National Institute
Monthly Wage Tracker

Underlying wage growth accelerates to 3.8% because of labour shortages in some sectors

Figure 1 – Average weekly earnings (incl. bonuses)

- - - - - AWE (incl. bonuses) Public   - - - - - AWE (incl. bonuses) Private
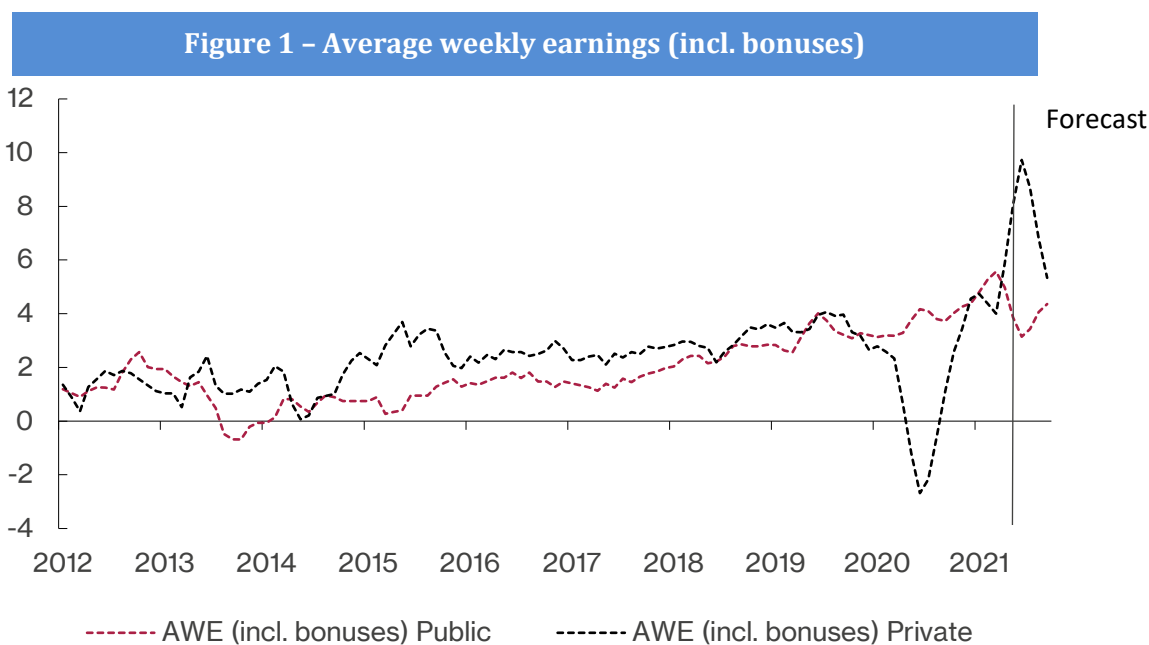
Main points

- A strong growth of labour demand and limited candidate availability is creating temporary labour shortages in some sectors like health and social services.
- Vacancies reached a record 862,000.
- Average weekly earnings are predicted to accelerate 8.5 per cent in the second quarter of 2021, easing to 5.4 per cent in the third quarter, because of compositional and base effects.
- Underlying wage growth which excludes base and compositional effects increased to 3.8 per cent in the three months to May.

"Reports of labour shortages in some sectors are starting to feed into wage inflation. But when the furlough scheme ends, labour availability will increase and this should limit the rise in wages. The post-pandemic jobs may be quite different from the pre-pandemic jobs and some employees may have to update their skills to match the new opportunities."

Cyrille Lenoël
**Principal Economist, NIESR**

Employment

The latest data for April from the Labour Force Survey show that **the labour market is continuing to recover from the pandemic, with employment, vacancies and wages all increasing.** The recovery, driven by improved confidence and the reopening of sectors of the economy, is broad-based across age groups, industries and regions.

