London's Economy Today

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In this issue

GLAECONOMICS

Faltering housing market as mortgage loans dry up due to credit crunch

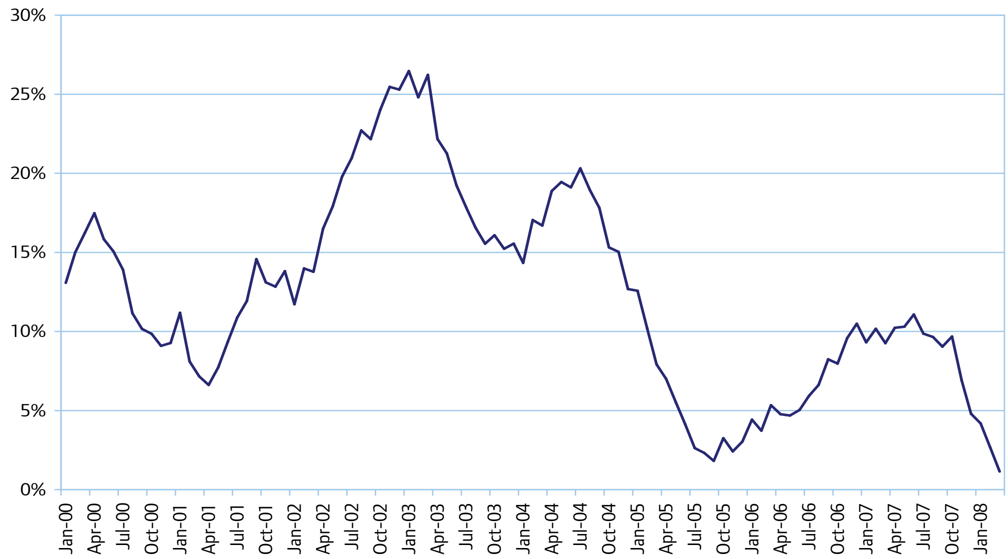
by Richard Davies, Economist and Gordon Douglass, Economist

House prices in the UK fell by 2.5 per cent in March, the biggest monthly fall since September 1992, according to the latest house price survey by HBOS. Nationwide reported that UK house prices had fallen for the fifth consecutive month in March (by 0.6 per cent.) The data from both lenders showed that the trend for annual UK house price inflation is sharply downwards but at the moment it is still just positive. Nationwide and HBOS are both now forecasting modest house price falls over the whole of 2008. However, this should be seen in the context of the high house price inflation over the past decade. On the HBOS measure, in March 1998 the average standard seasonally adjusted UK house price was £70,700, by March 2003 it had risen to £127,200 and in March 2008 it was £191,600.

Latest news...

- **The rationale for public sector intervention in the economy II.** This report examines the case for public sector intervention and provides case study examples relevant to London. Visit **www.london.gov.uk/mayor/economic_unit** to download this publication.

Figure 1: UK house price inflation, monthly year-on-year
Source: Nationwide



In its World Economic Outlook, published in April, the IMF said that it remained concerned about the UK housing market, which it believes to be 30 per cent over valued. They have said that the high levels of UK house prices are not sustainable given the current lack of affordability especially for first time buyers, increased borrowing costs and the tightening of lending criteria by banks.

The latest Royal Institute of Chartered Surveyors' (RICS) survey of the UK housing market, showed that the net balance of surveyors reporting a fall rather than a rise in house prices increased again and is now at its worse level since the survey began in 1978. London house prices declined for the fifth consecutive survey and the net price balance is at its most negative since February 2003. Demand has weakened due to concerns regarding the state of the economy and a large fall in the availability of mortgages, especially ones with low deposits. However, instructions are also weak with still a low level of forced sales. RICS believes that, "until new supply increases dramatically a significant crash remains unlikely."

Lenders tighten credit conditions further

The Bank of England's Credit Conditions Survey (Q1 2008) indicates that due to reduced risk appetite and problems raising funds in the wholesale money markets lenders have tightened lending criteria and reduced the supply of secured and unsecured credit to households. Corporate credit availability has also been reduced and the spreads on secured lending have increased. Lenders expected even worse credit conditions over the next three months. Default rates were reported to have risen and this was expected to also increase.

