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# **1. Financial Services Clustering and its Significance for London: Key Points**

## **Dynamics**

- London's labour market is one of its greatest assets. The supply of skilled labour, from both domestic and international pools, is a major factor sustaining growth.
- Personal relationships supported by close geographical proximity and on-going face-to-face contact are vital processes that sustain the London financial cluster.
- The localised nature of relationships between skilled labour, customers and suppliers is a critical factor which helps firms achieve innovative solutions, develop new markets and attain more efficient ways to deliver services and products to clients.

## **Advantages**

- The importance of London as a credible address is a major locational advantage for firms. The address becomes an invaluable brand in both a national and international context.
- Proximity to customers, skilled labour and professional bodies figures highly among the benefits of a London location, while knowledge is gained from being located close to competitors and support services.
- The wider attractions of London as a major world city offering cultural diversity, cosmopolitanism and vibrancy make it a place that people want to live and work in. This is a significant business asset.

## **Threats**

- The high cost of premises is a key reason for firms to consider relocating business activities out of the London financial cluster. However, firms are reluctant to do so because of the fear of losing skilled staff and the advantages of being located in an established financial cluster.
- The poor quality and reliability of transport, particularly the state of the London Underground and links to airports, is undermining the attractiveness of the central cluster.
- Government complacency, a lack of policy co-ordination and increasing levels of regulation are leading to a gradual erosion of London's business-friendly environment.

## **Conclusions**

- The intense concentration and clustering in the City of London and Canary Wharf should continue disproportionately in relation to other areas in central London because of the sheer advantages of being located in the premier European financial district and, alongside New York and Tokyo, one of the three global international financial centres.
- De-clustering of core functions is not occurring from the City/Canary Wharf. The locational advantages of remaining in the cluster will ensure that it has a sustainable future so long as policy is focused on ameliorating the threats of poor transport infrastructure, the high cost of premises and increasing levels of regulation.



## 2. Executive Summary

- (i) The intensity of concentration and clustering in the City of London and Canary Wharf will continue disproportionately in relation to other areas in central London because of the sheer advantages of being located in the premier European financial district and, alongside New York and Tokyo, one of the three global international financial centres.
- (ii) De-clustering of core functions is not occurring from the City/Canary Wharf. The locational advantages of remaining in the cluster (credible address, proximity to labour supply, innovation etc.) will, all things being equal, ensure that the cluster has a sustainable future irrespective of the poor transport infrastructure and the high costs of business premises.
- (iii) There is also a clear message for policy-makers that they must not be complacent. Focused governance is needed to ensure that the strength of the cluster is not eroded. This suggests the following key policy priorities:
  - International – EU Cross-border co-operation to promote the Single Market, European transport networks and non-competitive relations between London and other key European financial and business services centres.
  - National – UK Policy integration across institutional and administrative boundaries on regulation, taxation and employment policy, and increased involvement in EU policy. Strong support for, and investment in, London’s transport infrastructure.
  - Regional – South East Cross-Greater London Authority (GLA) boundary policy co-ordination on housing, transport, skills development and employment to reflect the region-wide functional relations of the London cluster.
  - London - GLA Focus on office development in close proximity to the established cluster, in particular the City hub, and promotion of co-ordinated policy for the cluster as a whole. Urgent implementation of improvements to Underground infrastructure/reliability and central London taxi movement.
  - The City – Corporation of London Focus on high-density development in areas close to existing office concentration and transport nodes with particular attention to the needs of banks and other activities on which the cluster depends.

## Basic Geography

The analysis of the location of London financial service firms shows a distinctive East-West concentration, with four separate clusters identified:

- (i) A very cohesive City of London cluster (east of St. Paul's) featuring banks, insurance, auxiliary finance, law and recruitment firms;
- (ii) A less cohesive West End cluster, with distinctive cluster zones (e.g. banks near Mayfair, advertising in Soho);
- (iii) An incipient general cluster north of the City of London featuring such services as architecture, business support;
- (iv) The law cluster that straddles the City of London and West End.

## Cluster Theory

Defining a cluster is difficult. No one definition is universal because clusters have different characteristics, functions, geographical scales and life spans (sustainability). Michael Porter (1998, pp.197-8) emphasises that clusters “are geographical concentrations of interconnected companies, specialist suppliers, service providers, firms in related industries and associated institutions.” It is widely accepted that clusters grow and become sustainable because of their proximity to customers, local linkages (externalities) with both customers and clients (demand factors), and their ability to transfer specialist knowledge at lower costs over very concentrated geographical scales (supply factors) (Swann et al., 1998; Porter, 1998). Clusters provide knowledge-rich environments which are associated with innovation and, importantly, the building of relationships, trust and reciprocity.

In the sphere of financial services, the research informs us that large, medium and small-sized financial service firms have a tendency to cluster in metropolitan areas because of the need to: access large pools of specialist labour and support services (e.g. accounting, actuarial, legal etc.); be in close proximity to the markets; benefit from agglomeration economies, which reduce transactions costs; develop and innovate intrinsic skills through the sharing of knowledge and practice (Davies, 1990; Roberts et al., 2000). Financial service firms that locate in strong clusters grow faster than average and strong financial clusters attract a disproportionate volume of new firm entry (Pandit et. al., 2001).

## Benefits of a London Location

The research identified numerous benefits for financial service firms to be located in central London. Four critical benefits were identified:

- (i) The importance of London as a credible address is one of the major locational advantages for firms. A credible address in the City of London is paramount for banks, legal firms and management consulting in particular, as the address becomes an invaluable brand in both a national and international context. For example, a City of London location turns a law firm into a *City law firm*, which provides classic ‘credence services’ to gain market share and cultivate relationships with clients through projected image, trust and reputation. Equally, if an investment bank wants to be credible as a global investment bank, it has to be in London.
- (ii) Proximity to customers, skilled labour and professional bodies figures highly among the benefits of a London location. Being close to customers is important for law firms. Insurance companies and real estate place greater significance on being near to market leading customers and, in the case of insurance, the physical exchange. All sectors note the importance of being able to recruit skilled individuals from the local labour pool, but this is particularly important for banking. A factor that is unusual is the importance of proximity to professional and regulatory bodies (Bank of England, Law Society, FSA).
- (iii) Access to knowledge is gained from being located close to competitors and support services. Banks place significantly higher importance on knowledge transfer and the ‘financial atmosphere’ in their locational preferences, whether located in the West End or City of London clusters. Of significance are the locational advantages of being able to gather knowledge from the inter-dependencies with other financial and support services. For banks, a tightly-bound geographical location is essential to sustain localised formal and informal networks, and social interaction, which still remains an important vector for knowledge accumulation and transfer in the West End and City of London clusters.



- (iv) The importance of the wider attractions of London as a major world city is particularly significant, especially its regulatory openness, cultural diversity, cosmopolitanism, lifestyle fashion, arts, restaurants, and the general vibrancy of a place in which people wanted to live and work.

Policy implications are found at two levels. First, banks and related financial services are the hub of the City cluster and therefore maintaining London's attractiveness for these activities must be a key policy priority. Second, the attraction of London as a major metropolis and cultural centre underwrites its economic attractiveness and there is therefore a premium on maintaining its cultural reputation.

### **London's Clustering Dynamics**

The research found that four major clustering engines ensure the continual growth and sustainability of the financial cluster in London: labour supply; personal relationships through face-to-face contact; innovation; and processes of co-location and competition.

- (i) London's labour market is one of its greatest assets. The supply of skilled labour, from both domestic and international pools, is a major factor that sustains the growth of the financial cluster, especially in the City of London and Canary Wharf. The questionnaire highlighted the strength of the flexibility of the London labour market compared to Europe as an important engine of financial cluster dynamism, and this was corroborated by the interview results which flagged the immeasurable value of the quality and quantity of international labour attracted to London from Europe, North America and the Far East. Several respondents noted the sheer intellectual infrastructure available in the financial cluster. Two important advantages arise from this: (a) labour is always attracted into the cluster because of the prestige of developing a career path in London, and the City in particular; and (b) the size of the labour market encourages mobility between firms and sectors.
- (ii) Personal relationships between firms, clients, suppliers, professional bodies, the state and financial regulators are still vital processes that sustain the London financial cluster. The research showed the importance of close geographic proximity in cluster dynamism because it sustains the process of face-to-face contact in daily working

environments through combinations of formal and informal business, social interaction and networks. Face-to-face contact is not only viewed as a production process in its own right, maintaining the well-being of the cluster, but is also a fundamental requirement for the establishment of trust, production of knowledge and the completion of complex transactions which require the input of a multitude of suppliers. Proximity is an advantage in terms of the ability to have face-to-face meetings. It allows meetings to be called at short notice and takes advantage of clients, suppliers, customers and others being able to walk to the meeting place. The compactness of the City of London is an advantage because it allows a greater density of interaction and produces spill-over effects into the social and cultural milieu of the cluster. Meeting socially in the cluster is of significant importance and the research reaffirmed the co-existence of both 'Old' clubby practices and 'New' circuits of networks focused around sports clubs, fitness centres and 'work-balanced' lifestyles.

- (iii) The localised nature of relationships between skilled labour, customers and suppliers is a critical factor which helps firms achieve innovative solutions to business transactions and produce design within the cluster. The research findings indicate that innovation sustains the financial cluster. Legal firms especially rate the importance of customers as potential innovators who demand increasingly sophisticated services. In contrast, banks, fund managers and insurance firms suggest that complementary suppliers (i.e. other banks and insurance companies) are very important in helping firms innovate through competition. Research findings also indicate that the larger the firm, the more it rates competition as a primary factor which encourages innovation with the cluster as firms diversify activities to compete for market share.
  
- (iv) Linked to innovation, co-location and competition within the cluster are important for helping firms develop new markets and more efficient ways to deliver services and products to clients. For banks especially, location in either the City of London or Canary Wharf is rated as being a vital contributor to their ability to compete through product innovation. Moreover, the research shows that banks, and in particular investment banks, are at the hub of the cluster, and their inter-relationships with other investment banks provide the impetus for innovation and product differentiation as they search for new market share.

Research findings from the interview survey shed new light on the relationship between the City of London and Canary Wharf. The interviews confirm that being close to customers and suppliers is of paramount importance. The cluster is sustained by having all the major actors in the network and a general view is that Canary Wharf is ‘close enough’ geographically to the City to benefit from the latter’s agglomeration economies. In short, Canary Wharf is viewed as an adjunct of the City and not a separate rival cluster.

Policy implications deriving from these dynamics all relate to the compactness of the City cluster. The key spatial policy should be to keep the cluster as compact as possible: this has implications for local transport policy especially in relation to Canary Wharf connections. Ease of movement within and around the cluster is critical to sustaining the dynamics of the cluster and therefore a polycentric development policy for dispersing critical services would seriously weaken the cluster.

### **Disadvantages of a London Location**

There is a down-side to geographical concentration in central London and three issues dominated the research findings.

- (i) The cost of premises is the most highly ranked disadvantage of a London location.
- (ii) The quality and reliability of transport. The state of the London Underground system is also a major problem, with transport deemed a “massive all-encompassing problem”, to quote one respondent. It affects commuting, business travel across central London and links to international airports, especially from the City/Canary Wharf to Heathrow.
- (iii) Government complacency/lack of policy co-ordination leading to a gradual erosion of London’s business-friendly environment. Interviewees flagged increasing regulation, direct and indirect taxation, employment policy and under-involvement in European policy-making as the most fundamental threats to the cluster.

The policy implications are quite specific in these areas. Transport should be a high priority while an overview of government policy having direct and indirect effects on London’s attractiveness as an international financial centre is needed.

## **De-clustering**

In addition to exploring the advantages to firms of clustering, the research investigated the factors that would encourage firms to relocate away from the financial clusters. Four major research findings can be reported.

- (i) The high cost of premises is the key reason for firms to consider relocating business activities out of the London financial cluster. For firms in the City of London, Canary Wharf has become an attractive location, particularly for banks, because of the relatively lower costs of premises and the availability of high specification premises.
- (ii) Firms, however, are reluctant to relocate to a non-central location because of the fear of losing skilled support staff due to the inadequacy of transport links across London, especially in relation to Canary Wharf. London Bridge is perceived as an attractive alternative to the City of London because it has good transport links and is within walking distance of the City.
- (iii) Firms would always want an operation in one or both locations (the City and/or Canary Wharf). Firms would not relocate to potential new business clusters in London or the South-East of England because they would lose the advantages of being located in an established financial cluster.
- (iv) Relocating outside of established London clusters or London itself is perceived as a viable option for back-office, routine administrative procedures, and such labour processes could lend themselves to de-clustering. Many firms suggested that in order to make a substantial benefit in terms of lower buildings and labour costs, they would need to move some distance from London, perhaps outside the South East/UK altogether.

Policy implications are not critical in this area; there are sound reasons for firms to de-cluster some of their activities just as there are sound reasons to keep high order office functions within the cluster. The development of Canary Wharf is not interpreted as de-clustering. It is essentially part of the City.

### 3. Basic Geography of Financial Services Clustering in London

#### Scope and Methods

This report is the culmination of a one-year research study which investigated the existence and significance of business clusters in the City of London and its surrounding areas, and the importance of such clusters on the dynamics of the London economy as a whole, in terms of its competitiveness and innovation. The study involved a combination of:

- (i) Desk-based archival research, particularly on cluster theory and the City of London;
- (ii) Cluster mapping of approximately 23,000 financial business services in London (using Geographical Information Systems) spanning twelve sectors: banks, insurance, auxiliary financial services, real estate, law, management consultancy, accountancy, advertising, recruitment, business support, architecture/engineering and IT;
- (iii) A questionnaire survey of 1,500 financial business services in London (particularly the City and City Fringe), with a stratified sample drawn from eighteen sub-sectors (as above, but also including: fund/asset management; publishing; market research; property management; printing; investment banking);
- (iv) Thirty nine on-site face-to-face interviews with firms, professional institutions, government bodies and other related agencies in the City of London and City Fringe. The interviews were undertaken with individuals who crossed seven business sectors (banking, auxiliary financial services, insurance, legal, accounting, consulting and property services), with the highest number executed with banks (14 in all) to reflect the sector's importance in London's financial community;
- (v) A continuous dialogue with a wide range of representatives from London's business service community (drawn from the private sector, Central and Local Government, professional bodies and academics) in the form of two Focus Groups.
- (vi) A comparative analysis of the geographies of business clusters in Frankfurt and the Randstad, Netherlands.
- (vii) A review of spatial policy documents at different levels (local, national, international) that provide the public policy framework for the London financial cluster.

The initial task of the study was to provide a very basic geography of financial and business services in London. The locations of firms in twelve service sectors have been investigated:

banks, insurance, auxiliary financial services, real estate, law, management consultancy, accountancy, advertising, recruitment, business support, architecture/engineering, and IT. Details of the analyses can be found the Appendix. In essence, for each sector there are three levels of abstraction in the construction of the geography of clustering.

- The level of individual firms – maps were constructed of the distribution of all firms in each sector to provide a preliminary geography of clustering and dispersion (see Appendix).
- The level of ‘cluster firm’ defined as a firm with 10 other firms in its sector located within 100m. of its office - maps of these firms for all twelve sectors are shown in the Appendix.
- The level of general service cluster zones defined by combining the cluster firm maps across sectors - see Figure 1 which describes the basic geography of clustering among financial and business services in London.

These maps are derived from combining Market Locations and Ordnance Survey data to find OS National Grid locations of some 23,000 firms in financial services sectors.

The degree of clustering of firms in a sector obviously depends to some degree on the number of firms in the sector (the more firms, the more likely they are to be located near one another). The sectors can be ordered as follows in terms of their proportion of firms that are defined as cluster firms: insurance, recruitment, banks, business services, law, real estate, advertising, management consultancy, architecture/engineering, auxiliary finance, accountancy, IT (see Table A1 in the Appendix). But such a statistical ordering only tells part of the story: to fully understand the nature of clustering of London’s financial and business services requires an investigation of their specific different geographies illustrated in the Appendix.

The overall map of clusters (Figure 1) has been produced in order to appreciate the general pattern of clusters in a situation where there is much geographical overlap between the various services. Specific spatial relations between services can be seen by inspection of the maps in the Appendix; here we focus upon the aggregate pattern. This geography consists of four distinct cluster zones of varying importance. The two main zones are:

- City of London (east of St Paul's) featuring cluster firms in banking, insurance, auxiliary finance, law and recruitment. This is a cohesive cluster zone of financial and related services, compact but with some separation (e.g. insurance clustered to the east of the main banking cluster)
- West End featuring cluster firms in banking, real estate, law, management consultancy, architecture/engineering, accountancy, advertising, recruitment, and business support. This is a larger but less cohesive cluster zone including all but three services. Within this zone there are distinct separations of services (e.g. banks near Mayfair, advertising near Soho and real estate west towards Hyde Park).

These cluster zones are so strong that we may think of London as a 'two city' global service centre. In addition, there are two less important zones that are nonetheless interesting:

- Northern frame (of the City of London) featuring cluster firms of architecture/engineering and business support. There are other services that feature in this zone at lower levels of abstraction and therefore this area might be interpreted as an incipient general cluster zone developing adjacent to the City.
- The law zone that forms a unique service cluster which straddles the space between the City and West End servicing the two main zones.

The 'two city' structure of financial and business service cluster firms is reflected in six of the twelve service sectors having developed in two clusters. However only three services have their cluster firms appreciably represented in the two main general zones: banks, law and recruitment firms. In addition, architecture/engineering and business support firms are clustered in the West End and the City's northern frame.

There are six service sectors that have largely developed their clusters in just one general zone: insurance and auxiliary finance firms in the City; and advertising, accountancy, management consultancy and real estate firms in the West End. The few IT cluster firms are to be found in the City's northern frame thus providing some credence to the idea of this zone as a future third general cluster zone in London.

**Figure 1: Major Cluster Areas**





## 4. Key Findings

### 4.1 Literature Review

#### Cluster Definition

The literature provides many definitions of what a cluster is. No one definition is entirely satisfactory simply because there are a number of cluster types, each type with different characteristics and sustainability potential (Markusen, 1996). However, a general definition that would be largely acceptable to most is the one used by Porter (1998, pp. 197-98):

Clusters are geographic concentrations of interconnected companies, specialised suppliers, service providers, firms in related industries, and associated institutions (for example, universities, standards agencies, and trade associations) in particular fields that compete but also cooperate.

What are the strengths of this definition? Firstly, it does not relate to a single industry; rather it merely requires that companies in a cluster are *interdependent* in some way. This makes sense. For example, we know from Saxenian's (1994) work that the Silicon Valley cluster includes not only microelectronics firms but also venture capitalists. Secondly, a cluster is defined not just in terms of companies but also supporting institutions. We know that these are important in strong clusters. Thirdly, non-market linkages are emphasised. These, borne out of a common culture and trust, are thought to be important particularly with respect to innovation. Finally, the definition encourages us to think of clusters as complex systems of industrial organisation.

The literature points out many times that clusters are systems that have evolved because they are well suited to deal with the characteristics of the modern business environment. This is not to say that clusters are new. There are examples of industrial clustering that go back at least to the industrial revolution and academic work on clustering goes back at least to Alfred Marshall (1919). Rather, it is to say that clusters have been rediscovered to represent the best adaptive industrial response to certain contexts, particularly those in which productivity improvements, knowledge intensity and the ability to change are central. The cluster is seen as an efficient organisational form that reaps the advantages of scale (e.g., lower cost) but without the disadvantages (e.g., lack of flexibility and entrepreneurialism) and reaps the advantages of being small (e.g., flexible and entrepreneurial) without the disadvantages (e.g., high cost). Additionally, clusters have been shown to tap successfully into available

economies of scope (where joint production is cheaper than the additive costs of separate production) (Scott, 1988). Empirical studies reflect these advantages and show that firms in strong clusters grow faster than average; clusters attract a disproportionate amount of new entry; productivity is higher within strong clusters; and firms in clusters are more innovative than average.

Furthermore, because clusters are complex systems that evolve naturally, they are difficult to imitate and therefore confer sustainable economic advantage to the locations in which they arise. Specifically, Maskell and Malmberg (1999) identify three main reasons why the success factors of one region will be hard to copy by another. The first is that regions benefit from accumulated stocks of R&D, specialised labour and infrastructure which make it easier for them to pursue further innovation. Secondly, it is difficult for other regions to recreate this expertise quickly. Thirdly, it is difficult for other regions to recreate the complex webs of relationships which connect firms and institutions within a regional system.

All of this points to a paradox. Increasing globalisation and reducing transport and communication costs mean that location has become more not less important. When firms can source inputs easily from anywhere in the world and locate where it is most cost efficient, the value of characteristics and processes that do not travel easily and/or cheaply over distance increases, making production in clusters more valuable and more sustainable.

Given these broad advantages over alternative systems of industrial organisation, it is not surprising that clustering is found to be the norm rather than the exception: industrial activity on the whole is geographically concentrated, quite often markedly so. Additionally, clustering is observed across many industry types: manufacturing and services; high and low technology. Equally interesting are the observations that world-class companies and institutions in a particular field tend to be geographically proximate, and that a country's most productive and most important industries tend to be geographically concentrated. A point that follows from these observations, and one that is stressed in the literature, is that the relevant geographical unit from a clustering point of view is not the nation but rather the city/region (Jacobs, 1984). Indeed, there is much support in the literature for the idea that core metropolitan areas in particular are the well-spring of economic dynamism and innovation, and exert a profound influence on the prosperity of the nations in which they are located. Related to this, a recent and growing body of literature demonstrates that

connections and flows between a clustered city-region and other similarly clustered city-regions are more important than connections between a clustered city-region and the nation in which it is situated.

### **Cluster Benefits and Costs**

An obvious reason for maintaining location in a cluster is simple inertia: sunk costs at a location make movement to another location unattractive. A firm may also be attracted to a cluster because of so-called “fixed factors”. These are benefits which exist at a location that are not a function of the co-presence of related firms and institutions, and include climate and cultural capital. Beyond these reasons and from the perspective of the clustered firm, clustering theory maintains that there are benefits and costs which are directly related to the co-presence that exists within a cluster. These can emanate on the demand or supply side. When benefits are greater than costs, the cluster grows (incumbent firms grow and new firms are formed). When costs are greater than benefits a cluster declines. These processes can constitute a ‘natural’ evolution of city-regions with de-clustering of specific sectors as some activities get dispersed when they cannot justify their high cost locations (Hoover 1948; Jacobs 1984). In addition, some of the benefits and costs are dynamic in that they increase as geographical concentration increases. Table 1 provides a summary and draws from the work of Swann *et al.* (1998) and Porter (1998).

**Table 1: Cluster Growth and Decline Factors**

	<b>Demand Side</b>	<b>Supply Side</b>
<b>Growth</b>	Customer proximity	Knowledge spillovers
	Reduced consumer search costs	Specialised inputs
	Informational externalities	Infrastructure benefits
		Better motivation and measurement
		Experimentation at lower cost
<b>Decline</b>	Congestion and competition in output markets (overheating)	Congestion and competition in input markets (overheating)
	Technological discontinuities	Cartels and over consolidation
	Changes in tastes and preferences	Powerful trade unions
		Stagnant local infrastructure

On the demand side, a firm may benefit from customer proximity which can be especially important when customers are sophisticated. Such customers can encourage innovation by being demanding and by alerting suppliers to new trends and innovations. Such knowledge exchange between customers and suppliers can be problematic because the value of knowledge is difficult for users to gauge before they have acquired or absorbed it. Clusters provide a solution to this problem. Roberts *et al.* (2000, p. 17) state:

The risks and uncertainties that arise in the market exchange for knowledge are reduced by the development of networks and a relationship of trust between the parties involved. Reputation and accreditation by relevant professional bodies are important mechanisms for reducing uncertainty.

