

# London's Economy Today



Issue 33 | May 2005

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## UK economy continues to slow

by Christopher Lewis

**London's economy is very successful and attractive to businesses. However, this success also brings challenges in terms of congestion and higher costs. The first joint Confederation of Business Industry (CBI) and KPMG London Business Survey (April 2005) found that transport was the most inhibiting factor for business - taxation ranked sixth - while almost 90 per cent of respondents said that the cost of living was considerably higher in London compared to other major capital cities.**

This month's supplement, which is in three parts, covers some of these issues by providing an overview of the GLA's input into the Lyons Inquiry, a summary of the latest findings on congestion charging and the scheme's impact on the retail sector, and GLA Economics' work concerning a living wage.

### London's tourism industry doing well

London's economy remains healthy and the capital's tourism industry is expected to experience a record year in 2005 after an increase in its share of worldwide tourism in 2004. The improvement in London's tourism industry is due to more overseas visitors rather than an increase in domestic tourists. Overall, employment prospects in the City of London are reasonable with City-type job vacancies in March at twice the level of the previous year. Research by recruitment consultancy Morgan

GLAECONOMICS

## Latest news...

### Secure your place at the following GLA Economics' events:

- Growing Together – explores the relationship between the London and the UK economy (Monday 6 June)
- The environmental effectiveness of London – compares London to other English regions (Wednesday 15 June)
- Employment projections for London (Monday 27 June)

### Get your copy of GLA Economics' latest reports:

- London's Economic Outlook: Spring 2005 - The GLA's medium-term planning projections
- Current Issue Note 4 – Interim borough level employment projections to 2016
- Working Paper 12: The congestions charge's impact on retail - The London experience

**For more information: 020 7983 4922 or [glaeconomics@london.gov.uk](mailto:glaeconomics@london.gov.uk). Reports can be downloaded from [www.london.gov.uk/mayor/economic\\_unit](http://www.london.gov.uk/mayor/economic_unit).**

McKinley suggests that hiring in the City of London is expected to pick up during the rest of the year, especially in operations and risk management. In April, the Purchasing Managers' Index (PMI) measures of seasonally adjusted business activity and new orders in London both fell but remain strong at 58.7 and 58.4 (this is significantly above 50, which is the level consistent with no change on the previous month). The average annual rate of growth in tube passenger numbers is still positive while the average annual rate of growth in bus passenger numbers, though declining is just above five per cent.

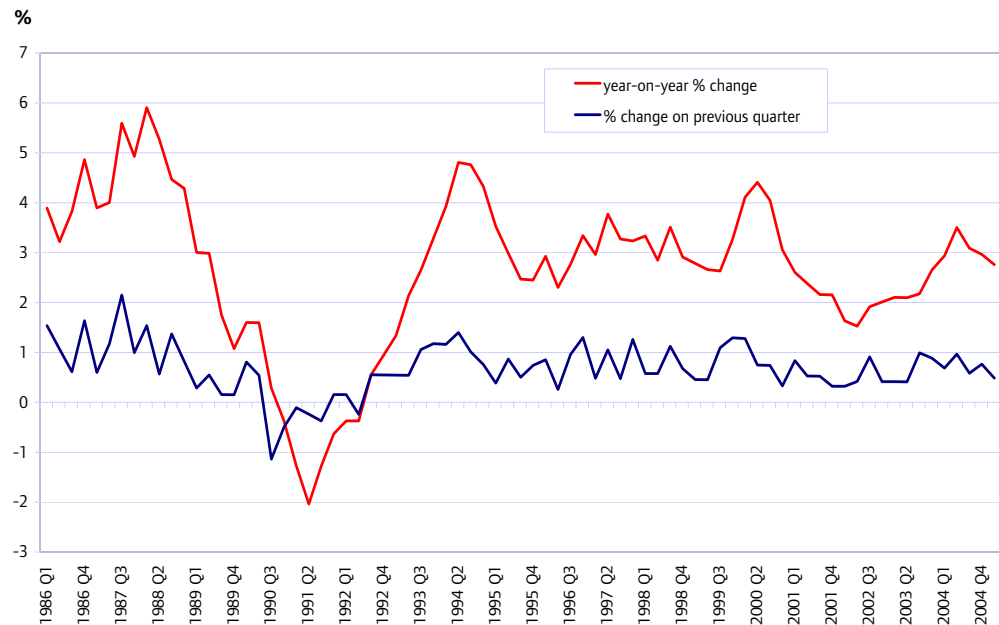
**'Good news for the London economy'**

### UK growth hit by falling manufacturing output

The UK economy slowed in the first quarter (Q1) of 2005 to quarterly growth of 0.5 per cent compared with 0.7 per cent in Q4 2004 (see Figure 1). This is the slowest quarterly growth rate since Q2 2003. Manufacturing output and total industrial production both actually fell by 0.7% in Q1. In March, manufacturing output fell by 1.6 per cent and there is now a negative two per cent trend rate for annual manufacturing growth. UK manufacturing investment also fell in Q1 by 1.5 per cent, which caused overall business investment to weaken by 0.1 per cent compared with Q4 2004. However, output growth in the service sector continues at a healthy pace (0.8 per cent in Q1) with growth strongest in the business services and finance sector at a robust 1.3 per cent in Q1. This is good news for the London economy in which the business services and financial sector is a strong driving force.