The Bank of England cuts interest rates again and announces £50bn scheme to improve liquidity in the banking system

On 10 April, the Bank of England's Monetary Policy Committee reduced the base interest rate for the third time in five months by 25 basis points from 5.25 to 5.0 per cent. However, despite this reduction in the base rate, the LIBOR rate at which the banks lend to each other remains stubbornly high at nearly 6 per cent, nearly 1 per cent higher than the base rate. This has caused interest rates on some mortgage products such as fixed rates and standard variable rates (SVR) to have actually increased over the last few months rather than fall. Higher mortgage costs and tighter lending criteria have been a major factor in the slow down in the housing market. Experian Business Strategies recently released data on debt balances for all outstanding mortgages, credit cards, loans and overdrafts. The data suggests that growth in lending has slowed markedly across all products and that lenders started tightening their credit criteria even before the credit crunch began in earnest in August 2007.

On 21 April the Bank of England announced a plan aimed at freeing up bank balance sheets and potentially enabling them to lend more to consumers and homebuyers. The scheme aims to improve liquidity in the banking system. Under the scheme, banks will be allowed to swap their "high quality" mortgage debts and credit card debts for Government securities. The swap will be for a period of one year and may be renewed for a total of three years. It will only apply to mortgage and credit card debts on banks' books at the end of 2007 and the swaps cannot be used to finance new lending. Usage of the scheme will depend on market conditions with initial use expected to be around £50bn.

Fewer job opportunities and lower office take-up in the City

A survey by recruitment firm Morgan McKinley found that there were 2 per cent fewer job opportunities in London's financial services industry in March compared to February, and 23 per cent less than in March 2007. Job opportunities are lower mainly due to investment banks cutting recruitment. Candidate supply has exceeded demand and the amount of time that it takes an individual to secure a job is 60 days, 11 days longer than a year ago.

There are other signs of an economic slowdown in London highlighted by the low take up of new office space in the City by banks and other financial companies. A quarterly update by Jones Lang LaSalle, showed that office take-up in the City fell by 40 per cent and by 60 per cent in Docklands in the six months to March compared with the six months previously. The City office market is now facing the first downward pressure on rents since 2004.

US economy grinding to a halt

There is continuing evidence of the deteriorating state of the US economy, as non-farm payroll employment fell by 80,000 in March. Employment losses in the first three months of 2008 have averaged 77,000 a month, leading to a rise in US unemployment to 5.1 per cent. Consumer confidence has also been badly affected. The University of Michigan's index of consumer sentiment fell to 63.2 in April from 69.5 in March. The survey found that consumers were concerned about "persistently high food and fuel prices, as well as rising unemployment". This survey has been carried out for more than 50 years and in this time there have only been a dozen surveys that have recorded a lower level of consumer sentiment than the current one.

Global economy set to slow

The IMF forecasts that UK and world growth is set to slow down in 2008 and 2009. In April, the IMF published its most recent World Economic Outlook in which it forecasts that world output growth will slow from 4.9 per cent in 2007, to 3.7 per cent in 2008 and 3.9 per cent in 2009. This is mainly due to the rapid slowdown in the US economy, which has been badly affected by the collapse of its housing market and the credit crunch. As a result, the IMF forecasts that the US will grow by just 0.5 per cent in 2008 and 0.6 per cent in 2009. The IMF believes that the UK is also very vulnerable to a severe economic downturn. The tightening of lending criteria by UK banks will adversely affect business investment and personal consumption. The IMF forecasts that UK growth will slow down from 3.1 per cent in 2007 to 1.6 per cent in 2008 and 2009.

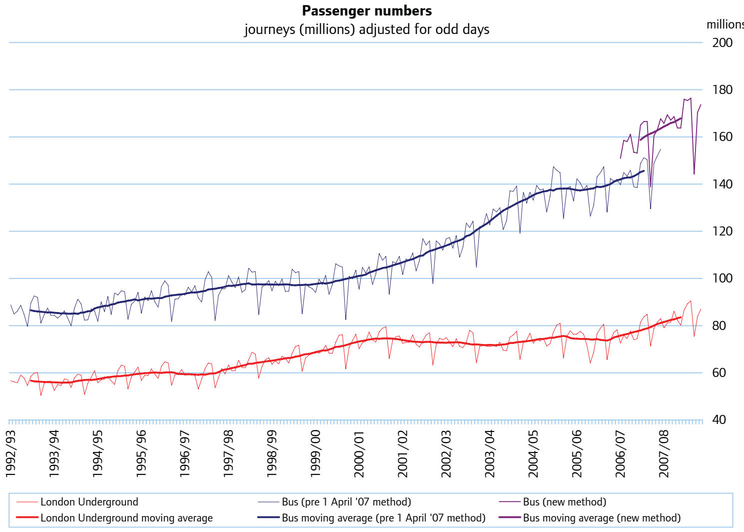
Oil prices have reached new record levels with Brent crude trading at around $115 per barrel. Although demand for oil may fall in developed countries as their economies slow down, this is likely to be offset by continued high demand for oil in emerging economies. This, supply concerns and the weak dollar are helping to keep oil prices high. With a background of a stagnating US economy, continuing financial turmoil, strong inflationary pressures and a slowing UK economy, the London economy faces difficult times. Momentum in the London economy was robust in 2007, so the sharp slow down may well not show up in official statistics until the latter part of 2008 and into 2009.

