

London's Economic Outlook: Autumn 2009

The GLA's medium-term planning projections



**Transport
for London**

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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 form a basis for the policy and investment decisions facing the Mayor of London and the GLA group. The unit is funded by the Greater London Authority, Transport for London and the London Development Agency.

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1. Executive summary

GLA Economics' fifteenth London forecastⁱ suggests that:

- London's Gross Value Added (GVA) growth rate should fall to -3.5 per cent in 2009. Growth should remain negative in 2010 before rising to 1.5 per cent in 2011.
- London is likely to see contractions in employment in 2009, 2010 and 2011.
- London household spending will probably fall in 2009 and 2010 before growing slowly in 2011. London household income will probably fall in 2009 before growing slowly in 2010 and 2011.

Table 1.1 summarises this report's forecasts and provides an average of independent forecasts.

Table 1.1: Summary of forecasts

Annual growth rates (per cent)	2008	2009	2010	2011
London GVA (constant 2003 £ billion)	1.4	-3.5	-0.2	1.5
<i>Consensus (average of independent forecasts)</i>		-3.6	-0.4	2.1
London civilian workforce jobs	0.7	-3.4	-2.3	-0.6
<i>Consensus (average of independent forecasts)</i>		-3.6	-2.1	-0.1
London household spending (constant 2003 £ billion)	2.8	-3.0	-1.9	0.5
<i>Consensus (average of independent forecasts)</i>		-3.5	-0.6	1.3
London household income (constant 2003 £ billion)	3.1	-2.3	0.6	1.7
<i>Memo: Projected UK RPIⁱⁱ (Inflation rate)</i>		-1.1	1.8	2.2
<i>Projected UK CPIⁱⁱⁱ (Inflation rate)</i>		1.7	1.6	1.4

Sources: GLA Economics' Autumn 2009 forecast and consensus calculated by GLA Economics.

2. Introduction

The autumn 2009 edition of *London's Economic Outlook* (LEO) is GLA Economics' fifteenth London forecast. The forecasts are issued every six months to assist those preparing planning projections for London in the medium term. The report contains the following:

- An overview of recent economic conditions in London, the UK and the world economies with analysis of important events, trends and risks to short and medium-term growth (Section 3).
- The 'consensus forecast' – a review of independent forecasts indicating the range of views about London's economy and the possible upside and downside risk (Section 4). In this document, 'consensus forecast' refers to the average of the four independent forecasters listed under Section 2.1.
- The GLA Economics forecast for output, employment, household expenditure and household income in London (Section 5).

2.1 Note on the forecast

Any economic forecast is what the forecaster views as the economy's most likely future path and as such is inherently uncertain. Both model and data uncertainty as well as unpredictable events contribute to the potential for forecast error. GLA Economics' forecast is based on an in-house model built by Volterra Consulting Limited. GLA Economics' review of independent forecasts provides an overview of the range of alternative opinions. Independent forecasts are supplied to the GLA for the main macroeconomic variables by the following organisations:

- Cambridge Econometrics (CE)
- The Centre for Economic and Business Research (CEBR)
- Experian Business Strategies (EBS)
- Oxford Economics (OE)

Only the most likely outcomes, which the different forecasting organisations provide, are recorded. Each forecaster may also prepare scenarios they consider less likely but these are not shown here. The low and high forecasts combine the lowest and highest forecasts respectively taken from each year separately and which, may therefore, come from different forecasters. High and low estimates therefore may not represent the view of any one forecaster over the whole of the forecast period.

Economic forecasting is not a precise science. These projections provide an indication of what is most *likely* to happen, not what will *definitely* happen.

3. Economic background: UK and advanced economies show signs of stabilisation

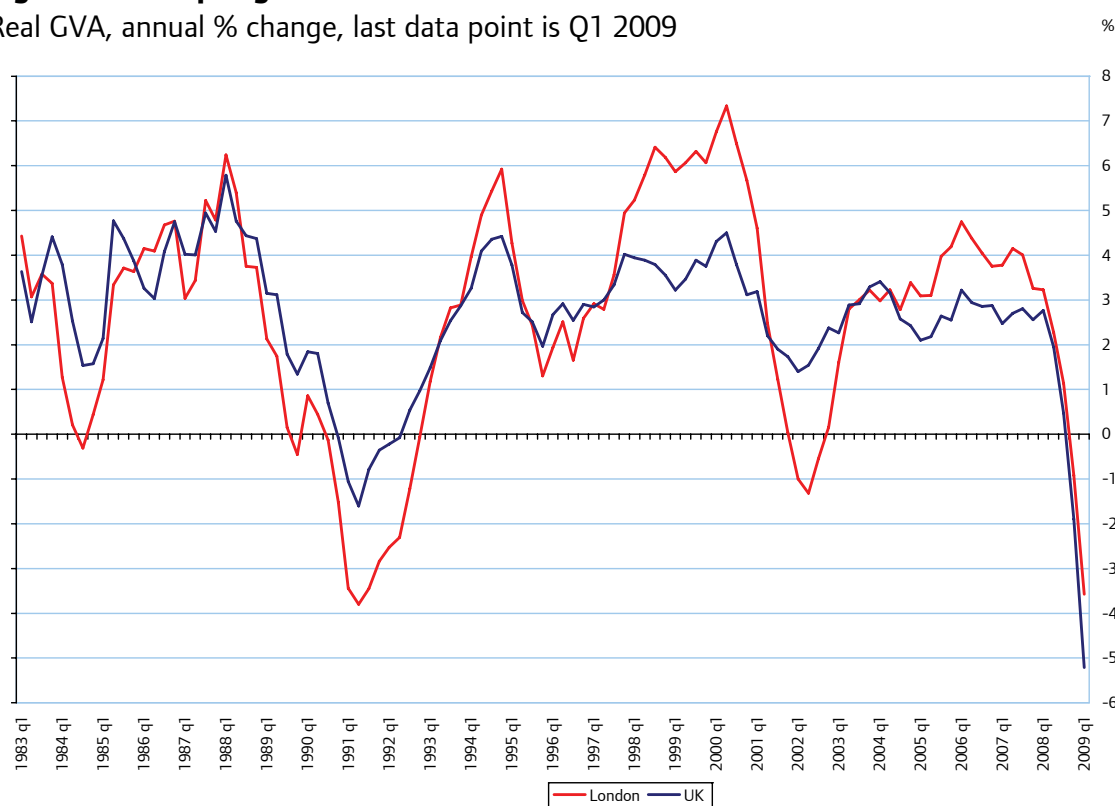
This section provides an overview of recent developments in the London, UK and world economies.

3.1 The London economy

London's economic output contracted at an annualised rate of -3.6 per cent in quarter one of 2009 compared to -5.2 per cent in the UK. Annual economic growth in London has been stronger than the UK as a whole since the third quarter of 2004.

Figure 3.1: Output growth – London and UK

Real GVA, annual % change, last data point is Q1 2009

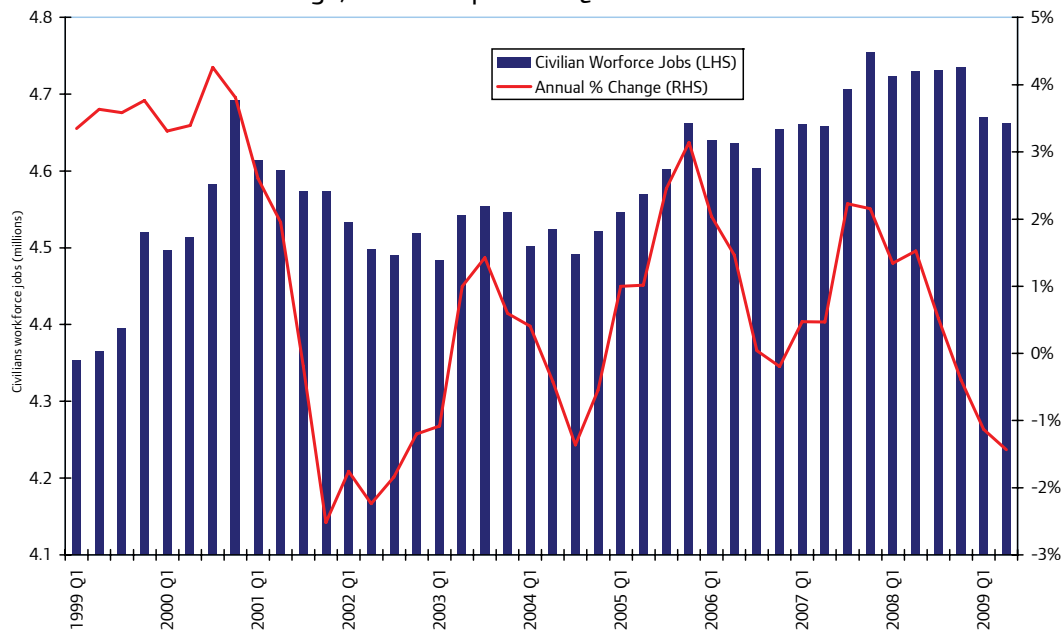


Source: Experian Business Strategies

Annual employment growth in London remained negative in the second quarter of 2009 at -1.4 per cent compared to -1.1 per cent in the previous quarter. The total number of workforce jobs in London was just over 4.6 million in quarter two 2009 (see Figure 3.2).

Figure 3.2: London civilian workforce jobs

Level and annual % change, last data point is Q2 2009

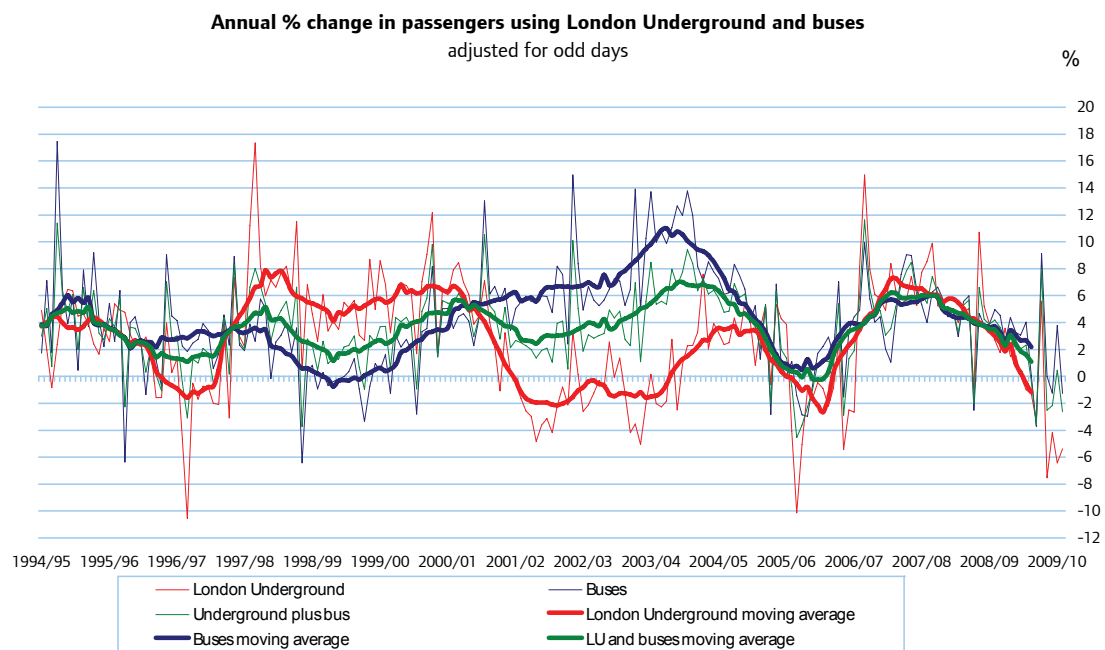


Source: Office for National Statistics

Public transport usage is a useful and timely indicator of economic activity in London. Figure 3.3 shows there has been a continued slow down in the annual growth in the moving average of both bus and underground usage in 2009. Annual growth in the moving average for underground usage recently turning negative.