A clustered firm may also benefit from reduced consumer search costs. The idea here is that the firm is more likely to be found by customers when it is located in a cluster. This is particularly important when consumers have specific requirements (and so explains why antique shops tend to cluster). Information externalities on the demand side may also exist; in other words, a cluster's reputation rubs off on the firm that is located in it. This can be a major benefit when a cluster has a high reputation (e.g., Harley Street and Saville Row for medical and tailoring services respectively).

On the supply side a major benefit is that knowledge spills over in a cluster and this is particularly important when valuable industry knowledge is tacit rather than codified. In a sense, tacit knowledge becomes a public good. When this happens, innovation is more prolific. Mechanisms for knowledge spillovers include labour market churn, social interaction and diffusion via clients and suppliers.

A second supply side benefit is access to specialised inputs. As a result, a firm benefits from lower search costs because it can easily recruit from a pool of specialised labour and can tap into a specialised supplier base. Infrastructure benefits can go beyond access to a good transport network to include institutions that coordinate activities across companies in order to maximise collective productivity, for example, trade associations which set standards and/or conduct marketing for the cluster as a whole. Better motivation and measurement can also exist within a cluster as local rivalry acts as a powerful spur. Also, it can be easier to measure performance against local rivals as they share a similar context leading to lower monitoring costs. Another important supply side benefit is that it can be easier to try out new ideas in a cluster since it is possible to gain instant feedback and all of the inputs (including sympathetic venture capital) required for experimentation are likely to be present in the cluster. Finally, a clustered firm may benefit from informational externalities on the supply side: the firm enjoys lower risk by observing successful production at a location.

With respect to decline factors on the demand side as the number of competitors increases, we would expect prices, and so profits, to fall. Also, a cluster specialised in a particular technology can go into decline if that technology is substituted (Porter (1998) provides the example of New England's loss of market share in golf equipment to California as the industry moved from the traditional materials of steel and wood to advanced materials). Finally, changes in tastes and preferences can lead to cluster decline.

On the supply side, congestion and competition in input markets can lead to higher wages and rents which in turn can lead to movement out of the centre of a cluster. Cartels and over-consolidation, traditional trade unions and stagnant local infrastructure are all potential decline factors as they can restrain competition and innovation, and slow productivity improvements. These potential supply side decline factors provide the main agenda for government industrial policy.

### **Cluster Types**

As indicated above, the extent to which clustering benefits arise varies according to cluster *type*. A number of important ideal types have been identified by Markusen (1996), each of which manifests a certain type of economic logic. Markusen's typology differentiates clusters according to: (1) Firm size, reflecting available economies of scale and scope; (2) The extent to which firms, suppliers and customers are connected within the cluster; (3) The

extent to which the cluster's orientation is internal or external; and (4) The extent to which economies of agglomeration (reductions in cost that arise from the geographic concentration of economic activity) are present. These and three other important features are shown in Table 2.

The classic cluster type is the Marshallian New Industrial District (NID) (Marshall, 1919; 1927). Such districts are populated by small, locally-owned firms. Major external economies exist in the form of access to a pool of suitable labour, specialisation, including specialised supply of inputs, and knowledge spillovers. Information is likely to flow more easily because of the natural tendency of people in the same trade to share ideas and discuss and demonstrate improvements. Building on these ideas other writers have pointed out that experimentation is also easier within a cluster: there is a high quantity and quality of feedback and firms are more likely to be able to find the complementary knowledge, resources and assets they need in order to bring their ideas to fruition. The high quantity of feedback reflects the dense concentrations of customers who can be found in clusters while high quality feedback reflects the tendency of clusters to attract sophisticated customers who can encourage innovation by being demanding and alerting suppliers to new trends.

Distinct but related to the NID are the Italianate or Third Italy (Best, 1990; Piore and Sabel, 1984) and Innovative Milieu (Camagni, 1991; Cappello, 1999) types where there is greater cooperation between incumbents to share risk, ensure stability and promote the region; often embodied in strong trade associations and regional government (high "institutional thickness").

Another very important type is the Hub-and-Spoke cluster where regional structure revolves around one or several major corporations in one or a few industries. The presence of large firms reflects available economies of scale and scope. Connections within the cluster are not evenly dispersed. Rather they tend to flow between hub and fringe firms. The orientation is external especially with respect to customers. High economies of agglomeration are present and particularly important is the pool of specialised labour. Also, knowledge spillovers may occur through labour market churn rather than informal social interaction as in the NID. Loosely related hubs in several industries may co-exist and intra-cluster connectedness (global nodes) may be reflected by labour mobility patterns.

A less important cluster type in terms of performance and sustainability is the Satellite Industrial Platform: a congregation of branch facilities of externally-based multi-plant firms often attracted to the location by government inducements on tax and rents. The presence of a few large firms reflects moderate to high scale economies. High rates of labour mobility in and out of the region at the senior level (within the parent firm) are typical while more junior labour tends to be hired locally. Cluster growth and sustainability are constrained as the main sources of competitive advantage and innovation are external to the region. Weak trade associations are typical but a strong role is often played by local government for the provision of infrastructure, tax-breaks and other generic business inducements (e.g., good schools). The fourth cluster type is the State-Anchored District where a major government tenant (e.g., defence plant, government department, university etc.) anchors the regional economy. The classic example is where state defence establishments lead to clusters of defence-related firms, but a wide range of different types of government establishment may be at the centre. Their on-going operation, once formed, can be similar to the Hub-and-Spoke cluster.

Most real-world clusters are what Markusen calls “sticky mixes” – hybrids of the above - although one type will probably dominate. For example, Silicon Valley has an NID in electronics but also a number of important hub firms, such as Lockheed, Hewlett Packard and Stanford University. It also hosts a number of branch plants, as in the Satellite Platform model, such as IBM, OKI, NTK Ceramics, Hyundai and Samsung, and benefits from proximity to the defence industry as in the State-Anchored District model. Finally, it should be noted that nothing is fixed, and a cluster may mutate from predominantly one type to another over time.

**Table 2: Characteristics of Types of Cluster**

	<b>Marshallian New Industrial District</b>	<b>Hub-and-Spoke</b>	<b>Satellite Platform</b>	<b>State-Anchored</b>
Number and size distribution of firms	Atomistic	Large hub firm(s) and atomistic fringe Micro-clusters may emerge in fringe	Few large firms	Large state organisation(s) with atomistic fringe
Connectivity	Highly intra-connected	Connections from hub to fringe	Low intra-connections Connections between incumbents and distant corporate parent	Connections between state organisation and fringe firms but essentially on a sub-contracting basis
Cluster orientation	Internal	External	External	External
Economies of agglomeration	High: labour market pooling, specialisation including suppliers, knowledge sharing	High: but internalised (except for within micro-clusters)	Low: main benefit of locating in region is to take advantage of factor endowments	Low: not important unless micro-clusters form
Labour mobility	High within district, low outside	Low within hub firms Loyalty to hub firm rather than the district	Low	Typically low within state firms but may have important flows of labour out of universities or research institutes
Importance of new firm formation	Important to the dynamics of specialisation	Low. Presence of hub firm may act as a magnet for new firm entry	Low	Spin-offs from universities or research institutes could be important
Institutional thickness	High: specialised providers of education and training. Strong trade associations	Not important Presence of hub firm(s) and success drives cluster dynamics	State may fund valuable investment in infrastructure and subsidies	Not important



## **Clustering in Financial Services**

What does the literature say on financial services clustering? On the supply side, large and complex financial services firms need access to large pools of specialised labour. Thus we observe that investment banks are almost exclusively based in financial centres such as London, New York and Frankfurt. This point is reinforced firstly by the fact that financial services skills are in large part acquired by shared experience (e.g., knowledge of how to trade Eurobonds is usually gained under the supervision of a senior Eurobond dealer) and secondly by the increased pace of innovation in financial services. This has further raised the importance of tacit knowledge which is more easily exchanged when agents are geographically close. Conversely, smaller scale financial services companies such as building society branches and independent insurers that are less complex and less reliant on tacit knowledge do not rely on large quantities of highly specialised labour and they can afford to be located outside major financial centres.

Another supply-related explanation for clustering arises from the reliance of financial services firms on a vast array of supporting services (e.g., accounting, actuarial, legal, management consulting, computing and software development, advertising and market research, recruitment, education, financial publishing) and again these are most prevalent in major financial centres. Related to this, the co-location of associated markets (banking, insurance, securities dealing, fund management, derivatives, maritime services, foreign exchange, bullion markets, and support services already mentioned) leads to economies of agglomeration resulting in improved flows of information, greater efficiency and higher liquidity. The importance of economies of scale has also increased in recent years, driven by the increased use of information technology. This new technology has enabled rapid innovation following a pattern that conforms to Barras' (1986; 1990) view that financial services innovation occurs in a "reverse product cycle" manner (that is, the process of innovation is *preceded* by the adoption of new technologies developed in other sectors).

Three distinct characteristics of services in general - that they are consumed simultaneously with their production, cannot be stored and are intangible (Roberts *et al.*, 2000) - imply an extensive producer-consumer relationship and underlie many of the demand-side benefits of financial services clustering. For example, because financial services are intangible, quality is often not associated with a physical product (as in the case of many manufactured goods) and is instead associated with the reputation of the firm's location. Thus we observe new

entrants preferring to locate in recognised financial districts. Also, the bespoke nature of some financial services (e.g., primary issues) requires a close supplier/customer relationships built on the trust that can only be generated through frequent face-to-face contact (Davis, 1990). The producer-consumer relationship can also be a major source of innovation. Finally, positive reinforcement can be observed. Liquidity attracts further liquidity building the cluster's reputation as it grows. Similarly, one firm's movement out of the cluster or out of the centre of a cluster can lead to the same move by others as if following a herd instinct.

What are the empirical findings on financial services clustering? Recent statistical research has yielded results which indicate that the benefits of clustering in service industries can be very similar to those found in high technology manufacturing industries. A series of statistical studies by Swann and Prevezer (1996), Beaudry *et al.* (1998), Cook *et al.* (2001) and Pandit *et al.* (2001) have investigated the dynamics of industrial clustering in three high technology manufacturing industries - computing, biotechnology and aerospace - and two service industries - broadcasting and financial services. These studies have used a common methodology which allows comparisons to be made.

The financial services study finds that such firms located in strong clusters grow faster than average and that strong financial services clusters attract a disproportionate amount of new firm entry. Furthermore, a comparison of this study with the others reveals that these positive clustering effects are of a similar magnitude to those found in high technology manufacturing.

### **Financial Services Cluster Types**

There is very little existing literature on cluster types within financial services. One study (Pandit and Cook, 2003) compares the UK financial services industry at three locations: London, the South West (mainly in and around Bristol) and Southern Scotland (mainly in and around Edinburgh). It finds that the South West resembles a Satellite Industrial Platform type of cluster. Insignificant economies of agglomeration are detected and the industry's history at this location is short, dating back only to the early 1970s. It was at that time that London companies moved the less knowledge intensive aspects of their business out of London to save costs. Incumbents are not well connected and are externally oriented towards their parents. Senior employees do not tend to move between cluster incumbents, rather they move within their geographically dispersed parent company. In contrast, South Scotland is found to resemble a Hub-and-Spoke type cluster, dominated by large banks and insurance companies. There is mobility of senior employees between cluster incumbents.

A larger contrast still is observed in London which is also found to resemble a Hub-and-Spoke type of cluster. Important hub firms are the major clearing banks and the large investment banks. Significant economies of agglomeration are detected in London and unlike the South Scotland cluster, these occur across the full-range of industry sub-sectors. Firm size is important especially for the larger banks as it permits economies of scale, greater liquidity and more organised markets, and helps support services. A major benefit is access to a pool of specialised labour, and the frequent churn of this pool is a major mechanism by which knowledge diffuses. An important feature of the London cluster is that labour mobility is also high between the four major international financial centres (London, New York, Frankfurt and Tokyo). Supporting institutions are found to be important but not to the extent observed in the NID and variants. London is also found to have elements of a State-Anchored Region in that the presence of the Bank of England and the principal regulator is significant.

### **4.2 Questionnaire and Interview Survey Findings**

This section reports the key findings from the questionnaire and interview surveys which investigated the City/Canary Wharf cluster and the relationships between this cluster and businesses in the cluster fringe. The discussion is organised in terms of major themes that have emerged from the survey data. In the case of both the interview survey and the

questionnaire, the traditional City of London Square Mile was at the heart of the analysis. However because the City business concentration is part of a wider business cluster, firms outside the Square Mile were also approached.

1,500 questionnaires were sent of which 310 were returned. The questionnaire is fully reproduced in the Appendix. In almost all cases, respondents were asked to rank the importance of a factor from 1 (not important) to 5 (very important) with an option of 0 if not applicable. This is illustrated in Table 3 where cells indicate the frequencies of respondents choosing a score for different questions covering benefits of a London location. The total scores reported in the final column are simply the sums of recorded scores for a given benefit. Therefore the more 4s and 5s a benefit receives, the higher will be its total score. A useful benchmark for interpreting these totals is the average (mean) of the total score across all questions (where it was possible to compute a total score) which is 855. This may be thought of as the score that you would typically expect a factor to receive. Accordingly, a useful rule of thumb in comparing the relative importance of each factor is that any total score below 808 is relatively unimportant while any total score above 901 is relatively important (this is the 95% confidence interval for the interested reader).

The bold divisions of benefits into groups in Table 3 indicate where there are no statistically significant differences in the total score within a group but where there is a statistically significant difference between groups (see Appendix). This indicates that factors within two heavy black lines were regarded as being of roughly equal importance by respondents, but that either side of a black line there is a difference in the degree of importance attached to a factor. This method of presentation is used below on other tables reporting the results of questionnaire analyses. In addition, tests were conducted for the possible existence of statistically significant differences in the benefit scores among different lines of activity and for significant differences among firms of different size. Such differences will be commented on by exception where they are particularly strong and interesting.

Two sets of analyses for differences by line of activity were performed. The first looked at the three most frequently occurring lines of activity in the sample: banking, legal services and insurance. These three comprise half the sample and for technical reasons explained in the Appendix allow the most fine-grained analysis to be performed. Other sectors had too few responses to analyse without re-working of the data which entailed aggregation at the cost of

losing detail about the degree of importance attached to each factor. A meaningful, and at times revealing, analysis was feasible using responses for investment banking, accounting, management consultancy and fund management to be added to the other three. The number of responses to many questions does not add up to 310 (the total number of questionnaires returned) for the simple reason that some respondents did not answer every question.

Thirty nine firms agreed to interviews which were organized in a semi-structured fashion. The sample of firms interviewed was drawn from the major institutions located in both the City and surrounding areas. As with the questionnaire survey, the interviews sought data from London's dominant financial sectors: banking, accountancy, management consultancy, insurance, law, property services/real estate, and auxiliary financial services (e.g., financial market intelligence). Individuals from UK and foreign institutions were interviewed. The in-depth interviews provide important qualitative evidence on the key clustering issues for London as seen through the eyes of top decision-makers in financial and business services, and on the processes underlying the questionnaire findings.

### **General Benefits**

There are several important benefits of a London location. The findings are summarised in Table 3 in which the numbers in each cell refer to the number of responses to each option. The importance of a credible address stands apart at the head of these advantages. It is also among the most consistently mentioned themes in the interview survey, being raised as an important consideration by firms across a spectrum of activities and locations. It may be tempting to dismiss this as a frivolous reason but location can perform a valuable economic role by transmitting a credible signal of a firm's history and quality to its customers. Economic theory suggests that firms which provide the highest quality will have the greatest incentive to acquire the most favourable locations. Accordingly, the occupancy of the most prestigious address is a reliable signal conveying valuable information in the market. Reputation effects are themselves a source of cluster advantages as opinion, good or bad, influencing the reputation of an individual or firm, will flow more easily in a more compact geographical space. The interview survey highlighted the notion of a credible address as a well regarded *brand*. For example, a City location turns a law firm into a '*City law firm*'. Similarly, insurance companies gain prestige when in close proximity to Lloyd's of London.

**Table 3: General Benefits of a London Location**

<b>How important are each of the following benefits of your location?</b> (Please tick <u>one</u> box per benefit.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.)							
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>0</b>	<b>Total</b>
Your address is important to being perceived as credible	18	23	63	111	91	2	1152
You benefit from a strong, skilled labour supply	21	22	62	95	85	22	1056
You benefit from being close to market-leading customers	18	46	66	88	77	12	1045
Your customers external to London find it easier to locate you	32	42	72	98	46	15	954
You benefit from being near professional bodies	36	59	79	68	52	11	923
Knowledge transfer from the City's "financial atmosphere"	28	45	75	72	57	28	916
You benefit from being near leading competitors	49	58	63	73	41	23	851
Customers external to London find it easier to interact with you	45	58	87	62	35	19	845
Ability to find firms who will supply bespoke services	34	75	83	56	36	22	837
It is the best place to be to take market share from rivals	37	60	74	65	39	32	834
Proximity to a relevant exchange or physical marketplace	55	36	70	44	57	45	798
Ability to benchmark against competitors	67	68	72	43	23	33	706
Local rivalry amongst competitors is a powerful spur	63	70	69	44	18	42	676
Ability to access real time information on market trends	80	65	49	44	27	41	668
Support from local government	119	66	33	13	11	64	457
Access to venture capital	113	46	31	13	11	90	405

There are some important differences among firms regarding the importance attached to some of these general advantages. Firms in legal services and management consultancy place significantly more importance on having a credible address and taking market share from rivals. These businesses provide classic "credence services" where it is difficult to evaluate the quality of the service provided in advance. For such services, customers rely heavily either on a long-standing relationship or a projected image (partly created by the right address), brand image, trust and reputation. This excerpt from an interview with a law firm summarises very clearly the importance of a 'City' address and associated branding:

Geographically we're a bit pompous – most people come to us and I guess the issue would come if we felt we had to open another office – it would be madness – Things would have to change dramatically before we would leave the City. There's a buzz about the place ... the reason we have an office in the City now is that this is the biggest legal market in the UK and one of the biggest legal markets in the world. We want to be part of that.

**Table 4: Locations of Firms Rating the Importance of a Credible Address as Important (4) or Very Important (5)**

(figures in brackets percentages of firms in each line of activity located in each postal district).

	Banks	Insurance	Law	Accounting	Investment Banking	Fund Management	Management Consultancy	Total
EC1	0	3(9%)	2(4%)	1(9%)	2(18%)	2(20%)	0	10
EC2	15(58%)	4(11%)	11(23%)	0	6(55%)	1(10%)	8(40%)	45
EC3	5(19%)	24(69%)	5(10%)	1(9%)	1(9%)	4(40%)	2(10%)	42
EC4	5(19%)	0	21(44%)	5(45%)	1(9%)	2(20%)	3(15%)	37
WC1	0	0	4(8%)	1(9%)	0	0	1(5%)	6
WC2	1(4%)	0	5(10%)	3(27%)	0	1(10%)	2(10%)	12
W6	0	0	0	0	0	0	1(5%)	1
E1	0	3(9%)	0	0	1(9%)	0	2(10%)	6
E14	0	1(3%)	0	0	0	0	1(5%)	2
<b>TOTAL</b>	26	35	48	11	11	10	20	161

The table needs to be read with some care. It is based on a simple count of firms and is not weighted in any way by size of firm. The location is based on the location of the office returning the questionnaire and in several cases the firms concerned had more than one office. The popularity of some locations in the aggregate is influenced by the fact that law firms are the most numerous in the survey and are the most likely to rate the credibility of address as being important or very important. The fact that a firm has rated the credibility of address as being important probably, but not necessarily, suggests that it believes its address to be credible.

The pattern revealed in Table 4 reinforces some of the impressions gained from the cluster mapping. This is to be expected as firms in each line of activity will seek locations at the heart of their cluster and value the central locations. The physical propinquity and the kudos of the most prestigious addresses will be mutually reinforcing. Banks and insurance occupy overlapping but differently-centred districts. The spread of law firms probably reflects their need to be near their clients, who may vary depending on what areas the firm specializes on. Management consultancies are more broadly spread.

Proximity to customers and being easily located by customers figure highly among the benefits of a London location. Also important are access to labour and knowledge transfer. A factor which is unusually important is the presence of professional and government bodies (e.g., Bank of England).

Being close to customers and being easily found by external customers tends to be of greater importance to legal firms, but the difference is not statistically significant. Property/real estate and insurance companies place significantly greater emphasis on being near market leading customers and being close to a physical exchange or market place. These comments are representative of firms in the two sectors:

And in terms of our location – it is very central, it's in the heart of the City, we're in the financial services industry and this affords a very convenient location for what is the HQ ... and it means communications are good. As it's in financial services we have a lot to do with financial institutions, with investors, our fund management business is just down the road, so there is an ease and proximity of communication.

Our premises have to be in the City of London because this is their market focus. So we wouldn't be anywhere else because this is what we deal with – the City of London and its office development.

Banks place significantly higher importance on knowledge transfer and 'financial atmosphere' and tend to place a higher importance than insurance or legal firms on being near a strong skilled labour supply and receiving support from local government. As one major investment bank suggested, it is in London because of the "sheer intellectual infrastructure" and "the professional suppliers available". But, the bottom line is, if a bank wants to be credible as a 'global bank' it has to be in London. Here are two typical comments from banks:



We're here for two reasons – one is that we have an ambition to be an international bank and you can't be an international bank unless you have something in London. The other is that the exposure to London markets and London personnel and the ways of doing things in London is something we want to gain experience of and communicate through the rest of the Group. This is the place to do international business.

There's no chance of us moving anywhere else. First and foremost, as long as London remains the financial centre for Europe, then I don't see ... [us] ... moving away from it. Even if we changed the direction of the company we'd still need to have a presence in London if you're going to be a serious player in the financial markets.

Banks and legal firms are significantly more likely to rate proximity to professional bodies as being an important advantage of their current location and management consultancies are significantly more likely to rate it as being unimportant than firms in other lines of activity. At interview, banks referred to bodies like the Bank of England or Financial Services Authority, and legal firms to the Law Society and the infrastructure of the court system. Exactly the same pattern of difference was observed regarding the importance of being able to find firms who could supply bespoke services in the City/Canary Wharf (see later).

There is a marked difference between firms in the importance attached to being near leading competitors as a general advantage of locating in the City/Canary Wharf. Banks, insurance and legal firms are much more likely to rate this factor as being important than firms in other lines of activity, and management consultancies significantly less so. The results are shown in Table 5. In this table, the crucial comparison is between the actual count, which is the number of firms in each line of activity who gave a response in each category, and the expected count, which is the pattern which would be observed if the number of firms in each line of activity had their responses spread over the three categories of response in the same proportions as for the total responses added over all firms. The table shows, for example, that we would expect only 9.8 of the 29 management consultancies to rate proximity to competitors as not important (if they were giving similar responses to the other firms in the sample); in fact, 21 of them did, which is a very marked difference. Therefore any case where there is a big difference between the actual count and expected count indicates that firms in a particular sector regard a factor as being unusually important or unimportant.

