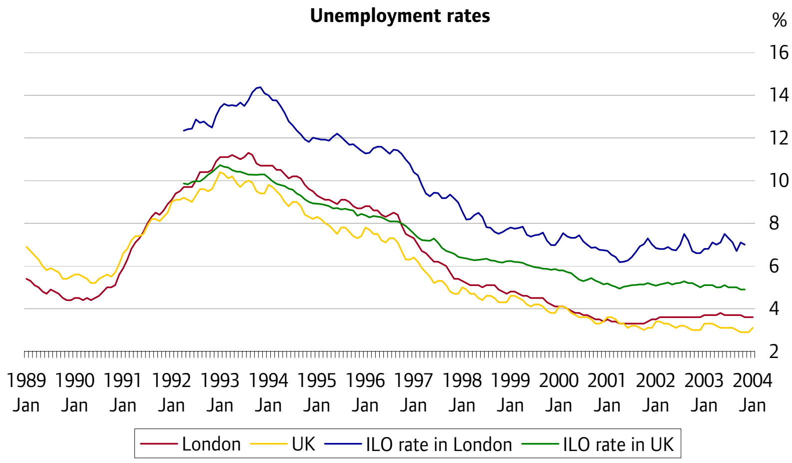


Source: RICS

Unemployment rates stabilise

- London's ILO unemployment rate fell to 7.0% in October–December, from 7.1% in the previous three months. The UK ILO unemployment rate also fell by 0.1% over the same period to 4.9%.
- UK and London claimant count rates remained stable in January. The London rate was unchanged from December at 3.6%, and also from January a year ago. London's rate is the third highest after the North East (4.5%) and Northern Ireland (4.2%). The UK claimant count rate was 2.9%.

Latest release: 11/02/04
Next release: 17/03/04

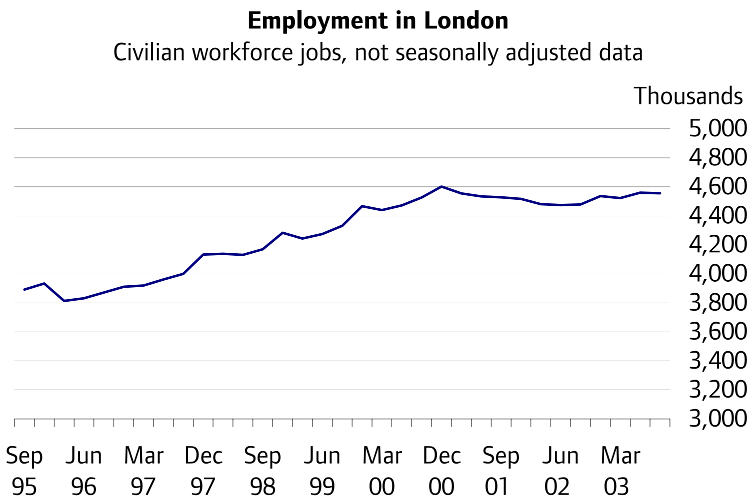


Source: ONS

Jobs in London

- Total employment in London rose by 77,000 to 4.555 million in the year to September 2003.
- This increase has been driven by a rapid growth in the number of self-employed jobs.

Latest release: 14/01/04
Next release: 22/04/04



Note: Civilian workforce jobs include employees, self-employed and government-supported trainees jobs.
Source: ONS

Congestion Charging and Retail – One year on

by Alon Carmel

Congestion charging was introduced on 17 February 2003. This feature summarises GLA Economics' analysis of the impact of the congestion charge scheme on retailing in London. It updates analysis in Issue 11 of *London's Economy Today* (July 2003) as new data has become available which supports our earlier assessment.

An early survey by the London Chamber of Commerce and Industry (LCCI) showed that a significant proportion of retailers in Central London had experienced disappointing sales, and that a significant proportion of them blamed the congestion charge. In addition, in a survey by the Commission for Integrated Transport small retailers (eg confectionary, tobacconists and newsagents) in particular said they were suffering from the congestion charge because they were dependent on distributors who had raised the prices of deliveries without passing on the cost-savings of shorter and more reliable delivery times.[1]

The picture now is somewhat clearer than it was when we last considered this issue in July 2003. There is still not enough data available to precisely quantify the impact of congestion charging on retail. However, the evidence that does exist supports GLA Economics' initial conclusion that the impact is likely to be small, with other factors being much more important in determining the profitability of the retail sector in London, and Central London.