Economic indicators

Increase in moving average of passenger numbers

- The most recent 28-day period is from 3 February 2008 to 1 March 2008. London's Underground and buses had 260.7 million passenger journeys; 173.7 million by bus and 87.0 million by Underground.
- The moving average increased to 251.4 million from an upwardly revised 250.1 million passengers every period. The moving average for buses was 167.9 million. The moving average for the Underground was 83.5 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).

Latest release: April 2008
Next release: May 2008

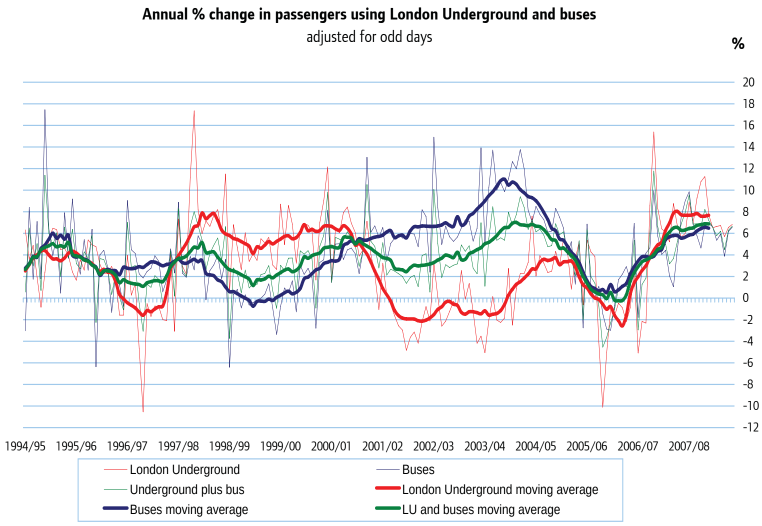


Source: Transport for London

Average annual growth rate of passengers remains constant

- The moving average annual rate of growth in passenger journeys was 6.9% (the same as the upwardly revised figure in the previous period.)
- The moving average annual rate of growth in bus passenger journey numbers decreased to 6.5% from an upwardly revised 6.6% in the previous period.
- The moving average annual rate of growth in Underground passenger journey numbers increased to 7.7% from 7.6% in the previous period.

Latest release: April 2008
Next release: May 2008

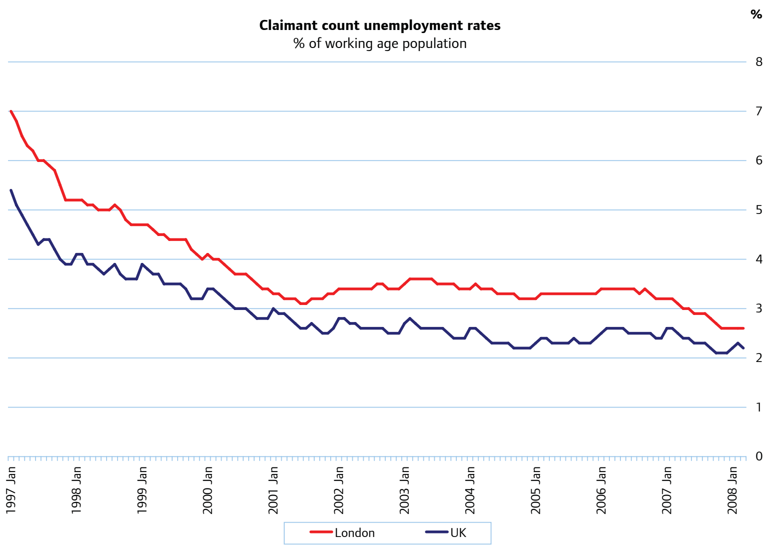


Source: Transport for London

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 March 2008.
- There were 131,900 unemployment claimants in London in March 2008 compared with 158,200 in March 2007.
- The claimant count unemployment rate of the UK remains below that of London.

