National Institute of Economic and Social Research

NIESR Monthly Wage Tracker

UK Wages Expected to Grow by 5.4 Per Cent in Q1

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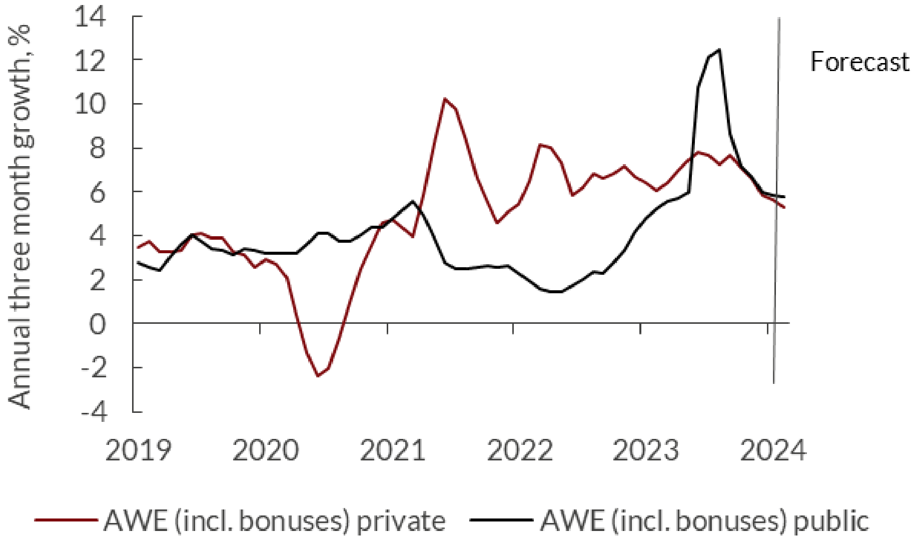
"Today's ONS figures indicate that the annual growth rate in average weekly earnings, including bonuses, was 5.6 per cent in the three months to January, and 6.1 per cent excluding bonuses. While these figures remain high by historical standards, allowing households to regain some of the purchasing power lost during the post-Covid period of high inflation, wage growth continues to soften. We expect wage growth returning to historical levels as the labour market continues to loosen, potentially prompting the Bank of England to consider cutting interest rates in the near future."

Paula Bejarano Carbo
Economist, NIESR

Figure 1 – Average weekly earnings in public and private sectors



Main Points

- **Pay growth softens, but remains strong by historical standards:** The annual growth rate of average weekly earnings, including bonuses, was 5.6 per cent in the three months to January 2024 while pay growth excluding bonuses was 6.1 per cent. These figures indicate that wage growth continued to soften at the start of 2024, after peaking in mid-2023 (Figure 1).

- **We forecast wage growth to continue slowing as the labour market continues to cool**: With vacancies falling steadily since mid-2022, the vacancy-to-unemployment ratio was 0.7 in the three months to January. If this trend continues and the labour market loosens further, wage growth is likely to slow down to its historical levels in the medium-term. We forecast economy-wide total pay (incl. bonuses) and regular pay to grow by 5.4 and 5.7 per cent in the first quarter of 2024, respectively.

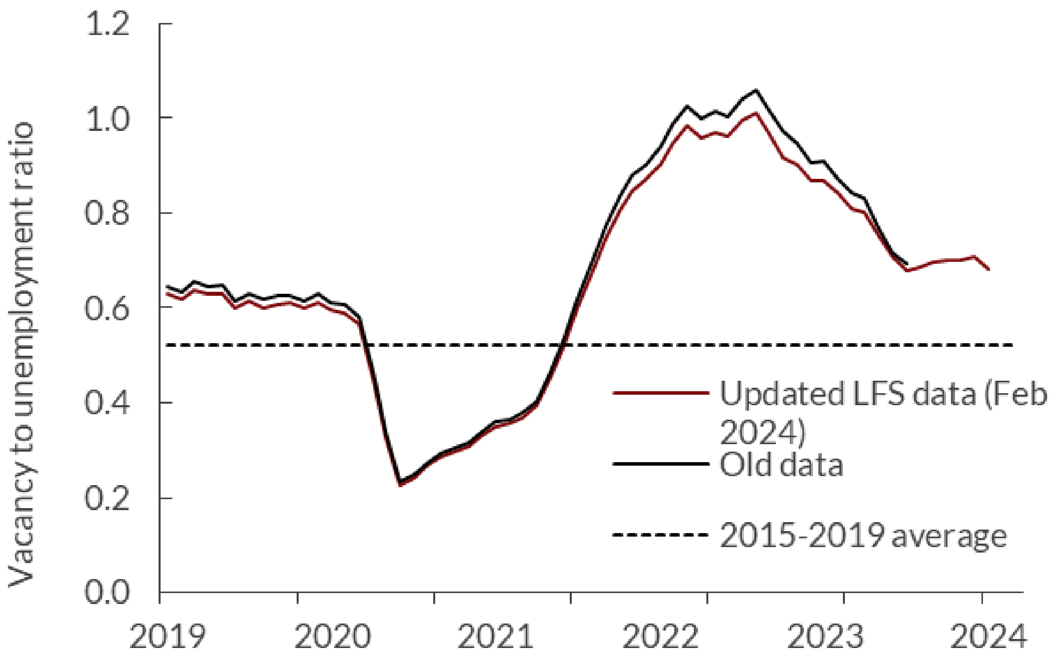
- **Despite pay growth softening, workers will continue to enjoy some real income gains:** Though we expect wage growth to soften over the course of 2024, these pay growth projections are high by historical standards – remaining above the economy-wide total and regular pay growth post-2001 averages of 3.3 and 3.2 per cent. Given recent trends in prices, we can expect workers to continue making real income gains in the coming months, which can be interpreted as a 'wage catch-up' period following over a year of real income losses.