The UK employment rate increased to 74.8 in the three months to May, 0.1 percentage points higher than the previous quarter, but still 1.8 percentage points lower than before the pandemic (December 2019 to February 2020). **The ONS has revised its employment rate series to show a larger than previously thought fall compared to pre-pandemic (1.8 percentage points compared to 1.4).** This means that the fall in labour participation during the pandemic is now 0.4 percentage points larger than previously thought. Before the latest pick-up, the employment rate had steadily declined from 76.5 per cent in the three months to February 2020 to 74.6 per cent in the three months to January 2021. Early estimates from HMRC suggest that **payrolled employment accelerated in June**, increasing by 356 thousand compared to 197 thousand in May.

The number of unemployed people declined moderately by 68,000 in the three months to May compared to the previous three-month period, bringing total unemployment to 1.6 million and the unemployment rate to 4.8 per cent. Thanks to supportive labour market policies – in particular the furlough scheme - the unemployment rate has only moderately increased during the pandemic, from 4.0 per cent at its onset to a peak of 5.2 per cent in the fourth quarter of 2020, declining since then.

The number of workers on furlough is fast decreasing. It is estimated to have decreased from 5.1 million in January to 2.5 million at the end of May thanks to the partial lifting of restrictions. As explained in NIESR's UK Economic Outlook, we forecast the number of furloughed workers to decrease to 1.4 million in the third quarter, dropping to zero in the fourth quarter (Figure 2)**.** But the pace of the recovery will depend on the follow through from increased transmission due to the reopening, countered by the efficacy of the vaccination programme as the roll out continues at pace. **The risk is that some restrictions may be reimposed after 19 July ("Freedom day") if the current wave of infections puts too much stress on the NHS.** An example is Israel, where wearing of face masks indoors was reimposed after a new wave of infections hit the country, despite a very high vaccination rate in the population.

Figure 2: Furloughed employment
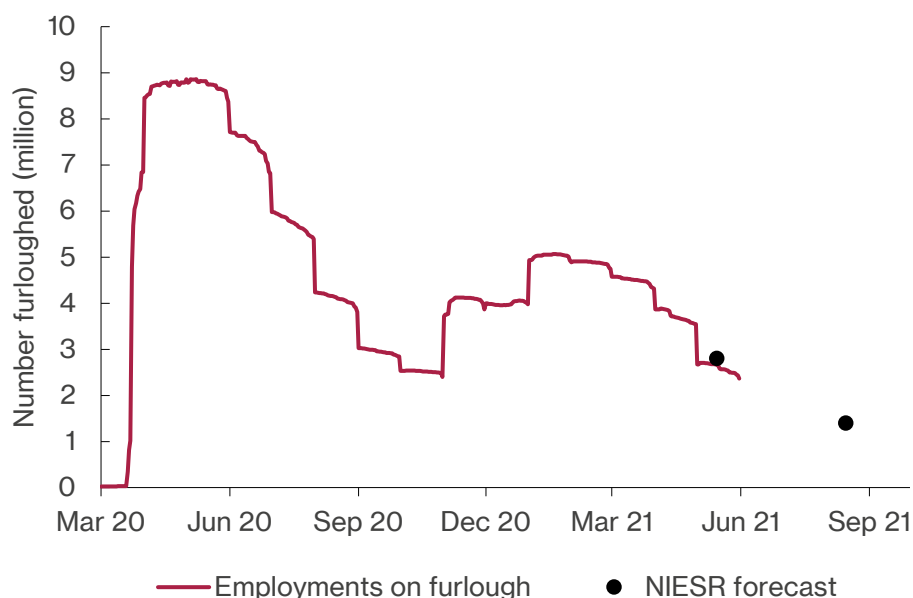
Source: HMRC, NIESR forecast

A record level of vacancies illustrates labour shortages reported in several sectors. The return of business confidence following the lifting of restrictions led to a sharp increase in vacancies reaching 862,000 in the three months to June, 39 per cent more than the previous quarter, and the highest level since at least 2001. Vacancies increased in all industries except public administration, with the largest increase in arts, entertainment and recreation.