Figure 3.3: London public transport usage

Annual % change in passengers using London Underground and buses (adjusted for odd days). Last data point is the 28-day period ending 25/07/09

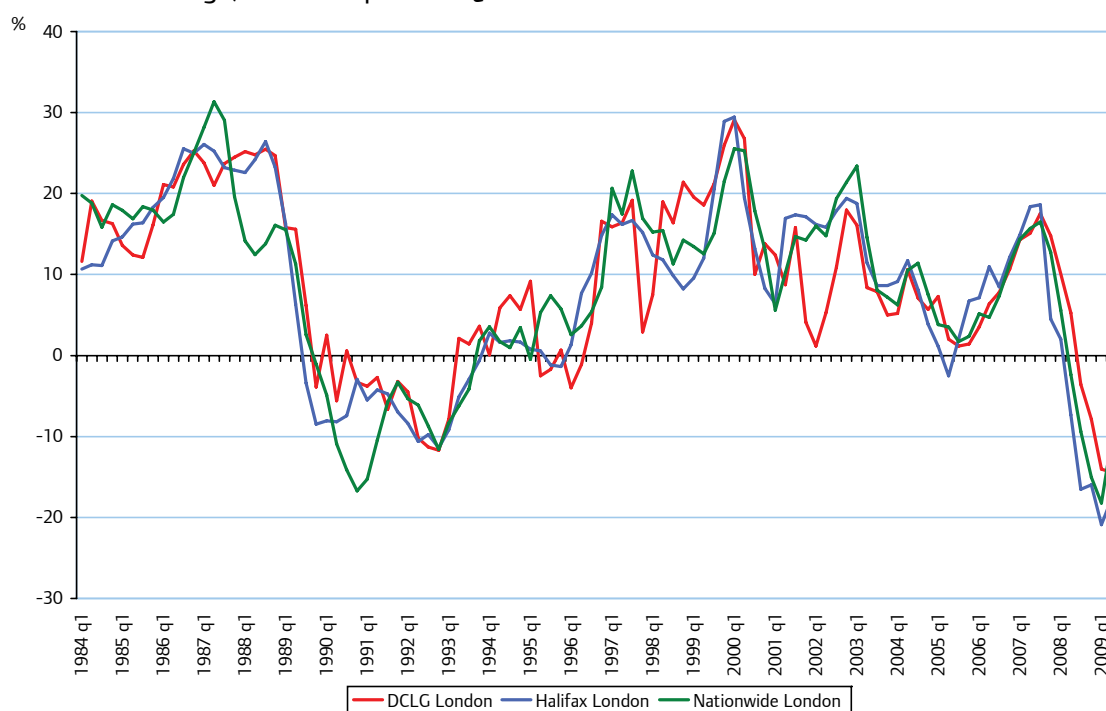


Source: Transport for London

Annual house price inflation slowed in the second half of 2007 and turned negative in 2008, although there have been recent signs of some improvement in the market^{iv}. Still with tightened lending criteria, subdued lending^v, and the continued economic downturn, house prices are likely to remain restrained for some time yet. Annual house price inflation in London as measured by DCLG, the Halifax house price index and Nationwide was very negative in the second quarter of 2009 (see Figure 3.4) and was close to the picture seen in the rest of the UK.

Figure 3.4 House price inflation in London

Annual % change, last data point is Q2 2009



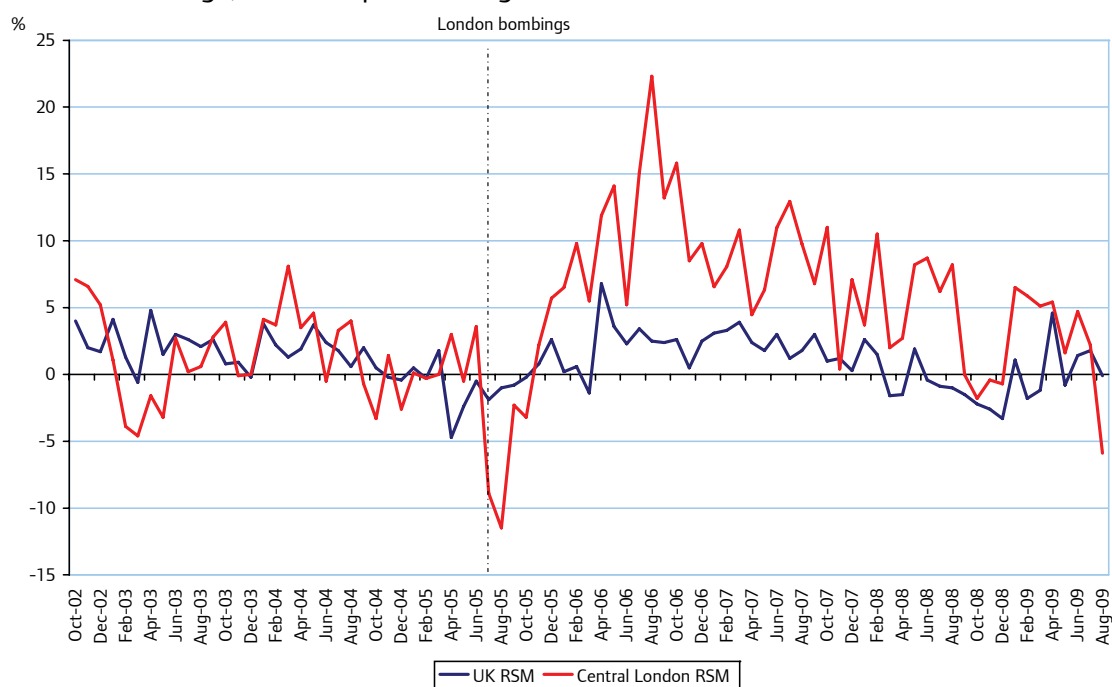
Source: DCLG, Halifax house price index, Nationwide

London's commercial property market began to pick up in the second quarter of 2009 from very low levels. Take-up rose "across all markets to 1.7 m sq ft as occupier sentiment improved noticeably from the first quarter's levels" and "there was a significant rise in investment turnover as purchasers took advantage of the perceived value in the Central London market" with transactions valued at £1.4 billion "more than double the previous quarters total". Still "availability continued to increase and now stands at 24.3 m sq ft, a 9.0% rise on the previous quarter's level", and "speculative construction activity continued to fall and is now 36% lower than last year"^{vi}.

The retail sector in Central London was weak in the final quarter of 2008 but had rebounded in the first half of 2009, before suffering a significant fall in August 2009. Retail sales fell by 5.9 per cent in August 2009 compared with a year earlier as monitored by the London Retail Consortium (see Figure 3.5). Meanwhile UK retail sales fell by 0.1 per cent in August 2009 compared to August 2008. Since November 2005, annual retail sales growth in the UK has remained below that of Central London apart from in November 2007 and August 2009.

Figure 3.5: Retail sales growth – Central London and the UK

Annual % change, last data point is August 2009

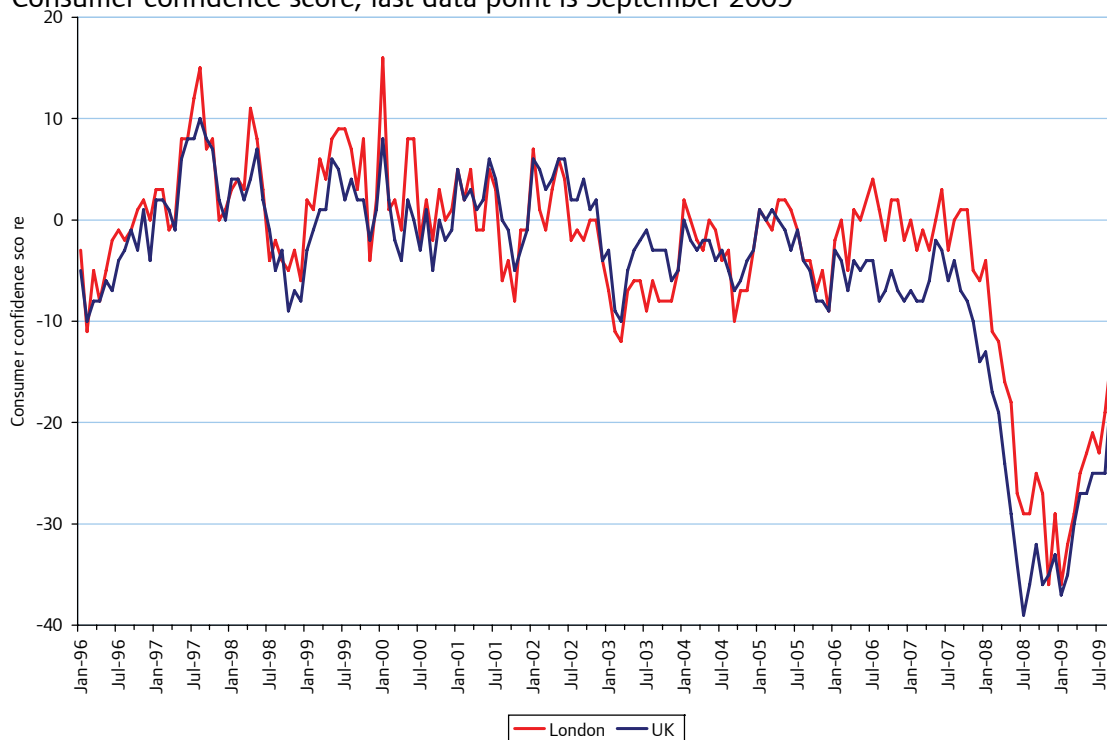


Source: UK Retail Sales Monitor – BRC/KPMG, Central London Retail Sales Monitor – London Retail Consortium

GfK NOP's regional consumer confidence index (see Figure 3.6) shows that consumer confidence is quite similar in London and the UK as a whole. There was a significant downturn in confidence in both London and the UK after the latter part of 2007 that coincided with the credit crunch. Confidence in September 2009 was higher than at the turn of 2009, however it still indicates that the current economic slowdown is negatively impacting upon consumers' expectations. The index 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.

Figure 3.6: GfK NOP's regional consumer confidence index

Consumer confidence score, last data point is September 2009



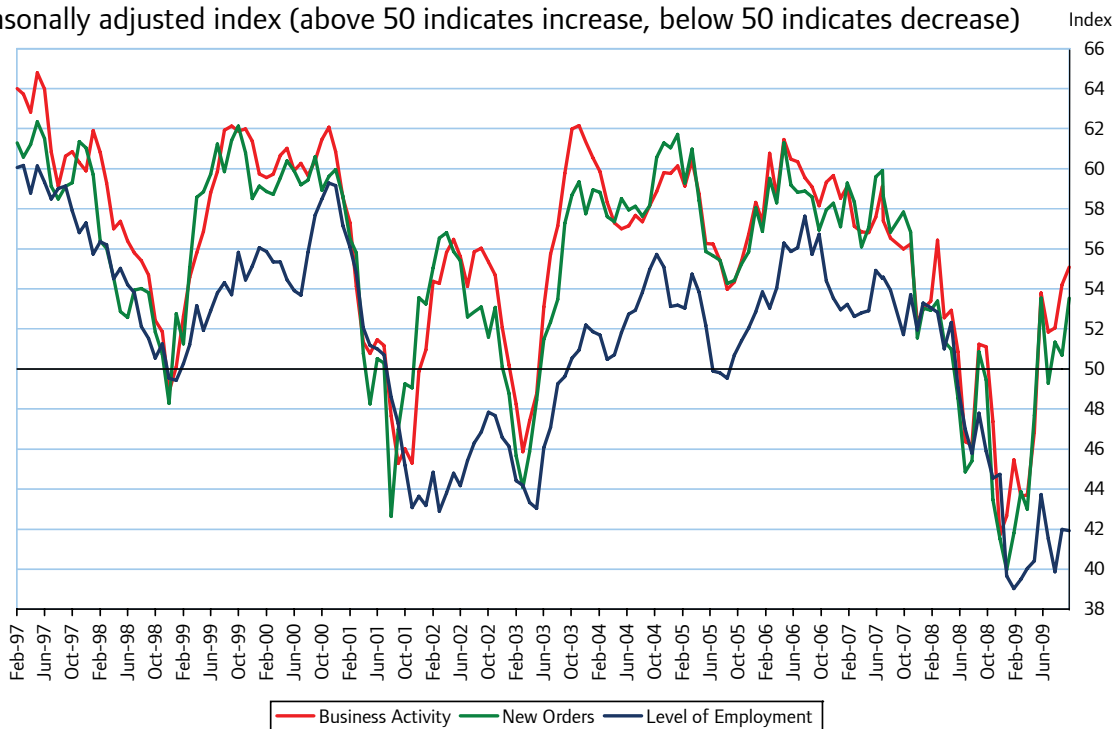
Source: GfK NOP on behalf of the European Commission

Business survey results indicate that business activity and new orders for London firms stabilised during the summer, although employment still shows a sharp contraction (see Figure 3.7).

Figure 3.7: Recent survey evidence on London's economic climate

Purchasing Manager's Index (PMI) survey, last data point September 2009

Seasonally adjusted index (above 50 indicates increase, below 50 indicates decrease)



Source: Markit Economics

3.2 The UK economy

UK Gross Domestic Product (GDP) fell by an estimated -0.6 per cent in the second quarter of 2009. This followed a fall of -2.5 per cent in the first quarter of 2009. The UK economy remains in its first recession (defined as two or more consecutive quarters of declining GDP) since the early 1990s (see Box 3.1).

Table 3.1: HM Treasury and consensus forecasts for the UK economy

Annual % change, unless otherwise indicated

	Average of Independent Forecasters		Budget April 2009	
	2009	2010	2009	2010
GDP growth (per cent)	-4.3	1.0	-3¾ to -3¼	1 to 1½
Claimant unemployment (Q4: mn)	1.81	2.09	-	-
Current account (£bn)	-27.6	-24.1	-48½	-51
PSNB (2009-10, 2010-11: £bn)	182.4	184.3	175	173

Note: mn = million, bn = billion

Sources: HM Treasury Comparison of Independent Forecasts, September 2009.

HM Treasury Financial Statement and Budget report Chapter B: The Economy and Chapter C: The Public Finances.

As can be seen in Table 3.2 annual growth was negative across the board in Q1 and Q2 of 2009. Manufacturing and construction both saw double digit negative annual growth rates in both Q1 and Q2 of 2009.