Banks, investment banks and fund management firms are significantly more likely to rate the ability to gain real time information about market trends as an important advantage of a City/Canary Wharf location than other firms, and accountancy firms and management

consultancies are significantly more likely to rate it as unimportant. At interview, these findings from the questionnaire survey were substantiated in more detail. Banks in particular, acknowledged that proximity to the market and organizations which provided real-time data is crucial for their survival in the market, which is mediated in many instances through personal interaction and social relations. The spur of local rivalry is significantly more likely to be viewed as an important benefit by banks and legal firms and significantly more likely to be viewed as unimportant by accounting firms and management consultancies compared to other firms. The ability to benchmark against competitors is of far greater importance to firms in legal services than other lines of activity, whereas not a single management consultancy, and only one accounting firm, sees this as being either an important or very important advantage. Larger firms place significantly more emphasis on the importance of being near to market leading competitors, the ability to benchmark, being near a strong, skilled labour force, and the spur of competition.

**Table 5: The Importance of Being Near Leading Competitors**

	Count	Not Important	Moderately Important	Important or Very Important	TOTAL
<b>Banking</b>	Actual	12.0	7.0	24.0	43.0
	<i>Expected</i>	<i>14.6</i>	<i>9.8</i>	<i>18.6</i>	<i>43.0</i>
<b>Insurance</b>	Actual	16.0	11.0	30.0	57.0
	<i>Expected</i>	<i>19.3</i>	<i>13.0</i>	<i>24.6</i>	<i>57.0</i>
<b>Legal services</b>	Actual	10.0	16.0	31.0	57.0
	<i>Expected</i>	<i>19.3</i>	<i>13.0</i>	<i>24.6</i>	<i>57.0</i>
<b>Investment banking</b>	Actual	6.0	8.0	6.0	20.0
	<i>Expected</i>	<i>6.8</i>	<i>4.6</i>	<i>8.6</i>	<i>20.0</i>
<b>Fund management</b>	Actual	7.0	4.0	4.0	15.0
	<i>Expected</i>	<i>5.1</i>	<i>3.4</i>	<i>6.5</i>	<i>15.0</i>
<b>Management consulting</b>	Actual	21.0	3.0	5.0	29.0
	<i>Expected</i>	<i>9.8</i>	<i>6.6</i>	<i>12.5</i>	<i>29.0</i>
<b>Accounting</b>	Actual	8.0	5.0	2.0	15.0
	<i>Expected</i>	<i>5.1</i>	<i>3.4</i>	<i>6.5</i>	<i>15.0</i>
<b>TOTAL</b>	Actual	80.0	54.0	102.0	236.0
	<i>Expected</i>	<i>80.0</i>	<i>54.0</i>	<i>102.0</i>	<i>236.0</i>

One feature brought out in a number of the interviews is the importance of the wider attraction of London as a major metropolis. As one firm put it, “its history, its appearance, its buildings, its culture, its arts”. Interviewees emphasised the need to maintain London’s image as the place in which people want to live and work with regard to contemporary lifestyle fashion and choices, and taxation. London’s openness, cultural diversity, cosmopolitanism and ‘buzz’ are seen as governing the marginal decision for global companies about where to locate new business. One banker stressed that “Importantly, as a financial centre, London is an open society that is accepting to overseas people and to business”. In sum, London has an advantage as a global node in that it combines a wide range of advantages to provide an especially attractive location to do business.

You can talk about banking, taxes and all these things that are important and relevant but at the end of the day you’ve got a cluster of skills, an environment in which people can elect to do business with minimal interference, a rigorous regulatory framework, the language and the fact that as far as the professionals are concerned London is still a reasonably pleasant, albeit expensive, place to live.

London is seen as a positive place to come to because there is so much to do – the social environment rather than just the economic e.g., in comparison with Frankfurt – you can do a similar job in Frankfurt but outside the job it just doesn’t have the richness of things to do in a London environment. And so London, not just as the City, but London as a whole has that pull. There’s no chance of our moving anywhere else.

The vibrancy of the arts is a major pull against the negative factors – the arts, restaurants and so on. Yes it’s a case of nurturing it.

## The Labour Market

The labour pool from which London can draw is clearly one of its greatest assets and a key factor which sustains the financial cluster in the City of London. The questionnaire and interview surveys indicated the extent to which the City of London and Canary Wharf display classic cluster advantages in the labour market.

**Table 6: Labour Market Benefits**

<b>To what extent does labour flexibility within London lead to the following results?</b> <i>(Please tick one box per benefit.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.</i>							
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>0</b>	<b>Total</b>
A fluid labour market helps attract good staff	15	31	90	96	50	22	981
It is generally easy to recruit good people at short notice	15	36	94	98	41	21	966
It helps spread a network of contacts	19	35	88	94	47	22	964
It helps to spread knowledge of good practice	18	33	10	92	34	21	943
We can quickly tailor our staffing levels to our needs	17	50	10	77	32	26	894

The pulling power of London's fluid labour market is one of the most important engines of cluster dynamism. While a small number of respondents did comment on the negative effects of mobility, such as the bidding up of salaries and losing key staff to competitors, the advantages of mobility seem to greatly outweigh the disadvantages. There is a general tendency for banks to rate these labour market advantages more highly than insurers or legal firms.

The importance of the quality, international characteristics and strength of the London labour market was consistently stressed in the interview survey. Many respondents in all sectors remarked that the depth of expertise across the range of the professions is vastly superior to anywhere else in Europe. It is interesting, if inaccurate, that several made the claim that the size of the labour force in financial services in London far exceeded the entire population of Frankfurt, and using a football analogy, one respondent noted that London is in the Premier League while Frankfurt wallows in the Third Division. Here are two typical responses:

One is there is a skills base, people both front and back office, that exists in London that you'd probably have difficulty finding elsewhere *in the volumes you need it* to support the industry. So because the industry's grown up and evolved in the City then around it you have a large pool of skilled resource in the areas you need it *and some of those areas are quite specific*. So that's the major point. [authors' italics]

Recruiting the best people, the focus on London, the job pool, the communications, the City is a hub, a financial hub, it is good to be in if you're a plc, its easier to orchestrate your relationships with your key UK investors – you have the labour market here and for more corporate jobs like corporate finance etc. ... all roads lead to London.

The existence of a large labour market in a cluster gives rise to two advantages. Firstly, labour is attracted into the market, since the depth of the market provides a better chance of continuity of employment. As many of the interviewees noted, the best qualified workers want to work in London, whether they be lawyers, accountants, property consultants or bankers. Secondly, the sheer size of the market provides an incentive for people to invest in highly specific skills because a large market will aggregate sufficient demand for those skills to provide a sufficient degree of continuity of employment. As Adam Smith so penetratingly observed over 200 years ago, the division of labour is limited by the extent of the market. Size, coupled with the status and prestige of London and the fact that the most interesting and most well-rewarded work is to be found there, acts as a magnet for talent.

London offers an excellent array of career opportunities both within large firms and through the ability to move easily between employers. Several firms spoke of the problems of attracting top talent if they were in the regions. This is part of a classic self-sustaining process in clusters. The advantages of the cluster, including the size of the labour pool and other spillovers between firms, mean that it is unusually productive and so more resources flow to it which further re-enforce its advantages. What also emerges as being important about this process in London is that it acts as a magnet not only for national but also international talent. This, and the rich ethnic mix which exists in London anyway, means that there is access not only to a pool of talent, but one which collectively speaks a vast range of languages. One respondent of a major global non-UK firm rated London as having the greatest ethnic diversity of any of the locations in which they operated, at least as far as the relevant labour market is concerned.

The prestige of the capital, the quality of the experience that can be gained there, the ability to perfect the English language, and London's reputation as a cultural centre are all features

of the mix which makes the city so attractive. An interesting point made by two respondents is that many non-UK employees are particularly keen to work and live in London so that their children will attend English-speaking schools and develop strong bilingual skills. Culture alone is not enough, however, and one respondent commented on how low the flow of international talent to Paris is compared to London. Attracting this international talent to a regional base is perceived to be very difficult.

The London labour market is seen to have a number of other important features. The flexibility of the market is regarded as being a key advantage compared to other European countries. As one non-UK banking respondent put it, “We’re not afraid to put people here”. In any dynamic economy, there will be the ups and downs of the business cycle, certain firms expanding while others contract, and a large labour pool helps to smooth these cycles, in particular helping firms find more labour more easily when expanding than compared to a smaller labour market. The ability of staff to gain experience in London is a means of transferring best practice internationally.

In x you get – I can’t do this, I can’t do that. I can’t employ these, I can’t employ those – in a way which just doesn’t exist in London. It is important. The reality is in London we have virtually total flexibility as long as we have the money.

An analysis of the geographical reach of London’s labour market in recruitment terms indicates two main trends. Firstly, most labour is recruited from within the South East. Secondly, the ability to draw in labour from around the world, not necessarily in great numbers, is important to all (and very important to a small number of firms). Therefore, it would appear to be equally important to maintain London and the South East as an area to which people can migrate. For some grades of staff, the recruitment is overwhelmingly of people already in London but the more senior and more specialized labour becomes, the further afield the relevant labour market extends and for some types of labour, the London market has global reach. In Table 7, banks and investment banks emerge as recruiting a significantly smaller proportion of their staff from the South East and insurance firms significantly more. One commented:

Our skills are brought from all over Europe to London. We see London as THE European hub in our European network.

Responses on staff commuting patterns in the interview survey reveal that in many cases firms' staff tend to come from certain specific areas in and around London and that the ease of access for skilled client facing, secretarial and back office staff to an existing central London office would be a key factor ruling out a significant change of location. The concentration of transport nodes around the City is seen as a major advantage in terms of staff recruitment. In banks and legal firms, high-earning skilled staff are said to favour living in the more expensive outer boroughs of London, for example, Richmond upon Thames and Wimbledon, in the West End, for example Kensington, or in the rural commuter belt. Some senior staff prefer to commute weekly to London and retain central London flats convenient for the office. There is also evidence of some inter-city weekly commuting to London from other UK and European cities for top staff. Skilled support staff tend to live further from the centre of London, either in the suburbs or outside London where housing prices are lower. Distance from central London was discussed as being related to age and household circumstances as well as cost. Younger skilled staff are said to favour living in fashionable and convenient central London districts while older staff of all grades with children are said to move further out from the centre in spite of added commuting time and cost. The location of favoured schools emerges as an important housing location factor in some interviews. For some staff, this is likely to be with reference to private schools.

**Table 7: Recruitment of Staff (all grades) from the South East**

	Count	<61%	61-80%	81-100%	TOTAL
<b>Banking</b>	Actual	16.0	12.0	16.0	44.0
	Expected	13.1	8.2	22.7	44.0
<b>Insurance</b>	Actual	13.0	6.0	40.0	59.0
	Expected	17.5	11.0	30.5	59.0
<b>Legal services</b>	Actual	15.0	14.0	31.0	60.0
	Expected	17.8	11.2	31.0	60.0
<b>Investment banking</b>	Actual	9.0	5.0	6.0	20.0
	Expected	5.9	3.7	10.3	20.0
<b>Fund management</b>	Actual	1.0	4.0	12.0	17.0
	Expected	5.0	3.2	8.8	17.0
<b>Management consulting</b>	Actual	14.0	3.0	13.0	30.0
	Expected	8.9	5.6	15.5	30.0
<b>Accounting</b>	Actual	5.0	2.0	9.0	16.0
	Expected	4.7	3.0	8.3	16.0
<b>TOTAL</b>	Actual	73.0	46.0	127.0	246.0
	Expected	73.0	46.0	127.0	246.0

The ability of firms to recruit senior managers via informal channels, which is likely to work most effectively in a compact geographical space, is highly important in sustaining the cluster. Not surprisingly, it is least important for graduate recruitment which tends to be

more routinised and where the candidates concerned will have less of a reputation that might be broadcast over informal channels. This is particularly important in investment banking and fund management. It is noticeably less likely regarded as important by legal firms. Firms in legal services rate the informal recruitment of graduates significantly more highly than do banks and insurers. Informal recruitment is also reasonably important for client-facing staff. Insurance companies are significantly more likely to rate informal recruitment of client-facing and back office staff as important. Evidence from the interview survey supported this finding: because of the compactness of the City of London and the high degree of interdependencies between banks, law firms, insurance companies and property services in particular, the informal recruitment of senior and graduate staff is routine in nature.

Finally, the presence of a pool of talented labour with relevant skills is a highly important factor which contributes to the ability of firms to innovate in the City of London and financial fringe (both West End and Canary Wharf). There is virtually no difference in the importance attributed to this factor by firms in different lines of activity. Evidence from the interviews suggests that labour market churn/turnover is an important mechanism for all sectors to bring innovation into the firm, whether that be the specificities of particular labour market processes or tacit and formal knowledge brought about via new cultural working practices or management structures.

### **The Importance of Personal Relationships**

London's financial cluster is sustained and reproduced through the continued importance of close geographical proximity as firms, institutions and professional bodies continue to forge and maintain important relationships through information technology, face-to-face contact, and formal and informal business and social interaction (Table 8).



**Table 8: The Importance of Close Proximity to Other Firms**

<b>How important are each of the following reasons for having a location in close proximity to other firms in London?</b> (Please tick <i>one</i> box per reason.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.							
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>0</b>	<b>Total</b>
It is easier to build and maintain personal contacts	12	15	46	123	101	7	1177
The ability to have face-to-face contact	14	15	37	108	117	12	1172
It is easier to build relationships of trust and cooperation	17	33	71	98	73	13	1053
It is easier to communicate because we have a common understanding of the business	27	33	67	108	51	17	981
We generally have complementary expertise with such firms	24	47	101	80	34	19	911
Multi-disciplinary teams can be assembled more quickly	30	46	73	86	41	27	890

The supreme importance of maintaining personal contact and being able to interact face-to-face is clearly manifest. In the financial cluster, one could argue very strongly that the process of face-to-face contact not only contributes to the creation of wealth for the cluster, but also acts as a factor of production. In the questionnaire survey, the importance of maintaining personal and face-to-face contact are the second and third most highly ranked factors across the whole questionnaire. The ability to establish relationships of trust is also one to which the compactness of the City still makes an important contribution. Synergy is also apparent in that there is clear evidence that the City is a system replete with mutually beneficial relationships. The existence of common understanding and complementary expertise are classic characteristics of dynamic clusters and are much in evidence here. While they are not the most highly ranked factors within this group, they are highly important compared to the generality of factors examined in the study. Larger firms are significantly more likely to rate trust and ease of communication as being important and to rate personal and face-to-face contact as being highly important more frequently than smaller firms.

The importance of this contact was underscored by the interview survey. Several firms emphasized the importance of a face-to-face meeting for conducting complex transactions where it is important to fashion agreement while reducing the chances of misunderstandings or creating antagonism. A face-to-face meeting has the advantage that more information is conveyed, including non-verbal signals which are important, for example in trying to judge whether someone is honest and trustworthy or in gauging whether the person is unhappy or

becoming upset. At the stage where deals are being transacted, a crisis can emerge at any time and it may need a meeting to sort the matter out quickly and satisfactorily. In comparison, e-mail is a poor substitute. One firm suggested that this requirement places a particular emphasis on the importance of senior staff being based in London. Similarly, several firms cited the need to be close to regulators in order to have the ability to meet face-to-face to resolve important issues and to cement an ongoing relationship. The impression gained in the interviews is that there is a deep-rooted need to conduct certain business in this way. One firm stated explicitly that simply the knowledge that it would be possible to call a snap meeting is important, even if such a meeting is eventually unnecessary. The importance of being able to meet people before doing business with them, to establish relationships and trust, to provide a customised service and to conduct negotiations was widely emphasised.

Proximity is an advantage in terms of the ability to have face-to-face meetings because it allows them to be called at short notice and it is possible to have a greater frequency of meeting because time and money costs are less than if people have to travel long distances. Some firms commented on how difficult it is to set up team meetings with staff who work for the same firm but at different geographical locations. Being able to meet more frequently helps build a team. A number of firms in banking and legal services commented on the need to have adequate space for large meetings because their size has grown as transactions have become larger and more complex, leading to larger numbers of professionals being involved in negotiations. Several firms emphasized that while there has been a burgeoning use of e-mail for intra- and inter-firm communication and of video conferencing for intra-firm communication, neither of these media would ever replace the need for physical face-to-face meeting. One respondent reported on the vastly increased use of video-conferencing and e-mail within his own firm, but also on the immense pressure on the firm's meeting room space. Several respondents commented that e-mail and video-conferencing work much better with people you know, so face-to-face meetings will continue to be important in forming relationships that can subsequently rely on more remote media of communication.

You're never going to replace face-to-face contact as you can't pick up body language; you can't build relationships truly over the phone and with video-conferencing. They help because they make things more efficient but it's never going to replace the face-to-face contact. Even internally there is a point when you have to go and meet people even if you've seen them on a video-conferencing basis because you don't get a feel for that relationship aspect.

It is important for firms to be able to meet, especially with their top-level clients who require, and are prepared to pay for, a Rolls Royce service. This may include receiving visits from back office as well as client-facing staff. One insurance firm emphasized the perceived importance for the client of meeting with the person who might be dealing with their claim in the event of mishap. Several interviewees emphasised the importance of trust:

Trust is very important and there's a price attached to that. We do a great deal to try to preserve and maintain our reputation and credibility and reliability.

The compactness of the City means that it is possible to have a greater density of interaction. This has a number of benefits, important among which is the ability to build both a relationship and a reputation.

We know most people in the City involved on the property side and just walking through the City you'll meet people that you know. It's important to have that relationship to know what's happening in the market – people you can trust, people you can use to advise you. And it's important with all the people that you deal with to have that regular contact. A lot of activity is done through personal contact; it's done through talking to people.

The compactness of the City is also an advantage in terms of serving overseas customers, since it affords them the chance to come to London and have meetings with all their advisers and perhaps also meet a range of different banks, for example. Talking about international clients, one firm stated:

If you're talking about corporate finance, big finance, you want to get together in a room. So if you have a community like London where you have lawyers and accountants and investment bankers all operating, then the client will tend to come to you. There may be meetings where you say you want to go and see them, for example in areas of the UK outside London, but at the execution phase then you would tend to do that near the people who drive the execution process – that tends to be the bankers and the lawyers for example where documentation is being produced.

An important benefit of the density of information which physical propinquity allows is that knowledge flows more easily. One respondent bemoaned the demise of the City lunch which was seen as a powerful way of ensuring that people knew what was going on and what the key developments in the market were. Another respondent explained:

You want to be able to meet with your biggest customers over lunch – take the head of x out to lunch and see what he thinks – and it's being able to say to someone – look I'm going to be walking past your building this morning I'll just pop in and see what you're doing about this, that and the other – again it boils down to human contact – if you want to keep your finger on the pulse and in the loop – you can't get that from the trade press and so ... actually a lot of that comes from dinner parties and cocktail parties – it's informal but that's what you miss if you're not in the loop.

Another benefit of dense interaction is that people become socialized in the sense that they absorb norms of doing business as well as the language in which business is done. There is a significant tendency for accounting and, to a lesser extent, legal firms to rate their complementary expertise as being important. Somewhat surprisingly, no fund management firm rated this factor as being important or very important. There are also significant differences in the frequency with which firms rate ease of communication due to a common understanding of the business as being important, with banks and, to a lesser extent, insurance and legal firms rating this factor as being important more frequently and investment banks and fund management firms rating it as being less important. There is some tendency for the ability to build and maintain personal contacts to be rated as very important more frequently by banks and legal firms. The ability to have face-to-face contact tends to be rated as very important most frequently by insurance firms as indicated by the following remarks:

Lloyds is still very much a little village where everybody communicates with each other and in insurance generally. All the badge players have to know each other and have to know what they're doing or they're going to go out of business.

**Table 9: Methods of Interaction between Firms**

<b>To what extent has your firm benefited from the following types of interaction with personnel in other companies? (Please tick <u>one</u> box per factor.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.</b>							
	1	2	3	4	5	0	Total
Contact by telephone for information e.g. about a legal matter, a technical question, the name of a trade contact	16	24	74	116	67	7	1085
Contact by telephone/e-mail for short-term problem solving	19	26	76	104	73	7	1080
Mixing with industry colleagues in social settings	22	36	78	95	66	9	1038
Mixing at local business meetings/events	17	38	74	103	62	11	1037
Chance meetings where you hear interesting information	28	52	76	89	56	5	996

The importance of personal relationships is underscored in the responses to question 10, the most highly ranked group of factors. It might appear at first blush that the fact that telephone and e-mail are the most highly scored ways of having important interaction with staff in other companies belies the need for physical proximity. However, these answers, together with those in Table 8, cast doubt on such a superficial conclusion, since an important interaction is likely to hinge on common understanding, trust and complementarity of expertise. Moreover, one is likely to interact more frequently with those with whom one has a more intense personal relationship.

Meeting socially, whether by chance or design, is palpably of great importance. Mixing at business events and telephone contact for information is significantly more likely to be rated as important by banks and larger firms. Contact for short-term problem-solving tends to be emphasized by management consultancies who have a disproportionate tendency to rate this as very important, though the difference is not significant. Banks and investment banks also have a tendency to rate contact for problem solving as important more frequently than other types of activity. The interview survey revealed that while chance meetings were not emphasized as a key driver of location decisions, they are an important benefit of proximity. The kind of things discussed in chance meetings tend to be industry gossip about what particular individual firms or people are doing, what key developments are taking place, and sometimes bouncing ideas for new products or services.

Results from the interview survey entirely corroborate the questionnaire survey regarding the importance of social relationships in sustaining the cluster and the significance of specific meeting places where interaction occurs. These interview excerpts demonstrate the existence of both ‘old’ and ‘new’ City practices of interaction in the cluster and articulate the importance of both tacit and formal knowledge transfer in the cluster via business and social interaction amongst all relevant sectors:

I think there’s still a circuit. There’s a circuit where senior chaps meet whether it’s dining in clubs or getting invited to events by the Corporation of London or whoever it is, there’s obviously client entertainment – there’s a huge merry-go-round at all levels. For example whether it’s the printing firms inviting the junior people ... or the chief executives going to Glyndbourne – that whole scene is very much alive and well.

New ways are down the sports club rather than the old clubs – down the gym. It needn’t be the boozy lunch – it’s places people want to go. The City has lots of good restaurants and clubs and stuff, and who wants to belong to a club it takes four years to get into – it’s a bit stuffy. Now it’s all about a balanced lifestyle type of networking.

Finally, it must be noted that the interview survey highlighted that being able to walk between firms, institutions, professional bodies, bars, gyms etc. was of great significance in sustaining both face-to-face contact in business transactions and social/business (in)formal interaction, especially in the compact geographical area of the Square Mile. As one bank emphasised, “walking distance is still important in the City”, and the over-riding view of the interviewees is that being able to walk to clients, suppliers, markets etc. remains one of the immeasurable locational advantages of the City of London.

### **Sources of Help with Innovation**

Table 10 sheds light on the sort of local relationships that help innovation in the cluster. A pool of skilled labour and customers are the two most important factors, and both are very highly ranked. Larger firms are significantly more likely to rate the labour pool as being important.

