

London's Economy Today



Issue 65 | January 2008

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US Federal Reserve makes dramatic cuts in interest rates

by Richard Davies,
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The US Federal Reserve reduced the US base interest rate by 75 basis points to 3.5 per cent on 22 January 2008. This decision was not made at one of its formal committee meetings, which is unusual, but was done as an emergency response to the increasing volatility in equity markets and the increasing risk of a severe economic slowdown.

The US Federal Reserve also held a regular meeting on 29-30 January when it cut interest rates by a further 50 basis points. The US base rate has now fallen to 3 per cent from the recent peak of 5.25 per cent in August 2007. The Fed is taking vigorous rate cutting action as fears that there could be a recession in the US increase. This would adversely affect other global economies including the UK. Even if the US does not have a recession the sharp slow down that it will experience this year will have a dampening impact on world growth and the London economy.

Volatility in global equity markets

Global stock markets have fallen since the New Year amidst an increasing risk that the US economy could be heading for recession. This is despite efforts by the US Government through its proposed package of fiscal stimuli and by the US Federal

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Latest news...



● **London's Central Business District: Its global importance** London's CBD is a premier global business district employing around 1.5 million people. Globalisation presents London's CBD with a range of economic opportunities.



● **Working Paper 27: Assessment of global imbalances** Global imbalances refer to the large and persistent (since 1992) US current account deficit on the one hand and large Asian current account surpluses on the other (e.g. in China). Adjustment of global imbalances require movements in global exchange rates and interest rates which present both threats and opportunities for London.

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Reserve through aggressive interest rate cuts to bolster the US economy. The FTSE 100 index fell by over 300 points or nearly 5.5 per cent on 21 January 2008. This was the largest fall in one day since the 9/11 attacks on New York in 2001. However, even taking this into account, the FTSE 100 was still trading at around June 2006 levels and since then there has been a slight recovery. Markets are expected to remain volatile for some time, as concerns remain about the health of the global economy. There have also been major fluctuations in the price of other assets. Government bond prices have appreciated as investors look for safer returns. The price of oil has fallen back slightly from recent peaks due to expectations of slower world growth and therefore a decrease in its demand.

Credit crunch still a major problem

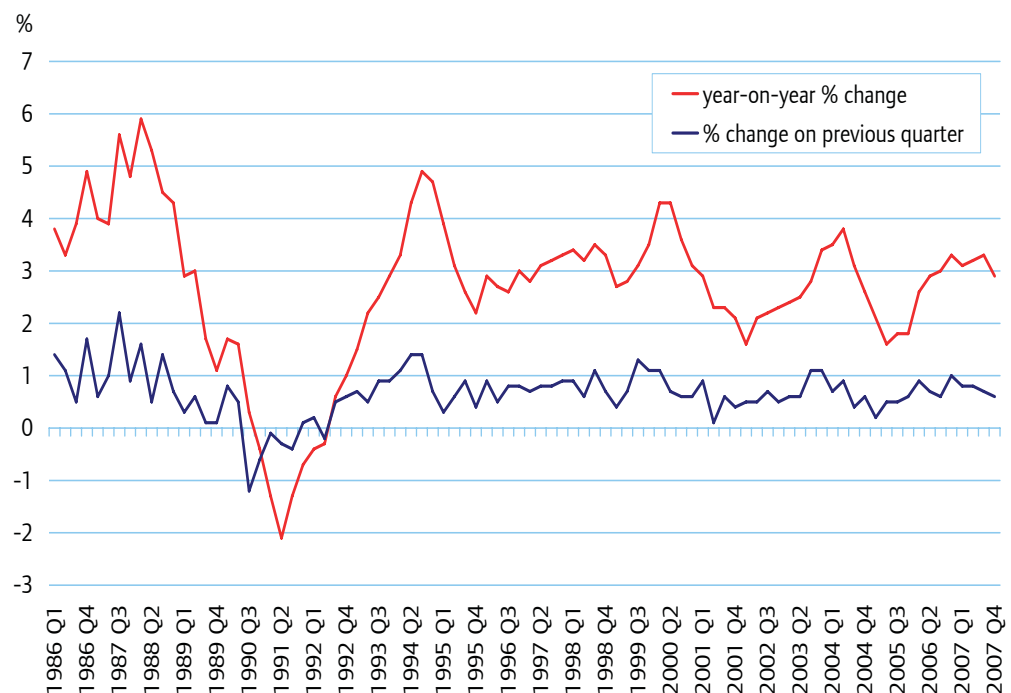
The Bank of England in its Credit Conditions Survey Q4 2007 reported that the availability of secured credit to UK households and corporations had been reduced in Q4 2007 and lenders expected a further reduction in Q1 2008. Lenders said that defaults on secured lending had remained broadly unchanged in Q4 2007. However, they expected that defaults on secured lending would rise in Q1 2008.

