Ernst & Young

Review of Transport for London's Assessment of the Business and Economic Impacts of the Congestion Charge in Chapter 6 of "Impacts Monitoring – Third Annual Report 2005".

Final Report

10th February 2006

This report is intended solely for the use of Transport for London and the Greater London Authority. In carrying out our work and preparing our report, we have worked solely on the instructions of Transport for London and the Greater London Authority and for Transport for London's and the Greater London Authority's purposes. Our report may not have considered issues relevant to any third parties, any use such third parties may choose to make of our report is entirely at their own risk and we shall have no responsibility whatsoever in relation to any such use.

Contents

Summary of Findings

1. Summary of Findings Report

Introduction

1.1. Congestion charging was introduced into Central London in February 2003, and was intended to contribute to four of the Mayor of London's transport priorities: to reduce congestion; to make radical improvements in bus services; to improve journey reliability for car users; and to make the distribution of goods and services more efficient.

1.2. Transport for London (TfL) has produced annual reports monitoring the impact of the congestion charge (the third report was published in April 2005). These reports measure reductions in congestion, but also consider the social, economic, and environmental impacts of the congestion charge

1.3. The evidence presented by TfL suggests that the charge has been successful in meeting its key objective; that of reducing traffic volumes and therefore congestion.

1.4. Prior to the introduction of the charge concerns were raised by the business community about the impact on London's economy. The monitoring reports assess what effect the charge has had on the economy. The Greater London Authority (GLA) economics unit conducted the latest assessment for TfL, and concluded that "congestion charging has had a broadly neutral impact on overall business performance in the charging zone"[1]. Despite this conclusion concerns continue to be expressed especially in the context of the potential West London expansion.

1.5. Recognising these potential concerns, TfL's internal audit group commissioned Ernst & Young LLP ("Ernst & Young") to undertake a review of the assessment conducted by the GLA Economics unit in order to confirm that the conclusions on the economic impact of the charge are objective and robust. This report presents the results of the review of the analysis of Chapter 6 of "Impacts Monitoring – Third Annual Report April 2005", referred to in this document as the "third monitoring report". This Report should be read in conjunction with the supporting Appendices which provide additional background to the conclusions presented in this Report.

Our Approach

1.6. Our approach to this study is to review the reasonableness of the approach used by TfL including: the quality and appropriateness of the data used; any gaps in the analysis; and the technical analysis of the way in which the data has been analysed. We have sought to ensure that the conclusions reached by TfL are consistent with the evidence presented.

1.7. We have reviewed both the overall framework that is used to guide the analysis, and the specific analysis that has been used to test and populate the framework.

1.8. This review has been conducted in a relatively short timeframe. Furthermore, as the congestion charge has only been in place for two years, the delay in the production of economic statistics limits how definitive any conclusions can be. Nevertheless, we have been able to form a clear view on the approach and conclusions of TfL.

Conclusions

1.9. TfL in its assessment of the economic and business impacts of the charge concludes that:

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[1] Impacts monitoring Third Annual Report April 2005 – section 6.2, 2nd bullet point

Summary of Findings

"The balance of evidence again leads to the conclusion that the scheme had a broadly neutral impact on London's economy."

1.10. Having reviewed the underlying data and the methodology employed by TfL, Ernst & Young believes that this conclusion is reasonable and that there is no evidence of attempts to draw conclusions that are not supported by the data. The economic area directly impacted by the congestion charge is dominated by financial and business services and these sectors appear to have been less directly affected by the charge than other sectors thereby limiting the potential for any negative effects. There is also some evidence of benefits to businesses from the charge and these benefits may go some way to offsetting any potential negative effects of the charge on some of the smaller economic sectors within the charging zone. Considered overall therefore, the impact of the scheme does appear to be broadly neutral based on the available data.

1.11. However, we believe that an expansion of the conclusions to include an additional discussion of the findings in two areas would provide useful additional context in which to assimilate the overall findings. These two areas are:

- The findings of some small negative impact in certain sectors; and
- The findings on the Retail sector as there are several sources of data on the impact on this sector that are spread throughout the report.

We discuss these two points in more detail below.

1.12. There is some limited evidence of a possible small negative impact in certain sectors. While the affected areas only account for small proportion of the central London economy and the data is often difficult to use to develop definitive conclusions, we believe they should be mentioned in TfL's analysis to avoid any accusations of failure to consider all the potential impacts. For balance however, we also highlight areas where there may be an offsetting, small positive impact. The key findings are:

Assessment of business change

- The Beta Model data shows that the number of enterprises in the CCZ declined in absolute terms in 2003 while increasing elsewhere, although this was a continuation of an existing trend. There is also some evidence of structural changes, in particular a decline in the proportion of enterprises with less than 5 employees in the central zone, and this may have been caused by the charge.
- However, there was a corresponding increase in employment in larger firms and, in addition, data from the ABI shows a stronger employment performance in the CCZ (albeit still an absolute decline) than other parts of London.

Case study evidence

- The case study evidence highlights some of the micro impacts of the congestion charge. In particular it highlights the cost to workers who operate outside the standard hours of business. It may have long term implications for "out of hours" economic activity, cause problems in retaining and recruiting staff, and put pressure on wages.
- However, the case study evidence also suggests that for some sectors where initially concerns had been raised, such as in the NHS, the expected negative impacts did not arise and there is a general acceptance of benefits.

