

Employment opportunity for all: Analysing labour market trends in London

March 2006



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EXECUTIVE SUMMARY

Since 1997 the Government has made significant progress towards its goal of employment opportunity for all. Employment rates are now higher across the UK, and the national employment rate is close to record highs. However, the pace of improvement in different regions has varied. In particular, the employment rate in London is now among the lowest of any UK country or region. Over recent years the gap in unemployment rates between London and the rest of the UK has narrowed, while the gap in economic inactivity rates has widened. Worklessness is particularly prevalent in Inner London, where rates of child poverty are also high.

London's population differs from the rest of the country in many ways. London is home to more people with characteristics known to be associated with labour market disadvantage, and to more people with multiple barriers to work. An examination of the evidence suggests that patterns of worklessness across the country are correlated with groups prone to disadvantage in the labour market. Further analysis of the latest employment data confirms this finding, although significant unexplained differences in employment rates in London – a 'London factor' – remain once differences in population characteristics are taken into account.

In aggregate, London is highly productive, and excels in high value added activities. However, relatively low gains to work for some groups and the ease with which vacancies are filled in the capital raise questions about the operation of the London labour market. Alongside the population issues mentioned above, skills and mobility problems also appear to be key issues in explaining the emergence and persistence of relatively high rates of worklessness in the capital.

In addition, some national policy responses to unemployment and economic inactivity can be less effective in London. Policies intended to raise the financial gain to work can be less effective in London because housing costs and costs of working can be higher. The Government's active labour market policies have to cope with significant numbers of people moving into and out of work in London and a workless population with more complex needs.

The Government recognises that simply explaining the higher incidence of worklessness in London on the basis of population characteristics is not enough. The fact that some groups have poorer labour market prospects remains unacceptable, regardless of where they live. Moreover, the identification of problems for key groups, such as lone parents, may give important clues as to deeper and more general labour market issues in London.

Further work is required to confirm the implications of the analysis presented in this paper, and to clarify the objectives and tradeoffs inherent in designing policies to raise employment rates in London. The Government will consider these issues further to inform future policy.

INTRODUCTION

Summary

Since 1997 the Government has made significant progress towards its goal of employment opportunity for all. Building on foundations of macroeconomic stability and sound public finances, the Government has introduced a range of policies to support people into employment and to ensure that work pays for everyone. These measures have offered the greatest support to groups who have, historically, had low rates of employment. As a result the employment level is close to record highs.

By contrast, in London the employment rate entered a period of decline in 1999, and is now among the lowest of any UK country or region. Worklessness is particularly prevalent in Inner London, where rates of child poverty are also high.

The Government is already taking steps to address the employment situation in London, following the recommendations published in a report by the Prime Minister's Strategy Unit in 2004. The Greater London Authority and the Association of London Government have launched a commission on child poverty. Going forward, action will be required at all levels of Government and the 2007 Comprehensive Spending Review provides a basis for coordinated action to tackle the challenges facing London.

In addition to making policy recommendations, the Strategy Unit report also highlighted unanswered questions about the underlying causes of worklessness in the capital, and the effectiveness of national policy responses in the London context. This paper presents further examination of these issues, building on the work of the Strategy Unit and others to inform future policy.

1.1 In the 2005 Pre-Budget Report, the Government noted that London was the UK region with the lowest employment rate, and the only region where the employment rate was no higher than in 1997. While the most recent data shows a marginal increase in the London employment rate since 1997, the capital has seen the smallest improvement over the period, compared to other regions. The Government said that it was examining the particular labour market challenges posed by London, to inform future policymaking.

1.2 This paper is part of that process. It builds on the work of the *London Project Report*, published by the Prime Minister's Strategy Unit in 2004,¹ and is part of a wide-ranging effort across Government to address the issues that it raised. Prepared with the strategic objectives of the 2007 Comprehensive Spending Review in mind, it should also be read in conjunction with the other London-related documents published alongside Budget 2006:

- *Financial services in London: Global opportunities and challenges*; and
- *Devolving decision making 3 – Meeting the regional economic challenge: The importance of cities to economic growth*.

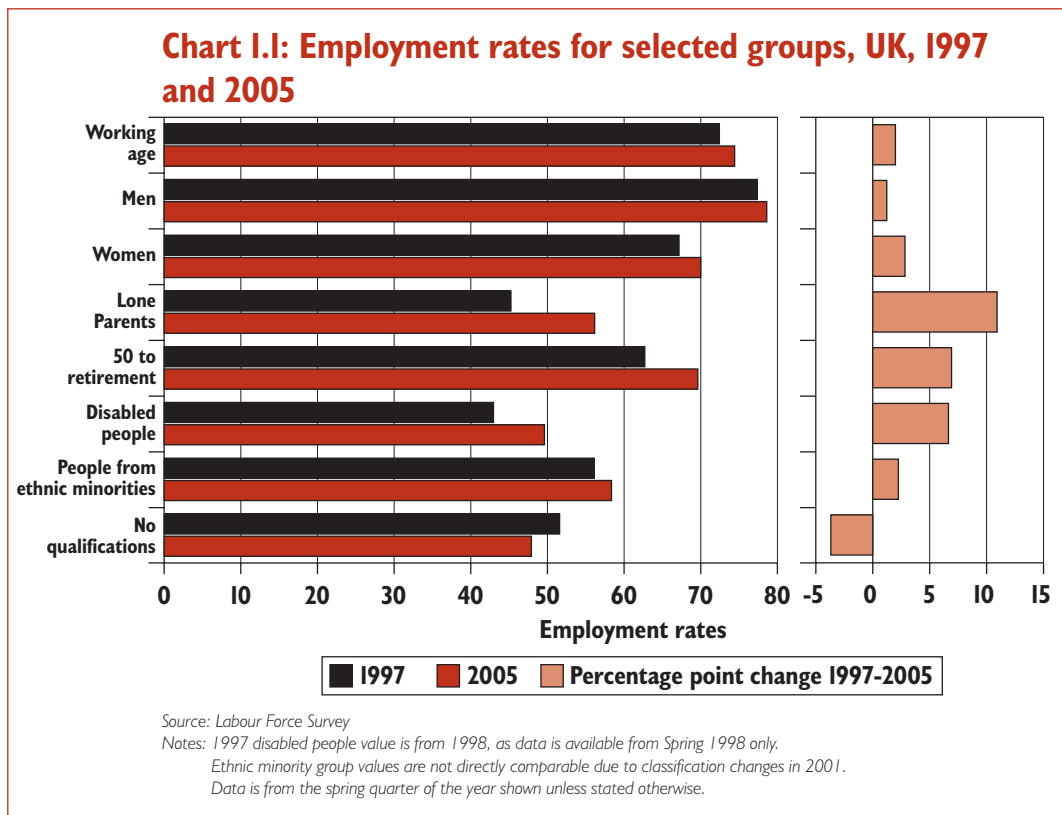
¹ *London Project Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2004

Employment opportunity for all **I.3** The Government’s long-term objective is employment opportunity for all.² This is the modern definition of full employment, and the foundation for a strong economy and a fair society. Employment opportunity for all is important both for economic growth and also for ensuring that the fruits of growth are shared widely. The Government believes that work for those who can is the best route out of poverty, and offers opportunities for independence and personal fulfilment.

I.4 Since 1997, the Government has combined employment growth with labour market stability and positive action to extend employment opportunities. A stable macroeconomic framework, sound public finances and a flexible labour market have all supported an expansion in labour demand. At the same time, labour supply has increased as the Government has ensured that basic employment rights are guaranteed; that work pays more than benefits; and that individuals are given practical assistance to move into work through active labour market programmes, assistance with the costs of working, and help developing their skills.

I.5 Over this period the labour market has performed strongly. The number of people in employment in the UK has risen by 2.4 million to 28.8 million. The employment rate for the working age population now stands at 74.5 per cent, the highest rate among the G7 countries with the exception of Canada, and close to record highs.

More support for those that need it most **I.6** Employment rates have increased most among many previously disadvantaged groups. Employment among lone parents has, for example, increased from 45 per cent in 1997 to 56 per cent today. Chart 1.1 summarises these changes.

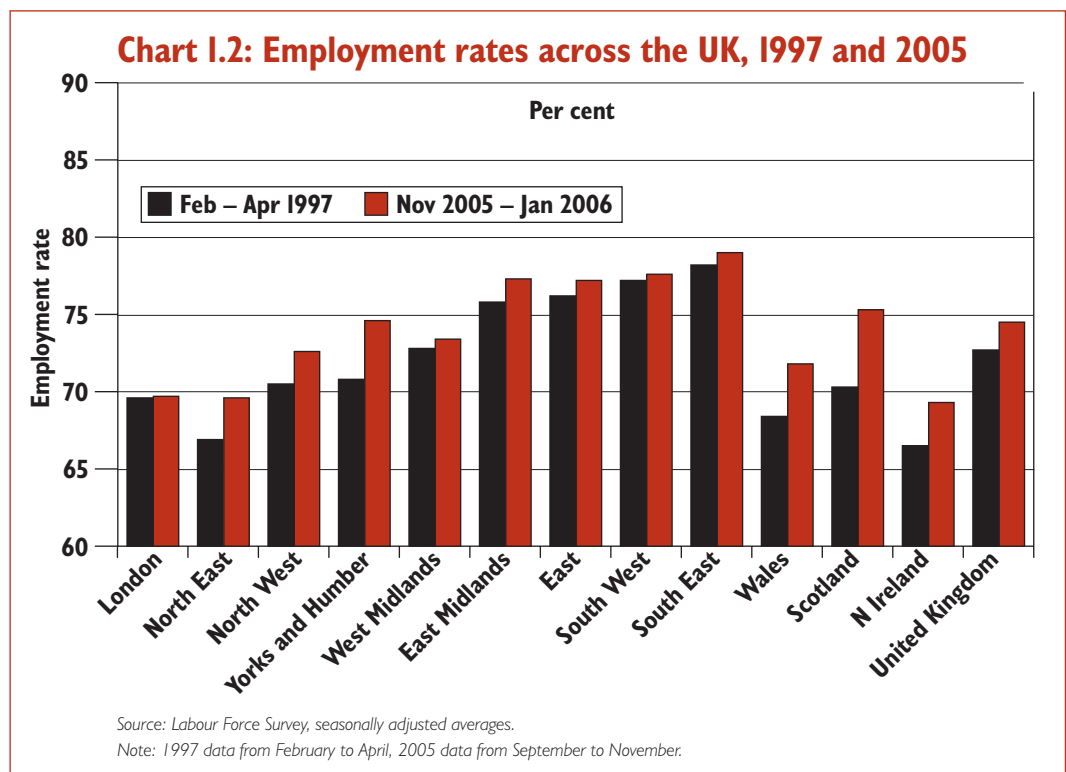


² Full employment in every region, HM Treasury, Department for Work and Pensions, December 2003

I.7 As set out in January's Welfare Reform Green Paper, *A new deal for welfare: Empowering people to work*, the Government will continue to offer greatest support to previously disadvantaged groups.³ The Government's long-term aspiration is to achieve an employment rate equivalent to 80 per cent of the working age population, with faster growth among groups with the lowest initial employment rates. Raising employment rates among many of these groups will be fundamental to meeting the Government's objective to reduce child poverty by half by 2010.

THE EMPLOYMENT CHALLENGE IN LONDON

I.8 Historically, employment rates in London have been higher than in the rest of the UK. This changed in the early 1990s. Since then employment rates in London have remained below the national average and the gap between London and the national rate is growing. The employment rate in London is now around the same level as it was in 1997, and is the lowest of any UK country or region apart from the North East.



³ *A New Deal for Welfare: Empowering people to work*, Department for Work and Pensions, January 2006

I.9 Of around 5 million residents of working age in London, around 3 and a half million are in work. Compared to the rest of the UK, employment rates in London are low, while rates of unemployment (especially long-term unemployment rates) and economic inactivity are high.⁴ On all these indicators the problem is more concentrated in Inner London than in Outer London.⁵ Table 1.1 summarises these differences.

Table 1.1: Employment, unemployment and inactivity rates in London and the rest of the UK, 2005

	Employment rate	Unemployment rate	Per cent Inactivity rate
London	69	8	25
Inner London	64	9	30
Outer London	72	7	22
Rest of UK	75	5	21

Source: Labour Force Survey, Autumn 2005.

Notes: Rest of UK defined as all UK countries and Government Office Regions excluding London.

I.10 Around 4.6 million jobs are located in the Greater London area, more than in any other region and a high ratio of jobs to residents. Since the early 1990s, London has created new jobs at an average rate of 70,000 each year. However, population change and commuting into London from surrounding regions means that this has made little difference to the gap in employment rates, which has widened to around 6 percentage points compared to the rest of the UK (see Table 1.1).

The London paradox

I.11 These changes and trends symbolise the paradox in London's employment performance. Less than a quarter of a century ago London was a city in decline, with a falling population and industry leaving, but with employment rates above national levels. Now London is a city transformed. Once again growing and thriving, its economic vibrancy and cultural and social diversity have made it a magnet for new business and for domestic and international migrants, fully justifying and strengthening its historic identity as one of only a few truly 'global' cities. But in the process of change the economic benefits of London's resurgence have not been shared evenly among the resident population. Compared to the rest of the country, employment rates are lower, household incomes are more polarised, and child poverty rates are among the highest in the country at 24 per cent (and reaching 35 per cent in Inner London), compared to 19 per cent for Great Britain as a whole.⁶

⁴ The following definitions are used throughout this document. The **employment rate** is the proportion of the working age population in employment (including self-employment). The working age population includes women aged 16 to 59 and men aged 16 to 64. The **unemployment rate** is the proportion of the active population (employed and unemployed) unemployed. This is the International Labour Organisation (ILO) definition of unemployment. The **inactivity rate** is the proportion of the working-age population who are neither employed or ILO unemployed. The **worklessness rate** is the proportion of the working-age population who are either unemployed or economically inactive.

⁵ Inner London includes the boroughs of Camden, Hackney, Hammersmith and Fulham, Haringey, Islington, Kensington and Chelsea, Lambeth, Lewisham, Newham, Southwark, Tower Hamlets, Wandsworth, the City of Westminster and the City of London. Outer London includes the boroughs of Barking and Dagenham, Barnet, Bexley, Brent, Bromley, Croydon, Ealing, Enfield, Greenwich, Harrow, Havering, Hillingdon, Hounslow, Kingston upon Thames, Merton, Redbridge, Richmond upon Thames, Sutton, and Waltham Forest. See map in Annex

⁶ *Households Below Average Income, 2004/05*, Department for Work and Pensions, 2006. Figures refer to average rates over a three year period from 2002-03 to 2004-05.

Child poverty I.12 Higher child poverty rates in London are driven by a range of factors, many of which are beyond the scope of this paper. However it is clear that labour market factors are central to any explanation. But much more important for child poverty rates are differences in access to employment, manifested in London by lower employment rates. The relationship between worklessness and high rates of child poverty becomes clearer when considered at the household level. One in four London children (26 per cent) are being raised in households where no one works. Some 19 per cent of London children are being raised in households headed by lone parents who are not working. This compares to figures of 18 and 12 per cent respectively in the rest of Great Britain.⁷

THE POLICY CONTEXT

I.13 The Government has acted to build on London's success, by establishing and devolving considerable powers to a new Greater London Authority (GLA), with a single executive Mayor chosen directly by the people of London and an Assembly that provides the necessary checks and balances to further strengthen accountability. The Government will grant further strategic and delivery responsibilities to the GLA in the Spring. Working with the GLA, the London Development Agency (LDA) and other relevant partners, the challenge for the Government is to support and encourage London's vibrant economy, while combining it with opportunity for all. This means harnessing London's strengths for its resident population, and taking full advantage of unique opportunities such as the hosting the Olympic and Paralympic Games in 2012. Achieving this will require co-ordinated efforts from all levels of government and beyond.

I.14 A lot is already happening. The Strategy Unit's *London Project Report* has provided a focus for combined efforts by central government and the Mayor on a range of issues facing the capital, including the labour market, and a programme of work will be set out shortly to enhance the delivery of public services in the capital.

I.15 In Budget 2005, the Chancellor accepted the recommendations in the National Employment Panel report *Enterprising People, Enterprising Places*. The resulting actions, to help ethnic minority groups fulfil their employment and enterprise potential in the UK's cities are of particular significance for London.⁸

I.16 January's Welfare Reform Green Paper acknowledged that the few areas in the UK where employment rates were below the European Union average were mostly in cities. The Green Paper proposes a city strategy built around a new institutional architecture of local area consortia – including local authorities, employers, Jobcentre Plus and other local partners – to co-ordinate efforts to improve local economies and raise local employment rates.⁹

⁷ HM Treasury analysis of *Family Resources Survey*, 2004/05, Department for Work and Pensions, 2006.

⁸ *Enterprising People, Enterprising Places: Measures to Increase Ethnic Minority Employment and Business Growth*, National Employment Panel, May 2005

⁹ *A new deal for welfare: Empowering people to work*, Department for Work and Pensions, January 2006

I.17 In addition, the GLA and the Association of London Government have made clear their intention to tackle child poverty in the capital with last month's launch of the London Child Poverty Commission. The task of the Commission is to investigate the reasons behind high child poverty levels in London, and to identify policy solutions. The Government warmly welcomes the launch of the Commission, and looks forward to considering the proposals it develops. Also, the Government is currently consulting on the scope for devolving the strategic and delivery responsibilities for skills in London from the Learning and Skills Councils to the GLA.

I.18 The 2007 Comprehensive Spending Review (CSR) offers an opportunity for further strategic co-ordination to extend employment opportunities in London. This paper informs and contributes to the CSR process.

THE APPROACH IN THIS PAPER

I.19 This paper builds on previous work across government concerning employment in London and, in particular, on the work of the Prime Minister's Strategy Unit. The *London Project Report* made a number of recommendations for immediate actions that the Government might take to raise employment levels in London. The Government has already acted on many of these. For example:

- the report highlighted the impact that high childcare costs in the capital were having on work incentives for some people in London, and recommended action to make childcare more affordable. The Government's Ten Year Strategy for Childcare, published in December 2004,¹⁰ increased the support available to those on low incomes facing high childcare costs – a step of particular benefit to Londoners. The Government also allocated £11 million for work with the GLA and London Development Agency to pilot innovative approaches to improving childcare affordability in London;
- the report noted problems with Housing Benefit administration in London and recommended changes to improve the stability of transitions into work. The Government has since initiated a comprehensive reform programme to address the complexity of the current system, which has already led to improvements in delivery. The Government is also making progress with structural reform of Housing Benefit, including piloting a new Local Housing Allowance; and
- the report identified problems with the provision of language training for speakers of other languages in London and recommended the development of a coherent strategy. The Government will shortly implement a three year action plan to address the training needs of Londoners who do not speak English as a first language, to benefit both those seeking work and those already in employment.

I.20 *The London Project Report* also raised a number of important questions about the underlying reasons for lower employment rates in London. The report proposed two main areas for further investigation, relating to the particular impacts on employment rates resulting from:

- the characteristics of London's population; and
- the operation of the London labour market.

¹⁰ *Choice for parents, the best start for children: a ten year strategy for childcare*, HM Treasury, December 2004.

I.21 In addition, the Strategy Unit raised questions about the effectiveness of existing national policy responses in the London context.

I.22 This paper explores these issues in more depth, setting out the implications for policy where possible and raising further questions where necessary. Chapter 2 sets out the problem of lower employment rates in London. Chapter 3 examines how far differences in the population of London compared to the rest of the UK can explain differences in the employment rates observed, and considers findings from existing research as well as HM Treasury analysis. Chapter 4 analyses the operation of the London labour market. It examines the effects of industrial change on employment opportunities for Londoners, and the impact of any labour market imperfections. Chapter 5 looks at the effectiveness of existing national policies in the London context. Finally, Chapter 6 summarises the paper's main findings, and considers the emerging policy implications and the issues for further consideration.

2

WORK AND WORKLESSNESS IN LONDON

Summary

For much of the last century, the proportion of people in employment in London was higher than in other parts of the country. London's relative position declined in the early 1990s, however, and a persistent gap has since emerged between the capital and other regions. London now has one of the lowest employment rates of any country or region in the UK, and is the region with the smallest improvement in employment rates compared with 1997.

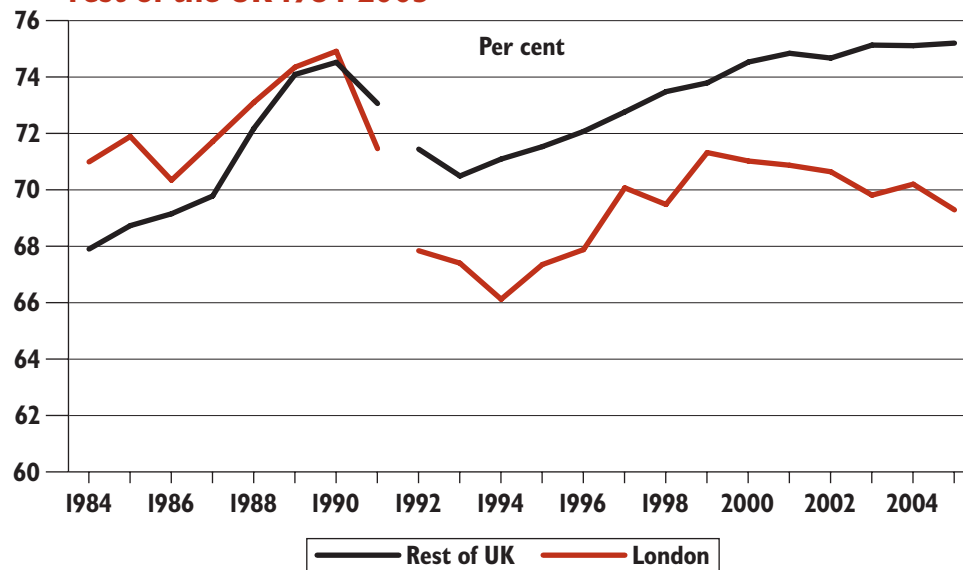
Over recent years the gap in unemployment rates between London and the rest of the UK has narrowed, although the average duration of Jobseeker's Allowance claims remains longer in the capital. Meanwhile the gap in economic inactivity rates has widened. Part of London's higher inactivity results from the city's large student population. However, there are proportionately fewer Incapacity Benefit claimants in the capital.

