

# London's Economy Today



Issue 36 | August 2005

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## Interest rates cut despite rising inflation

Christopher Lewis, Senior Economist

**Interest rates were cut by a quarter of a percentage point to 4.5 per cent by the Bank of England's Monetary Policy Committee at its meeting on 4 August 2005. Retailers, who have been facing a consumer-driven slowdown, have especially welcomed this news.**

The retail sector is not only important in terms of the output it contributes to London's economy but also to the leisure opportunity it provides shoppers. Retail is also a valuable form of employment for many groups in the labour market, partly due to the high proportion of part-time employment opportunities when compared to other sectors of the economy. In addition, retail provision can bring many social or economic benefits to disadvantaged communities. This month's supplement *Reluctant Retailers?* by Matthew Waite provides an overview of GLA Economics' work on retail and regeneration in London.

GLAECONOMICS

## International conference announced!

Mark your diaries! The date of GLA Economics' second international conference, **The Dynamic City**, has been announced: **Tuesday 8 November, 2005.**

The Dynamic City conference looks at how cities are evolving and how we are responding. Join speakers and delegates from around the world as they explore what it means to be a dynamic city in the 21st century.

Conference delegates will hear from some of the finest international speakers including renowned author **Saskia Sassen** (University of Chicago), **Bridget Rosewell** (Consultant Chief Economist, GLA Economics) and **Christian Lefevre** from the University of Paris.

Six workshops exploring some of the most challenging issues facing dynamic cities will be held in the afternoon of the conference. The workshops will be chaired by London experts and will include a presentation by a GLA Economics' economist and audience discussion. The six workshops are entitled Green City, Skilled City, People City, Accessible City, Knowledge City and Retail City.

**To find out more, to request a brochure or to register:**

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Overall, London's economy has remained firm since the recent terrorist attacks. In defiance of the terrorists, business in general is back to normal in London. There has been continued strength in the financial sector, which is especially important to the capital. Downward movements in UK stock markets following

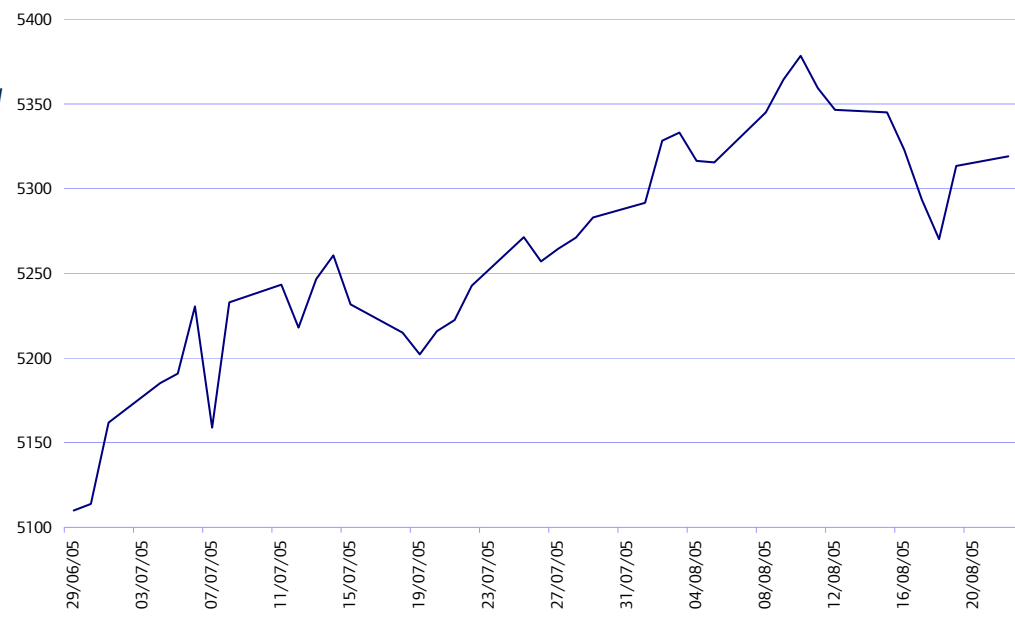
**'Downward movements in UK stock markets following the terrorist attacks on 7 and 21 July have been short lived.'**

the terrorist attacks on 7 and 21 July have been short lived with the FTSE 100 reaching near four-year highs indicating that the long-term effects on the economy are not expected to be significant (see Figure 1). The main impacts seem likely to be on tourism and central London's retail sector. London Retail Consortium figures show that July retail sales in central London were 8.9 per cent lower, on a like-for-like basis, than in July 2004. This compares with a smaller 1.9 per cent annual decline for the UK as a whole. Any spatial

displacement of retail spending away from central London, however, could benefit retailers in outer London as well as the wider South East region.