Summary of Findings

1.13. The potential impact on the Retail sector of the congestion charge has probably been the most widely debated issue since the idea of the charge was announced. The TfL analysis looks for evidence of potential impacts on the Retail sector via a number of sources and we believe it would be helpful to summarise the overall effect. The key sources are:

Assessment of Business Change

- The Dun & Bradstreet data shows that profitability growth in the Retail and Hotels & Restaurants sectors in the CCZ was negative and worse than in the rest of inner and outer London. However, as performance of the Retail sector in the CCZ was better than in the western zone, it is not possible to conclude that the congestion charge impacted Retail performance.

Recent retail trends

- There is evidence of a drop in retail sales growth and reduced foot fall in 2003.However as this effect began before the charge was introduced and was more marked at weekends, it is not possible to identify any adverse impact from the congestion charge rather it appears that other exogenous effects were the main driver of the changes.

Property prices

- The available evidence suggests that retail rental values did fall in the CCZ relative to the rest of inner London, and this may have been an impact of the charge. However, there are other factors to consider such as the war in Iraq.

TfL Survey

- The TfL survey did find qualitative evidence of a decline in Retail sales and an increase in costs that were attributed to the congestion charge. Even allowing for the potential bias in qualitative research of this type, there is evidence of a belief that the charge led to an adverse impact on the Retail sector.

Econometric Tests

- The studies suggest that there is evidence of a negative impact on John Lewis, but the analysis of the London Retail sector as a whole does not provide definitive evidence of a broader negative impact of the charge on the Retail sector. As the London study looks at an area beyond the CCZ area we can only draw indicative conclusions from it.

1.14. Our overall conclusion is that it is not possible to conclude that the Congestion Charge has had an adverse impact on the Retail sector. The evidence is mixed.

- The TfL survey is the main source indicating a negative effect but this is a qualitative survey of an emotive topic so must be treated with some caution;
- There is econometric evidence of an impact on John Lewis but no definitive evidence of an effect on the broader Sector;
- As we cannot separate the impact of the charge from the impact of other factors affecting the market at the time, it is not possible to conclude that the charge rather than other exogenous effects was the driver of the fall in CCZ property prices relative to the rest of London;

Summary of Findings

- In the case of Retail trends, the evidence suggests that factors other than the charge were the drivers of the change in footfall and Retail performance; and
- The Dun & Bradstreet data suggests that changes in Retail performance were influenced by factors not specific to the CCZ.

1.15. There are therefore more observations on the Retail sector than on other sectors. We believe that there has been a real attempt to identify any adverse effects but at this time it is not possible to conclude definitively that there has been an adverse effect.

1.16. The overall conclusions are based on the data available at the time. Data availability was a limiting factor in the analysis and TfL worked hard to make the best possible use of the available data. There are two main limitations to the data that must be taken into account when considering the robustness of the conclusions. The two key limitations are discussed below

a) Time frame

1.17. The charge has only been in operation for just over two years and so any observable impacts may be merely transitional, while the full effect on the economy will only become apparent over an entire economic cycle. It is therefore difficult to draw a definitive conclusion on the impact of the charge.

b) Prevalence of other factors

1.18. The charge was introduced when a number of exogenous factors were affecting economic performance such as macroeconomic conditions, the Iraq war and the central line closure.

1.19. The prevalence of other exogenous economic shocks at the same time as the introduction of the charge makes it difficult to isolate any specific impact of the charge.

Future Improvements

1.20. We believe that TfL should consider actions in two areas to improve the analysis in future years. There are areas where any formal analysis of the impact of a policy change should be accompanied by a detailed framework defining the method of assessment, the expected impacts, and the relevant data sources. We do not consider the framework outlined by TfL in the third monitoring report to be sufficient to inform the detailed analysis that is required. The framework that was provided in earlier versions of the report, and which we understand informs the 2005 Report, is an appropriate framework and it would be sensible to reintroduce this into the reviews in future years.

1.21. In addition, TfL published a consultation on the extension of the congestion charge into West London. It may be that the economic framework used in this document could be adopted as part of the annual monitoring reports to provide a clearer framework against which to judge the impact of the charge.

1.22. While we recognise TfL's resource and time constraints in preparing the analysis, the following could usefully be analysed in future years as more data becomes available:

- **Direct costs** – the charge raised £190m in revenue in 2004, a direct cost to London drivers. However, this is effectively a redistribution or transfer from the private to the public sector rather than a net cost.
- **Economic benefits** – TfL does not explore the economic benefits of the scheme.

Summary of Findings

- **Case studies –** TfL could usefully analyse a multi-site retailer, sectors with irregular working hours, and transport related sectors such as petrol retailers or mini-cab firms.
- **Financial & Business services** – this is the largest sector in terms of employment in the CCZ and we would therefore expect TfL to investigate the impact on this sector.

Summary

1.23. Ernst & Young therefore believes that the analysis underpinning and the conclusions drawn from TfL's assessment are reasonable and that TfL has sought to use the available data in an objective manner. Our review has confirmed that that making definitive conclusions is difficult given time-frame limitations and the exogenous shocks to the economy that occurred at the same time as the Congestion Charge was introduced.

1.24. We believe that some costs, albeit small, were not fully recognised but as the benefits of reduced congestion to the economy were one of the key supporting arguments in favour of the charge, and no credit for this is included in the assessment, TfL's overall conclusions are reasonable. We do recommend that the quantification of benefits needs to be explored further to give a complete picture of the impacts of the charge on London's economy and possibly to demonstrate that overall the charge could have generated net economic benefits even when all costs are taken into account.