Legal firms have a tendency to rate help from customers as important, but not significantly so. Banks and insurance firms have a tendency not to rate this factor as important so frequently. Local suppliers and firms that provide complementary activities are also important in helping firms innovate. Both banks and insurance firms are more likely to rate the presence of such firms as important than firms in legal services. Firms in the same line of

activity also assist to an appreciable degree in innovation, a phenomenon well documented in the case of manufacturing, and it is interesting to find evidence of it in the service sector. As revealed in Table 11, it is banks that are significantly more likely to rate the presence of other banks as making an important contribution to innovation. The same tendency is evident for fund management, but management consultancies are significantly more likely to rate the presence of other management consultancies as being unimportant. Larger firms are significantly more likely to rate the presence of other firms in the same line of activity as being important in this respect. Banks are also significantly more likely to rate the presence of firms who supply complementary goods and services as being important to innovation. The same tendency is more weakly evident for investment banks.

**Table 10: Local Relationships**

<b>How important are the following types of local firms/institutions in helping your firm achieve innovative solutions?</b> <i>(Please tick <u>one</u> response per firm/institution type.)</i> <i>Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.</i>							
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>0</b>	<b>Total</b>
A pool of talented labour with relevant skills	19	31	42	79	111	22	1078
Customers	21	38	60	69	102	16	1063
Firms who help you supply your service/product	28	44	80	71	58	26	930
Other firms in the same line of activity	38	64	96	67	18	20	812
Industry associations	65	72	77	44	18	29	706
Academic institutions	98	85	55	24	10	33	579
Local government	13	63	28	16	7	51	448

In terms of the importance of local customers, the questionnaire survey reveals a significant difference in the extent to which firms rely on local contacts to generate work, although the measure is crude. The majority of firms rely on local contacts for less than 60% of their work, illustrating the centrality of London as a global node.

**Table 11: The Importance of the Presence of other Firms in the Same Line of Activity in Promoting Innovation**

	Count	Not Important	Moderately Important	Important or Very Important	TOTAL
<b>Banking</b>	<i>Actual</i>	8.0	18.0	18.0	44.0
	<i>Expected</i>	14.5	16.0	13.4	44.0
<b>Insurance</b>	<i>Actual</i>	18.0	23.0	16.0	57.0
	<i>Expected</i>	18.8	20.8	17.4	57.0
<b>Legal services</b>	<i>Actual</i>	20.0	17.0	18.0	55.0
	<i>Expected</i>	18.2	20.0	16.8	55.0
<b>Investment banking</b>	<i>Actual</i>	6.0	7.0	7.0	20.0
	<i>Expected</i>	6.6	7.3	6.1	20.0
<b>Fund management</b>	<i>Actual</i>	3.0	6.0	8.0	17.0
	<i>Expected</i>	5.6	6.2	5.2	17.0
<b>Management consulting</b>	<i>Actual</i>	18.0	8.0	2.0	28.0
	<i>Expected</i>	9.3	10.2	8.5	28.0
<b>Accounting</b>	<i>Actual</i>	5.0	7.0	3.0	15.0
	<i>Expected</i>	5.0	5.5	4.6	15.0
<b>TOTAL</b>	<i>Actual</i>	78.0	86.0	72.0	236.0
	<i>Expected</i>	78.0	86.0	72.0	236.0

### **Proximity, Competition and Cooperation**

Question 4 on the nature of competition did not produce a particularly clear ranking of factors. Competition on cost/price, and on service differentiation emerges as more important than innovation, product differentiation and the ability to serve customers across borders, but their primacy is marginal. These results are unsurprising given the complexity and dynamism of the City market place, and the range of products and services in which competition takes place. One clear trend that did emerge is that banks and insurance companies are significantly more likely than other industries to rate competition through service differentiation as important. Again, this result might have been expected given the nature of business in the sectors in question.

Innovation is generally important and location appears to be most important for helping develop new markets and better ways to deliver services and products. Banks are more likely to rate location as being an important contributor to their ability to compete through product innovation and management consultancies less likely. Banks are also significantly more likely to regard their location in the City/Canary Wharf as making an important contribution to their ability to innovate through developing new services. Finally, banks are noticeably more likely to regard location as making an important contribution to their ability to innovate both through strategic re-orientation and the development of new organizational structures.



**Figure 2: Sector Inter-relationships**

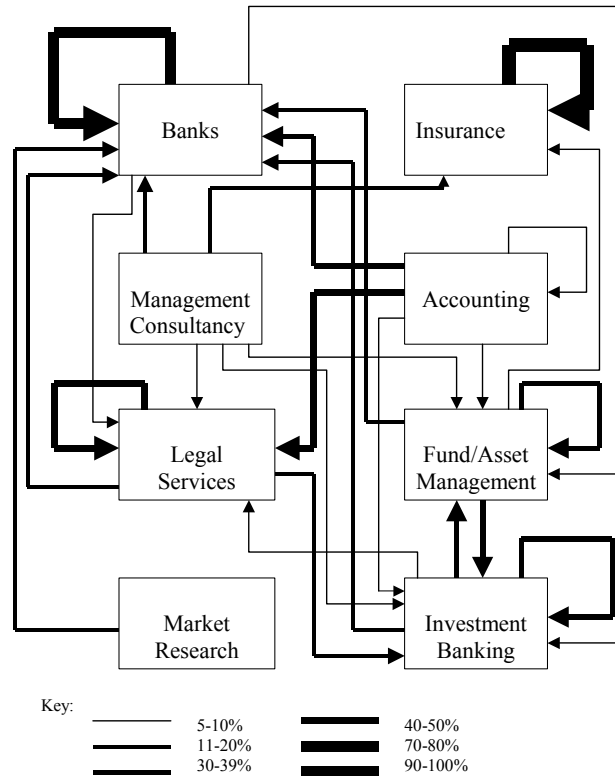


Figure 2 provides a schematic of which sectors are most closely inter-related. The figure has been constructed by first allocating each firm to a sector on the basis of what it classes as its most important line of activity. The next step was to examine which sectors those firms stated are the most important in terms of inter-relationships (Q8 on the questionnaire). Only those sectors ranked 1 were included. In answer to the question, 74 firms did not provide a ranking, but rather ticked three or more boxes: these have been excluded from the analysis. The arrowheads show the direction of the relationship with the arrowhead entering the sector rated as the most important with which to have a relationship. The thicker the line, the stronger the relationship. It is essential to bear in mind that the diagram conveys no information about the number of rankings: for example, there were only five valid rankings made by market research firms, one of which went to banking (20%). Table 12 gives information on the absolute number of number 1 rankings.

**Table 12: Number One Rankings for Importance of Inter-relationship Received by Each Sector**

	<b>Number of Times Ranked</b>	<b>Percentage of Total Ranks</b>	<b>Number of Times Ranked by Other Sectors</b>	<b>Percentage of Times Ranked by Other Sectors</b>
<b>Banking</b>	52	26%	23	23%
<b>Insurance</b>	47	24%	8	8%
<b>Maritime</b>	4	2%	4	4%
<b>Mgmt Consulting</b>	2	1%	1	1%
<b>Accounting</b>	4	2%	3	3%
<b>Legal Services</b>	35	18%	15	15%
<b>Advertising</b>	1	0.5%	1	1%
<b>Fund Management</b>	15	8%	12	12%
<b>Recruitment</b>	2	1%	2	2%
<b>Publishing</b>	1	0.5%	1	1%
<b>Market Research</b>	1	0.5%	1	1%
<b>Property</b>	3	1.5%	2	2%
<b>Printing</b>	0	0%	0	0%
<b>Investment Banks</b>	24	12%	19	19%
<b>IT Related</b>	4	2%	4	4%
<b>Electronic Info.</b>	2	1%	2	2%
<b>Telecomms</b>	2	1%	2	2%

Taking the table and the figure together, a number of factors stand out. Firstly, banks, including investment banks, appear to be at the hub of the cluster. This is true to a lesser extent of legal services and fund management. Secondly, there is a very high incidence of sectors ranking inter-relationships with firms in their own sector as most important, especially in banking and insurance. Thirdly, some sectors, most starkly accounting, appear to depend more on other sectors than other sectors depend on them.

The interview survey revealed further insights into which firms are most valued as neighbours. One general feature of the interview evidence is that being close to customers is the most important factor. Where international customers are concerned, the “closeness” relates to the fact that being in the centre of London puts firms on their beaten track, so while not close comparing HQ to HQ, they are close in the sense that they are regarded as easy to get to. Another general cluster advantage which works to the benefit of the cluster and the customer is that having a range of firms in the same line of activity in close proximity means that there is a strong competitive spur driving firms to innovate, improve service quality and keep down costs. The question arises of who the customer is. For many firms it is a question of derived demand in that they get work from other firms in the City/Canary Wharf who are

themselves servicing a corporate or private customer. For many firms, access to IT specialists is a crucial issue. Law firms need to be near banks, including investment banks, and insurance companies from whom they draw much of their work. Insurance lawyers are heavily concentrated around Lloyds. For law firms there is an added factor that they also need to be close to the courts.

The original reason we came here will have been very much influenced by the fact the old merchant banks were here – what we now call the investment banks. Investment banks are a source of work and a source of clients and that's always been valuable for practices like ours. Being here is all tied up with London as a prime international centre – there's absolutely no doubt about that. There's no other place in the world where it would be logical for us to have the most number of people. And that is entirely tied down to London's international standing because our focus has always been City related work and the City related work now is of such huge importance internationally. So we're very dependent on London retaining its status and therefore London remaining attractive to the key banks.

A number of firms remarked that it is not a big issue that some of their clients have moved to Canary Wharf. They acknowledge that it would make visiting the client more awkward, but view the extra burden as not being significant enough to warrant moving. In other words, Canary Wharf is viewed as being “close enough” geographically to the traditional Square Mile in terms of accessing clients located there.

Additionally, as financial services become more standardized and novel products or services are easy for rivals to copy, so firms are competing on service differentiation. There is a need to be close to clients in order to work out bespoke solutions and to provide a high level of personal service. One firm put great importance on being able to get their clients to visit their premises so that they could get a rich experience of the nature of the firm with whom they were dealing. In some businesses it is important to be near clients in order to cut down on the time and money costs of visiting them. This factor was above all stressed by accounting firms, where staff spend a particularly large proportion of their time with clients. One advantage of being close to other firms in the same line of business is the ability to work out solutions and share risk.

There is an awful lot of business that is done which is joint business between institutions. More and more large transactions are done jointly and the risk is spread between different organizations so there's a need not only to get together with a client but to get those proposing the solution together.

Being close to other types of firm which provide complementary services is important because it enables multi-disciplinary teams to assemble quickly to meet client needs. It is also convenient for clients, particularly those who travel some distance to London, to be able to see a range of their advisers quickly and efficiently. Several respondents pointed to the need to draw together complementary expertise to work out novel and bespoke services for clients. It is judged to be less likely the case that a client would have a pure financing or legal requirement. Another benefit of being able to draw in complementary expertise quickly, and build and maintain relationships with those who provide complementary expertise is that firms will recommend each other to clients. It is therefore important to be in the loop in the City/Canary Wharf in order to tap into this source of demand.

I think it was the case that you had to be in the City because of the need to physically interact. There were certain financial transactions which had to take place because of the time criticality – discount market members and messengers used to carry pieces of paper from one bank to another and they had to be in before 10 o'clock. With electronic banking that doesn't happen but there are other reasons why people still need to be in the City. Proximity and face-to-face contact are essential in the investment banking business. There are those that argue against it because clearly the very successful global investment banks have all got huge places down at Canary Wharf and they don't feel that necessity (to be in the Square Mile). But we feel comfortable here – we're close to the Bank of England, lawyers and accountants, the regulators who advise us. It's inconceivable to me that we would do anything other than stay in the City.

The above quotation illustrates an important point made by several respondents, that the historical reasons for being in their current location are somewhat different from the reasons they stay in their current location. Two respondents put it this way:

It's not only where your clients are, it's where your suppliers are. And that's suppliers across a broad range from the professional suppliers like lawyers and consultants and accountants through to all the other suppliers.

First of all if you have a centre which is relatively tight and you want to draw together a meeting of three disciplines then it's very easy and very quick. If people are distributed around, it takes longer and we have to be fast in financial services to be able to move quickly. It works in a number of ways. If you want to do something which is a collection of different people for a trade association ... you want to pull people into that meeting. You don't have to spend a lot of time out of the office to get to that meeting. So you get much more cohesion from people turning up at these meetings if the transport time is shorter – that's one reason why you have people in close proximity. You can draw people together very fast. Equally if you want to have a seminar or lunch – important people can leave the office and come back in the afternoon – there's a convenience point of view.

### **Disadvantages of a London Location**

Two of the most pressing problems for firms in London are the cost of premises and transport difficulties, particularly the state of the Underground system (Table 13). The issue of government regulation appears to be equally important to firms of all sizes and in different lines of activity. Interestingly, the Euro issue emerges as less significant although there is some tendency for this to be ranked as a more important issue by banks.

There is no statistically significant difference between firms in different lines of activity in the extent to which they rate government regulation as an important factor impeding the growth of London. However, there is a clear tendency (that a larger sample would likely pick up) for banks to rate this factor as being important more frequently than firms in other sectors. Also, there is no statistically significant difference in the extent to which firms rate cost of premises as being an important impediment. Again there are tendencies that a larger sample might pick up: banks have a noticeably greater tendency to rate costs of premises and insurance and legal firms a noticeably lower tendency. The pattern of responses regarding transport issues is somewhat more complex. There is virtually no difference in the pattern over the seven lines of activity considered regarding national transport links, but there are stronger differences, though not significant, between sectors regarding the Underground and international transport links. The state of the Underground appears of strongest concern to management consultancies and least so to firms in insurance and legal services. The greatest concern about international transport links appears to be among banks.

**Table 13: Disadvantages of a London Location**

<b>The Extent to Which Factors Were Judged to Impede the Growth of London.</b> <i>(1 = not important, 5 = important, 0 = not applicable)</i>							
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>0</b>	<b>Total</b>
Cost of business premises	8	19	64	110	103	5	1193
State of the underground	14	29	59	84	114	8	1155
National transport links	23	34	67	85	89	10	1077
Government regulation	29	41	66	68	80	22	981
International transport links	39	48	79	55	65	20	917
Local infrastructure (including buildings)	26	63	92	69	39	14	899
Environmental quality and pollution	43	72	99	48	20	26	776
The UK's current position outside the Euro zone	82	76	57	29	26	37	651
Availability of staff with language skills	73	68	69	41	12	44	640
Access to venture capital	101	52	50	15	8	80	455
Other	0	0	1	2	13	3	

Larger firms are significantly more likely to rate the failure to join the Euro as an important issue, but nevertheless do so in a comparatively small number relative to other factors. Smaller firms are significantly more likely to rate lack of access to venture capital as an important impediment, and this factor should therefore command greater attention than its comparatively low ranking suggests.

The centrality of the inadequacies of the transport system as a concern about the ability to operate effectively in the City/Canary Wharf is borne out by the interview survey, with almost every respondent emphasising it, and a number wanting to dwell on this single issue. Interestingly, while the cost of office premises is clearly a major business planning consideration (as discussed later), this was not prioritised as a threat to the cluster. Transport, however, is widely seen as “a massive all-encompassing problem”. The interview survey found that the significance of transport links at different spatial scales varies in terms of the particular operational difficulty it causes firms, the nature of the firm itself and its specific

location. Some firms' office networks are predominantly London-based while others have an extensive national network of regional and sometimes local branch offices. In many cases the choice of location is a trade-off between the relevant catchment area for staff and established travel to work patterns, the ability to reach and be reached by customers easily, and the cost of property. This respondent's comment illustrates the strength of feeling expressed by many on this subject:

Public transport is the end. The dispute between the DLR and the Jubilee Line for example. Technology is a mess in and out of London – it's disgusting, unreliable and uncomfortable. I hate travelling in and out – the bit here to Tower Bridge is the worst – the City is seized up. We've worked very hard to make things happen. France, Germany and Spain have much better transport. The problem is there's no consistency in policy, someone needs to be responsible.

There is a crucial issue regarding the ability to cross London especially for business trips. Some respondents pointed to the example of Lazards moving to the West End, where most of its major corporate clients are, to avoid the inconvenience of travelling between the City and the West End for meetings. Conversely, one respondent in a fringe location spoke of the intention to move to an office in the City in order to overcome the difficulty of travelling to clients there. "This is not monetary, pure cash, it's the lost time".

In terms of travel to work patterns, being located anywhere away from the centre is perceived to limit the geographic scope of where staff would travel from. To some extent this is more limiting at lower levels in the organization as senior staff have the wherewithal to pick a more favourable residential area with a view to travel to work. Many respondents expressed their concern about the impact of vexing and lengthy commutes on their staff, sapping their energy and enthusiasm. In addition to over-crowding and unreliability there was a degree of adverse comment on the sheer shabbiness of the Underground, and concern was expressed regarding the safety of the electrical installations. One firm explicitly stated that it had ruled out a move to Canary Wharf on the grounds that its staff would have found it difficult to get there. Another firm spoke of a decision not to move to Canary Wharf because it would involve "taking a risk on transport". This feature of travel-to-work patterns is a very important issue when thinking about relocation of activity. As the following quotations illustrate, while the cost of housing in London is not seen as a key issue threatening the cluster, there is a relationship between transportation difficulties and the cost of living centrally in London, identified by several respondents as itself being a growing problem:

I don't think (London housing costs) are higher. Actually the costs are less. Our costs of people living in Singapore or Hong Kong, even Moscow, are just as high as in London. They're less in Germany, slightly less in Paris. They're certainly less in Amsterdam but I wouldn't have said that is a factor at all.

I hear lots of complaints about transport, I hear less about houses. People seem to cope with housing just by moving further out. Then they get clobbered by the transport system – you become more and more reliant on having an efficient transport system which we manifestly don't have.

Within the Square Mile there is less of an issue regarding transport, since people can walk to appointments in about 15 minutes (this appears to be regarded as the upper limit for travelling to an appointment with ease). However, the problems of traversing the centre of London, particularly East-West, were identified by many respondents as a key concern. The following quotation illustrates the nature of the concern, which turns on the unpredictability of travel and the cost in terms of wasted time and energy:

How much time is wasted? A lot of time and money and someone should add it all up. All the routes East-West constantly jammed up. The tube incredibly unreliable, breaking down – the Central and the District Line. And if you're trying to get from or to Heathrow, you're in one of these traffic jams – it's getting to people.

The major concern regarding international travel is access to airports, especially the City-Heathrow link and to a lesser extent the reliability of transport once the airport has been reached. One respondent based in Canary Wharf reported leaving three hours before a Heathrow flight in order to avoid missing the flight, and clearly regarded this as being unreasonable. One respondent who expressed an opinion on whether the problems of international travel stopped people coming to London doubted that it would. Nevertheless, there were references to meetings being delayed or cancelled because people arriving on international flights had difficulty getting from the airport to the meeting. One thing which to some extent overcomes the problems of getting, for example, from Heathrow to the centre of London is that, once there, international firms are able to efficiently arrange a series of meetings with firms in close proximity.

City Airport is good, it's nearby, but getting to City Airport is a complete pain and people's experience generally of flying out of City Airport is that you're always delayed.

The accessibility of Heathrow and Gatwick from the City is a problem. If you look at where those links go to – you're talking Victoria, London Bridge. .... The Heathrow Express has made it considerably easier to get from Heathrow to Paddington but then



you've got the nightmare of trying to get from Paddington to the City which can take three times as long as getting from Heathrow to Paddington.

The poor state of the transport infrastructure, described by one respondent as being of "Third World" standard, is something which is perceived to create a negative impression of the city with international clients.

International clients travelling to London are pretty shocked at times because the infrastructure is so bad, lack of investment, how shabby it is, how poor the service is.

Considerable dismay was expressed by a number of respondents regarding the failure to develop a coherent policy to improve public transport in London. Anger was expressed by several at the attempts by the Mayor of London to cajole people into using cars less and public transport more when the public transport system is perceived to be inadequate. Furthermore, unfavourable comparisons were made between the inefficiency of the public transport system in London compared with superior systems, for example, in Paris and Frankfurt. Only Tokyo received a mention as being worse than London. A fair degree of scepticism was expressed regarding the likely impact of congestion charging, a common fear being that if it worked, it would simply displace the problem by shifting large numbers of people on to a creaking transport system which can barely cope with existing traffic. One respondent who had worked for 35 years in the City judged the decline in the standard of public transport over that period to have been "enormous". Another stated he had abandoned the District Line after 30 years in favour of his car because of a continual decline in standards. A number of respondents made the point that they had to be located in the cluster and were therefore forced to put up with declining transport conditions but that others may have a choice. One banking respondent said that until the firm's confidence in transport infrastructure increased, no new business activities are being brought to London. The view of an auxiliary financial services respondent summarised a common perspective: "What you've got to avoid if you've got a city and you're trying to protect your franchise is you've got to avoid the feeling that if you don't have to come into London, why bother".

While transport was singled out as a key problem by almost all respondents, many also commented on regulation and legislation as being an even more serious potential threat to business clustering in London. A principal concern appears to relate to European legislation which, crudely stated, is seen as likely to lead to a levelling-down of London, particularly in

relation to the erosion of flexibility, damaging the ability of firms in London to ‘get the job done’. One respondent referred to the threat as ‘death by a thousand cuts’. Shedding light on questionnaire responses on the Eurozone, the single currency is not regarded as an issue but UK involvement in European policy and the promotion of a single market is seen as highly important.

Another issue is the risk posed by ‘over-burdensome’ and complex UK regulation leading to increasing amounts of working time having to be diverted in trying to keep abreast of requirements. One respondent described the nature of the problem, “Monday to Friday I’m dealing with the queries put on me by the central regulators and the rest of the week I can spend doing my job”. On the other hand, there is a clear recognition that effective regulation is essential to maintain the credibility of the financial services sector. The main message that comes across is the need for balance. Some respondents spoke of a major general concern that a lack of coherence in policy making, including direct and indirect taxation, could lead to a range of changes which will erode London’s attractiveness as a place to do business, as one respondent put it, affecting “the marginal decision ... do we send business elsewhere?”. The following quotations illustrate some of these concerns:

It is just overwhelming, impossible for anybody to understand the complexities of the modern regulatory system. The regulators don’t understand it, the regulated don’t understand it ... the ability to move and do things for our clients – there are whole areas where we would refuse to act for people because, unless it’s a really large amount of money, it’s not going to be justified by the time we’ve got through the paperwork.

There comes a point in time where the degree of regulation has got to such a degree that it’s turning people off coming to the City and that’s a very fine line.

European legislation, employment and social, is a nightmare – it worries us and it’s all part of the chipping away. And it’s the things I deal with all the time – the prospectus directive – all these directives from Brussels which we’re having to work incredibly hard on.

It’s the barriers to entry. There are a couple of things. Stamp Duty is a core issue. If we want to make sure that London remains competitive then no matter what the Corporation do – let’s say they completely re-write their building planning policies, encourage environmentally friendly development ... if the government of the day continues to provide invisible barriers to trade – insurance premiums, tax, airport taxes, Stamp Duty – it’s the indirect taxes.