Compared to the overall London population, homeowners and the highly qualified are more likely to be employed. Women are less likely to be in work, and lone parents are much more likely to be economically inactive. Employment rates are also low for people born overseas and for those from ethnic minority groups. These differences are more acute for certain groups, and are especially concentrated in Inner London. Housing tenure may also be relevant. Employment rates tend to be lower for people living in social housing, and a relatively high proportion of Londoners live in social housing.

Compared to the rest of the UK, worklessness in London is particularly high among parents, lone parents, and those with low-medium skill levels. Moreover, part-time working is less common in London, and there are more households with one or more working-age members not in employment.

2.1 Over the past century, employment rates in London outperformed those in other parts of the country. During the latter half of the 1980s, the average employment rate in London was 72 per cent, 1.7 percentage points higher than that in the rest of the UK. The employment rate in London first fell behind that of the rest of the UK in the early 1990s. This situation has persisted over recent years.

Chart 2.1: Working age employment rates, London and the rest of the UK 1984-2005



Source: Office for National Statistics, Labour Force Survey, annuals 1984-1991 (using usual region of residence), and spring quarters 1992-2005 (using Government Office Regions).
 Note: Where available, regional data throughout this document is based on Government Office Regions. This data series is not available before 1992.

2.2 The relatively low employment rate among Londoners has developed against a backdrop of changes in London's social and economic composition. For example, the disparity in London's employment rate occurred at the same time as the city's population grew rapidly, at an average of 0.7 per cent per year between 1993 and 2003.¹ In contrast, the population in the rest of the UK grew at an average of 0.2 per cent per year over the same period.

2.3 London's lower employment rate has also persisted despite a significant increase in the number of jobs located in the capital. The total number of jobs in the workforce in London is around 4.6 million. Since the mid 1990s, new jobs have been created at an average rate of 70,000 every year. But despite this growth in jobs, current employment rates in London are only marginally higher than in 1997. Today, of London's 7.4 million residents, around 5 million are of working age but only 3 and a half million are in employment.

Part-time work 2.4 London also exhibits a different pattern of part-time working compared to other parts of the country. The proportion of individuals working fewer than 30 hours per week is significantly lower in London, suggesting that the distribution of work in London is more polarised between those working full time and those not working at all. This applies particularly to lone parents, who are less likely to work part time in London than elsewhere.² Only 41 per cent of employed lone parents in London work less than 30 hours, compared with 50 per cent of employed lone parents nationally. This gap reflects the increase in part-time working among lone parents outside of London.

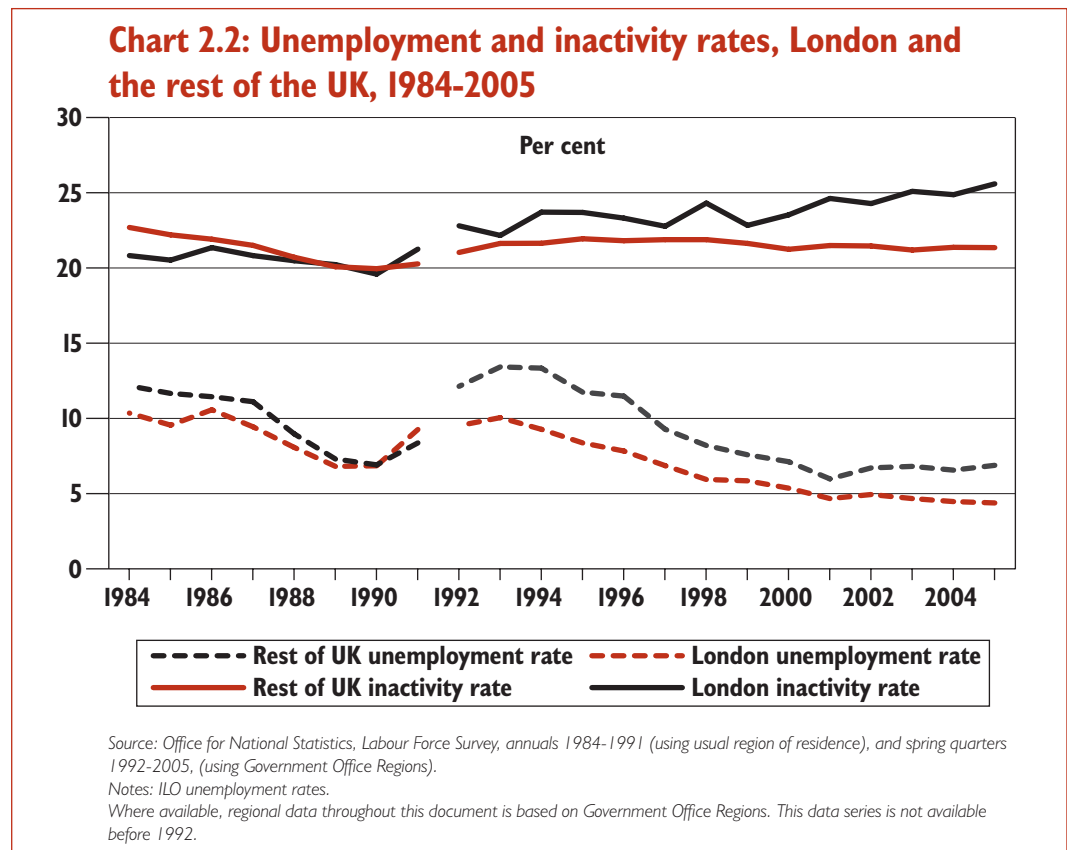
2.5 In order to understand why London's employment rate is comparatively low, it is necessary to look at the composition of worklessness in the capital and examine the trends in unemployment and inactivity.

¹ *Sustaining Success – Developing London's Economy*, London Development Agency (2005).

² *Lone Parents in London: Quantitative analysis of differences in paid work*, DWP In-house Report 136 (2004) McKay, S.

WORKLESSNESS IN LONDON

2.6 The two types of worklessness – unemployment and economic inactivity - are persistently higher in London than in the rest of the country. Chart 2.2 compares rates of unemployment and economic inactivity in London and the rest of the country over recent decades. As already noted, London’s relative position deteriorated in the early 1990s. Since the mid 1990s the gap in unemployment rates between London and the rest of the UK has narrowed slightly, but the economic inactivity gap has continued to widen.

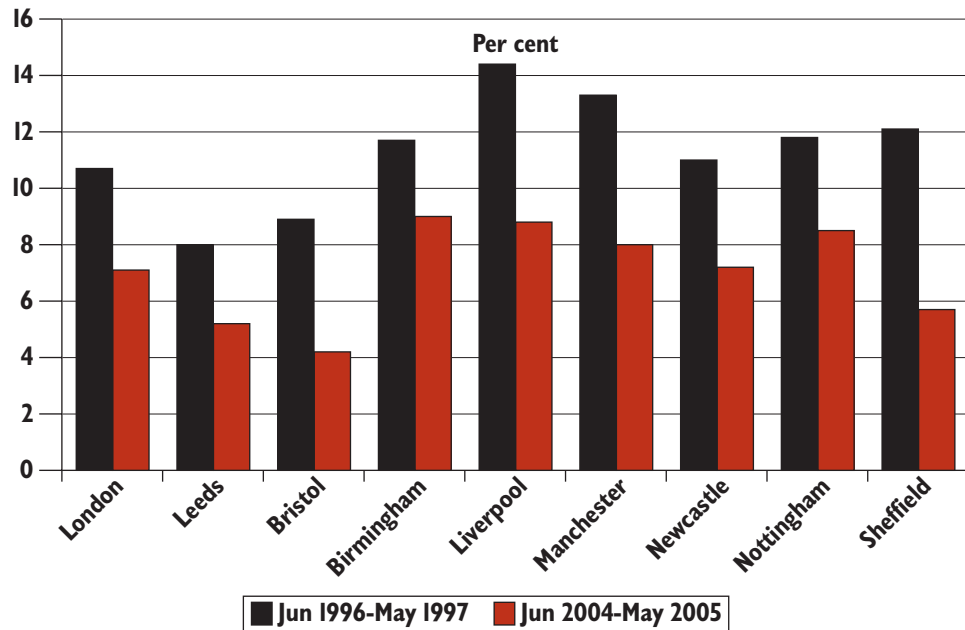


Unemployment

2.7 Unemployment statistics measure the number of people out of work but seeking employment. The standard measure of unemployment is defined by the ILO as all those actively seeking work and able to take up employment within two weeks. On this definition, the most recent data shows 281,000 unemployed Londoners. This is equivalent to 7.2 per cent of the working age population, and compares to an average rate of just 4.8 per cent in the rest of the UK.

2.8 Although London’s unemployment rate compares unfavourably to that of other UK regions and to the rest of the UK as a whole, a comparison with other urban areas over the last eight years shows that London has seen a broadly equivalent fall in unemployment. Currently, the unemployment rate in London is lower than in Birmingham, Liverpool, Manchester, Newcastle and Nottingham, although higher than in Leeds, Bristol and Sheffield. However, these comparisons need to be treated with caution as the relationship between the administrative and labour market boundaries varies between cities.

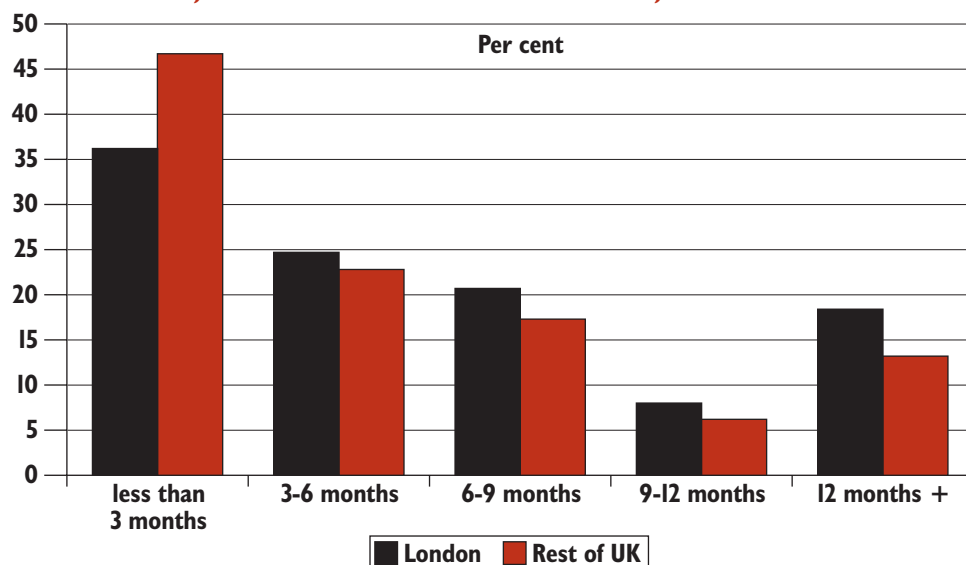
Chart 2.3: Unemployment rates in London and other English cities, 1997 and 2005



Source: Office for National Statistics, (Nomis).

Claimant count 2.9 The most recent data shows that 168,000 Londoners are currently claiming Jobseeker's Allowance, which is 18.3 per cent of all Jobseeker's Allowance claims nationally. The performance of Jobcentre Plus and labour market programmes in London is discussed further in Chapter 5.

Chart 2.4: Distribution of Jobseeker's Allowance claimants by duration, London and the rest of the UK, 2005



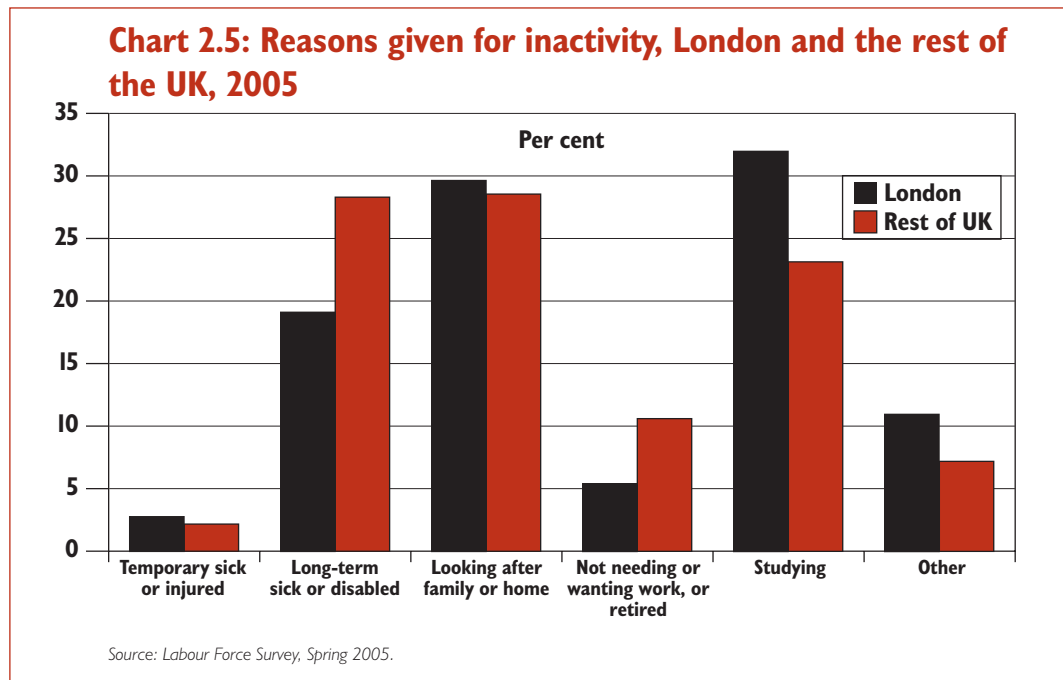
Source: Office for National Statistics, (Nomis), claimant count.

Length of Jobseeker's Allowance claim **2.10** London also appears to have a higher incidence of long-term Jobseeker's Allowance claims. Chart 2.4 shows that 18 per cent of unemployed Londoners have been claiming Jobseeker's Allowance for 12 months or more, compared to around 13 per cent in the rest of the UK.

Economic inactivity

2.11 As in the UK as a whole, the majority of workless Londoners are economically inactive rather than as unemployed. Economically inactive individuals are those members of the working age population who are out of work but not actively seeking employment. Recent data shows a total of 1.24 million inactive Londoners of working age. This is equivalent to 24.8 per cent of the working age population, compared to an average inactivity rate of 2.9 per cent in the rest of the UK.

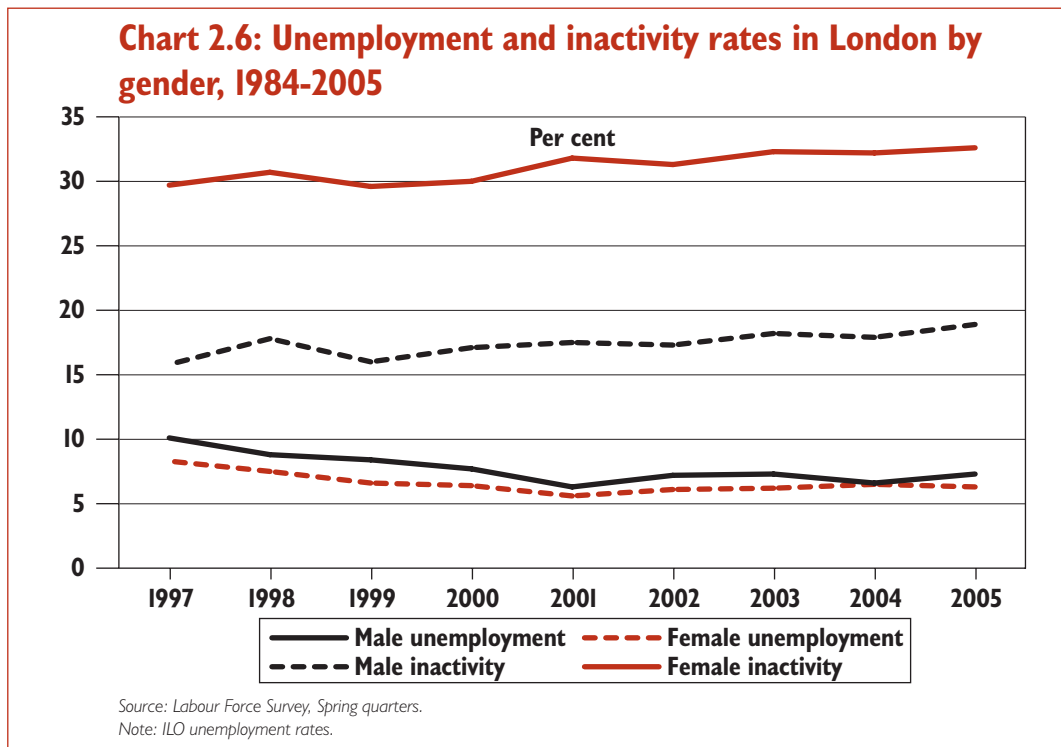
2.12 Individuals may be classed as inactive for a variety of reasons, for example looking after relatives or having a long-term illness. Chart 2.5 suggests the reasons for inactivity in London are distributed differently to those in the rest of the country.



Students **2.13** In particular, over 330,000 working age economically inactive Londoners are in full time education. This is not surprising given London's status as a global centre for higher education and learning. Adjusting the inactivity figures for London to exclude the student population reduces the incidence of inactivity from 25.3 per cent to 18.9 per cent. This goes a considerable way towards narrowing the gap in economic activity rates between London and the rest of the UK, where the inactivity rate excluding students is 17.0 per cent. Inactivity rates excluding students in London have been broadly flat over the last decade, at 19.1 per cent in 1994 and 18.9 per cent in 2005. Overall inactivity rates have gone from 23.7 per cent in 1994 to 25.3 per cent in 2005, suggesting that the rise in inactivity in London in recent years has been driven largely by increases in the number of students.

2.14 The other noticeable differences in the pattern of inactivity between London and the rest of the UK are that inactive Londoners are less likely to be long-term sick or disabled, and less likely to fall in the category 'not needing or not wanting work, or retired'. Some differences may be due in part to London's younger population profile.

Gender 2.15 Chart 2.6 tracks the pattern of unemployment and inactivity among men and women in London over recent decades. It shows that the rate of economic inactivity among women in London has remained high since the early 1990s. This is in contrast to the position in the rest of the country, where relative labour market outcomes for women have improved steadily. Male inactivity has also increased in London over the period. Male and female unemployment rates in London are, however, much more closely aligned.



CHARACTERISTICS OF WORKING AND WORKLESS LONDONERS

2.16 To better understand these trends it is helpful to consider both the differences between London's working and workless populations, and also how these compare with the situation in the country as a whole. The following sections present some headline comparisons to illustrate the complexity of employment and worklessness in the capital. Chapter 3 develops these further, by analysing worklessness while taking London's different population characteristics into account.

2.17 Table 2.1 focuses on the characteristics of those who are in work and those who are out of work, which differ in a number of important ways, by comparing the rates of employment and worklessness in London by various subsets of the working-age population.

Table 2.1: Work and worklessness by selected characteristics, London, 2005

	Employed	Workless	of which Unemployed	Inactive	Studying	Share in working-age population
All working-age Londoners	68.9	31.1	5.8	18.9	6.4	100.0
Men	74.7	25.3	6.6	11.3	7.3	48.6
Women	62.6	37.4	5.0	23.8	8.6	51.4
Black or minority ethnic	56.6	43.4	8.6	22.3	12.6	33.8
White	75.2	24.8	4.5	14.9	5.5	66.2
Born in the UK	72.4	27.7	5.4	14.4	7.9	62.8
Born abroad	63.0	37.0	6.7	22.4	7.9	37.2
Parents (including lone parents)	72.3	27.7	5.1	20.5	2.2	45.8
Lone parents	43.3	56.7	5.8	45.6	5.3	6.1
Aged 50 or over	69.9	30.1	3.4	26.4	0.3	19.3
High skill (NVQ4+)	85.8	14.2	4.0	3.0	7.2	33.7
Mid Skill (NVQ 3)	66.4	33.6	6.2	18.0	9.4	12.0
Low skill (NVQ2 or less)	64.0	36.0	6.7	12.4	17.0	21.9
Homeowners	78.6	21.4	3.9	11.7	5.8	56.2

Source: Labour Force Survey, Autumn 2005.

Note: Unemployed, inactive and studying given as a proportion of total working age population.

Personal characteristics 2.18

Table 2.1 shows that, compared to the overall working age population in London:

- men are more likely to be in work, and women more likely to be workless;
- people from ethnic minority groups and those born overseas are less likely to be in employment;
- lone parents are much more likely to be inactive; and
- homeowners and the highly qualified are more likely to be in employment.

2.19 Table 2.1 also shows that students explain the extent of worklessness in some groups more than in others. For example, people from ethnic minority groups are particularly likely to be economically inactive because they are studying.

Trends particularly evident in London 2.20

By comparing rates of employment in London to those in the rest of the UK (shown in Table 2.2), we can see the extent to which national trends are more pronounced in London.

Table 2.2: Employment rates by selected characteristics, London and rest of UK, 2005

	Rest of UK	London	Difference between London and the rest of the UK
All working-age population	75.4	68.9	-6.5
Men	79.6	74.7	-4.9
Women	71.0	62.6	-8.4
Black or minority ethnic	61.1	56.6	-4.6
White	76.4	75.2	-1.2
Born in the UK	76.0	72.4	-3.7
Born abroad	68.7	63.0	-5.7
Parents (including lone parents)	83.7	72.3	-11.4
Lone parents	57.2	43.3	-13.9
Aged 50 or over	70.5	69.9	-0.6
High skill (NVQ4+)	87.5	85.8	-1.7
Mid Skill (NVQ 3)	77.9	66.4	-11.5
Low skill (NVQ2 or less)	74.0	64.0	-10.0
Homeowners	81.6	78.6	-3.0

Source: Labour Force Survey, Autumn 2005.

2.21 Parents, and in particular, lone parents are much less likely to be employed in London than in the rest of the UK, as are those with medium and low skill levels.

Employment by ethnicity

2.22 The employment rate of ethnic minorities in London, at 56.6 per cent, is also low. Nationally, the employment rate for ethnic minorities is 59 per cent, compared to an overall national employment rate of 74.5 per cent. The Government, together with employers, is taking action to address this disparity as described in Box 2.1 below.

Box 2.1 Government actions to tackle the ethnic minority employment gap.