**Figure 1: FTSE 100**

Source: Wall Street Journal



In July, the Purchasing Managers' Index measures of seasonally adjusted business activity and new orders in London both showed solid expansion and still outstripped the national average. Both these London index levels fell slightly to 55.4 but they are still significantly above 50, which is the level consistent with no change on the previous month. London's seasonally adjusted index level of employment showed employment contraction, remaining just below the 50 mark for the second consecutive month. However, Office for National Statistics data shows that London's unemployment rate is similar to a year ago and the trend is currently relatively flat.

### **Bank lowers interest rates as UK growth remains weak**

Despite rising consumer price inflation the Bank of England lowered interest rates to 4.5 per cent in August. Action was taken to bolster subdued output growth and sluggish household spending. The preliminary estimate of UK growth was a below trend 0.4 per cent in Q2 2005, though this might well be revised slightly upwards in future releases. In addition UK manufacturing is experiencing a technical recession. The retail sector also remains weak with

total sales volume decreasing by 0.3 per cent in July. The total volume of sales is only 1.8 per cent higher than a year ago but at least this is an improvement from a low in annual growth of 1.0 per cent in May. Housing market activity has been broadly stable in recent months, but shows few signs of significant improvement. Furthermore, UK claimant count unemployment rose for a sixth month in a row in July. However, the decision by the Monetary Policy Committee at its 100<sup>th</sup> meeting was on a knife-edge with four of the nine members, including the Governor, voting against any move due to building inflationary pressures. Their worries were confirmed by data showing that UK Consumer Price Index (CPI) annual inflation rose to 2.3 per cent in July from 2.0 per cent (the target level) in June. This was the highest rate since the start of the CPI series in 1997. Annual manufacturing input price inflation, which is being driven by higher oil prices, rose to 13.5 per cent in July, its highest level since February 1985.

### Record high oil prices

Oil prices have risen above \$65 per barrel over the last month (see Figure 2). A shortage of refining capacity, continued strong demand and concerns over future supply have led to record nominal prices. Worldwide oil demand continues to be driven by the US and Chinese economies. The death of King Fahd and security threats in Saudi Arabia, alongside international political tensions caused by Iran announcing that it will resume uranium processing, have underpinned supply fears. In addition the increase in non-OPEC (Organisation of Petroleum Exporting Countries) oil supplies in 2005 is now expected to be less than previously forecasted. However, in relative terms oil prices are still lower than they were in 1980.

**Figure 2: Brent crude oil price (\$ per barrel)**

*Source: FT.com*



### US expansion contrasts with weaker eurozone growth

A healthy US economy combined with accelerating house price inflation and high oil prices has led the Federal Reserve to once again raise interest rates by 0.25 per cent (the tenth such increase since June 2004) to 3.5 per cent. US retail sales remained buoyant in July driven by a surge in car sales. July

also saw the strongest US job growth for five months, and at five per cent unemployment is at a four year low. US Gross Domestic Product (GDP) growth rose by 0.8 per cent in Q2 2005, following a rise of 0.9 per cent in Q1. In contrast eurozone growth slowed to 0.3 per cent in Q2 2005 from 0.5 per cent in Q1. The two major eurozone economies performed even worse with zero growth in Germany and only 0.1 per cent growth in France. The International Monetary Fund has cut its growth forecast for the eurozone to 1.3 per cent (from 1.6 per cent) in 2005 and to 1.9 per cent (from 2.3 per cent) in 2006. Consumer confidence within the eurozone remains weak and in contrast with the US and UK, unemployment remains high at above 8.5 per cent.

China has adopted a more flexible exchange rate regime. The yuan will no longer be pegged to the US dollar, but will float in a narrow band against a basket of currencies including sterling and the euro. The move also effectively revalues the yuan by just over two per cent against the US dollar so is unlikely to have a huge immediate effect on the world economy. However, the reform is being seen by many as a first step towards further currency liberalisation. Over time the importance of the Chinese economy in terms of the impact it has on the global economy will grow and grow. In July the first Chinese visitors to travel to Britain on approved destination tourist visas arrived in London. Japan's economy shows signs of further improvement. Despite parliament's rejection of the government's plan to privatize the nation's postal savings the economic reform agenda is expected to continue whatever the outcome of the snap election on 11 September.