Of course part of the attraction to many people are the relatively low direct rates of taxation but if in fact there is an increasing bill on indirect taxation whether its rates, property tax, whatever, then you're going to tilt the balance the other way too much and I think that's something the Government's got to be very, very conscious of.

A current concern commented on frequently in the interviews was the vulnerability of the City/Canary Wharf to terrorist attack. Some firms emphasised the importance of adequate contingency plans to cope with a major disaster. Nevertheless the concerns in themselves were not discussed as a serious threat to the cluster. The comment, "I think people have short memories with that sort of thing" summed up the general feeling though one respondent believed that, were a major attack on the City/Canary Wharf to take place, this could provoke movement out of London. A number of other issues were occasionally mentioned as being negative aspects of London, such as street crime, untidiness and restrictive City planning regulations, but these disadvantages appeared to be second order.

### **Declustering**

In addition to exploring the benefits and characteristics of London clustering, the factors that push firms to consider relocating away from the City were discussed - what sorts of functions they would consider moving out of the City, where they would consider moving them to, and what factors would militate against migration out of the City.

The high cost of office space is the key reason for considering moving business activities from a central City of London location. Moreover, as one firm observed "London is expensive for everything". Lower cost of premises is a commonly cited factor tempting firms to move to Canary Wharf, and in addition the fact that more suitable premises are available there for firms requiring large floor plates. Canary Wharf is also judged to have more reasonable and flexible landlords, and a good choice of utility suppliers. As these interviewees commented:

We do have accommodation at Canary Wharf but it's predominantly used for back office activity and it's just proved convenient to go that way.

The reason people have been going to Canary Wharf is because it's cheap, very, very cheap compared to the West End and I would put that down much more than anything else. A firm like us on the trading side we need big, big, open areas for traders and not every building in the old City of London can accommodate that – none of them could.

Looking at one of the main differentiating factors (Canary Wharf) as a future landlord ... is very facilitating of all the issues that we have to deal with. (The Corporation) is well meaning but ... it relates to history too, we're here because this is where it started, building round the exchanges, you can't flatten the City.

In spite of these advantages, many City based firms would not consider moving to Canary Wharf. Transportation is an important factor. One firm bemoaned the problem of lack of reliability. "It's a huge problem, people coming in late, the tube's been stuck somewhere." However, the problem would seem to be associated not just with transport capacity and reliability but also with distance from the multiplicity of transport nodes in the City and central London. One firm commented, "What we're interested in is the infrastructure of where we are, but the primary driver is workforce." As discussed earlier, accessibility of office location for key staff was widely discussed as a major advantage of a City/central London location. Crime was discussed by one respondent as a disadvantage of Canary Wharf over the City as a location for junior staff wishing to live nearby. The reluctance of staff to relocate to a non-central location and inadequacy of transport links are the key disincentives to move from a central City location especially in relation to Canary Wharf. As one interviewee commented:

In our business we have to be central - we could be West End, we could be City but we happen to be x - we could also be Canary Wharf. I personally don't think we would go to Canary Wharf - it's a hell of a long way away. (Being central) is to be where our clients are, they're the corporations and the companies - most of those are probably West rather than East of us apart from the financial services which are all around us. Investing institutions - people who manage money - our clients on the equities front or the debt front are all scattered around the City of London and whatever anyone says, proximity to them is important.

Conversely, London Bridge is seen as an attractive possible alternative location due to its good transport links and walking distance to the Square Mile. The problems of movement across central London by taxi or Underground particularly east-west were consistently cited as disadvantages of other fringe locations. Many firms have considerable sunk costs in their property which provide another disincentive to move. One firm reported that the cost of fitting out the building it presently occupied, including its critical IT installations, was almost as much as the building itself. It would therefore need a very compelling reason to induce them to move and face these set-up costs anew. On a related point, one firm reported that it is doing back-office e-processing overnight in the City for some of its Far Eastern offices because it already has the necessary systems in place to do so. One firm suggested that a

further impediment to moving to fringe locations in the East, including Canary Wharf, is that many wealthy senior decision-makers do not want to live on that side of the city.

The West End is perceived as an attractive fringe location in London for some business activities. Five institutions were interviewed in the West End of London, and in most cases, each of these institutions focuses on private clients or the local market rather than interfacing directly with the City of London. Two banks interviewed are located in the West End because they have to be in close proximity to their suppliers and customers in Mayfair and Westminster. The legal and accountancy firms interviewed travelled to their clients across London and the City, but are mindful that potential fee income is lost in travelling time (as travel time could not be charged to individual clients). But, as with the financial cluster, high rents and the decaying transport infrastructure were cited as real-time threats to the sustainability of the 'mini-cluster'.

Some enforced locational changes are the result of planned redevelopment. Firms in this situation discussed the requirement for the City to accommodate the needs of large, expanding firms and those of many smaller firms and start-up businesses. In this context, one firm believed that "given the number of new buildings going up in the City" adequate space should be available for business expansion; "the Corporation seems to have got that right". Relocation to potential new business clusters within Greater London is widely dismissed due to staff preferences, lack of proximity to the central cluster and the need to have a central London address to be "Brass plate up to the big organisations". A location outside Greater London in the South East or elsewhere in the UK is considered viable only for non-client-facing staff. Firms involved in dealing felt that they still need to be in the City/Canary Wharf because these activities have been "much less dematerialised" than other types of activity. Several firms sounded a note of caution about the extent to which back-office functions could be spun out from the City. Some back-office functions are purely routine and lend themselves to de-clustering, and many such activities have indeed already been relocated. Other back-office functions, however, are specialised and depend upon knowledge of City practices and probably also knowledge of the client. These operations are not candidates for de-clustering. More fundamental perhaps than the front office/back office or client-facing/non-client-facing distinction is whether or not the particular activity is routinised or commoditised as opposed to being bespoke or complex. If a business activity is commoditised or routine, it is amenable to declustering. But it is not that straightforward:

We haven't reached that stage in the circuit yet – we presently have the back office staff for the London business here in this building and it is not too difficult to ask the question – do you need to have a back office near x – what benefits does it bring – back office has no customer connection etc, with IT you can do it anywhere. The question is would you find, in Milton Keynes, skilled staff? Because back office is not anymore manual, routine, repetitive – you need quite a number of skills – and if you wouldn't find those people in Milton Keynes would they be prepared to move there?

Of the back office, there would be some functions you could ship out – finance, to a certain extent some admin. but the operational that actually are the analysts need to have a central location that you can catch that extra piece (of information) from. There's a balance – the senior members of those back office functions should be talking to the back office of the client. It's all very well selling something to the end user, you've then got to make sure you can deal with that effectively. So they need to be discussing those particular elements, they also need to be able to take feedback from the users in much more detail than comes through the sales people.

Even when relocation to the fringe makes sense, it also makes sense to maintain some presence in the centre of the cluster. Where in the fringe firms would consider moving to depends on what line of business they are in and where they are currently located. Firms servicing private clients might consider moving to the West End, which is where these clients tend to be located. One firm stated that it had considered moving to the West End for this reason, but had decided against it because trading is still an important part of its business and for this reason a City location is favoured. The same firm commented that those firms which have set up in the West End are mainly “boutique outfits” offering specialised services. Several firms stated that any move outside London would be unconscionable because of the damage it would do to their credibility. As one insurance respondent put it “The City still has the connotation of – good address, got to be there at the centre”. An auxiliary financial services respondent took the view “Every firm worth its salt operates with headquarters here in the City”.

Some firms made the point that in order to get a substantial benefit in terms of lower costs they would now need to move quite some distance from London, probably outside the South East but, as the following quotations illustrate, finding a move which is truly cost-effective is not necessarily easy:

There are firms that have successfully broken the mould, they've moved away from London to other places in the UK but it's not an absolute given. So if you were to look at x experience in Lewisham what they found out is that they didn't move far enough so people still have to get on a train to get to Lewisham and why would I want to work in Lewisham – why not go three stops further and work in London again? The opposite of that is x which took all of its back office staff down to Bournemouth which worked very

well. But the converse of that would be when x and x went to Dublin where the labour market was just too small and too tight and although they had cheaper occupancy, they were paying over inflated rates for labour. It's a pretty mixed bag of the positives and negatives of the people who've moved away from London.

These days it is hardly worth bothering unless you're moving to Birmingham or north of it to get the savings and obviously that increases the risk. Which is why – good news for London – I think most of us are still here ... You can forget that because the reality of life is anything international, whether you like it or not, this is not that big a country and so there's an incredible focus on London and coming to London and people understand that if you said our Head Office is in Blackburn you'd get a blank response from an international point of view and there's no point in trying to dress it up. All the lawyers, all the accountants are here. In Birmingham you drop down several layers in functional infrastructure. Why would you want to shift it elsewhere?

Several firms expressed an opinion on whether the promotion of financial services business clusters within London (additional to the City and Canary Wharf) or elsewhere in the UK would be viable. Most were sceptical, pointing to the business reasons for continued concentration in the City/Canary Wharf cluster and the need for alternative business reasons to decentralise to another location. One firm stated that the City is made up of mini-clusters anyway, of insurers and lawyers for example. It would therefore be problematic to introduce a polycentric model since it would be impossible to transplant the industry clusters and maintain their important juxtaposition with other related industry clusters. A range of other comments suggested the need for careful consideration of plans to establish any new clusters that are not in close proximity to existing infrastructure and business concentration as illustrated by the following interview extracts:

We (the UK) won't be able to afford to put up new infrastructure projects in Huddersfield or Glasgow if UK plc doesn't make the money that it needs to in London. If London is seen by certain people in government as just another English City – disaster.

We did look at moving to Reading and we looked at the costs of moving there as opposed to staying in the City ... it's the services, security, suppliers etc, etc which wouldn't be available outside the concentration ... Without IT infrastructure and specialists we die.

You can envisage some parts of London like Paddington Basin getting new tenants from Europe or elsewhere at a reduced rent but what you can't envisage is a service firm like ours setting up there. London Bridge may not technically be part of the City but it's the same area, and it's easy to communicate and travel between those parts, so I hope that answers the question.

If people say, we don't like what's going on in the City, we're going to create a new financial industrial complex somewhere, say Reading, that's engineering, that's not going to work. I mean Canary Wharf was to some extent that sort of experiment and it really hasn't worked ... people just didn't want to go out there and the infrastructure was absolutely useless ... (but) if they put this new airport in Kent, Canary Wharf will take off.

We considered as part of our strategic plan for this area whether we might review the lease on this building given that a lot of the building is used for back office activity. And perhaps it wasn't necessary to be bang in the middle of the City and we didn't want to go to Croydon or Bangladesh or Manchester, so we thought about London Bridge.

What you have in London is a European regional centre servicing the largest companies in Europe. For example, even a large global investment bank which has, let's say 250 people in Frankfurt, it will service German companies part out of Frankfurt but it will still service them out of London as well and that isn't going to happen from Manchester.

For a US company, given the choice, they could just about get their mind to Windsor i.e. outside London but if you said to their employees in Atlanta, we're moving you to Blackburn to work in our European head office, they'd all head for the hills.

I suppose I see Canary Wharf more as overspill than as a separate cluster ... it is surprisingly difficult to get people in different offices to act as part of the same team ... we have one big x office in the UK and it's much more cohesive (than between offices in 7-8 German cities). I think if that sort of competition between regional centres is replicated, it must damage the whole.

In short, if Canary Wharf is viewed as an extension of the City cluster or as an overspill of the cluster as viewed by many interviewees, then all things being equal, the weight of evidence from the interview survey suggests that declustering is not occurring from the City of London. In fact, given that the City of London remains a tightly defined geographical area of global capital, which is constantly articulated as a global node in a space of financial flows, with more connections to New York City, Hong Kong and Singapore than to Reading or Croydon, its future is very sustainable. Moreover, the intensity of concentration in the City of London will continue to cluster disproportionately in relation to other areas in the capital and South-East of England.



## 5. Policy Implications

This chapter examines the implications of the key research findings for policy and the role of public policy at different levels in promoting the London financial cluster. Spatial policy frameworks at different levels that have relevance for the cluster are reviewed in light of evidence from the questionnaire and interview surveys together with an international comparative study on issues of sustainability to identify key priorities for public policy.

### 5.1 Implications of the Key Findings for Policy

#### General Benefits

- London is a dynamic and successful cluster whose working is entirely in line with extant knowledge on the clustering phenomenon (indicated in our literature review as well as by our questionnaire and interview surveys). Access to the concentration of labour, customers and professional and government institutions is a critical advantage of proximity within the cluster. Maintaining London's attractiveness as a location for these activities should be a key policy priority.
- Banks and, to a lesser extent, law, insurance and fund management are at the hub of the cluster, and therefore particular weight needs to be placed on the requirements of these sectors as many others in the cluster depend on them.
- The labour market is of fundamental importance to the cluster; and keeping it attractive and fluid is therefore a top priority.
- Transport and regulation are the key policy areas where businesses see a threat to London and are urgent policy issues.

## **The Labour Market**

The scale and depth of the labour market (the two being related) is a crucial advantage. The expertise concentrated in the London financial cluster is based on the ability to attract the highest quality labour from a global labour market which is a self-reinforcing process. This puts a premium on keeping the labour market attractive. The attraction of London as a major metropolis and cultural centre is important in drawing in labour, especially international labour, hence there is a premium on keeping London's amenities and reputation in these areas up to scratch for the good of its commercial success.

The labour pool is embedded in the cluster, and is where the knowledge and expertise which give London its supreme position in financial services reside. Being near a strong, skilled labour supply is particularly emphasised by key hub firms, e.g. banks and large companies. From the business perspective, a further advantage of the labour pool which draws firms to have operations in the cluster is the flexibility of the labour market by international standards. The policy implication is that a watch needs to be kept that this advantage of labour flexibility is not eroded by over burdensome regulation.

The relevant labour market for many staff is heavily circumscribed by the choice of a firm's location and the feasibility of commuting. This is an argument for a review of transport priorities as the labour market will function in a more integrated way if people could travel more easily across the city. This consideration also has implications for the provision of new housing in London and the South East (where most staff live), and where this is built will bear upon which parts of the city have access to the labour force that will be housed there.

## **The Importance of Personal Relationships**

### **(i) Face-to-Face Interaction**

Many of the perceived benefits of being in the City turn on the fact that being physically close enables face-to-face contact and relationship building to take place. Much the same may be said of the importance of trust. E-mail, telephone and video conferencing, while extensively used, are seen as poor substitutes for face-to-face interaction. Both formal and informal interaction is of great importance. Some respondents indicated that certain business might not take place at all if face-to-face contact were not possible. This is a powerful

argument for keeping the cluster as compact as possible (possibly envisaged in terms of time and ease of travel rather than physical distance).

### **(ii) Knowledge Transfer**

Proximity within the cluster produces a density of interaction and information that promotes knowledge transfer. This is important for dynamism and the ability of firms in the cluster to serve clients in high value-added complex activities. It is particularly emphasised by banks who occupy a central place in the cluster. Such knowledge transfer is effected by a variety of mechanisms all of which are promoted by compact space and particularly associated with a City location. Examples include formal and informal meetings, labour mobility and chance meetings. The policy implication is that it is important to maintain, as far as possible, the geographic compactness of the cluster. In terms of transport policy, it is important that plans to develop locations near the City, such as London Bridge and at Canary Wharf, take into account ease of movement around the cluster.

### **(iii) Inter-firm Linkages**

There is clear evidence of close and important inter-firm linkages among local firms, particularly those with complementary expertise, which above all translate into an ability to provide high level services to clients e.g. the ability to form multidisciplinary teams which can work well together quickly and which, to a somewhat lesser extent as indicated by our evidence, also lead to innovation (see also Sources of Help with Innovation). The ability to form inter-disciplinary teams is particularly important in respect of client meetings and is again a particular advantage of locations in the City. The policy implication is that it is very important to keep a geographically compact, multifunctional cluster.

Proximity to the customer is highly important, perhaps more so than has been revealed in the existing clusters literature. This relates to major clients themselves based in or near the cluster, to firms who rely on other firms in the cluster for a derived demand for their services, and to the ease for international clients of doing business, perhaps with a range of firms based in the cluster. All three of these factors again have the policy implication that it is important to maintain a compact cluster. There are also implications for transport policy. The convenience and efficiency of geographical propinquity is being undermined by problems of traversing the city. In terms of international clients there is the added issue of getting to the City/Canary Wharf from Heathrow.

## **Sources of Help with Innovation**

Location appears to be most important in helping to develop new markets and better ways to deliver. The co-location of a pool of skilled labour and customers is an important stimulus to innovation. The link with innovation is particularly strong for banks. The implication for policy is that physical clustering of service firms and customers should be sustained and promoted to support innovation.

### **(i) Institutional Thickness**

Many firms in London benefit from being close to a relevant exchange and/or other important institutions such as a regulator or trade association. The policy implication is that the benefits derived from this source would be weakened by dispersing the cluster in line with a polycentric development model.

### **(ii) Role of Local Government**

Banks more than other lines of activity find help from the local authority beneficial. This implies an opportunity for co-operative working between banks and local government, and it merits review as to whether ways can be found to reinforce this link.

## **Proximity, Co-operation and Competition**

The balance of co-operation and competition is manifested in the City as in the classic clusters literature. Large firms and banks place particular importance on being near other leading competitors as a feature of being in the cluster and helping to maintain their competitiveness.

## **Disadvantages of a London Location**

### **(i) Transport**

Transport is highlighted as an extremely important concern of business with clear evidence that its shortcomings are acting as a drag on the efficiency of the City/Canary Wharf and possibly beginning to deter visiting international clients. While not imminently threatening the cluster, it appears to be a high policy priority to ease the problems identified, in particular travel-to-work, travel East-West across central London, and travel between Heathrow (and other airports) and the City/Canary Wharf.

## **(ii) Regulatory Context**

Here the evidence was equivocal insofar as firms indicated that while rigorous regulation is important in giving a quality assurance to work done in London, many also expressed the view that regulation is becoming burdensome, indeed unmanageable. Regulation emerges as a particularly important concern for banks. The policy implication is that the regulatory burden needs to be reviewed and monitored in relation to rival financial centres. There is also a need for co-operation across agencies to ensure that contradictory effects on London's attractiveness as a place to do business are not created.

## **(iii) Cost of Premises**

While this is most highly ranked disadvantage in the questionnaire survey, the interview evidence implies that it is more an annoyance to firms than a fundamental threat to the viability of the cluster (see also De-clustering). Policy must continue to provide top quality commercial premises for the diverse range of companies located in the cluster, from the global investment banks to small, specialised companies.

## **(iv) The UK and the Eurozone**

This is not a major problem but it appears more of a concern to banks than to firms in other lines of activity, which is significant given the centrality of banks within the cluster. Interview evidence revealed that a key concern is that the UK should be actively engaged in European policy, particularly in the development of the Single Market.

## **(v) Small Firms**

In the questionnaire survey, smaller firms indicate that the lack of access to suitable potential venture capital may be a concern. The immediate policy implication is that there is a need to review support for small firms. Moving beyond the issue of venture capital this may have implications for the provision of start-up premises and other forms of support to new/small businesses.

## **(vi) Second Order Issues**

There are a number of what appear to be second-order issues concerning business such as security, crime and environmental quality. While these are not prioritised as important threats to the sustainability of the cluster, they should be taken into account in future policy for the cluster and for London's transport infrastructure.

## **De-clustering**

It appears that it is the more routine/low revenue types of work that are being spun out of London (and, to some extent now, the South East) due to high space and labour costs. Accessibility for skilled staff is a key reason for an office location in the cluster together with the need to have a credible address. Policy will need to take account of the fact that these are decisive reasons for firms not moving high order office functions away from the cluster and in particular from the City.

### **(i) Relationship between the City and Canary Wharf**

Canary Wharf is now viewed as being essentially part of the City. The lesson is that it is possible to provide space for development a little way outside the City but the experience of Canary Wharf implies that this cannot be too far away and accessibility is a key policy issue (close proximity to the City is regarded as a benefit of London Bridge as a potential office location). Linked to this, the availability of suitable floorspace (particularly for banks) and the lower cost of premises are powerful reasons for firms moving to Canary Wharf yet many firms still in the City have no desire to do so. This indicates how resistant a lot of firms are to moving outside the City - they need a compelling reason to do so. Any plans to develop new spaces outside the City would need to question whether such developments would provide such a reason and if so, for what type of business.

### **(ii) Sustainability of the Cluster**

The cluster is robust. Few immediate threats are evident and the cluster is deeply embedded. London has advantages in high value, complex and bespoke services which, combined with the embeddedness of its expertise, gives it a hard to copy advantage over other financial centres.

## 5.2 The Role of Public Policy

### Global Policy Context of the Cluster

As the previous discussion has emphasised, it is essential that public policy frameworks should take full account of the London cluster's wider relations as a global city. The dynamics of the concentration of financial and business services within the confined space of the City/Canary Wharf are fundamentally linked to shifting global and regional market conditions and business practices. Activities within the London cluster perform a key role in the management of global business networks within the European region and spawn a multiplicity of interrelationships and impacts at a range of local UK, European and global geographical scales. Recent research sheds light on the complex interdependencies associated with the London cluster's agglomeration economies, and evidence from the questionnaire and interview surveys indicates the importance of appreciating these interdependencies in policy-making.

- First, the concentration of talent, knowledge, languages and decision-making in the London cluster operates as a global business platform for which flows (inward and outward) of people, skills and information are crucial. UK legislative and regulatory frameworks are therefore critical to the future of the cluster. The concern is that piecemeal changes across a wide range of policy issues could damage the flows that sustain business activity in London.
- Second, the questionnaire and interview survey findings provide evidence of many benefits derived from the dense spatial clustering of associated activities in the City/Canary Wharf and the key role played by physical proximity within London in generating global business agglomeration economies. A significant point revealed by the interviews is that relationships associated with the co-presence of skilled labour and global corporate customers are facilitated by close proximity and face-to-face interaction, and that such relationships are critical to the operation of high complexity, high value globalized business activity. Depth of concentration is therefore not only a major reason to be located in the London cluster but also a major reason why firms wishing to be successful international players cannot afford not to be located there. Both hard data from the questionnaire survey and qualitative data from the interview

survey therefore provide strong evidence that the close co-location of office space within London is essential to the continued presence of global financial and business services in the UK.

- Third, following from interdependencies between the global nature of financial and business service flows and the need for proximity, the findings on cluster benefits indicate a strong relationship between locational concentration and London's operation as a global and regional hub. The scale of London's trans-nationally constituted labour pool has been shown in both surveys to be critical to clustering since people and knowledge are the key assets of service business. Density of transport nodes is therefore very important to the ability of firms to access a labour market that extends across London and the South East. The major concerns expressed by respondents about transport in London reflect the crucial importance of movement for financial and business services activity. The success of the cluster in drawing international business to London relies upon international travel and travel for business meetings as well as commuting, which all generate cross-London movement. Hence, it is not surprising that inadequate public transport infrastructure, east-west movement by taxi for central London business meetings and access to Heathrow are prioritised by interview respondents as a key threat to the cluster alongside regulation and legislation, and that poor accessibility is widely seen as a major disadvantage of the geographically distant part of the London cluster based at Canary Wharf.
- Fourth, an additional important finding from the interview survey is the significance of non-economic factors for clustering: cultural and social criteria have an important role in determining which places people and business are attracted to. The interviews indicate the need to be aware of contemporary life-style preferences and to preserve London's attractiveness as a place where business people want to live, work and visit. Tax regimes, high quality education and housing appear to be important as is what has been described as the city 'buzz' associated with restaurants, the arts etc.

