National Institute of Economic and Social Research

NIESR Monthly Wage Tracker

Wage Growth Softens Below 7 Per Cent as Labour Market Loosens Gradually

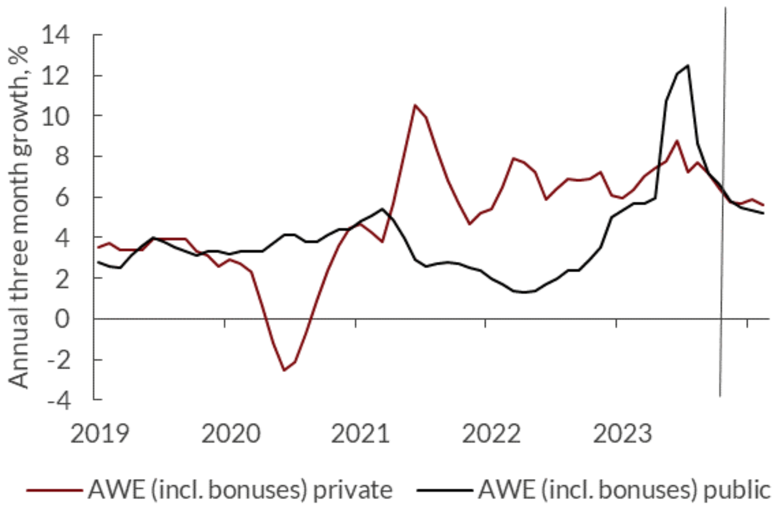
Paula Bejarano Carbo

16th January 2024

"Today's ONS figures suggest that the annual growth rate of average weekly earnings was 6.6 per cent in the three months to November 2023, and 6.5 per cent if we include bonuses. While these figures remain elevated by historical standards, they indicate that wage growth softened gradually towards the end of the year, after peaking over summer. That said, when we account for inflation, real regular pay (excluding bonuses) only rose by 1.4 per cent, while real total pay rose by 1.3 per cent – illustrating the extent to which elevated inflation erodes household incomes. With vacancies falling steadily on the quarter, and experimental estimates of the inactivity and unemployment rates not moving much, we can infer that the labour market continues to loosen – albeit at a slow pace – and that the general trend of softening wage growth will continue in the first quarter of 2024."

Paula Bejarano Carbo
Economist, NIESR

Figure 1 – Average weekly earnings in public and private sectors



Main Points

- **Pay growth remains strong:** The latest ONS estimates suggest that the annual growth rate of average weekly earnings, including bonuses, was 6.5 per cent in the three months to November 2023 while pay growth excluding bonuses was 6.6 per cent. These figures indicate that wage growth continued to soften towards the end of 2023, after peaking over summer (Figure 1).

- **We forecast wage growth to slow as the labour market continues to cool**: economy-wide total pay (incl. bonuses) and regular pay are estimated to have grown at 5.7 and 6.2 per cent, respectively, in the fourth quarter of this year relative to the third quarter. Our forecast for the first quarter of 2024 sees these figures at 5.6 and 6.0 per cent, respectively.

- **The further fall in vacancies is driving the cooling of labour market conditions:** with experimental estimates of the unemployment and inactivity rates remaining largely unchanged in recent months, it is decreasing vacancies that have been contributing to a gradual loosening of the labour market. Vacancies fell by 49,000 in the fourth quarter of 2023, representing a 5.0 per cent decrease on the quarter and marking the 18th consecutive period in which vacancy numbers have fallen. However, vacancies still remained above their pre-pandemic level.

Vacancies and employment

Due to data collection issues affecting the ONS Labour Force Survey (growing attrition in the survey response rate), today's release only contains traditional measures of earnings, vacancies and HMRC data. The ONS has released experimental estimates on UK employment, unemployment and economic inactivity, derived using growth rates from PAYE. The experimental ONS data indicate that the employment, unemployment and inactivity rates remained largely unchanged on the quarter, at 75.8 per cent, 4.2 per cent, and 20.8 per cent respectively. While these experimental estimates can help give us an idea of where the values are, in the absence of LFS data, our understanding of these variables remains incomplete and uncertain.

A good measure of labour market tightness is the unemployment-to-vacancy ratio. Figure 2 plots the unemployment-to-vacancy ratio, with data from June onwards reflecting an implied path calculated using experimental ONS unemployment and inactivity rate estimates and NiGEM estimates of the working age population. These figures for June onwards should therefore only be taken as illustrative of where the general path of labour market tightness could be expected to lie. With estimates of the unemployment and inactivity rates remaining largely unchanged in recent months, it is decreasing vacancies that are contributing to a gradual loosening of the labour market. In fact, the number of job vacancies fell by 49,000 in the fourth quarter of 2023, representing a 5.0 per cent decrease on the quarter and marking the 18th consecutive period in which vacancy numbers have fallen. Regardless of where the unemployment rate is exactly, we know that an unemployment rate around 4.2 per cent paired with a total number of vacancies of 934,000 remains well above the 2015-2019 average of the unemployment-to-vacancy ratio of 1.9 (Figure 2). As a result, the labour market remains tight, enabling high wage growth.