In 2003, in response to a Cabinet Office report 'Ethnic Minorities in the Labour Market', the Government established a Ministerial Ethnic Minority Employment Task Force to take forward a cross government strategy to overcome the barriers faced in education and employment, and through discrimination.

In addition, in 2005 the National Employment Panel Report 'Enterprising People, Enterprising Places' identified key recommendations to improve the employment and enterprise prospects of ethnic minorities. The main recommendations were accepted in Budget 2005. The report recommended a focus on 5 cities where two-thirds of the ethnic minority population live (London, Birmingham, Manchester, Bradford and Leicester), building on existing programmes and practice. The measures recommended by the NEP included new Centres of Vocational Excellence (CoVEs) for entrepreneurship as part of the overall support for ethnic minority enterprise; and Workforce Investment Boards to oversee new integrated employment and skills frameworks.

As part of the Welfare to Work agenda, the Government has introduced specific initiatives designed to improve the employment rate of ethnic minorities. For example, in 2002 Jobcentre Plus introduced Ethnic Minority Outreach to increase support for ethnic minorities to move into employment. The National Employment Panel supports three Fair Cities pilots in Birmingham, Bradford and Brent, which started in 2005. These are employer-led initiatives designed to improve job entries for ethnic minorities in these cities.

2.23 Employment rates differ substantially between ethnic minority groups in the UK. People from Indian and Black Caribbean groups have relatively high employment rates (70.1 per cent and 68.3 per cent respectively). On the other hand, people from Bangladeshi and Pakistani groups have the lowest employment rates among all ethnic minorities (40.8 per cent and 44.7 per cent respectively), with employment rates for Bangladeshi and Pakistani women even lower.

2.24 London's population is much more ethnically diverse than that of the UK as a whole. Some 29 per cent of Londoners are from an ethnic minority, compared to 8 per cent of the UK population as a whole. However, the labour market position of some particular ethnic minority groups in London is comparatively poorer than in the rest of the country.

Unemployment by ethnicity

2.25 Table 2.3 uses data from the 2001 Census to show the differences in unemployment rates by ethnic group in London. It also covers the differences between Inner and Outer London, and the rest of England and Wales. It shows that unemployment rates for ethnic minorities are significantly higher in Inner London than Outer London. It also shows that the unemployment rate for some ethnic groups are particularly high, for example, among the Bangladeshi population in London, it is over 20 per cent.

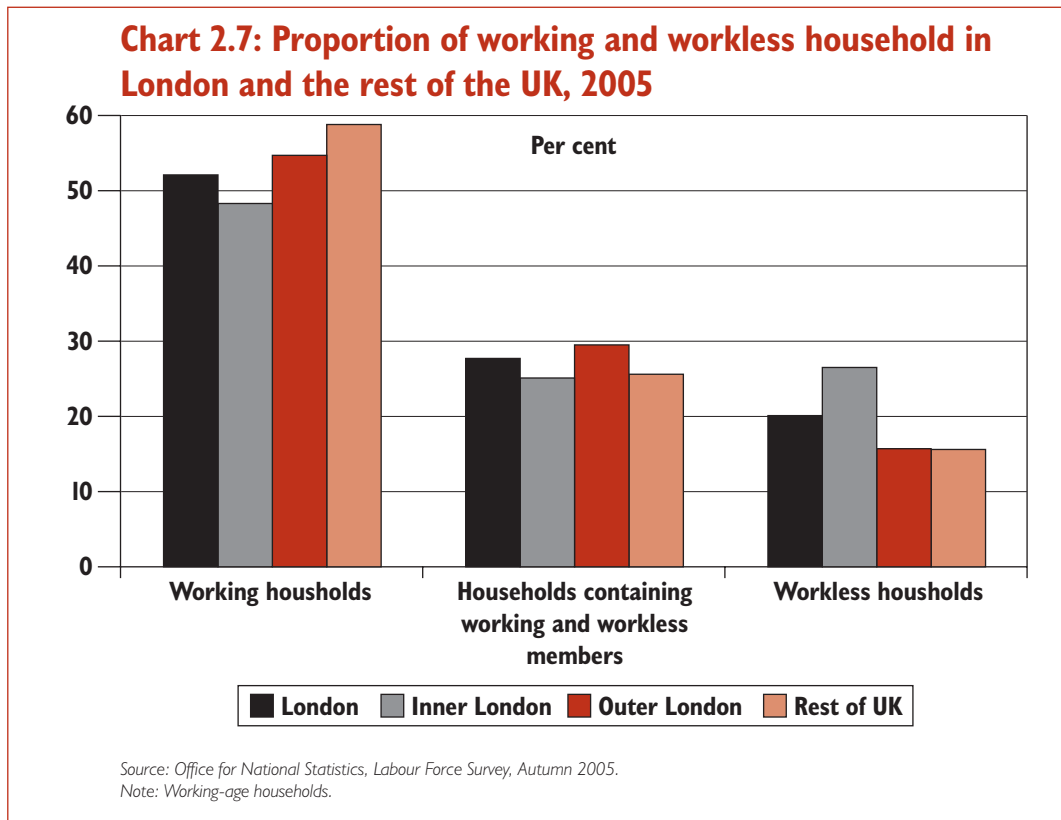
Table 2.3: Unemployment rates by ethnic group, London compared to England and Wales, 2001

	Inner London	Outer London	Greater London	England & Wales excluding London
All	8.9	5.4	6.7	5.0
White	6.6	4.5	5.3	4.7
Indian	8.0	5.5	5.9	7.1
Pakistani	13.8	11.5	12.2	16.5
Bangladeshi	23.1	11.5	20.5	15.5
Other Asian	12.7	8.2	9.3	9.2
Black Caribbean	15.4	8.9	12.3	11.1
Black African	17.4	14.1	16.0	12.8
Other Black	20.3	14.2	17.6	14.6
Mixed	14.8	9.9	12.3	11.5
Chinese or other	10.6	7.6	9.0	6.6
All ethnic minorities	15.1	8.5	11.3	10.5

Source: 2001 census, adapted from GLA Data Management and Analysis Group, Briefing 2003/26 Unemployment in London.

Individuals and households

2.26 The household-level distribution of work in London has important implications for the connections between worklessness, poverty and deprivation in the capital. Compared to the rest of the UK, London has a smaller proportion of two-person working households and a larger proportion of workless households. These trends are more pronounced for Inner London than for London as a whole.



Income distribution 2.27 The interaction of individual characteristics, household types and labour market outcomes in London gives rise to a particular distribution of household incomes. Compared to the country as a whole, incomes in London are polarised. This pattern is particularly stark in Inner London, where well over half of all households are located in either the top or bottom national income quintile. The prevalence of workless families is also consistent with the relatively high incidence of child poverty compared to other regions.

Social housing 2.28 In London, working age people living in social housing have an employment rate of 42.2 per cent, close to the UK employment rate for people living in social housing (43.7 per cent). However, 23 per cent of working age Londoners live in social housing, compared with only 15 per cent nationally. Therefore, if there were a causal relationship between social housing and worklessness this could have a disproportionate impact in London.

2.29 However, the relationship between worklessness and social housing cannot be looked at in isolation. To complete the picture it is also necessary to look at the combination of personal characteristics and situation. For example, there is little difference between the employment rates in London and the UK for people from ethnic minorities who face no other labour market barriers. The employment rates for people from ethnic minorities living in social housing in London and in the UK are also very similar, at 38.2 per cent and 38.7 per cent respectively. Similarly, employment rates for lone parents in social housing and the UK are very close, at 33.4 per cent and 36.1 per cent respectively. This suggests that combinations of disadvantage and situation may explain a significant proportion of the difference in overall employment rates between London and the rest of the UK. These complex relationships are considered further in Chapter 3.

SPATIAL VARIATIONS WITHIN LONDON

2.30 Significant spatial differences within London can often be larger than those between London and the other regions. Comparing the Inner London boroughs to their Outer London counterparts shows that worklessness in London is concentrated in Inner London. In many respects the Outer London boroughs bear more similarities to the surrounding region and other parts of the country.

Table 2.4: Employment, unemployment, inactivity and worklessness rates in London compared to neighbouring regions and the rest of the UK, 2005

	Employment rate	Unemployment rate		Inactivity rate		Worklessness rate	
		All	Long Term	All	Excluding Inactive students	All	Excluding inactive students
London	68.9	7.8	2.1	25.3	18.9	31.1	25.2
Inner London	63.9	8.5	2.8	30.1	21.9	36.1	28.5
Outer London	72.2	7.4	1.6	22.0	16.9	27.8	23.1
Rest of South East	78.4	4.4	0.7	17.9	14.6	21.6	18.4
Rest of UK	75.4	4.8	1.0	20.7	17.0	24.6	21.0

Source: Labour Force Survey, Autumn 2005.

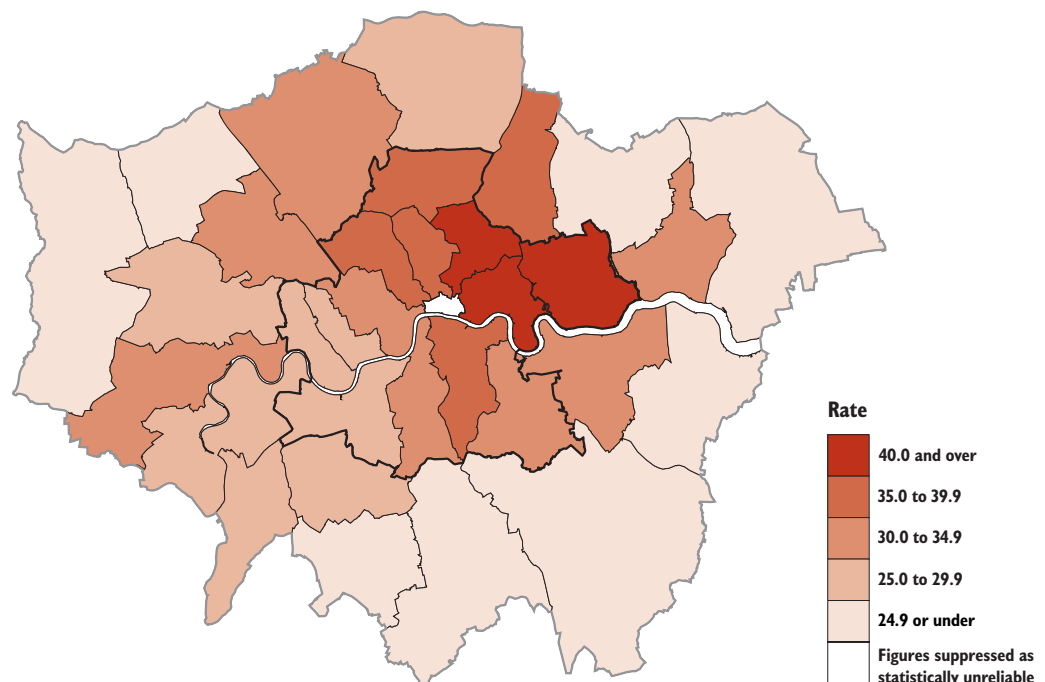
Notes: Long term unemployment is defined as percentage of the ILO unemployed who have been unemployed for longer than 12 months.

Rest of South East defined as the South East and East Government Office Regions combined.

Rest of UK defined as all UK countries and Government Office Regions excluding London.

2.31 Even within Inner and Outer London there are significant spatial variations in unemployment and inactivity. Worklessness is noticeably concentrated in particular London boroughs (forming an eastern ‘horseshoe’) and even in particular wards. This geographic pattern of worklessness is closely correlated with measures of deprivation and exclusion, which show also considerable persistence over time.

Chart 2.9: Worklessness rates¹ by London Borough, 2004-2005²



¹ The worklessness rate is defined as the proportion of the working-age population who are either unemployed or economically inactive.

² Based on four quarter averages from June 2004 to May 2005.

Source: Office for National Statistics, Labour Force Survey

EXPLAINING LOWER EMPLOYMENT RATES IN LONDON

2.32 The Strategy Unit identified a number of potential explanations for lower employment rates in London that deserve further investigation. These focused on the impact of population and labour market factors.

Population composition

2.33 There are some individual characteristics or household circumstances – such as being a student, being from an ethnic minority, or being a lone parent – that are associated with lower employment rates across the country. London has a greater proportion of people who fall into these categories, and this may be the reason why the overall employment rate in London is lower.

2.34 Chapter 3 considers this explanation in more depth. It examines the differences between the characteristics of Londoners and those living in the rest of the country and confirms that London does have a greater proportion of people with characteristics associated nationally with lower employment rates. The chapter then considers the extent to which compositional factors account for the overall difference in employment rates.

2.35 The compositional account can be tested using econometric analysis. The key indicator is the likelihood of an individual being employed in London compared to the rest of the country, once any characteristics of the individual that might have a bearing on their employment prospects have been taken into account. If the likelihood of employment is the same once differences in characteristics are taken into account, compositional factors would be explaining the observed difference in employment rates. Chapter 3 considers findings from existing studies, as well as further HM Treasury analysis.

Labour market factors

2.36 Labour market explanations for lower employment rates in London begin with two observations:

- **the fact of the change:** until the early 1990s, employment rates were higher in London than in the rest of the country; and
- **the persistence of the difference:** since then, employment rates have remained persistently lower in London compared to the rest of the UK, and in stark contrast to the higher rates in neighbouring regions.

2.37 The emergence and persistence of lower employment rates in London coincided with a period of intense and sustained changes in London's industrial base. This has altered the nature of economic activity in the capital fundamentally, as London exploits its comparative advantage in high-skilled and capital-intensive work. This change in the nature of labour demand may have led to some immediate problems of skills mismatch between the demands of London businesses and the supply of London labour, intensifying competition for the remaining jobs that require fewer specialist skills. It may also have led to some scarring effects on those Londoners pushed out of the labour market by the change. But economic theory would predict that in a well functioning and responsive labour market these problems would disappear after a reasonable period of adjustment. Individuals with skills that are in low demand in London but higher demand elsewhere would leave for better employment opportunities elsewhere. Others would improve their skills to better match demand. Migrants with the skills demanded by London employers would arrive to fill remaining skills gaps.

2.38 As mobility of low skilled workers is generally low, and because upgrading of skills is a slow process, adjustment is likely to take some time. Any persistence caused by problems of adjustment would be revealed in one of two ways:

- skills shortages for employers, caused by a lack of skill improvements among the residents or lack of migration; and/or
- an excess supply of people with the wrong skills, due to failure to equip residents with the right skills, or from constraints on mobility.

2.39 London's appetite for highly-skilled workers remains strong, but London does not appear to have a major problem in attracting workers in this category. London remains a magnet for young upwardly mobile domestic migrants and a global pool of talent.

2.40 Chapter 4 tests the argument that London has an excess supply of low-skilled labour, and any impact this may be having on the employment opportunities of Londoners. It looks at the intensity of competition for jobs in London and on the expected financial gains for Londoners who move into work. To the extent that any problems of excess labour supply are revealed, the chapter then considers the reasons why this situation may be persisting.

3

UNDERSTANDING WORKLESSNESS IN LONDON: POPULATION FACTORS

Summary

London's population differs from the rest of the country in many ways. The London population is more ethnically and socially diverse than in the rest of the country. Londoners are on average younger than non-Londoners, and more likely to form single person or lone parent households. Overall London is home to more people with characteristics known to be associated with labour market disadvantage, and to more people with multiple barriers to work.

An examination of the evidence on regional labour market outcomes suggests that patterns of worklessness across the country are correlated with the distribution of groups prone to disadvantage in the labour market. Key potential explanatory factors include age, gender, ethnicity, qualifications, health status and country of birth. The concentration of several of these factors in the London population is a prime candidate to explain the high rates of worklessness observed in the capital.

Several studies have examined this issue, and concluded that London's different population composition explains a significant amount of the variation in rates of worklessness between London and other regions. The analysis in this paper of the latest data is in line with other findings: a small but significant 'London factor' remains once population characteristics are controlled for. There is also strong evidence that, for lone parents and those with lower qualifications, being in London has a significant detrimental effect on employment rates.

3.1 Chapter 2 showed that London's employment rate fell below the rate in the rest of the UK in the early 1990s. Chapter 2 also described the differing characteristics of those who are in work and those who are workless in London and across the country, showing that worklessness disproportionately affects some particular groups within the London population.

Labour market disadvantage **3.2** The Government recognises that some individual characteristics can put people at a disadvantage in the labour market. Sometimes this is because individuals lack the skills, qualifications or experience to do the types of job on offer. Sometimes an individual's circumstances can make it harder for them to balance the pressures of work and family life. In other cases still, employer prejudice and discrimination can play a role. The success of the Government's national welfare-to-work programme reflects the action it has already taken to address the needs and concerns of different groups who suffer from labour market disadvantage.

3.3 The composition of London's population differs from that found in the rest of the UK on a number of important dimensions. Understanding that individuals with different characteristics can have different labour market prospects is therefore an important step in analysing and explaining the relatively poor labour market outcomes observed in London compared to other parts of the country.

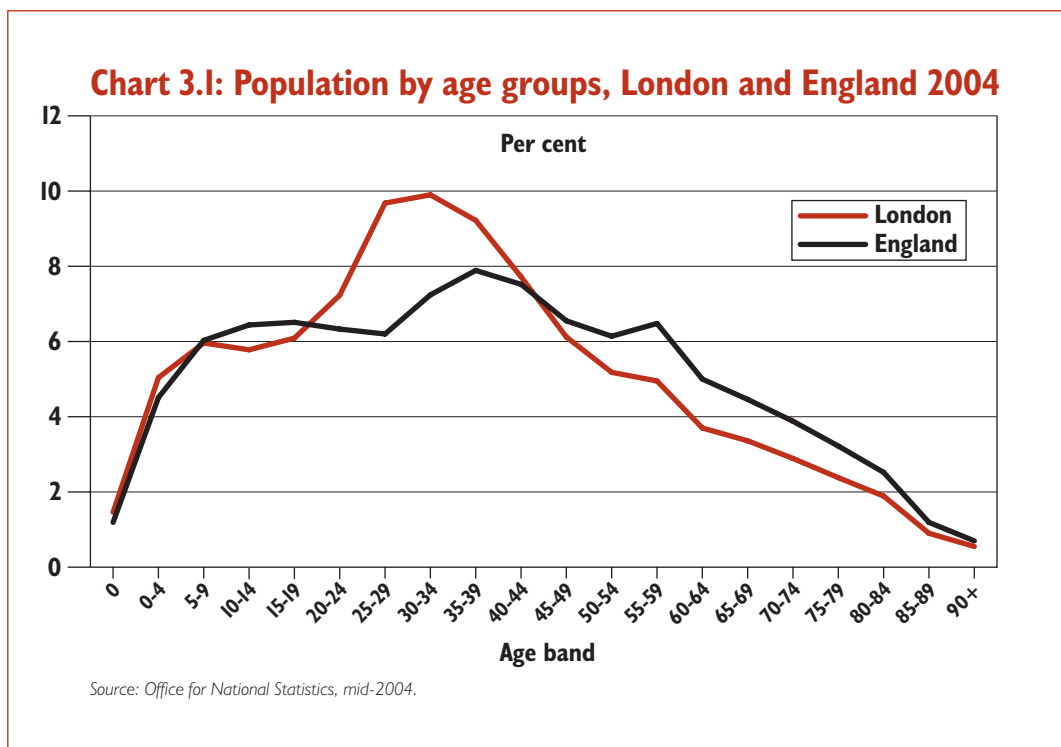
3.4 This chapter sets out the key evidence on London's population, and how the composition of the population in the capital differs from that found in the rest of the country. It then reports the results of several econometric studies that have attempted to quantify the relationship between a relatively high density of disadvantaged groups and a relatively high rate of worklessness in London.

LONDON'S DIVERSE POPULATION

How London is different **3.5** London's population differs from the rest of the country in many ways. Londoners are on average younger than non-Londoners, and the population in London is more ethnically and socially diverse than in the rest of the country. More Londoners are students, and Londoners are more likely to live in single person and lone parent households. There is a significant degree of polarisation in the capital, with London typically over-represented at both the top and bottom of the distribution of skill and household incomes.

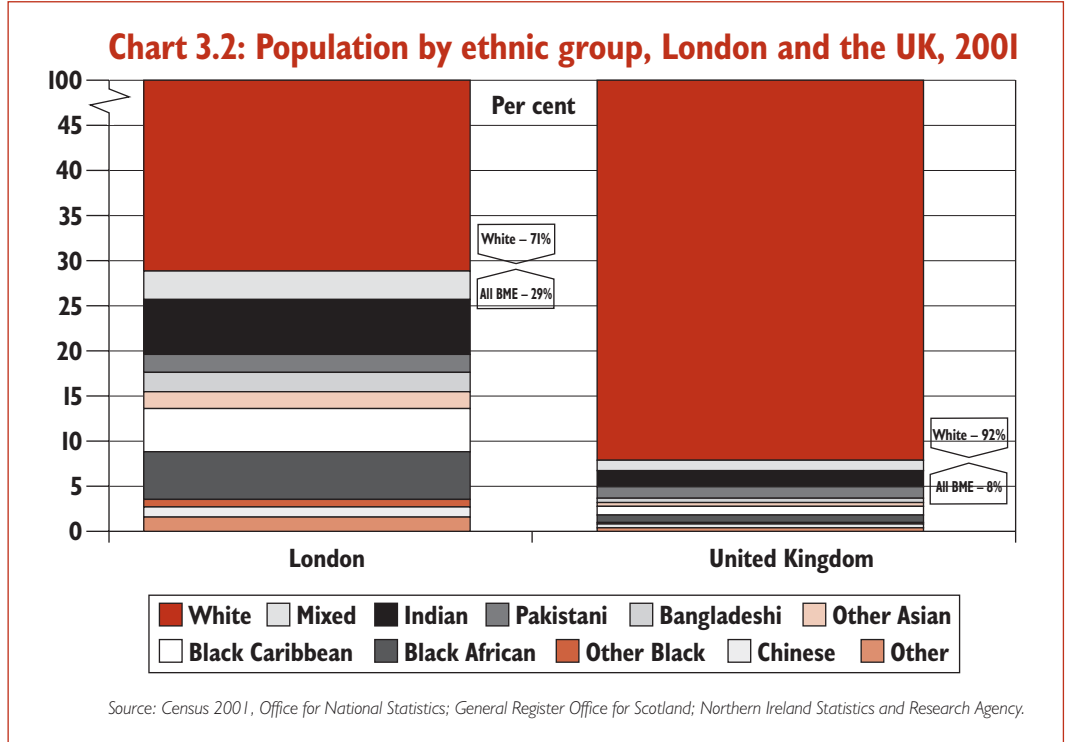
Age structure

Age 3.6 Overall, London's population profile is considerably younger than that of the country as a whole. The average Londoner is 36 years old, while the average non-London resident is 39. Chart 3.1 shows that, compared to England as a whole, London has significantly more young adults, but relatively fewer young people and individuals over 50.