Table 3.2: Recent growth in broad industrial sectors of UK economy

Annual % change

Industrial sectors	2008				2009	
	Q1	Q2	Q3	Q4	Q1	Q2
Agriculture, forestry, and fishing	-1.9%	0.9%	1.8%	-0.4%	-0.6%	-5.6%
Mining & quarrying inc oil & gas extraction	-5.2%	-6.2%	-6.6%	-8.6%	-8.2%	-8.3%
Manufacturing	0.9%	-1.1%	-2.9%	-8.3%	-13.7%	-12.4%
Electricity gas and water supply	2.4%	2.7%	-0.1%	-4.5%	-6.7%	-10.2%
Construction	3.1%	1.6%	-0.3%	-5.7%	-13.0%	-13.4%
Distribution, hotels and catering	2.5%	1.0%	-2.3%	-5.3%	-7.0%	-6.7%
Transport, storage and communication	2.0%	2.2%	2.6%	0.1%	-4.7%	-7.0%
Business services and finance	4.6%	3.8%	1.3%	0.4%	-3.7%	-4.9%
Government and other services	1.2%	1.4%	2.0%	0.7%	-0.6%	-0.8%

Source: Office for National Statistics (as of end-September 2009)

Table 3.3 shows that annual household spending was negative during the first half of 2009, whilst investment continued to fall heavily. These trends may well moderate during the rest of 2009 and into 2010.

Table 3.3: UK domestic expenditure growth

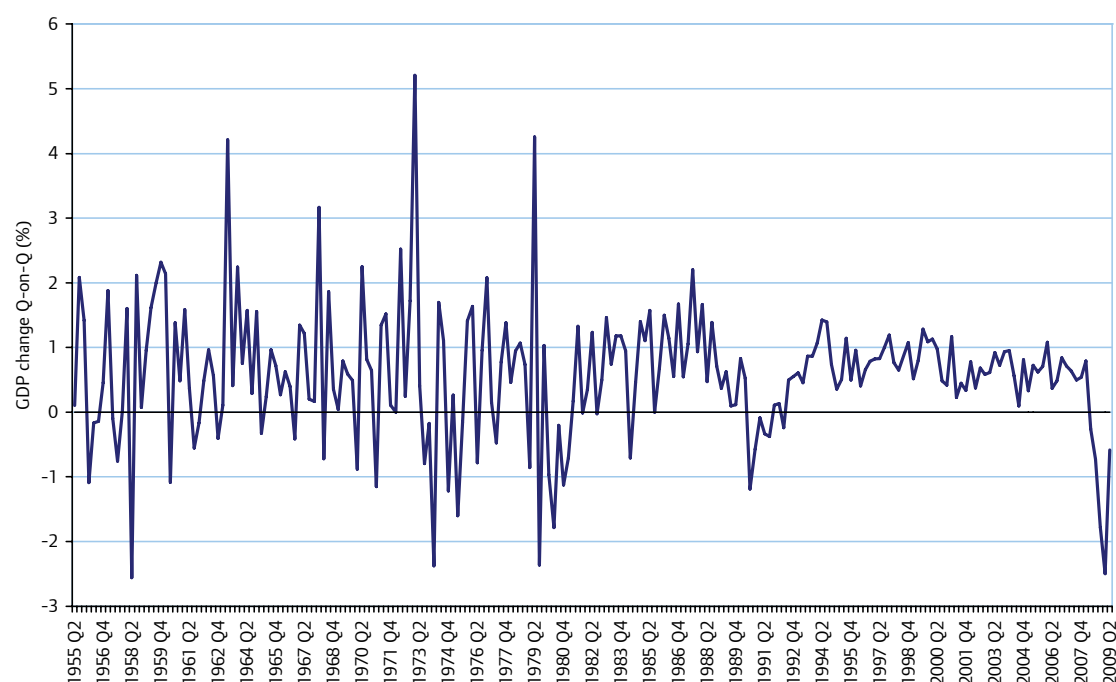
Annual % change

Expenditure	2008				2009	
	Q1	Q2	Q3	Q4	Q1	Q2
Households	2.2%	1.5%	0.7%	-0.8%	-3.1%	-3.6%
Non-profit institutions	3.7%	5.4%	3.8%	-0.7%	-4.0%	-7.6%
General Government	2.1%	2.5%	2.2%	3.1%	2.3%	2.2%
Gross fixed capital formation	-0.5%	0.0%	-3.9%	-8.7%	-12.2%	-17.2%

Source: Office for National Statistics (as of end-September 2009)

Box 3.1: The current UK recession in historical context

Although unusual in the context of very recent macroeconomic history the current recession is not uncommon in light of UK economic history, although it is likely that in its severity this recession will be the worst experienced by the UK in the post war period. Still, there have been a number of recessions (defined as two or more consecutive quarters of contraction in GDP) in the UK since 1945^{vii}, with prior to the current recession the most recent ones occurring in 1973/74, 1975, 1980/81, and 1990/91 (see Figure 3.8). These recessions lasted for a varying degree of quarters with the recessions of 1980/81 and 1990/91 lasting 5 quarters. The current recession has however so far seen larger falls in UK GDP than seen at comparable stages in previous recessions, with output having fallen by 5.6 per cent after five quarters of the current recession compared to only 2.5 per cent after five quarters of the 1990s recession and 4.7 per cent after five quarters of the 1980s recession^{viii}. The period of recovery from previous recessions have also varied. Output took eight quarters to return to its pre-recession levels after the 1980/81 and 1990/91 recessions ended.

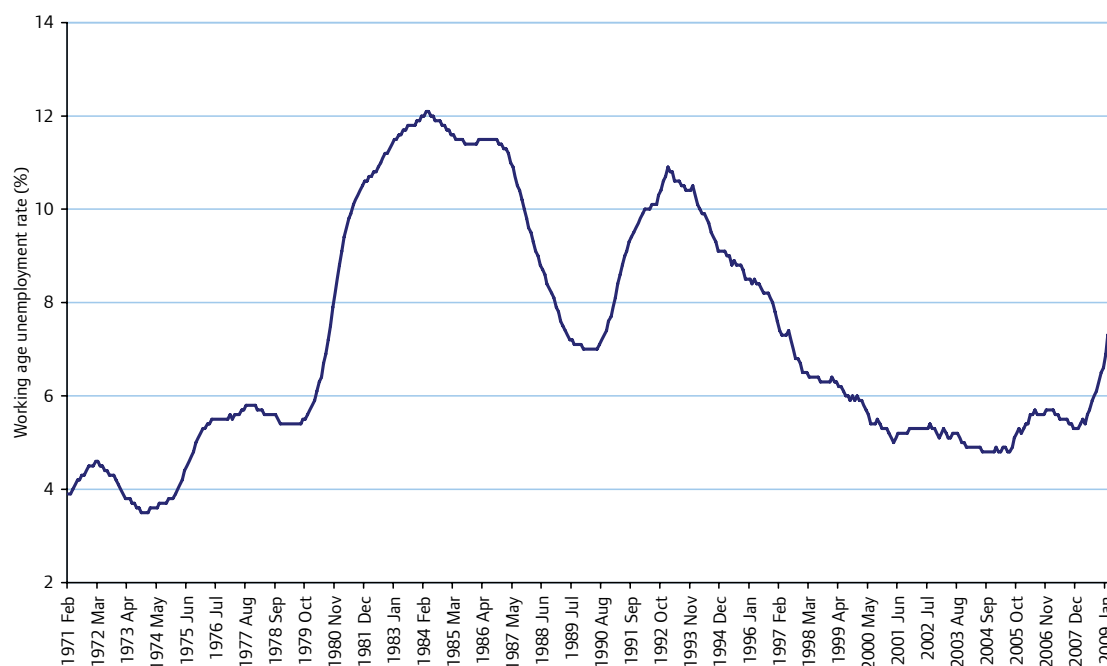
Figure 3.8 UK quarterly economic growth since 1955


Source: ONS (as of end-September 2009)

The causes of the recessions also varied with the 1970s recessions being triggered by the oil price shocks, the early 1980s recession triggered by the general economic malaise from the 1970s and the policy response to it, whilst the early 1990s recession was exacerbated by the Exchange Rate Mechanism (ERM). Given their different causes, deducing the likely outcome of this recession from previous recessions is impossible, however trends that have been followed in previous downturns are likely to be experienced again and give a guide to a possible course for the recession.

The previous recessions generally saw large increases in the unemployment rate (see Figure 3.9). Significant rises in the rate of unemployment were observed in the early 1980s recession and the early 1990s recession (though the increase was lower in the early 1990s recession). A similar situation is observed in the current recession with the Labour Force Survey (LFS) unemployment rate already hitting levels not seen since the mid 1990s. However as noted in the August 2009 Inflation Report^{ix} “at similar points in the 1980s and 1990s recessions, employment had fallen by more than in the current episode, despite smaller falls in output”. It is believed that this could partially be due to the more flexible labour market that the UK now has compared to the past with companies being more able to respond to a downturn in demand by introducing flexible working and by reducing hourly pay. There is however concern that this may have only delayed the full increase in unemployment.

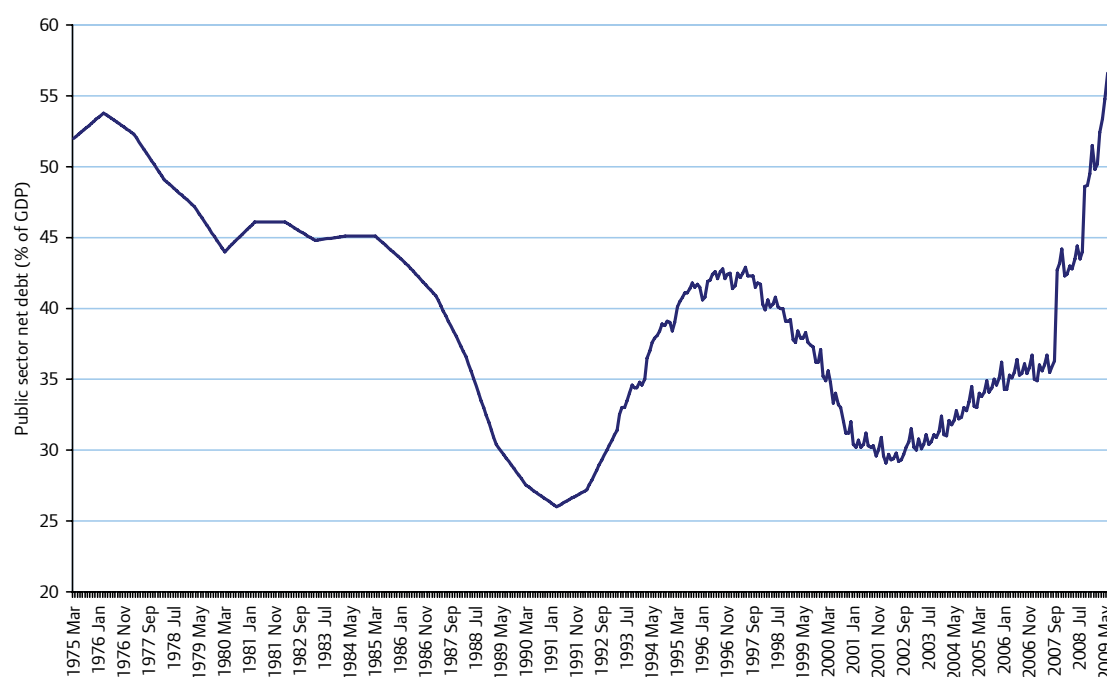
Figure 3.9: Unemployment rate since 1971 (LFS measure)



Source: ONS (as of end-September 2009)

As shown in Figure 3.10 public sector net debt has risen sharply during the current recession with analysis from the Institute for Fiscal Studies (IFS) showing that borrowing over the first five months of 2009/10 "has been two-and-a-half times as large as over the same months last year"^x. Further an initial examination of the 2009 Budget indicated that it did not foresee the budget balancing before 2017/18^{xi}. A further significant rise in public debt is therefore expected with the IFS calculating from Budget 2009 data that "the economic and financial crisis has increased the UK's underlying structural budget deficit by around 6.4% of national income. Unaddressed, this implies that the Government would have to borrow almost 8% of national income indefinitely"^{xii}. A similar if significantly smaller rise in public debt was experienced after the early 1990s recession, which required a tightening of public finances. A major tightening in public finances is expected over the coming years.

Figure 3.10: UK Public Sector Net Debt as a proportion of GDP since 1975



Source: ONS (as of end-September 2009). Note that data starts on an annual basis and finishes on a monthly basis.