The rise in vacancies suggests that the return of workers from furlough has not been enough to accommodate the recovery in labour demand. **The stock of 2½ million workers still on furlough suggests that there is room for employers to respond to further increases in business activity by taking back workers that were on furlough, but there may still be a mismatch between the sectors that are hiring and the skills of the people in furlough.**

Figure 3 compares vacancies and furlough by sectors. Two sectors stand out. On the one hand, the Health and Social Work sector shows a clear shortage with nearly twice as many vacancies as people still on furlough. On the other hand, the accommodation and food services seems to have excess labour with nearly 6 times as many furloughed workers as vacancies. There may also be a spatial mismatch between where the jobs are and where the workers live. The trends in the housing market with house prices increasing more outside London than in London means that there is a potential mismatch between where the workers have moved to and where the vacancies are.

Figure 3: The (mis)match between vacancies and furlough by sectors
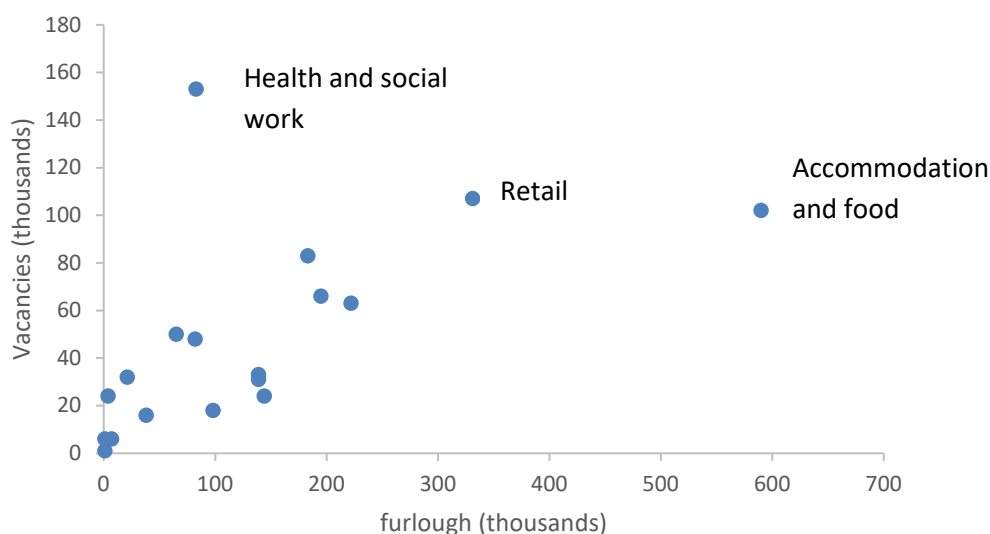
Note: Vacancies from ONS and furlough from HMRC. Vacancies are for June, and furlough for end of May.

Pay

In line with what we had forecast in the June Wage Tracker, average weekly earnings including bonuses (AWE) in Great Britain increased sharply in the three months to May to 7.3 per cent compared to a year ago, up from 5.7 per cent in the three months to April. This increase is partially explained by a combination of compositional and base effects, but is also likely to represent labour shortages in some sectors.

Our estimate of underlying wage growth which excludes base and compositional effects also increased to 3.8 per cent in the three months to May, up from 2.5 per cent in the three months to April. Using the same methodology as described in the June Wage Tracker, we estimate that the base effect accounts for 3.1 percentage points in AWE growth, and we use the ONS estimate of 0.4 percentage points for the compositional effect.

The acceleration in underlying wage growth is proof that the labour market is becoming tighter, even if the economy is far from full employment. The KPMG and REC UK Report on Jobs points to a decrease in candidate availability to explain the rise in wages, in particular for new recruits. The end of the furlough scheme in September will increase candidate availability and reduce pressure on wages, but strong wage growth could continue if there is a mismatch between the skills of the labour force and the demand of new jobs.