UK GDP growth eases slightly and is expected to slow further during 2008

The Office for National Statistics (ONS) has published preliminary estimates of UK GDP growth figures for Q4 2007. In Q4, the increase in GDP was marginally lower than in Q3 2007. A small rise in total production growth was more than offset by slightly weaker growth in services. UK annual GDP growth in Q4 2007 was 2.9 per cent, down from 3.3 per cent in the previous quarter (see Figure 1). Output from business services and finance increased by a strong 4.2 per cent between Q4 2006 and Q4 2007. However, growth in this important sector for the London economy fell in Q4 2007. This was mainly due to a weakening in financial intermediation, which is also having a negative impact on London's economy.

Figure 1:
UK GDP Growth

*Source: Office for
National Statistics*



UK business confidence declines

The Institute of Chartered Accountants in England and Wales' Business Confidence Monitor for Q4 2007, showed that UK business confidence declined for the second consecutive quarter to a two-year low. Pessimism about future business prospects over the next year has been due to the volatility in financial markets, the effect of higher interest rates since August 2006 and the slowing housing market. London remained more optimistic than the rest of the UK regions and confidence in the capital stands at +2.9 marginally up from the +1.5 registered in the previous quarter. However, due to London's exposure to the financial services sector, this confidence is likely to have been affected by recent turbulence in financial markets.

Mixed retail sales figures over the festive period

Retail sales figures over Christmas were mixed at best. Some retailers, particularly supermarkets, did well. However, the British Retail Consortium reported that overall UK retailers had their worst increase in Christmas sales for three years with like-for-like sales only increasing by 0.3 per cent in December from a year earlier. However, Footfall, the retail research body, has reported that shoppers had deliberately waited for the January sales, as the number of shopping visitors had increased in the first week of January on the same period last year.

London's economy to slow in the face of a tougher global background

There is no doubt that 2008 will be tougher for the global economy. The UK economy is expected to slow down from its current strong base of about 3 per cent to less than 2 per cent. The London economy will also weaken and has been adversely impacted by problems in the financial services sector.

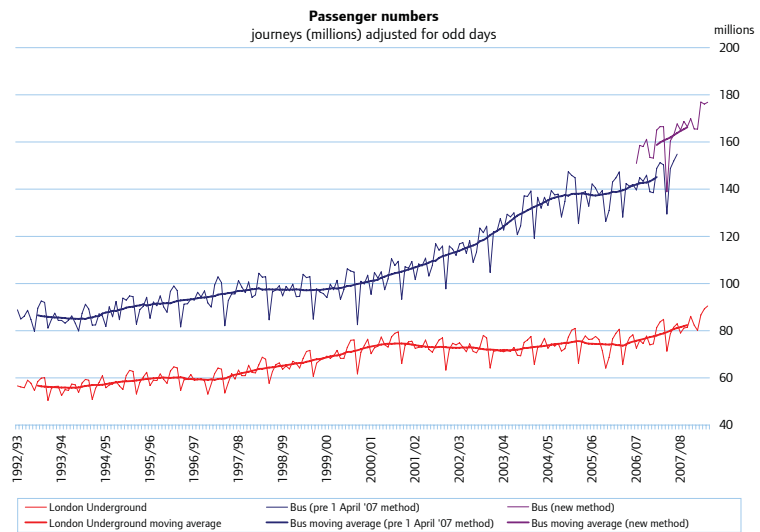
The credit crunch and volatility in financial markets continues and overall confidence is low. There is an increasing possibility of a US recession, which would adversely affect world growth. It remains to be seen the extent to which Asian economies have decoupled themselves from the US and if their strong economic growth can continue unabated so as to offset the expected sluggish growth in developed economies.

The actions of the Bank of England and other central banks in cutting interest rates and making more liquidity available to money markets, has helped to reduce inter-bank lending rates. Further interest rate cuts by the Federal Reserve and the Bank of England are expected during 2008. However, central banks in developed countries have a fine balancing act between mitigating the downward risks of a sharp economic slow down and concern over upside risks to inflation from higher energy and food prices. In this background the London economy faces far choppy waters in 2008 than it has for at least half a dozen years.

