

7. Conclusions: growth patterns in the last 25 years

The City's dynamism due mostly to international forces

The City has been one of the most dynamic parts of the British economy in the last 25 years. Its rapid growth has led to significant increases in employment and in the associated requirements for office space. The central conclusion of this study is that the dynamism of the last 25 years will continue in the next 25 years, and that plans for office and infrastructure development need to be adjusted accordingly.

A key step in the analysis has been to differentiate between City-type employment and other employment. City-type employment is in international financial services and the headquarters operations of UK financial services businesses. The "output" of these financial services' activities has risen quickly since the early 1970s, partly because of changes in the British economy, but mostly because of wider trends in the world economy.

In the British economy privatisation and financial deregulation, as well as the institutionalisation of investment and an increase in the ratio of the quoted to the unquoted parts of the corporate sector, have caused UK-focussed financial services' output to increase more rapidly than the UK's overall national output. These forces seems now to be largely played out. In particular, it seems unlikely that the ratio of the stock market's capitalisation to GDP will increase so markedly in the next 10 or 20 years as it has done since the mid-1970s.

More important and more enduring as an influence on the City's growth has been the dynamism of international financial services. Two long-run trends have been at work here. First, in most countries domestic financial services' output has grown at a higher rate than output as a whole, reflecting a well-established uniformity in the process of economic development which has been identified by Goldsmith. Secondly, international financial services' output has been increasing more rapidly than domestic financial services' output, partly because of the liberalisation of international trade and finance that has characterised the post-war world economy and partly because of the offshore revolution. (See Chapter 3 for a definition of "the offshore revolution".) With the trend growth rate of the world economy at 3% or 3 1/2% a year, domestic financial services' output may have been rising at, say, 5% to 6% a year in real terms. Since the early 1970s international financial services' output has been growing at a much higher rate, probably somewhere between 7% and 10% a year, depending on how "international financial services" are defined. (They may seem imprecise, but a very high figure is undoubtedly implied by the charts of the various business flows presented in Appendix iii.).

City-type output and employment: the main trends

An estimate of the past growth rate of "the City's output" is partly a matter of judgement, because - again - much depends on how the City is defined. A reasonable central estimate is that it has been growing at over 6% a year in real terms since the early 1970s. Broadly speaking, the increase in output is equal to the increase in

employment plus the increase in output per head, while there should be a relationship between output per head and average incomes. (Of course, the other element here is profits achieved in City activities, but these are difficult to identify and are in any case correlated with bonus payments which form part of staff remuneration.)

Chapter 4 suggested that City-type employment had been increasing typically by about 1 1/2% a year since the early 1970s. The growth was particularly rapid in the mid-1980s, but rising rents and a pause in the growth of international financial services led to a fall in City-type employment in London between 1987 and 1993. (Much of the fall seems to have been due to the relocation of UK-based financial services away from London, notably by insurance companies and by banks' back-office functions.) Rents also declined in the early 1990s, as large amounts of new space came on the market. The sharp increase in the availability of office space followed the establishment of the London Docklands Development Corporation and a more relaxed attitude towards planning consents by the key boroughs in the mid-1980s and a subsequent boom in office development. Strong employment growth resumed between 1993 and 1995, as much of the new space was taken up.

A widening earnings differential between the City and the rest of the UK

The gap between the 1 1/2% estimated annual increase in employment and the 6% annual increase in output implies a 4 1/2% a year increase in output per head. If this were the right figure, it would be higher than the national increase since the early 1970s, which has been slightly more than 2% a year. One consequence ought to be a widening differential between incomes in City-type employment and incomes in other occupations. Pay statistics in the *New Earnings Survey* provide clear confirmation that the differential has indeed been widening. The official data corroborate much anecdotal and impressionistic evidence of an increasing gap between City earnings and national average earnings. As discussed in Chapter 3, between 1968 and 1980 the earnings of non-manual males in the City were typically between 20% and 25% higher than the national average. But by 1985 the differential had reached 40% and by the end of the decade it had exceeded 60%. The differential continued to rise in the early 1990s.

