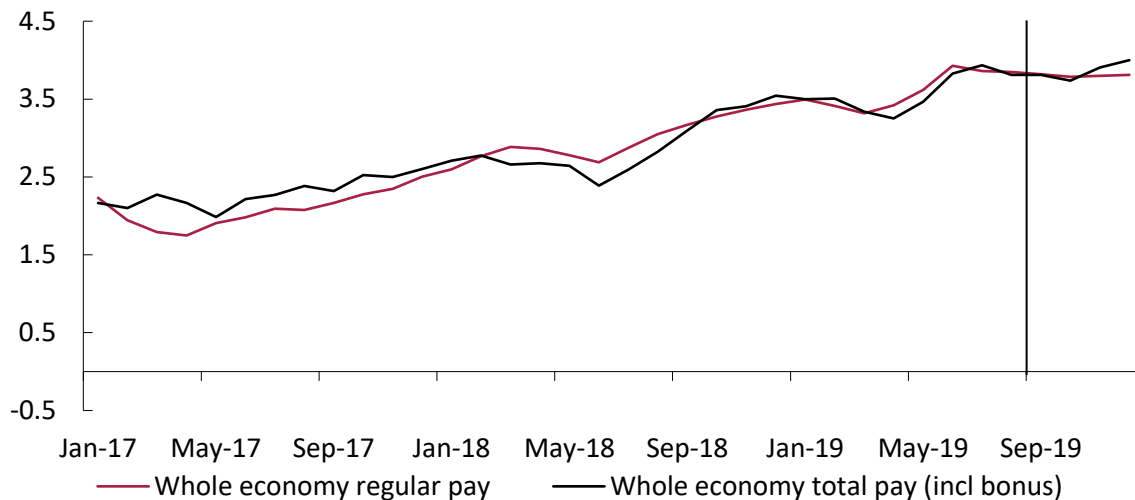


## LABOUR MARKET WEATHERING AN INCREASINGLY DIFFICULT ECONOMIC ENVIRONMENT

Figure 1 – Average weekly earnings growth (per cent per annum)



### Main points

- According to new ONS statistics published this morning, UK average weekly earnings (AWE) expanded by 3.8 per cent (excluding and including bonuses) in the three months to August compared to the year before (figure 1).
- With CPI inflation at 1.9 per cent in the three months to August, real wages grew at an annual rate of 1.9 per cent over the same period.
- Private sector earnings data in August turned out to be in line with the estimate published in our Wage Tracker last month and public sector earnings data was only slightly weaker.
- The Wage Tracker indicates that regular earnings growth will have stabilised at an annual rate of 3.8 per cent in the third quarter and is expected to remain largely unchanged in the fourth quarter.
- Based on NIESR Wage Tracker and GDP Tracker information, we estimate unit labour cost growth of around 3½ per cent per annum in the third and fourth quarters of 2019 while economic activity remains lacklustre.

*“In the economy as a whole, employment and wage growth are now stabilising amidst global and domestic uncertainties. While sectors engaging in international trade increasingly face difficulties, also affecting hiring and pay, domestically active service sectors are so far withstanding the economic challenges.”*

**Dr Arno Hantzsche**

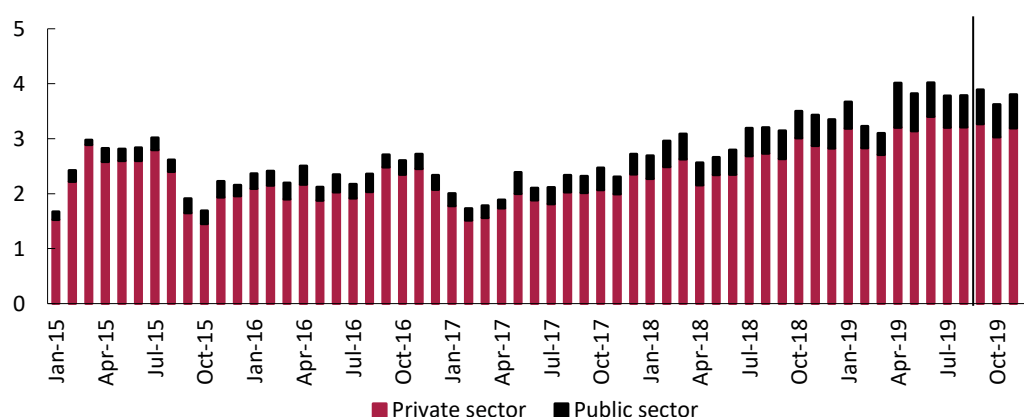
**Principal Economist in Macroeconomic Modelling and Forecasting**

## Details

Unemployment stabilised at 3.9 per cent in the three months to August. Yet aggregate labour market data somewhat conceal that some sectors, like professional services, operate near capacity and continue to face recruitment difficulties, while others, in particular manufacturing, see labour demand cooling rapidly as the result of a global and domestic weakening in growth momentum. Staff shortages translate into higher starting salaries, which rose at a sharp and accelerated pace in September, according to the KPMG and REC [Report on Jobs](#), after a slowdown in August. However, [IDR](#) report that firms target pay increases more than in the past to retain staff rather than raising awards broadly and Bank of England [Agents](#) mention the increased use of non-wage benefits. According to IHS Markit/CIPS, staff levels were reduced in [manufacturing](#) at the fastest pace in 6½ years in September and the [service sector](#) as a whole cut jobs for the first time in 5 months. Employment intentions remain slightly negative. Consistent with a labour market facing labour shortages in some areas while others shed labour, expectations are for median pay settlements to remain unchanged in the near term.