Figure 4: public and private sector average weekly earnings (including bonuses)
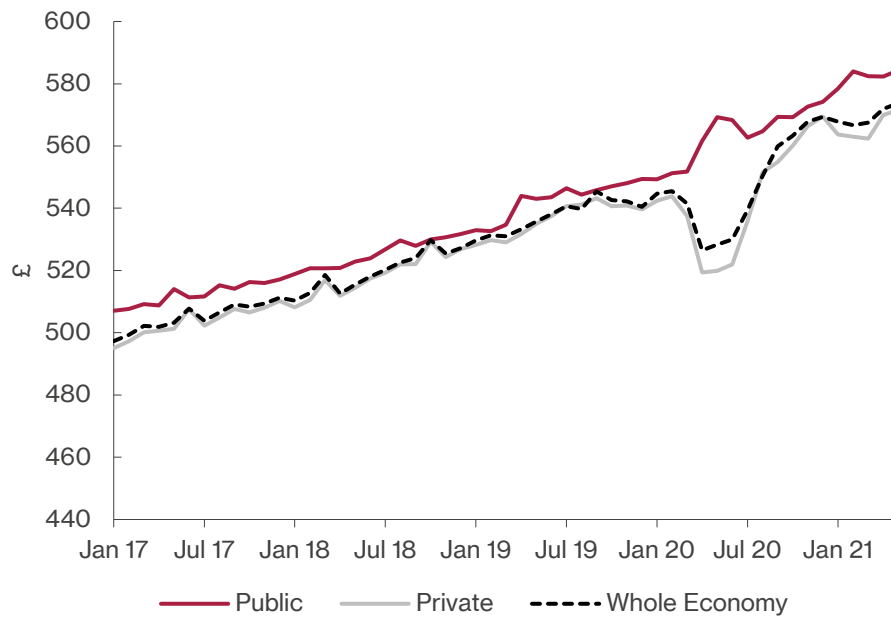
Source: ONS

The base effect should peak in June, causing AWE to accelerate to 8.5 per cent in the second quarter of 2021, and to ease to 5.4 per cent in the third quarter. The compositional effect should also vanish in the third quarter because of the end of the furlough scheme and a return to normal in most sectors of the economy. There is a risk that wage growth could be lower if unemployment increases. On the other hand, wage growth could be higher if labour market shortages continue, and higher prices feed into wage growth.