Latest release: April 2008
Next release: May 2008

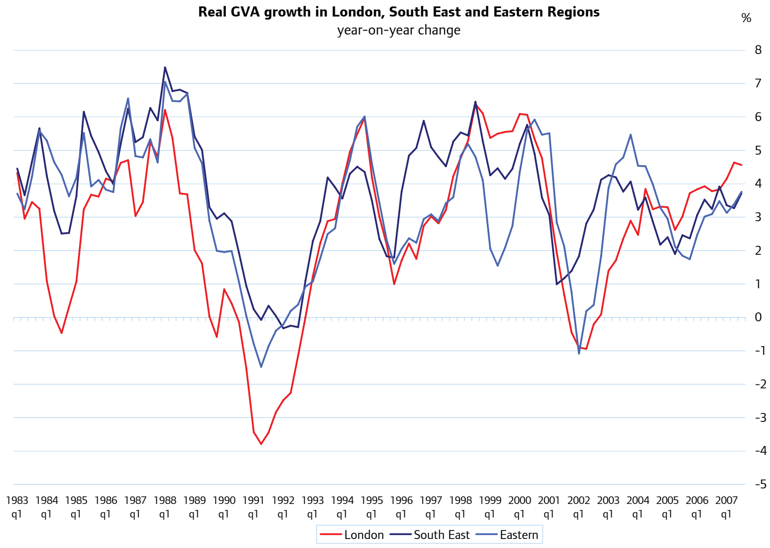


Source: Claimant Count, Nomis

Robust annual output growth in London in Q3 2007

- London's annual growth in output remained the same in Q3 2007 as the upwardly revised 4.6% in Q2 2007.
- Annual output growth in the South East increased to 3.7% in Q3 2007 from a downwardly revised 3.3% in the previous quarter.
- Annual output growth in the Eastern region increased to 3.8% in Q3 2007, from an upwardly revised 3.4% in Q2 2007.

Latest release: February 2008
Next release: May 2008

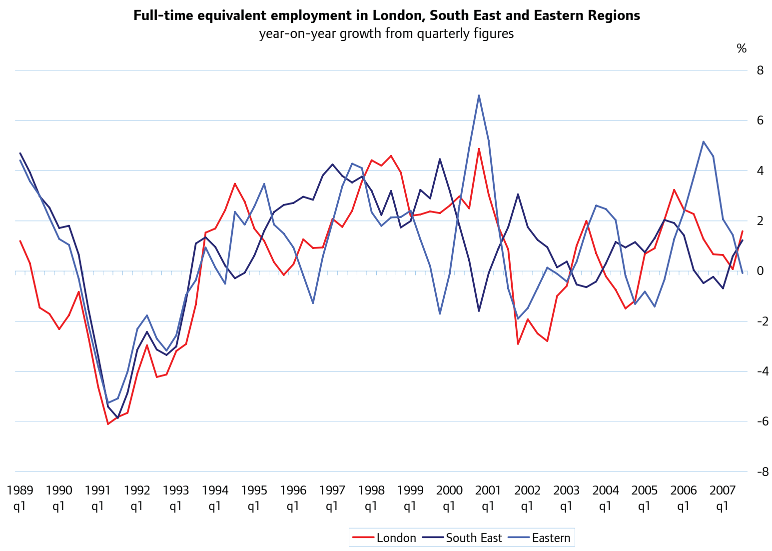


Source: Experian Business Strategies

Annual employment growth in London faster than the surrounding regions in Q3 2007

- London's annual employment growth increased to 1.6% in Q3 2007 from a downwardly revised 0.1% in Q2 2007.
- Annual employment growth in the South East increased to 1.2% in Q3 2007 from a downwardly revised 0.6% in Q2 2007.
- Annual employment growth in the Eastern region was –0.1% in Q3 2007, down from an upwardly revised 1.4% in the previous quarter.