### Global activity supported by US and Asian economies

As stated by the Bank of England, the July terrorist attacks in London are not expected to have a sizeable influence on economic activity. The impact on London's tourism industry and central retail sector will be greater but as long as further attacks do not happen it could be that a full recovery will occur over time. UK economy is currently growing below inflation is rising. However, growth is below trend and inflation is only just government's two per cent target. A series of rapid further interest rate cuts should certainly not be expected. Meanwhile UK growth in business services and finance remains strong, which is good news for the London economy. For example there was a record number of hedge fund launches in the first half of this year. Weak domestic demand in the eurozone is not being helped by high oil prices. Existing spare oil production capacity is historically low so prices are unlikely to fall significantly during the rest of the year. This will slightly dampen world economic activity but the global economy is expected to remain healthy with robust US and Asian growth, especially China and India.

**'A series of rapid further interest rate cuts should certainly not be expected.'**

London's a series of expected Overall the trend and only just above the of rapid

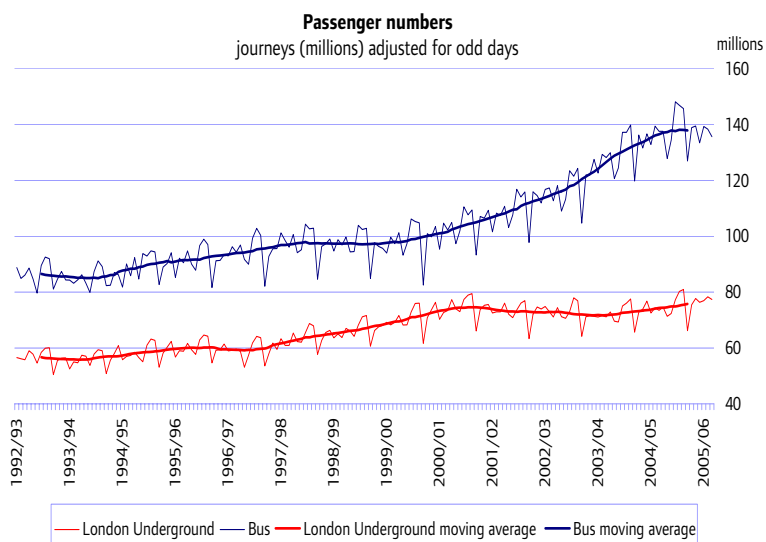
# Economic indicators

## Moving average of passenger numbers

- The most recent 28-day period is from 28 May to 25 June 2005. The statistics are for a period before the terror attacks of July 7 and July 21.
- London's public transport had 213.1 million passenger journeys; 135.7 million by bus, 77.4 million by Underground.
- The moving average increased to 213.7 million passengers every period. The buses' average was 138 million passenger journeys. The average for the Underground was 75.8 million.

Latest release: July 2005

Next release: August 2005



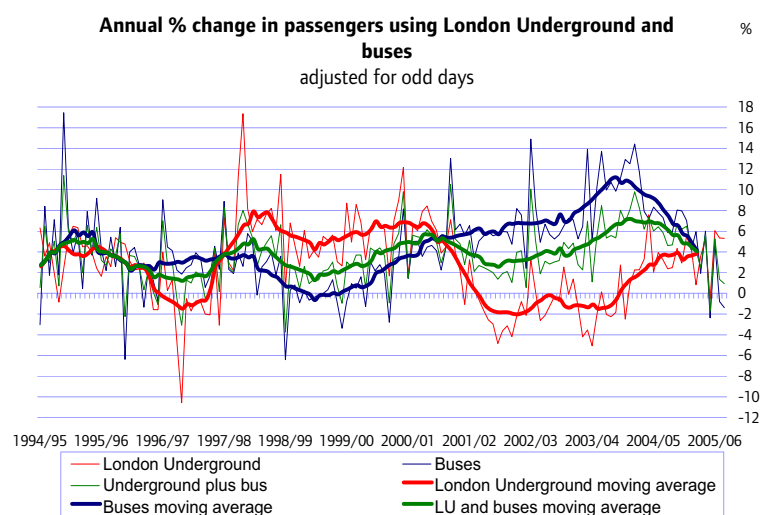
Source: Transport for London

## Passenger journeys' annual growth rate slows

- The average annual rate of growth in passenger journeys is 3.9%, below the annual growth in the previous period of 4.3%.
- The average annual rate of growth in bus journey numbers slowed further to 4%, down from 4.7% in the previous period.
- The average annual rate of growth in Underground passenger journey numbers increased from 3.5% to 3.7%.