This article starts by considering the channels through which the congestion charge might affect retailers in London. It then looks at other factors affecting retailing in London such as the wider economic environment, the Central Line closure and the effect of a fall in tourist numbers. This analysis is expanded in a forthcoming Current Issues Note.

The impact of Congestion Charging – the theory

There are two main ways in principle in which the congestion charge could reduce demand within the charging zone – a substitution (deterrence) effect and an income effect.[2] The substitution effect works by the charge deterring some former car-borne shoppers from driving into the charging zone. Instead they take their trade elsewhere, avoiding the charging zone. This redistributes retail spending from Central London out to other areas of London or areas outside of London, without necessarily reducing overall retail spending.

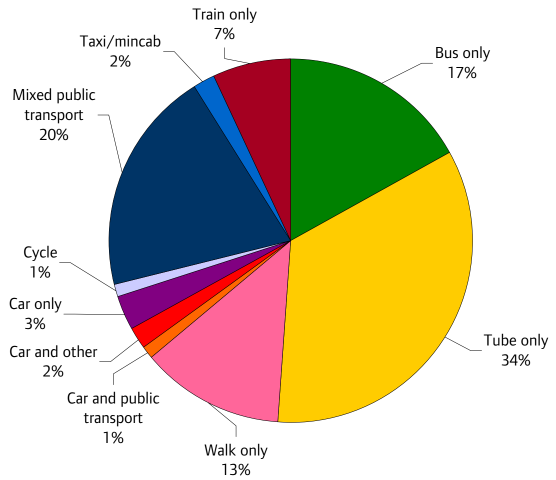
The income effect impacts on car users who continue to drive into the congestion charging zone. These drivers pay the charge and, as a consequence, their disposable income is reduced. As a result, the income effect could reduce overall retail spending.

While the income and substitution effect impact on car users, it should be noted that surveys show that only a small number of people drive into London to shop. Chart 1 shows that only 3 to 6% of all shoppers in Central London use their car to go shopping. As a result, the effect of the congestion charge scheme on retailers in London is likely to be relatively small.

Moreover, this note takes no account of the possible positive effects that may accrue to retailers in London from the congestion charge bringing about a more pleasant environment in which to shop.

Chart 1. Car-borne shoppers a small proportion

Source: TfL On-street Public Space Survey, 2002, Special Analysis



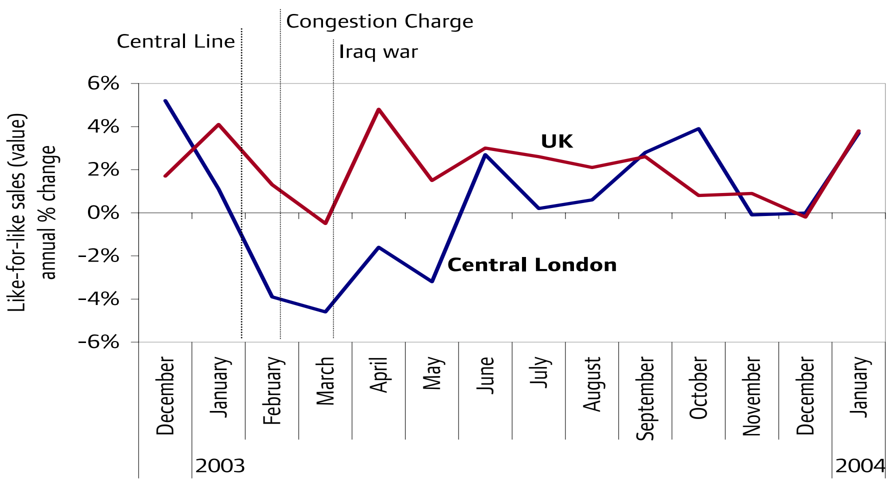
The impact of Congestion Charging – the evidence

New data on the trend in retail activity in London is provided by the recently launched London Retail Sales Monitor (Chart 2). According to these figures (based on actual sales figures for a representative sample of retailers in central London), growth in retail sales dipped significantly in the first and second quarters of 2003. This is consistent with London retailers' statements of disappointing sales highlighted in the LCCI's early survey.

Chart 2. A difficult spring for London retail

Source: KPMG/London Retail Consortium, Retail Sales Monitor

Note: The RSM index does not coincide with the Congestion Charging Zone – it includes Knightsbridge and Kensington as well as the West End.



