

# It's not that London is too big, but that other large UK cities are too small

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The elections are barely behind us now, and we should keep asking the question, ‘What are the economic forces polarising the UK?’ A big part of the story concerns the geographical concentration of economic activity in London (and the South East). Is this concentration good for those who live or work in London but bad for those who don’t? Is the attraction of London creating an economy that is distinct from the rest of the UK? And what are the implications?

Neither finance nor the globally oriented part of the London economy is as important as suggested by popular discussion. Financial services are clearly important, but most of London’s long-term job growth has come outside finance or those sectors closely linked to it.

What is most distinctive about London’s economy is its competitive strength and skill levels across a wide range of services. A large part of the superior economic performance of London (and the broader South East) comes from the concentration of skilled workers who would be paid relatively well wherever they lived. In turn, that concentration is partly because London provides greater opportunities for such individuals to use and develop their talents.

All of this means that London has higher wages, more expensive housing and a greater general cost of living, with the gap in all of these rising, as wage inequality has grown since the late 1970s. But at least for those who are young, able and willing to economise on housing costs, London offers opportunities that are simply not available elsewhere. And since many London residents later move on to other areas of the country, the city also acts as a source of highly skilled workers for local economies throughout the UK.

Whether this seems good or bad partly depends on how we tell the story about what is going on. If, as is popular, we talk about London sucking the talent from the rest of the country, then this sounds like a pretty bad thing. But if we think of London’s performance as the result of a large number of people responding to the opportunities that the city offers, then this changes the debate:

First, it becomes clear that we need to think about individual winners and losers. (See the [paper's Annex](#).)

Second, it helps to focus attention on why London offers those opportunities and whether they could be created elsewhere. A large body of evidence suggests that both size and the concentration of skilled workers is key to generating these opportunities, which makes it harder to generate similar opportunities elsewhere.

On the implications for overall economic growth, the debate is polarised. For some, it is obvious that spreading growth across the UK would make use of underused resources. For others, London and the South East are key, and we should focus on making sure they continue to perform. Since there is already a lot of redistribution away from London, the questions are first, whether there should be a lot more spatial redistribution than now, and second, whether we should put a high value on policies restraining London's growth (for example, tougher green belt policies; even lower allowances for public sector workers, etc.).

There is no evidence pointing to large benefits from spatial redistribution and much evidence that very restrictive planning in London and the South East has been harmful (see Hilber, 2015). Hence, artificially restraining the city's growth does not seem like a desirable policy.

### **Policy responses: who and where?**

Rather than focus on London's dominance, we should ask why other large UK cities do not offer similar economic opportunities and what can be done about it. Looked at this way, the evidence suggests that what we need is, paradoxically, the growth of one or two other large cities so that they provide similar opportunities. This is because overall population size helps generate more opportunities (as a result of what economists call 'agglomeration economies'). So too does the concentration of skilled workers and of certain types of knowledge-intensive industries (which employ those high-skilled workers).

*City size:* If size matters, perhaps the issue is not that London is too big, but that some of our second cities are too small. Applying Zipf's Law (which suggests that the second largest city tends to be half the size of the largest, the third city a third the size of the largest, and so on), the UK's larger cities after London all look too small. Population is quite spread out across a number of cities. Concentrating it in a smaller number of larger cities would bring us more in line with other countries. A powerful body of research points to the importance of agglomeration economies and the barriers to realising their benefits (in particular the UK planning system).

*Local growth policies:* The most appropriate scale for strategic decision-making on economic development policies is somewhere above local authorities (which are usually too small) but beneath regions (which are too big). The [deal-making approach](#) – through city deals, local growth deals and now devolution deals – also allows for greater policy variation. In practice, however, central government still ultimately makes decisions on deals and centralises the dispersion of funds.

*Policy variation across areas:* While in principle recent reforms allow for greater policy variation across areas, the extent to which politicians in central government can live with the consequences – in terms of variations in economic performance – remains to be seen. The 'Northern powerhouse' agenda – which aims to create a counterbalance to London by better integrating and empowering the collection of Northern cities – highlights these tensions. The evidence suggests that agglomeration economies work at smaller scales than the entire Northern economy, so more uneven development across Northern cities may be necessary if we want one of these cities to provide the kind of opportunities available in London.

### **Policy responses: what?**

Discussion around the systems through which urban and regional economic policy is delivered often distracts attention from more fundamental questions about the effectiveness of particular policy interventions. The government began to tackle this challenge through support for the What Works Centre for Local Economic Growth (and the wider What Works Network, in which I am involved).

*Transport infrastructure:* London's success depends on transport investment, but it is not driven by transport investment. Public sector transport investments are already quite evenly distributed, and evening out transport investment further [will not be particularly effective](#) in generating opportunities elsewhere. It is also highly debatable whether HS2 will narrow disparities with the government's own analysis pointing to disproportionate benefits for cities on the line (including London).

*Housing:* Supply restrictions mean that house prices rise very fast in response to local demand growth. Relaxing planning restrictions and building on the green belt would help (see Hilber, [2015](#)).

*Area-based initiatives:* Policies that offer support for particular areas of cities or regions (such as enterprise zones) are unlikely to be effective in addressing broad differences in performance. The evidence mostly suggests that these lead to displacement from other nearby areas rather than creating a large amount of new job growth. Similar problems limit the economic impact of other regeneration policies.

*Business support:* There is a depressing paucity of high quality studies evaluating business support policies. Overall, the current evidence on business support policies (such as improving access to finance, or offering advice and expertise) suggests that these types of policies are not very effective at generating employment growth. For more discussion, see Roland and Valero ([2015](#)) and the What Works ([2014](#)) access to finance and business support evidence reviews. But there is some evidence that specific policies can improve job growth. For example, Criscuolo et al ([2012](#)) find job increases from European regional aid but only for small and medium-sized enterprises and there does not seem to be a sustainable increase in *productivity*. We need to understand better what separates successful from unsuccessful interventions.

*Skills:* Local differences in the skill levels of workers play a large role in explaining disparities across cities. Education and training may have an important role to play in helping address these disparities. As with business support, policy needs to address similar concerns about cost-effectiveness although there does appear to be growing support for experimentation and evaluation aimed at improving the cost-effectiveness of policies. (For more discussion, see McNally, [2015](#).)

## Conclusion

There are large variations in economic performance across the cities and regions of the UK and on some measures, they have widened since the global financial crisis. The traditional policy mix – central government investments in local growth projects, transport and other infrastructure, funding for business support and access to finance, and a host of other interventions – has not been effective. There is a growing recognition that greater local control may be needed to improve policy effectiveness, although there is disagreement about the form this devolution should take. Whatever happens, it is important that policies that have wide scale impacts (such as transport and housing) are coordinated across local areas.

London's strong economic performance plays a large part in explaining widening disparities. Providing an effective counter-balance to London may require policy aimed at 'rebalancing' to be more spatially focused – for example, on Manchester. Concentrating resources in this way is controversial and difficult for constituency- based politicians (in both central and local government).

It is helpful to remember that we ultimately care about the effect of policies on people more than on places. Efforts to rebalance the economy should be judged on the extent to which they improve opportunities for all, rather than whether they narrow the gap between particular places.



Notes:

- This blog post is based on the author's paper [The UK's Regional Divide: Can Policy Make a Difference?](#), part

of the election analysis series of LSE's Centre for Economic Performance ([CEP](#)).

- The post gives the views of its author, not the position of LSE Business Review or the London School of Economics.
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