In recent months, support to whole-economy employment growth came increasingly from the public sector. Figure 2 depicts the growing contribution of public sector earnings growth to economy-wide regular earnings growth, which partly offset stabilising private sector earnings growth. Higher public spending is likely to allow for higher pay awards than in the recent past.

Figure 2 – Contributions to regular earnings growth (per cent per annum)



Source: ONS, NIESR estimates.

Our short-term forecasts for pay in the private and public sectors are reported in table 1. These suggest that total pay growth in both sectors will stabilise at 3½ to 4 per cent in the fourth quarter of 2019 as the economic outlook remains fragile. According to the [ONS](#), labour productivity fell by 0.5 per cent in the year to the second quarter of 2019. NIESR's [GDP Tracker](#) suggests that economic output increased by 0.5 per cent in the third quarter and will expand by 0.3 per cent in the final quarter of the year, after the 0.2 per cent drop in the second quarter. Robust average weekly earnings growth together with subdued productivity growth suggest that unit labour cost growth remains elevated, reaching 3.5 per cent and 3.3 per cent in the third and fourth quarter, respectively, after having risen to a 10-year high of 3.9 per cent in the second quarter. There is a risk that firms pass higher production costs on to consumers which could add to inflationary pressures in the economy.

Table 1 - Summary table of earnings growth

| <b>Average Weekly Earnings (average £ per week)</b>  |                      |              |                       |              |                      |              |
|--|----------------------|--------------|-----------------------|--------------|----------------------|--------------|
|  | <b>Whole economy</b> |              | <b>Private sector</b> |              | <b>Public sector</b> |              |
| <i>Latest weights</i>                                | 100                  |              | 82                    |              | 18                   |              |
|  | <b>Regular</b>       | <b>Total</b> | <b>Regular</b>        | <b>Total</b> | <b>Regular</b>       | <b>Total</b> |
| Feb-19   | 497                  | 529          | 490                   | 528          | 530                  | 533          |
| Mar-19   | 498                  | 530          | 491                   | 529          | 531                  | 534          |
| Apr-19   | 503                  | 534          | 494                   | 533          | 542                  | 544          |
| May-19   | 503                  | 537          | 496                   | 536          | 540                  | 542          |
| Jun-19   | 506                  | 539          | 498                   | 537          | 540                  | 543          |
| Jul-19   | 507                  | 541          | 500                   | 539          | 541                  | 546          |
| Aug-19   | 509                  | 542          | 502                   | 541          | 542                  | 545          |
| Sep-19   | 511                  | 544          | 503                   | 543          | 544                  | 547          |
| Oct-19   | 512                  | 547          | 505                   | 546          | 546                  | 549          |
| Nov-19   | 514                  | 549          | 506                   | 549          | 548                  | 550          |
| Dec-19   | 515                  | 550          | 508                   | 550          | 549                  | 552          |
| <b>% change 3 month average year on year</b>         |                      |              |                       |              |                      |              |
| Apr-19   | 3.4                  | 3.3          | 3.6                   | 3.3          | 3.0                  | 3.1          |
| May-19   | 3.6                  | 3.5          | 3.7                   | 3.5          | 3.5                  | 3.6          |
| Jun-19   | 3.9                  | 3.8          | 4.0                   | 4.0          | 3.9                  | 4.0          |
| Jul-19   | 3.9                  | 3.9          | 4.0                   | 4.0          | 3.5                  | 3.7          |
| Aug-19   | 3.8                  | 3.8          | 4.0                   | 3.8          | 3.3                  | 3.5          |
| Sep-19   | 3.8                  | 3.8          | 3.9                   | 3.9          | 3.3                  | 3.5          |
| Oct-19   | 3.8                  | 3.7          | 3.9                   | 3.7          | 3.3                  | 3.4          |
| Nov-19   | 3.8                  | 3.9          | 3.9                   | 3.9          | 3.4                  | 3.5          |
| Dec-19   | 3.8                  | 4.0          | 3.9                   | 4.0          | 3.5                  | 3.6          |
| <b>% change month on same month of previous year</b> |                      |              |                       |              |                      |              |
| Apr-19   | 4.0                  | 3.6          | 3.9                   | 4.0          | 4.5                  | 4.5          |
| May-19   | 3.8                  | 4.0          | 3.8                   | 4.1          | 3.8                  | 3.8          |
| Jun-19   | 4.0                  | 3.9          | 4.1                   | 3.8          | 3.4                  | 3.7          |
| Jul-19   | 3.8                  | 3.9          | 3.9                   | 4.0          | 3.2                  | 3.7          |
| Aug-19   | 3.8                  | 3.6          | 3.9                   | 3.7          | 3.2                  | 3.3          |
| Sep-19   | 3.9                  | 3.9          | 4.0                   | 3.9          | 3.5                  | 3.6          |
| Oct-19   | 3.7                  | 3.7          | 3.7                   | 3.4          | 3.3                  | 3.5          |
| Nov-19   | 3.8                  | 4.2          | 3.9                   | 4.3          | 3.4                  | 3.6          |
| Dec-19   | 3.9                  | 4.1          | 4.0                   | 4.2          | 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% points for the measure excluding bonuses and 0.4% 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 | <b>0.26</b>   | <b>0.24</b>    | <b>0.22</b>   |
| Including bonus | <b>0.31</b>   | <b>0.48</b>    | <b>0.38</b>   |

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.

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