**Figure 1: UK GDP growth**

Source: Office for National Statistics



During April, credit cardholders paid more off their credit cards than they spent (by £40 million) for the first time since May 1994. This is having a negative impact on high street retailers who are reporting poor financial results. A healthy consumer sector is important for the UK and London economies so it is key that current consumer weakness does not turn into a collapse. Low household expenditure growth meant that despite UK consumer price inflation increasing to its highest level for nearly seven years in March at 1.9 per cent (where it remained in April), it was unsurprising that the Bank of England kept interest rates on hold again in May and looks likely to continue to do so for the next few months at the very least. With manufacturing output price inflation increasing but consumer spending on goods slackening and annual house price growth cooling, the direction and timing of the next move in interest rates is unclear.

### US interest rates continue to rise as retail sales strengthen

US retail sales increased by a higher than expected 1.4 per cent in April. The February and March data has also been revised upwards so, buoyed by the strong housing market, there seems to have been a rebound in US consumer spending. The Federal Reserve raised US interest rates by a further quarter of a percentage point to three per cent on 3 May. With US job growth quickening and inflationary pressures still around, the Federal Reserve is likely to continue to increase interest rates at a measured pace throughout 2005. Current oil prices are increasing inflationary pressures throughout the world economy and not just in the US. However, there have been a few signs over the last month of a better balance in the oil market with prices falling to around \$50 per barrel.

### Eurozone to remain weak in 2005

The eurozone economies are not expected to grow strongly this year with the Organisation for Economic Co-operation and Development (OECD) cutting its growth forecast to only 1.2 per cent from 1.9 per cent. The French unemployment rate rose to its highest level for over five years in March to 10.2 per cent and the European Central Bank (ECB) has called Germany and Italy persistently underperforming countries. The role of the ECB in the weakness of the eurozone economies has been criticised by the OECD who have called for an early easing of monetary policy. However, the ECB seem very unlikely to take this advice and lower interest rates. The German economy's over reliance on export growth remains with domestic demand continuing to show little sign of life. In May, German business confidence fell for the fourth consecutive month to its lowest level since August 2003 and investor confidence fell to its lowest level for six months. Italian business confidence is at its lowest since November 2001 and in Q1 Italy actually slipped into recession' as the economy shrank by a further 0.5 per cent. After a mild recession during 2004 the Japanese economy grew by 1.3 per cent in Q1 2005, but its recovery remains fragile and is certainly not expected to continue at this pace. The OECD's latest report in May forecasts that Japanese growth in 2005 will only be 1.5 per cent.

### **Steady economic prospects for London**

Most recent indicators suggest that London's growth remains slightly above that of the rest of the UK with the business services and finance sector performing robustly. For example, in the latest office demand survey, City of London agents predict further growth in deals for offices in most sectors in Q2. The outlook for the number of enquiries is also positive, although expectations are not as strong as they were at the beginning of the year. Despite predicting that the London economy will slow down during the first nine months of this year, the Bank of Scotland expects that London's growth will remain above trend throughout 2005. In a global context, European economies remain weak and the UK economy has slowed down since the end of 2004 as manufacturing output has fallen. However, the world economy is still being supported for now by a buoyant US and China.

# Economic indicators

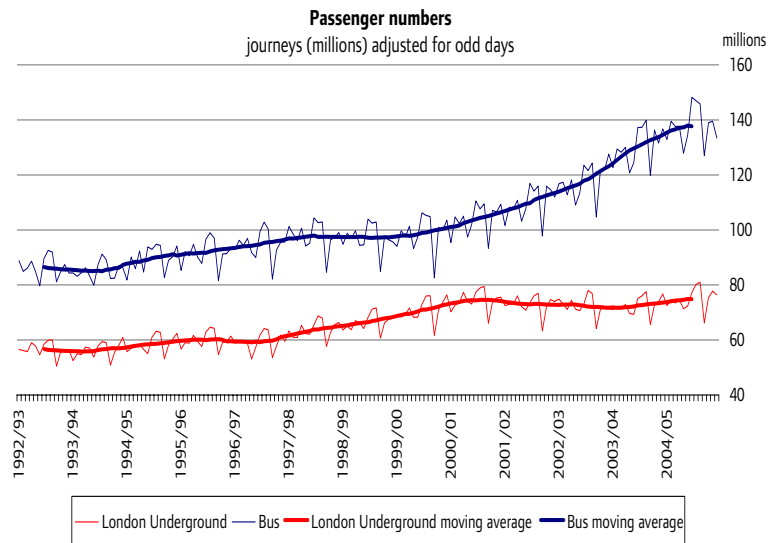
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## Moving average of Underground passenger numbers reaches new high

- In the most recent 28-day period, London's public transport had 209.8 million passenger journeys; 133.4 million by bus and 76.4 million by Underground.
- The moving average shows a small decrease to 212.5 million passengers every period. The average for buses decreased to 137.7 million passenger journeys. The average for the Underground was 74.8 million, above levels in 2000.