Vacancies and employment

Today's release suggests that the employment rate fell slightly on the quarter to 75.0 per cent, the unemployment rate was largely unchanged on the quarter at 4.0 per cent, and the inactivity rate increased marginally on the quarter to 21.8 per cent.

A good measure of labour market tightness is the vacancy-to-unemployment ratio. Figure 2 plots the vacancy-to-unemployment ratio, which stood at 0.68 in the three months to January, compared to an average of 0.52 in 2015-2019 and a historical average of 0.42. Decreasing vacancies have driven an overall gradual loosening of the labour market since 2022. In fact, the number of job vacancies fell by 43,000 on the quarter in the three months to February 2024, representing a 4.5 per cent decrease and marking the 20th consecutive period in which vacancy numbers have fallen. Figure 2 illustrates that the vacancy-to-unemployment ratio has remained stable in recent months, with a small reduction in the three months to January, and after steadily falling from the historically high levels recorded in 2022. That said, in our recent UK Economic Outlook, we forecast the unemployment rate to rise slowly in the medium term. If this trend of a gradual loosening of the labour market continues as result of falling vacancies and/or increased unemployment, we can expect wage growth to return to historical levels in a few years' time.

Figure 2 – Vacancy-to-unemployment ratio



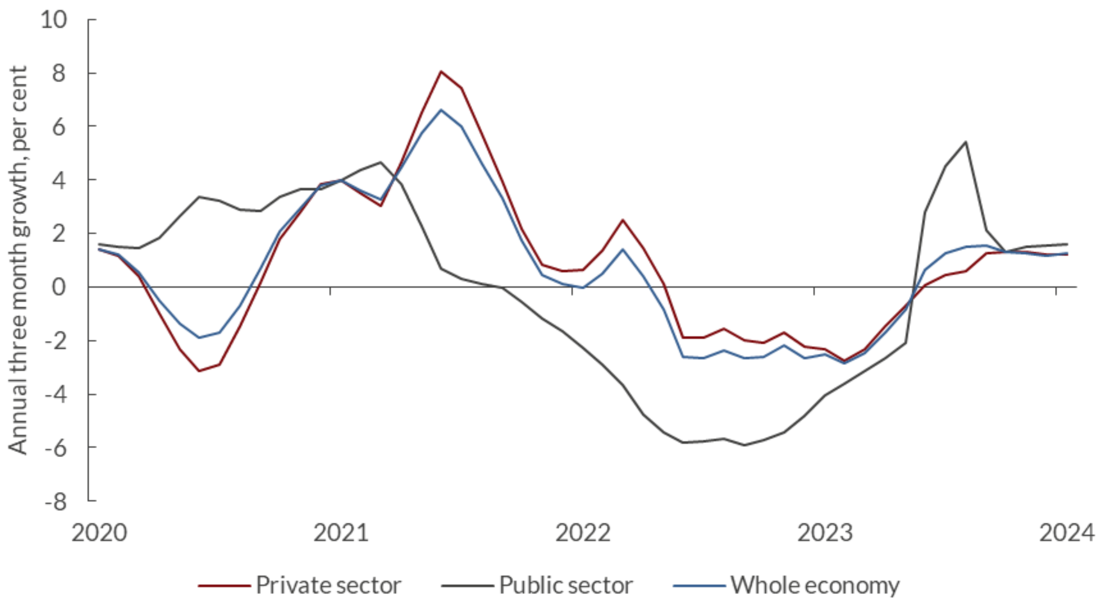
The latest KPMG and REC report on Jobs notes that the rate of salary inflation for permanent placements eased to a three-year low in February, as employer budgets have tightened following months of high nominal wage growth and the labour market continues to loosen. On the latter point, the rate of contraction in demand for staff was the quickest recorded since 2021 – with permanent vacancies falling for yet another month, and temporary vacancies falling for the first time in over three years. With hiring being subdued by high economic uncertainty and weak demand prospects, we can take these higher frequency data as further signs that the labour market will continue to loosen in the coming months.

Pay

The annual growth rate of average weekly earnings, including bonuses, was 5.6 per cent in the three months to January 2024 while pay growth excluding bonuses was 6.1 per cent. These figures indicate that wage growth continued to soften at the start of 2024, after peaking in mid-2023 (Figure 1).