Table 1 - Summary table of earnings growth

	Average Weekly Earnings					
	Whole economy		**Private sector**		**Public sector**	
Latest weights	100		82		18	
	Regular	**Total**	**Regular**	**Total**	**Regular**	**Total**
Jan-20	511	545	503	542	547	549
Feb-20	512	546	504	544	548	551
Mar-20	510	541	502	538	550	552
Apr-20	502	527	490	519	558	562
May-20	503	528	490	520	567	569
Jun-20	505	530	492	522	565	568
Jul-20	512	539	501	536	562	563
Aug-20	518	550	508	552	563	565
Sep-20	524	560	514	555	568	569
Oct-20	528	563	518	560	567	569
Nov-20	531	568	522	566	570	573
Dec-20	533	569	525	570	571	574
Jan-21	533	568	523	564	577	578
Feb-21	535	567	525	563	580	584
Mar-21	536	568	526	562	579	582
Apr-21	540	572	531	570	579	582
May-21	540	574	531	572	579	584
Jun-21	545	574	536	571	583	586
Jul-21	549	575	540	572	584	588
Aug-21	554	579	545	576	587	591
Sep-21	559	584	549	582	589	593
% change 3 month average year on year						
Jan-20	3.1	3.1	3.0	2.8	3.2	3.1
Feb-20	3.0	2.8	2.8	2.6	3.2	3.2
Mar-20	2.7	2.5	2.4	2.3	3.3	3.2
Apr-20	1.7	1.2	1.2	0.6	3.2	3.3
May-20	0.7	-0.3	-0.1	-1.2	3.8	3.8
Jun-20	-0.2	-1.4	-1.3	-2.7	4.1	4.2
Jul-20	0.2	-1.1	-0.9	-2.2	4.4	4.1
Aug-20	0.9	0.0	0.1	-0.6	4.1	3.8
Sep-20	2.0	1.4	1.4	1.1	4.1	3.7
Oct-20	2.9	2.8	2.5	2.6	4.1	4.0
Nov-20	3.6	3.7	3.3	3.4	4.3	4.3
Dec-20	4.1	4.6	3.9	4.6	4.3	4.4
Jan-21	4.2	4.8	4.1	4.7	4.8	4.8
Feb-21	4.4	4.5	4.2	4.4	5.2	5.3
Mar-21	4.6	4.4	4.3	4.0	5.5	5.6
Apr-21	5.7	5.8	5.7	5.9	5.0	5.0
May-21	6.7	7.4	7.2	8.1	3.7	3.9
Jun-21	7.6	8.5	8.5	9.7	3.0	3.1
Jul-21	7.5	7.9	8.3	8.7	3.0	3.4
Aug-21	7.3	6.7	7.9	6.8	3.7	4.1
Sep-21	6.9	5.4	7.3	5.3	3.9	4.4
% change month on same month of previous year						
Jan-20	2.8	2.8	2.7	2.7	3.0	3.0
Feb-20	3.0	2.8	2.6	2.6	3.2	3.4
Mar-20	2.4	1.9	2.0	1.7	3.6	3.2
Apr-20	-0.2	-1.1	-1.0	-2.4	2.8	3.3
May-20	-0.2	-1.5	-1.4	-2.8	5.0	4.8
Jun-20	-0.2	-1.5	-1.4	-2.8	4.4	4.4
Jul-20	1.0	-0.4	0.2	-0.9	3.9	3.1
Aug-20	2.0	1.9	1.4	2.0	3.9	3.9
Sep-20	2.9	2.8	2.6	2.2	4.4	4.2
Oct-20	3.7	3.7	3.4	3.5	4.0	4.0
Nov-20	4.1	4.8	4.0	4.6	4.4	4.6
Dec-20	4.3	5.4	4.4	5.6	4.4	4.6
Jan-21	4.3	4.2	4.0	4.1	5.5	5.3
Feb-21	4.5	3.8	4.2	3.5	5.8	6.0
Mar-21	5.1	5.0	4.8	4.5	5.3	5.4
Apr-21	7.6	8.5	8.4	9.8	3.8	3.6
May-21	7.4	8.7	8.4	10.0	2.1	2.6
Jun-21	7.8	8.2	8.8	9.4	3.1	3.2
Jul-21	7.3	6.7	7.8	6.8	3.9	4.4
Aug-21	6.9	5.3	7.2	4.4	4.2	4.5

Health warning

NIESR's Wage Tracker includes predictions for regular pay and bonus payments for the whole economy, as well as forecasts for private and public sector wages. The Wage Tracker exploits information from key macroeconomic indicators, including labour market trends, building also on information from monthly GDP nowcasts produced by NIESR's GDP Tracker and survey evidence, such as labour costs in the manufacturing and service sectors from the Bank of England Agents Score. The wage models also capture the interaction between private and public pay, shown to be relevant in work done by NIESR.

To check how our methodology would work in real time we have produced judgement-free forecasts of earnings growth for the period between 2010M07 and 2018M10. For whole economy earnings, the root mean square error is 0.2 per cent points for the measure excluding bonuses and 0.4 per cent points for the measure including bonuses. So, on average, our projections are likely to have an error of 0.2/0.4 percentage points above or below the forecasts we publish. These numbers indicate the degree of uncertainty around the point forecasts produced by the models at each point in time. The errors are greater for the measure of earnings including bonuses because bonus payments, particularly in the private sector, are subject to short-term volatility. In practice, we add residuals reflecting our judgement so the error bands may be larger or smaller.

Forecast schedule

The NIESR Wage Tracker provides a rolling monthly forecast for earnings growth. The ONS produces an estimate of Average Weekly Earnings (AWE) for any particular quarter some 40 days after the end of the quarter. The NIESR Wage Tracker will publish AWE forecasts 5 months ahead of the ONS release for the reference quarter, updating that forecast four times before the official data is out, similar to the monthly GDP Tracker schedule.

Notes for editors: For further information please contact the NIESR Press Office: press@niesr.ac.uk or Luca Pieri on 020 7654 1954 / l.pieri@niesr.ac.uk

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