Latest release: May 2005

Next release: June 2005



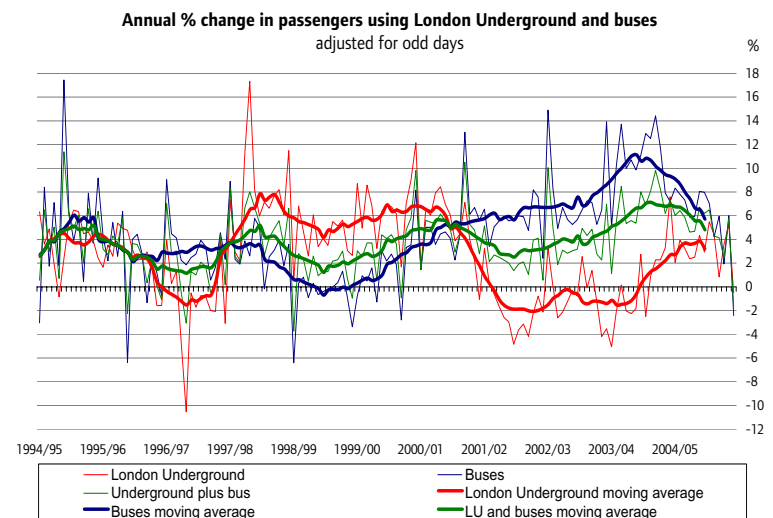
Source: Transport for London

## Slowdown in passenger journeys' annual growth

- The average annual rate of growth in passenger journeys is 4.5%, below the annual growth in the previous period of 5.5%.
- The average annual rate of growth in bus journey numbers has slowed and is now at 5.3%.
- The average annual rate of growth in Underground passenger journey numbers slowed to 3%, down from 3.8%.

Latest release: May 2005

Next release: June 2005



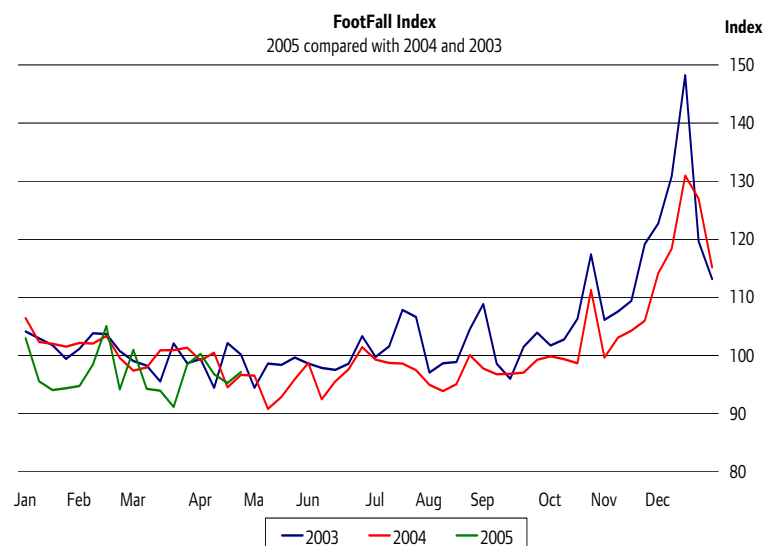
Source: Transport for London

## Shopping numbers recover a little in April

- The FootFall Index of shoppers in London recovered in April from its levels in mid-March.
- The level of the index in April is similar to the same time last year, but is now below that of 2003.
- The FootFall index measures the number of shoppers but does not necessarily reflect the level of spending.

Latest release: 25/04/05

Next release: every week



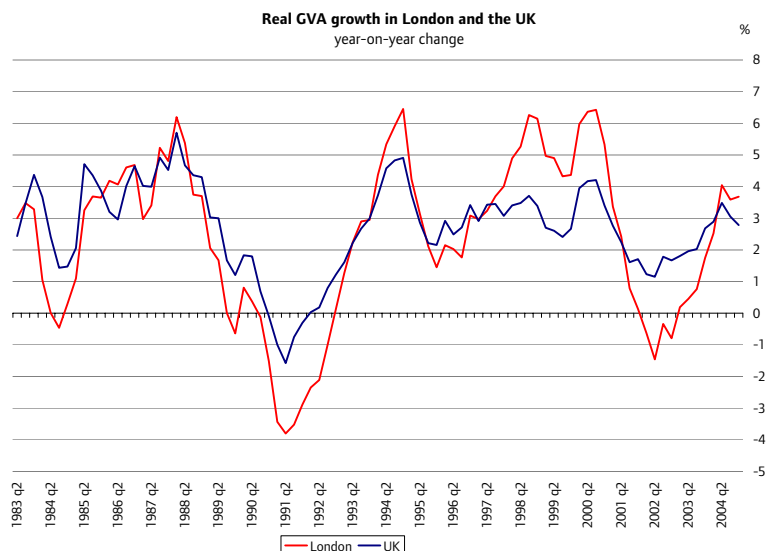
Source: FootFall Limited

## London's economy growing faster than the UK's

- London's annual growth in output was 3.7% in Q4 2004, up slightly from 3.6% in Q3. This continued 2004's robust growth.
- The UK's annual growth in output was 2.8% in Q4 2004 down from 3.1% in Q3.
- London's output growth remained higher than that for the whole of the UK.