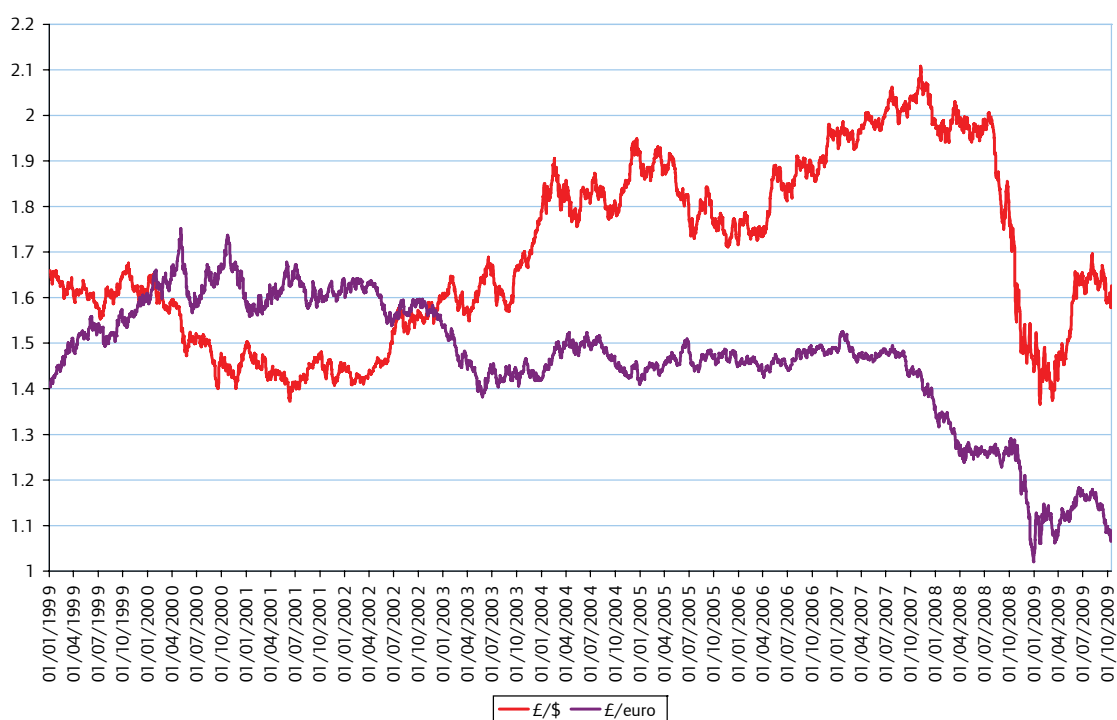
Although this recession shares many characteristics of previous recessions in other respects it differs. The most obvious example being the financial crisis in autumn 2008 which exacerbated the speed and magnitude of the current downturn and which research by the IMF indicates is likely to hamper the speed of any economic recovery^{xiii}. A further difference was the precarious nature of household finances at the start of the current downturn, with the household savings ratio in the UK having declined to -0.5 per cent in Q1 2008 and with it having been significantly below the long-term average for the UK for most of the 2000s. Thus it is likely that rebalancing of household balance sheets will need to occur. If this occurs too quickly this could seriously constrain consumer consumption decisions and therefore any economic recovery.

Although the strength and scale of any recovery is still in question it seems most likely to be slow and bumpy. As after previous recessions the initial up swing in GDP is likely to be driven by slowing destocking and then restocking. Any up swing, like after the 1990s recession will be aided by the recent significant depreciation of sterling. However, the required public sector fiscal restraint, tight credit conditions, rebalancing of household finances and the future withdrawal of the current extraordinarily loose monetary policy will all dampen economic growth over the next few years.

Interest rates have remained steady at 0.5 per cent since the Spring 2009 LEO and the Bank of England has continued its programme of Quantitative Easing (see Box 3.2). Annual consumer price index (CPI) inflation has fallen to 1.1 per cent in September 2009, from a recent high of 5.2 per cent in September 2008, whilst retail price index (RPI) inflation stood at -1.4 per cent. Inflation is now expected to pick up but downside risks to inflation in the medium term remain high due to an increase in unutilised national and global production capacity. The main upside risks to UK inflation is the depreciation of sterling since mid-2007 (see Figure 3.11), and that the Bank of England may be too slow in reeling back the current extraordinarily loose monetary policy in light of any economic upturn.

Figure 3.11: £ to \$ and £ to euro exchange rates

Last data point is 15/10/09



Source: Bank of England

The weakness of sterling is further illustrated by sterling's effective exchange rate index (EERI)^{xiv} (see Figure 3.12). There had been a fall of roughly 30 per cent since its recent peak in early 2007 up to March 2009. Sterling then rebounded somewhat before coming under pressure again in September and early October. The depreciation of sterling should provide some support to the UK economy due to import substitution as

well as increasing the competitiveness of the UK's exports. For example there is some evidence that a weaker pound has encouraged more UK tourists to take their holidays at home (including obviously to London).

Figure 3.12: Sterling EERI rate

Last data point is 14/10/09



Source: Bank of England

Box 3.2: Quantitative Easing

With interest rates cut to half a percentage point by March 2009 and the economy mired in recession the Bank of England has found it necessary to undertake more unorthodox actions to stimulate the economy such as Quantitative Easing (QE), which is the purchasing of assets using central bank money. The Bank of England notes that “the aim of quantitative easing is to inject money into the economy in order to revive nominal spending. The Bank is doing that by purchasing financial assets from the private sector. When it pays for those assets with new central bank money, in addition to boosting the amount of central bank money held by banks, it is also likely to boost the amount of deposits held by firms and households. This additional money then works through a number of channels^{xv}. Three key channels are:

1. **Asset prices and portfolio effects.** Purchases of assets financed by central bank money should push up the prices of assets. Higher asset prices mean correspondingly lower yields, reducing the cost of borrowing for households and companies leading to higher consumption and investment spending.
2. **Bank lending and quantity effects.** Banks end up with higher reserve balances held at the Bank of England as a result of asset purchases. These injections of reserves may make it easier for banks to finance a higher level of liquid assets. A higher level of liquid assets could encourage them to extend more new loans than they would otherwise have done.
3. **Expectations.** Asset purchases could have an important impact on expectations. By demonstrating that the MPC will do whatever it takes to meet the inflation target, expectations of future inflation should remain anchored to the target when there was a risk that they might otherwise have fallen^{xvi}.

On 5 March the Bank announced that it would create a £75 billion asset purchase package of mainly government gilts, which would be financed by the creation of central bank reserves. This was expanded to £175 billion on 6 August, with it now being worth the equivalent of roughly 12 per cent of GDP. The Bank in announcing this increase warned that, although the recession might soon come to an end, recovery might be slower and take longer than most people currently expect. The Bank was worried that, without additional stimulus, any recovery might be throttled by a shortage of lending to both businesses and individuals. In fact, the minutes of the meeting revealed that the Governor (as well as Tim Besley and David Miles) would have preferred an even larger increase in the size of the quantitative easing programme, taking it to £200bn^{xvii}. The fact that three members of the Committee wanted even more quantitative easing reflects the Committee's overall view that the risks to both inflation and economic growth over the medium term are still to the downside.

The effects so far of QE on the UK economy are hard to judge. However, David Miles in a speech on 30/9/09 titled 'Money, Banks and Quantitative Easing' believes that QE will support spending. He states that evidence is already consistent with the following three portfolio effects:

1. Gilt yields should fall in a way that went beyond what you would expect as people change their views on the evolution of the policy rate (Bank Rate).
2. That was reflected in a lower cost of issuing corporate bonds for companies.
3. And as a result issuance of bonds (and also equities) by companies increased as the sellers of gilts looked to alternative assets with a maturity that was closer to the assets they sold than bank deposits paying rates linked to short term interest rates^{xviii}.

3.3 The world economy

The IMF projected in October that the world economy would contract by 1.1 per cent in 2009^{xix}, with growth of 3.1 per cent forecast for 2010. Meanwhile the OECD forecasts a rise in output of 1.2 per cent in the third quarter of 2009 and 1.4 per cent in the fourth quarter of 2009 for the G7 countries, with an implied growth rate of -3.7 per cent in 2009^{xx}.

Developed economies are forecast to remain weak with the US economy projected by the IMF to decline by 2.7 per cent in 2009 and grow by only 1.5 per cent in 2010^{xxi} (an improvement on their July projections). The Eurozone economy is projected to decline by 4.2 per cent in 2009 and grow by 0.3 per cent in 2010^{xxii}. Growth in emerging market economies and developing economies is expected to slow from 6.0 per cent in 2008 to 1.7 per cent in 2009 before picking up to 5.1 per cent in 2010^{xxiii}. The IMF observes that "after a deep global recession, economic growth has turned positive, as wide-ranging public intervention has supported demand and lowered uncertainty and systemic risk in financial markets"^{xxiv}. It further notes that, "nonetheless, the recovery is expected to be slow, as financial systems remain impaired, support from public policies will gradually have to be withdrawn, and households in economies that suffered asset price busts will continue to rebuild savings. Risks to the outlook remain on the downside"^{xxv}.

In relation to the financial market and its stability the IMF notes that “systemic risks have been substantially reduced following unprecedented policy actions and nascent signs of improvement in the real economy. We appear now to be embarking on the road to recovery”^{xxvi}. However, it further notes that credit “remains strained, while household and financial sector balance sheet pressures and ongoing market dysfunctions remain drags on the recovery. This underscores the need for adopted policies to be more fully implemented, while others need to be fine-tuned or extended to ensure that confidence is restored further and credit channels are reopened. Equally, there is a medium-term need to reduce and ultimately reverse the transfer of private risk to sovereign balance sheets”.

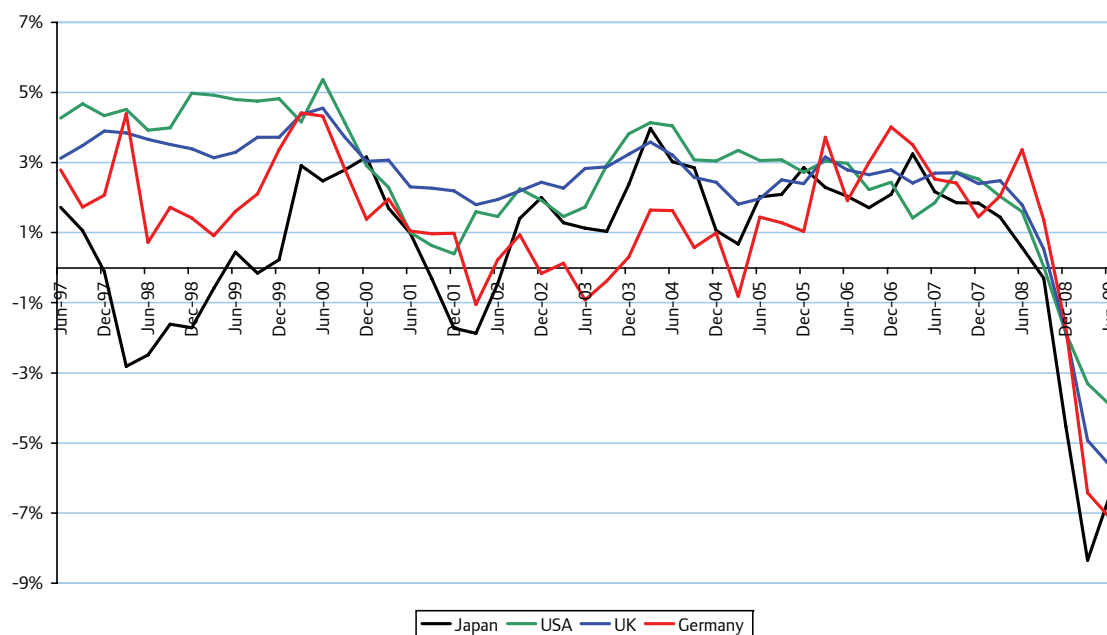
The **US** economy continued to shrink in the first two quarters of 2009. Unemployment has also continued to rise and stood at 9.7 per cent, a 26-year high, in August 2009^{xxvii}, which represents a loss of 6.9 million jobs since December 2007. However, the September 2009 Beige Book from the Federal Reserve reported “that economic activity continued to stabilize in July and August”^{xxviii}. Interest rates also remain low at a target rate of between 0 and 0.25 per cent, whilst support continues to be provided to the banking sector.

The **Eurozone** economy continued to contract in the second quarter of 2009^{xxix}, with output falling by 0.2 per cent, although this was less than the reduction of 2.5 per cent seen in the first quarter. The German and French economies resumed growth at a rate of 0.3 per cent in Q2 2009 with their economies being aided by considerable government support. The European Commission expects Eurozone output to decline by 4 per cent in 2009^{xxx}. There are concerns about structural imbalances in some European economies that may hamper the long-term prospects of the Eurozone economy^{xxxi}.

Japan's economy grew by 0.6 per cent in the second quarter of 2009. The IMF forecasts that Japanese output will fall by 5.4 per cent in 2009 and rise by only 1.7 per cent in 2010^{xxxii}.

Figure 3.13: GDP growth in selected industrialised countries

Real GDP, annual % change, last data point is Q2 2009.



Source: Ecowin

3.4 Emerging market economies

China's economy began to rebound in the second quarter of 2009 with output increasing by 7.9 per cent compared with the same period a year earlier, this compares with a decade low rate of growth of 6.1 per cent in the first quarter^{xxxiii}. The IMF forecasts that the Chinese economy will grow by 8.5 per cent in 2009 and 9.0 per cent in 2010^{xxxiv}. **India's** economy grew by an annualised 6.1 per cent in the year to Q2 2009^{xxxv}. The IMF forecasts Indian growth will be 5.4 per cent in 2009 and 6.4 per cent in 2010^{xxxvi}. **Russia's** economy contracted by an annualised rate of 10.9 per cent in the three months to the end of June^{xxxvii}, with the IMF forecasting that the Russian economy will contract by 7.5 per cent in 2009 and grow by 1.5 per cent in 2010^{xxxviii}.