Economic indicators

Increase in moving average of passenger numbers

- The most recent 28-day period is from 11 November to 8 December 2007. London's Underground and buses had 267.3 million passenger journeys; 176.8 million by bus and 90.5 million by Underground.
- The moving average increased to 248.6 million from 247.4 million passengers every period. The moving average for buses was 166.2 million. The moving average for the Underground was 82.4 million.
- The methodology used to calculate the number of bus passenger journeys was changed by TfL from 1 April 2007. For a detailed explanation please see LET edition 58 (June 2007).



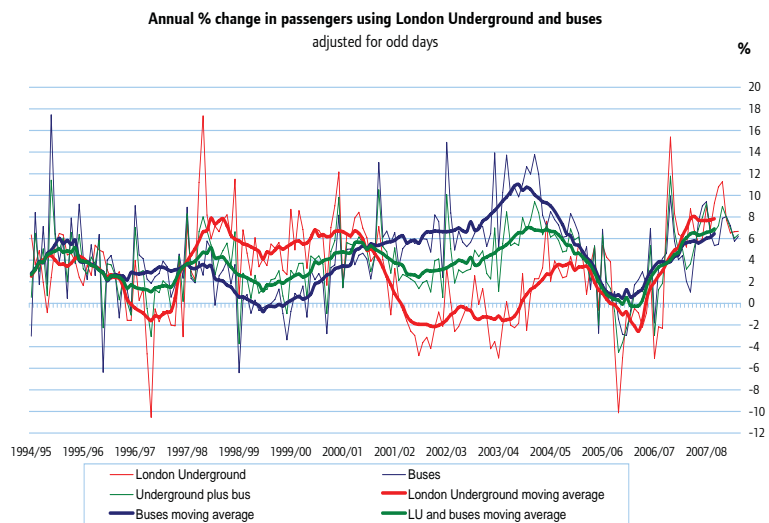
Source: Transport for London

Latest release: January 2008

Next release: February 2008

Average annual growth rate of passengers increases

- The moving average annual rate of growth in passenger journeys increased to 6.9% from 6.6% in the previous period.
- The moving average annual rate of growth in bus passenger journey numbers increased to 6.4% from 6.1% in the previous period.
- The moving average annual rate of growth in Underground passenger journey numbers increased to 7.8% from 7.7% in the previous period.



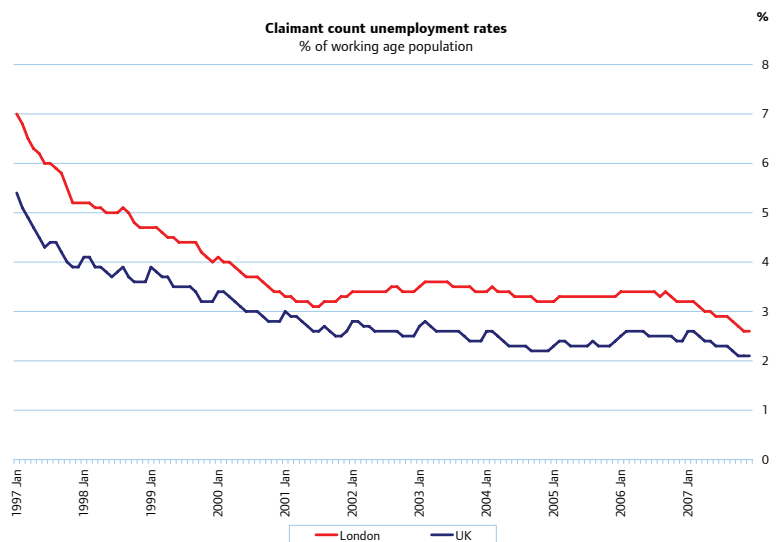
Source: Transport for London

Latest release: January 2008

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Claimant count unemployment

- The rate of claimant count unemployment (the percentage of resident working age population who are unemployed and claiming Jobseekers' Allowance) in London was 2.6% in December 2007.
- There were 131,100 unemployment claimants in London in December 2007 compared with 160,700 in December 2006.
- The claimant count unemployment rate of the UK remains below that of London.