Ethnic minority groups

3.7 Compared to the UK as a whole, London’s population contains a significantly higher proportion of individuals from ethnic minority groups. Data from the most recent census show that around 29 per cent of Londoners are from an ethnic minority group, compared to just 8 per cent in the UK as a whole.



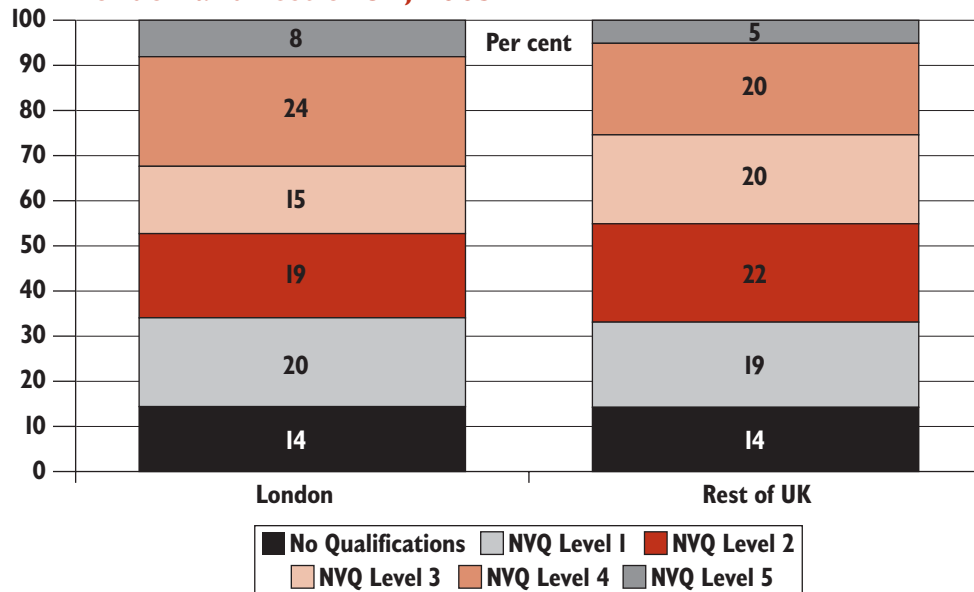
3.8 Chart 3.2 shows the considerable diversity within London’s ethnic minority population. The Strategy Unit reported that London is home to people of over 90 different nationalities, with communities speaking a total of 300 different languages.¹ This degree of ethnic diversity within the population is unique to London. There are large ethnic minority populations in other parts of the country, but these are more likely to represent concentrations of a smaller number of minority groups.

Skills and qualifications

Skills 3.9 The profile of skills and qualifications varies between London and the rest of the UK. Using highest qualification as a proxy for skills, in the rest of the UK, around 25 per cent of working-age people have qualifications equivalent to NVQ 4+ (degree or equivalent), 61 per cent are at NVQ 1-3, and the remaining 14 per cent have no formal qualifications. In London there are proportionately more people with advanced qualifications, fewer people in the middle of the distribution, and the same proportion with no qualifications.

¹The London Project Report, Prime Minister’s Strategy Unit, Cabinet Office, July 2004.

Chart 3.3: Working-age population by highest qualification, London and rest of UK, 2005

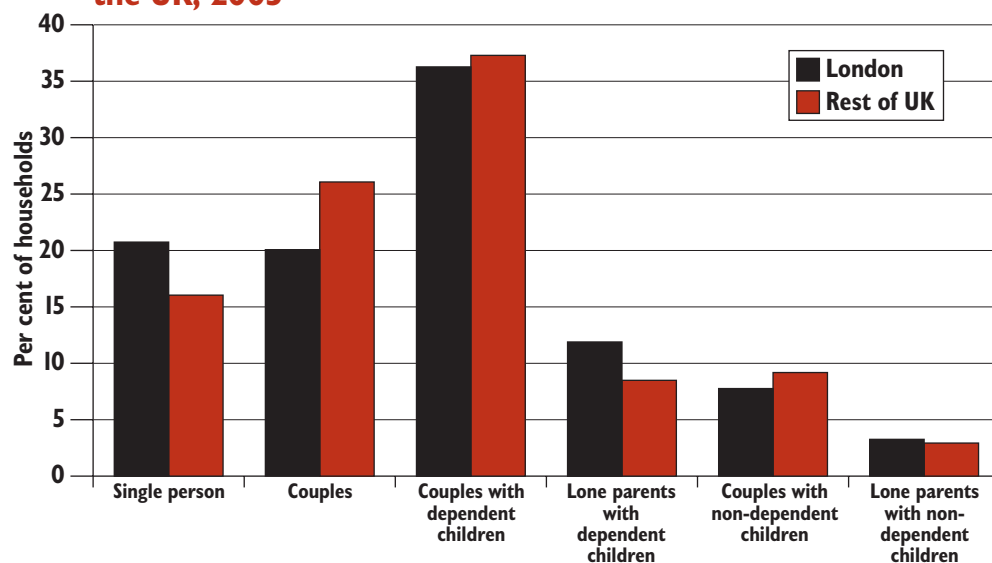


Source: Labour Force Survey, Spring 2005.

Households

Household composition 3.10 In addition to the different individual characteristics of Londoners, households in London are also different. Although the average household size in London is 2.35 persons, around the same as that in the rest of the country, there are pronounced differences in the types of family units that make up these households.

Chart 3.4: Households by family type, London and the rest of the UK, 2005



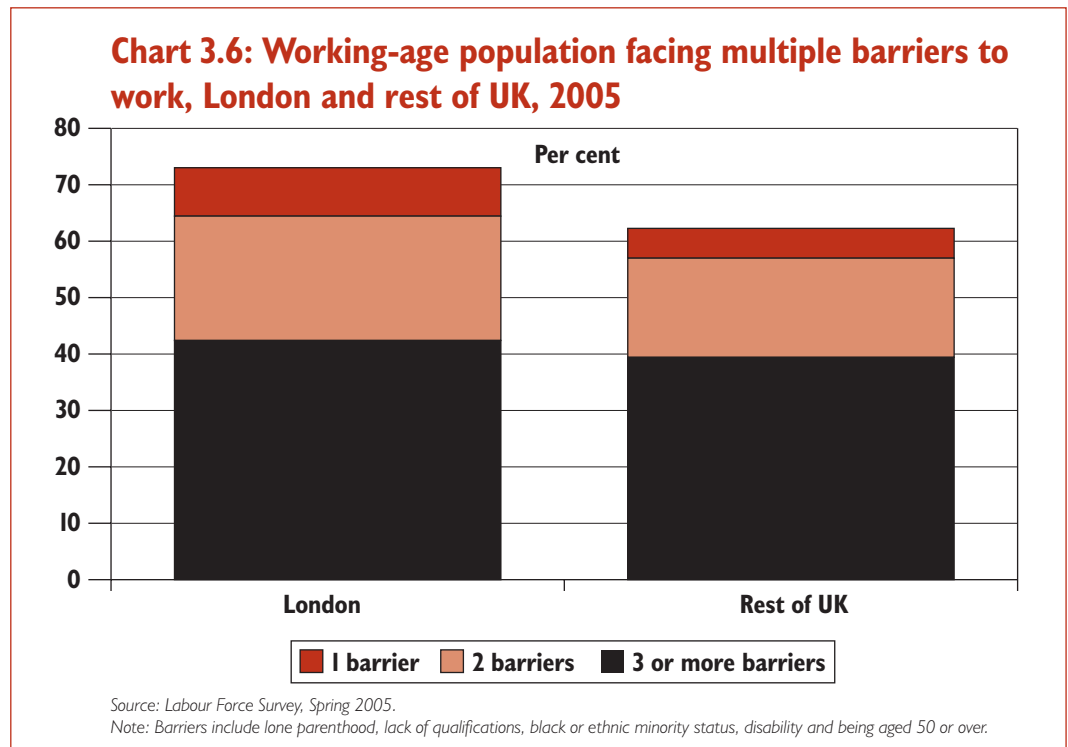
Source: Labour Force Survey, Spring 2005.

3.11 Chart 3.4 shows a breakdown of household types in London compared to the rest of the UK. London contains significantly higher proportions of both single-person households and lone parents with dependent children. There are also proportionately fewer couple-only households in the capital.

3.12 The characteristics of lone parents in London differ from those in the rest of the country in a number of ways. For example, they are more likely to be local authority tenants and less likely to be receiving any maintenance than lone mothers in the rest of the UK. London lone mothers are also more likely never to have worked.² For example, in Inner London 37 per cent of lone mothers have never had a job, compared to 32 per cent in Outer London and 23 per cent in the rest of UK.³

Multiple disadvantages

Multiple disadvantage 3.13 In addition to the differences that exist at the individual and household levels, London's population also differs in the extent to which people face combinations of factors that affect their labour market prospects. Chart 3.6 shows that while in the rest of the country around 23 per cent of individuals face two or more key barriers to work, in London this proportion rises to just over 30 per cent.



3.14 For some people facing several barriers to work, the chances of finding employment can be very low indeed. For example, analysis carried out by the Greater London Authority shows that of a sample of female lone parents with more than two children, health problems and no qualifications, only 4 per cent were in work.⁴ Indeed, London contains a relatively high proportion of individuals who have never been in formal employment.

² Lone Parents in London: Quantitative analysis of differences in paid work, McKay, S., DWP In-house Report 136 (2004).

³ Ibid

⁴ GLA Economics Working Paper 15, Worklessness in London, Explaining the difference between London and the UK, Meadows P., Greater London Authority, 2006.

UNDERSTANDING WORKLESSNESS: ANALYSING POPULATION FACTORS

3.15 Many of the characteristics more prevalent in the London population are known to be associated with labour market disadvantage, not just in London but also across the country as a whole. Factors known to be of particular importance in influencing labour market prospects include lone parenthood, a lack of qualifications, disability, ethnicity and age.

Population factors 3.16 This higher incidence of characteristics associated with labour market disadvantage is one potential explanation for the persistent gap in employment rates between London and the rest of the country. Several studies have attempted to establish the extent to which London's different population composition can explain its different labour market outcomes. The conclusions of some of the recent studies are summarised in Box 3.1.

Box 3.1: Explaining regional variations in economic activity

In 2004 the Prime Minister's Strategy Unit published a wide-ranging report on London, including an analysis of employment and worklessness.^a The report noted that London accounts for around 13 per cent of the UK population, but that 20 per cent of the UK's workless households are found in London. The report presented analysis undertaken in conjunction with the Department for Work and Pensions (DWP), which found that the concentration of vulnerable groups in London explained much of the high worklessness observed in Inner London. However, even after controlling for a range of characteristics, they found that the odds of worklessness remained higher in Inner London compared to most other parts of the country. This suggests that there are specific conditions that make it less likely individuals will find and take employment in London.

A recent paper published by the Greater London Authority (GLA) has also examined worklessness in London, and sought to explain the differences in rates of worklessness between the whole of London and the rest of the UK.^b The paper considers the characteristics of Londoners including age, gender, ethnicity, country of birth, parenthood, health status and qualifications, and the impact of overlapping characteristics on rates of worklessness. The analysis indicates that the different characteristics of Londoners and the higher proportion of full-time students can account for around 90 per cent of the difference in worklessness between London and the rest of the country. However, the study finds that for lone parents there is stronger evidence of an unexplained London effect that increases this likelihood of worklessness in the capital.

There has also been specific analysis of employment and worklessness among lone parents in London. Research for the GLA and DWP found that lone mothers in London are less likely to be in work than those in other regions.^c Again, much of this difference can be attributed to the different characteristics of lone mothers in London, who are more likely to have no work history, more likely to live in social rented properties, and more likely to be full-time students. The report found, however, that only part of the difference in employment rates can be attributed to the different characteristics of lone mothers in London - and that there is a local effect operating in London over and above differences in the composition of the population that is affecting the employment of lone mothers.

^a *London project report*, Prime Minister's Strategy Unit, July 2004.

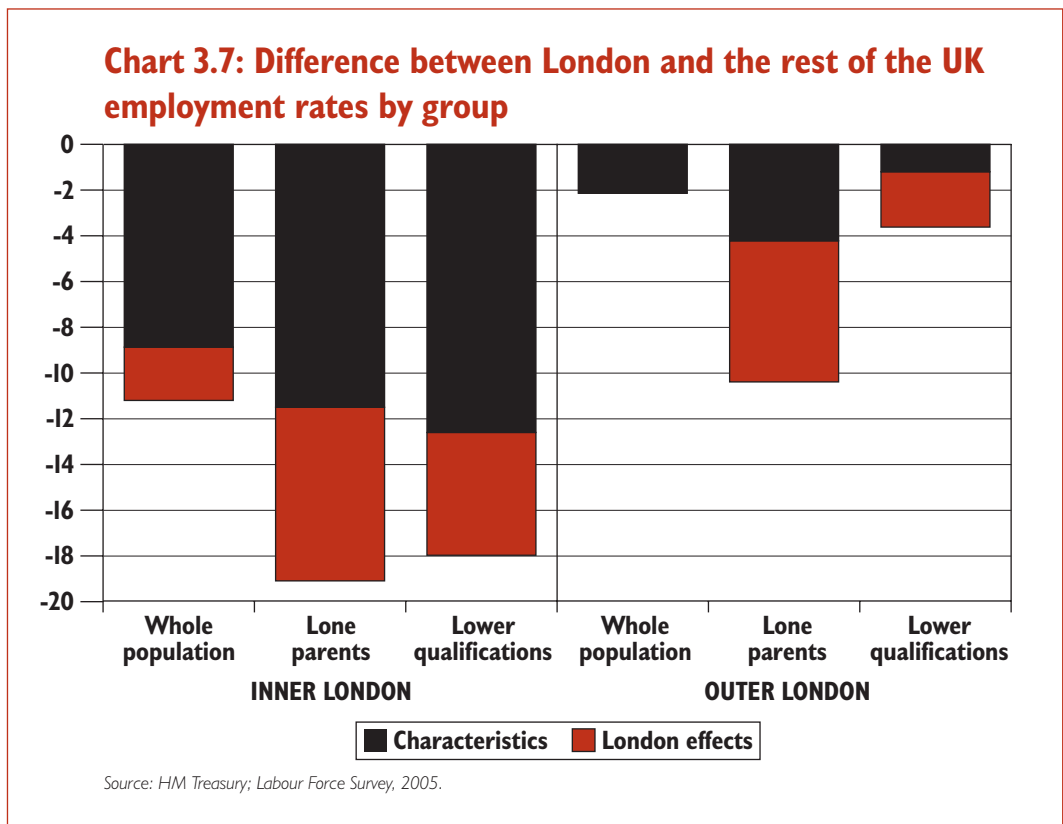
^b *GLA Economics Working Paper 15, Worklessness in London Explaining the difference between London and the UK*, Meadows, P., Greater London Authority, 2006.

^c *Lone Parents in London: Quantitative analysis of differences in paid work*, McKay, S., DWP In-house Report 136 (2004).

Understanding the impact of population composition

3.17 HM Treasury conducted similar analysis using data from the 2005 Labour Force Survey. As with other studies, HM Treasury tried to isolate the proportion of the difference in employment rates in London that still remained after the characteristics of Londoners were taken into account. The initial findings were broadly in line with those of the studies discussed in Box 3.1, but with some differences.

Inner and Outer London 3.18 Chart 3.7 shows that this compositional explanation could account for about 9 percentage points of the difference between employment rates in Inner London and the rest of the UK. The remaining unexplained 2.3 percentage point difference was found to be statistically significant. By contrast, all of the difference between employment rates in Outer London and the rest of the UK can be accounted for by population characteristics.



3.19 The findings in Chart 3.7 are therefore in broad agreement with those of the Strategy Unit, which also found a significant difference in employment rates in Inner London that cannot be explained by the observable characteristics of the population. The difference may be explained by population effects not considered in this analysis, such as the compound effects of multiple disadvantages. Alternatively, the explanation could lie elsewhere. Further analysis is required to understand these ‘London effects’.

Lone Parents 3.20 HM Treasury analysis also found that differences in employment rates for lone parents in Inner and Outer London could not be explained by characteristics alone. The unexplained difference was large and statistically significant. In fact, observable characteristics appear to account for only 40 per cent of the difference between the employment rates of lone parents in Outer London and in the rest of the UK, and 60 per cent of the difference in Inner London. These findings are consistent with McKay’s findings for lone mothers, discussed in Box 3.1.

Lower qualifications 3.21 Chart 3.7 shows that living in London also has a greater impact on the employment chances of those with lower qualifications⁵. In Outer London the majority of the difference in employment rates remains unexplained by the observable characteristics of the lower-qualified population. For those in Inner London with lower qualifications this ‘London factor’ is equivalent to 30 per cent of the difference in employment rates.

Housing tenure 3.22 Across the country, living in social housing is associated with lower employment rates. This is true for London also, but findings from HM Treasury’s analysis suggest that this is no worse in London compared to elsewhere. The effect of living in social housing on labour market outcomes is, however, an issue that requires further investigation.

Conclusion

3.23 Although the results of these studies are not directly comparable, there is a broad consensus that most of the difference in worklessness between London and the rest of the country is driven by the higher incidence of characteristics associated with labour market disadvantage among the London population. But there is evidence of an additional, so far unexplained, ‘London factor’ that is increasing worklessness in Inner London and, for certain groups, right across the capital. The labour market outcomes for lone parents and those with the lowest qualifications diverge furthest from what would be expected based on their observable characteristics alone.

3.24 The presence of an unexplained factor affecting labour market outcomes in London needs to be understood in order to assess the implications for employment policies in London. Chapter 4 looks at the London labour market and considers the extent to which labour market imperfections may be having an effect on employment rates.

⁵“Lower qualifications” is used to refer to those who are in the half of Londoners with the lowest qualifications (including those with no qualifications).

4

UNDERSTANDING WORKLESSNESS IN LONDON: LABOUR MARKET FACTORS

Summary

The labour market differences between London and the rest of the country extend beyond differences in the characteristics of their respective workforces. Compared to the rest of the country, London has experienced – and continues to experience – a different and intense pattern of industrial and occupational change. London is also subject to significant domestic and international migration flows.

In aggregate the London economy is highly productive, and there are proportionately more people in London in professional occupations and with advanced skills and qualifications. Although worklessness rates are high relative to the rest of the country, there does not appear to be a general labour demand problem in London, as the city continues to create new jobs.

These jobs tend, however, to be in the high value-added sectors in which London excels – and are often not well suited to the skills and capabilities of long-term workless Londoners or some of London's many new migrants. Moreover, barriers to occupational and geographic mobility – particularly among some lower income groups – may be inhibiting the labour market adjustments that might otherwise take place.

Overall it appears that, while population composition remains the primary explanation for lower employment rates in London, skills and mobility are also key issues in explaining the emergence and persistence of relatively high rates of worklessness in the capital.

4.1 Chapter 3 described the characteristics of London's population, and showed that the different characteristics found in London can explain most, but not all, of the higher worklessness in London compared to other regions. An unexplained difference in employment rates, described as a 'London factor', was observed in Inner London, and for certain groups across London. So before any policy prescriptions can be drawn, the effects of population composition need to be considered in the wider context of how the London economy and labour market operates.

4.2 Overall, London's economy exhibits strong performance. London is a global city that accounts for around one sixth of the UK's output. London's business and financial services together account for nearly half of the capital's total output and employ nearly one million people, a far greater proportion than elsewhere in the UK. The issues facing London's financial services sector are addressed in *Financial services in London: Global opportunities and challenges*, which is also published alongside Budget 2006. London also accounts for a substantial share of the total UK output of creative and leisure industries. Around 4.6 million jobs are located in the Greater London area, more than in any other region. Chart 4.1 shows that, since the early 1990s, London has created new jobs at an average rate of 70,000 each year.



4.3 This chapter focuses on the relationship between workless Londoners and the capital's labour market. It begins by setting out the evidence from a range of labour market indicators in London. It then considers explanations for how the current situation evolved and why it continues to persist.

LABOUR MARKET INDICATORS IN LONDON

4.4 Employment rates are only one indicator of how the labour market in London is operating. An examination of wider labour market indicators can yield important insights into the nature of the employment challenge in London facing policymakers.

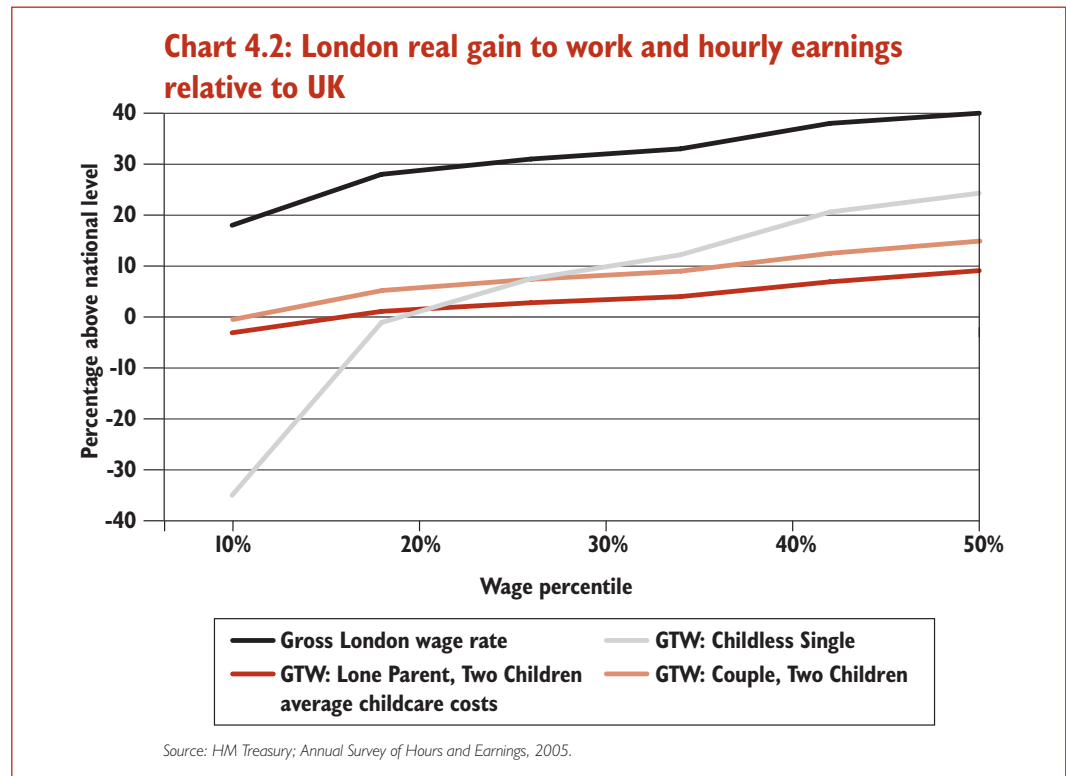
Gains to work

4.5 Evidence on wages shows that on average, gross wages in London are high relative to those of other regions – median hourly pay in London is £13.37, compared to £9.56 in the UK as a whole. However there is significant variation across the income distribution – for example pay at the 20th percentile of the distribution averages £7.95 in London compared to £6.21 in the rest of the UK. Meanwhile occupations with very high skill requirements pay a particularly sizeable premium in the capital.