Latest release: May 2005

Next release: August 2005



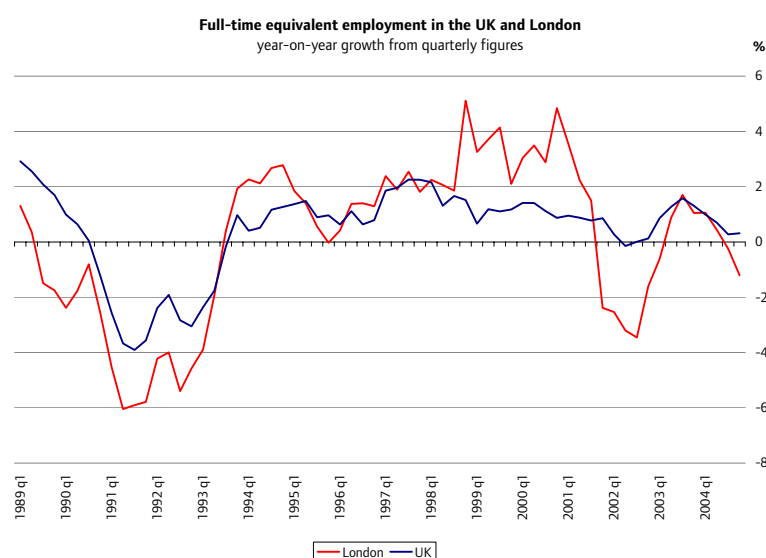
Source: Experian Business Strategies

## Employment change in London weaker than for the UK

- London's year-on-year employment growth was -1.2% in Q4 2004 compared to -0.2% in Q3 2004.
- Annual employment growth in the UK as a whole remained stable at 0.3% in Q4 2004.
- Despite higher annual output growth, London's employment growth is lower than that for the whole of the UK.

Latest release: May 2005

Next release: August 2005



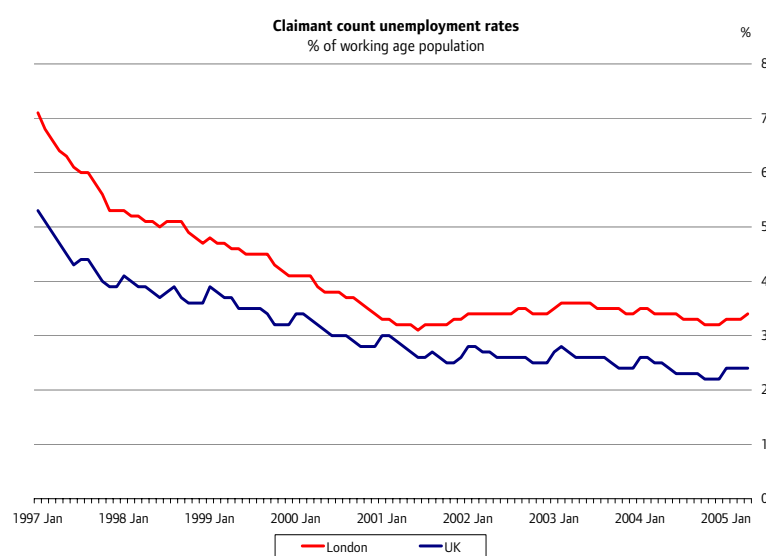
Source: Experian Business Strategies

## Claimant count unemployment remains low

- The rate of claimant count unemployment, people unemployed and claiming Jobseeker's Allowance, in London increased to 3.4% in April from 3.3% in March.
- There were nearly 165,000 unemployment claimants in London in April 2005, compared with just over 168,000 in April 2004.
- The claimant count unemployment rate in the UK remains below that of London.