Source: Claimant Count, NOMIS

Latest release: January 2008

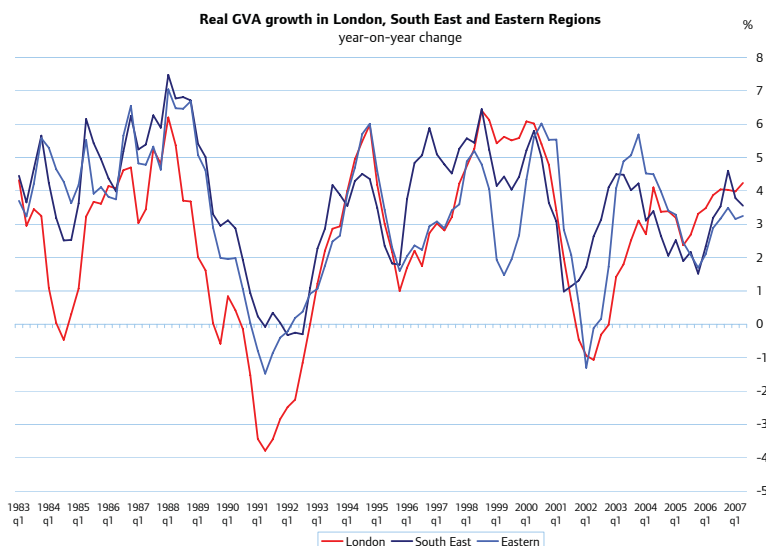
Next release: February 2008

Robust annual output growth in London in Q2 2007

- London's annual growth in output increased to 4.2% in Q2 2007 from 4.0% in Q1 2007.
- Annual output growth in the South East decreased to 3.6% in Q2 2007 from an upwardly revised 3.8% in the previous quarter.
- Annual output growth in the Eastern region increased to 3.3% in Q2 2007, from an upwardly revised 3.2% in Q1 2007.

Latest release: November 2007

Next release: February 2008

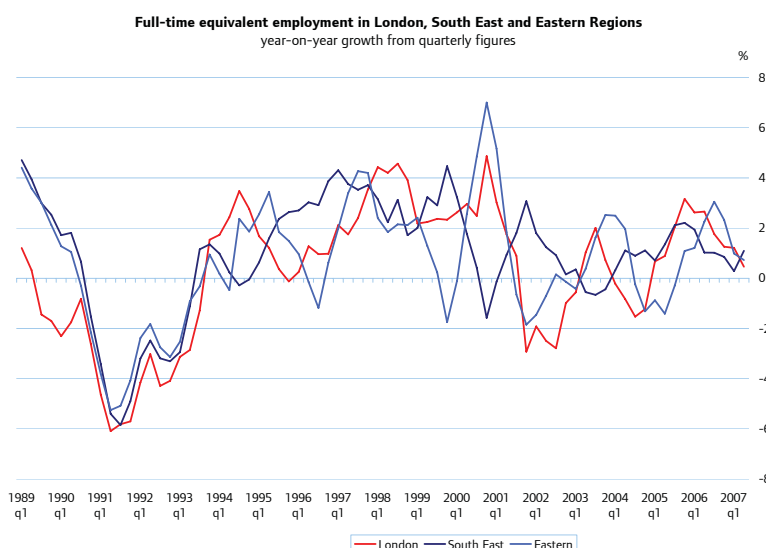


Annual employment growth in London and the surrounding regions

- London's annual employment growth decreased to 0.5% in Q2 2007 from an upwardly revised 1.2% in Q1 2007.
- Annual employment growth in the South East increased to 1.1% in Q2 2007 from an upwardly revised 0.3% in Q1 2007.
- Annual employment growth in the Eastern region was 0.7% in Q2 2007, down from 1.0% in the previous quarter.

