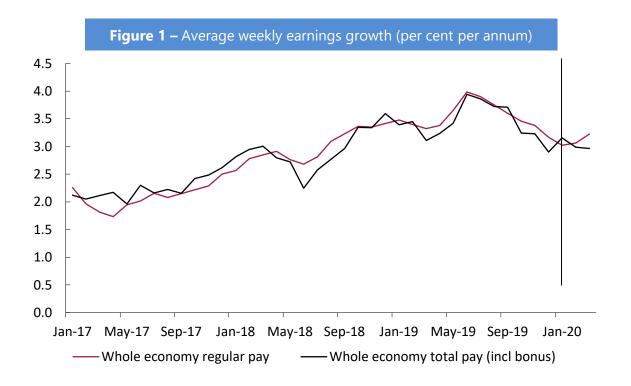


Tuesday 17 March 2020

# WAGE GROWTH LIKELY TO BE HIT BY THE COVID-19 OUTBREAK

## **Main points**

- According to new ONS statistics published this morning, UK average weekly earnings expanded by 3.1 per cent excluding bonuses in the three months to January 2020 compared to the year before, and by 3.1 per cent if bonus payments are taken into account.
- The Wage Tracker indicates that nominal earnings growth excluding bonuses will be 3.2 per cent in the first quarter of 2020 and exactly 3 per cent including bonuses.



Cyrille Lenoel, Senior Economist at NIESR, said: "However, the outlook for wage growth has significantly worsened as a result of the disruptions caused by the coronavirus outbreak in the United Kingdom at the beginning of March".

#### **Details**

Despite a tight labour market and an improvement in business confidence since the General Election, the outlook for wage growth has significantly worsened in March as a result of the impact of the coronavirus outbreak in the United Kingdom and in many other countries around the world.

Before that pivotal moment, earnings were growing at about 3 per cent and business investment had been improving in the UK since the General Election. The new ONS statistics published this morning show that average weekly earnings (AWE) expanded by 3.1 per cent excluding bonuses in the three months to January 2020 compared to the year before, and by the same 3.1 per cent if bonus payments are taken into account (figure 1). This is in line with our previous forecast of AWE growth of 3.2 per cent (and 3 per cent including bonuses) over the same period.

Markit's Business Outlook survey stood at 46 in February, which was the highest reading in 3 years. KPMG and REC report of Jobs observed that total demand for staff expanded in February at the quickest rate for over a year. Demand was mainly towards permanent placements. Permanent placement growth accelerated, starting pay for permanent staff rose at a quicker pace but temporary wage inflation softened. Permanent placements have been made more attractive compared to contract work by the IR35 changes due to take effect in April 2020, which means that contract workers will have to pay the same level of tax as permanent members of staff pay.

The UK labour market is in a situation with limited excess capacity. The employment rate in the three months to January 2020 was at record high of 76.5 per cent and the unemployment rate was at 3.9 per cent, very close to its record low of 3.7 per cent of the last 30 years. There were an estimated 817,000 vacancies in the UK for December 2019 to February 2020, which was 30,000 fewer than a year earlier.

Table 1 reports our estimates for earnings growth in the first quarter of 2020. We forecast regular earnings growth to reach 3.1 per cent in the three months to March in the private sector and 3.3 per cent in the public sector, consistent with an expected easing of fiscal policy. An upside risk to our forecast is that National Living Wage and minimum wage upratings may add to whole-economy earnings growth in the first half of 2020. A downside risk is the disruptive impact of the coronavirus crisis.

The Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 1.8 per cent in January 2020, increasing from 1.4 per cent in December 2019. The global demand shock from the reduction in activity related to the coronavirus is expected to put downward pressure on prices. The WTI price of crude oil was divided by two from 60 dollars in December 2019 to 30 dollars on 16 March 2020 as internal divisions in OPEC+ led to higher production despite a fall in demand. Lower commodity prices are expected to feed

into lower consumer prices. At a special meeting on 10 March 2020, the Bank of England reduced its Bank Rate by 50 basis points to 0.25 per cent.