Latest release: July 2005

Next release: August 2005



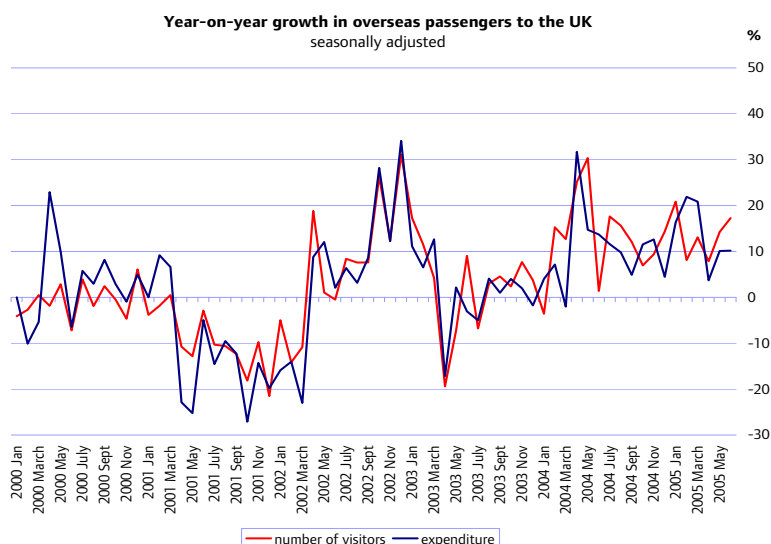
Source: Transport for London

## Growth in number of overseas visitors to the UK

- June 2005 saw growth in overseas visitor numbers to the UK. Up to half of overseas visitors spend time in London.
- The annual growth rate of overseas visitors to the UK was 17.3% in June 2005.
- The year-on-year growth in expenditure by overseas visitors in the UK was 10.2% in June 2005.

Latest release: August 2005

Next release: September 2005



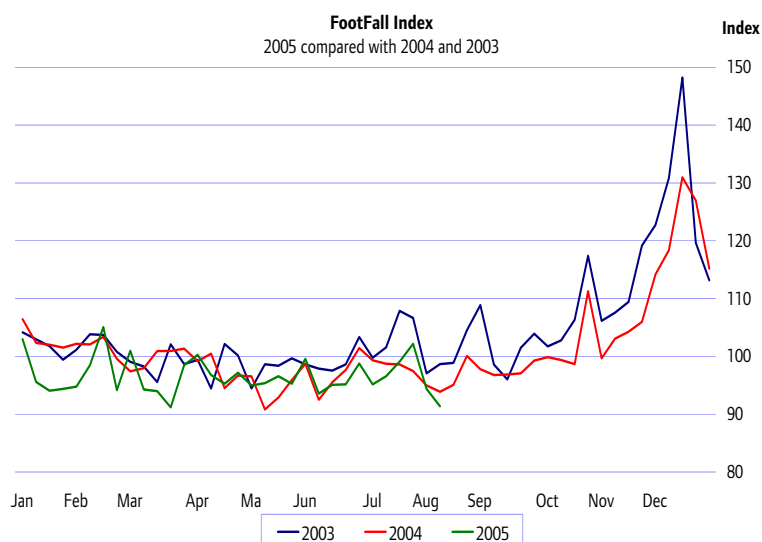
Source: Office for National Statistics

## Shopping numbers fall in early August following July recovery

- The FootFall Index of shoppers reported here is to the week ending 15 August 2005.
- The index in London fell to 91.2 in mid-August compared to the level of 102 in the last week of July.
- The level of the index in early August 2005 is lower than in early August 2003 and 2004.
- The FootFall index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: 15/08/05