4.6 In recent years, wages at the lower end of the income distribution have grown more slowly in London than elsewhere, while those at the top have grown faster. This means that the gap between the London premium earned by lower paid workers and that earned by higher paid workers has grown over time. In 1997 Londoners at the 10th percentile of the income distribution earned 25 per cent more than their counterparts in the rest of the UK, while those at the 90th percentile earned 36 per cent more. By 2005 these figures had changed to 18 per cent and 43 per cent respectively.

4.7 Relatively high wage rates in London compared to the rest of the UK do not necessarily mean that incentives to work are higher in London. A composite measure of the full gains to work should incorporate the total financial benefit that results from a move from worklessness to paid employment. A typical individual making this transition will lose

entitlements to some benefits and incur some in-work costs (such as travel), while they will receive income from employment and may gain some in-work benefits. These factors should be incorporated along with adjustments to reflect regional price variations to determine a ‘real’ gain to work.¹ It is difficult to construct a precisely accurate overall picture of gains to work in London, as gains depend on a number of factors. However, looking at a series of examples or specimen cases at various points on the wage distribution can provide a useful illustration of the issues.



4.8 Chart 4.2 shows the gross London wage premium at different points in the income distribution, and a calculation of gains to work based on specimen household analysis. It shows that the real gain to work for lone parents on the lowest wages in London is lower than in other parts of the country. For the lowest paid single people in London (roughly the bottom 20 per cent), the real gain to work is substantially lower. Overall, specimen household analysis suggests that:

- for the lowest paid Londoners, the wage premium in London is smaller than for those earning higher amounts;
- for the lowest paid Londoners, real gains to work are low relative to those experienced by low-paid individuals in other parts of the country; and
- the real gain to work in London relative to the rest of the UK is smaller for low-paid individuals than for those earning higher amounts.

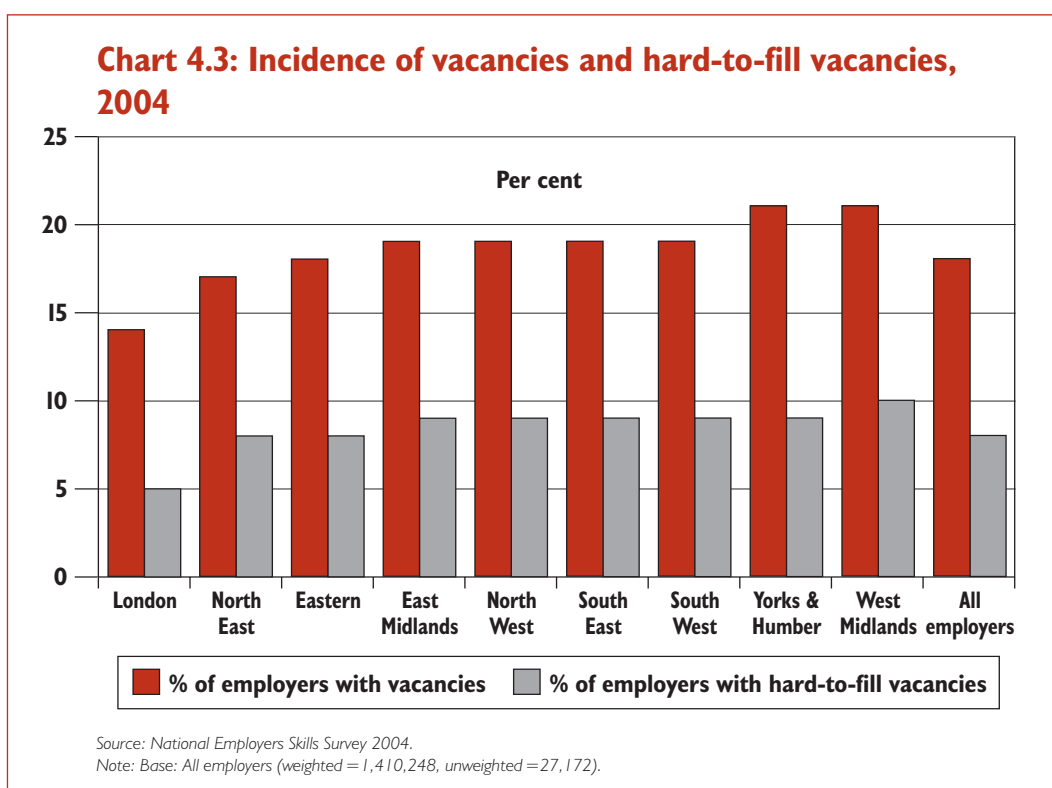
4.9 These specimens assume that households take up all of the forms of financial support that are available to them. Households that fail to take up some of the support available would experience correspondingly lower gains to work. In future work it would be helpful to analyse gains to work through a micro-simulation model in order to incorporate take-up rates more directly.

¹ ‘Real’ in this context refers to the estimated gain to work in a particular region after taking account of differences in average consumer price levels between that region and the UK average; based on data published by the Office for National Statistics in Wingfield et al, 2005, *Relative Consumer Price Levels in 2004*, Economic Trends, February 2005.

4.10 This analysis has considered the impact of lower wages in London relative to the UK for groups at the lower end of the income distribution, and the effects this may have on gains to work. The policy framework, including rules governing the operation of the tax and benefit system and the interaction of different policies in the London context, is discussed further in Chapter 5.

Vacancies

4.11 Data on vacancies and the ease with which they are filled provides some further evidence on how the labour market is operating. The Strategy Unit reported that employers in London find it relatively difficult to fill some jobs with high skill requirements, while also finding it easy to fill jobs with low skill requirements.² The most recent evidence, shown in Chart 4.3 below, demonstrates that employers find it relatively easy to fill vacancies in London compared to other regions and the UK as a whole.



Implications

4.12 Taken together, the cumulative evidence on the operation of the London labour market – real gains to work and vacancies – suggests that:

- for many on the margins of work, the financial reward from moving from worklessness into work, while still positive, is lower in London compared to other parts of the country; and
- employers in London have less difficulty recruiting for the kinds of entry-level jobs that workless people might be considering.

² *The London Project: Analytical Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2003, p.24.

4.13 Economic theory suggests that such differences would normally diminish over time as individuals and firms make adjustments to maximise wages and profits. The persistence of worklessness in London suggests this has not happened, the evidence outlined above being consistent with a surplus of lower-skilled labour in the capital. Such a surplus would tend to bid down relative wages at the bottom end of the labour market, while a high density of jobseekers would lower search costs for employers and make vacancies easier to fill.

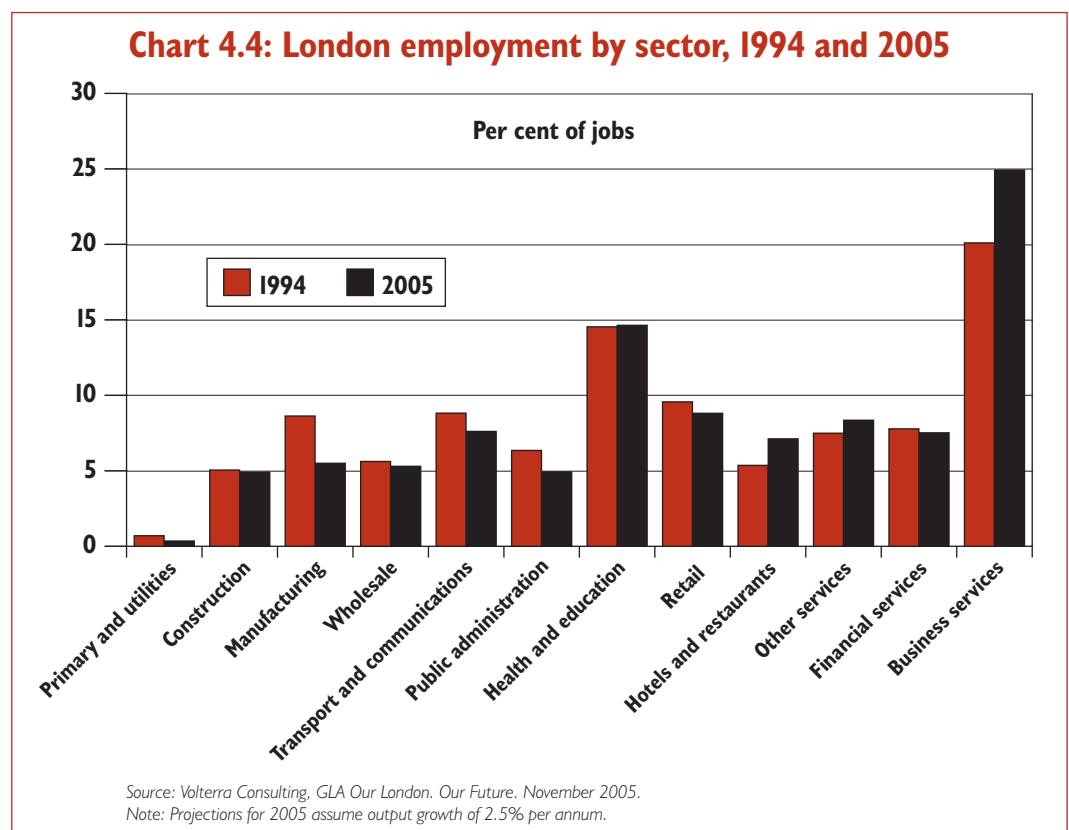
4.14 Moreover, there is little evidence that individuals with lower skills are being crowded out of low-skill jobs by individuals with moderate skill levels. The data on qualifications and occupations show that in a range of lower-skill occupations, Londoners have broadly similar qualifications to their counterparts in the rest of the country. The labour market indicators described here appear to be driven by a surplus of labour suited to low skill requirement work, rather than being a knock-on effect arising from a surplus of over-qualified people chasing entry-level jobs.

DRIVERS OF CHANGE IN LONDON'S ECONOMY

4.15 As described in Chapter 2, employment outcomes in London were better up until the early 1990s, and have fallen behind the rest of the country since then. There are several important drivers of change in London's economy that merit attention in order to better understand how and why relatively higher worklessness in London arose.

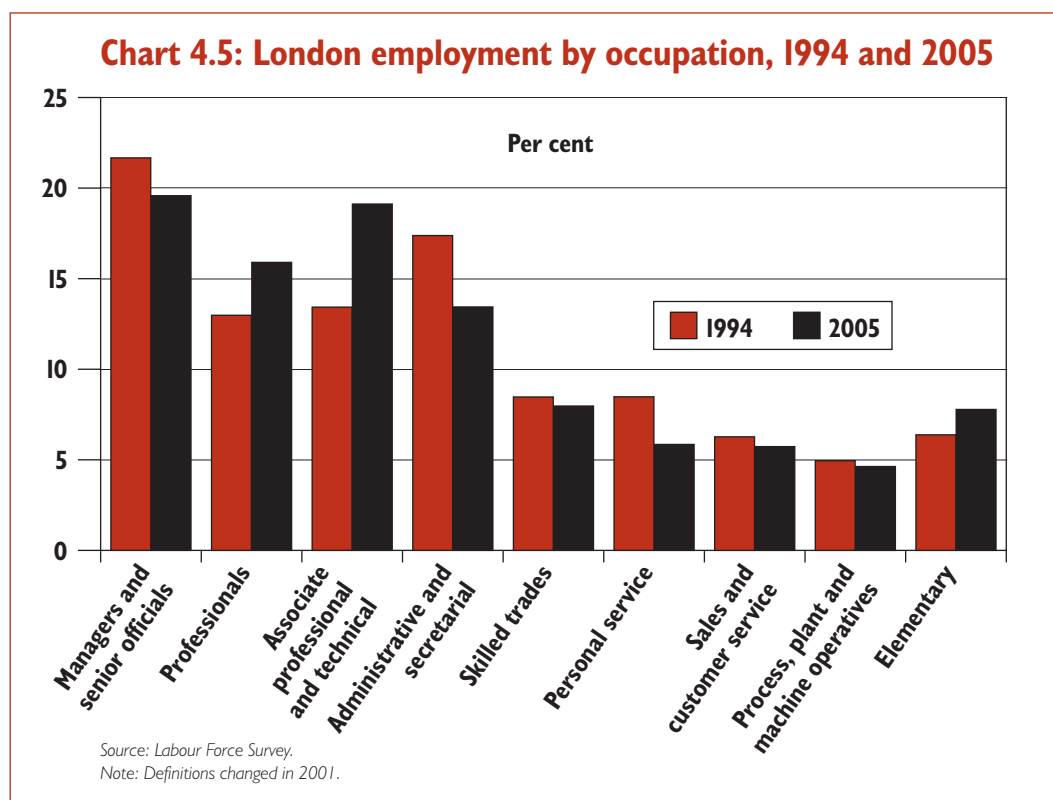
Industrial change

4.16 The modern London economy is increasingly dominated by service functions, while some other activities are in relative decline, as Chart 4.4 shows.



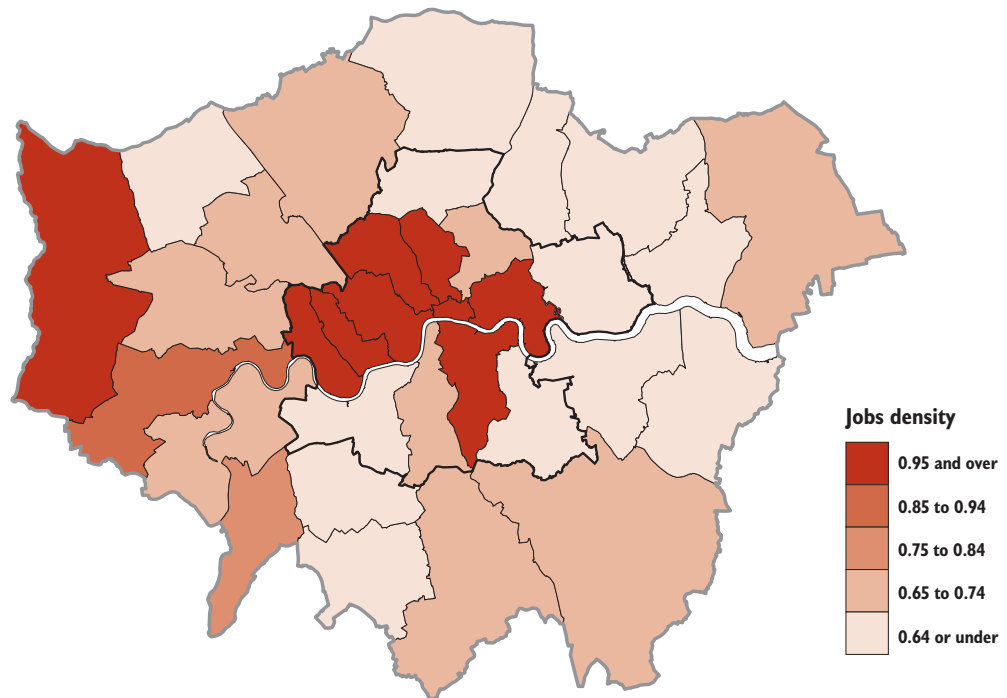
4.17 Recent changes in the pattern of jobs located in London are expected to continue over the medium term. London appears to provide an environment conducive to new business, with the evidence showing higher rates of new business startups in London compared to other UK cities. Even within sectors, technological progress has changed the type of jobs. For example, much of the data processing work that was previously conducted by clerical and administration staff is being done by computers. Furthermore, communications technology has allowed firms to outsource back office functions to other parts of the country or even internationally. And while some jobs have disappeared, technology has created new opportunities and increased the value of workers who can harness the new technology creatively.

4.18 These changes to London's industrial makeup have prompted corresponding changes in the occupations of people who live and work in London. Movement toward an increasingly service-based economy is reflected in recent data showing proportionately fewer people in manual and administrative occupations, and more people in professional, personal services and customer service occupations.



Space 4.19 The evidence on sectors and occupations in London suggests that the expansion of high productivity activities in London has been accompanied by a relative decline in activities with non-specialist and lower skill requirements. The pace of change in London has been accelerated by a scarcity of space in the capital. Chart 4.6 shows that employment densities in Inner London (and the M4 corridor) are significantly higher than in the surrounding areas. Constraints on space in central London drive up property prices, and make it increasingly unattractive for less capital intensive firms to locate in London.

Chart 4.6: Jobs density¹ by London Borough, 2003



¹ Jobs density is defined as the number of filled jobs in an area divided by the number of people of working age resident in that area.
Source: Office for National Statistics

4.20 Within London, economic activity often clusters in specific areas. Major centres include Westminster and the City, Heathrow in the west, Croydon to the south and, more recently, Docklands in the east. Hosting the Olympic and Paralympic Games in 2012, the development of the Thames Gateway, and the completion of the Channel Tunnel Rail Link, will all drive further growth in the east. The development of Heathrow Terminal 5 will also be a significant addition to the capital's infrastructure.

Commuters 4.21 The relatively high density of jobs in central London is supported by a substantial commuter workforce. Over 700,000 people commute into the Greater London area from the surrounding regions every weekday (and a further 270,000 commute the other way). London's relatively well developed and extensive transport network has thus supported the shift in economic activity in the capital, providing London firms with a large pool of labour from which to recruit. However, it is important to recognise that the administrative boundaries are not the same as London's labour market boundaries, which makes defining commuting and commuters to some extent arbitrary.

4.22 Overall, there appears to be a growing divergence between the types of jobs London residents are suited to doing, and the types of jobs that are actually being located in London. In particular, there has been a steady decline in jobs with non-specialist or lower skill requirements, which are those most frequently sought after by individuals on the margins of the labour market. Box 4.1 explores the consequences of London's dynamism on those with lower-end skills.

Box 4.1: London: Dynamism and Growth

The success of London's economy is its ability to restructure in response to changes in technology and new processes, from which it creates new specialisations and, in turn, further opportunities. London's flexibility and ability to change and adapt is key to the city's international success and its contribution to the UK's economic growth. Yet one of the drawbacks of this dynamic of innovation and creation is that those without the skills to meet changes in the workplace may find themselves facing employment difficulties and loss of opportunities.

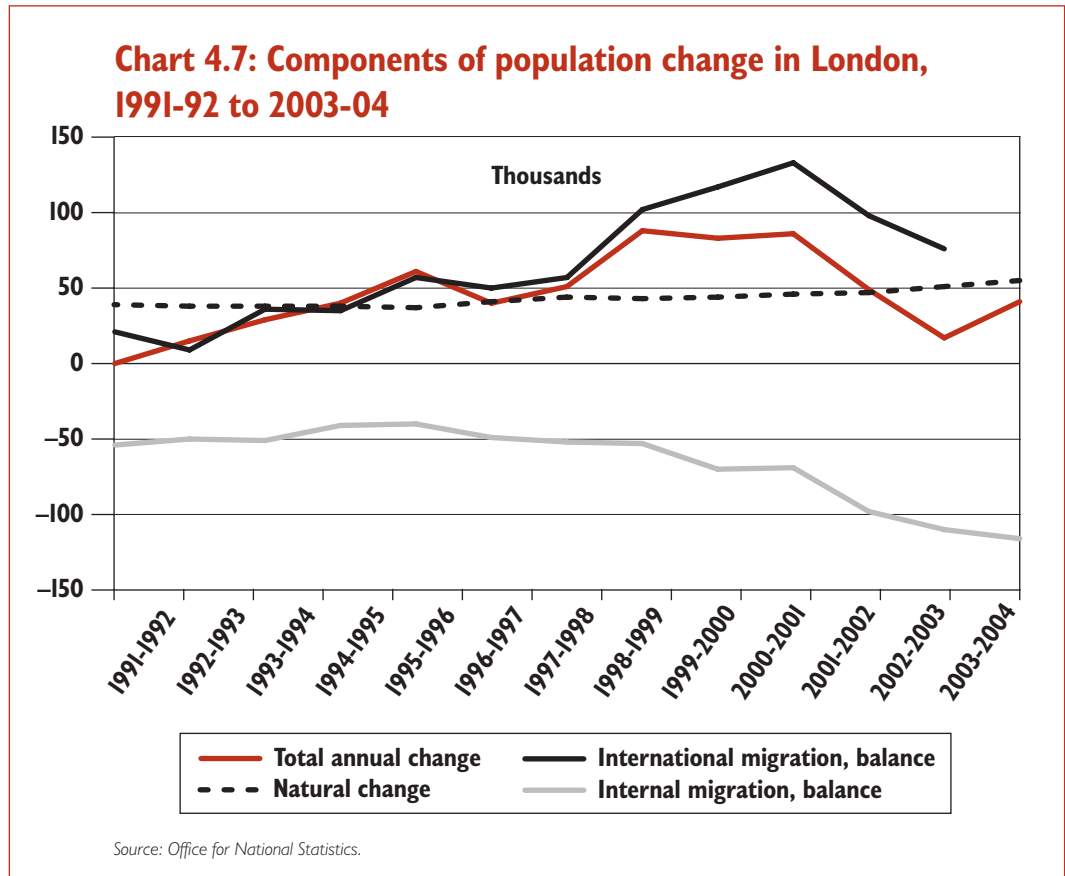
New technologies and lower communication costs are inseparable from the forces of globalisation facing all national economies and cities. As these powerful forces bring change to existing business processes they also create new industries and fast growth firms. These changes lead to new specialisations and divisions of labour, and further productivity and income gains. London greatly benefits as an international business centre, with a highly skilled and flexible international workforce able to benefit from these processes of change. Key growth sectors have been international finance, business services and creative industries, all emerging from London's ability to respond to technology and globalisation.