Latest release: November 2007

Next release: February 2008

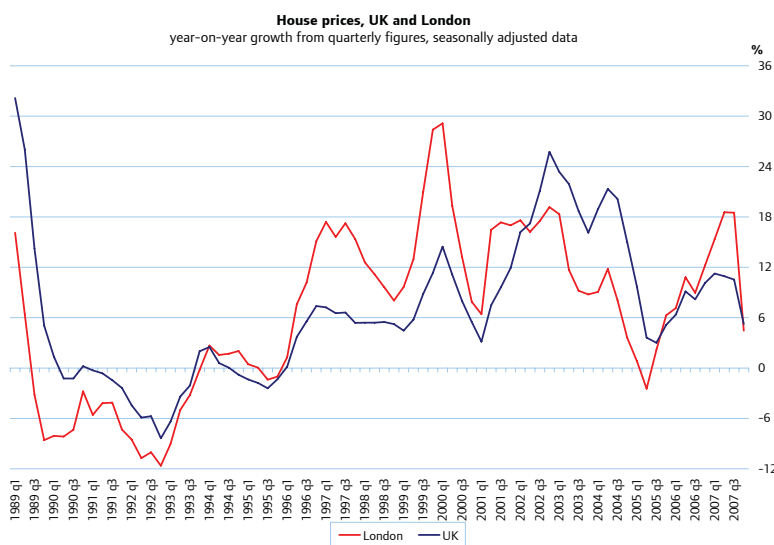


Annual house price inflation slows sharply

- Annual house price inflation, as measured by the Halifax Bank of Scotland, decreased in Q4 2007 in both London and the UK.
- Annual house price inflation in London fell substantially to 4.4% in Q4 2007 from 18.5% in Q3. Annual house price inflation in the UK decreased to 5.2% in Q4 from 10.5% in Q3.
- Annual house price inflation was lower in London than in the UK in Q4 2007 for the first time since Q3 2005.

Latest release: January 2008

Next release: April 2008

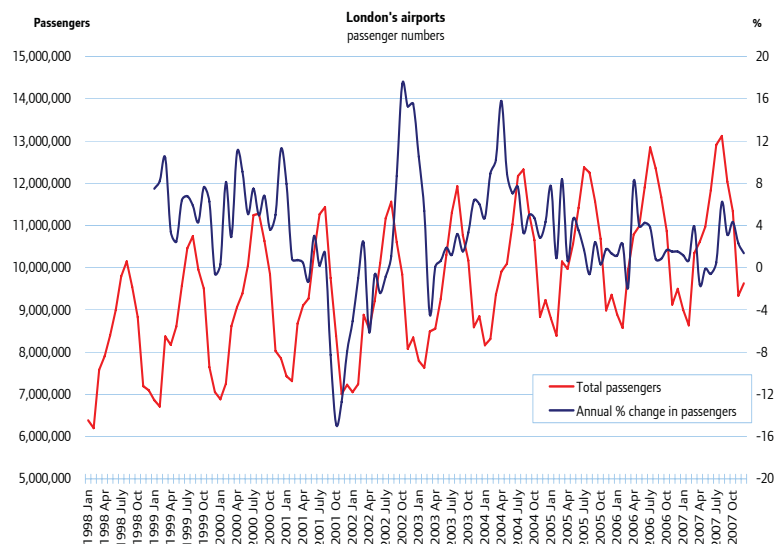


Positive annual growth in airport passenger numbers

- 9.6 million passengers travelled through London's airports in December 2007.
- The number of passengers using London's airports increased by 1.4 per cent from December 2006 to December 2007.
- The number of passengers using London's airports has risen year-on-year for the past six months.

Latest release: January 2008

Next release: February 2008



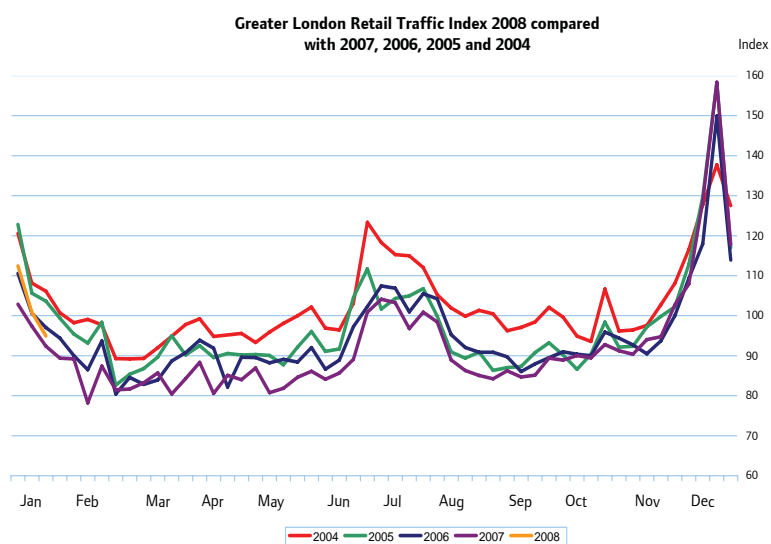
Source: Civil Aviation Authority

SPSL Retail Traffic higher over Christmas 2007

- The SPSL Retail Traffic Index of shoppers in London was 94.9 in the second full week of January compared to 100.8 in the previous week.
- The index was higher over Christmas 2007 than in the previous year. In early 2008 the index has also been greater than 2007 levels.
- SPSL's Retail Traffic Index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: Mid-January