When we adjust for inflation, annual real economy-wide total pay growth falls from 5.6 per cent to 1.3 per cent in the three months to January, indicating the extent to which inflation continues to erode workers' real incomes. Annual real total pay in the private and public sectors grew by 1.2 and 1.6 per cent in three months to January, respectively (Figure 3).

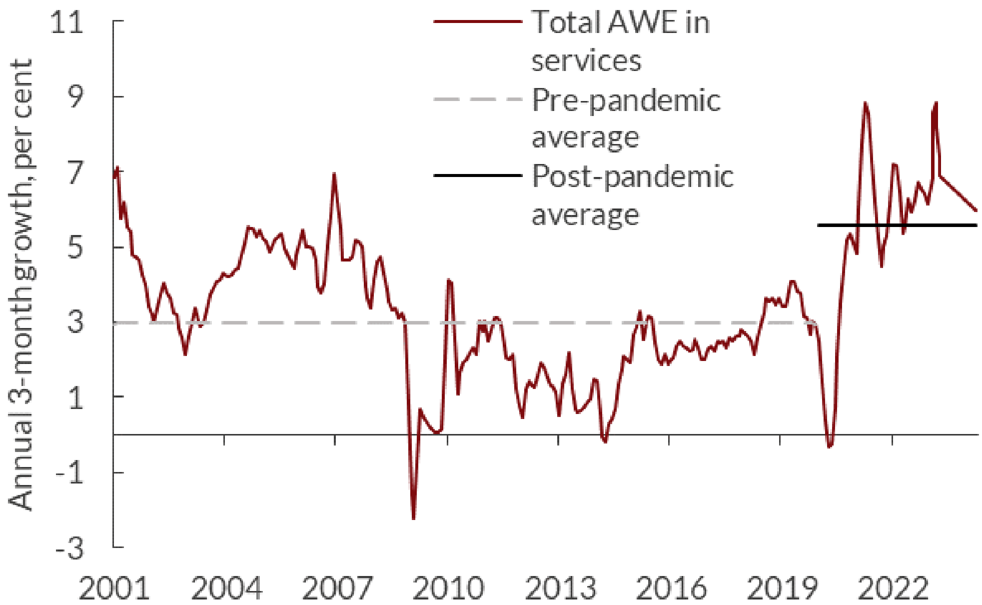
Figure 3 – Real average weekly earnings in public and private sectors



Private-sector annual regular pay growth was 6.1 per cent in the three months to January and 5.7 per cent if we include bonuses. Our forecast for the first quarter of 2024 sees these figures softening to 5.7 per cent and 5.3 per cent, respectively. Though we expect wage growth to soften over the course of 2024, these growth projections are high by historical standards - remaining above the private sector regular and total pay growth post-2001 averages of 3.2 per cent and 3.3 per cent. Given recent trends in prices, we can expect private sector workers to continue making real income gains in the coming months, which can be interpreted as a 'wage catch-up' period following over a year of real income losses.

Public-sector annual total AWE growth was 5.8 per cent in the three months to January. 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 forecast public sector total pay to grow by 5.8 per cent in the first quarter of 2024, well above its post-2001 average of 3.2 per cent.

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 5.8 per cent in the three months to January. As Figure 4 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 5.6 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.

While it is positive that wage growth in the services sector has been on a steady downwards trend since mid-2022, it remains well above its pre-pandemic average (Figure 4). Continuing high wage growth in the services sector alongside the labour market remaining somewhat tight by historical standards 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.

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

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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*
Dec-22	589	633	585	638	614	615
Jan-23	593	637	587	640	619	622
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	624	666	619	671	647	649
Dec-23	626	670	621	674	651	653
Jan-24	627	672	621	676	655	656
Feb-24	631	674	625	678	656	658
Mar-24	634	678	629	681	658	660
% change 3 month average year on year						
Jan-23	6.6	6.3	7.1	6.4	4.9	4.8
Feb-23	6.7	6.0	7.0	6.1	5.3	5.1
Mar-23	6.9	6.3	7.1	6.4	5.6	5.5
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	6.7	6.6	6.6	6.7	6.7	6.7
Dec-23	6.3	5.8	6.2	5.8	5.9	6.0
Jan-24	6.1	5.6	6.1	5.7	5.9	5.8
Feb-24	5.9	5.6	5.9	5.5	5.9	5.9
Mar-24	5.7	5.4	5.7	5.3	5.8	5.8
% change month on same month of previous year						
Jan-23	6.4	6.3	6.5	6.1	5.6	5.6
Feb-23	7.1	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	7.7	8.1	8.0	8.4	6.1	6.1
Jun-23	8.0	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	7.7	8.4	7.5	8.2	8.3	8.2
Oct-23	6.1	5.9	6.2	6.2	5.9	5.9
Nov-23	6.2	5.5	6.2	5.7	5.9	5.9
Dec-23	6.2	5.8	6.2	5.6	6.0	6.2
Jan-24	5.9	5.5	5.8	5.6	5.7	5.4
Feb-24	5.7	5.4	5.7	5.1	5.7	5.9
Mar-24	5.7	5.2	5.7	5.2	6.0	5.9