The latest KPMG and REC report on Jobs notes that economic uncertainty led to a further fall in permanent placements in December, decreased vacancy postings and increased redundancies. Despite this increase in caution on the labour demand side, the report notes that candidate availability grew at the end of the year, with survey data indicating increased labour supply. Taken together, this survey data aligns with experimental data pointing to a moderate but gradual loosening of the labour market in the second half of 2023.

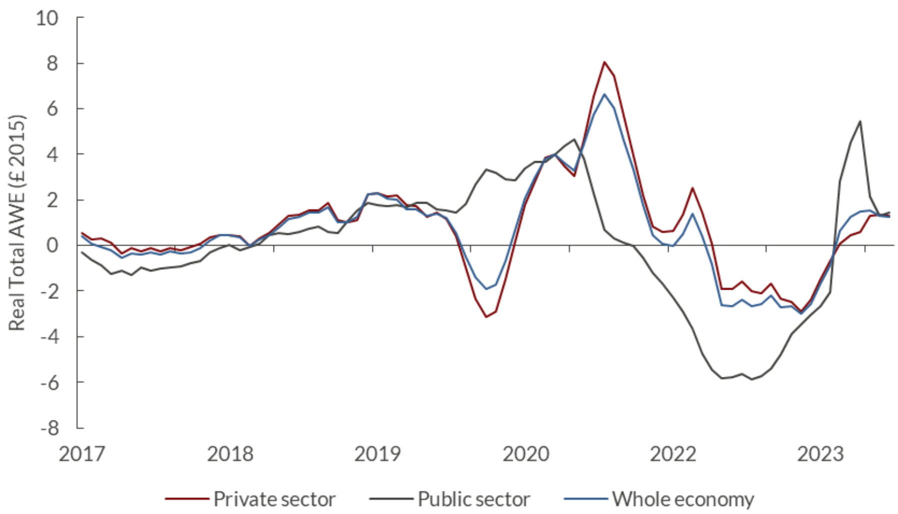
Figure 2 – Unemployed People Per Vacancy

Pay

The annual growth rate of average weekly earnings, including bonuses, was 6.5 per cent in the three months to November 2023 while pay growth excluding bonuses was 6.6 per cent. These figures indicate that wage growth continued to soften towards the end of 2023, after peaking over summer (Figure 1).

When we adjust for inflation, real economy-wide total pay growth falls from 6.5 per cent to 1.3 per cent in the three-month period to November, indicating the extent to which inflation continues to erode workers' real incomes. Real total pay in the private and public sector grew by 1.3 and 1.4 per cent in the three months to November 2023.

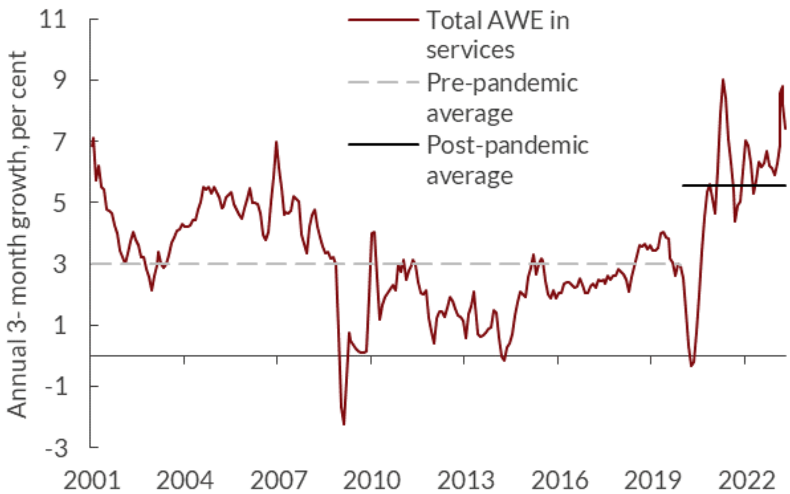
Figure 3 – Real average weekly earnings in public and private sectors



Private-sector regular pay growth was 6.5 per cent in the three months to November and 6.4 per cent if we include bonuses. We estimate these figures to have grown at 6.2 and 5.7 per cent in the fourth quarter of 2023. Our forecast for the first quarter of 2024 sees these figures at 6.3 per cent and 5.6 per cent, respectively.

Public-sector total AWE annual growth has been on an increasing path since April 2022 of 1.3 per cent and is currently sitting at 6.6 per cent. This figure has fallen substantially from the series high recorded in August of 12.5 per cent which was largely driven by one-off NHS and civil-service bonus payments. We estimate public sector total pay growth to have decreased to 5.8 per cent in the fourth quarter of 2023. We forecast public sector total pay to grow by 5.2 per cent in the first quarter of 2024.