Latest release: May 2005

Next release: June 2005



Source: Claimant Count, Nomis

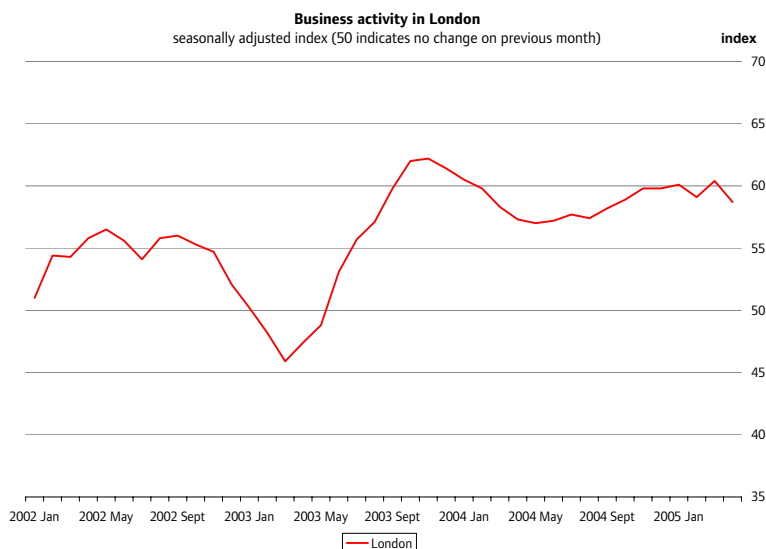


## Strong business activity in London

- London firms continued to expand their output of goods and services in April 2005.
- The Purchasing Managers' Index (PMI) of business activity recorded 58.7 in April, only slightly down from 60.4 in March.
- A rate above 50 on the index indicates an increase in business activity from the previous month.

Latest release: May 2005

Next release: June 2005

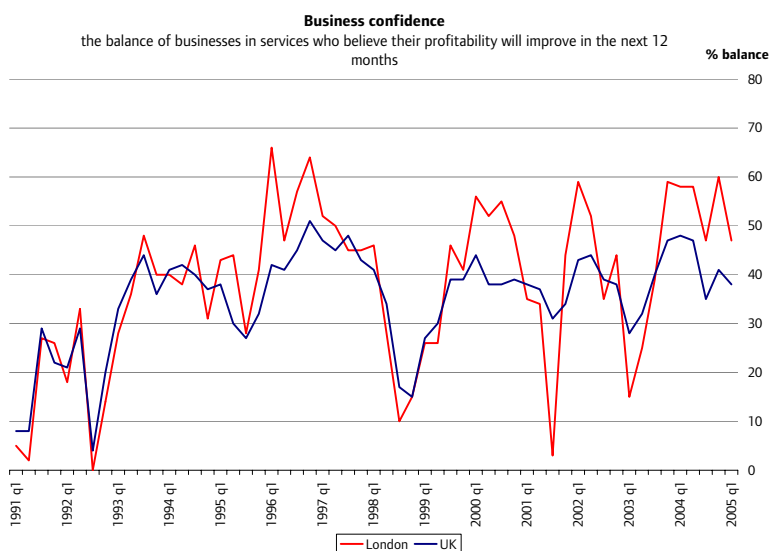


## Expectations of profitability remain higher in London than for the UK

- The British Chamber of Commerce (BCC)'s April Quarterly Economic Survey (QES) shows that London's service sector expects its profitability to improve.
- The net balance of London businesses in services expecting to increase profitability over the next 12 months was 47% in Q1 2005.
- The net balance of UK businesses in services expecting increased profitability over the next 12 months was 38% in Q1 2005.

Latest release: April 2005

Next release: July 2005

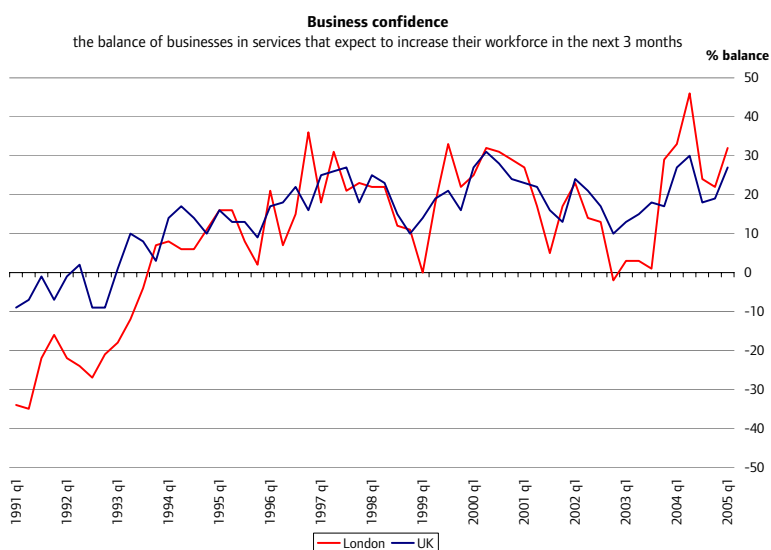


## London service businesses expect to increase their workforce

- The BCC's QES shows that London businesses in services expect to expand their workforce over the next three months.
- The net balance expecting to increase their workforce rose to 32% in Q1 2005 from 22% in Q4 2004.
- The net balance of service businesses in the UK expecting to increase their workforce increased to 27% in Q1 2005 from 19% in Q4 2004.

