

How much does the City of London cost the UK?

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The [Guardian](#) features Nick Shaxson's new book [The Finance Curse](#) as its Long Read this morning. In that article [new research](#), including by my co-author Prof Andrew Baker of Sheffield Political Economy Research Institute, is featured. This suggests that the City of London has imposed an enormous financial cost on the UK over the last twenty years. As [Nick says](#):

Of course, the City proudly trumpets its contribution to Britain's economy: 360,000 banking jobs, £31bn in direct tax revenues last year and a £60bn financial services trade surplus to boot. Official data in 2017 showed that the average Londoner paid £3,070 more in tax than they received in public spending, while in the country's poorer hinterlands, it was the other way around. In fact, if London was a nation state, explained Chris Giles in the Financial Times, it would have a budget surplus of 7% of gross domestic product, better than Norway. "London is the UK's cash cow," he said. "Endanger its economy and it damages UK public finances."

To argue that the City hurts Britain's economy might seem crazy. But research increasingly shows that all the money swirling around our oversized financial sector may actually be making us collectively poorer.

A [growing body](#) of economic research confirms that once a financial sector grows above an optimal size and beyond its useful roles, it begins to harm the country that hosts it. The most obvious source of damage comes in the form of financial crises — including the one we are still recovering from a decade after the fact. But the problem is in fact older, and bigger. Long ago, our oversized financial sector began turning away from supporting the creation of wealth, and towards extracting it from other parts of the economy. To achieve this, it shapes laws, rules, thinktanks and even our culture so that they support it. The outcomes include lower economic growth, steeper inequality, distorted markets, spreading crime, deeper corruption, the hollowing-out of alternative economic sectors and more.

Newly published research makes a first attempt to assess the scale of the damage to Britain. According to a new paper by Andrew Baker of the University of Sheffield, Gerald

Epstein of the University of Massachusetts Amherst and Juan Montecino of Columbia University, an oversized City of London has inflicted a cumulative £4.5tn hit on the British economy from 1995-2015. That is worth around two-and-a-half years' economic output, or £170,000 per British household. The City's claims of jobs and tax benefits are washed away by much, much bigger harms.

This estimate is the sum of two figures. First, £1.8tn in lost economic output caused by the global financial crisis since 2007 (a figure quite compatible with [a range suggested by the Bank of England's Andrew Haldane a few years ago](#)). And second, £2.7tn in "misallocation costs" — what happens when a powerful finance sector is diverted away from useful roles (such as converting our savings into business investment) toward activities that distort the rest of the economy and siphon wealth from it. The calculation of these costs is based on established international research showing that a typical finance sector tends to reach its optimal size when credit to the private sector is equivalent to 90-100% of gross domestic product, then starts to curb growth as finance grows. Britain passed its optimal point long ago, [averaging around 160%](#) on the relevant measure of credit to GDP from 1995-2016.

This £2.7tn is added to the £1.8tn, checking carefully for overlap or double-counting, to make £4.5tn. This is a first rough approximation for how much additional GDP Britons might have enjoyed if the City had been smaller, and serving its traditional useful roles. (A third, £700bn category of "excess profits" and "excess remuneration" accruing to financial players has been excluded, to be conservative.)

Let's put that in context: that's 2.5 years of GDP at current prices. It's over £3,000 per head per annum. But even ignoring the cost of the Global Financial Crisis, it's £4,500 a household a year at current prices. And that's because we let finance get out of hand, sucking the lifeblood out of everything else that we do.

The question to ask is obvious. Can we really afford to let this carry on?