Latest release: February 2008
Next release: May 2008

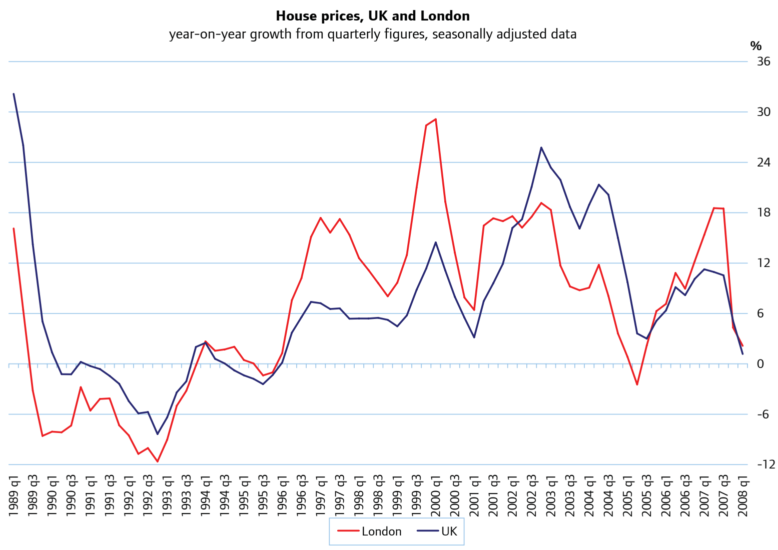


Source: Experian Business Strategies

Annual house price inflation slowing sharply

- Annual house price inflation, as measured by the Halifax Bank of Scotland, decreased in Q1 2008 in both London and the UK.
- Annual house price inflation in London fell to 2.1% in Q1 2008 from a downwardly revised 4.3% in Q4 2007. Annual house price inflation in the UK decreased to 1.2% in Q1 from a downwardly revised 5.1% in Q4 2007.
- Annual house price inflation was slightly higher in London than in the UK in Q1 2008.

Latest release: April 2008
Next release: July 2008

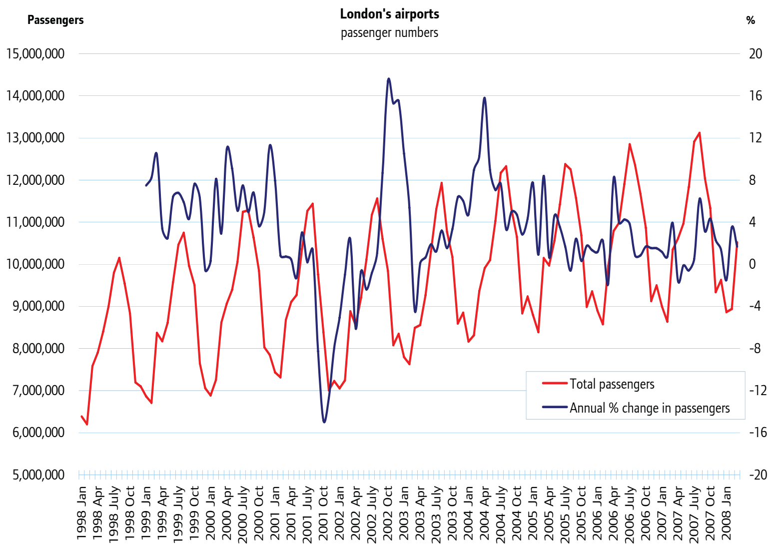


Source: HBoS

Positive annual growth in airport passenger numbers

- 10.5 million passengers travelled through London's airports in March 2008.
- The number of passengers using London's airports increased by 1.7 per cent from March 2007 to March 2008.
- The number of passengers using London's airports has risen year-on-year for the past two months.

Latest release: April 2008
Next release: May 2008

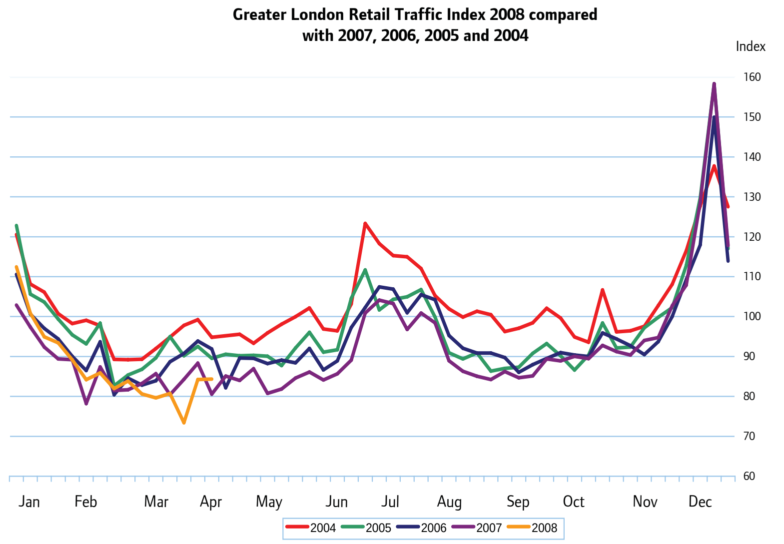


Source: Civil Aviation Authority

SPSL Retail Traffic similar to 2007 levels

- The SPSL Retail Traffic Index of shoppers in London was 84.4 in the first full week of April compared to 84.2 in the previous week.
- The index has been quite similar to 2007 levels this year.
- SPSL's Retail Traffic Index measures the number of shoppers and does not necessarily reflect the level of spending.