Figure 4 -Total average weekly earnings in the services sector



Services sector total AWE annual growth has been on an increasing path since the initial pandemic-related plummet, and currently stands at 6.7 per cent in the three months to November, particularly thanks to wholesaling, retailing, hotels and restaurants sector. As Figure 5 above shows, there seems to have been a shift in services sector total AWE growth pre-and post-pandemic; the average growth rate in AWE in this sector was 3 per cent from January 2001 to February 2020, while from March 2020 onwards this average has increased to 5.5 per cent (even accounting for the initial covid-related plummet). Since pay in the services sector makes up most of the input costs in this sector, it is the main driver of services inflation. As we have been noting in our recent CPI trackers, with energy price inflation 'dropping out' of the CPI basket in recent months, food and core inflation are the main factors keeping CPI inflation elevated.

Continuing high wage growth in the services sector alongside a low unemployment-to-vacancy ratio may concern monetary policymakers, who may take this as a sign that services inflation will continue to generate persistence in underlying inflation in the United Kingdom, despite monetary tightening efforts. Indeed, as noted in Haskel et al.'s (2023) recent model of the wage-price determinants of inflation in the United Kingdom, increased labour market tightness and its effect on elevated wage inflation became increasingly important components of CPI inflation throughout 2023.

Not only does strong wage growth pose an inflationary risk, but also it can create tension in financial markets. As we noted in our recent term premium tracker, strong labour market data may have led to a rise in the US term premium in October as investors became less sure about the path of short-term interest rates and possibly anticipated a further fed rate hike. One way to calm market uncertainty despite strong wage data would be for central banks to publish rate path forecasts, in order to align market expectations to a particular, but not definite, trajectory.

Caveat

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 Scores. 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 July 2010 and October 2018. For whole economy earnings, the root mean square error is 0.2 percentage points for the measure excluding bonuses and 0.4 percentage points for the measure including bonuses. 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 actual error bands may be larger or smaller.

Notes for editors:

For further information please contact the NIESR Press Office: press@niesr.ac.uk or Luca Pieri on 020 3948 4488 / l.pieri@niesr.ac.uk

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

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
Nov-22	587	634	583	639	610	613
Dec-22	589	632	585	636	614	616
Jan-23	592	635	586	639	620	624
Feb-23	597	640	592	645	620	621
Mar-23	600	644	595	648	621	623
Apr-23	605	651	601	655	624	625
May-23	611	655	607	658	626	626
Jun-23	614	670	610	663	629	711
Jul-23	617	665	612	667	633	656
Aug-23	620	664	615	669	634	641
Sep-23	622	673	617	674	642	645
Oct-23	619	664	614	670	643	646
Nov-23	623	666	618	671	645	648
Dec-23	627	670	622	674	647	653
Jan-24	629	674	625	678	649	653
Feb-24	632	676	628	680	651	655
Mar-24	635	678	631	683	653	657
% change 3 month average year on year						
Nov-22	6.5	6.9	7.3	7.4	3.3	3.4
Dec-22	6.7	6.5	7.3	6.8	4.2	4.2
Jan-23	6.6	6.3	7.0	6.5	4.9	4.9
Feb-23	6.6	5.8	7.0	6.0	5.3	5.3
Mar-23	6.8	6.2	7.1	6.4	5.6	5.7
Apr-23	7.3	6.8	7.6	7.0	5.7	5.7
May-23	7.5	7.3	7.8	7.5	5.9	5.9
Jun-23	7.8	8.4	8.1	7.8	6.3	10.7
Jul-23	7.8	8.6	8.1	8.8	6.6	12.1
Aug-23	7.9	8.3	8.1	7.3	6.8	12.5
Sep-23	7.8	8.0	7.8	7.7	7.4	8.6
Oct-23	7.2	7.2	7.2	7.2	7.0	7.2
Nov-23	6.6	6.5	6.5	6.4	6.6	6.6
Dec-23	6.2	5.7	6.2	5.7	5.7	5.8
Jan-24	6.3	5.7	6.4	5.7	5.3	5.5
Feb-24	6.2	5.9	6.4	5.9	5.0	5.4
Mar-24	6.0	5.6	6.3	5.6	5.0	5.2
% change month on same month of previous year						
Nov-22	6.9	8.0	7.6	8.7	4.1	4.3
Dec-22	6.5	4.8	7.1	4.8	4.8	4.6
Jan-23	6.3	6.0	6.4	6.0	5.8	5.9
Feb-23	7.0	6.7	7.4	7.1	5.4	5.4
Mar-23	7.1	5.9	7.4	6.1	5.6	5.6
Apr-23	7.7	7.8	8.1	7.9	6.1	6.1
May-23	7.8	8.1	8.0	8.4	6.1	6.1
Jun-23	7.9	9.3	8.3	6.9	6.6	19.9
Jul-23	7.9	8.3	7.9	7.8	7.1	10.3
Aug-23	7.8	7.3	7.9	7.2	6.7	7.4
Sep-23	7.6	8.4	7.5	8.2	8.3	8.2
Oct-23	6.2	5.9	6.2	6.2	5.9	5.9
Nov-23	6.1	5.0	6.0	5.0	5.7	5.7
Dec-23	6.4	6.1	6.4	6.0	5.3	5.9
Jan-24	6.3	6.1	6.7	6.1	4.7	4.7
Feb-24	5.9	5.6	6.1	5.5	5.0	5.5
Mar-24	5.9	5.3	6.1	5.4	5.2	5.4