The persistence of this widening in the earnings differential is important, as it is consistent with the argument that the decline in employment in these years was mainly due to the transfer of lower-value-added employment to other UK locations from the Square Mile and the surrounding boroughs. In other words, the City became increasingly specialised on high-value-added international financial services. The decline in employment was not due to the long-term boom in international financial services coming to an end. (This is not to deny that there may have been a cyclical pause in their growth.)

This summary of the City's growth patterns agrees with several items of evidence. The City Research Project found few grounds for believing that London is uncompetitive in international financial services. In fact, London's widely-acknowledged role as an innovator in the derivatives markets and the increase in its share of some key business flows (such as foreign exchange turnover) argue that the City's competitive position

may even be improving. This may seem difficult to reconcile with the disparity between the 6%-7% estimated trend growth rate of the City's output and the higher suggested trend growth rate of international financial services on a global basis. But there would be no particular problem of reconciliation if, as seems to have been the case, international financial services have been expanding their share of City output and employment (i.e., relative to UK domestic financial services).

Rising office space per head

Meanwhile the widening earnings differential between the City and the rest of the UK has been associated, very logically, with both an increase in office space per head and a marked rise in the size of the average employment unit (i.e., large employers have been replacing small employers). The increase in office space per head has been running at about 3/4% a year. Admittedly, part of this increase may have been due to companies' difficulties in finding alternative uses for over-rented accommodation in the recession of the early 1990s. The City office market has undoubtedly suffered from an increasing incidence of empty, rather than vacant, space. However, the increase in space per person is also consistent with a rise in the proportion of well-paid, higher-value-added employment, requiring more spacious accommodation. This type of employment has been gaining ground from traditional lower-valued-added employment (such as claims processing in insurance or stockbrokers' back-office work) in relatively cramped accommodation.

The rise in the size of the average employment unit has been noted in, for example, the Corporation of London's surveys of land use. It is part of two patterns of displacement. First, non-financial-services activities have left the Square Mile, while financial services' employment has expanded. Overall employment in the Square Mile has in fact fallen since the early 1970s. Secondly, within the financial services sector, large and efficient international firms with high value added per head - such as the American investment banks - have developed their businesses in the City and replaced smaller, less efficient organizations. Indeed, it is not going too far to say that many traditional employers (i.e., those predominant in the 1950s and 1960s, and usually UK-owned and serving the domestic financial services market) have been forced to leave their City location by a combination of rising rents and labour costs. The new international organizations can pay the extra costs, in many cases the older UK-based organizations cannot.

Some key statistics reconciled

Within the Square Mile City-type employment in 1995 is estimated at 195,000 City-type employment outside the Square Mile is harder to estimate, but may well have been between 50,000 and 60,000. The total of City-type employment is therefore about 250,000, compared with an estimate on the same basis of 178,000 in 1971. Total office employment in central London was of the order of 700,000 in 1995, but may over the next few years approach or even exceed 750,000. The office-based workforce is the main user of the London transport system, accounting for almost two-thirds of its daily 1.1m. transport-using journeys to work.

The size of the total central London office stock in 1995 was between 160m. sq. ft. and 190m. sq. ft., depending on the scope of the term "central London". The office stock in the Square Mile accounted for about 80m. sq. ft. and City-type employment for about 90m. sq. ft. of these totals. Both the central London office stock and the Square Mile office stock have risen substantially since the early 1970s, despite declines in total employment in both central London and the Square Mile. The divergence between the growth of the office stock and the decline in total employment reflects the increasing importance of high-value-added white-collar employment in offices, as other types of employment - in manufacturing, the utilities, crafts and printing - have contracted.

(The proportions of City-type employment to all central London office employment roughly match the proportions of City-type-occupied office space to the total central London office stock. Office space occupied by City-type employment is, first, less than the Square Mile office stock because of non-City-type employment in the Square Mile, but, secondly, larger than the Square Mile office stock because of City-type employment outside the Square Mile. Implicit in the estimate of 90m. sq. ft. occupied by City-type employment is the belief that City-type employment outside the Square Mile is higher than non-City-type employment in the Square Mile.)