Together these interdependencies can be seen to operate as important determinants of London spatial clustering posing a significant challenge for 'joined-up' policy-making. The identified strengths of the London cluster for business - skilled, talented people, business-friendly



environment, cultural assets - and the key potential threats to its future - transportation and regulation – illustrate the ability for a wide range of policy initiatives to either promote or damage concentration. This helps to explain the emphasis of some respondents on the problems of what is seen as conflict over London’s transport, the lack of policy co-ordination and a need for more direct UK government involvement in the financial services industry. The research findings indicate that the determinants of the future success of the London financial and business services cluster cross both horizontal (geographic) and vertical policy boundaries. This point is reinforced by the review of spatial policy frameworks that have a bearing on City clustering in light of the research findings.

### **Spatial Policy Frameworks of the Cluster**

To satisfy the international comparative elements of our terms of reference we need to explore spatial policy frameworks. Three interrelated themes underpin current European, national, regional and London spatial policy guidance (see also Interim Report, 2002). First the theme of ‘*sustainability*’ runs through policy statements at the level of the EU, the UK, the South East and London. The term, which emerged from the Brundtland definition of ‘sustainable development’ (WCED, 1987, p.43), is widely associated with economic, social and environmental relations. However, a lack of conceptual clarification has led to loose associations being made between ‘economic growth’ and ‘sustainable development’ in policy applications. Two closely related themes with particular relevance for the research findings are those of polycentric urban development and compact city development.

#### **(i) Polycentric Urban Development**

European non-statutory spatial policy guidance for government and administrative authorities at national, regional and local levels in the *European Spatial Development Perspective (ESDP)* aims to work towards balanced and sustainable development throughout the European Union territory (CSD, 1999). The achievement of three fundamental goals - economic and social cohesion; conservation of natural resources and cultural heritage and more balanced competitiveness of the European territory - are closely linked to the development of a ‘polycentric urban system’ within the EU (ESDP, pp.10-11 and pp.19-20). Spatial polycentricity has long been associated with priorities for balanced development in parts of continental Europe and the concept has been incorporated in current planning policy for the South East and London.

Polycentrism generally refers to the clustering of activities across a number of centres as opposed to concentration in one centre, though definitions and applications of the concept vary. In relation to London and the South East Region, polycentricity seems to have been interpreted both in terms of intra-urban and inter-urban regional clustering (see the draft London Plan - Mayor of London, 2002, p.40 and p.46; RPG9 - GOSE, GOEE, GOL, 2001, p.15). Polycentric Urban Regions (PURs) have been considered superior in relation to economic, social and environment sustainability objectives to what has been referred to as 'mono-centric' urban development commonly associated with London and Paris.

However, recent international European research indicates that some assumed advantages of PURs for economic, social and environmental sustainability are not supported by empirical evidence. The research also questions whether polycentric patterns of urban development can be successfully superimposed on existing spatial relationships through the policy process. A review of current evidence based on experience in the Rhein-Main, Germany and the Randstad, Netherlands for this study by Michael Hoyler (University of Heidelberg) and Robert Kloosterman (University of Amsterdam) supports these doubts. Regional spatial polycentricity is shown to have advantages and disadvantages in relation to three measurement criteria associated with economic, social and environmental sustainability: cross-regional functional interdependencies, distributional patterns of economic growth and development, and environmental impacts.

Importantly for this research, the comparative study suggests that the spatially concentrated development characterised by London within the UK has unexpected sustainability benefits. London's critical mass should facilitate investment in superior public transport infrastructure and is more spatially delimited. Its scale encourages an evolving spatial division of labour and it also has a strong identity that reflects a 'sense of place' and promotes 'imagined communities'. The study therefore supports evidence from the questionnaire and interview surveys that the scale of business concentration in one place provides the critical mass necessary to support a range of urban assets that are not easily created in smaller centres.

In addition, current academic thinking on polycentricity reflects the view of London as a highly interconnected global node as identified in this research. The conceptualisation of London clustering as a 'mono-centric' spatial form overlooks the multiplicity of functional connectivities at a range of local to global spatial scales associated with its role as a regional

hub or node within a European and global polycentric city network. As one of the three global financial services hubs, business agglomeration in the restricted space of the City/Canary Wharf has a specialised function within firms' global business networks, providing the spatial focus within Europe for a concentration of skills, decision-making and control. London's wider connectivities therefore play a key role in connecting the UK and Europe with international business activity. Indeed this perspective on concentration in London is reflected in the ESDP which recognises the emergence of urban networks across Europe and the pre-eminent position and importance of London as a global city (together with Paris and the Ruhr and Randstad metropolitan regions) in encouraging stronger EU integration into the global economy (ESDP, pp.64-65).

London's strong interdependencies with the Rhine/Ruhr, Randstad and Paris within the North West Europe area are identified in the ESDP as having special importance for the European Central Zone. The ESDP recommendation that co-operation between European governments and city authorities is needed to promote the inter-connections and complementarity of policy (ESDP, p.21) supports the findings of this research in that the lack of cross-boundary policy co-operation was identified as damaging to the cluster. Equally, co-operation will also be essential to strengthen mutually beneficial flows associated with business agglomeration in London. London's role as the leading 'gateway city' in the European Central Zone is emphasised in the ESDP but it is also regarded as causing a bottleneck to through-transportation movements to continental North West Europe (CSD, 2000). ESDP priorities in relation to transport support the need identified in the research to strengthen London's transport networks and their links with international and trans-European networks.

Strategic EU spatial policy in relation to polycentricity does not therefore appear to threaten the position of the London cluster but rather it seeks to spread the benefits of clustering to other parts of the EU through inter-city co-operation and improved transportation infrastructure.

## **(ii) Compact City Development**

The second important EU and UK strategic policy theme relevant to the research findings is an association between a sustainable urban form, 'densification' and the concept of the compact city (CEC, 1996; DETR, 1999; Urban Task Force, 1999). One respect in which the spatial concentration associated with London is held to have environmental sustainability

benefits compared to PURs is that development can be more easily spatially contained through planning policy. Within the UK, the *Urban Task Force Report* Recommendation 3 creates a presumption against excessively low-density urban development taken forward in *Planning Policy Guidance Note 3 - Housing* (DETR 2000a) and the *Urban White Paper* (DETR, 2000b). *Regional Planning Guidance for the South East (RPG9)* (GOSE, GOEE, GOL, 2001) and *the Draft Spatial Development Strategy for Greater London* (the draft London Plan) (Mayor of London, 2002). UK policy therefore endorses the importance of maintaining London's position as a global business centre, promoting sustainable economic, social and environmental development, the compaction of development, and encouragement of brown-field development.

### **(iii) The South East**

Regional policy supports the maintenance of existing Green Belt boundaries (RPG9, Policy E3, p.33) and discourages decentralisation of economic activity from London to the Rest of the South East (ROSE) which is seen as posing a threat to London's position as a global city (RPG9, p.14). Concerns that the South East Region is under-performing in European terms with pockets of uneven development give rise to aims for growth centred on knowledge-based industries in economic strategies for ROSE (South East of England Development Agency, SEEDA and East of England Development Agency, EEDA) and new development linked by non-car modes of transport (RPG9, p.39). London is expected to maximise its contribution to regional housing provision (RPG9, p.14) and this is reflected in plans to increase housing supply within London and encourage higher density development (London Plan, p112 and Policy 3A.1/2, p.115).

The research findings suggest that the housing needs and preferences of the City/Canary Wharf labour market should be taken into consideration in formulating local plans for new development within London and the South East taking into account specific locational determinants, such as income, household size and structure, for different categories of workforce. It seems unlikely that commuting from the South East and outer London suburbs will decline significantly for as long as business concentration in London is maintained since evidence from the interviews indicates that many financial and business services employees are prepared to undertake long and costly travel to work journeys to live in places where they wish to raise their families. While the high cost of housing in central London is believed to be a stimulus to longer distance commuting, the wide range of housing/location choices and

staff circumstances indicated by interview respondents suggests that there is in practice a complex relationship between cost, space, location and lifestyle choices. A recurrent pattern relating to staff living in central London identified in interview responses is that fashionable cosmopolitan locations seem to be favoured by younger skilled workforce, small, very central flats convenient for the office by weekly commuters, and top quality, central London residential districts by the most highly paid senior staff.

Compact urban development is closely associated in both South East Regional and London policy with objectives to cluster economic activity around key transport nodes promoting environmentally sustainable development. This principle is reflected in the identification of ‘Priority Areas for Economic Regeneration’ (PAERs) (RPG9, pp.15-16 and RPG9 Policy RE7, p.43) and ‘business clusters’ (RPG9, p.45) which focus on issues of economic and social sustainability to address problems of uneven regional development.

#### **(iv) Greater London**

The London Plan encourages compact sustainable development through high density clustering of economic activity (draft London Plan, p.7) and supports the need to maintain the role of the Central Activity Zone, in which the City of London is included, maximize plot ratios and support mixed-use development (op cit, Policy 2B.1, pp.75-76). Opportunity Areas to “intensify and accommodate substantial growth, especially in economic activity” (op cit, p.51) particularly in the Thames Gateway (op cit, pp.7-8 and p.59) are identified and ‘Areas for Intensification’ are proposed for identification by UDP boroughs (draft London Plan, Policy 2A.3, p.60), maximising plot ratios for mixed use development at key transport nodes (op cit, p.10, p.41).

Six ‘Opportunity Areas’ are identified in Central London. Planned major development to the east of London (op cit, p.8, p.59, p.82) is seen as of key importance in resolving the structural problems of the Thames Gateway identified at a Regional level (RPG9 Policy RE6, pp.42-43). Of significance for the City is the suggestion of “an expansion of some central London functions into the City fringe, Isle of Dogs (Canary Wharf) and Stratford” (see ‘London’s future spatial development’, op cit, p.51). The research suggests that it will be important that plans for major new growth in the East London sub-region, in which the City of London will be included, take full account of established complex functional business clustering relations.

The questionnaire and interview surveys demonstrate the key importance of close proximity and walking distance as benefits of clustering in the City for key international business functions, and the strong links between physical clustering synergies and specific sectoral interdependencies. Questions on choice of office location within London in the research indicate that depth of infrastructure and critical mass associated with dense co-location, a City address, accessibility for commuters, and staff preferences for working in the City are important factors militating against a move to a different London location.

Evidence from the interviews suggests that locations outside the City and central fringe compete on cost of office space and planning flexibility but that loss of centralised clustering synergies (including density of transport nodes) will preclude distant locations from the high value activities conducted by international financial and business service firms. The location of low-revenue back-office activity out of the cluster seems likely to continue but the consensus among respondents is that, in order to obtain cost savings and necessary skills, such re-location now needs to be outside London and the South East. At the same time, the presence of the cluster has fundamental benefits for less clustered sectors in central London, such as accountancy and consulting, which serve more spatially dispersed London client distributions, and for firms primarily serving corporate and private customers located in the West End. The interview survey suggests that there is more interest in locations to the west of the City than the east for this reason although transport connections and staff housing location preferences may also play a part in this.

The specificity of firms' office locational priorities according to sector and client base casts doubt on the ability of policy to plan successful new clusters, and this is supported by existing business clusters research. While the interview findings indicate that Canary Wharf is seen as having provided much-needed office space suited to contemporary business requirements that has until recently been restricted in supply within the City, its accessibility problems are regarded as an important locational drawback. It was felt that the planned expansion of office space in the City through new high-rise development (to cater for future business needs within the cluster) is one aspect of policy that the Corporation of London has right.

*The Mayor's Economic Development Strategy (EDS)* (London Development Agency (LDA), 2001) recognises the importance of taking an overview of the London economy through wide

consultation and detailed research in order to co-ordinate strategy for business and labour market geographies that cross local authority boundaries. The potential role of business clusters in the generation of supply chain opportunities (EDS, p.35), and the importance of regulatory framework (EDS, p.35) and transport infrastructure (EDS, p.37) are stressed and support the findings of this research.

While policy on regulation and transport have clearly been identified as critical to sustain the cluster, the issue of supply chain opportunities is also important since this addresses the important question in relation to sustainability - how to promote the benefits of clustering across space?. The interviews brought forth discussion of the range of connectivities associated with service suppliers, including outsourcing and back-office activity, for particular sectors and individual firms. Policy to encourage these interrelationships to tackle problems of uneven development will require a strong understanding of financial and business services operations within the cluster and co-ordinated action across local authority boundaries.

Transport is highlighted as a key issue within London and in the supply of London's labour force from the South East Region in London and regional policy statements. RPG9 recommends the development of plans that minimise the distance people have to travel within the South East (RPG9, Policy T1 (pp.56-57): the research suggests, however, that the wide geography of flows associated with the cluster – commuting and business travel, including the use of airports - must be allowed for in plans to encourage sustainable movement.

In line with transport issues identified by our research respondents, ten key priorities for *the Mayor's Transport Strategy (TS)* (Mayor of London, 2001) are specifically addressed in Policy 3.3 and para 3.39 of the Strategy (Ch 3 – Objectives and linkages). Reducing traffic congestion and investment on the Underground to increase capacity and increase reliability and frequency of services are listed first and second (TS, p.5). The related issues of increasing the capacity of transport infrastructure with respect to major new cross-London rail links and access to international airports and facilitating commuting through integration of National Rail and London transport systems are listed fifth and fourth (TS, p.5). However, perceived discord between key decision-makers in London and the Government on the London Underground and debates on routing options east and west of the city core for the

Crossrail 1 route were shown in the interviews to undermine business confidence in the ability of the public sector to resolve London's infrastructure problems.

In general, less significance is attached to commuting problems as an urgent threat to the City itself than to cross-London movement for business meetings. However, given the absolute importance for service firms of their labour supply, problems of phasing major new development with transport improvements could be seriously damaging to business particularly at Canary Wharf where there are fewer public transport nodes. A number of respondents commented on the importance of making public transport improvements urgently to support new office development in the City and at Canary Wharf. The research indicates the importance of improving journey time reliability by underground and taxi within central London. Congestion due to poor programming of road works and phasing of traffic lights was seen as a problem of poor public sector management. The introduction of a policy to restrict traffic movements in central London before Underground improvements are in place is widely criticised as unworkable and damaging to business.

#### **(v) The City**

Within the City, policy adopted in *the City of London Unitary Development Plan, (UDP)* on 9 April 2002, recognises key requirements identified in the research to promote the London financial and business services cluster:

Policy to provide appropriate office space in terms of capacity, flexibility, large floor-plate buildings, accommodation for local support services, amenities and telecommunications infrastructure (Ch 2 and 8), addresses the need for the Corporation to be able to respond to changing space requirements. The need for flexible space is shown in the interviews to be important to accommodate dynamically shifting business operational requirements associated with changing global market conditions. Policy for the extension of the cluster at the fringe is in line with the importance attached to the benefits of close proximity and walking distance within the cluster and the need for good access to transport links.

The protection and improvement of existing housing stock including accommodation for weekly business commuting and visitors (Ch 3 and 4) and provision of mixed uses – retail, recreation, art, cultural and entertainment facilities specified in the Plan (Ch 2, 5 and 6) - are



identified in the interviews as important to support work-life needs, informal relationships, knowledge and trust, and to encourage people to travel into the City.

Of key importance is UDP policy on the need for improved transport infrastructure, public transport capacity, taxi movements and local traffic management (Ch 9). The research findings suggest that reduction of the overall level of traffic within the City may be less important than the easing of movements in and out of the City as most journeys within the City are on foot. Problems in cross-central London movement were prioritised including travel to Heathrow. Use of licensed taxis and company vehicles as a major transport mode for cross-London business journeys is expected to continue until confidence in underground reliability is improved. Appropriate action to resolve these problems will require a co-ordinated response by a variety of agencies.

Spatial strategy for compact sustainable urban development in the South East and London is therefore supportive of business clustering within London. At the same time, implementation of policies for transport, office and housing development will need to be sensitive to specific flows and spatial relationships associated with financial and business services clustering that cross administrative and policy boundaries.

### **5.3 Conclusion - The Promotion of Financial and Business Services Clustering**

- The research findings shed light on the sectoral synergies associated with local proximity of financial and business services in the London cluster. Clustering continues to be important for key business functions in spite of the costs associated with demand for a limited supply of highly centralised space. The market drivers and interdependencies associated with the geography of clustering in London are complex, relating to inter-sectoral and client-servicing relationships. This suggests that public policy to promote the benefits of the financial and business services concentration will be better directed at facilitating the operation of established clusters rather than master planning new clusters.
- Movement of certain activities out of the cluster should not necessarily be seen as damaging to the cluster overall. The research suggests that locational centralising and decentralising movements of, for example, back-office activities, are part of an on-going evolutionary process that is important to the global competitiveness of international financial and business services. This demands positive planning for the flexible use of building stock but does not diminish the value and importance of the cluster for business. It seems likely that such movements are probably important to the long-term overall health and viability of the cluster. While Canary Wharf has provided much needed additional space for ‘City’ expansion, planned high-rise development and provision of flexible space, in relation to functional use, size and age/cost of office accommodation in the City are deemed to be important to meet future anticipated needs for dense clustering.
- The research suggests that successful clustering can be facilitated or eroded by public policy. Government administrative and organisational boundaries, lack of policy co-ordination and focused management relating to regulation and transport are perceived by the research respondents to be a barrier to effective decision-making and investment. Co-ordination across policy and departmental as well geographical boundaries will therefore be essential to support sustainable financial and business services clustering as indicated by the following summary of priorities for public policy revealed by the research.

## **Priorities for Policy-making Frameworks**

### **(i) International European Union Level**

The research findings emphasise the fact that business clustering in London is the product of interdependencies at a range of geographic scales and the comparative European studies on PURs suggest that this spatial concentration can have benefits for economic, social and environmental sustainability. This indicates that policy frameworks for the cluster should look beyond simplistic interpretations of financial and business services clustering as ‘less sustainable, mono-centric’ development.

European spatial policy guidance which encourages co-operative relationships between London and other key European global cities to spread the economic and social benefits of agglomeration in the region is in line with the research findings which indicate a need for increased cross-border policy co-ordination to promote the Single Market. The research findings also provide strong support for the ESDP priority to improve transport networks and increase flows between London as a gateway city and continental Europe.

### **(ii) National UK Level**

UK policy to encourage compact city development and maintain London’s role as a global financial centre are in line with the research findings on the economic, social and environmental benefits associated with business clustering. However, the findings indicate that policy integration across central and local government agencies is needed to sustain London’s role as an international financial and business services location.

The key policy priorities are transport and regulation. An important finding is the need to ensure that a range of policy developments do not combine to create barriers to international business operation in London through contradictory effects:

First, there is a need to maintain a business-friendly direct and indirect tax regime, inward flows of transnational skilled labour, employment flexibility, balanced and not too burdensome/complex regulation/legislation, investment in transport infrastructure and strong transport management. Second, a co-ordinated and active UK government role is needed in EU policy-making and harmonisation proposals for the financial services industry.

### **(iii) South East Regional Level**

Regional policy recognises the existence of interdependencies between London and ROSE in relation to London's regional labour market. However the research findings suggest that these will also need to be specifically taken into account in the local implementation of some aspects of regional policy:

First, in relation to housing development, policy supports the densification/compaction of development within London's boundaries by maintaining Green Belt restrictions and limiting growth within ROSE. Given the importance of commuting from ROSE to the cluster, the research suggests that urban capacity in areas popular with commuters should be monitored – patterns of housing availability will have an important effect on access to the City/Canary Wharf.

Second, in relation to transport, regional policy encourages development in proximity to transport nodes; given the concentration of network nodes in the City, this should benefit daily commuting. However, policy to minimise regional travel in general should be aware of existing commuting and business travel patterns which the research indicates can have an important effect on access to labour within the cluster and access to airports of London commuters living in ROSE. Detailed plans for sub-regional development and airports, particularly for the potential growth area London-Stansted-Cambridge/Thames Gateway, should similarly take account of existing functional relations and physical movement associated with City/Canary Wharf clustering.

Third, policy on regional human resource development should be aware of employment needs within the cluster (e.g. IT skills) and of opportunities to promote supply and servicing chains between emerging regional business clusters and the London cluster.

### **(iv) London Level**

Policy for continued concentration of high density office development in the City/CAZ supports continued compact development in the City which has been shown to be a key benefit to successful business operations and, in line with the research findings on future business space requirements, tall buildings are encouraged.

Of the locations identified as Opportunity Areas and Areas for Intensification for high density development, the research findings indicate that locations within walking distance of the City and close to commuter stations could provide valuable additional floorspace to the cluster fringe (London Bridge, Farringdon/Smithfield and Holborn, given the strong functional links between the City and West End based cluster zones). Proposed development around the City will need to take into account ease of movement around the cluster and the strength and fundamental importance of business functions, labour market and commuting geography as office locational determinants.

Plans for major new development in more distant London locations, particularly in the East London sub-region, are most likely to succeed by facilitating business inter-sectoral relationships, labour market and transport requirements. The research findings provide strong evidence of the important benefits of keeping the cluster as compact as possible and the need to promote accessibility in relation to time and ease of travel. This will require co-ordinated planning across existing UDP boundaries.

The proper phasing of major new office development in relation to public transport improvements is indicated to be crucial given the inadequacy of existing infrastructure to support current levels of economic activity. The likely continuing need for efficient commuting from ROSE will have implications for cross-London public transport capacity. Planned improvement of east-west public transport links (including Crossrail) are in line with needs identified in the research to promote the functioning of the labour market by allowing people to travel more easily across London. Routing decisions in relation to existing financial and business services clustering (City/Canary Wharf) could have a major impact on business competitiveness.

Business perceptions of a lack of co-ordinated strategy and management for public transport improvements are damaging business confidence. The research findings on congestion suggest that traffic management policy for central London to facilitate business meetings across central London, particularly by taxi, and to ensure that clients are willing to travel to the cluster, is a priority. Travel to and from airports, particularly for international clients, is also an issue.

Detailed policy on housing location and design within London should take account of different housing needs and preferences (across occupation, income group, household size and age structure) associated with financial and business services and other services that support this economic activity.

The research findings suggest that the continued location of government, regulatory, trade and professional institutions in close proximity to the cluster should be encouraged. Maintaining high quality London housing environments, schools, entertainment and cultural assets is likely to be important in retaining London's desirability as an international business hub.

#### **(v) Local Level - City of London**

Planned development of office space and telecommunications infrastructure in the City is in accordance with business needs identified in the research. The findings indicate the importance of maintaining the geographically compact and multifunctional form of the cluster and the benefits of the City's hub and spoke role.

Policy for the extension of the City cluster at fringe locations within walking distance supports the identified benefits of co-location and close proximity for financial and business services – walking distance is highly valued. The research suggests that particular weight needs to be placed on the needs of banks, and to a lesser extent law and fund management and insurance activities, which have a key role in the cluster. Links between banks and local authorities can be beneficial to the cluster and ways of reinforcing these could be considered.

Flexibility of space through retention, and planning controls relating to alteration, of older/cheaper office space is also identified as important for new business start-ups and smaller specialist firms. Findings on access to venture capital and start-up premises indicate that support for small firms in the City should be carefully monitored.