Latest release: Mid-April
Next release: Weekly

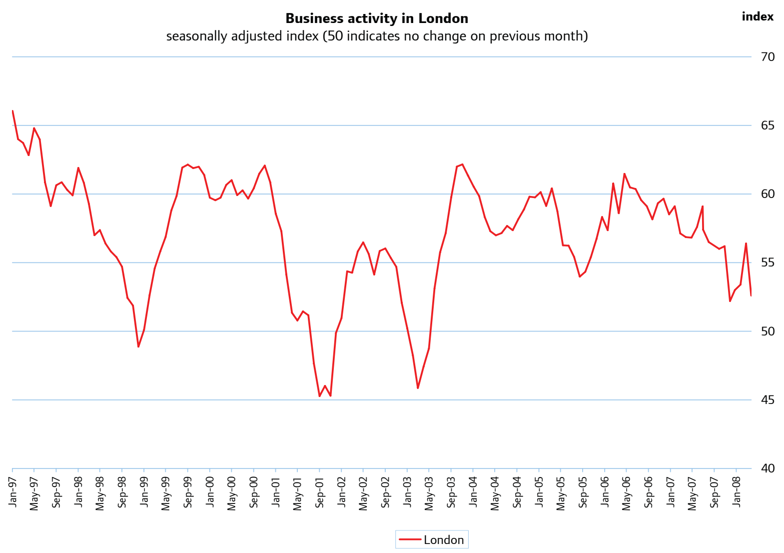


Source: SPSL

London's business activity slows down

- Output of goods and services by London firms continued to expand in March 2008, but at a slower rate than in February.
- The Purchasing Managers' Index (PMI) of business activity recorded 52.6 in March compared to 56.4 in February.
- 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: April 2008
Next release: May 2008

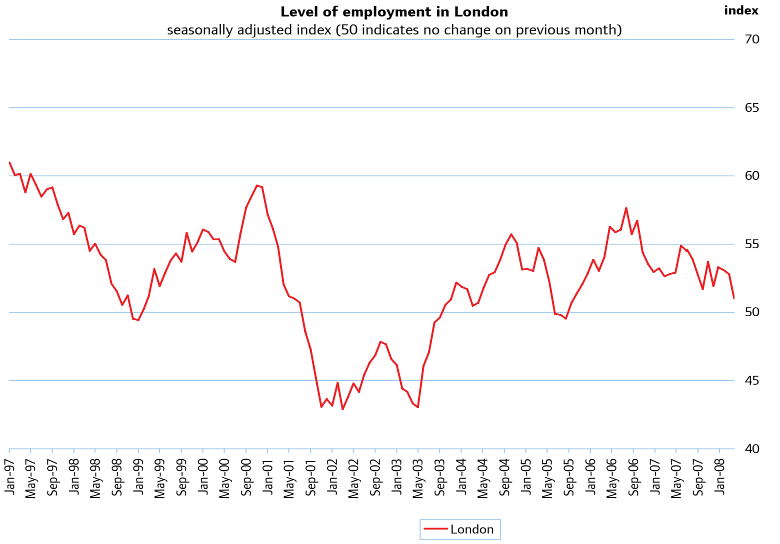


Source: The Royal Bank of Scotland/NTC Economics

Employment only just expanding in London

- London firms continued to increase their level of employment in March 2008 but at a slower rate than in February.
- The PMI for the level of employment was 51.0 in March compared to 52.8 in February.
- A rate of above 50 on the index indicates an increase in the level of employment from the previous month.