Next release: every week



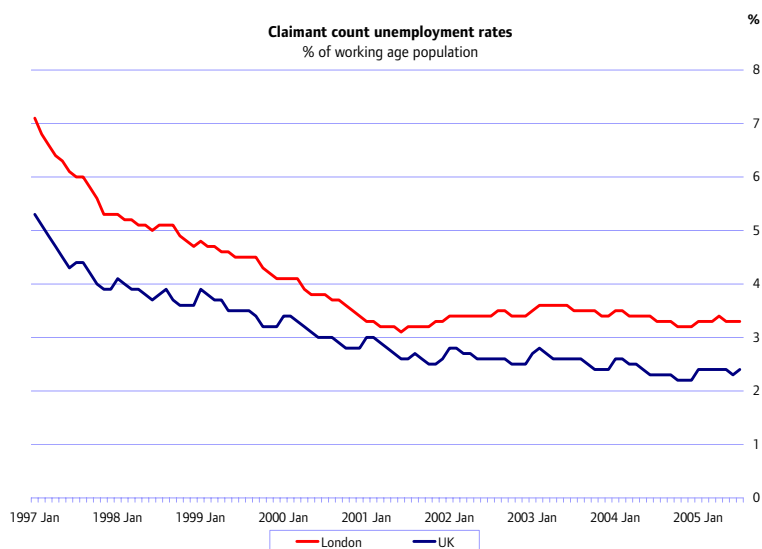
Source: FootFall Limited

## Claimant count unemployment rate stable

- The rate of claimant count unemployment, people unemployed and claiming Jobseeker's Allowance, in London remained constant at 3.3% in July 2005.
- There were 163,400 unemployment claimants in London in July 2005 compared with 163,000 in July 2004.
- The claimant count unemployment rate in the UK remains below that of London's.

Latest release: August 2005

Next release: September 2005



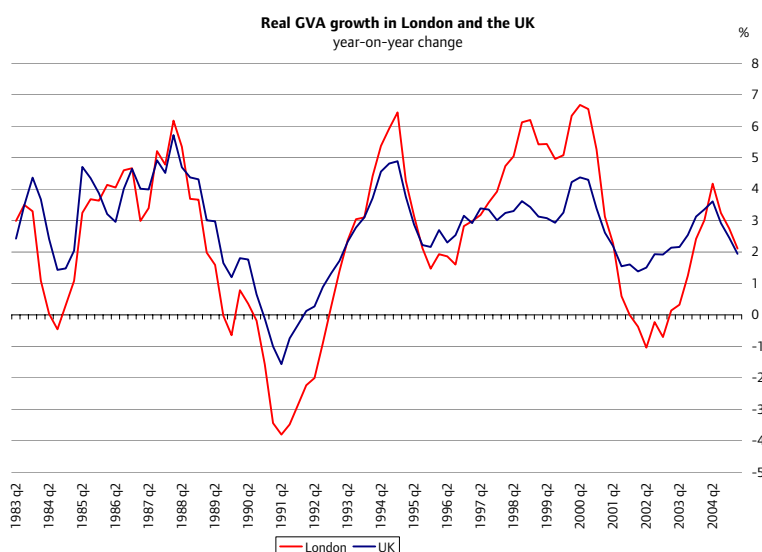
Source: Claimant Count, Nomis

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

- London's annual growth in output was 2.1% in Q1 2005, down from a revised 2.7% in Q4 2004.
- The UK's annual growth in output was 1.9% in Q1 2005, down from a revised 2.4% in Q4 2004.
- There have been changes to the series to reflect revisions by the Office for National Statistics and the availability of new data.

Latest release: August 2005

Next release: November 2005



Source: Experian Business Strategies

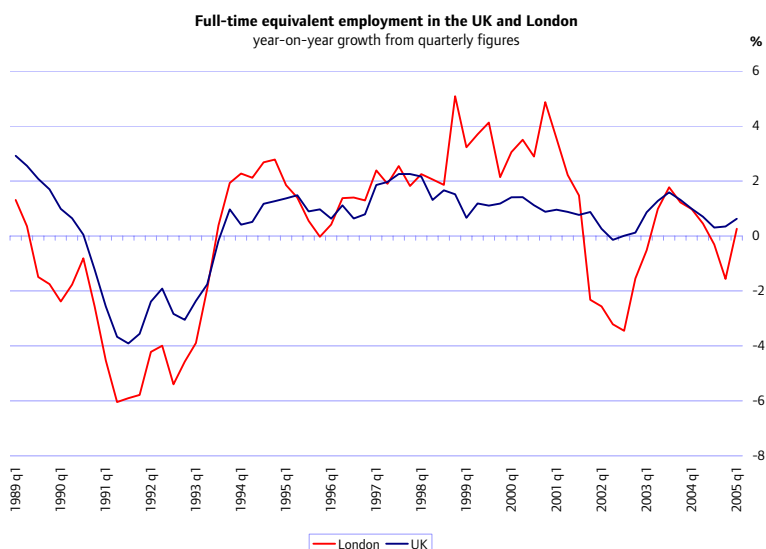


## London returns to employment growth

- London's year-on-year employment growth recovered to 0.3% in Q1 2005 compared to a decrease of 1.6% in Q4 2004.
- Annual employment growth in the UK as a whole increased to 0.6% in Q1 2005 from 0.3% in Q4 2004.
- There have been changes to the series to reflect revisions by the Office for National Statistics and the availability of new data.