3.5 Risks to the world economy

Downside risks are still prevalent to the world economic outlook, however they have lessened somewhat. Since the Autumn 2007 LEO the global credit crunch has been highlighted by GLA Economics as a downside risk and risks associated with 'toxic assets' remains a concern although perhaps to a lesser degree than that seen at the end of 2008. There are signs that the collapse in world trade that occurred at the end of 2008 and beginning of 2009 is beginning to ease. Further, the monetary policies of most central banks remains significantly relaxed providing continued support to the global economy. However, the fiscal position of many governments in the developed world is extremely weak and there is increasing evidence of the need for fiscal retrenchment. Once the global economic recovery takes hold and is on a steady footing the required monetary and fiscal tightening will dampen the speed of that recovery, especially in the

developed world. Global inflationary pressures remain subdued but the risk of a long deflationary period have reduced.

3.6 Summary

The London economy's annual rate of growth turned negative in the final quarter of 2008 and remained so in the first quarter of 2009 although it was still higher than in the rest of the UK. More recent economic indicators suggest that the London economy may have started to stabilise in the third quarter of 2009, although unemployment continues to rise. It would appear that the recession in London has so far been less severe than for the UK as a whole. The UK economy entered recession earlier than London's and its magnitude has been greater. However, this does not necessarily imply that London will perform better than the UK in the initial stages of the recovery. Consumption and especially investment are expected to remain subdued for some time to come with unemployment expected to continue to rise into 2010.

Government spending has increased in response to the recession but future fiscal retrenchment will be required in the coming years to bring the UK's public finances back to a sustainable long-term position. The temporary boost to demand provided by the reduction in VAT to 15 per cent will end with its return to 17.5 per cent at the end of 2009, which is likely to distort consumption patterns at the end of 2009 and beginning of 2010. The world economy was extremely weak during the beginning of 2009 but there is now evidence of stabilisation and some signs of growth.

One of the main downside risks remains the fragile nature of the banking sector, whilst a lesser risk surrounds any negative economic impact of swine flu^{xxxix}. London's exposure to the financial services sector possesses risks for the London economy as this sector continues to restructure and as its regulation evolves in light of the recent turmoil. Liquidity in the financial markets remains tight with the situation having improved but it is yet to return to normal. At least the depreciation of sterling since 2007 should continue to provide the economy with a boost from import substitution and improve export competitiveness. For example more people are now choosing 'staycations' rather than taking foreign holidays. Still, there remain a number of downside risks for the UK and London economies. Unemployment is expected to continue to rise, which will dampen consumption. Credit conditions remain tight for individuals and businesses so investment is likely to stay weak. At some point fiscal policy will have to be tightened and so will monetary policy. Hence, recovery can be expected to be slow and bumpy. Actual output levels will not return to pre-recession levels for a few years at least.

4. Review of independent forecasts

What the forecasts provide

In Chapter 5, GLA Economics' forecast of four economic indicators is provided: workforce employment, real output, private consumption (household expenditure) and household income in London. In this chapter the consensus view on the first three of these indicators is summarised, drawing on forecasts from outside (independent) organisations.^{xi} Both annual growth rates and 'standardised' absolute levels are reported. All the data is in real terms (constant prices). The source for all historic data in the following tables and charts is EBS.

Additionally, both the consensus and GLA Economics' own forecasts provide predictions of employment and output growth in six broad sectors:

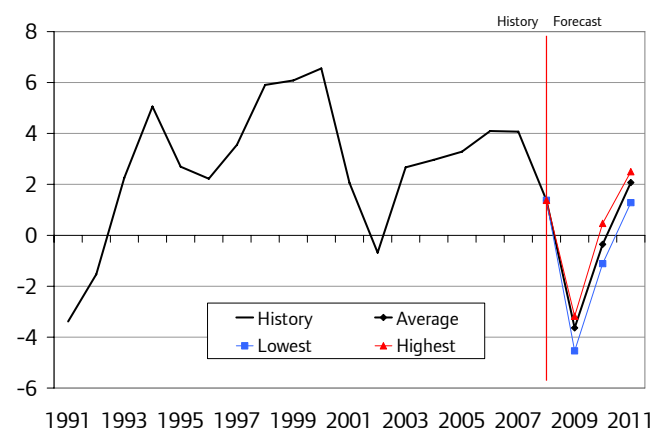
- manufacturing
- construction
- transport and communications
- distribution, hotels and catering
- finance and business services
- other (mainly public) services.

Output

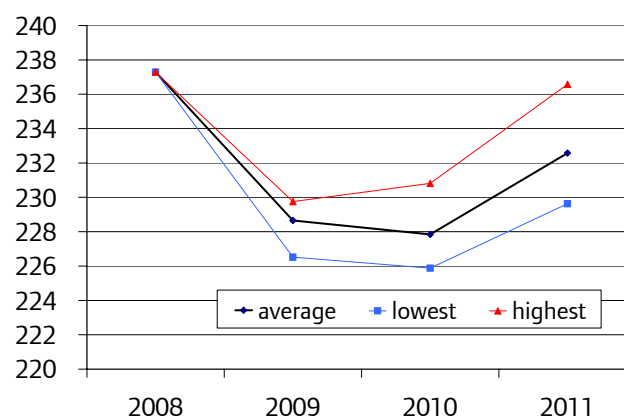
(London GVA, constant prices (2003 base year), £ billion)

The consensus (mean average view) is for real output growth to become negative in 2009 and 2010, before rebounding to 2.1 per cent in 2011.

Annual growth (per cent)



Level (constant year 2003, £ billion)



Annual growth (per cent)			
	2009	2010	2011
Average	-3.6	-0.4	2.1
Lowest	-4.5	-1.1	1.3
Highest	-3.2	0.5	2.5

Level (constant year 2003, £ billion)			
	2009	2010	2011
Average	229	228	233
Lowest	227	226	230
Highest	230	231	237

History: Annual growth (per cent)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
-1.5	2.3	5.1	2.7	2.2	3.6	5.9	6.1	6.6	2.1	-0.7	2.7	3.0	3.3	4.1	4.1	1.4

History: Level (constant year 2003, £ billion)

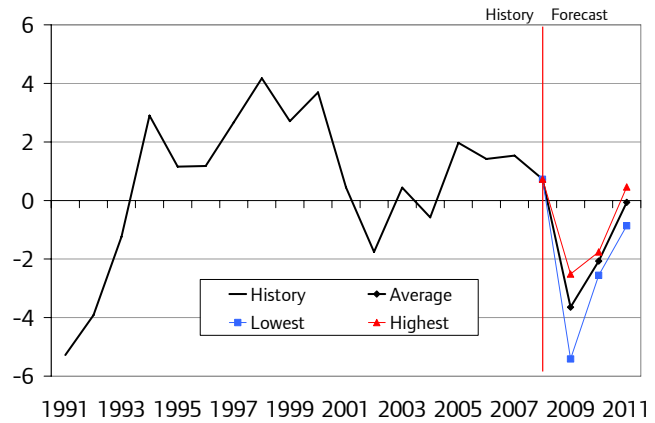
1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
139.6	142.8	150.0	154.1	157.5	163.1	172.7	183.2	195.2	199.2	197.9	203.2	209.2	216.1	224.9	234.1	237.3

Employment

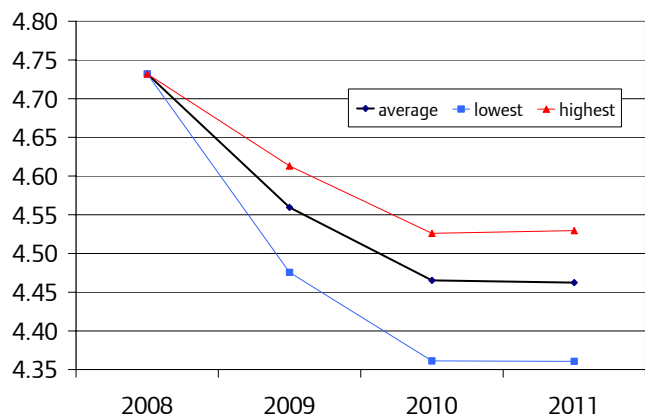
(London workforce jobs)

The consensus view is for the number of workplace jobs to decline by 3.6 per cent in 2009, by 2.1 per cent in 2010 and by 0.1 per cent in 2011.

Annual growth (per cent)



Level (millions)



Annual growth (per cent)			
	2009	2010	2011
Average	-3.6	-2.1	-0.1
Lowest	-5.4	-2.6	-0.9
Highest	-2.5	-1.8	0.5

Level (millions)			
	2009	2010	2011
Average	4.56	4.47	4.46
Lowest	4.48	4.36	4.36
Highest	4.61	4.53	4.53

History: Annual growth (per cent)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
-3.9	-1.2	2.9	1.2	1.2	2.7	4.2	2.7	3.7	0.4	-1.8	0.4	-0.6	2.0	1.4	1.5	0.7

History: Level (millions)

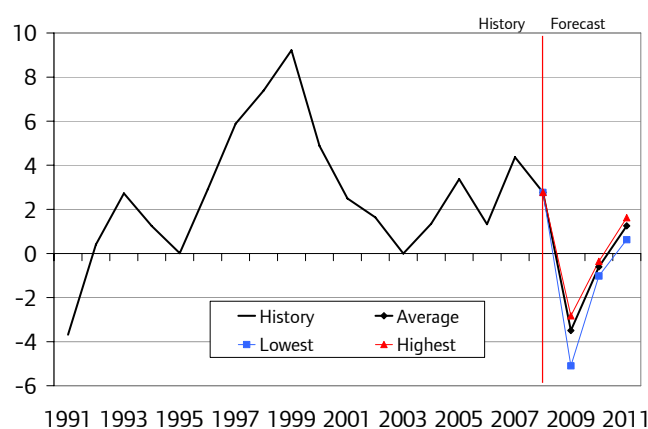
1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
3.83	3.78	3.89	3.94	3.99	4.09	4.26	4.38	4.54	4.56	4.48	4.50	4.47	4.56	4.63	4.70	4.73

Household expenditure

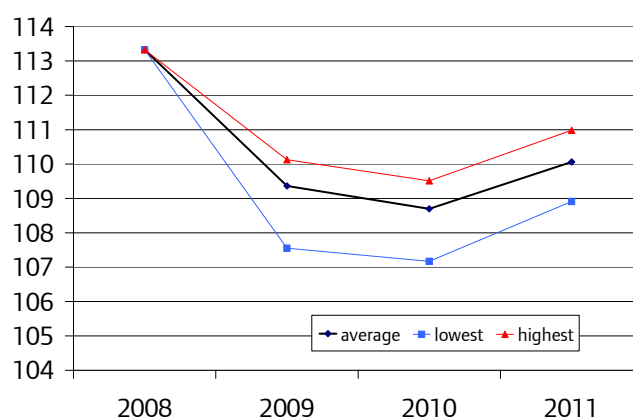
(London household spending, constant year 2003, £ billion)

The consensus view is for household expenditure growth to become negative at -3.5 per cent in 2009 and remain negative at -0.6 per cent in 2010 before picking up in 2011 to a positive growth rate of 1.3 per cent.

Annual growth (per cent)



Level (constant year 2003 £ billion)



Annual growth (per cent)			
	2009	2010	2011
Average	-3.5	-0.6	1.3
Lowest	-5.1	-1.0	0.6
Highest	-2.8	-0.4	1.6

Level (constant year 2003, £ billion)			
	2009	2010	2011
Average	109	109	110
Lowest	108	107	109
Highest	110	110	111

History: Annual growth (per cent)