Latest release: April 2005

Next release: July 2005

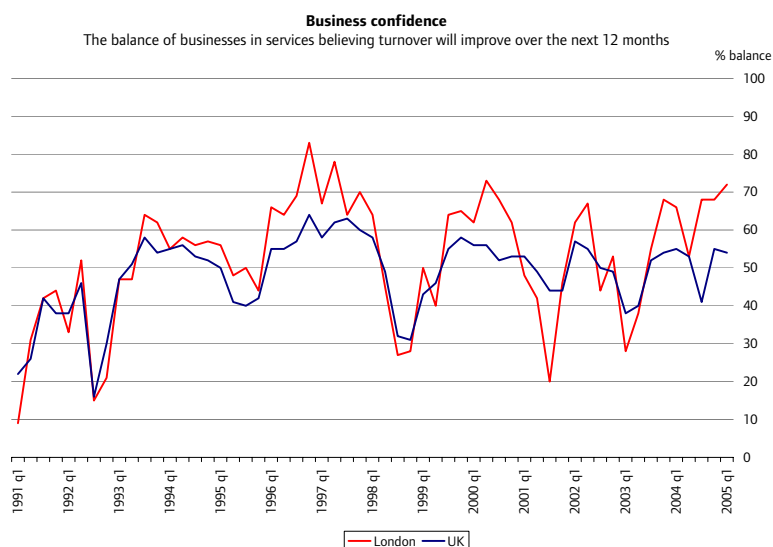


## London service businesses turnover expectations improve

- The BCC's QES shows that London businesses in services expect to increase their turnover over the next 12 months.
- The net balance of London service businesses expecting to increase their turnover grew to 72% in Q1 2005 from 68% in Q4 2004.
- The net balance of UK service businesses expecting to increase their turnover fell to 54% in Q1 2005 from 55% in Q4 2004.

Latest release: April 2005

Next release: July 2005



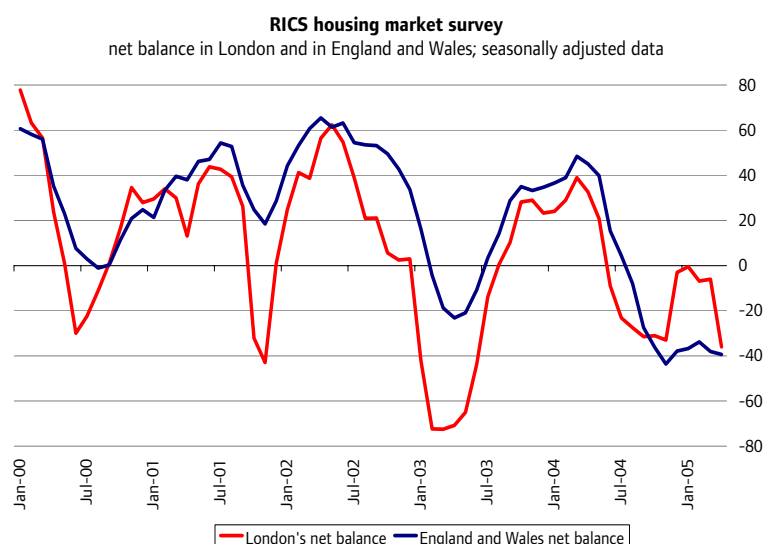
Source: BCC's QES

## Surveyors reporting a fall in London house prices

- The RICS survey showed a negative net balance for London house prices of -36 in April. This net balance is a sharp decline from the level of -6 in March.
- In recent months most surveyors have reported lower house prices in England and Wales. The net balance was -40 in April down from -39 in March.

Latest release: May 2005

Next release: June 2005



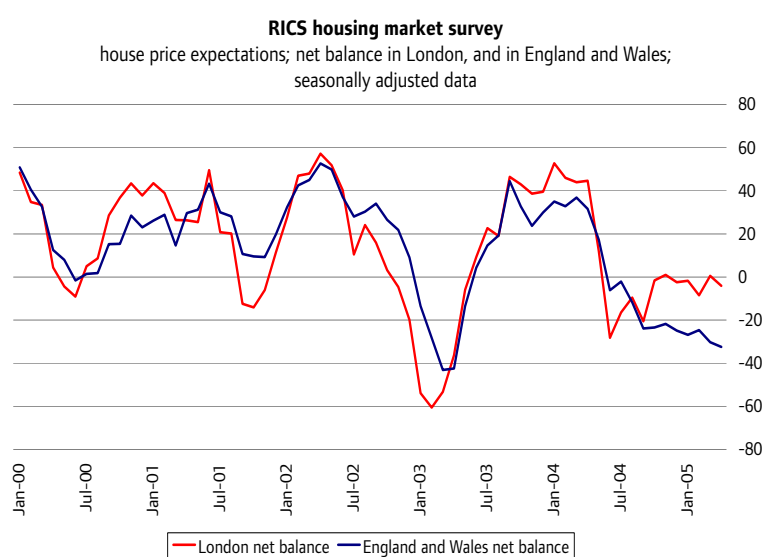
Source: Royal Institute of Chartered Surveyors

## Surveyors expecting relatively stable house prices in London

- The RICS survey shows a small majority of surveyors expect house price decreases over the next three months in London.
- The net expectations balance in London was -5 in April 2005, falling from a balance of zero in March.
- For England and Wales, the net balance for house price expectations continues to decline reaching -33 in April.