Latest release: August 2005

Next release: November 2005



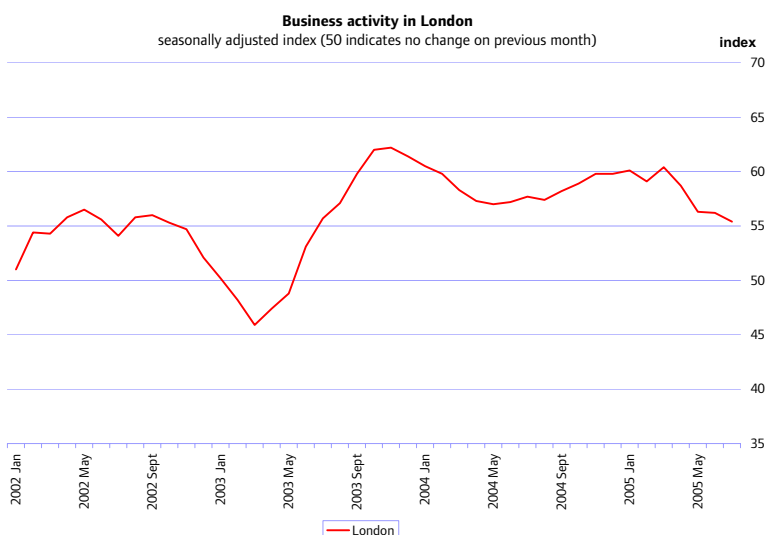
Source: Experian Business Strategies

## Business activity in London remains healthy in July

- London firms continued to expand their output of goods and services in July 2005.
- The Purchasing Managers' Index (PMI) of business activity recorded 55.4 in July, only slightly down from 56.2 in June.
- A rate above 50 on the index indicates an increase in business activity from the previous month.

Latest release: August 2005

Next release: September 2005



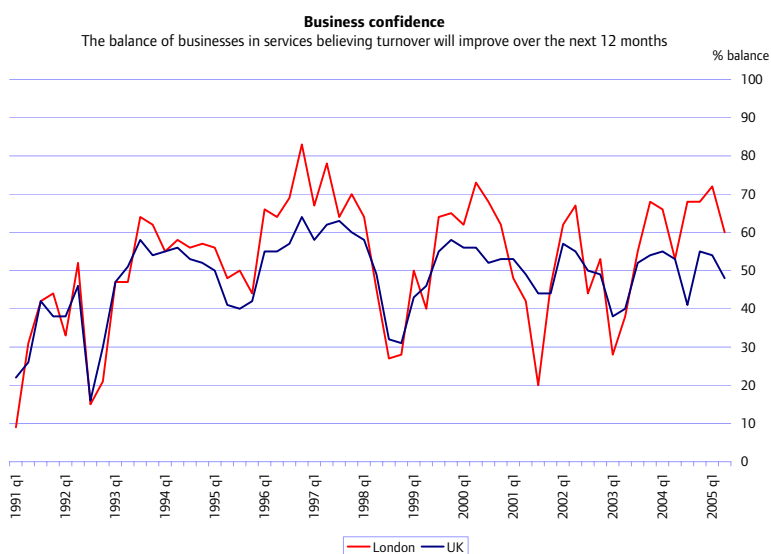
Source: PMI/The Royal Bank of Scotland

## London service businesses expect increasing turnover

- The BCC's Quarterly Economic Survey shows that London businesses in services expect growing turnover over the next 12 months.
- The net balance of London service businesses expecting to increase their turnover was 60% in Q2 2005, although this is down from 72% in Q1.
- The net balance of UK service businesses expecting to increase their turnover fell to 48% in Q2 2005 from 54% in Q1.