Latest release: April 2008
Next release: May 2008

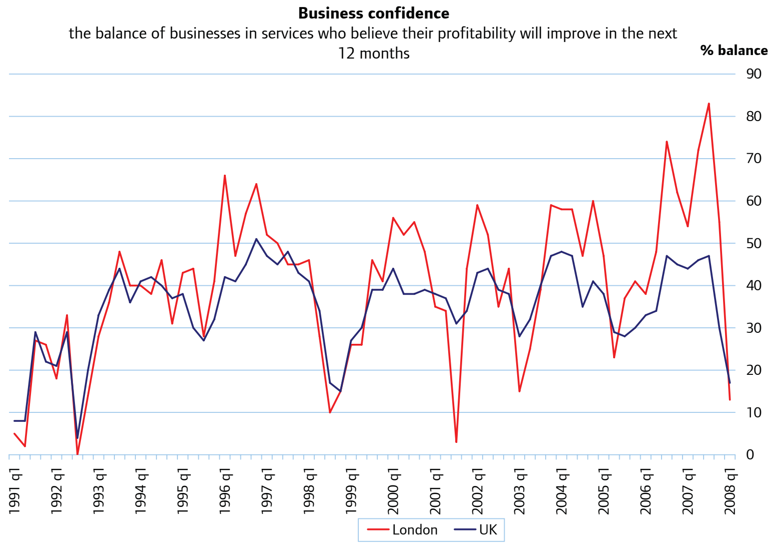


Source: The Royal Bank of Scotland/NTC Economics

Expectations of profitability in the service sector weakens sharply

- The British Chambers of Commerce's April Quarterly Economic Survey (QES) showed that overall London's service sector firms expected their profitability to improve, but the result was the weakest since Q3 2001.
- The net balance of businesses in services in London expecting to increase their profitability over the next 12 months was 13% in Q1 2008.
- The net balance of UK businesses in services expecting increased profitability over the next 12 months was 17% in Q1 2008.

Latest release: April 2008
Next release: July 2008

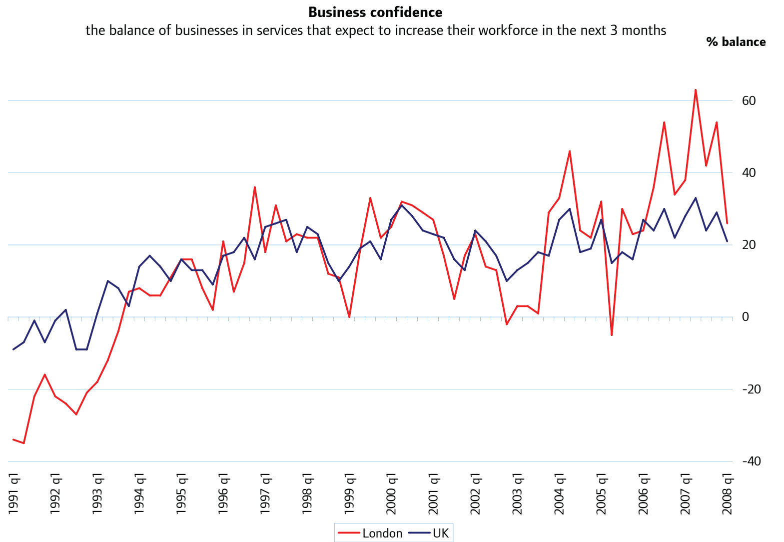


Source: British Chambers of Commerce, Quarterly Economic Survey

Employment expectations in the service sector weakens

- The British Chambers of Commerce's April Quarterly Economic Survey showed that London's service sector firms still expected to increase their workforce over the next three months.
- For London the net balance expecting to increase their workforce declined to 26% in Q1 2008 from 54% in Q4 2007.
- For the UK the net balance expecting to increase their workforce declined to 21% in Q1 2008 from 29% in Q4 2007.

Latest release: April 2008
Next release: July 2008



Source: British Chambers of Commerce, Quarterly Economic Survey

Employment in London by firm size

Richard Prothero,
Economist

GLA Economics have worked with the Office for National Statistics (ONS) to develop a new method for analysing employment data according to firm size. This article presents the key results from this analysis.

The analysis is based on data from the ONS Inter Departmental Business Register (IDBR). The IDBR can provide statistical samples at enterprise and local unit level: where the enterprise address is generally the head office and an individual site (factory, shop etc.) in an enterprise is called a local unit. Therefore, one enterprise may consist of one or many local units.

Whilst some published data on employment by firm size does exist, this has always focused on analysis of either enterprise level data or local unit level data but not both together. This new analysis provides an important advance: it is the first time that both the enterprise and local unit data from the IDBR have been combined within one methodology in order to compile a robust dataset of London employment by firm size.

Large firms are defined as those that employ more than 250 people in the UK. Figure 2 presents results for private sector employment in London showing the percentage share of London's private sector employment in each sector that is to be found within large firms. The results show that 51 per cent of London's private sector employment is to be found in large firms. This means that 49 per cent of London's private sector employment occurs within small and medium-sized enterprises (SMEs).

Figure 2: Share of private sector London employment within large firms by industrial sector

Source: Inter-Departmental Business Register, Office for National Statistics Table prepared by LDA/GLA

In addition to splitting London's private sector employment between the existing definitions of large, medium and small firms, GLA Economics' new analysis has also introduced a new definition of ultra large firms. These ultra large firms have been defined as firms that employ more than 2,500 people in the UK. Figure 2 shows that 31 per cent of all private sector employment in London occurs within these ultra large firms.