Latest release: May 2005

Next release: June 2005



Source: Royal Institute of Chartered Surveyors



**This month's supplement provides an overview of three key GLA Economics' work streams. Firstly, Bridget Rosewell looks at the evidence that the Greater London Authority (GLA) presented to the Lyons Inquiry (p.9). Secondly, Alon Carmel highlights the key findings in Transport for London's latest annual monitoring report on the congestion charge (p.11). And finally, Matthew Waite provides an overview of one of GLA Economics' newest work streams – the living wage (p.12).**

by Bridget Rosewell  
Consultant Chief Economist

## **Roaring at the Lyons**

The Lyons Inquiry is seeking to identify the most pressing issues affecting the present system of local government funding, how they might be resolved, and will set about analysing the practical impact of different options. The GLA's evidence to this inquiry looked at how to establish a more devolved system of financing the GLA group.

More decision-making should be devolved to increase accountability and encourage improvements in delivery. Too much central government financing weakens accountability and the ability to manage risk at a local level.

London is unique. It subsidises the rest of the UK and we do not expect this to change. Just over half of the GLA group's money comes from government grants, with sales, fees and charges providing 36 per cent and council tax payers accounting for just eight per cent. Other world cities have broader control over locally generated taxes which focuses responsibility for planning and management of risk more clearly.

Council tax is urgently in need of reform and the issues of accountability, gearing, regressivity, ring-fencing and capping addressed. However, we propose that the GLA precept is no longer funded through council tax. A regional income tax is the most realistic option for the replacement of the GLA precept alongside a reformed council tax that continues to fund the London boroughs.

**'London business rates subsidise the rest of the country by around £1.5 billion.'**

Replacing council tax as a source of GLA revenue would involve increasing the basic rate of income tax by around one per cent and if it also replaced the general grant, a regional income tax (RIT) would account for around four pence in the pound of basic rate income tax.

The RIT should initially be set at a level which funds the precept but if the GLA were to be devolved more powers to deliver services at a regional level then there would be a stronger case for replacing a proportion of the general grant with a 'slice' of existing income tax revenues.

Accompanied by greater devolvement of powers, the GLA should have powers similar to those of the Scottish Parliament to vary the income tax rate.

The business rate system should also be improved. More frequent revaluations than every five years (potentially annually) are needed so that business rate bills more fairly reflect real values and transitional relief becomes less of an issue. Business rates should also be re-localised immediately. Business rate setting should be devolved in London to the regional level with a limiting formula which could relate to the growth in nominal output.

London business rates subsidise the rest of the country by around £1.5 billion and this will continue, so a revised equalisation mechanism is needed.

The power to raise supplementary business rates could help fund infrastructure development. The business rate monies should be focused on infrastructure provision and providing for transport needs in particular.

A variety of local taxes could be introduced to widen the tax base and act as incentives to change behaviour. The congestion charge is an example of this and other examples can be considered in the future. However, the administrative burden is an important consideration. The only additional tax which is suggested is a tourist tax, levied on beds and operated through the rates system. This would raise revenue to cover the public services consumed by tourists.

**'We believe that the GLA should raise a more significant proportion of its own spending.'**

Current funding levels mean London under invests in its infrastructure, and economic and population growth is adding to the pressures. New solutions are needed which capture part of the financial benefits that accrue to beneficiaries of major infrastructure projects. A business rate levy is a possible option and provides the opportunity for tax incremental financing, where revenues provide the basis for borrowing.

Land value taxation has been proposed as an alternative form of taxation but it is not viable in the short term and there is still a balance to be struck between simplicity and targeting.

A devolved government needs devolved powers if it is to be effective and accountable. We believe that the GLA should raise a more significant proportion of its own spending.

by Alon Carmel  
Economist

## **Congestion charging - The latest findings**

Transport for London (TfL)'s third *Annual Monitoring Report* on the congestion charge was published in April of this year. The report presents three years of research and monitoring by TfL and GLA Economics about the scheme's business and economic impacts. This year's report is particularly important as it will inform the Mayor of London's decision on the western extension on which consultation is currently happening (until 12 July).

### **Immediate traffic effects**

The scheme's traffic effects and reduction in congestion were relatively immediate while effects on businesses would normally be expected to take time before becoming apparent. At this stage however, two years after the introduction of the scheme, any major impacts of the scheme would be expected to show up in available economic data.

### **Neutral impact on economy**

The balance of evidence indicates that the scheme had a broadly neutral impact on London's economy. London's economy was experiencing a slow down when the congestion charge was introduced which complicated the task of isolating any impact of the congestion charge. The report analysed data from as many different sources as possible and business performance was examined (in terms of numbers of businesses, employment, turnover and profitability) inside and outside the zone.

The Annual Business Inquiry, the Beta Model database, the Dun and Bradstreet database and the London Annual Business Survey were used and all pointed to no discernible impact on business performance from the charge. Sectoral evidence from the business performance research programme is less conclusive.