This is also consistent with the overall decline in economic activity seen in London. Chart 3 shows that, as with retail sales, total economic growth in London has fallen below the UK average in the recent past.

Chart 3. The economic slowdown in London and the UK – impact on growth

Source: EBS

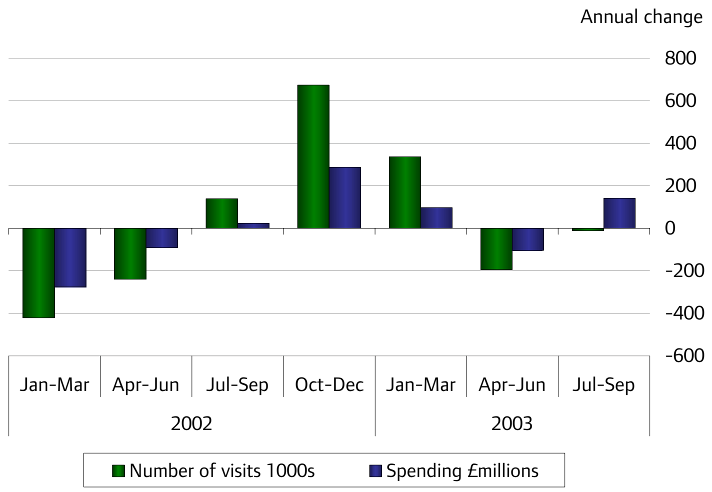
However, Chart 2 shows that retail sales recovered in June–October. December was disappointing both for London and the UK as a whole, but January showed continued recovery. This suggests that congestion charging has had a minimal permanent impact on Central London's retail economy because whilst sales fell below the UK trend at/or around the time of the introduction of the congestion charge, Central London retail sales have since picked up to move back in line with the UK trend. This would suggest that factors other than the CC are important in explaining the experience of Central London's retailers in early 2003.

As Chart 2 shows, the Central Line was closed in the early months of 2003. Another factor that will have impacted on retailers in Central London is the effect of the Iraq war and terrorism threat on tourism. Indeed, both these factors have been cited by the London Retail Consortium as a reason for the decline in retail activity in Central London. Retail areas such as Oxford Street, for example, rely heavily on overseas visitors but the number of visitors from overseas was 200,000 lower between April and June 2003 compared to the same period in 2002 (Chart 4).

ONS statistics show that overseas visitor spending in London was £100 million lower in the second quarter of 2003, than in the second quarter 2002 (Chart 4). Assuming that 26% of this is retail expenditure (Visit Britain estimates for overseas visitors' retail spending as a proportion of total spending) this means £26 million less was spent on the retail sector by overseas tourists in London in the second quarter of 2003. This is likely to be an underestimate of the total effect as these figures do not include any effect that worries about terrorist attacks and the effect of the Iraq war might have had in deterring domestic visitors.

Chart 4. London overseas visits and spending, annual change

Source: ONS



Conclusion

It is difficult if not impossible, at this stage, to precisely quantify the impact of the congestion charge on retail. However, the existing evidence suggests that any impact is small. Only 3 to 6% of all shoppers in Central London use their car for shopping. Moreover, while retail in Central London has turned down, this is against a background of declining economic activity in general, and in London in particular, a fall in tourism and the Central Line closure – all factors that have affected the retail trade in the congestion charging zone.

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[1] CfIT (2003) *The Impact of Congestion Charging on Specified Economic Sectors and Workers.*

[2] The charge might also affect supply by increasing the costs of production for example, but supply effects are not considered here.

New tourism and employment indicators

by Alon Carmel

- **GLA Economics has been working with London Underground to develop two new indicators for economic activity in London based on London Underground station counts.**
- **The 'Tourist' and 'Employment' stations indicators provide a barometer of tourism activity and general employment levels for Central London.**
- **Caution should be exercised in interpreting these indicators as they are likely to be affected by many different factors, some of which will have nothing to do with tourism or employment.**

Official statistics often come out with significant lags, making it necessary to find alternative data sources to inform policymaking. London Underground (LU) collects a vast amount of data on underground passenger use, which can be analysed by station and time of day. GLA Economics has been working with LU to use this data resource to supplement official statistics on tourism and employment. Using transport data to aid economic analysis is not unusual. The Tube ridership figures are frequently used by GLA Economics as an indicator of overall economic activity in London. This index is produced by Transport for London based on ticket sales, and is included in the economic indicators section of *London's Economy Today* each month. The new indicators will also be published periodically in *London's Economy Today*, and will – in combination with other statistics – be used to analyse the current state of the tourism market and London's economy more generally.