This dynamic model of growth benefits those with the skills and ability to adapt to work in new and emerging businesses. Economic change has contributed to the rising skills premium – the return to education that creates incentives for the young to develop deeper human capital. The demand for education in London is another one of its great strengths, with many leading institutions supporting the Government's emphasis on skills as a key driver of productivity.

But while dynamic growth benefits many, it can cause problems for others. Workers who are displaced or who do not have the appropriate skills may face prolonged periods of worklessness. For example, information technology has removed much of the processing work that was previously carried out by staff highly trained in shorthand or audio typing skills. Those who consider themselves unable to retrain or who lack the confidence or support to gain the necessary skills may find these negative consequences of vibrant city growth a reality. One of the challenges from London's success is leveraging its powerful economic performance to the benefit of all.

Population flows

4.23 Changes in London's industrial and occupational structure have occurred alongside significant changes in London's population. In the decade to 2001, London's population grew by 5 per cent, more than twice as fast as in the rest of the country. London's population is expected to continue growing, mostly as a result of natural change. Large domestic and international migration flows will continue to affect the composition of the London workforce, changing both the quantity and type of labour available to firms in the capital.



4.24 Migration flows to London occur both from other parts of the UK and from overseas. Chart 4.7 shows that net international migration inflows to London and net internal migration outflows from London have both increased. The chart shows net migration flows, however the corresponding gross flows of people into and out of London are significantly larger. In 2002-03, the last year for which complete figures are available, gross outflows from London were around 375,000 and gross inflows to London were around 340,000. In total, these flows in one year are equivalent to 10 per cent of London’s population.³

³ HM Treasury analysis of Office for National Statistics data.

Box 4.2 Migration into London

London's openness to migrants is a key feature both of its economy and of its success. Many of the people now working in the capital are not originally from London. In the UK as a whole there has been a persistent movement of people from the North of the country to the South. London itself typically receives around 150,000 people a year from the rest of the UK; there are also significant flows into the wider South East region.

In addition to domestic migrants, there are also a growing number of people coming to London from other countries. Over the last decade, gross inflows of international migrants have doubled from around 100,000 a year in the early 1990s to around 200,000 now. The continued supply of people of working age from all sources has allowed employment to keep growing, compared to other areas constrained by an ageing workforce.

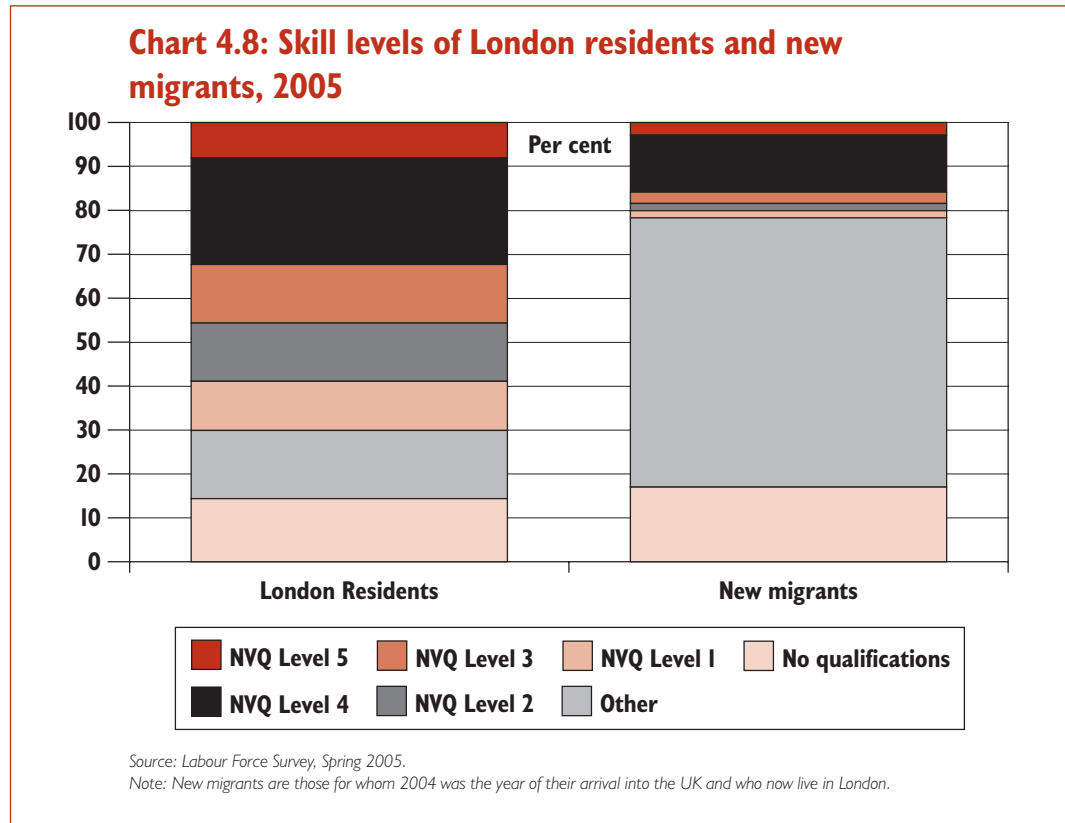
Inflows of migrants have been of major importance for London's economic growth. Box 4.1 describes how the combined effect of globalisation and technological progress has driven London to build on its comparative advantages and become an increasingly high-value knowledge based economy. As the London economy has restructured, the supply of highly skilled staff has tightened significantly, and the premium that workers are paid as a reward for their skills (the skills premium) has risen as a result.

While a higher skills premium will encourage more people to invest time and money into their education, significant changes to the balance of skills in the domestic labour force can only be accomplished over a long period. Continuing skills shortages can act as a barrier to the expansion the high value add businesses, and substantial skills premiums can also lead to widening inequality.

Migration, however, provides an additional source of skilled labour. Migrants have been an essential source of new skills, and their presence has ensure that there have been few skills gaps as the London economy has adjusted. Skilled internal migrants are especially important, because they operate within a national labour market and can quickly respond to any changes to skills demand in London.

Two recent studies of the effect of immigrants on the UK labour market found no evidence that immigrants have any effect on either the employment chances of domestic workers or local wage rates.^a

^a Dustmann, C.; Fabbri, F.; and Preston, I. (2005) *The Impact of Immigration on the British Labour Market*, The Economic Journal 115 (November): F324-F341, and Gilpin, N.; Henty, M.; Lemos, S.; Portes, J.; Bullen, C. (2006) *The Impact of Free Movement of Workers from Central and Eastern Europe on the UK labour Market*, Department for Work and Pensions Working Paper 29.



4.25 The characteristics of international migrants are markedly different from those born in the UK or who have lived in London for a long time. Chart 4.8 shows that a significant proportion of new international migrants to London have qualifications that are not officially recognised.

4.26 Box 4.2 describes how migration is a significant net benefit to both the London and national economies. The scale of population flows into and out of the capital is another factor distinguishing London from other parts of the UK, and is an important factor in understanding both how the London economy has developed and how it will continue to do so in the future.

LABOUR MARKET IMPERFECTIONS

4.27 Over time, most regional variations in employment and worklessness rates tend to diminish as the national labour market adjusts to balance the demand for and supply of labour in different parts of the country.

Labour mobility 4.28 Research into regional mobility in the UK has found that although mobility is marginally higher among the unemployed than the employed, it is much higher amongst the highly qualified than those with low or no qualifications. In addition, job-related mobility is due to most people finding a job and then moving rather than moving to find work. But recruitment for low-skilled jobs tends to take place locally rather than nationally. This may inhibit regional mobility by those with lower skills.⁴

⁴ Gregg, P. Machin, S. and Manning, A (2004) *Mobility and Joblessness in Card*, D. Blundell, R and Freeman, R. (eds) *Seeking a Premier League Economy*, NBER, University of Chicago Press.

Housing and tenure

4.29 Housing is a critical factor in understanding labour mobility and employment. Unresponsive housing supply, combined with Londoners' housing preferences, is reflected in the pattern of house prices, with average house prices in London being significantly higher than the national average, and those in Inner and west London commanding a premium within this. The housing market in Inner London is becoming more polarised, with high concentrations of social housing (around 38 per cent of the Inner London dwelling stock, compared to 19 per cent nationally) in some of the most expensive locations in London. In some London boroughs social housing is the dominant housing tenure, often concentrated on large mono-tenure estates.

Social housing 4.30 The Strategy Unit reported that households in lower social groups in London move less frequently than their counterparts elsewhere (4 per cent each year compared to around 11 per cent).⁵ Comparisons of mobility by tenure show that those in social housing, both local authority and housing association, exhibit comparatively low levels of mobility, with local authority tenants having a migration rate between regions lower even than owner-occupiers.⁶ There are characteristics of social housing that may influence this behaviour. The subsidy provided through a social housing tenancy at a sub-market rent is tied to the property, not the individual, and is not subject to review – even though tenants' circumstances may change dramatically over time. So a tenant will continue to benefit from the same sub-market rent so long as they remain in that property. Social tenants can also accumulate entitlements through their tenure, such as Right to Buy or Right to Acquire, which they would lose if they were to move to a different tenure.

4.31 This means that for social housing tenants, mobility can be heavily dependent on the availability and accessibility of alternative social housing provision in the area they would wish to move to. Even within their own area tenants may have limited choice, depending on their landlords' allocation policies. The evidence suggests that patterns of movement within the social housing sector are driven by what households are offered, rather than what they would necessarily choose, given greater opportunities.⁷ This can make it more difficult for those in social housing to move to access employment opportunities elsewhere.

CONCLUSION

4.32 The labour market differences between London and the rest of the country extend beyond differences in the characteristics of the respective workforces. Compared to the rest of the country, London has experienced (and continues to experience) a different pattern of industrial and occupational change, and significant domestic and international migration flows.

4.33 The evidence on gains to work and vacancies in London suggests that there may be an excess supply of low-skilled labour in the capital. There does not appear to be a general labour demand problem, as London continues to create new jobs. However these jobs tend to be in high value-added activities and may not be well suited to the skills and capabilities of some London residents. Barriers to mobility, particularly among certain lower income groups, can inhibit the labour market adjustments that might otherwise take place.

⁵ *The London Project: Analytical Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2003, p.46.

⁶ *Housing Policy and Labour Market Performance*, DETR, December 2000

⁷ *Who moves and why? Patterns of mobility in the housing association sector in London*, Christine Whitehead and Youngha Cho, Cambridge, 2003

4.34 Overall it appears that skills and mobility are key issues in understanding the persistence of relatively high rates of worklessness in London, and that they may contribute to some or all of the 'London factor' identified in Chapter 3. Further work needs to be done to establish their relative importance and the implications for policy.

4.35 The existing policy context is described further in Chapter 5.

5

POLICY RESPONSES IN LONDON

Summary

Since 1997, the Government has combined economic stability and moves to increase labour market flexibility with positive action to tackle unemployment and economic inactivity. This has included the introduction of a National Minimum Wage, targeted labour market programmes to help people move from welfare into work, and a range of interventions to tackle particular barriers to work in areas such as skills and childcare.

Policies intended to raise the financial gain to work can be less effective in London because housing costs and costs of working can be higher in the capital, compounding problems for some groups such as lone parents. Recognising this, the Government has already taken steps to improve the affordability and availability of childcare, improve the gain to work for lone parents through the In Work Credit, and to increase the previously lower take-up of tax credits.

The Government's active labour market policies have to cope with significant numbers of people moving into and out of work in London. The relative performance of the New Deal and other initiatives appears lower in London. This may reflect London's more challenging client group and its different labour market, although other factors, such as higher Jobcentre Plus staff turnover, may also be important.

The Government is already taking action to address childcare, skills and housing issues in the capital. The Government is also piloting a new local housing allowance and has improved the processing of Housing Benefit claims in London, helping to reduce barriers to work among low-income groups.

5.1 Since 1997, the Government has combined employment growth with labour market stability and positive action to tackle the problems created by long-term unemployment and inactivity. Its approach has been based upon a strategy of:

- promoting macroeconomic stability through a new monetary and fiscal framework, including operational independence for the Bank of England, and the application of strict fiscal rules;
- ensuring a labour market that is sufficiently flexible to encourage job growth but which also guarantees basic employment rights;
- ensuring that work pays more than benefits through the introduction of the National Minimum Wage, a series of reforms to the tax and benefit systems, and the introduction of tax credits;
- active labour market policies to help people move from welfare to work, ensuring that everyone is able to share in economic success while also contributing to overall economic stability by expanding the effective supply of labour; and
- a range of other policies and programmes to help individuals overcome barriers to work, such as strategic investments in skills and childcare.

5.2 As explained in Chapter 1, this national policy framework has been very successful. Since 1997, employment rates have increased in every UK region, although only marginally in London, and have increased fastest among many previously disadvantaged groups.

5.3 The previous chapters have shown the contribution that population and labour market factors make in explaining lower employment rates in London. But the Strategy Unit's *London Project: Analytical Report*¹ and *London Project Report*² also raised important questions about the effectiveness of some national policy approaches in the particular context of London. The reports highlighted:

- how work incentive policies may be less effective in guaranteeing a sufficient gain to work in London;
- how labour market programmes in London perform less well, serving a population with more complex needs, in a labour market where employers have a wider range of recruitment options when filling low skilled vacancies;
- inadequacies in the provision of other services such as basic skills courses and childcare; and
- how slower Housing Benefit processing times created additional barriers to moving into work.

5.4 This chapter considers in more depth these and other issues related to the effectiveness of national policies in the London context.

WORK INCENTIVES

5.5 The Government believes that work is the best route out of poverty and is committed to making work pay by improving incentives to participate and progress in the labour market. The key national policies for achieving this are the Working Tax Credit introduced in April 2003 alongside the Child Tax Credit and the National Minimum Wage. These policies work together boost in-work incomes, improve financial incentives to work and tackle poverty among working people.

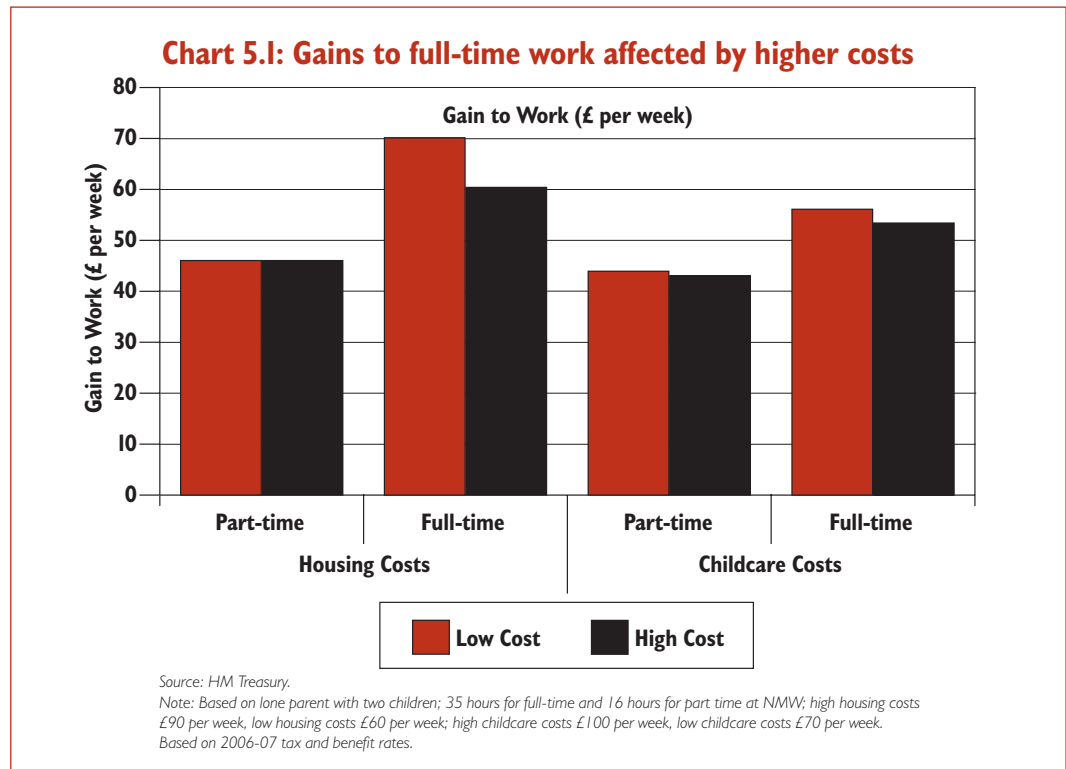
5.6 The National Minimum Wage guarantees a fair minimum income from work. The rate is currently £5.05 per hour for adults, and will rise to £5.35 in October 2006, with lower rates for 18-21 year olds and 16-17 year olds. The Working Tax Credit provides financial support on top of earnings for households with low incomes, ensuring a minimum income in work. For example, in April 2006, a family with one child and working full time (35 hours) can expect a minimum income of £265 per week as a combined effect of wages, tax credits and Child Benefit.

5.7 Chapter 4 was concerned with the effect that wages in London have on gains to work and showed that for some low earners, the real gains to work in London are lower than in the rest of the country. It is sometimes argued that national policies aimed at improving work incentives contribute to this because they are less effective in London than elsewhere. While higher housing and childcare costs, which are common in London, can affect incentives to work, the picture is not straightforward. This is because Housing Benefit and the childcare element of Working Tax Credit provide in-work support for housing and childcare, helping to maintain work incentives.

¹ *The London Project: Analytical Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2003

² *The London Project Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2004

Gains to work 5.8 To help illustrate the effect of higher housing and childcare costs on gains to work, Chart 5.1 shows how gains to work are affected by housing and childcare costs. The chart shows the gain to work for a lone parent moving into part-time and full-time work at the National Minimum Wage is the case where childcare costs and housing costs are ‘high’ or ‘low’.



5.9 As Housing Benefit can be paid in and out of work, it can protect work incentives for low income families. Chart 5.1 shows that the gains to work for a lone parent working part-time are unaffected by housing costs. A lone parent working full-time does see their gain to work reduced by higher housing costs, but it remains positive at around £60 a week. The reason the family sees a fall in their gain to work is that in-work, their income is high enough that they are no longer eligible for Housing Benefit and they have to pay their Housing Costs out of their net income.

5.10 Similarly, for families incurring childcare costs the childcare element of the Working Tax Credit helps to maintain work incentives. A lone parent working full-time and facing childcare costs of £100 a week has a £3 per week lower gain to work than the same family with childcare costs of £70. On the other hand, for a lone parent working part-time, the same difference in childcare costs makes less than a £1 difference in the weekly gain to work.

5.11 The illustration above shows that while high housing and childcare costs can affect gains to work, the tax and benefit system helps to protect the work incentives of many of those with the lowest gains to work, even in London. The evidence of lower gains to work in Chapter 4 is therefore not necessarily a sign that policy is failing to properly support low earners. Lower gains to work in London may, therefore, be associated with the idea of an excess supply of low-skilled labour.

Take-up 5.12 Historically, take-up of tax credits, and in particular the Working Families' Tax Credit, has been lower in London than elsewhere. There is evidence that the situation has improved considerably with the introduction of Child and Working Tax Credits. Statistics published in March 2006 by HMRC showed that although 65 per cent of eligible working families in London claimed tax credits, 79 per cent of the money was claimed the Child Tax Credit. This means that those who are not claiming are on average those with lower entitlements. While the proportion of families claiming is lower in London than elsewhere in the UK, the proportion of money claimed is closer to the national average, and is higher than in the East of England. This is consistent with low-income families in London being no less likely to claim tax credits than those in other regions that are on average as prosperous, and possibly the UK as a whole.

ACTIVE LABOUR MARKET POLICIES

5.13 The Department for Work and Pensions (DWP), through Jobcentre Plus, provides a range of welfare to work programmes aimed at supporting unemployed and inactive people to move towards, and into, employment. These include a suite of national programmes aimed at specific client groups, including the New Deal programmes, supplemented by targeted initiatives tailored to meet the needs of people living in the most deprived areas of the country. Jobcentre Plus contracts with over 2,000 providers across the public, private and voluntary sectors to deliver labour market programmes.

Jobcentre Plus 5.14 Through its office and call centre network and its Personal Advisers, Jobcentre Plus provides an integrated work-focused service to people of working age, both unemployed and economically inactive. Personal Advisers provide a frontline service to customers, delivering work-focused interviews aimed at supporting people with their jobsearch, identifying required support and referring people to employment programmes. Participation in these labour market programmes can be on a voluntary or mandatory basis depending on a person's circumstances.

Labour market programmes in London

New Deal 5.15 The New Deal is available across all the countries and regions of the UK. The New Deal provides mandatory support for young people who have been claiming Jobseeker's Allowance for over 6 months, and for adults who have been claiming for over 18 months. The New Deal also provides voluntary, targeted, provision for lone parents, disabled people, the over 50s, and partners of people claiming key benefits. Box 5.1 provides an overview of the New Deal programme.

5.16 Since its launch in 1998, over 3.4 million people have participated in the New Deal, of whom 538,000 (16 per cent) have been within the London region. To date, the New Deal has helped over 1.7 million people to find work, of whom 215,000 (13 per cent) have been within London.

Box 5.1: Welfare to Work Support in London - New Deal

New Deal for Young People for 18 to 24 year olds claiming Jobseeker's Allowance (JSA) for at least six months. The four-month Gateway period is followed by a choice of four full-time options: subsidised employment; full-time education/training; a job in the Environment Task Force; or a job in the voluntary sector. There is no "fifth option" to remain on benefits.

New Deal 25+ for 25-49 year olds claiming JSA for 18 out of the previous 21 months. The Gateway period of four months is followed by a period of intensive activity consisting of individually tailored packages of support such as work experience, work placements, occupational training, and motivational skills, underpinned by intensive jobsearch.