Latest release: July 2005

Next release: October 2005



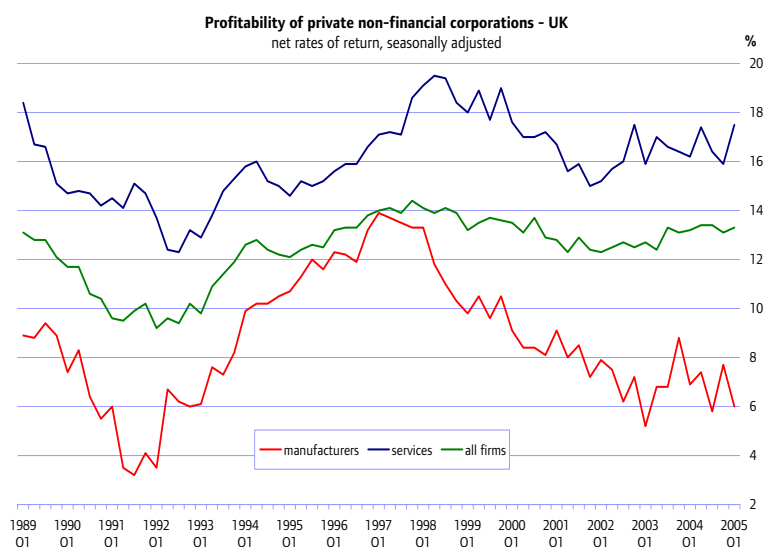
Source: BCC, Quarterly Economic Survey

## UK corporate profitability

- Overall UK corporate profitability remained strong at the end of 2004 and into the beginning of 2005. The net rate of return by private corporations was 13.3% in Q1 2005.
- The net rate of return in services was 17.5% in Q1 2005, increasing from 15.9% in Q4 2004.
- The net rate of return in UK manufacturing corporations is lower than for services at 6% in Q1 2005.

Latest release: July 2005

Next release: October 2005



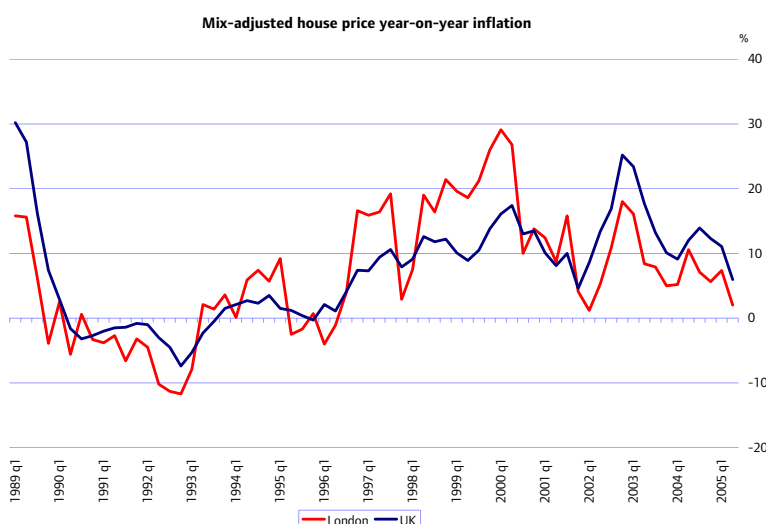
Source: Office for National Statistics

## London's housing market slows

- The ODPM house price index is an official measure of house prices.
- Annual house price growth in London slowed to 2% in Q2 2005 from 7.4% in Q1.
- Annual house price growth continues to be higher for the UK but this slowed to 6% in Q2 2005 from 11.1% in Q1.

Latest release: August 2005

Next release: November 2005



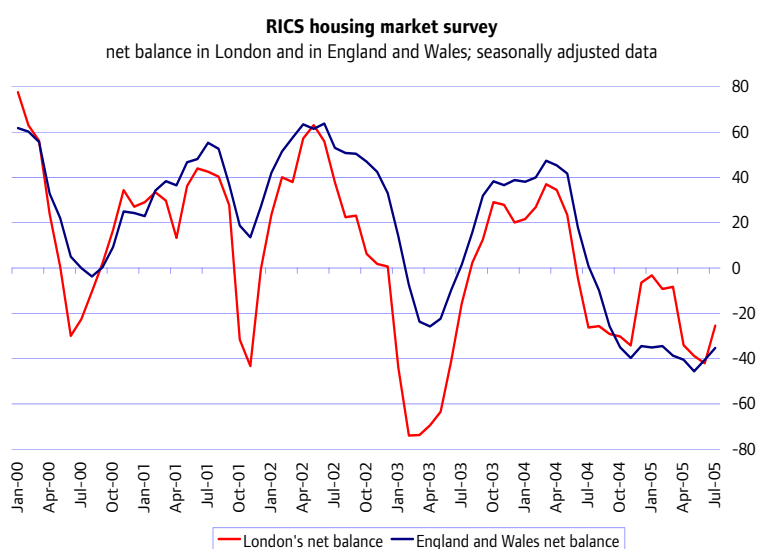
Source: Office for the Deputy Prime Minister

## Surveyors reporting a fall in London house prices

- The RICS survey showed a negative net balance for London house prices of -26 in July. This net balance is a recovery from the level of -42 in June.
- In recent months most surveyors have reported lower house prices in England and Wales. The net balance was -36 in July up from -41 in June.