Analysing the data by sector, it can be seen that there are three industrial sectors which have a particularly high share of employment within large firms in London. These are the financial services sector (76 per cent), the transport and communications sector (73 per cent) and the retail sector (68 per cent).

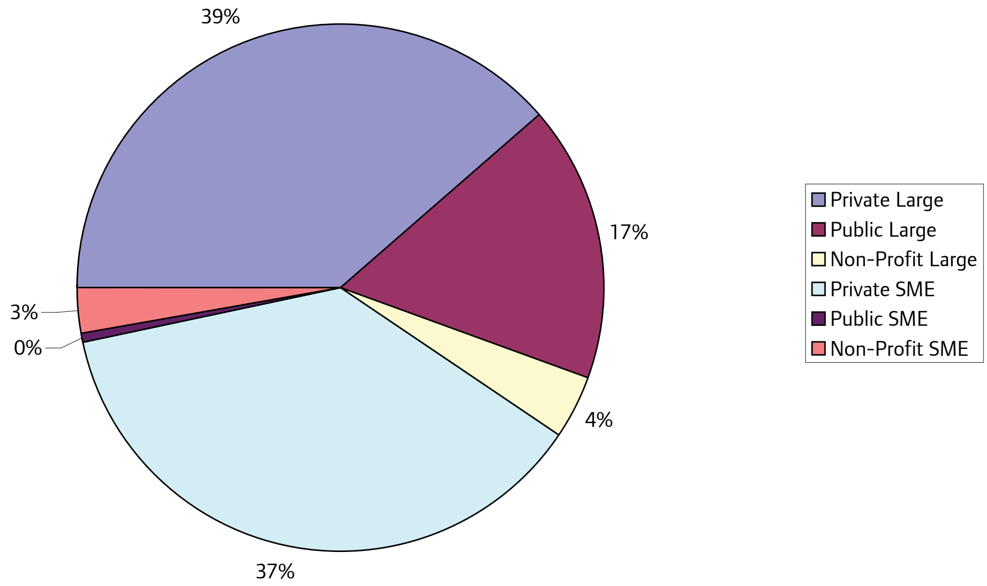
These results appear consistent with typical perceptions of the London economy. In the financial services sector there are a number of large national and multinational banks that dominate the high-street banking sector whilst the City of London also has a significant number of large multinational companies working within it. In the transport and communications sector, there are a number of major employers in the airline industry and the communications industry. Similarly, a lot of retail employment in London occurs at branches of the UK's major supermarkets or at branches of national comparison goods store chains.

In addition to data on private sector employment, data has also been analysed for public sector organisations and for non-profit organisations. This data has shown that employment in the public sector occurs almost entirely within large organisations. Thus, 97 per cent of London's public sector employment is within organisations that employ more than 250 people across the UK. In the case of the non-profit sector, 57 per cent of employment is within large organisations and 43 per cent within medium and small organisations.

The public sector employment data can be combined with the private sector data to provide a full picture of employment within London. This IDBR data shows that 76 per cent of London's employment is in the private sector, 17 per cent is in the public sector and 7 per cent is in the non-profit sector (see Figure 3). Sixty per cent of employees in London work for either a large private sector enterprise, a large public sector organisation or a large non-profit organisation.

Figure 3: London employment by firm size and private/public /non-profit status

Source: Inter-Departmental Business Register, Office for National Statistics Table prepared by LDA/GLA



A more detailed explanation of the analysis undertaken, together with further results can be found in the forthcoming (mid to late May 2008) GLA Economics publication *Working Paper 31: Employment in London by Firm Size*. Copies will be available to download from the GLA Economics website at: http://www.london.gov.uk/mayor/economic_unit/

Additional information

Data sources

Tube and bus ridership	Transport for London on 020 7222 5600 or email: enquire@tfl.gov.uk
GDP/GVA growth	Experian Business Strategies on 020 7630 5959
Tourism – overseas visitors	www.statistics.gov.uk
Tourism – domestic visitors	www.visitlondon.com
London airports	www.caa.co.uk
Business activity	www.rbs.co.uk/pmireports
Employment	www.rbs.co.uk/pmireports
House prices	www.nationwide.co.uk/hpi/
Unemployment rates	www.statistics.gov.uk

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. In 2008/09 there will be eleven 28-day periods, one 26-day period and one 31-day period. Period 1 starts on 1 April.

Bus ridership

Transport for London's measure of the number of passengers using buses in London in a given period. There are 13 periods in a year. In 2008/09 there will be eleven 28-day periods, one 26-day period and one 31-day period. Period 1 starts on 1 April.

Acronyms

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