New Deal for Lone Parents provides wide-ranging support through a personal adviser, including help with jobsearch, skills, childcare, or training opportunities.

New Deal for Disabled People provides support for people in receipt of a disability or health-related benefit through a network of Job Brokers delivered by private and third sector organisations.

New Deal 50+ helps unemployed and economically inactive people and their dependent partners who have been claiming key benefits for more than six months.

New Deal for Partners is available for partners of people who are claiming key benefits, and offers the same support as the New Deal for Lone Parents.

Employment Zones 5.17 Employment Zones (EZs) were introduced in April 2000 in fifteen areas of the UK experiencing high concentrations of long-term unemployment. Delivered by private and third sector organisations, EZs offer an alternative model of delivering labour market programmes, with a key feature being flexible customer funding. Together with a personal adviser, the customer identifies the help they need to move into employment. There is no central prescription other than the requirement for all customers to attend fortnightly interviews with their adviser.

5.18 EZs originally targeted unemployed people aged 25 and over who had been claiming Jobseeker's Allowance (JSA) for at least 12 months. Participation is mandatory for this client group. EZs were expanded in October 2003 to include lone parents in receipt of Income Support, unemployed people aged 18-24 otherwise returning to New Deal, and Jobseeker's Allowance claimants entitled to early entry. For young people, participation is mandatory. For lone parents, participation is voluntary.

Area-based labour market initiatives 5.19 In addition to the national New Deal programmes and Employment Zones, there are a number of labour market initiatives targeted at meeting the specific needs of the more deprived areas of the UK, including areas within London.

5.20 Action Teams for Jobs were launched in June 2000 with the aim of increasing employment rates among disadvantaged groups in deprived areas. They use flexible, locally planned responses and delivery includes: the use of discretionary funding; targeting areas and groups in most need; working in informal partnerships with the private and voluntary sectors; and working closely with employers. There are 11 Action Teams in London.³

5.21 Working Neighbourhood pilots were begun in April 2004 to provide a programme of intensive support in 12 neighbourhoods with very high concentrations of worklessness. One of these pilots is in London. The pilots combine earlier and more intensive intervention with community-based delivery and additional resources to overcome barriers to employment.

³ Jobcentre Plus run Action Teams in Greenwich, Hackney, Islington, Lambeth, Lewisham and Waltham Forest. Private sector providers run Action Teams in Brent, Haringey, Newham, Southwark and Tower Hamlets.

5.22 There is also a range of support aimed at meeting the specific needs of London's ethnic minority population:

- Ethnic Minority Outreach programmes are finding ways to reach ethnic minorities who are outside the labour market and have not been using Jobcentre Plus services. Outreach providers are a mix of private and third sector organisations;
- Ethnic Minority Flexible Fund resources are available in London local authority wards with high ethnic minority populations. The fund helps pay for innovative programmes to address local barriers to work for ethnic minority groups; and
- Fair Cities are employer-led pilot projects based on the identification of best practice models from UK, Europe and the USA. They complement existing programmes and initiatives run by Jobcentre Plus and Learning and Skills Councils, providing a 'pipeline' to local jobs for disadvantaged people, mainly ethnic minority groups. There is a Fair Cities pilot in Brent.

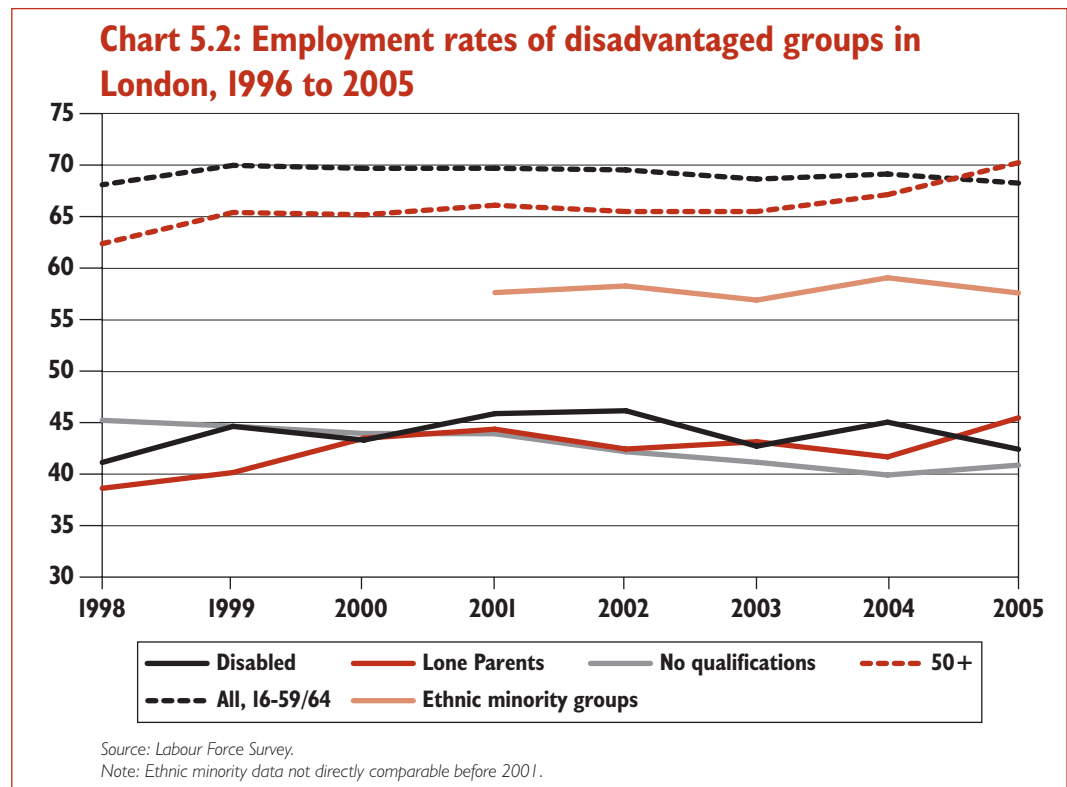
Financial incentives 5.23 The Government recognises that barriers to work can be more difficult to overcome in some areas of the country, and that work incentives can be particularly affected by the higher cost of living in areas such as London. To address this, financial incentives to encourage worksearch and to assist with the costs of the transition to work are being developed and their effectiveness tested. These include:

- Work Search Premium pilots, paying a £20 per week premium for 26 weeks to encourage lone parents who have been on Income Support for over a year to undertake intensive worksearch;
- In Work Credit pilots, which provide a 12 month £40 per week payment to lone parents to aid the transition to work. The In Work Credit pilots were extended to cover the whole of London from April 2005;
- the In-Work Emergency Fund, aimed at helping lone parents remain in employment by meeting the costs of emergencies during the first 60 days in employment;
- flexible funds are being piloted to enable Personal Advisers to tailor support to target specific barriers faced by lone parents;
- Employment Zone contractors are offering flexible in-work assistance to customers who require it; and
- Job Grant, available nationally, is a one-off payment to help with the transition to work and available to people who have claimed working age benefits for 26 weeks or more and start full-time work.

5.24 Since October 2003, the Government has also been testing a new strategy, Employment Retention and Advancement (ERA) pilots, for people in low-paid employment or who have moved into work from benefits. Alongside financial incentives to encourage retention in work, ERA is testing the effectiveness of continued support, for up to 33 months, from a dedicated Advancement Support Adviser.

Impact of labour market programmes in London

5.25 While London's employment rate has fallen marginally since 1997, there have been some significant improvements in the employment rates of some of the more disadvantaged groups targeted by the New Deals and other labour market programmes. As Chart 5.2 shows, there has been a significant increase in employment rates for lone parents and the over 50s in London since 1997, although there has been little overall improvement for disabled people and people from ethnic minorities.



5.26 London has enjoyed the same large-scale reductions in people remaining on unemployment benefits over the longer term enjoyed by the rest of the country (see Chart 5.2). The number of 18 to 24 year olds claiming Jobseeker's Allowance for over six months has fallen from 33,200 in January 1997 to 10,500 in January 2006. The number of adults claiming Jobseeker's Allowance for over 18 months has fallen from 92,000 in January 1997 to 15,800 in January 2006.

Impact of the New Deal

5.27 Repeated independent evaluations have demonstrated the positive impact of the New Deal at a national level. In 2000, the National Institute of Economic and Social Research (NIESR) concluded that, without the New Deal for Young People, the level of long-term unemployment would have been twice as high.⁴ Further studies have shown NDYP reduced overall youth unemployment by between 30,000 and 40,000,⁵ that young men are now 20 per cent more likely to find work as a result of the New Deal, and that the social benefits of NDYP outweigh the costs.⁶ Independent evaluation of New Deal for Lone Parents suggests that "the programme doubles the employment chances of participants: 50 per cent of participants entering work compared to 26 per cent of non-participants – an additional impact of 24 percentage points."⁷

⁴ *The New Deal for Young People: implications for employment and the public finances*. NIESR, December 2000.

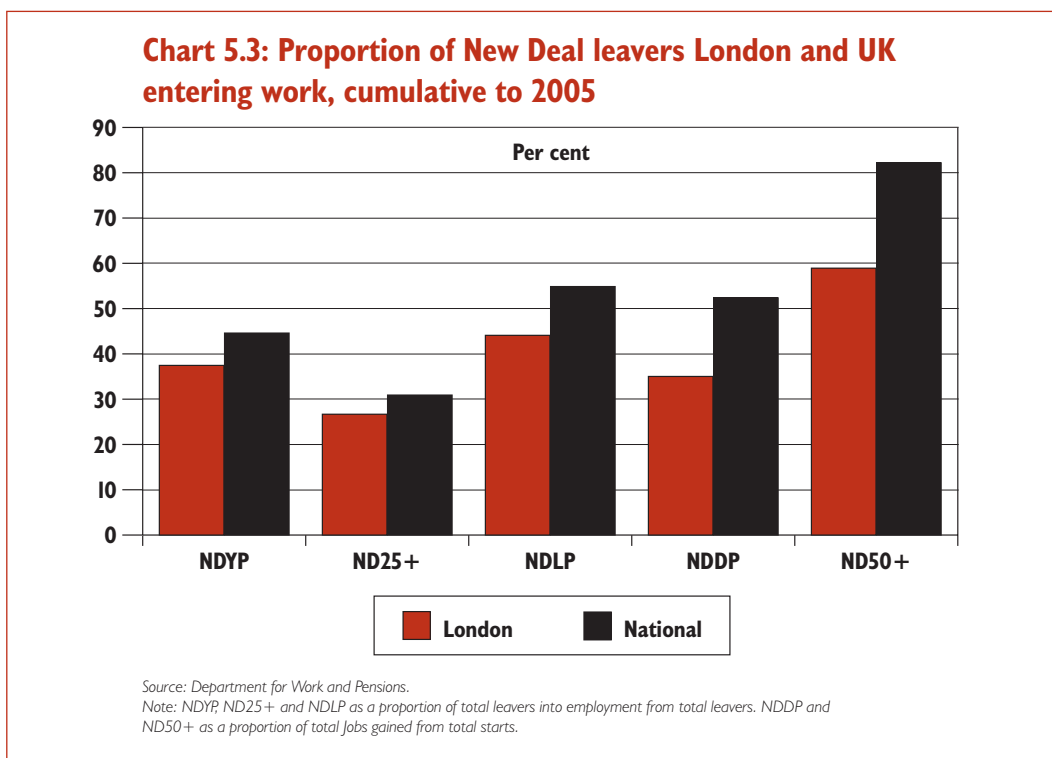
⁵ *New Deal for Young People: evaluation of unemployment flows*, Wilkinson, D. Policy Studies Institute, 2003.

⁶ *Active labour market policies and the British New Deal for unemployed youth in context*, Van Reenen, J., in *Seeking a premier league economy*, Blundell, R., Card, D. and Freeman, R. (eds), University of Chicago Press. June 2004.

⁷ *New Deal for lone parents: second synthesis report of the national evaluation*. Centre for Analysis of Social Policy, University of Bath (Evans, Eyre, Millar, Sarre), June 2003.

5.28 Although there has been no separate assessment of the impact of the New Deal in London, there is evidence that the New Deal for Young People has significantly boosted exit rates from unemployment in all regions, with London ranked in the middle in terms of New Deal effectiveness.⁸

5.29 Given the greater concentration of groups with labour market disadvantages in London, labour market programmes in the capital might be expected to have more difficulty reaching the levels of effectiveness seen in the rest of the UK. There are indications that this is the case. The proportion of New Deal leavers in London who find work through the New Deal is significantly lower than the national average, as Chart 5.3 illustrates. The proportion of leavers moving into jobs is 7 percentage points lower for NDYP clients, 10 percentage points lower for NDLP clients, and 24 percentage points lower for ND50+ clients, than nationally.



5.30 There is also evidence that, on average, New Deal participants in London spend longer on the New Deal than in other regions. Table 5.1 shows that all client groups spend significantly longer on the New Deal than the national average, and women in particular have significantly longer durations than in any other region. Women in London spend 25 days longer on the New Deal than average, and men between 25 and 29 spend nearly two months longer than in the South West. Although there are a number of potential reasons for this, this scale of difference could indicate that it is more difficult to move from the New Deal to work in London.

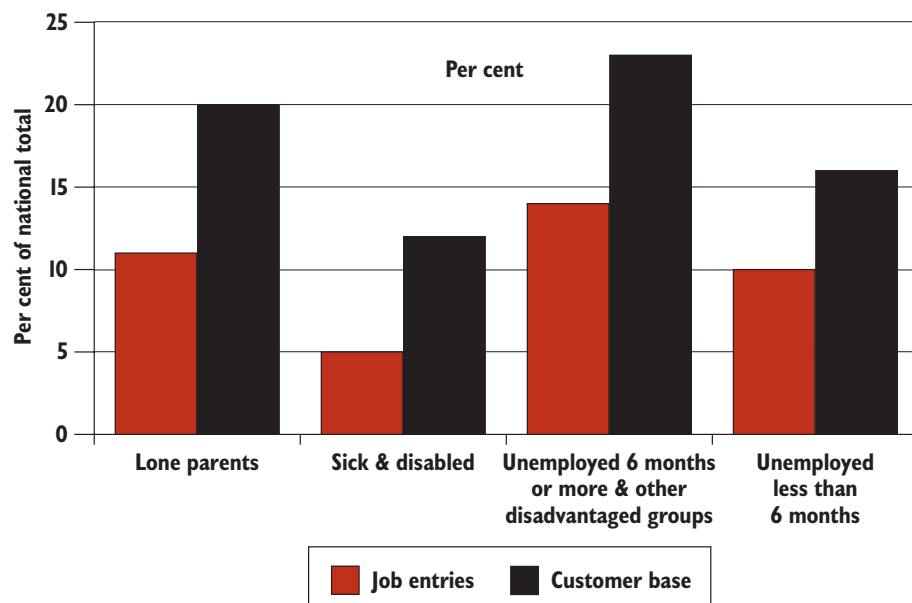
⁸ How well has the New Deal for Young People worked in the UK? McVicar, D and Podvinsky, J. Northern Ireland Economic Research Centre, April 2003.

Table 5.1 Mean duration of New Deal spells, by region, age group and gender, days

Region	Male 18-24	Male 25-29	Female 18-24	Female 25-29
London	119	162	110	125
South East	82	113	75	89
East Anglia	88	117	79	87
South West	81	108	73	88
West Midlands	103	145	92	107
East Midlands	96	123	85	102
Yorkshire and Humberside	98	130	86	104
North West	99	130	85	99
North	105	130	89	102
Wales	95	130	80	91
Scotland	93	126	80	88
Northern Ireland	117	167	88	95
UK	97	131	86	101

Source: *How well has the New Deal for Young People worked in the UK?* McVicar, D and Podvinsky, J. Northern Ireland Economic Research Centre, April 2003.

5.31 The picture of generally lower outcomes from programmes in London is also reflected in Jobcentre Plus' statistics on Job Entries. As chart 5.4 shows, London's share of Job Entries through Jobcentre Plus is significantly lower than would be expected given London's share of the national benefit caseload. Again, this is reflected across all client groups. Job entries for sick or disabled people in London – at 5 per cent of the national total – do not reflect London's 12 per cent share of the national customer base. Similarly, London has 20 per cent of the lone parent customer base, but only an 11 per cent share of lone parent job entries.

Chart 5.4: London job entries and customer base as a proportion of national totals, 2004-05

Source: *Jobcentre Plus District Job Entry Performance, 2004-05.*

Potential causes of lower outcome rates **5.32** While we might expect that the higher incidence of labour market disadvantage in London would make it harder to help people into work through labour market programmes, there are a number of other factors that might also contribute to differences in outcomes in London compared with the rest of the country. These include:

- findings from Chapter 4 suggesting more difficult labour market conditions for New Deal participants in London, with greater competition in those sectors and occupations on which benefit claimants have traditionally focused;
- employment being relatively less attractive to some New Deal participants in London. This could be because of lower gains to work for some, as suggested by the findings in Chapter 4; and
- London-specific delivery factors, such as recruitment difficulties or high staff turnover rates reducing expertise and continuity of contact, or weaker links with local employers that may affect the standard of programme support.

REMOVING BARRIERS TO WORK

Childcare

5.33 In the past, a lack of suitable, high quality, affordable childcare has acted as a barrier to the labour market participation of parents with caring responsibilities, especially women. It has also meant that many children have missed out on the social and developmental benefits that high quality childcare can provide. This can be especially important for children from otherwise disadvantaged households.⁹ By contrast, ensuring that all families have access to childcare that meets their needs can improve both the employment opportunities for parents and the development needs of children. The Government's Ten Year Childcare Strategy, published in December 2004, recognised this opportunity and committed the Government to ensuring that every family has access to suitable, high quality, affordable childcare.¹⁰

5.34 This commitment is especially important in London where:

- employment rates among women in London are the lowest of any region in the country (63 per cent in London compared with almost 70 per cent for the UK);
- child poverty rates in London are the highest of any region in the country (24 per cent compared with 19 per cent for Great Britain¹¹);
- childcare availability can be a particular problem. The number of childcare places in London has almost doubled since 1999 but, as Chart 5.5 below shows, London has the fewest childcare places per 100 children of any region of the country. Survey evidence also suggests that parents from some ethnic minority groups with large populations in London experience additional difficulties finding childcare suitable to their needs;¹² and

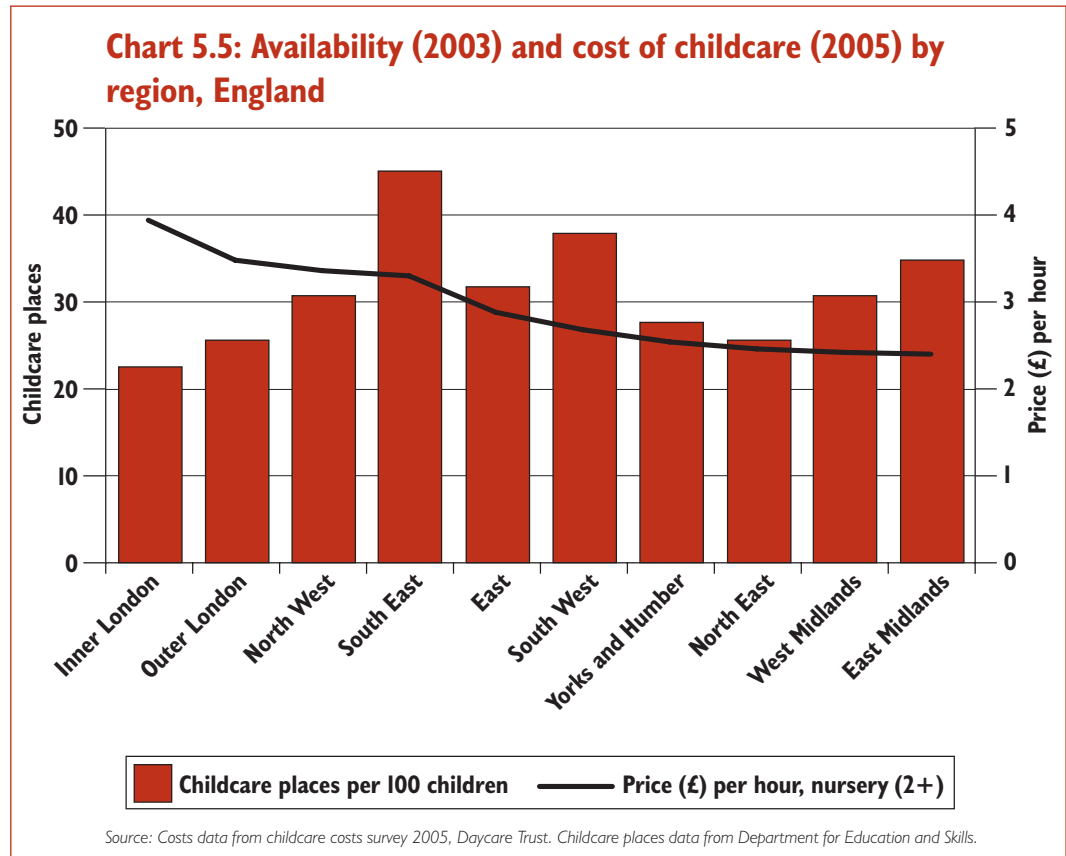
⁹ For evidence of the developmental benefits for children of high quality childcare see *A Literature Review of the Impact of Early Years Provision on Young Children, with Emphasis given to Children from Disadvantaged Backgrounds*, Edward C Melhuish, prepared for the National Audit Office, and *The Effective Provision of Pre-School Education (EPPE) Project: Findings from the Pre-School Period, Summary of Findings*, Sylva, K., Melhuish, E., Sammons, P., Siraj-Blatchford, I., Taggart, B., Elliot, K., Institute for Education, 2003, DFES Research Brief RBX 15-03.

¹⁰ *Choice for parents, the best start for children: a ten year strategy for childcare*, HM Treasury, December 2004.

¹¹ *Households Below Average Income, 2004/05*, Department for Work and Pensions, 2006. Figures refer to average rates over a three year period from 2002-03 to 2004-05

¹² *Use of childcare among families from minority ethnic backgrounds*, Bryson et al, National Centre for Social Research, 2005.