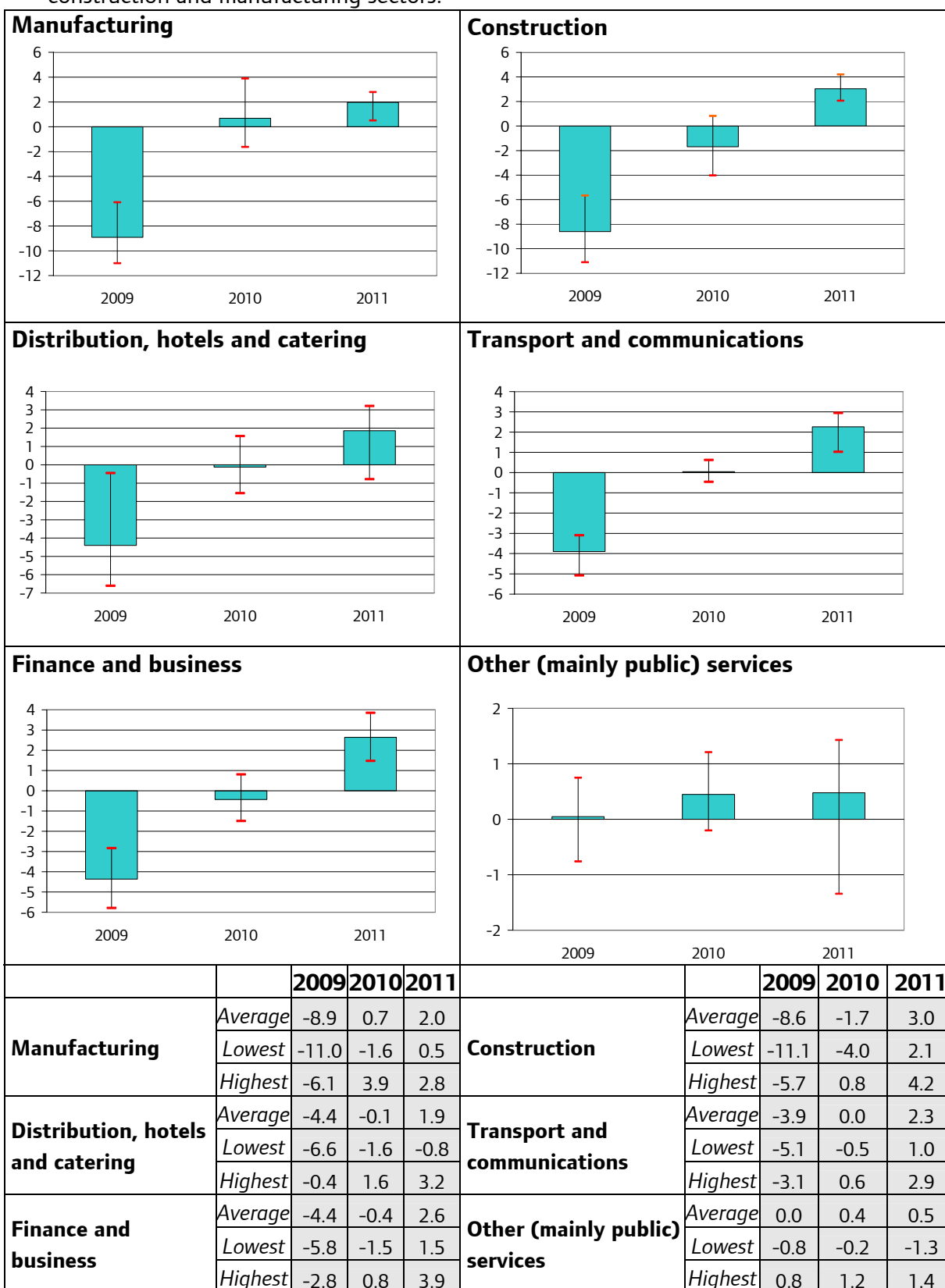
1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
0.4	2.7	1.2	0.0	2.9	5.9	7.4	9.2	4.9	2.5	1.6	0.0	1.4	3.4	1.3	4.4	2.8

History: Level (constant year 2003, £ billion)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
68.5	70.4	71.3	71.3	73.3	77.7	83.4	91.1	95.5	97.9	99.5	99.5	100.9	104.3	105.7	110.3	113.3

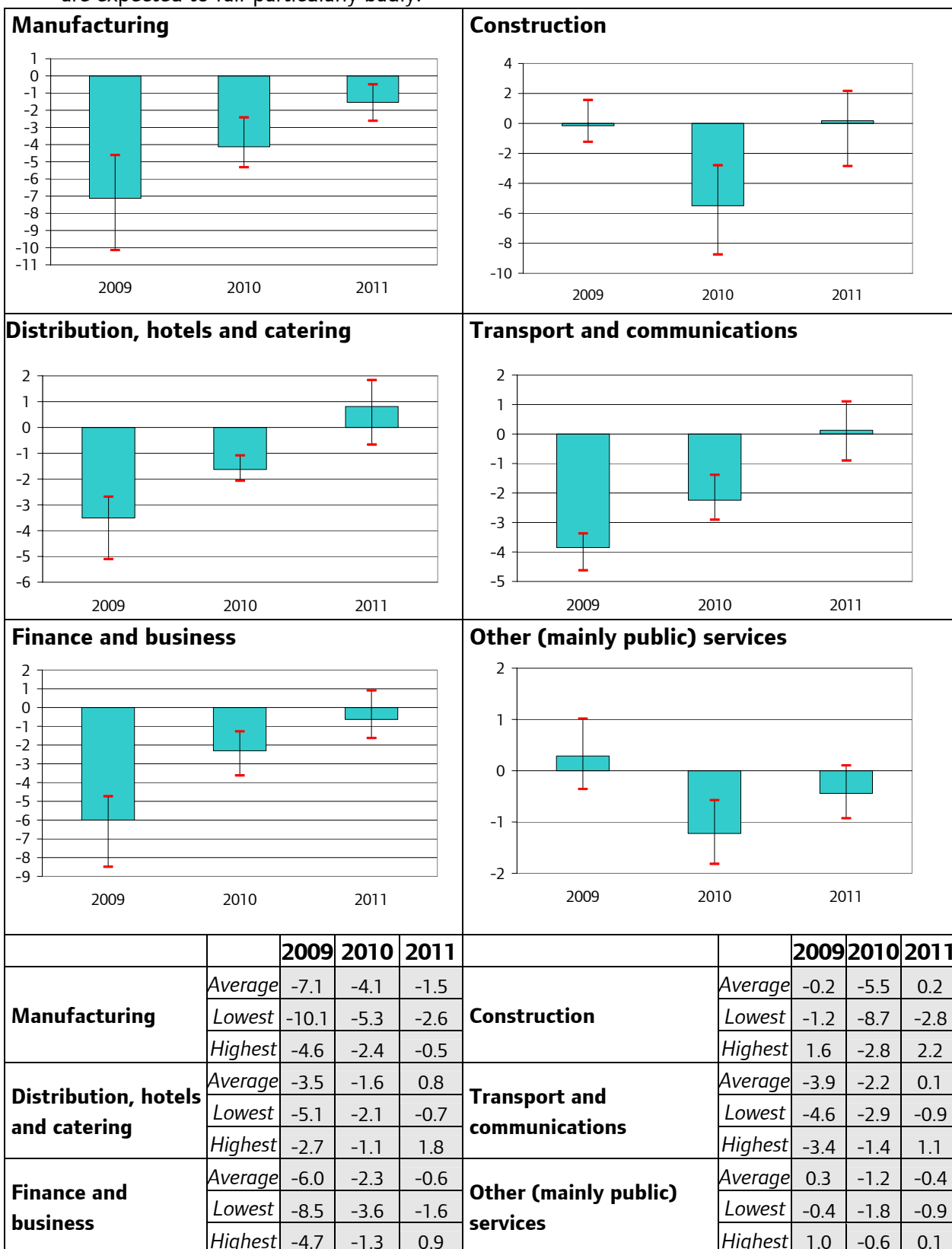
Output growth by sector (per cent annual change)

Almost all sectors are expected to have negative growth during 2009 before recovering somewhat in 2010 and 2011. The largest falls in growth in 2009 are expected in the construction and manufacturing sectors.



Employment growth by sector (per cent annual change)

Forecasted employment growth is negative for all sectors in 2009 apart from other (mainly public) services. The manufacturing and finance and business services sectors are expected to fair particularly badly.



5. The GLA Economics forecast

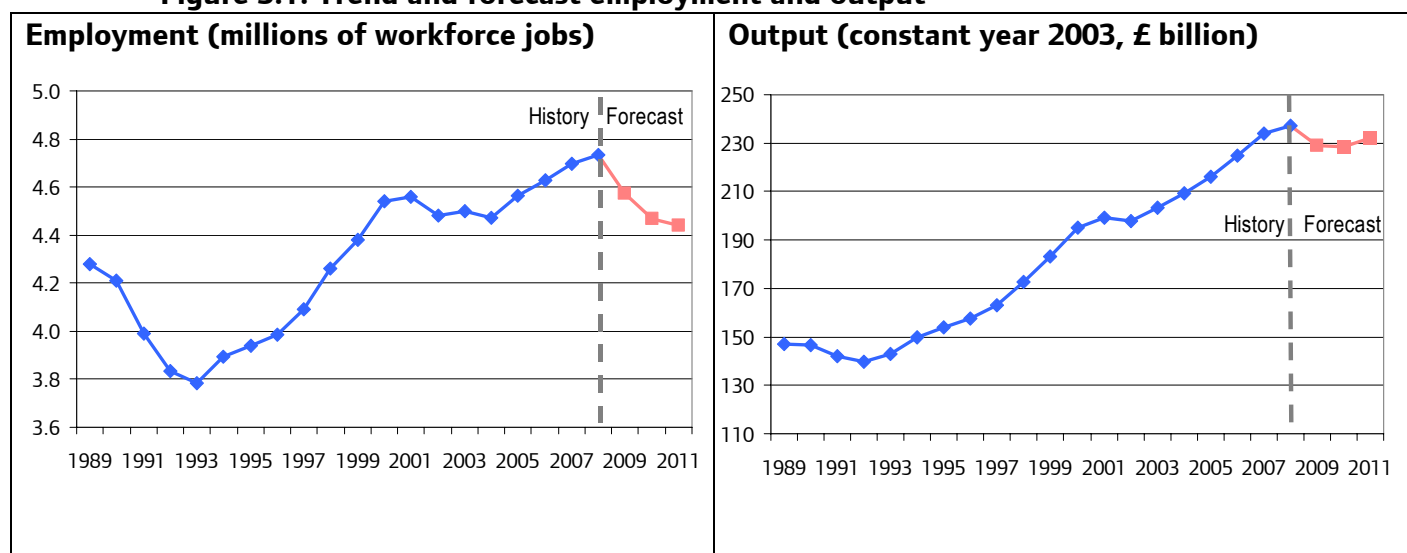
It is necessary to distinguish carefully between the GLA's long-term employment projections and this forecast, which contains the GLA's medium-term planning projections. Trend projections, by definition, do not incorporate cyclical variations. The actual course of output and employment will vary around this trend. Trend projections are essential for planning to provide capacity (such as office space, housing and transport) to accommodate the needs of the economy throughout and at the peak of the cycle, not just at its low points. For business planning (for example the likely course of revenue) estimates of actual numbers of jobs and actual output at any point in time are required. The medium-term planning projections provide these estimates. As time progresses and more data become available, it becomes possible to identify turning points in the data; whether underlying trends are continuing or new trends are being established. The source for all historic data in the following tables and charts is EBS.

5.1 Results

Following below trend growth in 2008 output is expected to fall in 2009 and 2010. Employment is forecast to fall in 2009, 2010 and 2011.

Household spending growth is expected to become negative in 2009 and 2010 before a slight recovery in 2011. Household income growth is expected to be negative in 2009 before recovering in 2010 and 2011.

Figure 5.1: Trend and forecast employment and output



Source: EBS for historic data and GLA Economics' calculations for forecast

Table 5.1: Forecast and historical growth rates

Annual % change

	2003	2004	2005	2006	2007	2008	2009	2010	2011
GVA	2.7	3.0	3.3	4.1	4.1	1.4	-3.5	-0.2	1.5
Workforce jobs	0.4	-0.6	2.0	1.4	1.5	0.7	-3.4	-2.3	-0.6
Household spending	0.0	1.4	3.4	1.3	4.4	2.8	-3.0	-1.9	0.5
Household income	3.2	1.0	3.1	1.6	0.1	3.1	-2.3	0.6	1.7

Table 5.2: Forecast and historical levels

(constant year 2003, £ billion except jobs)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
GVA	203.2	209.2	216.1	224.9	234.1	237.3	229.0	228.5	232.0
Workforce jobs (millions)	4.50	4.47	4.56	4.63	4.70	4.73	4.57	4.47	4.44
Household spending	99.5	100.9	104.3	105.7	110.3	113.3	109.9	107.8	108.4
Household income	115.7	116.9	120.5	122.4	122.5	126.3	123.4	124.1	126.2

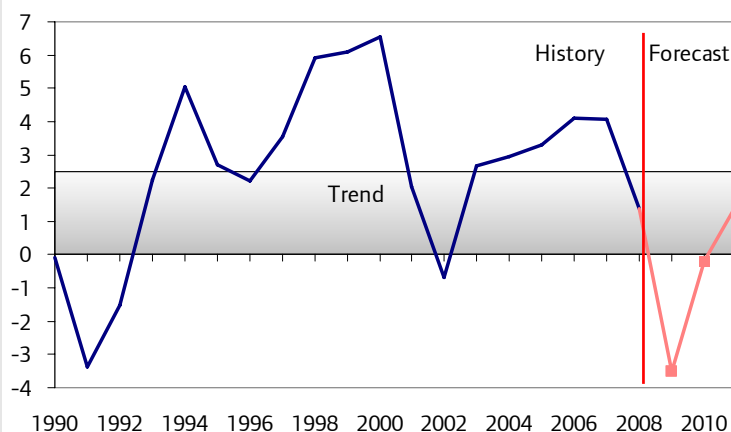
Output

(London GVA, constant year 2003, £ billion)

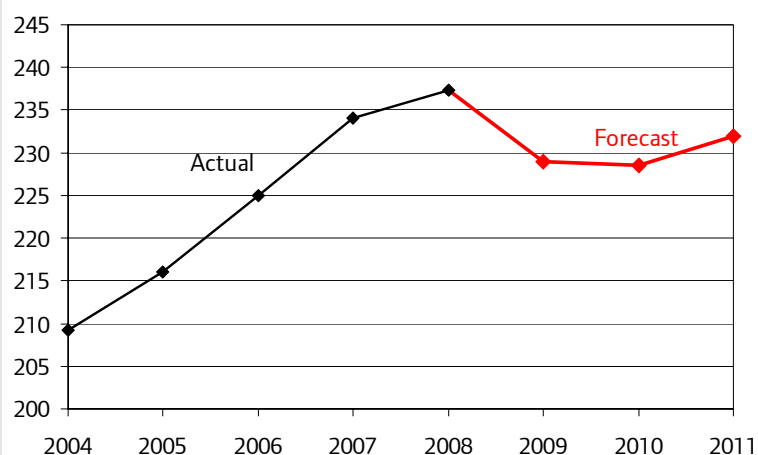
London's real GVA growth is forecast to be negative in 2009 and 2010. Forecast growth rates are -3.5 per cent in 2009, -0.2 per cent in 2010, and 1.5 per cent in 2011.