Next release: Weekly



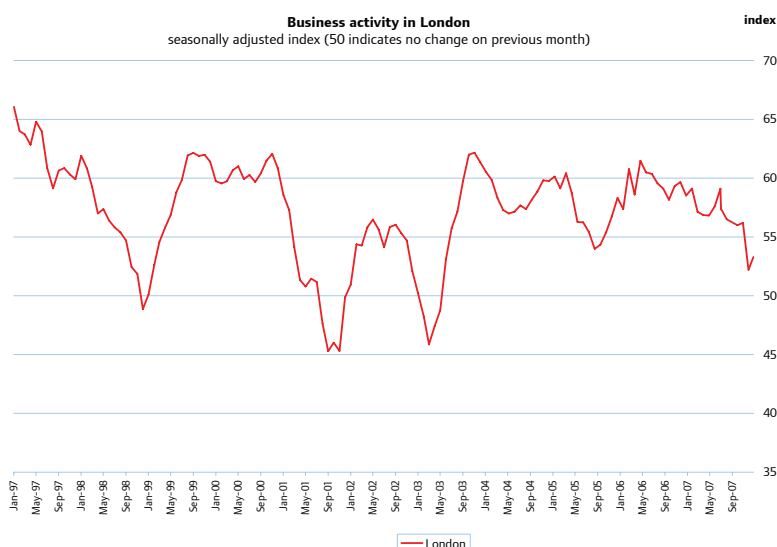
Source: SPSL

London's business activity still expanding

- London firms continued to expand their output of goods and services in December 2007.
- The Purchasing Managers' Index (PMI) of business activity recorded 53.3 in December 2007 compared to 52.2 in November.
- A rate of above 50 on the index indicates an increase in business activity from the previous month. The PMI for business activity has been above 50 since June 2003.

Latest release: January 2008

Next release: February 2008



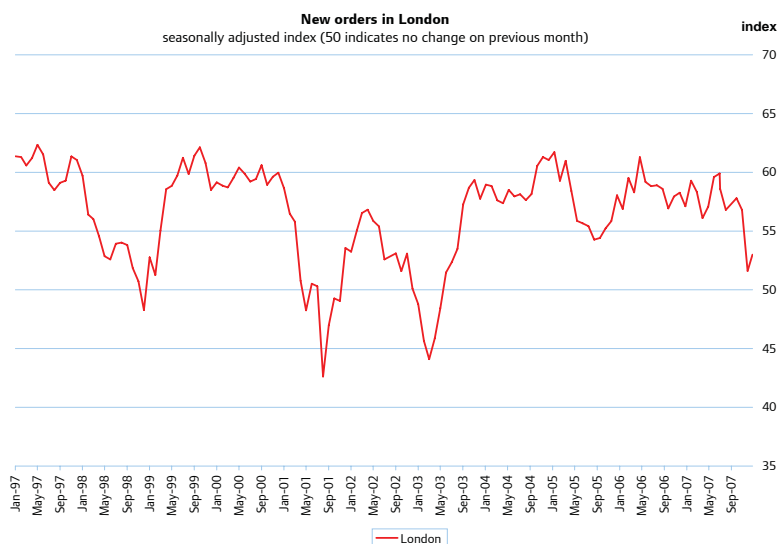
Source: The Royal Bank of Scotland /NTC Economics

New orders for London increasing slowly

- December 2007 saw growth in new orders for London firms.
- The PMI for new orders recorded 53.0 in December compared to 51.6 in November.
- A rate of above 50 on the index indicates an increase in new orders from the previous month.