Latest release: August 2005

Next release: September 2005



Source: Royal Institute of Chartered Surveyors



# Reluctant Retailers?

## The link between retail and regeneration

by Matthew Waite  
GLA Economics

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**‘Low-income’ and ‘high unemployment’ areas are not seen by some retailers as great investment opportunities. But research shows that retailers who assume that ‘underserved’ areas mean higher costs and lower revenues may be wrong. GLA Economics’ latest retail working paper, *Retail and Regeneration*, uses data from both sides of the Atlantic to show that there are business opportunities to be exploited from investing in deprived underserved markets.**

Underserved areas tend to have low-income households, high unemployment rates, low-skilled populations, low availability of suitable sites and in many cases are home to large ethnically diverse populations who may require a different mix of products to the mainstream population. The profitability of deprived areas is further questioned because of high crime rates, or at least high levels of perceived crime, and restricted parking facilities – both of which are thought to decrease foot traffic.

### **Retail in London: Working Paper B – Retail and Regeneration**

This groundbreaking paper looks at how retailing can contribute to the regeneration of deprived areas in London. Using a variety of sources, the paper reviews the economic case for investment into what are commonly referred to as underserved areas (areas with inadequate retail provision of goods and services).

In general, retailers appear to be reluctant to invest in deprived, underserved areas. This reluctance is not surprising as traditional appraisal methods imply that higher costs and lower sales may be incurred by retailers in deprived areas.

Underlying the analysis in GLA Economics’ working paper, *Retail and Regeneration*, is the understanding that retailers will not enter an area unless there is an economic case for doing so. Some areas therefore will not be served. However, *Retail and Regeneration* shows that there are a number of reasons why many areas currently considered as ‘no-go’ areas could in fact be suitable areas in which to invest and operate. Some attractive features of deprived areas include: the higher returns on commercial property seen in disadvantaged areas, little or no competition from other retailers, large supplies of readily available local labour and the potential access to profitable ethnic markets.

**‘Attractive features of deprived areas include: the higher returns on commercial property, little or no competition, large supplies of readily available local labour and access to profitable ethnic markets.’**

## Ready for regeneration

As well as the private benefits of investing in underserved and deprived areas, there are wider economic, physical and social inclusion benefits to be derived. In the first instance, retail development offers residents of disadvantaged communities access to retail goods and services. Retail is a valuable form of employment for many groups in the labour market, partly due to the high proportion of part-time employment opportunities available when compared to other sectors of the economy. Also, entry into some forms of retail employment requires few qualifications and is consequently a valuable form of employment in deprived areas that exhibit large populations with entry-level skills and low employment rates. In addition, developing in urban areas often requires the development of brownfield land which can considerably improve the quality of the local environment.

There are, therefore, a number of spin-off benefits to be gained from improving retail provision in underserved areas. Moreover, because these areas are underserved, the wider economic benefits created (e.g. higher employment) are more likely to be net benefits with little displacement from other stores – for example, a new store in an underserved area is more likely to be creating new, additional jobs rather than just taking away jobs from existing stores which are competing in the same area. As a result, there is a strong argument for the public sector to act as a catalyst for retail investment into underserved areas though the extent of its involvement is likely to decline as retailers themselves become more aware of the private benefits of investment in underserved areas.

***‘There is a strong argument for the public sector to act as a catalyst for retail investment into underserved areas.’***

Overall, *Retail and Regeneration* illustrates that there are business opportunities to be exploited from investing in deprived underserved markets. In addition to private commercial benefits, there are wider economic and social benefits

### Book your place at The Dynamic City conference

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to disadvantaged communities from increased retail development. To this end, initiatives such as the current work of Business in the Community<sup>1</sup>, which attempts to deliver private investment into currently underserved areas, are to be encouraged.

## Further studies

*Retail and Regeneration* is published as part of a wider GLA Economics' study into retail in London. In total, ten retail working papers will be published on a range of topics including grocery retailing, leisure and retail, smaller retailers, and retail and the labour market amongst others. For copies of the retail working papers currently printed, view:

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

If you'd like to subscribe to receive hard copies of future retail working papers, please email [glaeconomics@london.gov.uk](mailto:glaeconomics@london.gov.uk) or call +44 (0)20 7983 4922.

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### (Footnotes)

<sup>1</sup> [www.bitc.org.uk/index.html](http://www.bitc.org.uk/index.html)

## 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 of 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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GLA Economics provides expert advice and analysis on London's economy and the economic issues facing the capital. Data and analysis from GLA Economics provide a sound basis for the policy and investment decisions facing the Mayor of London and the GLA group. The unit was set up in May 2002.

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