The GLA Economics' forecast is similar to the consensus average forecast throughout 2009-11.

Annual growth (per cent)



Level (constant year 2003, £ billion)



Growth (annual per cent)				
	2008	2009	2010	2011
GLA	1.4	-3.5	-0.2	1.5
Consensus		-3.6	-0.4	2.1

Level (constant year 2003, £ billion)				
	2008	2009	2010	2011
GLA	237	229	229	232
Consensus		229	228	233

History: Annual growth (per cent)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
-1.5	2.3	5.1	2.7	2.2	3.6	5.9	6.1	6.6	2.1	-0.7	2.7	3.0	3.3	4.1	4.1	1.4

History: Level (constant year 2003, £ billion)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
139.6	142.8	150.0	154.1	157.5	163.1	172.7	183.2	195.2	199.2	197.9	203.2	209.2	216.1	224.9	234.1	237.3

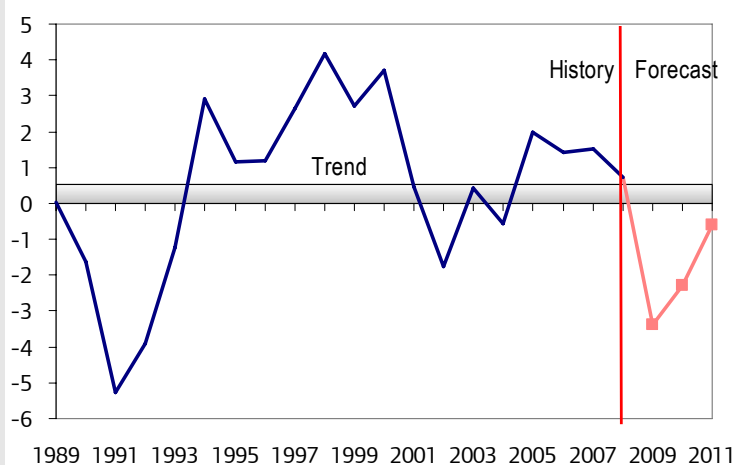
Employment

(London workforce jobs)

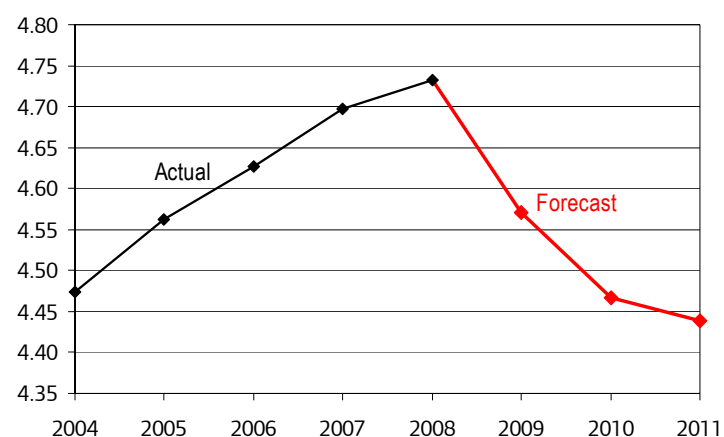
London's employment is forecast to fall in 2009, 2010 and 2011.

GLA Economics' forecast for employment growth is similar to the consensus average in 2009-2011.

Annual growth (per cent)



Level (millions of workforce jobs)



Growth (annual per cent)				
	2008	2009	2010	2011
GLA	0.7	-3.4	-2.3	-0.6
Consensus		-3.6	-2.1	-0.1

Level (millions of workforce jobs)				
	2008	2009	2010	2011
GLA	4.73	4.57	4.47	4.44
Consensus		4.56	4.47	4.46

History: Annual growth (per cent)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
-3.9	-1.2	2.9	1.2	1.2	2.7	4.2	2.7	3.7	0.4	-1.8	0.4	-0.6	2.0	1.4	1.5	0.7

History: Level (millions)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
3.83	3.78	3.89	3.94	3.99	4.09	4.26	4.38	4.54	4.56	4.48	4.50	4.47	4.56	4.63	4.70	4.73

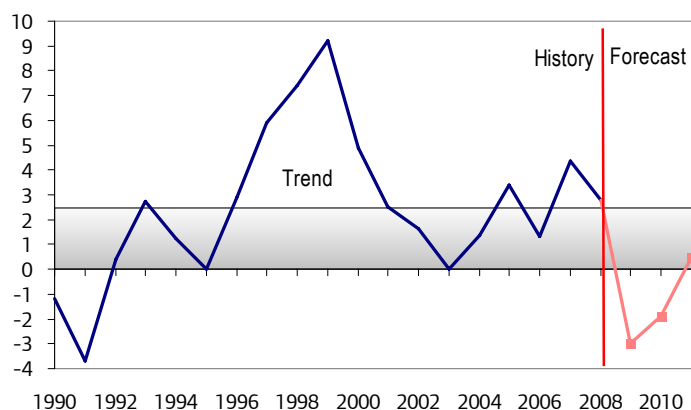
Household expenditure

(London household spending, constant year 2003, £ billion)

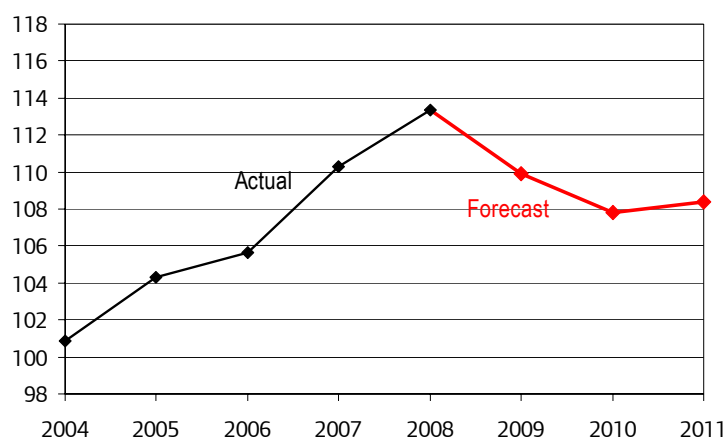
Growth in London's household spending is forecast to be negative in 2009 and 2010, before having a slight recovery in 2011.

This places GLA Economics' household spending growth forecast below the consensus average in 2010 and 2011.

Annual growth (per cent)



Level (constant year 2003, £ billion)



Growth (annual per cent)				
	2008	2009	2010	2011
GLA	2.8	-3.0	-1.9	0.5
Consensus		-3.5	-0.6	1.3

Level (constant year 2003, £ billion)				
	2008	2009	2010	2011
GLA	113	110	108	108
Consensus		109	109	110

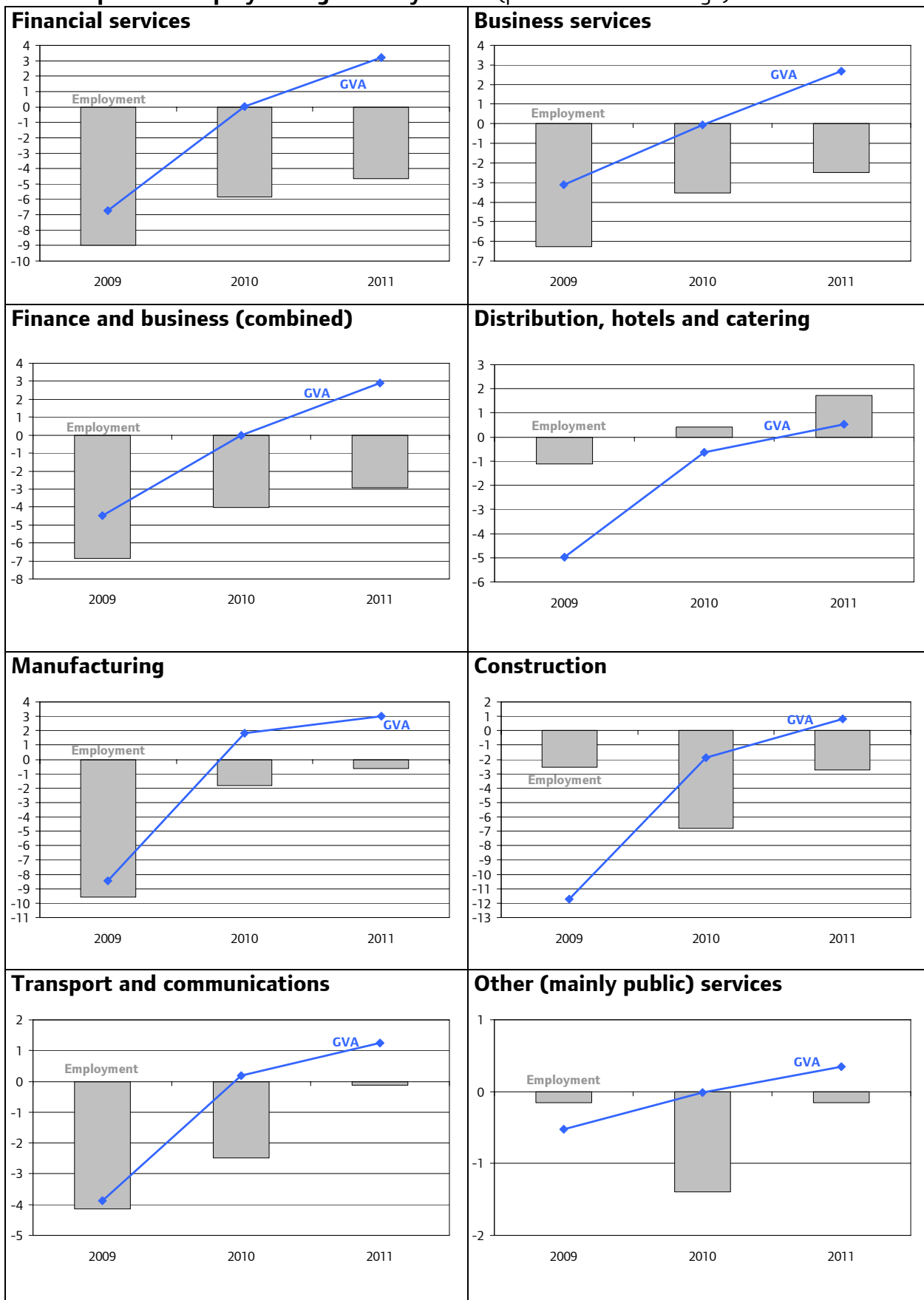
History: Annual growth (per cent)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
0.4	2.7	1.2	0.0	2.9	5.9	7.4	9.2	4.9	2.5	1.6	0.0	1.4	3.4	1.3	4.4	2.8

History: Level (constant year 2003, £ billion)

1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
68.5	70.4	71.3	71.3	73.3	77.7	83.4	91.1	95.5	97.9	99.5	99.5	100.9	104.3	105.7	110.3	113.3

Output and employment growth by sector (per cent annual change)



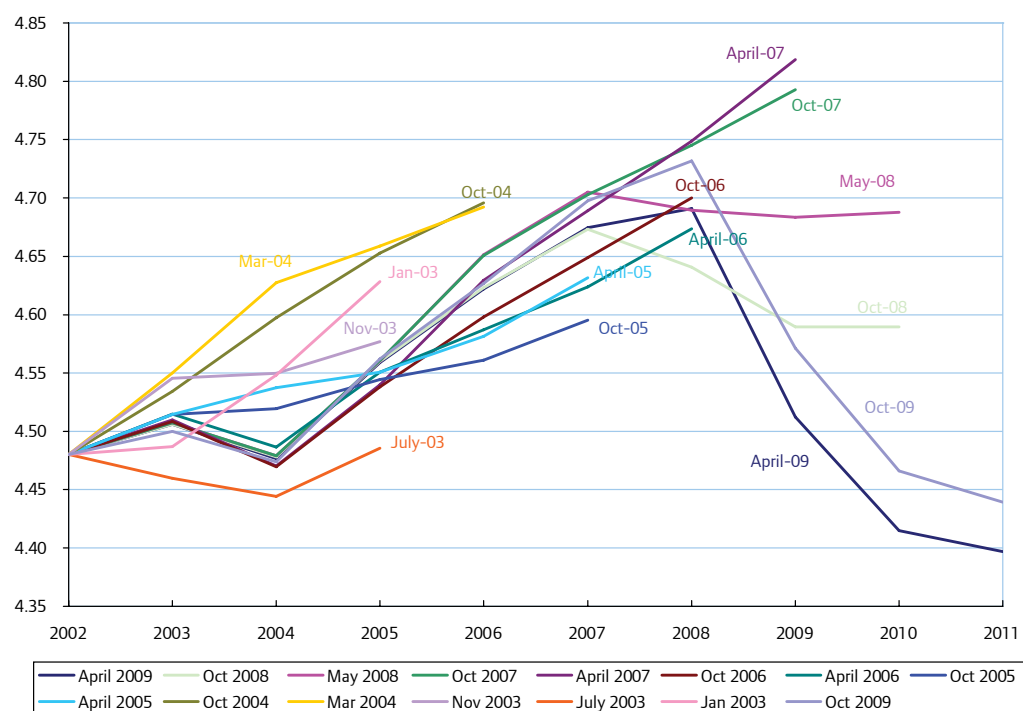
Output and employment growth by sector (per cent annual change)

	2009	2010	2011
Financial services			
Output	-6.7	0.0	3.2
Employment	-9.0	-5.8	-4.6
Business services			
Output	-3.1	-0.1	2.7
Employment	-6.3	-3.5	-2.5
Financial and business services combined			
Output	-4.5	0.0	2.9
Employment	-6.9	-4.0	-2.9
Distribution, hotels and catering			
Output	-5.0	-0.6	0.5
Employment	-1.1	0.4	1.7
Transport and communications			
Output	-3.9	0.2	1.2
Employment	-4.1	-2.5	-0.1
Other (mainly public) services			
Output	-0.5	0.0	0.3
Employment	-0.2	-1.4	-0.2
Manufacturing			
Output	-8.4	1.8	3.0
Employment	-9.6	-1.8	-0.6
Construction			
Output	-11.7	-1.9	0.8
Employment	-2.6	-6.8	-2.7
<i>(Memo: non-manufacturing)</i>			
Output	-3.3	-0.3	1.4
Employment	-3.1	-2.3	-0.6

5.2 Comparison with previous forecasts

This section compares the current forecast with previous forecasts in this series. Since the base years for the forecasts change and the base data is continuously revised, the forecasts have been rebased into a common base year for the comparison in Figures 5.2 and 5.3. The most recent forecast for London's workforce jobs growth and output growth is far lower than in previous forecasts apart from the April 2009 forecast.