Latest release: January 2008

Next release: February 2008



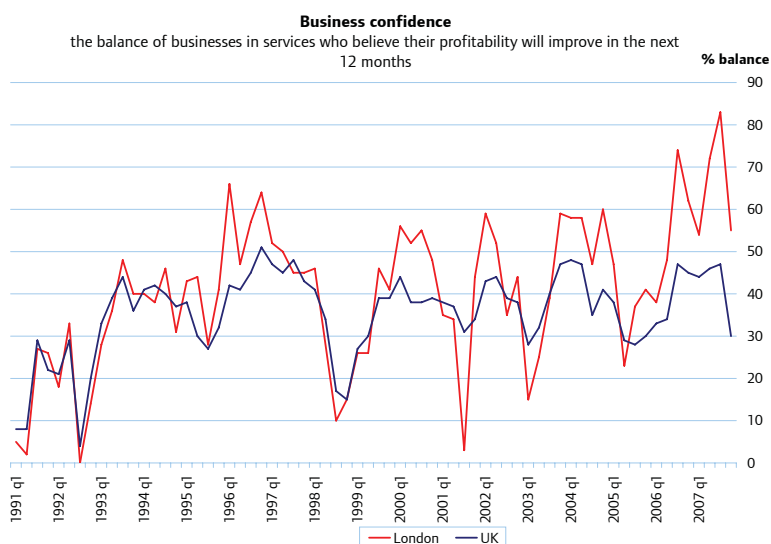
Source: The Royal Bank of Scotland /NTC Economics

Expectations of profitability remain higher in London than in the UK

- The British Chambers of Commerce's January Quarterly Economic Survey (QES) showed that London's service sector expected its profitability to improve.
- The net balance of businesses in services in London expecting to increase their profitability over the next 12 months was 55% in Q4 2007.
- The net balance of UK businesses in services expecting increased profitability over the next 12 months was 30% in Q4 2007.

Latest release: January 2008

Next release: April 2008



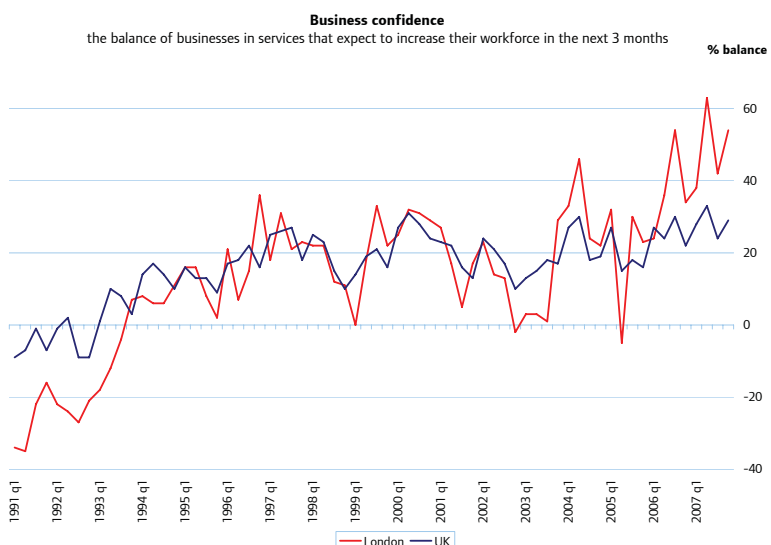
Source: British Chambers of Commerce, Quarterly Economic Survey

Employment expectations remain higher in London than in the UK

- The British Chambers of Commerce's January Quarterly Economic Survey showed that London's service sector firms expected to increase their workforce over the next three months.
- For London the net balance expecting to increase their workforce rose to 54% in Q4 2007 from 42% in Q3 2007.
- For the UK the net balance expecting to increase their workforce rose to 29% in Q4 2007 from 24% in Q3 2007.

Latest release: January 2008

Next release: April 2008



Source: British Chambers of Commerce, Quarterly Economic Survey

London Economic Development Snapshot

Katerina Angelopoulou,
Economist

The latest Snapshot report, the periodic publication that sets out the performance of London's economy against the objectives of the Mayor's Economic Development Strategy (EDS), was published this month.