Some sectors within the charging zone have shown better performance than outside the zone. Other sectors have performed worse inside the zone than outside. These differences are all relatively small, and are not consistent between different datasets. It is not possible to be certain what part of these small differences (positive or negative) result from the congestion charge. TfL's business attitude

surveys for 2004 suggest that there is continued recognition of transport benefits associated with the scheme, albeit at a slightly lower level than in 2003. A majority of businesses continue to support the scheme, provided that there is continued investment in public transport.

**'A majority of businesses continue to support the scheme, provided that there is continued investment in public transport.'**

### Retail impacts

Particular attention has focused on the retail sector since surveys have suggested that retailers are particularly concerned about the charge. In the most thorough study of the available data yet, GLA Economics and Professor Bell from Imperial College published an econometric analysis which found that:

- i) There was no effect on total central London retail sales.
- ii) There may have been an effect from the charge on John Lewis's store in Oxford Street.

The report discusses some hypotheses for why the John Lewis Oxford Street store might be affected by the charge even though the retail sector as a whole in central London was not. The main explanation suggested is that John Lewis's Oxford Street store had a greater proportion of car-borne shoppers than other stores.

### Resources:

The TfL report is available at:

[www.tfl.gov.uk/tfl/cclondon/pdfs/ThirdAnnualReportFinal.pdf](http://www.tfl.gov.uk/tfl/cclondon/pdfs/ThirdAnnualReportFinal.pdf)

The GLA Economics/Imperial econometric report is available at:

[www.london.gov.uk/mayor/economic\\_unit](http://www.london.gov.uk/mayor/economic_unit)

by Matthew Waite  
Senior Economist

## A 'living wage' in London

As a result of his manifesto commitment in the last Mayoral election, the Mayor of London established a living wage unit within GLA Economics to look at the issue of a realistic living wage in London and to examine related poverty issues. The unit's first report, *A Fairer London: The Living Wage in London*, was published at the end of March and considers the issue of a living wage in London and looks at what threshold might be considered as constituting poverty level wages in London.

### Calculating the living wage

A two-stage process was used to calculate a 'living wage' for London. First a 'poverty threshold wage' was calculated by using two methods. One approach estimates basic living costs and calculates the wage required to meet those costs which yielded a figure of £5.70 per hour for London. The other approach is based on income distributions and takes 60 per cent of median income as defining a poverty level wage – for London this yields a figure of £5.90 per hour. The poverty threshold wage used in the report is the average of the two figures, £5.80 per hour.

**'Around one in seven employees in London receives less than poverty level wages.'**

The fact that poverty level wages in London are significantly above the national minimum wage, which will be £5.05 per hour from October, is primarily due to the much higher

housing costs in London. If London's housing costs were the same as the UK average the poverty threshold wage in London would fall to around £5.30 per hour.

### **Staying above the poverty wage**

As stated above, the £5.80 per hour figure is a poverty threshold wage. The second stage of calculating London's 'living wage' looked at what was required to ensure that a person earning the living wage had a 'secure margin' over the level of poverty wages. The exact margin is a matter of judgement and was based on the research and analysis carried out for the report. In the end, a margin of 15 per cent was applied to the poverty level wage, yielding a figure of £6.70 per hour as the living wage for London.

Data from the Labour Force Survey can be used to establish the number of people that earn below a certain wage level in London. This data shows that, taking full-time and part-time employees together, around one in seven employees in London receives less than poverty level wages and around one in five receives less than the living wage.

As the first such report on a living wage for London, various simplifications and estimates were used in the study. Over the course of the next year the living wage unit will conduct further research to improve and develop these initial findings.

### **Resources:**

Download *A Fairer London*: [www.london.gov.uk/mayor/economic\\_unit](http://www.london.gov.uk/mayor/economic_unit).

## Data sources

<b>Tube and bus ridership</b>	Transport for London on 020 7941 4500
<b>GDP/GVA growth</b>	Experian Business Strategies on 020 7355 8200
<b>Tourism – overseas visitors</b>	<a href="http://www.statistics.gov.uk">www.statistics.gov.uk</a>
<b>Tourism – domestic visitors</b>	<a href="http://www.visitlondon.com">www.visitlondon.com</a>
<b>London airports</b>	<a href="http://www.caa.co.uk">www.caa.co.uk</a>
<b>Business activity</b>	<a href="http://www.rbs.co.uk/pmireports">www.rbs.co.uk/pmireports</a>
<b>Employment</b>	<a href="http://www.rbs.co.uk/pmireports">www.rbs.co.uk/pmireports</a>
<b>London FootFall</b>	<a href="http://www.footfall.com">www.footfall.com</a>
<b>Office space demand</b>	<a href="http://www.cbhillierparker.com">www.cbhillierparker.com</a>
<b>House prices</b>	<a href="http://www.nationwide.co.uk/hpi/">www.nationwide.co.uk/hpi/</a>
<b>Unemployment rates</b>	<a href="http://www.statistics.gov.uk">www.statistics.gov.uk</a>

## 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

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

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