The research indicates that increased densities associated with new office development will require early improvements to public transport capacity and reliability which are already considered damaging to business competitiveness. Policy for City traffic management to reduce through-traffic and ease taxi movements addresses the need to facilitate business-

related travel but this cannot be effective without central London improvements beyond the City, particularly on east-west routes.

Policy to promote mixed use development in the City – retail, housing and recreation facilities – is in accordance with work/quality of life issues and the desirability of promoting a sense of community identified in the research. Development of visitor, art, cultural, hotel and conference facilities, and the retention of trade and professional bodies is likely to be important in attracting people into the City. While security, crime and environmental quality are not current threats to the cluster, the need for continuing attention to these issues is indicated.

Transportation and regulatory issues, identified as the key threats to the future of the business cluster, reflect the City's role as a hub and the importance of maintaining an attractive and fluid labour market. While the cluster is locally situated within a small part of the city, its sustainability will therefore require cross-administrative boundary action that is sensitive to the geography of contemporary business including functional relations between the City and Canary Wharf.

# Appendix

## Bibliography

### i) Literature Review

The first task was to identify the sample of works that would be reviewed. The sample had to satisfy five criteria:

- The major academic disciplines (economics, geography and sociology) should be represented;
- Each work should make a unique contribution;
- Works that relate best to the industries and concerns of the City, Canary Wharf and the fringe should be emphasised;
- Works on innovation and competition that relate to clustering should be included;
- The total number of works should be approximately 50.

The sample was arrived at by appealing to a mixture of objective indicators and the subjective judgement of the research team. We started by considering the works included in the comprehensive, multidisciplinary bibliography on clusters and competition provided in Porter (1998, pp. 272-287). Next, members of the team were asked to nominate works that they thought should be included because they satisfied one or more of the five criteria but were not present in the Porter bibliography. Judgement on the final 50 was enhanced by checking the citations database *Web of Science* to ascertain the number of times a work had been cited. Having decided the sample, we designed a standard format for each of the préces. This format consisted of seven headings: *Bibliographic Details; Predominantly Theoretical or Empirical; Major Discipline; Methodological Details; Principal Conclusions; Weaknesses; and Observations*. The analysis of these préces is presented in the main body of the report. The sample is detailed below.



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## Data Analysis and Mapping Exercise

Maps showing the spatial distributions of firms in a central zone of London for different sectors were produced as follows. These are the upper maps in the map series below. Data on companies have been supplied by *Market Locations* from Companies House registers. Each Company record included a SIC coding and an address. The data from which the maps were derived was selected on the basis of 14 composite groups as shown below. The numbers in brackets are the SIC codes:

**BANKS:** Banks (65121), Building Societies (65122), Financial leasing (6521), Other credit (6522), Credit granting (65229), Factoring (65222), Mortgage finance (65223), Other credit granting (65229), Investment trusts (65321), Units trusts (65232), Security dealing (65233), Venture capital (65235).

**INSURANCE:** Life insurance (6601), Pension funding (6602), Non-life insurance (6603).

**AUXILIARY FINANCE:** Administration of financial markets ((6711), Fund management (67121), Security broking (67122), Auxiliary/intermediation (6713), Auxiliary/insurance and pension funding (6720).

**REAL ESTATE:** Development (7011), Letting conference centres (70201), Other letting (70209), Agencies (7031).

**IT:** Hardware consultancy (7210), Software consultancy (7220), Data processing (7230), Data bases (7240), Maintenance (7250).

**LAW:** Legal (74119).

**ACCOUNTANCY:** Accounting/auditing (74121), Tax consultancy (74123).

**MANAGEMENT CONSULTANCY:** Business consultancy (7414), Public relations (74141), Financial management (74142), General management consultancy (74143), Other management consultancy (74149).

**ARCHITECTURE/ENGINEERING:** Technical (7420), Architecture (74201), Urban planning (74202), Quantity surveying (74203), Engineering design consultancy (74204), Engineering industrial design (74205), Engineering technical consultancy (74206), Testing and analysis (7430).

**ADVERTISING:** Advertising (7440), Advertising space/time (74401), Creation and placement (74402), Other advertising (74409).

**RECRUITMENT:** Labour recruitment (7450)

**BUSINESS SUPPORT:** Cleaning (74701), Photographic (74819), Secretarial and translations (7483), Speciality design (74842), Exhibition organisers (74843), Conference organizers (74844), Other business (74849).

**CHARITIES:** Charitable social work (85321).

**ORGANISATIONS:** Business and employer organizations (9111), Professional organizations (9112), Trade unions (9120), religious organizations (9131), Other (9133).

Using the lookup function on the database package “Filemaker” the addresses were matched with OS Grid references from the OS Address point file. 1Km tiles of the address point file were selected to include the majority of financial service offices. The boundary of the tiles used is shown as the outer polygon on the map. Within this area it was possible to successfully locate 23,500 offices, of which 17,836 were within the categories included above.

Maps showing the spatial distribution of ‘clustered firms’ were produced from the simple distribution maps as follows. These maps are shown as the lower map in the map series below. A clustered firm is defined as one whose average distance to its 10 nearest neighbours (in its sector) is less than 100 metres. Excluding all non-cluster firms from the original distribution maps provides a clear picture of where clusters are to be found. Software was written to calculate a measure for each office, which was then used to select the smaller set of clustered offices for the maps below. These figures exclude offices that are dispersed over a large area and can be assumed to be largely concerned with retail financial services. The proportion of each category that was included within the cluster is shown Table A.1.

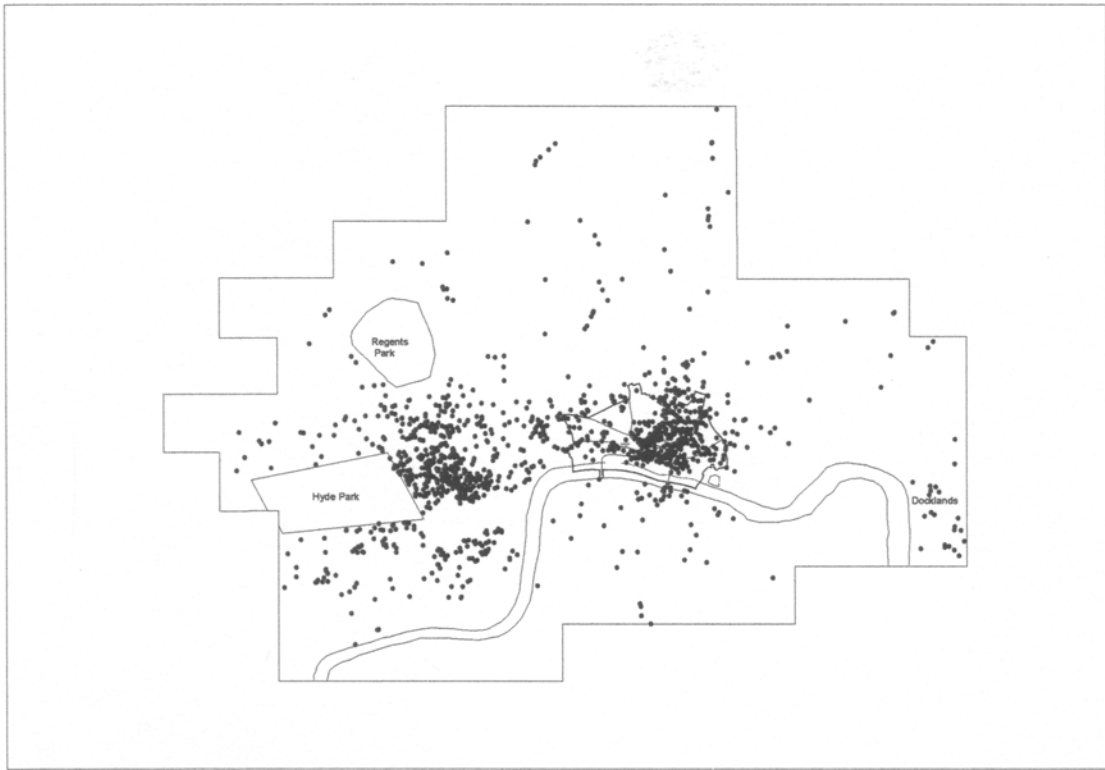
**Table A.1: Clustered Firms by sectors**

Category	Total offices	Number 'clustered'	Percentage clustered
Insurance	406	233	57.4
Recruitment	1731	967	55.9
Banks	1629	903	55.4
Business support	3332	1779	53.4
Law	1403	621	44.3
Real Estate	1956	778	39.8
Advertising	1140	450	39.5
Management Consultancy	1442	514	35.6
Architecture/ Engineering	1676	589	35.1
Auxiliary Finance	638	171	26.8
Accountancy	1005	236	23.5
Information Technology	1069	211	19.7

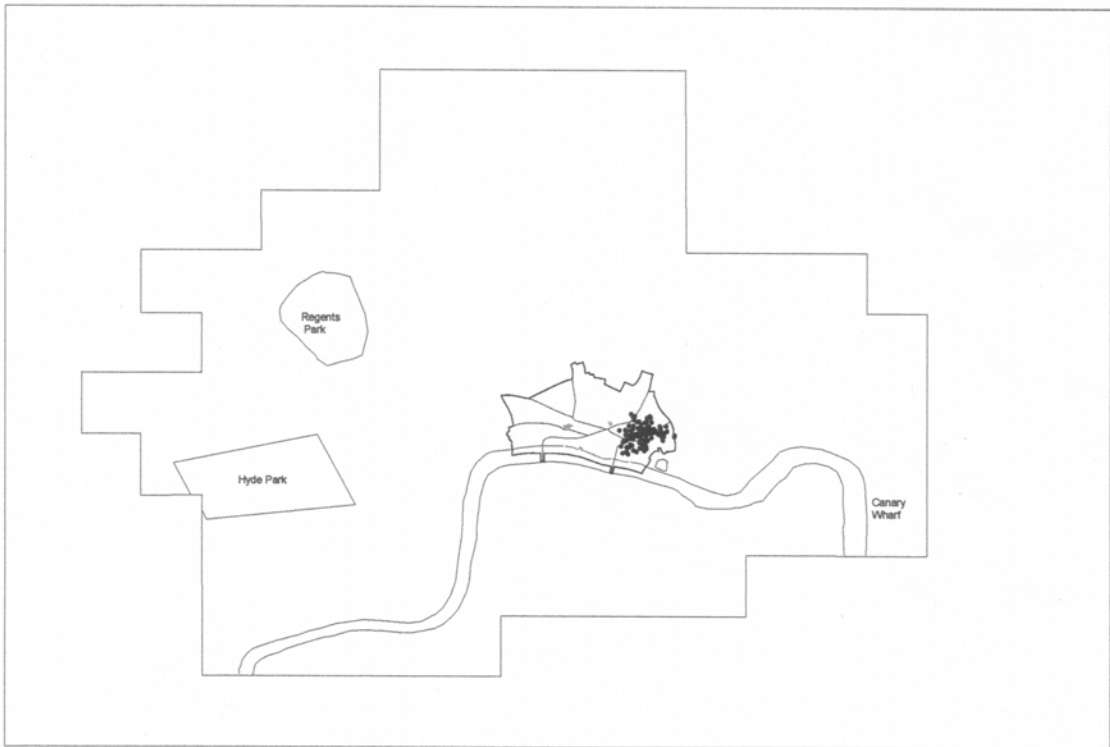
It is clear that there is a general relationship between the total number of offices and the ratio of those in the cluster to the total. By regressing %clustered against number of firms by sectors, residuals have been computed that indicate how over or under-clustered as sector is. These figures are given in brackets with the map titles. For instance, Insurance, Banks and Recruitment show a strong propensity to be in clusters, while Information Technology and Business Support are characteristically more dispersed.

The aggregate Cluster Zones map was constructed manually by identification of areas in which there is a continuous patch of clustered firms (see Figure 1 in chapter 3 above). There follows a series of maps presented in pairs. There is one pair for each sector. The top map shows the distribution of all firms in a sector, the bottom map the distribution of clustered firms in that sector.

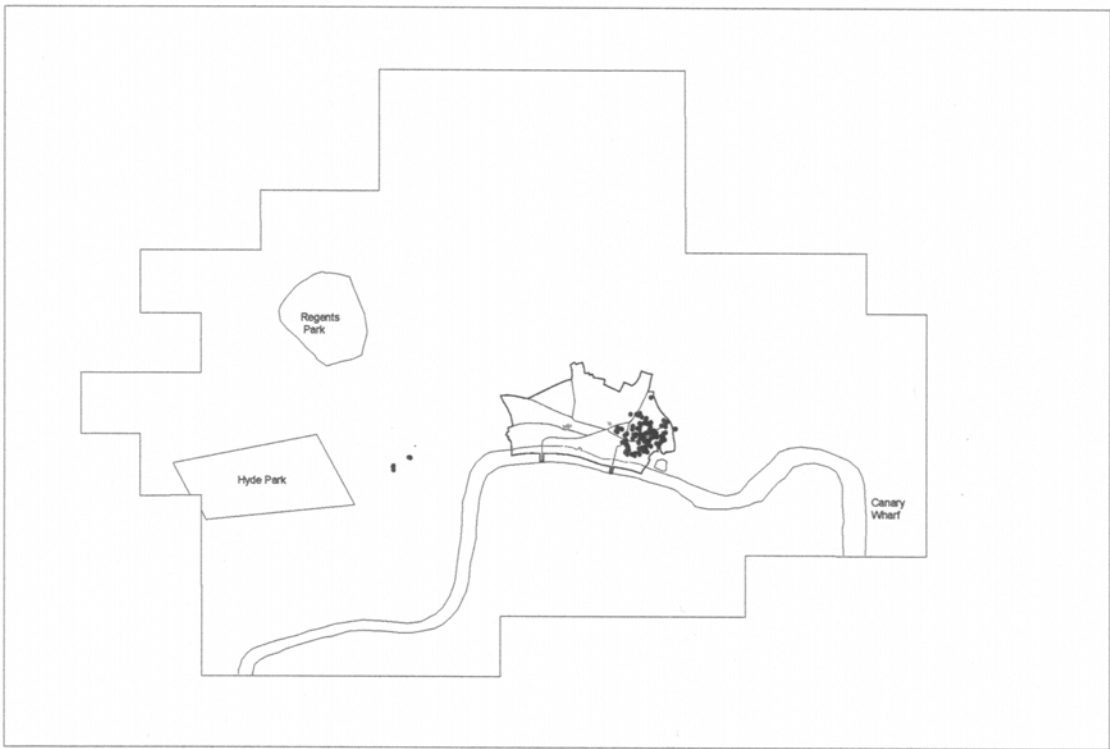
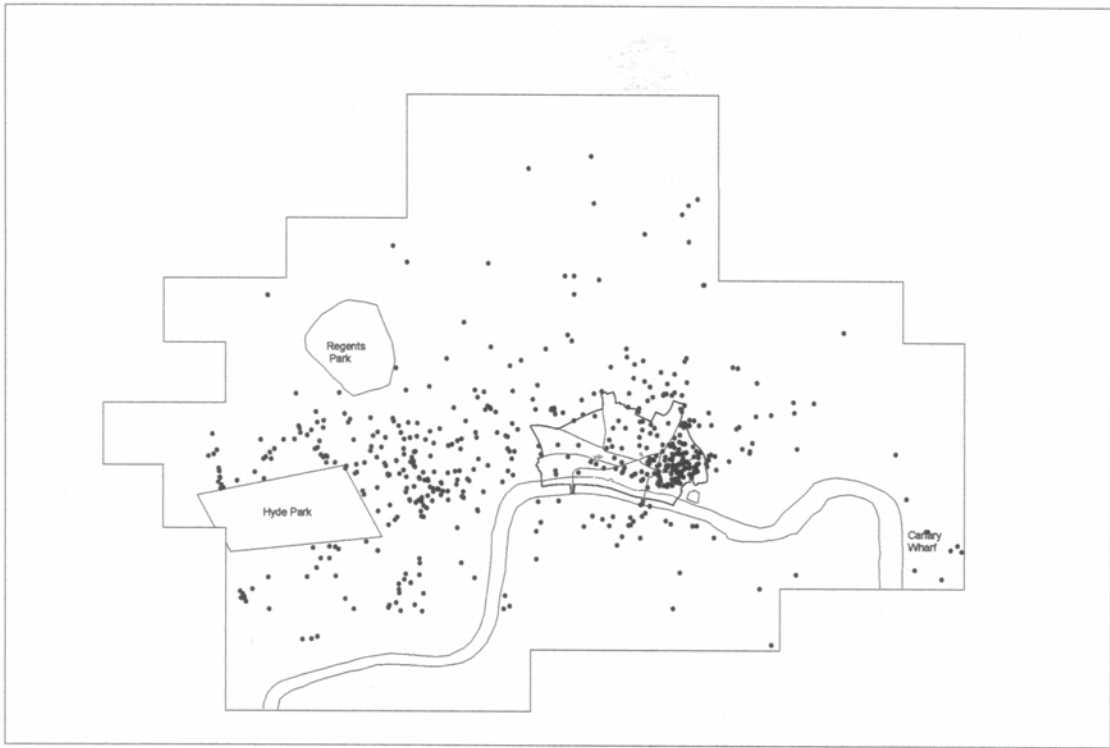




Banks (0.55)



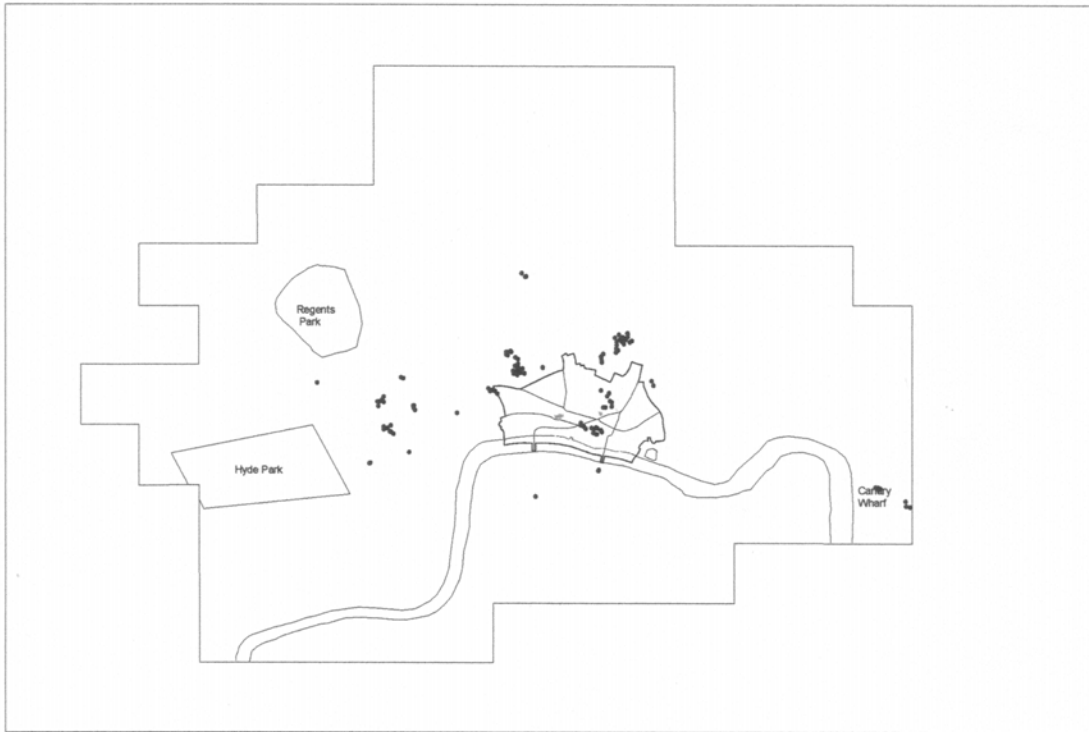
Insurance (0.57)



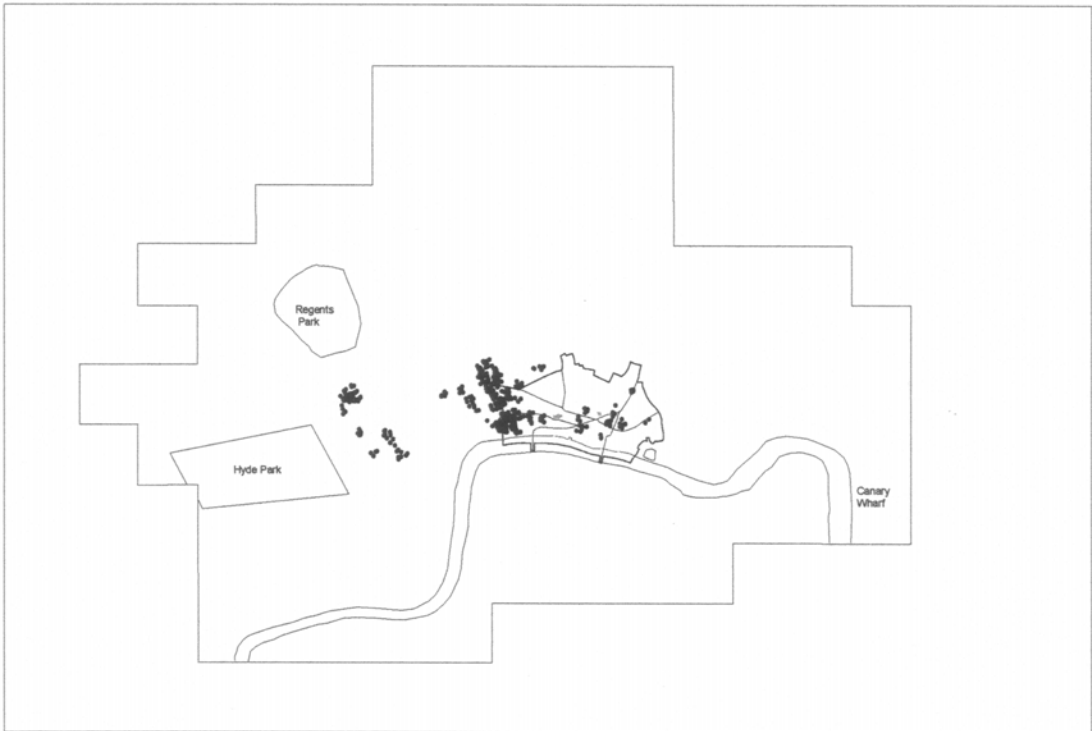
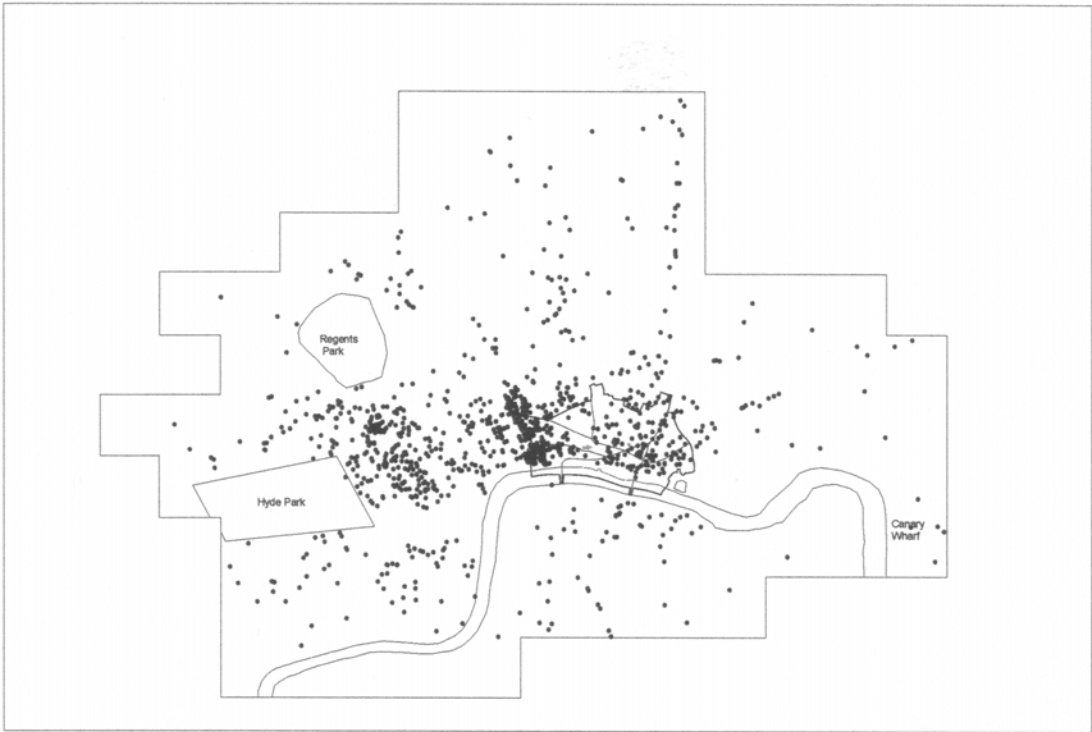
Auxiliary Finance (0.27)