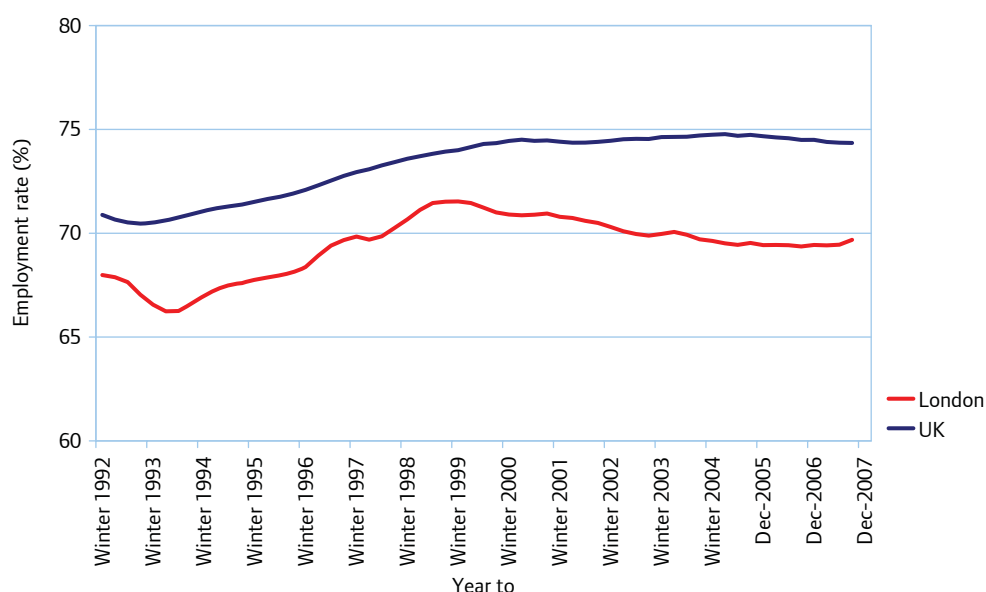
The Snapshot aims to:

- identify and review London's progress against the strategic priorities of the EDS;
- provide a basis on which to review the priorities for London's economic development; and,
- act as a catalyst for directing economic development activities in London.

The Snapshot shows that stakeholders in London's economy need to maintain their focus on London's relatively low employment rate, which particularly impacts on some disadvantaged groups and some deprived areas.

Figure 2: Employment rate in London and the UK

Source: LFS



The employment rate for London as a whole, increased slightly in the year to September 2007. However, the gap with the UK average still remains around 5 percentage points.

GLA Economics' most recent forecast (London's Economic Outlook: Autumn 2007) sees around trend employment growth over the next few years. The extent to which this closes the gap between the employment rate for London and the UK as a whole will depend on, amongst other things, the growth in London's working-age population relative to the UK as a whole and the ability of London's workless population – both the unemployed and economically inactive – to compete effectively for jobs in London's labour market.

There are however positive signs for some of the employment objectives of the EDS. For the past two years or so, the employment rate for the seven most disadvantaged boroughs of London (Camden, Hackney, Haringey, Islington, Newham, Southwark and Tower Hamlets - according to the Index of Multiple Deprivation 2004) has increased significantly, closing the gap with the London average to less than the minimum 8 percentage point gap which has existed for at least the past 15 years or so. Over the past six months, the gap has closed down even further to less than 6 percentage points.

Furthermore, whilst the employment rate for most disadvantaged groups shows little, if any, change over time, the employment rate for Black Asian and Minority Ethnic (BAME) groups shows some signs of improvement. The employment rate for the BAME groups is still well below that for the white ethnic group. Nonetheless, the difference has been reduced to below 15 percentage points for the first time since the early 1990s. Whilst this is to be welcomed, it remains to be seen whether the increase in the employment rate of the BAME group will be sustained over time.

Another area that the Snapshot highlights as requiring some attention is the household recycling rate. Whilst household recycling in London is rising, the share of household waste that is recycled is well below the England average. In 2006/07 around a third of the household waste was recycled in England compared to less than a quarter in London.

A significant change since the previous Snapshot report is the approval of the funding package for Crossrail. Crossrail is expected to benefit the London economy by improving access to jobs, increasing productivity and making London a more attractive place for businesses to locate.

For more information on the Snapshot see the LDA website:
http://www.lda.gov.uk/upload/pdf/London_Economic_Development_Snapshot_Jan_2008.pdf

Additional information

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Data sources

Tube and bus ridership
GDP/GVA growth
Tourism – overseas visitors
Tourism – domestic visitors
London airports
Business activity
Employment
Unemployment rates

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www.rbs.co.uk/pmireports
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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.

Gross domestic product (GDP)

A measure of the total economic activity in the economy.

Gross value added (GVA)

Used in the estimation of GDP. The link between GVA and GDP is that GVA plus taxes on products minus subsidies on products is equal to GDP.

ILO unemployment rate

The International Labour Organisation's calculation of the number of people out of work.

Tube ridership

Transport for London's measure of the number of passengers using London Underground in a given period. There are 13 periods in a year – twelve 28-day periods and one 29-day period. Period 1 starts at the beginning of the financial year rather than the calendar year.

Acronyms

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

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About GLA Economics

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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