- childcare costs are higher in London than elsewhere. One estimate suggests that costs for a nursery place for a child under two years of age are around 34 per cent more than across England as a whole.¹³ The cost of childcare in London compared with other regions is also shown in Chart 5.5 below. Higher childcare costs need not necessarily imply that childcare is less affordable for everyone in London compared to elsewhere, as ‘affordability’ is a function of the incomes of parents in London as well as higher costs. However, the Strategy Unit *London Project Report* did note that national limits on eligible childcare in tax credit claims could be acting as a barrier to work for some parents in London.



5.35 The Ten Year Childcare Strategy built on investments the Government has already made since 1997. Although most of the measures in the strategy will benefit parents across the country, some of the measures are likely to be of greater benefit to Londoners, and other measures have been specifically designed to address the additional needs of Londoners.

5.36 The Childcare Bill now before Parliament places a new duty on Local Authorities to secure a sufficient supply of childcare to meet the needs of working families. Local Authorities will be required to assess the childcare market in their area and work with the Private, Voluntary and Independent sector to address situations where supply does not meeting demand. The Government is already making progress in rolling out new children’s centres in London and across the country. These centres will build on the success of other programmes and offer a range of early years, health and family support services to young children in all of the most disadvantaged areas by 2008, with a centre in every community by 2010.

¹³ Annual Costs Survey, Daycare Trust 2005.

5.37 The aim of increasing the quality of childcare without compromising affordability is a particular challenge in London, where childcare is already expensive. However London is already benefiting from the changes proposed by the strategy:

- Childcare Affordability Pilots: the Government is contributing £11 million to a £33 million set of joint London Development Agency and Department for Education and Skills three-year Childcare Affordability Pilots. The Pilots run from November 2005 to March 2008, and are the largest region specific initiative programme of their kind in England. They will test a range of approaches aimed at improving the accessibility and affordability of good quality childcare for lower income families, with an expected 10,000 funded places to be offered in total;
- changes in the childcare element of Working Tax Credit: the Government has already extended the amount of eligible childcare that can be claimed, and, effective from April 2006, will raise the percentage of eligible childcare costs that can be claimed from 70 to 80 per cent. These are national changes, but are of most help to those on low incomes who face high childcare costs where affordability issues are most prominent; and
- the Transformation Fund: this will encourage quality without compromising affordability, by training a new generation of childcare workers and giving financial support to providers who hire workers with higher-level skills. Under the scheme, payments to providers in London can be higher than elsewhere to reflect the higher staffing costs in London.

Skills

5.38 Earlier chapters noted the difference in the skills profile of Londoners and the skills needs of London businesses. According to the National Employer Skills Survey London has the lowest proportion of employers with any skills gaps (14 per cent, 4 per cent lower than the next regions). London also has the lowest proportion of staff described as lacking proficiency (5 per cent).¹⁴ This suggests that London's employers experience fewer problems than those in other parts of the country finding the skills they need. This may reflect London's attraction to skilled workers not only from neighbouring regions, but also from the rest of the world. Global changes also place an increased emphasis on having skills to encourage and take advantage of innovation. Employers increasingly require basic literacy, numeracy and IT skills, and the need for team working and communication skills is rising. In the face of these challenges and opportunities increasing the skills of London's least qualified workers is becoming increasingly important.

5.39 Despite improvements over the last few years, the UK still has a large stock of workers with low or no skills, including poor basic literacy and numeracy. This stock of low skills directly accounts for some of the productivity gap with our main competitors, as well as wider impacts on social welfare. *Productivity in the UK 6: New Evidence and the Government's approach* published alongside Budget 2006 sets out the latest evidence on skills and productivity.

¹⁴ *National Employer Skills Survey*, Learning and Skills Council, 2004.

5.40 The Government is committed to improving the skills of the UK's workforce. Alongside the 2005 Pre-Budget Report, Lord Leitch, a former chief executive of Zurich Financial Services and the chairman of the National Employment Panel, published *Skills in the UK: The long-term challenge*¹⁵ detailing the interim findings of his independent review of the UK's long-term skills needs. It highlighted that, though skills levels have improved the UK must urgently raise skills levels still further and set itself a greater ambition to have a world-class skills base by 2020. The next phase of the Leitch Review will build on this analysis and address:

- the skills profile that the UK should aim to achieve by 2020 to support the needs of the economy and society over the longer-term;
- the appropriate balance of responsibility between Government, employers and individuals for the action required to meet this level of change; and
- the policy framework required to support this.

5.41 The Review will report its conclusions and recommendations to the Government in Summer 2006.

5.42 Sir Andrew Foster was also commissioned by Government to review further education (FE) colleges in England. The Review concluded in November 2005 and highlighted the potential of the FE sector to improve employability and supply economically valuable skills.¹⁶ Building on this report, and to ensure further education colleges and training providers in England are ready for more stretching skills ambitions, the Government is setting out a far-reaching programme of reform. The details of this reform programme will be contained in a White Paper to be published later this month.

5.43 Against the background of these two Reviews the Government is working in partnership with social and economic partners to deliver its Skills Strategy.¹⁷ The main objectives of the Skills Strategy are to improve national productivity and to improve the abilities and prospects for both individuals and employers. A further goal is to use skills as one of several key drivers to improve regional productivity and to close the gaps in performance between English Regions. A key part of the Strategy was the creation of Regional Skills Partnerships (RSPs) to ensure employers' skills and business support needs are integrated into regional economic development plans. The London RSP, has developed a Regional Action Plan setting out the broad strategic direction to ensure that the business and skills challenges facing the capital can be met. Through delivery of the Action Plan, RSP members are jointly committed to targeting resources towards its twin aims of inclusion and productivity.

5.44 An example of the impact of the London Skills Partnership is their response to the massive demand for English language training for speakers of other languages in London. To improve the provision the London Regional Skills Partnership has developed a 3 year Action Plan for English language training in London. This will address not just language needs, but also people's aspirations for studying, working and integrating into London life. The work-focused element will offer help to those not currently able to gain employment and those who are working but need to develop their skills.

¹⁵ *Skills in the UK: The long-term challenge*, The Leitch Review of Skills, December 2005.

¹⁶ *Realising the Potential, a review of the future role of further education colleges*, Sir Andrew Foster, November 2005.

¹⁷ *21st Century Skills, Realising our Potential*, Department for Education and Skills, July 2003; and *Skills: Getting on in business, getting on at work*, Department for Education and Skills, March 2005.

5.45 The Government will consider the options for improving the management of skills in London and is consulting on the scope for devolving further strategic and delivery responsibilities to the GLA. The Minister for Local Government and Communities will respond to the outcome of ODPM's consultation in the spring.

Housing

5.46 Chapter 4 identified the impact of social housing tenures on mobility and concentrations of worklessness. This situation is now changing as choice-based letting schemes are introduced by more social landlords. These enable tenants to begin to make the trade-offs between the availability and desirability of properties. The MoveUK scheme developed by ODPM, DWP and the devolved administrations aims to increase regional mobility in the social rented sector by offering tenants and their advisors access to geographic information on the availability of social housing, jobs and other general data on local services.

Housing supply 5.47 *The Government's Response to Kate Barker's Review of Housing Supply*,¹⁸ published alongside the 2005 Pre-Budget Report, set out a comprehensive package of proposals to help deliver investment in the infrastructure necessary to support housing growth, and to reform the mechanisms, particularly planning, by which new housing and infrastructure are delivered. As with skills, the Government is considering the case for devolving further responsibilities to the GLA. A cross-cutting review into supporting housing growth will feed into the 2007 Comprehensive Spending Review (CSR). This will enable coordination across government of the strategic delivery of local and regional infrastructure necessary to support additional housing. The CSR will also set out ambitious plans for increasing social housing supply. This will build on the increased funding provided through the 2004 Spending Review that will deliver an additional 10,000 new social homes a year by 2007-08 compared with 2004-05, a 50 per cent increase.

Housing Benefit 5.48 The structure and effective delivery of Housing Benefit are also important factors in improving labour market mobility and labour participation. The Government has initiated a comprehensive reform programme to address the complexity of the current system, and this has already led to considerable improvements in delivery. In the first half of 2002-03, for example, local authorities in London processed new claims in an average of 81 days. This had improved to 38 days by the first half 2005-06, a reduction of 43 days.

5.49 The Government is also making progress with structural reform of Housing Benefit. The flat-rate Local Housing Allowance (LHA) was first introduced in nine pilot areas between November 2003 and February 2004, and in a further nine areas from April 2005. The LHA provides a more simple, more transparent way of calculating payments. By making payments directly to the tenant rather than the landlord the LHA helps to promote personal financial responsibility and ease the transition to work. Early evidence from the pilots is promising. Building on this evidence, the Government is currently consulting on proposals to extend the LHA across the country.

¹⁸ *The Government's Response to Kate Barker's Review of Housing Supply*, HM Treasury, December 2005.

CONCLUSION

5.50 By introducing the National Minimum Wage, tax credits, targeted labour market programmes to help people move from welfare into work and a range of interventions to address particular barriers to work the Government is tackling worklessness for disadvantaged groups across the country. Employment rates have improved substantially for some groups, such lone parents, the over 50s and disabled people, and there have been significant reductions in the number of people claiming Jobseeker's Allowance for long periods.

5.51 In London, however, disadvantaged groups have not experienced the same level of improvement seen in other regions. Work incentive policies may also be less effective at increasing labour supply in London because housing costs and costs of working can be higher. Labour market programmes appear to be less effective at helping people at risk of labour market exclusion into work. The Government has already taken steps to improve the availability, affordability and quality of childcare in London, and to address skills and housing issues in the capital.

5.52 Further work is required to establish the precise reasons behind the difference in labour market programme performance in London, and to link these to the population and labour market factors discussed earlier in this paper. The following chapter summarises the findings of the analysis to date, identifies areas where further work is needed, and sets out the tensions likely to face policy makers and the issues for further consideration.

6

CONCLUSION

Summary

Building on the Strategy Unit's work on London, this document has examined the relatively high rates of unemployment and economic inactivity in the capital, focusing on factors associated with the composition of the population and the operation of the labour market. It has also looked at the effectiveness of existing national policies in the London context.

The Government recognises that simply explaining the higher incidence of worklessness in London is not enough. The fact that some groups have poorer labour market prospects remains unacceptable, regardless of where they live. However, the identification of problems for key groups, such as lone parents, may give important clues as to other labour market issues in London.

Further work is required to confirm the implications of the analysis presented in this paper, and to clarify the objectives and tradeoffs inherent in designing policies to raise employment rates in London. The Government will consider these issues further to inform future policy.

6.1 Chapter 2 set out the extent of the employment challenge in London, which has one of the lowest employment rates of any country or region in the UK, and is the region that has seen the smallest improvement in employment rates since 1997. Over recent years the gap in unemployment rates between London and the rest of the UK has narrowed, but the gap in economic inactivity rates has widened – although a large part of London's higher inactivity results from the city's student population.

6.2 Compared to the overall London population, homeowners and the highly qualified are more likely to be employed. Women are less likely to be in work, and lone parents are much more likely to be economically inactive. Employment rates are also low for people born overseas and for those from ethnic minority groups. These differences are more acute for certain groups, and are especially concentrated in Inner London. Compared to the rest of the UK, worklessness in London is particularly high among parents, lone parents, and those with low and medium skill levels. Moreover, part-time working is less common in London, and there are more households with one or more working-age members not in employment.

6.3 The Strategy Unit's *London Project Report* raised a number of key questions about why employment rates are low in London compared to other parts of the country. This document has examined two of the proposed explanations in more depth – factors related to:

- the characteristics of London's population; and
- the operation of the London labour market.

6.4 It has also examined the evidence on the effectiveness of existing national policies and programmes in the London context.

6.5 The evidence and analysis presented in the previous chapters suggests that both population and labour market factors have important parts to play in explaining employment rates in London. In addition, some national policy solutions appear to be less effective in London, although the reasons for this are not always clear. This chapter summarises the findings of the analysis to date, identifies areas where further work is needed, and sets out the tensions likely to face policy makers and the issues for further consideration.

FINDINGS

1. **Findings from Chapter 3 indicate that much of the difference in employment rates in London compared to the rest of the country can be explained by differences in population characteristics.** HM Treasury analysis and the findings of a number of other studies confirm that, compared to the rest of the country, differences in the composition of London's population are having an impact on employment rates. Views differ, however, as to how much of the difference can be explained in this way. The GLA found that almost all the difference in employment rates was compositional.¹ By contrast, the analysis presented in this paper confirms the *London Project Report's* finding that, in Inner London, there remains a small but significant difference in actual and expected employment rates once differences in characteristics have been taken into account.²
2. **The unexplained difference, or 'London effect', is more pronounced for groups of people with certain characteristics such as lone parents or people with fewer skills, and is apparent across London.**
3. **The 'London effect' could be the result of differences in the labour market, or differences in the effectiveness of policy in boosting labour supply.** Identifying the factors that are driving this, and to what extent, is clearly an important prerequisite for identifying the appropriate policy responses.
4. **Findings from Chapter 4 suggest that features of the London labour market are also contributing to lower employment rates.** Initial analysis suggests that, at the lower end of the labour market, gains to work in London are less for some groups, while vacancies are easier to fill. This is consistent with an excess supply of low-skilled labour, and may explain some of the 'London effect', especially for groups where this effect is more pronounced. For example, employment rates may be lower for workers with fewer skills because of the greater competition for appropriate jobs, and lower gains to work in London may be affecting the labour supply decisions of other groups such as lone parents.
5. **If an excess supply of low skill labour is, in part, responsible for lower employment rates in London, the reasons for its persistence are not certain.** This does not appear to be a problem of aggregate labour demand as there has been strong growth in the number of jobs in London over recent years. It is more likely to be the result of, for example, geographical or occupational mobility constraints facing people living in London and/or evidence of positive benefits to living in London that, for some people, may compensate for a lower likelihood of work. Further analysis is required to confirm initial findings and to understand the reasons why.
6. **Findings from Chapter 5 suggest that some national policy responses are less effective in London for some groups.** Work incentives can be lower in London for some groups, as the effect of the Government's policies to make work pay can be reduced by London-specific factors, such as high housing costs. Labour market programmes in London appear to be less effective at helping people at risk of labour market exclusion into work. The exact reasons for this are unclear, although it appears likely that the population and labour

¹ GLA Economics Working Paper 15, *Worklessness in London, Explaining the difference between London and the UK*, Meadows P, Greater London Authority, 2006.

² *London Project Report*, Prime Minister's Strategy Unit, Cabinet Office, July 2004.

market factors discussed in Chapters 3 and 4 are having a substantial impact. Providers of training and advice for the unemployed and inactive may themselves face greater delivery challenges with recruitment and staff turnover in London. This is not to ignore the often innovative approaches being taken in London to overcome these challenges. Changes are already underway in areas such as childcare, the provision of basic skills, and Housing Benefit administration. In some cases it will take time before the changes are fully implemented, and in others it may take time before the impact of the changes on labour market participation is fully realised.

6.6 Furthermore, understanding why certain groups of Londoners, such as lone parents, face particular barriers to work may also help policy makers to identify challenges which face Londoners more generally – such as the particular nature of childcare needs. In other cases, explaining the nature of the problem of low employment rates in London for certain groups may simply highlight a national problem for that group, and that may require a national solution. In addition, London labour market issues can affect a range of Government policies. For example, lower real gains to work may have an impact on the degree to which work protects a household from poverty.

6.7 At this stage, some of the analysis reported in this document is indicative, and further work is necessary to be able to make definitive judgements about the right direction for future policy. In particular, this will require further analysis of:

- the factors affecting the likelihood of employment;
- the distribution of gains to work in London compared to the rest of the UK and their effect on labour market participation; and
- the factors explaining the performance of labour market programmes.

IMPLICATIONS FOR POLICY

6.8 Chapter 3 considered the impact of population factors on employment rates in London. Chapter 4 looked at the impact of labour market factors on the same issue. The findings from this initial analysis, summarised above, show that both factors have explanatory power, and should shape future policy. The question is how? While it is difficult to make definitive judgements about the right direction for policy at this stage, it may still be valuable to outline the potential approaches that might shape decisions in the future.

6.9 Table 6.1 below summarises the likely implications for policy in four stylised examples of combinations of population and labour market findings that could exist in a city like London:

- in the London of Scenario 1, analysis of the population shows that the likelihood of being in work is the same in London compared to elsewhere, once differences in characteristics have been taken into account. In this example, there is no evidence of an excess supply of low skilled labour from indicators such as the gain to work or the competition for low skilled jobs. As a result, any difference in employment rates between London and the rest of the country could be explained by compositional factors;

- in Scenario 2, the likelihood of employment in London is similar, but there is also evidence that labour market factors are having an impact on employment opportunities. These labour market factors are not affecting the employment rate, but instead are being revealed through adjustments in wages;
- in Scenario 3, the likelihood of employment is lower in London once characteristics have been taken into account, but there is no evidence that this is being caused by labour market factors. There could be a couple of explanations for this. First, it could be that policy is less effective in London at helping people to overcome barriers to work, and this is reducing the likelihood of being in work. Second, it could be due to limitations in the way the likelihood of employment is determined. For example, there may be unobservable differences between people living in London and those living elsewhere that affect the likelihood of an individual working, but which cannot be controlled for, or differences that result from concentrations of disadvantage that are difficult to measure.
- In Scenario 4, both population and labour market factors appear to be reducing employment rates.

From the findings in Chapters 3 and 4, the real London appears closest to Scenario 4, although the Greater London Authority's findings suggests London may be closer to Scenario 2.

Table 6.1: Employment scenarios and possible policy implications

Scenario	Explanation for lower employment rate	Possible focus of policy solutions	Other issues
<p>1. Population:</p> <ul style="list-style-type: none"> Likelihood of work similar to elsewhere <p>Labour market:</p> <ul style="list-style-type: none"> No evidence of excess low skilled labour 	<ul style="list-style-type: none"> 'Pure' composition effect, no 'London effect' 	<ul style="list-style-type: none"> Labour market programmes and other policies to reduce barriers to work 	<ul style="list-style-type: none"> Raises distributional questions about resource allocation given likelihood of work similar to elsewhere Expansion of labour supply may reduce gains to work
<p>2. Population:</p> <ul style="list-style-type: none"> Likelihood of work similar to elsewhere <p>Labour market:</p> <ul style="list-style-type: none"> Evidence of excess low skilled labour 	<ul style="list-style-type: none"> No 'London effect' Labour market clearing, but at a lower wage Policy effective at reducing barriers to work 	<ul style="list-style-type: none"> Labour market programmes and other policies to reduce barriers to work Improve gains to work for limited groups <p>In addition, policies to:</p> <ul style="list-style-type: none"> Improve mobility and skills 	<ul style="list-style-type: none"> Raises distributional questions about resource allocation given likelihood of work similar to elsewhere Expansion of labour supply may reduce gains to work to critical levels if not combined with mobility and skills policies
<p>3. Population:</p> <ul style="list-style-type: none"> Likelihood of work lower than elsewhere <p>Labour market:</p> <ul style="list-style-type: none"> No evidence of excess low skilled labour 	<p>'London effect' explained by one or more of:</p> <ul style="list-style-type: none"> Policy less effective at reducing barriers to work Unobserved differences between those workless in London and elsewhere Evidence of compounding effects of disadvantage 	<p>Depends on the cause, but probably:</p> <ul style="list-style-type: none"> Labour market programmes and other policies to reduce barriers to work 	<ul style="list-style-type: none"> Expansion of labour supply may reduce gains to work
<p>4. Population:</p> <ul style="list-style-type: none"> Likelihood of work lower than elsewhere <p>Labour market:</p> <ul style="list-style-type: none"> Evidence of excess low skilled labour 	<p>'London effect' explained by labour market factors, and possibly one or more of:</p> <ul style="list-style-type: none"> Policy less effective at reducing barriers to work Unobserved differences between those workless in London and elsewhere Evidence of compounding effects of disadvantage 	<p>Policies to:</p> <ul style="list-style-type: none"> Improve mobility and skills <p>And probably:</p> <ul style="list-style-type: none"> Labour market programmes and other policies to reduce barriers to work Improve gains to work for limited groups 	<ul style="list-style-type: none"> Expansion of labour supply may reduce gains to work to critical levels

6.10 Table 6.1 shows that there are potential tensions to reconcile in designing appropriate policy responses:

- policy tensions between the solutions implied by the findings from the compositional analysis, and those implied by the labour market findings; and
- distributional tensions between Londoners and those living in the rest of the country.

6.11 Understanding these tensions and tradeoffs will be a key task for further work going forward. Further analysis is required to understand fully the linkages between policies designed to support more Londoners into work and policies designed to address labour market issues such as the poor gains to work currently experienced by some in the capital. There is also important read-across to skills and other policies that might improve occupational or geographic mobility.

6.12 The Strategy Unit findings and Treasury analysis suggest that there is a way to go before the likelihood of employment is equalised in London, although Meadows' findings for the Greater London Authority suggest that this has already been achieved. However, even if employment likelihoods were the same in London as elsewhere, compositional differences mean that London's employment rates would still be lower. There might be reasons for going beyond equalising employment chances in London compared to elsewhere, such as concern about the concentration of worklessness in London, scarring effects of labour market exclusion, or poverty risks given the distribution of work at the household level.

KEY QUESTIONS FOR THE FUTURE

6.13 This chapter has summarised the findings from the rest of the document, identified areas where further analysis is needed, and considered tensions likely to face policy makers in the future. It has also implied a number of questions, the answers to which might be key to determining future policy. These include:

- **what is the policy priority?** Should it be to equalise headline employment rates across regions? Should it be to equalise the likelihood of employment, given characteristics, across regions even if this left differences between headline rates? Should it be to improve the likelihood of employment for those with characteristics that currently put them at greatest risk of labour market exclusion? Or should it be to achieve another policy objective, such as to reduce child poverty rates, or to break up concentrations of worklessness?
- **how could work incentives be further improved without creating new distortions?**
- **given the population and labour market characteristics, what is a realistic expectation for labour market programmes within London?**
- **does the current incentive structure encourage the right resource allocation across regions to meet policy objectives?**
- **does London pose specific challenges to the effective delivery of active labour market policies, which might require different methods of delivering employment advice, training and support?**
- **what changes to other areas of policy might be necessary to raise the effectiveness of labour market programmes?**

6.14 The Government will consider these issues further to inform future policy.

MAP OF LONDON

Chart A.I: The London Boroughs