As companies may face disruptions in their supply chains as a result of the coronavirus health crisis, temporary or contract workers may be the first hit by a reduction in their working hours and unemployment may rise from its current rate of 3.9 per cent. In that adverse scenario, wage pressure could weaken and average weekly earnings growth to decrease from the current 3 per cent. The fall in the stock market illustrated by the decline of the FTSE 100 by 33 per cent year-to-date until 16 March shows that companies' earnings are expected to decline significantly this year as a result of supply chain disruptions and workers not able to come to their work environment. As a result, there is also a significant downside risk to our bonus growth forecast in the private sector.

If the current crisis were to have similar effects on wages as the Great Financial Crisis, then average weekly earnings could temporarily decrease by up to 2 per cent as they did between 2008 and 2009 (figure 2).

British workers may find themselves in a situation where real wages could grow for a period faster than economic growth, with downside risks both on wages and consumer prices growth. We expect real average weekly earnings to grow by 1.2 per cent in the first quarter of 2020, compared to the same quarter in 2019. However, such growth would only be temporary, as over the medium term, real wages are expected to grow in line with productivity.

Figure 2 – Average weekly earnings (per cent change 3 month average year-on-year)

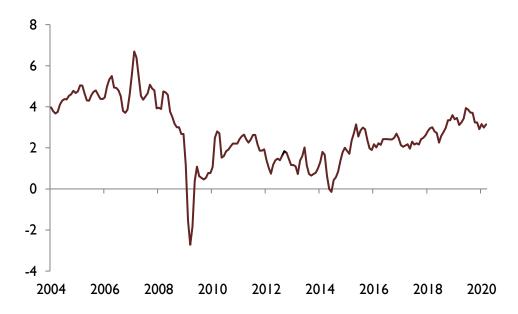


 Table 1 - Summary table of earnings growth

Average Weekly Earnings (average £ per week)							
	Whole economy		Private sector		Public sector		
Latest weights	100		82		18		
	Regular	Total	Regular	Total	Regular	Total	
Jun-19	506	538	498	537	540	544	
Jul-19	507	539	500	539	541	546	
Aug-19	508	540	501	539	542	544	
Sep-19	509	542	501	541	544	546	
Oct-19	510	543	502	541	546	547	
Nov-19	510	544	503	543	547	548	
Dec-19	511	544	504	543	548	549	
Jan-20	512	547	504	546	547	549	
Feb-20	514	545	506	544	549	553	
Mar-20	515	546	508	544	551	555	
% change 3 month average year on year							
Aug-19	3.8	3.7	4.0	3.8	3.2		
Sep-19		3.7	3.7	3.8			
Oct-19		3.2	3.5	3.1	3.4		
Nov-19		3.2	3.4	3.1	3.4		
Dec-19	3.2	2.9	3.3	2.8	3.4		
Jan-20		3.1	3.1	3.1	3.2		
Feb-20		3.0	3.1	2.9	3.2		
Mar-20	3.2	3.0	3.1	2.9	3.3	3.6	
% change month on same month of previous year							
Aug-19	3.5	3.4	3.7	3.5	3.2	2.8	
Sep-19	3.7	3.8	3.5	3.8	3.4	3.4	
Oct-19	3.2	2.5	3.3	2.1	3.4	3.2	
Nov-19	3.2	3.4	3.3	3.4	3.4	3.2	
Dec-19	3.0	2.8	3.3	2.8	3.4	3.2	
Jan-20	2.8	3.2	2.6	3.0	2.8	3.0	
Feb-20	3.3	2.9	3.2	2.8	3.4	4.0	
Mar-20	3.5	2.8	3.4	3.0	3.7	3.9	

## **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.

**Table 2 –** Root Mean Square Error for Average Weekly Earnings forecasts

	Public-sector	Private-sector	Whole economy
Excluding bonus	0.26	0.24	0.22
Including bonus	0.31	0.48	0.38

Notes: 3-month average year on year growth rates, percentage

### **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: <a href="mailto:press@niesr.ac.uk">press@niesr.ac.uk</a> / 07930 544631 / 0207 654 1954

National Institute of Economic and Social Research 2 Dean Trench Street, Smith Square London, SW1P 3HE, United Kingdom

Switchboard Telephone Number: 020 7222 7665

Website: http://www.niesr.ac.uk