Figure 5.2: Employment – latest forecast compared with previous forecasts
(millions of workforce jobs)

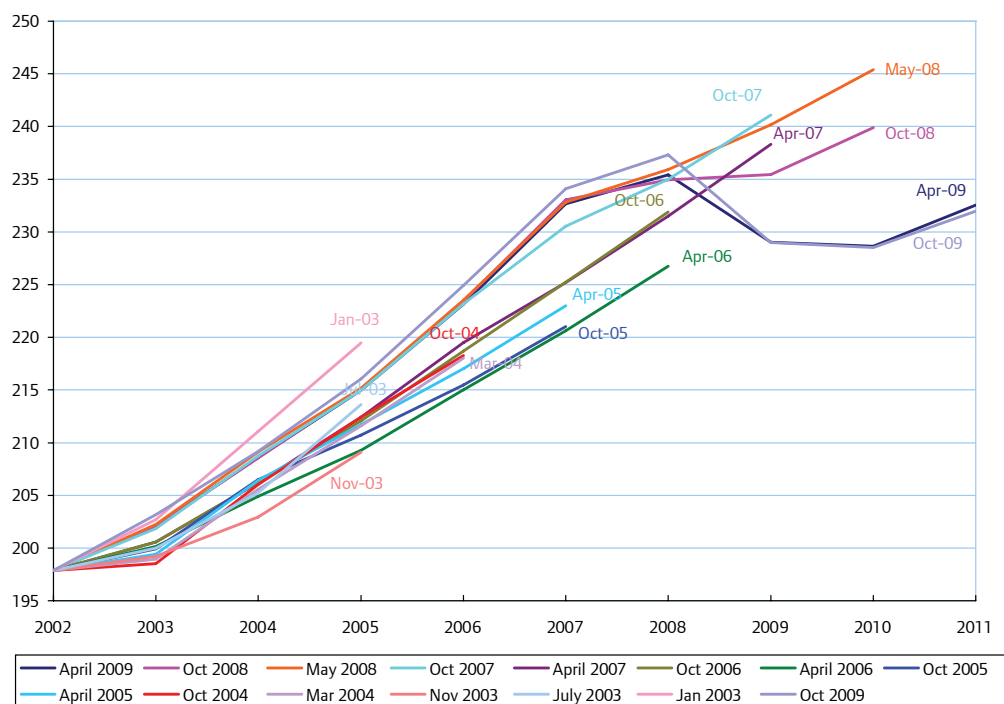


Source: Various London's Economic Outlooks

Table 5.3: Comparisons with previous published forecasts
(London workforce jobs, per cent annual growth)

Forecast	2003	2004	2005	2006	2007	2008	2009	2010	2011
Oct 2009	0.4%	-0.6%	2.0%	1.4%	1.5%	0.7%	-3.4%	-2.3%	-0.6%
April 2009							-3.8%	-2.2%	-0.4%
Oct 2008						-0.7%	-1.1%	0.0%	
May 2008						-0.3%	-0.1%	0.1%	
Oct 2007				1.3%	1.2%	0.9%	1.0%		
April 2007					1.2%	1.4%	1.5%		
Oct 2006				0.8%	1.1%	1.1%			
April 2006				0.6%	0.8%	1.1%			
Oct 2005			0.3%	0.7%	1.1%				
April 2005			1.4%	1.2%	0.9%				
Oct 2004		1.5%	0.1%	0.6%					
Mar 2004		1.7%	0.7%	0.9%					
Nov 2003	1.5%	-0.4%	0.9%						
July 2003	-0.5%	1.4%	1.8%						
Jan 2003	0.2%								

Figure 5.3: Output – latest forecast compared with previous forecasts
(constant year 2003, £ billion)



Source: Various London's Economic Outlooks

Table 5.4: Comparisons with previous published forecasts
(London GVA, per cent annual growth)

Forecast	2003	2004	2005	2006	2007	2008	2009	2010	2011
Oct 2009	2.7%	3.0%	3.3%	4.1%	4.1%	1.4%	-3.5%	-0.2%	1.5%
April 2009							-2.7%	-0.2%	1.7%
Oct 2008						0.8%	0.2%	1.9%	
May 2008						1.3%	1.8%	2.2%	
Oct 2007					3.3%	2.0%	2.6%		
April 2007					2.6%	2.8%	3.0%		
Oct 2006				3.1%	3.0%	3.0%			
April 2006				2.7%	2.6%	2.8%			
Oct 2005			2.0%	2.3%	2.6%				
April 2005			2.6%	2.5%	2.7%				
Oct 2004		3.8%	3.1%	2.7%					
Mar 2004		3.3%	2.9%	3.0%					
Nov 2003	0.7%	1.9%	3.0%						
July 2003	1.1%	2.6%	4.1%						
Jan 2003	2.4%	4.1%	4.0%						

Appendix A: Explanation of terms and some sources

Definitions, differences, and revisions

Forecasting organisations use varying definitions of the regional indicators they supply. It is therefore not always possible to assign a completely consistent meaning to the terms used.

Throughout this report, as far as is compatible with the individual definitions applied by the forecasters, 'employment' refers to 'workforce employment' as defined in, *Labour Market Trends. London's Economic Outlook: December 2003* and *The GLA's London Workforce Employment Series* provides a more detailed explanation of this term.

Forecasters' definitions are broadly compatible with this but in some cases differences arise from the treatment of small items such as participants in government training schemes or the armed forces. The GLA uses civilian workforce employment throughout.

Output refers to GVA, a term introduced by the 1995 revision of the European System of Accounts (ESA95). Some forecasters still estimate GDP, which differs slightly from GVA. Imputed rental income from the ownership of property is included in some cases but not in others. GLA Economics' *London's Economic Outlook: December 2003* provides a more detailed explanation of this term.

Estimates of nominal regional GVA are available up to 2008 from the ONS. No official estimates of real regional GVA are available because of the difficulties in producing authoritative regional price deflators, although the ONS has produced regional price indexes for the year 2004^{xii}. Most regional forecasters supply their own estimates of London's real GVA. The real London GVA figures used in this GLA Economics' forecast are supplied by EBS.

GVA estimates are less reliable than employment estimates because there is no independent source of information from which to judge the size of total sales by London-based agents. ONS estimates are calculated by the factor incomes method, beginning from wages paid to people with workforce jobs located in London. Profits are imputed on the basis of these earnings estimates from knowledge of national sectors of employment. Most regional forecasters adopt a variant of this technique.

Consumption refers to private consumption, otherwise known as household expenditure; in some cases the expenditure of non-profit organisations is included and in other cases it is not.

Appendix B: Glossary of acronyms

ABI	Annual Business Inquiry
bn	Billion
BRC	British Retail Consortium
CE	Cambridge Econometrics
CEBR	The Centre for Economic and Business Research
CPI	Consumer Price Index
DCLG	Department for Communities and Local Government
EBS	Experian Business Strategies
ECB	European Central Bank
EERI	Effective Exchange Rate Index
EU	European Union
FSA	Financial Services Authority
FT	Financial Times
GDP	Gross Domestic Product
GLA	Greater London Authority
GVA	Gross Value Added
HM Treasury	Her Majesty's Treasury
IFS	The Institute for Fiscal Studies
ILO	International Labour Organisation
IMF	International Monetary Fund
LEO	London's Economic Outlook
LFS	Labour Force Survey
LHS	Left Hand Scale
mn	Million
MPC	Monetary Policy Committee
OE	Oxford Economics
OECD	Organisation for Economic Co-operation and Development
ONS	Office for National Statistics
OPEC	Organisation of Petroleum Exporting Countries
PMI	Purchasing Managers' Index
Q2	Second Quarter
QE	Quantitative Easing
RHS	Right Hand Scale
RPIX	Retail Price Index (excluding mortgage interest payments)
RPI	Retail Price Index
TfL	Transport for London

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Footnotes

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- ⁱ The forecast is based on an in-house model built by Volterra Consulting Limited.
- ⁱⁱ RPI = Retail price index. Although not part of the GLA Economics forecast for London, for reader information HM Treasury Consensus Forecast, August 2009 of the RPI UK inflation rate are reported.
- ⁱⁱⁱ CPI = Consumer Price Index. Although not part of the GLA Economics forecast for London, for reader information HM Treasury Consensus Forecast, August 2009 of the UK CPI inflation rate are reported. Since December 2003 the Bank of England's symmetrical inflation target has been annual CPI inflation at two per cent.
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- ^v The Wall Street Journal, 'U.K. New Mortgage Lending Slows Further', 25 August 2009.
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- ^{vii} BBC, 'Q&A: What is a recession?', 8 July 2008.
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- ^{ix} Bank of England, 'Inflation Report', August 2009.
- ^x The Institute for Fiscal Studies, 'Public finance bulletin: September 2009', September 2009.
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- ^{xiii} The IMF, 'World Economic Outlook: Sustaining the Recovery', October 2009.
- ^{xiv} The Sterling Effective Exchange Rate Index measures the overall change in the trade-weighted exchange value of sterling. It is designed to measure changes in the price competitiveness of traded goods and services and so the weights reflect trade flows in goods and services.
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- ^{xli} Fenwick D and Wingfield D, 2005, Relative Regional Consumer Price Levels in 2004, Economic Trends No. 615, ONS, February 2005.

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Greek

Αν θέλετε να αποκτήσετε αντίγραφο του παρόντος εγγράφου στη δική σας γλώσσα, παρακαλείστε να επικοινωνήσετε τηλεφωνικά στον αριθμό αυτό ή ταχυδρομικά στην παρακάτω διεύθυνση.

Turkish

Bu belgenin kendi dilinizde hazırlanmış bir nüshasını edinmek için, lütfen aşağıdaki telefon numarasını arayınız veya adrese başvurunuz.

Punjabi

ਜੇ ਤੁਹਾਨੂੰ ਇਸ ਦਸਤਾਵੇਜ਼ ਦੀ ਕਾਪੀ ਤੁਹਾਡੀ ਆਪਣੀ ਭਾਸ਼ਾ ਵਿਚ ਚਾਹੀਦੀ ਹੈ, ਤਾਂ ਹੇਠ ਲਿਖੇ ਨੰਬਰ 'ਤੇ ਫ਼ੋਨ ਕਰੋ ਜਾਂ ਹੇਠ ਲਿਖੇ ਪਤੇ 'ਤੇ ਰਾਬਤਾ ਕਰੋ:

Hindi

यदि आप इस दस्तावेज की प्रति अपनी भाषा में चाहते हैं, तो कृपया निम्नलिखित नंबर पर फोन करें अथवा नीचे दिये गये पते पर संपर्क करें

Bengali

আপনি যদি আপনার ভাষায় এই দলিলের প্রতিলিপি (কপি) চান, তা হলে নীচের ফোন নম্বরে বা ঠিকানায় অনুগ্রহ করে যোগাযোগ করুন।

Urdu

اگر آپ اس دستاویز کی نقل اپنی زبان میں چاہتے ہیں، تو براہ کرم نیچے دئے گئے نمبر پر فون کریں یا دیئے گئے پتے پر رابطہ کریں

Arabic

إذا أردت نسخة من هذه الوثيقة بلغتك، يرجى الاتصال برقم الهاتف أو مراسلة العنوان أدناه

Gujarati

જો તમને આ દસ્તાવેજની નકલ તમારી ભાષામાં જોઈતી હોય તો, કૃપા કરી આપેલ નંબર ઉપર ફોન કરો અથવા નીચેના સરનામે સંપર્ક સાધો.