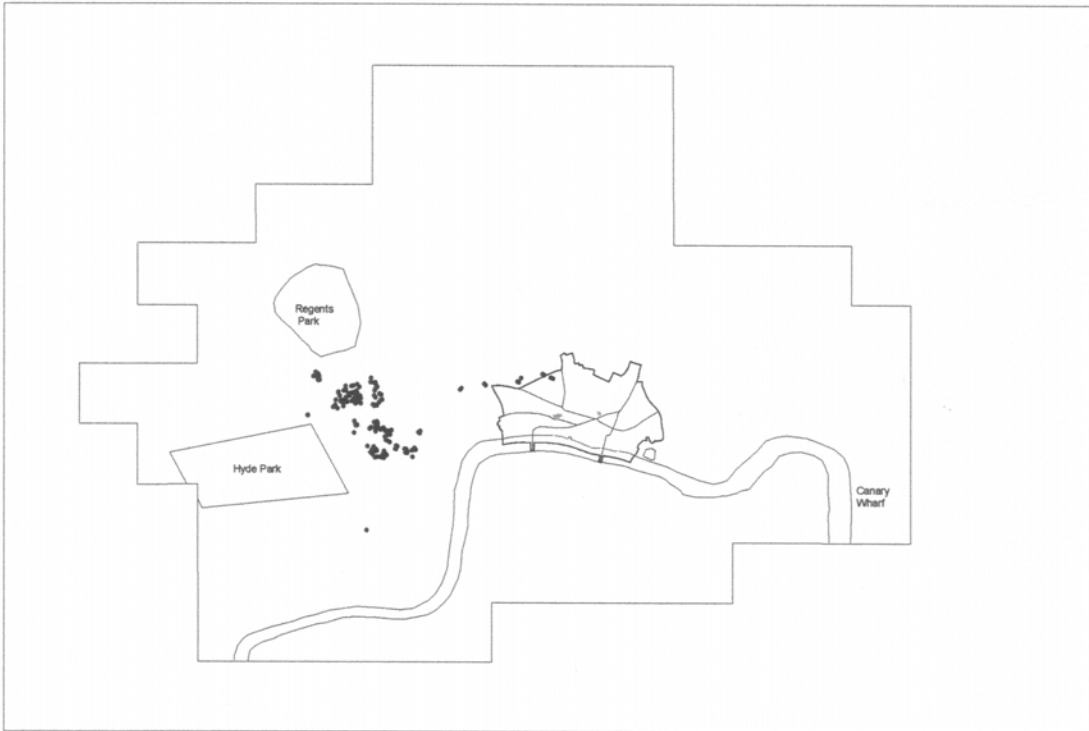
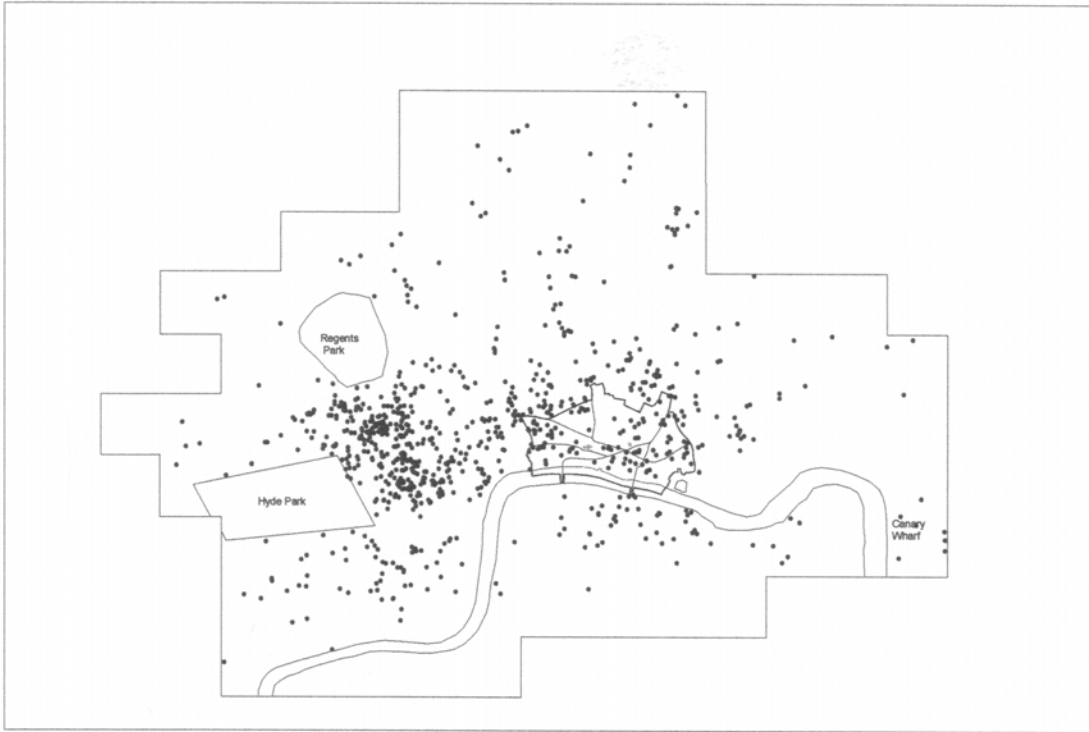
Real Estate (0.40)



Information Technology (0.20)



Law (0.44)

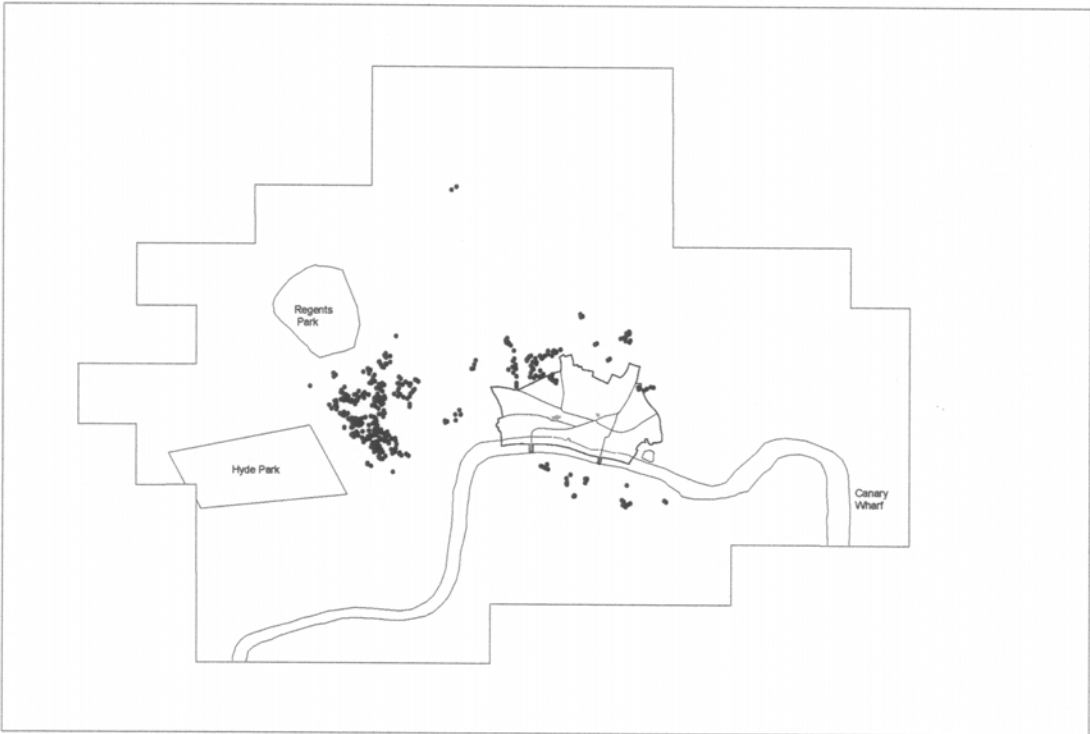


Accountancy (0.23)

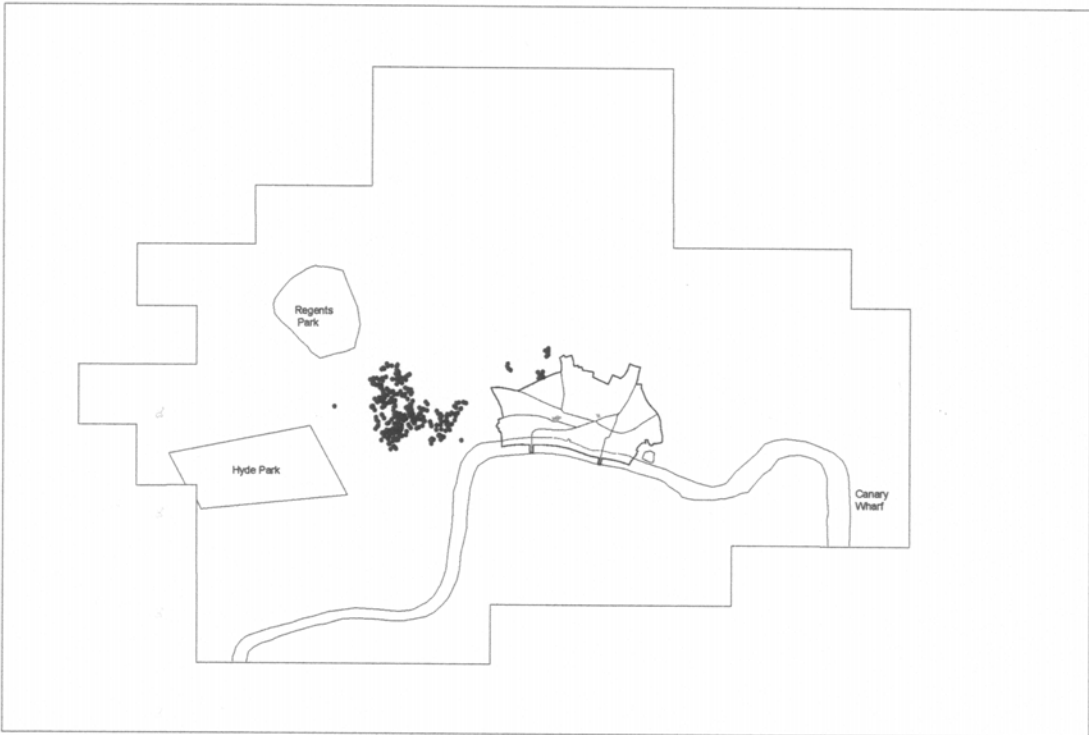


Management Consultancy (0.36)

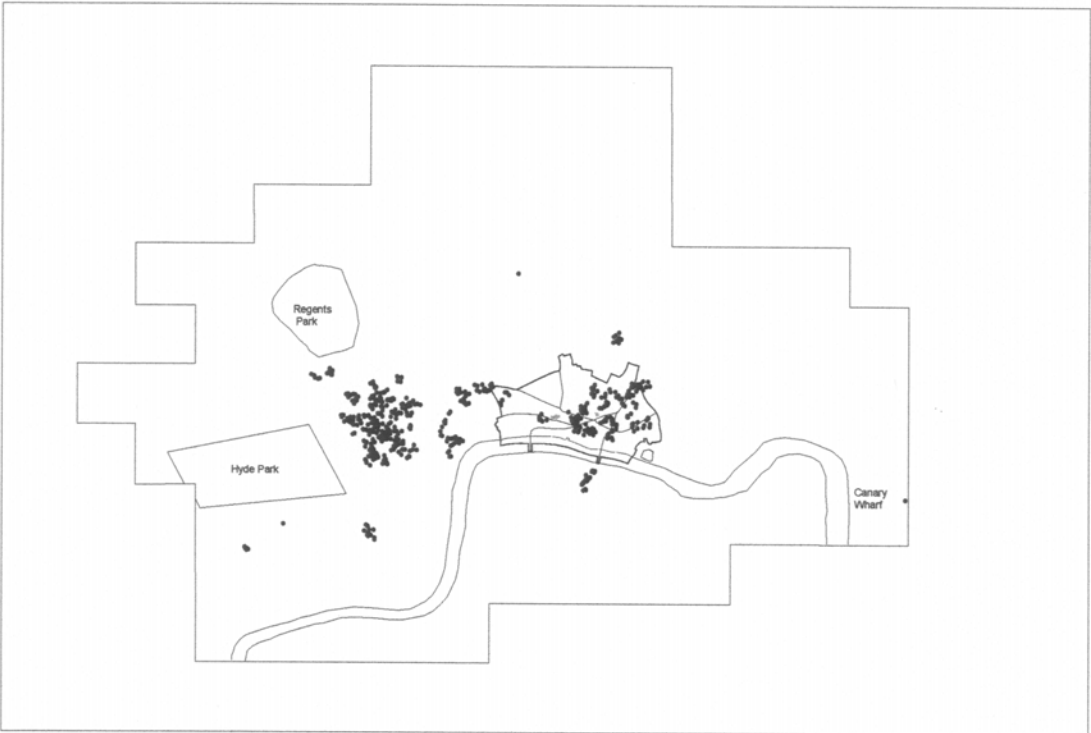




Architecture/Engineering (0.35)



Advertising (0.39)



Recruitment (0.56)



Business Support (0.53)

# Postal Survey

## ADVANTAGES AND DISADVANTAGES OF A LONDON LOCATION

1. How would you describe your company's *major business activity*? (Please rank up to three activities by entering a number in the relevant box, where 1 indicates the most important.)

<input type="text" value="48"/>	Banking	<input type="text" value="60"/>	Insurance	<input type="text" value="0"/>	Maritime services	<input type="text" value="30"/>	Management consultancy
<input type="text" value="16"/>	Accounting	<input type="text" value="61"/>	Legal services	<input type="text" value="0"/>	Advertising	<input type="text" value="17"/>	Fund/Asset Management
<input type="text" value="2"/>	Recruitment	<input type="text" value="1"/>	Publishing	<input type="text" value="8"/>	Market research	<input type="text" value="6"/>	Property management
<input type="text" value="1"/>	Printing	<input type="text" value="21"/>	Investment banking	<input type="text" value="2"/>	Other IT related	<input type="text" value="5"/>	Provision of electronic information
<input type="text" value="0"/>	Telecomms	<input type="text"/>	Other (please specify):				

2. How important are each of the following benefits of your location? (Please tick one box per benefit.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.

	1	2	3	4	5	0	Tot
Your address is important to being perceived as credible	18	23	63	111	91	2	1152
You benefit from a strong, skilled labour supply	21	22	62	95	85	22	1056
You benefit from being close to market-leading customers	18	46	66	88	77	12	1045
Your customers external to London find it easier to locate you	32	42	72	98	46	15	954
You benefit from being near professional bodies	36	59	79	68	52	11	923
Knowledge transfer from the City's "financial atmosphere"	28	45	75	72	57	28	916
You benefit from being near leading competitors	49	58	63	73	41	23	851
Customers external to London find it easier to interact with you	45	58	87	62	35	19	845
Ability to find firms who will supply bespoke services	34	75	83	56	36	22	837
It is the best place to be to take market share from rivals	37	60	74	65	39	32	834
Proximity to a relevant exchange or physical marketplace	55	36	70	44	57	45	798
Ability to benchmark against competitors	67	68	72	43	23	33	706
Local rivalry amongst competitors is a powerful spur	63	70	69	44	18	42	676
Ability to access real time information on market trends	80	65	49	44	27	41	668
Support from local government	119	66	33	13	11	64	457
Access to venture capital	113	46	31	13	11	90	405

**3. To what extent is London's economic growth impeded by the following?** (Please tick one box per factor). Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.

	1	2	3	4	5	0	Tot
Cost of business premises	8	19	64	110	103	5	1193
State of the underground	14	29	59	84	114	8	1155
National transport links	23	34	67	85	89	10	1077
Government regulation	29	41	66	68	80	22	981
International transport links	39	48	79	55	65	20	917
Local infrastructure (including buildings)	26	63	92	69	39	14	899
Environmental quality and pollution	43	72	99	48	20	26	776
The UK's current position outside the Euro zone	82	76	57	29	26	37	651
Availability of staff with language skills	73	68	69	41	12	44	640
Access to venture capital	101	52	50	15	8	80	455
Other (please specify):	0	0	1	2	13	3	

**4. What is the nature of competition in your line of business in London?** (Please rank in terms of importance).

	1	2	3	4	5	0	Tot
Competition on cost/price	44	57	59	59	55	31	798
Competition based on service differentiation	52	43	46	72	63	28	777
Competition based on innovation	38	53	68	61	41	43	769
Competition based on ability to serve customers across borders	41	57	52	57	53	46	756
Competition based on product differentiation	36	55	70	49	35	60	743

**About Innovation**

**5. How much does your location contribute to your ability to innovate in each of the following ways? Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.**

	1	2	3	4	5	0	Tot
Developing new markets	40	44	69	81	42	20	869
Developing better ways of delivering your service/product	46	51	90	59	30	29	804
Developing new services	52	57	70	68	21	36	753
Re-orienting you company strategically in the face of change	57	59	77	46	24	37	710
Improving internal organisational structure	64	72	74	40	14	49	660
Developing new products	57	55	58	53	18	64	643

**6. How important are the following types of local firms/institutions in helping your firm achieve innovative solutions? (Please tick one response per firm/institution type.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.**

	1	2	3	4	5	0	Tot
A pool of talented labour with relevant skills	19	31	42	79	111	22	1078
Customers	21	38	60	69	102	16	1063
Firms who help you supply your service/product	28	44	80	71	58	26	930
Other firms in the same line of activity	38	64	96	67	18	20	812
Industry associations	65	72	77	44	18	29	706
Academic institutions	98	85	55	24	10	33	579
Local government	139	63	28	16	7	51	448

**About Links with Local Firms and Institutions**

**7. What proportion of your work comes through contacts with other firms in London?**

86	0-20%	61	21-40%	66	41-60%	60	61-80%	27	81-100%
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**8. Which types of firms do you have the most important inter-relationships with? (Please rank up to a maximum of 3 with 1 indicating most important.)**

56	Banking	52	Insurance	5	Maritime services	3	Management consultancy
4	Accounting	39	Legal services	2	Advertising	19	Fund/Asset Management
2	Recruitment	1	Publishing	1	Market research	3	Property management
1	Printing	27	Investment banking	5	Other IT related	2	Provision of electronic information
3	Telecomms		Other (please specify):	_____			

**9. How important are each of the following reasons for having a location in close proximity to other firms in London?** (Please tick one box per reason.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.

	1	2	3	4	5	0	Tot
It is easier to build and maintain personal contacts	12	15	46	123	101	7	1177
The ability to have face-to-face contact	14	15	37	108	117	12	1172
It is easier to build relationships of trust	17	33	71	98	73	13	1053
It is easier to communicate because we have a common understanding of the business	27	33	67	108	51	17	981
We generally have complementary expertise with such firms	24	47	101	80	34	19	911
Multi-disciplinary teams can be assembled more quickly	30	46	73	86	41	27	890

**10. To what extent has your firm benefited from the following types of interaction with personnel in other companies?** (Please tick one box per factor.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.

	1	2	3	4	5	0	Tot
Contact by telephone for information e.g. about a legal matter, a technical question etc.	16	24	74	116	67	7	1085
Contact by telephone/e-mail for short-term problem solving	19	26	76	104	73	7	1080
Mixing with industry colleagues in social settings	22	36	78	95	66	9	1038
Mixing at local business meetings/events	17	38	74	103	62	11	1037
Chance meetings where you hear interesting information	28	52	76	89	56	5	996

**11. Where does informal interaction take place?** (Please rank up to three with 1 indicating the most important.)

102	Within the firm	107	Wine bars/pubs	77	Professional bodies	98	Restaurants	79	By e-mail
11	Sports clubs/events	7	Other clubs	150	Seminars/conferences	18	In the street	114	By telephone



*Characteristics of the London Labour Market*

**12. Approximately what proportion of your staff do you recruit from within each of the following areas?**

*(Please tick one box per area.)*

	0-20%	21-40%	41-60%	61-80%	81-100%
South East	27	26	46	59	152
UK (outside South East)	109	25	15	9	3
European Union (outside UK)	132	17	6	2	2
North America	130	2	4	0	1
Global (outside Europe)	132	2	3	2	3
Global (but for specific nationals to serve specific national	117	4	1	1	2

**13. How important are informal channels (e.g. personal relationships, local information through club membership, professional bodies, informal use of head-hunters etc.) for the recruitment of your skilled staff? (Please tick one box per staff category.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable**

	1	2	3	4	5	0	Tot
Senior management	29	31	43	82	73	42	913
Client-facing staff	30	41	72	63	53	41	845
Specialist staff (e.g. IT staff)	31	52	75	58	32	50	752
Senior technical staff (e.g. in-house lawyers, economists)	32	32	70	66	33	62	735
Back office staff	49	77	72	27	31	44	682
Graduate trainees	73	58	38	30	33	68	588

**14. To what extent does labour flexibility within London lead to the following results? (Please tick one box per benefit.) Rate in terms of importance on a scale from 1 to 5, where 1=not important and 5=very important; 0=not applicable.**

	1	2	3	4	5	0	Tot
A fluid labour market helps attract good staff	15	31	90	96	50	22	981
It is generally easy to recruit good people at short notice	15	36	94	98	41	21	966
It helps spread a network of contacts	19	35	88	94	47	22	964
It helps to spread knowledge of good practice	18	33	107	92	34	21	943
We can quickly tailor our staffing levels to our needs	17	50	103	77	32	26	894

**Please state any negative aspects you perceive of the flexibility of the London labour market**