The data is collected by LU in 15 minute time-bands for each entrance and exit for each station on the underground network. GLA Economics and LU then aggregate this data to provide a less volatile and more meaningful series. GLA Economics receives the data with a two to three week lag. Official tourism statistics for London are available with a three to four month lag. The data is aggregated in order to minimise problems caused by missing data for individual stations and at individual times. The other major problem is seasonal fluctuations. This can be corrected for to some extent by looking at year-on-year changes in the same week. However, Easter week does not fall on the same date each year, and there will still be unique events (eg the Jubilee) for which it is difficult to control (for example, see Chart 3).

For the Tourism Stations indicator, data is aggregated for 20 stations that LU's own surveys have shown are the most intensely used by tourists. The stations are: Bond Street, Goodge Street, High Street Kensington, Knightsbridge, Marble arch, Oxford Circus, Sloane Square, Tottenham Court Road, Warren Street, Southwark, Tower Hill, Barbican, Westminster, Pimlico, St Pauls, North Greenwich, Blackfrairs, Lambeth North, Covent Garden and Aldgate. Only data from the inter-peak period (ie 10:00–16:00) is used to filter out as many non-tourists as possible. This data is then added together by week to smooth the series.

Chart 1. LU tourism stations (annual % change)

Source: London Underground

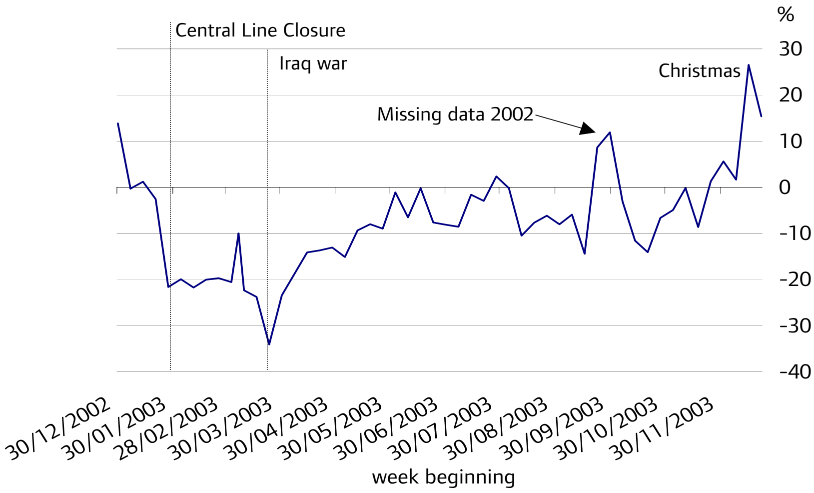
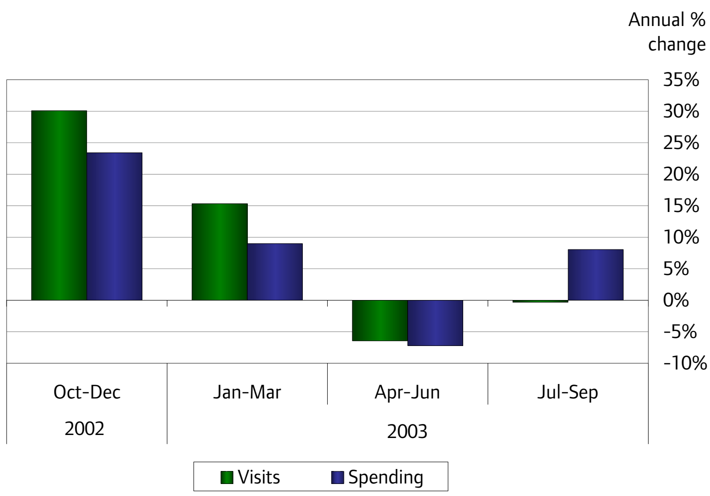


Chart 1 shows the LU tourism stations indicator and Chart 2 shows the official data on overseas tourist visits and spending for four quarters from October 2002 to October 2003. The LU data clearly reflects the major drop in overseas tourism in the second quarter 2003 due to the Iraq war. However, the dip starts in January 2003 probably reflecting the closure of the Central Line following the Chancery Lane derailment.

Chart 2. Offical data on overseas visitors and spending in London

Source: ONS



For the Employment Stations indicator, data is aggregated for 14 stations during the morning and evening peaks (ie 07:00–10:00 and 16:00–19:00). The stations are: Old Street, Liverpool Street, Bank and Monument, St Paul's, Chancery Lane, Moorgate, Barbican, Farringdon, Aldgate, Tower Hill, Cannon Street, Mansion House, Blackfriars and Holborn. This data is then further aggregated by week. There is some overlap between the groups of tourism and employment stations, but since the indicators cover different time periods, this should not cause double counting.

Chart 3. LU employment stations

Source: London Underground

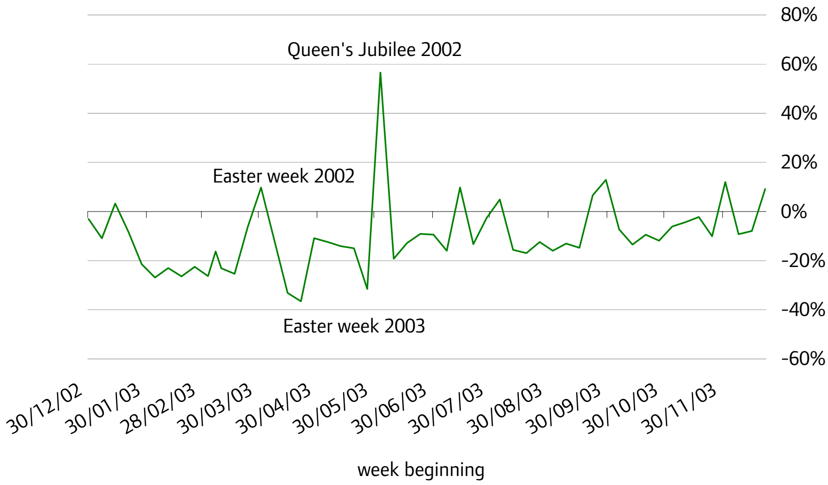
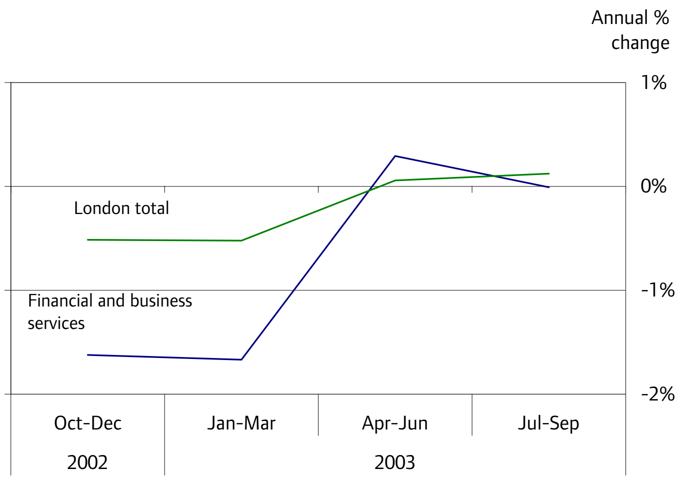


Chart 3 shows the LU counts data for employment stations, and Chart 4 the official data for comparison. Disregarding the volatility in the series, it does nonetheless appear to capture the gradual recovery in the official data from slightly negative in the beginning of the year, to around zero, or no annual change, towards the end of the year.

Chart 4. Official employee jobs data (annual % change)

Source: STES, ONS



The comparison with official data shows that while the LU-based indicators are far from perfect, they do seem to pick up on major movements. Caution should be used in interpreting the data, especially in investigating what events (eg bank holidays, strikes) might be distorting it. It should also be remembered that a decrease in underground numbers might reflect a modal shift away from the underground to buses for example. GLA Economics will continue to develop these indicators and test their reliability.

Additional information

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
BAA	British Airports Authority
BCC	British Chamber of Commerce
BITOA	British Incoming Tour Operators Association
CAA	Civil Aviation Authority
CBI	Confederation of British Industry
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, Bank of England
ONS	Office of National Statistics
PMI	Purchasing Managers' Index
PWC	PricewaterhouseCoopers
RICS	Royal Institute of Chartered Surveyors

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